

# How It Works: Discount Note Auction-Floater Advance



February 2023

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# What is the Discount Note Auction-Floater Advance?

The Discount Note Auction- (DNA) Floater provides long-term liquidity with short-term rate exposure and prepayment flexibility.

## Features of the Discount Note Auction-Floater Advance

<b>Coupon Type</b>	Floating	<b>Prepayable</b>	At each reset without a fee
<b>Available Term</b>	Up to 20 years	<b>Rate Reset Frequency</b>	4- or 13-weeks
<b>Interest Calculation</b>	Simple Interest (ACT/360)	<b>Minimum Size</b>	\$2,000,000
<b>Interest Paid</b>	At adjustment	<b>Availability</b>	Every Tuesday & Thursday, until 10:45am
<b>Principal Paid</b>	At maturity	<b>Settlement</b>	Next business day (t+1)
<b>Spread</b>	Fixed at initiation for the life of the advance		

# What are Discount Notes?

The FHLBank system is one of the largest issuers of debt globally, and discount notes play a key part.



Discount Note Auction Results (1/12/2023)	
4-week	4.383%
13-week	4.634%

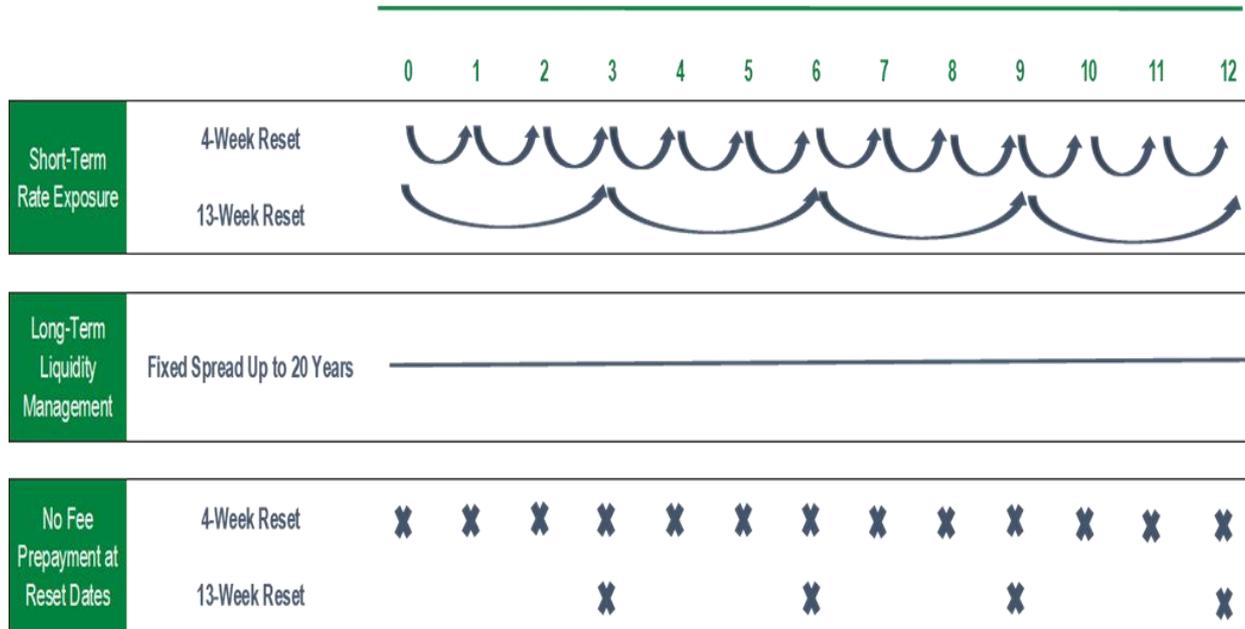
More information about discount notes can be found at the [FHLBanks Office of Finance website](#)

Source: Office of Finance, FHLBank Boston

# How Does the DNA Floater Advance Work?

The spread is fixed for the life of the maturity, while the index floats at pre-determined intervals.

Timeline (Months)



## Example

The member initiates the advance, locking in the spread and pricing the first coupon off the most recent auction result.

At either the 4-week or 13-week mark, the rate will reset based off the latest auction/index, while the spread remains fixed.

