



NEW ZEALAND
DEBT MANAGEMENT

New Zealand Government Securities Funding Strategy

2022/23: Edition 1

Te Kāwanatanga o Aotearoa
New Zealand Government



TE TAI ŌHANGA
THE TREASURY

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2022/23 Funding Strategy – at a glance

The objective of New Zealand Debt Management (NZDM) is to minimise the Crown’s borrowing costs over the long-term with due consideration to risk, while ensuring ongoing access to debt funding markets.

Core principles and achieving a balance between the following three goals:



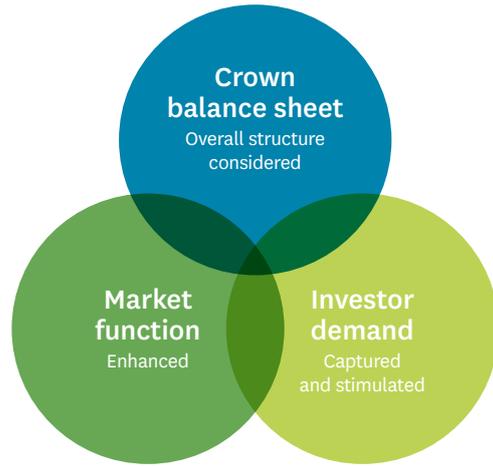
Even-handed



Consistent



Transparent



New Zealand Government Securities Market

Nominal Bonds:

Remains the primary funding instrument. For the 2022/23 fiscal year, issuance will be across multiple points on the curve, with a focus on building up benchmark bond lines.

Green Bonds:

New Zealand will issue its first Sovereign Green Bond in late 2022, with details of the framework available in September 2022 quarter. Green Bonds are nominal bonds issued in a green format.

Inflation-Indexed Bonds (IIBs):

More flexible approach to issuance and new single price auction method are in operation. Further steps to improve market function include: a tap syndication of the 2035 IIB alongside a buyback of the 2025 IIB is expected prior to 31 December 2022, along with individual IIB line capacity limits raised to NZ\$10 billion.

Treasury Bills (T-Bills):

Short-term (less than 1 year) issuance to provide flexibility in addressing short-term liquidity requirements. Fortnightly tenders, with NZ\$3 billion of T-Bills on issue forecast for end-June 2023.

European Commercial Paper (ECP):

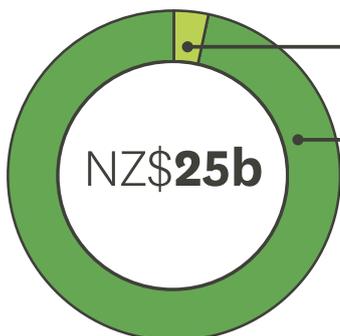
Short-term foreign currency issuance is steady to maintain market presence and provide optionality to increase in certain scenarios.

Foreign Currency (EMTN):

Programme documentation remains current but unutilised for more than 10 years. There is a preference is to support activity in NZD products.

