

AUCTION EXECUTION METHODS

1. INTRODUCTION

Government bonds can be placed via:

- public auction, so as to guarantee access by an extensive group of investors and maintain a high level of competition and transparency;
- a bank syndicate chosen from Government bond Specialists, that collects final investors' orders (a placement syndicate);
- electronic trading platforms.

The Italian Treasury prefers public auctions for issues on the domestic market, normally limiting the use of the placement syndicate to the introduction of new instruments (like the first issue of BTP€is in 2003 and of CCTeus in 2010) or when very in-depth evaluations need to be made as regards market interest, the quantity to offer or the issue price of the bond, as in the case of long-term BTPs and BTP€is.

A new issue method was introduced for the BTP Italia, the Government bond linked to Italian inflation, first issued in 2012 and envisaged for retail market demands. It uses the Italian Exchange's MOT (regulated bond market dedicated to retail trading) electronic platform.

2. AUCTION CALENDAR

At the end of every calendar year, the Treasury drafts and publishes the “[Annual Auction Calendar](#)” for the next year together with the “[Public Debt Management Guidelines](#)”, to inform dealers well beforehand on the frequency of auction placements and the quality profile that will guide the issuance policy during the year. In detail, the Calendar contains all the dates of the issue press releases, of the auctions and their settlements, grouped by bond category. The “[BOT Auction Calendar](#)” is also published, with the specifics for the bonds on this segment for the year, including the issue and maturity dates.

Moreover, the “[Quarterly Issue Programme](#)” is published four times a year. It discloses all the information regarding new medium/long-term bonds to be placed via auction and re-proposed regularly during the quarter, together with the information regarding the offer of outstanding bonds.

Lastly, a press release is made before each auction. Aside from announcing the bonds to be issued and their characteristics, it indicates the quantities offered in the auction as well as all relevant dates, including the bond settlement date.

Presently, the settlement date for all Government bonds is two business days following the auction date ($t + 2$). For BOTs this usually coincides with the maturity of corresponding bonds, so as to facilitate reinvestment. When the settlement date of medium/long-term bonds does not coincide with the date in which the bond's interest begins to accrue (the interest commencement date), subscribers pay the Treasury the corresponding accrued interest¹.

The settlement of all bonds is through the settlement and payment service run by Monte Titoli and the Bank of Italy.

¹ Coupon interest accrued during the interval of time between the interest commencement date and the bond's settlement date. This ([Metodo di calcolo dei dietimi e delle cedole dei titoli di Stato.pdf](#)) links to the document [in Italian] explaining the interest accrual and coupon calculation methods.

3. EXECUTION OF A GOVERNMENT BOND AUCTION

Government bond auctions are carried out at the Bank of Italy, Market Operations Service - Public Debt Division, in the presence of an employee of the same Bank and an official (the Treasury Officer) from the Ministry of Economy and Finance (MEF) representing the Minister who is responsible for the auction's regularity. The MEF Treasury Officer can also participate to auction operations via video-conference.

Authorized dealers' bids to participate in the auctions are sent online, using the National Interbank Network. Dealers can place bids for each bond offered until 11 am of the auction day. The system automatically rejects bids beyond the deadline. Dealers can repeatedly adjust their bids, substituting the previous ones, since the system only considers the final bid made within the deadline as valid.

So as to maintain data privacy, bids sent online are encrypted on the receiving monitor at the Bank of Italy. They can be decrypted with a digital key only after 11 am by an official of the Bank of Italy in charge of the auction. A series of automatic operations thus begins. These produce a printout in which bids are listed in decreasing price order or increasing yield order.

The summary printouts are an essential part of the auction minutes. The latter are signed by the Treasury Officer and by the Bank of Italy employee. They include the auction results and the circumstances that characterized their execution. Moreover, immediately after the auction's end, the information that most interests the market is broadcast via press release, both by the Bank of Italy and the MEF - and published on their websites - as well as by Bloomberg and Reuters.

Dealers' participation in the auctions is regulated by a special agreement drawn up with the Bank of Italy ("**Agreement between the Bank of Italy and dealers authorized to participate in Government bond placement, purchase and exchange operations**").

The Treasury makes use of two kinds of auction:

- **a competitive yield auction**, for **BOTs**;
- **a marginal price auction** where the auction price and the quantity issued is determined discretionally, used for **CTZs**, **BTPs**, **CCTs/CCTeus** and **BTP€is**.

