



**Da Afghanistan Bank**  
**Market Operation Directorate General**

## **Repo/Reverse Repo Regulation**

**YEAR**  
**2020**

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## Chapter 1: General Provisions

### Article 1: Basis

This regulation is based on the Articles 3 and 63 of Da Afghanistan Bank (DAB) Law to regulate securities Repo Market.

### Article 2: Objectives

The objectives of this Regulation are as follow:

- (1) Establish a basic framework for repo/reverse repo Operations of securities issued by Da Afghanistan Bank,
- (2) To facilitate and develop interbank market,
- (3) To provide an efficient source of short-term funding for commercial banks to manage their short-term liquidity shortage by selling and purchasing of government securities,
- (4) To provide a secure and flexible avenue for short-term investment,
- (5) To facilitate the flow of cash and security around the financial system and
- (6) To facilitate DAB's monetary policy operations.

### Article 3: Scope of Application

This regulation is applicable on DAB, banks licensed by DAB and other institutions permitted by DAB to participate in the Repo/Reverse Repo operations.

### Article 4: Definitions

- (1) The terms used in this Regulation shall have the following meanings:
  1. **Bank:** means a legal person engaging in the business of receiving money deposits or other repayable funds from the public for the purpose of making credits for its own benefit within the Islamic Republic of Afghanistan.
  2. **CNs:** Means Capital Notes.
  3. **CSD:** Means Central Security Depository
  4. **Delivery vs Payment:** is a settlement mechanism which stipulates that transfer of funds from the buyer of securities is made simultaneously with the transfer of securities by the seller of securities.
  5. **Haircut:** is the difference between the market value of the collateral and the amount borrowed/lent against that collateral.
  6. **Maturity:** means the date in which the security become due and payable and ceases to earn interest.
  7. **Market risk:** is the possibility of an investor experiencing losses due to factors that affect the overall performance of the financial markets in which he/she/it is involved.
  8. **Overseer:** Market Operation Department of DAB.
  9. **Repo Transaction:** also Known as "Repurchase Agreement" means a transaction wherein the securities are sold at a particular price by one party (Seller) to the other (Buyer) with commitments on the seller's part to repurchase the equivalent securities from the buyer on a certain date and at a certain price, both such date and price being fixed as a part of the same transaction.
  10. **Reverse Repo:** also Known as "Reverse Repurchase Agreement" means a transaction wherein the securities are bought at a particular price by one party (Buyer) from the one (seller) with a commitment on the Buyer's part to sell the Equivalent Securities back to the Seller on a certain date and at a certain price both such date and price being fixed as a part of the same transaction.

A 'Repo' transaction by an entity is 'Reverse Repo' transaction for the counterpart entity. For the purpose of these directions, the word 'repo' is used to mean both 'repo' and 'reverse repo' with the appropriate meaning applied contextually.

11. **Settlement:** means delivery of a security by a seller to a buyer and exchange of cash by the buyer to the seller and vice versa on or before the settlement date.
12. **Settlement Risk:** Settlement risk is the possibility that one or more parties will fail to deliver on the terms of a contract at the agreed-upon time
13. **Settlement Date:** For the first leg of the transaction the settlement date shall be no longer than one day from the deal date by the parties i.e. T+1. At the time of second leg of the transaction the settlement date shall be the agreement end date.
14. **Shut Period:** 'Shut period' means the period for which the securities cannot be traded. During the period under shut, no trading of the security which is under shut is allowed.
15. **Sukuk:** An Islamic Financial Certificate of equal value representing undivided shares in the ownership of tangible assets, usufructs and services or (in the ownership of) the assets of particular projects or special investment activities.

