AIST – French Treasury Agency
AIST Thematic Seminar

THE ROLE OF TREASURY SERVICES IN THE MANAGEMENT OF PUBLIC DEBT

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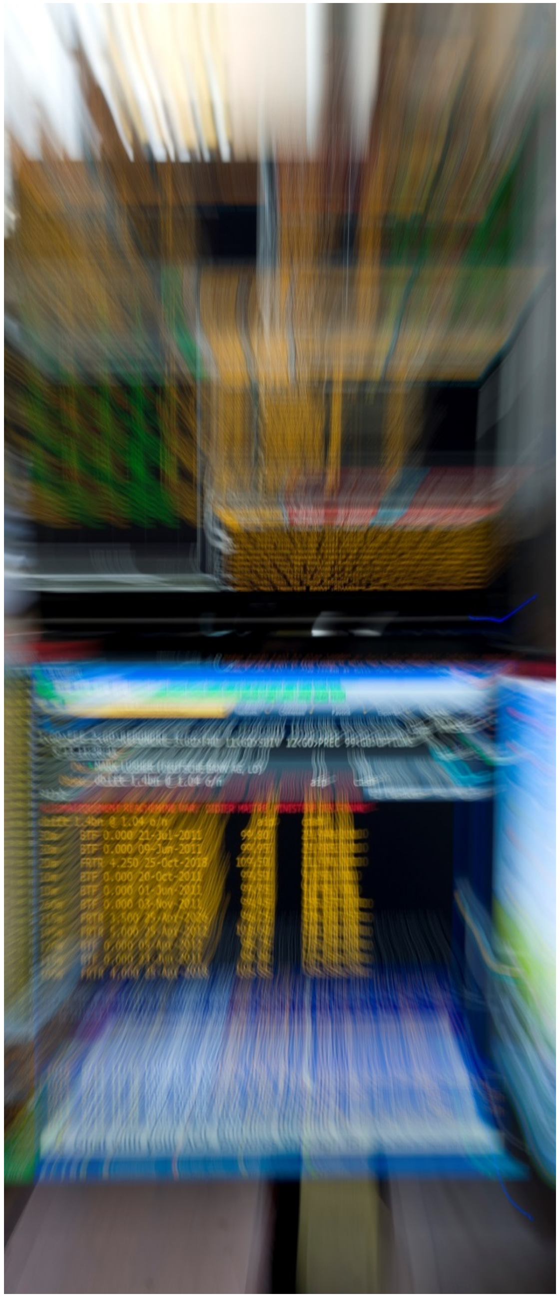


CHARACTERISTICS OF EMERGING FINANCIAL MARKETS

1) Observations:

- Small markets
- Illiquid markets

2) Benefits of developing these markets:

- Better management of public finance

- Efficiency gains

1) Stimulating local spending
2) Improving the balance of payments' account
3) Greater efficiency of monetary policy
4) Improving States' cash management
5) Better counterparty risk-sharing
6) Lower foreign exchange rate risk

