

Guidelines for public debt management for 2003-2004

1. Objectives of public debt management

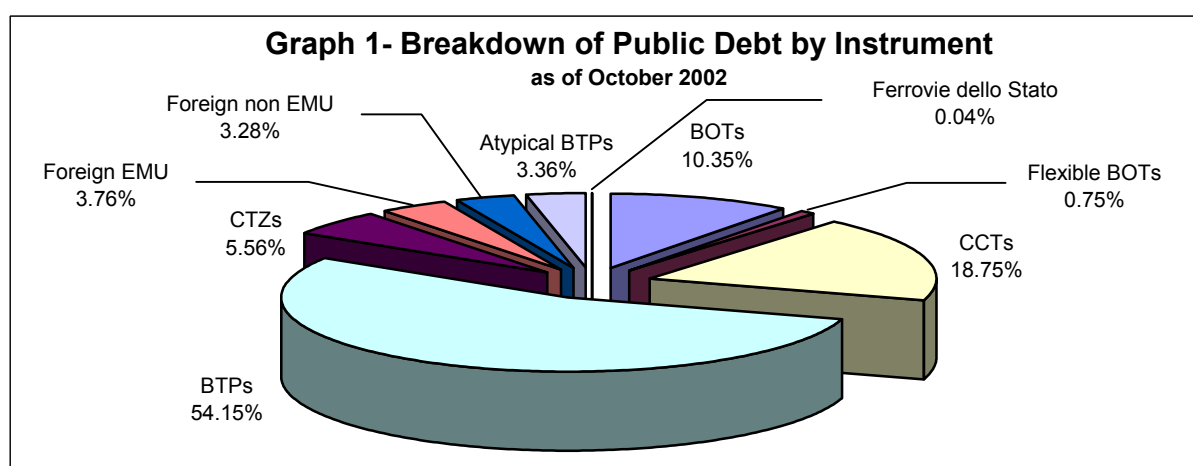
An efficient public debt management aims at meeting public borrowing requirements and refinancing debt redemptions, by choosing a strategy that optimally combines the cost and risks of funding.

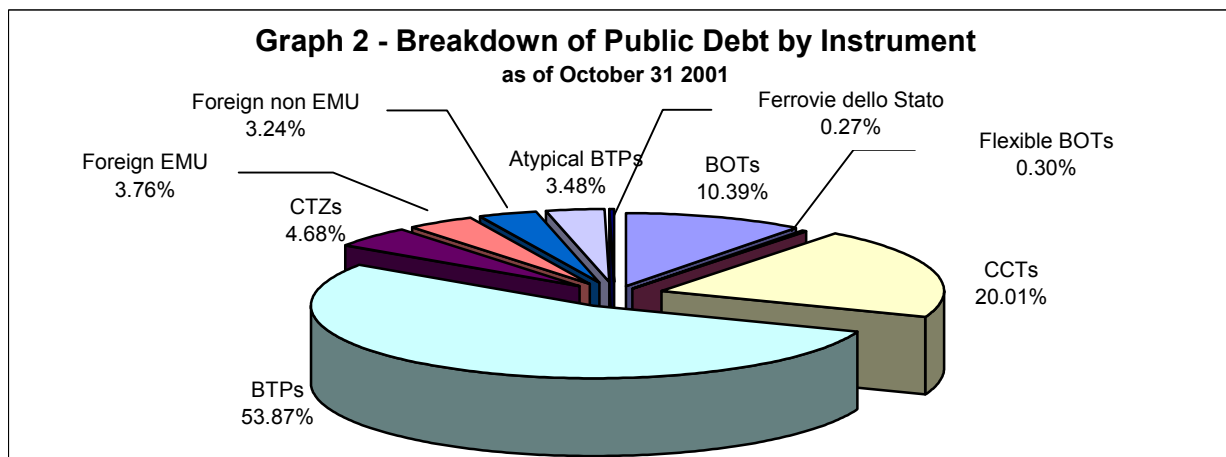
From the mid-1990s, debt management policy was carried out so as to get a debt composition consistent with the aim to contain the sensitivity of cost of financing to market interest rates (interest rate risk). In recent years, moreover, particular attention has been devoted to the management of refinancing risk embedded in the redemptions profile, by means of an appropriate issuance strategy and, starting in 2002, by implementing a bond exchange program.

