Minutes of monetary policy meeting

September 2015

Summary

At the Monetary Policy Meeting on 2 September, the Executive Board of the Riksbank decided to leave the repo rate unchanged at –0.35 per cent. The expansionary monetary policy, with a negative interest rate and the previous decision to purchase government bonds until the end of the year, is supporting the continued positive development of the Swedish economy so that CPIF inflation can be expected to be close to 2 per cent in 2016. The Riksbank remains highly prepared to make monetary policy even more expansionary in the event of the inflation outlook deteriorating.

It was noted at the meeting that the Executive Board agreed on the description of economic prospects and the inflation outlook in the draft Monetary Policy Report.

The expansionary monetary policy in Sweden has contributed towards economic activity strengthening, the labour market situation improving and there being a clear upward trend in inflation since last autumn.

The recovery is continuing abroad. But developments there are still surrounded by great uncertainty due to the fall in the price of oil and large fluctuations on the stock and foreign exchange markets.

Lower energy prices due to the fall in oil prices have led to a downward revision to CPIF inflation in the period ahead but, nevertheless, inflation is expected to rise clearly and the forecast for the CPIF excluding energy remains basically unchanged since the assessment made in July.

All in all, developments in Sweden and abroad have been in line with the assessment in July and the revisions to the forecast are small.

The Executive Board therefore unanimously decided to leave the repo rate unchanged at –0.35 per cent and to continue to purchase government bonds until the end of the year according to the plan determined by the Executive Board in July.

Given the uncertainty surrounding international developments, the Executive Board also agreed unanimously that the Riksbank needs to maintain a high level of preparedness to make monetary policy even more expansionary, even between ordinary monetary policy meetings, should the inflation outlook deteriorate.

By pursuing a continued highly expansionary monetary policy, the Riksbank is supporting the positive development of the Swedish economy so that CPIF inflation can be expected to be close to 2 per cent next year.

The meeting also discussed developments in China and other emerging market economies and the risk that the volatile oil price will influence the inflation assessment. It was noted in various ways that the development of the Swedish krona will continue to be important. Several members of the Executive Board also discussed how much scope there is for making monetary policy more expansionary. Finally, several members of the Executive Board emphasised that there is a great need to manage mandates and tools within the area of macroprudential policy promptly.

MINUTES OF MONETARY POLICY MEETING
Executive Board, No. 4

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DATE: 02/09/2015

TIME: 09.00

PRESENT: Stefan Ingves, Chairman
Martin Flodén
Per Jansson
Kerstin af Jochnick
Henry Ohlsson
Cecilia Skingsley

Susanne Eberstein, Chair of the General Council
Michael Lundholm, Vice Chair of the General Council

Yoav Soffer, Bank of Israel
Gary Watson

Meredith Beechey Österholm
Claes Berg
Carl-Johan Belfrage
Charlotta Edler
Lena Eriksson
Mattias Erlandsson
Eric Frieberg
Tobias Helmersson (§ 1)
Ola Melander
Pernilla Meyersson
Ann-Leena Mikiver
Marianne Nessén
Olof Sandstedt
Henrik Siverbo
Ingvar Strid
Ulf Söderström
Jens Vahlquist (§1)
Anders Vredin

It was noted that Carl-Johan Belfrage and Henrik Siverbo would prepare draft minutes of § 2 and 3 of the Executive Board's monetary policy meeting.

§1. Economic developments

Tobias Helmersson of the Markets Department began by presenting the latest developments on the financial markets. Since the monetary policy meeting in July, political unease in Greece, followed by uncertainty over China and other emerging market economies, has affected the development of the markets. Stock markets have fallen and decreases in commodity and energy prices have dampened international inflation and inflation expectations and pushed down government bond rates. More short-term interest rates in the United States and United Kingdom are reflecting expectations that their central banks will start the normalisation of monetary policy by raising their policy rates during the year and at the start of next year, respectively, while interest rates in Sweden and Germany are lower.

There have been fairly large movements in the krona exchange rate, as there have been on the foreign exchange market in general, but, in KIX terms, the krona is now at about the same level as when the last monetary policy decision was taken in July. Surveys and market pricing reflect expectations of a slightly lower repo rate at the end of the year but only a minority of market participants expect a repo rate cut in September.

Marianne Nessén, Head of the Monetary Policy Department, presented the draft Monetary Policy Report which, in the assessment of the Monetary Policy Department, would gain the support of the majority of the members of the Executive Board. She began by noting that the forecasts in the draft report were discussed by the Executive Board at meetings held on 17, 18 and 21 August. The draft Monetary Policy Report was tabled at a meeting of the Executive Board on 25 August. The Monetary Policy Report was also discussed on 31 August in the light of recent days' financial market turbulence.

Economic activity abroad has continued to improve gradually in line with the forecasts made by the Riksbank in July. However, storm clouds are on the horizon in the form of uncertainty over developments in China and elsewhere. The growth in KIX-weighted GDP is expected to amount to slightly less than 2 per cent this year and then rise to just over 2.5 per cent at the end of the forecast period. The economic development of the United States is expected to continue to be strong and the gradual recovery of the euro area is expected to continue.

Only minor revisions have been made to the forecasts for economic developments in Sweden. GDP growth was unexpectedly strong in the second quarter, which led to a certain upward revision of the forecast for the current year. Supported by the expansionary monetary policy, GDP is expected to grow at a faster pace than the historical average in the coming years. Unemployment will fall gradually from the current level of 7.3 per cent (seasonally-adjusted) to just below 7 per cent at the end of the forecast period. Household debt ratios are expected to increase in the period ahead as rapidly rising house prices are expected to lead to households' debts rising faster than their disposable incomes.

