

INTERNAL GOVERNMENT DEBT OF THE REPUBLIC OF MOLDOVA: TRENDS AND PERSPECTIVES

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Abstract: *The government debt of a country represents its borrowing engagements in order to assure the financial resources necessary for implementing its functions related to the production and economic processes, social sphere and functioning of other domains of activity. At the same time, the government debt facilitates the conduct of monetary policy by public authorities aimed at maintaining a stable exchange rate of the national currency and maintaining the optimal level of inflation. Therefore, the government debt is one of the indicators and elements that characterize the financial stability of a country and is approached in different policy documents in order to assure and maintain its efficient management. In this context, this article aims to presents an analysis of the internal government debt of the Republic of Moldova for the last 4 years, its structure, evolution and trends as well as the perspectives and future plans of the Republic of Moldova's authorities in order to assure a high level of financing its needs in conditions of minimum risks. The research methods used in reflecting the obtained results are the analysis, synthesis comparison and graphic method.*

Key words: *government debt, internal government debt, government securities, primary market, treasury bills, government bonds.*

JEL CLASSIFICATION: F65, G23, G28, H63, O16

INTRODUCTION

Due to its particularities, the government debt (GD) often acts as a barometer/ indicator for economic processes. In the best of times, it relaxes the domestic constraint on savings, smooths consumption, and finances investment. Investors see it as a safe haven, as an „alpha” and as a method of portfolio diversification. In the worst of times, it is associated with debt overhangs, banking collapses, exchange-rate crises and inflationary explosions. In such circumstances, the investors see it unenforceable, illiquid and prone to messy debt workouts.

Recurrent international financial crises have highlighted the need in developing internal debt markets to reduce dependence on foreign financing and vulnerability to volatility in international capital markets. Therefore, the development of internal government debt (IGD) markets became a priority for many emerging and developing countries as highlighted by the rapid growth of these markets. Thus, the main aspects that most of the countries, including the Republic of Moldova, have payed attention on for the past decade were improving the macroeconomic fundamentals, making structural reforms, implementing better debt management practices, diversifying the investor base and developing a functional and liquid secondary market.

THE ANALYSIS OF BIBLIOGRAPHY RESOURCES RELATED TO THE SUBJECT

In researching this topic were studied different bibliography sources such as studies made by national researchers in this field, the legal framework of the Republic of Moldova related to public debt as well the reports drafted by international experts of the International Monetary Fund and the World Bank on public debt management.

DESCRIPTION OF THE RESEARCH METHODS

The applied research methods in this article consist in:

- the economic analysis method – which implies the decomposition, the breakdown of the investigated process into elements and therefore, the research of each element as part of a whole.
- the synthesis method presumes the unification in a logical and coherent manner of the fragmentary elements and of the information explored on the topic.
- the comparison method implies studying the processes and economic phenomena through a reference criterion, establishing similarities and differences.
- the graphic method used for evaluating and representing the statistical data.

THE OBTAINED RESULTS

According to the framework of the Republic of Moldova, the IGD represents the total amount of unpaid obligations and interest due and unpaid, contracted, on behalf of the Republic of Moldova, by the Government, through the Ministry of Finance, from residents of the Republic of Moldova. Government securities issued to be placed on the domestic market of the Republic of Moldova and purchased by non-residents is also attributed to the internal government debt [3].

The statistical data published by the Ministry of Finance of the Republic of Moldova, the responsible authority for the administration of the GD, show that as of June 2020 the IGD of the Republic of Moldova amounted about 26,6 billion MDL (see figure 1) and represents about 13% of the GDP and around 43% of the total government debt (GD) of the country (see figure 2).

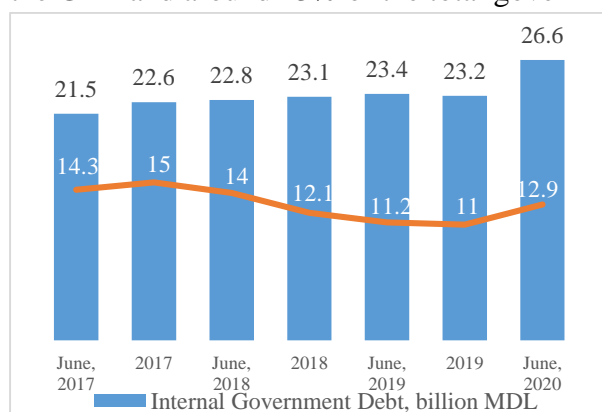


Figure 1. The amount of IGD of the Republic of Moldova for the period of 2017 – 2020

