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■ Assessment of economic activity and inflation prospects remains unchanged

Riksbank Governor Lars Heikensten spoke about economic developments on Monday at a seminar in Tanum arranged by the municipalities in northern Bohuslän.

"Developments in the financial markets have been unusually eventful in recent weeks. Since employment in the United States began to rise sharply there has been a change in the outlook for US monetary policy. Interest rate hikes are now anticipated, with some analysts expecting them to come fairly soon. This in turn has resulted in quite considerable revaluations in other markets too. In particular long-term interest rates have risen rapidly in the United States, by just over 1 percentage point since the end of March. But there has also been a rise elsewhere. The more risky emerging markets have seen increases of between 2 and 3 percentage points, while the rise in Japan, for instance, has not been more than 0.1 percentage points. That developments have not followed the same paths in all regions is a healthy sign; the long-term interest rates should reasonably reflect differences in risk and prospective inflation. In the euro area it is also positive that the rise in interest rates has been limited since it should facilitate the recovery. In Sweden the rise in yield on 10-year government bonds has so far stayed at 0.5 percentage points. This is not something that gives us cause for concern or reason to change our assessments of future developments," said Mr Heikensten.

"The crucial factor for monetary policy is of course as usual our assessment of future inflation. As regards economic activity and price pressures, recent developments have been considerably less dramatic than what the situation in the financial markets may suggest. New data have essentially confirmed the picture held by most forecasters, including the Riksbank. Consequently it appears that growth will be robust in the United States. This applies also to Asia and eastern Europe, for example, where developments may even prove somewhat better than many had expected. Also in the euro area it seems that the recovery will continue gradually, but in the words of the ECB, the signals there are still mixed. Against this background, the Riksbank made some slight adjustments to its outlook for international growth at the most recent monetary policy meeting on 28 April. There is nothing today to suggest that we have



reason to change this outlook in any significant way. A pickup in international economic activity will of course also have effects on international price pressures, which are expected to mount gradually and relatively cautiously in the years ahead in roughly the manner we indicated before," continued Mr Heikensten.

"In line with the increase in international growth Swedish exports have also risen. It now seems likely that export growth will be somewhat more pronounced than we forecast in March. In addition there are the positive effects on domestic demand of our repo rate cut and a number of expansionary measures in the spring budget. All in all, this prompted us at our last meeting to make a slight upward revision to our forecast for growth in the Swedish economy. I do not see reason today to make any further crucial revisions," said Mr Heikensten.

"So what then is our outlook for Swedish inflation in the period ahead? Neither has there been any significant change of scene in this regard. We expected in March that inflation would rise cautiously in line with economic activity and resource utilisation. This is still our outlook. However, the slightly higher growth that is now included in our assessment suggests that inflation could be expected to rise somewhat faster than we anticipated in the previous Inflation Report. There are also a couple of other factors that we must take into consideration:

- One is oil prices, which have risen more than expected. Exactly what lies behind the price increase is not clear. The increasingly robust international growth has probably affected the price, but at the same time there is the question of why this should only have had such a strong impact on the price now. Other factors that have affected the price very recently are most likely related to the supply of oil, not least greater unease in the Middle East. Presumably there is reason to expect somewhat higher oil prices during the forecast period, at least in the short term. It is more uncertain what view should be taken of oil prices in the longer-term. Nevertheless most factors indicate that oil prices will fall back from their currently elevated levels, which is also what futures markets appear to be expecting. In our conduct of monetary policy we must also decide what extent the rise in oil prices should be allowed to affect our interest rate decisions. This in turn depends both on how persistent the price changes are anticipated to be and on how they can be expected to affect inflation expectations.
- A second factor is the technical change in Statistics Sweden's method for computing CPI inflation. This will affect the forecasts of inflation for 2005 onward and dampen it by a couple of tenths of one per cent.

When all these factors have been considered it seems likely that the Riksbank's conclusion regarding inflation at the last meeting at the end of April remains unchanged. We said then that inflation was expected to be in line with the target at the end of the forecast period. This is still my assessment," concluded Mr Heikensten.