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Bond Market Forum

Secondary Market Liquidity in Domestic Debt Markets

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The Impact of the Investor Base on Domestic Treasury Securities Market (Republic of Poland)



Republic of Poland
Ministry of Finance
Financial Assets and Liabilities Department

10th Annual OECD-WBG-IMF Global Bond Market Forum

Washington DC, April 2008





Poland's key position in the enlarged EU

- European Union Member since 1 May 2004
- The largest and most populated new EU member State
- Poland's GDP accounts for ca. 41% of the new members' combined GDP

Key Statistics:

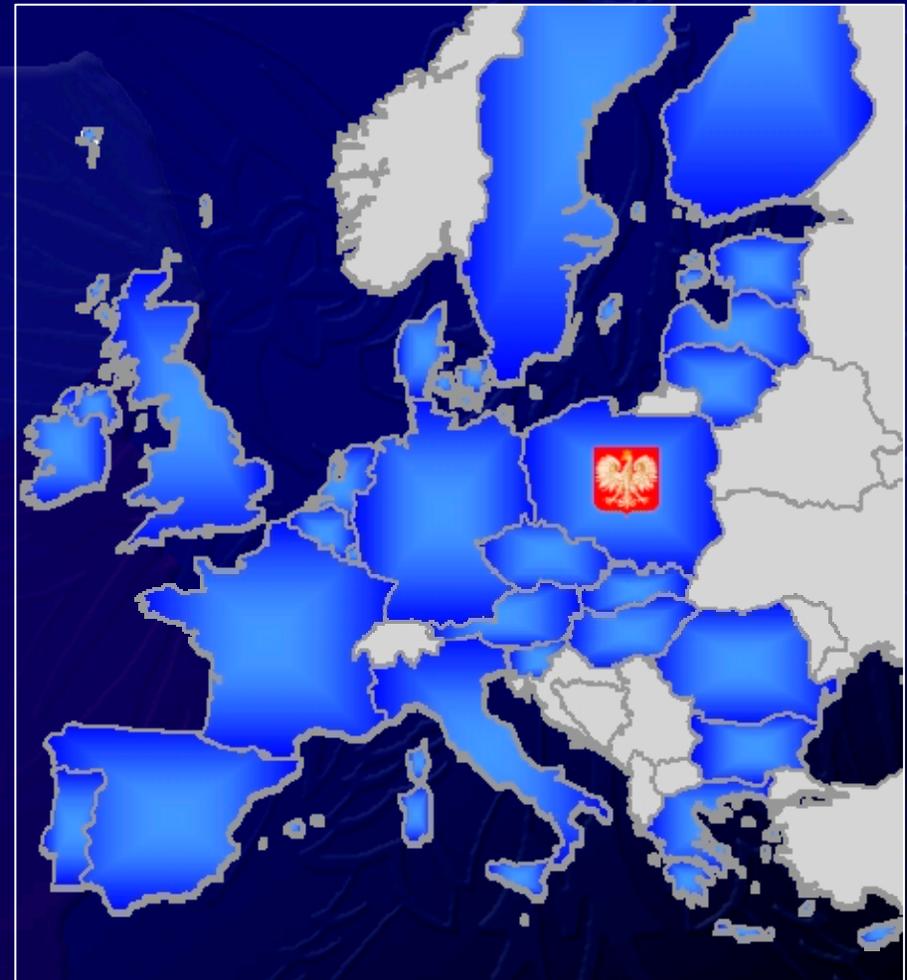
Nominal GDP 2006:	EUR 272 billion
Nominal GDP 2007:	EUR 307 billion

Population:	38 million
GDP per capita 2006:	EUR 7,139
GDP per capita 2007:	EUR 8,090

GDP growth in 2006:	6.2%
GDP growth in 2007:	6.5%

Ratings

- A2 Stable by Moody's
- A- Stable by S&P
- A- Stable by Fitch
- A- Stable by JCRA
- A- Stable by R&I





Domestic Treasury Securities Market



Source: *Ministry of Finance*



Development of the domestic market (1)

