RIKSGÄLDS KONTORET
THE SWEDISH NATIONAL DEBT OFFICE

The Swedish National Debt Office Annual Report 2003

www.rgk.se

Mandate and goal

The Swedish National Debt Office is the central government's financial manager. We have a mandate from the Government and the Riksdag (Swedish Parliament) to administer central government borrowing, manage the government debt, serve as the central government's "internal bank" and administer the government payment system via our Cash Management Department, as well as issue state guarantees.

The task of the Debt Office is to ensure that the central government's financial management is run efficiently. The goal of our government debt management is to minimise the long-term costs of the debt, while taking into account risks. Given the magnitude of the debt and of state payments and guarantee commitments, our mandate is important to Swedish central government finances, both in the short term and the long term.

For further information, see www.rgk.se
The complete formal Swedish-language report on the operations of the Debt Office can be found under "Om Riksgäldskontoret". To request a copy, you can also telephone the Debt Office, +46 8 613 45 00 or (from inside Sweden only) Customer Service, telephone 020-780 780.
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2003 in brief

- The central government budget showed a deficit of SEK 46 billion in 2003. This was the first time since 1997 that the Swedish state has reported a deficit.
- The central government debt rose by SEK 25 billion to SEK 1,229 billion.
- The Debt Office amortised the equivalent of SEK 25 billion of the foreign currency debt. This debt shrank to the equivalent of SEK 330 billion, or 27 per cent of total central government debt.
- The Swedish state paid SEK 42 billion in interest on its debt.
- During 2003, the Debt Office phased out its increase in dollar-denominated debt, achieving gains totalling SEK 4.5 billion.
- Active management of foreign currency debt yielded a gain of SEK 937 million during 2003.
- The Swedish state saved SEK 260 million by borrowing directly from private individuals and small businesses. Lottery bond sales totalled SEK 10 billion and accounted for most of this saving.
- The Cash Management Department continued its efforts to streamline deposits from and lending to government agencies, as well as the state payment system. This included signing new framework agreements for state payments, which will yield large savings for the Swedish state as a whole.
- During 2003 the Debt Office sharply reduced its guarantee provisions for the state-owned residential financing company Venantius, since the financial position of the company has greatly improved.

Efficient financial management

“Personally, I am proud that we at the Debt Office have created and developed such an active approach to central government debt management.”

The Swedish National Debt Office manages a central government debt that totalled more than SEK 1,200 billion at the end of 2003. The interest on this borrowing is more than SEK 40 billion per year. And we have issued state guarantees of more than SEK 160 billion. Even for those of us who work daily in these areas, it may sometimes be difficult to fully fathom the significance of such large numbers.

These figures show that the task assigned to us by the Riksdag and the Government is important. The decisions we make and the proposals we submit to the Government on the management of these large sums play a major role in central government finances, both in the short term and the long term. Carefully crafted decisions may lead to large savings. On the other hand, unwise decisions may have serious adverse consequences for the central government, and thus for the people of Sweden.

In this Annual Report for 2003, we tell about our operations and how we are working to fulfil our overall mandate: efficient financial management for the Swedish state. We also try to describe the results of what we do. Not everything can be measured. In such cases, we try to explain the basis for our decisions, so that our analysis and arguments can be examined. The management of an important mandate must also be evaluated.

Our mandate is perhaps most clearly formulated when it comes to government debt management. The goal is long-term cost minimisation, while taking into account risk. The most important decisions, which are made by the Government based on proposals by the Debt Office, concern the structure and maturity of the government debt. The Riksdag carries out an annual follow-up and evaluation of these decisions and of the Debt Office’s management.

Aside from submitting thoughtfully prepared proposals to the Government, our task is to continuously manage the debt in such a way that costs will be as low as possible, taking into account risk. For example, we chose to decrease amortisations of the foreign currency debt during a period when the Swedish krona was extremely weak and it was thus expensive to repay foreign currency loans. Since then, the krona has strengthened considerably and we

Some key figures, Swedish National Debt Office, 1999-2003, SEK billion

	1999	2000	2001	2002	2003
Central government debt, December 31	1,423	1,344	1,211	1,204	1,229
The debt as a percentage of GDP	68	61	53	51	50
Nominal SEK debt as a percentage of total debt	62	61	56	56	59
Inflation-linked debt as a percentage of total debt	10	10	10	13	14
Foreign currency debt as a percentage of total debt	29	29	34	31	27
Interest paid on the central government debt	90	90	81	67	42
Central government borrowing requirement (net)	–82	–102	–39	–1	46
Deposits at the Debt Office	125.0	108.1	116.3	74.2	78.4
Lending by the Debt Office	144.8	157.5	189.6	195.6	212.2
Loans outstanding with credit risk	4	4	22	10	9
Guarantee commitments outstanding	205	202	239	158	164
Provisions for future guarantee losses	0.4	0.4	1.5	5.3	3.4
Guarantee reserves	0.4	0.5	1.5	1.7	2.0

have reverted to amortising this debt at a normal pace. We also decided to increase the share of debt in US dollars and instead reduce euro-denominated debt when we believed that the dollar was heavily overvalued. During 2003, when we had let our dollar-denominated debt revert to its normal share of total foreign currency debt, we were able to report a saving of about SEK 4.5 billion.

These decisions are expressions of our approach to the mandate. We actively monitor financial markets and seek to evaluate whether the prevailing exchange rates and interest rates are at reasonable long-term levels. If we are fairly convinced that this is not the case, we will take advantage of the available opportunity to achieve savings, without taking major risks.

We are not always right, and these assessments are difficult. The easiest thing would be not to make any active decisions, since decisions that are not made are difficult to criticise afterward. But we believe that financial markets sometimes – too often – are distorted by herd behaviour. Actually more market players should assume responsibility for carrying out their own analysis and not follow the herd. If this were the case, the world's financial markets and the global economy would be considerably more stable.

Personally, I am proud that we at the Debt Office have created and developed such an active approach to central government debt management. It is an expression of solid talent in economic and financial analysis combined with what I would like to describe as a good civil service spirit. No bonuses linked to management results have ever been considered at the Debt Office. Bonuses risk distorting the focus and narrowing our attention to things that pay a bonus. Our mandate is larger than this. This is also something I am proud of.

Stockholm, March 2004

Thomas Franzén

Director General

The central government debt and the borrowing requirement

The central government debt rose by SEK 25 billion to SEK 1,229 billion. Measured in relation to GDP, it fell slightly and totalled about 50 per cent. The central government budget showed a deficit of SEK 46 billion, which the Debt Office had to borrow. This was the first time since 1997 that Swedish state finances showed a deficit. The deficit was equivalent to 2 per cent of GDP.

The central government debt and its funding

At the close of 2003, the central government debt amounted to SEK 1,228.8 billion. The Debt Office reports unconsolidated central government debt, i.e. also including holdings of Treasury securities by government agencies. The debt was equivalent to about 50 per cent of Gross Domestic Product (GDP). Altogether, the debt rose by SEK 24.6 billion or 2 per cent during 2003. Measured as a share of GDP, the debt fell by 0.9 percentage points.

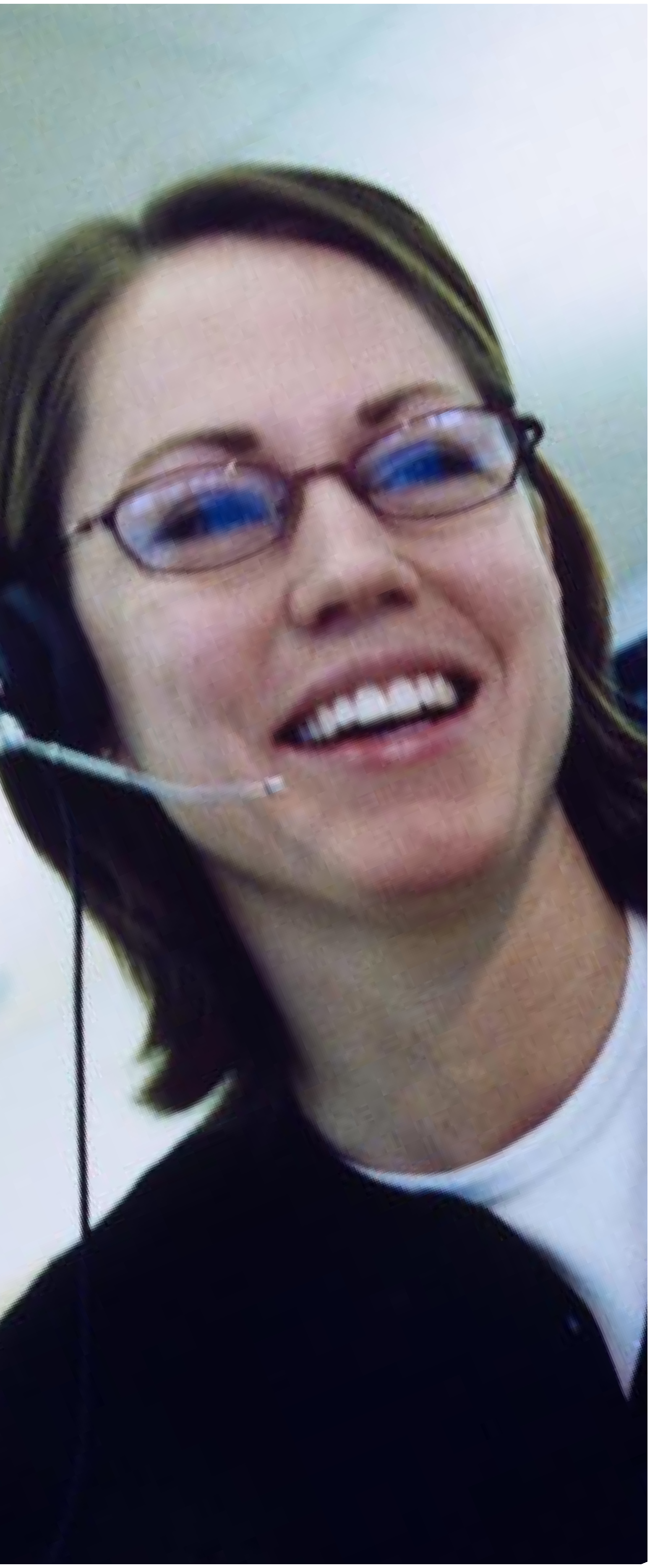
Interest payments on the central government debt totalled SEK 42 billion, or SEK 25 billion lower than in 2002. This was mainly due to smaller interest payments in Swedish kronor. Since the Debt Office will presumably be issuing loans with small premiums in the future, interest payments during the next few years will be higher than in 2003, even if interest rates remain at the current level.

