

*2010*

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Guidelines  
for public debt management

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Ministry of the Economy and Finance  
Department of Treasury  
Directorate II



# **Guidelines for Public Debt Management**

**2010**

## ***Foreword***

During 2009, the international financial crisis has continued to produce significant effects on the entire Euro area government bond market. The performance of Italian government bonds was largely influenced, on the one hand, by changes to risk aversion on international financial markets and hence on the global nature of cyclical and structural factors that determined it and, on the other, by the Eurosystem's liquidity conditions resulting from the monetary policy choices of the European Central Bank. Hence, as in 2008, also in 2009 factors of international instability are the ones which have mainly led government bond performance indicators, at the expense of domestic factors which, instead, appear to have played a less significant role.

Despite this general context, characterized by imbalances and conditions of significant instability on financial markets, the Treasury continued to guarantee the financing for the State Sector Borrowing Requirement through a policy of debt management appropriately aligned with changing market conditions. Some flexible instruments in the bond auction process introduced at the end of 2008 have been maintained and refined, in addition to issuance decisions aimed at achieving the objectives of the Treasury in a context of greater adherence to the changed conditions of the euro area government bond market. The increasingly intense dialogue with market operators has allowed the principles of transparency, predictability and regularity of debt issuance, even with the appropriate modifications, to be confirmed and implemented for the benefit of the issuer and the investors in Italian public debt.

This approach was also maintained when, during the year, tensions on the markets gradually loosened. Faced with a progressive improvement of inter-bank market conditions and with a moderate increase in the liquidity of trading on the secondary market, the Treasury quickly made use of the changed environment to place on the market instruments whose launch is notoriously more complex, like two new nominal fixed rate bonds with 15 and 30 year maturities, and a new European inflation-linked bond (BTP-€) on the 30 year segment. It was thus possible to ensure a continuity of issuances on the market on all sectors of the yield curve, while allowing the issuer to achieve its strategic aims in terms of exposure of the State budget to market risks in a more efficient manner.

While fully aware of the unpredictability of market dynamics, the Public Debt Management Guidelines for the year 2010 cannot disregard the results achieved in the year about to close and the management policies found below.

Like last year, the detailed account of debt management in 2009 is postponed to an in-depth document to be published in the first months of 2010.

## ***The 2010 issuance program***

### ***Introduction***

With the second half of 2009 risk aversion on the markets gradually declined even if in a rather discontinuous manner. On the secondary market for government securities the volume of trading began to rise again and the efficiency of quotations improved, but the overall picture does not yet seem to be immune to profiles of fragility that require constant monitoring. To ensure continuity in the policy of issuing debt with regard to regularity, transparency and predictability, the issuance choices will be on the whole aimed at consolidating the results achieved in terms of exposure to interest rate and refinancing risks, within a framework of containment of the cost of debt over the medium term, consistent with the evolution of interest rates that characterize the euro area.

Also in 2010, therefore, a large proportion of the issues will continue to be represented by on-the-run securities on the basis of the traditional Annual Auction Calendar and of the quarterly Issuance Program<sup>1</sup>. When market conditions will make it necessary, and depending on the liquidity situation of the single securities, the Treasury will reserve the option to offer also off-the-run securities. As was the case during 2009, the choices of off-the-run securities to be reopened will be dictated, in keeping with the overall objectives of debt management mentioned above, by a set of assessments, that will range from the need to contribute to the efficiency of trading on the secondary market (for individual bonds or segments of the yield curve), to analysis of the demand profile for the different instruments offered by the Treasury.

Due to their characteristics of transparency and uniformity of access to the primary market of Treasury issues, auctions will remain the main method for government bond placements. Thanks also to the recent technological innovations introduced, in fact, the auction system continues to ensure conditions of maximum efficiency for placements, in terms of implementation and operational risk.

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<sup>1</sup> As in the past, both these documents are accessible on the Italian Public Debt website ([www.publicdebt.it](http://www.publicdebt.it)).

Auctions of medium-long term securities will continue to be conducted in accordance with the principle of the discretionary determination by the Treasury of the amount placed, within a range previously announced. This range will be in reference to the single security in the case of on-the-run issues, whereas in the case of off-the-run issues it will cover all the securities offered in the same auction. The only exception to this rule will be Euro area inflation-linked bonds (BTP-€s), for which the range of the amount offered will include all securities issued at the same auction, both on-the-run and off-the-run.

