Minutes of monetary policy meeting

OCTOBER 2012

Summary

At the monetary policy meeting on 24 October, the Executive Board of the Riksbank decided to leave the repo rate unchanged at 1.25 per cent and to adjust the repo-rate path downwards.

At the meeting on 24 October, it was noted that inflationary pressures are lower and that the recovery on the labour market will be more sluggish than assessed in September. The Executive Board agreed that the repo rate therefore needs to be low for a longer period in order to stimulate the economy and bring inflation in line with the target. However, as at earlier meetings, there were differences with regard to how expansionary monetary policy should be.

Four Board members considered it appropriate to keep the repo rate unchanged at 1.25 per cent. Cutting the repo rate now would not have a particularly significant impact on inflation and economic activity in the year ahead but would, on the other hand, risk leading to inflation being above the target in 2014 and 2015. Two members wished to cut the repo rate, one by 0.25 percentage points and the other by 0.5 percentage points, in order for inflation to attain the target more quickly and for unemployment to begin falling earlier.

All of the members considered it appropriate to adjust the repo-rate path downwards. A majority consisting of four of the members considered that the downward adjustment of the repo-rate path proposed in the draft Monetary Policy Report represented an appropriate balance. They considered that this would lead to CPIF inflation reaching 2 per cent after just over one year and to resource utilisation normalising. The assessment was that the low repo-rate path would mean that the households' debt ratio would not increase but remain at the current level. However, two members considered that there was scope for an even lower repo-rate path and believed that such a path would more quickly lead to an inflation rate of 2 per cent and an unemployment rate closer to a long-run sustainable rate.

All of the members considered that the situation in the euro area remains uncertain and that the downturn there will be more prolonged as a result of the underlying structural problems that continue to burden the economies in the region.

The members agreed that the growth of Swedish GDP is now slowing down following strong growth so far this year and that the recovery on the labour market will be more sluggish than expected. The members also agreed that there are unutilised resources in the Swedish economy at present, although there were different assessments of the level of resource utilisation. There were also different assessments of what monetary policy can achieve at present with regard to reducing unemployment.

All of the members discussed the households' high debt ratio in various ways. However, there were different views on the risks this may pose to the economy. The members expressed a wish for this issue to be taken into account to a greater extent in the analysis in the future.

MINUTES OF MONETARY POLICY MEETING
Executive Board, No. 5

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DATE: 24 October 2012

TIME: 9:00

PRESENT:
Stefan Ingves, Chairman
Karolina Ekholm
Per Jansson
Kerstin af Jochnick
Barbro Wickman-Parak
Lars E.O. Svensson

Johan Gernandt, Chairman of the General Council (§§ 1 and 2)

Meredith Beechey Österholm
Hans Dellmo
Charlotta Edler
Eric Frieberg
Mia Holmfeldt (§1)
Ann-Christine Högberg
Jesper Johansson
David Kjellberg (§1)
Pernilla Meyersson
Marianne Nessén
Christina Nyman
Mattias Persson (§ 1)
Maria Sandström (§ 1)
Ulf Söderström
Lena Strömberg
David Vestin
Staffan Viotti
Anders Vredin
Magnus Wiberg

It was noted that Hans Dellmo and Magnus Wiberg would prepare draft minutes of § 1, 2 and 3 of the Executive Board’s monetary policy meeting.

§1. Economic developments

Maria Sandström of the Financial Stability Department began by presenting recent developments regarding the banking sector and the public-finance situation in the euro area countries.

David Kjellberg of the Monetary Policy Department presented recent developments on the financial markets. Since the monetary policy meeting held in early September, the situation on the financial markets has been somewhat calmer, partly due to the measures taken by a number of central banks. However, uncertainty regarding developments in the euro area remains. Above all there is uncertainty about if and when Spain will apply for support from the European Stability Mechanism, ESM. In the United States, macro data indicate that development has taken a more positive course. However, there is uncertainty about the outcome of the presidential and congressional elections in the United States and about fiscal policy in the future. According to market pricing, expectations of a lowering of the repo-rate have remained unchanged since the last monetary policy meeting. The repo rate is expected to be lowered gradually over the next six months. The krona is approximately 0.5 per cent weaker than at the time of the previous monetary policy meeting.

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 2, 9, 10 and 16 October. The text of the draft Monetary Policy Report was tabled at a meeting of the Executive Board on 18 October.

Since the monetary policy meeting held in September, indicators for the euro area have pointed to somewhat weaker development. The situation looks somewhat better for the United States. All in all, economic development outside Sweden has been weak, but more or less in line with expectations. Unease on the financial markets has subsided somewhat, partly as a result of measures taken by the ECB. The outcome for Swedish GDP in the second quarter, measured as a seasonally-adjusted quarterly change, has been revised downwards from 1.4 to 0.7 per cent, at the same time as indicators point to a slowdown during the third quarter. However, growth will normalise during the course of 2013. Employment has increased, but the number of individuals in the labour force has increased even more, and unemployment has therefore risen marginally. Indicators, for example redundancy notices, suggest that the labour market will be weaker in the period immediately ahead, and unemployment is expected to rise further. The recovery of the labour market is now expected to begin a little later and to be more sluggish, which partly relates to the fact that there are signs that it has become more difficult for job seekers to find vacant jobs. Both CPI and CPIF inflation are expected to be lower in the year ahead compared with the assessment at the previous monetary policy meeting, which is mainly due to lower energy prices. Lower inflationary pressures and a higher rate of unemployment than expected justify a lower repo-rate path. Christina Nyman of the Monetary Policy Department pointed out during the course of the meeting that the Economic Tendency Indicator of the National Institute of Economic Research for October fell because households as well as companies in all sectors were more pessimistic.

§2. Discussion of economic developments

Deputy Governor **Lars E.O. Svensson** began by noting that the current situation and the outlook for the global economy and the Swedish economy look bleaker than previously. Both CPIF and CPI inflation are well below the target. In September, CPIF inflation was 0.9 per cent and CPI inflation was 0.4 per cent.

Unemployment is very high, 7.8 per cent in seasonally-adjusted terms in September, increasing and well above any reasonable assessment of the long-run sustainable rate of unemployment. Compared to the midpoint 6.25 per cent in the interval 5-7.5 per cent, which the Riksbank considers to be the interval for a long-run sustainable rate of unemployment, the unemployment gap is approximately 1.6 percentage points, which corresponds to around 80 000 unemployed. As Mr Svensson showed in an Appendix to the minutes of the monetary policy held on 3 July, there are in his opinion strong reasons why this midpoint is a systematic overestimation of approximately 0.75 percentage points, as it has not taken into account the fact that average inflation has fallen below the average level of inflation expectations as measured in the Prospera surveys. This makes 5.5 per cent a better estimate of the long-run sustainable unemployment rate. This would mean that the unemployment gap is approximately 2.3 percentage points, which corresponds to approximately 115 000 unemployed. The unemployment rate in Sweden is now almost as high as in the United States, that is 8.1 per cent in August, and as in the United Kingdom, that is 8.0 per cent in June. There are also countries comparable to Sweden that have much lower rates of unemployment: Germany 5.5 per cent, the Netherlands 5.3 per cent, Austria 4.5 per cent and Norway 3.0 per cent.[1]

All in all, this represents very poor target attainment, said Mr Svensson. It would have been better with a more expansionary monetary policy from the summer of 2010 and onwards instead of the series of repo-rate increases that began then.

Why then is monetary policy so tight, despite low inflation and high unemployment? In this context, Stefan Ingves, in an op-ed in *Svenska Dagbladet,* and Per Jansson, in an op-ed and interview in *Dagens Nyheter,* have made statements that must reasonably be interpreted to mean that monetary policy should focus on limiting household

[1] OECD Main Economic Indicators

indebtedness, that is that the repo rate should be set with regard to the effects on housing prices and indebtedness.

Here Mr Svensson wished to put a question directly to Stefan Ingves and Per Jansson. If household indebtedness was not a problem, would they then support a repo-rate cut now?

If one believes that monetary policy should focus on limiting household indebtedness, then two issues should be resolved. First, one should be able to demonstrate that household indebtedness is a problem. Second, one should be able to show that the repo rate and monetary policy are effective tools for limiting household indebtedness.

Mr Svensson addressed the second issue first. One must then ask what effect monetary policy has on household indebtedness. As there is a link between housing prices and indebtedness – the households' debts mainly consist of mortgages and mortgages have a stable relation to housing prices – one can ask how monetary policy affects housing prices. This is an area that has been thoroughly researched and several different research papers using different approaches and data from various countries and periods of time, including the Riksbank's own inquiry into risks on the Swedish housing market, which was published in April 2011, provide a similar result.[2] This result is as follows: raising the policy rate to reduce housing prices has very high real-economic costs and these costs are, in Mr Svensson's opinion, unacceptably high. Every per cent by which one wishes to reduce housing prices leads to an approximately 0.6 per cent reduction in GDP and a 0.3 per cent increase in unemployment, which corresponds to approximately 15 000 individuals.

A one per cent fall in housing prices eventually leads to reduced indebtedness. However, as disposable income also falls the debt ratio decreases by less than 1 per cent. Here Mr Svensson put a new question to Stefan Ingves and Per Jansson. Did they agree with these calculations or did they have others that they wished to present?

One per cent lower housing prices cannot reasonably be said to affect the risks to financial stability. One may wish to reduce housing prices by at least 10 per cent. But this would cost at least a 6 per cent reduction in GDP and a 3 per cent increase in unemployment, which corresponds to approximately 150 000 more unemployed individuals.

In Mr Svensson's view the conclusion was rather obvious. One should not use the policy rate to try to affect household indebtedness, even if one believes that household

[2] Assenmascher-Wesche, Katrin and Stefan Gerlach (2010), "Credit and Bubbles", Economic Policy, vol. 25, pp. 437-482; and Claussen, Carl Andreas, Jonsson, Magnus and Björn Lagerwall (2011), "A macroeconomic analysis of housing prices in Sweden", the Riksbank's inquiry into risks on the Swedish housing market, April 2011, pp. 67–95.

indebtedness is a problem. It simply does not appear to be possible to use the policy rate and monetary policy to significantly affect household indebtedness without prejudice to the mandates of price stability and high employment. One should instead use other much more effective tools, such as mortgage caps, regulations governing deductions for interest paid on mortgages, taxes, capital requirements, risk weights and so on. These instruments are more targeted and do not incur the same devastating real costs. According to the report on the housing market that Finansinspektionen published in March 2012, the mortgage cap has had an effect and the loan-to-value ratio for new mortgages is falling for the first time for many years.[3]

A more fundamental issue arises because housing prices and indebtedness in relation to disposable income form part of the real economy. But monetary policy cannot normally have a lasting effect on the real economy. Monetary policy is stabilisation policy, not structural policy, and normally has real effects for only a limited period of time. Monetary policy usually has no long-term real effects.[4] Structural policy measures are required to create long-term real effects. Examples in the case of household debt include mortgage caps, taxes, deduction regulations, risk weights for mortgages and macroprudential policy.

