Kingdom of Sweden
Rating Report

SCOPE AAA STABLE OUTLOOK

Credit strengths

- Wealthy, diversified economy
- Strong fiscal framework and low public debt
- Robust external position

Credit challenges

- High household and corporate debt levels
- Risk of severe housing market correction

Rating rationale:

Wealthy, diversified economy: Sweden benefits from a wealthy, internationally competitive and diversified economy, which recovered quickly from the Covid-19 crisis. Growth in 2022 was supported by private consumption and investments although inflationary pressures have caused a slowdown since mid-2022, with economic growth expected to turn negative in 2023. Over the medium-term we estimate Sweden's growth potential at around 1.8%.

Robust fiscal framework and low public debt ratio: Credible fiscal policy enabled an effective fiscal response to the Covid-19 pandemic with a focus on the green transition and inclusion. It also placed the government in a strong position to shield households from the rising energy prices and increased military spending. The rating is supported by the strong fiscal framework, which anchors the debt-to-GDP ratio at 35% (+/-5%).

Robust external position: Sweden is an open, diversified economy that has benefitted from current account surpluses over the last two decades and has a net external creditor position. Paired with a good level of reserves, these aspects shield the country from short-term shocks.

Rating challenges include: i) financial stability risk, including from high household and corporate debt levels; and ii) the risk of a severe correction in the housing market.

Sweden's sovereign rating drivers

Risk pillars		Quantitative		Reserve currency	Qualitative*	Final rating
		Weight	Indicative rating	Notches	Notches	
Domestic Economic Risk		35%	aa+	SEK [+0]	+1/3	AAA
Public Finance Risk		20%	aaa		+2/3	
External Economic Risk		10%	aa-		+1/3	
Financial Stability Risk		10%	aaa		-1/3	
ESG Risk	Environmental Factors	5%	aaa		+1/3	
	Social Factors	7.5%	bb		0	
	Governance Factors	12.5%	aaa		+1/3	
Indicative outcome			**aaa**		**+2**	
Additional considerations					**0**	

Note: The qualitative scorecard adjustments, capped at one notch per rating pillar, are weighted equally with an aggregate adjustment rounded to the nearest integer. The reserve currency adjustment applies to currencies in the IMF's SDR basket. For details, please see Scope's Sovereign Rating Methodology. Source: Scope Ratings.

Outlook and rating triggers

The Stable Outlook reflects our view that risks to the ratings are balanced over the next 12 to 18 months.

Positive rating-change drivers

- Not applicable

Negative rating-change drivers

- Significant deterioration in fiscal outlook
- Significant deterioration in economic outlook, for example, due to a sharp correction in the housing market

Ratings and Outlook

Foreign currency

Long-term issuer rating	AAA/Stable
Senior unsecured debt	AAA/Stable
Short-term issuer rating	S-1+/Stable

Local currency

Long-term issuer rating	AAA/Stable
Senior unsecured debt	AAA/Stable
Short-term issuer rating	S-1+/Stable

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Bloomberg: RESP SCOP

Domestic Economic Risks

- **Growth outlook:** Sweden's economy rebounded quickly from the Covid-19 crisis, growing by 4.8% in 2021. By early 2021, economic output reached pre-pandemic levels on the back of a strong recovery in private consumption, investment and in-person services. However, this momentum slowed significantly from mid-2022 due to the fallout from the Russia-Ukraine war, as wider inflationary pressures and the close interconnection with European electricity markets caused energy prices to surge. This has resulted in tightening financial conditions, a sharp contraction in the housing market and falling real incomes. While economic output still increased by 2.8% in 2022, we expect GDP to decline by 1.0% in 2023. The recession is expected to be short-lived, with GDP growing again in 2024 by 1.3% before returning to Sweden's medium-term annual growth potential of around 1.8%.

