

Highlights of Government Debt Policy

GOVERNMENT DEBT POLICY TRENDS IN 2009

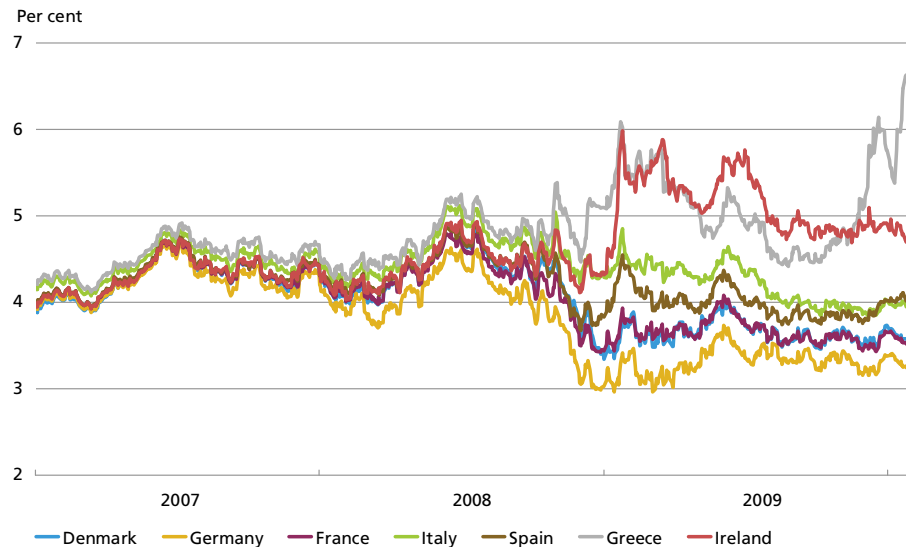
The slowdown in the world economy combined with the financial rescue packages led to a surge in government borrowing requirements. At the beginning of 2009 considerable uncertainty still characterised the financial system, causing concern as to whether the market would be able to absorb the increased supply of government bonds without yields rising strongly. Against that background, government debt management offices increased the flexibility of their issuance strategies. Issuance was concentrated in short-term government securities, and various issuance methods were used.

The uncertainty in the financial markets and increased risk aversion among investors meant that government bonds were still in demand. However, investors took a more selective approach to investment, which widened spreads between government issuers, cf. Chart 1.

Conditions in the financial markets improved during the 2nd quarter, reflecting accommodative monetary and fiscal policies. Although government borrowing requirements were adjusted further upwards, government debt management offices had easier access to the financial markets,

10-YEAR GOVERNMENT YIELDS

Chart 1



Note: Yields adjusted for maturity differences.

Source: Bloomberg.

and issuance was once again distributed more evenly across maturity segments. Higher risk appetite among investors and lower volatility in the financial markets meant that most yield spreads to Germany narrowed.

Outlook for 2010

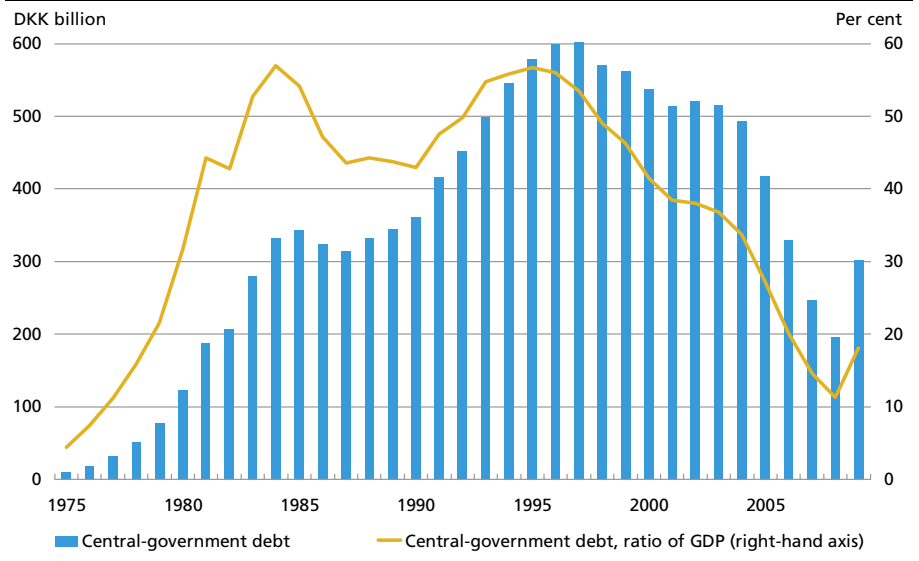
At the global level, large government budget deficits are anticipated in 2010, which will increase competition among government issuers. Investor focus on creditworthiness entails that financing costs will still vary greatly from country to country. The financial markets have improved since last year, but there is considerable uncertainty linked to a roll-back of the expansionary monetary and fiscal policies.

