RIKSGÄLDEN

21 February 2018

CENTRAL GOVERNMENT BORROWING

Forecast and analysis 2018:1

The Debt Office's assignment

The Debt Office is the Swedish government's financial manager. The mission includes central government borrowing and debt management. The aim is to do this at the lowest possible cost while avoiding excessive risk.

In *Central Government Borrowing – Forecast and Analysis*, which is usually published three times a year, the Debt Office presents forecasts for central government finances in the coming two years. On the basis of these forecasts, the Debt Office estimates how much the government needs to borrow and sets up a plan for borrowing which is also included in the report.

On the fifth working day of each month, the central government budget balance (the net of all incoming and outgoing payments) is published for the previous month in a press release. The outcome is compared with the forecast from *Central Government Borrowing – Forecast and Analysis* and any deviations are explained. In connection with the monthly outcome, the Debt Office also presents the debt development in the report Sweden's *Central Government Debt*.

Preface

In *Central Government Borrowing - forecast and analysis 2018:1* the Debt Office presents forecasts for central government finances and borrowing in 2018 up until 2019. An assessment of the economic development is given in the first section. The following section presents annual and monthly forecasts for the budget balance and the underlying analysis. These forecasts serve as the basis for borrowing, which is discussed in the last section of the report.

Hans Lindblad
Director General

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Summary

Continued strong growth of the Swedish economy contributes to the central government budget showing a surplus of SEK 80 billion this year and SEK 45 billion next year, according to the Debt Office's new forecast. The Debt Office is therefore reducing borrowing in government bonds to the lowest auction volume since 2007.

- Growth in Sweden is expected to remain high this year. Exports gain pace at the same time as both household consumption and investments make substantial contributions to GDP growth. Despite investments being high, unused resources continue to decease leading to the economy gradually slowing down next year. The forecast for GDP growth is 2.7 per cent in 2018 and 1.7 per cent in 2019.
- The labour market continues to be characterised by the fact that the group of people born abroad accounts for the main part of the increase in both employment and the labour force. Employment growth tails off as economic activity slows down, contributing to a levelling out of unemployment.
- The surplus in the central government budget is put at SEK 80 billion in 2018. This is an increase of SEK 33 billion from the previous forecast. The main reason for the difference is that the Debt Office expects a greater inflow to tax accounts in 2018 that does not relate to taxes or fees, i.e. pure capital investments. In addition, a slightly stronger economic situation contributes to greater growth of households' capital income and corporate profits than in the previous forecast.
- For 2019 the budget balance is expected to be SEK 45 billion, which is a decrease of SEK 10 billion from the forecast made on October. The main reason is an estimated turn-round in the flow of capital investments in tax accounts on account of expectations of rising market interest rates.
- Central government net lending, which is not affected by capital investments, is expected to be 1.0 per cent of GDP in 2018 and 0.9 per cent in 2019.
- The central government debt is estimated at SEK 1 247 billion at the end of 2018 and 1 151 billion at the end of 2019. This corresponds to 26 and 23 per cent of GDP.
- The Debt Office is decreasing borrowing in government bonds from SEK 40 billion to SEK 30 billion as an annual rate by reducing the issue volume from SEK 2 billion to SEK 1.5 billion as of March. This is the lowest auction volume since 2007. Borrowing in the other types of debt is kept unchanged.
- The Debt Office's assessment is that a further reduction of borrowing in government bonds is not appropriate since it would risk leading to higher borrowing costs and poorer borrowing preparedness in the longer term.
- Liquidity has deteriorated gradually in the government bond market, one sign being a marked increase in demand for the Debt Office's standing repo facility in the second half of the year. In view of this the Debt Office considers that its standing repo facility is more important than ever.
- The Debt Office expects to have to handle cash surpluses in liquidity management for a longer period than normal. In the longer term the cash surplus will decrease as outstanding bonds mature.

Swedish economy close to a cyclical peak

Growth in Sweden is expected to remain high this year. Exports gain pace at the same time as both household consumption and investments make substantial contributions to GDP growth. One important explanation for the slowdown in growth next year is a clear slowdown of housing investments, which decrease after several years of high growth. The forecast for GDP growth is 2.7 per cent in 2018 and 1.7 per cent in 2019. The labour market continues to be characterised by the fact that the group of people born abroad accounts for the main part of the increase in both employment and the labour force. Employment growth tails off as economic activity slackens, contributing to a levelling out of unemployment.[1]

The international economy continues to gain strength

International developments continue to be positive for the Swedish economy. The economic situation both in the US and the euro area and in the emerging economies gradually getting stronger. Even though the recent turbulence in stock markets is striking, financial markets have generally been characterised by a continuation of low key interest rates, low risk premiums and low volatility.

The situation in financial markets continues to be favourable for the real economy.
In broad outline the situation in financial markets is roughly the same as in conjunction with the Debt Office's previous forecast in October last year. Developments are still characterised by expansive monetary policy, which has contributed greatly to the economic recovery of the world economy after the financial crisis and the euro crisis. Monetary policy is now slowly becoming less expansive as the global economy strengthens. However, central banks are still in different phases regarding interest rate increases and the winding down of asset purchases. The Federal Reserve in the US has come furthest and raised its key interest rate for the fifth time in December, while the Bank of England has only raised its interest rate once, see figure 1. In contrast, the European Central Bank has still to increase its interest rates, and market expectations are that a first rate increase will not come until next year. From a global perspective, it is assumed that monetary policy will remain expansive in both 2018 and 2019.

Better macroeconomic prospects and rising corporate profits have led to a strong performance on stock exchanges in several parts of the world in the past year. Interest rate markets are still characterised by low rates and risk premiums, even though yields on ten-year government bonds have recently risen in several countries, partly as a result of expectations that key interest rates will

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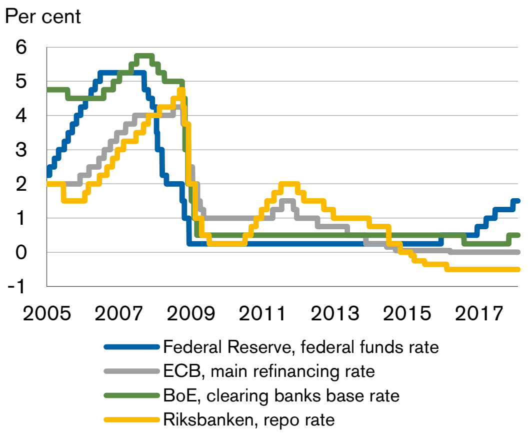
[1] *Information until and including 24 January has been taken into account in work on the forecast.*

rise more rapidly. However, in the low-interest environment that has prevailed in recent years, the probability has increased that imbalances have been built up in various asset markets.

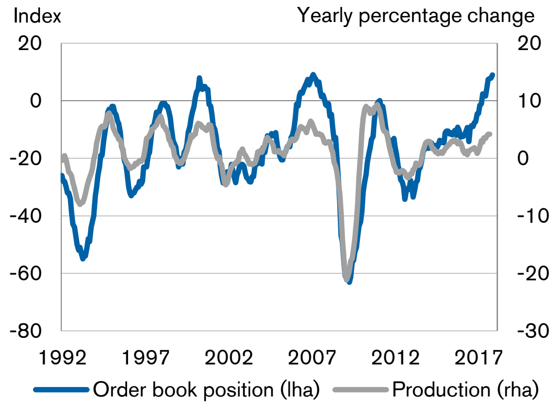
In Sweden, too, financial conditions remain favourable for the real economy, despite the recent turbulence in the stock market. Risk premiums in the interest rate market are generally low, as are the interest rates met by households and businesses. There are now signs that housing prices stabilised in January after falling for several months in a row in autumn 2017. However, single statistical outcomes should be interpreted with caution, for example on account of strong seasonal variations.

Figure 1. International policy rates



Sources: National sources.

Figure 2. Manufacturing industry in the euro area



Sources: DG ECFIN and Eurostat.

Moderate but increasing international growth

International growth, measured as trade-weighted GDP, has grown at a rising pace for a couple of years.[2] The global economic improvement is wide and both developed and emerging economies are growing. But even though growth is now higher than its historical average since 1980, it is still relatively moderate. Sweden has therefore not benefited from the same pull from the international economy in this economic upturn as at previous cyclical peaks.

The US economy has performed slightly better than expected since the Debt Office's previous forecast. In broad terms, however, the overall picture is the same as before with GDP growth of just over 2 per cent, unemployment of just over 4 per cent and relatively low increases in both prices and pay. But the outcome for pay increases in January was higher than expected by the market, and this contributed to the turbulence on stock exchanges at the start of February. Both households and consumers have become increasingly positive and the confidence indicators for both these groups are at high levels, in line with the highest figures recorded in the past 30-40 years. However, the growth of household consumption is relatively moderate and there is some discrepancy between the high confidence expressed by consumers and their actual consumption. Similar differences between

[2] International growth is weighted by the size of Swedish trade with each country, using total competitiveness weights (TCW).

confidence indicators and actual outcomes are common in a cyclical upturn. The Debt Office's forecast of GDP in the US is 2.6 per cent for 2018 and 2.3 per cent for 2019, which is an upward revision of 0.5 and 0.3 percentage points respectively.

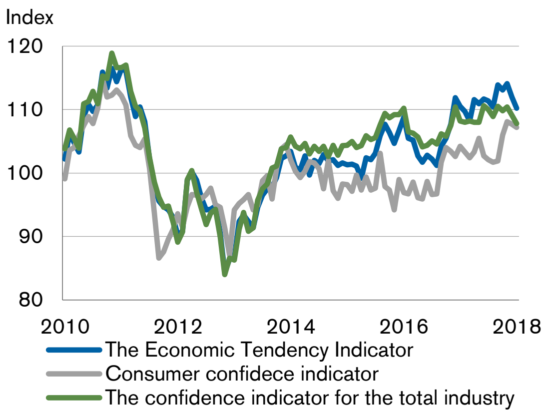
GDP growth in the euro area is continuing to perform slightly stronger than expected. Growth there is spread evenly and, at present, the four big economies – Germany, France, Spain and Italy – are all growing at an annual rate of between just under 2 and just over 3 percent. As in the US, both households and businesses are increasingly positive and confidence indicators are at historically high levels. From a Swedish perspective it is important that demand for investment goods increases and that the economic situation in industry in the euro area strengthens. Both order bookings and production in manufacturing show a clear upward trend, even though growth is moderate from a historical perspective, see figure 2. The Debt Office's forecast of GDP growth in the euro area is 2.3 per cent for 2018 and 1.9 per cent for 2019, which is an upward revision of 0.4 percentage points for 2018.

Continued good growth of Swedish GDP in next few quarters

Growth in Sweden was good in 2017. The main reason is strong investment growth, but household consumption also made a considerable contribution to GDP growth. The high growth means that the unused resources in the economy are decreasing and the Swedish economy is judged to be close to a turnaround. Resource utilisation measured in terms of GDP is judged to be higher than normal and the strained situation is also seen in the labour market. The proportion of businesses that state that they are experiencing a shortage of labour is still high and the difference between the actual and potential number of hours worked has been rising for a period. At the same time, the labour force is increasing a rapid pace and pay increases are relatively low, which may indicate that resource utilisation is being overestimated.

