



# Minutes of Monetary Policy Meeting

April 2016



# Summary

*At its monetary policy meeting on 20 April, the Executive Board of the Riksbank decided to purchase government bonds for a further SEK 45 billion during the second half of 2016. The purchases include both nominal and real government bonds, corresponding to SEK 30 and SEK 15 billion, respectively. The repo rate was held unchanged at -0.50 per cent. There is still a high level of preparedness to make monetary policy even more expansionary if this is needed to safeguard the inflation target.*

It was noted at the meeting that the Executive Board agreed on the picture of economic prospects and the inflation outlook described in the draft Monetary Policy Report.

Several members mentioned risks linked to uncertainty on the financial markets and to economic prospects abroad. The members also noted that international inflation is low and that several central banks are expected to conduct very expansionary monetary policy.

In Sweden, resource utilisation is currently close to normal, and economic activity is expected to continue to strengthen. Inflation has been slightly higher in recent months than the forecast in February. But although the forecast for inflation has been revised up slightly for the next few months, it is expected to be lower than the target for 2016, too.

The Executive Board agrees that monetary policy needs to continue to be very expansionary. However, the members have slightly different views as to whether it is appropriate to extend the government bond purchasing programme.

On the one hand, the Swedish economy is characterised by high growth and an ever-stronger labour market, and inflation has been higher than expected for several months. Rising resource utilisation also creates good conditions for a continuation of the upward trend in inflation. This may be an argument for not prolonging government bond purchases.

On the other hand, the upturn in inflation is uneven and to a high degree has been driven by a weak krona. A continued positive economic development in Sweden is therefore needed to safeguard the upward trend in inflation. At the same time, uncertainty in the wider world remains and several central banks are conducting a very expansionary monetary policy. The inflation forecast is thus highly sensitive to various international factors. This is an argument for extending the government bond purchasing programme to mitigate the risk of the krona appreciating too quickly, which would lead to weaker demand for Swedish exports and lower inflation.

A majority of the Board members considered it appropriate to continue buying government bonds for a further SEK 45 billion during the second half of 2016. To achieve a broad impact on different interest rates, the purchases should include both nominal and real government bonds corresponding to SEK 30 billion and SEK 15 billion respectively. Until further notice, maturities and coupons from the portfolio of both nominal and real government bonds will be reinvested. One board member considered that

monetary policy is sufficiently expansionary for inflation to rise towards 2 per cent, and that it is therefore unnecessary to extend the purchases of government bonds.

The Executive Board was unanimous in holding the repo rate at –0.50 per cent, and, as in February, expects to begin raising the interest rate slowly in mid-2017.

The Executive Board is also unanimous as regards having a high level of preparedness to make monetary policy even more expansionary, even between ordinary monetary policy meetings, if this is needed to safeguard confidence in the inflation target.



# MINUTES OF MONETARY POLICY MEETING

## Executive Board, No. 4

DATE: 20/04/2016  
TIME: 9.00 am

SVERIGES RIKSBANK  
SE-103 37 Stockholm  
(Brunkebergstorg 11)

Tel +46 8 787 00 00  
Fax +46 8 21 05 31  
registratorn@riksbank.se  
www.riksbank.se

Present: Stefan Ingves, Chair  
Martin Flodén  
Per Jansson  
Kerstin af Jochnick  
Henry Ohlsson  
Cecilia Skingsley

Michael Lundholm, Vice Chair of the General Council

Claes Berg  
Carl-Johan Belfrage  
Sophie Brauner  
Charlotta Edler  
Heidi Elmér  
Bo Enegren  
Mattias Erlandsson  
Jens Iversen  
Martin W Johansson  
Ola Melander  
Pernilla Meyersson  
Marianne Nessén  
Christina Nyman  
Carl Fredrik Pettersson (§ 1-3A)  
Maria Sjödin  
Ulf Söderström  
Anders Vredin

It was noted that Carl-Johan Belfrage and Bo Enegren would prepare draft minutes of the monetary policy meeting under Sections 2 and 3.

## §1. Economic developments

Carl-Fredrik Pettersson of the Markets Department began by presenting the latest developments on the financial markets. Since the monetary policy meeting in February, stock markets and commodity prices have risen. Contributory explanations have been less concern over developments in the Chinese economy, signals of slower policy-rate increases in the United States and a more expansionary monetary policy in the euro area. European bank shares have periodically been under pressure, however, which is linked to a concern for how negative interest rates affect banks' earnings and to the high proportion of bad loans in Italian banks.

The ECB announced monetary policy easing in March and there are market expectations of further rate cuts and an extension of the bond purchasing programme later this year. After a downward revision of the average forecasts from the members of the Federal Reserve's rate-setting committee in March, minutes and speeches give a mixed picture of US interest rate developments in the period ahead. For its part, the Bank of England is expected to await the outcome of the referendum in June on a British exit from the EU, while expectations of further stimulus from the Bank of Japan have strengthened in the wake of negative GDP outcomes and a near-zero per cent inflation rate.

Signals of a softer approach by other central banks, as well as unexpectedly high Swedish inflation outcomes, have caused the Swedish krona to appreciate by a few per cent since February. Another factor behind the appreciation of the krona is that the Riksbank is now perceived to be less inclined to cut the interest rate and more inclined to tolerate a strengthening of the krona. Prior to today's meeting, a majority of analysts expected an unchanged repo rate but an extended asset-buying programme.

Mattias Erlandsson of the Monetary Policy Department presented the draft Monetary Policy Report, which, it was assessed, would gain the support of the majority of the members of the Executive Board. He began by noting that the forecasts in the draft were previously discussed by the Executive Board at meetings held on 4, 5 and 8 April. The draft Monetary Policy Report was tabled at a meeting of the Executive Board on 12 April.

