

Reaching for Yield in Corporate Bond Mutual Funds

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The Review of Financial Studies, Volume 31, Issue 5, May 2018, Pages 1930–1965,
<https://doi.org/10.1093/rfs/hhx132>

Published: 24 November 2017

Abstract

We examine “reaching for yield” in U.S. corporate bond mutual funds. We define reaching for yield as tilting portfolios toward bonds with yields higher than the benchmarks. We find that funds generate higher returns and attract more inflows when they reach for yield, especially in periods of low-interest rates. Returns for high reaching-for-yield funds nevertheless tend to be negative on a risk-adjusted basis. Funds engage in rank-chasing behavior by reaching for yield, although these incentives are moderated by the illiquid nature of corporate bonds. High reaching-for-yield funds hold less cash and less liquid bonds, exacerbating redemption risks.

Received January 17, 2017; editorial decision September 23, 2017 by Editor Wei Jiang. Authors have furnished an [Internet Appendix](#), which is available on the Oxford University Press Web site next to the link to the final published paper online.

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