
Public sector debt: end-March 2000

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Public sector net debt fell by 2.8%, at nominal value,⁽¹⁾ during the financial year to end-March 2000. This was the second successive annual reduction, following seven consecutive annual increases up to 1998. At end-March 2000 public sector net debt represented 36.6% of GDP, the lowest figure since 1994 and 3 percentage points lower than at end-March 1999. This article continues the annual series in the Quarterly Bulletin⁽²⁾ analysing the outstanding financial liabilities of the public sector. It discusses developments during the year, and considers the implications of the current level and structure of UK government debt.

Responsibility for government debt management was transferred to the Debt Management Office (DMO) in April 1998, and in April 2000 Exchequer cash management responsibilities were also passed over. The Bank of England's interest in the level and composition of public sector debt is now concentrated in other areas. Government debt is relevant to the sustainability of fiscal policy, and may impinge on monetary conditions. It is a key part of the collateral used in financial markets, and as such plays an important role in operations to implement monetary policy. In addition, the structure of government debt may influence financial stability, not least because liquid government debt markets at a range of maturities provide a benchmark for private capital markets.⁽³⁾

- The Bank of England is interested in the quantity of outstanding debt and in its composition and ownership, because conditions in the government debt market may influence private sector behaviour, and thereby the prospects for inflation.⁽⁴⁾
- Government debt instruments are widely used as collateral in the secured lending markets. In particular, the Bank implements the Monetary Policy Committee's interest rate decisions through its open market operations. Many of these transactions are undertaken through sale and repurchase (repo) agreements in which government bonds are used as collateral. So significant changes in the quantity of outstanding gilts could affect the liquidity of both the gilt market and the related repo markets.
- The authorities responsible for maintaining financial stability need to monitor the level of risk inherent in the balance sheet of the public sector, as well as the

banking sector and the domestic economy more widely. They need to be alert to the risks of borrowing at short maturities, excessive reliance on borrowing from foreign residents, or large-scale open foreign exchange positions. Reliable statistics on the maturity, currency composition and holders of government debt instruments are necessary to assess these risks.

The level of public sector debt is an important indicator of the government's success in managing the public finances. In recognition of this, the UK government follows a sustainable investment rule, which states the objective of holding debt to a 'stable and prudent level', and has set a target of 40% for the ratio of net debt to GDP over the economic cycle. The government has a second fiscal rule to ensure that borrowing occurs only to finance public sector investments over the cycle. Achieving targets for the levels of the government debt and deficit are also two of the criteria for entry to the single currency monitored by the European Commission under the Maastricht Treaty. Along with inflation, the exchange rate and bond yields, the fiscal position of individual governments is seen as an important indication of a country's degree of convergence with the euro area.

The level of government debt is also monitored by other international organisations. For example, the IMF's Special Data Dissemination Standards, to which the UK government adheres, require that countries report both levels and maturity of central government gross debt on a monthly basis. These data (see Table C), along with information on the government's reserve position, are supplied showing positions in sterling and other currencies separately.

(1) For the purposes of measuring public sector debt, marketable debt instruments are conventionally valued at nominal (ie face) value. In this article all figures are given at nominal value, except where valuation at current market value is stated.

(2) Previously published in the November edition each year.

(3) Discussed further in the [Bank of England Financial Stability Review, June 2000](#).

(4) In June 1998 the Bank of England organised a conference on 'Government debt structure and monetary conditions'. [The discussion is summarised in an article in the November 1999 Quarterly Bulletin](#).

This article reviews developments in the UK public debt from each of these perspectives. It begins with the overall stock of public sector debt, including historical comparisons. The second section gives a more detailed analysis of the financial instruments which make up the debt. As British Government Stocks (gilts) are by far the most significant of these, the article focuses on the structure of the gilt portfolio and sets out changes in yields and market values during the year. The third section gives information on the ownership of debt and considers the UK government debt position relative to other countries. Finally, comparisons are drawn between the level of debt and the overall government balance sheet.

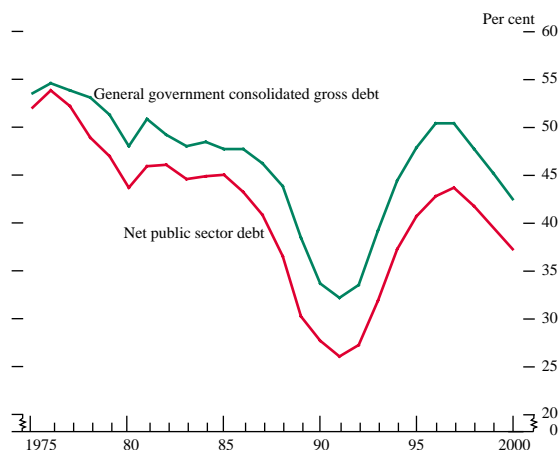
Total stock of outstanding public sector debt

The net debt⁽¹⁾ of the public sector (PSND) fell by nearly £10 billion (2.8%) in the 1999/2000 financial year, from £349 billion to £339 billion at nominal value (see Table A). The market valuation was about £35 billion higher than this. Nominal net debt fell by 3 percentage points, to 36.6% of GDP, the lowest ratio since 1994 (see Chart 1). The fall, which was largely in amounts borrowed through gilts and in holdings of foreign currency debt, reflected an £8.7 billion surplus in the public sector cash flow during the financial year (see Table B).

