



Ministry of Finance

Debt and Financial Assets
Management Department

Debt Portfolio Management Quarterly Review

September 2014



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Introduction

The Ministry of Finance (hereinafter the "Ministry") hereby submits the 39th Debt Portfolio Management Quarterly Review, presenting basic data on parameters of the portfolio of state liabilities and on parameters of the portfolio of state financial assets. The basic monitored strategic targets for 2014 had been quantified in the governing document The Czech Republic Funding and Debt Management

Strategy for 2014 (hereinafter the "Strategy") approved by the Minister of Finance and published on 16 December 2013. The Strategy specifies the operating scope for tactical management of the state debt and financial assets through issuance activity, financial investment and active operations by the Ministry on the secondary market.

1 - Main Events in Q3 2014

The Ongoing Decrease in CZK-denominated Value of the Gross State Debt

In the third quarter of 2014, the decrease in CZK-denominated value of the gross state debt has continued. The decrease has amounted to CZK 297 million in comparison to the end of the first half of 2014 and CZK 332 million in comparison to the end of 2013. The decrease in CZK-denominated value

of the gross state debt is in accordance with the Ministry's plan of stabilization of the state debt, which brings positive impacts, especially in the form of savings in interest expenditure of the state budget related to the issuance activity of the state during the year.

The Launching of Operations in Secondary Market of Government Bonds

The operations in secondary market of government bonds using the electronic trading platform MTS Czech Republic were launched once again during the September. These operations are buy-backs of medium-term and long-term government bonds maturing in 2015 and 2016, and also tap sales of medium-term and long-term government bonds from the Ministry's own portfolio. The total nominal

value of realized buy-backs amounted to CZK 2.2 billion and total nominal value of realized tap sales amounted to CZK 0.2 billion. The Ministry has noticed an increasing interest in both these types of operations in secondary market of government bonds and plans their extensive realization during the fourth quarter of 2014 in case of continuing demand from the side of the Primary Dealers.

The Extension of Instruments Used for Investing of State Treasury Liquidity

Within the investment of available EUR liquidity of state treasury, the Ministry newly uses also short-term government bonds as collateral of investment operations, enabling greater flexibility in investing in the financial market. In the situation where the Czech National Bank pays negative interest rate of

minus 0.2% p.a. on available liquidity on Ministry's accounts, it is important to look for further possible investment operations and to broaden the range of appropriate instruments for CZK and EUR state treasury liquidity management.

2 - Overview of 2014 Strategic Debt Management Targets

Regular quarterly assessment of actual structure of debt portfolio in relation to the announced strategic targets and limits, which constitute the main parameters of publicly defined strategic benchmark portfolio communicated mainly through the Strategy, and quarterly updates of the gross borrowing requirement and the funding programme are the main Ministry's tools to support the credibility and transparency of the whole process of the state debt and related financial assets management and executing borrowing operation on financial markets in accordance with

the best international practice and recommended standards. The overview of this assessment for the first three quarters of 2014 confirms, that the Ministry does not deviate from any of the announced targets and limits and that the borrowing operations executed in accordance with the alternative scenario of the funding programme announced in the Strategy correspond in their scope to the announced issuance plans with the exception of the retail bonds issuance where there has been a rationalization of parameters and a reduction of the planned issue.

Table 1: Funding Programme in 2014

INDICATOR	Announced plan for 2014	Q1 – Q3 2014
International issuance activity	CZK 0.0 to 80.0 billion ¹	CZK 0.0 billion
Gross issue of medium-term and long-term government bonds²	CZK 119.2 to 230.1 billion	CZK 127.9 billion
Gross issue of retail bonds	CZK 20.0 to 50.0 billion	CZK 1.6 billion ³
Net issue of money market instruments⁴	CZK -20.9 to 0.0 billion	CZK -17.7 billion
Gross issue of state treasury bills⁵	CZK 100.0 to 120.9 billion	CZK 82.8 billion
Loans from EIB	CZK 0.0 to 10.0 billion	CZK 0.0 billion

¹ The share of funding on foreign markets will not exceed 25% of annual gross borrowing requirement according to the methodology valid for 2014.

² Incl. tap sales from Ministry's own portfolio in the secondary market and the Ministry's investment operations.

³ Incl. reinvestments of yields in the total nominal value of CZK 189.0 million.

⁴ Incl. state treasury bills, lending facility for providing lending of government bonds, and other money market instruments.

⁵ Excl. treasury bills issued and redeemed within the respective period.

Source: MoF

In the area of **international issuance activity**, the Ministry did not realize any issuance operations in Q1-Q3, only redemptions of foreign issues in the total nominal value of EUR 1.5 billion were carried out. In Q1-Q3, also no tranche of loan received from European Investment Bank (hereinafter the "EIB") was drawn, in Q3 planned repayments in total amount of CZK 0.4 billion and the unplanned early repayments in total amount of CZK 2.6 billion were carried out. The total repayments of principals of loans from EIB amounted to CZK 7.5 billion in Q1-Q3.

Regarding **domestic issuance activity**, the total nominal value of the gross issue of medium-term and long-term government bonds amounted to CZK 11.1 billion in Q3. The total nominal value of the gross issuance of medium-term and long-term government bonds amounted to CZK 127.9 billion in Q1-Q3, representing 55.6% of maximum annual issuance limit for this type of financing under the alternative scenario of the 2014 funding programme. In Q3, the Ministry realized sales of government bonds in a secondary market using the MTS Czech Republic electronic platform in the total nominal value of CZK 0.2 billion, which were the only sales in a secondary market realized in this

year. No planned redemption of medium-term and long-term government bond took place in Q3, while the total nominal value of medium-term and long-term government bond redemptions amounted to CZK 46.0 billion in Q1-Q3. In Q3, the buy-backs of government bonds prior to their maturity in the total nominal value of CZK 2.2 billion were carried out, which were the only buy-backs of government bonds carried out in this year. The total nominal value of the net issue of medium-term and long-term government bonds in Q3 amounted to CZK 8.8 billion. The total nominal value of the net issue of medium-term and long-term government bonds in Q1-Q3 amounted to CZK 79.7 billion.

Regarding **savings government bonds**, the total nominal value of the gross issue of savings government bonds incl. the reinvestment of yields amounted to CZK 1.6 billion in Q1-Q3. As of the end of Q3, the total nominal value of savings government bonds outstanding amounted to CZK 80.6 billion, which represents 4.8% of total state debt and 6.5% of CZK-denominated government bonds excl. state treasury bills. In Q3, no planned redemptions of savings government bonds were carried out and the early redemptions of savings government bonds in the total nominal value

of CZK 45.3 million were carried out, which represents 0.06% of the total nominal value of savings government bonds outstanding. The total nominal value of planned and early redemptions of savings government bonds amounted to CZK 8.6 billion in Q1-Q3.

The total nominal value of the gross issue of **money market instruments** excl. their roll-over amounted to CZK 34.3 billion during Q3, of which CZK 22.0 billion represented the state treasury bills and CZK 12.4 billion the lending facility for providing the lending of government bonds. In Q1-Q3, the total nominal value of the gross issue of money market instruments excl. the roll-over amounted to CZK 95.2 billion, of which CZK 82.8 billion represented the state treasury bills and CZK 12.4 billion the lending facility for providing the lending of government bonds. The gross issue of money market instruments represents 78.7% of

maximum annual issuance limit for this type of financing. The total nominal value of the net issue of money market instruments amounted to CZK -17.7 billion in Q1-Q3.

