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WORKING GROUP ON SECURITIES DATABASES

RECOMMENDATION 7 OF THE G20 DATA GAPS INITIATIVE PHASE 2 (DGI-2)

COMPLEMENTARY NOTE NO 2 (CN 2) ON THE REPORTING TEMPLATES

CLASSIFICATION OF DEBT SECURITIES BY INTEREST RATE TYPE

Recommendation 7 on Securities Statistics of the G20 Data Gaps Initiative Phase 2 (DGI-2) is based on the methodology contained in the *Handbook on Securities Statistics* (*HSS*). In particular Chapter 7, paragraphs 7.36 to 7.44, covers the breakdown of debt securities by interest rate type.

This **Complementary Note No 2 (CN 2)** to the *HSS* provides further explanations on the **classification of debt securities by interest rate type** in the reporting templates on Recommendation 7 of the DGI-2.

The reporting templates 1 and 2 of Recommendation 7 of the DGI-2 request the reporting of securities statistics classified according to different criteria: currency, maturity, interest rate and, where relevant, market of issuance. Each classification criterion groups the securities in sub-sets that do not overlap and add up to the total.

Classification of debt securities under fixed or variable interest rate

The *HSS* (chapter 7) defines **fixed interest rate debt securities** as securities for which at the date of issue (a) the contractual nominal coupon payments are fixed and constant in terms of the currency of denomination for the life of the debt security, or for a certain number of years, and (b) the principal repayment is fixed in terms of the currency of denomination and time.

Fixed interest rate debt securities include securities issued at par (value) or at a discount or premium, deep discounted and zero coupon bonds, strips, perpetuals, convertible and exchangeable bonds, subordinated bonds, equity warrants, and others as far as the definition is met.

According to the *HSS*, **variable interest rate debt securities** have their coupon or principal payments (or both) linked to a general price index for goods and services (such as the consumer price index (CPI)), to a benchmark interest rate (such as the London interbank offered rate (LIBOR) or a bond yield), or to an asset price (such as gold). The reference value fluctuates in response to market conditions.

The *HSS* also considers a third category, **mixed interest rate debt securities**, which have both a fixed and variable coupon over their life. In particular, this category covers securities with a fixed coupon and a variable coupon at the same time, a fixed (or a variable) coupon until a reference point, and then a variable (or a fixed) coupon from that reference point to the maturity date, and those with coupon payments that are prefixed over the life of the debt security but are not constant over time.

The reporting templates 1 and 2 of Recommendation 7 of the DGI-2 request the reporting of data classifying the securities according to interest rate into two categories: fixed and variable interest rate. Given that these two categories must add up to the total it is necessary to allocate those securities defined in the HSS as mixed interest rate securities to one of these two categories.

Considering that the securities under the mixed interest rate category are not homogenous but contain certain features that make them closer to fixed or variable interest rates, it is necessary to consider those features for the reporting. Therefore, all **securities that contain a variable coupon combined with a fixed coupon should be classified under the category variable interest rate for the purpose of the templates of Recommendation 7**. Conversely, **those with prefixed different coupons along the life of the security (stepped interest rate) should be classified under the category fixed interest rate for the purposes of the templates on Recommendation 7**. Moreover, all these securities should remain in the same item and once allocated to a category not be reclassified on the basis of the current or future type of coupon.

Classification of variable interest debt securities in subcategories

The *HSS* classifies variable interest debt securities in three subcategories, namely inflation-linked, asset price-linked and interest rate-linked. The first two subcategories are grouped under the common denomination of index-linked.

Reporting template 1 of Recommendation 7 of the DGI-2 requests the reporting of data classifying variable interest rate securities into the three categories defined in the *HSS*. Given that these three categories must add up to the total variable interest rate securities, it is necessary to further clarify how to apply these categories.

For that purpose, it is noted that the subcategory inflation-linked is restricted to securities linked to price indices. The subcategory interest rate-linked is limited to securities linked to interest rate indices or bond yields. Therefore, the only subcategory with a wider coverage is the **asset price-linked, which should be understood not only referring to financial assets and commodities but by extension to any other link different from interest rates or inflation**. For example, securities with a coupon linked to baskets of securities, indices different from prices or interest rates, currencies, business or other types of links.

Mixed interest rates classified under variable rates for the purpose of Recommendation 7 reporting will be allocated to each subcategory depending to the type of interest rate link.

In conclusion, all debt securities to be reported in templates 1 and 2 of Recommendation 7 must be classified either as fixed or variable interest rate, and those in the last category should additionally be split into one of the three subcategories indicated in reporting form 1.