SEK Views

Dovish Riksbank fully discounted

WEDNESDAY
15 APRIL 2015

EDITOR
Carl Hammer
+ 46 8 506 23128

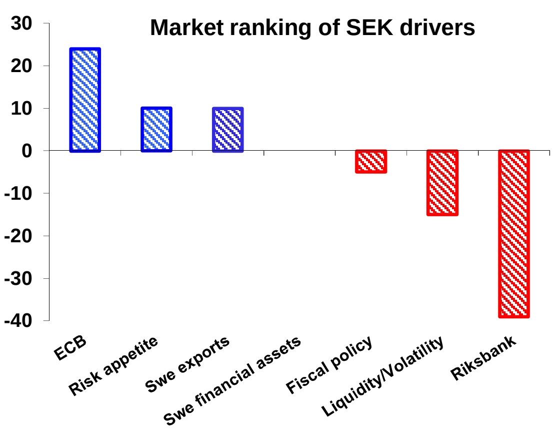
FX Survey and SEK outlook: "Riksbank krona message noted!" Our survey of leading SEK trading corporates and institutions suggests that while the market regards the Riksbank as a very krona hostile central bank, it has adapted itself to the situation. Market SEK-positioning remains short with 90% of respondents expecting further easing from the Swedish central bank and FX interventions if EUR/SEK breaches 9.00 near-term. Our conclusion is therefore that unless the Riksbank acts on these elevated and dovish expectations, it is all but certain the krona will appreciate testing the patience of a central bank already stressed by the challenge of defending its inflation target. Fulfilling those expectations also seems to be one of very few arguments why it should ease monetary policy further. We target EUR/SEK at 9.00 year-end 2015 as underlying fundamentals are krona positive. Fed rate hikes in H2 2015 will enable Riksbank also to lower its guard against too strong a SEK.

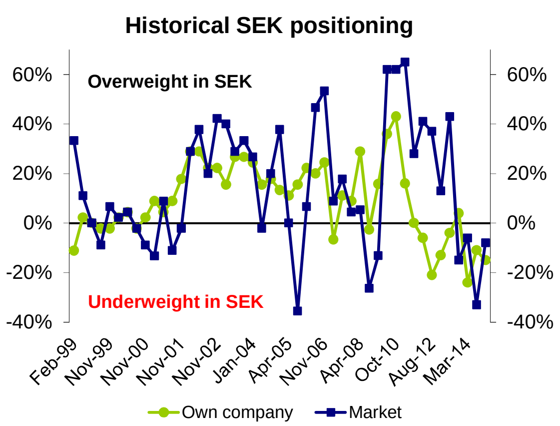
Swedish macro and Riksbank outlook: Forced to act again. Despite slight upward revisions to the forecasts for both inflation and growth we think that the Riksbank will deliver a 15bps rate cut at the April 28-29 meeting and also increase the bond purchases by another SEK 50bn. Market expectations for more measures from the Riksbank are high and a failure to deliver will lead to unwanted strengthening of the krona, which now is the main instrument for the Riksbank to fulfill the inflation target.

Fixed income recommendations: Driven by another rate cut and an extension to the Riksbank's QE program, we expect the Swedish government yields to decline and the curve to flatten. We recommend to buy SGB1058 (2025) outright. Expecting the long end to trade flat vs. Germany within a few months, we find great value in SGB1054 (2022) vs. Germany. Finally, we suggest buying 2019 covered bonds vs. the government.

Swedish equity market: OMX target remains at 1785: Our target set on 8 Feb 2015 assumed continued profit revisions in line with the negative trend experienced in recent years. We also concluded that if risk compensation was to be normalized, adjusting for lower long run rate equilibrium, stocks would on average need to be valued 30% higher. Swedish stocks currently trade at a 12-month forward looking PER of 18.0x, a 37% premium to its 10-year historical average.

FX trading recommendations: Buy USD/SEK for 9.40 as the on-going USD appreciation trend continues. Sell NOK/SEK at 1.11 (stop above 1.12) targeting 1.07. Sell EUR/SEK at 9.40 targeting 9.00.





Forecasts

CENTRAL BANKS

	EMU	US	UK	SWEDEN	NORWAY
Current target rate	**0.05%**	**0.00-0.25%**	**0.50%**	**-0.25%**	**1.25%**
Apr-15	Unch	Unch	Unch	**-0.40%**	
May-15	---	---	Unch	---	**Unch**
Jun-15	Unch	Unch	Unch	---	**1.00%**
Jul-14	Unch	Unch	Unch	Unch	---
Aug-15	---	---	Unch	---	---
Sep-15	Unch	+25 bps	Unch	Unch	Unch
Oct-15	Unch	Unch	Unch	Unch	Unch
Nov-15		---	Unch	---	---
Dec-15	Unch	+25 bps	Unch	Unch	Unch
End-15	**0.05%**	**0.75%**	**0.50%**	**-0.40%**	**1.00%**
End-16	**0.05%**	**1.75%**	**1.25%**	**0.00%**	**1.25%**

CONTENT

CONTACTS

Carl Hammer, Head of FX Research (Editor)
Jussi Hiljanen, Head of Fixed Income Research
Arvid Böhm, Chief Equity Strategist
Olle Holmgren, Senior Macro Strategist
Richard Falkenhäll, Senior FX Strategist
Karl Steiner, Chief FX Quant Strategist
Dag Muller, Technical Strategist

