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■ Pensions, globalisation and the current economic situation

Deputy Governor Kristina Persson spoke on Monday about globalisation, future pensions and the economic situation at the seminar "The future and pensions" organised by the insurance company Länsförsäkringar in Jämtland.

"Future pensions will be determined by developments in the economy in general and by wage growth. The scope for wage increases is limited in the long term by productivity growth. If real wages rise more quickly than productivity, the business sector loses competitiveness. This ultimately results in increased unemployment. The factors that determine how Sweden will manage competition and thereby pensions in the future are the capacity of the business sector and society as a whole to quickly adapt to changing conditions. This includes competing with new technology, new products and services," began Ms Persson.

"The Riksbank cannot affect productivity growth, but by maintaining price stability helps reduce uncertainty in the wage bargaining rounds and the economy as a whole. A high level of confidence in monetary policy has contributed to low inflation and to real wages increasing more rapidly over the past decade than during the previous decade," emphasised Ms Persson.

"The Swedish pension system is considered to be one of the most modern and most long-term sustainable in the world. It takes into account not only economic growth but also changes in the average length of life and in the labour supply. Lower growth in the economy and poorer developments in real wages mean that pension entitlements will increase more slowly in value and vice versa. With regard to the conditions for future pensions, it can be noted that productivity has increased more rapidly over the past ten years or so than previously and has been higher in Sweden than in most other OECD countries. If the trend productivity growth remains strong, the conditions will be good for wages and pension entitlements to grow at a good rate," continued Ms Persson.

"The percentage of elderly people in the population is increasing in all regions of the world, which means that many other countries may experience greater



■ difficulties in financing future pensions. Pension systems are often built according to a different demographic situation, as was previously the case in Sweden. Here the Swedish society can contribute knowledge and systems that may be useful to other countries," added Ms Persson.

"The low inflation in recent years can be partly explained by the increased globalisation that has contributed both to strong productivity growth and to low import prices. Swedish importers have to a great degree utilised the opportunity to import from low-cost countries. Globalisation has also led to increased competition. Swedish companies have therefore been forced to rationalise and become more efficient. All of this has stimulated productivity growth and had a subduing effect on inflation in Sweden," said Ms Persson.

"An important monetary policy question is how globalisation will affect the Swedish economy in future. On the one hand, globalisation is a strong force that can be expected to progress over many years to come. On the other hand, it is uncertain, for instance, how long the Chinese economy and other large emerging economies can continue to grow very rapidly without inflation accelerating, as a result of a shortage of qualified labour or of other problems arising," said Ms Persson.

"Let me briefly comment on the current economic situation. At its monetary policy meeting on 29 August the Executive Board of the Riksbank decided to raise the repo rate by 0.25 percentage points to 2.5 per cent. This decision was partly based on strong GDP growth so far this year both in Sweden and abroad. The strong demand is also reflected in the fact that household indebtedness and house prices are continuing to rise and that the labour market is showing stronger development," said Ms Persson.

"The main scenario in our most recent Inflation Report described continued strong growth abroad. However, there are possible risks that the global economy could slow down more suddenly. The question is how long China can continue to increase investment by around 30 per cent a year, without the economy overheating. A related issue is how long the investors' confidence in the rapid developments in China will endure. There are also risks with developments in the United States. There has already been a severe cooling of the housing market, which has earlier contributed to growth. If house prices were to fall substantially, this could have clearly negative effects on household consumption. Moreover, high oil prices are probably already contributing to a moderation in households' scope for consumption. If the economies in the United States and China were to slow down simultaneously, it could have very negative effects on the foreign-trade dependent Swedish economy," added Ms Persson.

"In May this year the Riksbank published a brochure entitled "Monetary Policy in Sweden" which provides an account of our monetary policy strategy. It is primarily the inflation outlook a couple of years ahead that guides monetary policy. However, the policy also gives consideration to the real economy. If inflation is below target despite good growth in demand, attempts to quickly return it to target through very expansionary monetary policy could lead to the domestic economy overheating. At a later stage this could lead to a sudden slowdown as a reaction to price bubbles in the asset markets, such as the housing market. In addition, deviations from the target may sometimes be so substantial that there is reason to allow inflation to return to target beyond the normal two-year horizon to avoid large fluctuations in economic activity," said Ms Persson.



■ "Globalisation and integration of large emerging economies mean that it is not sufficient to only take into account domestic production conditions when making monetary policy decisions. This is particularly important for a central bank in a small, open economy like the Swedish one. It may be more difficult now than before to interpret what the size of the production gap, that is, the difference between the actual production volume and the potential level, means for inflation. If demand rises rapidly and capacity utilisation increases in Sweden, this may perhaps be compensated to a greater degree than before by an increased supply via imports from low-cost producers, or by part of production being transferred to other countries. It is difficult to assess the effects this will have in future. We therefore need to continuously improve our analyses of global conditions and their consequences for productivity development, the labour market and prices," concluded Ms Persson.