Some thoughts on future challenges facing public debt managers

Presentation for World Bank Treasury's 2018 Sovereign Debt Management Forum

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October 2018

- How govt debt managers responded to the GFC
- The challenges facing govt debt managers
- A more active role for govt debt managers

The Global Financial Crisis

- Multi sigma tail risk event
- Private capital flows can generate global macro instability, key elements of Basel 2 could fail
- Major changes in government balance sheets, risk tolerance and investor habitat
- Major test of public debt management frameworks

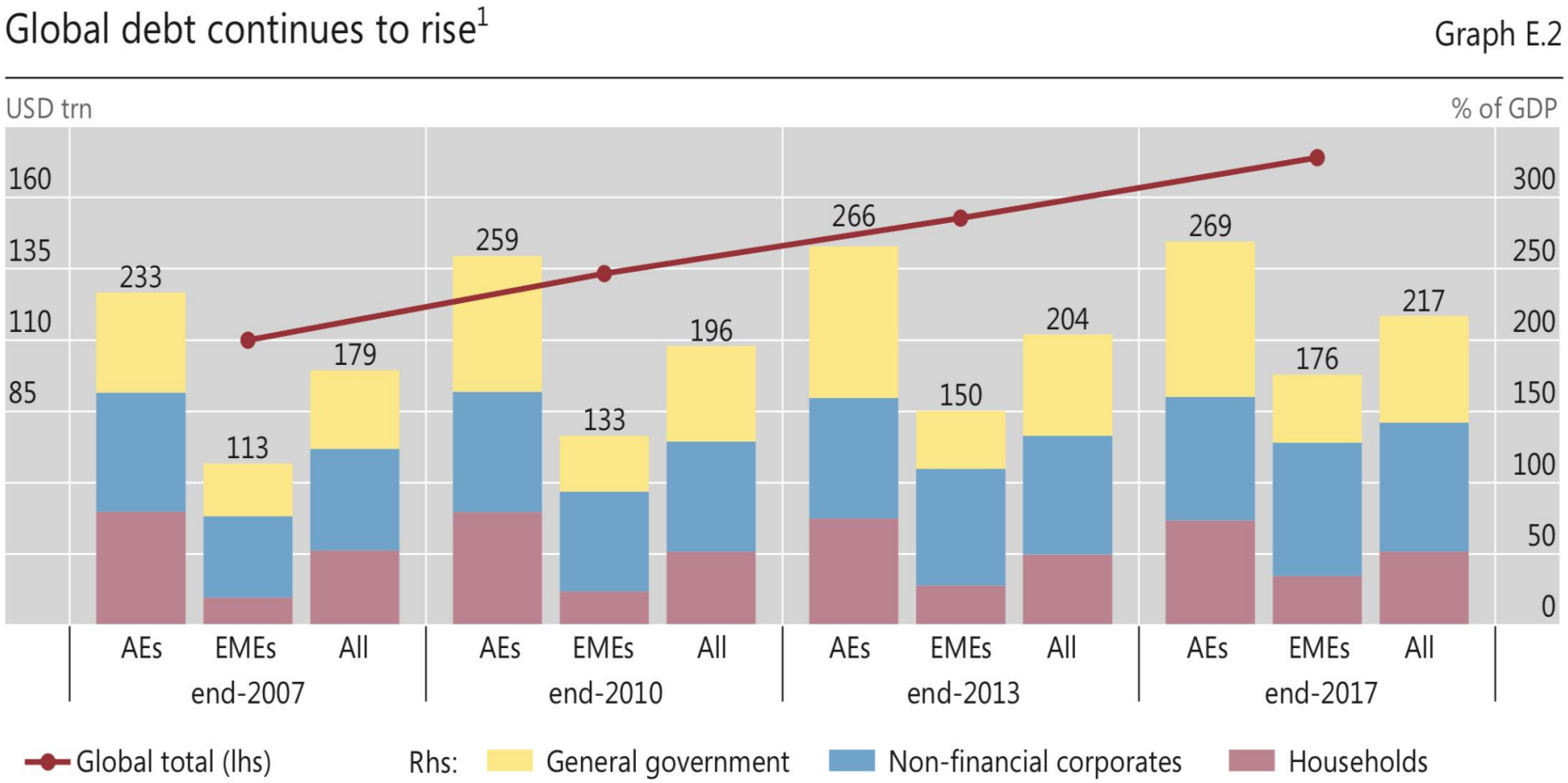
Measures taken by govt debt managers since GFC

- Reduce refinancing risk- extend maturity of new debt, diversify funding sources, expand investor relations
- Increased issuance of domestic currency debt/ reduced reliance on foreign-currency debt, flexible timing /issuance
- Investment in risk management and IT systems
- Improved dialogue with fiscal and monetary authorities

Challenges facing Govt debt managers

- Continued record high global and government debt
- Slower global growth and possible recession in advanced economies
- More complex interaction with macro-economic policy agencies

