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Considerations upon the Evolution of Yearly Costs Afferent to the Instruments of Governmental Public Debt in Romania

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Abstract

The hereby paper displays a research upon an important element of public debt, namely the manner yearly costs afferent to the instruments of governmental public debt developed during the period 2001 – 2010. We attempt at showing the influence such costs have upon the management strategy of public debt under nowadays economic circumstances, influenced by the tendencies of worldwide economic crisis.

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1. Introduction

In the present day economic context, public debt has a special impact upon national economy requiring a complex analysis that demands the carrying out of a correlation among public deficit, governmental expenditures, fiscal incomes and public debt. Consequently, as long as growing budget deficits are being registered, the level of public debt increases and the costs afferent to the instruments of governmental public debt are difficultly covered.

The tremendous negative effect of an important public debt is the substitution of private capital by public debt. On a long term, capital replacement has had a negative impact on economic growth and the living standard of the citizens. The crises have determined shocks on the financial markets that affected all types of

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assets, including the instruments of public debt (Piga, 2001).

With each new financial crisis, the management of public debt should develop new mechanisms whose goal is the re-configuring of the instruments of public debt, the monitoring of the external debt of the private field, the integration of the strategies regarding public debt at a macroeconomic level and the integration of management techniques that could anticipate the inherent risks deriving from the process of public debt management (Sturzenegger and Zettelmeyer, 2007).

Public debt should be correctly structured as regards interest's rates, the terms of payment and the currency according to which loans have been contracted. A poor structuring of such elements as well as the existence of a high level of the guarantees given by the Government in favour of the loans contracted by public institutions or by private companies represent factors that have determined the starting or the spreading of economic crises (Dascalu, 2008).

Owing to the hereby scientific approach we have carried out an analysis of the manner the yearly costs afferent to the instruments of governmental public debt developed during the analyzed period; we have also questioned the tendencies displayed by the growth indices of public debt and its afferent costs. At the same time, our intention has been the emphasizing of the manners owing to which the costs afferent to the instruments of governmental public debt influence the strategy of managing public debt year by year.

2. Theoretical approaches regarding the instruments of governmental public debt

Debt instruments employed in order to administer governmental public debt may be emitted and/or employed only by the Ministry of Public Finances; they are denominated in Lei and/or currencies through accessing the internal and external financial markets.

We display below a series of instruments of governmental public debt which nevertheless are not confined to the following items:

- State titles launched on international markets as well as State titles launched on internal market, including population treasury certificates that are not redeemed in due term and are changed into deposit certificates;
- Loans from Romanian or foreign financial institutions;
- Loans from foreign governments or governmental agencies, international financial institutions or other international financial organisms;
- Temporary loans out of the availabilities belonging to the general current account of the State Treasury;
- Structured instruments, such as supplier credits;
- Financial leasing. Let's mention that according to the legal stipulations in force, external financial leasing contracts of central public institutions have been transferred from private debt to governmental public debt;
- Cash – management instruments (deposits acquiring, repo operations);
- State guaranty letters;
- Loans from the European Union given according to the Rules of the Council of the European Union no. 332/2002 regarding the foundation of an average-term mechanism of financial assistance for the balances of payments of the member-states;
- Private placements.

State titles represent financial instruments that certify public debt. State titles include: bonds, treasury certificates, obligations, including population treasury certificates that are not redeemed in due term and are changed into deposit certificates or other financial instruments which represent State loans in the national currency or in foreign currencies. State titles can be short, average or long term emitted. Their emission is either materialized or de-materialized; there are also nominative or bearer State titles as well as negotiable or non-negotiable ones. The term of payment of *short term State titles* is up to one year and they include bonds and treasury certificates. *Average or long term State titles* include: State obligations whose term of payment is higher than one year and maximum five years from their emission, either interest bearer or discount titles.

Interest State titles are those State titles displaying a nominal value according to which a settled interest is paid on specified terms. *Discount State titles* are those State titles with no interest coupon sold at a value that is smaller than their nominal value. *Dematerialized State titles* are those State titles in case of which the emission, probation, and transmitting of incorporated rights is displayed through registering within the account registering system. These instruments can be employed by their owners as loan guarantees. *Materialized State titles* are those State titles possessing a physical form - an imprinted document – that includes compulsory mentions regarding the emitter, their nominal value, interest's rate or discount rate, the term of payment, the manner of transmitting as well as other elements specific for each category of titles.

As regards the increase of the attractiveness of State titles, let's mention that it can be provided through offering interest rates that are higher than the interest rate of bank deposits or of other saving instruments on the private market. *Interest rate* represents the interest expressed according to percents per year and paid for the capital of an interest bearer loan or State title. Let's also mention that the instruments of public debt represent, in fact, alternative means of getting financial funds (Holt, 2009).

