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Monetary Policy Update
December 2014

The economic recovery abroad is continuing. However, there are substantial differences in growth; in the United States and the United Kingdom growth is good, while developments in the euro area remain subdued. The oil price has fallen and is now at the lowest level since 2010. The low oil price is expected to give some positive stimulation to growth in many countries. At the same time, the falling oil price has contributed to the forecast for global inflationary pressures being revised down.

The parliamentary situation in Sweden is uncertain. However, the financial markets have been stable and not marked by uncertainty to the same extent as in October. Economic activity in Sweden is continuing to improve, but inflation is too low and long-term inflation expectations have fallen. Economic development in Sweden has been in line with the Riksbank's forecast in October and GDP and employment are expected to continue rising in line with this. However, inflation is expected to be somewhat lower for a time, primarily due to the falling oil price. The very expansionary monetary policy will contribute to demand in the economy gradually increasing and resource utilisation rising. CPIF inflation will rise gradually and attain 2 per cent in the middle of 2016.

Monetary policy now needs to be even more expansionary for inflation to rise towards the target sufficiently quickly and to reduce the risk of long-term inflation expectations continuing to fall. The repo rate therefore needs to remain at zero per cent for slightly longer. An appropriate time to begin raising the repo rate is the second half of 2016. CPIF inflation will then be close to 2 per cent. If monetary policy needed to become even more expansionary, it would mainly entail continuing to postpone a first repo-rate increase. The Riksbank is also preparing further measures that can be used to make monetary policy even more expansionary. Such measures, if necessary, could be presented with effect from the next monetary policy meeting.

Figure 1. Repo rate with uncertainty bands
Per cent

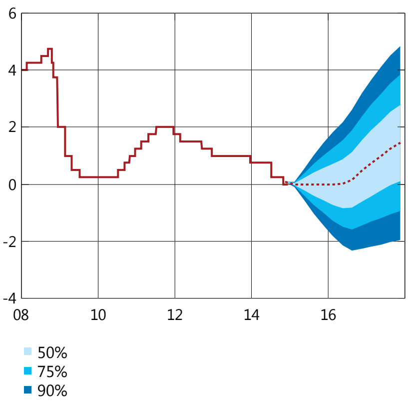


Figure 2. GDP with uncertainty bands
Annual percentage change, seasonally-adjusted data

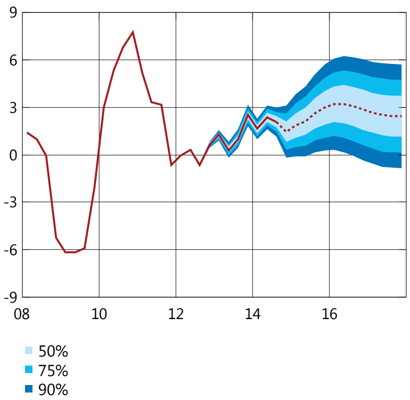


Figure 3. CPI with uncertainty bands
Annual percentage change

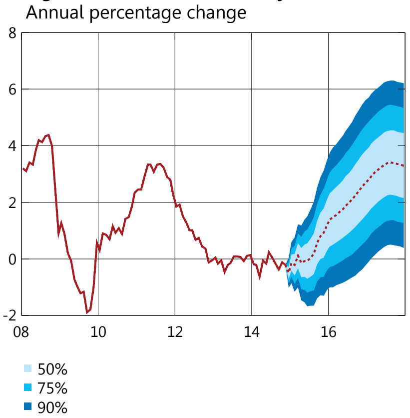
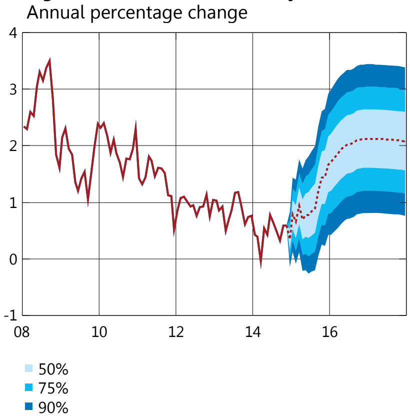


Figure 4. CPIF with uncertainty bands
Annual percentage change



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 Executive Board decided to adopt the Monetary Policy Update at its meeting on 15 December 2014. 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 October and the forecast updates made since then. The forecasts are based on the decision to hold the repo rate unchanged at zero per cent and that slow increases in the repo rate begins during the second half of 2016.

■ Global economic recovery continuing

The economic outlook remains largely the same as in October. GDP growth abroad is expected to continue to rise gradually during the forecast period. This development is supported by the central banks' expansionary monetary policy and by budget deficits being expected to decline more slowly in the coming period. The oil price has fallen by a further 25 per cent or so since the Monetary Policy Report was published in October. All in all, the oil price has therefore fallen by more than 40 per cent since last summer. The decline since October is thought to be primarily driven by supply factors. The steady increase in the production of shale-oil in the United States has had a greater impact on the price of oil, as demand for oil has slowed down. At the same time, the OPEC countries have tried to preserve their market shares by cutting their prices without reducing production. The oil price is expected to stabilise during the forecast period but to remain lower than the assessment in October. The lower oil price is expected to give some positive stimulation to growth in the United States and the euro area. With regard to the countries with the greatest significance for the Swedish economy as a whole, however, the positive effects are counteracted by a weaker development in commodity-producing countries like China and Japan. KIX-weighted GDP is therefore unchanged in relation to the forecast in October. KIX-GDP is expected, as before, to gradually increase from just below 2 per cent in 2014 to 2.6 per cent in 2017.

Inflation abroad is still low. The continued fall in the oil price means that the upturn in inflation during the forecast period will be weaker than was assumed in October. This applies in particular during 2015, when the KIX-weighted inflation rate is revised down 0.5 percentage points to 1.5 per cent. Towards the end of the forecast period, KIX inflation is expected to be just over 2 per cent. Monetary policy abroad is expected to remain expansionary.

■ Continued improvement in the US economy

The US economy is continuing to improve on a broad front and domestic demand is strong. Company profits are high and households are benefiting from an improved labour market, low interest rates, rising stock markets and continued improvement in credit terms. The forecast assumes that this will contribute to a continued increase in consumption and investment. The federal budget deficit has declined significantly in recent years. Going forward, the deficit is expected to decline more slowly. The low oil price will increase scope for consumption and provide positive stimulation to growth. All in all, GDP growth is expected to increase from just over 2 per cent this year to around 3.5 per cent next year. After that, growth will gradually slow down and approach 2.5 per cent in 2017.

In October, US CPI inflation rose by 1.7 per cent, calculated as an annual rate. Over the coming quarters, inflation is expected to fall substantially as a result of lower energy prices. However, the inflation is expected to rise to more than 2 per cent during 2016 as the spare capacity in the economy is put to use. Monetary policy is expected to remain expansionary throughout the forecast period.

