

REPUBLIC OF SRPSKA

GOVERNMENT

**REPUBLIC OF SRPSKA DEBT MANAGEMENT STRATEGY
FOR THE PERIOD 2020-2023**

February, 2021

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1. Goal, scope and assumptions

Republic of Srpska Medium-term debt management strategy (RS MTDS) specifies medium term goals and operations within the debt management, that Republic of Srpska Government intends to implement in the medium term. Implementation of stated measures and activities from the Strategy shall secure desired debt portfolio structure, taking into account cost and risk of the Republic of Srpska Government.

Since regular identification and publishing of the Debt management strategy which goals are based on cost and risk analysis, while taking into consideration macroeconomic and market circumstances and limitations is the key lever for active debt management, the Strategy is continuously monitored and the Republic of Srpska Government is informed annually on its implementation.

The scope of the RS MTDS covers all debt representing direct or indirect obligation of Republic of Srpska¹, with some exceptions.

External debt data include:

- 1) Republic of Srpska debt (except the part of the debt to the Paris Club of creditors-Germany, for which the repayment mechanism has not yet been determined);
- 2) Local self-government units debt, incurred on the basis of Republic of Srpska indirect debt;
- 3) Debt of SOEs and the RS Investment Development Bank (RS IDB), incurred on the basis of Republic of Srpska indirect debt.

Domestic debt data include:

- 1) RS Government debt (verified domestic debt according to the RS Law on domestic debt, debt in the form of treasury bills², medium-term bonds, bank loans and activated guarantees);
- 2) debt of the social security funds, incurred on the basis of Republic of Srpska indirect debt.

Debt (domestic and external) incurred by direct borrowing of local self-government units, social security funds, SOEs and RS Investment Development Bank is not covered by the MTDS, since it represents neither direct nor indirect obligation for Republic of Srpska, hence it cannot be managed by Republic of Srpska Ministry of Finance (RS MoF), on behalf of RS Government. Detailed table on the scope of the RS MTDS is presented in Annex I.

Republic of Srpska debt management goal is to provide financial resources for financing approved investment projects, RS debt refinancing and Republic of Srpska Budget execution, at minimal costs and risks.

¹ In accordance with the RS Law on Borrowing, Debt and Guarantees ("Official Gazette of Republic of Srpska", 71/12, 52/14, 114/17 and 131/20), indirect debt of Republic of Srpska is debt incurred on behalf of debtors (local governments, social security funds, Investment-Development Bank and the funds it manages, public companies and public sector institutions) and is being repaid by Republic of Srpska, from the funds debtors are paying for their relevant debt.

² As of 31 December 2019, there was no debt outstanding in the form of treasury bills, since all issued T-bills were settled until December 31, 2019

The RS MTDS is based on the following assumptions:

- 1) In the medium-term, Republic of Srpska Government will continue with implementation of the fiscal consolidation and reform plan, as presented in the RS Economic Reform Programme 2021-2023 (RS ERP 2021-2023), in order to ensure long term fiscal sustainability and transparency (as stipulated by the Fiscal Discipline Law);
- 2) Projections of macroeconomic indicators and fiscal framework (presented in Table 1 and 2), shown in the RS ERP 2021-2023³ and aligned Medium-term Budget Framework Document for the period 2021-2023 with Republic of Srpska Government policies (RS AMTbfd 2021-2023);
- 3) Any new borrowing where the borrower is Republic of Srpska Government will be contracted in accordance with the Law on Borrowing, Debt and Guaranties, i.e. through the Republic of Srpska Ministry of Finance;
- 4) There will be no recognition (takeover) of debt from other levels of Government;
- 5) Verification and settlement of obligations regulated in the Law on Domestic Debt of the Republic of Srpska (hereinafter: LDD RS) shall be performed in accordance with projection included in RS AMTbfd 2021-2023.
- 6) Central Bank of Bosnia and Herzegovina (CBBH) will continue to maintain monetary stability in accordance with the Currency Board Arrangement, by the provisions of the Law on Central Bank, and will not be issuing any securities in the domestic financial market;
- 7) Credit rating of Bosnia and Herzegovina will not be downgraded within the medium term⁴;
- 8) Institutional investor base in Republic of Srpska domestic financial market will be maintained and broadened in the medium term;
- 9) There will be no significant increase of the European central bank reference rate⁵;
- 10) Creditors will provide funds at acceptable terms;
- 11) Other analytical assumptions used for quantitative analysis of the Strategy shown in Annex II.

³ [ERP RS 2021-2023](#) contains detailed assumptions of macroeconomic projections and fiscal framework, as well as associated risks.

⁴ [Current BH Credit rating](#) is "B/positive outlook" (Standard and Poors) and „B3/stable outlook“ (Moody's). According to the last rating (Moody's) Republic of Srpska credit rating is "B3/positive outlook.

