



Ministry of Finance

Debt and Financial Assets  
Management Department

# The Czech Republic Funding and Debt Management Strategy

# 2021



23 December 2020



# **Ministry of Finance**

## **The Czech Republic Funding and Debt Management Strategy for 2021**

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Management Strategy for 2021**

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On 21 December 2020 the structure and method of covering the financing needs in the budget year 2021 were decided and the basic absolute and relative limits for issuance activity on the domestic and foreign markets and for active management of the state debt portfolio, financial assets and liquidity of the treasury single account in the individual currencies were approved (Ref. No. MF-33992/2020/2002-1).

This defined operational framework in the form of the submitted The Czech Republic Funding and Debt Management Strategy for 2021 enables the Ministry of Finance to act flexibly on the domestic and foreign financial markets while actively securing cash resources for covering the financing needs and ensuring the daily solvent position of the state, meaning the creation of initial conditions for smooth implementation of budget and fiscal policy of the government.

The Czech Republic Funding and Debt Management Strategy for 2021 is based on and is consistent with the State Budget Act of the Czech Republic for 2021, including the medium-term outlook to 2023, and the Macroeconomic Forecast of the Czech Republic from September 2020.

The Czech Republic Funding and Debt Management Strategy for 2021 is submitted via Debt and Financial Assets Management Department, which is responsible for operations related to the funding of the state, active management of the state debt portfolio and financial assets, management of the liquidity of the treasury single accounts, and short-term and long-term investment of available cash resources of state financial assets and the treasury single accounts on financial markets.

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## List of Abbreviations

bn	billion
Budgetary rules	Act No. 218/2000 Coll. on Budget Rules and Amendments of Some Relating Acts (Budgetary Rules)
CaR	Cost-at-Risk
CNB	Czech National Bank
CZK	Czech Koruna currency code
CZSO	Czech Statistical Office
ESA 2010	European System of Account 2010
EUR	Euro currency code
GDP	gross domestic product
MoF	Ministry of Finance
MTS	Mercato Telematico Secondario
T-Bills	state treasury bills
T-Bonds	medium-term and long-term government bonds

Published aggregate data in the tables and in the text may not correspond in the last decimal place to the sum of respective indicators due to rounding in some cases.



## Introduction

The Ministry of Finance (hereinafter the Ministry or MoF) presents to the public The Czech Republic Funding and Debt Management Strategy for 2021 (hereinafter the Strategy) in accordance with the calendar of published information, the purpose of which is to present the basic framework for the state funding for 2021 and set monitored limits and targets of state debt risk indicators valid for medium-term horizon of the outlook.

Based on actual development of financing needs, especially with regard to the state budget performance, development of available funds of the state treasury and development of situation on financial markets in the first half of the next year, the update of this Strategy will be published in June 2021. Ministry

keeps the option to introduce quarterly updates of the Strategy within The Czech Republic Debt Management Quarterly Report - 1<sup>st</sup> Quarter of 2021 and The Czech Republic Debt Management Quarterly Report - 1<sup>st</sup> - 3<sup>rd</sup> Quarter of 2021.

The detailed description of events in the area of state debt, the evaluation of issuance activity, the evaluation of secondary market of government bonds, the development of interest expenditure of the state budget, the risk monitoring of debt portfolio, and annual performance evaluation of primary dealers will be contained in The Czech Republic Debt Management Annual Report for 2020, which will be published on 12 February 2021.

## Key Events in 2021

### Financing Needs of CZK 546.3 Billion

- budgeted crisis state deficit of CZK 320.0 billion
- partial coverage of the financing needs by reducing cash resources of state financial assets in the amount of CZK 18.8 billion
- redemptions of two CZK-denominated issues of medium-term and long-term government bonds in total nominal value of CZK 116.8 billion
- redemption of pilot issue of government EUR-bond from 2019 in total nominal value of EUR 1.0 billion
- redemption of issue of EUR-denominated government bonds issued on foreign market in 2010 in total nominal value of EUR 2.0 billion, of which a part of EUR 1.0 billion was hedged at the exchange rate of CZK 24.55 per euro in 2011
- active management of state treasury single accounts with a focus on expanding offered maturities of term deposits and increasing the number of state treasury clients

### Primary Market of Government Bonds

- gross issue of CZK-denominated medium-term and long-term government bonds on domestic market in a minimum total nominal value of CZK 400.0 billion
- possibility of issuance of new benchmark issues of fixed- or variable-rate government bonds on domestic market with maturity from 2024
- possibility of issuing a new issue of a zero-coupon government EUR-bond in order to cover

the EUR-denominated financing needs and further development of the market infrastructure for government bonds denominated in a foreign currency issued under Czech law

- possibility of issuance of government bonds denominated in foreign currencies under foreign law in case of cost-favourable conditions
- re-opening of already issued government bonds and government EUR-bonds with maturity from 2022

### Secondary Market of Government Bonds

- fulfilment of quotation obligations through the MTS Czech Republic platform
- continued tap sales and exchange operations of government bonds, possible launch of government bonds buy-backs programme
- active support of the secondary market through medium-term and long-term government bonds lending facilities

### Direct Sale of Government Bonds to Citizens

- continuation of direct sale to citizens at quarterly intervals with supply of several types of government bonds
- possibility of subscribing at contractual distributors branches or via electronic access to asset account management
- continuation of electronization of the government bonds sale system to reduce distribution costs and the launch of new functionalities of electronic access to asset account management

## Rating of the Czech Republic

The Czech Republic is assigned the highest overall rating of all Central and Eastern European countries and has higher rating than the Euro Area member countries average for several years.