The current debt ratio is low by historical standards. Chart 2 shows that though the nominal debt level is high, it

is at a relatively low level as a proportion of GDP. This reflects the fact that nominal GDP rose at a faster rate than the level of debt from 1945 to the late 1970s, and the two have grown broadly in line since then (though varying over the cycle). The ratio since the 1970s is closer to that in the years prior to 1914 than at any time between.

Chart 1
Measures of public sector debt as a percentage of GDP, 1975–2000^(a)



(a) At end-March each year.

Table B
Composition of the PSNCR

£ millions	1997/98	1998/99	1999/2000
Central government net cash requirement (CGNCR)	3,542	-4,535	-9,146
Memo item: CGNCR on own account	2,650	-6,170	-10,559
Local government net cash requirement (LGNCR)	-820	-404	860
less borrowing from central government	955	1,869	1,400
General government net cash requirement (GGNCR)	1,767	-6,808	-9,686
Public corporations' net cash requirement (PCNCR)	-719	-386	1,009
less borrowing from central government	-63	-234	13
Public sector net cash requirement (PSNCR)	1,111	-6,960	-8,690
as a percentage of GDP	0.1%	-0.8%	-0.9%

Table A

Public sector net debt

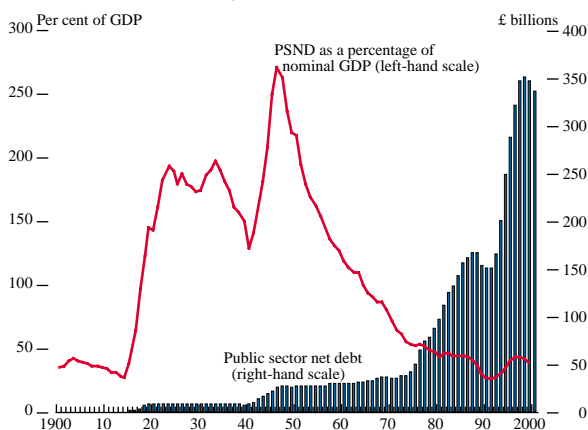
£ millions, nominal values (a); percentages in italics

31 March (b)	1998	1999	2000	Changes 1999–2000
Central government gross debt	393,879	392,277	382,886	-9,391
as a percentage of GDP	46.8	44.6	41.4	-3.2
Local government				
Total gross debt	51,933	52,742	53,437	695
less holdings of other public sector debt:				
Central government holdings of				
local government debt	43,397	45,273	46,656	1,383
Local government holdings of				
central government debt	170	273	254	-19
General government consolidated gross debt	402,245	399,473	389,413	-10,060
as a percentage of GDP	47.8	45.4	42.1	-3.3
Public corporations				
Total gross debt	26,044	26,775	26,812	37
less holdings of other public sector debt:				
Central government holdings of				
public corporation debt	25,668	26,440	26,453	13
Local government holdings of public				
corporation debt	0	4	1	-3
Public corporation holdings of central				
government debt	7,485	6,528	6,169	-359
Public corporation holdings of local				
government debt	810	780	812	32
Public sector consolidated gross debt	394,326	392,496	382,790	-9,706
as a percentage of GDP	46.8	44.6	41.4	-3.2
Total public sector liquid assets	41,474	43,847	43,991	144
as a percentage of GDP	4.9	5.0	4.8	-0.2
Net public sector debt	352,852	348,649	338,799	-9,850
as a percentage of GDP	41.9	39.6	36.6	-3.0

(a) Figures may not sum to totals because of roundings.

(b) Data from 1975 to 1999 are published in the *Bank of England Statistical Abstract 1999*, Part 1, Table 14.1.

Chart 2
Gross national debt, 1900–2000



Source: HM Treasury.

(1) Defined as gross financial liabilities at nominal value minus short-term assets.

The PSNCR and changes in the public sector net debt: reconciliation

Public sector net debt is a stock measure, and its change is calculated on a nominal, accrued basis. In contrast, the PSNCR, financed by transactions in assets and liabilities, is measured on a cash-flow basis. This leads to differences between the change in public sector net debt and the PSNCR for any given period, mainly because of the following:

- The value of foreign currency liabilities and assets is affected by fluctuations in exchange rates, and so the debt changes independently of any transactions that affect the PSNCR.
- When gilts are issued (or bought in ahead of their redemption date) at a discount or premium, the PSNCR is financed by the actual cash amount received (or paid out). The level of debt, however, is deemed to have changed by the nominal value of gilts issued (or redeemed).
- The capital uplift on index-linked gilts is recorded in the PSNCR only when it is paid out, ie when the stock is redeemed. In the measure of debt outstanding, it is accrued over the life of the stock.

£ billions	Year ending March 2000
PSNCR	-8.7
<i>Plus</i>	
Revaluation of foreign currency assets/liabilities	-0.5
Capital uplift on index-linked gilts	1.9
Discount/premium on gilt issues	-2.1
Other	1.1
<i>Equals</i>	
Change in public sector net debt	-8.4

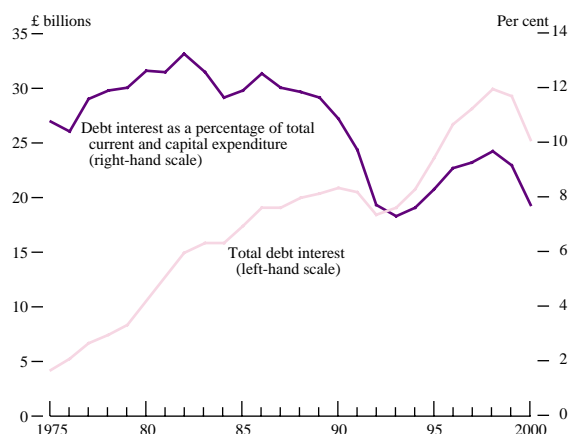
Note: Figures may not sum to total because of roundings.

