



The Riksbank's role in the economy and the economic situation

Mid Sweden University, Campus
Östersund
4 November 2014

Deputy Governor Martin Flodén

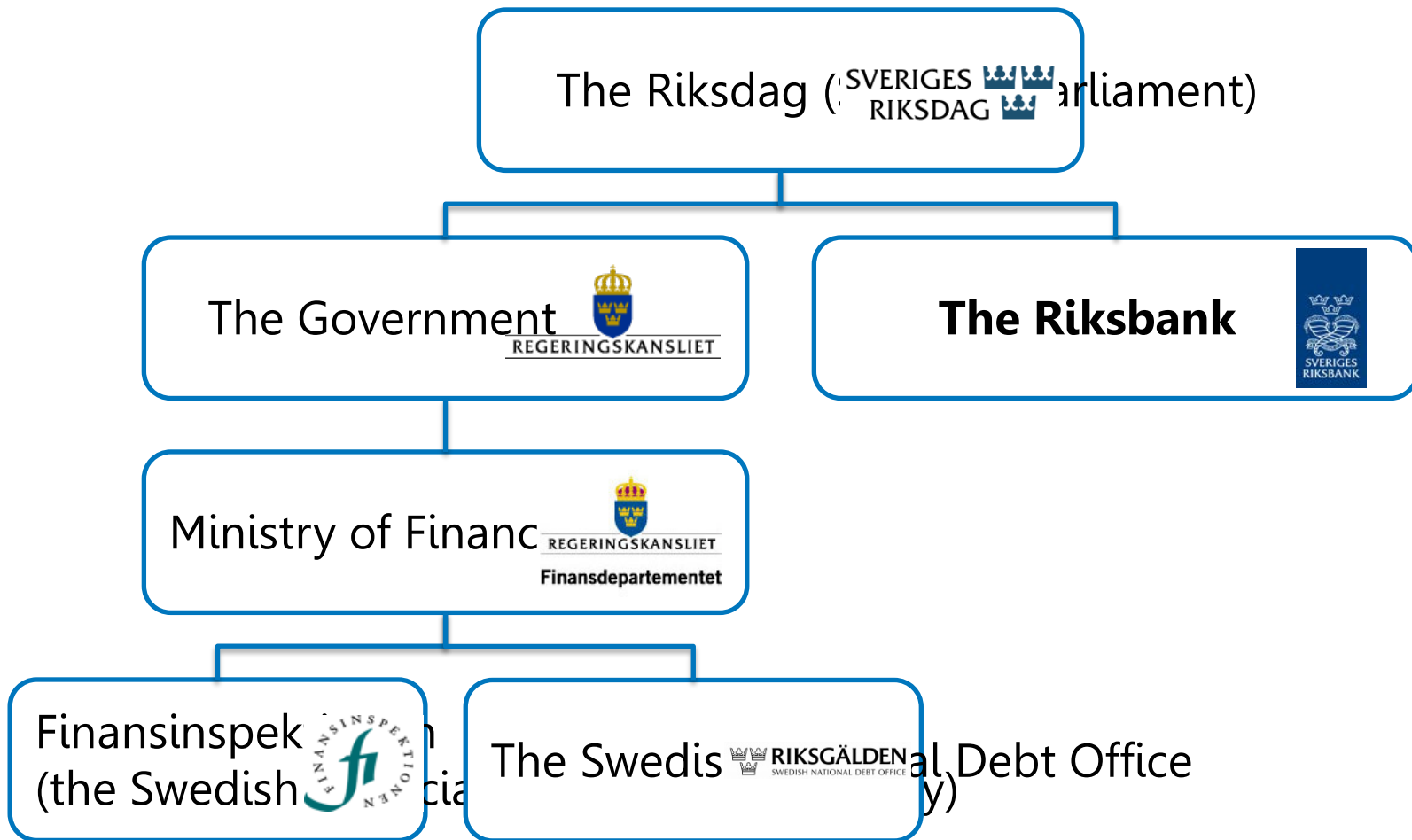
Overview

- About the Riksbank
 - Monetary policy
 - Financial crisis and economic recession
 - The economic situation and the most recent monetary policy decision
 - Financial stability and macroprudential policy
-



About the Riksbank

Public authority under the Riksdag



The governance of the Riksbank



RIKSDAGEN

Riksdagen utser
elva ledamöter.



Riksbanksfullmäktige

Fullmäktige
utnämner
sex ledamöter.



Riksbankens direktion

Executive Board of the Riksbank



Governor
Stefan Ingves



First Deputy Governor
Kerstin af Jochnick



Deputy Governor
Per Jansson



Deputy Governor
Cecilia Skingsley



Deputy Governor
Martin Flodén

The Riksbank's tasks



**Maintain
price stability**

**Promote a
safe and efficient
payment system**



Monetary policy

The Riksbank conducts *flexible inflation targeting*

- Stabilises inflation around 2 per cent *and...*
- ... employment and growth around long-run sustainable levels

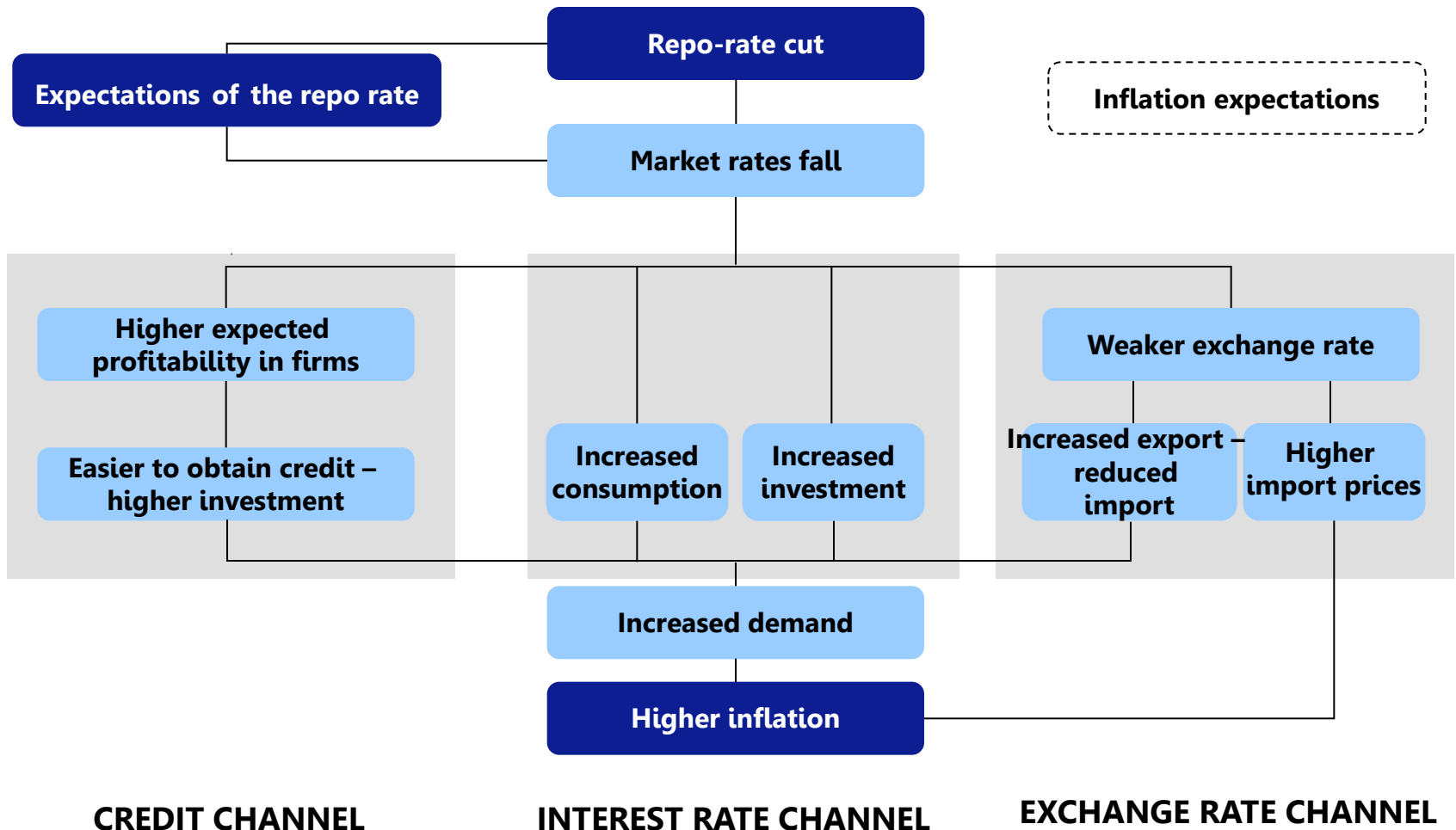
As the impact of monetary policy comes after a time lag, in practice it is a question of *forecast targeting*

Monetary policy tools

- The Riksbank determines the interest rate at which the banks can borrow from or deposit with the Riksbank
 - **Repo rate** applies to weekly transactions
 - Interest rate **corridors** apply to overnight transactions
 - Communication
 - Also publish forecasts for the repo rate 3 years ahead
 - Minutes of monetary policy meetings
-

How do the tools affect inflation?