- Relatively short history – since the political and economic transition of 1989
- Starting point in 1989: vast amount of foreign non-marketable debt, in majority not serviced due to solvency problems during the 80s
- Since 1989 the development from passive servicing into active management of public debt
 - restructuring and reduction of foreign debt
 - 1991 and 1994 - Paris Club - official creditors
 - 1994 London Club - commercial banks
 - establishment and development of domestic market of Treasury securities
 - regular T-bills auctions since 1991
 - regular fixed rate T-bonds auctions since 1994
 - borrowing in international markets
 - first bond issue in 1995
 - Substantial changes in debt structure, institutional and market environment, legal framework, organisation, infrastructure, methodology and instruments





Development of the domestic market (2)

Date	Wholesale instruments
1989	First T bonds
1991	First T bills
1992	1-year inflation-linked bonds
	3-year floating rate bonds
1994	2 and 5 year fixed rate bonds
1995	10-year floating rate bonds
1999	10-year fixed rate bonds (in response to demand from Open Pension Funds)
2002	20-year fixed rate bonds (in response to demand from insurance companies)
2004	12-year inflation-linked bonds
	3 and 7 year floating rate bonds (WIBOR)
2007	30 year fixed rate bonds
	Retail instruments
1999	2 and 4 year savings bonds
2004	10 year savings bonds





Public debt management strategy

Debt Management Strategy objective:

- Minimisation of debt servicing costs over a long term, within accepted limitations regarding the level of associated risks:
 - ✓ Refinancing,
 - ✓ Exchange Rate,
 - ✓ Interest Rate,
 - ✓ State Budget Liquidity,
 - ✓ Credit and Operational

Issuance Strategy:

- Aimed to broaden and deepen investor base for Poland
- Development of liquid benchmark yield curves
- Improving efficiency of domestic Treasury securities market
- Access international markets for strategic positioning and funding cost savings





Central government financing

- Relatively low borrowing requirements enable more effective debt management and achieving the desired debt structure
- Domestic market being the primary financing source

Financing by source in 2006-2008 (Treasury securities, EUR bn)

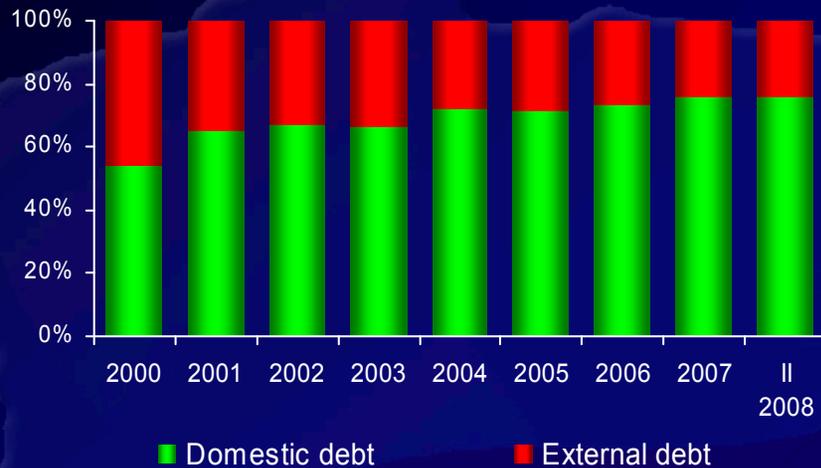
	2006		2007		2008 F	
	Net	Gross	Net	Gross	Net	Gross
Domestic market	10.4	32.6	8.4	28.9	10.2	30.9
Treasury bills	0.4	7.2	-1.2	5.3	0.0	5.4
Fixed rate Treasury bonds	8.4	21.2	6.2	17.7	6.4	19.8
Floating rate Treasury bonds	1.5	2.8	3.4	4.9	3.1	4.0
CPI linked Treasury bonds	0.4	0.4	0.3	0.3	0.6	0.6
Savings bonds	-0.3	1.0	-0.3	0.7	0.1	1.1
Foreign markets	3.0	3.5	3.2	3.2	3.9	3.9