2022/23 New Zealand Government Bond (NZGB) programme forecasts

Gross NZGB issuance

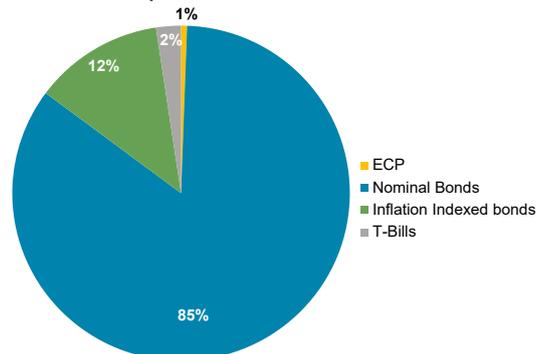


Product type

circa NZ\$1.5-3b Inflation-index bonds

circa NZ\$23b Nominal bonds, including Green Bonds

NZGS portfolio 30 June 2022



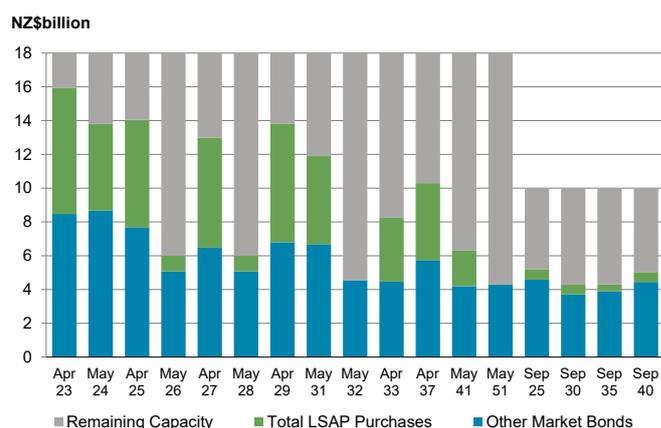
New Zealand Debt Management (NZDM) is a function within the Treasury¹ and is responsible for managing the Crown's² net cash flows and liquidity position. This document covers recent developments in the New Zealand Government Securities (NZGS) Market and updates NZDM's Funding Strategy for the 2022/23 year.

Recent Developments

Since the last Funding Strategy publication in February 2022, recent developments include:

- Macroeconomic Backdrop:** The New Zealand economy has continued to display resilience to COVID-19. While the economy contracted in the March quarter in response to the Omicron outbreak, easing border restrictions and robust investment are expected to support growth in 2022. The unemployment rate remains near record lows, while inflation reached a three-decade high of 7.3%. That said, tighter monetary policy, to dampen inflation, is expected to slow economic growth over time.
- Monetary Policy:** The Reserve Bank of New Zealand (RBNZ) has raised the Official Cash Rate (OCR) in seven consecutive meetings, with the OCR now at 3.0%. The RBNZ has projected the OCR to increase to around 4.0%. The RBNZ has also [announced](#) that it intends to reduce their Large Scale Asset Purchase (LSAP) holdings by selling NZGBs back to NZDM at a rate of NZ\$5 billion per fiscal year, beginning with the longest maturity, and allow shorter-maturity bonds to mature without reinvestment. The RBNZ's first sale of NZGBs to NZDM was in July 2022, with the RBNZ expecting LSAP NZGB holdings to reduce to zero in mid-2027.
- Fiscal Outlook:** As the temporary fiscal support measures in response to COVID-19 largely wind up in 2022/23, along with growth in tax revenue, the operating balance before gains and losses (OBEGAL) is expected to return to surplus in 2024/25. Although higher forecast expenses at the *Budget Economic and Fiscal Update* (BEFU) results in the return to surplus being one year later than previously forecast. Net debt is forecast to peak nominally at NZ\$84 billion in 2023/24 (19.9% of GDP), before declining to 15% of GDP by 2025/26. The core Crown cash shortfall is forecast to total NZ\$13 billion over the period 1 July 2022 to 30 June 2026.

NZGB portfolio and LSAP holdings



Source: The Treasury

- Fiscal Rules:** As the Government's response to COVID-19 has evolved and the economy has recovered, the Government has adopted two new fiscal rules:
 - returning OBEGAL to surplus by 2024/25, then maintaining an average surplus from 0% to 2% of GDP, as the primary fiscal rule
 - a net debt ceiling of 30% of GDP, that complements the OBEGAL target.

BEFU core Crown borrowing programme

Year ending 30 June (facevalue)	2022 (Actual)	2023 ³	2024	2025	2026	Total
Gross NZGB issuance (NZ\$billions)	20	25	25	25	15	110
NZGB maturities and repurchases (NZ\$billions)	0	22.9	18.8	20.2	17.8	79.7
Net NZGB issuance (NZ\$billions)	20	2.1	6.2	4.9	-2.8	30.3
NZGBs outstanding (NZ\$billions)	147.2	149.3	155.5	160.4	157.6	n/a
NZGBs outstanding (% of GDP)	40%	37%	37%	36%	34%	n/a
Forecast T-Bills on issue (NZ\$billions)	4	3	3	3	3	n/a

Source: The Treasury

1 The Treasury is the Government's lead economic and financial adviser. The Treasury provides advice to the Government on its overarching economic framework, on its fiscal strategy and on achieving value for money from its investments.
 2 The Crown is the Head of State of New Zealand. New Zealand Government Securities are issued in the name of "Her Majesty the Queen in right of New Zealand".
 3 Adjusted for actual repurchases and maturities in 2021/22.

