

## PDM NETWORK *Newsletter*

MAY 2009

Dear Partner, this *Newsletter* contains a list of the latest uploaded resources both in the documentation and in the event areas of the PDM Network website ([www.publicdebt.net.org](http://www.publicdebt.net.org)). The PDM Network has its main objective in the joint cooperation among its participants regarding the quantity and quality of information available on the website. So far, it is very appreciated a stronger collaboration in this field, **signalling to the Network Secretariat** any documents, news and events of interest at [publicdebt.net.dt@tesoro.it](mailto:publicdebt.net.dt@tesoro.it).

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### New Documents

#### PAPERS

##### ***Inflation Hedging for Long-Term Investors (2009)***

**Attie Alexander P. (IMF), Roache Shaun K. (IMF)**

Long-term investors face a common problem—how to maintain the purchasing power of their assets over time and achieve a level of real returns consistent with their investment objectives. While inflation-linked bonds and derivatives have been developed to hedge the effects of inflation, their limited supply and liquidity lead many investors to continue to rely on the indirect hedging properties of traditional asset classes.[...]

##### ***Global Currency Hedging (2009)***

**Campbell John Y. (Harvard University and NBER), Serfaty-de Medeiros Karine (OC&C Strategy Consultants), Viceira Luis M. (Harvard Business School and NBER)**

Over the period 1975 to 2005, the US dollar (particularly in relation to the Canadian dollar) and the euro and Swiss franc (particularly in the second half of the period) have moved against world equity markets. Thus these currencies should be attractive to risk minimizing global equity investors despite their low average returns. The risk-minimizing currency strategy for a global bond investor is close to a full currency hedge, with a modest long position in the US dollar. [...]

##### ***Domestic Public Debt in Developing Countries (2008)***

**Panizza Ugo (UNCTAD)**

Analysis of public debt in developing countries has traditionally focused on external debt. However, in recent years, several developing countries adopted aggressive policies aimed at retiring public external debt and substituting it with domestically issued debt. This paper discusses alternative definitions of external and domestic debt and then introduces a new dataset on domestic and external public debt. It uses this dataset to describe recent trends in the composition of public debt in developing countries and discusses the reasons for these trends. The paper also identifies possible challenges and opportunities arising from the

new debt management strategy adopted by several emerging and developing countries and points out that there are conceptual and practical issues with the traditional external/domestic debt dichotomy. [...]

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***The Composition of Public Debt in Developing and Emerging Countries (2008)***

Lima Lycia, Panizza Ugo (UNCTAD), Forslund Kristine (UNCTAD)

This paper uses a new dataset on the composition of public debt in developing and emerging Market countries to look at the correlation between country characteristics and domestic debt share. While the paper finds that most variables have the expected sign, it also finds that country characteristics cannot explain regional differences in the composition of public debt. Moreover, the paper finds a weak correlation between inflationary history and the composition of public debt. [...]

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***A Tale of Two Platforms: Dealer Intermediation in the European Sovereign Bond Market (2008)***

Dunne Peter (Queens University), Hau Harald (INSEAD and CEPR), Moore Michael (Queens University and Harvard University)

Interdealer trading in the European sovereign bond market is characterized by low spreads and high liquidity. This paper examines whether the dealer-customer segment of the market also benefits from low spreads. Customers are smaller banks and buy-side financial institutions who request quotes from primary dealers. They generally do not enjoy access to the interdealer trading platform. Surprisingly, the authors find that customer trades are on average competitively priced and often occur inside the interdealer spread. Moreover, higher market volatility increases interdealer spreads more than customer spreads. [...]

