

FUND OF INFORMATION

Get Bonds, Corporate Bonds

By TOM SULLIVAN

The case for high-quality corporate bonds.

BONDS -- HIGH-QUALITY CORPORATE BONDS -- MAY BE JUST the ticket to superior total returns heading into the new year.

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Treasury yields are so puny they're a joke. Ditto for money markets. And equities remain subject to volcanic eruption until further notice. But a diversified portfolio of single-A-rated and double-A-rated 10-year corporate bonds can garner you a yield of 8% or more.

"That's an equity-like return with a third of the volatility" of stocks, says Mark Kiesel, executive vice president in charge of credit at bond-fund giant Pimco. He hasn't liked the asset class for the past five years because of historically tiny risk premiums. But "in the last six months and going into 2009, they're finally looking very attractive," Kiesel says.

Kiesel wouldn't discuss specific moves the funds he manages are making. But he's likely repositioning the Pimco Corporate Income Fund (PCN), which has posted a negative total return of 22.84% year-to-date, and the Pimco Corporate Opportunity Fund (PTY), which is down 20.46%.

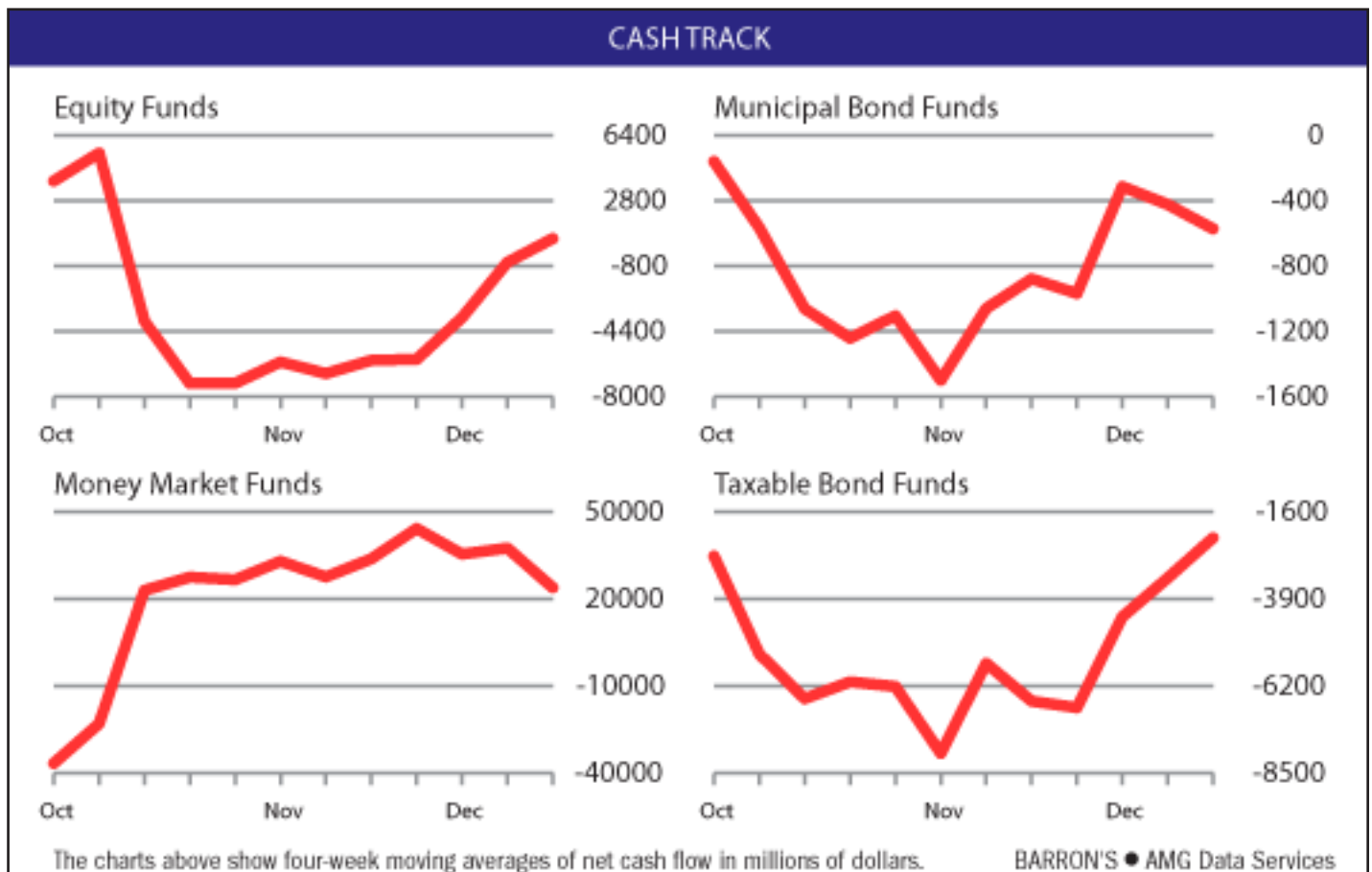
He particularly likes bonds issued by banks, now that the federal government has stepped up its support of the sector. He also likes bonds of infrastructure providers, such as pipelines and utilities. Avoid, however, funds that invest in retailers, autos, airlines and the housing sector, he says, as the recession progresses.

Among other fixed-income sectors, Kiesel sees opportunities in tax-exempt municipal bonds, mortgages and Treasury Inflation Protected Securities, or TIPS. Watch out for high-yield, or junk, bonds. The default rate, currently around 3%, could hit 10% before the recession ends, and recovery rates from bankruptcies could be lower than usual because of the huge amount of leveraged loans ahead of these securities in corporate capital structures.

The outlook for equity mutual and hedge funds is far more problematic. The high-net-worth group Tiger 21 reports allocations by its members to hedge funds are falling by almost 75%. Many won't be coming back. Ever. Mutual funds are also reeling from redemptions.

But one bright spot continues to be exchange-traded funds. Investors put \$61 billion into U.S. ETFs in September and October, according to Barclays Global Investors, even as a net \$126.7 billion flowed out of stock and bond mutual funds. Morningstar, meanwhile, estimates November's ETF inflows at \$26.15 billion, compared with outflows of \$41.48 billion for open-end mutual funds. "It's a secular move from stocks into ETFs," says Scott Burns, director of ETF analysis, "because of their transparency, tax benefits and ability to trade during the day."

The industry is also likely to see more reopenings of closed mutual funds following those massive redemptions. There were 66 reopenings through October of this year, about double the number for 2007, says Keith Sloane, senior vice president, mutual funds, whose Hartford Midcap Fund (ticker: HFMCX), reopened last week. The subadviser is Wellington Management. It's down 37.8% year-to-date through Thursday, but that's still in the top 10% of its peers, which tells you all you need to know about 2008.



Money Honey: Equity funds weekly net inflows averaged \$712 million for the four weeks ended Wednesday, reports AMG. Money funds drew a weekly \$23.8 billion. Taxable bond funds had outflows of \$2.3 billion. Municipal funds' had net weekly outflows averaging \$572 million.