

THE INVESTMENT ATTRACTIVENESS OF GOVERNMENT SECURITIES IN THE REPUBLIC OF MOLDOVA

ATRACTIVITATEA INVESTIȚIONALĂ A VALORILOR MOBILIARE DE STAT ÎN REPUBLICA MOLDOVA

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Abstract: Valorile mobiliare de stat reprezintă una dintre cele mai importante surse financiare pentru finanțarea deficitului bugetar de stat, pecum și a unor proiecte importante pentru dezvoltarea economiei naționale. O piață a valorilor mobiliare de stat dezvoltată, previzibilă și transparentă reprezintă în sine un obiectiv important pentru orice guvern, dat fiind că este un indicator al atractivității investiționale a țării pentru potențiali investitori. Prezentul articol propune o analiză retrospectivă a evoluției pieței valorilor mobiliare de stat din Republica Moldova, cât și a valorilor mobiliare de stat privite prin prisma atractivității investiționale a acestora.

Key Words: atractivitate investițională, valori mobiliare de stat, bonuri de trezorerie, obligațiuni de stat

JEL CLASSIFICATION: E4, E5, G1, H6

INTRODUCTION

The government securities market is one of the most important sector of the financial market in the Republic of Moldova: it provides resources to the government for meeting its needs, implementing its fiscal policy and is critical in bringing about an effective and reliable transmission channels for the use of indirect instruments of monetary control.

The government securities market was set up in the Republic of Moldova in 1995. Since then, the Ministry of Finance, as the state securities issuer, in cooperation with the National Bank of Moldova, as the state fiscal agent, has undertaken a series of measures in order to develop a modern government securities market based on the principles of transparency and the participants' fair competition.

Assumed that government securities (GS) are one of the most important sources which allow public authorities to finance the budget deficit and the projects for the development of the national economy, they are the subject of various policies developed by the Government. Thus, in order to facilitate the application of this investment instrument on the domestic market, according to the *Medium-Term Debt Management Program* of the Government for the period 2020-2022 the main objectives regarding GS market are: the diversification of GS sales channels with increasing access of individuals to GS purchasing and the insurance of the transparency and predictability of this market. Government securities have always been considered as an investment option which is suitable only for the important investors like banks or other financial institutions. However, government securities are, as well, one of the best options for investment for common investors. Here are the reasons why to invest in Government securities issued on the Moldovan market:

- they carry practically no risk of default, given the fact that they benefit from the full state guarantee. Since the establishment of the GS market in the Republic of Moldova, the Government has never withheld payment for their redemption or interest;
- are the most liquid financial instrument. As a result of trading the GS on the secondary market, the investor obtains certain funds. At the same time, the investor receives the interest for each day of holding the GS in the portfolio.
- they offer stable good long term returns which is not subject to taxation.

The *scope* of this study is, based on the investigation of evolution of the main indicators of the government securities market, to analyze the investment attractiveness of government securities in the Republic of Moldova.

PROPOSED RESEARCH METHODS

The performed research was implemented based on the analysis of the dynamics of main indicators of the market (volumes, structure by types of government securities, yields, main investors) during the period of 2016-2020, as well as based on the comparative analysis between the average yields of government securities, some macroeconomic indicators (consumer price index, exchange rate of the national currency) and the average interest rates on deposits offered by the banking sector. The research methods used in this study are as follows: the documentary method, the qualitative and quantitative data method, the synthesis method, the comparison method, as well as the graphical method.

Analyses is found on the statistical official data and reports available on the official websites of the National Bureau of Statistics of the Republic of Moldova (NBS), the Ministry of Finance of the Republic of Moldova (MF) and the National Bank of Moldova (NBM), as well as the legal framework related to the government securities market in the Republic of Moldova, Government Decisions etc.

RESEARCH OF EMPIRICAL ASPECTS

The Ministry of Finance issues government securities on the domestic market in the form of Treasury Bills and Government Bonds in national currency. The nominal value of a GS is MDL 100.

Treasury bills (T-Bills) are government securities issued at a discount and redeemed at the nominal value at maturity. The maturity of T-bills is up to one year. Thus, the Ministry of Finance issues T-bills for 91, 182 and 364 days. Sometimes, under specific circumstances and following the need to increase the budget deficit, funding at the expense of domestic sources, the Ministry of Finance issues T-bills with a maturity of 21 days. This mainly occurs in exceptional situations when potential investors are not sure about the stability of the national currency and prefer to make short-term investments in government securities market.

