



Sveriges Riksbank

ANNUAL REPORT 1998



The objective of the Riksbank is
to maintain price stability
besides promoting a safe and
efficient payment system

The Riksbank thereby contributes to
sustainable growth and
increased employment

1998 in brief

- *Governing Board appointed by the newly elected Riksdag on 21 October.*
- *New Riksbank legislation approved by the Riksdag on 27 November.*
- *New Governing Council, as of 1999, appointed by the Riksdag on 2 December.*
- *The six members of the new Executive Board, as of 1999, appointed by the Governing Council on 17 December.*
- *The Riksbank decides on 4 June to lower the repo rate from 4.35 to 4.10 per cent.*
- *The Riksbank decides on 3 November to lower the repo rate from 4.10 to 3.85 per cent.*
- *The Riksbank decides on 12 November to lower its borrowing and lending rates, in each case by 0.5 percentage points, to 3.25 and 4.75 per cent.*
- *The Riksbank decides on 24 November to lower the repo rate from 3.85 to 3.60 per cent.*
- *The Riksbank decides on 15 December to lower the repo rate from 3.60 to 3.40 per cent.*
- *The Riksbank signs the ERM₂ Agreement in September; the krona is not participating*
- *The Riksbank participates in IMF support, totalling about USD 41.5 billion, for Brazil.*
- *The Riksbank, together with the Financial Supervisory Authority and financial firms, forms a joint council for the coordination of general measures for the Year 2000 transition.*
- *More than two persons out of three in Sweden support the Riksbank's 2 per cent inflation target.*
- *Seven old banknotes demonetised at the turn of 1998.*
- *Four Inflation Reports and two Financial Market Reports published during the year.*

Selected statistics	1998	1997	1996
Year-end figures:			
Repo rate (per cent)	3.40	4.35	4.10
Money rate (three-month, per cent)	3.43	4.52	3.62
Bond rate (ten-year, per cent)	4.18	5.98	6.71
Exchange rate (TCW)	130.60	121.51	117.83
SEK/DEM	4.8512	4.4185	4.4325
SEK/USD	8.1320	7.9082	6.8859
Annual figures:			
GDP growth (per cent)	2.9	1.5	1.3
Unemployment (per cent)	6.5	8.0	8.1
CPI change (per cent)	0.4	0.9	0.8
Balance on current account (SEK billion)	38	51	44
Balance of trade (SEK billion)	140	141	125
Government borrowing requirement (SEK billion)	-10*	0	21

* Preliminary figure.

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The Riksbank's objective is price stability

The Riksbank is the Swedish central bank and is accountable for monetary policy.

The objective of the Riksbank's operations is to maintain price stability.

Monetary policy's principal instrument for maintaining price stability is the repo rate – the rate for bank financing in the Riksbank. The Riksbank adjusts the repo rate to influence the level of economic activity and hence in time the development of prices.

The Riksbank is also required to promote a safe and efficient payment system.

The Riksbank fulfils this objective by supplying currency in the form of notes and coins, holding credit balance on accounts, providing a basic infrastructure in the form of systems for the distribution of cash, the RIX system and so on, and carrying responsibility for the oversight of payment transactions.

Moreover, without prejudice to the objective of price stability, the Riksbank is to support general economic policy with a view to achieving sustainable growth and high employment.

INFLATION TARGETED SINCE 1993

Since the beginning of 1993 the Riksbank has conducted monetary policy with an inflation target formulated by the Governing Board. Inflation is to be held to an annual rate of 2 per cent, with a tolerance interval of ± 1 percentage point.

PRICE STABILITY OBJECTIVE ENSHRINED IN LAW

On 25 November 1998 the Riksdag (Sweden's parliament) passed legislative amendments with the aim of strengthening the independence of the Riksbank. The new legislation applies from 1 January 1999. The most important component is the statutory objective for monetary policy.

At its first meeting, in the beginning 1999, the Executive Board decided that the current formulation of the monetary policy target continues to apply. Monetary policy will go on aiming at keeping the change in the consumer price index at 2 per cent with a tolerance interval of ± 1 percentage point. There is reason, however, to clarify the formation of monetary policy.

Monetary policy normally aims at fulfilling the 2 per cent target in twelve to twenty-four months time. There are two grounds for departing from this rule. One is that in the relevant time perspective the consumer price index may be pushed upwards or downwards by one or more factors that are not considered to affect inflation more permanently. Changes in interest expenditure, indirect taxes and subsidies are examples of such factors. The other reason is that a quick return to the target in the event of a sizeable deviation can sometimes be costly for the real economy. If either of these situations occurs, the magnitude of the deviation from the target, defined in terms of the CPI, that may be motivated one to two years ahead will be clarified by the Riksbank in advance.

Such a clarification facilitates an appraisal of monetary policy's performance.

The new legislation closely corresponds to economic policy's grounds for a more independent central bank. A price stability objective is liable to carry little weight if people are not convinced it will be observed. Giving the objective an institutional foundation in various ways can strengthen its credibility and thereby improve the effectiveness of monetary policy. One way of providing such an institutional foundation is to give monetary policy the statutory function of fulfilling the price stability objective and delegating the conduct of monetary policy to an independent cen-

tral bank that is free to formulate monetary policy so that this objective is fulfilled.

A framework for monetary policy, consisting of a central bank with a demarcated independence to fulfil a price stability objective under democratic control, has been the foundation for central bank reforms in several other countries. This approach also lay behind the construction of the institutional framework for the European Central Bank (ECB) as expressed in the Maastricht Treaty and in the statutes of the European System of Central Banks (ESCB) and the ECB.

A turbulent year in financial markets

During 1998 the unrest in international financial markets that had started the year before in Asia became more pronounced. The international crisis prompted a successive downward revision of international economic prospects and also affected the outlook for economic growth in Sweden. However, notwithstanding considerable problems in other parts of the world, during the year Sweden's financial system continued to display stability.

FINANCIAL CRISES

Developments during 1998 and their consequences for the work of the Riksbank were strongly influenced by crises in international financial markets. The turbulence in financial markets was markedly accentuated when the Russian government announced a debt moratorium in the middle of August. Attempts to limit existing losses, together with concern about additional losses, caused investors to dispose of assets they perceived as risky and illiquid. Minor currencies, such as the Swedish krona, weakened and borrowers with unfavourable credit ratings were obliged to pay increasingly high interest rates.

The mood among investors became still more nervous in the light of the problems with the U.S. hedge fund Long Term Capital Management. There were growing fears that the situation could result in a general liquidity crisis and that banks would have difficulties in performing their basic economic function of supplying loans to households and firms that are deemed to be creditworthy. Such a development might also affect real economic activity. In order to prevent such a situation from arising, a number of central banks lowered their instrumental rates.

SWEDEN'S BANKING SYSTEM REMAINED STABLE

The problems in the international bank market never occasioned any widespread

instability in Sweden's banking system during the year. The direct exposures of Swedish banks were small, both to the emerging markets and to counterparties with high levels of risk. This is probably an effect of the bank crisis in Sweden in the early 1990s – the banks have become more prudent and also improved their risk assessment capability.

Another consequence of the Swedish bank crisis is that the authorities have intensified their efforts to prevent new risks from arising. For the Riksbank this involves a continuous analysis of financial market tendencies; the findings are presented twice a year in the Financial Market Report. The Financial Market Report from November 1998 contained an analysis of counterparty risks in the banking system. The Report proved highly topical in that it was counterparty risks which lay behind the autumn's widespread problems in western financial markets.

This analysis completed the Riksbank's presentation of the intellectual framework for its work of overseeing the stability of the financial system as a whole. The other two main components – the banking system's competitiveness and its credit risks on loans to households and firms – have been presented in detail in earlier issues of the Financial Market Report.

The Riksbank is also a participant in the international cooperation for strengthening the financial system. The work on EMU preparations was, however, less intensive during 1998 because the Riksdag decided that Sweden would not adopt the euro from the start. The ongoing work is governed by the Riksbank's ambition that, in the event of a decision to participate in the euro area, the preparations for which the Riksbank is responsible shall have been completed after an interval of not more than a year.



NEW MANAGERIAL STRUCTURE FOR THE RIKSBANK

As of 1999 the Riksbank is operating under new legislation. The amendments can be said to have formalised the independence that already characterised the Riksbank's ongoing work. One of the most notable changes is probably the altered organisation that the new legislation prescribes. The Riksbank is now managed jointly by the six full-time members of the new Executive Board, who also make the monetary policy decisions.

STOCKHOLM, APRIL 1999


URBAN BÄCKSTRÖM
GOVERNOR

Government decides the exchange rate system

The current regime, whereby the Government decides the exchange rate system, has had many predecessors, such as the gold standard, the currency snake and the currency basket.

On 19 November 1992 the Riksbank abandoned the fixed exchange rate regime. The change to a flexible rate came after a turbulent autumn in European financial markets. Finland had suspended the markka's ecu link in September and sterling and the Italian lira were withdrawn from the Exchange Rate Mechanism.

The fact that the Riksbank's Governing Board, not the Government, decided the exchange rate system distinguished the Riksbank from most other central banks. As of 1999, however, new legislation prescribes that the Government decides the exchange rate system.

Sweden has had a fixed exchange rate for most of this century, though its construction has varied. Under the gold standard the Riksbank undertook to exchange kronor for gold at a fixed rate; this set the krona's value in relation to other countries on the gold standard. The Swedish krona has also been linked directly to sterling as well as to the U.S. dollar. Other fixed exchange rate systems have been the European currency snake, the currency basket and the ecu peg. The krona's fixed rates with the basket and the ecu are instances of unilateral undertakings by Sweden, while the krona's participation in the currency snake was based on international agreements.

The change from the gold standard to a flexible exchange rate at the outbreak of World War I was generally regarded as temporary. After the war, Sweden was the first country to return to the gold standard, in 1924. The krona came off the gold standard again in September 1931; the fixed exchange rate was replaced by a price stabil-

ity objective for the Riksbank. For the first time, a central bank had the explicit objective of stabilising the price level.

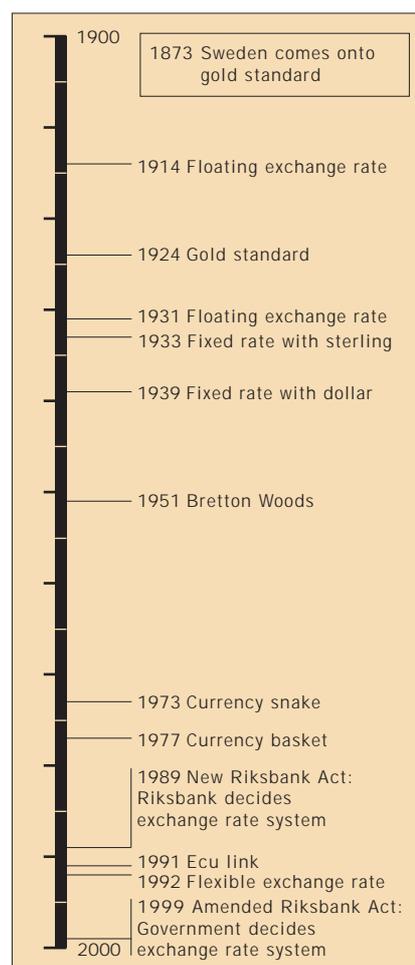
Once again, the flexible exchange rate was seen as temporary and in April 1933 the krona was linked to sterling. When the run-up to World War II led to rapidly rising inflation in Britain, the krona was linked to the U.S. dollar in August 1939.

International agreements for fixed exchange rates were concluded in Bretton Woods in 1944. A fixed value in gold was assigned to the U.S. dollar, together with fixed dollar rates for other currencies. Sweden joined the system in August 1951.

In 1972, Bretton Woods gave way to the European currency snake, in which the participating currencies were linked to each other but floated freely against other currencies. Sweden joined in March 1973.

Sweden participated in the snake until August 1977. In April that year the krona had been devalued, on the Government's initiative, by up to 6 per cent against the other snake currencies. When Sweden left the snake and adopted a fixed exchange rate in relation to a basket of currencies, the krona was devalued another 10 per cent.

The basket currencies were weighted with each country's share in Sweden's foreign trade, except that for the U.S. dollar which weight was doubled. The first five years with the currency basket saw two more krona devaluations. The Riksbank Governor, Lars Wohlin, took the initiative for the 10 per cent devaluation in September 1981, while the 16 per cent devaluation in October 1982 was decided in practice by the incoming Social Democrat Government. The krona's central rate with the basket was then maintained for the rest of the 1980s even though inflation in Sweden was, on average, around two percentage points above the OECD level.



In the 1980s, real independence for the central bank was increasingly emphasised as important for achieving price stability. This led to a new Riksbank Act in 1988, with the provision that, following consultation with the Government, the Riksbank is to decide the exchange rate system. This procedure was used twice: on 17 May 1991, when the currency basket was replaced by a link to the ecu, and on 19 November 1992, when the krona was left to float.

The year in review

Global economic development in the period of relevance for monetary policy will probably be somewhat weaker than estimated earlier. For this reason the outlook for inflation is somewhat more favourable. The probability of an outcome for wages that is appreciably above the main scenario has diminished. At the same time, the effects of the Asian crisis are highly uncertain. The conclusion is that at present there is no reason to alter the repo rate. *Governor Urban Bäckström, Stockholm Chamber of Commerce and Veckans Affärer, 27 January.*

The prospects for inflation from the demand side look a bit better than they did when the repo rate was last raised. Another positive sign is that the wage agreements which have been concluded so far in 1998 indicate a rate of wage increases that is somewhat lower than in the main scenario described in December. However, the recent weakening of the krona is a cause for concern. *Deputy Governor Lars Heikensten, Economics Association, Umeå, 19 February.*

Economic development in Sweden in the coming two years should be fairly favourable, with good growth, some increase in employment and moderate inflationary pressure. The crisis in Asia can be said to result in some deferment of the ongoing monetary policy realignment. *Urban Bäckström, Riksdag Standing Committee on Finance, 12 March.*

In the latest Inflation Report we considered that in the coming twenty-four months the rate of inflation would tend to rise but somewhat more slowly than we had expected earlier. The prospects pointed to a cautious tightening of the monetary stance in the coming twelve months. New statistics have been published since then but they do not entail any substantial changes in our outlook. *Lars Heikensten, Shareholders Association, Trelleborg, 21 March.*

Most of the evidence suggests that economic growth in Sweden will become stronger in the coming two years. To date, however, subdued price movements have accompanied the upswing. This mainly reflects a number of favourable transitory effects but there may also be signs of a somewhat lower inflation propensity. The strength displayed by productivity may perhaps enable the Swedish economy to expand somewhat faster without immediately generating inflationary pressure. But it is still too early to form a more definite opinion on whether the productivity trend has changed. It is now important that incoming statistics are followed closely and assessed. There is no reason at present to alter the repo rate. *Urban Bäckström, Monetary Policy Forum, 22 April.*

Like many central banks in central Europe, the Riksbank has moved from a situation that pointed to the likelihood of a relatively quick succession of continued interest rate increases to one where the need of higher interest rates in the near future seems to have disappeared. With the bright inflation prospects and a strict interpretation of the Riksbank's rule for monetary policy decisions, today there may even be grounds for considering a minor downward repo rate adjustment. *Lars Heikensten, Almega-affiliated Employers' Associations, 27 May.*

In the June Inflation Report the Riksbank's overall assessment of inflation in the coming years was adjusted downwards. As the rate of inflation twelve to twenty-four months ahead was judged to be below the target, the Riksbank considered that, at least for a time, there was room for a somewhat more expansionary monetary stance. The repo rate was therefore lowered 25 basis points. *Lars Heikensten, Local Authorities Economics Seminar, Malmö, 19 August.*

On the basis of theoretical analyses of

what ought to determine a country's use of a currency, together with information the Riksbank has obtained from interviews and surveys of Swedish firms and households, we have concluded that the introduction of the euro will not appreciably alter the role of the krona in the Swedish economy. *Lars Heikensten, World Trade Day, 25 August.*

Despite good economic fundamentals in Sweden, since the summer the krona has weakened sharply and last week this tendency accelerated. In a matter of days the exchange rate with the German mark declined by up to 5 per cent. In that situation the Riksbank decided to intervene in the foreign exchange market, which nowadays is unusual. We did so to demonstrate that we considered the krona's fall was excessive in relation to the fundamental state of the economy. *Urban Bäckström, Swedish Shareholders Association, 10 October.*

The assessment that growth in the rest of the world will be weaker than we counted on earlier led the Riksbank to conclude that with an unchanged repo rate, in the coming twelve to twenty-four months the rate of inflation would be below the target. The effects on inflation from the slowing tendencies were judged to be greater than the stimulus from the weaker exchange rate. Under these circumstances, on 3 November the Riksbank lowered the repo rate 25 basis points to 3.85 per cent. *Urban Bäckström, Standing Committee on Finance, 13 November.*

Today I have concentrated on the financial system in the longer perspective. But in the midst of all the uncertainty about the present situation, there is one thing about which we can be quite sure: this is not the last financial crisis. The financial market players – savers, investors, fund managers, supervisors and overseers – must not lower their guard. Not again. *Lars Heikensten, Shareholders Association, 30 November.*

Inflation expectations remain low

The objective of monetary policy is price stability. The Governing Board of the Riksbank formulated this objective in January 1993 and it has applied since the beginning of 1995. Inflation, measured as the change in the consumer price index (CPI), is to be held at an annual level of 2 per cent, with a tolerance interval of ± 1 percentage point. The inflation target is evaluated in an annual perspective.

In the four years, 1995–98, since the inflation target became operational, the CPI has risen at an average annual rate of 1.2 per cent. This is below the target but it does mean that the average change in the CPI has been inside the tolerance interval. With the retardation of inflation and the establishment of confidence in the inflation target, interest rates have fallen. The lower interest rates have dampened the rate of price increases and are an important reason why inflation has been below the target in these years. The underlying rate of inflation in this period has been close to the target, with average increases of 1.8 per cent for UND1X and 2.3 per cent for UNDINH.

During 1998 the average rate of CPI inflation was still low, only 0.4 per cent, and

the trend was downwards. In January the 12-month change in the CPI was 1.3 per cent, while in December it had dropped to -0.6 per cent.

The harmonised index of consumer prices (HICP) also pointed downwards during 1998. At the beginning of the year the rate of inflation in Sweden was the second highest in the EU area, exceeded only by Greece. The rate in Sweden then declined rapidly, and in September the 12-month change was the lowest in the EU area. The relatively faster retardation of inflation in Sweden was partly due to substantial cuts in indirect taxes; but underlying inflation was also lower. The average rate of increase in Sweden's HICP in 1998 was 1.0 per cent.

One of the main explanations for the low rate of inflation in Sweden is that the global economic effects of the crisis in Asia have been greater than assumed earlier. Import prices have therefore been more subdued than expected even though the krona was 2.3 per cent weaker on average in 1998 compared with 1997. Falling commodity prices contributed to this together with a slow price rise for manufactured products. In December the level of import

prices was 1.6 per cent lower than a year earlier and the downward effect of this on the CPI amounted to almost half of a percentage point.

