



Monetary Policy Update

September 2012

Economic developments in the euro area have continued to weaken and it will take time to rectify the underlying structural problems. However, the Riksbank assesses that the European debt crisis will be managed in such a way that the unease gradually subsides during 2013. At the same time, the recovery in the US economy is continuing, and the world economy as a whole is growing at a relatively good pace. Economic developments abroad are largely in line with the assessment made in the Monetary Policy Report published in July.

There was unexpectedly strong growth in the Swedish economy in the first half of this year. However, as a result of the weak developments in the euro area in particular, growth in Sweden is expected to slow down over the coming year and the labour market is expected to be weak. As developments abroad strengthen over the course of next year, economic activity in Sweden is expected to improve, which will mean higher growth and an increase in employment. The economic prospects for the Swedish economy are largely in line with the assessment made in July.

As growth in the Swedish economy is expected to be relatively weak in the coming year, the Riksbank's assessment is that the very rapid growth during the first half of the year will not push up inflation. Especially as the high GDP growth has gone hand in hand with an unexpectedly low growth in productivity. This, together with a faster than expected appreciation of the Swedish krona, means that cost pressures and inflation will be lower than was assessed in July.

The Executive Board of the Riksbank has therefore decided to cut the repo rate by 0.25 of a percentage point to 1.25 per cent. The repo rate is then expected to remain at this level until the middle of next year. As economic activity improves, and inflationary pressures increase, the repo rate will be raised gradually. The lower repo-rate path will contribute to CPIF inflation rising to 2 per cent and to a normalisation of resource utilisation during the forecast period.

Figure 1. Repo rate with uncertainty bands
Per cent, quarterly averages

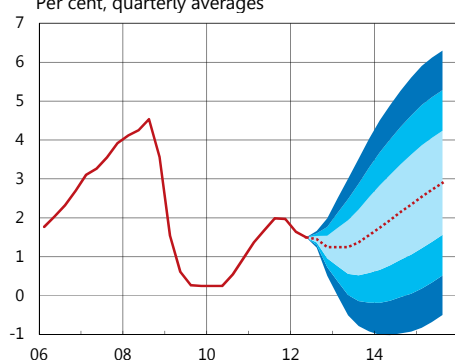


Figure 2. GDP with uncertainty bands
Annual percentage change, seasonally-adjusted data

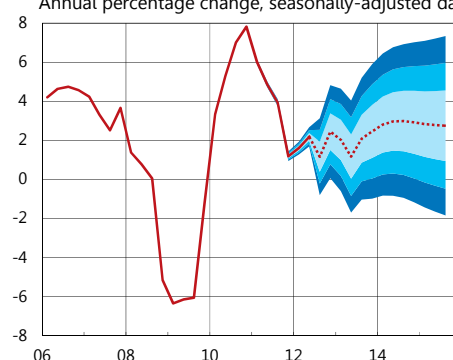


Figure 3. CPI with uncertainty bands
Annual percentage change

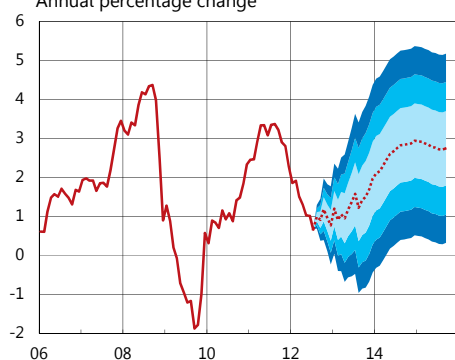
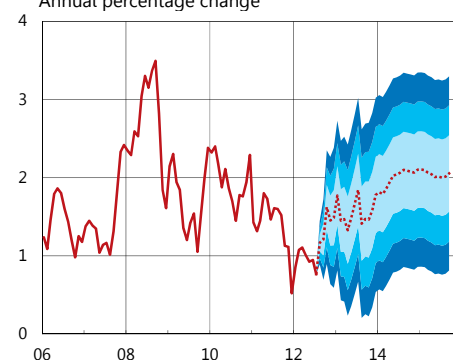


Figure 4. CPIF with uncertainty bands
Annual percentage change



■ 90 % ■ 75 % ■ 50 %

Note. The uncertainty bands in the figures are based on historical forecast errors, see the article "Calculation method for uncertainty bands" in MPR 2007:1. The uncertainty bands do not take into account the fact that there may be a lower bound for the repo rate.
Sources: Statistics Sweden and the Riksbank

The Executive Board decided to adopt the Monetary Policy Update at its meeting on 5 September 2012. The interest rate decision is presented in a press release at 9.30 a.m. on the day following the monetary policy meeting.

■ The economic outlook and inflation prospects

The economic and inflation prospects reported in this Monetary Policy Update are based on the assessments made in the Monetary Policy Report in July and the forecast updates made since then. The forecasts are based on the decision to cut the repo rate by 0.25 percentage points to 1.25 per cent and on a lower repo-rate path than the one outlined in the July assessment.

■ Growth in the world economy despite continuing euro crisis

The world economy as a whole is continuing to grow at a relatively good rate, around 4 per cent on average during the period 2012-2014. The oil price has recently risen and is expected to be higher throughout the forecast period, compared with the earlier forecast. This will dampen growth somewhat in the coming period. Developments in emerging markets also show signs of slowing down somewhat, although their situation is better than that of the more developed economies. However, many of the emerging economies have scope to conduct a more expansionary economic policy if this were to become necessary. The recovery in the US economy is continuing, albeit relatively slowly. Household consumption is increasing, and the housing market is improving. This means that the conditions for domestically-driven growth in the United States will improve further.

Developments in the real economy of the euro area continue to be burdened by the debt crisis and are expected to be weak in the coming period. The situation on the financial markets has improved somewhat. Although government bond yields for the euro area countries with sovereign debt problems remain high, they have fallen somewhat, particularly those with shorter maturities. This was in connection with the signals from the European Central Bank, ECB, that it is prepared to intervene if the problems in the debt-ridden countries worsen. The Riksbank assesses that the European debt crisis will be managed in such a way that the unease gradually subsides in 2013. As confidence in the financial markets and among households and companies gradually improves, growth in the euro area and abroad will increase. An expansionary monetary policy in many parts of the world will also contribute to the recovery.