Government Bonds are securities issued at discount, nominal value or premium, with maturities of one year or more, for which the issuer pays periodic interests in accordance with the fixed or floating interest rate as stipulated in the issuance conditions and which are redeemed at nominal value upon maturity. The Ministry of Finance issues GB with fixed rate for 2, 3 and 5 years and GB with floating rate for 2 years.

In accordance to the legal framework, the National Bank of Moldova is in charge of the organization, on behalf and at the request of the Ministry of Finance, of auctions for GS sale on the primary market. GS placement auctions are conducted in the electronic system of Bloomberg Professional Service - Bloomberg Auction System (BAS).

According to the rules for holding auctions, only commercial banks that have the quality of primary dealers, can participate in the auctions in their own name and on their own account, as well as at the expense of investors, at their request. The maximum volume of GS that can be held by an investor constitutes 50% of the volume of GS with the same ISIN identification number, proposed for sale on the primary market or in circulation.

GS are issued in book-entry form and, therefore, their issuance, record-keeping, confirmation of ownership and the payment of the principal sum at maturity date and of the related interest (coupons) is performed by the Single Central Depository of Securities (Central Depository) in the name of the Ministry of Finance.

The secondary market is organized through the unique trading platform E-Bond and the System of Central Securities Depository, where GS are traded after issuance on the primary market. The National Bank of Moldova is in charge of the management of interbank secondary market of government securities issued in book-entry form on the domestic market.

The main indicators regarding the Government Securities issuance in the period of 2016-2020 are presented in Table 1.

Table 1. Main indicators of the Government Securities primary market

Indicator	31.12.2016	31.12.2017	31.12.2018	31.12.2019	31.12.2020
Total amount of government securities issued, mln. MDL, total	18333.8	18153.8	12.922.5	11390.5	18224.5
Government securities issued and sold on the primary market, mln. MDL	10264.1	9900.2	9779.4	9327.1	18064.1
Converted government securities, mln. MDL	8069.7	8253.6	3143.1	2063.4	160.4
Number of government securities auctions, units	67	76	56	49	48

Source. Elaborated by the author based on <https://bnm.md>

Analysing the statistical data available on the official website of the Ministry of Finance of Moldova, it is found a slight steady decrease in the value of GS issued on the primary market during the period of 2016-2019, followed by an almost twice increase registered in 2020 (see Figure 1).

Thus, compared to 2016, the reduction for 2017 is 363.9 million lei, the one for 2018 is 484.7 million lei, and the one for 2019 – 937.0 million lei. The smaller issuance of GS in the period of 2017-2019 was due to the decrease of the Government' demand for financing on the internal market determined by the increase of the budget revenues, in the context of the economic recovery registered in that period.

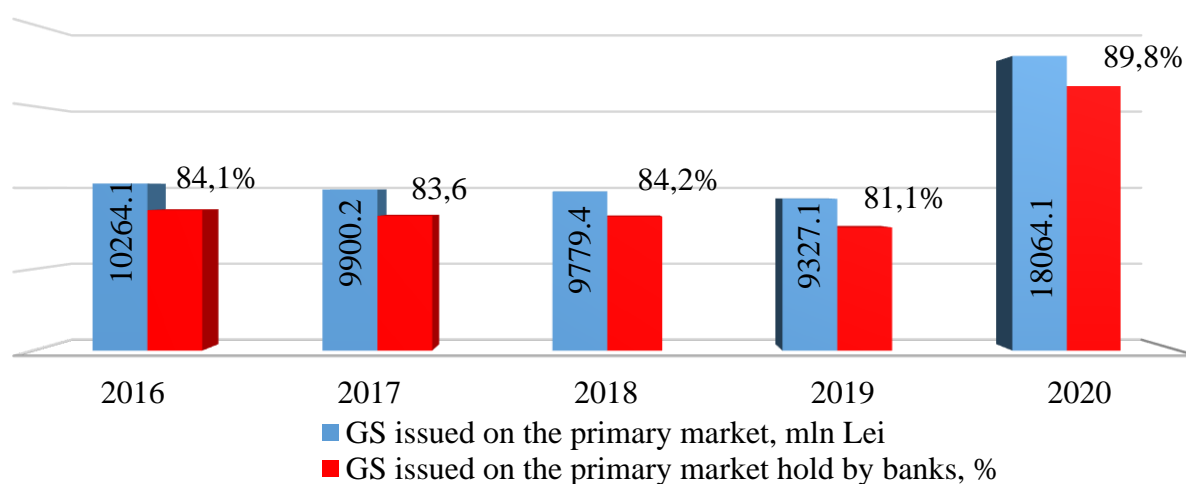


Figure 1. Banks' share in the total amount of government securities issued on the primary market, 2016-2020

