GUIDELINES FOR CENTRAL GOVERNMENT DEBT MANAGEMENT 2010

2010

Decision taken at the Cabinet meeting
November 12 2009

LONG-TERM PERSPECTIVES COST MINIMISATION FLEXIBILITY

REGERINGSKANSLIET

Contents

Summary

The Government's debt policy stance remains firm under the decision on the guidelines for 2010. The debt shares will be kept the same as well as the other target values. The system of governance, however, will be adjusted in accordance with the amended decisions made in 2009.

In the past year, the financial crisis and the economic downturn have affected the conditions for Swedish central government debt policy. The central government borrowing requirement has risen, interest rates have fallen and the Swedish krona has weakened. Against this background, two decisions on central government debt policy were amended:

- the maturity benchmark for the nominal krona debt was abolished (12 March 2009)
- the mandate for positions between the krona and other currencies was expanded from SEK 15 billion to SEK 50 billion (28 May 2009)

The changes in the governance system established in the 2010 guidelines are a direct result of these amended decisions.

The management of the maturity of the nominal krona debt will be separated from 2010 onwards so that loan instruments with a maturity of less than twelve years will be steered towards the maturity benchmark of 3.2 years. Borrowing instruments with a maturity longer than twelve years will be limited by a volume ceiling of SEK 60 billion for 2010. The maturity benchmark of 3.2 years is in line with the current policy stance for the nominal krona debt with maturities less than twelve years.

Control of position-taking will be changed. Positions between kronor and other currencies will be separated from the ordinary Value-at-Risk mandate. The size of the position mandate is unchanged at SEK 50 billion. The maturity of the foreign currency debt remains unchanged while the benchmark for the maturity of the inflation-linked debt will be adjusted for 2010 for technical reasons from 9.6 to 9.4 years.

The maturity of the three types of debt is to be steered towards:

- Foreign currency debt: interest rate refixing period of 0.125 years
- Inflation-linked debt: interest rate refixing period of 9.4 years
- Nominal krona debt:
  − instruments with a maturity of up to twelve years: interest rate refixing period of 3.2 years
  − instruments with a maturity over twelve years: maximum volume SEK 60 billion

The composition of the central government debt is to be steered towards:

- Foreign currency debt: 15 per cent
- Inflation-linked debt 25 per cent
- Nominal krona debt: 60 per cent

The central government debt is expected to increase from SEK 1 119 billion at the end of 2008 to around SEK 1 400 billion at the end of 2012 (unconsolidated gross debt). The debt ratio is expected to increase from 35 to 42 per cent of GDP. When the debt ratio was at its highest in 1994, it came to 78 per cent. Central government finances are strong in an international comparison.

The overall goal guiding central government debt management is that the debt is to be managed in such a way as to minimise the long-term cost while taking risk into account. The Government via the decision on the guidelines has overall responsibility for controlling the cost and risk in the central government debt. The Swedish National Debt Office is responsible for the strategic decisions within the framework of the guidelines and for their implementation in the operational management of the central government debt.

1 Central Government Debt Policy Objectives and Process

The process for the conduct and evaluation of central government debt policy has been in place since 1998. Since then, many decisions have been taken leading to the current process and central government debt. These decisions are based on many analyses and discussions. Over time, the sheer number of decisions has made it difficult to get an overview of the control system. With the aim of improving this overview, the structure of this year's decision on the guidelines has been changed. The result of these changes is an arrangement in the form tables with references. The overall goals of central government debt management and the purposes for which the National Debt Office may borrow on behalf of the central government are given below. The process for deciding the guidelines and evaluating debt management is also explained here. Section 2 contains the basis for the Government's decision on the guidelines. Section 3 contains the guidelines and the reasons for the Government's decisions when a guideline has been changed. Section 4 contains the principles to be followed in evaluating central government debt management. The Annex sets out the provisions for the Debt Office's management of funds and the requirements for consultation and cooperation and coordination.

To supplement the annual guidelines decisions, the Debt Office will also initiate and maintain a special document which will be a compendium of previous decisions, assessments and supporting analyses.

1.1 Goals of central government debt management

Regulations	Statutes
The central government debt is to be managed in such a way as to minimise the long-term cost while taking risk into account. Management is to take place within the framework of monetary policy requirements.	5 § Act on Central Government Borrowing and Debt Management (1988:1387)

1.2 Debt Office's remit and the purpose of borrowing

Regulations	Statutes
The Debt Office's remit is to raise and manage loans to the central government in accordance with the Act on Central Government Borrowing and Debt Management.	2 § Ordinance containing Instructions for the National Debt Office (2007:1447)
Following special authorisation, which is given for one fiscal year at a time, the Government or, after authorisation by the Government, the Debt Office, may raise loans for the central government to: • finance current deficits in the central government budget and other expenditure pursuant to decisions made by the Riksdag, • provide such credit and discharge such guarantees as decided by the Riksdag, • amortise, redeem and buy back central government loans, • in consultation with the Riksbank, satisfy the requirement for central government loans with different maturities, and • satisfy the Riksbank's requirements for foreign currency reserves.	1 § Act on Central Government Borrowing and Debt Management (1988:1387)

