Kingdom of Sweden
Rating Report

AAA STABLE OUTLOOK

Credit strengths

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

Credit challenges

- High levels of household and corporate debt
- Elevated risk of a market correction in the housing market

Rating rationale:

Wealthy, diversified economy: Sweden's economy recovered quickly from the Covid crisis. Growth in 2021 was supported by private consumption, investments and contact-related services. Direct impacts from the Russia-Ukraine war have been low given weak trade linkages.

Robust fiscal framework and low public debt ratio: A credible fiscal policy framework enabled the government to implement an effective fiscal response to the Covid-19 pandemic with a focus on the green transition and inclusion objectives. It also puts the government in a strong position to shield households from rising energy prices and increase 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, the latter shields the country from short-term shocks.

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

Sweden's sovereign rating drivers

Risk pillars		Quantitative scorecard		Reserve currency adjustment (notches)	Qualitative scorecard	Final rating
		Weight	Indicative rating		Notches	
Domestic Economic Risk		35%	aaa	Reserve currency adjustment (notches)	+1/3	AAA
Public Finance Risk		25%	aaa		+2/3	
External Economic Risk		10%	aa		+1/3	
Financial Stability Risk		10%	aaa		-1/3	
ESG Risk	Environmental Risk	5%	aaa		+1/3	
	Social Risk	5%	bbb+		0	
	Governance Risk	10%	aaa		+1/3	
Overall outcome		**aaa**		**0**	**+2**	

Note: The sum of the qualitative adjustments, capped at 1 notch per rating pillar, is weighted equally and 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 Ratings' methodology. Source: Scope Ratings GmbH

Outlook and rating triggers

The Stable Outlook reflects Scope's 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

- Sharp correction in the housing market damaging household and banking system balance sheets
- Significant deterioration in the fiscal outlook

Ratings and Outlook

Local and foreign 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

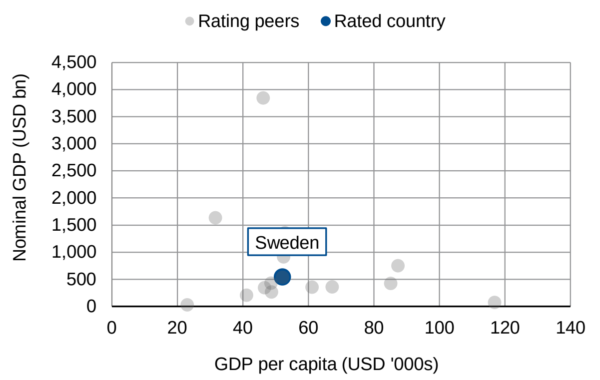
Domestic Economic Risks

- **Growth outlook**: After a contraction of 2.8% of GDP in 2020 due to the Covid-19 crisis, the Swedish economy is estimated to have grown by 4.8% in 2021 on the back of strong private consumption as well as recovering investments and contact-related services. Due to rising inflationary pressures since December 2021, GDP growth is expected to have slowed in the first quarter but to recover subsequently as household consumption normalises and supply bottlenecks ease. We expect GDP growth of 2.6% in 2022 and 2.3% in 2023. While Sweden is not isolated from rising global inflationary pressure, the direct impact on the Swedish economy from the Russia-Ukraine war has been contained so far as both countries absorb less than 3% of Swedish exports.
- **Inflation and monetary policy**: Following a period of very low inflation over the past two years, the inflation rate in Sweden has been increasing rapidly since December reaching 6.1% in March 2022 driven by higher energy prices. The Riksbank's Monetary Policy Committee decided in February to keep the repo rate unchanged at 0% and continue to purchase securities to compensate for maturing assets. Total asset holdings are expected to remain stable this year before decreasing gradually starting from next year. However, we expect that the rapid rise in inflation, which has intensified during the war in Ukraine, is likely to lead to an earlier policy rate hike than previously anticipated. Besides containing medium-term inflation expectations, this will also support the krona, which has rebounded after depreciating by 8% between November and February. We currently expect a gradual monetary tightening with one policy rate rise of 0.25pp in 2022 and a similar increase in 2023.
- **Labour market**: Sweden's labour market is recovering strongly following the Covid-19 shock. The unemployment rate fell to 7.3% in February 2022, near pre-pandemic levels. While the number of people unemployed for more than 12 months initially increased, the rate has fallen by 3.75pp since December 2021. This was accompanied by a rise in the labour force participation rate, which is at historically high levels (73.7%) supported by higher participation rates among older and foreign-born workers. We expect the unemployment rate to fall gradually over the next two years, reaching 6.9% in 2023.