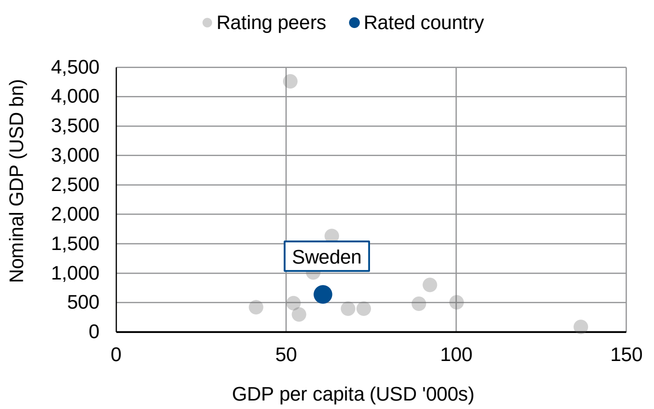
- **Inflation and monetary policy:** Inflation has been increasing rapidly since mid-2021, from 1.4% in July 2021 to 12.0% in February 2023. The inflation rate increased in February despite falling energy prices. Core inflation has remained exceptionally high at 9.3%, well above the Riksbank's target of 2%. Inflation is expected to fall quickly in 2023, although the risk of a slower decline remains. The Riksbank's Executive Board raised the policy rate by half a percentage point to 3.0% in February and signalled further rate hikes this year. In addition, the Riksbank ceased asset purchases at the end of 2022 and will start to sell government bonds from April 2023. Asset holdings have started to shrink, amounting to just over SEK 829.3bn (or 14% of GDP) as of February 2023.

- **Labour markets:** Labour markets remain resilient despite the slowing economic growth. The employment rate continues to be well above the pre-pandemic level, standing at 69.1% for 15–74-year-olds in February 2023, while the unemployment rate of 7.6% in February 2023 is only marginally above the pre-pandemic level of 7.4% in January 2020. Wage growth has been muted so far and labour unions have called for below-inflation wage increases, reflecting the challenging economic environment. With little risk of a wage-price spiral, we expect the unemployment rate to average 8% in 2023, up from 7.5% in 2022.

Overview of Scope's qualitative assessments for Sweden's *Domestic Economic Risks*

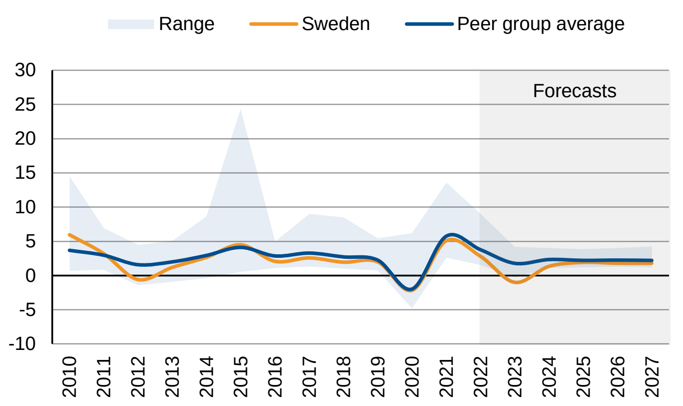
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Growth potential of the economy	Neutral	0	Moderate growth potential of around 1.8%
	Monetary policy framework	Neutral	0	Riksbank is a credible and effective monetary authority, still elevated inflation pressures
	Macro-economic stability and sustainability	Strong	+1/3	Competitive economy, favourable business environment and highly skilled labour force; healthy labour market with high employment and labour force participation rates

