

### *Corporate Bond Funds*

Corporate bond funds seek a high rate of income by investing in bonds issued by corporations. Generally, the average maturity of the investments of these funds are less than ten years. Some corporate bond funds will mix their maturities by investing in short-term, intermediate-term and/or long-term securities. The average weighted maturities of the portfolios of these funds may vary between three to ten years.

Corporate bonds carry a higher interest rate than U.S. government securities, but they also carry a higher risk of default. That default risk will generally increase with the length of the bond's maturity. Further, the market for corporate bonds is not as liquid as the market for most U.S. government securities and may even be illiquid for some bonds.

#### **High-Quality Corporate Bond Funds**

Ratings for bonds vary from AAA for the highest quality bonds posing the least credit risk to lower ratings. AA and A ratings represent solid issuers that pose low default risk.

High-quality corporate bond funds seek to provide income to investors by investing in fixed-income securities rated by a nationally recognized statistical rating organization as A or higher. Some of these funds will, however, invest in BBB rated securities, while others may limit their investments to securities rated A or higher.

Usually, the maturity of the bonds held in the portfolios of a high-quality corporate bond fund is ten years or less, but this may vary. Remember that bond funds that have longer average weighted maturity dates will generally pay higher yields. Nevertheless, the prices of these funds and the net-asset values tend to be more volatile than bond funds with lower average weighted maturities.

#### **Convertible Bond Funds**

Convertible bond funds seek to provide income, but at the same time take advantage of capital gain opportunities where the price of the common stock makes conversion appropriate. These funds seek both growth and income.

Remember that the value of convertible bonds will usually drop when interest rates increase. Similarly, the value of the bond will decrease when the conversion feature becomes less valuable, as when the value of the stock into which it can be converted falls.

#### **High-Yield Funds**

High-yield corporate bond funds invest in junk bonds. These funds seek a high level of income by investing most of their assets in bonds rated below BBB. Bond funds seeking high income may also invest in floating rate loans.

High-yield or junk bond mutual funds seek to provide higher income than other fixed-income instruments. Such securities also impose more risk on the investor.

### *U.S. Treasury Security Mutual Funds*

United States Treasury mutual funds seek to provide current income through investments in United States Treasury securities. These funds have preservation of capital as their objective. They invest in United States government securities that are backed by the full faith and credit of the United States government. Usually the average maturity of the bonds held in the portfolio of these funds is less than ten years.

Some of these funds may also include obligations of U.S. government agencies in their portfolios. Remember that not all U.S. government agencies' certificates are fully guaranteed by the U.S. government.

United States Treasury mutual funds seek to provide a low default or credit risk to investors. The net-asset value of these funds will, nevertheless, fluctuate in value as interest rates change. This means that an increase in interest rates could result in a reduced value of the investor's mutual fund holdings.

#### *Long-Term Treasury Funds*

Long-term Treasury mutual funds seek to provide current income and preservation of capital through investments in United States Treasury securities where the average maturity of the securities in the portfolio is greater than ten years. These securities will often pay a higher rate of return than short-term securities. Remember, however, that their prices will fluctuate more than short-term securities.

#### *Mortgage-backed Mutual Funds*

Mortgage-backed mutual funds generally seek to invest in pass-through or collateralized mortgage obligations (CMOs) that are backed by United States government securities. Some GNMA pass-through certificates may be privately issued, but have securities in the pool that are United States government securities. Other pass-through interests may involve privately-issued mortgages. Mortgage-backed funds usually seek a high level of income while maintaining a strategy for preservation of capital.

Pass-through securities and CMOs pose special risks to investors. For example, pass-through securities present prepayment concerns. In the event that interest rates decline, the owners of the underlying mortgages will prepay their mortgages at a faster rate, reducing the average life of the pass-through security. The return of principal will then have to be reinvested at a lower rate.

CMOs seek to reduce prepayment concerns by issuing multiple tranches. Prepayments are delayed for certain of those tranches. These securities, however, are subject to an extension risk in the event interest rates increase. In such an event, investors will slow prepayments of their mortgages. The average maturity of the CMO will then increase even as its value declines.

#### *International and Global Bond Funds*

International bond funds invest in fixed-income securities of countries located outside the United States. These are referred to as international bond funds. Global bond funds will invest in the bonds of United States companies, as well as foreign securities.

These funds impose currency and other risks. There is also a serious default risk from securities issued by less-developed countries. Brady bonds and certain other foreign debt instruments have credit enhancement features that are designed to limit such risks.

## Fixed-Income Funds

| <b>Fixed-Income Funds</b>                |   |   |
|--|---|---|
| <b>Type</b>                              | <b>Goals</b>  | <b>Investments</b>                              |
| <b>Money-Market Funds</b>                | ~ Investment return based on current market rates     | ~ Variety of short-term instruments             |
| <b>Corporate Bond Funds</b>              | ~ High rate of income                                 | ~ Corporate bonds                               |
| <b>High-Quality Corporate Bond Funds</b> | ~ Provide income for investors                        | ~ High-quality corporate bond funds             |
| <b>High Yield Funds</b>                  | ~ High Income Level                                   | ~ Junk Bonds                                    |
| <b>Convertible Bond Funds</b>            | ~ Provide income<br>~ Take advantage of capital gains | ~ Convertible bonds                             |
| <b>U.S. Treasury Mutual Funds</b>        | ~ Provide current income<br>~ Preserve capital        | ~ U.S. Treasury securities (less than 10 years) |
| <b>Long-Term Treasury Funds</b>          | ~ Provide current income<br>~ Preserve capital        | ~ U.S. Treasury securities (more than 10 years) |
| <b>Mortgage-Backed Funds</b>             | ~ Invest in pass-through mortgage obligations         | ~ CMOs  |
| <b>International Funds</b>               | ~ Investment in foreign countries                     | ~ CMOs  |

### *Municipal Bond Funds*

Municipal bond funds invest in securities issued by state governments, municipalities, state and local agencies, or authorities that qualify for tax-exempt treatment. Municipal funds seek current income that will be exempt from federal taxes.

Municipal securities mutual funds are subject to the risks associated with their municipal bond investments. These may include credit, interest rate and other risks. Municipal bond funds may also invest in synthetic, variable or floating rate securities. These transactions are complex and may expose investors to additional risks.

### Municipal Bond Funds

Investment Objectives:

- Current income that will be exempt from federal taxes

May Invest In:

- State government securities
- Municipal securities
- State and local agency securities

- Synthetic, variable or floating rate securities
- Authorities that qualify for tax-exempt treatment

Risks:

- Credit risks
- Interest rate risks