2. Debt-management policy in 2002

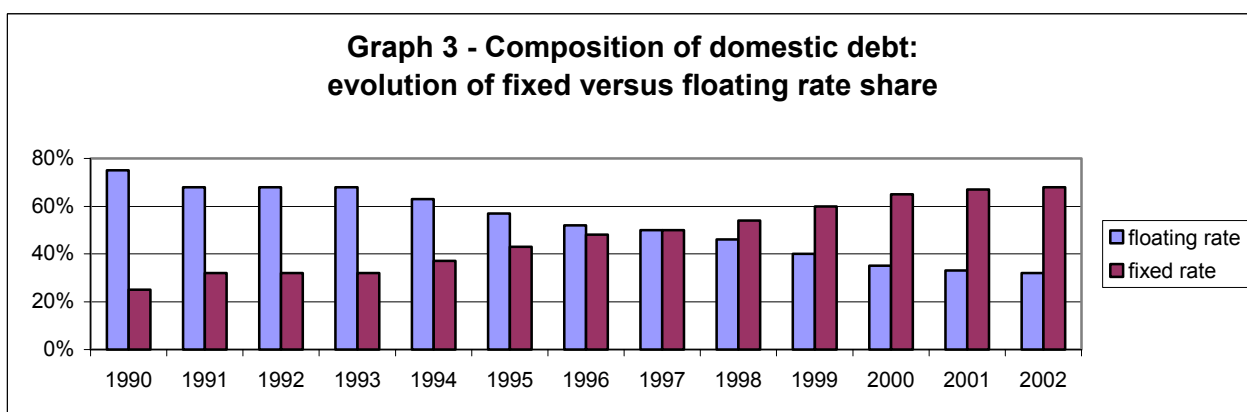
2.1. The evolution of debt composition

The debt issuance policy followed in 2002 did not give rise to significant changes in the debt structure with respect to last year. The share of fixed-rate, medium and long-term bonds (BTPs and CTZs) was kept at around 63%, while that of CCTs was slightly reduced (from 20.01% in 2001 to 18.75% in 2002) because of the incomplete renewal of redemption volumes in 2002 (about 56 billion euros). The share of bills (BOTs) slightly increased (from 10.69% in 2001 to 11.1% in 2002) because of the sharp increase in the demand for less-than-one-year maturity securities, resulting from the high volatility of financial markets during last year.



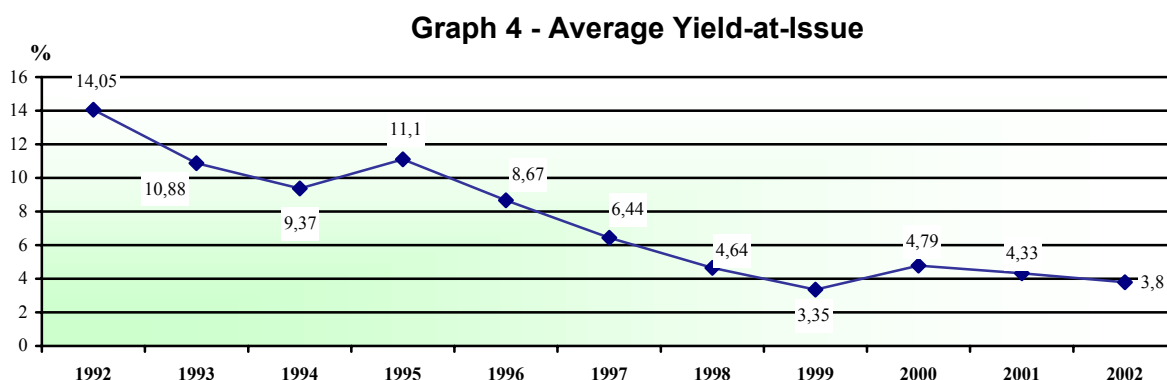


As far as domestic debt is concerned, the shares of fixed-rate bonds (BTPs and CTZs) and floating-rate securities (BOTs and CCTs) are unchanged with respect to last year (about 68% is represented by fixed-rate bonds and 32% by floating-rate securities). In line with the trend of the last five years, in 2003 the issuance policy will aim at keeping the share of floating-rate bonds between 25% and 30%.



