Monetary policy minutes

March 2024

S V E R I G E S R I K S B A N K

MONETARY POLICY MINUTES

Executive Board, No. 2

DATE: 26 March 2024

TIME: 9:00

DOCUMENT CLASSIFICATION: RB PUBLIC

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Robin Ahlén (§1-3a)
Maria Johansson (§1-3a)

It was noted that Hans Dellmo and Dominika Krygier would prepare the draft monetary policy minutes. These minutes cover only §§ 3-4.

§3a. Economic developments

Market developments since the last monetary policy meeting

Robin Ahlén, economist at the Markets Department, began by presenting the latest developments on the financial markets. Since the previous monetary policy meeting in January, government bond yields have risen in general. The upturn has taken place in light of resilient economies and higher inflation than expected, especially in the United States, and central bank committee members who rejected market expectations of rate cuts at the beginning of the year. During this period the market has reduced its expectations of the number of policy rate cuts this year by the US and European central banks, from around six to three or four. The market is largely expecting synchronised policy rate cuts among most G10 countries, although the spread of the expectations has increased somewhat this year.

Recent central bank announcements have led to government bond yields falling again somewhat. The Swiss central bank unexpectedly cut its policy rate and the Bank of England indicated that its next step will be a rate cut. The Federal Reserve left its policy rate unchanged, but the members' median forecasts still indicate three rate cuts this year, despite the forecasts for inflation and growth being revised up. Norges Bank indicated, as before, that there would be a cut in September, while the Japanese central bank left negative interest rates behind and concluded its so-called yield curve control, in the light of high wage increases, among other factors. The ECB left its policy rate unchanged in March, but the members have indicated that the policy rate may be cut in June. However, cuts after that are a more open question and will depend on the data.

Despite the higher interest rates, risky assets have continued to develop strongly. Credit spreads for companies with both low and high credit ratings are at the lowest levels in over two years. Stock exchanges have risen to new record levels, supported in particular by strong economic developments in the United States, hopes of AI, and expectations of interest rate cuts. In China developments are weaker, but stock markets have also recovered somewhat as a result of stimulus and signs of better economic activity.

The US dollar has strengthened given the strong US data and shifts in expectations of monetary policy in relation to other countries. The krona has to a large degree been affected by international factors and has weakened against the euro and the dollar recently. The market's pricing of inflation has risen in the short term in the United States and Europe since the previous monetary policy meeting, but the long-term market-based expectations are stable and support the picture of inflation falling towards the target.

Prior to the Riksbank's monetary policy decision in March, analysts are expecting an unchanged policy rate, which is also indicated in market pricing. A first rate cut is expected in May or June, and apart from inflation prospects, many analysts mention that the timing will depend on the development of the krona and when other central banks cut their policy rates, in particular the ECB. Market pricing indicates a policy rate just over 3 per cent towards the end of 2024. The Riksbank's updated forecast for the policy rate is expected to indicate a relatively high probability of a policy rate cut during the first half of the year and one or more further cuts in 2024. No one is expecting any changes to securities sales.

Financial stability - current situation and risks

Olof Sandstedt, Head of the Financial Stability Department, described the situation in the Swedish financial system. The system is functioning well in general, but higher interest rates are putting pressure on both households and companies.

The major banks’ large exposure to highly-indebted real estate companies still comprises a vulnerability. However, the situation for real estate companies has improved somewhat recently. Financing terms and conditions on the bond market are more advantageous and more real estate companies have been able to issue bonds. At the same time, there are risks linked to real estate companies’ operations. For instance, vacancy levels are elevated. The values of companies’ real estate could also fall more if interest rates remain high and economic activity slows down even more. Real estate companies therefore need to continue reducing their risks.

The major Swedish banks are assessed to have a good starting situation and they have margins above the formal capital requirements. However, company bankruptcies have increased, although this has so far had a limited impact on the major banks’ loan losses. The risk of default is elevated with regard to consumer loans, which can entail problems for institutions that focus on these loans.

The current monetary policy drafting process – new data and forecasts

Carl Andreas Claussen, Senior Adviser at the Monetary Policy Department, presented the current assessment of macroeconomic developments and the proposal for a monetary policy decision that the Monetary Policy Department judges will gain majority support in the Executive Board at today’s meeting. The basis for today’s decision has been discussed by the Executive Board at meetings on 12, 13 and 15 March. The draft Monetary Policy Report was tabled and discussed at a meeting of the Executive Board on 20 March.

As the Executive Board has already noted at the monetary policy meeting on 31 January this year, the risk of inflation becoming entrenched at levels that are too high has declined. Central questions in the preparations for the current meeting have been how monetary policy can best be formulated given the current developments in inflation and the remaining risks to inflation. The prospects for inflation and interest rates abroad have also been in focus. This applies not least to developments in the US economy and the Executive Board has discussed possible consequences for the Swedish economy and monetary policy if the US economy continues to develop more strongly than expected and the sluggishness in the downturn in inflation persists.

