

Kommuninvest i Sverige AB

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This report does not constitute a rating action.

Credit Highlights

Issuer Credit Rating

AAA/Stable/A-1+
Nordic Regional Scale
--/--/K-1

Overview

Enterprise risk profile	Financial risk profile
Low-risk local and regional government (LRG) lending, very experienced management team, strong market share, and importance for the municipal sector underpin the rating.	Kommuninvest's ongoing capitalization plan, through which the company receives equity contributions from its members, makes its capital adequacy predictable and stable.
Despite inflationary cost pressures and slower economic growth, we expect credit quality in the LRG sector to remain robust, bolstered by support from the central government.	The funding and liquidity positions are supported by tight matching of assets and liabilities, a very liquid treasury portfolio, and broad access to diversified funding.
Sweden's risk tax on credit institutions is likely to depress Kommuninvest's profitability and could affect competitiveness, unless Kommuninvest is granted an exemption.	

Kommuninvest's strong public policy role is underpinned by its strong and increasing market share. In the aftermath of the pandemic and the phasing out of extraordinary central government support, the financial position of Swedish LRGs has deteriorated. At the same time, LRGs throughout the country need to invest in the core infrastructure that supports the country's growing population. Given the sizable investment needs, lending growth at Kommuninvest has been solid; it increased by 3% during the first six months of 2023. In addition, the company's market share has continued to increase--by June 2023, it was about 60% (56% in 2019).

The risk tax on credit institutions increases Kommuninvest's costs and weighs on profitability. Before the risk tax was implemented, the Swedish parliament announced that Kommuninvest would be granted an exemption from paying the tax, starting in 2023. Although the government has yet to present a formal proposal, Kommuninvest is actively working to gain the promised exemption. We expect Kommuninvest will continue to absorb the increase in expenditure through a combination of measures such as cost savings; temporarily lower dividend payouts; and, potentially, via its lending margins. In 2022 and 2023, the central government distributed additional grants to mitigate the increase in funding costs for the LRGs.

The company benefits from a strong funding position thanks to diversified funding, efficient funding practices, excellent name recognition, and adequate liquidity, which enables it to withstand most shocks. Funding and liquidity are supported by tight matching of assets and liabilities, a very liquid treasury portfolio, and broad access to diversified funding. That said, most of Kommuninvest's lending has a short maturity profile, and the agency therefore requires a steady flow of high funding volumes.

We regard Kommuninvest's guarantee structure as predictable, supportive, and immediately enforceable.

Kommuninvest's members are highly creditworthy and liable for the agency's obligations under a joint and several guarantee. Hence, we would expect Kommuninvest's members to provide extraordinary support, if needed.

Outlook

The stable outlook reflects our expectation that the underlying municipal sector will maintain high creditworthiness, Kommuninvest's guarantee structure will remain unchanged, and the agency will continue to benefit from unwavering support from its members. We expect Kommuninvest's management to maintain low risk tolerances and continue to contain risks associated with the wholesale-funded nature of its activities. Moreover, we expect that Kommuninvest will maintain prudent risk policies so that its lending services--and ultimately the execution of its public policy role--will stay on track.

Downside scenario

We could lower our ratings on Kommuninvest if we observed a structural deterioration in the credit quality of the agency's members. We could also consider a downgrade if Kommuninvest's stand-alone credit profile (SACP) came under significant pressure; for example, if risk management faltered to such an extent that the agency's liquidity and capital position saw a material deterioration. This could occur if there were a widening funding gap and substantial stress on the agency's liquidity position, combined with structural weakening capital adequacy. Such financial pressure could hinder Kommuninvest's ability to fulfil its public policy mandate and reduce our confidence in the agency's risk management culture.