The Ministry of Public Finances, during the process of managing the risks associated with governmental public debt, is authorized to exert the following operations, yet without confining to them:

- Currency swaps, futures contracts, options and other operations specific for the management of currency risk;
- Forward contracts, swaps on interest rate, options and other operations specific for the management of interest risk;
- Administration operations of the service of governmental public debt through refinancing due debt and/or anticipated repayment of an existing debt which is not due, including the change of the terms afferent to the existing debt owing to anticipated redeem operations of the State titles, owing to their turning into new State titles, and to turning certain instruments into other instruments of governmental public debt;
- Operations of administering the credit risk afferent to the portfolio of governmental public debt through giving/receiving guarantees collateral to the other parties with which contracts/agreements are concluded during the process of administering governmental public debt.

The contracting of a new debt with a view of paying a financial obligation representing a due governmental public debt is defined as *refinancing governmental public debt*. The anticipated payment of an obligation representing a governmental public debt is the payment/anticipated redeem that can be carried out either as a result of the creditors exerting such an option or as a result of the Ministry of Public Finances exerting the option in order to efficiently administer governmental public debt and the service of governmental public debt (http://discutii.mfinante.ro/static/10/Mfp/Trezorerie/CadruLegal/HG1470_MO870.pdf)

The Ministry of Public Finances can conclude contracts/agreements with financial institutions that do not involve the financial obligations of the contracting parties but which stipulate the general terms according to which the operations between the parties are going to develop in order to implement the operations of administering the risks associated with the governmental public debt operations. Such agreements define and regulate the mutual compensation operations that involve the compensation – until getting a net amount – converted into a sole currency of the values of certain payment rights or obligations occurring between the Ministry of Public Finances and the financial institutions with whom they conclude agreements of administering governmental public debt and/or of administering the risks afferent to governmental public debt obligations.

4. Findings on the evolution of annual costs for government public debt instruments

For the period studied, the financial effort representing interest payments and fees for government debt instruments was 15.74% of total government public debt service (39.122, 5 million Lei).

Table 1. Evolution of annual costs for government public debt instruments between 2001 - 2010
- million Lei -

Year	Treasury Bills	Cash management	Liabilities	Euro-Liabilities	Financial Leasing	Loans from Financial Institutions	General Availability of Loans from the State Treasury Account	Total Annual Costs
2001	2.639,2	0,0	52,9	215,2	0,0	1.141,3	23,9	4.072,5
2002	1.593,2	0,0	124,9	527,8	0,0	1.238,5	143,0	3.627,4
2003	1.613,9	0,0	58,4	753,5	0,0	1.210,7	62,2	3.698,7
2004	684,1	0,0	338,6	870,9	0,0	1.235,1	65,5	3.194,2
2005	743,7	0,0	245,5	717,4	24,4	1.289,7	71,8	3.092,5
2006	45,2	0,6	330,6	576,3	18,1	1.399,1	85,2	2.455,1
2007	153,5	10,9	330,3	545,6	12,7	1.325,8	153,7	2.532,5
2008	212,6	64,2	889,2	642,1	4,8	1.393,2	265,3	3.471,4
2009	2.052,7	109,0	1.087,8	629,2	21,9	1.401,5	485,1	5.787,2
2010	2.342,4	153,7	1.386,4	1076,8	32,9	1.597,3	601,5	7.191,0
Total of Costs for Each Type of Instrument	12.080,5	338,4	4.844,6	6.554,8	114,8	13.232,2	1.957,3	39.122,5

Source: Ministry of Finance

Within the time allowed for the Case study, it is noted that annual costs for government public debt instruments had a fluctuating dynamics. If in 2001 they amounted to 4.072,5 million Lei in 2006 they reached a minimum level of 2.455,1 million Lei, and in 2010 they reached the highest level, 7.191,0 million Lei.

As seen from the data presented in Table 1, from the total cost of public debt instruments, the fastest development have experienced costs associated with loans from the general account availability of the State Treasury, from 23.9 million in 2001, they came to 605.1 million Lei in 2010, the bonds from 52.9 million Lei in 2001 reached 1386.4 million Lei in 2010 and the Eurobonds from 215.2 million Lei in 2001 reached 1076.8 million Lei in 2010.

The cost of debt contracted in 2010, by issuing state bonds to finance the domestic budget deficit and for public debt refinancing, was reflected in the indicator GDP share of interest payments (1.4% of GDP) in increase compared to the year 2009. Important to note is that the external financial package was contracted on favorable interest terms, respectively 3.375% and 2.375% for the second and third installments of the loan from the EC, and 2.25% for half of the installments 3 and 4 of the IMF loan. (Guvernul României, Programul de convergență 2011-2014). For 2011 the annual costs associated with the evolution of government debt instruments has remained at the level of those from 2010.

