

May 2024

# Understanding a Bond Portfolio: A Glossary

By IAM Capital Markets

## Issuer

The issuer of a bond is an entity or corporation seeking to raise cash by issuing an instrument of debt, a bond, in the capital markets. Most bonds IAM clients invest in are issued by corporations of various sizes or state and national governments. Investors looking to hold a particular type of bond may deal with a subset of issuers. For example, investors wanting index annuity bonds will find them issued by infrastructure companies while those looking for investment-grade hybrids may only find them available from major banks.

## Currency

A bond's currency is the currency in which the bondholder will pay the consideration amount (the amount required to purchase a bond from a previous bondholder) or the principal value (the amount required to purchase a bond from its issuer). It is also the currency in which the bondholder will receive coupon payments. Investors can purchase, for example, bonds issued in USD with AUD, but transactions are subject to exchange rates. We offer bonds in a range of currencies, including AUD, USD, and EUR.

## Sector

Sector refers to the industry the issuer is in. If an investor purchases a bond issued by a corporation in the basic materials industry, their loan may be providing funds for that company to procure natural resources to produce common goods.

## Payment Rank

The payment rank helps describe the level of safety associated with a particular asset sub-class; it is also the entitlement of different asset holders to repayment in the event of default. In the chart provided, commonly called the capital stack, the closer to the bottom the investment is, the riskier it is; the investor is more likely to lose out if the issuer defaults. Bonds can be ranked as senior or subordinated (also referred to as junior), and secured or unsecured. Holders of senior bonds are entitled to receive the return on their investments before holders of junior bonds are in the event of the issuer default. Secured bonds are collateralised by an asset (for example, property) so that in the event of issuer default, investors have a claim to the issuer's assets. An unsecured bond is not tied to any assets available for claim.

Senior secured debt
Senior debt
Subordinated debt
Hybrids
Equity

## Coupon Type

The most common types of coupons are fixed, floating, and inflation linked. If a coupon is fixed, the investor is paid the same coupon at each payment while the bond is in their possession. In Australia, floating coupons are set at a certain amount above or below the BBSW (the Bank Bill Swap Rate). The BBSW is reset by the Reserve Bank of Australia, so as the BBSW changes the coupon amount an investor is paid also changes. For variable coupons, the coupon is fixed up until the bond's first call date. We assume bonds will be called - they will be redeemed by the issuer - at their first call date.

## Coupon Formula

The coupon formula shows how a bond's coupon will be reassessed throughout a bond's lifetime. The frequency and the benchmark with which it reassessed is are determined by the type of bond it is.

## Current Coupon

The current coupon is the coupon a bondholder will receive at each payment date, The amount an investor receives from a coupon can change if it is set against a benchmark, for example, the BBSW, but the coupon formula itself remains unchanged throughout the life of a bond unless specified otherwise.

## Maturity Date

The end date of a bond. Unless stated otherwise, this is the date at which the principal amount (the amount initially paid to acquire a bond) is returned to the bondholder. An example exception to this general rule is capital indexed bonds, with which interest payments are given to the bondholder at the maturity date along with the principal amount. Bonds with no maturity date are perpetual instruments; bondholders may receive payments indefinitely.

## Call Date

A date set by the issuer on which they can redeem their bond by returning the principal value and accrued interest amount to the bondholder.

## Clean Consideration

The clean price is multiplied by the face value.

## Rating (S&P, Fitch, Moody)

Bond ratings are measures of financial security determined by rating agencies (S&P, Moody's, Fitch) using information about the financial strength of the company or entity providing the bond. An investment grade bond is a bond that has been rated above BBB- or Baa3 in the chart below. Bonds rated below investment grade level are considered junk bonds and are a riskier investment.

Moody's	S&P	Fitch
Aaa	AAA	AAA
Aa1	AA+	AA+
Aa2	AA	AA
Aa3	AA-	AA-
A1	A+	A+
A2	A	A
A3	A-	A-
Baa1	BBB+	BBB+
Baa2	BBB	BBB
Baa3	BBB-	BBB-
Ba1	BB+	BB+
Ba2	BB	BB
Ba3	BB-	BB-
B1	B+	B+
B2	B	B
B3	B-	B-
Caa1	CCC+	CCC
Caa2	CCC	
Caa3	CCC-	
Ca		

## Face Value

A bond's face value is the amount that is promised to be paid back to the bondholder by the issuer at the bond's maturity date. This is also referred to as the principal value.

## Yield

Also known as yield to maturity, this metric describes the total income a bondholder will receive expressed as a percentage assuming they hold it until maturity, and therefore receive all interest payments. It differs from running yield in that it accounts for all future cash flows.

### Margin (TM/ASW)

The trading margin is most relevant for bonds with floating-rate coupons. The margin describes how far above or below a bond's coupon is set from the swap rate, or the relevant benchmark being used. When calculating the yield to maturity, the current market price of a bond discounting its current cashflows, the margin is added to the benchmark to help account for risk.