An entirely different issue is the first issue about whether the current level of household debt is a problem at all, that is whether the level of indebtedness is sustainable or not and whether the borrowers and the lenders – the banks – have sufficient resilience to cope with disruptions. A lot could be said about this according to Mr Svensson, but he was content to note that the households have very strong balance sheets. This can be seen in Figure 1. The households have debts equivalent to approximately 170 per cent of disposable income. However, they have total assets, excluding collective pension claims, of approximately 510 per cent of disposable income, that is three times the debts. The households' "leverage ratio", that is, their net wealth in relation to total assets, is thus approximately 70 per cent. As a comparison it can be noted that the new regulatory framework Basel III stipulates that the banks should have a leverage ratio of at least 3 per cent.

Figure 1 also shows that the relation between debts and total and real assets is stable and has no clear trend. In addition, the households' collective pension claims are growing as a percentage of disposable income and are now more than 120 per cent of disposable income. These pension claims of course have an impact on the ability to service debt, even though they are not freely at the disposal of the households. As can also be seen in

[3] "Den svenska bolånemarknaden" (The Swedish mortgage market), report from Finansinspektionen, 13 March 2012.

[4] One exception is when average inflation deviates from average inflation expectations for a long period of time, see Svensson, Lars E.O. (2012), "The Possible Unemployment Cost of Average Inflation below a Credible Target", www.larseosvensson.net

Figure 1, the household savings ratio is at an historically high level, which contributes to a sustainable situation. The households' debts are thus not being used to fund consumption.

Deputy Governor **Karolina Ekholm** began by noting that she, like Mr Svensson, considered that the prospects for the Swedish economy have, if anything deteriorated since the meeting in September. Development in the euro area continues to look weak and it appears that it will take some time before we see a recovery. A number of new proposals and measures to manage the problems in the euro area have been announced, for example the ECB's new programme for purchasing of sovereign bonds on the secondary market, that is the OMT programme, the proposal on joint banking supervision and the establishment of the ESM. She said that the OMT programme has probably reduced the risk of a very negative scenario, but noted that we have still not seen how the programme will work in practice as no country has at present qualified to join it. According to Ms Ekholm, there are still too many things that need to be put into place – and to be designed in such a way that they really work – for the current underlying uncertainty about developments in the euro area to disappear or decrease in any substantial way.

The assessment in the draft Monetary Policy Report is that the recovery in the euro area will be somewhat slower than forecast in the Monetary Policy Update in September, which Ms Ekholm believed was reasonable. The figures for GDP growth in 2013 and 2014 have been revised downwards with a few tenths of a percentage point. This has consequences for the prospects for the Swedish economy, which is meeting weaker export demand from the euro area. Ms Ekholm pointed out that among our most important export markets it is only Norway that is doing really well. There the economy is booming with relatively high growth and low unemployment. However, inflation is low, partly as a result of a strong currency.

Ms Ekholm said that, as usual, the forecast for foreign policy rates plays an important role when assessing what may be an appropriate monetary policy for Sweden. In the forecast in the draft Monetary Policy Report these policy rates have been revised downwards somewhat towards the end of the forecast period, partly because the Federal Reserve has communicated that it expects to keep the policy rate low for a longer period of time than it communicated previously.

Ms Ekholm also said that in a small, open economy like Sweden's the domestic policy rate cannot deviate too much from policy rates abroad without the risk of affecting the exchange rate in a way that makes it difficult to attain the inflation target. Inflation in Sweden is, as in Norway, clearly below the inflation target and in both cases a strengthening of the currency is an important factor behind this, according to Ms Ekholm. If the currency continues to strengthen it will be difficult to reach the inflation target.

According to the forecast in the draft Monetary Policy Report it will take quite some time before inflation in Sweden reaches 2 per cent. Ms Ekholm emphasised that there is nothing to prevent inflation from deviating from the target for a limited period of time given the flexible inflation targeting pursued by the Riksbank. However, given the fact that average inflation has been below 2 per cent since the introduction of the inflation target, she felt that it is unfortunate that this tendency will now be reinforced in that inflation will be below the target until into 2014. She said that this may reduce confidence in the inflation target. Ms Ekholm also said that from this point of view the low policy rates that we expect to see abroad place a restriction on how high the repo rate can be set, at least as long as monetary policy is conducted on the basis of an inflation target.

Ms Ekholm noted that, as before, there was some difference between the forecast for foreign policy rates and market expectations as expressed in implied forward rates towards the end of the forecast period, as can be seen in Figure 3. To a certain extent this difference relates to the fact that market expectations regarding the policy rate in the United States are lower than the median forecast of the members of the Federal Open Market Committee towards the end of the forecast period.[5] Ms Ekholm considered it justified to take into account the communication from the central bank and that some deviation between the forecast and market expectations is therefore reasonable in this case. However, she was not sure that this explains all of the difference between the forecast for foreign policy rates and market expectations, so it may be the case that the policy-rate forecast has once again ended up somewhat higher towards the end of the forecast period than the level that Ms Ekholm would prefer. But, as at the latest meetings, Ms Ekholm did not consider that this deviation is large enough to justify questioning the forecast as such.

Deputy Governor **Per Jansson** began by declaring that at this meeting he intended to devote his time in this part of the discussion to describing his view of the risks abroad, with a focus on the crisis in the euro area. He wanted to discuss the Swedish economy during the monetary policy discussion, and it was then that Mr Jansson also intended to answer the questions put to him by Mr Svensson.

Mr Jansson initially wanted to clarify what he meant by "risks" in this context. It is inevitable that there will be some setbacks in the management of the crisis in the euro area. But this was not what he meant by “risks”. He was instead referring to different events that could pose a more serious threat to the progress of crisis management as a whole. Such events may be unlikely, but if they nevertheless do occur they will have major and worrying consequences. These are events that can hardly be captured in our

[5] The Federal Open Market Committee is the US central bank’s monetary policy committee that, among other things, decides on the policy rate in the United States.

forecasts, and it is perhaps even not desirable to do so, although this means that the forecasts are more like mode rather than mean forecasts.

Mr Jansson explained that his comments on these risks do not mean that he cannot support the forecast for the outlook abroad in the draft Monetary Policy Report, but rather that for various reasons he felt the need to clarify his own view of the risk situation. One reason is that some comments recently seem to be suggesting that the worst phases of the euro crisis are now over. Another reason is that the way one views the risks, even if they are not captured in the forecasts, has an impact on how prepared one needs to be to take action in economic policy. If the crisis in the euro area were to escalate more dramatically, then the basis for monetary policy and for Swedish economic policy as a whole would change.

Mr Jansson declared that he of course did not want to make things appear worse than they really are, but that unfortunately he could not share the view that the more serious risks had now diminished. Those who put forward the view that the risks have decreased often refer to the market development of various financial variables. He of course agreed that this has improved somewhat recently. But it is important to be clear that market developments have been significantly affected by the very extensive intervention measures that have been taken. This means that, in his view, it is not currently possible to clearly determine the real picture regarding risks simply by examining market developments.

There are several factors at present that are cause for real concern and that, if things go badly, could quickly and drastically change the more positive comments that we are hearing today.

First, there a number of serious difficulties associated with the ongoing negotiations on the so-called banking union. Expectations are high and there is a major risk that this will lead to disappointment. The schedule for this was given somewhat more concrete form at the European Council meeting last week. This may represent slight progress, but many difficult questions remain to be resolved. One factor that is fuelling concern in this context is that progress on the supervision aspects of the banking union has been seen by many as a precondition for moving forward with support for the Spanish banks. There are many question marks regarding if and how this can be done at present. In any event, the current schedule means that supervision under the banking union will probably not be in place until the second half of 2013 at the earliest. This means that even in the most optimistic scenario regarding the possibility to supply capital directly to the Spanish banks through the ESM, it will take a very long time before support is provided.

Second, Spain is facing further challenges in addition to the possible dependence of support to the banks on progress with the banking union. The banks need huge amounts of capital, and this is still under discussion. The figures vary from approximately EUR 50 billion to well above EUR 100 billion. Although it is not possible to say exactly how great the need is today, it will in any event be a question of extremely large sums. Such a large capital injection also gives rise to important questions about ownership in connection with the implementation of the support. This aspect should not be underestimated if the support is to be expedient and effective. In addition to the banking problems there is also the fact that several of the regions in Spain have financial problems.

Third, the problems in the Greek economy are far from solved. Many now say that it will be possible to pay out the next tranche in November and the Eurogroup will shortly decide on this on the basis of the troika report that has been drawn up. However, even if such a payment is made the fact remains that managing the crisis in Greece is very difficult and it is hard for the country to meet the commitments it has made. The question is what further easing will be needed and to what extent the lenders will agree to this. Unfortunately, these are questions that we will probably need to return to many times before the Greek economy is back on its feet again. A suspension of payments and a Greek exit from the EMU are not likely in the near future, but the risk of the Greek crisis deteriorating unfortunately remains.

In other words there are several major risks that could quickly and drastically lead to a much more worrying situation, said Mr Jansson. He did not mean by this that his forecast of the international outlook was different to that presented in the draft Monetary Policy Report. But the risks underline the fact that it is important to be prepared to take further actions in economic policy. Given this background, it is good that both monetary policy and fiscal policy in Sweden have some room for manoeuvre. Mr Jansson then repeated that he will return to his view of the Swedish economy in the monetary policy discussion.

First Deputy Governor **Kerstin af Jochnick** began by noting that she largely agreed with the assessment of economic developments abroad and in Sweden as described in the draft Monetary Policy Report.

The current assessment is that developments abroad will be somewhat weaker than the Riksbank forecast in the Monetary Policy Update in September. There will be some slowdown globally this year and next year but we still expect to see a recovery during the forecast period. A slight recovery is continuing in the United States. However, there is uncertainty about what form fiscal policy will take in the United States in 2013 and we will probably not know this until after the elections in November. US households are undergoing a debt adjustment process which is affecting demand in the US economy. However, there are signs of a recovery on the housing market, which is expected to make a positive contribution to growth in the longer term.

Growth in the BRIC countries will weaken this year, but the assessment is that it will contribute to the recovery of the global economy during the forecast period.

Economic development is weak in the euro area. This will have a dampening effect on Swedish growth in the year ahead. Other important Swedish export markets that are experiencing weak development are the United Kingdom and Denmark, while Norway is doing much better.

Ms af Jochnick also said that the forecast in the draft Monetary Policy report assumes that the crisis in the euro area will be managed and will gradually ease. There are also some signs of stabilisation on the financial markets. The proposed support for the Spanish banking sector, the proposed setting-up of a banking union and the decision by the ECB in September on a new support programme for government bonds appear to have calmed the markets. The proposals now under discussion will, if they are introduced effectively, promote stability in the euro area in the longer term. The important point that remains is to put these proposals into practice and to ensure that the various measures gain credibility. But it is too early to sound the all-clear. If Europe succeeds in implementing all the proposals on the table then we may see a turnaround in the ongoing crisis. Such a turnaround does not mean that the situation will immediately return to normal. It rather means that the EU will be able to shift its focus from resolving the acute crisis to developing more long-term, sustainable solutions for the financial system and public finances and to restoring the competitiveness of the crisis countries.