Developments since the monetary policy meeting in February have been characterised by further fluctuations on the financial markets and by continued major uncertainty about global economic growth. The recovery in the global economy is expected to continue, but growth has been revised down slightly compared with the previous forecast in February, which reflects the fact that the economic risks are deemed to have increased somewhat. Inflation prospects abroad remain basically unchanged, however.

Growth is high in the Swedish economy. Last year, GDP rose by over 4 per cent and this year growth is expected to be 3.7 per cent, a stronger development than forecast in February. Resource utilisation is deemed to be approximately normal and is expected to increase and be

higher than normal during the forecast period. The situation on the labour market continues to improve and employment will rise at the same time as unemployment will fall in 2016 and 2017. Thereafter, a certain upturn in unemployment is expected when many newly arrived refugees with a weak connection to the labour market enter the labour force.

Since the monetary policy meeting in February, inflation outcomes for January, February and March have been reported. The outcomes were slightly higher than expected for all three months. The price of clothes and shoes, among other items, rose unusually quickly, as did the prices of certain services. The inflation forecast has been revised up somewhat in the short term. Inflation will nevertheless remain below target for a time, among other reasons as a result of energy prices still having not recovered and of price increases for imported goods having been dampened due to the recent appreciation of the krona. However the conditions for rising inflation are deemed to be good. The Swedish economy is growing quickly and resource utilisation is rising. CPIF inflation is expected to stabilise around 2 per cent during 2017.

The forecasts in the draft Monetary Policy Report are based on the government bond purchasing programme being extended to the end of 2016, which means purchases for an additional SEK 45 billion so that they will amount to SEK 245 billion in total by the end of 2016. Furthermore, the forecasts are based on the repo rate being held at –0.50 per cent and on an unchanged repo rate path.

## §2. The economic situation and monetary policy

Deputy Governor **Martin Flodén** began by saying that he agreed with the picture of economic developments and supported the proposals for monetary policy decisions in the draft Monetary Policy Report.

Mr Flodén observed that the beginning of the year was characterised by falling stock prices internationally, mainly linked to concern for too rapid a slowdown in the Chinese economy, a break in the cautious economic recovery in the euro area and subdued growth in the US economy. This concern was obvious at the time of the monetary policy meeting in February, when Mr Flodén considered the Riksbank's forecast to hardly be unbiased; he saw it rather as a main scenario fraught with clear downside risks.

Subsequently, concerns on the financial markets have eased and stock prices have picked up. According to Mr Flodén, it is difficult to see clear real economic causes behind the large market movements at the beginning of the year. The fluctuations in economic indicators and data outcomes have been rather divergent after the February meeting. Some of the market upswing can probably be explained by measures and communication from central banks, including further stimulus from the ECB and the clear signal from the Federal Reserve that rate increases will occur at a slow pace in the period ahead.

Mr Flodén's overall assessment is that the international economic outlook has not changed much since the February meeting despite the Riksbank's forecasts being revised down slightly. The conditions are therefore still good for a slow upturn in growth abroad. Major risks and uncertainty factors remain, however, not least in Europe, where there are still sustainability problems in the public finances of several countries, continued weakness in many banks' balance sheets, and question marks surrounding future EU cooperation.

He also noted that outcomes in Sweden after the February meeting have been more clearly positive and that inflation is rising. There have been three inflation outcomes, all of them slightly higher than in the Riksbank's latest forecast. Underlying inflation in terms of the CPIF excluding energy is now close to two per cent, and other measures of underlying inflation have also risen. Inflation expectations have also picked up slightly, both in Prospera's surveys and according to market pricing. Growth for the final quarter of 2015 was also higher than expected, while employment and unemployment have developed approximately as forecast.

Mr Flodén pointed out that the strength of the Swedish economy and the clear inflation increase show that the expansionary, and partly unconventional, monetary policy is working. But the inflation increase is still not strong enough to continue unaided. According to the Riksbank's forecast, underlying inflation will now fall slightly, and it will take more time, and require a continued expansionary monetary policy, for inflation to establish itself more permanently on levels that are compatible with the inflation target.

According to Mr Flodén, there are several factors that explain why monetary policy still needs to be expansionary despite the strong growth. The Riksbank has spoken about these issues on many occasions, but he wished to mention two of them. First, international interest rates are still very low and monetary policy abroad continues to be very expansionary. How expansionary Swedish monetary policy will *de facto* be depends not just on the levels of the Riksbank's policy rate and asset purchases, but also on how the Swedish levels relate to levels abroad and to underlying real interest rates. Second, credibility for the Swedish inflation target may have been damaged by the long period of significantly below-target inflation. It is certainly a good sign that inflation expectations have picked up, but expectations are still clearly lower than the Riksbank's forecast for CPI inflation.

Another indication that the credibility of the inflation target is not yet on firm ground is, according to Mr Flodén, that the wage bargaining on the labour market seems consistently to have resulted in one-year agreements. It is probable that uncertainty regarding the future development of inflation has contributed to the labour market parties not being able to conclude longer agreements. We cannot rely on inflation gradually moving back to the target level on its own steam if inflation expectations are too low or if credibility for the inflation target is damaged. The inflation increase therefore needs the support of an expansionary monetary policy and strong economic activity.



Mr Flodén noted, however, that the recent upward inflation trend and increasingly strong resource utilisation of course have made the inflation increase more robust and that monetary policy is currently in a much more favourable position than 12-18 months ago. If economic activity continues to strengthen, it will be increasingly likely that inflation continues to move upwards in the long term even if credibility for the inflation target is damaged. Monetary policy does not then need to react as quickly to temporary setbacks.

