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Flash Comment

Swedish Debt Office

One factor we have discussed in our strategic view of the Swedish bond market is related to the government's decision late last year to raise the target for the total amount of bonds (currently SGB1056 and SGB1053) with maturity longer than 12 years from SEK60bn to SEK70bn. The present amount in these bonds is roughly SEK53bn. For this reason, we have advised investors to look out for signals of increased supply in the two longest bonds when the Debt Office releases its new borrowing forecast on 20 February. However, the Debt Office's Head of Funding Thomas Olofsson in a Reuters interview stressed that the Debt Office sees no rush to reach the target and that it sees limited interest from investors for more supply of such long risk. Eventually, the Debt Office will 'test the market' by issuing the longest bonds in the regular biweekly auctions, i.e. a relatively gradual approach with the timeframe depending largely on market interest.

Olofsson also mentioned that macroeconomic risks are roughly the same as was the case in October when the Debt Office made its previous borrowing forecast (SEK55bn for 2013 and SEK56bn for 2014), so from this point of view Olofsson sees no reason why any significant revisions would be required.

This reduces the risk of a 'rapid' increase in the supply of ultra-long bonds. At the same time, at some point, the Debt Office needs to approach the target established by the government despite the market showing 'limited interest'. We are positioned for steepeners because we expect a gradual normalisation of the – in our minds – very compressed risk premium in the Swedish government bond curve. Another factor to consider is the Debt Office borrowing (corresponding to SEK100bn) in EUR and USD for on-lending to the Riksbank. The compression of the risk premium coincided with an escalation of financial stress in Europe that triggered a large inflow of foreign capital into the Swedish bond market. Following the summer these inflows have abated, while at the same time foreign investors are offered an opportunity to buy Swedish government bonds in EUR and USD.

Also, even assuming a borrowing requirement close to SEK55bn it remains that we are likely to experience a significant shift in the relative supply of mortgage versus bonds this year. We estimate net supply of mortgages to around SEK-45bn (based on mortgage lending growth at 3%, 75% refinanced in SEK bonds and half of next year's redemptions pre-financed in 2013). Using the current Debt Office projections (gross issuance in 2013 of SEK74bn and SEK10bn in redemptions), the relative net supply of mortgage bonds would be close to SEK-110bn.

Today's key points

- Debt Office: no hurry to increase supply of the longest bonds

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