Inflation has been increasing for a while now. In July, CPIF inflation was 0.9 per cent and inflation as measured by CPIF excluding energy was 1.5 per cent. CPI inflation amounted to –0.1 per cent, strongly influenced by the Riksbank's earlier repo rate cuts. The forecast for the CPIF excluding energy remains basically unchanged since July, but lower energy prices mean that CPIF inflation is expected to be slightly lower in the period ahead. Expansionary monetary policy, rising resource utilisation, higher wages and higher demand that makes it easier for companies to raise their prices mean that CPIF inflation is rising and will be close to 2 per cent in 2016. Over the recent period, short-term inflation expectations have shown a rising trend. In the longer term, a certain degree of stabilisation has taken place, even if the level continues to be slightly below 2 per cent.

The forecasts in the draft Monetary Policy Report are contingent on the repo rate being held unchanged at –0.35 per cent. The repo-rate path reflects the fact that it is possible that the repo rate will be cut further. It is considered appropriate to begin slowly raising the repo rate at the end of 2016. The forecasts are also contingent on the Riksbank continuing to purchase Swedish government bonds as previously announced. So far, as per 2 September, in nominal terms, the Riksbank has purchased government bonds for SEK 81.5 billion of the planned SEK 135 billion decided earlier. The acquisition value has amounted to a total of about SEK 98 billion and the Riksbank has so far received almost SEK 1 billion in coupon payments related to these bonds. The difference, SEK 97 billion, corresponds to an increase of the liquidity surplus in relation to the banking system.

§2. The economic situation and monetary policy

Deputy Governor **Cecilia Skingsley** opened by pointing out that, since the monetary policy meeting in July 2014, the Riksbank has cut the repo rate by 1.1 percentage points and decided on the purchase of Swedish government bonds for SEK 135 billion. This is a powerful response aimed at returning inflation to a level compatible with the target of 2 per cent.

Now, one year later, it is clear that the trends are moving in the right direction. To start with, the decisions have had a clear impact on interest rate levels, credit granting and exchange rates. As regards target fulfilment, the underlying inflation rate measured as the CPIF excluding energy has risen from about 0.5 per cent in the spring of 2014 to 1.5 per cent in the latest outcome from July.

Furthermore, inflation expectations over shorter time horizons have shown a rising trend since the start of the year and the more long-term inflation expectations seem to have stabilised. The development of service prices is now close to the average rate since 2000, while that of goods prices is far above it. This is occurring while the inflation-sinking effects of energy prices and the interest-rate effects of the Riksbank's monetary policy are expected to subside. Considering, in addition, that growth is about 3 per cent, the overall picture is that the development of Sweden's real economy is relatively benign despite the turbulent international situation.

Ms Skingsley said that she supports the forecasts and assessments presented in the draft Monetary Policy Report. Macroeconomic developments have been about as expected since the July meeting, which means that she sees no need, at present, for further monetary policy stimulus. Despite this, Ms Skingsley said that the decision to advocate an unchanged monetary policy was not self-evident.

Ms Skingsley went on to explain that she considers the development of the financial markets deserves a more detailed comment. To start with, the events in Greece over the summer aroused great media interest, but the fairly limited market reactions and contagion effects observed show that Greece's difficulties can now mostly be seen as only affecting the country itself. She therefore supports the Riksbank's assumption that the challenges Greece continues to face will not jeopardise the recovery of the rest of the euro area.

New circumstances to consider include the stock market fall in China and the fall in commodity prices and the consequences of these for both emerging market and more advanced economies.

Ms Skingsley takes a cautious stance towards these market changes. The weaker development of China in line with its transformation from an export-driven to a more domestically-driven economy is both expected and reasonable. If this transformation occasionally leads to difficulties, such as, for example, asset price adjustments and unexpected policy decisions, this turbulence will just have to be lived with, as long as it does not form a significant threat to the recovery of Sweden. It is difficult at present to know whether China is facing a more difficult readjustment and a deeper decline than assumed by the forecast and to assess the extent of any effects that may also impact Sweden via financial markets and other countries. It is therefore important to monitor international events and act if necessary to maintain a reasonable trend for the development of prices in Sweden.

Ms Skingsley noted that one objection to her support for an unchanged monetary policy at the day's meeting could be that she had previously supported both repo-rate cuts and bond purchases with reference to international risks. However, one difference is that the current trends of Swedish inflation and Swedish inflation expectations are slightly more benign than they were a few months ago. But Ms Skingsley maintained that, should there be reason to fear a less favourable development for inflation in the period ahead, she is prepared, like before, to support more expansionary efforts to safeguard the inflation target's role as nominal anchor for price and wage formation.

First Deputy Governor **Kerstin af Jochnick** began by saying that she shares the assessment of developments in Sweden and abroad presented in the draft Monetary Policy Report. She supports the proposal to maintain the expansionary monetary policy and to hold the repo rate unchanged at –0.35 per cent and to continue the purchases of government bonds in accordance with the decision from July.

The expansionary monetary policy is supporting the continuing positive development of growth in the Swedish economy and the development of inflation so that CPIF inflation can be expected to be close to 2 per cent in 2016.

The development of international economic activity is continuing to improve, even though there has been a degree of turbulence on the financial markets in recent weeks. As noted in the Monetary Policy Report in July, the assessment of international developments is subject to uncertainty. In July, this was primarily uncertainty about developments in Greece and the euro area. Uncertainty is now greater on a global level. The Chinese stock market decline and the weakening of the country's currency have contributed to international unease and lower commodity prices. World trade has also developed weakly for some time but recovered somewhat in June. However, uncertainty over developments in China and other emerging market economies entails certain risks for the continued recovery of the global economy.

