**3.4 What is a Bond?**
*Student Activity Packet*
UNIT: INVESTING

## Name:

## Students will be able to:

- Explain what a bond is and the pros and cons of investing in bonds
- Understand the various factors that can influence bond prices such as interest rates
- Identify the differences between an individual bond and a bond fund
- Read a bond fund fact sheet

**NOTE:** Vocabulary for this unit can be found in the NGPF Personal Finance Dictionary

## INTRO

**PROMPT:**
Use the space below to answer the prompt.

1. **Your friend asks to borrow $50 and offers to pay you back with interest. What factors would you consider in your decision to accept or decline their request?**

## LEARN IT

**EDPUZZLE: Investing Basics: Bonds**
Just as you might loan money to a friend, you can loan money to a government or corporation through a bond. Bonds are one of the most common investment options available to you. Watch this video to learn more about bonds and follow your teacher's directions to answer the questions either in your student activity packet or within the EdPuzzle itself.

*NOTE: EdPuzzle videos shuffle answer choices and do not always match the order provided in the lesson here.*

1. **All of the following are true about bonds EXCEPT…**
    a. Bonds are considered a riskier investment option than stocks.
    b. A bond is a loan given to a company or government by an investor who receives interest in return.
    c. Companies and governments issue bonds to fund new projects or ongoing expenses.
    d. Bonds are a way for investors to diversify their portfolios and generate additional income.

2. **By the end of a bond's maturity, the investor will have received…**
    a. Only the face value of the issued bond
    b. The face value of the bond issued and interest payments
    c. Only interest payments
    d. Half the face value of the issued bond and interest payments

3. **What is default risk?**
    a. The risk that the investor is not able to pay the face value of the bond.
    b. The risk that the company or government is not able to make interest payments.
    c. The risk that the investor demands the face value of the bond before the bond fully matures.
    d. The risk that the company or government is unable to pay back the investor.

4. **You've decided you want to sell a bond before its maturity date. Interest rates are currently higher than when you bought the bond. What will you likely have to do to make your bond more appealing to investors?**
    a. Lower the interest rate
    b. Sell your bond at a discounted price
    c. Increase the interest rate
    d. Sell your bond at a higher price

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**INFOGRAPHIC: What are the Main Types of Bonds?**
As you learned in the previous video, you can buy a corporate bond or a government bond. There are different types of bonds within these two categories as well! Read through the infographic on this page to learn about the different bond types. Then, answer the questions.

1. **The higher the risk associated with a bond, the _______ (more/less) likely a corporation might default on paying the investor. Interest rates for riskier bonds tend to be _______ (higher/lower) so that investors are _____ (more/less) willing to take on that risk.**

    **BONUS: A riskier bond usually comes from a corporation that has a _____ (low/high) credit rating.**

2. **Which tends to be a riskier investment - corporate bonds or government bonds? Why?**

3. **Which type of bond would you be comfortable investing in? Explain.**

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**INFOGRAPHIC:** [The Bond See-Saw]
**VIDEO:** [Back to Basics: Understanding Yield and the Effects of Rising Rates]
If you buy a bond and hold it through its maturity date, the ups and downs of the bond market will not impact your investment. However, if you decide to sell a bond before its maturity date, you need to understand how the current market's interest rates impact the price of your bond. Read through this infographic and watch the video to learn more about this relationship. Then, answer the questions.

1. **When overall interest rates rise (to 10%), the bond you already own (with 5% coupon rate) becomes _______ valuable to potential buyers, so its price will __________.**

2. **When overall interest rates fall (to 2%), the bond you already own (with 5% coupon rate) becomes ______ valuable to potential buyers, so its price will ____________.**

3. **Generally, the longer the duration of the bond, the ___________ (lower/higher) the chance the bond price may change due to changes in yield.**

4. **Explain why someone who is not interested in selling their bond before its maturity date does not have to worry about the current bond market and its impact on the price of their bond.**

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**VIDEO:** [Individual Bonds vs. Bond Funds: What's the Difference?]
When investing in bonds, most investors choose to invest in bond funds, rather than selecting individual bonds. Watch this video to learn about bond funds and how they differ from bonds. Then, answer the questions.

1. **Fill in the chart below with information about bonds and bond funds.**

| | Bond | Bond Fund |
|---|---|---|
| How you make money | | |
| Pros | | |
| Cons | | |

2. **Do you think you would invest in an individual bond or bond fund? Both? Neither? Explain why.**

## DO IT

**ACTIVITY: FINE PRINT: Bond Mutual Fund Fact Sheet**
When selecting a bond fund to invest in, it's important to analyze its fund fact sheet. In this activity, you'll practice reading a bond mutual fund fact sheet. Follow the directions on the worksheet to complete this activity.

## EXIT TICKET

Follow your teacher's directions to complete the Exit Ticket.