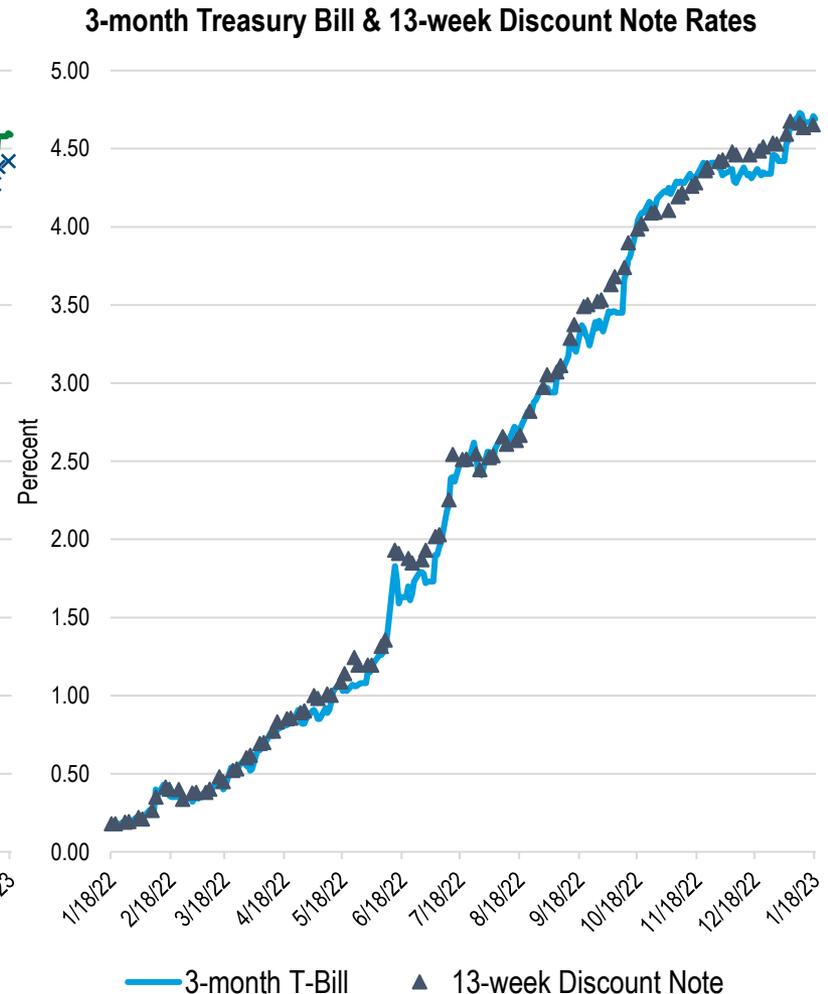
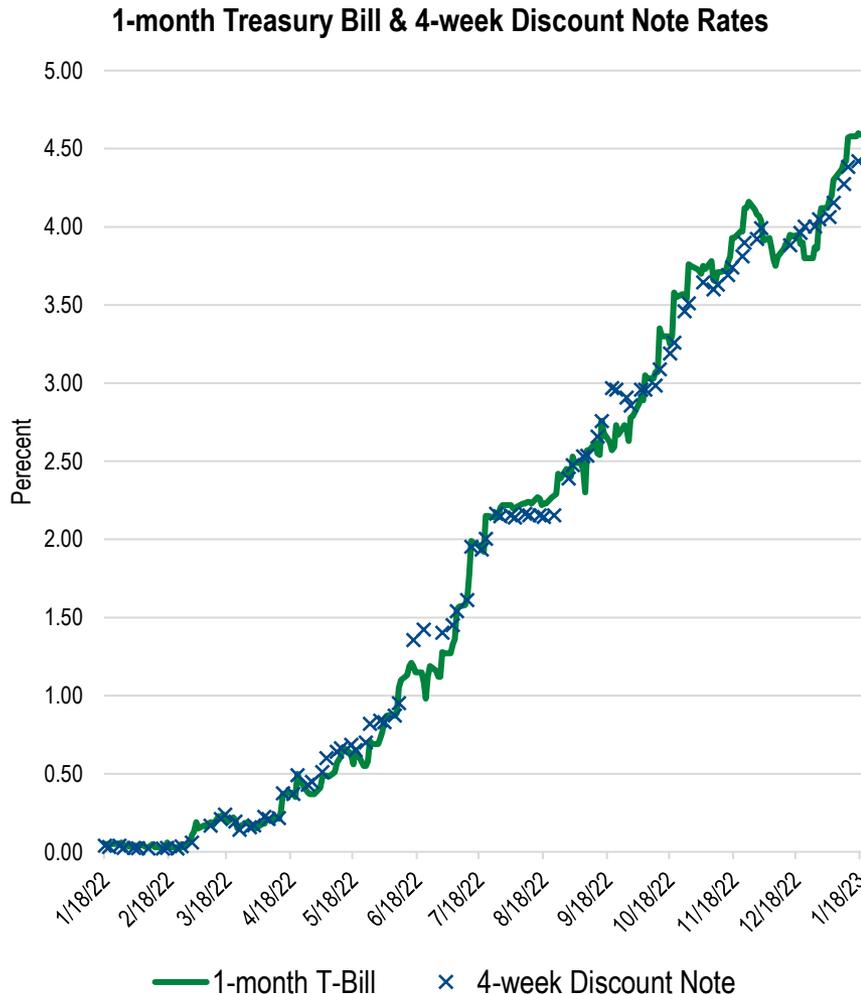
At that reset date, the member has the option to prepay the advance (in part or full) with no prepayment fee.