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***Sovereign Debt Restructuring: Search for an Optimum Voting Threshold (2008)***

Dey Joy (University of Delhi and University of Warwick)

Sovereigns have been defaulting on their debts over decades now. A sovereign debt default necessitates a restructuring of the debt instrument in order to reduce the size of the debt or lengthen the maturity period. One of the methods of debt restructuring is an 'exchange offer' where the old debt instrument, for example the bond, is exchanged for new debt instruments with altered terms and conditions, particularly the payment terms. Whereas some investors may agree to such restructuring and accept the exchange offer, others might have

different aspirations for their investments. A successful sovereign debt restructuring takes place when the debtor has acquired the consent of a pre-determined number of creditors, or the restructuring threshold. [...]

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***Development and Foreign Debt: The Stylized Facts 1970-2006 (2008)***

Paldam Martin (University of Aarhus)

The paper uses the data from the incomplete debt cycle for the LDC world from 1970 onwards to tell the typical story of debt. Two debt stories are contrasted: A good debt story: Here countries borrow and invest wisely, so that they grow more. A bad debt story: Here countries borrow when they are in crisis, and the debt grows and generates low growth in the next couple of decades. The analysis concentrates on two relations: (R1) the relation between borrowing and growth, and (R2) the relation between initial debt and growth. [...]

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***The Case for TIPS: An Examination of the Costs and Benefits (2008)***

Roush Jennifer (Federal Reserve Bank of New York), Dudley William (Federal Reserve Bank of New York), Steinberg Ezer Michelle (Federal Reserve Bank of New York)

Several studies have shown that, ex-post, the issuance of Treasury Inflation-Protected Securities (TIPS) has cost U.S. taxpayers money. The authors propose that evaluations of the TIPS program be more comprehensive and focus on the ex-ante costs of TIPS issuance versus nominal Treasury issuance and, especially when these costs are negligible, the more difficult-to-measure benefits of the program. [...]

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***The Sectorial Effects of Sovereign Default (2008)***

Lanau Sergi (Bank of England and Universitat Pompeu Fabra)

This paper explores the linkage between sovereign debt crises and manufacturing industry growth using a difference in difference methodology. Industries facing tough import competition perform relatively better after a sovereign default. Export oriented sectors grow more slowly around default times. These two facts are consistent with the theories stressing trade sanctions as the main cost of sovereign defaults. [...]

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***Domestic Bonds, Credit Derivatives, and the Next Transformation of Sovereign Debt (2008)***

Gelper Anna (Rutgers University School of Law)

Not long ago, financial markets in most poor and middle-income countries were shallow to nonexistent, and closed to foreigners. Governments often had to rely on risky borrowing abroad; the private sector had even fewer options. But between 1995 and 2005, domestic debt in the emerging markets grew from \$1 trillion to \$4 trillion. In Mexico, domestic debt went from just over 20% of the total government debt stock in 1995 to nearly 80% in 2007. [...]

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***Debt Sustainability under Catastrophic Risk: The Case for Government Budget Insurance (2008)***

**Borensztein Eduardo (IMF), Cavallo Eduardo (IDB), Valenzuela Patricio (IMF)**

Natural disasters are an important source of vulnerability in the Caribbean region. Despite being one of the more disaster-prone areas of the world, it has one of the lowest levels of insurance coverage. This paper examines the vulnerability of Belize's public finance to the occurrence of hurricanes and the potential impact of insurance instruments in reducing that vulnerability. The paper finds that catastrophic risk insurance significantly improves Belize's debt sustainability. [...]

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***Government Debt, Reputation and Creditors' Protections: The Tale of San Giorgio (2007)***

**Fратиanni Michele U. (Indiana University)**

San Giorgio (1407-1805) was a formal association aimed at protecting creditors' rights and reducing the risk of debt repudiation by the Republic of Genoa. The behavior of this institution is broadly consistent with debt models that predict lending if lenders can impose big penalties on debtors, and models in which lenders can differentiate between excusable and inexcusable defaults. San Giorgio shareholders enjoyed low credit risk but also lower returns on capital than those prevailing on comparable foreign assets for which creditors' protection mechanisms were lacking. [...]