Turning to developments in Sweden, Ms af Jochnick said that the demand situation had been rather good in the first half of the year but that there were now signs that demand would be subdued by the weakening of economic activity abroad. The downturn will particularly affect investment goods, which constitute a large part of Swedish exports. The uncertainty abroad also means that consumption will increase slightly more slowly than normal. Rising unemployment also forms part of the picture, but this is mainly due to the fact that more people have joined the labour force. It is therefore important to note that the problems on the labour market are largely of a structural nature, as described in an article in the Report. The structural problems include the possibility for new groups joining the labour force to find work, the matching of vacancies to job-seekers and the flexibility of the wage formation process.

Ms af Jochnick then pointed out that monetary policy should aim to find an appropriate balance between stabilising inflation around the inflation target and stabilising the real economy. With regard to the possibility of monetary policy to affect, for example, the labour market, she said that monetary policy can only affect that part of unemployment that is cyclical. It cannot, however, be used to deal with structural problems on the labour market. Other policy measures are required to improve matching on the labour market.

Several factors have contributed to the current low level of inflation: the low rate of increase in unit labour costs, the strengthening of the krona and low resource utilisation.

However, inflation is expected to gradually increase next year. This is because resource utilisation is increasing and wages are rising at a faster pace. The dampening effect of the krona on import prices will also diminish. Ms af Jochnick said that she intended to return to the monetary policy assessment that forms the basis for this forecast.

Governor **Stefan Ingves** began by emphasising that he shares the view of international developments and the Swedish economy presented in the draft Monetary Policy Report. There are no major changes compared to the monetary policy assessment in September. The meetings are also quite close together, in effect perhaps too close. We are witnessing an ongoing recovery in the United States, where the housing market is gradually improving. However, there is great uncertainty about fiscal policy, at least until the elections in November. The prolonged weak development in the euro area will have a dampening effect on Swedish exports in the year ahead. Prospects are mixed on other important export markets. Norway has developed strongly, while development in Denmark and the United Kingdom has been much weaker. However, like Sweden these countries should benefit once the recovery in the euro area begins. The performance of the real economy in several emerging economies has weakened this year, but these countries are nevertheless expected to support global growth during the forecast period. This adds up to a weak, but not exceptionally weak, development of economic activity abroad.

Mr Ingves noted that the forecast is based on the assumption that the crisis in the euro area will be managed and that uncertainty will gradually fade during the course of next year. Unfortunately, it is still unclear how the costs for the reconstruction of banks in the crisis countries will be distributed and how reconstruction will be carried out. However, the technical solutions should not affect the Swedish economy in general. For the Swedish economy it is important that solutions are implemented and that uncertainty is reduced.

It is worth noting in this context that the ECB’s programme for the relief purchase of government bonds on the secondary market presupposes that a number of measures are taken by the countries concerned and that so far there has been more talk than action.

It is not easy to make forecasts against this background. It now appears that the world is behaving differently than during ”The great Moderation”, when growth was good and inflation low. The real economy abroad now seems to be more volatile at the same time as average growth is lower than it was before the crisis. The situation in the euro area is an example. Despite weak resource utilisation, inflation is now being pushed up by increased indirect taxes and food and energy prices. We have to expect the forecasts to be wrong sometimes, said Mr Ingves.

So far, the Swedish economy has been resilient during the crisis abroad, as pointed out by the IMF, for example. The regulatory framework for fiscal policy has worked well and has helped to provide room for manoeuvre in fiscal policy. With a floating exchange rate and an inflation target, normal monetary policy has also played a central role, as have the extraordinary monetary policy measures that the Riksbank took earlier. As far as he could judge, the situation in Sweden will also remain stable as, among other things, Sweden will continue to have a stable current account surplus.

Weak developments abroad will now dampen growth in Sweden. However, when international demand eventually increases Swedish exports and growth will also increase.

Housing investment in Sweden is weak, and has been so for some time. This has partly related to an adjustment process following the Swedish crisis of the 1990s. To the extent that supply is curbed by more structural factors, such as a lack of competition and building restrictions, this is a question that must be dealt with by other policy areas than monetary policy.

Mr Ingves then pointed out that unemployment has increased despite the fact that employment has developed a little better than expected. This is because more people have joined the labour force than have become employed. There are also signs of poorer matching on the labour market. The groups with a lower employment rate have increased as a proportion of the labour force.

A central issue is the view of the role of the labour market in monetary policy. To the extent that increased unemployment is due to weaker demand it constitutes a motive for a stimulative monetary policy. However, if unemployment increases because matching on the labour market is working less effectively then measures are required in other areas. Monetary policy cannot improve matching on the labour market.

The overall assessment is that resource utilisation will be weaker than normal but not as extreme as in 2008. We are now experiencing a more normal downturn. Together with the strengthening of the krona, slowly increasing wage costs and falling energy prices, this has contributed to inflation pressures being low at the moment. The inflation forecast has been revised downwards, particularly for the year immediately ahead.

The rate of increase in lending to households has stabilised and is expected to more or less correspond to the increase in incomes in the period ahead. Both monetary policy and the mortgage cap have played a role in subduing lending to households. It is important that household indebtedness does not increase further. The issue of debt requires constant attention, said Mr Ingves.

Commenting on Mr Svensson's contribution, Mr Ingves pointed out that monetary policy, like fiscal policy, sometimes tends to be too near-sighted. He maintained that an unsustainable build-up of debt may in the long term result in high unemployment and an inflation rate below the target. He also pointed out that one must ask what is an appropriate combination of monetary policy and regulations. Regulations can in some cases act as an alternative to raising the repo rate and a more detailed analysis of what is an appropriate combination of monetary policy and regulations should be conducted. Appropriate measures have been discussed earlier, but have not yet been taken.

Deputy Governor **Barbro Wickman-Parak** began by referring back to the near-sightedness in monetary policy mentioned by Mr Ingves. Ms Wickman-Parak said that it is also easy to be near sighted when assessing economic activity. One example of this is the financial crisis of 2008, when many people dismissed signs of a turnaround in economic activity as temporary factors.

This autumn, both the euro area and the United States are experiencing a critical political phase. The budget problems in the United States have previously been overshadowed by events in the euro area, but are now beginning to attract increasing attention.

Ms Wickman-Parak then referred to the fact that an important assumption for the forecast is, as previously, that the euro crisis will be managed successfully. The situation for Greece and Spain is still uncertain, but at other levels measures have been taken that at least do not reduce the realism of this assumption. Temporary setbacks can of course occur in processes of this type where national interests may clash with each other. As Mr Jansson mentioned earlier, there is a risk that the situation may deteriorate beyond this and that a new significant crisis will arise, said Ms Wickman-Parak. This would drastically change the preconditions for monetary policy and in such a crisis situation the Swedish banks could once again experience difficulties in getting funding abroad.

There are signs of some stabilisation in, for example, industrial output in the euro area, while the households and companies have become increasingly pessimistic about the future. Even in core countries like Germany and France, confidence has fallen to low levels. In the draft Monetary Policy Report it is now predicted that the recovery in the euro area will be a little slower than was previously forecast.

Outcomes and indicators in the United States show that the economy is continuing to grow at a modest rate. If anything, the statistics have been a positive surprise in most cases. All of the indicators on the housing market are pointing in the right direction. The stock of unsold housing has, for example, fallen to normal levels and the time it takes to sell property is now below the historical average. Consumer confidence has also begun to recover from low levels. Ms Wickman-Parak agreed with Ms af Jochnick that the US households need to undergo a debt adjustment process but also said that it is important to emphasise that the households have already come quite a long way in this process. The labour market is moving in the right direction, although slowly. An important assumption in the forecast is that the Democrats and Republicans will be able to reach a budget compromise so that automatic austerity measures are not triggered after the turn of the year.

Some downward adjustments of the growth figures for the emerging economies have also been made since the Monetary Policy Update in September and all-in-all the forecast in the draft Monetary Policy Report means that the figure for global growth has been adjusted downwards by a couple of tenths of a per cent for this year and the years ahead. Ms Wickman-Parak declared that she supported the forecast but wished to add that she thought growth in the United States could be higher if the budget problems are successfully resolved. This would have an impact on the euro area and the world at large. The forecast for the euro area is anything but bright, particularly for next year. However, many countries have good potential for growth once confidence returns and global demand increases. If it were not for the significant political risks in both the United States and the euro area, Ms Wickman-Parak said that she would be inclined to advocate a higher path for growth abroad next year. But we are at a critical stage at present and hopefully we will be able to see where things are going a little more clearly during the winter.

Since the previous monetary policy meeting, Statistics Sweden has revised down the figure for Swedish growth in the second quarter. This was no surprise, although the downward revision was perhaps larger than expected. It was above all the figure for exports that was adjusted downwards and new orders and other indicators point to weak development over the next few quarters. However, despite this revision the Swedish economy has continued to demonstrate strong resilience and domestic demand has grown at a rather good rate. The downward revision of the forecast for growth this year, from 1.5 per cent to 0.9 per cent, is mainly due to the weaker second quarter. On the other hand, our view of the economic outlook for next year and onwards is approximately the same as in the monetary policy update.

If growth abroad is as predicted, then the chances of a recovery of Swedish growth are favourable. The uncertain situation has led to the postponement of investment abroad, and Sweden, whose exports largely consist of investment goods, will benefit when investment gathers pace once again. The countries in northern Europe should also be those that have the greatest potential for growth and in this case Sweden will benefit from the geographical distribution of its exports. At present, the Swedish manufacturing industry has a low investment ratio and a high level of capacity utilisation. When export demand strengthens, Swedish investments should be able to increase relatively quickly. In addition, the development of household incomes is expected to be relatively positive in the period ahead and the households have a high savings ratio at present. This means that there is good potential for increased consumption and for a recovery in the Swedish economy.

Employment has been somewhat stronger than predicted in the Monetary Policy Update in September. However, as the supply of labour has increased even more, unemployment has been marginally higher in the third quarter. Unemployment is also expected to continue to increase in the period ahead, partly as a result of a slight downward adjustment of employment and partly due to an upward revision of the supply of labour. The number of redundancy notices has increased since the summer. The increase is much less dramatic than in 2009, but the rate has accelerated recently. The prolonged period of uncertainty about the state of the economy, above all in the euro area, has certainly had an impact on this. This situation may deteriorate if it takes time before we see signs of a recovery abroad. It is important to monitor this situation carefully in the period ahead, said Ms Wickman-Parak. It should be remembered that redundancy notices do not necessarily mean that people will actually be made redundant. We learned this not least in connection with the financial crisis.

