

Focus

Many countries have set up large financial rescue packages to mitigate the economic consequences of the COVID-19 outbreak, resulting in increased spending. Consequently, government debt is growing worldwide. For example, the debt ratio of the Netherlands (government debt to GDP) is expected to increase from 48.6% to 63.1% and in the US it is even expected to increase from 107.7% to 120.0% (see graph). What does an increase in government debt tell us and up to what level can government debts continue to grow?

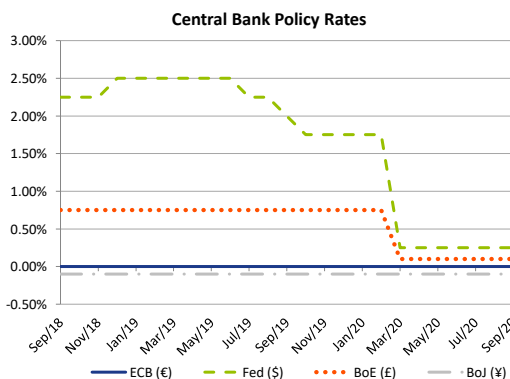
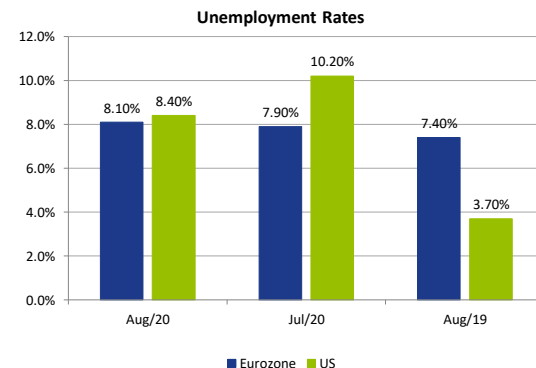
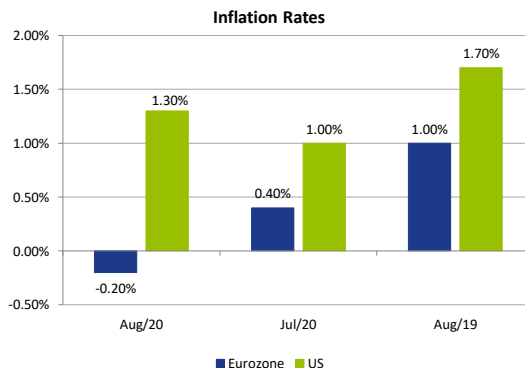
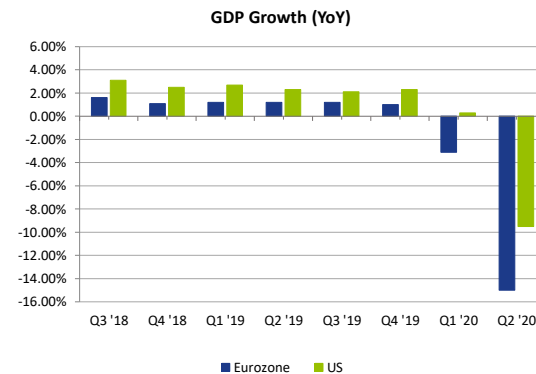
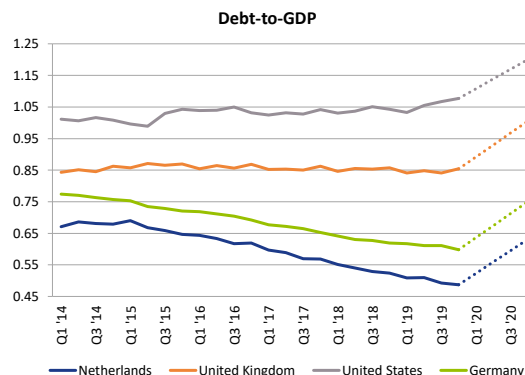
Most countries have a yearly budget deficit. Their expenditures exceed their income. This budget deficit must be supplemented with borrowed money (also known as government debt). Governments can raise money by issuing various financial products, such as bonds. Another common way is simply to borrow from the World Bank, central banks or private financial institutions.

Although government debt can be expressed in an absolute figure, it is usually measured as a percentage of gross domestic product (GDP), also called the debt ratio. By comparing absolute public debt with GDP, it becomes visible whether the debt can be repaid over time. As a country's economy grows, so does the amount of income a government can use to pay off its debt. There are, however, some arguments that the debt to GDP ratio is not the good approach to assess debt, as GDP difficult to measure accurately. In addition, national debt has to be repaid with tax revenue and not with GDP.

The World Bank has conducted a study to determine the impact of government debt on an economy ("Finding The Tipping Point -- When Sovereign Debt Turns Bad", 2010). This study shows that countries with a debt ratio of more than 77% experience a significant decrease in economic growth over long periods of time. Each percentage point of debt above this level results in a decrease of 1.7% in annual economic growth.

As a result, various governments have set standards regarding their public debt. For example, with the enactment of the Stability and Growth Pact (SGP), EU Member States have agreed to limit their debt to 60% of GDP. In the United States, they use a somewhat different method. In the United States, an absolute value public debt is used, which can only be increased with the approval of Congress.

