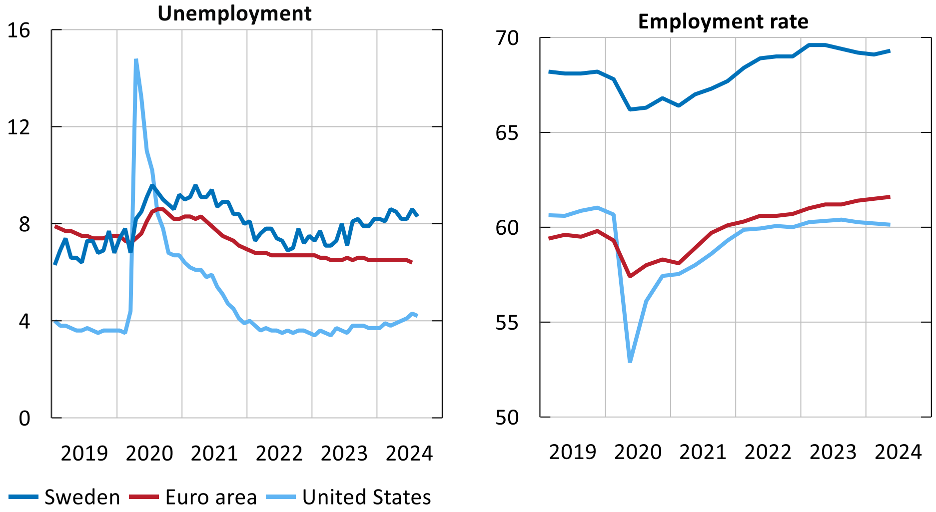
Figure 4. Unemployment and the employment rate abroad

Percentage of the labour force (left) and percentage of the population (right)



Note. Seasonally adjusted data. Unemployment and the employment rate among those aged 15–74 in Sweden and the euro area, and those aged 16 and older for the United States.

Sources: Eurostat, Statistics Sweden and the US Bureau of Labor Statistics.

Inflation is on the way down but inflation in service prices is still high

In August, HICP inflation in the euro area fell to 2.2 per cent. The downturn can largely be explained by a lower rate of increase in energy prices (see Figure 5). Since the end of last year, the annual rate of increase for services prices has been at around 4 per cent, which is substantially higher than normal (see Figure 6).[5] Agreed wage increases in the euro area slowed down during the second quarter but, in several countries, wages are still rising at a relatively rapid pace, which contributes to maintaining the rate of increase in service prices. This includes Germany.

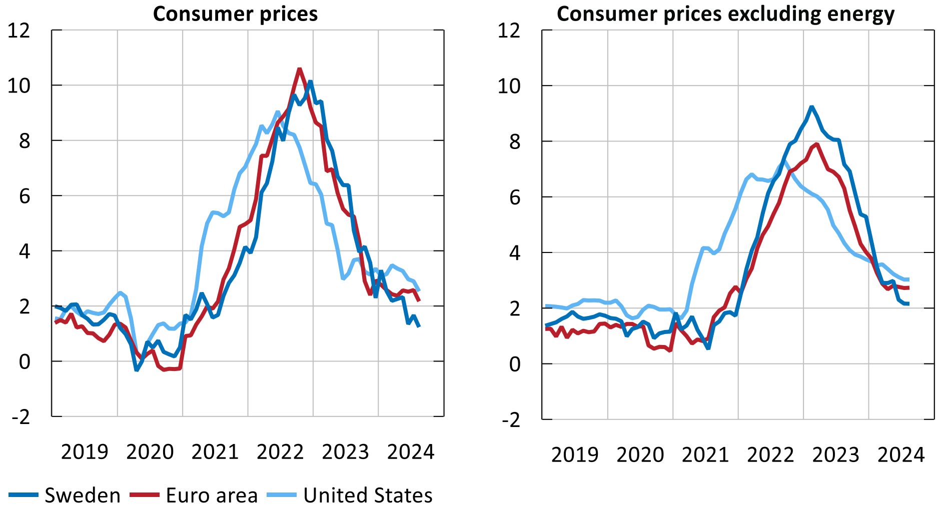
In the United States, CPI inflation has continued to fall and was 2.5 per cent in August. One reason for this is the lower rate of increase for energy prices, as well as the slower increase of services prices excluding rents and energy in recent months at the same time as the rate of increase in prices for goods has remained low. Moreover, other prices are now increasing at a more moderate pace. In terms of the PCE, inflation was 2.5 per cent in July.[6] US wage growth has slowed down over the last year. In addition, commodity prices have fallen on the world market and inflation expectations have slowed down in both the euro area and United States. This suggests lower inflationary pressures in the period ahead.

