Century
Bond

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What will you be doing in 2126? Absent major medical advances, time machines, and cryonic suspension chambers, most of us will not be doing much of anything. But this is the date at which the principal will be repaid on Alphabet’s new 100-year corporate bond. Alphabet is Google's parent company.

A 100-year corporate bond is rare, not least because long-dated bonds are normally only issued by governments. Most governments are expected to still be here in 100 years, but there is less confidence that companies will. One study showed that the average time a company spent in the S&P index was 20 years; not quite the same thing as ceasing to trade altogether, but it is still a telling statistic.

The last time a technology company issued such a long-dated bond was Motorola in 1997, the year Princess Diana called for a landmine ban, and Steve Jobs unveiled the first iPhone.

Sterling Bond
As well as its term, the second remarkable feature of the Alphabet bond is its currency of denomination. Usually, such bonds are issued in US Dollars. However this one was denominated in Sterling. In this case there was USD 20bn issued initially, followed by a further GBP 1bn. Although the Sterling portion was the notably smaller part of the package, it was noteworthy. Both bond offerings were very popular with investors, and several times oversubscribed.

Alphabet’s rationale
The rationale for issuing a bond that does not mature until the next century is straightforward from Alphabet’s perspective. By borrowing at a fixed rate for an extremely long period, the company locks in today’s financing costs while funding long term investments in areas such as artificial intelligence, data centres and Cloud infrastructure. Only companies with very strong balance sheets and durable business models can attract investors at such long maturities.

Pension scheme investment
Defined Benefit (DB) pension liabilities often stretch decades into the future, and long dated bonds can be valuable tools for matching assets to those obligations. A 100 year bond issued by a high quality corporate may therefore appeal to schemes seeking predictable, long-term cash flows. That said, investors must also accept pronounced sensitivity to interest rate movements and the uncertainty inherent in valuing a business over such an extended horizon: this is the credit risk associated with a company relative to “risk-free” government bonds.

Valuing the liabilities
Pension scheme actuaries make assumptions about the long-term expected rates of return on assets to put a current value on future benefit payments. Century bonds help provide some hard evidence where data are particularly scanty, particularly around discount rates and credit risk.

A key feature of long-dated bonds is their price sensitivity to small changes in interest rates. Consequently, it is important for pension scheme trustees to understand the potential risks with such an investment. Therefore, the results of stress-testing and scenario analysis will be particularly important when Trustees are seeking advice in this area.

Confidence in the future
Since its debut in February, the bond’s price has slipped a bit, but it is a welcome beacon of long-term confidence in uncertain times.