

## Macro Focus

### Swedish Green Bond: Time for issuance

- ▶ Good timing for green bond issuance and an important political signal for Sweden
- ▶ New playing field for state finances but deficit not as dramatic as expected this year
- ▶ The green bond will support spending towards Sweden's environmental targets

In the upcoming weeks the Swedish National Debt Office will issue a green bond (7-10 years) for the first time and we expect it to meet a great deal of interest. The funding raised with the selected bond will cover spending that contributes to progress towards Sweden's environmental targets.

#### Time for the National Debt Office's new green bond

The Swedish National Debt Office (SNDO) announced in July that the intention is to choose a maturity within the range of seven to ten years for its green bond, scheduled for issuance in late August/early September. Swedbank (joint lead manager) and a group of banks has been mandated to explore investor interest and then execute the sale of approximately SEK 20 billion (0.4% of GDP). According to the Government's framework for green bonds, the ceiling for the possible issue volume was set at SEK 30 billion. The green bond will be issued in Swedish kronor and under the Debt Office's program for Euro Medium Term Notes (EMTN). The final maturity will be set and communicated as the terms of issuance are announced towards the end of August.

#### Green bonds help direct funding towards green investments

Green bonds are tied to spending that furthers emission reductions or other environmental goals. The idea is to attract funding to green projects with favorable conditions and to enable investors to avoid fossil fuels related projects. Many influential global investors have already implemented green criteria. Green bonds may have sold at lower yields compared to otherwise similar assets in recent years, although this is hard to prove empirically and likely varies across bonds and issuers. Green bonds also hold important signal value: the issuers credibly bind themselves to green spending, which strengthens confidence in climate policy. The Swedish government also highlights that its issuance of a green bond could increase the legitimacy of the green bonds market and lower the threshold for other actors to do the same.

#### The bond will finance spending towards Sweden's environmental targets

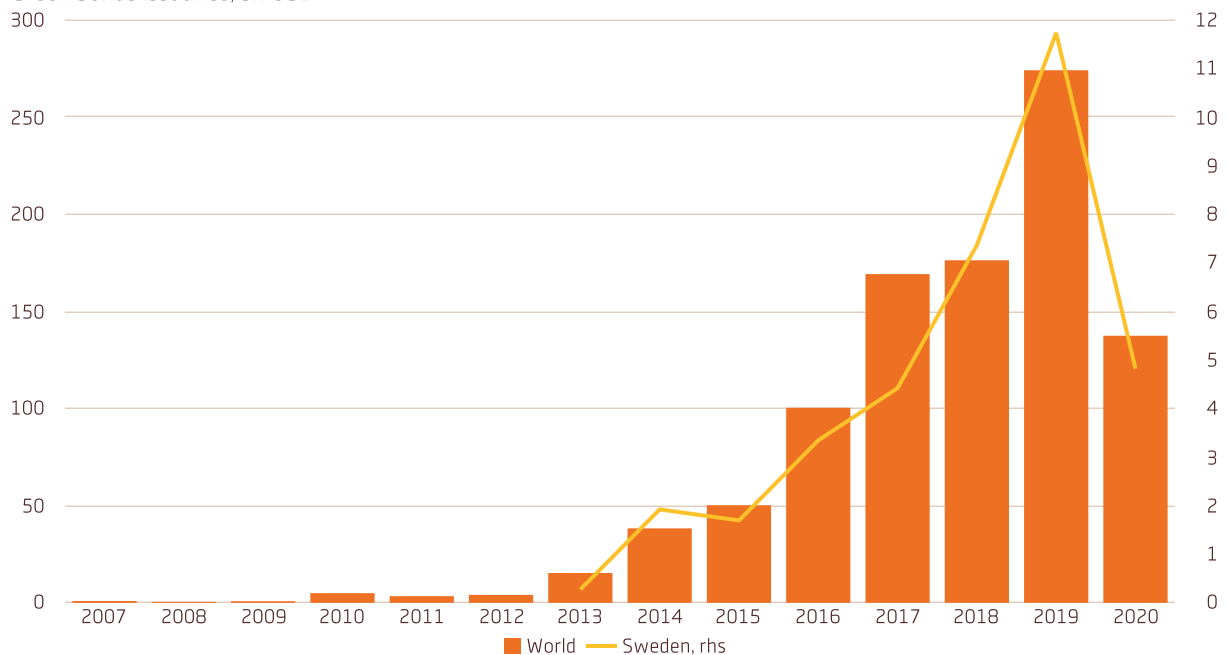
Green bonds are graded by an external evaluator. The Swedish government's green bond has been labelled "dark green" by the research center CICERO, which means that it targets spending in areas with considerable long-term climate benefits and meets a high regulatory and transparency standard. In line with the government's green bond framework, the bond will be used to support spending that contributes to progress towards Sweden's environmental targets. Funds will be allocated to expenditures from the previous and current year's accepted state budgets. According to the report by CICERO, 67 % of the first round of issuance will be directed to clean transportation, most of this on electrified railways. The rest will be allocated to green spending related to energy, climate, industry, and agricultural policy and to more general nature conservation.