### Running Yield

This term refers to a bond's interest rate and is calculated based on the coupon payment and the current market price. This is the annual income from coupon payments that is calculated by dividing the coupon by the current market price and multiplying it by 100. For example, if you have a bond with a 5% coupon that is available at \$101.50, then the running yield will be 4.92%.

### Clean Price

The clean price refers to the price of the bond excluding any accumulated interest associated with it. This is important to consider when an investor purchases a bond in between coupon payment dates; while the investor will receive the whole coupon payment at the next payment date, they will only be entitled to half of it. When this occurs, the new bondholder will pay the previous bondholder the appropriate amount.

### Accrued Interest

This is the portion of a coupon payment that a new bondholder pays the previous bondholder when acquiring their issuance between interest payment dates. The amount of interest the previous bondholder is entitled to is the amount between the coupon payment date and the date of purchase by the new bondholder.

### Gross Consideration

Gross consideration is the clean consideration added to accrued interest.

## Research Report Disclosure

IAM Capital Markets Limited (AFSL 283119) ('IAM Capital Markets') is a financial service business and provides general financial product advice only. As a result, this document, the Content and the Reports are not intended to provide financial product advice and must not be relied upon or construed as such. IAM Capital Markets does not express any opinion on the future or expected value of any financial product and does not explicitly or implicitly recommend or suggest an investment strategy of any kind. The Content and the Reports provided in this document have been prepared based on available data to which IAM Capital Markets have access. Neither the accuracy of that data nor the research methodology used to produce the Content and Reports can be or is guaranteed or warranted. Some of the research used to create the Content and the Reports is based on past performance. Past performance is not an indicator of future performance. Any forecasts are predictive in character and based on specified assumptions generally available at the time and no reliance should be placed on the accuracy of any forecast information. The actual results may differ substantially from the forecasts and are subject to change without further notice. The data generated by the research in the Content or the Reports is based on research methodology that has limitations; and some of the information in the Content or the Reports is based on information from third parties. IAM Capital Markets does not guarantee the currency of the Content or the Reports. If you would like to assess the currency, you should compare the Content or the Reports with more recent characteristics and performance of the assets mentioned within it.

You acknowledge that investment can give rise to substantial risk and a product mentioned in the Content or the Reports may not be suitable to you. The Content and Reports have been provided or made available by IAM Capital Markets without taking account of your objectives, financial situation, and needs. IAM Capital Markets strongly recommends that you seek independent accounting, financial, taxation, and legal advice, tailored to your specific objectives, financial situation or needs, prior to making any investment decision. Neither IAM Capital Markets, nor any of its directors, authorised representatives, employees, or agents, makes any representation or warranty as to the reliability, accuracy, or completeness, of the Content and Reports. Nor does IAM Capital Markets accept any liability or responsibility arising in any way (including negligence) for errors in, or omissions from the Content and Reports. IAM Capital Markets, its staff and related parties earn fees and revenue from dealing in the securities as principal or otherwise and may have an interest in any securities mentioned in this document. Any reference to credit ratings of companies, entities or financial products must only be relied upon by a 'wholesale client' as that term is defined in section 761G of the Corporations Act 2001 (Cth). IAM Capital Markets does not provide tax advice and is not a registered tax agent or tax (financial) advisor, nor are any of IAM Capital Markets' staff or authorised representatives. IAM Capital Markets does not make a market in the securities or products that may be referred to in this document.

An investment in notes, corporate bonds, syndicated loans, or any debt instrument should not be compared to a bank deposit. Notes, corporate bonds, syndicated loans, or any debt instrument have a greater risk of loss of some or all an investor's capital when compared to bank deposits. IAM Capital Markets is not licensed to provide foreign exchange hedging or deal in foreign exchange contracts services. IAM Capital Markets may quote to you an estimated yield when you purchase a bond. This yield may be calculated by IAM Capital Markets on either A) a yield to maturity date basis; or B) a yield to early redemption date basis. Some bond issuances include multiple early redemption dates and prices, therefore the realised yield earned by you on the bond may differ from the yield estimated or quoted by IAM Capital Markets at the time of your purchase.

© 2024 IAM Group | Income Asset Management Group Limited ABN 42 010 653 862 (ASX: IAM) and wholly owned subsidiaries, IAM Capital Markets Ltd ABN 86 111 273 048 AFSL 283119, IAM Cash Markets Pty Ltd ACN 164 806 357 as corporate authorised representative (no. 001295506) of AFSL 283119, Trustees Australia Limited ABN 63 010 579 058 AFSL 260038 and IAM Funds ABN 54 643 600 088, together the IAM Group.

The information in this website is for general information purposes only and does not purport to contain all matters relevant to any particular or financial instrument. It is not intended to be a recommendation, offer or invitation to purchase, sell or otherwise deal in securities or other investments. Before making any decision in respect to a financial product, you should read the relevant Financial Services Guide and Product Disclosure Statement available from IAM Group <https://www.incomeam.com> and seek independent and specific advice from an appropriately qualified professional. IAM Group shall not be liable for any errors, omissions, defects or misrepresentations in the information or for any loss or damage (whether direct or indirect) suffered by persons who use or rely on the information contained here.