Nominal GDP and GDP per capita, USD



Source: IMF World Economic Outlook (WEO), Scope Ratings

Real GDP growth, %



Source: IMF WEO, Scope Ratings forecasts

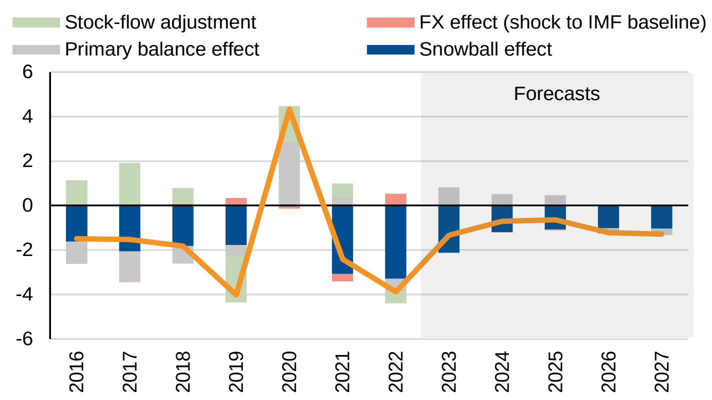
Public Finance Risks

- **Fiscal outlook:** Sweden's strong and resilient public finances have enabled the government to adopt effective fiscal measures through the Covid-19 pandemic and the current energy crisis. Since September 2021, EUR 6.8bn (1.3% of GDP) has been allocated to shield households and firms from the energy crisis in addition to a EUR 23bn (4.4% of GDP) emergency backstop for utilities. We expect budget deficits of around 1.0% of GDP in 2023 and 0.8% of GDP in 2024, reflecting lower tax income and higher central government spending in light of the economic slowdown. In addition to automatic stabilisers resulting in higher budget deficits, the 2023 budget includes spending on a temporarily reduced tax on gasoline and diesel, increased government grants to municipalities and regions, additional labour market support, and defence initiatives. Around SEK 40bn in the 2023 budget is unfunded, which is expected to lead to more bond issuances this year. However, in aggregate, we do not expect a significant expansionary fiscal policy as the government attempts to avoid fuelling inflationary pressures.
- **Debt trajectory:** The debt-to-GDP ratio increased from 35% in 2019 to almost 40% in 2020 before declining to 33% in 2022. We expect the ratio to continue to decline and reach 28% by 2027. The level could therefore fall below the fiscal framework's threshold of 35% (+/-5%). Sweden still has one of the lowest debt levels in the EU. The declining trend provides fiscal space for increased investments aimed at supporting long-term economic growth.
- **Debt profile and market access:** Sweden benefits from strong market access and low financing costs. The average sovereign debt maturity of 4.9 years as of February 2023 is shorter than that of AAA rated peers such as Denmark (9.1 years), the Netherlands (8.6 years) or Germany (7.6 years). In line with other highly rated countries, Sweden's 10-year government bond yield has increased since March 2022 from 0.8% to around 2.4% in March 2023. As a result of the weaker budget balance, Sweden's Debt Office will increase the supply of nominal government bonds from SEK 2bn to SEK 2.5bn per auction from the beginning of 2024. The volume of treasury bills will also increase, while the issuance volume of inflation-linked bonds will remain unchanged.

Overview of Scope's qualitative assessments for Sweden's *Public Finance Risks*

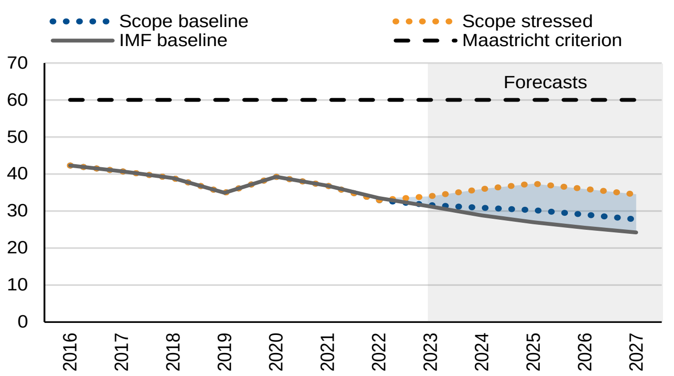
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Fiscal policy framework	Strong	+1/3	Appropriate countercyclical response to the Covid-19 and energy crises; track record of prudent fiscal policies
	Debt sustainability	Strong	+1/3	Declining public debt trajectory in the medium to long term
	Debt profile and market access	Neutral	0	Excellent market access, low government financing costs and relatively short debt maturity