## Chapter 2: Repo/Reverse Operating System and Transactions

### Article 5: Repo Operation System

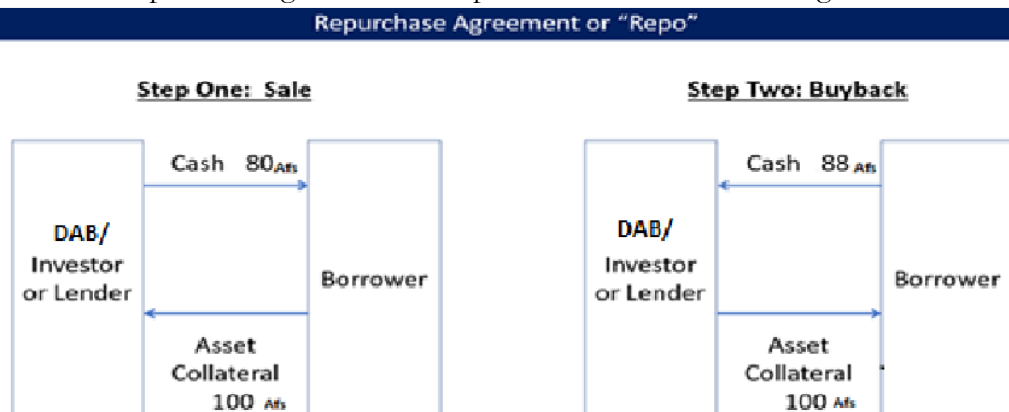
DAB has implemented a Central Securities Depository (CSD). The CSD system manages the life cycle of Government institutions' fixed income securities. Payment and transfer operations for all securities traded or purchased are guaranteed under the Delivery versus Payment (DvP) principle.

### Article 6: Repo Transaction

The repo/reverse repo transaction is executed under Delivery versus Payment (DvP) principle through the CSD system. After negotiation, the seller creates repo transition in the system and it goes for buyer's agreement, after the buyer agreed, he sends the transaction to DAB for approval. After DAB's approval, the transaction will be settled and the system sends messages to the related parties and the ownership of the security is transferred to the buyer and the amount under the transaction will be credited to the seller's account. All above transactions are done through CSD.

### Article 7: Nature of Transaction

(1) Nature of the repurchase agreement or Repo is described in below diagram:



- (2) Uses of Repo:
  1. Monetary Policy: The Monetary Policy measures flexible instrument of DAB control of bank and market liquidity which can be used for both injections of liquidity and mopping up.
  2. Liquidity management by banks allows banks to finance the mismatch of payments and receipts and to maintain lower cash or liquid assets on average.

#### **Article 8: Basic Structure of Repo**

- (1) The assets most often used under repos are Government securities.
- (2) One counter party – the seller – agrees to sell securities to the other – the buyer – and simultaneously agrees to repurchase the securities at a date in the future for a specified price.
- (3) In effect, a repo is the combination of a spot transaction (the initial sale) and a forward transaction (the agreed-upon repurchase).
- (4) The securities are repurchased at a price that is the sum of the initial acquisition price plus the agreed-upon interest
- (5) The seller is economically the borrower – because he receives money in exchange for the securities with a duty to repay the money in return for the securities.
- (6) The buyer is economically the lender – because he receives securities (essentially collateral) in exchange for the money
- (7) The term of the repo (the time between the initial sale and the repurchase) may be overnight, for a specific period, or open. In case the repo is open there shall be sufficient notice as specified by DAB from time to time by either of the party.
- (8) The repo has two parts (“legs”) – both of which involve the transfer of securities and cash.

#### **Article 9: Specific Issues and Risks to Address**

- (1) Settlement risk solutions will be the settlement of each leg on a delivery versus payment basis (DVP).
- (2) Counterparty solution will be control of the securities as collateral.
- (3) Market margin requirements require securities with a market value greater than the amount financed.

### **Chapter 3: Characteristics of Repo Agreements**

#### **Article 10: Repo Agreement Content**

- (1) A Repo Agreement shall contain the following contents:
  1. Tenure of Repo
  2. Principle Amounts
  3. Price Source
  4. Proposed Repo Rates
  5. Legal participants
  6. Shut period
  7. Haircut
  8. Proposed calculation of Repo returns

#### **Article 11: Tenure of Repo**

Repos shall be undertaken for a minimum period of one day and a maximum period of one year. The parties may also engage in open repurchase agreements where at the request of any one

party the deal is closed. The timing and tenure for a repo transaction should not exceed the maturity of underlying security.

#### **Article 12: Price Source**

Da Afghanistan Bank weekly capital notes closing price is recommended as a basis for mark to market. However, if there should be significant overnight or intraday price movements, the daily mark to market price source shall be agreed between the two counterparties. Any issues with regard to the price should be resolved amicably by referring to prevailing market prices.