Mr Flodén then asked what this reasoning meant for his view on today's monetary policy decision. He pointed out that recent developments in the Swedish economy indicate that we are on the right track and that the increasingly expansionary monetary policy in recent years has had the intended effect. Furthermore, as the economic picture from the last meeting is largely unchanged, he did not see any reason to change the direction of monetary policy. He did indeed enter a reservation against the rate cut at the last meeting but raising the repo rate now would send strange signals. Mr Flodén therefore advocated an unchanged repo rate as well as an unchanged forecast for the future repo rate.

Furthermore, Mr Flodén observed that the previously decided asset purchases mature in the summer and that one option is, of course, not to continue with such purchases. He emphasised that he does not think that a continued increase in inflation is dependent on such a decision, but that he saw an immediate end to the asset purchases as an unnecessary risk, especially when the ECB is increasing the pace of its asset purchases. According to Mr Flodén, there appears to be a high probability that the Riksbank's asset purchases will continue in the market's current pricing of bonds and the exchange rate. There is then a risk of interest rates starting to rise and the krona appreciating too quickly and strongly if the Riksbank concludes its asset purchases in the summer. Mr Flodén therefore said that he thinks it is appropriate to let the purchases continue for a while longer, but at a slower pace than before. He therefore supported the proposal for asset purchases in the draft Monetary Policy Report even though he thinks that the rate of purchase could have been reduced a little more than in the proposal.

One factor that has contributed to his continued support for asset purchases is that he does not see any major problems connected to them. This is particularly relevant when the Riksbank now includes inflation-indexed bonds among the purchased assets. Market pricing of these bonds, particularly in the short and medium term, seems to be based on inflation expectations that are considerably lower than those of the Riksbank. Buying inflation-indexed bonds, that are "cheap" in relation to the Riksbank's forecast, may well, according to Mr Flodén, strengthen confidence in the Riksbank's inflation forecast.

In conclusion, Mr Flodén supported the proposal to leave the repo rate unchanged and to continue to buy government bonds, at a slightly slower rate than previously, according to the proposal presented in the draft Monetary Policy Report.

Deputy Governor **Per Jansson** began by noting that there are currently plenty of encouraging signs for the Swedish economy. Inflation has surprised on the upside three months in a row. Outcomes have been higher than expected, regardless of whether developments in energy prices are taken into account or not. In March, CPIF inflation was 1.50 per cent, while CPIF inflation excluding energy prices was 1.86 per cent. The forecasting errors for both inflation measures were in the region of 0.2-0.3 percentage points. Mr Jansson pointed out that one has to go back over six years in time to find a rate of CPIF inflation excluding energy prices that is as high as in March.

Inflation expectations also continue to develop favourably, he proceeded. Expectations one and two years ahead are still below 2 per cent but are clearly rising. Five-year expectations, which can be seen as a measure of credibility of the inflation target, have also risen and overall are close to 2 per cent. In Prospera's most recent survey of money market participants, the inflation rate in five years' time was expected to amount to 1.94 per cent.<sup>1</sup> This continues to provide scope for the Riksbank to "see through" various temporary price shocks. Mr Jansson emphasised, however, that as both inflation and longer-term inflation expectations have been lower than the inflation target for a long time, there is still an elevated risk of even initially temporary price shocks having unusually large and sustained effects on inflation.

In addition, he pointed out that Sweden's GDP growth was very rapid for the whole of 2015 and especially so towards the end of the year. According to Statistics Sweden, seasonally adjusted growth in the fourth quarter was as high as 1.3 per cent. The Riksbank had expected growth to be 0.9 percent. This was an optimistic forecast compared with other Swedish forecasters but the outcome thus even exceeded this forecast by a fair margin. This strong development was a consequence of both rapidly rising domestic demand and high export growth. It is worth pointing out that export growth was solid despite a moderate upturn in demand on Swedish export markets, Mr Jansson noted. There are many indications that it is the depreciation in the Swedish krona exchange rate between 2014 and 2015 that has created the basis for the good export performance. In the period ahead, GDP growth is expected to slow somewhat but will nevertheless continue to be strong, especially in an international perspective.

Mr Jansson observed that the ever-improving economic situation in Sweden is also clearly reflected on the labour market. The employment rate has risen steadily for several years and in 2015 unemployment also fell quite sharply. In the near term, the Riksbank expects a continued favourable development of both employment and unemployment. In the slightly longer term, however, Mr Jansson sees major challenges for the Swedish labour market. Refugee immigration has been extensive and will in the coming years continue to be high in an historical perspective. As it takes time for new arrivals to establish themselves on the Swedish labour market, a

---

<sup>1</sup> According to TNS Sifo Prospera, see <http://www.prospera.se/inflation-expectations/>.

situation where the labour force gradually increases more quickly than employment is unavoidable. Hence, refugee immigration will lead to a rise in unemployment.

The immigration, on the other hand, also constitutes a great potential and without it, the working-age population would decline, Mr Jansson emphasised. Sensibly designed economic policy can help both to hold back the coming upturn in unemployment and to push unemployment back down again in the long run. Succeeding in this is, according to Mr Jansson, the most important task facing Sweden's economic policy going forward. And for us to succeed, a large number of measures will be required within many policy areas, not least improvements in housing policy, in order to create a sufficiently large and broad supply of housing. No measures should be considered off the table; what works should be the guiding principle.

Accordingly, Mr Jansson's assessment was that recent developments in Sweden have, all in all, been strong and that there are good conditions for them to continue to be so for some years yet. With regard to the international economy, there are certainly several risks, and uncertainty continues to be high. But since the middle of February, concern on the financial markets has abated somewhat, with rising equity and oil prices as a result. The stance of monetary policy abroad is also helping to stabilise and improve the situation.

