2 Government Debt

2.1 Revenues from taxation and other charges represent the primary source of State funding, but the State also borrows substantially to supplement annual funding. This report outlines the trend and composition of the debt funding and the cost of debt service. It also provides an update in relation to Ireland's activity in the sovereign debt market.

General Government Debt

2.2 The most comprehensive measure of government debt is General Government Debt (GGDebt), an internationally standardised measure of debt which all EU countries are legally obliged to use for their twice-yearly reporting of government deficit and debt under the Maastricht Treaty. The GGDebt is defined by EU regulations as the total gross debt at nominal value outstanding at year-end for the consolidated general government sector – that is, the total gross debt owed by all government bodies to third parties outside government.[1] Debt that one government body owes another does not count towards the GGDebt. In Ireland, the general government sector includes most public sector bodies, but not publicly owned banks, NAMA Investment Ltd, and those commercially-operated State companies which cover a majority of their operating costs through sales.

2.3 In April 2014, the Central Statistics Office (CSO) calculated Ireland's GGDebt at approximately €203 billion at the end of 2013 – an increase of 5.4% since end-2012.

Revised Measurement Framework

2.4 The current framework for measurement of GGDebt will be revised in September 2014.[2] The main implication of the new framework (ESA 2010) for Ireland will be that the Irish Bank Resolution Corporation Limited (now in special liquidation) will be included in the GGDebt calculation from 2011.

2.5 In accordance with the ESA 2010 methodology, the CSO revised the GGDebt figure for 2013 to €216 billion (2012: €210 billion) in July 2014.[3]

2.6 The ratio of GGDebt to gross domestic product (GDP) is a standard sustainability measure applied for the purposes of comparison across the EU. The GGDebt as a proportion of GDP rose from 43% in 2008 to 123% of GDP in 2013 based on the ESA 2010.

1 Specifically, GGDebt is defined as the consolidated liabilities of the general government sector in the following European System of Accounts 1995 (ESA95) categories: currency and deposits; securities other than shares excluding financial derivatives; and loans.

2 ESA 2010 will revise and update the common standards, classifications and accounting rules for member states in drawing up their national accounts and transmitting their data to Eurostat. Eurostat will publish EU aggregates in mid-October with a note illustrating all the changes.

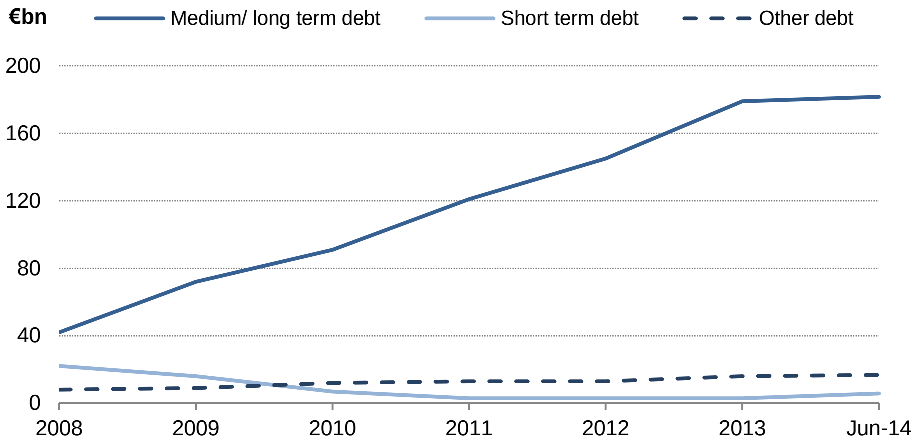
3 This was the CSO's first estimate according to the new ESA 2010 standards for National Accounts. It will not be subject to normal verification processes by Eurostat until September 2014 and should, therefore, be regarded as provisional.

Gross National Debt

2.7 The largest component of GGDebt is the gross national debt, which is debt arising from borrowings of the Exchequer undertaken by the National Treasury Management Agency (NTMA). This stood at €197.5 billion at the end of 2013 (2012: €161.5 billion). From end-2013 to end-June 2014, this increased by a further 3% to €204.2 billion.[1]

2.8 Figure 2.1 illustrates the trends in the major components of gross national debt from 2008 to end-June 2014.

Figure 2.1 Gross national debt at redeemable par values, 2008 – 2013 (year-end) and at end-June 2014



Source: Annex A, Figure A1

Medium and Long-Term Debt

2.9 Medium and long-term debt at end-December 2013 accounted for 90% of the gross national debt. It comprised mainly borrowings in the form of government bonds and loans under the EU-IMF Programme of Financial Support for Ireland which was agreed in late 2010.[2]

Fixed Rate Government Bonds

2.10 Of the €111 billion in government bonds outstanding at end-December 2013, fixed rate bonds accounted for €84.6 billion or 76%.