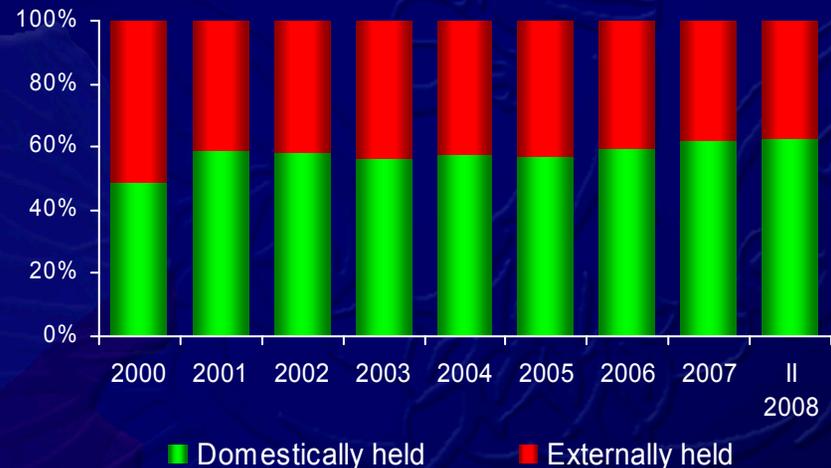


Domestic vs external debt

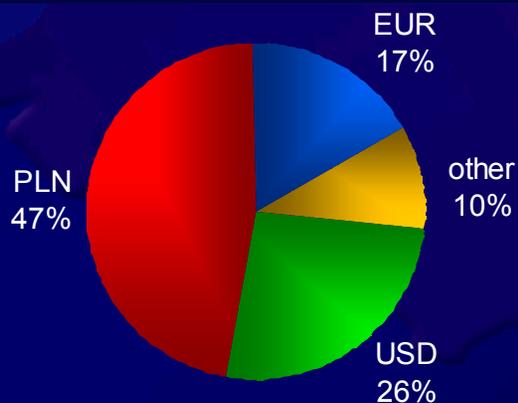
State Treasury debt by place of issue



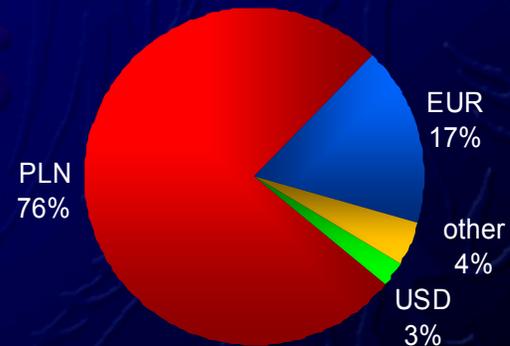
State Treasury debt by residency



Currency structure of State Treasury debt (December 1999)



Currency structure of State Treasury debt (February 2008)



Source: Ministry of Finance



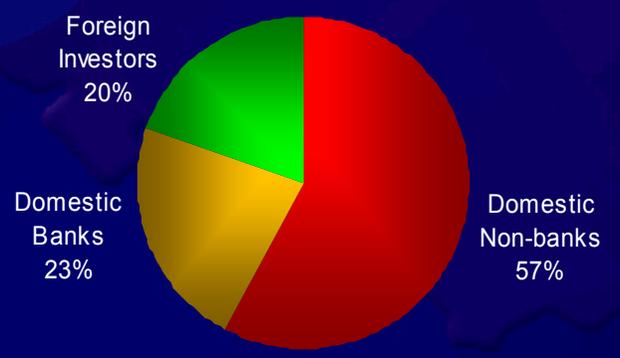
Domestic debt structure

- Primary Dealers system established in 2003
- In 2006 first foreign banks appointed as Primary Dealer – deeper institutional involvement on the domestic market
- New electronic platform created jointly with MTS in 2004 – opportunity to trade Polish bonds in a well-known environment
- Twelve most liquid benchmarks reaching or exceeding the outstanding amount of EUR 5bn

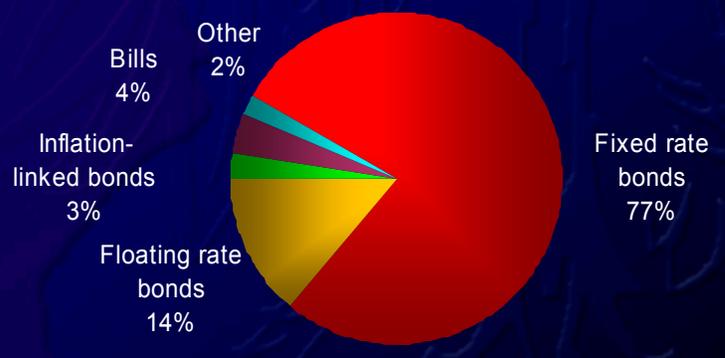
Domestic debt principal payments (EUR bn, February 2008)



