

Nordic Outlook

January 2024

Eagerly awaited interest rate cuts in a turbulent world



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Eagerly awaited interest rate cuts in a turbulent world

After several truly challenging years, the world economy is moving towards greater stability. Inflation is falling on a broad front, opening the way for lower interest rates, better household finances, lower costs for businesses, more stable consumption and, in some places, opportunities for a more active fiscal policy.

Several major concerns of recent years have faded to varying degrees. Although energy prices continue to fluctuate, not least in Sweden (which has had a cold winter so far), the price situation has greatly stabilised. We do not expect the extreme price peaks of 2022 to return. The stress in global value chains we saw in 2021 and 2022 is also largely gone. If we add that a soft landing for the US economy – both rare and eagerly awaited – seems within reach, we almost understand why Federal Reserve policymaker Christopher Waller declared in a recent speech that “For a macro-economist, this is almost as good as it gets.”

Of course, not everything is fine and dandy just because a degree of stabilisation is finally discernible. On the contrary, the world economy remains fragile. Even if the US avoids a recession, growth is anaemic in many places and risks are numerous. Given how surprised most people were by the strength of the upward phase of inflation, we cannot be sure what its downward phase will be like. If the inflation downturn encounters a setback, it will become harder for central banks to cut their key rates and we may quickly find ourselves in a completely different scenario for growth, interest rates and financial markets. Nor do we know with certainty to what extent the monetary policy tightening already implemented has had an impact, and what may remain.

Political and geopolitical risks must also be added to the macroeconomic uncertainty. The war in Ukraine is about to enter its third year, and although its direct economic impact on the rest of the world has diminished, the war continues to contribute to both

human suffering and global insecurity. The same applies to the conflict in Gaza, assaults on merchant ships in the Red Sea, attacks and counterattacks between Iran and Pakistan, North Korea’s new and more virulent rhetoric against South Korea and the increasingly tense situation between China and Taiwan. These conflicts, and other examples of increased tension between countries and regions, have both short- and long-term effects. There are many signs that we may be moving into a new world economic policy order in which politics, security aspects and a desire for “strategic independence” are replacing the globalisation and liberalisation trend of recent decades.

2024 is also a “super-election” year. More than half the world’s population lives in countries holding elections this year, which has never happened before. The US presidential election is the highest-profile contest, but India, the United Kingdom, South Africa, Russia, Indonesia, Bangladesh and other populous, important countries are holding national elections as well. We also have elections to the European Parliament. In other words, this year we look forward to following a lot of both economics and politics together with you.

This January 2024 issue of *Nordic Outlook* includes in-depth theme articles that address the following issues:

- Inflation risks
- A new world order
- A fateful US election
- Germany – a sputtering EU growth engine

We wish you pleasant reading!

Jens Magnusson
Chief Economist

Daniel Bergvall
Head of Economic Forecasting

The global economy

The United States | page 22

Inflation and wage growth have slowed, reinforcing our belief in a soft landing. The economy and labour market have remained resilient, and the Fed can cut its key interest rate without the economy having entered a recession.

China | page 29

Absent a significant growth catalyst, persistent problems in the real estate sector and low private sector confidence are limiting household spending. We expect GDP growth of 4.6 per cent this year and 4.4 per cent 2025.

The euro area | page 32

We expect GDP to speed up during the second half of 2024, and a major slump can thus be avoided. Last autumn's surprisingly fast decline in inflation is continuing, which will probably persuade the ECB to cut key rates as early as March.

The United Kingdom | page 38

High inflation and rising interest rates are having a clear impact on the UK economy. Inflation is falling, but the labour market is tight and wage growth is high. The Bank of England will begin its interest rate cutting this summer.



International overview

Greater predictability in a still turbulent world

Despite geopolitical tensions, we are starting 2024 with a dash of optimism. Many economies have moved in the right direction this autumn and winter. The slowdown is much as expected, risks are balanced, and our soft-landing scenario is alive. The inflation downturn is stirring hopes of key rate cuts, some as early as this spring. Employment will remain high, and household purchasing power will return. But overshadowing this are new conflicts, a record-warm 2023 and increased tensions as relations between countries, trade and industrial policies are reassessed.

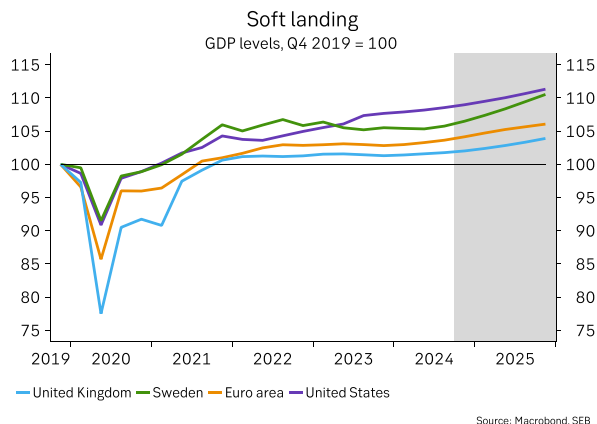
The new year has begun with mixed impressions, to say the least. Although economic predictability has increased, this is happening in an increasingly unpredictable world. The global security situation is serious and has become worse in recent years – with continued Russian aggression against Ukraine, clear risks that the war between Hamas and Israel may spread, attacks on shipping in the Red Sea and increased tensions in East Asia. Meanwhile, there are good reasons for economic optimism now that inflation is falling, in line with our earlier forecasts. This will also accelerate central bank rate cuts, resulting in less restrictive monetary policies during 2024-2025.

The global economic outlook is generally positive.

Growth in 2024 will be anaemic, especially in Europe, and labour markets will deteriorate moderately. But the foundations are being laid for a recovery in 2025, despite an environment of heightened security policy concerns. We continue to have a more positive view of inflation than the consensus, which is crucial for our central bank forecasts. We believe that big declines in GDP are not needed to bring down inflation. The ECB will be the first to cut interest rates in March, followed by the Fed and Sweden’s Riksbank in May. This will provide support to interest-sensitive sectors. Lower inflation will boost purchasing power. A more predictable economic world will support risk appetite and global stock markets, while stimulating consumption and investment.

Not a risk-free world. Quick turnarounds are fraught with risks. The interest rate wall erected by central banks may lead to delayed negative effects on both the

real economy and the financial system. We also foresee a risk of setbacks in the battle against inflation, leading to repricing of rate cut expectations. The super-election year 2024 may bring major changes in global economic and security policy cooperation and steps towards a more polarised world if the US elects a new president.



We are seeing a clear slowdown in growth in many countries, but it is surprisingly mild compared to the shocks and crises of recent years. There are continued differences between countries and sectors, but our forecast revisions are overall minor. Many countries will achieve a soft landing, avoiding deep economic downturns and sharply rising unemployment. This scenario runs counter to historical patterns, which have instead shown that high inflation could only be brought under control by a sharp economic slump. So far, statistics support the view that this cycle may be an exception. We still believe that a soft landing is possible. Yet the fact remains: Global growth of 3 per cent or less is anaemic from a historical perspective.

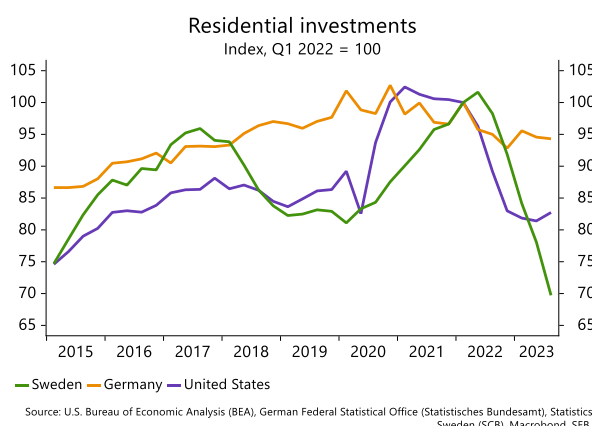
Global GDP growth

Year-on-year percentage change

	2022	2023	2024	2025
United States	1.9	2.4	1.6	1.8
Japan	1.0	1.7	1.2	1.2
Germany	1.8	-0.3	0.0	1.6
China	3.0	5.2	4.6	4.4
United Kingdom	4.3	0.5	0.2	1.4
Euro area	3.4	0.5	0.5	1.8
Nordic countries	2.7	0.1	0.8	2.4
Sweden	2.6	-0.4	0.1	2.8
Baltic countries	2.0	-1.0	1.2	2.9
OECD	2.9	1.6	1.4	2.0
Emerging markets	3.7	4.3	4.1	4.0
World, PPP	3.3	3.1	2.9	3.1

Source: OECD, IMF, SEB. PPP = Purchasing power parities

US strength and German weaknesses. In the US, growth and the labour market have remained resilient, while inflation and pay increases have slowed. We expect a late 2023-early 2024 slowdown in quarterly growth, but it will remain positive. In the euro area, growth is hovering around zero. Germany is the worst performer, as weak global demand combines with high energy prices and constrained fiscal policy to reduce growth (see the theme article on page 35). Sentiment indicators point to weaker overall growth, but no collapse. Housing investments have been a drag on growth in many countries but other capital spending – including public sector investments – has been surprisingly strong. Emerging market (EM) economies are growing in somewhat more stable fashion, but China is struggling to boost demand as households increase their savings, real estate sector woes continue and geopolitical tensions diminish trade.

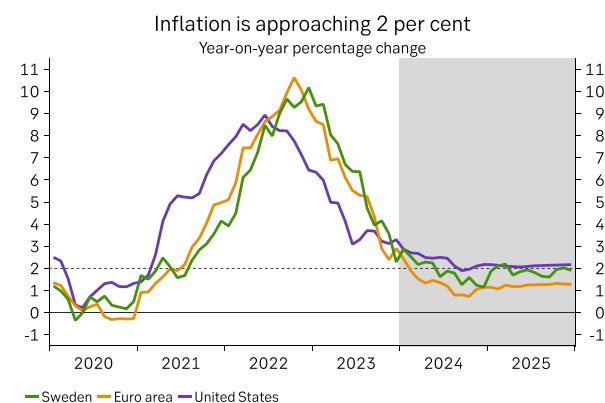


Inflation developments will be crucial

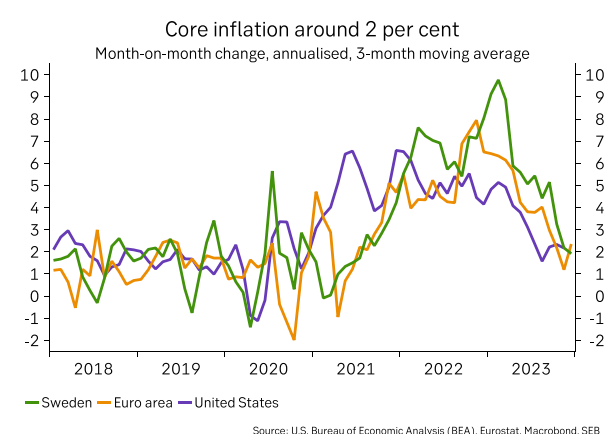
Aside from changes in the security policy situation, inflation is a crucial factor behind monetary policies and interest rates, household purchasing power and business investments. Although there are still question marks over underlying price pressures from services and wages, there are signs that inflation is falling towards central bank targets. Our forecast implies that both total and core inflation will be close to Fed, ECB and Riksbank targets within a few months. Weaker economic conditions and high inventory levels are forcing many companies to refrain from price hikes and adjust production levels. Base effects (when a new low-inflation month replaces a high-inflation month in 12-month change figures) also play a role, but we foresee a broader inflation downturn.

A focus on price momentum. Year-on-year inflation rates provide a retrospective view of price developments and do not fully illustrate the recent inflation downturn. To capture current price momentum, monthly figures (or price changes over the past three

months to smooth out the trend a bit) are more in focus. The latest annualised monthly figures indicate an inflation rate of close to 2 per cent. We believe this downward trend will continue, which implies that in a few months we should have inflation figures even data-dependent central banks can view as persistently low enough to launch rate cutting.



Both supply and demand-side factors are supporting lower inflation. The key rate hikes of the past two years have had an impact, easing demand pressure in the economy. On the cost side, broad producer prices are falling, partly because most commodity prices have fallen and global value and transport chains have normalised. At this writing, events in the Red Sea are an uncertainty factor that may lead to short-term production disruptions and inflationary impulses. But we do not consider these disruptions sufficiently widespread to fundamentally change the picture of falling global inflation.



New inflationary environment? The shocks and crises of recent years have clearly shown that we cannot take inflation of, or near, 2 per cent for granted. Inflation is on its way down, but many forces now at work could change the inflation environment going forward – on both the upside and the downside. The energy transition is one example; at least during a limited period, it may

lead to higher and more volatile prices. Similarly, artificial intelligence (AI) developments may potentially improve productivity and push down inflation, but their impact is uncertain in terms of timing and location.

Favourable inflation outcomes very likely

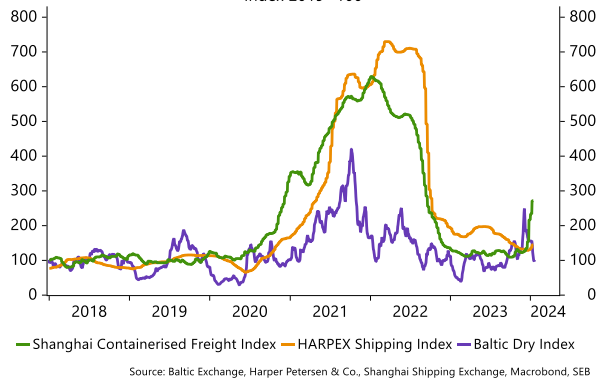
We interpret the recent downturn in inflation as a sign that demand has also eased, in line with lower economic activity. Slightly higher pay increases than the historical patterns in various Western countries are a concern, but since we are now in a situation where inflationary forces are working more broadly in the same direction, we see a somewhat greater likelihood that inflation will surprise us on the downside than on the upside. The inflation outlook is currently surrounded by unusually high uncertainty, however. This risk situation and the factors that might trigger a lower, or higher, inflation path are illustrated below (and in the theme article on page 12).

Are we underestimating the downward trend in inflation?

The strength of the inflation upturn in recent years surprised most people. Especially last autumn, we have seen that the downward trend has been strong – in some cases surprisingly so – and that high inflation figures were temporary. But even if inflation slows, the level of prices will remain well above its historical trend. In our main forecast, most prices will also remain high. But this is not certain. Yet if we imagine that one third of the price increases for goods, food and some services would be reversed, then core inflation would fall below 1 per cent by the end of 2024 and stay at that level in 2025 as well, while total inflation would drop below zero. Such a development would fuel demand via real incomes and larger interest rate cuts. We would probably also see faster growth in countries with high interest rate sensitivity, such as the Nordics.

resembling the 1970s, when inflation rose in two cycles, both triggered by rising oil prices. In this case, we expect that the second wave (contrary to the situation in the 70s and 80s) will be milder than the first and that it will be driven by higher energy and food prices, with spillover effects to other goods and services. Given a larger price upturn, central bank policymakers would face an even harsher dilemma – tightening monetary conditions to bring inflation under control while growth decelerates further. Both short-term rates and long-term yields would rise. Households that are already under financial pressure would cut back on consumption, and the decline in home prices would speed up again, especially in interest rate-sensitive economies.

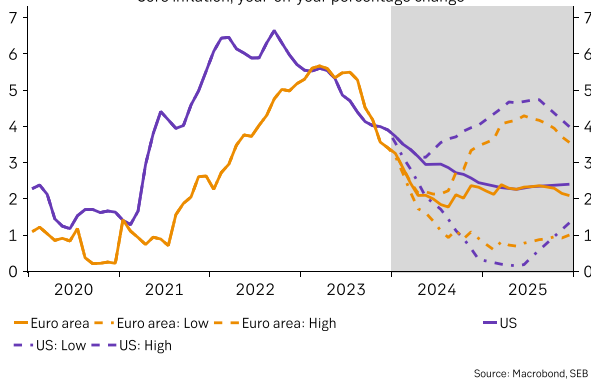
Some freight prices are accelerating
Index 2019=100



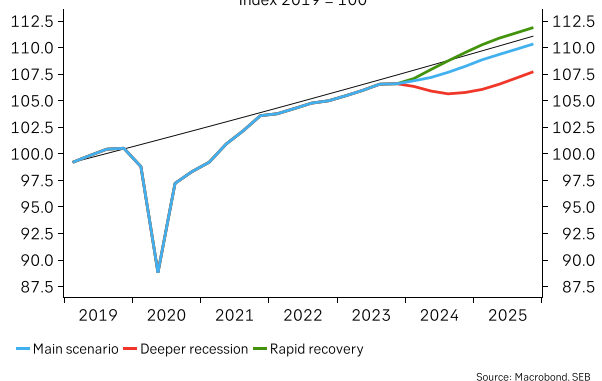
Balanced risk outlook for global growth

In our 2023 *Nordic Outlook* updates, we viewed risks as balanced or slightly on the downside. Underestimated interest rate sensitivity, geopolitical events and financial risks drove downward scenarios during the year. The theme of our positive growth scenarios was consistently linked to favourable inflation surprises.

Inflation scenarios
Core inflation, year-on-year percentage change



Scenarios for growth in the OECD countries
Index 2019 = 100



Geopolitics may fuel a new burst of inflation. The energy price shock of 2022 was a clear example of how quickly economic conditions can change. In our high-inflation scenario, we assume a series of events

Alternative inflation paths may lead to better or worse growth. Many uncertainties about inflation, central bank policies and the slowdown in growth have been clarified, and we now view the risk outlook for our

positive and negative scenarios as balanced. Inflation plays the main role in both cases this time around. Our growth scenarios are not directly linked to our alternative inflation scenarios, which illustrate possible paths (see the theme article on page 12). As described above, a faster downturn in inflation would lead to better real incomes and a faster decline in interest rates, enabling capital spending to accelerate. On the other hand, the geopolitical situation is more inflamed than for a long time. Large fluctuations in fixed income market pricing and last autumn's stock market rally are causing concern about possible setbacks. If the conflicts in the Middle East escalate – with rising energy and freight prices as a result – a repeat of the inflation upturn in 2021-2022 will not be far away. Since unemployment is relatively low in many countries, we see less upside potential in our positive scenario than downside divergence in our negative one.

Scenarios for the OECD countries

GDP growth, per cent

	2022	2023	2024	2025
Main scenario	2.9	1.6	1.3	2.0
Negative scenario			-0.2	0.9
Positive scenario			2.1	2.6

Source: SEB

Growing rivalry is changing the world

Global cooperation is being put to several tests. After 30-40 years of deregulation in global trade and growth in multilateral cooperation, the world is now taking steps in the opposite direction. The COVID-19 pandemic, the war in Ukraine and increased tensions between the US and China, among other developments, show the vulnerability of global value chains and the risks that have built up in a number of strategic areas. The previously optimistic (or naïve) view that trade democratises the world and makes conflict impossible is now being abandoned and replaced by trade barriers, tariffs and subsidies.

Globalisation is being replaced by regionalisation and fragmentation. This development is partly driven by a desire to correct past mistakes and market failures, but it also includes clear elements of protectionism, with politicians wishing to promote domestic production and take back national control over industrial policy (see the theme article on page 18). The extent of these changes and their economic impact – on capital flows, investments, prices, etc. – are uncertain, but these are issues we must deal with in the future. It is especially important to small export-dependent countries such as

the Nordics to ensure that the European Union has a strong voice when new regulations are hammered out.

Interest rate cuts will dominate 2024-2025

Late in 2023, several central banks confirmed that their key interest rate had peaked. Meanwhile the Fed and others opened the door to looser future monetary policies, including lower key rates. Falling bond yields and rising stock markets have already helped ease financial conditions. Our key rate forecasts from last autumn have been confirmed, supported by continued declines in core inflation and inflation expectations. The ECB will be the first central bank to cut key rates in March, while the Fed and the Riksbank will wait until May. The Bank of Japan will go its own way, abandoning its negative key rate this year but remaining at an extremely low 0.10 per cent at the end of our forecast period. Although the peak in the US key rate has become shorter according to the latest market pricing, it is not extremely short from a historical perspective. Assuming a Fed rate cut in May, it will be 9 months long. Since the 1990s, these peaks have varied in duration between 5 and 18 months.

Central bank key interest rates

Percentage at year-end

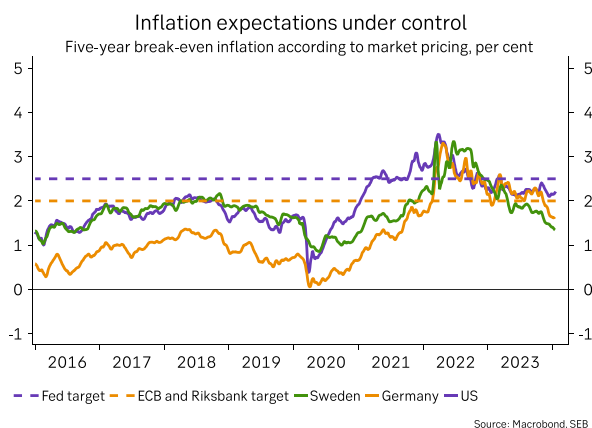
	Jan 18	2024	2025
Federal Reserve	5.50	4.00	3.00
ECB*	4.00	3.00	2.00
Bank of England	5.25	4.00	2.75
Norges Bank (Norway)	4.50	4.00	3.00
Riksbank (Sweden)	4.00	3.00	2.25

*Deposit rate

Source: SEB

Central banks need to come to terms with these

facts: (1) short-term real interest rates are rising as inflation falls, in an environment of lower economic activity, and (2) neutral real interest rates may return to low pre-pandemic levels, making monetary policy more restrictive the longer key rates stay at today's levels. Our forecasts of core inflation in the US and the euro area, for example, indicate that inflation targets will be achieved during our forecast period. This reduces the need for restrictive monetary policy, i.e. key rates above 2-2.5 per cent. The stress of higher long-term inflation due to structural changes – such as a more fragmented world economy and the energy transition – is being mitigated by the fact that the market's long-term inflation expectations have been surprisingly stable during the inflation shock. They have even been falling for the past two years.



The Fed is expected to slow the pace of reducing its balance sheet (quantitative tightening, QT). This decision is not primarily motivated by monetary policy but is related to the need for short-term liquidity in the financial system. When the Fed was buying assets, for example during the pandemic, there were three reasons: (1) to signal that the key rate would remain low for a long time, (2) to push down long-term yields and (3) to safeguard financial stability. QT has been less important as a monetary policy tool and has instead been motivated by a desire to normalise central bank balance sheets, thereby reducing the amount of excess liquidity. But financial stability considerations are important for the speed at which central banks move ahead with this process.

Energy: Lower but still elevated prices

Oil and especially European natural gas prices have fallen sharply since their peak in August 2022. In spite of this, demand for gas remains 15 per cent lower than normal in Europe, if we disregard temporary weather effects. One explanation is that energy is still expensive, with natural gas and electricity prices at some 60 and 110 per cent above their 2010-2019 averages, respectively. Europe's cost situation compared to the rest of the world has also worsened. European energy prices are based on relatively expensive gas. On top of that, CO₂ taxes have increased. Meanwhile, energy costs in many other countries are based on cheaper coal. For example, the US has far lower natural gas prices, and in most cases the mark-up due to environmental taxes is lower. In the short term, households find it hard to vary their energy consumption to any great extent, but the relative change in energy prices is something that affects businesses and helps keep demand below normal. Our gas and oil forecasts do not differ much from today's prices. The price of oil will be USD 85-90 per barrel in 2024-2025, and natural gas will remain stable at USD 40 per MWh.

Central bank policies determine long yields

Favourable inflation surprises last autumn and market expectations of earlier and faster interest rate cuts caused bond yields to fall sharply late last year. The decline since their October 2023 peak implies that the key rate cuts in our forecast have largely been discounted. With long-term yields already at low levels, continued downside potential is limited. A continued downturn would probably require the market to price in even further central bank rate cuts. Quantitative tightening (QT) is limiting downside potential as well. There is also uncertainty related to large budget deficits, especially in the US. But we do not believe that issuance volumes will be a driving factor over the next couple of years, since the US is expected to issue more short-term Treasury securities to ease pressure on longer maturities. The Fed is likely to reduce QT volumes earlier than the market has predicted. We believe that US 10-year Treasury yields will fall to 3.60 per cent by the end of 2025. Their German equivalent will be at 2 per cent.

The SEK turnaround has begun

The EUR/USD exchange rate bottomed out in September 2022 after nearly 15 years of a strong US dollar. Much of the euro's appreciation against the dollar since bottoming out occurred relatively soon after the turnaround, and during 2023 the euro's continued upward path was volatile. We expect a higher EUR/USD rate this coming year, driven by better risk appetite and wider interest rate spreads, as the Fed cuts its key rate at a faster pace than the ECB, but not necessarily first. In a broader foreign exchange (FX) market perspective, we expect economies – and currencies – that have performed weakly due to high interest rate sensitivity to undergo a reverse effect when key rates are cut in 2024 and 2025. This means that the JPY, NOK, NZD and AUD will be among the winners. The SEK should also benefit, although most of its appreciation probably already occurred in late 2023.