In continuity with the choices of recent years, also in 2010, the issuing procedure based on syndication will be used for the introduction of the new long-term nominal benchmarks (BTPs with maturities above ten years) and for the new BTP-€s.

As regards the CCT sector, the Treasury will continue to ensure the proper functioning of the market through an appropriate strategy of issuance management and market monitoring.

Money market instruments, such as 3 month bills (BOTs), or non-standard Treasury Bills (so-called flexible BOTs) and commercial paper, will be used to ensure the coverage of temporary cash needs. The regular performance of the 6 and 12 month BOT issuance program will be ensured, whose role, which is to render efficient access to medium-long term instruments compatible with the evolution of the State's cash requirements, remains crucial.

Issues in foreign currency, primarily on the global dollar market, and private placements, as in past years, will attempt to confirm the presence of the Treasury on international markets and to broaden the investor base. Issuance decisions will be determined both by conditions of demand and of reduction of financing cost, and will feature a fully flexible approach in terms of timing and issuance method.

Finally, it should be reiterated that all of the Treasury's borrowing choices will be significantly influenced by the need to continue to provide liquidity and efficiency to the secondary market in order to offer investors, whether institutional or retail, products that really facilitate their investment choices and ensure the ability to effectively enact their portfolio strategies.

### ***The Issuance program for securities placed through public auction***

The market will continue to be informed about Government auctions of nominal and euro-area inflation-linked bonds by means of the annual auction calendar, published on the Public Debt Management area of the Treasury Department's website ([www.publicdebt.it](http://www.publicdebt.it)) which lists, in

addition to the auction dates, also the announcement and settlement dates of the different types of securities. Moreover, at the end of each 3 month period, the Quarterly Issuance program will be published, announcing the new securities that will be introduced on the market in the following quarter and the minimum outstanding volumes that the Treasury commits itself to achieve for each security.

The issuance frequency will not undergo significant changes. While 3-month BOT placements will be made at mid-month, based on cash needs, the so-called flexible BOTs may be offered – for the same purpose – at mid and end-of-month auctions. 6 month BOTs and 24 month CTZs will, as usual, be offered regularly at the end of the month, while for 12-month BOTs the scheduled time remains mid-month.

Also medium-long term on-the-run security issues will respect the timing established over the past years: 3 and 10 year BTPs at the end-of-month auction and 5 year BTPs at the mid-month auction; 15 and 30 year BTPs will be offered at mid-month auctions according to demand and market conditions. For off-the-run security issues, timing will be more flexible: given the nature of these auctions, whose objective is essentially linked to the need to ensure a better functioning of the secondary market going to meet the specific needs of demand, they may be held either in the mid-month or end-of-month auction.

CCTs will respect the usual placement schedule, therefore they will be offered at end-of-month auctions along with 3 and 10 year BTPs.

Inflation linked securities will be proposed in a dedicated auction at the end of each month, according to the dates listed in the Annual Calendar. This regularity will be disregarded only when in the same month the Treasury launches a new security through syndication, or if market conditions are such that a suspension of supply is needed in order to ensure orderly trading on the secondary market.

It is nevertheless possible that the Treasury may proceed, in exceptional cases, to the reopening of outstanding securities (both short and medium-long term), without respecting this calendar: in these cases – which can occur only to respond to needs for liquidity and market demand and after extensive consultation with market participants – the auctions will be announced using the usual means of communication.

Table 1 below summarizes the auction frequency for each instrument.

**Table 1: Auction schedule**

|                             | <i>Mid-month Auction</i>  | <i>End-of-month Auction</i> |
|-----------------------------|---|-----------------------------|
| <i>Flexible BOTs</i>        | <i>Issued according to cash needs</i>                                   |                             |
| <i>3 month BOTs</i>         | <i>Issued according to cash needs</i>                                   |                             |
| <i>6 month BOTs</i>         |   | <i>X</i>                    |
| <i>12 month BOTs</i>        | <i>X</i>  |                             |
| <i>24 month CTZs</i>        |   | <i>X</i>                    |
| <i>3 year BTPs*</i>         |   | <i>X</i>                    |
| <i>5 year BTPs*</i>         | <i>X</i>  |                             |
| <i>10 year BTPs*</i>        |   | <i>X</i>                    |
| <i>15 and 30 year BTPs*</i> | <i>The two securities will be offered on the basis of market demand</i> |                             |
| <i>7 year CCTs*</i>         |   | <i>X</i>                    |
| <i>BTP€is</i>               |   | <i>X</i>                    |

\* Please note that, for the categories marked with an asterisk, off-the-run securities with a similar residual maturity may be offered at medium to long term auctions other than those in the table.

