



Debt Portfolio Management Quarterly Review

JUNE 2010

The Ministry of Finance submits the twenty second *Debt Portfolio Management Quarterly Review* to present the underlying debt portfolio risk management measures and performance with respect to the planned annual financing programme and achieving the medium-term strategic targets of debt management policy. For the year 2010, these targets were quantified by the *Financing and Debt Management Strategy for 2010* released on 3 December 2009 and based on the Finance Minister's decision. The Strategy specifies operating space of the asset and liability management through issuance activity, financial investment and active operations of MoF on secondary market of government bonds and financial derivatives.

I. Review of Strategic Targets for 2010

The 2010 state debt management policy is guided by the set of quantitative targets and criteria approved by the Minister of Finance for issuance activities and the active management of debt portfolio as summarized in the following table.

Financing programme and strategic targets in 2010

Criterion	Guidelines for 2010	June 30, 2010
International issues	Max. 50 % of the total annual gross borrowing requirement CZK 0.0 to 140.0 bn	0,0 % CZK 0.0 bn
Gross government bonds issues	CZK 102.3 to 292.3 bn	CZK 85.6 bn
Net money market issues	CZK -25.0 to +25.0 bn	CZK 1.0 bn
Loans from EIB	CZK 12.7 bn	CZK 3.3 bn
Short-term state debt	20 % and less	16.4 %
Average time to maturity	5.5 to 7.0 years	6.3 years
Interest Rate Re-fixing	30 to 40%	31.7 %

Note: EIB – European Investment Bank. Source: MF CR.

As regards **international funding**, the Czech Republic has drawn one tranche of loans from the European Investment Bank in the amount of **CZK 0.8 billion** during the second quarter. During the first half of 2010, loans were drawn in total amount of CZK 3.3 billion, which represents 25.9 % of the limit in the State Budget Act for 2010.

Regarding **domestic issuance activity**, the total gross issuance of government bonds reached **CZK 45.3 billion** during second quarter, from which tap sales were executed in the amount of CZK 1.0 billion via Reuters Dealing system and the tap sales were also bought by the European Investment Bank in the amount of CZK 2.0 billion. During the first half, the total gross issuance reached CZK 85.6 billion, including CZK 2.5 bn tap sales executed via Reuters Dealing system and CZK 4.0 bn bought by EIB. The total gross issuance reached about 29.3 % of the maximal supply initially announced on 3 December 2010. The net issuance of government bonds was **CZK 24.4 billion** during the second quarter (CZK 64.6 bn during the first half). Buy-backs of government bonds were not executed during the second quarter as well as during the first half 2010.

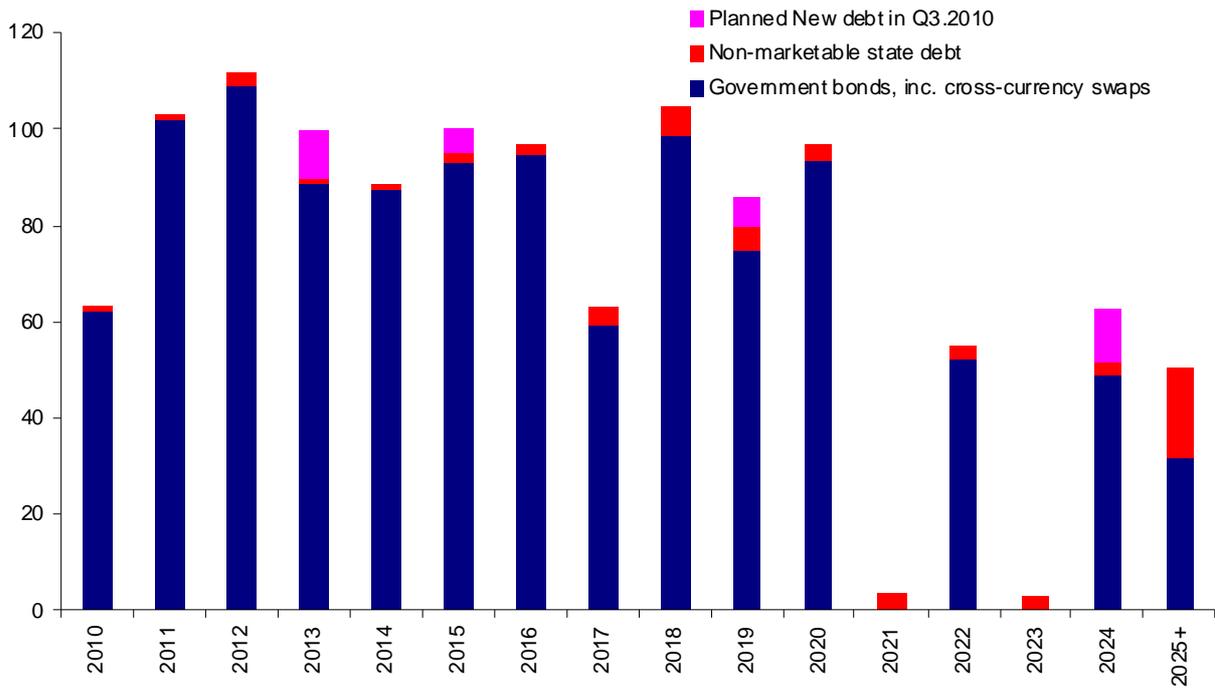
The volume in issue of money market instruments increased by **CZK 1.7 billion** during the second quarter (CZK 1.0 bn during the first half 2010).