Mr Jansson wished to recall the situation as it prevailed at the time of the monetary policy meeting in February. The repo rate was then cut, despite a number of circumstances indicating that decisions on additional monetary policy measures were not needed. Bearing this in mind, one might think that it is fairly evident that the Riksbank should not "rock the boat" this time around, he continued. As far as he personally was concerned, Mr Jansson identified two circumstances at the monetary policy meeting in February that led him to ultimately vote in favour of a more expansionary policy. Firstly, the fact that the Riksbank made a major and protracted downward revision of the inflation forecast. And secondly, his assessment that both the Federal Reserve and the ECB would choose a soft line in their monetary policy going forward. What it basically was all about was trying to mitigate a risk of the krona exchange rate appreciating too quickly if the Riksbank's monetary policy strategy was perceived to be tighter than before, at the same time as monetary policy abroad was, if anything, going in the other direction.

Mr Jansson noted that, this time, the Riksbank had not made any substantial downward revision of the inflation forecast. Despite this, his assessment was that there was still an overhanging risk of the krona appreciating too quickly if the Riksbank were to decide at today's meeting to refrain entirely from taking additional measures. In this perspective, there was still a danger, according to Mr Jansson, that a decision not to take any additional measures could be perceived as a change in the Riksbank's monetary policy strategy, despite the forecast of inflation not being revised down. Given this background, he supported both the forecast and the monetary policy presented in the draft Monetary Policy Report.

Mr Jansson wished to emphasise that, despite this, he continues to share the view that the Riksbank's preparedness to do more in monetary policy terms should relate to safeguarding the upward trend in inflation and the confidence in the inflation target. As in February, he was still of the opinion that the Riksbank must avoid wasting the monetary policy ammunition that is left and use it only if there is a real need. This is important, not least in order to avoid creating unnecessarily large risks for negative side-effects of the expansionary monetary policy. But as long as a major and rapid appreciation of the krona constitutes a serious threat to the upturn in inflation, it is risky to demand that substantial forecast revisions must precede every decision on new measures. If one does this, it may prove difficult, or, in the worst case, impossible to repair the damage that has already occurred. Monetary policy must therefore continue to be proactive and be conducted with great consideration for the prospects for monetary policy abroad.

Mr Jansson also pointed out that the Riksbank's forecasts are constructed as mean forecasts and should therefore in principle take all prevailing risks into consideration. If, for example, there is a risk of the krona appreciating sharply, this should already be included in the forecasts for different variables. In practice, however, it is difficult to achieve this in a satisfactory manner and it is often necessary to show special consideration for certain risks that may have particularly severe consequences. It is also worth noting that the forecast in the draft Monetary Policy Report is conditional on the currently proposed monetary policy decision. This further subdues the effects on different forecast variables that relate to the risk of a substantial and rapid appreciation of the krona exchange rate, he underlined.

Mr Jansson concluded with a few more specific comments on the Riksbank's preparedness to do more. As he had explained, he had this time decided to vote in favour of continuing to buy securities, for a further SEK 45 billion in the second half of 2016, so that the purchases will amount to SEK 245 billion in total by the end of 2016. In the context, he also supported the proposal to use 15 of these 45 billion kronor to buy real government bonds. In light of the ECB's recent decision to extend its purchases, he saw it as natural to continue to buy securities for a longer period of time. As the Riksbank's holdings of nominal government bonds grow, it is also natural, according to Mr Jansson, to extend the purchases to include other securities. But this does not mean, as pointed out in the draft Monetary Policy Report, that purchases of securities are now the only possible measure if a need to do more in monetary policy terms were to emerge. The report makes it clear that the repo rate's lower bound has still not been reached, that measures can be taken in the operational monetary policy framework to further support the policy being pursued, and that the Riksbank is ready to intervene on the foreign exchange market if the krona appreciates so quickly as to jeopardise the upturn in inflation. As previously, the report also makes it clear that measures can be taken between the ordinary meetings.

First Deputy Governor **Kerstin af Jochnick** began by saying that she supported the assessments in the draft Monetary Policy Report with regard to developments both abroad and in Sweden. She

also gave her support to the proposal to extend purchases of government bonds by a further SEK 45 billion until the end of 2016.

Regarding developments on the financial markets, Ms af Jochnick noted that the situation is possibly a little better now than it was at the time of the last monetary policy meeting in February. The equity markets have recovered slightly but there is still uncertainty around, for example, European banks and their capacity to supply credit. While a great deal of focus has recently been on making banks more robust, parts of the European banking system are still under pressure due to a large proportion of bad loans and the fact that banks' business models have not been adapted to the new conditions. Bank loans announced by the ECB delay the problems but don't make them disappear. There is also a risk of the uncertainty around European banks recreating stress in the market and putting pressure on bank equities. Such a scenario would risk further subduing the upturn in the European economy.

She also pointed out that global growth is increasing but that there are still question marks regarding the pace and size of this increase. The uncertainty surrounding the strength of growth in many countries and weak inflation is leading many central banks to continue pursuing a very expansionary monetary policy. Growth in the euro area is improving but inflation is low. The effects of a possible Brexit are very difficult to assess. In any case, support in the referendum for the United Kingdom to leave the EU will add to the uncertainty that is already hampering growth in both the euro area and Sweden.