CENTRAL-GOVERNMENT DEBT IN 2009

Danish central-government debt rose in 2009 after a number of years with large government surpluses, cf. Chart 2. At year-end, the central-government debt amounted to DKK 302 billion, corresponding to 18 per cent of GDP. On a per-capita basis, government debt had risen from approximately DKK 35,000 in 2008 to approximately DKK 55,000 in 2009.

Most of the increase can be attributed to central-government re-lending to the Financial Stability Company and capital injections into banks and mortgage-credit institutes. Adjusted for capital injections into banks and mortgage-credit institutes and government re-lending, the debt amounted to DKK 173 billion, corresponding to 10 per cent of GDP, cf. Table 1.

CENTRAL-GOVERNMENT DEBT, 1975-2009 Chart 2



CENTRAL-GOVERNMENT DEBT, END-2009

Table 1

| | DKK billion | Per cent of GDP |
|--|-------------|-----------------|
| Domestic debt | 488 | 29 |
| Foreign debt | 140 | 8 |
| Government funds | -115 | -7 |
| Central government's account at Danmarks Nationalbank | -211 | -13 |
| Central-government debt | 302 | 18 |
| Capital injections into banks and mortgage-credit institutes | -46 | -3 |
| Re-lending to the Financial Stability Company | -29 | -2 |
| Other re-lending | -53 | -3 |
| Central-government debt adjusted for lending | 173 | 10 |

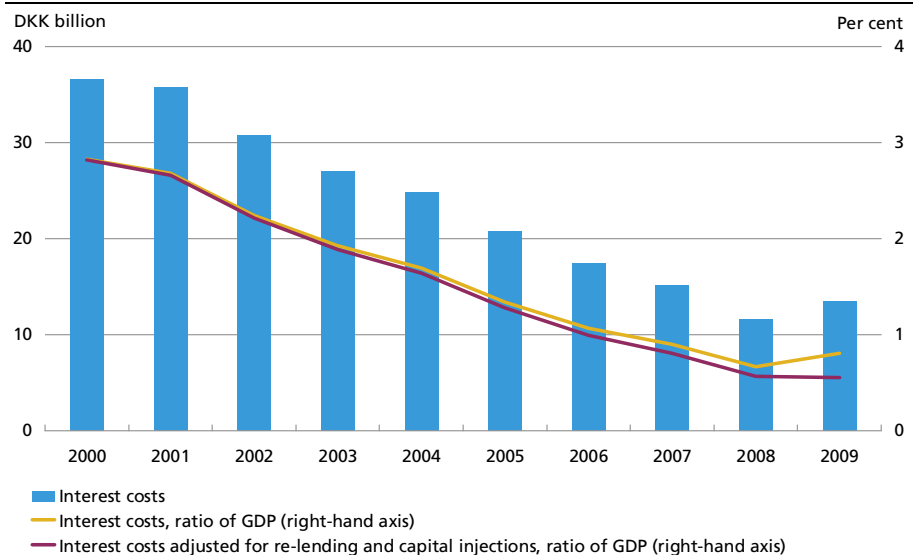
Note: A positive figure indicates a liability; a negative figure indicates an asset.

Interest costs

The increase in the central-government debt in 2009 implied that interest costs rose by DKK 1.8 billion to DKK 13.5 billion, cf. Chart 3. The central government's costs for financing of re-lending and capital injections into banks and mortgage-credit institutes are offset by interest payments from the companies. The interest payable on the capital injections averages 10.1 per cent, reflecting the risk incurred by the central government in this context. Adjusted for interest income from re-lending and capital injections, interest costs on the central-government debt declined by DKK 0.6 billion in 2009.