Source: Elaborated by the author based on <https://mf.gov.md>

A distinct situation is characteristic for 2020, when GS were sold in the amount of 18.1 billion lei, which represents an increase by 1,8 time as compared to 2016. The higher amount of GS issued on the primary market in 2020 was determined by the higher budget expenditures generated by the pandemic crisis. Another factor to be taken into consideration when analysing this dynamic is that the GS offered on the domestic market during a year is directly dependent on the value of funds planned in the *Annual Law of the state budget*. Thus, based on the provisions of the state budget Laws for the years of 2017–2020, it is noted that in 2020 the government expected to cover about 4 billion lei on financing needs from the GS account, an amount that exceeds, on average, 3-4 times the values planned for the years of 2017– 2019.

Analysing the structure of GS issued on the domestic market, by their type, it can be noticed that the most traded GS are represented by short-term GS, namely Treasury bills (see Figure 2). According to Figure 2, during the analysed period, the investors' appetite for 182-day and 364-day T-bills has emphasised during the analysed period. Thus, the share of the mentioned government securities has creased from 31,3% in 2016 to 41,0% in 2020 and respectively, from 38,3% in 2016 to 41,3% in

2020. At the same time, the share of T-bills issued for 91 days has registered a steady decrease, from 28,9% in 2016 to 11,3% in 2019. Besides, the analysis presents a still low interest of the investors for long-term GS. Thus, in 2020 the shares of 2, 3 and 5-year GB registered the following values: 2,5%, 1,5% and 2,4%, respectively.

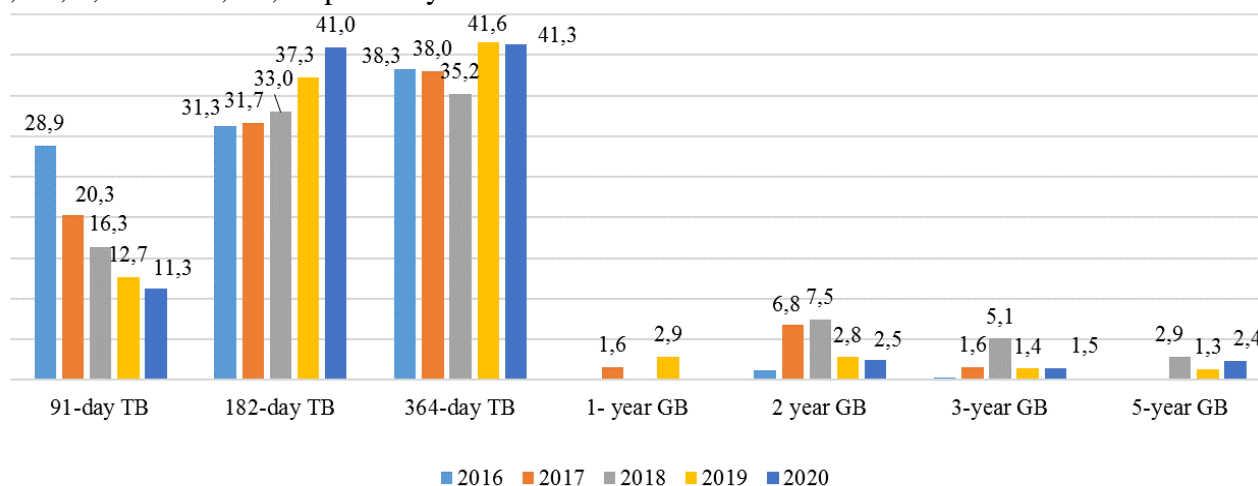


Figure 2. Government securities structure by type of securities in the period of 2016-2020, %

Source: elaborated by the author based on <https://mf.gov.md>

The banking sector remains the main investor in GS. About 85% on average of total amount of GS issued in the period 2016-2020 are purchased by banks. Figure 2 presents the evolution of the structure of the banks' share of total GS issued on the primary market in the last 5 years.

According to data from Figure 1 it can be observed that the banks' share of total GS issued on the primary market increased in 2020 to about 90% as compared to 81% in 2019 and the average of 83% for 2016-2019.

