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Separate minutes of the Executive Board meeting No.14

DATE: 2008-10-08

TIME: Kl 11

PRESENT: Stefan Ingves, Chairman
Lars Nyberg
Irma Rosenberg
Lars E.O. Svensson
Barbro Wickman-Parak (§§ 1-2 by telephone)
Svante Öberg

Leif Pagrotsky, Vice Chairman of the General Council

Sigvard Ahlzén
Hanna Armelius
Kai Barvèll
Kerstin Hallsten
Jesper Hansson
Karolina Holmberg
Ann-Christine Högberg
Per Kvarnström
Pernilla Meyersson
Christina Nyman
Mattias Persson
Tommy Persson
Åsa Sydén
Sara Tägtström
Staffan Viotti
Anders Vredin

§ 1. Monetary policy review

It was noted that Hanna Armelius and Sara Tägtström would prepare draft minutes of § 1 and 2 on the agenda for the meeting.

It was also noted that the meeting had been called by the Chairman because several central banks were planning coordinated action to mitigate the consequences of the ongoing financial crisis.

1.1 Developments regarding financial stability

Mattias Persson, Head of the Financial Stability Department, began with a brief report on the most recent events on the financial markets. On Monday and Tuesday, there were dramatic falls in share prices around the world. The reason for this was increasing concern that intervention on the part of various governments would not be enough to prevent a considerable weakening of the global economy, together with anxiety about the European bank sector. The Stockholm Stock Exchange fell by over 7 per cent on Monday. In the UK, an extensive rescue package for the nation's banks was presented this morning. The basis spreads, that is the difference between the interbank rates and the expected policy rates, have doubled in Sweden, the euro area and the UK since the meeting in September. In the USA they have almost tripled. Most of this increase has taken place over the last few days. This shows that the situation on the money markets is very strained. Today, Wednesday, the demand for Swedish treasury bills and treasury bonds has been very high, and as a result the rates for government securities fell substantially during the morning. The CDS spreads (Credit Default Swaps) have increased once again in both the USA and the euro area. CDS premiums have also increased for Swedish banks recently. To summarise, unrest on the financial markets has grown both in Sweden and globally over the last few days.

1.2 Macro economic developments in Sweden and abroad

Christina Nyman of the Monetary Policy Department presented background material on macroeconomic developments in Sweden and abroad. She began by noting that global financial unrest has increased since the previous Monetary Policy Meeting in early September. The assessment then was that there would be a downturn in economic activity. The assessment now is that the global financial crisis is reinforcing the ongoing downturn with diminished inflationary pressures as a result.

The labour market situation in the USA has deteriorated much more rapidly than was assumed in September. According to company surveys, employment (payrolls) fell by 159 000 individuals in September, which is double the average fall in the preceding three months. Jobless claims have continued to increase in recent weeks. There are some indications that the labour market in the euro area is also weakening. The purchasing manager indexes that have been published abroad since the financial crisis deepened in mid-September also show a marked deterioration in the economic climate. This picture is also supported by a number of other confidence indicators for households and companies.

The oil price as well as the prices of other commodities have continued to fall on the world market. Yesterday, the spot price for Brent crude was just over USD 80 per barrel and the forward prices are approximately USD 20-30 lower than they were at the meeting in September. Inflation expectations abroad have declined in pace with falling prices for oil and other commodities. The Swedish krona has weakened against the euro, but above all against the dollar. In trade-weighted terms, the krona has weakened by almost 5 per cent since the beginning of September.

The statistics received in Sweden for retail sales, industrial production, new orders and foreign trade for August indicate that developments so far are approximately in line with the assessment made in September.

However, the purchasing managers' index for September indicates a clear slowdown in economic activity in the period ahead and was at the lowest level since measurements began in 1994. The Economic Tendency Survey shows that household sentiment has

declined rapidly during the year and this confidence indicator is now much weaker than normal.

There are also clear signs of a weakening of the labour market. The number of new vacancies and the number of unfilled vacancies continued to fall in August. Information from the Public Employment Service indicates a considerable increase in the number of redundancy notices in September.

There has been significant tightening over and above monetary policy in recent weeks. Interbank rates have risen by approximately 30 points above the repo rate since the meeting in September at the same time as monetary policy expectations have fallen. The short-term basis-spread (3 months) has doubled since the meeting in September. There have also been some signs of a credit squeeze in the Swedish banks.

Inflation prospects have weakened since September. The assessment is that the decline in economic activity in conjunction with lower prices for oil and other commodities will have a dampening effect on inflation in the period ahead. The weakening of the krona will, however, counteract this to some extent. The purchasing managers' index clearly shows that price pressures in industry will be lower in the period ahead. The measurements of household inflation expectations one year ahead made by the National Institute of Economic Research fell to 2.4 per cent in September from a level of 2.9 per cent in August and 3.7 per cent in July. According to Prospera's survey in September, however, inflation expectations remain at approximately the same level as in June. At the same time, the survey shows that the money market players expect a lower repo rate in the period ahead.

Against the background of the worsening financial crisis in recent weeks and the latest macroeconomic statistics, the assessment is that the ongoing slowdown in economic activity will be reinforced with diminishing inflationary pressures as a result. The effect on the real economy, i.e. production and employment, will be through several channels. More expensive and more restrictive financing opportunities for households and companies will dampen consumption and investments. Increasing uncertainty about future developments, together with wealth effects, will lead to households and companies becoming more restrictive. It is probable that the forecasts for both inflation and GDP will be revised downwards.

§ 2. Monetary policy decision

The Chairman notified the meeting that the Riksbank has received information that a number of central banks, including the US Federal Reserve and the ECB, will reduce their policy rates by 0.50 percentage points and that this will be announced at 13.00 today. The Riksbank has been asked to participate in this joint action.

The members agreed, given the discussions that have so far taken place in the course of the work on the next Monetary Policy Report and the short time available, that the decision should be made without extensive discussion.

All of the members of the Executive Board considered that it would be appropriate to cut the repo rate by 0.50 percentage points to 4.25 per cent. A reduction in the repo rate in the current situation would mitigate the consequences of the financial crisis for the real economy. Although developments in Sweden to some extent differ from those in other

countries, a cut is warranted here too. The fact that the cut will be coordinated with other central banks will increase confidence and the likelihood that it will have positive effects.

The Executive Board decided

- to lower the repo rate by 0.50 percentage points to 4.25 per cent and that this decision would apply from 15 October 2008,
- to lower the lending rate to 5.00 per cent and the deposit rate to 3.50 per cent, with effect from Wednesday 15 October 2008,
- to announce the decision at 13.00 on Wednesday 8 October with the motivation and wording contained in draft Press Release no. 44 2008 (Annex A to the minutes) and
- to publish the minutes of today's meeting at 9.30 on Wednesday 15 October.
- The interest rate that is to apply to the loans granted within the framework of today's auction of six-month loans shall be 0.50 percentage points lower than the interest rate calculated in accordance with the previously announced terms.
- The bidders who are allocated loans in the auction have the right to withdraw their bids if they so wish, but this would not affect the allocation to other bidders.

This paragraph was confirmed immediately.

Minutes by:

Ann-Christine Högberg

Checked by:

Stefan Ingves, Chairman

Lars Nyberg

Irma Rosenberg

Lars E.O. Svensson

Barbro Wickman-Parak

Svante Öberg