Ministry of Finance and National Bank of the Republic of Macedonia

Strategy For Development of Government Securities Market

Prepared by the members of the ***Working group for development of Government securities market***

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Summary

The Strategy For Development of Government Securities Market is a document that consolidates the efforts of the Government of the Republic of Macedonia for more efficient financing of budget liquidity gap determined by the time discrepancy of public revenues and expenditures i.e. budget deficit of the Republic of Macedonia, while supporting the development of financial markets at the same time.

The preparation of this document that envisages the realization of the short-term securities issuance project is in accordance with the 2003 Macroeconomic Policy of the Republic of Macedonia.

Strategy objectives and assessments of current capital market situation

The main emphasis in the Strategy is put on the need for extending the sources of budget deficit financing, which in turn should contribute to costs reduction on long term, and short-term financing of current expenditures; stimulation of more dynamic development of financial markets in the Republic of Macedonia; promotion of financial sector competition that should facilitate the creation of new financial instruments and products; improvement of the coordination between the fiscal and monetary policy by creating conditions for interventions via own instruments in different segments of financial markets on long term; drawing of the non-risk government securities yield curve in order to easily determine the price of other financial market instruments; creation of financial instruments adequate to the needs of institutions that should arise from the pension system reform; promotion of savings by infiltrating in the population sector etc.

At the moment, there is no system in the Republic of Macedonia for financing government needs through regular issuance of government securities. Since 1994 there have been auctions of short-term securities i.e. Central Bank bills, used as an instrument for monetary regulation. Government securities market is characterized with occasional issuances on the primary securities market, determined by the need for solving structural problems: so called old foreign exchange savings, payment to banks upon foreign exchange savings, elimination of selective credits, rehabilitation and reconstruction, and privatization of Stopanska banka a.d. Skopje later on, as well as denationalization. Considering that these bonds are issued for settling certain liabilities of the government through one-off and restricted issuances, their characteristics do not match potential investors needs (primarily long terms). Part of these securities is relatively liquid on the secondary market (through the Stock Exchange), and the government stimulates their trading by giving certain benefits.

The external debt has dominant share in *the structure of the overall public debt* of the Republic of Macedonia, which includes the issued bonds. Regarding the fact that major part of bonds issued by the government are denominated in foreign currency i.e. Euros, it can be concluded that the major part of the public debt of the country consists of liabilities in foreign currency which puts in risk the balance of payments of the country.

In conditions of undeveloped government securities market, the shift towards domestic sources for financing public debt can be difficult, and therefore, the development of government securities market is necessary not only for stimulating financial markets development, but also for *efficient public debt servicing,* to the end of maintaining macroeconomic stability.

Activities for development of primary and secondary securities market

To the end of implementing the shot-term securities issuance project, legislative regulation in the area of short-term securities trading will be completed and institutional framework of public debt management will be established. The plan is to adopt an act on over-the-counter trading, amend the bylaws, elaborate procedures on primary and secondary short-term government securities trading, create system for settlement of transactions with government securities in the Central Securities Depositary enabling settlement of the transactions in the course of the same day.

Development of the *primary government securities market* will be based on market principles when covering budget deficits, which include ***flexible and competitive determining of interest rates.*** Having in mind the confidence level of potential investors (banks, non-banking financial institutions, non-financial sector companies, individual investors - households), as well as their financial power, at the beginning we will start by issuing government securities ***with 3 months maturity period in domestic currency***. We will gradually extend the maturity period of government securities depending on how successful the government will be in gaining greater confidence of the potential investors and in line with economic development of the country, particularly development of institutional investors (insurance companies, private pension and investment funds).

Regarding the government securities sales techniques, priority is given to **auction sale** in the Republic of Macedonia. This is due to the fact that at the beginning **banks are expected to be dominant investors in government securities**, and they have greater knowledge of auction mechanism and prefer market-based interest rates. So far banks have actively participated in Central Bank bills auctions, which contributed to gaining experience in the functioning of the auction mechanism. The active participation of legal entities and physical persons on the Central Bank bills auctions through banks during the past two years is also in favor of the auction sale.

Referring to the selection of the type of tender for auction sale of government securities in the Republic of Macedonia, we plan to begin with the **American type of auction**. Main reason for selecting this type of tender is because the banks and their clients have knowledge about this type of auction compared to uniform price tender, resulting from their participation on Central Bank bills auctions where American type of auction is applied. Moreover, in conditions of existing difficulties for predicting the demand for government securities, the implementation of the Dutch type of auction may lead to accepting lower uniform price, meaning higher costs for the government. Nevertheless, this does not mean that the Dutch type of auction should not be applied at all, rather its adoption would be more adequate in the later phases of market development after the demand for government securities stabilizes on a certain level, which will enable utilization of the advantages from decreased uncertainty in interest rates movement.

Banks in the Republic of Macedonia will ***directly participate*** on the government securities auctions, while other participants can submit bids for purchasing government securities through the banks.

Due to the difficulties for determining the precise amounts for each individual auction, at the beginning of short-term securities issuing, the Republic of Macedonia will announce semiannual auction calendar that will set quarterly amounts for sale of government securities, whereby the precise amount for each auction will be announced several days prior to the action. At the same time, in order to ensure stability in the supply, there will be no large fluctuations in determining the amount of securities for each auction, which is of particular importance for maintaining the interest of investors in government securities. The support of ***the secondary government securities market*** development will be taken into account while setting the frequency of auctions.

The development of the secondary government securities market depends on creation of competitive market infrastructure. Practice shows that over-the-counter markets provide much more competitiveness in securities trading than institutional markets, such as the Macedonian Long-term Securities Stock Exchange and Money and Short-term Securities Market in our country. It is very important for the investors the time settlement of concluded transactions to be carried out on the same day (t+0) by transferring securities ownership at the same time with the payment, which in general is provided by non-institutional markets i.e. over-the-counter markets.

Coordination between monetary and fiscal policy will exist for successful development of government securities market, as a result of the need to achieve mutually consistent targets aiming at the main economic policy objectives (price stability, sustainable economic growth, full employment, etc).

Central Bank of the Republic of Macedonia will be the government's agent with respect to the government securities issuance, which will contribute to further facilitation of the coordination between monetary and fiscal policy. To prevent short-term securities markets fragmenting in conditions of parallel existence of Central Bank bills and T-bills, the Central Bank will continue to issue securities with maturity period of up to 1 month, and thereby easily manage liquidity level and interest rates of the banking system. At the same time, government securities will be issued with longer maturity periods (three months and longer) and in amounts matching the budget needs and possibilities. This way, Central Bank's efforts to achieve the ultimate goal of monetary policy will be focused on markets with very short terms, and the Ministry of Finance can gradually prolong the term for covering budget deficits.

A Committee for coordination of the public debt management, monetary and foreign exchange policy will be established, which will discus and decide on the activities to be undertaken for further development of primary and secondary government securities market.

An Action Plan was drafted for implementation of the objectives and activities set in the Strategy, and it is an integral part of the Strategy.

1. Introduction

The Strategy for Development of Government Securities Market is a **document** summarizing the efforts of the Government to better finance budget liquidity gap conditioned by time discrepancy of public revenues and expenditures, i.e. the budget deficit of the Republic of Macedonia, simultaneously supporting the development of financial markets.

The preparation of this document is in accordance with the **2003 Macroeconomic Policy of the Republic of Macedonia**, underlining the importance of financial markets development as a significant precondition for intensifying the economic growth. Simultaneously, this Strategy supports the realization of the objectives of the **Public Debt Management Strategy**, where the following objectives are underlined as most significant: providing necessary financial resources for country development, reducing the expenses for servicing public debt on long term and developing financial markets in the Republic of Macedonia.

Main emphasis in the Strategy has been placed on market financing of budget expenditures and development of government securities market, and development of financial markets in the Republic of Macedonia in general. Thereby, market determination of interest rates on issued government securities and coverage of broad circle of investors are the basic market principals, on the adherence to which the realization of this Strategy objective depends, directed towards development of government securities market.

The Strategy reviews the current conditions on the primary and secondary government securities market, as well as the conditions of the external and the domestic debt of the country, thus helping to explain the need for its development. Thereby, it underlines the basic preconditions and reasons for development of government securities market, as well as the risks related to the financing of government needs by issuing securities.

Taking into account the significance of having clear legal regulation for supporting the development of government securities market, the Strategy pays special attention to the legal framework for issue of and trading with government securities, simultaneously, this part encompasses the issue of institutional framework for public debt management as well.

Taking into consideration the initial stage of development of government securities market in the Republic of Macedonia, this Strategy is especially focused on the development of primary government securities market. Thereby, key elements for establishing developed government securities market are considered to be proper choice of financial instruments, coverage of broad circle of potential investors and choice of adequate sales techniques. This Strategy also identifies the activities to be undertaken to the end of developing secondary government securities market. Finally, it considers the necessary coordination arrangement between the monetary and the fiscal policy in direction of distinguishing the instruments and creating forms of cooperation for information sharing to the end of achieving the common objective - development of government securities market.

2. Objectives of the Strategy for development of government securities market

The primary objective of this Strategy is **development of primary and secondary government securities market**, which, consequently, should enable **more efficient financing of budget needs on short term** (smooth current financing of public expenditures) **and on long term,** (providing long-term financial resources for supporting the development of the economy). Thereby, at the beginning, the efforts will be focused on developing short-term government securities market to the end of more efficient liquidity management of the budget, the time limit of which will be gradually extended depending on the country's success in gaining the confidence of potential investors and developing institutional investors. The realization of this objective will enable **market financing of the Budget deficit in domestic currency and at the same time decreasing the macroeconomic risk related to the external financing.** Besides this key objective, the Strategy is focused to achieving the following significant objectives:

- Fostering more dynamic financial market development in the Republic of Macedonia;
- Expanding the budget deficit financing sources that should contribute to long-term cost reduction;
- Promoting competition in the financial sector that should contribute to creation of new financial instruments and products;
- Increasing the operational independence of the central bank and facilitating the implementation of the monetary policy via creating conditions for further development of market-oriented monetary instruments, meaning implementation of real flexible open market operations;
- Improving the coordination between fiscal and monetary policy via creating conditions for intervening in different financial market segments (primary and secondary, respectively) on long term;
- Outlining the yield curve from zero-risk government securities to the end of determining the price of other financial market instruments more easily;
- Creating financial instruments adequate to the needs of institutions to emerge from pension system reform;
- Promoting the saving via inclusion of the population;

P Better education of the public regarding financial market importance for economic development.