The main reason for this increase is that in the context of Covid-19 crisis that impacted the banking sector inclusively through a decreased credit portfolio, buying government securities for banks represented an important source for obtaining reliable profits. In general, a reason for banks to actively buy GS is the importance of the effective liquidity risk management for the banks. GS represents assets that are highly liquid and are generally risk-weighted at 0% under the Basel III standardized approach for capital.

Another important indicator when analysing the GS market is the rate of return of the government security, or the yield. Thus, according to Figure 4, the nominal yields on Treasury bills registered an increasing trend in 2015, followed by the decrease in 2016 and a relative stable trend up to February 2021. The main determinant of such volatility of T-bills yields registered in 2015-2016 was the sizable increase of the inflation rate in 2015, as the result of the contraction by 0,3% of Moldovan economy in that period driven by the 2014 bank fraud. Yet, since 2016 the Moldovan economy has re-entered into the recovering process.

Generally, the yields of GS are influenced by the evolution of macro indicators, like GDP growth, inflation, exchange rate, consumption, as well as developments in international government securities markets. In order to find out if GS yields are impacted by macro indicators, the author has measured the correlation coefficient between the average yield of Treasury bills and both the inflation rate and the exchange rate of MDL against USD.

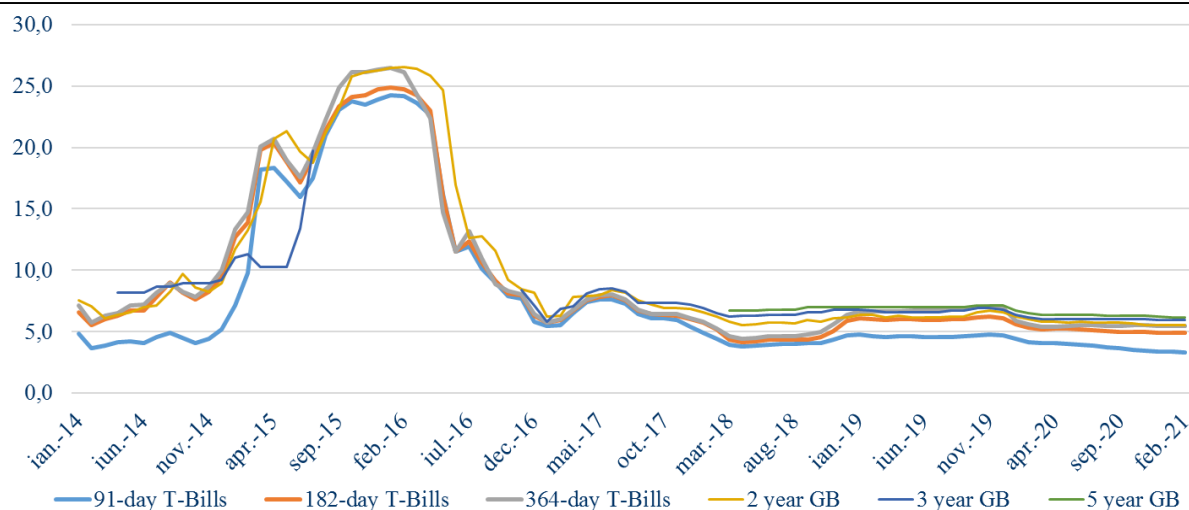


Figure 3. T-bills nominal yields by type of securities in the period of 2014-2020, %

Source: elaborated by the author based on <https://mf.gov.md>

According to correlation coefficient resulted from the analysis (see Figure 4), the average yield of GS with the maturity of up to 1 year is positively linked to the inflation volatility (correlation coefficient=0,78539).