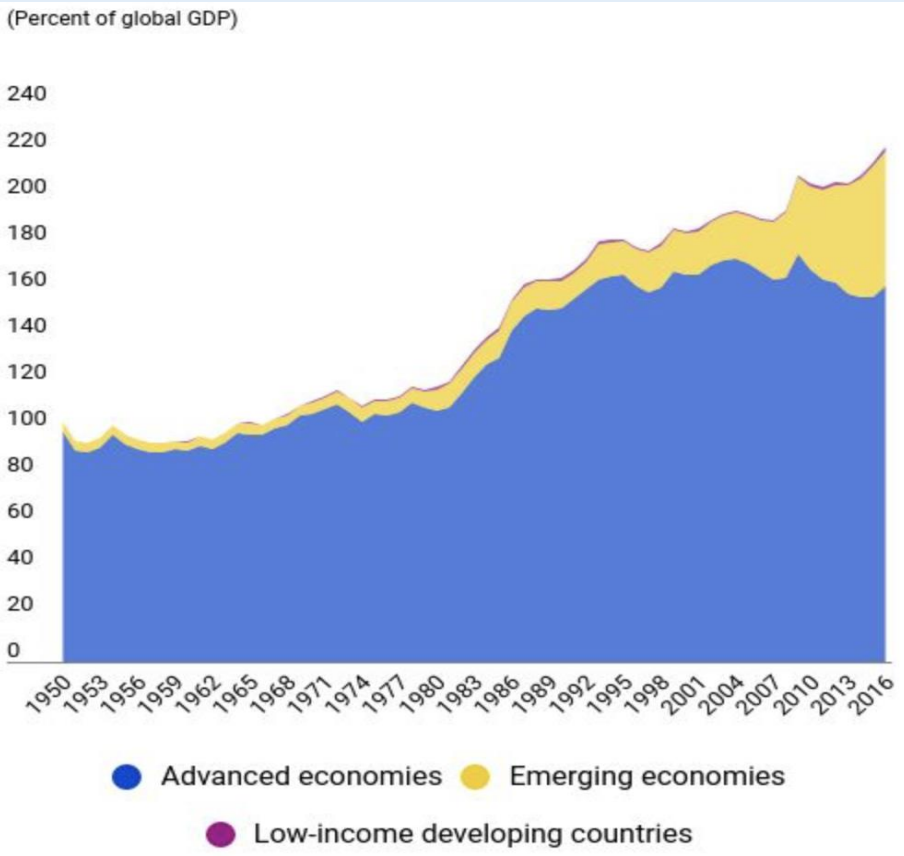
Challenges: global debt continues to rise



[1] Weighted averages based on GDP and PPP exchange rates. The sample includes all reporting economies except Ireland, owing to large data fluctuations caused by the restructuring of large multinational corporations.

Sources: IMF, *World Economic Outlook*; BIS total credit statistics; BIS calculations.

Global debt at record high



Sources: Mbaye, Moreno Badia and Chae forthcoming; Global Debt Database, and IMF staff estimates.
Note: Global debt refers to the sum of gross debt of the public and nonfinancial private