The short-term state debt increased by 2.2 percentage points and reached the share of **16.4 %** at the end of the second quarter 2010. It means that the Ministry of Finance maintains the planned long-term target.

Average time to maturity reached the level of **6.3 years** at the end of the first half, i.e. remains within the announced target band 5.5–7.0 years for 2010.

Redemption profile of state debt (CZK billion)

(end of Q2 2010; updated on 30 June 2010)

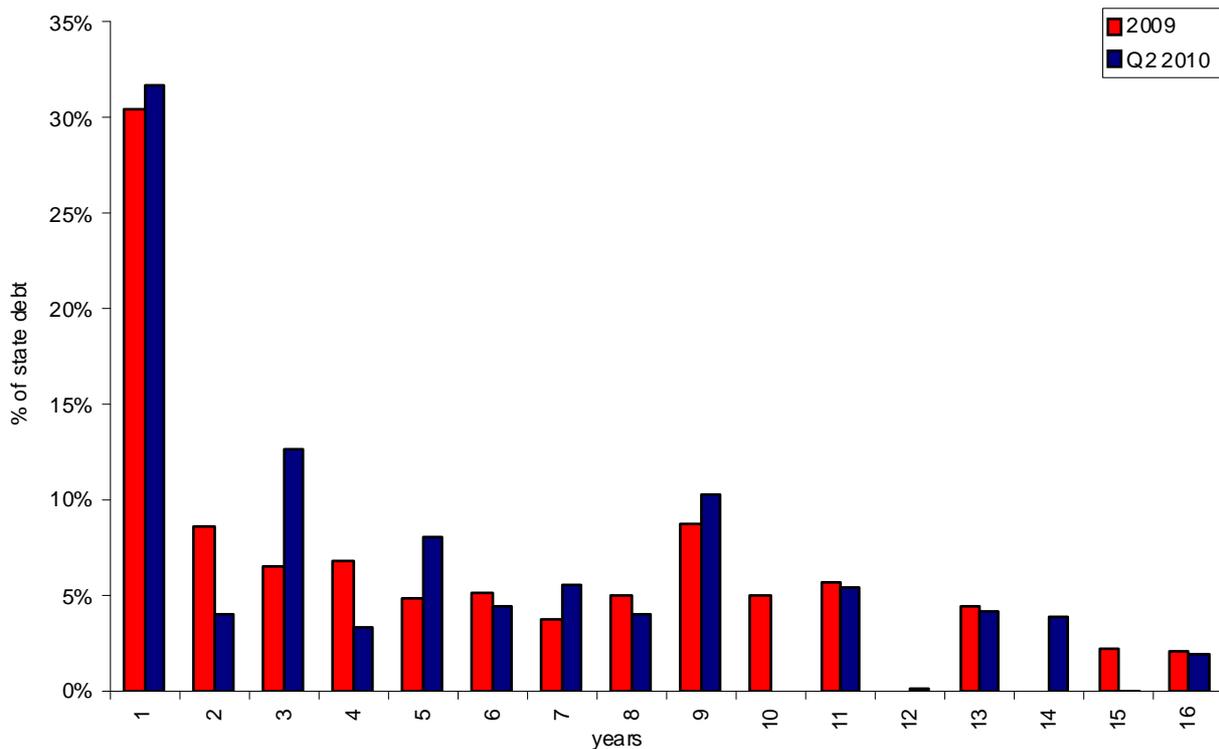


Note: Excluding money market instruments
Source: MF CR.

Beginning with the year 2006, **the interest rate re-fixing** up to one year replaces the modified duration targeting in the area of market risk management. The *Financing and Debt Management Strategy for 2010* sets the average yearly range between 30 % and 40 %. This risk measure increased to 31.7 % at the end of the first half 2010 and returned to the target range.

Re-fixing profil of state debt

(end of Q2 2010 compared with end of 2009; updated on 30 June 2010)



Note: Including derivatives
Source: MF CR.