■ Prolonged downturn in the euro area

Developments in the real economy of the euro area are still marked by the sovereign debt crisis, and the forecast is in line with the assessment in the most recent Monetary Policy Report. The main obstacle to growth in the euro area is developments in southern Europe; GDP is falling in Spain and Italy, for instance. So far, developments in Germany have been more resilient, but indicators for the third quarter point to weaker developments. The overall assessment is that growth in the euro area will be slightly negative in 2012 and slightly positive in 2013. After that, growth will become gradually higher. In relation to the weak state of the economy, inflation in the euro area is expected to be high in 2012. This is partly due to import prices rising when the euro weakens and to increases in administrative prices and VAT rates contributing to higher inflation. However, the underlying cost pressures are expected to be low over the coming years, and monetary policy is thus expected to remain very expansionary during the entire forecast period. There is still considerable uncertainty over developments in the euro area and it will take time to rectify the underlying structural weaknesses, such as high public debt, problems in the banking sector and weak competitiveness. The uncertainty over developments in the euro area is expected to remain until a credible strategy for the long-term management of these

problems is in place. The Riksbank assumes that this will occur gradually and that the uncertainty over developments in the euro area will begin to wane in 2013.

■ Continued growth in the United States

Developments in the US economy have been in line with the forecast made by the Riksbank in July. Growth is low and expected to remain lower than the potential level until the middle of 2013. Fiscal policy is expected to be tightened further in 2013. However, there is considerable uncertainty over what fiscal policy will be conducted, as this will be partly affected by the outcome of the presidential election in November this year. If no new political decisions are taken, there will automatically be severe tightening of public finances in 2013. It is assumed in the forecast that decisions will be taken to avoid this and that fiscal policy will instead be tightened by a smaller amount, 1.5 per cent of GDP, in 2013. The continued recovery in the housing market is expected to increase growth in the coming period as investment in construction accelerates, employment rises and household wealth strengthens. The forecast for GDP growth in the coming years is on the whole the same as the one made in July. An important condition for a continued recovery is that the labour market improves. The high corporate profits create good conditions for this. Profits as a percentage of GDP are now at one of the highest levels since the early 1950s.

CPI inflation has fallen over the past year and is expected to be close to the target of 2 per cent during the forecast period. But rising energy prices, for instance, will mean that inflation is slightly higher than before during the autumn. The spare capacity in the US economy is expected to be relatively large in the coming years. It is therefore assumed in the forecast that monetary policy will remain very expansionary until the end of 2014, in line with the US central bank's most recent forecast.

■ Growth outlook for other countries divided

The severe slowdown in GDP growth in the United Kingdom during the second quarter of this year means that GDP is expected to fall by 0.4 per cent in 2012. Growth is expected to gradually increase as global economic activity improves. Domestic demand in the UK economy will also rise as the need for tighter fiscal policy declines. At the end of the forecast period, growth is expected to be marginally higher than in the previous forecast. This is partly the result of a more expansionary monetary policy, mainly in the form of further bond purchases and various measures to stimulate credit supply. Inflation, which is currently relatively high, is expected to fall during the coming years, and at the end of the forecast period to be in line with the target.

In Norway, GDP is expected to grow by almost 4 per cent this year and growth prospects are good for 2013 and 2014, too. The rapid growth is mainly due to good growth in employment and real wages, an expansionary monetary policy and large incomes from the oil industry. Inflation in Norway is low, largely because of the large appreciation of the Norwegian krona during 2011. Inflation is expected to be around 1 per cent during 2012, and then to rise towards the target of 2.5 per cent at the end of the forecast period. In line with the forecast by Norges Bank, the policy rate is expected to remain at the current level of 1.5 per cent for the remainder of 2012 and then gradually begin to rise slowly.

GDP growth in Japan is expected to be 2.7 per cent this year. Substantial investment at the beginning of this year is an important contributing factor to the relatively high growth. Activity in the Japanese economy is expected to be weaker next year, however. The Chinese

economy is growing at a rapid pace, compared with many other countries. But weak global demand means that GDP growth in China is now expected to be lower than was forecast in the July Monetary Policy Report. Inflation is still low and below the government's target of 4 per cent, so there is scope for continued expansionary fiscal and monetary policy.

■ **The krona has strengthened faster than expected**

Since the monetary policy meeting in July, the krona has strengthened against most other currencies. The forecast in July was for the krona to strengthen over the coming years, but this has happened more quickly than expected. There are several likely explanations for this, which are linked to developments in Sweden in relation to those abroad. For example, Swedish GDP growth has been unexpectedly strong, while statistics from the euro area have pointed towards growth remaining weak. Sweden's relatively strong public finances have probably also played a role. Monetary policy easing in the euro area has contributed to increasing the difference between Swedish interest rates and those abroad, which may also be significant. The Riksbank's assessment is that the krona is at present close to its long-run level, and that it will remain around this level during the coming years.

■ **Strong growth in Sweden in the first half of the year**

Growth in Sweden during the first half of this year was surprisingly strong, particularly given the uncertain economic situation in the euro area. It was primarily Swedish exports that increased more than expected. However, during the remainder of the year growth in exports is expected to be slowed down by the weaker demand from abroad. Swedish households are still relatively optimistic and contributing to upholding demand in the Swedish economy. During next year, confidence is expected to strengthen and economic activity abroad to improve gradually. This means that export growth will increase and investment will accelerate. Strong public finances and a stable Swedish banking sector, together with an expansionary monetary policy will also contribute to increasing growth in the Swedish economy during 2013 and 2014. Swedish GDP is expected to increase by 1.5 per cent this year, by 1.9 per cent next year and by 2.8 per cent in 2014.

■ **Modest increase in household consumption**

Household consumption has increased at a relatively good pace over recent quarters. Given the uncertain developments abroad, households are relatively optimistic. However, households' net wealth has deteriorated over the past year, despite a rise on the stock market during the summer. Wealth will show weak development in the coming period, mainly due to a subdued development in housing prices. Household wealth in relation to income is still at a high level, seen from an historical perspective. The subdued housing market will mean that lending to households increases at a slower pace. Household debt as a percentage of disposable income is still at a high level, however, just over 170 per cent. The debt ratio is expected to remain at roughly the same level over the coming years.

The deterioration in the labour market over the coming year will mean that household incomes increase more slowly, which will dampen growth in consumption somewhat. Then, during 2013 and especially 2014, household incomes will rise as the situation on the labour market improves and wages increase at a faster rate. Households will thus increase their consumption gradually during the forecast period.