"Bringing Down High Debt" by Vitor Gaspar and Laura Jaramille, 18 April 2018

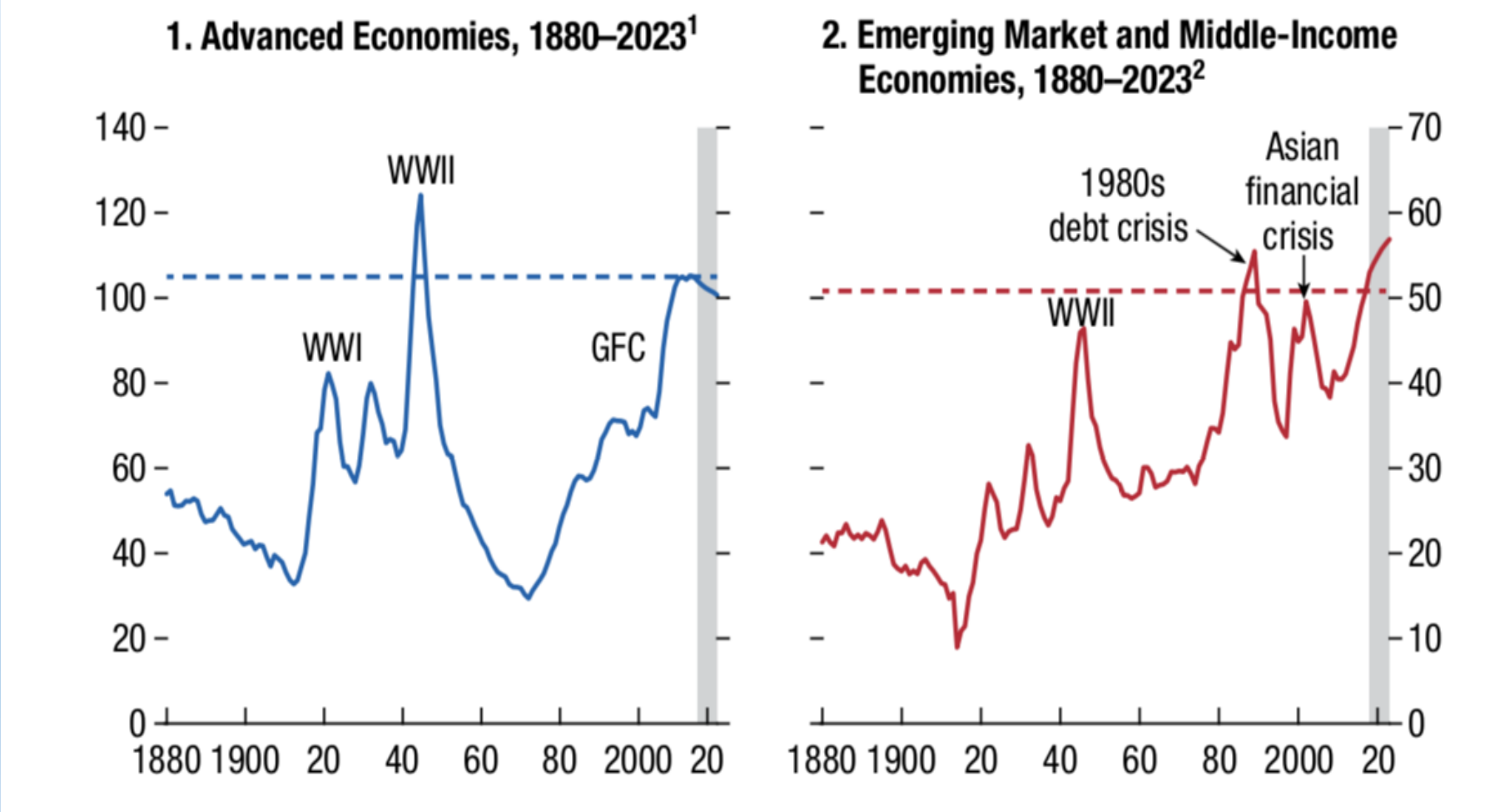
Growth in EM and AE debt is in different sectors

Debt (% GDP)			
	2007	2017	Change
EM	113	176	63
General Gov	37	48	11
Private	76	128	52
AE	233	269	36
General Gov	70	109	39
Private	163	160	-3

BIS data

Average debt-to-GDP ratios at historic highs

General Government Debt (Percent of GDP)



IMF Fiscal Monitor: Capitalizing on Good Times, “Figure 1”, April 2018

General govt debt likely to remain at record levels

% GDP			
		2017	2023
EM			
	net borrowing	-3.8	-3.6
	gross Debt	50	56
AE			
	net borrowing	-2.4	-2.2
	gross debt	103	102
LIDCs			
	net borrowing	-4.3	-3.4
	gross debt	44	42

IMF WEO database

Fix debt of nonbank emerging market borrowers

Bank of International Settlements and Federal Reserve Bank of St Louis; Ana Maria Santacreu, "Global Debt is Rising, Especially in Emerging Markets", 20 November 2017

Emerging market exchange rate

Jan 2018 = 100

[1] US Federal Reserve Board of Governors other important trading partners (OITP) index. Currencies of Asian and Latin American emerging-market economies make up the bulk of the OITP index .