Despite the negative effects of the current SARS-CoV-2 coronavirus pandemic on the domestic economy and uncertainty about future developments, all major international agencies confirmed their ratings, including maintaining a stable outlook, in 2020. The agencies appreciated

the low indebtedness, including the favorable debt structure, and the readiness of the domestic economy to absorb the negative shocks caused by the current crisis.

The Czech Republic belongs among the exceptionally reliable issuers and enjoys considerable interest from domestic and foreign investors, as confirmed by its high credit rating with a stable outlook from all the major credit rating agencies with international scope of activity.

**Table 1: The Czech Republic's Credit Rating**

Rating agency	Local currency long-term liabilities	Outlook	Foreign currency long-term liabilities	Outlook	Affirmed
Moody's	Aa3	Stable	Aa3	Stable	27/5/2020
S&P Global Ratings	AA	Stable	AA-	Stable	30/10/2020
Fitch Ratings	AA-	Stable	AA-	Stable	24/7/2020
JCR	AA	Stable	AA-	Stable	5/11/2020
R&I	AA-	Stable	AA-	Stable	9/3/2020
Scope Ratings	AA	Stable	AA	Stable	2/10/2020
Dagong Global Credit Rating	A+	Stable	A+	Stable	16/10/2018
ACRA Europe	AA	Stable	AA	Stable	24/7/2020
ACRA	AA	Stable	AA	Stable	12/10/2020

Source: Moody's, S&P Global Rating, Fitch Ratings, JCR, R&I, Scope Ratings, Dagong Global Credit Rating, ACRA Europe, ACRA

## Financing Needs and State Debt Development

The financing needs are determined by the standard components that must be covered by cash resources in a given year, i.e. the state budget cash deficit, and regular redemptions, redemptions before the maturity date, buy-backs and exchanges of nominal values of state debt, including the related

derivatives. Financing operations on the side of state financial assets and within the treasury single accounts then take place on the side of cash resources that can be involved into the covering of the financing needs simultaneously with the state's realized borrowing operations on financial markets.

**Table 2: Financing Needs**

CZK bn	2021F	2022F	2023F
State budget deficit <sup>1</sup>	320.0	286.0	252.0
Transfers and other operations of state financial assets <sup>2</sup>	-	-	2.8
T-Bonds denominated in local currency redemptions <sup>3,4</sup>	141.4	137.3	202.7
T-Bonds denominated in foreign currency redemptions <sup>4</sup>	56.0	77.0	0.0
Redemptions and early redemptions on savings government bonds	0.0	0.0	0.0
Money market instruments redemptions <sup>5</sup>	25.4	0.0	0.0
Repayments on credits and loans <sup>6</sup>	3.5	3.2	2.6
<b>Total financing needs</b>	<b>546.3</b>	<b>503.5</b>	<b>460.0</b>
<b>Total financing needs (% of GDP)<sup>7</sup></b>	<b>9.3%</b>	<b>8.2%</b>	<b>7.2%</b>

<sup>1</sup> For 2021, the budgeted deficit according to the draft of State budget Act for 2021 approved by the Chamber of Deputies of the Parliament of the Czech Republic on 18 December 2020 and for 2022 and 2023 the approved medium-term outlook of the state budget.

<sup>2</sup> Transfers according to paragraph 36, section 3 of Act No. 218/2000 Coll. and other operations of state financial assets.

<sup>3</sup> Including the effect of already executed buy-backs and exchange operations in previous years. Excluding future buy-backs and exchange operations of T-Bonds.

<sup>4</sup> Including the currency hedging of the T-Bond principals denominated in foreign currency; T-Bonds redemptions are stated in CZK equivalent.

<sup>5</sup> Excluding the T-Bills issued and other money market instruments realized in the future.

<sup>6</sup> Credits and loans received from international financial institutions.

<sup>7</sup> Source for GDP in ESA 2010 methodology for 2021 to 2023 Macroeconomic Forecast of the Czech Republic – September 2020.

Note: Excluding future issuance activity.

Source: MoF

For 2021, the planned financing needs amount to CZK 546.3 billion, i.e. about 9.3% of GDP, but its actual value will primarily depend on the actual state budget performance and on the actual amount of exchange operations and buy-backs of government bonds carried out in this year. The financing needs in the 2021 to 2023 shows, in absolute terms and as a share of GDP, a declining trend, which is given by declining total state debt redemptions excluding the impact of future issuance activity and declining planned state budget deficits in the medium term.