- Borrowing Programme:** At BEFU, the forecast New Zealand Government Bond (NZGB) programme for 2022/23 was set at NZ\$25 billion, NZ\$7 billion higher than forecast at the prior *Half Year Economic and Fiscal Update* (HYEFU). NZGB borrowing programmes in future years were increased by a further NZ\$19 billion. Of the NZ\$26 billion total increase in forecast borrowing programmes, NZ\$20 billion was due to the repurchases of LSAP NZGBs, while the remaining NZ\$6 billion is due to the slight deterioration in the fiscal outlook. NZGBs purchased from the RBNZ will be retired. The entire borrowing programme will be issued according to the NZDM funding strategy, independent of bond maturities repurchased from the RBNZ.
- Liquidity Management:** A gradual reduction in cash and liquid assets is forecast. Cash and liquid assets are forecast to reach close to the **NZ\$15 billion minimum liquidity buffer** after the April 2023 nominal bond maturity.
- Green Bond Programme:** The green bond framework is expected to be released in the September 2022 quarter, with the inaugural syndication following in late 2022 subject to market conditions.
- IIB Issuance Approach:** The more flexible approach to issuance and change to the single-price auction mechanism is now in operation. At BEFU, we announced further steps to increase investor participation and improve turnover in the IIB market:
 - higher individual line capacity limits of NZ\$10 billion
 - a tap syndication of the 2035 IIB alongside buyback of 2025 IIB is expected in August 2022.

World government bond index (WGBI): In April, FTSE-Russell announced that the New Zealand fixed-rate government bond market met the market size required for entry into the WGBI as of the March 2022 review. Nominal NZGBs will be included in the WGBI from 1 November 2022. FTSE-Russell project NZGBs will comprise approximately 0.20% of the index.

Funding Strategy Principles

NZDM's primary objective is to minimise the Crown's borrowing costs over the long-term with due consideration to risk, while ensuring a well-functioning market for New Zealand Government securities (NZGS).

For the NZGB market, meeting this objective is currently best achieved by taking a strategic, rather than short-term tactical approach to funding activities. NZDM aims to smooth the Crown's borrowing through time to reduce the variability in annual programmes which could impact market function.

Delivery of funding activity is underpinned by the core principles of transparency, consistency and even-handedness, and future actions are communicated in a timely manner.

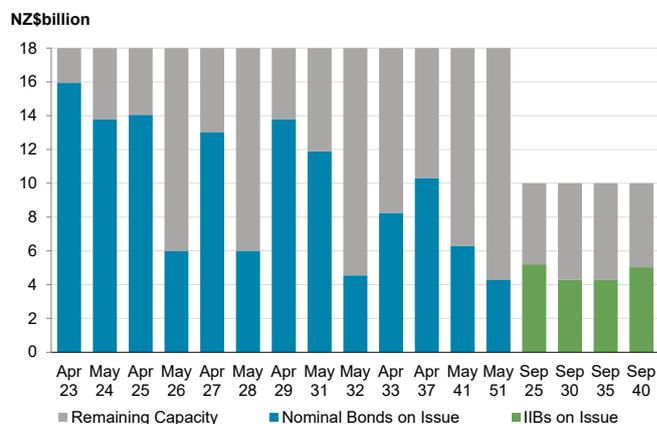
The funding strategy aims to balance three key goals:

- Considering the overall structure of the Crown's balance sheet.
- Capturing and stimulating investor demand.
- Promoting well-functioning and liquid NZGS markets.