Rationale

Enterprise risk profile: Kommuninvest's very strong management and status as primary lender to Swedish LRGs support the ratings

Kommuninvest's public sector mandate is to provide funding solely to its members, which comprise entities in the Swedish LRG sector. Kommuninvest lends directly to its member municipalities and regions, and to companies under their control (in which case, a guarantee from the owner LRG is required). As such, Kommuninvest's loan book is exposed only to Swedish LRG risk. The agency has a strong market position and its market share has been gradually increasing for many years. Kommuninvest's market share reached about 60% of total lending to the sector in June 2023 (59% in June 2022). In 2023, Kommuninvest attracted one new member; as a result, 295 of Sweden's 310 LRGs are members. Kommuninvest's lending growth has consistently outpaced the domestic sector average, suggesting a competitive offer. It maintained above-average growth, even during the pandemic and while the Russia-Ukraine conflict has continued.

Kommuninvest has a clear public policy mandate based on its ownership, support structure, niche lending, and nonprofit mission. It plays a very important role in financing the Swedish LRG sector, by securing funding on favorable terms from national and international capital markets. Kommuninvest's role as a supplier of stable financing to the LRG sector was especially valuable during the pandemic and following the outbreak of the Russia-Ukraine conflict.

During these periods of stress, many Swedish LRGs turned to Kommuninvest to meet their funding needs.

Kommuninvest has sharpened its focus on sustainable loan products, which are increasingly in demand in the sector. More than 15% of its loans are now green loans. The company has granted a total of Swedish krona (SEK) 100 billion in loans, to 600 approved projects. In June 2023, Kommuninvest granted a SEK3.8 billion loan to a municipal housing company that aims to promote long-term social initiatives.

The Swedish central government's risk tax applies to all credit institutions and took effect on Jan. 1, 2022. This required Kommuninvest to increase its lending margins and so increased funding costs at LRGs. Before the tax was implemented, the Swedish parliament called on the government to exempt Kommuninvest and, until an exemption is granted, to compensate LRGs for the increase in their funding costs. However, no formal proposal to exempt Kommuninvest from the risk tax has been presented; Kommuninvest is working to realize such a proposal. While Kommuninvest is obliged to pay this tax, its costs will be under pressure. In 2022, the tax amounted to SEK257 million; we expect this to increase to SEK326 million in 2023. The cost pressure has been offset by the increase in net interest income as market interest rates rose.

We expect Kommuninvest will continue to absorb the increase in expenditure through a combination of measures such as cost savings; temporarily lower dividend payouts; and, potentially, via its lending margins. Therefore, we anticipate that the long-term effect on the agency's financial profile will be limited. So far, the impact on margins has been negligible, but if Kommuninvest has to raise its margins to absorb higher costs, its competitiveness compared with other sources of funding available to the LRG sector could be weakened. Despite this, we expect the agency's overall policy role to remain intact, especially for small and midsize municipalities.

In preparation for the regulatory leverage ratio requirement and internal targets for capitalization, Kommuninvest has actively engaged with its members to secure additional core capital through higher contributions, redistribution of dividends, capital injections, and the replacement of a subordinated loan from the members. A new model for capital contributions was agreed in April 2020. The current capitalization plan will run until 2024, after which Kommuninvest and its members will agree a new plan, lasting through 2028. Given the somewhat weaker lending growth prospects, annual capital contributions under the 2024-2028 plan could be lower than those up to 2024. This setup highlights the constructive dialogue between Kommuninvest and its members, and confirms our view of the agency's management, relationship with members, and overall capitalization.

In our view, Swedish LRGs operate within a mature institutional framework that supports their high credit quality. Regions and municipalities benefit from autonomy in setting local taxes and a comprehensive equalization system. Important systemic features and principles are formalized in legislation. In addition to LRGs' own revenue-raising capacity, the central government plays an important role by providing general and earmarked grants to the sector. To combat the financial effects of the pandemic, the central government provided generous support packages in a timely manner, allowing LRGs to uphold sound financial positions. Moreover, in response to rising inflation and pension expenditure, the central government announced additional grants to the sector from 2024. Sweden's national economy is wealthy, its financial system is advanced, and links between the LRG sector and the 'AAA' rated sovereign are tight.