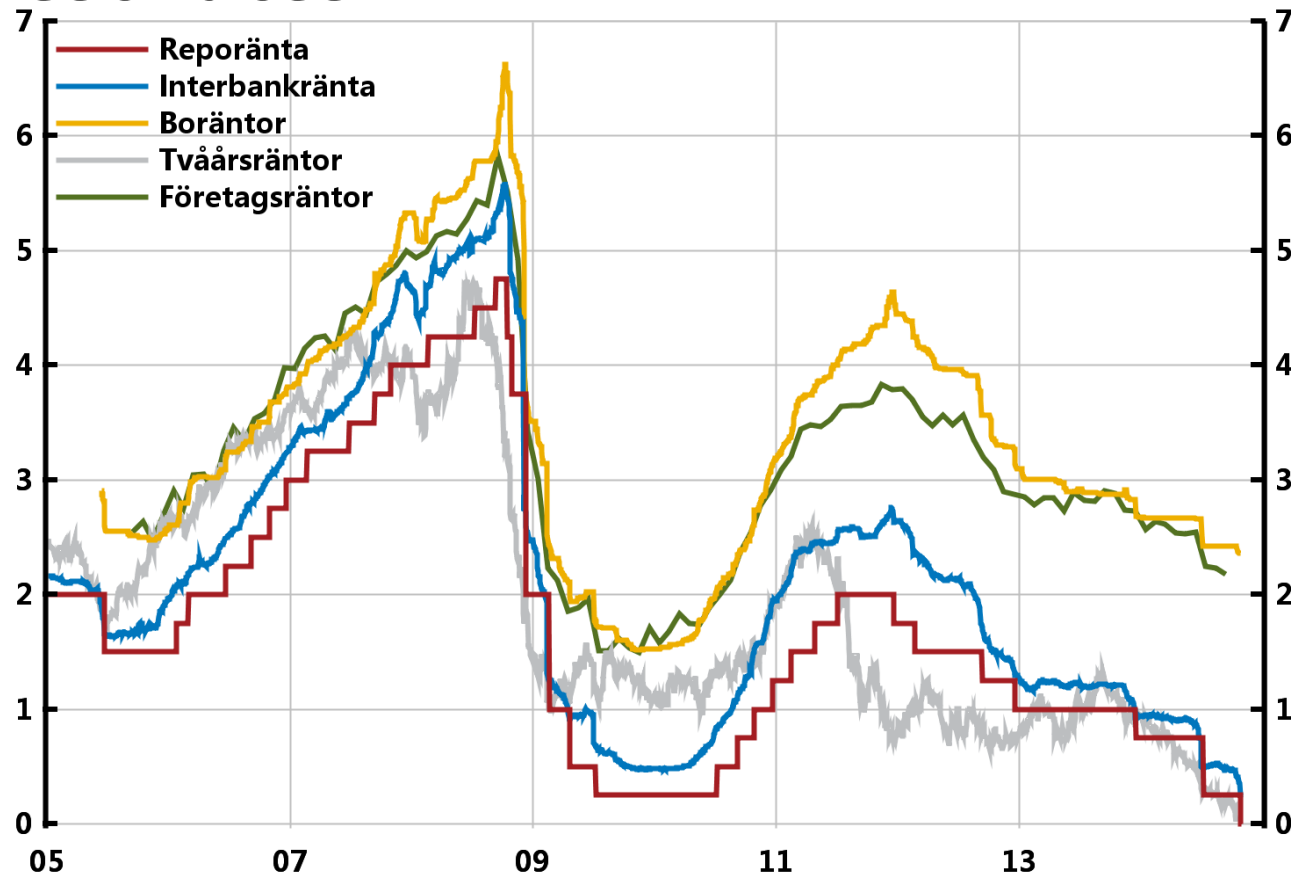
- the monetary transmission mechanism



The repo rate and repo-rate path lay the foundations for other interest rates

Per cent

Interest rates

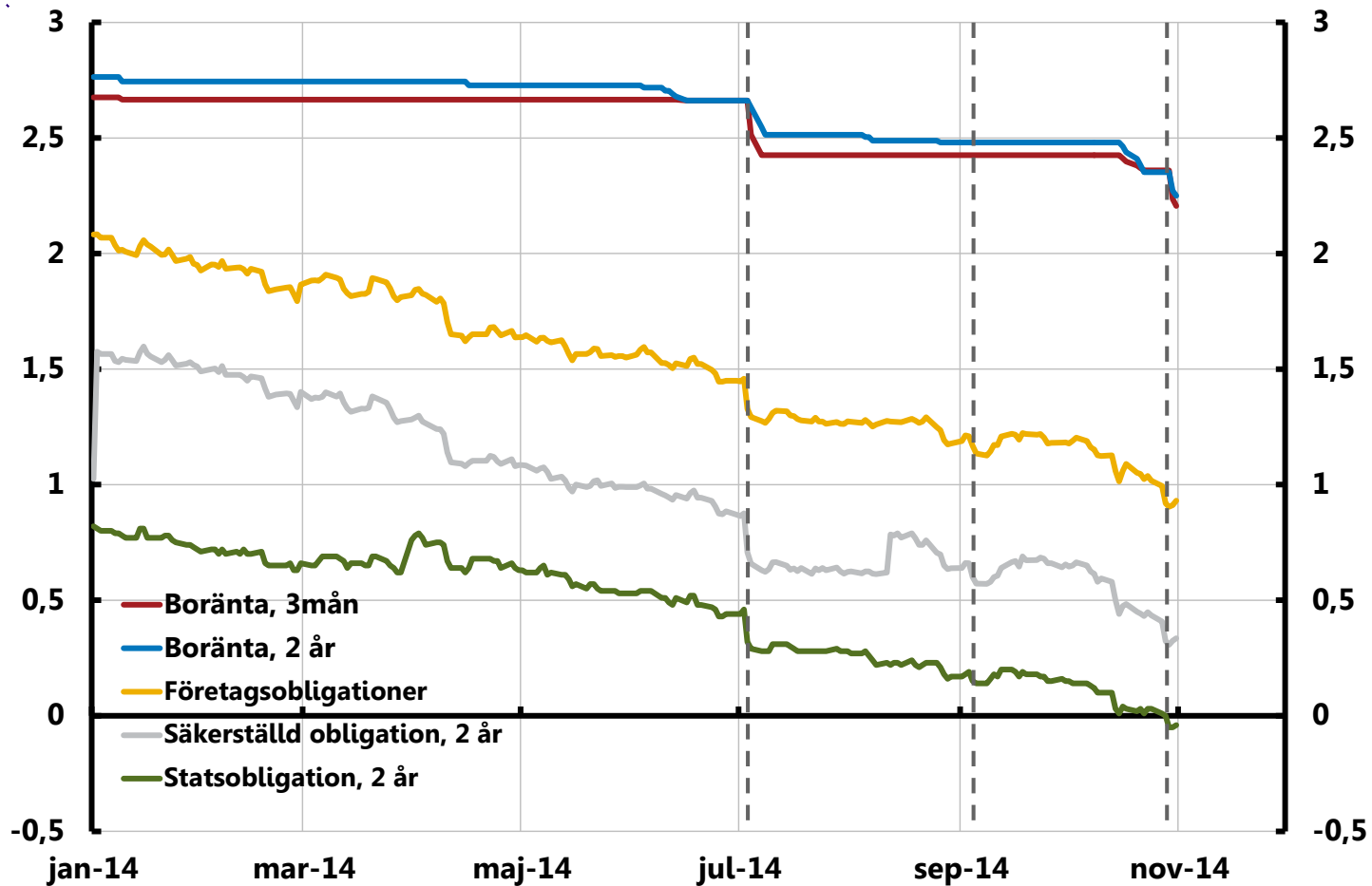


Note. Interbank rate refers to STIBOR 3-month rate. Mortgage rate is an average of 3-month listed mortgage rates. Corporate rate is MFIs' new lending to non-financial

Sources: Macrobond, Statistics Sweden and

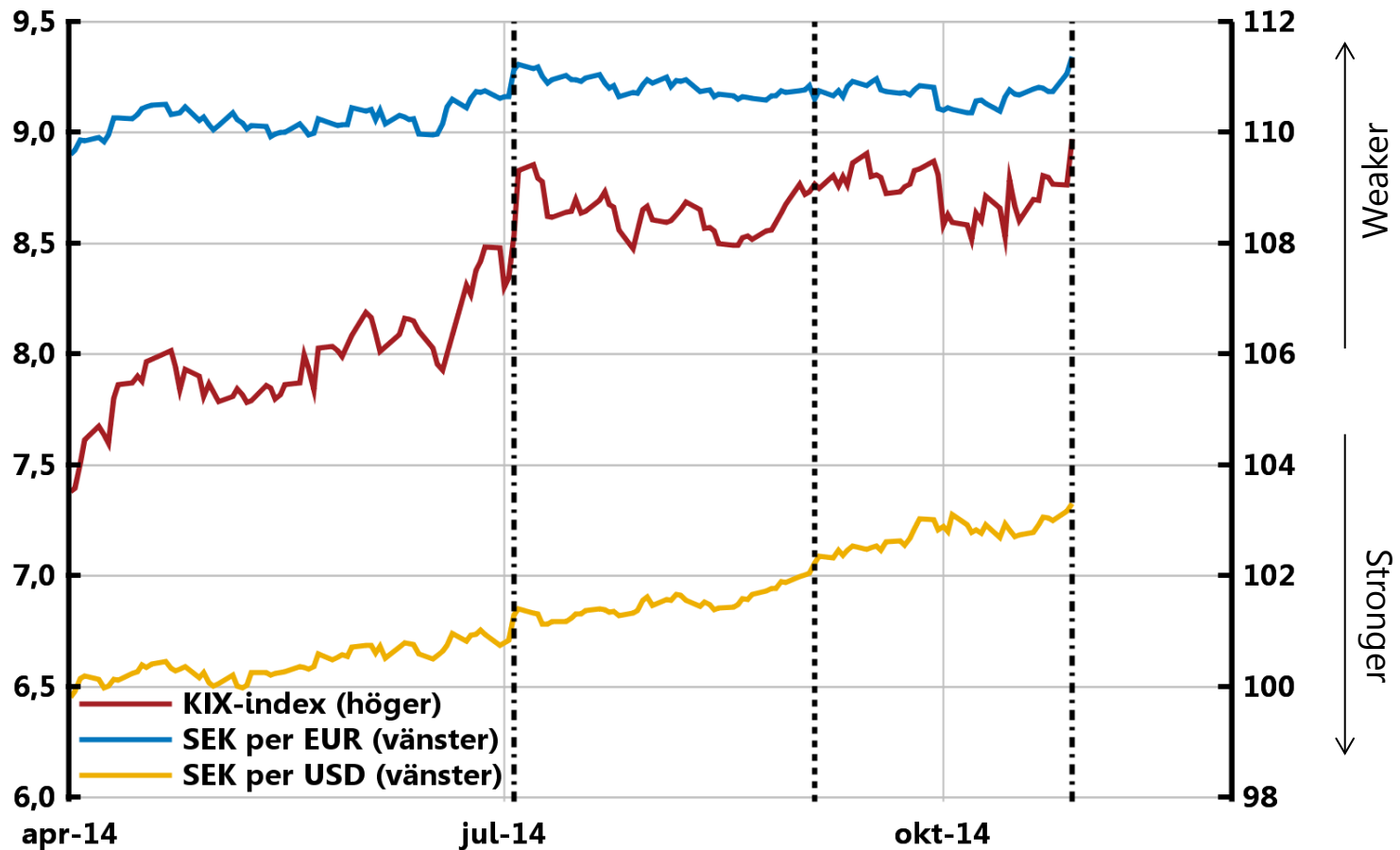
The repo rate affects other interest rates...

Per cent



... and the krona

SEK per foreign currency, Index 18 November 1002 = 100

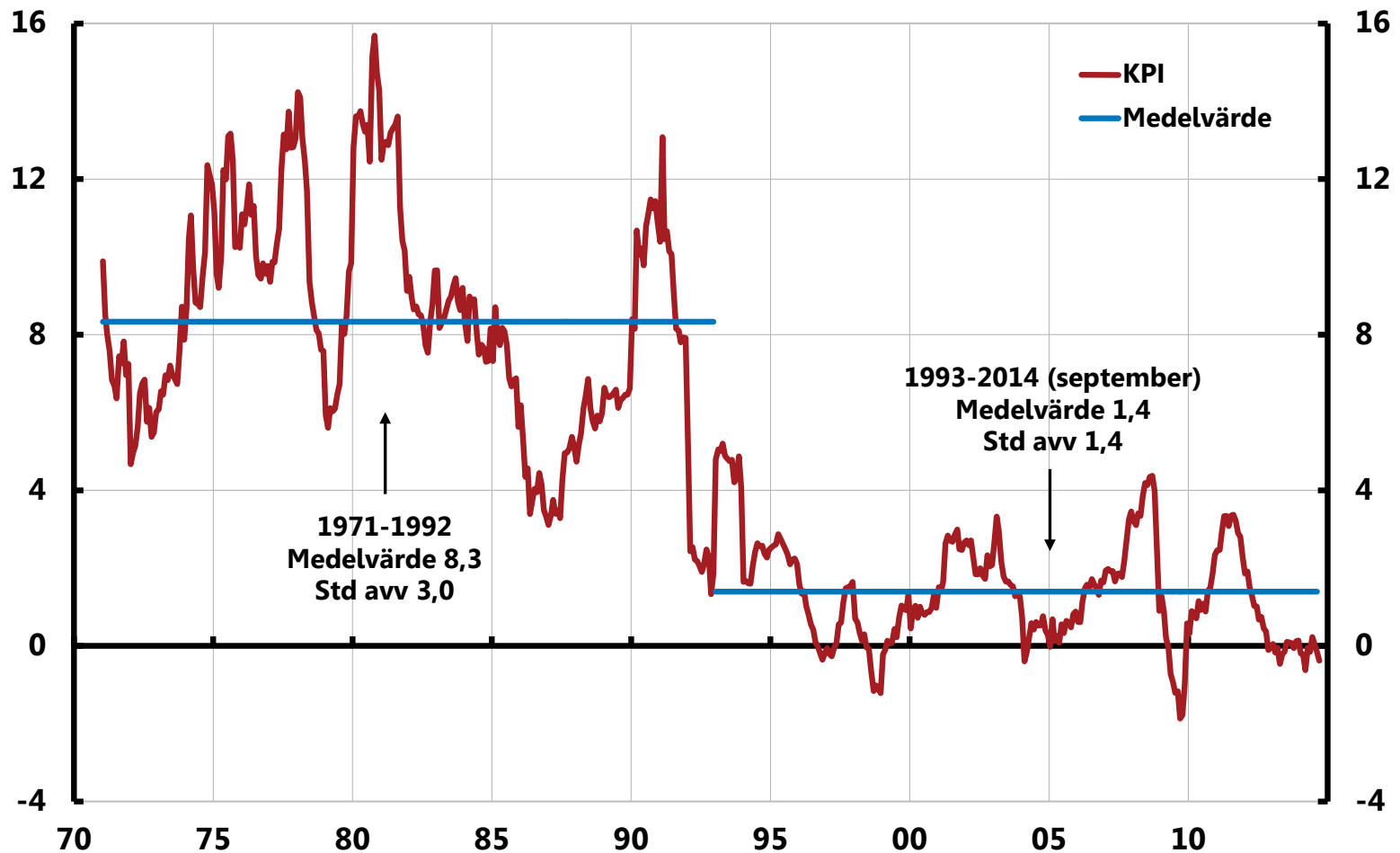


Note. The broken lines show the Riksbank's repo-rate decision in July, the Riksbank's and the ECB's policy-rate decisions in September and the Riksbank's repo-rate decision in October.