Wholesale Funding Strategy 2022/23

Term Funding

NZGB portfolio 30 June 2022



Source: The Treasury

Gross issuance for 2022/23 is set at NZ\$25 billion, up from NZ\$20 billion in 2021/22. Two syndications are planned before 31 December 2022:

1. A tap syndication of the 2035 IIB, alongside a buyback of the 2025 IIB.
2. The inaugural green bond.

Issuance of existing NZGBs will also be via our weekly tenders and spread across multiple bonds. NZGBs are not issued via private placements, which is considered inconsistent with the core principles of transparency, consistency and even-handedness.

Only **Registered Tender Counterparties** (RTC) are able to participate in tenders and eligible for syndicate panels. To qualify as an RTC, an intermediary must play a significant role in intermediation of NZGS to investors, as well as commit to supporting secondary market liquidity and price transparency.

Nominal Bonds

Nominal bonds continue to be the primary funding instrument. Nominal bond line capacity remains capped at NZ\$18 billion which balances the need to promote liquidity in each security, while managing the size of maturity cash flows and refinancing risk.

The NZGB nominal portfolio is constructed to:

- accommodate demand at different points on the curve which contributes to a diversified investor base
- target tender issuance into the 5-year, 10-year, and 30-year benchmark securities
- aim to build new bond lines quickly to at least NZ\$4 billion
- ensure regular spacing between bond lines across the yield curve. One-year gaps are typical out to 10 years. The spacing between maturities increases to 3-4 years for longer tenors, which is conditional on future funding requirements.

Details of the upcoming month's tender schedule are published in advance to provide market participants with as much certainty as possible, while maintaining some flexibility to adjust the issuance profile throughout the year. At each weekly tender, multiple bond lines are offered to cater to a range of investor demand.

Green Bonds

Green Bonds, which are nominal bonds issued in a green format, are expected to be an enduring part of the NZGB portfolio. Sovereign Green Bonds will help ensure high quality Government projects with robust environmental outcomes are financed, delivered, monitored and reported on.

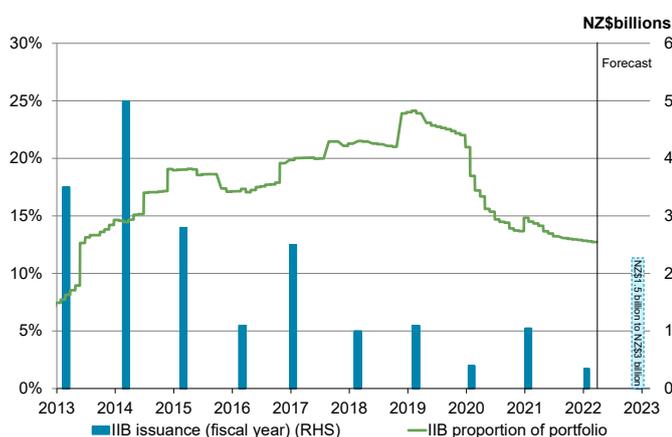
NZDM is developing the Green Bond framework, with details expected to be announced in September 2022 quarter.

The inaugural issuance of New Zealand sovereign Green Bonds is expected via syndication late in 2022. The maturity date and other details will be announced in subsequent NZDM updates.

Inflation-Indexed Bonds (IIBs)

IIB issuance is expected to be between NZ\$1.5 billion and NZ\$3 billion in 2022/23.

Proportion and annual issuance of IIBs



Source: The Treasury

Although the proportion of IIBs in the NZGB portfolio has decreased from a peak of 24% in 2019 to around 13% currently, IIBs continue to be a core product alongside nominal bonds. IIBs contribute to investor diversification and inflation adjusted coupon and principal amounts align repayments with the variability in Crown revenues thus reducing the risk on the Crown's balance sheet.

