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RECENT DEVELOPMENTS IN GOVERNMENT SECURITIES MARKET (TANZANIA)

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Recent Developments in Government Securities Market (Tanzania)

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Contents

- Introduction
- Market Developments
- Implication of the Global Financial Crisis
- Cost sharing framework
- Alternative Short Term Papers
- Conclusion

INTRODUCTION

- ⌚ Domestic Financial Markets in Tanzania are still at a nascent stage, secondary market trading in Government Securities is not vibrant. This retards price discovery.
- ⌚ Lack of electronic connectivity between the domestic debt data base at the Bank of Tanzania with the debt database at the Ministry of Finance
- ⌚ Treasury bills are used largely for liquidity management and implementation of monetary policy

Rationale for introducing Treasury bills

- ⌚ Establish a reference point for interest rates and spearhead development of secondary market.
- ⌚ A vehicle for sterilising excess liquidity in the economy.
- ⌚ Non-inflationary mechanism.

∞ Maturities include 35, 91, 182 and 364 day bill

∞ Weekly competitive multiple pricing (Dutch) auctions

Advantages

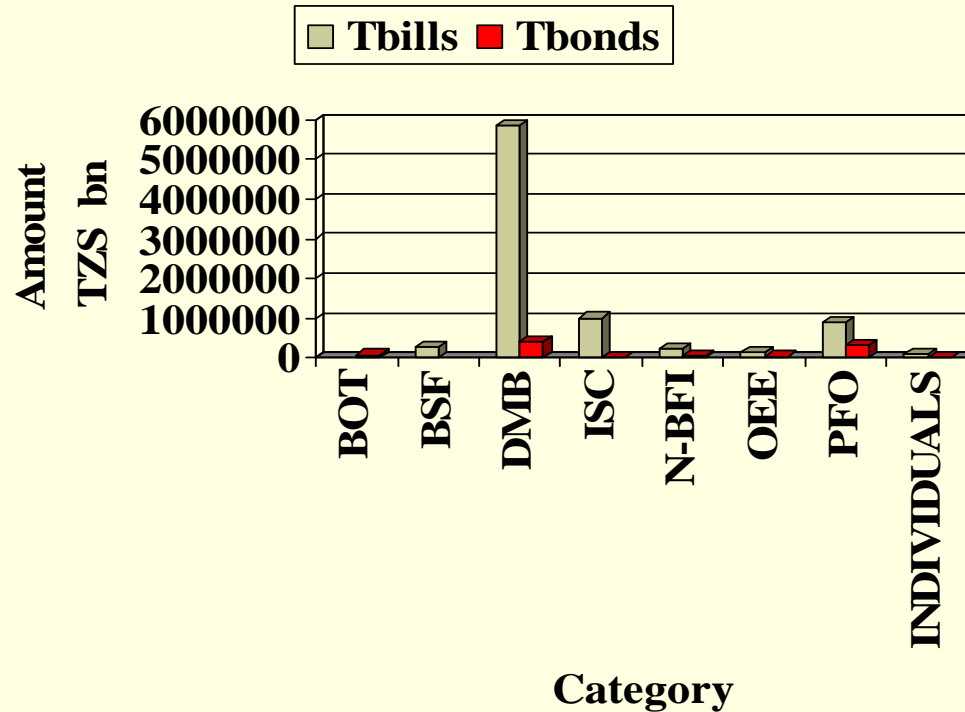
- Secure
- Transferable and Negotiable
- Pledged as collateral
- Return is competitive

MARKET DEVELOPMENTS

- ⌚ In Jan 2008, auction frequency of T-bills & bonds was changed from weekly to fortnightly and once every month respectively.
 - Increase competition
 - Stimulate secondary market trading
- ⌚ Settlement cycle changed from T+ 2 to T+1
 - To enhance efficiency in liquidity management by matching settlement and redemption

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- ⌚ Enhancement of BOT Central Depository System (CDS) in progress and program to establish national CDS initiated
 - ⌚ Preparations for benchmark bond program are in progress
 - ⌚ Country rating program in progress
 - ⌚ Offshore sovereign bond issuance under consideration

Participants in the Market (2005-2008)