⁵ European Central Bank; [Monetary policy decisions](#)

Table 1: Overview of the macroeconomic indicators for the period 2016-2019, forecast for 2020 and projections for the period 2021-2023

	2016	2017	2018	2019	2020	2021	2022	2023
GDP								
GDP nominal, mil.BAM	9.630,6	10.077,0	10.679,6	11.251,3	10.890,2	11.254,0	11.714,9	12.194,8
Population, in mil.	1,2	1,2	1,1	1,1	1,1	1,1	1,1	1,1
GDP per capita, in BAM	8.320,0	8.739,7	9.303,6	9.848,0	9.557,1	9.902,4	10.335,2	10.787,1
GDP growth, nominal (%)	4,6	4,6	6,0	5,4	-3,2	3,3	4,1	4,1
Inflation - average annual rate	-1,2	0,5	1,2	0,5	-0,9	0,3	0,7	1,1
Real growth rates %								
GDP growth, real	3,5	3,1	3,9	2,5	-3,5	2,6	3,2	3,0
Private consumption	2,4	2,6	2,5	2,8	-3,6	1,7	2,0	2,2
Public consumption	2,3	-0,8	1,8	1,5	2,8	-0,5	1,1	0,7
Gross investments in fixed assets	3,8	-0,7	11,0	-2,1	-6,0	6,0	8,0	7,1
Assumptions:								
Average net salary, in BAM	836,0	831,0	857,0	906,0	952,0	961,0	973,0	985,0
Export of goods, in mil. BAM	2.869,1	3.476,1	3.741,8	3.610,4	3.203,9	3.421,8	3.646,6	3.849,6
Export of goods, annual growth (%)	9,8	21,2	7,6	-3,5	-11,3	6,8	6,6	5,6
Import of goods, in mil. BAM	4.426,9	4.899,1	5.222,3	4.782,2	4.445,6	4.739,9	5.066,1	5.381,6
Import of goods, annual growth (%)	1,3	10,7	6,6	-8,4	-7,0	6,6	6,9	6,2
Export over Import (%)	64,8	71,0	71,7	75,5	72,1	72,2	72,0	71,5
Unemployment rate (%)	24,8	21,0	17,2	11,7	11,0	10,1	9,2	8,4

Source: RS ERP 2021-2023, RS MoF, RS IoS

Table 2: Fiscal framework for the period 2020-2023

	Second Budget Rebalance 2020	Budget 2021	AMTBFD 2022	AMTBFD 2023
A. BUDGET REVENUES (I+II+III+IV)	2.802,2	2.846,8	2.921,1	3.059,3
I Tax revenues	2.570,2	2.586,7	2.695,4	2.828,6
II Non tax revenues	189,5	219,6	225,5	230,4
III Grants	39,0	40,2	0,0	0,0
IV Transfers among the budgetary units	3,5	0,3	0,3	0,3
B. BUDGET EXPENDITURES (I+II+III)	3.070,0	3.052,6	3.068,4	3.133,5
I Current expenditures	2.662,4	2.701,8	2.782,8	2.845,6
II Transfers among the budgetary units	406,5	343,4	280,7	280,4
III Budget reserve	1,0	7,5	4,9	7,5
C. GROSS BUDGET SURPLUS/DEFICIT (A-B)	-267,8	-205,8	-147,3	-74,2
D. NET EXPENDITURES FOR NON-FINANCIAL ASSET	-126,0	-120,8	-122,0	-123,6
E. BUDGET SURPLUS/DEFICIT (C+D)	-393,8	-326,6	-269,3	-197,8
F. NET FINANCING (G+H)	393,8	326,6	269,3	197,8
G. NET PROCEEDS FROM FINANCIAL ASSETS	69,0	81,5	108,1	119,4

Table 2: Fiscal framework for the period 2020-2023

	Second Budget Rebalance 2020	Budget 2021	AMTbfd 2022	AMTbfd 2023
H. NET BORROWING	332,6	278,7	193,5	110,1
I. OTHER NET PROCEEDS	-7,8	-33,6	-32,3	-31,6

Source: RS MoF

2. Existing debt

2.1. Portfolio overview

RS MTDS debt amounts to 4,840.0 million BAM (2,768.9 million USD i.e. 43.0% of GDP) on 31 December 2019. External debt amounts to 69.9% of the total (3,382.3 million BAM or 1,935.0 million USD, i.e. 30.1% of GDP), while domestic debt amounts to 30.1% of the total (1,457.7 million BAM or 833.9 million USD, i.e. 13.0% of GDP).

The external MTDS debt is composed of:

- 1) Relevant external debt, i.e. loans contracted through the BH Ministry of Finance and Treasury, as well as allocated „old” external debt (debt originated before 2 April 1992);
Relevant external debt outstanding amounted to 3,014.1 million BAM on 31 December 2019 (1,724.3 million USD which is 62.3% of total debt, and 26.8% of GDP).
- 2) Direct external debt (debt directly contracted with external creditors by the Republic of Srpska);
Direct external debt outstanding amounted to 368.2 million BAM on 31 December 2019 (210.7 million USD, which is 7.6% of the total debt, or 3.3% of GDP).

Debt contracted with multilateral creditors accounts for the largest share in external MTDS debt (72.8%), followed by bilateral creditors (16.8%), as well as bonds issued at the international market (10.5%). In terms of individual creditors, the largest share in external MTDS debt is towards the European Investment Bank (EIB; 32.1%), World Bank – IDA and IBRD (WB; 31.8%), Paris Club (5.7%), Government of Japan (4.9%), and International Monetary Fund (IMF; 3.0%). In terms of currency composition, EUR and SDR have the largest share, with 65.0% and 22.3%, respectively, JPY participates with 4.9%, USD with 2.9%, while other currencies (KRW, CPU, CHF, SEK, DKK, and CAD) participate with 4.9%.

