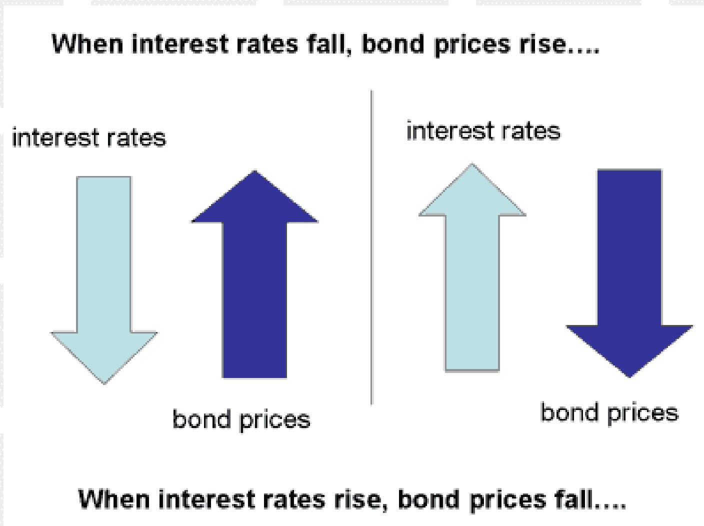
Is my bond account OK?

Recent Experience

My account is invested 100% in bonds, and nothing else. I thought I was safe, but my monthly account statement shows that I've lost considerable value. I asked my financial advisor about this and they told me:

- When interest rates rise, bond prices fall
- Recently, interest rates rose a whole lot, and all within a very short period of time
- Interest rates[1] bottomed out[2] at just 0.499%
- But have since risen[3] to 3.483%
- That's a 598% proportionate increase
- In fact, this has been the most extreme interest rate increase in well over 125 years
- No bond portfolio[4] could report a positive return during such a period . . . it's just not possible



My Doubts and Fears

How should I feel about this? How should I interpret it? Are bonds a bad investment? Do bonds no longer fit or meet my investment needs? Will I keep losing money?

The brief answers are:

- Your financial wellbeing has not been diminished or undermined
- Bonds remain a critical and remarkably beneficial component serving your short-term needs

[1] Interest rates are defined by the yield on a 10-year U.S. Treasury bond
[2] Interest rates bottomed out mid-day March 9, 2020
[3] This yield was reached mid-day on June 14, 2022
[4] This assumes we are talking about publicly traded bonds and not private one-off loans; it also assumes that the portfolio has a positive effective maturity and a positive effective duration (greater than what one would find with a money market fund)

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- No, it is extremely unlikely that you will keep losing money

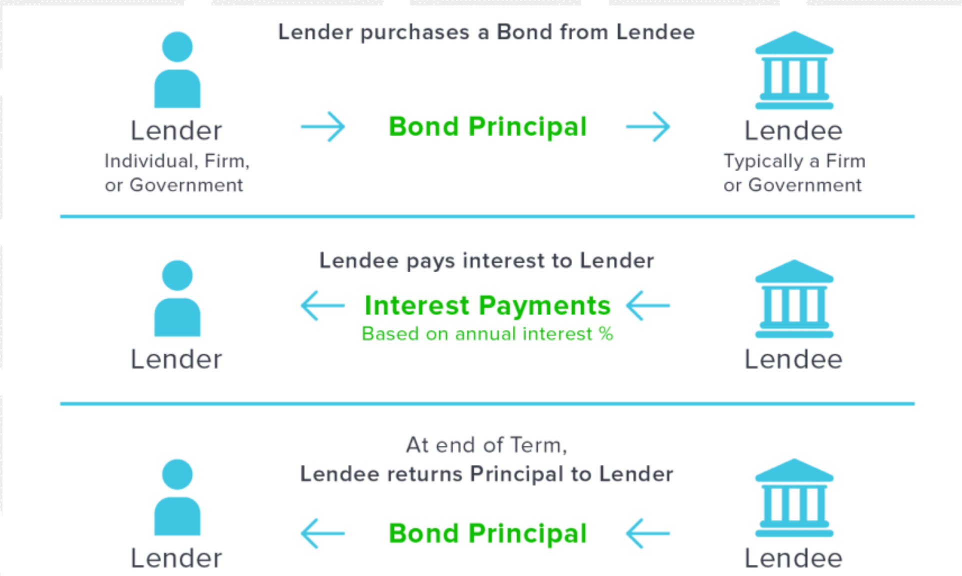
OK, but let's put some flesh on the bone here. Attempting to backup each of these observations . . . making them intuitive.