2.11 During 2013, there were two bond sales (€7.5 billion nominal) and three bond buy-backs/cancellations. The sales included the first 10-year benchmark bond issue since January 2010, at a yield of 4.15%. In January 2014, the NTMA raised €3.75 billion from the sale of a new ten-year bond maturing in March 2024 at a yield of 3.54%. In March 2014, the NTMA announced the resumption of scheduled bond auctions, three of which took place in the period to end-June 2014.[3] The total nominal value of bonds auctioned was €2.75 billion with yields ranging from 2.97% to 2.73%.

1 End-June 2014 figures have not been audited.

2 Formal Agreement on a three-year financial support programme from the EU, the euro area Member States and the International Monetary Fund was reached on 7 December 2010.

3 These were the first scheduled bond auctions since September 2010.

Floating Rate Government Bonds

2.12 In 2010, as part of the process of bank capitalisation, the Minister for Finance issued promissory notes to the value of €30.85 billion to three financial institutions – Anglo Irish Bank, Irish Nationwide Building Society (INBS) and the Educational Building Society (EBS). Anglo and INBS were subsequently merged to become the Irish Bank Resolution Corporation Limited (IBRC). The net effect of this measure was to create State debt outside the NTMA-managed gross national debt.

2.13 On 7 February 2013, joint special liquidators were appointed to IBRC. The promissory notes which were held by the Central Bank of Ireland as collateral for lending to IBRC at the time were replaced with Government bonds. For this purpose, eight new floating rate bonds with a nominal value of €25.034 billion were issued by the NTMA to the Central Bank of Ireland with maturities ranging from 25 to 40 years. The first of these bonds is due to mature in 2038 and the remaining bonds are due to mature every two years thereafter between 2041 and 2053. The bonds pay interest every six months (June and December) based on the 6-month Euribor interest rate plus a fixed interest margin which averages 2.63% across the eight issues and ranges from 2.50% to 2.68%. These floating rate Government bonds accounted for 23% of the government bond balance at end-December 2013.

2.14 The promissory notes outstanding at 30 June 2014 relate solely to EBS. The interest rate on these is fixed at 5.46%. A summary of the movement in the nominal value of promissory notes between 2010 when they were issued and June 2014 is outlined in Figure 2.2.

Figure 2.2 Issue and redemption of promissory notes (position as at 30 June 2014)

	IBRC	EBS	Total
	€m	€m	€m
Promissory notes issued in 2010	30,600	250	30,850
Payments in 2011[a]	(3,060)	(25)	(3,085)
Payments in 2012[a]	(3,060)	(25)	(3,085)
Payments in 2013[a]	–	(25)	(25)
Cancellations in 2013[b]	(25,034)	–	(25,034)
Payments in 2014	–	(25)	(25)
Nominal value at end-June 2014	–	201	201

Source: Department of Finance

Notes: a The annual payments include an element of principal and interest. The nominal value of promissory notes is reduced by the principal element of the payment each year. The payment to IBRC in 2012 was made by the NTMA issue of bonds with a nominal value of €3.46 billion.

b IBRC promissory notes were replaced with floating rate government bonds (see paragraph 2.13).

Amortising Bonds

2.15 In 2012, the NTMA issued amortising bonds for the first time. These bonds make equal annual payments (comprising principal and interest) over their lifetime, and are designed to meet the needs of the pension industry. Of the government bonds in issue at end-December 2013 almost €1.4 billion (or 1.2%) related to amortising bonds.

EU-IMF Programme of Financial Support

2.16 Ireland's EU-IMF programme provided for funding from EU facilities, the IMF and bilateral loans. The net euro amount received by the Exchequer under the programme was €67.5 billion (after adjustment for below par issuance, deduction of a prepaid margin, and the effect of foreign exchange transactions). The final programme disbursement of €0.8 billion from the European Financial Stabilisation Mechanism (EFSM) took place in March 2014.