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### Green bonds issuance has increased rapidly

Green bonds issuance, bn USD



Sources: BNEF, Swedbank Research & Macrobond

The Swedish government's climate and environmental spending has increased considerably over the past few years and was estimated at SEK 12.5 billion in the budget proposal for 2020. We believe that Sweden's green spending will increase further in the coming years, especially as the government is likely to finance "green stimulus" projects after the corona crisis. This will likely mean investments in areas such as power grid networks, energy efficiency in buildings, electric transport, and hydrogen. Set in the context of Sweden's environmental policy, the SEK 20 billion raised with the green bond will finance a considerable chunk of spending, but it will only be used to cover spending from 2019 and 2020: green subsidies and investments will continue to push up lending and more green bonds could be issued in the future.

### New playing field for state finances in the wake of the corona crisis

In its latest forecast (Government Borrowing- Forecast and Analysis 2020:2, May 19th) the Debt Office expected a large deficit in the central government budget and an increase in government debt due to the coronavirus. Support measures and a shrinking economy (The Debt Office expected GDP to fall by 6.5 % this year) were expected to put a strain on the budget. A deficit of SEK 402 billion was expected for this year and SEK 76 billion for 2021. To meet the increased borrowing requirements, the Debt Office is now increasing borrowing in all debt types. In view of the sudden and sharp increase in borrowing needs, the timing of the introduction of a green bond is well chosen. The NDO has increased the volume ambition for the green bond, from approximately SEK 10 billion to SEK 20 billion.

At the beginning of the year, there were concerns in the bond market that a green bond would risk crowding out the issue space for ordinary bonds. At present, there is a very high demand for Swedish government bonds and we also expect that the green bond will meet a great deal of interest. Still, the green bond will still only cover a small share of the total central government debt which currently amounts to SEK 1 180 billion and in May was expected to increase to SEK 1 556 bn in 2021. Given the new playing field for the state finances the possibilities to broaden the scope of the loan portfolio have increased and the NDO will also issue an ultra-long bond with a maturity of 25 years in November for SEK 10 bn with the possibility to increase issuance if the demand is high.

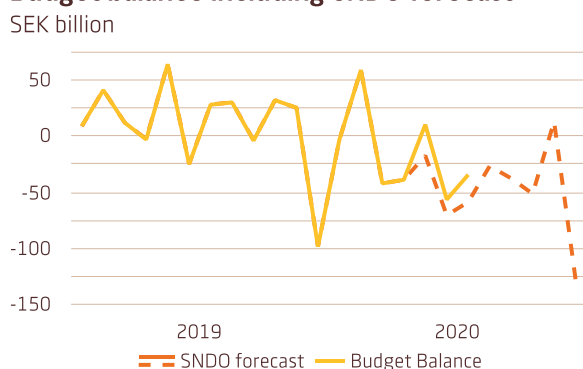
**NDO's government borrowing forecast in May (SEK billion)**

	2020	2021
Nominal government bonds	97 (51)	115 (60)
Inflation-linked bonds	13 (9)	17 (9)
Green bonds	20	0
Treasury bills (outstanding stock, year-end)	220 (55)	250 (68)
Liquidity management instruments	232 (113)	110 (43)
Foreign currency bonds (excl., Riksbank)	44 (0)	29 (0)
Foreign currency bonds (incl., Riksbank)	105 (59)	78 (48)
<b>Net borrowing requirement</b>	<b>402 (14)</b>	<b>76 (14)</b>

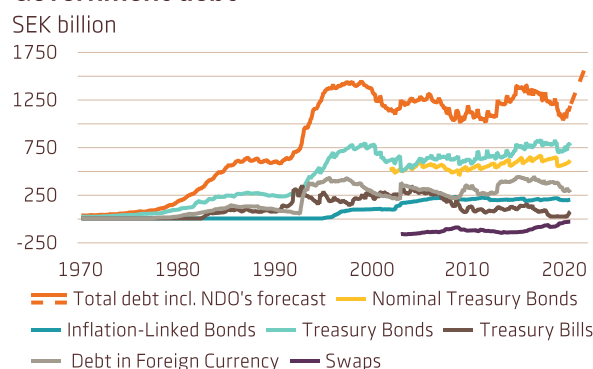
Note: NDO's forecast from February in parentheses. Note: In May, the volume of the green bond was not yet determined, and the original plan was SEK 10 billion. Liquidity management includes commercial papers in foreign currency

**Government finances clearly better than expected in the most recent months**

Swedish central government payments resulted in a deficit in the period May-July of SEK 80.7 billion. The Debt Office's forecast was a deficit of SEK 147 billion. The deviation is largely due to higher tax income than forecasted. Furthermore, payments to local governments were SEK 21 billion higher than forecasted. However, the higher payments to local governments were largely due to a redistribution between months. Approximately SEK 15 billion of these payments were forecasted to take place during other months in 2020. The Debt Office has been very explicit regarding their options in a worse or a better scenario. In a better scenario, which now seems very likely given that the government finances have developed better than expected and the economic outlook has improved since May, short-term funding will decrease. The largest revisions to the May forecast were made within short-term funding, liquidity management and the auctions of treasury bills and this is mainly due to the uncertainty for state finances in the longer run. However, it's likely that we will continue to see deficits in 2021 and 2022. Only relatively small changes are thus expected in the borrowing need for government bonds. If the outcome for the budget balance were to be better than forecasted, the Debt Office suggests that they could reduce borrowing again as the short-term loans mature. Instead, if the borrowing requirements would increase it could also increase the borrowing in foreign currency (bonds and commercial paper) if additional SEK borrowing is not considered appropriate.

**Budget balance including SNDO forecast**

Sources: Swedbank Research & Macrobond

**Government debt**

Sources: Swedbank Research & Macrobond

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