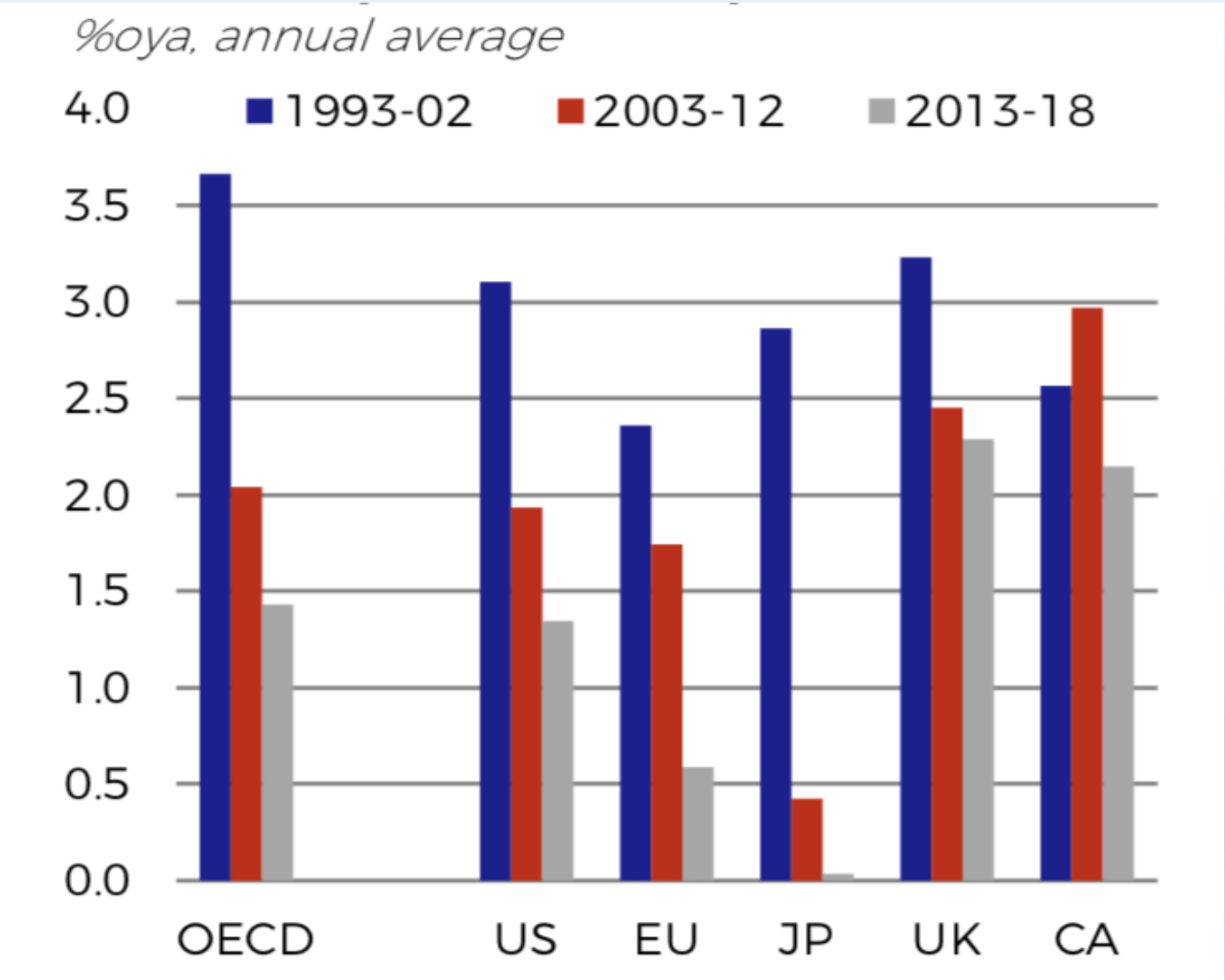
Source: Federal Reserve Board.

Consensus growth projections (6-10 years ahead)

	Pre GFC (%)	LT Consensus Forecast (%)
US	Over 3	2.1
Euro area	Over 2	1.3
Japan	1.5	0.7
EME	Down 1/5th to ½ pre GFC growth rate	

