



PRESS RELEASE

DATE 26 March 2004

NO. 15

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

■ Is a policy of wage solidarity compatible with the Riksbank's inflation target?

Deputy Governor Villy Bergström gave a speech today at the trade union day in Västerås.

"This year's wage bargaining rounds, which cover the greater part of the private sector and the entire central government sector, are in full swing. However, the wage agreements for the industrial sector have mostly been concluded now, which paves the way for stable bargaining. Payroll expenses account for 70 per cent of the value added in the economy and have vital significance for the development of costs and prices and thereby also for monetary policy. Wage bargaining rounds therefore entail a risk of wage agreements being signed at levels that are not compatible with the Riksbank's annual inflation target of two per cent. However, the fact that the central wage agreements in the industrial sector have been signed at moderate levels, together with factors such as the relatively slow recovery in the economy and the weak labour market imply that this will not be the case, although there is still some risk with the local wage bargaining. Recent statistics indicate there is some scope to conduct a more expansionary monetary policy and the outcome of the wage bargaining rounds so far does not appear to prevent this," began Mr Bergström.

"It is the labour force's capacity to produce goods and services, i.e. productivity, which in the long term determines the scope for developments in real wages. Real wages can only rise as long as productivity increases. If wages rise too rapidly, companies may be forced to raise their prices, which would result in higher inflation. The alternative is to restrict operations and dismiss staff. It is usually said that nominal wages cannot increase by more than the total of the inflation target of 2 per cent plus productivity growth. If, for instance, productivity in Sweden was assumed to follow a growth trend of around 1,5 per cent, an average rate of wage increase of around 3,5 per cent would be sustainable in the long term. However, this reasoning is based on the existence of



■ equilibrium in the economy, i.e. both internal and external balance. This is not the case today, when we have overly high unemployment and a surplus on the current account. If more people are to obtain work, wages cannot be allowed to increase at this rate, particularly as the surplus on the current account indicates an appreciation in the exchange rate," said Mr Bergström.

"The definition of a long-term sustainable rate of wage increase may differ from sector to sector, due to the different conditions for production technology, competitiveness and thus productivity growth. The goods-producing, competitive industrial sector is showing a relatively rapid increase in productivity, while the protected services sector, especially the public sector, is showing a much lower increase. This leads to greater scope for wage increases in the business sector and this could lead to demands for equally large increases from the public sector, where wages lag behind the private sector. This is reflected in the recurring focus on low-wage groups in this sector. It is therefore possible to fear a structural problem with wage demands in various sectors that do not reflect the respective sectors' productivity increases," continued Mr Bergström.

"Let us assume that productivity growth in the various sectors will continue as it was during the period 1998-2003 and that the average rate of wage increase will be approximately 3.5 per cent a year. This indicates that the Riksbank's target of 2 per-cent inflation is fully possible to achieve in the years to come, despite differences in productivity growth between the good-producing and services-producing sectors. If the focus on low-wage earners does not lead to a higher average rate of wage increase than this, the Riksbank's target is compatible with a policy of wage solidarity. On the other hand, problems could arise if the differences in productivity growth increase substantially and the trade union movement at the same time adheres to the policy of wage solidarity," concluded Mr Bergström.