Domestic MTDS debt is composed of:

- 1) medium-term bonds;
Debt outstanding under medium-term bonds amounts to 867.8 million BAM on 31 December 2019 (496.4 million USD, which is 17.9% of total debt, or 7.7% of GDP). Maturity of bonds issued with amortisation is 5 years, while maturity for bonds with bullet repayment is 5, 7 and 10 years.

2) Domestic commercial bank loans;

Debt outstanding under these loans amounts to 251.1 million BAM (143.6 million USD which is 5.2% of total debt, or 2.2% of GDP). These are amortizing loans with fixed or variable interest rate, 5 to 12 years maturity and 3 months to 3 years grace period.

3) Bonds issued for repayment of debt stipulated by the RS LDD are as follows:

- i) bonds for repayment of war claims with maturity from 13 to 15 years and grace period of 3 to 5 years, with interest rate of 1.5% and amortising repayment;
- ii) amortising frozen foreign currency savings bonds with maturity of 5 years, without grace period, and with interest rate of 2.5%;
- iii) amortising bonds for the settlement of liabilities to suppliers and liabilities under executive court decisions, with a 15 year maturity, 5 year grace period and interest rate of 1.5%;

These bonds are registered at the RS Central Registry of Securities and listed on Banja Luka Stock Exchange. Debt outstanding from these bonds amounts to 260.8 million BAM on 31 December 2019 (149.2 million USD, which is 5.4% of total debt, or 2.3% of GDP).

4) planned bond issuing for repayment fo verified liabilities defined in RS LDD, with 13 year maturity and 3 year grace period, with interest rate 1.5% and amortising repayment;

Outstanding debt under these obligations amounts to 16.9 million BAM (9.7 million USD, which is 0.3% of total debt, or 0.2% of GDP).

5) Cash payments (according to action plan) for settlement of obligations under the executive court decisions related to war damage claims and general liabilities, as stipulated by the RS LDD;

Debt outstanding under this category amounts to 61.2 million BAM on 31 December 2019 (35.0 million USD, which is 1.3% of total debt, or 0.5% of GDP).

Expenditures for 2021-2023 planned in RS AMTBFD 2021-2023 are increased by assessed amount of matured liabilities under planned issuances and cash payments (according to assessed timeframe of verification of war claims, frozen foreign currency savings and general liabilities), which reflects on financing needs.

The most important cost and risk indicators of the existing portfolio are presented in Table 3, while Table 4 shows cost and risk indicators in the period 2014-2019.

Table 3: Cost and risk indicators of the existing portfolio

	External debt	Domestic debt	Total debt
Amount (in million BAM)	3.382,3	1.457,7	4.840,0
Amount (in million USD)	1.935,0	833,9	2.768,9
Nominal value of debt to GDP (%)	30,1	13,0	43,0
Present value of debt to GDP (%)	23,8	13,0	36,7
Cost of debt			
Interest to GDP (%)	0,6	0,4	1,0

Table 3: Cost and risk indicators of the existing portfolio

	External debt	Domestic debt	Total debt
Weighted average interest rate ⁶ , in % (WAIR)	1,9	3,2	2,3
Refinancing risk			
Average time to maturity, in years (ATM)	8,0	3,9	6,8
Debt maturing in 1 year (% of total)	5,7	12,9	7,9
Debt maturing in 1 year (% of GDP)	1,7	1,7	3,4
Interest rate risk			
Average time to refixing, in years (ATR) ⁷	6,2	3,8	5,5
Debt refixing in 1 year (% of total)	28,2	15,8	24,5
Fixed rate debt (% of total)	75,2	95,5	81,3
Currency risk			
External debt (% of total)			69,9
Short-term external debt (% of reserves)			4,6

Source: MoF RS

Table 4: Cost and risk indicators of the existing portfolio at the end of 2014 and values in the period 2015-2019

	2014	2015	2016	2017	2018	2019
Nominal value of debt to GDP (%)	48,0	48,3	49,8	45,5	43,8	43,0
Present value of debt to GDP (%)	41,4	41,1	42,4	39,2	37,1	36,7
Cost of debt						
Interest to GDP (%)	1,0	1,1	1,2	1,0	1,0	1,0
Weighted average interest rate, in % (WAIR)	2,1	2,2	2,3	2,2	2,3	2,3
Refinancing risk						
Debt maturing in 1 year (% of total)	10,2	12,1	13,7	16,0	10,4	7,9
Debt maturing in 1 year (% of GDP)	4,9	5,8	6,8	7,3	4,6	3,4
Average time to maturity of external debt, in years (ATM)	7,7	7,6	7,8	8,0	8,0	8,0
Average time to maturity of domestic debt in years (ATM)	4,2	3,2	3,4	3,4	3,5	3,9
Average time to maturity of total debt in years (ATM)	6,6	6,1	6,3	6,4	6,7	6,8
Interest rate risk						
Average time to refixing, in years (ATR)	4,4	4,1	4,6	4,8	5,4	5,5
Debt refixing in 1 year (% of total)	46,1	45,4	42,0	38,2	28,4	24,5
Fixed rate debt (% of total)	60,7	62,5	66,0	71,9	78,6	81,3
Currency risk						
External debt (% of total)	67,7	68,0	66,6	64,1	71,2	69,9
Short term external debt (% of foreign reserves)	5,7	7,4	9,2	8,1	5,8	4,6

Source: RS Mof

The composition of Republic of Srpska debt analyzed under the MTDS (RS MTDS debt) is mostly the result of the basic debt management principle implemented in the past, which is maximization of external concessional borrowing. Therefore, the RS MTDS debt portfolio is characterized by a high share of external debt with relatively long maturities and low average implied interest rate.

