



The economic situation and monetary policy

BNP Paribas
Stockholm

November 20, 2014

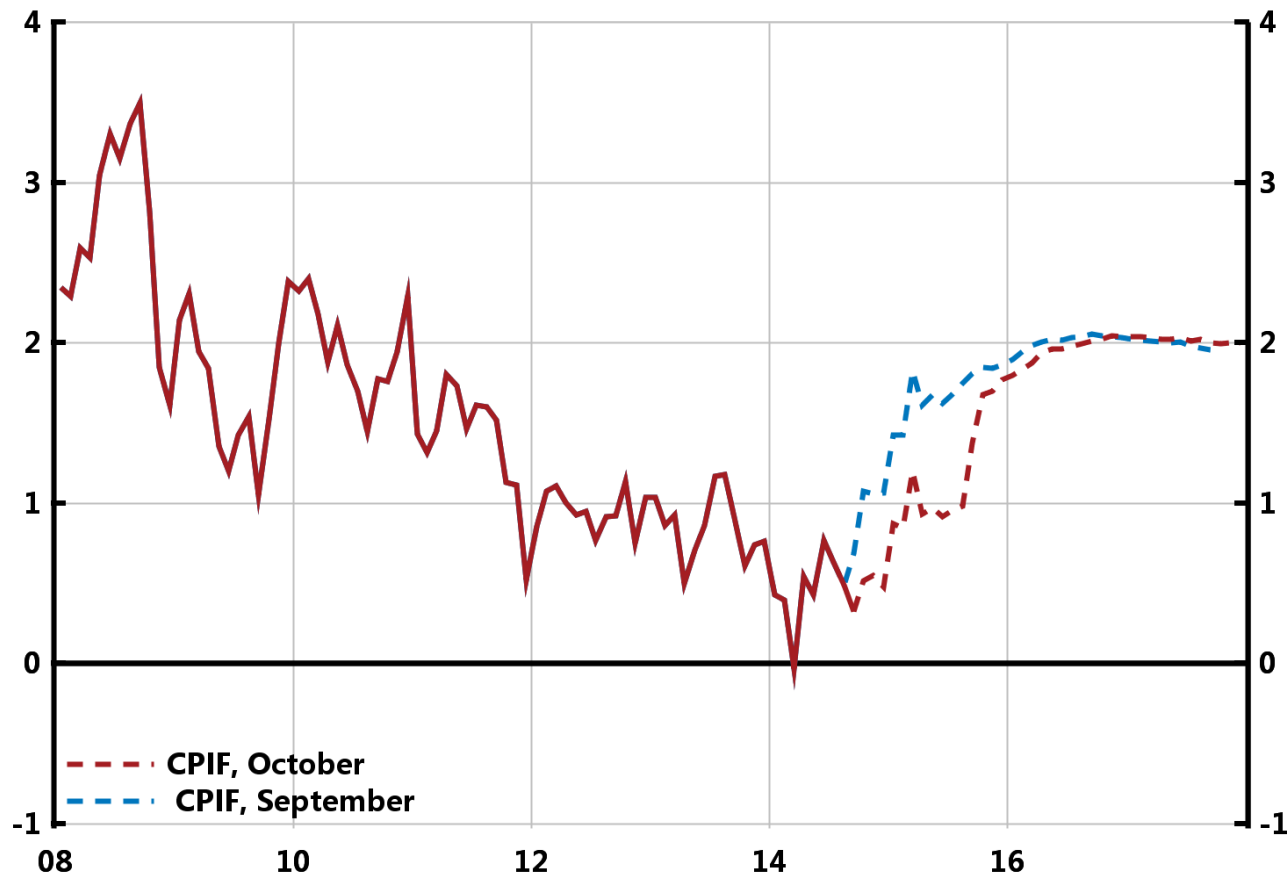
Martin Flodén
Deputy Governor

**Economic activity improving
but inflation is too low**

Zero repo rate until mid-2016

Low inflation in Sweden

CPIF, annual percentage change

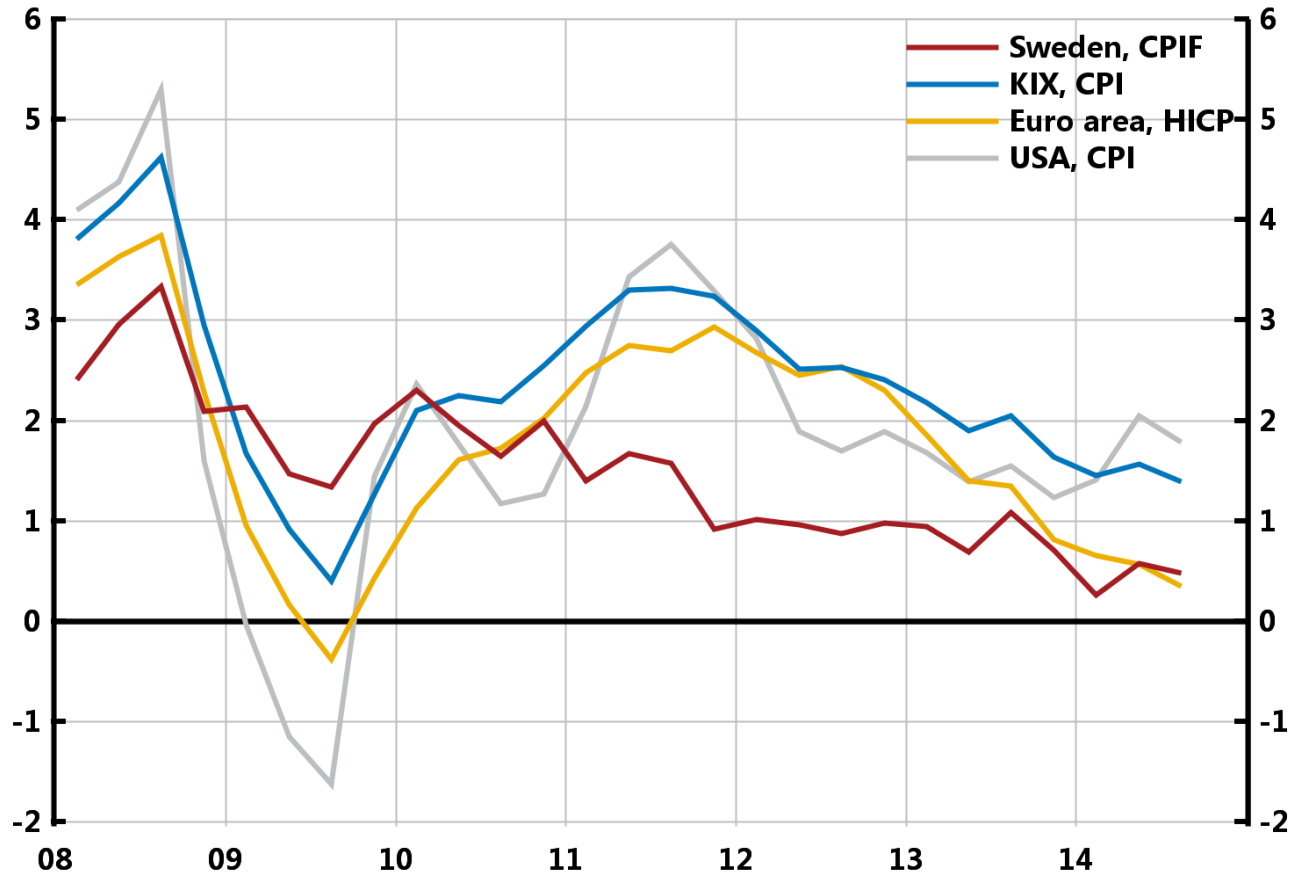


Note: The CPIF is the CPI with a fixed mortgage rate.