3. Current conditions

3.1 Government securities market

Primary feature of the government securities market in the Republic of Macedonia is **inexistence of continuous primary market**, contributing to lagging of financial market development in the Republic of Macedonia behind the ones in the countries in transition. So far, the Republic of Macedonia has not introduced a system of financing government needs via regular issues of securities. What exist in this country since 1994 are auctions of Central Bank bills, used as monetary regulation instruments.

The inexistence of a continuous primary government market is determined by number of factors, as follows:

- funds for servicing the external government debt were primarily provided via new borrowing at the international financial institutions and via credit from the National Bank of the Republic of Macedonia;
- the receipts realized from the sale of socially-owned enterprises were a significant source for financing public expenditures;
- until 2001, the treasury system, as system for efficient management with public financial resources was absent;
- the cash rationing system (non-timely payment of the due liabilities) was used when executing the public expenditures etc.

Occasional presence of the Government on the primary market was determined by the need to solve the problem with the so called old foreign exchange saving, payment to the banks upon the old foreign exchange saving, elimination of selective credits, rehabilitation and reconstruction, and later on, privatization of Stopanska Banka AD Skopje, as well as denationalization (*Table 1*).

Table 1. Bonds currently issued in the Republic of Macedonia

(in millions of euros)

Purpose	Year of issuance	Issued amount	First payment	Last payment	Maturity (years)	Annual interest rate (%)	Payment of principal	Payment of interest	Debt condition-end of 2002	Debt condition-end of 2003
Restructuring of Stopanska banka	1996	75.0	1996	2010	15	Discount rate	1 of April	Every month	42.7	37.4
Selective credits	1996	17.03		2020	25	No interest	-	-	17.03	17.03
Foreign exchange saving deposits	2000	546.5	2002	2011	10	2	1 of April and 1 of October	1 of April and 1 of October	494.2	430.7
Privatization of Stopanska banka	2001	120.1	2001	2014	14	3-month euribor + 1percentage point	31 of March 30 of June 30 of September 31 of December	31 of March 30 of June 30 of September 31 of December	111.5	105.1
Denationalization (first issue)	2002	2.1	2003	2012	10	2	1of June	1of June	2.1	1.5
Denationalization (second issue)	2003	39	2004	2013	10	2	1of June	1of June		39.0
Total:		**799.73**							**667.53**	**630.73**

Source: Ministry of Finance of the Republic of Macedonia

Table 2. Trading with government securities on the secondary market in the first half of 2003

Month	Bonds of the Republic of Macedonia for "old foreign exchange savings"			Bonds of the Republic of Macedonia for denationalization - first issue			Bonds of the Republic of Macedonia for denationalization - second issue			Share of all bonds in total sale
	Sale (in denars)	Average price	Share in total sale	Sale (in denars)	Average price	Share in total sale	Sale (in denars)	Average price	Share in total sale	
January	20.395.912	61,42	19,7	573.571	58,70	0,5				20,3
February	35.496.869	61,06	32,4	11.485.537	58,61	10,5				42,9
March	33.511.397	63,74	17,3	3.299.197	62,03	1,7	17.409.582	52,29	9,0	28,1
April	14.529.174	57,16	6,15	141.976	55,15	0,06	116.844.049	50,78	49,4	55,6
May	25.636.428	59,29	17,3	1.965.363	60,00	1,33	69.668.611	56,49	47,2	65,9
June	68.873.878	63,77	28,8	1.957.778	58,11	0,81	97.946.709	59,14	41,0	70,6

Source: Bulletins of the Macedonian Stock Exchange A.D. Skopje

Regarding the fact that these bonds were issued to settle certain government liabilities, their characteristic do not match the needs of the potential investors (above all, long maturity period). Small part of these securities is relatively liquid on the secondary market (Stock Exchange) and their trading is stimulated by the government via extending certain privileges (*Table 2*).

3.2 Public debt of the Republic of Macedonia

Public debt covers all financial liabilities of the government towards domestic and foreign creditors, i.e. the external and the domestic debt of the government. Although there is no universal definition, there is a consensus among the economists that the appropriate level of the total debt-to-GDP ratio is the one that: a) does not reduce the flexibility and solvency of the fiscal policy, b) does not increase the share of debt repayment in the budget deficit, c) does not have adverse effect on the expectations on the financial markets and d) does not put pressure on the real interest rates of commercial banks. According to Maastricht criteria, the total debt of each EMU member state should not exceed 60% of GDP. On December 31, 2002, the total public debt (domestic and external)[1] of the Republic of Macedonia amounts to US$ 2.2 billion or 59% of GDP.

3.2.1 Domestic debt

Domestic debt of the Republic of Macedonia refers to liabilities on the following basis:

- Bond for taking over claims from Stopanska Banka due to privatization (new bond);
- Bond issued for rehabilitation of Stopanska Banka (big bond);
- Old frozen foreign exchange deposits bond;
- Denationalization bonds;
- Liabilities on the basis of utilized long-term credit from the National Bank of the Republic of Macedonia; and
- Issued guarantees for the benefit of legal entities that have utilized credits from domestic commercial banks - domestic guarantees;

The priority of the Republic of Macedonia is to regularly service its liabilities on the basis of issued bonds in the country and utilized credits from domestic institutions. Each year, the funds for settling the domestic debt are planned in the Budget, and further on, they are settled on regular basis. Thus, on December 31, 2002, the domestic debt amounted to EUR 667 million, i.e. US$ 655 million and its share in the total debt is 29.7%.

[1] Total public debt was calculated as a sum of external debt and total issued bonds and credit towards the National Bank of the Republic of Macedonia.

3.2.2 External Debt

The total external debt of the Republic of Macedonia is consisted of liabilities of the Government of the Republic of Macedonia towards foreign multilateral, bilateral and private creditors on the basis of used short-term, medium-term and long-term loans and credits, and it also includes public sector and domestic private legal entities.

External debt of the Republic of Macedonia (public and private), as of December 31, 2002 amounted to US$ 1,517.67 million.[1]

The long-term debt as of December 31, 2002 is result of the realized new borrowing, debt servicing and exchange rates differences.

External debt structure by creditors

The major part of the external debt of the Republic of Macedonia is consisted of debt to the Paris Club of Creditors and London Club of Creditors as well as the debt to IDA (International Development Association), which is a multilateral creditor.

1.	**OFFICIAL CREDITORS**	**1.048,15**
1.1	**MULTILATERAL CREDITORS**	**756,01**
1.1.1	IMF	67,39
1.1.2	IBRD/IDA	440,65
1.1.3	IFC	17,86
1.1.4	European Investment bank	102,13
1.1.5	EUROFIMA	11,96
1.1.6	Bank of Development by European Council	14,50
1.1.7	EBRD	57,00
1.1.8	EU	64,62
1.1.9	IFAD	5,20
1.2	**BILATERAL CREDITORS**	**292,14**
1.2.1	Paris Club of creditors[2]	227,86
1.2.2	Other Bilateral creditors	64,28
1.3	**PRIVATE CREDITORS**	**469,52**
1.3.1	London Club "NFS" from 1997	253,77
1.3.2	Other private creditors	215,75
	TOTAL:	**1.517,67**

The structure of the external debt of the Republic of Macedonia shows that the largest part of the debt refers to liabilities toward bilateral creditors - Paris Club (15% of the total external debt) and London club of Creditors (17% of the total external debt), which is part of the debt inherited from former Yugoslav Federation.

STRUCTURE OF THE EXTERNAL DEBT BY CREDITORS
AS OF 31.12.2002, DENAR MILLION

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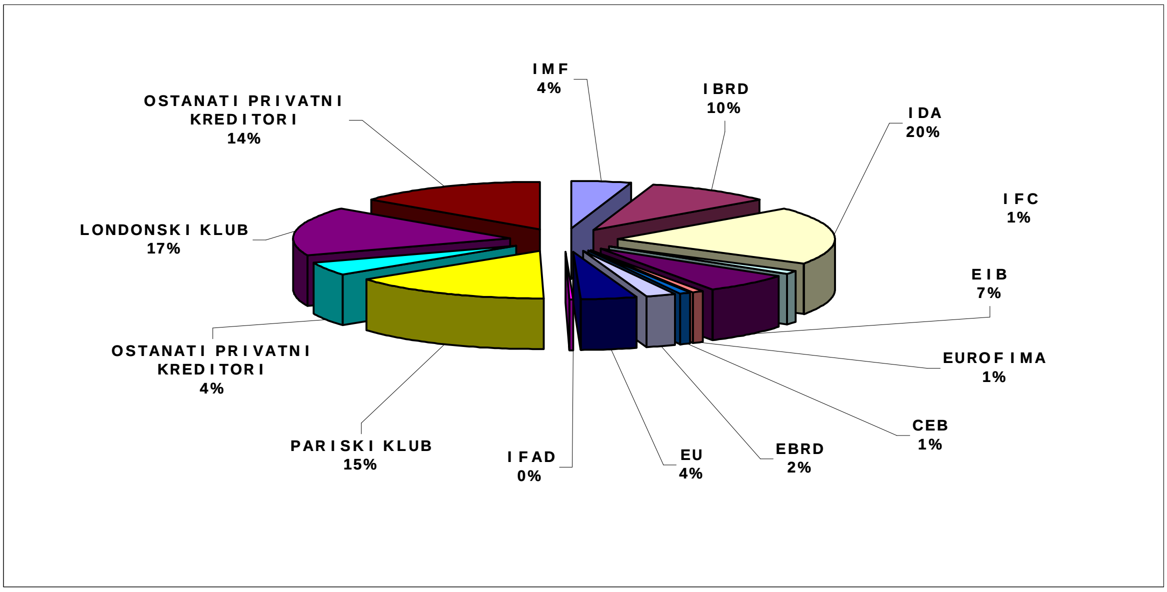
[1] Short term, medium-term and long term external debt.