2.17 The external support under the programme comprises

- €22.5 billion from the IMF Extended Fund Facility
- €22.5 billion from the EFSM
- €17.7 billion from the European Financial Stability Fund (EFSF) (this is net of a prepaid margin of €530 million[1]) and
- bilateral loans from the United Kingdom (€3.8 billion), Sweden (€0.6 billion) and Denmark (€0.4 billion).

2.18 The liability outstanding at end-June 2014 was €67.6 billion. The liability outstanding differs from the drawdown amount due to the effect of hedging instruments in place to hedge currency risk on the IMF and UK loans, euro equivalents translated at those dates and adjustment for below par issuance. See Annex A, Figure A2 for further details.

2.19 There have been a number of amendments to the terms of the EU-IMF funding since the first drawdowns were made. In 2011, an agreement was reached to reduce the interest margins and extend maturities for loans granted by the EFSF and EFSM. Subsequently, the interest margins on the bilateral loans were also reduced. In April 2013, EU and euro area Finance Ministers agreed in principle to extend further the weighted average life of borrowings under both the EFSF and the EFSM. The revised maturity dates for the EFSF loans are reflected in Figure 2.3 and the first of these is now due to mature in 2029. The revised maturity dates for individual EFSM loans will only be determined as they approach their original maturity dates. It is not expected that Ireland will have to refinance any of its EFSM loans before 2027.

2.20 The first repayment to the IMF will be in 2015 and the first bilateral loans to mature will be in 2019.

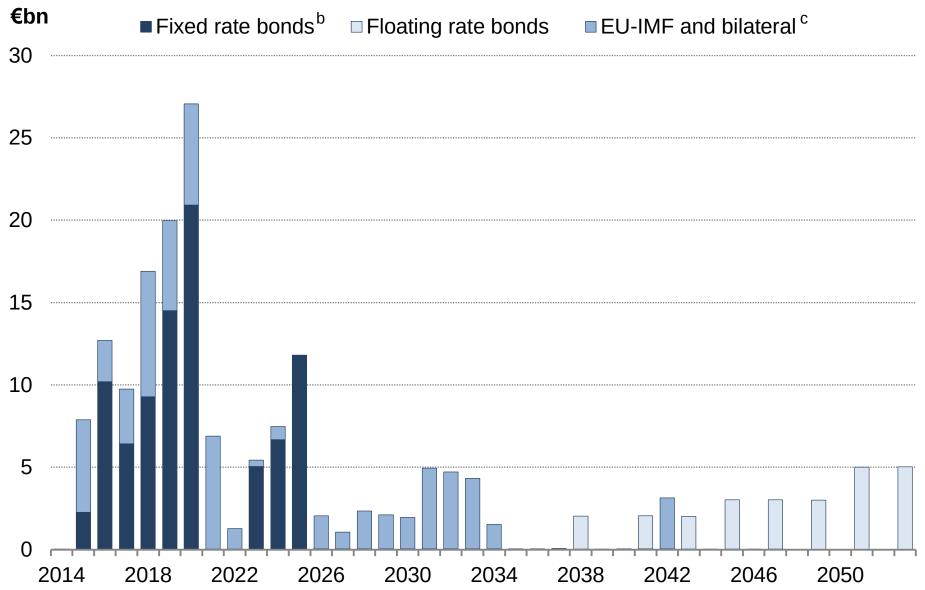
Maturity Profile

2.21 Medium and long-term debt has various maturity dates. At end-June 2014, the residual maturity of fixed rate government bonds in issue ranged from under one year to 11 years, while the maturity of floating rate bonds ranged from 24 to 39 years, and the maturity of amortising bonds ranged from 13 to 33 years. The longest maturity for borrowing under the EU-IMF programme is currently just over 28 years.

2.22 Figure 2.3 shows the residual maturity profile of Government bonds and funding under the EU-IMF programme (totalling €181 billion) at end-June 2014.

1 The first drawdown from the EFSF in February 2011 amounted to €4.2 billion. At that date, Ireland was required to prepay the present value of the interest margin charges that would accrue over the life of the loan of €530 million, along with additional fees and charges of €72 million. The net amount disbursed was €3.6 billion. It was confirmed by the NTMA in June 2014 that €485 million of the €530 million prepaid margin will be rebated to Ireland in 2016. The remaining €45 million is due to member state guarantors.