Ms af Jochnick maintained that developments in the United States are an important factor in the Riksbank's international forecast. Her assessment is that GDP growth in the United States will be good but that there are certain question marks concerning the development of inflation. Despite increasingly strong economic activity, inflation remains low, which can be explained, not least, by the fall in oil prices over the last year and also by the appreciation of the dollar. Wage growth has also been relatively weak. Both the fall in oil prices and the strong dollar will influence inflation in the near future but these effects will decline over time. One important question internationally regards when the Federal Reserve will feel sufficiently convinced that underlying inflation is on the way up and deem that an initial policy rate increase can take place.

Closer to Sweden, GDP in the United Kingdom is developing well, while the euro area has seen moderate growth. Uncertainty about Greece over the summer has certainly had a restraining effect on GDP growth in the euro area but there are indicators that now point to increasingly strong growth, according to Ms af Jochnick. Inflation continues to be low here too, but should rise successively when demand increases and companies raise their prices.

For Sweden's part, it is Ms af Jochnick's assessment that the expansionary monetary policy has contributed towards increasingly strong growth and towards the trend for inflation now rising. The forecast for inflation, measured in terms of the CPIF excluding energy, is basically unchanged since the July report. Energy prices developed slightly more weakly than in the report from July, leading to the forecast for inflation measured in terms of the CPIF and CPI being adjusted downwards slightly. According to the forecast in the draft Monetary Policy Report, CPIF inflation will be close to 2 per cent in 2016.

International demand will develop increasingly well in the main scenario, even if there is some uncertainty about the strength of demand for Swedish exports in the period ahead. So far, however, increased Swedish export market shares seem to have counteracted the effects of the weakening of world trade. The combination of continued high consumption and increasingly strong exports should result in higher resource utilisation and rising wages. This, in turn, will lead to companies being able to raise their prices.

There is, however, some uncertainty as regards companies' scope for raising prices. This applies to both Sweden and abroad. The fall in the price of oil, increased competition due to digitisation and so on, and the effects of volatile foreign exchange markets are examples of factors that could restrain the rise in inflation in several countries.

Furthermore, Ms af Jochnick noted that collective bargaining rounds in 2016 will also set an important parameter for the development of inflation in Sweden. An article in the draft Monetary Policy Report provides a good description of the conditions ahead of the collective bargaining rounds for 2016. Stable rules and predictability have long created good conditions for the Swedish economy. In this respect, the social partners have great responsibility for ensuring stable development over the coming years. Considering that international competitiveness now seems relatively favourable and that inflation is expected to be close to 2 per cent in 2016, it seems reasonable for the inflation target to form a starting point for the negotiations.

Ms af Jochnick then summarised her assessment, which is that the Swedish economy is developing increasingly well and that inflation is rising towards the target. Economic growth abroad is increasingly positive but there is uncertainty over the strength of the upswing and over how rapidly inflation is rising. If the low level of inflation becomes entrenched, there is a risk that long-term inflation expectations will also be affected.

When she balances the arguments for and against changing the monetary policy decided upon in July, it is Ms af Jochnick's assessment that the expansionary monetary policy should be held unchanged. However, the Riksbank needs to stay prepared to make monetary policy even more expansionary if inflation prospects should deteriorate.

Finally, Ms af Jochnick repeated her concern over the development of the housing market and households' rising debts. It is clear that the housing market is suffering from major structural problems that will take a long time to repair, at the same time as household debts are continually increasing. International analysts too have identified the Swedish housing market and household indebtedness as a potential problem for the Swedish economy on several occasions. During the summer, yet another analysis arrived from the European Council with a specific recommendation to Sweden to take measures to influence both demand for credit and the supply of housing. The Government and other authorities bear a great responsibility for achieving long-term stable development of the housing market at the same time as household indebtedness must be managed. The risk is otherwise great that indebtedness will burden the Swedish economy later on, possibly exacerbating a future economic slowdown.

Ms af Jochnick concluded by noting that a better order is needed in Sweden to counteract the rise of financial imbalances. The framework for macroprudential policy needs urgently to be put into place and developed in conjunction with fiscal and monetary policies.

Deputy Governor **Martin Flodén** supported the draft Monetary Policy Report and the decision to hold the repo rate unchanged at the day's meeting.

Mr Flodén noted that, following the monetary policy decision in July, we have seen continued signs that the Riksbank's monetary policy is having the intended effects on economic development. The repo-rate cuts implemented over the last year or so have had a broad impact on market rates and have thereby increased the scope for consumption and investment for households and companies. They have also led to a weaker exchange rate. This, in turn, has contributed towards fairly good growth in the Swedish economy despite weak growth abroad, and to various measures of underlying inflation in Sweden showing a rising trend even though corresponding measures abroad remain low. It also seems that inflation expectations have stabilised, at least according to surveys, and, in both the Riksbank's Business Survey and the Economic Tendency Survey of the National Institute of Economic Research, companies are now expressing increasingly clear plans to raise their prices in the period ahead.

But there are also causes for concern, according to Mr Flodén. Ahead of the monetary policy meeting in July, there was great and immediate uncertainty over the situation in Greece and the consequences this crisis would have for the economic development of the euro area. Even if the most acute uncertainty over Greece has now subsided, it remains unclear how the country's debt problems should be handled in the long run. For example, if the new election later in September does not result in a clear mandate to implement the reform plan Greece has negotiated with its creditors, turbulence may rapidly return and it may then not be possible to rule out significant contagion effects to the rest of the euro area.