Holders of domestic State Treasury debt (February 2008)



Domestic debt composition by instruments (February 2008)



Source: Ministry of Finance



Investor Base



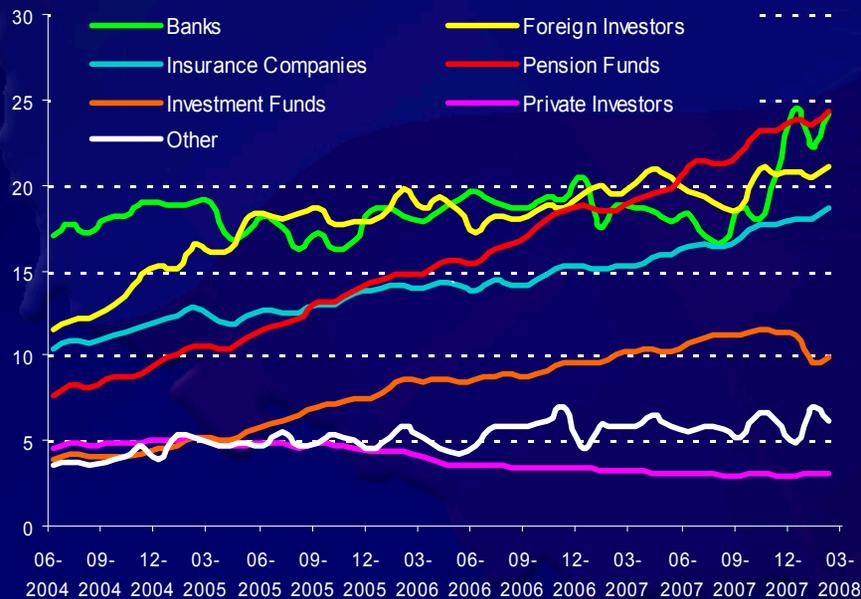
Source: *Ministry of Finance*



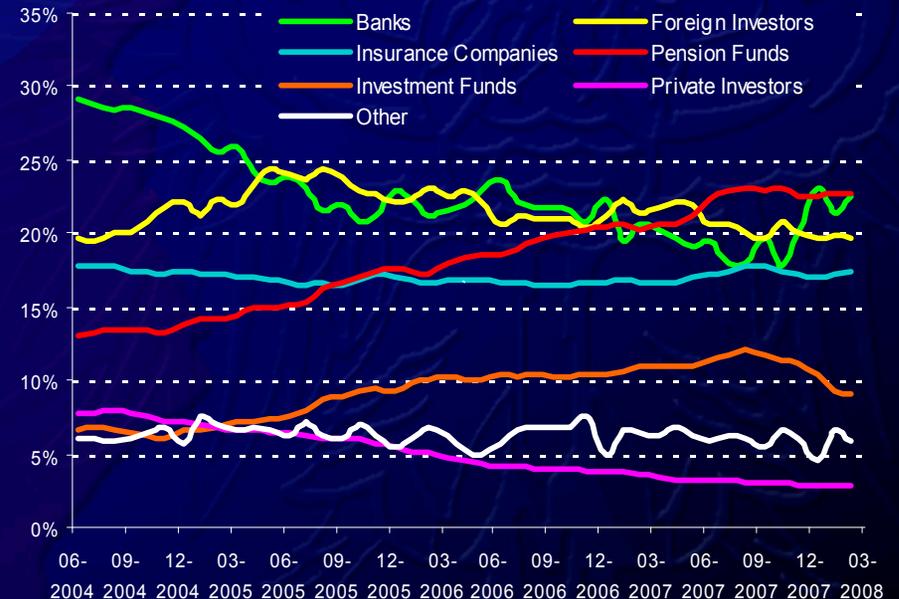
Domestic debt holders

- Diminishing role of domestic banks (before "credit crunch")
- Stable share of foreign investors and insurance companies
- Increasing role of long-term investors from a non-banking sector (OPF)
- Decreasing share of investment funds during "credit crunch"

Holders of domestic T bonds (EUR bn)



Holders of domestic T bonds (% share)



Source: Ministry of Finance



Domestic investor base

- Steady growth of assets of stable, long-term domestic investors
- Net assets increase since 2000 (annual average):
 - Open Pension Funds – 47% p.a.
 - Investment Funds – 54% p.a.
 - Insurance Companies – 19% p.a.