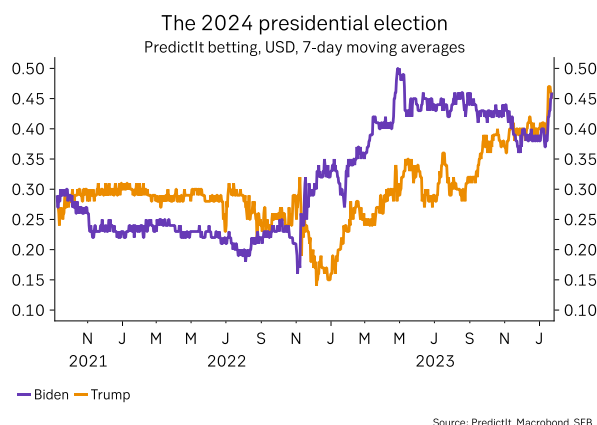
Support for the SEK and NOK in the short and long term.

The Swedish krona experienced a sharp rebound late last year. This came after a weak start to 2023, when it weakened to around SEK 12 per euro, but by year-end it stood at SEK 11.10 per euro. We expect SEK appreciation to continue after a pause, driven by a soft landing in the US, upcoming key rate cuts and the improved risk appetite that such a scenario is expected to generate. We also believe that SEK support will continue into 2025, but more because key rate cuts should help Sweden's interest rate-sensitive economy grow faster – a reversal of what happened when rates

were hiked rapidly and the economy slowed sharply. The same factors will benefit the Norwegian krone, which will also be supported by Norges Bank's later, slower pace of rate cuts.

Super-election year 2024

This year, geopolitical uncertainty will be spiced up by the fact that countries with a total of more than half the world's population – just over 4 billion – are going to the polls. To some extent, this figure may lead to exaggerated hopes for change, since only slightly more than half of these elections are regarded as free. The election in Taiwan a couple of weeks ago (which belongs to the free election category) has fuelled uncertainty about the island's relationship with China, since the more China-critical governing party DPP won. But topping this year's political agenda is undoubtedly the US presidential election in November. Most indications are that it will be a rematch between the incumbent president, Joe Biden, and former president Donald Trump. The US presidential election is important from several international perspectives, such as the Paris Agreement, NATO and support for Ukraine (see the theme article on page 12). In addition, there are elections in eight of the world 10 most populous nations, including India, Pakistan, Bangladesh, Indonesia, Mexico and Russia. In the EU, elections to the European Parliament will also take place. Although political changes often take time, the 2024 elections are occurring amidst geopolitical tensions and ongoing wars, while new rulebooks are being written on trade, environmental issues, global cooperation and conflict resolution. The year's many elections may thus play a bigger role than usual. In many countries, there is also increased support for nationalist parties, which may complicate international cooperation in the future.



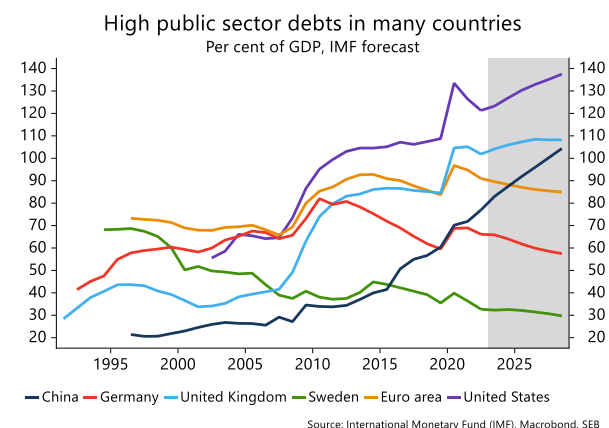
Stocks still have further upside potential

Last year's stock market returns, after the autumn rally, probably surpassed what most people expected at the beginning of 2023. The upturn, which was driven by

investors' belief in a soft landing, lower inflation, lower long-term bond yields and hot AI stocks, is now searching for new drivers. If our main scenario for the world economy proves correct, the most important driver will be corporate earnings growth, but it will probably take a couple of quarters before we see such an effect in global stock markets. We expect some volatility when earnings take over as a driving force, especially in the interim before we see that GDP growth is accelerating. Equities with already high valuations, especially tech stocks, need to prove their worth by generating earnings. Our scenario is that an upturn may begin when the rate cutting cycle starts. While we wait for a macro recovery, our focus is instead on "2023 losers" such as Nordic companies, small caps and fossil-free energy stocks.

Fiscal policy will focus on necessities

Despite an anaemic economy, fiscal policy will be largely neutral in the next couple of years, making it easier for central banks to cut interest rates. Already high public sector debt is limiting room for manoeuvre in many places and has occasionally been a source of concern in financial markets over the past six months. In many cases, fiscal policy regulations – some of which were on hold during the pandemic and the energy crisis – also impose limits on how expansionary budgets can be. Countries such as Sweden and Germany, which have relatively low debt and have experienced major declines in growth over the past year, could pursue a more active fiscal policy. In these cases, a combination of rules and political priorities has instead set limitations. Inflation is now falling and is thus disappearing as a constraining factor for fiscal policy in Sweden and elsewhere, but the scope for expanding subsidies or cutting taxes is also limited by the need to invest more in defence, security policy and the green transition due to the tense geopolitical situation and last year's record temperatures.



Theme:

Inflation risks

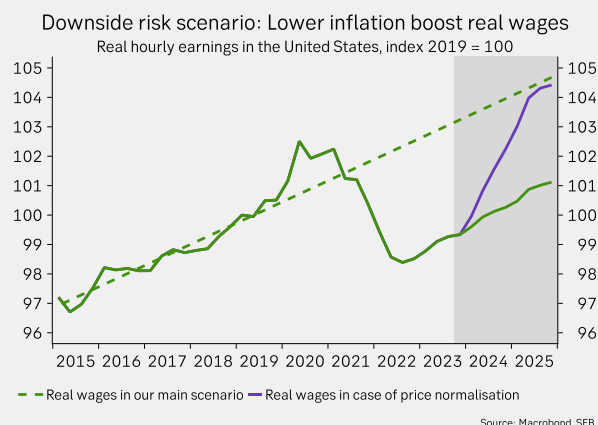
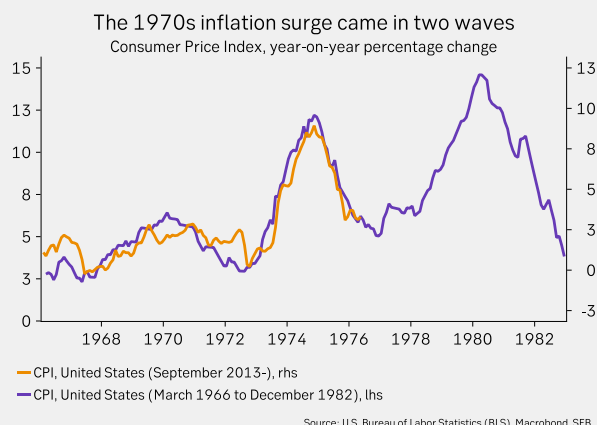
Are we underestimating downside forces, or is a new wave coming?

Inflation is clearly on its way down worldwide. Both we and the market expect it to be close to central bank targets in 2025, after a brief period of below-target inflation. But the large price increases of recent years represent a major shift from the long period of very stable inflation that began in the mid-1990s. This theme article highlights what we regard as the main risks in our forecasts and provides examples of what low- and high-inflation scenarios may look like. The focus of the article is on the United States and the euro area, but the risks are similar in most countries, including Sweden. The risks over the next 12-18 months are expected to be larger on the downside.

Surprisingly powerful... The strength of the inflation upturn in recent years surprised both central banks and forecasters. The starting point for the upturn was exceptional, with extremely large fiscal stimulus measures that boosted demand at the same time as lockdowns were causing major production and transport disruptions. The pandemic was followed by the war in Ukraine, with extremely large increases in energy and food prices.

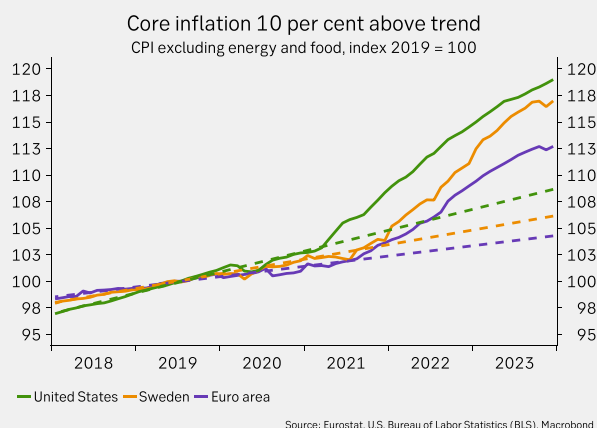
...yet temporary. Over the past 6-12 months, inflation and inflation expectations have fallen rapidly. Most indications are that the upturn was temporary. However, there is a lot of uncertainty about how far the inflation rate will fall or whether some of the price increases may even be reversed. Meanwhile, the past few years demonstrate that low inflation cannot be taken for granted and that because of the complicated geopolitical situation, there is a significant risk of new production and price disruptions. The events of the 1970s have been cited as one example. The inflation of that decade came in two waves, with both upturns initially driven by rising oil prices. Based on these risks, we have developed risk scenarios for inflation in the euro area and the US.





Downside risk scenario: Some of the 2021-2023 price upturn will be reversed. The inflation rate has slowed, but the price level is still well above the trend that prevailed five years before the pandemic. At the same time, despite a slight recovery, real wages are far below their historical trend. This decline is not explained by falling productivity.

The overall dynamic in the euro area will be similar, but there are differences in how various elements of the CPI react. Although the origins of the inflation upturn are the same, we cannot ignore the fact that fiscal stimulus measures have driven demand to a far greater extent in the US than in the euro area. Resource utilisation was and is tighter in the US. This means there is probably a larger demand component in US inflation, for example contributing to a smaller reversal in service prices in the euro area. On the other hand, goods prices in the euro area were more affected by high energy prices, so the decline in goods prices will be greater in the euro area than in the US. Measured as core inflation, the scenario is similar for both.



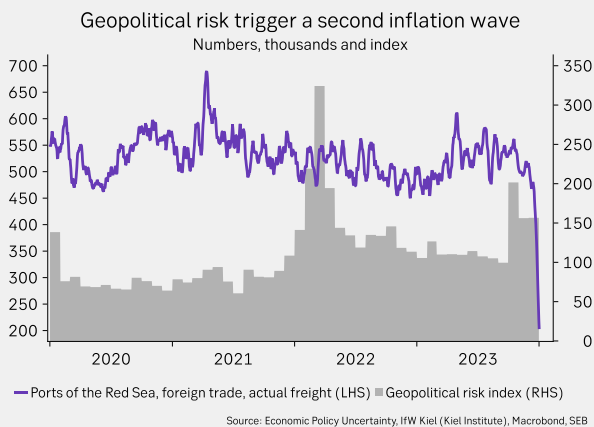
Real wages in the euro area are strongly affected by energy prices, which is one reason why real wages initially fell more than in the US. The peak in energy prices has long since passed, but due to the lingering effects of price controls and various types of contracts, the energy component of the inflation metric is moving sluggishly. There are probably countervailing factors, but this means that real wages will recover a little faster towards the end of our forecast horizon, when energy prices will still be keeping CPI below a 2 per cent annual growth rate.

Rapidly rising wages are offsetting only a small part of the price increases, and our main forecast indicates that real wages will remain well below the pre-pandemic trend. Higher profit margins in the business sector have contributed to the price upturn, although there are significant differences between sectors. Prices for both food and other goods are 15 per cent above the pre-pandemic trend, while rents and other services are almost 10 per cent higher. Our main forecast is that commodity prices are among those that will generally not fall, which is consistent with the historical pattern. But if we assume that just below 30 per cent of the divergence from trend closes during the next two years, real wages will revert to the 2015-2019 trend. As a result, core inflation would temporarily fall to just above zero by the end of 2024 and then recover to around one per cent towards the end of 2025. Headline inflation would fall to just below zero over the same period.

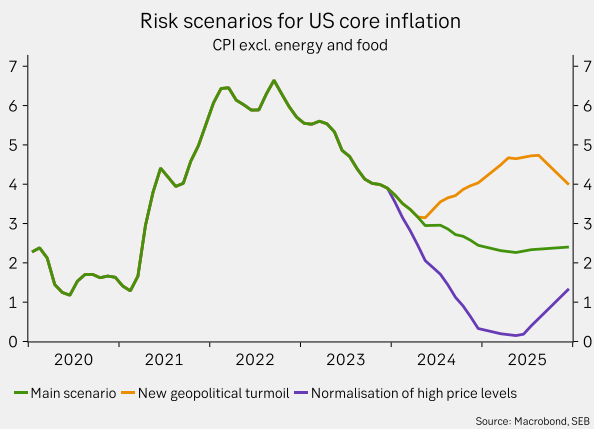
Upside risk scenario: New geopolitical turmoil.

Determining the magnitude of the impact of a new geopolitical crisis that creates a second wave of rising commodity prices as well as production and transport problems is more difficult than our low inflation scenario. Our high inflation scenario is reminiscent of what happened in the 1970s, when inflation rose in two cycles, both triggered by soaring oil prices. Unlike in the 1970s, we are now assuming that the second wave of price increases will be more limited than the first. This scenario assumes that international food and goods prices will climb to a level 10 per cent higher than their peaks in 2022, while oil, natural gas and electricity prices rise 30 per cent from current levels. The upturn in

processed goods prices will be driven by a combination of secondary effects from increased prices of energy and other inputs, but also by supply constraints caused by barriers to world trade. Higher inflation expectations will contribute to faster wage increases in this scenario. Over a year and a half, food and other commodity prices will increase by 5 per cent more than in our baseline scenario, while services prices will increase by 3 per cent more. As a result, core inflation in the US will rise to just above 4.5 per cent in 2024 but fall back slightly towards the end of 2025. A rapid rise in energy prices will cause headline inflation to climb 5.5 per cent by early next year and then fall back.

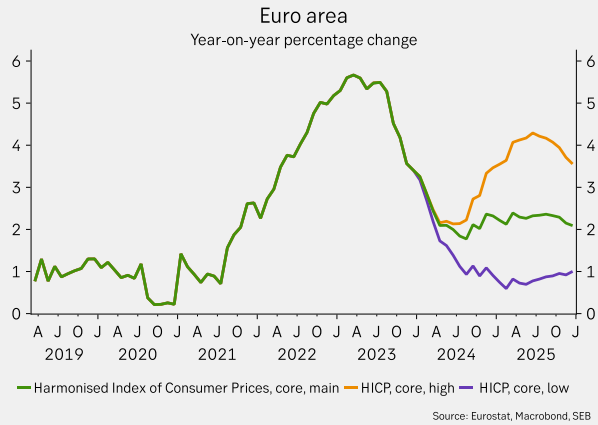


In this scenario of a second inflation wave, the deviation in the US and the euro area will also be similar, but with slightly divergent dynamics. Because of different institutional conditions, the US economy usually responds both faster and with greater volatility than European economies. Examples are rapid changes in the labour market and rapid wage adjustments, but this can also be seen in greater variation when comparing different parts of the CPI basket.



Initially, the US will be in a situation of tighter resource utilisation, which in this scenario will also contribute to a stronger reaction in service prices to various spillover effects. Meanwhile the vulnerable energy situation in

the euro area will lead to a greater impact on goods prices. Food, but especially energy, will also contribute more to inflation. Despite lower core inflation, the euro area's CPI divergence will be larger in the upside risk than that of the US.

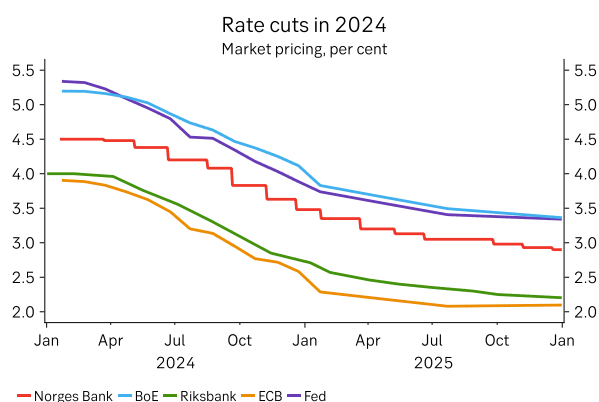


Symmetric scenarios may lead to asymmetric monetary policy reactions. The above two scenarios provide a roughly symmetrical picture in relation to our main scenario. But the monetary policy response may be somewhat different. In scenarios where price levels are partially reversed, relative prices will be partly restored, and it will be possible to say that some prices have been unjustifiably high. Profit margins will be falling, while the wage share of GDP will be regaining lost ground. Lower inflation will improve household purchasing power without central banks needing to support demand further, although this will probably mean that key rates can be cut somewhat earlier and somewhat more than in our forecast horizon. In the second wave scenario, on the other hand, central banks will need to act more forcefully to further curb inflation driven partly by compensation demands in future wage negotiation rounds – either by hiking key rates more or by keeping them high for a long time to come. Compared to the second inflation wave of the 1970s, it is important to remember that a different monetary policy regime prevailed at that time and that under today's system, it should be possible to contain a second wave relatively fast.

Fixed income Central banks in driver's seat

Discounting the upcoming rate cutting cycle, long bond yields have already fallen to levels where the potential for further decline is relatively modest unless policy rates are reduced significantly below the levels we currently expect. Quantitative tightening (QT) and increased supply are expected to put upward pressure on Swedish yields and widen the spread vs Germany. Delayed rate cuts by Norges Bank and increased long-end supply will limit performance in Norwegian bonds.

Favourable inflation developments and lower policy rate expectations pushed bond yields sharply lower in the fourth quarter of 2023. Yield curves in the United States, euro area and Scandinavia are inverted, with long yields already at low levels. Developments in bond yields will primarily depend on how expectations about the upcoming rate cutting cycle evolve.



US rates: Policy rate expectations are key.

Historically, long yields tend to trend lower throughout interest rate cutting cycles. Given already low yield levels, the downside is relatively modest even if the federal funds target is cut to our forecast of 2.75-3.00 per cent at the end of 2025. Clearer signs of labour market weakening may temporarily make long yields undershoot to levels that are not sustainable if a soft-landing scenario becomes confirmed during the year, in line with our expectations. Supply pressure will not be a key driver for bonds in 2024, especially since it is likely to be counteracted by the Federal Reserve slowing the pace of its balance sheet reduction. The 10-year

Treasury yield will be 3.80 per cent in mid-2024 and decline further to around 3.60 per cent in 2025.

Euro area: Only minor downside in long rates. We believe that the European Central Bank (ECB) will start cutting policy rates in March and reduce the deposit facility rate to 2.00 per cent in 2025. Long yields in core countries are already low, and we expect only minor declines in the coming two years. The ECB has decided that it will speed up the reduction of its securities holdings beginning in July, which also act as a drag. We believe that the German 10-year yield will fluctuate around 2.00 per cent during our forecast period.

10-year government bond yields

Per cent

	Jan 18	Jun 2024	Dec 2024	Dec 2025
United States	4.14	3.80	3.70	3.60
Germany	2.31	2.10	2.00	2.00
Sweden	2.28	2.35	2.30	2.40
Norway	3.59	3.50	3.25	3.15

Source: National central banks, SEB

Sweden: Upward pressure from QT. After trending gradually higher, the 10-year yield spread to Germany fell at the end of 2023. We expect the upward trend to resume. The Riksbank strongly indicated that it would increase selling of government bonds again in February. We expect it to raise monthly volumes from SEK 5 billion to SEK 7-8 billion. The National Debt Office is also likely to gradually increase supply in 2024, due to a SEK 40 billion recapitalisation of the Riksbank and a larger government budget deficit. We predict that the 10-year spread to Germany will rise to 30 basis points by year-end.

Norway: Upward pressure from supply. Because of excessively high core inflation and NOK depreciation, Norges Bank prolonged its rate hikes into December, resulting in the yield spread between Norwegian government bonds (NGBs) and Germany to widen. Exchange rate concerns and sticky core inflation are reasons for Norges Bank to delay its rate cuts relative to the ECB. Moreover, NGB supply will increase by NOK 20-30 billion to 100-110 billion this year of which the majority will be centred in the long end. This adds steepening pressure on the yield curve and limits potential for spread tightening against Germany. We expect the 10-year spread vs Germany to be broadly unchanged at 125 basis points by end-2024, narrowing slightly to 115 basis points by end-2025.

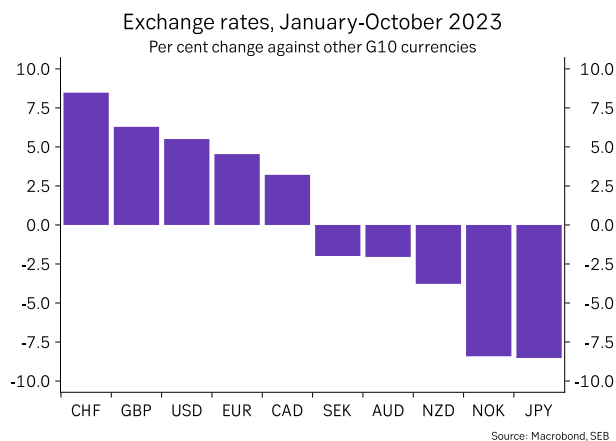
The FX market SEK turnaround has begun

As expected, Swedish krona weakness turned into strength late in 2023 when central banks were increasingly regarded as done with key rate hikes. We expect currencies that were weak during the hiking cycle to appreciate as the rate cutting cycle begins. This implies a stronger Swedish krona, Norwegian krone and Japanese yen, among others. The EUR/USD upward journey during 2023 was volatile. We expect the EUR/USD to end 2024 higher than when the year began.

Stronger SEK and NOK this year. The turnaround for the Swedish krona finally came in November-December 2023. Its appreciation was strong and came after a weak start to the year, and in late September even a record low against the euro. Some of its appreciation has reversed in early 2024. Our assessment is that as central banks, led by the ECB and the Fed, move towards rate cuts, the krona will regain its strength. The EUR/SEK exchange rate will thus be lower at the end of 2024 than when the year began. Initially, the main driver will be a soft landing in the US economy and gradually US rate cuts. This will provide support in the form of a better relative interest rate differential, but mainly through an improvement in global risk appetite similar to what happened in late 2023.

Krona support will continue, but with new drivers. The krona should receive continued support into 2025, but more because rate cuts will have a faster positive impact on Sweden's interest rate-sensitive economy. There are even better arguments for the krone early this year, since Norges Bank is expected to provide extra support through later and fewer rate cuts as inflation falls more slowly in Norway than other G10 countries. The biggest risk to our scenario of a stronger SEK and NOK is if the US economy makes a hard landing. This would lower global risk appetite and initially weaken SEK and NOK rates. But an analysis of similar earlier periods shows that both the SEK and NOK usually only lose ground initially, then strengthen even more. A hard landing does not necessarily mean they will be weaker against the euro at the end of 2024 than at the beginning, but they do risk being significantly weaker for a short period.

The hiking cycle was a clear driving force for currencies last year. In 2023, the driving force until November was the rate hiking cycle. Currencies backed by countries with lower interest rate sensitivity (CHF, GBP, USD and EUR) received support, while rate-sensitive JPY, NOK, NZD, AUD and SEK performed weakly.



This year's rate cutting cycle will probably push in the other direction. Expectations are high that the rate cutting cycle will begin this year. The big question is how soon and how quickly these cuts will come. In a soft-landing scenario, where rates can be cut at a calm and controlled pace, the FX market should be able to move in the opposite direction compared to 2023. This was the dominant FX market trend in November and December 2023, but in early 2024 the market encountered a slight correction. Once the rate cutting cycle starts to become a driving force again, the JPY followed by the NOK, NZD and AUD will be winners. The SEK should also do well, but some of its appreciation potential probably materialised as early as the end of 2023. The scope for a strong SEK performance this year is probably a little smaller.

Exchange rates

	Jan 18	Jun '24	Dec '24	Dec '25
EUR/USD	1.09	1.12	1.14	1.18
USD/JPY	148	139	132	127
EUR/GBP	0.86	0.91	0.93	0.97
EUR/SEK	11.41	11.15	10.95	10.75
EUR/NOK	11.45	11.15	11.05	10.90
USD/SEK	10.51	9.96	9.61	9.11
USD/NOK	10.55	9.96	9.69	9.24

Source: Bloomberg, SEB

EUR/USD and Fed vs ECB. The EUR/USD rate bottomed out in September 2022 after about a 14-year decline. Its upward trajectory was bumpy last year, but we expect EUR/USD to continue rising slowly this year, driven by risk appetite and better interest rate differentials as the Fed cuts more, but not necessarily earlier, than the ECB.

The stock market

More upside in 2024

Strong returns for global equities surprised many investors in 2023 as recession failed to materialise. In 2024, the return driver will shift from valuation to earnings as the economy recovers. This could lead to some turbulence at first, but we expect another positive year, with cyclicals in the lead.