There were also a number of transitory effects on inflation that monetary policy neither can nor should react to, at least as long as they do not alter inflation expectations. The continued fall in house mortgage expenditure during 1998 had a marked downward effect on the CPI; the impact in December was -0.7 percentage points. Indirect taxes and subsidies were also changed substantially during the year; the net effect of such changes on inflation in December was -0.6 percentage points. These transitory factors accordingly had a

Indexes of inflation

Consumer price index (CPI): the average development of prices for domestic private consumption. Calculated monthly by Statistics Sweden.

Underlying inflation (UND1X): the CPI excluding changes in interest expenditure and direct effects of changes in indirect taxes. Calculated monthly by Statistics Sweden.

Domestic underlying inflation (UNDINH): the CPI excluding import price movements, changes in interest expenditures and direct effects of changes in indirect taxes. Calculated monthly by Statistics Sweden.

Harmonised index of consumer prices (HICP): the CPI excluding the following items: house mortgage interest expenditure; tenant-owned housing charges; certain components of health and medical care; property tax, depreciation, some repairs, insurance and leasehold rent for owner-occupied housing; pools and totaliser betting. Calculated monthly by Statistics Sweden.

Monetary policy's target variable, the CPI, includes price effects from changes in indirect taxes and subsidies, as well as price movements for imported goods. Assessments of inflationary pressure need to consider the extent to which pressure is coming from such factors. In the Inflation Report the Riksbank therefore publishes various indicators of underlying or core inflation, for example UND1X and UNDINH. The HICP is constructed for comparisons of price stability among the member states of the European Union (plus Iceland and Norway); it is also used as a target variable in the EMU.

During 1998 Statistics Sweden began to compute indicators of underlying inflation on behalf of the Riksbank. The calculations start from the Riksbank's definitions of underlying inflation, UND1 and UNDINH, but there are minor differences in the methods. Statistics Sweden has chosen to refer to its indexes as UND1X and UNDINH.

Diagram 1. CPI and underlying inflation, percentage 12-month change



combined downward effect on CPI inflation in December of 1.3 percentage points.

Both the domestic component of inflation and short-run inflation expectations were lower than expected. Inflation's average annual underlying rate was 0.9 per cent in terms of UND1X and 1.8 per cent in terms of UNDINHX. The higher level of domestic underlying inflation came mainly from price increases for services and from goods that are priced administratively.

A factor of central importance for the inflation process is inflation expectations. In that economic agents aim to maintain or improve the real level of income, expectations that future inflation will be high are liable to result in inflationary price and wage increases.

During 1998 households and industrial firms expected that the rate of inflation in the coming twelve months would be about 1 per cent. Surveys of the major Swedish and foreign investors in the bond market showed that their two-year inflation expectations were just over 1 per cent and their five-year expectations close to 2 per cent. All in all, inflation expectations derived from survey data and financial prices pointed to very low inflation in the short run and a rate in the longer run that was in line with the Riksbank's inflation target. Even in an economy where confidence in price stability has been established, inflation expectations may fluctuate to some extent, at least in the short run. Such fluctuations may be caused, for example, by changes in current inflation that the Riksbank neither can nor should react to.

STABLE

DOMESTIC ECONOMY

The economic recovery that began in Sweden towards the end of 1996 and continued in 1997 became even stronger during 1998.

Diagram 2. CPI inflation and inflation expectations of households and industry, percentage 12-month change



Note. The expectations have been shifted twelve months ahead to coincide with the CPI changes to which they refer.

Diagram 3. Bond market investors' yearly expectations of inflation two and five years ahead, per cent

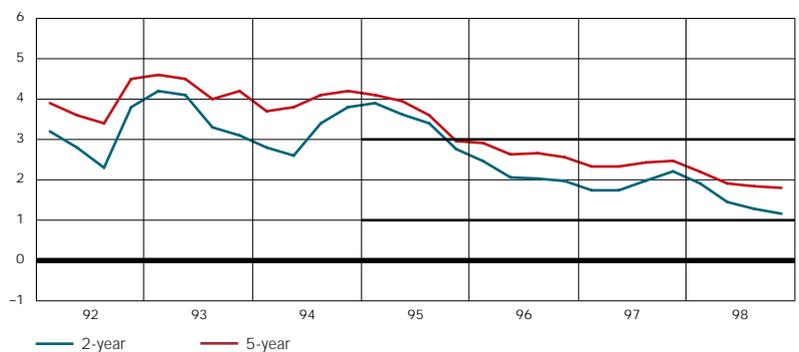
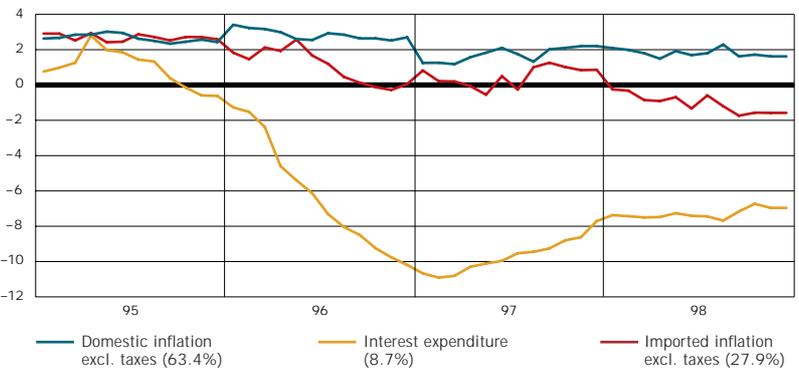


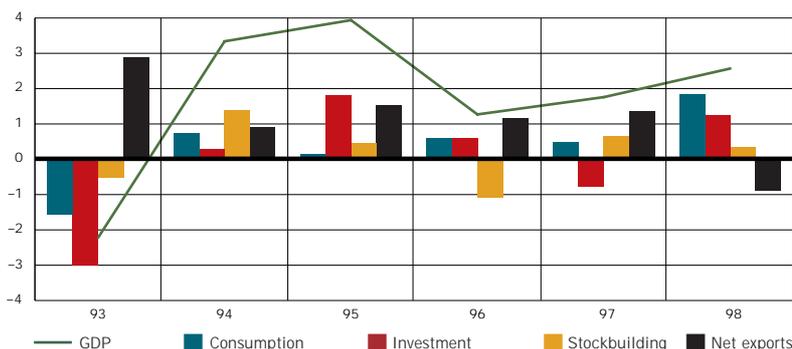
Diagram 4. CPI components, percentage 12-month change



The credibility that resulted from the consolidation of government finances has been a major factor behind the lower interest rates and these in turn have provided a basis for the recovery in the domestic sector. Net exports, which had made a major contribution to GDP growth in the preceding years, developed less favourably than expected, partly on account of the Asian crisis. GDP growth in 1998 is estimated to have been almost 3 per cent.

Private consumption has shown an upward trend since the second half of 1996; the annual increase in 1998 is estimated to have been 2.7 per cent. The growth came mainly from rising demand for durable goods but increases were also noted for certain types of services, such as entertainment, restaurants, telecommunications and foreign travel. Several factors are contributing to the growth of consumption: the wealth, incomes and expectations of house-

Diagram 5. GDP growth and its components, per cent (GDP) and percentage points



holds all developed favourably during 1998. The Stockholm Stock Exchange did fall sharply in the autumn but recovered relatively quickly; in the year as a whole the stock market rose 10.5 per cent. This was accompanied by an 11.2 per cent increase in house prices. The lower interest rates also helped to stimulate consumption.

Gross fixed investment recovered after the temporary dip in 1997. High capacity utilisation prompted a strong increase in business investment in particular. Public investment also rose, after falling for a number of years. The economic improvement contributed to a rapid consolidation of government finances. Some of the surplus was used for additional spending, above all in the form of increased grants to local governments.

Foreign trade has expanded markedly in recent years. Exports of goods and services are currently equivalent to approximately 45 per cent of GDP, while imports are equivalent to almost 40 per cent. With the Asian crisis and the international economic slowdown, export growth for goods and services is calculated to have slackened from 12.8 per cent in 1997 to 5.1 per cent in 1998. With the strong domestic demand, imports are judged to have risen 8.9 per cent. This points to a negative contribution to GDP growth from net exports in 1998.

With the higher economic activity, labour demand rose during 1998. The number in employment grew by 57,000 persons, of which 38,000 in private services. Public sector employment stopped falling during the year and turned into an increase of 15,000 persons. The level of registered unemployment declined 1.5 percentage points from 1997 and the rate in December was 5.5 per cent. It was mainly the good development of employment that lay behind the reduction of unemployment.

The narrow money supply (M_0 , currency in circulation) rose 5.1 per cent in 1998. The broad money supply (M_3 , which also includes bank deposits and certificates of deposit) rose 2.1 per cent. One explanation for the lower rate of increase in M_3 was that households reduced their bank deposits in December. Total advances to households from banks and housing credit institutions rose 5.8 per cent in annual terms.

WEAKER INTERNATIONAL ECONOMIC OUTLOOK

The financial crisis in the emerging markets in Asia worsened during 1998 and also had effects in Russia and parts of Latin America. As a result, the global rate of GDP growth slackened more markedly than had been foreseen a year ago. World economic growth is calculated to have dropped from 4.0 per cent in 1997 to 2.0 per cent in 1998. The crisis also led to increased uncertainty in financial markets throughout the world, with large fluctuations in share prices.

The Asian crisis contributed during 1998 to somewhat clearer signals of an economic slowdown in the United States. However, domestic demand developed favourably; private consumption is calculated to have risen 4.7 per cent and gross fixed investment 8.9 per cent.

Expectations of poorer opportunities for growth in the coming years prompted the U.S. Federal Reserve to lower its instrumental rate in three steps during the autumn, by a total of 0.75 percentage points to a level of 4.75 per cent. The poorer growth prospects had to do with financial turbulence as well as limited conditions for domestic demand and decreased opportunities for exports. More than half of U.S. exports go to regions where demand is ex-

pected to be very unfavourable in 1999 (Japan, Latin America and Canada).

Growth in the euro area was good in 1998, though the Asian crisis and its wider consequences did subdue the upswing. Domestic private consumption and investment developed particularly well compared with 1997.

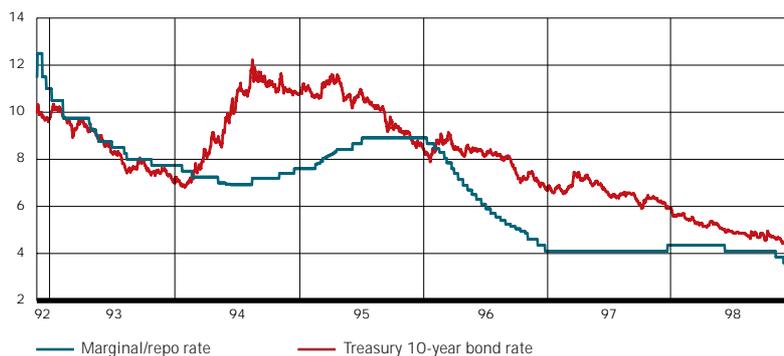
The rate of HICP inflation fell during the summer in France and Germany to the lowest levels in the euro area, 0.6 and 0.7 per cent, respectively. Inflation was highest in Ireland and Italy, at 3.0 and 2.2 per cent, respectively. The average rate of inflation in the euro area was just over 1 per cent, which is well in line with the ECB's objective.

In October 1998 the ECB announced that its monetary policy's primary objective of price stability was to be defined as a year-on-year increase in the euro area HICP of below 2.0 per cent, to be maintained over the medium term.

The move to Stage Three of EMU on 1 January 1999 had caused instrumental rates in the euro area to converge in recent years. Even so, at the beginning of 1998 the spread between a number of these national rates was still comparatively large. The rates in Ireland and Italy, for example, were 6.75 and 5.50 per cent, respectively, as against 3.30 per cent in both Germany and France. During the year there was some convergence but the spread remained broadly the same until the beginning of December. In a joint action the central banks in the euro area then lowered their instrumental rates to 3.0 per cent (except for Italy, where the rate was lowered to 3.50 per cent). The monetary easing that this joint action represented was to be seen in the light of the global financial crisis and expectations that this would greatly reduce the growth of exports from the euro area.



Diagram 6. Interest rates, per cent



The economic situation in Japan remained weak, with few signs of a recovery from the prolonged recession. Better conditions were, however, created for resolving the bank crisis in that the legal provisions for bank support were adopted. Domestic demand remained weak during 1998, mainly as a consequence of decreased investment but also because private consumption fell. Moreover, exports to Asia dropped sharply when demand declined in Southeast Asia in particular. The downward trend in industrial output, which was marked in the first half of 1998, has been checked but is still strongly negative, with an expected fall of 7.0 per cent in 1998.

The financial crisis that arose in the spring of 1997 in Southeast Asia developed during 1998 into a deep recession, with falling production in all the countries that were affected initially (Indonesia, South Korea and Thailand). One effect of the crisis has been a marked improvement in current-account balances in this region. This swing has come from steeply falling imports and broadly unchanged exports. The lack of export growth is a consequence of domestic financial problems and weak demand from countries in this region. But as growth is still strong in China, India and Taiwan, it is estimated that for the whole of Asia excluding Japan, GDP growth in 1998 was negligible rather than negative.

In Latin America the financial crisis has mainly affected Brazil, where GDP growth below 1 per cent is estimated for 1998 and the forecasts for 1999 point to a recession, with repercussions in other countries in this region. Under these circumstances, a support programme coordinated by the International Monetary Fund, totalling over USD 41 billion together with fiscal restrictions, was agreed in December 1998. In Russia the situation worsened during 1998, partly as a con-

sequence of the financial crisis. GDP is estimated to have fallen as much as 6 per cent.

FOUR REPO RATE CUTS IN 1998

In the Inflation Report in December 1997, the Riksbank had judged that the rate of inflation one to two years ahead would exceed the 2 per cent target. The assessment envisaged that full capacity utilisation would be reached towards the end of 1999 and that wage increases in 1998–99 would average 4 per cent a year. On 11 December 1997 the repo rate was therefore raised 0.25 percentage points to 4.35 per cent with effect from 17 December. The Report also noted, however, that the picture of inflation was not clear-cut; the incipient crisis in Asia might lead to a more marked slowdown in the international economy and thereby to lower inflation prospects.

In the Inflation Report in March 1998, inflation prospects seemed more subdued than in the December Report's main scenario. This was partly because the Asian crisis was now judged to be more protracted and severe. Other factors were the steep fall in petroleum and other commodity prices and indications, from wage settlements in the winter, that wage increases would be somewhat lower than expected earlier, in the region of 3.5 to 4 per cent a year in 1998–2000. On the other hand, the domestic economic situation was largely unchanged and full capacity utilisation was expected some time during 2000. The Report's main scenario pointed to inflation being marginally above the target one to two years ahead. This favoured some tightening of the monetary stance; but as a further worsening of the Asian crisis could not be ruled out, the Riksbank decided to leave the repo rate unchanged for the time being.

Price tendencies during the rest of the spring were more subdued than the Riksbank had expected. Prices were particularly weak for goods that are imported or exposed to competition from imports; besides reflecting a further fall in petroleum and other commodity prices, this was due to effects that the weak growth in Asia was now beginning to have on other parts of the global economy. Meanwhile, the low inflation expectations meant that wage settlements during the spring continued to be restrained. While the Riksbank's economic assessment was broadly unchanged, the strong productivity growth did suggest that in two years time there would still be some unutilised capacity. All in all, therefore, inflation prospects were judged to be more subdued than before. In the June Inflation Report, the main scenario indicated that inflation one to two years ahead would be below the 2 per cent target. The assessment of uncertainties, with the risk of a considerable international economic slowdown, supported the picture of a more subdued path for inflation. In the light of this, on 4 June the Riksbank decided to lower the repo rate 0.25 percentage points to 4.10 per cent with effect from 10 June.

In the September Inflation Report the Riksbank judged that inflation one to two years ahead would be somewhat below the target; at the end of the forecast period, however, the rate was expected to be approximately 2 per cent and thus in line with the target. The Riksbank considered that there were two main and counter-balancing factors that would be crucial for inflation prospects and the future formation of monetary policy. On the one hand international activity could be weaker than envisaged in the main scenario and thereby lead to lower inflation; on the other hand, at the same time, exchange rate uncer-

Diagram 7. Nominal effective (TCW) exchange rate, index: 18 November 1992=100

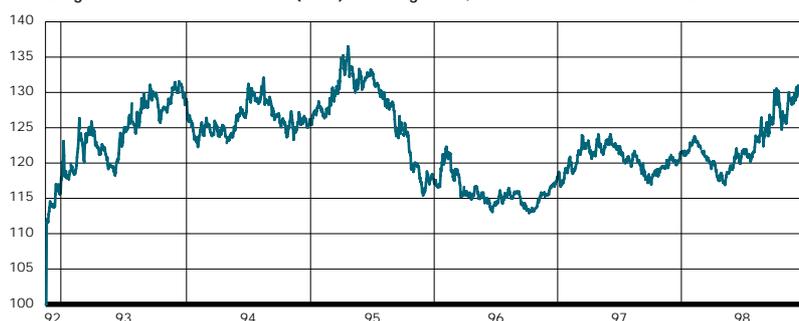
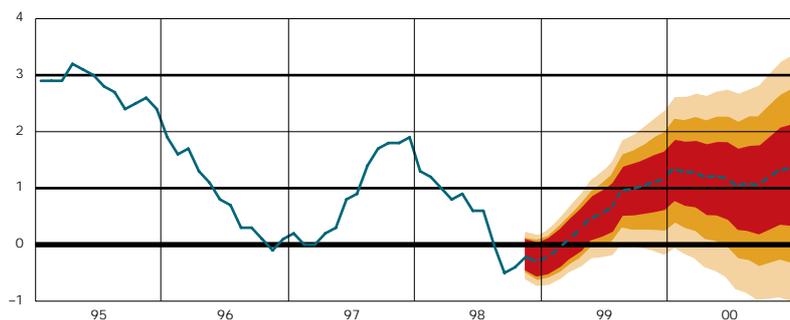


Diagram 8. CPI with uncertainty intervals, percentage 12-month change



Note. The uncertainty intervals show the 50, 75 and 90 per cent chances of CPI inflation being within the respective range.

tainty had grown during the summer and a more permanently weak currency might lead to stronger inflationary pressure. In addition, the financial turbulence, in the global economy as well as in Sweden, made future developments extremely difficult to assess. The Riksbank therefore refrained from changing the repo rate.

During the autumn the turbulence in international financial markets grew. The financial crisis contributed to a rapid depreciation of the krona, to its weakest level in the past three years. In relation to economic fundamentals, with good growth, low inflation and a growing surplus on public finances, however, the abrupt and pronounced depreciation seemed to be unmotivated. In order to underscore this view, the Riksbank intervened in the foreign exchange market on 7 October, purchasing kronor for foreign currency.

There may be grounds for the Riksbank to promote a stable exchange rate as long as the inflation target is not jeopardised. The primary consideration in the formation of monetary policy is how inflation prospects relate to the inflation target; the exchange rate is only one of many factors in the Riksbank's inflation assessment. At the same time, the exchange rate is import-

ant for real economic tendencies. A highly volatile exchange rate is liable to disturb resource allocation.