■ **Unexpectedly strong Swedish exports will slow down**

Swedish exports fell substantially at the end of 2011, and then increased during the first two quarters of this year. However, the weak developments in several of Sweden's most important export markets will hold back growth in exports in the coming period. Indicators such as orders to the Swedish export industry also point to a slowdown. In addition, the krona has strengthened faster than expected. All in all, this means that Swedish exports are expected to increase moderately in 2012. But as demand in the euro area increases and international economic activity improves, Swedish exports will pick up again in 2013 and especially in 2014.

■ **Cautious companies postponing investments**

Total fixed gross investment is expected to show a weak increase over the coming period and then to gradually pick up speed during the latter part of 2013. This is connected to the assumption that uncertainty over developments in the euro area will subside then, which will lead to higher demand and thus an increased investment requirement. Once uncertainty wanes, companies are expected to make planned investments that were postponed earlier. In the manufacturing industry, in particular, there is an underlying need for investment, as the level of investment there is very low in relation to production. This points to investment being able to increase quickly when demand accelerates. Housing investment, which is now declining rapidly, is also expected to gradually pick up as the prospects for the economy as a whole improve.

■ **Stable public finances**

The Riksbank's fiscal policy forecasts are based on an assessment of what can be regarded as a normal fiscal policy in relation to the economic cycle. They also assume that the government's target of a 1 per cent budget surplus over an economic cycle will be attained. At present, public sector saving is assessed to be close to zero. During 2014, when the labour market improves, financial saving will increase somewhat to 0.5 per cent of GDP. The forecast includes tax cuts and increases in public expenditure in the magnitude of SEK 30 billion, divided between 2013 and 2014. This is the same assumption as made in the July Monetary Policy Report and in line with what the government notified in its recent forecast in August.

■ **Moderate weakening of the labour market**

Over the past year, the Swedish labour market has been stable. The percentage of the working-age population in work has remained largely unchanged, and there has only been a moderate increase in unemployment. Indicators point to a weak development in the labour market over the coming six months, and the Riksbank assesses that employment will remain largely unchanged for the remainder of the year. This assessment is in line with the one presented in the Monetary Policy Report published in July. As the number of people in the labour force is expected to continue to increase, partly for demographical reasons, this means that unemployment will increase slightly further. As economic activity improves in 2013 and 2014, unemployment will fall and at the end of the forecast period it is expected to be around 6.5 per cent.

The number of hours worked has been weak in relation to GDP in 2012. During 2013 and 2014, however, the number of hours worked is expected to recover as demand in the Swedish economy increases.

■ Low but rising resource utilisation

The Riksbank's overall assessment is that resource utilisation is at present slightly lower than normal. This assessment is supported by the Riksbank's indicators of resource utilisation, which summarise the information from surveys and from the labour market. According to statistics from Statistics Sweden and the National Institute of Economic Research, capacity utilisation in the manufacturing industry is currently normal or slightly lower than normal. GDP in relation to its long-run trend also indicates normal or slightly lower than normal resource utilisation. Indicators on the labour market, such as labour shortages, unemployment, the employment rate and the hours worked gap, that is, the difference between the actual number of hours worked and the sustainable level, also imply spare capacity in the economy.

As economic activity strengthens, GDP and the number of hours worked will increase at a faster pace. This means that resource utilisation will increase and normalise during the latter part of the forecast period. This outlook is roughly the same as in July.

■ Gradual increase in wages

More than three quarters of the wage agreements in this year's wage bargaining rounds have been signed, and so far the industrial agreement of 2.6 per cent has acted as norm. According to the short-term wage statistics, wages are expected to increase at a faster rate over the coming two years in relation to this year. During the forecast period they are expected to increase by on average around 3.3 per cent a year, which is slightly less than the historical average.

The unexpectedly high GDP outcome for the second quarter entails an unexpectedly strong labour productivity. The forecast for productivity growth is thus revised up, mainly with regard to this year. Labour unit costs are expected to increase by an average of 1.9 per cent a year during the forecast period. This is more than in recent years, but in line with the historical average. Compared with the forecast in July, unit labour costs are expected to increase at a slower pace, particularly this year.

■ Low inflationary pressures ...

Inflation is low at present. Inflationary pressures in the economy have been low for some time, because of the low rate of increase in unit labour costs, the stronger krona and the low resource utilisation. Compared with the assessment in July, cost pressures have declined further, which will contribute to lower inflation in the coming period. The lower cost pressures are mainly due to lower unit labour costs and the stronger krona.

As economic activity strengthens and resource utilisation increases, wages will rise faster and CPIF inflation will rise towards 2 per cent at the beginning of 2014. A more expansionary monetary policy that stimulates the economy will also contribute to maintaining the rate of price increase in the coming period. CPI inflation will rise more than CPIF inflation, as households' interest expenditure will increase at a faster pace when the Riksbank begins to raise the repo rate. CPI inflation is expected to be 3 per cent at the end of 2014. During periods with large interest rate adjustments, measures of inflation that do not include interest expenditure, such as CPIF inflation, provide a better picture of inflationary pressures. In the longer run, when the repo rate has stabilised, CPI and CPIF inflation will converge.

CPIF inflation excluding energy has been revised down slightly for most of the forecast period as a result of the lower cost pressures. However, the higher energy prices mean that CPIF inflation is now expected to be higher over the coming period than was assessed in July, and is then expected to be lower.

■ **...justify a lower repo rate**

Developments in countries important to Sweden are currently expected to be relatively weak. This means that GDP growth in Sweden will also be relatively weak in the coming year. It is therefore hardly likely that the very rapid growth during the first half of the year will push up inflation, particularly as the high GDP growth has gone hand in hand with an unexpectedly high productivity growth. This, together with a faster appreciation of the Swedish krona than expected, means that cost pressures and inflation will be lower than was assessed in July.

The Executive Board of the Riksbank has decided to cut the repo rate to 1.25 per cent to prevent inflation from falling too low in the coming period. The repo rate is expected to remain at this level until the middle of next year, which will contribute to CPIF inflation rising to 2 per cent at the beginning of 2014.

The starting situation is that resource utilisation is lower than normal. When resource utilisation and inflation rise, the repo rate will be increased gradually and amount to almost 3.0 per cent at the end of the forecast period. The repo-rate path is lower throughout the forecast period than was forecast in the Monetary Policy Report published in July. Such a repo-rate path will contribute to inflation rising to 2 per cent and to resource utilisation normalising during the forecast period.