Deputy Governor **Lars E.O. Svensson** then commented on Stefan Ingves' and Kerstin af Jochnick's remarks concerning poorer matching on the labour market and that aggregate demand and monetary policy cannot influence this. The discussion in the Fiscal Policy Council's report for 2012 is relevant in this context.[6] This shows that matching for both experienced and inexperienced labour is cyclically sensitive and improves when the situation on the labour market improves. It is, however, more cyclically sensitive in the case of inexperienced labour. This means that if the demand for labour increases, matching improves most for inexperienced labour. The business cycle, and thus monetary policy, therefore plays a role in how the labour market works, and a more expansionary monetary policy that leads to a higher demand for labour improves matching most for the vulnerable groups. This is not so surprising. It is after all the vulnerable groups that are most cyclically sensitive, that are dismissed first and hired last. If they are to get jobs and acquire work experience and get new jobs in the future then an extra expansionary monetary policy is required.

Mr Svensson then commented on Mr Ingves' remarks on the structural and long-term effects of monetary policy. As Mr Svensson mentioned earlier, the gross solvency of the households, that is the relation between their net wealth and total assets, is high and stable at around 70 per cent. Liabilities and assets are thus in proportion to each other. If society becomes more prosperous over time and capital and assets increase in relation to disposable income, which mainly consists of wages, it is also natural for debts to increase in relation to disposable income. If one now believes that debts are too high in relation to disposable income and wishes to reduce them, does this mean, given that debts are in proportion to assets and wealth, that one should also try to reduce the households' assets and wealth? Can monetary policy do this?

[6] Fiscal Policy Council (2012), Swedish Fiscal Policy, report of the Fiscal Policy Council 2012, chapter 5.

Deputy Governor **Per Jansson** then commented on Mr Svensson's discussion of unemployment among the "experienced and inexperienced". Achieving significant reductions in unemployment is not simply a question of counteracting small variations in employment among those with weaker links to the labour market. Just over a year ago, there was an article in the Monetary Policy Report that showed that in order for it to be possible to bring down unemployment to below 6 per cent the Swedish labour market must meet very high demands.[7] This means among other things that unemployment among young people must be substantially reduced from present levels. Mr Jansson added that it is also important in this discussion to emphasise that no-one has claimed that there are no cyclical elements in the development of the labour market. However, this is not the fundamental issue here. The OECD has carefully reviewed the problems on the Swedish labour market and during their visit to Sweden recently the OECD team did not mention interest rates or monetary policy at all in this context.

In response to Mr Jansson's remarks, Deputy Governor **Lars E.O. Svensson** then said that he was primarily talking about the effects of a more expansionary monetary policy on matching.

Deputy Governor **Barbro Wickman-Parak** agreed that there are cyclical elements in unemployment that monetary policy can influence. Many of those registered with the Public Employment Service can, according to the Service, be classified as "vulnerable". The percentage of those so classified has increased by ten percentage points since the mid-2000s. It may also be the case that the demand for simpler jobs will not return. Commenting on Mr Svensson's remarks on gross solvency, Ms Wickman-Parak noted that household solvency is indeed good at present, but the solvency of the US households just before the financial crisis of 2008 was also good. Good solvency does not therefore guarantee that households will not experience problems later on.

Deputy Governor **Karolina Ekholm** said that the role of monetary policy with regard to affecting unemployment is a very important issue that merits further study. A number of analyses have been conducted, including the article on matching on the labour market in the draft Monetary Policy Report. When a large proportion of the unemployed consists of groups that have a weak position on the labour market and therefore ahigh unemployment risk, this of course pushes up average unemployment, as explained in the article. However, Ms Ekholm agreed with Mr Svensson that there are indications that unemployment for these groups is particularly sensitive to the level of aggregate demand and that monetary policy may therefore have an important role to play in reducing unemployment for these groups. Ms Ekholm's interpretation was that some of the recently-implemented labour-market reforms have enabled groups with a weak position

[7] See the article "Low unemployment – a challenge", Monetary Policy Report July 2011.

on the labour market to enter the labour force to a greater extent. In order for them to stay in the labour force it is important that they find employment, which is not easy when there is a downturn due to weaker development abroad. Unemployment will decrease if they exit the labour force. This could make monetary policy appear to be successful, despite the fact that such a development would be very negative for the Swedish economy. It is important that monetary policy makes its contribution to helping these groups to find employment and stay in the labour force. However, it is of course important to clarify what expectations one may reasonably have of monetary policy in this area. Ms Ekholm said that one should avoid creating expectations about something that monetary policy cannot achieve.

Governor **Stefan Ingves** commented on Mr Svensson's remark that household wealth is relatively high by noting that the households make interest and amortisation payments from their regular income or cash flow. It is the cash flow that mainly affects aggregated demand rather than how wealthy people are on paper. A higher level of indebtedness that results in higher interest and amortisation expenditure thus has a negative effect on general demand.

Deputy Governor **Lars E.O. Svensson** responded to Mr Ingves' remarks on the households' interest payments by pointing out that these interest payments are of course important when assessing whether household indebtedness is at a sustainable level. This is the same type of calculation that is used when determining whether sovereign debt is at a sustainable level, that is the usual debt equation. In the case of the households it is first a question of specifying a sustainable mortgage rate after tax. A high estimate may be 5 per cent. A long-term level of the repo rate of 4 per cent plus a high spread of 3 percentage points gives a mortgage rate before tax of 7 per cent, and after tax of approximately 5 per cent.[8] From this we should deduct an estimate of the sustainable growth in disposable income, say 4 per cent – the total of 2 per cent real growth and 2 per cent inflation. This leaves us with 1 per cent. In order to keep the debt ratio at a constant level of 170 per cent of disposable income, the households should thus together pay as debt service 1 per cent of 170 per cent of disposable income, that is 1.7 per cent of disposable income. Households that own their homes do not have to pay rent, which can amount to 20 per cent of disposable income, but do pay fees to tenant-owner associations or municipal fees for water supply and refuse collection and so on, but this expenditure amounts to well below 20 per cent of disposable income. According to Mr Svensson, this supports the claim that 170 per cent of disposable income may be a long-term sustainable level.

[8] A tax level of 30 per cent on capital income gives a mortgage rate after tax of (1-0.3)*7=4.9 per cent.

Apart from assessing whether household indebtedness is sustainable in the long term, it is also important to assess whether the households have sufficient resilience to disturbances. Mr Svensson considered that Finansinspektionen's mortgage report of March 2012 is the best source of knowledge on this.[9] This report shows that new mortgage borrowers, who are the most vulnerable, can pass very demanding stress tests and are thus highly-resilient to disturbances. We have also had stress tests in real time. The financial crisis of 2008-2009 hit Swedish households in the form of a large fall in exports and GDP and a rapid increase in unemployment. The euro crisis has now entailed a new stress test. The Swedish mortgage borrowers have also passed this stress with flying colours, said Mr Svensson.

§3. Monetary policy discussion

Deputy Governor **Lars E.O. Svensson** advocated a significantly lower repo-rate path than the one in the main scenario of the draft Monetary Policy Report. As at the previous meeting, he considered that the forecasts for foreign policy rates and growth abroad were too high and that a lower repo-rate path in Sweden would lead to a higher rate of CPIF inflation closer to the target and a lower level of unemployment closer to a long-run sustainable rate and thus provide a better-balanced monetary policy.

Mr Svensson's interprets the Sveriges Riksbank Act and its preliminary works such that monetary policy has a mandate to maintain price stability and attain the highest sustainable rate of employment, where the latter is in practice the same thing as the lowest sustainable rate of unemployment.

Even if one were to accept the assumptions in the draft Monetary Policy Report with regard to growth abroad and higher future policy rates abroad, a lower repo-rate path than that in the main scenario provides better target attainment for CPIF inflation and unemployment. This is illustrated clearly in Figure 2, which shows the main scenario and forecasts for alternative repo-rate paths, the latter with the aid of the Riksbank's model, Ramses. This conclusion also applies if one assumes that inflation and unemployment react more slowly to interest rate changes than is the case in the Ramses model. If the reaction is slower, this is an argument in favour of a larger and earlier cut in the repo rate. This conclusion applies regardless of whether one measures the unemployment gap against 6.25 or 5.5 per cent long-run sustainable rate of unemployment.

Foreign forward rates, which are represented by the grey line in Figure 3, are according to Mr Svensson a more realistic forecast of foreign policy rates in the current situation. This

[9] "Den svenska bolånemarknaden" (The Swedish mortgage market), report from Finansinspektionen, 13 March 2012.

provides arguments for a much lower repo-rate path. This is shown in Figure 4. Under the assumption of policy rates abroad following forward rates, the figure shows the forecasts for CPIF inflation and unemployment with the main scenario's repo-rate path and with two lower repo-rate paths. Lower policy rates abroad in line with forward rates give, all else being equal, a greater interest rate differential between the repo-rate path and policy rates abroad, a stronger krona, lower inflation, lower exports and higher unemployment, as shown in Figure 4.

The lower repo-rate paths in Figure 4 lead to much better target attainment. One may ask which of the lower repo-rate paths would lead to the best target attainment, the one that goes down to 0.75 per cent or the one that goes down to 0.50 per cent. Calculations of corresponding forecasts for CPIF inflation and unemployment are of course uncertain. It is possible that the inflation forecasts are overestimated and are too high. It may also be the case that the unemployment forecasts are too optimistic and are too low – that it will be more difficult to reduce unemployment. If so, this supports the lower repo-rate path. It also entails having a good margin for downside risks that have not been adequately covered in the assessment in the report. The lower path is still above expected short-term rates in the euro area and the United States.

As the repo rate is now not much above zero and there are significant downside risks in the development of the economy, there is a positive likelihood that the situation will deteriorate so much that the repo rate may need to be cut to such an extent in the period ahead that the zero lower bound will apply, that is that one would wish to lower the repo rate below zero if this was possible. In such a situation one may ask if one should wait to cut the interest rate and hold one's fire so that cuts can be made later if needed, or if one should cut the interest rate straight away. The answer provided by a number of theoretical and empirical research papers on this question is unequivocal: it is better to cut the interest rate more and earlier than to wait. This gives the cut more time to have an impact and reduces the risk that the zero lower bound will bind in the future. This leads on average to a better development of the economy. If the situation subsequently improves then the interest rate can be raised again. This argument supports the lower repo-rate path in Figure 4.

Given this, Mr Svensson advocated that the repo rate should be cut by 0.5 percentage points to 0.75 per cent at the meeting and then follow a repo rate path of 0.5 per cent from the beginning of the first quarter 2013 to the end of the first quarter 2014, followed by an increase to 1.5 per cent at the end of the forecast period.

Deputy Governor Barbro Wickman-Parak began by noting that inflation is below the target and that unemployment is high, and that according to several analysts the repo rate should therefore be lowered. It is easy to verify the first two statements. On the other hand, the monetary policy response to these conditions is, according to Ms Wickman-Parak, neither simple nor self-evident.

It is natural that the monetary-policy debate intensifies ahead of the monetary policy meetings. Proposals that the repo rate should be changed usually have the most impact, and this is the case this time too, as a repo-rate cut has many advocates. Ms Wickman-Parak said that she respects and understands those who come to such a conclusion. But an aspect that tends to be overlooked is that the repo rate is already very low and that already in September the Riksbank predicted that it would remain low for quite some time and that the real interest rate would remain negative until well into 2014.