DEVELOPMENT STAGES

1) Reducing non-negotiable debt to the profit of negotiable debt

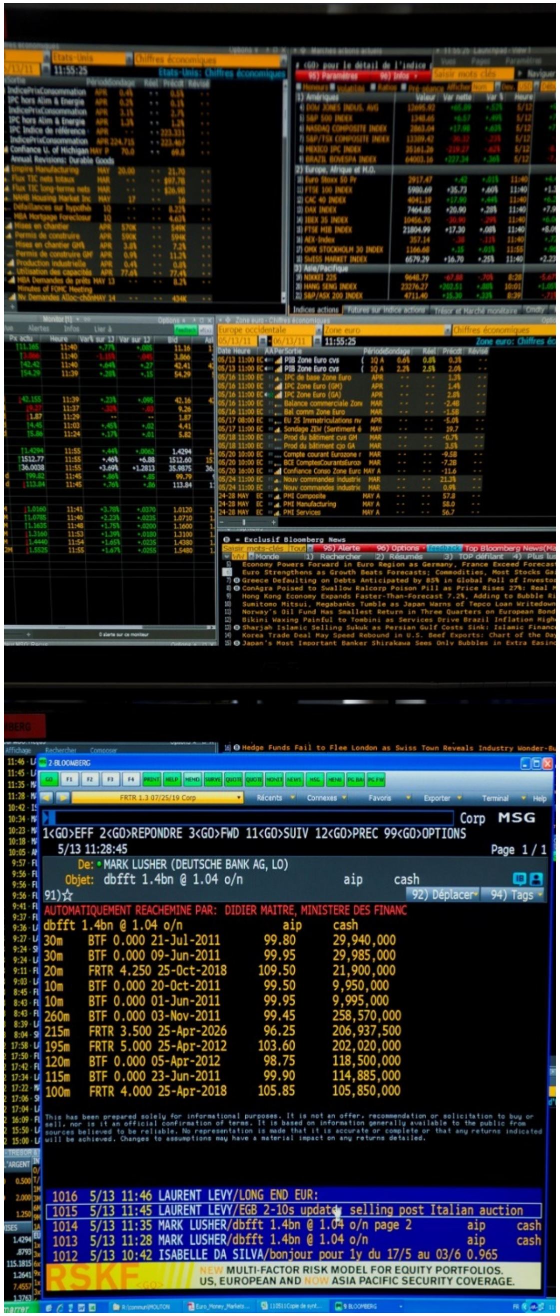
2) Dematerializing transferable securities

3) De-compartmentalization and capital market reform
   → Single capital market

4) Organizing the primary market

5) Developing the secondary market
   → A **deep** market
   → A **liquid** market

6) Setting up a group of partners to the Treasury to manage the primary and secondary markets of public debt



REFORM OF THE POLICY ON THE ISSUE OF PUBLIC DEBT IN FRANCE

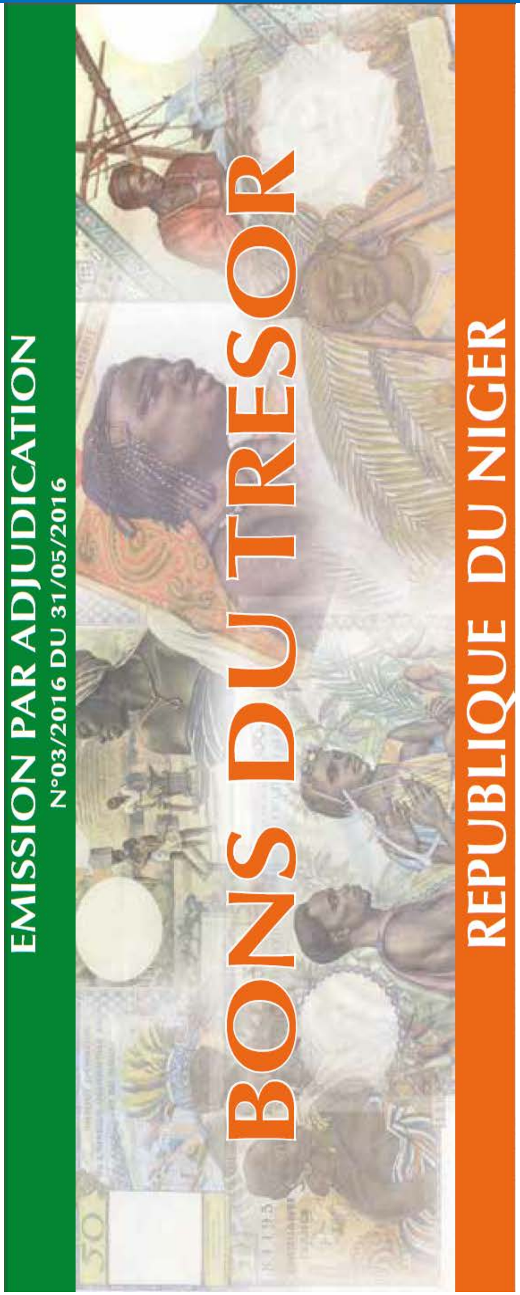
<u>Four series of measures</u>:

1) Opening and modernizing the market of Treasury bills

2) Normalizing the State’s tenders on the monetary market

3) Creation of the first two contracts on the financial futures market (“MATIF” in French), bearing upon a ten-year notional State contract and on three-month Treasury bills

4) Establishing a network of permanent correspondents to the Ministry of Finance, called Specialists in Treasury Values (STV)



NECESSARY CONDITIONS TO DEVELOP A PERFORMING MARKET

1) <u>Regulation of the securities market</u>:

Legal framework regulating the securities market

Regulatory framework for a rigorous control

Communication of the data by the financial sector

2) <u>Market infrastructure</u>:

Organizing transactions and settlement/delivery

Developing a system of market makers

Lift any regulatory tax-related obstacle

Increase liquidity with repurchase agreements and futures contracts

3) <u>Strengthen demand for government securities</u>:

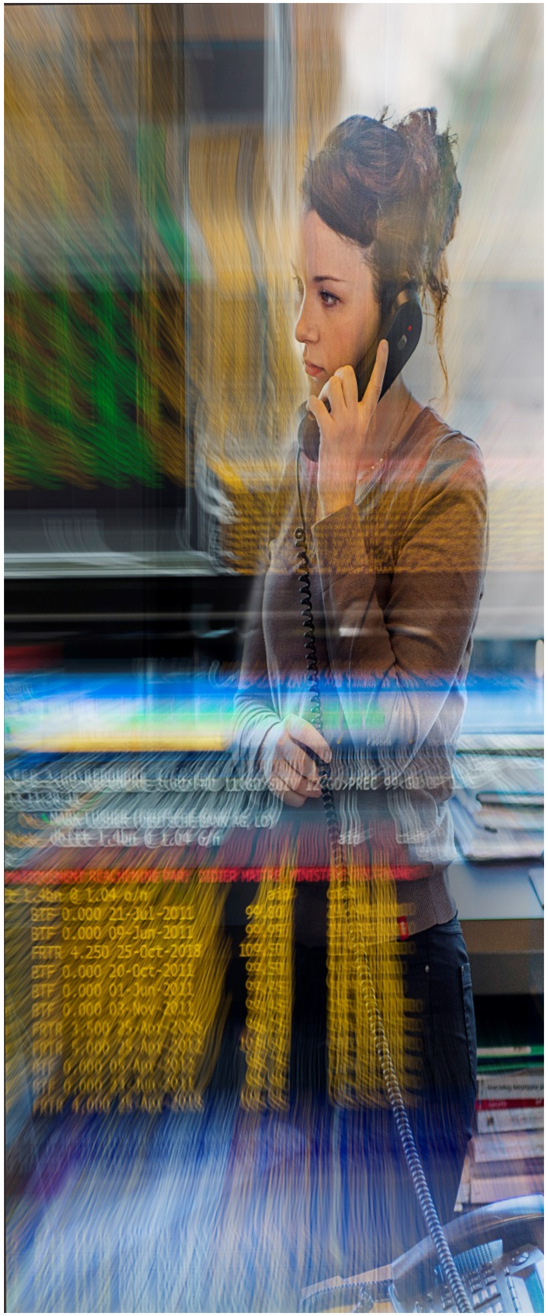
Encourage the development of institutional investors

Participation of foreign investors

4) <u>Increase the supply of government securities</u>:

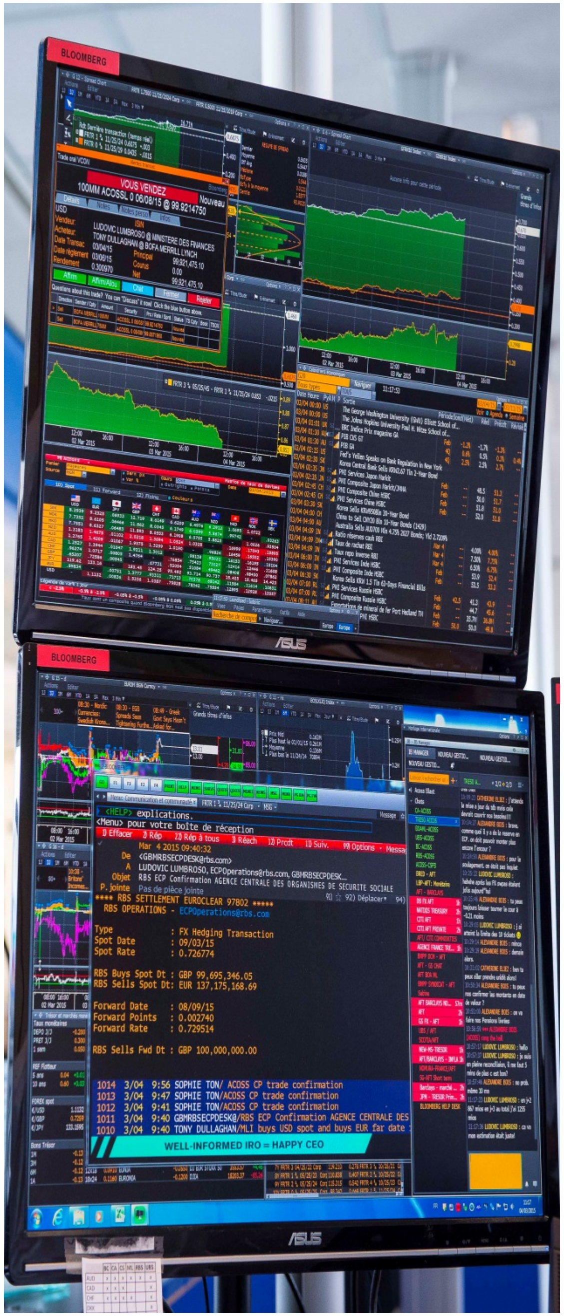
Predictable and transparent debt management

Creating normalized securities with safe distribution mechanisms (tender, syndication)



DIFFERENT WAYS OF ISSUING DEBT

1) TENDER
2) SYNDICATION OR UNDERWRITING
3) PUBLIC OFFERING
4) « TAP »
5) ISSUING ON THE STOCK EXCHANGE
6) NEGOTIATED SUBSCRIPTION BY A SINGLE LENDER
7) PRIVATE PLACEMENTS
8) EXCHANGE PROCEDURES



TECHNIQUES TO TENDER

Advantages of tender:

1) Method which became predominant on all markets

2) Allowing for near-perfect competition

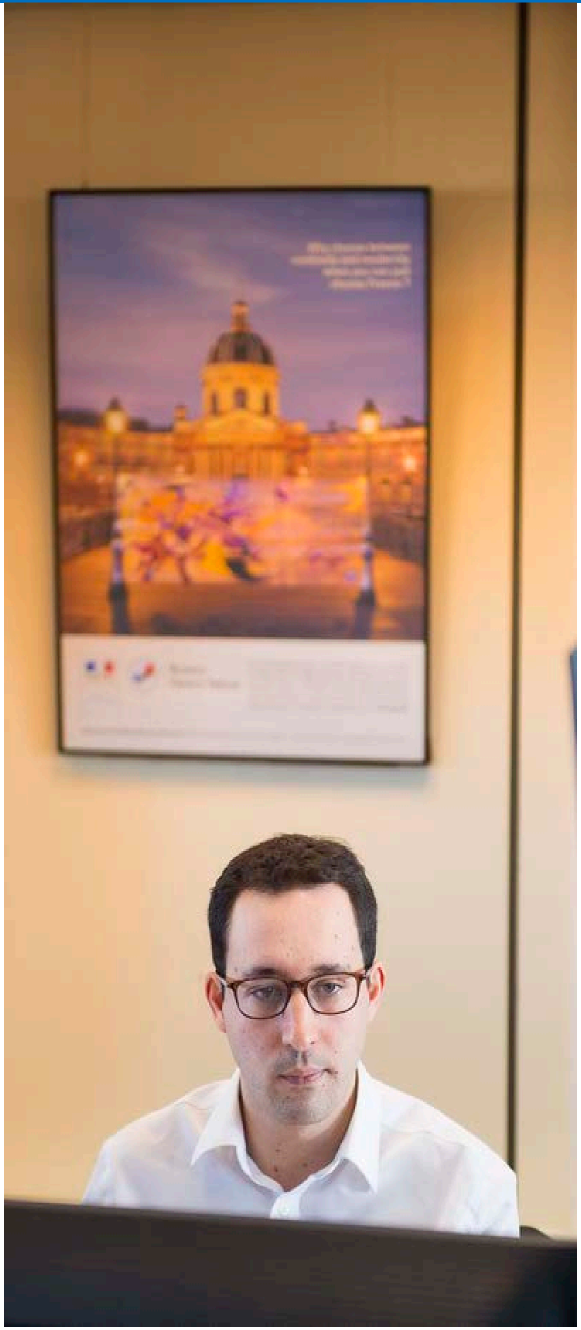
3) This method guarantees government debt issuance at least cost