Sources: Macrobond and the Riksbank

Lower inflation since the inflation target was introduced

CPI, annual percentage change





Financial crisis and
economic recession

Recent years have been marked by two major problem areas...

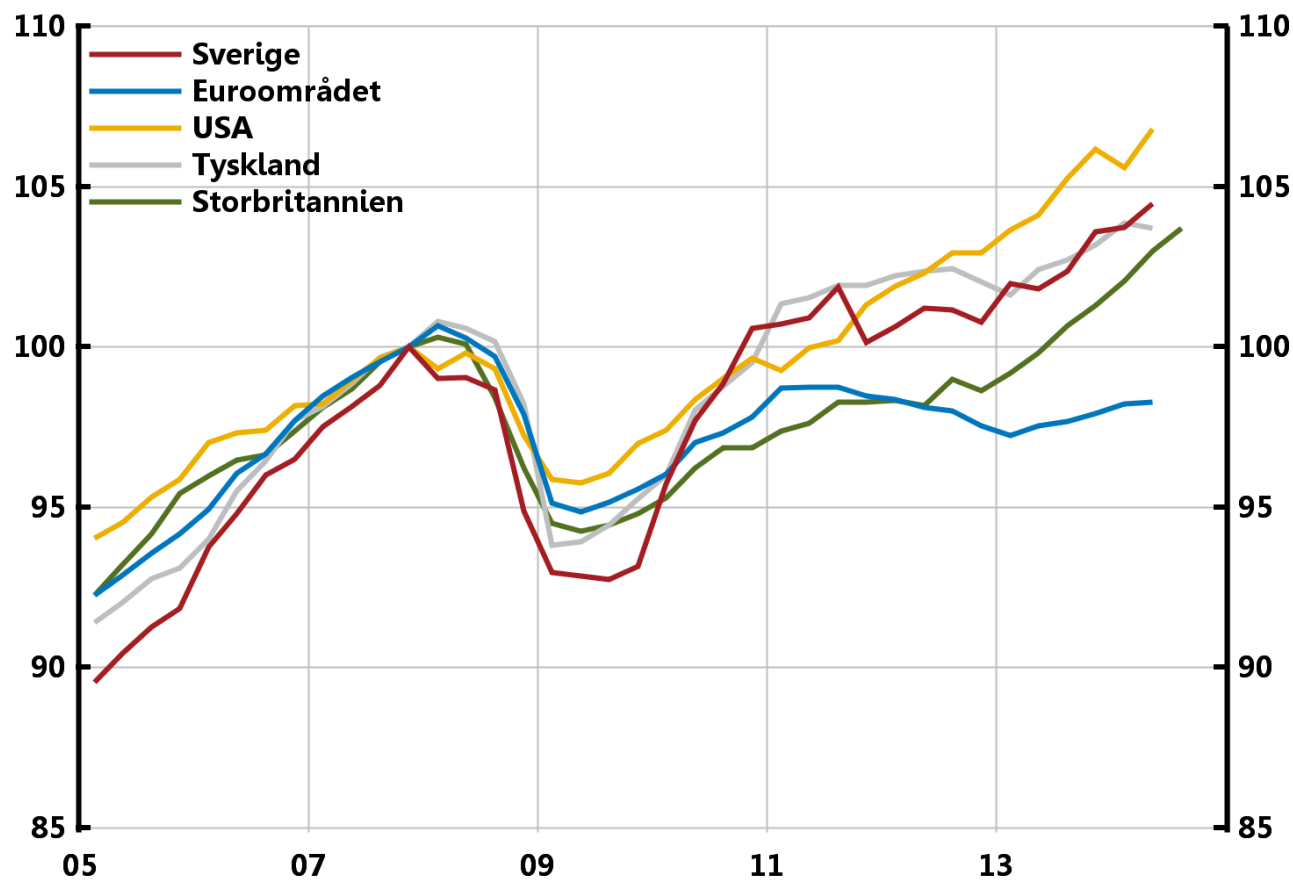


- Managing weak real economic development and falling inflation
- Managing risks linked to major financial systems with structural vulnerabilities



Global financial crisis led to "the great recession"

Index, 2007 Q4 = 100



The great recession: policy reactions

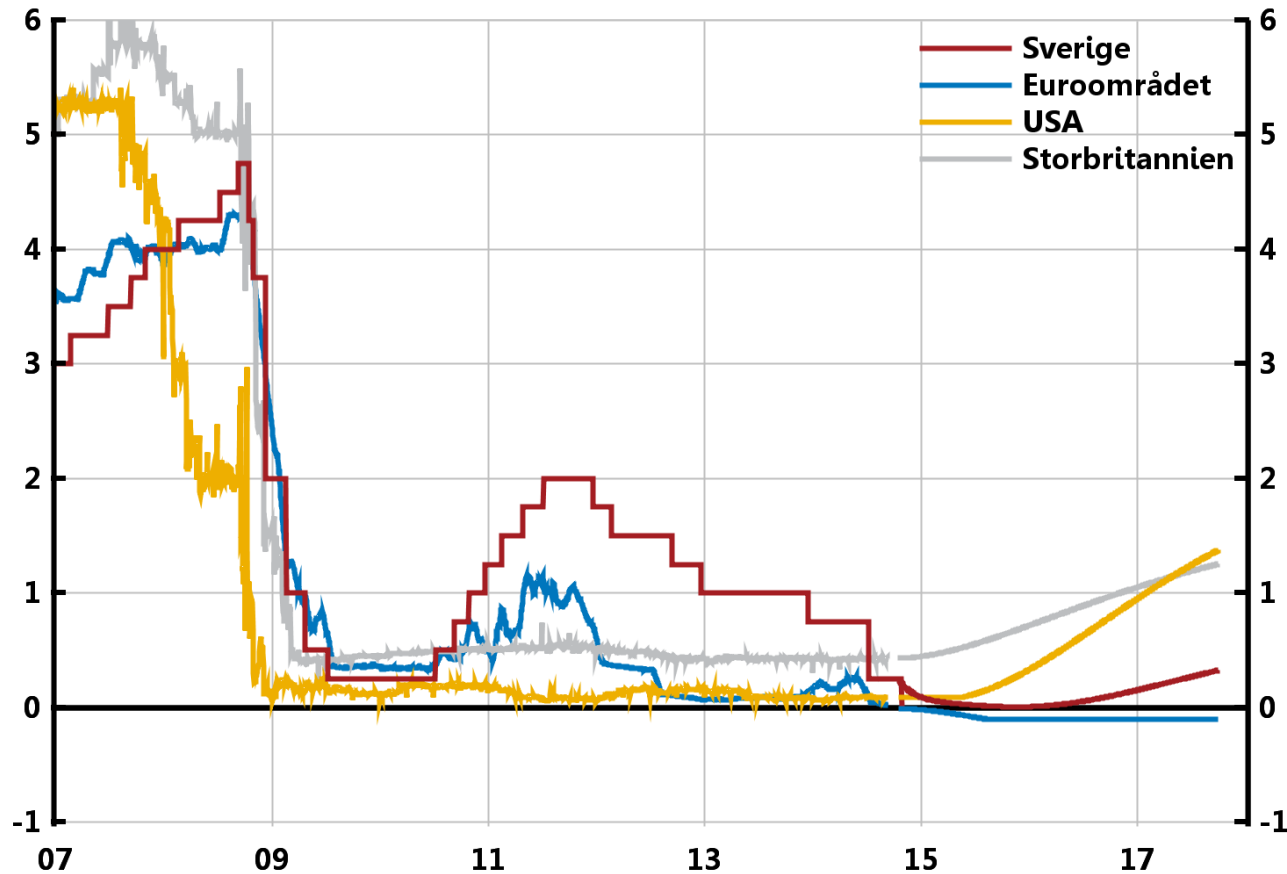
Fiscal policy

Monetary policy



Policy rates cut to their lower bound..

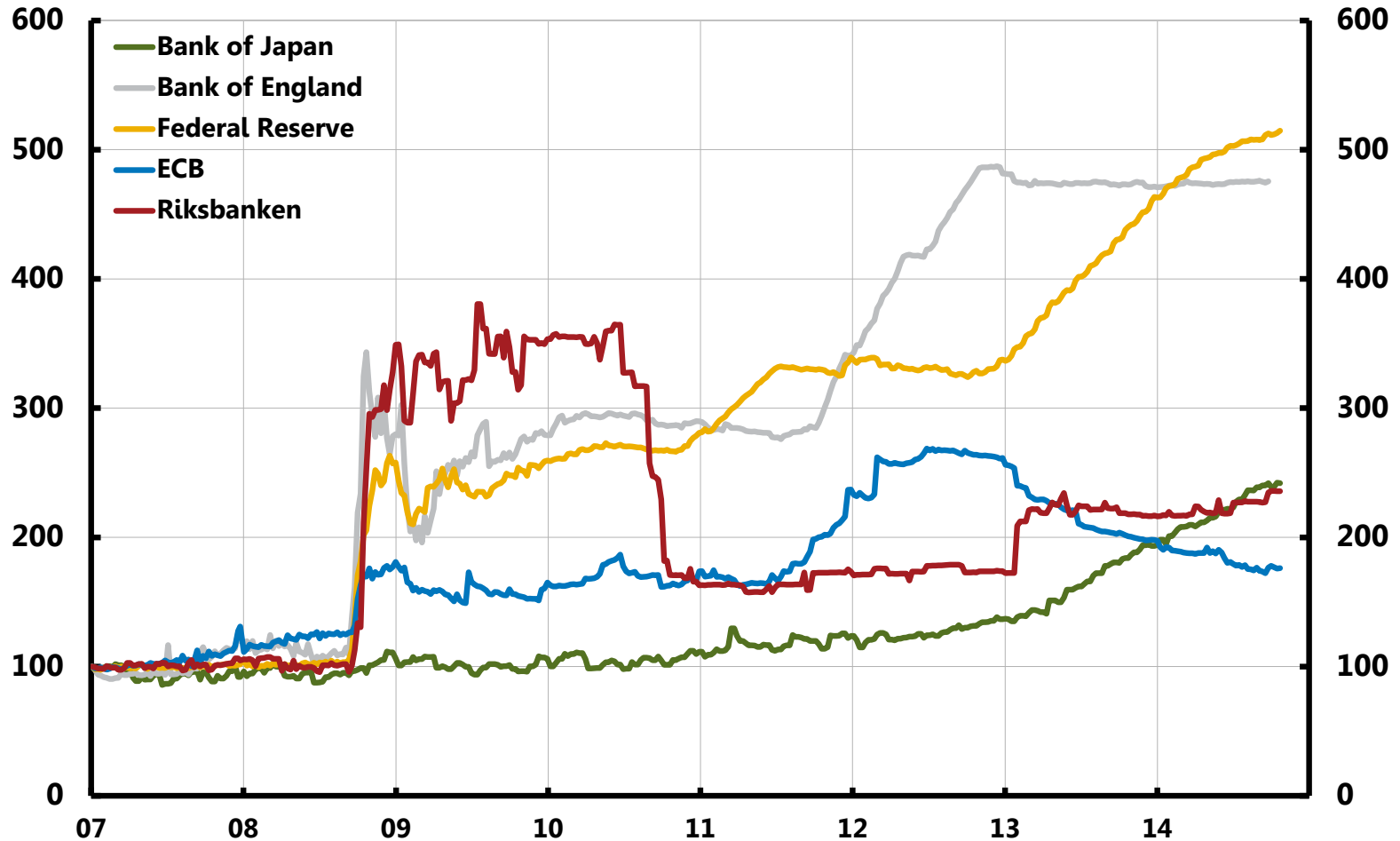
Policy rate, per cent



Note. Unbroken lines show forward rates prior to the Riksbank's repo-rate decision in October. Sources: The Riksbank and Reuters