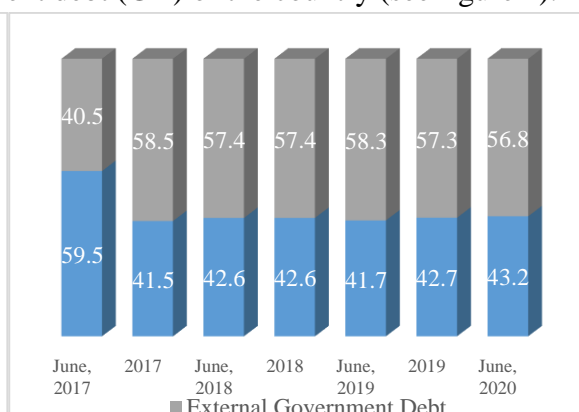


Figure 2. The structure of GD of the Republic of Moldova for the period of 2017 – 2020, %

Source: Made by author based on data provided by the Ministry of Finance [5, 6]

For the entire period, from end, 2017 to mid, 2020, the IGD represents the minor part of the GD of the Republic of Moldova. However, the IGD registered in June 2020 has the highest amount in comparison to the previous periods that are shown in the figure 1.

As instruments generating IGD, in the Republic of Moldova may be applied such financial instruments like government securities (GS) and domestic government loans (loans from commercial banks and other domestic loans). The types of GS that may be issued on the primary market in Republic of Moldova are:

- Treasury bills - short-term GS, issued at a discount and redeemed at maturity at their nominal value, with a term of circulation of up to one year (91, 182 and 364 days).
- Government bonds - long-term GS, issued at a floating or fixed interest rate. Interest on government bonds is paid periodically (quarterly/ half-yearly) in the form of coupons. Government bonds can be sold at a discount, at their nominal price or at a premium, and are redeemed at maturity at their nominal value (from 1 year to 5 years) [2, 3].

Analyzing the statistical data published by the Ministry of Finance of Moldova, may be stated that the IGD of the Republic of Moldova, according to the data presented in Figure 3, consists entirely of GS.

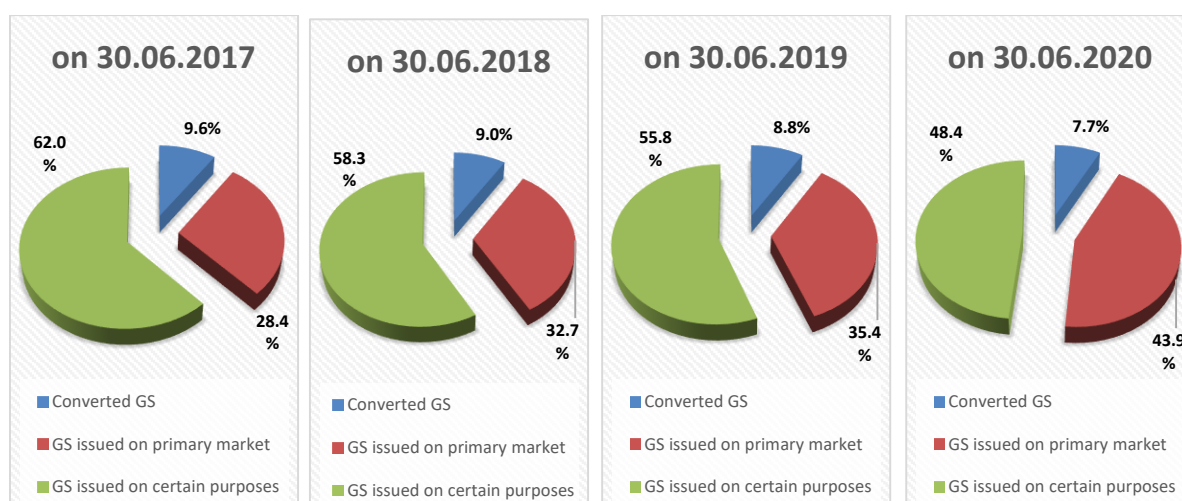


Figure 3. The structure of IGD of the Republic of Moldova in the period of June 2017– June 2020, %

Source: [2]

From the Figure 3, it can be mentioned that among the GS that form the IGD, most are GS issued for certain purposes set by law (48.4% as of June 30, 2020). These represent government bonds issued in order to execute the obligations of the Ministry of Finance of Moldova resulting from the state guarantees granted to the NBM for lending to commercial banks. On the second place, in terms of volume, are the GS issued on the primary market (about 44% as of June 30, 2020). At the same time, in 6 months of 2020 there is an increase (by 8.5 p.p.) of the share of GS issued on the primary market compared to the same period of 2019. A share of 7.7% of the total domestic government debt of Moldova are represented by converted GS, which are the GS obtained in the NBM portfolio following the conversion in 1998 and 2008 of the loans previously granted to the Government by the NBM.