■ Slow recovery in the euro area

GDP growth in the euro area was somewhat stronger than expected during the third quarter. However, the growth rate is still low and confidence indicators for both households and companies once again swung downwards in November, after a temporary upturn in October. The results from the ECB's Asset Quality Reviews and stress tests of banks' balance sheets were published at the end of October. They had a positive reception from the market and are now assessed to be an important factor in strengthening confidence in the banking system.

For some time now, there have been signs that the credit market has stabilised. The fall in lending to non-financial companies has slowed down, which makes it easier for the expansionary monetary policy to have an impact in the coming period. Growth will also benefit from rising demand in the rest of the world, a lower oil price, weaker exchange rate and a slower reduction in the budget deficit going forward. However, the lower oil price is expected to have relatively minor effects on growth, as households are weighed down by continuing debt adjustments. From a historical perspective, the recovery is expected to be slow and there is still a need for structural reforms to strengthen competitiveness.

The fact that the economy is now showing somewhat stronger figures than expected, together with the fall in the oil price, has led to the forecast for GDP growth in the euro area being revised up for this year and next year. Growth this year is expected to be 0.9 per cent, and then gradually increase to almost 2 per cent in 2017. The labour market in the euro area will improve gradually but resource utilisation is expected to be low during the forecast period. The large fall in the price of oil leads to a downward revision in the forecast for inflation. The weakening of the euro to some extent counteracts the effects of the oil price on inflation. Inflation, which is currently very low, is expected to rise slowly and amount to 1.5 per cent in 2017. Monetary policy is expected to remain very expansionary throughout all of the years covered by the forecast.

■ Subdued activity on important export markets

The strong growth in the United Kingdom is expected to slow down and at the end of the forecast period to be in line with the historical average. Fiscal policy is expected to tighten over the coming years. However, this will be counteracted by an expansionary monetary policy, more generous credit terms, rising global growth and a recovery in productivity that together will contribute to continued good growth in the coming years. Wages and unit labour costs are expected to rise at a faster pace as unemployment declines. This will contribute to inflation returning to 2 per cent in 2017. However, the lower oil price means that the inflation forecast is revised down somewhat, particularly during 2015.

In Norway, growth has been strong so far this year, but the oil-dependent Norwegian economy is expected to be weighed down in the coming period by the large fall in the oil price. GDP growth in the coming years is therefore expected to be weaker than was previously forecast. The large depreciation in the Norwegian krona will contribute to improving the competitiveness of the economy after a long period of high wage increases, and will mean that inflation is higher in the coming years than was assumed in October.

The Russian economy is weak. The negative effects of the EU sanctions, Russia's counter-sanctions and the fall in the oil price further reinforce the growth problems linked to reduced production capacity. The economy is expected to go into recession next year.

In China, a slow transition of the economy is taking place, where growth is becoming less dependent on investment and exports and more oriented towards private consumption. This is expected to hold back GDP growth in the coming years. GDP is expected to slow down from around 7.5 per cent this year to around 6.5 per cent in 2017. During the coming year, CPI inflation will be held back by lower food and energy prices and by a fall in property prices. However, CPI inflation is then expected to rise once again to almost 3 per cent in 2017.

Japan's GDP has fallen for the past two quarters. The large negative effects of the VAT increase in April have meant that the second planned VAT increase in October 2015 have been postponed until April 2017. This affects the future course of GDP. The forecast for GDP growth in 2014 has been revised down to 0.2 per cent as the result of a weak outcome in the third quarter. Growth is expected to be around 1 per cent in the coming two years and then to fall back to 0.5 per cent in 2017, when the postponed VAT increase is implemented. Inflation is expected to amount to around 1.5 per cent in 2015–2016 and to attain the 2 per cent that is the Japanese central bank's inflation target i 2017. Monetary policy is expected to be highly expansionary.

■ Reduced financial uncertainty and lower interest rates

Government bond rates in developed economies are still low, as growth prospects are modest and as the world's central banks are expected to hold policy rates at low levels for a long time. Lower inflation expectations will also hold back nominal interest rates.

According to market pricing, the Federal Reserve and the Bank of England are expected to begin raising their policy rates in autumn 2015, but at a slow pace. The European Central Bank (ECB) aims to expand its balance sheet in the coming years to bring up inflation towards the target (close to but below 2 per cent). At present, the market is not expecting any policy rate increase within the next three years.

The Swedish krona weakened in connection with the monetary policy decision in October, but has gradually strengthened again. However, in trade-weighted terms the krona is still somewhat weaker than prior to the monetary policy meeting in October. In terms of individual currencies, the krona has continued to weaken against the US dollar and is also weaker against the euro and sterling. The dollar appreciation has been unexpectedly large, which together with small fluctuations against the euro, indicates a somewhat slower krona appreciation in the near time, compared with the forecast in October. However, the krona is expected to gradually strengthen during the forecast period as a whole, in both nominal and real terms, as it is assessed that the real exchange rate is currently weaker than its long-term level.

■ Gradually stronger demand from abroad contributes to higher GDP growth in Sweden

GDP growth in Sweden was slower than normal in the third quarter, partly as a result of subdued consumption and exports. All in all, the confidence indicators are at normal levels, which indicates growth in line with the historical average over the coming quarters.

In recent years, exports have shown weak development, which is partly linked to a low level of investment in Sweden's most important export countries. Going forward, economic activity abroad is expected to improve gradually and demand for Swedish goods and services to increase. However, export market growth is held back by the slow recovery in the euro area. This means that Swedish export goods are expected to increase more slowly than in previous upturns. Over the past year, imports have increased more rapidly than exports and net exports have contributed negatively to GDP growth. The contribution is also expected to be close to zero in the coming years.

Household saving in relation to income has risen in recent years. As economic activity improves, consumers are expected to save less of their incomes and consumption is expected to increase more rapidly. Finansinspektionen's proposal regarding amortisation requirements is assessed as having minor effects on household consumption and saving in the coming years. This means that saving will decline somewhat less than it would otherwise have done.

Investments in housing and construction have increased rapidly, at the same time as investment in machinery has declined in recent quarters. However, Statistics Sweden's recent investment survey indicates that industrial investment will increase next year. As demand rises and capacity utilisation increases, the need for new investment will also increase. This development is supported by favourable funding terms and low interest rates. Housing investment, which is at its highest level since the crisis in the 1990s, is expected to level off and will thus not contribute to GDP growth as much as before.

GDP growth is expected to increase by 1.8 per cent this year and by 2.6 per cent next year. During 2016, growth is expected to be 3.3 per cent, and then to slow down to 2.2 per cent in 2017 when resource utilisation is normal. Compared with the forecast in October, only marginal changes have been made to the forecast for GDP growth. These are linked to the oil price, the exchange rate and the amortisation requirement.

■ Still no slowdown in household debt

Housing prices and household indebtedness have increased rapidly in recent months. Rising incomes, low interest rates and a large demand for housing in many cities is expected to mean that housing prices continue to rise in the coming years. This also contributes to households' debt and wealth increasing. Finansinspektionen's proposal regarding amortisation requirements is only expected to have a marginally dampening effect on the rate of increase in housing prices and household indebtedness during the forecast period.

