SSNIT INVESTMENTS SERIES

SIXTH EDITION

INTRODUCTION

The sixth edition of the SSNIT Investments Series opens the discussion on the Fixed Income Portfolio. The portfolio is managed by the Fixed Income & Financial Advisory Services Department (FIFAS) under the Investment & Development Division (IDD) and Treasury Department under the Finance Division. FIFAS handles the debt/lending arrangements of the Trust to third parties and typically undertakes medium and long-term fixed income transactions with tenures exceeding one year, while the short-term fixed income transactions are handled by the Treasury Department. The Trust's fixed income portfolio comprises Bonds & Notes, Term Loans, Students' Loans and Treasury placements. These investments provide a return in the form of periodic coupon/interest payments. The Bonds sub-asset class will be the focus in this edition.

OVERVIEW OF BONDS

Bonds are issued by borrowers with the promise to make periodic payments (coupons) and return the principal or face value of the amount borrowed at maturity. Investors, like SSNIT, who subscribe to bond issues typically lend money to the Bond Issuer. Issuers of bonds in our investment environment (Ghana) are corporate entities, District & Municipal Assemblies and the Government.

Some key features of Bonds:

- Face Value/Notional Amount – The principal amount or value of a bond at the time of issue. It is also the amount that the bond holder expects to receive at maturity. Coupon is computed based on the face value (principal amount).

  Bonds could be issued at a premium, at par or at a discount.

  For example, a bond with a face value of GH¢100, if issued at GH¢100, is said to be issued at par. If it is issued at, say, GH¢95, it will be said to have been issued at a discount and conversely, if issued for, say, GH¢110, at a premium.

- Maturity Date – This is the set date at which the principal amount is repaid to the Lender. In Ghana, maturity dates range from 1 to 20 years. Based on the maturity period, bonds are referred to as bills (when issued in days such as 91-day, 182-day), notes (1-2 years), medium term bonds (3-7 years) or long-term bonds (7+ years).

- Coupon/Yield – Is the interest rate the Issuer agrees to pay the bond holder. This is usually paid quarterly or semi-annually but can vary per the terms of the bond issue. Bonds that do not pay coupon otherwise called Zero Coupon Bonds, are bonds priced at a discount from the face value but the bond holder receives the full face value of the bond at maturity. The difference between the amount paid for the bond and its face value received at maturity represents the interest from the bond.

  Coupons may be either fixed, providing a fixed stream of regular interest payments over the life of the bond, or floating, thus providing varied interest amounts per period on re-adjustment of the underlying rate.

  To minimize the risk of interest rate fluctuations, coupon rates on Bonds are reset at the commencement of each cycle (i.e. quarterly, semi-annually or annually) to protect both the bond holder and issuer. Floating interest rate may be linked to inflation, exchange rate or other interest rates.

- Rating – It is the evaluation of the riskiness of the bond issuer.
- Call feature – This feature allows the Issuer to redeem the bond before its maturity date and pay-off the lender.
- Tradable feature – Bonds could be tradable or non-tradable.

  After issuance in the primary market, some categories of bonds may be listed on an Exchange for secondary trading among investors. However, most secondary trades are organized 'over-the-counter'. Over-the-counter refers to the trading of financial securities through dealer networks as opposed to a centralized Exchange. In other words, it is a decentralized market without a central physical location where market participants' trade with one another through various communication modes such as the telephone, email and other proprietary electronic trading systems.

  Non-tradable bonds however, must be held by the bond holder until maturity to redeem.

Bond Risk

Bonds like other financial instruments are associated with some level of uncertainties called risks. Mostly, a higher compensation is demanded for riskier bonds and vice versa. There are several sources of risks associated with holding bonds. These include:

- Interest Rate Risk – Bond prices usually tend to have an inverse relationship with interest rates (that is, when interest rates fall, bond prices rise, and when interest rates rise, bond prices fall). Interest rate risk is the risk that changes in interest rate may reduce (or increase) the market value of a bond.
- Default Risk – Issuers of bonds could default on their obligation to make principal and coupon payments if they are unable to raise the needed cash for the bond obligation. Bonds issued by governments are usually considered risk-free, but all other bonds contain default risk.
- Inflation Risk – When bond repayments are fixed over the life of the bond, the real values of the payments fall if there is increase in the general price levels over the holding period.
- Liquidity (Marketability) Risk – The inability of a bond to have a ready market creates a liquidity risk for the holder who might want to sell the bond.

Bonds however, are considered less risky compared to other investment securities like equities or loans. An issuer company undergoing administration in the event of liquidation will pay bond holders first before any other investment security is considered.

SSNIT BOND PORTFOLIO

The Trust has participated in a number of bond issues over the years, contributing to the cause of both corporate entities and the Government. The current Bond portfolio has ten (10) bonds made up of seven (7) Corporate and three (3) Government Bonds. The Trust is however, yet to participate in Municipal bond issues. *Due to confidentiality clauses in the Agreements, we are unable to disclose the details of the bonds in the Investments Series*.

The total Bond portfolio of GH¢1,175 million as at September 2017 constituted 12.8% of the Trust's total investment portfolio and 36.0% of the fixed income portfolio. Out of the total, GH¢1,055 million (90%) were in Government bonds whilst the remaining GH¢120 million (10%) were in Corporate bonds.

Performance of SSNIT Bond Portfolio

The performances of bonds in the portfolio are assessed by comparing the actual returns on the bonds to the benchmark returns. The benchmark returns are specified in the Trust's asset allocation policy.

Extract from the Trust's Asset Allocation Policy

Investment Asset	Benchmark Return
Corporate Bonds	3yr Fixed Rate + Margin
Government Bonds	3yr Fixed Rate + Margin
Municipal Bonds	3yr Fixed Rate + Margin

Over the past five years (i.e. 2012 - 2016), the Bond portfolio has contributed about 24% on average, to the annual gross investment income of the Trust.