



Improving governance in public debt management

Public Debt Management Law: Recent Experience

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Competent Authority & Legislation in force

Public Debt Management functions were transferred from the Central Bank of Cyprus (CBC) to the Ministry of Finance (MoF) in August 2010;

The Public Debt Management Office (PDMO) was established by an internal administrative decision as a Division within the MoF.

Laws & Regulations for the issuance of Government Bonds (CGB) and Treasury Bills (TB):

- Legal powers for issuing CGB & TB: the Cabinet (Council of Ministers);
- Legal powers for deciding the terms of CGB & TB: the Minister of Finance;
- No legislation for the regulation of PDM functions or for the establishment of a PDM Office;

* European Central Bank (ECB) Opinion [14 May 2010 (CON/2010/39)]: i.a. ... Keep a clear distinction between PDM Policy and Fiscal Policy i.e. do not use Public Debt Management Policy (PDMP) as an instrument of Fiscal Policy.



The fallacy of using PDMP as a Fiscal Policy tool (1/3)

Sovereign issuers can use PDMP in such a way so as to reduce fiscal expenditure and increase revenue;

In doing so, countries may fatally ignore the fundamental objectives of PDMP;

Some examples include:



The fallacy of using PDMP as a Fiscal Policy tool (2/3)

Action	Temporary Outcome	Medium-term risk
Increase the share of short-term public debt	may reduce borrowing cost	but increase refinancing and interest rate risk
Increase the share of foreign currency and variable interest rate loans	may reduce borrowing cost	but increase FX & IR risk
Engage in speculative borrowing operations by raising funding in foreign currency (without hedging/ FX Swaps) in anticipation of FX favourable movements (thus FX profit)	chance to increase revenue	but possibility to suffer a FX disaster



The fallacy of using PDMP as a Fiscal Policy tool (3/3)

Action	Temporary Outcome	Medium-term risk
Borrow excessively short-term funds from the international money markets at low interest rates and then deposit them with banking institutions in specific segments of the market that pay higher interest rates (before 31 st Dec. let them expire so that one can avoid an increase in the public debt statistics)	may once-off increase fiscal revenue	but increased exposure in high counter-party & market risk/plus failure in achieving the necessary structural-fiscal adjustment/ <u>risk fiscal sustainability</u>
Eliminate buffer stock, sinking funds and any strategic funds	temporarily reduce public debt & fiscal expenditure (cost of servicing the PD)	in the medium term increase exposure to market, liquidity, political and natural disaster risk at unacceptable levels
Exert political pressures on SOE to participate in the financing of the government at lower interest rates than market rates	temporarily reduce fiscal expenditure (cost of servicing the PD)	in the medium term increase exposure to market, liquidity, political and natural disaster risk at unacceptable levels.

Practical interim measures taken by the PDMO/ MoF for the reduction of the risks



Transparency (as an early warning system)

- A separate PDMO web-site was immediately constructed;
- All borrowing and cash management transactions are timely posted on the web-site;
- An annual PDM report is prepared and submitted voluntarily to the Parliament and to the Auditor-General;
- Quarterly PDM reports are posted on the web-site;

Relationship with markets and institutions

- An open and transparent policy esp. regarding the flow of information to national, EU and international institutions is followed;
- The relationship and the cooperation with CRAs has been re-enforced;
- Reasonable access to the financial media has been provided;
- Unlimited access for existing institutional investors has been safeguarded;

Institutional framework & infrastructure

... and most important!: - TA from the World Bank was requested.



World Bank Technical Assistance (TA)