Key

- BOT: Bank of Tanzania
- BSF: Bank of Tanzania Special Funds
- DMB: Deposit Money Banks
- ISC: Insurance Companies
- N-BFI: Non-Bank Financial Institutions
- OEE: Other Official Entities
- PFO: Pension Funds

IMPACT OF GLOBAL FINANCIAL CRISIS

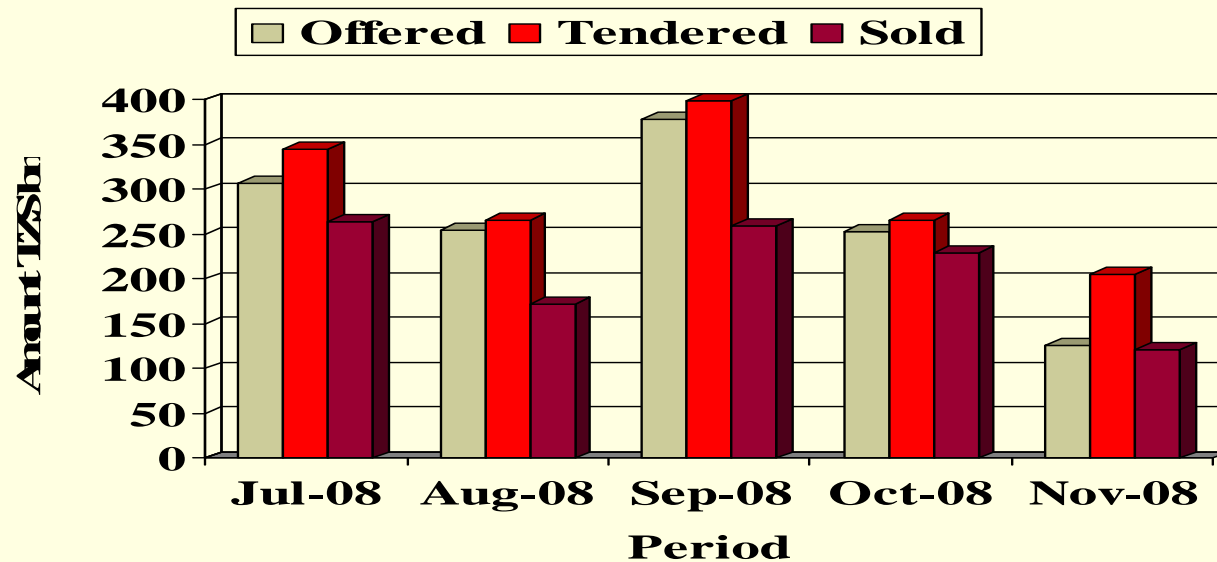
- Impact on Tanzania
 - So far limited impact on TZ's financial markets due to existing restrictions on capital account transactions, more so for short-term capital movement
 - Banks and other financial institutions are less involved in the highly sophisticated financial transactions and products.

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- Impact likely on the country's real economy, as exports, investment and plans of companies would be affected by the troubled world economy.
 - Foreign aid may to be scaled down next year if the crisis persists.