[5] The average annual change in services prices since January 2000 is 2.1 per cent in the euro area, 3.0 per cent in the United States and 2.3 per cent in Sweden.

[6] PCE is the Federal Reserve's preferred measure of inflation. Rents have a lower weighting in this measure than in the CPI. See the fact box "The difference between the measures CPI and PCE in the United States" in the Monetary Policy Report March 2024, Sveriges Riksbank, for a description of the differences between the CPI and PCE measures.

Figure 5. Consumer prices in various countries and regions

Annual percentage change

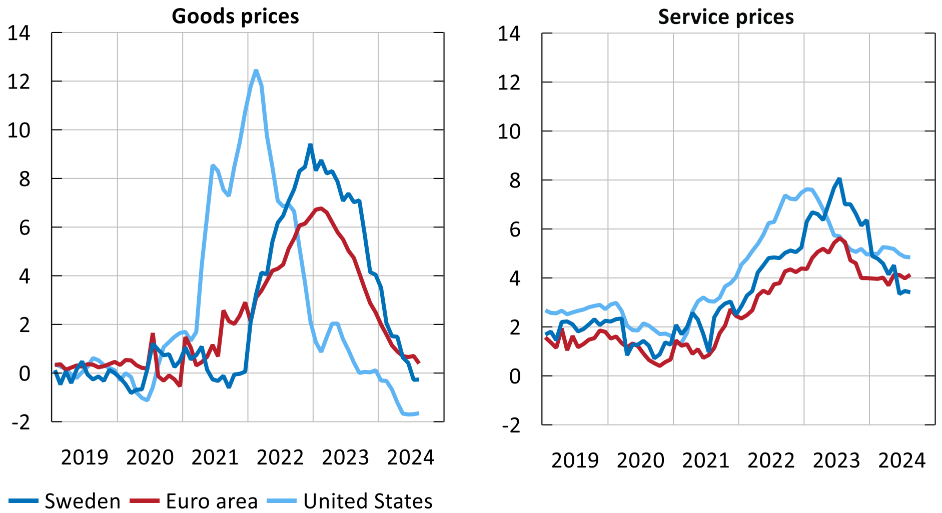


Note. Refers to the CPIF for Sweden, the HICP for the euro area and the CPI for the United States.

Sources: Statistics Sweden, Eurostat and US Bureau of Labor Statistics.

Figure 6. Prices of goods and services abroad

Annual percentage change



Note. Refers to the CPIF for Sweden, the HICP for the euro area and the CPI for the United States.

Sources: Eurostat, Statistics Sweden, US Bureau of Labor Statistics and the Riksbank.

1.2 Financial conditions

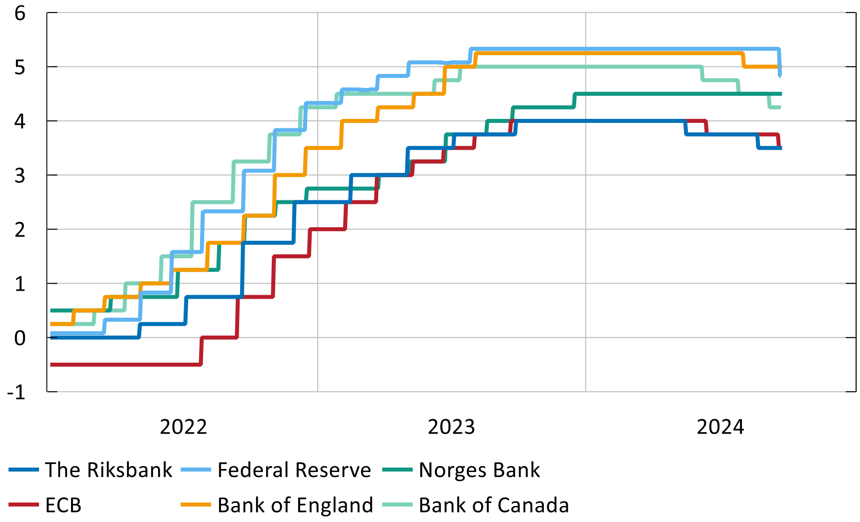
ECB and Federal Reserve cut their policy rates in September