Short-term state debt (debt payable within one year) as of the end of Q3 increased by 3.4 percentage points in comparison to the end of Q2 and amounted to **16.1%** and thus reached the value below the limit of 20.0% out of the total state debt which is in line with announced Strategy for 2014.

The **medium-term state debt** (debt payable within five years) as of Q3 decreased by 0.2 percentage points in comparison to the end of Q2 and amounted to **53.6%**. The value thus remained below the limit of 70.0% out of the total state debt valid for 2014 and for the medium-term horizon.

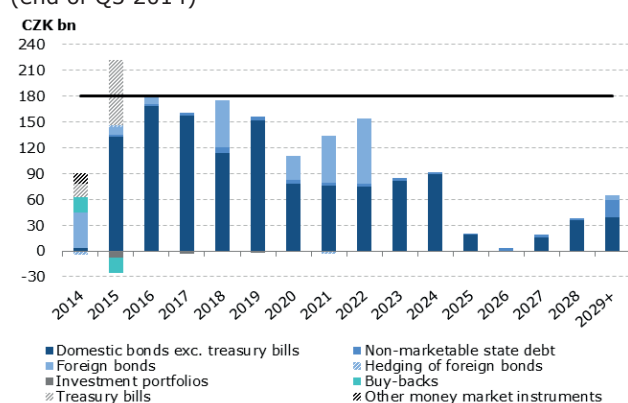
Table 2: Strategic Targets, Limits and Risk Parameters of Debt Portfolio in 2014

INDICATOR	Announced limits and targets for 2014	30 Sep 2014
Short-term state debt	20.0% and less	16.1%
Medium-term state debt	70.0% and less	53.6%
Average time to maturity	5.0 to 6.0 years	5.5 years
Interest re-fixing up to 1 year	30.0 to 40.0%	36.4%
Average time to re-fixing	4.0 to 5.0 years	4.3 years
Net foreign-currency exposure of state debt	Max. 15.0 to 17.0%	10.1%

Source: MoF

Figure 1: Redemption Profile of State Debt and Financial Assests

(end of Q3 2014)



Note: The positive axis shows liabilities and planned buy-backs on bonds due in 2015 and later years carried out in 2014, the negative vertical axis shows state financial assets and planned buy-backs carried out in 2014. CZK-denominated CZGB include savings government bonds. Excl. the roll-over of money market instrument.
Source: MoF

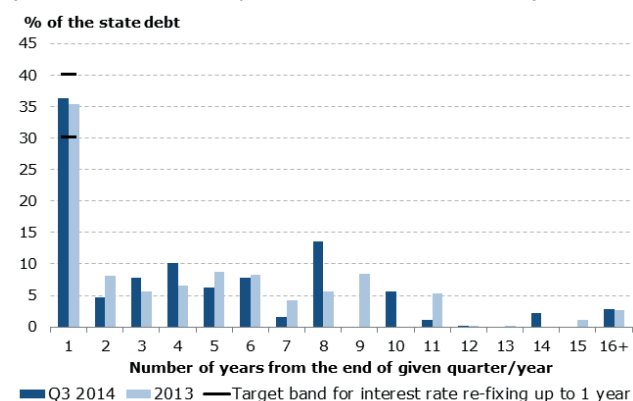
The **average time to maturity** of the state debt as of the end of Q3 decreased by 0.2 years in comparison to the end of Q2 and amounted to **5.5 years**. The average time to maturity of the state debt is thus in the middle of the announced target band of 5.0 to 6.0 years valid for 2014.

Interest re-fixing of the state debt up to one year as of the end of Q3 increased by 3.6 percentage point in comparison to the end of Q2 and amounted to **36.4%**. This indicator thus remained within the medium-term target band of 30.0 to 40.0% valid for 2014.

Average time to the state debt re-fixing as of the end of Q3 decreased by 0.2 years in comparison to the end of Q2 and amounted to **4.3 years**. This indicator thus remained within the medium-term target band of 4.0 to 5.0 years.

Figure 2: Re-fixing Profile of State Debt

(end of Q3 2014 compared with the end of 2013)



Note: Incl. derivative transactions.

Source: MoF

The main indicator for currency risk management is the proportion of net foreign-currency exposure of the state debt to the total state debt. The strategic limit announced for 2014 is 15.0% (up to 17.0% in the short term). The value of this indicator at the end of Q3 increased by 0.1 percentage point in comparison to the end of Q2 and amounted to 10.1% and is thus below its limit. The share of net foreign-currency exposure of the state debt denominated in euro in relation to overall net foreign-currency exposure of the state debt amounted to 89.8%, as the value remained at the same level in comparison to the end of Q2, thus indicating the euro's dominance in the foreign-currency state debt portfolio.

3 - Borrowing Requirement of the Central Government

Starting with the Strategy for 2014, the Ministry has switched to the new, internationally recommended and used methodology of gross borrowing requirement reporting, which, unlike the original methodology, includes money market and

other instruments with original maturity of up to one year outstanding at the end of particular year to be refinanced over the course of following year excluding any roll-over within the year in the total gross borrowing requirement.

Financing Needs and Sources of the Central Government

The financing needs of the central government is determined by the items that must be financed in the given year, i.e. the budgeted state budget deficit, potential cash extra-budgetary financing requirement and all redemptions and early redemptions on nominal values (principal) of state

debt, including the related derivatives. Operations on the side of state financial assets, including net changes in the cash reserve, or the provision and repayment of extra-budgetary loans and credits to other states and domestic legal entities, are funding sources.

Table 3: Financing Needs and Sources (CZK billion)

Financing needs	2012	2013	Q1-Q3 2014
Primary balance of state budget	59.6	30.4	-8.8
Net expenditure on state debt	41.4	50.9	43.2
Extra-budgetary financing needs	0.0	0.0	0.0
Redemption on government bonds in the respective year	115.6	108.6	98.8
Buy-backs and exchanges of government bonds from prior years	-2.0	-8.1	-4.0
Buy-backs and exchanges of government bonds due in coming years ¹	8.1	7.5	2.2
Redemption and early redemptions on savings government bonds in given year	9.6	7.7	8.6
Redemption on state treasury bills excl. roll-over ²	162.6	189.1	112.9
Redemption on other money market instruments excl. roll-over ²	0.0	0.0	0.0
Repayments on EIB loans	5.3	2.8	7.5
Total financing needs	400.2	388.8	260.5
Gross state treasury bills issuance excl. roll-over ²	189.1	120.9	82.8
Other money market instruments excl. roll-over ²	0.0	0.0	12.4
Gross CZGB issuance	164.6	145.6	127.9
Gross issue of government bonds on foreign markets	69.0	0.0	0.0
Gross issue of retail bonds	45.4	39.1	1.6
EIB loans	4.0	4.3	0.0
Net change in cash reserve	-69.4	79.5	38.2
Net change in on-lending	0.0	1.7	0.0
State financial asset operations	-2.4	-2.3	-2.5
State budget surplus excl. state financial asset operations	0.0	0.0	0.0
Re-financing from the state treasury	0.0	0.0	0.0
Total financing sources	400.2	388.8	260.5
Non-debt financing sources	71.8	-78.9	-35.7
Gross borrowing requirement	472.0	309.9	224.8

¹ Excluding operations with medium- and long-term government bonds during current budgetary year.

