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The Danish government has a good starting point to finance the expenses related to Corona

- The support packages decided in response to the coronavirus significantly increase the financing need of the government.
- Denmark's low debt, AAA-rating and sound public finances gives a good starting point to finance the increased expenses.
- Denmark has access to several sources of financing, both in domestic and foreign currency. This ensures demand from a broad investorbase.

The support packages passed by the Danish parliament to counter the negative economic impact from the coronavirus means that the central government is expected to increase its spending significantly and will see large but initially temporary shifts in liquidity during the summer. Therefore, it is necessary for the government to show flexibility by using the various financing sources available. This includes issuing in both Danish kroner and foreign currency.

Increased financing requirement

An estimate of the central governments projected revenue and expenditures shows that in the period from the beginning of April to end-July the government's financing requirement is slightly above kr. 250 billion cf. Chart 1. The estimate is subject to great uncertainty. Compared with the estimated financing requirement before the corona crisis it has increased around kr. 200 billion until end-July.

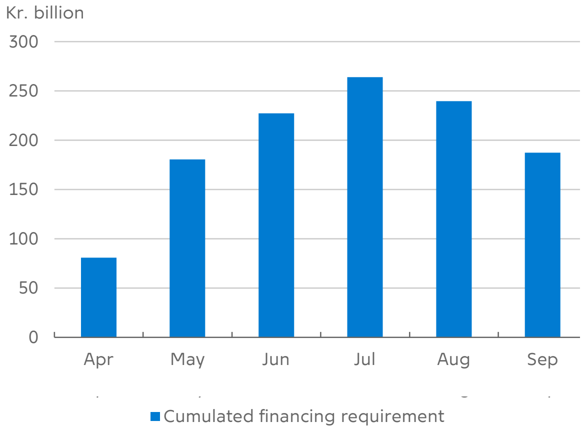
During this crisis the financing need is expected to materialize faster and more sudden compared to earlier crises and downturns. This implies that the central government this time has to secure financing in a high pace.

Denmark has a good starting point
Although, it is a large amount the central government has to finance in the coming months, it does so from a good starting point:

- As one of few countries in the world, Denmark has the highest credit rating, AAA, at all the major rating agencies.
- Denmark has a low government- and EMU-debt (with a very low risk), and a large cash buffer on the central government account at the central bank. This gives room to increase the debt and ensures additional flexibility for the central government to obtain the needed financing.
- Through many years Denmark has maintained a surplus on the balance of payments. By now Denmark has considerable foreign net assets.
- The large Danish private pension savings ensure a natural demand for Danish krone assets.

Thus, it is a fundamentally sound Danish economy that will finance the support packages and the subsequent higher level of debt. Compared to the situation of many other countries, Denmark has a good starting point.

The government has a financing requirement of around kroner 250 billion until end-July Chart 1



Note: The chart illustrates the government's cumulated financing requirement from the end of March to the end of September. The projection is based on Danmarks Nationalbank's monthly distribution of the government's revenues and expenditures, adjusted for the announced effects of the government's initiatives targeting the corona crisis. The estimate is subject to great uncertainty.
Source: Danmarks Nationalbank.

Financing of the support packages

Through many years the central government has maintained a solid liquidity buffer in the form of a high balance on the governments account in the central bank and by maintaining access to a number of funding sources that were not needed with the issuance need in previous years. This means the central government has several tools available to cover the funding need, cf. Box 1.

In ordinary times, the Danish government debt policy follows a very predictable trajectory, where the issuing strategy is announced for the coming year with fairly constant issuance throughout the year.

The increased funding need in 2020, combined with global financial market uncertainty, makes it necessary to exhibit a higher degree of flexibility in the issuance. The flexibility may for instance relate to the distribution of issuances and by issuing to a broader investor base than possible only when issuing in Danish kroner. This also ensures that individual market segments are not burdened unnecessarily.

The financing requirement will be covered by a combination of the following funding sources:

Government bonds:
The issuance target for government bonds in 2020 was in March raised from kr. 75 billion to kr. 125 billion. In general, the goal is to distribute the issuance evenly throughout the year. However, the government's access to other funding sources allows continuous adjustments of the distribution such that issuance during the year is mainly determined by investor demand.

On the one hand, the flexibility in the issuance volume means that bond sales in the coming months can be increased if there is high investor demand, including higher issuance in the 30-year segment than previously announced. On the other hand, if there is limited investor demand government bond sales in the coming months could be lower than an even distribution of the yearly issuance would otherwise indicate.

Treasury bills:
T-bills are a source of short-term financing in Danish kroner. Therefore, part of the funding of the announced temporary covid-19 measures will naturally be obtained in T-bills.

The opening of two new T-bills in March means that the government now has a total of four issues that matures within the next 12 months. The expansion of the T-bill programme makes it possible to attract a larger set of investors. Depending on demand, the end-of-year outstanding amount in T-bills could be significantly higher than the earlier announced target of kr. 30 billion.

