



Debt Portfolio Management Quarterly Review | SEPTEMBER 2011 |

The Ministry of Finance submits the 27th Debt Portfolio Management Quarterly Review. The purpose is to present the underlying debt portfolio risk management measures and performance with respect to the planned annual financing program. Consequently, achievements of the medium-term strategic targets of debt management policy are reported. For the year 2011, these targets were quantified in the Financing and Debt Management Strategy for 2011 released on December 2, 2010. The Strategy specifies operating space of the asset and liability management through issuance activity, financial investment and active operations of Ministry of Finance on secondary market of government bonds and financial derivatives.

1 - Review of Strategic Targets for 2011

The 2011 state debt management policy is guided by the set of quantitative targets and criteria approved by the Ministry of Finance for issuance activities and the active management of debt portfolio is summarized in the following table.

Table 1: Financing programme and strategic targets in 2011

Criterion	Guidelines for 2011	September 30, 2011
International issues	Max. 40 % of the total annual gross borrowing requirement CZK 0.0 to 88.0 bn	0.4 % CZK 0.9 bn
Gross government bonds issues	CZK 86.0 to 194.0 bn	CZK 132.5 bn
Net money market issues	CZK 20.0 to 40.0 bn	CZK 29.9 bn
Loans from EIB	CZK 5.5 bn	CZK 3.3 bn
Short-term state debt	20 % and less	16.6 %
Average time to maturity	5.25 to 6.25 years	5.8 years
Interest Rate re-fixing up to 1 year	30 to 40 %	30.7 %
Average time to re-fixing	4 to 5 years	4.6 years
Foreign-currency state debt	At most 15 to 17 %	9.8 %

Note: EIB – European Investment Bank. Gross government bonds issues includes tap sales and the sales to EIB.

Source: MF

As regards **international funding**, there was no change during the 3rd quarter of 2011 compare to the 2nd quarter of 2011. The total volume of international funding has reached CZK 0.9 bn. during three quarters of 2011. In the first quarter Czech Republic has only realized clearance sale of floating rate bond denominated in EUR in the amount of **EUR 37.5 mil**, i.e. **CZK 926.9 mil**. In the third quarter of 2011 four tranches of loans have been drawn from the European Investment Bank valued at CZK 2.7 bn. The total volume of loans from EIB has been drawn at CZK 3.3 bn. at the end of the third quarter of 2011.

Regarding **domestic issuance activity**, the total gross issuance of government bonds reached **CZK 36.4 bn**. during the 3rd quarter of 2011, including CZK 0.0 bn. bought by EIB. The total gross domestic issuance activity has reached CZK 132.5 bn. during three quarters of 2011 and about 68.3 % of the maximal supply initially announced in the Strategy for 2011 was