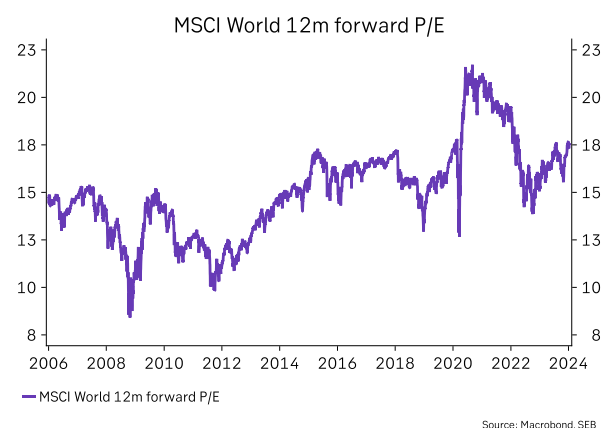
From an equity perspective, there were three key questions to get right in 2023. The most important one that investors needed to answer correctly was about something that did not happen. At the start of the year, many investors were positioned for a recession in the wake of key interest rate hikes and inflation shocks. As it turned out, this scenario was averted because the inflation shock had its origins on the supply side and fell without a recession. This resulted in an increase in equity valuations as investors repositioned for a less negative growth AND interest rate outlook than expected.

The second key question was whether to embrace AI hype. Investors did, allowing stock prices to move higher for AI-related companies despite elevated valuations, and we think they were right to do so, because a) it really is a revolutionary technology and b) tech stocks are supported by high earnings growth. The third key question was whether China's reopening would boost its economy. It did not, mainly because the real estate market crisis ended up dragging the economy back down, along with commodities and EM stocks.

As we head into 2024, a new set of questions is emerging. The repricing of the interest rate outlook is largely completed, and valuations for global stocks are now at the top end of their pre-pandemic range and well above the historical median. If the US 10Y Treasury yield breaks below 3.5 per cent, markets are likely to see it as a reflection of recession risks and the correlation is likely to flip, so that equities no longer react positively to bond yield declines. If the economy does not weaken, then markets may have priced too many rate cuts already.



The alternative driver is earnings growth, but it will most likely take a few quarters before an economic recovery opens the way for an upside to earnings. When this happens, it will reverse at least one of last year's main trends. A Chinese recovery could kickstart a global manufacturing upswing, but the policy conditions do not appear to be in place. At the same time, elevated tech stock valuations need to be supported by earnings as interest rate support fades, but with 12M forward earnings-per-share (EPS) growth of close to 25 per cent in the global technology sector, that support is in place.



We may see some volatility as rising earnings replace higher valuation as the main driver of returns, especially if there is an 'air pocket' between the trough for rates and the start of an earnings upgrade cycle. In the near term, this limits upside for the broader global stock market.

However, our base case is that a global expansion will start once the rate cutting cycle starts and that earnings growth will allow global equities to deliver (USD) returns of 5-10 per cent, with cyclicals in the lead. In the early part of the year, while we wait for a macro recovery, we recommend exposure to cheap relative losers in 2023 like Nordics, small cap and clean energy stocks.

Theme:

A new world order

Towards more geopolitically oriented economic policies

The role of the market economy as a force for change is increasingly being deprioritised, while national security policies and geopolitical rivalries are increasingly overshadowing the formulation of economic policy. We are also seeing an increasing fragmentation of the world economy and a strongly articulated desire among the world's leading economies to make themselves less interdependent. This trend is not uniform, but clear steps are being taken towards a more geopolitically oriented economic policy agenda, especially by the United States.

These developments risk having far-reaching consequences for the globalised economy and the world order that we have come to know over the past 30-40 years. They are now forcing both companies and financial institutions to prepare for sometimes rapid and significant changes in their operating environments.

The many crises of recent years, not least the COVID-19 pandemic, the climate and energy crises and a serious new security policy situation, have exposed challenges in the functioning of the global market economy and its strategic supply chains. Many of these shortcomings need to be addressed by both the public and private sectors, and “just-in-time” thinking needs to be balanced by “just-in-case” thinking. The far-reaching transformation of our societies that the climate crisis requires, for example, have also created an additional appetite for political interventionism.

It is all about creating new forms of collaboration between private and public actors, supporting individual industrial sectors, controlling trade flows or reshaping markets to achieve the desired political results. However, it is not easy for political systems around the world to pursue sustainable and predictable policies that create the right conditions for private actors to invest and contribute to solving long-term systemic global problems. Nor is it an easy balancing act to combine market forces with increasing political control.

The rising degree of political intervention in the economy that we are now seeing risks eventually also including parts of the economy that are not strategically important from a security perspective. This development is taking place in parallel with more visible cracks in our democratic systems, often driven by an increasing contradiction between taking back national control and continued internationalisation.

There is a risk that this development will intensify the fragmentation of the world economy that is already underway. It would result in further efficiency losses, a decline in innovation power and poorer prospects for solving global challenges such as the climate crisis. Small open economies such as the Nordic and Baltic countries would be especially hard hit.



New US economic leadership

The world has entered a new era of major shifts and sudden interruptions. Renewed strategic competition – economic, ideological and technological – between the world’s two largest economies, the United States and China, is ending an era of economic hyper-globalisation that has been dominant since 1991 (when the Soviet Union collapsed) and 2001 (when China joined the World Trade Organisation, WTO). This period of “geopolitical peace” enabled multinational enterprises to develop an efficient system of global value chains.

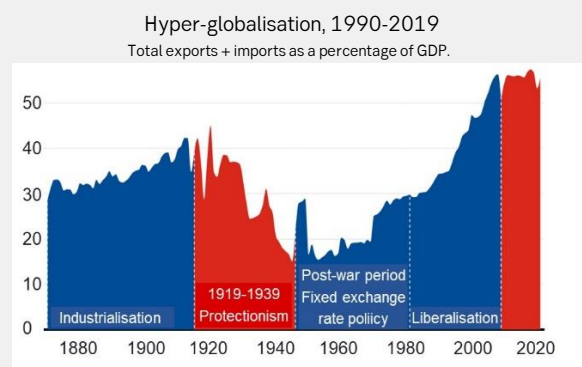
Now that the world’s largest economy, the US, is re-examining its global economic leadership and putting an emphasis on security policy considerations and the role of government in the market economy, a rapid shift is under way towards a new system. The new US stance may have a powerful impact on global trade and investment flows and serve as a model for other countries. This transition may thus have potentially far-reaching consequences for the world order we know and for the global economy.

One of the clearest signs of a shift in global economic policies is related to the large-scale industrial policy investments being made in many leading economies. This is changing the operating environment for both companies and financial institutions and means that we are moving away from a world that has emphasised the importance of global cooperation and the role of the market economy as a positive force for change. Instead, the focus is now on the strategic needs of the nation-state. International dependence is seen as a weakness that politicians actively want to remedy, and the market economy is being subordinated to other interests.

This is a world in need of new global rules of the game, since the current rules are no longer being fully complied with. Until we have new rules, there is a risk that “might makes right” will prevail. This situation is thus similar to the state of the world economy before 1945. Given the many years of globalisation, rules-based international order and economic integration we have behind us, the transition to a new world order can be expected to be both stressful and challenging for many countries and companies.

The US-led globalisation we have seen over the past 30-40 years was rejected as an ideal by the US in April 2023 in a now-historic speech by President Joe Biden’s national security advisor, Jake Sullivan. This speech¹ immediately became known as the “New Washington

Consensus”. While the old consensus made use of global institutions and, for example, the WTO’s economic rule-book, the new consensus prefers strategic value-based alliances and geopolitical trade agreements instead of free trade and economic multilateralism. By embracing this new policy, the US appears to be moving away from long-standing commitments to economic internationalism and free/open markets that had been guiding principles of US economic policy since the end of the Cold War.



Sullivan’s main message is that US foreign policy was crafted in an era that is now part of history, that government should play a greater role in the market economy and that international power is determined by the strength of the domestic economy. Sullivan even argues that globalisation and the market economy have weakened the US. Alliances with other countries must therefore be updated to reflect the challenges of today and coming decades. The US Congress probably shares the White House’s conclusions. The key question is whether global trade is a zero-sum game in which “one man’s meat is another man’s poison”, as some security policy experts suggest, or whether everyone gains from global trade, as most economists claim.

One area where America’s new attitude is being manifested is trade. The WTO, multilateralism and free trade are becoming less and less important. Much of this is related to minimising Chinese influence. For some time, Mexico – not China – has been America’s biggest trading partner. In an oft-quoted speech from 2022, Treasury Secretary Janet Yellen elaborated on the new US trade policy thinking. She used terms like “friend-shoring of supply chains” to describe how trade relations with countries that are especially close to the US should be strengthened in order to reduce risks in strategic supply chains and in the American economy.

Industrial policy – growing importance

Another area characterised by America’s new approach is industrial policy, which President Biden has

¹ See “Renewing American Economic Leadership,” April 27, 2023.

introduced into US politics on a broad front through the Inflation Reduction Act, the Chips and Science Act and the Infrastructure Act. According to McKinsey, over the next ten years the federal government will supply nearly USD 2 trillion² through these three programmes, which together are capable of shaping the US economy and US technological development and steering global investment flows. Much of President Biden's legacy is expected to focus on these large-scale investments.

In both China and the European Union, and in many other big economies, there is similar thinking about trade and industrial investments. China's "Dual Circulation Strategy" is also all about increasing the country's independence, among other things by stimulating domestic consumption and continuing to move higher in industrial and technological value chains. China has also identified a number of key technologies in which it wants to increase domestic industrial capacity. The EU, like the US and China, is seeking to increase its independence under the slogans *strategic autonomy* and *technological sovereignty* and has launched a climate-oriented industrial policy and investments in batteries and semiconductors. However, the EU has not rejected globalisation in the same way as the US, and there is still greater acceptance of trade with China in such fields.

The aim of these industrial policy initiatives is to correct for the inability of the market to create desired developments and to regain strategic industrial and technological capabilities that companies have delegated to other parts of the world for reasons of efficiency. The drawback of this approach is that such a policy runs the risk of creating new problems if the political system lacks sufficient information or is coloured by political choices. It will now become the task of politicians to allocate resources and determine the design of supply chains or which markets, industries and innovations have a future.

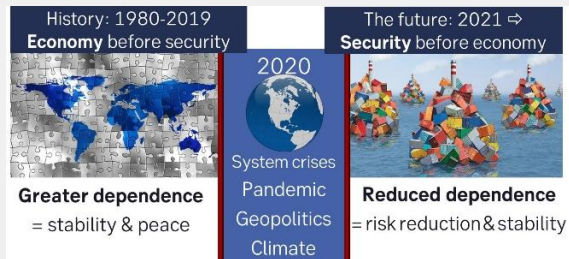
The pandemic and the new security policy order have shown that national and global security challenges may need to be prioritised. As part of this, various kinds of trade restrictions may be tools that provide increased stability. But there is a risk that this will destroy free competition and the positive drive to promote the best solutions in market terms. It will also lead to increased costs and a risk that restrictions and subsidies may also expand to goods that are considered non-strategic.

In retrospect, before 2020 there was perhaps a simplistic view that mutual dependencies via deep

economic and financial cooperation would ultimately - lead to greater stability and fewer military conflicts. Systemic crises affecting all of the world's countries – an accelerating climate crisis, the pandemic and the rapidly deteriorating security situation – were a rude awakening. It became clear that increased economic and financial integration does not automatically lead to democratisation and shared values.

Two or more competing blocks?

Systemic crises became catalysts that has caused a shift in the world economy towards greater fragmentation. This development may not only threaten economic and financial stability, but also poses a risk in dealing with new systemic crises such as pandemics. Confidence gaps between countries have grown in fields such as technological development and AI, while access to critical natural resources is becoming strategic and turning into a security policy pawn in an ongoing global political game.



The dominance of the West is being questioned and challenged to some extent today by regional powers and countries that are trying to find the lowest common denominator for increased and deepened cooperation: economic, financial, ideological, technological and in politics and security policy. China and Russia are signalling a desire to deepen their bilateral cooperation, even if the potential for this and its substance are not entirely clear. India is an example of a growing force in international politics that is now balancing between East and West.

The Global South – with the original BRICS countries (Brazil, Russia, India, China and South Africa) at its core – has one common ambition: reducing the dominance of the US, but also of Europe, in international organisations as well as their economic, financial and ideological influence. BRICS has recently expanded. A number of countries are showing interest. Saudi Arabia, the United Arab Emirates, Egypt, Iran and Ethiopia are new BRICS members – a motley collection of countries with a vague agenda and low decision-making power. However, their increased interest in BRICS indicates that countries are now re-examining their strategic relationships and spreading their eggs across more baskets in an

² "Reinvesting in America", McKinsey & Co. 2024

increasingly challenging period when US international commitments can no longer be taken for granted.

The costs of fragmentation

Politician-driven geo-economic fragmentation has a negative impact on the world economy through various channels. Trade restrictions and state aid policies distort competition, leading to reduced economies of scale (poorer resource utilisation and higher costs). Restrictions in such areas as technology transfer, standard-setting and global collaboration worsen the chances of solving the climate crisis and future pandemic outbreaks and controlling the potential downsides of the AI revolution. There is a risk that regulated trade in certain commodities may hamper a transition to the green economy.

Production chains are changing. We are seeing signs of regionalisation and diversification and the creation of parallel structures. Contrary to what many observers expected, however, in some cases we are also seeing increasingly long and complex chains. While there are increasing signs that direct links between the US/EU and China have decreased, they are being replaced by indirect links, i.e. countries that have varying degrees of economic, financial and ideological relations with both blocs. Countries that have benefited from this situation include Vietnam, India and Mexico. The world is moving towards ever-longer global value chains due to the new security order. A study from the Bank for International Settlements confirms that value chains have recently become longer, especially for goods provided by China suppliers and demanded by US customers.

Clear signs of increased fragmentation after 2022

Change in growth rate. Percentage points

	Within blocs	Between blocs	Outside blocs
Trade	-1	-5	-2
Direct investments	-2	-3	+5

Source: "Cold War II", IMF, December 11, 2023, SEB. Based on votes at the UN, a hypothetical "Western bloc" incl. the US, Europe, Canada, Australia, and New Zealand. The "Eastern bloc" incl. China, Russia, Belarus, Mali, Nicaragua and Syria.

Although deglobalisation cannot be confirmed with certainty, fragmentation is becoming increasingly clear. New trade and direct investment data indicate that processes now under way will cause the world to take steps towards competing blocs, with the US and China as their clear "centres of gravity". The International Monetary Fund (IMF) notes that, based on voting at the United Nations, two blocs are crystallising: a "Western bloc" mainly including the US and Europe, and an "Eastern bloc" dominated by China and Russia. The rest of the world has so far not shown a clear pattern as to which bloc it wants to belong to.

A compilation of statistics (see above table) reveals:

- (1) the number of discrete government interventions affecting global trade reached a new record of 228 in 2023, according to data from Global Trade Alert;
- (2) according to the IMF, global trade has fallen since Russia's attack on Ukraine in February 2022, but it has fallen even faster between the Western and Eastern blocs than within each bloc, from a growth rate of 3 per cent before the Ukraine war to minus 2 per cent – a decline of 5 percentage points. The growth rate of intra-bloc trade has fallen from 2.2 to 1.7 per cent;
- (3) growth rate of foreign direct investments has fallen more between than within the blocs. Note that countries outside blocs have seen a clear increase in FDI.

The costs of fragmentation to the global economy can be measured in terms of both short- and long-term effects. The IMF's estimates, which are uncertain,

suggest a global GDP decline of 2.5 to 7 per cent. In the long term, the world economy will suffer from various kinds of efficiency losses that are difficult to translate into concrete figures: fewer economies of scale due to less specialisation and exchange of knowledge, financial fragmentation that raises the global price of capital and makes investments in digital and physical infrastructure and necessary green investments more expensive.

The risk of financial fragmentation has increased due to a freeze on assets of the Russian central bank. This has probably been one reason why China's central bank has continued to reduce its holdings of US Treasury securities. There is a risk that fragmentation will weaken the supply of global investment capital and push real interest rates higher. Restrictions on labour mobility and border closures will also have a negative impact on the potential for desired knowledge transfer, innovation and help in solving countries' growing demographic problems, i.e. declining birthrates and ageing populations.

Today we are in the midst of change, and the picture is not clear-cut. We do not yet know how all these trends will affect the overall situation. Although we are still seeing examples of international cooperation and continued globalisation, it is equally clear that the role of the market economy as a force for change is being subordinated to other interests, that national industrial policy efforts in contravention of WTO rules are increasing and that the fragmentation of the global economy is thus growing. In the long run, this may lead to higher costs and inflation. Companies and financial institutions increasingly need to monitor developments and, in some cases, take steps to prepare for important changes in their operating environments over the next few years.

The United States

Soft landing will lead to Fed rate cut in May

The economy and labour market have remained resilient, while inflation and wage growth have slowed. This reinforces our belief that a soft landing will enable the Fed to cut its key rate in May without the US having entered a recession. Delayed effects of high interest rates and fading support from pandemic savings buffers will result in slower growth during the first half of 2024, followed by a gradual recovery in the second half. The presidential election is an uncertainty factor for 2025.

We expect growth to have slowed in Q4 2023 (to be published on January 25). For the full year, we predict a 2.4 per cent increase – slightly above our November forecast. We foresee a further slowdown during the first half of 2024, followed by acceleration in the second half and a return to trend growth in the course of 2025. We have adjusted our GDP forecast for 2024 upward from 1.1 per cent to 1.6 per cent, leaving it unchanged at 1.8 per cent for 2025. As before, we believe that the US will avoid a recession with falling GDP. Historically, such a soft landing has been hard to achieve. We see reasons for optimism, although some risks remain.

Key data

Year-on-year percentage change

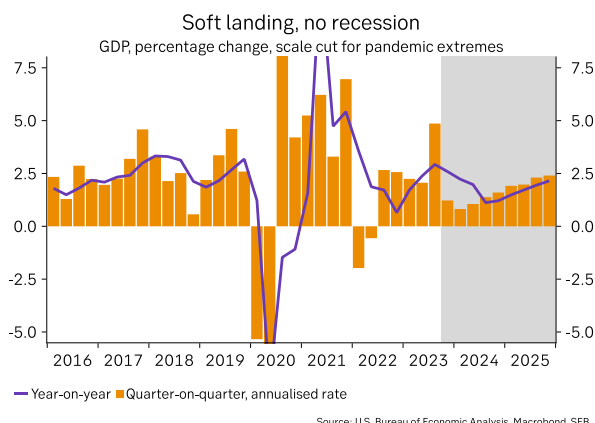
	2022	2023	2024	2025
GDP	1.9	2.4	1.6	1.8
Unemployment*	3.6	3.6	3.9	4.0
Wages and salaries	5.3	4.3	3.8	3.1
Core PCE (Fed target metric)	5.2	4.1	2.1	2.0
Public sector balance**	-3.7	-8.2	-8.0	-8.0
Public sector debt**	121	123	127	132
Fed funds rate, % ***	4.50	5.50	4.00	3.00

*% of labour force **% of GDP, ***upper end of Fed's range.

Source: Macrobond, SEB

A rapid decline in inflation is easing pressure on the Fed.

Inflation has fallen, even though the economy has stayed strong, reinforcing our belief that inflation can be brought under control without a major rise in unemployment.



Source: U.S. Bureau of Economic Analysis, Macrobond, SEB

The Fed's favourite inflation metric is the deflator for private consumption expenditures excluding food and energy, or core PCE. For the past six months, core PCE has been below the Fed's 2 per cent target. This supports our thesis that inflationary forces will subside as the economy moves from an overheated to a more normal situation. Strong productivity growth and favourable supply-side effects have helped. We expect improved real incomes as inflation falls, as well as lower interest rates, to provide new tailwinds for consumption and capital spending in late 2024 and during 2025, offsetting reduced support from the labour market. Higher global demand suggests a gradual recovery in exports.

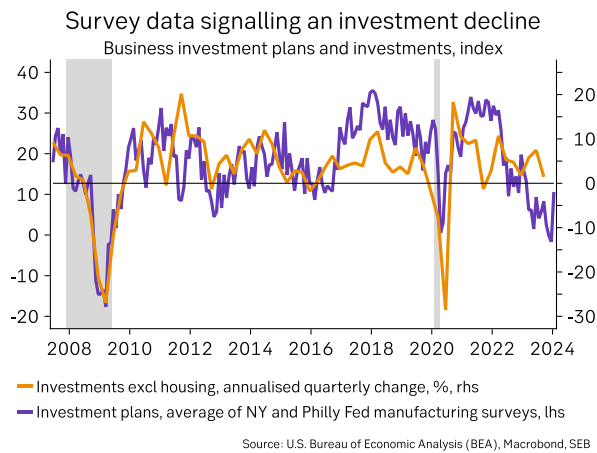
Long, uncertain lags after Fed rate hikes

Delayed effects from the Fed's key rate hikes are the main downside risk to the US economy. Rate hiking cycles tend to expose tensions in the financial sector. Last spring's crisis among medium-sized regional banks was stopped by the Fed, but it is too early to predict no new rounds of bank stress. Hybrid work, vacant office space and large loan maturities in 2024 have raised concerns about commercial property lending, but the fact that the Fed is ready to start cutting interest rates reduces the risk of credit problems. Strong household and business balance sheets will also contribute to resilience. Since the Fed's rate hikes began, credit conditions in the banking sector have tightened in a way that has historically coincided with recessions, but the pace of tightening has slowed and lending is rising again.

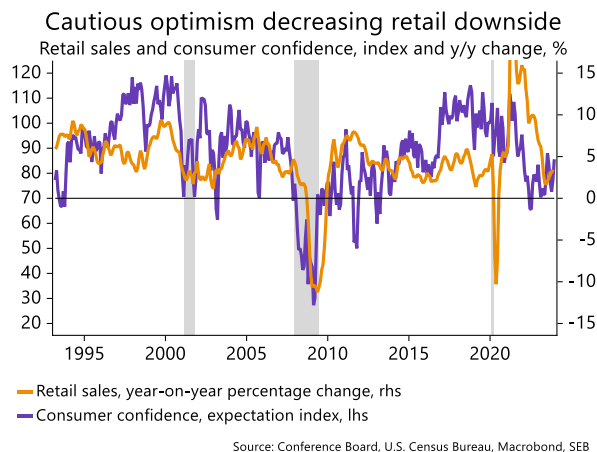
Short-term downside risk to business investments.

We have probably not yet seen the full impact of Fed rate hikes on demand. According to the Fed's indicator for financial conditions, previous tightening will have a negative GDP effect of about 1 percentage point for the coming year. Investment plans in regional manufacturing sector surveys fell last year, indicating a risk of a further downturn in the near term. High interest rates are also slowing publicly subsidised investments in

the green transition. But housing investments rebounded in Q3 2023, after two years of steady decline, and recent mortgage rate declines suggest that the housing market is close to bottoming out.



Business indicators are signalling slower growth but not recession. The ISM index has stabilised at levels consistent with falling industrial activity, weakening markedly in the service sector in December. Consumer confidence has rebounded.



Resilient but not completely immune households.

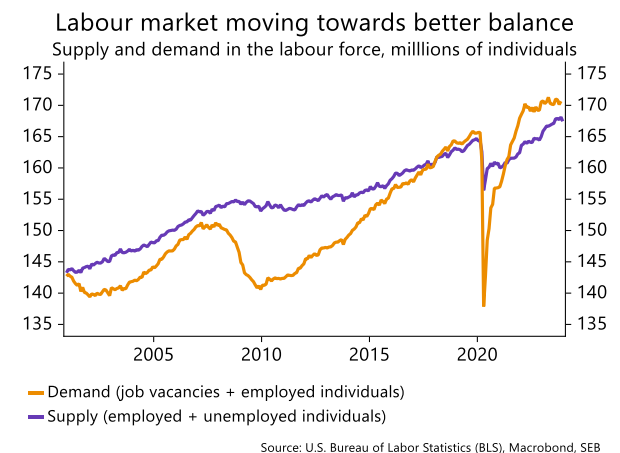
Long fixed interest mortgage periods have mitigated the impact of Fed rate hikes. In addition, about a third of loans were refinanced during the pandemic at interest rates as low as 2.5-3.0 percent for 30 years. However, interest-sensitive consumption such as cars and appliances has come under pressure. Support from the large savings buffers dating back to the pandemic is expected to fade. Estimates of how much of these reserves remain and how they are allocated among households are uncertain. Deposits in savings accounts, the most liquid reserves, are back at their pre-pandemic level and more households have had problems servicing their loans. This may indicate that buffers have been concentrated in the hands of more affluent households that probably have a lower propensity to consume. We

predict that private consumption growth will slow from 2.2 per cent last year to 1.8 per cent in 2024 and 1.7 per cent in 2025 – well below the pre-pandemic average of 2.5-3.0 per cent.

Mixed signals from the labour market

The dynamics of the labour market are another risk. Over the past 3 months, non-farm employment has increased by an average of 165,000 jobs per month, slightly below the pace before the pandemic, when the labour market was strong but not overheated. However, non-cyclical sectors such as health, education and the public sector account for a growing share of employment, while demand in other sectors has slowed. Businesses are also gradually reducing their number of temporary workers, which is usually a harbinger of a weaker labour market. More pessimistic assessments among households in consumer surveys point in the same direction. Hiring plans among small businesses suggest a continued slowdown in the short term, but at a still modest pace.