### *Nominal securities sector*

#### **BOTs and liquidity management**

BOT issues will continue to be conducted according to the traditional maturities of 3, 6 and 12 months.

12 and 6 month BOTs will be offered regularly, respectively at the middle and the end of each month, and amounts will be determined according to demand and market conditions. For both maturities, in 2010 the Treasury will continue to offer securities through ordinary auctions and re-openings reserved to Specialists in Government bonds; the latter, traditionally provided for 6 month BOTs, since 2009 have been extended to include 12 month BOT issues.

The amount offered at the re-opening will usually be 10% of the nominal amount offered in the ordinary auction; however, this percentage represents a minimum value, which may be increased,

after the ordinary auction closes, in keeping with market conditions and demand needs expressed by the operators.

To determine the issue of 6 month securities, the Treasury will pay particular attention to ensure efficiency in the CCT market.

Quarterly securities, as well as BOTs issued with non-standard durations (so-called flexible BOTs), will be offered fully exploiting the flexibility of the instrument in relation to cash needs.

Regarding the functioning of the primary market, competitive bidding will remain the placement system for the whole BOT sector. Issues will continue to be conducted through the auction system inaugurated in 2009, which provides for the submission of bids by operators in yield terms rather than price, according to the prevailing practice in the Euro area money markets.

In 2010, the Treasury will also continue to use the Commercial Papers (CP) instrument, also in non-euro currencies, to achieve maximum flexibility in terms of amounts and maturities, essential requirements for an accurate liquidity management. The use of CPs will also aim at increasing the diversification of investors operating on short and very short-term instruments offered by the Treasury.

Finally, during the next year the Treasury will maintain its presence in the money market on short and very short-term maturities, through financial transactions related to the management of the Treasury account daily balances (OPTES). These transactions may take place via auction or bilateral negotiation, and may have overnight or longer duration, according to cash needs and market conditions. During 2010, the Ministry of Economy and Finance, in agreement with the Bank of Italy, might introduce new ways of carrying out OPTES operations, also in light of the recent approval of the State Budget reformation law (so-called “Stability Law”) and the resulting innovations that will involve the management of the State treasury and of the Availability Account held by the Treasury at the Bank of Italy.

## **24-month CTZs**

Faced with a redemption volume of almost 30 billion euros, 5 billion more than in 2009, the Treasury will offer to the market CTZs that will bring the total outstanding amount to a moderate increase compared with the end of the present year. Complete regularity of end-of-month auctions will be guaranteed, where, also during the year that is about to close, there has been a strong interest both from domestic institutional investors and from major international players. The quantities

offered to the market in individual auctions will be appropriately tailored also according to changes in the monetary policy which normally has a major impact on the investment decisions of this sector's operators. Particular attention will be given to developments, in this context, of demand from the retail sector.

## **CCTs**

In 2010 approximately 37.7 billion euros of CCT redemptions, a lower volume with respect of 2009, a year during which the stock of outstanding CCTs was reduced significantly. For 2010, the issuer's ongoing commitment to ensure the proper functioning of the market will remain, both in terms of issuance policy and of the management of outstanding instruments. The market's liquidity will continue to be constantly monitored and analyzed on the secondary wholesale market, in terms of trading and prices. In particular, 6-month BOTs will continue to be offered in volumes appropriately suited in each individual auction in a way that the CCT market continues to maintain adequate standards of efficiency.

Overall, these issues will be enough to substantially balance the maturities of the year.

Also in 2010 the Treasury reserves greater flexibility in the securities that will be offered to the market, including the possibility of proposing off-the-run instruments according to market conditions. As for on-the-run securities, the auction will be marginal with discretionary price fixing by the Treasury according to the situation on the secondary market, within a previously announced range of amounts on offer. If more than one off-the-run security is issued in the same auction, the range on offer will include them together.

As before, the Treasury will keep its commitment to provide a broad diversification of coupon cycles and to reach a final volume of outstanding securities apt to maintain adequate levels of efficiency on the secondary market.

