Bonds 101

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Bonds are often misunderstood but bonds can help bring balance and stability to investor's portfolios. Bonds can be very dynamic as they come in many different varieties but they all share certain common qualities.

What You Need to Know about Bonds: Bonds mature. Unlike stocks or real estate investments which are perpetual, bonds have a set maturity date or **Duration**. A bond with a longer duration will typically have a higher yield. Bonds are rated by various agencies as to the financial strength of the entity that is issuing them. **Credit Quality**is very important to a bond. A bond that has a rating of BBB or higher is considered to be an **Investment Grade** bond. Generally speaking, the lower the credit quality of a bond, the higher its yield. Below investment grade, which is BB or lower, is more commonly known as **High Yield**or **Junk Bonds**. **Inflation Risk**is the fact that as the cost of everything we buy rises our income from our bonds remains the same. **Interest Rate Risk**can be much more dramatic. Bonds have an **Inverse** relationship to interest rates. When interest rates go higher, the value of older bonds goes down. The opposite also holds true, when interest rates go down, older bonds values will increase.

Treasury bonds are issued by the U.S. Government and generally are not subject to state taxes. They carry the highest rating of AAA and have virtually no **credit risk** (the likeliness that a bond may default or fail to make interest payments) but you still are exposed to **interest rate risk** and **inflation risk**.

Municipal bonds are issued by states, cities, counties and special projects. The appeal of municipal bonds is that the interest they pay is free from federal income tax and in some cases state and local taxes. Your personal tax status plays a major role in determining if Munis are right for you.

Corporate Bonds as their name states are issued by companies. Credit risk becomes very relevant when dealing with corporate bonds. The rate of interest you receive from a corporate bond has a lot to do with the issuing company's financial strength. The less financially stable a company may be, the higher the rate they have to offer to attract investors.

International Bonds offer a world of opportunity. Investors have the ability to purchase bonds from around the globe both from developed and emerging markets. Whether it is a foreign government or foreign company the same risks apply, that would to a U.S. bond. However, when dealing with foreign bonds, you have added risks because you are dealing with a foreign currency and political system.

In summary there are many types of bonds and they can be as conservative as a savings account to as aggressive as your most speculative stocks. Which bonds are right for you is something you can determine with your advisor.

Regards,

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