Moderate upturn in unemployment. The pattern from previous economic cycles is that a 0.5 point increase in the jobless rate triggers a negative spiral in the labour market and the economy. We expect unemployment to peak at around 4 per cent, in line with the Fed's view of long-term equilibrium unemployment but close to historical threshold changes ahead of a recession.

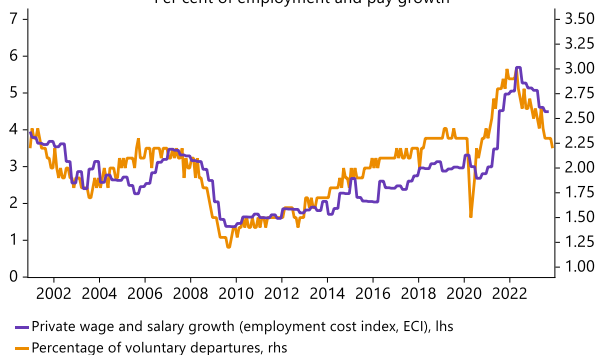


However, last year's unemployment uptick was entirely explained by an unusually strong increase in the labour supply. This reflected higher labour force participation, but above all rapid population growth due to immigration. The participation rate fell in December after being unchanged for 4 months, and we now believe that it will level off as demand weakens. Immigration is an uncertainty factor, but there is considerable political pressure for tighter rules. Our forecast is that the labour supply will grow at a more

normal rate over the next couple of years, while employment growth will slow.

More balanced labour market will ease wage pressures. Demand for labour remains strong, based on vacancies and advertisements, but is approaching more normal levels. Together with rising supply, this has been enough to slow pay increases. Wages and salaries are still rising faster than before the pandemic, but we expect them to slow to a pace compatible with the inflation target as the labour market continues to normalise. Our assessment is supported by the decline in voluntary “quits” and lower premiums for people who change jobs, two metrics that tend to correlate with wage trends. However, indicators such as planned wage and salary changes among small businesses are signalling some short-term upside risks.

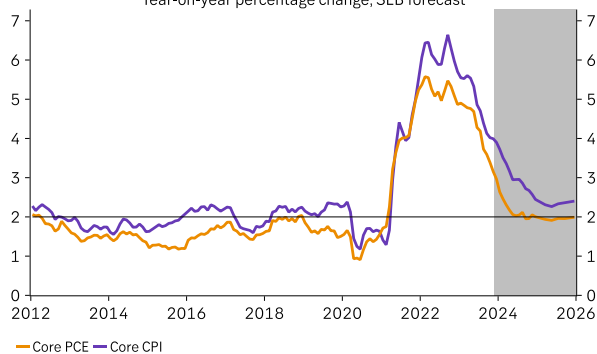
Voluntary departures indicate lower wage pressure
Per cent of employment and pay growth



Source: U.S. Bureau of Labor Statistics (BLS), Macrobond, SEB

Core PCE inflation on target this year. We have only made small changes to our inflation forecast since *NO Update* in November. Last year’s decline was driven by falling energy prices as well as normalised value chains and renewed price pressure on goods, including used cars. Rents are now the main upside driver and have risen faster in recent months, but new leases continue to indicate further rent inflation decline in the CPI going forward. Prices for other services are still rising faster than before the pandemic, but the upturn should slow as pay increases continue to decelerate. Our forecast is that core CPI inflation will level off slightly above target in 2025 and that core PCE will be back at 2 per cent this spring. Like geopolitics, the fact that core inflation has fallen rapidly in relation to various indicators poses an upside risk.

Fed’s favourite inflation metric back at target this spring
Year-on-year percentage change, SEB forecast



Source: Macrobond, SEB

The Fed has signalled that interest rates will remain restrictive until it receives convincing evidence that inflation is persistently approaching its target, but that lower inflation may also justify cuts aimed at avoiding monetary tightening via rising real interest rates. CPI inflation accelerated slightly on a monthly basis but the key drivers, such as rents, have lower weights in the PCE measure. We expect FOMC members to lower their interest rate forecasts further at their March meeting, followed by an initial rate cut in May. We expect the federal funds rate to be in the 3.75-4.00 per cent range by year-end and close to a normal level of 2.75-3.00 per cent by the end of 2025. Estimates of a neutral key rate after the pandemic are uncertain, but Fed policymakers’ median estimate remains at 2.50 per cent. The Fed is continuing to shrink its balance sheet, since not all maturing bonds are being reinvested. This drawdown, currently at 95 bn USD per month, will be determined by the level of reserves in the banking system, and according to the Fed’s plan it may continue even after interest rate cuts have begun. We believe that the Fed decide to taper the pace before summer and end the drawdown early in 2025.

Somewhat tighter fiscal policy. Congressional leaders and the White House have agreed on a 2024 budget framework, but it has not been permanently accepted by Congress. The budget includes limited cuts compared to 2023 and our forecast is a broadly neutral fiscal policy stance in 2025. The national debt has risen to new record levels as a percentage of GDP, but there is no obvious solution to fundamental problems (high and growing social security spending, insufficient tax revenues after repeated tax cuts and rising interest costs on debt). The November presidential election will establish the framework for financial, trade, security and climate policies after 2024. Donald Trump now appears to have taken the lead, but the outcome remains uncertain. Read more in the theme article on page 25.

Theme:

A fateful US election

Potential risks to international trade and security

The November 5 presidential election looks set to be another close contest between seniors Joe Biden, 81, and Donald Trump, 77. The election may have momentous consequences for both the United States and the rest of the world. A new Trump term of office might lead to a radical reshaping of the federal government, the start of another trade war and greater uncertainty about global security policy. If he wins a second term, Biden will probably have less opportunity to have a major political impact. This article discusses events ahead of the election and what we can expect from the two main candidates.

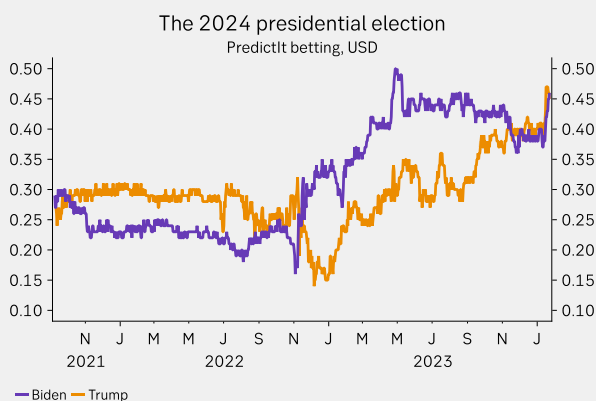
Trump won big in the Iowa caucuses and now has an almost unassailable lead over his competitors in opinion polls of 66 per cent vs about 12 per cent for Nikki Haley. Ron DeSantis has now dropped out of the race and endorsed Trump. Haley has pinned her hopes on the January 23 New Hampshire primary. If she doesn't do better there, the Republican race may be over. Trump also narrowly leads Biden, according to several opinion polls since late 2023. According to the political betting website PredictIt, the race remains tight.

Trump has been indicted in four different criminal cases, but these are unlikely to have any impact on the primaries. A trial related to Trump's role in the January 6, 2021 storming of the US Capitol will begin on March 4 at the earliest, the day before Super Tuesday, March 5, when more than a third of Republican convention delegates will be selected. Of the other three cases, the two most important ones – those linked to Trump's handling of classified documents taken from the White House and his attempted election interference in Georgia – will begin in May and August at the earliest. The indictments appear to have helped Trump in the polls, but this could change. Two-thirds of his Republican supporters say they would vote for him even if he is convicted of a crime, but defections could still be large enough to hurt his chances of winning.



Two states, Colorado and Maine, have barred Trump from running, citing the 14th Amendment of the Constitution, which was approved soon after the Civil War and prohibits insurrectionists from holding public office. The matter is now before the US Supreme Court. Most observers believe that the justices would rather let the voters decide than have Trump excluded.

Ultimately, the election will be decided by the candidates' ability to mobilise core voters and attract centrist voters in a few "swing" states. Third-party candidates are a wild card, since they may possibly siphon away votes in these key states. This is considered a greater risk for Biden than Trump. Regardless of the outcome, the US will remain divided; the last president to win more than 60 per cent of the popular vote was Richard Nixon in the 1970s. Given the structure of the Electoral College system, not even 50 per cent is needed.



Trump's candidacy is unique and controversial, given all the legal proceedings against him and accusations that he tried to change the outcome of the 2020 election. Trump's plans for a radical transformation of what his supporters regard as a corrupt federal government are described by his opponents as a threat to the competence and independence of the civil service, or even as the first steps towards a dictatorship. At the end of his 2017-2021 term as president, Trump unveiled "Schedule F". This implied that tens of thousands of government jobs would be reclassified, making it possible to replace civil servants with people loyal to Trump. Conservative organisations, led by the Heritage Foundation, have developed an agenda for a new Republican term of office, Project 2025. According to Project 2025, the president's power over the federal government would be strengthened by sharply cutting or shutting down various departments and agencies. The project includes a detailed plan for the first 180 days and recruitment of staff for a new administration. Project 2025 is not officially connected

to Trump, but several of those involved have close ties to his campaign.

Trump's first term was marked by chaos. He will probably be better prepared ahead of a second term, both in terms of personnel and plans. Trump's success in appointing a new conservative majority on the Supreme Court and appointing many lower-level federal judges may also make things easier for him, even if these judges cannot always be expected to rule in his favour. However, Trump's (and Biden's) ability to gain congressional approval of his policies would be curtailed by the requirement of a qualified majority (60 per cent) in the Senate on many issues that cannot be directly linked to the budget, where a simple majority is sufficient. However, a US president has a greater degree of freedom in foreign policy.

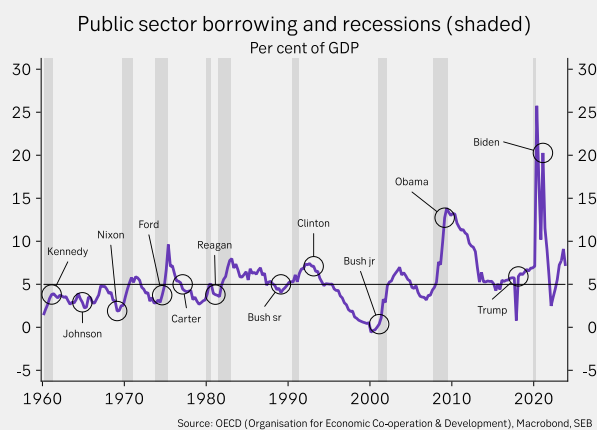
It is uncertain how financial markets will react if Trump is re-elected. The markets find it hard to price in long-term political risks. Tax cuts and deregulation during Trump's first term elicited positive reactions in the stock market, but it is not obvious that this would be repeated in the current environment of lingering inflation risks and growing concern about the unsustainably large US budget deficit. Trump's trade and security policy plans would probably have a major international impact.

A new trade war seems likely. Trump has revealed plans to impose general import tariffs of 10 per cent. Other countries would probably respond to this with their own restrictions, creating the risk of an escalating global trade war. New frictions with China can also be expected. Trump plans to phase out imports from China of essential electronics, steel and pharmaceuticals within a four-year period, while also banning Chinese companies from owning US energy and technology infrastructure. Evaluations of the tariffs imposed during Trump's first term indicate that the gains made by directly affected sectors, such as the steel industry, were more than offset by higher costs for import-heavy downstream operations. But Biden's policies also include protectionist features. Biden has retained tariffs against China imposed by Trump, and his Inflation Reduction Act (IRA) has posed new challenges in trade relations with the EU (see *Nordic Outlook*, August 2023).

As in 2016, reduced immigration is high on Trump's list, including restrictions on both asylum seekers and migrant workers. From an economic perspective, stricter rules for migrant workers may become an obstacle to economic growth by making it harder to find skilled labour. They may also cause problems for the Fed, as long as demand for labour has not slowed. Rapid

population growth due to higher immigration contributed to a less overheated labour market last year. However, Biden is also under pressure to manage the flow of migrants across the border with Mexico.

The need for tighter fiscal policy is a core issue for Republicans. But historically, federal deficits have risen under Republican presidents. In some cases, this is because their terms of office have coincided with economic crises, but other reasons include expensive wars and tax cuts. While in opposition, Republicans have blocked expansion of spending under Democratic presidents, while Democrats have not focused on limiting spending under Republican presidents. Threats to long-term fiscal sustainability come mainly from rising interest costs on the large and growing national debt as well as from runaway Social Security and Medicare spending. So far, Congress has proved incapable of reaching agreement on reforming the federal pension and health care system, and we do not expect this to change in the next term. New tax cuts would further exacerbate the situation. During his first term, Trump implemented large tax cuts for both corporations and individuals. Some of these will expire after 2025, but they are likely to be extended. However, new tax cuts may be financed by higher tariffs. Biden has promised not to raise taxes on incomes below USD 400,000, which means that the revenue - side is not expected to look much better under Biden either.



Can the Fed be affected? Fed Chair Jerome Powell was severely pressured by President Trump to cut interest rates. Powell's term as Fed Chair expires in 2026. Like Janet Yellen before him, he runs the risk of being replaced. However, Trump's ability to bring about a radical reshaping of Fed policy would be limited by the fact that the terms of five of the other six members of the Fed's Board of Governors will run beyond 2030.

A U-turn on the climate issue. Trump is expected to roll back Biden's climate regulations and green subsidies

under the IRA. But climate policy, like many other issues, is largely decided at the state level. In many cases, climate investments initiated with the support of Biden's IRA climate package have gone to Republican states and private ventures. A reluctance to harm local businesses and jobs reduces the likelihood that investments that have already begun will be stopped.

Risk of international consequences. In many ways, a victory for Trump could have even bigger consequences for the rest of the world than for the US. Given its heavier dependence on foreign trade, Europe would be hit harder by a trade war than the relatively closed US economy. In the field of security policy, Trump wants to see a reassessment of NATO and is critical toward support for Ukraine. However, according to a new law, Trump does not have the right to decide by himself whether the US should leave NATO. Trump is also expected to decide to withdraw again from the Paris Agreement.

A second Biden term is expected to be less radical. In the Senate, more Democrats than Republicans are up for re-election. Forecasts indicate that the Democrats will lose their majority. Biden would thus be forced to negotiate with a fully or partially Republican-controlled Congress, with little chance of getting his economic policies through. Biden's campaign slogan is "finish the job". During his first two years as president, Biden implemented much of the economic policy he campaigned on in 2020: a large stimulus package and three reform packages covering infrastructure, semiconductors and climate investments. But voters are not satisfied. According to polls, about half of voters associate Bidenomics with higher inflation and/or tax increases. The stock market, which Trump viewed as his main measure of success, has performed better under Biden, but that has not helped Biden's poll numbers. Nor has last year's combination of falling inflation and a continued strong labour market. It is possible that voters are paying more attention to high prices and the fact that inflation soared during Biden's presidency, partly due to his own stimulus policies. Aside from Biden's age, another stumbling block in opinion polls is that Democrats are divided on support for Israel.

The right to abortion is one issue where Republicans are out of step with much of the electorate. This has led to unexpected victories for Democrats in Republican states. However, it is unclear to what extent Biden can capitalise on this. State-level successes on the abortion issue have also relied on support from Republican women, who may not be prepared to vote for Biden in the presidential election.

Japan

Wage growth will determine Bank of Japan exit policy

GDP growth in 2024 and 2025 will be sustained primarily by domestic demand, partly offsetting anaemic global activity. This spring’s pay increases will determine both GDP growth and the Bank of Japan’s timing in abandoning negative interest rates. We expect the BoJ to hike its key rate this spring, but monetary policy will remain clearly expansionary throughout our forecast period.

Faster price increases and global uncertainty slowed household consumption and investment activity in the second half of 2023. The government’s new stimulus package, approved in November and totalling 2.8 per cent of GDP, will soften the impact of these trends and support purchasing power and growth. The package includes subsidies for businesses aimed at speeding the transition to a more secure, green and digital economy. Households with small financial margins will receive cash, income/real estate taxes will be temporarily reduced, and energy subsidies are extended until spring.

Developments last autumn show that the recovery is fragile and that downside risks dominate. The security situation will require a big increase in defence spending over the next few years, accelerating economic growth. We believe GDP will increase by 1.2 per cent both this year and next, just above trend growth, which we estimate at 0.5-1.0 per cent. Demographic headwinds – a rapidly ageing population – are a brake on growth.

Key data

Year-on-year percentage change

	2022	2023	2024	2025
GDP	1.0	1.7	1.2	1.2
Unemployment*	2.5	2.6	2.5	2.4
CPI	2.5	3.2	2.1	1.3
Public sector balance**	-6.8	-5.6	-3.7	-2.6
Public sector debt**	260	255	252	251
Key interest rate, %***	-0.10	-0.10	0.10	0.10

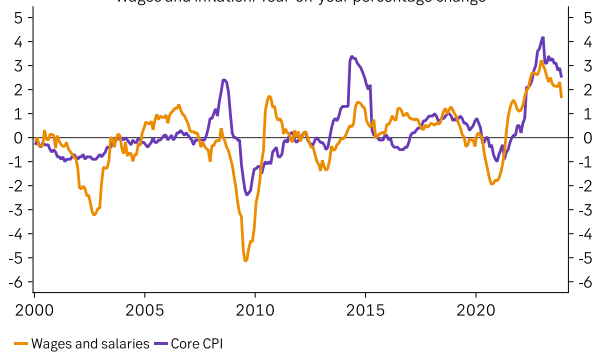
*% of labour force **% of GDP ***at year-end. Source: IMF, SEB

Businesses have maintained their earnings level, helped by falling commodity prices and the yen’s 22 per cent depreciation in 2022-2023 against a basket of currencies. This is expected to continue stimulating companies to allow both higher wage growth (see below) and to boost their capital spending. Reshoring of business operations to reduce vulnerability in global value chains as well as increased automation to address Japan’s severe labour shortage will boost capital spending, while corporate investments in digitisation are expected to boost productivity.

We expect the labour market to remain very tight.

This situation will be driven by a gradual increase in service consumption, which is benefiting from normalisation after COVID-related restrictions, and by a weak yen that is stimulating domestic tourism. Meanwhile the labour supply is shrinking due to an ageing population. There is a broad consensus in the economy – including among companies – on the need for higher pay increases. Wage and salary growth peaked early in 2023 at 3.2 per cent but has since slowed. The union benchmark for this spring’s wage agreement is “5 per cent or more”. We believe wage growth may reach around 3 per cent, which will increase inflationary pressure somewhat.

Spring wage negotiations will determine monetary policy
Wages and inflation. Year-on-year percentage change



Source: Macrobond, SEB

The BoJ’s shift in monetary policy is taking place in ultra-small steps. This is welcomed by the world’s asset markets, which have benefited greatly from cheap yen financing for many years. Last autumn, the BoJ took new steps to make its yield curve control (YCC) more flexible – with successful results and without large long-term interest rate movements. We expect the BoJ to abandon negative interest rates this spring, but its monetary policy will remain expansionary. Policy formulation and a strengthening of the yen will be facilitated by the fact that other central banks are expected to cut their key rates in 2024 and 2025. Our forecast is that the USD/JPY rate will be 132 at the end of 2024 and 127 at the end of 2025.

China

Slow growth despite first quarter fiscal boost

Absent a significant growth catalyst, China will see continued anaemic growth during our forecast period, despite a fiscal boost at the beginning of 2024. This weakness is primarily due to continuing trouble in the real estate sector and poor private sector confidence that is limiting household spending. We expect GDP growth of 4.6 per cent this year and 4.4 per cent in 2025.

Base effects boosted otherwise lacklustre GDP growth in 2023. Despite a relatively high growth rate in 2023, underlying growth – parsing out base effects – has hovered closer to 3.5 per cent. A moderate pick-up in economic activity after the first quarter of 2023 following the end of COVID restrictions largely fizzled out as spending and investment from household and private businesses remained low. The real estate crisis and debt defaults by property developers put pressure on the financial system, and the government rolled out a plethora of monetary and housing-support measures which may have staved off a more rapid deterioration but have done little to raise the growth outlook materially.

Key data

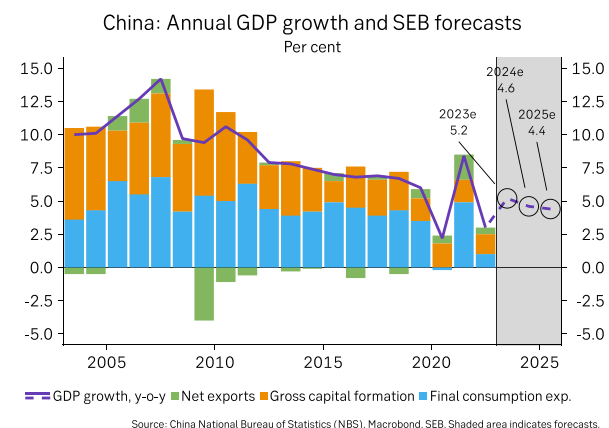
Year-on-year percentage change

	2022	2023	2024	2025
GDP	3.0	5.2	4.6	4.4
CPI	1.8	0.4	1.3	1.9
Fiscal balance	-4.7	-4.9	-4.7	-5.0
1-year loan prime rate, %**	3.80	3.45	3.45	3.45
7d reverse repo rate, %**	1.80	1.7	1.7	1.7
USD/CNY**	6.36	7.1	6.8	6.5

*% of GDP **At year-end. Source: IMF, SEB

Growth catalysts largely absent as private sector confidence remains subdued. Fiscal and monetary policy appears unlikely to boost growth, unless there is a pick-up in private sector activity. Poor job security as well as limited wage growth amid a housing-related hit to savings should continue to dampen sentiment, ultimately holding back consumption within our forecast

horizon. Meanwhile, a global downturn and ongoing trade conflicts with both the US and EU will cap demand for Chinese goods and limit export contributions to GDP.



Fiscal policy to provide some support. To the extent that the reopening surge following the end of COVID restrictions has largely passed, the service sector is also unlikely to boost growth much. To some degree, fiscal policy will provide accommodation early this year. This includes an increase in the general budget deficit in October, with an extra 1 trillion yuan in sovereign bond issuance, which should cushion local government financing of infrastructure spending. We expect the government's budget deficit to moderate somewhat.

Policy to preserve stability rather than to achieve high growth. Future policy decisions will be critical to the economic outlook and pose upside and downside risks in our growth forecasts. On one hand, policymakers have demonstrated a willingness to boost aggregate demand to avoid Japan's experience in the 1990s, when simultaneous contractions in public and private demand led to a deflationary spiral. Yet, as we have argued previously, China's fiscal space is relatively limited and higher GDP growth than our forecast entails would require a revival of activity among consumers and private businesses. Deflation in CPI prices returned late in 2023, but core inflation also remains muted. The steps required to lift confidence along these lines would require more widespread reforms – an unlikely outcome during our forecast period. Meanwhile, foreign outflows from China should continue amid regulatory concerns, low domestic demand and geopolitical risks. Among the latter, we count a possible increase in tensions around the Taiwan Strait as well as broader Sino-US rivalry as key risks in 2024. We therefore expect GDP growth in 2024 to reach 4.6 per cent and 4.4 per cent in 2025. In addition, we expect the People's Bank of China (PBoC) to keep rates on hold during our forecast period and for the CNY to strengthen to 6.8 per USD by the end of this year.

Emerging markets

The rate-cutting cycle has begun

Emerging market (EM) growth will be hurt by China’s ailments but helped by geopolitical winners such as India and Mexico. Rate-cutting is well underway despite idiosyncratic swings in Russia and Turkey. A disinflationary process will open the way for further cuts in 2024, easing monetary conditions, but geopolitics and lingering inflationary pressures may prolong this process. Geopolitical risks from Ukraine to the Middle East to Taiwan will remain significant during our forecast period.

Disinflationary pressures paving the way for further rate cuts this year. Overall GDP growth in EM countries was slightly higher in 2023 than the year before, largely driven by lacklustre performance in China (see p. 29), but also by downturns in many other countries. Disinflationary pressures paved the way for central banks to either start cutting key interest rates or at least tilt forward guidance toward rate cuts in the near future. Excluding large idiosyncratic rate swings in countries like Russia and Turkey, EM central banks will remain ahead of advanced economies in the rate cycle. For the moment, GDP growth continues to look relatively modest, and all our covered EM countries except Brazil and Turkey have yet to recover to their pre-pandemic GDP trend levels.

Key data

GDP, year-on-year percentage change

	2022	2023	2024	2025
Emerging markets (aggregate)	3.7	4.3	4.1	4.0
India (fiscal year)	7,2	7,0	6.7	6.3
Brazil	2.9	3.0	1.8	2.0

Source: IMF, SEB

Low growth potential among EM countries, but not all.