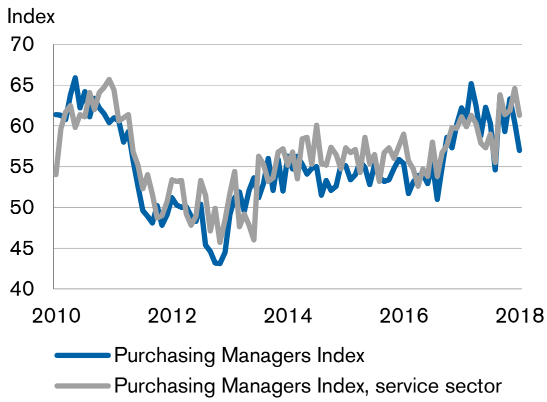
In the third quarter of last year GDP grew by 0.8 per cent compared with the preceding quarter. Investment growth remained high. Housing investments increased, but more slowly than before, at the same time as other investments in the business sector showed sharp growth. After strong export growth in the second quarter, exports grew more slowly in the third quarter. Along with high import growth, this meant that foreign trade made a negative contribution to GDP. In all, the outcome for GDP was in line with the Debt Office's October forecast. But investment growth was considerably stronger than expected while exports performed more weakly than expected.

Figure 3. Confidence indicators for households and businesses



Note: The Economic Tendency Indicator has been standardised to mean 100 and standard deviation 10.
Source: National Institute of Economic Research.

Figure 4. Purchasing Managers Index, total and for the service sector



Note: An index number over 50 indicates growth while an index number below 50 indicates decline.
Source: Swedbank/Silf.

At present the mood in the Swedish economy is good and confidence is high among both households and businesses. While the Economic Tendency Indicator of the National Institute of Economic Research (NIER) did fall in both December and January, the level is high and continues to indicate that the situation in the Swedish economy is brighter than normal, see diagram 3. Confidence is high in all industries in the business sector, and especially in manufacturing and construction and civil engineering. More businesses than normal state that they are experiencing a shortage of labour, and hiring plans in the business sector point to strong employment growth in the coming months. The purchasing managers' indexes for both the economy as a whole and the services sector are also at a high level. These indexes were well above 50, the level that indicates growth in the economy, throughout all of last year but fell back in the most recent measurement, see figure 4.

The Debt Office's assessment is that GDP growth will continue to be good over the next six months, see figure 5. However, as of the second half of 2018 growth will slow down, partly as a result of decreasing housing investments, and GDP is expected to grow by 2.7 per cent in 2018 and by 1.7 per cent in 2019, see table 1. As a result of higher investments and stronger export growth, GDP growth in 2018 has been revised upwards by 0.2 percentage points compared with the forecast from October last year, see table 2. For 2019 the forecast is unchanged.

Table 1. GDP and its components, constant prices, forecast

Percentage change[1]	2016	2017	2018	2019
GDP	3.2	2.5	2.7	1.7
Household consumption	2.2	2.4	2.2	1.9
General gov't consumption	3.1	0.5	1.2	1.0
Gross fixed cap. formation	5.6	7.3	4.3	1.3
Change in inventories[2]	0.0	-0.1	0.0	0.0
Exports	3.3	3.6	4.8	3.6
Imports	3.4	5.0	4.6	3.4
Net exports[2]	0.1	-0.4	0.3	0.2
GDP (calendar adjusted.)	3.0	2.7	2.8	1.7

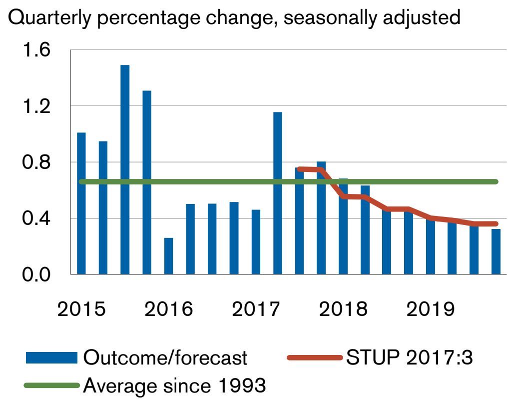
Table 2. GDP and its components, revisions compared to previous forecast

Percentage change	2016	2017	2018	2019
GDP	-0.1	-0.3	0.2	0.0
Household consumption	0.0	0.2	0.0	0.1
General gov't consumption	-0.3	0.3	-0.1	0.1
Gross fixed cap. formation	-0.1	0.2	1.1	-0.7
Change in inventories[2]	0.0	0.0	0.0	0.0
Exports	-0.1	-0.1	0.5	0.3
Imports	-0.1	1.1	0.7	0.0
Net exports[2]	0.0	-0.5	-0.1	0.1
GDP (calendar adjusted.)	-0.1	-0.3	0.2	0.0

[1] Actual change compared with previous year.
[2] Change as percentage of GDP previous year.
Sources: Statistics Sweden and the Debt Office.

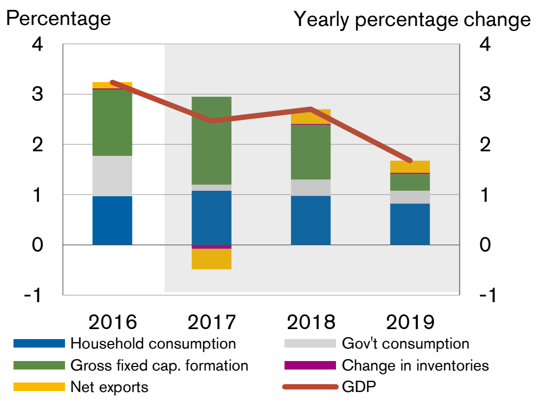
The largest contribution to GDP growth this year again comes from investments, even though the contribution is lower than last year, see figure 6. Good growth of household consumption still makes a large contribution to GDP and stronger export growth means that the contribution of foreign trade to GDP is positive.

Figure 5. GDP, outcome and forecast



Sources: Statistics Sweden and the Debt Office.

Figure 6. Contribution to GDP



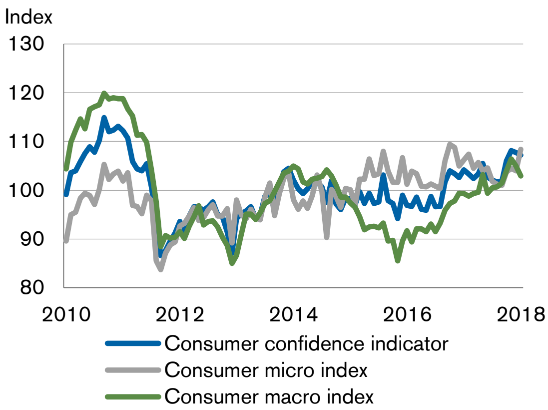
Sources: Statistics Sweden and the Debt Office.

Continued good consumption growth among households

The growth of household consumption has been high in the past year, and this has made a considerable contribution to the good GDP growth. However, in the third quarter there was a slight decline in consumption growth.

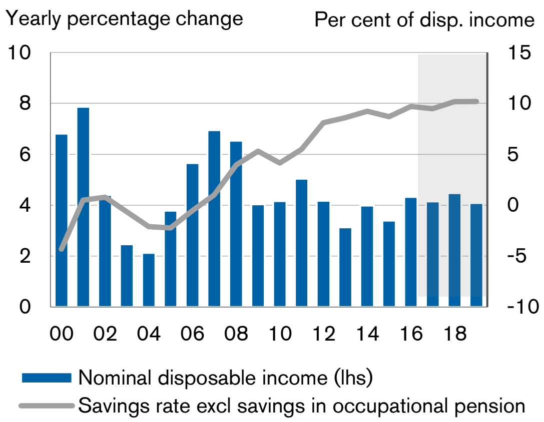
The household confidence indicator shows a better mood that normal. Even though this indicator has fallen in the past two months, it is at a high level after having recorded a relatively large rise in the second half of 2017. Households take a brighter than normal view of their own and of Sweden's finances, see figure 7. Moreover, their view of their own finances improved in the latest confidence survey.

Figure 7. Consumer confidence indicator incl. micro and macro index



Source: National Institute of Economic Research.

Figure 8. Household's nominal disposable income



Source: Statistics Sweden and the Debt Office.

Compared with the last five years, household disposable income is judged to show a relatively large increase in nominal terms in 2018. The reasons include strong employment growth and fiscal policy measures in the form of lower tax for pensioners and higher child allowances, see figure 8. In combination with high household confidence this means that household consumption is also expected to rise at a good rate in the first half of the year. The decline in housing prices in autumn 2017 is not expected to have any clear effects on household consumption. When the economy weakens, the growth of consumption also declines. Higher interest rates mean that household disposable income grows more slowly, and this also contributes to the weakening of consumption. The Debt Office's view of consumption growth is virtually unchanged from the October forecast, and consumption is expected to grow by 2.2 per cent in 2018 and 1.9 per cent in 2019.

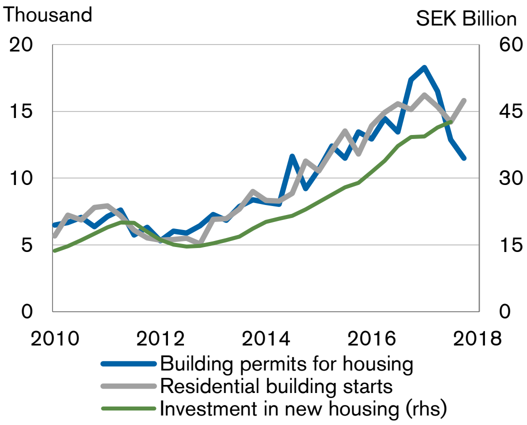
Fiscal policy and demography drive public consumption in 2018

High expenditure for migration and integration have resulted in a rapid increase in public consumption in recent years. As the costs of refugee reception have decreased, the growth of public consumption has weakened considerably. In 2017 public consumption is expected to grow by 0.5 per cent, which can be compared with 3.1 per cent in 2016.

Demographic developments, with more young and older people in the economy, mean that demand for welfare services is expected to increase in the coming years and public consumption is expected to rise faster again this year and next year. This year fiscal policy measures contribute to maintaining consumption growth. Public consumption is expected to grow by 1.2 per cent in 2018 and 1.0 per cent in 2019. The revisions from the October forecast are small.

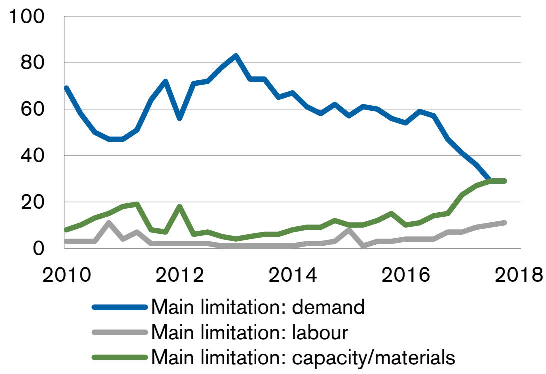
Housing investments are expected to decrease this year and next year.
The high growth of investments has been one of the foremost drivers of GDP development in recent years. It is mainly housing investments that have increased, and today they are at a high level from a historical perspective. In 2017, the number of housing starts has stopped growing, se figure 9. The statistics of housing and building have also been revised downward since the Debt Office's previous forecast and housing investments in 2017 is now expected to be lower than before. In combination with fewer building permits and the lower housing prices in autumn last year, this affects the forecast for housing investments, which are now expected to decrease in both 2018 and 2019, even though they remain at a high level.

Figure 9. Building permits, building starts and investment in new housing



Note: Own seasonal adjustment.
Source: Statistics Sweden and the Debt Office.

Figure 10. Main limitation to production



Source: National Institute of Economic Research.

Other business sector investments grew strongly throughout 2017, especially in the case of service producers and in manufacturing industry and the energy industry. Capacity utilisation in industry is high and has increased in the past two years. More manufacturing industry representatives than before give a shortage of plant and machinery capacity as the main obstacle to increasing production, see figure 10. Investments in plant and machinery have been relatively low since the financial crisis and there is an investment need in industry. Along with rising international demand for investment goods this means that business sector investments, excluding housing, are expected to increase faster than in previous forecasts.