⁶Weighted average interest rate is calculated as a ratio of aggregate interest payments to aggregate debt outstanding under each instrument at the end of 2019, with total outstanding debt of all instruments at the end of 2019.

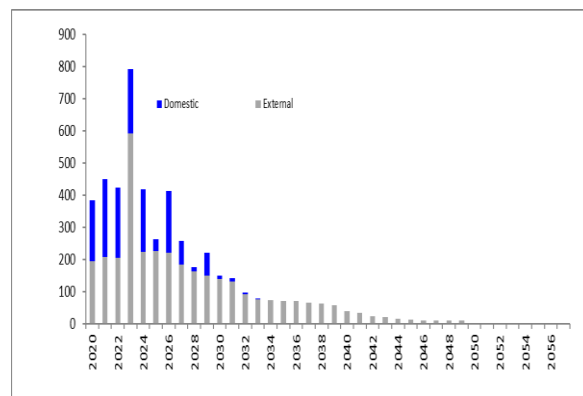
⁷Average time to refixing, ATR.

Overall, existing portfolio is associated with low costs. The weighted average interest rate of the total portfolio is 2.3%, external portfolio 1.9% and domestic portfolio 3.2%. This is mainly the reflection of external concessional loans and low interest rates on bonds issued for reconciliation of domestic debt obligations, defined by the RS LDD.

Exchange rate risk is moderate. Out of the total portfolio, 45.4% is denominated in EUR, while 30.1% is denominated in BAM. Under the current currency board arrangement, with BAM pegged to EUR, only 24.5% of the portfolio is exposed to exchange rate risk (or 19.6% after SDR decomposition and excluding the debt in EUR). In USD is denominated 2.0% of the portfolio (or 8.5% after SDR decomposition), which impose some risk, having in mind historical volatility of the USD against the EUR, as well as projections for the future.

Refinancing risk and refixing risk is moderate. Fixed rate instruments stand for 81.3% of the total portfolio. Average time to maturity of the portfolio is 6.8 years. Average time to maturity of external portfolio is 8.0 years, as a result of long-term concessional loans, while average time to maturity for domestic debt is 3.9 years. Redemption profile of existing debt, presented in the Chart 1, shows the peak in 2023, as a result of significant amounts coming due on the basis of external debt (17.5% of the total MTDS external debt), mainly bonds issued at the international market, as well as beginning of repayment for several tranches of EIB loans and bullet repayment of the tranche provided by European Commission.

Chart 1. Repayment profile of the existing portfolio



Source: RS MoF

Maintaining cost and risk indicators at a relatively low level is the challenge for RS, considering the change in the structure of financing sources. The current debt portfolio is characterised by relatively favorable cost and risk indicators, as a result of significant use of the concessional financing sources, as well as bonds issued for reconciliation of domestic debt obligations with a relatively low costs and long maturities. As concessional financing sources are expected to be less available in the future, there will be a need for increased reliance on commercial funds from external and domestic sources, provided that increase in costs and risks is at the acceptable level.

2.2. Strategy implementation in 2018 and evaluation of identified debt indicators

Debt management in 2019 was conducted in accordance with the guidelines defined by the Debt Management Strategy for the period 2018-2021 (MTDS 2018-2021), which has been adopted by the Republic of Srpska Government in September 2018.

For the purpose of achieving the main debt management goal, defined in the MTDS 2018-2021, i.e. providing necessary financial resources, in 2019 investment projects were financed mainly from external concessional sources, while budget consumption was financed mainly from domestic sources, in the form of securities issued at the domestic market, as well as from loans

provided by domestic banks, and in part from external sources i.e. loans issued by international financial institutions.

Out of the total financing in 2019, 40.6% was provided through the external instruments (where 77.6% were fixed out of which 74.0% in EUR), while 90.9% was provided through fixed instruments. In terms of currency composition of total financing in 2019, 59.4% was denominated in BAM, 30.0% was denominated in EUR, while 10.6% was denominated in other foreign currencies except EUR in other foreign currencies.

In terms of financing sources for budget consumption in 2019, 8.5% was provided through external variable instruments (5.5% of the total financing), while 91.5% was provided through external and domestic fixed instruments (59.4% of the total financing). With regards to the currency composition of financing the budget consumption in 2019, 91.5% was denominated in BAM, while 8.5% was denominated in EUR.

The following table shows budget spending financing structure in 2019 planned in MTDS 2018-2021, and realised financing in 2019, per instrument.

