# Updating the Guidelines for Public Debt Management
## Progress Report
## October 2013

*This progress report summarizes the initial suggestions by the Working Group on updates to the Guidelines. The main areas covered in the initial proposals of the five subgroups include: (i) transparency and communication; (ii) institutional framework; (iii) debt management strategy; (iv) risk management framework; and (v) development and maintenance of an efficient market for government securities. These preliminary suggestions will be discussed with IMF-World Bank members during the 2nd Consultative Meeting on October 15, 2013.*

## I. Main Initial Suggestions

### Transparency and communication

**In addition to the transparency of objectives, the subgroup working in this section suggested that debt managers also publicly disclose their desired debt structure over the medium- to long-term,** taking into account associated costs and risks, as well as annual targets. The public should also be informed about the debt management framework, including the macroeconomic setting, market conditions, and cost-risk characteristics of the existing debt portfolio. For those debt managers who adopt quantitative targets a description of the borrowing plan with debt and risk targets is highly desirable.

**To guarantee transparency and efficient communication with investors and other stakeholders, the government should pay particular care to accountability,** presenting periodical results in light of the borrowing plan's strategies and targets. This would allow the public a better understanding of the debt management performance relative to the target. With regards to enhancing transparency of debt statistics, it is recommended that governments report the methods for calculating government debt figures, measures for roll-over risk, maturity structure, derivatives and explicit contingent liabilities. To facilitate cross country comparison by investors, countries should report information in a standardized format.[1]

**If debt management operations include derivatives, the subgroup suggested that statistics on the derivative portfolio be published at least annually and conform to standard accounting practices.** Derivative operations, as employed by some debt managers, can be a valuable tool to supplement debt management strategies. Accounting for these operations is crucial for strengthening confidence in the soundness of the sovereign's financial position, since their risk characteristics and cost structures of derivatives can be quite different from those of standard debt instruments. Key risk, cost, and valuation metrics of the derivative portfolio should be formulated according to recognized accounting practices and made public on a regular basis.

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[1] See the OECD *Report for raising, managing, and retiring public debt.*

**Institutional framework**

**If a government is forced to restructure its public debt in a time of crisis, the subgroup suggested that one tool that can help mitigate the risk of future litigation by a minority of bondholders is collective action clauses (CACs).** The design and incorporation of these clauses in bond documentation could allow a super-majority to bind all bondholders to the financial terms of a restructuring and to limit the ability of a minority of bondholders to disrupt the restructuring process by enforcing their claims after a default.

**Debt management strategy**

**The subgroup suggested including risks arising from the use of derivatives.** In particular, it suggested cautioning governments on potential consequences of derivative structures and the legal basis (e.g., in the case of a downgrade) and highlighted the importance of managing counterparty/credit risk involved when transacting in derivatives. DMO collateralization policies and practices are being reviewed in many countries, while clearance of derivative trades through central counterparties (CCPs) is currently discussed in many countries.

**Minimum requirements to the credit ratings of counterparties in derivatives transactions and in investments in financial assets (e.g., in relation to cash buffers) is also discussed.** In Europe, financial sector regulators aim at reducing the demand for credit rating agency (CRA) services stemming from regulatory requirements. The central issue is whether governments have the resources and instruments to evaluate the credit risk of all counterparties on an ongoing basis and what practical advice the *Guidelines* can give if this is not the case.

**The subgroup also suggested changes related to the asset and liability management (ALM) framework** to address current practical issues and to provide suggestions on implementing such a framework. It is suggested to include limitations of ALM reflecting first that it is difficult to define clearly the relevant balance sheet of the government, as it is far more complex and diversified than that of a private company, and second, that assets are not always easy to identify, neither is revenues dependence on financial variables. Consequently, applying a partially integrated ALM or a liability-only approach could be considered a second-best solution in the *Guidelines*.

**Risk management framework**

**In view of tail risks observed in recent crises, the subgroup reviewed the risk modeling framework stated in the *Guidelines* and suggested to stress the importance of considering extreme case scenarios** in order to better assess risks of the debt portfolio.

**The subgroup also suggested adding the importance of monitoring contingent liabilities from sub-federal units and state-owned companies,** as well as the potential liabilities arising from commercial arrears reflecting especially experiences from some European countries. As contingent liabilities, public-private partnerships (PPPs) have arisen in recent years from project financing. The subgroup felt that governments should establish sound legal and organizational frameworks for them because of their complex structures and build technical capacity.

**Development and maintenance of an efficient market for government securities**

**The subgroup suggested that debt managers balance the gains of mitigating rollover risk against the interest rate risk associated with the re-fixing of floaters,** including the unreliability of domestic references. Attempting to extend the yield curve quickly beyond a certain point has proven to be very challenging for many countries. Some emerging countries have tried to address this problem by issuing large amounts of long-term inflation-index debt and floating-rate debt, since such debt may be attractive to investors in countries where government indebtedness is high and the credibility of the monetary authority is low. Similar considerations should be made when issuing inflation-linked issues, especially in countries where the credibility of monetary authorities is low.

**The subgroup suggested the inclusion of public education aimed at informing the investing public** in simplified language about the relevant instrument and their inherent risks. This may be reinforced by providing such information in the term sheet or information memorandum used to promote the instrument.

## II. NEXT STEPS

**The five subgroups that comprise the Working Group will continue to refine the notes on the different sections of the *Guidelines*.** Each note will include suggested updates/additions and propose changes to the respective sections, taking into account additional comments received at the Consultative Meeting. The Chair will consolidate these and the Secretariat will circulate the consolidated draft notes to both IMF and World Bank memberships for comments. It will then incorporate comments from the memberships and prepare a draft board paper with proposed updates to the *Guidelines* to be submitted to their respective Boards in the first quarter of 2014.