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Corporate bonds are the focus of this issue of *The Journal of Fixed Income*. This topic is quite relevant and timely given the recent stock market decline, falling corporate profits, and the large number of downgrades by bond rating agencies. In the lead article, David Brown provides a framework for analyzing credit spread innovations. Important components of these innovations include maturity specific, time varying liquidity and risk premiums. The empirical findings for different credit quality and maturity portfolios are consistent with the economic predictions from the Longstaff and Schwartz model of the default margin. In the next article, Karan Bhanot provides useful empirical evidence on selecting the appropriate specification for the dynamics of credit spreads. This evidence is particularly important to trading strategies that depend on the mean reversion of credit spreads.

The question of credit rating consistency has been the focus of many empirical investigations. Cantor and Falkenstein provide a careful statistical analysis and re-examination of whether default rates by credit rating categories are consistent across sectors and over time. They show that the introduction of sector and macroeconomic shocks inflates the sample standard deviations and provide evidence that inconsistencies generated by a simple binomial default probability are actually not statistically significant.

The growing market for credit swaps provides an excellent risk management tool for corporate bond managers. Jason Wei presents a sophisticated valuation model for credit swaps that utilize both firm value and rating transition information. Hence, firm-specific asset return volatility can then be used to explain the variation in swap premiums for bonds in the same rating class.

In the next article, Reilly and Wright investigate the composition and characteristics of the high yield corporate bond market. In particular, their empirical finding supports the risk sharing intuition associated with an increasing equity effect as rating quality declines. Furthermore, it is also useful to note that the market interest rate effect declines with quality. Hence, it is not surprising that high yield managers are more focused on much the same business fundamentals as an equity analyst. In the following article, Fredman and Reising examine another below investment grade market, leveraged loans investments. They show that as the market for leveraged loan investments evolved, pricing efficiency resulted in the decline of return and

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risk over time. Therefore, this information is useful in formulating expectations of future return and risk in the leveraged loan market.

Finally, Díaz and Skinner provide an in-depth look at the construction of a corporate yield curve. They verify that corporate yield curve estimates are less reliable than Treasury yield curve estimates. However, they also show that the accuracy of corporate yield curve estimates can be improved by pooling the information from broad credit ratings.

We hope you enjoy this issue of *The Journal of Fixed Income*. Your continued support of the Journal is greatly appreciated.

Stanley J. Kon
Editor