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## **Recommendations on the Principal Characteristics and Calculation Conventions of Listed Bonds and Bills**

OMX Nordic Exchange in Iceland (the Exchange) is currently working at harmonising the framework and practices on its markets with the most common practices on markets abroad. The purpose of such harmonisation is primarily to facilitate access by foreign investors to the market, resulting in improved price formation and greater access to capital for issuers.

The Icelandic fixed-income market differs in a number of respects from leading markets abroad. Although important steps towards co-ordination have been taken on the initiative of both the National Debt Management Agency (NDMA) and the Housing Financing Fund (HFF), more still needs to be done. To this end, the Exchange has decided, following a review process, to recommend to issuers of listed bonds that their new issues comply with international practice with regard to their principal characteristics and calculations. The recommendations are listed below. For further information, please contact Brynjar Orn Olafsson ([brynjar.olafsson@omxgroup.com](mailto:brynjar.olafsson@omxgroup.com) tel. +354 525 -2856).

### **Bonds**

#### **Recommendation No. 1: Bullet bonds (zero-coupon or with coupons)**

There are a variety of reasons for issuing bonds and their characteristics, including the arrangements for repayment, are often determined by the nature of the undertaking the issue is intended to finance. Unless there are specific reasons for doing otherwise, the Exchange recommends to issuers that they issue bullet bonds (zero-coupon or with coupons). These types of bonds are simple to handle and in common use abroad. They require neither specialised expertise nor adaptation of the systems used by foreign traders to keep track of their bond assets.

#### **Recommendation No. 2: Annual interest payments**

In most European countries it is common practice to make interest payments annually, while in English-speaking countries (the UK, US, Australia, Canada and New Zealand) payments are generally made semi-annually, as shown in Table 1. The Exchange recommends that coupon bonds have annual coupon payments, as is the custom in most European countries.

#### **Recommendation No. 3: Clean price**

Most bonds listed on the Exchange are quoted at settlement price, i.e. dirty price, and in the case of indexed bonds, include inflation adjustment. There are, however, important exceptions to this rule, such as the most recent Treasury notes series and HFF bonds, where the listed market price is the clean price, although this is naturally taken into consideration upon settlement. The quoted prices on all leading bond markets abroad are clean prices. The Exchange recommends that issuers quote clean prices in transactions with their new bond series and, in the case of indexed bonds, without inflation adjustment.

#### **Recommendation No. 4: Day count convention: Actual/Actual (ICMA)**

In calculating yields and accrued interest on bonds, it makes a difference what day count convention is used. There are a number of different practices in this regard. Common practice on the Icelandic market is the so-called 30/360 method, which is based on 30 days for each month and 360 days for each year. HFF bonds are calculated on a 30E/360 basis. The difference between these two methods is in how the 31<sup>st</sup> day of the month is treated in counting. The 30E/360 convention is used on national government bond markets in Denmark and Sweden,



while in Norway the Actual/365 convention is followed. On the largest government bond markets abroad, including those in the UK, the US, Germany, France and elsewhere, the actual/actual (ACT/ACT ICMA) convention is applied. In this case the actual number of days in the intervening period is used. The Exchange recommends that issuers follow the actual/actual (ICMA) day count convention in their new bond issues. The most recent domestic Treasury notes series, RIKB 10 0317 and RIKB 13 0517, have already adopted the actual/actual convention. NDMA made this decision with the aim of harmonising its issues with the most widespread practice elsewhere. These new Treasury notes series accord in all respects with the recommendations set forth here.

**Table 1. No. of annual interest payments and day-count conventions for bonds in various states**

Country	No. int. payments annually	Day-count convention
Australia	2	actual/actual
Austria	1	actual/actual
US	2	actual/actual
Belgium	1	actual/actual
United Kingdom	2	actual/actual
Denmark	1	30E/360
France	1	actual/actual
Ireland	1	actual/actual
Italy	1	actual/actual
Canada	2	actual/actual
Norway	1	actual/365
New Zealand	2	actual/actual
Spain	1	actual/actual
Switzerland	1	30E/360
Sweden	1	30E/360
Germany	1	actual/actual

*Source:* Moorad Choudhry, *The Repo Handbook* (Oxford: Butterworth Heinemann, 2002).

## **Bills**

### **Recommendation No. 5: Day count convention: Actual/360**

Up until now, it has been customary on the Icelandic money market to price bills using the 30/360 day count convention. Calculation of money market instruments with a maturity of less than 1 year is especially sensitive to the choice of day count convention. As an example, according to the 30/360 day count convention, the number of days from 1 October 2006 to 31 December 2006 is 89 while using the Actual/360 convention it would be 91. In the Eurozone and US money markets it is customary to use the Actual/360 convention, and the Icelandic Central Bank's interbank market also follows this practice. The Exchange recommends that issuers follow the Actual/360 day count convention in their new bill issues.