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

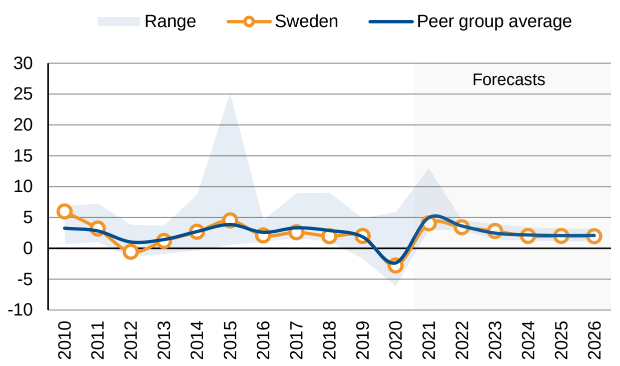
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Growth potential of the economy	Neutral	0	Moderate growth potential
	Monetary policy framework	Neutral	0	Riksbank is a credible and effective monetary authority
	Macro-economic stability and sustainability	Strong	+1/3	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 '000s



Source: IMF, Scope Ratings GmbH

Real GDP growth, %



Source: IMF, Scope Ratings GmbH

Public Finance Risks

- **Fiscal outlook**: The strength and resilience of the public finance position enabled the government to adopt a large package of fiscal measures amounting to SEK 400bn for 2020-21 (7.5% of 2021 GDP) and an additional SEK 1trn (18.8% of 2021 GDP) in various forms of loans and guarantees. Government projections published in April show that the 2021 budget deficit was smaller than expected at -0.2% of GDP versus an earlier projection of -0.8%. This was supported by the rapid economic recovery, which led to higher tax revenues and dividends from state-owned enterprises. The government budget balance is expected to reach -0.5% in 2022 as Covid-19 support measures are phased out and then turn into a surplus of 0.7% in 2023.

  The government announced a broad set of measures in March amounting to around 0.3% of 2021 GDP to support households in light of rising energy prices. The measures include a reduction to petrol prices (SEK 3.7bn), compensation payments for car owners (SEK 4bn), further support for electric car purchases (SEK 3.9bn), continued compensation payments to households for high electricity costs (SEK 900m), and increased housing allowances for families (SEK 500m).

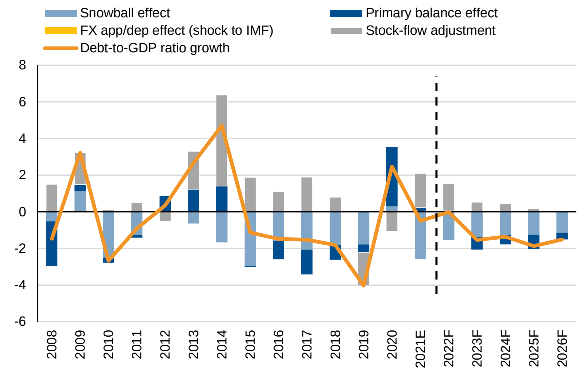
- **Debt trajectory**: Due to better-than-expected budget deficit figures, we expect public debt levels to continue their downward trend. The debt-to-GDP ratio increased from 35% in 2019 to just over 37% in 2020. We expect this ratio to reach its pre-pandemic level next year and then fall further to 31% by 2026. The debt level would therefore shift towards its lower limit of the 35% (+/-5%) of GDP threshold highlighted in the fiscal framework. This debt level is one of the lowest among EU Member States.

