



# The Debt Management Office

Based on a client presentation

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# Outline

- The Debt Management Office
  - Different institutional arrangements
  - Internal organisation and operation
- Building a DMO
  - What should happen; and what goes wrong

*[for wider Governance Framework, see separate presentation]*



# The Debt Management Office

# Why Create a Debt Management Office?

- Clarity and transparency
  - Internally, with focus on the debt management task
  - Externally, in the perception of the markets in relation to objectives and intent
  - Linked with accountability and governance
- Improving capacity, efficiency and effectiveness
  - Getting decisions right
  - Emphasis on portfolio risk management
  - Expertise, professionalism

# Why do Countries set up DMOs?

*Kalderon & Blommerstein, OECD 2002*

- Motives for Separate office
  - Autonomy from political sphere
  - Emphasises separation between debt management & monetary policy
  - Greater transparency between government functions
  - Ability to concentrate expertise
  - Staff recruitment and retention (pay flexibility)
- Linked with improved transparent and accountable framework
  - Accountability must be supported by governance framework
  - Needs high level political support for transparency and accountability

- Signals a break with the past
- **But:** major administrative task – beware of diversion of effort

# Different International Institutional Arrangements

- Operational independence from MoF & Central Bank
- Responsibilities often include cash management, also asset management, contingent liabilities and on-lending
- Relatively recent trend – most debt offices since late 1990s
- Spectrum of institutional arrangements in OECD
  - Part of Treasury / MoF (Italy, Greece) or another ministry (Spain)
  - “Bureau” within Treasury / MoF (Finland, USA)
  - Independent agency within Treasury / MoF (Australia, New Zealand, Netherlands, UK, Belgium, France)
  - Agency within central bank (Denmark)
  - Autonomous agency within government (Sweden, Austria, Portugal, Ireland)
  - Company owned by Government (Germany)
- Some use Central Bank as agent; all use Bank for some services

# Governance and Structures

- The greater the DMO's institutional “distance” from the MoF...
  - The greater the managerial responsibility and systems independence
  - The more sophisticated are the DMO's operational requirements and capabilities – both market (derivatives etc) and reporting (performance measurement)
- But...
  - The more developed the business strategy has to be
  - The greater the precision of objectives – and the need to define and measure them; and report on them
  - The heavier the audit and information flow requirements
  - The more important is MoF's “intelligent customer” capability

# Inside or Outside the Ministry of Finance

## Inside

- Puts less strain on governance framework; reduces principal-agent risks
- Proximity to budget and planning functions
- Easier for MoF to monitor performance; and DMU to feed its expertise into MoF
- Establishing the office is much more straightforward

## Outside

- Establishes separate status; signals break with the past
- Helps establish credibility with market
- Encourages more commercial management approach
- Easier to recruit and retain skilled staff