1.3 The guidelines process

Regulations	Statutes
The Debt Office is to submit proposed guidelines for central government debt management to the Government by 1 October each year.	3 § Ordinance containing Instructions for the National Debt Office (2007:1447)
The Government is to allow the Riksbank to comment on the Debt Office's proposed guidelines.	6 § Act on Central Government Borrowing and Debt Management (1988:1387)
The Government is to make a decision by 15 November each year on guidelines for the Debt Office's management of the central government debt.	6 § Act on Central Government Borrowing and Debt Management (1988:1387)
The Debt Office is to submit documentation to the Government for evaluation of central government debt management by 22 February each year.	3 § Ordinance containing Instructions for the National Debt Office (2007:1447)
The Government, beginning in 2008 and every second year thereafter, is to evaluate central government debt management .The Government Communication is to be presented to the Riksdag by 25 April.	7 § Act on Central Government Borrowing and Debt Management (1988:1387)
The Debt Office is to establish principles for the implementation of the guidelines for central government debt management adopted by the Government.	15 § Ordinance containing Instructions for the National Debt Office (2007:1447)

2 Basis for the Government's decision on the guidelines

The Government's basis: This year's guidelines cover 2010-2012. The decision on the guidelines for 2011 and 2012 should be considered preliminary. This section clarifies those concepts of cost and risk of overall importance in the design of the guidelines.

Decision levels and decision parameters are established as part of the control system for central government debt management. The starting point is the Act on Central Government Borrowing and Debt Management (1988:1387), which establishes the objectives and overall division of responsibility. The Government has overall responsibility for controlling the cost and risk of central government debt. The Government delegates the task of implementing the management of the debt within established frameworks to the Debt Office.

The basis for deciding the guidelines is the size of the debt, its expected development and the situation in the lending markets. The basis for decisions about the size of the position mandate is the exchange rate for the Swedish krona. The Government's view of cost and risk in central government debt management is also of overall importance in drawing up the guidelines.

The central government debt is measured in different ways, depending on the aim of the measure. The official measure, *the Swedish Central Government Debt (DDS)*, shows the central government's future commitments in terms of For control of the central government debt, the central government consolidated cash flows (CCF) has been used since 2007. This measure measures risk in the central government debt by including the central government's future commitments in terms of cash flows. It also includes coupon payments and inflation compensation in addition to the nominal final amounts. In calculating CCF, certain receivables from assets that fall within the framework of the Debt Office's debt management are also included.

2.1 The central government debt

Size and development

Central government debt is the result of central government budgets that historically have had larger deficits than surpluses. Exchange rate changes have also affected the size of the central government debt since a portion of this debt has been borrowed in foreign currencies.

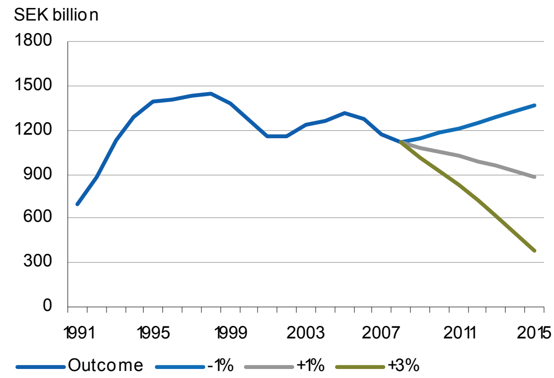
One basis for considering central government debt policy is the size of the debt and its expected development. In principle, robust public finances and declining central government debt increase the scope for risk-taking in exchange for lower expected costs.

In recent years, central government finances have been sound, leading to a decline in central government debt. From 1999–2008, central government debt declined by SEK 255 billion, for a total debt of SEK 1 119 billion at the end of 2008 (measured as unconsolidated central government debt). During the same period, the debt as a share of GDP declined from 73 to 35 per cent. The central government debt will increase over the next few years. One explanation for the increase in the debt is the decline in central government revenue and the increase in expenditure when the economy weakens. On-lending to the Riksbank, Iceland and Latvia totalling around SEK 110 billion in 2009 and 2010 also contributes to the debt increase. As on-lending is offset by equally large receivables, the CCF measure is not affected. In the 2010 Budget Bill, the central government debt at the end of 2012 is estimated at SEK 1 399 billion, or 42 per cent of GDP.

The surplus target and the central government debt

In central government debt policy, the size of the debt and its development are not subject to control. The development of the debt is instead indirectly controlled via the Riksdag and the Government's surplus target for general government net lending. One way of estimating the development of central government debt is to use this target as a basis. The Debt Office's proposal on the guidelines contains estimates of central government debt development, computed assuming that the surplus target of 1 per cent of GDP on average over a business cycle is met. The estimates computed indicate that if the surplus target is met for 2009–2015, central government debt will amount to SEK 900 billion in 2015. If net lending is two percentage points lower than the target, central government debt will be SEK 1 400 billion in 2015 (Figure 1).