■ **Economic developments are uncertain**

The situation in the euro area is still fragile. If the situation worsens substantially, this could mean that Swedish households and companies become more cautious, demand could weaken and inflation could be lower than assumed in the forecast. On the other hand, if the Swedish economy proves to be unexpectedly resilient and if confidence among households and companies rises more quickly than expected, this could lead to higher demand and inflation.

The Riksbank assesses that the krona will remain at roughly its present level in the coming period. Normally, however, the krona weakens in periods of uncertainty, and this could also happen over the next few years, particularly if financial unease intensifies. However, the krona may also appreciate more than is assumed in the forecast. This could happen if Sweden's relatively stronger economy leads to a greater demand for Swedish assets, because they are perceived to be a relatively safer investment.

Both the economic outlook abroad and the exchange rate may thus develop differently than in the main scenario and thereby have different effects on growth and inflation in Sweden. This could also mean that the monetary policy stance is a different one.

■ New information since the July Monetary Policy Report

Financial markets

- During the summer, concern over the crisis in Europe has continued to affect developments on the financial markets. Yields on bonds issued by European countries with sound public finances, such as Germany and Sweden, have been very low. On the other hand, borrowing costs on the bond market have remained high for Spain and Italy, as a result of their problems with public finances. In Spain, both the regions and the banks are experiencing problems with their finances, which has contributed to speculations that Spain risks needing to apply for a full-scale support package for the country as a whole.
- Developments on the stock markets show that the broad stock market indexes in Sweden, the United States and the euro area have risen since July. At the same time, the volatility on the stock markets has declined. Stress indicators point to the unease on the financial markets possibly having declined somewhat since July.
- Weaker growth prospects have led to a decline in monetary policy expectations, regarded in terms of forward rates, in the United Kingdom and the euro area since the July monetary policy meeting, while expectations remain low in the United States. At the beginning of July the ECB cut its policy rate by 0.25 percentage points to 0.75 per cent, and the Bank of England increased its asset purchase programme by GBP 50 billion to GBP 375 billion.
- In connection with its interest rate decision in August, the ECB signalled that it was prepared to take measures if the situation in the countries with sovereign debt problems worsened. One possible measure is to purchase government securities with a short maturity, on condition that the country in need of support applies for assistance to the EFSF or ESM. The ECB's statement contributed to yield levels on bonds with a shorter maturity in Italy and above all Spain falling somewhat from the highest levels attained at the end of July. In response to the Spanish government's application for support for the banks, the Eurogroup finance ministers have agreed to provide assistance in the form of joint loans. With the aim of making the funds more flexible and efficient, the ECB and the EFSF have signed a technical agreement that means the ECB can intervene on the secondary market for government bonds on behalf of the EFSF.
- Pricing on the Swedish money market indicates that the Riksbank is expected to cut the repo rate to just over 1 per cent at the end of 2012. Various surveys also show that the market expects a lower repo rate towards the end of the year. According to the latest Prospera survey, money market participants are counting on the Riksbank's repo rate being 1.3 per cent in a year's time. Towards the end of 2014 the repo rate is expected to be 1.6 per cent.
- The average mortgage rate paid by households continued to fall in July, but the banks' and mortgage institutions' listed mortgage rates indicate that the actual borrowing rates charged to households were almost unchanged in August. According to the National Institute of Economic Research's Economic Tendency Survey, households are expecting short-term mortgage rates to increase over the coming year. However, the bank lending rates companies are charged rose slightly in July.

- The krona has strengthened over the summer. In trade-weighted terms, the krona increase has at most amounted to around 5 per cent, compared with early July. The krona has been noted at its strongest level in over ten years, both against the euro and in trade-weighted terms. Economic statistics that have been relatively strong in Sweden compared with the rest of the world, combined with higher market rates in Sweden than abroad, and the relatively strong Swedish public finances, have probably contributed to strengthening the krona.
- The price of crude oil has risen since the end of June, and forward pricing indicates a higher oil price during 2012 than was forecast in the Monetary Policy Report published in July. There are several reasons why the oil price has risen. During the oil strike in Norway during the summer, the supply of oil declined. At the same time, maintenance work on oil platforms in the North Sea has resulted in lower production. In the Middle East, the EU's sanctions against oil imports from Iran were implemented in full on 1 July as a reaction to Iran's potential nuclear weapons programme.

International economy

- GDP in the euro area fell by 0.8 per cent in the second quarter of this year, when calculated as an annual rate. GDP fell in Spain and Italy, among other countries, while GDP in Germany increased by a good 1.2 per cent, when calculated as an annual rate. Various indicators for the third quarter point to continued weak developments, for instance, the European Commission's confidence survey fell in both July and August. Consumer confidence also fell substantially, and is now down at the lowest level for three years. Although the purchasing managers' index for the manufacturing industry rose somewhat in August, the index for the services sector remained at a low level. The labour market has weakened further. The number of unemployed rose in July and unemployment remained at the record-high level of 11.3 per cent. The inflation rate was 2.6 per cent in August, according to preliminary statistics.
- GDP growth in the United States increased by 1.7 per cent during the second quarter, when calculated as an annual rate. According to the University of Michigan, consumer confidence rose slightly in August, but it is still at low levels. Consumption rose at the beginning of the third quarter and there are signs that the housing market situation is improving. The time it takes to sell a house has continued to fall to levels below the historical average and confidence among construction companies has risen in recent months. However, the recovery on the labour market has slowed down over the summer, and unemployment rose marginally in July. Inflation in the United States, measured as the annual change in the consumption deflator (PCE), has fallen rapidly in recent months and was 1.3 per cent in July. CPI inflation in July amounted to 1.4 per cent, while CPI inflation adjusted for energy and food prices was 2.1 per cent.
- In the United Kingdom, GDP fell by 1.8 per cent during the second quarter, when calculated as an annual rate. The downturn was reinforced by temporary factors, such as more public holidays than normal. However, developments were weak even taking into account these temporary factors. Inflation rose slightly in July, to 2.6 per cent. In addition to the increase in its asset purchase programme, the Bank of England and the government have introduced a joint programme that aims to increase lending to

households and companies. The idea is to reduce the banks' funding costs in exchange for these new funds being used for lending.