Taking a closer look at IGD of the Republic of Moldova by the type of GS issued, it can be noticed that, it did not register significant changes during the analyzed period (2017-2020), and the most traded GS are represented by short-term GS (see Figure 4).

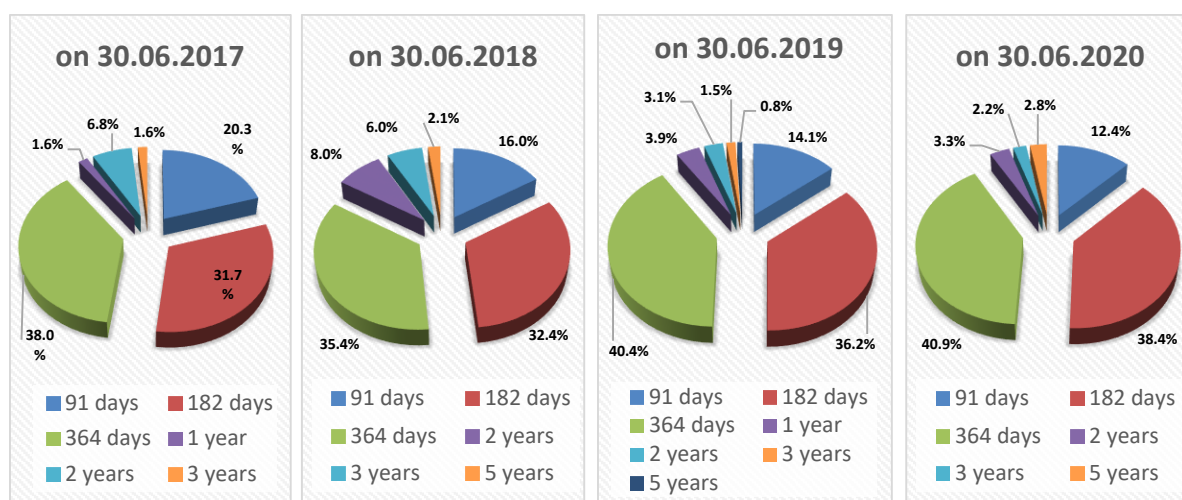


Figure 4. The GS structure sold on the primary market of the Republic of Moldova in the period of June 2017– June 2020, %

Source: [2]

Therefore, the treasury bills with a maturity of 364 days are ranked first in the category of the most requested short-term GS (approximately 41% of the total GS traded as of June 30, 2020), these being followed by those with a maturity of 182 days (about 38%) and 91 days (12%). Less requested GS, as of June 30, are government bonds with a maturity of 3 years, their share of the volume of GS traded in 6 months of 2020 being only 2.2 percent, which is an increase of 0,7 p.p. compared to the similar period of 2019, but also a significant reduction (with about 3 p.p.) compared to the period of 2017 - 2018.

An important moment to note is the fact that starting with 2018, the Ministry of Finance of the Republic of Moldova, as issuer of the GS, expanded the spectrum of proposed securities, by initiating the issuance of government bonds with a maturity of 5 years. The extension of the maturity term of the GS from 3 years to 5 years was aimed at expanding the maturity of the portfolio of government securities in circulation, as well as reducing the risk of domestic debt refinancing. As it can be seen from Figure 5, the share of government bonds with a maturity of 5 years traded in 6 months of the current year (a.2020) is relatively small, but which almost doubled compared to the similar period of the previous year.

Concerning the structure of IGD of the Republic of Moldova by the type of investors, it's important to mention that the major investor in GS is the banking sector (see figure 5).