Whilst a more flexible approach to IIB issuance has improved market functioning, overall participation in the market remains subdued. Consequently, at BEFU, we announced further steps to increase investor participation and to improve turnover of the IIB market:

- Individual IIB tranche size caps have been increased from NZ\$6 billion to NZ\$10 billion.
- A tap syndication of the 2035 IIB will be undertaken alongside a repurchase of the 2025 IIB.

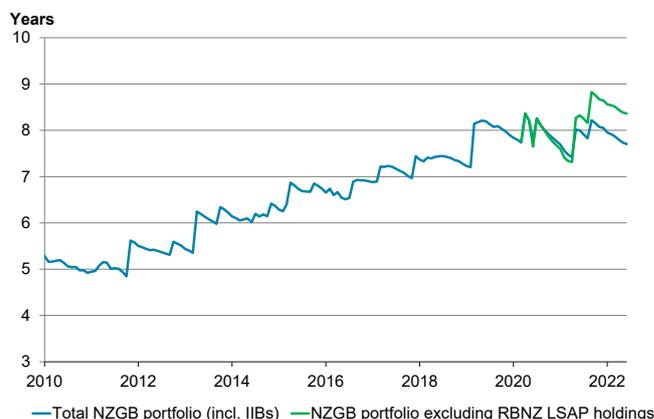
To satisfy demand from our existing IIB investors, we still intend to issue longer-dated IIBs in the future. For more detail on our IIB strategy, see the latest NZDM Insights – [Supporting the New Zealand Inflation Indexed Bond Market](#).

Euro Medium Term Note (EMTN)

NZDM maintains up-to-date legal documentation for an EMTN programme, should this be required. However, this facility has not been used since 2004 and there is no current intention to undertake long-dated foreign currency issuance, given objectives to support NZD securities markets. In addition, market pricing, relative to NZD securities, is also unfavourable.

Average Maturity

Average weighted term to maturity of NZGB portfolio



Source: The Treasury

The average weighted term to maturity of the bond portfolio has increased consistently over recent years. Several factors have been considered in this decision:

- Investor diversification, including capturing demand from investors seeking duration or aiming to offset long-dated liabilities.
- Reducing refinancing risk.
- Contributing to the development of New Zealand's capital markets by extending the risk-free curve.

There are no plans to extend the NZGB curve beyond the 30-year point. With regular issuance into tenors across the curve, the average weighted term to maturity is expected to stabilise around current levels.

Secondary Market Support

Maximising liquidity in the secondary market for NZGS remains a priority. Strong relationships with intermediaries that support the NZGS markets are crucial to achieving this outcome. The funding strategy also incorporates elements to help maximise secondary market liquidity:

- Focusing on core NZD denominated instruments.** This helps to maximise liquidity in existing NZGS, and a well-developed NZD denominated NZGS market supports domestic capital markets.
- Issuing new bond lines via syndication.** Syndicated issuance ensures a sizable volume of a bond line is on issue from initiation. After an initial blackout period of typically at least two months, tender issuance into the bond line commences which helps promote liquidity in the new bond line.

- **Undertaking bond buybacks.** NZDM generally repurchases bonds prior to maturity to smooth Crown cash flows. This also enables investors to recycle proceeds further out the yield curve.

NZDM continues to monitor market conditions in relation to the indicated plans to commence a repurchase programme of the 15 April 2023 nominal bond. Should conditions support an initial transaction, a further announcement will be made.

- **Broadly matching ACGB maturities.** NZDM aims to issue NZGBs with maturities that closely align with Australian Commonwealth Government Bond (ACGB) equivalents to enable investors to easily assess relative value and trade between these assets, helping support secondary market liquidity.

Short-term Funding

Treasury Bills (T-Bills)

T-Bills provide flexibility to address short-term cash needs which may arise from upcoming bond maturities, or seasonal or unexpected changes in cash flows. Short-term funding incorporates a core issuance assumption of NZ\$3 billion of T-Bills to retain market presence and function. This is around NZ\$1 billion higher than pre-pandemic levels, reflecting an increase in outstanding debt, as well as larger and more frequent bond maturities, the latter supported by greater depth in short-term funding markets.

