



# Monetary Policy Update

## December 2013

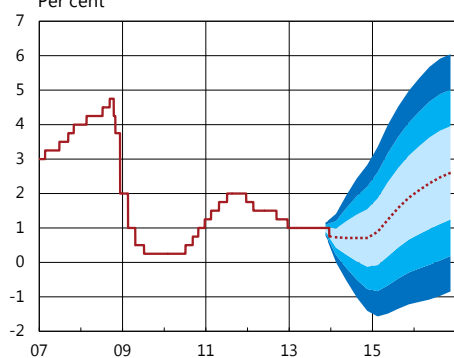
The recovery in global economic activity is continuing, although inflationary pressures abroad are lower than expected. An expansionary monetary policy supports economic activity and several large central banks have communicated that their policy rates will be low for a long time to come. The prospects for the euro area are improving and growth in the United States is on increasingly stable ground.

After just over a year of weak growth, prospects for the Swedish economy are brightening. The labour market has improved and confidence in the Swedish household and corporate sectors has continued to rise. Together with a gradual increase in demand from abroad, this means that growth will pick up next year. The demand for labour should therefore increase further and unemployment should fall more tangibly.

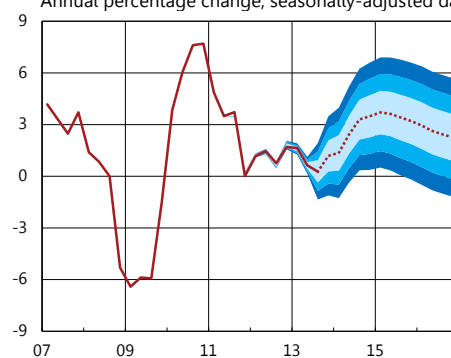
For some time now, monetary policy has involved balancing how low the repo rate needs to be for inflation to approach the target soon enough against the increased risks linked to households' high indebtedness that can stem from a low interest rate. Inflation has been unexpectedly low and, despite the recovery, inflationary pressures over the coming year are expected to be much lower than was forecast in the October Monetary Policy Report. This means that the need for short-term stimulus weighs heavier. At the same time, households' high indebtedness remains a risk to sustainable long-run development.

Given the unexpectedly low inflation and that inflationary pressures are expected to be lower in the coming period, the Executive Board of the Riksbank has decided to cut the repo rate by 0.25 percentage points to 0.75 per cent. The repo rate is expected to remain at this level until the beginning of 2015, before gradual increases begin. It is assessed that the recovery will then be on firmer ground and that inflation will be rising. In this way, monetary policy will contribute to CPIF inflation rising towards 2 per cent.

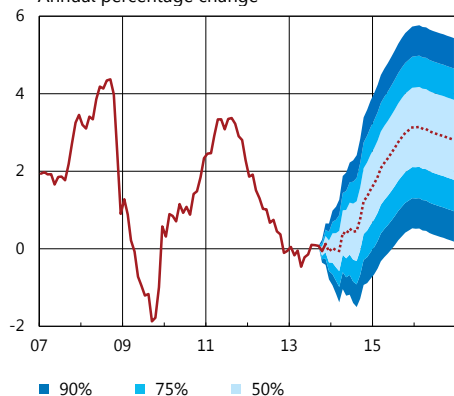
**Figure 1. Repo rate with uncertainty bands**  
Per cent



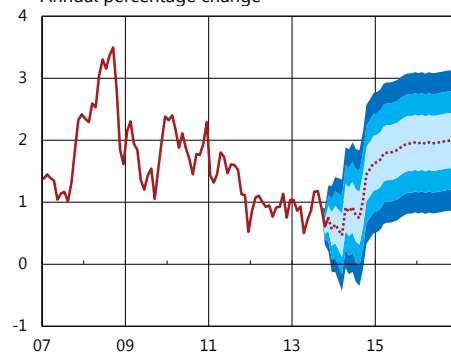
**Figure 2. GDP with uncertainty bands**  
Annual percentage change, seasonally-adjusted data



**Figure 3. CPI with uncertainty bands**  
Annual percentage change



**Figure 4. CPIF with uncertainty bands**  
Annual percentage change



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. Outcome data for the repo rate are daily rates and forecasts are quarterly averages.

Sources: Statistics Sweden and the Riksbank

## ■ 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 October 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 0.75 per cent. The repo rate is expected to remain at this level for roughly one year, after which it will begin to be raised gradually. At the end of the forecast period, the repo rate will be 2.6 per cent.

### ■ Continued recovery but low inflationary pressures

Global growth will continue to improve during the forecast period. GDP growth in the countries that are most important to the Swedish economy is expected to rise from around 1 per cent this year to 3 per cent in 2016. Growth is promoted by somewhat less tight fiscal policy in most countries in the coming period, monetary policy will remain expansionary and credit terms will be eased. All in all, economic prospects are roughly the same as when the previous assessment was made in October. At the same time, inflation abroad has fallen in recent months and been lower than expected. This has meant that the international inflation forecast, or more precisely the forecast for the countries with greatest significance for the Swedish economy, has been revised down. As in the October report, cost pressures abroad are expected to remain relatively modest in the coming period. But as growth and demand accelerate, inflation will rise somewhat. At the end of the forecast period, it is expected to be just over 2 per cent.

### ■ Expansionary monetary policy abroad

Several of the major central banks have communicated that their policy rates will remain low for a long time. As the US economy has strengthened, however, expectations of a more imminent tapering of the Federal Reserve's asset purchases have risen. This has led to a rise in government bond yields in the United States and the euro area recently, at the same time as prices of higher-risk assets, such as equities, have fallen tangibly. Various measures of risk, such as volatility and spreads, remain low, however. All in all, the expectations of a more imminent tapering of the asset purchases have had much smaller impact on the financial markets than when such expectations arose earlier this year.

### ■ Higher growth in the euro area going forward

The economic outlook for the euro area is continuing to improve slowly. GDP growth has been marginally positive for the past two quarters and various confidence indicators are pointing to continued growth. Developments are still marked by the need for both private and public sectors to reduce their debt, which means that the recovery will take time. But there are some positive signs. Credit terms have become somewhat less strict and interest rates to households and companies are falling in several countries. This, combined with rising global demand, improves the conditions for growth. At the same time, fiscal policy will be less tight in the coming period. All in all, the forecast is that GDP in the euro area will rise to around 2 per cent a year during the latter part of the forecast period.

The upturn in unemployment appears to have slowed down, but the relatively slow recovery over the coming years will mean that resource utilisation remains weak throughout the forecast period. Inflation is expected to rise slowly towards the ECB's target of inflation close to, but below, 2 per cent. The weak resource utilisation and low inflation mean that monetary policy will remain very expansionary. As before, necessary conditions for the

forecast are that the reform process in the euro area progresses and that credible measures are gradually implemented to manage the underlying structural problems. All in all, growth is expected to develop in line with the assessment in October, while inflation is expected to be lower.