² Within the respective period.

Source: MoF

Financing of the Gross Borrowing Requirement

The gross borrowing requirement determines the part of the sources for the government's financing needs secured through borrowing operations, i.e. it stipulates the value of cash resources that the government must obtain primarily by issuing and selling government bonds and drawing credits and loans. The gross borrowing requirement may be lower than the annual financing needs if

state financial assets or a short-term re-financing from the state treasury is involved as a source of financing; on the contrary, it may be higher if assets are accumulated through borrowing operations e.g. for the purpose of pre-financing and building up the cash reserve, or for the purpose of providing extra-budgetary credit and loans.

Table 4: Financing of the Gross Borrowing Requirement (CZK billion)

	2012	2013	Q1-Q3 2014
Gross borrowing requirement	472.0	309.9	224.8
Gross issue of state treasury bills excl. roll-over ¹	189.1	120.9	82.8
Other money market instruments excl. roll-over ¹	0.0	0.0	12.4
Received collateral in cash	0.0	0.0	0.0
Gross issue of CZGB on the domestic market up to 6 years ²	70.4	44.0	46.7
Gross issue of CZGB on the domestic market 6 to 11 years ²	76.3	76.8	44.7
Gross issue of CZGB on the domestic market more than 11 years ²	17.8	24.8	36.5
Gross issue of government bonds on foreign markets ²	69.0	0.0	0.0
Gross issue of retail bonds ³	45.4	39.1	1.6
EIB loans	4.0	4.3	0.0
Other financing sources	0.0	0.0	0.0
Total financing of gross borrowing requirement	472.0	309.9	224.8

¹ Within the respective period.

² Nominal value; premiums and discounts are included in net costs on state debt service, i.e. they are included in the net borrowing requirement.

³ Including reinvestment of yields.

Note: CZGB, 2014–2020, VAR% is included in the gross issue of CZGB on the domestic market up to 6 years and CZGB, 2014–2025, 2.40% is included in the gross issue of CZGB on the domestic market 6 to 11 years.

Source: MoF

Net Borrowing Requirement and Change in State Debt

The net borrowing requirement of the central government is a key factor in the change in the nominal CZK-denominated value of the gross state debt, and is determined by the difference between the gross borrowing requirement and total redemption on the nominal values (principal) of

state debt, including the related derivatives. The net borrowing requirement represents the value of cash resources that the central government must borrow in the current year beyond the resources already borrowed in previous years.

Table 5: Net Borrowing Requirement of the Central Government (CZK billion)

	2012	2013	Q1-Q3 2014
Gross borrowing requirement	472.0	309.9	224.8
Redemption on government bonds in given year	115.6	108.6	98.8
Buy-backs and exchanges government bonds from prior years	-2.0	-8.1	-4.0
Buy-backs and exchanges government bonds due in coming years ¹	8.1	7.5	2.2
Redemption and early redemptions on savings government bonds in the given year	9.6	7.7	8.6
Redemption on state treasury bills excl. roll-over ²	162.6	189.1	112.9
Other money market instruments excl. roll-over ²	0.0	0.0	0.0
Repayments of EIB loans	5.3	2.8	7.5
Net borrowing requirement	172.8	2.3	-1.3

¹ Excluding operations with medium-term and long-term government bonds during current budgetary year.

² Within the respective period.

Source: MoF

The net borrowing requirement is financed using the same instruments as the gross borrowing requirement. In financing the net borrowing requirement, however, it is necessary to take into account the value of total redemption on the nominal values (principal) of the given debt portfolio instruments, including the impact of derivatives. If the resources for covering the financing needs do not include the refinancing mechanism of treasury single accounts and simultaneously there was no change in exchange

rates, the net borrowing requirement as per the current national methodology corresponds to the year-on-year change in the balance of the gross state debt in the domestic currency.

The net debt portfolio is determined by the gross state debt and state financial assets administered by the Ministry. The methodology for determining individual items in the net debt portfolio is set out in the Strategy.

Table 6: Net Borrowing Requirement of the Central Government and Change in State Debt (CZK billion, % of GDP)

	2012	2013	Q1-Q3 2014
Gross state debt as at 1 Jan	1,499.4	1,667.6	1,683.3
Primary state budget balance	59.6	30.4	-8.8
Net expenditures on state debt service ¹	41.4	50.9	43.2
Extra-budgetary financing needs	0.0	0.0	0.0
Net borrowing requirement excl. asset operations	101.0	81.3	34.4
State financial asset operations ²	2.4	2.3	2.5
On-lending (net change) ³	0.0	-1.7	0.0
Cash reserve (net change) ⁴	69.4	-79.5	-38.2
State budget surplus excl. state financial asset operations	0.0	0.0	0.0
Net borrowing requirement	172.8	2.3	-1.3
Net issue of state treasury bills	26.5	-68.2	-30.1
Net change in balance of other money market instruments	0.0	0.0	12.4
Net issue of government bonds on domestic market	42.9	37.7	79.7
Net issue of government bonds on foreign market	69.0	0.0	-48.8
Net issue of retail bonds	35.8	31.4	-7.0
Net change in balance of received loans and credit	-1.3	1.5	-7.5
Financing of net borrowing requirement	172.8	2.3	-1.3
Revaluation of state debt ⁵	-4.4	13.4	1.0
Promissory notes repayments ⁶	-0.1	0.0	0.0
Gross state debt change	168.3	15.7	-0.3
Gross state debt as at the end of period	1,667.6	1,683.3	1,683.0
Share of GDP (%)	41.2	41.2	39.8

¹ Balance of budgetary chapter 396 – State debt.

² Balance of budgetary chapter 397 – State Financial Assets Operations, incl. budgetary transfers.

³ Extra-budgetary loans with maturity of over 1 year granted to other countries and domestic legal entities.

⁴ Cash reserve generated by bonds issues according to Section 35(4) of Act No. 218/2000 Coll, excl. revaluation of the part denominated in foreign currencies due to the exchange rate changes.

⁵ Exchange rate changes due to revaluation of debt denominated in foreign currencies.

⁶ Promissory notes covering part of the Czech Republic ownership interests in international financial institutions.