[2] The balance of the debt toward Paris club of creditors does not include the amount of the debt toward four PC countries (France, USA, Japan and Kuwait), with which no agreements upon the Reprogram 2000 have been made, yet.



Structure of the external debt by maturity

The orientation towards borrowing from multilateral creditors and the reprogramming of the liabilities towards the Paris and London Club of Creditors have led to relatively favourable maturity structure of the external debt of the Republic of Macedonia. The major part in the debt i.e. about two thirds have credits with maturity period over 10 years, followed by credits with repayment period of 6 to 10 years, and liabilities with maturity period between 1 and 5 years.

Level of indebtedness

According to the international standards for defining the level of indebtedness and on the basis of the indicator share in the total external debt (long-, medium- and short-term) in the gross domestic product (average in the last three years), which in 2002 amounted to 45.2%, the Republic of Macedonia is among the medium to moderately indebted economies.

The total external debt regarding export of goods and services (average in the last three years) is 118.1%, total servicing of debts regarding export of goods and services (average in the last three years) is 17.2%, and the repayments of interest are 3.9%. According to these three criteria, the Macedonian economy is in the group of low indebted countries. The level of indebtedness ranges within tolerant frames, and compared to the appropriate indicators of the other transitional economies, the indebtedness is on satisfactory level. However, when following the indebtedness with the export indicators, one should take into account separate specificities of Macedonian export. In fact, large share of export goes to inward processing relief operations, whereby the real value of export is significantly lower. Also, significant part of the claims is realized with compensation activities. If the level of indebtedness were calculated only with the effective foreign currency inflow from the export of goods and services, it would be higher.

Level of indebtedness of the Republic of Macedonia

According to several criteria							
Total external debt (% of GDP)		Total external debt (% of export of goods and services)		Debt servicing (% of export of goods and services)		Repayment of principal (% of export of goods and services)	
2001	2002	2001	2002	2001	2002	2001	2002
42.3	45.2	107.9	118.1	14.7	17.2	4.4	3.9

Source: National Bank of the Republic of Macedonia

The standards for defining the level of indebtedness, and on that basis the classification of the country in certain group of countries, are given separately for each indicator as follows:

- Total external debt to average gross domestic product in the last three years, high indebtedness over 50%; moderate indebtedness means 60% of the limit value (50%), but not reaching the critical level being the interval between 30-50%; and lower indebtedness below 30%.

- Total external debt to average export of goods and services in the last three years, high indebtedness over 275%; moderate indebtedness means 60% of the limit value (275%), but not reaching the critical level being the interval between 165-275%; and lower indebtedness below 165%.

- Servicing the debt to average export of goods and services in the last three years, high indebtedness over 30%; moderate indebtedness means 60% of the limit value (30%), but not reaching the critical level being the interval between 18-30%; and lower indebtedness below 18%.

- Repayment of interest to average export of goods and services in the last three years, high indebtedness over 20%; moderate indebtedness means 60% of the limit value (20%), but not reaching the critical level being the interval between 12-20%; and lower indebtedness below 12%.

According to the World Bank recommendations, if three out of four indicators are within given interval, the country is classified in the appropriate group of countries. However, note that the approximation to the critical level, i.e. limit value of certain indicator should be interpreted very carefully, given the fact that when moving from one to another group of countries, one should take into account the movement in the previous period, not only in the current period.

4. Basic prerequisites for successful development of the government securities market

The development of government securities market must be seen as **dynamic process**, in which **stability** of the macroeconomic and financial system is the most important when creating an efficient market and establishing the Government's credibility as issuer of securities. Prerequisites to be met for establishing efficient market for securities denominated in domestic currency are stable government with high credibility, firm fiscal and monetary policy, efficient legal, tax, and regulatory infrastructure, safe debt repayment arrangements, and liberalized financial system with competitive mediators and certain level of treasury system development.

Maintenance of the macroeconomic balance and stability of the national economy was one of the main priorities of the Republic of Macedonia. In the Republic of Macedonia, the macroeconomic stability is, above all, result of the price stability, stable Denar exchange rate, more harmonized relations in the trade balance and the balance of payments and the sustainability of the fiscal position on medium term. In addition, in the last decade, there has been a qualitative improvement of the reform processes, contributing to the revival of the economic activity in the Republic of Macedonia.

Although the Republic of Macedonia was exposed to transition process and the changes realized in the fiscal, monetary, financial, tax and customs system, foreign trade system, the macroeconomic stability was maintained.

(Table 3)

BASIC MACROECONOMIC INDICATORS

	1999	**2000**	**2001**	**2002**	**2003**	**2004**
				Estimation	***Forecast***	***Forecast***
Real sector						
Gross domestic product						
- Real growth	4.3	4.5	-4.5	0.7	2.75	4.0
-Current prices, million of denars	209,010	236,389	233,841	241,243	252,242	266,393
-Millions USA dollars	3730	3899	3437	3727	4627	4982
Inflation (CPI, average)	0.7	5.8	5.5	1.8	1.75	3.0
Wage (monthly average, net)						
- Nominal growth	2.9	5.5	3.5	6.9	3.9	3.5
- Real growth	3.6	-0.3	-1.7	4.5	2.1	2
Unemployment rate (LFS)	32.4	32.1	30.5	31.9	30.4	29.0
Fiscal sector				*(% of GDP)*		
Revenues of central budget	22.6	24.5	22.2	23.8	22.1	21.3
Expenditures of central budget	21.8	21.8	28	29.2	23.5	22.2
Budget deficit/surplus	0.8	2.7	-5.8	-5.4	-1.4	-0.9

External sector						
Export (FOB) (growth rate)	-7.9	11.0	-12.5	-3.7	21.7	6.6
Import (FOB) (growth rate)	-6.7	19.3	-16.6	12	13.1	3.7
Trade balance (US$ million)	-496	-690	-521	-765	-769	-759
Trade balance (% of GDP)	-13.3	-17.7	-15.2	-20.5	-16.6	-15.2
Current account, balance (US$ million)	-32.5	-75.3	-235.4	-321.0	-292	-347
Current account (% of GDP)	-0.9	-2.1	-6.8	-8.6	-6.3	-7.0
Foreign exchange reserves (US$ million)	450	700	756	735	816	839
Foreign exchange reserves (monthly coverage of import)	2.4	4.3	4.2	3.6	3.9	3.9
External debt (US$ million) (end-period)	1438	1438	1444	1549	1650	1697
External debt (% of GDP)	38.6	36.9	42.0	41.6	35.7	34.1
Foreign direct investments (US$ million)	32	175	443	78	105	120
Monetary sector						
Credit to private sector (nominal growth rate)	9.4	17.2	7.3	9.9	9.5	7.2

Source: State Statistics Bureau, Ministry of Finance and NBRM.

Since the independence, continuous reform has been implemented in the financial system (from the aspect of regulation, ownership, corporate governance, market operations principle), which gradually started to yield obvious results. The financial system in the Republic of Macedonia currently consists of the following financial institutions: banks, savings houses, Macedonian Long-Term Securities Stock Exchange, brokerage houses, insurance companies and leasing companies, and capital funded pension funds and investment funds will be added in near future.

Banking sector is the most developed segment of all financial segments in the Republic of Macedonia. By December 2002 inclusive, the banking sector in the Republic of Macedonia comprised

21 universal type banks and 17 savings houses. Taking into account the functions they perform and the share of 99% they have in the overall financial potential, the banks represent almost the whole Macedonian banking system. In addition to the other banking operations, the banks have a possibility to participate in the capital market by issuance of their own securities and intermediation in the securities operations of other entities.

Capital market in the Republic of Macedonia is relatively new segment, however, compared to the markets in the region, it is quite developed. In 1992, Securities and Exchange Commission was established. The Macedonian Long-Term Securities Stock Exchange was established in 1995, and on December 31st 2002, the newly established institution - Central Securities Depositary - started operating.

The trading of securities, which are in dematerialized form, is conducted via the first - official, and the second - unofficial market on the Macedonian Long-Term Securities Stock Exchange. So far, there are total of 97 joint stock companies listed on the Stock Exchange, the shares of which are put on sale, being an exceptional success for a small economy.

The issuance of government bonds contributes to greater development of capital market. The bonds provided great activity and new moments and possibilities on the capital market.

Following the trends of merger and globalization of financial institutions in 2003, the projects for bilateral connections of the Macedonian Long-Term Securities Stock Exchange continue.

One of the most significant reforms in the fiscal part, i.e. in the part of public finance management is the **implementation of the Treasury system** in 2001. The term "Treasury system" is a sum of government functions directed towards provision of an efficient financial management of the public financial resources, fiscal discipline and earmarked and transparent public spending. The functions through which these objectives are realized are: budget execution (payment operations for the needs of the Budget institutions), public revenue management, budget accounting, debt management, liquidity management etc.

One of the most significant Treasury functions in general, and especially in context of government securities market is the cash management, i.e. planning and management of the public resource liquidity. A developed liquidity planning system is necessary for the following:

- Smooth financing of the public expenditures during the whole fiscal year;
- Avoiding the situation of accumulating outstanding liabilities;

- Avoiding liquidity shocks in the economy;
- Minimizing the price of the sources for financing the Budget needs;
- Maximizing the return of the temporarily free funds;
- Achieving the basic goals of the Budgetary policy, i.e. achieving the planned economic targets;
- Promotion of the coordination between the fiscal and monetary policy for the benefit of the overall macroeconomic policy.

The significance of this function is especially emphasized in the smaller economies, where the government is a very significant market entity, i.e. the economic tendencies in general depend on its expansive or restrictive policy.

