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ADDITIONAL INTEREST EARNINGS OF OASDI TRUST FUNDS RESULTING FROM CHANGED INTEREST RATE PROVIDED IN 1960 AMENDMENTS

by Marice C. Hart
Division of the Actuary

This note presents an analysis of interest earnings of the OASDI Trust Funds with regard to the effect of statutory changes in the basis of determining the interest rate for special issues. *In summary, the change made by the 1960 Amendments has benefited the trust funds by about \$62 million in fiscal years 1961-64.*

The 1960 Amendments provided that the rate for special issues would be based on the average market-yield rate, computed as of the end of the preceding month, for all marketable interest-bearing obligations not due or callable for at least 4 years. Comparison is made with the interest rate provided by the 1956 Amendments, which was based on the average coupon rate of securities issued for at least 5 years, and with the interest rate provided by the 1939 Amendments, which was based on the average coupon rate of all interest-bearing obligations. Table 1 shows the three interest rates, by months, from the effective date of the 1960 Amendments.

The special investments issued for the trust funds mature on June 30, and consist of one-year (or less) certificates, one- to five-year notes, and bonds with maturities up to 15 years. Generally, investments in notes and bonds are made only at the end of the fiscal year, on June 30. Special certificates are issued three times a month throughout the year. Investments are liquidated on the last day of the month to provide funds for benefit payments. Certificates are liquidated first, then notes and bonds in order of maturity date, with the lower interest rate issues redeemed first.

The pattern of investments in and redemptions of special issues has been studied during the

period October 1960 through June 1964. With respect to special certificates issued during a fiscal year and maturing on June 30 next, interest earnings are included in this study only for certificates held at least one full month; that is, interest on certificates issued in a month and liquidated on the last day of that month is excluded. Thus, the estimates of the added interest earnings on these certificates are understated, and the amount of gain shown represents a minimum. As to longer-term issues in notes and bonds, interest earnings are based on the actual period that the securities were held, with liquidation assumed to occur on the last day of the month.

Table 2 summarizes the holdings in special issues as of October 31, 1960, and at the end of each of the fiscal years 1961-64. Because both trust funds have been decreasing over much of this period, it has been necessary to liquidate notes and bonds during the year, and these liquidations have been largely in issues at 2½% and 2-5/8%. Receipts are high in the early part of the year, particularly in February and May, and thus funds are usually available for long-term investment on June 30. Most of the investments in the higher interest rate issues mature in 1975 or later, so that these issues will continue to be held while the lower interest rate issues with earlier maturity dates will be liquidated first. At present, no notes are held by either fund, while the bonds with the earliest maturity date are 2-5/8% 1967 bonds for the OASI Trust Fund and 2-5/8% 1970 bonds for the DI Trust Fund.

Table 3 shows the effect of the 1960 change, by fiscal years and by type of special issue. In

the first fiscal year, 1961, additional interest earnings were realized only on certificates. Investments on June 30, 1961, in notes and bonds at 3-3/4% that were held for the entire fiscal year 1962, resulted in substantial gains for that year. For the OASI Trust Fund, the entire investment was in bonds maturing in 1975 and 1976, while for the DI Trust Fund, a part of the investment was in 2-5 year notes, and the remainder was in bonds maturing annually from 1967 to 1976.

On June 30, 1962, most of the OASI funds available for investment were held in 1-year certificates, with a small amount in 2-year notes, which were liquidated during fiscal 1963. For the DI Trust Fund, the amount of 3-3/4% special issues maturing in each year from 1964 to 1976 was increased and bonds maturing in 1977 were added. During the year, nearly half of the notes issued June 30, 1961 for the DI Trust Fund were liquidated.

On June 30, 1963, the only long-term investment for both funds was in 3-7/8% bonds maturing June 30, 1978. During the year, liquidations in the OASI Trust Fund were in 2 1/2% and 2-5/8% bonds with maturity dates to June 30, 1966, while for the DI Trust Fund the remaining 3-3/4% notes issued on June 30, 1961-62, as well as 2 1/2% and 2-5/8% bonds, were liquidated.

On June 30, 1964, 4-1/8% bonds maturing June 30, 1979 were issued for both funds. At present, the OASI Trust Fund holds \$4.5 billion in 3-3/4%, 3-7/8%, and 4-1/8% bonds maturing 1975-1979, so that these investments will continue to be held, while 2-1/2% and 2-5/8% bonds with earlier maturities will be liquidated if necessary. However, the DI Trust Fund holds about \$20 million in 3-3/4% bonds maturing each year (beginning with 1970), and these bonds will be liquidated along with bonds at lower rates maturing at the same time. In fact, some \$60 million has been liquidated since June 30, 1964. Nonetheless, some \$700 million at rates of 3-3/4%, 3-7/8%, and 4-1/8% will be held during fiscal 1965.

As shown in Table 3, the additional interest earnings during the 4 fiscal years since the change was made have aggregated \$62 million, and for fiscal year 1965 are estimated to be more than \$30 million.