Figure 1. Development of central government debt under different assumptions about the surplus target

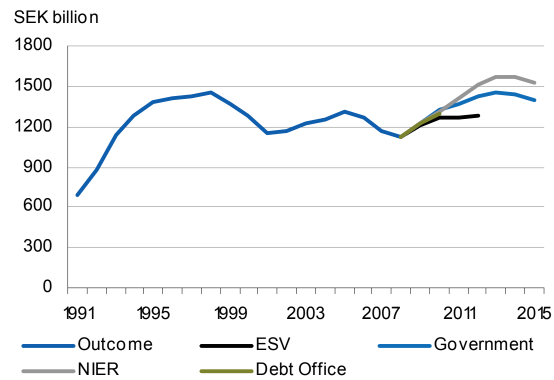


Source: The Debt Office

Forecasts and development of central government debt

Another way of estimating the development of central government debt is to use temporary forecasts as a basis. The Government, the National Institute of Economic Research, the Swedish National Financial Management Authority and the Debt Office make all the official forecasts of public finances and thus of the development of central government debt. The aims, time horizons and methods differ from one forecast to another. In all these forecasts, central government net debt is expected to increase in the next few years. At the end of 2012, the forecasts indicate that central government debt will come to SEK 1 300–1 500 billion and at the end of 2015 to around SEK 1 500 billion (Figure 2).

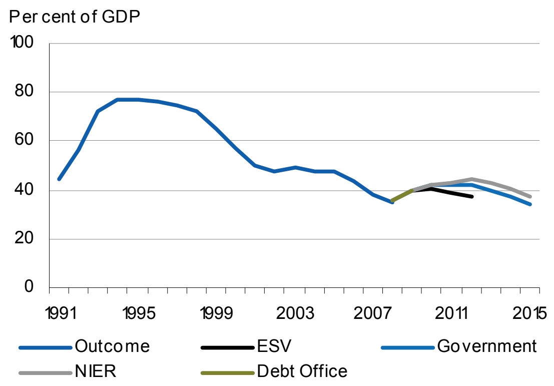
Figure 2. Trends in central government debt, outcome 1991–2008 and forecasts 2009–2015



Source: The Debt Office

In relation to GDP, the same forecasts indicate that the central government debt will decline after 2012, so that in 2015 it will come to just under 40 per cent of GDP (Figure 3).

Figure 3. The development of central government debt as a percentage of GDP outcome 1991–2008 and forecasts 2009–2015



Source: The Debt Office

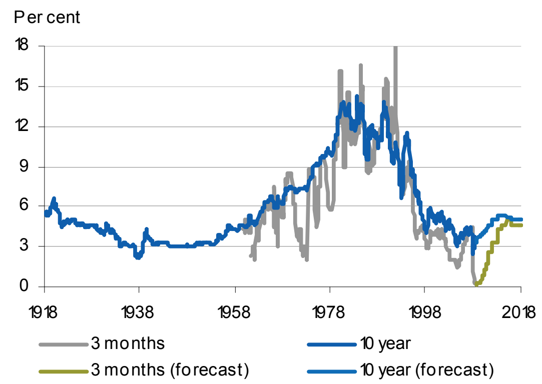
All the estimates point to a rise in central government debt during the period to which the guidelines decision refers (2010-2012). As a composite starting point, the decision on the guidelines is based on an unconsolidated central government debt of approximately SEK 1 300 billion at the end of 2010, rising to SEK 1 400 billion at the end of 2012. The increase using the CCF measure is largely the same, as the on-lending is not assumed to affect the borrowing requirement in this period. The unconsolidated debt as a percentage of GDP is expected to come to about 42 per cent, at the end of both 2010 and 2012. This debt ratio can be seen in relation to the 1994 debt ratio of 78 per cent. Central government finances are also strong in international comparisons.

2.2 Loan markets

Another basis for assessing central government debt policy is the situation in the loan markets. One important factor is the current and the expected slope of the yield curve. The yield curve, which in this context describes the interest rate on treasury bills and government bonds of different maturities, generally has a positive slope. This means that borrowing with shorter maturities involves lower expected costs than borrowing with longer maturities. There is, however, a higher risk inherent in borrowing with shorter maturities, since the debt must be refinanced more often (refinancing risk) and interest expenditure will vary more (interest rate refixing risk). A yield curve with a steeper slope increases the trade-off between cost and risk. The interest rate level, like its volatility, for different maturities may also be important in controlling the maturity of the central government debt.