With the implementation of the Treasury system reform in the Republic of Macedonia in 2001, i.e. with the implementation of the key Treasury functions, pre-conditions were created for efficient public revenues and expenditures management. The function liquidity management was implemented by abandoning the concept *ad-hoc* financing and putting more emphasis on the planned approach of the Budget institutions operations. In this sense, appropriate procedures were introduced: planning Budget allocations at a monthly level, planning more significant expenditures at a weekly basis, providing records of the commitments undertaken by the Budget users (including their maturity date), an obligation for informing about expected inflow for all revenues independently on their source etc.

The consolidation of all public financial resources within a single Treasury Account ("Single Treasury Account" concept) played a significant role for the development of this function. The consolidation enabled centralized monitoring and control of all Budget revenues and revenues of the Budget institutions, as well as Budget expenditures and expenditures of the Budget institutions.

In conditions of an emphasized planned approach in the usage of the public resources by the Budget institutions, as well as in conditions of consolidated funds, it is enabled to commence with regular projections of the Budget liquidity and the other inflows and outflows realized by the Budget institutions. It is a tendency and necessity for the short-term liquidity projections (weekly projections) to become monthly, quarterly and annual. The continuation of the temporal horizon is a necessity to the end of conducting efficient government policies with respect to the type, maturity and amount of the funds necessary for financing the budget needs in short and long term.

It is not possible to develop the government securities market in the absence of a quality financial planning. The development level attained by the Treasury in the Republic of Macedonia provides more active role of the government on the government securities market (determining strategic directions for borrowing, usage and choice of new, appropriate instruments, determining sustainable level of issuance, risk assessment etc).

5. Basic reasons for developing government securities market

Basic reasons for developing government securities market in the Republic of Macedonia are the following:

- **More efficient financing of the budget needs on short and long term**. The efficient of the budget needs in short term means unobstructed execution of the budget expenditures in order to perform the government function and to avoid a situation of accumulating arrears. The failure to settle the outstanding liabilities on time adversely affects the credibility of the government-debtor. Likewise, the failure to settle government liabilities may also have social consequences (transfers in the social area, payment of pensions, transfers for child allowances etc.) The application of the government securities as an instrument for amortization of short-term discrepancies between the public revenues and public expenditures, i.e. as an instrument for timely provision of funds, will have a key influence for the realization of what was mentioned before. The efficient financing of the budget needs in long term means provision of financial resources for financing the public capital projects that have direct influence on the economy development, for refinancing the existing debt, etc.

- The **indebtedness** of the country is increasing, thus increasing the percentage share of the public debt in the gross domestic product. The Republic of Macedonia reached the limit of public debt to GDP ratio, pursuant to the Maastricht criteria, in 1999 (60.8%[6]), followed by its insignificant reduction. However, the unfavorable security situation in 2001, which led to decrease of the economic activity and expansion of the budget expenditures, as well as the obligations undertaken under the Framework Agreement, can again accelerate the increasing trend of the country indebtedness. Significant excess of the set limit applied in the EU member states can impede the external financing of public debt, which covers about two-thirds of the total public debt, thus having adverse effect on the macroeconomic stability. Thereby, in conditions of undeveloped government securities market, the movement towards domestic sources of financing of public debt would be obstructed.

- Undeveloped government securities markets are **obstacle for further development of market-oriented instruments of monetary policy**. After the monetary independence of the Republic of Macedonia, numerous activities were undertaken to the end of paving the way leading towards full

[6] Source: Public Debt Management Strategy - Ministry of Finance of the Republic of Macedonia, 2001

utilization of indirect monetary instruments. The evolution towards indirect, market-oriented instruments of monetary regulation was hindered by the absence of government securities, commercial securities, sound financial institutions and deep and transparent financial markets. However, the National Bank of the Republic of Macedonia abandoned the usage of direct monetary instruments at the beginning of 2000, thus reflecting the general tendency of the economy towards increasing the role of the market signals and introducing market institutions and instruments. In the past several years, due to the existence of structural excess of liquidity in the banking system, basic instrument for monetary regulation is issuance of Central Bank bills. This instrument, together with the auction of credits and foreign currency swap operations, is in the group of open market operations, which are part of the monetary instrument set of the National Bank of the Republic of Macedonia, as well as of other countries with undeveloped financial markets. Further development of the monetary instruments and the possibility to apply flexible open market operations will depend on the development of government securities market, such securities being risk-free financial instrument for efficient implementation of the monetary interventions.

- With the planned pension system reform, a multi-pillar pension system will start functioning, thus raising the issue of investing the funds collected on the basis of pension insurance contributions in the new Fund, on one hand, and covering the deficit in the existing Pension Fund, on the other.[3] The successful resolution of this problem will largely depend on the development of the government securities market, which should create financial instruments adequate to the needs of these institutions. Otherwise, we could face an outflow of capital on the basis of collected pension insurance contributions due to investments in safer and more profitable instruments outside the country.

- The development of **investment funds** is impeded. At the beginning of 2000, the Law on Investment Funds was enacted. It was prepared according to West European principles and standards, and harmonized with the Directive on Collective Investment in Negotiable Securities. Three years after the institutional framework was established, there has not been any investment fund on the financial market of the Republic of Macedonia, despite all expectations. One of the main reasons is the absence of developed government securities market, since such securities, being risk-free instruments, have a significant share in the portfolio of investment funds.

6. Risks connected with the government securities issuance and with the public debt management in general

1. Risk of refinancing

[3] The planned pension system reform will cause a deficit in the existing Fund since 7% of the funds collected on the basis of pension insurance contributions, currently paid to the existing Fund, will be gathered into the new Pension Funds.

Risk of refinancing refers to risks related to time of debt repayment, availability of funds for debt repayment and costs related to the need for new borrowing.

Risk of refinancing increases when high amounts of debt and other repayments mature at the same time. Therefore, it is important for the debt to be distributed as equally as possible and to avoid concentration of liabilities at the same period. The introduction of the government securities will create for the Republic of Macedonia a possibility for reduction of the shocks caused by the concentration of the liabilities in certain months of the year. The objective of the public debt management policy will be gradual orientation towards the capital markets and private creditors and greater share of the debt expressed in government securities. In order to achieve this, it is necessary to pay more attention to the financial needs planning[7].

2. Risk connected with the debt amount

Usually, while this type of risk is assessed, the considerations are in direction whether the debt amount may create conditions for disturbing the financial stability. For a country in which the debt is relatively big and has a tendency of permanent increase, it is logical for the analysis to be directed towards determining the level to which the debt must be reduced. The most appropriate indicator that is applied is the share of the debt in the gross domestic product. The policies connected with the management of this type of risk should be directed towards maintenance of sustainable budget deficit level.

3. *Market risk*

The market risk refers to the risk of change in the exchange rates and the interest rates on the domestic and international capital market. The market risk is especially dangerous in the case when the major part of the debt is foreign currency denominated. Therefore, the policy should be directed towards reduction of the foreign debt share in the overall debt by early repayment of part of the liabilities and refinancing a part of the due foreign debt with domestic debt. Instrument for this are the government securities with fixed price (interest) that can be used simultaneously for promotion of the domestic savings and financial markets development.

4. Liquidity risk

[7] A precondition for successful financial needs planning is the existence of the concentration of the competences with respect to the total government debt management in one institution.

The liquidity risk is connected with the possibility for synchronizing the short-term liabilities with the funds necessary for their financing. **The fiscal reserve** (compulsory minimal amount of funds deposited at the government account) is applied as instrument for reducing this type of risk, thus preventing the government as a creditor to come to a situation not to be able to pay its liabilities on time by which its credibility would be disturbed. Here, there is again need for precise projecting of budget liquidity.

The above-mentioned risks do not exhaust the analysis of the debt-connected problems, but they provide basis for setting priorities for the debt management. Moreover, the risk structures of the public debt are often connected with the inappropriate macroeconomic policies - fiscal, monetary and foreign exchange policy whereby there is a cause-consequence connection.

7. Legal and institutional framework

One of the main preconditions for faster development of the government securities market is clear definition of the legal, regulatory and supervisory framework. The basic parts of the legislation that support the efficient securities market include: explicit authorization of the government to borrow; budget rules for government securities issuance, rules for organization of the primary market; the role of the central bank; the public debt management policy; the rules for issuance of government securities and rules that will govern the functioning of the secondary market. The legal framework defines the encouragements for all market participants - the government as an issuer, central bank, regulatory agencies, market intermediaries and investors. The legal framework must define the rights and obligations of the parties (the issuer, investor and intermediaries) included in the trading of securities on the primary and secondary market.

From a point of view of the **primary market,** it is required for the government to introduce the principles of equality and publicity. The government introduces rules by which it will provide equal access (to everybody interested that wants to buy government securities) and fair competition. The principle of publicity means openness of the government to the future transactions with government securities, with respect to timely informing about the time schedule of the auctions, the amounts of the issuances and their maturity.

From a point of view of the **secondary market**, the government usually regulates the following 3 objectives: (1) provision of fair, efficient and transparent market, (2) minimizing the systemic risk, and (3) protection of the investors and financial service beneficiaries. The primary objective is protection against inappropriate trading practices such as market manipulation and insider trading. In order to provide fair and transparent market, it is necessary for the information that will affect the prices to be available to all market participants at the same time. In order to reduce the systemic risk, it is necessary to meet some requirements such as safe systems for clearing of the transactions, internal controls and supervision and meeting the minimum capital requirement by the market intermediaries. The investor protection, in some European Union countries is provided through the counterpart schemes that serve as protection against fraud and negligence.

The legal basis for borrowing in the Republic of Macedonia is determined in the **Law on Budgets** ("Official Gazette of the RM" No. 79/93, 3/94, 71/96, 46/2000, 11/01, 93/01, 46/02, 24/03) in which the framework and the principles for taking loans and issuing guarantees to the public sector are determined.

