



Debt Portfolio Management Quarterly Review

SEPTEMBER 2010

The Ministry of Finance submits the twenty third *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	September 30, 2010
International issues	Max. 50 % of the total annual gross borrowing requirement	17,6 %
	CZK 0.0 to 140.0 bn	CZK 49.2 bn
Gross government bonds issues	CZK 102.3 to 292.3 bn	CZK 138.7 bn
Net money market issues	CZK -25.0 to +25.0 bn	CZK 40.3 bn
Loans from EIB	CZK 12.7 bn	CZK 5.4 bn
Short-term state debt	20 % and less	17.6 %
Average time to maturity	5.5 to 7.0 years	6.1 years
Interest Rate Re-fixing	30 to 40%	31.9 %

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

As regards **international funding**, on September 6th the Czech Republic has issued the fifth public benchmark Eurobond denominated in EUR in the amount of **EUR 2.0 bn**, i.e. **CZK 49.2 billion**, which is 35.1% of maximal international issuance activity according to initially declared financial programme for year 2010. Further, the Czech Republic has drawn three tranches of loans from the European Investment Bank in the amount of **CZK 2.1 billion** during the third quarter. During the first three quarters of 2010, loans were drawn in total amount of CZK 5.4 billion, which represents 42.5 % of the limit in the State Budget Act for 2010.

Regarding **domestic issuance activity**, the total gross issuance of government bonds reached **CZK 53.2 billion** during third 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 1.0 billion. During the first three quarters, the total gross issuance reached CZK 138.7 billion, including CZK 3.5 bn tap sales executed via Reuters Dealing system and CZK 5.0 bn bought by EIB. The total gross issuance reached about 47.5 % of the maximal supply initially announced on 3 December 2010. The net issuance of government bonds was **CZK 53.2 billion** during the third quarter (CZK 117,7 bn during the first three quarters). Buy-backs of government bonds were not executed during the third quarter as well as during the first three quarters.

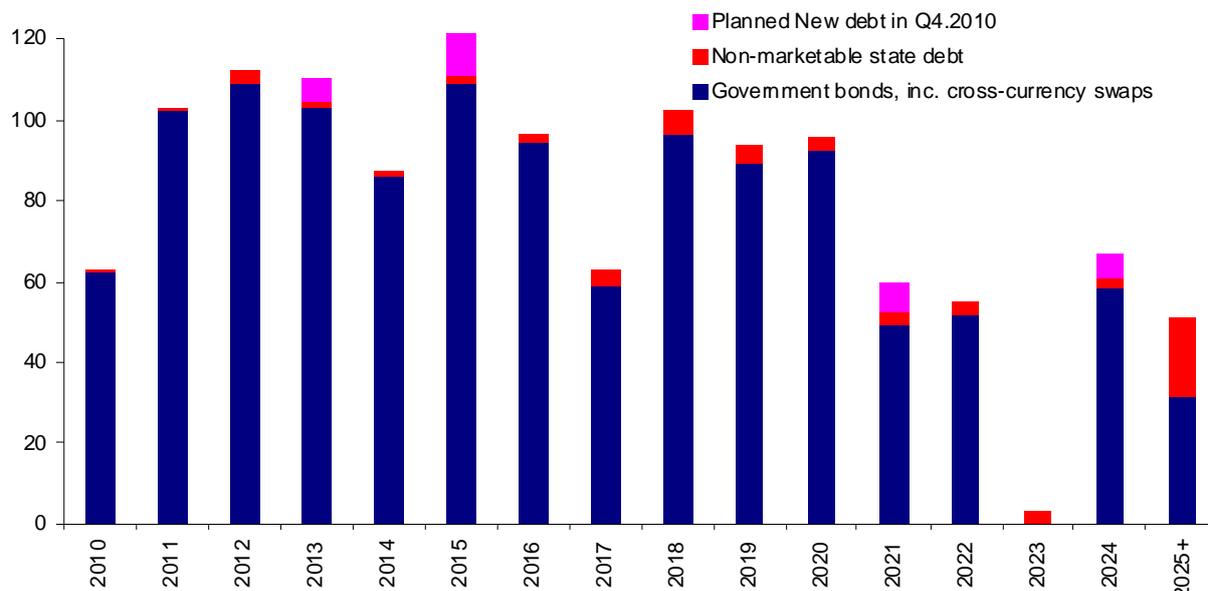
The volume in issue of money market instruments increased by **CZK 39.3 billion** during the third quarter (CZK 40.3 bn during the first three quarters 2010).

