2024 Treasury: the increased participation of domestic and non-resident investors will absorb the greater funding needs

Despite the goal to reduce the government deficit to 3% of GDP in 2024, the Treasury's funding needs will remain high. In addition, the market will have to absorb all the debt that is currently in the hands of the ECB and which it will not reinvest. In this context, we provide some perspective on the volume of debt that the market will have to absorb during this year.

The Treasury's strategy following the end of the ECB's net purchases

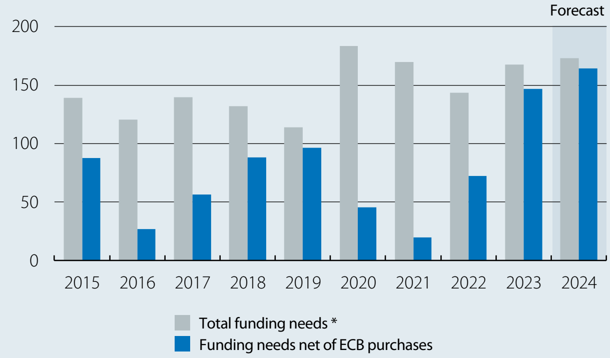
The Treasury's financing strategy for 2024, published in mid-January, includes projected net issues of 55 billion euros, which will be covered entirely by medium- and long-term instruments. This is a significant amount, but less than the 65 billion issued in 2023. The gross issues of medium- and long-term debt, which is the sum of the anticipated repayments, will amount to 173,118 million euros, slightly higher than the 167,500 million of 2023.

The change of scenario is significant because the ECB will continue – and in fact intensify – its withdrawal initiated in 2022. It should be recalled that under the APP (Asset Purchase Programme),[1] net purchases were extended until June 2022; from July 2022 to February 2023, 100% of the bonds that matured were reinvested; between March and June 2023, partial reinvestments were made, and since July last year the reinvestments have been reduced to 0, such that the portfolio is shrinking at the rate at which the assets mature. In the case of the PEPP (Pandemic Emergency Purchase Programme), net purchases were extended until March 2022; between April 2022 and June 2024, 100% of maturities will be reinvested; between July and December 2024, the reinvestments will be partial, and finally, from 2025 onwards, they will cease and the portfolio will shrink as the remaining assets mature.

Taking all this information into account, in 2023 the ECB made negative net purchases of Spanish sovereign debt amounting to –15 billion euros and reinvested maturities worth 36 billion. In 2024, we estimate that the ECB will make net purchases worth –38 billion and will reinvest medium- and long-term debt worth around 47 billion. As a result, the ECB's gross purchases in 2024 would be 12 billion less than in 2023 (0.8% of GDP).

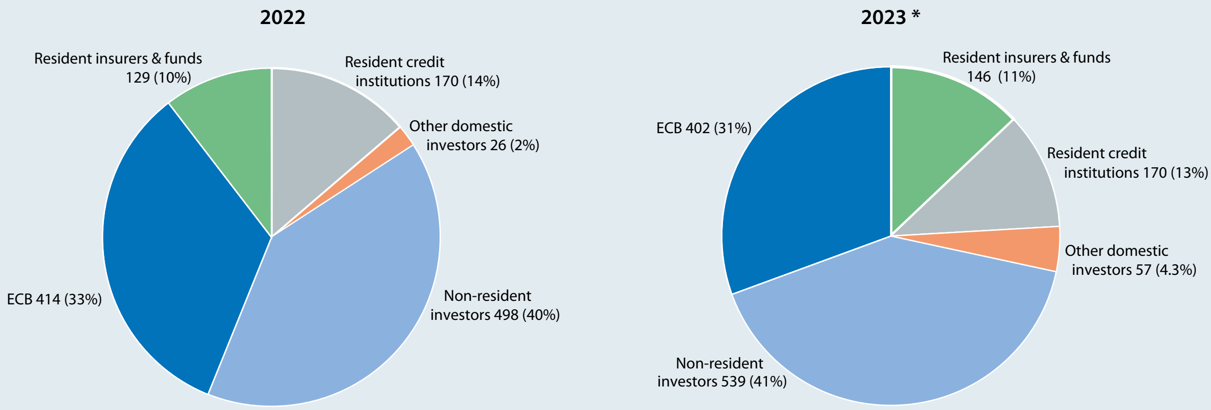
Despite the reduced role of the ECB, the context of higher interest rates compared to the period 2016-2022 should make these assets more attractive to investors, whether domestic or non-resident, and facilitate the absorption of Spain's funding needs, a trend which has already been observed in 2023. Thus, the holdings of Spanish debt show a good diversification of the investor base (see second and third charts). In 2023 (with data to October), foreign investors showed their confidence by increasing their holdings of Spanish debt (excluding Treasury bills) by

Spain: treasury funding needs
(EUR billions)



Note: ** The repayment figures do not include Treasury bills. For instance, 89,348 million euros in bills will be repaid in 2023 and the Treasury Strategy anticipates that 84,454 million will be repaid in 2024.*
Source: *CaixaBank Research, based on data from the General Secretariat of the Treasury.*

Spain: state debt holdings (bills and bonds)
(EUR billions) Structure (%)



Note: ** Data as of October 2023.*
Source: *CaixaBank Research, based on data from the General Secretariat of the Treasury.*

1. Since 2014, the ECB has acquired assets under its Asset Purchase Programme (APP), including government debt securities, corporate bonds, asset securitisation bonds and covered bonds.

65 billion euros compared to the end of 2022, well above the historical average for 2003-2021 (16.4 billion). In this way, of the total holdings of our debt (including Treasury bills, which account for just 5% of the debt portfolio), the portion held by foreign investors has risen to 41%, compared to 40% at the end of 2022, and their participation was particularly high in the syndicated issues of 2023.

