The Six Biggest Mistakes and How to Avoid Them

A resource guide for people interested in owning municipal securities in their portfolios

Moors & Cabot Investments
EST. 1890

How to Avoid the Six Biggest Muni Bond Buying Mistakes

They say we learn from our mistakes, but how about not making them in the first place? At the very least, you can try to avoid the expensive ones.

The problem is, how can you learn from a mistake that you don't even know you're making? It's kind of like the tree that falls in the forest when no one's around to hear it. Does it make a sound?

A better idea is to learn from other people's mistakes.

One thing is certain, and that is when you review billions of dollars in bonds each year (like we do), you see people make a lot of careless mistakes. We know it's not their fault. The muni bond market is complicated, and people have many ways to invest in muni bonds.

The problem is that there are just too many choices, the choices are complicated, and getting the best advice isn't always easy because even the best financial advisor is not necessarily an expert in muni bonds. The reason for this guidebook is to help you avoid the six biggest muni bond buying mistakes; to help you be aware!

After you read this guidebook, you may realize the impact of past missteps. By all means, please go easy on yourself—no one can blame you for making a mistake you did not know you were making.

1: Ask the Right Questions

Most investors don't directly own muni bonds in their investment portfolio because the why, what, who, how, when, and where of owning muni bonds can be confusing. (Don't even get us started on all the misunderstanding about fixed income in general!)

The biggest challenge for investing in muni bonds has to do with all the options available. Most investors don't know how easy it is to own a custom muni bond portfolio and the advantages of doing so. This is why people end up in pooled investments like large mutual funds, exchange traded funds (ETFs), or in large separately managed accounts (SMAs).

Don't get us wrong, owning a large muni bond fund, ETF, or SMA is fine if you have limited financial resources or your organization's individual retirement program doesn't allow you to hold individual securities. Otherwise, why would you limit your investment options before considering every opportunity to improve your investment results? It so happens that some investments are complicated and require expertise that you or your financial advisor simply may not have.

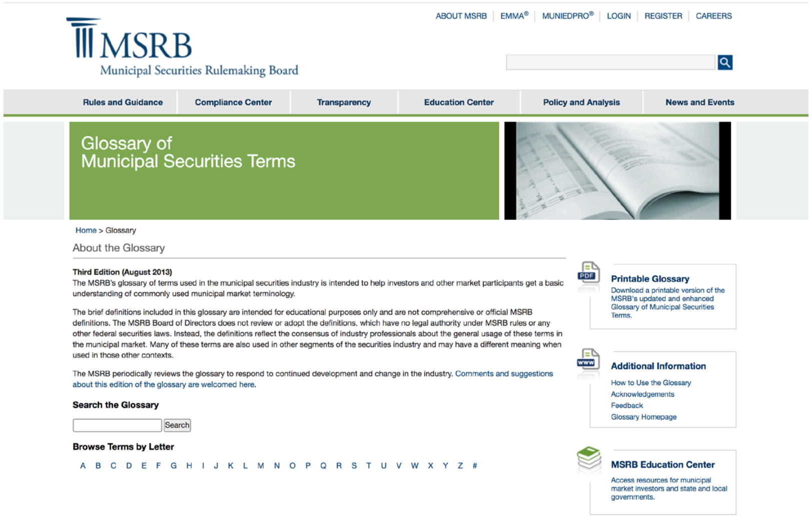
There are other reasons large institutions want you in a large fund, ETF, or SMA, but we won't go there. If you are reading this, you probably don't need us to tell you that it's easier to put every client in a one-size-fits-all investment instead of a custom portfolio that meets an individual's specific needs.

Before you find yourself in a one-size-fits-all investment, consider the six essential questions:

- ☐ **Why should I consider muni bonds?**
- ☐ **What is the risk in owning muni bonds?**
- ☐ **How do I know which muni bonds to own?**
- ☐ **When is the best time to invest in muni bonds?**
- ☐ **Where can I access quality muni bonds?**
- ☐ **Who should manage my muni bonds?**

Keep reading and learn the answers to these questions and much more.

While you're at it, here's a handy [Glossary of Municipal Security Terms,](#) produced by the Munici-pal Securities Rules Board [(MSRB)](#), that will help you along the way.



2: Get the Best Price

What you end up paying for your muni bonds depends mostly on where and how you buy them. Different trading systems offer different pricing and things can get downright expensive—relatively speaking. Here's some great info from Municipal Securities Rulemaking Board (MSRB) on the subject:

MSRB

How Are Municipal Bonds Quoted and Priced?