#### ■ **US growth on more stable ground**

The situation in the US economy is continuing to improve. During 2013, GDP growth has increased, despite very tight fiscal policy. At the same time, employment has risen and unemployment has fallen. Corporate profits remain high and there are now some signs of rising incomes in the household sector. During the coming period, the conditions for growth will benefit from the fact that households, companies and banks have already made some progress in reducing their debts in relation to their incomes.

The fiscal policy agreement reached with regard to the US budget and debt ceiling at the end of October was temporary, and new decisions need to be reached to achieve a more long-term solution. A budget proposal for the budget years 2014 and 2015 has been approved by the House of Representatives, but more detailed decisions are required at the beginning of next year before the budget is determined. Moreover, a decision remains to be taken on the debt ceiling. The Riksbank's forecast is based on the assumption that decisions on the budget and raising the debt ceiling are taken before the deadline is exceeded. In this case, the budget consolidation can proceed during the coming years, but fiscal policy will become much less tight. All in all, GDP growth is expected to be 3 per cent in 2014 and just over 3 per cent in the following years. Inflation is expected to gradually rise during the forecast period, but the relatively low inflation rate means that monetary policy will remain very expansionary in the coming years. On the whole, growth is expected to be in line with the assessment made in October, while inflation is expected to be somewhat lower over the coming year.

#### ■ **Other export markets also improving**

Growth in the United Kingdom is expected to increase gradually in the coming years, partly as a result of better global demand and continued expansionary monetary policy. Moreover, growth in the United Kingdom will also benefit during the coming period from households and companies having made progress in reducing their debts in relation to their incomes. Inflation is expected to continue falling and be in line with the Bank of England's inflation target of 2 per cent at the end of the forecast period.

Growth prospects in Norway have been dampened and housing prices have fallen recently. In line with Norges Bank's forecast, housing prices are expected to continue to fall slightly in the coming period and GDP for the mainland economy is expected to grow by around 2.5 per cent on average in the coming years. The rate of inflation has slowed down somewhat during the autumn and is expected to fall below the inflation target of 2.5 per cent soon and to remain around 2 per cent for most of the forecast period. Norges Bank is therefore now expected to begin to raise its policy rate at a slower pace than was assumed in the October report.

In China, the changeover from investment-driven to consumption-driven growth in demand is proceeding. As in the October Monetary Policy Report, this is expected to lead to a somewhat lower rate of growth in the coming period. In addition, measures are expected to be taken to deal with the unsustainable lending to regional authorities and state-owned

companies, which should result in more restricted credit granting in the coming period and will also dampen growth. All in all, China's GDP is expected to grow by just over 7 per cent a year in the coming years, while inflation is expected to be around 3 per cent.

An expansionary economic policy has benefited growth in Japan and inflation has recently risen to just over 1 per cent. Going forward, the forecast for inflation and demand is largely affected by the planned VAT increases in April 2014 and October 2015. As in the assessment made in October, GDP growth is expected to slow down to 1 per cent a year during the period 2015-2016, while average inflation is expected to be in line with the target of 2 per cent.

### ■ Temporary weakening of the krona

The Swedish krona has weakened in trade-weighted terms (KIX) since the Monetary Policy Report was published in October. In nominal KIX terms, the krona has weakened by around 2 per cent since the end of October. The Riksbank's assessment is that the real exchange rate is currently in the weaker part of an estimated interval for its long-run level. The krona weakening is assessed as temporary and as economic activity improves and the policy rate is raised, the krona is expected to strengthen somewhat, both in real and nominal terms, during the forecast period.

### ■ GDP growth in Sweden will pick up next year

Growth in Sweden was low in the third quarter of this year. Both exports and consumption were weaker than expected. The prospects for the Swedish economy are brighter in the coming period. Confidence in both the household and corporate sectors has risen substantially and is now higher than normal. Expansionary fiscal and monetary policies are contributing to relatively high increases in household incomes and provide the right preconditions for stable growth in consumption in the coming period. Together with a continued recovery abroad, this means that the prospects for and increase in growth in the Swedish economy are good.

Global trade has begun to increase at a faster pace and as industrial activity improves abroad, Swedish export market growth will also improve, that is growth in imports in the countries to which Sweden exports. This will mean that Swedish exports begin to rise during the first half of 2014, which will also contribute to an increased need for investment. Once exports pick up, GDP growth will accelerate. According to Statistics Sweden's investment survey in October, companies in most sectors are planning to increase investment next year and housing investment has already begun to increase significantly. This year, GDP is expected to increase by 0.9 per cent, which is a slight upward revision compared with the forecast in October. The upward revision is linked to Statistics Sweden's upward revision of the figures for growth during the first half of the year. The more expansionary monetary policy means that the growth forecasts for 2015 and 2016 are also somewhat higher than the forecast in October. GDP is expected to increase by 2.5 per cent in 2014, 3.7 per cent in 2015 and 2.8 per cent in 2016.

### ■ Housing prices and indebtedness still rising

Housing prices have risen over the year. This is partly because of the low supply of housing in relation to demand, the low interest rates and households' increasingly positive view of economic prospects. Housing prices are expected to continue rising during the forecast

period. This means that larger loans will be required to purchase a home, which will push up household debt. Higher housing prices also mean that the value of households' real wealth will increase.

Growth in debt is expected to be somewhat higher than growth in incomes, and household debt as a percentage of disposable incomes is thus expected to increase by around 6 percentage points, to 178 per cent, at the end of 2016. All in all, growth in both housing prices and debt is expected to be slightly higher than in the October Monetary Policy Report. The expected increase in the banks' risk weight floor for mortgages has to some extent affected the forecast for debt and housing prices, although the effects are very uncertain.

#### ■ **Gradual strengthening in general government net lending**

The Riksbank's forecasts for fiscal policy are based on measures that have been notified and on an assessment based on how fiscal policy is usually adapted to economic activity and the surplus target. The Riksdag (the Swedish parliament) is expected to decide on unfinanced measures of just over SEK 20 billion for 2014, mainly aimed at households. General government net lending is expected to amount to -1.4 per cent of GDP in 2013 and -1.5 per cent of GDP in 2014. As economic activity improves, general government net lending is expected to gradually increase and become marginally positive in 2016. Compared with the October Monetary Policy Report, the forecast for general government net lending is slightly lower now. This is due in part to lower tax revenues during the forecast period.

#### ■ **Employment continuing to increase**

During 2013, there was an increase in both employment and the labour force, despite the relatively weak GDP growth. Employment has risen somewhat faster than the labour force recently, which has meant that unemployment has fallen. However, unemployment is still relatively high, during the autumn it has been close to 8.0 per cent.