Ms af Jochnick also noted that Swedish monetary policy has been very expansionary for a long time, with the aim of supporting developments in the Swedish economy and ensuring that inflation reaches the target of two per cent. The Riksbank has had a difficult task to manage: partly because inflation in Sweden has been low for a long time, and partly because very expansionary monetary policy abroad has created risks that the Swedish krona will appreciate too fast. We are now in a situation where the Swedish economy is doing well in many ways. Growth is good and inflation is rising. Both households and companies are contributing to this development through consumption and investment. There are those who say that the low interest rates are creating uncertainty for households and companies, but this assessment is not backed up by their behaviour. The responses given by companies in the Riksbank's business survey point rather to difficulties in raising prices rather than uncertainty caused by the low interest rate level. Compared with other countries, Sweden has high growth and close-to-normal resource utilisation. Other signs of a high level of economic activity are the number of newly registered cars and the labour shortages in certain sectors.

Inflation has, however, been below target for a long time, Ms af Jochnick continued. There are several reasons for the low level of inflation in recent years. Weak developments abroad have been of significance. Low commodity prices, especially of energy, have held back cost increases. But this is not the entire explanation. In recent years, companies' profit margins have been under

pressure and they have found it difficult to raise prices. In surveys, companies themselves have indicated that this may be due to increased uncertainty about the future and greater competition. Globalisation and ever-greater online shopping have probably played a significant role, she thought.

Ms af Jochnick noted, however, that CPIF inflation has shown an upward trend since 2014 and the krona depreciation that occurred in 2014 and the first half of 2015 is deemed to be an important cause of the upturn. She pointed out that the krona has, however, strengthened since mid-2015, but that rising resource utilisation in the Swedish economy has simultaneously contributed to a trend rise in more domestically determined service prices. She stated that the development of inflation in 2016 is expected to be uneven for a variety of reasons and that it will take more time before inflation is more permanently close to the target. Energy prices have fallen over the past year and price increases for imported goods are slowing down as a result of the recent krona appreciation. This means that the Riksbank does not expect the CPIF to stabilise around 2 per cent until 2017.

Ms af Jochnick further emphasised that although the Riksbank does not have a target for the exchange rate, the development of the krona is important when it comes to assessing inflation. The Riksbank's assessment is based on a slow appreciation of the krona. As resource utilisation in the economy increases and we see labour shortages emerging in certain industries, it is reasonable to assume that this will be reflected in companies raising their prices for products and services and that the krona will play a lesser role.

To safeguard the upward trend in inflation and to continue to support developments in the Swedish economy, it is Ms af Jochnick's assessment that the Riksbank should continue its government bond purchasing programme until the end of the year. She believes that, in this situation, it is reasonable for the Riksbank to buy government bonds at a slightly slower pace, while broadening the purchases to include real bonds in order to have a wide impact on different interest rates.

Furthermore, Ms af Jochnick noted that housing prices in Sweden are continuing to rise rapidly. The Riksbank has previously highlighted the problems of high housing prices and household indebtedness but there is also an ever-greater risk that the problems on the Swedish housing market will affect companies' assessment of how attractive it is to operate in Sweden. This may have effects on growth and development in the longer term. When the Riksbank, in the draft Monetary Policy Report, talks about the risks associated with low interest rates, it is Ms af Jochnick's assessment that one of the greatest risks continues to be households' growing debts. Price developments on the housing market mean that households are taking on more and more debt. This is also evident from Finansinspektionen's most recent mortgage survey.

Ms af Jochnick also noted that housing prices in recent years have increased significantly more than household incomes. The average debt-to-income ratio is now over 400 per cent in

Finansinspektionen's survey and more than 35 per cent of households with new mortgages have a debt-to-income ratio of over 400 per cent. Ever-higher household indebtedness increases the vulnerability of the Swedish economy and, with a higher level of interest rates, risks hampering growth and ultimately the Riksbank's possibility of achieving the inflation target. Ms af Jochnick wished therefore to once again underline how important it is to limit the build-up of debt by households in different ways.

Deputy Governor **Cecilia Skingsley** began by saying that she supported the forecasts presented in the draft Monetary Policy Report. However, she did not support the proposal to extend the programme for bond purchases.

Prior to the monetary policy decision in February, there was unease on the international financial markets, with occasionally severe market fluctuations. Since then the volatility has declined, although the uncertainty over global economic developments remains high. In February, adjustments were made to the forecasts implying that the Swedish inflation target would be attained further ahead in time. According to Ms Skingsley, this meant it was reasonable to cut the repo rate to -0.5 per cent. Since then, the Swedish economy has continued to develop well. Resource utilisation can be described as normal and inflation data has been as expected or somewhat higher. In other words, the surprises have been relatively small.

An important question for Ms Skingsley with regard to today's decision was the prospects for the international economy. International growth was muted at the end of 2015 and indicators turned down at the beginning of 2016. However, the assessment was that the economies that are most important for Swedish foreign trade had temporary slowdowns and the forecast indicates continued recovery. Another important element in the assessment of domestic price pressures is that the results of the wage bargaining rounds so far have not led to any major revision in the wage forecasts.

The forecast revisions in the draft Monetary Policy Report are minor on the whole, but they include a decision to make further bond purchases during the second half of the year. However, Ms Skingsley's assessment is that the forecast revisions would have been acceptable even without the bond purchases. The Riksbank's forecasts are formulated so that the risks of a worse outcome are, in principle, as large as the risks of a more favourable outcome. But the monetary policy decision also entails making an assessment of the risks that are not so easily captured in the figures of the macro forecasts. One example of such a risk is that the impact of monetary policy has deteriorated after a long period of low inflation and reduced confidence in the inflation target. For Ms Skingsley this has been an important reason for supporting the expansionary monetary policy over the past year. Another assessment that must be made partly outside of the forecasting spreadsheets concerns the risk of undesirable capital movements that could jeopardise developments in economic activity and inflation.