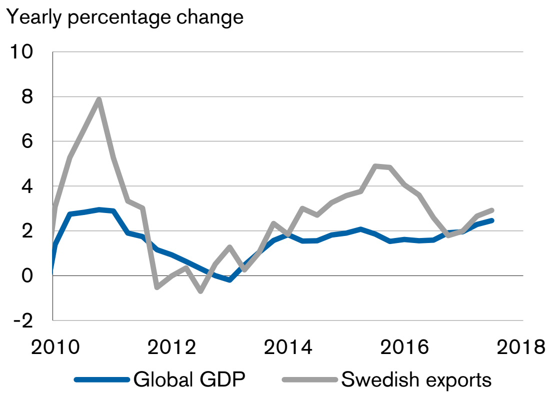
The higher investments in the business sector do not fully offset the decrease in housing investments in 2018 and 2019 and aggregate investment growth has been revised downwards in the forecast period. However, the strong outcome for the third quarter has led to an upward revision of growth for the whole of 2018 compared with the October forecast. Investments are judged to have grown by 7.3 per cent in 2017, which is the highest rate of growth since the financial crisis. In 2018 and 2019 they are expected to grow by 4.3 per cent and 1.3 per cent respectively.

Higher international growth contributes to good export performance

After performing strongly in the second quarter of last year, exports grew much more slowly in the third quarter. At the same time imports increased strongly and foreign trade made a negative contribution to GDP growth.

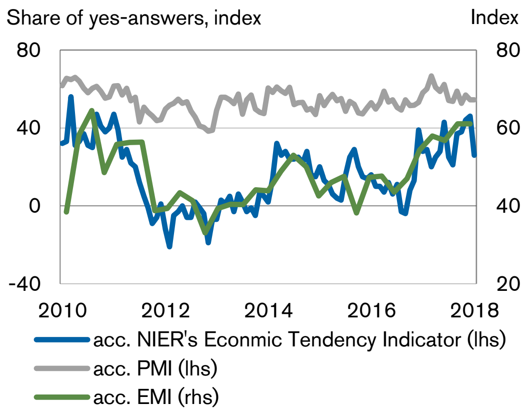
The prospects for rising exports in the future are good. International growth has increased and has also grown more strongly than expected, see figure 11. International demand for investment goods has risen, and this favours Sweden's export industry. The mood in the export industry is good. For example, Business Sweden's export managers index was above its historical mean for the whole of 2017, indicating optimism among export companies. The rating of export order received is higher than normal within the framework of both the export managers index and the purchasing managers index, see figure 12. However, the expectations of export order growth in manufacturing industry decreased in the NIER's latest business confidence survey. Today they are at a historically normal level after having been high at the end of 2017.

Figure 11. Global growth and Swedish exports



Note: Global GDP is TCW-weighted.
Sources: Statistics Sweden, national sources and the Debt Office.

Figure 12. The rating of export order



Note: Global GDP is TCW-weighted.
Sources: Statistics Sweden, national sources and the Debt Office.

The forecast for exports has been revised upwards from the October forecast and they are now expected to grow by 4.8 per cent his year and 3.6 per cent next year. This is an increase of 0.5 percentage points for 2018 and 0.3 percentage points for 2019.

Imports grew strongly in the third quarter of last year and imports for the whole of 2017 have been revised upwards. Imports are also expected to continue to grow at a relatively high rate in the first half of 2018. Since housing investments have a lower import content than other investments in the business sector, this change in the composition of investments means that the level of imports is maintained even though investment growth has been revised downwards. As investments and household consumption weaken, import growth also declines in the second half of this year and next year. Imports are expected to grow by 4.6 per cent in 2018 and 3.4 per cent in 2019. For 2018 the forecast has been revised upwards by 0.7 percentage points. The forecast for 2019 is unchanged. However, the strong growth of exports means that the contribution from foreign trade is expected to be positive.

Employment grows more slowly and unemployment levels out

The labour market has performed in line with the Debt Office's previous forecast, with annual growth in employment and the labour force of around 2 per cent. The even and high growth of both employment and the labour force over a long period of time is a break with the pattern of the last two economic upturns, when growth accelerated rapidly instead for a shorter period of time. One important reason for the trend in recent years is migration, which has contributed to the fastest increase in the population of working age (15-74 years) for more than 80 years.

The labour force is growing as a result of migration.

The labour force also continued to grow rapidly in the second half of 2017. In all, this means that its growth in 2017 was 2 per cent, which is the fastest growth of the labour force since 2001, when official statistics for the 15–74 age group start. One factor making a strong contribution to this trend is that in recent years the population has grown faster than for 150 years, on account of migration. The share of the population that is of working age has also been growing faster than for a very long time. The group of people born abroad has a significantly higher share in the 16-64 age group (just under 80 per cent) compared with the group of people born in Sweden (just under 60 per cent). The total number of new residence permits issued is expected to stabilise at around 100 000 per year in the future, after the effects of the large number of asylum seekers who came in autumn 2015 has subsided, see figure 13.[3] At the same time, the group of people born in Sweden of working age will decrease slightly, which means that, in the longer term, the labour force as a whole is expected to grow roughly in line with its historical average. The Debt Office's forecast of the growth of the labour force is 1.2 per cent for 2018 and 0.8 per cent for 2019, which is an upward revision of 0.1 percentage point for 2018.

High but declining employment growth among people born abroad

Employment grew rapidly in the second half of 2017, even though its growth decreased compared with the very high growth around the end of 2016 and start of 2017. A large part of the increase in employment in recent years has been among people born abroad. This is also the group where the slowdown in employment is clearest, even though the slowdown comes from high growth figures. For a couple of months, indicators of aggregate employment have been pointing to a continuing weakening of employment growth. For example, the index for employment in the purchasing managers index has shown a clear fall. Taken together, the outcome and indicators point to a continuing slight slowdown of employment in the future. The picture of such a trend is supported by short-term econometric models. The forecast is unchanged from the previous report and employment is expected to grow by 1.2 per cent in 2018 and 0.6 per cent in 2019.

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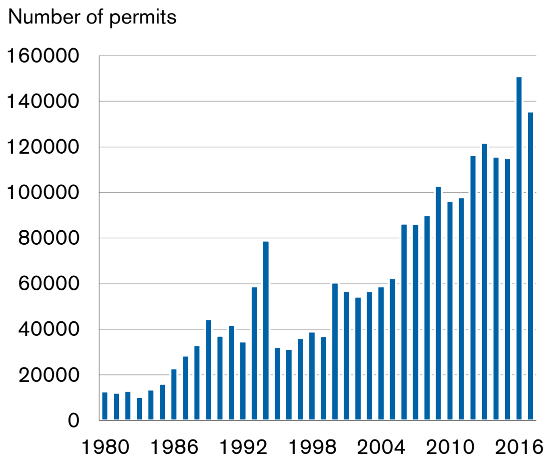
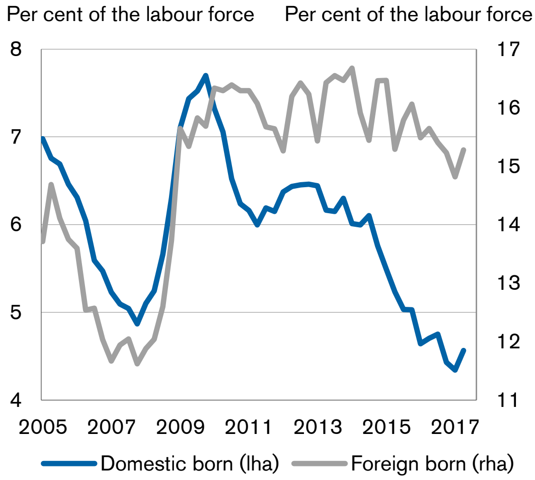
[3] The overall effect on the population and the labour force is also affected by what proportion of the total receives permanent residence permits and how big a part of the population chooses to move from Sweden. However, these two parts have not varied as much over time as in-migration to Sweden has.

Figure 13. Number of permits, total 1980-2017



Source: Swedish Migration Agency.

Figure 14. Unemployment for domestic born and foreign born



Source: Statistics Sweden.

Unemployment is levelling out

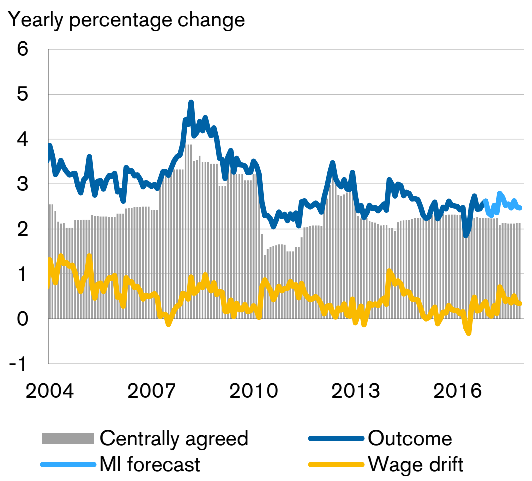
Unemployment has fallen for several years in a row, but has been relatively constant in the past year. However, unemployment among people born in Sweden and people born abroad has developed very differently in the past ten years, see figure 14. Among people born abroad it has fallen relatively slowly since both employment and the labour force have grown rapidly. Despite the much more moderate employment increase among people born in Sweden, unemployment for this group has fallen since the labour force has been largely constant in the past five years. The forecast is that employment will grow more slowly than the labour force in the future, as a result of which unemployment will level out in the coming year and rise slightly at the end of the forecast period. Unemployment is expected to be 6.6 per cent in 2018 and 6.8 per cent in 2019, which is a downward revision of 0.1 percentage point for 2018.

Moderate upward pressure on wages and prices continues

The outcomes of short-term wage statistics in recent months, point to a continuation of lower and lower increases in pay. However, the Swedish National Mediation Office's short-term wage statistics are preliminary, and their forecast of the definitive outcome indicates that rates of pay rises have begun to increase. This is in line with the development expected in the Debt Office's previous forecast and with the picture of pay growth given by pay according to the National Accounts (NA). However, wage drift, i.e. pay increases over and above central agreements, is moderate against the background of the strong performance of the economy in general and the labour market in particular, see figure 15. As the other revisions of the macro forecast are small and the outcome for pay is in line with expectations, the revisions of the pay forecast are marginal. The Debt Office's assessment is that NA pay will grow by 3.5 per cent in 2018 and 3.4 per cent in 2019.

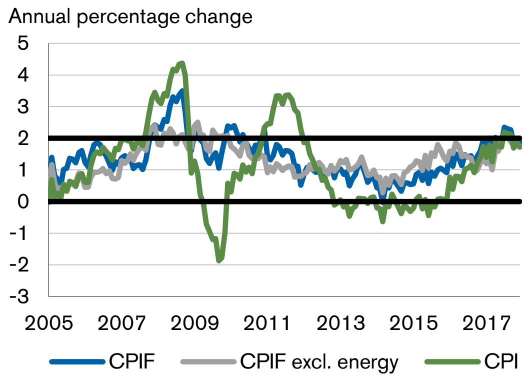
The aggregate effects of the revisions for the labour market and pay mean that the forecast of payroll growth is virtually unchanged. In line with historical patterns it is expected to grow at roughly the same rate as GDP in current prices. The forecast is that the payroll will grow by 4.7 per cent in 2018 and 4.2 per cent in 2019.

Figure 15. Central agreements, wage drift and total wage increases for the total economy acc. to the short-term wage statistics



Source: Swedish National Mediation Office.

Figure 16. Inflation rate, different measures



Source: Statistics Sweden.

Inflation measured as CPIF averaged 1.9 per cent in 2017 and has continued to be about 2 per cent in recent months, see figure 16.

