

# Press Release

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## The Riksbank and the Swedish economy

Deputy Governor Villy Bergström gave a speech at a meeting arranged by Nordea in Stockholm on Monday. Mr Bergström's speech was based on the most recent Inflation Report, which was published on 19 March. He touched on economic developments up to the interest rate decision on 25 April and the motives behind the Riksbank's interest rate hike.

“International developments have largely followed the picture painted by the Riksbank in the most recent Inflation Report. The expansionary economic policy in a large number of industrial nations vouches for a recovery this year. In the USA growth appears to be slightly stronger than expected, according to statistics for the first few months of the year. For instance, domestic demand has developed positively and both the household and corporate sectors appear to have strong confidence in future developments. The euro area is also showing a development in line with the Riksbank's assessment in March, i.e. more subdued than in the USA, but with signs of a tentative recovery. However, there is still some uncertainty regarding the sustainability and strength of the recovery in global economic activity. Factors contributing to the uncertainty include the imbalances that remain in the US economy, the conflict in the Middle East and the higher oil prices. A further cause for concern is the higher inflation figures in the euro area. The Riksbank's total assessment, according to the press release of 26 April, was that the picture of international economic activity painted in the March Inflation Report, of a gradual recovery during the present year, followed by a relatively high growth rate, still stands, ” said Villy Bergström.

“As regards Sweden, the growth in demand has largely followed the picture outlined in the Inflation Report. The services industry has maintained a good level of activity and now there are also signs of a recovery in manufacturing. Economic policy currently has a stimulating effect on the economy and households have greater scope for consumption as a result of low real interest rates, increased transfers and lower taxes. As described in the press release, however, the Riksbank concludes that, given the rise in oil prices and weak developments on the stock markets, combined with problems in the telecom sector and raises in interest rates, it is possible that demand will be marginally weaker than expected in the previous

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Inflation Report. GDP growth in Sweden is expected to be in the interval 2.5-3.0 per cent”, continued Bergström.

“Sweden is presently in a good starting position. During the 1960s and up to the 1990s we had constant problems with the balance on the current account. It now looks as though these problems are behind us. We also have sound central government finances, which provides a completely different scope for manoeuvre than we had, for instance, in the early 1990s. Here Sweden has an advantage even compared with countries like Germany, which has recently been burdened with budget problems. However, despite our good starting position, we still have some problems. What particularly comes to mind here is the functioning of the labour market,” said Mr Bergström.

“Labour costs are increasing slightly faster than is compatible with the inflation target, as pointed out in the Inflation Report, and resource utilisation still appears relatively strained. In recent years, increased costs have to some extent been counteracted by firms reducing their profit margins, but the indications are that there is now little scope for this. There are also major differences in wage increases between different sectors and different professional categories, which was also pointed out in the Inflation Report. In some areas of the industrial sector, wages of white-collar workers have risen more than those of blue-collar workers. In addition, wages have risen particularly markedly in the rapidly expanding services sector. Relative wage differences are a normal element of a dynamic economy, but the Swedish labour market has previously shown that large relative changes often lead to compensatory wage drift,” said Mr Bergström.

“In combination with a weaker growth in productivity, partly due to slightly lower demand, labour costs have risen by a relatively large amount in many service industries. There is a risk that the higher costs will have a greater impact on prices in future, particularly in industries with a lack of competition, such as construction, retail trade, banking and insurance,” continued Villy Bergström.

“The Riksbank's total assessment is that over the next six months inflation will fall from the current high levels as the effects of last year's transitory price increases subside, although it is possible that in the short term the higher petrol and oil prices may slightly slow down the decline. After this, the relatively high resource utilisation is expected to contribute to labour costs and domestic inflation increasing somewhat once again. The Riksbank's most recent interest rate hikes should be regarded in the light of these developments,” concluded Mr Bergström.