In a historical perspective, current interest rate levels are remarkably low. Since the Riksbank lowered the repo rate in July, the three-month interest rate has consistently been less than one per cent, while the interest rate on ten-year government bonds has been just over three per cent in the same period. It is difficult to judge what a normal interest rate level is and how the interest rate level will develop. One approach is to look at historical interest rate levels. Comparisons further back in time should, however, be made with caution as both fixed-income markets and the way the economy functions change over time (Figure 4).

Figure 4. Ten-year and three-month government borrowing rate, Sweden



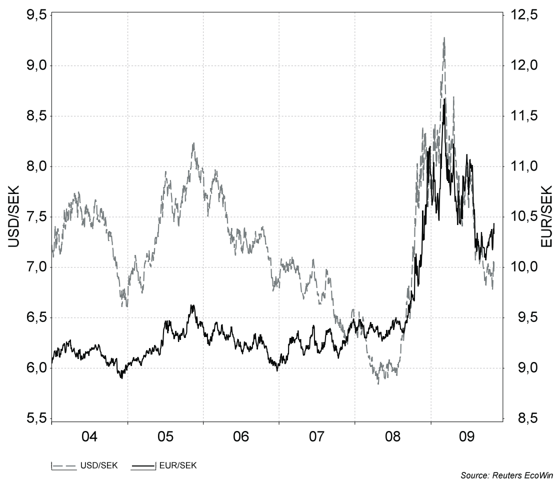
Source: The Debt Office

Considering that rises and falls in the interest rate level offset each other in the long run, the yield curve's level is of minor importance in the choice of long-term maturity. It could be said that the advantage of having a long-term debt when interest rates rise is reduced by a loss when interest rates fall again. Instead the slope of the yield curve and the ability of the borrower (the central government) to pay the rapidly rising interest costs is what is crucial.

2.3 The Swedish krona

The exchange rate for the krona is an important starting point for the Government in setting the size of the position mandate. Within the established mandate, it is possible for the Debt Office to take positions to reduce the cost of the debt, while taking risk into account. In autumn 2008, the Swedish krona weakened substantially as a result of the financial crisis, the economic downturn and the growing uncertainty about developments in the Baltic States (see Figure 5). As the krona remained weak during spring 2009, the Government, acting on a proposal from the Debt Office, decided to increase the scope for position-taking from SEK 15 billion to SEK 50 billion. In summer 2009, the krona strengthened as the financial markets stabilised and more positive signs of a recovery appeared. The krona is still weak, however, compared with its status prior to autumn 2008. From the end of May to mid-October, the Debt Office has gradually built up a position of about SEK 38 billion. As the financial crisis recedes and the economy improves in the next few years, the krona is expected to strengthen somewhat.

Figure 5. The krona in relation to the US dollar and the euro



2.4 Cost and risk

As previously stated, the overall goal of central government debt policy is that the debt is to be managed in such a way as to minimise the long-term costs while taking risk into account. The guidelines, in terms of definitions and measures constituting the basis for controlling cost and risk in central government debt management, are compiled below. Clarifications related to the new guidelines follow the table.

Guidelines for cost and risk

The Government's decision	Debt Office proposal	Comment
a. The central government debt composition and maturity chosen are the primary determinants of the balance between expected cost and risk.	Is consistent with the Government's decision.	New guideline, which clarifies the current arrangement
b. The overall cost measure is to be the average cut-off yield.	Is consistent with the Government's decision.	Corresponds to current guideline
c. The overall risk measure is to be the average cut-off yield risk.	Is consistent with the Government's decision.	Corresponds to current guideline

d. The share of each of the different types of debt in the central government debt is to be calculated by a measure that takes into account all cash flows in the central government debt, i.e. future coupon payments and expected compensation for inflation.	Is consistent with the Government's decision.	New guideline, which clarifies the current arrangement
e. The maturity is to be measured by an average interest rate refixing period where all cash flows including expected compensation for inflation are included. Cash flows are not to be discounted.	Is consistent with the Government's decision.	Corresponds to current guideline. Clarifies what the measure means.
f. Positions are not to be included in the calculations of debt shares and maturities.	Is consistent with the Government's decision.	New guideline, which clarifies the current arrangement
g. When taking positions, market values are to be used as measure of costs and risks in management.	Is consistent with the Government's decision.	Corresponds to current guideline

Clarifications – Costs and risk

2.4 a: In principle, strong central government finances and falling central government debt increase the scope for risk-taking in debt management in exchange for lower expected costs. The slope of the yield curve provides a trade-off between cost and risk. A shorter maturity reduces the expected costs. Borrowing in shorter maturities, however, involves a higher risk since the debt is refinanced more often (the refinancing risk) and there is more variation in interest rate expenditure (interest rate refixing risk). A debt which includes more types of debt (diversified portfolio) theoretically leads to lower risk. If the debt from a purely hypothetical point of view had consisted solely of nominal loans in Swedish kronor, interest rate costs would have been entirely dependent on the development of the Swedish nominal interest rate. The actual central government debt consists of two additional types of debt, inflation-linked loans in kronor and foreign currency loans which have interest rates that to some extent follow their own pattern. The foreign currency debt is also justified by the preparedness argument as access to the international lending market offers a broader investor base.

