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Asset and Liability Management

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Two Approaches for Considering Asset and Liability Management

**Balance Sheet
Management**

**Government
Financial Assets
and Liabilities**

Look for Natural Hedges

**Portfolio
Management**

**DMO Managed
Financial Assets
and Liabilities**

Look to Actively Hedge

Government Financial Asset Portfolios

1. Foreign exchange reserves
 - managed by the central bank (may involve fund managers)
2. Cash and liquidity portfolios
 - managed by DMO or Treasury (cash management)
3. Financial investment portfolios (including derivatives)
 - managed by DMO but could be placed with central bank particularly for foreign currencies
4. Sovereign wealth funds (~ 45 countries)
 - managed under own legislation and/or by fund managers
5. Other designated funds
 - insurance & pension funds, student loans, sinking funds, guarantee redemption funds, disaster risk such as SEADRIF

DMO Financial Asset Portfolios

1. Lending and onlending
 - Provided to SOEs and sub-national governments
2. Cash and liquidity portfolios
 - For cash management and/or to meet debt service payments
3. Financial investment portfolios
 - Financial assets or funds managed by DMO
4. Derivative portfolios (normally matched to a derivative liability)
 - Asset component used for hedging and managing risks
5. Sinking funds
 - Established to cover large bond maturities
6. Guarantee redemption funds
 - Created by guarantee fees