The high resource utilisation in the Swedish economy during the forecast period is assumed to lead, with some lag, to higher pay increases. In addition, companies will have greater possibilities of increasing their prices. There are, however, few indications that inflation is going to rise sharply. Companies' inflation expectations in a one-year perspective are relatively low according to the NIER, and model estimates indicate falling rather than rising inflation. The expectations of money market participants also point, according to the survey company Prospera, to the krona strengthening as the Riksbank is expected to start increasing the repo rate, which would then have a dampening effect on the inflationary pressure. The Debt Office's forecast is that CPIF inflation will average 1.9 per cent in both 2018 and 2019.

Table 3. Key numbers labour market, prices and wages

Percentage change	2016	2017	2018	2019
Labour force	1.0	2.0 (1.9)	1.2 (1.3)	0.8 (0.8)
Employment	1.5	2.3 (2.3)	1.2 (1.2)	0.6 (0.6)
Unemployment[1]	6.9	6.7 (6.6)	6.6 (6.7)	6.8 (6.8)
CPIF	1.4	2.0 (2.0)	1.9 (1.8)	1.9 (1.9)
Hourly wage (NA)	2.2	3.3 (3.4)	3.5 (3.5)	3.4 (3.4)
Wage sum	4.9	4.9 (4.8)	4.7 (4.7)	4.3 (4.2)

[1] Percent of the labour force

Balanced risks but greater uncertainty surrounding the Swedish housing market

The risk picture is still characterised by difficulties in forecasting an economic turnaround. Economic turnarounds are not normally characterised by a slow weakening of growth and a return to an average level. Instead the upturn is often strong and the downturn faster and deeper than foreseen by forecasts. However, the present economic upturn has been more long-lasting than normal, especially regarding employment growth, which has been sustained for a longer period of time.

Some of the international uncertainty concerns structural challenges in the euro area that have long been under discussion, for example how the UK's exit from the EU will be put into effect and how the bad loans held by European banks will affect economic developments in general. In the short term it is possible that growth internationally, and in Europe in particular, will be stronger than expected. Indicators point to a good situation for industry with well-filled order books and what appears to be a pent-up investment need. In addition to the possibility of stronger GDP growth in the euro area, such a development might also put further upward pressure on pay and, ultimately, also on inflation and interest rates. For Sweden, this could lead to stronger growth of exports and investments and impulses for faster growth of pay and prices.

In autumn last year several signals came of a weakening of the housing market, with lower housing prices and a levelling out of housing starts. In addition, the number of building permits fell the autumn, which taken together is an explanation of why housing investments are now expected to decrease this year and next year. In recent years rising housing investments have been the strongest factor contributing to the high growth of GDP. There is great uncertainty about what will happen to both housing construction and housing prices in the immediate future. A deep and prolonged fall in construction and prices could affect both investments and consumers. If households' wealth decreases and their level of borrowing increases, the result may be that they choose to reduce their cons

Larger surplus in central government budget in 2018

The surplus in the central government budget is expected to be at SEK 80 billion in 2018 and SEK 45 billion in 2019. This is an increase of SEK 33 billon for 2018 and a decrease of SEK 10 billion for 2019 compared with the October forecast.[4] Only a small part of these changes is due to macroeconomic factors. Instead most of them are explained by changes made to assessments regarding capital investments in tax accounts. Central government net lending, which is not affected by capital investments, is expected to be 1.1 per cent of GDP in 2018 and 1.0 per cent in 2019.

Budget balance higher in 2018, but lower in 2019

As a result of a slightly stronger economic situation the capital income of companies and private individuals grows more than in the previous forecast. But the Debt Office also expects a greater inflow to tax accounts in 2018 that does not relate to taxes or contributions, i.e. pure capital investments.

In addition, higher dividends on state-owned shares, the sale of Apoteksbolaget AB and a transfer from the Swedish Export Credit Agency's credit reserve to an account at the Debt Office have a positive effect on the budget balance. Moreover, expenditure in social insurance decreases, mainly on account of lower expenditure for sickness benefit.

The budget balance decreases by SEK 35 billion between 2018 and 2019. A weakening of the economy in 2019 means that tax income will grow more slowly, but the change between these years is mainly due to a turnaround in the flow of capital investments in tax accounts. The Debt Office's assessment is that in the second half of 2019 rising market interest rates will mean that it is no longer attractive to invest capital in tax accounts. This means that an inflow of capital investments to tax accounts in 2018 is expected to turn into an outflow in 2019. The difference between the years is estimated at SEK 36 billion. For detailed information about capital investments in tax accounts, see page 20.

As in the previous forecast the Debt Office assumes that fiscal policy reforms will have a negative impact on the budget balance of SEK 15 billion for 2019. The Debt Office makes no assessment of whether this will affect expenditure or income.

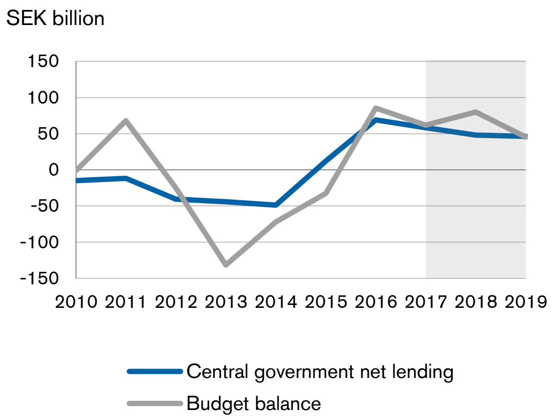
[4] *Information until and including 8 February has been taken into account in the forecast.*

Table 1. Budget balance forecast

SEK billion	2017	2018	2019
Primary balance	**69**	**95**	**67**
SNDO Net lending	**3**	**-2**	**1**
of which on-lending	*-4*	*-9*	*5*
Interest payments	**-10**	**-13**	**-22**
Budget balance	62	80	45

Note: Budget balance is equal to net borrowing requirement with opposite sign

Figure 1. Central government net lending and budget balance



Strong outcome in 2017

The outcome figure for the central government budget in 2017 was SEK 62 billion. The strength of the economy meant that tax income remained high. Drivers included rising employment and high investments in housing. Other factors contributing to the budget surplus were falling social insurance expenditure and moderate expenditure growth in other areas compared with 2016. Compared with 2016 the budget surplus decreased by SEK 24 billion in 2017. One reason was that tax income in 2016 was greatly affected by capital investments in tax accounts. In all, central government tax income in 2017 was virtually unchanged compared with 2016.

The Debt Office made the assessment that in 2016 large deposits were made in tax accounts that did not refer to taxes or contributions. The reason was that the interest rate obtained on tax accounts was high compared with alternative investments with the same low risk. In its forecasts in 2017 the Debt Office assessed that these deposits would decrease slightly when the interest rate on tax accounts was reduced to zero per cent on 1 January 2017. Instead the balance in tax accounts increased by approximately SEK 10 billion.

It is not possible to be exact about the scale of capital investments in tax accounts since it is up to every company and private individual to determine what size of extra tax payments they want to make. So this is a matter of rough assessments based on the development of tax bases and balances in tax accounts. The Debt Office's assessment is that at the end of 2017, despite zero interest, there was about SEK 60 billion in tax accounts that did not relate to taxes and contributions.

Outcomes and forecast changes since October

The budget balance in 2018 increases by SEK 33 billion to SEK 80 billion compared with the previous forecast. This is mainly because tax income is estimated to be SEK 30 billion higher. Next year the budget balance is expected to be SEK 45 billion, which is SEK 10 billion lower than in the previous forecast.

Table 2. The largest forecast changes

SEK billion	2018	2019
Forecast October 2017	47	55
Primary balance	**31**	**-10**
Of which:		
Tax income	30	-6
Dividends	2	3
Government grants to local governments	0	0
Labour market	-1	0
Social insurance	3	4
Migration	1	0
International aid	0	0
Other	-5	-11
SNDO Net lending	**4**	**2**
Of which:		
On-lending	0	2
Interest payments	**-1**	**-2**
Forecast February 2018	80	45

Note: The table shows changes in terms of budget balance. A positive amount means that the budget balance improves and vice versa.

Deviations since the previous forecast

Monthly outcomes for the budget balance have been much stronger than expected since the previous forecast. The total deviation from October to January was SEK 31 billion and the great bulk of it is due to higher tax income. A small part of it can be explained by macroeconomic factors. Tax on consumption and tax on corporate profits have been slightly higher than estimated, and payroll growth is marginally higher than forecast as a result of the strong performance of the labour market.

Even though these tax bases have grown slightly better than forecast, this can only explain a small part of the higher tax income. Instead, the Debt Office's assessment is that the bulk of it can be explained by a new payment pattern and higher capital investments in tax accounts. The unusual interest rate situation has meant that there are incentives to make early payments of tax, especially for legal persons. This has led to certain adjustments to the monthly distribution in the forecast of tax income in 2018 and 2019. But it has not affected the level of the whole-year forecasts.

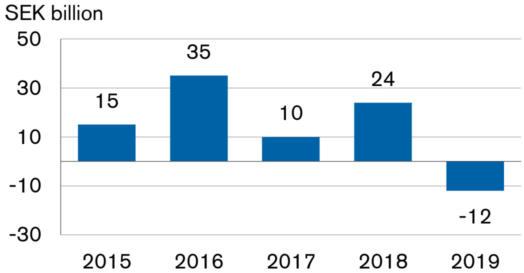
Capital investments in tax accounts increase in 2018, but decrease in 2019.
The inflow of payments to tax accounts that are not related to taxes or contributions has increased more than previously assessed by the Debt Office. Ahead of 2017 the Debt Office expected that excess deposits would decrease by just over SEK 10 billion. Instead, the total balance increased by around SEK 10 billion, see figure 2. This is chiefly because companies have deposited more money than expected. Households, on the other hand, have reduced their deposits and their tax account balance is probably back at close to normal levels.

The incentives for companies to deposit money in tax accounts are greater than for private individuals. The risk of deposit money in tax accounts is the same as of buying T-bills but the interest rate on tax accounts is higher, even though it is zero. Depositing money in and withdrawing money from tax accounts is a relatively quick process. In practice it functions like a bank account with an unlimited deposit guarantee from central government. A more relevant interest rate with which to compare the tax account interest rate is three-month Stibor. As long as Stibor is below zero, and the conditions regarding tax accounts does not change, the Debt Office makes the assessment that investments by companies will continue. For 2018 the Debt Office expects deposits from companies to total SEK 24 billion, which is SEK 12 billion more than in the previous forecast.

As of the end of this year and during next year market participants expect cautious interest rate increases by the Riksbank. One way of reading these expectations is to look at forward contracts for Stibor. According to these Stibor will pass zero per cent and approach 0.25 per cent during the second half of 2019. This should mean that the capital investments start to decrease. The Debt Office's assessment is that withdrawals of SEK 12 billion will be made in the second half of 2019. The previous forecast was that the deposits would be unchanged in 2019.

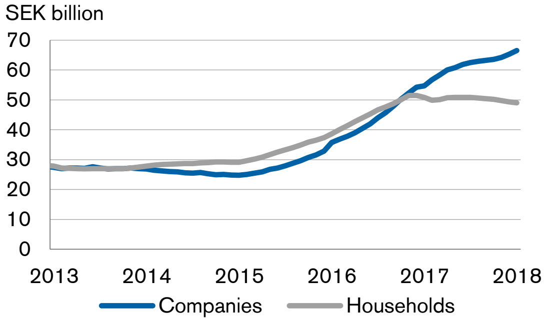
The assessment both of what will happen to interest rates and of how they will affect deposits in tax accounts are, of course, very uncertain. A faster increase in interest rates could result in earlier and much greater withdrawals, while unchanged interest rates would lead to further deposits by companies.