The exacerbation of the international financial crisis made it clear that the real economic consequences were likely to be greater than envisaged earlier. It was the suspension of payments in Russia in August that mainly contributed to this but so did the near failure of the U.S. hedge fund Long Term Capital Management. New statistics from the IMF and the OECD led to further downward revisions of growth and inflation forecasts for the OECD area. The consequences of this for growth and inflation in Sweden were judged to counter the stimulatory effect of the krona's depreciation. In the light of this, on 3 November the Riksbank decided to lower the repo rate from 4.10 to 3.85 per cent. This was followed on 12 November by a downward adjustment of the Riksbank's interest rate corridor: the deposit and lending rates were both lowered 0.5 percentage points to 3.25 and 4.75 per cent, respectively, with effect from 18 November.

When the corridor was adjusted, the Riksbank's inflation assessment had also become firmer; the overall assessment indicated that inflation one to two years

ahead would be below the target. On 24 November the Riksbank therefore decided to lower the repo rate another 0.25 percentage points to 3.60 per cent.

In the December Inflation Report the outlook for growth was considered to have worsened somewhat since the September Report. The international economic prospects also seemed to be more subdued. The Riksbank considered that with the lower growth, the economy would still have some unutilised resources in one to two years time. The earlier repo rate cuts and the depreciation of the krona were expected to counter the effects of this to some extent. However, the overall assessment pointed to underlying inflation being below the target and that transitory effects would lower CPI inflation still more. The 12-month change in the CPI was judged to be 1.2 per cent at the end of 1999 and 1.4 per cent at the end of 2000. Under these circumstances, on 15 December the repo rate was lowered 0.20 percentage points to 3.40 per cent.

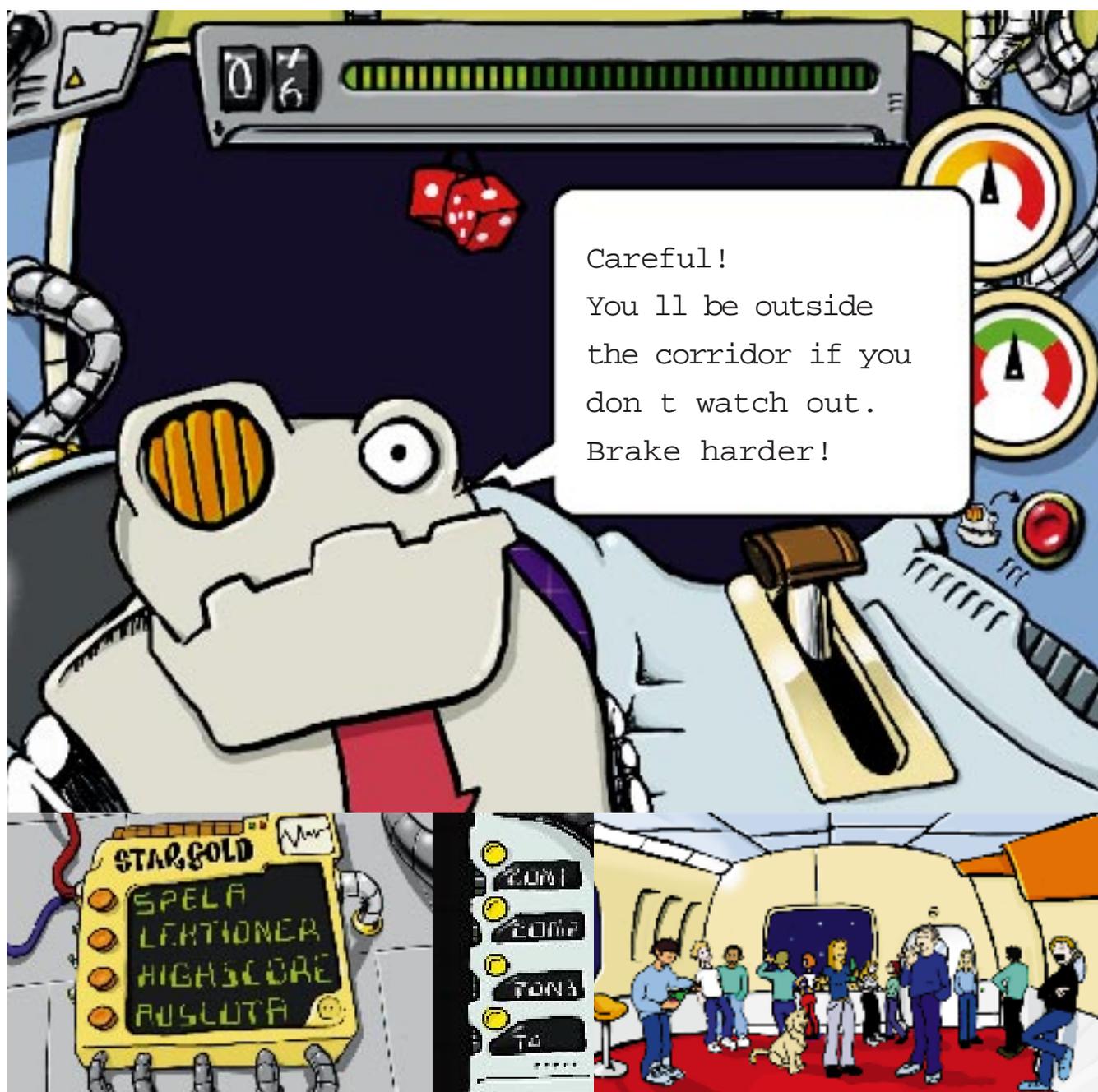
Uncertainties in inflation assessments

For various reasons, the assessment of economic activity and inflation that is presented in the Inflation Report includes elements of uncertainty. With a view to elucidating this, since the December 1997 Report the Riksbank has presented the inflation assessment with an uncertainty interval; a new method for calculating the uncertainty interval, together with the probability distribution for the overall inflation assessment, was then introduced in the June 1998 Report. This is intended to clarify the element of uncertainty in the forecast and whether any forecasting error is more likely to be upside than downside. The graphic representation of the uncertainty interval is shown in Diagram 8, which refers to the situation at the beginning of December 1998.

The calculation of the uncertainty interval involves some subjective judgements but also uses historical relationships. Two aspects of the forecast distribution are assessed subjectively: whether there are grounds for being more, or less, uncertain than usual and whether the risk of forecasting errors is upside, symmetric or downside. The interval visualises the inflation assessment's inherent uncertainty. This uncertainty concerns the existence of economic shocks as well as the transmission mechanisms.

In the spring of 1999 the Riksbank will be introducing a computer game, Star Gold, on the Internet (www.riksbank.se), with upper secondary pupils as the main target group. The purpose of the game, which is in Swedish, is to provide insights into the Riksbank's primary objective, price stability, and the foundations for monetary policy.

Players who find themselves in trouble can get assistance from the robot.



Satisfactory stability

The good competitive position of Swedish banks reinforces stability; in the latest Financial Market Report it was concluded that the Swedish financial system is currently stable.

One of the main functions of the Riksbank is specified in the Riksbank Act as being to 'promote a safe and efficient payment system'. There are mainly two means of payment in Sweden: account holdings and notes and coins. Of all the payments, it is estimated that 90 to 95 per cent in value terms are based on credit balances on various types of deposit account. It is the payment system that makes account-based payments feasible as an alternative to the use of cash.

THE PAYMENT SYSTEM

Oversight over the payment system is essential because an efficient system can be said to oil the wheels of the economy. This helps to lower costs and reduce risks in the production of goods and services, thereby promoting growth and employment. By the same token, a disturbance in the payment system may have negative effects on the entire economy. Since the autumn of

1997, the Riksbank has published its assessment of financial system stability twice a year in the Financial Market Report.

Work at the Riksbank on monitoring financial stability covers two main areas. This follows from the construction of the payment system, which can be said to consist of two components: the infrastructure and financial firms.

The *infrastructure* consists of the technical and administrative systems whereby payments can be executed between financial firms and other economic agents, as well as between different financial firms. It also includes systems for entering into and completing transactions with financial assets. The infrastructure comprises marketplaces in which financial assets are traded, clearing systems in which payments are compiled, and settlement systems for registering and completing pledging and ownership transactions with financial assets.

Normally only certain *financial firms* have access to the payment system's infrastructure. In order to use the system, other firms and private individuals therefore have to turn to these financial entities. As the firms with a central position in the payment system are the banks, it is on these in-

stitutions, particularly the four major bank groups, that the Riksbank focuses when analysing the financial system. In that systemic crises can be triggered by a bank suspending payments, it is this risk that the Riksbank needs to analyse and try to preclude.

THE BANKS

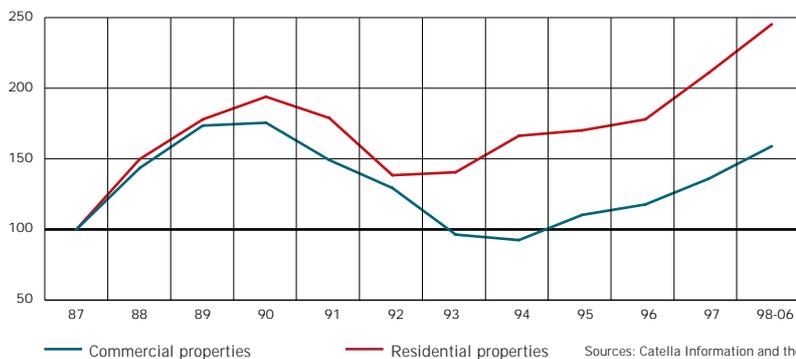
Analytical framework

Monitoring and assessing risks in the bank sector is a major aspect of the Riksbank's oversight of payment system stability. The work is divided into *market analysis* and *risk analysis*.

The *market analysis* concentrates on the competitive situation in the bank sector. This follows from the perception that one of a financial system's foundations is a competitive banking system that is sufficiently profitable. Weak earning power is liable to induce banks to take increased risks, which may then lead to considerable losses and a greater likelihood of payments being suspended. One important component of the market analysis is the trend in bank sector costs. The market analysis was discussed in the *first Financial Market Report*, which was published in November 1997.

The *risk analysis* looks at the financial risks involved in the banks' operations. The risks to which banks are exposed in their operations were reviewed in the *second Financial Market Report*, which appeared in May 1998. Particular attention was paid to the credit risks in bank lending to households and firms because historically these risks have at times been substantial. The main purpose of the analysis was to elucidate the relationship between *bank credit risks* and the macro economic trends. The analysis of credit risks showed that stability in the bank sector was satisfactory. No signs were detected of a risk of more widespread

Diagram 1. Prices for commercial and residential properties in metropolitan areas, index: 1987=100



loan losses in connection with the economic upswing. It is often in connection with rising activity that a build-up of risks occurs in bank loan portfolios. The Report did, however, note that property prices had been rising rapidly, above all in the metropolitan regions. The ability of various categories of borrower to meet commitments was also assessed in the Report.

The *third Financial Market Report*, which was published in November 1998, focused on *counterparty and settlement risks*, which occur in connection with transactions between financial firms. The starting point is what happens if a counterparty to a financial market transaction cannot meet its commitments; the other party may then incur losses of various kinds, depending on the type of transaction and the stage at which the problem arises. The transactions between financial firms amount in practice to the connections between the banks and the payment system. The analysis of counterparty and settlement risks accordingly joins up the two main components of the Riksbank's analysis of financial system stability.

The Report noted that banks have large exposures in the form of counterparty and settlement risks, a phenomenon that is particularly evident in the Swedish bank market, which is dominated by a few large banks. This heightens the risk that sizeable problems for one bank will have contagious effects on the financial system. Other components of the risk analysis are liquidity risk and market risk.

Stability in Sweden's bank sector

In the November 1998 Report, certain signs were noted that a build-up of the risks associated with bank lending was on the way, in the first place in the real-estate sector. However, much of this tendency could

Diagram 2. Pre-tax return on bank shareholders' capital in selected countries, per cent

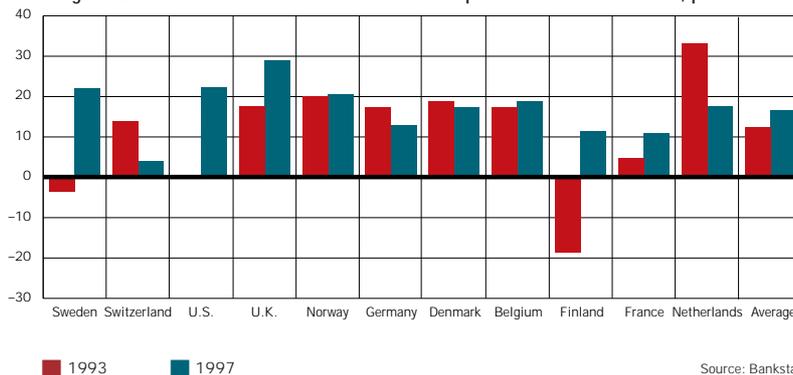
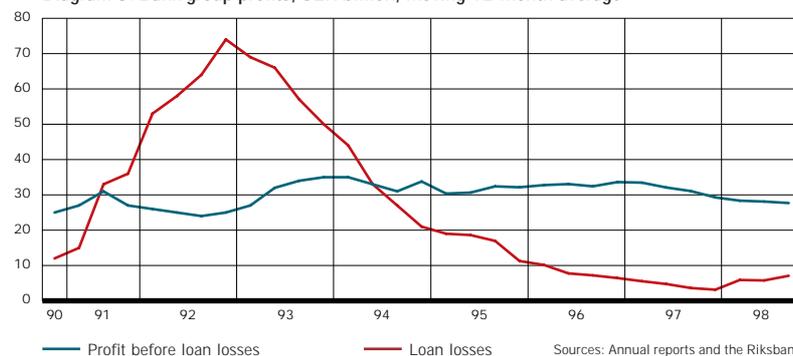


Diagram 3. Bank group profits, SEK billion, moving 12-month average



be attributed to economic factors such as falling interest rates, for example.

The element of uncertainty in assessments of financial system stability is accentuated by the international financial market unrest. A suspension of payments by sizeable international banks is one way in which the problems could spread to Swedish banks. The direct exposures of Swedish banks to problem countries are comparatively small and the banks, in an international comparison, look strong at present. That is one reason why they may cope with international turbulence more successfully than banks in other countries. Profitability seems to be developing satisfactorily, though the international unrest may have some downward effect on results. The good competitive position of Swedish banks reinforces stability. In the latest Report the overall assessment was that the Swedish financial system is currently stable.

PAYMENT SYSTEM
INFRASTRUCTURE

General analysis and oversight

In its work on payment system infrastructure the Riksbank aims to reduce systemic risks and heighten the system's efficiency.

Because large payments involve greater risks than small ones, the Riskbank can best work towards its goal of contributing to financial stability by concentrating on large value payments. This means an emphasis on the RIX system which handles all large value transactions and also on the systems for handling securities. Besides involving very large amounts, these systems are crucial for the functioning of the securities market and thereby for the Riksbank's other main function, monetary policy. The relevant Swedish securities systems, OM and VPC (Central Securities Depository)¹, handle large values and settle in the RIX system. Shortcomings in such securities systems can have a considerable negative impact on financial markets.

The RIX system

Work on modifying the RIX system has been in progress in the past two years, partly with a view to improving stability and efficiency, partly in connection with the adaptation to EMU.

A new mode of communication, message handling through SWIFT², has been introduced by degrees, starting in June 1997. Since September 1998 it is being used



<p>for all payments initiated by the participants in the RIX system. This enables these players to integrate their own systems with the RIX system and thereby process a larger volume of payments. TARGET³, the joint system for payments between EU central banks, is based on SWIFT communication.</p> <p>Marking to market was introduced in 1998 for the securities that banks pledge as collateral for Riksbank loans. Previously, collateral was accepted for up to 97 per cent of its face value. Since April 1998, it is marked to market and then reduced by a 2 per cent 'haircut'. Another change is that securities issued by an affiliated institution are no longer acceptable as collateral in the RIX system; in practice, this means that a bank can no longer pledge securities issued by the same group's housing intermediary.</p> <p><i>The Target system</i></p> <p>Although Sweden did not participate in the start of the euro area, the Riksbank is included in the joint payment system, TARGET. The primary purpose of this system is the settlement of monetary policy transactions for EMU but it can also be used by banks for rapid and reliable settlement of payments throughout the EU area. Only payments in euro can be settled. During 1998 the Riksbank completed a system, E-RIX, that parallels the RIX system for kronor and functions as the Riksbank's share of the TARGET infrastructure. E-RIX came into operation on 4 January 1999.</p> <p>The participants have separate euro accounts with the Riksbank from which euro payments, domestic as well as cross-border, can be made and received. During the autumn of 1998, moreover, it became clear that central banks in non-euro EU countries would be in a position to provide banks in their country with intraday euro</p>	<p>liquidity collateralised with securities; for Sweden the supply is limited to one billion euro. The eligible securities include Swedish Treasury paper and housing bonds. Routines for cross-border pledging of securities were also worked out during 1998. They enable a bank to obtain credit from the central bank in one country against securities pledged with the central bank in another country.</p> <p><i>Securities settlement</i></p> <p>During 1998, VPC and its counterparts in Denmark and Norway had preliminary discussions about creating a joint clearing and settlement system for the securities markets in the three countries. The Riksbank has been involved in these deliberations because the cash leg of the securities systems' transactions is settled in the central bank. During the year, moreover, work was in progress together with VPC on improving cash settlements connected with VPC's settlement of securities transactions.</p> <p>On behalf of the European Central Bank, the existing securities settlement systems in the EU area were appraised in the first half of 1998. This was done on the basis of the standards that have been established with a view to reducing the risks to which the central banks may be exposed through their loans to banks in the context of monetary policy as well as the payment system. VPC was one of the two systems that were approved without any particular reservations or comments.</p> <p><i>Retail payments market</i></p> <p>The Riksbank also has a more limited function as the overseer of retail payments (by households and firms). Specific aspects of efficiency and stability in this respect were delineated during 1998. Similar international work is being done in the G-10</p>	<p>forum for central bank cooperation. The aim is to identify those aspects that are relevant for central banks, define the role of central banks in the retail payments market and consider how this responsibility is to be managed on a daily basis.</p> <p>This work included a study to elucidate the factors which may lead to conflicts between market players as regards terms of access (pricing, for example) to important infrastructural components of the payment system. Such conflicts reduce efficiency. The development of new payment facilities is often slowed down or stopped by conflicts among participants.</p> <p>One conclusion from the study was that the Riksbank has a part to play in the promotion of cooperation between market players as regards payment infrastructures and innovative technology.</p>

1. OM's system for registering derivative contracts listed on OM's exchanges; VPC's system for interest-bearing securities and equity listed on the Stockholm Exchange.
2. SWIFT (Society for Worldwide Interbank Financial Telecommunication) is a bank-owned organisation.
3. Trans-European Automated Real-time Gross Settlement Express Transfer.



Monetary cooperation in the IMF, G-10 and EU

Analyses of the financial crisis and efforts to construct ways of managing it were central themes in the work of international organisations for economic cooperation.

WORK IN THE INTERNATIONAL MONETARY FUND

The International Monetary Fund (IMF), an organisation for international monetary cooperation, continuously monitors economic developments in member states and provides temporary financing for countries with balance-of-payments problems. A country obtaining this financing concludes an IMF agreement on economic reforms to overcome any fundamental imbalances.