II. State debt costs and Cost-at-Risk in 2010

Planned and actual budgetary expenditures and revenues in the first half 2010 are captured in following table:

Planned and actual budgetary expenditures and revenues on state debt in 2010

Measure (CZK mil)	Actual H1 2009	Budget 2010		Actual H1 2010	% Execution	Index 2010/2009 (%)
		Approved	After changes			
1	2	3	4	5	5:4	5:2
Total balance	29 610 (-) 3 830	76 357 (-) 6 868	72 380 (-) 6 868	27 058 (-) 5 794	37.4 84.4	91.4 151.3
1. Total interest costs	29 402 (-) 3 718	61 981 (-) 6 568	62 131 (-) 6 568	26 841 (-) 5 633	43.2 85.8	91.3 151.5
Domestic debt	22 370 (-) 3 143	47 256 (-) 5 790	47 406 (-) 5 790	20 387 (-) 5 418	43.0 93.6	91.1 172.4
<i>Of which:</i>						
Money market instruments	1 154 (-) 907	2 851 (-) 1 600	2 851 (-) 1 600	725 (-) 289	25.4 18.1	62.9 31.9
Government bonds	21 217 (-) 2 235	44 405 (-) 4 190	44 555 (-) 4 190	19 661 (-) 5 128	44.1 122.4	92.7 229.4
Foreign debt	7 032 (-) 575	14 725 (-) 778	14 725 (-) 778	6 455 (-) 215	43.8 27.7	91.8 37.5
<i>Of which:</i>						
International issues	6 186 (-) 574	12 374 (-) 778	12 374 (-) 778	5 777 (-) 215	46.7 27.7	93.4 37.6
EIB loans	846	2 352	2 352	678	28.8	80.2
Short-term loans	(-) 2	-	-	-	-	-
2. Total fees	199 -	700 -	697 -	58 (-) 0	8.4 -	29.2 -
3. Redemption	9	4	4	-	-	-
4. FX gain/loss	- (-) 113	1 000 (-) 300	1 000 (-) 300	158 (-160)	15.8 53.4	- 142.2
5. Transfers for projects¹	-	12 671	8 548	-	-	-

Note: (-) means revenues (gains).

Source: MF CR.

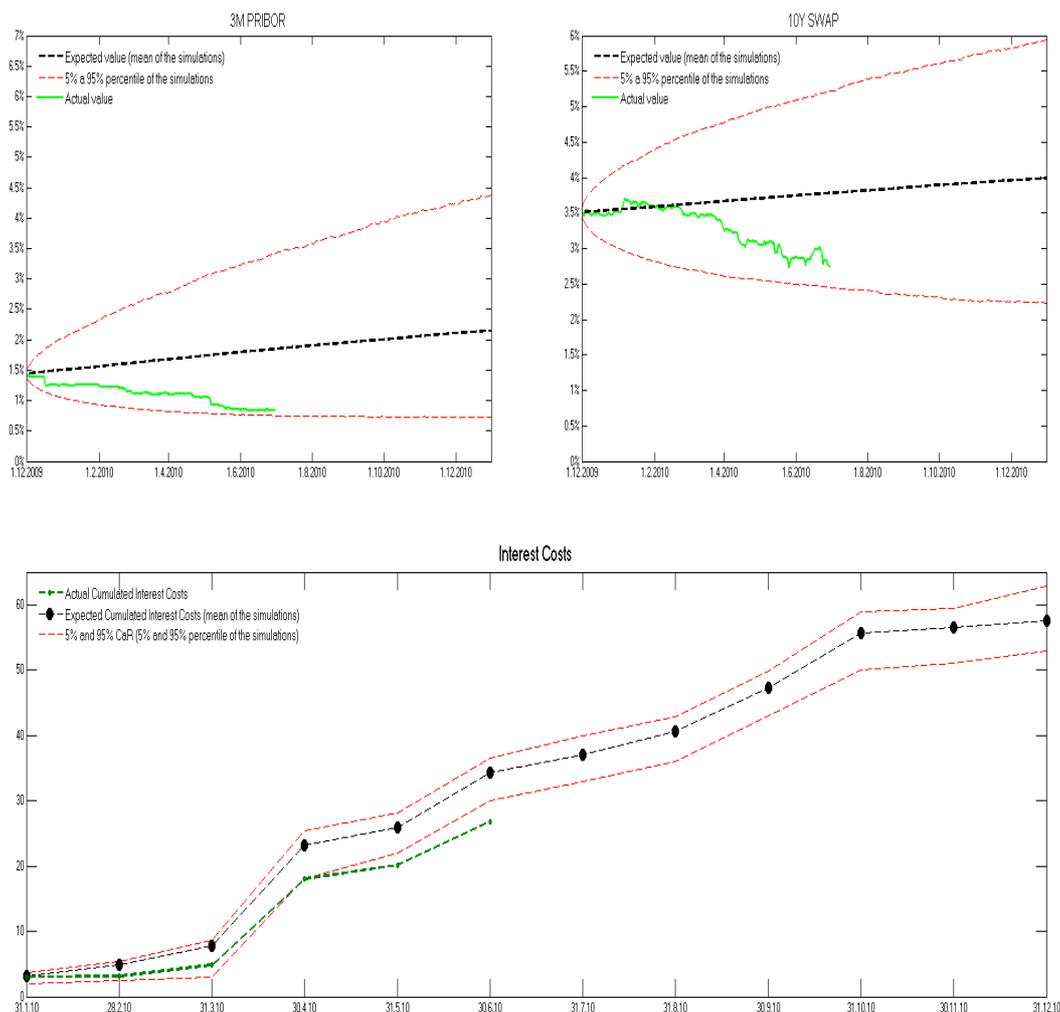
The **net debt service costs** on the state debt in the first half 2010 amounts **CZK 21.3 billion**. Accrued interest income and government bonds premiums achieve CZK 5.1 billion and financial investments on the money market gain CZK 0.3 billion. The gross debt service costs reached CZK 27.1 billion.