Debt as a share of disposable income, what is known as the debt ratio, has risen over the past year, after remaining relatively unchanged since the middle of 2010. In the years ahead, debts are expected to increase faster than incomes, and the debt ratio is therefore expected to rise to a good 187 per cent at the end of 2017. Compared with the assessment in October, the debt ratio has been revised up, mainly as a result of Statistics Sweden revising down disposable incomes.

■ Public sector saving not noticeably affected by new budget

Public sector saving for 2013 amounted to −1.4 per cent of GDP. During 2014, the deficit is expected to grow to the equivalent of 2.2 per cent of GDP. The Riksbank's forecast for public sector net lending is in turn based on announced measures and an assessment based on how fiscal policy is usually adjusted to the state of the economy and the policy objectives set by the fiscal-policy framework. The budget framework now decided on differs from the Government's budget as presented in October. The main differences are that the earlier budget included reforms amounting to SEK 25 billion, which would be primarily funded through tax increases. Instead, the budget framework adopted contains reforms to the value of around SEK 10 billion, which are funded through both increases in income and decreases in expenditure. Both the Government's budget and the one now adopted fund all of the reforms krona for krona and thus do not have any significant effects on the forecasts for general government net lending. During 2016–2017 budget reinforcements are expected to be implemented, regardless of the composition of the Government, to ensure that general government finances approach the surplus target.

■ Labour market continuing to strengthen, but major challenges lie ahead

Employment and the labour force have continued to grow and unemployment is falling gradually. The labour market is expected to be somewhat weaker at the end of 2014 and the start of 2015, compared with the assessment in October. However, the Riksbank's assessment that the labour market will continue to strengthen in the coming period still stands. The number of redundancies remains at very low levels and the number of newly-registered job vacancies with the Swedish public employment service has risen substantially over the year. Companies' employment plans as described in the National Institute of Economic Research's Business Tendency Survey also indicate a continuing increase in employment. As economic activity strengthens, the demand for labour will also increase and employment is expected to rise at a good pace. At the same time, there are major challenges as a large percentage of the unemployed are made up of groups with only a weak connection to the labour market.

Labour force participation, which has shown a rising trend in recent years, is expected to level off and fall somewhat during the forecast period. This is mainly because groups with a lower degree of participation, such as older people and those born abroad, are expected to increase as a percentage of the population. During the forecast period, the employment rate for the 15–74 age group, that is the number of those employed as a percentage of the population in this age group, is expected to remain at the current level of 66.5 per cent. Unemployment is expected to decline gradually to around 6.5 per cent, in line with the earlier forecast.

■ Resource utilisation rising slowly

The Riksbank's overall assessment is that resource utilisation in the economy is still lower than normal. This is supported by the Riksbank's indicator of resource utilisation, which contains information on labour shortages in the business sector and on capacity utilisation according to the National Institute of Economic Research's Economic Tendency Survey.

The unexpectedly strong outcome in the number of hours worked during the third quarter is largely assessed to be temporary and therefore has very little effect on the Riksbank's overall assessment. As in the forecast in October, employment is expected to be lower and unemployment to be higher than their long-run sustainable levels.

The very low interest rates, together with stronger global and domestic demand, will contribute to higher GDP and employment and to a larger number of hours being worked in the coming period. Resource utilisation will thus increase. As in the assessment made in October, resource utilisation is expected to be roughly normal during the latter part of the forecast period.

■ Rate of wage increase will rise gradually

According to the National Mediation Office's compilation, the agreed wage increases for 2015 amount to 2.3 per cent, and the Riksbank assesses that wages according to the short-term wage statistics will increase by around 3 per cent. The next major round of collective bargaining will be in 2016, when wage agreements covering almost 2.8 million employees will expire. During 2016 and 2017, wages according to the short-term wage statistics are expected to increase by around 3.5 per cent a year. Apart from the assessments of future wage agreements, developments in economic activity and on the labour market are important factors for the Riksbank's forecasts of wage developments in the period ahead.

Productivity growth in the Swedish economy is weak this year, but the assessment is that it will become stronger in the coming years. Towards the end of the forecast period, productivity is expected to grow by approximately 1.7 per cent per year, which is close to the historical average since 1994. At the same time, productivity growth is higher than it has been in recent years and will thus contribute to higher GDP growth in the forecast period. Growth in unit labour costs is expected to be somewhat lower in 2015–2016, compared with the assessment in October, and then to rise to 2.0 per cent in 2017. Unit labour costs will increase by 2.0 per cent on average during the forecast years, which is in line with the historical average since 1994.

■ Inflation is very low

Measured in terms of the CPI, inflation is negative. The very low CPI inflation rate is partly connected with household mortgage expenditure having fallen, which in turn is due to a gradually lower repo rate. However, even if one disregards the effect of falling interest expenditure, inflation is much lower than the Riksbank's target. CPIF inflation was 0.6 per cent in November, measured as an annual percentage change.

The rate of price increase in services, in particular, has continued to be significantly lower than the historical average. Another contributing factor to the low inflation is the falling energy prices.

Compared with the October Monetary Policy Report, energy prices are now expected to be lower. The oil price has fallen heavily since the summer and is expected to contribute to lower inflation in the coming years. Apart from the direct effects on petrol and diesel prices, delayed effects will also arise as the lower energy prices affect other costs and prices, such as transport prices. Electricity prices have also fallen during the autumn, mainly as a result of the mild weather. However, the forecast for electricity prices has been revised upwards somewhat, in line with the higher forward rates.

Since the Monetary Policy Report was published in October, the exchange rate forecast has been revised somewhat. The Swedish krona is now expected to strengthen somewhat later, which indicates slightly higher inflation than was previously forecast. At the same time, several factors contribute to dampening inflationary pressures. In addition to lower energy prices, rental agreement negotiations so far indicate that rents will increase less than expected in 2015. All in all, this means that CPIF inflation is expected to be slightly lower for some time. When adjusted for changes in energy prices, inflation has been somewhat higher than expected in recent months and the forecast for the coming year remains largely unchanged, compared with the October report.

Seen in a longer-term perspective, there are several explanations for the low inflation. For instance, weak demand has contributed to a slow rate of increase in international prices, there have continually been spare resources on the labour market and companies have found it difficult to pass on their cost increases to consumer prices. There are indications in the Riksbank's Business Survey that inflation has also been held back by low demand and increasing competition.

As economic activity abroad improves gradually and demand for Swedish goods and services will increase. Together with an increasingly strong domestic demand, this means that resource utilisation in the Swedish economy will gradually rise. The very expansionary monetary policy will contribute to this development. Employment is growing and unemployment is falling back. During the latter part of the forecast period, wage increases are expected to become gradually higher and there should be greater scope for companies to raise their prices. All in all, there are good conditions for inflation to rise in the coming years.

CPIF inflation rises during 2015 and amounts to 1.7 per cent in the end of the year. In line with the assessment in October, CPIF inflation attains 2 per cent until the middle of 2016. Households' mortgage interest expenditure will rise when the increases in the repo rate begin. This will in turn lead to CPI inflation increasing faster than CPIF inflation in 2016 and 2017. During periods with large interest rate adjustments, CPIF inflation, which does not include the direct effects of interest rate adjustments, provides a better picture of underlying inflationary pressures than the CPI. However, in the long run, CPI and CPIF inflation will coincide.

