

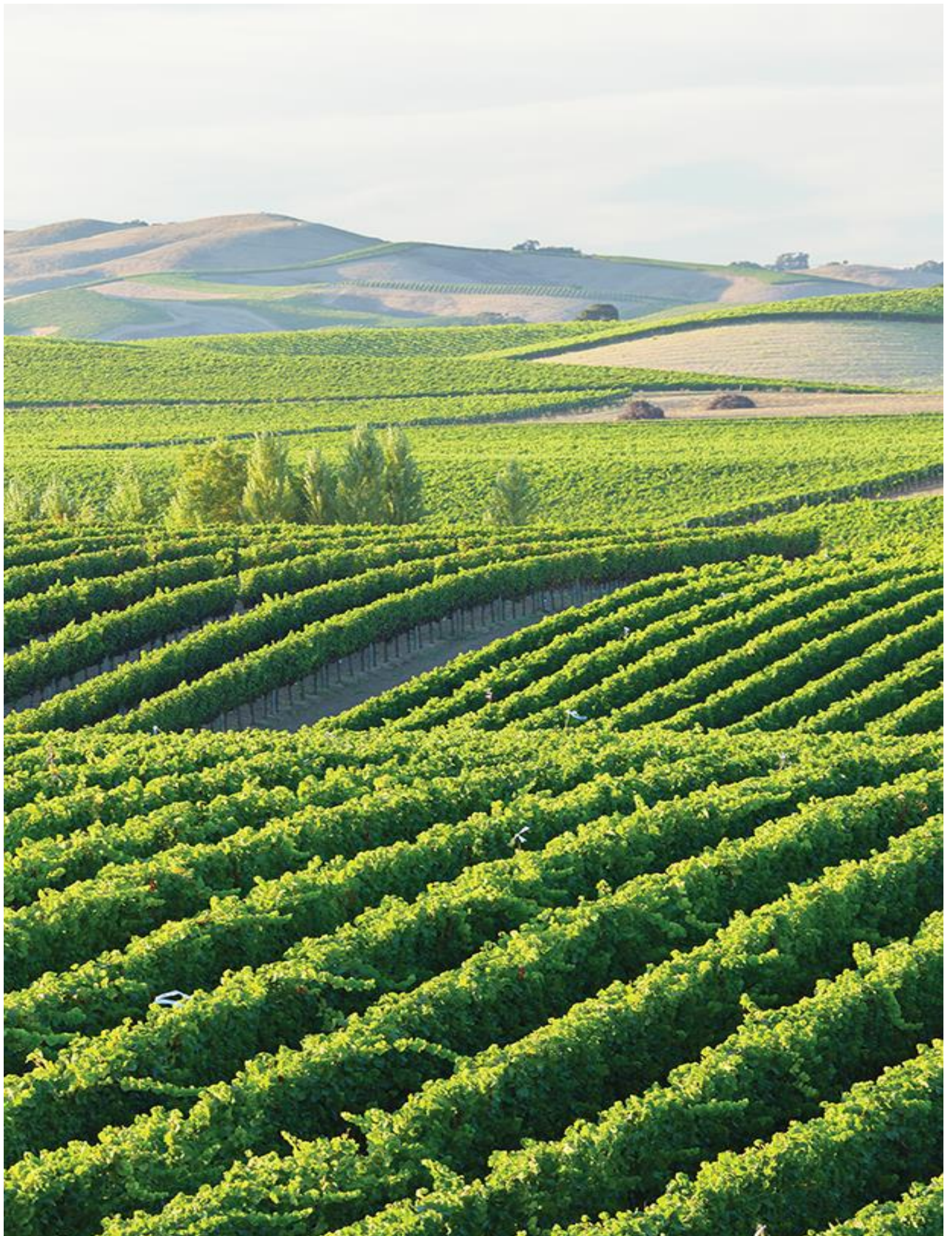
The Quick Start Guide

To U.S. Treasury Bonds

Investor Education

Hawk Hill Wealth Management Group





Summary

US Treasury Bonds offer investors a unique and compelling opportunity to secure an investment backed by the full faith and credit of the US government.

They're widely considered as one of the safest investments available.

This document aims to explain options for acquiring these instruments and help potential investors gain a basic understanding of the characteristics of these investments.



Purchase Options

Primary OR Secondary

Treasury bonds, like other securities, can be purchased in both primary and secondary markets. Let's delve into the differences and characteristics of both markets.

Primary Market

The primary market is where new securities are issued directly by the U.S. Department of the Treasury to investors. Here, investors purchase bonds directly from the source.

