

Building Blocks of Wealth

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B IS FOR **Bonds**
LENDING MADE SIMPLE

WHAT IS A BOND?

A bond is an investment in which you lend money to a company or government. In return, they promise to pay you interest over time and return the amount you originally invested. That amount is called the principal, and it's paid back when the bond ends, or matures.

You can think of buying a bond as acting like the lender. Instead of borrowing money from a bank, you're lending money to a business, a city, or even the federal government. The bond is their written

promise to repay you with interest after a set period of time.

WHY BONDS MATTER

Bonds matter because they bring stability. Unlike stocks, which can rise or fall sharply, bonds usually move steadily. They may not deliver significant growth, but they provide regular income and balance risk.

For many investors, bonds act like an anchor in a portfolio. When markets swing up and down, bonds keep things more predictable and easier to manage.

Bonds come in several forms, each with its own purpose.

Government Bonds: Issued by the federal government. US Treasury bonds are considered among the safest investments because the government has never defaulted on its debt.

Municipal Bonds: Sold by states, cities, or towns to raise money for public projects like schools or highways. Often, the interest you earn isn't taxed by the federal government, which can make them especially attractive to some investors.

Corporate Bonds: Issued by companies to fund their growth or operations. They usually pay higher interest than government bonds but come with more risk if the company struggles.

How bonds can grow you money

BONDS DON'T MAKE YOU WEALTHY OVERNIGHT, BUT THEY CAN HELP IN THREE IMPORTANT WAYS:



Interest Payments

Bonds pay interest, often every six months. This income can provide stability.



Safety of Principal

At maturity, you get back the money you invested initially, unless the borrower defaults.



Diversification

Adding bonds to a portfolio of stocks spreads out your risk, since bonds often hold steady when stocks fall.

THE PROS AND CONS OF OWNING BONDS

Pros

PREDICTABLE INCOME: Bonds pay regular interest, which makes them appealing to cautious investors.

LOWER RISK: Government and many municipal bonds are generally safer than stocks.

BALANCE: Adding bonds to a portfolio helps smooth out volatility and creates steadier overall returns.

Cons

LOWER RETURNS: In the long run, bonds usually don't grow as much as stocks.

INFLATION RISK: If inflation rises faster than your bond's interest rate, the money you earn loses buying power.

DEFAULT RISK: With corporate bonds, there's always a chance the company could run into trouble and fail to repay its debts.



WHAT TO KNOW ABOUT BOND RATINGS

Not all bonds are equally safe. Credit rating agencies assign grades that show how likely the borrower is to repay.

AAA or AA bonds: These are considered very safe but usually pay lower interest.

Lower-rated bonds (junk bonds): Riskier, but they pay higher interest to attract investors.

These ratings give you a quick way to compare safety and return, helping you decide whether the reward is worth the risk.

WHAT ABOUT SAVINGS BONDS?

Savings bonds are special government bonds designed for individuals, not big institutions. They're simple, safe, and affordable.

Series EE bonds: These bonds are guaranteed to double in value if you hold them for 20 years. They earn a fixed rate of interest.

Series I bonds: These bonds protect you against inflation. Their interest rate changes every six months based on inflation, so they help your money keep pace with rising prices.

Savings bonds are often given as gifts or used to teach children about investing. They won't make you rich quickly, but they're backed by the US government and carry very little risk.

BONDS IN EVERYDAY LIFE

You might already own bonds without realizing it. Retirement accounts often include bond funds. Local governments issue municipal bonds to build schools, hospitals, or highways, and when you invest in them, you're helping fund those projects.

Savings bonds are often given as gifts, especially to children. For example, a grandparent might buy one for a grandchild. Over the years, the bond earns interest and becomes worth more than its original amount.

A QUICK EXAMPLE

Imagine Moshe buys a \$1,000 corporate bond with a 5 percent interest rate. Each year, the company pays him \$50 in interest. After 10 years, the bond matures, and he gets back his original \$1,000. Along the way, he earned a steady income, and he recovered his principal at the end.

THE TAKEAWAY

Bonds help keep an investment plan steady. They pay interest, protect savings, and balance out risk from other investments. Government and savings bonds are safe and easy ways for someone just starting to invest to begin.

Rivka Resnik is the author of three financial literacy textbooks—one for middle school and two for high school—available at cost price to any Jewish school through the OU and Living Smarter Jewish.