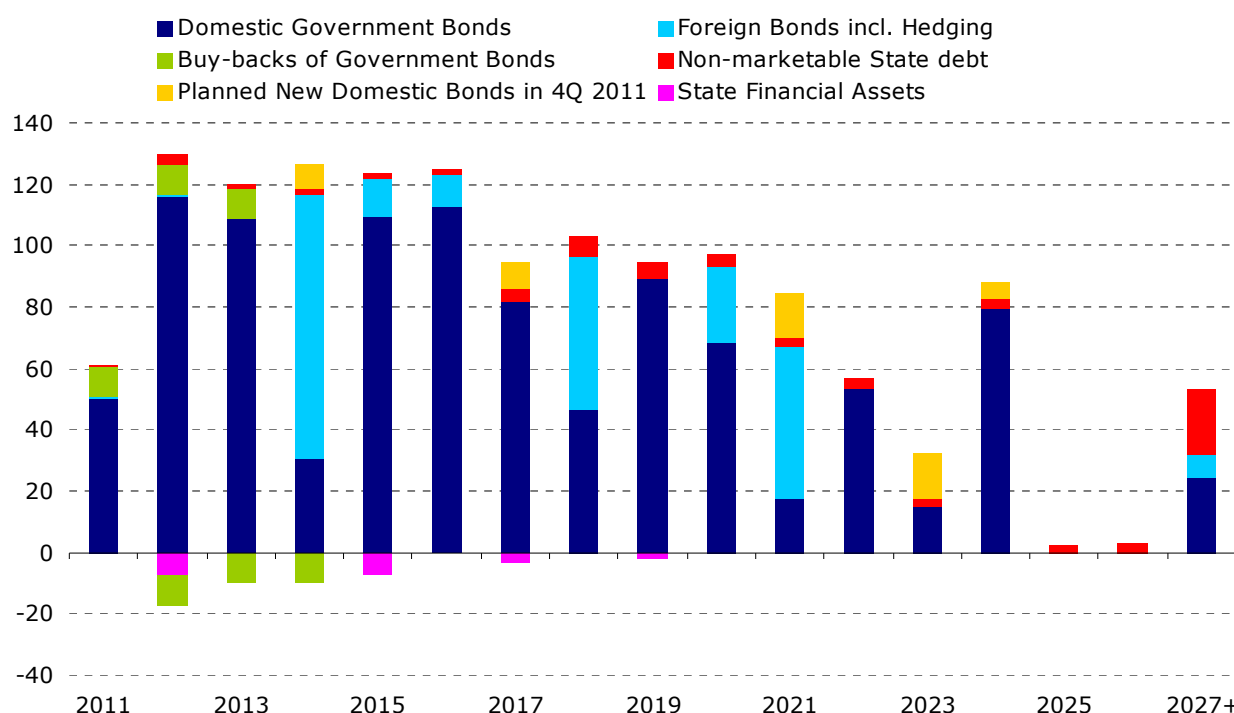
used. The net issuance of government bonds was **CZK 36.4 bn.** during the 3rd quarter of 2011. Buy-backs of government bonds were not executed during three quarters.

The volume in issue of money market instruments increased by **CZK 2.2 bn** during the 3rd quarter of 2011.

The short-term state debt decreased by 0.4 percentage points and reached the share of **16.6 %** at the end of the 3rd quarter of 2011. The figure remains, in accordance with Strategy, and refinancing risk is maintained below the 20% limit ceiling.

Average time to maturity decreased by 0.2 year at the end of the 3rd quarter of 2011 and reached 5.8 years. Average time to maturity remains within the announced target bracket, i.e. 5.25–6.25 years for 2011.

Figure 1: Redemption profile of state debt (CZK billion)
(End of 3Q 2011; updated on September 30, 2011)



Note: Excluding money market instruments on the debt and assets side. The positive vertical scale shows liabilities, the negative vertical scale shows state financial assets and for 2011 – 2013 planned buy-backs. Profile does not include the impact of planned retail government bonds with maturities 2012 and 2016.