During the weeks that have passed since the previous monetary-policy meeting, nothing dramatic has happened with regard to the prospects for the Swedish economy. The slowdown we are now witnessing was predicted already at the previous meeting. This was one of the reasons why the repo rate was cut despite the high figure for growth in the second quarter in the statistics then available.

With regard to inflation it is important to analyse where we are coming from and where we are going. Inflation is low primarily because the rate of increase in labour costs has been weak in recent years and because of the earlier strengthening of the krona. Now the former is increasing at the same time as it is expected that the krona will remain rather stable. The figure for inflation has been adjusted downwards somewhat for the next 12 months but this is mostly due to temporarily lower energy prices The important thing is the forecast that inflation will be in line with the inflation target in early 2014. It is difficult to do anything about the fact that inflation will be low in the near future given that monetary policy acts with a time lag. With a somewhat lower repo rate the return in the form of higher inflation would be marginal; 0.1 percentage points this year and next year, as shown by the illustrative calculation in Chapter 2 of the draft Monetary Policy Report. A larger repo-rate cut would thus be needed to do anything about the low level of inflation in the near future, but this would risk overshooting the target further ahead.

So far, employment has been somewhat stronger than expected, but the indications are that employment is now weakening, which the Riksbank also predicted at the previous monetary policy meeting. The increase is now expected to be somewhat smaller and the recovery to be more sluggish. This is mainly due to the assessment that it will take longer for job-seekers to find work. An instructive article in the Report provides several indications that matching efficiency has deteriorated since the crisis. The repo rate cannot do anything about this type of problem.

However, there are reasons to adjust the repo-rate path downwards somewhat. The main reason for lowering the repo-rate path is the situation on the labour market. Although the upward adjustment of unemployment is primarily due to structural factors, there are also cyclical factors. By postponing increases in the repo rate and allowing it to remain lower throughout the forecast period, we can help to mitigate these effects. The fact that interest rates abroad are now expected to be somewhat lower and that an unchanged

Swedish repo-rate path could then affect the krona and inflation has also been a factor in this decision. Given the great uncertainty about global economic activity, a repo-rate cut is more probable than a repo-rate increase this winter, as shown by the repo-rate path.

The assessment is that the repo-rate path is such that the household debt ratio will stop increasing and remain more or less unchanged in the years ahead. We have every reason to monitor this going forward, not because there is any immediate risk to financial stability but because it can create problems for production and employment beyond the forecast horizon. The fact that resolving debt problems costs a lot in terms of production and employment has been clearly illustrated in many different countries and on many occasions throughout history.

Deputy Governor **Per Jansson** said that as in September there have been two conceivable policy alternatives for him. Both of these alternatives meant that he now advocated a more expansionary monetary policy than he did in September. The basic reasons for this are described in detail in the draft Monetary Policy Report.

The first alternative entailed leaving the repo rate unchanged now but then gradually lowering the repo-rate path, and this meant that there was also a slightly greater likelihood of a repo-rate cut already in December. The second alternative was to immediately cut the repo rate by 0.25 percentage points and to immediately apply a lower repo-rate path than in September.

After careful consideration, Mr Jansson had decided to advocate the first alternative, that is to gradually lower the repo-rate path but to refrain from an immediate repo-rate cut. In his opinion, there were several reasons for preferring this alternative.

The first reason to be content with only lowering the repo-rate path was that, as everyone knows, monetary policy acts with a time lag. The analysis of monetary policy alternatives at the end of Chapter 2 in the draft Monetary Policy Report suggests that an immediate repo-rate cut would have little impact on the low level of inflation, and the economy as a whole, in the year ahead. On the other hand, there is a risk that CPIF inflation would rise above the target in a few years' time.

Chapter 2 in the draft Monetary Policy Report also discusses the possibility that the time lag of monetary policy is particularly long at present. That this may be the case is due to the fact that a more expansionary monetary policy in Sweden does not change the situation abroad. The risky situation abroad may mean that Swedish households and companies are currently more cautious than usual when making decisions on consumption and investment. According to this reasoning, it will perhaps take several years, when the situation abroad has improved, for the more expansionary monetary policy to have a more distinct impact. As the scenarios for the monetary policy alternatives do not take such an extra time lag into account, it is even possible that the already limited short-term effect on CPIF inflation is exaggerated in the scenario with a lower repo rate and that the more long-term effect is underestimated. There is therefore a risk that CPIF inflation would overshoot the target in the long term even more than in the case where such an extra time lag does not exist.

Another reason to refrain from an immediate repo-rate cut relates to the risks associated with household indebtedness. Although it is possible that monetary policy's impact on household indebtedness is also slower than normal at the moment, a lowering of the repo rate would, all else being equal, still increase the risks in this area. This would particularly be the case if against the background of a delayed impact of monetary policy one chose to make a bigger adjustment in monetary policy than normal. It is worth emphasising here that even if the impact is delayed not much is gained if it nevertheless does eventually occur.

The assessment is that with the lowering of the repo-rate path CPIF inflation will be close to 2 per cent in about one and a half years' time. Mr Jansson said that inflation being below the inflation target for a certain period of time is a "cost" that can be accepted if it means that the risk of a really bad development of household debt can be reduced a little. He shared the view of many others that the risks associated with the housing market and household debt have not increased recently. And it is an important point to emphasise in this context that the development of these risks is conditional on the monetary policy conducted by the Riksbank. However, the fact that the risks have not increased does not mean that the situation is without problems. Household debt remains at a very high level in both historical and international terms. At the previous monetary policy meeting in September, Mr Jansson said that the Swedish authorities' preparedness to take measures in this field can be improved. There is no reason to change this assessment today. If anything, the recent discussion on raising the loan-to-value restriction, that is allowing the households to increase their mortgages as a percentage of the market value of their homes from the current level, means that things are moving in the wrong direction.

Mr Jansson emphasised that taking household debt into account to some extent did not mean that he was demanding that monetary policy should now be contractionary. On the contrary, according to all conceivable measures monetary policy is currently highly expansionary and with the lower repo-rate path the real repo rate is expected to fall further below today's very low level. As Figure 1:31 in the Monetary Policy Report shows, the real repo rate will be negative until the latter part of 2014. The fact that monetary policy has this highly expansionary stance often seems to be forgotten in the public debate and sometimes in our own discussions too, for example the one we just had on the labour market. Mr Jansson said that it was very difficult to see how one can conclude that monetary policy is a major problem for economic development in Sweden when it is as expansionary as it actually is.

Given this, he said that he supported the proposal in the draft Monetary Policy Report to leave the repo rate unchanged at 1.25 per cent but to also adjust the repo-rate path downwards for the rest of the forecast period. At the end of 2015 the repo rate will be 2.6 per cent, which is almost 0.5 percentage points lower than forecast in the September Monetary Policy Update. He also supported the forecasts for the Swedish economy presented in the draft Report.

Mr Jansson pointed out that this adjustment of the repo-rate path is in fact not so small given the new information that has become available since September. The draft Monetary Policy Report explains that the repo-rate path has been affected by factors such as a somewhat more sluggish adjustment on the Swedish labour market and lower international policy rates towards the latter part of the forecast period. Letting these factors affect the repo-rate path is not a self-evident move that directly follows from new data releases. It is instead a question of new assessments of the Swedish labour market and international policy rates and how these will ultimately affect the repo rate in Sweden. The draft Monetary Policy Report concludes that the recovery on the Swedish labour market is more sluggish because matching between job-seekers and vacancies has deteriorated. It is not obvious that monetary policy should be more expansionary under such circumstances. He nevertheless advocated a more expansionary monetary policy because it is difficult to know what the sustainable rates for unemployment and employment are, and because it is important that monetary policy contributes to the recovery on the labour market. Nor is it self-evident that adjustments of international interest-rate assumptions far in the future should be allowed to affect the repo-rate path in Sweden. This is based on conceived effects via the krona exchange rate but, as is well known, these are highly uncertain.

Finally, Mr Jansson commented on Mr Svensson's argument that a substantial increase in the repo rate is required to have any significant impact on housing prices and household debt. Mr Jansson was not certain that this must be the case. First, there is a substantial variation in the elasticities presented in the empirical literature in this field. The literature shows, not least, that the effects of monetary policy on housing prices vary over time. A common result, for example, is that the effects are greater the more financially deregulated an economy is.[10]

It is fully conceivable that the effects of monetary policy in this area depend on how actively one communicates on the issues. By clearly signalling that one perceives a

[10] See for example Iacoviello, Matteo and Raoul Minetti (2003), "Financial Liberalization and the Sensitivity of House Prices to Monetary Policy: Theory and Evidence", The Manchester School, vol.71, pp. 20-34.

particular situation or development to be a problem, it is perhaps possible to affect behaviour without needing to take any concrete measures at all. In other words, housing prices and household debt can perhaps be influenced without needing to significantly raise the repo rate. But this requires active communication and such communication is of course only possible if one believes that there is actually something to worry about.

This view is close to that held by Michael Woodford – a view that he discussed in a paper in Sveriges Riksbank Economic Review earlier this year.[11] In this paper he says that it is much easier to understand that interest-rate policy has a role to play in this context if we abandon the view that it is a question of controlling "bubbles" and instead see it as counteracting the build-up of various risks. Woodford explicitly says that he believes the possibilities of monetary policy to play a role in this context are often incorrectly dismissed and that even rather small changes in short-term interest rates can have significant effects.

However, Mr Jansson agreed that other measures may be more effective than the repo rate in counteracting a dangerous development of household indebtedness. But the repo rate will nevertheless always be of some importance, irrespective of the other measures taken.

Deputy Governor **Karolina Ekholm** made a different assessment to Mr Jansson as to what would be an appropriate monetary policy in this situation. She said that revising the repo-rate path downwards significantly towards the end of the forecast period was well-motivated considering that most of the indications are for low foreign policy rates for a long period to come and that the development of the Swedish labour market can be expected to be worse than the Riksbank previously expected.

However, there are good reasons for also lowering the repo-rate in the near future. Inflation is far below target and unemployment is high. A lower repo rate could thus be used to try to improve the situation on the labour market without this leading to any risk of excessive inflation.

Ms Ekholm then commented on the reasons Mr Jansson gave for not immediately lowering the repo rate. One reason was that most of the effect of a repo-rate cut on inflation is expected to come at the end of the forecast period, when CPIF inflation will be slightly above 2 per cent. So it will not be possible to do much about the low inflation we see ahead of us through to the start of 2014.

Ms Ekholm was somewhat sceptical of the assessment that the effect of a repo-rate cut would be so delayed. Much probably depends on how the exchange rate is affected and on how much of an impact exchange rate fluctuations have on inflation – and this impact

[11] Woodford, Michael (2012), "Inflation Targeting and Financial Stability", *Economic Review* 2012:1.

can occur relatively rapidly, said Ms Ekholm. But if the effect of repo rate changes is delayed, this would suggest that the repo rate should already have been lower today. Because then, a long period with inflation below target could have been avoided. But in earlier reports, when the consequences of a lower repo rate were discussed, they were rejected with exactly the same argument. Ms Ekholm said that, in conjunction with the assessment of the monetary policy conducted over the year, an investigation should be carried out into when the repo rate should have been lowered to best stabilise inflation around the target of 2 per cent.

