# THE ROLE OF PUBLIC DEBT MANAGERS IN CONTINGENT LIABILITY MANAGEMENT

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# Different sources, different magnitudes

natural disasters

Government credit guarantees

financial sector implicit contingent liabilities

PPP guarantees

non-guaranteed borrowing by public sector

Government sponsored insurance

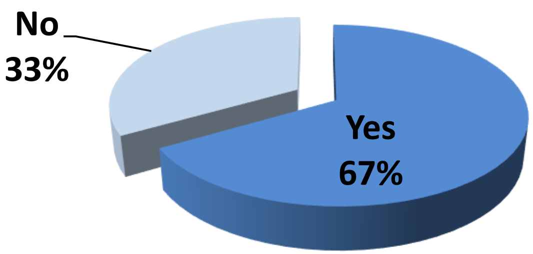
# Scope of work

Main sources of «explicit» contingent liabilities

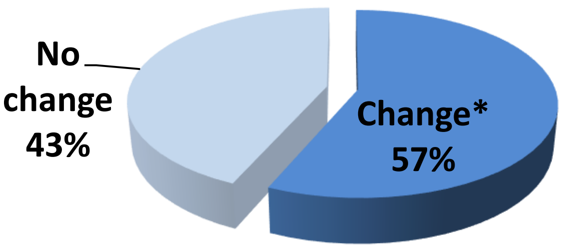
- Government credit guarantees
  - debt service guarantees provided to public and private institutions
  - program loan guarantees (e.g. student, housing, SME loan guarantees, export credit guarantees)
  - government guaranteed bonds provided to banks, etc.
- Contingent liabilities arising from PPPs
  - revenue guarantees
  - termination payment commitments
  - debt assumption commitments
  - direct credit guarantees extended to the project companies
- Government sponsored insurance programs
  - government funded deposit insurance programs
  - other insurance programs supported by governments

# OECD Survey – summary results

Do you have any role in the management of contingent liabilities?




Has there been any change in your role after the global financial crisis?




| Is the DMO responsible in the management of the following contingent liabilities at any level? | Yes | No | TOTAL |
|---|---|---|---|
| Government credit guarantees | 12 | 10 | 22 |
| Program loan guarantees | 3 | 16 | 19 |
| Government insurance schemes | 2 | 17 | 19 |
| PPP guarantees | 2 | 17 | 19 |
| Other (s) | 2 | 13 | 15 |

# OECD Survey – summary results

| | Do you calculate the expected cost? | | | Monitor regularly? | | | Report regularly and publicly? | | |
|---|---|---|---|---|---|---|---|---|---|
| | Yes | No | TOTAL | Yes | No | TOTAL | Yes | No | TOTAL |
| Credit guarantees | 11 | 8 | 19 | 17 | 1 | 18 | 17 | 1 | 18 |
| Program loan guarantees | 6 | 3 | 9 | 6 | 3 | 9 | 7 | 2 | 9 |
| Government insurance schemes | 3 | 5 | 8 | 5 | 3 | 8 | 4 | 4 | 8 |
| PPP guarantees | 5 | 2 | 7 | 5 | 2 | 7 | 4 | 3 | 7 |
| Other (s) | 3 | 3 | 6 | 4 | 2 | 6 | 4 | 2 | 6 |

# Recommendations and policy conclusions of the paper

## Government credit guarantees

- Cost and risk analysis at the application stage is key for informed decision-making
- In case of program loan guarantees – such as export credits, SME guarantees, student and housing guarantees – clearly setting the rules and objectives of the programs is essential because of the large number of application
- Fees corresponding to at least the expected cost of each guarantee should be charged
- The terms of the credit guarantee contracts should be drafted in a way that the government's risk exposure is defined and limited in time and scope,
- Ceilings for guarantees helps promote fiscal discipline, limit the fiscal risk exposure and direct the policy-makers towards prioritization among the applications,
- Contingency reserve funds increase government's ability to cover possible future losses and monitor its financial position vis-à-vis the existing guarantees
- Both quantitative and qualitative information on credit guarantees should be disclosed to give a complete picture of the government's total financial position

# Recommendations and policy conclusions of the paper

## Contingent Liabilities arising from the PPPs

- PPP regulatory and management frameworks should be strengthened
- A central government unit should analyze the costs and risks of the suggested PPP guarantees in contracts for informed-decision making
- Guarantee valuation is key because guarantees change the risk sharing between the public and private partner
- Central monitoring of PPP guarantees for fiscal and debt sustainability is recommended
- The DMOs can work together with the central budget authority in data consolidation, forecasting and reporting practices on the PPP contingent liabilities; or include this information in their debt reporting.