All in all, the global growth of public debt might indicate that we are heading towards a period of lower economic growth, if the research of the World Bank is to be believed. However, this research was conducted over a period (1980-2008) with interest rates that were considerably higher than the current interest rate. Various governments state that their growth in public debt will only be temporary and that raising new debt is therefore justifiable. When the lockdown measures can stop, there will no longer be any need for the emergency funds. The question is now when this will be and how easy it will be to reduce government debt when everything is 'back to normal'.



| Country Ratings | S&P | Moody's | Fitch |
|-----------------|------|---------|-------|
| Netherlands | AAA | Aaa | AAA |
| Germany | AAA | Aaa | AAA |
| France | AA | Aa2 | AA |
| United Kingdom | AA | Aa2 | AA- |
| Russia | BBB- | Baa3 | BBB |
| United States | AA+ | Aaa | AAA |
| Japan | A+ | A1 | A |
| China | A+ | A1 | A+ |
| Australia | AAA | Aaa | AAA |

Review & preview

On the 29th of September, the British House of Commons has approved the United Kingdom Internal Market Bill proposed by Prime Minister Johnson. The controversial bill enabled the UK to change previously agreed terms with the European Union concerning the border between Ireland and Northern Ireland after the Brexit. According to Johnson the new bill will prevent a split between Northern Ireland and the rest of the UK. The EU has already said it will take legal action against the bill. If necessary, The EU can involve the European Court of Justice.

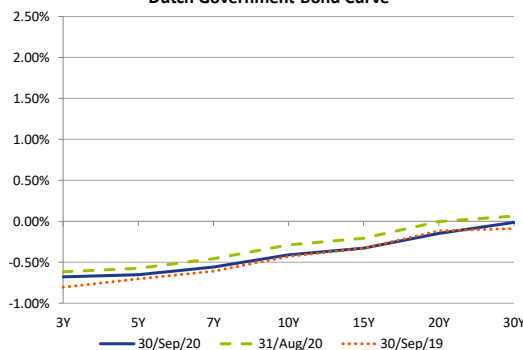
Market researcher Conference Board has stated that consumer confidence in the United States has significantly increased in September. The index increased from 86.3 in August to 101.8, the highest value since the start of the corona crisis. The increase is partly a result of the more positive outlook on the labour market: unemployment decreased from 8.4% in August to 7.9% in September. Another important factor is the decrease of COVID-19 infections. Research shows that consumer confidence is down in areas where the infection rate has increased. Experts warn that a new outbreak could reverse consumer confidence.

The German government wants to raise more additional funds in the final quarter of 2020 than previously expected. Germany will issue more than EUR 50.5 billion in government bonds in the next quarter. This is EUR 6 billion more than expected last year. The additional funding will primarily be used to combat the economic effects of the coronacrisis. The amount of funding is lower than in the third quarter of 2020, when EUR 146 billion of debt was issued. Germany will have an expected budget deficit this year of EUR 218.5 billion, and a deficit of EUR 96.2 billion in 2021. The debt-to-GDP ratio is expected to increase to more than 75%, against 60% before the coronacrisis,

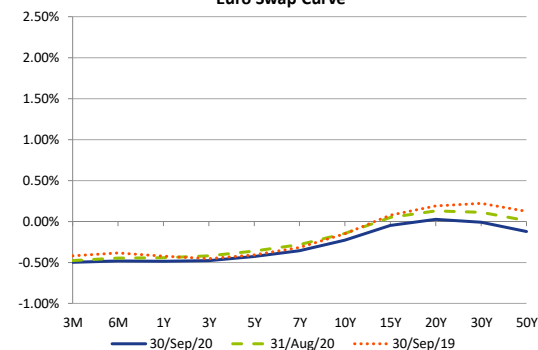
Agenda

- 8 October: Core inflation NL
- 13 October: Core inflation US
- 15 October: Unemployment rate NL
- 21 October: Core inflation UK
- 28 October: BoJ interest rate decision

Dutch Government Bond Curve



Euro Swap Curve



| Bank Ratings | S&P | Moody's | Fitch |
|--------------------|------|---------|-------|
| Rabobank | A+ | Aa3 | A+ |
| ING Bank | A+ | Aa3 | AA- |
| ABN AMRO | A | A1 | A |
| BNG Bank | AAA | Aaa | AAA |
| NWB Bank | AAA | Aaa | n.a. |
| Deutsche Bank | BBB+ | A3 | BBB |
| BNP Paribas | A+ | Aa3 | AA- |
| Barclays Bank | A | A1 | A+ |
| Credit Suisse Int. | A+ | A1 | A |

| Currencies | 30/Sep/20 | 31/Aug/20 | 30/Sep/19 |
|------------|-----------|-----------|-----------|
| EUR/USD | 1.172 | 1.194 | 1.090 |
| EUR/GBP | 0.907 | 0.893 | 0.887 |
| EUR/CHF | 1.079 | 1.079 | 1.088 |
| EUR/JPY | 123.655 | 126.405 | 117.795 |
| EUR/DKK | 7.445 | 7.443 | 7.466 |
| EUR/SEK | 10.498 | 10.319 | 10.725 |
| EUR/CAD | 1.561 | 1.557 | 1.443 |
| EUR/AUD | 1.636 | 1.618 | 1.615 |
| EUR/CNY | 7.960 | 8.175 | 7.791 |

Yields 10Y Government Bonds