Sources: Statistics Sweden and the Riksbank

Inflation low abroad too

Percentage change

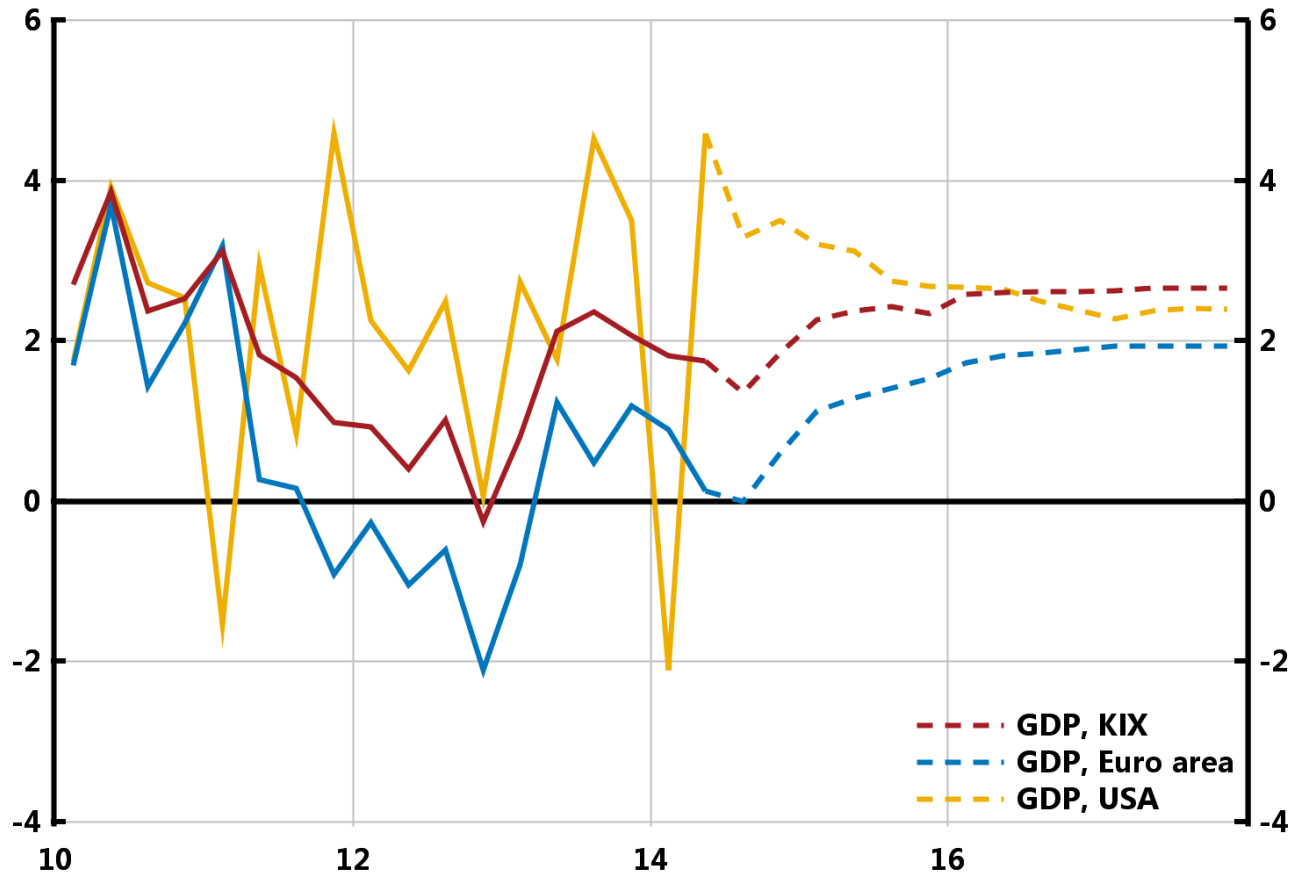


Note: Euro area refers to HICP and USA refers to CPI. KIX is an aggregate of the countries that are important to Sweden's international transactions.

Sources: Bureau of labour statistics, Eurostat, national sources and Statistics Sweden