Table 5: Financing structure for budget spending planned in MTDS and realised in 2019, per instrument

Instrument	Planned	Realised
External variable EUR	3,9%	8,5%
IMF variable USD	27,0%	0,0%
Domestic loan 5y fix	0,0%	22,0%
Domestic bonds 5y fix	26,5%	27,4%
Domestic bonds 7y fix	23,7%	27,0%
Domestic bonds 10y fix	18,9%	15,1%
	100,0%	100,0%

Source: RS MoF

Strategy planned financing of budget spending in 2019 was realised in the amount of 120.1%, where the realisation of external variable instruments is in the amount of 33.1% (denominated in EUR 265.0%), and domestic fixed is in the amount of 159.0%.

Out of total financing realised in 2019 for investment projects, 89.8% was acquired through external fixed instruments (31.5% of total financing), and 69.9% was denominated in EUR (24.5% of total financing).

Following table shows financing structure of investment projects in 2019 planned in MTDS 2018-2021, and realised financing in 2019, per instruments.

Table 6: Financing structure of investment projects planned in MTDS 2018-2021 and realised financing in 2019, per instrument

Instrument	Planned	Realised
External variable EUR	10,6%	10,2%
External fix USD	37,1%	30,1%
External fix EUR	52,3%	59,7%
	100,0%	100,0%

Source: RS MoF

In relation to strategy planned financing of investment projects in 2019, amount of 104.5% was realised where realisation of external variable instruments (nominal in EUR) is in the amount of 101.0%, and external fixed is 104.9% (nominal in EUR in the amount of 119.2%, and other foreign currencies except EUR in the amount of 84.8%).

In 2019 possibility for selecting conditions for withdrawing tranches existed with 4 tranches, realised under 4 previously approved loans (51.2 of external financing, i.e. 20.8% of total financing), and for all that 4 tranches the fixed interest rate was chosen, and weighted average interest rate was 1.3%.

In 2019 National Assembly of the Republic of Srpska accepted borrowing through two new external borrowing, both nominal in EUR, with variable interest rate (one borrowing has the possibility of selecting fixed interest rate upon withdrawing). Effects of mentioned borrowing on debt structure will be realised in the following period when the funds are withdrawn.

In 2018, Republic of Srpska Ministry of Finance initialised the procedure for fixing the interest rate for 6 World bank loans (International Bank for Reconstruction and Development - IBRD) which had such possibility, having in mind the guideline defined by the Debt Management Strategy, with regards to managing the interest rate risk, defining that share of fixed rate debt should be above 60% of the total debt. Republic of Srpska Ministry of Finance initiative was supported by the Federal Ministry of Finance and Ministry of Finance and Treasury, and in 2018 the request for interest rate conversion was submitted to the World Bank. Conversion was approved in 2019, with weighted average interest rate at 1.8%.

The following table shows debt structure indicators identified by the Strategy, their target values and their values at the end of 2015-2019 period (at the end of each year).

Table 7: Identified debt structure indicators and their values in 2015-2019

Goal	Indicator	Strategy defined	Values				
			end-2015	end-2016	end-2017	end-2018	end-2019
Foreign exchange risk							
	External debt, excluding debt in EUR (% of total)	≤ 35	32,6	30,6	26,5	25,9	24,5
Domestic market development							
	Domestic debt (% of total)	≥ 25	32,0	33,4	35,9	28,8	30,1
Refinancing risk							
	ATM (years)	≥ 4	6,2	6,3	6,4	6,7	6,8
	Short term debt - original maturity (% of last year revenues)	≤ 8	5,4	5,5	3,3	0,0	0,00
Interest rate risk							
	Fixed rate debt (% of total)	≥ 60	62,5	66,0	71,9	78,6	81,3
Cost of debt							
	WAIR ⁸ (%)	≤ 3,5	2,3	2,3	2,2	2,3	2,3

Source: RS MoF

In 2019, comparing to previous four years, refinancing risk is decreasing (measured by average time to maturity and share of short term debt in last year revenues), as well as interest rate risk (measured by fixed rate debt as % of total), foreign exchange risk (measured by the share of external debt, excluding debt in EUR, in total), and as well cost of debt (measured by weighted average interest rate). In the last five years, all strategy defined indicators of debt structure showed favourable trend, except in 2018, when, comparing to 2017, share of domestic debt in total debt deteriorated (as a result of replacing domestic with external instruments, mainly securities issued at the international market), as well as weighted average interest rate which slightly increased, but still remaining at low level.

3. Source of financing

In the medium term, the Strategy is focused on financing mainly through issuing of securities on domestic and international financial markets. According to the development of the Republic of Srpska, concession multilateral and bilateral financing sources will be available in the monitored period in small amounts and will be mainly used for financing investment projects. Also, important to point out is that in order to receive concession funds, certain objectives at Bosnia and Herzegovina level are to be fulfilled, which could be a limiting factor.

Following table indicates external financing sources included in the Strategy.

⁸See footnote 8.