Figure 2.3 Residual maturity profile of government bonds and EU-IMF programme funding held at end-June 2014[a]



Source: Annex A, Figure A2 and Figure A3

Notes:
a The EU-IMF Programme balances are shown net of currency hedging transactions where relevant.
b Includes amortising bonds.
c EFSF loans reflect maturity extensions agreed in June 2013. EFSM loans are also subject to a seven year extension. It is not expected that Ireland will have to refinance any of its EFSM loans before 2027. However, the revised maturity dates of individual EFSM loans will only be determined as they approach their original maturity dates. The original EFSM maturities are reflected above.

Short-Term Debt

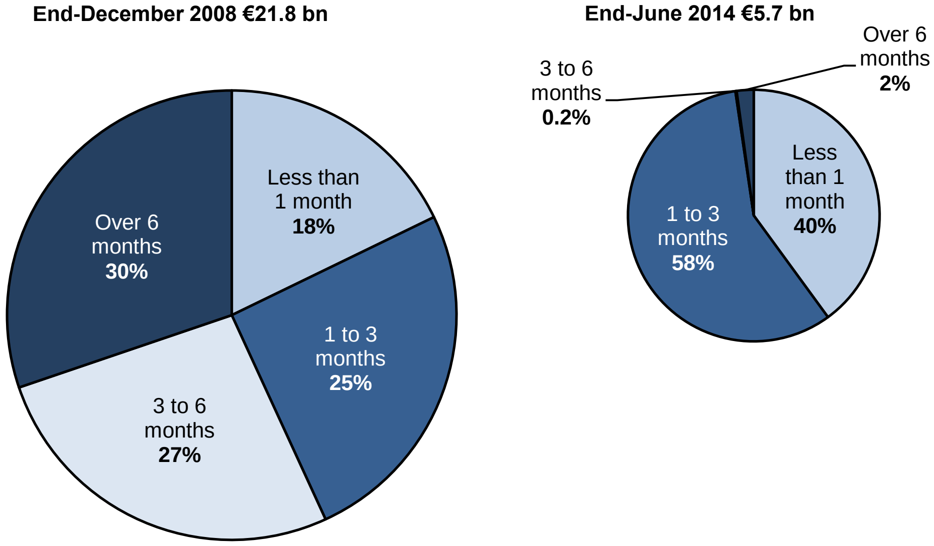
2.23 Short-term debt is debt with an original maturity of less than one year. Short-term debt[1] accounted for €2.6 billion of gross national debt at end-December 2013 and €5.7 billion at end-June 2014. Short-term instruments are used to provide liquidity and flexibility in the timing of long-term funding operations.

2.24 The main forms of short-term borrowings are treasury bills, exchequer notes and the euro commercial paper programme. Regular auctions of short-term treasury bills, (which resumed in July 2012), continued throughout 2013 with eight auctions during the year. Between January and June 2014, three auctions have taken place. Exchequer notes and euro commercial paper are sold through reverse enquiry. At end-December 2013, NAMA held €1.6 billion in exchequer notes – over 60% of the total short-term debt.

