

Cautious Riksbank unlikely to halt krona's strength in 2021

Despite a more resilient end to 2020, Sweden's Riksbank remains cautious about the outlook. A further extension to the quantitative easing programme is possible later in the year, particularly if the downside risks surrounding the virus materialise - though a return to negative rates remains unlikely



Riksbank starts the year cautiously, despite more resilient 2020 data

The Swedish Riksbank has framed its first meeting of the year with a cautious tone. Sure, the end of 2020 was more resilient than expected given the rising number of restrictions - something that's reflected in an upward revision to the near-term level of GDP. And while the shallow nature of Sweden's economic hit means it will only be a matter of months before activity returns to pre-virus levels, the Riksbank doesn't expect core inflation to get sustainably closer to the 2% target until 2023.

It comes as no surprise therefore that the central bank has continued to signal a flat path for the repo rate out to 2024. But what about QE? The Riksbank expanded its bond buying envelope last

November, giving it scope to continue purchases throughout this year. At this meeting, the central bank has indicated it will front-load more of the remaining chunk of the SEK700bn package during the first half of the year.

That implies some tapering later in 2021, though a further expansion of this programme is entirely possible, particularly if the downside risks surrounding the vaccination and virus story materialise. However, we continue to doubt that policymakers will take the repo rate back into negative territory again - the fact that the central bank resisted this at the peak of the pandemic last spring suggests the bar for a rate cut is set pretty high.

SEK: Not overly dovish but not strong enough to push EUR/SEK below 10.00

With the central bank striking a balancing act between a somewhat improved economic outlook, and inherent caution, the knee-jerk reaction saw the krona strengthen as some market participants had been entertaining the idea of more asset purchases, particularly after the Riksbank's dovish surprise at its November meeting.

While modestly surprising the market, the bias coming from the meeting today is not enough, on its own, to push EUR/SEK below the 10.00 level. For this to happen, we need to see the 2Q economic recovery in the eurozone and Sweden, which will then benefit cyclical currencies such as SEK. Near-term, we expect EUR/SEK to continue hovering around the 10.10 gravity line, with the next leg of SEK strength likely coming in 2Q, rather than in coming days.

Author

James Smith

Developed Markets Economist, UK

james.smith@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 <http://www.ing.com>.