Financing remits for 1999/2000 and 2000/01

The financing requirement⁽¹⁾ for central government for 1999/2000, which determines the amount of gilts and other debt instruments issued, was revised downwards during the financial year. This reduced the amount of gilt sales required, from the forecast of £17.3 billion to an actual amount of £13.6 billion. This was mainly the result of an improvement in the 1999/2000 central government net cash requirement (CGNCR), from a forecast deficit of £6.2 billion to an actual surplus of £9.2 billion. This improvement in the government's finances resulted in the cancellation of planned sales of Treasury bills and other short-term debt, and instead a net £8.8 billion of these instruments were redeemed. Net National Savings contributions also fell during the financial year (by -£1.1 billion), in contrast to the initial assumption of a slight increase (of £0.1 billion).

Interest and dividend payments on public sector debt during 1999/2000 were £3.9 billion lower than in the previous year. At £25.3 billion, this represented 7.7% of total public sector current and capital expenditure in the year, compared with 9.2% in 1998/99 (see Chart 3). This fall partly reflected the reduced net cash requirement, but was also influenced by a decline in short-term interest rates.

Chart 3
Public sector debt interest^(a)



Source: Office for National Statistics.

(a) At end-March each year.

The latest assumption for the 2000/01 financing requirement was published by the DMO on 12 June 2000. This took into account the proceeds from the auction of mobile telephone licences in April, which, at £22.5 billion, were considerably higher than HM Treasury forecasts had previously assumed. The latest forecast for 2000/01 projects a cash surplus of £5.6 billion. Nevertheless, gilt sales totalling £10.0 billion are still planned for the year, made up of long-dated conventionals (£6.5 billion) and index-linked stock (£3.5 billion). The earlier plan to issue £2.2 billion of medium-dated conventional stock has now been abandoned. This emphasises the DMO's policy of concentrating issuance in long-dated conventionals and index-linked bonds, driven by market demands for these products, which are increased by the regulatory solvency requirements (the Minimum Funding Requirement).

Most forecasters expect that net public sector debt will continue to fall in the short term. The use of proceeds from the mobile phone auctions to redeem debt instruments and reduce new issuance makes this outcome more likely.

Analysis of public sector debt components

Total public sector gross debt (ie PSND before liquid assets are deducted) consists almost entirely of central government gross debt (CGGD) (see Table A). This is despite significant levels of local government and public corporations' gross debt (£53 billion and £27 billion respectively at end-March 2000); the vast majority of this is

(1) Published by the Debt Management Office, an Executive Agency of HM Treasury.

borrowed from central government and is thus netted out when calculating the consolidated figure. Also, although more than £6 billion of local government debt is not held by central government, this is offset in the public sector debt figures by a similar level of central government debt held by public corporations, such as the Post Office.

British Government Stocks (gilts)

Gilts continue to be the main component of the outstanding stock of government debt, accounting for 74% of CGGD at end-March 2000 (see Table C and Chart 4). This was 1 percentage point higher than a year earlier, despite total gilts falling during the financial year by £2.4 billion, to £283 billion.

Table C
Central government gross debt

£ millions, nominal values; *percentage of total in italics*

End-March (a)	1999		2000	
British Government Stocks	285,394	72.8	282,996	73.9
<i>of which: index-linked</i>	62,289	15.9	65,703	17.2
<i>other</i>	223,105	56.9	217,293	56.8
Sterling Treasury bills	4,721	1.2	4,453	1.2
National Savings	63,621	16.2	62,581	16.3
Certificates of tax deposits	574	0.1	535	0.1
Other sterling debt	26,147	6.7	23,368	6.1
Central government sterling gross debt	380,457	97.0	373,933	97.7
North American government loans	453	0.1	359	0.1
US\$ floating-rate notes	1,239	0.3	1,254	0.3
US\$ bonds	3,098	0.8	3,134	0.8
Euro Treasury bills (b)	2,341	0.6	0	0.0
Euro 9 ¹ / ₈ % 2001 bond	1,672	0.4	1,500	0.4
Euro Treasury notes	3,010	0.8	2,701	0.7
Debt assigned to the government	6	0.0	5	0.0
Central government foreign currency gross debt (c)	11,819	3.0	8,953	2.3
Total central government gross debt	392,276	100.0	382,886	100.0

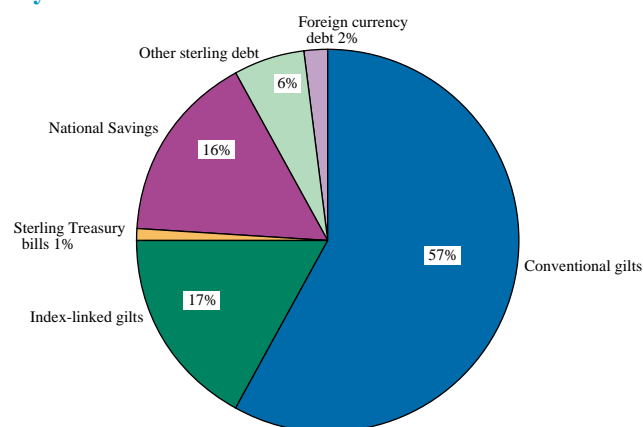
(a) Data from 1975 to 1999 are published in the *Bank of England Statistical Abstract 1999*, Part 1, Table 14.2.

