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## INFLUENTIAL ACADEMICS

# Bond theories leave campus

**Barry B. Burr**

There are few gray heads among academics specializing in fixed-income study, noted Jess B. Yawitz, a pioneer of the research backing structured fixed-income products, suggesting how relatively young interest is in the field.

Mr. Yawitz was attracted to the area in the late 1960s and early 1970s because of the lack of research in fixed income compared with the surfeit of studies on equities.

"I looked to bonds to make a contribution," he said.

He succeeded. Mr. Yawitz became a leading strategist who helped bring structured fixed-income, such as immunization from academic research into widespread institutional use.

In the process, he left the Graduate School of Business, Washington University, where he had been John E. Simon professor of finance, to join Goldman, Sachs & Co. in 1985. Recently, he was named chief investment officer of Goldman Sachs Asset Management, its new separate-account, fixed-income investment management unit.

His entry into the field coincided with the reintroduction in the early 1970s of duration, a measure of fixed-income risk first developed in the 1930s.

"The state of bond math was more advanced than the investment management at the time," he said. But the growing volatility of rates then spurred interest in the dormant concept, which shows more accurately than simple maturity the behavior of fixed-income prices in relation to changes in interest rates.

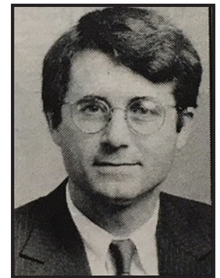
"It was a good coincidence that many of us got in at the ground floor," he added.

In the late 1970s and early 1980s as interest rates rose to record levels and pension sponsors sought to capture high returns, duration-based strategies gave them the confidence to move huge sums to immunization to protect their returns. Some individual funds placed more than $1 billion in such strategies.

Such moves were the outgrowth of investment executives linking more closely the prospective liability payout stream to asset management. Typically plans regard their assets and liabilities as two separately managed pieces.

"In retrospect, none of us thought the interest in fixed-income research in the mid-1970s would turn out to be as important as it has," he said.

With the introduction of the Financial Accounting Standards Board Statement 87, which brought the pension plan onto the balance sheet, investment strategy linking assets and liabilities has become common, he said.


J. Yawitz

As for the contributions he and others in the field have made, he said: "We advanced the dialogue. We were concerned with the measure and management of interest rate risk. That sums up a major part of our careers."

But, "academic research doesn't reach its full potential until it's tested in the real world."

Looking ahead, he sees sponsors and other institutions involved in asset-liability management "putting more of a focus on the particular purpose for which a pool of assets is utilized." In other words, a sponsor might divide a plan into separate asset-liability pools.

"Maybe there is a pool of assets designated as a hedge against interest-rate risk; maybe a pool to hedge inflation; or maybe, to maximize rate of return."

Also, "there is more discipline being brought to bear in asset allocation…As a result, more specific marching orders are being given to money managers."

Although many might look at duration-based strategies as a passive way to manage fixed income, Mr. Yawitz said, "I see plenty of room for value-added trading strategies. If you want a portfolio with a duration of eight years, finding the cheapest way to form the portfolio is a challenge."

"I think there will be less fascination on beating aggregate indexes" for fixed-income strategies, he added.

"I think more important will be customized indexes, tailored to the liabilities of a plan. Duration will play an important role" to try to ensure assets perform in line with matching liabilities.

"On the equity side, I don't see a comparable liability-driven strategy." He dismisses more recent interest in measuring the duration of equities. "It's not an exercise I'm ever going to devote any of my time to. It's almost a philosophical argument. The precision with which one could measure equity duration is so low, I don't think it's meaningful."

"In the bond tables, I can get a precise price for a 20-year bond… There is no analogy of bond tables for equities." That is determining prices at various interest rates.

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