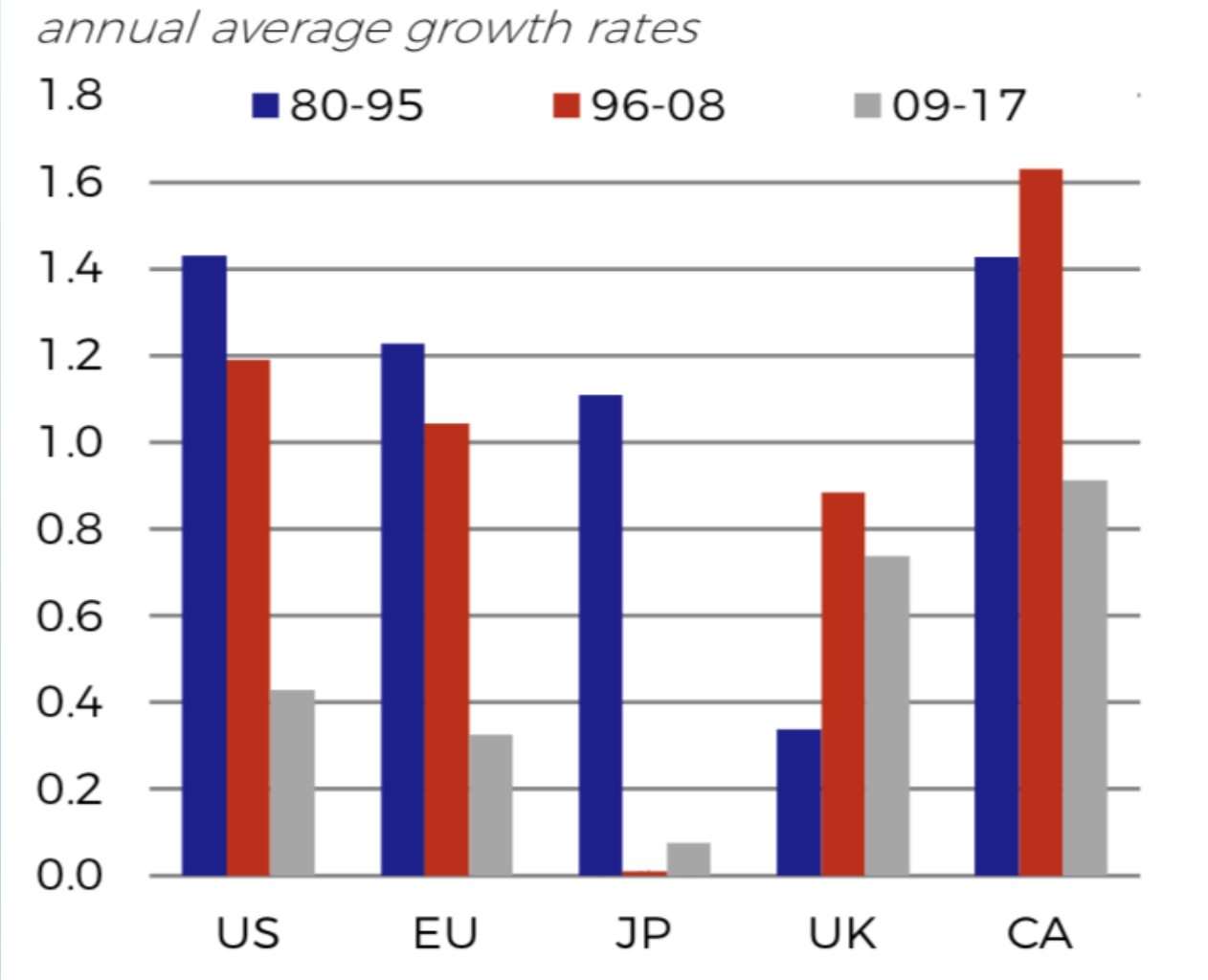
BIS Annual Economic Report 2018

Growth of productive capital stock



"Probing the Supply Side", Suttle Economics Notes # 45, 18 July 2018

Labour force growth



"Probing the Supply Side", Suttle Economics Notes # 45, 18 July 2018

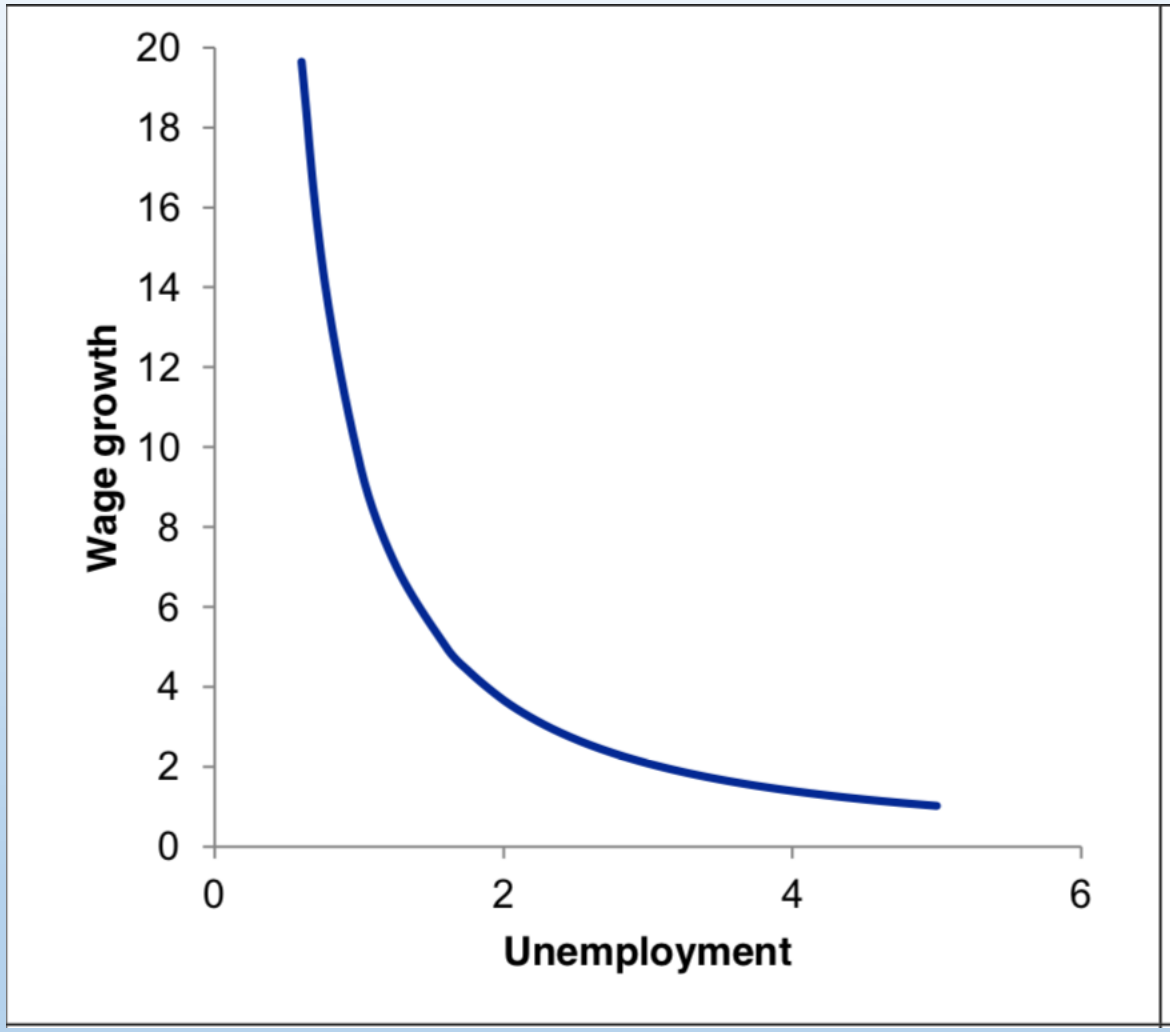
Factors that could trigger recession