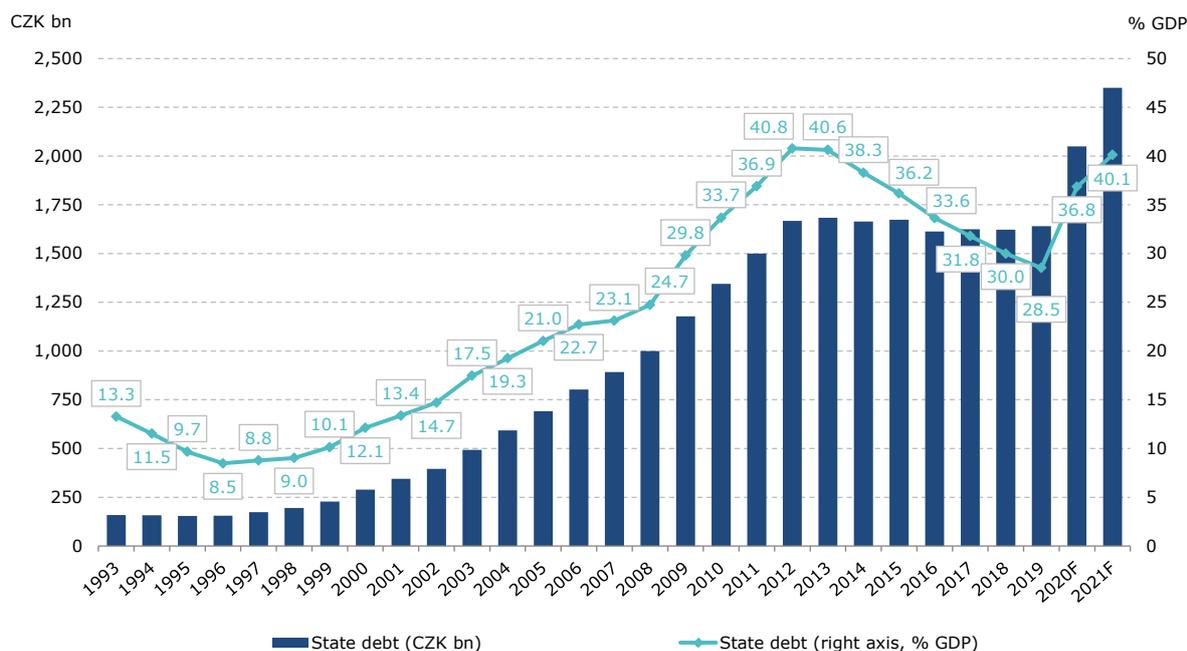
Declining state debt redemptions in the years 2021 to 2023 are affected by the Ministry's issuing activity, when the average maturity of newly issued medium-term and long-term government bonds in 2020 reached more than seven years and does not significantly increase the financing needs in the medium term, and exchange operations to an increased extent compared with previous years, when the Ministry exchanged government bonds maturing in 2021 in total nominal amount of almost CZK 30 billion with government bonds with an average time to maturity reaching approx. 10 years. Compared to 2018, when state debt redemptions reached a historical amount over CZK 307 billion, state debt redemptions decreased

by CZK 81 billion in 2021, by CZK 90 billion in 2022 and by CZK 102 billion in 2023.

However, planning the level of financing needs in the medium term, including its coverage, is very difficult and bears risks due to uncertain future developments in the area of SARS-CoV-2 coronavirus spread in the Czech Republic and the impact of measures on public budgets to prevent it.

The resulting gross borrowing requirement, which is derived from the financing needs and represents the part of financing needs, which must be covered through borrowing operations on financial markets, especially government bond markets, is dependent on the involvement of financial assets into covering the financial needs, i.e. in particular the available state treasury resources and the state reduction of the state financial assets accounts. In case of involvement of these liquid assets into covering the financing needs, the resulting gross borrowing requirement is lower than total financing needs in respective period. In the opposite case, when there is an accumulation of financial assets, the gross borrowing requirement is higher than the financing needs.

**Figure 1: Czech Republic's State Debt Development**



Note: Source for GDP in ESA 2010 methodology for 1993 to 2019 is CZSO, for 2020 and 2021 Macroeconomic Forecast of the Czech Republic – September 2020. Source: MoF, CZSO

In recent years, the Ministry has focused on stabilizing the absolute value of state debt, i.e. reducing its share in GDP, thus creating sufficient headroom for a possible increase in order to cover the effects of the pandemic on the state budget and strengthening the liquidity reserves of the state treasury. The final level of state debt in 2020 in absolute or relative value will depend on the actual state budget performance, issuance activity on the financial market at the very end of this year and the level of GDP.

Despite the extraordinary economic and health crisis, the Ministry estimates the increase in state debt in 2021 in relative value to a similar level as in 2012. However, the change in state debt will fully depend on issuance activity, which will be flexibly adapted to the state budget performance, situation on domestic and foreign financial markets and the effective involvement of the funds of payment accounts of public sector organizations included in the state treasury system in order to smoothly cover the crisis financing needs while maintaining a prudent approach to financial and credit risk management and minimizing costs in the long term. All operational decisions concerning the covering of financing needs will be transparently communicated with the public, especially with primary dealers and recognized dealers of government bonds, in particular through the publication of current issuance calendars or revisions of the issuance strategy in other Ministry's publications.

Following the amendment to the Act No. 218/2000 Coll. on budgetary rules and on amendment to some related laws (budgetary rules), as amended from previous years, the Ministry will strive for continued centralization of the state liquidity management by extending numbers of clients included in the treasury single accounts and the related strengthening of liquid reserves of state debt financing.

Based on Act No. 214/2020 Coll. an amendment to the act on budgetary rules, which was approved in 2020, Czech Export Bank and Export Guarantee and Insurance Corporation entered the state treasury system with effect from 17 April 2020. After a six-month transitional period, both of these institutions became full-fledged clients of the state treasury with all the positive effects on the stabilization of funds within the treasury single accounts liquidity management.

In accordance with the further planned development of the term deposit project within CZK-denominated accounts subordinated to the state treasury, the pilot phase of which began on 1 November 2019, the offered maturities of term deposits with maturities of 2, 3, 4 and 5 years were introduced with effect from 4 January 2021. It represents significant development of this instrument supporting further longer-term stabilization of the state treasury funds, which can thus be used for the purposes the state debt and available state treasury liquidity management over a period exceeding one year.

## Funding Programme and Issuance Activity

### Medium-Term and Long-Term Government Bonds

In 2021, the Ministry plans to carry out gross issue of CZK-denominated medium-term and long-term government bonds on domestic market in total minimum nominal value of CZK 400.0 billion. The Ministry will issue medium-term and long-term government bonds maturing along the whole yield curve in order to achieve the objectives and

limits set in the Strategy for the medium-term horizon. In dependence on the development on financial markets and the monetary policy situation, the Ministry plans to issue new issues of medium-term and long-term government bonds denominated in local currency with maturity from 2024.

