RIKSGÄLDEN
SWEDISH NATIONAL DEBT OFFICE

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# Central Government Guarantees and Lending

## A Risk Analysis

Reg.no 2023/199

# The Debt Office's mandate

The Swedish state provides guarantees and loans for purposes determined by the Riksdag (Swedish Parliament) and the Government. A guarantee entails that the central government stands surety for the payment obligations of another party. This gives rise to a credit risk for the state. In the same way, a credit risk arises when the state lends money to parties such as a company or private individual.

The portfolio includes student loans, export guarantees, housing guarantees, and guarantees to the benefit of international financial institutions of which Sweden is a member. These commitments are collectively referred to in this report as the regular portfolio.

The Swedish National Debt Office has submitted the report *Central Government Guarantees and Lending – A Risk Analysis* to the Government every year since 2012. The report is prepared in collaboration with EKN (the Swedish Export Credit Agency), Boverket (the Swedish National Board of Housing, Building and Planning), Sida (the Swedish International Development Cooperation Agency), and CSN (the Swedish Board of Student Finance) as well as other relevant government agencies.[1]

**Increased awareness for better risk management**

This risk analysis report is a supplement to the financial reporting of the guarantee and lending operations provided in the central government's annual report. That report includes outstanding amounts, provisions for losses, and the fees charged by the central government as part of these activities. The purpose of the risk analysis is to provide further information about the credit and liquidity risks involved in the commitments. This report therefore focuses primarily on:

[1] A report containing a comprehensive risk analysis of central government guarantees and lending is to be presented on 15 March in accordance with the Ordinance containing instructions for the National Debt Office (2007:1447).

- The risk of major credit losses in the portfolio; i.e. losses that exceed expectations and normal deviations (credit risk analysis).
- Events or circumstances that could give rise to large credit losses.
- The central government's ability to handle large unforeseen outgoing payments and the risk of payments linked to guarantees and loan commitments leading to higher borrowing costs in the central government's liquidity management operations (liquidity risk analysis).

This in-depth analysis promotes transparency about the operations and also makes it easier for policymakers to determine whether further risk-mitigation measures are needed.

# Summary

The Debt Office considers the risk of large losses in the regular portfolio to be low. This is a slightly higher risk level than in the previous year. This portfolio amounts to SEK 781 billion and includes student loans, export credit guarantees, and guarantees to the benefit of international financial institutions. The main reason for the moderate risk level is an increased proportion of commitments with high or very high credit risk. The war in Ukraine and the worsened security landscape in Europe bring heightened uncertainty in terms of macroeconomic developments. The regular portfolio has limited exposure in Ukraine, Russia, and Belarus, but a significant proportion has defaulted or is expected to do so. For the deposit insurance scheme, which amounted to SEK 2,131 billion on 31 December 2021, the risk of large losses is expected to remain at the same moderate level as last year. The term large losses refers to SEK 20 billion over a five-year horizon.

## Moderate risk of large losses in the regular portfolio

The Debt Office considers the risk of large losses in the regular portfolio to be moderate. This is an increased risk level compared with the previous year. For the vast majority of the portfolio, creditworthiness remains good, although the proportion of commitments with very poor creditworthiness has risen sharply. The portfolio is considered to have limited sensitivity to normal economic downturns, which is largely due to the generally good creditworthiness. There are a number of significant concentrations in the portfolio, although the risk of large losses occurring among them is considered to be low. Other parts of the portfolio are well-diversified across numerous geographic areas and industries. A worsened state of affairs globally, together with relatively large amounts that are expected to default while at the same time the regular portfolio has grown by almost 30 per cent in the past three-year period, prompts an anticipated increase in risk to a moderate level.

The concentrations mainly regard individual large commitments, a geographical concentration to Sweden (39.2 per cent) of which a considerable part consists of student loans, and an industry concentration to telecom operators (11.1 per cent). Among the commitments with concentrations, creditworthiness is relatively high.

If large losses were to arise, they would most likely be caused by an unusually deep and/or unusually lengthy recession hitting one or more of the portfolio's concentrations particularly hard, at the same time as that recession causes heightened losses in other parts of the portfolio. The generally good creditworthiness of the portfolio contributes to it being relatively resilient to normal

economic downturns. The war in Ukraine has changed the European security landscape, and the future course of events and implications for the real economy and financial markets remain uncertain. The Debt Office is therefore closely monitoring developments and maintaining an ongoing dialogue with other agencies and participants in the financial markets. The regular portfolio has limited exposure in Ukraine, Russia, and Belarus, although a substantial proportion is expected to default. The moderate risk in the portfolio is largely attributable to the principles and regulatory frameworks governing the central government's guarantee and lending operations, and application thereof. The central government's risk-taking is moderated by the limits placed on guarantees and loans in terms of amount and period, the fact that the expected cost is reported and financed at the time of decision, and that risk-limiting conditions are applied.

**Table 1 Credit risks in the regular portfolio**

| Risk factor | Risk of large credit losses (previous year) |
|---|---|
| Risk from changes in the general economic environment | Moderate (Low) |
| Name concentration (individual large commitments) | Low (Low) |
| Close connections between guarantee holders or borrowers | Low (Low) |
| Industry concentration | Low (Low) |
| Geographic concentration | Low (Low) |

Note: The risk level is assessed according to a four-degree scale – low, moderate, elevated, and high.

## Moderate risk of large losses in the deposit insurance scheme

The Debt Office considers the risk of large losses in connection with the deposit insurance scheme to be moderate.

For the major banks and other institutions deemed systemically important, the deposit insurance scheme may need to be utilised to provide consumer protection in resolution. The Debt Office considers the risk of that occurring to be low. This is mainly because the probability of default and resolution interventions is considered low, as these institutions have high creditworthiness. Institutions would have to suffer significant losses for such interventions to be needed. Also, the contribution of the deposit insurance scheme in resolution is limited in terms of amount.

If a non-systemically important institution were to fail, the deposit insurance commitment would instead be fulfilled by the central government paying compensation directly to the depositors and then acquiring a claim on the institution. It would take the failure of one of the largest non-systemically important institutions, or the failure of several institutions, for large losses to occur. The Debt Office considers the risk of that occurring to be moderate.

In the event of an outgoing payment through the deposit insurance scheme, there is the possibility of recovering these funds. However, the recovery rate can vary widely between individual institutions.

**Table 2 Risk by type of fulfilment**

| Type of fulfilment | Risk of large losses (previous year) |
|---|---|
| Direct fulfilment | Moderate (Moderate) |
| Fulfilment in resolution | Low (Low) |

Note: The risk level is assessed according to a four-degree scale – low, moderate, elevated, and high.

# Flexible cash management gives low liquidity risk

The Debt Office considers that the liquidity risks in the guarantee and lending portfolio remain low. These liquidity risks arise because it is not known if or when potential amounts would have to be paid out. The Debt Office considers that such less-likely amounts could be borrowed on short notice. Although the borrowing cost would certainly be somewhat higher in some cases, it would only be in the short term and linked to individual payments.

# The sale of government bonds can entail additional costs

From a liquidity risk perspective, it is worth noting that assets in the fund must be realised upon a payout. A large volume of government bonds may then need to be sold within a short period of time, which could adversely affect the selling price. Although this has no direct effect on the central government's borrowing costs, it does entail an additional cost for the deposit insurance scheme.

The Swedish National Debt Office is the central government financial manager and the national resolution and deposit insurance authority.
The Debt Office thus play an important role in the Swedish economy as well as in the financial market

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