With regard to recent developments, the US economy has thus been surprisingly strong, while growth in the euro area has been considerably weaker. This is due in part to the euro area economies being hit harder by the energy crisis following Russia's invasion of Ukraine. In addition, fiscal policy has been less expansionary in the euro area than in the United States. However, the labour markets have developed strongly in both the euro area and the United States.

The forecast assumes that international economic activity will improve. From the end of 2025 onwards, weighted GDP growth in Sweden's most important trading partners is expected to be around 2 per cent a year, which is just below the historical average since 1980.

The downward trend in inflation has continued both in the euro area and the United States, but the fall in inflation has to some extent come to a halt in recent months, especially in the United States. It is services prices that have held up inflation in both the euro area and the United States, which is due among other things to wages, which are important for services prices, having increased relatively fast. In the United States, it is to a large degree rents that are contributing to the sluggishness in the downturn in inflation.

However, inflation abroad is expected to fall going forward. In the euro area, HICP inflation is expected to fall back to the target of 2 per cent as early as the second half of this year, while CPI inflation in the United States is not expected to be close to 2 per cent until the beginning of 2025. Inflation in the United States is measured in terms of both the CPI and the PCE (consumption deflator). The Federal Reserve mainly looks at PCE inflation. PCE-inflation has fallen faster than CPI inflation and was in January much closer to 2 per cent than CPI inflation.

Considerable uncertainty remains with regard to global inflation. This concerns, for instance, geopolitical tensions – which can affect energy prices and companies' costs – and uncertainties linked to the strength of developments in the United States and the euro area. This is discussed in alternative scenarios in the draft report.

In Sweden, economic activity has continued to slow down. The slowdown is still driven by the interest-sensitive parts of the economy, such as household consumption and housing investments. At the same time, net exports have continued to develop strongly.

Confidence among consumers and companies has begun to recover, however, and economic activity is expected to gradually increase over the course of the year. Household consumption is predicted to recover somewhat in the first half of this year, as inflation falls back and real wages increase. However, reduced employment is forecast to partially hold back consumption growth. Housing investment is expected to recover towards the end of the year. In 2025 and 2026, GDP is expected to grow by around 2 per cent as an annual rate. Unemployment is estimated to rise somewhat going forward and peak at 8.4 per cent this year. Compared with the forecasts in November, the prospects are somewhat better.

If we look at inflation in Sweden, it has fallen slightly more than expected. Measured as the CPIF and the CPIF excluding energy, it amounted to 2.5 and 3.5 per cent respectively, as an annual rate, in February. Price changes in the shorter term have fallen, and are now in general close to 2 per cent, as an annualised rate. The rate of wage increases has risen as expected in recent months.

Forward-looking indicators point to a continued fall in inflationary pressures. Companies' price plans have fallen further and are largely in line with price increases of 2 per cent. The Riksbank's Business Survey for February also shows that price plans among household-related companies are falling. The forecast assumes that wage growth will slow down some way into 2024 in line with the profile for the agreed wage increases.

Overall, inflation measured both as the CPIF and the CPIF excluding energy is expected to continue to fall and reach 2 per cent within the next year. CPIF inflation is expected to reach the target earlier, around the middle of 2024, which is explained by energy prices being expected to be much lower than last year. CPI inflation is expected to be higher than the other inflation measures in 2024, due to earlier interest-rate increases, but will reach 2 per cent at the beginning of 2025. Developments are in line with what was expected in November, and the inflation forecast is largely unchanged.

However, there remains a risk of setbacks for inflation, and there are several reasons why inflationary pressures could increase once again. As discussed in the draft report, this concerns geopolitical tension, the development of the krona, how domestic demand develops and companies' pricing behaviour.

The proposed forecast in the draft report is based on the proposal for monetary policy described in Annex A to the minutes and which the Monetary Policy

Department judges will gain a majority in the Executive Board at today's meeting. The proposal is that the policy rate is held unchanged at 4 per cent at today's meeting. Further, it is assumed that the policy rate will be cut gradually over the year. The forecast proposal implies around three cuts of 0.25 percentage points on each occasion. At the same time, the Riksbank's asset holdings will continue to decrease through maturities and the sales of government bonds decided on in January.

Mattias Erlandsson, Deputy Head of the Monetary Policy Department, briefly described the current statistics with regard to Swedish producer prices and the National Institute of Economic Research's Economic Tendency Survey.

§3b. The economic situation and monetary policy

Deputy Governor Per Jansson:

I support the forecasts and the monetary policy assumptions in the draft Monetary Policy Report. At our last monetary policy meeting on 31 January, I considered it "not . . . impossible" that a first policy-rate cut could be implemented as early as at today's meeting. For this to come into question, however, my opinion was that not only would the favourable development of inflation have to continue, but the plans for policy-rate cuts from the major central banks abroad would probably also need to be outlined much more clearly. Overall, I considered it not "particularly probable" that such conditions would prevail as early as at today's meeting and thought therefore that a first cut at the meeting in either May or June was much more realistic. To be on the safe side, I also pointed out that it was of course impossible to rule out a worse scenario in which we would have to wait until after the summer before implementing a first rate cut.

