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The Maturity Profile and Servicing Costs of Irish Government Debt

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While the public finances are forecast to improve in the coming years as the economy recovers and temporary pandemic related spending dissipates, Department of Finance projections indicate that the public finances will remain in deficit out to 2025. These deficits will need to be funded through the issuance of new debt, and maturing debt will need to be rolled over. Against this backdrop, this Box looks at the current maturity profile and interest expenditure of Irish Government debt.

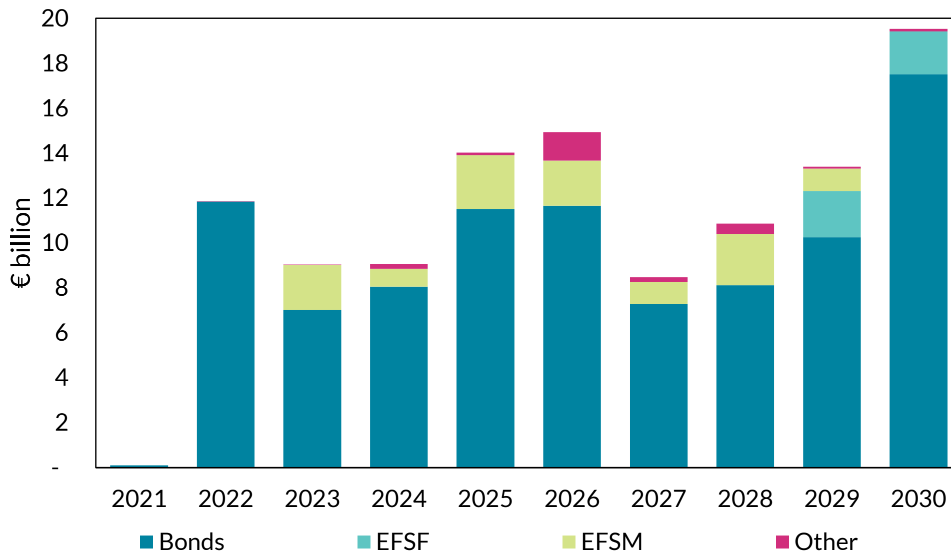
Developments in maturity and interest expenditure

According to National Treasury Management Agency (NTMA) data, the outstanding stock of medium and long term debt stands at €198.4bn. Of this, just €59bn (30 per cent) is maturing over the next five years (Figure 1).[1] From 2015 to 2020, the NTMA replaced high interest rate debt with newly issued, lower interest rate debt and extended the maturity profile to one of the longest in Europe. When combined with the increased cash balances built up over recent years, this provides the Government with strong funding flexibility in the years ahead. There are no bonds maturing until March 2022. In addition, €2.5bn in EU SURE (the European instrument for temporary Support to mitigate Unemployment Risks in an Emergency)[2] funding was received in Q1 of this year, further reducing near term borrowing requirements.[3]

[1] There is an extra €5.2bn of EFSM loans which fall due in the 2021-25 period. However, the EFSM loans are subject to possible extension which may mean they do not mature by 2025. Including the loans would mean €43bn (22%) is maturing by end 2025.
[2] This Facility was established by the European Union in May 2020 as part of its response to the pandemic. It provides loans on favourable terms to assist Member States address sudden increases in public expenditure to preserve employment.
[3] NTMA Presentation

Maturity profile of Irish Government debt has been extended

Figure 1: Maturity profile until 2030 as at July 2021

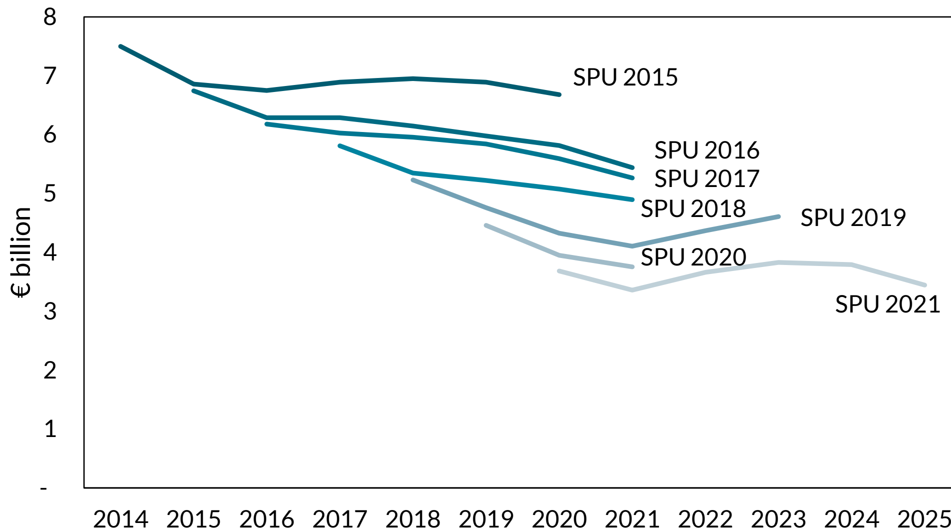


Source: NTMA

Despite the deterioration caused by the Covid-19 pandemic, the public finances have benefited from historically low interest rates. Year-to-date, the average yield on benchmark bond issuance is 0.14 per cent compared with a 2.8 per cent average issuance yield in 2014. Given this reduction in the marginal cost of debt, the average cost of debt has been steadily declining and will be close to 1.5 per cent in 2021. This has led to Government interest expenditure declining over the last five years. It has continued to decline despite the Covid shock necessitating gross public debt increasing markedly since March 2020. Figure 2 shows how in recent years, the annual Department of Finance Stability Programme Updates have consistently revised down forecasted general government interest expenditure reflecting the ongoing, low interest rate environment.