Source: MF

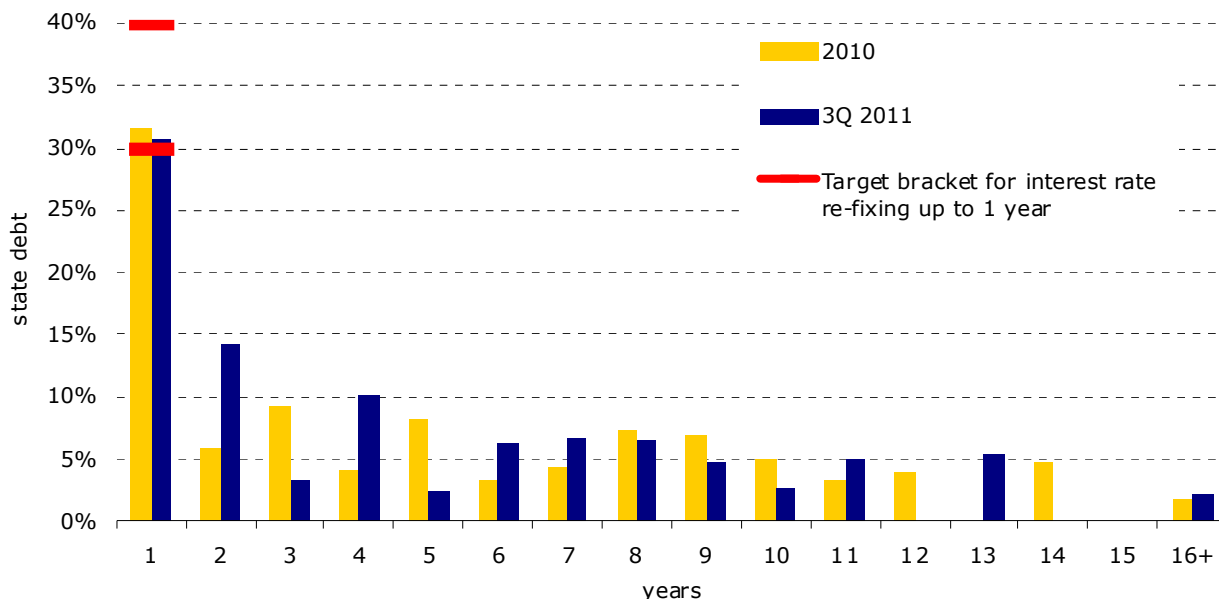
Interest rate re-fixing up to one year increased by 0.4 percentage points during the 3rd quarter of 2011. This indicator reached the share of **30.7 %** and remains within the announced medium-term target bracket, i.e. 30 to 40 %.

Starting in 2011 the new strategic goal has been declared for interest rate debt management – **the average time to state debt re-fixing**. The Ministry has set an explicit target of a 4 to 5 year interval for this indicator. At the end of the third quarter the average time to state debt re-fixing reached the level of **4.6 years** and remains in this quarter within the announced long-term target bracket.

From 2011 onwards the Ministry will actively manage **the share of foreign-currency state debt**. The strategic limit declared by the Ministry for 2011 and beyond is 15% (in short term up to 17 %). The foreign-currency state debt reached the share of **9.8 %** and remains below the 15 % ceiling, which indicates low and stable foreign-currency exposition.

Figure 2: Re-fixing profil of state debt

(end of 3Q 2011 compared with end of 2010; updated on September 30, 2011)