There is no simple answer to the question, "What should the price be, exactly?" Many factors affect the pricing of investments. For municipal bonds, both during an initial offering, called the "primary market", and in later "secondary market" trading, factors that affect the price include credit quality, the prevailing interest rates for bonds generally and for similar bonds more specifically, and broad market trends that can make investors more or less likely to prefer investing in debt over equity (i.e., stock).

Here's a link to MSBR to read more >>

Here are the most common terms associated with a muni bond that affects pricing:

- **Coupon:** the annual interest rate that the bond issuer agrees to pay you
- **Maturity Date:** the date that the bond issuer will pay back the principal to you and stop making interest payments
- **Call Date**: the date that the bond issuer may call the bond by paying back principal, accrued interest, and stop making interest payments
- **Yield-to-Maturity (YTM):** the total amount of interest plus principal you would earn if you held the municipal bond to its maturity date
- **Yield-to-Call (YTC):** how much you would earn in interest and principal if you held the bond only to the call date

Although there are many websites that provide muni bond pricing for an annual subscription, such as MunicipleBonds.com and BondView.com to get current pricing you need to go through bond dealers, banks, brokerage firms, and in some cases, directly through municipalities.

Of course, you can alway reach out to us if you're interested in building a personalized muni bond portfolio.

3: Beware of Benchmarks

A benchmark is a standard that other similar items can be compared to. In investing, benchmarks are indexes created to include multiple securities representing some aspect of the total market. Benchmark indexes represent all types of asset classes. The S&P 500 and Dow Jones Industrial Average are two popular examples of large-cap stock benchmarks.

Let's be clear—there is nothing wrong with benchmarks. Everybody needs a standard or point of reference to compare things to.

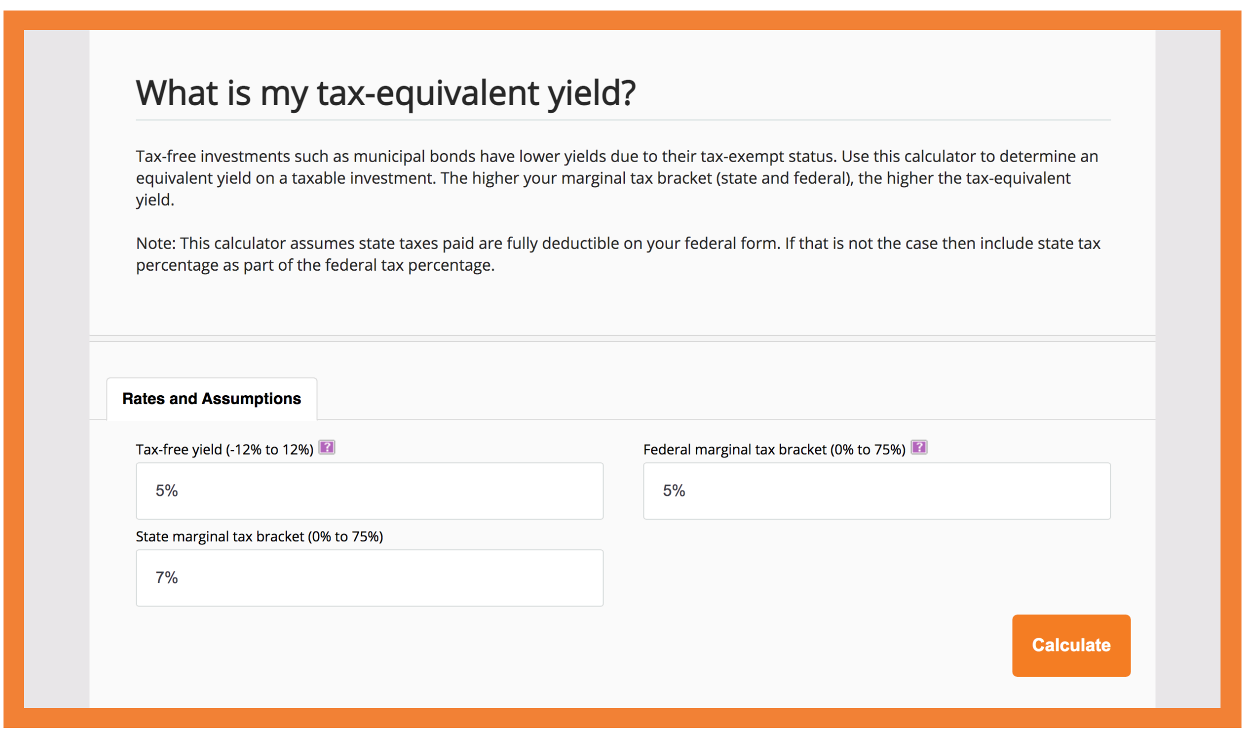
Institutions use benchmarks as a standard against which the performance of a security, mutual fund, or investment manager can be measured. This can be a useful tool when sorting through the myriad of options available today. The predicament is in the tendency to over-apply a broad measurement to determine individual requirements, because...