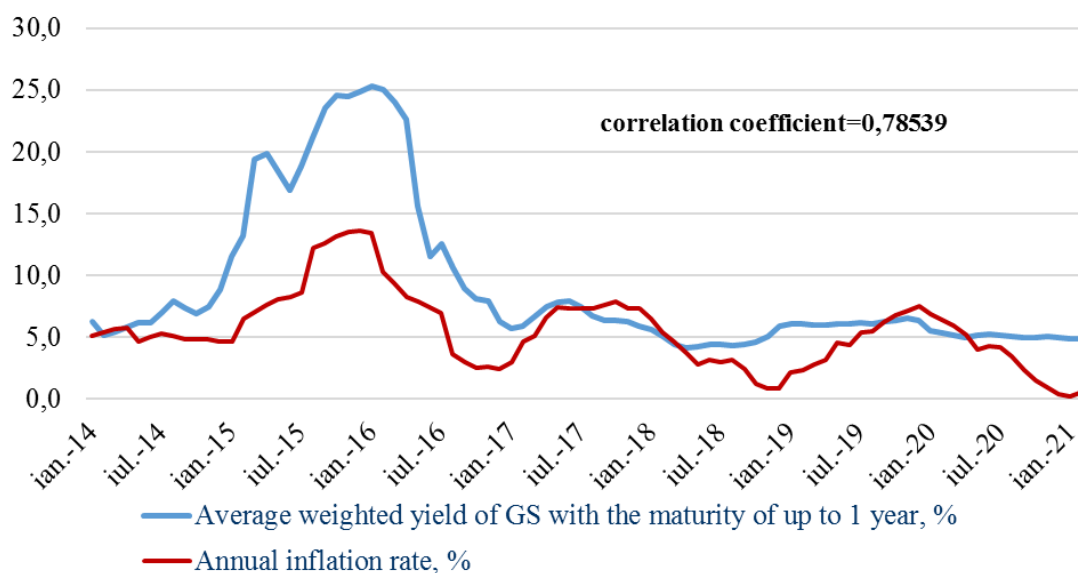


Figure 4. The correlation between the weighted average yield on GS with the maturity of up to 1 year and the inflation rate

Source: elaborated by the author based on <https://mf.gov.md>, <https://bnm.md>

Also, according to correlation coefficient resulted from the analysis (see Figure 5), the average yield of GS with the maturity of up to 1 year is positively linked to the exchange rate volatility (correlation coefficient=0,51650).

From the investment attractiveness point of view, along with the analysis of such elements specific to GS market, like types of GS issued, conditions of GS market, it is important to perform a comparative analysis of the rate of return on GS in comparison to the returns offered by other investment instruments existing on the financial market.

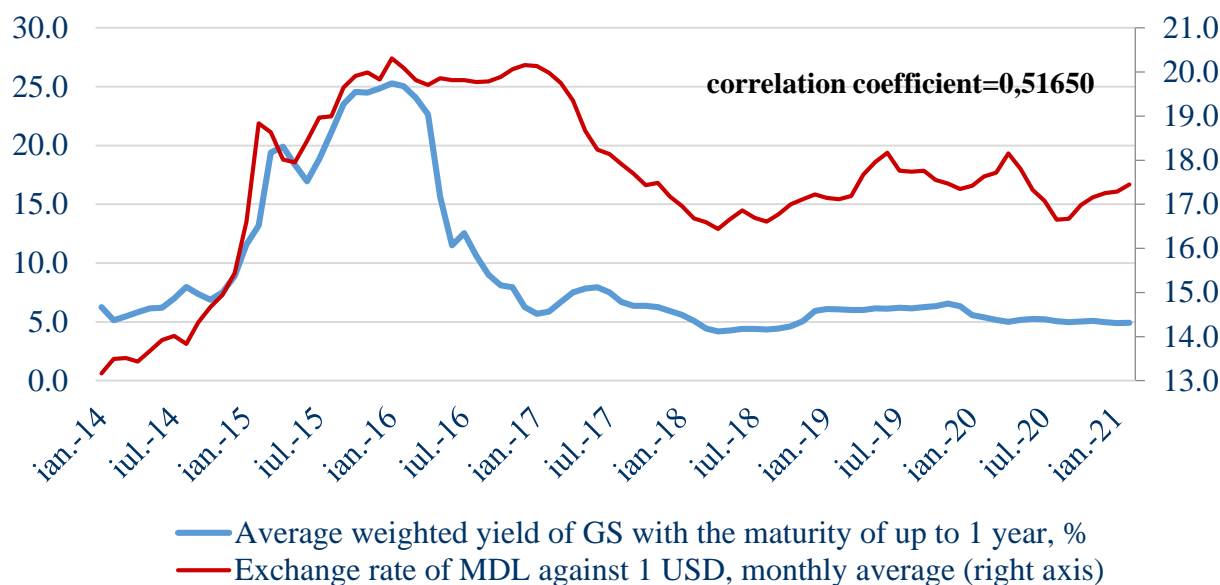


Figure 5. The correlation between the weighted average yield on GS with the maturity of up to 1 year and the exchange rate of MDL against USD

Source: elaborated by the author based on <https://bnm.md>

Actually, the principal investment instruments that create a strong competition for GS on the market are bank deposits. Thus, from Figure 6 it can be observed that during the investigated period the average yield on treasury bills with the maturity of up to 1 year, has recorded, with short exceptions, higher values compared to the interest rates on the banking system for deposits with the same maturity.

