[Bond Case Briefs]

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[Bonds Are Starting to Look Attractive. Investors Should Be Careful in Chasing Yield.]

With the Federal Reserve aggressively raising interest rates, bonds' yields have been climbing (and their prices falling). Pros are mixed on when is the time to buy.

As bond yields remained ultralow for many years, dividend stocks didn't have a lot of competition for income investors' attention. But now, as the Federal Reserve continues to raise interest rates and tighten monetary policy to fight raging inflation, the competitive landscape has changed dramatically and swiftly.

Investors, however, need to use caution before they start chasing fast-rising bond yields. The 10-year U.S. Treasury note's yield was shade below 3% this week, up from about 1.5% at the end of 2021. Bond yields and prices move in opposite directions—in this case, pressuring prices in various fixed-income classes such as high yield, investment-grade corporates, and municipals ahead of what's expected to be more rate hikes and tightening by the Fed.

Still, "for the first time in over a year, we are starting to see interest from our client base in allocating to fixed income," says Robert Michele, chief investment officer at J.P. Morgan Global Fixed Income, striking a more upbeat view about bond-investing prospects at current levels.

Institutional investors such as pension funds and insurers, he says, have shown interest in investment-grade corporates yielding in the 4.5% neighborhood and even around 5% with longer maturities, among other assets.

Some individual investors, Michele adds, have been putting money into municipal bonds, whose yields have also risen nicely this year, as well as some taxable bonds.

Michele says that market expectations for the federal-funds rate—the central bank's short-term interest rate benchmark—indicate that it will be at roughly 3.25% a year from now, compared with the current target of 0.25% to 0.5%. (The Fed is expected to boost that Wednesday by a half percentage point.)

Michele believes that short-term rates of 3.25% a year from now—or in that vicinity—makes sense, and is something that bond investors can live with. "It feels like we've put in a bottom in terms of bond prices for the next six-to-nine months," he says.

Still, the bond market is fraught with crosscurrents.

Tom Tzitzouris, head of fixed-income research at Strategas, says that while sophisticated investors can trade in and out of Treasuries as yields and prices bounce around, "for the long-term investor, I don't see this as an entry point."

He wants to see the 10-year Treasury note's yield to move up to around 3.25%, or even a little higher. "I do believe the 10s can get up there," Tzitzouris says. "I don't know if we're going to get up there next week or next month or next year. [But] that would be a good point for a buy-and-hold investor" to jump into bonds.

Tzitzouris adds that he doesn't see much value in the 10-year at its recent yield range because it's "below even the most optimistically low inflation expectation over the next decade of 3%."

Michele is a little more upbeat about fixed-income opportunities, including investment-grade corporate bonds. "There's still a high degree of confidence that the Fed has enough tools in this cycle to engineer a soft landing," he says, adding that corporate profitability has been strong.

He also likes municipal debt, which "might be the one part of market that's is the most underappreciated." Ten-year AAA municipal bonds recently had taxable equivalent yields of roughly 4%, well above where they were at the beginning of the year.

Barron's

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