- **Market access**: Sweden benefits from strong market access and low financing costs. The 10-year government bond yield has been volatile since the fourth quarter of 2021. It decreased from 0.4% in October to 0.2% in December but then rose to around 0.8% at the end of March because of rising inflationary pressure and an expectation of an earlier policy rate hike. Due to the stronger budget balance, borrowing requirements for 2021-23 will be SEK 84bn lower than previously forecasted, and interest payments will continue to have a minor impact on the budget balance. The debt office is cancelling its planned bond issuance in foreign currency in 2022 and has lowered the issuance volume of both inflation-linked and nominal government bonds.

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

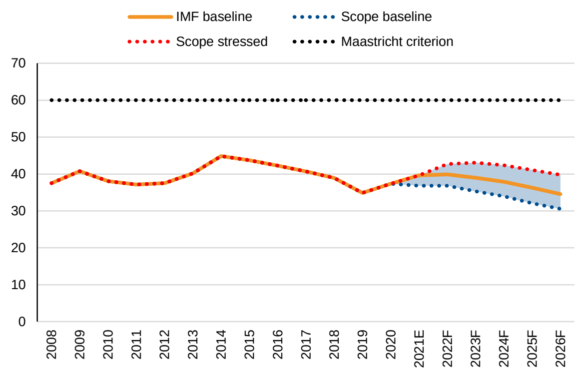
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Fiscal policy framework	Strong	+1/3	Appropriate countercyclical response to the Covid-19 crisis, track record of prudent fiscal policies
	Debt sustainability	Strong	+1/3	Declining public debt trajectory in the mid to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

Contributions to changes in debt levels, pps of GDP



Source: Scope Ratings GmbH

Debt-to-GDP forecasts, % of GDP



Source: Scope Ratings GmbH

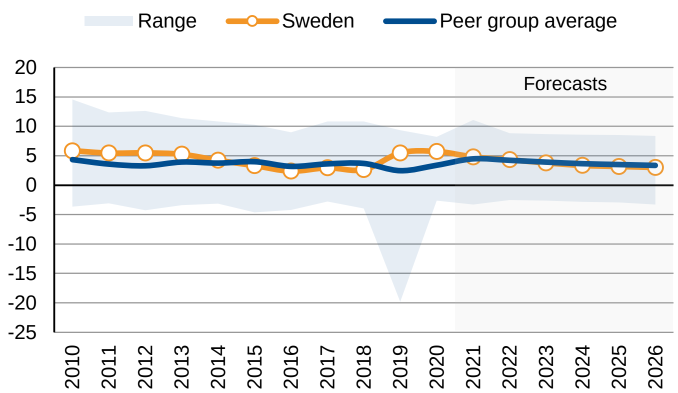
External Economic Risks

- **Current account**: Sweden has been running consistent, albeit declining, current account surpluses for the past two decades. The current account surplus widened to 5.7% of GDP in 2020 then fell slightly to 5.5% in Q4 2021. The current account balance is supported by exports of goods – especially machinery and chemicals – and lower domestic demand for external goods and travel services, which has reduced imports. Exports increased by around 7% in 2021 but are likely to slow this year as companies continue to report supply chain disruptions. Service exports are also expected to be temporarily weaker given containment measures, which reduced tourism levels in Sweden. The IMF projects the current account balance will gradually decline towards 3% over the medium term.
- **External position**: Sweden's external debt stood at 173.7% of GDP in 2021, 8pps higher than in 2020, but significantly lower compared with 2009 debt levels of around 200% of GDP. External debt is mainly related to financial institutions (54% of total external debt), intercompany lending (22%) and non-financial corporates (17%), while the central bank and government account for the remaining 7%. Liquidity international reserves amounted to 9.1% of GDP in February 2022, providing a buffer against financial market volatility.
- **Resilience to shocks**: Official reserve assets averaged USD 44bn in 2021 and fell to USD 42.3bn in February 2022. Given Swedish banks' high dependence on wholesale funding in foreign currency and the disruptions that can occur to such funding in times of financial distress, it is important for Sweden to maintain adequate levels of foreign reserves. Trade shocks due to the Russia-Ukraine conflict are expected to be limited for Sweden as Swedish trade with Ukraine is low, amounting to less than 1% of exports and imports. Russia makes up only 1.3% of total exports, and imports from Russia are low as well given that Sweden mainly sources its energy domestically.

