Monetary policy and the inflation target – the importance of clarity and openness

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Today's presentation

• Current monetary policy
  • July decision
  • Brief summary of events during the summer

• The importance of clarity and transparency in monetary policy
  • Our experiences of publishing our own repo-rate forecasts
  • The CPIF as a formal target variable and illustration with a variation band
Current monetary policy
Strong Swedish economic activity

Good GDP growth

Unemployment has fallen

Note. Annual percentage change and percentage of labour force, 15–74 years. GDP measured using calendar-adjusted data.

Sources: Statistics Sweden and the Riksbank
Krona important for the development of inflation

Note. Index, 28 Nov 1992 = 100. The KIX is an aggregate of countries that are important for Sweden's international transactions. Outcomes refer to daily data up to and including 30 June 2017.

Sources: National sources and the Riksbank
Continued expansionary monetary policy needed to stabilise inflation around 2 per cent

Note. Annual percentage change. The CPIF is the CPI with a fixed interest rate.

Sources: Statistics Sweden and the Riksbank
Monetary policy supporting economic activity and inflation

Repo rate unchanged at -0.50 per cent

Purchases of government bonds during the second half of the year

Note. Per cent and SEK billion respectively.

Source: The Riksbank
Low interest rates needed – but important to have measures aimed at housing market

• Household high and rising debt
  – a risk to the national economy

• Measures needed in the housing market, taxation policy and macroprudential policy

• Finansinspektionen’s proposal for tougher amortisation requirement a welcome step
Developments during the summer

Unexpectedly strong GDP growth in the second quarter

Higher inflation than expected in June and July

Note. Annual percentage change GDP measured using calendar-adjusted data. The CPIF is the CPI with a fixed interest rate. Squares refer to new outcomes after the report was published.

Sources: Statistics Sweden and the Riksbank
The importance of clarity and transparency in monetary policy
Our experiences of publishing our own repo-rate forecasts
Several reasons why we began publishing our own repo-rate forecast in 2007

• Facilitates communication concerning monetary policy

• Previous repo-rate assumptions entailed problems for the forecasting work

• Can influence market expectations
Good experiences

• Has given the general public greater insight into monetary policy and better possibilities for evaluation and accountability.

• Has improved the internal analysis work, partly through increased use of alternative scenarios

• The cooperation between the Executive Board and the staff has deepened in that the forecasts and monetary policy are now more closely linked
But there have also been challenges

• Periodically, there have been major differences between the repo-rate path and forward rates

• The accuracy of the repo-rate forecasts
Both the Riksbank and others have overestimated the future level of the repo rate

Global trend towards lower real interest rates

Financial crisis and sovereign debt crisis led to large policy rate cuts

Note. Per cent. Real yields refer to 10-year real government bonds. The ECB’s policy rate refers to the deposit rate.

Sources: Bank of England, ECB, Federal Reserve, Thomson Reuters and the Riksbank
Lessons for the future

• Accuracy of the repo-rate forecasts
  • We need, for instance, to develop the analysis of changes in long-term interest rates

• Communication of monetary policy
  • Actual changes in the interest rate compared with changes in the forecasts for the interest rate
The CPIF as a formal target variable and illustration with a variation band
The CPI is influenced by the repo rate in the short term in the “wrong direction” – a challenge for communication

Note. Repo rate in per cent and the CPI expressed as an annual percentage change.

Sources: Statistics Sweden and the Riksbank
The CPI and the CPIF – what is the difference?

• **Interest expenses** = **capital stock** * **interest rate**

• Capital stock ≈ the value of the home when purchased (sluggish series)

• **Interest rate** = mortgage rate; influenced to a large degree by the repo rate

• In the CPIF, the mortgage-rate index is constant

Sources: Statistics Sweden and the Riksbank
To attain clearer monetary policy – CPIF as formal target variable

Note. Annual percentage change. The CPIF is the CPI with a fixed mortgage rate.

Source: Statistics Sweden
Variation band illustrates uncertainty

- To illustrate uncertainty
- Based on historical developments
- Not a ‘target range’ – monetary policy aims at 2 per cent regardless of whether inflation is inside or outside the band

Note. Annual percentage change. The CPIF is the CPI with a fixed interest rate.
Source: Statistics Sweden and the Riksbank
Work during the autumn

• The commission of inquiry on a new Sveriges Riksbank Act continues

• Important to have measures on the housing market – Finansinspektionen’s amortisation requirements being processed

• Next monetary policy meeting on 6 September