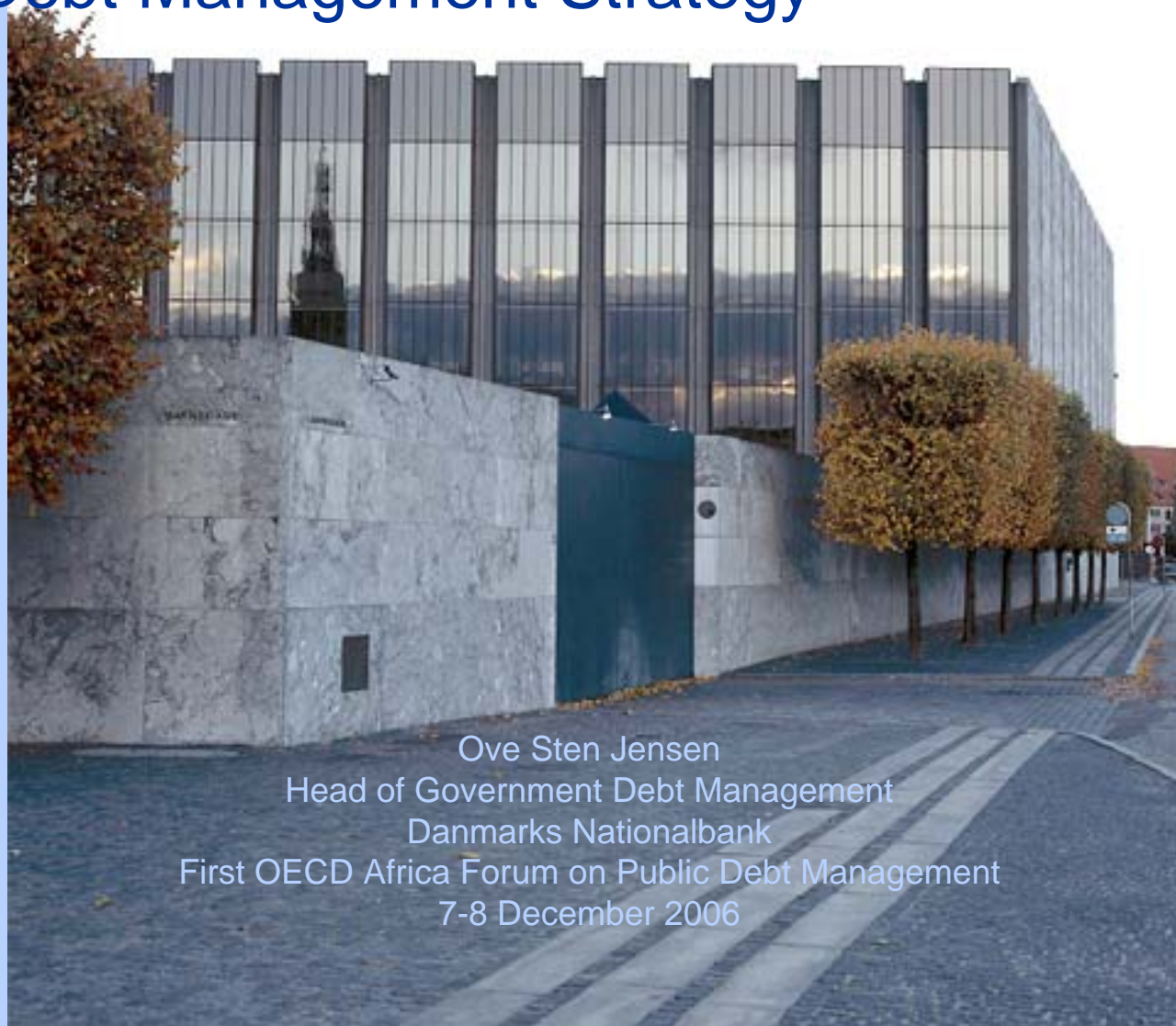
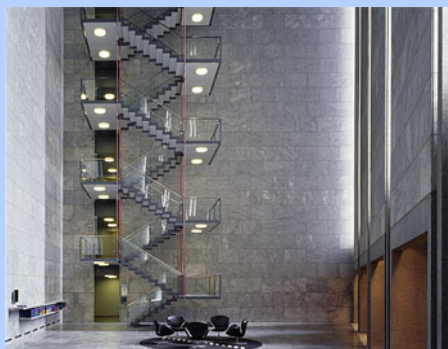




# Development, Formulation and Implementation of Debt Management Strategy



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# The Objective of Government Debt Management Policy

In OECD countries primary objectives:

- To cover the central government financing requirement at the lowest possible long-term borrowing costs, subject to a prudent degree of risk (cost-risk trade off).

