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## **PERFORMANCE EVALUATION OF PRIMARY DEALERS IN CZECH GOVERNMENT SECURITIES |September 2012|**

The Ministry of Finance (hereinafter the Ministry) hereby presents its regular Performance Evaluation of Primary Dealers in Czech Government Securities. The Primary Dealers are evaluated for Q4 2011 to the end of Q3 2012. As from 1 October 2011, the evaluation methodology has changed significantly. This change is related to implementation of the pan-European MTS Czech Republic electronic platform for trading on the domestic secondary bond market from 1 July 2011 and to signature of the *Primary Dealer Agreement for Czech Government Securities* (hereinafter the Agreement) by the Ministry and the Primary Dealers on 1 October 2011. Conclusion of the Agreement established a new and more efficient trading structure, as is common in other advanced countries of the European Union and which brought standardisation and professionalism to the cooperation in financing and managing the state debt as well as its complete transparency. The modernisation of this framework was rounded off by publication of the new *Rules for the Primary Sale of Government Securities organized by the Czech National Bank*, which came into effect on 1 January 2012. Under this newly formalised framework, and on the basis of the consensually agreed

rules, the Ministry became active on the secondary market after an almost two-year break, in particular by directly buying back government bonds before their maturities and by tap sales of government bonds from the Ministry's own portfolio.

Starting with the Performance Evaluation of Primary Dealers in Czech Government Securities for 2011, the Ministry has been publishing the point scores obtained by individual Primary Dealers in the published evaluation groups. The Ministry expects to achieve greater transparency by this step. In accordance with the Amendment Agreement signed on 30 June 2012 also the first seven Primary Dealers are published (only five Primary Dealers were published in accordance with the old Agreement). Other Primary Dealers receive a notification with the outcome of their performance evaluation.

Starting with this performance Evaluation of Primary Dealers in Czech Government Securities, the Primary Dealers are evaluated exclusively by the new methodology published in the new Agreement.

### **Evaluation for Q4 2011 to Q3 2012**

The performance evaluation of Primary Dealers in Czech government securities for Q4 2011 to Q3 2012 was performed according to the evaluation methodology **valid from 1 October 2011**. The methodology is part of the Agreement. In order to attain an overall and objective evaluation of Primary Dealers' activities, the performance evaluation is based on three criteria: sub-criteria for the evaluation of Primary Dealers' activities on the primary market (Criterion A), sub-criteria for the evaluation of Primary Dealers' activities on the secondary market (Criterion B), and sub-criteria for the evaluation of the effectiveness of derivative operations, marketing and sovereign advisory (Criterion C).

The fact that the weights for criteria A and B are similar reflects the increased importance of the secondary market, which enables the evaluation of active market

makers in relation to performance in primary auctions of government bonds. The performance evaluation of each Primary Dealer can reach a maximum of 100 points, and this score is calculated on a relative basis. Primary Dealers' activities are thus evaluated quarterly on the basis of the APEI (Aggregate Performance Evaluation Index defined in Attachment I of the Agreement), and always for four consecutive evaluated periods. According to Article I of the Agreement, each calendar quarter is an evaluated period, starting from 1 October 2011.

Within evaluated activities on the primary market, a given Primary Dealer's primary auctions share (i.e. the share of total nominal value of bids submitted by the Primary Dealer on total nominal value of government bonds sold in all government bond auctions during the

evaluated period) is monitored under the sub-criterion A.1. Using the ratio of accepted bids of the Primary Dealer to the total nominal value of bids submitted by the Primary Dealer, under the sub-criterion A.2. the Ministry monitors investors' willingness to hold Czech government bonds. Another important aspect of evaluation of participation on the primary market is the auction pricing strategy under the sub-criterion A.3., through which the Ministry evaluates Primary Dealers' willingness to offer higher price. Under the sub-criterion A.4., the Primary Dealer is rated better if it is a regular auction participant. The maximum number of points under the sub-criterion A.5. is given to the Primary Dealer that subscribes the largest share of government treasury bills sold by the Ministry in the given period.

