

Sweden's Riksbank takes two tentative steps towards tightening

The Riksbank's decision to forecast rate hikes in 2024 is a notable shift, even if in practice the date of the first move is likely to come a fair bit earlier than policymakers are currently hinting. Interestingly it has also become one of the first central banks to signal it will begin the process of shrinking its balance sheet, potentially as early as 2023.



Sweden's Riksbank is far from the most hawkish central bank in the G10 arena. But even so, it has made two subtle, but notable shifts in that direction at its November meeting.

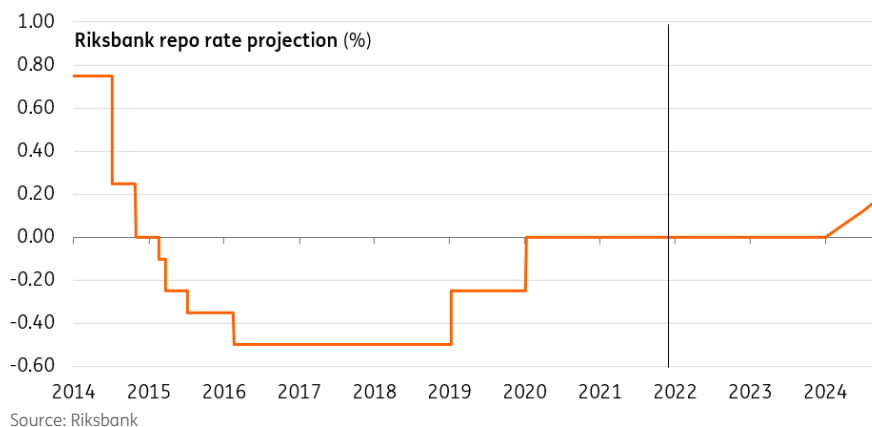
1 Riksbank hints at (very) modest tightening in 2024

Firstly, policymakers have for the first time pencilled in a very modest amount of tightening for 2024, and the central bank now sees the repo rate at around 0.2% at the end of that year. In practice rates are likely to have gone up much earlier than that, not least when you consider our call for the ECB to begin hiking in 2023. Our current forecast has the Riksbank increasing the repo rate for the first time at the end of that year.

But the challenge for the Riksbank is that markets are already pricing quite a bit of tightening –

around 40bp over the next year. That probably explains the reticence to include more tightening in the central bank’s rate path, even if policymakers were openly talking about rate hikes in the second half of the forecast horizon in the meeting minutes from September.

The Riksbank's interest rate projection includes some modest tightening for the first time post-Covid



2 Policymakers are hinting that the balance sheet size could be reduced from 2023

The second interesting feature of November’s meeting is that policymakers are now signalling that they expect to shrink the size of the balance sheet in 2023 – or put another way, begin the slow journey of unwinding the vast quantity of bonds accrued under quantitative easing. This is not a total surprise, though we thought policymakers might hold back on changing their stance on this until next year.

The details are scarce at this stage, though the latest forecasts imply the reduction will be pretty gradual. If you take the mid-point of the Bank’s fan chart projection, it expects the balance sheet to reduce from its end-2021 size of SEK920bn to around 740bn.

Perhaps the most interesting takeaway here is that it suggests balance sheet reduction, or quantitative tightening as it is sometimes known, could come well before the first rate hike. That would probably set the Riksbank apart from elsewhere, even if some other central banks (like the Bank of England) have hinted this process could start at a reasonably early point in the next rate hiking cycle.

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