- Norwegian GDP growth was around 3.9 per cent, when calculated as an annual rate, during the second quarter of this year. Norwegian industrial production rose in June, while foreign trade showed a significant surplus. Inflation measured as an annual percentage change in consumer prices fell to 0.2 per cent in July, and inflationary pressure is expected to remain low in 2012.
- During the second quarter of this year, Japan's GDP increased by 1.4 per cent, when calculated as an annual rate. Industrial production showed a weaker development than expected in June, partly as a result of lower exports of cars to the United States. In China, GDP growth increased by 7.4 per cent during the second quarter, when calculated as an annual rate. During June and July, the central bank and the government have implemented a number of monetary and fiscal policy measures to stimulate growth. The central bank has cut its lending rate in two steps by a total of 56 basis points. At the same time, the government has brought forward its investments in infrastructure, for instance, which has increased the investment levels. Growth in Brazil was a good 1.6 per cent during the second quarter, when calculated as an annual rate. Indicators point to growth this year being slightly weaker than was assessed in July.

GDP in Sweden

- GDP in Sweden increased by as much as 5.7 per cent in the second quarter of this year, when calculated at an annual rate.¹ Compared with the same quarter one year earlier, GDP in Sweden grew by 2.3 per cent (calendar-adjusted). The outcome shows that Swedish exports increased rapidly, despite the unease abroad. GDP growth was much stronger than forecast by the Riksbank in the Monetary Policy Report in July. However, the increase in domestic demand was in line with the forecast. Growth in the Swedish economy is expected to be significantly lower during the second half of the year than it was during the first half of the year. A contributing factor is the weak demand from abroad, which will lead to slower growth in Swedish exports.
- However, the indicators point to weak growth in the Swedish economy in the period immediately ahead. The Economic Tendency Survey of the National Institute of Economic Research increased somewhat in August but is below its historical average. With reference to the different parts of the business sector, it was mainly the service branches that contributed to this increase, while sentiment in the manufacturing industry weakened further. The weak industrial activity was confirmed by the purchasing managers' index for August, which fell to the lowest level since 2009.
- Household consumption increased by 0.8 per cent during the second quarter of this year, compared with the same quarter last year. There was strong growth in the consumption of services while the consumption of durable goods was relatively weak. Retail sales increased in July but consumer confidence declined somewhat in August. However, confidence is still above the historical average.

¹ The initial version for the second quarter is based on more limited data and is more uncertain than a regular round of calculations. Statistics Sweden points out that the outcome is in part based on less reliable data than usual.

- Household borrowing has gradually declined and there has been a clear falling trend since the beginning of 2010. The annual growth rate for household borrowing fell further in July, to 4.4 per cent. Price increases on the housing market have been subdued and prices are now at roughly the same level as a year ago. According to Valueguard's index (HOX), which examines recent trends, prices for single-family dwellings fell in July while prices for tenant-owned apartments increased somewhat.
- Exports increased by 1.7 per cent in the second quarter compared to the corresponding quarter last year, which was significantly faster than forecast in the Monetary Policy Report in July. Service exports were particularly strong, while growth in goods exports was more subdued. Weak developments in large parts of Europe are expected to hold back Swedish exports in the period ahead. Export orders have increased somewhat but are weaker than normal and the foreign trade statistics for July support the picture of weak exports in the period ahead.
- Gross fixed capital formation increased by 1.8 per cent during the second quarter, compared with the corresponding quarter last year. Statistics Sweden's investment survey in May indicates a moderate increase in investment in 2012 as a whole, which means that growth will be weaker than normal in the second half of the year. The number of housing starts indicates that housing investment will remain weak for some time. Investment in stocks is expected to make a negative contribution to GDP growth in the period immediately ahead. This is because there is less need to build up stocks when demand declines.
- In the second quarter, public consumption expenditure increased by 1.1 per cent compared with the corresponding period last year. This was faster than expected in the previous forecast. It was above all the expenditure of the central government and the county councils that increased, while the expenditure of the municipalities fell.

Labour market

- The development of the Swedish labour market has been somewhat better over the previous two months than was expected in the July Monetary Policy Report. The number of those employed and the number of people in the labour force have been marginally higher than earlier calculations. The seasonally-adjusted unemployment rate reached 7.5 per cent in July, which was somewhat lower than the forecast in July. However, the number of hours worked was slightly less than expected during the second quarter.
- Outcomes and indicators do not suggest any clear deterioration in the immediate future. The number of new job vacancies reported to the Employment Service has increased somewhat recently and the number of redundancy notices is still at a relatively low level. However, according to the latest Economic Tendency Survey, companies in the business sector as a whole have become more pessimistic about the development of employment.
- The National Mediation Office's short-term wage statistics indicate that wages in the entire economy rose by an average of 2.4 per cent, calculated as an annual percentage change, during January to May this year. This figure will be revised up as retroactive wages are paid out. The assessment is that wages will increase by 3.1 per cent this year,

which is a marginal downward revision compared with the assessment in the July Monetary Policy Report.

- Statistical data from tax returns up to the end of June this year indicate that wage sums and labour costs in the economy as a whole grew somewhat more slowly during the second quarter than was assessed in the July Monetary Policy Report. The number of hours worked was also somewhat lower than the assessment in July. The surprisingly strong growth in GDP also means that labour productivity has developed unexpectedly strongly. All in all, unit labour costs are thus increasing more slowly this year than previously assessed.

Inflation

- The outcomes for the CPI and CPIF were in line with the forecasts in the July Monetary Policy Report. In July, the annual rate of increase in the CPI stood at 0.7 per cent. The annual rate of increase in the CPIF, that is, the CPI with a fixed mortgage rate, amounted to 0.8 per cent. Low electricity prices during the summer have helped to keep the rate of increase in both the CPI and the CPIF low. When adjusted for changes in energy prices, the rate of increase in the CPIF was somewhat higher at 1.1 per cent.
- Towards the end of the year CPIF inflation will rise to approximately 1.5 per cent, which is mainly due to an increasing rate of increase in the price of oil products. Adjusted for energy prices, the assessment is that the rate of inflation will remain low in the months ahead. A strengthening of the krona and low unit labour costs have helped to keep inflation low. The annual rate of increase in the CPI will be somewhat lower than for the CPIF over the next few months, as households' interest expenditure is increasing at a slower rate than previously.
- According to the National Institute of Economic Research's Business Tendency Survey, households' inflation expectations one year ahead fell marginally from 2.2 per cent in July to 2.1 per cent in August. The Prospera survey of inflation expectations among participants on the money market showed that expectations one and two years ahead remained unchanged between July and August. One year ahead, market participants expect the rate of inflation to be 1.4 per cent, while two years ahead they expect it to be 1.8 per cent. Inflation expectations five years ahead amount to 2 per cent.

