Bond Case Briefs

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Chicago Issues Bonds With ‘Stunningly’ High Yields.

The city of Chicago has been battling a financial crisis since mid-May when a state court rejected its fix for its underfunded pension plan and Moody’s downgraded its debt to junk status.

As part of the larger solution to the financial chaos that downgrade unleashed, the city is issuing $1.1 billion in bonds, both taxable and tax-free. The cash raised will reduce its reliance on short-term debt to pay its bills.

Those new bonds priced Thursday and Friday at rates that have surprised some municipal bond investors, who find them very attractive.

A taxable issue (the city had to issue taxable bonds since the money isn’t technically going towards a public good) that is maturing in 2042 priced Thursday with a yield of 7.98%.

The tax-free issue maturing in 2039 priced Thursday at 5.69%. For an investor in the highest federal tax bracket, that’s equivalent to a 9% taxable yield.

“That’s stunningly high,” says Jim Colby, chief municipal strategist at Van Eck Global. ”It’s far and away significantly cheaper and more attractive than anything of a similar credit quality in the muni space.”

One reason these yields strike experts so high is because both Fitch Ratings and Moody’s Investors Service rated the issues BBB-plus, which is investment grade (Moody’s wasn’t hired to rate these issues by the city). ”Chicago is not Detroit,” says Colby. “It is not a city whose credit rating should be below investment grade.”

Colby says he’ll be looking at the tax-free issue for both the investment grade and high-yield exchange-traded funds he manages (both can by triple-B securities). For comparison, the 30-day yield of his Market Vectors High Yield Municipal Index ETF (HYD) is currently 4.61% in comparison, says Colby.

Dan Heckman, senior fixed income strategist at U.S. Bank Wealth Management, cautions that the yields are higher because some market participants judge that they are riskier than bonds with the same credit ratings.

“The market really views them as a weaker credit than the rating agencies,” says Heckman. “They are attractive if you have an appetite for what is frankly a weaker credit.”

Barron’s

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