Since February, the European Central Bank has made new stimulus decisions. Furthermore, the Federal Reserve has signalled a slower pace for its rate increases. These are circumstances that Swedish monetary policy must take into account, according to Ms Skingsley. However, much of this was already known at the monetary policy meeting in February, and was part of the reason why she supported the decision to cut the repo rate then.

She sees today's choice of stance, to extend the programme for buying government bonds or not, as a question of risk assessment. One advantage of taking action now and providing stimulus in the form of extending this programme is that inflation is currently driven by the earlier krona depreciation. This is a driving force that will soon wane and there is still low tolerance for a significantly larger krona appreciation than in the Riksbank's forecast. Although domestic price pressure is beginning to increase, it is still uncertain how this will develop. Ms Skingsley's assessment is, however, that this risk factor has not increased since February, but remains roughly the same.

Ms Skingsley also said that the Riksbank has long been clear with regard to being highly prepared to do more if necessary, even between the ordinary monetary policy meetings. All of the tools described earlier, the repo rate, the repo-rate path, the bond purchases and direct foreign exchange interventions are still available. And given the rising resource utilisation in the Swedish economy and the fact that inflation is expected to be close to 2 per cent in the coming year, the scope for waiting to see what happens is greater now. A strict interpreter of the inflation-targeting regime could claim that this is not sufficient. At present, with weak international price pressures, domestic prices need to be pushed up instead, to ensure the inflation target of 2 per cent is attained. But according to Ms Skingsley, such monetary policy would be contradictory to the actual spirit of the flexible inflation-targeting regime, namely to stabilise inflation around the target, while endeavouring to stabilise production and employment around paths that are sustainable in the long term.

Ms Skingsley then explained, to sum up, that she shares her colleagues' views on economic prospects in the draft Monetary Policy Report, but that she makes a different assessment of the risks. This has brought her to a different assessment of the need to extend the bond purchases, and she has drawn the conclusion that there is scope to await a decision on further stimulus.

Governor **Stefan Ingves** began by explaining that he agrees with the description of the current situation in the draft Monetary Policy Report. As he sees it, today's decision is a form of intermediate decision with regard to continuing down the chosen path to bring inflation back on target. He supports the monetary policy now being proposed and considers it a well-balanced policy not to touch the repo rate and to continue with and even extend the bond purchases to include real bonds. This is also a way of showing that the Riksbank has the technical preparedness to extend the securities purchases if necessary. Monetary policy will thus remain very expansionary for a further period of time. Inflation is on the way up, but is not yet on target.



Inflation abroad is low. The price falls of the past year on oil and other commodities mean that inflation will remain low in 2016. However, expansionary monetary policy in several countries will contribute to improving economic activity and to rising inflation. All in all, inflation abroad (KIX-weighted) is expected to increase from just over 1 per cent in 2016 to just over 2 per cent in 2017 and 2018. The challenge is to attain in the near future an inflation rate that is somewhat higher than that abroad, this applies not least in comparison with the EMU.

Inflation in Sweden has been somewhat higher than expected during the first quarter of the year. However, CPI inflation has been held back by falling interest costs and is still low. In contrast, CPIF inflation has shown a rising trend since the beginning of 2014. Among the CPI sub-groups, the clearest rise can be seen in the rate of price increase among goods and food. The depreciation of the krona that took place in 2014 and up to the middle of 2015 is assessed to be an important reason for the upturn. Since the middle of 2015, the krona has appreciated and the rate of price increase has slowed down with regard to both goods and food. At the same time, there has been a trend rise in the more domestically determined service prices, adjusted for rents, foreign travel and taxes, among other things. This upturn is considered to be due to rising resource utilisation in the Swedish economy. It also shows that the monetary policy stimulus has had an effect. As the same time, the forecast assumption of rising service prices is very important as a slow appreciation in the krona means it is not possible to count on any major inflationary impulse from import prices.

Despite the strong growth and resource utilisation close to normal, inflation is expected to rise slowly in 2016. Energy prices have fallen over the past year and price increases for imported goods are slowing down as a result of the recent krona appreciation. Towards the end of 2016, CPI and CPIF inflation are expected to rise relatively quickly. One reason is that energy prices and interest expenses, which fell earlier, are no longer subduing the rate of inflation to the same extent.

However, there is still considerable uncertainty on a number of points. Central factors here are the low inflation and monetary policy abroad. Monetary policy abroad has been expansionary for a long time and was made even more expansionary after the new year. In the euro area, the ECB decided to cut its policy rate in March, and to extend the asset purchase programme, as well as announcing new long-term loans to the banks. In the United States, the Federal Reserve held its policy rate unchanged in March. Indications were also given that, going forward, the interest rate would be raised at a slower pace than was previously assumed.

These measures were largely expected. Mr Ingves noted at the previous monetary policy meeting that it is still important that the Riksbank is not afterwards forced to react to monetary policy abroad becoming more expansionary. It is much more difficult to manage increased monetary policy stimulus abroad after the event. This contributed to the decision in February to make monetary policy more expansionary. The base scenario is a protracted normalisation, with a

continued very expansionary monetary policy abroad, and this will of course spill over into a small open economy like Sweden's.

One factor that is affected by monetary policy abroad, is the yield differentials. Yield differentials against Germany declined up to the middle of 2015 and then began to rise again. For instance, the yield differential for 10-year government bonds declined to around zero per cent in the middle of 2015, but has since then risen to more than 0.5 per cent. When the yield differential has increased again, the krona has strengthened somewhat against other currencies. This contributes to the inflation upturn not yet being on firm ground. An overly rapid krona appreciation could risk prolonging the period of low inflation and could weaken confidence in the inflation target.