(b) The Bank of England assumed responsibility for the issuance of euro bills from 1 April 1999.

(c) Sterling valuation rates:

31 March 1999: £1 = US\$ 1.6138, Can\$ 2.4415, €1.4951
31 March 2000: £1 = US\$ 1.5952, Can\$ 2.3146, €1.6662

Chart 4
Composition of central government gross debt
by instrument: end-March 2000^(a)



(a) Figures may not sum to 100% because of roundings.

The stock of index-linked gilts continued to rise. Including capital uplift (the accrued inflation-linked valuation adjustment), the total held outside central government rose by £3.4 billion during 1999/2000. This was more than offset by a year-on-year fall of £5.8 billion in market holdings of conventional gilts. At end-March 2000 the nominal value of index-linked gilts in market hands totalled £65.7 billion, a 5% annual rise. Excluding the capital uplift, issuance of index-linked gilts totalled £1.6 billion. In cash terms, £3.0 billion was raised—meeting the DMO's commitment to issue at least £2.5 billion in index-linked stock during the year.

Index-linked issuance represented 22% of total gilts issued during 1999/2000, the remainder being conventionals. New issuance of conventional gilts totalled £9.8 billion at nominal value. This included two auctions of the long-dated benchmark 6% Treasury Stock 2028 (totalling £4.5 billion at nominal value) and one auction of the 10-year benchmark 5³/₄% Treasury Stock 2009 (£2.8 billion).⁽¹⁾

The average remaining life of market holdings of gilts at end-March 2000 was 9.9 years (see Table D). This is the highest figure among the world's major economies and, since longer maturities minimise the need to continually raise new funds to redeem maturing debt, indicates a relatively stable financial position. The figure for the United Kingdom has been relatively unchanged in recent years, despite the preference within HM Treasury's issuance strategy towards long-dated stocks.⁽²⁾ The falling gilts sales requirement has made it difficult to balance the market's desire for more long-dated stock with the government's reduced need to raise funds. Chart 5 shows the maturities of existing dated stocks, by nominal value in market hands, at end-March 2000. The modified duration figures, which indicate the percentage fall in the average market price of the gilt portfolio that would be associated with a single percentage point rise in yields, show an upward trend since 1990.

Table D
Average remaining life of dated stocks in market hands^(a)

	Years to maturity at 31 March									
	1992	1993	1994	1995	1996	1997	1998	1999	2000	
Latest possible redemption										
All dated stocks (b)	10.0	10.8	10.6	10.4	10.1	10.1	10.2	10.0	9.9	
Excluding index-linked stocks	8.4	9.4	9.1	9.1	8.8	8.8	9.0	8.9	8.9	
Earliest possible redemption date										
All dated stocks	9.8	10.5	10.4	10.2	9.9	9.9	10.0	9.9	9.9	
Excluding index-linked stocks	8.1	9.0	8.9	9.1	8.8	8.7	8.9	8.8	8.8	
Modified duration										
All dated stocks	6.0	6.7	6.7	6.3	6.1	6.3	6.9	7.4	7.4	
Excluding index-linked stocks	5.3	5.9	5.9	5.5	5.3	5.5	6.1	6.4	6.3	

(a) These data are based on the nominal value of dated stocks held by the market at 31 March each year.

(b) Index-linked stocks are given a weight reflecting capital uplift accrued to 31 March.

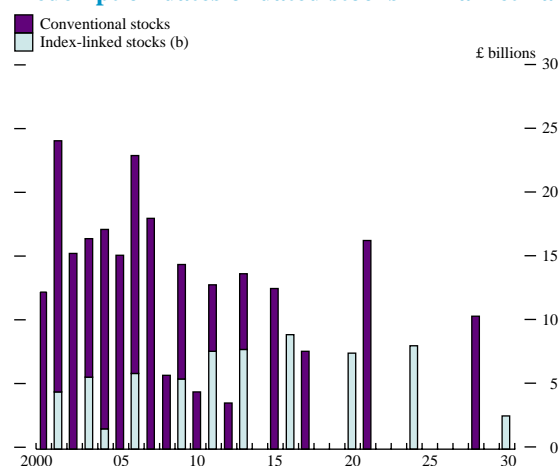
The gilt yield curve, which measures the return on investments in gilts by maturity, began the financial year fairly flat, with yields very similar across all maturities.

(1) Details of gilt transactions are given each quarter in the 'Markets and operations' article in the *Bank of England Quarterly Bulletin*.

(2) *Debt Management Report*, HM Treasury, March 2000.

This picture changed during the year to the extent that the 5-year benchmark yield rose by around 125 basis points while the yield on the 20-year benchmark fell by 26 basis points. The increase in 5-year yields largely reflected a more general rise in short-term interest rates: the Bank of England repo rate in March 2000 was 50 basis points higher than a year earlier. At the long end, reductions in the net supply of gilts, combined with the continued strong demand for these assets by pension funds and life insurance companies, pushed market prices higher and yields lower.

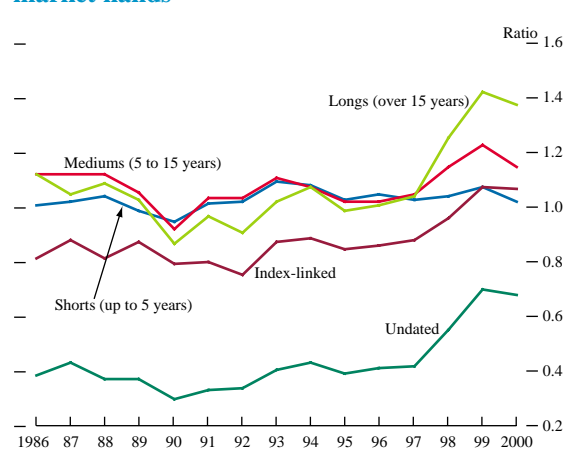
Chart 5
Redemption dates of dated stocks in market hands^(a)



(a) As at end-March 2000, using latest possible redemption dates.
(b) Figures include accrued capital uplift to 31 March 2000.

