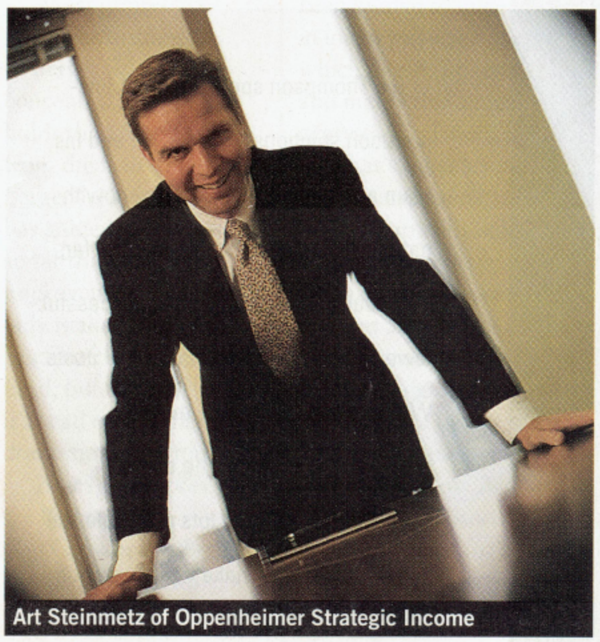
BONDWATCH

# The Only Bond Fund You'll Ever Need?

**Why own** one fund that invests in junk bonds, another that specializes in emerging-market debt and a third with a portfolio filled with U.S. Treasurys when one fund will invest in all three?



Art Steinmetz of Oppenheimer Strategic Income

That's the idea behind the multisector bond fund. Although the concept isn't new, this type of fund is gaining popularity, thanks to 401(k) plan providers looking for an easy way to fill the bond-fund slot in retirement plans. At last count there were 46 multisector funds, up from only nine at the end of 1987. And big firms like Fidelity, MFS and Cigna have all recently launched new entries.

The appeal is simple. If you invest in different groups of bonds, there is less risk. If one type of bond is falling, it's likely that another type is rising, and that gives investors some comfort. Another enticement: These funds have produced superior returns. In the three years ended May 31, multisector funds gained an average annualized 9.7 percent, compared with intermediate bond funds' average gain of 7.2 percent.

Yet the approach is riskier than it appears. Most multisector managers shift from one type of bond to another, depending on where the best returns are. Currently that means many of these funds are heavily weighted in junk bonds, which have been outperforming recently. But junk bonds are among the most volatile of fixed-income offerings. "Multisector funds are fine for investors who want all their bonds in one fund," says David Giunta, senior vice president of Fidelity's retail mutual fund group. "But they need to understand their aggressive nature."

Another caveat: These funds have been a big hit with brokers and financial planners, so many of them have a load and high expenses.

Shortcomings aside, for investors who like the eggs-in-one-basket approach, we've found four top-performing funds that keep expenses in check and volatility—as measured by fund tracker Morningstar—low.

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**T. Rowe Price Spectrum Income.** This no-load offering is a fund of funds, meaning it invests in eight of T. Rowe's fixed-income funds. It has posted average annual gains of 9.0 percent in the past five years, compared with the category average return of 7.6 percent. The fund's expenses of 0.75 percent are the lowest on our list.

**Franklin Strategic Income (A).** This fund has a three-year average annual return of 12.3 percent, compared with the category's average of 9.7 percent. But the fund manages to post high returns while taking less risk than its peers, according to Morningstar's risk ratings.

**Oppenheimer Strategic Income (A).** The old-timer on our list, this fund was launched in 1989. And manager Art Steinmetz has been at the helm all that time. Now the fund, the largest in the category, claims $9.5 billion in assets. Although it has a load of 4.75 percent, expenses are only 0.93 percent. It's the fourth-best-performing multisector fund in the past five years, with an annual gain of 8.5 percent. While Steinmetz may shift his asset allocation from time to time, he never completely dumps any of its sectors.

**MFS Strategic Income (A).** In contrast to Oppenheimer, this fund frequently dips in and out of the various sectors. A year ago international bonds composed 30 percent of the portfolio; today's percentage: zero. The heavy trading doesn't hurt returns; the fund's five-year average annual gain ranks MFS fifth in its objective.

*—Mary Romano*

**CYBER TALK**

**"Nobody's going to ring a bell at the start of a bear [market] . . . [but] every bear market we've had has been triggered by dramatic change in inflation expectations."**

—Michael Weiner, One Group Value Growth, on Sage