Source: MoF

Table 7: Balance and Structure of the Net Debt Portfolio (CZK billion)

	2012	2013	30 Sep 2014
Gross state debt	1,667.6	1,683.3	1,683.0
State treasury bills	189.1	120.9	90.8
Other money market instruments	0.0	0.0	12.4
Received collateral in cash	0.0	0.0	0.0
Government bonds issued on domestic market	1,042.0	1,079.7	1,159.4
Government issued on foreign markets	310.3	323.7	275.8
Retail bonds	56.2	87.6	80.6
EIB loans	70.0	71.5	64.0
Promissory notes ¹	0.0	0.0	0.0
Liquid state financial assets	191.5	116.7	81.0
Nuclear investment portfolio	18.5	20.7	22.4
Pension investment portfolio	22.4	22.6	22.7
Special-purpose state financial assets accounts	10.6	10.7	11.4
On-lending ²	0.0	0.0	0.0
Cash reserve ³	139.9	62.7	24.5
State budget surplus	0.0	0.0	0.0
State financial assets	193.2	116.7	81.0
Liquid state financial assets	191.5	116.7	81.0
On-lending ⁴	1.7	0.0	0.0
Net debt portfolio	1,474.4	1,566.7	1,602.0

¹ Promissory notes covering part of the Czech Republic ownership interests in international financial institutions.

² Extra-budgetary loans with original maturity of over 1 year granted to other countries and domestic legal entities and residual maturity less than 12 months.

³ Available cash resources created according to Section 35(4) of Act No. 218/2000 Coll. incl. the impact of exchange rate difference of the CZK value of the part of the cash reserve in foreign currencies.

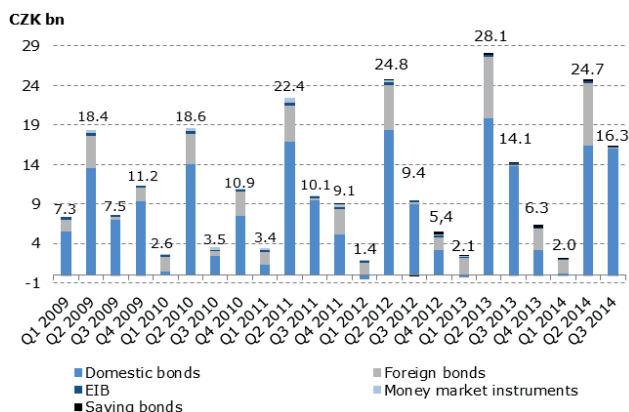
⁴ Extra-budgetary loans with original maturity of over 1 year granted to other countries and domestic legal entities and residual maturity greater than 12 months.

Source: MoF

4 - Interest Costs on State Debt and Cost-at-Risk

The following figure presents an overview of interest expenditure and revenue realised under budgetary chapter 396 – State Debt. More detailed information on the budgeted and actual expenditure and revenue in Q1-Q3 2014 is included in the Appendix. The actual net interest costs on the state debt in Q1-Q3 reached CZK 43.0 billion, which is CZK 1.3 billion lower than the actual net interest costs in the corresponding period in 2013.

Figure 3: Net Interest Costs on the State Debt, 2009-2014

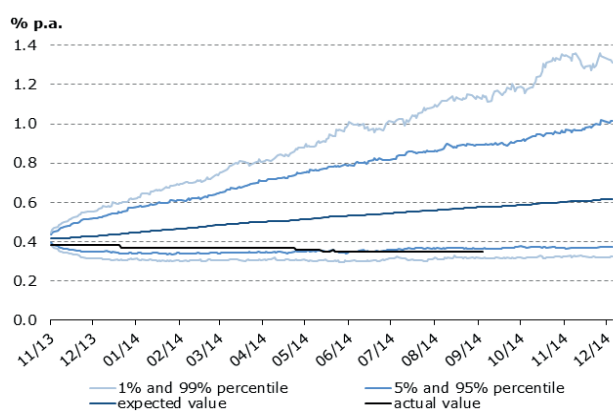


Note: Excl. fees related to the state debt service.
Source: MoF

The state debt interest costs model Cost-at-Risk (CaR) for the year 2014 was published in the Strategy. Calculations of the CaR values are based on term structure of interest rates as of 27 November 2013.

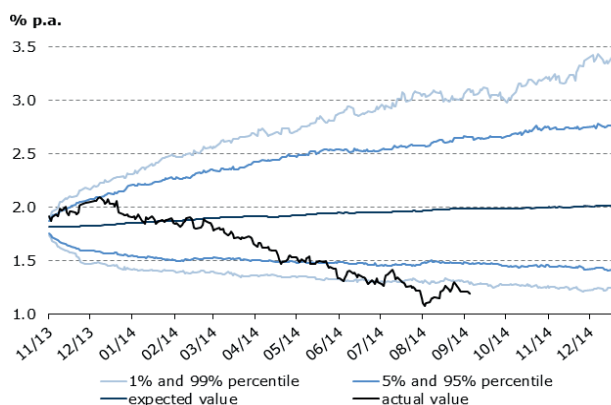
The comparison of the actual development of the 3-month PRIBOR and 10-year swap rates with their simulations for the period from 27 November 2013 to 31 December 2014 are shown in the following figures.

Figure 4: Daily Simulated v. Actual 3-month PRIBOR Interest Rates in 2014



Source: MoF

Figure 5: Daily Simulated v. Actual 10-year CZK Swap Rates in 2014

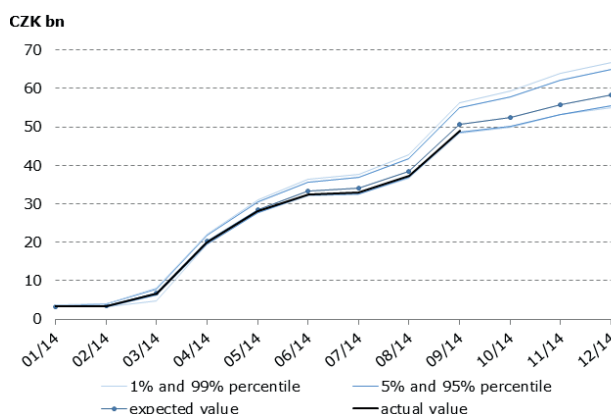


Source: MoF

The development of gross interest costs of the state debt in comparison with simulated costs for 2014 is shown in the following figure. The actual realized gross interest costs amounted to CZK 48.9 billion in Q1-Q3 and were CZK 1.7 billion lower than expected costs of CZK 50.6 billion predicted by the model.

In case of interest revenue, the predicted interest revenue is approx. CZK 1.0 billion higher compared to the actual revenue. The difference is caused primarily by the lower income in terms of auction premiums due to the changes in issuance plan. The fulfilment of the budgeted revenue of the budgetary chapter 396 – State Debt of CZK 7.4 billion is expected in Q4.

Figure 6: Simulated v. Actual Gross Cumulated Interest Costs of the State Debt 2014



Note: Interest costs are calculated on a cash basis in accordance with the current state budget methodology.
Source: MoF

The following table presents a comparison of the actual net interest costs on the state debt, the simulated values of expected costs (average of

simulations) and Cost-at-Risk (95% and 99% percentile of simulations) for Q1-Q3 in comparison to the corresponding period in 2013.