You are not an institution. Your needs are unique to your situation.

Broad market benchmarks are good for seeing the big picture, but individuals should benchmark their performance to their specific investment objectives, including their tax situation, risk tolerance, and time horizon.

Large mutual funds, ETFs, and SMAs track an institutional benchmark, and at a high level, this is a good thing. However, when it comes to reaching your investment goals, go beyond a traditional benchmark and make sure the investments you own meet your needs. This is where a financial professional can make all the difference through a comprehensive planning process. In the meantime, try this tax-equivalent calculator to determine if you could benefit from the tax advantages of a personal muni bond portfolio:

https://www.calcxml.com/calculators/inc11



4: Kick the Ladder

Everyone knows a ladder is good for grasping things that are out of reach. Not everyone knows, though, that a bond ladder is a portfolio of fixed-income securities that have staggered annual maturity dates in 1 year, 2 years, 3 years, etc...

Another thing not everyone knows is that if you have been in a bond ladder over the past several years, chances are you have been sacrificing yield. This is because a bond ladder (purchasing bonds with a formulaic maturity schedule regardless of yield) is relatively ineffective in this low interest rate environment and has been for many years. An alternative is simply investing for value, not following a ladder formula that may hurt your yield.

For example, a kicker/cushion bond is a callable bond that is priced assuming it will be redeemed at a future call date in advance of its final maturity. These typically provide material yield improvements over non-callable bonds. If you truly do need a ladder, you can ladder call dates with kicker/cushion bonds and earn more yield, sometimes 1% to 2% more yield, and reduce your duration/interest rate risk in the process.

What we are talking about is active management at a personal level. By contrast to a bond ladder, we are not necessarily waiting for bonds to mature and instead opportunistically seeking to purchase and sell securities to add value, taking advantage of market inefficiencies. In today's low-rate world, this is imperative.

The thing about this kind of investing is that it requires a highly experienced bond professional who is constantly watching the market to find opportunities as they arise.

The municipal bond market has a plethora of bonds to choose from, and the combination of quality, maturity, call date, and coupon is critical to identifying value.

Good choices are essential service revenue bonds, essential to our everyday life—such as infrastructure like airports, bridges, tunnels, and water systems. Because they are essential, they can make a pretty good hedge against the possibility of the bonds defaulting, and they may be a better alternative to a bond ladder of General Obligations (GOs). Also, GOs with high quality profiles are great portfolio additions. Ultimately, it comes down to the combination stated above that drives whether you have good or poor values in your portfolio.

5: Always Remember, Ratings Can Be Overrated

When governments and corporations issue bonds, they often pay to receive a credit rating on the creditworthiness of the debt from some or all of the major ratings agencies including: Standard & Poor's, Moody's, and Fitch Ratings.

These ratings incorporate a variety of factors, such as an issuer's financial strength and future potential, and they provide an indicator of the likelihood a bond will default or fail to make its interest and principal payments on time.

To make matters a little more murky, look no further than what the ratings agencies say about how their own ratings are "opinions and are not to be relied upon alone..., do not forecast future market price movements, and are not recommendations to buy, sell, or hold a security."

What good is a ratings agency? They are a loose guideline to point you in the right direction but cannot be your sole source, as ratings are often out of date...sometimes a decade old.

Keep in mind that ratings agencies can be reactive, not proactive. Unfortunately, many fixed income investors rely almost completely on these ratings to make their investment decisions. Don’t get us wrong, we believe ratings agencies serve an important purpose, just not necessarily the one the average investor relies on them for.