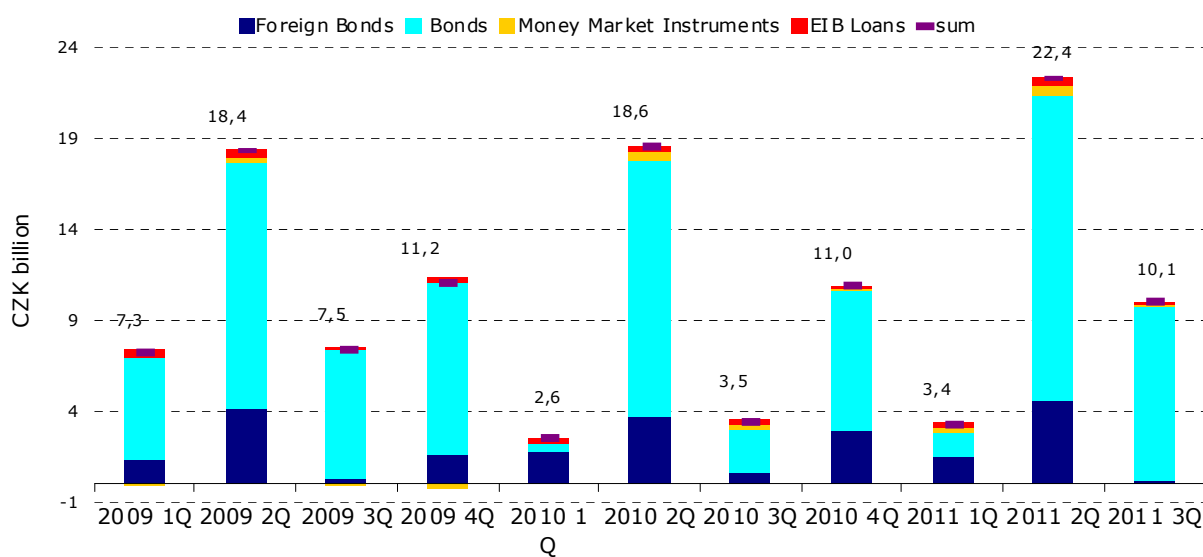


Note: Including derivatives
Source: MF

2 – State debt costs and Cost-at-Risk

Figure 3 presents a breakdown of net interest costs related to the state debt in last two years. More detailed information describing the budgetary expenditures and revenues can be found in appendix (table 11). Figure 3 demonstrates regularity in lower net interest costs in the first and third quarter. The year to year comparison highlights relatively higher interest costs in 3rd quarter of 2011.

Figure 3: Quarterly Breakdown of Change in Interest Costs

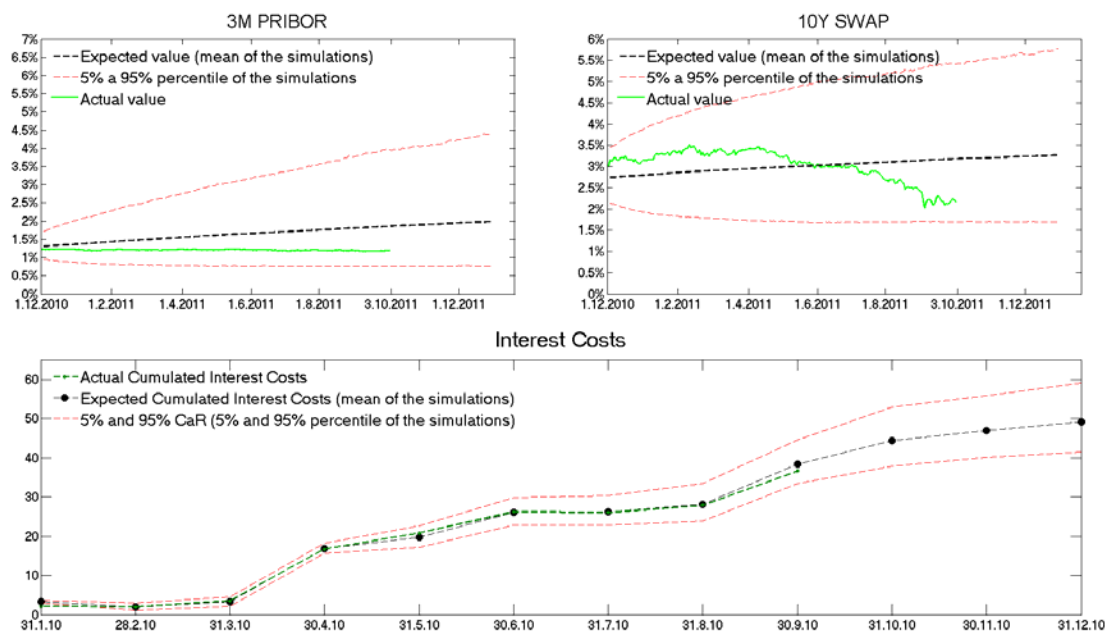


Source: MF

The state debt interest costs model Cost-at-Risk (CaR) for the year 2011 was published in the Financing and Debt Management Strategy for the year 2011. Calculations of the CaR values are based on future interest rates simulations.

The actual versus simulated developments of the PRIBOR 3M and 10Y CZK swap from December 1, 2010 till December 31, 2011 are displayed in the upper part of the figure 4. The development of the actual versus simulated net interest costs for the year 2011 is shown in the lower part of the figure 4.

Figure 4: Actual versus simulated evolution of the interest rates and the actual versus simulated monthly net interest costs (CZK billion)



*Note: Interest costs are calculated on the cash principle relevant for the current methodology of the state budget.
Source: MF*

Table 2 refers to the comparison between the actual development of net interest costs and the development of the simulated interest costs during three quarters of 2011 in comparison with the same period of the last year. The comparison is summarized in the following table.