The changes in gilt prices at different maturities are reflected in the market to nominal valuation ratios shown in Chart 6. Overall, £318 billion of gilts at market value were owned by the market at end-March 2000, 5% lower than a year earlier. However, this still represented an average 12% premium to the total at nominal value. The sharpest fall in

Chart 6
Ratios of market to nominal values of stocks in market hands^(a)



(a) At end-March each year.

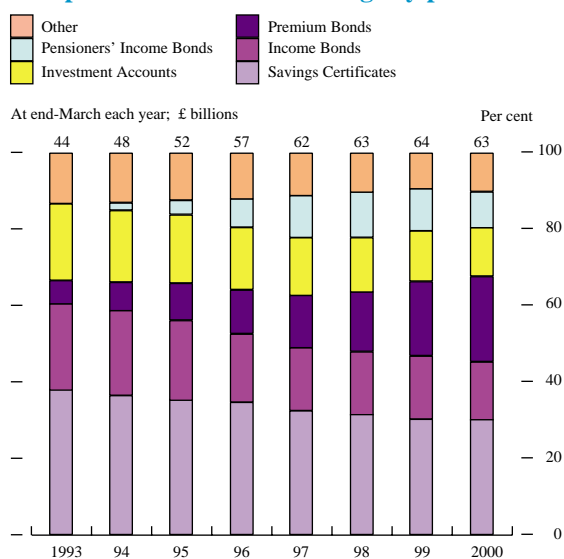
market prices over the financial year was among medium-dated stocks, which at end-March 2000 were trading at an average 18% premium to their nominal value, a reduction of 8 percentage points from a 23% premium a year earlier.

National Savings instruments

The outstanding balance of National Savings instruments at end-March 2000 was £62.6 billion, £1.1 billion lower than a year earlier. During 2000/01 the balance is forecast to fall by a further £0.8 billion—reflecting instruments falling due for redemption in 2000/01—according to the 2000 *Debt Management Report*. Gross sales (ie sales and deposits including accrued interest) are expected to be around £12.5 billion, compared with £10 billion in 1999/2000.

National Savings instruments accounted for 16% of central government gross debt at end-March 2000 (see Chart 7), roughly the same as a year earlier. The proportion of National Savings held in Premium Bonds has now risen for eight consecutive years, to 22% in March 2000 from 6% in March 1993. As a consequence, the share of other instruments fell during 1999/2000, including Income Bonds which fell by 2 percentage points to 28%.

Chart 7
Composition of National Savings by product



Source: Department of National Savings.

Sterling Treasury bills

Sterling Treasury bills accounted for 1.2% of central government gross debt at end-March 2000. At £4.5 billion, this was 6% lower than a year earlier.⁽¹⁾

Foreign currency

At end-March 2000 the sterling value of foreign currency debt outstanding was £9.0 billion, a 24% drop since

(1) More detailed analysis of the changes in Treasury bill issuance during the financial year is reported quarterly in the 'Markets and operations' article.

EC excessive deficit procedure: treatment of financial derivatives

There has been much discussion among statisticians and debt managers across Europe about the treatment of financial derivatives in government debt statistics. This box explains the background.

In 1997 the international guidelines for national statistical accounts, the System of National Accounts (SNA), were expanded by an international working group, led by the International Monetary Fund (IMF), following consultations aimed at amplifying and simplifying coverage of financial derivatives. These revisions included detailed guidance on the definition of financial derivatives for statistical purposes, the valuation of positions, the classification of margin payments and the treatment of settlement payments associated with interest rate swaps (including cross-currency swaps) and forward-rate agreements (FRAs).

The treatment of swap settlement flows under ESA95 was consistent with the initial SNA guidance, which explicitly stated that payments associated with interest rate swaps and FRAs should be included as property income. This means that the flows would be treated as revenues (or expenses), which in turn would contribute towards some sectoral balances (eg the general government deficit). This treatment was changed under the revised SNA.

It has been proposed that ESA95 be revised to maintain consistency with SNA. However, while this proposal has been accepted as necessary in a national accounts context, the implications for government deficit statistics have resulted in considerable resistance from those responsible for the management of government debt in certain countries. Because Maastricht debt and deficit are compiled on an

ESA95 basis, any change to the accounting basis has knock-on implications for the debt and deficit figures.

For government deficits the proposed revision means that the revenues and payments arising from swap transactions conducted by government debt managers for hedging purposes, ie to reduce the risk inherent in borrowing in other currencies, would be treated as financial flows. It is argued that the use of these instruments within this context is for genuine debt management reasons, and is not speculative. Smaller countries, with weaker currencies, have used foreign currency interest rate swaps to hedge against fluctuations in the value of their own currency.

Such transactions are not widely used in the United Kingdom. All foreign currency borrowing by UK debt managers is directed towards helping to finance the foreign currency reserves, with the foreign exchange and interest rate risks hedged as part of the reinvestment of the proceeds within the reserves. It is very rare that foreign currency debt is swapped into sterling, and gilts have never been directly swapped either into sterling or into foreign currency. Any swaps that are undertaken are booked within the reserves rather than within the government debt accounts.

