

# Corporate Bonds

## What's this?

Companies (and governments) **borrow** money in Capital Markets by issuing/selling Bonds to Investors/Lenders.

Bonds are **Debt Securities** and the Borrower (Issuer) is obliged to **pay interest** and to **repay** the bond at a specified date (maturity Date).

## Terminology:

**Principal:** borrowed amount (Nominal / Par) -> e.g. 10,000,000 USD

**Coupon:** periodic interest payment (quarterly, annual) -> e.g. 500,000 USD p.a. / per 100 USD Par

**Coupon Rate:** Coupon Payments / Principal -> 5.0% p.a.

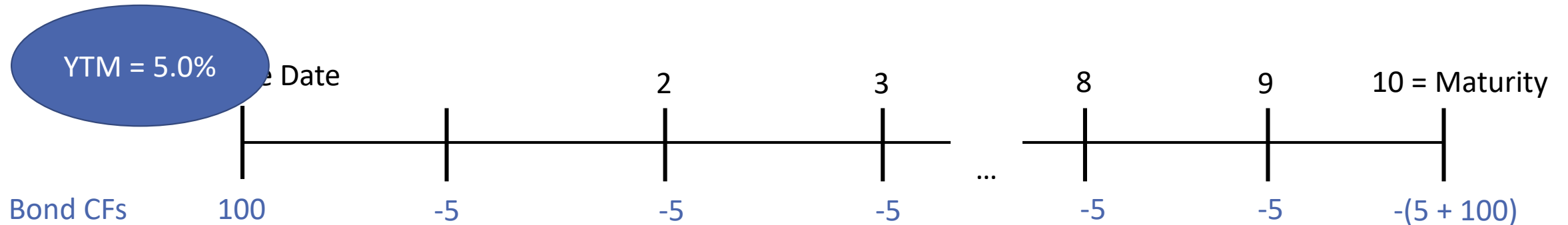
**Maturity:** Issuer repays Principal on the Maturity Date -> e.g. 5 Years from Issue Date

**Price:** Price of Bond at a specific point in time during the Bond's Term (per 100 USD Par)

**Yield to Maturity (YTM):** see next slides

# Corporate Bonds – Cashflows (1)

The XYZ Company issues a **10Y** Senior Unsecured Bond with a Coupon Rate of **5.0%** (annual payments in arrears).

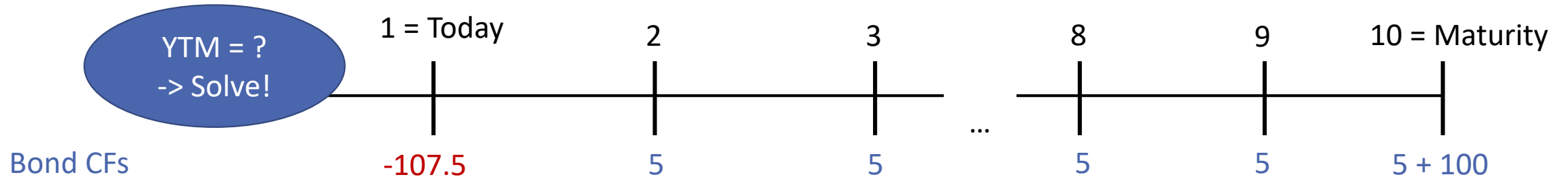


YTM is nothing else than the IRR on a Bond's Cashflows -> Bond's Rate of Return

At Issue Date (typically): YTM = Coupon Rate

## Corporate Bonds – Cashflows (2)

The XYZ Company issued a **10Y** Senior Unsecured Bond **one year ago** with a Coupon Rate of **5.0%** (annual payments in arrears). Today's Bond Price is **107.5** (per 100 par Value). Calculate the Bond's current **YTM**.



Reasons for **increasing** (**decreasing**) Bond Prices:

- **Falling** / **Rising** Interest Rates in the markets
- **Higher** / **Lower** credit quality (rating) of Issuer

# Corporate Bond - YTM

## Why is it useful?

If Price  $\neq$  Par(100): Coupon/Coupon Rate is not a useful metric for the Bond's Rate of Return

Investors: YTM shows what can be earned / Rate of Return

Investors: Easy to compare Bonds based on their YTM

Issuer: YTM of existing bonds good indication for Coupon Rate of upcoming Bonds

Issuer: YTM of existing long-term bonds is good approx. for cost of long-term Debt (part of WACC)