FX FORECASTS

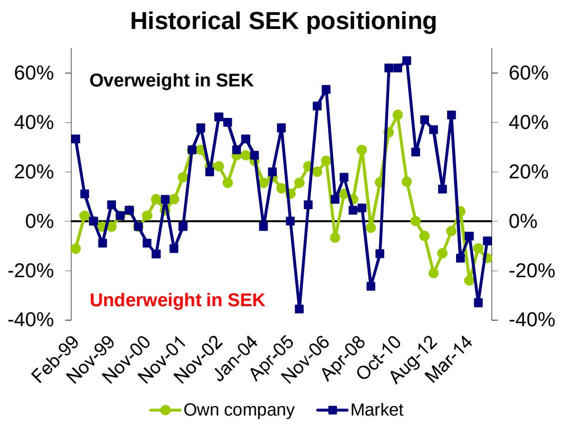
		FORECASTS					ACTION LEVELS	
FX	***14/04/2015***	**1M**	**Q2 15**	**Q3 15**	**Q4 15**	**Q1 16**	**Buy**	**Sell**
EUR/USD	*1.067*	1.07	1.05	1.00	0.95	0.96	0.95	1.10
EUR/SEK	*9.328*	9.35	9.35	9.20	9.00	8.90	9.00	9.40
EUR/NOK	*8.46*	8.45	8.75	8.55	8.35	8.30	8.40	8.90
EUR/CHF	*1.037*	1.04	1.04	1.07	1.08	1.10	1.00	1.10
USD/JPY	*119.4*	120	122	125	128	130	118.0	-
USD/CAD	*1.25*	1.27	1.30	1.32	1.30	1.29	1.24	1.32
GBP/USD	*1.477*	1.44	1.42	1.40	1.41	1.44	1.41	1.50
USD/CNY	*6.212*	6.25	6.35	6.25	6.20	6.25	-	-
Cross rates	***14/04/2015***	**1M**	**Q2 15**	**Q3 15**	**Q4 15**	**Q1 16**	**Buy**	**Sell**
EUR/SEK	*9.328*	9.35	9.35	9.20	9.00	8.90	9.00	9.40
USD/SEK	*8.744*	8.74	8.90	9.20	9.47	9.27	8.32	9.40
GBP/SEK	*12.914*	12.62	12.64	12.88	13.36	13.35	12.65	13.30
NOK/SEK	*1.10*	1.11	1.07	1.08	1.08	1.07	1.04	1.11
JPY/SEK	*7.32*	7.28	7.30	7.36	7.40	7.13	-	7.40
CAD/SEK	*7.00*	6.88	6.85	6.97	7.29	7.19	-	7.20
AUD/SEK	*6.67*	6.55	6.50	6.62	6.63	6.49	-	-
CNY/SEK	*1.41*	*1.40*	*1.40*	*1.47*	*1.53*	*1.48*	-	-
CHF/SEK	*9.00*	8.99	8.99	8.60	8.33	8.09	-	9.00

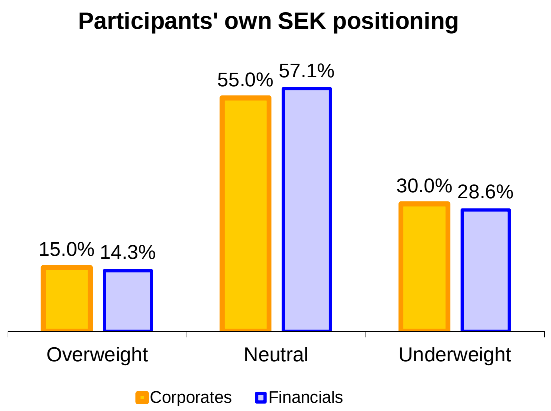
***NOK Forecasts are subject to revision on Apr 16th when SEB releases *NOK Views*.**

FX survey & SEK outlook

Our survey of major companies and institutions again confirms that the market is positioned (net short -15%) for a weak Swedish krona. With the exchange rate level also the most important policy variable for the Riksbank, the market is convinced Swedish monetary policy will be eased even further. Consequently, despite the weak macroeconomic arguments for additional stimulus measures, the Riksbank will likely be forced to announce them as the SEK is certain to appreciate otherwise.

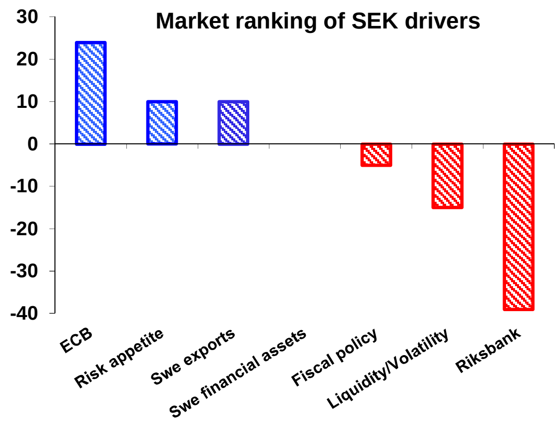
Since 1999 SEB has polled the major traders of large Swedish companies/institutions and selected foreign hedge funds concerning their outlook for the SEK. Survey participants have declared an underweight (net short) position in SEK since early 2012. This time there is little difference in SEK positioning between corporates (-15%) and institutions (-14%). The perception of overall market positioning is also similar to that of its participants.



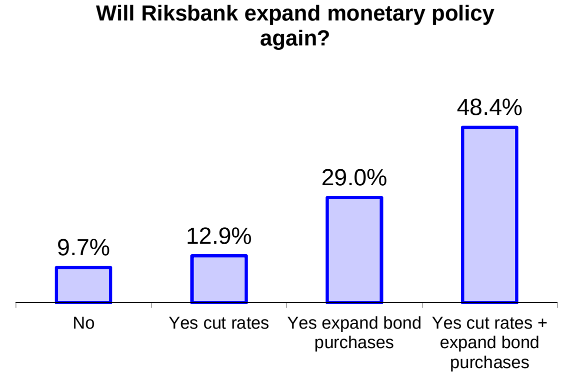


CONCLUSION ON POSITIONING: It is somewhat surprising given overall trade-weighted krona weakness that participants (particularly institutions) have not reduced their short SEK position. Dovish Riksbank expectations probably explain why the market remains short. Positioning confirms our own SEK flow data showing that the market overall still anticipates a weaker krona.

MARKET DRIVERS FOR SEK: ALL ABOUT MONETARY POLICY. To nobody's surprise probably respondents' ranking of krona drivers confirms that the foreign exchange market is dominated by expectations surrounding the activities of the central bank. As in our last SEK Views report, ECB policy (Oct-14: +16) is deemed the most positive factor for the SEK. However back then this was regarded as the only positive driver, with all others seen as negative for the SEK. Also as then, the Riksbank remains the SEK's worst enemy although the scale of negative expectations regarding the Swedish central bank has moved from -18 to -39. Meanwhile, some 71% of respondents believe the Riksbank cannot continue over time to expand monetary policy as aggressively as the ECB has stated it intends to do (i.e. there is limited potential for bond purchases in Sweden). **Hence there is significant scope to disappoint on the already very dovish Riksbank expectations.**

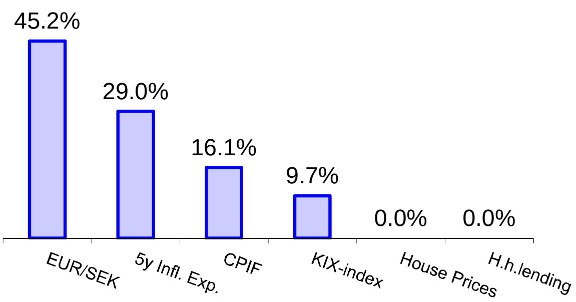


These dovish expectations are also confirmed by respondents when asked if they thought further easing would take place: only one in 10 expects the Riksbank to remain on hold from now on. Currently, the interest rate market prices another 6 bps repo rate cut – apparently expectations are higher than market pricing suggests. One reason of course might be that pricing of additional bond purchases (as likely as a repo rate cut in our opinion) is harder to estimate in market pricing (compared to the RIBA/FRA market).