The solution proposed by Eurostat, which is supported by statisticians in most EU Member States, is to adopt the revised treatment of swaps within the main accounting framework of the ESA, thereby retaining consistency with wider international standards, but to recognise the need for a second measure of net borrowing which reflects the role of swaps as part of the wider cost of borrowing. No decision has yet been taken.

March 1999 (see Table C). This fall was almost entirely the result of the transfer of responsibility for euro bill issuance from HM Treasury to the Bank of England from 1 April 1999. At end-March 1999, market holdings of euro bills stood at £2.3 billion, ranging in maturity from one month to six months. By end-September 1999 all bills issued by HM Treasury had therefore matured.

Although the Bank of England is now the issuer of euro bills, there were no significant changes in the euro bill issuance programme. The proceeds are used by the Bank to finance the provision of intra-day liquidity, on a secured basis, to members of the euro payment system, and are held on the Bank of England's balance sheet as foreign currency assets.

The government's foreign currency reserves are an important component of the liquid assets of the public sector (see Table E). At end-March 2000 reserves totalled £21.5 billion, of which £6.8 billion was held in US dollars, £5.5 billion in euro and £3.0 billion in yen. Holdings of gold within this totalled £3.2 billion, at market value, at end-March 2000.

Table E
Public sector liquid assets

£ millions, nominal values

31 March (a)	1998	1999	2000	Change 1999-2000
Central government				
Official reserves	21,293	22,147	21,498	-649
Bank and building society deposits	2,292	1,762	3,398	1,636
Total central government liquid assets	23,585	23,909	24,896	987
Local government				
Bank deposits	7,994	8,519	7,434	-1,085
Building society deposits	3,796	3,756	4,324	568
Other short-term assets	3,693	4,334	4,754	420
Total local government liquid assets	15,483	16,609	16,512	-97
Public corporations				
Bank and building society deposits	1,469	2,029	1,455	-574
Other short-term assets	937	1,300	1,128	-172
Total public corporation liquid assets	2,406	3,329	2,583	-746
Total public sector liquid assets	41,474	43,847	43,991	144

(a) Data from 1975 to 1999 are published in the *Bank of England Statistical Abstract 1999*, Part 1, Table 14.1.

Ownership of government debt instruments

Some information is available about the sectoral identity of holders of government debt instruments. The estimated

distribution of the central government sterling gross debt is shown in Table F. Table G gives more detail for March 2000, showing estimated holdings of individual debt instruments by each sector. These are provisional estimates, based on a range of data sources, and are subject to revision.

Table F
Distribution of central government sterling gross debt: summary^(a)

£ billions; *percentage of total in italics*

Amounts outstanding at 31 March

	1999		2000		Change 1999/2000
		<i></i>		<i></i>	
Public sector	5.8	<i>1.5</i>	3.6	<i>1.0</i>	-2.2
Banks	32.9	<i>8.6</i>	29.2	<i>7.8</i>	-3.7
Building societies	1.0	<i>0.4</i>	1.1	<i>0.3</i>	0.1
Institutional investors	183.0	<i>48.1</i>	186.3	<i>49.8</i>	3.3
Individuals and private trusts	89.9	<i>23.6</i>	93.0	<i>24.9</i>	3.1
Other UK residents	9.6	<i>2.5</i>	1.2	<i>0.3</i>	-8.4
Non-residents	58.3	<i>15.3</i>	61.9	<i>16.5</i>	3.6
Total	380.5	<i>100.0</i>	373.9	<i>100.0</i>	-6.6

Note: Figures shown may not sum to totals because of roundings.

(a) See Table G for more detail.

These figures show that banks' holdings of debt instruments continued to fall, for the fourth consecutive year, during 1999/2000. On the other hand, institutional investors,

including insurance companies and pension funds, increased their stock during the year. Despite the overall fall in the sterling CGGD, individuals, private trusts and non-UK residents increased their holdings.

International comparisons

Along with other EU countries, the United Kingdom is required under the terms of the Maastricht Treaty to report government finance statistics to the European Commission for economic convergence reasons.

The Stability and Growth Pact (SGP) measures general government consolidated gross debt (GGCGD), calculated as a percentage of nominal GDP.⁽¹⁾ Most measures of debt monitor the ratio against GDP because GDP is closely linked to the tax base of the economy, and hence to the government's ability to service its debt. If the government can maintain its current spending and taxation plans indefinitely, while meeting its debt-servicing obligations, its fiscal stance is considered sustainable.

The latest figures submitted to the Commission show that UK gross government debt at end-December 1999 represented 46.0% of GDP. Apart from Luxembourg, this

Table G
Estimated distribution of central government sterling gross debt: 31 March 2000

£ billions, nominal values (a)

