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Market View

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High-Yield Bonds Beckon

Carret Credit Insight
Carret Asset Management

July 29: We are frequently asked about the correlation of the high-yield bond market to the stock market. While we always reference that high-yield correlation is historically 30% of equity market volatility, periods like March provide real-life examples. In March, high yield bonds (as measured by the **iShares iBoxx $ High Yield Corporate Bond** ETF, ticker: HYG) plummeted 21%. We know that bonds, unlike equities, have maturity dates, and if a company doesn't default by the maturity date, bondholders are paid in full. Thus, downdrafts like March typically prove to be buying opportunities. The opportunity lasted a mere few weeks. By quarter-end, the 21% decline had been meaningfully erased.

The Federal Reserve's support of the high-yield bond market is unlike anything we have ever seen. The Fed is buying high-yield ETFs and select individual bonds. The "fallen angel" program is helping BBB-rated companies that fall into junk territory—Delta Airlines [DAL] and Ford Motor [F], to name two of the largest examples. In turn, investor demand for new issues was met with the largest monthly high-yield bond issuance ever of $47 billion in June, topping September 2013's issuance of $46.4 billion.

The market has improved materially from the March lows; however, investing in high-yield bonds during a recession requires thorough and intense credit research. The risks are greater today and because of the Fed intervention, the returns are lower.

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[Link to article]

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