Other countries recovering – but slowly and out of step

Quarterly changes in per cent

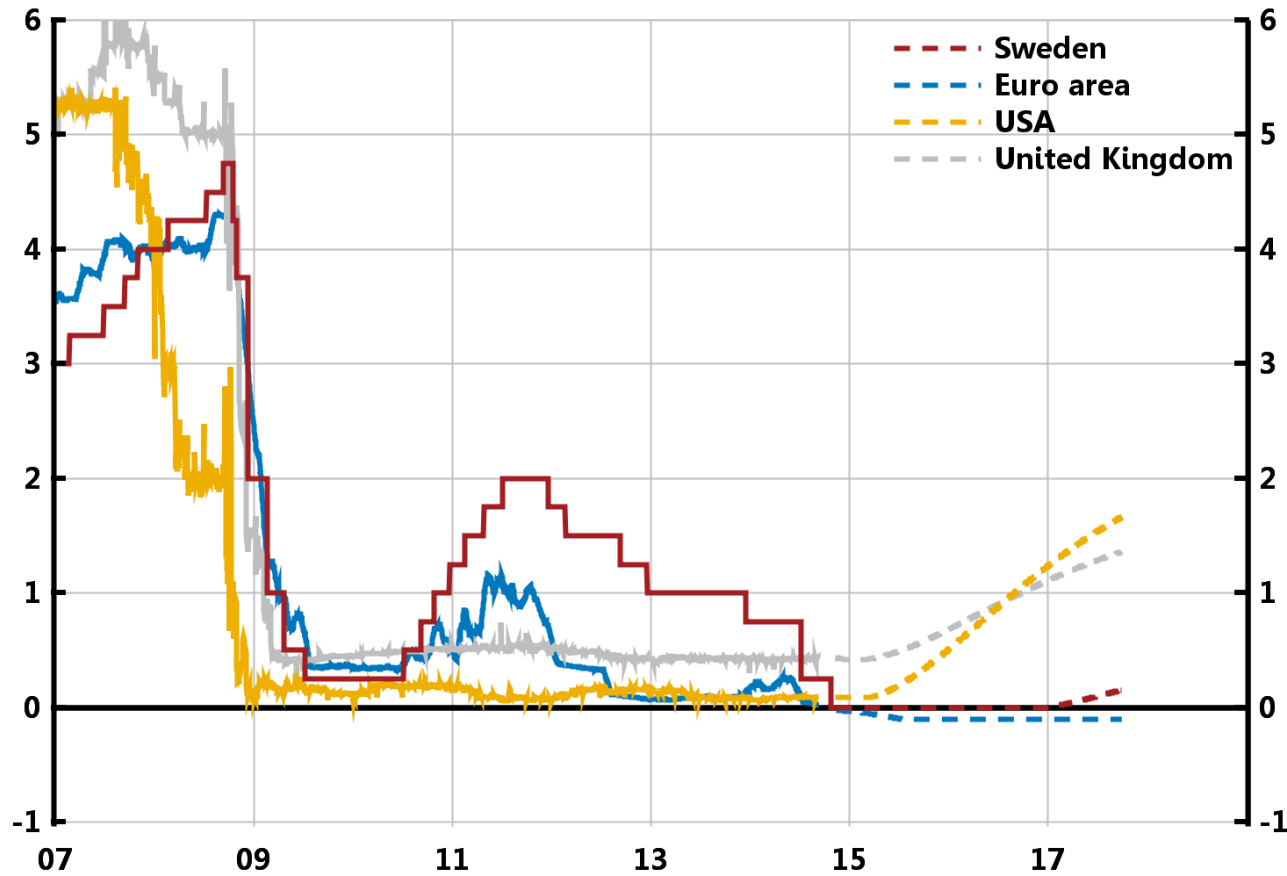


Note: Quarterly changes in per cent calculated as annual rate, seasonally-adjusted data. The KIX is an aggregate of the countries that are important to Sweden's international transactions. Forecasts from PPR October.

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

Monetary policy also out of step...

Policy rate, per cent

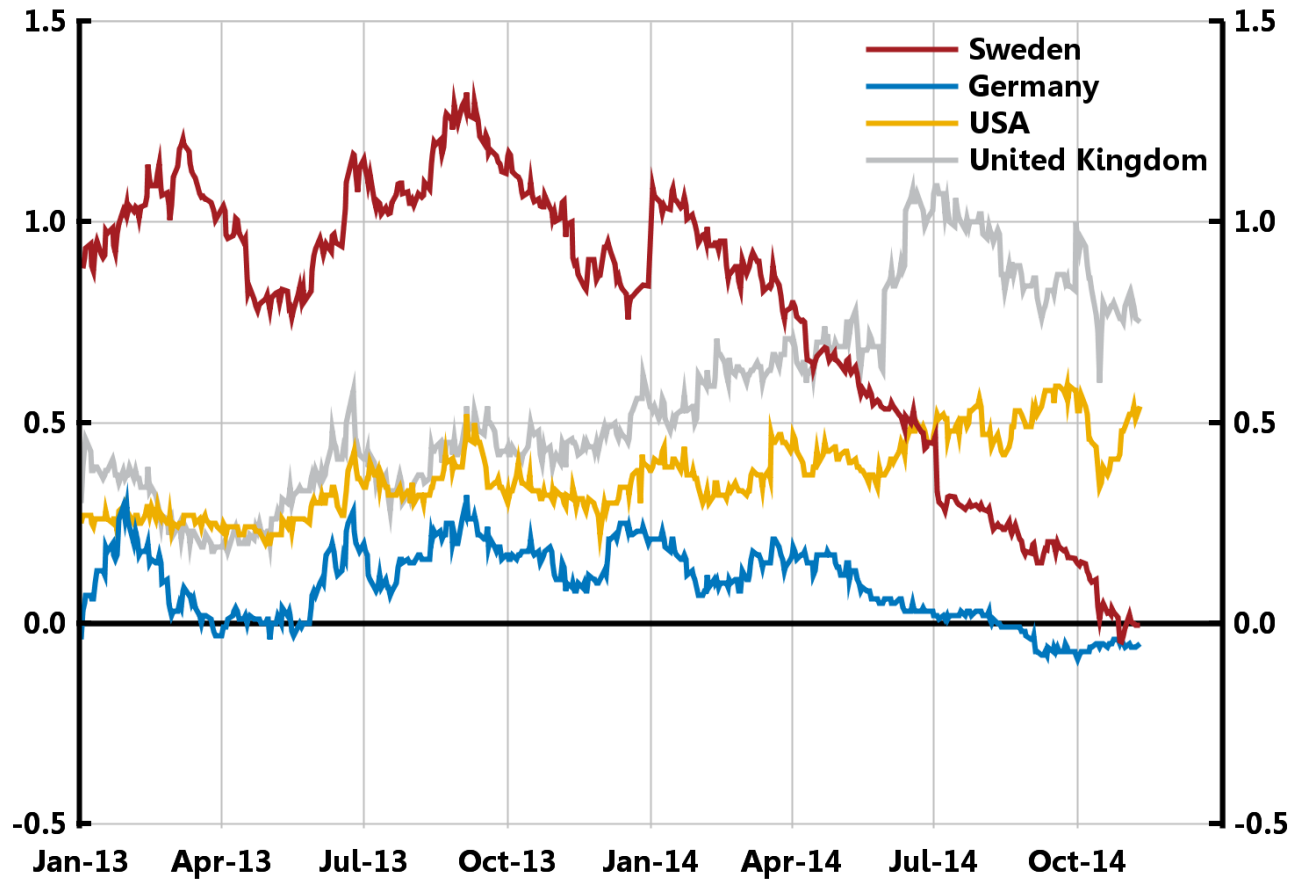


Note: Lines refer to future rates estimated November 11 and broken lines refer to before the repo-rate decision in October.

