



Annex A to the minutes

DATE: 4 January 2016
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REF. NO. 2016-00041

■ Foreign exchange intervention as a complementary monetary policy measure

Decision by the Executive Board

The Executive Board decides that

- 1 the Riksbank shall intervene on the foreign exchange market as a complementary monetary policy measure if interventions are considered necessary to ensure that developments in the krona exchange rate do not comprise a serious risk to the upturn in inflation,
- 2 the Governor together with the First Deputy Governor shall be given the task of deciding, with the right for each of these to delegate to another, on the details regarding time and amounts for the interventions in accordance with the decision described in the Mandate for foreign exchange interventions, and that
- 3 the Governor and First Deputy Governor, or those to whom they have delegated, shall inform the other members of the Executive Board prior to making decisions in accordance with point 2.

Background

Interventions on the foreign exchange market are a means at the disposal of a central bank that can be used as a complementary monetary policy measure. In a situation where the development of the exchange rate comprises a serious risk that inflation will not approach the target in a satisfactory manner, the central bank may be justified in using interventions on the foreign exchange market as a complementary measure in its work to safeguard price stability.

Deliberations

A high level of confidence in the inflation target is important

During 2015, the Riksbank has cut the repo rate from 0.0 per cent to –0.35 per cent, adjusted the repo-rate path downwards and purchased large amounts of government

■ bonds and also announced additional purchases during the first half of 2016. The aim of this monetary policy is to push up inflation and stabilise it around the target of 2 per cent and help bring inflation expectations in line with the inflation target. Continued high confidence in the inflation target creates the conditions for good economic developments. It is clear that the inflation target has contributed to favourable economic developments in Sweden. Over the past 20 years, inflation has been low and stable and growth in GDP and real wages has been relatively high, which can be compared with the 1970s and 1980s, which were marked by high average inflation and substantial fluctuations in prices and wages. This made economic planning more difficult for all participants and created socioeconomic costs. A level playing field and predictability reduce uncertainty and create stability in the economy.

Monetary policy meeting on 14 December: Continuing expansionary monetary policy and preparedness to act

At the most recent monetary policy meeting on 14 December, the Executive Board noted that growth in the Swedish economy was strong, that inflation had shown a rising trend over the year and that inflation expectations had stabilised and turned upwards. However, the upturn in inflation is volatile, as illustrated by the unexpectedly weak outcome for November. The Executive Board of the Riksbank therefore assessed that monetary policy needed to remain very expansionary for inflation to continue rising and to stabilise around 2 per cent. The repo rate was held at 0.35 per cent and the plan to continue to purchase government bonds during the first half of 2016 remained. The Executive Board also communicated that it is still prepared to make monetary policy even more expansionary, even between the ordinary monetary policy meetings.

The Riksbank's very expansionary monetary policy has contributed to good growth, falling unemployment and a rising trend in inflation. But there is still considerable global uncertainty and the upturn in inflation still depends to a large extent on the weak krona, which has contributed to a rise in the prices of imported goods and services. The Riksbank's forecast entails a slow strengthening of the krona in the coming years. The positive contribution of the exchange rate to inflation will then gradually subside. At the same time, high growth and lower unemployment support an upturn in the more domestically-generated inflation. If the krona were to strengthen faster than was forecast and before domestically-generated inflation picks up, this could stop the rise in inflation and make it more difficult to uphold confidence in the inflation target.

Need for further monetary policy measures

The Riksbank does not have a target for the exchange rate. However, the value of the Swedish krona in relation to the most important currencies is an important factor in assessing inflation. A rapid strengthening of the krona may therefore need to be counteracted by an even more expansionary monetary policy.

Developments on the foreign exchange markets since the monetary policy meeting in December have meant that the krona has strengthened against several currencies. According to the KIX exchange rate index, the krona is now clearly stronger than was forecast in the December Monetary Policy Report. This development is expected to comprise a major risk of bringing the upturn in inflation to a halt and preventing inflation from stabilising around 2 per cent. As described in the April 2015 Monetary Policy Report, a strengthening of the exchange rate that comes too soon and is too

- rapid also risks dampening inflation more than normal when inflation has been low over a longer period of time, for instance, because inflation expectations become lower.

As a complementary monetary policy measure the Riksbank may therefore need to intervene on the foreign exchange market. The Riksbank assesses that foreign exchange interventions can contribute to a development in the exchange rate that is compatible with inflation rising towards 2 per cent.

Foreign exchange interventions do not aim to influence the long-run krona exchange rate, but to counteract an overly rapid strengthening before inflation has stabilised around 2 per cent. The foreign exchange transactions made within the framework of these interventions are a means of upholding the inflation target and continuously safeguarding price stability. Interventions shall therefore only take place as long as they are considered necessary to ensure that developments in the krona exchange rate do not comprise a serious risk to the upturn in inflation.

The Riksbank still has a high level of preparedness to make monetary policy even more expansionary, even between the ordinary monetary policy meetings. In addition to foreign exchange interventions, the repo rate can be cut further and the Riksbank can purchase more securities. In addition, there is scope to launch a lending programme to companies via the banks should this be necessary.