Table 2. Growth indices of public debt and of its cost corresponding to period 2001 – 2010

Year	Growth index of public debt * (%)	Increase index of public debt costs * (%)
2001	133,7	110,3
2002	129,7	89,1
2003	117,1	102,0
2004	108,7	86,4
2005	105,7	96,8
2006	107,3	79,39
2007	130,0	103,2
2008	133,4	137,1
2009	134,2	166,7
2010	132,0	124,3

* It is calculated as the ratio between the level of each year and the previous year
Source: Ministry of Finance and own calculations

Analyzing the data presented in Table 2, we see that during 2001-2007, the growth rate of public debt was higher than the public debt costs increase index, and from 2008 to 2009 the growth rate of public debt costs exceeded that of public debt, then in 2010, the situation returned to the period from 2001 to 2007. The same situation is present and at the level of the year 2011. In conclusion, the faster growth of public debt costs has negative financial impact on the tax position of the state.

Conclusion

The hereby scientific approach relies on the analysis of the costs afferent to the instruments of governmental public debt and the growth indices of public debt and its afferent costs; the approach has shown that during the analyzed period they displayed a fluctuant evolution while the growth index of the costs afferent to public debt surpassed the growth index of public debt. All these facts have been determined by the implications of the worldwide financial crisis, beginning with 2008, which negatively influenced Romania's economic and financial activity.

Consequently, according to the legal regulations in Romania, the market terms and the macroeconomic background should undergo a process of transformation; at the same time, the objectives settled by the strategy of administering governmental public debt should also change targeting the following:

- The controlled growth and maintaining of governmental public debt at a sustainable level;
- The development of the market of State titles, assuming that most financing needs are going to be provided owing to negotiable debt, namely owing to State titles emitted on the capital internal and external markets;
- The decrease of long term governmental public debt costs in the context of an acceptable level of the risks afferent to the portfolio of governmental public debt;
- The providing of an adequate structure of public debt.

As a result, these objectives are going to be attained through employing the instruments specific to the administration of governmental public debt and liquidities in the context of the risks displayed, afferent to the portfolio of governmental public debt. The costs of governmental public debt should be considered according to the market financing terms at the moment of contracting/emitting and according to the goals targeting the limitation of the risks associated with the debt portfolio. Consequently, the cost afferent to high amounts of

State titles emitted in order to finance de budget deficit on the internal market and in order to refinance public debt is displayed by the index indicating the share of interest payments within GDP which increased during the analyzed period. The emissions of State titles on the internal market mainly concerned short term dues as a result of the increase of the degree of incertitude regarding the terms of the liquidities on monetary market, of that concerning economic growth and, implicitly, as a result of the evolution of the budget deficit and of inflationist expectations mainly concerning year 2010.

The ending of the package of multilateral financial assistance together with the worldwide trend of economic recovery and the measures taken by central banks have contributed to the increase of the investors' confidence materialized in the significant diminution of CDS quotations in case of Romania. Such positive reflects that are the result of the external financial package contracted have nevertheless determined an increase of the share of governmental public debt denominated in Euro; accordingly, exposure to certain market risks increased while the share of governmental public debt in Lei within the total amount of governmental public debt decreased; implicitly, the share of the governmental public debt in Euro within the total amount of governmental public debt increased.

Although, the use of the financing instruments – loans from the availabilities of the general current account of the State Treasury – displays the advantage of the temporary financing of the budget deficit at small costs, under 1%, on a short term, it also has important drawbacks: due to the fact that it is an atypical instrument, specific to our country, whose use depends on the level of the availabilities existing in the general current account of the State Treasury and due to the fact that it determines the growth of the exposure to refinancing and liquidity risk as well as of the risk of interest rate, it has a negative impact on the management of governmental public debt. Accordingly, the accumulation of budget deficits temporarily financed represent another element requiring that temporary financing is gradually refinanced through State titles during a long period of time in order to decrease the impact on the internal market and not to highly affect the cost of such refinancing. (http://discutii.mfinante.ro/static/10/Mfp/buletin/executii/strategia2011_2013.pdf).

We consequently recommend both the continuation of the implementation of public policies in Romania and of the main objectives regarding the management of governmental public debt during the next period so that the State's financial effort does not prevent the country from a durable economic growth. In conclusion, the efficiency costs of governmental debt instruments will be determined by the amount of the future and the dynamics of public debt in the current context of the economy, as well as by continuing fiscal policy started in 2009 that will generate economic growth, so that the public debt will reach sustainable levels and therefore the costs they will reduce considerably.

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