Primary Dealers in Government Securities

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Preface

In the last 10 years there have been a growing number of countries that have established or are in the process of establishing a primary dealer system. This paper discusses theoretical and operational issues related to the establishment of a primary dealer system for countries that may be considering taking this step. Drawing on a survey of country practices conducted in 2001, the first part of the paper discusses the rationale, costs and benefits, and key prerequisites, while selection criteria, obligations, and privileges, among other issues, are discussed in the second part. The paper also tries to address whether a primary dealer system fits into the overall strategy for financial market development in the country. In this context, under appropriate circumstances, primary dealers can support the primary market for government securities by helping to provide a consistent, dependable source of demand. At the same time, they can foster development of the secondary market by providing two-way quotes for selected issues of government securities and by servicing the retail market. Under a primary dealer system, the debt manager and the group of primary dealers pursue a common strategy in support of the effective functioning and development of primary and secondary markets for government securities. Among the countries surveyed, there was broad agreement among authorities that a primary dealer system is to be highly recommended.

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In the last 10 years there have been a growing number of countries establishing primary dealer (PD) systems. This paper discusses the role of primary dealers, as well as operational and technical issues related to the establishment of a PD system, in the overall management of public debt for countries that may be considering establishing such a system. One of the goals of the paper is to provide guidance on how to design a primary dealer system in an appropriate way to meet market development needs.

The paper tries also to determine under what conditions a PD system would make a positive contribution to the functioning and development of the government securities market. Even though it is difficult to give a precise analytical answer to this latter question for all countries, the paper will try to address this issue by drawing from practical experiences for individual countries. To provide empirical support and detailed information for the project, a survey on primary dealer practices and views was sent in 2001 to 47 countries, varying widely in terms of size and stage of economic development, and responses were received from 39 of these countries.

It is important to note that industrial countries already have PD systems, although many that do have established them only in the last few years. In addition, a number of emerging market and developing countries have either adopted, or are in the process of adopting, PD systems, but many others have not done so.