Structure of central government debt, 1999–2003, SEK billion

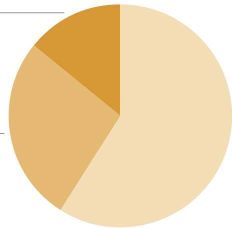
Instrument	1999	2000	2001	2002	2003	Change, 2002–2003
Nominal SEK loans						
Treasury bonds	567.2	467.4	357.0	358.3	398.4	40.1
Treasury bills	249.7	283.6	258.7	249.4	269.1	19.7
Overnight loans	0.0	0.0	12.5	4.9	0.0	–4.9
Lottery bonds	54.4	50.2	44.1	40.9	38.7	–2.2
National Debt Accounts	4.3	2.4	2.3	1.5	1.5	0.0
National Debt Savings	6.2	7.3	11.4	15.5	17.8	2.3
Total nominal SEK borrowing	**881.8**	**810.9**	**686.1**	**670.6**	**725.5**	**55.0**
Inflation-linked SEK borrowing						
Treasury bonds	134.1	136.7	115.8	157.2	171.8	14.6
National Debt Savings	1.0	1.1	1.2	1.2	1.1	–0.1
Total inflation-linked SEK borrowing	**135.2**	**137.8**	**117.1**	**158.3**	**172.9**	**14.6**
Foreign currency borrowing	**406.1**	**394.9**	**407.4**	**375.3**	**330.4**	**–44.9**
Central government debt	**1,423.0**	**1,343.5**	**1,210.6**	**1,204.2**	**1,228.8**	**24.6**

Interest on the debt and other expenditures, 1999–2003, SEK billion

Expenditures (+) and income (–)	1999	2000	2001	2002	2003
Interest on SEK borrowing	68.49	61.16	45.40	45.40	38.22
Interest on foreign currency borrowing	22.04	21.80	24.07	17.47	16.15
Interest on deposits from and lending to government agencies and other income	–2.40	–1.54	–3.27	0.37	–6.83
Total interest	**88.13**	**81.42**	**66.20**	**63.24**	**47.54**
Issue premiums/discounts	–2.40	0.78	–4.64	–7.73	–14.45
Currency exchange losses/gains (realised)	–6.25	–6.20	12.32	6.65	4.37
Capital losses/gains (realised)	10.16	15.03	5.17	4.59	3.81
Other items	0.18	–0.83	2.02	0.43	0.75
Total premiums/discounts, realised losses/gains etc	**1.69**	**8.77**	**14.87**	**3.94**	**–5.52**
Total net expenditures on appropriation item "Interest on government debt" (92:1)	**89.82**	**90.19**	**81.07**	**67.18**	**42.02**



Debt structure, December 2003



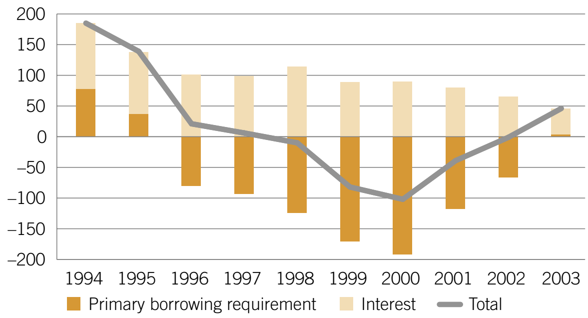
The central government borrowing requirement

The central government borrowing requirement – the net amount of all payments to and from the Swedish state – amounted to SEK 46 billion in 2003. This is synonymous with a budget deficit of SEK 46 billion. The last time the state budget showed a deficit was in 1997. The central government debt rose by SEK 25 billion and amounted to SEK 1,229 billion at the end of 2003. The difference between the borrowing requirement and the increase in debt was mainly due to a decline in foreign currency debt by about SEK 18 billion, since the value of the krona against other currencies climbed during the year.

The primary borrowing requirement (all payments except interest) deteriorated by SEK 70 billion compared to 2002. The main cause of the deterioration was that expenditures rose sharply. Among expenditures, the main increase from 2002 to 2003 was in pensions.

Net tax revenues rose by a total of SEK 5 billion between 2002 and 2003, mainly due to the growth in nominal terms of such tax bases as earned income and consumption. However, taxes revenues not subject to preliminary charges, such as capital gains tax and final settlement on corporate taxes, fell by a total of SEK 15 billion. One important cause is that capital gains have decreased since the stock price bubble burst in 2000, when capital gains taxes generated SEK 25 billion more than in 2003. In addition, transfers from the Riksbank, Sweden's central bank, were SEK 20 billion less than in 2002.

Central government borrowing requirement, 1994-2003 (SEK billion)



Borrowing and debt management

During 2003, amortisations on foreign currency debt were equivalent to SEK 25 billion. Inflation-linked borrowing rose from 13 to 14 percent of total central government debt.

The Government approved the following overall guidelines for 2003.

- The foreign currency debt would be amortised by SEK 25 ± 15 billion. The foreign currency debt was amortised in the amount of SEK 25 billion.
- Inflation-linked loans as a percentage of central government debt would increase in the long term. During 2003, a level of about 14 per cent was achieved.
- Average duration for nominal kronor-denominated and foreign currency debt would be 2.7 ± 0.3 years. The Debt Office chose not to deviate from the benchmark, with the result that during 2003, duration was around 2.7 years.
- Borrowing would be structured in such a way that no more than 25 per cent of total debt would fall due in the next 12 months. The share of borrowing that fell due averaged 27 per cent and we thus deviated somewhat from the benchmark.

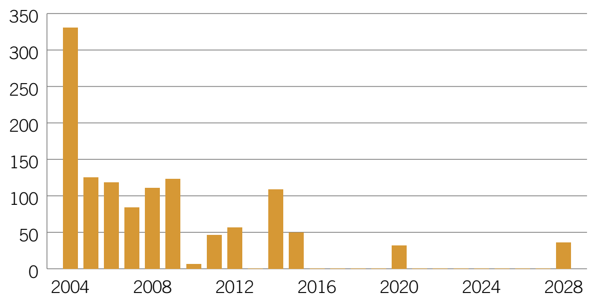
The Debt Office's actions

The Debt Office chose not to deviate from the duration benchmark. The Debt Office's analysis indicates that around this value, a reasonable trade-off between cost and risk would be achieved. The analysis is based on the assumption of a yield curve with a positive slope on average. The lower cost of short-term borrowing should be weighed against the increased refinancing risk resulting from such borrowing.

For some years, the Debt Office has maintained different durations in nominal SEK debt and foreign currency debt. The reasons for this have mainly been practical. It requires a somewhat higher duration than 2.7 years in nominal SEK debt to maintain a liquid yield curve up to ten years. When preparing its benchmark decisions in prior years, the Debt Office has shown that the cost and risk effects of dividing up duration in this way are insignificant.

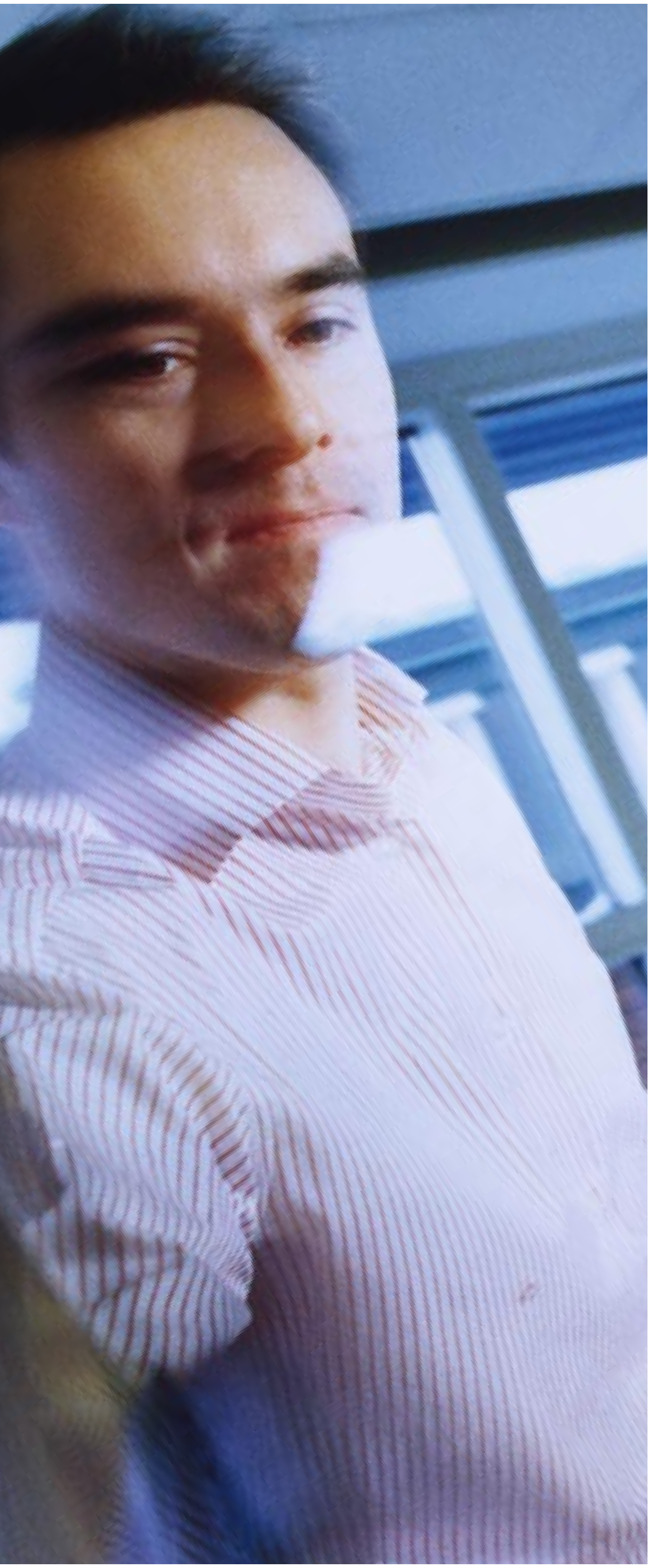
As previously, the target for the overall duration of nominal debt, 2.7 ± 0.3 years, was achieved by maintaining duration of 2.9 years in nominal SEK debt and 2.3 years in foreign currency debt.