According to the Law on Budgets, the budget document determines the limit of the annual increase of the total current debt, and for covering the budget deficit. Likewise, the Law determines that funds for repayment of the principals and interests due during the fiscal year are provided from the government budget for the current year on the basis of the previously concluded contracts.

The debt can take form of a **loan, bonds** or **treasury bills.** According to the Law on Budgets only the Government has right to take loans from legal and physical persons from the country and abroad on the basis of Law, for covering the budget deficit, and to provide guarantees for repayment of the liabilities on the basis of loans received for this purpose. The Government, at request by the Minister of Finance, makes decision for taking loans and providing guarantees. Either the National Bank or the Central Securities Depository may be in charge of the treasury bills on behalf go the government. Either the National Bank or the Central Securities Depository may perform all technical services necessary for implementation of the decision connected with the government debt, granted by the Minister of Finance.

With respect to the debts issued in form of bonds and treasury bills, the provisions from the **Securities Law** ("Official Gazette of the RM" No. 63/00, 103/00, 34/01, 4/02 and 37/02) are appropriately applied. The bond is a debt security by which the issuer is obliged to pay to the bond holder once or in installments on certain day, the amount of the face value of the bond and the interest. The Treasury bill is a short-term security issued by the Republic of Macedonia in order to collect funds for overcoming the temporal difference between the inflow of revenues and execution of expenditures of the Budget of the Republic of Macedonia, i.e. for financing the budget deficit. The Government adopts the Act on Securities Issuance. The contents of the Act and the elements it should contain are listed in the Securities Law.

Pursuant to the legal regulations in the Republic of Macedonia (*Securities Law*), the trading of the long-term securities is carried out on the Macedonian Long-Term Securities Stock Exchange for which infrastructure is created that enables DVP settlement. Simultaneously, in accordance with the abovementioned law the trading of short-term securities is anticipated to be carried out via the institutionalized money market, whereby the regulation does not exclude trading of short-term securities beyond this institution. Thus far, except for Central Bank bills[8], other short-term securities have not been issued through regular issues due to which there was not a need for connection of the institutionalized money market with the Central Securities Depository in order to enable DVP settlement of the concluded transactions.

Taking this into consideration, it should be estimated whether a better solution at the beginning would be usage of the existing Stock Exchange infrastructure for trading of short-term government securities on the secondary market, which would also mean a need for amending the Securities Law to that end. It will contribute to avoidance of investing in a new system which should provide trading of short-term government securities in the transitional period until the occurrence of the over-the counter market. The efforts of the fiscal and monetary policy will be directed in the near future toward reduction of the transaction costs, which a main precondition for development of liquid secondary government securities market. Likewise, there is a possibility for the institution money market to be equipped both with software and personnel for fulfilling its legal obligation, i.e. performing the function - market of both money and short-term securities.

The recording of the debts in the Republic of Macedonia, the awarded loans and issued guarantees are kept in the Single Treasury that functions within the Ministry of Finance. For this purpose, Debt Management Unit was established within the Treasury Department in 2001. Likewise, in parallel with the introduction of the treasury operations, other units in the Treasury Department were established, including the Liquidity Management Unit that projects the liquidity needs of the government. It is expected that these two units will be additionally equipped with personnel and technique in parallel with the increase of the activities connected with the pending government securities issuance and the need for more comprehensive monitoring of the debt in the broadest sense of the word with a unique objective for better public debt management and reduction of the costs for its financing.

The preparation of the **new Law on Public Finance** is ongoing. This law will regulate many issues such as: the type of the public debt, the criteria limiting the total level of the public debt, transparency in debt management etc.

[8] The Central Bank are traded outside the institutionalised money market, whereby there are procedures stipulated by the National Bank of the Republic of Macedonia for settlement of the concluded transactions that enable DVP settlement.

8. Development of the primary government securities market

Development of the primary government securities market is based on acceptance of the market principles in management of the budget deficit through issuance of securities. Therefore, the policy of public debt management has to avoid generation of possible distortional effects on the primary government securities market. The privileged access of the government to the domestic funds, created through regulatory framework could create captive markets, which results in a slow down of the development of the secondary markets. The same situation appears when the central bank has to play the role of buyer of last resort of the new issues of the government securities when it has to cover the budget deficit with low interest rates. Therefore, the issuance of the government securities has to be based (postulated) on market principles referring on the flexible and competitive determination of the interest rates.

Development of the primary market of government securities has to be part of the process of economic stabilization through defining the noninflatonary sources of financing. If the issuance of government securities has been understood as a possibility for increment of the expenditures and creation of higher budget deficit that would cause unavoidable increment of the inflationary expectations and increasement of the interest rates, which would finally cause increment of the borrowing cost to the government.

The key elements of the establishment of the primary government securities market include: selection of the financial instruments, identification of the potential investors and selection of the adequate issuance (selling) techniques.

8.1 Financial instruments

The fiscal authorities have different financial instruments for public debt management on their disposal: treasury bills, conventional bonds (coupon bonds with fixed interest), floating-rate bonds, zero-coupon bonds, indexed-linked bonds, convertible bonds, call bonds etc. These financial instruments could be classified according to different criteria, which will be explained below in order to be achieved better understanding of the main government paper characteristics.

Depending on the maturity, the financial instruments for public debt management could be divided into short term, up to one year, and long term, more than one year. The government prefers issuance of long-term securities, because short term papers have to be rolled over more frequently and they bear the risk of refinancing. Reliance on short-term financial instruments results in short-term defining of the yield curve which does not satisfy the financial markets requirements for providing information about evaluation of the securities with longer maturities issued by riskier issuers.

From the point of view of the characteristics of the interest rate, the financial instruments for public debt management could be divided into securities with fixed interest rate and securities with a floating interest rate. The government prefers issuance of securities with fixed rate because floating interest rate bears uncertainty about the future costs for servicing of the public debt.

Depending on the period of interest payment, the public debt management financial instruments could be divided into coupon and zero coupon securities. The coupon securities are standard type of debt securities with serial coupon payments (annual and semi-annual). Zero coupon securities are discount financial instruments with payment of the interest and the principal once upon the maturity date. Therefore, the yield is implicitly shown through appreciation of the capital in the period between the issuance and maturity date.

Depending on the period of principal payment, the financial instruments for public debt management could be divided into annuity payment securities, where the principal is paid during the maturity period, or one-time payment securities, where the principal is paid at the maturity date.

Generally, the budget deficit could be financed with short-term and/or long-term interest rates. Financing of the budget deficit with short-term interest rates has been done through issuance of treasury bills or bonds with floating interest rates. On the other hand, financing of the budget deficit with long-term interest rates has been done through issuance of bonds with fixed interest rates. In terms of higher uncertainty about the future movements of the interest rates, reliance on short-term financing is recommended whereby the floating rate bonds are used for lengthening the government-borrowing period. On the other hand, in terms of issuance of short-term securities and floating rate bonds, government is more exposed because necessary monetary and fiscal measures are not undertaken in the terms of unexpected and unfavorable movements. Thus any increment of the interest rates cause increasement of the costs for servicing of the public debt directly. Besides these disadvantages of the financing with short-term interest rates, the stage of development of the financial markets in the transition countries allows budget deficit to be financed only on short-term basis at the beginning. In terms of undeveloped financial markets where the real level of long-term interest rates could not be defined, especially in terms of high and variable inflation, lengthening of the government-borrowing period could be achieved gradually according to the stage of development of the financial markets.

Assuming the macroeconomic and political environment of Republic of Macedonia that influence the investors in securities, the basic precondition for achieving the goals of this Strategy is a proper selection of the financial instruments in the initial stage of development of government securities market. The possibility for success in achieving the preferred level of development of government securities market is higher if **the short term papers are initially issued (treasury bills).** Therefore, assuming the level of confidence of potential investors and the financial ability of economic agents, at the beginning optimal maturity of government securities is **three months**. Extending the maturity of government securities will happen gradually depending on the success of the government in obtaining the investors confidence and in keeping up with the economic development of the country, and especially of the development of institutional investors (insurance companies, private pension funds and investment funds). Therefore, assuming the time needed for reaching higher economic development and taking significant part in the Macedonian financial system by the institutional investors, it will be essential at the beginning the biggest part of the efforts about development of government security market to be concentrated on drawing of **the short term yield curve up to a year**. Namely, after seeing the interest in the issued three-month treasury bills, attention should be paid to creating conditions for placement of **the six and twelve-month treasury bills as a benchmark maturity** on the short term end of the yield curve.

One way to increase the interest in for government securities by potential investors and to extend their maturity is to issue government securities denominated in foreign currency or index securities linked to the exchange rate of the Euro because of high level of euroisation of domestic saving. On the one side, it can stimulate the demand for government securities and can extend their maturity, but on the other it will enhance the euroisation of the national economy. Having in mind the initial stage of development of the financial markets this could be even stronger in the Macedonian case because of the demonstrative effect by the government which may encourage future investors and issuers to prefer index securities linked to foreign currencies and resulting in their domination on financial markets. Therefore, it is recommendable in the initial stage of development of the government securities market to start with **short-term instruments denominated in domestic currency**.

Apart from the fact that it will take a longer period for starting with continuous primary market of long term government securities, here should be emphasized **the key (benchmark) maturities on the long term end of the yield curve** which are identified by economic literature based on experience of the countries with developed government securities markets and more generally financial markets. Thus, in the great number of countries as benchmark maturities for issuance of government securities on the long-term end of the yield curve are chosen: **2, 5 and 10 years**. The principal advantage of extending the yield curve is a reduction of refinance risk and creation of basis for determining easily the prices of other financial instruments. Having this in mind, it is understandable why a great number of Governments make efforts to extend the maturity of their securities and to create a benchmark yield curve[4]. Whether certain government securities will have benchmark characteristics depends on the market preferences. However, it does not mean that the government can not promote certain securities as benchmark issues through taking some measures that direct the interest of market participants to chosen benchmark maturities. This is especially important for the Republic of Macedonia because of the initial stage of development of financial markets where the government through identifying the preferences of potential investors can determine more easily the needed measure which should be taken in order to direct the investors to the chosen benchmark maturities on the yield curve.