Figure 2. The Debt office´s assessment of excess deposits in tax accounts



Note: The figure shows the net of excess deposits.
Source: Statistics Sweden, Swedish tax agency, SNDO

Figure 3. Balance in tax accounts, 12 month moving average



Higher income from corporate taxes

Central government income from corporate taxes has been revised upwards by SEK 4 billion in 2018 and SEK 2 billion in 2019, compared with the October forecast, see table 3.

The strong growth of the Swedish economy has resulted in good profit growth in the business sector. Domestic demand has grown strongly for a long time, driven by high investments and by consumption. The international recovery, not least in the EU, is now estimated to be somewhat stronger than previously estimated, which will also lead to rising demand for export companies. This bright picture is supported by forward indicators, where, for example, the export managers index, the purchasing manager's index and the NIER's confidence survey are all at levels above their historical average. This strengthens the picture of good profit growth for some more time to come. The forecast for profit growth has therefore been revised upwards slightly for both 2017, which is still a forecast year in this context, and 2018.

As growth in the economy weakens at the end of the forecast period, profits fall back again. The assessment made of profit growth in 2019 is revised slightly downwards and profits are then expected to grow slightly more slowly than their historical average. However, the upward revisions for 2017 and 2018 mean that the level of corporate profits in 2019 will still be higher than the October estimate.

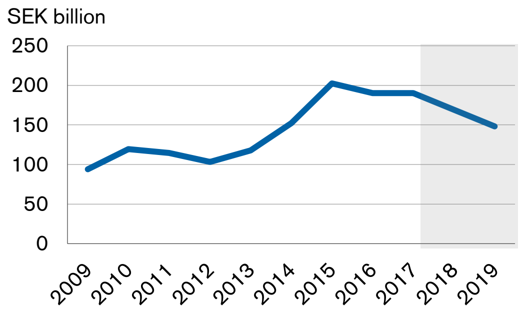
Slightly lower income from payroll taxes

Central government income from payroll taxes will be SEK 2 billion lower in both 2018 and 2019 than in the previous forecast. The growth rate of payroll is estimated to be 0.1 per cent higher in 2019 than previously estimated, which has a certain positive effect on payroll taxes. In contrast, the part of final tax paid in on a preliminary basis is expected to decrease slightly compared with the previous forecast, and this has a negative effect in cash terms for 2018.

Table 3. Tax income, change from previous forecast

SEK billion	2018	2019
Payroll taxes	-2	-2
Consumption taxes	1	0
Corporate taxes	4	2
Supplementary taxes	27	-6
Total	30	-6

Figure 4. Household capital gains



Source: Swedish tax agency and the Debt Office.

Marginal changes in the forecast of consumption taxes

Income from taxes on consumption is expected to rise by SEK 1 billion in 2018 and be unchanged in 2019, compared with the previous forecast. Marginal adjustments have been made to the forecast for private consumption and investments, which chiefly affect payments of VAT and selective taxes. The growth of VAT income at the end of 2017 was slightly stronger than estimated, and this also has a positive effect for 2018 and 2019.

High capital gains for households

The final tax assessment outcome for households' capital gains in 2016 was SEK 190 billion, which was fully in line with the Debt Office's forecast. For 2017, which is still a forecast year in this context, the Debt Office has revised capital gains upwards to roughly the same level as in 2016. This is a result of the large supplementary payments which have been made since the previous forecast. The Debt Office's assessment is that gains from home sales continued to increase in 2017 compared with 2016, despite unease in the housing market at the end of last year. Statistics from Svensk Mäklarstatistik (Swedish Real Estate Agents Statistics) show that the total sales value increased by about 10 per cent between these years. How this affects the gains reported is not certain, but historically the correlation has been strong. The Debt Office's assessment is that gains from the sale of securities will decrease, which is an effect of more people going over to saving in investment savings accounts (ISAs).

In 2018 and 2019 households' capital gains decrease, see figure 4.

Rising dividends on state-owned shares

In 2018 and 2019 central government income from share dividends is estimated to be SEK 2 and 3 billion higher respectively than in the previous forecast. The main explanation is that Vattenfall AB is paying a dividend for the first time for four years. The company reports a substantial improvement of earnings for 2017 after several years of poor earnings on account of write-downs. In its press release on its annual accounts for 2017 a dividend of SEK 2 billion is proposed.

LKAB is also expected to pay a slightly higher dividend than previously expected. The company's earnings have strengthened, mainly on account of rising market prices for iron ore products. In total, central government income from share dividends is estimated at SEK 12 billion in 2018 and SEK 15 billion in 2019, see table 4.

Table 4. Dividends on state owned shares

SEK billion	2018	2019
Akademiska hus AB	1.5	1.5
LKAB	0.8	1.3
Telia Company	3.7	4.0
Vattenfall AB	2.0	4.0
Sveaskog AB	0.8	0.8
Other corporations	3.1	3.1
Total	11.9	14.7

Lower sickness figures reduce expenditure for social insurance

Expenditure for social insurance will decrease by SEK 3 billion in 2018 and SEK 4 billion in 2019 compared with the previous forecast. The main explanation is that expenditure for sickness benefit is estimated to be lower than previously. The number of new sick cases decreased by about 7 per cent in 2017 from 2016. The Swedish Social Insurance Agency (Försäkringskassan) expects the number of sick cases to also decrease in 2018, which explains virtually all of the forecast revision. Historically the variation in the number of sick cases started has been great and is difficult to explain in terms of public health, demography or the state of the economy.

Central government expenditure for migration decreases between years
Expenditure for the Swedish Migration Agency is estimated to decrease by SEK 1 billion in 2018 and to be unchanged in 2019 compared with the previous forecast. Its expenditure falls by approximately SEK 19 billion between 2017 and 2018 and a further SEK 9 billion in 2019. This year this is an effect of a decreasing number of people in the Migration Agency's reception system. Next year the Migration Agency's expenditure for payments to municipalities is expected to begin to decrease.

Net lending by the Debt Office decreases
Net lending by the Debt Office in 2017 amounted to SEK -3 billion, which means that it strengthened the central government budget balance. During the year Ireland applied to repay its loans prematurely, and also did so at the end of 2017. This decreased lending by SEK 5 billion.

Net lending by the Debt Office

Net lending by the Debt Office to government agencies and other parties is an item on the expenditure side of the central government budget. This means that if the Debt Office net lending increases, the budget balance is weakened. This can also be expressed by saying that the net borrowing requirement increases.

Net lending to government agencies and other parties is not financed by appropriations and does not come under the expenditure ceiling. Net lending consists of the change of all lending from and deposits in the central government's internal bank, which is a division of the Debt Office. Net lending covers both ongoing central government activities, such as student loans, deposits in the premium pension system and lending to infrastructure investments, as well as temporary items such as on-lending to the Riksbank and to other countries. The temporary items may be decided at short notice and contribute to strong variations in net lending from year to year.

Net lending by the Debt Office affects the budget balance and central government debt. In contrast, central government net lending is only affected by certain parts of the Debt Office's net lending. For example, the payment and amortisation of student loans and capital advances to banks affect net lending by the Debt Office but not central government net lending.

For 2018 net lending by the Debt Office is expected to total just over SEK 2 billion. This is SEK 4 billion lower than in the previous forecast. The main reason for the reduction is that the Swedish Export Credit Agency (EKN) is going to move its credit reserve from currency accounts with commercial banks to an account at the Debt Office. This means that net lending decreases by just under SEK 6 billion in the second half of 2018.

Net lending in 2019 is expected to be SEK -1 billion as the change in deposits received will exceed lending. Compared with the previous forecast this is a reduction of about SEK 2 billion that is explained by lower on-lending to the Riksbank on account of changes in exchange rates. However, this on-lending is unchanged measured in foreign currency.

Change between years

The table shows how the budget balance changes between 2015 and 2019 and how different parts affect this change.

The budget balance increases by SEK 18 billion between 2017 and 2018. Tax revenue increases by SEK 70 billion, but this is countered to a great extent by rising expenditure in, for example, social insurance.

Between 2018 and 2019 the budget balance is weakened by an estimated SEK 35 billion. One important explanation is an estimated inflow of excess deposits to tax accounts in 2018, which turns into an outflow in 2019. In combination with a weakening of the economy this means that tax income will be virtually unchanged between these years at the same time as expenditure increases.

Expenditure for migration and development assistance increased strongly between 2015 and 2017, but falls back in 2018 and 2019, mainly on account of a lower inflow of asylum seekers.

SEK billion	2015	2016	2017	2018	2019
Budget Balance	-33	85	62	80	45
Change from previous year	40	118	-24	18	-35
Primary balance	**47**	**101**	**-31**	**26**	**-28**
Of which:					
Tax income	76	145	4	70	-1
Government grants to local governments	-7	9	-12	-5	-6
Labour market	0	1	0	-3	-1
Social insurance	-6	0	4	-14	-1
Migration & International aid	-10	-26	-5	14	7
Sales of state-owned assets	0	0	0	2	-2
Share dividends	7	-7	-4	3	3
EU contribution	4	5	2	-7	-4
Other	-18	-27	-20	-33	-23
Debt Office's net lending excl. on-lending	**19**	**1**	**7**	**-1**	**-11**
On-lending	**-7**	**-4**	**10**	**-5**	**15**
Interest on government debt	**-19**	**20**	**-9**	**-2**	**-10**

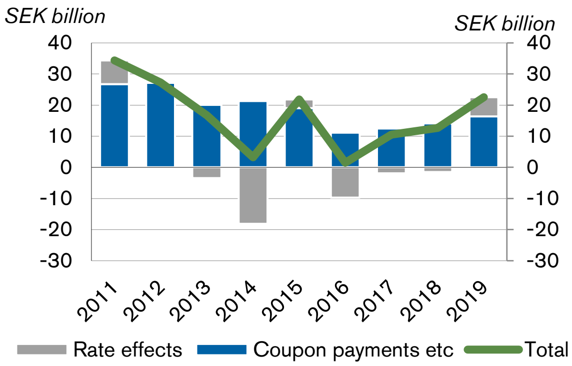
Interest payments on central government debt

Central government interest payments are estimated at SEK 13 billion this year and SEK 22 billion next year, see table 5 below. The forecast has been revised upwards by about SEK 1 billion for both 2018 and 2019, and this is mainly explained by higher exchange losses.

Table 5. Interest on central government debt

SEK billion	2018	2019
Interest on loans in SEK	12.4	21.5
Interest on loans in foreign currency	-0.2	-0.1
Realised currency gains and losses	0.4	0.9
Interest payments	**12.6**	**22.3**

Figure 5. Interest payments, 2011-2019



Interest payments increase by around SEK 10 billion between 2018 and 2019. Much of the increase is explained by planned switches in which the Debt Office buys back an inflation-linked bond maturing in 2020. The inflation-linked bond was introduced in 1996 and has a great deal of accrued inflation compensation that is paid in conjunction with the buybacks. If the switches are carried out, the inflation compensation paid will, as a result, be lower than at maturity in 2020.

The Debt Office uses cut-off rates in calculating central government interest payments and in measuring the Riksbank's foreign currency loans. The cut-off date for this forecast is 31 January 2018.

Table 6. Cut-off rates for interest rates, per cent

Duration	3 mth	6 mth	2 y	5 y	10 y	30 y
Government bonds	-0.8	-0.8	-0.5	0.2	0.9	2.2
Inflation-linked bonds	-2.5	-2.5	-2.3	-1.7	-1.0	0.3
Swap interest rate SEK	-0.4	-0.4	-0.1	0.7	1.4	
Swap interest rate EUR	-0.4	-0.3	-0.1	0.5	1.1	1.6
Swap interest rate USD	1.7	1.9	2.3	2.6	2.8	

Table 7. Cut-off rates for currency exchange

Spotrates	2018-01-31
SEK/EUR	9.78
SEK/USD	7.85
SEK/CHF	7.30
SEK/JPY	0.07
SEK/GBP	11.17
SEK/CAD	6.40

Central government net lending

Central government net lending shows a more even development than the net borrowing requirement and the budget balance, which are cash flow measures. As a proportion of GDP, this lending is estimated at 1.1 per cent in 2018 and 1.0 per cent in 2019. This is a slightly stronger development than in the previous forecast, and is mainly due to stronger economic growth.