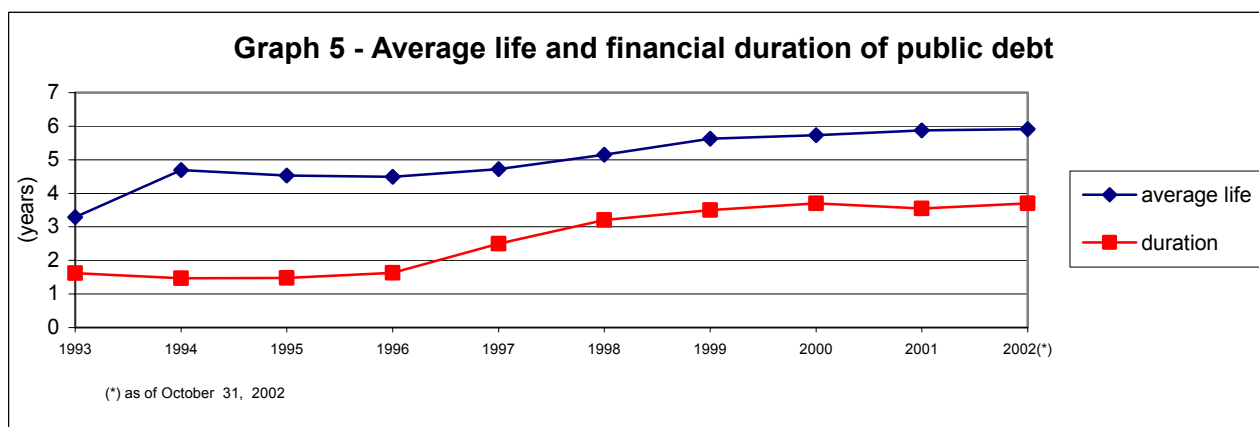
2.2. Results achieved

The strategy adopted last year, defined consistently with market conditions, allowed for a further reduction of the debt average cost at issuance, which decreased from 4.33% in 2001 to 3.80% in 2002 (as of end of October).



The average life of debt has shown a slight increase, in line with the trend recorded over the last three years. At the end of October 2002, the average life was 5.91 years, compared to 5.82 years as of the end of October 2001. This result is primarily due to the new composition of the BTP sector, with a net issuance that, compared to last year, privileged the 15-30 year segment over the 5-10 year one. Indeed in 2002, the Treasury started a new BTP program with a 15-year maturity. After the first two syndicate issues (for a total of 6.5 billion euros), since June the new bond has been offered through the auction system according to a regular issuance calendar.

The financial duration (McCauley duration) rose from 3.55 years at the end of 2001 to 3.7 years in 2002 (as of end-October).



2.3. The exchange program

One of the most relevant innovations of 2002 is the implementation of a bond exchange program designed to:

- ❑ manage refinancing risk more efficiently;
- ❑ obtain a smoother debt redemption profile;
- ❑ enhance the liquidity of the secondary market.

In 2002 eight exchange offers took place, with an average volume of about 900 million euros allotted and an average volume of 1,300 million euros bid. The maturities subject to repurchase were mainly those of 2002, 2003, and 2004, exchanged for benchmark bonds with longer duration.

The mechanism adopted for the exchange was a single-price auction where the Treasury sets discretionally the price and the amount of the bonds to be allotted. In the near future a continuous and straight system on the regulated secondary market will be implemented in order to obtain:

- ❑ a greater flexibility in the choice of bonds to be exchanged and in the timing of transactions;
- ❑ an additional tool to support the secondary market in situations of inefficient performance;
- ❑ a reduction in the cost of funding due to a better control of *front-running* phenomena.