[4] Benchmark yield curve is constructed from financial instruments with the same level of credit risk (risk-free government securities) and the key (benchmark) maturities, which enables more efficient pricing of other financial instruments.

From the point of view of the types of financial instruments, it should be taken into account that the design of instruments should be made according to the preferences of different groups of investors in order to enhance the demand for government securities. At the same time, it is necessary to pay a high level of attention when deciding on widening the range of financial instruments in order to satisfy different needs of investors because a great number of financial instruments may cause segmentation on the shallow markets of government securities in the initial stage that finally results in low level of liquidity. Experience from some developed countries suggests that the costs caused by market segmentation exceed the effects of diversification of government securities. Therefore, the government from the beginning will be focused on **optimal range of diversified securities** through standardization of benchmark type of securities and benchmark maturities in order to promote liquid markets at the both ends of the yield curve, the long term one and the short term one.

8.2 Potential investors

The big number of investors in government securities has different preferences, but common for all of them is the intention to connect the level of risk and maturity of securities with the same characteristics of their financial sources. The government could not know the needs of every single potential investor in government securities, but identification of groups with similar preferences could help in the formulation of the government securities policy. In general, there are two major groups of investors in government securities: institutions from financial and non financial sector (big investors) and individual investors (small investors).

The big investors from financial and non-financial sector are: banks, non bank financial institutions (insurance companies, pension funds, investment funds etc.) and companies from non financial sector.

Banks prefer short-term securities with fixed interest rates or medium term securities with variable interest rates, usually tightened to the movement of interbank interest rates. The banking institutions are oriented toward securities, which have most liquid markets, with possibility to settle the transactions in real time, for timely satisfaction of their liquidity needs. On the contrary, non-bank financial institutions, which are traditional investors in government securities, typically target longer time horizons and are interested in medium and long term securities. Companies from the non-financial sector are not oriented toward investments in longer-term securities, but they use the government securities markets for effective management of their own liquidity. Due to cyclic cash flows, companies from the non-financial sector have the need to invest in bigger amounts of liquid securities for short time period. Attracting the companies from non financial sector to invest in long term securities could be achieved trough development of repo markets, which enable investments in long term securities to be transferred into short term securities.

Individual investors (households) prefer low risk and low denominated financial instruments with fixed income because they do not have wide knowledge in securities with variable interest rates, which are aimed for specialized financial institutions. The motive for holding such securities is saving, so usually the demand is oriented toward long-term securities. The bought securities are held by individual investors usually till maturity, and the existence of deep and liquid markets is not so relevant for these investors, while deciding to buy government securities. In terms of high inflation keeping the individual investors on the government securities market is conditioned by presence of financial instruments, which protect the real value of their capital. In such case, the most used instrument are indexed bonds, which on the other hand bear the risk of increased costs of the Budget for servicing the debt. Besides that, keeping the market of individual investors implies higher administrative costs in comparison with big investors. Regardless these disadvantages, the government is interested in development of individual investors' market in order to widen its field of Budget deficit financing, which initiates the decrease in costs, stimulates the financial market development and encourages saving. .

Important role in widening the spectrum of investors in government securities may be played the foreign investors. In stable macroeconomic conditions, foreign investors may contribute to increase in liquidity and continuation of maturity of the securities. However, if foreign investors are concentrated on the short-term part of the yield curve, than eventual lost of confidence in government credibility may negatively affect the macroeconomic stability of the country.

Depending on the financial needs and the aim of public debt management, the government may be oriented toward a certain group or toward all potential investors. Which group of investors would have the priority greatly depends on the tradition and the institutional development, and macroeconomic and financial conditions as well. In general, diversification of investors is basic condition for the development of government securities market because it contributes to higher demand, prolongation of the maturities of securities, decrease in the costs of the government, stimulating financial innovations etc. In transition countries the dominant investors in government securities are the banks, while individual investors usually place their funds in banks' deposits. But, this relation changes in line with the development of the economy and financial markets. Regarding this, the fiscal authorities must be aware, not only of the temporary needs of the certain group of investors, but of all other investors, with the purpose to design securities on most efficient way according to their preferences.

As a result of the unfavorable economic situation in which companies act and the absence of institutional investors as well (only insurance companies with passive role regarding the participation in financial markets), at the beginning, **banks** are expected to be the biggest investors in government securities in the Republic of Macedonia, and they prefer short-term securities. The planned founding of **private pension funds** in Republic of Macedonia during 2004 should contribute to widening of the investor base and gradual prolongation of the maturity of government securities. Potential investor in government securities is the **Deposit Insurance Fund** as well, which has accumulated substantial amount of funds, from premiums of saving deposits, which due to legal restrictions for their placement in safe investments, in the former period were invested in central bank bills or as deposits in the National Bank of the Republic of Macedonia.

The widening of investor base in government securities with the companies and household sector, could contribute to increase in saving and stimulation of financial markets development. Considering this, the first step has already been made by the central bank, trough infiltration and issuance of central bank bills. During the last two years, the interest in buying CB bills by **legal and natural persons** has increased considerably, resulting primarily from high interest rates. Having this in mind, accepting **market interest rates** by the government is very important with aim to attract the potential investors in government securities.

Generally, according to the legal framework of the Republic of Macedonia it is allowed non-residents to invest in domestic securities. Having in mind the risk, which stems from non-residents investing in domestic securities driven by speculative motives, protection mechanisms have been set which reduce the attractiveness of short term investing in securities by non-residents. Therefore, it is expected that the Republic of Macedonia will be protected from inflow of speculative short-term investments in financial instruments that may produce negative macroeconomic effects in case of deterioration of the economic and political situation in the country.

What is significant at attracting the potential investors is that the government securities will not sell themselves, therefore the **promotion campaign** is very important for increasing the confidence and interest of potential investors. Simultaneously, the promotion campaign is aimed at education of the public for these kinds of securities and their importance for financial market development, and economy as well. Successful promotion campaign is especially important for increasing the interest of the population in investment in government securities.

8.3 Techniques of sale

There are four basic techniques of sale of government securities: syndicate sale[5], public subscription, continuous sale and auctions. The use of different techniques of sale of government securities depends on the level of financial markets development, and institutional development, too. The choice of the technique depends on the type of government securities. The auction mechanism is a commonly used technique for sale of treasury bills. On the other hand, the longer-term securities are more *sale problematic* and importance is given to other techniques. Generally, there is a trend for wider acceptance of auction mechanism for government securities selling. The parallel use of various

[5] This technique is similar to private placement, as technique of sale designed to satisfy the needs of a particular group of investors, usually institutional investors.

techniques is not excluded, but then the coordination is very important in order to avoid the negative effects.

In comparison with other techniques, the auction mechanism is the most market-oriented way to minimize the cost of budget deficit financing. The advantage comes from the competition among certain number of participants, which aim to buy part of the limited offer of government securities. The auction should be designed in a way to use the advantages from interest rates flexibility and competition among investors. Also, the auctions are more transparent channel for distribution of government securities compared to other techniques of sale.

In Macedonia, regarding the techniques of sale of government securities, the advantage should be given to **auction sale**. This is relevant because at the beginning the banks are expected to be the dominant investors in government securities, they know the auction mechanism and prefer market formation of interest rates. In addition, in the past the banks have actively participated in CB bills auctions, which contributed to obtaining experience in auction mechanism. One more argument for auction sale of government securities is the active participation of legal and natural persons in CB bills auctions in the past two years.

The participation in auctions should be limited to a particular group of investors. Usually the direct participation in auctions is allowed to banks and some other financial intermediaries, while other investors submit bids indirectly, trough participants with direct access to auctions. The basic principle for determination of participants is to allow the satisfactory level of competition, in order to impede potential connection between participants with speculative motivations. It is also possible to give the exclusive right to participate in the auctions to certain number of agents, commonly called primary dealers, which in return should provide simulative services for development of government securities market.

Having in mind that the fiscal authorities in Macedonia will need to attract investors in government securities, as many as possible, at the beginning it is more adequate to promote big number of auction participants, that could contribute to easier participation on the primary market and higher level of competition. Regarding that, direct participants should be the **banks**, complying with some criteria (for example, minimum amount: 1.000.000 denars). The other participants could submit bids for buying government securities trough banks where denomination of securities could be relatively small (for example: 10.000 denars) in order to allow easier access of higher number of small investors. Extending exclusive right for auction participation to few participants could be actualized later when the efforts of fiscal and monetary policy would be aimed at secondary market development.

The important question in auction design is the mechanism for allocation of bids and determination of the price that the participant is going to pay. There are two major types of tenders for sale of government securities: multiple price and uniform price auction tender. Within the both tenders the bids are graded by price, starting from the highest price (lowest interest rate) down, until the total offered amount is exhausted. At the first type of auction, known as American auction, the successful bidder pays the price offered. At the second type of auction, known as Dutch auction, the successful bidders pay same price that is equal to the lowest successful price. This means that the most participants are paying lower price that they offered in their bids for buying government securities. Thus, the amount of funds that government receives is lower in comparison to the American type of auction. Then, why the issuer is interested in this type of auction? The answer is given in the theory of auctions, which suggests that Dutch auction reduces the uncertainty and stimulates the participants to participate in auctions assuming that they will pay lower price than offered.

This uncertainty is rather bigger in the American type of auction, where there is a risk for the participants to buy securities at a price higher than the market price. Namely, the secondary market trading would probably start at average auction price, including the unsuccessful bids, so the price will move close to the lowest accepted price. Every participant who had auctioned with much higher price than the market price would loose because the securities, which were successfully bought at the primary market have lower price at the secondary market. This risk is known as *winner's curse* and is much bigger where financial markets are undeveloped, with higher variability in the prices of securities. Due to high uncertainty, the investors may avoid participation at auctions and could focus on buying government securities at the secondary market, which results in lower competition on the primary market owing to concentration of the bids in the hands of few participants.