■ Monetary policy considerations

Compared with the Monetary Policy Report in October, the oil price has fallen markedly, the forecast for inflation in the coming year has been revised down and inflation expectations have declined somewhat. The Executive Board of the Riksbank therefore assesses that the repo rate needs to remain at zero per cent for a slightly longer period. The new repo-rate path means that increases in the repo rate will begin during the second half of 2016 and it will attain 1.45 per cent towards the end of 2017.

■ Economic activity strengthening but inflation is too low

The economic recovery abroad is continuing. However, there are substantial differences in growth; in the United States and the United Kingdom, growth is good while developments in the euro area remain subdued. The oil price has fallen and is now at the lowest level since 2010. The low oil price is expected to give some positive stimulation to growth around the world. At the same time, the falling oil price has contributed to the forecast for global inflationary pressures being revised down.

Economic activity in Sweden is continuing to improve, but inflation is too low. Since October, economic development has been in line with the Riksbank's forecast and GDP and employment are expected to continue rising in line with the earlier assessment. However, inflation is expected to be somewhat lower for a period of time, primarily due to the falling oil price. The very expansionary monetary policy will contribute to demand in the economy gradually increasing and resource utilisation rising. CPIF inflation will rise gradually and attain 2 per cent in the middle of 2016.

■ Zero repo rate until inflation is close to 2 per cent

Monetary policy needs to remain very expansionary for inflation to rise towards the target. Inflation is now expected to be somewhat lower for a period of time. In addition, inflation expectations in the longer run have fallen slightly further and are below the inflation target of 2 per cent. For inflation to rise towards the target sufficiently quickly and to reduce the risk of longer-run inflation expectations continuing to fall, monetary policy needs to become more expansionary. The Executive Board of the Riksbank therefore assesses that the repo rate needs to remain at zero per cent for a somewhat longer period than was forecast in October. The expansionary monetary policy underlines the Riksbank's aim to safeguard the role of the inflation target as nominal anchor for the price- and wage formation.

The highly-expansionary monetary policy is expected to lead to an increase in demand in Sweden in the years immediately ahead. Companies will then be able to raise their prices and in this way pass on their cost increases to consumers to a greater extent. Thus, the inflation is expected to rise. The new repo-rate path means that the repo rate will remain at zero per cent until CPIF inflation is close to 2 per cent. The assessment is that it will be appropriate to begin increasing the repo rate in the second half of 2016. CPIF inflation will then be close to 2 per cent, GDP growth will have been relatively high for just over a year and unemployment will have been falling for some time. The repo rate will then rise gradually and reach 1.45 per cent towards the end of 2017. This is a very low repo rate at a time when economic activity is good, resource utilisation is close to its normal level and CPIF inflation is in line with the inflation target.

If monetary policy needed to become even more expansionary, this would primarily entail continuing to postpone a first increase of the repo-rate. The Riksbank is also preparing further measures that can be used to make monetary policy even more expansionary. Such measures, were they necessary, could be presented with effect from the next monetary policy meeting.

■ Measures needed to dampen the risks linked to household indebtedness

The low repo rate will continue to stimulate economic activity and will also contribute to strengthening the trend with rising housing prices and household indebtedness. This means that the vulnerability of the Swedish economy increases. Finansinspektionen's proposal for an amortisation requirement is a step in the right direction, but is expected to only have marginal effects on household indebtedness. Further measures are therefore required to reduce the risks. It will be necessary to introduce such measures gradually and over a long period of time. The responsibility for this lies with other policy areas than monetary policy. Conceivable measures include tightening the cap on loan-to-value ratios, restricting the percentage of mortgages at variable interest rates, adjusting tax relief, raising the minimum levels of the banks' discretionary income calculations and extending taxation of housing. In addition, measures that increase the supply of housing and lead to a more effective housing market are necessary to achieve a lasting solution that reduces the risks associated with household indebtedness in the long term.

■ Uncertainty over economic outlook and inflation prospects

Expansionary monetary policy and rising demand in Sweden and abroad mean that inflation is expected to rise gradually over the coming years. However, it is uncertain how quickly inflation will rise, particularly given that inflation has been weaker than expected for some time. The fall in the oil price is expected to affect inflation both directly through lower energy prices and indirectly through lower prices for services and other goods. But it is uncertain how great these effects will be. Developments abroad, and then mainly in the euro area, are a further source of uncertainty. If economic activity does not recover as expected in the euro area, this will have a negative effect on the Swedish economy.

Since spring 2014, the krona exchange rate has weakened in trade-weighted terms, which has to some extent counteracted the low inflationary pressures. In the coming years, the krona is expected to strengthen again, at the same time as inflation rises. However, it is difficult to assess how quickly the exchange rate will strengthen and what effects this will have on the economy.

The recent developments in housing prices and debt are also a source of concern. Household debt as a share of disposable income, the debt ratio, will increase relatively rapidly in the forecast and has also been revised upwards somewhat in relation to the October Monetary Policy Report. A continuing upward trend in the debt ratio entails a risk that the economy will develop in a way that is not sustainable in the long run. If households were to rapidly reduce their debts for one reason or another, this could have a substantial impact on demand and unemployment. This could also give rise to persistent difficulties in stabilising inflation around the inflation target.

■ New information since the October Monetary Policy Report

Financial markets

- The uncertainty that characterised the financial markets at the beginning of October has declined, although some concern over growth still remains. Prices of shares and higher-risk bonds have risen.

- The oil price has continued to fall and the price of Brent crude was less than 65 dollars a barrel in the middle of December, a decline of more than 40 per cent since the peak level in June. The downturn since the summer is probably due to a combination of demand and supply factors, where the latter is judged to have dominated since October. The United States has steadily increased its production of shale-oil for several years now, while the OPEC countries have not expressed any willingness to limit production.

- Government bond yields are still very low in a historical perspective. In Germany and Sweden, yields on government bonds with a maturity of up to two years are negative, and government bond yields with longer maturities are at historically-low levels. In the United States, yields rose slightly in November, but are nevertheless lower than at the start of the autumn.

- The low bond yields to some extent reflect market expectations that many central banks will hold their policy rates low for a long time. Although favourable US macro statistics mean that market pricing is now indicating a somewhat less expansionary US policy-rate path, a first increase in the Fed Funds rate is nevertheless not expected until autumn 2015. In the United Kingdom, weak inflation prospects contribute to expectations of a first policy rate increase being postponed to the end of 2015. Following the ECB's monetary policy meeting in November, market expectations of further stimulation have increased, and the ECB intends to expand its balance sheet by around EUR 1,000 billion. Since the Monetary Policy Report was published in October, the Japanese central bank has extended its asset purchase programme to ensure that inflation attains 2 per cent. The Norwegian central bank unexpectedly cut its policy rate at its monetary policy meeting in December, and the Chinese central bank has made its monetary policy more expansionary, cutting its policy rate in November for the first time in two and a half years.