## **Medium-term nominal BTPs (3, 5 and 10 year)**

The Treasury will guarantee complete regularity of 3 and 10 year BTP auctions, offered in end-of-month placements, while the 5 year BTP will be offered at mid-month auctions. In choosing the amounts offered in the monthly auctions, market conditions will be carefully evaluated, to ensure a successful outcome of the placements, both for the investors and for the issuer, and guarantee



appropriate levels of liquidity on the secondary market. New benchmark bonds will be introduced to contain the refinancing risk while, especially for the 10 year sector, the development of each security's outstanding amount, during the auction program, will also be managed so as to contribute to the efficiency of the recently introduced futures contract.

As for 2009, marginal auctions will be held with the discretionary price setting referred to above, and the Treasury may resort to the re-opening of off-the-run securities when required by market conditions and permitted by the general debt management strategy. As with CCTs but unlike BTP€s, the issue of on-the-run securities, offered singularly, and off-the-run securities, whose range of volumes offered at auction will include them together, will continue to be different.

### **Long-term nominal BTPs (15 and 30 year)**

The long-term BTP sector will have a strategic importance for the issuance policy of 2010. On the basis of the development of market conditions and of the yield curve, the Treasury will be committed primarily to support the liquidity of bonds introduced in 2009 (on-the-run securities) of 15 and 30 year maturities. In proposing these issues the Treasury reserves extensive flexibility in choosing the maturity to be issued at the mid-month auction, when also long-term off-the-run securities may be reopened to meet, consistent with the overall general strategy, the needs of demand. Auctions will be performed in the same way as those of the medium term BTP sector both for on-the-run and off-the-run securities.

To the extent that market conditions make it necessary and feasible, the Treasury may also launch new securities through syndications, an instrument that has proved particularly effective, even in highly volatile conditions like those of 2009, to ensure a wide and immediate distribution of the new instruments among the final customers.

### ***The inflation-linked bonds (BTP€is) sector***

The BTP€ issuance policy will follow the path of the past years, based on monthly placements which will take place via auction or, in the case of new securities, via syndication. In the monthly auctions – whose dates have, since a few years, been published on the Annual Calendar – the Treasury may propose one or more securities according to how the market situation for this sector evolves. Both in the case of a single security and in that of multiple securities, unlike in the past

years, the Treasury will announce, as with nominal securities, a range of volumes on offer within which the marginal price and the resulting amount allocated for each individual security will be fixed at its discretion. The previous system, under which in each auction each security was offered individually with the announcement of the maximum amount on issue, is thus superseded. From 2010, at the end-of-month auctions one or more securities (whether on-the-run or off-the-run) may thus be offered with the indication of an aggregate offer range.

The Treasury's strategy for the sector will be aimed at consolidating the BTP-€ share on the stock of the outstanding debt. Taking into account also the September redemption, when the second 5 year BTP-€ launched by the Treasury reaches maturity, the total volume of issues will be such to guarantee the above mentioned objective, market conditions permitting. The offer will be distributed in order to contribute to the liquidity of the entire real yield curve, also by launching new securities on parts of the European inflation curve that are not currently covered. In this sense, attention will be paid particularly toward those areas that currently have securities with an outstanding amount such as to require their closure, taking into account the refinancing risk and the preferences of investors.

### ***Exchange and buyback transactions***

In 2010, as in past years, the Treasury may resort to exchange and buy-back transactions, to manage the refinancing risk by smoothing out the redemption profile and supporting at the same time the liquidity and efficiency of the government bond secondary market.

The Treasury will evaluate each time if such transactions are to be carried out on the primary market, using the auction system managed by the Bank of Italy, or on the regulated secondary market, through the telematic trading system.

### ***The foreign currency issuance program***

#### ***US dollar global benchmark program***

Over the next year, depending on the conditions of the financial market, of demand and of economic convenience, the Treasury will continue to maintain its presence on the dollar market,

with issues in Global format, of an amount equal to at least 2 billion USD, on one or more segments of the yield curve.

***Issuance activity on other markets***

The Medium Term Note (EMTN) program for non “domestic” issues, in euros or other currencies, will continue to be used during 2010, both in public and private placements, should the opportunity arise. This program aims to meet the demand coming mainly from institutional investors. The opportunity for issuance will be determined in relation to market conditions.

For private placements, the proposals received in response to the demand from one or more institutional investors will be evaluated, and the maturities considered cannot be less than 3 years, whereas the minimum trading amount must be at least 500,000 euros, for a nominal amount of normally not less than the equivalent of 200 million euros. The Treasury will evaluate whether or not to proceed with these issues by verifying the reduction of the cost of funding compared to the BTP curve and avoiding any overlaps with “public” issuance program.