THE CENTRAL GOVERNMENT'S INTEREST COSTS

Chart 3



GOVERNMENT BORROWING

Domestic borrowing

At the beginning of 2009, domestic central-government borrowing focused on building up the 10-year on-the-run issue. In view of the upward adjustment of the borrowing requirement, the issuance strategy was changed in the 2nd half of the year, with an equal distribution on the 2- and 10-year maturity segments, cf. Chart 4. In addition, issuance in the 5-year segment was resumed.

Domestic borrowing totalled DKK 117 billion, DKK 14 billion higher than the borrowing requirement. This reflects that Government Debt Management began to finance the 2010 borrowing requirement towards the end of the year.

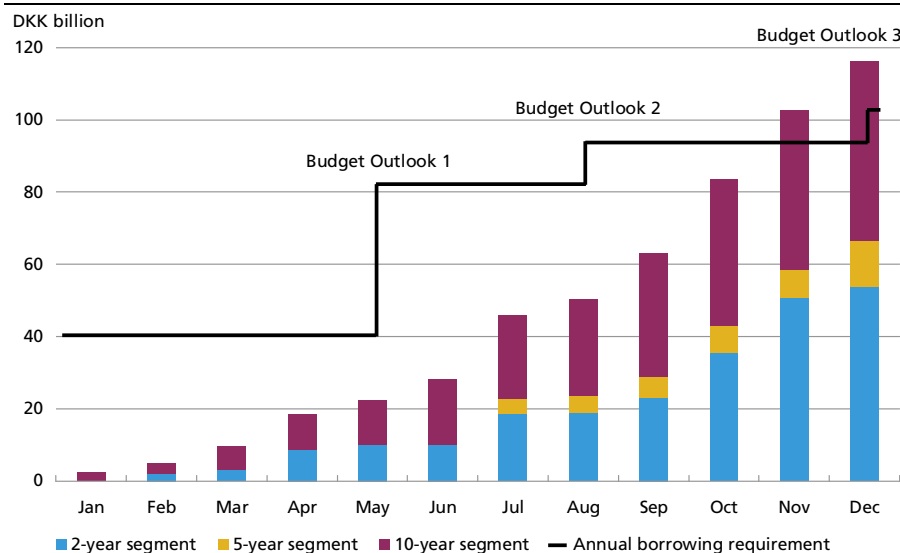
Foreign borrowing

In the context of the financial turmoil, it was found to be appropriate to increase the central government's contribution to the foreign-exchange reserve at the beginning of 2009. Against that background, the central government raised medium- and long-term foreign debt totalling DKK 82 billion in the 1st half of the year, primarily in 3-year dollar loans and a 5-year euro loan. At the same time, the central government's short-term foreign debt by way of Commercial Paper was reduced.

In the 2nd half of the year, the foreign-exchange reserve increased following intervention purchases by Danmarks Nationalbank in the market.

ACCUMULATED SALES AND BORROWING REQUIREMENT, 2009

Chart 4



Note: In addition DKK 0.9 billion was sold in the 30-year bond.

Against that background, it was decided not to refinance foreign debt maturing in the 2nd half of the year. The central government's foreign debt increased by DKK 6 billion net in 2009.

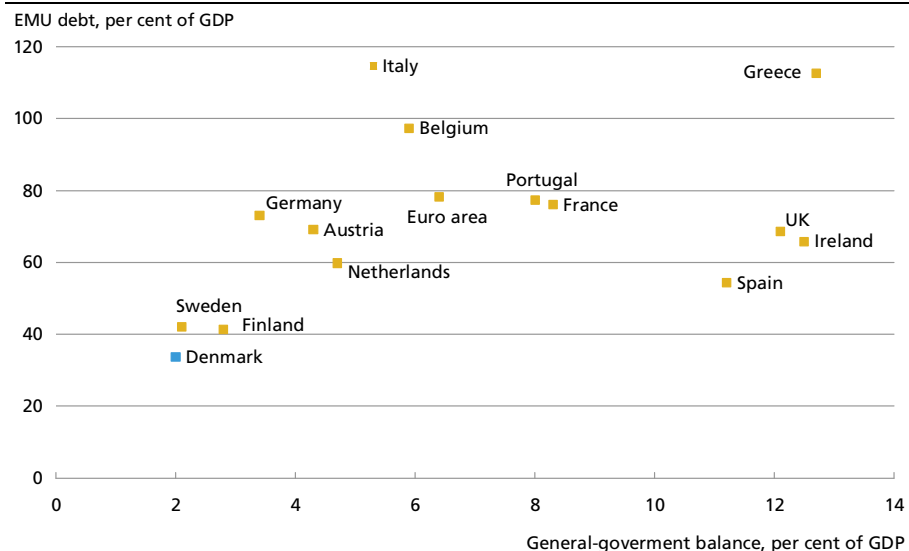
A LOW LEVEL OF DEBT IN AN INTERNATIONAL CONTEXT

