INVESTOR EDUCATION

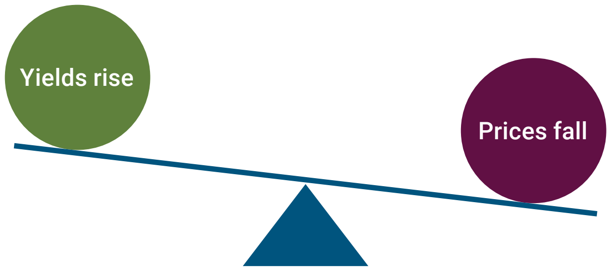
PIMCO

5 Things you Need to Know About: Rates

When interest rates move, it's not just borrowers who are concerned with the outcome. As an important driver of bond prices, interest rates are also closely watched by bond investors.

1. INTEREST RATES AND BOND PRICES

One of the key drivers of bond pricing is interest rates. If rates rise, older bonds with lower rates will drop in price to compensate for the lower coupon payments (and vice versa).



2. THE INFLATION DOUBLE THREAT

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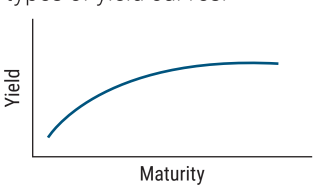
Inflation erodes the purchasing power of future income payments from bonds.	Inflation can lead to interest rate increases which, in turn, push down bond prices.

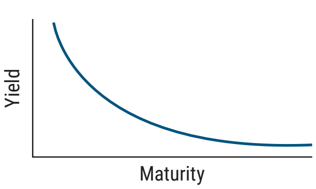
3. THE YIELD CURVE

The yield curve plots the interest rates for similar quality bonds against their maturities (years to expiration). There are three main types of yield curves.



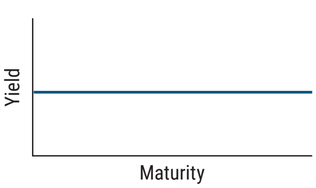
Normal Yield Curve

Seen during periods of economic expansion, it indicates that long-term bond yields are higher than short-term yields.



Inverted Yield Curve

Seen during periods of recession, it indicates that long-term bond yields are lower than short-term yields.



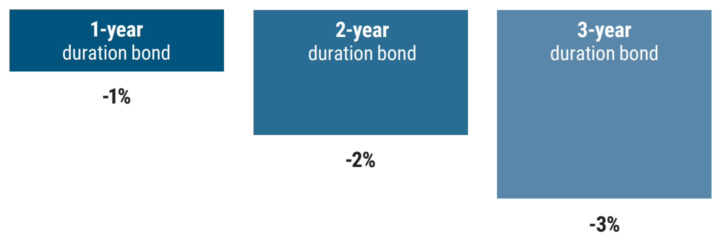
Flat Yield Curve

Seen when the economy is transitioning from expansion to slowdown (and vice versa).

4. DURATION RISK

Duration risk reveals how sensitive a bond is to interest rate movements. In general, the higher the duration, the more the bond value will fall if interest rates rise.

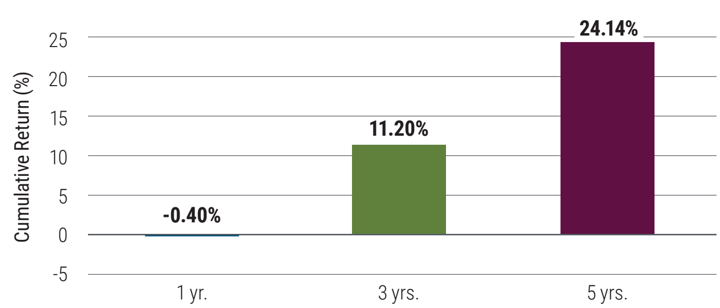
How a 1% rise in interest rates impacts bonds with different durations



5. RISING RATES

Rising rates don't have to mean bad news for bond investors. As the chart shows, a fixed income investment may decline in the short-term because the existing bond holdings fall in price. However, higher interest rates lead to a higher yield on the invested bonds in subsequent periods. Investors can also reinvest maturing bonds into higher-yielding securities, which can return a bond portfolio back to growth more quickly.

The upside of rising rates



Sample for illustrative purposes only. Source: PIMCO, as of 31 August 2023. The chart shows the estimated performance of the Bloomberg U.S. Aggregate Index assuming a parallel rate rise of 1%, and no further changes in rates thereafter. Credit spreads are assumed to remain constant. In the analysis contained herein, PIMCO has outlined hypothetical event scenarios which, in theory, would impact the index returns as illustrated in this analysis. No representation is being made that these scenarios are likely to occur or that any portfolio is likely to achieve profits, losses, or results similar to those shown. The scenarios do not represent all possible outcomes and the analysis does not take into account all aspects of risk. Total returns are estimated by re-pricing key rate duration replicating portfolios of par-coupon bonds.

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CMR2023-0907-3102983