Table 8: Expected v. Actual Net Interest Costs in Q1-Q3 2013 and Q1-Q3 2014 (CZK billion)

	Q1-Q3 2013	Q1-Q3 2014
Actual net interest costs	44.3	43,0
Expected (simulated) net costs	45.5	43,7
Cost-at-Risk 95%	53.3	50,4
Cost-at-Risk 99%	56.8	52,1
Deviation of expectation from actuality	1.2	0,7

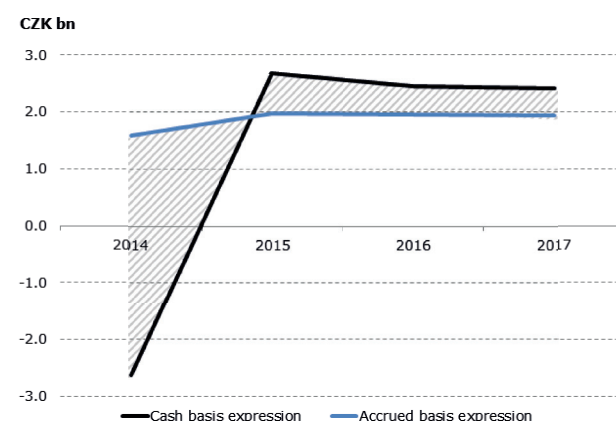
Source: MoF

In Q1-Q3, the actual net interest costs on the state debt amounted to CZK 43.0 billion. The expected net interest costs for the same period predicted by the model were CZK 43.7 billion. The actual net interest costs thus remained below the level of both CaR 95% and CaR 99%, which were set at CZK 50.4 billion and CZK 52.1 billion, respectively. The primary goal of the model was fulfilled when net interest costs did not exceed CaR levels. The model estimated the net interest costs to be CZK 0.7 billion higher than the actual net interest costs.

Although the budgetary chapter 396 – State Debt is budgeted on a cash basis, the Ministry also monitors the costs of the state debt portfolio on an accrual basis, as an accrual expression provides more realistic picture of the actual costs of that year. The net interest costs of the state debt issued in first half of 2014 expressed on an accrual basis reached CZK 1.6 billion in 2014 compared to CZK -2.6 billion expressed on a cash basis, i.e. on a cash basis, the newly issued debt in first half of 2014 brought a revenue of the state budget, as the effect of auction premium of CZK 4.8 billion prevailed. The difference between accrual and cash basis expression of costs is shown in the following figure. While the costs expressed on accrual basis

are relatively stable in each year, as in 2014, the costs amount to CZK 1.6 billion, in 2015, the costs amount to its maximum value of CZK 2.0 billion, in 2016 and 2017, the costs will slowly decrease. A different trend can be seen in the net interest costs of the same debt on cash basis, as in this year, the net interest costs amount to CZK -2.6 billion, in 2015, the net interest costs amount to CZK 2.7 billion and in 2016 and 2017, the net interest costs amount to approx. CZK 2.4 billion.

Figure 7: Net Accrued and Cash Interest Costs of Newly Issued Debt



Source: MoF

Table 9: Accrued Interest Costs of the Newly Issued State Debt (CZK billion)

	Nominal value	Net interest costs			
		2014	2015	2016	2017
Cash basis expression	212.2	-2.6	2.7	2.4	2.4
Accrued basis expression	212.2	1.6	2.0	2.0	1.9
Gross issuance of CZGB	127.9	1.5	1.9	1.9	1.9
Gross issuance of state treasury bills	82.8	0.0	0.0	-	-
Foreign issues	-	-	-	-	-
Gross issuance of savings government bonds	1.4	0.0	0.0	0.0	0.0
Drawing of EIB loans	-	-	-	-	-

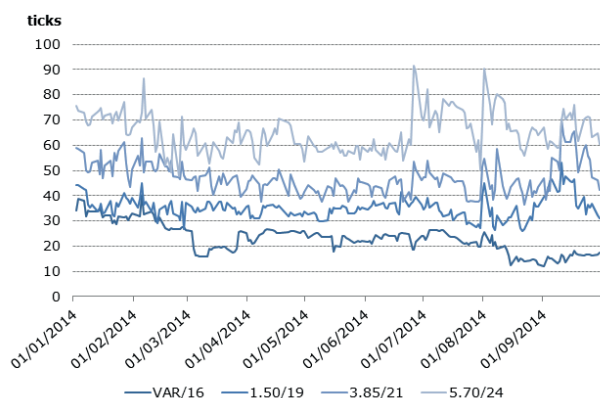
Note: Excl. reinvestments of yields.
Source: MoF

5 - Secondary Market of Government Bonds

The MTS Czech Republic trading platform for Czech government bonds, which Ministry implemented on July 2011, considerably contributes to the efficiency and transparency of the domestic secondary market of government bonds. The key parameter of the effective price discovery on the secondary market of government bonds is the bid-offer spread of the given government bond. The narrower the bid-offer spread is the more liquid and effective the market is.

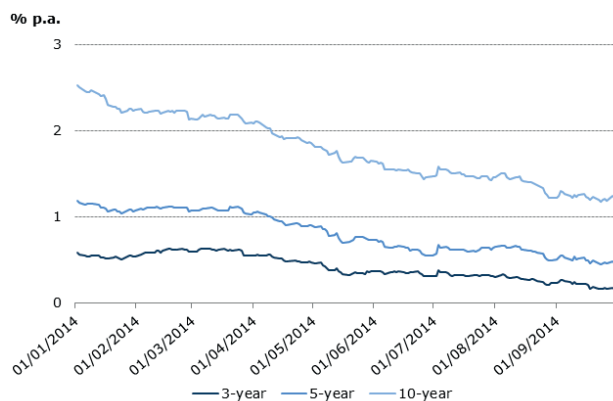
Since the beginning of 2014, the volatility and slight decrease of bid-offer spread can be observed. The most significant volatility can be observed in Q3 particularly regarding the government bonds on the long end of the yield curve. The bid-offer spread of the Czech variable-rate government bond maturing in 2016 has been constant in the previous two quarters of the year.

Figure 8: Average Quoted Bid-offer Spreads on MTS CR in Q1-Q3 2014



Source: EuroMTS and MoF

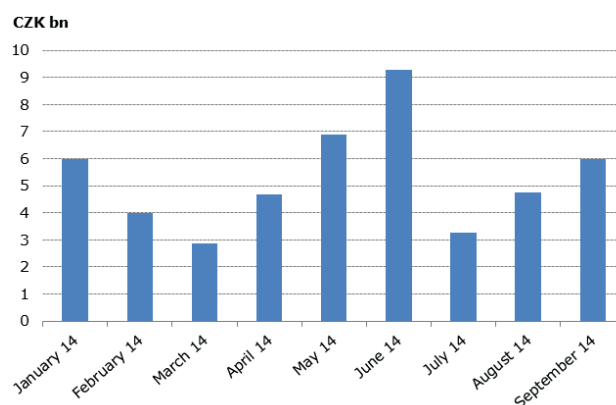
Figure 9: Yields of Government Bonds Traded on MTS CR in Q1-Q3 2014



Source: EuroMTS and MoF

The total monthly nominal value of government bonds traded on MTS Czech Republic trading platform amounted to CZK 4.7 billion on average in Q3, which represents the decrease of ca CZK 2.3 billion in comparison to Q2 caused mainly due to the lower activity during the holidays. In September, the activity on the secondary market of government bonds rose to an above average level in 2014, amounting CZK 5.3 billion.