**Figure 2: Average Nominal Value of CZK-denominated T-Bonds per Issue**



Source: MoF

Due to the unprecedented issuance activity in this year, the Ministry had to abandon the plan to stabilize the number of CZK-denominated issues of medium-term and long-term government bonds to twenty, but plans to achieve this goal in the long term. When choosing particular maturities and type of instrument, the Ministry will flexibly react on development of

market conditions and the demand from the primary dealers and recognized dealers. The issuance activity including the inclusion of variable-rate medium-term and long-term government bonds will be carried out with the respect to the riskiness of the debt portfolio and maintaining strategic targets and limits for risk parameters in medium-term horizon.

**Table 3: Framework Issuance Plan of CZK-denominated T-Bonds on the Domestic Market in 2021**

CZK bn	Framework scope of sale
<b>Fixed-rate and variable-rate T-Bonds</b>	<b>Min. 400</b>
Maturity segment of up to 10 years	Max. 450
Maturity segment of over to 10 years	Max. 150

Source: MoF

If there is an unexpected change of the government bond market conditions or unplanned economic development, the Ministry reserves the option of not issuing new bonds. The Ministry also supplements the issuance of medium-term and long-term government bonds on the primary market with tap sales of government bonds from its own asset account on the secondary market in case that the primary dealers' and recognized dealers' interest especially when the usage of these government bonds within medium-term and long-term government bonds lending facilities drops or as a more flexible alternative to the sale of government bonds, which are included in primary auctions to a lesser extent. Furthermore,

tap sales of government bonds with a long time to maturity may be used to manage the average time to maturity of the debt portfolio. Tap sales will continue to be available through MTS Czech Republic.

The competitive part of the primary auction of medium-term and long-term government bonds on domestic market will be held on the traditional auction day of Wednesday while the non-competitive part of primary auctions will be held on Thursday. The settlement will take place according to the T+2 standards for settling operations on the primary market, usually on Friday. The possibility to bid within the competitive part of the auction is made possible for both primary dealers

and recognized dealers, but access to the non-competitive part of the auction remains exclusively to a group of primary dealers.

The issuance calendars of medium-term and long-term government bonds together with indicative maximum total nominal value sold in auctions for respective quarter of the year will be published monthly usually the fourth Monday of the month preceding the respective month, unless otherwise announced. The Ministry reserves the right to specify one or more alternative medium-term and long-term government bonds to be included in the relevant auction or change the offered government bond for another one with a similar time

to maturity. When choosing particular maturities and instrument type, the Ministry will flexibly react to the development of market conditions and demand from primary dealers and recognized dealers.

The selection of particular medium-term and long-term government bonds for the relevant auction will be announced at least one working day before the date of the competitive part of the auction. The nominal value of medium-term and long-term government bonds offered in the competitive part of the auction will be published in indicative maximum amount or in indicative range within the issuance calendars.

## **Money Market Instruments and Other Debt Instruments**

State treasury bills could be issued in all available maturities in order to cover short-term financing needs, to strengthen the state treasury liquidity reserves and, in the case of maintaining the interest rate differential between the auction yield of state treasury bills and the returns from investing liquidity of treasury single accounts, as well as obtaining additional funds in order to invest these funds in the money market with a positive impact on the state budget. Thus, the Ministry will maximize the current market situation with regard to the effective liquidity management of the treasury single accounts. State treasury bills will be issued on traditional auction day of Thursday with a T+1 settlement, usually on Friday.

The issuance calendars of state treasury bills with particular maturities offered in individual auctions will be published monthly usually on fourth Monday of the month preceding the respective month unless announced otherwise by the Ministry. The nominal value of state treasury bills offered in auction will be published in predetermined indicative range or an indicative maximum value will be announced. However, the Ministry reserves the right to change the range or maximum value according to the actual development of market conditions or the demand from primary dealers and recognized dealers. Together with the issuance calendars, the Ministry will publish also the indicative maximum total nominal value of state treasury bills issues for respective quarter.

During 2021, the Ministry will also use the medium-term and long-term government bonds lending facilities intensively in the form of repo operations and also in the form of collateralized loans, under which the Ministry provides government bonds of Czech Republic from own asset account against another government bond or CNB bill for a short period of time. These facilities may be used for the period up to 90 days. The aim of these operations is to increase the liquidity of government bonds on secondary market particularly in case of short-term excess of demand over supply regarding the particular government bond. The scope of realized medium-term and long-term government bonds lending facilities will primarily depend of the demand for particular government bonds from the investors with the fact, that the Ministry will be ready to flexibly satisfy this demand accordingly to the availability of government bonds on its asset account.

If necessary, the Ministry plans to continue to benefit from favourable conditions on the money market for short-term refinancing of foreign currency debt of central government in the form of deposit operations or foreign exchange swaps. Funds may also be obtained from the European Investment Bank or Council of Europe Development Bank through the already signed loan contracts or from other international institutions, if Ministry achieves cost-favourable conditions than in case of the issuance of government bonds on domestic market with a similar residual time to maturity.

## **Programme for Buy-Backs and Exchanges Operations on Secondary Market**

The Ministry plans the inclusion of government bonds into buy-backs and exchanges operations in dependence on market condition in particular segment of the yield curve and their execution will primarily depend on the demand from primary dealers and recognized dealers. The exchange operations and buy-backs of medium-term and long-term government bonds will be technically available through the MTS Czech Republic. The impacts of these operations will affect the financing