Contributions to changes in debt levels, pp of GDP



Source: Scope Ratings forecasts

Debt-to-GDP forecasts, % of GDP



Source: IMF WEO, Scope Ratings forecasts

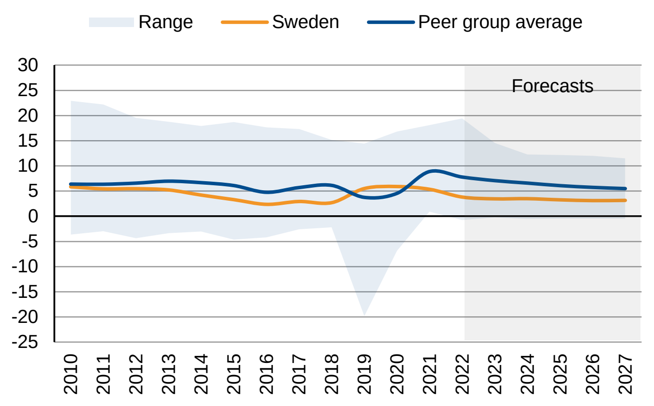
External Economic Risks

- **Current account:** Sweden has been running consistent, albeit declining, current account surpluses for the past two decades. The current account surplus widened to 5.9% of GDP in 2020, but preliminary estimates for 2022 indicate a decline to 3.8%. This will be mainly driven by a lower net export of goods including merchandise, manufactured goods and minerals, and by higher imports of services, in part due to a post-pandemic recovery in travel and business services. We expect the current account balance to stabilise at around 3.0%-3.5% of GDP in the medium term.
- **External position:** Sweden's external debt stood at 172.5% of GDP in 2022, 2 pp higher than in 2021, but significantly lower than in 2009, when it was around 200%. External debt is mainly related to financial institutions (57% of total external debt), intercompany lending (22%) and non-financial corporates (15%), while the central bank and government account for the remaining 6%. Sweden's international reserves, amounting to 12% of GDP in January 2023, provide a buffer against financial market volatility.
- **Resilience to shocks:** Official reserve assets averaged USD 43bn in 2022 (7% of GDP) and stood at USD 47.7bn in January 2023. It is important for Sweden to maintain an adequate level of foreign reserves due to Swedish banks' high dependence on wholesale funding in foreign currency, a funding source that can be disrupted in times of financial distress. The IMF's Financial System Stability Assessment (FSAP) of March 2023 found the Swedish banking system to be resilient to large liquidity shocks despite its substantial share of wholesale funding. In addition, the Riksbank demonstrated during the Covid-19 crisis that it can quickly establish swap facilities. The Swedish Krona has established itself as a regional safe-haven currency and now ranks as the sixth non-traditional reserve currency globally, behind the Swiss Franc and Korean Won. Sweden's net international investment position continues to improve and is expected to exceed 25% of GDP in 2022.

Overview of Scope's qualitative assessments for Sweden's *External Economic Risks*

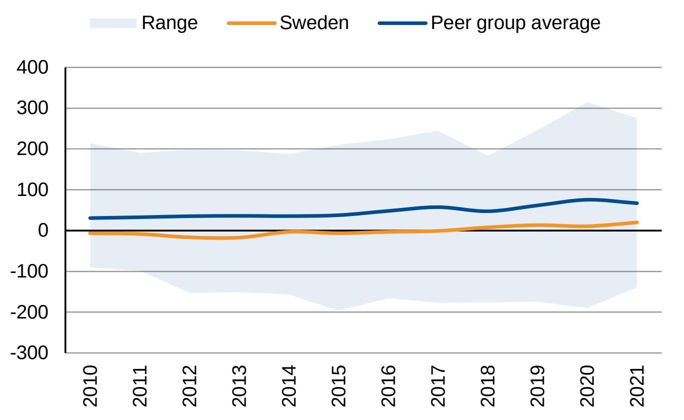
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aa-	Current account resilience	Neutral	0	External sector competitiveness underpins track record of current account surpluses
	External debt structure	Neutral	0	High external debt, especially in the financial institutions sector, in line with peers
	Resilience to short-term shocks	Strong	+1/3	Net external creditor position; regional safe-haven status of Swedish Krona