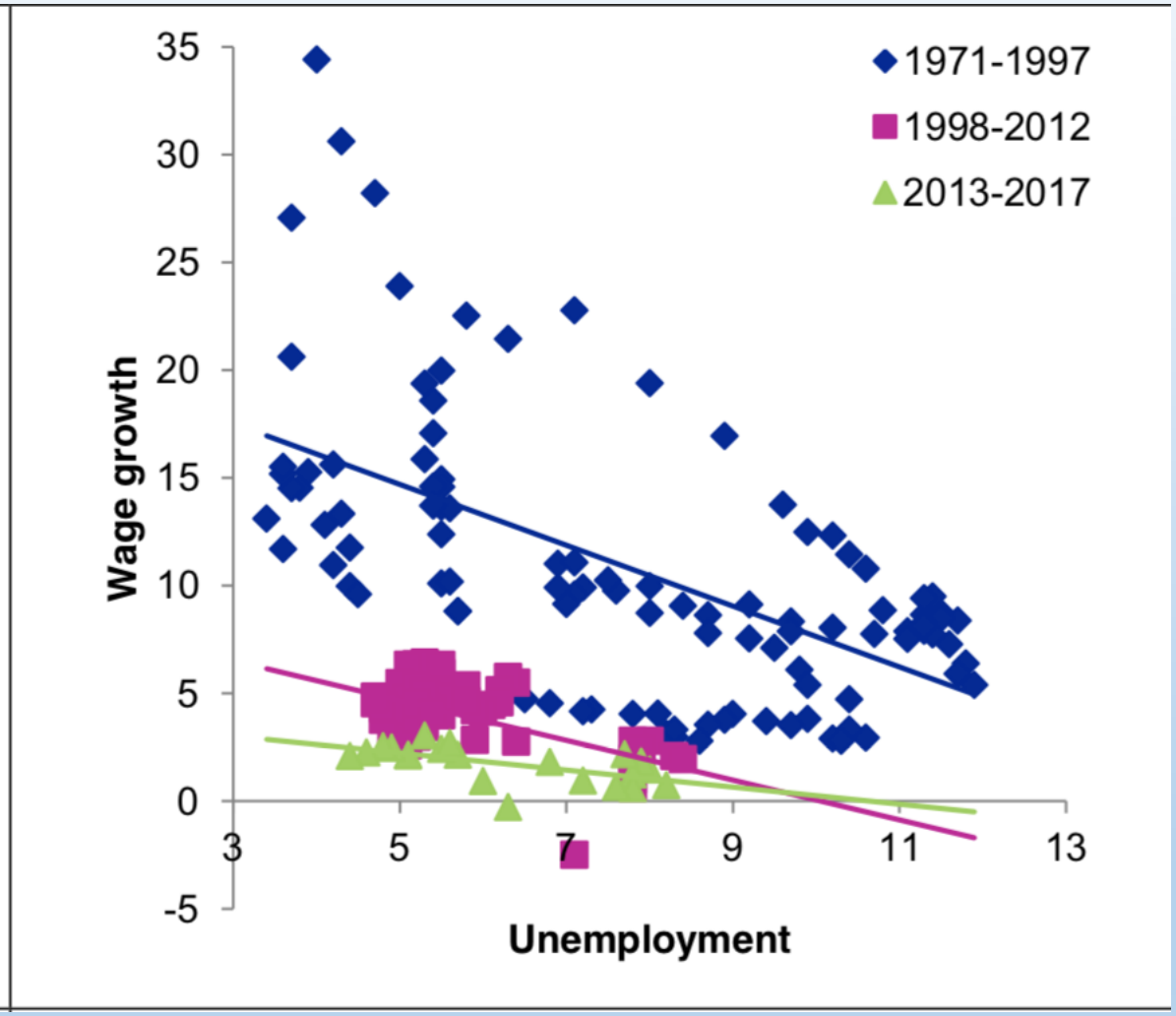
- Tightening in global monetary conditions (4 of last 5 tightening cycles in USA → crises in EME)
- US fiscal stimulus wanes (2019)
- Sharp adjustment in price of financial assets (2001, 2008)
- Rising oil prices (73-75, 81-83, 90-91)
- Slowdown in world trade
- Increased business and consumer uncertainty