On the other hand, international investors have reduced their holdings of Treasury bills in favour of domestic investors. Retail investors have led the domestic interest in Treasury bills, becoming their main holder, with an historical increase of 21 billion euros through to October 2023. As a result, retail investors accounted for 31.7% of the total holdings of bills at that date, amounting to 22,893 million euros, making them the biggest category of investors in this segment. Thus, domestic investors as a whole hold 28.4% of all debt (26.3% at the end of 2022).

Looking at the total stock of debt, we estimate that public debt held by the ECB will account for 30% of total debt in 2024 (32% of GDP), leaving the remaining 70% (75% of GDP) in the hands of other investors. Between 2012 and 2015, the portion of the total debt held by investors other than the ECB far exceeded this figure (peaking at 102% of GDP in 2014).

Other supporting factors

There are other factors beyond the greater role of private investors that help us to understand under what conditions the Treasury will have to meet these funding needs in 2024, such as more favourable financing costs despite the monetary tightening of the last year, which now looks set to be gradually unwound, and a long average life of the debt.

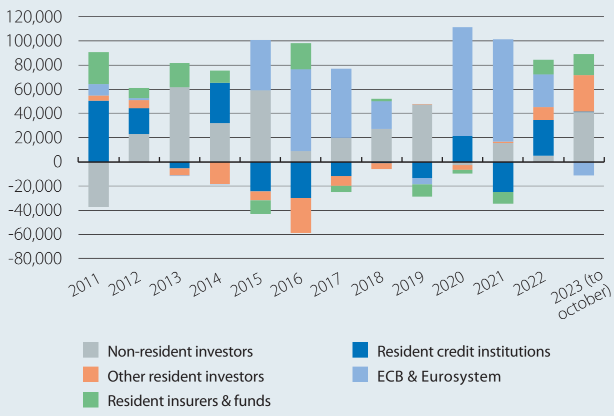
In particular, in 2023 the average financing cost of new emissions (including bills) rebounded to 3.44%, after standing at 1.35% in 2022 and in negative territory (–0.04%) in 2021. Despite this, the average cost of the stock of debt as a whole has increased only slightly, from 1.64% in 2021 to 1.73% in 2022 and to 2.1% in 2023. This is because, in order to anchor the low financing costs of recent years, the Treasury chose to issue debt in the longer sections of the maturity curve. This has allowed the average life of Spanish debt to be increased, now standing at 7.8 years.

In 2024, the average cost of the total stock of debt is expected to rise very slightly, due to the maturity of debt issued years ago at rates above the current ones and because of the long average duration. In this way, the interest payments on the total stock of general government debt, taking into account the markets' current expectations of a somewhat bigger decline in interest rates than had been anticipated a few months ago, could reach 2.5% of GDP in 2024. Although similar to the level of 2023, this is much lower than a decade ago – in 2014, for example, it reached 3.5%.

Looking ahead to the medium term, in 2026 the general government may have incurred interest costs of around 2.6% of GDP, which would amount to around 44 billion euros, compared to the 35 billion which we forecast for 2023. Thus, even if the monetary tightening is gradually unwound, the cost of debt will still be higher than it was during the years of ultra-low rates, such that there will be a gradual rise in the cost of debt. Therefore, given the high level of public debt, it will be essential to design a fiscal consolidation strategy that is gradual but sustained over time and which conforms to the new fiscal rules approved by the EU.

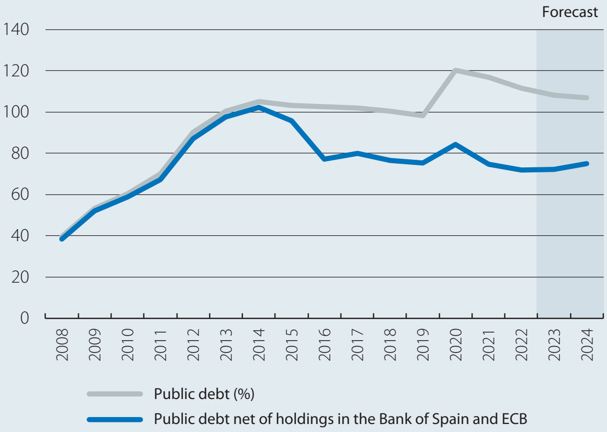
Javier Garcia-Arenas

Spain: annual change in state debt holdings (bills and bonds)
(EUR millions)



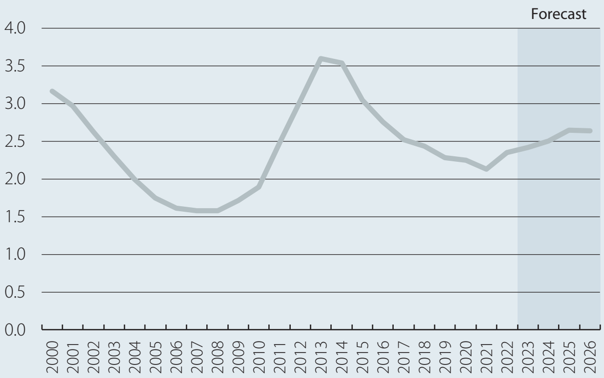
Source: *CaixaBank Research, based on data from the State Treasury.*

Spain: public debt
(% of GDP)



Source: *CaixaBank Research, based on data from the Bank of Spain and the ECB.*

Spain: interest payments on public debt
(% of GDP)



Note: *Since the average maturity is 8 years, the prediction is made using the implied 8-year market rate.*
Source: *CaixaBank Research.*