Ministry
of Finance

Debt and Financial Assets
Management Department

The Czech Republic Funding And Debt Management Strategy

2013 REVISION

8 July 2013

Ministry of Finance

The Czech Republic Funding and Debt Management Strategy 2013 - Revision as of 30 June

The Czech Republic Funding and Debt Management Strategy 2013 - Revision as of 30 June

8 July 2013

Ministry of Finance
Letenská 15, 118 10 Prague 1
Tel.: 257 041 111
E-mail: podatelna@mfcr.cz

ISSN 1805-7136 (Print)
ISSN 1805-7144 (On-line)

Electronic archive:
www.mfcr.cz/statedebt

Summary

The Ministry of Finance (hereinafter the "Ministry") hereby presents the Revision of *The Czech Republic Funding and Debt Management Strategy 2013* (hereinafter the "Strategy") as of 30 June 2013, which revises in particular the gross borrowing requirement of the central government and the basic parameters of the funding programme for 2013 (hereinafter the "Revision"). In the Strategy published on 12 December 2012 (Ref. No. MF – 117380/2012/20), the Ministry reserved the right to revise the Strategy in case the amendment to the Act No. 218/2000 Coll., Budgetary Rules Act and Some Related Acts Amendment Act (hereinafter the "Budgetary Rules"), is approved. The amendment came into force as of 1 January 2013. The Revision is based on the assumption that the state budget deficit for 2013 will approximate the budgeted amount of CZK 100.0 billion and will not exceed it.

The New Framework for State Treasury Liquidity Management

The amendment to the Budgetary Rules brought an essential extension of the treasury single account in CZK and a possibility to maintain treasury single accounts in foreign currencies. The treasury single account in EUR was established by the Czech National Bank on 2 April 2013. The amendment distinguishes two types of clients, whose accounts fall within the treasury single accounts, based on the possibilities to manage their cash resources and their accounts with the Czech National Bank and commercial banks.

Clients, whose accounts fall mandatorily within the treasury single accounts, are not entitled to maintain accounts with commercial banks; they have to keep all the cash resources in the accounts with the Czech National Bank. It makes it impossible to transfer the cash resources outside the state treasury system and it constitutes rather stable part of the central state liquidity resources, which can be used for the funding of state. Clients, whose accounts are included in the treasury single accounts optionally, open the accounts with the Czech National Bank designed only for receiving cash resources from the state budget, state funds or the National Fund. They are not limited in transferring the cash resources from the accounts included in the treasury single accounts to any commercial bank.

During the first quarter of 2013, the treasury single accounts balances were gradually extended by all the cash resources in the accounts of the mandatory clients, i.e. state organizational units, state funds and the Land Fund of the Czech Republic, the National Fund, the former National Property Fund and state contributory organizations, which are obliged to transfer all their cash resources to the Czech National Bank within the transitional period of five years, and also by the cash resources in the accounts of the optional clients designed for receiving cash resources from the state budget, state funds and the National Fund, namely local government units and voluntary municipal associations, regional councils of cohesion regions, public research institutes and public universities, Railway Infrastructure Administration and other legal entities, whose accounts are maintained with the Czech National Bank with the Ministry's consent.

Table 1: State Treasury Accounts Balances (CZK billion)

		31 Dec 2011	30 Jun 2012	31 Dec 2012	30 Jun 2013
Original accounts	Cash reserve[1]	70.6	134.8	139.9	114.3
	Other cash resources[2]	31.4	54.8	69.4	69.0
New accounts	Mandatory clients	-	-	-	53.4
	Optional clients	-	-	-	13.7
Liquidity excl. cash reserve		**31.4**	**54.8**	**69.4**	**136.1**
Total liquidity available		**102.0**	**189.6**	**209.3**	**250.4**

[1] Generated according to the Section 35(4) of the Budgetary Rules particularly by the issuance and sale of government bonds.
[2] Balances of the state financial assets accounts, former National Property Fund account, tax and custom authorities accounts and the state organizational units' reserve funds and cultural and social needs funds accounts.
Source: Czech National Bank and Ministry of Finance

As of the end of the first half of the year, the state treasury disposed of the total liquidity of CZK 250.4 billion, including the cash resources in EUR, which represents an increase by CZK 41.1 billion compared to the end of 2012. The state treasury liquidity (excluding the cash reserve reduced by the Ministry by CZK 25.6 billion in order to finance redemption on treasury bills) increased by CZK 66.7 billion during the first half of the year. It represents a net inflow of new liquidity resources, which are available to the Ministry for financing of an unexpected borrowing requirement or in case of an increased uncertainty in financial markets during the calendar year.

During the first half of 2013, the treasury single accounts average daily balance increased by CZK 138.8 billion to CZK 298.1 billion compared to the same period of the previous year. Further slight increase in the total additional state treasury liquidity is expected in the course of the second half of 2013, when the respective clients will gradually transfer further cash resources to the accounts within the treasury single accounts.