Net lending is generally a better indicator of the underlying central government finances than the budget balance. Net lending accrues payments to the point in time when the economic activity took place.

Table 8. Central government net lending

SEK billion	2015	2016	2017	2018	2019
Budget balance	**-33**	**85**	**62**	**80**	**45**
Delimitations	**29**	**36**	**-4**	**0**	**13**
Sale of limited companies	0	0	-2	3	3
Extraordinary dividends	-9	-2	0	0	0
Parts of Debt Office's net lending	17	16	-2	3	3
Other delimitations etc.	21	22	-1	-6	8
Accruals	**16**	**-52**	**2**	**-29**	**-11**
Taxes	16	-41	2	-32	-15
Interest payments etc.	0	-12	1	3	4
Central government net lending	**12**	**69**	**59**	**51**	**48**
Per cent of GDP	0.3	1.6	1.3	1.1	1.0

Net lending is also adjusted for payments that do not affect central government's financial wealth. If, for example, central government sells financial assets such as shares, this does not affect net lending. Central government merely redistributes assets in its balance sheet, i.e. shares are exchanged for cash. However, when the payment is made, the budget balance is affected and the central government debt decreases. Amortising the central government debt does not affect the net asset position of central government either since its assets decrease just as much.

In the same way, net lending is not affected by lending to the Riksbank. This is because, in its balance sheet, central government receives an asset (a claim on the Riksbank) that corresponds to the increased indebtedness incurred in order to finance lending to the Riksbank. On the other hand, the budget balance and central government debt are affected.

Nor is central government net lending affected by capital investments in tax accounts. They are counted as deposits instead of tax income.

Monthly forecasts

The budget balance varies strongly between months. The following table presents monthly forecasts until and including December 2018.

Much of the variation between months is explained by how tax income, tax refunds and on-lending by the Debt Office are spread over the year. Some individual payments also impact on the monthly pattern, one example being the annual payment of premium pension funds.

The large deficit in December is normal and part of the explanation is payment of premium pension funds, excess tax and interest payments on the central government debt.

Table 9. Budget balance per month, SEK billion

	Primary balance	Net lending	Interest on central government debt	Budget balance
Feb-18	55.1	-1.5	1.2	54.8
Mar-18	2.1	3.9	-4.1	1.9
Apr-18	2.6	2.8	-0.8	4.6
May-18	41.1	7.1	-1.0	47.2
Jun-18	-21.5	5.3	-3.9	-20.1
Jul-18	5.9	5.6	0.4	11.8
Aug-18	22.1	4.8	0.5	27.4
Sep-18	-1.2	3.9	1.0	3.7
Oct-18	2.1	3.8	1.8	7.8
Nov-18	23.9	4.2	-1.2	27.0
Dec-18	-39.9	-38.2	-8.0	-86.1

Sensitivity analysis

The Debt Office does not produce any overall sensitivity analysis for the budget balance. Instead a partial analysis of the effects that changes in certain key variables have is presented. The table shows an estimate of what different changes mean for the budget balance on a one-year term.

Increase by one per cent/percentage point	Effect on budget balance
Gross wages 1	7
Household consumption in current prices	3
Unemployment (ILO 15-74) 2	-3
Interest rate level in Sweden 3	-5
International interest rate level 3	-2
Asylum seekers, increase of 10 000	

[1] Local government taxes on employment are paid to local authorities with a one-year time lag. This means that the effect on the budget balance in one year's time is bigger than the permanent effect
[2] Includes effects on unemployment insurance benefits, the job and development guarantee programme and the job guarantee scheme for young people.
[3] This relates to an effect on interest payments on government debt.

Forecast comparisons

The Debt Office forecasts a much higher budget balance in 2018 than the Swedish Financial Management Authority (ESV and the National Institute of Economic Research (NIER). Much of the difference is explained by differences in the assessments made of capital investments in tax accounts. The ESV and the NIER expect rising market interest rates to lead to a decrease of SEK 30 billion in capital investments in 2018. The Debt Office instead expects a continued inflow of SEK 24 billion in 2018. In the Debt Office's assessment, the interest rate increase come later and the outflow from tax accounts does not occur until 2019.

	Debt Office (21 Feb)		Government (20 Sep)		NIER (21 Dec)		ESV (17 Nov)	
SEK billion	2018	2019	2018	2019	2018	2019	2018	2019
Budget Balance	80	45	44	72	36	84	12	47
of which:								
Sales of state assets	2	0	5	5	0	0	0	0
Adjusted net borrowing requirement	**78**	**45**	**39**	**67**	**36**	**84**	**12**	**47**

Lower volume of government bonds

As a result of the larger budget surplus the Debt Office decreases its borrowing in government bonds for the fifth time in two years. The new issue volume will be SEK 1.5 billion per auction, corresponding to an annual rate of SEK 30 billion. The Debt Office's assessment is that a further reduction from that level is not appropriate since it would risk leading to higher borrowing costs and poorer borrowing preparedness in the longer term. Borrowing in inflation-linked bonds, T-bills and foreign currency bonds is unchanged from the previous forecast.

Issue volumes reach a lower limit

The central government borrowing requirement, including refinancing of maturing loans, is estimated at SEK 160 billion in 2018 and SEK 183 billion in 2019, see table 1. This is a decrease of SEK 66 billion and 50 billion respectively compared with the previous forecast. The decrease is due not only to the Debt Office increasing its forecast of the budget surplus but also to a stronger outcome than expected in 2017.

As a consequence of the lower borrowing requirement the Debt Office is reducing the issue volume of government bonds by SEK 500 million per auction. The issue volumes of the other types of debt are kept unchanged, see table 2.

Table 10. Gross borrowing requirement

SEK billion	2017	2018	2019
Net borrowing requirement	-62	-80	-45
Business day adjustment etc. [1]	4	2	1
Retail borrowing & collateral, net [2]	14	9	6
Money market redemptions [3]	144	122	15
T-bills	84	88	20
Liquidity management	60	35	-5
Bond redemptions, net switches and buy-backs	145	106	206
Government bonds	69	5	99
Inflation-linked bonds	15	0	21
Foreign currency bonds [4]	62	101	87
Total gross funding requirement	246	160	183

[1] Borrowing is reported by business date while net borrowing requirement is reported by settlement date.
[2] Net change in retail borrowing and collateral.
[3] Initial stock maturing within 12 months. Commercial paper is included in Liquidity management.
[4] Calculated with the original issuance exchange rate.

This reduction brings the issue volume of government bonds back to its historically low level from 2007. Although, this time the net supply on the government bond market is less compared to then due to the Riksbank's purchases. The Debt Office makes the assessment that an even lower issue volume risks reducing market liquidity to the extent that investors leave the market, which would result in poorer borrowing preparedness and higher long-term borrowing costs for central government. So further reductions would not be consistent with the objective of minimising the long-term costs for the management of the central government debt while taking account of risk.

The reduction of bond borrowing would, moreover, be countered by greater demand for the Debt Office's standing repo facility. As a result, an increasing share of central government financing would be moved from long-term borrowing in the bond market to short-term borrowing in the repo market.

Table 11. New borrowing forecast

	2017		2018		2019
SEK billion	Outcome	Feb	(Oct)	Feb	(Oct)
Money market funding [1]	122	15	(75)	83	(121)
T-bills	88	20	(20)	20	(20)
Liquidity management [2]	35	-5	(55)	63	(101)
Bond funding	124	145	(150)	99	(112)
Government bonds	51	32	(40)	30	(40)
Inflation-linked bonds	12	9	(9)	9	(9)
Foreign currency bonds	61	105	(102)	61	(63)
central government	0	0	(0)	0	(0)
on behalf of the Riksbank	61	105	(102)	61	(63)
Total gross funding	246	160	(226)	183	(233)

[1] Outstanding stock as at year-end.
[2] Commercial paper is included in Liquidity management.

In the past the Debt Office has repurchased government securities in auctions as an alternative to reducing issue volumes. But buying back krona bonds today would probably have the same effect as reducing borrowing: i.e. the market would function less well and demand for repos would increase. Experience also shows that such buy-backs can be expensive. However, the Debt Office could buy back small volumes of foreign currency bonds if there was an interest in the market in selling.

The unlimited repo facility is more important than ever

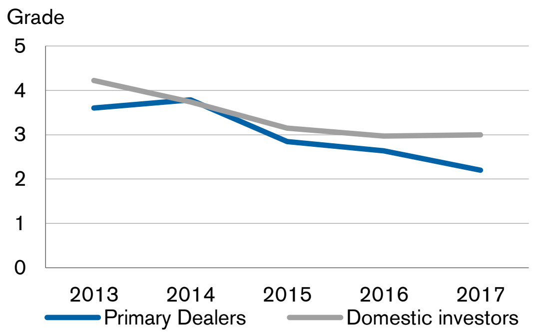
One of the Debt Office's most important strategies for achieving the objective of central government debt management is to work for a well-functioning government securities market. The unlimited repo facility for bonds is central to that strategy.

In recent years, liquidity in the market for government bonds has gradually worsened because of several factors working in the same direction. Financial market regulations, lower issue volumes and bond purchases by the Riksbank have contributed to the situation becoming increasingly strained.

At the end of January 2018 the Riksbank owned more than half of the outstanding stock of government bonds with maturities up to the ten-year segment, see figure 4. This share will increase in 2018 since the Riksbank intends to reinvest maturing bonds in advance. The survey that the Debt Office conducts each year among its counterparties confirms the picture that the market for government bonds is not functioning as well as before. Figure 1 shows how liquidity is perceived by primary dealers and Swedish investors, expressed as grades on a five-point scale.

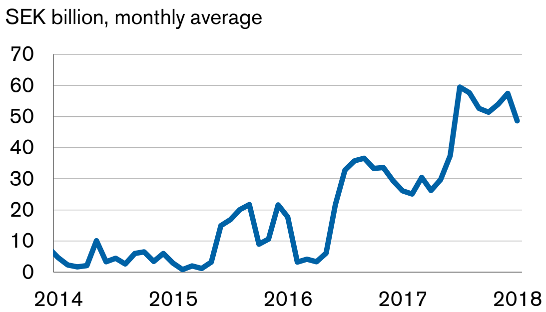
In view of the worsened liquidity in the market the Debt Office considers that its standing repo facility is more important than ever. Demand for repos has increased markedly in recent years and would, in all probability, be even stronger if issue volumes were reduced even more, see figure 2.

Figure 1. Perceived liquidity in government bonds



Source: Kantar Sifo Prospera

Figure 2. Government bond repos



Cash surplus for a longer period than normal

The new borrowing plan means that the Debt Office will need to handle cash surpluses in liquidity management for a longer period than normal. This also means that in the short term the central government debt will not decrease at the same rate as the budget balance is strengthened, see the box *Assets in liquidity management* on page 39. In the longer term the cash surplus will shrink as outstanding bonds mature, and then the debt will fall more quickly. In 2019 and 2020, government bonds and inflation-linked bonds amounting to around SEK 120 billion mature each year.

Historically low borrowing in government bonds

The issue volume of government bonds is reduced from SEK 2 billion to SEK 1.5 billion as of the auction on 7 March. This returns it to the same low level as during a short period ten years ago, see figure 3. The number of auctions is unchanged and borrowing will therefore decrease to an annual rate of SEK 30 billion.