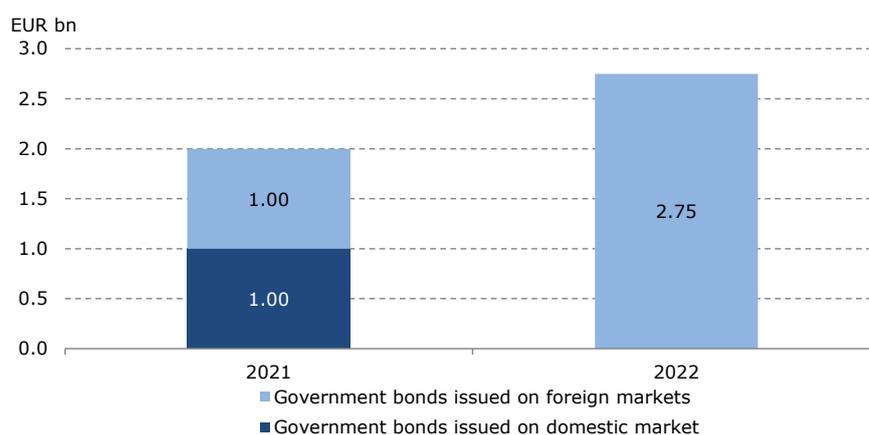
needs and borrowing requirement accordingly and will have positive impact on refinancing risk of state debt management. In exchange operations, the state treasury bills may be included, especially in the case of their issuance in order to strengthen the treasury liquidity reserves, as it was successfully introduced this year in response to financial market uncertainties associated with the pandemic spread of SARS-CoV-2 coronavirus.

## Refinancing of Foreign Currency State Debt in 2021 and 2022

In the following two years, resources will be secured to cover redemptions of government bonds denominated in euro resulting from previous issuance activity on domestic and foreign markets in total nominal value of EUR 4.75 billion including currency hedging. These redemptions consists of medium-term and long-term government bonds

issued on foreign markets in 2010 and 2012 in total nominal value of EUR 3.75 billion including currency hedging and the Government EUR-Bond of the Czech Republic, 2019–2021, 0.00 % issued on domestic market in 2019 in total nominal value of EUR 1.0 billion.

**Figure 3: EUR-denominated Government Bond Redemptions Including Currency Hedging**



Source: MoF

Given the developments in the euro bond market and the currently expected monetary policy of the European Central Bank, the Ministry may proceed with long-term refinancing of foreign currency debt next year. The specific coverage will be decided to minimize the costs and financial risks associated with borrowing operations on domestic and foreign financial markets.

In the case of maintaining favourable conditions in the form of negative or zero yields on the euro bond market and interest from primary dealers and recognized dealers, the Ministry plans to issue new issues of the government EUR-bond on domestic market under Czech law or re-open already issued government EUR-bond due in 2027 for full or partial refinancing of euro financing needs and will continue to take further steps to develop and make this form of financing more attractive to international investors. The Ministry, as a new member of the Users Committee of the Central Securities Depository Prague, initiated and reached in 2019 an agreement with its members to make the central depository, as an ancillary settlement system, a direct participant in the TARGET2 payment system, a clearing system operated by the central banks of the euro area countries. This happened in line with the project plan on 2 March 2020 representing a significant step forward in the development of the domestic capital market and its closer interconnection with euro area bond market infrastructure. At the same time, it was a necessary step towards the planned inclusion of the Czech Republic's government EUR-

bonds issued under Czech law and registered in the domestic central depository among the eligible assets under Eurosystem credit operations as another key milestone in 2021.

The alternative in the form of syndicated issuance of medium-term and long-term government bonds on foreign markets under foreign law will depend primarily on actual conditions on domestic and foreign markets. A foreign issue is subject to lower interest expenses related to the issuance of government bonds on the foreign market compared to a similar issue of government bonds on the domestic market, after taking into account additional costs in the form of fees for leading managers of the issue, preparation of necessary documentation and other related activities.

Partial coverage of the euro financing needs may also be achieved through drawing on extraordinary loans from international financial institutions, or by revising previously received tranches of loans from the European Investment Bank and converting them into the euro.

If the Ministry finds it appropriate with regard to the prudential approach to financial risk management and the minimization of interest expenditure, foreign currency debt up to EUR 1.0 billion may be covered by euro funds as part of increasing liquidity of treasury single accounts or by deposit operations, repo operations and foreign exchange swaps.

## Direct Sale of Government Bonds to Citizens

At the end of 2018, the Ministry opened a direct distribution channel for government bonds for citizens offering a conservative and stable form of savings assessment, thus re-establishing the successful project of sale of savings government bonds intended for citizens and selected legal entities which was suspended in 2014 due to the fall in government bond yields to historical minimum. The Ministry allows households to participate in the financing of the government of the Czech Republic and to appreciate their savings under very similar conditions as institutional investors. After evaluating the pilot phase, which ended at the end of the first half of 2019, the Ministry decided to continue.

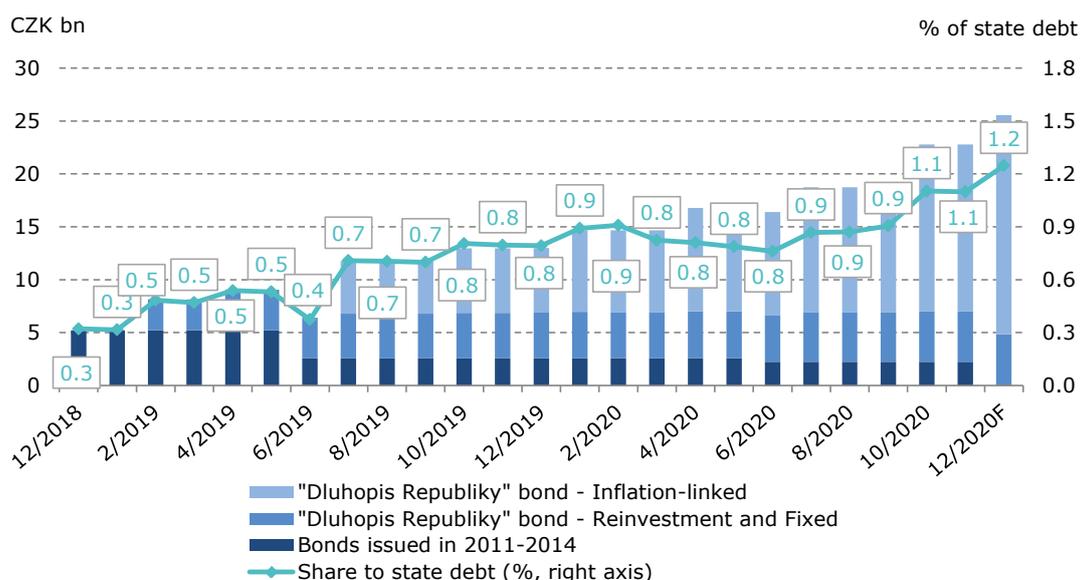
The Ministry considers the increase in the share of households in state debt to be desirable. Retail investors are usually conservative and not subject to short-term fluctuations in international bond markets, which contributes to greater stability and diversification of the investor base with a positive impact on the refinancing and interest rate risk of the debt portfolio. Holding government bonds for natural persons is advantageous even though they are mostly domestic entities and part of the interest expenditure of the state debt service will generate additional income of domestic households.