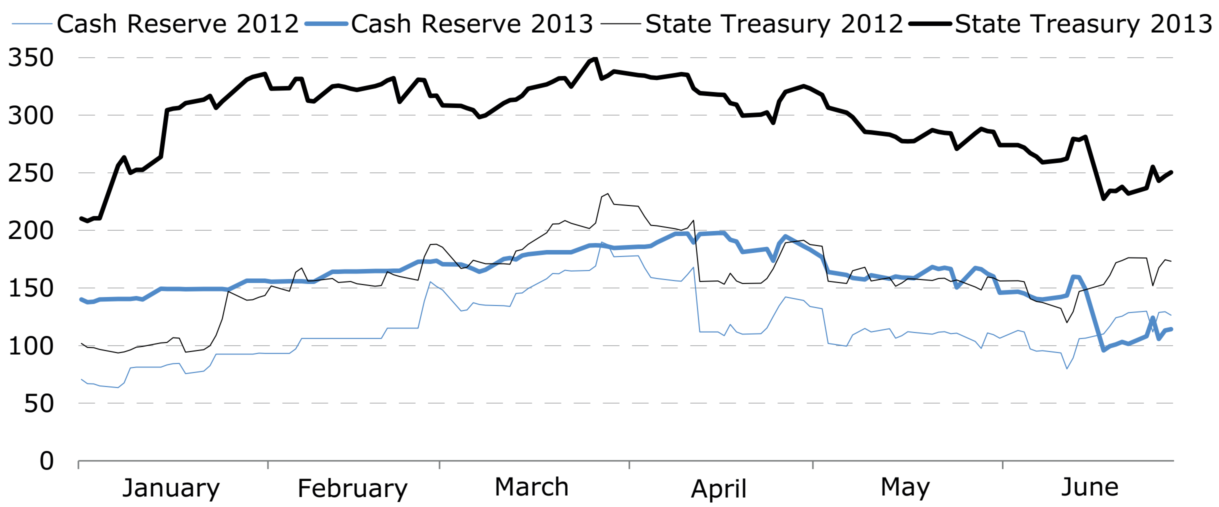
Table 2: State Treasury Accounts Daily Balance (CZK billion)

	2011	2012	H1 2012	H1 2013
Average daily balance	79.5	178.7	159.3	298.1
CZK	59.5	156.2	134.3	242.5
EUR	20.0	22.5	25.0	55.6

Source: Czech National Bank and Ministry of Finance

The development of the state treasury balance in the first quarter of 2013 is related to the gradual inclusion of new clients' accounts among accounts falling within the state treasury, which caused considerable one-time increases. Since the state treasury management system is going through extensive changes and new clients' behavior cannot be predicted yet, it is necessary to maintain sufficient daily liquidity, including the treasury single accounts balances in CZK and EUR.

Figure 1: Development of the Cash Reserve and the State Treasury Balance in the first half of 2012 and 2013 (CZK billion)



Source: Czech National Bank and Ministry of Finance

The amendment to the Budgetary Rules and subsequent increase in additional liquidity in the treasury single accounts strengthened the state's position on financial markets. Additional state treasury liquidity contributes to the decrease in the liquidity and refinancing risk of the debt portfolio and gives further possibilities for budgetary savings by reducing the state debt service costs. The final state treasury liquidity management setting in terms of the gradual cash reserve reduction and the implementation of refinancing system will depend on the development of the mandatory clients' accounts balances in the second half of 2013 and the optional clients' transfers of cash resources from the accounts with the Czech National Bank to the commercial banks, which is currently difficult to predict and has to be analyzed based on the longer time series data.

Gross Borrowing Requirement of the Central Government and Funding Programme for 2013

The gross borrowing requirement of the central government for 2013 published in the Strategy amounted to CZK 230.7 billion, the planned gross borrowing requirement after the revision by CZK 110.0 to 140.0 billion comes to CZK 90.7 to 120.7 billion. Actual gross borrowing requirement in 2013 will depend in particular on the development of state budget balance, new state treasury clients' behavior and the development of financial markets, which are currently experiencing increased volatility. During the second half of the year, the Ministry will analyze all these circumstances in detail, so that in 2013 and in the medium-term outlook the increase in risk and endangering the smoothness of the funding of state is avoided. The resulting decrease in the gross borrowing requirement will be determined primarily by the final decision on the amount of the cash reserve from previous years, which will be included into the funding of state, in contrast to the published plan.