Sources: Reuters and the Riksbank

...which gives increasing spreads

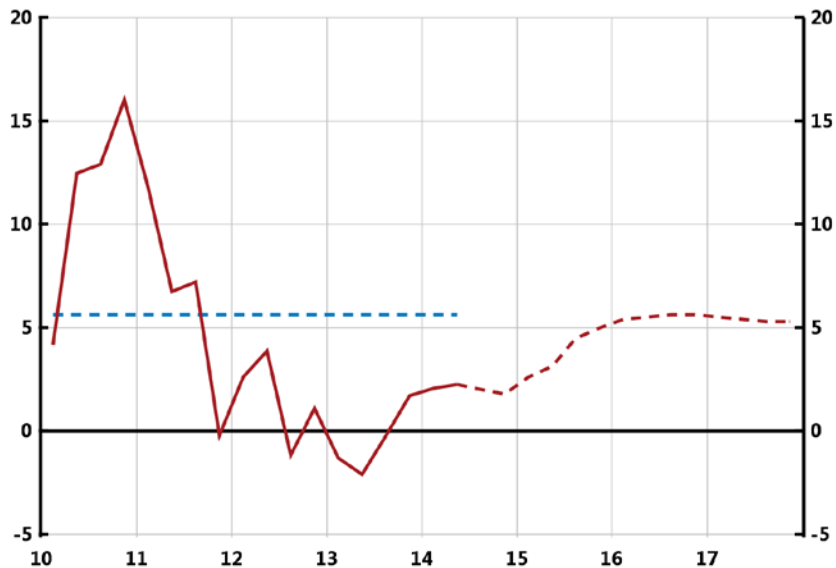
2-year government bonds, per cent



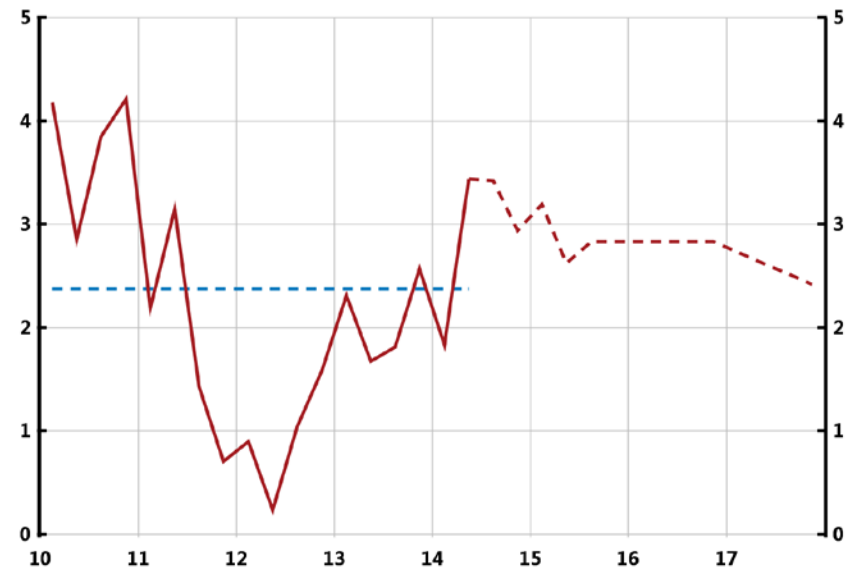
Weak exports, but strong households in Sweden