...and supplemented with unconventional measures

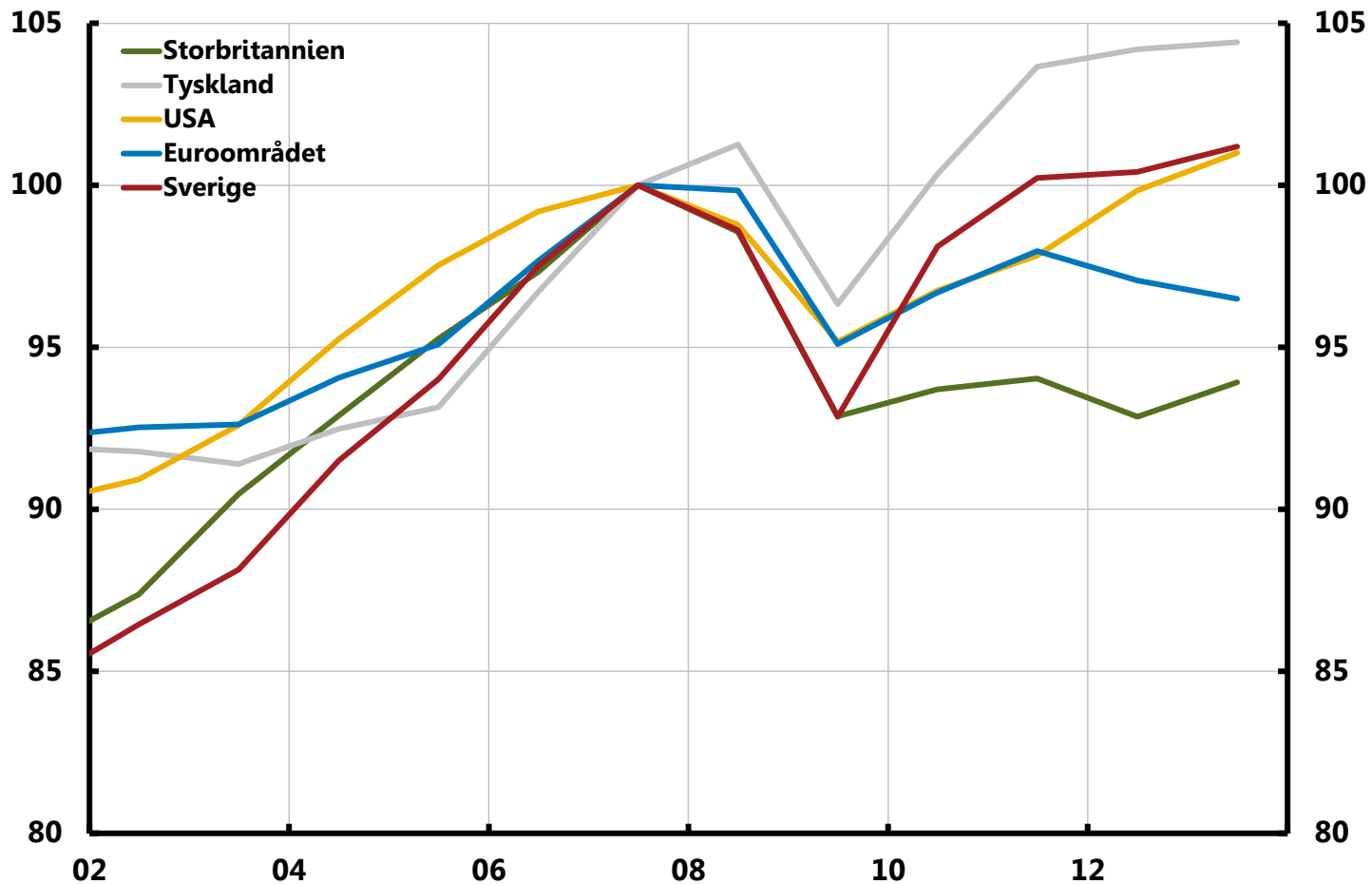
The central banks' balance sheets, index, January 2007 = 100



*"Worst monetary policy in the western
world"*

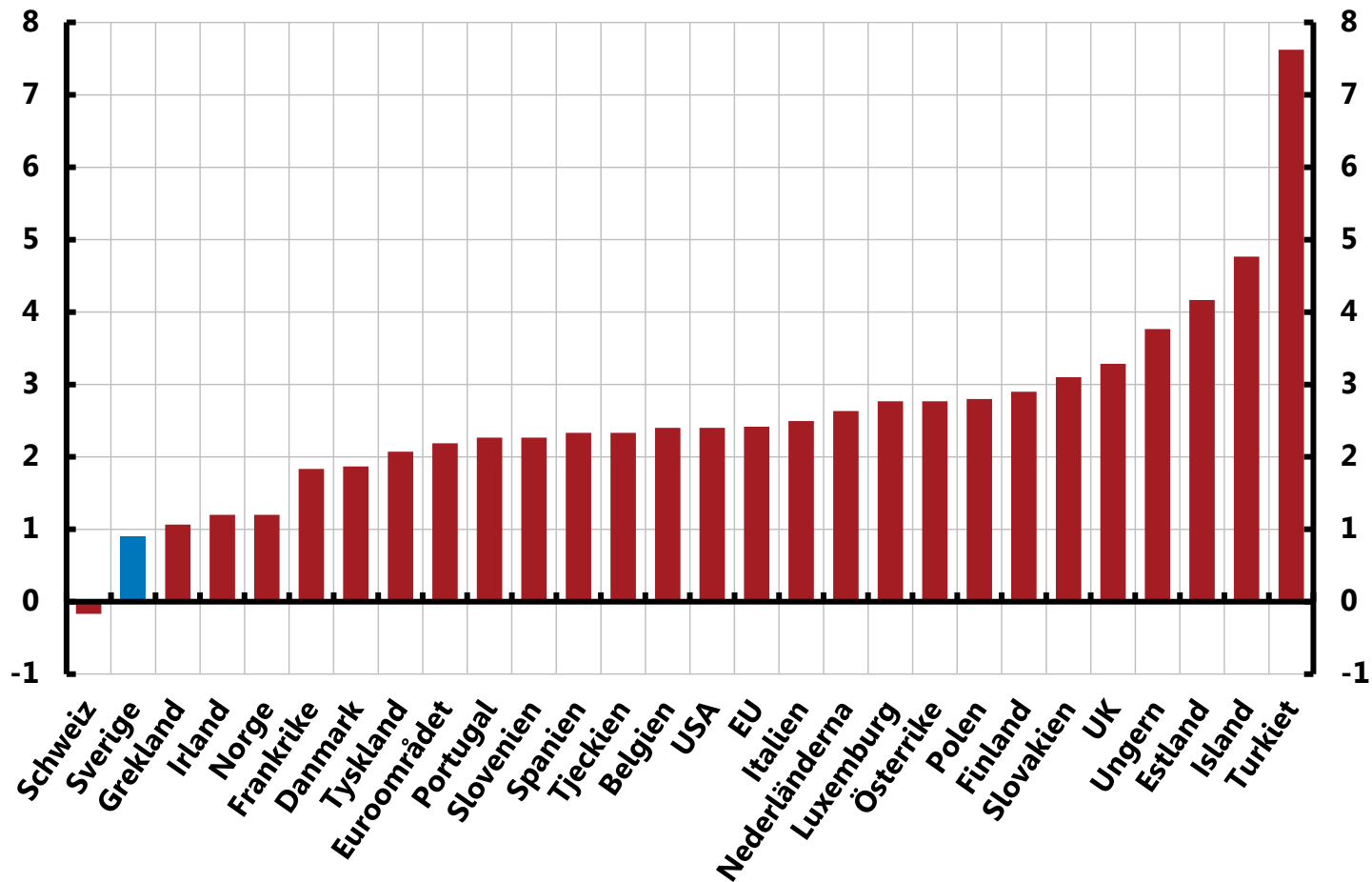
Paul Krugman visiting Stockholm in January 2014.

Sweden has recovered well from the crisis...



... but inflation has become too low

HICP 2011-2013





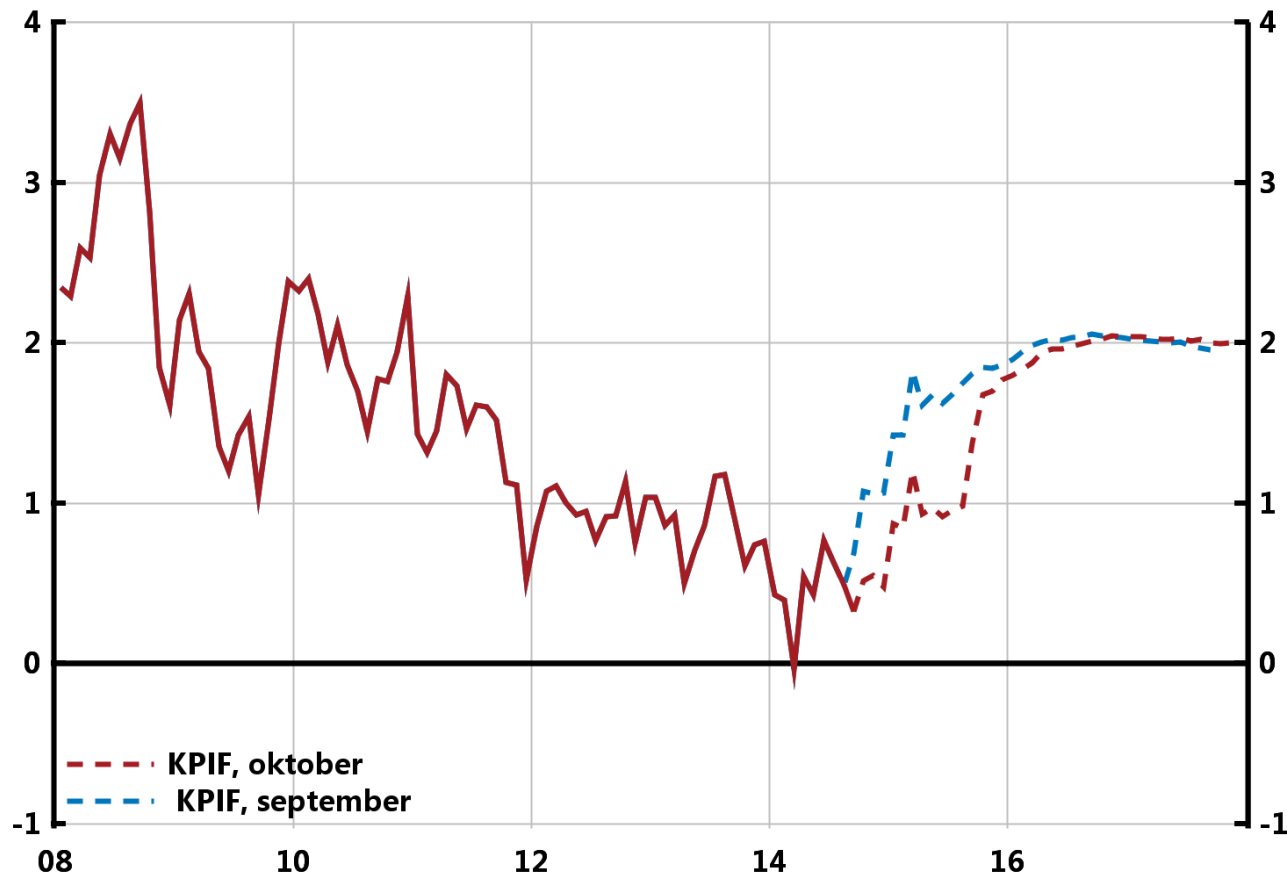
The economic situation and the most recent monetary policy decision

