Extract from a speech by Governor Urban Bäckström 25th Aug. 1998

The present situation

First, however, some words about the situation at present. The picture of economic developments in Sweden that was discernible before the summer indicated that the pattern in recent years, with high growth and low inflation, would continue in the years ahead.

In the Inflation Report last June it was considered that in the coming period of twelve to twenty-four months that is relevant for the construction of monetary policy, inflation would be below the targeted rate. The Riksbank accordingly noted that there was room for a somewhat more expansionary monetary stance, at least for the time being. The repo rate was lowered 25 basis points.

Some new information that has been obtained during the summer does not appreciably alter the picture we painted in June. If anything, the statistics on overall real economic activity and inflation point more in the direction of a future inflation tendency that is weaker than in the main scenario in our June report, though in that case the revisions would be only marginal. In one respect—the exchange rate tendency—there is evidence that may point in the other direction. The krona has become weaker than we envisaged earlier. While the Riksbank does not target the exchange rate, the krona's tendency is an important indicator for the prediction of inflationary pressure in the Swedish economy. All else equal, a permanent weakening or strengthening of the krona has implications for future inflation.

Most things suggest that the current weakening of the krona is a temporary phenomenon—the present level of the exchange rate is at odds with more fundamental conditions in the Swedish economy. Neither are there any signs of decreased confidence in the low-inflation policy. It should be underscored, however, that if the observed weakening of the krona can be regarded as permanent, then there is also reason to count on the weaker exchange rate leading to inflation above the rate we foresaw in the June report. That would have consequences for monetary policy. All this presupposes, of course, that other factors have not simultaneously improved inflation prospects. The question of how the exchange rate tendency should be weighed in with other factors to arrive at an overall assessment of inflation is something to which we will be returning.