Financial risk profile: Very strong capitalization and solid liquidity position provide financial buffers

Kommuninvest maintains a strong capital position and we anticipate that our risk-adjusted capital (RAC) ratio after adjustments will remain around 15% going forward. All of Kommuninvest's equity is eligible as Tier 1 capital, and we incorporate it into our total adjusted capital ratio. Our RAC ratio before adjustments for Kommuninvest was very strong, at 53%, on June 30, 2023, up from 46% a year before. In light of the ongoing capitalization plan and expected lending growth, we estimate the ratio will reach 55% by year-end 2023. We make adjustments for the single-name concentration from individual LRGs--after these, the RAC ratio drops to about 16% (about 15% at year-end 2022).

Kommuninvest has a very strong Tier 1 regulatory capital ratio, at about 482% (as of June 30, 2023). This is largely thanks to the zero risk-weighting of Kommuninvest's lending, as well as counterparty risk in derivatives being covered by a guarantee from its members. The leverage ratio remained strong at about 9% on the same date.

In the coming years, we expect growth in lending to be somewhat weaker, partly impeded by macroeconomic headwinds and inflationary pressure. These have prompted many LRGs to restrict their capital expenditure. At the same time, Kommuninvest already has a high market share and little room to expand its membership base, making it harder to outpace domestic lending growth. Slower lending growth will support our capital ratios but could also mean somewhat lower capital contributions from members. Regardless, we expect Kommuninvest's experienced management to remain committed to upholding a strong capital position and strengthening it, in line with its asset base.

Kommuninvest benefits from excellent name recognition in domestic and international capital markets. This provides it with a deep investor base. Despite recent market turbulence caused by the pandemic and Russia's invasion of Ukraine, Kommuninvest has managed to maintain reliable access to capital markets. In Sweden, securities issued by Kommuninvest are considered to be of the highest quality when calculating the liquidity coverage ratio. They were also included in the Swedish Riksbank's asset purchase program, during the pandemic. Most of Kommuninvest's issuance is plain vanilla, benchmark size, and within strategic funding markets denominated in Swedish krona, U.S. dollar, and euros. Moreover, the importance of green bonds has continued to increase, making up 22% of new funding in the first half of 2023.

In addition, Kommuninvest has a euro commercial paper (ECP) program and a Swedish krona commercial paper program, through which it can borrow in a number of currencies. The agency has gradually reduced its exposure to nonbenchmark and callable funding. Its exposure to the Japanese Uridashi market, which it decided to leave in November 2021, is now negligible, at less than 1% of the portfolio. Kommuninvest aims to maintain a strong presence in its strategic funding markets.

We view as positive Kommuninvest's strategy of closely matching assets with liabilities and predominantly relying on funding in krona. This strategy limits the need for derivatives and contributes to Kommuninvest's stable funding profile. Cumulatively, its maturing assets cover about 120% of maturing liabilities over the next 12 months. That said, it both borrows and lends over a shorter term than its peers, creating a mismatch in lending and funding compared with the underlying capital investment cycle in the LRGs and their companies, and a high roll-over rate. Although there is no legal obligation to roll over loans, municipalities expect it. In our view, a significant failure to roll over loans would likely damage the agency's franchise, which limits the benefit of shorter exposures. Instead, it creates roll-over

risk in volatile markets.

Kommuninvest's high level of expertise concerning liquidity portfolio management and execution, enables it to undertake stringent asset-liability management and maintain cost efficiency. The liquidity portfolio comprises very liquid and short-term securities, issued solely by highly rated government-related entities. The average duration is below six months, highlighting the very liquid nature of the holdings. Kommuninvest also exercises proactive liquidity management, which we view as important, in light of its shift to two-way credit support annexes in its derivatives counterparty portfolio.

Our liquidity ratio of about 1x for Kommuninvest indicates that we consider the agency able to meet its financial obligations over a one-year period. Our ratio factors in potentially stressed market conditions, under which we assume the agency would have no access to the capital markets. However, we understand that loans to its members are typically renewed before the maturity date and so do not necessarily result in a liquidity inflow for the agency. Given Kommuninvest's relatively short maturity profile in its lending, we believe Kommuninvest has a somewhat weaker liquidity position compared with Nordic peers.