■ Tables

The forecast in the previous Monetary Policy Report is shown in brackets.

Table 1. Repo rate forecast

Per cent, quarterly average values

	Q2 2012	Q3 2012	Q4 2012	Q3 2013	Q3 2014	Q3 2015
Repo rate	1.5	1.5 (1.5)	1.3 (1.4)	1.4 (1.6)	2.2 (2.4)	2.9 (3.1)

Source: The Riksbank

Table 2. Inflation

Annual percentage change, annual average

	2011	2012	2013	2014
CPI	3.0 (3.0)	1.2 (1.1)	1.3 (1.7)	2.6 (2.8)
CPIF	1.4 (1.4)	1.1 (1.0)	1.6 (1.7)	2.0 (2.1)
CPIF excl. energy	1.0 (1.0)	1.1 (1.2)	1.5 (1.7)	2.0 (2.0)
HICP	1.4 (1.4)	1.1 (1.0)	1.5 (1.7)	2.0 (2.1)

Note. The CPIF is the CPI with a fixed mortgage rate. HICP is an EU harmonised index of consumer prices.

Sources: Statistics Sweden and the Riksbank

Table 3. Summary of financial forecasts

Per cent, unless otherwise stated, annual average

	2011	2012	2013	2014
Repo rate	1.8 (1.8)	1.5 (1.5)	1.4 (1.6)	2.0 (2.3)
10-year rate	2.7 (2.7)	1.6 (1.6)	2.1 (2.5)	3.3 (3.5)
Exchange rate, TCW-index, 18 Nov. 1992 = 100	122.3 (122.3)	120.4 (122.6)	116.9 (118.6)	118.0 (118.2)
General government net lending*	0.1 (0.1)	-0.2 (0.1)	-0.5 (0.2)	0.5 (1.0)

* Per cent of GDP

Sources: Statistics Sweden and the Riksbank

Table 4. International conditions

Annual percentage change, unless otherwise stated

GDP	2011	2012	2013	2014
Euro area (0.14)	1.5 (1.5)	-0.4 (-0.4)	0.5 (0.4)	1.9 (1.9)
USA (0.19)	1.8 (1.7)	2.3 (2.2)	2.4 (2.4)	3.2 (3.2)
Japan (0.06)	-0.7 (-0.7)	2.7 (2.7)	1.4 (1.6)	1.2 (1.0)
OECD (0.54)	1.9 (1.9)	1.6 (1.5)	1.9 (1.9)	2.7 (2.6)
TCW-weighted (0.46)	1.3 (1.3)	0.4 (0.4)	1.1 (1.1)	2.1 (2.1)
World (1.00)	3.9 (3.9)	3.5 (3.5)	3.8 (3.7)	4.3 (4.2)

Note. The figures in parentheses indicate the global purchasing-power adjusted GDP-weights, according to the IMF, 2011.

CPI	2011	2012	2013	2014
Euro area (HICP)	2.7 (2.7)	2.5 (2.4)	1.8 (1.6)	1.6 (1.7)
USA	3.2 (3.2)	2.1 (2.0)	1.9 (1.8)	2.0 (1.9)
Japan	-0.3 (-0.3)	0.1 (0.1)	0.0 (0.1)	0.3 (0.3)
TCW-weighted	2.6 (2.6)	2.1 (2.1)	1.7 (1.6)	1.6 (1.7)

	2011	2012	2013	2014
Policy rates in the rest of the world, TCW-weighted, per cent	0.8 (0.8)	0.3 (0.4)	0.3 (0.4)	0.4 (0.7)
Crude oil price, USD/barrel Brent	111 (111)	113 (105)	110 (95)	104 (93)
Swedish export market	4.0 (3.9)	1.2 (1.4)	3.8 (3.5)	6.5 (6.3)

Note. The Swedish export market index is calculated as a weighted average of the imports of the 15 countries which are the largest recipients of Swedish exports. They receive approximately 70 per cent of Swedish exports. The weight assigned to a country is its share of Swedish exports of goods.

Sources: Eurostat, IMF, Intercontinental Exchange, OECD and the Riksbank

Table 5. GDP by expenditure

Annual percentage change, unless otherwise stated

	2011	2012	2013	2014
Private consumption	2.0 (2.0)	1.7 (1.5)	1.8 (1.6)	2.4 (2.5)
Public consumption	1.8 (1.8)	0.9 (0.5)	1.0 (0.9)	0.7 (0.7)
Gross fixed capital formation	6.2 (6.2)	4.1 (4.7)	2.6 (1.5)	5.5 (5.5)
Inventory investment*	0.6 (0.6)	-1.0 (-1.2)	0.0 (0.2)	0.1 (0.1)
Exports	6.9 (6.9)	1.3 (-0.3)	3.9 (3.4)	6.5 (6.5)
Imports	6.3 (6.3)	-0.2 (-0.5)	3.8 (3.4)	6.8 (6.7)
GDP	3.9 (3.9)	1.5 (0.6)	1.9 (1.7)	2.8 (2.8)
GDP, calendar-adjusted	4.0 (4.0)	1.9 (0.9)	1.9 (1.7)	2.9 (2.9)
Final figure for domestic demand*	2.6 (2.6)	1.8 (1.7)	1.6 (1.3)	2.4 (2.4)
Net exports*	0.7 (0.7)	0.7 (0.1)	0.3 (0.2)	0.3 (0.3)
Current account (NA), per cent of GDP	7.0 (7.0)	7.2 (6.6)	7.2 (6.6)	7.2 (6.5)

*Contribution to GDP growth, percentage points

Note. The figures show actual growth rates that have not been calendar-adjusted, unless otherwise stated. NA is the National Accounts.