With all this in mind, here are the bond credit rating categories with a brief explanation of each:

RATINGS AGENCY

S&P GLOBAL RATINGS DEFINITIONS

FITCH RATINGS DEFINITIONS

MOODY’S RATINGS SCALE AND DEFINITIONS

6: Don’t Fear Commitment

(with a quality muni bond portfolio and an experienced bond trader)

Typically, a long-term bond has higher risk and higher yield than a short-term bond. This is because when interest rates go up, the value of your bonds will go down and vice versa. So, you get paid more for taking longer interest rate exposure, which is the risk of price fluctuation due to interest rates rising.

Here’s an example of a one percentage point increase to a short-, intermediate-, and long-term treasury bond, based on data on 5/10/2021:

- 2 year............1.94% loss
- 5 year............4.66% loss
- 10 year..........8.72% loss
- 30 year..........19.44% loss

There is a big difference between muni bonds and treasury bonds, and—unfortunately—people apply this basic concept about maturities when selecting their muni bonds. This ignores the opportunity for higher yields and lower risk typically hidden from the untrained eye.

You Can Do It!

Now that you know the six biggest muni bond buying mistakes, you are better prepared to build a muni bond portfolio that meets your unique investment goals. That is, if you are up for digging into the resources we've provided in this document.

With a Little Bit of Hard Work, It's Doable!

If you find you do want help building a custom muni bond portfolio, you can give us a call—we are always happy to be of service.

About Moors & Cabot

Since 1890, the year we were founded, investments in bonds have played an essential role in building our country. Since the original tax code was enacted in 1913, we have been helping clients, just like you, benefit from the tax advantages muni bonds provide.

Disclaimer

Member of SIPC, which protects securities customers of its members up to $500,000 (including $250,000 for claims for cash). Explanatory brochure available upon request or at www.sipc.org.

Past Performance is not indicative of future results. Municipal Bonds are issued by state and local governments and their agencies. They include general obligation debts backed by the full faith and credit of the issuer, as well as revenue bonds guaranteed by a particular stream of revenue. Municipal bonds can be either tax exempt or taxable under current law. Please consult a tax professional for more information.

Contact:

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INVESTMENTS

Effective January 2021

Customer Relationship Summary

Helping you make an informed decision — Form CRS

Introduction	Moors & Cabot (M&C) is registered with the Securities and Exchange Commission as a broker-dealer and investment adviser. The firm is also actively engaged as an insurance broker or agent as well as a registered municipal advisor. Moors & Cabot is a member of the New York Stock Exchange (NYSE), Financial Industry Regulatory Authority (FINRA) and Securities Investor Protection Corporation (S.I.P.C.) Please note that brokerage and investment advisory services and fees differ. It is important for the retail investor to understand the differences. Free and simple tools are available for you to use at https://www.investor.gov/CRS, a website maintained by the SEC. These tools can provide you with educational materials about broker-dealers, investment advisers, and investing. This relationship summary provides information that helps you make an informed decision about whether or not to invest with us and will answer the following questions: • What investment services and advice can you provide me? • What fees will I pay? • What are your legal obligations to me when providing recommendations as my broker-dealer, or when acting as my investment adviser? How else does the firm make money and what conflicts of interest do you have? • How do your financial professionals make money? • Do you or your financial professionals have legal or disciplinary history? • Where can I find additional information?
Important Terms	• A **broker-dealer** is a firm that acts as an intermediary between buyers and sellers of securities for which they will usually receive a commission and may purchase or sell those securities in/out of their own account. • An **investment adviser** is generally any person or group that provides investment advice or conducts securities analysis in exchange for a fee.

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What investment services and advice can you provide me?

M&C offers both brokerage services and investment advisory services to retail investors and institutional investors. Clients may include individuals, high net worth investors, charitable organizations, corporations and other business organizations.

We are a full service wealth management and investment firm. Our capabilities include equity and fixed income sales & trading, portfolio management, retirement planning, insurance and annuities, trust services, municipal finance, banking and cash management services, etc. In addition, we offer alternative investments and tax credits.

Additional information about brokerage and advisory services is available at www.moorscabot.com.

Conversation corner

Questions you might wish to ask when considering our services:

- Given my financial situation, should I choose an investment advisory service? Should I choose a brokerage service? Should I choose both types of services? Why or why not?
- How will you choose investments to recommend to me?
- What is your relevant experience, including your licenses, education, and other qualifications? What do these qualifications mean?

Brokerage Services

Brokerage services allow you to provide us with instructions to buy, sell and hold your investments. Depending on your account type, we may make recommendations about your investments. You make each investment decision and do not delegate such decisions to us. Applicable federal and state securities laws, regulations and self-regulatory organizations set forth our responsibilities. Your investment professional helps you identify your investment profile, goals and strategies to assess which types of investments may be appropriate for you and must act in your best interest.