Following the rapid increases in policy rates, most central banks around the world are in a situation where they are now gradually easing their monetary policy, even if interest rate levels are still contractionary (see Figure 7). On 12 September, the ECB cut its deposit rate by 0.25 percentage points, to 3.5 per cent.[7] The ECB emphasises that it is unwilling to commit to a certain interest rate path in advance and that interest rate decisions will be taken on a meeting by meeting basis.

The Federal Reserve cut its policy rate on 18 September for the first time since March 2020. At its meeting, the target interval for the Federal funds rate was cut by 0.5 percentage points to 4.75-5.00 per cent. The central bank communicated that the upside risks for inflation have declined and that the downside risks for the labour market have increased, and that it is therefore appropriate to begin easing monetary policy to avoid an overly weak economic development. The Federal Reserve emphasises that they are not following a predetermined interest rate path, but will take decisions one meeting at a time. The FOMC members' own assessments of the future policy rate, illustrated by the 'dot-plot', were lowered for 2024 and 2025 and indicate a policy rate of 4.4 per cent before the end of the year and 3.4 per cent at the end of 2025.[8]

Figure 7. International policy rates

Per cent



Sources: National central banks and the Riksbank.

[7] The ECB also cut the interest rate for its lending facility and the interest rate for its main refinancing operations. See ECB monetary policy decision, 12 September 2024.

[8] Refers to the mid-point for the policy rate interval. See *FOMC Projections material,* September 2024, Federal Open Market Committee, Federal Reserve.

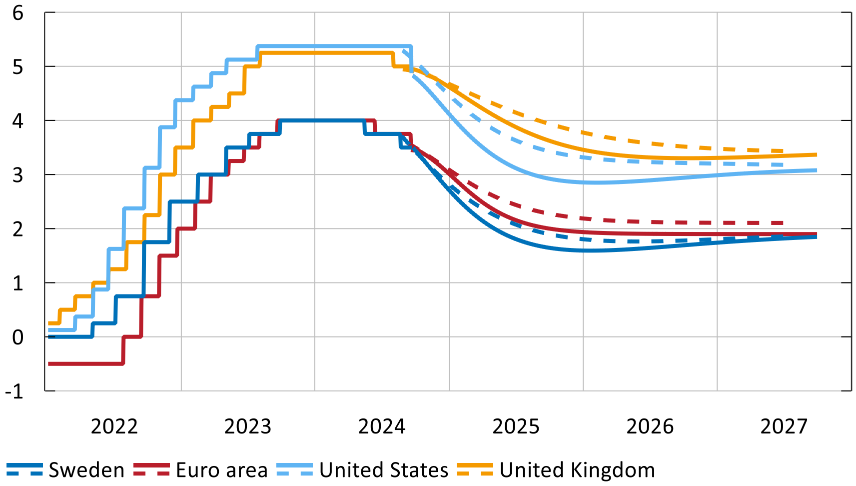
Market expectations of international policy rates have fallen again

At the beginning of the year, there were widespread expectations that central banks abroad would cut their policy rates several times over the year. During the spring, these expectations were reversed, largely due to surprisingly high inflation outcomes and stronger economic activity. Over the summer, market expectations have shifted down again apace with clearer signs of lower inflation outcomes and economic slow-down. The expectations of the Federal Reserve's monetary policy have varied substantially, with market pricing having shifted several times in response to new economic outcomes.

According to the pricing of futures contracts for short-term money market rates, market participants expect the Federal Reserve to cut the policy rate by around 1.7 percentage points until the middle of next year. For the ECB, expectations of rate cuts are somewhat lower. The ECB is expected to cut the deposit rate by around 1.3 percentage points over the same time period (see Figure 8).