#### **Article 13: Repo Rates**

- (1) In case of bank to bank repo transaction the rate is freely negotiable between both parties, within the cap and ceiling proposed by DAB that shall be circulated from time to time.
- (2) For the repo transactions between banks and DAB, the rates shall be as follows:

Type of Maturity	Rate
<b>Overnight to 1 week</b>	C + 7 Days CN cut off rate
<b>1 week to 1 Month</b>	C + 28 Days CN cut off rate
<b>1 Month To 3 Month</b>	C + 91 Days CN cut off rate
<b>3 Month to 6 Month</b>	C + 182 Days CN cut off rate
<b>6 Month to 1 Year</b>	C + 364 Days CN cut off rate

- (3) Coefficient (C) shall be determined by DAB Executive Board from time to time.
- (4) Repo and reverse repo rates are published on DAB website from time to time.

#### **Article 14: Eligible Participants**

Currently Da Afghanistan Bank and commercial banks are the eligible participants of the repo operations. DAB shall communicate about the participation of other members to take a part in this market when deems necessary.

#### **Article 15: Eligible Securities:**

- (1) The following Securities are eligible for Repo/Reverse Repo transactions:
  1. DAB Capital Note;
  2. Sukuks issued by Government of Afghanistan.

#### **Article 16: Shut Period**

- (1) The shut period is set to be 3 days to the maturity for the securities.
- (2) Participants are not allowed to trade their security which is to mature in 3 days.

#### **Article 17: Haircut**

The haircut on the repo transactions is 10%.

#### **Article 18: Calculation of Repo Returns**

- (1) Repo rates are quoted on an investment basis with a bank discount Annualized factor.
- (2) The amount of interest earned on funds invested in a Repo is determined as follows:
  1. Interest earned = funds invested x Repo rate x (number of days/360).
  2.  $1,000,000 \times .0575 \times (1/360) = 159.72$
- (3) If the funds were invested in a ten-day term agreement at the same rate of 5.75 percent, the investor's interest earnings would look as follows:
  1.  $AFN 1,000,000 \times .0575 \times (10/360) = AFN 1,597.22.$

## Chapter 4: Operating Requirements and Code of Conduct

### Article 19: Business Hours

The timing and business hour of the repo transaction is same as DAB business hour from 08:00 to 15:00 Saturday to Wednesday and 8:00 to 1:00 on Thursdays.

### Article 20: Settlement

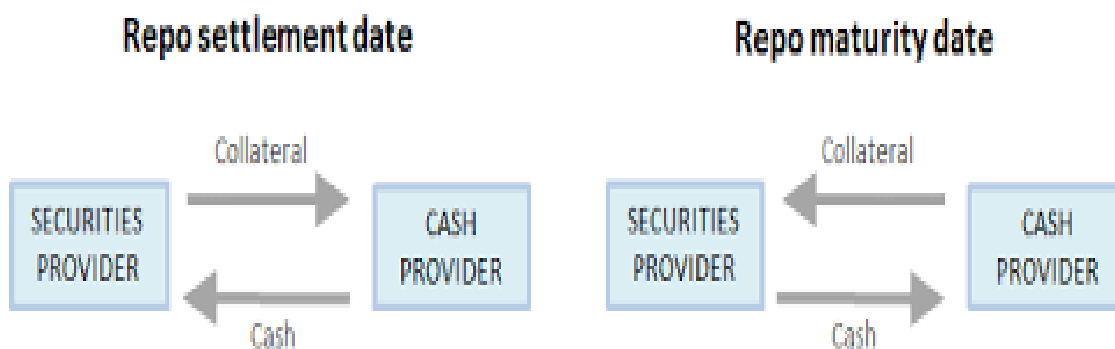
Settlement of repos will be done within normal business hours which are 08:45 hours to 16:00 hours from Saturday to Wednesday and will have a maximum of T+1 settlement period. Any transactions that are outside of this normal practice should be specified beforehand. Participants are encouraged to ensure same-day settlement. However, participants may settle outside same-day settlement arrangement and any such transactions should be specified beforehand.

