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■ Developments in the Swedish economy

Deputy Governor Lars Nyberg spoke today to the Swedish Shareholders' Association about the Riksbank and the current economic situation.

"As you know, the objective of monetary policy in Sweden is to maintain price stability, which the Riksbank has defined as keeping the rate of change of the CPI at 2 per cent, with a permitted deviation of +/- 1 percentage point. To fulfil this objective, it is important to have credibility for monetary policy. This requires openness and clarity from our side. Thus, an important part of our activities is to explain monetary policy and the inflation assessment on which it is based. At the beginning of February, the Riksbank's Executive Board will be meeting to discuss afresh recent economic developments, their implications for the inflation outlook and thereby the conduct of monetary policy. It is primarily my views in relation to these matters that I will discuss today," said Mr Nyberg.

"New data have largely confirmed the picture of international and domestic economic activity that was presented in the December Inflation Report, and the recovery appears increasingly stable. Developments in the financial markets are also indicating a continued economic upswing. As regards the US economy, the signals have been generally positive both concerning the household and business sectors. The dollar has continued to weaken, however, which can be assumed to be due to developments in the current account deficit, coupled with a growing deficit in the federal budget. However, the depreciation has occurred from a level that was generally judged to be much too high. In the euro area, new data essentially supports the picture presented in the Inflation Report. However, the strong performance of the euro could result in exports being weaker than expected, and thereby also growth," said Mr Nyberg.

"In Sweden, outcomes for the third quarter 2003 indicate that the economic upswing is continuing. This is also suggested by other indicators, such as retail sales growth and the business tendency surveys of the National Institute of Economic Research. However, the picture is not yet entirely unambiguous. Industrial production has been relatively weak, and new orders have declined.

Moreover, new estimates of the public finances indicate that public consumption this year may be somewhat weaker than assumed in December. This suggests weak employment growth in the public sector while a rise in private sector employment cannot yet be discerned. Inflation so far has been largely as expected, marginally somewhat weaker at the end of last year. The weak labour market conditions have been reflected in unexpectedly robust productivity growth. This may have contributed to the somewhat more favourable inflation situation. Whether the strong productivity growth will continue for a longer period is still uncertain, however, but developments so far give reason for a somewhat more optimistic view of Swedish supply conditions. It remains to be seen what the overall effect of all this will be on the outcome of the wage bargaining round, but as I see it, there is presently reason to be cautiously optimistic," said Mr Nyberg.

"The debt burden of Swedish households has grown throughout the economic slowdown. Low interest rates and rising disposable incomes have led households to gradually increase their borrowing, and their debts are now on a par with those at the beginning of the 1990s, prior to the big property crisis. Moreover, the trend towards higher borrowing appears to be continuing. House prices have also risen, despite the economic slowdown. We share these experiences with many other countries where inflation has fallen and stabilised at a low level. It is possible that households' increased propensity to borrow is a natural adjustment to an environment with low inflation and low interest rates. The difference with the years before the crisis and the introduction of the inflation targeting regime is that interest costs in relation to incomes are lower, which makes it possible to bear the high levels of debt. Nonetheless, there is reason to keep a vigilant eye on developments. In any case, the higher debt burden has made households more sensitive to rising interest rates and falling house prices," said Mr Nyberg.

"All in all, developments in the real economy both in Sweden and abroad have been roughly in line with our expectations in December. Labour market growth has continued to be weak, however. The low inflation means that even small increases in nominal wages could lead to higher real wages, which as I see it, has reduced the risk of the wage bargaining round disturbing the inflation outlook. Moreover, productivity data have continued to be unexpectedly positive, which could probably enable the economic upswing to be more prolonged without it giving rise to inflation. I also believe that we have reason to be a little less concerned about high electricity prices spreading and permanently affecting prices in other sectors of the economy. All of these factors indicate that inflationary pressure will be somewhat more subdued than we forecast in December. Consequently, this could suggest that an additional cut in the repo rate is possible, especially as inflation prospects were already fairly benign in December. It is true that we are approaching an economic recovery that sooner or later will require monetary policy to be tightened again, but there are no indications that the upswing would be so robust and quick that it would speak against a looser monetary policy at present. This is the situation as I see it ahead of the Executive Board meeting on 5 February. As usual, we will of course make our decision next week in the light of all the information that is available at the time," concluded Mr Nyberg.