



OUR REF: FMD/DIR/GEN/CIR/03/005

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TO ALL DEPOSIT MONEY BANKS AND DISCOUNT HOUSES

**GUIDELINES FOR THE CONDUCT OF REPURCHASE TRANSACTIONS
UNDER CBN STANDING FACILITIES**

I. Introduction

1. The CBN offers to enter repurchase transactions (repos) under its Standing Lending Facility (SLF) and Term Repurchase Facility (TRF). The objectives of these facilities are to provide Naira liquidity to eligible institutions that are unable to access funds on the inter-bank market and to set an upper limit on rates. The rates on the facilities are set at margins above expected market rates so as to provide sufficient incentive for banks to look first to the interbank market before seeking recourse to the CBN for funds.
2. These guidelines contain the terms and conditions for the operation of the SLF and the TRF and should be read in conjunction with the Nigerian Master Repurchase Agreement (NMRA). All references to sections in these guidelines are references to sections in the NMRA.
3. The NMRA is the legal document that governs all repos between the two parties that have signed it. The legal nature of a repo involves an agreement to sell securities at an agreed price, and to buy them back at a future date at an agreed price. Important aspects of the NMRA are contained in this guideline but counterparties must ensure they are fully conversant with all aspects of the NMRA.

II. Eligibility

4. The SLF and TRF are available only to banks and discount houses that have executed the NMRA with the CBN. All such transactions will be conducted under the NMRA signed between the counterparty and the CBN.

III. Duration, Pricing and Transaction Amounts

5. ***The Standing Lending Facility is an overnight facility.*** It is available on all banking days between the hours of 2pm and 3.30pm. Settlement is for same day value. The SLF rate is set by the Monetary Policy Committee of the CBN and is published on the CBN website (www.cbn.gov.ng). It is the applicable '*Pricing Rate*' pursuant to section 2 of the NMRA.

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6. ***The Term Repurchase Facility is a term facility.*** It is available on all banking days between the hours of 9am and 3.30pm. Term Repos can be transacted with the CBN for periods and at rates as published on the CBN website. The Term Repo Rate is the applicable 'Pricing Rate' pursuant to section 2 of the NMRA.
7. Transactions under these facilities can be conducted in amounts (based on the face values) of a minimum of N100 million and in multiples of N1 million thereafter.

IV. Other Terms and Conditions of CBN Repo Transactions

Purchase and Repurchase Prices

8. ***The Purchase Price*** is the price at which the *Purchased Securities* are to be transferred from Seller (borrower) to Buyer (lender) on the *Purchase Date*. The price will be calculated using appropriate market yields and after applying the appropriate *Margin Ratio* (detailed below).
9. ***The Repurchase Price*** is the price at which the *Purchased Securities* are to be transferred from Buyer to Seller on the *Repurchase Date*. It is calculated using a money market formula with the applicable rate being either the rate as applied to the SLF (in the case of an SLF transaction) or the relevant Term Repo Rate (in the case of a TRF transaction). In the terminology of the NMRA, the applicable interest rate is defined as the *Pricing Rate*.

$$\text{Repurchase Price} = \text{Purchase Price} + (\text{Purchase Price} \times \text{Pricing Rate} \times \text{days} / 365)$$

Purchased Securities

10. ***Purchased Securities*** are the securities that the seller (borrower) must deliver to the buyer (lender) on the *Purchase Date*. The CBN will accept the following securities under the facilities covered in these guidelines;
 - Nigerian Treasury Bills (NTBs)
 - Federal Government of Nigeria Bonds
 - CBN Bills
 - Asset Management Corporation of Nigeria (AMCON) Bonds
11. The maturity dates of all securities to be used must be at least three business days after the *Repurchase Date* of the transaction.

Margin Ratio

12. The *Margin Ratio* defined in section 2(y), is the '*Market Value of the Purchased Securities* at the time the transaction was entered into divided by the *Purchase Price*'. The CBN will apply a *Margin Ratio* to compensate for the risk that the value of securities could fall during the period of the repo. The longer the duration of the

securities, the higher the price volatility and therefore, the higher the risk that the value of the securities could fall during the period of the transaction.

13. **For securities with a term-to-maturity of five years or less the *Margin Ratio* will be 1.05, and for securities of greater than five years, the *Margin Ratio* will be 1.10.** Where there is a combination of securities provided (i.e. some shorter than five years and some longer than five years), the *Margin Ratio* will be a weighted-average of the securities provided.
14. In recognition of the fall in price of a bond after the coupon is due together with the requirement for the buyer to transfer the coupon to the seller, where a bond provided has an *Income Payment Date* that falls within the period of the repo, then the applicable *Margin Ratio* for such transaction, will be increased by one half of the coupon rate applicable to the bond. This approach reduces the need for the seller to make a *Margin Transfer* immediately the *Income Payment Date* has passed.