Current account balance, % of GDP



Source: IMF WEO, Scope Ratings

Net international investment position (NIIP), % of GDP



Source: IMF, Scope Ratings

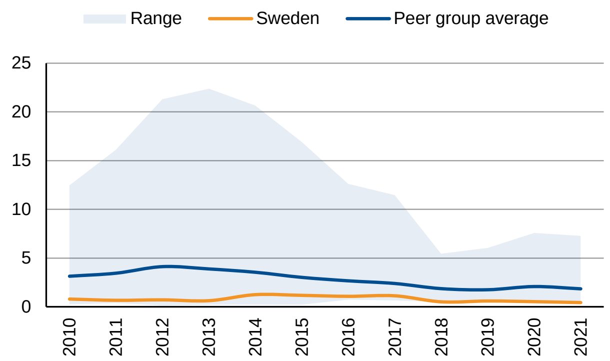
Financial Stability Risks

- **Banking sector:** The Swedish banking sector is large at around three times 2021 GDP. The sector is concentrated in five banks that are highly interconnected and dependent upon global financial markets for funding. Swedish banks are also highly exposed to the mortgage and commercial real estate sectors, though significant capital buffers, stable CET1 ratios in excess of 20% and low levels of non-performing loans dampen the associated risks. The Swedish Financial Supervisory Authority increased the countercyclical capital buffer to 2% effective from June 2023 in light of the slowing economy and rising interest rates. The rise in mortgage rates and the correction in house prices are posing a challenge for the banking sector as the largest banks account for 75% of mortgage lending. Systemic risks are now elevated but remain manageable. A major macro-financial shock, however, could still put banks' healthy capital levels under pressure. The latest FSAP stress tests indicate that the systemwide CET1 ratio could fall by 620bp, especially for banks heavily exposed to commercial real estate, but that no bank would fall below minimum capital requirements.
- **Private debt:** Private-sector debt stood at 269% of GDP as of Q3 2022, the highest among Nordic economies. Household debt has fallen over the past two years from a peak of 95% in Q1 2021 to 90% in Q3 2022. However, the household debt-to-income ratio has increased by more than 35 pp in the past 10 years and exceeded 200% in 2022. Household debt mainly relates to mortgages, which tend to have short maturities of two years or less and constitute around 50% of banks' lending portfolios. Non-financial corporate debt also remains near its peak, at 180% of GDP in Q3 2022. Highly leveraged commercial real estate companies especially face refinancing risk as market spreads widen, with non-bank debt above 40% of their total debt.
- **Financial imbalances:** The Booli index shows that real estate prices peaked in H1 2022. Real estate prices in some regions have subsequently fallen by just over 20%, reflecting a broad correction following the rapid rise in interest rates. As of February 2023, house and apartment prices are around 17% and 10% below their respective peaks. High private debt in combination with typically short rate fixation has led to a high sensitivity to interest rate changes. The interconnectedness of Sweden's financial system could amplify this risk in the event of a severe macro-financial shock. Large banks tend to finance mortgage loans using covered bonds held by insurance companies, pension funds and other banks.