Another argument against lowering the repo rate was that a less expansionary monetary policy would dampen household indebtedness and correspondingly the risk of excessive future fluctuations in resource utilisation and inflation. It is clear that there are different opinions on to what extent monetary policy should consider household indebtedness. Ms Ekholm noted that the growth of household credit has shown an almost trend decrease since 2006, from 12–13 per cent in 2006 to below 5 per cent at present, as can be seen in Figure 3:8 in the draft Monetary Policy Report. Household debt as a percentage of disposable income has levelled off recently, as Mr Svensson demonstrated in Figure 1. Housing prices have also been relatively stable recently. As can be seen in Figure 3:9 in the draft Monetary Policy Report, it is difficult to see any unambiguous trend in house prices over the last two years. As Mr Jansson pointed out, this slowdown of credit growth and the stabilisation of housing prices are conditioned on the monetary policy that has been conducted. But other important factors are Finansinspektionen's recommendation of a loan-to-value ceiling and the fact that risks associated with high indebtedness have been keenly discussed in the media and at the political level recently.

In the current situation, there is no compelling reason to use the repo rate – which influences so much more than just household credit and housing prices – to further dampen the development of the housing market. This does not mean that the repo rate can never, under any circumstances, be used in this manner. It is just that there is no clear need to do so just now. In any event, the somewhat unclear gains that might be made by holding to a higher repo rate than is justified by inflation and resource utilisation must be weighed against the costs, in terms of possibly a less credible inflation target and unemployment becoming entrenched at a high level. Ms Ekholm said that, for her, these unclear gains had a fairly low weight.

One important factor when weighing up these gains and costs is the effect of the repo rate on housing prices and credit growth against the effect on inflation and unemployment. Mr Svensson has referred to studies that conclude that the effect on housing prices is minor, while the effect on unemployment is major. Mr Jansson has stated that these results are sensitive and differ somewhat between different studies. It is important to determine how the repo rate affects these different aggregates to get an idea of how the weighting between any reduced risks linked to high indebtedness and worsened resource utilisation looks.

Ms Ekholm advocated a lowering of the repo rate by 25 points at today's meeting. She also wanted to place greater probability on a further decrease, as opposed to an increase. Ms Ekholm preferred a path lying closer to about 0.50 percentage points below the main scenario's path, and which rises slightly more slowly than that path. A better balanced repo-rate path would bottom out at 0.75 per cent and reach about 1.75 per cent at the end of the forecast horizon. As previously, it is difficult to maintain that this path gives the best possible balance between stabilising inflation around the inflation target and unemployment around a long-term sustainable level. In model simulations, it quite clearly gives better target fulfilment than the main scenario's repo-rate path. As it is difficult to assess what would be an appropriate forecast of foreign policy rates, Ms Ekholm had examined simulations in which both the main scenario's forecast and implied forward rates had been used as a starting point. Using the main scenario's forecast for policy rates abroad, Ms Ekholm's repo-rate path led to a forecast for inflation in which it exceeds the target of 2 per cent by a greater degree than she actually considers to be in line with a well-balanced monetary policy. But, as she considered that the main scenario's forecast of policy rates abroad was a little too high towards the end of the forecast period, she deemed that this repo-rate path is still preferable.

First Deputy Governor **Kerstin af Jochnick** supported the proposal in the Monetary Policy Report to hold the repo rate unchanged at 1.25 per cent and to adjust the repo-rate path downwards over the entire forecast period.

A short time has passed since our last monetary policy meeting. The economic information received since then on both Sweden and the international situation has largely been in line with the assessment made in September. Revisions have been made in a few areas.

In comparison with the information held by the Riksbank in September, international GDP growth has been revised downwards slightly. The assessment is that the recovery, both internationally and in Sweden, will be more prolonged. Inflation outcomes have also been lower than in the forecast. All in all, the inflation forecast is slightly lower than in the previous assessment. This is one of the reasons why the repo-rate path should be adjusted downwards. With a lower repo-rate path, the Riksbank will contribute to inflation eventually rising and reaching 2 per cent measured in terms of the CPIF at the start of 2014. Resource utilisation is rising and will become normal during the forecast period.

The repo rate should be held at a level that allows us to reach the inflation target and stabilise employment over a long-term perspective. Whether the low interest rates are creating a risk of financial imbalances must also be weighed into this assessment. There are many examples of how imbalances risk arising when interest rates are low for a long time.

The increase in lending to households is now down to reasonable levels. Ms af Jochnick's assessment was that the mortgage cap has contributed to this. However, household indebtedness continues to be high and it is thus important that the low level of interest rates does not create any incentive for a more rapid rate of increase in indebtedness. When households have large debts, they become vulnerable to economic downturns, interest rate increases and falls in housing prices.

As the Riksbank does not have any other means than the repo rate at its disposal, it is natural to discuss the trade-offs that need to be made. Monetary policy is not the best means for limiting household indebtedness – other measures are primarily needed here instead. But, as few other tools are used to reduce the risks of high indebtedness, monetary policy has a greater responsibility to prevent the unbalanced development of asset prices and indebtedness. An overall question that has to be put is thus how a healthy development of household indebtedness can be attained. This is a broad question and must include considerations of what healthy credit granting is, what healthy risk-taking is, and how the taxation system should be designed in terms of interest deductions. The Riksbank has also discussed the issue of risk weights for mortgages with Finansinspektionen. According to Ms af Jochnick, this is a matter of ensuring that household indebtedness develops in a healthy manner as a preventive measure. The Riksbank's analysis needs to be developed in this area. For monetary policy to function well, a better understanding of how the low interest rates affect indebtedness and asset prices over time is needed.

Governor **Stefan Ingves** noted that he supported the proposal to leave the repo rate unchanged and to adjust the repo-rate path downwards slightly.

A short time has passed since the last monetary policy meeting and nothing dramatic has happened in terms of the international outlook. Economic development abroad is slightly weaker. Swedish inflationary pressures are slightly lower at present. There is thus reason to adjust the repo-rate path downwards slightly. A low repo-rate will help to increase the presently low rate of inflation to around 2 per cent, measured in terms of the CPIF, in 2014 and 2015. Resource utilisation will increase and reach a normal level during the latter part of the forecast period. All in all, the downward adjustment of the repo-rate path means that the likelihood of a repo-rate cut in the winter is greater than the likelihood of an increase. This is a fairly traditional view of monetary policy when the repo rate is low but the Swedish economy is simultaneously gradually moving towards a normalisation of economic activity.

The forecasts for policy-rate paths abroad have been revised downwards. There are reasons for this. An unchanged Swedish repo-rate path would then entail an increase in interest-rate differentials in relation to other countries. However, we should not attach to much importance to this as the effect in Sweden comes through the exchange rate, and we know from experience that exchange-rate forecasts are very hard to make. Forecasts based on assumptions of interest-rate differentials far in the future are, of course, even more uncertain.

It is also important to note that the policy rate and the implied forward rate for government securities cannot be used mechanically in the analysis of the monetary policy transmission mechanism. In several countries, the interest rates faced by companies and households are significantly higher than the policy rate. The monetary-policy transmission mechanism in the euro area does not work normally when its impact varies from country to country. Monetary policy appears to be more expansionary than it actually is when the financial sector does not function normally. When the central bank's policy rates are low, it is important to also analyse how the volume of various credit aggregates, the money supply and the rate of circulation are developing. Focusing solely on interest rates and interest-rate paths is not enough. Quantities and the state of various balance sheets must not be forgotten.

Sweden's current account has shown a surplus every year since 1994. Total financial saving in Sweden is high. The forecast expects a continued strong surplus in the current account. Given the international unease and the debt consolidation underway in many countries, this is a sign of strength. However, monetary policy's role here is limited. For the Riksbank, this is a matter of meeting the inflation target. Strong Swedish competitiveness and a continued current account surplus presuppose a reasonable development of wages and productivity. Should international demand collapse in a really bad scenario, it would be difficult for monetary policy to fully compensate for this fall in demand. Monetary policy is already expansionary, as illustrated by the fact that the real repo rate is negative over the larger part of the forecast period.

Deputy Governor **Lars E.O. Svensson** commented on Mr Jansson's earlier statement that monetary policy in Sweden is very expansionary according to "every conceivable measure". However, it is not completely obvious which is the most relevant measure of how expansionary monetary policy is. Compared with historical levels, the nominal repo rate is of course low – and the real repo rate is also quite low. But is this the relevant comparison?

A comparison which is at least as relevant is with international nominal and real policy rates. In Figure 3, we can compare the repo rate, represented by the red line, with the KIX-weighted international policy rates. Even if we accept the Riksbank's forecast for international policy rates, which is the yellow line, instead of that for foreign forward rates, which is the grey line, the interest rate differential is large, 1.5 percentage points over several years. Figure 5 compares Swedish real policy rates with real short-term rates in the euro area and the United States. In 2010 and 2011, Swedish real interest rates were up to 3 percentage points higher. Later, the interest rate differential reaches 1.5 percentage points. Measured in this way, Swedish monetary policy is not at all particularly expansionary – on the contrary, it is fairly contractionary compared with the rest of the world.

A relevant comparison can also be made with the neutral interest rate, which can be defined as the real interest rate over a certain timespan, for example 1–2 years, which would reduce unemployment to its long-run sustainable level. In such a comparison, Swedish monetary policy is, of course, very contractionary.

Mr Svensson commented on Mr Jansson's statement that inflation should not overshoot the inflation target. Mr Svensson considered that this is a highly dubious criterion. It means that over the forecast period, average inflation will be below target, and the criterion will contribute to the problem we have seen since 1997, namely that average inflation has ended up significantly below target. As inflation expectations according to Prospera are well-anchored at the target, this means, as Mr Svensson has earlier emphasised and written a paper on, that average unemployment will be higher than if average inflation had been on target.[12]

Mr Svensson also commented on Mr Jansson's opinion that household indebtedness is at a very high level and that this is a problem. Households' debts amount to 170 per cent of disposable income. But, as the relation between the households' debts and their total assets, excluding collective pension savings, is fairly stable in Sweden, at about 1:3, this of course means that the households' total assets are also at a very high level. Is this also a problem?

In an earlier contribution, Mr Jansson questioned the minor quantitative effects of monetary policy on housing prices that Mr Svensson had referred to, that every 1 per cent of decreased housing prices costs 15 000 unemployed, and pointed out that this could vary with circumstances. However, there are large margins in these estimates. If the cost was one-third, which is to say 5 000 unemployed for every percentage of housing prices, it would still be substantial. Mr Svensson noted that his figures are primarily based on the Riksbank's own investigation into risks on the housing market, which considers specific Swedish conditions.[13] However, they are in line with the results of studies of other countries.

