Public Financial Management in a Crisis Context

Max Alier
Resident Representative in Ukraine
International Monetary Fund
Kyiv, November 10, 2011

Treasuries' Main Objective

(1) Ensuring adequate cash availability for the government to meet its commitments…

(2) …at the lowest possible cost…

(3)…while minimizing risks.

Crisis Times

Normal times

Focus on rate, FX, and roll-over risks.

Crisis times:

Focus on liquidity risks—cash buffers are King!

Crisis Times

1. Increased and more volatile funding needs.
2. Changes in demand of government debt.
3. Changes in composition of demand of government debt, both sources and instruments.

All these happening rapidly and in the context of a weakened financial system.

RESULT: lower predictability makes more difficult the job of DMOs . This requires flexibility and changes in cash/debt management strategies to achieve (1) that are usually at odds with achieving (2) and (3).

(Broad) Lessons from the 2008-09 Crisis

1. Debt management plays a key role well beyond meeting the unexpected borrowing requirements; it is an integral part of the overall policy response to the crisis.

2. At times of disruptive surges in risk aversion, by absorbing timely some risks, the government contributes to the stabilization and recovery of financial markets.

3. Need to take advantage of the benign phase of the economic cycle to improve and strengthen debt management frameworks, including having a well functioning debt market even if not needed (surplus countries). Once a crisis hits options for action rapidly disappear.

(Specific) Lessons from the 2008-09 Crisis

Flexibility is key…

- to reassess the optimal borrowing strategy;
- to adapt the issuance methods;
- to explore alternative distribution channels.

While at the same time minimizing the damage to long-term objectives. Improved communication (with markets and central bank) together with increased transparency can go a long way in this direction.

Lessons from the 2008-09 Crisis—Emerging Markets

Before the crisis:

Adequate macroeconomic policies allow to seize the opportunity provided by the "good times".

Adequate debt management allows to reduce exposure to rates and exchange rate risks.

Lessons from the 2008-09 Crisis—Emerging Markets

Before the crisis:

1. Reduce the debt-to-GDP ratio.
2. Lower interest rates (consistent is low inflation).
3. Extend the yield curve—issue longer maturities.
4. Change composition away from short-term floating-rate and FX-linked instruments to longer term fixed-rate ones.
5. Broaden investors base by developing local markets, in particular institutional investors.
6. Have a proactive debt/liability management .

Lessons from the 2008-09 Crisis—Emerging Markets

During the crisis:

1. Actively and creatively look for alternative funding mechanisms: (i) better cash management; (ii) non-market sources of funding (e.g. IFIs); (iii) expand investors base.
2. Adapt the debt management strategy to shifts in demand.
3. Implement liability management operations to support the market.

The LICs Case

1. Less degree of integration in global financial markets reduce the speed of contagion but does not necessarily stops it.

2. In addition to the lessons discussed before. In the case of LICs efforts should not be spared in creating adequate institutions (e.g. legal frameworks) and capacity building.