Annual percentage change

Exports



Consumption



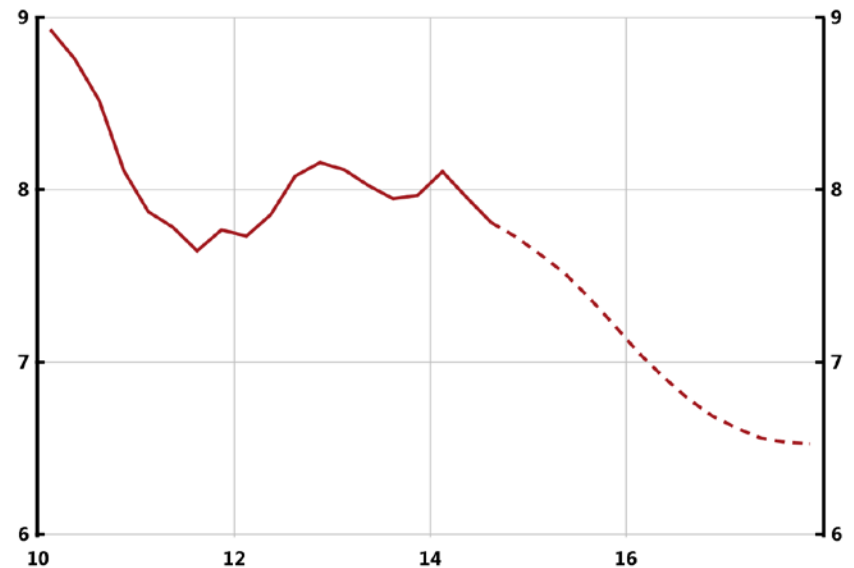
Continued labour market improvement

Per cent

Employment rate



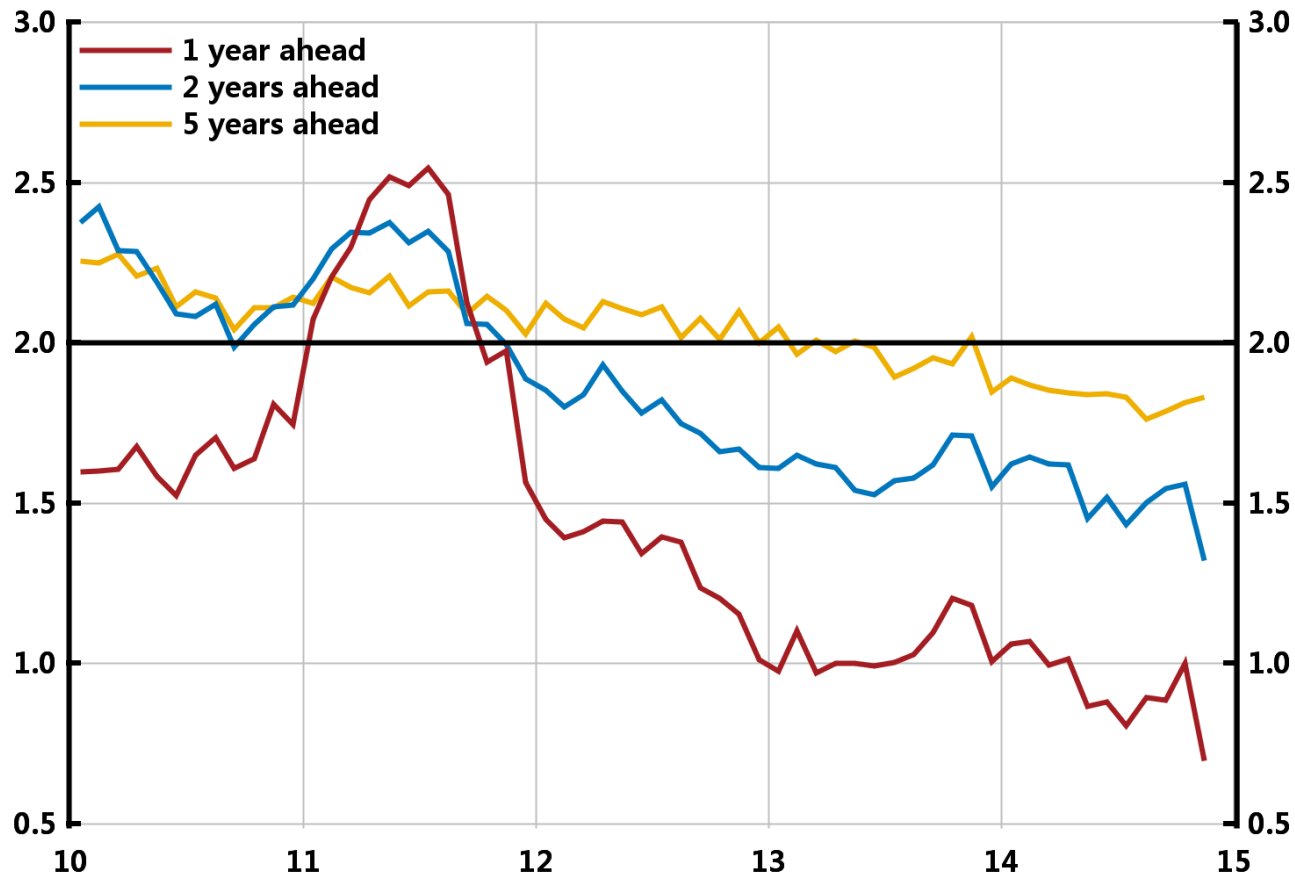
Unemployment rate



Important to have firmly-anchored inflation expectations

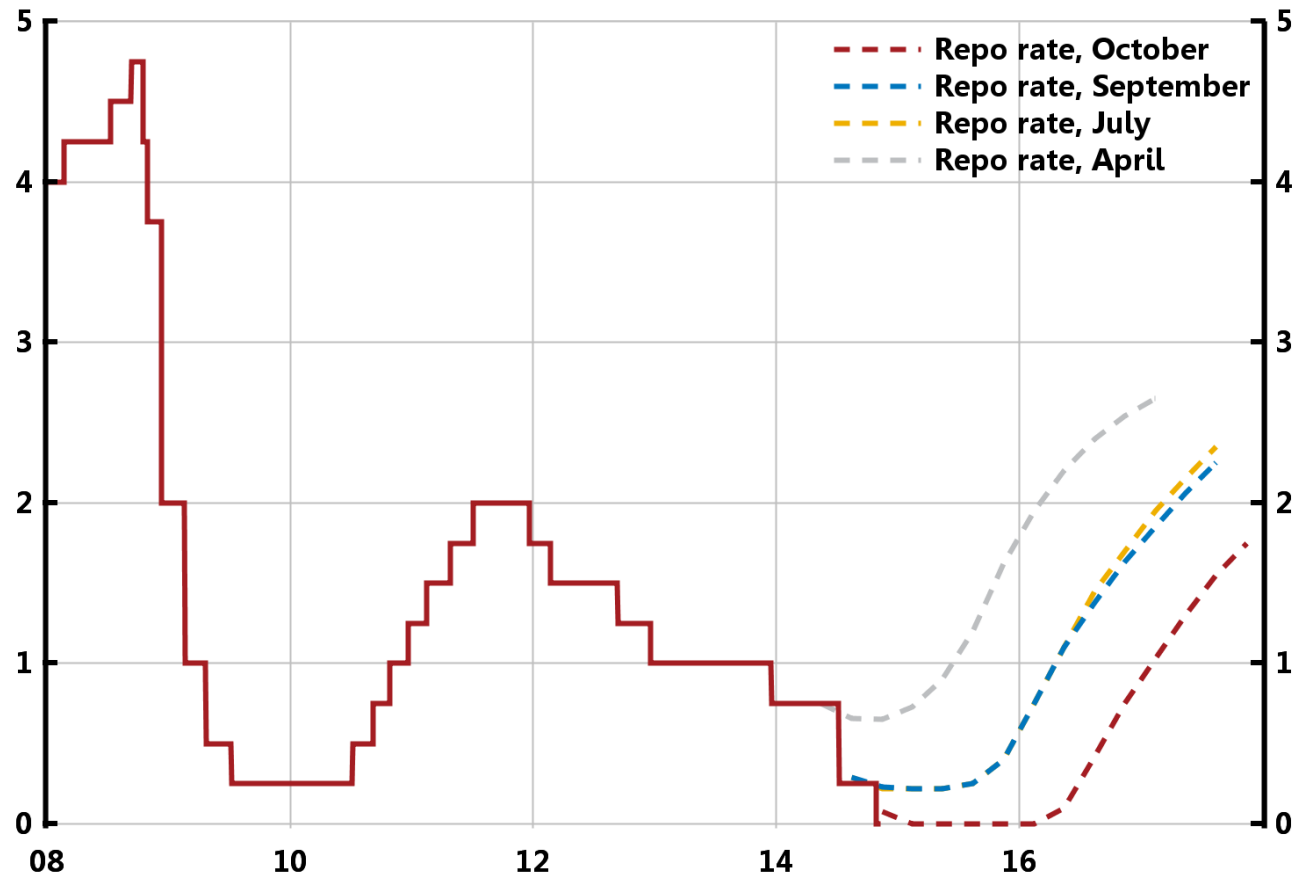


Per cent



Low repo rate over a long period of time

Per cent



Monetary policy when the interest rate is zero

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

Sweden: my summary

Problems

- High household debt
 - Little amortisation
 - Tax incentives
- Housing
 - Rising prices
 - Rent control
 - Low construction
- Mortgage markets
 - Adjustable rates
 - Short, market-based, funding

Mitigating factors

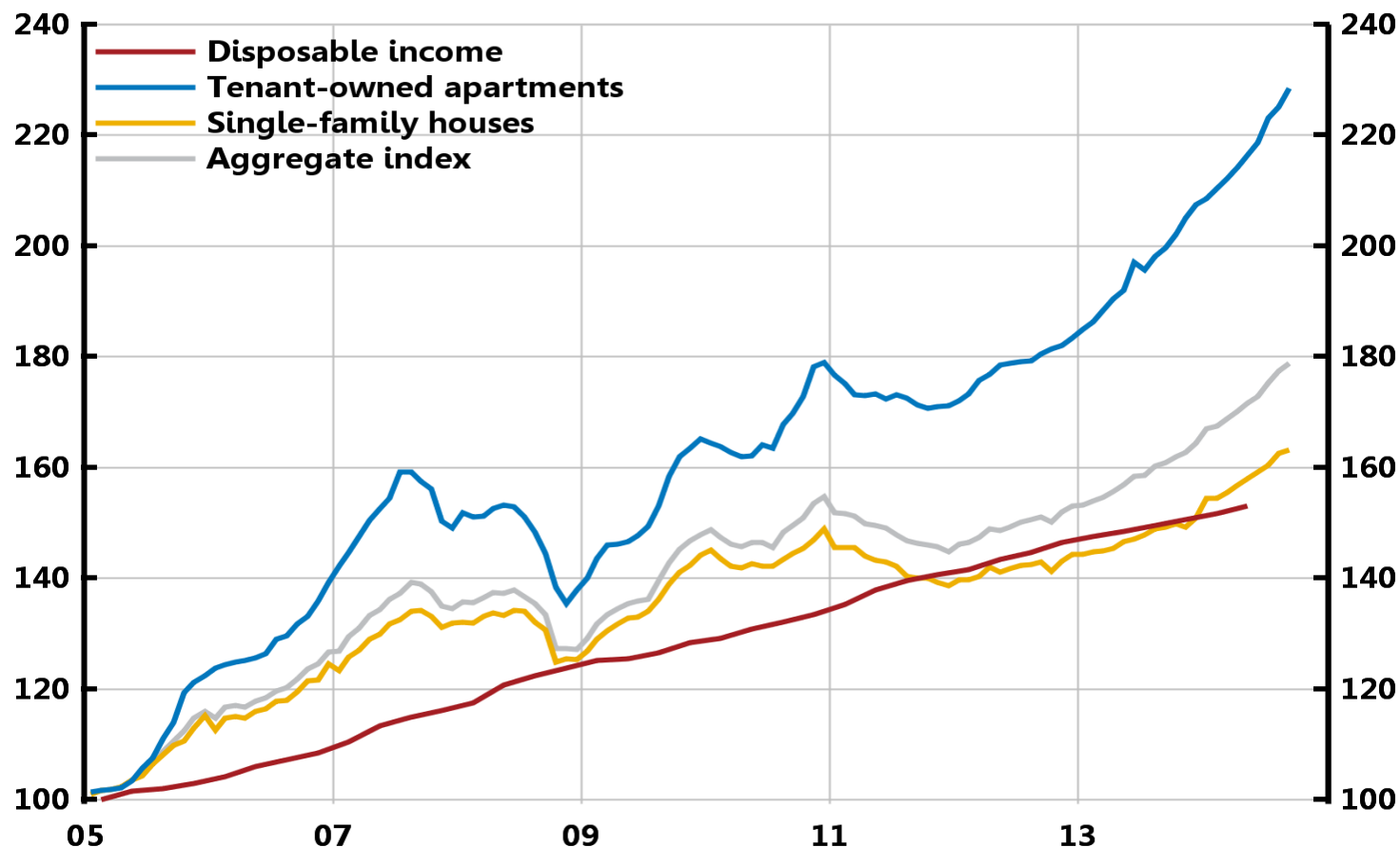
- High household savings
- Strong public finances
- Current account surplus
- Low construction



- Bloated balance sheets
 - Maturity mismatch
 - ...