[12] Svensson, Lars E.O. (2012), "The Possible Unemployment Cost of Average Inflation below a Credible Target", www.larseosvensson.net

[13] Claussen, Carl Andreas, Magnus Jonsson and Björn Lagerwall (2011), "A macroeconomic analysis of housing prices in Sweden", *The Riksbank's commission of inquiry into risks on the Swedish housing market*, April 2011, p. 67–95.

Finally, Mr Svensson also commented on Mr Jansson's remarks in which he mentioned Michael Woodford's paper in Sveriges Riksbank Economic Review, in which leverage, defined here as assets relative to equity, is assumed to be procyclical, to vary with the GDP gap and to increase the risk of a financial crisis.[14] In this case, a contractionary monetary policy can temporarily limit leverage and reduce the risk of a crisis. But this also requires an assumption that there is no other instrument, such as a capital requirement or a mortgage cap, that can limit leverage. In his comments on the article in the Economic Review, Mr Svensson demonstrates that as soon as such an instrument exists – and capital requirements and mortgage caps already exist– monetary policy will no longer need to take account of leverage.[15]

In addition, Mr Svensson had not seen that there was any empirical support in Sweden for the assumption that leverage and the leverage ratio for commercial banks in Sweden is particularly cyclical or that it could be influenced by monetary policy. According to available data, unemployment and the repo rate seem to be largely uncorrelated with the banks' leverage.

Deputy Governor **Karolina Ekholm** commented on two matters that Mr Ingves had previously taken up. The first of these was that too far-reaching conclusions should not be drawn from the implications for Sweden of a downward revision of the long-term forecast for policy rates abroad. Ms Ekholm agreed that a great deal depends on how the exchange rate is affected and that exchange rates are very hard to forecast. However, in the Riksbank's models, the development of the Swedish economy is very sensitive to assumptions of the development of policy rates abroad, even far in the future, and how these rates may affect the exchange rate. This sensitivity is due to the fact that the Swedish economy is a small, open economy in which the exchange rate is of great significance to both inflation and resource utilisation. From this point of view, it is important to make these forecasts as good as possible, even if they are uncertain.

Ms Ekholm also commented on Mr Ingves' reasoning on the Swedish current account surplus, saying that no value judgement should be attached to the fact that Sweden has a large surplus and has had so for some time. The surplus is a reflection of aggregate saving exceeding aggregate investment. Saving is high in Sweden. As Mr Svensson pointed out, saving is high among households. It is also high in the public sector, compared with other countries. The level of investment is perhaps neither exceptionally low or exceptionally high, but higher investment would not necessarily be a negative development. Quite simply, the current account surplus is a reflection of the relatively subdued domestic absorbtion of goods and services, a situation we have had for many

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[14] Woodford, Michael (2012), "Inflation Targeting and Financial Stability", *Economic Review* 2012:1.

[15] Svensson, Lars E.O. (2012), "Comment on Michael Woodford, 'Inflation Targeting and Financial Stability'", *Economic Review* 2012:1.

years. Countries with a large current account deficit certainly have reason to think that Sweden could by all means implement a policy to increase domestic absorbtion so that we import more goods and services from them. Ms Ekholm said that it is enough to note that Sweden has a large current account surplus without making a value judgement about it.

Deputy Governor **Per Jansson** commented on a couple of points that Ms Ekholm and Mr Svensson had raised. Ms Ekholm mentioned "unclear gains" with regard to taking household debt into account. Mr Jansson agreed that these are very difficult questions and was certain that the Riksbank is not the only central bank grappling with them. However, Mr Jansson found it hard to ignore the fact that so many countries had run into problems with excess indebtedness in one way or another, and that so many had previously been certain that this indebtedness would not be a problem. According to Mr Jansson, this called for a precautionary principle to be applied.

At the same time, it is not the case that the Swedish economy is now paying a "premium" in the form of a repo rate that is several percentage points higher than it would otherwise be. As was mentioned earlier, despite everything, this premium is quite small. But it provides enough scope to express his unease. As was mentioned earlier, communicating on an issue can, in itself, be quite important.

Finally, Mr Jansson commented on Mr Svensson's remark that Swedish households are very wealthy. This is correct if all wealth items are included. But, if you only look at the part of wealth that forms a liquid reserve, in which homes and private and collective insurance schemes are excluded, then the result is not at all as impressive. This must be considered when discussing how robust household balance sheets actually are.

Deputy Governor **Barbro Wickman-Parak** said that, when discussing the repo rate as opposed to other tools for dampening a credit expansion, it is worth remembering that all of the tools mentioned have repercussions for demand and growth. This applies to amortisation requirements, reduced interest deductions and increased risk weights for mortgages. The interest rate is the price of money and will continue to play a part in borrowing.

Ms Wickman-Parak said that overseas forward rates, even those far in the future, have played a prominent role in the Executive Board's discussions. A reasonable approach is not just to mechanically proceed on the basis of forward rates or central bank communication, but to also try to judge their reality against the background of one's view of economic activity. One example of this is that few reservations have been expressed about the forecasts for growth and inflation in the United States in the years ahead presented in the draft Monetary Policy Report. But is this development consistent with a policy rate close to zero for the whole of 2015?

In a reply to Ms Wickman-Parak, Deputy Governor **Lars E.O. Svensson** considered that the growth forecast for the United States in the draft Monetary Policy Report is slightly too optimistic. Regarding the forecast for policy rates abroad, Mr Svensson agreed that this is a matter of assessing which forecast is most realistic. To come close to the international growth and inflation forecasts, Mr Svensson considered that interest rates as low as indicated by the forward rates will be needed.

As regards which forecast is most realistic, it can also be helpful to look back. The Riksbank's forecasts for international policy rates have been high in relation to outcomes. Forward rates have also been high in relation to outcomes, but lower than the Riksbank's forecasts, and forecasting errors have been smaller. The outcome for policy rates has been much lower for longer than the Riksbank expected. Mr Svensson feared that policy rates will need to continue to be low for quite a long time to come.

The Chairman, Governor **Stefan Ingves**, then summarised the monetary policy discussion.

At the meeting today, it was noted that inflationary pressures are lower and that the recovery on the labour market will be more sluggish than assessed in September. The Executive Board agreed that the repo rate therefore needs to be low for some time to come in order to stimulate the economy and bring inflation in line with the target. However, this time too there were differences with regard to how expansionary monetary policy should be.

Four Board members considered it appropriate to keep the repo rate unchanged at 1.25 per cent. Cutting the repo rate now would not have a particularly significant impact on inflation and economic activity in the year ahead but would, on the other hand, risk inflation being above the target in 2014 and 2015. Two members wanted to cut the repo rate, one by 0.25 percentage points and the other by 0.5 percentage points, to bring inflation to the target more rapidly and to reduce unemployment earlier.

All of the members considered it appropriate to adjust the repo-rate path downwards. A majority consisting of four of the members considered that the downward adjustment of the repo-rate path proposed in the draft Monetary Policy Report represented an appropriate balance. They considered that CPIF inflation would thus reach 2 per cent after just over one year and that resource utilisation would normalise. The assessment was that the lower repo-rate path would mean that the households' debt ratio would not increase but remain at the current level. However, two members considered that there was scope for an even lower repo-rate path and believed that such a path would more quickly lead to an inflation rate of 2 per cent and an unemployment rate closer to a long-run sustainable rate.

All of the members considered that the situation in the euro area remains uncertain and that the downturn there will be more prolonged as a result of the underlying structural problems that continue to burden the economies in the region.

The members agreed that the growth of Swedish GDP is now slowing down following strong growth so far this year and that the recovery of the labour market will be more sluggish than expected. The members also agreed that there are unutilised resources in the Swedish economy, although there were different assessments of the level of resource utilisation. There were also different assessments of what monetary policy can achieve at present with regard to reducing unemployment.

All of the members discussed the households' high debt ratio in various ways. However, there were different views on what risks this may pose to the economy. The members expressed a wish for this issue to be taken into account to a greater extent in the analysis in the future.

§4. Monetary policy decision

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 Thursday 25 October 2012 at 9.30,
- to hold the repo rate unchanged at 1.25 per cent and that this decision would apply with effect from Wednesday 31 October,
- to publish the decision above on Thursday 25 October 2012 at 9.30 with the motivation and wording contained in a press release, and
- to publish the minutes of today's meeting on Wednesday 7 November at 9.30.

Deputy Governor Karolina Ekholm entered a reservation against the decision to hold the repo rate unchanged and against the repo-rate path in the Monetary Policy Report. She advocated a lowering of the repo-rate path to 1.0 per cent and a repo-rate path that is further lowered to 0.75 per cent, stays at this level until the end of 2013, and is then successively raised to about 1.75 per cent by the end of the forecast period. This was justified by her assessment that a repo rate that is associated with a higher forecast of CPIF inflation and a lower forecast of unemployment constitutes a better-balanced monetary policy.

Deputy Governor Lars E.O. Svensson entered reservations against the Monetary Policy Report and the decision about the repo rate and repo-rate path in the Monetary Policy Report. He advocated a lowering of the repo rate to 0.75 per cent and then a repo-rate path that stays at 0.5 per cent from the first quarter of 2013 through the first quarter of 2014, and then rises to 1.5 per cent by the end of the forecast period. This was justified by his assessment that the Report's forecasts of foreign policy rates further ahead and foreign growth are too high and that his repo-rate path, considering these circumstances, is associated with a forecast of CPIF inflation that is closer to the inflation target and a forecast of unemployment that is closer to a long-run sustainable rate and therefore constitutes a better-balanced monetary policy.

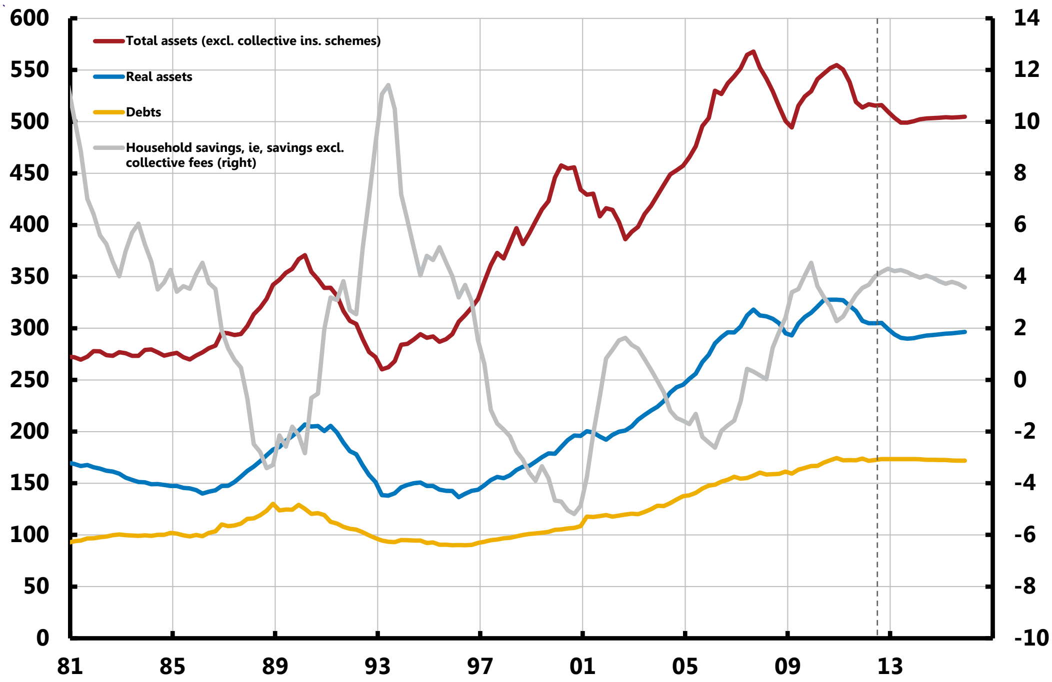
This paragraph was verified immediately.