Weaker global demand, ongoing geopolitical risks and a slow process of deglobalisation will combine to exert downward pressure on GDP growth during our forecast period. Except for gold and to some extent copper, commodity prices have fallen or remained largely

stable, giving commodity producers a limited boost going forward. In our view, potential GDP growth for most EMs looks set to remain at the historically low levels reached during the pandemic. Yet pockets of optimism exist in Asia and Latin America, as winners in geopolitical rivalries and reshoring processes such as India and Mexico stand out.

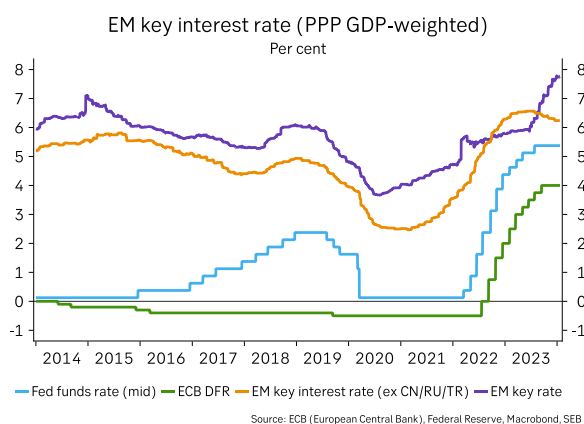
Country	YoY % chg	QoQ % chg	Lvl as % of pre-pand. trend	Lvl as % of pre-pand. level
India	7.5	2.2	-3.6	17.6
Philippines	5.6	3.3	-10.9	8.5
China	5.3	1.0	-2.2	19.9
Indonesia	5.1	1.0	-5.1	11.3
Turkey	4.5	0.3	8.8	23.3
Russia	4.2	0.9	-3.7	3.9
Malaysia	3.3	2.6	-5.2	12.9
Mexico	3.3	1.1	-1.3	5.2
Singapore	2.8	1.7	-1.9	11.4
Brazil	2.5	0.1	1.8	7.2
Thailand	1.5	0.8	-11.8	1.3
Poland	0.6	1.5	-6.4	10.6
Hungary	-0.3	0.9	-10.0	5.0
South Africa	-0.5	-0.2	-3.6	0.7
Czech Republic	-0.8	-0.6	-13.4	-1.6
Ukraine	-0.9	0.7	-33.8	-27.1

Source: National sources, Macrobond, SEB

One of the few clear growth stories so far is India, which looks set to benefit from a range of domestic and external factors allowing high future GDP growth, a disinflation process that will allow the Reserve Bank of India to start cutting rates during the second quarter this year and an amenable geopolitical and investment climate boosting investments and exports. We expect Indian GDP growth to be 6.4 per cent in fiscal 2024 and 6.2 per cent during the following fiscal year. We also believe that the incumbent government will be re-elected this year, which should indicate policy stability, albeit amid ongoing concerns over deteriorating democratic institutions.

Significantly lower inflation in central Europe. In central Europe, the Czech Republic, Hungary, and Poland have all experienced significant downturns. This has alleviated inflationary pressures. Annual inflation is now between 12 to 18 percentage points below peak levels following the Russian invasion of Ukraine. Yet uncertainty over the fiscal policy stance in Poland following the election of a new more pro-EU government, as well as underlying inflationary pressures and wage growth, pose continued risks in the region. We nonetheless see room for further rate cuts in 2024, even though the central bank of Poland could surprise on the hawkish side in the near term. More

lasting political change in Poland will also probably take time, and concerns over coalition stability and entrenched Law and Justice Party influences in political institutions imply that ongoing political risks remain.



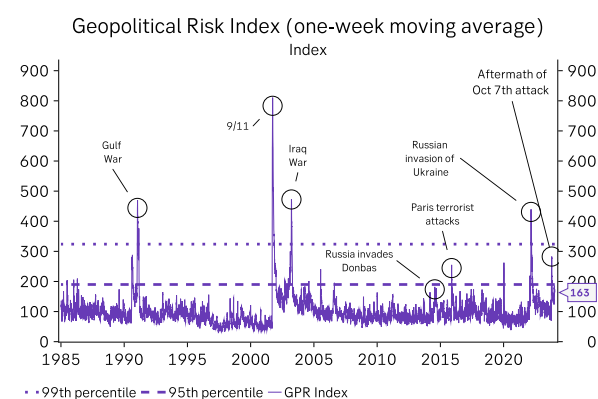
Concerns over durability of Turkish policy stance.

Turkey experienced a large economic policy shift following the June 2023 elections, and a new monetary policy team has raised key rates by 34 percentage points. During the same period, however, deteriorating inflationary expectations largely cannibalised this real policy stance. Even with the key rate at 42.5 per cent, annual inflation is expected to reach 70 per cent in the first quarter of this year. Ongoing concerns over the durability of the policy stance limit investor confidence and largely explain the depreciation of the lira.

Mexico to benefit from reshoring, but there are limited upside risks. In Latin America, hawkish central banks drove up real rates significantly in 2023. With both current inflation and inflation expectations falling durably, Brazil started its rate-cutting cycle last year and Mexico looks set to initiate rate-cutting during the first half of this year. As such, both the Brazilian real and the Mexican peso have lost some of the gains achieved last year. In Mexico, this year's elections are expected to result in the incumbent party candidate coming out on top. Mexico looks set to benefit from global reshoring efforts and geopolitical changes, but nationalist government policies and tight monetary conditions (so far) will limit the upside to GDP growth.

Geopolitical risks remain at the forefront. Several flashpoints pose significant geopolitical risks to our forecasts. The possibility, if not growing likelihood, of a second Donald Trump presidency in the US will have significant effects on EMs, via international politics, conflicts, trade and markets. The Israel-Gaza war has so far had only marginal effects on market outcomes, despite the ongoing humanitarian disaster. Risks of a regional escalation of the conflict appears either to be discounted by oil markets, or at least outweighed by

other factors pointing to ample supply and limited global demand. Attacks on commercial shipping in the Red Sea – and the extent to which these will affect supply chains and costs – as well as concerns over intensified fighting on Israel's northern border with Hezbollah in Lebanon will be ongoing risks in the near term. An escalation is not our baseline, but it is unclear to what extent the observed market pricing fully captures the risks in the region.



In the Russia-Ukraine war, growing concerns over the West's continued financing of Ukraine and supply constraints on military capacity have put increased pressures on the war effort. Russia has largely transformed into a war economy and the Wagner revolt of last year does not seem to have affected Russia's ability to wage war. A Republican US government would likely imply even less support for Ukraine and a possible opening of negotiations with Russia.

Renewed China-Taiwan tensions. With the Taiwan presidential elections over, we expect renewed tensions between China and Taiwan. In our view, the Chinese government's current focus on domestic economic change, as well as ongoing purges within the military, diminish the possibility of a wider conflict in the near-to-medium term. Yet this still leaves multiple avenues for deteriorating relations between the two governments, including Chinese military manoeuvres interfering with Taiwanese trade, as well as broader economic sanctions and related measures.

Wedged between the blocks. EM countries are likely to perceive themselves as wedged between Western countries on one hand and China and to some extent also Russia on the other hand. While we do not expect a large shift out of US dollar assets by EM central banks, we do foresee a continued shift into other assets that are perceived as safer from Western sanctions, especially if the US and the EU move ahead in more substantially using seized Russian government assets to support Ukraine financially.

The euro area

Weak growth and political challenges

GDP is expected to have fallen in the second half of 2023, but growth will speed up in the second half of 2024 and a major slump can thus be avoided. The surprisingly fast decline in inflation last autumn is continuing and is an important piece of the puzzle enabling consumption and capital spending to accelerate in the future. The decline in inflation will persuade the ECB to cut key rates as early as this March.

Growth in the euro area slowed in 2023, and GDP fell marginally in the third quarter. We expect the decline to have continued during Q4. The outlook varies between countries and sectors. Germany has shown especially weak performance due to its anaemic manufacturing sector, while more service-dependent Spain has reported relatively high growth rates and has bounced back from its large decline during the pandemic. But recently, conditions in the service sector have deteriorated. Overall sentiment indicators are weak and point to falling economic activity, though this is not yet fully reflected in hard data.

Key data

Year-on-year percentage change

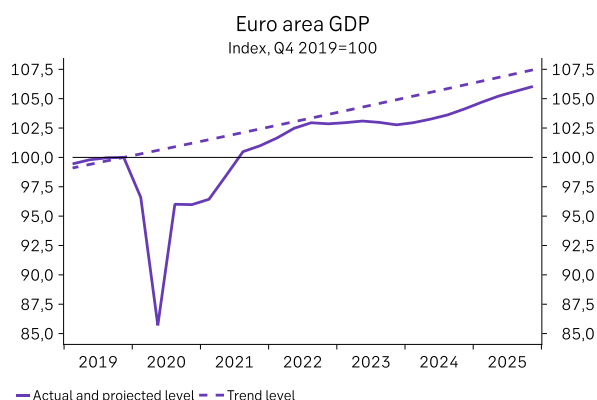
	2022	2023	2024	2025
GDP	3.4	0.5	0.5	1.8
Unemployment*	6.7	6.5	6.8	6.8
Wages and salaries	4.5	5.3	4.3	3.3
CPI	8.4	5.4	1.3	1.2
Public sector balance**	-3.6	-3.1	-2.7	-2.4
Public sector debt**	90.9	89.6	88.5	87.2
Deposit rate, %***	2.00	4.00	3.00	2.00

*% of labour force **% of GDP *** at year-end. Source: Eurostat, SEB

Weak ending to 2023 and technical recession. We believe that the euro area experienced a technical recession in the second half of 2023 (falling GDP for two consecutive quarters; Q4 data will be published on January 30). Full-year GDP will show an increase of only 0.5 per cent, and this slow growth is relatively

broad-based. Due to weak foreign demand, exports are falling. High export prices, driven by energy and other factors, are also contributing to weak export performance. High inflation and interest rates have weakened household purchasing power, but this is partly offset by strong labour markets and high nominal pay hikes. Capital spending is slowing because of the impact of monetary policy on the economy.

Acceleration, but at a moderate pace. Although growth is still weak, headwinds will ease this year. Especially in the second half, we will see a slight acceleration. Somewhat better global demand will benefit exports. Because inflation will continue to fall, we have seen the end of the European Central Bank’s key interest rate hiking cycle. A series of rate cuts will begin as early as March 2024. Combined with nominal pay increases above the historical average, the scope for consumption will once again expand. Increased investments related to the green transition and digitisation will also contribute to GDP growth further ahead. But due to the large decline in real wages that occurred when inflation accelerated, plus the effects of sharp rate hikes in recent years, the recovery will be weak. Meanwhile we expect fiscal policies to tighten in the next couple of years, since most countries have limited manoeuvring room due to already high debt and fiscal policy rules. Starting this year, we believe EU member countries will again have to comply with stricter budget deficits and public sector debt rules (which were paused during the pandemic). Overall, GDP will increase by slightly above 0.5 per cent in both 2023 and 2024 and a bit below 2 per cent in 2025. At the end of our forecast period, GDP will still fall short of trend level.



Source: Eurostat, Macrobond, SEB

Differences between countries. Germany, with its heavy dependence on natural gas, has been hit harder by the effects of Russia’s invasion of Ukraine than other major euro area economies. Energy prices remain high, putting pressure on both households and businesses

(especially energy-intensive ones). Weak international demand – especially slower growth in China – and more structural challenges in the vital automotive industry have further dampened output. Domestic political turmoil and the budget crisis late in 2023 helped create an uncertain investment climate (see the theme article “Germany – a sputtering growth engine” p.35). Such countries as France, Spain and Italy have fared better in terms of growth after the pandemic, although they have also been affected by high inflation and rising interest rates.

GDP forecasts

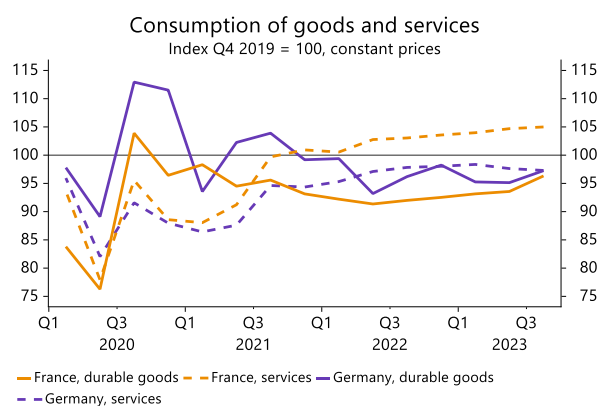
Year-on-year percentage change

	2022	2023	2024	2025
Germany	1.8	-0.3	0.0	1.6
France	2.5	0.8	0.6	1.6
Italy	3.9	0.7	0.5	1.2
Spain	5.8	2.4	1.3	1.8
Euro area	3.4	0.5	0.5	1.8

Source: Eurostat, SEB

Labour markets remain resilient. Despite a sharp slowdown in growth, labour markets have shown high employment growth. This trend is in line with other regions and is not unique to the euro area. A robust service sector and a shortage of skilled workers may partly explain why unemployment has barely climbed. Another possible explanation is that businesses are holding on to employees despite hard times in order not to risk labour shortages when the economy rebounds. Although the economy is clearly slowing, we believe that partly due to the above factors, the jobless rate will rise only moderately during our forecast period before starting to fall again late in 2025. Long-term demographic challenges will increasingly affect labour markets. A larger percentage of older people in the population will limit the labour supply and push unemployment lower.

Consumers will see improvements from a weak position. High inflation and rapid ECB rate hikes have dampened household consumption, which has stagnated. Since Russia's invasion of Ukraine, goods consumption has been especially sluggish, while service consumption has improved due to pent-up demand after the pandemic. Inflation will keep falling in 2024, while pay hikes will be relatively high and unemployment will rise only modestly, which we view as important explanations for accelerating consumption and growth. However, reduced fiscal policy support will partly offset the upturn in consumption.



Source: Eurostat, Macrobond, SEB

Political risks are as important as economic risks. In the short term, the focus of attention is on the continued decline in inflation, the timing of the ECB's first rate cut and how much the economy is slowing or even falling. Later in our forecast horizon, politics and the risks associated with it will become increasingly important – nationally, at EU level and globally. In Germany, domestic political turmoil has increased since the Constitutional Court's ruling before Christmas that parts of the national budget were unconstitutional. This has led to renewed negotiations within the governing coalition and reluctant cuts in the 2024 budget (see the theme article “Germany – a sputtering growth engine”). Ahead of the June 2024 European Parliament election, right-wing populist parties appear to be gaining ground, increasing the risk that it may be hard to form a parliamentary majority. It may also be hard to achieve progress on EU cooperation and enlargement issues if countries such as Hungary continue to veto various proposals. Countries that have been allowed to start talks on joining the EU, such as Ukraine and Moldova, risk a lengthy negotiation process. The outcome of November's US presidential election may have a major impact on EU domestic and foreign policy. An isolationist and protectionist US president may mean both lower exports and higher defence spending for a number of already fiscally strained EU countries.

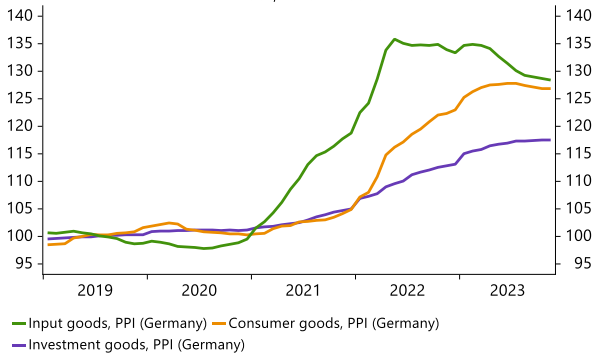
Significantly lower inflation rate

Inflation has fallen since peaking late in 2022, driven by both large base effects and declining energy prices. During the second half of 2023, core inflation – excluding energy, food, alcohol, and tobacco – fell surprisingly fast. This will lead to faster growth and earlier rate cuts. Service prices have increased more slowly than expected, and the gap between service and goods inflation has thus narrowed.

Producer prices are falling, but still to a limited extent for consumer goods. Price trends in different parts of the production process still vary. Producer prices for

input goods have peaked, then clearly decreased. This picture is also consistent with price expectations according to purchasing managers' indices, which are signalling continued declines in input prices, although their downward momentum seems to have slowed recently. The same trend is not yet visible for consumer goods at the producer level, suggesting that price hikes may remain in the system and that the slowdown at final consumer level will be prolonged.

Goods prices: Weaker downturn early in production chain
Index, 2019 = 100



Source: German Federal Statistical Office (Statistisches Bundesamt), Macrobond, SEB

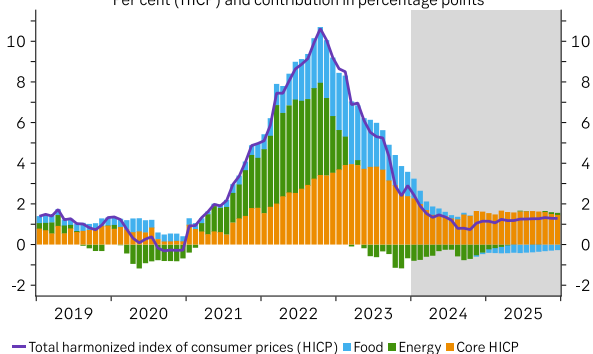
Core inflation will revert to the ECB's target by spring.

While the risks of higher inflation remain substantial, the rapid decline indicates that demand pressures have eased more than expected. Core inflation is now falling faster than we forecast in November, though the decline is still slower than that of headline inflation. As base effects fade, the gap between the two inflation metrics will be narrower. Both headline and core inflation will fall below 2 per cent by early spring.

ahead. We believe that the risk of a wage-price spiral is small, but higher-than-expected pay hikes risk delaying the decline in core inflation.

This spring will begin with interest rate cuts. The decline in inflation over the past several months, especially for core inflation, has had a major impact on financial markets, resulting in lower market interest rates and yields. No further ECB rate hikes are to be expected, and the timing of the initial rate cut has moved ever closer. Despite last autumn's more favourable inflation figures, the ECB will maintain a hawkish tone until it actually cuts interest rates. A continued decline in inflation – especially core inflation – and a determination that already approved pay hikes are not too high are criteria needed for the ECB to begin cutting interest rates. The central bank is approaching a point where it feels comfortable with the decline in inflation in both the short and long term, and our assessment is that key rates will be cut as early as March 2024. The weakness of the economy in the euro area countries is not a decisive factor, but due to generally anaemic demand and weakening labour markets, the ECB's concerns about new inflationary impulses are easing. Overall, the bank will cut interest rates four times by a total of 100 basis points during 2024 and by the same amount in 2025. The deposit rate will thus be 2.0 per cent at the end of our forecast period.

Stubborn core inflation, but rapidly falling HICP
Per cent (HICP) and contribution in percentage points



Source: Macrobond, SEB

Pay increases will be crucial. Price trends in the service sector and a persistently rapid pace of wage and salary growth, together with the risk of a new energy price shock, are the main upside risks to our inflation forecast. In the spring of 2024, many new collective pay agreements will be negotiated. These will be crucial for domestic inflationary pressures further

Theme:

Germany

A sputtering EU growth engine

Germany's growth model is being challenged from several directions. The energy crisis, weak global growth, increased fragmentation, a Chinese slowdown and a weak federal government with a constrained fiscal policy have shaken up this growth model. A weak economy and domestic political turmoil have increased political discontent and support for the xenophobic AfD party ahead of the 2025 elections. Germany needs an effective government that is capable of implementing reforms that will boost growth in the long term. The German economy is also important to Sweden due to large-scale trade between them. More than 10 per cent of Swedish merchandise exports go to Germany, while 17 per cent of Sweden's imported goods originate there.

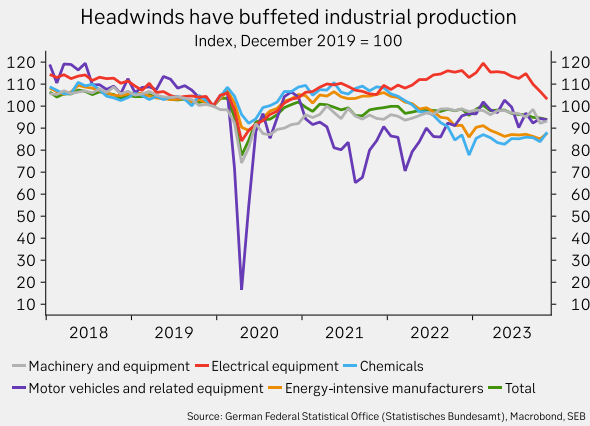
Germany's GDP recovery the weakest of the Big Four.

At the beginning of the COVID-19 pandemic, as well as during the reopening phase in the euro area economies, it looked as if the German economy had managed relatively well. A bit into 2021, Germany began to lag behind the other major euro zone economies. This coincided with Russia's invasion of Ukraine. Its GDP is now around the same level as in the fourth quarter of 2019. Last year was especially tough, with German GDP expected to have shrunk marginally. Household consumption and exports have been the main negative contributors to GDP growth, while overall capital spending has essentially stagnated.



The vital industrial sector is being challenged.

Industry, which is highly important to Germany (accounting for nearly 30 per cent of value added, compared to 17 per cent in France) has been fighting an uphill battle in recent years. Both cyclical and structural factors are behind its anaemic performance. Russia’s invasion of Ukraine has greatly affected energy-intensive companies impacted by high energy prices. Dependence on Russian natural gas had to be reduced, and a necessary energy transition is imminent.

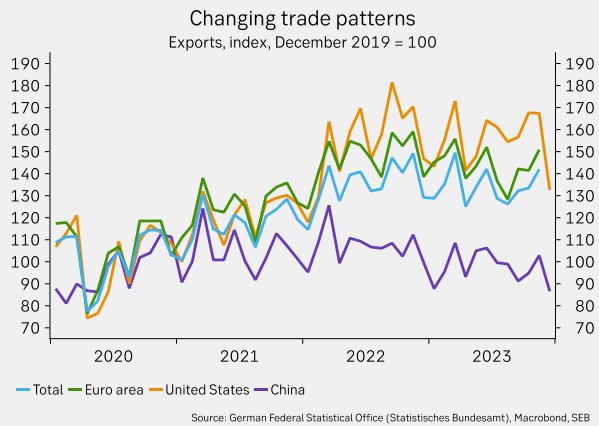


Germany’s large automotive industry is under pressure due to high costs, lower demand and increased competition from China – particularly for electric cars, which are increasingly exported, especially to Europe. Greater geopolitical risks and more protectionism in world trade may also hurt Germany’s automotive industry, which exports a large share of its production and plays a major role in overall exports. Motor vehicles – including cars – account for more than 15 per cent of the country’s exports.

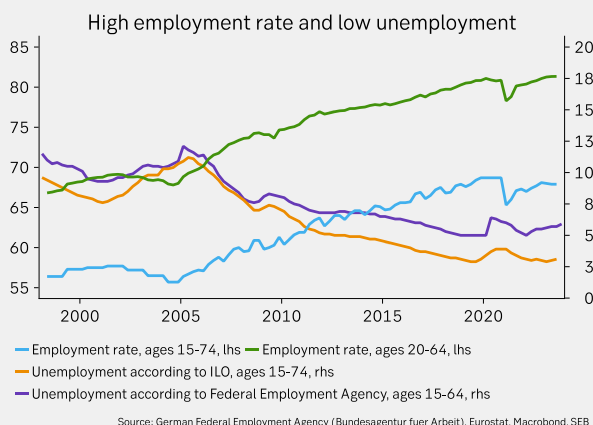


It is hard to be export-dependent when global demand is declining. Lower global demand and higher energy prices have had an unfavourable effect on German exports, which have fallen. In 2022, exports were equivalent to more than 50 per cent of GDP, and since a large proportion of exports consists of vehicles,

machinery, etc., the downturn is hitting industrial production hard. Above all, exports to China are falling. The slowdown in Chinese growth has a major impact on German exports, since China is one of Germany’s main export partners, along with the United States, France and the Netherlands. Over time, exports have shifted from China to other major trading partners such as the US. This may be related to the increased fragmentation of the world economy.



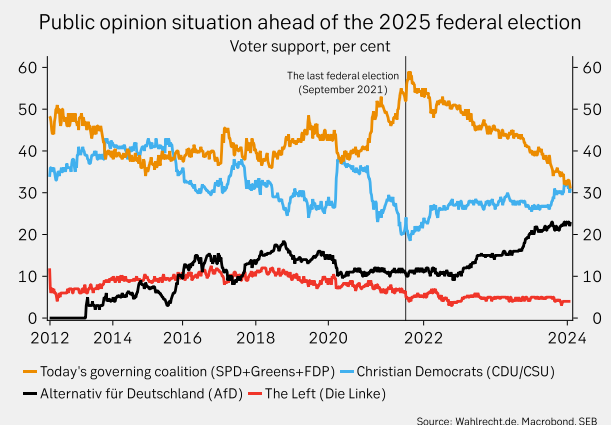
Strong labour market. Despite Germany’s anaemic economic activity, the labour market has been resilient. Unemployment is at low levels, although according to some metrics it has increased somewhat recently due to the weak economy. A shortage of skilled labour, especially in the service sector, is one explanation. Germany faces major demographic challenges. The high proportion of older people in the population will limit its labour supply in the future. To some extent, immigration has alleviated the demographic challenges facing the country, but in the medium term, demography will become a factor that increasingly constrains growth. The employment rate is at historically high levels, although for people aged 15-74 it has not fully recovered from the pandemic. However, in the 20-64 age group, employment has recovered and is even at slightly higher levels than before the pandemic. The increase in the employment rate over time has to do with the Hartz reforms (named after Peter Hartz, who chaired the committee behind the reforms) implemented in Germany’s labour market in the early 2000s with the aim of increasing job-seeking, strengthening incentives for the unemployed to accept work and boosting labour force participation, especially among women and older people.



