## BOX 3: MALTA GOVERNMENT STOCKS MARKET: 2023 IN REVIEW[1]

Global economic recovery and tighter monetary policy by major central banks to tame high inflation characterised financial markets in 2023. Such circumstances pushed yields on fixed income securities higher, reaching levels last seen a decade ago, for which the local market was no exception.

The analysis examines the primary and secondary markets for MGS throughout the year 2023. The issued MGS for the year are detailed in terms of wholesale and retail participation, as well as the allotment amounts across both investor types. Participating patterns are examined, showcasing the varying levels of demand across five different investor categories. The Treasury received robust demand from both retail and wholesale investors, across four issuances and one private placement,[2] offering €1.59 billion out of the €1.60 billion borrowing plan targeted for 2023. This analysis also sheds light on wholesale investor's return appetite as revealed through the Average Weighted Yield (AWY) of individual issues held during the year. The choice of maturity terms and coupons by the issuer are explored, before delving into the secondary market. The local sovereign paper emerged as the most traded security on the secondary market, supported by the Central Bank of Malta's role as market maker. Turnover in this paper is further evaluated for 2023 and for a ten-year period, where on-exchange trading slightly surpassed levels recorded in the previous three years though remaining well below peak figures. Lastly, movements in MGS holdings across investor categories are analysed.

### Primary market developments

During 2023, the Treasury targeted to raise up to a maximum of €1.60 billion through MGS issuance. The market responded with strong demand, for nine new fixed rate MGS spread across four regular issuances and a rollover in a 62+ Malta Government Savings Bond (MGSB). Applications reached a total of €1.73 billion, out of which €1.46 billion were allotted, underscoring the strong appetite among investors for Maltese government paper.

Trends in applications varied throughout the year with the highest bid-to-cover ratio of 2.11 times observed in the July issuance, showing the highest number of applications submitted from both retail and wholesale investors. In contrast, the September issuance was the least popular, with a bid-to-cover ratio of 1.26 which was mostly held back by the limited interest of retail investors, placing only €81.62 million in this particular issuance. More information on the MGS issuances of 2023 can be viewed in Table 1.

Wholesale investors accounted for 70.5% of total participation across the year, while retail investors applied for 29.5% of total applications. At a glance, one may depict retail participation as weak. However, when analysing take up of amounts offered to both the retail and wholesale sector in combined issuances, it can be noted that demand levels in 2023 reached those seen earlier in the presented decade (see Chart 1). Retail issuances were halted for

[1] This box is a summary of "The Malta Government Stocks Market - 2023 in Review", a report published on the Bank's website. It is prepared by Kimberley C. Agius, Emmanuel Farrugia and Therese Lethridge, Senior Research Analysts within the Monetary Operations and Government Securities Department. The views expressed are those of the authors and do not necessarily reflect those of the Central Bank of Malta. Any remaining errors are the sole responsibility of the authors.

[2] Private placement refers to the rollover of the 62+ MGSB.