Sweden, the other Nordic countries and the Baltic countries form a constituency for the IMF's Executive Board and are represented there by a Nordic-Baltic executive director.¹ Sweden's positions on matters presented for Board decisions are prepared by the Riksbank together with the Finance Ministry. The Riksbank and the Ministry are also represented on the IMF Interim Committee and at the IMF's annual meeting.

In 1998 the IMF worked mainly on mastering the international financial crisis that had arisen in Asia in the second half of 1997. During 1998 the crisis spread to Russia and Brazil.

Other activities included the ratification of the Eleventh General Review of Quota and of an amendment to the IMF Articles of Agreement to allow for a special one-time allocation of Special Drawing Rights².

Improvement in South Korea

The *second line of defence*, a bilateral borrowing facility for South Korea that Sweden and other industrialised countries had approved in 1997, was not activated during

1998. The South Korean economy improved in a number of respects but growth remains negative and further reforms are needed, for instance in the banking and corporate sectors.

The crisis in Russia

In the wake of the Asian crisis, Russia's financial markets came under increased pressure in the spring. A massive capital outflow pushed interest rates up and large interventions were needed to defend the rouble. IMF negotiations began in May for a new economic policy package, with additional financial support from the Fund to replenish foreign reserves and enhance confidence in the rouble.

On 20 July the IMF Executive Board approved an economic reform programme for Russia, combined with USD 11.2 billion in financial assistance. As the Fund's resources were strained, the *General Arrangements to Borrow* (GAB, a credit facility that gives the Fund access to additional funds to cover extraordinary financing requirements) were activated to finance USD 8.5 billion of the new programme. As a GAB participant, the Riksbank provided a share of USD 200 million. When the IMF Executive Board had approved the arrangement, a first payment totalling USD 4.8 billion was made. Further payments planned for September and December 1998 were deferred because Russia had not made the agreed reforms.

The crisis in Brazil

During the autumn the crisis spread to Brazil, which experienced large capital outflows. An economic reform programme was agreed with the IMF in December. Support was provided as a financing package totalling about USD 41.5 billion, assembled from three sources: USD 18 bil-

lion from the IMF, USD 9 billion from multilateral development banks and USD 14.5 billion in loans from the Bank for International Settlements (BIS).

Of the IMF funds, over USD 12 billion was to be financed via the *New Arrangements to Borrow* (NAB, see below). As a NAB participant, the Riksbank was providing USD 350 million.

The BIS credits are guaranteed by the central banks in the twenty-one participating countries (including the Group of Ten). Sweden is guaranteeing USD 300 million. As such a guarantee lies outside the Riksbank's regular operations, the Riksbank has requested a sovereign guarantee to cover its commitment to the BIS. The Government intends to present a proposal to the Riksdag to issues this guarantee.

IMF quotas raised

With growing demand for IMF resources, an enlargement of the Fund's capital had been decided in principle in 1997. When this decision had been confirmed in 1998, it remained for each country to approve and pay in the increase. Ratification by member states was in progress throughout the year; when countries representing more than 85 per cent of the Fund's capital had accepted the increase, it became effective on 22 January 1999.

The quota increase have raised the IMF's financial capital from SEK 1,645 billion to SEK 2,388 billion. For Sweden, the increase has raised the Riksbank's capital contribution from SEK 18 billion to SEK 27 billion. The increase, due in spring 1999, was approved by the Riksdag on 24 November 1998, accompanied by ratification

1. The directorship and the responsibility for coordination rotate among the Nordic countries.

2. SDRs are held by central banks and some multilateral organisations. They augment foreign reserves and their value is based upon a trade-weighted index of the G-5 countries' currencies.



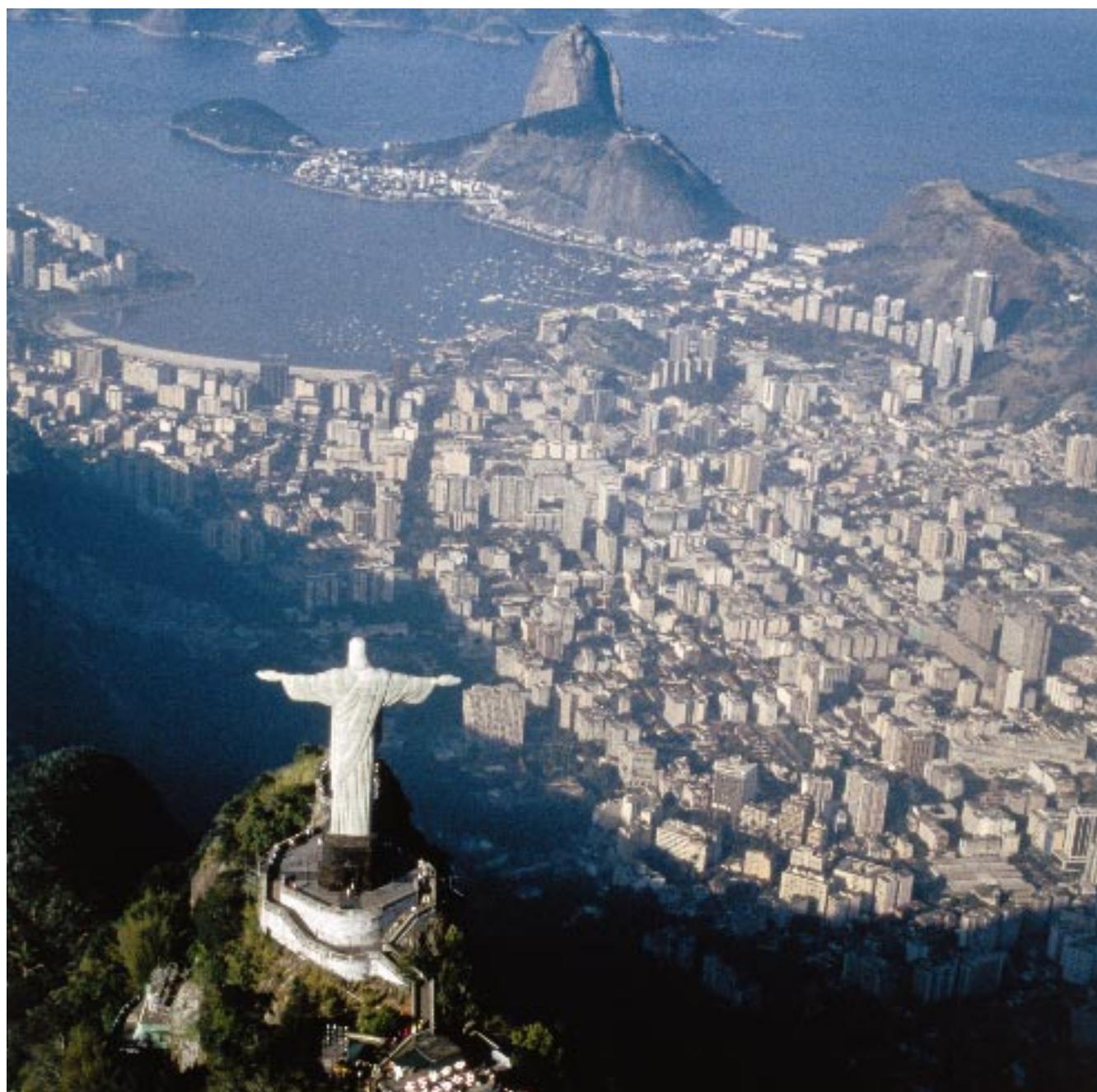
<p>of the amended IMF Articles of Agreement to allow for a special one-time allocation of SDRs to certain countries.</p> <p><i>The HIPC-Initiative</i></p> <p>In 1998 the HIPC³ initiative, which was launched by the IMF and the World Bank, was prolonged to the end of 2000. The purpose of the initiative is to provide debt relief to the poorest and most heavily indebted developing countries, given that they undertake economic reforms. All creditor categories are involved, not just the World Bank and the IMF. Debt relief has been approved in principle for seven countries.⁴ The full financing of the IMF's share had not yet been agreed at the end of 1998.</p> <p style="text-align: center;">INTERNATIONAL FINANCIAL ARCHITECTURE</p> <p>In April 1998, finance ministers and central bank governors of the G-7 countries and fifteen growth economies assembled to reach a broad consensus on the feasibility of strengthening the functions of the international financial system. The initiative, which accompanies the efforts in this field that are being made under the auspices of the IMF and the World Bank, is known as the Willard Group. The meeting identified three key areas for closer analysis in three working groups: increased transparency and accountability; reinforcement of national financial systems; and the managing of international financial crises.</p> <p>Reports from the working groups in the autumn were discussed by the finance ministers and central bank governors in connection with the annual meeting of the IMF and the World Bank. Sweden was invited to the discussion.</p> <p style="text-align: center;">WORK IN THE GROUP OF TEN</p> <p>The Group of Ten (G-10)⁵, a forum for</p>	<p>international economic cooperation, was set up in connection with the General Arrangements to Borrow (GAB, see above). G-10 cooperation is undertaken between the member states' central banks as well as between central banks and finance ministries. Sweden is chairing the G-10 Ministers' and Governors' meetings for a year from autumn 1998.</p> <p>In November 1998 the GAB were supplemented by New Arrangements to Borrow (NAB), involving the G-10 and another fourteen countries⁶. The GAB total about USD 24 billion, while the NAB amount to USD 48 billion, though if both are used concurrently, the aggregate commitment is limited to USD 48 billion. The arrangements aim to augment IMF financing in the event of a threat to international monetary stability. The Fund carries the credit risk on behalf of a country for which it provides loans with GAB or NAB financing. The Riksbank's commitments total USD 540 million for GAB and USD 1.2 billion for NAB, with a combined limit of USD 1.2 billion.</p> <p>Intensive G-10 work was done in 1998 in the Basle-based Euro-currency Standing Committee, the Basle Committee on Banking Supervision and the Payments System Committee. Common themes were the analysis of the financial crisis and the design of tools for managing it.</p> <p style="text-align: center;">TECHNICAL ASSISTANCE</p> <p>Technical assistance aims to build up institutional competence in transition countries (former centrally-planned economies) and in developing economies. The Riksbank contributes by enhancing the competence of other central banks in typical central bank functions. There has also been a large demand for technical assistance in banking supervision and the management of bank-</p>	<p>ing crisis. In such matters the Riksbank usually cooperates with the Financial Supervisory Authority.</p> <p>The Riksbank's contributions in technical assistance are now concentrated to Russia and the Baltic countries in particular. Demand for technical assistance has also grown from Southeast Asia in connection with the crisis there.</p> <p>Through various international organisations as coordinators, the Riksbank mainly participates in the IMF/G-10 cooperation and EU-TACIS⁷. The Riksbank has also provided bilateral assistance.</p> <p style="text-align: center;">ECONOMIC COOPERATION WITHIN THE EU</p> <p>During spring 1998 the work in the European Monetary Institute (EMI) mainly involved completing preparations for the European Central Bank (ECB) and the European System of Central Banks (ESCB), which were established on 1 June, when the EMI was liquidated. The Riksbank Governor has a seat on the ECB General Council and the Riksbank is involved in some of the committees set up by the Council.</p> <p>The Riksbank, along with the Finance Ministry, has been represented on the Monetary Committee⁸ and the Economic Policy Committee. The Riksbank Governor takes part in the biannual informal meetings of the Ecofin Council. Furthermore, the Riksbank participates in the EU</p> <p><small>3. Heavily Indebted Poor Countries. 4. Bolivia, Burkina Faso, Guyana, Ivory Coast, Mali, Mozambique and Uganda; progress with adjustments in Bolivia and Uganda has already resulted in debt relief. 5. The Group of Ten now consists of eleven countries: Belgium, Canada, France, Germany, Italy, Japan, Netherlands, Sweden, Switzerland, United Kingdom and United States. 6. The fourteen countries are: Australia, Austria, Denmark, Finland, Hong Kong, Kuwait, Luxembourg, Malaysia, Norway, Saudi Arabia, Singapore, South Korea, Spain and Thailand. 7. EU-financed projects for Russia and Ukraine. 8. Replaced as of 1999 by the Economic and Financial Committee.</small></p>

<p>cooperation through its representation on the Commission's Bank Advisory Committee as well as on committees for Eurostat, the Commission's statistical agency.</p> <p style="text-align: center;">ESTABLISHING EMU AND ECB</p> <p>In May 1998 the Heads of State or Government of the EU countries confirmed that eleven countries met the criteria for participation in the economic and monetary union (EMU) from the start on 1 January 1999. Prior to that, Denmark and the United Kingdom had declared they did not intend to join from the start, in accordance with derogations in the Treaty protocol. Greece did not fulfil all the convergence criteria. With reference to Sweden, the Heads of State or Government noted that the krona did not fulfil the Treaty's exchange rate criterion and the Riksbank legislation had not been fully adapted for EMU participation. In other respects Sweden was considered to fulfil the Treaty's convergence criteria.</p> <p>The decision by the Heads of State or Government was based on convergence reports from the Commission and the EMI in March. Both reports noted that the new Riksbank legislation would not be passed in time – the Treaty stipulated that statutory central bank independence was to apply by the time the ESCB was established. The reports also noted that the legislation was silent about the Riksbank's integration in the ESCB even though Sweden had no formal derogation from EMU participation. The legislation was also criticised in some other respects.</p> <p>Noting that Sweden did not meet the exchange rate criterion for EMU, the Commission's report mentioned that the krona had never participated in the Exchange Rate Mechanism and its fluctu-</p>	<p>ations in relation to ERM currencies reflected, among other things, the absence of an exchange rate target.</p> <p>In connection with the decision as to which countries would be participating in the euro area from the start of Stage Three, the Ecofin Council announced in advance that the ERM central rates would apply as bilateral exchange rates between the participating currencies at the changeover. The irrevocable exchange rates for the conversion of each currency into euro at the start of Stage Three were not fixed, however, until 31 December 1998. These rates are obligatory for all conversions between national currencies and the euro, as well as between all participating national currencies.</p> <p>The ECB was formally established on 1 June 1998 after the Heads of State or Government of the eleven participating countries had appointed the six members of the ECB Executive Board. The EMI President, Wim Duisenberg, was appointed President of the ECB. The Executive Board manages the day-to-day work of the ECB, which from the start of Stage Three of EMU is responsible for the monetary policy of the euro area.</p> <p style="text-align: center;">THE PREPARATORY WORK</p> <p>In spring 1998 the EMI prepared the necessary legal, organisational and logistic rules for the ESCB. The formal decisions were made after the ESCB had been established on 1 June.</p> <p>The operations of the Riksbank are affected in some respects by the ESCB's work even though Sweden, following the Riksdag's decision, is not participating from the start. The ECB General Council is, for example, to carry on the EMI's function of monitoring the coordination of monetary policies in the EU area until all member</p>	<p>states have adopted the euro. The General Council is to examine the conditions for non-euro countries' future participation in the monetary union. This will involve regular assessments of the development of convergence in these countries and the supervision of the exchange rate mechanism, ERM2.</p> <p>An example of the cooperation between central banks in the ESCB is that during 1998 the Riksbank, under special terms, was incorporated in TARGET, the cross-border payment system of the ESCB. The Riksbank will also be complying with harmonised rules for accountancy and statistical reporting. As regards internal work, the Riksbank's aim is for euro participation to be feasible not later than one year after a decision to this effect.</p> <p><i>Monetary policy in Stage Three of EMU</i></p> <p>In autumn 1998 the ECB Governing Council decided that the price stability target for euro area monetary policy is to be a rate of inflation below 2 per cent, maintained over the medium term. The strategy is based on a reference rate of 4.5 per cent for monetary growth and a number of economic and financial indicators of inflationary pressure.</p> <p>Interest rates are to be steered mainly through open market operations in the form of weekly refinancing transactions, managed by the national central banks in accordance with the ECB's decisions. The ECB Governing Council has also decided that monetary policy counterparties are to observe minimum reserve requirements and have deposit and borrowing facilities in the national central banks.</p> <p>All monetary policy transactions in the ESCB are made with the TARGET system. The ECB Governing Council decides which securities are eligible as collateral.</p>



<p>For cross-border payments there is a special arrangement between the national central banks for the mutual safekeeping of securities.</p> <p><i>ERM₂ cooperation</i> In accordance with the Amsterdam Declaration by the European Council in June 1997, a new exchange rate mechanism has been adopted from the start of Stage Three, when the earlier mechanism was discontinued. In 1998 this resolution was complemented in a central bank agreement on the operative procedures for ERM₂. Central rates have been set between the euro and the currencies of the non-euro countries concerned. ERM₂ participation is voluntary for non-euro countries. At the Vienna informal Ecofin meeting in September, the finance ministers of the future euro countries, the ECB and the ministers and central bank governors of Denmark and Greece agreed that these two countries' currencies would participate in ERM₂ from the start of Stage Three, the Danish krone with a fluctuation band of ± 2.25 per cent and the Greek drachma with ± 15 per cent.</p> <p>The Riksbank has signed the central bank agreement on ERM₂ without a euro central rate being set for the krona.</p> <p><i>Banknotes and coins</i> Following the European Council decision in Luxembourg in December 1997, euro notes and coins are to be introduced on 1 January 2002. Until then, notes and coins denominated in national currencies are exchangeable. The ECB Governing Council has adopted guidelines for this. Following the launch of notes and coins in euro, they will circulate alongside national currencies in the euro area during a transitional period of up to six months.</p>	<p>The ECB is competent to decide about the production and issuing of notes. Coins, on the other hand, will remain a national concern, subject to Ecofin Council decisions about their technical design and ECB Governing Council decisions about the quantity in circulation. During 1998 the ECB continued the process of preparing the technical specifications for euro notes and the coordination of production so that the notes will have a uniform appearance. The Ecofin Council has set technical specifications for euro coins; the reverse face is to have a national identity for each participating country.</p> <p style="text-align: center;">COORDINATING EURO PREPARATIONS</p> <p>The move to Stage Three also required preparation in the private sector, not least by financial institutions. This work was monitored essentially by the national central banks, though the ECB coordinated certain supervisory aspects and was also in direct contact with financial sector representatives.</p> <p><i>Euro coordination in the Cabinet Office</i> Since 1996 the coordination of euro preparations in Sweden has been organised by the Finance Ministry. In 1998 work continued on reviewing the preparations in society and identifying the need for measures for Stage Three and in the event of Sweden adopting the euro. The Riksbank is responsible for euro preparations in the financial sector.</p> <p>The Government had set up a reference group for Swedish euro preparations in 1997. The group, headed by the Finance Minister, includes the Riksbank Governor as well as other ministers and representatives from the business community and the labour market organisations. In 1998 the</p>	<p>group worked on monitoring the extent to which Swedish preparations are affected by Sweden being outside the euro area, identifying needs and problems connected with a possible participation by Sweden at a later date and developing the dialogue with players that are affected by the euro's introduction.</p> <p><i>Financial sector consultation and information</i> The Riksbank has been cooperating with the financial sector on changeover issues since 1996. This work is arranged in the group for Consultation and Information with the Financial Sector (SIFS), which consists of a managerial body and five sub-units, for monetary and exchange rate policy, statistics, notes and coins, payment system and legal matters, respectively. In the light of the extent to which Sweden's financial sector is affected by the euro, even with Sweden outside the euro area from the start, matters discussed by the managerial body in 1998 included this sector's readiness for handling euro after the move to Stage Three.</p> <p>Other SIFS matters were the ESCB's monetary policy strategy, the Riksbank's participation in TARGET, euro currency, and the harmonisation of statistics in the fifteen EU countries.</p> <p>Under SIFS auspices, in January 1998 a second situation report on the euro in the Swedish financial sector was published. The report describes the preparations in Sweden and the implications of being outside of the monetary union for the financial sector's practical preparations. Effects of the monetary union on financial markets, in Sweden as well as in Europe, are also considered, as are the changes that are occurring in Sweden's financial sector even though Sweden is not adopting the euro from the start.</p>

The financial crisis hit Brazil in autumn 1998. In order to tackle the problems, in December Brazil and the IMF agreed on a programme of economic policy reforms. Support was provided by assembling a financing package totalling about USD 41.5 billion and consisting of USD 9 billion from multilateral development banks, USD 18 billion from the IMF and USD 14.5 billion in the form of BIS loans. Sweden contributed to the second and third components.