Overview of Scope's qualitative assessments for Sweden's *Financial Stability Risks*

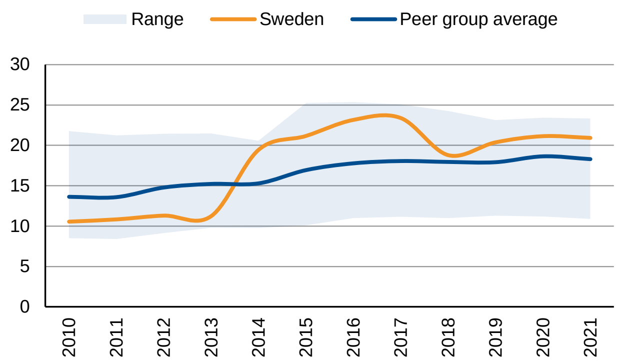
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Banking sector performance	Neutral	0	High bank capitalisation levels; dependent on global financial markets for funding
	Banking sector oversight	Neutral	0	Prudent oversight under Riksbank and Financial Supervisory Authority
	Financial imbalances	Weak	-1/3	High private-sector indebtedness, large size of the banking sector vis-à-vis the real economy and highly interconnected financial system; high interest rate sensitivity given short mortgage rate fixation

Non-performing loans, % of total loans



Source: World Bank, Scope Ratings

Tier 1 ratio, % of risk-weighted assets



Source: IMF, Scope Ratings

ESG Risks

- **Environment:** Sweden is on track to meet its EU greenhouse gas emission reduction target of 50% by 2030. Other aims include meeting 100% of electricity needs from renewable sources by 2040 and becoming a net-zero economy by 2045. Even so, the Climate Policy Council of Sweden believes policies need to go further to achieve carbon neutrality by 2045. In 2021, around 29% of energy consumption came from fossil fuels, 22% from nuclear and 49% from renewable sources, in particular hydropower. The country has a low dependence on natural gas, accounting for 2% of total energy consumption, but still a high dependency on oil (25%). Sweden was one of the first countries to implement a carbon tax (in 1991) and imposes SEK 1,200 (around EUR 110) per tonne, among the highest levels worldwide, although still applied to a limited share of emitting sectors.

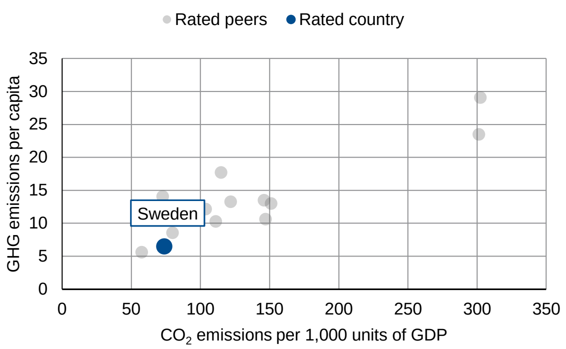
- **Social:** Sweden has relatively favourable demographics when compared with highly rated peers, with a working age population projected to remain stable over the medium term, as well as an advanced social safety net that contributes to low income-inequality. The national employment rate is well above the EU average (76.8% of the total population aged 15 to 64 in Q4 2022 against an EU average of 70.1%) and the gender-employment gap is among the lowest in the EU (5.8% of the total population in 2021 against 10.6%). The digital skills level is also very high compared with other EU countries.

- **Governance:** Following the general elections in September 2022, the right-wing block including the Moderates, Sweden Democrats, Christian Democrats and Liberals secured 176 of the 349 seats in the Riksdag, against 173 seats obtained by the Centre-Left, which includes the Social Democrats. The Moderates leader Ulf Kristersson subsequently formed a minority coalition government with the Christian Democrats and the Liberals. The anti-immigration Sweden Democrats, which emerged as the largest right-wing party, will not be an official member of the government, but the four parties will pursue a unified government policy. The coalition is expected to take a tougher stance on immigration and refugees, introduce criminal justice reforms and remain committed to climate change goals. Significant compromise among coalition partners will be needed to agree and implement some of these reforms.