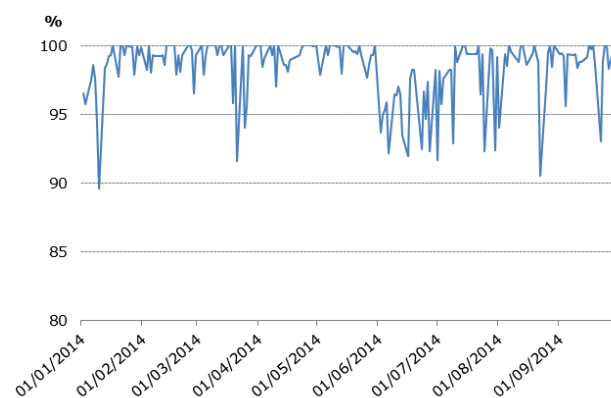
Figure 10: Nominal Value of Transactions on MTS CR in Q1-Q3 2014



Source: EuroMTS and MoF

The obligations of Primary Dealers on the secondary market include fulfilling of criteria of the minimum quoted total nominal value according to bond maturity, the minimum quoted time during one trading day and the maximum quoted spread on bonds subject to quoting obligations. The Daily Compliance Ratio ("DCR") is established each day on the basis of these obligations. On these obligations the daily fulfilment of quoting obligation is based every day, where on monthly basis every Primary Dealer is obliged to fulfil the DCR at least at 90.0%.

Figure 11: Average Daily Quoting Obligation Fulfilment - Daily Compliance Ratio in Q1-Q3 2014



Source: EuroMTS and MoF

The average DCR of Primary Dealers oscillated below 100% level in all three previous months, which means that the long-term development from previous periods, when the DCR didn't fall below 90%, has continued.

Also in Q3, the Ministry allowed using a lending facility for providing lending of government bonds. Primary Dealers may use this facility for borrowing government bonds for a period up to 90 days within repo operations. Although the primary goal of these operations is to increase the liquidity of government

bonds on secondary market, especially in case of the short-term excess of demand over the supply of the particular bond, due to the very low repo rates, the Ministry considers these operations as a preferred source in the segment of short-term financing of the borrowing requirement. These operations thereby also contribute to savings on net interest costs on the state debt. The acquired financial funds are invested for higher yield on the money market under state treasury liquidity management, which leads to an increase in the yields from the investment activities of the Ministry.

Table 10: Realized Lending Facilities of Government Bonds in Q3 2014

Instrument	ISIN	Collateral amount	Financial funds received	Financial funds paid
CZGB 0.50/16	CZ0001003842	3,010,000,000.00	3,029,908,527.78	3,029,840,816.28
CZGB VAR/16	CZ0001002331	340,000,000.00	341,724,022.22	341,718,041.67
CZGB VAR/17	CZ0001003438	447,000,000.00	462,392,072.50	462,391,622.95
CZGB 4.00/17	CZ0001001903	25,000,000.00	27,833,750.00	27,833,100.55
CZGB 0.85/18	CZ0001004246	460,000,000.00	468,270,178.09	468,258,972.13
CZGB 4.60/18	CZ0001000822	2,685,000,000.00	3,152,126,288.88	3,152,058,483.13
CZGB 1.50/19	CZ0001003834	200,000,000.00	210,691,666.67	210,687,365.05
CZGB 5.00/19 ¹	CZ0001002471	250,000,000.00	306,511,111.11	306,503,703.76
CZGB 3.75/20	CZ0001001317	200,000,000.00	235,408,333.33	235,402,497.25
CZGB 3.85/21	CZ0001002851	3,520,000,000.00	4,285,111,319.44	4,285,029,939.92
CZGB 4.70/22	CZ0001001945	310,000,000.00	401,661,000.00	401,651,469.86
CZGB VAR/23	CZ0001003123	8,068,190,000.00	8,632,135,706.66	8,631,835,592.14
CZGB 5.70/24 ¹	CZ0001002547	4,002,000,000.00	5,639,888,233.33	5,639,760,974.66
CZGB 2.40/25	CZ0001004253	1,100,000,000.00	1,195,764,109.59	1,195,744,395.58
CZGB VAR/27	CZ0001004105	1,520,000,000.00	1,497,819,341.66	1,497,764,849.63
CZGB 2.50/28	CZ0001003859	2,017,590,000.00	2,204,086,984.61	2,204,086,984.61
CZGB 4.85/57	CZ0001002059	25,000,000.00	34,075,104.17	34,074,292.29
Total		28,179,780,000.00	32,125,407,750.04	32,124,643,101.46

¹ Collateral used from the Ministry's portfolio and investment nuclear portfolio.
Source: MoF

In Q3, medium-term and long-term government bonds in a total nominal value of CZK 28.2 billion were provided from the Ministry's portfolio, from the nuclear investment portfolio, and from received collateral from reverse repo operation under state treasury liquidity management through the lending facility against received financial funds in the amount of CZK 32.1 billion, which were invested

on the money market under state treasury liquidity management and under financial assets operations within the nuclear portfolio. The interest in the lending facilities has been high during 2014 despite the fact, that there are long-term declines in yields of Czech government bonds. In Q3, the average repo rate achieved under the lending facility was -0.03% p.a.

6 - State Treasury Liquidity Management

The total state treasury resources are subdivided into the two separate single accounts, which are distinguished by the currency, i.e. CZK single account and EUR single account. The treasury liquidity management is performed separately on

both single accounts. In accordance with Act No. 218/2000 Coll., on the budgetary rules, the balance of the particular treasury single account cannot be negative.

Table 11: State and Structure of Resources and Investment Position of State Treasury (CZK, EUR billion)

	2012		2013		30 Sep 2014	
	CZK	EUR	CZK	EUR	CZK	EUR
Liquid state financial assets	162.3	1.2	94.0	0.8	68.5	0.5
National Fund and former National Property Fund	15.8	0.0	19.2	2.2	32.1	2.1
Other mandatory clients of state treasury	20.5	0.0	76.9	0.0	66.6	0.0
Optional clients of state treasury	0.0	0.0	4.4	0.0	12.3	0.0
Liabilities to the state treasury (-)	0.0	0.0	0.0	0.0	0.0	0.0
Total liquidity position of the state treasury¹	198.7	1.2	194.5	3.0	179.4	2.6
Reverse repo operations (T-bills collateral)	5.2	0.0	18.0	0.0	2.0	0.2
Reverse repo operations (T-bonds collateral)	0.0	0.0	0.0	1.4	0.0	0.5
Reverse repo operations (CNB bills collateral)	158.5	0.0	141.5	0.0	146.9	0.4
Reverse repo operations (foreign securities collateral)	0.0	0.0	0.0	0.0	0.0	0.0
Provided deposits and short-term borrowings and loans	13.1	0.0	14.0	1.0	15.1	1.5
On-lending ²	1.7	0.0	0.0	0.0	0.0	0.0
Investment in T-bills and T-bonds	18.5	0.0	19.2	0.0	15.5	0.0
Investment in foreign securities	0.0	0.0	0.0	0.0	0.0	0.0
Provided collateral (in cash)	0.0	0.0	0.0	0.0	0.0	0.0
Cash resources in CZK treasury single account ³	1.6	1.2	1.8	0.7	0.0	0.0
Ministry's cash resources in commercial banks accounts	0.0	0.0	0.0	0.0	0.0	0.0
Total investment position of the state treasury	198.7	1.2	194.5	3.0	179.4	2.6