Sources: Statistics Sweden and the Riksbank

Table 6. Production and employment

Annual percentage change, unless otherwise stated

	2011	2012	2013	2014
Population, aged 16-64	0.3 (0.3)	0.1 (0.1)	0.2 (0.2)	0.2 (0.2)
Potential hours worked	0.8 (0.8)	0.6 (0.6)	0.5 (0.5)	0.4 (0.4)
GDP, calendar-adjusted	4.0 (4.0)	1.9 (0.9)	1.9 (1.7)	2.9 (2.9)
Number of hours worked, calendar-adjusted	2.3 (2.2)	0.3 (0.5)	0.3 (0.1)	1.1 (0.9)
Employed, aged 15-74	2.1 (2.1)	0.4 (0.3)	0.4 (0.4)	1.1 (1.1)
Labour force, aged 15-74	1.2 (1.2)	0.5 (0.4)	0.5 (0.5)	0.3 (0.3)
Unemployment, aged 15-74*	7.5 (7.5)	7.6 (7.6)	7.6 (7.7)	6.9 (7.0)

* Per cent of labour force

Note. Potential hours refer to the the long-term sustainable level for the number of hours worked according to the Riksbank's assessment.

Sources: Statistics Sweden and the Riksbank

Table 7. Wages and unit labour cost for the economy as a whole

Annual percentage change, calendar-adjusted data, unless otherwise stated

	2011	2012	2013	2014
Hourly wage, NMO	2.5 (2.6)	3.1 (3.1)	3.3 (3.2)	3.4 (3.5)
Hourly wage, NA	3.3 (3.4)	3.4 (3.3)	3.5 (3.5)	3.7 (3.8)
Employer's contribution*	-0.2 (-0.2)	0.1 (0.2)	0.0 (0.0)	0.0 (0.0)
Hourly labour cost, NA	3.1 (3.1)	3.5 (3.5)	3.5 (3.5)	3.7 (3.8)
Productivity	1.7 (1.7)	1.5 (0.4)	1.6 (1.7)	1.8 (1.9)
Unit labour cost	1.4 (1.4)	1.9 (3.1)	1.9 (1.8)	1.9 (1.8)

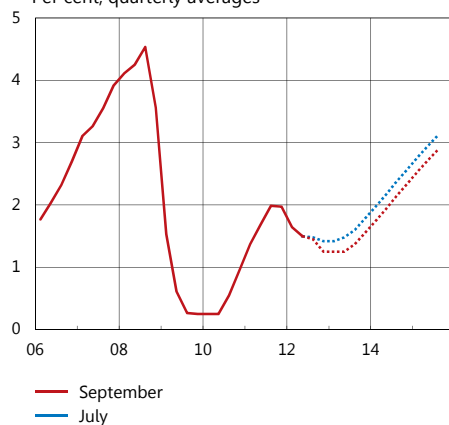
* Contribution to the increase in labour costs, percentage points.

Note. NMO is the National Mediation Office's short-term wage statistics and NA is the National Accounts. Labour cost per hour is defined as the sum of actual wages, collective charges and wage taxes divided by the seasonally adjusted total number of hours worked. Unit labour cost is defined as labour cost divided by seasonally adjusted value added at constant prices.

Sources: National Mediation Office, Statistics Sweden and the Riksbank

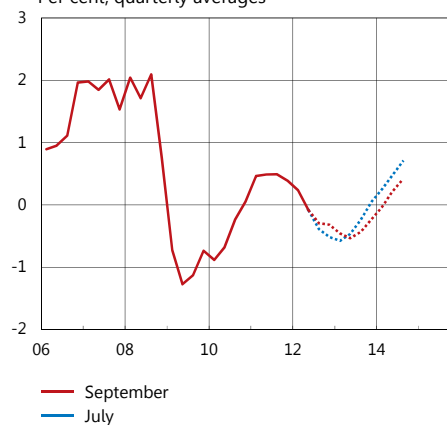
■ Figures

Figure 5. Repo rate
Per cent, quarterly averages



Source: The Riksbank

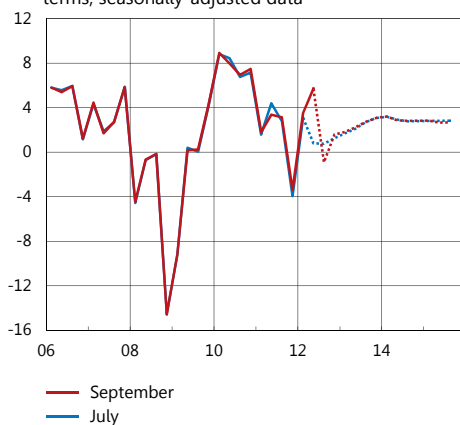
Figure 6. Real repo rate
Per cent, quarterly averages



Note. The real repo rate is calculated as an average of the Riksbank's repo rate forecasts for the coming year minus the inflation forecast (CPIF) for the corresponding period.

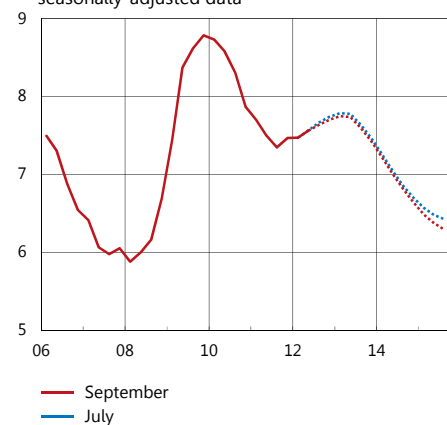
Source: The Riksbank

Figure 7. GDP
Quarterly changes in per cent calculated in annualised terms, seasonally-adjusted data



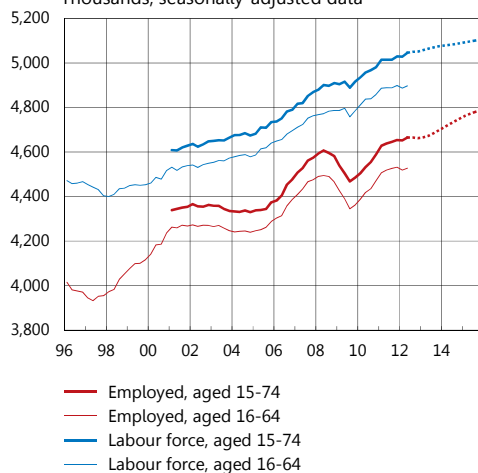
Sources: Statistics Sweden and the Riksbank

Figure 8. Unemployment
Per cent of the labour force, aged 15-74, seasonally-adjusted data



