

Press Release

7 DECEMBER NO. 78

Repo rate raised 0.25 percentage points to 4 per cent

At the meeting on Wednesday, 6 December, the Executive Board of the Riksbank decided to raise the repo rate 0.25 percentage points, from 3.75 to 4 per cent, with effect from 13 December. Today's interest rate increase aims to ensure that a good and stable economic development in Sweden is maintained with continued price stability.

The Board's decision is based on the picture of inflation prospects in the Inflation Report that is published today. The overall assessment in the Report is that the rate of inflation one to two years ahead will be somewhat above the Riksbank's target. The growing inflationary pressure is mainly a consequence of total demand being judged to rise more rapidly than a balanced economy can cope with in the longer run. There are also risks of higher inflation in connection with, for example, the development of wages, oil prices and the exchange rate.

The assessment of inflation in the Report's main scenario envisages that economic activity continues to be relatively strong, with good domestic growth. While statistics in recent months indicate that the economic trend may be somewhat more subdued than the Riksbank counted on earlier, they do not alter the basic picture. It is still considered that demand will rise so rapidly that unutilised resources are brought into production successively and thereby lead to gradually more appreciable capacity restrictions. Given an unchanged repo rate of 3.75 per cent, the rate of inflation excluding transitory effects from indirect taxes, subsidies and house mortgage interest expenditure (UNDIX) is judged to be 1.8 per cent one year ahead and 1.9 per cent after two years. Compared with the assessment in the October Inflation Report and considering that the forecast period has now shifted one quarter into the future, this represents some upward adjustment of the forecast rate one year ahead and a marginal downward revision of the two-year forecast.

The assumptions underlying inflation's path in the main scenario include gradually falling oil prices and an appreciation of the krona. The uncertainty in these respects is considerable, as recent developments have clearly shown. Both the oil price and the krona's path are definite upside risks for inflation in the years ahead. The development of wages must also be included among the factors that could lead to inflation being higher than in the main scenario. This has to do with an

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increasingly strong labour market, with rising employment, increasingly low unemployment and growing labour shortages. These upside risks are partly balanced by the possibility of international activity being weaker than assumed in the main scenario. But all in all, the balance of risks in the inflation forecast is judged to be somewhat on the upside one year ahead and more substantially so after two years. When the risk spectrum is included, the rate of UNDEX inflation is judged to be 2 per cent one year ahead and 2.3 per cent after two years. The corresponding assessment of CPI inflation gives rates of 2.0 and 2.5 per cent.

The future direction of monetary policy will depend on the strength of economic activity but also on the development of other determinants of inflation, such as wages, oil prices, inflation expectations and the exchange rate.

As of 13 December the Riksbank's deposit and lending rates will be adjusted from 2.75 and 4.25 per cent, respectively, to 3.25 and 4.75 per cent. The intention is that these rates will no longer be used for signalling (see Press Release no. 79).

The minutes of the Executive Board's monetary policy discussion at yesterday's meeting will be published on 20 December.

A press conference at the Riksbank will be held at 10 a.m., entry by press card at 11 Brunkebergstorg. The conference will be opened by Governor Urban Bäckström and First Deputy Governor Lars Heikensten. That will be followed by a review of the Inflation Report with Lars Heikensten together with Claes Berg and Per Hansson, head and deputy head, respectively, of the Monetary Policy Department, and Hans Lindblad, head of the department's Division for Macro Economic Analysis. The seminar will also be transmitted (in Swedish) on the Riksbank's website, www.riksbank.se, under the heading 'För journalister/Video'.

The Inflation Report can be downloaded from the website under the heading Publications/Inflation Report or ordered from Information Riksbank, e-mail address: forradet@riksbank.se, fax: +46 8 787 05 26, telephone: +46 8 787 01 00.