Figure 8. Market expectations of policy rates in the future

Per cent



Note. The figure shows policy rates and market-based expectations according to forward pricing (Nelson-Siegel (1994)). Solid lines represent expectations on 23 September 2024. Dashed lines represent expectations immediately prior to the Monetary Policy Update in August.

Sources: National central banks and the Riksbank.

Market rates at both short and longer maturities have fallen slightly

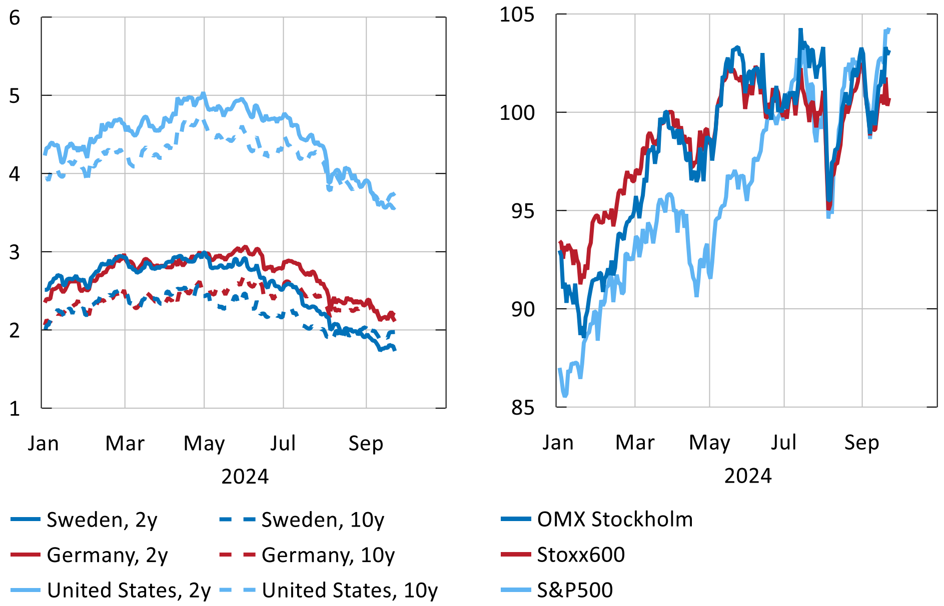
Since the Monetary Policy Update in August, both short and long-term government bond yields and yields on higher-risk bonds have fallen slightly in Sweden, the euro area and the United States (see Figure 9). In the euro area and United States, the yield spread between risky bonds and swap rates increased temporarily in conjunction with the financial turbulence at the start of August.[9] Even though monetary policy remains

[9] Risky bonds refers to covered bonds, municipal bonds and corporate bonds, for example.

contractionary, the shrinking yield spreads are making it easier for banks and companies, for example, to obtain funding on the market. The global financial conditions can change rapidly, however. One example of this was the market turbulence observed at the beginning of August, when for instance yen-financed carry-trades were rapidly settled.

Figure 9. Government bond yields and stock market movements in Sweden, the euro area and US

Per cent (left) and index, 27 June 2024 = 100 (right)



Note. The left-hand figure refers to zero coupon rates for Sweden and Germany, as well as benchmark rates for the United States.

Sources: Macrobond and the Riksbank.

Stock markets have also continued to develop strongly and have recovered from the downturn at the start of August (see Figure 9). Measured using the VIX index for the United States and Germany, volatility on the stock market is lower today, overall, than it was during the summer. Indicators measuring financial stress on the markets are also at low levels.

Lower lending and deposit rates for households and companies

As the Riksbank has cut its policy rate, the interest rates faced by households and companies have also fallen. Since the start of the year, the average mortgage rate on new loans has fallen by about as much as the Riksbank has so far cut the policy rate (see Figure 10).[10] For mortgage rates on loans with a longer maturity that also include expectations of lower interest rates going forward, mortgage rates have fallen more than the policy rate, however (see Figure 11). For instance, the average rate on new mortgages with a fixed interest period of between one and three years has fallen by around one percentage point since the beginning of 2024. In the corporate sector too,