Maturity profile, overall government debt, Dec. 31, 2003
SEK billion

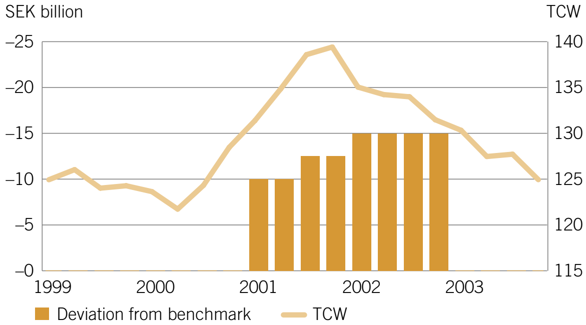


Size, structure and duration of central government debt, 1999–2003, SEK billion (if not otherwise stated)

	1999	2000	2001	2002	2003
Duration of nominal debt, years	2.9	2.9	2.7	2.5	2.7
Nominal SEK debt	882	811	686	670	726
As percentage of total debt	62	61	56	56	59
Inflation-linked borrowing	135	138	117	158	173
As percentage of total debt	10	10	10	13	14
Foreign currency debt	406	395	407	375	330
As percentage of total debt	29	29	34	31	27
Unconsolidated central government debt	1,423	1,344	1,211	1,204	1,229



Pace of amortisation and krona exchange rate



The chart shows the exchange rate of the Swedish krona against the Total Competitiveness Weights (TCW) index of currencies and the deviations between the Government's benchmark for the pace of amortisation and the benchmark set by the Board of the Debt Office. The deviations in 2001 and 2002 signify smaller amortisations than the benchmark.

The foreign currency mandate

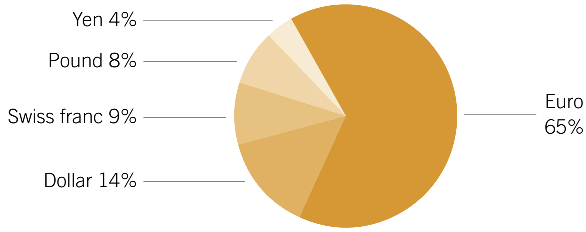
In December 2002, the Debt Office decided to amortise foreign currency debt in line with the Government's guidelines, i.e. amortise SEK 25 billion. Our analysis indicated that the exchange rate of the krona against the foreign currency benchmark and the trade-weighted TCW currency index had strengthened and was reasonably valued.

At the end of 2003, the exchange rate of the krona against the euro was at about the same level as one year earlier. However, the dollar had weakened substantially against the euro, and thus also against the krona. As a consequence of these developments, the TCW index for the krona had strengthened to about 125.

Foreign currency debt mostly in euro

The foreign currency debt is mainly denominated in euro. The allocation among currencies is intended to decrease the risk of fluctuations in the value of the foreign currency debt measured in SEK, but cost considerations are also taken into account. In 2000, the Debt Office increased the share of Swiss francs, a low interest rate currency, and decreased the share of euro. This led to losses during the first years, but in 2003 it led to SEK 1.6 billion in gains. This re-weighting in favour of the Swiss franc has meant an estimated cost saving of about SEK 600 million.

Benchmark portfolio by currency, Dec. 31, 2003



Funding

During 2003, the Debt Office doubled its issue volume of nominal bonds compared to 2002. Demand for inflation-linked bonds was strong and the Debt Office issued nearly SEK 20 billion worth of such bonds. Inflation-linked bonds remained less costly than other borrowing.

Financial markets in 2003

During 2003, short-term interest rates fell in both Europe and the United States, due to continued easing of monetary policy. At year-end the US Federal Reserve's key short-term interest rate was 1 per cent. In the euro zone, the European Central Bank's key rate was 2 per cent. In Sweden, too, the Riksbank continued to lower its key interest rate. At year-end, the Riksbank's repo rate was 2.75 per cent. Long-term interest rates changed sharply during the year. In both the euro zone and the US, long-term rates were close to 4 per cent both at the beginning and the end of 2003, but before the summer they dropped nearly to 3 per cent. The corresponding developments occurred in Sweden: long-term Swedish Treasury bonds ended the year at yields of about 4.70 per cent and touched 3.90 per cent at their lowest. Despite largely unchanged nominal long-term interest rates, in real terms these rates fell by 0.2 percentage points to 2.9 per cent. The American dollar weakened considerably against most major currencies during the year. The Swedish krona thus strengthened, especially against the dollar but also to some extent against the euro.

Nominal SEK borrowing

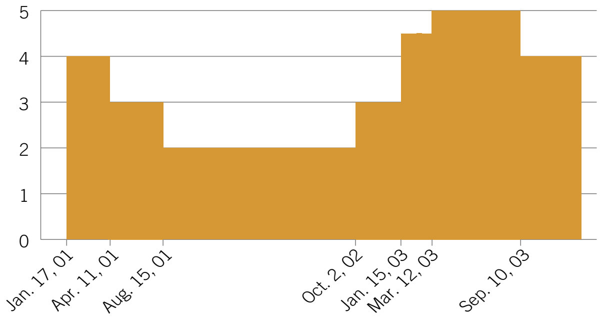
Doubled bond volume

Funding by means of bonds rose to SEK 105 billion in 2003, compared to SEK 50 billion during 2002.

The Swedish central government's net borrowing requirement was unexpectedly large at the end of 2002. The increase had to be funded with Treasury bills. As a result, duration became shorter than the target of 2.9 years. For this reason, auction volume was raised from SEK 3 billion to SEK 4.5 billion at the beginning of 2003 and then

Issue volumes of Treasury bonds 2001-2003

SEK billion



to SEK 5 billion per auction in March. The adjustment of nominal krona debt to the duration target was achieved during the year, and the Debt Office thus decreased issue volume to SEK 4 billion per auction in September.

Borrowing in the form of bonds mainly took place in the Debt Office's reference loans with maturities of two, five and ten years, which are traded in the electronic interbank market.

Average running yield was somewhat lower than the average market rate. The running yield outcome was due to interest rates on the issue date. The choice of issue date is not based on the Debt Office's perception of interest rates. The difference between average running

Volume issued in SEK million and average running yield by loan

Loan	Maturity	Volume issued	Average running yield	Offered rate on issue date
1044	2006-04-20	18,000	3.59	3.59
1043	2009-01-28	36,994	4.10	4.11
1046	2012-10-08	8,998	4.66	4.67
1041	2014-05-05	40,991	4.66	4.67
Total		**104,983**	**4.25**	**4.26**

Average cover ratio, nominal bonds, 1999–2003

	1999	2000	2001	2002	2003
Cover ratio [1]	2.65	2.87	2.34	2.89	3.16

[1] *Volume of bids submitted divided by issue volume offered.*

yield and market rate on the issue date showed that the bonds were issued in parity with prevailing market rates. The Debt Office follows a borrowing policy characterised by transparency and predictability. Auctions have a predetermined schedule.

The Debt Office's bond issues during 2003 were over-subscribed. Despite increased volume per auction, the cover ratio was higher during 2003 (3.16) than in 2002 (2.89).

Larger Treasury bill portfolio

Treasury bill auctions normally take place every two weeks. Treasury bills are used in response to seasonal and other temporary variations in the borrowing requirement. Issue volumes of Treasury bills thus vary sharply from one month to another. During 2003, auction volume varied between SEK 5 billion and SEK 35 billion per auction. The Treasury bill portfolio amounted to SEK 269 billion in borrowing amounts outstanding at the end of 2003. A total of SEK 400 billion in Treasury bills was offered.

The average running yield in the auctions during 2003 was 3.08, which was considerably lower than in 2002. However, it was in line with market interest rates, which fell during 2003.

Average cover ratio, Treasury bills, 1999–2003

	1999	2000	2001	2002	2003
Cover ratio [1]	2.33	2.90	2.22	2.81	2.29

[1] *Volume of bids submitted divided by issue volume offered.*

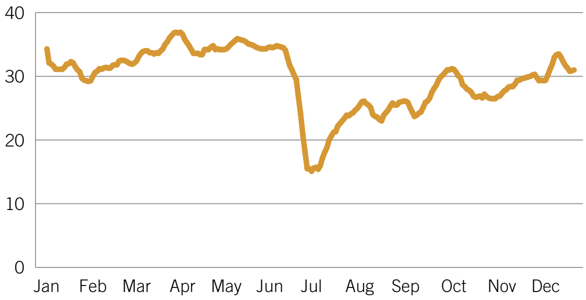
Short-term borrowing using swaps

One alternative to borrowing in the form of Treasury bills is to issue Treasury bonds and then swap them to short-term interest. During the year, we carried out interest rate swaps equivalent to SEK 10 billion. The box on page 13 describes this technique. The Debt Office limits the scale of its interest rate swaps in order to avoid an excessively dominant market position.

When the Debt Office replaces Treasury bills with swap borrowing, this also involves an increase in risks (i.e. counterparty risks) in central government borrowing.