What is a Bond

A bond is a contract, it is a promise. The contract promises to pay you certain amounts of money on certain pre-specified dates. These payments are of two types:

- Periodic interest payments (typically once every six months)
- Final payment, or the return of principal (paid on the maturity date of the bond)

So, a bond is a simple promise to pay you a specific amount of money on specific dates, not a penny more, and not a penny less.



What Happens When Interest Rates Rise

When interest rates go up, bond prices fall. But rising interest rates don't affect or change the bond contract. Rising interest rates can't affect what was promised. You will still get back[5] exactly what you were previously promised.

This observation is very important. And it explains why banks and insurance companies in the United States generally carry their bonds[6] at cost. In other words, banks and insurance companies generally ignore how the investment marketplace

[5] If the entity that issued the bond declares bankruptcy, then you are expected to receive part but not all of what is promised by the bond contract
[6] Investment grade bonds

values or prices their bonds. They ignore declines in “reported prices” because they know[7] that they’ll still receive the previously promised interest payments and promised maturity values.

Integrated’s Bond Portfolios

Integrated offers six different bond portfolios. Four of these are structured as buy and hold until maturity bond ladders. When Integrated constructs these bond ladders, we have two overarching objectives:

- Minimize the cost (both direct and indirect)
- Deliver an extremely high level of diversification

Integrated recognizes that this objective is best achieved through the use of cost-effective Bond Term Funds (also called “BTFs”). A Bond Term Fund is a prepackaged portfolio of bonds that are held until they mature. As a consequence, Bond Term Funds have a maturity date, on which they liquidate and distribute all of the monies resulting from the maturing bonds contained within the fund. This structure minimizes cost while maximizing diversification. It constitutes a remarkable improvement in bond management, best serving the end investor’s needs.

Bottom Line

Yes, as interest rates rise, bond prices fall in reported value. If interest rates rise fast enough and within a short enough period of time, then your monthly account statement will report falling values. But does this really matter? You’ll still receive the promised bond payments, both return of principal and periodic interest. These have not been diminished.

Your future wellbeing has not been impacted.

Finally, and worth keeping in mind . . . your financial advisor has a menu of possible investment solutions that are directly relevant to the dynamics mentioned above. But the solution that is most appropriate to your unique needs and circumstances can only grow out of a meaningful discussion with your advisor. Reach out to them, talk with your advisor.

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[7] Baring bankruptcy of the bond issuer

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This is not a solicitation or offer to buy or sell any security.

You must do your own due diligence and consult a professional investment advisor before making any investment decisions.

The use of a proprietary technique, model, or algorithm does not guarantee any specific or profitable results.

The risk of loss in trading securities can be substantial. You should therefore carefully consider whether such trading is suitable for you in light of your financial condition. No strategy, including asset allocation and diversification, can assure success or protect against loss. Stock investing involves risk, including loss of principal. Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and bonds are subject to availability and change in price. International debt securities involve special additional risks. These risks include, but are not limited to, currency risk, geopolitical and regulatory risk, and risk associated with varying settlement standards. These risks are often heightened for investments in emerging markets. International debt securities involve special additional risks. These risks include, but are not limited to, currency risk, geopolitical and regulatory risk, and risk associated with varying settlement standards. These risks are often heightened for investments in emerging markets. The fast price swings in commodities and currencies will result in significant volatility in an investor's holdings.

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