At today's meeting, I would like to provide an update on my view of the appropriate time to start cutting the policy rate. That I have concluded that it is too early to make the first cut at today's meeting follows of course directly from my support for the monetary policy assumptions made in the draft report. As I see it, it is possible to support the monetary policy in the draft report but nevertheless have some dissenting opinions. The question is when these dissenting opinions become so large and significant that they can no longer be expressed as verbal nuances and scepticism but require a formal reservation. This is of course a boundary that all Executive Board members must draw for themselves. But having the opinion that the policy rate should be cut right now is probably something that no one thinks can be combined with support for the monetary policy assumptions in today's draft report.

Having said that, I still see a value in providing some clarification for why I myself have come to the conclusion that it is too early to cut the policy rate at today's meeting. If we look first at the development of inflation, it is actually possible to consider it as fulfilling the requirement of already being sufficiently favourable to be compatible with a rate cut now.

Since our last meeting, we have had two new inflation outcomes, for January and February, which indicate that inflationary pressures are continuing to ease. CPIF inflation is still being affected quite considerably by sharp fluctuations in energy prices and rose from 2.3 per cent in December to 3.3 per cent in January. But in February, CPIF inflation fell back again and was largely at the same level as in December, 2.5 per cent. In the period ahead, energy prices are predicted to have less and less of an impact on CPIF inflation and after having remained at approximately its current level for a few months, CPIF inflation is expected to be very close to the inflation target from the summer of this year onwards. However, inflation excluding energy prices is declining steadily in relatively large steps. Since December, it has decreased by nearly 2 percentage points, spread quite evenly over January and February, and amounted to 3.5 per cent in February.

The more high-frequency measures of price growth in general provide support to the assessment that inflation as an annual rate continues to fall back towards the target. The monthly changes in CPIF inflation, various measures of underlying inflation and the larger consumer price sub-groups decreased almost without exception in February. The rates of price increases over the last three and six months also generally paint a bright picture of developments, especially if one takes into account that the, in many cases, very low monthly change for November is now falling out of the three-monthly trend.

Perhaps the most worrying aspect is the sluggishness one can see in the decline in services inflation. Here, measures at different frequencies are showing a tendency to stick around annual rates of 5 per cent or just slightly lower. As the weight of services prices in the consumer price index is just over 45 per cent, it is very important that the adjustment in these price increases does not stop here. At the same time, one should remember that it is entirely natural for services inflation to be quite significantly higher than goods inflation on average. So although services prices are still increasing too quickly, the decline we need to see going forward in order for price growth to be compatible with the inflation target does not necessarily need to be very large. Another circumstance to consider in the context is that a not insignificant part of the rapid rate of increase in services prices has to do with earlier cost increases and certain specific events. The transitory nature of these drivers indicates lower price increases in the period ahead.

Yet another aspect here is that monetary policy must be designed looking forward in time. If we cut the policy rate too early, the "last mile" can be long and difficult.

On the other hand, cutting the rate too late could cause problems with below-target inflation. I have considerable sympathy with the view in the draft report that we, after the very high inflation of recent years and changed pricing behaviour, need to have further confirmation that inflation really is on its way to stabilising close to the target. But the timing of when it is appropriate to start cutting the policy rate is a very difficult question and, in any case, it needs to happen at some point before inflation has reached the inflation target – the question is just how close to the target one needs to be before it is time to act.

So, it is not first and foremost the development of inflation that has led me to my conclusion that it is best to wait a little longer before cutting the policy rate. Instead, it is primarily that the likelihood of more serious delays in the Federal Reserve's rate cuts has increased. And it cannot be ruled out that a postponement of monetary policy easing in the United States may ultimately have a bearing on the timing of the ECB's rate cuts as well.

Before I continue to elaborate on these thoughts, allow me to note that an additional factor to consider here is the recent, rather unfavourable development in the krona exchange rate. Against the euro, the krona exchange rate is today more or less on the same level as before the publication of the monetary policy decision in November last year. Against the US dollar, the krona exchange rate has even depreciated slightly over the same period. This less favourable starting point for the krona exchange rate is obviously not without significance in the context.

If we return to the Federal Reserve's rate-cutting plans, it can be noted that the central bank's latest decision on 20 March was received with optimism by markets. There are many indications that this was to a large extent linked to only minor changes being made to the monetary policy plans for the current year. Here, the interpretation of markets is still that the rate will be cut three times by 0.25 percentage points in 2024, probably starting in June. Beyond 2024, however, the Federal Reserve ratcheted up its policy-rate expectations a little. This, together with a strongly performing real economy and the slow adjustment of inflation towards target, leaves the door ajar for an adjustment to the rate-cutting plan also in the short term. That this is a risk that must be taken seriously is underlined by comments from both representatives of the Federal Reserve and market analysts. As I have already mentioned, it cannot be ruled out that a postponement of rate cuts in the United States may also have a bearing on the ECB's monetary policy plans, especially of course if the delay becomes significant. All this is naturally bad news for the krona exchange rate and ultimately creates risks for the inflation outlook.