Swap spread with five-year maturity, 2003

Basis points



Inflation-linked borrowing

Sharp increase in demand for inflation-linked bonds

The Debt Office has issued inflation-linked bonds since 1994. They comprise about 14 per cent of the central government debt. According to the Government's guidelines, this share should increase in the long term. The pace of increase is determined by the trend of demand and cost, relative to other types of debt. The demand for inflation-linked bonds remained strong during 2003. This was reflected in high cover ratios and favourable running yields, while the Debt Office issued more inflation-linked bonds than in 2002.

Growth in inflation-linked bond portfolio

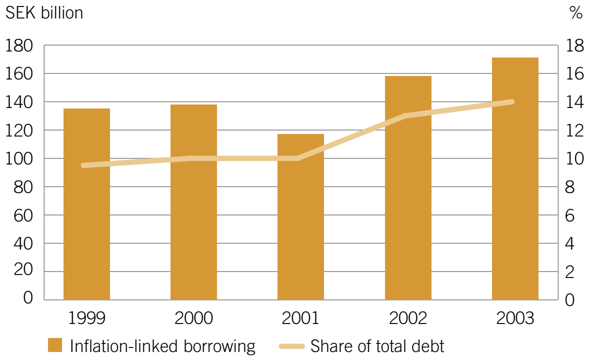
During 2003 a number of market players re-allocated their assets. This contributed to heavier demand for fixed income products and especially for inflation-linked bonds. Trading in the secondary market rose compared to the preceding year, and there was greater interest than previously in the Debt Office's issues. Nor did the demand for these bond issues slow when real interest rates fell during the year.

The total outstanding portfolio of inflation-linked bonds rose from SEK 157.2 billion to SEK 171.8 billion during

Inflation-linked bond auctions, 1999–2003

	1999	2000	2001	2002	2003
Net issue volume, SEK billion	1.6	2.4	–2.9	2.0	18.2
Net volume sold, SEK billion	4.6	6.4	11.4	23.4	18.2
Cover ratio	1.7	4.5	4.8	4.4	3.8
Average yield, %	3.94	3.93	3.64	3.59	2.83
Average break-even inflation, %	1.33	1.51	1.67	1.90	2.09

Change in the inflation-linked bond portfolio and its share of total government debt



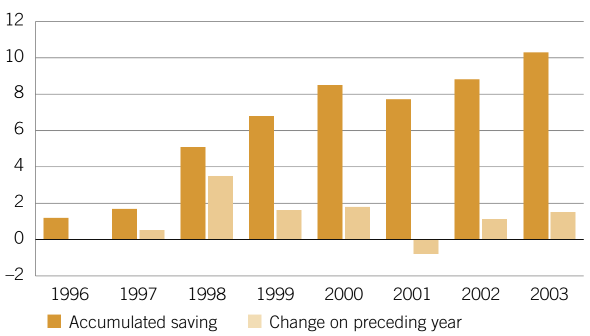
2003. Measured as a share of total government debt, this represented an increase from 13 to 14 percent. During 2003, the Debt Office issued SEK 18.2 billion worth of inflation-linked bonds. At the beginning of the year, the Debt Office's target was to issue SEK 15 billion in such bonds.

During 2003, the Debt Office issued inflation-linked bonds at break-even levels of between 1.7 per cent and 2.5 per cent and an average of about 2.1 per cent, which was in line with the Riksbank's inflation target.

Improved saving

The estimated accumulated saving from inflation-linked borrowing since the Debt Office began issuing such bonds in 1994 rose to SEK 10.3 billion, compared to SEK 8.8 billion in 2002. The year's saving was thus SEK 1.5 billion. The saving is calculated as the difference in cost between borrowing in the form of inflation-linked and nominal bonds. The increase was due to the passage of another year and the low rate of inflation during the year. A large proportion of this accumulated saving stems from low inflation rates in prior years, and since a substantial share of inflation-linked bond issues occurred before 1997, the Debt Office reports the aggregate cost saving from the time it began issuing these bonds. However, the actual saving depends on the trend of inflation during the entire period until the maturity of each respective loan.

Estimated saving from accumulated borrowing in inflation-linked bonds during the period 1996-2003



Foreign currency borrowing

Total borrowing SEK 21.5 billion

During 2003, the Debt Office amortised SEK 25.4 billion in foreign currency debt. Foreign currency loans totalling SEK 46.8 matured during the year. The Debt Office borrowed the equivalent of SEK 21.5 billion, both by issuing bonds in foreign currencies (direct foreign currency borrowing) and by issuing SEK-denominated bonds that were then swapped into foreign currencies (krona/swap borrowing).

Interest-rate swaps in kronor are used as one element of foreign currency borrowing and as an instrument for short-term borrowing.

Various forms of borrowing in currencies, volumes 1999–2003

SEK billion	1999	2000	2001	2002	2003
Maturities of public loans and private placements	64.7	59.3	28.2	35.4	29.5
Maturities of currency swaps	–	–	9.2	18.1	11.2
Realised exchange rate differences	–6.2	–6.2	12.3	6.7	5.2
Miscellaneous	1.4	–1.6	4.6	–7.4	
Total maturities	**59.9**	**51.5**	**54.3**	**52.8**	**45.9**
Public loans and private placements	22.3	–	–	33.1	10.6
Krona/foreign currency swaps	40.0	24.4	35.0	21.2	10.6
Commercial paper [1]	–25.7	–	4.2	–3.3	–0.9
Total borrowing	**36.6**	**24.4**	**39.2**	**51.0**	**20.3**
Net borrowing	**–23.3**	**–27.1**	**–15.1**	**–1.8**	**–25.6**
Miscellaneous [2]					0.2
Amortisation					**–25.4**

[1] *CP borrowing refers to borrowing minus amounts falling due (net borrowing).*

[2] *Amortisations of foreign currency debt during 2003 amounted to SEK 25.4 billion. Net borrowing of SEK 25.6 billion should thus be adjusted by SEK 0.2 billion related to exposure changes from currency exchange transactions not included in the items reported in the table.*

The Debt Office's limited borrowing requirement combined with strong interest in our bonds in foreign currencies resulted in favourable terms for direct foreign currency borrowing during the year. The Debt Office issued two new bond loans and expanded outstanding loans. These loans were primarily sold to small and medium-sized investors in Europe.

The variable cost of capital market borrowing amounted to between 25 and 28 basis points below USD LIBOR for larger loan amounts and between 27 and 30 for smaller loans. The average cost of 27 basis points below USD LIBOR was more than 7 basis points lower than in 2002.

Krona/swap borrowing (see box page 13) means that the gains from the difference between the swap interest rate and Treasury bond yield (swap spread) is locked in against the short-term interest rate in euro (EURIBOR). The swap spread successively shrank until the Swedish referendum on euro zone membership in September. Expectations of Swedish membership were partially priced into the swap spread. After that, the swap spread widened somewhat, but otherwise followed international developments. Krona/currency swaps equivalent to SEK 10.6 billion were carried out during 2003. The average borrowing cost was 28 basis points below USD LIBOR.

Cost of various forms of borrowing, 1999–2003

Basis points below USD LIBOR	1999	2000	2001	2002	2003
Krona/foreign currency swaps	60.0	66.6	47.0	26.6	28.2
Public loans	3.0	–	–	19.8	26.9
Private placements	24.8	–	–	–	–
Commercial paper	18.8	–	–	–	–
Average	**39.6**	**66.6**	**47.0**	**22.5**	**27.5**

Liquidity management

The Debt Office's liquidity management is related to the short-term funding and investment needs of the central government. As a rule, liquidity follows a pattern of surplus liquidity during a few days in the middle of a month in conjunction with tax payments. This surplus disappears the same day that payment is disbursed for the

Treasury bill that matures during that month. The Debt Office has a funding requirement on 76 per cent of the banking days during the year.

Average daily deficit of SEK 17 billion

In its liquidity management, the Debt Office uses overnight loans, repos on government securities and other interest-bearing securities and liquidity bills. Most sums are borrowed or invested in the overnight loan market.

The deficit averaged SEK 17 billion on days with deficits. These were funded in advance via sale of on-tap and liquidity bills. The remaining deficits were 71 per cent funded via the overnight loan market and 29 per cent via the repo market. The chart to the left shows the variations in borrowing requirement during a typical month, where negative figures represent surplus liquidity.

In case of surplus liquidity, the Debt Office invests in the repo and overnight loan market. During periods of large surpluses, the Debt Office buys Treasury bills and other interest-bearing securities outstanding.

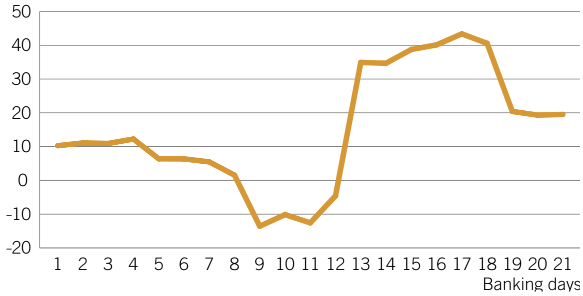
During 2003, the Debt Office continued to issue one- and two-month on-tap bills and liquidity bills. During the year, it issued on-tap bills and liquidity bills with a nominal value of SEK 426 billion.

Currency exchanges of about SEK 40 billion kronor

During the year, the Debt Office exchanged about SEK 38.5 billion worth of currencies. These currency exchanges are one element of liquidity management, and their primary purpose is to ensure that there is enough foreign currency to cover the Debt Office's daily flows.