2.4 d: Since 2007, the measure used for the control and management of the central government debt has been the consolidated cash flow (the CCF measure). The measure reflects the aggregate risk exposure in the central government debt, as in addition to the nominal final amount, it includes the outstanding coupon payments and accrued inflation compensation. The CCF measure also contains a selection of assets, which are within the framework of the Debt Office's debt management.

2.4 e: For controlling the maturity, the maturity measure known as the average interest rate refixing period (IRP) has been used since 2006. The previous duration measure was replaced by the IRP since the duration measure led to undesirable, practical problems as the measure is affected by current market rates.

2.4 f: Since 28 August 2008, the foreign currency debt has been covered by the system for the control of shares. Positions under guideline III (Section 3.2) are taken outside the control of shares and maturities. The positions are placed in their own portfolio which separates them from the rest of the debt and makes it possible to monitor the results separately. See also Section 3.3.3.

3 Decision on the Guidelines for Central Government Debt Management 2010

3.1 Summary

The Government's decision on the guidelines for 2010 leaves the Government's debt policy unchanged. The control system will, however, be adjusted to the amended decisions taken in 2009, as follows:

– A new control system for the maturity of the nominal krona debt is being established. The control will be split up so that borrowing instruments with a maturity shorter than twelve years will be guided towards a maturity benchmark of 3.2 years, while borrowing instruments with a maturity longer than twelve years will be limited by a volume ceiling of SEK 60 billion in 2010.

– Control of the Debt Office's scope for position-taking will be changed. Positions in kronor vis-à-vis other currencies will be separated from the ordinary Value-at-Risk mandate. The size of the mandate for positions in kronor vis-à-vis other currencies is unchanged at SEK 50 billion.

The guidelines decided are in accordance with the Debt Office's proposal. The Riksbank in its comments on the Debt Office's proposal has stated that from a monetary policy perspective, it has no objections to the Debt Office's proposed guidelines.

3.2 Decision on the 2010 guidelines for central government debt management

I. The composition of central government debt – debt shares

The Government's decision	Debt Office Proposal	Comment
a. The share of foreign currency debt should be 15 per cent of central government debt.	Is consistent with the Government's decision	Corresponds to current guideline
b. The control interval around the benchmark should be ±2 percentage points.	Is consistent with the Government's decision	Corresponds to current guideline
c. If the foreign currency share is outside the control interval, the share of foreign currency debt should be restored to the benchmark. If the deviation is due to currency movements, the share of foreign currency debt is to be brought back within the interval.	Is consistent with the Government's decision	New guideline. Government's reason, see Section 3.3.4
d. The Debt Office is to set the benchmark for the distribution of the foreign currency debt among different currencies.	Is consistent with the Government's decision	Corresponds to current guideline

e. The share of inflation-linked krona debt should be 25 per cent of central government debt in the long run.	Is consistent with the Government's decision	Corresponds to current guideline
f. In addition to inflation-linked krona debt and foreign currency debt, central government debt is also to consist of nominal krona debt.	Is consistent with the Government's decision	Corresponds to current guideline

II. The maturity of central government debt

The Government's decision	**Debt Office proposal**	**Comment**
a. The maturity of the foreign currency debt is to be 0.125 years during 2010. The target for 2011 and 2012 is to be 0.125 years.	Is consistent with the Government's decision.	Corresponds to current guideline.
b. The maturity of the inflation-linked krona debt is to be 9.4 years at the end of 2010. The maturities at the end of 2011 and 2012 will preliminarily be 8.7 years and 9.0 years respectively.	Is consistent with the Government's decision.	Guideline changed.. Government's reason, see Section 3.3.2.
c. The maturity of the nominal krona debt for maturities of up to twelve years is to be 3.2 years in 2010. The target for 2011 and 2012 is to be 3.2 years.	Is consistent with the Government's decision after supplementary information on 23 October 2009; see Section 3.3.4.	Guideline changed,. Government's reason, see Section 3.3.2.
d. The ceiling for the outstanding volume of maturities exceeding twelve years is to be SEK 60 billion in 2010. The ceiling for 2011 and 2012 will be SEK 65 billion and SEK 70 billion respectively.	Is consistent with the Government's decision.	Guideline changed. Government's reason , see Section 3.3.2.
e. The Debt Office is to decide on a deviation interval for the benchmarks for the maturities.	Is consistent with the Government's decision.	Corresponds to current guideline.