Table 8: External financing sources

Creditor name	Interest rate	Maturity	Grace period	Currency	Risk
IBRD	variable/fix	15-32	5-7	EUR	refixing risk for variable interest rate
EIB	variable / fix	25-30	5-8	EUR	refixing risk for variable interest rate
EBRD	variable	15	3	EUR	refixing risk for variable interest rate
KfW	fix	9-16	0,5-7	EUR	refinancing risk
IMF	variable	5	3	SDR	refinancing risk; refixing risk for variable interest rate; foreign exchange risk for SDR
Eurobonds	fix	5	4	EUR	refinancing risk
European Commission ⁹	variable/fix	n/a	n/a	EUR	refixing risk for variable interest rate
Other	variable/fix	18-31	3-10	EUR/SDR/JPY	refixing risk for variable interest rate; foreign exchange risk for SDR and JPY

Source: RS MoF

Domestic financing sources are mainly used for financing budget expenditures. Entities investing in securities i.e. bonds (maturity 3, 5, 7 and 10 years with bullet repayment and fixed interest rate) and in T-bills (maturity 6 and 12 months) are investors with the head office predominantly in Bosnia and Herzegovina. Along with BH domestic investor base expanding, lately we have an increase of foreign investors' interest outside of Bosnia and Herzegovina. Investors are mainly domestic banks, but also insurance companies, funds and others. Bank limits are to be taken into consideration, meaning their exposure to public sector, especially considering that fiscal deficit in 2020 caused by the COVID-19 pandemic was mainly financed by domestic market funds. At last it is important to mention potential financing limitations regarding projected budget deficit in 2021-2023. Bonds and T-bills trading on secondary market was made available, but such trading is limited. Most often trade done on secondary market is the trade of bonds for war damage claims, frozen foreign currency savings and general liabilities. Development of the secondary securities market is one of the conditions for attracting investors, which could at the same time decrease the interest rate. Along with mentioned securities, Republic of Srpska has the possibility to use loans from domestic banks as a financial instrument.

When selecting market for borrowing, borrowing currency and financing instrument in the monitored period, development status and trend of domestic and international financial markets will be taken into consideration (meaning level of interest rates, premiums, risks, yield curve and similar). Also acceptable risk exposure will be taken into consideration.

Debt management policy will be led by achieved goals, mainly by identified long-term goals, but decisions on short-term and medium-term borrowing will be adopted annually in accordance

⁹ Repayment conditions will be selected upon withdrawal, where maximum average maturity is up to 15 years.

with provision of the Law on Borrowing, Debt and Guarantees of the Republic of Srpska. Change of borrowing plan during the fiscal year is possible depending on changes of general fiscal aggregates and contingencies¹⁰.

4. Medium term debt management strategy

The main RS debt management goal is to provide financial resources for financing the approved investment projects, RS government debt refinancing and RS budget execution, at minimal costs and risks.

In order to achieve the debt management main goal, the following operative goals and principles of borrowing are defined:

- 1) Continuous promotion and presence on domestic and international financial markets through issuing of securities and other instruments which could eventually lower the borrowing costs in medium and long-term;
- 2) Provide debt portfolio in accordance with previously identified indicators of debt structure – maturity profile, interest rate structure, borrowing costs, domestic debt balance, currency risks exposure (notwithstanding debt in EUR due to currency board arrangement) and its targeted amounts;
- 3) Continue to conduct transparent and predictable borrowing process.

In the following medium term period (2019-2022), the above mentioned goals will be achieved through the Strategy of *diversifying financing sources, instruments and investor base*. This strategy is based on financing of budget expenditure by mainly issuing of medium-term securities on international and domestic markets, with bullet repayment, and in a lesser amount by domestic and external loans. For financing investment projects, external financing sources are used as a result of maximum exploitation of access to concessional sources (WB, EIB, EBRD, KfW, CEB, etc.), which lowers refinancing risks and cost. Average share of domestic sources is lowered due to increase of external sources financing.

This Strategy improves the Republic of Srpska's position regarding future sources of financing, mainly by entering on international financial market, development of domestic financial market through usage of short and medium-term instruments, with focus on instruments with longer maturity, along acceptable increase of costs and risk levels, which is mitigated by continuous usage of available support of multilateral creditors.

Following table indicated stylised instruments for financing debt portfolio, their share in gross financing for 2020-2023, and their projected share in debt portfolio at the end of 2023.

¹⁰ Contingency such as COVID-19 pandemic

Table 9: Stylised instruments for financing debt portfolio, their share in gross financing for 2020-2023, and their projected share in debt portfolio at the end of 2023

Instrument name	Maturity	Grace period	% of portfolio at end-2019	% of gross financing needs					% of portfolio at end-2023
				Average	2020	2021	2022	2023	
External variable USD (concessional)	18	4	1,8	0,0	0,0	0,0	0,0	0,0	0,6
External variable EUR (concessional)	18	4	13,4	12,5	5,6	21,2	14,4	8,7	14,0
External fix USD (concessional)	20	5	20,6	3,7	11,5	3,5	0,3	0,2	12,9
External fix EUR (concessional)	20	5	25,2	12,4	4,7	3,2	40,0	7,6	22,4
IMF variable USD (concessional)	5	3	2,1	6,4	27,8	0,0	0,0	0,0	4,8
Eurobonds fix EUR (market)	5	4	6,8	39,1	0,0	66,4	0,0	71,5	23,0
Domestic loans variable (market)	6	1	1,3	0,0	0,0	0,0	0,0	0,0	0,1
Domestic loans fix (market)	8	1	2,1	2,7	5,1	0,0	7,4	0,0	1,4
Domestic T-bills fix (market)	1	0	0,0	4,3	12,2	1,1	3,6	1,7	0,3
Domestic bonds 3y fix (market)	3	2	5,9	1,4	0,0	0,8	4,6	0,9	1,6
Domestic bonds 5y fix (market)	5	4	6,5	9,7	25,8	0,0	12,6	3,9	7,3
Domestic bonds 7y fix (market)	7	6	4,9	4,3	3,9	1,7	9,2	3,5	4,8
Domestic bonds 10y fix (market)	1	9	9,4	3,6	3,4	2,1	8,0	2,0	6,7
External sources			69,9	74,1	49,5	94,3	54,6	88,0	77,8
Domestic sources			30,1	25,9	50,5	5,7	45,4	12,0	22,2

Source: RS MoF

Standard cost indicators and strategy risks are shown in the following table.