3. Guidelines for debt management for 2003

3.1. The general criteria

The issuance policy of the Treasury over the next year will continue to be based on the following criteria:

- **transparency:** the principal element of transparency is represented by the use of auction as the issuance method, which allows even non-residents access to the primary bond market. Additionally, all the information concerning Treasury issues and debt management are available on the web site of the Public Debt Division (www.tesoro.it/publicdebt). Information to the market is also available thanks to frequent meetings with investors, both national and international, and to continuous contacts with *Specialists in Government Bonds* to discuss the most relevant issues of debt management;
- **regularity:** bond auctions are carried out on the basis of an annual calendar, which is available to investors in the month of November for the following year;
- **predictability:** with the “Guidelines” the Treasury informs the market on the strategy of debt management that will be pursued in the following year, based on the market situation known at that moment. Being committed to a *market-oriented* approach, throughout the year the securities’ supply is decided according to the needs of investors so as to reduce the impact on the market. Accordingly, at the end of each quarter, a calendar is published containing all the information on bonds to be issued in the following quarter;
- **liquidity of financial instruments:** the number of new issues for each instrument is set so as to obtain a volume outstanding consistent with the degree of liquidity reached on the secondary market. The main objective of this policy is to enhance trading efficiency on the market.

The fulfillment of these criteria, that allowed in the past for an increase in the diversification of investors in Italian public debt securities, in terms of both geographical distribution and investor type, will continue to be provided even for the new market segments the Treasury intends to enter next year.

The Treasury is taking in consideration the opportunity to issue instruments with a maturity of more than thirty years (Ultra-Long bonds), for which a significant interest has been shown by institutional investors. The Treasury, moreover, is evaluating the launch of inflation-linked bonds.

As in the case of the 15-year BTP launch, the Treasury will issue the new bonds through a syndicate, in order to evaluate the size and the geographical distribution of demand.

3.2. The BTP and the Eurobond

Notably, the BTP format is characterized by a high level of liquidity. However the Treasury, throughout 2003, will continue to issue Eurobond format securities so as to meet the specific needs of those investors that are not completely satisfied by the domestic bond program.

4. Issuance Calendar for 2003

4.1. Domestic bond issuance program

As usual, the annual issuance calendar, containing the dates of announcements and settlements for the auctions of domestic bonds, was made available on the web site of the Public Debt Division (www.tesoro.it/publicdebt) in November. The auction settlement dates are set according to redemption dates, in order to reduce fluctuations in the liquidity of the banking system.

According to market conditions and the demand of investors, the Treasury will follow the calendar here noted:

Table 1 – Auction Calendar

	First half of the month	Second half of the month
Cash Management Bills – 3-mos. BOT	Issuance tailored to meet cash needs	
6-mos. BOT		X
12-mos. BOT	X	
24-mos. CTZ	(*)	X
3-yr. BTP	X	X
5-yr. BTP		X
10-yr. BTP	X	
15-yr. BTP	The bond will be issued alternatively with the 30-year according to market demand	
30-yr. BTP	The bond will be issued alternatively with the 15-year according to market demand	
7-yr. CCT	X	

(*) See section 4.7

4.2. Cash-management

The Treasury, since last year, devoted the issues of three-month BOTs and the so-called “mini – BOTs” to cover temporary cash unbalances.

Following this strategy, the Treasury, in keeping with the general objectives of debt management outlined above, will progressively adopt a more active management of liquidity with the aim of reducing fluctuations of the cash account.

Such a policy will be carried out resorting to the existing instruments (exploiting the flexibility, in terms of quantity and maturity, of the “mini-BOTs”) and to new and more appropriate ones, such as repo contracts and the inter-bank deposits.

The whole cash-management activity will be carried out compatibly with market efficiency and transparency, in continuous coordination with monetary authorities.