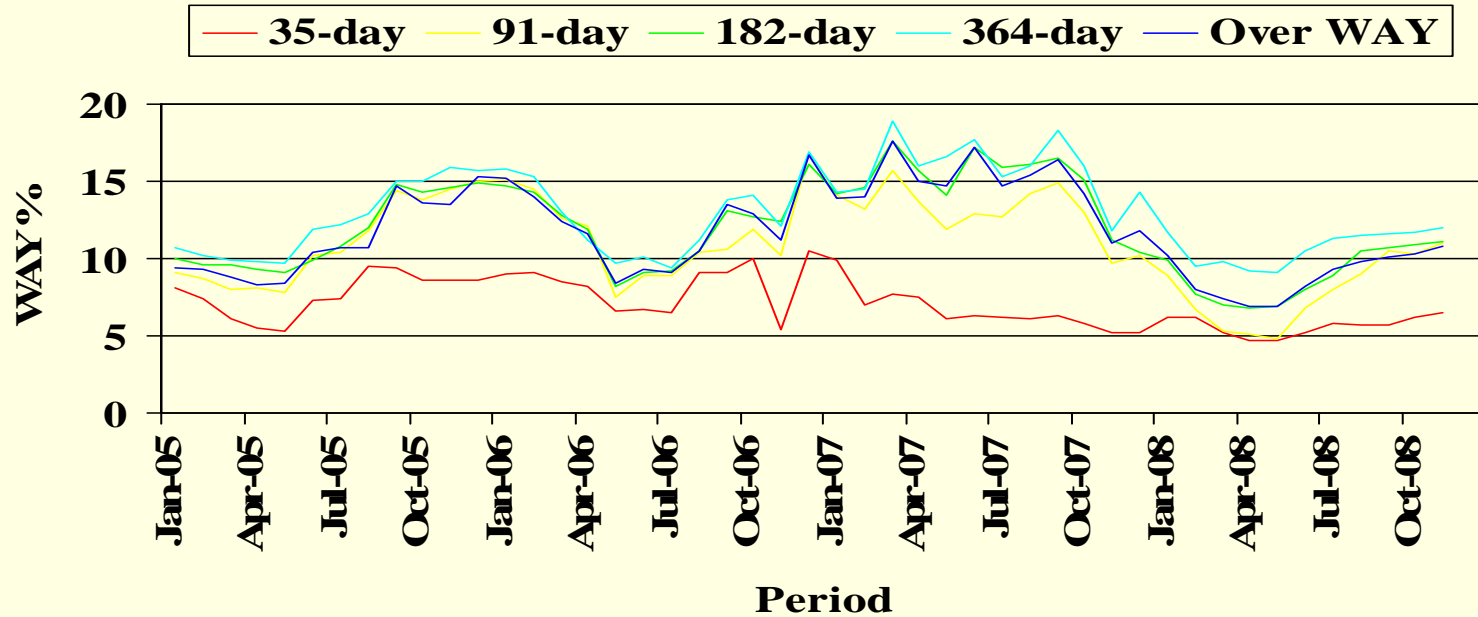
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- ⌚ Jan-May 2008 yield on T-bills plummeted , partly to change in the frequency of auctions
 - ⌚ A turnaround in the performance of T-bills beginning June 2008, led to a rise in yields
 - Seasonality: May-Sept, banks reduce participation in T-bills market in order to meet corporate borrowers strong demand for loans to purchase export crops

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- More money in circulation during harvest season
 - Relatively high and rising inflation
 - Issuance of NMB IPO
 - Increased loan syndications

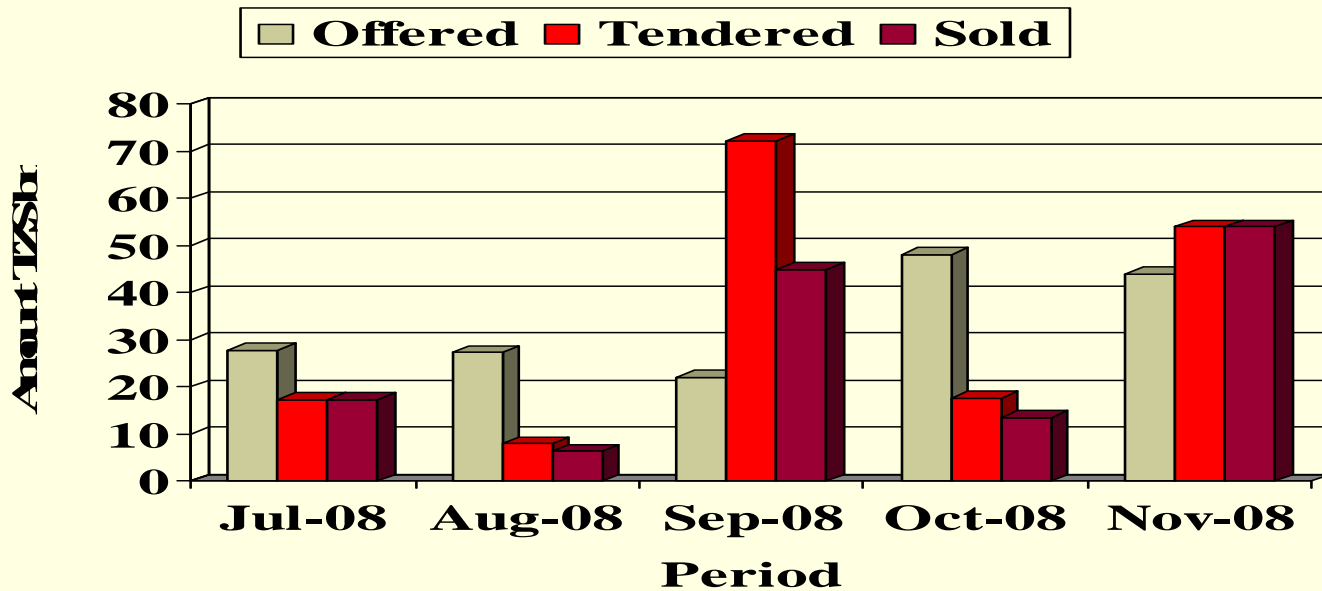
Treasury bills Performance from July- November 2008