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***Debt Maturity: Is Long-Term Debt Optimal? (2007)***

**Alfaro Laura (Harvard Business School), Kanczuk Fabio (Universidade de Sao Paulo)**

The authors model and calibrate the arguments in favor and against short-term and long-term debt. These arguments broadly include: maturity premium, sustainability, and service smoothing. It is used a dynamic equilibrium model with tax distortions and government outlays uncertainty, and model maturity as the fraction of debt that needs to be rolled over every period. In the

model, the benefits of defaulting are tempered by higher future interest rates. [...]

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***Nominal Versus Indexed Debt: A Quantitative Horse Race (2007)***

**Alfaro Laura (Harvard Business School), Kanczuk Fabio (Universidade de Sao Paulo)**

The main arguments in favor and against nominal and indexed debt are the incentive to default through inflation versus hedging against unforeseen shocks. The authors model and calibrate these arguments to assess their quantitative importance. They use a dynamic equilibrium model with tax distortion, government outlays uncertainty, and contingent-debt service. Their framework also recognizes that contingent debt can be associated with incentive problems and lack of commitment. Thus, the benefits of unexpected inflation are tempered by higher interest rates. [...]

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***What "Hides" Behind Sovereign Debt Ratings? (2007)***

**Afonso Antonio (ECB), Gomes Pedro (London School of Economics), Rother Philipp (ECB)**

In this paper the authors study the determinants of sovereign debt credit ratings using rating notations from the three main international rating agencies, for the period 1995-2005. They employ panel estimation and random effects ordered probit approaches to assess the explanatory power of several macroeconomic and public governance variables. Their results point to a good performance of the estimated models, across agencies and across the time dimension, as well as a good overall prediction power. [...]

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***A Compendium of Policy Instruments to Enhance Financial Stability and Debt Management in Emerging Market Economies (2007)***

**Mendoza Ronald U. (UNDP)**

Drawing on available theory and evidence, this paper attempts to identify some key factors contributing to international financial instability to develop a taxonomy of policy instruments to enhance financial stability and debt management in emerging market economies. The purpose is to relate each instrument to particular aspects of the broader policy challenge, thus clarifying differences and/or similarities among instruments and proposals. [...]

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***Regaining Market Access: What Determines the Duration of Exclusion? (2007)***

**Richmond Christine (UCLA), Dias Daniel A. (UCLA and CEMAPRE)**

This paper examines why some countries are able to regain access to international capital markets immediately after resolving a default, whereas other countries appear to be punished for longer periods. The authors first develop a methodology to determine when market access occurs after default settlement. Their main findings from examining the duration of exclusion from international capital markets between 1980-2005 in Latin American countries are the following: i) countries regain partial market access after 1.8 years on average (median of 1.0 year) while it takes 4.8 years on average (median of 4.0 years) to regain full market access; [...]

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***A Free Lunch for Emerging Markets: Removing International Financial Market Imperfections with Modern Finance Instruments (2007)***

**Bauer Christian (University of Bayreuth), Herz Bernhard (University of Bayreuth), Hoops Stefan (Lehman Brothers)**

Regulations and frictions of the market for emerging market bonds keep up the price of capital demanded by emerging countries. Instruments of modern finance, i.e. a pool of emerging market bonds refinanced via an enhanced Asset Backed Securities structure, can significantly reduce the interest payments. In an extensive simulation study based on empirical data, the cumulated interest savings for a horizon of 10 years amount to up to 44% of the credit sum. [...]

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***A Tale of Two Markets: Bond Market Development in East Asia and Latin America (2006)***

**Eichengreen Barry (University of California), Borensztein Eduardo (IDB), Panizza Ugo (IDB)**

This Occasional Paper provides a comparison of market developments in the East Asia and Latin America. It shows that Asian bond markets are larger and better capitalized and that the tenor of Asian bonds is longer, reflecting the region's high savings rates, history of stable policies and relatively strong investor protections. On the other hand, Latin American bond markets are more liquid by most measures, and they have had more success in attracting foreign investor participation. [...]