- Forward pricing of the repo rate and the Riksbank's forecast coincide until autumn 2016, when the repo-rate path indicates a first policy rate increase. According to forward pricing, the market is expecting an increase to 0.25 per cent at the beginning of 2017 and after that a slower rate of increase than is indicated in the Riksbank's forecast. The expectations in the TNS Sifo Prospera survey in December are somewhat higher and indicate a repo rate of 0.6 per cent at the end of 2016.

- Measured in terms of the KIX exchange-rate index, the krona weakened in connection with the repo-rate decision in October. Since then the krona has strengthened somewhat, but it is still slightly weaker than prior to the monetary policy meeting in October. In bilateral terms, the krona has continued to weaken against the US dollar and is also weaker against the euro and sterling. At the same time, the krona has strengthened against a number of other currencies, including the Norwegian krona, the Russian rouble and the Japanese yen.

- In October, households' average mortgage rates fell 0.1 percentage points to 2.1 per cent and the banks' listed mortgage rates indicate that interest rates have fallen further since the Riksbank's repo-rate cut at the end of October. Lending rates from banks to Swedish non-financial companies also fell to 2.1 per cent in October. Companies are still being charged low interest rates on the corporate bond market.

- Lending to households increased by 5.9 per cent in October, measured as an annual percentage change. During 2013 and 2014, the rate of lending to households has increased gradually and growth is now at its highest since 2011. The corresponding credit growth for non-financial companies is also increasing and amounted to 3.9 per cent in October. However, the increased bank lending to companies in recent months has coincided with a slower increase in companies' funding from securities, which at the all-in-all entails modest changes in companies' total borrowing.

International situation

- The international economic recovery is proceeding slowly. However, developments differ substantially between several of the major economies in the world. If one looks at the developed economies, GDP in the United States and the United Kingdom is growing relatively quickly, at the same time as the euro area is still being weighed down by the debt crisis, and the Japanese economy is in recession. There is no uniform development in the emerging markets, either. Growth is still high in China and India, but has slowed down over the past year. In Russia and Brazil, on the other hand, growth is weak. All in all, GDP growth abroad was somewhat stronger in the third quarter than was assumed in October. The lower oil price may be expected to stimulate growth in many economies, but the global confidence indicators turned downwards again in November after a small upturn in October.

- GDP in the euro area grew by 0.6 per cent in the third quarter, compared with the immediately preceding quarter and calculated as an annual rate. Thus, growth was somewhat higher than the Riksbank's forecast in October, but a continued weak development in the confidence indicators for companies and households in November means that there are still no signs of a more tangible recovery. Since the beginning of the year growth has slowed down substantially in Germany and the other core countries, at the same time as several of the earlier crisis countries had a more positive development. According to preliminary statistics, HICP inflation in the euro area amounted to 0.3 per cent in November, which is the lowest inflation rate in five years and somewhat lower than was forecast in October. It was primarily the accelerating fall in energy prices that contributed to the fall in inflation. Core inflation, that is, HICP inflation excluding energy, food, alcohol and tobacco, remained unchanged and amounted to 0.7 per cent. Inflation is expected to remain low in the coming months, partly as a result of the fall in the price of oil. Market pricing and survey-based measures imply that inflation expectations have continued to fall. Five years ahead, expectations are at 1.8 per cent, according to the ECB's latest Survey of Professional Forecasters, which is the lowest level since the monetary union was established.

- The US economy is developing strongly and GDP growth was 3.9 per cent in the third quarter, compared with the second quarter of this year and calculated as an annual rate. Growth was marked by a strong development in domestic demand. According to the purchasing managers' index, corporate sector confidence remained high in November in both the manufacturing industry and the services sector. Household confidence has strengthened in recent months and the monthly statistics for household consumption in October and the retail trade in November indicate a strong development in the fourth quarter, too. The situation on the labour market has also continued to improve and employment increased rapidly in November. Unemployment then amounted to 5.8 per cent. CPI inflation was 1.7 per cent in October.

- New statistics for the Chinese economy imply lower growth in the coming quarters, as domestic demand has developed somewhat weaker than expected. Both exports and imports slowed down in November, at the same time as company confidence in the manufacturing industry deteriorated. The lower economic activity has meant that CPI inflation declined to 1.4 per cent in November, the lowest inflation rate in five years. The low inflation contributed to the Chinese central bank unexpectedly cutting its policy rate from 6 per cent to 5.6 per cent in November, the first cut in two and a half years.

- The Japanese economy began the year relatively strongly, but the recovery broke off after the VAT increase in April. Following a severe decline in the second quarter, GDP fell further somewhat during the third quarter. Growth in the third quarter was significantly lower than was assumed in the October Monetary Policy Report. The weak development has contributed to the VAT increase for next year being postponed until April 2017. To obtain a mandate for his policy, the prime minister has called a new election in December. New statistics for exports and industrial production imply a somewhat higher growth in the fourth quarter. CPI inflation, which is still affected by the VAT increase, was 2.9 per cent in October, at the same time as inflation excluding the effects of higher VAT was only around 1 per cent.

- Developments on other important Swedish export markets have been mixed. GDP in the United Kingdom grew by 2.8 per cent in the third quarter, compared with the previous quarter and calculated as an annual rate. Growth is still largely explained by strong performance in the services sector and by household consumption. However, development in exports has been weaker and investment declined in the third quarter. Optimism among both households and companies was dampened somewhat in November, but is still at good levels from an historical perspective. Inflation has fallen heavily in recent years, but increased marginally to 1.3 per cent in October. In Norway, activity in the economy slowed down during the third quarter after a very strong second quarter. Household consumption fell during the third quarter for the first time in four years and even non-oil related investment declined. The Danish economy, on the other hand, showed unexpectedly strong growth in the third quarter, although there is an unusually high level of uncertainty regarding the statistics.

GDP in Sweden

- According to the National Accounts, Swedish GDP increased by 1.3 per cent in the third quarter compared with the second quarter and calculated as an annual rate. At the same time, the figure for GDP was revised downwards somewhat for 2013 as whole and for the second quarter of 2014. The development of GDP in the third quarter is largely in line with the forecast in the October Monetary Policy Report. Investment growth and the build-up of stocks in the business sector were stronger than expected, but this was largely offset by the fact that household consumption grew more slowly and imports more rapidly than forecast in October.

- The Economic Tendency Indicator of the National Institute of Economic Research fell somewhat in November but, with the exception of households, all of the sector indicators are still higher than their historical mean values. The downturn was relatively evenly distributed across the various sectors except for the indicator for the manufacturing industry, which increased somewhat. The purchasing managers' index for the manufacturing industry also increased in November, but is still below its historical average. All-in-all, the assessment is that the confidence indicators suggest that the Swedish economy will grow at a normal rate in the fourth quarter.

- Following rapid growth in the second quarter, consumption increased only marginally in the third quarter compared with the second quarter. The relatively low level of growth in the third quarter is deemed to be temporary. Although monthly statistics for household consumption in October indicate weak growth and the household confidence indicator continue to fall in November, retail sales recovered in October following several months of somewhat weaker growth and the number of newly-registered cars continues to be high.