Nevertheless, Mr Flodén deems the short-term risks associated with Greece to be relatively minor. Developments in China and on certain financial markets are somewhat more worrying. The substantial falls on the equity markets are hardly a source of unease in themselves, particularly not as they were preceded by very rapid rises. But they raise the question of whether unease on the stock markets is a symptom of comprehensive real economic problems in China and other emerging market economies, and whether this then means that growth there is slowing down faster than forecast by the Riksbank. The recent unease on the financial markets in emerging market economies is probably also connected with expectations of a policy-rate rise in the United States in the autumn, something which indicates that the adjustment of the global economy to a more normal interest-rate situation may be problematic, even if interest rate increases take place at a modest pace.

If these misgivings are correct and there is a powerful weakening of growth in emerging market economies, Mr Flodén says it may be difficult to live up to the inflation forecast in the draft Monetary Policy Report. This is because, according to the forecast, a certain improvement of growth abroad is an important factor that will contribute towards a higher rate of inflation in Sweden over the coming year. If, instead, there is a weakening of the global economy, it will be difficult to counteract lower inflationary pressures with the use of the monetary policy tools the Riksbank currently has at its disposal. Mr Flodén's assessment is that, while it is certainly possible to cut the repo rate by at least one more step and somewhat increase asset purchases, the remaining scope for making monetary policy more expansionary is now limited.

Mr Flodén wished to make three clarifications of his reasoning straight away. Firstly, he agrees with the forecast in the draft Monetary Policy Report, in which the growth of Sweden's most important export markets is expected to improve in the period ahead. The United States and United Kingdom are already growing strongly and large parts of the euro area are showing signs of rising growth. In China, a gradual slowdown is the most likely development. There are thus good conditions for the international economy to be able to contribute towards the continued strong development of the Swedish economy and to the continuing rise of inflation. So the concerns he raised do not form a main scenario.

Secondly, the fact that the remaining scope for monetary policy measures is limited does not mean that the measures taken by the Riksbank have been ineffective. Mr Flodén pointed out that he has already discussed the impact of recent monetary policy on the development of inflation. Consequently, reaching the floor for the repo rate or the ceiling for asset purchases would hardly give us a reason to retreat from the implemented monetary policy, even if a weak international economy would make these monetary policy stimulus measures insufficient to keep to the current inflation forecast.

Thirdly, Mr Flodén noted that there is still scope for additional monetary policy measures. It is possible to cut the repo rate further or increase asset purchases if inflation prospects should deteriorate.

Mr Flodén also wanted to comment on the development of the oil price over the summer. The oil price has fallen since the monetary policy decision in July and this means that the forecast for CPIF inflation has been revised downwards by a few tenths of a percentage point over the coming year. Mr Flodén wondered why an attempt should not be made to counter this with a more expansionary monetary policy and answered that he agrees with the explanations provided in the draft Monetary Policy Report and that Ms Skingsley also described. There are signs of a robust rise in inflation through the rising measures of underlying inflation, for example CPIF inflation excluding energy. The fall in oil prices is not expected to affect this development, so the forecast for CPIF inflation excluding energy has not been revised downwards. Mr Flodén also pointed out that the fall in oil prices primarily means a changed time profile for CPIF inflation: it will become slightly lower over the year ahead but slightly higher in the following year when the recent fall in oil prices is no longer included in the annual figures. It is difficult to influence this changed time profile as monetary policy acts with a lag.

Deputy Governor **Per Jansson** opened by saying that, just as was stated in the draft Monetary Policy Report, arguments exist, at present, both for maintaining the monetary policy stance decided in July and for making monetary policy more expansionary. After much consideration, Mr Jansson had decided to cast his vote for the first alternative. He thus supports both the forecast and the monetary policy presented in the draft Monetary Policy Report. So what then are the arguments for leaving monetary policy unchanged or for making it more expansionary?

Mr Jansson started by presenting the arguments for keeping monetary policy unchanged. These are connected with the fact that the inflation outlook has improved in various respects.

Firstly, inflation has surprised on the upside. At the meeting in July, the Riksbank estimated that CPIF inflation for July would amount to 0.70 per cent. The outcome was 0.94 per cent, that is, more than 0.2 percentage points higher than expected. For the market, the forecast error was even larger at 0.4 percentage points. And this was in spite of the market's forecast having a strong informational advantage over the Riksbank's assessment. The positive inflation surprise can also be seen when the volatile energy prices are excluded. Excluding these prices, CPIF inflation amounted to 1.54 per cent in July, compared to the forecast of 1.31 per cent. This is the highest outcome for inflation excluding energy prices since the summer of 2010, Mr Jansson pointed out.

Secondly, recent outcomes for longer-term inflation expectations confirm that the downward trend in confidence that the Riksbank will meet its inflation target has been broken.[1] After having shown a low-frequency downward trend for several years, longer-term inflation expectations turned upwards or stabilised over the spring and summer. Expectations are still a few tenths of a percentage point below 2 per cent but the important point is that the downward trend has now been stopped, stressed Mr Jansson.

[1] According to TNS Sifo Prospera. See http:/www.prospera.se/inflation-expectations/.

This slightly increases the Riksbank's possibilities for "seeing through" variations in energy prices and other, more transitory effects on inflation, he continued.

Thirdly, developments have confirmed for some time that the Riksbank's expansionary monetary policy is having an effect. The repo-rate cuts are having an impact on the relevant short-term market rates and the purchases of government bonds are also pushing rates with longer maturities downwards. At the same time, the krona exchange rate has weakened since last year, which has contributed towards higher prices for imported goods and services. This provides an important explanation for the recent rise in inflation, said Mr Jansson.