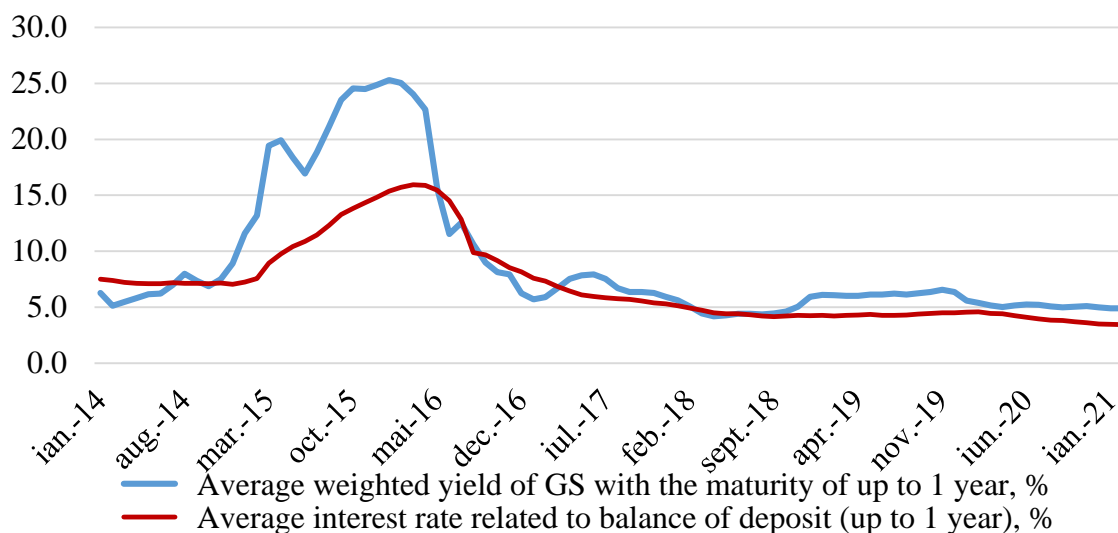


Figure 6. The weighted average yield on GS with the maturity of up to 1 year and the average interest rate related to the balance of deposit with the term of up to 1 year, %

by the author based on <https://bnm.md>

In this context we can conclude that government securities remain a more attractive source of investment compared to deposits in the banking system. In addition to the higher interest rate, a higher attractiveness of GS in relation to bank deposits is also due to higher liquidity as well as increased security as they are guaranteed by the government. According to *Law no. 575/2003 on deposits guarantee in the banking system*, starting with January 1, 2020, the bank deposits are guaranteed in the amount of 50 thousand lei regardless of the value of the deposit.

CONCLUSIONS

Government securities plays an important role in the public debt management. A well-developed, predictable and transparent government securities market is important to most governments as it increases the attractiveness of the country for potential investors. According to the analysis of the evolution of Government Securities market indicators for the period of 2016-2020, it can be noticed that the volume of GS issued on the primary market is correlated with the Government' demand for financing on the internal market.

The banking sector remains the main investor in GS. The main reasons are that government securities represent an important source for obtaining reliable profits and correlate with the importance of the effective liquidity risk management for the banks.

The study also reveals a steady increase of the investors interest for T-bills with longer maturity in the last years in the context of increasing yields of GS with longer maturity.

Generally, the yields of GS are influenced by the evolution of macro indicators, like, economic growth, inflation, exchange rate, consumption, etc.. The analysis shows positive correlations between the average yield of treasury bills and both the inflation rate and the exchange rate. From the investment attractiveness point of view, the study reveals that government securities remain a more attractive source of investment compared to deposits in the banking system.

And finally, government securities have always been considered as an investment option which is suitable only for the important investors like banks or other financial institutions. However, the study shows that these securities are one of the best options for investment for common investors or retail investors as well, as they carry practically no risk of default, offer good long-term returns and are the most liquid financial instruments. In order to make the investments in government securities more attractable for common private investors, the public authorities aim at the diversification of GS sales channels with increasing access of individuals to GS purchasing and the insurance of the transparency and predictability of this market.

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