Structure	DN Index	Spread	Initial All-in Rate (as of 1/13/23)
1-year maturity, 4-week reset	4.38%	0.25%	4.63%
2-year maturity, 4-week reset	4.38%	0.30%	4.68%
5-year maturity, 4-week reset	4.38%	0.49%	4.87%

Source: Office of Finance, FHLBank Boston

# Do Discount Notes Correlate with Other Short-Term Rates?

Discount notes tend to trade closely to U.S. Treasuries of similar terms, with a correlation > 0.99.

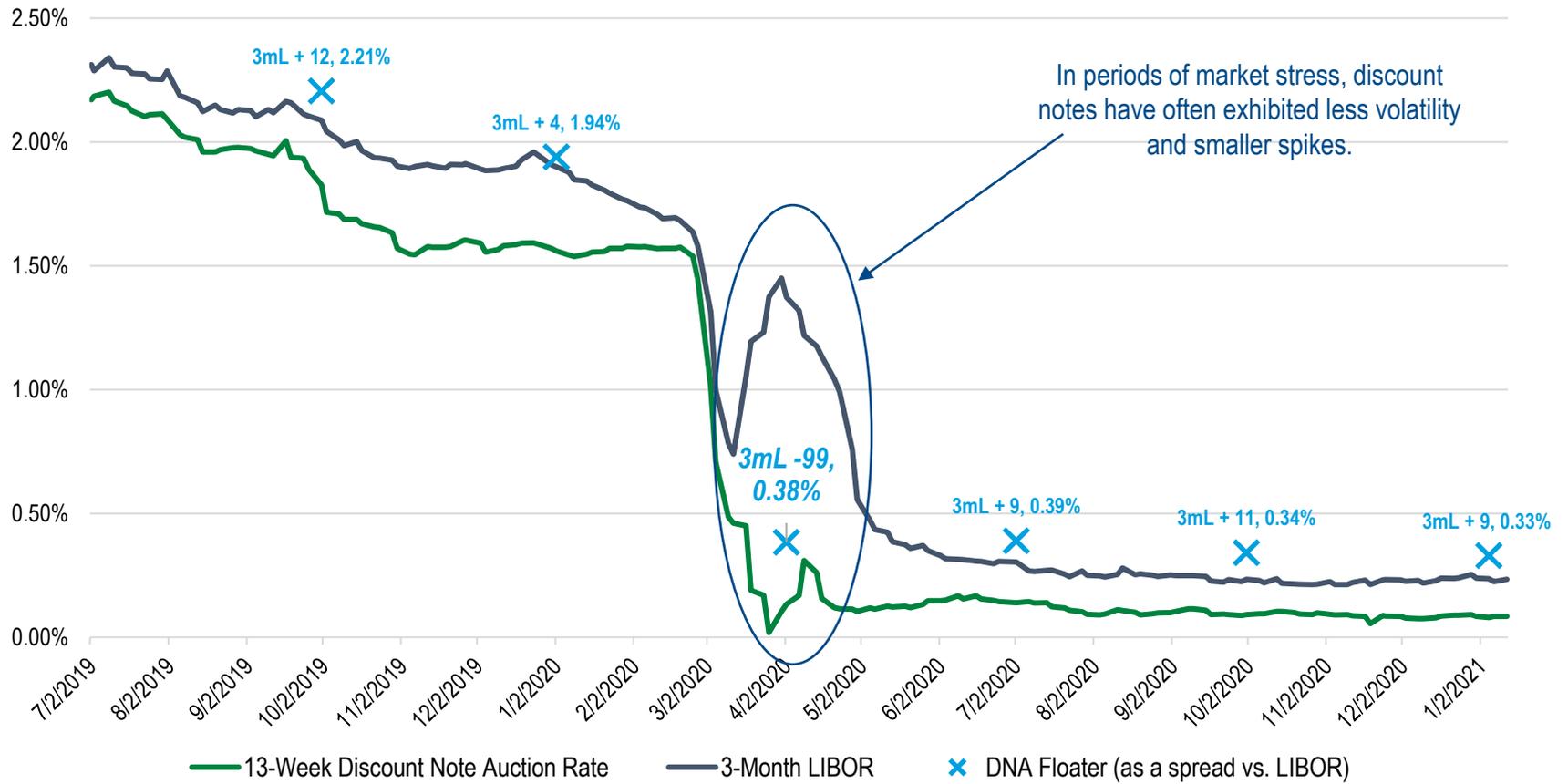


Source: Office of Finance, Federal Reserve Bank of St. Louis, FHLBank Boston

