Zuger Kantonalbank

Fixed income assets (e.g. bonds, time desposits)

Asset class fact sheet

This document informs you about the characteristics, advantages and risks of direct investments in fixed income assets and is designed to help you make your investment decisions. If you have any questions, please do not hesitate to contact your client adviser at any time.

Fixed income assets is the generic term for all forms of interest-bearing or generating debt instruments (securities), such as for example debentures, bonds, mortgage notes and bonds, that certificate claims. As a rule, these are used for short- to long-term external financing or capital investment purposes.

Fixed income assets can be issued by companies, banks or by the public sector (e.g. federal government, municipality) (issuers). The normal maturity can be up to 30 years. As a rule, a debt instrument certificates the right to repayment of the investment sum (nominal value) and any possible interest payments (coupons). Repayment is performed at the end of the maturity.

Typical fixed income assets

Time deposits, Public notes issued by banks, classic bonds, variable-rate bonds, mortgage notes, zero-coupon bonds (zero bonds), terminable bonds and warrant bonds (convertible bonds).

Principal characteristics of fixed income assets

- Nominal value – sum that is repayable to the investor on the due date.
- Coupon – periodically due interest sum (as percentage of the nominal value).
- Maturity date – the final bond payment deadline, on which the capital and the still-outstanding interest is due for payment.
- Provisions governing premature termination or partial repayment – right of the issuer to repay the bond in full before the due date.
- Securities provided by the issuer – promises of the issuer in the formal bond agreement to perform or to omit certain activities in order to provide the investor with additional security.

Bond ratings

The quality of a bond is based on the financial ability of the issuer to perform interest payments and to repay the nominal value in full upon maturity. The financial circumstances of the issuer is checked by credit rating agencies and is given a rating. A rating of this nature helps to assess the credit quality (creditworthiness) of a bond in comparison to other bonds.
Moody's and Standard & Poor's (S&P) are two major, independent, international credit rating agencies that assess the credit quality of bonds and give these ratings.

S&P	Moody's	Meaning of the ratings
AAA	Aaa	The ability of the debtor to fulfil their financial obligations is outstanding.
AA	Aa	The ability of the debtor to fulfil their financial obligations is very good.
A	A-1, A	The ability of the debtor to fulfil their financial obligations is good, but slightly vulnerable if the situation deteriorates.
BBB	Baa-1, Baa	The ability of the debtor to fulfil their financial obligations is reasonable, but vulnerable if the situation deteriorates.
BB	Ba	The debtor is not in great jeopardy in the short term. If the situation deteriorates, however, this would give rise to significant uncertainty factors.
B, CCC, CC, C	B, Caa, Ca	If the situation deteriorates, losses are likely or a default is highly likely.
D	C	Payment default in the event of financial obligations.

Benefits

Stability
Fixed income assets tend to be less volatile (fluctuation of financial market parameters) than equities and are therefore considered to be more conservative investments.

Fungibility
Fixed income assets are traded on an organised capital market (stock exchange) or OTC between financial institutions. If a counterparty can be found, they can be sold or bought before the due date. Prices are determined by the current interest situation as well as supply and demand.

Steady returns
In the case of fixed income bonds with coupons, coupon payments (in contrast to equity dividends) are continuously performed at regular intervals.

Risks

Potential loss
If an issuer fails to fulfil their payment obligations arising out of a bond, a partial or total loss of the investment capital is possible (further information is set out in the section "Credit risk").

Market risk
The investor bears the risk that fluctuations in interest could have a negative impact on the value of the fixed income asset during its term. The market value of a bond during its term may be below the redemption price upon maturity.

Credit risk
The investor bears the credit risk of the issuer, i.e. the risk of the insolvency of the debtor. This potentially means a partial or total loss of the invested capital.

Liquidity risk
In an illiquid market, investors are exposed to the risk that the bond could be held either to the end of its term, or may need to be sold before maturity at an unfavourable price.

Foreign exchange risk
The investor may be exposed to a foreign exchange risk if the bond is denominated in a currency other than the domestic currency of the investor.