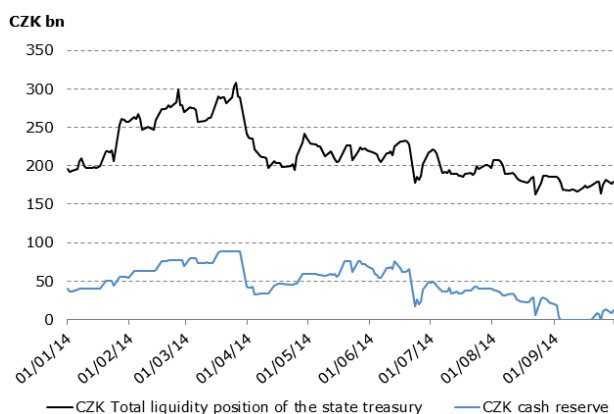
¹ Available liquidity of the state treasury incl. investments outside state treasury liquidity management accounts.

² Extra-budgetary lending to other states and on-lending to institutions with state-backed guarantees for their core business with original maturity longer than 1 year and expected residual maturity less than 12 months.

³ Until 31/3/2013 it is a part of the cash reserve denominated in EUR, as the CNB established the treasury single account in EUR for the Ministry of Finance on 2/4/2013.

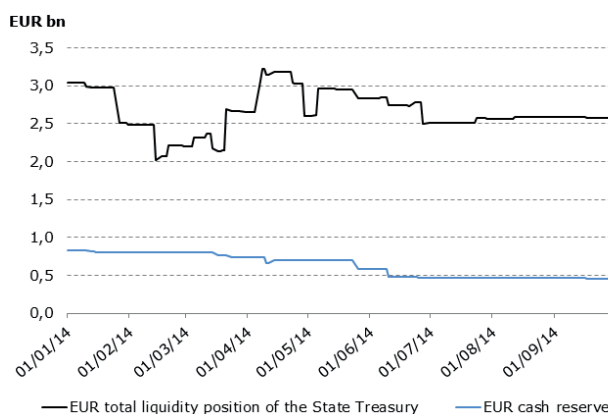
Source: MoF

Figure 12: Total liquidity position of the CZK State Treasury Balance and the Cash Reserve



Source: MoF

Figure 13: Total liquidity position of the EUR State Treasury Balance and the Cash Reserve



Source: MoF

Within the CZK state treasury liquidity management and the state financial assets investment operations in the nuclear portfolio, short-term investments with the use of the CNB bills and state treasury bills as a collateral in total nominal value of CZK 3,769.6 billion were carried out in Q1-Q3 2014. The average interest rate achieved when investing with the use of this collateral was 0.04% p.a. Within the CZK state treasury liquidity management, short-term investments in form of deposit operations in total nominal value of CZK 1,277.6 billion were carried out in Q1-Q3 2014. The average interest rate achieved when investing in form of deposit operations was 0.04% p.a.

Within the EUR state treasury liquidity management, short-term investments with the use of the short-term, medium-term and long-term government bonds as collateral in total nominal value of EUR 9.0 billion were carried out in Q1-Q3 of 2014. The average interest rate achieved when investing with the use of medium-term and long-term government bonds as collateral was 0.21% p.a. Within the EUR state treasury liquidity management, short-term investments in form of deposit operations in total nominal value of EUR 12.0 billion were carried out in Q1-Q3 of 2014. The average interest rate achieved when investing in form of deposit operations was 0.19% p.a.

Appendix

State Debt and Liquid State Financial Assets Parameters

Table 12: State Debt Parameters

	30 Sep 2013	31 Dec 2013	31 Mar 2014	30 Jun 2014	30 Sep 2014
Total state debt (CZK billion)	1,653.5	1,683.3	1,683.4	1,683.3	1,683.0
Market value incl. derivatives (CZK billion)	1,831.5	1,863.3	1,886.1	1,903.9	1,911.1
Short-term state debt (%)	15.4	15.8	12.1	12.7	16.1
Medium-term state debt (%)	54.7	53.6	50.5	53.8	53.6
Share of state treasury bills (%)	8.3	7.2	5.8	5.8	5.4
Other money market instruments (%)	0.1	0.0	0.2	0.7	0.7
Average time to maturity (years)	5.7	5.6	5.7	5.7	5.5
Interest re-fixing up to 1 year (%)	35.0	35.4	31.8	32.8	36.4
Average time to re-fixing (years)	4.4	4.3	4.5	4.5	4.3
Variable-rate state debt (%)	16.7	16.8	17.1	17.8	18.0
Modified duration (years)	4.0	4.0	4.1	4.2	4.1
Modified duration excl. CZK IRS (years)	4.0	3.9	4.1	4.2	4.1
Net foreign currency exposure of the state debt (%)	8.8	9.4	9.6	10.0	10.1
Foreign currency state debt (%)	18.2	19.0	19.0	16.6	16.6
Share of € on net foreign currency exposure of the state debt (%)	88.8	89.4	89.4	89.8	89.8
Non-marketable state debt (%) ¹	4.1	4.2	4.2	4.0	3.8
Retail state debt (%)	4.5	5.2	5.2	4.8	4.8
Marketable debt (CZK billion)	1,511.9	1,524.2	1,525.6	1,535.7	1,538.4
Market value (CZK billion)	1,683.1	1,696.2	1,720.0	1,747.4	1,757.7
Short-term marketable debt (%)	15.7	16.6	12.4	13.6	17.2
Medium-term marketable debt (%)	54.3	52.7	49.3	52.9	52.6
Share of money market instruments (%)	9.1	7.9	6.4	6.4	5.9
Lending facility - government bonds (%)	0.1	0.0	0.2	0.8	0.8
Average time to maturity (years)	5.6	5.5	5.6	5.7	5.5
Interest re-fixing up to 1 year (%)	32.9	33.7	29.7	31.4	35.4
Average time to re-fixing (years)	4.6	4.6	4.7	4.8	4.5
Variable-rate marketable debt (%)	13.9	13.9	14.2	15.1	15.5
Modified duration (years)	4.2	4.1	4.3	4.5	4.3
Modified duration excl. CZK IRS (years)	4.2	4.1	4.3	4.5	4.3
Net foreign currency exposure of the state debt (%)	9.7	10.4	10.6	11.0	11.0
Foreign currency state debt (%)	19.9	21.0	21.0	18.2	18.2
Share of € on the net foreign currency exposure of the state debt (%)	88.8	89.4	89.4	89.8	89.8

¹ Excl. retail state debt.
Source: MoF

Table 13: Parameters of Liquid State Financial Assets

	30 Sep 2013	31 Dec 2013	31 Mar 2014	30 Jun 2014	30 Sep 2014
Liquid state financial assets (CZK billion)	138.9	116.7	160.1	117.6	81.0
Share of assets up to one year on total state debt (%)	7.5	6.0	8.6	6.4	4.3
Interest re-fixing up to one year (%)	89.5	86.8	90.3	91.8	91.2
Average time to re-fixing (years)	0.4	0.5	0.3	0.4	0.5
Investment portfolios	42.9	43.3	43.7	44.6	45.0
Average yield (%)	1.3	1.3	1.3	1.3	1.2
Average time to maturity (years)	1.5	1.4	1.3	1.2	1.1
Modified duration (years)	0.9	1.1	0.9	0.9	0.8

