All Signal, No Noise

MARKET ANALYSIS

Riksbank Preview: November 2022

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Upside risks to 75bp

23 November, Tim Davis

The Riksbank delivered a 100bp hike in September (against an expected 75bp hike) and its forward guidance strongly steered towards a 50bp hike at this week's meeting. The Riksbank had been attempting to front load policy and support SEK. However, with the peak in the rate path not revised any higher than had been expected, the move was seen as a dovish 100bp hike and with the exception of an initial kneejerk move SEK depreciated against EUR.

Analyst expectations following the September meeting were split between 50bp or 75bp for the November meeting, but now each of the ten sellside previews that we have read looks for a 75bp hike (and 83% of investors in the SEB investor survey expect a 75bp hike with the remaining 17% expecting an even larger 100bp hike). The reason for this is the upside surprise to core inflation. The Riksbank forecast CPIF ex energy would be 7.38%Y/Y in October, but it came in at 7.9% - five tenths higher than forecast. Headline CPIF actually surprised to the downside at 9.3%Y/Y (versus the 9.75%Y/Y Riksbank forecast). However, combined with a 75bp ECB hike – and communication from some Riksbank Executive Board members that a spread above the ECB rate needs to be maintained and there being two ECB meetings before the February Riksbank meeting seems enough to push the Riksbank to hike at least 75bp in November.

Other economic data has been mixed and concerns about the housing market continue to pick up. The housing market was a key concern at the previous meeting too, and with the passthrough of Riksbank hikes to the housing market fast by G10 standards. However, it was judged by the Riksbank that frontloading hikes was preferable to show that it was serious about containing inflation. The MNI Markets team thinks that although a 100bp hike cannot be ruled out (and the risks are more in favour of a 100bp hike than 50bp hike in our view) that concerns about the housing market and an impending recession will be enough to stop the Riksbank from delivering such a large rate hike again. We would also argue that the 100bp hike in September did not really have the desired market impact and therefore the desire to repeat such a step will likely be reduced.

In terms of the rate forecast, most analysts expect a 25bp shift higher, and we would broadly agree that this is the most likely outcome. Based on our calculations a 25bp February hike is in the forecast with around a 10% probability of something more beyond this. We think the risk is that the Riksbank leaves the door open to either a 25bp or 50bp hike in February and shifts the peak in its rate path around 35-40bp higher. We also note, however, that with two new members joining the Executive Board ahead of the February meeting and with Governor Ingves leaving, there could potentially be a different tone to Riksbank meetings in 2023.

Despite 100bp hike, the Riksbank's outlook for Nov/Feb matched analyst expectations

	June MPR			September decision / MPR			Analyst expectations prior to Sep		
	Hike	Cumulative	Implied	Hike	Cumulative	Implied	Hike	Cumulative	Implied
Sep-22	50	50	1.250	100	100	1.75	75	75	1.500
Nov-22	37.5	87.5	1.625	50	150	2.25	75	150	2.250
Feb-23	25	112.5	1.875	25	175	2.50	0-25	150-175	2.25-2.50

Source: Riksbank, MNI calculations

SEB Investor Survey Highlights

- 83% expect a 75bp hike while 17% look for a 100bp hike.
- The rate path is expected at 2.75% YE2023, to remain there at YE2024 and at 2.50% at YE2025.
- “The survey participants own rate expectations in 2023/2024/2025 (median) are mainly in line with the expected rate path.”
- QE reinvestments are expected to end the end of this year and 63% of investors expect no bond sales, while 37% expect the Riksbank will sell bonds (33% expect this in 2023).
- 35% of investors expect no reinvestments in Q4-22 while 17% expect a reduction relative to Q3-22 and 39% expect an unchanged pace from Q3-22.
- “The survey was conducted during 15-18 November among large Swedish FI investors.”