Table 2: Cost-at-Risk deviation from the actual interest costs for three quarters of 2010 and 2011

	30.9. 2010	30. 9. 2011
Actual net interest costs (CZK billion)	35.4	36.6
Expected net (simulated) costs (CZK billion)	47.3	38.4
Cost-at-Risk 95% (CZK billion)	49.8	44.6
Expectation	33.5	4.7

Source: MF

3 – State Debt Parameters (end of quarter)

Table 3: Debt Parameters

	30.9.2010	31.12.2010	31.3.2011	30.6.2011	30.9.2011
Total state debt (CZK billion)	1 384.8	1 344.1	1 404.4	1 412.9	1 456.8
Market value, inc. derivatives (CZK billion)	1 499.8	1 429.2	1 484.0	1 495.5	1 579.1
Short-term state debt (%)	17.6	16.1	17.2	17.0	16.6
Share of money market instruments (%)	9.3	8.4	9.8	10.0	9.8
Average time to maturity (years)	6.1	6.3	6.0	6.0	5.8
Interest rate re-fixing up to one year, inc. derivatives (%)	31.9	31.7	32.6	30.3	30.7
Average interest rate re-fixing (years)	5.0	5.0	4.9	4.9	4.6
Variable-rate market debt	11.4	12.1	12.6	13.7	14.5
Modified duration (years)	4.5	4.4	4.2	4.2	4.3
Modified duration, exc. CZK IRS (years)	4.4	4.4	4.1	4.2	4.2
Foreign currency debt (%)	10.7	10.4	9.8	9.9	9.8
Foreign currency debt, exc. cross-currency swaps (%)	15.8	16.7	15.6	15.5	15.3
Share of € on foreign currency debt	89.2	87.9	88.6	88.3	87.7
Nonmarketable state debt (%)	4.6	5.0	4.8	4.8	4.8
Marketable state debt (CZK billion)	1 321.8	1 276.6	1 337.3	1 345.4	1 387.0
Market value (CZK billion)	1 435.4	1 360.0	1 415.3	1 426.3	1 507.0
Short-term marketable debt (%)	18.3	16.9	18.0	17.6	17.3
Share of money market instruments (%)	9.7	8.9	10.3	10.5	10.3
Average time to maturity (years)	5.8	6.0	5.7	5.7	5.5
Interest rate re-fixing up to one year, inc. derivatives (%)	28.9	28.3	29.5	27.0	27.4
Average interest rate re-fixing (years)	5.2	5.3	5.1	5.1	4.8
Variable-rate marketable debt (%)	7.5	7.8	8.5	9.7	10.5
Modified duration (years)	4.6	4.6	4.3	4.4	4.4
Modified duration, exc. CZK IRS (years)	4.5	4.5	4.3	4.3	4.3
Foreign currency debt (%)	11.2	11.0	10.3	10.4	10.3
Foreign currency debt, exc. cross-currency swaps (%)	16.6	17.5	16.4	16.2	16.1
Share of € on foreign currency debt	89.3	87.9	88.6	88.3	87.8

Notes: **Interest rate re-fixing up to one year** = Money market instruments + Fixed-rate short-term debt + Variable-rate state debt + Effect of interest rate derivatives.

Source: MF

Table 4: State Financial Assets

	31. 12. 2010	30. 9. 2011
State financial assets		
Interest rate re-fixing up to one year (%)	88.4	85.6
Average time to re-fixing (years)	0.7	0.7
Investment portfolio and on-lending		
Average return (%)	2.0	2.0
Average time to maturity (years)	2.0	1.9
Modified duration (years)	1.8	1.8

Source: MF

4 – The net borrowing requirements

The central government's net borrowing requirements are determined primary by the state budget deficits. The final level of the net borrowing requirement is also influenced by state financial assets operations, lending and on-lending, and changes in the level of the financial reserve generated by bond issues. The net borrowing requirement is the principal factor driving the change in the nominal value of gross state debt. Since part of the state debt is denominated in foreign currencies, the state debt is also affected by changes of the particular bilateral exchange rate.

