

#### Box 4

##### GOVERNMENT FINANCIAL ASSETS AND NET GOVERNMENT DEBT IN THE EURO AREA

In assessing sovereign debt sustainability, government holdings of financial assets, and not only gross government liabilities, should also be taken into account. An indicator of net government debt provides useful complementary information to gross government debt levels, in particular when an increase in government liabilities is accompanied by a simultaneous increase in government financial assets.<sup>1</sup>

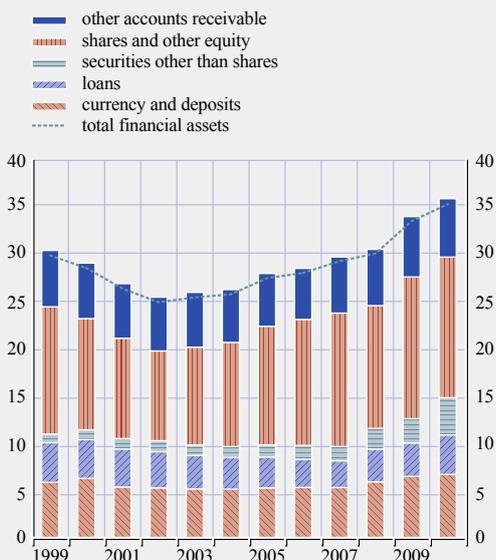
As shown in Chart A, the average amount of euro area governments' financial assets stood close to 35% of GDP in 2010. Out of this, 4.8% of GDP are estimated to be directly related to the financial crisis, mainly involving the net acquisition of financial assets such as currency and deposits (via lending by the government), as well as loans and equity, especially in the cases of the Netherlands and Ireland. Average euro area net government debt stood at 56.6% of GDP in 2010 – that is, the total value of government liabilities was more than twice the market value of government financial assets.

The ratio of financial assets to GDP differs from country to country (see Chart B). The resulting net government debt-to-GDP ratios vary accordingly. Some countries with high gross government liabilities also show high net government debt ratios, even above 100%

<sup>1</sup> In practice, net debt can be derived as the arithmetic difference between the stock of government liabilities and the stock of government financial assets in a given year, measured in market value following the European System of Accounts 1995. The stock of government liabilities includes the financial instruments that constitute the definition of the EDP debt (currency and deposits, loans and securities other than shares excluding financial derivatives), plus financial derivatives and other accounts payable. See R. Mink and M. Rodríguez-Vives, "The Measurement of Government Debt in the Economic and Monetary Union", Sixth Banca d'Italia Workshop on Public Finance, 2004. Japan represents a relevant example as the Japanese government held financial assets worth above 75% of GDP as at end-2009. Since government gross liabilities were around 185% of GDP, the resulting net government debt-to-GDP ratio in Japan was around 110% in 2009.

**Chart A Composition of euro area government financial assets**

(1999 – 2010; percentage of GDP)



Sources: Eurostat, national data and ECB calculations.

**Chart B Government financial assets and net government debt in euro area countries**

(2010; percentage of GDP)



Sources: Eurostat, national data and ECB calculations.  
Note: Euro area countries are sorted according to the ratio of their financial assets to GDP.

of GDP, as in the case of Italy. By contrast, some countries with a combination of low gross government debt and a high proportion of financial assets display net debt values of only one digit (Slovenia) or negative (Estonia, Luxembourg and Finland).

The feasibility of using government financial assets as a means of temporally smoothing governments' financing needs – and the associated role that such assets can play in reducing funding risks relevant for financial stability – depend on their liquidity and marketability. Short-term financial assets (such as currency and deposits, short-term debt securities, short-term loans and other accounts receivable), which account for around 40% of total financial assets in the euro area on average, are considered more liquid. By contrast, the market value of the financial assets acquired by governments, particularly in the context of the recent financial crisis, is uncertain, in particular if the pressure to sell such assets in depressed market conditions is high. All in all, while government financial assets provide some buffer for liquidity and refinancing needs, the liquidity and marketability of the underlying assets are of high relevance in assessing their role in attenuating sovereign risk.