If I sum up the conditions for a first policy-rate cut already at today's meeting, I conclude that, although the development of inflation looks favourable enough, the uncertainty surrounding the timing of rate cuts at the major central banks abroad is still too great, and has even increased. This summarises in a nutshell why I today support the decision to leave the policy rate unchanged at 4 per cent.

So what do the conditions look like for cutting the policy rate at our next meeting on 7 May? From what I have said today about the development of inflation, it is clear that I am quite satisfied with the current situation. If inflation edges down a little further, maybe thanks to lower rates of increase in services prices, it would naturally not be unwelcome. But the important thing here is above all that developments do not deteriorate. Instead, I see the major threat to being able to cut the rate in May, in line with what I have said above, coming from postponements in the rate-cutting plans of the Federal Reserve and the ECB. More significant delays in these plans risk causing the unfavourable development of the krona exchange rate to continue, or even to worsen. This may in turn delay the adjustment of inflation towards target, in the worst case, in a serious way. Against this backdrop, the Federal Reserve's meeting on 1 May will be very important.

Deputy Governor Martin Flodén

I support the proposal to leave the policy rate unchanged today and the analyses and considerations presented in the draft Monetary Policy Report.

At our last monetary policy meeting, in January, I said that the picture of inflationary pressures returning to levels compatible with the inflation target had become clearer. My assessment was that a policy rate cut could be appropriate during the second or third quarter if the prospects for inflation continued to improve. I pointed to the monthly rates of underlying inflation and forward-looking indicators, such as companies' price plans.

These variables have continued to develop favourably. We have received two new inflation outcomes, for January and February. In January, rents and certain administratively set prices rose quickly, but this was expected. In February, inflation was slightly lower than expected. Although the monthly rate for services prices was unexpectedly high, this is largely explained by a few individual, and presumably volatile, prices of tickets to sporting events.

I would like to reiterate that these subdued price increases have occurred in an environment where monetary policy is contractionary and demand in the economy is weak. Therefore, fact that price increases have been in line with the inflation target for a while does not necessarily mean that inflationary pressures are normal.

But there are many indications that inflationary pressures are now approaching normal levels and that it will therefore soon be appropriate to start loosening monetary policy. Companies' price plans in both the National Institute of Economic Research's Economic Tendency Survey and the Riksbank's Business Survey are now at levels that are compatible with the inflation target. Producer prices have stabilised recently. Different measures of inflation expectations, at different horizons, are now at favourable levels. And wages are not rising disconcertingly rapidly.

All this suggests that a policy-rate cut can be justified at one of the next monetary policy meetings.

Let me focus on remaining factors that suggest it is not appropriate to cut the rate today and that may remain important when we are to decide on a possible rate cut at our next monetary policy meeting.

The first factor is the geopolitical tensions and the risk of them leading to new supply shocks, which in turn give rise to new cost increases. It is difficult to paint a positive picture of the geopolitical situation, but I judge that the risk of developments leading to new cost shocks has nevertheless subsided somewhat in recent months. I would feel even more secure in this judgement if global energy and commodity prices remain stable one or two more months despite the geopolitical situation.

Another international factor to monitor is the surprisingly strong developments in the US economy. The combination of strong demand in the United States and global supply shocks was a key cause of the rapid rise in inflation in Sweden in 2022. I see the risk of us receiving a similar cost impulse in the near future as quite small, primarily because I expect the US central bank would now rapidly adjust its monetary policy to such developments.

But this means that their monetary policy reaction may instead have an impact via the exchange rate. Expectations of US monetary policy have shifted clearly in a contractionary direction in recent months, and the dollar has appreciated as a result. A challenge to the Riksbank's monetary policy is that US monetary policy seems recently to have had a particularly large impact on the Swedish exchange rate; information indicating higher US inflation seems also to lead to a depreciation of the krona against currencies other than the dollar.

The krona's development, as is well known, is also one of the factors that affect the Riksbank's conditions for cutting the rate in the near term. The krona has depreciated a few per cent against both the US dollar and the euro in recent weeks. If this development continues, import prices risk starting to rise again. In that case, monetary policy may have to remain contractionary for longer.

Linked to the risk of the krona depreciating, we often receive questions as to whether the Riksbank can cut the policy rate earlier than other central banks. I do not think that an early Swedish rate cut need have a major impact on the exchange rate. But this assumption is partly based on the rate being cut in a situation where it is sufficiently clear that other central banks are also close to cutting their rates.

The assumption is also based on an early initial rate cut not leading to expectations that the Riksbank will then continue to cut the rate by more and faster than other central banks.

My expectation is the reverse, i.e. that the Riksbank's rate cuts will be smaller and slower when monetary policy moves towards a less contractionary level. As the Swedish economy is interest-rate sensitive, we can expect rate adjustments to have a faster and greater pass-through here than abroad. For this reason, the Riksbank increased its policy rate less than both the US and the European central banks when monetary policy needed tightening in 2022 and 2023. It is also likely that our cuts will be smaller. This, in combination with my judgement that the krona is significantly undervalued, suggests that the krona will appreciate.