Daily borrowing requirement during a typical month (March 2003)

SEK billion



The swap market

In order to create a short-term interest rate exposure via the swap market, as a first step the Debt Office issues a bond in Swedish kronor. Then it carries out an interest rate swap in Swedish kronor, in which the Debt Office receives fixed interest and pays floating interest Stockholm Interbank Offer Rate (STIBOR). The gain on this transaction is that the interest rate on the bond is lower than the interest rate that the Debt Office receives in the interest rate swap (the difference is called swap spread). Meanwhile the Debt Office pays a somewhat higher interest rate (STIBOR) than the Treasury bill interest rate. This borrowing technique leverages the central government's relative strength as a borrower in long maturities, enabling it to reduce its borrowing costs. It can thus achieve short-term borrowing by issuing Treasury bills or by first issuing a Treasury bond and then carrying out an interest rate swap.

Creating foreign currency exposure via the swap market involves using the domestic bond market as a source of borrowing (krona/swap borrowing). First the Debt Office issues a bond, which is swapped to short-term interest (see above). Then it carries out a currency swap, in this case a "basis swap", which involves changing a floating interest rate in kronor for a floating interest rate in a foreign currency. Meanwhile the Debt Office buys the foreign currency in the spot market when it enters into the transaction and sells the foreign currency when closing it. The basis swap has the same maturity as the interest rate swap but interest payments are based on three- or six-month floating interest rates. In the basis swaps, the Debt Offices receives floating STIBOR and pays floating interest in euro at the European Interbank Offer Rate (EURIBOR). Using this technique, the Debt Office can take advantage of the swap spread minus a small cost for implementing the basis swap. In principle, the borrowing cost is the floating EURIBOR rate minus the swap spread.

In practice, the room for interest rate swaps is limited by the fact that the Debt Office is a large player in this market. This room can be used to replace Treasury bills or as a part of foreign currency borrowing. In the trade-off, the costs of direct foreign borrowing are important.

Active management of foreign currency debt

The Debt Office's active management of foreign currency debt resulted in a gain of more than SEK 900 million during 2003. Most of this gain came from positions in the foreign currency market. The increased dollar debt, which was unwound during the year, also resulted in a total gain of SEK 4.5 billion. During 2003, the Debt Office engaged two new external managers, Blackrock and Goldman Sachs.

Operations and evaluation of results

Positive results in foreign currency debt management

The Debt Office's total active management of the foreign currency debt during 2003 showed a gain of SEK 937 million, equivalent to 0.26 per cent of the average value of the foreign currency debt during the year.

Belief in weaker dollar

The main strategy of foreign currency debt management during the year was to position the Debt Office for a weaker dollar. During the first half of 2003, the Debt Office mainly bought euros for dollars and during the last six months of 2003 yen for dollars as well. Throughout 2003 the Debt Office was also positioned for a stronger euro against the Swiss franc. Especially during the first and fourth quarters, respectively, these positions gave rise to most of the year's gains.

Belief in lower euro interest rates

The most successful strategies on the fixed income side were positions that foresaw lower European interest rates as well as American interest rates again rising above European ones. The Debt Office also periodically positioned itself successfully for lowered or unchanged interest rates from the ECB and Federal Reserve by purchasing short-term interest rate contracts. We also took advantage of the high volatility in the dollar market through trading in swaptions.

Positive return for external managers

To spread the risks of management as well as to obtain a yardstick of the Debt Office's active management of foreign currency debt, since 1992 the Debt Office has engaged external managers. These external managers also serve as an important source of information for internal debt management. During the year, the Debt Office worked with seven external managers: ABN Amro, Blackrock, Credit Suisse Asset Management (CSAM), Fischer Francis Trees and Watts (FFTW), Goldman Sachs Asset Management (GSAM), Pimco Asset Management and State Street Global Advisors.

The Debt Office continuously evaluates the external managers. Since CSAM and FFTW were not regarded as having achieved the return requirements we had established, they were replaced. Beginning on October 1 the Debt Office engaged Blackrock and GSAM.

The managers' risk mandate is based on notional reference portfolios that are equivalent to a total of SEK 30 billion. The average return for external managers was 0.16 per cent of average managed debt amount during the year. The spread between managers was rather wide, with –0.05 per cent as the worst return and 0.61 per cent as the best return.

Risk management in the foreign currency debt

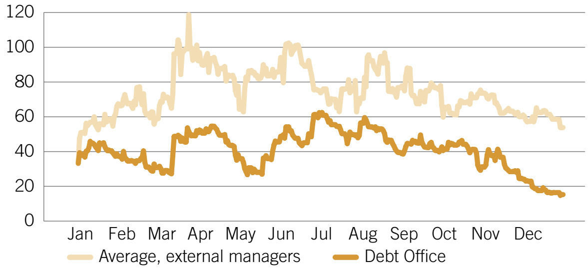
The Debt Office pursues active management of the foreign currency debt for the purpose of lowering costs, compared to passively managed debt. The techniques it uses are the same, in principle, as those used by other major financial market players.

Value-at-Risk (VaR)

Since January 2003, the Debt Office has pursued active management under a mandate based on Value-at-Risk (VaR). VaR is a measure of the risk in positions taken that is calculated with the help of historical data on volatility and correlation of fixed income and foreign exchange markets. According to guidelines decided by the Board,

Value-at-Risk, 2003

SEK million. One-day investment horizon, 95 per cent confidence interval.



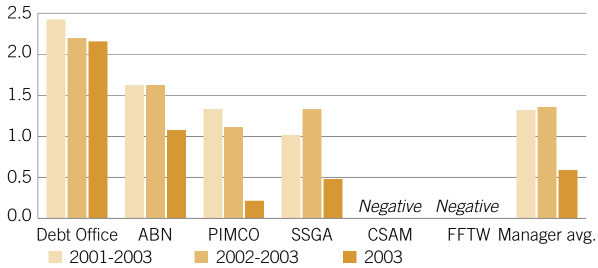
active management may never exceed SEK 220 million in daily VaR. The mandate is supplemented with more traditional absolute position limits. The positions in a given currency may not be larger than the equivalent of 6 per cent of the managed debt amount. Fixed income positions may not affect the total duration of the managed debt amount by more than 0.4 years in each individual currency and 0.6 years overall. The total actively managed debt amount has been fixed at SEK 200 billion.

In 2003 the risk position or VaR in active debt management averaged SEK 41 million per day, i.e. on average it did not exceeded an expected daily loss of SEK 41 million in 95 per cent of cases. This was equivalent to 0.012 per cent of the foreign currency debt and was somewhat lower than the corresponding figure in 2002. The highest expected daily risk level was SEK 61 million and the lowest SEK 15 million, which represented an average risk utilisation of about 25 per cent of the maximum allowed during the year. External managers with high risk utilisation were around 50 per cent of the maximum allowed, while those with lower risk utilisation were around 25–30 per cent.

Risk-adjusted return

During 2003 the Debt Office achieved an "information ratio" of just above 2. The information ratio states a return divided by the volatility (standard deviation) in this return and is a widely used measure. The information ratio shows the relationship between the return on management and the risk that is taken. A high figure means that the manager has taken relatively little active risk in relation to the return that is achieved.

Risk-adjusted return on active management during the period July 2001 to December 2003



Increased dollar debt

During the summer of 2003, the Debt Office unwound its strategic euro/dollar position. The last part of this position was closed through a number of small transactions at an average exchange rate of around USD 1.10 per euro. Altogether, the Debt Office thereby realised a total currency gain equivalent to about SEK 4.2 billion. At the same time, the Debt Office was also able to take advantage of a positive interest rate differential during the period when we borrowed, via forward contracts, at a low American interest rate and invested at a higher European interest rate. This positive interest rate differential was equivalent to about SEK 300 million: SEK 200 million during 2002 and SEK 100 million during 2003. To summarise, the Debt Office realised a gain of about SEK 4.5 billion. When it was realised, our gain helped lower the interest costs on the foreign currency debt and consequently lowered the borrowing requirement in Swedish kronor.

In December 2000, the Debt Office exchanged about SEK 24 billion, representing six per cent of the foreign currency debt, from euro debt to dollar debt. During 2003 the Debt Office carried out a number of partial closures of its position at successively better exchange rates until May. At that point it noted the best closing exchange rate, just below USD 1.17 for one euro. The position was unwound by means of a number of small transactions at an average exchange rate of around USD 1.10 per euro. Overall, this meant that the Debt Office bought dollars at an exchange rate of USD 0.897 per euro and sold them at an average exchange rate of USD 1.087 per euro.

Returns, 1999–2003

Active management resulted in a positive return of SEK 138 million in the period 1999-2003. Large negative returns during 1999 and 2000 were followed by large positive returns in 2002 and 2003. As the table below indicates, fixed income positions accounted for the entire positive five-year return. In this context, it should also be noted that the strategic dollar position approved by the Board limited the scale of the positions for a weaker dollar taken in active management. With the exception of 2000, the Debt Office's active management yielded better returns than its external managers achieved.

Since the Debt Office began active management of foreign currency debt in 1992, it has achieved a cost saving of about SEK 12 billion, which is equivalent to 0.36 per cent of the foreign currency debt. Positive returns are mainly attributable to the years 1992–1998 and 2002–2003 and positions in the fixed income market accounted for most of the saving, but foreign exchange positions also showed a positive return for the entire period from 1992. These figures do not include the gain of about SEK 4.5 billion from the increased dollar debt.

Return on management of foreign currency debt

	1999	2000	2001	2002	2003	Entire period
Return in SEK million						
Total management	–546	–584	–103	434	937	138
Debt Office	–506	–604	–78	392	880	84
Of which: Fixed income positions	65	110	83	–78	224	404
Foreign exchange positions	–571	–714	–161	470	656	–320
External managers	–40	20	–25	42	57	54
Return in per cent						
Debt Office	–0.12	–0.16	–0.02	0.11	0.51	0.32
External managers	–0.33	0.17	–0.12	0.14	0.14	0.00
Risk [1]						
Debt Office	0.10	0.28	0.12	0.11	0.24	0.17[2]
External managers	0.22	0.23	0.21	0.24	0.42	0.26[2]

[1] *Annual standard deviation calculated on the basis of monthly data.* [2] *Average annual standard deviation.*

The retail borrowing market

The retail borrowing market enables private individuals and small businesses to invest money at good interest rates without any fees. The Debt Office also issues lottery bonds. During 2003, sales of lottery bonds totalled SEK 10 billion. The success of National Debt Savings continued, and the portfolio rose by SEK 2 billion to about SEK 19 billion in 2003. The retail borrowing market saved the central government SEK 260 million, while savers obtained a good return on their money.