Over the past eight subscription periods, citizens purchased the "Dluhopis Republiky" bonds in a total nominal value of over CZK 20.4 billion,

while the Ministry offered to subscribe for 6-year reinvestment, inflation-linked and fixed government bonds. In the next subscription period started from 21 September 2020 to 22 December 2020, potential subscribers were able to subscribe to reinvestment and inflation-linked government bonds with the issue date of 31 December 2020. The yields of each issue of the "Dluhopis Republiky" bonds were set at the level of market conditions and thus do not burden the state budget more than the potential issue of medium-term and long-term government bonds with the same time to maturity. The bond yield will be reinvested after each interest period by subscribing additional government bonds on the relevant asset account in the Ministry's register in the amount of the bond yield after tax, according to the relevant legal regulations.

In 2020, the issues of the "Dluhopis Republiky" bonds fully covered redemptions of savings government bonds in total nominal value of CZK 2.8 billion and due to the expected net issue of CZK 12.6 billion significantly contributed to an increase in the share of government bonds intended for citizens in state debt from 0.3% at the end of 2018 to 1.2% at the end of 2020. Despite the historical increase in state debt, the share of government bonds intended for citizens in total state debt increased further, which clearly confirms their high attractiveness, while expressing the share of government bonds intended for citizens in state debt ratio would be 1.6% at the end of 2019.

**Figure 4: Development of Government Bonds for Citizens Nominal Value Outstanding**



Source: MoF

As part of the continuation of the project, the Ministry plans to offer another issues of the "Dluhopis Republiky" bonds to citizens during the year 2021, while it will be possible to subscribe these bonds

on a daily basis in the subscription periods, which will be continuously linked to each other. The bonds will be subscribed on the relevant asset account at the end of subscription period at quarterly intervals.

It will be possible to subscribe all offered issues of the "Dluhopis Republiky" bonds via electronic access to asset account management or through selected branches of contractual distributors, which are currently Československá obchodní banka, a. s., and Česká spořitelna, a.s.

One subscriber can subscribe bonds at a minimum of 1,000 pieces, i.e. CZK 1,000, up to 5,000,000 pieces, i.e. CZK 5 million. The subscriber may be only a natural person and in accordance with the terms and conditions the bonds are not freely marketable on regulated markets.

The goal of the Ministry is to continue the gradual electronicization of the system of distribution and administration of government bonds for citizens, among other things in order to minimize the costs associated with the distribution of government bonds. During 2020, new functionalities of electronic access

were launched. Its users now have the option, for example, to request a complaint about non-payment of yield or non-payment of nominal value or to generate and print gift certificates or commemorative certificates of the issue. At the same time, it is also possible to fill in a sworn statement directly in the electronic access environment. The launch of other functionalities will continue at the end of this year and during the following year 2021.

The decision of the Ministry was also endorsed by the Czech Fiscal Council on 5 December 2018 with its view that, in terms of the long-term sustainability of public finances and overall financial stability, the issuance of government bonds for citizens is considered as positive as this is not only an appropriate tool to mitigate risks from the point of view of the structure of the holders of state debt, but it also increases public awareness and public interest in the public sector economy.

## Strategic Targets, Limits and Risk Parameters of the Debt Portfolio

In connection with the sufficient liquidity of treasury single accounts and relatively stable balances of the accounts owners mandatorily included into treasury single accounts, improvement of the efficiency and modernization of state treasury liquidity management, the Ministry announces strategic targets and limits of refinancing and interest risk in medium-term horizon. This concept allows the Ministry to flexibly react on short-term market conditions and interest of investors for instruments in particular segment of time to maturity or re-fixing.

Short-term deviation from established strategic medium-term targets and limits for risk parameters of debt portfolio for refinancing and interest risk is possible. However, the issuance in medium-term horizon will be planned so that the targets and limits defined in this Strategy will be fulfilled in medium-term horizon.

For 2021, the Ministry maintains the concept of refinancing risk management through the average time to maturity of state debt indicator and interest risk management through the average time to re-fixing of the state debt indicator using a medium-term target value of this indicator. Despite the unprecedented issuance activity of the

Ministry during 2020 and a significant increase in state debt compared to 2019, it was not necessary in 2020 to revise or short-term modify and loosen the strategic targets and limits for risk parameters of debt portfolio. Despite the high uncertainty about the economic development in the following year and ultimately in the medium-term horizon, the Ministry does not propose to adjust the risk targets and limits applicable for the medium-term horizon, as none of the risk indicators deviate significantly from the set target, or does not approach the set limit.