2.25 Figure 2.4 compares the maturity profile of short-term debt at end-2008 and end-June 2014.

1 This excludes short-term borrowing from other State funds.

Figure 2.4 Maturity profile of short-term debt, December 2008 and end-June 2014



Source: Annex A, Figure A4

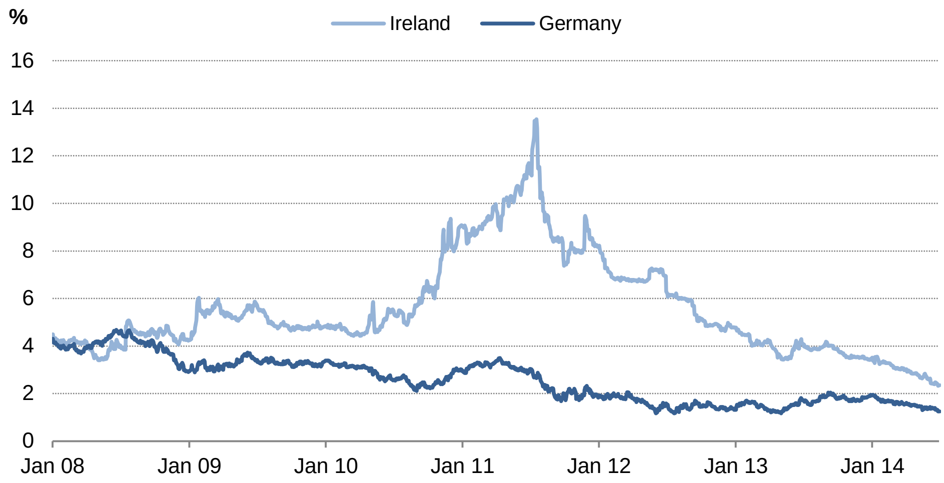
Debt Service Costs

Ireland's Debt Market Position

2.26 Because of the high cost of debt, the NTMA did not actively seek new funding in the bond markets during the period September 2010 to July 2012. Following its return to the debt markets during 2012, sales of bonds achieved yields of 5.9% and 6.1%.[1] At end-December 2013, the yield on ten-year Irish Government bonds had fallen to 3.51% compared with Germany which was at 1.93% – a difference of 1.58 percentage points. By June 2014, rates had further decreased to 2.36% for Ireland compared with Germany at 1.25%, and the difference had narrowed to just 1.11 percentage points (see Figure 2.5).

1 The yield is the annual return investors will receive for holding the bonds.

Figure 2.5 Irish and German ten-year bond yields, 2008 – June-2014



Source: National Treasury Management Agency (Bloomberg and NTMA calculations)

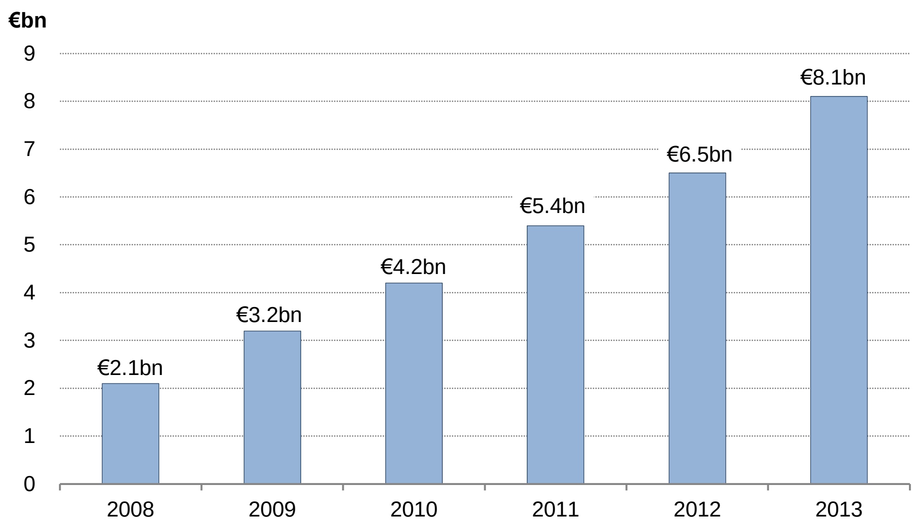
Note: Where a ten-year Irish bond yield is not available, the Irish yield is a synthetic yield derived from yields on other Irish Government Bonds for that period.

2.27 The debt service cost disclosed in the NTMA's accounts for 2013 was almost €8.1 billion when measured on a cash basis. When account is taken of a transfer of €625 million from current funds to a statutory sinking fund, the servicing outlay was €7.5 billion.[1] This is net of €125 million interest received and includes fees and expenses of €134 million.

2.28 The cost of servicing the debt rose by almost 25% between 2012 and 2013. The cost in 2013 was 3.9 times the cost in 2008 (see Figure 2.6).

2.29 When the debt service cost is measured on an accruals basis, the servicing cost for 2013 was €7.4 billion.[2] The equivalent cost for 2012 was €6.2 billion – a 19% increase year-on-year.

Figure 2.6 Debt service costs 2008 – 2013 (cash basis)



Source: National Treasury Management Agency

1 The sinking fund is used to make principal repayments. Each year, annuities are provided for in the Finance Act and are paid into the Capital Services Redemption Account from the Central Fund. A specified amount of the annuity is used for servicing the national debt (interest payments) and the balance for principal repayments (referred to as the sinking fund).

2 The accruals basis recognises the costs incurred rather than those paid and does not take account of sinking fund movements.

Average Cost of Borrowing

2.30 The NTMA estimates the overall weighted average cost of servicing the gross national debt at just under 4% at end-June. At end-June 2014, around 88% of gross national debt was at fixed rates, including debt where hedging had been undertaken.[1] The balance of the debt was at floating interest rates.