3.1 Competitive yield auction

Unlike other Government bonds, BOTs are placed with an auction in which dealers place their bids in yield, not price, terms. Moreover, in a competitive yield auction each bid, if placed, is awarded at the rate proposed. It follows that a competitive yield auction closes with a range of allocation rates. With these, the Bank of Italy calculates the weighted average yield and the corresponding weighted average price.

Authorized dealers can place up to five bids. Their yields must differ by at least one thousandth of one percent. Bids must be of at least 1.5 million euros and at most the entire quantity offered by the Treasury at the auction. Bids for greater amounts will be considered only for the amount on auction. The minimum denomination for investors is 1,000 euros.

Bids at the lowest yields are allocated first, followed by the others in increasing yield order, until the amount on offer is covered. If bids at the final awarded yield cannot be completely satisfied, they will be divided proportionally, rounding off when needed.

To avoid that the weighted average yield is negatively influenced by bids made at yields that are not in line with the market, a minimum acceptable (or safeguard) yield is calculated. Similarly, a maximum acceptable (or exclusion) yield is calculated in order to exclude any speculative bids from the auction. These yields are calculated as in the following example:

BOT AUCTION ALLOCATION EXAMPLE.

Dealers' bids can be made at positive, negative or null yields.

As established by a [decree of the Ministry of Economy and Finance](#) ², dealers must apply the weighted average price of the auction to investors who subscribe bonds of the same auction.

3.2 Marginal price auction

The marginal price auction is used to place medium/long-term bonds. In a marginal price auction allocated bids are all awarded at the same price, the marginal price. The auction price and quantity is determined discretionally. In this way the quantity issued is not set beforehand, but is between a minimum and maximum amount announced in the press release published some days before the auction.

The amount placed is determined by excluding bids made at prices that are not suitable with respect to market conditions, on the basis of a ranking in which dealers' bids are listed anonymously. The lowest price among those bid by awarded dealers is the auction (marginal) price which is applied to all awarded dealers. If bids at the marginal price cannot be completely satisfied, they will be divided proportionally, rounding off when needed.

Dealers can place up to five bids, each at different prices, for a minimum amount of at least 500,000 euros of nominal capital and less than the amount being issued. Bids beyond the latter limit will be accepted up to the amount on offer. The minimum denomination for investors is 1,000 euros.

Prices must vary by at least one thousandth for CTZs and one hundredth for the other bonds. Other variations will be rounded upwards.

4. AUCTION REOPENING RESERVED FOR GOVERNMENT BOND SPECIALISTS

Medium/long-term Government bonds and 6/12-month BOTs have reopenings (a supplementary placement) reserved for [Government bond Specialists](#). To be able to access the reopening, Specialists must have taken part in the main auction with at least one valid bid. Bonds are assigned at the marginal price of the ordinary auction for medium/long-term bonds and at the weighted average price of the ordinary auction for BOTs. The maximum amount offered in reopenings is usually 10% of the ordinary BOT issue. For medium/long-term bonds it is 30% of the amount offered in the first tranche of new bonds and 15% for the following reopenings.

The amount to assign to each Specialist is proportioned to what the dealer subscribed in the previous auctions and, in part, is linked to the dealer's performance on the secondary market in the wholesale trading venues chosen³. Should one or more Specialists, during the reopening, place bids for amounts lower than what they are entitled to, the residual amounts will be redistributed proportionately to the other Specialists using the above mentioned criteria.

The bidding deadline of the reopening reserved for Specialists is extended to 3.30 pm of the business day following the ordinary auction. Settlement of the supplementary auction is with the same value date as the ordinary auction.

5. RECOVERY PROCEDURES

² Government bond placement transparency decree of 15 January 2015.

³As per articles 23 (paragraphs 10, 11, 13 and 14) and 28 (paragraph 2) of Ministerial Decree no. 216 of 22 December 2009.

The auction mechanism includes recovery procedures in case a dealer's IT system malfunctions. The dealer must contact the Bank of Italy to inform of the problem and obtain authorization to transmit bids via fax.

Recovery procedures are also in place in the case of network downtime. In these cases the bidding deadline is postponed. The decision to postpone and the new deadline are communicated to dealers using economic-financial information circuits. Should the interruption last beyond 5 pm, the MEF will decide on how to proceed and its decisions will be communicated with the above mentioned means.