III. Position-taking

The Government's decision	**Debt Office proposal**	**Comment**
a. The Debt Office may take positions to reduce the central government debt costs, while taking into account risk.	Is consistent with the Government's decision	Corresponds to current guideline
b. Position-taking refers to transactions which aim at reducing costs, but which are not justified by underlying loan or investment needs.	Is consistent with the Government's decision	New guideline to clarify the current arrangement. Government's reason, see Section 3.3.4.
c. Positions may be strategic (long term) or operational (current). The Debt Office is to decide on the distribution of the risk mandate.	Is consistent with the Government's decision	Corresponds to current guideline. However, the first sentence has been added for the purpose of clarification. Government's reason,

		see Section 3.3.4
d. Positions may not be taken in the Swedish fixed income market.	Is consistent with the Government's decision	Corresponds to current guideline
e. The maximum limit for position-taking is to be SEK 600 million, measured as daily Value-at-Risk with a 95 per cent probability. Positions are to be taken with derivative instruments. The limitation is to apply to all transactions with the exception of strategic positions between kronor and other currencies (see f and g below). f. Strategic positions in kronor relative to other currencies may not exceed SEK 50 billion. These positions need not be taken in derivatives and are exempted from the limitation in terms of Value-at-Risk. g. Kronor positions are to be built up gradually and announced in advance.	Is consistent with the Government's decision Is consistent with the Government's decision Is consistent with the Government's decision	Corresponds to current guideline Guideline changed. Government's reason, see Section 3.3.3. New guideline to clarify the current arrangement.
h. Operational positions in kronor relative to other currencies may in connection with exchanges between kronor and other currencies be taken to a limited extent. The Debt Office is to state the maximum permitted extent.	Is consistent with the Government's decision	New guideline. Government's reason, see Section 3.3.4.

IV. Market and debt maintenance

The Government's decision	Debt Office proposal	Comment
a. Through market and debt maintenance, the Debt Office is to contribute to the good performance of the government securities market with a view to achieving the long-term goal of keeping costs to a minimum while taking risk into account. b. The Debt Office shall decide on the principles for market and debt maintenance.	Is consistent with the Government's decision Is consistent with the Government's decision	Corresponds to current guideline Corresponds to current guideline

V. Loans to meet the need for central government lending

The Government's decision	Debt Office proposal	Comment
a. The possibility of raising loans to meet the need of central government lending may only be used if required on account of threats to the functioning of the financial market. b. The Debt Office is to be given the right to have outstanding loans in 2010 amounting to a maximum nominal value of SEK 200 billion for this purpose.	Is consistent with the Government's decision Is consistent with the Government's decision	New guideline to clarify the current arrangement. Government's reason, see Section 3.3.4. Corresponds to the current guideline for 2009

c. Placements of funds raised through loans to meet the need of central government lending should be guided by the principles stated in the Government Support to Credit Institutions Act (2008:814).	Is consistent with the Government's decision	New guideline, which clarifies the current arrangement. Government's reason, see Section 3.3.4.

VI. Borrowing in the retail market

The Government's decision	Debt Office proposal	Comment
a. The Debt Office is to help reduce the cost of the central government debt by retail market borrowing.	Is consistent with the Government's decision	Corresponds to current guideline

3.3 Reasons for the Government's decision

3.3.1 Balancing cost and risk

In previous guidelines, the Government has established that the trade-off between cost and risk (the slope of the yield curve) is the primary factor and the interest rate level is of secondary importance in decisions on the maturity of the central government debt.

At present, the difference between the ten-year rate and the three-year rate is more than double the historical average of around one percentage point. The explanation is that the short rates are extremely low. The trade-off between cost and risk is thus more advantageous than usual, thus in principle justifying a reduction in the maturity. The expected cost of the central government debt could thus be reduced in exchange for somewhat higher risk in its management. Conversely, however, it may be argued that the State should not increase risk-taking in a situation in which the central government debt is expected to rise in the next few years. Moreover, it should be noted that interest rates on long maturities are historically low and, under certain conditions, may very well be cost competitive compared with short borrowing.

The opposing arguments given above do not provide any clear-cut grounds for changing the maturity. Therefore, the stance on the maturity of the central government debt remains unchanged.

The amended decision of March 2009, which made it possible for the Debt Office to issue a new long bond, was made primarily for cost reasons, but it also reduced the risk in the central government debt, as the average maturity in the nominal krona debt was lengthened. The aggregate risk-taking in debt management was reduced when the maturity rose to over 5 years. The amended decision of May 2009, when the Debt Office was given greater possibilities to take strategic positions in kronor relative to other currencies, increased the risk in the central government debt. The decision was taken to increase the potential for reducing borrowing costs implied by the krona exchange rate at that time.

Given the above arguments and the adjustment of the control of the benchmark for the maturity for the nominal krona debt established for 2010, the Government deems risk-taking in the management of the central government debt to be well balanced. It has thus been decided that the stance on both maturities and position mandates will remain unchanged. Nor has the Government found any reason to change the benchmarks for the debt shares steering the composition of the central government debt.

