

# Central Bank Securities

## What are securities?

The Central Bank of Samoa introduced tenders of central bank securities in January 1998 as part of a package of reforms aimed at liberalising (opening up) the financial sector.

A Central Bank of Samoa security is a short-term financial instrument, in much the same way that a bank deposit is a financial instrument.

As with other financial instruments, there are two parties involved - the issuer, who is raising funds, and the investor. In this case, the Central Bank of Samoa is the issuer and raises funds by issuing the security, and the investors are those who purchase the security.

When the Central Bank receives the funds, it issues the investor with a certificate of title which acts as a receipt and evidence of ownership.

This certificate is the actual security. It states how much has been invested, when the investment matures

and how much the Central Bank will pay back when the investment matures. Repayment is guaranteed by the Central Bank of Samoa.

The securities are issued in accordance with the Prospectus for Central Bank of Samoa securities. The Prospectus is a legal document which stipulates the features of the securities and how the securities must be issued.

## How are they issued?

The securities are issued through a tender, or auction, as the process is sometimes known.

There are two ways of participating in a tender. Participants in the tender - the bidders - can submit either a competitive bid or a non-competitive bid.

In placing a competitive bid, the bidders submit bids for the amount of securities they want to purchase and the yield they want to receive, where the yield is the return on the funds invested.

For example, a bidder might bid for \$50,000 at a yield of 8 percent.

At least 90 percent of the securities offered for sale are earmarked for competitive bidders. Up to 10 percent of the securities offered for sale can be purchased by non-competitive bidders.

For a non-competitive bid, bidders only bid the amount they wish to purchase. No yield is specified as the securities are allocated at the weighted average yield of the successful competitive bids.

Non-competitive bids are therefore suitable for those who are not confident about bidding an interest rate or those that want to be certain of purchasing at least a small portion of the securities available.

The securities are issued at a discount. This means that if you are successful in the tender, then you pay less than the face value and then at maturity you get the face value of the security.

The higher the yield bid, the lower the purchase price. For example, if the face value of the security is \$1,000, and you were successful

with your bid of 8 percent, then you would pay \$980.44 when you purchase the security and you would receive \$1,000 on maturity.

At its discretion, the Central Bank offers securities at 14, 28, 56, 91, 182 and/or 365-day maturities.

## **Who can participate?**

Any Samoan resident over the age of 18 years is eligible to participate in the tenders. This means that banks, non-bank financial institutions, businesses, church groups, trusts and members of the public can all participate.

Prior to bidding in a tender, bidders must have registered with the Central Bank of Samoa. Registration is straightforward and requires the bidder to complete a registration form.

## **Why does CBS issue securities?**

The Central Bank issues securities for monetary policy reasons. When the Central Bank issues securities, it is trying to slow down

money and credit growth by withdrawing money from banks and the public.

If the rate of credit growth or money supply growth is too high then there will be too much spending in the economy, relative to the amount of goods and services available to the economy. Too much money will be chasing the limited goods and services that are available. If this happens, inflation will be too high and the country's foreign reserves will decline with the increased demand for imports.

Tenders are often held weekly, but the timing of the auctions, and the amount of securities offered for sale, can vary depending on how the Central Bank views monetary conditions, its monetary policy stance, and the demand for the securities.

## The tender cycle

There are five stages in the tender cycle: the Central Bank announces the auction details, bids are lodged, successful bids are determined, results are announced, and the securities are issued.

1. Announcing the tender - Once the Central Bank has decided to hold an auction, it issues an Invitation to Bid which gives details of the amount of securities to be sold in the tender, when and where bids can be lodged, and when the results of the tender will be announced.

2. Bidding - Bids are entered on a bid form and this is lodged at the Central Bank in a locked tender box. This box is only opened once the tender has closed. Any single bid must be for at least \$1,000 but there is no limit on the maximum amount that can be bid, subject of course to the total amount of securities that are being offered for sale at the tender.

3. Determining the successful bids - After opening the tender box, the Central Bank ranks the bids from the lowest interest rate to the highest interest rate. Starting with the lowest interest rate bid, it allocates the value of securities bid at that rate until the total amount of securities on offer in the tender has been allocated. When the amount remaining is less than the bids at the next highest interest rate, then this amount is allocated in proportion to the amount of the individual bids.

4. Announcing the results - Results are announced on the same day that the tender closes. Successful and unsuccessful bidders are informed by telephone and in writing. The Central Bank also issues a press release giving summary results on the total amount bid, the total amount issued, and the weighted average yield for successful bids. Details of individual bids and the identity of successful bidders are not divulged.

5. Issuing the securities - The securities are only issued on payment. There are special payment arrangements in place for banks since they have accounts with the Central Bank. For others, payment can be made by bank cheque, personal cheque, or cash.

## **Selling securities before maturity**

If an investor wishes to sell the security before it matures, then this can be done by trading the security on the open market or selling the

security back to the Central Bank.

The securities are transferable, which means that the holder of the security can sell it before its maturity date to anyone else who is eligible to hold the security. All that is required is for the original owner to sign the back of the certificate, indicating that the original owner has relinquished ownership. This signature is known as an endorsement.

The securities are also negotiable which means that the buyer and the seller are free to negotiate between themselves the price at which the security will be sold.

If for some reason the holder of the security does not wish to sell to another member of the public or cannot find someone who is willing to purchase the security, then the holder can still sell the security to the Central Bank but the Central Bank will pay a lower price than could be obtained elsewhere. When the Central Bank purchases securities in this way, the transaction is referred to as rediscounting.