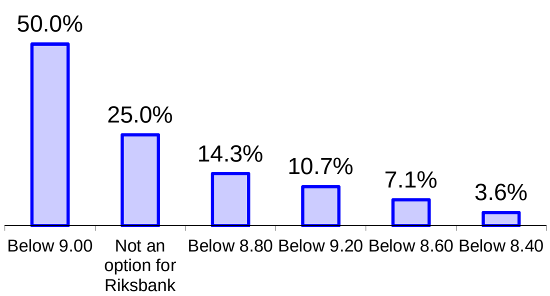
A CIRCULAR REFERENCE NOTED... The Riksbank is stated to be the most important (and negative) factor for the SEK. However, recently the krona has also become the most important short-term variable for the Swedish central bank to consider when determining future monetary policy. Some 55% of survey respondents said EUR/SEK (and the KIX-index) is the most significant consideration for the Riksbank. Clearly, the central bank is thought to be leaving financial stability concerns to others to worry about, as no one thought house prices or growth in household lending to be the most important policy variable currently.

Most important Riksbank policy variable?



... WITH 9.00 THE LEVEL TO WATCH. Considering further the krona's importance we asked at what level if any participants thought the Riksbank would consider actually intervening in the FX market to keep the SEK from appreciating (Question: "At what EUR/SEK level do you think the Riksbank will intervene in the FX market by selling SEK"?). When previously asked this question the market (as we did) thought that at a EUR/SEK rate between 8.00-8.50 the SEK would be sufficiently strong to cause the Riksbank to act. Recent verbal interventions by the Swedish central bank in the context of a global currency war have clearly lowered the Riksbank's tolerance level regarding SEK appreciation. Further, the market has also adopted this view as over 60% of respondents expect actual FX interventions if EUR/SEK breaches and trades below 9.00.

Riksbank to intervene in the FX market?



CONCLUSION ON SEK DRIVERS: Predictably, the exchange rate is closely connected with the Riksbank policy outlook. According to the results of this our most recent survey, Riksbank threats (i.e. verbal interventions) are thought credible by market participants who: 1) regard the Swedish central bank's policy as very SEK negative; 2) expect further easing by the Riksbank; and 3) believe the bank will take action in the FX market if the EUR/SEK falls below 9.00.

STRONGER SEK EXPECTED WITH FLAT EUR/USD. In-line with consensus expectations survey participants collectively expect a further, albeit very small, krona appreciation vs. the EUR. Meanwhile, two out of three survey participants regard the present trade-weighted SEK exchange rate as too low, i.e. the currency is undervalued. The implied EUR/USD forecast is flat.

	EUR/SEK		USD/SEK	
	Jun-15	Dec-15	Jun-15	Dec-15
Median	**9.30**	**9.15**	**8.85**	**8.80**
High	9.70	10.00	10.00	10.11
Low	8.90	8.80	6.50	6.80

Average during survey EUR/SEK 9.35, USD/SEK 8.65

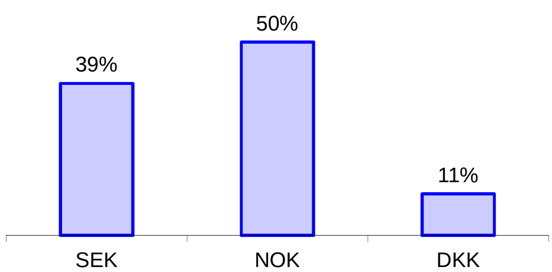
Implied EUR/USD fc: 1.05 and 1.04

Respondents have a fairly optimistic view on future rate hikes from the Federal Reserve: 70% expect the Fed to raise its policy rate in either Sep-16 or Oct-16. Meanwhile, the ECB policy outlook appears credible although a small net percentage (10%) expects the bank to taper its purchases before completing its current stated policy (EUR 1.1trn to Sep-16).

As usual, the most important currency for survey participants is the USD (despite 70% of Swedish exports going to Europe). Some 70% of corporate respondents also state that so far the weaker SEK has not affected their pricing.

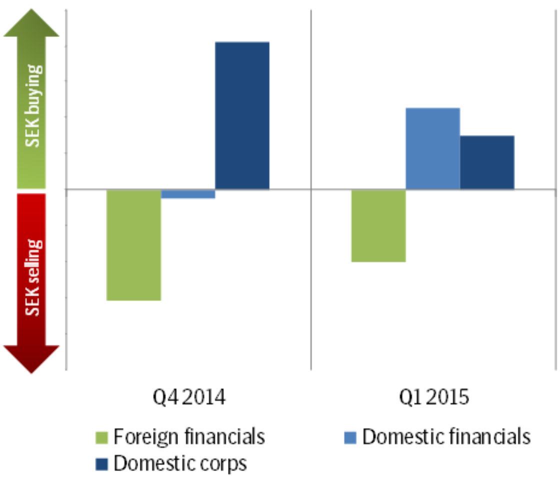
NOK ALMOST CHALLENGED BY SEK. In recent years NOK/SEK has established a trading range between 1.04 and 1.12. At the current spot rate (during the survey period) of 1.07 it is hardly surprising that the NOK is preferred to the SEK. While we agree in the very short-term, we eventually expect the low oil price to weigh on the NOK targeting levels back towards 1.05 over the next 6-12 months.

Which Scandinavian currency will outperform the others?



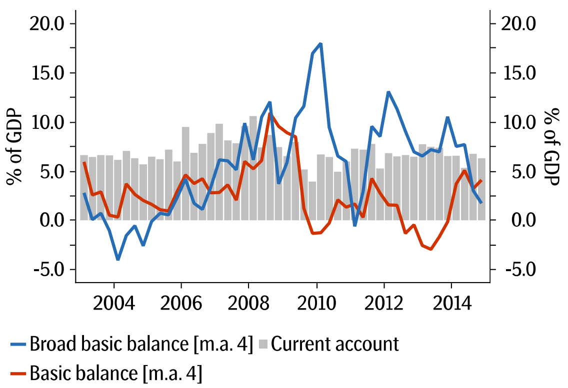
SEB FX RESEARCH: FLOWS WILL ULTIMATELY BE SEK SUPPORTIVE. We agree with survey participants that the SEK is currently undervalued and that inevitably it will appreciate in H2 2015. As we have written on several occasions **our proprietary SEB SEK flows still show the speculative market to be using SEK as a funding currency** (see charts below). Although Swedish corporates bought significant amounts of krona in Q4 2014 (a partly seasonal pattern), there has been **no significant change in current FX hedging policy** which has been kept to a bare minimum" (meaning hedge ratios and durations are kept low). **The collapse in EUR/SEK in late February and early March was primarily driven by rebalancing flows from domestic financial institutions.** These were probably not the result of an active decision but rather passive rebalancing flows. Local corporates/ institutions and foreign institutions are geared for a weak(er) SEK. **Positioning will ultimately provide the SEK with a tail-wind (which would be hard to prevent given present strong underlying fundamentals and the currency's attractive valuation).**

Net SEB SEK flows (vs. EUR)



Long-term portfolio flows were previously positive for the SEK given the increasing share of foreign ownership of government bonds and equities. In recent years however, that ratio has remained stable between 45-50% as **foreign real money and central banks take a more neutral interest in Swedish financial assets.**

Sweden, Current account balance & portfolio flows



The composition of the country's current account is also changing: the trade surplus is falling slowly while the still high current account surplus is sustained by increasingly positive net income flows (which are likely to be partly reversed if/when Swedish interest rates rise again). Going forward the (falling) current account surplus is SEK supportive but 50% is kept abroad (as reinvested earnings) arguing for a very modest positive effect on the short- to medium-term SEK outlook.