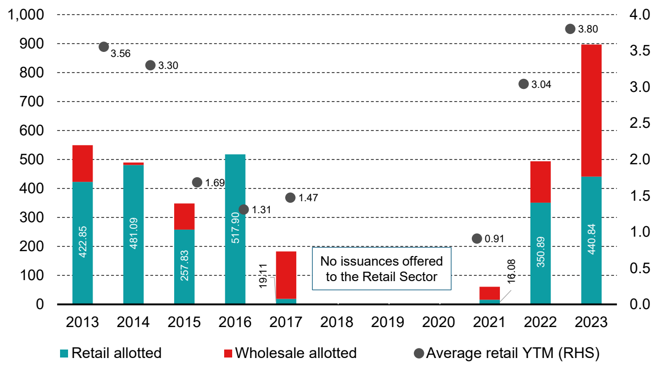
**Table 1**
**LIST OF 2023 ISSUANCES**

| | February | June | July | September | October | |
|---|---|---|---|---|---|---|
| | 3.50% MGS 2028 VI | 62+ MSGB Issue 2023[(1)] | 3.55% MGS 2026 V | 4.00% MGS 2033 IV | 3.85% MGS 2026 VI | |
| | 4.00% MGS 2043 I | | 3.75% MGS 2033 III | 4.30% MGS 2038 II | 3.95% MGS 2028 VII | |
| | | | 4.00% MGS 2038 I | | | **Totals** |
| | EUR | EUR | EUR | EUR | EUR | EUR |
| **Total amount on offer** | **350,000,000** | **85,971,100** | **400,000,000** | **400,000,000** | **350,000,000** | **1,585,971,100** |
| Original issue | 200,000,000 | 85,971,100 | 270,000,000 | 260,000,000 | 200,000,000 | 1,015,971,100 |
| Overallotment option | 150,000,000 | - | 130,000,000 | 140,000,000 | 150,000,000 | 570,000,000 |
| **Total applications** | **415,679,500** | **70,092,200** | **569,049,000** | **327,115,400** | **351,900,000** | **1,733,836,100** |
| Retail | 179,179,500 | 70,092,200 | 180,049,000 | 81,615,400 | - | 510,936,100 |
| Wholesale | 236,500,000 | - | 389,000,000 | 245,500,000 | 351,900,000 | 1,222,900,000 |
| **Total amount allotted[(2)]** | **349,179,500** | **70,092,200** | **399,549,000** | **303,615,400** | **341,900,000** | **1,464,336,100** |
| **Bid-to-cover ratio[(3)]** | **2.08** | **-** | **2.11** | **1.26** | **1.76** | **1.71** |

[(1)] Eligible bondholders of this security were offered to rollover their maturing holdings in the new savings bond issue.
[(2)] Total applications from Retail Investors were fully allotted.
[(3)] Bid-to-cover ratio is applied on the original issue amount.
Source: Malta Treasury Department.

a three-year period due to ultra-low yields prevailing at the time. Following the increase in returns given by rising yields, the Treasury reopened applications for retail investors in mid-2021 for only one issuance. Furthermore, the low participation rate of 29.5% may be attributed to a significant increase in the Treasury's debt supply, with the volume of debt offered to the retail sector in 2023 reaching its highest level since 2013.

**Chart 1**
**RETAIL PARTICIPATION IN COMBINED MGS ISSUANCES[(1)]**
*(EUR millions; percentage)*




Source: Malta Treasury Department.
[(1)] The chart aggregates only issuances offered to the retail sector on a yearly basis, thus omitting issuances offered exclusively to wholesale investors. The wholesale allotment is shown to depict the magnitude of the retail vis-à-vis the wholesale participation. The 62+ MGSB rolled over in 2023 is not included for comparability reasons.

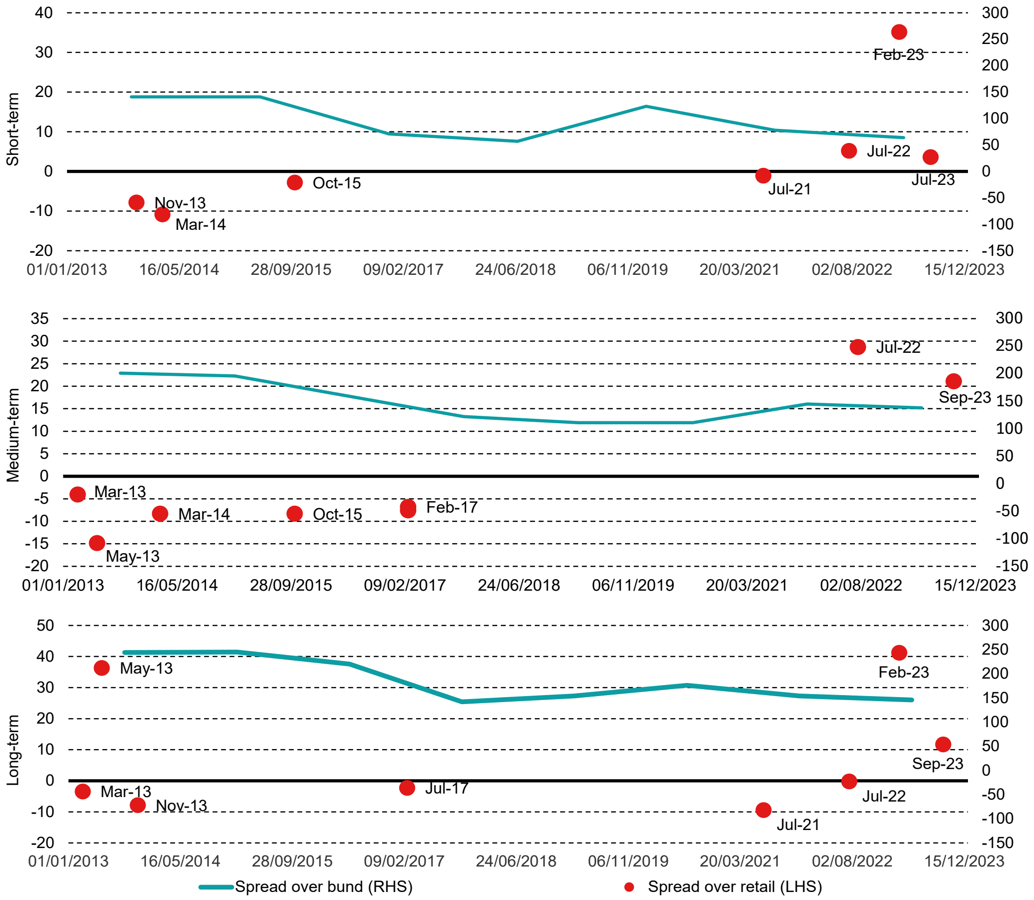
At issuance, participants are classified into five investor categories, of which financial companies showed most interest in the MGS offerings, applying for a total amount of €1.11 billion, or 67.1% of total submissions. The individual and household, and non-profit entity[3] categories followed with €299.45 million and €134.74 million, respectively in applications. The final two categories, namely government[4] and non-financial companies, collectively represented 14.9% of total applications.

