Riksbank tightening some way off despite latest cautious optimism

The Swedish Riksbank has again signalled it will keep its main interest rate at zero for the foreseeable future, as a muted outlook for wage growth dominates the prospects for economic recovery later this year. Still, an improving global outlook should give the krona a lift over coming months

Stefan Ingves is the Governor of the Swedish Central Bank

Riksbank probably done with easing, but tightening is some way off

In many ways the Swedish Riksbank finds itself in a similar position to that of other central banks across Europe. The economy has grown more resilient to Covid-19 restrictions, and indeed a more robust winter performance than expected has enabled the Riksbank to upgrade its forecasts slightly for this year, though the overall profile beyond 2021 is virtually unchanged for both growth and inflation.

We suspect the Riksbank will be one of the latter developed market central banks to begin the monetary tightening process

That implies little need to add further stimulus. Along with keeping its key policy measures on hold, the Riksbank also signalled it will gradually taper the pace of purchases through the rest of the year (or front-load the remaining portion of its SEK700bn purchase envelope, to put it another way). We also continue to think that a renewed foray into negative rates, which the Riksbank has thus far opted against during the pandemic, remains unlikely.

But again, like other European countries, inflation is likely to be a benign story beyond 2021 – at least compared to the likes of the US, where we expect CPI to remain sticky above the Fed's target for some time. Barring a brief above-target spurt over the next couple of months, Swedish CPIF is likely to average below 2% across the medium-term. Wage growth, which is heavily influenced by a recent negotiated settlement that was largely similar to previous years, suggests price pressures are unlikely to come from the labour market.

As a result, we suspect the Riksbank will be one of the latter developed market central banks to begin the monetary tightening process over the next few years.

SEK: Gradual upside ahead despite limited help coming from Riksbank

As expected, the Riksbank meeting delivered few surprises and it was a non-event for the currency, with EUR/SEK by and large stable in response to the meeting.

Like the European Central Bank, the Riksbank acknowledged the improving economic outlook (upgrading GDP and CPI forecasts for this year) but remains cautious, signalling no change in interest rates over the policy horizon. The quantitative easing programme also continues.

In contrast to Norway's krone and the Norges Bank, the Riksbank won't provide any tailwinds to SEK this year. Yet, we still expect EUR/SEK to move below the 10.00 level this summer as the currency will benefit from the improving eurozone economy and a more synchronised global economic recovery in the second half. Recall that Sweden is a small open economy levered to global growth, which SEK should in turn benefit from, even if the Riksbank remains cautious and keeps rates at zero this year and next.

We also note that EUR/SEK above 10.00 is modestly overvalued based on our BEER model.

Author

James Smith
Developed Markets Economist, UK
james.smith@ing.com

Disclaimer