

Fast Comment Sweden

4.25 percent revisited; Riksbank forecast change

- Policy rate not yet restrictive enough to control inflation
- Need to support krona after global central bank hawkishness, or risk new fuel to inflation fire
- We add 25bp hikes in September and November, re-raising forecast peak from 3.75 to 4.25 percent

Policy rate not yet restrictive enough to control inflation

We forecast that the Riksbank will need to do more to control inflation, and have added two 25bp hikes to our forecast.

While it is a fair assessment that Riksbank monetary policy is now somewhat restrictive, it appears to not be restrictive enough. The real rate of interest is positive for most horizons along the yield curve except for the very short end, and the neutral rate is in our view low, close to zero (but slowly rising, see p.7 in our [January Global Macro Forecast](#)). Despite this restrictive stance, the economy remains inflationary with still-high profits, rising household incomes via higher employment and accelerating wages - fueling a rising nominal spending trend, and making further price rises possible, feeding back to the start of the loop: profits. And in parallel to this, note that the Riksbank will likely revise up its forecasts for growth and the labour market.

Admittedly, we have seen the first signs of fading pricing power, but our view is that this is a slow process. Not least, the wage pressure in Sweden has not really been picking up until now (see also [Macro Comment on labour share, profits and inflation](#) here).

Need to support krona after global central bank hawkishness

Another channel in the monetary policy transmission mechanism where the Riksbank has had too little impact is the exchange rate. The krona has weakened substantially, stoking inflation pressures, and in the end it is relative interest rates that matter for exchange rates. We think the Riksbank needs to drive up Swedish real rates to support the krona.

Setbacks in the global fight against inflation mean that [we have today revised up forecasts](#) for the policy rates of all central banks we cover. This adds to the challenge for the Riksbank, which will need to raise its policy rate more than previously anticipated to have the desired effect on inflation through the FX channel.

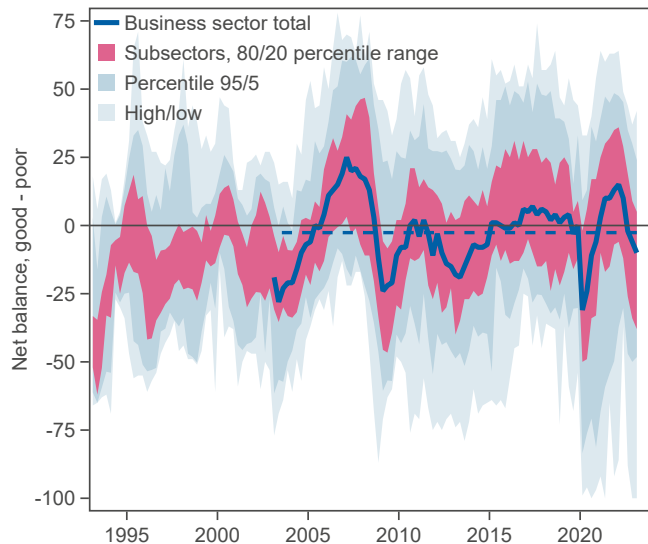
We add 25bp hikes in September and November, taking peak to 4.25%

Like before, we forecast the Riksbank [to deliver a 25bp hike and an acceleration of QT](#) at its June policy announcement on Thursday. But beyond that, waiting for the lagging effects of past policy tightening will not be sufficient. Instead, we judge that the Riksbank will need to raise the policy rate at a steady but gradual pace ahead, and expect the Executive Board of the Riksbank to deliver 25bp hikes at the September and November meetings.

So could the Riksbank raise by 50bp straightaway on Thursday? No, we think that is unlikely. Inflation outcomes have not deviated substantially from the Riksbank's forecast and in the current data-dependent world of central-banking, the more worrying inflation outlook we paint above is not enough to push the Riksbank into a stressed situation. Nor does the Riksbank feel confident that it can steer the krona predictably enough to warrant an extra hawkish surprise too. And lastly, remember that what made us abandon our previous [4.25%-call back in April](#) was the fact that the Swedish central wage agreement looks like an advantage for the Riksbank, compared to the situation of other central banks: The moderate two-year deal has limited the risk of a full-fledged wage-price spiral, and the Riksbank has been clear that it allows them to act with more patience to finally beat inflation.

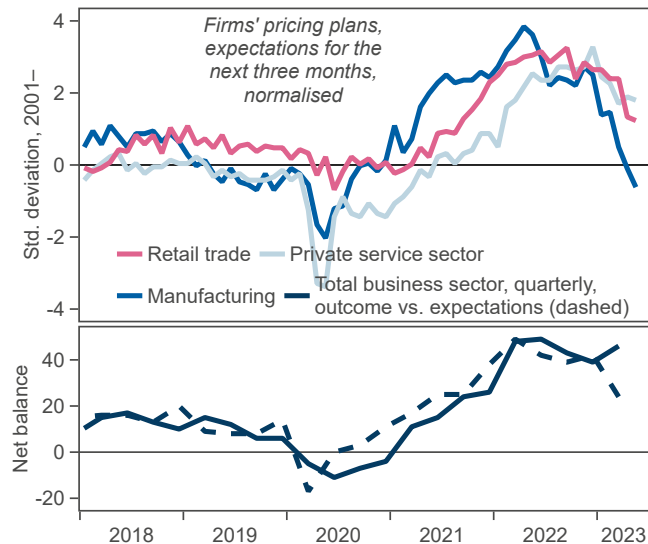
Our new central bank forecasts and market developments has also made us revise our krona FX forecast and interest rate forecasts.