Overview of Scope's qualitative assessments for Sweden's *ESG Risks*

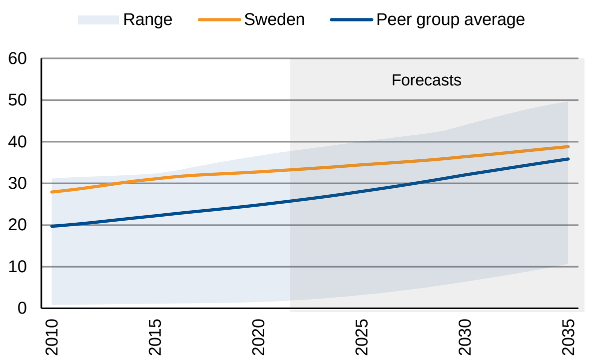
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Environmental factors	Strong	+1/3	High environmental standards, ambitious targets for achieving carbon neutrality by 2045 and very high carbon taxes
	Social factors	Neutral	0	Relatively favourable demographics compared with peers, advanced social safety net and healthy labour market
	Governance factors	Strong	+1/3	High-quality institutions and stable political environment

CO_2 emissions per GDP and per capita, $mtCO_2e$



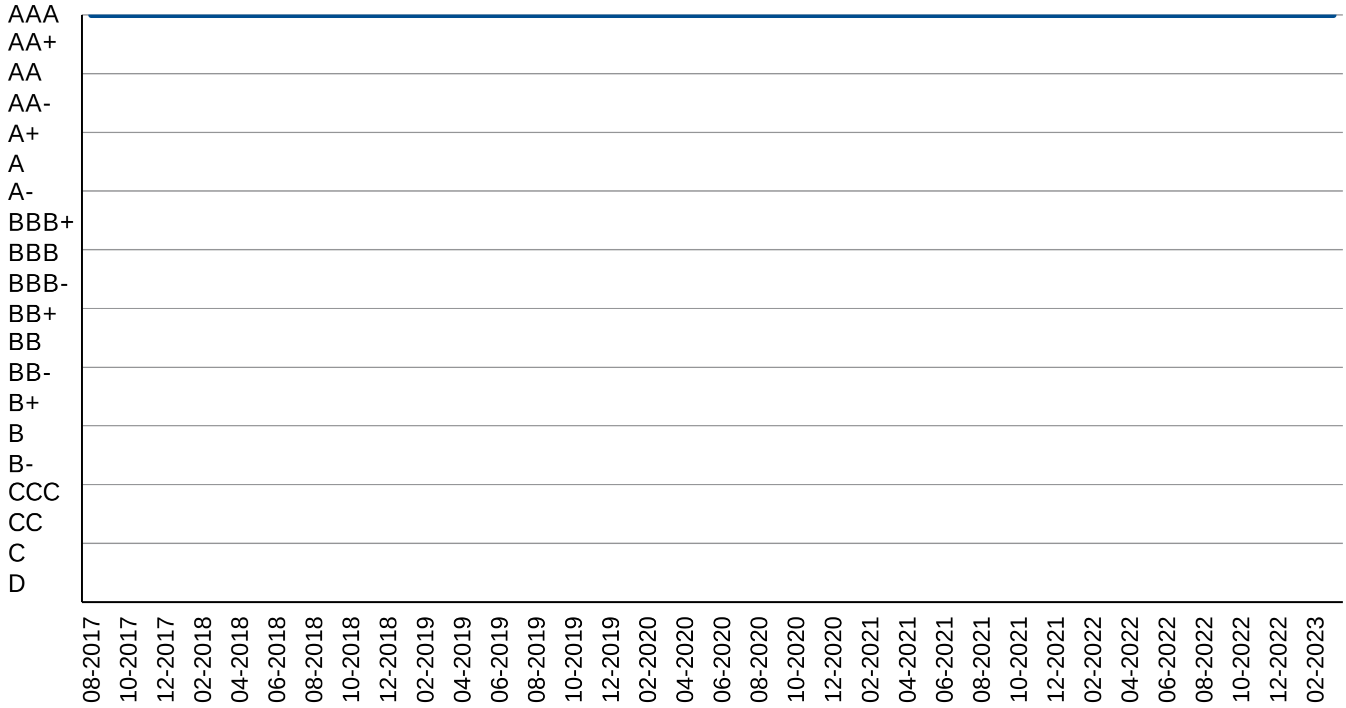
Source: European Commission, Scope Ratings