- Investment growth in the third quarter continued to be marked by substantial investments in housing. At the same time, total investment was dampened by the fact that investments in machinery were weak once again. Statistics Sweden's survey of investment plans in the business sector in October, indicates moderate investment growth in both 2014 and 2015. Nevertheless, it is assessed that a gradual increase in demand in later 2014 and early 2015 will contribute to an increased need to investment in the business sector.

- The development of foreign trade in the third quarter was well in line with development over the last 12 months. Exports continued to increase at a moderate rate at the same times as imports increased much more rapidly. All-in-all, foreign trade thereby continued to hold back GDP growth. However, according to both the Economic Tendency Survey and the purchasing managers' index, the figures for new export orders are at levels close to their historical averages and exports are expected to increase as international demand increases more rapidly in the quarters ahead.

Labour market

- The labour market continue to show positive development, although the start of the fourth quarter was somewhat weaker than expected. For October and November together, employment has been somewhat weaker and the labour force has been in line with the forecast in October, which means that unemployment is somewhat higher than expected.

- Indicators of the demand for labour suggest that employment will continue to increase in the quarters immediately ahead. The number of newly-reported job vacancies has continued to increase at the same time as the number of redundancy notices remains low. According to the Economic Tendency Survey, employment plans in the business sector decreased somewhat during the summer and autumn but increased again somewhat in November and they are still higher than an historical average.

- The overall outlook is that the labour market will improve at a somewhat slower rate in the fourth quarter of 2014 and the first quarter of 2015, compared with the forecast in October. This is mainly due to the assumption that the number of employed will show weaker development and contribute to somewhat higher unemployment.

Cost pressures and inflation

- According to the short-term wage statistics from the National Mediation Office, wages in the economy as a whole increased by an average of 2.8 per cent during the first nine months of the year, expressed as an annual percentage change. The statistics are still preliminary and are usually revised up when retroactive payments are entered. All in all, wages in the economy as a whole are expected to increase by 3.0 per cent this year.

- On the other hand, the National Accounts' measure of hourly wages in the economy as a whole increased only slightly in the third quarter, much due to an unexpectedly strong increase in the number of hours worked. Developments in the third quarter contribute to the assessment that this measure of hourly wages will increase less in 2014 than indicated by the short-term wages statistics.

- The unexpectedly rapid increase in the number of hours worked in the third quarter also contributed to labour productivity falling unexpectedly by 0.7 per cent, expressed as an annual percentage change. The annual rate of increase in unit labour costs was thus significantly higher than forecast in October. Revisions to the National Accounts have meant that the figures for unit labour costs were also somewhat higher than expected in 2013 and the first half of 2014. The quarterly development of the number of hours worked usually varies considerably and it is assessed that much of this high growth is a temporary phenomenon and will fall back in the fourth quarter. This will also entail a recovery in labour productivity and a lower rate of increase in unit labour costs.

- All in all, inflation has developed in line with the forecast in the October Monetary Policy Report. Compared with the assessment in October, goods and food prices have shown somewhat stronger development, but this has at the same time been counteracted by weaker developments in energy and services prices. Measured as an annual percentage change in the CPI, inflation was negative in November. The very weak development of the CPI is partly due to a fall in households' mortgage interest costs as a result of the gradual cuts in the repo rate.

- However, inflation is low even if one disregards the effects of decreasing interest costs. The annual rate of increase in the CPIF, that is, the CPI with a fixed mortgage rate, was 0.6 per cent in November. If changes in the volatile energy prices are also disregarded, CPIF inflation was somewhat higher, 1.0 per cent.

- Measured as an annual percentage change, the CPIF is expected to increase by 0.3 per cent in December and then to increase more rapidly during the first quarter of 2015. The forecast for CPIF inflation has been adjusted down for the first quarter of 2015, mainly as a result of lower fuel prices, but also through the indirect effects the rapidly-falling oil price is expected to have on other products in the CPI. Although producer prices for consumer goods sold in Sweden have increased by just over 2 per cent compared to October last year, it is expected that the companies will continue to find it difficult to pass on their cost increases to consumer prices. Producer prices have above all increased on the imports market, which is mainly due to the weakening of the krona. At the same time, producer prices on the domestic market are still increasing more slowly than a historically-average rate of increase, although the rate is gradually accelerating.

- Household interest expenditure has fallen marginally more than the Riksbank forecast in October following unexpectedly substantial reductions in mortgage rates. As household interest expenditure continues to fall, CPI inflation will be lower than CPIF inflation in the months ahead too.

- Money market players expect the rate of inflation to be 0.7 per cent one year ahead and 1.3 per cent two years ahead, at the same time as inflation expectations five year ahead fell to 1.7 per cent according to the survey published by TNS Sifo Prospera in December. According to the Economic Tendency Survey in November, households expect inflation to be 0.0 per cent one year ahead, which also applies to the currently perceived inflation rate.

■ Tables

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

Table 1. Repo rate forecast
Per cent, quarterly averages

	Q3 2014	Q4 2014	Q4 2015	Q4 2016	Q4 2017
Repo rate	0.3	0.1 (0.1)	0.0 (0.0)	0.5 (0.8)	1.5 (1.8)

Source: The Riksbank

Table 2. Inflation
Annual percentage change, annual average

	2013	2014	2015	2016	2017
CPI	0.0	−0.2 (−0.2)	0.3 (0.4)	2.0 (2.1)	3.2 (3.2)
CPIF	0.9	0.5 (0.5)	1.0 (1.2)	2.0 (2.0)	2.1 (2.0)
CPIF excl. energy	1.1	0.7 (0.7)	1.4 (1.5)	2.1 (2.1)	2.1 (2.1)
HICP	0.4	0.2 (0.2)	0.9 (1.2)	2.0 (1.9)	2.1 (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

	2013	2014	2015	2016	2017
Repo rate	1.0	0.5 (0.5)	0.0 (0.0)	0.2 (0.3)	1.1 (1.4)
10-year rate	2.1	1.7 (1.8)	1.2 (1.4)	2.2 (2.4)	3.1 (3.3)
Exchange rate, KIX, 18 Nov. 1992 = 100	103.0	106.7 (106.7)	107.7 (106.4)	103.9 (102.6)	102.6 (101.4)
General government net lending*	−1.4	−2.2 (−2.3)	−1.3 (−1.4)	−0.7 (−0.7)	−0.4 (−0.4)

* 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	2013	2014	2015	2016	2017
Euro area	0.14	0.47	−0.4	0.9 (0.6)	1.1 (0.9)	1.7 (1.7)	1.9 (1.9)
USA	0.19	0.08	2.2	2.3 (2.3)	3.4 (3.3)	2.9 (2.7)	2.5 (2.4)
Japan	0.06	0.03	1.6	0.2 (0.7)	0.9 (0.9)	1.1 (0.8)	0.5 (0.9)
China	0.15	0.07	7.7	7.4 (7.4)	7.0 (7.2)	6.8 (6.9)	6.6 (6.6)
KIX-weighted	0.79	1.00	1.1	1.9 (1.9)	2.1 (2.1)	2.5 (2.5)	2.6 (2.6)
World (PPP-weighted)	1.00	—	3.3	3.2 (3.2)	3.7 (3.7)	3.9 (3.8)	3.8 (3.8)

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 2011 that are used for 2014, and on an assumption that the weights will develop according to the trend of the past five years in the coming forecast year.