SO WHERE IS SEK HEADING NOW? SEB FX research expects/has expected the trade-weighted SEK to bottom out in early 2015 because the Riksbank cannot keep pace with the scale of monetary expansion to which the ECB has committed itself (i.e. balance sheet expansion at over 10% of GDP until Sep-16 at least). From a macroeconomic perspective, it is hard to argue that Sweden, with its strong GDP growth and rapidly rising asset prices, needs further non-conventional easing of its monetary policy. However, low inflation persists, while inflation expectations are still significantly below target. Most likely, the Riksbank remains determined to do all it can to ensure CPIF moves back towards its target. Therefore, when evaluating the SEK's prospects it is monetary policy that still provides the head-wind. With FX markets in the hands of policymakers, the ultimate question concerns when the Riksbank will regard inflation as sufficiently high to take a more relaxed position on the exchange rate. We forecast CPIF will continue slightly higher in coming months: **a CPIF rate at or above 1.5% y/y should probably ensure a slightly more relaxed Riksbank attitude.**

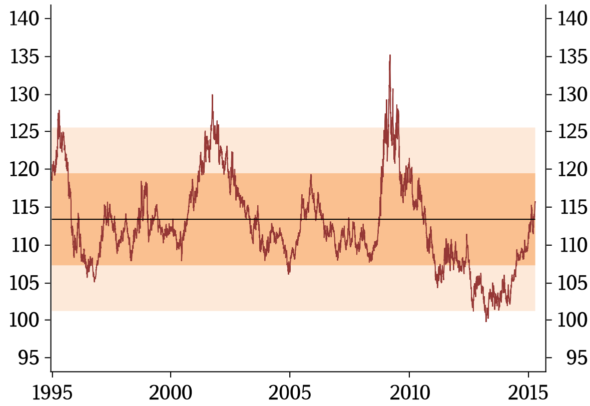
We expect EUR/SEK to continue to range-trade as we anticipate further easing on 29 Apr. Ultimately however: 1) strong fundamentals, 2) an attractive valuation, 3) short speculative market positioning, and 4) supportive flows will inevitably cause the SEK to appreciate to 9.00 and below vs. the EUR. 5) Fed rate hikes in H2 2015 and potentially lower asset purchases by the ECB will also facilitate the task for the Riksbank. We target EUR/SEK at 9.00 in Dec-15.

TECHNICAL OUTLOOK KIX-INDEX:
The medium-term SEK-bearish wave-count remains in play and still looks productive. With support reconfirmed at a 2012 peak that was recently re-tested, extension towards a 2009-13 50% retracement ref at 117.50 seems likely. But to complete the ongoing five-wave sequence in full, we doubt 117.50 is sufficient. Medium-term Fibo-refs at 121.70/80-123.30 are in play as a preferred objective for the move.

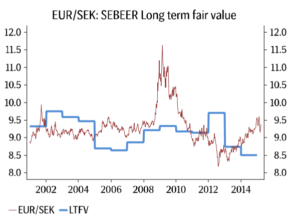
Undervalued krona remains under pressure from Riksbank policy – EUR/SEK at 9.35 in Q2.

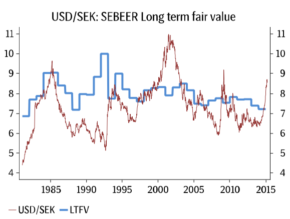
Compared to a year ago the krona has weakened by more than 9% in trade-weighted terms (KIX-index). This reflects the local currency's depreciation due to further easing of monetary policy by the Riksbank and the generally stronger US dollar. In trade-weighted terms (KIX-index) the krona now trades very close to its historical average, suggesting the previously overvalued currency may have returned to a more sustainable level closer to its fair value.

SEK KIX-index



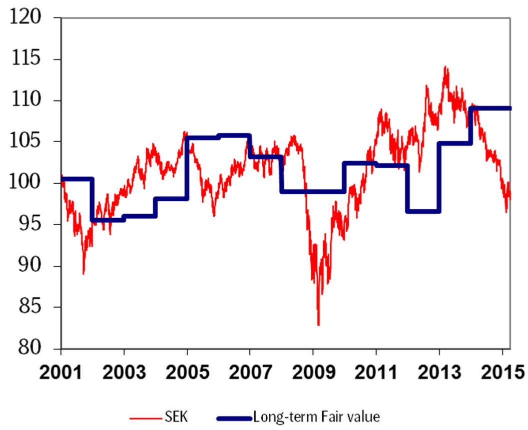
However, this view represents only one estimate of the krona's long-term fair value. The empirical SEBEER long-term fair value model takes a slightly different approach, being based on the exchange rates of 28 currencies against the US dollar since 1980. In the SEBEER model the long-term fair value is determined using four different factors: relative inflation; relative productivity growth; relative long-term interest rates; and relative terms of trade. According to this model the krona's current long-term fair value against the US dollar is 7.20 and 8.50 against the euro. **Trading at 8.62 against the US dollar and 9.37 against the euro this indicates that, from a long-term perspective, the krona is currently undervalued.**





To obtain a broader understanding of the krona's valuation we have calculated a trade-weighted index for the currency based on SEBEER model estimates against its most important trading partners. The outcome suggests **that the krona is approximately 10% undervalued in trade-weighted terms**, due to the combination of an increased long-term fair value estimate in recent years and a weaker spot exchange rate.

