Why Tracking the Agg Leads to Inferior Results: A Cheat Sheet

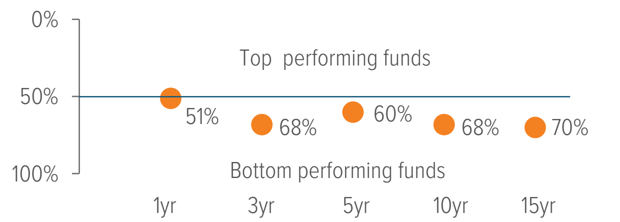
Index funds are designed to closely mirror the performance of a reference benchmark. But what happens if the index itself is flawed?

The Bloomberg U.S. Aggregate Index (Agg)[1] is not designed to deliver an optimal return profile for investors. So it makes sense that over the past 15 years, the Agg has trailed active core/core-plus bond funds, landing below median in both short- and long-term periods.

Simply put, **if you were looking for strong bond options, the Agg would not be your top choice!**

The Agg fell below median in every time period

Ranking in core/core-plus Morningstar category



As of 12/31/25. Source: Morningstar Direct. Bloomberg U.S. Aggregate Index ranking against all active funds in the intermediate core and core-plus bond categories.

3 reasons why passive bond funds fail

1 The index favors the most indebted issuers

Stock indexes like the S&P 500 give bigger weight to companies whose stock prices have gone up, so investors end up owning more of the strongest performers.

The Agg works very differently. It's based on how much debt a company has, so the borrowers with the most debt get the biggest weight. This can push investors into risks they didn't expect—like the large exposure to mortgage-backed securities during the financial crisis. Because passive bond funds simply follow the index, they take on these risks too.

2 Limited opportunity set restricts passive funds

The Agg excludes entire segments of the bond market that can boost returns and add diversification. It mainly holds U.S. Treasuries, government-related bonds, investment-grade corporate bonds, and certain mortgage- and asset-backed securities. Because passive funds must follow the index, they miss out on other areas in the bond market. Active managers can invest in these broader areas, giving them more ways to find value and better manage risk.

3 Active bond funds are already pretty cheap

One reason investors favor passive funds is their low-cost structure. But unlike active stock funds, active bond funds are more cost-efficient. Because the gap between active and passive bond fees is small, the low cost benefit of passive bond funds isn't as big a benefit.

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A note about risk

Bonds are subject to market, issuer, credit, prepayment, extension and other risks, and their values may fluctuate. Indexes are unmanaged and not available for direct investment.

[1] The Bloomberg U.S. Aggregate Bond Index is a widely recognized, unmanaged index of publicly issued investment grade U.S. government, mortgage-backed, asset-backed and corporate debt securities. Index returns do not reflect fees, brokerage commissions, taxes or other expenses of investing.

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