Table 5: The net borrowing requirement of the central government and change in the state debt

CZK billion	2009	2010	30. 9. 2011
Gross state debt the beginning of the period	999.8	1 178.2	1 344.1
Primary balance of state budget, excluding on-lending	147.9	120.6	69.2
Net expenditures on state debt ¹	44.5	35.8	35.9
Extra-budgetary borrowing requirement	0.0	0.0	0.0
Net borrowing requirement, net of assets operations	192.4	156.4	105.1
State financial assets operations ²	5.4	3.0	2.4
On-lending (net change) ³	0.0	1.7	0.0
Financial reserve (net change) ⁴	-19.6	7.1	5.9
Net borrowing requirement	178.2	168.2	113.4
Changes in nominal state debt ⁵	0.2	-2.4	-0.7
Gross debt change	178.4	165.8	112.7
Gross state debt at the end of the period	1 178.2	1 344.1	1 456.8
(% on GDP)	(32.5)	(36.4)	(39.1)

¹ balance of budgetary chapter 396 – State debt excl. expenditures – Transfers on projects financed by loans from EIB

² balance of budgetary chapter 397 – State Financial Assets Operations

³ on-lending to other states and enterprises with full state-backed guarantee on their core business

⁴ cash reserve generated by bonds issues according to the Act No. 218/2000

⁵ exchange rate changes due to re-evaluation of foreign currencies denominated debt and state debt amortization within budgetary chapter 396.

Source: MF

The net borrowing requirement is the first component of the gross borrowing requirement, which determines the magnitude of the state's borrowing operations in the given year. The second component consists of redemptions on the state debt in the given year and the buy-backs and switches of government bonds before their original maturity.

Table 6: Gross borrowing requirement and instruments for funding of the central government

<i>mld. CZK</i> <i>(% GDP)</i>	2009	2010	30. 9. 2011
Net borrowing requirement	178.2	168.2	113.4
Redemptions on state debt. incl. buy-backs and switches within a budgetary year	98.0	83.0	51.8
Redemptions on loans from EIB	0.8	1.1	0.9
Buy-backs and switches of bonds due in following years ¹	2.0	0.0	0.0
Redemptions on state debt. incl. buy-backs and switches within a budgetary year	0.0	0.2	0.4
Gross borrowing requirement	279.0	252.6	166.6
	(7.7)	(6.8)	(4.5)
Net money market issuance ²	9.4	25.1	29.9
Gross government bonds issuance ³	257.7	217.1	133.4
Loans from EIB	11.9	10.4	3.3
Net loans from the State Treasury	0.0	0.0	0.0
Funding of borrowing requirement	279.0	252.6	166.6

¹ *excl. operations with government bonds due within a budgetary year*

² *excl. revolving within a budgetary year*

³ *nominal amount. ie. premia and discounts are included in net costs on state debt not entering net borrowing requirement.*

Source: MF

Net debt portfolio reflects the state debt and state financial assets. The methodology defining individual items is stated in the "The Czech Republic funding and Debt Management Strategy 2011".

Table 7: State and structure of net debt portfolio and financial sources of the State Treasury

<i>CZK billion</i>	2009	2010	30. 9. 2011
Gross state debt at the beginning of the period	1 178.2	1 344.1	1 456.8
Money market instruments	88.2	113.3	143.3
Medium-term and long-term bonds	1 031.6	1 163.2	1243.7
Loans from EIB	57.9	67.2	69.5
Bills of exchange ¹	0.6	0.3	0.3
Short-term liabilities to the Treasury	0.0	0.0	0.0
State financial assets at the end of the period	102.2	113.9	122.2
Nuclear investment portfolio	13.5	15.1	16.6
Pensions investment portfolio	21.2	21.6	21.8
Special-purpose financial assets accounts	9.2	10.2	10.8
Lending and On-lending ²	0.0	1.7	1.7
Financial reserve ³	58.3	65.3	71.3
Net debt portfolio at the end of the period	1 076.0	1230.2	1334.6

