

CURVE FLATTENER ADVANCE PRIMER

I. Product Information

Background

The Federal Home Loan Bank of Boston offers the Curve Flattener advance. The Curve Flattener advance can be a cost-effective solution for members seeking protection against a flattening yield curve since its advance rate will decline as the yield curve flattens.

Characteristics

The Curve Flattener advance is a fixed-term, floating-rate, non-amortizing advance. The coupon is the sum of two components—one that is fixed for the term of the advance and a second that will vary during the term of the advance and measures the difference between two points on the Constant Maturity Swap yield curve. (See below, “How it Works”). It is permissible for the interest rate on the Curve Flattener advance to reset at an interest rate less than zero.

Curve Flattener advances are available in terms out to 20 years. Curve Flattener advances have a \$2 million minimum, but smaller requests may be accommodated in special offerings, which the Bank may offer from time to time. The advance is prepayable, in whole or in part, on any date with two business-days notice, subject to a fee to make the Bank financially indifferent to the member’s decision to prepay. Partial prepayments may be in amounts as small as \$100,000 and in intervals of \$100,000 thereafter.

How it Works

In this example, a member takes down a Curve Flattener advance with a five-year term using the two- and 10-year points on the CMS curve. The member pays an initial advance rate of 1.68 percent, comprised of a fixed component of 0.27 percent added to a rate differential component of 1.41 percent. The rate differential component is the difference between the 10- and 2- year points on the CMS curve (2.00 percent and 0.59 percent, respectively) on the day of the transaction. The rate differential component will be calculated on a quarterly basis, and it is added to the fixed component to establish the advance rate for the next three months. If the curve gets flatter (the rate differential component declines), the advance rate declines, and, conversely, if the curve gets steeper (the rate differential component increases), the advance rate increases. The advance rate resets quarterly. The table below illustrates how a Curve Flattener advance with these terms reacts as the shape of the CMS yield curve changes. This table is for illustrative purposes only and is not representative of actual pricing for the Curve Flattener advance. Furthermore, the table is not intended to be an indication of the future performance of the Curve Flattener advance or of future interest rate trends associated with the Curve Flattener advance.

Curve Flattener Advance

5 Year Term
10Y CMS & 2Y CMS

| Fixed | | Rate Differential | | | |
|-----------|--------------------|------------------------|---------------------------|--------|-------------------------|
| Component | (10Y CMS – 2Y CMS) | Component ¹ | Advance Rate ² | | |
| 0.27% | 1.25% | 1.62% | -0.37% | -0.10% | } Flatter (or inverted) |
| 0.27% | 1.50% | 0.79% | 0.71% | 0.98% | |
| 0.27% | 1.75% | 0.69% | 1.06% | 1.33% | |
| 0.27% | 2.00% | 0.59% | 1.41% | 1.68% | START |
| 0.27% | 2.25% | 0.49% | 1.76% | 2.03% | } Steeper |
| 0.27% | 2.50% | 0.39% | 2.11% | 2.38% | |
| 0.27% | 2.75% | 0.29% | 2.46% | 2.73% | |

¹ Rate differential component equals longer-term CMS less shorter-term CMS

² Advance rate equals the sum of the fixed component and the rate differential component

Additional Characteristics

Curve Flattener advances can be requested until 1:00 p.m. on a Boston business day and typically disburse two business days after the trade date. Interest on a Curve Flattener advance is calculated on an actual/360-day basis and is paid quarterly on rate-reset dates. The principal on the Curve Flattener advance is due at maturity. Members choose two points on the CMS yield curve (the 1-, 2-, 5-, 10-, and 30-year points are available), which will be used to calculate the rate differential component. The rate differential component is equal to the longer term minus the shorter term. The advance rate on a Curve Flattener advance can be less than zero. Members specify the term and the points to construct the rate differential component based on their own interest-rate risk management objectives.

If you would like to find out more about the Curve Flattener advance or have additional questions, please call the Money Desk at 800-357-3452 or your relationship manager.

Members may have to purchase additional activity stock in some cases. The activity stock capitalization requirement on a Curve Flattener advance is 4.5 percent.

Uses

Many financial institutions are exposed to changes in the shape of the yield curve and may be especially vulnerable to a flattening of the yield curve, i.e. when the difference between long-term interest rates and short-term interest rates declines. Such is the case if deposits are priced off short-term interest rates while many assets are priced off long-term interest rates. When the spread between these parts of the yield curve declines, net interest income can be negatively impacted. Members can use a Curve Flattener advance to offset some of this exposure to changes in the shape of the yield curve.

The Bank has financial strategists who can help members analyze the types of funding that meet their specific needs. If you would like an analysis, please contact the strategists at 800-357-3452 or via email at strategies@fhlbboston.com.

A member should review the [Products and Solutions Guide](#) prior to taking an advance to understand the terms of the contract and the prepayment provisions. Certain market conditions may occasionally prevent the Federal Home Loan Bank of Boston from being able to execute the Curve Flattener advance.

This statement does not purport to disclose all of the risks and other material considerations associated with Curve Flattener advances. Members should not construe this disclosure statement as business, legal, tax, or accounting advice from the Bank. Members should consult with their own business, legal, tax, and accounting advisers with respect to Curve Flattener advances and should refrain from using a Curve Flattener advance unless they have fully understood the terms and risks of the Curve Flattener advance.