2.31 At end-December 2013, the overall weighted average cost of servicing the gross national debt was estimated at 3.9%. Four components accounted for 99% of the gross national debt as outlined in Figure 2.7.

Figure 2.7 Average cost of borrowing, end-December 2013

Product	% Gross national debt December 2013[a]	Average interest rate %
Fixed rate bonds and amortising bonds	44	4.84[b]
Floating rate bonds	13	3.02[c]
EU-IMF Programme	34	3.14[d]
State Savings Schemes	8	3.05[e]

Source: National Treasury Management Agency

Notes:
- a Figures shown total 99%. The remaining 1% of gross national debt is short-term debt and other forms of medium/long-term debt.
- b This is the bond coupon which differs from the yield.
- c This equates to an interest rate of 6-month Euribor plus an average margin of 263 basis points. The rate reflects the relevant rate reset (in December 2013). The NTMA has entered into interest rate swaps to hedge an element of the exposure to interest rate movements. However the rates quoted do not take account of this hedging.
- d The rate is the estimated all-in fixed euro equivalent cost reflecting hedging costs.
- e This rate reflects accrued interest and expenses in 2013 as a percentage of average State Savings Schemes balances. The maximum interest rates (AER) payable on the fixed term fixed rate products available for purchase at end-December 2013 ranged from 1.32% to 2.66%.

Cash and Other Financial Assets

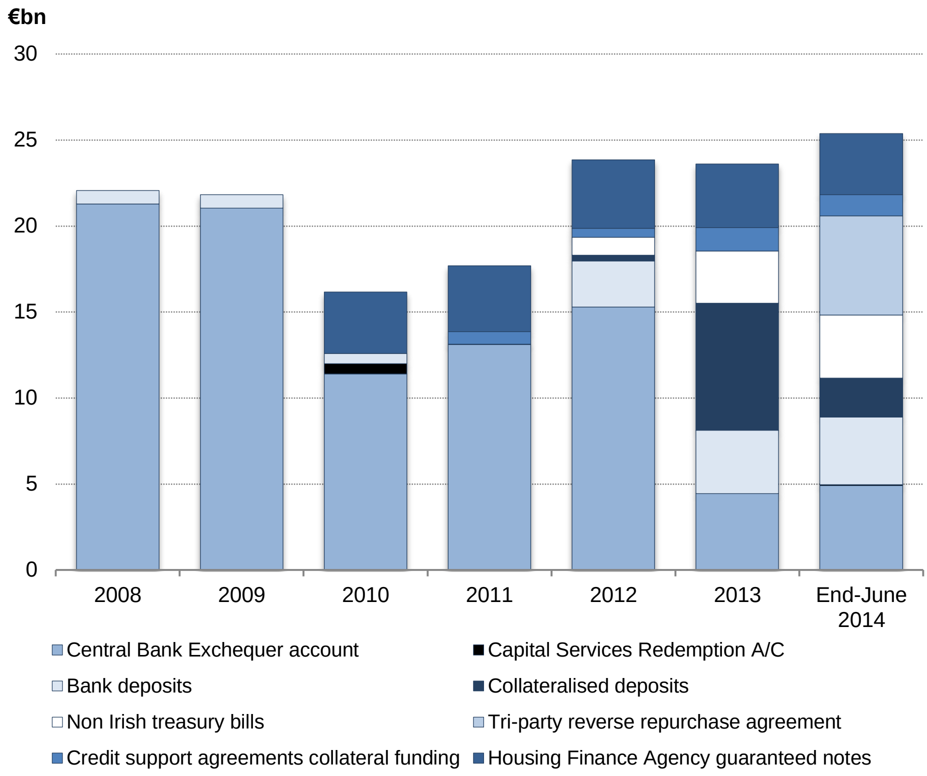
2.32 Ireland's national debt is defined by the NTMA as the gross national debt incurred by the Exchequer less cash balances and other financial assets held.

2.33 The Exchequer held significant balances of cash and other financial assets over the past number of years. At end-2013, a total of €23.6 billion was held. This had increased by 7.5% (to €25.4 billion) at end-June 2014 (see Figure 2.8).

2.34 The NTMA's stated intention was to have twelve to fifteen months of advance funding in place when the EU-IMF programme reached its conclusion at the end of 2013 to cover medium and long-term debt redemptions and any Exchequer deficit.