	Total	British Government Stocks (b)				Treasury bills	Other
		Total	Up to 5 years to residual maturity	Over 5 years and up to 15 years	Over 15 years and undated		
Public sector							
Local government	0.1	<i>0.1</i>	0.0	0.1	0.0	0.0	0.0
Public corporations	3.5	<i>3.5</i>	1.4	1.9	0.2	0.0	0.0
Total public sector	3.6	<i>3.6</i>	1.4	2.0	0.2	0.0	0.0
Banks (c)	29.2	<i>7.7</i>	3.6	2.7	1.5	1.8	19.7
Building societies	1.1	<i>0.8</i>	0.8	0.0	0.0	0.0	0.3
Institutional investors							
Insurance companies	104.7	<i>103.9</i>	24.7	43.8	35.3	0.6	0.2
Pension funds	77.3	<i>76.5</i>	20.6	36.0	19.9	0.6	0.2
Investment and unit trusts	4.4	<i>4.2</i>	1.8	1.7	0.7	0.0	0.2
Total institutional investors	186.3	<i>184.5</i>	47.1	81.5	55.9	1.2	0.6
Individuals and private trusts	93.0	<i>27.7</i>	11.8	10.7	5.2	0.0	65.3
Other UK residents	1.2	<i>0.1</i>	0.0	0.0	0.0	0.3	0.8
of which: Private non-financial companies	1.2	<i>0.1</i>	0.0	0.0	0.0	0.3	0.8
Non-residents							
International organisations	2.7	<i>0.7</i>	0.4	0.2	0.1	0.0	2.0
Central monetary institutions	16.7	<i>15.9</i>	9.0	4.1	2.8	0.8	0.0
Other	42.5	<i>41.9</i>	18.2	13.0	10.7	0.6	0.0
Total non-residents	61.9	<i>58.5</i>	27.6	17.2	13.6	1.4	2.0
Total	373.9	<i>283.0</i>	92.4	114.1	76.5	4.5	86.5

Note: Figures shown may not sum to totals because of roundings.

(a) Some of these estimates are based on reported market values; some others rely on broad nominal/market value ratios.

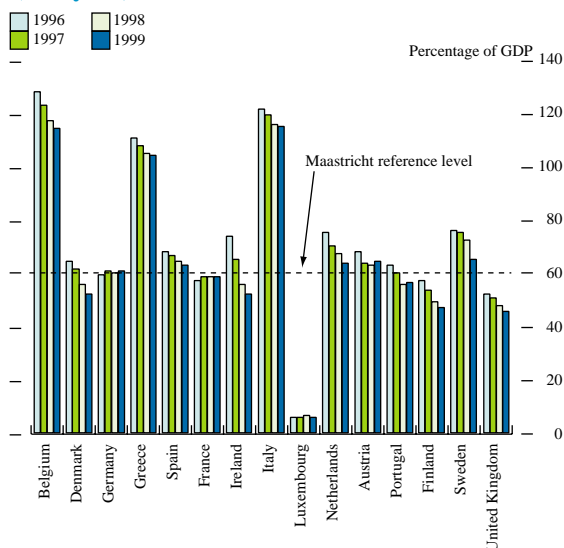
(b) A sectoral analysis of gilt holdings from 1975 to 1999 is published in the *Bank of England Statistical Abstract 1999*, Part 1, Table 14.4.

(c) Includes the Issue and Banking Departments of the Bank of England.

(1) At present the SGP's definition of GGCGD differs slightly from the definition used in the calculation of debt in the United Kingdom, where the emphasis is on debt representing the stock equivalent of the net cash requirement (PSNCR). The UK definition, although broadly based on the internationally agreed European System of Accounts (ESA95), does not currently include accruing liabilities arising from instruments where no actual transfer of funds takes place, such as finance leases. The Bank of England, HM Treasury and the Office for National Statistics are considering bringing the UK definition into line with that of the Pact.

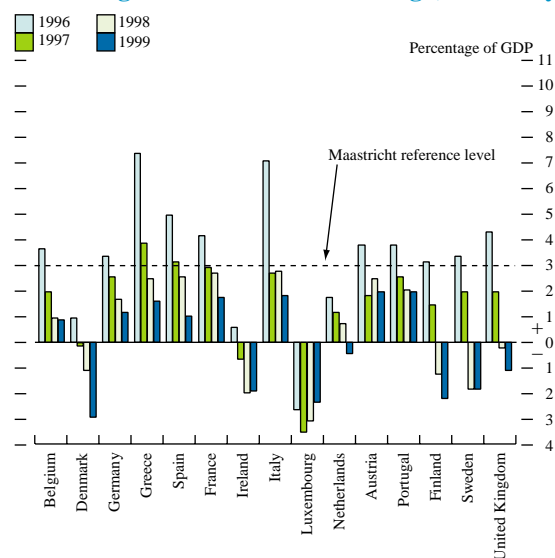
was the lowest among EU countries (see Chart 8), and is comfortably below the reference level of 60%. Debt ratios reported by Belgium, Greece and Italy remained above 100% of GDP in 1999.

Chart 8
General government consolidated gross debt
(end-year)



Source: Eurostat.

Chart 9
General government net borrowing (calendar year)



Source: Eurostat.

The deficit reported under the Pact is the ratio of general government net borrowing to GDP, and the terms of the Pact allow deficits of up to 3%. Figures reported for 1999 by all countries met this condition, and the United Kingdom (-1.2%) was one of seven countries to report a net surplus (see Chart 9). In line with improving economic conditions, net borrowing in almost all EU countries has fallen consistently since 1996.

(1) Source: OECD *Economic Outlook*.

(2) More details are given in *Blue Book 2000*, Office for National Statistics, July 2000.

Some comparable information is available for other, non-EU, countries. For the United States, federal debt has been relatively stable in relation to GDP over the last four years, standing at 51% at end-December 1999. In contrast, Japanese government debt has increased rapidly in recent years, reaching a ratio of 84% at end-1999.⁽¹⁾

Government balance sheet

Although measured at nominal value, the debt of government closely reflects its financial liabilities, which are measured at current market value. Table H shows how this relates to the total level of government assets and liabilities as published in the national accounts,⁽²⁾ at market value. The government sector is a net borrower in financial balance sheet terms, with financial assets falling short of financial liabilities by some £330 billion at end-1999. However, with non-financial assets, including buildings and infrastructure, valued at £447 billion, the net 'worth' of the general government sector was valued at a positive £117 billion at end-1999. The short-term assets, which contribute to the calculation of nominal net debt, represent a relatively small proportion of the total general government assets figure of £626 billion.