T-Bills are made available through fortnightly tenders and total volumes on issue may vary above NZ\$3 billion, due to factors such as the relative cost of issuance versus alternative short-term funding instruments and short-term cash needs. It is expected, over the long-term, that T-Bills on issue may vary from NZ\$3 billion to NZ\$10 billion, depending on cash requirements.

European Commercial Paper (ECP)

ECP issuance was restarted in April 2020, with ECP on issue typically ranging from NZ\$1 billion to NZ\$2 billion. NZDM intends to maintain a small volume of ECP on issue so the market can be easily accessed, should it be required.

The Crown's programme operates through a closed dealer group. Consequently, any issuance to end investors can only be distributed by those banks named on the programme. ECP is issued by reverse enquiry with NZDM setting pricing levels to the ECP programme dealers daily.

Investor Engagement

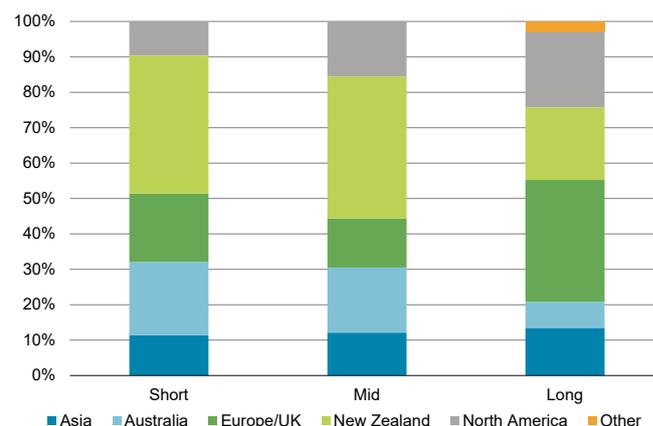
The funding strategy aims to stimulate demand from different investor types, whether by geography, style or mandate. NZDM has a structured investor engagement programme which includes *Investor Update* and *Investor Insights* publications, along with regular meetings and presentations to investors.

As at end-July 2022, non-residents held NZ\$56 billion of NZGBs, representing 59% of the market free float⁴, an increase of NZ\$16 billion from 12 months ago. For many investors, NZGBs are an 'off-benchmark' position highlighting the importance of stimulating foreign investor interest and demand alongside that of domestic financial institutions.

Syndication statistics provide insights into the investor base and reveals demand to be well-diversified across investor types and geographies. The data available on the NZDM website aggregates syndication statistics since the 2020 calendar year. NZGB secondary market turnover data from registered tender counterparties is also available on the website.

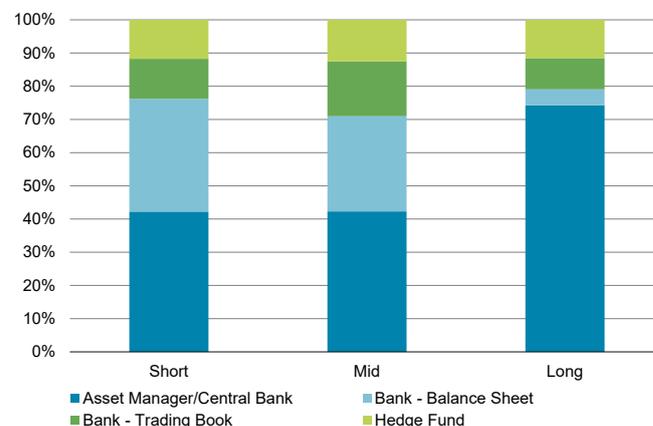
Stimulating a broad range of investor groups is a core objective of the engagement programme. The most recent syndication, the 2051 nominal bond, saw several new investors participating and issuance of Green Bond may contribute further investor diversification.

Syndication allocation by region and term



Source: The Treasury

Syndication allocation by investor type and term



Source: The Treasury

4 Outstanding bonds less RBNZ large scale asset purchases.