The number of hours worked has not increased to the same extent as the number of persons employed over the past year, which has meant that average working hours have shown weak development. This is partly because the number of persons employed who are absent from work has increased. However, the low average working hours are assessed as temporary. During the coming period, average working hours are expected to rise as the number of hours worked increases. Indicators point to employment continuing to rise in the future. The employment rate, that is the percentage of employed as a share of the population aged 15-74, is expected to reach a higher level in 2016 than prior to the financial crisis.

Compared with the forecast made in October, developments on the Swedish labour market have been stronger than expected. The level of employment and the labour force are expected to be higher than in 2014, at the same time as unemployment falls somewhat faster. However, the assessment remains that unemployment will not begin to fall more tangibly until the second half of 2014. At the end of the forecast period, unemployment is expected to be 6.4 per cent.

### ■ Resource utilisation lower than normal but will rise

The Riksbank's overall assessment is that resource utilisation is at present lower than normal. The GDP gap and the hours worked gap, that is how much GDP and the number of hours worked deviate from their long-term trends, are currently negative. Unemployment is relatively high, and the employment rate is assessed as lower than its long-run sustainable rate. However, the low interest rate, together with the higher global demand, will lead to growth in the economy rising in the coming period and thus to an increase in employment and the number of hours worked. Towards the end of the forecast period resource utilisation is expected to be more or less normal. This is the same as the assessment made in October.

### ■ Rising wage increases when economic activity strengthens

The wage bargaining rounds for 2013 are now largely complete. Most of the agreements signed are for three years, which means that the next major round of collective bargaining will take place in 2016. This will involve around 400 wage agreements, covering 2.7 million employees, expiring in 2016. The agreed wage increases for the period 2014-2015 were on average 2.2 per cent a year for the economy as a whole. However, local wage formation and wage drift mean that the actual wage increases are expected to be higher than indicated by the agreement outcomes. Actual wages as measured in the short-term wage statistics are assessed to be around 3.1 per cent a year 2014-2016. The rate of wage increase is thus estimated to gradually rise during the forecast period due to the improvement in economic activity and the labour market. So far this year, wages have increased somewhat more slowly than expected, which means that the forecast in the short term has been revised down somewhat in relation to the assessment made in October.

Labour productivity has been relatively weak in recent years. Going forward, growth in labour productivity is expected to be higher as economic activity improves.

Cost pressures in the economy, in terms of unit labour costs, are determined by developments in both wage costs and labour productivity. The weak productivity growth has meant that cost pressures in the economy have been maintained and over the past two years they have increased by 2-3 per cent a year. In the coming period, when growth in labour productivity is higher, cost pressures will increase at a somewhat slower pace, by just under 2 per cent a year.

### ■ Low inflation for some time to come

In recent months, inflation has been lower than was forecast in October. The outcomes for October and November entail low price increases on services, while goods prices continued to fall. However, the fall in goods prices has slowed down in 2013, while service prices have increased more slowly than expected.

The rate of increase in service prices slowed across the board in October and is lower than the historical average. This means that service prices will continue to increase at a much slower pace than unit labour costs in the economy as a whole. One important explanation for the low inflation rate is thus assumed to be that companies have found it difficult to pass on their cost increases to consumers. This could in turn be because demand is, and has been, weaker than normal and because there has been such uncertainty over international developments. The unexpectedly low outcomes in recent months, particularly with regard

to service prices, indicate that underlying inflationary pressures are lower than expected and that it may take longer before inflation rises. A more expansionary monetary policy is therefore necessary for inflation to rise towards 2 per cent.

An expansionary monetary policy also means that resource utilisation will rise during the forecast period, which will lead to higher wage increases and greater scope for companies to raise their prices. In addition, international goods prices are expected to rise as global economic activity improves. The krona has weakened recently, but a gradual appreciation is expected in the coming period. All in all, import prices measured in Swedish krona are expected to increase during the forecast period.

Inflationary pressures will therefore increase gradually over the period. Measured as an annual percentage change, inflation will be low in the coming year and will then increase rapidly towards the end of 2014, when the weak outcomes of recent months no longer impact the annual rate of increase. After that, CPIF inflation is expected to increase gradually to 2 per cent in 2015.

When the repo rate begins to rise again, household mortgage expenditure will increase, which will lead to CPI inflation rising faster than CPIF inflation. The rate of increase in the CPI is expected to be around 3 per cent at its highest, towards the end of 2015. After that, CPI inflation will slowly fall towards the target. During periods with large interest rate adjustments, measures of inflation that do not include the direct effects of interest rate adjustments, such as the CPIF, provide a better picture of underlying inflationary pressures. In the longer run, when the repo rate has stabilised, CPI inflation and CPIF inflation will coincide, however.

## ■ Monetary policy considerations

The Executive Board of the Riksbank has decided to cut the repo rate by 0.25 percentage points, to 0.75 per cent, and to adjust the repo-rate path downwards. The repo rate is expected to remain at 0.75 per cent for around one year. It is assessed as appropriate to slowly begin raising the repo rate at the beginning of 2015. Towards the end of the forecast period, the repo rate will be 2.6 per cent.

### ■ More tangible improvement next year

The recovery in global economic activity is continuing in line with the assessment made in October, but inflationary pressures abroad are lower than expected. An expansionary monetary policy supports the recovery and several large central banks have communicated that their policy rates will remain low for a long time to come.

After just over a year of weak growth, prospects for the Swedish economy are brightening. The labour market has improved and confidence in the Swedish household and corporate sectors has continued to rise. Together with a gradual increase in demand from abroad, this means that growth will pick up next year. The demand for labour should therefore increase further and unemployment should fall more tangibly.

In Sweden, too, inflationary pressures are lower than expected. Compared with the most recent assessment in October, inflation is now expected to be much lower during the coming year. Resource utilisation will increase in the period ahead, which will lead to higher wage increases and greater scope for companies to raise their prices. CPIF will therefore rise to 2 per cent in 2015, which is roughly the same assessment as before.

All in all, the forecasts for real economic developments abroad and in Sweden are roughly the same as in the October Monetary Policy Report. However, inflationary pressures are expected to be lower, particularly in the coming year, both in Sweden and abroad.

### ■ Repo rate cut to contribute to higher inflation

Given the unexpectedly low inflation and that inflationary pressures are expected to be lower in the coming period, the repo rate is being cut to 0.75 per cent. The repo rate is expected to remain at this level for around a year. In this way, monetary policy will contribute to CPIF inflation rising in 2015 towards 2 per cent at roughly the same rate as in the forecast made in October. It is assessed as appropriate to slowly begin raising the repo rate at the beginning of 2015. The recovery is then expected to be on firmer ground and inflation is expected to be on the way up. At the end of the forecast period, the repo rate will be 2.6 per cent. The forecast for the repo rate, both nominal and real, is lower than in the Monetary Policy Report in October.