3.3.2 Maturity of the central government debt

Since the 2009 decision on the guidelines, the Government has steered the maturity in the central government debt by setting separate target values for each of the three types of debt. Under the previous process, the Government decided the benchmark for the maturity for the debt as a whole. The Debt Office was then instructed to decide how the maturity would be allocated between the three types of debt. Up to 13 March 2009, the benchmark for the nominal krona debt was 3.5 years. At that time, the Government decided to temporarily suspend the maturity benchmark for the nominal debt to make it possible for the Debt Office to issue a government bond with a long maturity. The aim was to be able to make full use of advantageous costs in an environment with low long rates. A further motive was to reduce the refinancing risk and spread the borrowing over more maturities at a time when the outlook for public finances was deteriorating and uncertainty was growing. On 23 March 2009, a 30-year nominal government bond was issued. The volume came to SEK 38 billion and the interest rate was 3.75 per cent. As a result of this bond issue, the maturity of the nominal krona debt rose from 3.4 years to 5.2 years. This illustrates that even relatively small issue volumes with long maturities have a major impact on the average maturity. Another consequence was that the maturity profile became very uneven.

The change in circumstances requires a new control of the benchmark for maturity in the nominal krona debt. Control of the maturity of the nominal krona debt will be separated into *borrowing instruments with maturities shorter than twelve years* and *borrowing instruments with maturities longer than twelve years*.

For *borrowing instruments with maturities shorter than twelve years,* the maturity of the nominal krona debt in 2010 should be 3.2 years. The target for 2011 and 2012 should also be 3.2 years (see clarification in Section 3.3.4 II. c). The maturity for this part of the debt implies an unchanged stance in borrowing. The reason for the Government choosing to refrain from shortening maturities, despite the current steep yield curve, is that interest rates with long maturities are also low in a historical context and the state of public finances does not support greater risk-taking.

For loan instruments with a maturity exceeding twelve years, a ceiling is being established for the outstanding volume. This ceiling should be SEK 60 billion in 2010. The ceiling for 2011 and 2012 should be SEK 65 billion and SEK 70 billion respectively. The level, SEK 60 billion, gives the Debt Office room on a few occasions to issue more long bonds, in addition to the SEK 38 billion outstanding in the 30-year bond. In this way, scope is created to be able on a few occasions to take advantage of periods of strong demand for long bonds.

The benchmark for the maturity of the inflation-linked krona debt at the end of 2010 should be 9.4 years. The maturities at the end of 2011 and 2012 should preliminarily be 8.7 years and 9.0 years respectively. The decision entails a slightly shorter maturity compared with the preliminary benchmarks set by the Government in the decision on the guidelines for 2009. This adjustment is being made for technical reasons. The maturity can in practice only be controlled by new issues, exchanges and buybacks. Since the market for inflation derivatives is relatively undeveloped, it is the Debt Office's opinion that it is too expensive at present to use derivatives to control the maturity of the inflation-linked debt. Compared to the size of the inflation-linked debt, the issue volumes are small and thus they have little impact on the maturity. Furthermore, the inflation-linked bond market is not as deep and liquid as the market for nominal bonds. Thus for reasons of cost, issues in maturities that would steer the debt towards a particular benchmark are not always justified.

3.3.3 Position-taking

The Debt Office has for some time been able to take positions to reduce the cost of central government debt, while taking risk into account. Position-taking refers to transactions which aim at reducing costs, but which are not justified by underlying loan or investment needs. Up to 28 May 2009, it was possible for the Debt Office to take strategic positions in kronor relative to other currencies for a maximum of SEK 15 billion. On 28 May 2009 the Government raised the position mandate to SEK 50 billion. This was done to make it possible for the Debt Office to further exploit the potential for lower borrowing costs provided by the krona exchange rate at that time. It was the opinion of the Government and the Debt Office that the krona will strengthen when the financial turmoil recedes.

As a result of the decision on the guidelines for 2010, the two position mandates will be combined into a single decision and the new mandate will not be covered by the VaR mandate, as was the case with the first mandate of SEK 15 billion. The requirement for transparency means that positions between kronor and other currencies should be settled gradually and over a longer period than is compatible with VaR as a control measure. The decision on the guidelines for 2010 also means that no part of the position mandate needs to be taken with derivatives since direct borrowing in foreign currency can also be an effective way of creating an exposure between kronor and foreign currency. Direct borrowing in foreign currency may also reduce the strains in the Swedish government securities market.

3.3.4 Clarifications for other guidelines

Clarifications are given below for those cases in which there has been an addition or a change made in a guideline (Section 3.2).

I. c: Since 28 August 2008, the system for the control of percentages has applied to the foreign currency debt. The aim of the control interval around the benchmark is primarily to avoid costs resulting from control measures that are only caused by temporary exchange rate movements.