The Governing Council, a new, enlarged body



L. to. r.: Kenneth Kvist, Göran Hägglund (deputy), Johan Gernandt, Stephan Tolstoy (deputy), Peter Egardt, Ingegerd Troedsson, Britt Bohlin, Sven Hulterström, Jörgen Andersson, Susanne Eberstein, H-G Wessberg (deputy), Kjell Nordström, Marianne Carlström (deputy), Lars Granberg (deputy) and Barbro Andersson (deputy).

Following the approval of new Riksbank legislation, an eleven-member Governing Council and as many deputies took up office from the turn of 1998.

On 25 November 1998 the Riksdag (Sweden's parliament) approved new Riksbank legislation. Under the transitional provisions, on 2 December the Riksdag appointed the new Governing Council, consisting of eleven members and as many deputies, with effect from 1 January 1999.

The members are: Sven Hulterström, Johan Gernandt, Sinikka Bohlin, Jörgen Andersson, Kenneth Kvist, Mats Odell, Ingegerd Troedsson, Britt Bohlin, Peter Egardt, Kjell Nordström and Susanne Eberstein. The deputies are: Reynoldh Furstrand, Stephan Tolstoy, Carin Lundberg, Sven-Erik Österberg, Siv Holma, Göran Hägglund, Margaretha af Ugglas,

Marianne Carlström, Hans Gustaf Wessberg, Lars U. Granberg and Barbro Andersson Öhrn. At the statutory meeting on 2 December, Sven Hulterström was appointed Chairman and Johan Gernandt Vice Chairman.

FUNCTIONS OF THE GOVERNING COUNCIL

The Governing Council appoints six full-time members as the Executive Board of the Riksbank and designates one of them Chairman of the Board and thereby Governor of the Riksbank. The Council also decides the severance of Executive Board members from their appointment. The Instrument of Government prescribes that the Governing Council may so decide only if the member no longer meets the requirements for the performance of duties or has been guilty of serious misconduct.

The Council decides the salaries and other terms of employment of Executive Board members and its consent is required before a member, on leaving the Board, may take up certain employment or assignments after less than one year.

The Governing Council manages the operations of the Auditing Department, makes proposals to the Riksdag on the allocation of the Riksbank's net revenue and decides the working order for the Riksbank.

The Governing Council may submit comments on referrals and put questions to the Riksdag and the Government about constitutional amendments or other State measures in its area of responsibility.

GOVERNING BOARD IN 1998

Up to the general election in September 1998 the Board consisted of: Kjell-Olof Feldt (Chairman), Bengt Westerberg (Vice Chairman), Urban Bäckström (Governor), Birgitta Johansson, Johan Gernandt, Bengt K.Å. Johansson, Berit Löfstedt and Ingegerd Troedsson. The deputies were: Inge Carlsson, Sinikka Bohlin, Stephan Tolstoy, Lars Hedfors, Carin Lundberg, Peter Egardt, Agne Hansson and the Deputy Governors: Stefan Ingves and Lars Heikensten.

On 20 October the new Riksdag appointed seven members to the Board: Kjell-Olof Feldt, Johan Gernandt, Bengt K.Å. Johansson, Berit Löfstedt, Kenneth Kvist, Mats Odell and Ingegerd Troedsson. Governor Urban Bäckström continued his term of office. The following were appointed deputies: Sinikka Bohlin, Stephan Tolstoy, Inge Carlsson, Lars Hedfors, Siv Holma, Göran Hägglund, Peter Egardt and the Deputy Governors: Stefan Ingves and Lars Heikensten. At the statutory meeting on 21 October the Governing Board appointed Kjell-Olof Feldt Chairman and Johan Gernandt Vice Chairman.



Clear mandate

The collective and individual responsibilities and powers of members of the Executive Board have been specified and distinguished from the responsibilities of the Governing Council.

As of 1999 the Riksbank is managed by an Executive Board. All monetary policy decisions are made by the Board. Members of the Board may neither seek nor take instructions in the fulfilment of monetary policy duties. Before making a major monetary policy decision, the Riksbank is required to inform the minister appointed by the Government. Meetings of the Executive Board may be attended by the Chairman and Vice Chairman of the Governing Council with the right to speak but not to make proposals or to vote.

The Executive Board drafts the Riksbank's budget and submits it for the attention of the Riksdag's Standing Committee on Finance, the Office of the Parliamentary Auditors and the Governing Council. The Board also presents an annual report on the preceding accounting year to these instances. Moreover, a written report on monetary policy is to be presented to the Riksdag at least twice a year.

THE 1999 EXECUTIVE BOARD

On 17 December 1998 the Governing Council as of 1999 appointed the six members of the Riksbank's new Executive Board. Urban Bäckström was appointed Chairman of the Board and Governor of the Riksbank for a term of six years. Lars Heikensten was appointed First Vice Chairman for a term of five years, with responsibility for the preparation of monetary and exchange rate policy as well as international functions as a member of the EU's Economic and Financial Committee and the Governor's alternate in the International Monetary Fund, the Group of Ten and the European Central Bank.



L. to r.: Villy Bergström, Eva Srejber, Lars Heikensten, Kerstin Hessius, Urban Bäckström and Lars Nyberg.

Eva Srejber was appointed Second Vice Chairman for a term of four years, with responsibility for the preparation and coordination of international matters, the coordination of the financial sector's EMU preparations and internal as well as external information. Ms Srejber is the Governor's alternate in the Bank for International Settlements and has functions in the European Central Bank. Villy Bergström, with a 3-year term, is responsible for research and statistics.

Kerstin Hessius, with a 2-year term, is responsible for matters concerning payment instruments, internal auditing and risk management. Ms Hessius is also responsible for the Riksbank's work on coordinating the financial sector's preparations for the Year 2000 transition. Lars Nyberg, with a 1-year term, is responsible for the preparation of matters concerning the pay-

ment system, the Riksbank's companies and Riksbank submissions. Mr Nyberg also has international functions in the field of oversight.

Functional arrangement with clear goals



Peter Lundkvist, Göran Zettergren and Malin Andersson from the Economics Department and Peter Walter from the Monetary and Exchange Rate Policy Department engaged in work on the Inflation Report.

Major external changes and important new functions increased the workload substantially for many activities during the year.

EXECUTIVE BOARD SECRETARIAT

The functions of the Secretariat are organised under three headings: legal, advisory and secretariat. The managerial system is also organised by the Secretariat. The legal function provides legal services for the Bank's management and departments. Together with the secretariat function, it also provides administrative support for management. The advisory function provides management with expert advice.

During 1998 the lawyers participated in EMI/ECB work on the drafting of the legal framework for the ESCB as of 1999. They also took part in the national legislative work on amendments to the Riksbank Act from the turn of the year. Other activ-

ities included the production of new legal documentation for the RIX system and work on preparations for the adaptation of the Riksbank's operations to the new legislation.

In 1999 the lawyers will be contributing to ECB work on legal matters concerning the non-euro countries, as well as to Swedish legislative work. They will also be developing the legal conditions for cross-border use of collateral. Moreover, they intend to begin work on monitoring observance of internal and external regulations and will present a report on legal risks in the Banks' financial operations. Another task in 1999 is to review the legal documentation for the system of monetary policy instruments.

The archive function, which involves maintaining a proper standard of public records and providing both internal and external services for personnel and re-

searchers, was still included in the Secretariat in 1998.

ECONOMICS DEPARTMENT

The primary function of the Economics Department is to contribute to the foundation for the Executive Board's monetary policy decisions so that the Riksbank's inflation target is fulfilled. As it takes one to two years for monetary measures to affect inflation, policy has to be based on inflation's forecast path.

Economic theory and practical experience indicate that in this time horizon inflation is affected by four factors: international inflation, domestic demand relative to supply, cost shocks (changes in oil prices and indirect taxes, for instance) and inflation expectations. A continuous analysis of these four factors is therefore a central feature of work in this Department. The major part of the results is presented by the Riksbank four times a year in the Inflation Report. The aim is to provide a simple and educational account of the analysis in order to clarify monetary policy and stimulate debate.

Continuous development work is undertaken to improve forecasting techniques and knowledge about effects of monetary policy. To support this work, the Department uses and is constantly developing a number of models of different sizes. The two large models are known as RIXMOD and NIGEM.

The Department represents the Riksbank on a number of EU and ECB committees, which involves a considerable amount of work on the preparation of Sweden's positions in European cooperation.

MONETARY AND EXCHANGE RATE POLICY DEPARTMENT

The practical implementation of the Executive Board's monetary policy decisions



Executive Board Secretariat Head: Robert Sparve Employees: 14	Monetary and Exchange Rate Policy Department Head: Richard Gröttheim Divisions: Analysis, Trading, Investment, Secretariat Employees: 33	Payment System Department Head: Kai Barvell Divisions: RIX system, Financial system, Financial administration, Analysis and control Employees: 43	Research Department Head: Anders Vredin Employees: 5	Personnel Department Head: Ingemar Andréasson Employees: 13
Economics Department Head: Claes Berg Divisions: Macro economic analysis, International macro analysis, Price analysis, Monetary analysis Employees: 33	Information Department Head: Michael Wallin Employees: 12	Financial Statistics Department Head: Sigvard Ahlzen Divisions: Current account, Financial account, Methods and publications, Financial market Employees: 43	Cashiers' Department Head: Tom Dagne Central staff and technology division, eleven branches, eight depots (four run by the Post Office, four by Securitas Varde AB) Employees: 345	Organisation and Administration Department Head: Agneta Rönström Employees: 97
	International Department Head: Christina Nordh Berntsson Employees: 12		Internal Auditing Department Head: Gunilla Werner Carlsson Employees: 9	IT Department Head: Staffan Wallén Employees: 61
				Planning and Accounting Department Head: Lena Kvist Employees: 10

is the responsibility of this Department. The Riksbank's monetary policy repos are constructed and executed by the Trading Division so as to bring the repo rate to the intended level. The dealers obtain information about market tendencies through daily contacts with currency, bond and money markets.

The Investment Division manages the Riksbank's foreign reserves, a portfolio totalling over SEK 100 billion, mainly in the form of foreign treasury securities and gold. Besides aiming for a good yield, which is transferred to the Treasury, the managers obtain valuable information about tendencies in the international bond markets.

Information about Swedish and international financial markets is processed by the Analysis Division. The main focus is on market reactions to current monetary policy and expectations of the policy's future direction. The analyses accordingly provide an important basis for monetary policy decisions.

In 1998 there were considerable changes in the financial markets, mainly as regards the preparations for the new European currency, the euro. This entailed changes in the computer systems used by both the Investment and the Analysis Division. The review of the computer systems to prepare for Stage Three of the monetary union was accompanied by the start of work on ensuring that the systems are certified for the Year 2000 transition. Further Year 2000 testing of the systems is scheduled for the spring of 1999.

Changing markets and new forms of securities present the Analysis Division with opportunities for new in-depth studies and new areas to explore, besides representing a potential for alternative investments.

INFORMATION DEPARTMENT

The coordination of internal and external information is the task of this Department. In 1998, much of the coordination work had to do with making people in Sweden more aware that maintaining stable prices is the Riksbank's objective and why this is desirable. Riksbank personnel lectured at universities, university colleges and educational associations all over Sweden, visiting around thirty different educational establishments. The Information Department arranged a number of seminars, courses and study days for upper secondary teachers and journalists. The Riksbank also received thousands of upper secondary pupils and other interested visitors.

The Department's Information Centre answers or refers hundreds of calls a month, from media, financial market players and the general public. Access to the Riksbank and the prompt provision of accurate information are important. The Department regularly uses various means to monitor how media and people in general perceive the Riksbank and monetary policy.

The information on the home page on the Internet (www.riksbank.se) was extended substantially and the number of website visits rose from under 8,000 in January 1998 to over 19,000 in December. The Riksbank regularly holds press conferences at which the Inflation Report is presented; the conferences in September and December were also accessible on the website.

INTERNATIONAL DEPARTMENT

Participation by the Riksbank in international cooperation is coordinated by this Department, which also assists the Executive Board with its international contacts, takes part in international meetings with members of the Board and prepares such meetings.

In EU matters the Department is particularly involved in preparing issues to do with economic policy cooperation for consideration in the Economic and Financial Committee and its alternate group. The Department also prepares matters for the Executive Board's participation in ECB meetings and continuously follows the committees on which the Riksbank is represented.

The Department performs the secretariat function for the Riksbank's joint consultations and exchange of information with the Swedish financial sector concerning adjustments to the European monetary union.

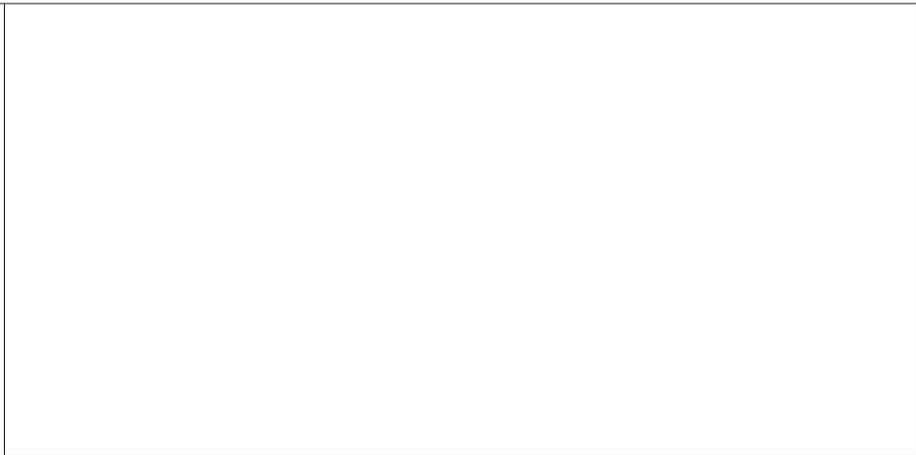
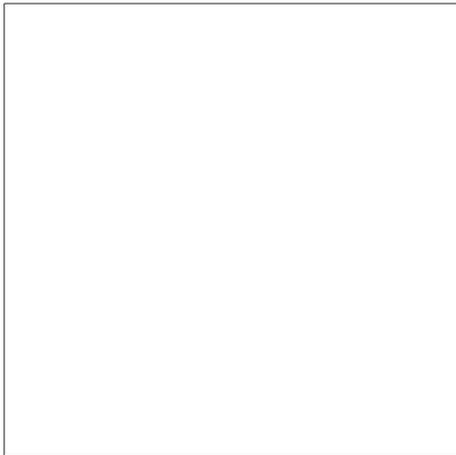
Another responsibility of the Department is the Riksbank's connections with the International Monetary Fund (IMF). Positions on matters for the IMF Executive Board are coordinated with the Finance Ministry as well as with the other countries in the same constituency as Sweden.

Cooperation with the Finance Ministry and other central banks on international issues for the G-10 is likewise coordinated and prepared by the Department, which also prepares certain matters to do with bilateral loans.

The international policy group, which is the core of all this coordination, is headed by the competent deputy governor and includes representatives for other departments involved in the international work. The International Department functions as the group's secretariat.

PAYMENT SYSTEM DEPARTMENT

The RIX Division operates, supervises and develops, the Riksbank's system for the settlement of payments, RIX. The new settlement system for euro payments, E-RIX, became operational at the turn of 1998. Banks participating in the RIX system can



Mats Wallinder from the Payment System Department and Håkan Nyholm and Gent Jansson from the Executive Board Secretariat produced a publication on the rules for RIX settlement.

FINANCIAL STATISTICS DEPARTMENT

Statistics on the balance of payments and financial markets are produced, presented and explained by this Department. The statistics serve, for example, as a basis for the Riksbank's monetary policy assessments as well as for the oversight of the financial system. They also provide a foundation for the public's need of economic analysis.

In 1998 work continued on adapting the statistics to EMU requirements. This involves altered definitions and methods, as well as greatly increased reporting by financial and non-financial firms. The Riksbank now reports statistics to the ECB on a monthly basis.

The international coordination of statistics also continued in other contexts. The reporting of bank statistics to BIS was modified and increased during 1998, not least to improve the possibility of analysing risks of financial crises. An important new field is statistics on financial derivatives. With respect to the balance of payments, the Riksbank and Statistics Sweden have concluded an agreement with Eurostat (the statistical arm of the European Union) on the continuous delivery of statistics. Moreover, Sweden has adopted the Special Data Dissemination Standard (SDDS) that the IMF initiated and established; the Riksbank has accepted the function of national coordinator and acts as the go-between with the IMF.

The Riksbank took part in two global surveys in 1998. One of them, initiated by BIS, concerned the turnover in foreign exchange and derivative markets. The other, on behalf of the IMF, involved mapping cross-border holdings of securities.

The adaptation of statistics will continue in 1999. The remaining EMU require-

now send and receive payments in real time to and from other banks in the European Union. This provides Swedish banks with a facility for using the new structure for payments that has been set up in Europe.

The Financial Administration Division handles the monetary and exchange rate policy transactions of the Riksbank and manages the securities that banks are required to pledge for loans in kronor or euro. In 1998 a great deal of work was done on tests and preparations for the euro's introduction. Preparations in case Sweden joins ERM2 and the euro area will continue during 1999, along with the work to ensure that systems are certified for the Year 2000 transition.

The work of the Analysis and Control Division in 1998 was notably affected by an increased focus on risk management. A

new risk policy was produced for the management of exchange reserves. Daily risk monitoring has improved the quality of the control and supervision of the different types of risk. A risk group, with overall responsibility for ongoing risk management and control, was also established during the year.

The Financial System Division continued to develop the analytical framework for the oversight of financial system stability. Two issues of the Financial Market Report were presented, one focusing on credit risks in the bank sector and the other on counterparty and settlement risks associated with transactions between financial firms. The Division also takes part in international work, mainly in the contexts of G-10 cooperation and the European System of Central Banks.

ments concern interest rate and flow statistics for the financial market and a country breakdown for the balance of payments. In addition, more detailed data will be presented on Sweden's external assets and liabilities.

A programme for enhancing competence is being constructed in order to promote efficiency and development. Another project focuses on matters to do with quality and will result in a general quality policy. Extensive work is being done to secure IT systems and related routines in the run-up to the Year 2000 transition.

The Department's statistics and reports are published on the Riksbank's website on the Internet (www.riksbank.se).