4.3. Six- and twelve-month BOTs

The amount of 6-month BOTs to be issued will be established according to redemption flows and in order to guarantee efficiency on the CCT market. Therefore, the Treasury is committed to assure regular issues and suitable sizes, both at ordinary auction and sessions reserved to Specialists. More in particular, the amount of 6-month BOTs offered at auction will be decided according to previous auction results and to market conditions.

As far as the 12-month BOTs are concerned, it will be regularly issued an amount which will improve the liquidity in the secondary market.

4.4. Commercial Papers

The liquidity management will continue to take advantage of the Commercial Paper program, given the flexibility in terms of maturity, amount and type of investors provided by these instruments.

In 2002 the number of dealers admitted to the program was broadened, while for 2003 the following targets will be pursued:

- a greater participation of the Treasury in the US market, which is notably more liquid than the European one;
- the widening of the spectrum of the offered maturities;
- the access to the main international telematic networks, which are commonly used by a large number of investor to send their bids;

4.5. CCTs

The Treasury will regularly issue CCTs in the first half of each month, expecting to launch not less than 3 new bonds with an average outstanding of 14 billion euros.

4.6. BTPs

BTP 30 years	No new benchmark issues in 2003	First or second half of the month (*)
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In continuity with the issuance policy followed in recent years, BTPs will be offered with the traditional maturities (3, 5, 10, 15 and 30 years), according to the following outline:

Table 2 – New BTP Issuance in 2003

<i>Bond type</i>	<i>Minimum number of new bonds in 2003</i>	<i>Outstanding to reach (billions of Euros)</i>	<i>Auction</i>
BTP 3 years	Minimum 3	12 - 16	First and second half of the month
BTP 5 years	Minimum 2	14 - 18	Second half of the month
BTP 10 years	Minimum 2	18 - 21	First half of the month
BTP 15 years	Minimum 1	14 - 18	First or second half of the month (*)

(*) The Treasury reserves the right to issue 15-year BTP or the 30-year BTP according to market demand.

The Treasury reserves the right to issue first *tranches* of new bonds with more-than-10-year maturity through syndicate, in order to obtain a greater efficiency in placing bonds, thanks to a wider investors' geographical distribution and a more diversified investor base.

The Treasury, moreover, reserves the opportunity to offer the 15-year BTP or the 30-year BTP according to market conditions.

4.7. CTZs

The Treasury aims at reducing the amount outstanding of CTZs. Being aware of the interest shown for this instrument by both national and international investors, during 2003, the Treasury will regularly offer CTZ in the second half of the month auction, while keeping the option to issue these instruments also in the first half of the month auction.

It is expected that not less than three new bonds will be issued, with an outstanding between 11 and 15 billion euros.

5. Foreign currency program

During 2003 the Treasury will continue to be present in international capital markets through a two-leg action:

1. the benchmark program in US dollars, which already performs a strategic role for the issuance policy of the Republic of Italy;
2. the funding activity in non US-dollar currencies.

With respect to the program in US dollars, the Treasury aims at maintaining the benchmark status among non-US sovereign issuers. The issuance policy will continue to guarantee high liquidity to new bonds, through issues of appropriate sizes and, where possible, by having them quoted on the principal electronic platforms. The Treasury is focusing greater attention on improving relationships with investors, in particular with those residing in the USA and Asia, so as to promote the Republic of Italy as a global issuer of bonds and, consequently, to attract new potential investors. In this way, the Treasury aims at establishing a reliable funding channel that can be complementary to the domestic bond issuance program.

The funding activity on other markets, conducted through the M-T-N program - which allows the Treasury to place bonds denominated in several foreign currencies - will be based mainly on arbitrage opportunities. Indeed, by means of small size transactions, which occasionally become benchmark in the respective markets, the Treasury will be able to react with flexibility to arbitrage opportunities on international markets, resulting from the comparison with the cost of *funding* on the domestic one.

In terms of volumes, the Treasury plans to issue a total of at least 12 billion euros, with the following breakdown:

- at least 10 billion dollars, as a part of the benchmark program in US dollars;
- the remaining in other markets.