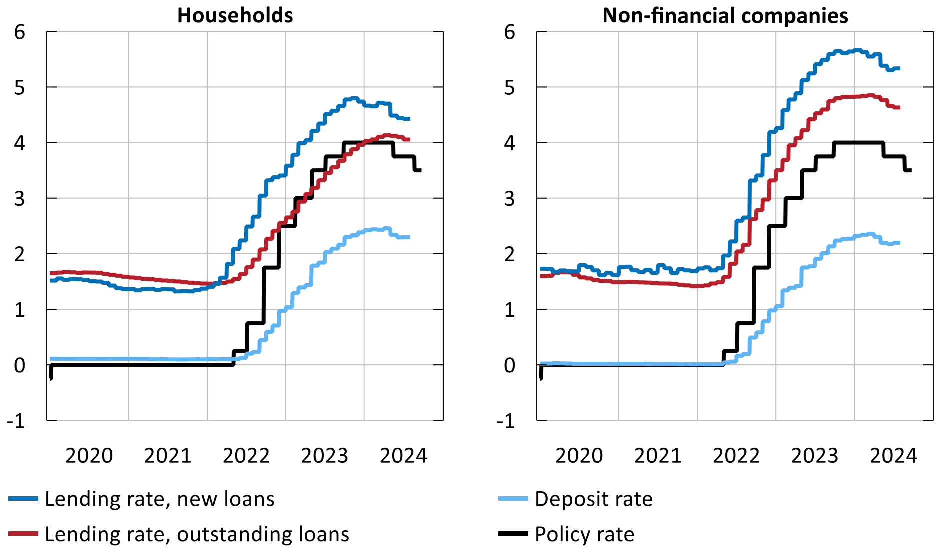
[10] Based on Statistics Sweden's financial market statistics until the end of July and the banks' published average interest rates in August.

all industries are facing a lower interest rate on their outstanding bank loans (see Figure 10).

The deposit rate has also fallen, although not by as much as the average lending rates. When the policy rate is cut, deposit rates usually fall by less than lending rates. This is partly because competition for deposits is relatively high, not least from other financial instruments in which depositors can invest their liquidity. The transmission from the policy rate to the interest rates met by households and companies is following historical patterns and working well.

Figure 10. Average lending and deposit rates to households and companies and the Riksbank's policy rate

Per cent

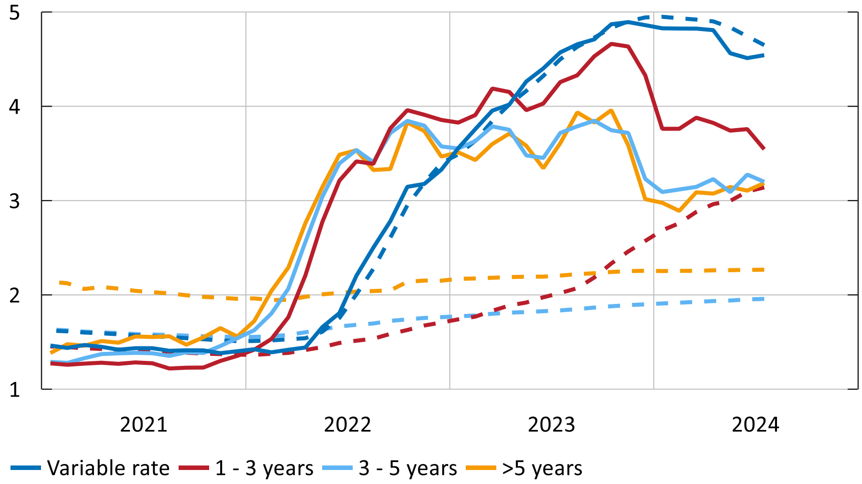


Note. Volume-weighted averages of lending and deposit rates at all maturities. For households, this refers to interest rates on loans from monetary financial institutions, housing credit institutions and alternative investment funds. Household lending rate refers to loans for housing purposes. For companies, this refers to loans from monetary financial institutions. New loans also includes renegotiated loans. The last outcome refers to July 2024.

Sources: Statistics Sweden and the Riksbank.