Operations

The Debt Office's borrowing from private individuals and other small investors totalled SEK 59 billion at the end of 2003, which was somewhat higher than the preceding year. The retail borrowing market accounted for 4.8 per cent of total central government debt. A minor re-allocation occurred among the various debt instruments. The outstanding volume of lottery bonds shrank somewhat, while the National Debt Savings borrowing portfolio rose somewhat. The "Treasury Instruments" project continued, with Treasury bills being launched in the retail market during the year.

Products

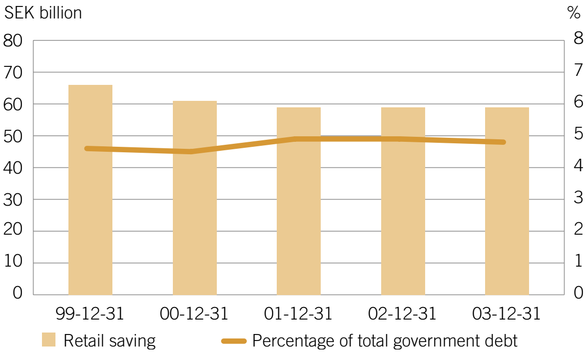
SEK 10 billion in lottery bonds

Two new lottery bond loans were issued during 2003. During the spring, the Debt Office sold loan 2003:1 when three loans, 1996:2 and 2000:1–2, matured. The total issue volume of the two new loans was SEK 9.7 billion. Maturities totalled SEK 11.9 billion, which meant that the portfolio of lottery bonds outstanding decreased by SEK 2.2 billion during the year.

The Debt Office anticipated that about 65 per cent of the volume falling due would be issued in the form of the new loans. However, sales turned out better than expected. The issue volume of the loan that was sold in the autumn exceeded the volume falling due by a billion kronor. This was the first time since 1988 that the Debt Office issued more in a new loan than the loans that simultaneously fell due. With a volume of SEK 5.5 billion, it was the largest single lottery bond loan issued since 1986. One conceivable explanation is that in periods of low interest rates, lottery bonds are a competitive alternative to bank savings.

The Debt Office accounted for more than 50 per cent of total sales, which was somewhat higher than in 2002.

The retail borrowing market as a percentage of government debt



National Debt Savings continuing to increase

National Debt Savings continued to grow during 2003, although the increase was somewhat lower over the year as a whole than during 2002. The total National Debt Savings portfolio amounted to SEK 18.8 billion at year-end. This was an increase of SEK 2.2 billion during 2003.

Marketing efforts for National Debt Savings were aimed at reaching the broadest possible target group. In its marketing, the Debt Office also called greater attention

National Debt Savings, volume outstanding and change during the year, SEK billion

	Volume outstanding	Change in 2003
Fixed nominal interest rate [1]	7.3	–0.3
Fixed inflation-linked interest rate	1.1	–
Floating interest rate	9.6	2.3
Floating interest rate, Monthly Savings	0.8	0.3
Total National Debt Savings	**18.8**	**2.2**

[1] *Also includes SEK 0.4 billion in savings at nominal floating interest rate.*

to the fact that this product includes floating, fixed and inflation-linked savings alternatives. This is a change compared to prior years, when marketing focused on "the Savings Account", which carries a floating interest rate linked to the Riksbank's repo rate. Marketing was adjusted to a shift in customer demand towards longer interest rate refixing periods.

The total number of National Debt Savings customers at year-end was about 137,300, an increase of about 13,000 customers during the year. The average balance in National Debt Savings at year-end was about SEK 134,000 per account.

More people discovering Treasury Instruments

In the autumn of 2002, the Debt Office introduced a programme known as Treasury Instruments, in which private individuals and other small investors may participate in the Debt Office's auction sales of Treasury instruments via the Internet. Internet customers take part in the same auctions as institutional investors and can submit bids of between SEK 25,000 and SEK 5 million. Initially, only auctions of nominal Treasury bonds were opened to the retail borrowing market. In February 2003, the Debt Office also made Treasury bill auctions available to retail customers, and since January 2004 also inflation-linked bonds.

The Debt Office has about 2,000 registered Treasury instrument customers, about half of them added during 2003. Around one fourth of registered customers have submitted bids.

Treasury Instruments is targeted both to private individuals and companies. Companies are an important target group, since they often have larger amounts to invest than private individuals. Of registered customers, nearly 10 per cent are companies. Meanwhile they account for as much as one third of sales volume to the private borrowing market at auctions.

The marketing of Treasury instruments differs somewhat from the marketing of the Debt Office's other retail market products, since it aims at a relatively narrow target group. The target customer for Treasury instruments is a more financially knowledgeable person than the target customer for National Debt Savings and Lottery Bonds. The marketing is also more long-term oriented than for the other products. Its purpose is to boost awareness of Treasury Instruments in the long term and thereby also expand the number of registered and active customers.

Results

To determine the Debt Office's share of the savings market, a suitable definition of this market is required. Like last year, the Debt Office has chosen a broad definition that includes all interest-bearing savings alternatives (deposits in bank accounts, fixed income funds and retail bonds for smaller investors). Using this definition, the total Swedish savings market was SEK 786 billion on September 30, 2003. The Debt Office's share was 7.1 per cent.

In 2003 retail market borrowing resulted in a saving of about SEK 260 million compared to borrowing in the money and bond market. Most of this saving is attributable to lottery bonds. 1999 to 2003, the Debt Office's total saving on retail borrowing was about SEK 1.3 billion. The purpose of the Treasury Instruments programme is to broaden the investor base in the long term. It can also be regarded as a pilot project for developing new, modern sales channels via the Internet.

Treasury Instruments
– number of bids and volume issued in 2003

	Nominal Treasury bonds	Treasury bills	Total
Number of bids	143	717	860
Bids per auction	6	34	40
Issue volume (SEK K)	16,035	115,945	131,980
Issue volume per auction (SEK K)	697	5,521	6,218

Saving due to retail market borrowing compared to equivalent maturities in the money and bond market

SEK million	1999	2000	2001	2002	2003
Lottery bonds	136	271	287	317	240
National Savings Account	3	3	2	–	–
National Debt Savings	5	5	10	10	20
Total saving	**144**	**279**	**299**	**327**	**260**

Cash Management Department

Sweden's central government agencies borrow and invest their funds in the Cash Management Department of the Debt Office. They borrow for fixed investments and deposit funds not immediately needed for disbursements. In 2003, the Debt Office signed agreements with three banks to make the Swedish state payment system more efficient. Every year the state manages payments totalling 4,000 billion.

The Cash Management Department, known in Swedish as "the state's internal bank", must provide good service and apply the same interest rates at which the Debt Office itself borrows or invests in the capital market.

Government agencies must also be able to disburse and receive payments easily and efficiently. The Cash Management Department is responsible for ensuring that the state payment system lives up to these requirements.

Operations

New framework agreements for state payments

On January 1, 2004, the framework agreements that the Debt Office signed on July 3, 2003 with Swedbank (FöreningsSparbanken AB), Nordea Bank AB and SEB AB entered into force.

Proposal for changes in handling of intra-state payments

At present intra-state payments, like all other payments, occur as payment transactions in the banking system. Among other things since such transactions are subject to fees under the new framework agreements, there is reason to examine whether and how these transactions can be handled as inter-account transfers in the Cash Management Department's business system instead of as actual payments. To study this possibility, in 2002 the Debt Office initiated a project that has examined various alternatives for changing the processing of intra-state payments between the Debt Office and government agencies. The project's proposal was published in October 2003.

Under the proposal, the work of both the agencies and the Debt Office related to deposits and lending would become easier. Overall, the proposal should lead to more cost-effective operations. The proposal is being circulated among a number of agencies for comment early in 2004. According to plans, the introduction of systems support for intra-state payments in keeping with the proposal will occur during 2004.

Setting of interest rates unchanged

The Debt Office applies market terms to loans and deposits, based on borrowing costs in the capital market. This means that loans and deposits are valued on market terms both when initiated as well as in case of early redemption. Market valuation is based on prices in secondary markets for Treasury bills and nominal Treasury bonds.

Automated processing means greater efficiency

Today's time-consuming manual processing of appropriations to government agencies can hopefully be performed with a greater degree of automation. During the

Fees replace float in new framework agreements

The banks will not, as earlier, receive interest income when money is moved within and between banks. This "float" has been part of the state's general interest cost, but the individual agency has not seen or noticed this cost in its payment operations. Agencies will now instead pay fees for their payments. This should also increase incentives for agencies to streamline their payment operations.

Framework agreements replace various special agreements

The framework agreements have made it possible to terminate a number of separate agreements, and the agencies that had these may now instead use the new framework agreements. Competition for state payments should increase, which in turn is expected to help streamline payment operations and decrease overall costs to the state.

autumn of 2003, a project was carried out that will make it possible to transmit information on appropriations from the Hermes IT system at the Ministry of Finance to the Cash Management Department's SIBSYS system. Increased automation will not only save resources but should also contribute to greater security in processing.

New borrowing model simplifies administration

The new model for borrowing by agencies that was introduced in 2002 has simplified borrowing administration. By the end of 2003, about 70 per cent of the agencies had switched to this model. New borrowing terms as well as interest rates have given the agencies good incentives to change to the new borrowing model. The fees introduced on January 1, 2004 will hopefully increase interest among other agencies to switch to the new borrowing model.

High customer satisfaction index

Every year the Debt Office carries out a customer survey of how central government agencies perceive the quality and service provided by the Debt Office. In its 2002 survey, the Debt Office introduced a ten point scale. Responses were weighed together in a total index of questions on quality and service. This customer satisfaction index was 81 (out of a maximum of 100). In 2003 the score was again 81, which should be regarded as a favourable result.