**=> Preferable for EMCs to establish office within MoF**

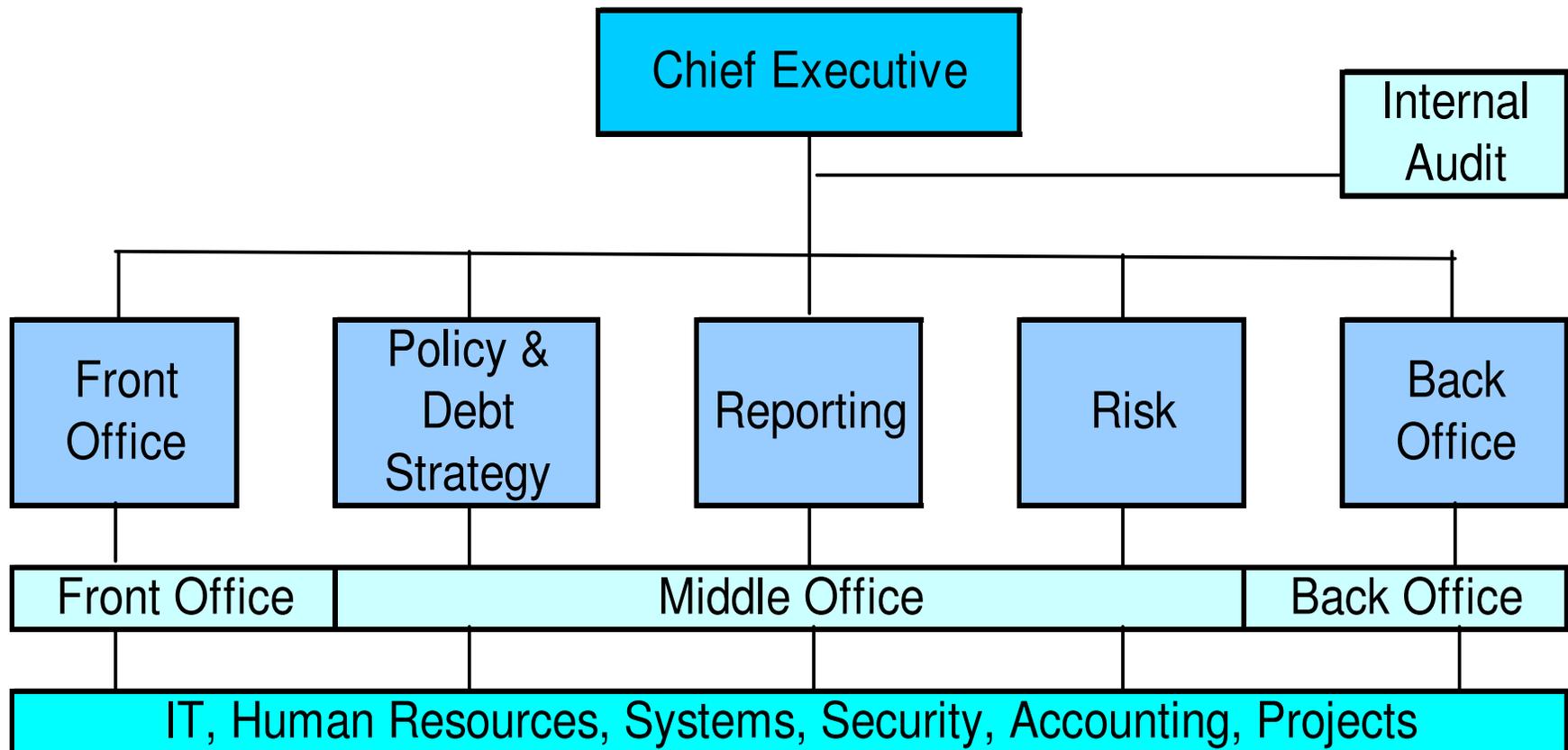
# Internal Governance: Principles

- Setting risk management policies & procedures, consistent with objectives and best market practice
- Establishing arrangements for:
  - Internal policy making, delegation and communication
  - Operational risk monitoring & control
  - Audit
- Addressing resource needs and building capacity
  - Business Planning
  - Staff requirements, training, IT
- Building professionalism, commitment and a strong culture

# Internal Specialisation

- Separate front, middle and back-office
  - Allows specialisation
  - Avoids duplication
  - Contributes to risk management
- Distinguish between key responsibilities
  - Senior management
  - Front office: primary issuance and execution, internal and external, secondary market transactions (debt and cash)
  - Middle office: policy and portfolio strategy development and accountability reporting
  - Middle office: risk management: policies, processes and controls
  - Back-office: transaction recording, reconciliation, confirmation and settlement; debt servicing; debt data
  - Internal audit and compliance – reporting to Head of Office

