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CONTACT: Tomas Lundberg, Press Officer, tel. +46-8-787 02 15



SVERIGES RIKSBANK
SE-103 37 Stockholm
(Brunkebergstorg 11)

Tel +46 8 787 00 00
Fax +46 8 21 05 31
registratorn@riksbank.se
www.riksbank.se

■ Inflation lower than expected

Deputy Governor Irma Rosenberg spoke today at SBAB's Annual General Meeting on the subject of household indebtedness and price developments in the housing market. Mrs Rosenberg commented also on the economic situation and monetary policy.

Households' debt situation

"Household debt has increased steadily in recent years despite fluctuations in equity prices and weak economic activity. Meanwhile, house prices have continued to rise, even if there are significant regional differences. The discussion of Swedish households' indebtedness has been fuelled by developments in many other countries, such as the UK, the US and Australia where the build-up of debt has risen considerably more than here. This has raised the question of whether the situation is sustainable or whether there is a risk of households accumulating too much debt and of property price bubbles arising in various countries. The Riksbank monitors regularly households' ability to pay in order to be able to assess the stability of the financial system. Swedish household debt as a percentage of disposable income is indeed approaching the levels seen before the financial crisis at the beginning of the 1990s. But due to low interest rates, households' interest costs as a percentage of income have been more or less halved since then and are now at an historically low level," observed Mrs Rosenberg.

"It also appears that the rise in house prices can be fairly well explained by fundamental factors such as interest rates, incomes and new production in relation to the development in housing demand. This suggests that a house price bubble is not in the offing, at least not at national level. We don't currently envisage that the household sector as a whole will have any difficulties in meeting its obligations. Nor do we foresee any problems for the banks or the stability of the financial system. However, this does not mean that problems cannot arise for individual households when interest rates sooner or later begin to rise. Therefore, at today's low levels of interest rates it is especially important for borrowers to take



account of this in their estimates and to carefully consider how much debt they can bear," said Mrs Rosenberg.

"Household indebtedness is of course also significant for monetary policy decisions to the extent that they influence the inflation assessment. A rising debt ratio also increases households' sensitivity to changes in interest rates. The larger the proportion of loans that are taken at variable rates, the stronger this effect becomes. But the aim of repo rate changes is exactly to influence demand, which is sensitive to interest rates, and this is why we take account of these factors in our analyses and why we include them, for instance, in our forecasts of consumption," noted Mrs Rosenberg.

The economic situation and monetary policy

"Recent data have essentially confirmed the international outlook that we presented in December. But in some countries and regions the upswing appears to be proceeding faster than expected. This applies particularly to the US, but also to Asia, eastern and central Europe, and Latin America. Moreover, in the UK and Norway, both of which are important export markets for Sweden, growth has been unexpectedly robust. In the euro area, however, growth has been sluggish, and it seems in the period ahead that it will be somewhat weaker than we expected in December. International price pressure is low for manufactured goods. At the same time, commodity prices have soared. The fast growth in China is probably an important factor contributing to this," said Mrs Rosenberg.

"The economic upswing is also strengthening in Sweden, largely in line with the December forecast. However, the composition of growth appears to have been somewhat different than we expected in December. The pickup in investment has been postponed further but this has been countered by somewhat stronger private consumption and exports. There is reason to expect somewhat higher exports in the year ahead than forecast in the December Inflation Report. Furthermore, owing to somewhat stronger growth in disposable income, lower interest rates and rising asset prices, there is cause to be a little more optimistic about future consumption growth. At the same time, it is worth remembering that there appears to be plenty of unutilised resources initially. Even if economic activity should strengthen as anticipated, there will also be unutilised resources during the larger part of the forecast period," said Mrs Rosenberg.

"The labour market has been weaker than we expected in our December forecast. Consequently, wage costs are likely to rise slightly less than anticipated in December. The wage agreements that have recently been settled in industry and the retail trade sector are in line with this. Productivity growth has also been comparatively strong. Even if we believe that the rise in productivity can partly be explained by economic developments, there also appears to be more permanent aspects. One interpretation is that this partly can be due to previous investment in new technology also beginning to produce results outside the IT and telecommunication sectors. It is therefore likely that productivity may rise a little faster in the years ahead as well. As a result, unit labour costs could be a further bit lower.



■ We took some account of this in February, but since then the picture has become clearer and has strengthened," noted Mrs Rosenberg.

"The current low level of inflation is largely due to the fact that electricity prices have, as expected, fallen sharply. But in recent months inflation has been weaker than we predicted in December. This is due to a number of factors. Imported inflation has been weaker than anticipated, partly in the wake of the krona's appreciation in recent years but also as a result of continued low international price pressure. Domestic prices have also risen less than expected. It is likely that this is due in part to slightly slower increases in wage costs and to higher productivity growth than previously assumed. Lower cost pressure, both international and domestic, is also judged to contribute in the period ahead to a more subdued rise in inflation compared with the assessment in February. This implies that inflation will be well below target both one and two years ahead. Against this background I see room for clearly looser monetary policy," concluded Mrs Rosenberg.