Friday Times

Friday, December 20, 2019

Business

Swedish CB ends five years of negative rates with hike to zero

Bank sees benchmark rate on hold at 0.0% through 2021

STOCKHOLM: Sweden's central bank raised its benchmark repo rate by a quarter point to zero yesterday, as expected, defying a slowdown in the economy and global uncertainty to draw a line under five years with negative interest rates.

The increase from -0.25 percent makes the Riksbank the first central bank to inch its way back up to what was long considered the floor for interest rates. Rates are still negative in the euro zone, Japan, Denmark, Switzerland and Hungary. "The Riksbank assesses that conditions are good for inflation to remain close to the target going forward," the central bank said in a statement.

"Therefore, in line with the assessment in October, the Executive Board has decided to raise the repo rate from -0.25 percent to zero percent." Deputy governors Per Jansson and Anna Breman - the latter in her first rate-setting meeting - entered reservations against the decision. Both wanted the central bank to wait before hiking. The central bank repeated that it expected the repo rate would remain unchanged through 2021. All but one analyst in a Reuters poll had forecast a rate increase. The Swedish crown gained against the euro after the decision. The world's oldest central bank cut rates to -0.10 percent in 2015, worried that the euro zone crisis would hit already weak prices and lead to a Japanese-style deflationary spiral. It was forced to go further, with rates dipping as low as -0.50 percent in 2016, before ultra-loose policy weakened the crown, pushed up import prices and boosted the export-reliant economy.

Few would argue that policy has been too tight. But many question the timing of the hike - only the second since mid-2011 - as the economy is slowing.

After years of strong growth, the economy has slowed this year. Inflation is below target and not expect to be stable around 2 percent for years. Activity in the industrial sector at its lowest level since 2012 and business confidence is falling. However, the Riksbank is worried that negative rates are damaging the economy in other ways.

In the topsy-turvy negative world, savers have suffered at the expense of borrowers. Real estate prices have soared and households and corporations have taken on more and more debt, threatening a financial meltdown if there is an unexpected shock. Cheap loans have also kept alive "zombie" firms, which otherwise would have gone to the wall, reducing overall productivity in the economy.

With government debt yields around zero or below, pension funds and insurers have to take greater risks to meet their liabilities. The move also puts the Riksbank at odds with other major central banks. The European Central Bank and the Federal Reserve in the United States have both eased policy recently and others are on hold as they await clarity on developments in the global economy.

Norway's central bank left its benchmark rate unchanged at 1.50 percent on Thursday.

While the Riksbank has been keen to exit negative policy, it could be forced into a U-turn if Brexit or the ongoing trade conflict between the United States and China turns nasty and inflation dives again. "They raised the rates mainly because they said they would-they backed themselves into a corner," said David Oxley, Senior Europe Economist at Capital Economics. "All paths, for me, lead back to a rate cut." — Reuters

STOCKHOLM: Governor of Sveriges Riksbank, the central bank of Sweden, Stefan Ingves speaks during a press conference at the Riksbank headquarters in Stockholm yesterday. — AFP

Sweden grapples with housing market reform as risks mount

STOCKHOLM: When bailiffs came knocking earlier this year, it was the first time Kaddi Bah realized the four-room Stockholm apartment she shared with her sister and another friend was being illegally sub-let. Now Bah, a 27-year-old hotel receptionist, has been evicted after authorities confiscated the property from the owner as part of a crackdown on black market rentals.

Since late November, she has shared a one-room apartment with a friend. The only other choice would be to move back in with her father and several other relatives who share an apartment, and where she had to sleep on the floor. "It's very stressful. The room is full of stuff and it's about as far from my work as you can get. But there's nothing I can do," she said. Bah's predicament is just one symptom of Sweden's dysfunctional housing market. Controls on private sector renting and a shortage of publicly allocated housing-you can wait 30 years for an apartment in attractive parts of Stockholm-have nurtured the perfect conditions for a lucrative market in illegal sub-lets where the final tenant must pay way over the odds.

At the same time, a toxic cocktail of negative interest rates and a shortage of housing has seen property prices double over the last 15 years. Mortgage lending has soared and now accounts for around three-quarters of all lending in Sweden at some $450 billion-close to the country's annual GDP. That is fuelling fears that banks are massively exposed should the real estate bubble burst. Sweden has been here before. A property crash in the 1990s saw two banks fail and forced a devaluation of the currency. Interest rates briefly hit 500% while unemployment surged amid a deep recession. "The whole system relies on nothing going wrong, ever, anywhere," central bank chief Stefan Ingves said in October.

STOCKHOLM: A building under construction is seen in Stockholm.— Reuters

Biggest risk

There are new signs of strain. After a recent building boom, many properties now stand empty. Developers who had sought to cash in on high prices have been forced to offer deep discounts and other incentives-if they can sell at all. Tighter credit rules have squeezed out potential borrowers even though near-zero interest rates mean the monthly cost of repaying a mortgage is often less than renting. "The market has changed from a few years ago," Linda Leppanen, the head of property development for the North of Stockholm at IKANO Bostad said. "The apartments we are selling now ... on average, prices are down by 20 percent."

IKANO, owned by the family of IKEA founder Ingvar Kamprad, is offering all the apartments in one of two new buildings in Stockholm for rent after the other block failed to sell out. Interest has been huge, with around 900 applications for the first 27 rented homes.

Another developer, Einar Mattsson, tempted buyers with an offer of up to 6,000 Swedish crowns ($625) a month of free food delivered to their door and packed away in their fridge by the delivery driver, who sends a video as a receipt. Some property firms are in trouble. Financial problems at Oscar Properties, a developer in Stockholm, have seen its shares fall more than 90 percent since the start of 2017. It lost nearly 500 million crowns in 2018, after apartment sales fell by more than half to just 79 units.

In November, the financial watchdog warned that banks are underestimating the risks in the commercial property market and proposed they build bigger financial buffers.

Action plan

Politicians are beginning to take action. A deal between the Social Democrat and Green coalition government and two smaller center-right parties has broken decades of inertia. The government has introduced subsidies for builders and is tweaking capital gains tax for house sellers to encourage more turnover.

The so-called January Agreement between the four parties promises wider changes, not least to a system that barely taxes real estate and offers tax breaks to borrowers with mortgages that can extend for a lifetime. "All the parties which signed the January Agreement have been clear that we will deliver what the agreement states and that includes an overview of the tax system," Markets and Housing Minister Per Bolund told Reuters.

Bolund would only say measures would likely be neutral for taxpayers, with hikes in one area offset by cuts in others. But even with the current broad political consensus, sweeping measures will take time to implement and the financial system will remain vulnerable for years. Meanwhile, Brexit or the trade war between the United States and China could tip the world into a new economic crisis. — Reuters