BONDS Scarsdale Investment Group, Ltd.

All Bond Portfolios

Cross-Generational Conversations about Bond Investing

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An 81-year-old client had a conundrum. Short-term bonds are not yielding very much, forcing him to purchase longer-term bonds for a higher return. He did not want to purchase them because he is concerned about his heirs inheriting bonds that are longer-term which they may not value or want.

His question is not unique. It seems that when we consider purchasing long-term bonds and see maturities stretching ten to twenty years or more, and consider our health and age, we wonder if we will be around to see them mature. Clients may ask: Do you know how old I will be when the bonds come due? The finiteness of the maturities makes us ponder our own longevity and may lead us to think about what will happen when we’re gone.

The bonds' longer maturities seem to emphasize that the world will continue without us. We might die, but life goes on. People continue to work, pay their bills, invest in new infrastructure, take on debt and pay that debt. On some level, we do not want to accept the finiteness of our lives. Our glib answer to the question of age and bond maturities is: Your heirs will be happy with shorter-term bonds.

Why Buy Individual Bonds?

Somehow investors do not worry about the stock market outlasting them or drastically declining in value because the media is out to convince us that stocks only go up, in the long run. This is despite major stock market crashes, which devastate portfolios and cash flows, which only recover their past highs years into the future. We focus on the stock market milestones, not the length of time it took to achieve those milestones, or whether we have secured those gains by selling.

Bond funds also mask the maturity issues. Though bonds funds hold bonds, the portfolios actually function as quasi-stock portfolios because the shares of the funds never come due. The funds do not have a defined endpoint, so the bond holdings will continually be rejiggered. Fund managers will sell bonds that do not fit their fund's maturity parameters. They will purchase lower grade, riskier bonds to boost their return, and sell those bonds if they are downgraded to junk status.

In the midst of the Covid-19 economy, bonds backed by highway tolls, charter schools, college tuitions and dormitory revenue, transportation revenue, nursing homes and some other medical related revenue streams face downward rating pressure. Heather Gillers, writer for The Wall Street Journal, notes: "The S&P Municipal Bond High Yield Index has fallen more than 10% since the beginning of March [2020 to the end of April 2020], and some expect the deterioration to continue."[i]

Bond fund managements' objective is to maintain a high enough performance rating so they can hold onto existing investors and attract new ones. That entails taking risks that you otherwise might not embrace if you knew what bonds were held in the fund.

What the purchase of high-quality individual bonds provides is a known credit quality, good, predictable cash flow, and a defined date for return of capital. Bonds are the only asset class for which this is true: they come due (mature). They have an endpoint at which they will liquidate and return your principal to you. You do not have to sell in the market to regain your capital.

<u>Cross-Generational Conversations</u>

Our discomfort with the possibility of outliving our investments might encourage us to contemplate the ability of the next generation to manage the bond portfolios we have created. This might be a time in your life to reach out to your potential heirs and see if they have any interest in learning about what bonds are all about. This might be an opportunity for you to reach across the generations to educate your heirs about what they might potentially inherit. If not, they might be unprepared to fully appreciate the portfolio that you have created, and more likely be led to sell and invest in the more traditional risky assets.

It can be awkward when you try to talk across the generations. Marc Agronin, psychologist, wrote about cross-generational conversations during the corona virus.[ii] I have extrapolated his views to conversations about investing.

The forty somethings – many of whom have distant or limited relationships with their elders – suddenly find that their elders are trying to explain a way of investing that they do not comprehend. Raised on risk taking, without fully understanding the risks, they might not be able to comprehend how you could invest in bonds as your primary investment. Furthermore, Marc Agronin states, the forty-somethings feel a need to protect you from your frailties. They might sound abrasive, as they try to deter the older generation from what they consider foolishness.

Fifty and sixty-somethings may be coming from a different place. Accustomed to having to take care of both younger and older generations, they may begin to see themselves in a vulnerable place. They may lose their job or see it in jeopardy. They may realize that the older person susceptible to the corona virus is them. With the stock market gyrating and high yield junk bonds losing value, they might be willing to listen to a bond investor's methodology. After all, it is widely said that the percentage of bonds in your portfolio should increase as you age.

Seventy and eighty-somethings may have come to accept the perspective that life is limited. That this is the time they have to live and not worry about what the future will hold. This might include what are considered foolish expenditures or escapades from the perspective of the younger adults in the family. The younger generations may not understand why their seniors are taking what they see as unnecessary risks, such as meeting with friends, going to the store, or continuing their usual activities. The seventy and eighty-somethings, Marc Agronin says, know that time must be cherished and enjoyed.

What is most important overall is that we see each other as individuals with differing skill sets and needs. We need to listen to each other's stories, reflect on what is said, and be willing to accept the other as is. The only one we can change is ourselves.

And Our Spouses

Bond investors might also reach out to their spouses who may not been involved in the investment process. Our good friend Sam invested in bonds and hoped to leave a cushion of income for his wife, in the event that he predeceased her. After he died, she instead developed a friendship with a suave stock salesman who convinced her to sell all of her bonds for his alternative investments.

It is only by educating our spouses and the younger generation that they can come to appreciate the high-quality bond portfolio left for them that generates a predictable cash flow and preserves their principal.

We like to tell the story of a man who pleaded with his wife to let him take his money with him when he died. After much badgering, she finally agreed much to the dismay of her relatives and friends, for it was widely known. Upon his death, standing by the open casket, she dropped a check into the coffin. She told him: "Here is a check for the full amount of your assets. Please feel free to cash it whenever you can." Thus, she kept her promise and maintained her sanity.

The Cycle of Life

The philosopher, Eckhart Tolle states that the opposite of death is not life, but birth. Life, he says, is eternal. He describes how a fallen log in a forest is covered with new life, as the bugs find a home and new plants root in the rotten log. I find this very comforting to see how the cycle of life renews itself.

I see bond investing in the same light. Each generation has new needs. Those needs are translated into projects requiring capital that is funded by issuing bonds. The projects are built and the bonds are redeemed. The cycle continues so long as our country stays strong. It is in the interest of our governments to see that bond investors are protected so bond investors are willing to reinvest and grow our country’s economy.

How to Make a Connection

However, if we ever hope to tell our children about why we believe in the All Bond Portfolio, we must start with finding out about them. We must ask questions about their lives. Ask questions about how they are feeling and coping, what they need, and how they perceive the future.

If they feel comfortable, they might even have some questions for you. Perhaps one simple way to open up the conversation is to add your love-ones to our newsletter, at our website: www.allbondportfolios.com.

Key Words: S&P Municipal Bond High Yield Index, Marc Agronin, Eckhart Tolle, cross-generational conversations, Why Buy Individual Bonds?, Bond Funds Differ from Individual Bonds

[i] Heather Gillers. Virus Pressures Higher-Risk Munis." *The Wall Street Journal.* April 28, 2020.

[ii] Marc Agronin. "Why It's So Hard to Talk to Your Parents About the Coronavirus (and Vice Versa). *The Wall Street Journal.* April 20,2020.