Fourthly, economic developments in Sweden underline that conditions are favourable for a sustainable rise in inflation towards the inflation target. In recent years, unit labour costs, – which are usually a good indicator of underlying inflationary pressures – have increased more or less at a historically normal rate. This reflects solid growth in domestic demand and a resilient labour market with trend increases in both the employment rate and the labour force participation rate. In turn, this is paving the way for Swedish companies to be able to successively raise their prices, particularly when international economic activity is improving and demand for Swedish exports is rising. However, while we are on the way there, it will be important for the krona exchange rate to continue to contribute positively to inflation. Otherwise there will be a risk that the rise in inflation will be delayed. This delay could be significant if such a scenario also leads to inflation expectations starting to fall again, reasoned Mr Jansson.

Mr Jansson then went on to discuss the arguments for making monetary policy more expansionary. He noted that these are very much linked to international developments and risks.

Recently, there have been significant falls in oil and commodity prices. Unease is now high that these price falls will further push down both actual and expected inflation. The difficulties in getting inflation to rise in recent years mean that it cannot be ruled out that longer-term inflation expectations may also be affected. In this case, it would be even more difficult to achieve a higher rate of inflation.

The falling commodity prices are a consequence of, among several things, the Chinese economy slowing down and successively being readjusted away from the commodity-heavy industrial sector. This is one explanation for the fall in value of currencies in many emerging market and developing economies that are dependent on commodity exports to China. This development may also be significant for the Federal Reserve and the ECB. It cannot be ruled out that the Federal Reserve will react by postponing its policy-rate increases slightly and that the ECB will communicate an intention to further increase its purchases of securities. As current interest rates and exchange rates are determined by expectations of the future, this could rapidly lead to tighter monetary conditions in the Swedish economy, said Mr Jansson.

Mr Jansson thereby reached the conclusion that it is primarily via lower inflation expectations and a stronger exchange rate that the unease abroad risks negatively impacting the Riksbank's ability to achieve a continuing rising inflation trend. The facts that the longer-term inflation expectations have fallen for an extended period and that the exchange rate could rapidly develop unfavourably argue in favour of an early reaction to these risks. At the same time, the slightly brighter inflation outlook gives the Riksbank a certain scope to "wait and see", concluded Mr Jansson.

One fairly important circumstance from a decision-making point of view is that the improvements to inflation consist of outcomes known with certainty while the international factors are largely made up of uncertain risks. This, combined with the Riksbank's rapid capacity – even between ordinary monetary policy meetings – to make new decisions to render monetary policy more expansionary, argues in favour of the "wait and see" strategy. Noting that it was this strategy that he himself had decided to support after weighing all the arguments up, Jansson emphasised that the scope for “waiting and seeing” was not big and that the strategy assumes preparedness for a rapid rethink should circumstances change.

As regards future monetary policy, Mr Jansson said that it is important to note that it is not possible to expect a situation in which every inflation outcome corresponds exactly to the Riksbank's forecast. Monetary policy cannot precisely steer inflation and it is likely that future developments will be characterised by certain setbacks, particularly as energy prices are so volatile at present. So the decisive point is not whether the Riksbank's forecast is realised precisely but whether the upward trend in inflation can be maintained.

Until autumn next year, the Riksbank now expects energy prices to subdue inflation slightly more than previously anticipated but the reverse will apply thereafter. Since energy prices are currently extremely volatile and difficult to predict, inflation excluding these prices may very well be slightly lower or slightly higher than is assumed in the current forecast. Under current circumstances, therefore, it is primarily inflation excluding energy prices that needs to continue to demonstrate an upward trend. If this happens, there is also a good chance of inflation expectations continuing to develop positively. The forecast revisions for CPIF inflation excluding energy prices are now very small, Mr Jansson pointed out.

So, under what circumstances may it then, in the period ahead, be appropriate to make monetary policy more expansionary and how could this be done, wondered Mr Jansson. As he sees it, one needs here to differentiate between two different scenarios.

In the first scenario, international unease will have a greater effect on the longer-term inflation expectations of agents, making it more difficult for the Riksbank to maintain the upward inflation trend. This scenario perhaps involves a slightly faster slowdown in the Chinese economy than anticipated at the same time as low inflation for a long period will cause falling oil and commodity prices to have more of an impact on inflation expectations than they normally would. This development could affect the timing in monetary policy at both the Federal Reserve and the ECB. Given such a development, a stronger krona exchange rate would certainly not make things easier. Overall, the conditions for Swedish monetary policy would change somewhat but it is not a question of moving the goalposts entirely. Mr Jansson felt that in such a scenario it may be sufficient to react by cutting interest rates and extending the purchase of securities. By how much rates would need to be cut and purchases of securities extended would, of course, depend on the circumstances.

The other scenario is characterised by a similar course of events, but here the problems will be significantly greater. Perhaps the Chinese economy slows down more markedly and the spillovers to other emerging market and developing economies are extensive. Both the Federal Reserve and the ECB may then see a need to revise their plans for monetary policy more substantially. If so, the krona risks being exposed to substantial appreciation pressure and several factors will contribute to push down inflation expectations. Mr Jansson believed that in this scenario, doing "more of the same" would probably not be sufficient and that more extensive interventions by the Riksbank would probably be required. In addition to new rate cuts and purchases of securities, foreign exchange market interventions and possibly even measures to help companies or banks deal with liquidity and funding difficulties may become necessary.

Governor **Stefan Ingves** began by saying that he supports the proposal to hold the repo rate unchanged at –0.35 per cent and leave the repo rate path basically unchanged. He also felt it appropriate to continue the purchases of government bonds as planned in July. Mr Ingves stated that he shares the view of international developments and the Swedish economy presented in the draft Monetary Policy Report.

