Scarlet Oak Financial Services
Faye Sykes, CLTC, NSSA
CEO & Independent Advisor
1117 Perimeter Center West
Suite W-212
Atlanta, GA 30338
800-871-1219
fsykes@scarletoakfs.com
www.scarletoakfs.com

Analyzing Bonds

Analyzing Bonds

Introduction

A bond is a type of fixed-income debt instrument issued by a governmental entity or by a private or publicly traded company. When analyzing a bond, you should examine the interest taxation, maturity, rating, yield, and call features.

Interest taxation

For many people, the first consideration in buying a bond is how the interest is taxed. In most cases, the interest on bonds issued by state and local municipalities is free from federal and, sometimes, state taxation. Bonds issued by private or publicly traded companies are fully taxable. Bonds issued by the U.S. government are free from state taxes but fully taxable for federal income tax purposes. Thus, whether you buy a taxable or tax-free bond will depend, in part, on your tax bracket. If you are in a high tax bracket, buying a municipal bond may make tax sense for you. If you are not in a high tax bracket, the tax benefits may not be enough to offset a lower interest rate.

Maturity

A second issue to consider in buying bonds is the maturity date. In other words, when will the bond be paid off by the issuer? Bonds are issued with varying maturities--some bonds have very short maturities (less than a year); other bonds have maturities up to 30 years. Bonds with a longer maturity tend to pay higher interest rates, but the price of the underlying bond may fluctuate more in the marketplace than that of a shorter-term bond. (Bonds are often traded in the secondary market after they have been issued.) Bonds with shorter maturities tend to pay lower interest rates, but the underlying price of the bond does not fluctuate as much as that of longer-term bonds. Your own time horizon will also be a factor in your decision.

Credit ratings

A third factor to consider is the credit rating of the issuer (i.e., the financial strength of the company or entity issuing the security). The bonds of less financially strong issuers tend to pay higher interest rates. Bonds issued by the U.S. government, on the other hand, typically pay the lowest interest rates (for a given maturity). There is a tradeoff between the interest rate you receive and the risk associated with the bond. Bond ratings are determined by ratings services.

Yield

The yield of the bond is also an important part of the analysis. The yield is what the bond pays out every year, expressed as an interest rate. Some people also look at the yield to maturity, which is a combination of the interest paid out plus any appreciation in the underlying value of the bond principal. The yield (and the yield to maturity) on any bond will depend on the credit rating of the issuer, the length of the maturity, the type of bond it is, and the general market for interest rates. Before buying a bond, you should compare bonds of a similar type and maturity to see which offers the best yield.

Call features

A final consideration when buying a bond is the "call" or conversion feature of the bond. Some bonds may be redeemed (or "called") by the issuer before the final maturity date. An issuer may call a bond if interest rates have fallen, and the issuer would like to issue new bonds with the lower interest rate. Typically, many municipal bonds have call features. You should carefully read the bond indenture before purchasing to determine if a call feature is on that bond. Some bonds also have conversion features, where the bond is convertible into the common stock of the company issuing the bond. Usually, you can convert each bond into a predetermined number of common shares of stock in the company issuing the bond.

To schedule an appointment with Faye Sykes, click here .

Broadridge Investor Communication Solutions, Inc. prepared this material for use by Scarlet Oak Financial Services.

Broadridge Investor Communication Solutions, Inc. does not provide investment, tax, legal, or retirement advice or recommendations. The information presented here is not specific to any individual's personal circumstances. To the extent that this material concerns tax matters, it is not intended or written to be used, and cannot be used, by a taxpayer for the purpose of avoiding penalties that may be imposed by law. Each taxpayer should seek independent advice from a tax professional based on individual circumstances. Scarlet Oak Financial Services provide these materials for general information and educational purposes based upon publicly available information from sources believed to be reliable — we cannot assure the accuracy or completeness of these materials. The information in these materials may change at any time and without notice.

Scarlet Oak Financial Services outgoing and incoming e-mails are electronically archived and subject to review and/or disclosure to someone other than the recipient. We cannot accept requests for securities transactions or other similar instructions through e-mail. We cannot ensure the security of information e-mailed over the Internet, so you should be careful when transmitting confidential information such as account numbers and security holdings. If the reader of this message is not the intended recipient or an employee or agent responsible for delivering this message to the intended recipient, you are hereby notified that any dissemination distribution or coping of this communication is strictly prohibited. If you have received this communication in error, please notify us immediately by replying to this message and deleting it from your computer. Advisory Services offered through Capital Asset Advisory Services, LLC., a Registered Investment Advisor.

Scarlet Oak Financial Services
Faye Sykes, CLTC, NSSA
CEO & Independent Advisor
1117 Perimeter Center West
Suite W-212
Atlanta, GA 30338
800-871-1219
fsykes@scarletoakfs.com
www.scarletoakfs.com

scarlet·oak·financial·services