Executive Summary

OECD governments are facing unprecedented challenges in the markets for government securities as a result of continued strong borrowing amid a highly uncertain environment with growing concerns about the pace of recovery, surging borrowing costs, sovereign risk and contagion pressures.

The fourth OECD Sovereign Borrowing Outlook provides estimates of borrowing needs for 2011 and projections for 2012. In comparison to pre-crisis levels, gross borrowing by OECD governments is expected to remain at the elevated level of USD 10.4 trillion in 2011. In 2012, the borrowing needs of OECD sovereigns are projected to reach USD 10.5 trillion, with a strong increase in longer-term redemptions in 2012. Against this backdrop, net borrowing is estimated to fall to USD 2.1 trillion in 2012, while government debt ratios are expected to remain at high levels.

Raising large volumes of funds at lowest cost, with acceptable roll-over risk, remains therefore a great challenge for a wide range of governments, with most OECD debt managers continuing to rebalance the profile of debt portfolios by issuing more long-term instruments and moderating bill issuance.

Additional challenges for government (and corporate) issuers are the complications generated by the pressures of a rapid increase in sovereign risk, whereby “the market” suddenly perceives the debt of some sovereigns as “risky”. A lack of consensus on what exactly constitutes sovereign risk is an important complication to properly measure and price this risk. Since the track-record of ‘sovereign risk pricing’ is not very impressive, suggested market measures of this risk should be treated with great caution. One should, therefore, be very cautious in concluding that the sovereign debt of an OECD country has indeed lost its ‘risk-free’ status.

Issuers had to deal with euro area-induced contagion effects. Contagion can be transmitted via direct channels (including losses from balance sheets and off-balance sheet exposures via CDS markets) and indirect avenues. Although direct effects are easier to quantify, indirect channels could prove to be more damaging. Indirect channels of contagion include a re-pricing of both sovereign risk and counter-party risk among financial intermediaries. This, in turn, may lead to higher funding costs and roll-over risk for sovereigns and financial institutions, impaired ability to pledge sovereign securities as collateral and flight-to-safety by investors.

In this challenging environment many debt management offices had at times to adjust their issuance procedures and techniques so as to cope with unprecedented volatility and highly uncertain issuance conditions.