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PRESS RELEASES

Good things come to those who wait: after six years, Croatia again has a public debt management strategy

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It took six years before the Government finally adopted a public debt management strategy[1] (on January 26, 2017), this time for the period 2017-2019. Given another key public finance management strategy - the State Assets Management Strategy, the Government is now faced with the challenge of coordinating its goals through clearly formulated operative measures.

The Public Debt Management Strategy for the Period 2017-2019 (hereinafter: Strategy) provides legal and institutional frameworks for public debt management, information on public debt and government guarantee stocks, as well as overviews of: financial borrowing in 2015 and 2016, public debt in the period 2011-2016 and the macroeconomic framework and credit ratings. In addition to the current status information, the document also includes public debt management guidelines for the period 2017-2019, debt development projections including sensitivity tests and goal achievement risks. It ends with a conclusion.

Legal and institutional frameworks for public debt management are incomplete. Two and a half pages are devoted to the administrative framework for public debt management (which is, by the way, scattered across multiple laws and strategic documents). A better approach would be if all regulations governing the formal strategy development obligation, public debt reporting, transparency, budget borrowing limits, the definition of powers and responsibilities concerning public debt issuance and management, as well as techniques for debt sale on the market should be consolidated in a single *Public Debt Act*. Briefly, governments should have long ago adopted, and the Parliament should have passed a public debt act as a key institutional prerequisite for the development and management of a transparent public debt market in Croatia. This would obviate the need to burden the Fiscal Responsibility Act with additional provisions on budgetary constraints on government borrowing.

Levels of public debt and guarantees. Against a background of the financial crisis, former governments substantially increased the share of public debt in GDP (from 39.6% of GDP in 2008 to 84.2% in 2015, i.e. by 44.6 percentage points). Slightly less than half of that increase was due to the conversion of contingent government liabilities (mainly guarantees to public companies) into explicit public debt, and the rest represented new borrowing. Croatia still borrows massively from commercial banks, and it is not clear why it does not rely more on borrowing by issuing bonds in the market, despite the many benefits of that type of borrowing. Ever since 2008, borrowing has been due to the

[1] For the purposes of that document, **public debt** is the general government debt as the nominal value of the general government sector debt (according to the Eurostat reporting rules), whereas **government debt** is a portion of public debt settled directly from the national budget.

government's assumption of credit liabilities of state-owned companies in the shipbuilding, railway and road transport sectors.

Favourable public debt structure. Croatia's public debt is exposed to currency risk, as 65% of the debt is denominated in euros, about 30% in HRK and 5% in US dollars. By means of currency swap transactions, liabilities arising from USD-denominated debt have been converted into EUR-denominated liabilities. Given the lower EUR/HRK exchange rate variability, this has markedly reduced currency risk. This approach reflects prudent debt management, although the final assessment should require additional data on the cost of such transactions. The maturity structure of debt can be improved by restructuring a portion of debt by means of debt instruments falling due in 2023 and 2027 when the repayment burden will be considerably lower than in the rest of the maturity period, as well as by gradually extending maturities to ten years and above, and reducing short-term debt. In operational terms, the ***Ministry of Finance deserves good rating for its public debt management.*** This is also corroborated by the increase in the share of fixed-rate debt from 80.2% to 86% over the period 2011-2016, which completely eliminated the interest rate risk of the public debt portfolio.

Strategic goals and targets of public debt management. One of the Government's strategic goals and a national priority is to reduce the share of public debt in GDP to about 75% by 2019. Other public debt management goals include: mitigating refinancing risk and reducing the share of short-term debt, mitigating currency and interest rate risks and increasing public debt and borrowing transparency. While not specially highlighted, strategic targets (the debt structure-related values aimed at reducing the risks), as well as the time horizon of implementation are also set out in the last table of the Strategy. These values will provide a basis for a subsequent assessment of the Government's public debt management performance.

Sustainability and projections of public debt. The achievement of the Government's goals to cut the public debt to GDP ratio by more than 10 percentage points and keep deficit below 3% of GDP by 2020 will further depend on the realisation of privatisation receipts (expected to amount to HRK 2.8bn, in cumulative terms, in 2017 and 2018). This requires close coordination between the Government and Ministry of Finance on one side and the State Assets Ministry on the other. The latter ministry must formulate a clear state asset management plan and carry out the planned privatisation of state-owned companies.

Public debt transparency and better communication with the public. Indications are that the Government will upgrade the Ministry of Finance's public debt management department to the status of a directorate and strengthen and increase its public debt management team (which has so far been understaffed), thus making an important contribution to the quality of debt management. After a long time, the Strategy imposes an obligation on the Ministry of Finance to publish a treasury bills monthly issuance calendar and a quarterly bond issuance schedule in 2017. However, both the Government and Ministry of Finance should radically improve their communication with the professional and general public through their official websites, by publishing monthly public debt information on a regular basis. The data should be regularly updated and presented in an electronic format. The Strategy has to be translated into English and published on the websites of the Government and Ministry of Finance, with a view to improving transparency and the Government's credibility. This will boost investor confidence, which may positively affect the country's credit rating and the cost of borrowing in the financial markets.

The Government deserves commendation for preparing a strategic document which directly contributes to the transparency and credibility of the country in the financial markets. It is now expected to coordinate the Ministry of Finance's public debt management operations with the activities of the State Assets Ministry regarding the preparation of privatisation of state-owned companies and to announce the expected financial and economic effects of such activities.