

What Do Bond Ratings Mean?

Bond ratings gauge a bond issuer's financial ability to repay its promised principal and interest payments. Ratings are based on an analysis of the issuer's financial condition and creditworthiness. In essence, the higher the rating, the more likely it is that a bondholder will receive his or her principal again when the bond matures.

Credit rating agencies assess the risks of certain bonds, issuing grades that reflect the issuer's ability to meet the promised principal and interest payments. The best-known independent rating services are Standard & Poor's, Moody's Investors Service, and Fitch Ratings. The following are the rating scales for each agency, ranging from the highest quality to the lowest (and possibly default). They are rated in descending alphabetic order from A to D.

Standard & Poor's: AAA, AA+, AA, AA-, A+, A, A-, BBB+, BBB, BBB-, BB+, BB, BB-, B+, B, B-, CCC+, CCC, CCC-, D

Moody's: Aaa, Aa1, Aa2, Aa3, A1, A2, A3, Baa1, Baa2, Baa3, Ba1, Ba2, Ba3, B1, B2, B3, Caa1, Caa2, Caa3, Ca, C

Fitch: AAA, AA+, AA, AA-, A+, A, A-, BBB+, BBB, BBB-, BB+, BB, BB-, B+, B, B-, CCC, DDD, DD, D

A credit rating is not a recommendation to purchase a particular bond. Bonds with higher ratings typically have a lower yield. Bonds with lower ratings generally offer higher yields, but the risk that the issuer will default is greater. You should carefully weigh the risks of investing in these bonds.

In addition to credit risks, bonds are subject to interest rate and inflation risks, and they have different maturities. The principal value of bonds fluctuates with changes in market conditions. If sold prior to maturity, a bond may be worth more or less than its original value.

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