### Article 21: Sudden Events Handling

Due to the occurrence of any unforeseen event or circumstances beyond the control, the Market Operation Committee will take the final decision. In case of system destruction or technical issues the manual transaction will take place.

### Article 22: Manual Transaction

- (1) Both parties send their application to DAB,
- (2) The application must be timely and in the official manner.
- (3) The application must contain the details of security taking part in the exchange.
- (4) The application must contain amount, term, repo rate, maturity date and any other Information may be requiring by DAB.
- (5) The following transaction will be generated by CSD:



### Article 23: Code of Conduct

- (1) Da Afghanistan Bank develops repo market for benefit of banking system in Afghanistan to facilitate the liquidity management for banking institution and for central bank as a tool to achieve monetary policy objective.
- (2) A properly functioning ongoing repo market for Government Security (Capital Notes), where buyers and sellers participate to accomplish their own business or investment objectives, will also help to achieve DAB's secondary objective to foster liquidity, solvency and proper functioning of a stable market based financial system. But the establishment of an efficient market is not possible without having some specific conduct rules followed in this market.
  1. **Purpose of rules:** These rules are developed to ensure integrity and honesty in repo market for government Security (Capital Notes). This will encourage liquidity, efficiency and promote public confidence in Capital Notes. Pursuant to Capital

Notes Secondary Market Regulation, every participant of Capital Note Secondary Market transaction is required to adhere to the following conduct rules for any transaction involving Capital Notes Secondary Trading.

2. **Standards of Conduct.** All participants conducting business of Government Security (capital notes) in secondary market shall observe high standards of commercial honor in the transactions of their business as per the contractual obligations. In case any default results from any of the party, DAB can impose penalty in monetary or non-monetary forms. In case the issue repeats, DAB may suspend the participant or take the extreme step of banning the offender. The participants shall prohibit any business conduct or practice which is unbecoming or detrimental to the public interest. Participants must act fairly, honestly and in good faith while entering into, executing and administering trades in repo market or secondary market.
3. **Prohibited Conduct:**
  - 1 - No participant may induce a secondary market transaction involving Capital Note by means of manipulation, deception, or fraud.
  - 2 - No participant, acting in concert with another, may engage in any conduct that directly or indirectly fixes purchase or selling price or any other trading condition.
  - 3 - No participant, acting alone or in concert with others, may engage in any other conduct that substantially prevents or lessens competition in the market.

#### **Article 24: Fees and Commissions**

- (1) Charges, if any, for services performed by a bank for an investor in connection with a secondary market transaction must be reasonable and must not unfairly discriminate between investors.
- (2) If a bank buys for its own account from an investor, or sells from its own account to an investor, the bank must buy or sell at a price that is fair, taking into consideration market conditions and the expense involved in the transaction.
- (3) If a bank acts as agent for an investor in any transaction, the bank may not charge the investor more than a fair commission or service charge, taking into consideration market conditions, the expense involved in the transaction, and the value of any service the bank may have rendered by reason of experience and knowledge of the market.

#### **Article 25: Reporting**

- (1) On a weekly basis, each securities depository must report to DAB:
  1. Its holding on behalf of investors in the form provided by DAB.
  2. All secondary market Transactions for that week as follows:
    - 1 - A transaction between banks shall be reported by the (selling bank)
    - 2 - A transaction between a bank and an investor shall be reported by the bank
    - 3 - A transaction between two investors shall be reported by the securities depository for the (seller).
- (2) The transaction report is required to be submitted in the form prescribed by DAB and shall contain the following information:
  1. The security number of the Capital Notes
  2. The par value of the Capital Note
  3. Maturity date of capital notes
  4. Transaction date
  5. Repo date
  6. Repo Rate
  7. The price of the transaction
  8. The time of execution and



9. Any other information required by the bank.

## **Chapter 5: Market Surveillance and Dispute Resolution**

### **Article 26: Market Surveillance**

- (1) DAB will carry out surveillance of the repo market to:
  1. Detect disorderly market conditions and infringements of this Regulation and other applicable rules
  2. To identify anomalous price patterns and other issue-specific developments.
- (2) To facilitate surveillance, DAB may require banks and investors to report such information regarding the repo market as DAB determines necessary or appropriate to enable DAB to conduct adequate surveillance.
- (3) Additional rules to regulation on Capital Notes Secondary Market are required to be followed by market participants:
  1. **Responsibility**

Banks shall ensure that all personnel engaged in Capital Notes trading market are properly qualified and trained and are aware of regulation for Capital Notes on Secondary Market Trading and these rules.
  2. **Confidentiality**

Banks shall ensure that dealings in the Capital Notes Secondary Market with customers and counterparties is on a confidential basis, except with express permission of the party concerned or as required by Capital Notes Secondary Market regulation or request for information by Da Afghanistan Bank.

