Tracking The Retail Investor’s Appetite For High Yield Corporate Bonds

View from the Observation Deck

1. High yield corporate bonds are speculative-grade securities (a much higher level of credit risk) that tend to pay a higher rate of interest than their investment-grade counterparts.

2. One of the primary indicators used for assessing risk levels in the high yield corporate bond market is the industry default rate. A bond default occurs when the issuer fails to make an interest or principal payment within the specified period.

3. The long-term global speculative-grade default rate, as tracked by Moody’s, has averaged approximately 4.3%, according to its own release. In July 2017, the default rate stood at 3.1%.

4. Moody’s believes that the default rate will be lower a year from now. It is forecasting a default rate of 2.2% by July 2018.

5. As indicated in the chart, asset levels in high yield corporate bond funds relative to total taxable bond fund assets dropped dramatically during the 2008-2009 financial crisis. With the exception of 2013, these asset levels have remained below the average from 2000-2016 (see chart).

6. What makes 2013 interesting is that interest rates rose markedly that year. The yield on the benchmark 10-year Treasury note increased 127 basis points, from 1.76% to 3.03%, according to Bloomberg.

7. From 2000-2016, total high yield corporate bond issuance as a percentage of total corporate bond issuance averaged 17.00% (not shown in chart), according to data from SIFMA.

8. From 12/31/99-12/30/16, a period that included a number of challenges and shocks to the economy, the BofA Merrill Lynch U.S. High Yield Constrained Index posted an average annual total return of 7.20%, according to Bloomberg. For comparative purposes, the S&P 500 Index posted an average annual total return of 4.51% over the same period.

This chart is for illustrative purposes only and not indicative of any actual investment. The illustration excludes the effects of taxes and brokerage commissions and other expenses incurred when investing. Investors cannot invest directly in an index. There can be no assurance that any of the projections cited will occur. The BofA Merrill Lynch U.S. High Yield Constrained Index tracks the performance of U.S. dollar denominated below investment grade corporate debt publicly issued in the U.S. domestic market. The S&P 500 Index is a capitalization-weighted index comprised of 500 stocks used to measure large-cap U.S. stock market performance.

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