Table H
General government balance sheet

£ billions	1997	1998	1999
31 December			
Non-financial assets			
Tangible assets			
Residential buildings	71.2	79.0	78.7
Agricultural assets	2.8	2.8	2.7
Commercial, industrial and other buildings	110.7	115.5	118.4
Civil engineering works	183.5	203.3	223.7
Plant and machinery	16.4	16.8	17.5
Vehicles, including ships and aircraft	5.1	5.0	4.6
Stocks and work in progress	0.8	0.9	0.6
Total tangible assets	390.5	423.3	446.2
Total intangible assets	0.7	0.9	1.1
Total non-financial assets	391.2	424.2	447.3
Total financial assets	166.9	169.2	178.3
Total assets	558.1	593.4	625.6
Total liabilities	491.2	528.8	508.6
Net worth	66.9	64.6	117.0

Source: ONS, *Blue Book*.

Conclusion

The UK net public sector debt ratio is currently low by both historical and international standards. Over the economic cycle it appears to be within the range targeted by the government's sustainable investment rule, and is well below the Maastricht reference level of 60%. Most forecasters expect the level to continue to fall in the short term. With government receipts exceeding expenditure in 1999/2000, which is likely to be repeated this financial year, the present picture is one of stable and sustainable public finances.

UK government debt has a relatively long average maturity, which limits roll-over risk, and a small proportion is held in foreign currency instruments, reducing external risk.

The declining debt position has created a shortage of long-dated and index-linked government stock. The DMO is attempting to address this issue, for example through switch auctions, but if the stock continues to decline, shortages of stock at one maturity or another will remain. Should the debt ratio continue to fall, the reduced liquidity

of the government bond market could potentially affect the ability to sell or repo out government bonds in the event of funding strain.⁽¹⁾

The reduced availability of gilts creates opportunities for fund-raising for long-term investment by companies, and the gilt shortages may add pressure for changes in the Minimum Funding Requirement, applicable to certain long-term investors, to ease the pressure on pension funds and other long-term investors.

(1) This (and other questions posed by shrinking government bond markets) is discussed in the Bank of England *Financial Stability Review*, June 2000.

Annex

Notes and definitions

Central government gross debt

Comprises:

British Government Stocks (BGS): Sterling, marketable, interest-bearing securities issued by the UK Government. The nominal value of index-linked gilt-edged stocks is increased by the amount of accrued capital uplift. The whole nominal value of all issued stocks is recorded, even where outstanding instalments are due from market holders (where this is the case, the outstanding instalments are recorded as holdings of liquid assets). This article uses the same definition of short and medium-dated gilts as the National Loans Fund (NLF) accounts (under five years and five to ten years respectively). In the financing requirement, however, and in general market usage, short-dated gilts are defined as three to seven years and medium-dated as seven to fifteen years.

Treasury bills: Short-term instruments generally issued with either a one-month or a three-month maturity. The bills, which can be traded on the secondary market, are sold at a discount and redeemed at par. The amount of discount depends on the price accepted by the issuer at the tender.

National Savings securities: Non-marketable debt comprising a variety of products available to the public.

Certificates of tax deposit: Non-marketable debt available to taxpayers generally, which may be used in payment of most taxes.

Other sterling debt: Includes *coin* in circulation, *Ways and Means advances* (the method by which government departments and the Bank of England Issue Department lend overnight to the NLF), *NILO stocks* (non-marketable stocks, issued directly to the National Debt Commissioners, whose terms reflect those on existing BGS), the *temporary deposit facility* (deposits by central government bodies and public corporations with the NLF), deposits with the National Debt Commissioners of *funds lodged in courts*, market holdings of *Northern Ireland government debt* (principally Ulster Savings Certificates), *bank and building society lending*, *balances of certain public corporations with the Paymaster*

General, funds held on behalf of the European Commission, other third-party deposits (from the Insolvency Service), and the *net liabilities, guaranteed by government, of the Guaranteed Export Finance Company (GEFCO)*, following the reclassification of its transactions to central government in 1987.

Foreign currency debt: Converted to sterling at end-period middle-market closing rates of exchange and comprises *foreign currency bonds* (denominated in US dollars, Deutsche Marks and euro), *euro notes and bills*, *long-term post-war loans* from the governments of the United States and Canada and *assigned debt* (debt originally drawn under the Exchange Cover Scheme and transferred to the government following privatisations of public corporations).

Public sector consolidated gross debt

This includes *central government gross debt*, as well as all *local government and public corporation debt*. All holdings of each other's debt by these three parts of the public sector are netted off to produce a consolidated total.

The local government sector comprises all bodies required to make returns under the various local authorities Acts. Public corporations are trading bodies (including nationalised industries), which have a substantial degree of independence from the public authority that created them, including the power to borrow and maintain reserves. For further details, see Chapter 4 of the *Financial Statistics Explanatory Handbook*, published by the Office for National Statistics.

Public sector net debt

The public sector net debt is derived from the consolidated debt of the public sector by deducting the public sectors' holdings of liquid (short-term) assets.

General government consolidated gross debt

Central government and local government gross debt with holdings of each other's debt netted off to produce a consolidated total.