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# Play-It-Safe Bonds Becoming Mighty Inviting

***Returns Better Than Some Stocks'***

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They're for the risk-averse. And who wouldn't want a little steadiness in this wind-blown market?

They're for the quiet, steady side of your portfolio, the portion that lets you sleep well at night.

They're bonds -- and they usually don't give you much bang for the buck. But lately -- low-priced and with decent yields -- they have been returning far more than their riskier cousins: stocks.

"You can get equity-like returns in the corporate bond market for the first time in decades," said Gary Cloud, portfolio manager of the AFBA 5Star Balanced Fund in Kansas City, Mo.

Lately, bond prices have dropped so much and their yields, or expected returns, have spiked so high that bonds are looking attractive as something other than a safe haven. Some municipal and corporate bonds are yielding substantially more than U.S. Treasurys.

So what's behind this state of affairs? On one level, it's the bond market rule of thumb at work: As prices fall, bond yields rise. Prices have tumbled for municipal bonds as stressed hedge funds have unloaded lots of debt. Prices of corporate bonds have sunk along with companies' weakening earnings and the economy's dim prospects.

The higher yields, while attractive, do signal a higher degree of risk. Munis and corporates will never be as safe as Treasurys, which are backed by the U.S. government. With munis and corporates, there is always the chance of default as city budgets stumble or companies collapse. Nonetheless, bonds' risks are traditionally considered far lower than those of stocks. Look no further than the vicious volatility and staggering declines of stocks this year.

The recent gains in bond yields are eye-popping. Over the past decade, the yields of 10-year, highly rated corporate bonds have averaged about 1.25 percent above 10-year Treasurys. As of Thursday, corporate yields were averaging 4.98 percent above Treasurys, according to Barclays Capital (formerly Lehman Brothers) investment grade corporate credit yield index.

The same has been true, though not to the same degree, of municipal bonds, which state and local governments issue to pay for projects such as school construction. Municipal bonds tend to have lower yields than Treasurys because they are exempt from federal and sometimes even local taxes. But lately, some have had higher yields than Treasurys.

In recent days, the yields on municipal and corporate bonds have come down a little, narrowing the gap with Treasurys, suggesting that investors see risks declining. Still, the yields remain high by historic standards, analysts said. "We're seeing yields we haven't seen in nine or 10 years," said Philip G. Condon, head of municipal bond portfolio management for retail and tax-exempt advisory clients at DWS Investments.

Richard Bernstein, chief investment strategist for Merrill Lynch, points out that Treasurys are this year's best performing asset class. "I think there comes a point when people will begin to realize that the certainty of the return, even though it's low, may be worthwhile," he said.

For individual investors, bonds can provide diversification for a portfolio. But beware: Buying individual bonds can be more difficult than buying stocks. You need to go through a broker. A better option, some strategists said, is to buy a bond fund.

"It's a tremendous opportunity," Cloud said, "but it's also not an area that individual investors should go into on their own."

Moreover, remember the long-term performance of most bonds. You will be hard-pressed to find an analyst or strategist who advises you to dump your stocks in favor of bonds. The recommended portfolio has a mix of stocks and bonds. "Bonds will normally not give you a big amount of growth over time," said Bill Walsh, president of Hennion & Walsh, a Parsippany, N.J., securities firm specializing in municipal bonds. "I know the last few weeks have scared people and made them nervous [about stocks], but over time, history has proven the equities market will give you growth."

If you're looking for more of a return on your bond investment, then munis or corporates may be for you, analysts said. But stick with high-quality ones. The credit quality of governments and companies is monitored by the ratings agencies: Standard & Poor's, Moody's and Fitch Ratings.

Keep in mind that the lower the credit quality, the higher the interest rate you will get for buying that bond. But analysts said you don't have to take a chance on so-called "junk bonds" and all the risks they come with because the yields on high-quality bonds are high enough to make them worthwhile. "Err on the side of caution from the credit perspective," said Bob Nelson, managing analyst for Thomson Reuters. "For the individual, the real concern in this market environment should be on credit quality."