1 Fixed rate debt also includes EFSF loans disbursed as part of the EFSF's pooled funding mechanism. The cost of these EFSF pooled loans is related to the EFSF's cost of funds in managing the pool and can change from time to time.

Figure 2.8 Cash and other financial assets 2008 – June 2014



Source: Annex A, Figure A5

2.35 The composition of the Exchequer cash and financial assets has changed significantly in recent years. At end-2008, almost all were held in the form of deposits at the Central Bank. Such balances accrue interest at the Euro Overnight Index Average rate (EONIA). At end-June 2014, EONIA was 0.336%. In June 2014, a cap was placed by the European Central Bank on Exchequer balances remunerated at EONIA.

2.36 Around 79% (€18.5 billion) in cash and other financial assets held at end-2013 was available to the State immediately or at short notice. Housing Finance Agency guaranteed notes of €3.7 billion were not readily realisable. €1.4 billion used to fund collateral deposited with derivative counterparties under credit support agreements, while not readily realisable, are given a cash value that reflects changes in the market value of related derivatives or as the derivatives mature.[1]

2.37 The NTMA also invests available cash balances in short term bank deposits (including collateralised deposits[2]) and in non-Irish Treasury Bills. These investments earn a higher rate of return than EONIA but may also carry a higher risk.

2.38 At end-June 2014, the NTMA had invested almost 23% of cash and other financial assets (€5.8 billion) in tri-party reverse repurchase agreements with financial institutions.[3] The administration of the transactions including settlement, collateral allocation and other functions are carried out by a third party agent (Euroclear). Collateralised deposits are now predominately completed under tri-party agreements. At end-June 2014, the overall weighted average maturity remaining on these agreements was 70 days (53 days if account is taken of collateralised deposits).

1 This is the net of collateral posted of €2.3 billion and collateral received from NAMA (€802 million), IBRC (€102 million) and other counterparties (€44 million).

2 In order to manage counterparty credit risk, the NTMA receives collateral such as Government bonds for cash placed on deposit.

3 A reverse repurchase agreement is where one party buys an asset from another party and commits to sell the asset back to the second party at a future date.

Conclusions

2.39 The main component of general Government debt is cumulative borrowing undertaken by the NTMA on behalf of the State, referred to as gross national debt. This increased by a net €36 billion (22%) in 2013, mainly due to the issue of floating rate notes to replace the promissory notes (€25 billion) and borrowing required to fund the exchequer deficit (€11.5 billion).[1]

2.40 At end-June 2014, the gross national debt had risen to €204 billion, up by 3% since end-December 2013. Additional short-term debt and Government bonds account for the majority of the increase.

2.41 The NTMA estimates the weighted average cost of servicing the gross national debt at just under 4% at end-June 2014. Around 88% of the gross national debt was at fixed rates, including debt where hedging had been undertaken. The remainder of the debt was at floating interest rates.

2.42 At end-2013, the NTMA held cash and other financial assets of €23.6 billion. By end-June 2014, this had risen by just under 8% to €25.4 billion. There is no specific monetary limit set by the Minister for Finance for the level of cash and financial assets maintained by the NTMA. The NTMA has stated that, in order to bolster investor confidence and in accordance with prudent liquidity risk management, it currently aims to maintain cash and other liquid assets equivalent to at least twelve months' Exchequer funding requirements.

2.43 The form in which Exchequer balances are held has changed significantly with a move away from holding balances in the Central Bank, to investing in higher yielding (but also higher risk) instruments. Nevertheless, the return on cash and related assets is lower than the average cost of borrowing. As a result, there is a cost associated with maintaining high levels of cash balances.

1 The balance relates to a reduction of €0.5 billion due to a decrease in cash and other financial assets and some other factors.

