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■ The Riksbank and monetary policy

First Deputy Governor Irma Rosenberg gave today a speech at Nordea in Copenhagen. Ms Rosenberg began by speaking about how the Riksbank works today and then gave an account of her views on the economic situation in connection with the May monetary policy meeting.

"In February this year we presented for the first time our own forecast for the repo rate. The reason why we took this step was that we want to become even more open and clear towards the general public about how the Riksbank views both future developments in the Swedish economy and their consequences for monetary policy. At the same time, I wish to emphasise that our own forecast for the interest rate path does not entail any promise by the Riksbank; it is merely a forecast and is constantly being reviewed. Just as before, economic developments will determine how we change the repo rate in the future. Our forecast may also differ somewhat from the long-term interest rate expectations in the financial markets. This does not need to be anything strange, as we may perhaps assess future economic developments slightly differently. On the other hand, short-term market expectations will of course be more clearly affected by our forecast. This is quite natural as the repo rate primarily affects the short-term rate," began Ms Rosenberg.

"By publishing our own interest rate path we are in principle being as clear as we possibly can. The new way of working therefore reduces the need to signal prior to the monetary policy meetings how the Executive Board views the interest rate level. It is normally sufficient to signal clearly in connection with the monetary policy meetings. It is only in exceptional cases that there is reason to give further signals when the next meeting and interest rate decision are approaching. Of course, individual members will still be able to express their own opinions in public. But this will be mainly a case of afterwards explaining their personal considerations at the monetary policy meetings. As we will now also be naming the Board members in the minutes of the meetings, it will be even clearer what stance each member has taken. This will also make it easier to examine the motives behind the decisions," continued Ms Rosenberg.

"I now intend to go on to say a few words about how I viewed the economic developments in connection with the most recent monetary policy meeting. The new information received in recent months indicates that inflationary pressures have become slightly higher than was expected in the Monetary Policy Report in February and at the monetary policy meeting in March. This is partly because the Government's Spring Budget Bill looks to be more stimulating for demand, at least during next year, than we had previously anticipated. Another reason for the changed picture is that the agreements in the collective wage bargaining rounds so far indicate that wages will increase more quickly than we had previously estimated. The size of the wage increases will depend on how the labour market functions, among other things. Important questions are whether the labour supply will increase to the extent we have expected, whether the matching of demand for and supply of labour will work and what consideration is given to the labour market situation in the wage negotiations. We currently have a strong labour market situation and it is then reasonable to assume that wage increases will be slightly higher than they have been in recent years. However, the outcome of the central wage bargaining rounds has nevertheless been higher than we saw reason to expect, given that there is still fairly substantial spare capacity in the labour market," observed Ms Rosenberg.

"At our most recent monetary policy meeting in early May my opinion was that the economic picture had not changed so much that we needed to raise the repo rate quickly. Inflation was still low and the assessment was that it will rise slowly. This was because there were still several factors holding back inflationary pressures. Price pressures from abroad were expected to continue and productivity was expected to improve at a good rate. Corporate profits were good and there were many indications that profitability in the business sector had continued to improve. My opinion was therefore that it was not necessary to raise the interest rate at the most recent monetary policy meeting. However, developments indicated that the repo rate would need to be raised more during the forecast period than in the February report. This is to ensure an inflation rate in line with the target and a balanced development in the real economy," said Ms Rosenberg.

"The rate of future interest rate increases must now be balanced so that inflation does not accelerate more than expected, but so that growth in production and employment is not slowed down too soon. We should return to the question of how quickly and how much the rate should be raised at our June monetary policy meeting. We will then have more information on the wage bargaining rounds and on how production has developed this year," continued Ms Rosenberg.

"I intend to conclude with a few words on the consequences of the abolition of property tax and its replacement by a lower local government charge. The tax change will affect inflation in that the housing costs in the CPI will change. This change will give a relatively large direct effect on inflation, although this will only be temporary. There is not normally any reason to use monetary policy to counteract such tax effects. With regard to indirect effects on inflation via general demand, it can be noted that the cut in property tax as described in the Government proposal is fully financed in the housing sector. This means that disposable incomes will not be affected in total. However, the tax changes may influence property prices. If property prices rise due to fundamentals, such as a change in property tax, this is not normally a problem for monetary policy to deal with. But if household demand increases as a result of this, monetary policy must of course take into account what effects it might have on inflation and GDP growth," concluded Ms Rosenberg.