Rising prices, particularly on tenant-owned apartments

Index, 2005 = 100, seasonally-adjusted data

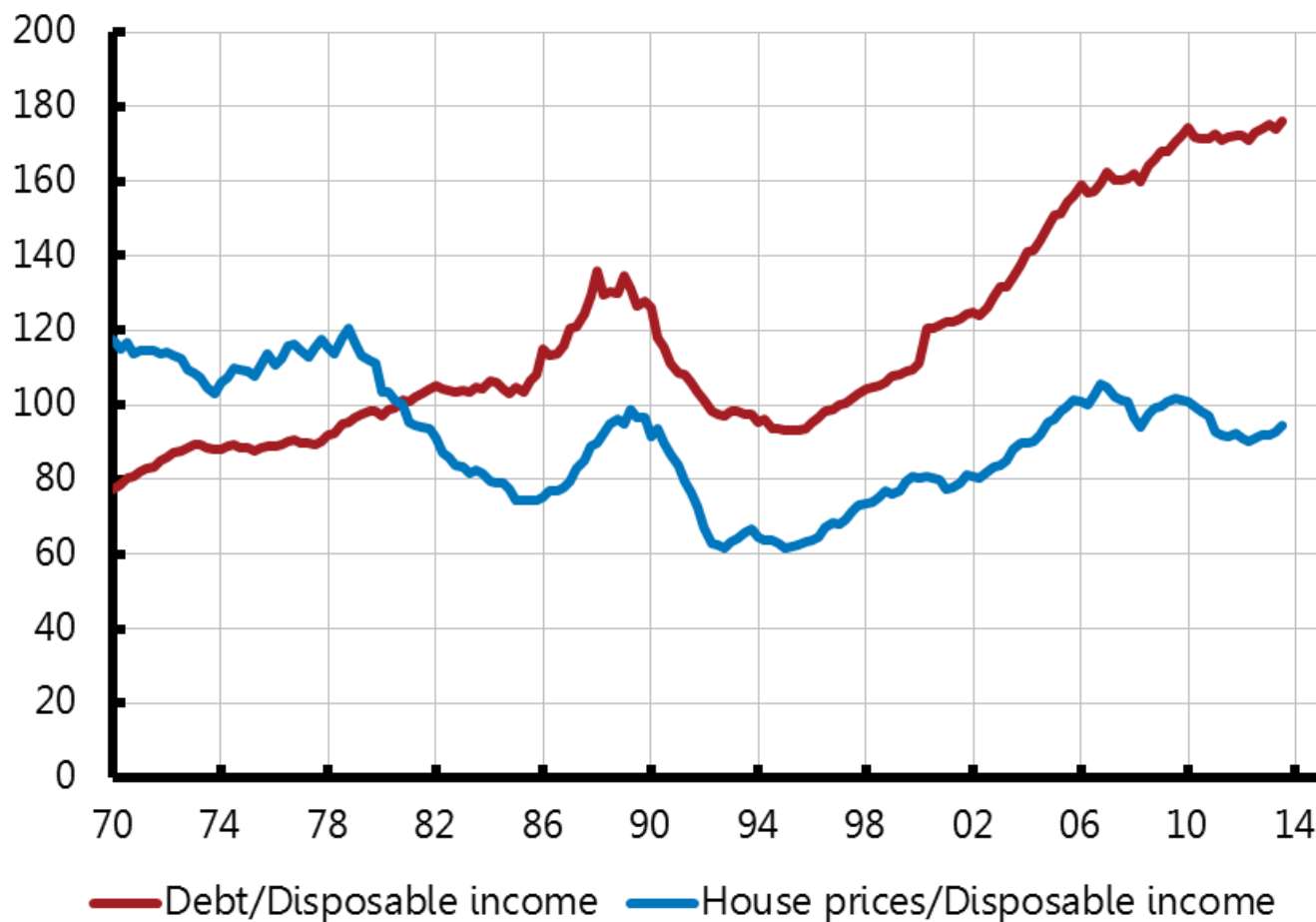


Note: Disposable income expressed as a four-quarter moving average.

Sources: Statistics Sweden, Valueguard and the Riksbank

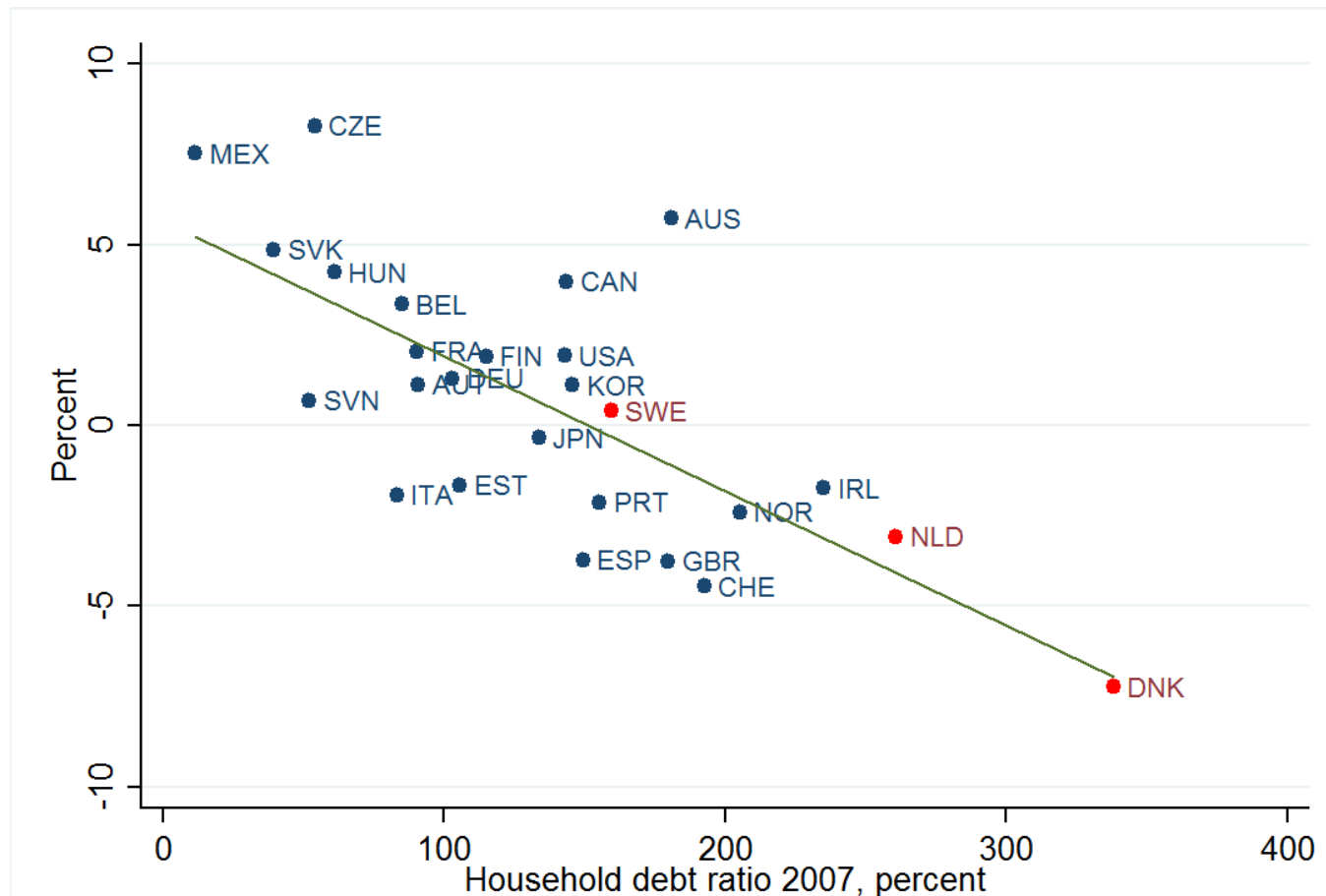
House prices and household debt are high and rising