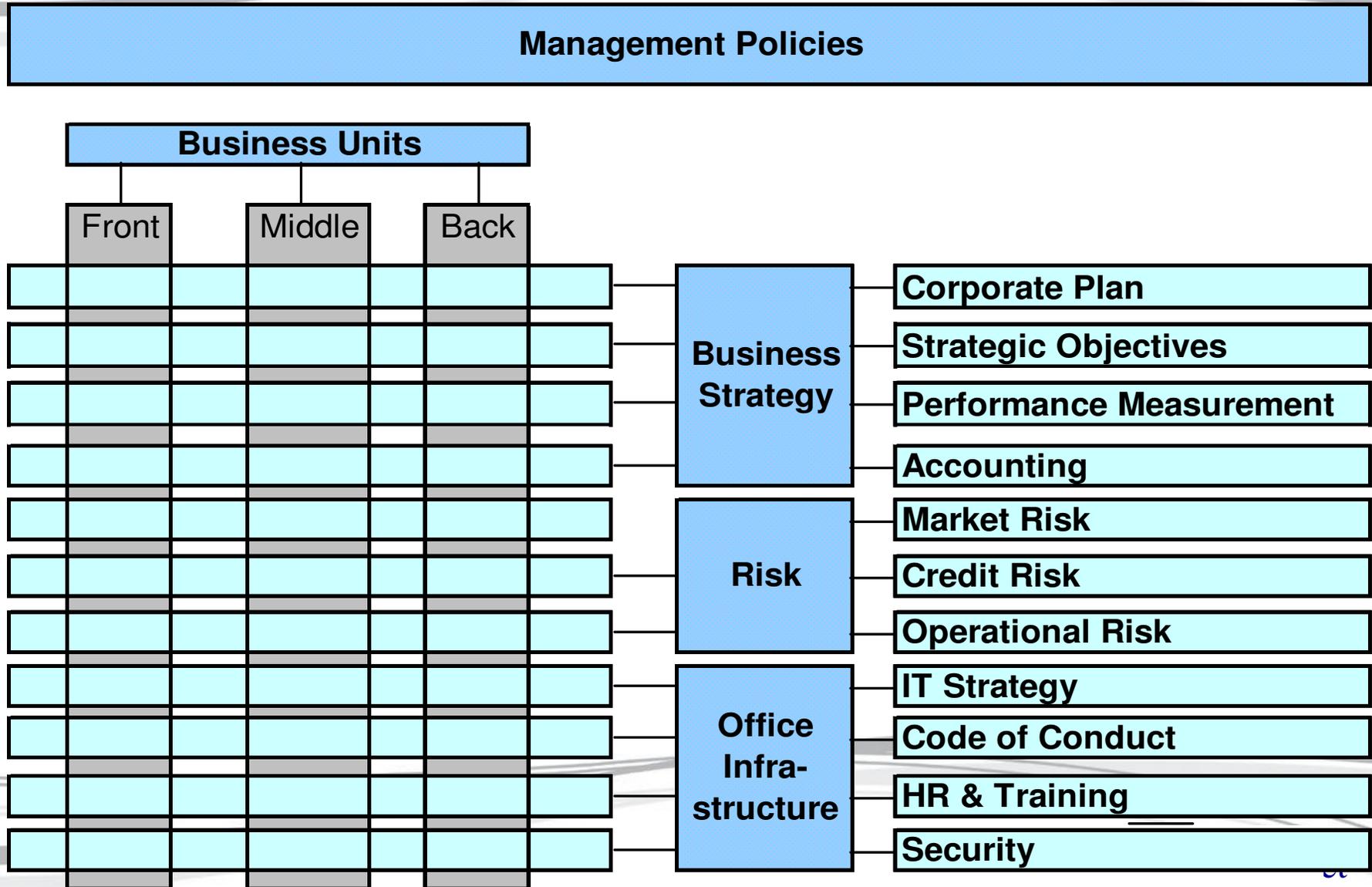
# Internal Organisation



# Working Horizontally

- Management team acts collectively to meet a DMO's objectives
- Make effective use of the skills and resources within DMO
  - Many issues must take into account views of more than one team
  - Means working across teams or directorates, and being able to allocate staff to handle issues that straddle different parts of the office
- Everyone should understand what DMO as a whole is trying to achieve; and how their work contributes to objectives
  - Internal communication is important
  - Objectives and targets cascaded to all individuals at all levels
- Must be good awareness of the risks associated with DMO's functions
  - Split of responsibilities between front, middle and back office
  - Operational risk management framework
  - Risk awareness

