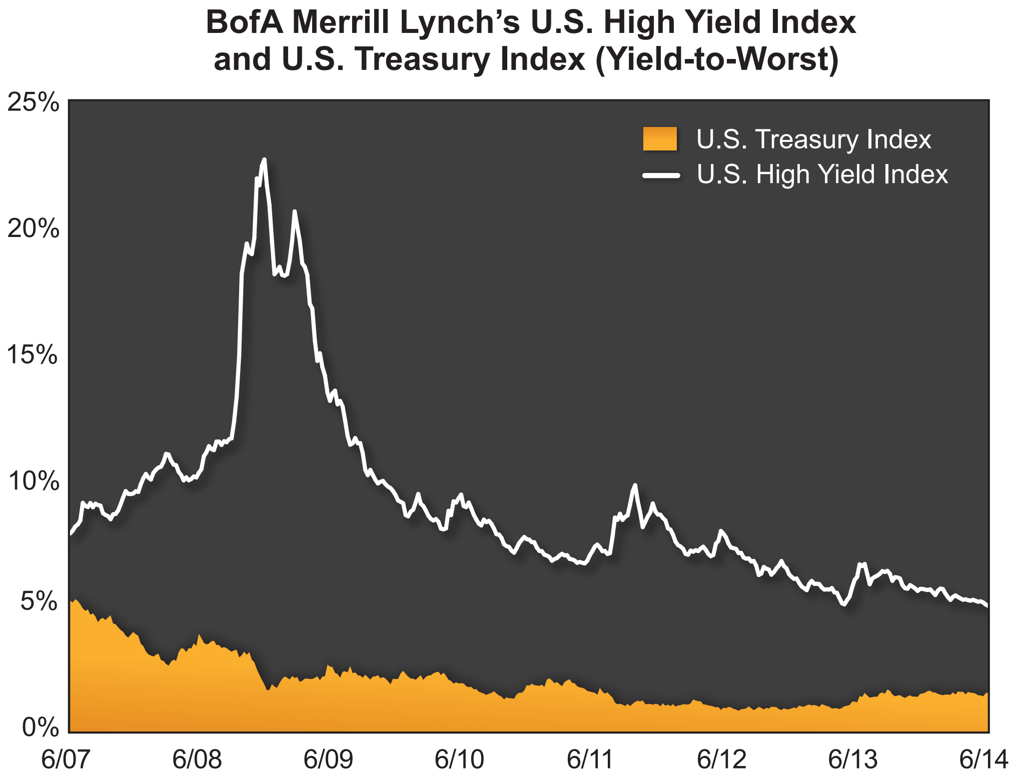
High Yield Corporate Bond Yields Reach Historical Lows



Source: Bloomberg. Data is weekly from 6/22/07 through 6/13/14.

View from the Observation Deck

1. Yesterday's release from the Federal Reserve noted that Fed members had raised their forecast for the federal funds target rate at the end of 2015 from 1.00% to 1.00-1.25%, and its 2016 target from 2.25% to 2.50%.
2. This is significant because it provides investors with some additional guidance. The general consensus among economists has been that the Fed would not likely begin raising rates until around mid-2015.
3. The first year of previous Fed tightening phases has signaled a peak to bull markets in high yield corporate bonds. (Click here to view previous post on 8/28/12)
4. On a yield-to-worst basis, which takes into account such variables as call protection, the 4.93% yield (6/17) on the BofA Merrill Lynch U.S. High Yield Index represents an historical low, according to *Barron's*.
5. Using the 4.93% yield figure, the current yield spread between high yield corporate bonds and the 10-Year Treasury note has narrowed to within 2.50 percentage points.
6. Historically speaking, once the spread narrows to this level it can be an indication that high yield corporate bonds may be getting a bit pricey for the risks associated with speculative-grade debt.
7. Last November, *Barron's* reported that Martin Fridson, high yield corporate bond guru and head of FridsonVision LLC, released a forecast calling for a steep rise in high yield corporate bond defaults beginning in 2016.
8. So as of today, it appears that high yield corporate bonds could remain on solid footing until we approach mid-2015, in our opinion. We intend to monitor things closely moving forward.