

Riksbank: Growing dissent hinders efforts to support the krona

The Riksbank hiked by 50bp as expected, and signalled another 25bp move in June or September. However, two members argued for a smaller increase today and rate projections showed the next quarter-percentage hike should be the last one. Governor Thedeen kept pointing to the need for a stronger krona, but the dovish tilt makes SEK-supporting efforts harder



Erik Thedéen, governor of the Riksbank

A dovish 50bp hike

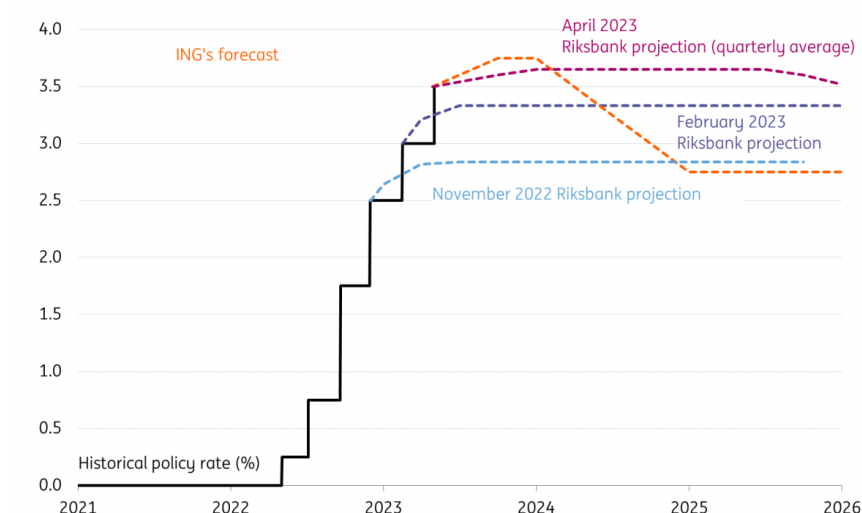
The Riksbank increased its policy rate by 50bp today to 3.50%, as widely expected, and signalled it will probably deliver another 25bp hike in either June or September. The updated rate projections show that should be the last move in the Riksbank tightening cycle, with rates peaking at 3.75% and being held around that level for the foreseeable future. This was the first bit of the dovish surprise: market expectations had priced in a peak rate higher than 3.75% and part of the consensus (including ourselves) had expected the new projections to display a 4.0% peak rate.

The other element of surprise came from the explicit dissent by two members of the Executive Board (Deputy Governor Anna Breman and Deputy Governor Martin Floden). They both argued in

favour of a 25bp hike today and against the rate path projections, which they judged too hawkish in light of “well-anchored inflation expectations, moderate wage increases and the weak and downward-revised forecast for domestic demand”.

The other projections included an upward revision in CPI and CPIF inflation – especially the core measure (excluding energy) - as well as for the size of the GDP contraction in 2023 (from -1.1% to -0.7% year-on-year).

New rate projections

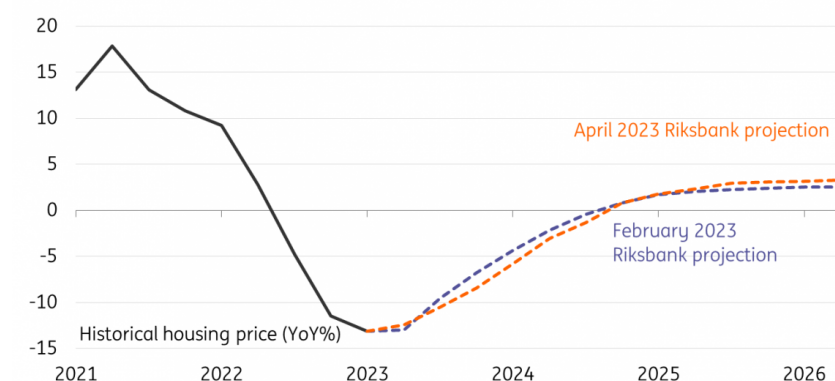


Source: ING, Riksbank

Words aren't enough to support the krona

It is clear that there is a growing divergence of views within the Riksbank Board, and that today's decision was probably the result of some sort of compromise, similar to what we saw at the latest European Central Bank meetings. The concerns of the Riksbank's doves are reasonable, and while the anchored inflation point is a debatable one, the housing and growth fears are indisputable. As shown below, a higher peak rate meant that the projected slump in house prices is also longer-lasting, despite the slightly better-than-expected house price data in the first quarter.

House pain to be prolonged



Source: ING, Riksbank

We could see how Governor Erik Thedeen remained focused on his efforts to support the krona. His verbal attempts to support the currency have ranged from claiming that there are strong arguments in favour of SEK strengthening to highlighting how a persistently weak krona may affect policy. Unsurprisingly, those attempts did not prevent EUR/SEK from staging a big rally today as SEK dropped on the dovish surprise at the same time as the EUR was finding idiosyncratic strength.

We think that, more than the signal that rates will peak at 3.75%, it was the explicit dissent within the board that hit the krona today, and may well hinder the ongoing effort by Governor Thedeen to prop up the currency.

FX intervention? Still a risky path

Ultimately, this may be raising the chances that the Riksbank will have to take FX intervention into consideration. We continue to doubt an intervention campaign is a viable option for the Riksbank, considering the relatively contained amount of FX reserves and political hurdles that accompany unilateral FX buying for developed countries.

For now, we think that further SEK depreciation may see the Riksbank react with more verbal intervention including the threat of FX intervention to test the market's reaction function. One key issue is still that many headwinds to the krona are beyond the Riksbank's control (especially linked to idiosyncratic strength in the euro and risk sentiment swings) and the economic strains in Sweden have clearly dented the attractiveness of the krona from a fundamental perspective.

Our view is that EUR/SEK will remain around 11.30/11.40 in the near term, with risks of a spike to the 11.50 area in periods of risk aversion or should some risk premium related to the Swedish housing market/economic outlook be built back into the pair.

The dissent that has emerged within the Riksbank's Board today poses upside risks to our baseline scenario for a descent below 11.00 in the second half of the year, although a generalised improvement in risk sentiment as the Federal Reserve's tightening cycle comes to an end, and the krona's high beta to Europe's decent growth story still point to a stronger SEK into year-end barring a material deterioration in the housing and economic outlook in Sweden.

Author

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an

investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.