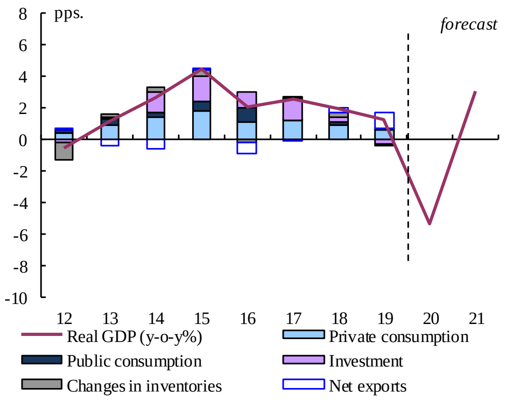
2.27. SWEDEN

The Swedish economy showed a relatively robust performance in the first quarter of 2020, in spite of the COVID-19 pandemic triggering a sharp deterioration in economic activity from mid-March onwards. Real GDP grew 0.1% q-o-q in the first quarter, mainly due to positive net exports. Even though only some restrictions were put in place to counter the spread of the disease, both the demand and supply side of the economy took a hit. While the rather less restrictive measures helped cushion the immediate impact on the economy, particularly on domestically oriented branches, exporting industries experienced strong declines in output as cross-borders value chains were disrupted. Durable consumer goods, travel services and capital goods-producing sectors were particularly affected.

Real GDP is expected to show a sharp fall in the second quarter of 2020, with a recovery following in the second half of the year. The uncertain outlook for demand and lower capacity utilisation should lead to a sharp decline in capital formation this year. Equipment investment is also expected to suffer, as it is the investment category that reacts most strongly to the business cycle. Private consumption decreases follow on from substantial job losses and uncertainty, as well as the impact of restrictions. The sharp fall in economic activity forecast in Sweden's main trading partners is expected to translate into a large decline in exports.

Economic growth is set to turn positive in 2021 as impediments slowly dissipate and the economies of major trading partners recover. A return to work should foster a bounce back in consumption growth in 2021. In 2020, economic growth is expected to fall to -5.3% before recovering to 3.1% in 2021. A second pandemic wave in Sweden or its major trading partners is the main downside risk to the GDP forecast for Sweden.

Graph 2.27: **Sweden - Real GDP growth and contributions**



The shrinking economy, sharply lower energy prices, the stabilisation of the krona and the postponement of wage negotiations are set to dampen price pressures this year. These dampening factors are expected to outweigh increases in food prices, which remain relatively strong in view of unchanged demand and bottlenecks in production and supply. Overall, HICP inflation fell to around 0% in April and May 2020 and is forecast average 0.6% for the year as a whole. Base effects from energy prices and reinvigorated domestic demand are expected to support a rise in inflation to over 1% in 2021. However, underlying inflation is set to moderate further on the back of economic slack and muted wage growth.