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

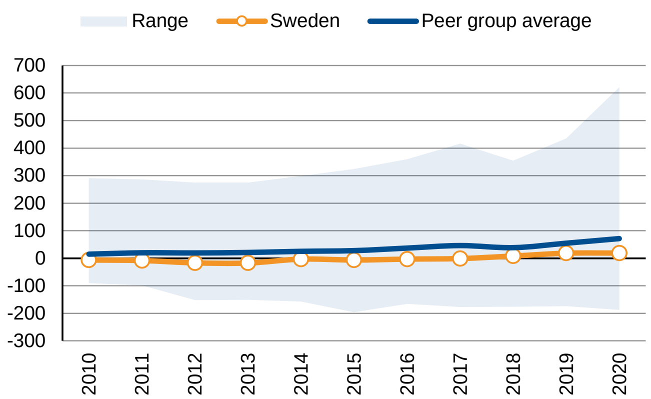
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aa	Current account resilience	Neutral	0	External sector competitiveness underpins track record of current account surpluses
	External debt structure	Neutral	0	High external debt, especially as concerns the financial institutions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

Current account balance, % of GDP



Source: IMF, Scope Ratings GmbH

NIIP, % of GDP



Source: IMF, Scope Ratings GmbH

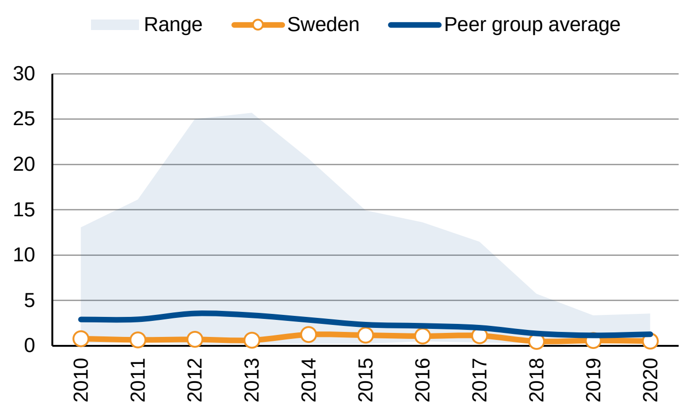
Financial Stability Risks

- **Banking sector**: The Swedish banking sector is large. It is concentrated in five major banks that are highly interconnected and dependent upon global financial markets for funding. The sector remained resilient during the Covid-19 crisis, supported by significant capital buffers, stable CET1 ratios of around 20% and low levels of non-performing loans. Liquidity buffers strengthened from the start of 2020, and profitability was robust as earnings and returns on assets started to improve last year, easing the absorption of any credit losses. Given the robust economic recovery in 2021, the Financial Supervisory Authority decided to increase the countercyclical capital buffer to 1% in September 2021, effective September 2022. Major banks have also started issuing dividends to shareholders in Q4 2021 following a temporary ban on such payments.
- **Private debt**: Swedish households continue to show high and increasing debt levels. They were approximately 7% higher in December 2021 than one year earlier given the sharp increase in house prices during the pandemic. Households' debt-to-income ratio reached almost 200% on average in 2021, and the IMF expects this to increase to 211% by 2024. Households are therefore increasingly sensitive to price drops in the housing market and rising interest expenses. Debt levels of non-financial corporations also remain high at 124% of GDP in 2021, with a 9% increase in outstanding volumes of issued securities in Q1 2022 compared to the same period last year.
- **Financial imbalances**: The HOX Index (which measures Swedish real estate prices) averaged around 285 during 2021, increasing 9.7% in February 2022 compared to the same month last year. One of the main vulnerabilities in the Swedish banking sector relates to its growing exposure to the commercial real estate sector, representing between 10% and 25% of banks' lending. Additional risks for the banking sector stem from the exposure of some of the main banks, such as Swedbank AB and Skandinaviska Enskilda Banken AB (SEB), to the Baltic region, which may be among the most affected from the Russia-Ukraine war.

