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# Information for private investors

January 2015

## ORB

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### Accrued interest on conventional and index-linked gilts

#### Introduction

This guide provides additional information on accrued interest for private investors wishing to trade gilts on London Stock Exchange's electronic Order book for Retail Bonds (ORB). It provides summary information on the various calculation methods for both conventional and index-linked gilts and gives worked examples.

This factsheet may serve as a companion to the brochure *Trading Bonds on London Stock Exchange - A Guide for Private Investors*, which gives an overview of the various types of bonds available in addition to introductory information on bond pricing and yields. This factsheet should be read in conjunction with *Accrued Interest - A Guide for Private Investors*, which provides summary information and worked examples of the various calculation methods for corporate bonds as well as simple calculations for conventional gilts.

#### Gilts day count convention

For all gilts, the standard day count convention is ACT/ACT. This means that the calculation for accrued interest takes the actual number of days on which the seller has accrued interest (the period between the previous coupon date and the settlement date of the bond trade) and divides this by the actual number of days in the interest period to determine which proportion of the coupon amount should accrue to the bond seller.

#### Conventional gilts

For conventional gilts, a fixed coupon is paid throughout the lifetime of the security and the full nominal principal amount invested is returned to the gilt holder at maturity.

Accrued interest for conventional gilts is calculated as follows:

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$$\text{Accrued Interest} = \frac{\text{actual days between previous coupon and settlement date}}{\text{actual days in coupon period}} \times \frac{\text{coupon amount}}{2}$$

The coupon amount in the formula above is divided by 2 because coupon payments on gilts are made semi-annually. The relevant amount when calculating the accrued interest is therefore the amount paid for six months and not the annual interest rate.



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Stock Exchange Group

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## Accrued Interest on conventional gilts (standard dividend period)

### ORB identifiers

Name: Treasury 5% 2025

TIDM: TR25

ISIN: GB0030880693

Coupon dates: 7 March and 7 September

Annual Coupon: 5%

Trade Date: 13 April 2015 (T+1 settlement on 14 April 2015)

Clean Price: 129.21

Accrued Interest =  $\frac{38 \text{ (period between 7 Mar 2015 and 14 Apr 2015)}}{184 \text{ (period between 7 Mar and 7 Sep 2015)}} \times \frac{5}{2}$

= 0.5163

Dirty price = 129.7263 (clean price + accrued interest)

## Index-linked gilts

Unlike conventional gilts which pay a fixed coupon throughout their lifetime and which return a fixed principal amount at maturity, coupon and principal payments for index-linked gilts are adjusted in line with inflation. These adjustments are made using the Retail Price Index (RPI).

There are two types of index-linked gilts which have slightly different calculation methods for adjusting coupon payments and therefore for determining accrued interest. All the new index-linked gilts issued after September 2005 use the three-month indexation lag structure as opposed to the eight-month lag methodology used for index-linked gilts issued before that date.

### 8-month indexation lag gilts

Inflation adjustments to the coupon payments of index-linked gilts with an 8-month lag are made based on the level of the RPI eight months prior to the issue of the gilt (the 'base RPI') and the level of the RPI eight months prior to the relevant coupon payment date (the 'reference RPI').

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## Standard coupon payment on index-linked gilts (8-month indexation lag) (standard dividend period)

### ORB identifiers

Name: TREASURY 2 1/2% IL TREASURY 16

TIDM: TR16

ISIN: GB0009075325

Standard coupon dates: 26 January and 26 July

Issue date: 19 January 1983

Annual Coupon: 2½%

Next Coupon date: 26 January 2015

Base RPI: 81.622306717364 (May 1982)

Reference RPI: 257.7 (October 2014)

$$\text{Coupon payment per } \pounds 100 \text{ nominal} = \frac{257.7}{81.6223} \times \frac{2.5}{2}$$

$$= 3.9465 \text{ (rounded down to 4 decimal places)}$$

Similarly, when calculating accrued interest for index-linked gilts, this ratio of base RPI to reference RPI is also included in the standard accrued interest formula.

## Accrued interest on index-linked gilts (8-month indexation lag)

Trade Date: 13 April 2015 (T+1 settlement on 14 April 2015)

Clean Price: 329.61

$$\text{Accrued Interest} = \frac{78 \text{ (period between 26 Jan 2015 and 14 Apr 2015)}}{181 \text{ (period between 26 Jan and 26 Jul 2015)}} \times \left[ \frac{2.5}{2} \times \frac{257.7}{81.6223} \right]$$

$$= 1.7001$$

Dirty price = 331.3107

## 3-month indexation lag gilts

Since September 2005, all new index-linked gilts are issued with a 3-month indexation lag rather than the 8-month lag detailed above. Coupon payments are adjusted based on the ratio of base RPI three months before the gilt's issue to the reference RPI three months before the coupon payment date, however these RPI values are calculated for each day in the month (rather than a single RPI value being applied for a whole calendar month) based on a linear interpolation between the RPI two months before and the RPI three months before the relevant date. Index ratios are calculated and published for each day.

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## Accrued Interest on Index-linked Gilt (3-month indexation lag) (standard dividend period)

### ORB identifiers

Name: TREASURY 1 1/4% IL TREASURY 22/11/27

TIDM: T27

ISIN: GB00B128DH60

Standard coupon dates: 22 May and 22 November

Issue date: 26 April 2006

Annual Coupon: 1¼%

Next Coupon date: 22 November 2014

Base RPI: 194.07

Reference RPI: 257

Index factor = 1.3243

Trade Date: 4 August 2014 (T+1 settlement on 5 August 2014)

Clean Price: 120

Accrued = 75 (period between 22 May 2014 and 5 Aug 2014) x  $\left[ \frac{1.25}{2} \times 1.3243 \right]$   
Interest 184 (period between 22 May 2014 and 22 Nov 2014)

= 0.3374

Dirty price = 120.3374

## Further information

For further information, please contact the Fixed Income team+44(0)20 7797 3921

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