OECD Sovereign Borrowing Outlook 2016

Summary in English

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While sovereign borrowing requirements have slightly declined, redemption profiles remain challenging. Sovereign debt ratios are still high by historical standards in OECD countries.

Sovereign borrowing in the OECD area, which had risen rapidly as result of the policy response to the global financial crisis, has declined owing to fiscal consolidation. However, net borrowing remains positive. The level of sovereign debt against the backdrop of slowdown in real activity remains high by historical standards. Surveys of the outlook for borrowing indicate that aggregate central government marketable debt across the OECD will rise slowly but steadily and exceed USD 40 trillion in 2016.

Redemption profiles of outstanding medium- and long-term central government debt remain challenging over the next few years. In order to address roll-over risk, debt managers aim to lengthen and smooth out the redemption profile. Such a strategy tends to involve higher debt-servicing costs over the short term, given that yield curves are generally upward sloping. At the same time, it makes debt-servicing costs more predictable, and this advantage is currently achieved at limited cost because of the low interest rate environment. Therefore, funding strategies of many Debt Management Offices (DMOs) have leaned steadily on long-term local currency financing instruments.

Secondary market liquidity has remained an important source of concern for debt managers

From a debt management perspective, liquidity in financial markets is important for the cost of borrowing. Also, strong liquidity is essential for a government bond market to provide reliable and efficient price signals for other financial markets, even in times of market dislocation or stress. Since the onset of the global financial crisis, unconventional monetary policies, new regulations and structural changes in the investor base have affected the liquidity of government bond markets. DMOs are addressing the issue of liquidity risk by stepping up their efforts to monitor liquidity indicators, putting in place several measures to better evaluate and motivate dealer performance in market-making, and adapting their own issuance strategies.

Debt managers' perspectives regarding the implications of the regulatory changes in the financial system (Basel III, Solvency II, CACs, MiFID II, Dodd-Frank Act, etc.) for the functioning of the primary markets suggest that these new regulations could put more pressure on dealers' balance sheets and adversely affect market liquidity and the demand for government securities. However, it is difficult to quantify their full impact on primary markets of government bonds at this stage. In response to regulatory changes and their impacts, debt managers have recently made changes to issuing strategies, procedures and techniques. Most debt offices have increased the frequency of auctions, while some of them introduced a post-auction option facility and mini-tenders to investors.

Debt managers continue to witness structural changes in the investor base for government securities which also has an impact on secondary market liquidity. Particularly, the importance of public sector institutions as investors in sovereign bonds has increased over the last decade. This development has

been driven by a combination of factors: i) quantitative easing programmes; ii) the substantial accumulation of foreign exchange reserves; and iii) risk-averse investment strategies of growing sovereign wealth funds. Public sector institutions are generally perceived as being a more stable investor group than private investors. However, the increased share of public sector investors raises concerns about concentration risk and market liquidity. Against this backdrop, debt managers recognise the importance of a diversified investor base, and have focused on attracting investors with different mandates and investment horizons through issuance strategies and investor relations policies.

Additional pressure from investors and other stakeholders to increase the transparency of debt management operations and policies

Since the onset of the global financial and economic crisis and the associated huge increase in sovereign borrowing operations, governments have been facing additional pressure from investors and other stakeholders to increase the transparency of operations and policies. Enhanced transparency of strategies, operations and policies for public debt management reduces investor uncertainty, thereby increasing the attractiveness of government bond markets. This in turn broadens the investor base, lowers risk premiums and eases borrowing costs. However, maximum transparency may not be the ideal strategic objective for a DMO, due to the potential for reduced flexibility and overlycomplex information.

Against this backdrop, the OECD Task Force on Transparency of Debt Statistics, Operations and Policies examined current data dissemination practices and developed concrete recommendations to those managing government debts. The Task Force highlighted the importance of regular and timely publication of debt statistics. This Task Force also stressed that debt managers should give careful consideration to intelligibility and accessibility features when disclosing information regarding debt statistics, operations and policies.

Key findings

- Net borrowing requirements have continued to decline from their peaks of 2008 and 2009 and gross borrowing requirements from their peak of 2012.
- The share of long-term bonds in issuance operations has been increasing in recent years and it is expected to reach 59% in 2016, almost 10 percentage points higher compared to 2007 and 2008. This change in the borrowing structure has lengthened the average maturity of outstanding marketable central government debt.
- The share of long-term debt is estimated to exceed 90% of total central government marketable debt in 2016.
- More than a third of total outstanding long-term debt in the OECD area in 2015 is expected to mature over the three years from 2015 to 2018.

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doi: 10.1787/sov_b_outlk-2016-en