Mr Ingves pointed out that we in Sweden are in an unusual macroeconomic situation and he outlined a scenario to illustrate this. In this scenario, the ECB needs to take more measures going forward to make its monetary policy more expansionary. Moreover, the Federal Reserve needs to wait for longer before reducing its monetary policy stimulus. Mr Ingves wondered how we would communicate Swedish monetary policy if such a scenario were to become reality. Would it be possible to refer to the output gap being closed and to raise the repo rate? This is not at all obvious. Because what would then happen to the krona? What would happen to inflation? It is a strange combination we see before us of a positive output gap in the Swedish economy at the same time as the repo rate remains negative. Mr Ingves said that at present he does not have any answers to these questions but he noted that it would have been difficult to imagine the current situation 20 years ago, when the inflation target was established. Today's "figure combinations" appear rather unique.

Mr Ingves pointed out that it is no longer possible to expect a weaker exchange rate to contribute to higher inflation and that as he has already noted, there are evident risks that the krona will strengthen. A key question for Swedish monetary policy is therefore whether domestic demand will actually continue to function as a driving force behind inflation. Furthermore, it will take time before increased demand has a full impact on inflation. According to a study, there is a time lag of almost two years between a change in resource utilisation and its maximum effect on inflation.<sup>2</sup>

There is also another, more traditional, monetarist way of looking at monetary policy by focusing on the money supply and credit growth. Credit granting to households and companies is increasing. In February the annual rate of increase in bank loans to households was unchanged at 7.5 per cent and the money supply is growing much faster than GDP. It is difficult to imagine that such rates of increase in lending to households will not lead to a rise in prices for goods and

---

<sup>2</sup> Andersson, Björn, Corbo, Vesna and Mårten Löf (2015), "Why has inflation been so low?", *Sveriges Riksbank Economic Review*, 2015:3.

services. But there are, of course, also time lags between the increase in the money supply and higher inflation.

This presents the Riksbank with an obvious dilemma as most of the lending is to households' home purchases, which pushes up housing prices and household indebtedness, and not to corporate investment. Unfortunately, it is a fact that the best forecast variables for a coming bank crisis in a country are housing price rises and increasing indebtedness in the household sector, Mr Ingves pointed out. A much higher policy rate could contribute to slowing down the build-up of debt in the household sector. But this would be at the cost of a severe slowdown in the economy, rising unemployment and even lower inflation. The conclusion is that fundamental reforms are needed in the housing market, as well as reduced incentives for households to take on debt and a review of the framework for macroprudential policy. Otherwise there are considerable risks to economic stability in Sweden, said Mr Ingves.

There are also political risks that could lead to weaker confidence in the European Union, which would have repercussions on Sweden. This concerns, for instance, difficulties for the EU in managing the refugee immigration. Another risk is the outcome in the referendum on British membership of the EU. It is difficult to assess the probability of the United Kingdom leaving the EU and the possible consequences of this outcome. However, there would most probably be clear disadvantages for the Swedish economy and international cooperation. Another evident risk concerns Greece, which does not yet meet the conditions set for attaining its bailout programme objectives. These are political risks, which are always difficult to quantify but also increase the risks for Swedish monetary policy.

Mr Ingves then rounded off by presenting his conclusions regarding monetary policy. Over the past year, the repo-rate cuts have been supplemented with purchases of nominal government bonds and the current purchase programme expires at the end of June 2016. If inflation does not rise as expected, this could impact confidence in the inflation target. To ensure that the trend in inflation continues, it is appropriate to continue with the securities purchases for the remainder of the year. This reduces the risk of the krona appreciating earlier and faster than forecast. It requires continued preparedness to take further measures, even between the ordinary monetary policy meetings. It is possible, for instance, to cut the repo rate further, and to buy more securities. It is also worth repeating that the Riksbank is prepared to intervene on the foreign exchange market at short notice if the development of the krona threatens the upturn in inflation.

Deputy Governor **Henry Ohlsson** began by expressing support for the proposal to hold the repo rate unchanged at -0.5 per cent and to also hold the repo-rate path unchanged. He also supported the proposal to extend the programme for purchasing government bonds.

At present, GDP growth in Sweden is high. According to the forecast in the draft Monetary Policy Report, growth will be clearly above the historical average over the coming year and will remain at a high level thereafter. Another important observation is that global trade in goods is increasing again, after a decline that has proved to be temporary. This is very important for a small, open, export-dependent economy like Sweden's. Resource utilisation in the Swedish economy is also normal and is expected to become even higher. This suggests that inflation should rise as resource utilisation increases. Another important observation is that consumption of durable goods is increasing. Mr Ohlsson interprets this to mean that households have confidence in the future and are expecting a good economic development in the coming years.

The inflation rate is still showing a rising trend. The monthly measurements are varying in an irregular manner and are strongly affected by temporary factors. Sometimes the outcomes are higher than expected, and at other times they are lower than expected. Mr Ohlsson's firm opinion is that the rising trend is nevertheless clear. It is important to attain the inflation target, but it is also important to realise that this can take time.

The most recent measurement in April showed the expected annual rate of inflation five years ahead to be 1.9 per cent, according to money market participants. This is close to, but below, the inflation target. At the same time, we can see that inflation expectations one and two years ahead are below the inflation target, but also showing a rising trend. The April figures are 1.1 and 1.6 per cent respectively.

The labour force surveys (LFS) for February 2016 report an unemployment rate of 7.6 per cent (not seasonally adjusted). This is a welcome decline of 0.8 percentage points compared to the corresponding month a year earlier. Unemployment has thus declined over the past year, but is still too high, in Mr Ohlsson's opinion.