Fiscal policy may also have contributed to smaller rate increases in Sweden. In several other countries, fiscal policy has been relatively expansionary in recent years and has thereby increased the need for contractionary monetary policy. In Sweden, where public finances are strong, there is not now the same need for fiscal policy consolidation as in many other parts of the world. It is therefore feasible that future Swedish fiscal policy, once inflationary pressures have eased, will be more expansionary than it is abroad. This may further contribute to the Riksbank cutting the rate more slowly than other central banks. Ultimately, also this could support a stronger krona.

A concluding factor I would like to mention relates to expectations. Despite the Swedish economy being very interest-rate sensitive, a policy-rate cut of 0.25 percentage points should not have a particularly substantial effect. Monetary policy should remain contractionary even if the policy rate were several points lower than today. But after the rapid rate hikes of the last two years, it is possible that a rate cut – the first in over eight years – will be seen as an important turning point.

I see signs of increased optimism, for example in the housing market, already as a result of us not having increased the policy rate at several consecutive meetings and in particular since we started to discuss rate cuts more clearly. In addition, wages are now rising faster than prices and unusually large tax refunds will be paid out during the spring.

In this situation, it is important that we get our communication right so that expectations of rate cuts do not overtake our decisions.

If either the krona depreciates or household demand increases rapidly simply on the expectation of an early rate cut, an early rate cut will become inappropriate. And similarly, if the reactions to a first rate cut are substantial, it will take a long time before it is appropriate to continue with further rate cuts.

A rate cut at one of the meetings in the second quarter of this year may, on the other hand, be more justified if it, at least in broad terms, is expected and priced in by the financial markets without the effects on the krona and household demand having become unjustifiably large.

First Deputy Governor Anna Breman

I support the proposal to leave the policy rate unchanged. I also support the proposed policy-rate path and the other forecasts and assessments in the draft Monetary Policy Report.

Monetary policy has contributed to lower inflationary pressures. When inflation increased sharply, we raised the policy rate rapidly and considerably. We could not prevent inflation from rising, but we could prevent it becoming entrenched at a high level, causing a wage-price spiral. Long-term inflation expectations have remained well-anchored, the social partners have shown substantial responsibility in wage setting and demand has been subdued. Inflation has fallen and is now approaching the target.

The conditions for a recovery in the Swedish economy are favourable at the same time as inflation stabilises close to the target. Swedish industry and exports continue to perform well. When inflation falls towards the target, real wages rise. In combination with lower policy rates, this helps to strengthen households' purchasing power. This will in turn contribute to decent growth and a stronger labour market in the coming years.

This forecast is based on the assumptions clearly stated in Chapter 2 of the draft report. In the forecast, the krona appreciates and the geopolitical tensions do not lead to any significant supply shocks or rising energy costs. At the same time, companies' pricing behaviour is assumed to return to historically more normal patterns. The assumptions are reasonable. I It is important, however, to bear in mind that the forecast is based on risks not materialising or alternatively that the effects of setbacks will be minor and very transitory. The risk picture is complex, partly because different risks, such as geopolitical tensions, the krona exchange rate and companies' pricing behaviour, can interact and reinforce each other.

At today's meeting, the key issue to me is how we weigh favourable conditions for low and stable inflation against a complex risk picture. How do we move towards a less restrictive monetary policy without jeopardising the favourable conditions for both inflation and the real economy?

My current assessment is that a well-balanced monetary policy is to gradually lower the policy rate, probably starting in May or June. There is considerable uncertainty about the level of the policy rate in the longer run.[1] This means that monetary policy must be characterised by a learning approach, with preparedness to adjust the policy rate as we gradually work out which rate level is compatible with normal resource utilisation and sustainably low and stable inflation.

I would like to highlight three factors that I consider important for the transmission of monetary policy and that can also provide guidance on the timing and extent of possible rate cuts: (I) the risk picture, (ii) expectations of households, companies and the market, and (iii) global financial conditions.

First, my assessment is still that the consequences of managing unexpectedly high inflation are more negative compared with unexpectedly low inflation. If the policy rate is contractionary to begin with, monetary policy can be rapidly made more expansionary if inflation falls more than expected. If instead inflation becomes higher than expected, the costs to the real economy of having to raise the policy rate further risk being considerable. This suggests the best approach is a gradual and cautious adjustment of monetary policy towards a less contractionary level. For a longer discussion of this, see the alternative scenarios in the draft report and the minutes from our previous monetary policy meeting.

Second, both the actual level of the policy rate and the expectations of future rates affect the financial conditions and the behaviour of households and companies. For low-debt households and companies, or those with large economic buffers, expectations of future rate cuts can be enough for them to venture forward and increase consumption and investment. But for high-debt households and companies, actual rate cuts are probably required to achieve the same effect. More recently, market expectations and the Riksbank's rate path have started to converge. This is essentially positive, but it is more difficult to know how the expectations of households and companies affect the Swedish economy and inflation. A further complication is that the market's expectations of the Federal Reserve have changed, which has strengthened the dollar against the krona. If this trend continues, it risks again having a negative impact on Swedish inflation.

[1] See the analysis "Structural factors determine interest rates in the longer run" in the draft report.