# Examples of Horizontal Policies



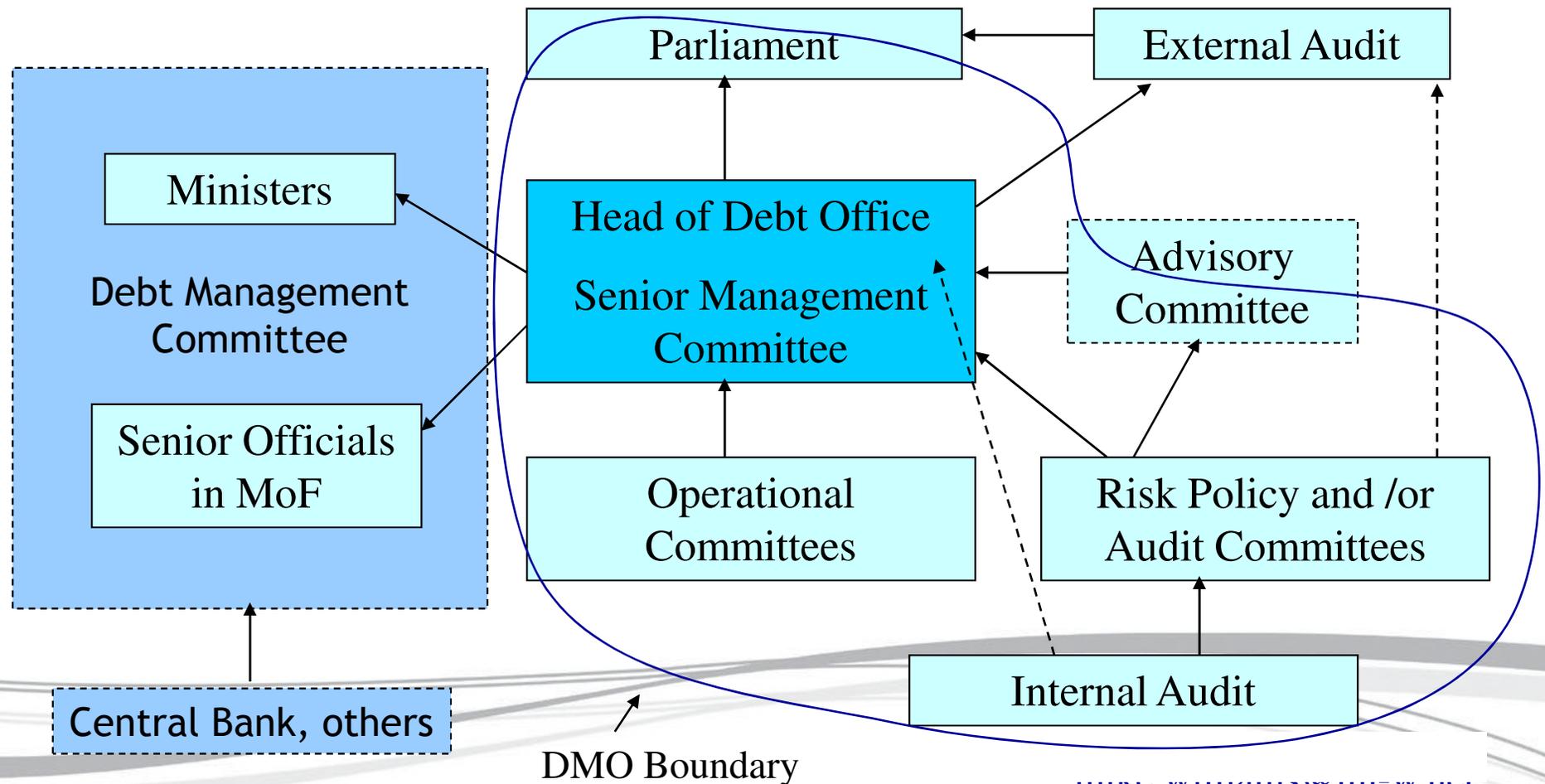
# Internal Control

- Policy Control
  - Senior management
    - Main business planning decisions; risk monitoring
  - Operational Committees
  - Supported by regular reports to management and to MoF
- Risk Management
  - Credit and Risk committee – establish policies and limits
  - Expertise in middle office
    - Analytical capability
    - Advice
    - Monitoring and reporting
  - Internal audit & compliance functions, supported by Audit Committee
  - Separation of operational and processing areas

# Operational Risk

- Operational Risk
  - “The risk of loss resulting from inadequate or failed internal processes, people and systems or from external events” [Basel Committee “*Principles for the Management and Supervision of Operational Risk*” (Feb 2003)]
  - Most frequent (probably)
    - Errors (in recording data, making payments)
    - Systems failure
    - Business disruption (fire alarms, electricity failures)
- Operational risk expertise in Middle Office
  - Risk assessment and prioritisation
  - Developing a common and consistent control framework
  - Providing advice and co-ordinating reports
    - Processes and controls documented
    - Embedded monitoring, “exception logs”, management “certification
    - Regular senior management review of risk profile

# External and Internal Governance Structure - Typical International Arrangement





# Building the DMO

# Challenges and Complexity

- Challenges
  - Finding good people; building the “team”
  - Understanding the “business”; establishing business processes
  - Obtain premises, plan, procure and test IT
  - Manage external relationships
    - Central Bank, Regulators
    - Market makers, investors, exchanges
    - Government (policy and services)
- Achieve a “seamless” transition – financing the borrowing requirement throughout, avoid market disruption
  - Bilateral discussion throughout
  - Publishing policy documents
  - Consulting on timetable
- Manage as project – identify tasks and dependencies, long-lead items, priorities, responsibilities, etc