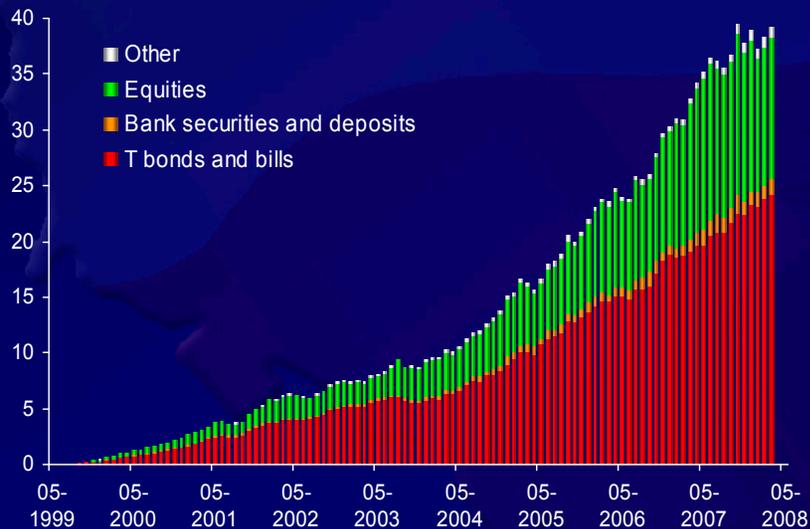
Source: Ministry of Finance



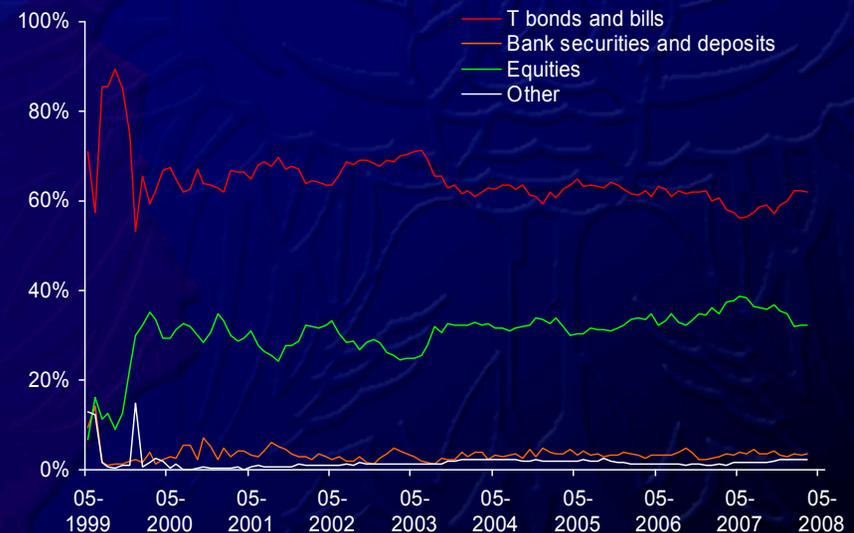
Open Pension Funds investment portfolio (1)

- Pension system reform introduced in 1999; privately managed Open Pension Funds established
- OPF accumulating assets for 10 years; first pensions from OPF to be paid in 2009
- Foreign investments – on average 1% of total investment portfolio (legal limit 5%)
- Treasury bonds – on average 65% of the portfolio

Open Pension Funds investment portfolio
(EUR bn)



Open Pension Funds investment portfolio
(% share)