Example

15. An FGN bond with a semi-annual coupon of 10.50 percent maturing 18 March 2014 (i.e. less than three years to maturity), pays 5.25 percent coupons (i.e. 10.50/2) on 18 March and 18 September each year. The registered owner of the bond at the close of business on the day preceding the coupon payment date (i.e. 17 March and 17 September) receives the coupon. That is, where a bond trade is settled on the coupon date, then the seller receives the coupon.
16. If this bond is used in a repo with a *Purchase Date* before 18 September 2011 and a *Repurchase Date* after 18 September 2011, then the required *Margin Ratio* would be 1.1025 (equaling 1.05 plus 0.0525 percent).

Market Value of Purchased Securities (MVPS)

17. The MVPS will be based on yields as obtained from generally recognized sources. Up-to-date secondary market yields will be obtained where possible or Financial Markets Dealers Association rates may also be used. Ultimately, the CBN will determine the yields applicable to each security.
18. The formula for calculating the price of each security is as follows:

Nigerian Treasury Bills and CBN Bills

$$\text{Settlement Price} = \text{FV} - (\text{FV} \times \text{R} \times \text{Days} / 365)$$

Where: FV = the face value
R = the applicable discount rate
Days = are the day to maturity

Note that in a leap year the base is 366 and not 365.



Federal Government of Nigeria Bonds

Settlement Price =

$$\text{FV} \left\{ \frac{\frac{1}{(1+i)^n} + r \left[c + \frac{1 - \frac{1}{(1+i)^n}}{i} \right]}{(1+i)^{a/b}} \right\}$$

- FV = the face value
- r = the annual coupon divided by two hundred (i.e. the semi-annual coupon interest rate (%))
- i = the yield divided by two hundred
- c = if the settlement date is the coupon payment date 'c' has the value of 0, otherwise it has the value of 1.
- n = the number of full half years between the next coupon payment date and the maturity date
- a = the number of days from the settlement date to the next coupon payment date
- b = the number of days in the half year ending on the next coupon date

AMCON bonds

19. In the absence of secondary markets yields for AMCON bonds, the CBN will use the equivalent modified duration FGN Bond yield. A margin may be added if the CBN considers that the AMCON bond should trade at a premium (in yield) to FGN bonds.

Margin maintenance

20. Pursuant to the NMRA section 4, the CBN may request that a counterpart make a *Margin Transfer*. The CBN may make such a request in circumstances where the *MVPS* together with the market value of *Margin Transfers* (cash and securities transferred when meeting previous *Margin Transfers*) falls below 102 percent of the aggregate of the repurchase prices of all repo transactions undertaken between the CBN and the particular counterparty.

21. Under the NMRA section 4(g), a *Margin Transfer* can be made in either cash (*Cash Margin*) or in securities (*Margin Securities*). The CBN would prefer that all *Margin Transfers* be in the form of *Margin Securities*.

22. The value of the *Margin Transfer* (cash plus market value of *Margin Securities*) must be such that the ratio of, MVPS plus *Margin Transfer* divided by the aggregate of all *Repurchase Prices*, restores the *Margin Ratio* to the ratio applicable at the commencement of the repos [the ratio may be a weighted-average in circumstances where some securities have a term-to-maturity of less than five years and some have more than five years, as detailed in IV 3.]
23. When the CBN gives notice of a *Margin Transfer*, the counterparty must transfer to the CBN, the *Cash Margin* and/or *Margin Securities* by 3pm on the day after which the *Margin Transfer* was requested.
24. The CBN will not make *Margin Transfers* to counterparts in these transactions.

Treatment of coupon payments

25. Pursuant to the NMRA section 5, where a transaction extends over the Income Payment Date (i.e. coupon payment date), the buyer (i.e. CBN) shall credit the seller with income received on the same day that it receives the income.

Substitution of securities

26. The CBN will not allow substitution of securities under these facilities.

Penalty for non-repayment on the Repurchase Date

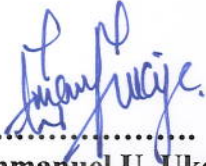
27. Notwithstanding the rights of a non-defaulting party in s10, where a counterparty does not repay the *Repurchase Price* on the *Repurchase Date* a new repo will have been deemed to have been entered into between the parties, where the *Repurchase Price* becomes the new *Purchase Price* and the new *Pricing Rate* is set at the rate applicable on the Standing Lending Facility plus five percentage points. The duration of the new repo will be overnight.

V. Initiation and Settlement

28. A counterparty wishing to access funds through these facilities must submit a request to Central Securities Clearing System Ltd (CSCS) for it to transfer securities from the account of the counterparty to the account of the CBN. The counterparty will provide to the Market Liquidity Management Office, Financial Markets Department, CBN Lagos, in line with current deadlines, a copy of the confirmation that the securities have been transferred. Once the CBN receives acknowledgement from CSCS that the collaterals have been moved, it will credit the counterparty's T24 account with the *Purchase Price* of the repo.



29. On the *Repurchase Date*, the counterparty's T24 account at the CBN will be debited with the *Repurchase Price* and the *Purchased Securities* will be transferred to the counterparty's account at the CSCS.



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