SEBEER Long-term Fair value, SEK Index



RELATIVE REAL INTEREST RATES AND INFLATION EXPLAIN MUCH OF THE VARIATION IN SEK LONG-TERM FAIR VALUE. The long-term fair value of the krona has increased substantially in recent years after falling temporarily in 2012. What explains this substantial variation in the trade-weighted long-term fair value of the krona since 2012? To find out we consider the model's explanatory variables and the ways in which they have changed over the years. Apparently, **a large share of the alterations in the krona's long-term fair value is due to fluctuations in relative real interest rates and inflation, particularly compared to the euro which accounts for over 50% of the trade-weighted krona index.**

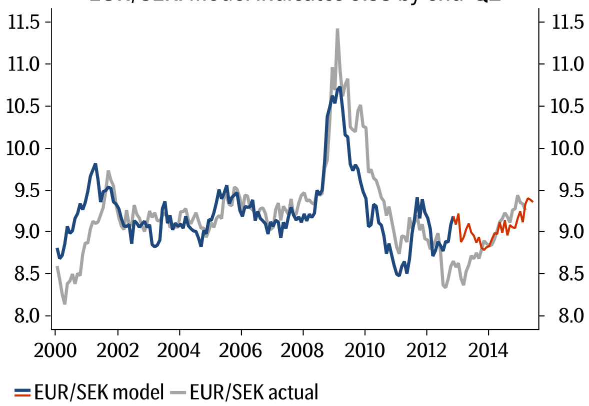
In 2012, the euro's long-term fair value increased temporarily against both the krona and US dollar. This was because USD and SEK real interest rates fell substantially and became negative, while that of the euro remained largely stable. In 2013 however, this situation changed with the euro's real interest rate also decreasing. Additionally, the real interest rate for the krona actually increased again, which altogether almost fully eliminated the real interest rate differential between the euro and krona that year. The krona's long-term fair value has also been supported by lower Swedish inflation than in the US and euro zone. From a valuation perspective low inflation is positive for the long-term fair value of a currency. This is also the case for the SEBEER model, a position fully consistent with the theory of relative purchasing parity and the law of one price, which suggests that exchange rates should compensate for differences in price changes over the long-run.

RIKSBANK POLICY TO MAINTAIN PRESSURE ON SEK. In addition to its long-term fair value variations in the EUR/SEK exchange rate may be largely explained using a

fairly simple model that considers only a very few fundamental factors such as general risk appetite, relative 2y interest rates between Sweden and Germany, and Swedish manufacturing production. The only period when this type of model lost much of its predictive power was at the height of the euro zone crisis when it indicated that EUR/SEK should trade substantially higher than the actual market price. This was, however, a consequence of increasing capital inflows as Sweden temporarily became a safe haven for capital during the worst of the euro zone crisis. However, since the beginning of 2014 the relationship between the model and the EUR/SEK spot rate appears to have been re-established.

Based on actual data at the end of March, the model suggests the EUR/SEK's current fair value is approximately 9.35, i.e. near its current level. Much of the SEK's weakness reflects further easing of monetary policy by the Riksbank and the use of a weak currency as a policy tool to raise inflation expectations.

EUR/SEK: Model indicates 9.35 by end-Q2



Although our model uses both general risk appetite (VIX-index) and manufacturing confidence to reflect the impact of the business cycle, these two factors have changed too little since the beginning of 2014 to explain why the model now indicates a weaker krona. Instead further rate cuts by the Riksbank and government bond purchases have lowered the Swedish 2y government bond yield from 1.1% at the beginning of 2014 to -0.3% currently. Moreover, this has reduced the 2y swap rate differential between Sweden and Germany, a model component, from 0.70% at the beginning of 2014 to -0.14% at the end of March this year. This provides an important explanation as to why the model has continued to indicate a higher EUR/SEK.

Although the Riksbank has come a long way in easing Swedish monetary policy, we expect further measures. Indeed, **we anticipate another rate cut at its April meeting to -0.4% and a further SEK 50bn increase in asset purchases.** These moves should exert more downside pressure on Swedish 2y interest rates such that **we forecast the spread between Swedish and German 2y swap rates will continue to widen to -0.3%.** This will ensure the krona will remain under pressure to depreciate against the euro over the near-term. **If we incorporate this monetary policy assumption into our EUR/SEK model, and also assume that manufacturing confidence recovers slightly and that risk appetite improves, this would indicate that the krona should trade around 9.35-9.40 against the euro by end of Q2.**

Riksbank outlook: forced to act again

We expect the Riksbank to cut the repo rate by 15bps to -0.40% in April and also increase asset purchases by SEK 50bn. The spectrum of possible outcomes is however wide and we have derived three risk scenarios, two of which assume an unchanged repo rate in April. The probability of a rate cut is assessed at 70%, though this includes some risk of a larger 25bps reduction. The probability of increased QE is higher (80%), although there is considerable uncertainty regarding the scale of such measures. Forecasts for both inflation and growth are likely to be revised upward. Fear of a stronger exchange rate continues to be the most important driver for policy measures.

MORE MEASURES FROM THE RIKSBANK. Although the Riksbank is likely to revise its forecasts for both inflation and growth upwards, we expect the board to deliver a 15bps rate cut in its Apr 29 *Monetary Policy Update* and expand its asset purchase program by a further SEK 50bn. With both actual inflation and inflation expectations increasing and the krona relatively weak, the outlook for the April rate decision is not clear. Still, given the central bank's strong commitment to bring inflation back on target, we think the board will wish to avoid disappointing markets, which most likely would cause unwanted strengthening of the krona.

Given the uncertainty regarding the size of the rate cut and also the scale and composition of possible QE measures, the spectrum of possible outcomes for the April rate decision is wide and complex. Below we describe four different scenarios that we believe cover the most probable outcomes. However, we do not claim to have covered all possibilities.

Main scenario (50% probability): Repo rate is cut by 15bps and bond purchases increased by SEK 50bn.

Dovish risk scenario (20% probability): Repo rate is cut by 25bps and bond purchases increased by SEK 70bn.

Hawkish risk scenario 1 (15% probability): Unchanged repo rate, but bond purchases increased by SEK 30bn.

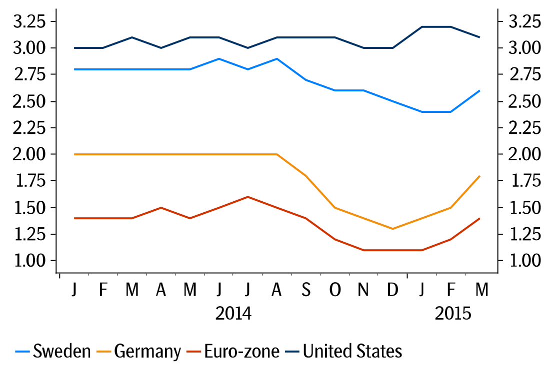
Hawkish risk scenario 2 (15% probability): Unchanged repo rate and no new bond purchases.

The board has already announced that the repo rate path will be lowered. Since the Riksbank did not publish a new rate path after the inter-meeting rate reduction in March, it is certain there will be a downward revision on Apr 29 compared to the February path. In its press release following the inter-meeting rate cut to -0.25%, the Riksbank stated that it was the pace of rate hikes rather than the timing of the first hike that would be revised. According to the March press release, the repo rate is expected to remain at its current level at least until the second half of next year, similar to the wording in the February press release, which said that a rate hike was expected during the second half of 2016. According to the February repo rate path, the first repo rate hike was indicated in September or October next year. We expect the board to delay the first hike to October or December, but make a larger revision to the path in 2017 reducing the path by 0.6-0.7%-points. Further, after such a substantial revision the Riksbank repo rate path would remain well above market expectations.