Regardless of this disadvantage of the American auction, all arguments are not on the side of Dutch auction. Namely, in terms of developed financial markets, when the government issues limited amount of securities, the demand may be greater than the supply, which indicates that the investors are ready to pay higher prices, that at the end results in lower costs for the government. However, Dutch auction does not benefit from this advantage, known as consumer surplus, which is the difference between the price that the participant is ready to pay and the price that he really pays.

The Dutch auction leaves space for manipulation by bigger participants, which may auction at very high prices, knowing that they will pay uniform price lower that auctioned, while their big amounts of bidding exclude a lot of small participants from the auction. Also, the uniform price may fluctuate from one auction to another, because it presents the marginal, not weighted price[6].

Regarding the choice of tender for auction sale of government securities in Macedonia, the advantages are on the side of the American type of auction. The major reason for this argument is found in the familiarity of the banks and their clients with this type of auction in comparison with the uniform price tender, due to their participation in CB bills auctions, where American auction is used. Also, in terms of difficulties for projecting the demand for government securities, the use of Dutch auction may result in acceptance of lower uniform price, which means greater costs for the government. However, this does not mean that the Dutch auction should not be used at all, but its

[6] Although, the theory is in favour of the Dutch auction, according to research made by Bartolini and Cottarelli for the use of auctions in sale of government securities during 1994, from 42 countries that use auctions, over 90% use multiple price auctions.

acceptance is more adequate for the later stages of market development, after stabilization of the demand for government securities on certain level, which would enable the use of advantages of lower uncertainty on the movement of interest rates.

Having in mind the uncertainty of the auction process in general, the issuer may allow submitting of non-competitive bids, which means buying government securities at weighted (or uniform) price. This gives the smaller investors an opportunity to buy government securities at a reasonable price, thus reducing the risk of failure. In order to increase the interest in government securities by investors that prefer such way of price determination, it is advisable to provide the opportunity of submitting **non-competitive bids** in auctions of government securities. The total amount of accepted non-competitive bids should be limited in order to determine the auction prices by participation of sufficient number of competitive bids. Bearing in mind that inclusion of non-competitive bids complicates the auction process, at the beginning it will be allowed to submit only competitive bids, keeping the possibility of inclusion of non-competitive bids later.

Naturally, auction process allows speculative behavior, which emphasizes the need for setting a mechanism for protection of the government from paying unreal high interest rates. One solution is by determination of a **maximum interest rate**, which would protect the government from speculative behavior of certain investors. However, due to the major weakness of determination of maximum interest rate, which is grouping the interest rates of the bidders around its level, it is necessary to define better criteria for rejection of bids with unreal high interest rates. Therefore, criteria for determination of upper level of interest rate based on submitted bids will be defined for every auction separately, where bidders will be informed about the functioning of the criteria.

Information about the government intentions for selling government securities could enable the potential investors to form their investment strategies for optimal portfolios easier. Therefore, it is common practice to announce the **auction calendar** for the following year. The fiscal policy must pay attention to the secondary market development, when determining the frequency of auctions. Namely, frequent auctions may result in small amounts of government securities sold at auctions, that have negative influence on the secondary market liquidity. Typically, the treasury bills auctions are held once a week or twice a month, while longer term government securities auctions are held in longer interval, once a month or quarterly.

Besides the announcement of dates of auctions, the auction calendar usually includes the amounts of government securities that government would offer at each auction. Having in mind the difficulties in determining the precise amounts for each auction, what could be done in Macedonia in the first stage is announcing **the six-month calendar**, which will include **quarterly amounts** for sale of government securities, while the precise auction amount would be announced few days before the auction. However, at the moment of deciding on the auction amount, its high fluctuations from one to another auction should be avoided in order to provide a steady offer, which is especially important for maintaining of the interest of investors in government securities. Namely, government debt management should be focused on providing stability of government securities offer, while cash management should be concentrated on overcoming of the temporary budget imbalances.

The transparency in the auction process is an important condition for acquiring and maintaining the confidence in the techniques of sale of the government securities. Therefore, auction rules and conditions will be disclosed to the public. Also, information regarding the auction results will be disclosed, including: minimum, maximum and average price, supply, demand, realization, etc.

9. Development of secondary government securities market

Developed secondary markets in government securities provide liquidity and enable market participants to execute large volume transactions with little impact on government securities prices. Developed secondary markets guarantee liquidity of investments and continuous price determination. Consequently, investors are interested in enlarging the government securities portfolio because they are able to sell the securities any time at acceptable prices. Increased demand for government securities contributes to an increment of their prices, and consequently a decrement of the costs for financing the budget deficit. At the same time, developed secondary markets in government securities increase the efficiency of central bank interventions trough carrying out flexible open market operations and improve the functioning of transmission mechanism of monetary policy.

Building of competitive market infrastructure is an important condition for development of secondary markets in government securities. They can be traded trough a wide variety of mechanisms, including organized exchanges, over the counter markets and other similar trading systems. Trading moves from one to another system step by step, according to the development of financial markets, changing of the market participants' needs and progress in information technology. Supporting of a competitive market infrastructure is important for narrowing of bid-ask spreads of government securities, which contributes to an increment of their liquidity. Dynamic competition between stock of exchange and over the counter markets, that is supportive of competitive markets, preserve exploitation of dominant monopoly or oligopoly position.

Having in mind that the development of government securities market in Macedonia is in initial phase, the effort at the beginning will be more concentrated on the development of a primary market. Therefore, at the beginning more frequent presence of the government on the primary market will be necessary in order to stimulate the demand for government securities. Once the target amount for sale is reached and the demand for government securities is stabilized the fiscal and monetary authorities should be concentrated on development of secondary markets for government securities. However, some activities should be taken at the beginning in order to create an infrastructure for trading on secondary markets.

According to the Macedonian legislation (Law on Securities) trading in long term securities is allowed to be executed only with the Macedonian Stock Exchange (MSE) which is connected with the

Central Securities Depositary (CSD) where an infrastructure providing DVP settlement exists. At the same time, according to this Law trading in short term securities should be organized on the institutionalised money market, but the Law does not prohibit trading outside this institution, as is the case with MSE. Apart from the central bank bills of the National Bank of the Republic of Macedonia[7], so far no other short-term securities have been issued on regular basis, which have not made an urgent need for building of connection between CSD and the institutionalised money market in order to provide DVP settlement.

Having in mind the Macedonian experience regarding the trading of securities on the Stock Exchange, in the future it is important to create conditions for the development of a competitive market infrastructure, which would contribute for a decrease in transactions costs, on market basis. In this direction, in the near future the fiscal and monetary policy would be directed towards development of over-the-counter-markets that could decrease the transaction costs on competitive basis, and that is the main reason for development of a liquid secondary market of government securities.

An important question for the development of secondary markets in government securities, especially for development of a secondary market in short-term government securities, is settlement of concluded transactions. Namely, as shorter is the time between concluding and settlement of transactions the more liquid are the government securities. Mostly, transactions concluded on organized exchanges are not settled during the same day. This is the case also in Macedonia because CSD at the moment is prepared to support settlement of transactions over T+1. Expecting that the biggest investors in government securities will be banks that prefer **real time settlement**, great attention will be paid to it when the efforts are concentrated on development of over-the-counter market.

During the initial phase of development of secondary market in government securities there is a small number of transactions impeding correct pricing of securities. Therefore, encouragement of some financial intermediaries for supporting of secondary market can foster its development and deepen its liquidity. **Market makers** are financial intermediaries, mostly primary dealers, which hold appropriate amount of government securities, quote bid and offer prices on continuous basis and are prepared for trading at quoted prices. Their function is supporting of liquidity of secondary markets in government securities trough equilibration of supply and demand, incorporation of available information and quick execution of transactions.

Market makers have some privileges and obligations for promoting of government securities market. Some of the obligations are as follows: active participation in government securities auctions, continuous quotation of bid and offer prices, taking the prescribed percentage in transactions on secondary markets in government securities, taking the prescribed amount of government securities, reporting for concluded transactions to the central bank, etc. At the same time, they have some

[7] Central bank bills are traded outside the institutionalised money market and for settlement of transactions there are prescribed procedures by National Bank of the Republic of Macedonia, which provide DVP settlement.

privileges: exclusive right to participate at irregular auction for government securities, credit lines from central bank, exclusive right to participate in some of the interventions of the central bank, tax exemptions, etc.

Having in mind the role of market makers in the development of liquid markets in government securities, fiscal and monetary policy will support their activities for promoting of rapid development of government security markets in Macedonia. Therefore, promotion of market makers will occur once the interest of financial intermediaries for investment in and trading with government securities is noticed. Their promotion probably will be done in parallel with the development of over the counter market.

Development of government securities markets can be fostered by introduction of **repo**. Repo is prompt sale of securities with an obligation to buy them back at agreed price in future. It enables an overcoming of money or securities shortages and that is why it is widely accepted by the private sector and the central bank in its interventions. In order to exploit the advantages provided by the repo in fostering the development of government securities market, and more general financial markets, the National Bank of the Republic of Macedonia in near future will engage in preparing of **Master repo agreement**, which is a basis for concluding repo transactions.

Moreover, encouragement of development of related markets such as futures, options, short selling, etc. will enhance the development of government securities market in Macedonia.

10. Coordination between the monetary and the fiscal policies in the development of government securities market

Coordination between the monetary and the fiscal policies is a consequence of the need to set consistent targets in order to achieve the main goals of economic policy (price stability, sustainable growth, full employment etc.). Probability for emerging of a conflict in making efforts to reach the set targets of the monetary and the fiscal policies imposes existence of an efficient coordinating arrangement in order to solve potential problems. Otherwise, shortage of coordination between monetary and fiscal policy may result in macroeconomic disequilibrium and may create high uncertainty for the private sector that leads to loss of credibility of the monetary and the fiscal authorities.

