Teaching Note
Reinvestment Risk: Bonds

<https://www-classroom.wharton.upenn.edu/reinvestment-risk/>

A. Case Overview: presents a synopsis of the exercise that is being taught.

When a significant portion of a bond investor’s revenue may be dependent upon reinvesting coupon payments, it becomes essential to understand and assess reinvestment risk. Most students will be familiar with yield to maturity (YTM) as an approach to understanding bond valuation. This Teaching Tool explores the difference between YTM and realized compound yield (RCY) as an introduction to reinvestment risk.

In the assignment, students select a bond’s price, coupon rate, and time to maturity. In addition to calculating YTM from these values, the unique tool also enables students to enter one additional variable: what they believe the reinvestment rate will be for the coupon payments. They can then use the tool to compare the YTM with the realized compound yield at their selected reinvestment rate.

B. Learning Objectives: after this lesson the following objectives should be met.

Upon completing this assignment, students will:

* Understand the difference between yield to maturity (YTM) and realized compound yield (RCY)
* Learn about exposure to reinvestment risk

C. Teaching Approach/Pedagogy: an explanation of how the lesson will be taught, and who the target audience is.

Undergraduates are the primary target audience for the case. Although no prior knowledge is assumed, a background in [Time Value of Money](https://wrds-www.wharton.upenn.edu/pages/classroom/time-value-money-compound-interest/) and [Bond Valuation](https://wrds-www.wharton.upenn.edu/pages/classroom/bond-valuation/) concepts would be helpful. Assignment instructions are found in the accompanying PowerPoint slide deck, which you may distribute to students.

D. Assignment and Discussion Questions: provides questions that stimulate thought and facilitate understanding of the lesson.

1. Why can the realized yield on a bond be different from the anticipated yield on a bond?
2. What are some ways to mitigate reinvestment risk?

E. Conclusion and Feedback: assesses whether learning objectives were met and solicits feedback from students about the effectiveness of the assignment.

Were the learning objectives met? Be sure to solicit feedback from students in order to ascertain what worked and what didn’t work with the assignment.

**YOUR FEEDBACK IS VITAL TO THE WRDS CLASSROOM INITIATIVE. PLEASE USE THE FOLLOWING LINK TO SEND COMMENTS AND SUGGESTIONS:**

[**https://wrds-www.wharton.upenn.edu/contact-support/**](https://wrds-www.wharton.upenn.edu/contact-support/)