Several economic indicators will be presented ahead of the Apr 29 rate decision, but unemployment (due on Apr 21) is the only indicator that could potentially influence our conclusions. Monthly readings for the trade balance, PPI and retail sales (presented on Apr 28) normally do not have any implications for near term monetary policy.

HIGHER INFLATION AND GDP. Growth was significantly stronger in Q4 last year, with GDP increasing by 1.1%, 2.7% y/y, 0.5-1.0%-points higher than the Riksbank's own estimate (0.5%, 1.5% y/y). However, short-term indicators have been mixed with e.g. NIER business sentiment falling back over the last two months. Also, the central bank is likely to make some downward adjustments to its international growth estimates, mainly due to slower GDP increases in the US. We believe large components of the strong increase in Q4 growth will be regarded as reflecting temporary volatility, and expect the Riksbank to adjust its 2015 growth projection to 3.0%, in line with our own forecast.

Consensus GDP forecasts for 2015



Labour market developments remain mixed compared to the Riksbank's projections with unemployment still sticky as a result of increasing labour force participation. At the same time employment is proving surprisingly strong. Short-term indicators imply that these trends will continue going forward. Consequently, we expect the Riksbank to adjust its forecasts accordingly.

CPIF inflation is likely to be revised higher both this year and next, although drivers are likely to be seen as temporary. CPIF in April was 0.1%-points above the Riksbank's estimate, driven mainly by higher gasoline prices. We think this will lead to an upward revision of the forecast also later this year. The estimate for 2016 will be raised slightly due to announced tax hikes on petrol and own home repairs, which will add 0.3-0.4%-points to CP in January next year. Probably the Riksbank has already included some tax hikes in its estimates, so we think the upward revision will be smaller than the contribution from the new taxes.

MAJOR REVISION OF THE EXCHANGE RATE FORECAST. Furthermore, we believe the Riksbank may remove major components of its forecast for krona appreciation, core considerations the central bank has taken into account in devising estimates for almost 20 years. This move would emphasise that the board regards keeping the exchange rate weak as an important tool in helping it reach its inflation target.

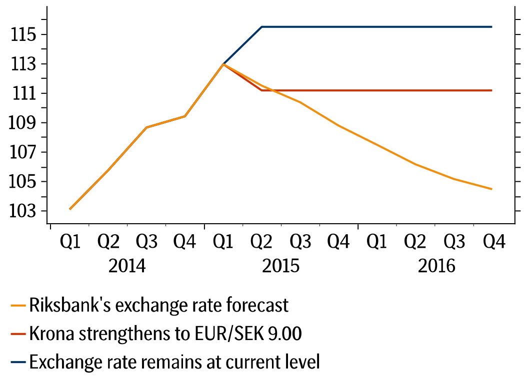
If our assessment that the Riksbank will project a significantly weaker krona is correct there could be reason to make a larger upward adjustment of its inflation forecast. However, we doubt that the current prediction of a stronger krona is fully incorporated in the inflation forecast and think that the Riksbank will make only a minor upward adjustment to its inflation projections for this reason.

What we expect the Riksbank to forecast on April 29

	Riksbank expected	Riksbank forecast in Feb
CPI 15	0.2	0.1
CPI 16	1.3	1.9
CPI 17	2.7	3.3
CPIF 15	1.0	0.9
CPIF 16	2.1	2.0
CPIF 17	2.2	2.2
GDP 15	3.0	2.7
GDP 16	3.2	3.3
GDP 17	2.2	2.2
Unemploym. 15	7.7	7.6
Unemploym. 16	7.3	7.1
Unemploym. 17	6.9	6.7
Employment 15	1.4	1.3
Employment 16	1.4	1.2
Employment 17	1.0	0.9
Wages 15	2.9	2.9
Wages 16	3.4	3.4
Wages 17	3.5	3.5
KIX 2015	114,0	110.7
KIX 2016	112.0	105.8
KIX 2017	110.0	103.6
Int. GDP 15	1.9	2.0
Int. GDP 16	2.3	2.4
Int. GDP 17	2.6	2.6

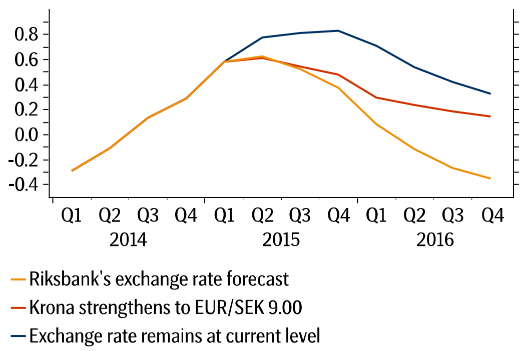
EXCHANGE RATE CONTINUES TO BE MOST IMPORTANT MONETARY POLICY DRIVER. We have previously concluded that the board sees the krona as the main instrument that, within a reasonable period, can bring inflation back on target. (see *Central Bank Insights* from 2014-03-03). The fact that the SEK currency index has weakened by around 2-3% since the February rate decision is most likely welcomed by the Riksbank board. As shown in the chart below, upward pressure on CPIF from the weaker exchange rate will continue to build during most of this year and also boost inflation next year.

Sweden: Exchange rate index (KIX) in different scenarios



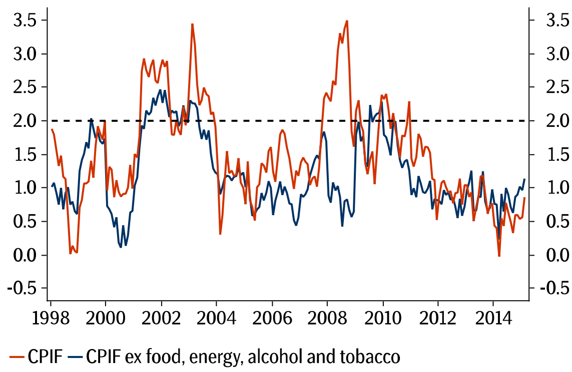
Still, upward pressure on CPIF from the krona depreciation would peak towards the end of this year and gradually decline in 2016. In our view this suggests that the board would probably be pleased if the krona weakened even further. If the Riksbank fails to deliver new policy measures in April, we estimate that the krona would strengthen to EUR/SEK 9.00. In such a scenario, CPI would be 0.4%-points lower at the end of this year and 0.2%-points lower at the end of next year, according to our models. To illustrate, we have also included the marginal impact on CPI, assuming the Riksbank's exchange rate forecast is correct. **The central bank estimates CPIF at the end of 2016 at 2.2%, which means that other inflation drivers (excluding the exchange rate) at the end of next year would need to be almost unrealistically high. This supports our conclusion that the exchange rate forecast is inconsistent with the CPIF estimate.**