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

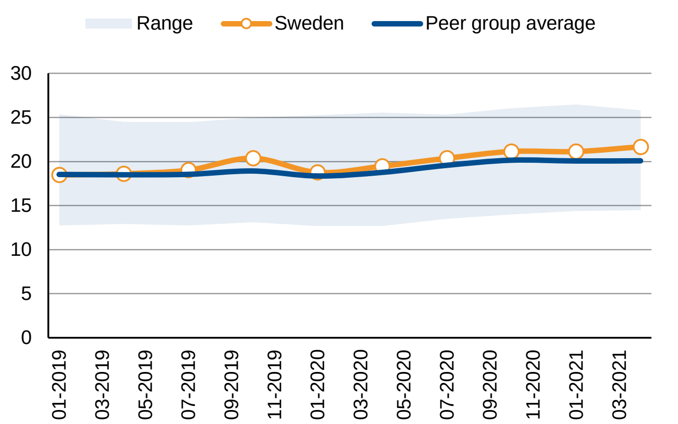
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Banking sector performance	Neutral	0	High bank capitalisation levels, dependent on global financial markets for funding
	Banking sector oversight	Neutral	0	Prudent oversight under Riksbank and FSA
	Financial imbalances	Weak	-1/3	High private-sector indebtedness, large size of the banking sector vis-à-vis the real economy, high interconnectedness in the financial system

NPLs, % of total loans



Source: IMF, Scope Ratings GmbH

Tier 1 ratio, % of risk-weighted assets



Source: IMF, Scope Ratings GmbH

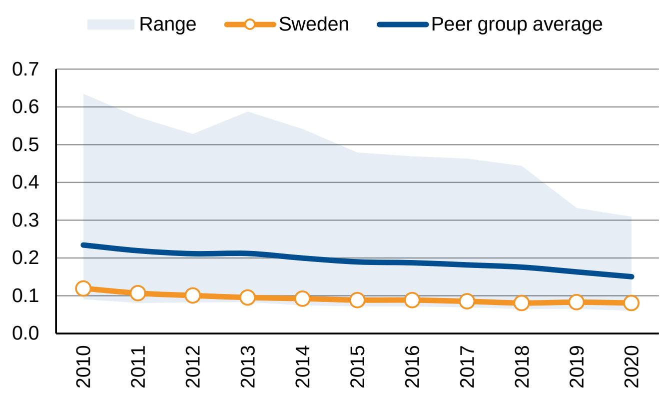
ESG Risks

- **Environment**: Sweden is on track to meet its EU greenhouse gas (GHG) emission reduction target of 50% by 2030. In addition, it aims to meet 100% of its electricity needs from renewable sources by 2040 and become a net-zero economy by 2045. In 2020, around 30% of energy consumption came from fossil fuel, 22% from nuclear and 46% from renewable sources, in particular hydropower. The country has a low dependence on natural gas, which accounts for only 2% of its total energy supply. Of that, approximately half is imported from Russia, along with just 8% of Sweden's total crude oil imports, mitigating risks of shortages or supply disruptions. Sweden was one of the first countries to implement a carbon tax in 1991 and currently imposes it at about USD 140 per tonne, which is the highest level in the world.
- **Social**: Sweden has relatively favourable demographics, with a working age population projected to remain stable over the medium term, and an advanced social safety net, contributing to low income inequality. The national employment rate is well above the EU average (74.9% of the total population in 2020 vs an EU average of 67.1%) and the gender-employment gap is among the lowest in the EU (5.4% of total population in 2020 vs 11%). The level of digital skills is very high.
- **Governance**: Prime Minister Stefan Löfven resigned in August 2021 after having lost the support of the governing coalition, which comprises the centre-left Social Democratic Party, the Green Party and the centre-right Liberal and Centre parties. Finance Minister Magdalena Andersson replaced him in November, becoming the first female prime minister in the country's history. As the parties in the governing coalition did not fully support the proposed budget, she now leads a one-party minority government. An ongoing commitment to implement the previously agreed budget measures means significant future reforms could prove challenging. Nevertheless, her party still leads the polls ahead of the next election, which is scheduled for September 2022.

