PERSONAL FINANCE

# Coronavirus-panicked investors may turn to this investment to get the best of both stocks and bonds

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## KEY POINTS

- Convertible bonds are a hybrid investment that offer some downside protection through their bond status but also can later be converted to common stock of the issuing company.
- These investments are not risk-free, however.
- Funds that focus on convertibles were down 13% in the first quarter, compared to at least 20% in the major stock indexes.

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These hybrid investments are corporate-issued bonds that pay interest — generally higher than U.S. Treasury rates but lower than those on regular corporate bonds. After a predetermined length of time — usually four to seven years — or when the company's shares reach a certain price, the convertibles convert to a certain amount of stock.

"They give you the opportunity to get upside potential but also downside protection," said Zachary Patzik, a fixed income strategies analyst at Morningstar. "If you look at how the performance has been over the years, it's been a pretty solid stream for investors."

*Image Source | Getty Images*

The U.S. convertible bond market is worth about $200 billion, a small slice of the full investing universe. While there are mutual funds and exchange-traded funds that focus on convertibles, other funds or investment managers also use them as part of a broader strategy.

weaker credit ratings, or have generally less immediate financial soundness but good growth potential.

Cruise line operator Carnival, for instance, recently issued $1.75 billion in convertible bonds with a 5.75% interest rate. The company has taken a big hit to revenue as the coronavirus pandemic and resulting economic fallout has upended the travel industry. Carnival's stock price has plummeted this year to about $12.50 from above $38, a drop of about 75%.

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While Carnival may very well recover, an investor in any convertible bond runs the risk that the issuing company will go belly up before the conversion happens. Of course, there's always the bankruptcy danger with individual stocks, as well.

"If you're looking for bond exposure, where you want a portion of your portfolio to not behave like stocks, then convertibles aren't what you should be buying," said certified financial planner Kashif Ahmed, president of American Private Wealth in Bedford, Massachusetts. "When stocks fall, convertibles do, as well."

faring, was down 20% in the first quarter. Likewise, the Dow Jones Industrial average was down about 23% in that time period.

While convertible bonds slid, as well, the loss was less: a bit under 13% in the convertible funds tracked by Morningstar.

“We like them because they ameliorate risk,” said CFP David Demming, founder and president of Demming Financial Services in Aurora, Ohio. “They provide the opportunity to earn high single digits or even maybe low double digits.

“They won’t be the highest-performing, but they add a different dimension to your portfolio.”

Of course, with economic conditions worsening in the U.S. and questions over whether all hard-hit companies will come out of this intact, it’s worth being cautious.

“In this environment, if convertible bonds are available at a reasonable price, smart

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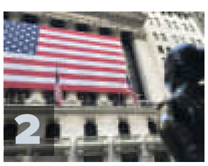

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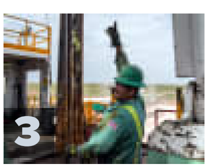

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