The revised funding programme for 2013 is based on the funding operations carried out in the first half of the year and on the revised gross borrowing requirement of the central government. In the first half of the year, 30.9% of the gross borrowing requirement originally planned for 2013 (44.5% including the redemption on and the gross issuance of treasury bills) were financed solely through the domestic bond market. The total nominal amount of the gross domestic issuance of medium-term and long-term government bonds amounted to CZK 81.2 billion, of which CZK 4.1 billion were sold on the secondary market and CZK 2.1 billion within the state financial assets investment operations in the nuclear portfolio. The total nominal amount of the net issuance of medium-term and long-term government bonds in the first half of 2013 came to CZK 18.3 billion. It reflects the redemption on 40th issue of government bonds in the total nominal amount of CZK 62.9 billion. In June, the "spring" series of issues of savings government bonds was issued in the total nominal amount of CZK 17.5 billion. The total nominal amount of the gross issuance in form of the reinvestment of yields in the first half of the year amounted to CZK 83.0 million. During the first half of the year, the Ministry reduced the total nominal amount of the net issuance of money market instruments outstanding by CZK 27.5 billion as a reaction to the increase in the available short-term state treasury liquidity. Had there not been for this controlled reduction, as of the date of the Revision 42.8% of the gross borrowing requirement originally planned for 2013 would be already financed.

In the second half of the year, The Ministry also will carry out the crucial part of the funding programme on the domestic bond market and will continue to evaluate current development of conditions on the foreign markets. Given the rather short-term nature of the additional state treasury liquidity, the Ministry decreases the planned total nominal amount of net issuance of money market instruments in 2013 to CZK -80.0 to -50.0 billion from original CZK -10.0 to 10.0 billion. The final decrease will depend on the domestic and foreign investors' demand for Czech government bonds and on the final annual gross borrowing requirement. The Ministry also adjusts the planned total nominal amount of the gross issuance of CZK-denominated medium-term and long-term government bonds to CZK 96.7 to 170.7 billion. In case of favorable conditions on the foreign markets in terms of costs and achievable maturity in comparison with the domestic bond market, the Ministry will sell the government bonds denominated in foreign currencies in the maximum total nominal amount of approximately CZK 48.3 billion, i.e. 40% of the maximum annual gross borrowing requirement, excluding redemption on treasury bills within the year.

Table 3: Funding Programme for 2013 (CZK billion)

	Strategy	Revision	H1 2013
Gross borrowing requirement[1]	**230.7**	**90.7 to 120.7**	**71.3**
Direct loans from international financial institutions	**1.6**	**0.0 to 4.0**	**0.0**
Loans from the EIB	1.6	0.0 to 4.0	0.0
Other international financial institutions	0.0	0.0	0.0
Issuance of medium-term and long-term government bonds and savings government bonds	**219.1 to 239.1**	**136.7 to 200.7**	**98.8**
Issuance of medium-term and long-term government bonds on the domestic market[2]	87.1 to 219.1	96.7 to 170.7	81.2
Issuance of medium-term and long-term government bonds on the foreign markets	0.0 to 92.0	0.0 to 48.3	0.0
Issuance of savings government bonds[3]	20.0 to 40.0	30.0 to 40.0	17.6
Net issuance of money market instruments	**-10.0 to 10.0**	**-80.0 to -50.0**	**-27.5**
Gross issuance of treasury bills[4]	179.1 to 199.1	109.1 to 139.1	87.9
Redemption on treasury bills[4]	189.1	189.1	115.4
Net change in other money market instruments	0.0	0.0	0.0
Total gross borrowing requirement[5]	**419.8**	**279.8 to 309.8**	**186.7**

[1] Excl. operations with money market instruments.
[2] Incl. tap sales from the Ministry's own portfolio and purchases into the investment portfolios.
[3] Incl. the savings government bonds issued as the reinvestment of yields of respective issues.
[4] Excl. treasury bills issued and redeemed within the respective period.
[5] Incl. redemption on money market instruments and excl. roll-over of money market instruments within the respective period.
Source: Ministry of Finance

The loans from the European Investment Bank will be drawn in the total amount within the range of CZK 0.0 to 4.0 billion. The change is related to the unused budgeted expenditure of the Ministry of Transport from previous years, which will be realized gradually during 2013 and financed by the tranches of the respective loan. The final total amount of funds from the loans will further depend on the interest rates offered by the EIB and the comparison to the interest costs of the funding through the government bonds.

***

This publication was prepared based on the information available as of 30 June 2013. The Ministry reserves the right to promptly respond to the actual development of the gross borrowing requirement of the central government in the course of the second half of 2013 using its tools. Implementation of the planned funding programme and announced strategic objectives will depend on development of the situation on the domestic and foreign financial markets in terms of financial risk management and minimizing state debt service costs.

This publication is also available on the following website:

www.mfcr.cz/statedebt

www.sporicidluhopisycr.cz

Debt and Financial Assets Management Department
Letenská 15, 118 10 Prague 1 – Malá Strana
E-mail: podatelna@mfcr.cz, Reuters <MFCR>