This brings me on to my third point. Sweden is a small, open economy that is affected by how inflationary pressures and financial conditions evolve globally. Risk sentiment in financial markets and what other central banks do, especially the Federal Reserve and the ECB, affect Swedish market rates and the krona exchange rate. A well-considered monetary policy in Sweden can, depending on the circumstances, lead to a policy rate close to those of other central banks or one that deviates from theirs.

Let me illustrate this with a brief comparison between Sweden, the euro area and Norway. The Riksbank acted before the ECB by raising the policy rate earlier. Net purchases and reinvestments of bonds were also concluded earlier than the ECB. We are also actively selling government bonds, which the ECB is not. The Riksbank's and the ECB's policy rates are now at the same level, but the ECB has hiked the policy rate more than the Riksbank as it started from a lower level. Norges Bank, on the other hand, started its rate hikes earlier than the Riksbank, and Norway now has a higher policy rate than Sweden. Both Swedish and Norwegian households have short interest-rate fixation periods, which means that consumption is affected relatively quickly by rate increases. The pass-through of the exchange rate to inflation and how wage formation works are other factors that differ between countries, but that are important for the transmission of monetary policy.

The conclusion from this brief comparison is that basically the same factors drove up inflation in the euro area, Norway and Sweden, but that the transmission of monetary policy differs. Monetary policy has therefore been similar, but not identical. The Riksbank's monetary policy will continue to be focused on achieving sustainably low and stable inflation, taking domestic economic conditions into consideration while at the same time dealing with a significant impact on Swedish inflation from abroad.

Allow me to summarise. I support an unchanged policy rate and the assessment that the policy rate can probably be cut in May or June. However, the risk of setbacks remains. Monetary policy should always be prepared to adjust to new conditions. The conditions for a stabilisation of inflation have improved. But, a smooth return to sustainably low and stable inflation should not be taken for granted.

Deputy Governor Aino Bunge

I support both the proposal to leave the policy rate unchanged at 4 per cent at this meeting, and the forecasts and assessments made in the draft Monetary Policy Report.

Developments since our previous meeting have in many ways been in line with what we foresaw at the end of January. We are approaching an easing of monetary policy and can probably cut the policy rate during the first half of this year, if the positive development in inflation prospects continues.

The background to this is that we are in a different place than we were one year ago. Inflationary pressures in Sweden are continuing to decrease, and the outcome for inflation in February was slightly lower than our most recent forecast in November. And the same applies to both the CPIF and the CPIF excluding energy. This reinforces the picture that inflation is on its way to stabilising around the target. It is also reflected in the inflation expectations of other agents in the economy (see Figure 27 in the draft report).

The Swedish economy and the labour market have shown resilience during the period of high inflation and contractionary monetary policy, but activity has now clearly slowed down. This also points to lower inflationary pressures ahead. Developments in the Swedish real economy are divided, as described in the draft report, where the slowdown has continued to be driven by the interest-sensitive parts of the economy, such as household consumption and housing investment.

Although the monetary policy we conduct at the Riksbank is independent, Sweden's economic development is very much affected by what happens abroad. We neither can, nor should, ignore this. And this includes effects of other countries' monetary policy and the exchange rate, to which I shall return. With regard to the real economy, the draft report concludes that developments are now going partly in different directions with regard to the United States and the euro area, with US growth being considerably stronger.

One thing that is clear in a comparison of the Swedish economy with other countries is that wage increases are moderate. This entails a reduced risk of inflation once again accelerating through the influence of wage growth. We noted already when the Industrial Agreement was signed last spring that the risk of a wage-price spiral had declined significantly.

However, despite the essentially bright prospects, risks remain also for Swedish inflation. One clear risk concerns the exchange rate. The Swedish krona has depreciated after a period of stronger development and it is on the whole somewhat weaker than at the time of our previous meeting. The krona exchange rate is a factor that will affect monetary policy as a result of the impact on Swedish import and consumer prices. Our forecast is based on a stronger krona going forward, but it is, as always, very uncertain.

We have seen signs that companies' pricing behaviour is on the way to normalising. However, the experiences of the upturn in inflation in 2021-2022 indicate that this is something we should monitor carefully going forward, not least with regard to prices of services. It is also an area where I want continued confirmation that things are going in the right direction before we cut the policy rate.

In a scenario where global supply shocks coincide with a weaker krona, there may be a return to a pricing behaviour where companies quickly pass on their costs to consumer prices. This could lead to unexpectedly high inflation going forward. The draft report contains an interesting analysis of the correlation between producer prices and consumer prices, which illustrates important aspects of how companies' pricing changed in an environment with sharply rising producer prices.