CPI	2013	2014	2015	2016	2017
Euro area (HICP)	1.4	0.4 (0.5)	0.5 (1.1)	1.3 (1.4)	1.5 (1.5)
USA	1.5	1.7 (1.8)	0.9 (2.3)	2.1 (2.5)	2.8 (2.5)
Japan	0.4	2.8 (2.8)	1.6 (2.2)	1.5 (2.2)	2.1 (2.0)
KIX-weighted	1.9	1.4 (1.5)	1.5 (2.0)	2.1 (2.2)	2.3 (2.2)

	2013	2014	2015	2016	2017
Policy rates in the rest of the world, per cent	0.2	0.2 (0.2)	0.1 (0.1)	0.3 (0.3)	0.5 (0.6)
Crude oil price, USD/barrel Brent	108.8	100.4 (103.2)	74.2 (93.8)	78.7 (94.6)	81.5 (94.2)
Swedish export market	1.5	3.1 (3.0)	5.0 (4.9)	5.5 (5.5)	5.8 (5.8)

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

	2013	2014	2015	2016	2017
Private consumption	1.9	2.4 (2.9)	2.6 (3.0)	2.8 (2.9)	2.3 (2.5)
Public consumption	0.7	1.5 (1.1)	1.9 (2.0)	1.9 (2.0)	1.3 (1.3)
Gross fixed capital formation	−0.4	4.7 (4.1)	4.9 (4.4)	5.6 (5.4)	3.7 (3.8)
Inventory investment*	0.1	0.2 (0.2)	0.1 (0.0)	0.0 (0.0)	0.0 (0.0)
Exports	−0.2	2.2 (1.9)	4.9 (4.3)	6.5 (6.0)	5.0 (4.9)
Imports	−0.7	5.1 (4.1)	5.9 (5.3)	6.6 (6.3)	5.5 (5.5)
GDP	1.3	1.8 (1.9)	2.6 (2.7)	3.3 (3.3)	2.3 (2.3)
GDP, calendar-adjusted	1.3	1.9 (2.1)	2.4 (2.5)	3.1 (3.0)	2.5 (2.6)
Final figure for domestic demand*	1.0	2.5 (2.5)	2.8 (2.9)	3.1 (3.1)	2.3 (2.4)
Net exports*	0.2	−1.0 (−0.8)	−0.2 (−0.3)	0.2 (0.1)	0.0 (−0.1)
Current account (NA), per cent of GDP	6.8	5.4 (5.6)	4.7 (5.1)	4.6 (4.9)	4.4 (4.6)

*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

	2013	2014	2015	2016	2017
Population, aged 16–64	0.6	0.7 (0.7)	0.8 (0.8)	1.0 (1.0)	0.9 (0.9)
Potential hours worked	0.6	0.6 (0.6)	0.6 (0.6)	0.7 (0.7)	0.6 (0.6)
GDP, calendar-adjusted	1.3	1.9 (2.1)	2.4 (2.5)	3.1 (3.0)	2.5 (2.6)
Number of hours worked, calendar-adjusted	0.3	2.0 (1.5)	1.0 (1.3)	1.0 (1.1)	0.8 (0.8)
Employed, aged 15–74	1.0	1.5 (1.5)	1.4 (1.4)	1.1 (1.0)	0.7 (0.7)
Labour force, aged 15–74	1.1	1.4 (1.4)	0.9 (0.9)	0.5 (0.4)	0.4 (0.4)
Unemployment, aged 15–74 *	8.0	7.9 (7.9)	7.5 (7.4)	6.9 (6.9)	6.6 (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

	2013	2014	2015	2016	2017
Hourly wage, NMO	2.5	3.0 (3.0)	3.0 (3.0)	3.4 (3.4)	3.5 (3.5)
Hourly wage, NA	2.1	2.1 (2.5)	3.3 (3.4)	3.7 (3.8)	3.7 (3.7)
Employers' contribution*	0.2	0.1 (−0.2)	0.0 (0.2)	0.0 (0.1)	0.0 (0.0)
Hourly labour cost, NA	2.3	2.2 (2.3)	3.3 (3.6)	3.7 (3.9)	3.7 (3.7)
Productivity	0.9	−0.1 (0.5)	1.4 (1.2)	2.0 (1.9)	1.7 (1.7)
Unit labour cost	1.4	2.3 (1.7)	1.9 (2.4)	1.7 (2.0)	2.0 (1.9)

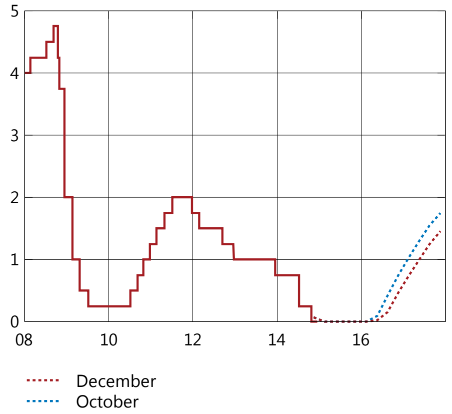
* Contribution to the increase in labour costs, percentage points

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

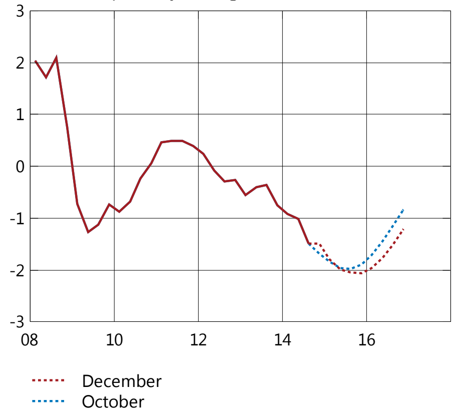
Figure 5. Repo rate
Per cent



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

Source: The Riksbank

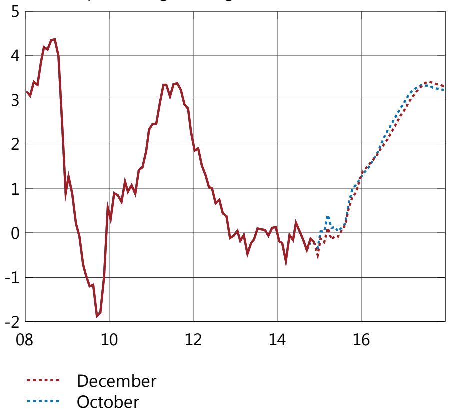
Figure 6. Real repo rate
Per cent, quarterly averages



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.