**Better economic climate but too low
inflation**

Zero repo rate until mid-2016

Low inflation in Sweden

CPIF, annual percentage change

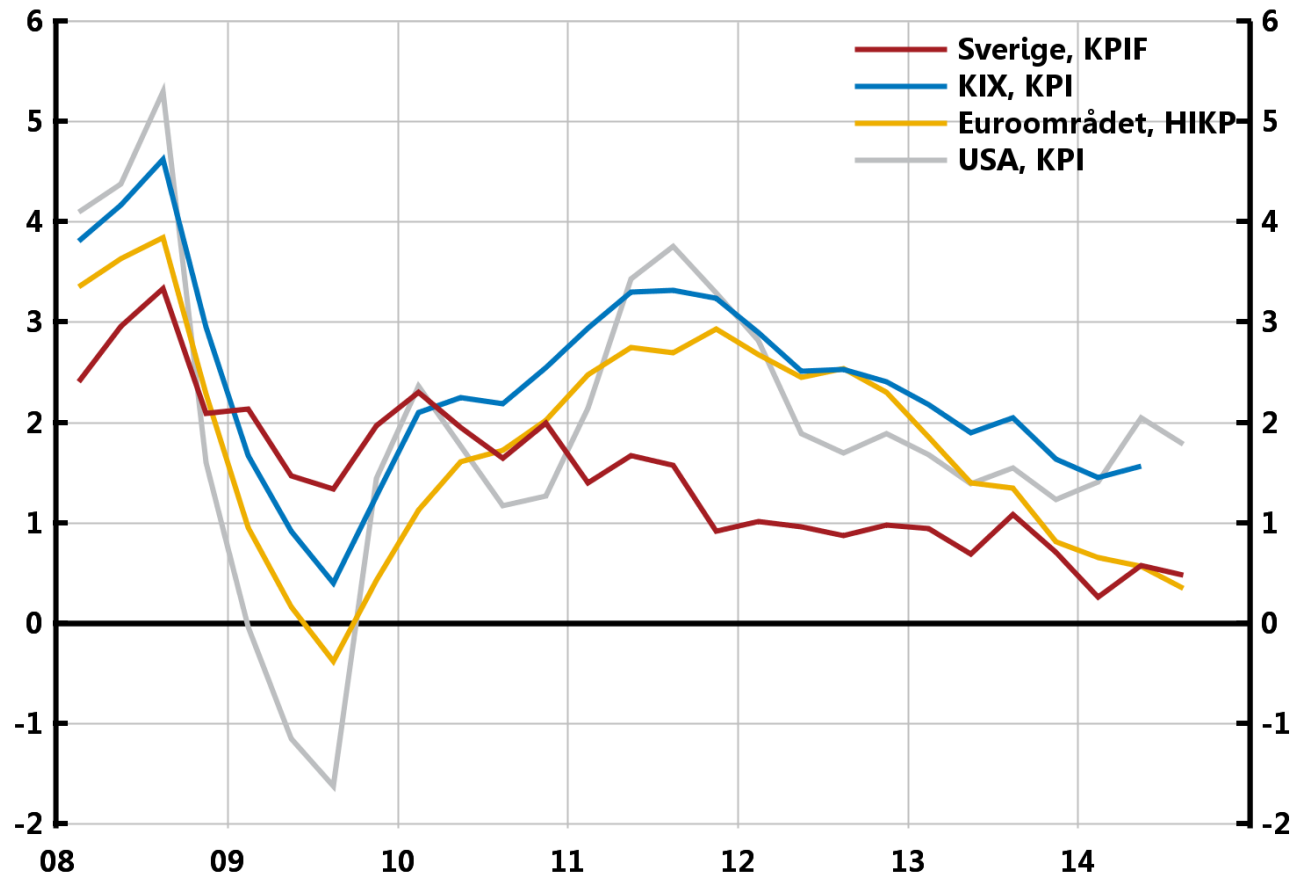


Annual percentage change. The CPIF is the CPI with a fixed mortgage rate.

Source: Statistics Sweden and the Riksbank

Now low inflation abroad, too

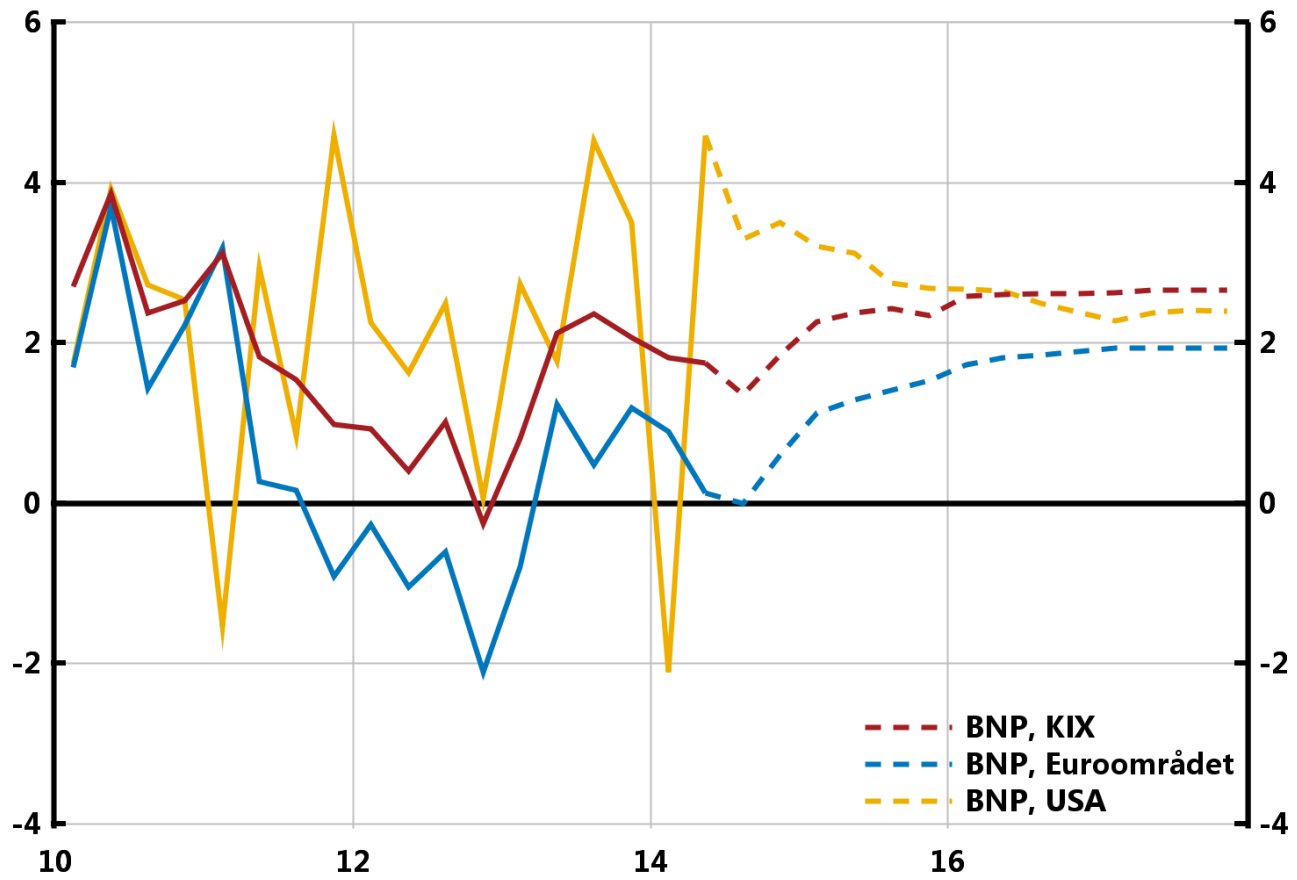
Percentage change



This refers to HICP for the euro area and to CPI for the United States. The KIX is an aggregate of the countries that are important to Sweden's

Sources: The Bureau of Labor Statistics, Eurostat, national sources and Statistics

Other countries recovering – but slowly and out of step

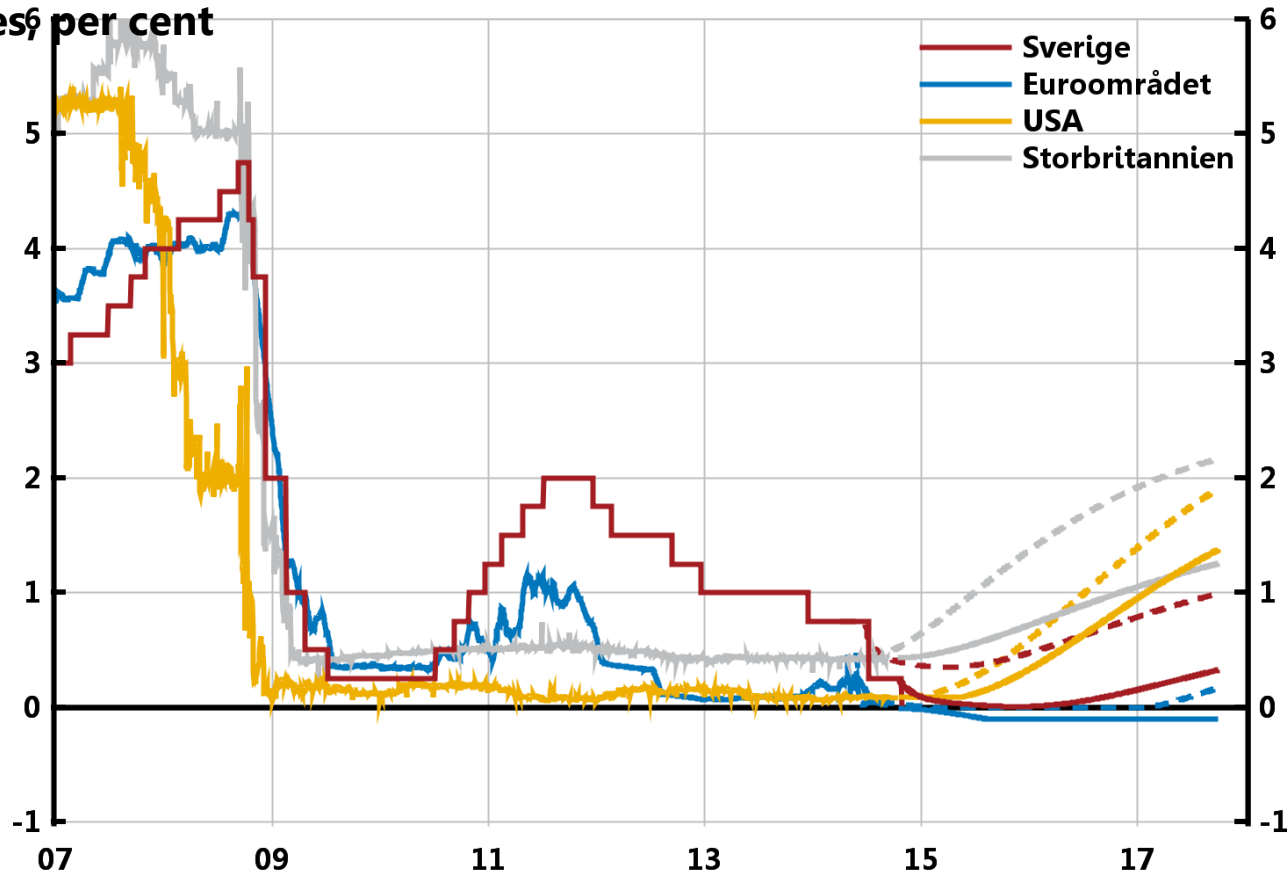


Quarterly changes in per cent calculated as annual rate, seasonally-adjusted data. The KIX is an aggregate of the countries that are important to Sweden's international

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

Monetary policy is also out of step...