Source: MoF

Medium-term and Long-term Government Bonds and Treasury Bills Issues in Q3 2014

Table 14: Issues of Medium-term and Long-term Government Bonds in Q3 2014

Instrument	Issue/ tranche no.	Auction date	Settlement date	Maturity date	Currency	Max. nominal value offered in the competitive part of auction	Total nominal value sold
CZGB 0.85/18	88/4	17/9	22/9	17/3/2018	CZK	5,000,000,000	5,347,690,000
CZGB VAR/27	90/3	17/9	22/9	19/11/2027	CZK	8,000,000,000	5,511,190,000
Total							10,858,880,000

Instrument	Issue/ tranche no.	Coupon	Average net price	Average yield to maturity (% p.a.)	Bid-to- cover ratio	Sold in the competitive part of the auction/ max. nominal value offered	Sold in the non- competitive part of the auction/ max. nominal value offered
CZGB 0.85/18	88/4	0.85 %	102.21	0.212	3.66	100.00	7.00
CZGB VAR/27	90/3	VAR %	99.15	-3.430 ¹	2.77	62.50	6.39
Average						76.9	6.61

¹ Discount margin
Source: MoF

Table 15: Treasury Bills Issues in Q3 2014

Issue no.	Maturity (months)	Auction date	Issue date	Maturity date	Offered nominal value	Placed nominal value	Yield (% p.a.)
696	12	10/7	11/7	10/7/2015	6,000,000,000 to 8,000,000,000	6,413,000,000	0.08
697	9	24/7	25/7	24/4/2015	6,000,000,000 to 8,000,000,000	5,583,000,000	0.07
698	12	4/9	5/9	4/9/2015	4,000,000,000 to 6,000,000,000	6,000,000,000	0.07
699	9	25/9	26/9	26/6/2015	4,000,000,000 to 6,000,000,000	4,000,000,000	0.06
Total					20,000,000,000 to 28,000,000,000	21,996,000,000	0.07¹

¹ Average weighted yield to maturity of treasury bills issues in Q3 2014.
Source: MoF

Table 16: Tap Sales in Q3 2014

Instrument	Issue no.	Transaction date	Settlement date	Maturity date	Original maturity (years)	Average price	Nominal value
CZGB VAR/16	55	23/9	26/9	27/10/2016	8.0	100.560	100,000,000
CZGB VAR/16	55	25/9	30/9	27/10/2016	8.0	100.510	100,000,000
Total							200,000,000

Note: Tap sales include only operations carried out through MTS Czech Republic.
Source: MoF

Table 17: Buy-backs in Q3 2014

Instrument	Issue no.	Transaction date	Settlement date	Maturity date	Original maturity (years)	Average price	No. of counter-parties	Nominal value
CZGB 3.80/15	44	10/9	15/9	11/4/2015	10,0	102,146	2	350,000,000
CZGB 3.40/15	60	12/9	17/9	1/9/2015	5,5	103,203	1	500,000,000
CZGB 6.95/16	34	12/9	17/9	26/1/2016	15,0	109,370	1	50,000,000
CZGB 3.80/15	44	16/9	19/9	11/4/2015	10,0	102,105	1	100,000,000
CZGB 3.40/15	60	19/9	24/9	1/9/2015	5,5	103,139	1	55,000,000
CZGB 6.95/16	34	19/9	24/9	26/1/2016	15,0	109,230	1	162,000,000
CZGB 3.40/15	60	23/9	26/9	1/9/2015	5,5	103,119	1	1,000,000,000
Total								2,217,000,000

Note: Buybacks include only operations carried out through MTS Czech Republic and Thomson Reuters Dealing 3000.
Source: MoF

Table 18: Redemption and Re-fixing Profile of Domestic Government Bonds Issues in Q3 2014

Domestic government bonds	Placed nominal value	Average time to maturity at the issue date	Average time to maturity at 31/12/2014	Average time to re-fixing at the issue date	Average time to re-fixing at 31/12/2014
Fixed rate	5,347,690,000	3.5	3.2	3.5	3.2
Floating rate	5,511,190,000	13.2	12.9	0.2	0.4
Total	10,858,880,000	8.4	8.1	1.8	1.8

Note: Nominal value in CZK; average time to maturity and re-fixing in years.
Source: MoF

Budgetary Revenues and Expenditures on the State Debt in 2014

Table 19: Planned and actual budgetary expenditures and revenues on state debt in 2014

Indicator (CZK million)	Actual Q1-Q3 2013	Budget 2014		Actual Q1-Q3 2014	% execution	2014/2013 (%)
	1	Approved	After changes	4	5=4/3	6=4/1
1. Total interest expenditure and revenue	50,993 (-) 6,733	65,199 (-) 7,400	64,227 (-) 7,400	48,936 (-) 5,948	76.2 80.4	96.0 88.4
Domestic debt	40,207 (-) 6,624	51,161 (-) 6,952	50,189 (-) 6,952	38,485 (-) 5,858	76.7 84.3	95.7 88.4
Money market instruments	184 (-) 138	944 (-) 64	944 (-) 64	55 (-) 188	5.8 293.7	29.7 136.6
Of which: derivative operations	36	-	-	-	-	-
Savings government bonds	173 0	1 251 -	1 251 -	228 0	18.2 -	131.3 -
Government bonds	39,849 (-) 6,486	48,966 (-) 6,888	47,994 (-) 6,888	38,203 (-) 5,670	79.6 82.3	95.9 87.4
Foreign debt	10,784 (-) 101	14,028 (-) 448	14,028 (-) 448	10,450 (-) 91	74.5 20.2	96.9 90.0
International issues	10,215 (-) 101	13,142 (-) 448	13,142 (-) 448	9,993 (-) 91	76.0 20.2	97.8 90.0
Of which: derivative operations	2,885 (-) 101	3,103 (-) 448	3,103 (-) 448	2,192 (-) 91	70.6 20.2	76.0 90.0
Loans from EIB	568	886	886	457	51.5	80.3
Bank accounts	2 (-) 8	10 -	10 -	1 0	7.1 -	31.8 -
Bank accounts interests (+ paid, - received)	2 (-) 8	10 -	10 -	1 0	7.1 -	31.8 -
2. Total fees	298 -	599 -	599 -	181 0	30.2 -	60.7 -
Total balance	51,291 (-) 6,733	65,798 (-) 7,400	64,826 (-) 7,400	49,117 (-) 5,948	75.8 80.4	95.8 88.4

Note: (-) means revenues (gains).

Source: MoF

The total **net expenditures** on the state debt service in Q1-Q3 amounted **CZK 43.2 bn**. Revenues from accrued interest yields and bond

premiums contributed CZK 5.7 bn to reduction of the gross expenditures on the state debt service which reached CZK 49.1 bn.

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www.mfcr.cz/statedebt

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