

## Sweden

### Riksbank with a Slightly Dovish Tilt

- As expected, the Riksbank (4:2 split) left the key policy rate unchanged at 1.0% at today's monetary policy meeting, and maintained its near-term easing bias. Meanwhile, the Bank was slightly more dovish than expected as it lowered its conditional interest rate path marginally for 2014-15 (by 1-6bp). In other words, the Central Bank raised the probability of a near-term interest rate cut to 20% (16% previously), and postponed the timing of initial monetary tightening from Sep/Oct to Oct/Dec. Otherwise, the rate path was left unchanged.
- Financial stability considerations continue to figure high among the majority board, with today's report confirming the Bank's uncertainty in terms of interpreting the new macro prudential framework and its implications on monetary policy. In turn, the Bank reiterated that it will analyze financial risks and their possible impact on the economy. We maintain that once the new macro prudential tools become operational and turn out to be sufficient (i.e. the current upturn in house prices and reacceleration in household credit growth remain in line with the assumptions in the MPR), this should leave room for the Riksbank to use its policy instrument – the repo rate – more actively to get inflation back up to target. Comments from the Riksbank confirm this: *"Once measures have been taken in the field of macro-prudential policy, the risks linked to household debt can be assumed to decline. This will have an impact on the conditions for monetary policy, but it is difficult to determine as yet how much and how quickly,"* the policy statement said. Hence, inflation data should become increasingly more important for monetary policy. As we forecast well-below target inflation in coming years, we reckon the Riksbank should be in no rush to tighten monetary policy. We therefore confirm our long-held view of stable rates throughout 2014, and note that current market pricing (and Riksbank forecasts) now has become more consistent with our view (discounts a first rate hike in the latter part of 2014). Ahead of the September meeting, market pricing discounted about a 75% probability of an initial interest rate hike in April next year.
- Changes to the economic forecasts in the new Monetary Policy Report are largely as expected, with lower GDP growth (cut by 0.5pp to 0.7% Y/Y this year lowered by 0.1pp to 2.6% Y/Y in 2014) and inflation this and next year (CPIF has been lowered by 0.1pp this and next year to 0.9% Y/Y and 1.3% Y/Y, respectively), while upgrading its view on the labour market (jobless rate cut by 0.1pp to 8.0% this year and 7.8% in 2014).
- A central part of the MPR is the Bank's risk scenarios. The first alternative scenario assumes increased financial unease in the euro area due to rising interest rates caused by Fed tapering. This clearly poses downside risk to the conditional interest rate path. The second scenario focuses on a stronger recovery in the world economy, which implies stronger Swedish GDP growth and higher inflation. This is clearly an upside risk to the conditional interest rate path in the baseline scenario.
- As expected, low resource use, subdued inflation, high unemployment and weak 2Q GDP growth fuelled calls among the minority of the board for an easier monetary policy stance. Both Deputy Governor Ekholm and Flodén entered reservations against the stable repo rate and the rate path. They both advocated a 25bp rate cut and a repo-rate path that stays at 0.75% through 3Q 2014.

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