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***Do Sovereign Defaults Hurt Exporters? (2006)***

**Borensztein Eduardo (IDB), Panizza Ugo (IDB)**

This paper uses a difference-in-difference methodology similar to the one originally proposed by Rajan and Zingales (1998) to test

whether defaulting hurts the more export-oriented industries. [...]

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***The Elusive Costs of Sovereign Defaults (2006)***

**Panizza Ugo (IDB), Levy Yeyati Eduardo (Universidad Torcuato di Tella and WB)**

Few would dispute that sovereign defaults entail significant economic costs, including, most notably, important output losses. However, most of the evidence supporting this conventional wisdom, based on annual observations, suffers from serious measurement and identification problems. To address these drawbacks, the authors examine the impact of default on growth by looking at quarterly data for emerging economies. They find that, contrary to what is typically assumed, output contractions precede defaults. [...]

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***International Debt: The Constructive Implications of Some Moral Mathematics (2006)***

**Reddy Sanjay G.**

Present arrangements governing the accumulation and discharge of debt by states are difficult to justify fully on the basis of underlying normative considerations. States are different from individuals in important respects and the deontological justifications that explain why individuals have a strong burden to abide by promises to repay do not straightforwardly apply to countries. [...]

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**OTHER WEB RESOURCES**

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***Towards a Common European T-Bill (2009)***

**EPDA**

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***Website of the Inter-Agency Group on Economic and Financial Statistics (2009)***

**BIS, ECB, Eurostat, IMF, OECD, UN and the World Bank**

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***Financial Market Trends (2009)***  
from OECD website

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***IMF Work Program (2009)***  
from IMF website

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***Boring Bonds? (2009)***  
from IndexUniverse website

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## NETWORK NEWS

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### **European Primary Dealers Association (EPDA) website**

The NEW website  
<http://epda.sifma.org/>

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### **Audit of Public Debt: UNITAR Lessons**

From UNITAR website  
<http://www2.unitar.org/dfm/dfmelearning/Courses/APD/APDCourseInfo2.htm>

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### **Debt Watch - Caribbean Newsletter**

From Michele Robinson website  
[http://www.michelerobinson.net/debt\\_watch](http://www.michelerobinson.net/debt_watch)

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**Annual Reports & Guidelines: please go to the "Information Corner" on [www.publicdebtnet.org](http://www.publicdebtnet.org)**

## Events, Courses

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### UPCOMING

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#### NEW

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8 June 2009 - 8 June 2009; New York, USA  
**SIFMA's Municipal Bond Summit**

9 June 2009 - 11 June 2009; Manila, Philippines  
**Understanding Global Financial Markets and Products**

22 June 2009 - 26 June 2009; Bamako, Mali  
**French Regional Domestic Debt Workshop**

29 June 2009 - 24 July 2009; Online/Internet-based  
**Fundamentals of Risk Management**

29 June 2009 - 31 July 2009; Online/Internet-based  
**Fundamentals of the Derivative Markets**

6 July 2009 - 17 July 2009; Freetown, Sierra Leone  
**Analysis for Sierra Leone**

7 September 2009 - 15 October 2009; Online/Internet-based  
**Advance Risk Management**

7 September 2009 - 16 October 2009; Online/Internet-based  
**Legal Aspects of Public Debt Management**

14 September 2009 - 30 October 2009; Online Course

### **Effective Public Debt Management**

14 September 2009 - 30 October 2009; Online/Internet-based

#### **Debt Rescheduling with the Paris Club**

12 October 2009 - 13 November 2009; Online/Internet-based

#### **Fundamentals of the Bond Market**

26 October 2009 - 27 November 2009; Online/Internet-based

#### **Audit of Public Debt**

30 October 2009; Washington, D.C., USA  
**Estrategias para el manejo de la Deuda Pública durante la Crisis**

2 November 2009 - 11 December 2009; Online/Internet-based

#### **Basic Course on Public Debt Management**

6 November 2009; Brussels, Belgium  
**EPDA's 4th Annual European Government Bond Conference**

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### PREVIOUSLY SIGNALLED

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22 April 2009 - 2 July 2009; different places  
**ISDA Conference**

