

**ATTACHMENT I**

**EXAMPLE OF INTEREST RATE SWAP**

**Details of Interest Rate Swap Agreement**

Notional principal	\$10,000,000
Term	5 years
Swap	Member makes fixed payments to AC. Member received floating payments from AC.
Fixed interest rate	11%
Floating interest rate	Bankers Acceptance rate (BA) + 50 bps Initially set at 10.75% $(10.75 + .50) = 11.25\%$
Margin rate GOC, 3-7 years	2%
Margin rate for fixed interest rate swap	$2\% + 25\% \text{ premium} = 2.50\%$
Margin rate for GOC < 1 year	$1\% \times \# \text{ days to reset date} / 365 = 1\% \times 90 / 365$

**Assumptions**

Three months into the swap agreement	90 days to next reset date
Current market interest rate for fixed swap (term of 4 years, 9 months)	11.50%
Bankers acceptance interest rate reset	BA + 50 bps

**Margin Requirements**

Margin on fixed rate payments (10,000,000 x 2% x 1.25)	\$250,000
---	-----------

Margin on floating rate payments (10,000,000 x 1% x 90/365)	24,658
--	--------

---

Margin before offsets	\$274,658
-----------------------	-----------

Margin reduction (inventory offsets):

Assume inventory long GOC 8%, October 1, 2000

Par \$10 million / Market value 99.575 (10,000,000 x 99.575 x 2%)	(199,150)
--	-----------

Assume inventory short BA maturity in one month

Par \$9 million / Market value 99.90 (9,000,000 x 99.90 x 2% x 1/12)	( 14,985)
---	-----------

---

Net margin required	<u><u>60,523</u></u>
---------------------	----------------------

---

**Market Deficiency Calculation:**

Three months into the agreement, the market has changed and the Member must mark to market this swap. Current market interest rate for fixed term interest rate swaps (4 years and 9 months) is 11.50%. The Bankers Acceptance rate is reset to current market rate and therefore requires no mark to market.

**Part 1**

Fixed Rate Differential	0.50%
Notional Principal	<u>\$10,000,000</u>
Annual Payment Differential	<u>50,000</u>
Present Value of \$50,000 at 11.50% for four years, nine months on a semi-annual basis	<u>\$ 175,256</u>

**Part 2**

1. Interest on fixed principal for three months $\$10,000,000 \times 11\% \times 91/365 =$	\$ <274,246>
2. Interest on floating principal for three months $\$10,000,000 \times 11.25\% \times 91/365 =$	<u>\$ &lt;280,479&gt;</u>
	<u>\$ &lt; 6,233&gt;</u>

**MTM Total**

Part 1	175,256
Part 2	<u>&lt;6,233&gt;</u>
	<u>\$ 169,023</u>

In this example, the current market interest rate has risen, therefore, the fixed rate (in this case, the Client) has a loss. Netted against this loss is the client's right to receive the \$6,233 accrued interest.