Policy rates⁶ per cent

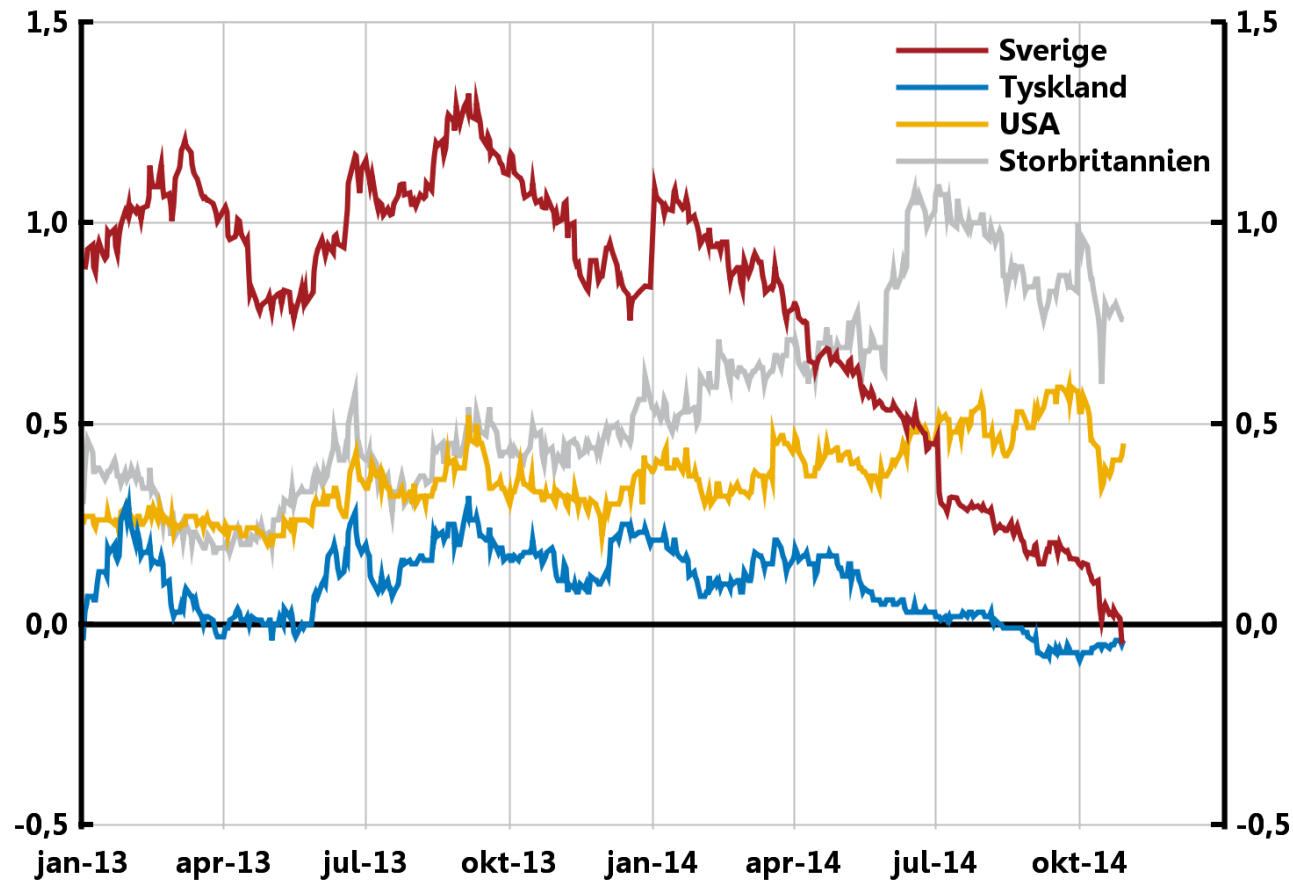


Note. Unbroken lines show forward rates prior to the Riksbank's repo-rate decision in October and broken lines show them prior to the Riksbank's repo-rate decision in

Sources: The Riksbank and Reuters

...which gives increasing spreads

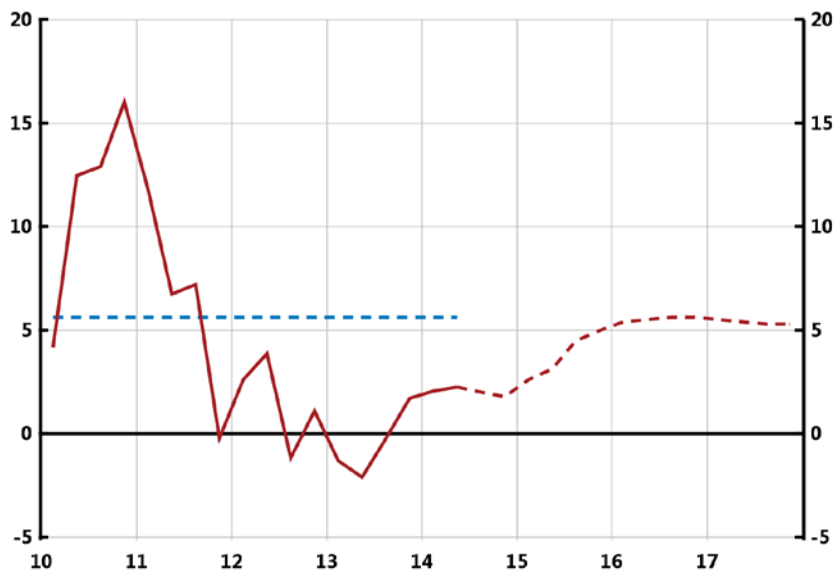
2-year government bond yields, per cent



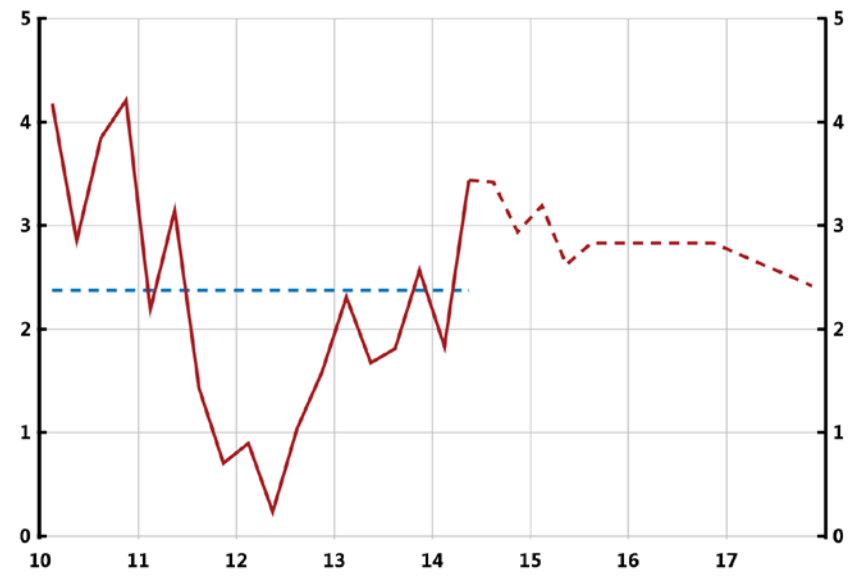
Weak exports, but strong households in Sweden



Exports



Consumption

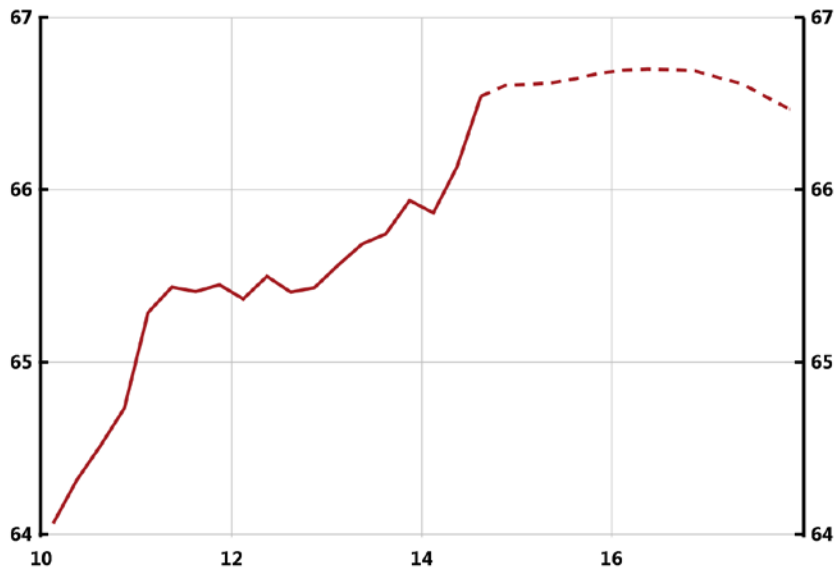


Annual percentage change, seasonally and calendar-adjusted. The broken blue line represents the average for the period 1994Q1-2014Q2.

