

INFLATION RATES CLOSE TO LOWER TOLERANCE LIMIT

The degree of inflation target fulfilment should be evaluated in an annual perspective, not from isolated monthly figures. This is because it takes time for monetary policy to counter an unexpected development of inflation and transitory effects should be regarded as of secondary importance in an evaluation.

Since the inflation target came into force, the annual increase in consumer prices has averaged 1.5 per cent. This average outcome is below the inflation target but well inside the tolerance interval. In the same period the average rate of underlying inflation, measured as UND1, has been close to 1.5 per cent, while for UNDINH it has been 2.0 per cent.

Various kinds of transitory effect have been particularly marked in certain periods. From June 1996 to July 1997 the 12-month change in the CPI was outside the lower tolerance limit, largely because the general fall in interest rates affected the CPI through lower house mortgage interest expenditure. Much of the fall in interest rates was an effect in turn of increased confidence in general economic policy and the Riksbank's repo rate cuts during 1996.

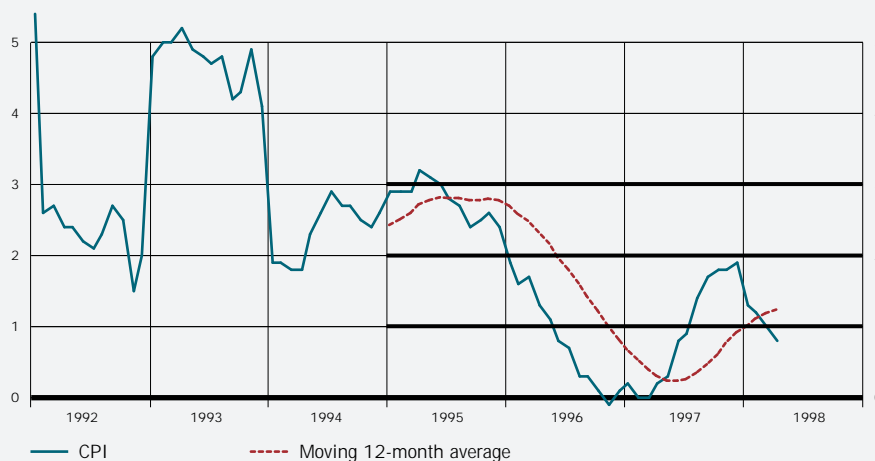
In April this year the 12-month change in the CPI was 0.8 per cent, which is likewise outside the lower

tolerance limit and to a large extent a consequence of transitory effects. Changes to indirect taxes and subsidies, together with lower interest expenditure, had a downward effect on the CPI of 0.25 percentage points. In an annual perspective the picture is somewhat different. The average of the 12-month CPI change figures over the year up to April is 1.2 per cent, which is inside the inflation target's tolerance interval.

The factors that exert transitory effects on inflation and should therefore be disregarded in the construction of monetary policy are not self-evident and may also differ from case to case. It is difficult, moreover, to estimate the extent to which consumer prices are affected by different transitory effects.

Under these circumstances, to obtain assistance in the specification of an adequate indicator of underlying inflation, at the end of April 1998 the Riksbank contacted the CPI Enquiry which the Government has set up. The Riksbank has also requested Statistics Sweden to initiate the regular publication of one or more series of figures on underlying inflation. The idea is that these figures would be published each month together with the CPI.

Figure B4.
Consumer price index.
Percentage 12-month
changes (CPI) and
moving 12-month average
of these changes.



Note. The horizontal lines from 1995 onwards represent the Riksbank's annual target and tolerance interval for the CPI.

Sources: Statistics Sweden and the Riksbank.