¹ *Bills of exchange to cover equity holdings of the Czech Republic with international financial institutions*

² *lending to other states and to enterprises with full state-backed guarantee on the core business*

³ *disposable cash balance build up by issuance of government debt according to the Act No. 218/2000. Section 35.*

Source: MF

5 – Appendix

Table 8: T- bonds issue in 3rd quarter of 2011

T-bond	Issue	Auction Date	Settle-ment date	Maturity date	Curren-cy	Offered Nominal Volume	Placed Nominal Volume
VAR/2023	63. Issue / 2. Tranche	20.7.	25.7.	18.4.2023	CZK	8 000 000 000	6 850 000 000
4.00/2017	51. Issue / 12. Tranche	10.8.	15.8.	11.4.2017	CZK	8 000 000 000	7 282 450 000
5.70/2024	58. Issue / 12. Tranche	7.9.	12.9.	25.5.2024	CZK	8 000 000 000	6 256 050 000
VAR/2016	55. Issue / 10. Tranche	14.9.	19.9.	27.10.2016	CZK	8 000 000 000	7 786 790 000
2.75/2014	62. Issue / 4. Tranche	21.9.	26.9.	31.3.2014	CZK	8 000 000 000	8 197 720 000
Total					CZK	40 000 000 000	36 373 010 000

* CZK value

T-bond	Issue	Interest rate type	Average net price	Average Yield to Maturity	Bid-to-cover ratio	Competitive auction	Non-Competitive auction
VAR/2023	63. Issue / 2. Tranche	VAR %	101.74	48.569 *	2.48	85.0 %	0.6 %
4.00/2017	51. Issue / 12. Tranche	4,00 %	105.77	2.877	1.33	88.6 %	2.5 %
5.70/2024	58. Issue / 12. Tranche	5.70 %	125.83	3.193	1.11	78.2 %	0.0 %
VAR/2016	55. Issue / 10. Tranche	VAR %	98.79	24.673 *	2.36	87.5 %	9.8 %
2.75/2014	62. Issue / 4. Tranche	2.75 %	102.72	1.633	2.34	89.3 %	13.2 %
Average					1.92	85.7 %	5.2 %

* Spread to the benchmark rate in bps (*discounted margin*)

Table 9: T-note issue in 3rd quarter of 2011

Issue No.	Maturity (months)	Auction Date	Settlement date	Maturity date	Offered Nominal Volume	Placed Nominal Volume	Yield (% p.a.)
SPP 624	6	30.6.	1.7.	30.12.2011	7 000 000 000	6 970 000 000	1.02
SPP 625	3	14.7.	15.7.	14.10.2011	7 000 000 000	7 258 000 000	0.81
SPP 626	12	4.8.	5.8.	3.8.2012	8 000 000 000	10 094 000 000	1.29
SPP 627	3	25.8.	26.8.	25.11.2011	8 000 000 000	9 672 000 000	0.78
SPP 628	12	1.9.	2.9.	31.8.2012	7 000 000 000	8 600 000 000	1.17
SPP 629	3	15.9.	16.9.	16.12.2011	7 000 000 000	8 000 000 000	0.78
SPP 630	9	29.9.	30.9.	29.6.2012	8 000 000 000	8 863 000 000	1.05
Total					52 000 000 000	59 457 000 000	1.00*

* Average weighted yield to maturity of the T-notes issues in 3. quarter

Table 10: Redemption and re-fixing profile of T-bond issues in 3rd Quarter 2011

T-bond	Volume	Average time to maturity at the issue date	Average time to maturity at 31. 12. 2011	Average time to re-fix at the issue date	Average time to re-fix at 31. 12. 2011
Float	14 636 790 000	8.21	7.86	0.4	0.58
Fix	21 736 220 000	6.5	6.19	6.5	6.19
Total	36 373 010 000	7.19	6.86	4.98	4.84