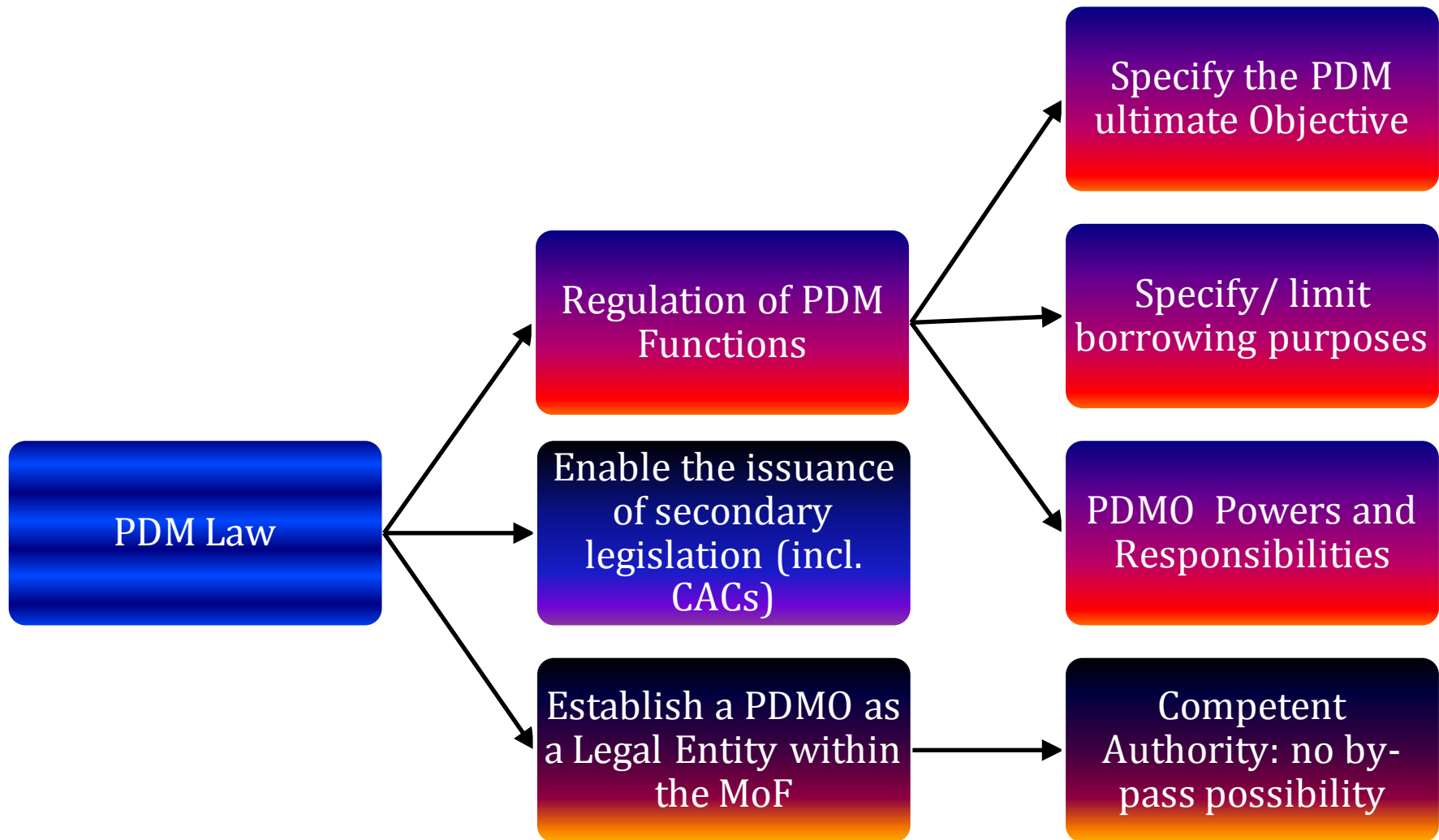
Under one of our contracts, the WB provided TA for the drafting of the PDM legal framework:

➤ *The new law would strengthen **accountability**, by ensuring that PDM **objectives** are clear and that borrowing strategies are developed and implemented in line with **sound practices**;*

Within this context, the mandate included:

➤ *the establishment of a PDMO within the MoF, but with a certain degree of independence, empowered to formulate and implement PDMP.*

The building blocks of the new PDM Law



Division of Powers & Responsibilities between Political and Technocratic Levels



	<u>Before PDM</u>	<u>Law</u>		<u>After PDM</u>	<u>Law</u>
<u>Powers & Responsibilities</u>	<u>Minister/ Cabinet</u>	<u>PDMO</u>		<u>Minister/ Cabinet</u>	<u>PDMO</u>
Medium-Term Strategy Proposal	-	-		-	√
Medium-Term Strategy Approval	-	-		√	-
Annual Borrowing Plan Proposal	-	-		-	√
Annual Borrowing Plan Approval	-	-		√	-
Borrowing purpose specified by Law	√	-		-	-
Ad hoc decisions for issuance of Gov Securities	√	-		-	-
Ad hoc decisions for the terms of Gov Securities	√	-		-	√
Liquidity Buffer Stock Proposal	-	-		-	√
Liquidity Buffer Stock Decision	√	-		√	-
Risk assessment of Gov Guarantees	-	-		-	√
Decision on Gov Guarantees	√	-		√	-
Opinion for the amendment of the Law	-	-		-	√
Authorization of transaction officers	√	-		-	√
Preparation of PDM Reports	-	-		-	√



Main decision-making powers of the PDMO (1/2)

Considerable decision-making powers for the Head of the PDMO, such as:

- to *accept or reject bids* submitted in an auction in accordance with an approved auction calendar;
- to *determine the terms and conditions* of the auctions in government securities (provided it is part of the approved borrowing plan);
- to *issue and determine the terms and conditions* of any cash management bills;
- To *negotiate and determine the terms* of the loans;
- to *enter into financial swaps* and other derivative transactions (within operational guidelines);



Main decision-making powers of the PDMO (2/2)

- to *offer buybacks* and switches of central government debt securities, and invest any surplus cash in the market (in accordance with the investment policy);
- to *manage any sinking funds* on behalf of the Government;
- to *assess the financial risk* of government guarantees; and
- to *act as the liaison* between the Ministry of Finance and the *Credit Rating Agencies*.





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THANK YOU FOR YOUR ATTENTION!

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