The short-term state debt increased by 1.2 percentage points and reached the share of **17.6 %** at the end of the third quarter 2010. It means that the Ministry of Finance maintains the planned long-term target.

Average time to maturity reached the level of **6.1 years** at the end of the third quarter, i.e. remains within the announced target band 5.5–7.0 years for 2010.

Redemption profile of state debt (CZK billion)

(end of Q3 2010; updated on 30 September 2010)

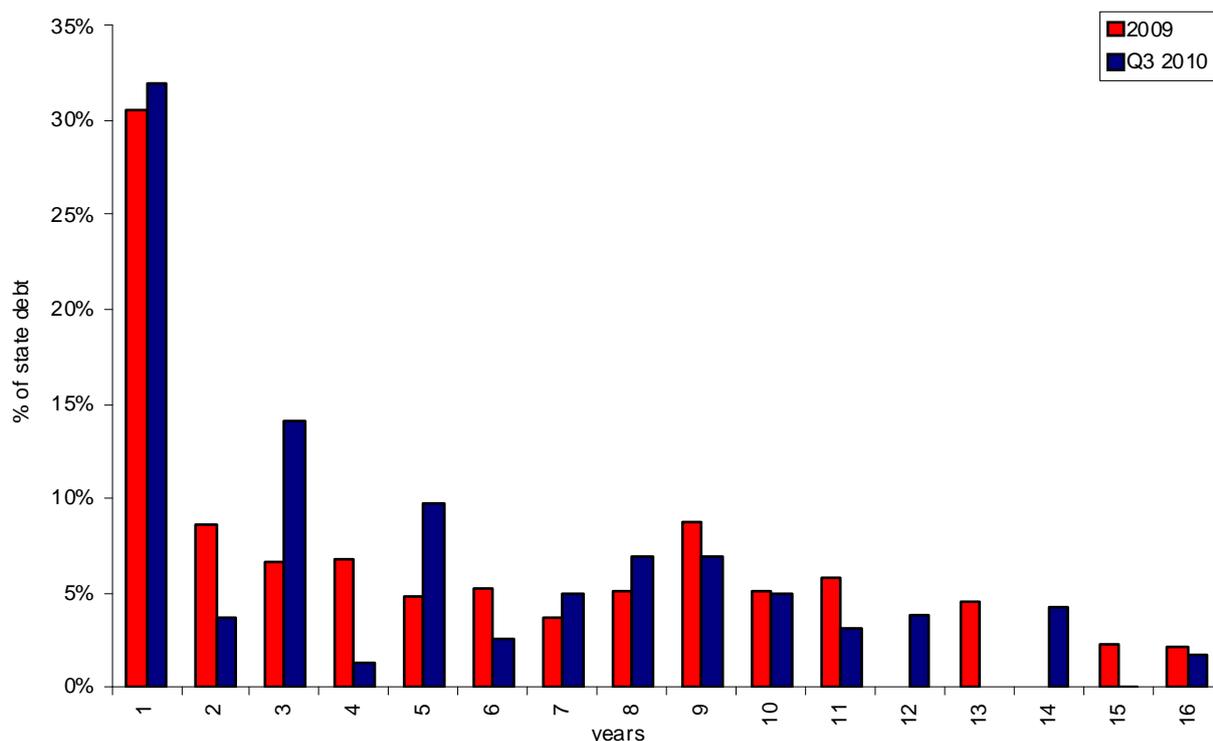


Note: Excluding money market instruments
Source: MF CR.

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 31.9 % at the end of the third quarter 2010 and remains in the target range.

Re-fixing profil of state debt

(end of Q3 2010 compared with end of 2009; updated on 30 September 2010)



Note: Including derivatives
Source: MF CR.