# How Has the Advance Fared in Volatile Markets?

Having locked-in spreads ahead of market shocks can allow for reduced repricing risk.

2019-2021 Example: 13-Week Discount Note Auction vs 3-Month LIBOR

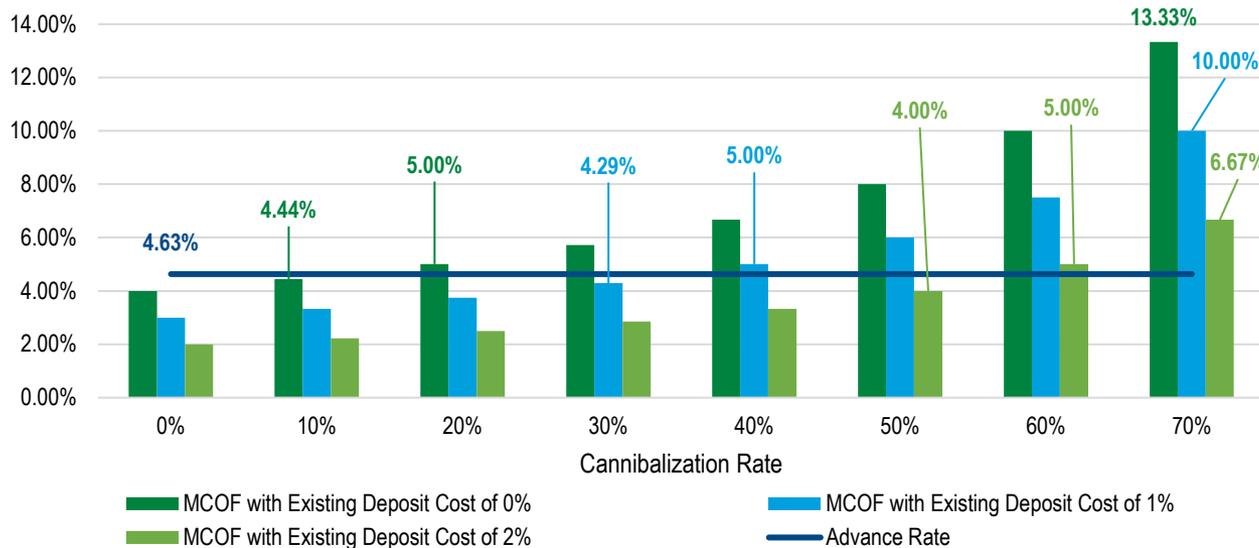


Source: Office of Finance, Federal Reserve Bank of St. Louis, FHLBank Boston

# How Do Depositories Use the DNA Floater?

The advance can be supportive of liquidity metrics today, while aligning with an asset sensitive interest-rate risk profile and potentially volatile future wholesale funding needs.

