

Recent developments in inflation

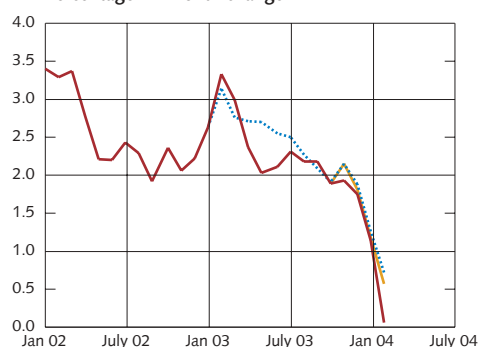
This box describes and analyses developments in inflation since the December Inflation Report. As expected inflation has fallen, due in part to lower energy prices. However, the decline has been somewhat sharper than previously forecast, mainly owing to a low rate of imported inflation (excluding oil prices). In addition, productivity growth has been unexpectedly robust.

Unexpectedly low inflation

Last year and at the beginning of this year inflation fell sharply. For the most part, this drop was expected following the unusually steep price increases at the beginning of last year (see Figure B14). In the March Inflation Report in 2003, the Riksbank forecast UND1X inflation to be 3.1 per cent in February 2003 and 0.7 per cent in February 2004. The outcomes were 3.3 per cent and 0.1 per cent, respectively. Thus, even though a large decline in inflation was expected, the fall was even sharper than indicated by the Riksbank's forecasts (and those of other forecasters). Figure B14 shows also that the Riksbank as recently as December 2003 overestimated UND1X inflation at the beginning of 2004. UND1X inflation was expected to stand at 0.6 per cent in February but the outcome was 0.1 per cent (the forecast error in January was considerably smaller).

So for a long time the Riksbank has been forecasting a substantial decline in inflation between February 2003 and February 2004, mainly due to an expected adjustment of energy prices to more normal levels. The fact that the fall proved somewhat larger than anticipated is chiefly a result of price developments in the last few months, principally an unexpectedly low rate of imported inflation (excluding oil prices). This in turn appears to be partly because international price pressure has been lower than expected and partly because the impact of the krona appreciation in the past year (particularly against the dollar) appears to have been greater. For example, prices of clothes and footwear in the CPI fell by 4.7 per cent in February compared with the same month last year (see Figure B15). The latter may also be due to overoptimistic plans on the part of the retail trade sector, thus necessitating unexpected price cuts. The recently strong productivity growth has most likely also been a significant factor.

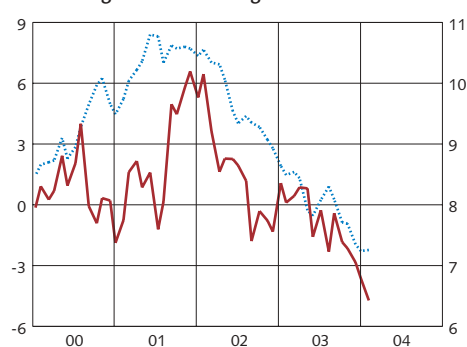
Figure B14. UND1X, outcome and forecasts. Percentage 12-month change



— UND1X
 Inflation Report 2003:1
 — Inflation Report 2003:4

Sources: Statistics Sweden and the Riksbank.

Figure B15. Rate of price increases for clothes and footwear in the CPI and the dollar exchange rate. Percentage 12-month change and SEK/USD



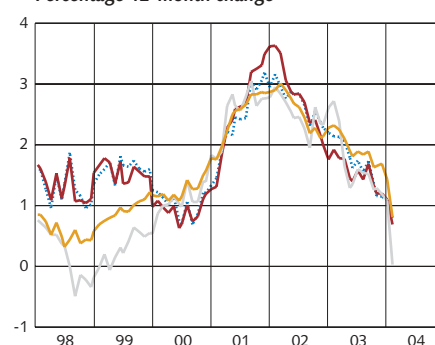
— Clothes and shoes (left scale)
 SEK/USD (right scale)

Sources: Statistics Sweden and the Riksbank.

Continued decline in underlying inflation.

In order to analyse how inflation changes in the long term, the Riksbank studies measures of underlying inflation. However, this is not an unambiguously defined measure but can be calculated in different ways. Figure B16 depicts different measures of underlying inflation. The outcome for all measures shows that inflation adjusted for various shocks has more than halved in the last two years.