There are generally no set account minimums or investment amount applicable to brokerage accounts. We do not exercise discretionary investment authority in your brokerage account or monitor your brokerage account investments for you. This means that you are responsible for reviewing your account and investments to make sure your investment mix is appropriate for you and for deciding whether to follow our investment recommendations. As an independent firm, we do not offer any proprietary products and our investment offerings are only limited with respect to the products or types of investments permitted by law or regulation and provided through agreements with certain sponsors.

Additional detailed information about our brokerage services may be obtained on our website at www.moorscabot.com.

Investment Advisory Services

We provide investment advisory services through a Portfolio Management Program (PMP) wrap account on either a discretionary or a non-discretionary basis. We also offer “advice only” services for a fee on assets that may be held at custodians other than our clearing firm, RBC. For advice only service, we will review the assets and may make recommendations to the client, who has the sole responsibility to implement any buy, sell or reallocation recommendation. In addition, we offer fee-based financial planning services that may include evaluation and analysis related to estate, investment, education, risk, and retirement planning. On a limited basis, clients may receive consultation on specific areas of financial, investment, or non-securities concerns where the fee is often negotiated.

Financial Advisors provide continual and regular investment advice or investment supervisory services to clients, communicate regularly with clients, and provide ongoing monitoring of advisory accounts in accordance with the terms of the advisory agreement. PMP wrap accounts generally involves a $50,000 account minimum, unless otherwise agreed to with the client. M&C provides investment advice on all types of securities and does not offer any proprietary products. Discretionary authority is documented in a written advisory agreement. For non-discretionary accounts, we are required to obtain verbal consent prior to making transactions in the account and the investor makes the ultimate decision regarding the purchase or sale of investments.

Additional information about our investment advisory services and programs is detailed further in Part 2A of Form ADV at https://www.moorscabot.com.

What fees will I pay?

Please understand that fees are different for Brokerage and Advisory services. You will pay commissions, fees, or other costs whether you make or lose money on your investments. Commissions, Fees, or other costs will reduce any amount of money you make on your investments over time. Please make sure you understand what fees and costs you are paying.

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Brokerage Services Fees
Compensation in brokerage accounts is generally either direct or indirect. Direct compensation is taken directly from the affected account. Indirect compensation (e.g. mutual fund sales charge) is compensation paid other than directly from the account and may impact the value of the investment(s) in your account. Commissions are charged when you buy or sell equities and fixed-income investments when M&C acts as agent or broker.

The standard commission charges do not reflect any discounts offered or agreed upon between you and your Investment Professional. Retail investors will be charged more often when there are more trades in a brokerage account, creating an incentive to encourage more frequent trading. Markups and markdowns may be applied when you buy or sell securities where we act as principal by buying and selling from our own inventory, primarily for bonds. You may be charged Sales loads (i.e. sales charges), commissions or concessions derived from the offering and sale of various managed investments such as mutual funds, unit investment trusts, insurance and annuities. In some instances, other transaction fees (i.e. postage and handling costs) on the purchase or sale of certain equity and fixed-income products in brokerage accounts may be charged. For certain eligible accounts, interest on margin balances is charged. Miscellaneous costs may include fees for IRAs, wire transfers, returned checks, transfer on death services, account termination, account transfers, physical certificates, etc.

Our standard commission and fee schedule is provided upon the opening of an account and available upon request.

Investment Advisory Services
M&C charges asset based fees according to a standard fee schedule in which the fee percentage declines as asset size increases. Asset based fees are negotiable on a case-by-case basis and will generally not exceed 2.5%. Fees are billed on a quarterly basis in advance, and deducted from the account. The advisory account will be credited any 12b-1 fees received from mutual fund assets. In lieu of asset-based fees, M&C offers the same service on a transactional basis. In this case, commissions will vary by security and based on standard commission rates. Under this arrangement, total costs may higher or lower that the asset-based fee instances depending on the negotiated rate, investment strategy, or portfolio turnover. M&C may also charge fixed fees or hourly fees for financial Planning, consulting, or other related advisory services. We do not charge performance based or incentive fees

Asset based fees in our wrap program include all transaction costs and fees. Please note that an investment adviser charging an asset-based fee involves a potential conflict of interest. The greater the assets in an advisory account, the more fees will be paid. Accordingly, M&C may have an incentive to encourage investors to increase the assets in their account. Our fees may be higher or lower than fees charged by other investment advisers or broker-dealers.