II. c: On 23 October 2009 (in connection with the publication of the Debt Office's report Central Government Borrowing: Forecast and Analysis 2009:3), the Debt Office called the Government's attention to their finding that the benchmark for the interest rate refixing period for the nominal krona debt with maturities up to twelve years should be 3.2 years instead of the 3.0 years stated in the proposal for the guidelines – given the intentions behind the proposal. An updated analysis done after the guidelines proposal had been submitted showed that 3.0 years would be too short to match the unchanged direction of the borrowing. To avoid adjustments on account of the long bond, the Debt Office has explained that the benchmark for the interest rate refixing period for the nominal krona debt with maturities up to twelve years should be 3.2 years.

III. b and c: The aim of giving the Debt Office scope for position-taking is to further reduce the cost of the central government debt. Within the framework of the guideline the Board of the Debt Office decides on strategic long-term positions and the specification of internal guidelines for the day-to-day operational management.

III. h: Since 2003 it has been possible for the Debt Office to exchange foreign currency directly in the market. The exchange of currency flows is part of the Debt Office's day-to-day liquidity management. The exchanges are to be evenly distributed over time in order to minimise the risk of an unfavourable exchange rate at the time of payment. The Board of the Debt Office establishes a relatively even foreign exchange distribution over the year. The exchange path forms the basis for comparison of what is neutral from the standpoint of results. In order not to create unnecessary transaction costs, a deviation mandate is being established within which the transactions are regarded as results neutral.

V. a: The possibility of borrowing in order to provide for the need for central government loans to the financial sector was introduced in autumn 2008 with the aim of promoting financial stability. In this connection, the Act on Central Government Borrowing and Debt Management (1988:1387) was amended.

V. c: The Government Support to Credit Institutions Act (2008:814) makes clear that in accordance with the Act, support should be granted under normal market conditions to prevent any distortion of competition. The long-term cost to the State should be as low as possible. The support should be designed so that state financial aid can be recovered to the extent possible.

4 Evaluation

A preliminary evaluation of the guidelines for 2010 will be presented in the 2012 Budget Bill. Since the central government debt policy objective is to be long term, the result will also be evaluated over rolling five-year periods. . The evaluation for 2007–2011 will be submitted to the Riksdag no later than 25 April 2012. The Debt Office is to submit the documentation on which the evaluation is to be based to the Government no later than 22 February every year.

The Government's decision	Debt Office proposal	Comment
a. Evaluation of board decisions are to be made in qualitative terms in the light of the knowledge available at the time of the decision. Where possible, the evaluation is also to contain quantitative measures.	Is consistent with the Government's decision	Corresponds to current guideline
b. Board decisions are to be evaluated in qualitative terms in light of the information available at the time the decision was made. Where possible, the evaluation is also to include quantitative measures.	Is consistent with the Government's decision	Corresponds to current guideline
c. Evaluation of the operational management should, inter alia, cover borrowing and management of the different types of debt and market and debt maintenance measures as well as management of currency exchanges.	Is consistent with the Government's decision	Corresponds to current guideline
d. The realised cost difference between inflation-linked and nominal borrowing should be reported for inflation-linked borrowing.	Is consistent with the Government's decision	Corresponds to current guideline
e. The cost saving compared with alternative borrowing should be reported for retail market borrowing.	Is consistent with the Government's decision	Corresponds to current guideline
f. Strategic and operational positions within the given risk mandate should be currently taken up, as income and evaluation should be made in terms of the market values.	Is consistent with the Government's decision	Corresponds to current guideline

Annex

In addition to the guidelines in previous sections, the following provisions apply to the Debt Office's management of funds. Provisions, etc. for coordination and cooperation can also be found in the following text.

Management of funds, etc.

Regulations	**Statutes**
a. The Debt Office is to deposit its funds, to the extent that they are not needed for disbursements, in an account at the Riksbank, a bank or a credit market company, or in government securities or other debt instruments with a low credit risk. Deposits may be made abroad and in foreign currency.	5 § Ordinance containing Instructions for the National Debt Office (2007:1447).
b. The Debt Office is to cover the deficits that occur in the Government's central account.	7 § Ordinance containing Instructions for the National Debt Office (2007:1447)
c. Management of exchanges between Swedish and foreign currency (currency exchanges) is to be predictable and transparent.	6 § Ordinance containing Instructions for the National Debt Office (2007:1447)

Consultation and collaboration

Regulations	**Statutes**
a. The Debt Office is to consult the Riksbank on matters concerning the components of borrowing that may be assumed to be of great importance for monetary policy.	12 § Ordinance containing Instructions for the National Debt Office (2007:1447)
b. The Debt Office is to consult the National Institute of Economic Research and the National Financial Management Authority on matters concerning its forecasts of the central government borrowing requirement.	11 § Ordinance containing Instructions for the National Debt Office (2007:1447)
c. The Debt Office should obtain the Riksbank's views on how the funds borrowed to meet the need for central government lending are to be invested in accordance with the Act on Central Government Borrowing and Debt Management (1998:1387).	Corresponds to current guideline found in the guidelines decision for 2009