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Western European Indicators and Insights

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Andrew Wroblewski
Chief Economist, Eurozone and UK

London
+44 20 7959 3244
awroblewski@decisioneconomicsinc.com

Sweden: Hiking process paused.

Boost for the Krona?

As expected, the Riksbank kept its key repo rate at 2.00% after its latest Board meeting, effectively postponing the further hike that was implicit in its previous rhetoric and forecasts and which would have extended the seven hikes in this tightening cycle. Explaining its thinking, the Riksbank statement noted the concern over public finances abroad had increased and that global growth prospects have deteriorated. From its perspective, the slowdown in the Swedish economy is thus expected to be more pronounced than was forecast at its previous meeting in July. The Board therefore decided to hold the repo rate and to postpone continued increases slightly.

As always, the Riksbank underscored that forecasts for the economy and monetary policy are based on the information currently available and new information further ahead may lead to changes in these forecasts. There is currently considerable uncertainty over economic developments, meaning that the actual path for policy coudl be both higher or lower than the official projections point to.

Regardless, the Board stressed further hiking ahead, very likely resuming late in the year but thereafter at a somewhat slower pace than previously envisaged. As a result, fresh hikes over the next two years are still seen taking the key rate to 3.6% by Q3 2014, as opposed to 3.8%, with rates one year hence rising to 2.4%, half a point lower than previously assumed.

Otherwise, there was little of note from the statement or the details in the Monetary Policy Update. The latter produced revised economic projections that differed only slightly from previous ones, except for those pertaining to 2012. These envisage headline CPI averaging 3.0% this year (down from 3.1% in the July projections) and 2.1% in 2012 (down from 2.8%), but with the 2013 forecast down to 2.6%. The Board puts more emphasis on underlying inflation (ie excluding swings in mortgage rates) which is expected to remain below the Riksbank 2% target until 2013. These inflation updates came alongside largely softer real activity projections, although the Board increased its growth forecast for the current year minimally (to 4.5%) while trimming it clearly for 2012 (to 1.7%) and largely adhering to a 2013 forecast of 2.4%.

Also of some note, but not that surprising given similar dissent before, two members of the six-strong Riksbank Board (Svensson and Ekholm) again entered reservations with regards to the repo rate path projected, both preferring to leave policy on hold for longer.

The fact that the Riksbank would pause policy had been advertised by recent Board comments. It is clear that the Board recognizes adverse developments abroad, whilst also still wary about domestic inflation pressures coming from a possible push up in wages to the current headline inflation rates that has been pushed higher by the rise in mortgage rates. In this regard, the postponing of further rate hikes may actually help deter wage increases if headline inflation proves to be lower than otherwise.

Even so, markets may still note a desire by the Riksbank to hike further, alongside forecasts that point to a continued if not very resilient and upbeat economy. Against this background, one risk is that the Swedish currency may emerge as a substitute for the Swiss Franc in terms of a European safe-haven. A clearer picture of Riksbank thinking may come with the arrival of the minutes to this meeting on September 20.