Commercial papers:
Like the T-bill programme, the government's two Commercial Paper programmes are a source of short-term financing and are therefore well-suited to offset temporary liquidity shifts. The programmes were activated at the end of March, and total outstanding amount has reached around kr. 35 billion by mid-April. The programmes will be increased further and thereby contribute significantly in meeting the government's funding need over the coming months.

EMTN issuance:
The government may also issue longer maturity bonds in foreign currency (European Medium Term Notes programme, EMTN). Foreign denominated bonds are normally issued to support the foreign exchange reserve, but can also be used to finance the government's current deficit. So far there has not been any EMTN issuance, but the programme is active, and the government can issue EMTNs within a short time.

The government's account:
At the end of March, the balance on the government's account at the central bank was around kr. 130 billion. A substantial part of the government's funding requirement in 2020 can therefore be met by drawing on the government's account.

In the current situation, several – if not all – of the above funding sources of the government will be needed. The distribution between the various funding sources will partly depend on investor demand. The preferred option would be to cover most of the government's funding need by issuing in Danish kroner. However, being one of the few countries in the world with the highest credit rating, Denmark is

Funding sources of the government

Box 1

The central government has access to several sources of funding to meet its borrowing requirements.

The central government's account
The central government holds liquid funds on its account at Danmarks Nationalbank. The balance on the account is part of the central government's liquidity reserve. The balance on the account can fluctuate considerably over the course of a year, mainly due to the large deposits and disbursements of e.g. taxes and salaries of public sector employees. In accordance with Article 123 of the Maastricht Treaty (prohibition of monetary financing), the central government's account must never show a deficit. The central government borrowing is therefore planned to always ensure a positive balance on the government's account.

Treasury bills
Treasury bills, T-bills, are short-term debt securities. The T-bill programme gives the central government access to short-term financing and is part of the central government's liquidity reserve. T-bills are standard products that are issued in kroner. T-bills are zero-coupon papers, i.e. the interest payments are not coupon-based, but are included in the price at which the bills are issued. The programme can be increased either through auctions or tap sales, which are direct sales in the secondary markets. The programme can be expanded with papers with other maturities.

Commercial papers
The central government may raise short-term foreign loans via two Commercial Paper programmes, one European (ECP programme) and one US programme (USCP programme). They may be used both as part of the central government's liquidity reserve and to facilitate quick build-up of the foreign exchange reserve. Unlike T-bills, commercial papers, CPs, are non-standard products with a very high degree of flexibility. The issues can, for example, be adjusted in terms of denomination, maturity (up to 12 months) and currency. The central government can issue up to a limit of USD 12 billion in each of the two programmes. Under the USCP programme, all issuances are in dollars, while it is possible to issue in a number of currencies, including dollars and euro, under the ECP programme. CPs are issued as zero-coupon securities directly to an investor through the central government's bank counterparties in the programmes. The market for CPs is typically very deep. The CP programmes therefore provide the central government with quick and flexible access to liquidity that can withstand even larger liquidity shifts.

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in a favorable position when it comes to obtaining attractive financing conditions in the international debt capital markets.

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Government bonds in kroner
Issuance of government bonds in kroner is the primary tool for the central government to cover the long-term funding need. The central government's on-the-run issues include nominal bonds with maturities between 2 and 30 years, as well as an inflation-linked bond. For a number of years, the central government debt policy has focused on ensuring that the issuances are evenly distributed over the year and concentrated in a few maturity segments, primarily the 2- and 10-year bonds. The strategy has been to support a liquid and well-functioning market during a period of limited borrowing requirements.

Government bonds in foreign currency (EMTN programme)
The central government primarily issues bonds denominated in foreign currency in order to maintain the foreign exchange reserve, but it can also raise foreign loans to finance the domestic borrowing requirements. When the central government borrows in foreign currency, the loan proceeds are placed in the foreign exchange reserve, and the balance on the central government's account increases by the equivalent amount in kroner. Under the EMTN programme, the central government can issue relatively quickly in currencies where the debt market is very deep, while reaching a diversified investor base both in terms of region and investor type.

PUBLICATIONS

NEWS

News offers a quick and accessible insight into an Analysis, an Economic Memo, a Working Paper or a Report from Danmarks Nationalbank. News is published continuously.

ANALYSIS

Analysis from Danmarks Nationalbank focuses on economic and financial matter. Some of the analyses are published with a regular frequency e.g. *Outlook for the Danish economy and Financial stability*. Other analyses are published continuously.

REPORT

Report comprises recurring reports and reviews of the functioning of Danmarks Nationalbank. For instance Report includes the *Annual report* and the annual publication *Danish government borrowing and debt.*

ECONOMIC MEMO

Economic Memo is a cross between Analysis and Working Paper and it often shows the ongoing study of the authors. The publication series is primarily targeted at professionals and is solely available in English. Economic Memo is published continuously.

WORKING PAPER

Working Paper presents research projects by economists in Danmarks Nationalbank and their associates. The series is primarily targeted at professionals and people with an interest for academia. Working Paper is published continuously.

The analysis consists of a Danish and an English version. In case of doubt regarding the correctness of the translation the Danish version is considered to be binding.

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