Despite recent international unease, the recovery abroad is expected to continue. Growth is primarily being driven by developed countries and is expected to be more subdued in emerging market economies.

In the United States, the labour market is improving, consumption is healthy and people are optimistic about the future. The assessment is also that inflation will rise towards the two-percent mark. This should provide impetus for other countries. Recovery in the euro area is slower and the indicators more divided. The acute uncertainty surrounding Greece has subsided but it will take a long time to reverse the trend there. As in July, the Riksbank expects continued moderate growth in the euro area.

In China, a sharp fall in the stock market has been noted following a dramatic rise. The fall itself should not contribute to a rapid slowdown of the economy since only a small fraction of households own shares. GDP growth is also expected to slow down. But a number of real economic indicators point to risks of a more substantial decline. Furthermore, it is difficult to assess the reliability of GDP statistics in China.

Developments in the Chinese economy have also contributed to high volatility on global currency and stock markets and have been one of the factors behind lower commodity prices. It is mainly currencies in emerging market economies that have weakened, especially in commodity-producing countries.

Mr Ingves noted that the overall picture of growth internationally is nevertheless rather similar to the one presented in the July Monetary Policy Report. GDP growth in the countries that are most important for Swedish exports (KIX-weighted) is basically the same as it was in July, although the contributions from the various countries are slightly different.

Inflation has risen slightly during the second quarter among many of Sweden's trade partners. This is mainly due to the effects of the earlier fall in oil prices starting to wane. Oil prices have fallen again during the summer and have once again subdued inflation internationally. Overall, KIX-weighted inflation has been revised down slightly but is expected to rise from 1.1 per cent this year to 2.4 per cent in 2017.

The recovery abroad is expected to continue. Together with low domestic interest rates, this will contribute to faster-than-average GDP growth in Sweden during the forecast period.

CPI inflation in Sweden has been low for several reasons. The trend for prices of goods and services has been weaker than normal for some time. Falling energy prices have also subdued inflation, especially over the last twelve months. Previous cuts to the repo rate have also dampened the CPI.

The Riksbank now expects inflation to rise. The inflation trend points upwards. Different measures of underlying inflation have, for example, increased since the end of last year. Goods and food prices are currently rising faster than their historical average. The rate of increase in prices for services is closing in on its historical average. The negative contribution of energy prices to inflation is furthermore expected to decrease in the period ahead and turn positive around the turn of the year.

The forecast for inflation, measured in terms of the CPIF excluding energy, is basically unchanged since the July report. Compared with the July report, energy prices and household interest expenditure are expected to develop slightly less strongly, meaning that the forecast for CPIF and CPI inflation has been adjusted downwards somewhat. CPIF inflation is expected to be close to 2 per cent during 2016.

Mr Ingves then mentioned a few risks associated with the assessment and with the monetary policy deliberations.

Recent international unease underlines the fact that the development of GDP growth abroad is difficult to assess. Emerging market economies that recovered quickly after the crisis are now growing slightly more slowly, while developed countries that had a more sluggish recovery are growing slightly faster. Swedish exports seem to have done reasonably well despite this variation, according to Mr Ingves.

Moreover, global trade decreased during the first half of 2015. Swedish exports have not, however, been pulled down to the same extent. It looks as though increased Swedish export market shares are counteracting the decline in global trade. Sweden's current account also continues to show a substantial surplus. But there is uncertainty surrounding international developments which we must be well aware of. If the international and financial unease regarding China and other emerging market economies continues, growth in Sweden also risks being affected, Mr Ingves said. The same probably applies if global trade were to stagnate for a long time.

In a world with the free movement of capital, the room for manoeuvre for domestic monetary policy is obviously affected by monetary policy in other countries. About twelve months ago, the Riksbank needed to make monetary policy more expansionary, partially as a result of what other central banks were doing and were expected to do. After that, the Riksbank has continued to loosen monetary policy and also introduced unconventional measures. But a fundamental international factor affecting domestic monetary policy remains the future actions of the central banks in the large currency areas. An earlier and faster appreciation of the krona exchange rate than forecast would risk subduing inflation. It is therefore important that the picture of the Federal Reserve's expected rate hikes becomes clearer, Mr Ingves added. It is also important for GDP growth in the euro area to improve to an extent that allows the ECB to revert to a more normal monetary policy. Mr Ingves noted that, historically speaking, it is remarkable that the Swedish yield curve is partly negative and is below or equal to the German curve. This is a simple measure of current monetary policy expansiveness.

Mr Ingves also pointed out that there are other risks that are difficult to quantify. Further oil price falls pose a risk of lower inflation and inflation expectations. At the same time, the volatility of the oil price makes the situation even more difficult to assess.

Mr Ingves also expressed his opinion that the inflation path looks reasonable in the period ahead given the current monetary policy. The inflation trend in Sweden points upwards. But we cannot be certain that inflation will develop as forecast. There has recently been considerable international and financial unease and its effect can be argued in many different, but not unreasonable ways. This means that monetary policy finds itself somewhat "on hold". Either inflation will develop as forecast, in which case the policy plan remains in place, or inflation will be lower than forecast, in which case the policy needs to be altered. The option to make monetary policy even more expansionary still remains. Neither has the Riksbank reached the end of the road as regards using the balance sheet for monetary policy purposes and there is a preparedness to act between the ordinary monetary policy meetings, if need be.

In conclusion, Mr Ingves wished to reiterate what had been said on previous occasions. When monetary policy is very expansionary and the policy rate is negative, it must be supplemented with macroprudential measures. Monetary policy deliberations have been very difficult over the past twelve months. But since it is easier for the central bank to stimulate demand, keep an eye on the exchange rate and push up inflation, it must be the task of other authorities to concentrate on subduing the mortgage market. If they can't, there is a clear risk of very poor development in the Swedish economy later on.