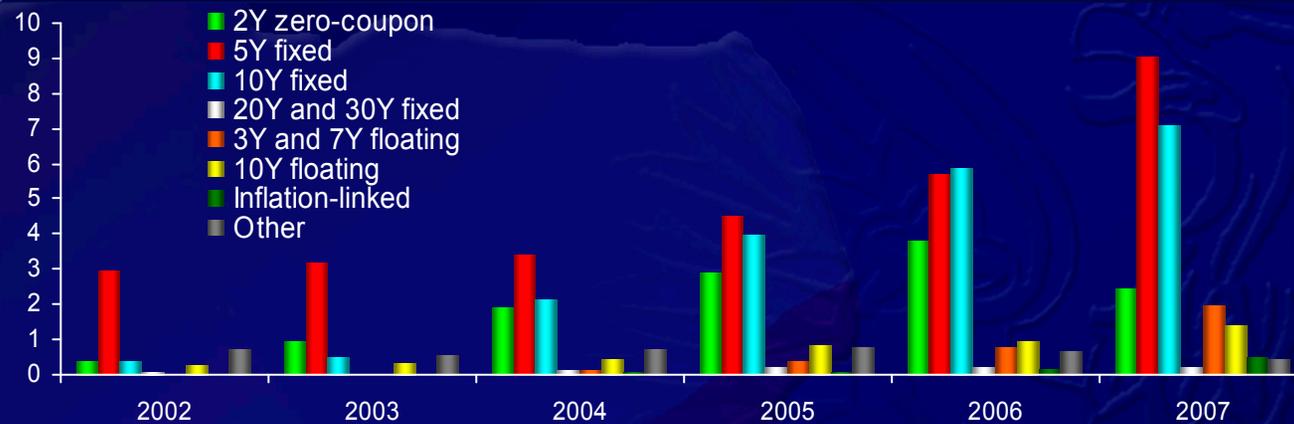


Source: Ministry of Finance

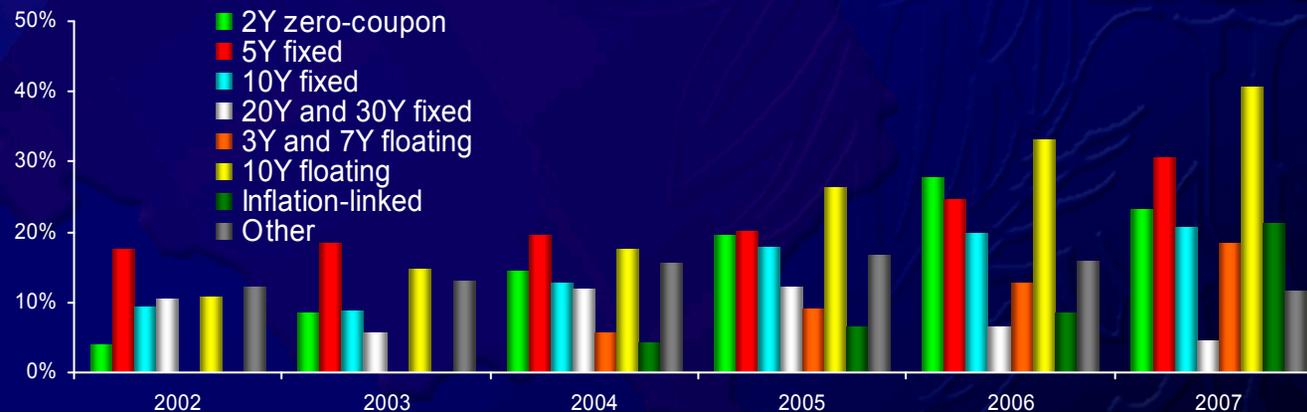


Open Pension Funds investment portfolio (2)

OPF's T bonds holdings by instrument (EUR bn)



OPF's T bonds holdings by instrument (% share)