Sweden: Marginal impact on inflation from krona in different exchange rate scenarios, %-points y/y



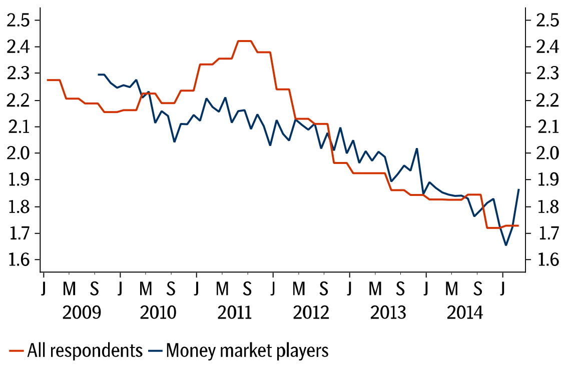
WHEN WILL THE EASENING CYCLE END? With inflation rising from lows in 2012-14 and growth above trend we expect the monetary policy easing cycle to end sometime during the second half of this year. There are, however two caveats to this assessment, which mean that the risk to our forecast remains biased towards the introduction of further measures, making it hard to forecast an end to the tightening cycle with much conviction.

Sweden: CPIF and core CPIF, % y/y



The first is the fact that inflation over the last 20 years has trended below target, with CPIF above 2% only during periods of rising food and energy commodity prices, and most often also a significantly weaker krona. **Furthermore, periods of high inflation have been connected with long downward trends in unemployment and faster wage growth.** The weaker exchange rate and tax hikes are important drivers for our estimate of higher inflation going forward, with most of this likely to have a transitory impact on the inflation rate. The low historical trend and the absence of decisive inflation drivers are likely to be the reason why inflation expectations remain depressed. **In our view, CPIF inflation slightly above 1.5% will be sufficient for the Riksbank to stop stimulating policy, although it will be very difficult for the board to argue for rate hikes, especially as unemployment is set to decline very gradually, if at all.** This is also likely to be the case if inflation proves higher than expected and rises above 2.0%, given that drivers are regarded as temporary.

Swe: Inflation expectations, 5y ahead Riksbank survey



The second problem is the risk that continued ECB expansion will cause the krona to appreciate against the euro as soon as the Riksbank signals that expansion is over.

WHAT HAS HAPPENED SINCE FEB 12? Inflation for March and April together with GDP growth for Q4 2014 are the most important metrics presented since the February *Monetary Policy Report* and as indicated above both growth and inflation were much higher than expected. Inflation expectations have also increased among money market players and households, although they remained depressed according to the wider Prospera survey that includes the views of labour market organisations. Furthermore, all inflation expectations remain far below the inflation target.

International growth indicators have been mixed, but with disappointing data in the US and its impact on expectations for Fed rate hikes having the largest impact on financial markets, interest rates have continued to decline from low levels driven also by the start of the massive ECB QE programme.

What has happened since December?

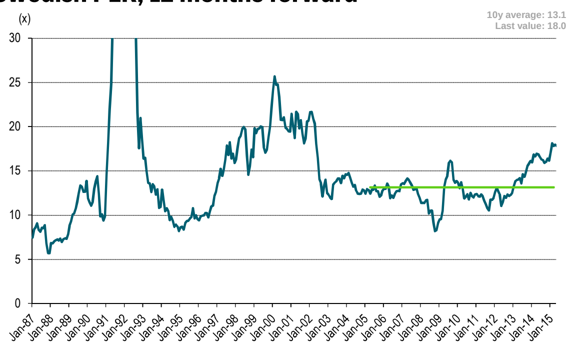
What	Compared to Riksbank December MPR	Rate path
CPI	CPIF 0.1%-points above the Riksbank's forecast, CPIF ex energy 0.1%-point lower.	↗
Inflation Expectations	Household CPI expectations 0.9% in 12m (March) but wider survey including labour market organizations remains low (0.5%/1.1%/1.7%)..	↗
Labour market	Unemployment rate in January 0.1-0.2%-points higher than expected. Employment stronger than expected	→
GDP and growth indicators	Q4 2014 GDP significantly stronger, sentiment mixed but biased to the downside.	↗
Household demand	Retail sales higher.	↗
Industry	PMI higher, NIER confidence lower. Industrial production and exports continue to disappoint.	→
Housing prices / credit growth	SEB Housing Price Indicator strong. House prices and credit growth are accelerating.	↗
Global economy	US and emerging markets indicators disappoint, but stronger EU.	↘
Financial conditions: stock market /credit	Bond yields down, equities higher in Europe unchanged in the US..	↗
Global monetary policy	ECB purchase programme well underway significantly, PBOC cuts rates, Fed in no hurry to hike.	↗
Financial conditions: SEK	SEK (KIX) 2% weaker	↗

Olle Holmgren

Swedish equities

Since our last SEK Views update, Swedish equities (OMXS30) have surged returning 27%, and 16% year to date. European and Nordics markets in general and Sweden in particular accelerated at the beginning of the year as the ECB announced its stimulus package. Since then, the Swedish market has continued to be fuelled by announcements of further QE packages and profit supportive tailwinds from foreign exchange. **Our target is for the OMXS30 to reach 1785 by the end of 2015 at the latest.** See further details in our most recent strategy report *Brightness in the Gloomy Boom* (24 March 2015). Our target set on 8 February 2015 assumed continued profit revisions in line with the negative trend experienced over the last years. We also concluded that if the risk compensation was to be normalized, adjusting for a lower long run rate equilibrium, stocks would have to be valued 30% higher on average. Swedish stocks are trading at 12-month forward looking PER at 18.0x, a 37% premium to the 10-year historical average. **However, a structural shift in valuation suggests a 7% premium to the new long-run equilibrium.**

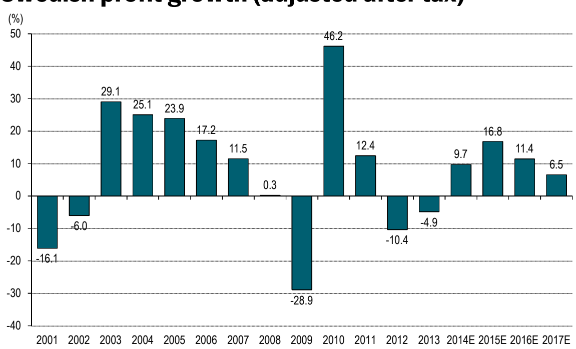
Swedish PER, 12 months forward



Source: SEB

Reviewing earnings neutral multiples such as the P/BV suggests a premium of 20% to the 10-year average, as Swedish stocks trade at 2.5x. From a macro perspective Swedish stocks earnings should benefit from favourable currency movements and over-trend GDP growth as global growth should pick up according to our SEB GLEI. Albeit shallow compared with history, we predict an earnings growth cycle recovery as we estimate profits to grow 16.8% in 2015 from 9.7% in 2014.