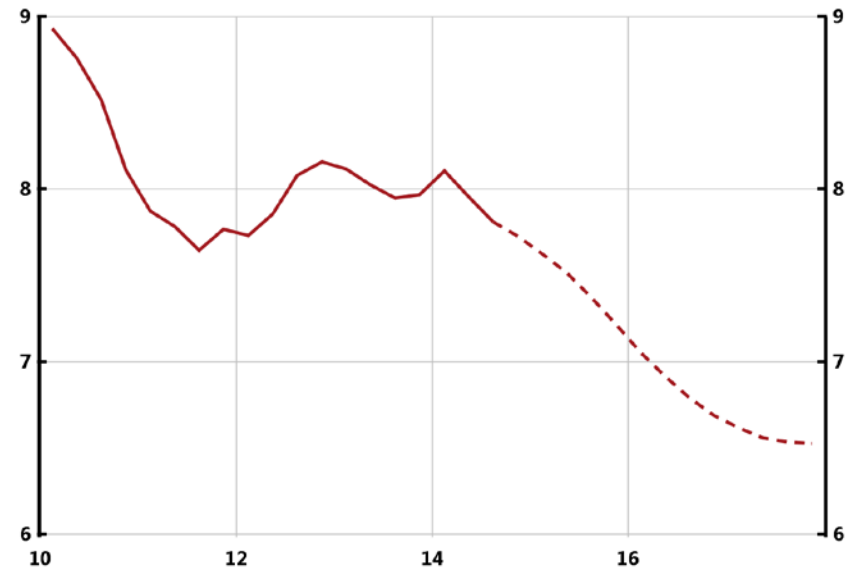
Sources: Statistics Sweden and the Riksbank

Labour market continuing to improve

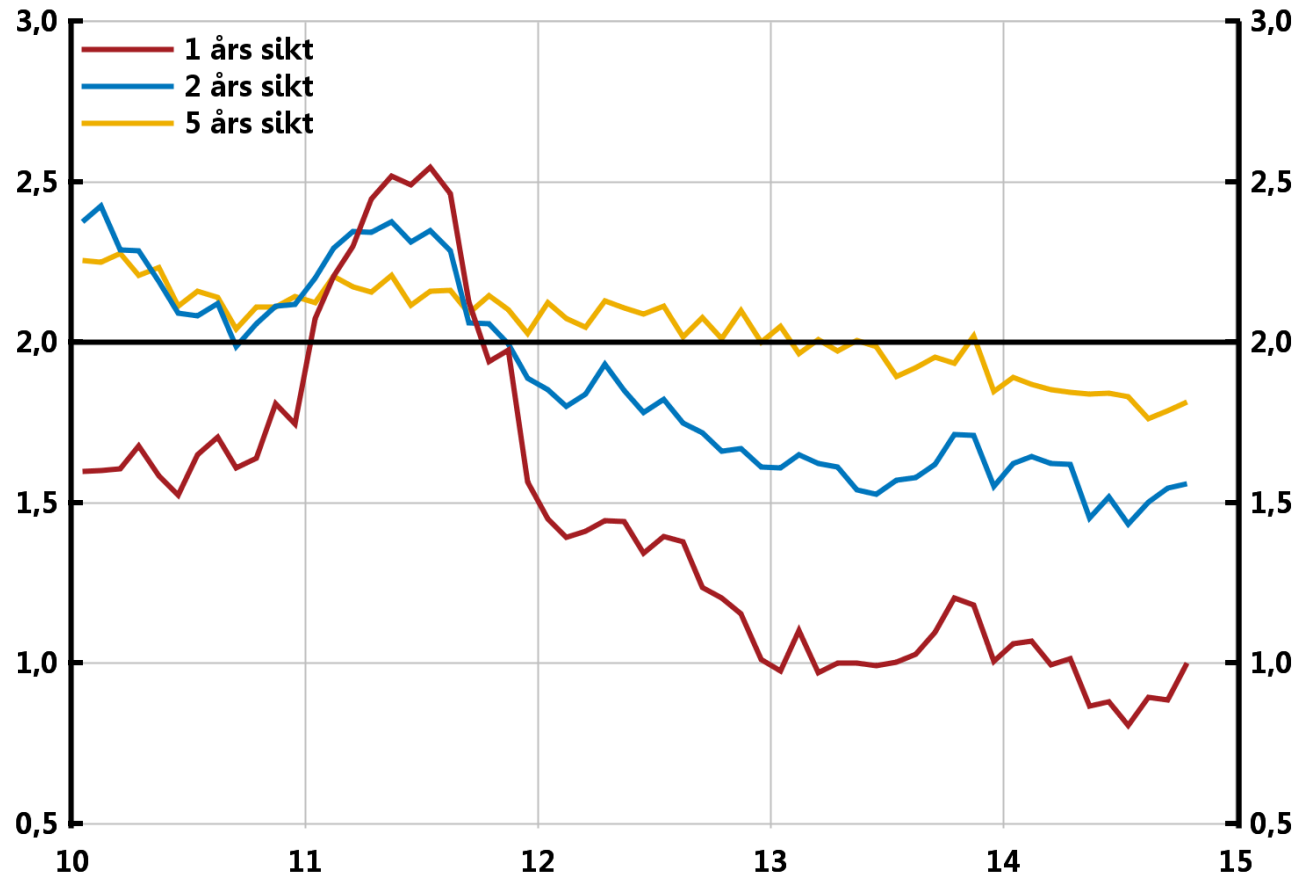
Employment rate



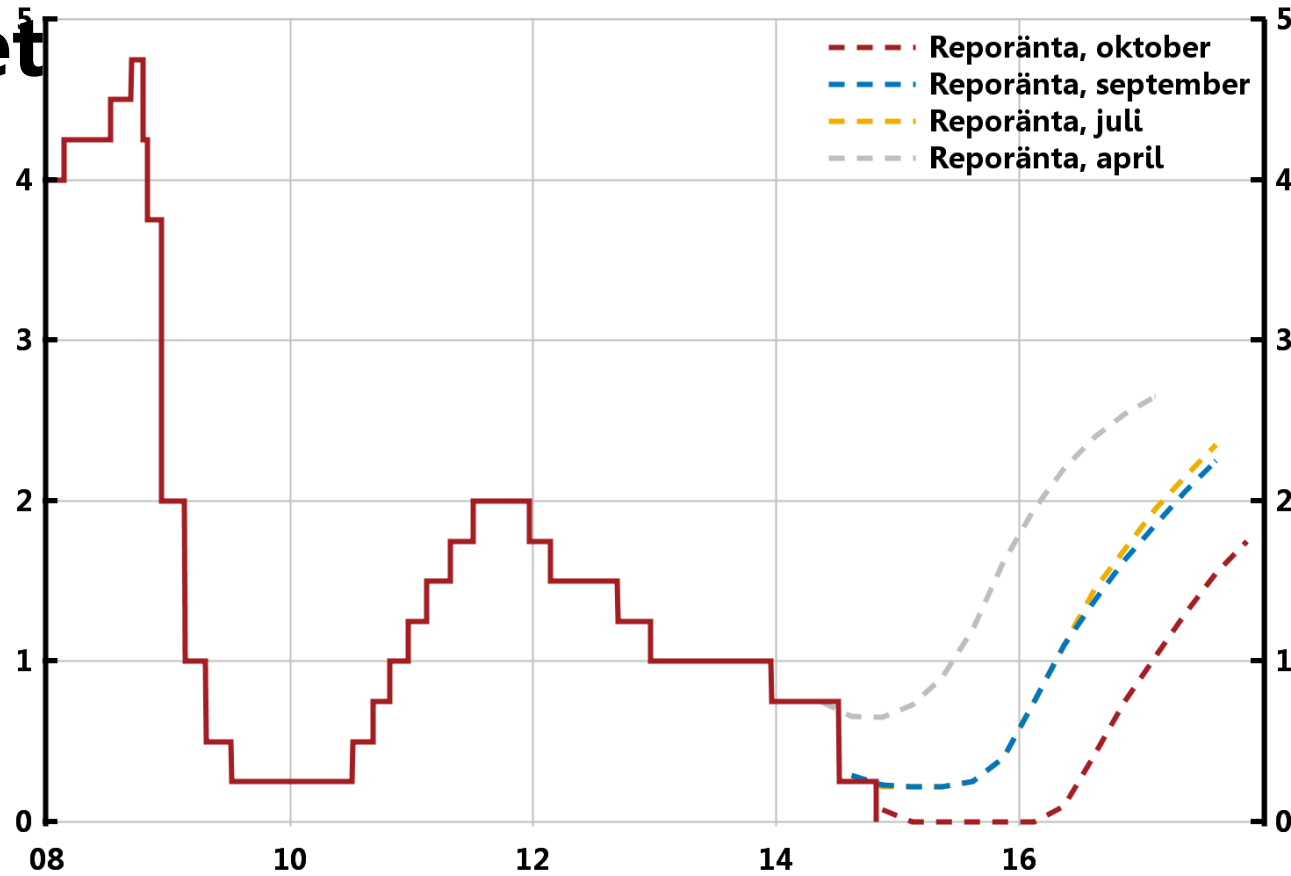
Unemployment



Important to have firmly-anchored inflation expectations



Low repo rate for a long time so inflation can rise towards the target



Monetary policy when the policy rate is zero



- The low repo rate and the repo-rate path are deemed to be enough for inflation to rise towards the target.
- The repo rate may be held low even longer
- Possibility that further measures will be taken



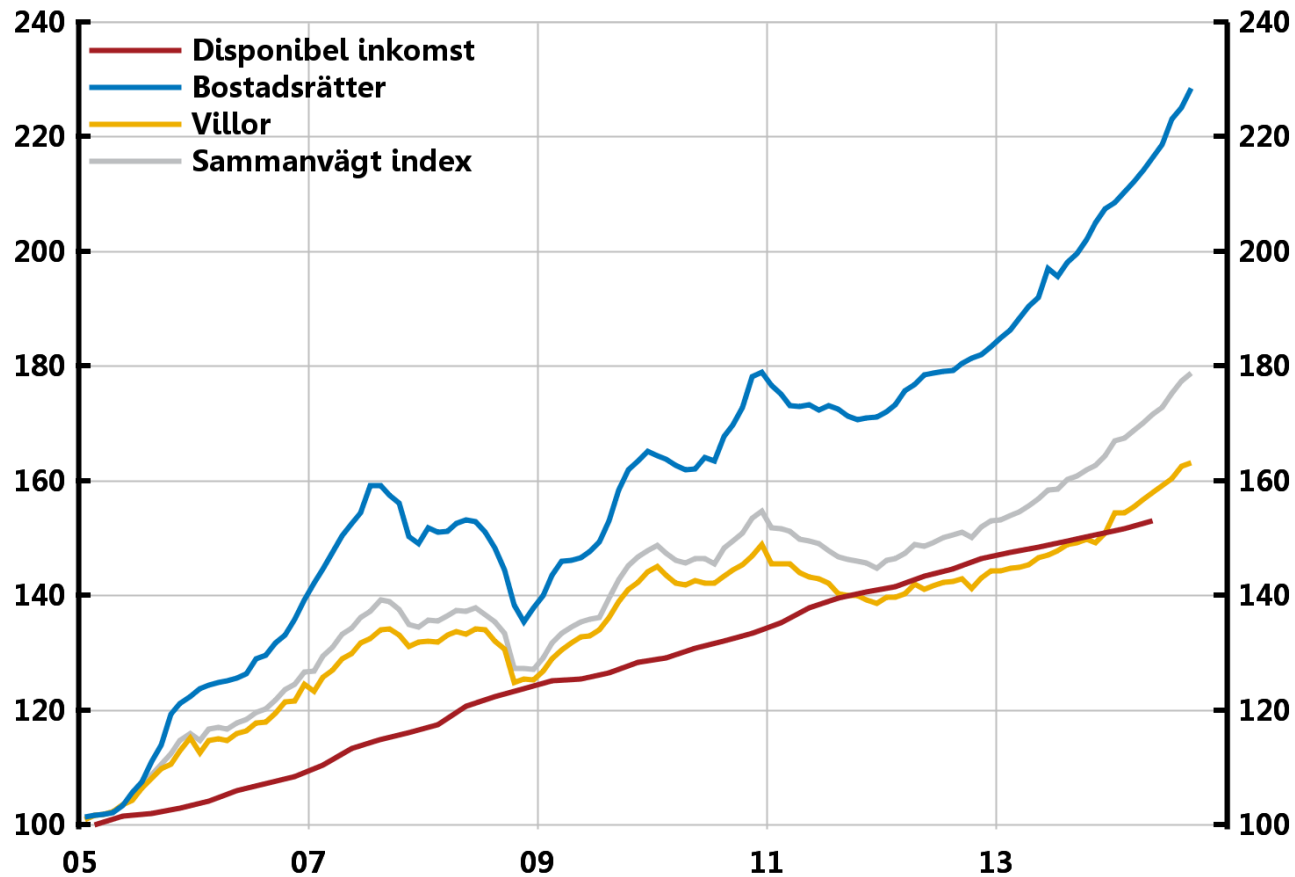
Risks associated with household indebtedness must be managed