The monetary policy considerations have for some time concerned balancing how quickly inflation will approach the target with a lower interest rate against the increased risks linked to households' high indebtedness. Inflation has been low for a long time, and the unexpectedly low outcomes in recent months regarding in particular service prices imply that it may take longer for inflation to rise. Without a more expansionary monetary policy, there is a risk that inflation would not reach 2 per cent in the coming years, and there is thus good reason to cut the repo rate by 0.25 percentage points and to adjust the repo-rate path downwards. At the same time, households' high indebtedness remains a risk to sustainable long-run development.



A repo-rate cut can contribute to a deterioration in the risk outlook for household indebtedness. It is possible that a particularly difficult situation could arise if households' expectations of future mortgage rates are too much affected by the current interest rates. Surveys show that the households' expectations of mortgage rates five years ahead are lower than is compatible with the Riksbank's assumptions regarding the repo rate in the long term. Low mortgage rate expectations could lead to a stronger upward trend in both housing prices and debts. If households were to reduce their debts quickly, there is a risk that unemployment would rise sharply and that long-term difficulties in stabilising inflation around the inflation target might arise.

The Riksbank assumes that the banks' risk-weight floor for Swedish mortgages will be raised from 15 to 25 per cent, in line with the intentions communicated by Finansinspektionen. This measure should increase the resilience of the financial system in the long run. It is also assessed to contribute to dampening household debt to some extent. However, the effects of this measure on indebtedness are difficult to judge. If macroprudential policy were to lead to a decline in the risks linked to household indebtedness, this would ease the monetary policy considerations associated with these risks. However, several policy areas will probably need to cooperate to manage the risks linked to household debt, particularly if housing prices and debt increase rapidly. The Riksbank will therefore, as before, monitor and analyse risks and resilience in the financial system and ascertain how these affect general economic development and thereby monetary policy.

#### ■ Uncertain economic outlook and inflation prospects

Developments abroad, particularly in the euro area, and the demand for Swedish exports remain an important source of uncertainty in the forecast. The prospects for the euro area have improved somewhat, but developments in industrial production, for instance, are still weak. A lot of work remains to be done to rectify the structural problems. If the situation in the euro area were to worsen again or if the recovery were to be faster than forecast, this would have consequences for developments in Sweden.

The fact that inflation in Sweden has been low for a long time, and lower than expected in recent months, also entails uncertainty for the forecast. In addition to economic activity, inflation in Sweden is also affected by developments in the exchange rate and in companies' domestic costs, as well as how quickly companies can pass on their cost increases to consumer prices. It is difficult to assess exactly how these factors affect developments in inflation and one cannot rule out the possibility that inflation will remain low for a longer period of time or that it will rise faster than expected when it actually begins to rise. This would affect the monetary policy stance.

## ■ New information since the October Monetary Policy Report

### Financial markets

- The major central banks' communication on future monetary policy has continued to play a leading role on the financial markets. Expectations that interest rates will be low for a long time to come have boosted prices for assets that carry a higher risk, such as shares and various forms of credit. All in all, the expectations of a more imminent tapering of the Federal Reserve's asset purchases have given rise to much milder reactions on the financial markets than when expectations of tapering arose earlier this year. Weak growth and low inflation outcomes in the euro area have led to increasing expectations that the ECB will take unconventional measures.
- Relatively strong economic statistics from the United States recently have strengthened expectations of a more imminent tapering of the Federal Reserve's asset purchases, which has contributed to an increase in US and European government bond yields at longer maturities. European bond yields were held back in November, however, not least as a reaction to the ECB's unexpected decision to cut its policy rate. Longer-term UK bond yields have risen in line with those in the United States following strong indicators from the United Kingdom.
- Swedish government bond yields at longer maturities remain largely unchanged since the October Monetary Policy Report. On the other hand, shorter-term Swedish bond yields have fallen. In particular, the unexpectedly low inflation outcome for October led to strong reactions on the fixed-income markets. The fact that government bond yields continue to be low has led to increased interest in Swedish mortgage bonds, which has helped to reduce the banks' borrowing costs. The fixed mortgage rates offered to households have thus also fallen since October.
- Household expectations of the future level of variable mortgage rates have fallen. The variable mortgage rate two years ahead is expected to be 3.5 per cent according to the Consumer Tendency Survey of the National Institute of Economic Research. Previous expectations were at 3.6 per cent.
- Total lending to households has continued to increase and reached 4.9 per cent in October, as an annual percentage change, according to Statistics Sweden's financial-market statistics. It is above all borrowing with tenant-owned apartments as collateral that has increased; in October the increase was 8.3 per cent. Outcomes show that the prices of tenant-owned apartments have continued to increase more rapidly than the prices of detached houses in recent months, at 11 and 6 per cent respectively compared to a year ago.
- Companies perceived funding conditions to be marginally better in November than in October, according to the survey of the National Institute of Economic Research. Corporate borrowing costs have fallen, as have those of the households. Historically, the rate of corporate borrowing from banks is at a low level. According to figures from Statistics Sweden the lending rate was 1.4 per cent in October, as an annual percentage change. However, large companies are borrowing extensively on the securities market. Borrowing with property as collateral is now growing more rapidly among the companies.

- In August, the government proposed that Finansinspektionen should be the authority with main responsibility for the macroprudential-policy instruments in Sweden. Macroprudential policy aims to increase the resilience of the financial system and to prevent the build-up of financial imbalances in the economy. The Riksbank assumes that the risk-weight floor for Swedish mortgages will be raised from 15 to 25 per cent in line with the intentions communicated by Finansinspektionen.
- The Swedish krona has weakened since October as short-term interest rates have fallen. The krona has been highly affected by the same factors as Swedish forward rates. The krona is now being traded at over SEK 9.00 against the euro, which is close to the average of 9.11 in the period 2000-2007. The US dollar has strengthened against several major currencies recently as a result of improved growth prospects. In nominal KIX terms, the krona has weakened by around 2 per cent since the end of October.

