

## 'Sweden well prepared for the autumn storms'

Written by Johan Nylander

Thursday, 01 September 2011 09:27 - Last Updated Thursday, 01 September 2011 11:22

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*Handelsbanken head office Stockholm*

- [Sweden's economic recovery slows to a halt](#)
- [Sweden cuts 2012 growth forecast](#)

Sweden's finance ministry last week slashed its growth forecast for next year and said the budget surplus would shrink to all but nothing.

Sweden, which had one of the strongest economic growth rates in Europe until a month ago, has hit the buffers with strong recovery from the 2008-2009 crisis grinding to a halt, the National Institute of Economic Research (NIER) said on Wednesday.

However, Jan Häggström, Chief Economist at Handelsbanken, said that the country is "well prepared for the autumn storms" in a macro forecast.

"Despite the ongoing sharp slowdown, the Swedish economy is in pretty good shape, but global economic risk is currently very high. Luckily, both the Swedish government and the Riksbank have the muscles to fight a downturn. Contrary to many other countries, Sweden has some room for policy easing", he said.

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*Full summary:*

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The global economy may be at a crucial inflection point, and mature market economies now risk stalling after only a brief and tepid recovery following the financial crisis. The exceptionally expansionary economic policy subsequent to this near-death experience has stabilised activity short term, but this comes at a cost. As budget deficits widened sharply, government indebtedness has become unsustainable in many countries. Against this background, the western world may be in for many years of growth well below historical averages. More than ever before, the global economy is now dependent on emerging markets, in particular, China.

US economic growth slowed significantly in the first half of this year. While temporary factors played a role, the slowdown is likely also due to structural problems. In addition, uncertainty about the economic outlook is now an important obstacle to a more robust recovery. It does not help that the Fed has become harder to read and fiscal policy has become less predictable. However, in our view, prevailing domestic economic conditions are likely not bad enough to trigger a double dip in the US.

The entry of Italy, Spain and France into the sovereign debt crisis is forcing a new round of fiscal tightening in the eurozone. On top of this, eurozone banks are now in the midst of a much worse crisis of confidence than post-Lehman, implying a looming credit crunch that will add to weaker growth. The EUR will likely weaken, as the ECB will have to do what it takes to keep the financial system from collapsing. In this scenario, the weaker eurozone members will get even weaker, while the stronger members will still enjoy robust demand from emerging markets and get an additional boost from a weakening currency.

The crisis in the eurozone is deepening and growth expectations have been scaled down accordingly. The ECB has to make a u-turn and do its utmost to keep banks and governments afloat. At the end of the day, we believe that the ECB will have no choice but to follow in the footsteps of the US Fed. Against this background, we expect the EUR to weaken against the USD. In the absence of a weaker euro, the eurozone may be looking at a Japanese scenario.

Japan has surprised somewhat on the upside lately. The impact of the earthquake earlier this year was more limited than most analysts initially feared. Japan's fundamental problems are, however, unchanged. These challenges are further aggravated by the strong yen, a consequence of global economic fears. The authorities are fighting a losing battle to keep the yen down, as history tells us that intervention seldom works.

Emerging markets have been a key driver in the global economy in recent years. Asia, in particular, has been remarkably buoyant considering the gloom elsewhere. As financial fragilities have resurfaced in the form of sovereign and banking indebtedness in Europe, the question of whether or not emerging markets will continue to propel the global economy forward

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has become crucial. While not immune to problems in the developed western economies, we believe that emerging markets will remain strong. They will provide markets for countries which are well-positioned in global markets, and in contrast to the US, Europe and Japan, they can relax economic policy if need be.

Sweden has strong domestic credentials, but is nevertheless a small vessel on the choppy global economic ocean. Global weakness near-term and lingering effects from the debt crises are set to curb traditional export markets. Strong fundamentals promote decent domestic demand, but the recovery is about to end. Despite the ongoing sharp slowdown, the Swedish economy is in pretty good shape, but global economic risk is currently very high. Luckily, both the Swedish government and the Riksbank have the muscles to fight a downturn. Contrary to many other countries, Sweden has some room for policy easing.