Old age dependency ratio, %



Source: United Nations, Scope Ratings

Appendix I. Rating history



NB. Positive/Negative Outlooks are treated with a +/-0.33-notch adjustment. Credit Watch positive/negative with a +/-0.67-notch adjustment.

Appendix II. Rating peers

Rating peers are related to sovereigns with an indicative rating in the same rating category or in adjacent categories per Scope's Core Variable Scorecard embedding a methodological reserve-currency adjustment.

Peer group*
Denmark
Finland
Germany
Ireland
Luxembourg
Netherlands
Norway
Sweden
Switzerland

*Publicly rated sovereigns only; the full sample may be larger.

Appendix III. Statistical table for selected CVS indicators

Pillar	Core variable	Source	2017	2018	2019	2020	2021	2022
Domestic Economic	**GDP per capita, USD '000s**	IMF	53.5	54.3	51.7	52.7	60.8	56.4
	Nominal GDP, USD bn	IMF	541.0	555.5	533.9	547.1	635.7	603.9
	Real growth, %	IMF	2.6	2.0	2.0	-2.2	5.1	2.6
	CPI inflation, %	IMF	1.9	2.0	1.7	0.7	2.7	7.2
	Unemployment rate, %	WB	6.7	6.4	6.8	8.3	8.7	-
Public Finance	**Public debt, % of GDP**	IMF	40.7	38.9	34.9	39.2	36.8	33.5
	Interest payment, % of revenue	IMF	-0.1	-0.1	-0.1	-0.2	-0.2	-0.3
	Primary balance, % of GDP	IMF	1.4	0.8	0.5	-2.9	-0.4	0.0
External Economic	**Current account balance, % of GDP**	IMF	3.0	2.7	5.5	5.9	5.4	3.8
	Total reserves, months of imports	IMF	2.8	2.5	2.4	2.8	2.4	-
	NIIP, % of GDP	IMF	-1.2	7.9	12.5	9.9	21.0	-
Financial Stability	**NPL ratio, % of total loans**	IMF	1.1	0.5	0.6	0.5	0.4	-
	Tier 1 ratio, % of risk-weighted assets	IMF	23.2	23.1	18.5	18.8	21.1	20.2
	Credit to private sector, % of GDP	WB	131.3	131.9	131.1	137.8	-	-
ESG	**CO_2 per EUR 1,000 of GDP, mtCO₂e**	EC	86.8	80.7	77.7	73.9	70.4	-
	Income share of bottom 50%, %	WID	24.1	24.3	24.3	23.8	23.8	-
	Labour-force participation rate, %	WB	82.7	83.0	83.1	-	-	-
	Old-age dependency ratio, %	UN	32.0	32.2	32.5	32.8	33.1	33.4
	Composite governance indicators*	WB	1.7	1.7	1.7	1.6	1.6	-

This table presents a selection of the indicators (24 out of 29 – with the governance indicator reflecting a composite of six indicators) used in Scope's quantitative model, the Core Variable Scorecard.

[1] Forecasted values are produced by Scope
[2] Average of the six World Bank Worldwide Governance Indicators
Source: European Commission, IMF WEO, World Bank, Scope Ratings

Appendix IV. Economic development and default indicators

IMF Development Classification	Advanced economy
5y USD CDS spread (bps) as of 31 March 2023	15.9

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