Extremely high likelihood of support via a joint and several guarantee from all members

Kommuninvest has a solid membership base that is bound to it by a joint and several guarantee mechanism. We assess Kommuninvest's guarantee structure as predictable and immediately enforceable by law. Any investor, without a court order, could call upon any guaranteeing member to make good on a claim on Kommuninvest. The legal enforceability of the guarantee underpins our assessment of an integral link between the members and Kommuninvest. At the same time, Kommuninvest has a very important role in providing cost-efficient funding to its members. Consequently, we consider that extraordinary support from its largest members, which have an average credit quality at about 'aa+', is extremely likely. This leads to an uplift to Kommuninvest's SACP, resulting in a long-term indicative rating of 'aa+'.

In addition, we believe that many of the other members, outside the group of guaranteeing supporting members, would also be able to support Kommuninvest in a situation of distress. These members' aggregate revenue represents more than 20% of the entire LRG sector, underpinning our assessment of support mutualization. Therefore, we apply an additional notch of uplift to the long-term issuer credit rating on Kommuninvest.

Key Statistics

Table 1

Kommuninvest i Sverige AB--Selected indicators						
	--Year ended Dec. 31--					
(Mil. SEK)	2023H1	2022	2021	2020	2019	2018
Business position						
Total adjusted assets	609,874	553,257	524,261.7	527,333	471,299	417,186
Customer loans (gross)	484,415	470,682	460,651	445,789	408,218	355,710
Growth in loans	2.9*	2.2	3.3	9.2	14.8	14.7
Net interest revenues	502	666	681	711	828	886
Non interest expenses	120	224	260	248	242	266.5

Table 1

Kommuninvest i Sverige AB--Selected indicators (cont.)						
(Mil. SEK)	--Year ended Dec. 31--					
	2023H1	2022	2021	2020	2019	2018
Capital and risk position						
Total liabilities	599,548	543,088	514639.4	518659	463719	409599
Total adjusted capital	10,310	10,150	9124.7	8476	7581	7588
Assets/capital	47	46	57	62	62	55
RAC before diversification (%)	52.7§	52.7§	42.3§	39.3§	38.2§	41§
RAC after diversification (%)	16.1§	16.1§	14.0§	13.9§	14.8§	17§
Gross nonperforming assets/gross loans	0	0	0	0	0	0
Funding and liquidity (%)						
Liquidity ratio with loan disbursement (1 year)	1.03§	1.03§	1.1§	1.1§	1.1§	1.1§
Liquidity ratio without loan disbursement (1 year)	1.04§	1.04§	1.1§	1.1§	1.1§	1.1§
Funding ratio (1 year)	1.2§	1.2§	1.2§	1.2§	1.3§	1.2§

H1--First half. *Year-on-year. €Year-to-date, §As of end-June. RAC--Risk-adjusted capital. SEK--Swedish krona. N.A.--Not available. Source: S&P Global Ratings.

Ratings Score Snapshot

Table 2

Kommuninvest i Sverige AB--Ratings score snapshot	
Issuer credit rating	AAA/Stable/A-1+
SACP	aa-
Enterprise risk profile	Strong (2)
PICRA	Strong (2)
Business position	Strong (2)
Management and governance	Very strong (1)
Financial risk profile	Strong (2)
Capital adequacy	Very strong (1)
Funding and	Positive and
Liquidity	Adequate (3)
Support	(+2)
GRE support	(+2)
Group support	0
Additional factors	(+1)

PICRA--Public-sector industry and country risk assessment. GRE--Government-related entity.

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Governments | International Public Finance: Public-Sector Funding Agencies: Methodology And

Assumptions, May 22, 2018

- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, July 20, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Institutional Framework Assessment: Swedish Municipalities And Regions Have Flexibility To Balance Costs, Nov. 29, 2023

Ratings Detail (As Of December 13, 2023)*

Kommuninvest i Sverige AB

Issuer Credit Rating	AAA/Stable/A-1+
<i>Nordic Regional Scale</i>	--/--/K-1
Senior Unsecured	AAA

Issuer Credit Ratings History

03-Jul-2006	AAA/Stable/A-1+
21-Nov-2008 <i>Nordic Regional Scale</i>	--/--/K-1

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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