Treasury bills yields



Treasury bonds Performance from July-November 2008

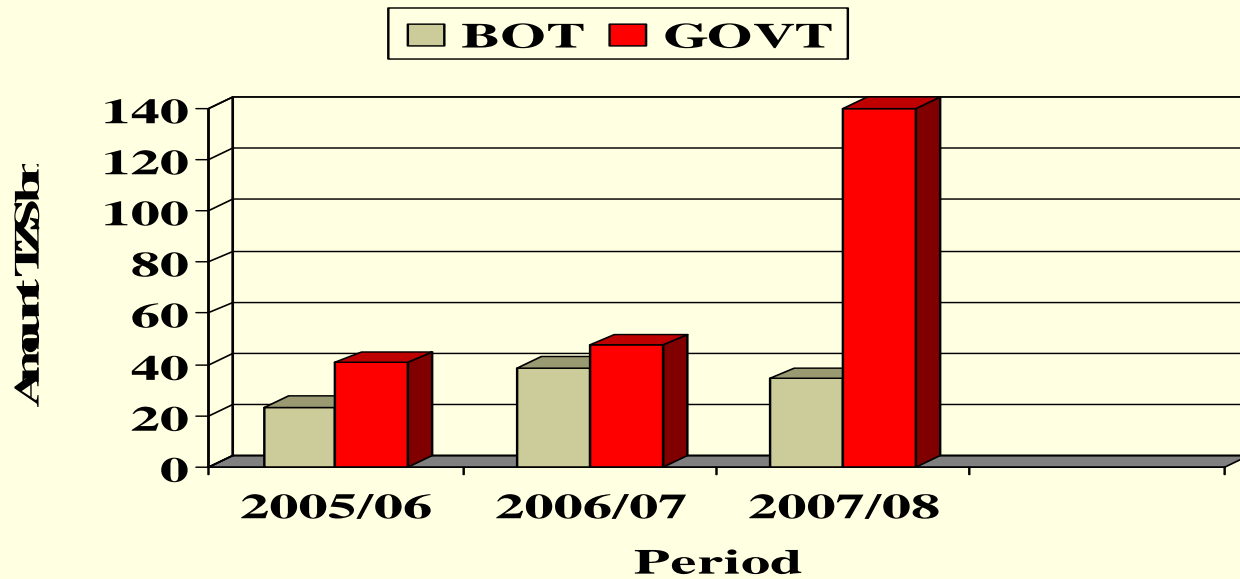


Implications of an increase rise in the Use of Treasury bills

- As volumes of Treasury bills increase the cost of redemptions also goes up.
- Refinancing risk becomes a challenge.
- In the past, the Bank used to meet the cost on short term paper used for monetary policy implementation, while, the government met the cost of short term paper used in financing its budget requirements.

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- Currently, the Bank and the government have agreed on a framework of sharing the cost.
 - The Bank's share of the cost is limited to 15% of its annual income.
 - Going forward, an MOU has been prepared whereby obligations of each party are spelt out and a formula for cost sharing has been agreed upon.

Liquidity management cost sharing



Alternative Short term paper

- In order to complement the Treasury bills, the Bank intends to introduce alternative short term papers e.g. Term Deposit Auction (TAD), Certificates of Deposit, Commercial papers and continue with sales of foreign exchange.

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- Term auction Deposit (TAD) is a money market instrument for managing liquidity.
 - Term deposits are obtained through an auction system run for a predetermined term at fixed or variable interest rate.