Figure 3. Auction volume of government bonds

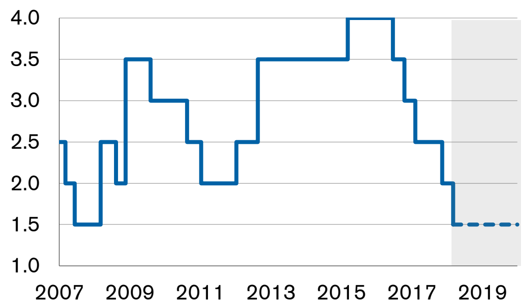
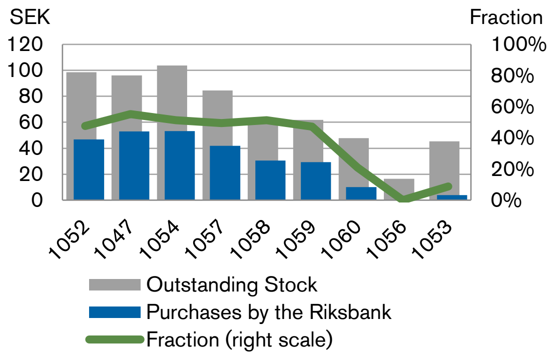


Figure 4. Outstanding government bonds



As a result of this reduction a slightly greater focus is needed on borrowing in the ten-year segment in order to top up the volume of new bonds. Ten-year bonds will therefore account for a larger part of the issue volume. The remaining auctions will mainly be held in the five- and two-year segments, but other maturities may be also offered if this is justified in order to maintain the liquidity of the bonds.

Table 12. Important dates 2018

Date	Time	Activity
2 May	09.30	Info on switches to SGB 1061
30 May	11.00	Introduction of SGB 1061
31 May - 4 Jun	11.00	Switches to 1061
20 Jun	09.30	Borrowing forecast 2018:2

Table 13. Important dates 2018

Date of change (IMM date) [1]	2-year	5-year	10-year
Current reference bonds	1047	1057	1060
19 Dec 2018			1061
19 Jun 2019	1054	1058	

As previously announced, the Debt Office is introducing a new bond in the ten-year segment at the auction on 30 May this year. The bond SGB 1061 will have the redemption date of 12 November 2029. The Debt Office offers switches to the new bond in conjunction with its introduction. The Debt Office also plans to offer switches before the bond becomes a ten-year reference bond, see tables 3 and 4.

Reference bonds

The reference bond in electronic trading is the bond that is closest to two, five or ten years in terms of maturity. Reference bonds are only changed on the IMM date (third Wednesday in March, June, September and December) provided the new bonds are the bonds that are closest in terms of maturity to two, five or ten years on the subsequent IMM date. The underlying bond in a forward contract will always be the same as a reference bond during the last three months of the contract. The date of change of reference bonds refers to the settlement date. The first trading day for a new reference bond is normally the Monday preceding an IMM date.

Unchanged volume of interest rate swaps

The volume of interest rate swaps remains at SEK 5 billion per year during the forecast period. The outstanding stock of swaps continues to decrease since the volume of new swaps is small in relation to the maturing of swaps previously entered into, see table 5.

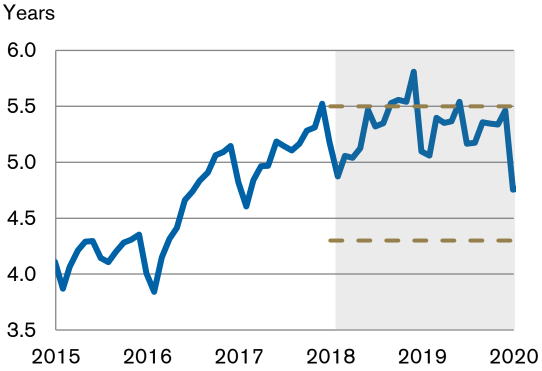
Table 14. Change in outstanding swaps

	2017		2018		2019
SEK billion	Outcome	Feb	(Oct)	Feb	(Oct)
Interest rate swaps [1]	5	5	(5)	5	(5)
Swaps total	5	5	(5)	5	(5)
Swaps maturing	39	29	(29)	41	(41)
Swaps, net change	-34	-24	-(24)	-36	-(36)

[1] Interest rate swaps from fixed to floating rate in SEK.

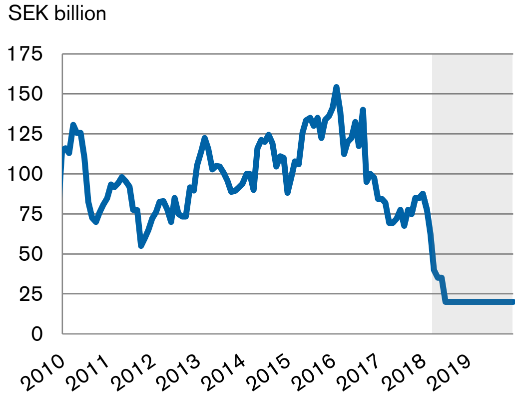
The Debt Office uses interest rate swaps to shorten the duration of the nominal krona debt. Historically this has led to the cost of the debt being lower. For a time, however, the cost saving has been judged to be small, so the volume of swaps has been reduced gradually. This has contributed to a continuing rise in duration, see figure 5. According to the Government's guidelines, the duration of the whole of the nominal krona debt is to be between 4.3 and 5.5 years. During the forecast period it is expected to be in the upper part of that interval on account of the cash surpluses in liquidity management.

Figure 5. Nominal SEK debt duration [1]



[1]As of 2018 the duration target includes the entire nominal krona debt, including the long dated bonds.

Figure 6. Outstanding stock of T-bills



Borrowing in T-bills remains at a low level

At year-end the issue volume of T-bills was reduced to SEK 5 billion per auction at the same time as the number of auctions was halved. Borrowing is expected to stay at that level throughout the forecast period. The reason given for the reduction in the October forecast was that the ever higher volume in the standing repo facility acts as a kind of involuntary short-term borrowing that crowds out other short-term borrowing.

As a result of the low issue volume, the outstanding stock of T-bills will decrease from SEK 88 billion at the start of 2018 to SEK 20 billion at year-end, see figure 6.

Issue volume of inflation-linked bonds is also unchanged

Planned borrowing in inflation-linked bonds is the same as in the October forecast. At that time the issue volume was reduced to SEK 500 million per auction, corresponding to an annual rate of SEK 9 billion. Borrowing will remain at that level until and including 2019.

As is the case for nominal bonds, the Debt Office prioritises issues in the ten-year segment in order to build up the volume of the newest bonds, SGB IL 3112 and SGB IL 3113. In the second place, auctions are held of the slightly shorter bond SGB IL 3109. There may also be individual issues of other maturities in order to promote liquidity in the market.

The share of inflation-linked debt in the central government debt is expected to average around 23 per cent during the period. According to the Government's guidelines this share is to be steered towards 20 per cent in the long term. In the short term the share mainly depends on how the level of the central government debt changes. Since the central government debt is expected to decrease, the average will be slightly above the long-term benchmark during the forecast period, see figure 7. The Debt Office is seeking to attain a more even maturity profile in the inflation-linked debt with roughly the same outstanding volume in the various bonds, see figure 8.

The Debt Office tries to avoid letting excessive amounts go to maturity since this can put a strain on the market and create reinvestment risks for investors. During next year the Debt Office therefore plans to offer switches in which the Debt Office buys back part of the outstanding volume of SGB IL 3102. That bond matures in December 2020.

In June it will be one year until SGB IL 3110 matures. During the final year there are no issues or switches of the bond. However, as in the past the Debt Office will continuously offer buy-backs during this period. Primary dealers pay a premium to use this facility since the Debt Office buys the bond at a certain discount.

Figure 7. Proportion of inflation-linked debt

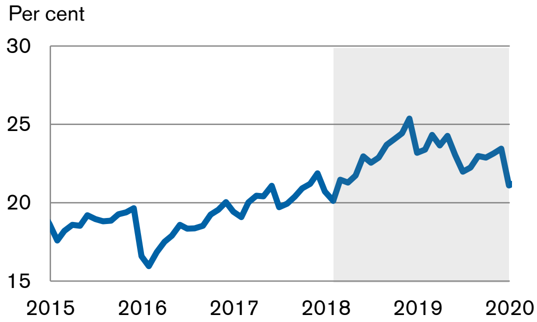
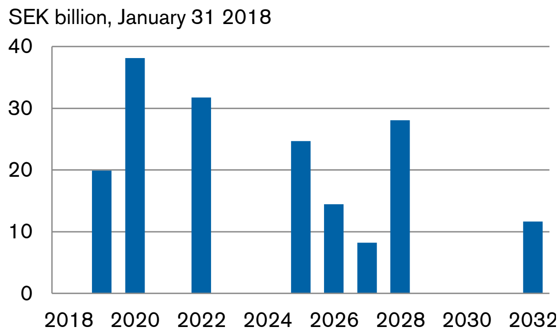


Figure 8. Outstanding inflation-linked bonds



Evaluation of the standing switch facility
To support liquidity in the market for inflation-linked bonds the Debt Office offers a standing switch facility that permits primary dealers to make switches between inflation-linked bonds for a certain premium. At present the facility is limited to SEK 500 million per primary dealer and week.

The Debt Office considers that these switches help to improve the functioning of the market and it intends to keep the present volume for the time being. However, the Debt Office will closely monitor how the facility is used in order to determine subsequently whether its pricing should be adjusted or whether its volume should be limited further.

Foreign currency borrowing only for the Riksbank

The Debt Office continues to issue bonds in foreign currencies solely to refinance loans to the Riksbank. This borrowing corresponds to an estimated SEK 105 billion and 61 billion in 2018 and 2019 respectively. The total borrowing over these years is marginally higher than in the previous forecast due to changes in exchange rates. Calculated in foreign currency, the volume is unchanged.

More than half of the volume to be refinanced in 2018 was borrowed at a maturity of five years in the opening weeks of the year. Figure 9 shows the outstanding claims on the Riksbank on 31 January 2018. In total, on-lending to the Riksbank corresponds to SEK 231 billion. Its financing accounts for the main share of the Debt Office's outstanding foreign currency bonds, see figure 10

Figure 9. On-lending to the Riksbank

Billion SEK, 29 September 2017

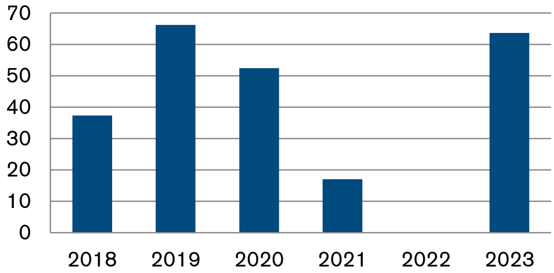
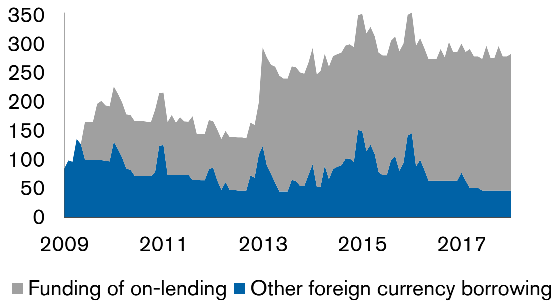