RESEARCH DEPARTMENT

The main function of this Department is to carry out high quality research in fields of relevance to the Riksbank. The quality of Riksbank research is judged, just like that of all other research, by other researchers' assessing whether or not the reports are worth publishing in scientific periodicals. This presupposes a lively exchange with researchers in the academic world as well as in the central bank domain. In 1998, many researchers from both worlds visited the Riksbank and the latter's researchers attended other central banks and scientific conferences in order to check the quality and relevance of their work. For this, however, external contacts do not suffice. The daily contact with other Riksbank departments is at least as important. Many of the Department's research projects are initiated or undertaken in cooperation or consultation with other departments at the Bank. By providing advice and participating in policy groups, the researchers also endeavour to support analyses by other departments.



Johannes Rosenberg and Birgitta Lundin from the Information Department collaborated on the banknote withdrawal campaign with Per-Olof Arevik and Mats Nilsson from the Cashiers' Department.

The Department was set up as recently as 1997, which means that work to date has consisted to a large extent both of formulating tasks, assigning priorities and finding ways of carrying them out and of establishing the Department's function in the Bank. Two more researchers will be recruited in 1999. New research projects and inter-departmental cooperation are to be initiated and developed. The areas with priority are the Bank's credit risks, the empirical analysis of inflation and monetary policy's effects, and the theoretical analysis of inflation target policy.

CASHIERS' DEPARTMENT

The supply of banknotes and coins in Sweden is the responsibility of this Department. Eleven Riksbank branches and eight depots supply banks and post offices with

currency at a specified level of services. The major part of the operations is financed from income. The Department is currently being split into two components: one for the authority function and the other a separate company for managing the physical handling of cash.

Commemoration coins in two denominations (1,000 and 200 kronor) were issued in September 1998 to mark the 25th anniversary of the accession of HM King Carl XVI Gustav.

In the autumn the Department ran an information campaign on the withdrawal of seven old banknotes at the turn of the year. The cancellation date was subsequently postponed to the end of March 1999. A trial campaign was also conducted to find out to what extent the substantial quantity of dormant coins could be

brought into circulation. The campaign resulted in some re-circulation.

The Department participates in the European Central Bank's committee work on the future issue of euro notes. It is likewise active under the European Commission in matters to do with euro coins. Continuous consultations with Swedish banks and retailers are arranged, including appraisals of alternative scenarios in the event of Sweden adopting the euro.

Planning by the Riksbank for the Year 2000 transition includes heightened readiness for supplying cash. One measure here is a temporary halt to the destruction of worn notes.

INTERNAL AUDITING DEPARTMENT

The Department devoted its efforts in 1998 to complying as well as possible with the Governing Board's instructions to see to it that the Riksbank's accounts are true, fair and in accordance with generally accepted accounting principles, to inspecting internal controls with particular reference to safeguarding the valuables of the Riksbank, and to ensuring that the Bank maintains a satisfactory quality of information and systems security in its systems.

Much time was spent on enhancing competence in methods and work was done on a process analysis of the Riksbank's operations. The Department also takes part in the ECB's committee work on internal auditing and scrutinises the joint systems in the European System of Central Banks.

Work in 1999 will be marked by the organisational changes at the Riksbank that result from the new legislation, as regards the Bank's operations as well as the cooperation between this Department and the Auditing Department under the new Governing Council.

PERSONNEL DEPARTMENT

The Department has accentuated its efforts for integrating training, recruitment, work environment functions and rehabilitation efforts in the Bank's operations.

During 1998 the drive for training in IT, languages and communication continued and was augmented with inputs of an economic nature. With a view to improving job situations and work climates, stress profiles were measured in two departments. A project aimed at promoting internal mobility was begun and will continue in 1999.

Following extensive work on specifications and the appraisal of tenders, at the end of 1998 a contract was signed for the procurement of a new PA system. The implementation of the system, which is to be introduced in stages from 1 April onwards, will leave its mark on work in 1999.

ORGANISATION AND ADMINISTRATION DEPARTMENT

Premises, services, and equipment are supplied by this Department, which also supports the work of organisational and administrative rationalisation and development and manages the journal, real estate, transport, security, internal services and, as of 1999, the Riksbank's archive.

In 1998 alterations to the head-office building continued in connection with the work on a new security facility. The Department was involved in the review of the administrative bloc and this resulted in some organisational changes and adjustments to service levels.

IT DEPARTMENT

Work at this Department in 1998 focused on preparing and modifying computer systems for Stage Three of the European monetary union. Much work was also done on testing and adapting systems and tech-

nical environments to cope with the Year 2000 transition. All personnel at the Department are engaged, in principle, in this work, which will continue at an undiminished rate in 1999. The Year 2000 project also includes technical systems and installations at the Bank that are normally not the Department's responsibility. Another task in 1998 was the upgrading of the PC environment and the introduction of a new operative system, NT. Work was also in progress on replacing the internal network; this is scheduled for completion in the first half of 1999.

Besides the above, there is the ongoing operation of systems and technical environments. The Department's workload in 1998 was accordingly unusually heavy. The technical environment is tending to become increasingly complex. Additional resources in the form of consultants were therefore used to a greater extent than in earlier years.

PLANNING AND ACCOUNTING DEPARTMENT

The Department has an overall responsibility for the Riksbank's general accounts and also develops methods for directing and monitoring activities.

As regards accountancy, preparations are in hand for adapting the Riksbank's accounts to the principles and systems that are used in the central bank system. Changes are being made on a continuous basis to improve accounting and make it more efficient. One of the projects for 1999 is a review of invoicing.

The process of planning and monitoring has been developed and refined in recent years. A control system based on the methodology of balanced score cards is being introduced as one item in total operational control. This work will be stepped up in 1999.



Since the beginning of 1998 the Riksbank offers universities and university colleges lectures by Riksbank economists, who are known as Riksbank Ambassadors. Around thirty of these ambassadors gave lectures in 1998, in locations from Luleå in the north to Lund in the south. Their audiences totalled more than 5,000 students at some thirty universities and university colleges. The subjects were "Monetary policy with an inflation target" and "Monetary policy in practice".

These scenes are from a visit to Gotland University College by Peter Stenkula from the Executive Board Secretariat and Tomas Thyblad from the Monetary and Exchange Rate Policy Department.



Major efforts to secure the transition



Erik Gustavsson from the Organisation and Administration Department working on Year 2000 issues with Anders Hellström, Vivianne Lamell and Kent Juhnestam from the IT Department.

The Riksbank's internal security for the Year 2000 transition will be completed by mid 1999. Planning for the transition also includes heightened readiness as regards the supply of cash.

Work on precluding risks of disturbances on account of the transition to a new millennium has been in progress for some time in Sweden's financial sector. The work has been monitored closely, on behalf of the Government, by the Financial Supervisory Authority, which has also formulated requirements and presented a series of progress reports on the adjustments.

GENERAL RESPONSIBILITY

As the authority responsible for the payment system, the Riksbank also has a general responsibility for these issues in relation to banks and other financial institu-

tions with a function in this context. Along with the Riksbank, most financial firms are reaching the stage of external testing—tests involving the systems of more than one organisation. These tests will throw more light both on the ability of the financial system as a whole to cope with the transitional problems and on any need for initiatives and measures of a more general nature. The Riksbank has therefore assembled representatives of the financial sector and the competent authorities to discuss how these issues should be handled. This will, of course, be accompanied by continued preparations by each institution, as well as by the monitoring activity of the Financial Supervisory Authority.

INTERNAL ADAPTATIONS

Work on internal adaptations is also in

progress at the Riksbank and involves computer systems as well as the handling of cash. The Riksbank had already completed an inventory of its systems in 1997. In the spring of 1998 work was focused on analysing and rectifying faulty systems, accompanied by contacts with suppliers to upgrade their products to Year 2000 status. Meanwhile, separate Year 2000 computer environments were constructed for tests. A number of systems were then tested individually in the autumn. Embedded systems, such as controls for lifts and ventilation equipment, et cetera, were appraised in 1998. Extra earmarked investments were made to increase the capacity of the test environment, for instance.

The individual tests are being completed early in 1999, after which testing will focus on verifying that the Riksbank's central systems can communicate with each other. This will be accompanied by tests with external bodies such as RIX participants, the ECB and statistical reporters. Work will be completed on replacing faulty components in property and security systems, including subsequent tests. The plan is to have all systems tested and approved by mid 1999. To cope with the Year 2000 transition, additional technical investments will also be required in 1999.

Each department is drawing up contingency plans. This work is to be completed in September 1999, when readiness will be raised. During the most critical months around the year-end there will be a moratorium on changes to components, programmes and the like, with extra-high readiness for correcting any faults.

Planning by the Riksbank for the turn of the millennium also includes heightened readiness as regards the supply of cash. One measure here is a temporary halt to the destruction of worn notes.



PSAB Pengar i Sverige AB and cash handling

The formation of a limited company to manage the distribution and storage of cash changes the role of the Riksbank in this field. The Bank will act solely as an authority, with three main functions: issue banknotes and coins, be responsible for the supply of payment instruments in Sweden and supervise the company.

The Riksbank is engaged in one of the largest organisational changes in its history. On 17 December 1998 the Governing Board of the Riksbank decided that the physical handling of cash that is now managed by the Riksbank would be transferred to a separate company. The Riksbank will own the company initially but other owners are also conceivable in time.

The change follows a review of the management of cash handling that the Cashiers' Department presented in March 1998. The report, *Cash in Sweden and cash management in 2002*, showed that it was possible to reduce the cost of handling cash in society and transform the participation of the central bank in this activity into a function as a supervisor and analyst.

PSAB PENGAR I SVERIGE AB

On behalf of the Riksbank, the new company, *PSAB Pengar i Sverige AB* ('Money in Sweden plc'), will have functions that include managing the distribution and storage of cash and controlling its authenticity. In addition, the company will be in a position to compete in the market for other payment and cash-handling services.

Ensuring that cash is available throughout the country is a practical task with many similarities to the operations of private enterprises. It can be profitable to coordinate these activities with other services in the market for cash that are outside the Riksbank's domain. If the operations are transferred to a company with a clear profit

motive, they can be made more efficient and more focused on commercial development. The potential for improving efficiency should lead to a reduction of cash-handling costs for the Riksbank as well as the private sector and ultimately result in a social benefit.

ALTERED ROLE FOR THE RIKSBANK

The role of the Riksbank in this field is pared down to that of an authority with three basic functions: issue banknotes and coins in Sweden and supervise the company. The supervisory function involves ensuring that the company performs its assignment from the Riksbank in a satisfactory manner and that the company's operations as a whole are not liable to conflict with the Riksbank's general cash-handling objective. An important aspect here is that the company is neutral as regards competition. In addition to its supervisory function, the Riksbank will need to manage the procurement of notes and coins, the destruction of notes and the readiness stocks of cash. General issues to do with means of payment will also have to be analysed.

From the decision by the Governing Board in December it follows that a limited company is to be formed at the beginning of 1999. Material for a decision by the Executive Board concerning the transfer of activities and assets to the company is to be prepared for consideration in the spring of 1999. By then the authority function is also to be specified as regards the supply of cash in Sweden and agreements are to be drafted for the regulation of the new company's operations. When the company has been completely separated from the Riksbank, the question of whether or not to sell it should be addressed.



The distribution and storage of notes and coins are two of the operations that will be managed by the new company.

A changing organisation



Maria Hammarström and Tobias Bök plan educational projects for 1999.

The Riksbank is largely an organisation of knowledge. The continuous development of competence is most important for the ability to shoulder its responsibilities successfully in an increasingly complex world.

The past year has been full of preparations for and work on factors in the Riksbank's environment that have affected its operations and will continue to do so. These factors include not only the new Riksbank legislation, the formation of a company to manage the handling of cash, the technical problems with the turn of the millennium and the course of the financial crisis but also the growing demands to consider the environment.

Dependence on the rest of the world is becoming more and more apparent, with adaptation to EMU as another important factor. Today's environment calls for a high degree of competence, new thinking and flexibility.

COLLEAGUES

At the turn of 1998 the Riksbank had 754 employees, of whom 56 per cent were women and 44 per cent men. The breakdown by age shows some increase during 1998 in the proportion aged 51 to 60 years and some reduction in the age group 41-50 years. During the year the Riksbank recruited 63 persons externally and 27 internally, which in both cases is somewhat more than the year before. Of the 46 persons who left the Bank in 1998, 34 did so at their own request, 11 went into retirement and one person left because of a shortage of work.

PHILOSOPHY AND STRATEGY

In the past couple of years the themes for work at the Riksbank have been: concentrate on the main tasks, flexibility and internal mobility, cooperation, responsibility and initiative, internal and external transparency, competence and learning, and leadership and delegation.

The aim is to create and maintain a work mode and a culture that enable the Bank to fulfil its objectives in the best possible way. This implies continuous reassessment, development and learning anew. In an increasingly complex world, the Riksbank has deliberately endeavoured to build up a competent, credible organisation. The employees are taking a growing share of the responsibility for the operations. A new culture is being established with the focus on qualified competence. Knowledge, information and decision-making have ceased to be solely the responsibility of management. The individual employee has access to all the relevant information and is accordingly in a position to acquire an overall view, take responsibility and make decisions. With the personnel's increasingly high qualifications, a rational use of the new competence presupposes wider powers. This implies new and different requirements for management and leadership in the Bank.

TRAINING

AT EVERY LEVEL

The Riksbank is working on a long-term basis to develop management and leadership. The implementation of a new philosophy of learning and change has begun, using such key concepts as cooperation, transparency, constantly learning new things, and taking responsibility and initiatives. A total of 65 managers and key personnel have taken part in this development programme.

A couple of years ago the Riksbank also initiated work on developing the control of internal operations. The new philosophy for this supports the move towards a more knowledge-intensive organisation as a means of fulfilling the overriding objectives and strategies. This means that in the control of operations, a number of different dimensions

are weighted together. These dimensions include the personnel and human capital.

The training has been provided in a number of fields. The course *Modern Central Banking* can be mentioned in particular. It aims to give the Riksbank's economists, who tend to be highly specialised, a holistic perspective on how central banks in general and the Riksbank in particular have developed over time and how they operate today. In 1998, communication also had priority in order to support the drive for both internal and external transparency. Courses were held in presentation techniques, conference techniques, project leadership, and cultural differences. The Riksbank has made considerable efforts to raise linguistic competence, primarily in English. About 70 persons participated in language training during the year.

The handling of competence issues in the Bank is supported by means of competence analysis, which is designed to elucidate the relationship between competence and results. The analysis discloses the results that are needed and the extent to which they are produced. The requisite competence can then be identified and competence enhancement can be concentrated accordingly. Development work is also in progress on personnel consultations, career development and leaving interviews.

EXCHANGES WITH OTHER
CENTRAL BANKS

In the autumn of 1998 the Riksbank invited central banks in Europe to a seminar on *The Learning Organisation in a Central Bank*. The purpose of this exercise in the philosophy of learning and change was to exchange experiences and discuss the possibilities of central banks functioning as learning organisations. The seminar attracted a great deal of interest and was attended by representatives from the train-

ing, organisation and personnel departments of twelve central banks.

The Nordic central banks have a form of mutual cooperation with a grants programme. The grants cover two weeks and those receiving them have an opportunity of further development in a specific field or theme. Every year these banks accept grant-holders from each other. In 1998 the theme in Sweden was information and IT.

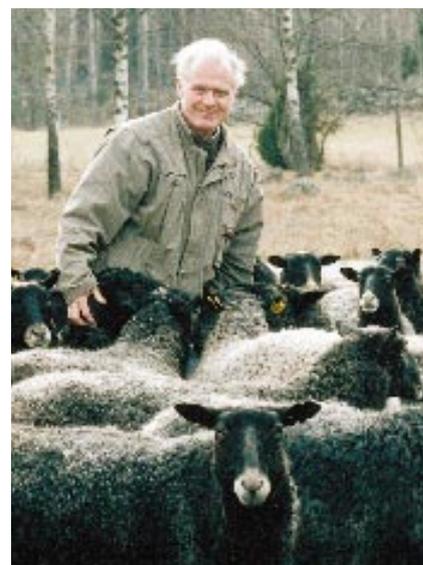
EQUALITY GOALS

The Riksbank also focuses on work for equality both by making department heads directly responsible for developing workplace equality and by formulating specific goals for this. One of the goals is that the proportion of women among the Riksbank's managers is to be 40 per cent by 2001. Today the proportion is 25 per cent.

ENVIRONMENTAL STANDARDS

Environmental work at the Riksbank is based on the environment policy that was adopted some years ago. The established environmental management system is continuing the work of locating and limiting negative environmental impacts from the Bank. As a result, the Riksbank has introduced environmental standards for procurement routines, improved energy efficiency, concluded agreements with companies for the recovery of electronic components and installed the first environment station.

The competence enhancement of all employees that began in 1998 focuses on knowledge of ecological relationships and the perception that everyone, individuals as well as organisations, has a part to play in the efforts for a good environment. Some employees with tasks in property administration and procurement have also



For some years now the Riksbank has had an environment manager, Claes-Göran Lundberg.

had special training in their specific field. In any organisation, high environmental competence is essential for successful environmental work. The training will therefore continue to be a regular feature of the Bank's work for the environment. A new element will be training in reporting environmental consequences in projects and enquiries.

A project has been initiated for cooperation on environmental matters and an exchange of experience with the central bank of Austria. As a result, an initiative will be taken for extended environmental cooperation with other central banks in the European Union.

Comments on the accounts

THE BALANCE SHEET

During 1998 the balance-sheet total increased by SEK 25,205 million. Events during the year that notably affected the balance sheet are reported below.

The gold reserve is valued as of 31 December 1998 at the market price, whereas previously it was booked at a fixed historical price (see note 1). The market valuation increased the book value by SEK 12,686 million. In accordance with a decision by the Governing Board on 17 December 1998, this amount was entered against the Contingency Fund under Capital.

The General Arrangements to Borrow (GAB) and the New Arrangements to Borrow (NAB) were activated during 1998 to provide financial assistance to Russia and Brazil, respectively. The Riksbank paid out the equivalent of SEK 371 million under GAB and SEK 906 million under NAB. The advances are made to the International Monetary Fund (IMF), which in turn lends the funds to Russia and Brazil. The IMF accordingly carries the credit risk in relation to these countries. During 1998, moreover, the IMF has utilised just over SEK 2 billion of the capital contributed by Sweden.

The Riksbank's ecu claim on the European Central Bank (ECB) was settled when the mutual swap agreement expired at the turn of 1998. This agreement, which served to create official ecus, involved the Riksbank, along with the other national central banks in the EU area, transferring 20 per cent of their gold and USD assets in exchange for claims in ecus.

Higher market prices and reinvested earnings have contributed to the increase in the item 'Foreign banks and securities'. The changeover to trade-day accounting raised the level of this item by SEK 208 million; the balancing item is entered as settlement payables under 'Other foreign liabilities'.

The loan facility that the Riksbank has provided as a second line of defence for South Korea was not utilised during 1998. In the 1997 Annual Accounts this facility was booked as an amount of SEK 208 million under 'Other foreign assets' as well as under 'Other foreign liabilities'; in the present Annual Accounts the item is booked off the balance sheet (see note 32).

Treasury securities with a nominal value of SEK 20,000 million have been sold to the National Debt Office in order to adjust the size of the domestic securities portfolio to the current monetary policy regime.

