Italy's Treasury Earned EU8.1 Billion in Winning Swaps Streak

By Flavia Krause-Jackson

Feb. 23 (Bloomberg) -- Italy's **Treasury** earned 8.1 billion euros ($10.9 billion) from interest-rate and currency swap operations since 1998 in an eight-year winning streak.

The Rome-based Finance Ministry lost 392 million euros in 2008 and 337 million euros in 2007 in the transactions, according to 1998-2008 figures supplied by Eurostat, the **European Union's** statistics office. Until then, the government had made money on the operations.

Recent losses are linked to a sudden switch in monetary policy and declines in the euro, the worst performer against the dollar this year. The single currency fell 22 percent from a record high of almost $1.60 in April 2008 to $1.25 in November of the same year. The euro, which began circulation in 2002, is currently trading at $1.36.

"Used well, swaps can be helpful and important to protect one from risks," said **Attilio Di Mattia**, a money manager at Aurelius Capital Management in Vienna, who helps oversee 4.5 billion euros of assets including European and U.S. securitizations. "Right now rates are low, once they rise, we'll have to see what happens."

The European Central Bank slashed borrowing costs from a record-high of 4.25 percent in September 2008 to an all-time low of 1 percent within eight months. Policy makers had steadily doubled borrowing costs from 2 percent in November 2005 to 4 percent in June 2007.

Derivatives are financial instruments derived from stocks, bonds, loans, currencies and commodities, or linked to specific events like changes in interest rates or weather. Interest-rate and currency swaps are derivatives used to hedge against sudden changes in rates and excessive exchange-rate volatility.

EU Inquiry

EU regulators are scrutinizing the use of derivatives to try to determine if governments used swaps to temporarily reduce their deficits to qualify for the single currency or help keep their shortfall within EU limits after entry. An inquiry by the Greek Finance Ministry has highlighted a series of derivative agreements with banks that helped conceal mounting debts by deferring interest payments.

Italian Finance Minister **Giulio Tremonti** has a "firm hand" over **public finances**, limiting the increase in the deficit and managing the euro area's second-highest debt even as the economy contracted last year, **Goldman Sachs Corp.** said in a research note on Feb. 18 to investors.

Italy has avoided the fate of some of the euro zone's smaller economies -- Portugal, Ireland, Greece and Spain -- that have drawn investor concern about their ability to control deficits and debt. Italian Prime Minister **Silvio Berlusconi** said on Feb. 10 that those nations were doing "much worse" than Italy and that the "markets have given us their faith."

The **premium** investors demand to buy 10-year Italian bonds over comparable German bonds has risen 8 basis points this year to 83 basis points. The same spread on Greek debt has widened 84 basis points this year to 323 basis points.

Debt interest payments cost Italy the equivalent of 4.8 percent of GDP, according to Goldman. The country has benefited from lower borrowing costs.

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