Figure 11. Average mortgage rates to households for various fixed terms

Per cent



Note. Refers to mortgage rates from monetary financial institutions, housing credit institutions and alternative investment funds. Solid lines represent new and renegotiated loans, dashed lines represent outstanding loans. The last outcome refers to July 2024.

Source: Statistics Sweden.

Credit growth remains on low levels and housing prices are rising slowly

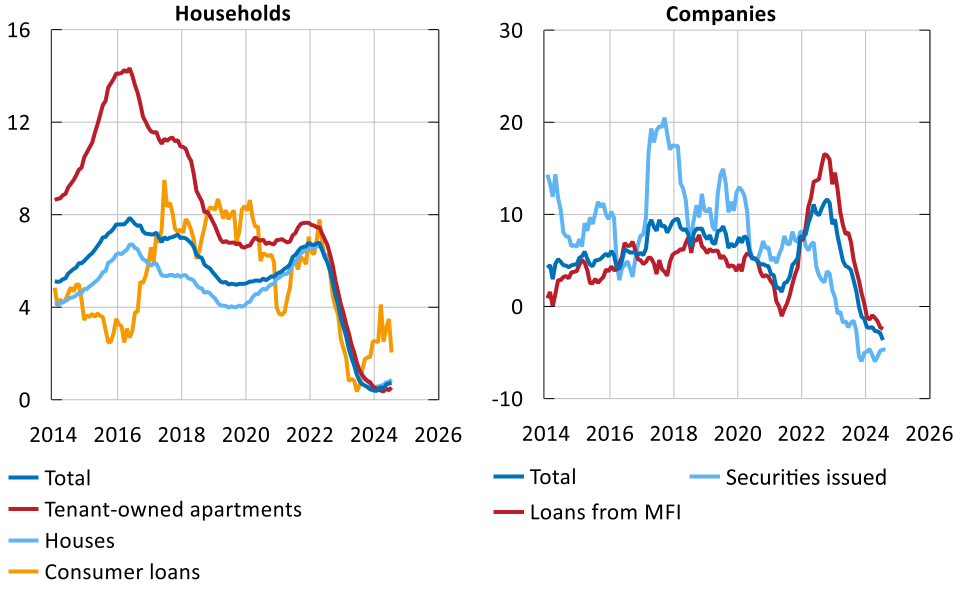
Despite the slightly lower lending rates, lending to households and companies remains on low levels. It is still negative for companies (see Figure 12).[11] Companies within all sectors, except for the categories “property sector – housing” and “other services”, which are cutting their borrowing.

Since the start of the year, housing prices have risen by about 2.5 per cent. Housing prices are now on about the same level as before the pandemic. Even though turnover on the housing market has started to recover slightly, the supply of housing has continued to increase during the year. The large supply in relation to turnover may have a restraining effect on housing prices.

[11] Corporate borrowing can take place via bank loans or by the issuance of securities on the bond market. Even if total credit growth is negative, there are some signs that lending via the bond market in Swedish kronor is increasing slightly due to increased risk appetite and lower risk premiums.

Figure 12. Household and corporate borrowing

Annual percentage change



Note. Lending by monetary financial institutions (MFIs) to households and non-financial corporations adjusted for reclassifications and bought and sold loans. Securities issued by non-financial companies have been adjusted for currency impact. Loans from MFIs constitute about two thirds of total lending to companies, while securities issues constitute around a third.

