Difference Between Secured and Unsecured Bond

www.differencebetween.com

Key Difference - Secured vs Unsecured Bond

The key difference between secured and unsecured bond is that **a secured bond is a type of bond that is secured by pledging a specific asset as collateral by the issuer of the bond** whereas **an unsecured bond is a type of bond that is not secured against collateral.** A bond is a debt instrument issued by corporates or governments to investors in order to obtain funds for projects and expansion purpose. They are issued at a par value (face value of the bond) with an interest rate and a maturity period. Secured and unsecured bonds are two popular types of bonds among many.

What is a Secured Bond?

A secured bond is a type of bond that is secured by pledging a specific asset as collateral by the issuer of the bond. In the case of default due to nonpayment, the issuer has to pass the ownership of the asset onto the bondholder. Secured bonds can also be secured with the income stream that results from the project that the bond issue was used to finance. Mortgage bonds and equipment trust certificates are two forms of widely used secured bonds.

Mortgage Bond

A mortgage bond is a bond secured by a mortgage or pool of mortgages. These bonds are typically backed by real estate holdings by companies who own a significant amount of property, where a legal claim gives the bondholder the right to possess the mortgaged asset in case the company fails to make the payments. Mortgage bonds are the most common types of secured bonds.

Equipment Trust Certificate

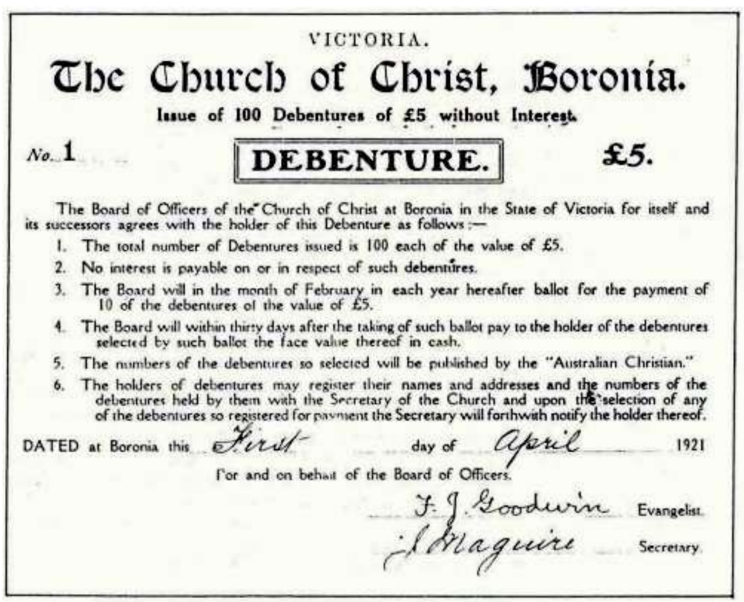
An equipment trust certificate is financed by an asset that is easily transported or sold. The title to the equipment is held by a trust and investors can purchase trust certificates as a means of providing funds to a specific company. The capital repayments and the interest are paid by the company to the trust who in turn make the payment to the investors. When the debt payments are completed, ownership of the asset is transferred back to the company by the trust.

What is an Unsecured Bond?

Also referred to as **debentures**, an unsecured bond is a type of bond that is not secured against collateral. For a company to issue an unsecured bond with the intention of obtaining finance from investors, it should be a reputed company with a good credit standing. Credit rating is offered by an independent organization, usually a credit rating agency after assessing the ability of the company to meet financial obligations.

In an unsecured bond, the bondholder cannot recover the value of the investment if the bond issuer defaults. Therefore these are highly risky instruments compared to secured bonds due to the absence of collateral and are supported by high-interest payments. The interest rate offered depends significantly on the financial stability and trustworthiness of the company or the governmental organization.

The possibility of default and the inherent risk in government unsecured bonds is very low compared to corporate bonds. When governments need additional funds to repay bonds, taxes are increased to gain access to increased funds. Even in the rare circumstance that a governmental body declares liquidation, bonds are usually covered by other governmental bodies. On the other hand, the default risk of corporate unsecured bonds are higher and if the company is to liquidate, the bond holders receive at least a portion of their investment before shareholders are settled.



VICTORIA.

The Church of Christ, Boronia.

Issue of 100 Debentures of £5 without Interest.

No. 1 **DEBENTURE.** £5.

The Board of Officers of the Church of Christ at Boronia in the State of Victoria for itself and its successors agrees with the holder of this Debenture as follows :—

1. The total number of Debentures issued is 100 each of the value of £5.
2. No interest is payable on or in respect of such debentures.
3. The Board will in the month of February in each year hereafter ballot for the payment of 10 of the debentures of the value of £5.
4. The Board will within thirty days after the taking of such ballot pay to the holder of the debentures selected by such ballot the face value thereof in cash.
5. The numbers of the debentures so selected will be published by the "Australian Christian."
6. The holders of debentures may register their names and addresses and the numbers of the debentures held by them with the Secretary of the Church and upon the selection of any of the debentures so registered for payment the Secretary will forthwith notify the holder thereof.

DATED at Boronia this First day of April 1921

For and on behalf of the Board of Officers.

F. J. Goodwin Evangelist.

J. Maguire Secretary.

Figure 01: Unsecured Bond

What is the difference between Secured and Unsecured Bond?

Secured vs Unsecured Bond	
Secured bond is a type of bond that is secured by pledging a specific asset as collateral by the issuer of the bond.	Unsecured bond is a type of bond that is not secured against collateral.
Interest Rate	
The interest rate applicable for a secured bond is lower than the rate applicable for an unsecured bond.	Unsecured bonds are subjected to higher interest rates due to the inherent risk.
Default Risk	
Default risk of a secured bond is generally low since nonpayment result in a loss of the asset to the bond issuer.	Default risk of a government unsecured bond is generally low, so is the default risk of an unsecured bond issued by a corporate with a good credit rating.

Summary - Secured vs Unsecured Bond

The difference between secured and unsecured bond mainly depends on whether a collateral is involved or not. Their characteristics also vary with regard to the interest rates and the possibility of default. A secured bond is a suitable investment for investors who have a less tolerance for risks. Return and risk on an unsecured bond can vary significantly, from low-risk and low return to high-risk and high-return.

References
1. "Secured Bond." Investopedia. N.p., 12 May 2005. Web. Available here. 06 June 2017.
2. "Unsecured Bonds." My Accounting Course. N.p., n.d. Web. Available here. 06 June 2017.
3. "Mortgage Bond." Investing Answers Building and Protecting Your Wealth through Education Publisher of The Next Banks That Could Fail. N.p., n.d. Web. Available here. 06 June 2017.

Image Courtesy:
1. "Debenture" By Appu suvarna - Own work (CC BY-SA 4.0) via Commons Wikimedia

How to Cite this Article?

APA: Difference Between Secured and Unsecured Bond. (2017, June 10). Retrieved (date), from http://www.differencebetween.com/ difference-between-secured-and-vs-unsecured-bond

MLA:"Difference Between Secured and Unsecured Bond." Difference Between.Com. 10 June 2017. Web.

Chicago:"Difference Between Secured and Unsecured Bond". Difference Between.Com. http://www.differencebetween.com/ difference-between-secured-and-vs-unsecured-bond / (accessed [date]).