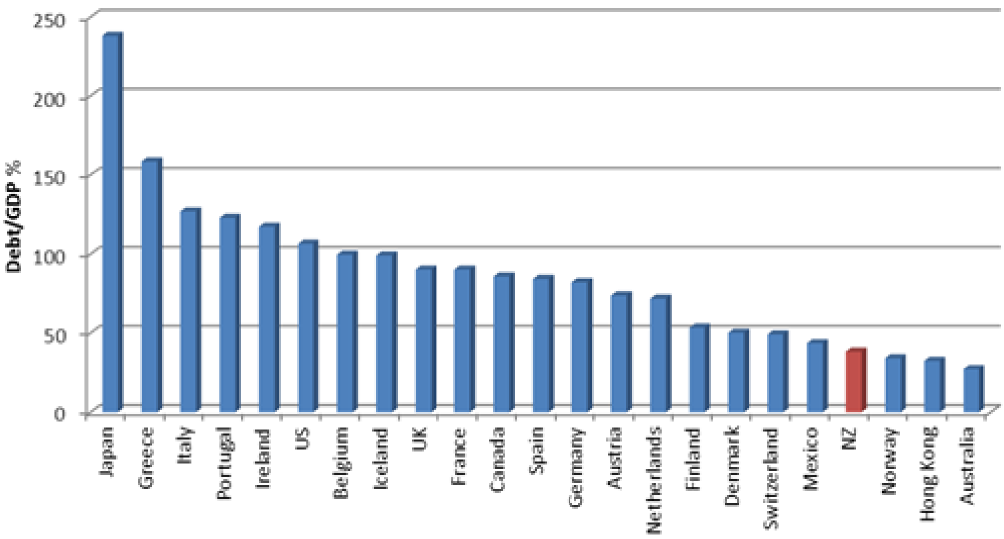
Investing in global bonds - a smarter way

Graham Ansell | ANZ NZ Investments | 14 May 2014

If you were lending somebody money, would you lend them more money just because they had more debt? Further, would you continue to lend them even more money if they kept borrowing more money? If you are investing according to a debt-weighted benchmark, that is exactly what you are doing - because most of the fixed interest benchmarks that portfolio managers are given to manage their bond portfolios against are based on debt-weighted indices.

Figure 1 shows the gross debt of various countries, as a percentage of the size of their economies.

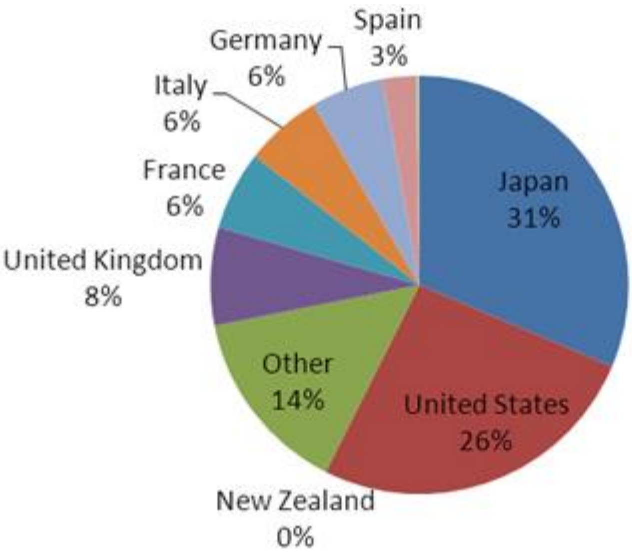
Figure 1: Gross govt debt as % of GDP



Source: IMF

Figure 2 shows the composition of the government component of the Barclay's Global Aggregate Bond Index. As shown, government bonds make up around 54% of the index.

Figure 2: Barclay's Global Aggregate Bond Index - government debt composition
February 2013



Sources: Bloomberg.

So what does this mean? For example, take Japan. It issues around a third of all global government debt - in fact, it's debt to GDP position is easily the worst in the developed world. But, as Japan issues more debt, the benchmark's exposure to Japanese governement bonds keeps getting bigger. Other things being equal, this implies portfolio managers are encouraged to keep increasing exposures to Japanese government bonds, to ensure they are not deviating too far from benchmark.

With more and more investor money being invested in global bonds, this is an important consideration when building an investment portfolio.

Read "Does lending to debtors make sense for bond investors?"

Graham Ansell is GM Investment Management, ANZ NZ Investments (Auckland).