I would now like to go more in-depth into another uncertainty factor, namely the economic outlook in Sweden, and in particular households' saving and consumption. Swedish households are sensitive to interest rates from both a historical and international perspective. And this is due to their high degree of indebtedness, combined with the high levels of debt being mainly at a flexible interest rate. As I mentioned earlier, it is the weak consumption, together with falling housing investment, which is mainly weighing down growth in Sweden, and the weak demand makes it more difficult to raise prices. We can see from the most recent Financial Accounts for the fourth quarter of 2023 that the adjustments are large, households continue to borrow less and save more. For the first time since 1996, amortisation to banks and mortgage institutions exceeded new loans during the quarter.[2]

However, given their substantial interest-rate sensitivity, households have if anything shown a greater resilience than expected during the rise in inflation. As we have discussed at earlier meetings, this is probably linked to two factors: that the labour market has been relatively strong and that savings buffers were built up during the pandemic. Demand is now weak, as we have noted, but at the same time, household sentiment could change to a more positive direction if several factors are pointing in the same direction: interest cuts, tax refunds and a housing market that is recovering, as well as potentially more expansionary fiscal policy. This could lead to increased consumption and an increased use of savings buffers, to the extent that they still remain. But as we at the Riksbank have indicated on many occasions, the distribution of household savings is opaque as a result of the lack of statistics.

When I consider my impressions overall, my assessment is that it is well-balanced to leave the policy rate unchanged at this meeting, but that the conditions appear good for a cut in May or June. In my very first contribution at the monetary policy meeting in February last year, I discussed the new Sveriges Riksbank Act including

[2] See Households borrowed less and saved more (scb.se)

the significance of real economic considerations in monetary policy.[3] I said that that consideration for the real economy is one of the most important trade-offs we have to make at each policy rate decision. I still believe this, and there is more scope for this trade-off when the risks of a long period of too high inflation have declined, and thus also the risks of reduced confidence in the inflation target.

An important message in the Monetary Policy Report is that the adjustment of monetary policy from a contractionary level should be done with caution. In line with my earlier reasoning concerning household consumption and savings, rapid and large interest rate cuts could lead to demand increasing too strongly and causing inflation to rise again.

Part of how our decisions affect the economy, the monetary policy transmission mechanism, is the communication of the decisions and the forecasts for the future policy rate. Starting with this report, the policy-rate forecast will be shown in two different time horizons. The reason for this is to clarify the difference in how we view the decisions in the near term and those in the longer term, which are more uncertain. I think it is good that we try to make our presentations of the interest-rate forecasts easier to understand. Further ahead, monetary policy will unavoidably need to be adjusted if new shocks hit the economy. We must be clear about this towards companies and households.

A closely-related question we often get is what level should be regarded as “normal” or “neutral” for the policy rate. The draft report contains an analysis showing how structural factors determine interest rates in the longer run. The conclusion is that the factors that have driven down real interest rates globally for several decades are still dominant. However, there is considerable uncertainty over the development of various factors in the future. Even if the major trends regarding demography and so on remain, changes are now taking place that are relatively difficult to assess, such as AI, climate investments, the composition of the population and unfortunately also geopolitical risks. I completely share the assessment in the draft report that monetary policy therefore needs to be characterised by a learning approach, where we adjust the policy rate gradually and increase our knowledge of what interest-rate level is compatible with normal resource utilisation.

Governor Erik Thedéen

I support the proposal to leave the policy rate unchanged at 4 per cent, and I support the forecasts made in the draft Monetary Policy Report. Monetary policy has been contractionary for a long period of time, the inflation rate has fallen and there are many indications that inflation is now approaching the target of two per

[3] See Monetary policy minutes February 2023 (riksbank.se).

cent. We are thus approaching a situation where we can begin to make monetary policy less restrictive.

Before I go into more detail on how I view the monetary policy situation, I would like to briefly recapitulate what has happened over the past year. Around one year ago, CPIF inflation was close to 10 per cent. At that time, we had on repeated occasions been surprised by the strength of the inflation impulse and an unusually large amount of companies in the retail trade sector were planning price increases in the immediate future. The level of activity in the economy was relatively high, particularly during the first half of the year. On the foreign exchange market, the krona exchange rate depreciated, which risked creating new inflationary impulses. We were worried that a change in pricing behaviour among companies would make the work on bringing inflation back down to the target more difficult.

In this situation, there were strong reasons to move monetary policy in a more contractionary direction. The policy rate was raised last year in stages from 2.5 to 4 per cent, before we decided in November 2023 to leave the policy rate unchanged. Inflation was then still high, but inflationary pressures looked better. During December last year and January this year, inflation prospects continued to improve. At our previous monetary policy meeting, we assessed that we were on firmer ground, that the interest rate had probably peaked, and that there was a possibility that the interest rate could be cut during the first half of this year.

It is now clear that the tighter monetary policy has contributed to dampening activity in the Swedish economy, from high levels. The lower demand has made it more difficult for companies to pass on higher costs to their customers. At the same time, the rate of price increases at the producer stage has slowed down. This indicates that the effects of the supply shocks, that were an important cause of the global upturn in inflation, have abated. These changes combined have contributed to CPIF inflation falling back and to companies' pricing plans now seeming to be compatible with the inflation target. The more short-term inflation dynamic, measured as 1-, 3- and 6-month changes annualised, shows that inflation is well on the way towards 2 per cent. It is also positive for the inflation outlook that the social partners have agreed via the so-called benchmark on wage increases for 2023 and 2024 that are at a balanced level. This means that wage growth in Sweden poses a lower risk for inflation than in many other comparable countries.

