IN BOND INVESTING

What is Effective Maturity?

https://www.perplexity.ai/search/In-investing-what-04KhbJH.S8qOlreTNZZO4g

Effective Maturity is a measure that determine the actual duration or length of time a fixed-income security (bond) remains outstanding factoring in possible:

- prepayments,
- embedded options (e.g., call or put options),
- and other features that may impact the final return.13

It represents the true period over which fixed-income security generates its ultimate cash flows and return, which may differ from the stated maturity date.1

For bonds with call, put, or prepayment features, the effective maturity incorporates the effect of those optional maturity dates mathematically.3 It accounts for factors that can shorten or extend the holding period, such as borrowers prepaying loans in mortgage-backed securities or issuers exercising call options to redeem bonds early.14

What is Effective Duration?

https://www.perplexity.ai/search/In-investing-what-3Rk_xE3ZRQ6QarkKIXs3VQ

Effective Duration is a measure of a bond or bond portfolio's sensitivity to changes in interest rates.

It considers the impact of changes in interest rates will have on a bond's cash flows.

Effective duration is particularly useful for bonds with embedded options, such as callable or mortgage-backed securities, where expected cash flows fluctuate as interest rates change. It provides a more accurate price sensitivity measure than traditional duration measures that assume fixed cash flows.23

Key Points About Effective Duration

It estimates the percentage change in a bond's price for a 1% change in interest rates.2
Bonds with higher effective duration have greater price sensitivity to interest rate changes, and thus, higher interest rate risk.12

It allows investors to compare interest rate risk across different bond investments and manage portfolio risk exposures.2

FROM ANOTHER SOURCE - the same info different description

What is the difference between Duration & Maturity?

https://www.financestrategists.com/wealth-management/bonds/duration-vs-maturity/

- Duration measures a bond's price sensitivity to changes in interest rates
- Maturity is the length of time until its principal is repaid.

The two concepts are closely related, but they are not interchangeable.

What Is Duration?

Duration measures a bond's sensitivity to changes in interest rates. It estimates how much a bond's price will change for a given change in interest rates.

Duration is typically expressed in years. The higher the duration, the more sensitive the bond's price is to interest rate changes, and vice versa.

Relationship Between Duration and Interest Rates

- The relationship between duration and interest rates is inverse.
- That is, when interest rates rise, bond prices fall,
- and when interest rates fall, bond prices rise.
- The magnitude of the price change depends on the bond's duration.
- Bonds with longer durations are more sensitive to interest rate changes and will experience larger price changes than bonds with shorter durations.

Uses of Duration in Finance

Duration helps investors and analysts estimate how much a bond's price will change in response to changes in interest rates.

What Is Maturity?

Maturity is the length of time until a bond's principal is repaid. It is the date on which the bond issuer must repay the bondholder the face value of the bond.

Maturity is expressed in years and is essential in determining the bond's price.

Types of Maturity

- Short-term maturity - Generally, a period of less than one year,
- Medium-term maturity has a duration of one to ten years.
- Long-term maturity typically has a duration of more than 10 years.