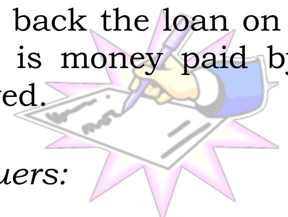
Activity Sheet 2: Kinds of Bonds

Bonds are loans - *very big loans*. There are many different bond issuers or organizations who sell bonds: U.S. corporations, the U.S. Treasury, cities and states as well as federal, state, and local government agencies. Many overseas governments and businesses also sell bonds on the U.S. market, as well as in international markets.

To insure the lenders making these very big loans are paid back, borrowers often need to show they have the ability to do so. Often you will hear the term “backed by” when reading about a bond. “Backed by” refers to what the company will sell in order to repay its debt (the money it borrowed).

Just like any other loan, the bond issuer agrees to pay back the loan on a set date and agrees to pay interest on the loan. Interest is money paid by the lender to the borrower in addition to the amount borrowed.

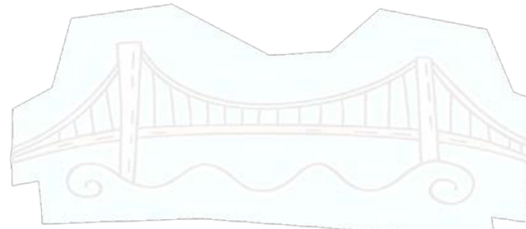


The chart below explains the four main types of bond issuers:

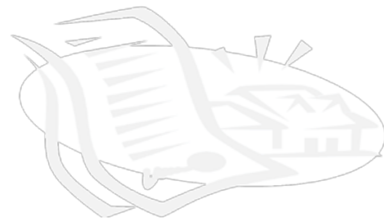
<u>Corporate Bonds</u> Bonds are major sources of corporate borrowing The most common type of corporate bond, are backed by the general credit of the corporation, Asset-backed bonds are backed by specific corporate assets, such as property or equipment.	**<u>Municipal Bonds</u>** Millions of bonds have been issued by state and local governments. General obligation bonds are backed by the full faith and credit of the issuer, Revenue bonds by the income generated by the particular project being financed.
<u>Agency Bonds</u> Some government sponsored but privately owned corporations (like Fannie Mae and Freddie Mac), and certain federal government agencies (like Ginnie Mae and Tennessee Valley Authority) issue bonds to raise funds either to make loan money available or to pay off new projects.	**<u>U.S. Treasury Bonds</u>** Treasury notes An intermediate-term obligation of the U.S. Treasury having a maturity period of one to ten years and paying interest semiannually. Treasury bills, A short-term obligation of the U.S. Treasury having a maturity period of one year or less and sold at a discount from face value.

Use what you read to answer the questions below:

1. The local government wants to build a new bridge to connect two parts of a growing city. Which type of bond would a local government issue? Why?

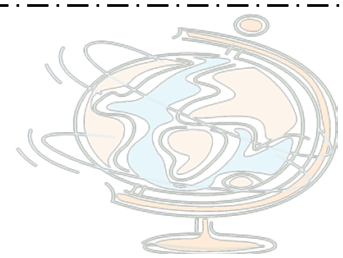


2. A home mortgage company backed by the government wants to raise money for more first time home mortgage loans. Which type of bond would the government sponsored agency issue? Why?



3. An investor wants to make the safest possible bond investment and plan to collect the interest for ten years. Which type of bond should the investor purchase? Why?

4. A large corporation wants to expand into Asian markets. They want to issue a bond and plan to guarantee the bond with land holdings in Latin America so What type of bond would they issue? Why?



5. A major corporation wants to issue a bond, they have a reputation for being a trustworthy company. They want to use their credit rating to guarantee the bond. What type of bond would they issue? Why?

6. An investor wants to support the increase of water power in America and would like to purchase a bond from the Tennessee Valley Authority. What type of bond would he purchase? Why?