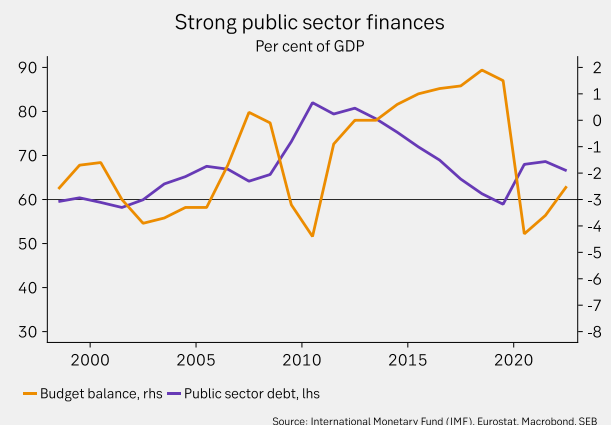
Domestic political turmoil continues. Last year was a challenging period for the German federal government. The “traffic light coalition” (die Ampel-Koalition) of the Social Democrats (SPD), Green Party (die Grüne) and Liberals (FDP) had problems agreeing on both economic issues and legislative proposals such as last spring’s important law on space heating. Under this proposal, newly installed heating systems should predominantly be powered by renewable energy. In the autumn, domestic political turmoil increased further when Germany’s Constitutional Court rejected the financing of the Climate and Transformation Fund (KTF), creating a big hole in the 2024 budget. The government went back to the negotiating table, and just before Christmas an agreement was reached on a tighter budget than previously planned. The debt brake law (limiting the structural budget deficit to no more than 0.35 per cent of GDP) is coming into force again, although there are discussions – especially within the SPD – about changing the regulatory framework to boost capital spending. A weak economy and a divided government coalition have increased popular discontent. This is especially clear from various opinion polls ahead of the 2025 election, showing that the xenophobic Alternative für Deutschland party has surged from 10 to 22 per cent voter support since mid-2022. In state-level elections last year, the AfD performed strongly, including in Hesse where it became the second-largest party and in Bavaria, where it took third place. State elections will continue this year with Saxony, Brandenburg and Thuringia.

Fiscal policy will have an impact on growth. Statistics and various statements from the government indicate that EUR 10-17 billion must be cut from this year’s federal budget. All else being equal, this will mean smaller deficits and a lower borrowing requirement. The debt-to-GDP ratio is now also expected to fall somewhat faster than previously estimated. Germany is the major euro area economy with the strongest public finances, and tighter fiscal policy is likely to increase

pressure on other euro area countries with weaker public finances, such as Italy. The cuts proposed by the German government include a gradual reduction in diesel fuel subsidies for agriculture and forestry, an increase in aviation tax, a reduction in appropriations for various ministries and stricter rules on “basic income” grants. We estimate that budget cuts will reduce GDP growth by 0.3–0.5 percentage points.



Some light at the end of the tunnel. Although 2024 appears likely to be another challenging zero-growth year, GDP will again start rising – especially during the second half. Private consumption is recovering on the back of a notable rise in real incomes. The labour market is robust, nominal wage growth is high and inflation is falling. Households also have large savings that can support consumption. International demand is picking up again, which is boosting exports. Lower interest rates will make it easier for capital spending to increase again. There are thus good reasons to expect faster growth ahead, although it may be limited by long-term challenges in the manufacturing sector and structural factors such as demographics. An energetic and – above all – cohesive government is required to deal with these issues, and the current government has found it difficult to demonstrate such qualities. The 2025 election will therefore be important for Germany’s long-term growth.



The United Kingdom

Stagnating growth

High inflation and rising interest rates have begun to have a clear impact on the UK economy. Household demand is subdued, and even if purchasing power improves ahead, growth looks set to be very low in 2024. Inflation is finally falling, but underlying inflationary pressures are being sustained by a continued tight labour market and high wage growth. The Bank of England will thus not begin its interest rate cutting cycle until summer.

The UK economy proved surprisingly resilient during the first half of 2023, despite persistent headwinds. But the strong labour market that has supported consumption has begun to cool, and unemployment will likely rise over the next couple of years. The savings buffers that households built up during the pandemic are starting to thin out after a few years of rising living costs.

Key data

Year-on-year percentage change

	2022	2023	2024	2025
GDP	4.3	0.5	0.2	1.4
Unemployment*	3.7	4.1	4.6	4.7
Wages and salaries	6.0	7.0	3.5	3.5
CPI	9.1	7.3	2.7	1.9
Public sector balance**	-5.5	-4.5	-3.9	-3.7
Public sector debt**	102	104	106	107
Key interest rate, %***	3.50	5.25	4.00	2.75

*% of labour force **% of GDP ***at year-end. Source: IMF, ONS, SEB

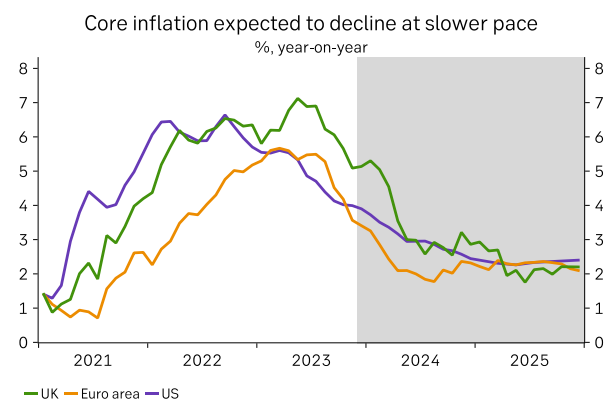
Acceleration, but at a moderate pace. A long period of high inflation and high interest rates continues to be a drag on the economy. Several indicators point to very subdued production around the turn of the year and during the coming quarters. In addition, various long-term challenges remain – weak productivity, stagnant investments and declining labour market participation rates. But during the second half of 2024, the economy will begin to recover. Purchasing power is slowly starting to improve for households, even though unemployment is rising, and lower inflation means that

the Bank of England (BoE) can finally start cutting its key interest rate. In addition, international demand is increasing, yet growth will be subdued this year as well. In 2025, however, both inflation and interest rates will have fallen further, and GDP growth will accelerate.

Tight labour market starting to cool off. As a result of declining growth, we expect unemployment to continue rising slowly during our forecast period. At the same time the labour supply will continue to shrink, and strikes demanding higher wages are expected to continue. The labour market situation thus remains strained in the wake of Brexit and the pandemic.

Limited fiscal support. With already high public debt and high interest costs, there is limited scope for much-needed fiscal stimulus. The budget deficit is expected to have reached 4.5 per cent of GDP in 2023 but will fall to 3.9 per cent in 2024. This year, the UK will also go to the polls, probably during the second half according to Prime Minister Rishi Sunak. The political situation is fragmented and there is no credible majority in Parliament, further limiting the impact of fiscal policy.

Core inflation is falling more slowly than in other countries. Although we expect inflation to keep falling in the coming months, underlying inflation will be sustained by continued rapid pay growth. During the year, inflation will fall sharply, but it will remain at 2.7 per cent at the end of 2024.



A tough balancing act for the Bank of England. With declining growth and falling inflation on one side of the scale, and with continued high pay increases and a tight labour market on the other, the BoE faces a tough balancing act. The risk of a wage-driven inflation surge remains significant, which means that we believe that the BoE will wait a bit longer before cutting interest rates than the Fed and ECB, for example. But a series of rapid cuts will begin in June, and the key rate will be at 2.75 per cent by the end of 2025.

The Nordics

Sweden | page 40

Lower inflation and falling interest rates will greatly reduce downside risks and suggest that the recovery will be stronger, but a continued downturn in housing construction and a weaker labour market will work in the opposite direction.

Denmark | page 46

Home prices will continue to hold back residential investments for another while, but consumption and housing indicators are improving. Growth will accelerate to 3 per cent in 2025. The labour market remains strong, pushing wages higher.

Norway | page 44

We expect mainland GDP growth to fall this winter, although strong oil-sector demand limits the risk of a steep decline. Core inflation will remain high, suggesting that Norges Bank will postpone key rate cuts until autumn.

Finland | page 48

Subdued global demand has hurt Finland's export-dependent manufacturing sector, putting pressure on capital spending and the labour market. GDP will shrink by 0.2 per cent this year but will rebound to 2.0 per cent growth in 2025.

Sweden

Lower inflation increases hopes of a turnaround

GDP fell in the second half of 2023. Although economic activity will be weak for a while longer, a deeper slump seems avoidable. Household consumption has fallen as it did during the 1990s recession but is bottoming out. Unemployment will rise a bit further, but the decline in inflation will boost real incomes and push down interest rates. Fiscal policy will also provide support in 2025. The Riksbank will cut its policy rate this May and growth will accelerate this year, especially starting in Q2.

Sentiment indicators suggest continued GDP declines over the next few quarters, but data have again been a little less weak than anticipated. We expect GDP to increase again in 2024, but very slightly, after falling by 0.4 per cent last year. Due to lower inflation and falling interest rates, downside risks have decreased significantly. This also points to a stronger recovery. Growth will be 2.8 per cent next year, well above trend. We have revised our forecasts for 2023, 2024 and 2025 upward compared to November. Because of high debt, often at variable interest rates, rate hikes have had a large negative effect in Sweden. Now that interest rate will be cut, the positive impact will also be large, but a continued downturn in housing construction and a weaker labour market will pull in the opposite direction during 2024. Favourable inflation surprises will continue this spring, persuading the Riksbank to cut its policy rate as early as May.

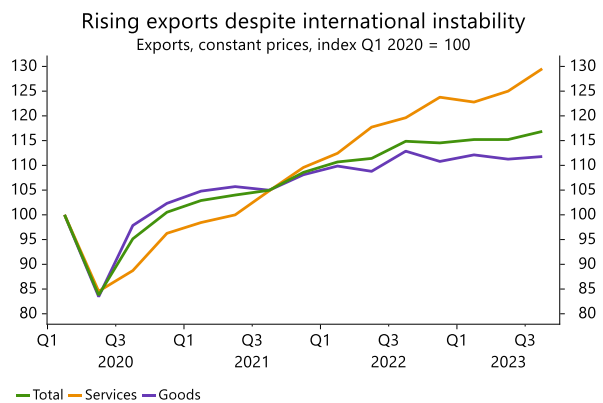
Key data

Percentage change

	2022	2023	2024	2025
GDP	2.6	-0.4	0.1	2.8
Unemployment*	7.5	7.6	8.6	8.7
Wages and salaries	2.8	3.7	3.7	3.5
CPI	8.4	8.5	3.0	1.4
Public sector balance**	1.3	-0.3	-2.2	-0.9
Public sector debt***	32.8	31.4	33.0	33.5
Policy rate, %***	2.50	4.00	3.00	2.25

*% of labour force **% of GDP *** at year-end. Sources: Eurostat, SEB

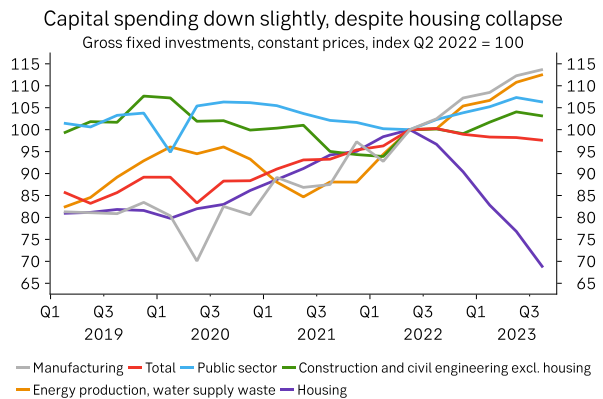
Resilience in industry despite shaky international conditions. The manufacturing sector remains more resilient than expected. Indicators are mixed, but the manufacturing purchasing managers' index (PMI) has risen to just below the neutral level of 50, awakening hopes that a downturn can be avoided. Merchandise exports have stagnated since early 2022, while relatively strong service exports have enabled total exports to continue rising. Short-term indicators point to stable exports during the first half of 2024, and the decline we previously expected now seems less likely. Average total exports will rise by 1.5 per cent in 2024, and by five per cent when the international economy picks up in 2025.



Source: Statistics Sweden (SCB), Macrobond, SEB

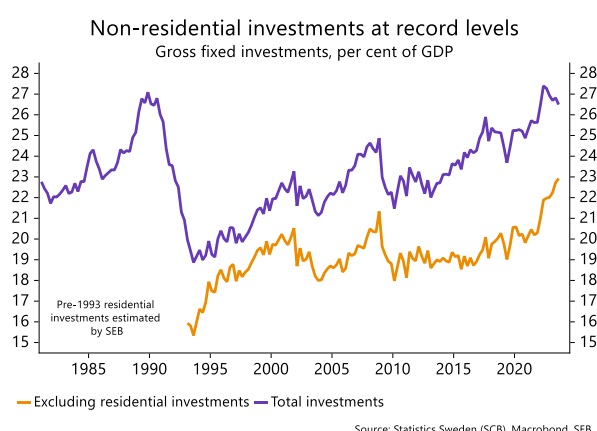
Good investment climate, except for housing.

Resilience in the manufacturing sector is supporting capital spending, which has increased steadily in recent years. Important factors are the weak krona, which has helped keep corporate earnings up, and the green transition. The upturn is relatively broad-based, but automotive, machinery and electrical products are key elements. Public sector investments have also increased steadily over the past 2-3 years, as have investments in heating and energy production. Except for housing, capital spending as a share of GDP has risen to almost 23 per cent, the highest since at least the early 1980s.



Source: Statistics Sweden (SCB), Macrobond, SEB

Plunging residential investments. Despite good investment growth in general, a steep fall in housing construction means that total capital spending has gradually decreased since the first half of 2022. Residential investments are continuing to decline rapidly, and the upturn in industrial and public sector investments will probably slow somewhat from high levels. We continue to expect a clear downturn in capital spending during 2024 but believe that this decline will be somewhat smaller than we previously estimated. Lower interest rates and stronger economic activity suggest that residential investments will rebound in 2025. Due to high interest rate sensitivity, their interest costs will quickly begin to fall.



Mixed outlook, but consumption will accelerate next autumn. The outlook for a continued nominal upturn in consumption is mixed. The fall in real wages over the past two years has been record-sized, but total real household incomes have fallen less, since subsidies, benefits, and tax cuts along with strong employment have worked in the opposite direction. Savings have decreased, but not dramatically, and the savings ratio is not too far below its pre-crisis level. Meanwhile unemployment has begun to climb, and the very low level of consumer confidence is signalling that household finances remain squeezed. We expect consumption to fall slightly during the first half of 2024 and believe that the recovery will begin during the second half, after the Riksbank has begun cutting its policy rate. In 2025, expansionary fiscal policy will help boost household incomes. We assume that lower taxes and increased benefits, totalling SEK 35 billion, will increase incomes by more than one percentage point.

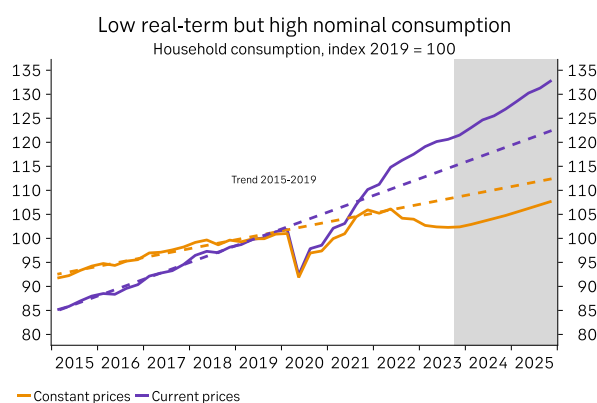
Households' income and savings ratio
Year-on-year percentage change

	2022	2023	2024	2025
Real disposable income	-0.3	-1.6	0.7	3.5
Private consumption	2.1	-2.6	1.4	3.2
Savings ratio, % of income	13.0	13.6	13.2	12.9

Source: Statistics Sweden, SEB

Large downturn in consumption volume

Household consumption continues to be the main factor in determining how deep and protracted the downturn will be, and lower inflation and interest rates will continue to reduce downside risks. Consumption volume had fallen by over 4 per cent in the third quarter of 2023 compared with mid-2022, which is on a par with the declines during the deep recessions of the early 1980s and early 1990s. The downturn is being driven by rising prices, while nominal consumption has risen to levels well above the historical trend. Because of the clear deceleration in inflation, the main force pushing down real consumption is now fading significantly.



Downward pressure on home prices is easing. A large supply of housing and low sales of new homes indicate that the housing market is not yet fully in balance. But interest rate cuts are now approaching, providing support to the housing market. This is reflected in the SEB Housing Price Indicator, which rose sharply in January. Home prices remained largely unchanged in 2023. We expect this sideways trend to continue over the next six months. From mid-2024, we expect a gradual home price increase.

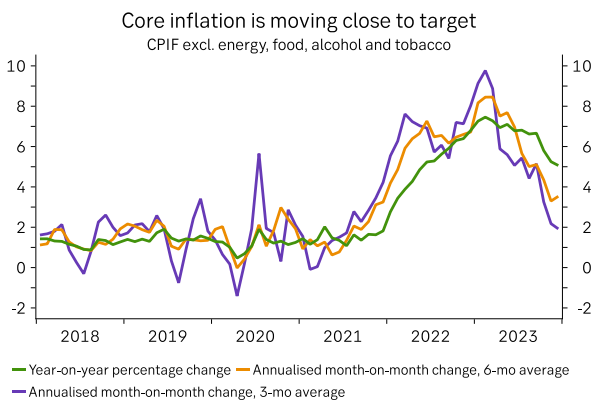
Higher unemployment rate in 2024

After resisting the economic slowdown since mid-2022, the labour market is now showing clearer signs of deceleration. In the second half of 2023, unemployment rose by more than 0.5 percentage points to about 8 per cent, and employment is now falling. Layoffs, vacancies and recruitment plans according to the Economic Tendency Indicator of the National Institute of Economic Research (NIER) suggest that the labour market will continue to weaken this year, but not dramatically. We expect the jobless rate to level off at around 9 per cent after this summer. As the recovery picks up speed in 2025, unemployment will gradually fall.

Slightly higher pay increases, but not too high for the Riksbank. Labour market weakness is being confirmed by falling resource utilisation indicators (RUIs). Shortages according to both the NIER survey and the Riksbank’s RUI have fallen back to average historical levels from record levels in late 2021. Due in part to this downturn, over the past six months hourly earnings have increased by only 0.2-0.3 percentage points more than wage agreements. In November, we adjusted our wage and salary forecasts for both 2023 and 2024 downward to 3.7 per cent, or 0.2-0.3 points per year below the Riksbank’s forecast. Pay increases in Sweden continue to seem low. A weaker labour market and lower inflation suggest that pay hikes will slow in 2025 when the next national wage round takes place. Our forecast of 3.5 per cent in total pay increases during 2025 remains unchanged. The need to catch up with the very large decline in real wages suggests that for a few more years, wages and salaries will continue to increase faster than before the pandemic.

Inflation temporarily below target

Swedish inflation has finally also fallen. Helped by strong base effects from extremely high electricity prices in December 2022, CPIF (CPI with constant interest rates) fell to 2.3 per cent in December 2023. This downturn is partly temporary, and base effects from energy will lift inflation in early 2024. Cold weather has also caused this winter’s electricity prices to rise significantly, though levels are far from 2022 peaks. Electricity futures indicate that prices will fall back this spring and summer. Combined with falling fuel prices, this suggests that energy prices will fall by almost 10 per cent in 2024.



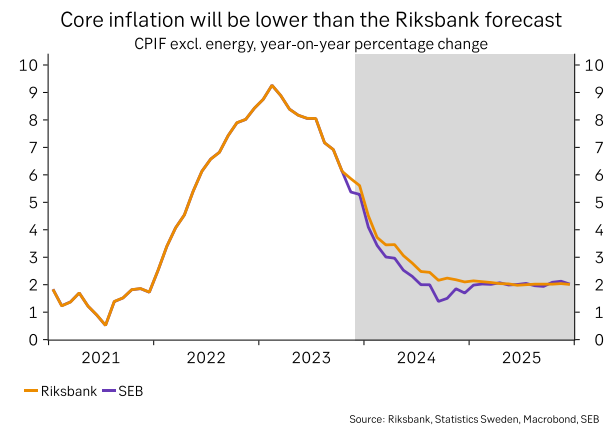
Source: SCB, Macrobond, SEB

The latest inflation figures are pointing in the right direction. Underlying inflation has also slowed significantly in recent months. CPIF excluding energy was 5.3 per cent in December, or 4.0 percentage points below its peak in February 2023. Compared with a year ago, core inflation is still well above the Riksbank’s 2 per

cent target, but annualised month-on-month price changes have been close to 2 per cent, although strong seasonal effects make this assessment uncertain. The downturn is mainly driven by base effects on food and other goods, but there are signs that service inflation is also slowing. The inflation downturn in Sweden is still lagging the euro area, but the gap has narrowed in recent months. Short-term indicators suggest that inflation will continue to slow in 2024. For example, plans to raise retail prices are only slightly higher than before the pandemic.

High service inflation is causing transitory concerns.

Service inflation remains high, creating some uncertainty, but reduced or even negative effects from previously high energy prices and moderate wage increases strongly suggest that it is on its way down. Continued large rent increases due to higher interest rates, administrative prices and public sector fees are offsetting the decline in inflation and are the clearest upside risk. We expect CPIF excluding energy to fall to slightly below the 2 per cent inflation target late in 2024 and then rise roughly to target in 2025. Because of lower energy prices, CPIF will fall below target as early as this summer and approach one per cent by the end of the year. In 2025, CPIF will increase at the same rate as core inflation.



Source: Riksbank, Statistics Sweden, Macrobond, SEB

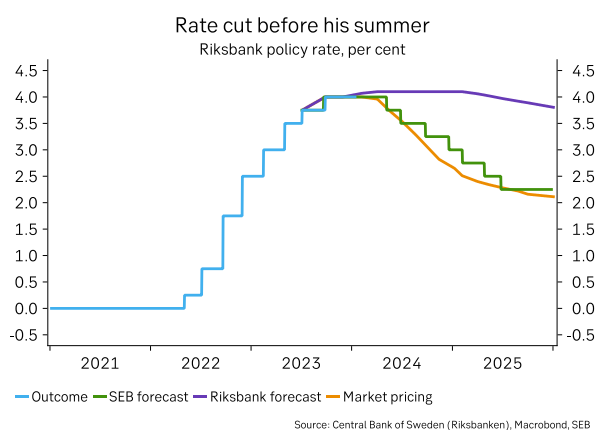
Price reversal and the krona create uncertainty. As in the euro area, there is great uncertainty about how far inflation will fall, and a possible price reversal in the euro area (see p. 12) will most likely be similar in Sweden. The appreciation of the krona late in 2023 reduces upside risks significantly, although the exchange rate – according to our models – will continue to contribute to higher inflation for most of 2024.

Interest rate cut before this summer

The Riksbank’s policy rate forecast from November indicated a relatively high probability of another rate hike in early 2024. After core inflation surprised

markets on the downside in November, together with clear expectations of imminent ECB and Fed rate cuts, the Riksbank has downplayed the rate path in speeches and interviews. It is very likely that the end of the hiking cycle has been reached. The probability of interest rate cuts this year is also high, but the timing and pace are uncertain. The Executive Board has indicated that it wants to ensure that inflation is in line with its target before the rate cut. This suggests that market expectations of a cut by March are too optimistic.

The Riksbank does not want to be first. We also believe that the Riksbank wants to avoid renewed krona depreciation and that they are happy to let the ECB cut its key rate first, at least as long as the krona does not appreciate much further. At the same time, economic growth and the labour market are weaker in Sweden, where high rate sensitivity makes the price of postponing rate cuts high. We expect the first rate cut to be in May, but January's hard-to-assess inflation figures are creating uncertainty. We expect the policy rate to be cut by a total of 100 basis points this year and by a further 75 bps, to 2.25 per cent, in 2025. Inflation and inflation expectations will be crucial, and rate cuts of more than 25 bps at a time may be necessary if inflation surprises on the downside. Meanwhile the downward cycle may be delayed if the decline in inflation is more sluggish than expected.



More QT despite lower interest rates. Even though the Riksbank will start cutting interest rates within a few months, we are sticking to our assessment that its government bond divestments (quantitative tightening, QT) will increase from SEK 5 billion to SEK 7-8 billion after its policy announcement in early February. The Executive Board has indicated that this balance sheet reduction should be viewed primarily as a normalisation and that interest rates are its most important policy tool. November's Monetary Policy Report clearly stated that QT will be expanded following the February announcement, and several Executive Board members

have said that bond sales have improved the functioning of the market and helped strengthen the krona.