mni

Central Bank Watch - Riksbank

November 23, 2022

MNI Riksbank Data Watch List

Inflation		Current	3m ago	3m Chg	6m ago	6m Chg	2Y History	Hit / Miss	Vs Trend	Surprise Index	Z-Score
CPI	% y/y	10.9	8.5	↑	6.40	↑					1.95
CPIF	% y/y	9.3	8.0	↑	6.40	↑					0.95
CPIF Excl Energy	% y/y	7.9	6.6	↑	4.5	↑					1.34
PPI	% y/y	20.6	25.6	↓	24.5	↓					-0.85
Economic Activity		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Swedbank Manuf PMI	Index	46.8	52.2	↓	54.6	↓					-2.10
Private Sector Production	% y/y	5.0	3.8	↑	3.80	↑					1.47
Economic Tendency Survey	Index	84.6	101.8	↓	109.90	↓					-1.71
Swedbank Service PMI	Index	56.9	58.2	↓	67.50	↓					-0.91
Monetary Analysis		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
M3 Money Supply	% y/y	5.19	8.66	↓	9.96	↓					-1.95
Lending to HH	% y/y	5.01	6.12	↓	6.72	↓					-1.77
Lending to Non-Fin Corp	% y/y	16.53	13.84	↑	10.81	↑					1.34
Avg. new HH loan rate	%	3.09	2.22	↑	1.59	↑					1.60
Consumer / Labour Market		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Retail Sales YoY	% y/y	-5.85	-4.34	↓	1.83	↓					-1.94
Consumer Confidence	Index	48.3	60.6	↓	79.3	↓					-1.43
Unemployment Rate	%	7.1	6.4	↑	8.20	↓					-0.43
Household Consumption	% y/y	1.5	3.7	↓	4.50	↓					-1.05
Markets		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Equity Market (OMXS30)	Index	2097	2033	↑	2059	↑					-0.85
Sweden 10-Y Govt Bond	%	2.01	1.39	↑	1.72	↑					1.42
SEK Yield Curve (2s-10s)	bps	-37.9	-32.0	↓	56.1	↓					-0.56
SEK KIX TWI	Index	124.04	119.14	↑	118.14	↑					1.13

Source: MNI, Bloomberg

Sell Side Previews (A-Z)

Barclays

- Expect 75bp hike as “the fragile mortgage structure in Sweden should dissuade Riksbank from further substantial tightening, likely capping the terminal rate at 3% in the bank's rate path forecast.”
- Expect a further 50bp February hike to a terminal 3.00% rate.

Danske

- Expect 75bp this week.
- “A 50bp hike, which would be in line with the Riksbank’s path from September, is also still feasible, but given that inflation has been higher and international central banks are delivering more than the Riksbank envisaged at the September meeting, a larger step is warranted”
- “Another 100bp hike cannot completely be ruled out, but in our view the probability is lower than it was in September.”
- “Our expectation for the rate path is that the peak level is lifted to around 2.75-3.00%, slightly below market pricing, but somewhat higher than our own call (peak at 2.75%, following 25bp in February).”
- “We believe that the market reaction will again not only be based on the size of the hike, but rather the message the Riksbank communicates about upcoming meetings.”
- “Expect the Riksbank to announce an end to QE reinvestments as of year-end… do not believe the Riksbank will start selling bonds actively and expect a passive rolling off of the current holdings… we deem markets (especially for government bonds) to be too fragile to handle active selling.”

DNB

- “Believe that this is a very close call, but expect that the Riksbank will want to send a strong signal that it takes the inflation target seriously, leading to a 75bp hike to 2.50% as a response to the high CPIF-XE reading”
- “Despite reasonable arguments for sticking to 50bp, a 75bp hike would be more in line with the Riksbank’s desire to send a strong signal to economic agents that it will do what is needed to get the inflation back to target within a reasonable amount of time. If data comes in favourably in the coming months, it would be possible to take a wait-and-see approach in February.”
- Expect the peak in the rate path to be revised higher to around 2.7%.

Handelsbanken

- Expect 75bp hike and changed forecast in light of the Economic Tendency Survey and Riksbank’s Business Survey pointed to high levels for price plans.
- Following last week’s “very high underlying inflation another 100bp hike cannot be ruled out.”
- Expect further 25bp hike in February.

ING

- Expect a 75bp hike as the “higher-than-expected inflation data trumps the mounting concerns about the housing market for the Riksbank.”
- “Expect the Riksbank’s new rate projections to factor in a further 25-50bp of tightening next year, and much will depend on the outcome of wage negotiations in the spring.”
- Expect 50bp February hike.

JP Morgan

- “See the probability distribution as 60% for 75bp, 25% for 100bp and 15% for 50bp.”
- Arguments for 75bp: “core inflation is well-above the Riksbank´s forecast. Second, near-term upside risks to inflation remain, especially for goods and food inflation. Third, keeping a “safe distance” to the ECB is needed in order to not weaken the SEK, all else equal.”