Figure 10. Foreign currency bonds

SEK billion



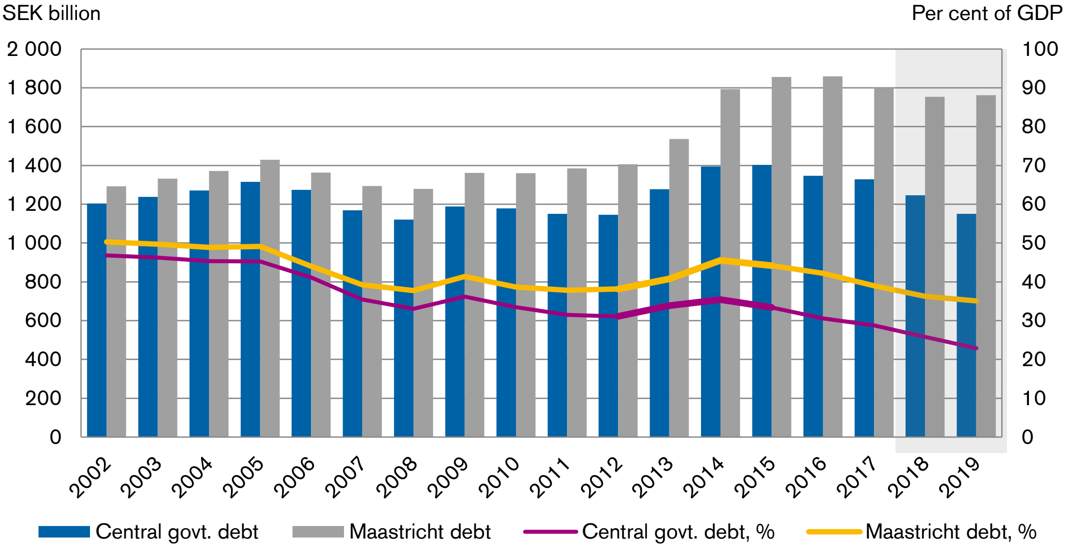
The central government debt continues to decrease

The central government debt continues to decrease during the period, both in absolute terms and as a share of GDP, see figure 11. The Debt Office expects the central government debt to fall to SEK 1 151 billion at the end of the forecast period, corresponding to 23 per cent of GDP. The debt does not decrease by exactly the same amount as the surplus in the central government budget. One explanation is the assets in liquidity management. The change in the debt also depends on upward adjustment of accrued inflation in the inflation-linked debt and revaluation of the foreign currency debt at new exchange rates.

There are great variations in central government payments between days and between months. Buying back outstanding bonds during temporary periods of surpluses in payments and then borrowing again when payments show a deficit would be both expensive and associated with risks. Instead, during periods of surplus in the central government treasury the Debt Office invests money temporarily in the money market until it is needed to pay for expenditure or maturing loans. Since the official measure of the central government debt is the gross debt, such assets in liquidity management are not deducted.

On account of the strong central government finances and the great demand for the standing repo facility, the Debt Office is likely to manage cash surpluses for a longer period than usual. The Debt Office has therefore made an upward revision of its previous forecast of outstanding assets in liquidity management. The gross amount is thus expected to be appreciably higher than the net amount reported in, for example, table 2. The forecast of assets in liquidity management is shown in table 6. The background to the forecast is described in the box *Assets in liquidity management*.

Figure 11. Development of the central government debt



The Debt Office reports the unconsolidated central government debt. The Maastricht debt covers the whole of the public sector and is a measure of the consolidated debt. See the fact box *Different measures of government debt in statistics*.

Table 15. Net borrowing and the central government debt

SEK billion	2014	2015	2016	2017	2018	2019
Net borrowing requirement	72	33	-85	-62	-80	-45
Business day adjustment etc. [1]	-4	0	-7	4	2	1
Net borrowing per business day	68	32	-92	-58	-79	-45
A. Nominal amount including money market assets	1 321	1 353	1 261	1 203	1 124	1 080
Inflation compensation	25	19	21	23	28	22
Exchange rate effects	30	29	40	11	-6	-1
B. Nominal amount to current exchange rate incl. inflation compensation and money market assets	1 376	1 401	1 321	1 237	1 147	1 101
Assets under management	18	3	26	91	100	50
C. Central government debt	**1 394**	**1 403**	**1 347**	**1 328**	**1 247**	**1 151**
Assets under management	-18	-3	-26	-91	-100	-50
On-lending	-233	-247	-263	-238	-231	-231
D. Central government debt incl. on-lending and assets	1 143	1 154	1 059	999	916	869
Nominal GDP	3 937	4 200	4 405	4 621	4 833	5 023
C. Central government debt, % of GDP	35	33	31	29	26	23
D. Central government debt incl. on-lending and money market assets, percentage share of GDP	29	27	24	22	19	17

[1] Borrowing is reported by business date while net borrowing requirement is reported by settlement date.

Measures of central government debt in statistics

There are several different ways of measuring central government debt. The Debt Office reports the *unconsolidated central government debt*. This measure shows central government gross debt and includes all loans raised by the Debt Office on behalf of central government, irrespective of who owns the claims on central government. The debt is reported at its nominal terminal value according to the principles applied in the EU.

Some government agencies own government bonds and T-bills. This kind of intra-government ownership is deducted in the *consolidated central government debt*. That measure gives an overall picture of the financial position of central government and is used in the Government's budget bill and in the central government annual report. The consolidated debt is calculated by the Swedish Financial Management Authority.

One debt measure often used in international comparisons is *general government consolidated gross debt*, also called the *Maastricht debt*. This debt is larger than the central government debt since it covers the whole of the public sector, i.e. including municipalities, county councils and the pension system. Its calculation is based on conditions in the Maastricht Treaty. According to the EU's government debt criterion the Maastricht debt must not exceed 60 per cent of GDP. The Maastricht debt is also the measure that is used in the budgetary framework and that applies to the debt anchor of 35 per cent that the Riksdag has decided will apply as of 2019. The general government consolidated gross debt is published by Statistics Sweden.

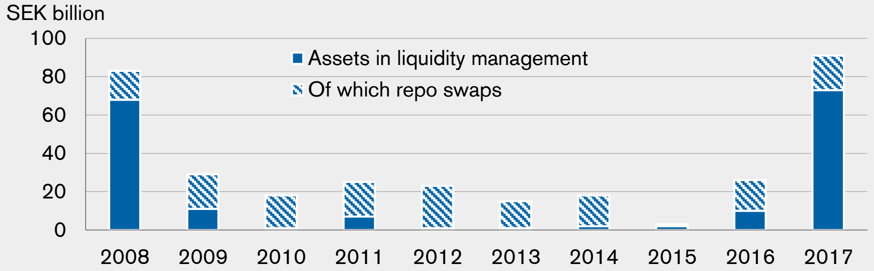
Assets in liquidity management

At the end of 2017 the Debt Office had placed SEK 91 billion in assets in liquidity management. This amount is far in excess of the normal year-end level and the main reason is that borrowing subsequently turned out to be higher than necessary in view of the unexpectedly strong central government finances. In addition, the volumes in the Debt Office's standing repo facilities with primary dealers reached record highs. The funds that the Debt Office received in these repos contributed to the large cash surplus.

In the past ten years, assets in liquidity management have swung between SEK 3 and 91 billion, see figure 12. Excluding 2008 and 2017 the average is around SEK 20 billion. The large assets in 2008 were due to the sales of Vin & Sprit, Vasakronan and the central government share of OMX which brought in some SEK 77 billion to the government treasury. Those funds were then invested temporarily and decreased gradually afterwards on account of lower borrowing in subsequent years.

Historically the main reason for year-end investments has been repo swaps with primary dealers in the Debt Office's standing repo facility.[1] On average they have amounted to SEK 11 billion in recent years. The demand for repo swaps usually increases in conjunction with year ends. In some years the Debt Office has also had smaller assets in the form of collateral on account of changes in the market value of derivative instruments.

Figure 12. Assets in liquidity management at year end 2017



From a cost and credit risk perspective the large cash holding is relatively unproblematic. The bulk of it is invested at the repo rate in Riksbank certificates that have no credit risk. Moreover, this investment normally provides a saving since the Debt Office usually borrows at an interest rate below the repo rate. On the other hand, the official measure of the central government debt is higher than it would otherwise have been since the central government debt is reported gross so that assets in liquidity management are not deducted.

The great demand for the standing repo facilities is expected to continue in the coming years and the Debt Office assumes it will be managing cash funds for most of the forecast period. The forecast of assets in liquidity management has therefore been revised upwards to SEK 100 billion in 2018 and SEK 50 billion in 2019.

[1] In a repo swap the Debt Office offers primary dealers a switch of one bond or T-bill for another one along with an agreement on the opposite transaction in the future.

Market information

Table 16. Government bonds, auction dates

Announcement date	Auction date	Settlement date
28-Feb-18	07-Mar-18	09-Mar-18
14-Mar-18	21-Mar-18	23-Mar-18
28-Mar-18	04-Apr-18	06-Apr-18
11-Apr-18	18-Apr-18	20-Apr-18
25-Apr-18	02-May-18	04-May-18
09-May-18	16-May-18	18-May-18
23-May-18	30-May-18	01-Jun-18
02-May-18	31-May-18*	04-Jun-18
02-May-18	01-Jun-18*	05-Jun-18
02-May-18	04-Jun-18*	07-Jun-18
05-Jun-18	13-Jun-18	15-Jun-18

*Switch auction

Table 17. Outstanding government bonds

Maturity date	Coupon %	Bond no.	SEK Million
12-Mar-19	4.25	1052	98 550
01-Dec-20	5.00	1047	96 054
01-Jun-22	3.50	1054	103 631
13-Nov-23	1.50	1057	84 477
12-May-25	2.50	1058	59 376
12-Nov-26	1.00	1059	61 891
12-May-28	0.75	1060	47 865
01-Jun-32	2.25	1056	16 500
30-Mar-39	3.50	1053	45 250
Total government bonds			613 594

Table 18. T-bills, auction dates

Announcement date	Auction date	Settlement date
21-Feb-18	28-Feb-18	02-Mar-18
21-Mar-18	28-Mar-18	03-Apr-18
30-Apr-18	08-May-18	11-May-18
13-Jun-18	20-Jun-18	25-Jun-18
27-Jun-18	04-Jul-18	06-Jul-18

Table 19. Outstanding T-bills

Maturity date	SEK Million
21-Feb-18	20 000
21-Mar-18	27 500
18-Apr-18	5 000
16-May-18	5 000
20-Jun-18	20 000
Total T-bills	77 500

Table 20. Inflation-linked bonds, auction dates

Announcement date	Auction date	Settlement date
08-Mar-18	15-Mar-18	19-Mar-18
05-Apr-18	12-Apr-18	16-Apr-18
19-Apr-18	26-Apr-18	30-Apr-18
17-May-18	24-May-18	28-May-18
31-May-18	07-Jun-18	11-Jun-18

Table 21. Outstanding inflation-linked bonds

Maturity date	Coupon %	Bond no.	SEK Million
01-Jun-19	0.125	3110	19 895
01-Dec-20	4.00	3102	38 132
01-Jun-22	0.25	3108	31 758
01-Jun-25	1.00	3109	24 676
01-Jun-26	0.125	3112	14 432
01-Dec-27	0.125	3113	8 214
01-Dec-28	3.50	3104	28 062
01-Jun-32	0.125	3111	11 646
Total Inflation-linked bonds			176 815

Rating

Rating company	Debt in SEK	Foreign currency debt
Moody's	Aaa	Aaa
Standard & Poor's	AAA	AAA
Fitch	AAA	AAA

Primary dealers

Primary dealer	Government bonds	Inflation-linked bonds	T-bills	Telephone
Barclays	•			+44 207 773 8379
Danske Markets	•	•	•	+46 8 568 808 44
Handelsbanken Markets	•	•	•	+46 8 463 46 50
NatWest Markets	•			+44 207 805 0363
Nordea Markets	•	•	•	+45 3333 1609
				+46 8 614 91 07
SEB	•	•	•	+46 8 506 231 51
Swedbank	•	•	•	+46 8 700 99 00

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

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