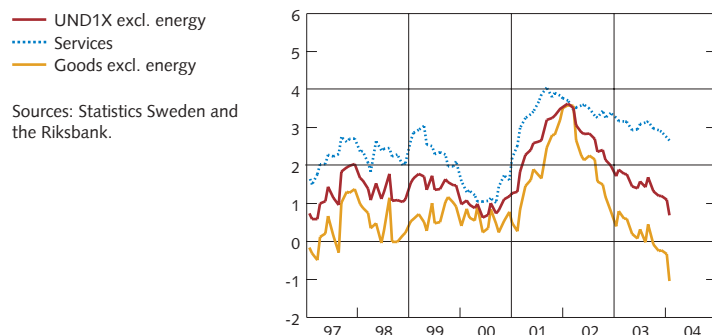
Figure B16. Different measures of underlying inflation. Percentage 12-month change



— UND1X excl. energy
 UND1X excl. energy and food
 — UND24
 — trim85

Note. The alternative measures are calculated on the basis of CPI divided into approximately 70 different subgroups. UND24 is weighted together with weights adjusted for historical standard deviations between the annual rate of increase in the CPI and the respective subgroup over the past 24 months. In trim85 the 7.5 per cent most positive and negative yearly price changes each month have been excluded. Sources: Statistics Sweden and the Riksbank.

Figure B17. UND1X excluding energy prices: breakdown of goods and services.
Percentage 12-month change



Lower rate of price increases for both goods and services

Inflation has differed between goods and services (see Figure B17). Goods prices usually rise more sluggishly than services prices since productivity growth is normally faster in the goods sector than in the services sector. Another difference is that the former is more exposed to international competition than the latter. On average, goods prices excluding energy have fallen over the last six months. Producer price inflation has shown a similar change (see Figure B18). One important

reason is probably that the low international inflation for manufactured goods in the past year and the stronger krona have both led to an easing of imported inflationary pressure.

The rate of price increases for services has remained relatively high even if it has also declined over the past year. One reason is that the rate of price increase for more administratively priced services fell back (see Figure B19). However, municipal charges, for example, are still rising faster than prices of other services. One important reason is probably that local governments are compensating themselves for their strained financial situation by raising various charges, such as those on refuse collection.

Higher oil prices but lower electricity prices.

Compared with the forecast in the December Inflation Report, the annual rate of increase in energy prices overall has fallen largely as expected. Nevertheless, oil prices have averaged around USD 2 per barrel higher than expected. The higher price of oil has been countered by the weaker dollar, which has meant that the prices paid by consumers for petrol and heating oil have been approximately in line with expectations.

Up to and including February, consumer prices for electricity have fallen largely as expected. However, prices on the Nordic electricity exchange, Nord Pool, have been lower than was indicated by the forward market at the end of last year. Many factors point to the relatively mild winter as one important reason for the lower electricity prices on Nord Pool. The price decline on the exchange has also resulted in a drop in consumer prices for electricity. Electricity trading companies have begun to cut both until-further-notice prices and prices of fixed-price contracts. Electricity prices fell by an annual rate of 2.5 per cent in February, excluding the effects of changed energy taxes, which was consistent with the assessment in the December Inflation Report.

To sum up, the past year has been characterised by a steep drop in the rate of price increases for most goods and services in the CPI, as indicated by the different measures of underlying inflation. The fall in the inflation rate has been sharper than expected, especially in the past few months.

Figure B18. Manufactured products in the producer channel: domestic market prices and import prices.
Percentage 12-month change

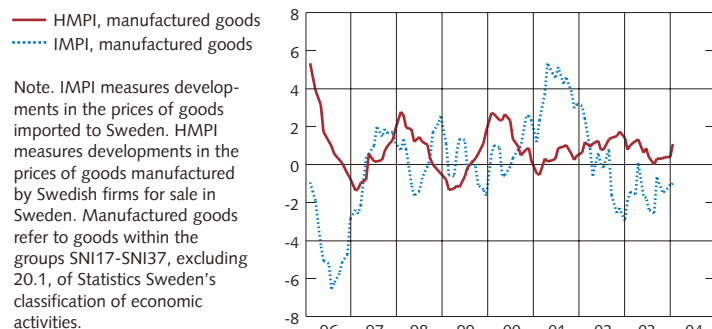


Figure B19. Services prices.
Percentage 12-month change