Mr Ingves noted that there is an ongoing discussion outside the Riksbank as to whether the Bank should also purchase mortgage bonds or not. In light of the fact that he has, on numerous occasions, maintained that we should have two interest rates in Sweden, with a higher rate for the mortgage market, Mr Ingves said that he does not feel the time is right to consider purchasing mortgage bonds. On the contrary, the market should be tightened in some way or other, given the risks we now see.

Deputy Governor **Henry Ohlsson** began by saying that he supports the proposal to leave the repo rate unchanged and leave the repo rate path basically unchanged.

Mr Ohlsson further noted that the inflation rate has bottomed out and started to pick up. And, although the monthly measurements vary somewhat, the trend is still clear. But there are threats to the rise towards the inflation target. International unease and the expansionary monetary policy of the European Central Bank may cause the Swedish krona to appreciate.

Furthermore, inflation expectations are still below the inflation target of 2 per cent. The latest measurements can be interpreted as the beginning of a rise in inflation expectations, even though the monthly measurements vary somewhat. Five-year expectations among money market participants stood at 1.8 per cent in August, close but still under the target. It is desirable for credibility's sake that expectations move up towards the target. This argues in favour of continued expansionary monetary policy. It is therefore important to complete the planned purchases of government bonds in order to increase inflation and inflation expectations, Mr Ohlsson stated. He did not feel, however, that the repo rate should be cut further in the current economic climate.

A question one might ask oneself, Mr Ohlsson said, is what to do if we start to get close to full resource utilisation in the Swedish economy. As he sees it, there are both signs starting to indicate this and signs suggesting the opposite. Current GDP growth is rapid and the forecast in the Monetary Policy Report is for it to be even more rapid in the coming years. This could suggest that we are rapidly moving towards high resource utilisation. At the same time, the population is growing much more rapidly than it has done previously. This means that it will be even more important than before to differentiate between overall GDP growth and per capita GDP growth. As the Monetary Policy Report points out, per capita growth is more modest and is expected to remain so in the coming years. This could suggest that we are not moving rapidly towards high resource utilisation, Mr Ohlsson said.

There are also other signs indicating spare capacity in the Swedish economy. Unemployment remains on what Mr Ohlsson considers to be a high level, even if it has fallen during 2015. According to the Swedish Labour Force Surveys (LFS), unemployment was 6.5 per cent (not seasonally adjusted) in July 2015. This can be compared to 7.1 per cent in the same month last year.

The number of employed persons is indeed increasing but so too is the labour force. This means that unemployment is not falling so fast. The rapid population growth plays an important role here as well. With rapid population growth, it will be more important than before to highlight the labour force participation rate and the employment rate in order to understand the development. This is something that is done in the Monetary Policy Report, Mr Ohlsson noted.

At the same time, he felt that there are several signs on the labour market that spare capacity may not be so substantial. The number of job vacancies as a share of the labour force is currently on the same level as before the financial crisis, according to Statistics Sweden's short-term job vacancy statistics. Arbetsförmedlingen's statistics show that the number of unfilled job vacancies is currently higher than before the financial crisis. In addition, the National Institute of Economic Research's Business Tendency Survey indicates a growing labour shortage. This shows that there are major matching problems on the Swedish labour market, with high unemployment and yet a shortage of labour, Mr Ohlsson concluded.

Another way is to look at the situation for unemployment insurance fund members who can be said to have a relatively strong position on the labour market. According to Arbetsförmedlingen's statistics for July 2015, open employment among fund members was 2.6 per cent. The corresponding figure a year ago was 2.8 per cent. The difference between 2.6 per cent unemployment among fund members and 6.5 per cent unemployment in the entire labour force also says something about the major discrepancies on the Swedish labour market.

The conditions for monetary policy set by current resource utilisation and the outlook for it in the years ahead are well reflected, according to Mr Ohlsson, by the current repo-rate path.

In conclusion, Mr Ohlsson felt that an unchanged repo rate, a basically unchanged repo-rate path and completion of the planned purchase of government bonds together represent a well-considered expansionary monetary policy, bearing in mind the current state of the Swedish economy. Mr Ohlsson also said that he supports the Monetary Policy Report.

§3. Discussion

Deputy Governor **Martin Flodén** explained that he wished to say a few words about his view of the inflation target and the Riksbank's monetary policy strategy. In the last few months, an increasing number of commentators have suggested that the Riksbank should reconsider the inflation target and change strategy. The arguments vary from person to person but can be summarised thus: the Riksbank should be satisfied with the current development, i.e. low inflation and reasonably good growth. As a result, the Riksbank should either reduce the inflation target or be more tolerant of an inflation rate that is lower than the target for a prolonged period. With a lower inflation target, it is argued, the Riksbank could immediately raise the repo rate back into positive territory and hence ensure that households and pension fund managers receive sufficient return on their investments, instead of enticing them to make riskier investments by having negative interest rates.

Mr Flodén pointed out that this is an argument with which he does not agree at all, even though he can perfectly understand why people feel that monetary policy with negative interest rates is a strange phenomenon. The current economic development, with low inflation and reasonably healthy growth, is of course not independent of the monetary policy pursued by the Riksbank. With a tighter monetary policy, inflation would be even lower and growth weaker. And if we also reduced the inflation target, either permanently or temporarily, inflation expectations would probably decrease. This would contribute to even lower inflation and could also lead to further falls in already low nominal long-term rates. Mr Flodén can therefore not see how such a change in the monetary policy strategy would lead to a better economic outcome.