May/June 2009 - Paris, France  
**Designing Government Debt Management Strategies**

May/June 2009 - Paris, France

**Implementing a Debt Management Strategy**

3 June 2009 - 5 June 2009; Montreux Palace Hotel, Montreux, Switzerland

**The International Capital Market Association Annual General Meeting and Conference**

22 June 2009 - 26 June 2009; Lagos, Nigeria

**Seminars on Public Financial Management for Effective Aid Management for Policymakers and Parliamentarians**

24 June 2009 - 26 June 2009; Cape Town, S. A.

**3rd OECD Regional Workshop on African Debt Management and Bond Markets**

29 June 2009 - 8 July 2009; Kigali, Rwanda

**Training of Trainers in the World Bank / IMF Debt Medium Term Debt Strategy (MTDS)**

20 July 2009 - 30 July 2009; Banjul, The Gambia

**Post-HIPC Debt Sustainability Analysis for The Gambia**

20 July 2009 - 31 July 2009; Worthing, UK

**New Challenges in Debt Management**

20 July 2009 - 5 August 2009; Maseru, Lesotho

**Application of Assets/Liabilities Management (ALM) framework for Debt and Reserves Management**

3 August 2009 - 7 August 2009; Lagos, Nigeria

**Comprehensive CS-DRMS 2000 + User Training Featuring latest version 1.3 & Security Auction System**

7 September 2009 - 18 September 2009; Worthing, UK

**Managing Risk and Developing a Debt Strategy**

10 September 2009 - 11 September 2009; Basel, Switzerland

**Monetary Policy and Financial Stability**

5 October 2009 - 19 October 2009; Worthing, UK

**Advanced CS-DRMS User Training**

12 October 2009 - 16 October 2009; Lagos, Nigeria

**Debt Recording for Sub-national Debt Management in Nigeria**

9 November 2009 - 18 November 2009; Lusaka, Zambia

**Regional Dissemination and Training on UNCTAD - DMFAS 6.0**

9 November 2009 - 11 November 2009; Palais des Nations, Geneva

**Seventh International Debt Management Conference**

16 November 2009 - 17 November 2009; Washington DC

**Joint BIS/ECB/ World Bank Public Investors Conference 2009**

30 November 2009 - 11 December 2009; Worthing, UK

**Effective Domestic Debt Management**

14 December 2009 - 18 December 2009; Joint Vienna Institute

**Workshop on Debt Management Performance Assessment Tool and Debt Sustainability Framework**

**The PDM Secretariat is grateful to Emmanuelle Roux (SIFMA), Enrique Cosio-Pascal (consultant, Public Debt Finance) and Michele Robinson (consultant, Debt Watch - Caribbean) for their resource contribution.**

## Communication Corner

### e-LEARNIG COURSE MATERIALS

The PDM network website will shortly host material from e-learning course "Audit of Public Debt" organized by UNITAR thanks to Enrique Cosio-Pascal contribution. This course will be downloadable from the learning area in the "Information corner" and is oriented toward those auditors that would be participating to internal or external audit of public debt management.

### NEW WEBSITE AREA

The Network's website home page (public version) includes a *new area* called "**Information corner**". In this section, all Partners and other internet users can find organised information on specific topics of public debt management: Statistics, Bond Auctions, DMOs Programmes and Reports, Learning area, Monthly Newsletters.