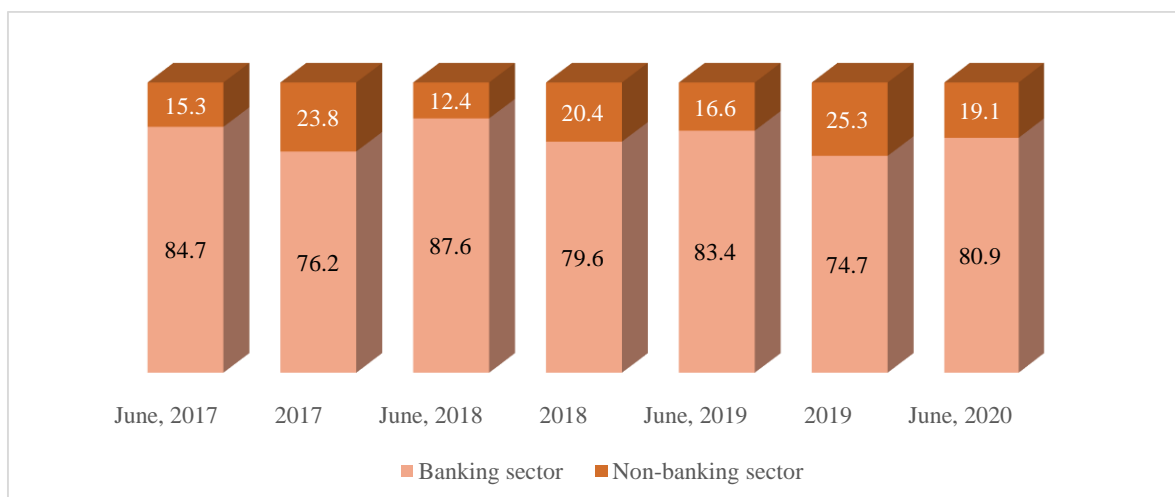


Figure 5. The IGD structure of the Republic of Moldova by the type of investors in the period of June 2017– June 2020, %

Source: Made by author, based on [6]

As of 30th of June 2020, around 81% of the GS on the primary market are hold by the banking sector, and the rest of 19% - by the nonbanking sector, which is represented by national and international investors, that may purchase GS on the primary market through primary dealers.

Besides transactions on the primary market, the GS may be sold on the secondary market as well. According to the national law, transactions on the secondary market with GS are carried out under the following conditions:

- in the case of treasury bills - they take place only outside the regulated market (Stock Exchange) and outside of the multilateral trading system, through primary dealers and other authorized institutions;

- in the case of government bonds - take place both, outside the regulated market and outside the multilateral trading system through primary dealers, as well as on the regulated market and within the multilateral trading system, in accordance with the legislation in force.

The secondary market operates on the principle of direct trading and is organized through the single E-Bond trading platform and the Single Central Depository System of securities, where the trading of GS takes place after issuance on the primary market [2]. The trading platform was launched in October 2018 and in 15 months of activity (October 2018 – December 2019) it supported 56 transactions. The liquidity rate, calculated as the ratio between the total volume of monthly transactions on the secondary market and the total volume of GS in circulation, recorded less than 1.0% in this period of time, which attests an incipient level of this market’s development.

However, on medium term, the Government of the Republic of Moldova expects to get resources for financing the budget deficit in an amount of about 6% from GDP (see table 1).

Table 1. Internal financing planned for the period of 2020 - 2022

Indicators	2020	2021	2022
GS on the primary market, % of GDP, from which:	5,8%	5,9%	6,0%
Treasury bills,%	85,0%	83,0%	80,5%
Government bonds, %	15,0%	17,0%	19,5%

Source: Made by the author based on [4]

At the same, the authorities intend to continue focusing all their efforts in developing and consolidating the internal market, both primary and secondary, by taking in the near future (till 2022) the following measures:

- the extension of the maturity of GS issued on the market and the gradual increase of the share of long-term GS in circulation;
- continuing in issuing government bonds with a maturity of: 2 years, with fixed and variable interest rate, 3 and 5 years, with fixed interest rate, and depending on market demand, the possibility of issuing government bonds with a maturity of 7 and 10 years, with a fixed interest rate;
- continuing the implementation of the E-Bond platform;
- increasing the individuals access to the purchase of GS as a tool for saving, and diversifying the channels for selling by supporting the development of a distribution program GS on electronic trading platforms.

CONCLUSIONS / RECOMMENDATIONS

Even though the IGD is the minor part of the GD of the Republic of Moldova, its instruments provided on the local market represent a significant source of financing the public needs. Also, in order to respond to the investors needs, the authorities of the Republic of Moldova are concentrating all the efforts for developing and improving the existing instruments so that the state budget balance could be covered in the necessary amount and with low risks/ costs. However, improving the debt instruments is not sufficient. Selling most of the IGD instruments to the commercial local banks, makes it dependent on this category of investors and vulnerable. Therefore, the authorities should consolidate efforts in diversifying the investor's base as well, along with the debt instruments, which would minimize the concentration risks, rise the amount of attracted financial resources and reduce the financing costs.

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