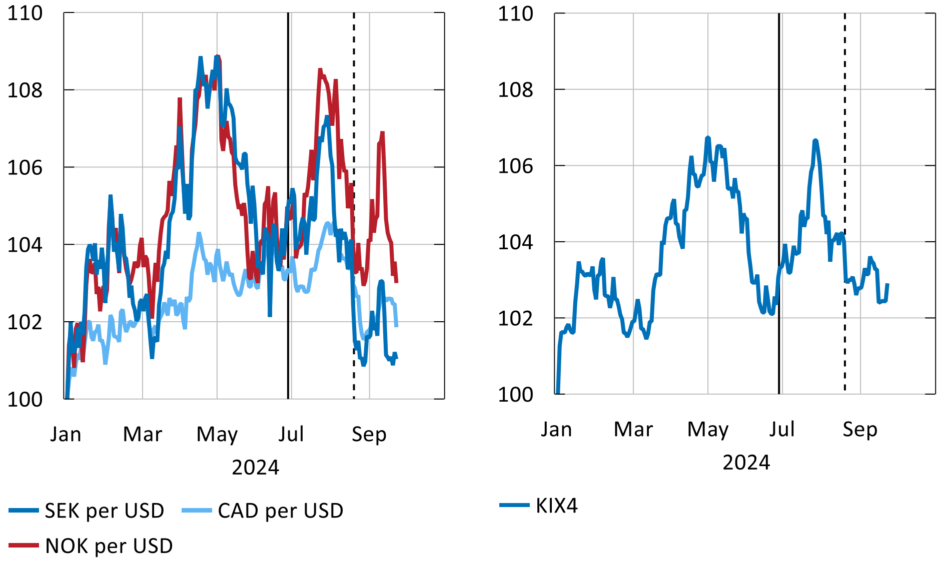
Source: Statistics Sweden.

Lower interest rates in the United States are supporting the appreciation of smaller currencies

The market has continued to adjust its expectations of the development of interest rates in the United States downwards. This has contributed to the further depreciation of the dollar and has supported smaller currencies, such as the Swedish krona. Overall, the krona has developed in line with other small currencies and, measured in terms of the KIX, the krona is at around the same level as the Monetary Policy Update in August (see Figure 13). In the Riksbank's forecast, the krona is assumed to strengthen in the period ahead.

Figure 13. Development of a number of smaller currencies against the dollar plus nominal exchange rate against KIX4

Index, 1 January 2024 = 100



Note. A higher value indicates a weaker exchange rate. The KIX4 (krona index) is a weighted average against the US dollar, euro, pound sterling and Norwegian krone. The dashed vertical lines mark the date of the Monetary Policy Update in August and the solid vertical lines mark the date of the Monetary Policy Report in June.

Sources: Macrobond Financial AB and the Riksbank.

1.3 Swedish real economy

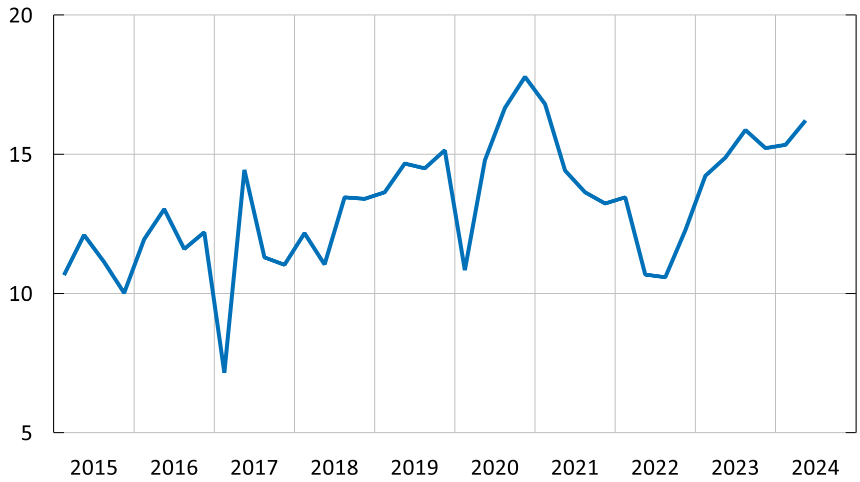
Swedish consumption remains weak

Swedish GDP decreased by 0.3 per cent during the second quarter of the year, compared with the previous quarter (see Figure 3). The downturn can largely be explained by weak consumption and investment, while the greatest positive contribution came from net exports. The household savings ratio has been high and consumption has been restrained since interest rates started to be raised in 2022 (see Figure 14).[12]

[12] See also "Households continued saving at the same time as the growth rate for mortgages increased", Financial accounts, second quarter 2024, Statistics Sweden.

Figure 14. Household savings ratio

Percentage of disposable income



Note. Seasonally adjusted data. Households and non-profit institutions serving households (NPISH).

Sources: Statistics Sweden and the Riksbank.

The National Institute of Economic Research's Economic Tendency Survey fell marginally in August and overall contributes to the view of slightly weaker development than the Riksbank expected in its June forecast. However, there remain signs of future optimism among households. For example, their assessment of Sweden's economy and their own economies in 12 months is higher than normal.