Both the domestic and the foreign debt have been given the highest credit rating, AAA, by the rating agencies Fitch Ratings, Moody's and Standard & Poor's. Denmark's credit rating reflects that the level of debt is low in an international context, among other things, cf. Chart 5.

Ownership distribution of domestic government securities

Denmark's high credit standing contributes to sustaining foreign interest in Danish government securities. The non-resident ownership share was around one third of krone-denominated Danish government bonds. Non-residents primarily own short-term government bonds, cf. Chart 6. The insurance and pension sector owns 50 per cent of the central government's domestic bonds, primarily in the longer maturity segments. This is attributable to the long-term commitments of the Danish pension companies. The ownership distribution for domestic government bonds remained broadly unchanged throughout 2009.

GENERAL-GOVERNMENT BALANCE AND EMU DEBT, 2009 Chart 5

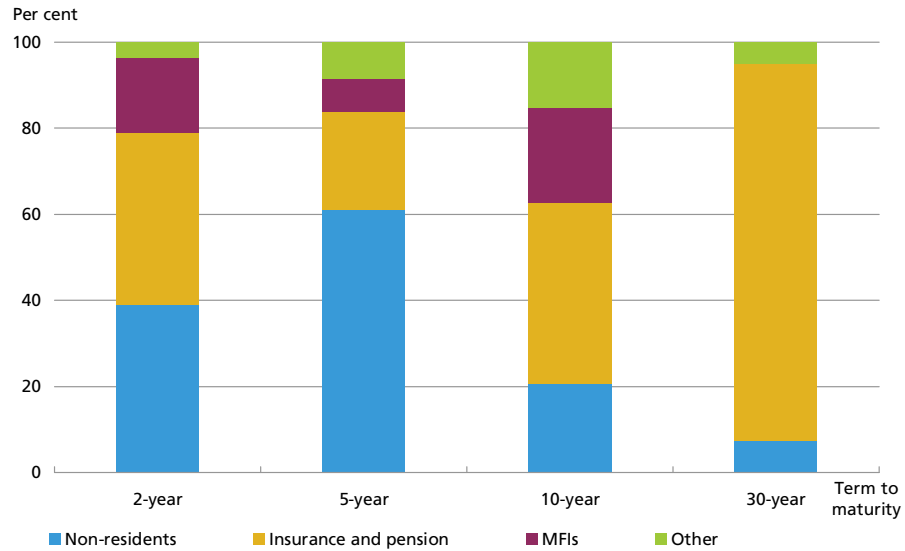


Note: EMU debt includes the general government's gross debt. Since the European Commission's autumn forecast a majority of general-government budget balances have deteriorated further. The European Commission will publish a new forecast in the spring of 2010.

Source: European Commission's autumn forecast, August 2009.

OWNERSHIP SHARES OF DOMESTIC SECURITIES, END-2009

Chart 6



Note: Ownership shares exclude the government bond portfolios of the government funds. The 2-year segment comprises government bonds with term to maturity of up to 3.5 years, the 5-year segment comprises government bonds with term to maturity from 3.5 to 6.5 years, the 10-year segment comprises government bonds with term to maturity from 6.5 years to 15 years, and the 30-year segment comprises 4.5 per cent bullet loans 2039.

Source: Danmarks Nationalbank, *Securities Statistics*.

ISSUANCE STRATEGY IN THE COMING YEARS

The large government surpluses in the period 2005-08 meant that central-government issuance focused on the 10-year maturity segment, cf. *Government Debt Policy in the Light of Falling Debt*¹. As government budget deficits are expected in the coming years, it has been necessary to reassess the issuance strategy only two years after publishing the above report. In future, it will be necessary to build up liquid bond series in other maturity segments besides the 10-year segment. The strategy is to issue bonds in the 2-, 5- and 10-year segments on the basis of a 40-20-40 percentage distribution. In addition, issuance of T-bills will be resumed.