## International situation

- The recovery is continuing abroad, but has made more progress in some parts of the world than others. Since the Monetary Policy Report was published in October, GDP outcomes have generally been in line with the Riksbank's forecasts, while confidence indicators suggest a continued improvement in the period ahead. However, inflation has been lower than expected in several countries.
- Developments in the euro area indicate that the improvement will continue to be slow. GDP growth was 0.3 per cent in the third quarter, calculated as an annual rate, which was the second consecutive quarter with positive growth. In Germany, which is of major importance to Swedish exports, GDP growth in the third quarter was above the average for the euro area as a whole, while it was lower in France and Italy. Indicators for the early part of the fourth quarter have been mixed. Figures for industrial production and the retail trade fell for the second consecutive month in October, but strong confidence indicators suggest that activity will improve in the period ahead. The European Commission's survey indicator continued to rise in November, as did the purchasing managers' index for the manufacturing industry. Unemployment in the region fell somewhat to 12.1 per cent in October. According to a preliminary estimate, inflation was 0.9 per cent in November after falling more than expected to 0.7 per cent in October. In November, the ECB cut the refi rate by 0.25 percentage points to 0.25 per cent, after which it was left unchanged in December.
- In the United States, recent statistics indicate on the whole that the economy is continuing to improve. In the short term, there is also less uncertainty about fiscal policy as the House of Representatives has approved a proposed budget for the next two budget years. However, more detailed decisions are needed at the beginning of 2014. GDP increased by 3.6 per cent in the third quarter, calculated as an annual rate, which was a higher figure than expected. Household consumption was strong in October. A stronger labour market, rising share prices and better credit conditions indicate that consumption will continue to grow at a good rate. There are also signs that household incomes are increasing more rapidly than previously. At the same time, rising housing prices and a relatively high level of confidence in the construction sector indicate that the housing market is gradually recovering. The inflation rate fell in October, in part due

to lower energy prices. CPI inflation reached 1.0 per cent. When adjusted for energy and food prices, inflation was 1.7 per cent.

- Developments on other export markets of importance to Sweden have been roughly in line with expectations. Activity has improved in the United Kingdom; GDP increased by 3.2 per cent in the third quarter, calculated as an annual rate. Industrial production increased somewhat in October and the purchasing managers' indexes in the manufacturing sector and the service sector both remained well above 50, which indicates continued growth in the fourth quarter. CPI inflation has fallen but still remains above the inflation target of 2 per cent. In December, the Bank of England left its policy rate unchanged at 0.50 per cent. In Denmark, growth was subdued and GDP increased by 1.4 per cent in the third quarter, calculated as an annual rate, but indicators suggest that activity will improve in the period ahead. Industrial production increased in October, confidence in the manufacturing industry improved in November and household confidence remains at a relatively high level. CPI inflation is low and was at 0.5 per cent in November. In Norway, GDP grew by 1.9 per cent in the third quarter, calculated as an annual rate. However, the indications are that growth will decline towards the end of the year. In addition, both industrial production and retail sales fell in October. Housing prices have fallen in Norway in recent months after rising since the beginning of 2009. CPI inflation increased in November and is now in line with the target of 2.5 per cent. In December, Norges Bank left its policy rate unchanged but moved the time for the first policy rate increase forward by approximately one year against the background of the lower forecasts for growth and inflation.
- In Japan, growth has slowed down somewhat and GDP increased by 1.1 per cent in the third quarter, calculated as an annual rate. Indicators for the beginning of the fourth quarter show an improvement in activity in the manufacturing industry, while household demand has declined. In China, GDP was 7.8 per cent higher in the third quarter of 2013 than in the corresponding quarter in 2012. In October, CPI inflation rose to 1.1 per cent in Japan, and in November it fell to 3.0 per cent in China. Several emerging economies suffered capital outflows and thus weaker currencies when expectations of a tapering of asset purchases in the United States increased earlier this year. These currencies strengthened somewhat in October but have weakened again since then.

## GDP in Sweden

- Swedish GDP increased by 0.3 per cent in the third quarter of 2013, calculated as an annual rate, which was lower than the forecast in the October Monetary Policy Report. However, the figure for growth in the first half of the year has been revised upwards somewhat, which means that the level of GDP was in line with the previous assessment. Compared to the second quarter, household consumption increased more slowly than forecast, and the development of both exports and imports was weaker than expected. However, investment was stronger than in the assessment made in October. Nevertheless, investment in stocks fell unexpectedly and made a negative contribution to GDP growth. Growth in the last quarter of the year is now expected to be higher than the assessment in the Monetary Policy Report. An important reason for this is that the contribution to GDP from the build up of stocks is expected to be relatively large following the stock reductions made in the third quarter.

- The Economic Tendency Survey of the National Institute of Economic Research has risen in recent months and reached 104.1 in November, which is approximately four units above the historical average. All of the confidence indicators except those for the private service sector were positive in November. The same improvement was also evident in the purchasing managers' indexes for the manufacturing and service sectors in November. All-in-all, the indicators are now higher than their historical averages and thus suggest that GDP will grow more rapidly in the period ahead. At the same time, the production index for the business sector fell in October. Production increased slightly in the service sector, while there was a tangible fall in the manufacturing sector.
- Household consumption increased by 1.3 per cent in the third quarter, calculated as an annual rate, which was less than forecast in October. The volume of sales in the retail sector was unchanged in October. However, household confidence has increased recently and the aggregated confidence indicator of the National Institute of Economic Research is above its historical average. This means that consumption is expected to increase somewhat more rapidly in the quarters immediately ahead.
- Investment increased by 5.0 per cent in the third quarter compared to the preceding quarters, calculated as an annual rate, which was higher than the assessment in the October Monetary Policy Report. The main explanation for this is the continued high growth in housing investment. In the business sector, investment was subdued. However, capacity utilisation increased during the third quarter and the investment survey for October indicates that corporate investment will increase next year. The companies have destocked and this has had a negative effect on GDP growth over the two most recent quarters. Moderate restocking is expected in the quarters ahead.
- Exports fell by just over 3 per cent during the third quarter, calculated as an annual rate. This was the fifth consecutive quarter in which exports declined. Exports were thus weaker than assessed in October. According to the statistics on foreign trade, goods exports also declined somewhat in October compared to September, and leading indicators such as new export orders indicate that the development of exports will continue to be weak in the period immediately ahead. Imports were also weaker than assessed in October and fell for the seventh consecutive quarter. The reduction compared with the previous quarters was 4.6 per cent, calculated as an annual rate. According to the statistics on foreign trade, the level of goods imports was unchanged in October compared with September.
- Public consumption expenditure increased by 0.5 per cent in the third quarter, calculated as an annual rate, which was somewhat lower than the assessment in the October Monetary Policy Report. Expenditure increased in both the central- and local-government sectors.

## Labour market

- Since the Monetary Policy Report was published in October, the Swedish labour market has been somewhat stronger than the Riksbank's assessment. Unemployment has developed roughly as expected, but both employment and the labour force have increased more than expected. In November, seasonally-adjusted unemployment was 8.0 per cent.