4) The Treasury is no longer obliged to pay commissions to tenderers

5) It allows for time gains (the fastest method)

The secondary disadvantages of tender:

1) The necessary remoteness of private individuals from the primary market (non-exclusive: direct bidding)
2) A specific disadvantage, the «curse of the winner»



PRIMARY DEALERS

The status of primary dealer: obligations and rights

1) **Obligations**:

a) Obligatory participation to State debt issuance, as the single and direct contact points for the Treasury

b) Supporting the secondary market of sovereign bonds, through their role as market makers ensuring liquidity

c) Counseling role for the issuing State and the Treasury

d) Organizers of the government securities market (quotations, settlement and delivery…)

e) Relations with investors

2) **Rights**:

a) Exclusive participation to competitive bids

b) Access to non-competitive bids (NCB)

c) Participation to syndication or consortium

d) Access to « out of sync » regulation in the UEOMA zone, repo facility in France, etc…

THE DIFFERENT STATUSES OF SPECIALISTS IN GOVERNMENT SECURITIES

Several types of primary dealers may be listed: see the French example

1) **<u>The status of Treasury Value Specialist (TVS)</u>**: it allowed for the launching of primary dealership activities in 1987.

2) **<u>The status of Correspondent in Treasury Values (CTV)</u>**: to prepare future candidates to the status of TVS.

3) **<u>The status of Pension Specialist in Treasury Value (PSTV)</u>**: to better organize repo markets and to increase the liquidity of government securities market.

The three statuses merged just before the switch to the Euro.

4) **<u>The status of Intermediary in Treasury Values (ITV)</u>**: a less constraining status for TVS candidates, created upon the switch to the Euro

ASSETS FOR A CANDIDACY TO TVS

1) Legal status, equity
2) Functional link to TVS activities
3) Trading team and Treasury values
4) Retailing team, repo team (if on the repo market)
5) Origination/syndication team
6) Diffusing quotations
7) Limiting risks and the size of the balance sheet allocated to the activity
8) Support teams for TVS activities
9) IT means
10) Cash management, if loans/borrowing occur with the debt manager