II. State debt costs and Cost-at-Risk in the first three quarters of 2010

Planned and actual budgetary expenditures and revenues in the first three quarters of 2010 are captured in following table:

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

Measure (CZK mil)	Actual Q1-Q3 2010	Budget 2010		Actual Q1-Q3 2010	% Execution	Index 2010/2009 (%)
		Approved	After changes			
1	2	3	4	5	5:4	5:2
Total balance	38 558 (-) 5 223	76 357 (-) 6 868	70 589 (-) 6 868	35 788 (-) 10 866	50,7 158,2	92,8 208,0
1. Total interest costs	38 319 (-) 5 111	61 981 (-) 6 568	62 131 (-) 6 568	35 430 (-) 10 706	57,0 163,0	92,5 209,5
Domestic debt	30 461 (-) 4 295	47 256 (-) 5 790	47 406 (-) 5 790	28 028 (-) 10 347	59,1 178,7	92,0 240,9
<i>Of which:</i>						
Money market instruments	1 532 (-) 1 388	2 851 (-) 1 600	2 851 (-) 1 600	1 212 (-) 468	42,5 29,2	79,1 33,7
Government bonds	28 929 (-) 2 907	44 405 (-) 4 190	44 555 (-) 4 190	26 815 (-) 9 879	60,2 235,8	92,7 339,9
Foreign debt	7 858 (-) 816	14 725 (-) 778	14 725 (-) 778	7 402 (-) 359	50,3 46,1	94,2 44,0
<i>Of which:</i>						
International issues	6 747 (-) 814	12 374 (-) 778	12 374 (-) 778	6 514 (-) 359	52,6 46,1	96,6 44,1
EIB loans	1 112	2 352	2 352	888	37,7	79,9
Short-term loans	(-) 2	-	-	-	-	-
2. Total fees	231 -	700 -	697 -	201 (-) 0	28,8 -	87,0 -
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	6 757	-	-	-

Note: (-) means revenues (gains).

Source: MF CR.

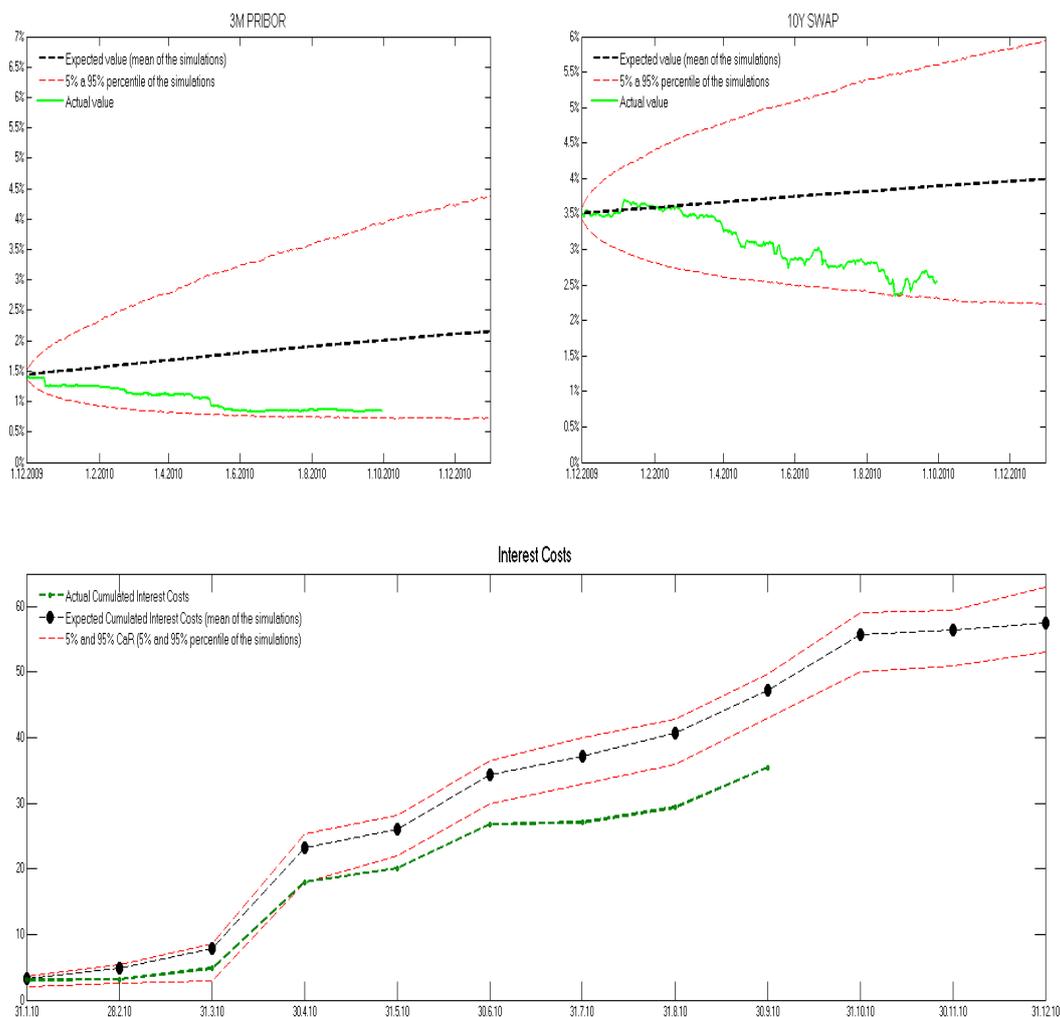
The **net debt service costs** on the state debt in the first three quarters of 2010 amounts **CZK 24.9 billion**. Accrued interest income and government bonds premiums achieve CZK 9.9 billion and financial investments on the money market gain CZK 0.5 billion. The gross debt service costs reached CZK 35.8 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 CZK 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 three quarters 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 third quarter 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 Q3 2009 and 2010