Table 10: Cost indicators and strategy risks at end-2023

	Initial 2019	Strategy 2023
Debt/GDP (%)	43,0	53,1
Debt PV/GDP (%)	36,7	46,9
Cost of borrowing		
Interest/GDP (%)	1,0	1,3
Weighted average interest rate, in % (WAIR)	2,3	2,5
Refinancing risk		
Debt maturing in 1 year (% of total)	7,9	7,2
Debt maturing in 1 year (% of GDP)	3,4	3,8
Average time to maturity for external debt, in years (ATM)	8,0	6,6

Table 10: Cost indicators and strategy risks at end-2023

	Initial 2019	Strategy 2023
Average time to maturity for domestic debt, in years (ATM)	3,9	3,3
Average time to maturity for total debt, in years (ATM)	6,8	5,8
Interest rate risk		
Average time to refixing, in years (ATR)	5,5	4,6
Debt refixing in 1 year (% of total)	24,5	25,6
Fixed rate debt (% of total)	81,3	80,5
Currency risk		
External debt (% of total)	69,9	77,8
External debt excluding debt in EUR (% of total)	24,5	18,0
Short-term external debt (as % of reserves)	4,6	4,6

Source: RS MoF

At the end of observed four year period comparing to the situation at end-2019 indicators of solvency, liquidity, refinancing risks, interest rate and currency risk will be slightly deteriorated, which is the result of financing sources structure change, and projected deficit for 2020-2023.

During the strategy implementation, all borrowing activities will be performed in accordance with the following best practice principles, as follows:

- 1) activities at the domestic and international financial market will be performed professionally, transparently, expediently and in a timely manner, while contracted obligations will be fulfilled in the due time and amount;
- 2) selection of the borrowing conditions will be (in priority order) focused at government debt refinancing, providing funds for financing the budget execution, compliance with the debt covenants set in the Fiscal Discipline Law and achievement of the identified debt indicators;
- 3) when planning borrowing activities, attention will not be focused on the comparative short term advantages of each specific borrowing transaction, but rather on the development and enhancement of long term borrowing opportunities in financial market;
- 4) in general, the most favourable borrowing terms and conditions will be ensured, while taking into account principle under 2).

In order to implement the preferred strategy, following basic tasks of the RS MoF have been set out:

- 1) developing and maintaining relations with partners and investors at the domestic and international market;
- 2) designing and, if necessary, revising medium term Borrowing Plan and Auctions calendar based on the cash flow, in order to ensure stable model of total budget inflows on monthly basis;

- 3) publishing auction calendar on the quarterly basis and, whenever possible, providing information on planned issuances for a longer time period, as well as medium term borrowing plan;
- 4) continuously maintaining the offer of short term and medium term financial instruments at the domestic financial market, ensuring that instruments and procedures are efficient and favourable for primary trading in order to facilitate the development of domestic securities market;
- 5) monitoring the debt portfolio in relation to identified debt indicators and reporting on their values on an annual basis;
- 6) analysing opportunities and harmonise practices and procedures related to domestic securities market with those of EU, if it's feasible in medium-term,
- 7) managing Republic of Srpska credit rating process providing necessary participation of line institution representatives.

In order to decrease exposure to financial risks following measures should be implemented:

- 1) prolonging average debt maturity issued as securities, as much as possible regarding the situation on domestic and international market,
- 2) prolonging average domestic debt maturity,
- 3) decrease of external debt share nominal in other currency except EUR,
- 4) equal allocation of debt repayment obligations per years in future long-term period.

In accordance with the defined objectives and basic principles of debt management, considering debt structure, change of financing structure and situation at the financial markets, previously defined debt structure indicators their values will not be changed, as shown in the Table 7.