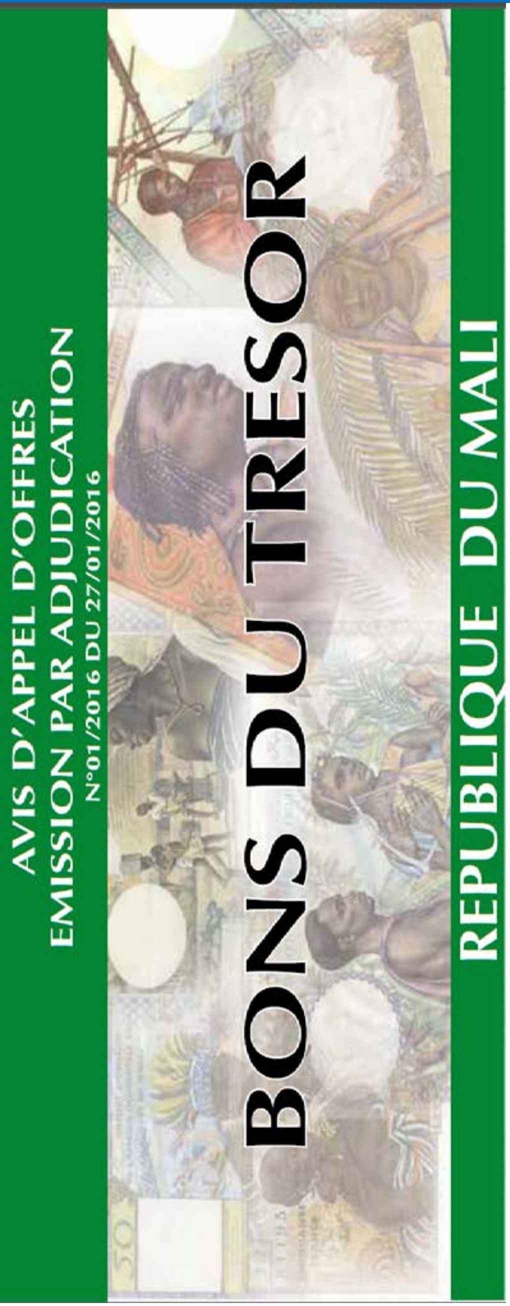
MARKET LIQUIDITY FOR GOVERNMENT BONDS

<u>Liquidity definition</u>: the capacity to convert, at any time, bonds into cash and vice-versa, in the short term and at reasonable cost.

Liquidity is reached through:

1) <u>On the primary market</u>:
- Standardized goods
- The assimilation techniques upon the issuance of bonds
- A limited number of lines
- Borrowing lines with large volumes of money

2) <u>On the secondary market</u>:
- An organized, developed and well-managed secondary market
- Creating a group of specialists in government securities
- Market-making – narrow trading spread
- A tax regime simplified for securities
- A safe and well-organized market for lending securities and for repo markets



SECURITIES: PUBLIC DEBT INSTRUMENTS

1) <u>Non-negotiable instruments</u>:

« National saving bills », France's example with nonnegotiable notes and bills.

Non-negotiable instruments are exclusive to financial institutions. Method of private loans or loans against promissory notes.

2) <u>Negotiable instruments</u>:

* <u>Short-term negotiable debt instruments:</u>

Treasury bills and cash management lasting less than one year, for institutional bodies, and also for companies, banks and financial institutions.

Example in France with FRTB (Fixed Rate Treasury Bills)

* <u>Negotiable bonds in the short and medium term</u>:

Fixed-rate and variable-rate bonds, between 3 and 10 years

Building the yield curve, with bonds issued regularly following an issuance schedule, in a yearly program of State financing. See bonds with special characteristics and their taxation.

3) <u>Other mechanisms of State borrowing</u>:

Limited resorting to loans from the Central Bank

DEBT MANAGEMENT: PITFALLS TO AVOID

1) **Weakening the State's financial position**
- maturity structure
- non-hedged exposure to exchange rate risk
- implicit contingent liabilities

2) **Management practices distorting the cost of interest**
- bonds guaranteed by future tax revenue
- debt securities with null or reduced taxation

3) **Incorrect accounting of guaranteed debt**
- weak coordination of loans taken out by lower administrative levels
- loan guarantees

4) **Resorting to financing means outside the market**
- special agreements with the central bank
- the creation of a captive market for government securities

5) **Defective control and registration of debts**
- excessive power to borrow
- insufficient control of the amount of the outstanding debt
- legal constraints on certain types of borrowing

DEBT MANAGEMENT STRATEGY IN FRANCE

"The French Treasury Agency manages the State's debt and cash in the best conditions of security and in the interest of the taxpayer."

- **Regularity and transparency** are the cornerstones of our strategy

Auction calendar published one year in advance

- FRTB every Monday
- OAT -fungible Treasury bonds- (>7Y) every first Thursday of the month (except in August and December)
- OAT (2Y to 7Y) indexed every third Thursday of the month (except in August and December)

- Benchmarks ever 2, 5, 10, 15, 30 and 50 years
- Regularity in the rhythm and composition of issuance
- No opportunism in its approach

- Introducing more **flexibility** in late 2007

- No more "off the run" issues
- No more lines during auctions
- Larger price ranges for issuance
- 2 optional tenders (August and December)
- From January 1st, 2013 onwards, new debt is issued as OAT (no longer BTAN - fixed-rate Treasury notes) with new maturity dates (May and November)