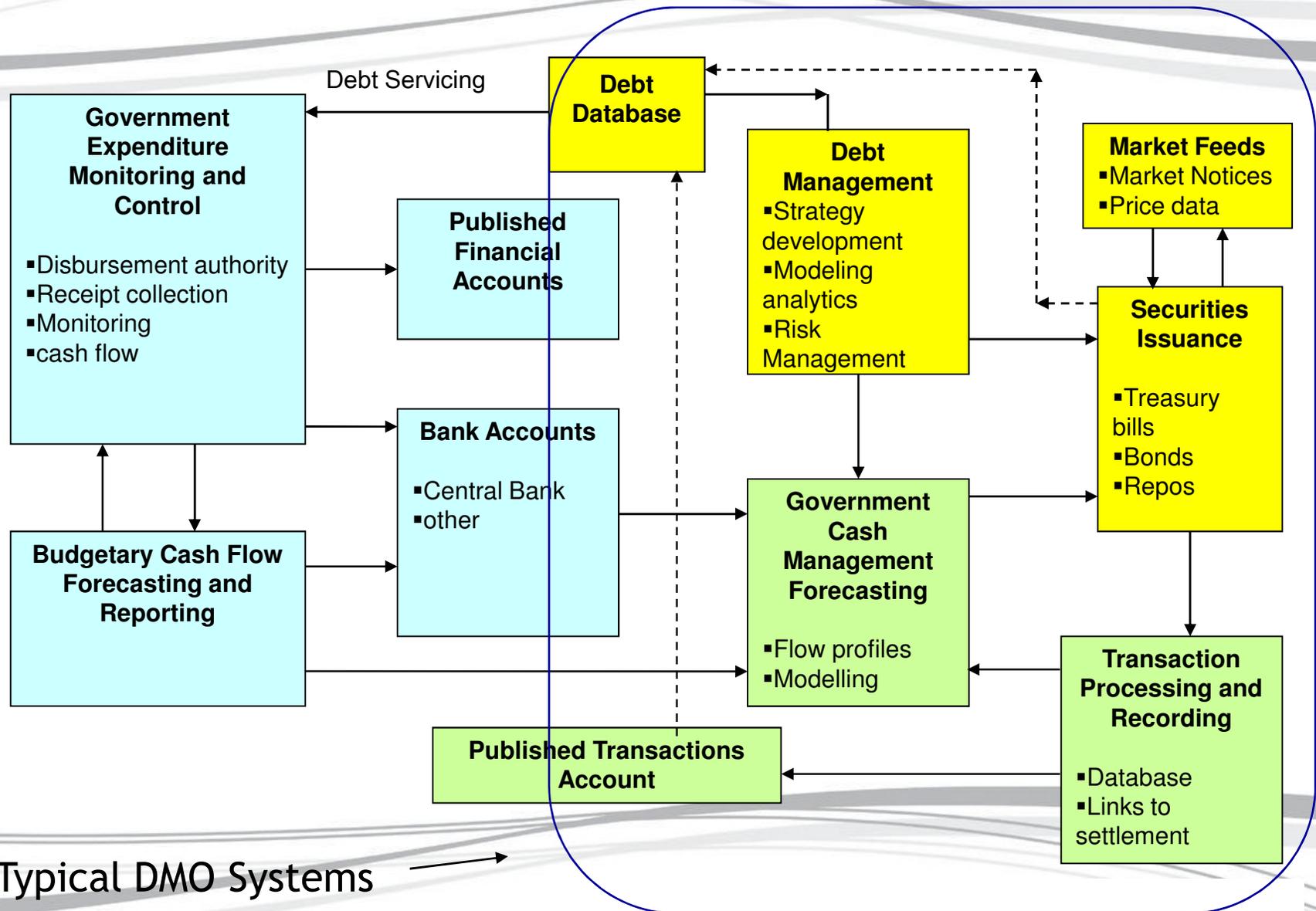
# Building Capacity

- Role of the business plan
- Establishing internal management structures
  - Horizontal decision-making
  - Internal communications
  - Operational risk management
  - Team building
- Training to close skill gaps
  - Develop training plan linked to business objectives
  - May be only route to closing gaps (some secondments)
  - Means to professionalism
    - Make skills available to others in Government
    - Helps attract and retain staff
- Enhance individuals' commitment