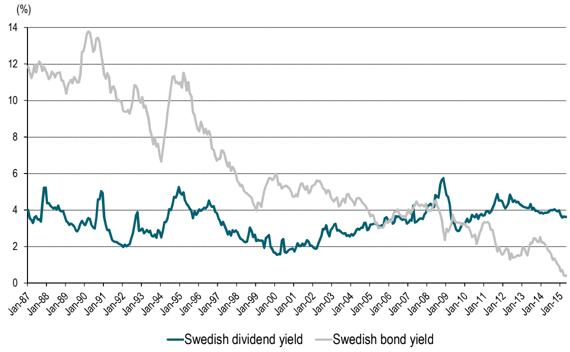
Swedish profit growth (adjusted after tax)



Source: SEB

As the business cycle has been lacklustre, low volumes have challenged margins. Thus if demand and economic growth are to pick up according to our estimates, margins should also improve in a mid-term perspective. In a low interest-rate environment, dividends become even more important. Currently the Swedish dividend yield of 3.6% looks high when compared with both a Swedish bond yield as well as in an historical perspective. The spread is currently at an all-time high in benefit to the dividend yield.

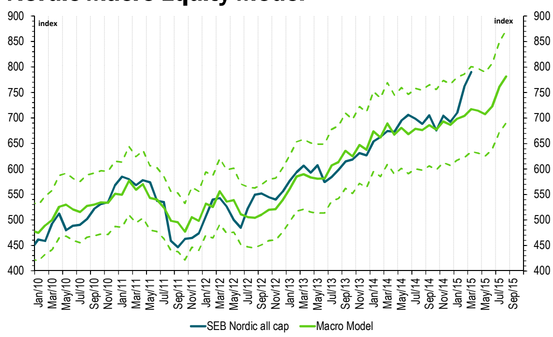
Swedish 10Y government and dividend yield



Source: SEB

Returning to the discussion of earnings revaluation in combination with continued low-rate environment has induced us to lower our required rate of return by 100bps to 6.5. When reviewing our SEB Nordic Macro Equity model, it seems that markets have already priced in the favourable macro backdrop and continued monetary stimulus. We argue that this might just be an FX readjustment as the sharp increase of the SEB Nordic All Cap index realigns with our forecast when recalculated in a global currency such as the SDR. Thus, what looks as a sideways moving market until August 2015 may in fact provide further support as leading indicators begin to filter through the market.

Nordic Macro Equity Model



Source: SEB

With this back-drop for Nordic equities, and remembering that correlations within the Nordics is high, we argue that Nordic stocks will continue to benefit from a global economic lift-off, favourable currency movements and continued monetary stimulus. **Thus we recommend investors with global mandates to be overweight Nordic equities.**

Disclaimer

Analyst Certification
We, the authors of this report, hereby certify that the views expressed in this report accurately reflect our personal views. In addition, we confirm that we have not been, nor are or will be, receiving direct or indirect compensation in exchange for expressing any of the views or the specific recommendation contained in the report.

This statement affects your rights

This research report has been prepared and issued by SEB Research a unit within Skandinaviska Enskilda Banken AB (publ) ("SEB") to provide background information only. It is confidential to the recipient, any dissemination, distribution, copying, or other use of this communication is strictly prohibited.

Good faith & limitations
Opinions, projections and estimates contained in this report represent the author's present opinion and are subject to change without notice. Although information contained in this report has been compiled in good faith from sources believed to be reliable, no representation or warranty, expressed or implied, is made with respect to its correctness, completeness or accuracy of the contents, and the information is not to be relied upon as authoritative. To the extent permitted by law, SEB accepts no liability whatsoever for any direct or consequential loss arising from use of this document or its contents.

Disclosures

The analysis and valuations, projections and forecasts contained in this report are based on a number of assumptions and estimates and are subject to contingencies and uncertainties; different assumptions could result in materially different results. The inclusion of any such valuations, projections and forecasts in this report should not be regarded as a representation or warranty by or on behalf of the SEB Group or any person or entity within the SEB Group that such valuations, projections and forecasts or their underlying assumptions and estimates will be met or realized. Past performance is not a reliable indicator of future performance. Foreign currency rates of exchange may adversely affect the value, price or income of any security or related investment mentioned in this report. Anyone considering taking actions based upon the content of this document is urged to base investment decisions upon such investigations as they deem necessary. This document does not constitute an offer or an invitation to make an offer, or solicitation of, any offer to subscribe for any securities or other financial instruments.

Conflicts of Interest
SEB has in place a Conflicts of Interest Policy designed, amongst other things, to promote the independence and objectivity of reports produced by SEB Research department, which is separated from the rest of SEB business areas by information barriers; as such, research reports are independent and based solely on publicly available information.

Your attention is drawn to the fact that SEB, its affiliates or employees may, to the extent permitted by law, have positions in, buy/sell in any capacity, or otherwise participate in, any financial instrument referred to herein or related securities/futures/options or may from time to time perform or seek to perform investment banking or other services to the companies mentioned herein.

Recipients
In the UK, this report is directed at and is for distribution only to professional clients or eligible counterparties. In the US, this report is distributed solely to persons who qualify as major institutional investors. Any U.S. persons wishing to effect transactions in any security discussed herein should do so by contacting SEB Securities Inc ('SEBSI').

The distribution of this document may be restricted in certain jurisdictions by law, and persons into whose possession this document comes should inform themselves about, and observe, any such restrictions.

The SEB Group: members, memberships and regulators
Skandinaviska Enskilda Banken AB (publ) is incorporated in Sweden, as a Limited Liability Company. It is regulated by Finansinspektionen, and by the local financial regulators in each of the jurisdictions in which it has branches or subsidiaries, including in the UK, by the Prudential Regulation Authority and Financial Conduct Authority (details about the extent of our regulation is available on request); Denmark by Finanstilsynet; Finland by Finanssivalvonta; Norway by Finanstilsynet and Germany by Bundesanstalt für Finanzdienstleistungsaufsicht. In the US, SEBSI is a U.S. broker-dealer, registered with the Financial Industry Regulatory Authority (FINRA). SEBSI is a direct subsidiary of SEB.

With an eye for trading opportunities

Did you know that you can do all your trading business via the Internet?
By using Trading Station, you are always in contact with the global trading market.
You get access to the latest exchange rates, and you can buy and sell at the blink of an eye – spots, swaps or forwards.

To find out how you can develop your electronic trading, visit us at www.seb.se/mb.

Or call one of our traders to activate our e-service:
Gothenburg +46 31 774 90 60
Malmö +46 40 667 69 10
Stockholm +46 8 506 231 40