Additional information about advisory fees is detailed further in Part 2A of Form ADV at https://www.moorscabot.com.

Other Fees and Costs

All fees you pay to us are separate and distinct from the fees and expenses charged by mutual funds, exchange traded funds (ETFs), and publicly traded real estate investment trusts (REITS) (and similar securities) to their shareholders. These fees and expenses are listed in each fund's prospectus. Other fund costs and expenses may include 12b-1 or shareholder servicing fees that include the following: management fees, fund expenses, administrative fees, and distribution costs. Other common costs may be charged by the custodian. Some examples of these are deferred sales charges, exchange fees, IRA account fees, wire fees, odd lot differentials, account transfer fees, etc.

What are your legal obligations to me when providing recommendations as my broker-dealer or when acting as my investment adviser? How else does the firm make money and what conflicts of interest do you have?

Standard of Conduct

When we provide you with a recommendation as your broker-dealer or act as your investment adviser, we must act in your best interest and will not put our interest ahead of yours. At the same time, our compensation may create some potential conflicts of interest. When we serve as your investment adviser, we follow a Code of Ethics to ensure we meet our required fiduciary

Conversation corner
Questions you might wish to ask when considering our services:

- **How might your conflicts of interest affect me, and how will you address them?**

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obligations and keep your interests first at all times. You should understand and ask us about these conflicts because they can affect the recommendations and investment advice we provide you. Here are some examples to help you understand what this means.

Examples of Ways We Make Money and Conflicts of Interest

Depending on what you buy or sell in a brokerage account, you may pay commissions, markups or markdowns, sales charges and/or administrative fees. In addition, you may pay transaction-based fees on the purchase or sale of certain equity and fixed-income products. The investments within your account also may have ongoing expenses such as distribution and/or service fees (12b-1 fees), trail and renewal commissions that reduce your investment returns. M&C receives a portion of these payments.

In an advisory account, the fee is based on the market value of all assets held in your account and is assessed quarterly based on the tiered fee rate schedule. As the value of the assets in your account increases or decreases, you are charged according to the tiered fee rate schedule.

While we don't offer proprietary products, we may receive revenue from unaffiliated third-parties when making a recommendation to buy or sell certain investments. We also benefit financially from cash balances in the bank deposit sweep program which is determined by the "spread" between the interest paid on deposit and the interest and other income earned on loans, investments and other assets.

Wherever compensation is received by M&C, there exists a financial incentive and a potential conflict interest that can affect retail investors. For additional information about potential conflicts of interest, please see www.moorscabot.com.

How do your financial professionals make money?

Advisors receive a portion of commissions, markups/markdowns, and sales charges. The amount differs depending on the investment and the amount of the transaction. The payout level may also vary based on the financial professional's years of experience, the location of the branch, the type and amount of the investment, and discounts. In advisory accounts, compensation is a portion of the advisory fee which are based on the value of the account.

Depending on the type of investment account (brokerage or advisory), there exists a financial incentive to either trade more frequently and/or increase the account asset size.

For more information about fees and commissions, please see www.moorscabot.com.

Conversation corner

Questions you might wish to ask when considering our services

- **As a financial professional, do you have any disciplinary history? For what type of conduct?**
- **Who is my primary contact person? Is he or she a representative of an investment adviser or a broker-dealer? Whom can I talk to if I have concerns about how this person is treating me?**

Do you or your financial professionals have legal or disciplinary history?

Yes. All disciplinary events are disclosed to the public as required. More Information is provided in:

- Form ADV (Item 11 of Part 1A or Item 9 of Part 2A).
- Form BD (Items 11 A–K) (except to the extent such information is not released to BrokerCheck, pursuant to FINRA Rule 8312).
- Items 14 A–M on Form U4 (Uniform Application for Securities Industry Registration or Transfer), or in Items 7A or 7C–F of Form U5 (Uniform Termination Notice for Securities Industry Registration), or on Form U6 (Uniform Disciplinary Action Reporting Form) (except to the extent such information is not released to BrokerCheck, pursuant to FINRA Rule 8312).

https://brokercheck.finra.org/ is a free tool to research the background and experience of financial brokers, advisers and firms.

Where can I find additional information?

You can always ask your financial advisor for more information and request a copy of this relationship summary at 800-451-0500 and/or compliancemailbox@moorscabot.com

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http://www.advisorinfo.sec.com
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