Note: Volume in CZK

Table 10 presents the overview of the redemption and re-fixing profile of the portfolio of T-bond issues. The average time to maturity at the issuing date represent T-bond maturity at the same time. Whereas average time to maturity at 31. 12. 2011 is related to the Ministry strategic target set as range 5.25 – 6.25 years of the average time to maturity of the debt portfolio. For more information about the strategic targets you are advised to consult "The Czech Republic Funding and Debt Management Strategy". Time to re-fix follows analogical approach. The strategic target is set as a range 5.25 – 6.25 years.

Table 11: Planned and actual budgetary expenditures and revenues on state debt in the first three quarters of 2011

Measure (CZK mil)	Actual Q1-Q3 2010	Budget 2011		Actual Q1-Q3 2011	% Execution	Index 2011/2010 (%)
		Approved	After changes			
1	2	3	4	5	5:4	5:2
1. Total interest costs	35 430 (-) 10 706	71 286 (-) 5 336	70 674 (-) 5 336	43 004 (-) 7 172	60.8 134.4	121.4 67.0
Domestic debt	<i>28 028</i> <i>(-) 10 347</i>	<i>57 115</i> <i>(-) 4 836</i>	<i>56 503</i> <i>(-) 4 836</i>	<i>35 374</i> <i>(-) 6 841</i>	<i>62.6</i> <i>141.5</i>	<i>126.2</i> <i>66.1</i>
Money market instruments and on-lending	1 212 (-) 468	3 818 (-) 1 000	3 818 (-) 1 000	1 439 (-) 505	37.7 50.5	118.7 108.0
Government bonds	26 815 (-) 9 879	53 297 (-) 3 836	52 685 (-) 3 836	33 934 (-) 6 336	64.4 165.2	126.5 64.1
Foreign debt	<i>7 402</i> <i>(-) 359</i>	<i>14 171</i> <i>(-) 500</i>	<i>14 171</i> <i>(-) 500</i>	<i>7 630</i> <i>(-) 328</i>	<i>53.8</i> <i>65.7</i>	<i>103.1</i> <i>91.5</i>
International issues	6 514 (-) 359	11 790 (-) 500	11 790 (-) 500	6 774 (-) 328	57.5 65.7	104.0 91.5
EIB loans	888	2 381	2 381	856	35.9	96.4
Short-term loans	-	-	-	-	-	-
Bank accounts	- -	- -	- -	0 (-) 2	- -	- -
Bank accounts interests (+ paid, - received)	- -	- -	- -	0 (-) 2	- -	- -
2. Total fees	201 (-) 0	700 -	700 -	59 (-) 0	8.4 -	29.2 0.5
3. Redemption	-	4	4	-	-	-
4. FX gain/loss	158 (-)160	1 000 (-) 300	1 000 (-) 300	- -	- -	- -
5. Transfers for projects	-	5 501	2 339	-	-	-
Total balance	35 788 (-) 10 866	78 491 (-) 5 636	74 717 (-) 5 636	43 062 (-) 7 172	57.6 127.3	120.3 66.0

Note: (-) means revenues (gains).

Source: MF

The **net debt service costs** on the state debt in the first three quarters of 2011 amounts **CZK 35.9 billion**. Accrued interest income and government bonds premiums achieve CZK 6.3 billion and financial investments on the money market gain CZK 0.4 billion. The gross debt service costs reached CZK 43.1 billion.

* * *

This publication is available also on the website:

www.mfcr.cz/statedebt

The next issue of Quarterly Review will be published on January 9, at 2.00 p.m.

Further information:

Aleš Maršál, Head of Risk Management and Portfolio Strategy

Debt and Financial Assets Management Department MF ČR

Letenská 15, 118 10 Praha 1

Phone: 257 042 456, e-mail: ales.marsal@mfcr.cz, Reuters <MFCR>