More complex environment for monetary policy

- Inflation outcomes increasingly shaped by globalisation
- Phillips curves/ output gaps not deliver forecast inflation/ inflation expectations
- No/little influence over long term interest rates
- Uncertainty as to neutral interest rate
- Shift to unconventional monetary policies

UK data for Phillips Curve

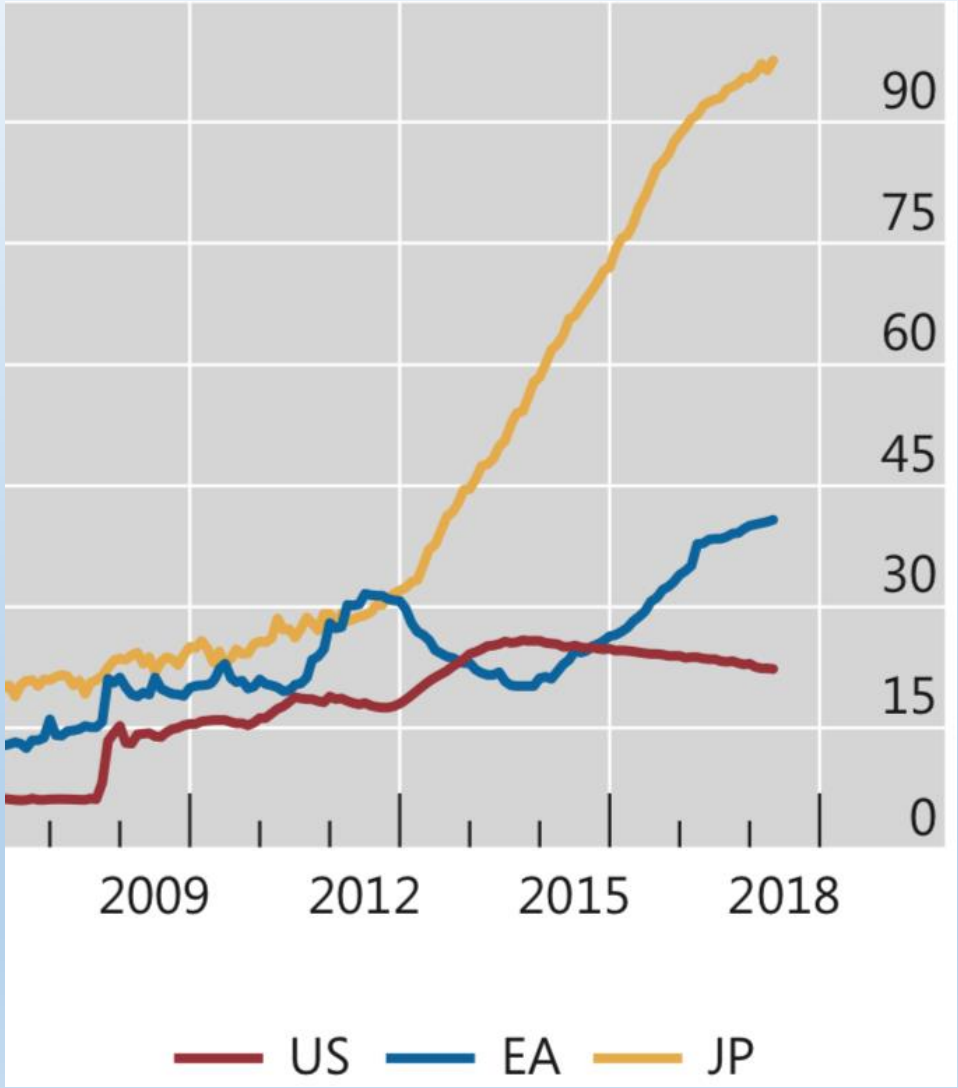




From a Bank of England Speech by Jon Cunliffe
Jon Cunliffe, "The Phillips Curve-lower, flatter or in hiding?
14 November 2017