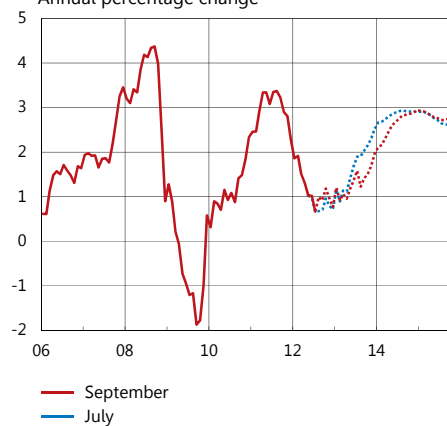
Sources: Statistics Sweden and the Riksbank

Figure 9. Labour force and number of employed
Thousands, seasonally-adjusted data



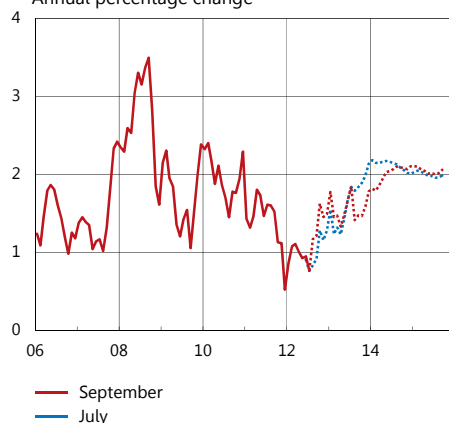
Sources: Statistics Sweden and the Riksbank

Figure 10. CPI
Annual percentage change



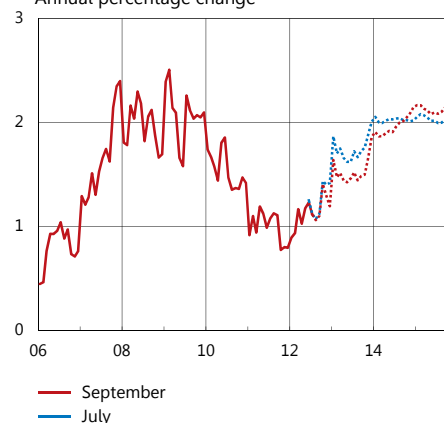
Sources: Statistics Sweden and the Riksbank

Figure 11. CPIF
Annual percentage change



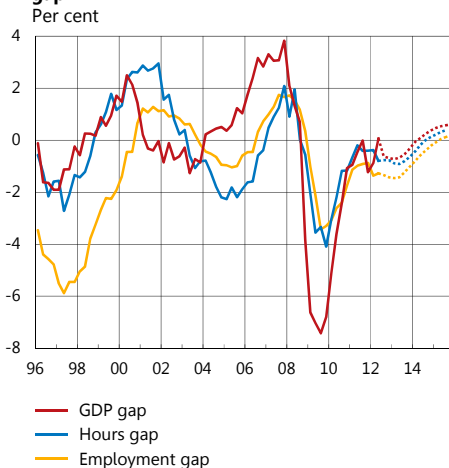
Note. The CPIF is the CPI with a fixed mortgage rate.
Sources: Statistics Sweden and the Riksbank

Figure 12. CPIF excluding energy
Annual percentage change



Note. The CPIF is the CPI with a fixed mortgage rate.
Sources: Statistics Sweden and the Riksbank

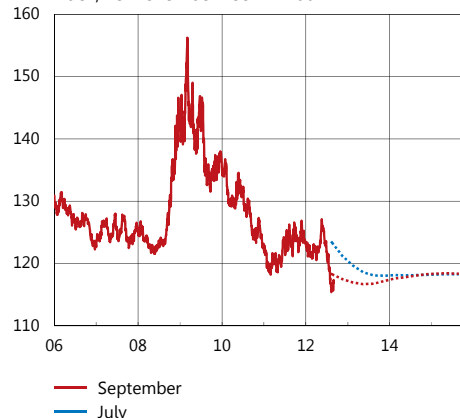
Figure 13. GDP gap, hours gap and employment gap
Per cent



Note. GDP gap refers to the deviation from trend in GDP calculated using a production function. The hours gap refers to the deviation in the number of hours worked from the Riksbank's assessed trend.

Sources: Statistics Sweden and the Riksbank

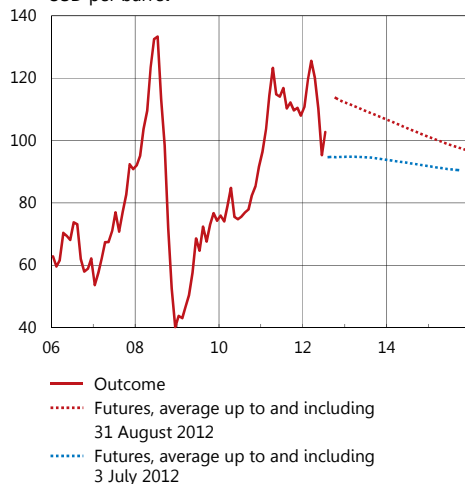
Figure 14. TCW-weighted nominal exchange rate
Index, 18 November 1992 = 100



Note. Outcome data are daily rates and forecasts are quarterly averages. TCW refers to a weighting of Sweden's most important trading partners.

Source: The Riksbank

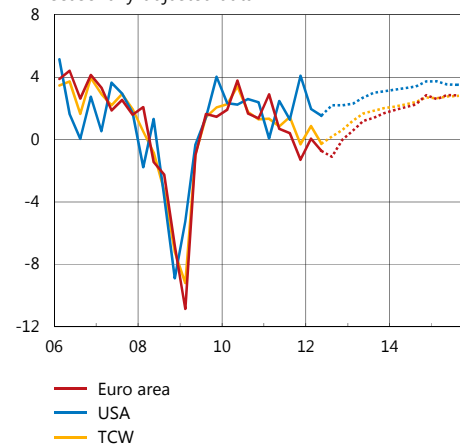
Figure 15. Oil price, Brent crude
USD per barrel



Note. Futures are calculated as a 15-day average. Outcomes represent monthly averages of spot prices.

Sources: Intercontinental Exchange and the Riksbank

Figure 16. GDP in different regions and countries
Quarterly changes in per cent, annual rate, seasonally-adjusted data



Note: TCW refers to a weighting of Sweden's most important trading partners.

Sources: Bureau of Economic Analysis, Eurostat and the Riksbank