MINISTER
Zora Vidović

Annex 1. Scope of the RS MTDS

		Included (✓) / Excluded (X)	Reasoning behind including into MTDS	Amounts as of 31/12/2019	
				mil. BAM	mil. USD ¹¹
1	Total debt (1.1.+1.2.+2a)		100,0%	5.388,5	3.082,7
1.1.	External debt		63,4%	3.415,5	1.954,0
1.1.1.	Republika Srpska			2.122,0	1.214,0
1.1.1.1.	“Relevant” external debt	✓	Direct liability with clear repayment obligation	1.784,0	1.020,6
1.1.1.2.	“Relevant external debt” - Paris Club Germany	X	Direct liability with repayment method not defined yet	9,1	5,2
1.1.1.3.	Direct external debt	✓	Direct liability with with clear repayment obligation	328,9	188,2
1.1.2.	Local self-government units			128,4	73,5
1.1.2.1.	“Relevant” external debt	✓	Indirect liability with clear repayment obligation	104,3	59,7
1.1.2.2.	Direct external debt	X	Neither direct nor indirect liability	24,1	13,8
1.1.3.	SOEs and Investment Development Bank			1.165,1	666,5
1.1.3.1.	“Relevant” external debt	✓	Indirect liability with clear repayment obligation	1.125,8	644,0
1.1.3.2.	Direct external debt	✓	Indirect liability with clear repayment obligation	39,3	22,5
1.2.	Domestic debt		36,6%	1.970,4	1.127,2
1.2.1.	Republika Srpska			1.451,4	830,3
1.2.1.1.	Verified domestic debt			338,8	193,8
1.2.1.1.1.	Issued bonds (frozen foreign currency savings, war claims, general liabilities)	✓	Direct liability with with clear repayment obligation	260,8	149,2
1.2.1.1.2.	Planned bond issuances (war claim bonds)	✓	Direct liability with with clear repayment obligation	16,9	9,7
1.2.1.1.3.	Cash payments (general liabilities, war claims, frozen foreign currency savings, tax refunds)	✓	Direct liability with with clear repayment obligation	61,2	35,0
1.2.1.2.	Medium-term bonds	✓	Direct liability with with clear repayment obligation	867,8	496,4
1.2.1.3.	T-bills	✓	Direct liability with with clear repayment obligation	0,0	0,0
1.2.1.4.	Commercial bank loans	✓	Direct liability with with clear repayment obligation	244,8	140,1
1.2.2.	Local self-government units	X	Neither direct nor indirect liability	316,0	180,8
1.2.3.	Social security funds			203,0	116,1
1.2.3.1.	Direct debt	X	Neither direct nor indirect liability	199,4	114,0
1.2.3.2.	Indirect debt	✓	Indirect liability with clear repayment obligation	3,6	2,1
2	Guaranties (a+b+c)			578,9	331,2
a	Activated RS guaranties	✓	Called guaranties included in debt	2,6	1,5
b	Inactivated RS guaranties	X	Guaranties yet to be called	576,3	329,7
c	Implicit RS guaranties	X	Debt of SOEs and municipalities and other forms of implicit guaranties	0,0	0,0
3	Total debt included in MTDS		89,8%	4.840,0	2.768,9
4	Total debt excluded from MTDS		10,2%	548,6	313,8

Source: RS MoF

¹¹Values in USD based on the exchange rate USD /BAM = 1,747994, in accordance with Currency exchange No. 257 of the Central Bank of Bosnia and Herzegovina, as of 31 December 2019.

Annex 2. Analytical underpinnings

This section presents other analytical underpinnings used for quantitative strategic analysis. Debt service projections are generated for each strategy under the baseline and alternative scenarios, applying interest rate and exchange rate shocks. Costs are calculated based on the debt service profile generated under the baseline scenario, while risk is measured as debt service increase due to the interest rate and exchange rate shocks applied.

Baseline scenario is based on most probable market condition. Following table includes projections for interest rates of stylised instruments and foreign exchange rate in 2020-2023, used in baseline scenario.

Table: Projection for interest rates of stylised financing instruments and foreign exchange rate in 2020-2023

	2020	2021	2022	2023
Stylised instruments				
External Var USD (concessional)	1,4%	1,6%	1,7%	1,8%
External Var EUR (concessional)	0,8%	0,9%	1,0%	1,1%
External Fix USD (concessional)	2,9%	3,3%	3,5%	3,7%
External Fix EUR (concessional)	1,8%	1,8%	1,9%	2,0%
IMF Var USD (concessional)	1,1%	1,2%	1,4%	1,5%
Eurobonds fix EUR (market)	4,9%	5,3%	5,7%	6,0%
Domestic loans variable (market)	2,3%	2,4%	2,5%	2,6%
Domestic loans fix (market)	3,5%	3,5%	3,6%	3,7%
Domestic T-bills fix (market)	1,0%	0,9%	0,9%	0,9%
Domestic bonds 3y fix (market)	1,8%	1,7%	1,8%	1,9%
Domestic bonds 5y fix (market)	2,5%	2,5%	2,6%	2,7%
Domestic bonds 7y fix (market)	3,0%	3,1%	3,1%	3,2%
Domestic bonds 10y fix (market)	3,5%	3,6%	3,6%	3,7%
Exchange rate				
BAM/USD	1,79%	1,81%	1,81%	1,81%

Source: RS MoF and BiH MoFT

For the purpose of sensitivity analysis of the strategies, following shocks are applied:

- **Exchange rate shock:** 30% depreciation against USD in 2021, comparing to the initial exchange rate projection for the same year;
- **Interest rate shock:** comparing to the baseline scenario, in 2021 it has been applied 4% increase in interest rate for medium-term domestic and long-term external instruments and 2% increase in interest rate for short-term domestic instruments;

- **Combined shock:** comparing to the initial projection, it has been applied 20% depreciation against USD in 2021, combined with 2% interest rate shock in 2021 for medium-term domestic and long-term external instruments, as well as 1% interest rate shock for short-term domestic instruments.