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

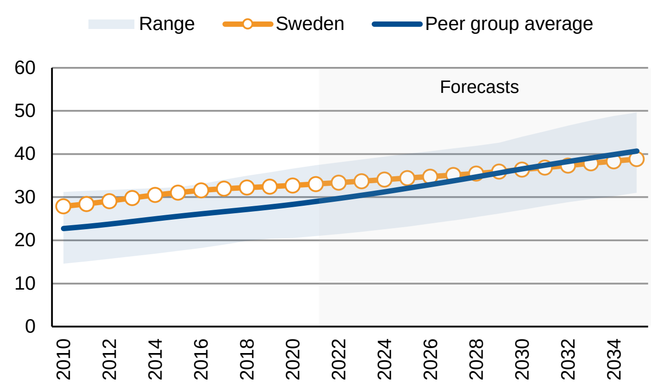
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Environmental risks	Strong	+1/3	High environmental standards, ambitious targets for achieving carbon neutrality by 2045, very high carbon taxes
	Social risks	Neutral	0	Relatively favourable demographics, advanced social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

CO_2 emissions per GDP, MTCO2e



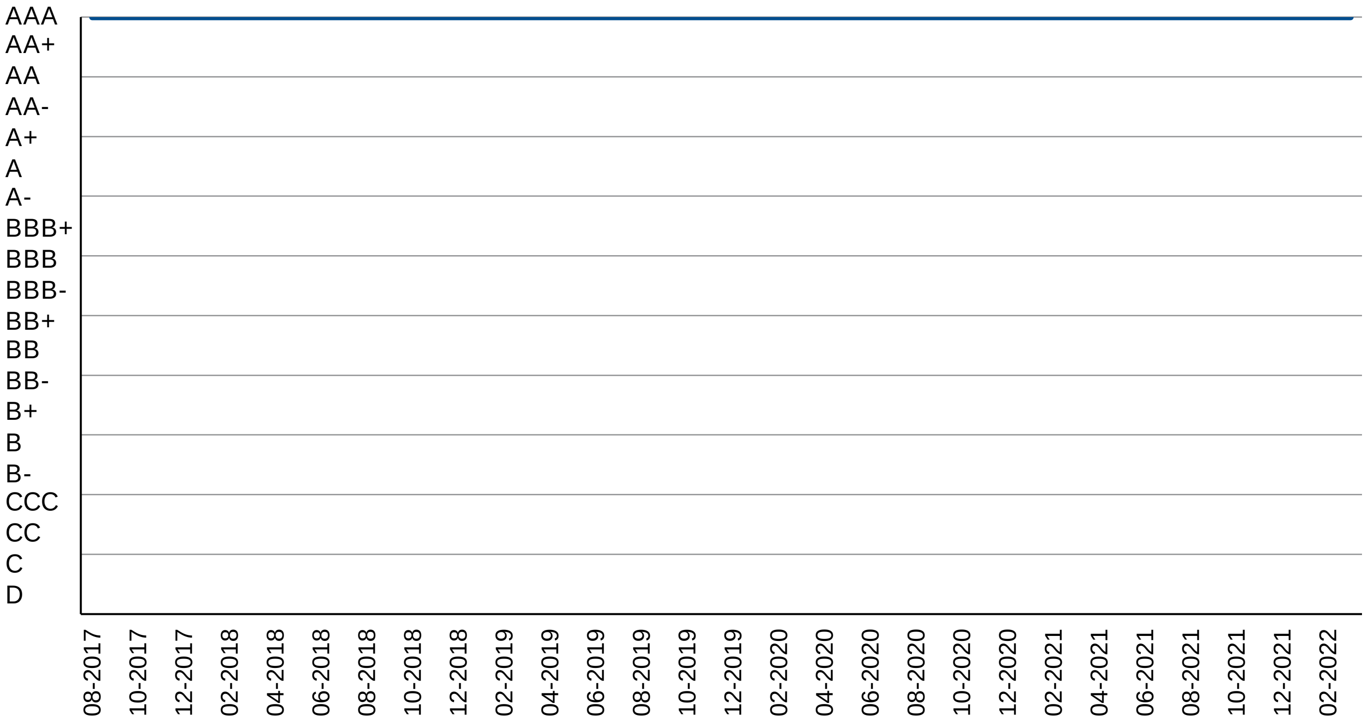
Source: European Commission, Scope Ratings GmbH