- Indicators of the demand for labour continue to suggest that the labour market is stable. In recent months, the number of redundancy notices has been lower than in the corresponding period in 2012 and is close to the average since 1998. This indicates that the companies have a more positive outlook, which is also reflected in the Business Tendency Survey where companies in the business sector as a whole report that staff cuts are expected to cease at the end of 2013. The recruitment rate also increased somewhat in the third quarter. According to Statistics Sweden, the number of vacant jobs has fallen somewhat while the number of job vacancies reported to the Swedish Employment Service has remained more or less unchanged at a relatively high level for the last two years.
- All-in-all, employment is expected to continue to increase in late 2013 and early 2014. Despite this, the assessment is that there will be only a marginal reduction in unemployment in the period immediately ahead as the number of those in the labour force is also expected to continue to increase. Compared to the previous forecast, employment and the labour force are expected to increase more rapidly, while the forecast for unemployment remains unchanged.
- According to the National Accounts for the third quarter of 2013, the seasonally-adjusted number of hours worked was more or less unchanged compared to the second quarter of the year, which was in line with the forecast in the October Monetary Policy Report. Monthly outcomes and indicators suggest that the number of hours worked will increase somewhat more rapidly over the next six months compared to the assessment in October.

## Cost pressures and inflation

- The National Mediation Office's short-term wage statistics indicate that wages rose by an average of 2.1 per cent, calculated as an annual percentage change, during the first nine months of this year. The preliminary outcomes have been historically low but it is expected that they will be revised upwards when payments of recently-agreed wage increases enter the statistics. For 2013 as a whole, the assessment is that wages throughout the economy will increase by 2.5 per cent, and somewhat above this level in the first quarter of 2014. Compared to the most recent assessment, wages will increase somewhat more slowly.
- According to the National Accounts, labour costs per hours worked increased by just over 2 per cent in the economy as a whole, calculated as an annual percentage change, in the third quarter of this year. Labour productivity remained low, which was one of the factors behind unit labour costs increasing by approximately 2.7 per cent in the same quarter. At the same time, the rate of increase was revised downwards during the first six months of 2013. It is now assessed that unit labour costs will increase by approximately 2 per cent this year, as an annual percentage change, which is a downward revision compared with the assessment in October.
- Household expectations of inflation one year ahead fell marginally from 1.5 per cent in October to 1.4 per cent in November according to the survey of the National Institute of Economic Research. The latest Prospera survey, which was conducted in December, revealed minor changes in the money market participants' inflation expectations.

Inflation expectations one, two and five years ahead fell somewhat and were at 1.0 per cent, 1.6 per cent and 1.8 per cent respectively.

- Since the Monetary Policy Report, the inflation outcomes for October and November have been published. In October, inflation was significantly lower than expected and was still low in November. Both the CPI and the CPIF increased marginally to 0.1 per cent and 0.7 per cent respectively, calculated as an annual rate, compared to -0.1 per cent and 0.6 per cent in October.
- It was above all lower prices for services and food that led to the inflation rate being lower than expected in October. One explanation of the unexpectedly low food prices may be that it is only now that the reported producer-price reductions are affecting consumer prices. Global food commodity prices have fallen throughout the year but have not previously contributed to lower consumer prices. The rate of increase in service prices slowed across the board in October and is lower than the historical average. The rate of increase in service prices will thus continue to increase at a much slower pace than unit labour costs.
- In the months immediately ahead, CPIF inflation is expected to amount to just over 0.5 per cent, measured as an annual percentage change, which is well below the previous assessment. CPI inflation will also remain low in the period immediately ahead for the same reasons. The assessment is that household mortgage expenditure will continue to fall over the next 12 months, which will further dampen CPI inflation.

## ■ Tables

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

**Table 1. Repo rate forecast**

Per cent, quarterly averages

	Q3 2013	Q4 2013	Q4 2014	Q4 2015	Q4 2016
Repo rate	1.0	1.0 (1.0)	0.7 (1.2)	1.9 (2.2)	2.6 (2.9)

Source: The Riksbank

**Table 2. Inflation**

Annual percentage change, annual average

	2012	2013	2014	2015	2016
CPI	0.9	-0.1 (0.0)	0.6 (1.2)	2.5 (2.7)	3.0 (2.9)
CPIF	1.0	0.8 (0.9)	1.0 (1.3)	1.8 (1.9)	2.0 (2.0)
CPIF excl. energy	1.0	1.1 (1.2)	1.1 (1.5)	2.0 (2.0)	2.1 (2.1)
HICP	0.9	0.4 (0.5)	0.9 (1.3)	1.8 (1.9)	2.0 (2.0)

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

	2012	2013	2014	2015	2016
Repo rate	1.5	1.0 (1.0)	0.7 (1.0)	1.4 (1.8)	2.4 (2.7)
10-year rate	1.6	2.1 (2.2)	2.6 (3.0)	3.4 (3.7)	4.0 (4.2)
Exchange rate, KIX, 18 Nov. 1992 = 100	106.1	103.1 (102.7)	104.9 (102.3)	102.4 (101.5)	101.6 (101.2)
General government net lending*	-0.4	-1.4 (-1.3)	-1.5 (-1.1)	-0.5 (-0.2)	0.3 (0.6)

\* Per cent of GDP

Sources: Statistics Sweden and the Riksbank

**Table 4. International conditions**

Annual percentage change, unless otherwise stated

GDP	PPP-weights	KIX-weights	2012	2013	2014	2015	2016
Euro area	0.14	0.47	-0.6	-0.4 (-0.4)	1.1 (1.3)	1.9 (1.9)	2.1 (2.1)
USA	0.19	0.09	2.8	1.8 (1.6)	3.0 (3.0)	3.5 (3.5)	3.4 (3.3)
Japan	0.06	0.03	1.9	1.6 (1.9)	1.8 (2.1)	1.1 (1.1)	1.2 (1.2)
China	0.15	0.08	7.8	7.7 (7.6)	7.4 (7.3)	7.0 (7.0)	7.0 (7.0)
KIX-weighted	0.79	1.00	1.0	1.1 (1.0)	2.4 (2.3)	2.8 (2.8)	3.0 (3.0)
World (PPP-weighted)	1.00	-	3.2	3.0 (2.9)	3.8 (3.7)	4.0 (4.0)	4.1 (4.1)

Note. Calendar-adjusted growth rates. The PPP-weights refer to the global purchasing-power adjusted GDP-weights for 2012, according to the IMF. The National Institute of Economic Research updates the weights for the KIX krona index at the start of every year with a time lag of three years. The figures in the table are based on the new KIX weights for 2010 that are used for 2013, and on an assumption that the weights will develop according to the trend of the past five years in the coming forecast year.