# The Business Plan

- Develop the goals and tasks over the medium term (the next 3 years or so); and shorter-term targets
  - ensure a common understanding across all those involved
  - encourage thinking about the future, not just current pressures
  - provide a basis for identifying priorities
- Build the internal management structures, including for communication and operational risk management
- Identify capability gaps and – the “projects” needed to close them
- Develop the capacity building plan – covers IT and staff
- Contributes to building a common culture across the debt management unit, including through the business planning process itself

# Debt (& Cash) Office: Systems



# Debt Management Systems

- Core functionality
  - Debt recording and data analysis: debt stocks, flows and indicators; debt servicing obligations; debt reporting, and accounts; inc  
contingent liabilities
  - Capture of market data (price and other data) – in real time if any  
part of the portfolio is being actively traded
  - Interfacing with financial management, accounting & data systems
  - Transactions processing: deal capture, deal release, settlement &  
accounting
  - Risk and performance analysis – of 3 [different] types
    - scenario analysis for strategy formation
    - tactical trading support
    - credit exposure and monitoring.
- The initial requirement is the First in the list above – the  
debt recording and back office database systems

# The Challenge of Building the Team

## The Aim

- Building a professional and committed team; with high standards
  - Capability
  - Best practice
  - Responsiveness
  - Innovation
- Collective understanding and focus
- Rewarding the right behaviours
  - Public sector ethos [role of “profit”]
  - Open (learn from errors; ‘no blame’)
  - What comprises good performance

## Some Tools

- Limited pay flexibility: but
  - Combination of greater authority and accountability can improve job satisfaction.
  - Delegation allows greater flexibility to respond to changes in the economic environment - improving the office’s sense of purpose.
  - Importance of “branding” [inc. the T-shirt!]
- Visibility as a centre of excellence, with the support of Ministers, helps improve the status of staff
- Training – improves efficiency and morale, helps recruitment

# Retaining Staff: International Experience

- Widespread concern internationally
  - Legislative constraints, civil service regulations
  - Low salaries, high turnover
  - Lack of structured training
- Responses
  - Extra pay, cash bonuses – although often not available
  - “Well being” schemes – gym membership, crèches, occupational health
  - Structured training, including
    - International support networks (conferences, twinning, study tours)
    - Scholarships abroad
  - Internships from local universities
  - Establish recognised centre of excellence
    - Embed good practice (clear goals, risk management, formalise procedures)
    - Varied training
    - Team spirit, branding
    - Skills “lent” elsewhere (in MoF)

# Some Lessons from the UK

- Establish respective roles and responsibilities (in relation to rest of Treasury / MoF, Central Bank etc) and publish them
  - agree the internal rules with the Ministry of Finance, inc the scope for managerial freedom, via delegations
- Manage stakeholders (Ministers, market, Central Bank, Parliament)
- Involve staff
  - Horizontal mechanisms
  - Branding
- Signal what matters
  - Delivery
  - Professionalism
  - Risk management, inc operational risk
  - Business Planning
  - Effective internal “project management”

# What Goes Wrong - 1

- Turf wars: lack of agreement between competing baronies
  - One example: ministry of planning, budget dept MoF, external finance dept MoF, Treasury dept MoF, (and probably central bank) all saw itself as core of new DMO
  - PDC often papering over cracks – no desire for collaboration
  - Treasury may persist in setting up separate front office for cash management – unless integrated
- Semi-independent DMO stretches governance structures
  - Little MoF control, lack of accountability
  - DMO used as an excuse to pay high salaries
  - DMO seen as an end, rather than a means to an end – business planning important
  - Germany joint CEOs – from private and public sector – did not solve problems

# What Goes Wrong - 2

- Running disagreement with central bank
  - Role of TBills and issuance decisions (confusing debt and monetary policy)
  - Data and payment responsibilities (separate copies of DMFAS/CS-DRMS)
  - Fiscal “agent” acts as the “principal” eg for auctions
- Poor balance between front, middle and back office
  - Front office has the exciting tasks; middle office the cerebral tasks; and back office the humdrum tasks.
  - Front office often out of effective middle office control
  - Lack of understanding of operational risk and its importance
- Lack of active or sufficient management.
  - Overstretch, especially when different office cultures pushed together
  - CEO often chosen because of a front office background – a manager is more important [same may apply to relevant minister]