Expected debt servicing costs have persistently declined

Figure 2: Government interest expenditure forecast



Source: DoF SPUs 2015 to 2021

While the public finances of all euro-area countries have benefited from the low interest rate environment of the last 10 years, Ireland has recorded one of the largest reductions in average borrowing costs, at close to 3 percentage points.[4] A continuation of the current accommodative financing conditions would help to reduce the cost of funding further. However, future decreases in the interest bill are likely to be of a smaller magnitude than previous years as the average interest rate is already low by historical standards.

Support of ECB Asset Purchase Programmes

The ECB's asset purchase programmes have played an important role in supporting favourable finance conditions in the euro area, also reflected in the low interest rates on Irish Government debt.[5] Eurosystem cumulative net purchases of Irish government bonds under the ECB's Pandemic Emergency Purchase Programme (PEPP) and Public Sector Purchase Programme (PSPP) amounted to around €59bn (book value) at the end of July 2021.[6]

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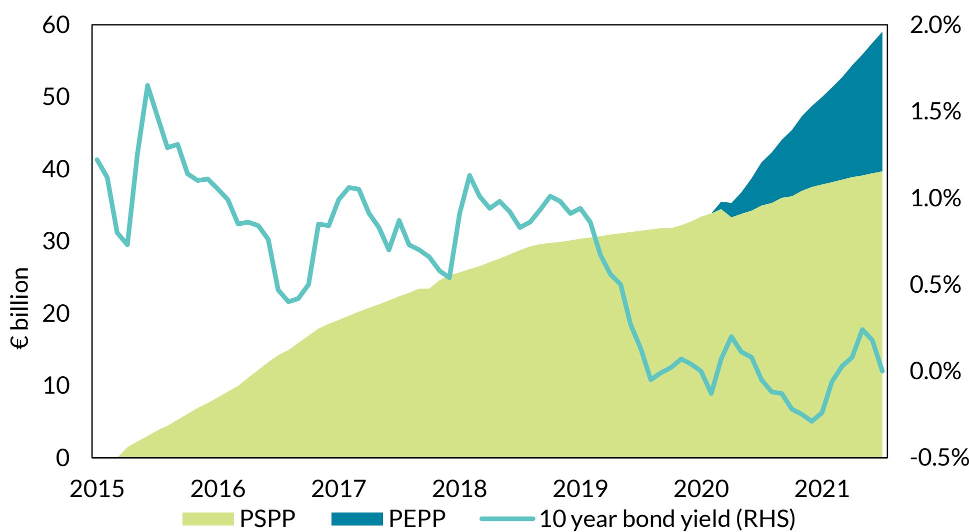
[4] European Commission
[5] See Confrey *et al.* (2021), Rostagno *et al.* (2019), and Chadha and Hantzsche (2018)
[6] Central Bank of Ireland annual report

Figure 3 shows the extent of net purchases under these two programmes. Holdings under the PSPP began to level off in 2018 and 2019 following the end of the net asset purchase phase of PSPP in December 2018. However, they began to rise gradually again following the recommencement of PSPP net asset purchases in November 2019 and the extraordinary market events of March 2020 led to sharply increased net purchases, primarily under the newly introduced PEPP. These large and sustained purchase programmes ensured euro area sovereign bond yields remained at low levels even as fiscal positions deteriorated. The favourable financing conditions have allowed the NTMA to further reduce the cost of the Irish national debt while continuing to lengthen its weighted average maturity.

Eurosystem purchases of Irish Government debt have increased since the onset of the pandemic

Figure 3: Eurosystem net cumulative purchases of Irish Govt. debt under PSPP and PEPP



Source: ECB, FRED

Risks remain

While the average interest rate has fallen considerably over the last five years, as the IMF has noted[1] the marginal interest rate (i.e. the rate on newly issued debt) is more relevant from a risk perspective. The average interest rate changes gradually as new debt is issued but the marginal rate, as was seen during the sovereign debt crisis in 2010, can exhibit far greater volatility. The IMF have indicated that marginal borrowing costs, prone to rising suddenly during periods of financial stress, have a larger

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effect than average borrowing costs on the probability of default.[7] While the General Government balance is projected to improve over the forecast period, nominal debt is still expected to be above €250bn in 2023 (23 per cent higher than its pre-Covid level). This outstanding debt stock as well as future deficits will need to be funded by future borrowing, and conditions may not be as benign when the time comes to re-finance this debt as they are currently.

[7] IMF research