Annex A

Figure A1 Cumulative borrowing at redeemable par values, at year-end 2008 to 2013 and end-June 2014[a]

	2008 €m	2009 €m	2010 €m	2011 €m	2012 €m	2013 €m	June-2014 €m
Medium/long-term debt[b]							
Government bonds	41,863	70,858	90,102	85,310	87,853	111,007	113,207
EU-IMF programme funding[c]	–	–	–	34,629	55,898	66,942	67,622
Other medium/long-term	483	670	673	673	772	772	892
Short-term debt[d]							
Short-term debt	21,783	16,261	6,972	2,920	2,690	2,645	5,727
Other debt							
Borrowings from other State funds[e]	2,605	1,783	1,524	1,696	786	676	788
Government savings schemes[f]	5,723	7,396	10,338	11,546	13,483	15,506	16,011
Gross national debt	**72,457**	**96,968**	**109,609**	**136,774**	**161,482**	**197,548**	**204,247**

Source: National Treasury Management Agency

Notes:
a End-June 2014 figures have not been audited.
b Original maturities of more than one year.
c The balances are stated net of currency hedging transactions.
d Original maturities of one year or less.
e The main element of this borrowing relates to the Post Office Savings Bank Fund.
f Maturities up to ten years.

Figure A2 EU-IMF programme of financial support for Ireland, December 2013 and end-June 2014[a]

	December 2013		End-June 2014[b]	
Lender	**€m**	**Average term (years)[c]**	**€m**	**Average term (years)[c]**
IMF	22,528	7.3	22,380	7.3
EFSF[d]	17,881	20.7	17,881	20.7
EFSM	21,700	12.4	22,500	12.3
Bilateral loans[e]	4,833	7.5	4,861	7.5
Total	**66,942**		**67,622**	

Source: National Treasury Management Agency

Notes:
a The liability outstanding at end-June 2014 differs from the drawdown amount due to the effects of hedging instruments to hedge currency risk, exchange rate movements and adjustment for below par issuance. The balances are stated net of currency hedging transactions.
b End-June 2014 figures have not been audited.
c Weighted average term from date of drawdown.
d The EFSF figures are shown net of a prepaid margin of €530 million. The NTMA confirmed in June 2014 that €485 million of the prepaid margin will be rebated to Ireland in 2016. (The total aggregate liability including the prepaid margin at end-June 2014 was €68.15 billion.)
e The bilateral loans are with the United Kingdom, Denmark and Sweden.

Figure A3 Residual maturity profile of government bonds, at year-end 2008 to 2013 and end-June 2014[a]

	Under 5 years	5 to 10 years	Over 10 years	Total
	€m	€m	€m	€m
2008	15,931	11,857	14,075	**41,863**
2009	25,687	29,296	15,875	**70,858**
2010	28,298	53,520	8,284	**90,102**
2011	33,670	43,356	8,284	**85,310**
2012	30,548	44,733	12,572	**87,853**
2013	32,490	40,656	37,861	**111,007**
End-June 2014	35,898	39,488	37,821	**113,207**

Source: National Treasury Management Agency

Note: a End-June 2014 figures have not been audited.

Figure A4 Residual maturity profile of short-term debt, at year-end 2008 to 2013 and end-June 2014[a]

	Less than one month	One to three months	Three to six months	Over six months	Total
	€m	€m	€m	€m	€m
2008	3,880	5,518	5,803	6,582	**21,783**
2009	4,561	8,628	2,913	159	**16,261**
2010	2,186	3,286	1,392	108	**6,972**
2011	2,796	106	18	–	**2,920**
2012	1,147	1,417	93	33	**2,690**
2013	445	747	1,428	25	**2,645**
End-June 2014	2,288	3,305	9	125	**5,727**

Source: National Treasury Management Agency

Note: a End-June 2014 figures have not been audited.

Figure A5 Cash and other financial assets, at year-end 2008 to 2013 and end-June 2014[a]

	2008 €m	2009 €m	2010 €m	2011 €m	2012 €m	2013 €m	End-June 2014 €m
Central Bank Exchequer account	21,269	21,026	11,399	13,099	15,280	4,432	4,907
Capital Services Redemption Account	–	–	600	–	–	—	53
Housing Finance Agency guaranteed notes	—	—	3,585	3,848	3,982	3,704	3,547
Bank deposits	790	790	580	30	2,680	3,679	3,928
Collateralised deposits	—	—	—	—	340	7,389	2,261
Non-Irish treasury bills	—	—	—	—	1,045	3,041	3,665
Credit support agreements collateral funding	—	—	—	715	523	1,356	1,244
Tri-party reverse repurchase agreements	—	—	—	—	—	—	5,765
Total cash and financial assets	**22,059**	**21,816**	**16,164**	**17,692**	**23,850**	**23,601**	**25,370**

Source: National Treasury Management Agency

Note: a End-June 2014 figures have not been audited.