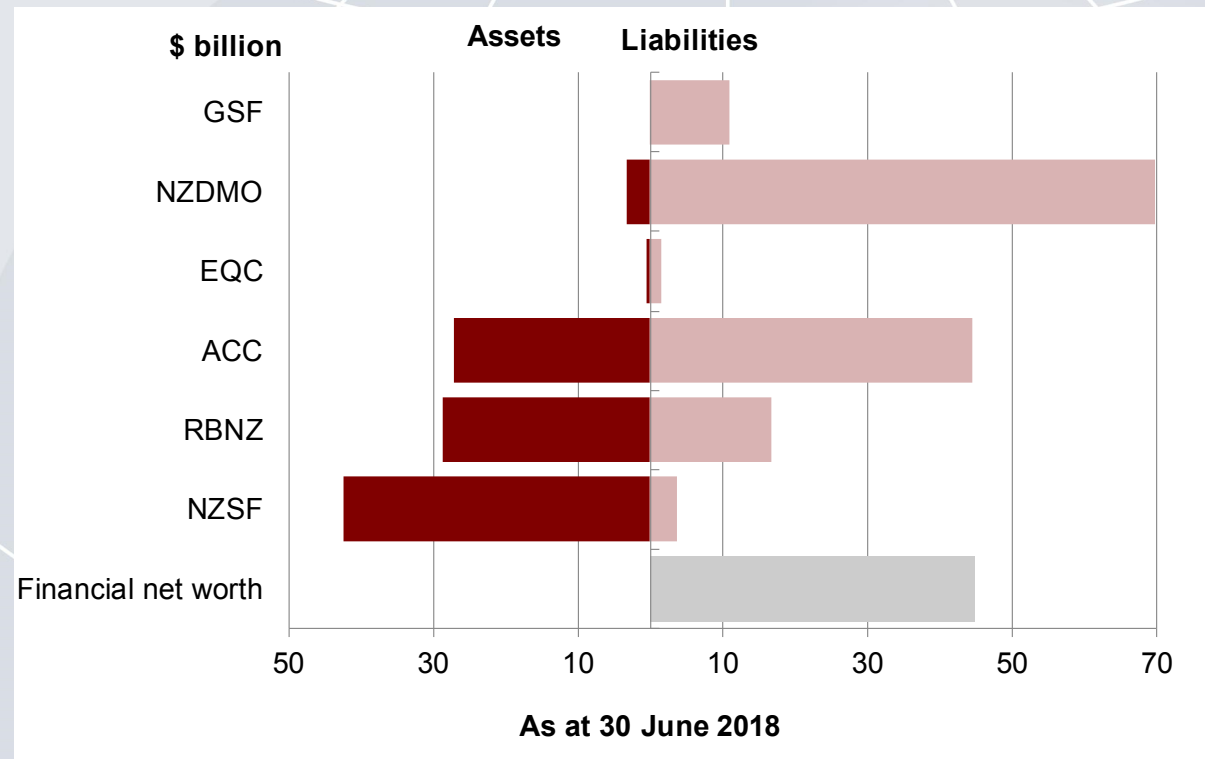
Financial Balance Sheet of New Zealand

- GSF: Government Superannuation Fund
- NZDMO: now NZDM
- EQC: Earthquake Commission
- ACC: Accident Compensation Corporation
- RBNZ: Reserve Bank of New Zealand (Central Bank)
- NZSF: New Zealand Superannuation Fund (SWF)

“Notional” NZDMO balance sheet includes other financial assets

Objective is to manage wider Government balance sheet risk

Figure 22 – Financial assets and liabilities



Source: The Treasury

NZ Government Financial Assets

Financial assets

		Actual	
	Note	30 June 2018 \$m	30 June 2017 \$m
By class			
Cash and cash equivalents		19,340	18,732
Reinsurance, trade and other receivables	12	6,385	4,905
Long-term deposits	13	5,379	4,730
Derivatives in gain	13	3,153	4,381
Marketable securities	13	40,532	39,558
IMF financial assets	13	2,053	1,837
Share investments	14	36,256	30,700
Kiwibank loans and advances	15	18,281	17,795
Student loans	15	9,301	9,197
Other advances	15	1,840	1,591
Total financial assets		142,520	133,426

Source: NZ CFS as at 30 June 2018

NZ Government Financial Liabilities

Financial liabilities

		Actual	
	Note	30 June 2018 \$m	30 June 2017 \$m
By class			
Issued currency		6,375	5,980
Accounts payable	18	9,221	10,517
Borrowings:	19		
Government bonds		62,393	64,349
Kiwibank customer deposits		16,160	15,960
Settlement deposits with Reserve Bank		7,603	6,471
Derivatives in loss		5,067	3,113
Treasury bills		4,114	4,071
Finance lease liabilities		1,318	1,412
Government retail stock		182	190
Other borrowings		18,815	16,240
Total borrowings		115,652	111,806
Total financial liabilities		131,248	128,303