CPI	2012	2013	2014	2015	2016
Euro area (HICP)	2.5	1.3 (1.5)	1.1 (1.5)	1.5 (1.6)	1.7 (1.7)
USA	2.1	1.5 (1.5)	1.6 (1.8)	2.1 (2.1)	2.4 (2.4)
Japan	0.0	0.3 (0.3)	3.2 (3.2)	2.0 (2.0)	1.7 (1.7)
KIX-weighted	2.6	1.9 (2.0)	1.9 (2.2)	2.2 (2.2)	2.3 (2.3)

	2012	2013	2014	2015	2016
Policy rates in the rest of the world, per cent	0.4	0.2 (0.2)	0.2 (0.2)	0.4 (0.5)	1.0 (1.0)
Crude oil price, USD/barrel Brent	111.8	108.6 (108.8)	107.6 (105.0)	102.1 (99.1)	96.8 (94.5)
Swedish export market	1.6	1.3 (0.9)	5.4 (5.1)	6.5 (6.5)	7.0 (7.0)

Note. The export market aims to measure demand for imports in the countries to which Sweden exports. This is calculated by aggregating the imports of 32 countries and covers around 85 per cent of the Swedish export market. The weights comprise the respective country's share of Swedish export of goods. Policy rates in the rest of the world refer to a weighted average of USA, the euro area, Norway and the United Kingdom.

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



**Table 5. GDP by expenditure**

Annual percentage change, unless otherwise stated

	2012	2013	2014	2015	2016
Private consumption	1.6	1.8 (2.0)	2.7 (3.2)	3.5 (3.3)	2.6 (2.5)
Public consumption	0.3	1.2 (1.0)	0.8 (0.9)	1.2 (1.2)	1.1 (1.1)
Gross fixed capital formation	3.3	-1.2 (-3.2)	4.3 (4.6)	7.5 (7.5)	5.4 (5.4)
Inventory investment*	-1.2	-0.1 (0.4)	0.3 (-0.1)	0.0 (0.0)	0.0 (0.0)
Exports	0.7	-1.7 (-1.4)	2.3 (4.0)	6.6 (6.5)	6.7 (6.7)
Imports	-0.6	-2.2 (-0.9)	3.0 (4.4)	6.9 (6.9)	7.2 (7.2)
GDP	0.9	0.9 (0.7)	2.5 (2.6)	3.7 (3.5)	2.8 (2.7)
GDP, calendar-adjusted	1.3	0.9 (0.8)	2.6 (2.7)	3.5 (3.3)	2.6 (2.5)
Final figure for domestic demand*	1.5	0.9 (0.6)	2.3 (2.6)	3.5 (3.3)	2.6 (2.5)
Net exports*	0.6	0.1 (-0.3)	-0.2 (0.0)	0.3 (0.2)	0.2 (0.2)
Current account (NA), per cent of GDP	6.5	6.3 (5.7)	5.9 (5.5)	5.8 (5.3)	5.7 (5.2)

\*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

	2012	2013	2014	2015	2016
Population, aged 16-64	0.6	0.6 (0.6)	0.7 (0.7)	0.7 (0.7)	0.7 (0.7)
Potential hours worked	0.5	0.5 (0.5)	0.6 (0.6)	0.6 (0.6)	0.6 (0.6)
GDP, calendar-adjusted	1.3	0.9 (0.8)	2.6 (2.7)	3.5 (3.3)	2.6 (2.5)
Number of hours worked, calendar-adjusted	0.6	0.5 (0.5)	1.4 (1.3)	1.4 (1.3)	1.0 (1.0)
Employed, aged 15-74	0.6	1.1 (1.0)	1.1 (0.9)	1.0 (1.1)	1.0 (0.9)
Labour force, aged 15-74	0.8	1.1 (1.0)	0.8 (0.7)	0.3 (0.5)	0.3 (0.3)
Unemployment, aged 15-74 *	8.0	8.0 (8.0)	7.8 (7.8)	7.1 (7.2)	6.5 (6.6)

\* Per cent of the labour force

Note. Potential hours refer to 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 labour costs for the economy as a whole**

Annual percentage change, calendar-adjusted data unless otherwise stated

	2012	2013	2014	2015	2016
Hourly wage, NMO	3.0	2.5 (2.6)	2.7 (2.8)	3.2 (3.2)	3.4 (3.4)
Hourly wage, NA	3.1	2.6 (2.7)	2.9 (3.0)	3.4 (3.4)	3.7 (3.7)
Employers' contribution*	0.3	-0.1 (-0.1)	0.0 (0.0)	0.0 (0.0)	0.0 (0.0)
Hourly labour cost, NA	3.4	2.5 (2.5)	2.9 (3.0)	3.4 (3.4)	3.7 (3.7)
Productivity	0.6	0.4 (0.2)	1.2 (1.4)	2.0 (2.0)	1.6 (1.5)
Unit labour cost	2.7	2.1 (2.3)	1.6 (1.6)	1.3 (1.4)	2.1 (2.2)

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

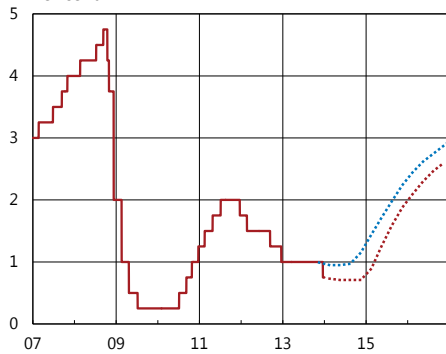
Note. NMO is the National Mediation Office's short-term wage statistics and NA is the National Accounts. Labour cost per hour is defined as the sum of actual wages, social-security charges and wage taxes divided by the seasonally adjusted total number of hours worked. Unit labour cost is defined as labour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



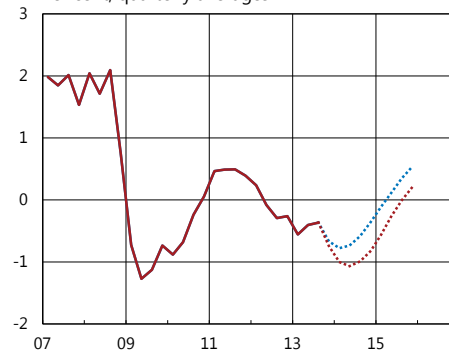
— December  
— October

Note. Outcome data are daily rates and forecasts are quarterly averages.