The currency risk is specified by the net foreign-currency exposure of state debt indicator taking into account also the foreign-currency exposure of state financial assets. In this context, net foreign-currency exposure of state debt with the impact on state debt level and net foreign-currency exposure with the impact of the level of interest expenditure on state debt service are distinguished. The limit is stipulated for both indicators and is valid for each year of medium-term horizon without the possibility to exceed it. However, its value is subjected to the condition that there will be no sharp depreciation of Czech Koruna exchange rate. Compared to the refinancing and interest risk, the currency risk is relatively small.

### Refinancing Risk

The limit for the share of the short-term debt (debt due within 1 year) is stipulated at 20.0% of the total state debt for the medium-term horizon. The limit for the share of the medium-term debt (debt due within 5 year) is stipulated at 70.0% of the total state

debt for the medium-term horizon. For average time to maturity of the state debt, the target value of 6.0 years is stipulated for the medium-term horizon with the possibility of deviation of 0.25 years.

## Interest Risk

For interest re-fixing of the debt portfolio within 1 year, the limit is retained at 40.0% of the total state debt for the medium-term horizon. For average

time to re-fixing of the state debt, the target value of 5.0 years with the possibility of deviation of 0.25 years is stipulated for the medium-term horizon.

## Currency Risk

For 2021, the Ministry retains the limit for both net foreign-currency exposure of the state debt indicators, i.e. net foreign-currency exposure of state debt with the impact on state debt level and net foreign-currency exposure with the impact

of the level of interest expenditure on state debt service, at the level of 15.0% (up to 17.0% in the short-term) of total state debt, while foreign exchange swaps will also be included in the net foreign-currency exposure.

## State Debt Service Expenditure and Cost-at-Risk

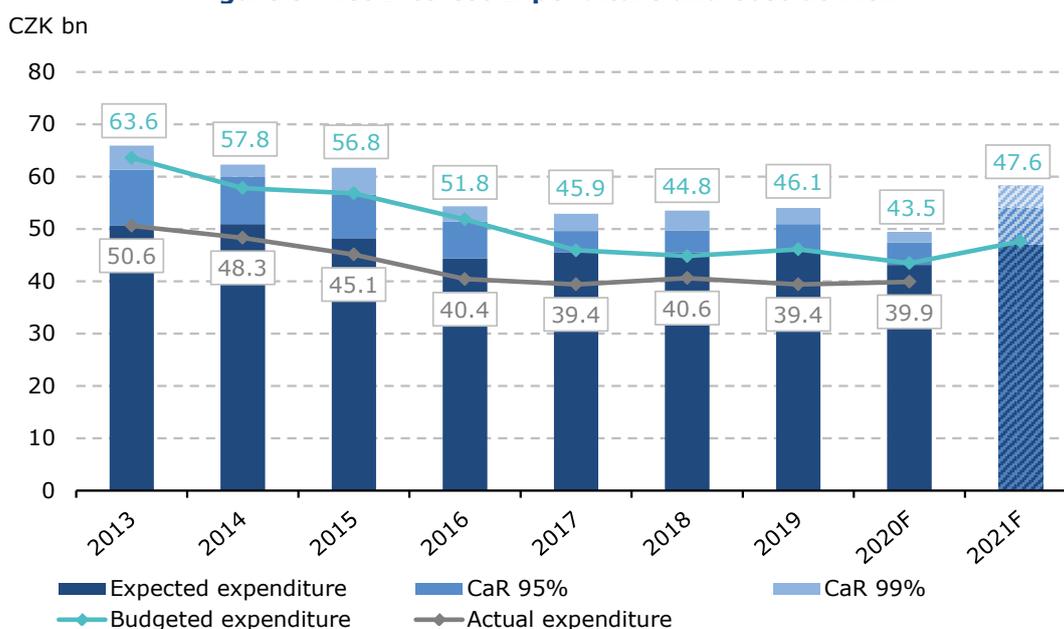
The Ministry applies a model framework known as Cost-at-Risk (furthermore CaR) for measuring and managing interest rate risk since 2005. This framework is based on the Value-at-Risk methodology and simulates future expected and maximum interest expenditure for a particular degree of risk, which is derived from the volatility of the time structure of interest rates. The stochastic element of the CaR model is the yield curve, and the deterministic element is the dynamic structure of the portfolio of state debt, which is based on the base case scenario of the funding programme while respecting the set strategic goals for managing financial risks.

The primary goal of the model is to determine the maximum interest expenditure on state debt,

which with 95% or 99% probability will not be exceeded (furthermore CaR 95% and CaR 99%). The secondary goal of the model is to estimate the actual interest expenditure on state debt. The simulation framework operates separately with the interest expenditure and interest revenue. The outcome of aggregation of interest expenditure and interest revenue is the net interest expenditure on state debt. Interest expenditure on state debt service in the model framework does not include fees related to state debt service, which are of a deterministic nature.

Over all the years the CaR methodology has been applied, the model has fulfilled the primary goal, since the simulated maximum interest expenditures were not exceeded in any of those years.

**Figure 5: Net Interest Expenditure and Cost-at-Risk**



Note: In 2013 to 2021, the figures represent the originally approved budget. Figure in 2020 is expected value.  
Source: MoF

**Table 4: Net Interest Expenditure and Cost-at-Risk**

CZK bn	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
<b>Budgeted expenditure<sup>1</sup></b>	63.6	57.8	56.8	51.8	45.9	44.8	46.1	43.5	47.6	49.6	51.6
<b>Actual expenditure<sup>2</sup></b>	50.6	48.3	45.1	40.4	39.4	40.6	39.4	39.9	-	-	-
<b>Expected expenditure</b>	50.6	50.9	48.2	44.3	45.6	45.5	45.8	43.1	47.0	50.0	52.2
<b>CaR 95%</b>	61.3	60.0	56.6	51.4	49.6	49.7	50.9	47.4	54.1	62.1	65.9
<b>CaR 99%</b>	65.9	62.3	61.7	54.3	52.9	53.5	54.0	49.4	58.3	69.9	74.2

<sup>1</sup> From 2013 to 2021 the figures represent the originally approved budget. In 2022 and 2023 medium-term outlook.