Minutes by
Ann-Christine Högberg

Verified by:

Karolina Ekholm	Stefan Ingves	Per Jansson
Kerstin af Jochnick	Lars E.O. Svensson	Barbro Wickman-Parak

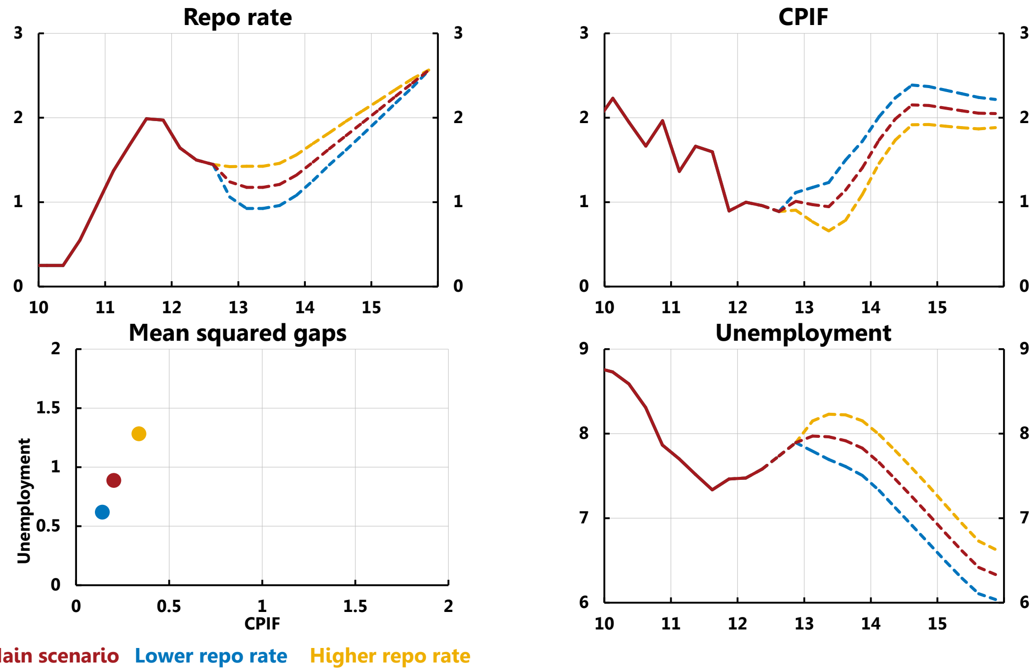
Figure 1. Swedish households' debts, total and real assets and savings



Sources: Statistics Sweden and the Riksbank

Figure 2. Monetary policy alternatives, October 2012

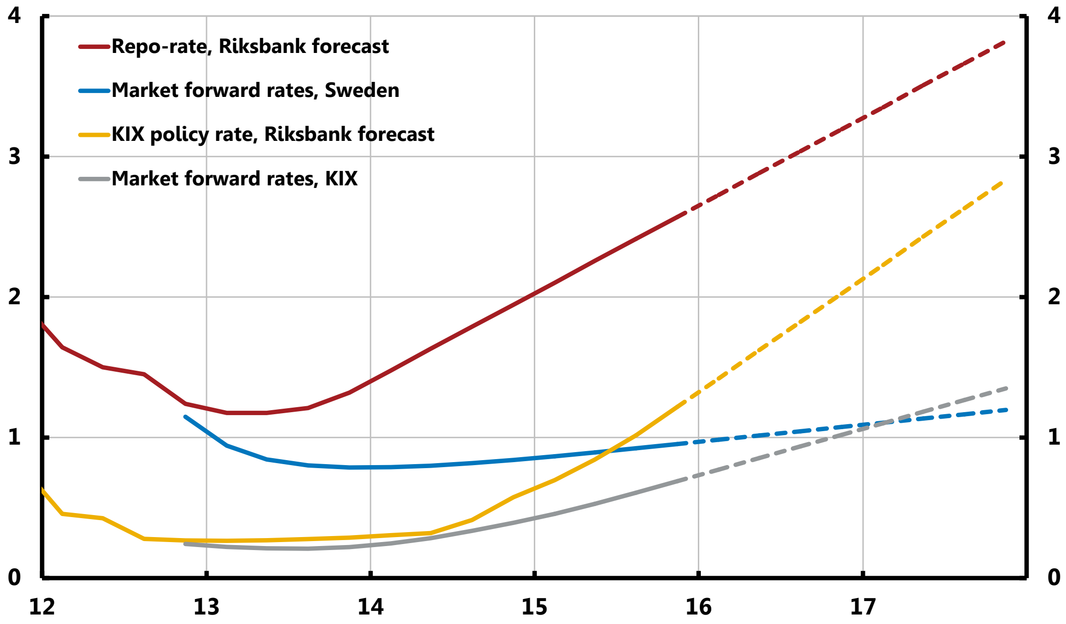
Policy rates abroad according to the main scenario. Long-run sustainable unemployment rate 6.25 per cent. Deviations according to Ramses.



Sources: Statistics Sweden and the Riksbank

Figure 3. Repo-rate path, forward rates and forecast for KIX-weighted policy rate, October 2012

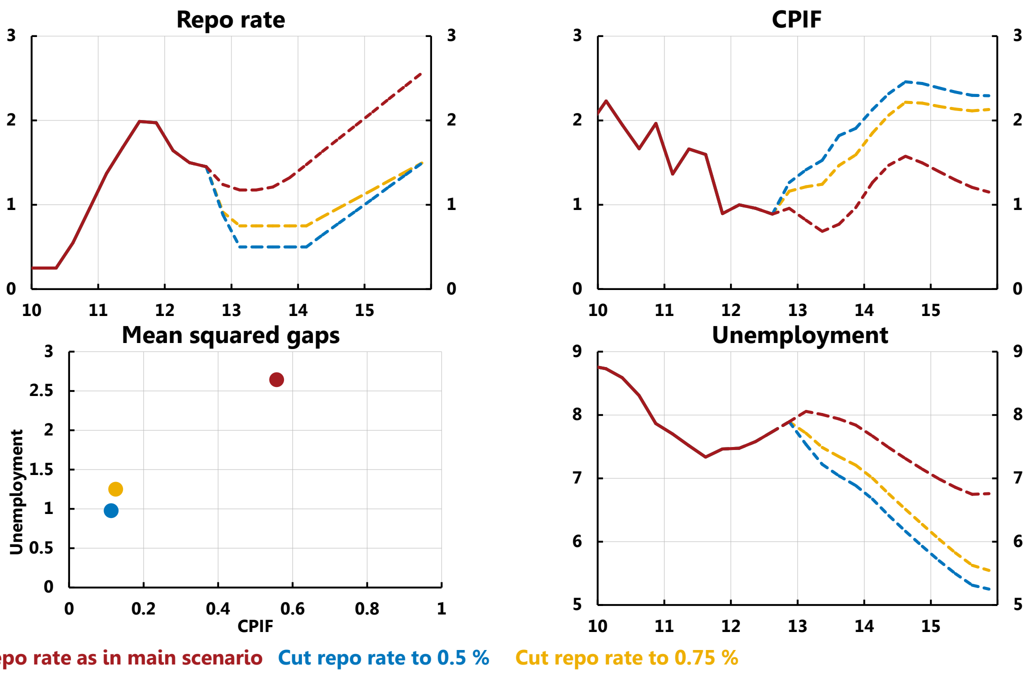
Per cent. Forward rates from 18 October



Sources: National sources, Reuters EcoWin, the Riksbank and own calculations

Figure 4. Monetary policy alternatives, October 2012

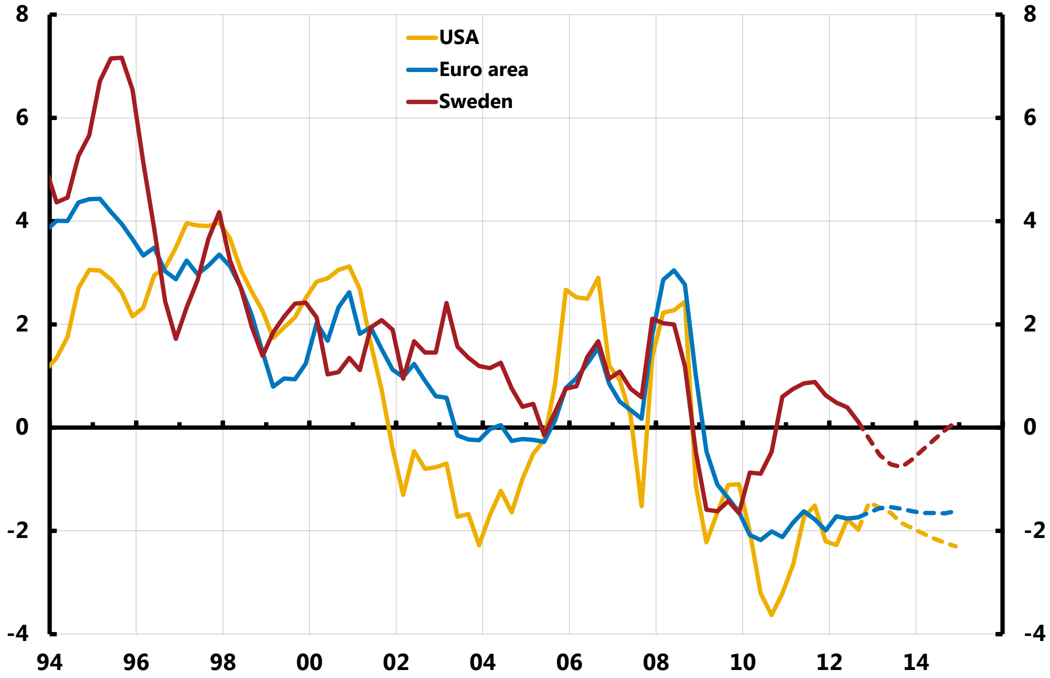
Policy rates abroad according to implied forward rates. Mean squared gap calculated using sustainable unemployment rate of 5.5 per cent.



Sources: Statistics Sweden and the Riksbank

Figure 5. Real policy rate, 1 year

Per cent



Sources: ECB, IMF, OECD, Statistics Sweden and the Riksbank

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