Pricing power starting to fade? Profitability normalising...



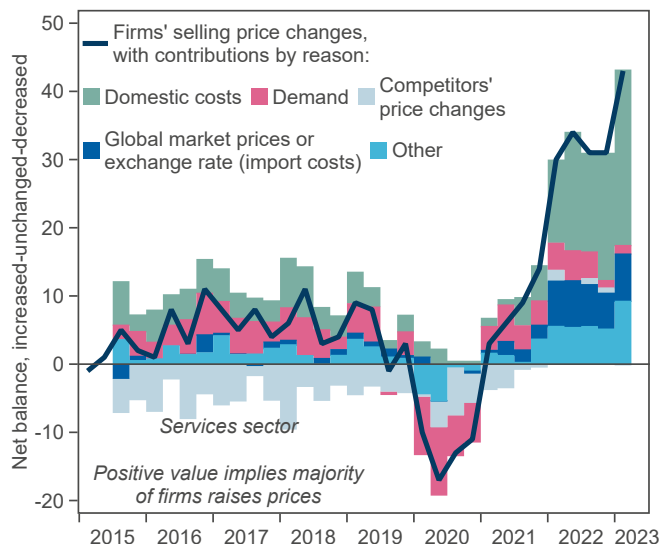
Sources: Macrobond, NIER and Handelsbanken

...without firms resolutely upholding pricing raising plans



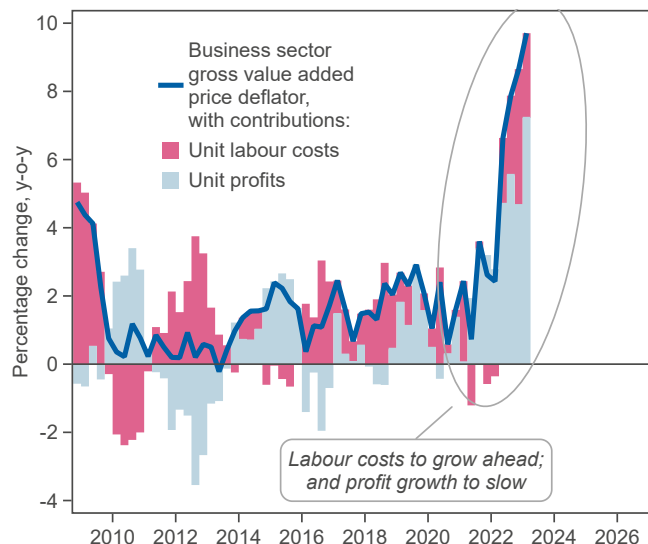
Sources: Macrobond, NIER and Handelsbanken

But long way to go as labour (domestic) costs pick up...



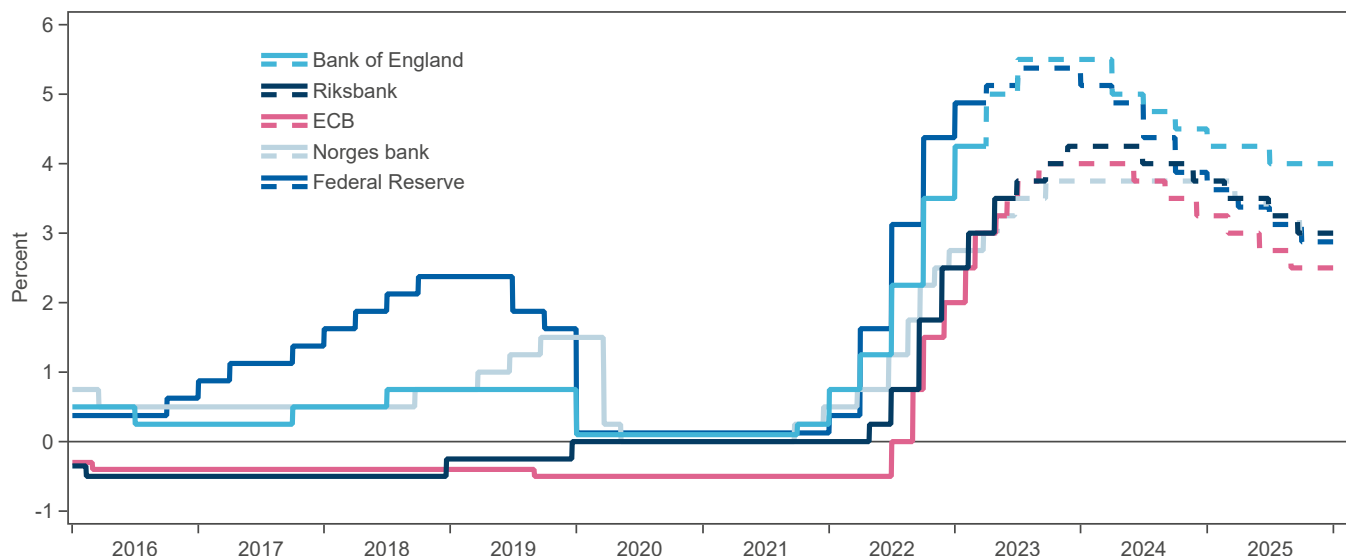
Sources: Macrobond, NIER and Handelsbanken

...and firms are unlikely to fully absorb through profits fall



Sources: Macrobond, Statistics Sweden and Handelsbanken

The Riksbank to peak above the ECB



Sources: Macrobond and Handelsbanken

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