Secondary objectives:

- Develop domestic financial markets (money and capital market)
- Access to capital market (refinancing risk).

Relevance for emerging markets:

- Developing markets and financial infrastructure vs. Cost-risk trade-off models
- Time horizon for objectives and strategy setting is long-term (eg. 10 years).



# Institutional Framework for the Debt Management Strategy

## Separation fiscal and monetary policy

- Central bank vs. MOF/DMO
- Funding rules for financing the government
  - i) no monetary financing
  - ii) funding rules ("the norm" for domestic and foreign borrowing/exposure)
- Coordination of policy and positive spill-overs (T-Bill market).

## Relationship between MOF and DMO

- Overall political decisions vs. debt management
- In Denmark quarterly meetings with written conclusions
- Need for a consistent strategy for the whole debt (not a partial approach) => What is the mandate of the DMO?



# The Debt Portfolio

Evolving treasury functions (in OECD a trend towards ALM approach).

## Debt Portfolio:

- Domestic debt (develop domestic market)
- Foreign debt (foreign exchange reserves)
- Cash management (government account)
- Asset portfolios (ALM approach)
- Other government exposures (Forex-, interest rate exposures).

Important in strategy to have a consistent and full scale approach (debt from different agencies, guarantees).



# Instruments in Debt Portfolio

## Some principles:

- Important to have marketable papers
- Domestic bonds vs. foreign bonds
- Debt instruments and the risks involved should be understood (structured products?).

## Debt instruments in OECD-countries

- T-Bills and nominal bonds (benchmarks 2, 5 and 10 years, some countries longer bonds)
- ILB's especially for the bigger issuers
- Interest and currency swaps (separation between funding and risk management policy).



# Primary and Secondary Market

## Some principles in the debt management:

- Predictable ("no surprises")
- Transparency (strategy announced to the public)
- Liquidity
- Trade-off between predictable policy and transparency?

## Primary Market:

- Auctions/syndications (in Denmark also electronic tap issuance)
- Role of primary dealers.

## Secondary Market:

- Market making (quoting obligations)
- Electronic market vs. OTC market.



# Debt Management Strategy for 2007 (the Danish Case)

Strategy is decided in December at meeting between DMO and MOF (based on papers from DMO).

## December meeting

- Follow up on strategy 2006 (evaluation of strategies)
- Strategy for 2007 in a longer-term perspective (10 years).

Strategy is announced to the public (strategic benchmarks)

- Papers for issuance and benchmarks
- Buy back policy
- Securities lending facilities
- Market risk (duration targets).



# The Formulation of the Debt Management Strategy

Split between funding and risk management policy.

Political focus (MOF) on the trade-off between costs and risks.

Elements used by the DMO in the formulation of the debt management strategy:

- Medium term analysis (10 years)
- Scenario analysis (funding requirements, debt instruments, buy back, swaps) => analysis ensure consistency in policy
- Cost-at-Risk analysis (simulation model) => duration/interest rate fixing
- Stress-tests (budget changes etc.).

Results of analysis is strategic benchmarks:

- Funding policy (debt instruments, liquidity requirements)
- Market risk (duration, interest rate fixing).



# Implementation and Adjustment of Debt Management Strategy

- Strategy is implemented by the DMO
- DMO has flexibility in strategy
- Major adjustments in policy discussed at quarterly meeting with MOF
- New information/adjustments communicated to the public
- Transparency and credibility



# Some Conclusions

- The strategy based on debt management objectives
- Strategy is determined in a medium term perspective
- Broader functions for DMOs
- Debt management strategy:
  - Funding policy
  - Cost-risk trade-off