Analysing the resulted AWYs by wholesale investors over the set retail yield to maturity (YTM) gives insight on wholesale investors' yield requirements. In the issuances opened

[3] The largest portion of the non-profit entity classification is made up of Resident Nominees who are not necessarily non-profit. These investors do not hold a direct account with the MSE and place their applications through a broker. In the secondary market, this category also includes movements in both resident and non-resident nominees.
[4] The government category refers mainly to government agencies and public sector entities.

to both investor types, wholesale investors demanded higher yields than those offered to retail investors, as per price setting published by the Treasury. The most notable premium was seen in the first issuance of the year for the 4.00% MGS 2043 I, with 41 basis points in AWY over that locked in by retail investors. The income goals of the investor could provide one explanation for this premium. However the possibility of yield fluctuations between the publication of retail prices and the opening of the wholesale auction could potentially contribute to the higher AWY. Moreover, the Government's increased borrowing needs from 2020 onwards may have also signalled investors the opportunity to request higher returns and constrain the Treasury to entertain such bids. This becomes more pronounced after considering that the deviations across a ten-year period were persistently negative between the years 2013 and 2017, with only one exception in the long-term bracket, as seen in Chart 2. Deviations in spreads turned positive after 2020 even though the Maltese risk premium over the German bund[5] declined over this ten-year period by 77 basis points, 63 basis points, and 98 basis points in the short, medium and long-term, respectively in line with other euro area sovereigns that share similar economic fundamentals. This may signal

**Chart 2**
**DEVIATION OF SUCCESSFUL AWY FROM RETAIL YTM**




Sources: Malta Treasury Department; Central Bank of Malta.
Note: Only issuances which were open to both wholesale and retail investors are shown.