Lower inflation will allow stimulus in 2025

The government's budget bill for 2024 contains a total of SEK 40 billion in spending increases and tax cuts. Much of this consists of higher grants to local governments that are not inflation-indexed, and fiscal policy is regarded as neutral. We believe that new measures worth about SEK 5 billion will be unveiled in the spring budget in April, making 2024 fiscal policy slightly expansionary. The government continues to prioritise the fight against inflation, and the fiscal policy stance is very cautious. With lower inflation, this argument will fade, but we believe the government will wait until 2025 before shifting to more expansionary fiscal policy, partly because of the approaching 2026 election. Government and NIER calculations indicate relatively large structural budget surpluses. We expect expansionary measures totalling SEK 60-80 billion in 2025, equivalent to 1-1.5 per cent of GDP.

Strong finances in spite of deficits. Government finances remained stronger than expected during most of 2023, but late in the year there were signs that tax revenues were being hurt by the weak economy. The central government budget surplus was SEK 19 billion in 2023, or 12 billion lower than the National Debt Office forecast. There are many indications that the central government will show a deficit in both 2024 and 2025. In addition, local government finances will weaken as GDP falls. This year, central government finances will also be affected by the Riksbank's recapitalisation, although due to a sharp decline in bond yields late in 2023 and Riksbank FX hedging the required amount appears to be significantly smaller than the SEK 80 billion that the Riksbank expected as recently as last October. We expect a capital injection of SEK 40 billion, which will contribute almost 2 per cent of GDP to the public sector deficit this year. Despite deficits, central government finances remain extremely strong, and Sweden's public sector debt is stabilising at just over 30 per cent of GDP.

Lower surplus targets? The government has said that its surplus target of 0.3 per cent of GDP will be re-examined. Central government debt is just over 15 per cent of GDP and a lower target is likely. A deficit target of 1.5 per cent of GDP would cause public sector debt to stabilise at around today's level, but a more cautious approach will probably be chosen. Also important is the allocation between central and local governments and pension funds. Savings in pension funds are expected to approach 1 per cent of GDP, opening for central government deficits even with a balance target.

Norway

Delayed rate cuts

Economic activity was lacklustre during most of 2023, dampened by weak domestic demand. We expect growth in mainland GDP to fall this winter, although strong petroleum-sector demand limits the risk of a steep decline. Improving real disposable income, lower cost inflation and easing monetary policy will underpin domestic demand in 2025, resulting in trend-like growth in mainland GDP. Core inflation will remain high in an international comparison, suggesting that Norges Bank will postpone key rate cuts until autumn.

Economic activity has slowed, with sequential growth in mainland GDP broadly unchanged during the first three quarters of 2023. This weakness has been driven by domestic demand, notably a steep fall in mainland capital spending. Household consumption will further dampen activity near term. According to Norges Bank’s regional network, activity will fall this winter, causing the output gap to turn negative. Improving real disposable income, lower cost inflation and easing monetary policy will underpin domestic demand in 2025, causing mainland GDP growth to rebound from 0.5 per cent in 2024 to a trend-like 1.4 per cent in 2025. Total GDP will be supported by strong petroleum sector activity, with growth predicted to rise by 2.1 and 1.6 per cent in 2024 and 2025, respectively.

Key data

Year-on-year percentage change

	2022	2023	2024	2025
GDP	3.0	0.5	2.1	1.6
Mainland GDP	3.8	0.9	0.5	1.4
LFS unemployment*	3.2	3.6	3.9	3.7
Wages and salaries	4.3	5.5	4.9	4.0
CPI-ATE inflation	3.9	6.2	4.1	2.5
Key interest rate, %	3.50	4.50	4.00	3.00

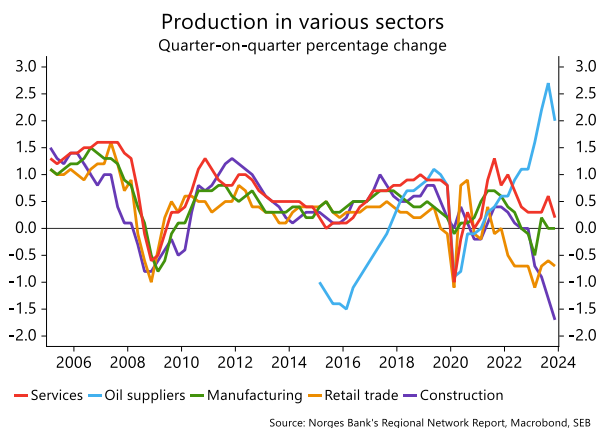
*% of labour force. Source: Macrobond, SEB

Neutral fiscal policy. The government is advocating responsible spending. The fiscal impulse is estimated at 0.4 percentage points of mainland GDP in 2024, but adjusting for foreign-related spending the budget will be neutral. Absent a sharper economic slowdown

triggering a more pronounced rise in unemployment, opposition to increase fiscal spending will be strong.

Large discrepancies between sectors

Aggregate business sentiment is weak, although there are still wide variations across industries. Suppliers to the oil industry continue to enjoy support from a cyclical upswing in petroleum capital spending. Oil investments have increased by 16.8 per cent over the past year and are expected to rise further by an accumulated 8.0 per cent in 2024-2025. Meanwhile, pessimism in the construction and retail sectors has intensified, and the vast service sector has become less optimistic. We project that private mainland capital spending will be a drag on growth in 2024. High investment activity in previous years will dampen business investments, although some projects related to climate and energy transition will limit the overall decline. Residential investments have plunged 22 per cent since their peak in Q1 2022, and lower housing starts point to a further decline in the first half of 2024. Lower cost inflation and higher home prices will underpin capital spending further out.



Modest export growth, despite the weak NOK.

Despite improved competitiveness owing to the weak krone exchange rate, exporters of traditional goods are modest in their production expectations. Anaemic growth among Norway’s main trading partners is limiting demand, reflected in more spare capacity. Weak domestic demand is restraining corresponding imports, and net trade in traditional goods is projected to be a slight drag in 2024, while turning positive in 2025.

Home prices surprisingly resilient

Existing home prices fell 0.3 per cent in 2023 – the first annual decline since 2008. Prices nonetheless defied widespread expectation of a correction this past autumn. Difficulties with seasonal adjustments may have temporarily supported prices, but activity has nonetheless held up well although transaction times

have lengthened. We continue to project a small correction this winter due to higher lending rates and rising unemployment. Further ahead, a limited supply of new homes owing to plunging residential investments – combined with improving purchasing power – point to an acceleration in home price inflation. We forecast existing home price growth of 0.9 and 5.3 per cent in 2024 and 2025, respectively.

A mild upturn in unemployment

The labour market is cooling, albeit gradually. According to the Norwegian Labour and Welfare Administration (NAV), registered unemployment rose 0.2 percentage points during 2023 to 1.9 per cent. New registered job vacancies have continued to trend lower, pointing to a further increase ahead. Employment growth has remained positive but hiring plans have been lowered, suggesting falling employment during the winter led by expected layoffs in construction, retail trade and manufacturing. The volatile Labour Force Survey (LFS) suggests that employment will stabilise later this year, supporting our projection of a relatively mild upturn in unemployment. We forecast that registered unemployment will peak at around 2.5 per cent in 2025.

Wage and salary growth likely increased by 5.5 per cent in 2023, implying three consecutive years with negative or zero growth in real wages. This year's pay negotiations will be tough, with unions calling for positive real pay increases. Nominal wage growth will fall due to slowing CPI, but the tight labour market combined with high oil sector activity and improved competitiveness among exporters suggest pay rises of 4.9 and 4.0 per cent in 2024 and 2025, respectively.

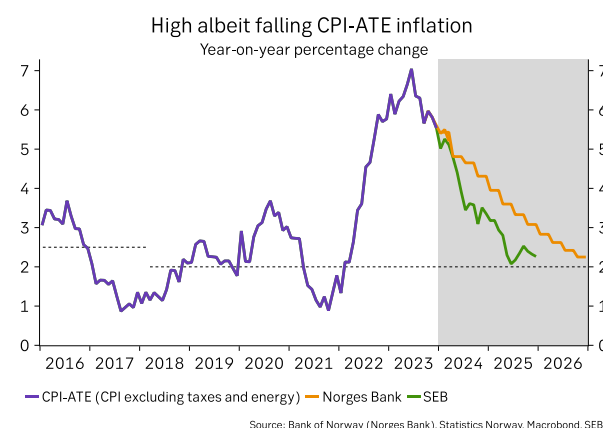
Weak private consumption through winter

Consumer confidence remains depressed, reflecting weak real disposable incomes and rising mortgage rates, yet private consumption has held up surprisingly well, underpinned by high job security and savings. However, a sharp drop early in the year related to car purchases points to a decline in private consumption of 1.0 per cent in 2023. A further fall in goods consumption this winter, as reflected in depressed sentiment among retailers, suggests that private consumption will remain modest in 2024. Accelerating real wage growth and lower interest rates will support consumption later, though higher unemployment and a build-up in household savings buffers will limit consumption growth to 2.1 per cent in 2025.

Inflation well above target in 2024

CPI-ATE (CPI excluding taxes and energy) fell to 5.5 per cent in December. Inflation has continuously moderated

since the 7.0 per cent peak in June last year, and the decline has been slightly larger than predicted. Still, inflation is high compared to many other countries. The weak exchange rate has sustained the rise in core goods prices. Food prices have continued to rise, adjusted for seasonal effects. Gradually higher rents have also underpinned service prices. These factors will contribute to continued high core inflation near term, although indicators still point to an accelerated decline from spring. Slowing international food prices and related input prices suggest that food inflation will fall rapidly in 2024, and recent krone appreciation implies that upward pressure due to the exchange rate will wane. We have lowered our CPI-ATE forecast and predict a more marked decline in inflation from summer compared to Norges Bank's trajectory. Core inflation of 4.1 and 2.5 per cent in 2024 and 2025, respectively, are still high in an international comparison.



Subsidies have restrained the impact of energy prices on CPI. With energy prices now falling, the effect on CPI is thus quite small compared to Sweden, for example. CPI inflation is projected to average 3.9 and 2.8 per cent in 2024 and 2025, respectively.

Key rate cuts from September

Excessive inflation and concerns regarding second-round effects from the weak exchange rate justified a final key rate hike to 4.50 per cent in December. Tight monetary policy is deemed necessary to return inflation to target within a reasonable period. Norges Bank thus intends to stay on hold until Q3, lowering its key rate gradually thereafter to 3.50 per cent by end-2025. Our expectation of a faster moderation in core inflation, combined with a significant stronger-than-projected krone, suggests a faster pace, but sticky core inflation in early 2024 and uncertainty regarding the outcome of upcoming wage negotiations imply that rate cuts will be delayed until September. We forecast a key rate of 4.00 and 3.00 per cent by end-2024 and end-2025, respectively.

Denmark

Waiting for take-off

Consumption and housing indicators are improving, and we still expect growth to accelerate from 1 per cent in 2023 to 3 per cent in 2025. Home prices will continue to hold back residential investments for some time. The labour market remains strong and will push wages higher, but not to any problematic levels.

Revised Q3 GDP data. Since the last *Nordic Outlook*, Statistics Denmark has revised its GDP growth data for the third quarter of 2023 downward by 0.6 percentage points. This means that GDP declined by 0.7 per cent q/q in both Q2 and Q3. Over the first three quarters of the year, GDP was still 1.1 per cent higher than in 2022, and macro indicators suggest there was a return to positive GDP growth in Q4. As a result, we have only reduced our GDP growth estimate marginally to 1 per cent for 2023 and have kept our forecast profile unchanged, with growth of 1.5 per cent in 2024 and 3 per cent in 2025.

Key data

Year-on-year percentage change

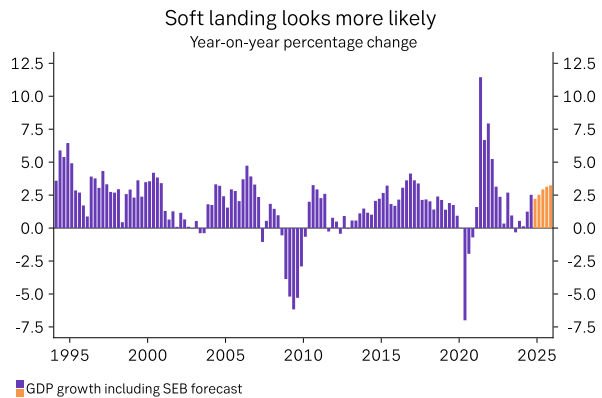
	2022	2023	2024	2025
GDP	2.8	1.0	1.5	3.0
CPI	7.7	3.3	1.0	1.6
Wages and salaries	2.6	3.3	3.6	4.1
Public sector fiscal balance*	3.4	3.5	3.5	4.0
Public sector debt*	30.1	30.0	29.0	27.0
Current account*	13.3	10.0	9.0	8.0
Key interest rate (CD rate), %	1.75	3.60	2.60	1.60

*% of GDP. Source: Statistics Denmark, DØRS, SEB

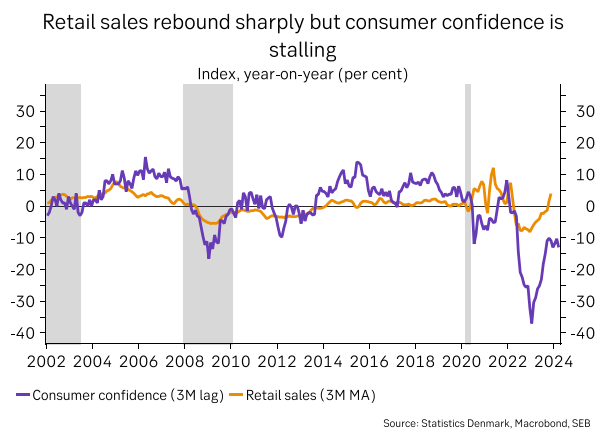
Volatile GDP indicator better than expected.

Denmark's GDP data have been unusually volatile in recent quarters, since they have been impacted both by a boom-bust cycle in shipping and a surge in pharmaceutical exports driven by the success of Novo Nordisk's new anti-obesity drugs. Statistics Denmark also warns that seasonal adjustments will have

increased uncertainty in the wake of the pandemic. We are thus careful not to overemphasise the most recent quarterly data, especially since the weakness in GDP growth seems at odds with other macro data.



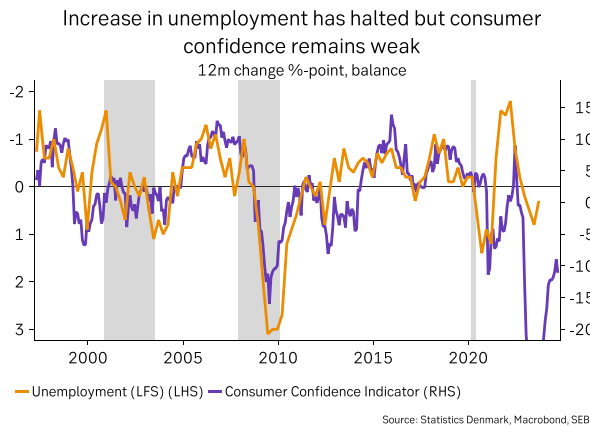
Jump in retail sales. Net exports have been the main growth driver in 2022 and 2023, but private consumption is finally showing signs of life. Retail sales jumped 1 per cent in November from October, their fourth consecutive gain, and the three months from September to October saw a gain of 4.9 per cent compared to the preceding three months. While consumer confidence remains subdued, rising real wages and continued employment gains appear to have started to lift spending. After the 2022 slump, consumption growth probably reached positive territory by the end of 2023, and we expect this to pick up to more than 3 per cent in 2024.



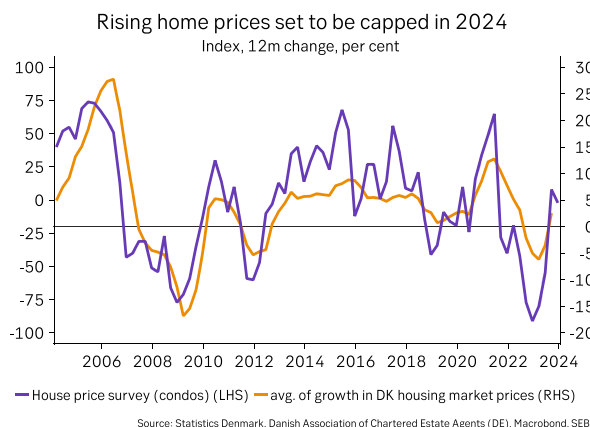
Employment and real wages anchor growth.

Consumer confidence may still be soft, but it decoupled from the normal historical relationships during the inflation shock. Most importantly, the traditional link between the labour market and confidence has broken down completely. Based on the historical relationship, with employment growth of around 1 per cent and unemployment edging higher, consumer confidence should be positive, not on a par with the trough in 2009.

A change in this relationship is reasonable, since we normally view unemployment as the key driver for income expectations while the shock in 2022 was due to surprisingly high inflation. Nonetheless, with headline inflation averaging close to zero over the past three months and real wages rising around 3 per cent annually, even this shock to confidence is likely to fade in the coming months.



Home prices are rising again. In the housing market, recent months have seen a decline in the 30-year mortgage rate, taking the coupon on the benchmark bond from 6 to 4 per cent. Coupled with an easing of lending conditions for households, this has allowed home prices to start climbing again. This shift is likely to be capped in 2024, since the moratorium on taxes can no longer be locked in by new buyers, but the risk of a crisis that could spill over to other parts of the economy has diminished.

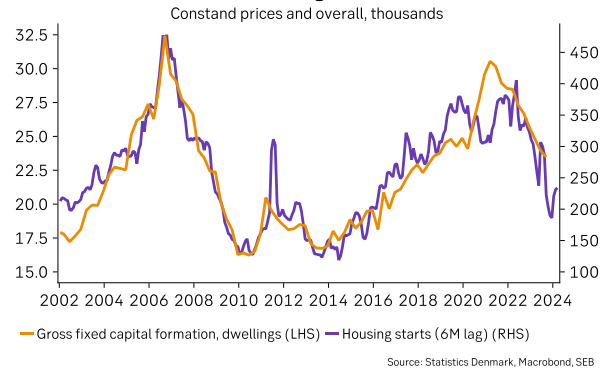


Construction down 23 per cent from 2021 peak.

While home prices have increased a little, construction investments remain a drag on the economy. Residential investments peaked in early 2021 and were down 23 per cent from that peak during Q3 2023. We do not expect any recovery in this area until home prices have recovered a bit more lost ground. On the other hand, business investment has bottomed out, and high

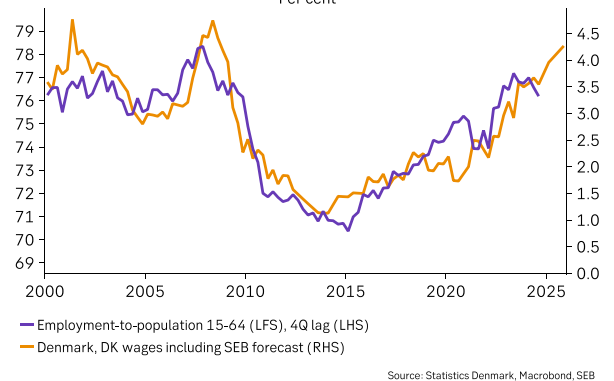
capacity utilisation suggests there is an upside for machinery and equipment investment in the next couple of years.

Lower construction activity likely to be among headwinds in the housing market



The labour market remains surprisingly strong, also compared to the latest GDP releases. Total employment is still growing more than 1 per cent on an annual basis, and unemployment has only seen a mild increase of less than 1 pp during the downturn and is expected to start falling again. The historical relationship between the employment-population ratio and wage inflation suggests that wage inflation could pick up from the current 3 per cent in 2023 to more than 4 per cent in 2025. With a sustained current account surplus of more than 10 per cent of GDP, we do not see this level of wage inflation as problematic.

Acceleration in wage inflation to pick up



Stable policy rate spread. The burgeoning and chronic current account surplus also provides a strong foundation for the krone-euro peg, but the question is whether widening of the policy rate spread to -40 bps was a step too far. The DKK/EUR exchange rate did weaken temporarily last autumn to levels where Danmarks Nationalbank normally intervenes but has since recovered and is now very close to central parity. We expect both the key rate spread and the DKK to remain stable in 2024.

Finland

Lower exports and capital spending prolong recession

Weak performance during the second half of 2023 pushed the Finnish economy into a recession, with full-year GDP falling by 0.5 per cent. Depressed exports and falling capital expenditures will cut GDP by a further 0.2 per cent in 2024. A broad-based recovery will not happen before 2025, when we expect 2 per cent growth.

Weak exports dampen hopes for recovery. A steep decline in capital spending and exports caused GDP to fall by 1.5 per cent year-on-year in the third quarter of 2023. For a long period, the export-dependent manufacturing sector managed to dodge headwinds from weak global demand, but order books have now fallen almost to the depths last seen during the COVID-19 crisis. This time around, a quick recovery thus seems unlikely. In the coming quarters, production levels will decline even further, forcing companies to start cutting costs while putting pressure on both investments and the labour market. Exports will stagnate in 2024 but will increase by 4 per cent in 2025 as global demand improves.

Key data

Year-on-year percentage change

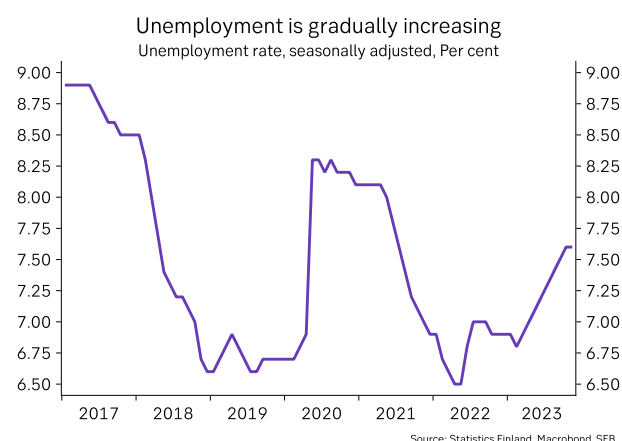
	2022	2023	2024	2025
GDP	1.6	-0.5	-0.2	2.0
Household consumption	1.5	-1.0	0.2	1.5
Exports	3.7	-1.0	0.0	4.0
Unemployment*	6.8	7.2	7.8	7.3
Wages and salaries	2.4	4.5	3.5	2.5
HICP inflation	7.2	4.3	1.5	1.5
Public sector fiscal balance**	-0.8	-1.5	-2.5	-2.0

*% of labour force **% of GDP. Source: Eurostat, SEB

Home construction standstill depresses capital spending. Despite a slight uptick late last year, the number of housing starts fell in 2023 to levels not seen since 2009. A continued low number of building permits will mean another grim year in 2024. Home prices have fallen by roughly 20 per cent from their peak in mid-

2021. Together with higher interest rates, this is preventing people from buying homes and is discouraging developers from starting new residential projects. To keep its deficit within limits, the public sector – usually active in the market – has not been much help. Higher interest rates are forcing companies in general to postpone their investment plans, which worsens the outlook even more. Since the underlying factors behind this recent decline will not change much, capital spending will decrease by a further 1.8 per cent in 2024, before rebounding by 4 per cent in 2025.

Deterioration in the labour market. Low demand in the manufacturing and construction sectors has resulted in a first wave of furloughs and layoffs, but with limited impact so far. Unemployment is gradually increasing and will soon reach levels seen in the aftermath of the pandemic. The jobless rate will hit 7.8 per cent in 2024, falling back to 7.3 per cent in 2025. Despite the upturn in unemployment, wage growth will remain above its long-term average this year.



Subdued household demand. Despite a relatively strong labour market, households have been extremely cautious in their spending, because inflation has eroded real income. Consumer confidence has continued to weaken in recent months, which could lead to a further decline in retail sales. On the positive side, inflation has almost come to a halt. In 2024 we expect HICP to increase by 1.5 per cent, leading to a recovery in real wages. Consumption will remain roughly at its 2023 level this year and will increase by 1.5 per cent in 2025.

A tricky situation for the government. The government that took office last summer on a strong austerity mandate is in a tricky position, with the economy in a recession and unemployment on a rise. Despite a worsening economic situation, it still seems unlikely that much fiscal stimulus will be handed out. This means that the budget deficit will stay within the 3 per cent threshold this year and next.

The Baltics

Lithuania | page 50

The economy will recover somewhat, fuelled by household consumption and government investments. Subdued global demand will hold back exports. The labour market will deteriorate a bit more. We expect GDP growth of 1.5 per cent in 2024.

Latvia | page 51

Strong growth in real wages will support the recovery in retail trade and services. Rising consumption will be the key driver of economic growth this year. Energy prices and geopolitical instability are the main risks to our forecast.

Estonia | page 52

The economy has fallen into a deep recession due to the decline in exports and low confidence among households and businesses. Given the continued weak export outlook, a rapid recovery is not very likely. GDP will fall by 0.5 per cent this year.