The quantitative criterion B is based particularly on statistical and monitoring instruments available on the MTS Czech Republic platform and focuses on quotation activities, their quality, traded nominal values of benchmark issues and trades with the Ministry. The most important indicator is the sub-criterion B.1., the Compliance Ratio, which evaluates the quotation activities of the Primary Dealer based on the quotation duration of bonds subjected to quoting obligations, where maximum allowed spread between bid and offer price condition and minimum nominal value of quotation condition (both defined in *MTS Czech Republic Market Rules*) must be fulfilled. If a Primary Dealer does not fulfil this sub-criterion by at least 90.0% (i.e. the value

unanimously approved at the first MTS Czech Republic Committee meeting on 20 September 2011) on a monthly basis, it obtains 0.0 points for the given month. Sub-criterion B.2. evaluates the quality of the quotation activities of the Primary Dealer regarding bonds both subjected and not subjected to quoting obligations on DETS based on bonds' duration, bid/offer spread, nominal value of quotation and duration of quotation. Under the sub-criterion B.3., the Primary Dealer is evaluated based on bonds' total nominal value traded on MTS Czech Republic platform taking bonds' duration and number of executed transactions into account, where transactions on the side of provider of quotation have greater weight. Under the sub-criterion B.4., the Primary Dealer is evaluated based on its share on total nominal value of secondary market operations executed by the Ministry during the evaluated period according to particular types of operation (repo operation, buy/sell back operations, depo, tap sales and buy-backs of government bonds on the secondary market).

The qualitative criterion C focuses on derivative operations, marketing and sovereign advisory. Primary Dealers are evaluated in ascending order according to the prices of various derivative instruments they provided and their long-term contribution to the effectiveness of the state debt management. The Ministry also evaluates the quality of advisory services, ability to cooperate and share information, technical and human resources in relation to risk management, and optimization of the debt portfolio.

#### Criteria, sub-criteria and their weights for evaluating Primary Dealers valid as of 1 October 2011

A. Primary market	45.0	B. Secondary market	40.0	C. Qualitative criterion	15.0
A.1. Primary Auctions Share - Government Bonds	25.0	B.1. Market-making Obligations on DETS (Compliance Ratio)	10.0	C.1. Derivative Pricing and Credibility	5.0
A.2. Dependability	5.0	B.2. Qualitative Performance on DETS	10.0	C.2. Marketing & Sovereign Advisory	10.0
A.3. Auction Pricing strategy	5.0	B.3. Traded Volume on DETS	10.0		
A.4. Auction participation	2.5	B.4. Debt Management Market Operations	10.0		
A.5. Primary Auctions Share - Treasury Bills	7.5				

Source: Ministry of Finance

Given the varying performance levels of individual Primary Dealers on the primary and secondary markets, the Ministry decided to publish both the overall ranking of Primary Dealers as well as the rankings of Primary

Dealers on the individual markets. Activities of all 13 Primary Dealers were evaluated for Q4 2011 to Q3 2012.

**Overall evaluation for Q4 2011 to Q3 2012**

Ranking	Primary Dealer	Points*
<b>1st</b>	<b>Erste Group Bank AG / Česká spořitelna, a.s.</b>	<b>71.2</b>
2nd	KBC Bank NV / Československá obchodní banka, a.s.	70.3
3rd	PPF banka a.s.	68.9
4th	Société Générale / Komerční banka, a.s.	68.2
5th	Citibank Europe plc	58.5
6th	UniCredit Bank Czech Republic, a.s.	53.4
7th	Goldman Sachs International	38.7

\* max. 100 points  
Source: Ministry of Finance

**Primary market for Q4 2011 to Q3 2012**

Ranking	Primary Dealer	Points*
<b>1st</b>	<b>PPF banka a.s.</b>	<b>34.4</b>
2nd	Erste Group Bank AG / Česká spořitelna, a.s.	32.8
3rd	Société Générale / Komerční banka, a.s.	27.0
4th	UniCredit Bank Czech Republic, a.s.	26.1
5th	KBC Bank NV / Československá obchodní banka, a.s.	23.9
6th	Citibank Europe plc	15.2
7th	Deutsche Bank AG	13.6

\* max. 45 points  
Source: Ministry of Finance

**Secondary market for Q4 2011 to Q3 2012**

Ranking	Primary Dealer	Points*
<b>1st</b>	<b>KBC Bank NV / Československá obchodní banka, a.s.</b>	<b>31.4</b>
2nd	Citibank Europe plc	29.9
3rd	Société Générale / Komerční banka, a.s.	29.8
4th	PPF banka a.s.	24.5
5th	Erste Group Bank AG / Česká spořitelna, a.s.	23.5
6th	UniCredit Bank Czech Republic, a.s.	16.8
7th	Goldman Sachs International	15.4

\* max. 40 points  
Source: Ministry of Finance

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The next Performance Evaluation of Primary Dealers in Czech Government Securities will be published  
on 31 January 2013 at 14:00

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