Old age dependency ratio, %



Source: United Nations, Scope Ratings GmbH

Appendix I. Rating history



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.

Peer group*
Austria
Denmark
Estonia
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

This table presents a selection of the indicators (24 out of 29) used in Scope's quantitative model, the Core Variable Scorecard.

	2016	2017	2018	2019	2020	2021E	2022F	2023F
Domestic Economic Risk								
GDP per capita, USD '000s	51.6	53.5	54.3	51.7	52.1	58.6	61.7	65.8
Nominal GDP, USD bn	515.7	541.0	555.5	533.9	541.1	622.4	660.9	711.2
Real growth, %[1]	2.1	2.6	2.0	2.0	-2.8	4.8	2.6	2.3
CPI inflation, %	1.1	1.9	2.0	1.7	0.7	2.7	4.8	2.2
Unemployment rate, %[1]	7.0	6.7	6.3	6.8	8.3	8.8	7.1	6.9
Public Finance Risk								
Public debt, % of GDP[1]	42.3	40.7	38.9	34.9	37.3	36.8	36.8	35.3
Interest payment, % of government revenue	0.0	-0.1	-0.1	-0.2	-0.4	-0.4	0.2	0.1
Primary balance, % of GDP[1]	1.0	1.4	0.8	0.4	-3.2	-2.8	-0.8	-0.2
External Economic Risk								
Current account balance, % of GDP	2.4	3.0	2.6	5.5	5.7	5.5	4.9	4.4
Total reserves, months of imports	2.88	2.83	2.51	2.40	2.77	-	-	-
NIIP, % of GDP	-3.3	-0.9	8.1	16.8	18.0	-	-	-
Financial Stability Risk								
NPL ratio, % of total loans	1.1	1.1	0.5	0.6	0.5	-	-	-
Tier 1 ratio, % of risk-weighted assets	23.2	23.4	18.8	20.4	21.1	21.1	-	-
Credit to private sector, % of GDP	128.5	131.3	131.9	131.1	139.2	-	-	-
ESG Risk								
CO_2 per EUR 1,000 of GDP, $MTCO_2e$	88.3	85.0	80.6	82.7	80.6	-	-	-
Income quintile share ratio (S80/S20), x	4.7	4.5	4.9	-	-	-	-	-
Labour force participation rate, %	82.3	82.7	83.0	83.1	-	-	-	-
Old age dependency ratio, %	31.6	32.0	32.2	32.5	32.8	33.1	33.4	33.7
Composite governance indicator[2]	1.7	1.7	1.7	1.7	1.6	-	-	-

[1] Forecasted values are produced by Scope and may differ from those presented in the charts of the previous sections.
[2] Average of the six World Bank Governance Indicators
Source: European Commission, IMF, World Bank, Scope Ratings GmbH

Appendix IV. Economic development and default indicators

IMF Development Classification	Advanced economy
5y USD CDS spread (bps) as of 22 April 2022	11.5

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