Source: The Riksbank

**Figure 6. Real repo rate**

Per cent, quarterly averages



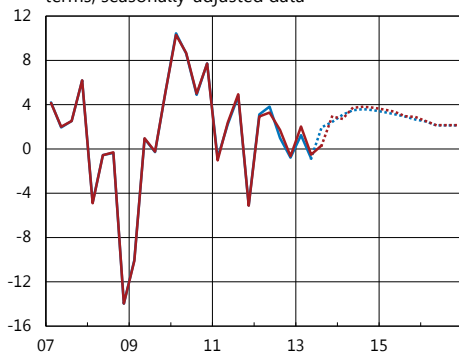
— December  
— October

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

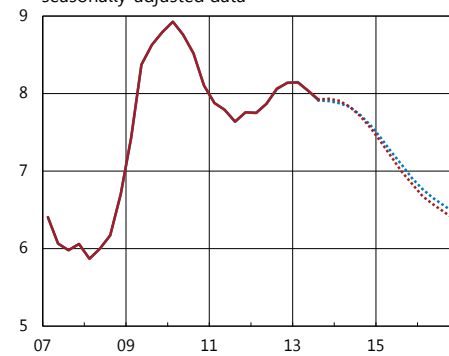


— December  
— October

Sources: Statistics Sweden and the Riksbank

**Figure 8. Unemployment**

Per cent of the labour force, aged 15-74, seasonally-adjusted data

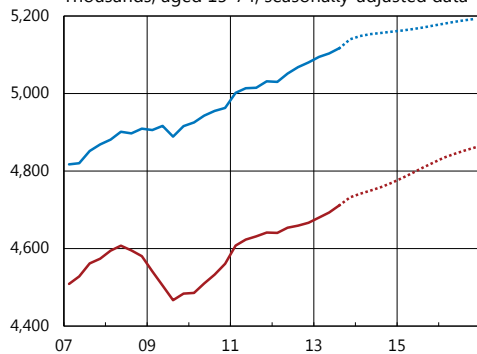


— December  
— October

Sources: Statistics Sweden and the Riksbank

**Figure 9. Labour force and number of employed**

Thousands, aged 15-74, seasonally-adjusted data



— Employed  
— Labour force

Sources: Statistics Sweden and the Riksbank

**Figure 10. CPI**

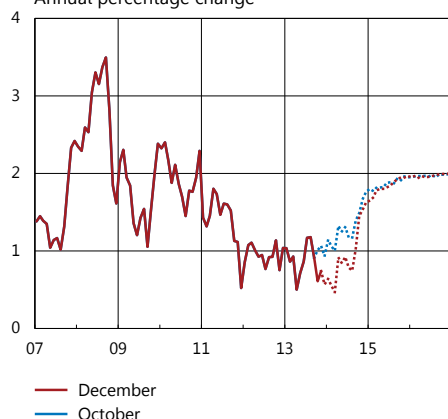
Annual percentage change



— December  
— October

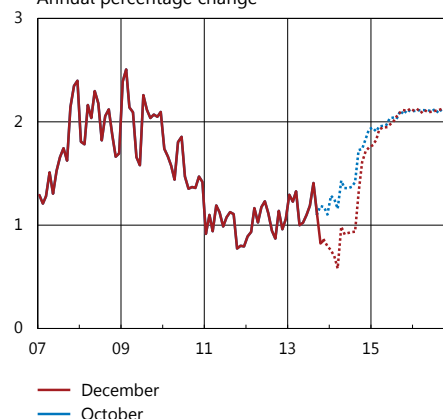
Sources: Statistics Sweden and the Riksbank

**Figure 11. CPIF**  
Annual percentage change



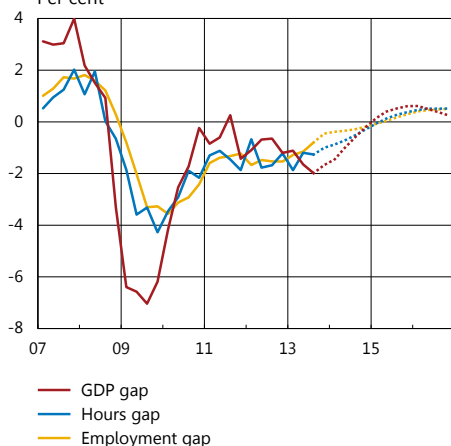
Note. The CPIF is the CPI with a fixed mortgage rate.  
Sources: Statistics Sweden and the Riksbank

**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

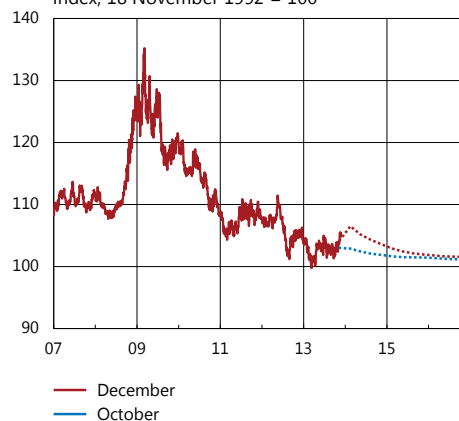
**Figure 13. GDP gap, hours gap and employment gap**  
Per cent



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

Sources: Statistics Sweden and the Riksbank

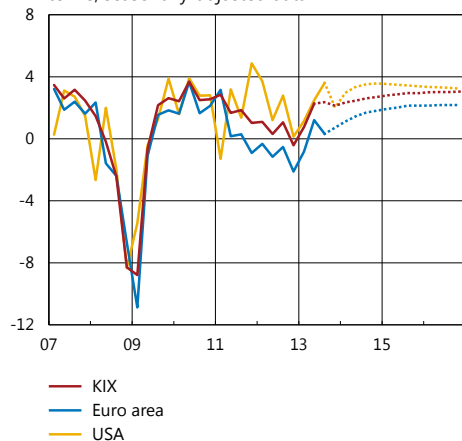
**Figure 14. KIX-weighted nominal exchange rate**  
Index, 18 November 1992 = 100



Note. Outcomes are daily rates and forecasts refer to quarterly averages. KIX is an aggregate of countries that are important for Sweden's international transactions.

Source: The Riksbank

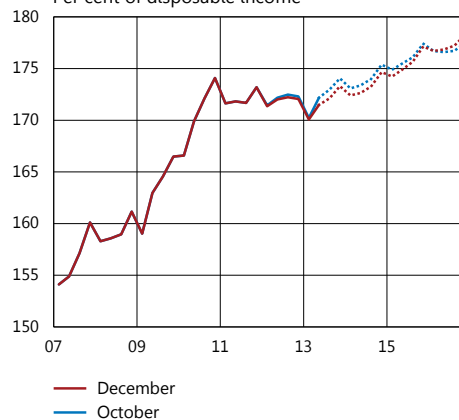
**Figure 15. GDP in different regions and countries**  
Quarterly changes in per cent calculated in annualised terms, seasonally-adjusted data



Note. KIX is an aggregate of countries that are important for Sweden's international transactions.

Sources: Bureau of Economic Analysis, Eurostat, national sources and the Riksbank

**Figure 16. Household debt**  
Per cent of disposable income



Sources: Statistics Sweden and the Riksbank