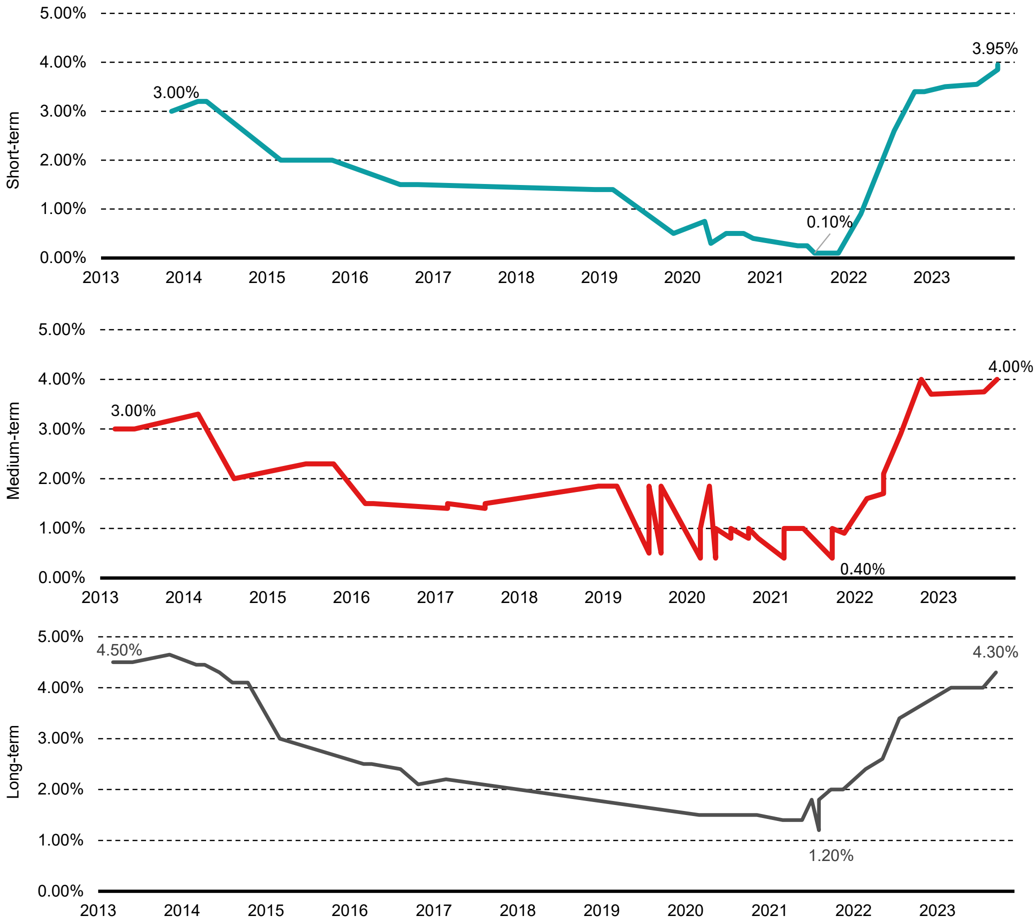
[5] Based on Indicative Secondary Market prices published by the Central Bank of Malta.

that wholesale investors require a higher return premium over the bund than that indicated through secondary market pricing. Nevertheless, confidence in the secondary market does not seem to be waning as such prices were utilised by brokers in secondary market trading in 2023, with most of the traded prices having only slight deviations.

All issuances in 2023 introduced new bonds in the central government's portfolio, having different maturities[6] spanning from three to 21 years paired with coupons that ranged from 3.50% to 4.30%. MGS coupons across all tenors in 2023 approached or exceeded those seen a decade ago as global yields surged, reflecting the high inflation rates in 2022. Restrictive monetary policy to tame inflation inevitably pushed interest rates higher.

As illustrated in Chart 3, MGS coupons were relatively high in 2013, declined gradually and rose again over the last two years. The downward trend in coupon rates after 2013

**Chart 3**
**COUPONS ACROSS A TEN-YEAR PERIOD**




Source: Malta Treasury Department.

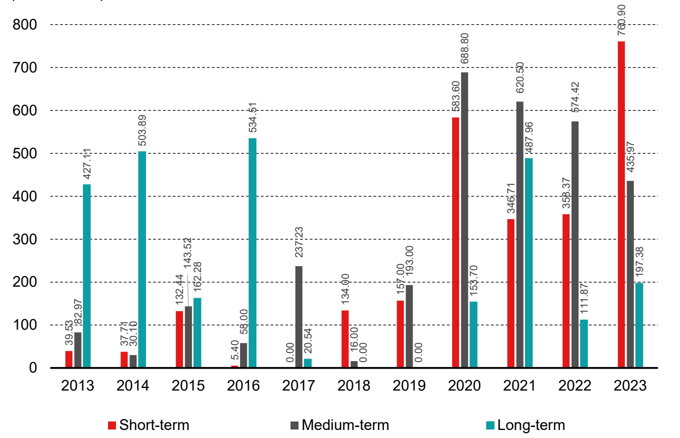
[6] Maturity terms between one and six years are categorised as short-term bonds, including both years. Those of seven till 14 years are medium-term tenors, whilst those of 15 years and higher are considered long-term issues.

was influenced by several factors, mostly by the ECB's monetary policy decisions, including negative interest rates starting in mid-2014 and the Quantitative Easing Programme introduced in March 2015 amid a period of disinflation. Coupon rates continued to decline, reaching their lowest point in 2021 during the COVID-19 pandemic, as negative interest rates were maintained to counter the sharp economic contraction. Since the end of 2021 yields started to increase, reaching high levels in 2023.