# Recommendations and policy conclusions of the paper

## Government sponsored insurance programs

- Ensuring stability in the financial markets is crucial for public debt managers  and a credible and well managed deposit insurance framework would contribute to this end.
- Regular coordination with the deposit and other insurance managers  is important thereby public debt managers can be informed about the fiscal risks arising from the financial sector.
- Clear legislative frameworks defining the scope and nature of government's role within the insurance programs are recommended.
- Public debt managers are recommended to be well informed of the contingent liabilities under the government sponsored insurance programs.
- Analyses involving finance ministries and debt management offices are highly recommended before enrolling governments in the insurance programs with direct and contingent fiscal commitments.

# Task force countries

**7 detailed case studies**

Denmark

Iceland

Sweden

Turkey

Brazil

South Africa

Mexico

# Contingent liability management

## Application

- Criteria setting
- The authority /institution to apply (centralized vs. decentralized structures)

## Approval

- Approving body
- Political decision
- Informed decision making
- Ensuring neutrality/ comparison among options

## Monitoring

- Centralization
- Portfolio risk management
- Audit
- Risk mitigation tools
- Reporting

## Assessment

- Credit risk analysis (modeling)
- Cost analysis
- Benefit analysis
- Administrative costs
- Limit/ceiling
- Ex ante valuation
- Pricing

## Recording

- When to record The issuance vs. realization of the guarantee
- Central registry
- Budgeting/provisioning
- Statistical treatment

# Examples from task force countries - Turkey

| | |
|---|---|
| **Application** | • Treasury guarantees for external financing only<br>• Centralized issuance for Treasury guarantees but decentralized structure for the PPPs.<br>• SOEs, Municipalities and their affiliates, public banks are eligible<br>• No-overdue debt to treasury condition |
| **Assessment** | • Credit risk analysis by the mid-office assigning a credit rating to the applicant<br>• The model calculates the expected loss, pricing is also based on the model calculations<br>• Application is assessed against the ceiling |
| **Approval** | • Minister approves the application<br>• Political decision<br>• Informed decision making |
| **Recording** | • Guarantee is recorded in the information system by the back office<br>• No budgeting ex ante, below the line (memorandum) item<br>• Risk account<br>• Statistically, no effect on central government debt unless the guarantee is called |
| **Monitoring** | • Centralized monitoring for Treasury guarantees not for other types<br>• Portfolio risk management conducted by the treasury mid office<br>• Audit<br>• Risk mitigation tools<br>• Risk account<br>• Reporting |

# Examples from task force countries - Sweden

| | |
|---|---|
| **Application** | • Main criteria to apply – to be financially viable<br>• Decentralized issuance, guarantee issuing institution is authorized by the parliament<br>• Well established guidelines for the issuers |
| **Assessment** | • Credit risk analysis conducted by specialists in issuing authority<br>• Specific limits might be assigned to agencies having the issuance power<br>• Ex ante valuation (expected loss is calculated)<br>• Pricing (covering for costs, state aid rules apply) |
| **Approval** | • Parliamentary approval<br>• The approval process is transparent<br>• Informed decision making<br>• Neutrality/ comparison among options is ensured |
| **Recording** | • Budgeting for subsidized amounts<br>• Statistical treatment: net of inflows/outlays increases the central government debt<br>• High level of transparency promoting sound risk management |
| **Monitoring** | • Centralized monitoring and reporting role of the SNDO<br>• Each responsible authority also monitors<br>• Notional reserve account<br>• Annual accumulation of guarantees is reported to the parliament |

# Examples from task force countries - Brazil

| | |
|---|---|
| **Application** | • Eligible institutions: SOEs and sub-national entities<br>• Counter-guarantee is a precondition to apply<br>• Application is made either to debt management department or states and municipalities department |
| **Assessment** | • No fee is charged<br>• Limit: Federal Government guarantees outstanding cannot exceed 60 % of annual revenues<br>• Credit rating methodology is used by the national treasury for the sub-national entities |
| **Approval** | • Decentralized issuance by the entities of Federal Government<br>• Political decision<br>• Informed decision making<br>• Ensuring neutrality/ comparison among options |
| **Recording** | • No budgeting ex ante<br>• Recordings are done in nominal amounts/stock outstanding is monitored |
| **Monitoring** | • Debt management department at the Treasury centrally monitors<br>• Reporting to the parliament |

# Key messages from the country practices

- No single structure of management
- Ex ante assessment of costs to ensure informed decision making
- Pricing reflecting costs
- Portfolio risk management(centralized to the extent possible)
- Close monitoring at the central government level
- Transparency

# Main challenges

- Managing uncertain commitments is a challenge in itself
- The issuance decisions are political processes
- Reporting and accounting for CLs is complex and international standards and implementations are still away from each other worldwide
- Learning by doing wave in PPP area raises concerns for fiscal sustainability
- Capacity building in mid offices of DMOs or within finance ministries is necessary

Thank you for your attention…

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