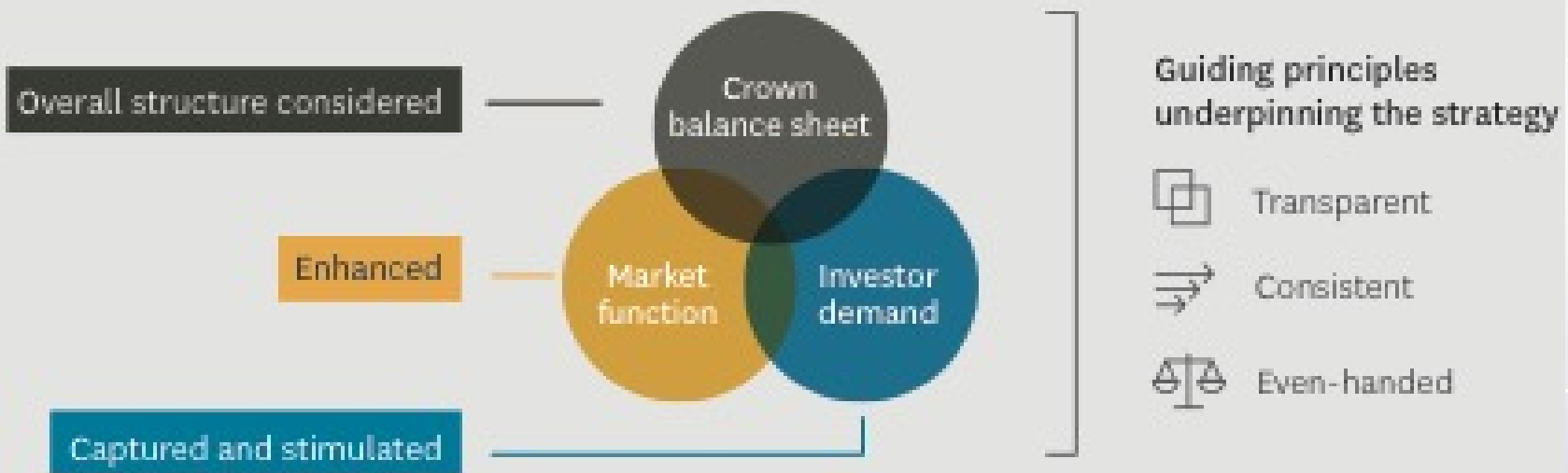
Source: NZ CFS as at 30 June 2018

NZDMO Funding Strategy

The funding strategy at a glance

NZDMO has the objective of minimising the Crown's borrowing costs over the long term while keeping risk at an appropriate level. To achieve this objective, NZDMO takes a strategic rather than tactical approach to funding.

Achieving a balance between the following three goals:

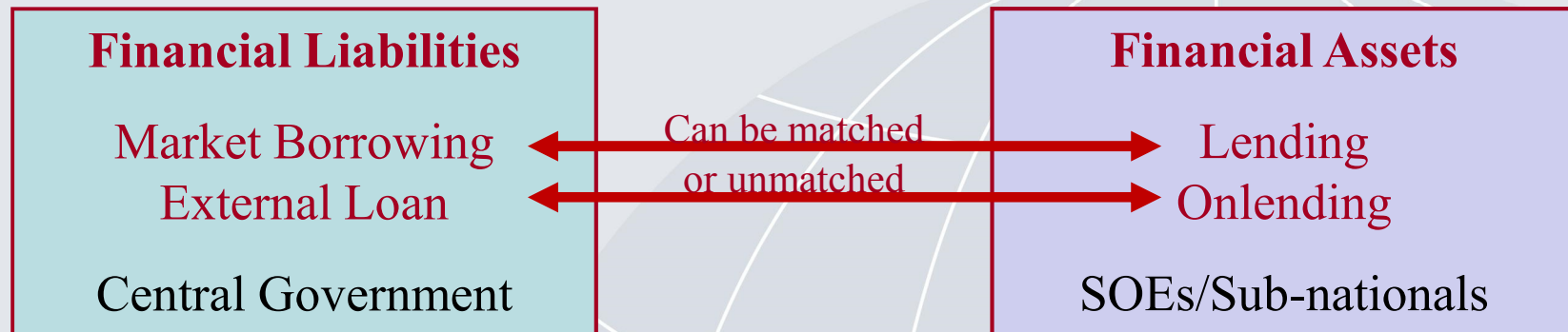


Source: The Treasury

NZDMO Foreign Currency ALM

- Assets and liabilities are valued daily on a mark-to-market basis
- Profit (or loss) is generated from changes in the market value of the portfolio
- Tactical trading is employed to increase profit or reduce risk
- Comprehensive risk measures and limits are used (VaR, stop loss limits, stress testing)
- Risk adjusted performance measurement has been developed to assess profits against risk utilisation

Example of ALM Liability Portfolio



If unmatched, manage as a net liability portfolio and undertake hedging of net portfolio risks including netting of payment flows (i.e. manage mis-match risks)

- use financial instruments (including derivatives) to actively manage currency, interest rate and cash flow risk
- seek to minimise the “cost of carry”
- primarily hedge the cash flows for current budget year

Example of ALM Liquidity Portfolio

Debt Service Payments

For external debt service payments due over the next 1, 3, 6 and 12 months:

- identify each debt service payment by currency, amount and due date
- each week (or month), hedge the payment exposure for the next 3-6 months and maintain on rolling 3-month basis

Matched

Financial Investments

Place an equivalent amount as an investment(s) to hedge the payment due:

- match each cash flow by currency, amount and due date
- invest to match cash flows or cover forward using derivatives
- monitor net position and unmatched exposures

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