Lending and deposits rose, but payment volume declined

Lending to government agencies etc. rose by SEK 16.7 billion or 8.5 per cent during the 2003 financial year. Total lending amounted to more than SEK 212 billion on December 31. During the same period, deposits rose by SEK 4.4 billion or 6 per cent. Total deposits amounted to more than SEK 78 billion on December 31.

Payment volume declined during 2003. This applied to both incoming and outgoing payments.

Payment flows through the government cheque account

SEK billion	2002	2003
Incoming payments	2,093	2,023
Outgoing payments	2,087	2,025
Total	**4,181**	**4,048**

Lending and deposit volume, SEK million, December 31, 2003

		Lending			**Deposits**		
			Change, 2003			Change, 2003	
		Position SEK M	12 months SEK M	12 months Per cent	Position SEK M	12 months SEK M	12 months Per cent
State enterprises	Luftfartsverket *(Civil Aviation Administration)*	7,017	508	7.8	0	0	–
	Sjöfartsverket *(Maritime Administration)*	0	0	–	621	–82	–11.7
	SJ Stab *(rail company)*	0	–300	–100.0	0	0	–
	Svenska Kraftnät *(national grid)*	665	166	33.1	0	0	–
Limited companies	A-Train AB *(high-speed railway)*	1,000	0	0.0	0	0	–
	Botnia AB *(railway)*	2,865	1,215	73.6	0	0	–
	RIKAB *(TV licence fees)*	709	377	113.3	235	157	201.3
	Jernhusen AB, Euromaint AB *(rail prop. & systems)*	1,250	–3,065	–71.5	0	0	–
	SVEDAB *(Öresund Link)*	3,360	170	5.3	0	0	–
	Svenska Spel AB *(gaming)*	0	0	–	1,700	–200	–10.5
Agencies	Banverket *(National Rail Administration)*	10,903	1,666	18.0	1,225	0	0.0
	CSN *(National Board of Student Aid)*	121,503	9,094	8.1	0	0	–
	FMV *(Defence Materiel Administration)*	15,256	2,466	19.3	2,950	0	0.0
	PPM *(Premium Pension Authority)*	1,764	140	8.7	27,903 [3]	–158	–0.6
	Statens Fastighetsverk *(National Property Board)*	5,948	440	8.0	221	29	15.1
	Vägverket *(National Road Administration)*	6,145	1,733	39.3	2,200	271	14.0
	Other agencies	33,794 [1]	2,100	6.6	41,390 [2]	4,365	11.8
Total		**212,179**	**16,708**	**8.5**	**78,445**	**4,425**	**5.9**

[1] *Incl. SEK 16.4 billion, agencies' borrowing for fixed assets.* [2] *Incl. SEK 23.4 billion, interest-bearing accounts.* [3] *Premium pension funds, the National Social Insurance Board.*

Guarantees & loans with credit risks

The Debt Office is responsible for ensuring that the risk assumed by the Swedish state in connection with guarantees is limited, that the rights of the state related to guarantees are safeguarded and that follow-ups and reporting occur. Over a long period of time, the costs of these guarantee operations shall correspond to their revenues. In 2003, the Debt Office's guarantee commitments totalled about SEK 164 billion.

By pricing its guarantees according to insurance principles, the Debt Office shall contribute to the efficient utilisation of the state's economic resources. The Debt Office shall work to ensure that lending operations by other government agencies are carried out efficiently.

Operations

The Debt Office's guarantee portfolio of SEK 164 billion is dominated by international commitments, infrastructure projects, the financial service sector and pension obligations. The portfolio is characterised by high exposure to individual projects. The largest single commitment, Öresundsbro Konsortiet or ÖSK (construction of a fixed link between Sweden and Denmark), amounts to more than SEK 30 billion. From a risk perspective, the portfolio is even more concentrated. Provisions for future losses at ÖSK comprise more than 75 per cent of the total provisions in the portfolio.

During 2003 the Debt Office issued a new guarantee of SEK 170 million for the state-owned rail freight company Green Cargo (formerly a unit of SJ). This guarantee is constructed in such a way that indemnification may occur only if the company has gone bankrupt. Some twenty new guarantees were issued for ÖSK related to borrowing transactions entered into during the year.

Decreased risk for Venantius guarantees

The financial position of the state-owned housing finance company Venantius improved, since its equity increased and its liabilities decreased. The risk associated with the Debt Office's guarantee commitment thus fell significantly since the valuation was carried out in 2000. The Debt Office stated in a communication to the Government in August 2003 that no further appropriations of subsidy funds from the central government budget need to be made during 2004. At year-end 2003, provisions for future losses of Venantius had been reduced to SEK 300 million.

Guarantees for Svensk-Danska broförbindelsen, SVEDAB

Before the new guarantee model was introduced, the National Rail Administration and National Road Administration issued a loan guarantee for SVEDAB's borrowing from the Debt Office and a capital coverage guarantee for SVEDAB. The Debt Office has sent a communication to the Government requesting that the loan guarantee will be cancelled and asking the Government to confirm that the capital coverage guarantee is exempted from the guarantee model and that the Debt Office's responsibility for it has thereby ceased.

Guarantee for Centre for Physics and Astronomy

In the spring of 2001, the Royal Institute of Technology and Stockholm University issued a state guarantee in

Guarantee commitments, 1999–2003, SEK million

Sector	1999	2000	2001	2002	2003
Infrastructure projects	31,010	32,480	34,073	34,496	40,467
Financing and properties	72,447	64,263	52,176	24,628	20,152
Pension obligations	23,494	23,791	23,151	16,853	10,927
International obligations	75,891	80,159	86,360	80,923	90,390
Insurance for airlines etc	–	–	42,137	–	–
Other commitments	2,596	1,051	892	888	1,680
Total	**205,438**	**201,744**	**238,789**	**157,788**	**163,616**

connection with the financing of the Centre for Physics and Astronomy which was not compatible with the guarantee model. A Government decision is expected shortly, under which aside from an administrative fee, the two institutions will pay an annual fee that will be placed in a fund to reduce the residual value risk to the state that will arise when their property financing expires.

New guarantee for Swedish Export Credit Corporation

In keeping with a decision of the Riksdag, the Swedish state has taken over the heavy engineering company ABB's minority shareholding in the Swedish Export Credit Corporation. On behalf of the Government, in December 2003 the Debt Office issued a guarantee fund of callable capital to the Export Credit Corporation in the amount of SEK 600 million, as a replacement for two earlier guarantee funds of SEK 300 million each issued by the Debt Office and ABB, respectively. At the same time a guarantee obligation from the Swedish Foreign Ministry, which was not compatible with the guarantee model, was withdrawn.

The Swedish state's claims

In 1998 the Debt Office took over more than a thousand recourse claims totalling SEK 330 million from the County Administrative Boards and the National Board of Fisheries. Since then, SEK 56 million in other claims have been added as a result of new indemnifications of agricultural and rural loan guarantees. Since 1998, SEK 37 million has been recovered and SEK 199 million has been written off. The portfolio of claims has now decreased to SEK 150 million. The remaining claims (about 550 altogether) are being actively pursued.

Loans with credit risks

Credit risk fee is not always charged

At the end of 2003, the Debt Office's loans outstanding with credit risks was SEK 8.6 billion, a decrease of SEK 1.5 billion. As with guarantees, loans may give rise to losses for the Swedish state and lead to a larger borrowing requirement. However, there is no framework for loans equivalent to the guarantee model that requires risk-based fees.

For years, the Debt Office has pointed out the importance of establishing a credit model that would ensure responsible management of loans from the state carrying credit risks.

Financing agreement with Saab in place

In September 2003, the Debt Office signed an agreement with the aerospace company Saab AB on partial financing of development costs for the fixed leading edge of the wing for the new Airbus 380 super jumbo jet. Repayment of this financing will depend on how many Airbus 380 aircraft are sold. The state's risk is thus closely connected to the future growth of civil aviation traffic, especially for large passenger aircraft.

Refinancing of the Arlanda Link

During the autumn of 2003, the former private owners sold all their shares in A-Train AB, which the Debt Office approved as a lender. Since it began service in 1999, the company's high-speed railway to Stockholm-Arlanda Airport has operated at a loss. In the judgement of the Debt Office, the prerequisites for repayment of the company's conditional loan, given by the state, have not deteriorated. On the contrary, the refinancing creates a certain respite for A-Train, since the company has been granted loans without amortisations.

Continued lending to rail companies

When the state enterprise Statens Järnvägar, SJ (Swedish State Railways) was transformed into several limited companies in 2001, the idea was that these companies would gradually shift from Debt Office to market borrowing. The ambition that all SJ borrowing at the Debt Office would be repaid by the end of 2003 was not fulfilled, so the borrowing limits were extended in time. One of the reasons was the economic problems of SJ AB, which also led to a capital contribution of SEK 1,555 million from the Swedish state during 2003.

Risk Management

The Government has stated that the Debt Office shall endeavour to achieve best market practices in risk management and ensure that its management of financial and administrative risks meets the requirements specified in legislation on financial service companies and the regulations and general advisories of the Financial Supervisory Authority.

The Board of the Debt Office establishes principles on how the debt management guidelines set by the Government shall be applied in its practical operations. A credit committee and an operational risk committee oversee the task of risk management in these two fields.

Operations in 2003

Market risks in active debt management

The VaR model's ability to forecast losses was evaluated (see page 15). This evaluation showed good agreement. According to the VaR model used by the Debt Office, an estimate is made that with 95 per cent probability, loss incurred will be less than a stated figure. When the model was evaluated, it turned out that the actual number of days with losses larger than forecasted only deviated by 0.2 per cent.

Credit risks in derivative operations

The Debt Office's credit risks in derivative operations are caused by changes in the market value of the swaps, forward contracts and options the Debt Office enters into. If the market value of these contracts develops favourably for the Debt Office, this leads to a claim against the counterparty, i.e. a credit risk exposure.