Continuing weak labour market

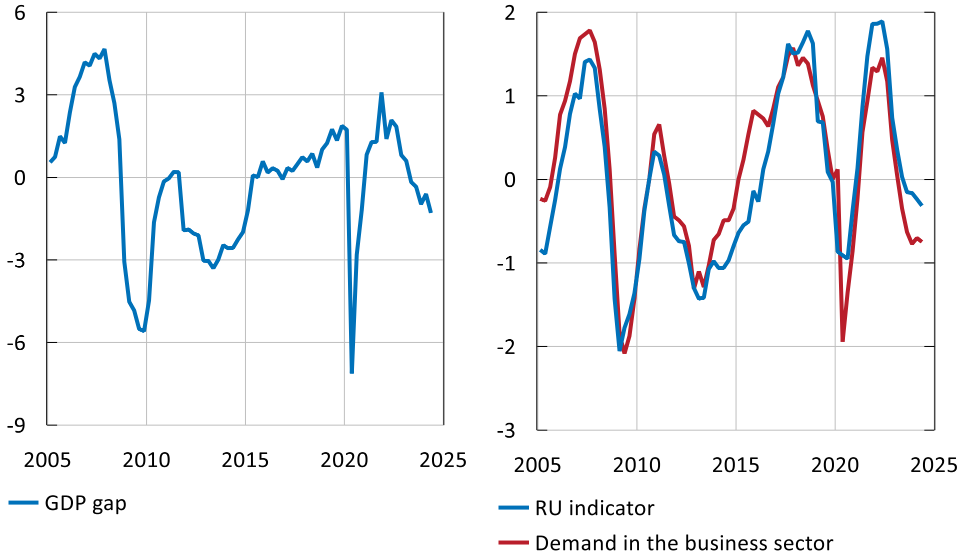
Unemployment has risen since the end of 2022 (see Figure 4). The low demand in the economy and labour market indicators all point to the continuing relatively weak development of the labour market in the near term. The number of redundancy notices and bankruptcies is on an elevated level and the number of newly-registered vacancies has fallen significantly. On the other hand, recruitment plans are weakly positive, with the service sector in particular planning new recruitment.

Recession close to bottom

Resource utilisation in the Swedish economy is currently assessed to be somewhat lower than normal and the economy is in mild recession. One way of estimating resource utilisation is to assess the size of the gap between actual and potential levels for GDP, for example, known as the GDP gap. Another indicator of resource utilisation is the view taken by companies of the current demand situation, which is measured regularly by the National Institute of Economic Research. The Riksbank's assessment is that the GDP gap is lower than normal, which corresponds well to the current demand situation (see Figure 15). The Riksbank's resource utilisation indicator, the RU indicator, which weighs together various indicators, also suggests that resource utilisation has fallen and is marginally below normal. But indicators for growth have risen since the start of the year and are starting to approach levels compatible with normal growth. The assessment is thus that economic activity will not weaken much more.

Figure 15. GDP gap and demand in the business sector

Per cent (left), standard deviation (right)



Note. GDP gap refers to the deviation from the Riksbank's assessed long-term trend. The RU indicator is a statistical measure of resource utilisation. The RU indicator and demand situation in the business sector are both normalised so that the mean value is 0 and the standard deviation is 1.

Sources: National Institute of Economic Research, Statistics Sweden and the Riksbank.

ANALYSIS – Microdata gives insights into how companies adjust their prices

One way of gaining an understanding of how companies adjust their prices is to investigate how often and by how much prices change for products included in the consumer price index (CPI). The results show that it is primarily the frequency, and not the magnitude, of price changes that correlates with the rate of inflation. This was evident in 2022 and 2023, when inflation was high. At that time, companies increased their prices much more frequently than before, while the average size of price changes did not change much. As inflation has fallen, companies have also started to change their prices less frequently. This indicates that pricing behaviour is now more in line with what it was before the period of high inflation.

To understand what affects inflation, it is important to understand how companies set their prices and whether and, if so, how this changes under different economic circumstances. There are studies indicating that the pass-through to consumer prices