Issuance strategy in 2010

The central government's domestic issuance requirement in 2010 is DKK 107 billion. Issuance in the existing 2-, 5- and 10-year on-the-run issues will continue in the 1st half of 2010, cf. Table 2. In the 2nd half of the year, a new 5-year on-the-run issue will be opened, maturing in 2016 to fill a gap in the central government's redemption profile. In addition, a new 10-year on-the-run issue will be opened, maturing in 2020 or 2021. The bond

¹ *Danish Government Borrowing and Debt 2007*.

KEY ON-THE-RUN ISSUES, 1ST HALF 2010

Table 2

| | |
|-------------------------|--------------------------------|
| Maturity < 1 year | Treasury bills |
| 2-year segment | 4 per cent bullet loans 2012 |
| 5-year segment | 4 per cent bullet loans 2015 |
| 10-year segment | 4 per cent bullet loans 2019 |
| 30-year segment | 4.5 per cent bullet loans 2039 |

issuance strategy will be to aim for a 40-20-40 percentage distribution. The outstanding volume in the 30-year bond can be built up to around DKK 90 billion. In addition, a T-bill programme will be opened on 25 February and is expected to cover around DKK 40 billion of the issuance requirement, cf. Box 1.

Government Debt Management resumed foreign borrowing at the end of 2008 after some years' absence. The absence from the international borrowing markets entailed that a number of investors had to reopen lines to invest in Danish securities. It was also necessary for Government Debt Management to re-establish broader contacts with investors and international banks.

To ensure access to foreign capital markets, the future strategy will be to issue an annual 5-year euro loan of EUR 1-2 billion.

ISSUANCE AND TRADING IN GOVERNMENT SECURITIES

Primary dealers

Danish government bonds are issued to and bought back from banks that have entered into primary dealer contracts with the central government.

ISSUANCE STRATEGY 2010

Box 1

Domestic strategy

- Government bonds are issued on the basis of a 40-20-40 percentage distribution on the 2-, 5- and 10-year maturity segments.
- In the 2nd half of 2010, a new 5-year on-the-run issue maturing in 2016 will be opened. This series will be built up towards a final outstanding volume of around DKK 40 billion over a 2-year period.
- In the 2nd half of 2010, a new 10-year on-the-run issue maturing in 2020 or 2021 will be opened. This series will be built up towards a final outstanding volume of around DKK 80 billion over a 2-year period.
- T-bills will account for around DKK 40 billion of the domestic issuance requirement.
- 4.5 per cent bullet loans 2039 can be built up to a final outstanding volume of around DKK 90 billion.
- Issuance in the other bullet loans is possible.

Foreign strategy

- In 2010, a 5-year euro loan of EUR 1-2 billion is issued.

PRIMARY DEALERS AND MARKET TAKERS, 2010 Table 3

| Primary dealers in government bonds | Primary dealers in T-bills | Market takers in government securities |
|-------------------------------------|----------------------------|--|
| Barclays Bank | Arbejdernes Landsbank | Bank of America Merrill Lynch |
| BNP Paribas | Danske Bank | Citigroup |
| Danske Bank | JP Morgan | Commerzbank |
| JP Morgan | Jyske Bank | Deutsche Bank |
| Morgan Stanley | Nordea | DZ Bank |
| Nordea | Nykredit Bank | Nomura |
| Nykredit Bank | SEB | Royal Bank of Scotland |
| SEB | Sydbank | |
| Spar Nord Bank | | |
| Sydbank | | |

Note: A market taker can trade at prices quoted by the primary dealers, but cannot quote prices. Banks, who are primary dealers in either government bonds or T-bills, can be a market taker in the government security segment, where they do not act as a primary dealer.

The central government's primary dealers in government bonds are 10 regional and international banks, cf. Table 3. A primary dealer system for T-bills with 8 participants has been established in connection with the re-opening of the T-bill programme. A broad group of primary dealers enhances interest in Danish government securities and supports competition in connection with issuance and buy-backs by the central government.

Issuance via auctions supplemented with tap sales

Government Debt Management introduced regular auctions in 2009. Experience from issuance via auctions has been positive. Issuance of government bonds via regular auctions will therefore continue, supplemented with tap sales. Issuance on tap provides a regular supply of government securities in the on-the-run issues, making it easier for the banks to accommodate demand from investors on non-auction days.