<sup>2</sup> Figure in 2020 is expected value.

Source: MoF

The expected value of net interest expenditure in 2021 amounts to CZK 47.0 billion. The expected value of net interest expenditure amounts to CZK 50.0 billion in 2022 and CZK 52.2 billion in 2023. In medium-term outlook of state budget for 2022 and 2023, the expenditure frameworks of budget chapter 396 - State Debt are below CaR 95% indicator. For 2022 the expenditure framework amounts to CZK 49.6 billion and is CZK 12.5 billion lower than 95% percentile of interest expenditure. For 2023 the expenditure framework amounts to CZK 51.6 billion and is CZK 14.3 billion lower than 95% percentile of interest expenditure. The increasing trend of budgeted and simulated interest expenditure is given primarily by

the volatility of interest rates, which increases with longer simulation horizon. Due to the fact that the state budget is compiled only for the following year, the simulation horizon of interest expenditure for the budget compilation for following year will be shorter, and given the market conditions remain unchanged, it is expected, that the values of CaR 95% and CaR 99% indicator will decrease due to the lower volatility of the interest rates simulations.

More detailed quantification of interest expenditure on state debt service in 2021 and in medium-term horizon through application of CaR methodology will be a part of The Czech Republic Government Debt Management Annual Report for 2020.

## Primary Dealers and Recognized Dealers in Czech Republic Government Bonds

With effect from 7 December 2020, J.P. Morgan Securities plc passed all rights and obligations to J.P. Morgan AG in connection with regulatory changes. Furthermore, from 1 January 2021, all rights and obligations arising from the Primary Dealer Agreement for Czech Government Securities shall pass from ING Bank N.V. to ING Bank Śląski S.A.

For the year 2021, the number of primary dealers who signed the Primary Dealer Agreement for Czech Government Securities with the Ministry is 9. Their list is content of the following table. Goldman Sachs International remains recognized dealer of Czech government bonds for 2021.

**Table 5: List of Primary Dealers and Recognized Dealers in Czech Republic Government Bonds for 2021**

Primary Dealers and Recognized Dealers	
Citibank Europe plc	Société Générale / Komerční banka, a.s.
Erste Group Bank AG / Česká spořitelna, a.s.	PPF banka a.s.
KBC Bank NV / Československá obchodní banka, a. s.	Raiffeisen Bank International AG
ING Bank Śląski S.A.	UniCredit Bank Czech Republic and Slovakia, a.s.
J.P. Morgan AG	Goldman Sachs International (Recognized Dealer)

Source: MoF

# Calendar of Information Published in the First Half of 2021

## January

Mo	Tu	We	Th	Fr	Sa	Su
				1	2	3
4	5	6	7	8	9	10
11	12	13	14	15	16	17
18	19	20	21	22	23	24
25	26	27	28	29	30	31

## February

Mo	Tu	We	Th	Fr	Sa	Su
1	2	3	4	5	6	7
8	9	10	11	12	13	14
15	16	17	18	19	20	21
22	23	24	25	26	27	28

## March

Mo	Tu	We	Th	Fr	Sa	Su
1	2	3	4	5	6	7
8	9	10	11	12	13	14
15	16	17	18	19	20	21
22	23	24	25	26	27	28
29	30	31				

## April

Mo	Tu	We	Th	Fr	Sa	Su
			1	2	3	4
5	6	7	8	9	10	11
12	13	14	15	16	17	18
19	20	21	22	23	24	25
26	27	28	29	30		

## May

Mo	Tu	We	Th	Fr	Sa	Su
					1	2
3	4	5	6	7	8	9
10	11	12	13	14	15	16
17	18	19	20	21	22	23
24	25	26	27	28	29	30
31						

## June

Mo	Tu	We	Th	Fr	Sa	Su
	1	2	3	4	5	6
7	8	9	10	11	12	13
14	15	16	17	18	19	20
21	22	23	24	25	26	27
28	29	30				

- Publication of the The Czech Republic Debt Management Annual Report for 2020  
- on the second Friday in February
- Expected publication of The Czech Republic Funding and Debt Management Strategy for 2021 - Second Half Update  
- on the last working day of the first half of 2021
- Publication of The Czech Republic Debt Management Quarterly Report  
- on the third Friday in April
- Publication of statistics of the Central Government Debt and Fiscal Data for the Czech Republic (SDDS Plus standard)  
- on the second Friday in February and on the third Friday in April
- Publication of the annual statistics on Development and Structure of the State Debt, Financing Needs and Sources of the Central Government and Interest Expenditure on the State Debt  
- on the second Friday in February
- Publication of the Statistics on Government Bonds by Type of Instrument, Statistics on Government Bonds by Type of Holder and Statistics on Government Bonds by Maturity  
- on the last working day of the month
- Publication of the issuance calendars of T-Bills and T-Bonds for following month  
- the fourth Monday in the month prior to the month of the respective auctions, except June, when issuance calendar will be published together with The Czech Republic Funding and Debt Management Strategy for 2021 - Second Half Update

Ministry reserves the right to change the date of publication due to flexible response to financial markets situation. Any change will be communicated to the public in time through Ministry's website.







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The publication was prepared based on the information and data available on 21 December 2020. The Ministry reserves the right to promptly respond to the actual development of financing needs using its tools in the course of 2021. The fulfilment of the funding programme and announced strategic goals will depend of the development of the situation on domestic and foreign financial markets in terms of the minimization of expenditure on state debt service and financial risk management.

This publication is also available on the following website:

[www.mfcr.cz/statedebt](http://www.mfcr.cz/statedebt)

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