Capital Notes Secondary Market trading participants shall not disclose, discuss, or request that others disclose or discuss, the participation of any customer or counterparty in the Capital Notes Secondary Market.

Banks shall ensure that their own trading activities are kept confidential including information with respect to customers and trading and planning strategies.
  3. **Resources and Systems**

Banks must devote adequate human, financial and operational resources to their trading activities in the Capital Notes Secondary Market.

Banks must implement operation and technological safeguards to ensure that their Capital Notes trading activities in Secondary Market can be fully supported.
  4. **Conflict of Interest**

Banks are required to avoid conflicts of interest in their dealings with customers, counterparties and the public. Such conflicts can arise in many different circumstances, but one of the underlying principles is that a fair, efficient and liquid Capital Notes Secondary Market relies in part on open and unbiased dealings by banks, and Banks fulfillment of their duties to customers before their own interests or those of their personnel.
  5. **Criminal and Regulatory Offenses**

Banks shall ensure that their trading in the Capital Notes Secondary Market does not contradict any law of Islamic Republic of Afghanistan, including without limitation, Anti Money Laundering and Combating Financing of Terrorism Laws or Da Afghanistan Bank regulations and requirements.
  6. **Clear Communication**

Banks shall use clear and unambiguous language in course of their trading activities, particularly when negotiating trades on in the secondary market.
  7. **Failure to Comply with these rules**

If a bank or investor fails to comply with any requirement of these conduct rules, DAB may:

- 1 - Suspend or withdraw authorization of the bank to act as a securities depository
- 2 - Suspend or bar the bank from conducting transactions on behalf of investors
- 3 - Suspend or bar the bank or investor from participating in auction of new issues of Capital Notes or in Secondary Market transactions.

#### **Article 27: Dispute Resolution**

- (1) The Participants agree that every effort shall be made to resolve amicably by direct negotiation, any disagreement or dispute arising between them under or in connection with these Rules.
- (2) Where attempts at direct negotiation have been unsuccessful, notification of intent to dispute must be sent to the other participant and the Overseer as well setting out a full description of the matters in dispute within 3 days of such intention arising.
- (3) Pending the resolution of the dispute, the participants will continue to perform all their obligations under these Rules.
- (4) The Chief Executive Officer of the participants must personally or through nominees attempt to resolve the dispute, on the basis that the participants wish to retain an ongoing relationship.
- (5) If the Chief Executive Officers, or their nominees, are unable to resolve any dispute within (3) days of the notice or any other time frame as the Participants may agree, then either participant may give notice to the other participant that the matter is not resolved and that participant shall refer the dispute to arbitration before a single arbitrator in accordance with the Arbitration Act of the Laws of Afghanistan or any statutory modification or re-enactment thereof for the time being in force. The decision of such arbitrator shall be final and binding on the Parties.

#### **Article 28: Reservation of Right**

- (1) Da Afghanistan Bank reserves the right to supplement or amend this regulation.
- (2) Da Afghanistan Bank further reserves the right to modify the terms and conditions of repo operation from time to time.
- (3) Notice of any such changes will be provided through electronic communication or by circulars to the participants.

#### **Article 29: Master Re-purchase Agreement**

- (1) Secondary market deals between commercial banks shall be governed by a Master Re-purchase Agreement.
- (2) For the purposes of Paragraph 1 of this Article, such agreement shall be prepared by the Afghanistan Banks Association and approved by Da Afghanistan Bank.
- (3) Da Afghanistan Bank shall determine the time for applicability of the master repurchase agreement, when it deems necessary.

#### **Article 30: Enforcement**

This regulation is effective immediately after adoption by the Supreme Council of Da Afghanistan Bank.