Per cent, Index 1981=100



Economies with high debt are more vulnerable to shocks

Consumption growth 2007-2012, adjusted for other contributing factors

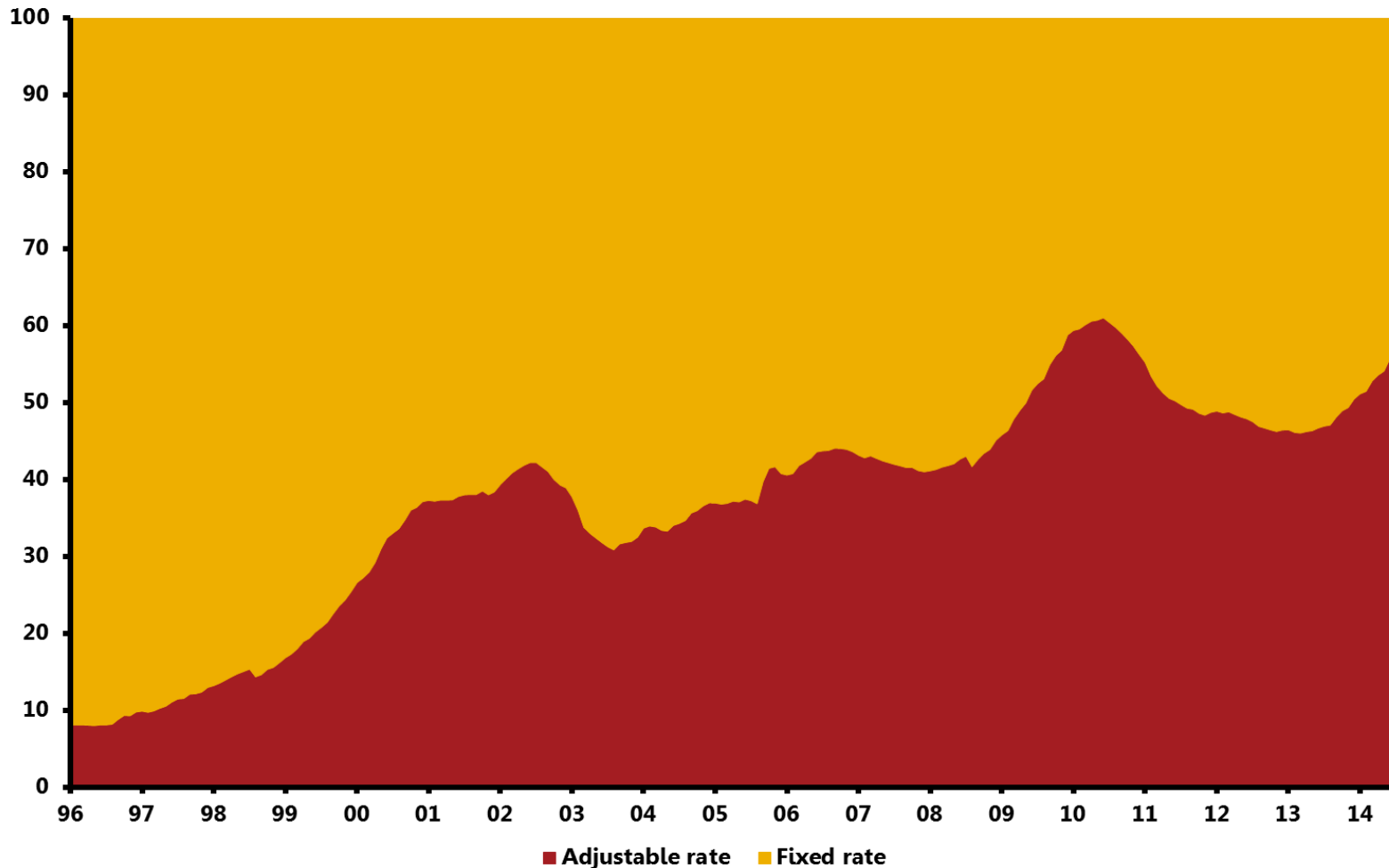


Note: Consumption growth has been adjusted for the CA balance, debt growth and consumption growth prior to 2007

Source: Flodén, M. (2014), "Did Household Debt Matter in the Great Recession?"

