

FHLBoston

Dividends Make FHLB Boston Advances Pricing Even More Attractive

The Federal Home Loan Bank of Boston's board of directors recently declared a dividend equal to an annual yield of 4.99 percent, the approximate daily average three-month LIBOR yield for the fourth quarter of 2017 plus 350 basis points. The spread over LIBOR of 350 basis points represents an increase of 50 basis points from the most recent dividend payout formula.

Great News for Members

The increased cash dividend is certainly advantageous for members and reduces the "all-in" cost of doing business with the Bank.

All members are required to hold activity-based stock in proportion to outstanding advances ranging from a requirement of three percent for advances with an original maturity of one day to a requirement of four percent for advances with an original maturity of two days and longer. By viewing this stock purchase as a "cost" of borrowing, **the difference between the dividend rate and the cost to finance the stock purchase can be viewed as a reduction in the cost of advances.** All stock purchases are assumed to be financed at the three-month advance rate.

The table shows the impact of the 4.99 percent dividend on the "all-in" cost of advances.

A member borrows a \$1 million advance for a period of 91 days, which requires a stock purchase of \$40,000 (four percent of the advance amount). The interest cost on the advance for 91 days would amount to \$4,803. The net benefit of owning the stock is the difference between the dividend rate of 4.99 percent and the interest cost of financing the stock purchase 1.90 percent (three-month advance rate).

The net benefit is \$306, reducing the total interest cost to \$4,497. This reduces the "all-in" advance rate to 1.78 percent, or a reduction of 12 basis points from the posted advance rate. For members borrowing for a term of one day, the activity-based stock requirement is three percent, or 75 percent of the activity-based stock requirement for longer terms so the resultant benefit would be 75 percent of the 12 basis points benefit of borrowing longer term, or nine basis points. As you can see, the greater the amount of activity-based stock purchased, the larger the impact on borrowing costs.

Principal	FHLB Boston Advance Rate	Interest Cost on Advance
\$1,000,000.00	1.90%	\$4,802.78

Required Stock (4% of Advance)	Current Dividend Rate	Interest Earned on FHLB Boston Stock
\$40,000.00	4.99%	\$497.63

Funding Rate on Stock Purchase	Interest Cost on Stock Purchase	Net Benefit from FHLB Boston Stock Purchase
1.90%	\$192.11	\$305.52

Total "All-In" Rate	Economic Impact of Dividend	Net Interest Cost
1.78%	0.12%	\$4,497.26

Note: Days to Maturity (91); Advance Day Count (360)

The Bottom Line

At a time when members are considering the effect of rising interest rates on their net interest margins and evaluating different sources of wholesale funding, **be sure to consider the positive impact of the Bank's increased dividend on the cost of advances.**