When he weighs the need for a more expansionary monetary policy against the risks linked to an even more expansionary policy, and when he looks at the advantages and disadvantages of the monetary policy measures at the Riksbank's disposal, Mr Ohlsson can only come to the conclusion that the repo rate and the repo-rate path should be held unchanged. On the other hand, he considers that the government bond purchases should continue, even during the second half of 2016. At the same time, he considers that the pace for these should be slowed down. One can discuss whether SEK 45 billion is the most appropriate amount, but Mr Ohlsson was not prepared to enter a reservation at today's meeting in favour of a lower amount.

Mr Ohlsson's reasons for these stances are that he is convinced that the monetary policy decided so far and the continued bond purchases are sufficiently expansionary. It is important to have patience and to await the effects of the expansionary monetary policy on the inflation rate.

However, there are threats. Too rapid an appreciation of the krona could threaten the chances of attaining the inflation target. Although monetary policy does not have a target for the exchange rate, developments in the exchange rate affect developments in inflation. Mr Ohlsson assessed that there are situations where interventions on the foreign exchange market are the best alternative in counteracting a development where the krona appreciated too rapidly. He also noted that the krona has appreciated by almost 3.5 per cent in KIX terms since the second quarter of 2015 and up to and including the first quarter of 2016, at the same time as inflation has shown a rising trend towards the target.

An important starting point for Mr Ohlsson is that rising inflation should not only come from a weaker krona. As he sees things, it is more a question of attaining the inflation target through price increases that result from increased domestic activity, or in other words, increased domestic resource utilisation.

He thus considers it to be a well-balanced monetary policy, taking into account the need for and risks with a more expansionary monetary policy, and in the current situation for the Swedish economy, to hold the repo rate and the repo-rate path unchanged and to extend the programme for purchasing government bonds. He also supported the draft Monetary Policy Report.

Governor **Stefan Ingves** then summarised the discussion. He noted that the Executive Board agreed on the picture of economic prospects and the inflation outlook described in the draft Monetary Policy Report.

Several members mentioned risks linked to uncertainty on the financial markets and to economic prospects abroad. The members also noted that international inflation is low and that several central banks are expected to conduct very expansionary monetary policy.

In Sweden, resource utilisation is currently close to normal, and economic activity is expected to continue to strengthen. Inflation has been slightly higher in recent months than the forecast in February. But although the forecast for inflation has been revised up slightly for the next few months, it is expected to be lower than the target for 2016, too.

The Executive Board agrees that monetary policy needs to continue to be very expansionary. However, the members have slightly different views as to whether it is appropriate to extend the government bond purchasing programme.

On the one hand, the Swedish economy is characterised by high growth and an ever-stronger labour market, and inflation has been higher than expected for several months. Rising resource utilisation also creates good conditions for a continuation of the upward trend in inflation. This may be an argument for not prolonging government bond purchases.

On the other hand, the upturn in inflation is uneven and to a high degree has been driven by a weak krona. A continued positive economic development in Sweden is therefore needed to safeguard the upward trend in inflation. At the same time, uncertainty in the wider world remains and several central banks are conducting a very expansionary monetary policy. The inflation forecast is thus highly sensitive to various international factors. This is an argument for extending the government bond purchasing programme to mitigate the risk of the krona appreciating too quickly, which would lead to weaker demand for Swedish exports and lower inflation.

A majority of the Board members considered it appropriate to continue buying government bonds for a further SEK 45 billion during the second half of 2016. To achieve a broad impact on different interest rates, the purchases should include both nominal and real government bonds corresponding to SEK 30 billion and SEK 15 billion respectively. Until further notice, maturities and coupons from the portfolio of both nominal and real government bonds will be reinvested. One board member considered that monetary policy is sufficiently expansionary for inflation to rise towards 2 per cent, and that it is therefore unnecessary to extend the purchases of government bonds.

The Executive Board was unanimous in holding the repo rate at –0.50 per cent, and, as in February, expects to begin raising the interest rate slowly in mid-2017.

The Executive Board is also unanimous as regards having a high level of preparedness to make monetary policy even more expansionary, even between ordinary monetary policy meetings, if this is needed to safeguard confidence in the inflation target.

### **§3. Decision on the Monetary Policy Report and the repo rate**

The Executive Board decided

- to adopt the Monetary Policy Report according to the proposal, Annex A to the minutes, and
- to hold the repo rate at -0.50 per cent.

### **§4. Decision to purchase government bonds**

Heidi Elmér presented this agenda item.

The Executive Board decided in accordance with the proposal, Annex B to the minutes.

Deputy Governor Cecilia Skingsley entered a reservation against the decision to purchase further bonds to a value of SEK 45 billion. She advocated an unchanged monetary policy with reference to the economic situation in Sweden.

## §5. Other decisions

The Executive Board decided

- to publish the Monetary Policy Report and the decisions under Sections 3 and 4 at 9.30 a.m. on Thursday 21 April 2016 with the motivation and wording contained in a press release, and
- to publish the minutes of today's meeting on Wednesday 4 May 2016 at 9.30 a.m.

Sections 3 - 5 were verified immediately.

Minutes by

Sophie Brauner

Verified by:

Stefan Ingves

Martin Flodén

Per Jansson

Kerstin af Jochnick

Henry Ohlsson

Cecilia Skingsley



**SVERIGES RIKSBANK**  
SE - 103 37 Stockholm  
(Brunkebergstorg 11)

Tel +46 8 - 787 00 00  
Fax +46 8 - 21 05 31  
[registratorn@riksbank.se](mailto:registratorn@riksbank.se)  
[www.riksbank.se](http://www.riksbank.se)