Marginal Cost of Funds Analysis (MCOF) Assumed 4% New Deposit Rate



## How Much Cannibalization Can You Withstand?

- Existing Deposits at 0%? = ~13%
- Existing Deposits at 1%? = ~35%
- Existing Deposits at 2%? = ~56%

### Funding Comparison: Retail CDs vs. DNA Floater Advance

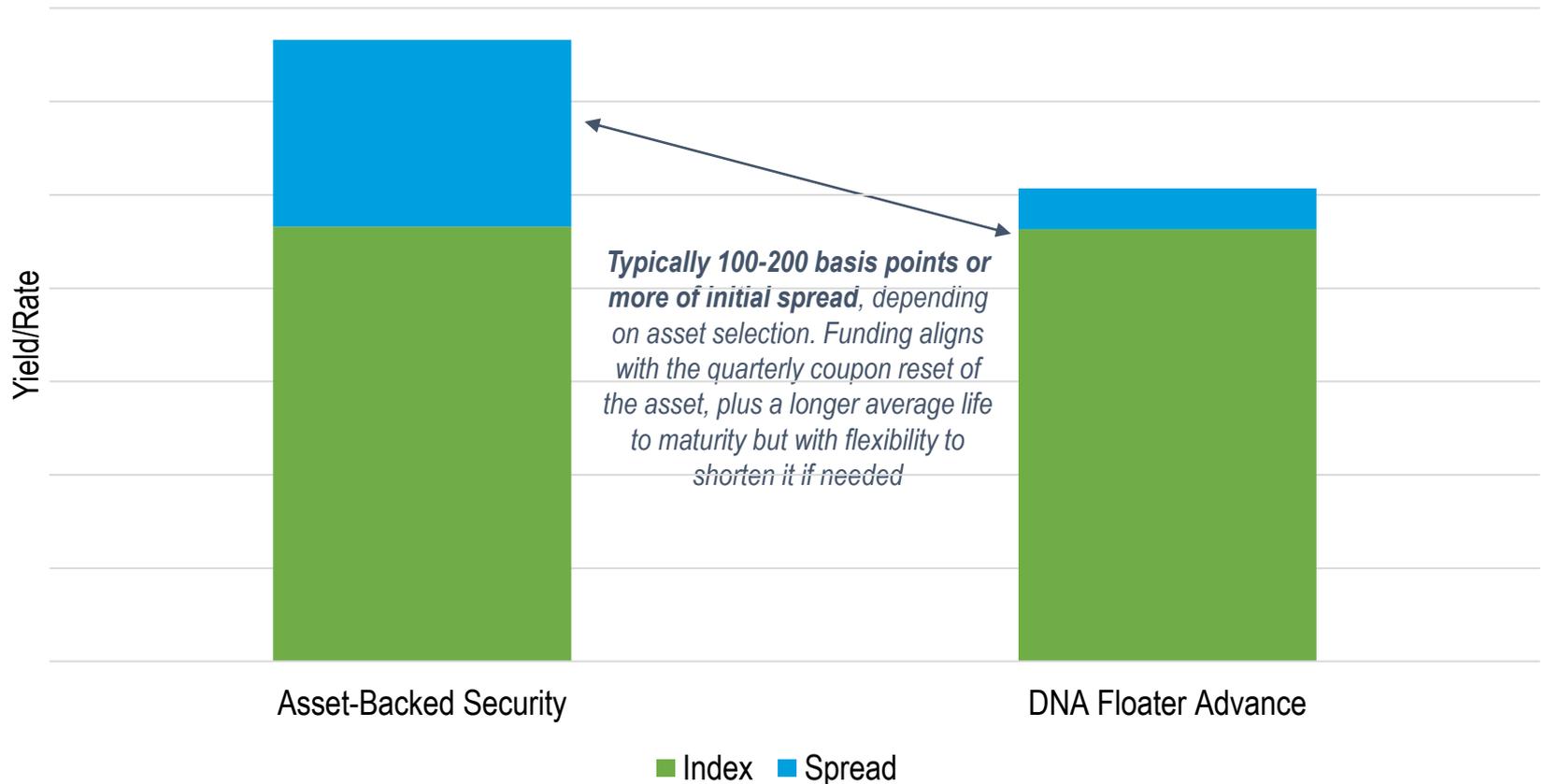
	RATE	AVERAGE LIFE	NEXT REPRICING
1-month retail CD	4.00%	1 month	1 month
12-month retail CD	4.00%	12 months	12 months
<b>1-year maturity, 4-week reset DNA Floater Advance</b>	<b>4.63%</b>	<b>12 months</b>	<b>1 month</b>

Source: Office of Finance, FHLBank Boston

# How Do Insurance Companies Use the DNA Floater?

Members can deploy the advance effectively to fund floating-rate investments, achieve an interest-rate risk match and line up with the potential average life of the asset(s).

## Spread Lending Example



Source: FHLBank Boston

# Thank You



Andrew Paolillo

Andrew.Paolillo@fhlbboston.com

617-292-9644

If you have questions or if you want more information, please contact us or your relationship manager.