Advantages:

Direct Purchase: Investors buy bonds directly from the government at a price that's determined at auction.

No Middlemen: Since the purchase is direct, there are typically no brokerage fees associated with buying Treasury bonds in the primary market.

Digital Platform: TreasuryDirect is the official online platform used by individual investors to purchase and manage U.S. government securities directly in the primary market.

Disadvantages:

Limited Availability: Investors can only purchase bonds during specific auction times.

Bid System: Depending on the demand, investors may need to place competitive bids to secure bonds, which can be a bit complex for some.

Limited Trading Abilities: TreasuryDirect is designed primarily for buying and holding securities. Users needing to sell a bond prior to maturity will find the platform limiting.

Account Recovery Issues: Users report challenges recovering accounts after losing login details, facing a cumbersome process and long wait times on helpline calls with US Federal Government staff

Secondary Market

The secondary market is where investors buy and sell previously issued securities. These bonds are sold by and bought from other investors, not the government.

Advantages:

Liquidity: Treasury bonds in the secondary market are highly liquid. Investors can easily sell their bonds if they need cash before the bond's maturity.

Diverse Options: Investors have access to bonds with a wider range of maturities than what's currently being offered in the primary market.

Broker Integration: Many commercial brokerages allow for the purchase and sale of Treasury bonds in the secondary market, making it convenient for investors to manage their entire investment portfolio in one place.

Access Expertise and Knowledge: Some brokerages assign registered advisors to larger client accounts; these advisors are available to answer questions which can mitigate any potential errors to optimize investor results.

Disadvantages:

Bond Markup: Purchasing bonds in the secondary market often has a slight markup, unlike the primary market. While US Treasury bonds typically have a markup below 0.10%, this can reduce the Yield to Maturity compared to buying the same bond in the primary market.

Increased Complexity - Navigating the secondary market can be complex for an individual investor due to its vast array of choices, intricacies of interest rates, and other influencing factors.

Account Minimums – Many online discount brokerages have adapted their platforms for secondary bond transactions, but most such trades occur through major firms catering to wealthy individuals and institutions. These large firms often have account minimums, which can deter smaller investors.

Understanding Taxable Equivalent Yield (TEY):

Taxable Equivalent Yield (TEY) is a concept primarily used when comparing the potential returns on taxable investments, like bank CDs, to tax-exempt investments, such as municipal bonds. However, when discussing U.S. Treasury bonds, the concept can be adjusted slightly.

U.S. Treasury bonds are subject to federal income tax but are exempt from state and local taxes. Therefore, for an investor considering U.S. Treasury bonds, the taxable equivalent yield can help compare the after-tax yield of a Treasury bond to a fully taxable investment.

Here's a brief explanation:

Taxable Equivalent Yield = Treasury Bond Yield / (1 – State Tax Rate)

Where:

Treasury Bond Yield is the yield on the U.S. Treasury bond.

State Tax Rate is the investor's marginal federal tax rate.

For example, let's assume a U.S. Treasury bond yields 5.45% and a California investor's state tax rate is 12.3%.

$TEY = 0.0545 / (1 - 0.123) = 0.0545 / 0.877 = 0.0621$ or 6.21%

This means that for this particular investor, a taxable CD would need to yield at least 6.21% APY to be equivalent to the after-tax yield of a 5.45% Yield U.S. Treasury bond.

It's essential for investors to use the TEY to make informed comparisons between taxable and tax-advantaged investments.

Conclusion:

US Treasury bonds represent a secure investment, backed robustly by the US government. Whether purchased from the primary market for direct acquisition and fewer fees, or the secondary market for liquidity and varied maturity choices, the choice largely depends on individual investor goals.

With tools like the Taxable Equivalent Yield, investors can further make informed decisions on their investments, balancing between taxable and tax-advantaged opportunities.

The key is understanding one's unique investment priorities and leveraging available information to optimize returns.

Investment and insurance products offered through RBC Wealth Management are not insured by the FDIC or any other federal government agency, are not deposits or other obligations of, or guaranteed by, a bank or any bank affiliate, and are subject to investment risks, including possible loss of the principal amount invested. RBC Wealth Management does not provide tax or legal advice. All decisions regarding the tax or legal implications of your investments should be made in connection with your independent tax or legal advisor. No information, including but not limited to written materials, provided by RBC WM should be construed as legal, accounting or tax advice.

© 2023 RBC Wealth Management, a division of RBC Capital Markets, LLC, Member NYSE/FINRA/SIPC. All rights reserved.