The choice of maturity terms for new issues reflects issuers' strategic objectives and financial planning. Issuing longer-dated debt when yields are low allows for the collection of funds locked at lower borrowing costs. Given the high yields in 2023, the Treasury only allotted €197.38 million over three long-term bonds as shown in Chart 4. The issuance of long-term debt was preferred until 2016, possibly due to lower interest rates, which is also noted in 2021 when issuances in the medium maturity bracket reached €620.50 million. Short-term bonds, however, gained prominence in the primary market from 2020, with the largest amount allotted in 2023. Given the general expectation of a drop in short-term interest rates, issuing short-term debt during 2023 may have been strategic to reissue at lower rates in the near future.

Debt sustainability also takes a role, whereby considerations towards maintaining low debt servicing costs whilst ensuring long-term feasibility, are taken. Additionally, an issuer should seek to evenly distribute debt across years to avoid large redemptions within a short timeframe, and therefore curbing what is known as refinancing risk. The chart displays that generally issuances always included different maturity terms, irrespective of the yield environment. The variable in each case, however, was the amount to be allotted.

**Chart 4**
**TENORS ISSUED ACROSS A TEN-YEAR PERIOD**
*(EUR millions)*




Source: Malta Treasury Department.

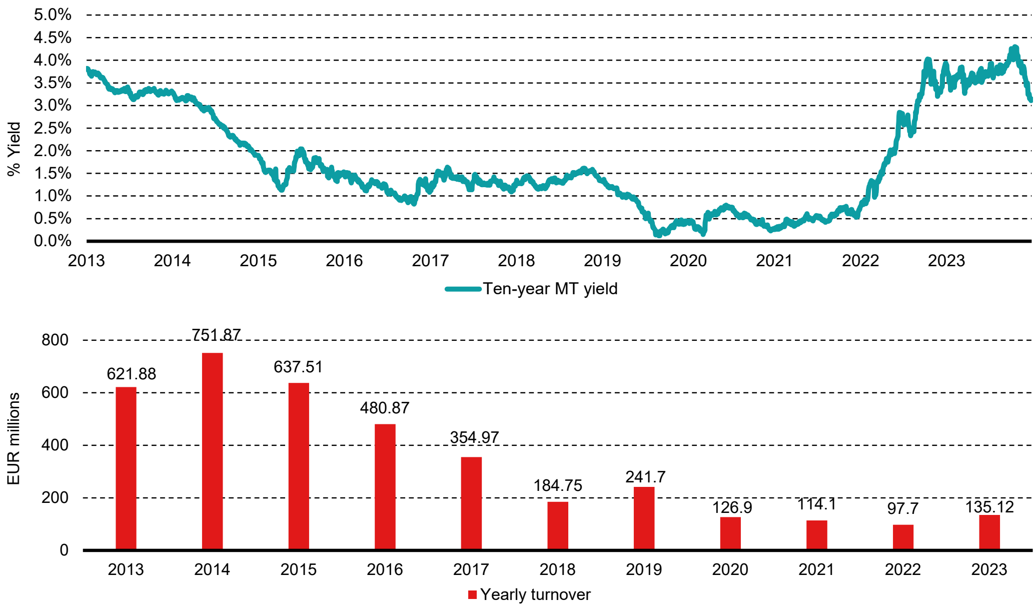
## The secondary market

A total market value of €169.26 million was traded in local sovereign debt securities, equivalent to 51.3% of total on-exchange turnover in all prominent security types. More specifically, 40.1% of total market value trading (€132.36 million) was exchanged in MGS alone, with an additional 11.2% (€36.90 million) dealt in Malta Treasury Bills (MTBs). Corporate bonds were the second most traded security type overall (30.2%), followed by Ordinary Shares (17.6%), with Prospects and Preference Shares trailing behind accounting for less than 1% of the total market value traded throughout the year.