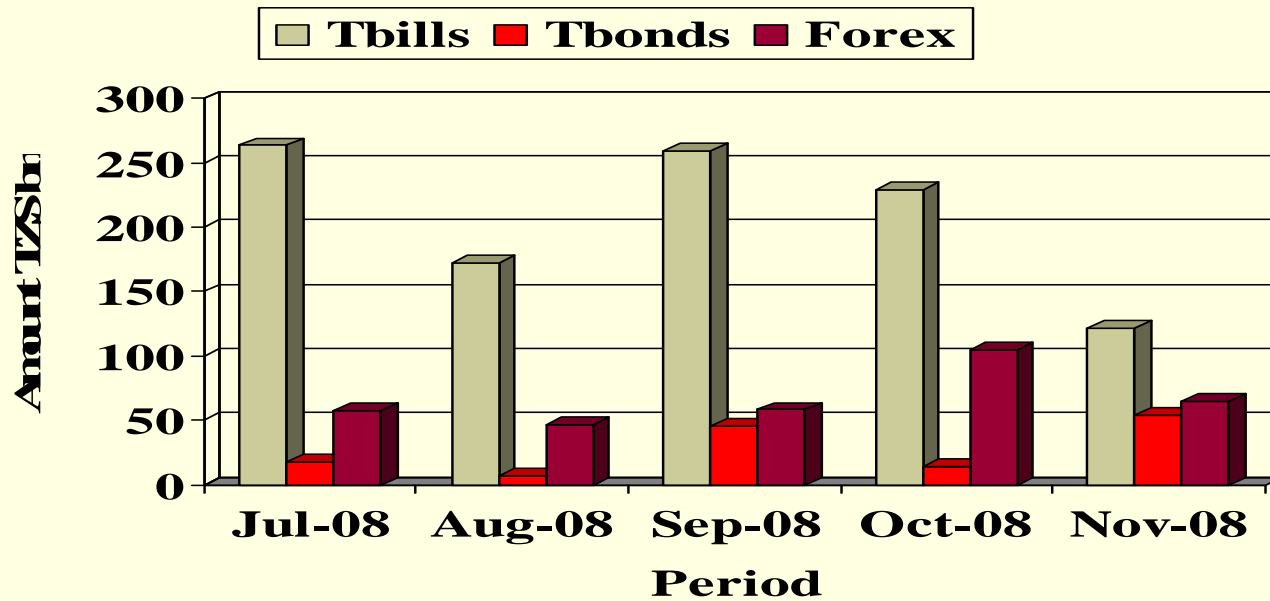
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- Tenure to be determined by the Bank but in most cases it ranges from 3 days to a few years.
 - From the perspective of the central bank, the money is unavailable for the investors until the term has ended, although features like call and put options can shorten the maturity.
 - On the side of banks this facility allows them to invest their excess liquidity and earn a competitive return.

Features of Term Auction Deposit

- Eligible bidders: All banks in Tanzania.
- Auction Type: Competitive auction bidding system based on interest rate.
- Tenure: Flexible, ranging from 15 to 180 days
- Frequency of issuance: As and When determined by the Bank.
- Announcement of offer: OMO dealing procedures apply, amount and tenure determined by the Bank.

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- Submission of bids: OMO dealing procedures apply, i.e. Telephone, posting on Reuters dealing screen, manual submission through fax or work in.
 - Minimum bid threshold: TZS 500 million, TZS 100 million for late bids
 - Time of auction: 1100 hrs, late deposit set at 100 basis points below the day's weighted average TAD rate
 - Auction results: 1300 hrs, OMO dealing procedures apply, including posting of results on BOT website.

Sale of Foreign Exchange



Conclusion

- The financial crisis is a wake up call to the region
 - Banks and other financial institutions should strengthen the management of their portfolios, take more prudent strategy in foreign currency – denominated investment products
 - Focus on areas of vulnerability associated with surges in capital flows
 - Currency and maturity mismatch in balance sheets

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- Credit and asset bubbles and excessive investment in property and other sectors
 - Unsustainable currency appreciations and external deficits
 - Cushion against a sudden reversal of capital flows
 - The Bank is monitoring risk vigilantly, investment decision in favour of:
 - Safety, Liquidity & Return** remain on focus
 - Reducing exposures, moving away from deposits in favour of sovereign securities

“THANK YOU”