Central bank total assets

Percentage of GDP



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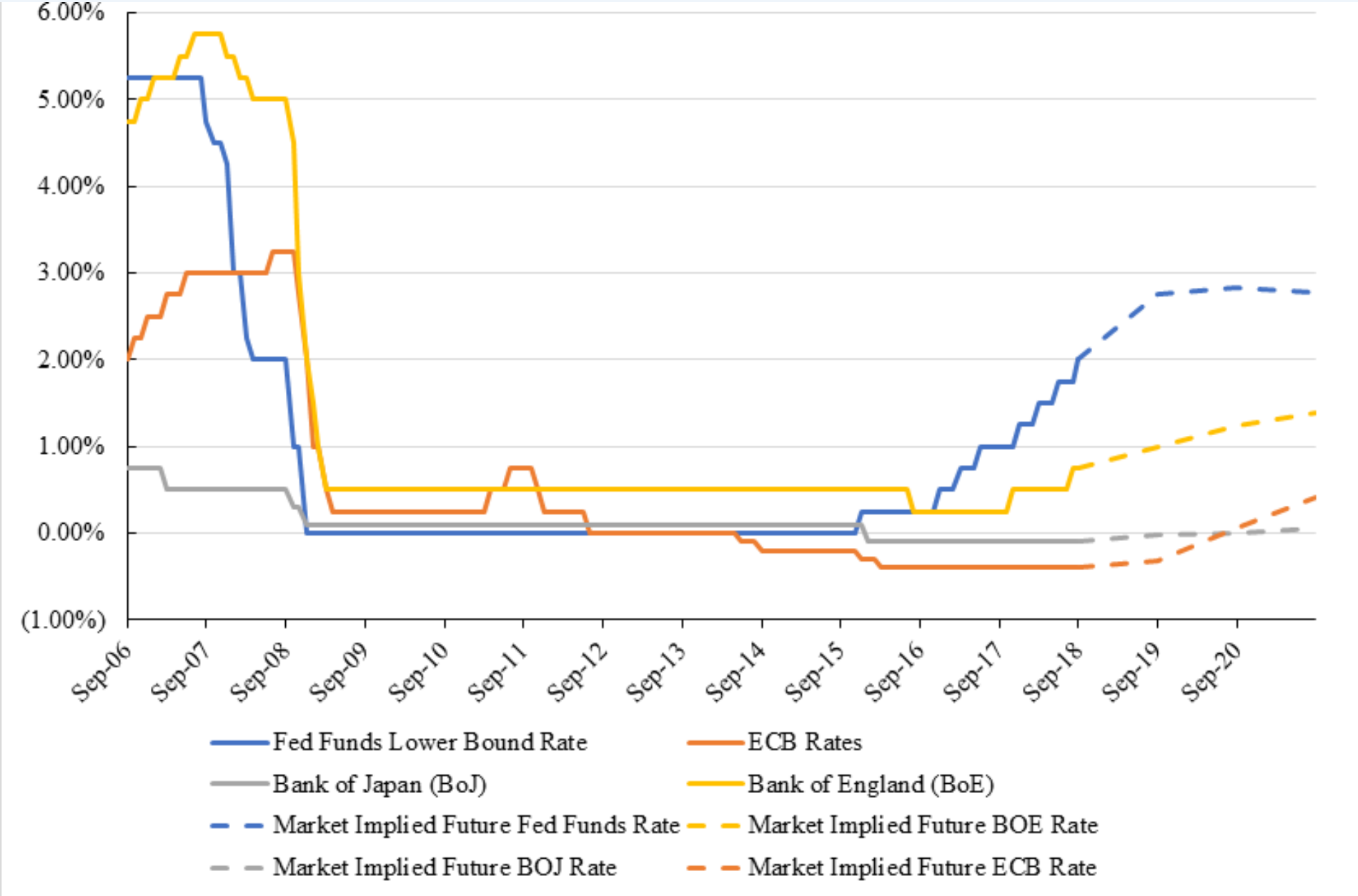
Central Bank rates



Institute of Institutional Finance (IIF) global debt monitor data and Bloomberg

Quantitative easing (QE) intersects with public debt management (PDM)

- Large scale QE shortens duration of govt bond market
- Each institution has well-defined objectives, values independence, prizes its credibility in the market. Both part of government balance sheet
- Debt agency and central bank have to resolve tension

QE and PDM goals

- Several options if QE expected to be large and prolonged:
  - leave overall duration of govt portfolio unchanged
  - maintain duration for PDM operations
  - reduce duration for PDM operations consistent with central banks operations
  - central bank amends scale and maturity of QE

More active role for govt debt managers

- QE unlikely to be temporary
- Contingent liabilities
- Greater interaction with central banks/regulators on FM regulation and financial stability issues

Role re contingent liabilities (CLs)

- IMF study- ¾ of 230 CL episodes had fiscal cost (median 2% GDP)
- Critical role for govt agency in monitoring risk exposures from CL, aggregating information, advise Govt on fiscal risk
- OECD study- govt debt managers often on periphery or excluded
- Critical partnership with Ministry of Finance needed

Greater interaction with FM regulators and on Financial stability

- Need good understanding of domestic financial system and regulatory policies
- Systemic financial stability issues interface with PDM
- Greater dialogue needed-financial stability reporting, stress tests, regulatory/macroprudential policies

Public debt managers face several key challenges

- Enormous progress in PDM over last 30 years
- Record global debt, public debt sustainability, slower trend growth, possible recession
- More active engagement with:
  - central banks- unconventional monetary policy, esp QE
  - finance ministry- overseeing govt fiscal exposure to CLs
  - financial regulators- regulatory changes affecting financial mkts and financial stability measures