The item 'Monetary policy repos' fluctuates with the liquidity requirement of the banking system. During 1998 the banking system had a liquidity deficit and the Riksbank therefore advanced liquidity by means of its monetary policy repos. In the event of a liquidity surplus, the Riksbank issues certificates in order to withdraw liquidity.

The Riksbank acquired a share of the capital of the European Central Bank (ECB) when the latter was established on 1 June 1998. On the establishment of the ECB, the European Monetary Institute went into liquidation.

Amounts representing proceeds from the sale of gold by the Riksbank, with a simultaneous agreement to repurchase the same quantity of gold, are booked as of 31 December 1998 under 'Other foreign liabilities'; for 1998 these amounts total SEK 2,669 million. In 1997, when net accounting was practised, a total of SEK 660 million was deducted under 'Foreign banks and securities'.

The item 'Currency in circulation' varies with the demand for this means of payment. The volume of notes in circulation normally peaks around the turn of the year, partly in connection with the increased retail turnover.

The Riksdag decided to allocate net revenue for 1997 in accordance with the Governing Board's proposal, which meant that SEK 9,300 million was transferred to the Treasury, SEK 4,951 million was transferred to the Contingency Fund and the remainder, SEK 429 million, was transferred to the Balancing Account. The transfer to the Balancing Account was already booked in the 1997 Annual Accounts.

THE PROFIT AND LOSS ACCOUNT

The Riksbank's net revenue for 1998 before balance-sheet allocations amounts to SEK 21,863 million (1997: 14,680 million).

The result of both domestic and foreign operations in 1998 is favoured by increased market prices for the portfolio securities as a result of falling interest rates. The result of foreign operations is also favoured by the krona's depreciation against the currencies in the foreign reserves. The element of risk in the management of the foreign reserves is controlled through limits stipulated by the Governing Board, for instance on the currencies and counterparties that are eligible for asset investment.

The increase in interest received on loans to banks and others is a consequence of the banking system needing to cover a liquidity deficit throughout 1998.

Administrative income totals SEK 169 million, which is SEK 18 million more than the budgeted figure, largely on account of increased dividend payments from Tumba Bruk and BIS.

Administrative expenditure totals SEK 661 million, which is SEK 27 million more than the budgeted figure. The main reason for the deviation is that liabilities for holiday pay and for December's social security costs have been booked on the accounting date; these one-off items had not been budgeted.

Accounting principles

The balance sheet and profit and loss account for the Riksbank have been compiled as provided for in the Riksbank Act and in accordance with the Accounting Instruction that the Governing Council has approved for the Riksbank.

ALTERED ACCOUNTING PRINCIPLES

The gold reserve is valued as of 31 December 1998 at the market price, whereas previously it was booked at a fixed historical price.

Gold repos (gold swaps) are recorded gross as of 31 December 1998 (see below under Repo accounting). Previously, the proceeds were recorded net under 'Foreign banks and securities'. Assets used as collateral for repo transactions are reported off the balance sheet.

These changes—to market valuation of the gold reserve and gross recording of gold repos—are an adaptation to the rules for the consolidated balance sheet of the Eurosystem¹ and can therefore be regarded as good accounting practice for a central bank.

Transactions in the money and bond markets are booked on the trade day as of 31 December 1998. Previously they were registered on the trade day and treated as off-balance-sheet liabilities up to the settlement day.

Moreover, as of 31 December 1998 staff-related items such as holiday pay claims and liabilities in respect of social security contributions and pension commitments are included in the accounts, in the case of pension commitments as a memorandum item.

VALUATION PRINCIPLES

Assets and liabilities are booked at current market values, except in the case of fixed

assets. Securities are valued at the market's closing rate. Claims and liabilities in foreign currency are valued at the buying rate on the accounting day. Accrued interest is included in the market value of interest-bearing assets and liabilities.

Unrealized exchange gains/losses are credited/debited to the net operating results under 'Translation of exchange rates'. This item also includes the valuation of any forward position.

After the market valuation, interest received on securities represents the aggregate return in the form of interest as well as realized and unrealized price gains and losses. Partly on this account, changes in domestic and international interest rates may cause reported net revenue to fluctuate appreciably between accounting periods.

REPORTING OF BUSINESS TRANSACTIONS

Business transactions are recorded at the time when the parties exchange risks and rights. For money, bond and foreign exchange market transactions this implies trade-day accounting. Lending and borrowing transactions, including straight repo transactions, are booked on the payment day.

REPO ACCOUNTING

A repo is an agreement to sell assets such as securities and gold and simultaneously undertake to buy back equivalent assets at a specified price in the future.

These repurchase agreements are recorded as loan transactions and therefore do not affect the holdings of gold and securities.

Assets pledged by the Riksbank as collateral for repos are still included in the accounts and valued in accordance with the rules for the other holdings of securities.

The equivalent of the sales price is registered as a liability and the pledged assets are booked off the balance sheet.

Assets received by the Riksbank under reverse repos are not included in the accounts because they constitute loan collateral; the equivalent of the purchase price is registered as a claim.

The difference between the two payments in a repo (spot and forward) is treated on an account basis over the duration of the repo.

ACCOUNTING FOR MATERIAL FIXED ASSETS

Fixed material assets are booked at acquisition value and depreciated as planned. Write-downs are made for depreciation that is considered to be permanent. Buildings are depreciated over a period of 50 years, other fixed assets over 5–15 years. Inventories are written off over 3–7 years. In certain cases, personnel costs for internal development work on IT investments are included in the asset's acquisition value.

1. The ECB and the central banks of the 11 countries that have currently adopted the euro.

Balance sheet

31 DECEMBER

Assets, SEK million	Note	1998	1997
Gold and foreign assets			
Gold and foreign reserves			
Gold	1	13,834	909
Claims on the IMF	2	13,707	9,242
ECU claim on the ECB/EMI	3	-	10,598
Foreign banks and securities	4	108,735	70,239
		136,276	90,988
Other foreign assets	5	120	2,461
Domestic assets			
Treasury securities	6	32,842	53,088
Advances, banks	7	2,265	4,117
Monetary policy repos	8	41,581	36,216
Other domestic assets	9	203	1,124
		76,891	94,545
Fixed assets			
Fixed assets	10	1,087	1,175
Total assets		214,374	189,169
Liabilities, SEK million			
Foreign liabilities			
Net allocation of Special Drawing Rights in the IMF			
	11	2,838	2,641
Other foreign liabilities	12	4,100	3,983
		6,938	6,624
Domestic liabilities			
Deposits, banks	13	1,679	1,961
Deposits, other	14	-	7
Special accounts	15	15	34
Other domestic liabilities	16	341	3,864
		2,035	5,866
Currency in circulation			
Notes	17	82,288	78,986
Coins	18	3,980	3,809
		86,268	82,795
Balancing account and capital			
Balancing account	19	47,422	47,422
Capital	20	49,848	32,211
		97,270	79,633
Result for the year		21,863	14,251
Total liabilities and capital		214,374	189,169

Memorandum items, see note 32.

Profit and loss account

31 DECEMBER

SEK million	Note	1998	1997
Foreign operations			
Interest income	21	7,229	7,919
Interest expense	22	-417	-458
Translation of exchange rates	23	9,685	3,786
Total foreign operations		<u>16,497</u>	<u>11,247</u>
Domestic operations			
Interest on Treasury securities et cetera	24	4,263	3,602
Interest on loans to banks et cetera	25	1,630	496
Interest expense et cetera	26	-44	-197
Total domestic operations		<u>5,849</u>	<u>3,901</u>
Administrative income	27	169	149
Administrative expenses	28	-661	-633
Other income	29	17	21
Other expenses	30	-8	-5
Result before balance-sheet allocations		21,863	14,680
Balance-sheet allocations			
To balancing account	31	-	-429
Result for the year		21,863	14,251

Notes to the accounts

NOTE 1 GOLD

	1998	1997
Quantity		
Troy ounces (millions)	5.96	4.72
Price		
USD per ounce	287.40	42.22
SEK/USD	8.08	4.56
Book value, SEK million	13,834	909

The 1998 total of 5.96 million Troy ounces is equivalent to 185.4 tonnes. Excluding the gold in the ECB/EMI swap, the gold reserve booked in the 1997 accounts had a market value of SEK 10,825 million.

NOTE 2 CLAIMS ON THE IMF

SEK million	1998	1997
Special Drawing Rights in the IMF	3,341	2,943
Reserve position in the IMF	9,015	6,252
Advances under GAB	371	-
Advances under NAB	906	-
Accrued interest on claims	74	47
Total	13,707	9,242

The holding of SEK 3,341 million in Special Drawing Rights (SDRs) in the International Monetary Fund (IMF) is equivalent to 292 million SDRs. The Riksbank has been allocated a total of SDR 246.5 million for no real consideration; this gives rise to a balance-sheet liability (see note 11).

Sweden's capital contribution to the IMF totals SEK 18,463 million (SDR 1,614 million) and is booked net of the IMF's account for Swedish kronor as the item 'Reserve position in the IMF'.

During 1998 the Riksbank advanced SDR 32.5 million to the IMF under GAB and SDR 79.2 million under NAB, whereupon the IMF lent these amounts to Russia and Brazil, respectively. The Riksbank's total GAB and NAB undertakings in re-

spect of these two countries are SDR 142 million and SDR 251 million, respectively. The Bank's aggregate GAB and NAB commitments total SDR 859 million (see note 32).

NOTE 3 ECU CLAIM ON THE ECB/EMI

The Riksbank's ecu claim on the ECB/EMI, which arose from the creation of official ecus, was settled when the mutual swap agreement with the ECB/EMI expired on 31 December 1998.

NOTE 4 FOREIGN BANKS AND SECURITIES

Predominantly foreign treasury securities and government guaranteed securities, plus credit balances such as deposits and nostro accounts in foreign banks.

NOTE 5

OTHER FOREIGN ASSETS

This item includes the claim on the ECB in respect of the portion of the Riksbank's capital contribution to the EMI that was surplus to its capital contribution to the ECB.

NOTE 6

TREASURY SECURITIES

Treasury bills and bonds, as well as a small number of other bonds.

NOTE 7

ADVANCES, BANKS

This item comprises a total of SEK 25 million (28 million) in the form of advances on the banks' borrowing accounts with the Riksbank and SEK 2,240 million (4,089 million) in the form of overnight loans connected with fine-tuning transactions. The purpose of the latter transactions is to fine tune liquidity in the banking system so that the aggregate net position in the standing

facilities (deposits and advances) is close to zero (see note 13).

NOTE 8 MONETARY POLICY REPOS

Advances in the form of monetary policy repos, which involve the Riksbank buying and paying for securities and simultaneously agreeing to reverse the transaction at a specified future date. The equivalent of the payment is booked as a claim for the duration of the repo.

NOTE 9 OTHER DOMESTIC ASSETS

Mainly advances to Riksbank employees. The loans are arranged on normal banking terms and managed by agreement with Nordbanken.

NOTE 10 FIXED ASSETS

SEK million	1998	1997
Shares and rights		
AB Tumba Bruk 860,000 shares with par value at SEK 100 each	43	43
S.W.I.F.T. 13 shares with par value at BEF 5,000 each	0	0
Bank for International Settlements 16,021 shares with par value at 2,500 gold francs each	267	267
European Central Bank 5 per cent of 2.7 per cent of total rights	57	-
European Monetary Institute 2.9 per cent of total rights	-	165
Book value, shares and rights	367	475
Real estate		
Acquisition value	784	793
Accumulated depreciation prior to current year	-282	-263
Accumulated depreciation on items sold during year	33	1
Current year's depreciation	-18	-20
Book value, shares and rights	517	511

<table border="1"> <thead> <tr> <th>SEK million</th> <th>1998</th> <th>1997</th> </tr> </thead> <tbody> <tr> <td>Machinery and inventories</td> <td></td> <td></td> </tr> <tr> <td>Acquisition value</td> <td>527</td> <td>469</td> </tr> <tr> <td>Accumulated depreciation prior to current year</td> <td>-280</td> <td>-244</td> </tr> <tr> <td>Accumulated depreciation on items sold during year</td> <td>12</td> <td>12</td> </tr> <tr> <td>Current year's depreciation</td> <td>-56</td> <td>-48</td> </tr> <tr> <td>Book value, machinery and inventories</td> <td>203</td> <td>189</td> </tr> <tr> <td>Total fixed assets</td> <td>1,087</td> <td>1,175</td> </tr> </tbody> </table>	SEK million	1998	1997	Machinery and inventories			Acquisition value	527	469	Accumulated depreciation prior to current year	-280	-244	Accumulated depreciation on items sold during year	12	12	Current year's depreciation	-56	-48	Book value, machinery and inventories	203	189	Total fixed assets	1,087	1,175	<p style="text-align: center;">NOTE 14 DEPOSITS, OTHER</p> <p>The accounts with staff associations, Riksbank employees and others that were booked as a net item here for 1997 were closed in the course of 1998.</p> <p style="text-align: center;">NOTE 15 SPECIAL ACCOUNTS</p> <p>Statutory deposits by companies, mainly in the form of investment reserves. During 1998 the total in these deposits decreased by SEK 34 million to 15 million. The deposits in these accounts were to have been returned to the companies and taxed not later than in the 1996 tax year (the 1997 tax year for companies that were not assessed for tax in 1996). The amount remaining consists of deposits that have not yet been returned because of uncertainty about the depositor.</p> <p style="text-align: center;">NOTE 16 OTHER DOMESTIC LIABILITIES</p> <table border="1"> <thead> <tr> <th>SEK million</th> <th>1998</th> <th>1997</th> </tr> </thead> <tbody> <tr> <td>Liability with National Debt Office</td> <td>225</td> <td>247</td> </tr> <tr> <td>Suppliers' claims</td> <td>41</td> <td>27</td> </tr> <tr> <td>Valuation of forward position</td> <td>-</td> <td>34</td> </tr> <tr> <td>Balanced exchange effect of ECB/EMI swap</td> <td>-</td> <td>3,315</td> </tr> <tr> <td>Valuation of ECB/EMI-swap</td> <td>-</td> <td>212</td> </tr> <tr> <td>Other liabilities</td> <td>75</td> <td>29</td> </tr> <tr> <td>Total</td> <td>341</td> <td>3,864</td> </tr> </tbody> </table>	SEK million	1998	1997	Liability with National Debt Office	225	247	Suppliers' claims	41	27	Valuation of forward position	-	34	Balanced exchange effect of ECB/EMI swap	-	3,315	Valuation of ECB/EMI-swap	-	212	Other liabilities	75	29	Total	341	3,864	<p>claims totalling SEK 20 million and miscellaneous liabilities for settlement in 1999.</p> <p style="text-align: center;">NOTE 17 NOTES</p> <p>Value of banknotes in circulation, by denomination (SEK million)</p> <table border="1"> <thead> <tr> <th>Denomination</th> <th>1998</th> <th>1997</th> </tr> </thead> <tbody> <tr> <td>1 000 kronor</td> <td>40,999</td> <td>39,226</td> </tr> <tr> <td>500 kronor</td> <td>29,211</td> <td>27,157</td> </tr> <tr> <td>100 kronor</td> <td>9,431</td> <td>9,906</td> </tr> <tr> <td>50 kronor</td> <td>955</td> <td>962</td> </tr> <tr> <td>20 kronor</td> <td>1,355</td> <td>1,366</td> </tr> <tr> <td>10 kronor</td> <td>251</td> <td>277</td> </tr> <tr> <td>5 kronor</td> <td>86</td> <td>92</td> </tr> <tr> <td>Total</td> <td>82,288</td> <td>78,986</td> </tr> </tbody> </table> <p style="text-align: center;">NOTE 18 COINS</p> <p>Value of coins in circulation, by denomination (SEK million)</p> <table border="1"> <thead> <tr> <th>Denomination</th> <th>1998</th> <th>1997</th> </tr> </thead> <tbody> <tr> <td>10 kronor</td> <td>1,444</td> <td>1,371</td> </tr> <tr> <td>5 kronor</td> <td>901</td> <td>863</td> </tr> <tr> <td>2 kronor</td> <td>9</td> <td>9</td> </tr> <tr> <td>1 kronor</td> <td>880</td> <td>843</td> </tr> <tr> <td>0.50 krona</td> <td>208</td> <td>200</td> </tr> <tr> <td>Commemorations coins</td> <td>538</td> <td>523</td> </tr> <tr> <td>Total</td> <td>3,980</td> <td>3,809</td> </tr> </tbody> </table> <p style="text-align: center;">NOTE 19 BALANCING ACCOUNT</p> <p>This account has been used since 1988 in accordance with the guidelines that the Governing Board set forth that year for the disposition of the Riksbank's net revenue. Since then, the allocation to the balancing account has been booked on the year's profit and loss account.</p> <p>As of 1998 this allocation will be booked on the balance sheet for the year in which the disposition of net revenue is decided. This is a consequence of the revised Riksbank Act, which stipulates that the</p>	Denomination	1998	1997	1 000 kronor	40,999	39,226	500 kronor	29,211	27,157	100 kronor	9,431	9,906	50 kronor	955	962	20 kronor	1,355	1,366	10 kronor	251	277	5 kronor	86	92	Total	82,288	78,986	Denomination	1998	1997	10 kronor	1,444	1,371	5 kronor	901	863	2 kronor	9	9	1 kronor	880	843	0.50 krona	208	200	Commemorations coins	538	523	Total	3,980	3,809
SEK million	1998	1997																																																																																																			
Machinery and inventories																																																																																																					
Acquisition value	527	469																																																																																																			
Accumulated depreciation prior to current year	-280	-244																																																																																																			
Accumulated depreciation on items sold during year	12	12																																																																																																			
Current year's depreciation	-56	-48																																																																																																			
Book value, machinery and inventories	203	189																																																																																																			
Total fixed assets	1,087	1,175																																																																																																			
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<p>The Riksbank's fixed assets were incorporated in the balance sheet in 1994. The assets were booked at acquisition values less depreciation for the years for which the asset had been held. The Riksbank's collection of coins and medals is not included in the balance sheet</p>																																																																																																					
<p style="text-align: center;">NOTE 11 NET ALLOCATION OF SDRs IN THE IMF</p> <p>This liability is the counterpart of the Riksbank's allocation of Special Drawing Rights in the International Monetary Fund. The total allocation is currently SDR 246.5 million (see note 2).</p>																																																																																																					
<p style="text-align: center;">NOTE 12 OTHER FOREIGN LIABILITIES</p> <p>This item includes the Riksbank's SEK accounts with other central banks and international organisations (loro accounts). Repos with nonresidents and settlement payables are also booked here.</p>																																																																																																					
<p style="text-align: center;">NOTE 13 DEPOSITS, BANKS</p> <p>The balance of banks' deposit accounts with the Riksbank, SEK 84 million (130 million), and deposits arising from transactions for fine tuning and/or market maintenance, SEK 1,595 million (1,831 million). (See note 7.)</p>	<p>The liability with the National Debt Office consists of incoming payments that had not been transferred to the Office at the turn of the year.</p> <p>The balanced exchange effect and evaluation of the ECB/EMI swap were reversed when the swap was settled on 31 December 1998 (see note 4).</p> <p>Other liabilities include holiday pay</p>																																																																																																				

Governing Council shall continue to make proposals for the allocation of net revenue, while the balance sheet and profit and loss account are to be presented by the Executive Board. As before, both the proposals and the accounts are to be approved by the Riksdag.