Table 4 makes a similar comparison using the interest rates under the 1939 Amendments. A slightly smaller gain is shown, due to the fact that the 1939 rate has equaled or exceeded the 1956 rate during all of the period except the 5 months April-August 1963.

Table 1

EFFECTIVE INTEREST RATES COMPARED WITH RATES UNDER PROVISIONS
OF 1956 AMENDMENTS AND 1939 AMENDMENTS

	<u>Period</u>	<u>Effective Rate</u>	<u>1956 Rate</u>	<u>1939 Rate</u>	
1960	October	3.625%	2.625%	3.125%	
	November	3.750	2.750	3.125	
	December	4.000	2.750	3.125	
1961	January	3.625	2.750	3.125	
	February	3.750	2.750	3.000	
	March	3.625	2.750	3.000	
	April	3.750	2.875	3.000	
	May	3.625	2.875	3.000	
	June	3.750	2.875	3.000	
	July-August	3.875	2.875	3.000	
	September	4.000	2.875	3.000	
	October-November	3.875	2.875	3.000	
	December	4.000	3.000	3.000	
	1962	January-February	4.000	3.000	3.125
		March	3.875	3.000	3.125
April		3.750	3.000	3.125	
May-June		3.750	3.125	3.125	
July		3.875	3.125	3.125	
August		4.000	3.125	3.125	
September		4.000	3.125	3.250	
October		3.875	3.125	3.250	
November		3.750	3.125	3.250	
December		3.750	3.250	3.250	
1963		January-February	3.750	3.250	3.250
	March	3.875	3.250	3.250	
	April-August	3.875	3.375	3.250	
	September-October	4.000	3.375	3.375	
	November	4.125	3.375	3.375	
	December	4.000	3.375	3.375	
1964	January	4.125	3.375	3.375	
	February-March	4.125	3.500	3.500	
	April	4.250	3.500	3.500	
	May-June	4.125	3.500	3.500	

Table 2

INVESTMENTS IN SPECIAL ISSUES
(in millions)

Type of Investment	Oct. 31 1960	June 30			
		1961	1962	1963	1964
OASI Trust Fund					
Total	\$15,816	\$16,200	\$15,074	\$14,221	\$14,799
Certificates	167	441	1,080	—	—
Notes	1,934	1,387	257	—	598
Bonds	13,715	14,372	13,737	14,221	14,201
2-1/2%	4,825	4,560	3,925	2,671	1,324
2-5/8%	8,890	8,572	8,572	8,572	8,397
3-3/4%	—	1,240	1,240	1,240	1,240
3-7/8%	—	—	—	1,738	1,738
4-1/8%	—	—	—	—	1,502
DI Trust Fund					
Total	\$ 2,092	\$ 2,299	\$ 2,304	\$ 2,165	\$ 1,903
Certificates	232	34	1	6	—
Notes	386	464	336	84	1
Bonds	1,475	1,802	1,967	2,076	1,901
2-1/2%	188	188	188	142	30
2-5/8%	1,287	1,287	1,287	1,287	1,092
3-3/4%	—	327	493	493	493
3-7/8%	—	—	—	154	154
4-1/8%	—	—	—	—	133

Table 3

ADDITIONAL INTEREST EARNINGS, EFFECTIVE RATE OVER
RATE PROVIDED BY 1956 AMENDMENTS
(in thousands)

<u>Fiscal Year</u>	<u>Certificates</u>	<u>Notes</u>	<u>Bonds</u>	<u>Total</u>
		OASI Trust Fund		
1961	\$1,227	-	-	\$ 1,227
1962	1,621	-	\$10,851	12,472
1963	1,148	\$ 324	10,851	12,323
1964	1,099	-	19,543	20,642
Total	5,095	324	41,245	46,664
		DI Trust Fund		
1961	\$1,447	-	-	\$ 1,447
1962	585	\$ 679	\$2,859	4,123
1963	229	570	3,895	4,694
1964	51	189	4,663	4,903
Total	2,312	1,438	11,417	15,167

Table 4

ADDITIONAL INTEREST EARNINGS, EFFECTIVE RATE OVER
 RATE PROVIDED BY 1939 AMENDMENTS
 (in thousands)

<u>Fiscal Year</u>	<u>Certificates</u>	<u>Notes</u>	<u>Bonds</u>	<u>Total</u>
		OASI Trust Fund		
1961	\$1,032	-	-	\$ 1,032
1962	1,502	-	\$ 9,301	10,803
1963	1,329	\$ 324	9,301	10,954
1964	1,099	-	20,166	21,265
Total	4,962	324	38,768	44,054
		DI Trust Fund		
1961	\$1,016	-	-	\$ 1,016
1962	521	\$ 582	\$ 2,451	3,554
1963	240	494	3,487	4,221
1964	51	164	4,447	4,662
Total	\$1,828	\$1,240	\$10,385	\$13,453