The Debt Office's policy for managing this type of credit risks is based on contractual structures for reducing credit risk, as well as limits related to exposure, expected risk of loss, counterparty ratings and maturity of transactions.

The most fundamental technique for contractually reducing credit risk is to enter into derivative transactions under a framework agreement. The Debt Office uses a framework agreement developed by the International Swap and Derivatives Association (ISDA), which enjoys backing in the legislation of most developed countries.

In order to manage credit risks efficiently and create more flexible transaction potential, during the past two years the Debt Office has sought to establish CSA agreements with its counterparties. At the same time, limits have been made less restrictive.

A Credit Support Annex (CSA) is an appendix to the ISDA agreement that establishes a system for collateral transfer between the parties in order to eliminate the exposure that arises in derivative transactions.

Fulfilment of goals

In its market and credit risk management of foreign currency debt, the Debt Office employs methods that meet market standards in the financial service sector. Continuity planning has improved by means of further enhancement of the emergency plan, improved fire safety and the development of operational agreements and backup procedures. The task of establishing a back-up operations site is underway.

The Debt Office fulfils the requirements specified in legislation on financial service companies and in the instructions and general advisories of the Financial Supervisory Authority. The overall assessment is that the Debt Office meets best market practices in financial risk management, but that some work remains concerning other risks.

Income statement

SEK million

	December 31, 2003	December 31, 2002
Operating income		
Income from appropriations	41,609	67,157
Income from guarantee issuance fees	293	126
Income from fees on deposits from and lending to government agencies etc	–	21
Income from fees and other compensation	0	1
Interest income, interest-bearing account etc	65	74
Total operating income	**41,968**	**67,379**
Operating expenses		
Financial expenses for central government debt management		
Interest expenses	–83,002	–124,841
Interest income	39,813	55,430
Issue premiums/discounts	3,432	7,502
Realised capital losses	–3,811	–4,594
Realised currency exchange gains/losses	–4,366	–6,650
Unrealised currency exchange gains/losses	18,465	31,463
Expired bonds, coupons and prizes reported as income	13	11
Commissions to banks etc	–156	–159
Total	**–29,611**	**–41,838**
Other operating expenses		
Employee expenses	–88	–80
Costs of premises	–17	–17
Reappraisals of guarantee claims	9	–3
Provisions for future guarantee losses	1,940	–3,857
Expenses for disbursement of guarantee subsidy	–1	–40
Other operative expenses	–181	–201
Depreciation	–5	–3
Total	**1,656**	**–4,201**
Total operating expenses	**–27,955**	**–46,039**
Revenue collection work		
Income from fees etc and other income not at disposal of agencies	17	
Income from revenue collection	3,300	20,000
Funds paid to the central government budget from revenue collection work	–3,317	–20,000
Total revenue collection work	**0**	**0**
Change in capital for the year	**14,012**	**21,339**

Balance sheet

SEK million

	December 31, 2003	December 31, 2002
ASSETS		
Intangible fixed assets	**1**	**–**
Capitalised development work expenditures	1	–
Tangible fixed assets	**14**	**9**
Machinery, equipment, fixtures etc	14	9
Financial fixed assets	**218,632**	**215,213**
Other long-term holdings of securities	6,369	19,623
Long-term receivables from other agencies	202,714	184,910
Other long-term receivables	9,548	10,680
Receivables	**6,063**	**7,961**
Accounts receivable	112	35
Receivables from other agencies	1,651	1,482
Other receivables	4,301	6,444
Cut-off items	**25,808**	**27,847**
Prepaid expenses	15,115	16,144
Miscellaneous accrued income	10,693	11,703
Settlement with the government	**1,066,338**	**1,025,344**
Settlement with the government	1,066,338	1,025,344
Short-term investments	**7,469**	**–**
Overnight borrowing	7,469	–
Cash, bank etc	**2,098**	**2,233**
Cash, bank etc	2,098	2,233
TOTAL ASSETS	**1,326,424**	**1,278,607**
CAPITAL AND LIABILITIES		
Agency capital	**–55,272**	**–70,004**
State capital	3,768	3,997
Change in capital brought forward	–73,053	–95,340
Change in capital according to income statement	14,012	21,339
Allocations	**3,402**	**5,342**
Provision for future guarantee losses	3,402	5,342
Central government debt	**1,228,835**	**1,204,228**
Borrowing in Swedish kronor	898,409	828,904
Borrowing in foreign currencies	330,426	375,324
Liabilities etc	**94,000**	**91,227**
Liabilities to other agencies	76,645	72,388
Trade creditors	23	19
Other liabilities	17,332	18,820
Cut-off items	**55,458**	**47,814**
Accrued expenses	30,801	31,728
Other deferred income	24,657	16,086
TOTAL CAPITAL AND LIABILITIES	**1,326 424**	**1,278,607**
Contingent liabilities		
Guarantee commitments without provisions for future guarantee losses	85,230	74,314
Debt instruments	7,382	7,256
Registered savings and lottery bonds	1	2

The Board

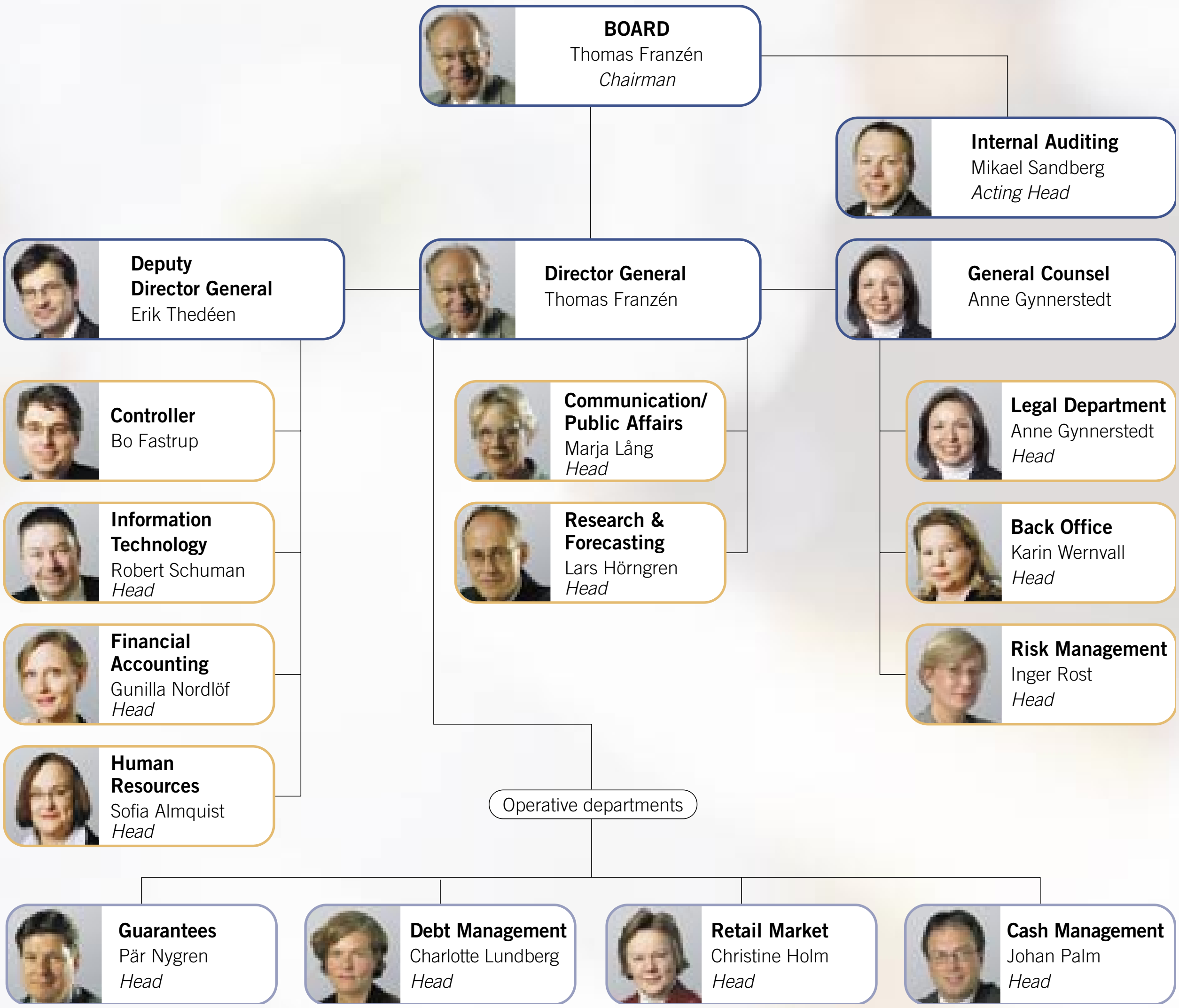
From the left: Ingemar Hansson, Marie Engström, Peter Englund, Inger Nordlander, Åsa Mindus Söderlund, Per-Olof Svensson. Thomas Franzén and Mikael Odenberg are missing from the photo.

Board of the Swedish National Debt Office
The Board of the Swedish National Debt Office consists of eight persons, of whom four shall be Members of Parliament. The Chairman is Thomas Franzén, Director General of the Debt Office. The others are Professor Peter Englund, Marie Engström (MP, Left Party), Director General Ingemar Hansson, Economist Åsa Mindus Söderlund, Inger Norlander (MP, Social Democratic Party), Mikael Odenberg (MP, Moderate Party) and Per-Olof Svensson (MP, Social Democratic Party).

Organisation and department heads

The Swedish National Debt Office had 145 employees at its office in central Stockholm on December 31, 2003. Their average age was 42 years. More than 60 per cent of employees had an academic degree. Half of the managers are women. Of all employees, 58 per cent are women and 42 per cent men. Absences due to illness totalled 3 per cent during 2003.

Professional development is important, since large and rapid changes are occurring in the financial service sector. During 2003 we initiated a project to achieve an organisation with a higher degree of management by objectives. We also documented our basic values.



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