- "The concern about another 100bp hike is likely that the move in September clearly failed in terms of strengthening the SEK. Thus, markets were more focused on the low terminal rate projection. Also, large rate hikes increases uncertainty about the housing market, another negative for the SEK. We therefore assign only 25% likelihood to a 100bp hike next week. If the 100bp scenario plays out, we expect Breman and Flodén to dissent."
- "Expect a "mechanical" 25bp upward shift to the rate path. Upside risks are capped due to uncertain growth outlook"
- Tail risk that to "combine a large rate hike with a quicker reduction of the balance sheet. One option is to start actively selling only government bonds from 1Q23. This should underpin the currency, while refraining from outright selling covered bonds makes sense given housing prices are plummeting. This is a tail risk scenario, however."
- Expect "rate hike of 50bp in February (previously 25bp). Besides the spread control argument, our forecast is based on the fact that only the December inflation report will be available at the February meeting, and we expect core inflation to increase to 8.4%oya from currently 7.9%."

Nordea

- Expect 75bp hike with "Stefan Ingves, Per Jansson and Henry Ohlsson are likely to vote for a rate hike of 75bp. Anna Breman and Martin Flodén are also influenced by the surprisingly high inflation, but will probably favour a more modest rise of 50bp."
- "Risks ahead of next week's announcement are balanced."
- "See a parallel upward shift of 25bp in the rate path for almost the entire forecast period. This means a peak of just over 2.75% and an endpoint of approximately 2.50% in Q4 2025"
- See "alternative scenario" of either selling government bonds or lending bonds via repo.
- "Expect the central bank to raise rates also in February next year, but by a more modest 25bp to 2.75%. Afterwards the bank will leave the policy rate unchanged for the rest of 2023. The reason is that the economy will decelerate sharply next year, contributing to inflation moving lower. For the same reason we expect the policy rate to be lowered to 2.00% in H1 2024."

SEB

- Expect 75bp hike "but risks for another 100bps is almost as large while the chance for a 50bps hike that looked at least possible ahead of the October CPI, now seems very distant."
- See 60% probability of a 75bp hike with the rate forecast at 3.00% at the end of 2023.
- See 40% probability of a 100bp hike with the rate forecast at 3.25% at end-2023.
- "Given a high probability that Sweden is heading for a recession, we expect the policy rate to reach a peak in the first half of next year. We continue to forecast a final 25bps hike to 2.75% in February."

Swedbank

- Expect 75bp hike.
- "The Riksbank's own path implies 50 bps, but after the October CPI the risk, if anything, is that it raises by 100 bps."
- "Regardless of what is decided, the stage is set for reservations."
- Expect "rate path to show another hike of 25 bps in the first half of 2023"
- "At the February meeting we expect the policy rate to be raised by another 50 bps to 3%."

TD Securities

- Expect 75bp hike "as core CPIF has surged and major CBs have hiked more than the Bank expected."
- "Think a 50bps move is more likely [than 100bps], as headline CPIF is much lower than the Bank's forecast."

MNI Policy: A 75BP Hike Expected As Cycle Peak Nears

By David Robinson, 22 November

The Riksbank is widely expected to hike by 75-basis-points on Thursday after its November meeting, following its 100bps increase in September, but hefty declines in property prices and the Swedish central bank's own research showing high household sensitivity to interest rates suggest it will signal the end of the tightening cycle is near.

After delaying the start of its tightening campaign compared to its peers, the Riksbank has moved aggressively, with all five Executive Board members voting to increase the policy rate to 1.75% in September, when its forecast showed the policy rate peaking at a little over 2.5% in Q3 2023. While market pricing indicates that this anticipated cycle high is likely to be increased this time round, the increment is unlikely to be large.

The board's strategy of front-loading hikes to reinforce its commitment to getting inflation back to target is clear but so are downside risks.

As highlighted in analysis published in September's Monetary Policy Report Sweden's, high debt levels and the widespread use of floating rate or short-term fixed mortgages mean a policy rate of 2% would have an equivalent effect on household interest payments to one of 8% in the mid-1990s. First Deputy Governor Anna Breman also warned of the swift impact of interest rate rises in the September minutes.

HOUSE PRICES FALL

The widely used Valueguard home price index (HOX) fell 3.0% on the month in October alone, or by 2.1% seasonally-adjusted, with prices down 12% from their recent peak. Analysts' forecasts are for 20%-plus declines in house prices peak-to-trough.

The knock-on impact on the economy and the likelihood of recession in 2023 will weigh on the rate profile looking forward, with the Riksbank projecting unemployment to move back above 8% in 2024.

Late summer's inflation surge surprised the Riksbank but the target CPIF measure, which does not take changes in mortgage rates into account, dipped to 9.3% in October from 9.8% in September. The central bank's latest forecast for it to reach almost 11% at the beginning of 2023 may remain little changed in November's forecast round.

November will be Governor Stefan Ingves's final policy-setting meeting, and it may see the last sizeable hike of this cycle.