Duration: friend or foe?

The case for dynamism in unconstrained bond portfolios

by Amelie Chowna, Senior Fixed Income Investment Specialist

Duration is the dominant driver of long-term returns for most bond markets. For corporate bonds with a risk premium (credit spread), duration also plays a key role in shaping the risk-return profile.

Since the global financial crisis, duration has been seen as the primary hedging tool for credit risk. Our analysis shows that between 2008 and 2020, the correlation between credit spreads and government bond yields has often been negative.[1] For example, when credit spreads widen amid a risk-off environment, this would typically be accompanied with a decline in government bond yields, thus cushioning the negative effect from the credit spread widening.
However, this correlation has fundamentally changed, becoming more positive since the return of inflation in 2021. This new backdrop challenges the long-held view that duration is something to 'buy and hold.' In today's world, fixed income investors need an active and dynamic approach to managing duration in portfolios.

Exploring duration as a hedge for credit risk

Between 2011 and 2020, credit portfolios enjoyed strong returns thanks to declining bond yields, driven by an environment of low growth and inflation.
During this period, duration provided a good hedge for credit exposure. Our research shows that in periods of significant (10 basis points or more) widening in credit spreads, on average, US 10-Year Treasury yields decreased when looking at both weekly and monthly data.

Changes in US 10-Year Treasury yield in periods of 10bps of widening in US credit spreads or more.

bps	2011 to 2020
Weekly series	-0.13
Monthly series	-0.22

Bloomberg, as at 30 September 2025.

But all of this changed when inflation picked up in 2021. Since then, global government bonds have recorded relatively poor returns and exhibited levels of volatility not too dissimilar to that of global high yield bonds.

[1] L&G, Bloomberg as at 30 September 2025.

Performance and volatility of global fixed income sectors (2021-2024)

	Annualised Return	Annualised Volatility	Worst Return in a single calendar year
Global Treasuries	-0.7%	4.2%	-10.8%
Global Corporates	-1.0%	5.8%	-14.1%
Emerging Market Debt	-0.5%	5.4%	-15.3%
Global High Yield	3.8%	4.9%	-11.0%

Bloomberg, as at 31 December 2024. Past performance is not a guide to the future.

When we look again at periods of significant credit spread widening, but consider data covering 2021 – 2025 to date, we can see that US Treasury yields still dropped in these moments on a weekly basis, but the opposite is true when looking at monthly series, which suggests that any relief provided by duration has been short-lived.

bps	2021 to 2025
Weekly series	-0.13
Monthly series	0.14

Bloomberg, as at 30 September 2025.

A dynamic approach to duration management

Duration can add to long-term returns but needs to be managed in a more dynamic way. Over the last 40 years, duration has been something to 'buy and hold', but we believe this is no longer appropriate for unconstrained bond strategies seeking improved risk-adjusted returns in volatile markets.

A more volatile, shorter-cycle backdrop will require a sharper focus not only on active duration management for the entire portfolio, but also on its interaction with risk assets.

For unconstrained bond portfolios with multi-credit exposure, we believe duration is only valuable when it provides potential diversification benefits, e.g. when correlation between credit spreads and government bond yield is negative. When the correlation is more positive, for example in times of high inflation, we believe having a lower exposure to duration can be more beneficial.

The age of agility

We believe the current market backdrop demands a more responsive and flexible approach to duration management in fixed income portfolios. Keeping a keen eye on market sentiment with regards to recession versus inflation risks and also actively adjusting our duration exposure in line with evolving macro-economic conditions has been a key driver of our team's performance and how we aim to lower risk. Agile duration management is essential for unconstrained bond strategies now and going forwards.

Key Risks

The value of an investment and any income taken from it is not guaranteed and can go down as well as up, and the investor may get back less than the original amount invested. Past performance is not a guide to future performance.

Assumptions, opinions, and estimates are provided for illustrative purposes only. There is no guarantee that any forecasts made will come to pass. It should be noted that diversification is no guarantee against a loss in a declining market.