Chart 5 visualises the trading activity in MGS during the last decade. Throughout the earlier years of the timeline, expansionary monetary policy decisions were needed to support slowing economies, directly contributing to a lower yield environment. Yields dropped between 2013 and 2016, as shown through the ten-year MT-yield curve in Chart 5, with sharp drops in 2014, which may have created avenues for profit and in turn, offloads on the secondary market. In fact, turnover touched a peak in 2014 for a nominal amount of €751.87 million. Yields kept tumbling thereafter, following the introduction of the Public Sector Purchase Programme by the ECB in 2015 and continued to fall to their lowest points between 2019 and 2020. Due to such low yields and in turn low coupon rates, the Treasury refrained from opening applications to the retail sector between 2018 till 2020. This could possibly partly explain the low turnover volumes in these respective years. Yields sharply reversed their trajectory in 2022, reaching levels last seen in 2013, supported with the release of high inflation prints, pushing bond prices lower. Turnover picked up in 2023, surpassing volumes seen in the previous three years.

The Central Bank of Malta maintained its role as a market maker by providing liquidity on the secondary market for MGS and MTBs. The Bank continues to operate in the local secondary market, taking guidance from its indicative prices published daily on its official website. The Bank accounted for 41.2% (€55.70 million) of total on-exchange transactions in MGS during the year and acted on behalf of public entities for another 18.3% (€24.78 million). The Bank was relatively more active in MTBs trading, responsible for 83.8% (€30.95 million) of the security's total on-exchange turnover, with only one other broker purchasing the remaining 16.2% (€6.00 million). Total outstanding government debt by the end of 2023

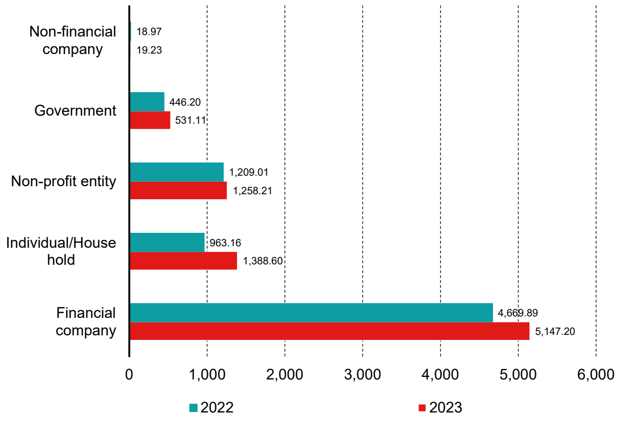
**Chart 5**
**TEN-YEAR MT YIELDS AND MGS TURNOVER**




Sources: MSE; Central Bank of Malta.

reached €8.34 billion following a net issuance of €1.01 billion. As a result, all five main category groupings grew in volume as shown in Chart 6. The investor base in the secondary market was primarily composed of financial institutions, holding 61.7% of the total outstanding amount. The individuals and households' category increased their holdings by €425.44 million over the previous year, taking over the non-profit entities category placing with the second-highest volume in holdings.

**Chart 6**
**TOTAL MALTA GOVERNMENT SECURITIES HOLDINGS BY CATEGORY**
*(EUR millions)*




Source: MSE.

## Concluding remarks

The Treasury's plan to issue up to €1.60 billion in MGS was received with robust demand. Higher coupons were necessary to attract substantial interest from both wholesale and retail investors, fulfilling the original allotment in every issuance. Financial companies dominated applications throughout the year in those issues opened to wholesale bidders. Individuals and households also demonstrated strong participation, indicating a particular interest in short-term MGS, closely followed by long-term bonds. Through the analysis of the AWY emanating from wholesale bidding revealed that the highest requested premium reached 41 basis points above the yield offered to the retail investor, indicating a rise in the cost of borrowing for the Government in recent years. The MGS secondary market experienced a modest recovery in 2023, when compared to recent years. The Bank's involvement as a market maker was crucial, accounting for a substantial portion of the total on-exchange transactions, underscoring its importance in the local financial market. Data on the distribution of MGS holdings across various investor categories showed financial companies as the dominant holder category of MGSs, followed by Individual and household and non-profit entities investors.

The insights gained from the 2023 market performance coupled with considerations of the prevailing market conditions may provide a solid foundation for future borrowing strategies, ensuring that Malta can effectively manage its public debt while fostering a robust investment environment. Further monitoring of such trends and patterns could provide valuable insights that contributes towards maintaining the local sovereign debt security's stability and attractiveness among a wide investor base.