In market economies the needed coordination between the monetary and the fiscal policies can be achieved in two ways:

1. Where financial markets are developed, through the work of market forces where there is strict separation between objectives, functions and instruments of the monetary and the fiscal policies. In this case, monetary authorities are focused on achieving price stability through intervening on deep and liquid markets by market-oriented instruments. At the same time, developed financial markets

enable the fiscal authorities to cover the budget deficit through issuance of securities under conditions, which exist on financial markets.

2. Where financial markets are underdeveloped, through setting of common objectives and pursuing of joint actions for their achievement. In this case, where there are not deep and liquid secondary markets of securities, monetary authorities in conditions of structural liquidity surplus operate on the primary market in order to achieve their main objective. At the same time, fiscal authorities use this market to satisfy their budget needs. Therefore, reaching of high level of coordination between monetary and fiscal policy when intervening on the same market is a precondition for achieving common objectives.

In these terms, fiscal and monetary authorities can use either same or different instrument for achieving common objectives. Namely, in the first case the Ministry of Finance issues securities for covering the budget deficit and at the same time the Central Bank uses government securities (treasury bills) for achieving monetary objectives. In the second case, the Ministry of Finance issues securities for covering the budget deficit and at the same time the Central Bank issues own bills for monetary purposes. The main advantage of the first approach, usage of government securities for achieving fiscal and monetary objectives, is promotion of the development of government securities market and reduction of the risk of market segmentation as a result of using one type of security. On the other side, for achieving different objectives by using one instrument is necessary to reach high level of coordination between the monetary and the fiscal policies in order to maintain operational autonomy of the Central Bank that is in the most cases hard to attain. In that sense, although the usage of CBbills does not eliminate the need for coordination between the monetary and the fiscal policies, it contributes to separation between monetary and public debt management that gives an operational flexibility to the Central Bank when carrying out monetary interventions.

Very rare presence of the government on the primary market of securities in the past contributed to keeping hidden the potential conflict between monetary and fiscal policy in the Republic of Macedonia. Namely, until now the budget deficit was financed mostly from abroad that did not cause a conflict between fiscal and monetary policy when carrying out monetary interventions trough issuance of CBbills by the National Bank of the Republic of Macedonia.

Having in mind that the government is going to issue short-term securities, which have similar characteristics with the CBbills, the use of these securities at the same time may lead to unnecessary conflict between them and to market segmentation. Therefore, careful design of the instruments and sale techniques can contribute to minimization of market segmentation. In this situation, it is recommendable for the **Central Bank** to issue securities with **up to one-month maturity** that can allow it to manage easily the level of liquidity and interest rates in the banking system. At the same time, **government securities** can be issued with longer maturity (**three months and longer**) and the amounts corresponding to budget requirements. In this way, the efforts of the central bank for achieving the final objective of the monetary policy will be focused on markets with very short-term maturity, and the Ministry of Finance will be able to extend gradually the maturity for financing of budget deficit. In the next phases of the government securities development, the role of the CBbills would gradually decrease, and the government securities are planned to serve as an instrument for monetary operations (picture 1).

Picture 1

I phase	Primary market	Secondary market
TB	Government debt management	
CB	Monetary management	

II phase	Primary market	Secondary market
TB	Government debt management	Monetary management
CB	Monetary management	Monetary management

III phase	Primary market	Secondary market
TB	Government debt management	Monetary management
CB		

TB-Treasury bills

CB-CBbills

In supporting of the development of government securities market the Central Bank **will reduce monetary interventions on the primary markets referring to issuance of CBbills** in order to create wider area for government securities. At the same time, in order to concentrate the efforts on management of liquidity and interest rates in the banking system the Central Bank will allow an access to central bank bill auctions **only to banks**, and the legal entities and natural persons will be directed to the market of government securities for supporting of its more rapid development. Having in mind that it is assumed that the banks are the biggest investors in government securities at the beginning, which at the same time are dominant owners of CB bills, it is expected that this will reduce the risk of market segmentation for these securities.

In developed market economies the interest rates on government securities issued for financing of the budget deficit are market determined under the influence of the monetary interventions of the central bank which are conducted in order to regulate the liquidity in the banking system and to send signals for the general level of interest rates. On the other hand, in the economies with underdeveloped financial markets determination of interest rates is the question producing conflict between management, the aim of which is more important: low cost for financing of budget deficit or price stability through setting the interest rate on appropriate level, respectively.

When the level of the interest rate of the CBbills of the National Bank of the Republic of Macedonia is devoted to maintaining of stable exchange rate, and when the interest rate of government short-term securities will follow it, there is a probability for emerging of this kind of conflict. Resolving this potential conflict about appropriate level of interest rates should come from the common objective for development of government securities market respecting the basic rule that the interest rates are determined by the market under the influence of the monetary interventions of the Central Bank.

Besides the level of interest rates, coordination between the monetary and the fiscal policies will be necessary in determining the amount for sale of government securities and the time of conducting of auctions. In order to achieve more successfully the needed coordination in this segment, it will be necessary the Ministry of Finance to inform the Central Bank on time about the **purpose (amount)** of issuance of government securities. In that way, the auction days for government securities will be determined in the annual calendar in order **not to overlap** with the auction days for central bank bills. During the past period, the coordination between the monetary and the fiscal policies on the operational level has been significantly improved as a result of joint presence of representatives of both institutions on the meetings which take place in the Ministry of Finance and the Central Bank in order to forecast the budget expenditures and revenues, and the liquidity of the banking system, respectively.

The question, which should receive the attention from coordination aspect, is the choice of market participants in the auctions. Namely, as far as auctions of government securities are concerned most of them include different financial intermediaries. On the other hand, when conducting monetary interventions the Central Bank is primarily focused on banks. Having in mind that at the moment in the Republic of Macedonia the role of other financial intermediaries regarding their activities on the financial markets is minimal, at the beginning it is intended the banks to be direct participants that will enable setting **unified set of participants**. Bearing in mind that the supervision of the banks is done by the central bank, selection of the primary dealers in the future will be made **jointly** by the Ministry of Finance and the Central Bank. At the same time, introduction and selection of market makers for government securities will be made jointly, too.

The decision NBRM to be the agent of the government for the issuance of government securities would facilitate the coordination between the monetary and the fiscal policies. Primarily, the role of the central bank would consist of organizing the treasury bills auctions, for which the infrastructure already exists and is used for central bank bills auctions. Also, the NBRM will collect the data on legal and natural persons, which buy securities on the primary market, through the banks and will deliver the data to the Central Securities Depository, where the ownership of securities is registered. In connection with the organization of the auction process, the central bank will prepare procedures and directions for using the auction application by the direct participants. Besides organizing the auction the NBRM will provide necessary information for the selection of the primary dealers and market makers, it will participate in defining of the criteria for selection, and it will follow the compliance of the set criteria.

In the previous period, the coordination between the monetary and the fiscal policies has been improved substantially, as a result of the mutual participation of representatives from both institutions on the meetings, held in the Ministry of Finance and the National Bank of the Republic of Macedonia, where the Budget revenues and expenditures and banking system liquidity are planned, respectively. In order to improve the coordination between the monetary and the fiscal policies, on operational and strategic level, it is important to create a **Committee for coordination of debt management and monetary policy**. In that Committee the NBRM would inform about the movement of interest rates, foreign exchange rate, banking system liquidity, conditions on the financial markets, and would have advisory role, while the Ministry of Finance would decide on the amount and the interest rates of the securities, which would be issued, according to the recommendations of the Central Bank and Budget needs. Besides this, in the frame of the Committee it would be discussed and decided upon all activities, which would be undertaken for future development of primary and secondary market of government securities.

11. Action plan

Activities	*Obligation of:*	*Deadline*
1. Ratification of the Strategy for development of government securities market	Government of RM	September 2003
2. Legal and institutional framework		
- Adjustments in the laws regarding issuance, registration, trading and settlement of the government securities.	MF	December 2003
- Distribution of responsibilities regarding issuance, registration, trading and settlement of the government securities per institutions (Ministry of Finance, National Bank of the Republic of Macedonia, Central Securities Depository, Macedonian Stock Exchange).	MF	September 2003
- Act for issuance of government securities.	MF	November 2003
- Rules for issuance of government securities.	MF & NBRM	October 2003
-Fiscal agency agreement	MF & NBRM	October 2003
- Registration of securities agreement	MF	October 2003
- Distribution of responsibilities per departments and employees in MF and NBRM regarding the rules for issuance of GS, analysis, planning,	MF & NBRM	December 2003

monitoring of the secondary trading, accounting, reporting, internal control, etc.		
- Public debt Law	MF	2004
3. Meetings		
- Central Securities Depository, Macedonian Stock Exchange, Securities Commission, Money and short term securities market.	MF & NBRM	September 2003
- Banks	MF & NBRM	September 2003
- Insurance companies, big corporations, Deposit Insurance Fund, Pension Fund and Pension Supervision Agency	MF & NBRM	September 2003
4. Adjustments in auction application and Treasury software		
- Upgrade of auction application	NBRM	August 2003
- Procedures for using the auction application - Internal (NBRM & MF) - External (banks)	NBRM	September 2003
- Testing the auction application	NBRM	September 2003
- Upgrade of software for the purpose of Treasury operations	MF	
5. Preparing the six-month calendar of GS auction - Amounts (quarterly) - Frequency of auctions	MF	November 2003
6. Estimation of costs for 2004 - Interest - Promotion - Costs for issuance and registration - Other costs.	MF	November 2003
7. Promotion campaign - Brochures, education of public, TV advertisement	MF & NBRM	October 2003
8. Changes at CB bills auctions - Exclusion of clients - Reduction of the auction frequency	NBRM	2003
9. Establishment of the Committee for coordination of debt management, monetary and foreign exchange policy	MF & NBRM	December 2003
10. Preparation of Master Repo Agreement	NBRM	December 2003
11. Introduction of OTC	MF, NBRM, CDS	2004
12. Introduction of market makers	MF & NBRM	2004
13. Issuance of GS on longer terms	MF	2004