¹ Transfers for projects financed from international financial institutions credits

The state debt interest costs model **Cost-at-Risk (CaR)** for the year 2010 was published in the *Financing and Debt Management Strategy for the year 2010*. Calculations of the CaR values are based on future interest rates simulations.

The actual versus simulated developments of the PRIBOR 3M and 10Y swap from 1 December 2009 till 31 December 2010 are displayed in the upper part of the figure. The development of the actual versus simulated gross interest costs for the first half 2010 is shown in the lower part of the figure.

Actual versus simulated evolution of the interest rates and the actual versus simulated monthly gross interest costs (CZK billion)



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

The comparison between the actual development of interest costs and the development of the simulated interest costs at the end of the first half 2010 in comparison with the same period of the last year is summarized in the following table.

Cost-at-Risk deviation from the actual interest costs at the end of Q2 2009 and 2010

	2009	2010
Actual interest costs (CZK billion)	27.2	26.8
Expected (simulated) costs (CZK billion)	22.7	34.3
Cost-at-Risk 95% (CZK billion)	24.3	36.5
Expectation bias (%)	-16.5	27.8

Source: MF CR.

III. State Debt Parameters (end of quarter)

Debt Parameter	Jun 2009	Sep 2009	Dec 2009	Mar 2010	Jun 2010
Total state debt (CZK billion)	1 137.3	1 167.7	1 178.2	1 216.8	1 246.1
Market value, inc. derivatives (CZK billion)	1 139.0	1 191.8	1 225.6	1 291.7	1 316.0
Short-term state debt (%)	13.4	12.9	14.7	14.2	16.4
Share of money market instruments (%)	7.0	6.8	7.5	7.2	7.2
Average time to maturity (years)	6.6	6.4	6.5	6.3	6.3
Interest rate refixing up to one year, inc. derivatives (%)	26.8	27.5	30.5	29.7	31.7
Variable-rate state debt (%)	10.5	11.7	13.1	12.8	12.6
Modified duration (years)	4.3	4.2	4.2	4.1	4.5
Modified duration, exc. CZK IRS (years)	4.1	4.1	4.1	4.0	4.4
Foreign currency state debt (%)	6.2	7.0	8.6	8.1	8.3
Foreign currency debt, exc. cross-currency swaps (%)	14.2	13.4	15.4	14.4	14.3
Nonmarketable state debt (%)	4.6	4.6	5.0	5.0	4.9
Marketable state debt (CZK billion)	1 085.5	1 114.0	1 119.8	1 156.1	1 184.8
Market value (CZK billion)	1 087.0	1 137.6	1 166.5	1 230.1	1 253.5
Short-term marketable debt (%)	13.9	13.4	15.3	14.8	17.1
Share of money market instruments (%)	7.4	7.1	8.0	7.6	7.5
Average time to maturity (years)	6.3	6.1	6.2	6.0	6.0
Interest rate refixing up to one year, inc. derivatives (%)	23.6	24.3	27.2	26.3	28.4
Variable-rate marketable debt (%)	6.6	7.8	9.0	8.6	8.4
Modified duration (years)	4.4	4.4	4.4	4.2	4.7
Modified duration, exc. CZK IRS (years)	4.2	4.2	4.2	4.1	4.6
Foreign currency marketable debt (%)	6.5	7.3	9.0	8.5	8.7
Foreign currency debt, exc. cross-currency swaps (%)	14.8	14.1	16.1	15.1	15.0

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

This publication is available also on the website:
www.mfcr.cz/statedebt

The next issue of Quarterly Review will be published on October 8, 2010, at 2.00 p.m.

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