Mr Flodén noted that his argument naturally presupposes that the current monetary policy strategy contributes to higher inflationary pressure. Otherwise, cutting the interest rate to negative levels and purchasing large volumes of government bonds would, of course, be unjustified. He pointed out that he has already mentioned several indicators suggesting that the monetary policy is actually working and has contributed to higher underlying inflation. It is also important to note that the negative interest rate and asset purchases thus far seem not to have given rise to any clear disruptions on the markets. A negative interest rate is primarily a phenomenon on certain financial markets, the participants of which are specialists who see that things are mostly working the same as when the interest rate is positive. Households can read about negative rates in the newspaper but have, as before, zero interest on their bank accounts and positive interest on their mortgages. There has hence been no reason for them to react any differently in the wake of recent interest rate cuts. For example, the demand for cash has not increased. And, according to the Riksbank's assessment, the rather extensive purchases of government bonds have not led to poorer liquidity on the market. There are participants who are being negatively affected by low interest rates, for example pension fund managers who have pledged a certain minimum nominal return. But their main problem is the fact that long-term interest rates are low, something which can be explained by low expectations of future inflation and growth. The aim of the pursued monetary policy is, of course, to push up inflation and inflation expectations, as well as to contribute to healthy growth, which will also lead to higher long-term rates. A lower inflation target or tighter monetary policy would in no way benefit these participants.

The most obvious problem that Mr Flodén associates with the low repo rate is the continuing rise in household indebtedness and the fact that this may be happening with unreasonable expectations of future interest rate levels. Bearing in mind what Mr Ingves and Ms af Jochnick had just said, as well as a great many previous statements from the Riksbank, Mr Flodén emphasised that this is a problem than can and should be dealt with by the Government, the Riksdag and other authorities using macroprudential tools.

Deputy Governor **Per Jansson** noted that, in order to save time in his previous contribution, he did not discuss the problems on the Swedish housing market and with household debt. He wished therefore to underline that he shares the view expressed by Ms af Jochnick and Mr Ingves in this area. The data clearly indicate that the problems are getting worse and the long delay in deciding on measures to counteract the risks is thus problematic, Mr Jansson said.

He also wished to take the opportunity to say that there is a growing need to identify and analyse other types of financial imbalances that can occur as a result of the extremely expansionary monetary policy. This is an important task for both the Riksbank and Finansinspektionen going forward.

In conclusion, Mr Jansson wished to point out that he also agrees with much of what Mr Flodén had just said. The wide range of opinions on monetary policy – there are, for example, some who wish to reduce the inflation target while others wish to raise it – in itself suggests that it is too early to draw conclusions and make changes. In general, he felt that Sweden needs to safeguard the important reforms of the 1990s. This applies in particular to the reforms of monetary policy, fiscal policy and wage formation. It is clear that these reforms play a key role when it comes to explaining why Sweden has coped much better than many other countries during the financial crisis and subsequent years. Mr Jansson was therefore of the opinion that we would be wise to proceed cautiously with changes, so that we do not "throw the baby out with the bathwater".

Governor **Stefan Ingves** then summarised the discussion. The Executive Board agreed on the description of economic prospects and the inflation outlook in the draft Monetary Policy Report.

The expansionary monetary policy in Sweden has contributed towards economic activity strengthening, the labour market situation improving and there being a clear upward trend in inflation since last autumn.

The recovery is continuing abroad. But developments there are still surrounded by great uncertainty due to the fall in the price of oil and large fluctuations on the stock and foreign exchange markets.

Lower energy prices due to the fall in oil prices have led to a downward revision to CPIF inflation in the period ahead but, nevertheless, inflation is expected to rise clearly and the forecast for the CPIF excluding energy remains basically unchanged since the assessment made in July.

All in all, developments in Sweden and abroad have been in line with the assessment in July and the revisions to the forecast are small.

The Executive Board therefore unanimously decided to leave the repo rate unchanged at –0.35 per cent and to continue to purchase government bonds until the end of the year according to the plan determined by the Executive Board in July.

Given the uncertainty surrounding international developments, the Executive Board also agreed unanimously that the Riksbank needs to maintain a high level of preparedness to make monetary policy even more expansionary, even between ordinary monetary policy meetings, should the inflation outlook deteriorate.

By pursuing a continued highly expansionary monetary policy, the Riksbank is supporting the positive development of the Swedish economy so that CPIF inflation can be expected to be close to 2 per cent next year.

The meeting also discussed developments in China and other emerging market economies and the risk that the volatile oil price will influence the inflation assessment. It was noted in various ways that the development of the Swedish krona will continue to be important. Several members of the Executive Board also discussed how much scope there is for making monetary policy more expansionary. Finally, several members of the Executive Board emphasised that there is a great need to manage mandates and tools within the area of macroprudential policy promptly.

§4. Decision on the Monetary Policy Report and the repo rate

The Executive Board decided after voting

• to adopt the Monetary Policy Report according to the proposal, Annex A to the minutes,

• to publish the Monetary Policy Report on 3 September 2015, at 9.30 a.m.,

• to hold the repo rate unchanged at –0.35 per cent and that this decision would apply from Wednesday, 9 September 2015,

• to publish the decision above at 9.30 a.m. on Thursday 3 September 2015 with the motivation and wording contained in a press release, and

• to publish the minutes of today's meeting on Wednesday 16 September 2015 at 9.30 a.m.

This paragraph was verified immediately.

Minutes by

Lena Eriksson

Verified by:

Stefan Ingves	Martin Flodén	Per Jansson
Kerstin af Jochnick	Henry Ohlsson	Cecilia Skingsley