NOTE 20 CAPITAL

The capital account of the Riksbank consists of:

SEK Million	1998	1997
Capital	1,000	1,000
Reserve fund	500	500
Contingency fund		
Allocations from net revenue	34,800	29,842
Write-up of gold reserve	12,686	-
Write-up of fixed assets	627	634
Write-up of BIS shares	235	235
Total	49,848	32,211

The Riksbank Act states that the Riksbank is to have capital in an amount of SEK 1,000 million, a reserve fund of SEK 500 million and a contingency fund. Since 1998 the contingency fund has been used in accordance with the guidelines set forth that year for the disposition of the Riksbank's net revenue. It is also used for entering the amounts of asset write-ups.

NOTE 21 INTEREST INCOME, FOREIGN OPERATIONS

Interest income as well as realized and unrealized profits and losses on securities.

As a consequence of the year-end valuation at market prices, unrealized profits and losses in the holding of foreign securities are included in the result.

NOTE 22 INTEREST EXPENSE, FOREIGN OPERATIONS

The greater part of this item consists of

interest on the net allocation of Special Drawing Rights in the IMF. The item also includes interest on the Riksbank's lora accounts with foreign banks and organisations as well as expenditure for stock-broking fees and charges for safekeeping and accounts in the management of the foreign exchange reserves. In 1998 the latter charges amounted to SEK 13 million (13 million).

NOTE 23 TRANSLATION OF EXCHANGE RATES, FOREIGN OPERATIONS

The net write-up by SEK 9,685 million (3,786 million) includes realized as well as unrealized exchange-rate effects on foreign assets and liabilities. The positive balance is a combined result of exchange rate movements and the composition of the foreign reserves.

NOTE 24 INTEREST ON TREASURY SECURITIES ET CETERA, DOMESTIC OPERATIONS

This item consists of all coupon interest as well as realized and unrealized profits and losses on holdings of domestic securities. As a consequence of the year-end valuation at market prices, unrealized profits and losses in the holding of domestic securities are included in the result.

NOTE 25 INTEREST ON LOANS TO BANKS ET CETERA, DOMESTIC OPERATIONS

Mainly interest income from the monetary policy repos.

**NOTE 26
INTEREST EXPENSE ET CETERA,
DOMESTIC OPERATIONS**
Mainly interest to banks on their deposit accounts with the Riksbank.

NOTE 27 ADMINISTRATIVE INCOME

SEK million	1998	1997
Notes and coins	100	88
Premium bonds	12	12
Clearing and settlement	9	10
Other income	48	39
Total	169	149

Income from notes and coins is earned on services performed for the Post Office, banks and other customers, for example counting, quality-sorting and packing of currency.

Premium bond income comes mainly from the Riksbank's participation in the issue and redemption of the National Debt Office's premium bonds.

Clearing and settlement income consists mainly of fees from banks and others for participation in the Riksbank's clearing and settlement system (the RIX system). The main items in other income are rent and the share dividends from Tumba Bruk and BIS.

NOTE 28 ADMINISTRATIVE EXPENSES

SEK million	1998	1997
Operating expenses		
Staff	302	270
Information, hospitality	11	11
Transport, travel	18	18
Consultant and other services	23	16
IT expenses	36	27
Economics Prize	13	12
Other operating expenses	67	47
Total operating expenses	470	401
Banknotes and coins	117	164
Depreciation	74	68
Total administrative expenditure	661	633

<p>Expenditure on information includes costs for the Riksbank's regular publications (for example the Annual Report, Statistical Yearbook, Quarterly Review, Inflation Report, and Financial Market Report), information projects, the staff magazine <i>Banco-posten</i> et cetera.</p> <p>Of the total of SEK 18 million in 1998 for transport and travel, foreign travel accounts for 11 million, travel in Sweden for 6 million and miscellaneous transport for the remainder.</p> <p>The main items under 'Other operating expenses' are the Riksbank's share of costs for the liquidation of the EMI (SEK 4 million), the contribution to the Royal Coin Cabinet (10 million), office expenses and real estate management.</p> <p>Expenses for notes and coins totalled SEK 117 million, of which 70 million for notes, 32 million for coins and 15 million for commemoration coins.</p> <p>NOTE 29 OTHER INCOME Income that is not assignable to the Riksbank's current operations or administration. The main item in 1998 is a capital gain on the sale of property in Gothenburg.</p> <p>NOTE 30 OTHER EXPENSES Expenses that are not assignable to the Riksbank's current operations or administration.</p> <p>NOTE 31 TO BALANCING ACCOUNT The portion of net revenue that is allocated to the balancing account has previously been booked through the profit and loss account for the same year. As of the 1998 accounts this portion is to be entered on the balance sheet in the year in which the disposition of net revenue is decided (see note 19).</p>	<p>NOT 32 MEMORANDUM ITEMS²</p> <p>Pledged collateral</p> <p>Securities with a face value equivalent to USD 70 million and DEM 75 million, pledged in connection with foreign securities repos.</p> <p>Securities with a face value equivalent to SEK 1,401 million, pledged in connection with Swedish securities repos.</p> <p>Securities with a face value equivalent to USD 21 million, pledged as marginal collateral.</p> <p>Gold in an amount of 1.1 million Troy ounces, pledged in connection with gold repos.</p> <p>Gold in an amount of 2.6 million Troy ounces, advanced as loans.</p> <p>Contingent liabilities</p> <p>Pension commitments totalling SEK 331 million.</p> <p>An agreement was concluded in 1998 whereby computers for home use are leased to Riksbank employees, who have the option of buying them after three years at the current market price.</p> <p>Commitments</p> <p>Mutual short-run exchange support agreements with the Nordic central banks to provide up to ECU 2,000 million, with the credit provided by any one central bank limited to ECU 1,000 million, except that for the Icelandic central bank the limits are ECU 200 million and 100 million.</p> <p>Mutual short-run exchange support agreement with one central bank.</p> <p>Agreement under the General Arrangements to Borrow (GAB) to provide the IMF with a credit facility of up to SDR 382³ million, of which SDR 32.5 million has been paid out.</p> <p>Agreement under the New Arrangements to Borrow (NAB) to provide the IMF with a credit facility of up to SDR 859³ million, of which SDR 79.2 million has been paid out.</p> <p>Guarantee for an amount of USD 300 million on loans to Brazil from the Bank for International Settlements; the Government has decided to request the Riksdag to issue a sovereign guarantee for this commitment.</p> <p>Standby credits with foreign banks.</p> <p>Undertaking to lend up to USD 312.5 million to South Korea as part of a second line of defence.</p> <p>At end 1998 there was no outstanding forward currency position; at end 1997 there had been a negative</p>	<p>tive position with a nominal value of SEK 155 million, equivalent to a negative market value of SEK 34 million.</p> <p>Forward interest rate contracts outstanding with a positive value at end 1998 totalled SEK 7,961.8 million (5,221 million) in nominal terms and SEK 37.9 million (5 million) at market prices. Such contracts with a negative value totalled SEK 2,175.8 million (5,260 million) in nominal terms and SEK 8.1 million (4 million) at market prices.</p> <p>Undertaking to pay in an amount equivalent to SDR 781.5 million in the form of an additional capital contribution to the IMF.</p> <p>Agreements whereby the Riksbank guarantees the value of Swedish Treasury securities and housing bonds that are pledged as collateral for intraday credits between commercial banks and central banks in the euro area.</p> <p>Undertaking to provide the Nobel Foundation with funds for the annual award of a prize in economic sciences in memory of Alfred Nobel.</p> <p>2. Amounts are given in the relevant currency; 1998 year-end exchange rates, expressed in SEK, are 8.07 for 1 USD, 4.84 for 1 DEM, 9.48 for 1 ECU, 11.44 for 1 SDR and 2,320.61 for 1 Troy ounce of gold.</p> <p>3. The combined GAB and NAB commitment is limited to SDR 859 million; the IMF carries the credit risks.</p>

PROPOSED ALLOCATION
OF NET REVENUE
FOR 1998

FIVE-YEAR OVERVIEW

Proposed allocation of net revenue for 1998

The Governing Council of the Riksbank has received a report on the 1998 financial year from the Executive Board, in accordance with Article 3, Chapter 10 of the Riksbank Act (1988:1385, with amendments). The Governing Council considers that the guidelines for the disposition of net revenue that were set forth by its predecessor, the Governing Board, in 1988 remain appropriate for the disposition of net revenue in 1998. On 12 February 1999 the Governing Council accordingly decided to submit the

following proposal for the disposition of the Riksbank's net revenue.

Disposition of net revenue in 1998, which totals SEK 21,863 million before balance-sheet allocations:

SEK million	
Transfer to the Treasury	7,600
To Contingency Fund	10,639
To Balancing Account	3,624
Total	21,863

Five-year overview

SEK billion	1998	1997	1996	1995	1994
Balance sheet					
Gold and foreign assets	136,396	93,449	140,241	171,325	181,786
Domestic assets	76,891	94,545	71,184	85,112	90,319
Fixed assets	1,087	1,175	1,169	864	654
Total assets	214,374	189,169	212,594	257,301	272,759
Foreign liabilities	6,938	6,624	6,583	5,941	6,146
Domestic liabilities	2,035	5,866	37,888	98,129	125,635
Currency in circulation	86,268	82,795	80,791	76,660	76,442
Balancing account and capital	97,270	79,633	73,276	72,025	55,942
Net revenue	21,863	14,251	14,056	4,546	8,594
Total liabilities and capital	214,374	189,169	212,594	257,301	272,759
Profit and loss account					
Foreign operations	16,497	11,247	14,230	18,546	-727
Domestic operations	5,849	3,901	4,806	666	-8,850
Administrative income	169	149	145	144	131
Administrative expenses	-661	-633	-541	-533	-598
Other	9	16	-10	-7	-11
Result before balance-sheet allocations	21,863	14,680	18,630	18,816	-10,055
Balance-sheet allocations	-	-429	-4,574	-14,270	18,649
Result for the year	21,863	14,251	14,056	4,546	8,594

On 27 January 1759 Carl Michael Bellman, better known today as a poet and troubadour, appears before the Bank of the Estates of the Realm to be examined for his insights into studies and bookkeeping:

- asked, what is posting? Replied, transferring to the ledger.
- asked, whereto what I owe be entered? Replied, entered as debit Capital account and credit Sundry.
- asked, how to enter what passeth during the year? Rep: in their particular accounts.
- asked, be what one has to claim debited? Replied, yes.
- asked, when capital is borrowed, be it debited or credited? Rep: Credited.
- When a month be posted, asked, how its accuracy be tested? Repld: by trial balancing.
- asked, what this doth signify? Rep: see whether the items be correctly entered in debit and credit.
- asked H. Comm: whether it be not understood by summing? Rep. yes.

Whereafter was granted to him upon request permission now to do service in the Bank.



NOBEL MEMORIAL PRIZE IN
ECONOMIC SCIENCES

Profounder understanding of welfare issues

LAUREATES:

- 1969 R. FRISCH AND J. TINBERGEN
- 1970 P. SAMUELSON
- 1971 S. KUZNETS
- 1972 J.R. HICKS AND K.J. ARROW
- 1973 W. LEONTIEF
- 1974 G. MYRDAL AND F.A. VON HAYEK
- 1975 L. KANTOROVICH AND T.C. KOOPMANS
- 1976 M. FRIEDMAN
- 1977 B. OHLIN AND J. MEADE
- 1978 H.A. SIMON
- 1979 T.W. SCHULTZ AND A. LEWIS
- 1980 L.R. KLEIN
- 1981 J. TOBIN
- 1982 G. STIGLER
- 1983 G. DEBREU
- 1984 R. STONE
- 1985 F. MODIGLIANI
- 1986 J.M. BUCHANAN
- 1987 R.M. SOLOW
- 1988 M. ALLAIS
- 1989 R. HAAVELMO
- 1990 H. MARKOWITZ, M. MILLER AND W. SHARPE
- 1991 R. COASE
- 1992 G.S. BECKER
- 1993 R.W. FOGEL AND D.C. NORTH
- 1994 J.C. HARSANYI, J.F. NASH AND R. SELTEN
- 1995 R.E. LUCAS JR.
- 1996 J.A. MIRRELEES AND W. VICKREY
- 1997 R.C. MERTON AND M.S. SCHOLES
- 1998 A. SEN



Professor Amartya Sen in an interview in December 1998 at the Royal Swedish Academy of Sciences.

The Sveriges Riksbank Prize in Economic Sciences in Memory of Alfred Nobel was awarded for 1998 to Professor Amartya Sen, who has improved the theoretical foundation for comparing different distributions of society's welfare and defined new poverty indexes.

Instituted in 1968 in connection with the tercentenary of the Riksbank, the Sveriges Riksbank Prize in Economic Sciences is awarded annually for work in economic sciences of the outstanding importance referred to in Alfred Nobel's will dated November 27th, 1895. The Swedish Academy of Sciences makes the award in accordance with the principles for the Nobel Prizes instituted under that will and the prize equals the amount fixed for each of those prizes.

THE 1998 LAUREATE

For 1998 the prize was awarded to Professor Amartya Sen, Trinity College, Cambridge, England, for key contributions to research on fundamental problems in welfare economics. His contributions range from axiomatic theory of social choice, over definitions of welfare and poverty indexes, to empirical studies of famine. Professor Sen has clarified the conditions which permit aggregation of individual

values to collective decisions, and the conditions which permit rules for decision making that are consistent with a sphere of rights for the individual. By analysing the available information about different individuals' welfare when collective decisions are made, he has improved the theoretical foundation for comparing different distributions of society's welfare and defined new and more satisfactory poverty indexes. In empirical studies, Professor Sen's applications of his theoretical approach have enhanced our understanding of economic mechanisms underlying famines.

Can the values which individual members of society attach to different alternatives be aggregated into values for society as a whole, in a way that is both fair and theoretically sound? When and how can we compare the distribution of welfare in different societies? What are the factors that trigger famines? By answering question such as these, Amartya Sen has made a number of noteworthy contributions to central fields of economic science and opened up new fields of study for researchers. By combining tools from economics and philosophy, he has restored an ethical dimension to the discussion of vital economic problems.

Press conferences on the Internet

PUBLIC
INFORMATION

The screenshot shows the Riksbank website interface. At the top, there is a navigation bar with the Riksbank logo and text in Swedish and English. Below this, there are several sections: 'SENASTE NYTT' (Latest News) with a list of recent press releases; 'RÄNTOR' (Interest Rates) with a table showing rates for Repo, short-term, long-term, and KPI; 'VALUTAKURSER' (Exchange Rates) with a table for the Euro; 'DETTA HITTAR DU ÄVEN PÅ VÅR SITE' (You will also find this on our site) with a list of links to various resources; and 'KAMPAJNYTTA' (Campaign News) with a notice about tax-free withdrawal times. There are also images of banknotes and a 'PRESSCENTER' section.

During 1998, a growing proportion of the information provided by the Riksbank was available on the Internet. This is an idea for the website's new layout – the Swedish version – from spring 1999.

The Riksbank had launched a home page in March 1997, since when there has been a substantial increase in the amount of information that is provided about the Riksbank and its operations. The major innovation during 1998 was the camcorder transmission of Riksbank press conferences on the Internet website.

The website includes information about the amended Riksbank Act that applies as of 1999. There is a presentation of the Executive Board, together with the Riksbank's new procedures, including the matters that are decided by the different bodies. Current information about and from the Riksbank includes press releases, speeches, submissions and minutes from meetings of the Executive Board and the Governing Council. A calendar lists the dates of Executive Board meetings as well as the publication dates for the minutes of monetary policy meetings and the Inflation Report.

Most of the statistics produced by the Riksbank are likewise included in the website. The Inflation Report and the Financial Market Report are also available, as are most other reports, in PDF files for direct downloading. Other items are information about and pictures of banknotes and coins, as well as information about EMU and links to other central banks and associated bodies such as the IMF, the World Bank, BIS and the ECB.

INTERNET NEWS

In the spring of 1999 both the content and the layout of the home page are to be renewed. The Riksbank will also be introducing a computer game, Star Gold, on its website, with upper secondary pupils as the target group. The purpose of the game is to provide insights into the Riksbank's primary objective, price stability, and the foundations for monetary policy.

PRIZE FOR ANNUAL REPORT
It can also be mentioned that among the entrants to the Swedish Publishing Prizes for 1998, the Riksbank won first prize in the annual report category.

RIKSBANK PUBLICATIONS
IN ENGLISH
The number of Working Papers published in 1998 was a record, 25 titles (listed on the website). One Occasional Paper, describing the RIXMOD economic model, was presented.

- Periodical publications**
- Annual Report (1/year)
 - Statistical Yearbook (1/year)
 - Financial Market Report (2/year)
 - Inflation Report (4/year)
 - Quarterly Review (4/year)

Ad hoc publications

- The Euro in the Swedish Financial Sector – situation report 2, January 1998
- The Euro in the Swedish Financial Sector – situation report 3, January 1999

EMI-/ECB-publications

- Assessment of EU securities settlement systems against the standards for their use in ESCB credit operations – September 1998
- Standards for the use of EU securities settlement systems in ESCB credit operations – January 1998

All these publications are available free of charge from the Riksbank's Information Centre:

Internet: www.riksbank.se
E-mail: info@riksbank.se
Telefax: +46 8 787 01 26
Telephone: +46 8 787 01 00

Lowest interest rate since the 1950s

2 JANUARY

The *official discount rate* (reference rate) is confirmed by the Riksbank Governor at 2.5 per cent (unchanged).

1 APRIL

The *official discount rate* (reference rate) is confirmed by the Riksbank Governor at 2.5 per cent (unchanged).

4 JUNE

The *fixed repo rate* is lowered by the Riksbank Governor from 4.35 to 4.10 per cent with effect from 9 June.

1 JULY

The *official discount rate* (reference rate) is confirmed by the Riksbank Governor at 2.0 per cent with effect from 2 July.

1 OCTOBER

The *official discount rate* (reference rate) is confirmed by the Riksbank Governor at 2.0 per cent (unchanged).

3 NOVEMBER

The *fixed repo rate* is lowered by the Riksbank Governor from 4.10 to 3.85 per cent with effect from 4 November.

12 NOVEMBER

The Riksbank's *deposit and lending rates* are lowered, in each case by 0.5 percentage points, to 3.25 and 4.75 per cent, respectively, with effect from 18 November.

24 NOVEMBER

The *fixed repo rate* is lowered by the Riksbank Governor from 3.85 to 3.60 per cent with effect from 25 November.

15 DECEMBER

The *fixed repo rate* is lowered by the Riksbank Governor from 3.60 to 3.40 per cent with effect from 16 December.

PHOTO: MATS LUNDOVIST, NILS-INGVAR SVENSSON,
BERNO HJÄLMRUD, JONAS KARLSSON/BILDHuset,
STEFAN BOHLIN, LARS FÖRSSTEDT, GUNILLA WELIN/ETC BILD,
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JEAN-MARC TRUCHET/TONY STONE IMAGES,
* C.M. BELLMAN - P. KRAFFT Srf., NATIONALMUSEUM,
STOCKHOLM, SWEDEN.



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