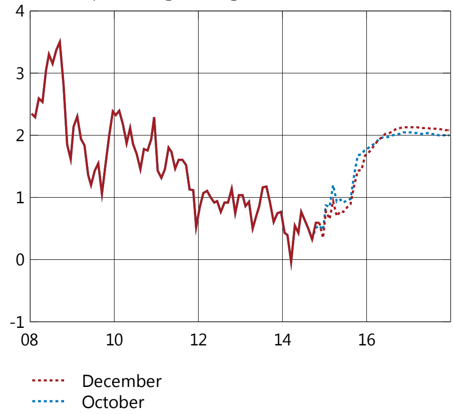
Sources: Statistics Sweden and the Riksbank

Figure 7. CPI
Annual percentage change



Sources: Statistics Sweden and the Riksbank

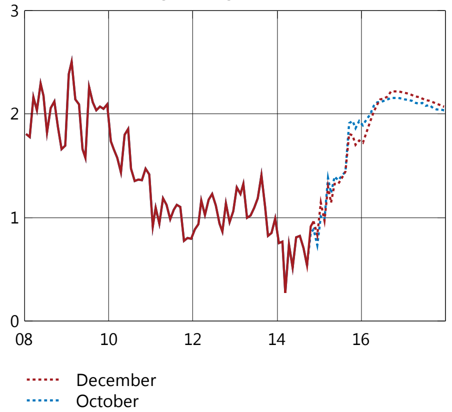
Figure 8. CPIF
Annual percentage change



Note. The CPIF is the CPI with a fixed mortgage rate.

Sources: Statistics Sweden and the Riksbank

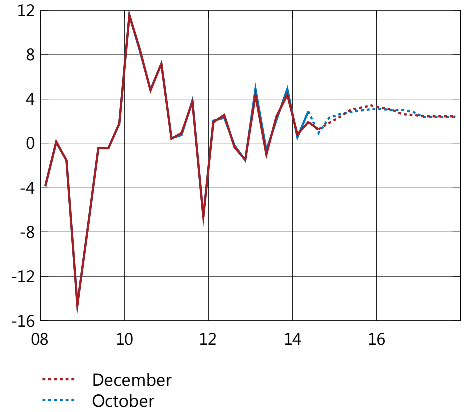
Figure 9. CPIF excluding energy
Annual percentage change



Note. The CPIF is the CPI with a fixed mortgage rate.

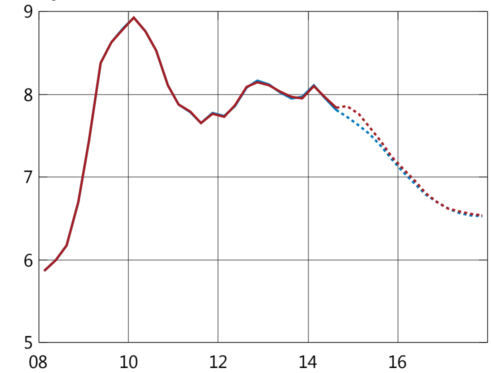
Sources: Statistics Sweden and the Riksbank

Figure 10. GDP
Quarterly change in per cent, calculated as an annual percentage change, seasonally-adjusted data



Sources: Statistics Sweden and the Riksbank

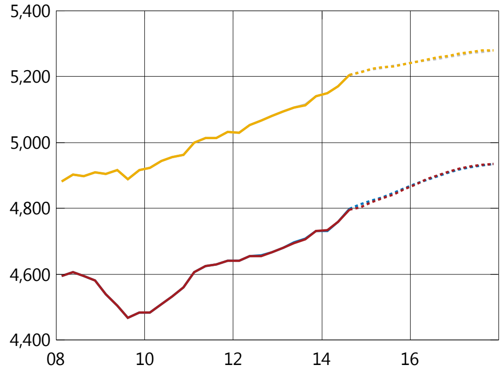
Figure 11. Unemployment
Per cent of the labour force, aged 15–74, seasonally-adjusted data



December
October

Sources: Statistics Sweden and the Riksbank

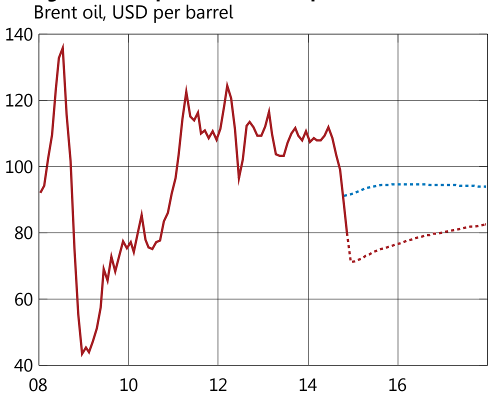
Figure 12. Labour force and number of employed
Thousands, aged 15–74, seasonally-adjusted data



Employed, December
Employed, October
Labour force, December
Labour force, October

Sources: Statistics Sweden and the Riksbank

Figure 13. Oil price and futures prices
Brent oil, USD per barrel

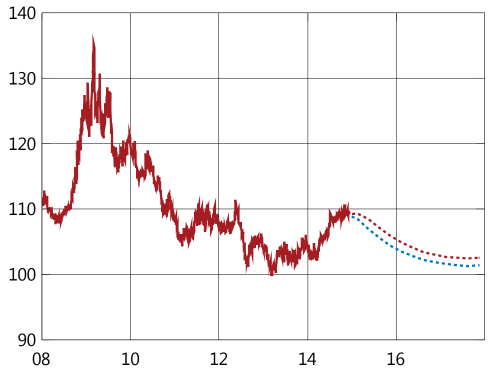


Crude oil (Brent), December
Crude oil (Brent), October

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

Sources: Macrobond and the Riksbank

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

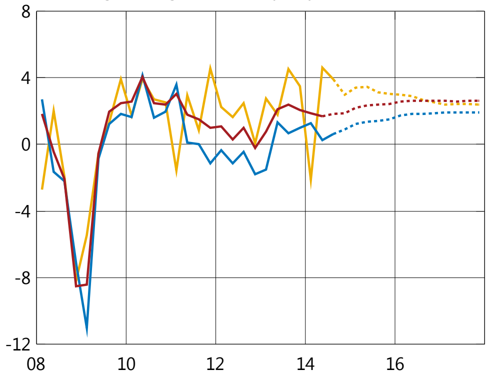


December
October

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 change in per cent, calculated as an annual percentage change, seasonally-adjusted data

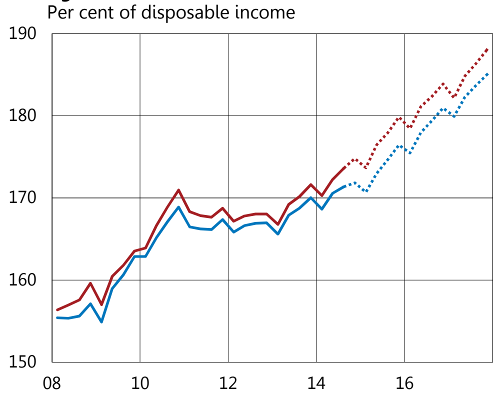


KIX
Euro area
USA

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



December
October

Sources: Statistics Sweden and the Riksbank