Lithuania

Waiting for a recovery in household consumption

The economy is projected to rebound in 2024, albeit moderately, fueled by a recovery in household consumption. Government investments will also support growth, while exports will stagnate due to weak external demand. The situation in the labour market will deteriorate somewhat further. Fiscal policy will be expansionary in 2024. This year’s presidential and parliamentary elections will probably impede the constructive adoption of necessary but unpopular laws.

Household consumption and exports fell markedly last year. But partly because of a sharp growth in investments, 2023 GDP fell only marginally. We foresee a stagnation in economic activity during the early part of this year and a recovery in the second half, partly due to stronger consumption. We have left our 2024 and 2025 GDP growth forecasts unchanged.

Key data

Year-on-year percentage change

	2022	2023	2024	2025
GDP	2.4	-0.2	1.5	2.8
Household consumption	2.0	-1.6	2.8	3.2
Exports	12.2	-5.2	1.0	4.0
Unemployment*	5.9	6.6	6.8	6.5
Wages and salaries	13.4	12.4	8.5	7.0
HICP inflation	18.9	8.7	2.0	2.7
Public sector fiscal balance**	-0.7	-0.6	-2.5	-1.8

*% of labour force **% of GDP. Source: Eurostat, SEB

Goods exports are slumping, but service exports are still rising.

The decline in goods exports is strongly related to a sharp drop in re-exports. Re-exports to Central Asia and the Caucasus fell, returning close to pre-war levels. Exports of Lithuanian-origin goods also fell in 2023, but the situation has been stabilising recently. Projected orderbooks have improved somewhat, and manufacturers are indicating some kind of stabilisation in production in the short term. Diversification of products and markets is helping to avoid a stronger decline in exports.

Capital spending will decelerate significantly in 2024.

Government investments, supported by EU structural and Recovery and Resilience Facility (RRF) funds, will keep supporting the economy this year. Construction companies working with infrastructure projects are fully booked, but the situation is entirely different for companies working in the residential and commercial property markets. There is a slowdown in capital spending by new foreign investors, partly due to increased geopolitical concerns.

Wage growth below double digits in 2024.

As inflation decelerates, household purchasing power will improve significantly this year. We expect headline inflation of only 2 per cent in 2024. Our forecast is a slight rise in unemployment in 2024, but given the real wage increase, consumption will climb. In contrast to many Western economies, consumer confidence remains historically high. We expect the household saving ratio to rise somewhat in 2024. Since most mortgages have variable interest rates, interest expenditures are now peaking and will decline as early as the second half of 2024.



Home prices avoided a correction in 2023.

Considering the sharp increase in interest rates and low property market activity, the absence of a major correction is a bit surprising. If housing prices stagnate in 2024 and interest rates fall, that should improve housing affordability and may support a home price increase in 2025.

Expansionary fiscal policy in 2024.

The public budget deficit will jump in 2024 as the government focuses on increasing the income of low earners and public sector employees. Last year’s government attempt to improve the efficiency of the tax system and shift away from taxing labour towards taxing wealth and capital was a failure. Another short-term challenge – to find new sustainable sources to finance increased defence spending – may lead to higher taxation.

Latvia

Somewhat brighter outlook due to domestic demand

Various signals indicate that economic activity bottomed out at the end of 2023. We expect a gradual recovery during the first half of this year, with better momentum in the second half as solid real wage growth supports consumption, while increased EU fund inflows will boost capital spending. Exports will remain sluggish in 2024.

The outlook will improve. Overall economic sentiment has remained below average for some time. We believe the economy will remain stagnant in early 2024 but will steadily improve. Strong real wage growth will support a recovery in retail trade and services. Rising household consumption will be the key driver in 2024. Lower interest rates will provide additional impulses to the economy. Energy prices and geopolitical instability are the main source of uncertainty and risks.

Key data

Year-on-year percentage change

	2022	2023	2024	2025
GDP	3.4	-0.4	2.0	2.7
Household consumption	6.4	-1.5	1.6	2.2
Exports	10.3	-6.2	2.4	3.2
Unemployment*	6.9	6.5	6.5	6.4
Wages and salaries	7.5	11.5	8.2	7.7
HICP inflation	17.2	9.0	1.4	2.4
Public sector fiscal balance**	-4.6	-2.6	-2.8	-2.5

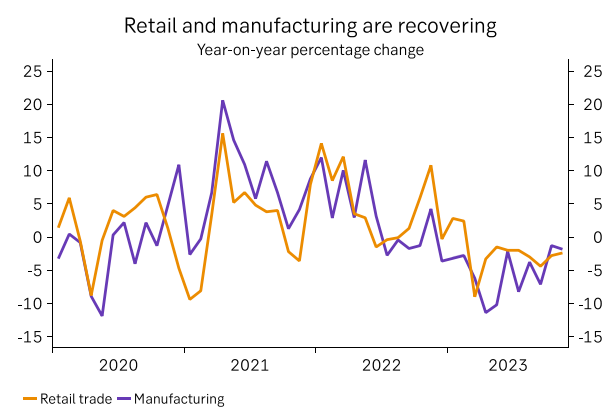
*% of labour force **% of GDP. Source: Statistics Latvia, SEB

Exports and manufacturing continue to face headwinds. Exports will benefit from improving global demand and lower interest rates, but we see no reason to bet on rapid advances in important sectors such as wood products, since housing construction in major export markets is still weak. The recovery in manufacturing may thus remain slow throughout 2024. Service exports have better prospects. Due to the war in Ukraine and sanctions on trade with Russia, downward pressure on the transit trade and exports will continue. Adverse weather may have an impact, but

we expect stronger farm production this year. Improved household and corporate confidence will support the real estate and financial sectors.

EU funds offer an opportunity. According to the government budget, a historically large amount of EU funds – EUR 1.6 billion – will be available in 2024. A large share will flow through the construction sector, with the most significant investments being planned for climate change mitigation such as public transport, modernisation of energy networks and improvements in energy efficiency of buildings. Funds will also be available for regional infrastructure, business promotion and innovation and low-rent housing construction.

Solid real wage growth to continue. Wage and salary growth of 11.5 per cent in 2023 was somewhat higher than expected, but it will decline to around 8 per cent this year, though solid real wage growth will continue as inflation falls. The decline in inflation is mainly due to lower energy prices, but this effect will gradually fade. Food prices should become more stable, and price levels may fall in some cases. Inflationary pressure will remain steady in services, due to rising wage costs. We expect inflation to decrease from 9 per cent in 2023 to 1.4 per cent in 2024 and pick up to 2.4 per cent in 2025.



Source: Latvian Central Statistical Bureau, Macrobond, SEB

Labour shortage still an issue for companies. In Q3 2023, unemployment increased by 0.1 percentage points compared to Q2 and reached 6.5 per cent. Due to sectoral challenges, we expect a short-lived and limited increase in unemployment going forward. Including seasonal fluctuations, unemployment will average 6.5 per cent this year and decrease to 6.4 per cent in 2025.

Little fiscal manoeuvring room. The Saeima (parliament) has adopted a three-year framework for the government budget. Key priorities are internal and external security, education and health. Defence spending will reach 2.4 per cent of GDP in 2024. We expect the 2024 budget deficit to be 2.8 per cent and government debt 41 per cent of GDP.

Estonia

The downturn is not over

A sharp decline in exports and low confidence among households as well as businesses have driven the economy into a steep recession. According to our estimates, GDP fell by 3.4 per cent in 2023. Due to the continuing weakness of Estonia's main trading partners, a quick recovery remains very unlikely. In 2024 GDP will fall by another 0.5 per cent. The economy will again start growing in 2025, when we expect a 3.5 per cent upturn.

A broad-based slump in exports. The Estonian economy has relied heavily on demand from the Nordic countries, especially Finland and Sweden. Since both economies are in a downturn, partly driven by housing construction, a sizable part of Estonia's manufacturing sector is without orders. The downturn in trade is more broad-based, however. Exports to many other markets have also declined by double-digit figures. We estimate that exports will fall by a further 1 per cent in 2024, followed by a 5 per cent upturn in 2025 as global growth improves.

Key data

Year-on-year percentage change

	2022	2023	2024	2025
GDP	-0.5	-3.4	-0.5	3.5
Household consumption	2.0	-1.8	0.0	3.0
Exports	3.0	-8.0	-1.0	5.0
Unemployment*	5.5	6.7	8.7	7.5
Wages and salaries	11.6	11.2	6.5	6.0
HICP inflation	19.4	9.1	3.8	2.5
General government fiscal balance**	-0.9	-2.0	-3.5	-3.0

*% of labour force **% of GDP. Source: Eurostat, SEB

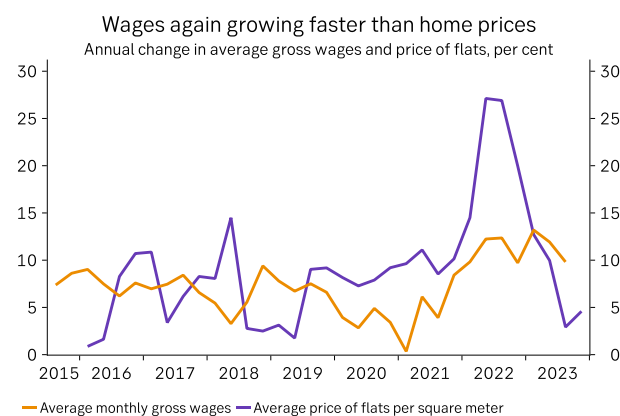
Unemployment will rise. The decline in exports is also impacting the labour market, since manufacturing remains the largest employer. Employment has been falling since late summer but has decreased much less than expected given the decline in industrial output. In recent years the scarcity of labour has been a major problem for businesses. Employers are thus unwilling to make quick adjustments, hoping that demand will return soon. Yet it seems unlikely that current employment levels can be maintained. There is still an abundance of

vacancies in the service sector, but due to geographic mismatches, few of those working in manufacturing, or the unemployed, can fill those jobs. We now estimate that average unemployment will increase to 8.7 per cent in 2024 and fall back to 7.5 per cent in 2025. Wage growth will ease but remain above 6 per cent during our forecast period. Thus, real wages are again rising at a firm pace, supporting household consumption.

Resilience in business investments is temporary.

Business sector investments have been holding up fairly well, despite rising interest rates. The same goes for new lending, which has remained healthy despite significantly lower demand for real estate financing. An expected decline in interest rates will help to sustain investment appetite, although a marginal fall from previous high levels will be hard to avoid.

Decreasing construction, but prices will hold. Unlike the situation in the Nordic countries, home prices have managed to avoid a decline. In the fourth quarter of 2023, the average cost per square meter of flats was 4.6 per cent higher than in Q4 2022. Without more significant deterioration in the labour market, home price levels will probably stagnate in 2024. Real estate developers have become pessimistic regarding the market outlook, however. This will lead to much lower construction activity. Some support to the construction sector is being offered by public sector investments in transport and defence infrastructure.



Ambiguity regarding public finances. The government has eased its previously hawkish tone regarding public finances. It is now hinting that it may postpone some of the tax hikes it has planned for 2025 and instead increase borrowing to finance the budget deficit. With no detailed plans released yet, we expect the deficit to total 3.5 per cent of GDP in 2024 and public debt to increase to 22 per cent of GDP.

Global key indicators

Yearly change in per cent

	2022	2023	2024	2025
GDP OECD	2.9	1.6	1.4	2.0
GDP world (PPP)	3.3	3.1	2.9	3.1
CPI OECD	9.5	6.7	3.1	2.3
Oil price, Brent (USD/fat)	99	82	85	88

US

Yearly change in per cent

	2022 level, USD bn	2022	2023	2024	2025
Gross domestic product	25,744	1.9	2.4	1.6	1.8
Household consumption	17,512	2.5	2.2	1.8	1.7
Public consumption	3,570	-1.0	2.8	0.5	-0.1
Gross fixed investment	5,476	1.5	2.2	1.6	4.3
Stock building (changes as % of GDP)	157	0.5	-0.4	-0.1	0.0
Exports	2,995	7.0	2.7	1.9	1.7
Imports	3,966	8.6	-1.7	1.3	3.0
Unemployment (%)		3.6	3.6	3.9	4.0
Consumer prices		8.1	4.1	2.4	2.2
Core CPI		6.1	4.8	3.0	2.3
Public sector financial balance. % av BNP		-3.7	-8.2	-8.0	-8.0
Public sector debt. % av BNP		121.3	123.1	127.3	131.6

Euro area

Yearly change in per cent

	2022 level, EUR bn	2022	2023	2024	2025
Gross domestic product	13,492	3.4	0.5	0.5	1.8
Household consumption	7,063	4.2	0.5	1.1	1.7
Public consumption	2,899	1.6	0.1	0.7	1.5
Gross fixed investment	3,020	2.6	0.8	0.5	1.9
Stock building (changes as % of GDP)		0.3	-0.2	-0.1	0.0
Exports	7,436	7.2	-0.7	1.0	3.1
Imports	7,192	7.9	-1.2	1.6	2.9
Unemployment (%)		6.7	6.5	6.8	6.8
Consumer prices		8.4	5.4	1.3	1.2
Core CPI		3.9	4.9	2.3	2.3
Public sector financial balance. % av BNP		-3.6	-3.1	-2.7	-2.4
Public sector debt. % av BNP		90.9	89.6	88.5	87.2

Other major economies

Yearly change in per cent

		2022	2023	2024	2025
United Kingdom	GDP	4.3	0.5	0.2	1.4
	Unemployment	3.7	4.1	4.6	4.7
	Inflation	9.1	7.3	2.7	1.9
Japan	GDP	1.0	1.7	1.2	1.2
	Unemployment	2.5	2.6	2.5	2.4
	Inflation	2.5	3.2	2.1	1.3
Germany	GDP	1.8	-0.3	0.0	1.6
	Unemployment	3.1	3.0	3.5	3.5
	Inflation	8.7	6.0	1.4	1.4
France	GDP	2.5	0.8	0.6	1.6
	Unemployment	7.3	7.3	7.6	7.6
	Inflation	5.9	5.7	1.4	1.0

Emerging markets

Yearly change in per cent

		2022	2023	2024	2025
China	GDP	3.0	5.2	4.6	4.4
	Inflation	1.8	0.4	1.3	1.9
India	GDP	7.2	7.0	6.7	6.3
	Inflation	5.7	5.4	5.6	4.4
Brazil	GDP	2.9	3.0	1.8	2.0
	Inflation	5.8	4.6	4.1	3.8
Russia	GDP	-2.1	3.0	1.5	1.3
	Inflation	11.9	5.8	7.0	5.0
Poland	GDP	5.1	0.4	2.7	3.3
	Inflation	16.7	11.8	5.5	4.0

Financial forecasts

End of period

Official interest rates	18-Jan	Jun-24	Dec-24	Jun-25	Dec-25
US	5.50	5.00	4.00	3.50	3.00
Japan	-0.10	0.00	0.10	0.10	0.10
Euro area, deposit rate	4.00	3.50	3.00	2.50	2.00
United Kingdom	5.25	5.00	4.00	3.25	2.75

Bond yields. 10 year	18-Jan	Jun-24	Dec-24	Jun-25	Dec-25
US	4.14	3.80	3.70	3.65	3.60
Japan	0.61	0.82	0.93	0.94	0.95
Germany	2.31	2.10	2.00	2.00	2.00
United Kingdom	4.01	3.80	3.65	3.60	3.55

Exchange rates	18-Jan	Jun-24	Dec-24	Jun-25	Dec-25
USD/JPY	148	139	132	129	127
EUR/USD	1.09	1.12	1.14	1.16	1.18
EUR/JPY	161	156	150	149	150
EUR/GBP	0.86	0.91	0.93	0.95	0.97
GBP/USD	1.27	1.23	1.23	1.22	1.22

Sweden

Yearly change in per cent

	2022 level, SEK bn	2022	2023	2024	2025
Gross domestic product	5,985	2.6	-0.4	0.1	2.8
Gross domestic product. working day adjusted		2.7	-0.2	0.1	3.0
Household consumption	2,615	2.1	-2.6	1.4	3.2
Public consumption	1,485	0.0	2.3	0.4	0.8
Gross fixed investment	1,618	5.2	-2.0	-3.0	4.0
Stock building (changes as % of GDP)	78	1.0	-1.0	0.1	0.2
Exports	3,174	6.6	2.6	1.5	5.0
Imports	2,986	8.7	-1.1	1.6	5.6
Unemployment (%)		7.5	7.6	8.6	8.7
Employment		3.1	1.4	-0.8	0.2
Consumer prices		8.4	8.5	3.0	1.4
CPIF		7.7	6.0	1.9	1.9
CPIF ex. energy		5.9	7.5	2.4	2.0
Hourly wage increase		2.8	3.7	3.7	3.5
Household savings ratio (%)		13.0	13.6	13.2	12.9
Real disposable income		-0.3	-1.6	0.7	3.5
Current account. % of GDP		5.8	6.7	6.8	6.0
Budget balance, SEK bn		164	19	-103	-78
Public sector financial balance. % av BNP		1.3	-0.3	-2.2	-0.9
Public sector debt. % av BNP		32.8	31.4	33.0	33.5
Financial forecasts	18-Jan	Jun-24	Dec-24	Jun-25	Dec-25
Policy rate	4.00	3.50	3.00	2.25	2.25
3-month interest rate. STIBOR	4.08	3.55	3.05	2.30	2.30
10-year bond yield	2.28	2.35	2.30	2.40	2.40
10-year spread to Germany. Bps	-3	25	30	40	40
USD/SEK	10.49	9.96	9.61	9.35	9.11
EUR/SEK	11.39	11.15	10.95	10.85	10.75
KIX	125.5	125.0	123.0	120.4	120.5

Finland

Yearly change in per cent

	2022 level, EUR bn	2022	2023	2024	2025
Gross domestic product	268	1.6	-0.5	-0.2	2.0
Household consumption	138	1.5	-1.0	0.2	1.5
Public consumption	64	0.5	4.0	0.5	1.0
Gross fixed investment	71	3.1	-6.0	-1.8	4.0
Stock building (changes as % of GDP)		2.0	0.6	0.4	0.2
Exports	122	3.7	-1.0	0.0	4.0
Imports	128	8.5	-6.0	-0.5	3.0
Unemployment (%)		6.8	7.2	7.8	7.3
Consumer prices		7.2	4.3	1.5	1.5
Hourly wage increase		2.4	4.5	3.5	2.5
Current account. % of GDP		-2.5	-0.8	-1.0	0.0
Public sector financial balance. % av BNP		-0.8	-1.5	-2.5	-2.0
Public sector debt. % av BNP		73.3	75.0	76.5	78.0

Norway

Yearly change in per cent

	2022 level, NOK bn	2022	2023	2024	2025
Gross domestic product	5,705	3.0	0.5	2.1	1.6
Gross domestic product	3,643	3.8	0.9	0.5	1.4
Household consumption	1,816	6.2	-1.0	0.3	2.1
Public consumption	1,037	1.1	3.0	1.8	1.5
Gross fixed investment	1,124	5.2	-0.5	-2.0	0.1
Stock building (changes as % of GDP)	108	0.7	0.1	0.0	0.0
Exports	3,166	4.7	1.8	4.2	2.2
Imports	973	12.3	1.8	-0.5	1.7
Unemployment (%)		3.2	3.6	3.9	3.7
CPI		5.8	5.5	3.9	2.8
CPI-ATE		3.9	6.2	4.1	2.5
Annual wage increases		4.3	5.5	4.9	4.0
Financial forecasts	18-Jan	Jun-24	Dec-24	Jun-25	Dec-25
Deposit rate	4.50	4.50	4.00	3.50	3.00
10-year bond yield	3.59	3.50	3.25	3.25	3.15
10-year spread to Germany. Bps	128	140	125	125	115
USD/NOK	10.54	9.96	9.69	9.44	9.24
EUR/NOK	11.44	11.15	11.05	10.95	10.90

Denmark

Yearly change in per cent

	2022 level, DKK bn	2022	2023	2024	2025
Gross domestic product	2,832	2.8	1.0	1.5	3.0
Household consumption	1,225	-1.5	0.7	3.2	3.8
Public consumption	617	-2.8	0.0	0.7	0.8
Gross fixed investment	616	3.3	-3.0	6.8	6.1
Stock building (changes as % of GDP)	61	0.4	-1.4	-0.5	0.0
Exports	1,983	10.9	10.9	7.1	4.1
Imports	1,668	6.5	8.9	10.3	4.9
Unemployment (%)		4.8	4.8	4.4	3.6
Consumer prices		7.7	3.3	1.0	1.6
Hourly wage increase		2.6	3.0	3.3	4.0
Current account. % of GDP		13.3	10.0	9.0	8.0
Public sector financial balance. % av BNP		3.4	3.5	3.5	4.0
Public sector debt. % av BNP		30.1	30.0	29.0	27.0
Financial forecasts	18-Jan	Jun-24	Dec-24	Jun-25	Dec-25
Deposit rate	3.60	3.10	2.60	2.10	1.60
10-year bond yield	2.48	2.25	2.15	2.15	2.15
10-year spread to Germany. Bps	17	15	15	15	15
USD/DKK	6.87	6.65	6.54	6.42	6.31
EUR/DKK	7.46	7.45	7.45	7.45	7.45

Lithuania

Yearly change in per cent

	2022 level, EUR bn	2022	2023	2024	2025
Gross domestic product	67	2.4	-0.2	1.5	2.8
Household consumption	39	2.0	-1.6	2.8	3.2
Public consumption	11	0.4	0.4	0.2	0.0
Gross fixed investment	14	3.6	9.0	2.5	5.0
Exports	59	12.2	-5.2	1.0	4.0
Imports	60	12.4	-3.5	2.0	4.7
Unemployment (%)		5.9	6.6	6.8	6.5
Consumer prices		18.9	8.7	2.0	2.7
Wages and salaries		13.3	12.4	8.5	7.0
Public sector financial balance. % av BNP		-0.7	-0.6	-2.5	-1.8
Public sector debt. % av BNP		38.1	38.2	40.0	42.5

Latvia

Yearly change in per cent

	2022 level, EUR bn	2022	2023	2024	2025
Gross domestic product	39	3.4	-0.4	2.0	2.7
Household consumption	23	6.2	-1.5	1.6	2.2
Public consumption	7	2.8	6.7	4.1	2.7
Gross fixed investment	8	0.6	6.9	5.6	3.7
Exports	28	10.3	-6.2	2.4	3.2
Imports	30	11.1	-2.7	1.5	2.0
Unemployment (%)		6.9	6.5	6.5	6.4
Consumer prices		17.2	9.0	1.4	2.4
Wages and salaries		7.5	11.5	8.2	7.7
Public sector financial balance. % av BNP		-4.6	-2.6	-2.8	-2.5
Public sector debt. % av BNP		41.0	39.7	41.0	40.2

Estonia

Yearly change in per cent

	2022 level, EUR bn	2022	2023	2024	2025
Gross domestic product	36	-0.5	-3.4	-0.5	3.5
Household consumption	19	2.0	-1.8	0.0	3.0
Public consumption	7	0.1	0.5	2.0	1.0
Gross fixed investment	10	-3.7	-6.5	-2.0	5.0
Exports	31	3.0	-8.0	-1.0	5.0
Imports	31	3.2	-6.5	-1.5	4.0
Unemployment (%)		5.5	6.7	8.7	7.5
Consumer prices		19.4	9.1	3.8	2.5
Wages and salaries		11.6	11.2	6.5	6.0
Public sector financial balance. % av BNP		-0.9	-2.0	-3.5	-3.0
Public sector debt. % av BNP		18.4	19.0	22.0	23.5

Jens Magnusson
Chief Economist
+ 46 70 210 22 67

Daniel Bergvall
Head of Economic Forecasting
+46 73 523 52 87

Karl Steiner
Head of Analysis
+46 70 332 31 04

Robert Bergqvist
Theme: A new world order
Japan
+46 70 445 14 04

Erica Dalstø
SEB Oslo
Norway
+47 2282 7277

Pia Fromlet
Theme: Germany
Euro area
+46 70 739 32 66

Dainis Gaspuitis
SEB Riga
Latvia
+371 67779994

Jussi Hiljanen
Fixed income
+46 8 506 231 67

Olle Holmgren
Theme: Inflation risks
Sweden
+46 70 763 80 79

Marcus Johansson
Theme: A new world order
+46 70 739 16 04

Cecilia Kohonen
Communication Manager
+46 70 763 79 95

Elisabet Kopelman
Theme: A fateful US election
United States
+ 46 70 655 30 17

Elizabeth Mathiesen
SEB Copenhagen
Denmark
+45 285 517 47

Erik Meyersson
China,
Emerging markets
+46 70 739 16 83

Mihkel Nestor
SEB Tallinn
Finland, Estonia
+372 6655172

Tadas Povilauskas
SEB Vilnius
Lithuania
+370 68646476

Amanda Sundström
United Kingdom
+46 70 445 14 04

Thomas Thygesen
SEB Copenhagen
Denmark, Equity market
+45 2147 9656

Marcus Widén
Theme: Inflation risks
Macro forecasting
+46 70 639 10 57

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