	2009	2010
Actual interest costs (CZK billion)	35,4	35,4
Expected (simulated) costs (CZK billion)	31,4	47,3
Cost-at-Risk 95% (CZK billion)	34,3	49,8
Expectation bias (%)	-11,3	33,5

Source: MF CR.

III. State Debt Parameters (end of quarter)

Debt Parameter	Sep 2009	Dec 2009	Mar 2010	Jun 2010	Sep 2010
Total state debt (CZK billion)	1 167.7	1 178.2	1 216.8	1 246.1	1 384.8
Market value, inc. derivatives (CZK billion)	1 191.8	1 225.6	1 291.7	1 316.0	1 499.8
Short-term state debt (%)	12.9	14.7	14.2	16.4	17.6
Share of money market instruments (%)	6.8	7.5	7.2	7.2	9.3
Average time to maturity (years)	6.4	6.5	6.3	6.3	6.1
Interest rate refixing up to one year, inc. derivatives (%)	27.5	30.5	29.7	31.7	31.9
Variable-rate state debt (%)	11.7	13.1	12.8	12.6	11.4
Modified duration (years)	4.2	4.2	4.1	4.5	4.5
Modified duration, exc. CZK IRS (years)	4.1	4.1	4.0	4.4	4.4
Foreign currency state debt (%)	7.0	8.6	8.1	8.3	10.7
Foreign currency debt, exc. cross-currency swaps (%)	13.4	15.4	14.4	14.3	15.8
Nonmarketable state debt (%)	4.6	5.0	5.0	4.9	4.6
Marketable state debt (CZK billion)	1 114.0	1 119.8	1 156.1	1 184.8	1 321.8
Market value (CZK billion)	1 137.6	1 166.5	1 230.1	1 253.5	1 435.4
Short-term marketable debt (%)	13.4	15.3	14.8	17.1	18.3
Share of money market instruments (%)	7.1	8.0	7.6	7.5	9.7
Average time to maturity (years)	6.1	6.2	6.0	6.0	5.8
Interest rate refixing up to one year, inc. derivatives (%)	24.3	27.2	26.3	28.4	28.9
Variable-rate marketable debt (%)	7.8	9.0	8.6	8.4	7.5
Modified duration (years)	4.4	4.4	4.2	4.7	4.6
Modified duration, exc. CZK IRS (years)	4.2	4.2	4.1	4.6	4.5
Foreign currency marketable debt (%)	7.3	9.0	8.5	8.7	11.2
Foreign currency debt, exc. cross-currency swaps (%)	14.1	16.1	15.1	15.0	16.6

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 January 10, 2011, at 2.00 p.m.

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