MODULE 4: Vocab & Key Terms

The Power Of Debt & Bonds

Fixed Income Securities

A type of debt instrument that provides a steady income stream in the form of interest payments (due at predetermined intervals) over the life of the security. Examples include bonds, CDs, and treasury notes.

Bond Yields

The rate of return on a bond calculated as its coupon rate divided by the current market price.

Credit Ratings

An evaluation assigned to bonds based on their creditworthiness and ability to repay investor's capital in full and on time. Generally, higher ratings indicate higher quality and more desirable bonds for investors.

Principal

The amount of capital initially lent to the borrower through the bond.

Face Value

The net present value of all future cash flows related to an existing bond. This is used to show how much the bond owner will receive through maturity.

Coupon

The dollar value of the periodic interest payment promised to bondholders (usually paid semiannually) **Coupon ($)=Coupon Rate x Face Value**

Yield to Maturity

Maturity is the length of time until the principal is scheduled to be repaid. The yield is the rate of return assuming the investor holds the bond until its maturity date. It rises and falls depending on the market value of bond and number of payments left until maturity

Internal Rate of Return (IRR)

The rate of return that sets the net present value of an investment equal to zero.

Interest Rate Risk

The risk associated with adverse changes in interest rates over time, causing prices for existing bonds to fall if rates rise or remain constant since new issues will be issued at current market rates which are typically lower than existing issues' coupon rates

Inflation Risk

The risk that inflation will erode purchasing power over time and reduce the initial value received from investments with fixed returns such as bonds and other fixed-income securities because they do not provide any protection against inflationary pressures.

Call Provisions

Certain clauses are written into bond contracts that allow issuers to buy back particular outstanding bonds prior to their maturity date under certain conditions such as reaching a preset price, redemption amount, or exceed a specified cap on maximum coupon payments.