As usual, there is a considerable measure of uncertainty in the growth and inflation prospects, and this needs to be taken into account when formulating monetary policy. For example, there is reason to closely monitor developments in services prices, where the rate of increase is still somewhat elevated. At present, however, most of the risks concern developments abroad. Perhaps the risks that are most difficult to assess have to do with geopolitical tension, with wars in

Europe and the Middle East. These conflicts can lead to new shocks, for instance, in supply chains and in energy and food prices. Given the worsening geopolitical situation, it is not possible to rule out relatively severe supply shocks, or other more general effects on the Swedish and global economies as a result of the geopolitical risks.

Other risks concern more normal uncertainty regarding economic developments abroad. The US economy has, for instance, been surprisingly strong over the past year, which is visible in a large upward revision in our forecast for expected growth in 2024, from 1.2 to 2.3 per cent. The market is still counting on the Federal Reserve cutting its policy rate this year, although the possible timing has been postponed. Stronger growth in the United States could lead to higher inflationary pressures both there and globally, and this could lead to new inflationary impulses in Sweden, too. The market is also expecting that the ECB will cut its policy rate this year, beginning around the summer. For our part, an important question is how the major central banks' policy rate changes will affect the Swedish krona. Higher interest rate abroad could weaken the krona. We therefore need to continue to closely monitor the development of the krona as leading central banks begin to ease their monetary policy. But we should not link Swedish monetary policy directly to other central banks' actions. It is the inflationary pressures and the prospects for inflation here in Sweden that determine our monetary policy.

At our previous monetary policy meeting, I said that there were clear signs that we could be on the way into a new monetary policy phase, where it would gradually be possible to ease monetary policy. Now I see several signs that we are really in a new phase. As I have already mentioned, the inflation dynamic has continued to develop in line with the inflation target and our inflation forecasts have become more accurate.

In this regard, we are now on firmer ground. This makes it easier to comment on the forecast for the policy rate. Previously, when developments in inflation were volatile and difficult to predict, my main focus was on following incoming data and formulating monetary policy with this as a starting point. Incoming data is of course always important, but now that the development of inflation appears more stable, I am prepared to look further ahead when monetary policy is formulated. Figure 1 in the draft report contains an interest rate path that extends over the three coming quarters. I think it provides a good summary of how monetary policy may look during the remainder of the year, given there are no unforeseen events.

According to the figure, the policy rate can begin to be cut cautiously with effect from May or June. My assessment at present is that there is some probability of a cut in May, on condition that inflation prospects, including the development of the krona, do not deteriorate significantly. One reason to potentially begin cutting the rate in May is that we would then have greater flexibility to proceed cautiously with further adjustments to the interest rate. Cautious and gradual cuts in the policy rate in line with the interest-rate path would give us time to regularly evaluate how our measures affect economic activity and inflation prospects. Such a strategy would also make it possible to gradually adapt the pace of the cuts, if it were shown that inflationary pressure abate more slowly or more quickly than in our current assessment. We can then pause the cuts and slow down an overly rapid upturn in economic activity if this is necessary. And vice versa, we would also have the possibility to increase the pace of the cuts, if there is reason to do so.

A significant uncertainty factor when we begin to cut the interest rate concerns how the economy will react. We know, for instance, that rate increases have affected the interest-rate sensitive parts of the economy, such as housing construction, a sector where unemployment has risen significantly. But in other parts of the business sector, such as the export industry, activity is still relatively good. And the labour market has in total only weakened slightly and may be considered relatively strong, given the higher prices and interest rates. Given the relatively good situation on the labour market, for instance, there is a not insignificant risk that the economy will react more strongly to interest-rate cuts than we are assuming in our forecasts. This could lead to a larger upturn in demand, which could have a negative effect on the development of inflation. Moreover, this risk could be greater in Sweden than in many other countries, given households' high debts that are also mostly at variable interest rates. This uncertainty indicates that cautious, gradual interest-rate easing would be a good idea and would give us the opportunity to closely follow and analyse how the economy reacts to lower interest rates. It improves the conditions for attaining stable economic developments with inflation in line with our target of 2 per cent.

To summarise, inflation prospects are improving and the risk of inflation becoming entrenched at levels that are too high has declined. We are therefore approaching a situation where the need to conduct a contractionary monetary policy is declining. However, there are still risks of setbacks, and it is important that the krona does not continue to depreciate from its current levels, as this could lead to increased inflationary impulses.

§4. Monetary policy decisions

The Executive Board decided

- on monetary policy measures in accordance with the provisions of the draft Annex A to the minutes, Policy-rate decision. The Riksbank sets the policy rate at 4 per cent, which means that it is held unchanged,
- to establish the Monetary Policy Report according to the proposal, Annex B to the minutes Monetary Policy Report,
- to publish the monetary policy decision with the reasons for it in a press release at 09.30 on Wednesday 27 March 2024,
- to publish the minutes from today's meeting at 09.30 on Thursday 4 April 2024.

This paragraph was confirmed immediately.

Minutes taken by

Hans Dellmo Dominika Krygier

Verified by

Erik Thedéen Anna Breman Per Jansson

Martin Flodén Aino Bunge

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