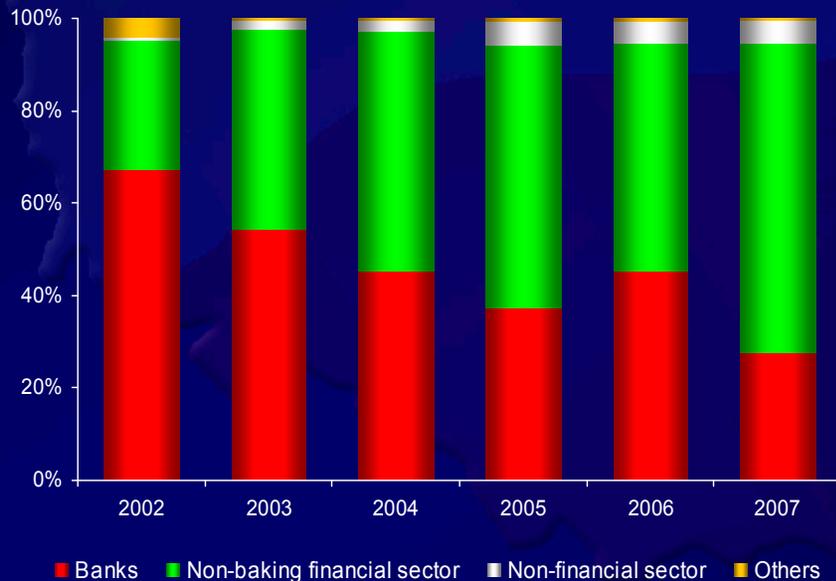
Source: Ministry of Finance



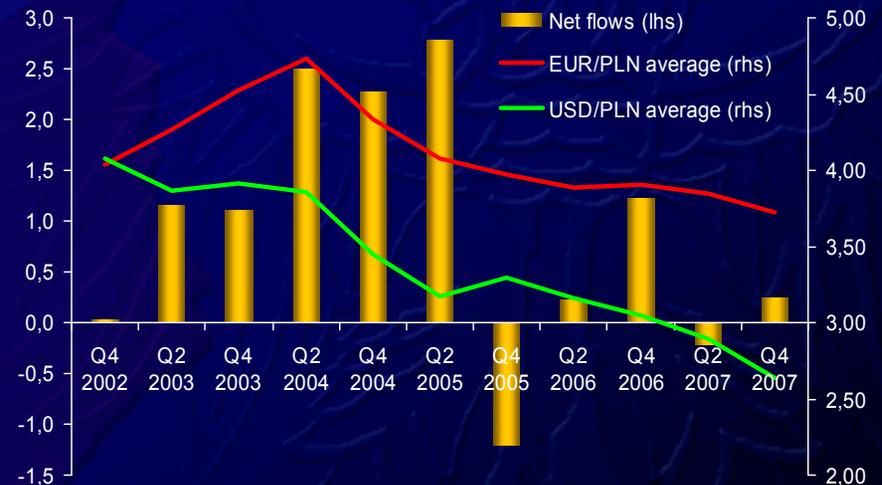
Foreign investors

- Since entering the EU over 20% share in domestic outstanding Treasury securities
- Dominant share in fixed long-term and index-linked
- Support for development of the derivatives market (hedging the exchange rate risk)
- Institutional involvement on the Polish market (primary dealers, ownership of domestic financial institutions)

Holdings of foreign investors by sector (% share)