- A long period of low repo rates will contribute to higher inflation
- But can simultaneously increase risks in the economy
- Measures in other policy areas needed

Rising prices, particularly on tenant-owned apartments

Index

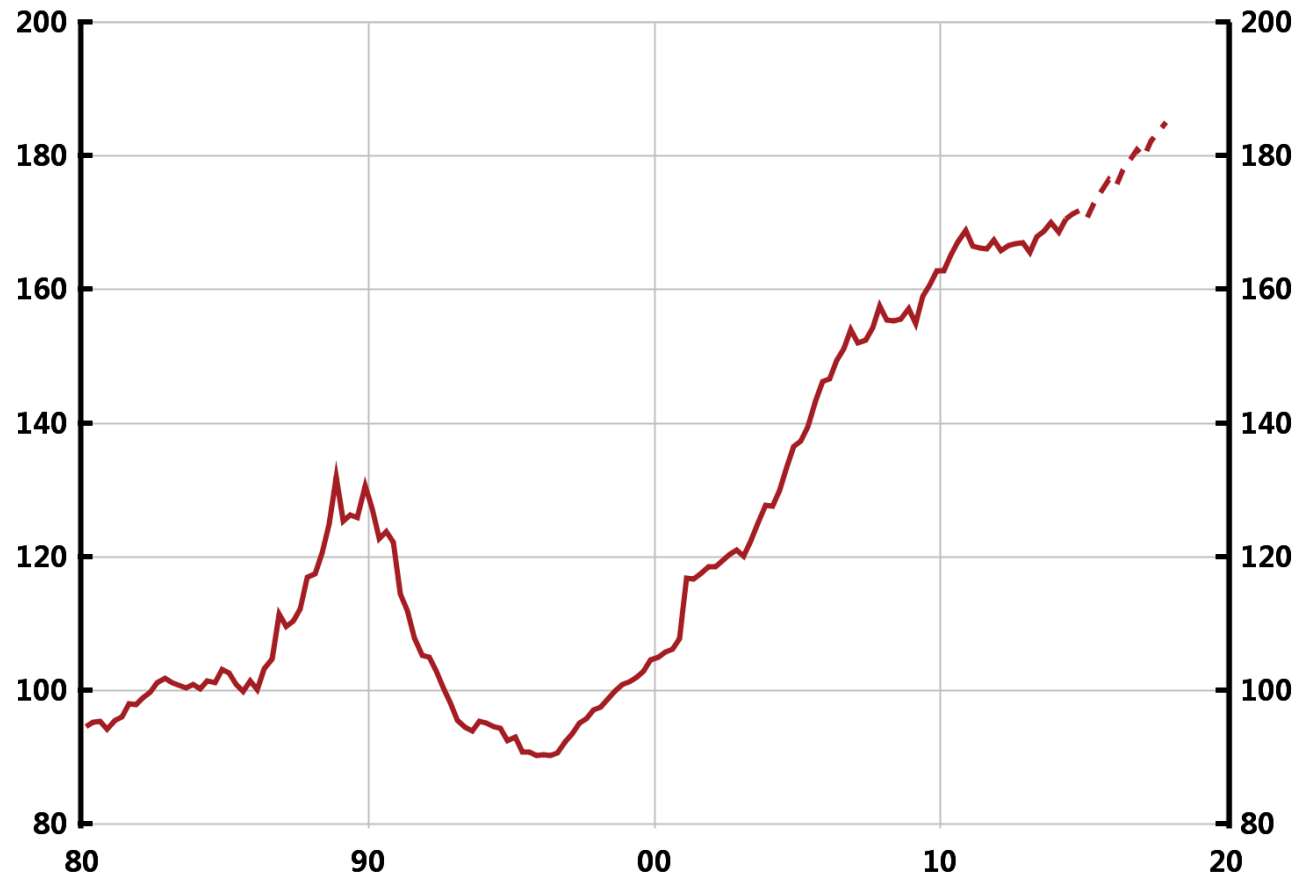


Note. Disposable income is quarterly data, housing prices are monthly data. Index, January 2005 (Q1 2005) = 100

Sources: Valueguard, Statistics Sweden and the Riksbank

Household saving ratio is high

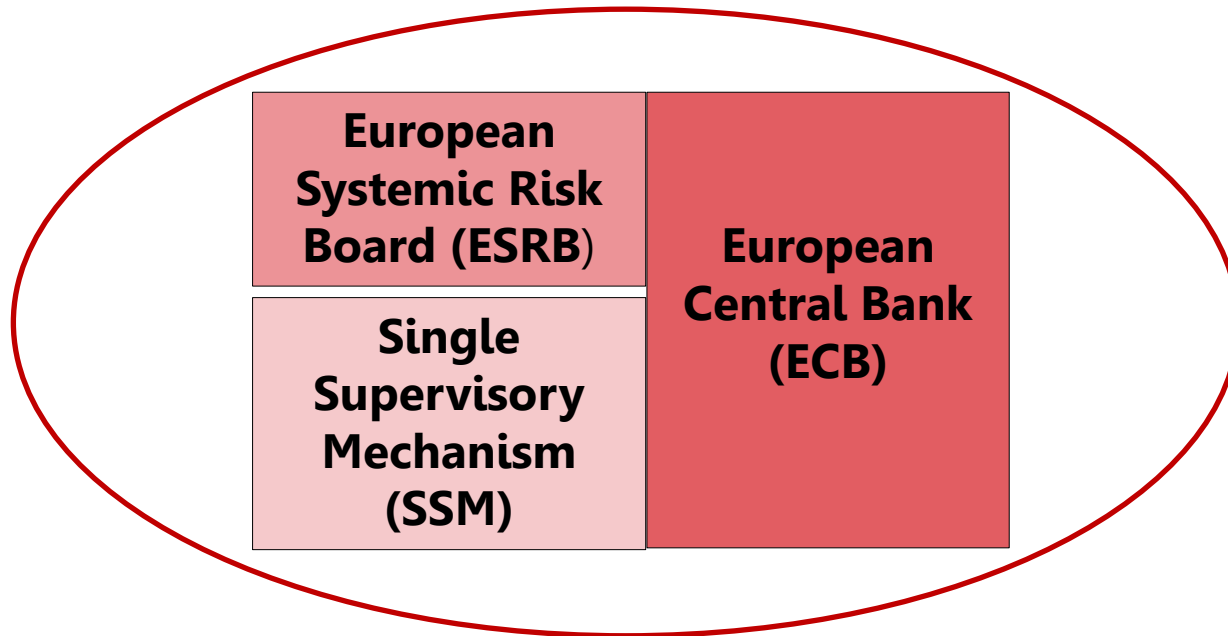
Household debt as a percentage of disposable income





Financial stability and
macroprudential
policy

Macroprudential policy: A new policy area is emerging

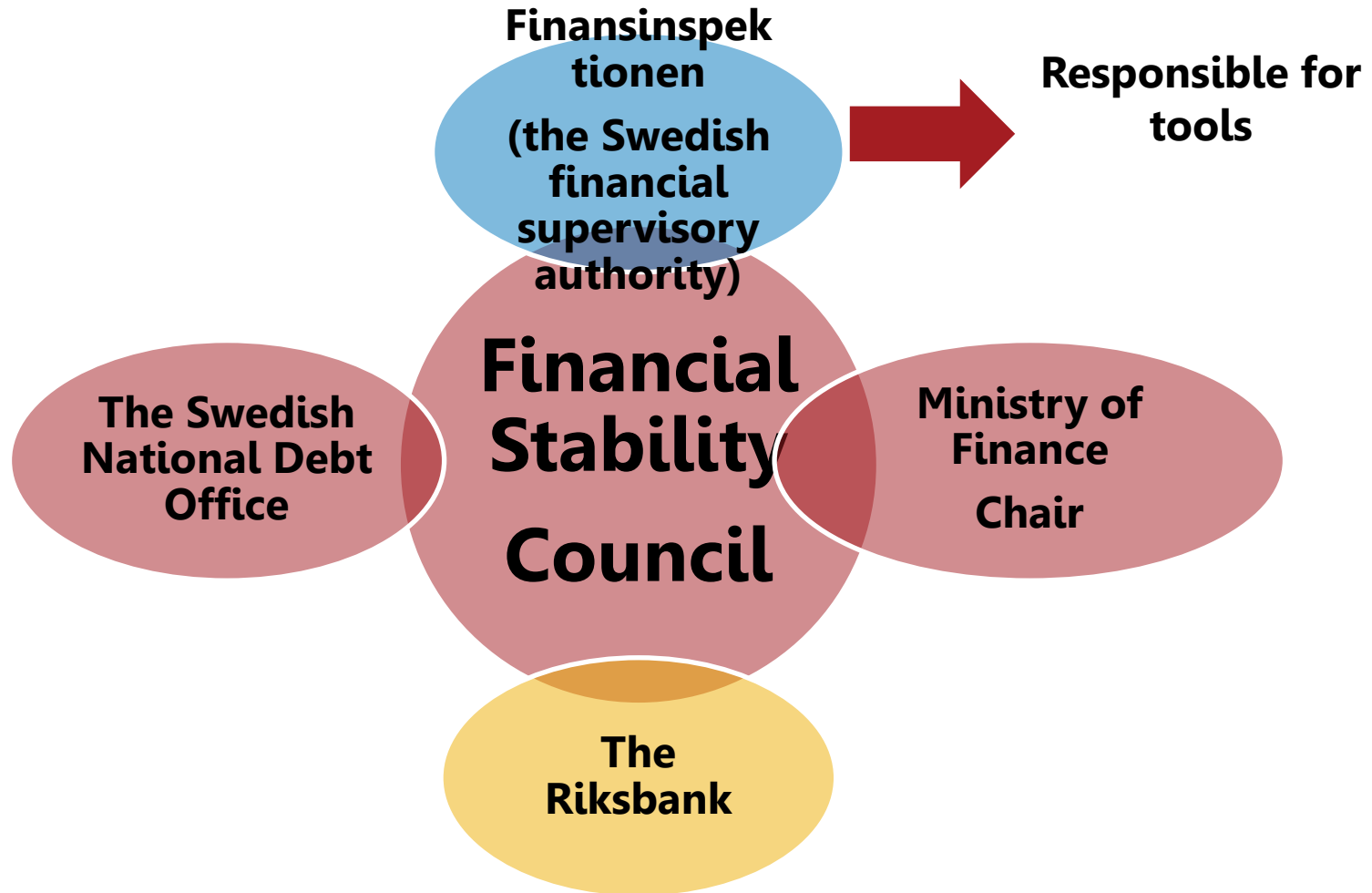


**European Banking
Authority (EBA)**

**European Insurance and
Occupational Pensions
Authority (EIOPA)**

**European Securities
and Markets
Authority (ESMA)**

In Sweden, Finansinspektionen is responsible for the macroprudential policy tools



Macroprudential policy tools

- Macroprudential policy tools aim to limit systemic risk...
 - Strengthen resilience among the banks
 - Counteract the build-up of risk, e.g. too rapid credit expansion
- ...but can also have effects on the macro economy, largely through the same channels as the repo rate

Examples of macroprudential policy tools



- Structural capital adequacy requirements
 - Countercyclical capital requirements
 - Sectoral-capital requirements/risk weights
 - Tools to govern liquidity
 - Mortgage cap: LTV (Loan to value), LTI (Loan to income)
 - Amortisation
-

How to manage the risks in Sweden?

- Monetary policy must now focus on bringing up the low inflation
 - The risks linked to high household debt must be managed by other policy areas
 - Better amortisation culture
 - Longer fixed-interest periods?
 - Reduced tax deductions?
 - Mortgage cap supplemented with LTI?
 - ...
-



Thank you!