## E-MAIL NOTIFICATION SERVICE FOR PARTNERS

We are glad to remind that a **notification service** is provided on the Network website for Partners. By this service, they will receive an e-mail when a new document or event is uploaded onto the website in the category of their choice (i.e. primary market, secondary market, or other categories or macro-categories). To activate the service Partners should access in the private area of the website and choose the "GO" button in the "Mailing List" box. They can click on the categories they are interested in and, after clicking again on "subscribe" they will receive an email whenever a new document is uploaded in the preferred category. For any assistance contact the PDM Secretariat at [Publicdebtnet.dt@tesoro.it](mailto:Publicdebtnet.dt@tesoro.it)

## Participating Institutions in PDM Network

**OECD:** Australian OFM, Austrian DMA, Belgian DMA, Belgian Central Bank, Canadian Foreign Affairs and International Trade, Czech Central Bank, Czech MoF, Danish DMO, Danish Central Bank, Dutch Central Bank, Dutch DMA, Dutch MoF, Finnish Treasury, Finnish MoF, French Central Bank, French DMA, French MoF, German Central Bank, German MoF, German FA, Greek DMA, Greek MoF, Hungarian DMA, Hungarian MoF, Icelandic DMA, Irish NTMA, Irish MoF, Italian Central Bank, Italian MoF, Italian Development Co-operation Office, Japanese MoF, Japanese Central Bank, Luxembourg MoF, Mexican MoF, New Zealander DMO, Norwegian MoF, Polish MoF, Polish Central Bank, Portuguese Central Bank, Portuguese DMA, Slovak MoF, Slovak DMA, Spanish Central Bank, Spanish MoF, Swedish DMO, Swedish MoF, Swiss State Secretary for Economic Affairs SECO, Turkish Treasury, US GAO, , UK Central Bank, UK DMO, UK Treasury.

**Non OECD:** Albanian MoF, Angolan National Bank, Brazilian MoF, Brazilian Central Bank, Bulgarian MoF, Chilean Central Bank, Chinese MoF, Colombian MHCP, Cyprian Central Bank, Cyprian MoF, Dubai DMO, Dubai Government, Egyptian MoF, Estonian MoF, Ethiopian MoF, Ghanaian Central Bank, Ghanaian MoF, Hong Kong Monetary Auth., Indian Reserve Bank, Indian NIPF, Israeli MoF, Israeli Central Bank, Kenyan MoF, Latvian DMO, Lebanese MoF, Lesotho MoF, Lithuanian MoF, Macedonian MoF, Malawian Reserve Bank, Maltese Treasury, Maltese Central Bank, Moldovan MoF, Moroccan MoF, Nigerian DMO, Pakistani MoF, Papua New Guinean Treasury, Romanian MoF, Romanian Central Bank, Rwandan MoF, Singaporean MoF, Slovenian MoF, Solomon Islands MoF, South African National Treasury, Sri Lanka Central Bank, Thai MoF, Ugandan Central Bank, Uruguayan MoF.

**Multilateral Institutions:** OECD, European Commission, ADB, African Development Bank Group, Asian Development Bank Institute, Commonwealth Secretariat, European Central Bank, European Bank EBRD, Inter-American Development Bank, IFC, International Monetary Fund, MEFMI, WAIFEM, World Bank, UNCTAD.

**Universities:** University of Brussels, University of Cambridge, University of California, University of Milan, University of Molise, University of Padua, University of Rome "La Sapienza", CRIEP (Italy), University of Rome "Tor Vergata".

**Others :** Center of Excellence in Finance, Devfin Advisers AB, Finance for Development-FMO, ICMA, ISEDA, KFW Bankengruppe, Japan Bank for International Cooperation, Michele Robinson Consult, Oxford Policy Management, Pragma Corporation, Public Debt Finance, Reykjavik Academy, Sifma-Epda, Storkey & Co. Ltd. ,

## Some Figures...

**On 8<sup>th</sup> June 2009, the number of documents available on the PDM Network website is 718.**