Net flows of foreign investors (EUR bn) vs. PLN exchange rate

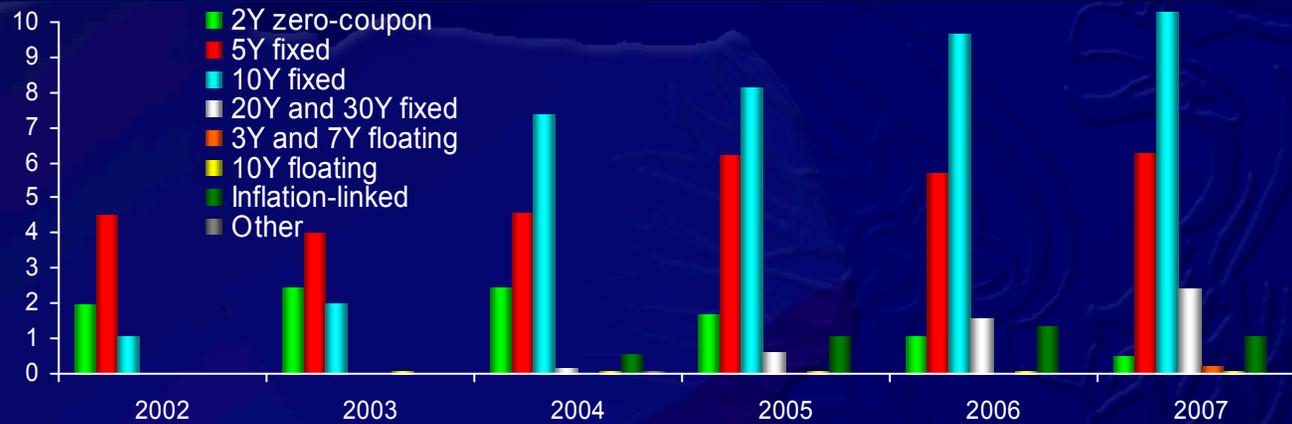


Source: Ministry of Finance

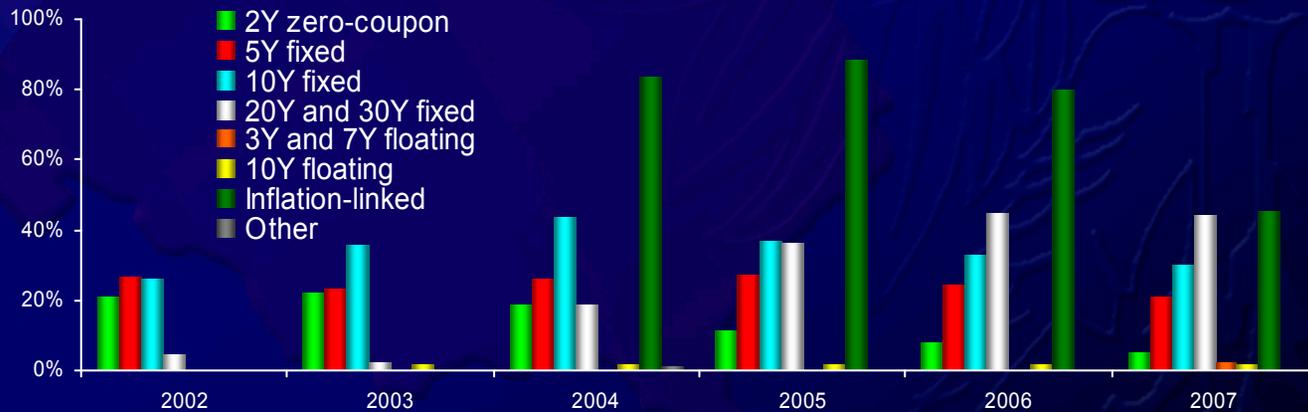


Foreign investors by market segments

Foreign investors T bonds holdings by instrument (EUR bn)



Foreign investors T bonds holdings by instrument (% share)



Source: Ministry of Finance



Domestic secondary market

- Trading concentrated on the OTC market
- Domestic secondary market – monthly average value of transactions (single counted):
 - ✓ 2006: PLN 568bn (EUR 146bn)
 - ✓ 2007: PLN 621bn (EUR 164bn)
 - ✓ I-III 2008: PLN 589bn (EUR 165bn)



Source: Ministry of Finance

Benchmark bonds



OPF and foreign investors share in outstanding benchmark bonds (February 2008)

Benchmark issue	Maturity / Type	Outstanding amount (PLN bn)	Held by OPF	Held by foreign investors
DS0509	2009 / fixed	28,6	25,7%	26,3%
PS0310	2010 / fixed	29,6	34,3%	20,6%
PS0511	2011 / fixed	23,6	31,2%	20,9%
DS1013	2013 / fixed	22,6	18,8%	35,4%
DS1015	2015 / fixed	24,6	18,6%	32,6%
DS1017	2017 / fixed	17,3	18,8%	31,5%
WS0922	2022 / fixed	20,6	8,1%	37,5%
WS0437	2037 / fixed	1,0	3,0%	38,0%
WZ0911	2011 / floating	19,7	13,4%	4,0%
WZ0118	2018 / floating	19,4	25,8%	0,1%
IZ0816	2016 / CPI linked	9,3	26,0%	36,3%



Source: Ministry of Finance

Summary



- Substantial role of Open Pension Funds and foreign investors in the development of the Treasury Securities market
 - Deepening the market and improving its liquidity
 - Lengthening the yield curve
 - Foreign investors influence on the development of the derivatives market and institutional involvement on the Polish market