A large proportion of mortgages have adjustable interest rates

Per cent

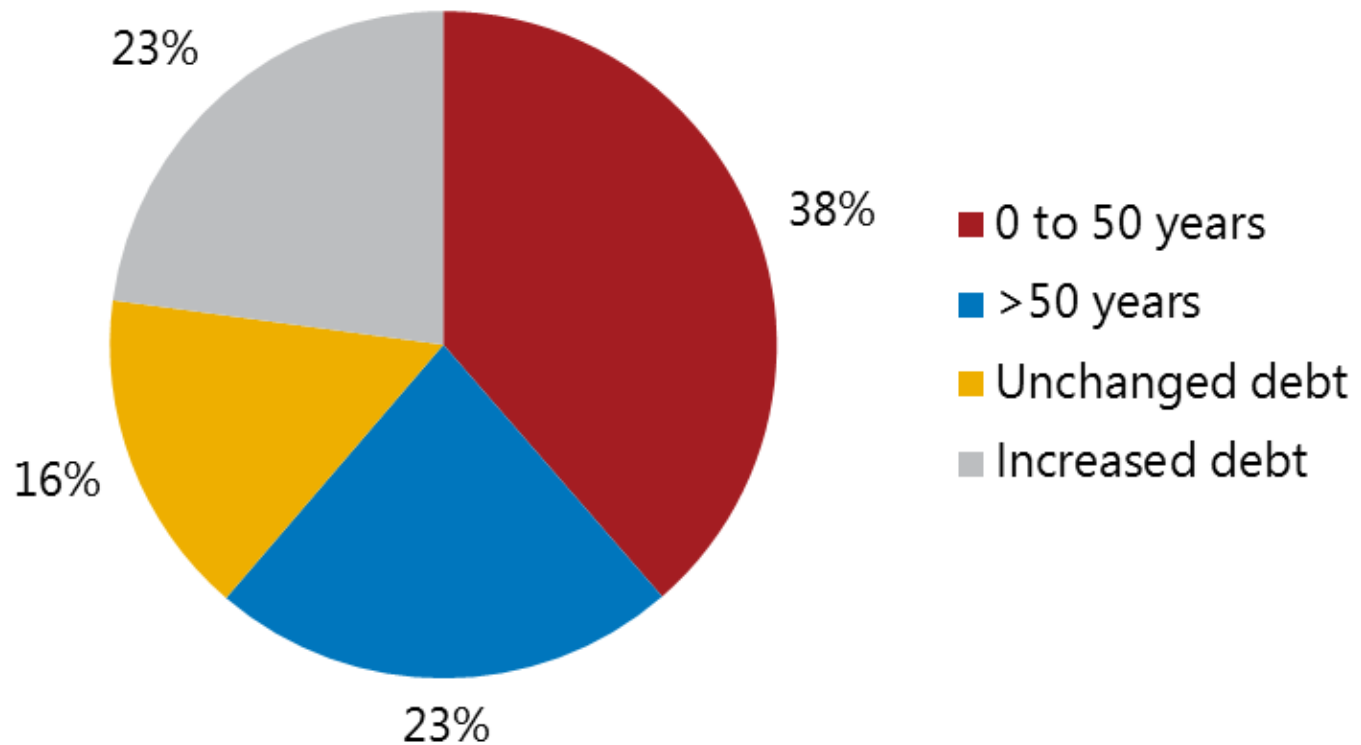


Note: Per cent, in stock of mortgages. Adjustable rate refers to mortgages with interest-rate fixation of 3 months or shorter.

Sources: Statistics Sweden and the Riksbank

Little amortisation

Percentages

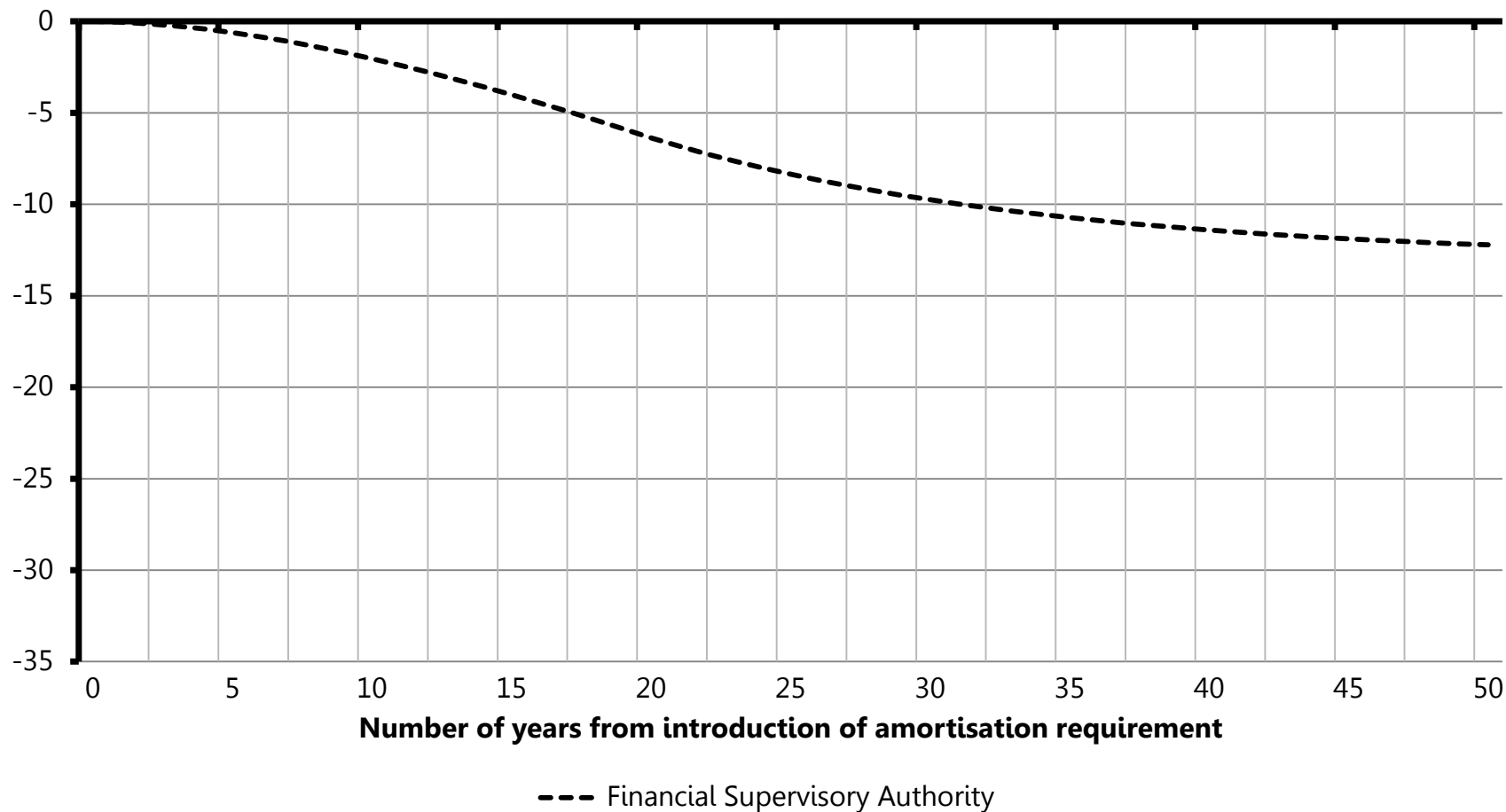


Amortisation: the FSA's proposal

- Financial Supervisory Authority proposed new amortisation requirements on November 11
 - Applies to new mortgages only
 - If $70\% < LTV < 85\%$ → amortise 2% of the mortgage
 - If $50\% < LTV < 70\%$ → amortise 1% of the mortgage
 - If $LTV < 50\%$ → no amortisation requirement
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The effects of different amortisation requirements on the debt ratio

Percentage points deviation from a base scenario



The way forward?

- Main objective: prevent unsustainable increase in household debt
- Policy action needed now
 - But this will be a gradual process
 - Several measures will be needed



The way forward?

- Amortisation
 - Interest-rate deductability?
 - Loan-to-value ceiling complemented by loan-to-income ceiling?
 - Increase the proportion of fixed rate mortgages?
 - Bank funding, longer maturity?
 - Supply-side measures to increase the supply of housing
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