Monetary policy minutes

September 2019

SVERIGES RIKSBANK

Summary

At the Monetary Policy Meeting on 4 September 2019, the Executive Board of the Riksbank decided to leave the repo rate unchanged at –0.25 per cent. As previously, the forecast for the repo rate indicates that the rate will be increased towards the end of the year or at the beginning of next year. However, low interest rates abroad and worsened sentiment mean that the repo rate is thereafter expected to be increased at a slower pace compared with the assessment in July.

The board members supported the picture of the economic outlook and inflation prospects described in the draft Monetary Policy Report. After several years of high growth, the Swedish economy has entered a calmer phase, something that has been included in the Riksbank's forecasts for some time. Resource utilisation is softening but is still higher than normal and inflation has been close to the inflation target of 2 per cent since the beginning of 2017. According to some measures, long-term inflation expectations have fallen somewhat this year, but the overall picture is that they are close to 2 per cent. The development of inflation has been approximately in line with the Riksbank's forecasts and, in the current situation, this argues in favour of keeping to the previously communicated direction of monetary policy for the next six months.

Even though the real economy and inflation abroad have largely developed as expected, the board members stressed that sentiment has worsened and that the risk of a faster slowdown has increased. This is partly linked to the ongoing trade conflict between the United States and China and uncertainty surrounding the United Kingdom's withdrawal from the EU. Several members pointed out that market rates have fallen significantly during the year and that expectations of monetary policy have become increasingly more expansionary. Several central banks have also cut their policy rates or communicated that monetary policy may be made more expansionary. Market pricing indicates that market participants expect powerful monetary policy stimulation measures.

Increased unease in the global economy and interest rates that are expected to be low for a longer time mean that, in the members' assessment, the repo rate needs to be raised at a slower pace in the period ahead, compared with the assessment in July.

All the members supported the forecast for the repo rate. One member expressed doubt about the forecast that the rate will be increased towards the end of the year or at the beginning of next year but, despite this, did not enter a reservation against the repo rate path. Several members emphasised that even though the Riksbank cannot act independently of global developments, in many respects Sweden is in a more favourable situation compared with other countries, with continued reasonably strong economic activity and inflation that has been close to target for some time. The Riksbank therefore has slightly greater degrees of freedom than previously to deviate from monetary policy abroad. A few

members highlighted developments on the housing market and the risks associated with the high level of household indebtedness, which constitutes a vulnerability for the Swedish economy.

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MINUTES OF MONETARY POLICY MEETING
Executive Board, No. 4

DATE: 4 September 2019

TIME: 09.00

PRESENT: Stefan Ingves, Chairman
Kerstin af Jochnick
Martin Flodén
Per Jansson
Henry Ohlsson
Cecilia Skingsley

Susanne Eberstein, Chairperson, General Council of the Riksbank
Michael Lundholm, Deputy Chairperson, General Council of the Riksbank

Meredith Beechey Österholm
Vesna Corbo
Charlotta Edler
Mattias Erlandsson
Eric Frieberg
Pia Fromlet
Anders Gånge
Jesper Hansson
Jens Iversen
Kristian Jönsson
Maria Kindborg
Henrik Lundvall
Ann-Leena Mikiver
Carl-Fredrik Pettersson (§ 1-3A)
Åsa Olli Segendorf
Maria Sjödin
Ulf Söderström
Anders Vredin
Fredrik Wallin (§ 1-3A)
Ingrid Wallin Johansson (§ 1-3A)
Gary Watson

John Rwangombwa, Governor – National Bank of Rwanda
Thomas Kigabo, Chief Economist – National Bank of Rwanda

It was noted that Pia Fromlet and Henrik Lundvall would prepare the draft minutes of the monetary policy meeting.

§3a. Economic developments

Market developments since the last monetary policy meeting

Ingrid Wallin Johansson of the Markets Department began by presenting the latest developments on the financial markets. It has been an eventful summer on the financial markets. Geopolitical risks, risks of a global economic slowdown and expectation of significantly more monetary policy stimulation in many countries have continued to affect developments on the financial markets since the monetary policy meeting in July. It was also noted that the turbulence surrounding the United Kingdom's EU withdrawal has increased since July, but that the direct effect has primarily been on assets linked to the United Kingdom, such as the British pound. At the same time, the political situation in Italy, with the imminent formation of a government, has resulted in lower yield differentials between Italy and Germany.

Despite market turbulence, equity prices and yield differentials between corporate bonds and government bonds have not demonstrated any clear trend of late. Although volatility on the equity markets has been higher in August compared with immediately previous months, the upturn has not been dramatic. At the same time, downturns in equity indices have been rather limited. Neither have yield differentials between corporate bonds and government bonds noted any major change during the summer. Stability on the market can probably be linked to expectations that central banks will continue to support economic activity with more monetary policy stimulation. In addition, there are signs that investors are turning to riskier assets in an environment where returns on safer assets are low.

On the fixed-income market, there are more worrying signals, however. The fall in market rates has accelerated during the summer. Government bond yields with long maturities have fallen to their lowest ever levels in many countries. Yields on Swedish government bonds have periodically been below zero for all maturities. It has also been highlighted that the US yield curve for government bonds is inverted between two and ten years' maturity, something that has been interpreted as a signal of a greater risk of recession.

The worsened risk outlook has also led to an increase in the demand for safe assets such as gold, which has driven up the gold price to its highest level in six years. Currencies that are seen as particularly safe in times of unease, such as the Swiss franc, the Japanese yen and the US dollar, have strengthened. The Swedish krona has weakened since the July meeting and is currently close to its weakest levels since the financial crisis.

For a number of months, the market has been expecting more monetary policy stimulation globally. This has begun to materialise during the summer. The US Federal Reserve cut its policy rate by 0.25 percentage points in July and the market is expecting several more cuts this year and next year. The European Central Bank (ECB) is also expected to implement more expansionary measures in September, for example lower policy rates, the resumption of bond purchases and tiered deposit rates at the central bank.

Prior to this monetary policy meeting, market participants' expectations are that the repo rate will be left unchanged and that the repo rate path will be lowered. The market does not believe the repo rate will be increased in Sweden this year or next year, but instead, forward pricing indicates a high likelihood of cuts during next year. The majority of forecasts from analysts indicate an unchanged repo rate up until the end of 2020.

The current monetary policy drafting process – new data and forecasts

Jesper Hansson, Head of the Monetary Policy Department, began by presenting the forecast that the Monetary Policy Department judged would gain the support of a majority of the Executive Board. The monetary policy drafting process has included discussions with the Executive Board regarding the forecasts and the monetary policy assumptions at meetings on 19, 20, 23 and 26 August. The draft Monetary Policy Report was discussed and tabled at a meeting of the Executive Board on 28 August.

Two issues have been discussed in particular detail during the drafting process. The first is the downturn in sentiment among companies and households that has taken place in many countries and the associated uncertainty about the economic outlook abroad. Although several large economies have grown during the first half of this year at a pace that is approximately in line with previous forecasts, confidence among purchasing managers in the United States and among companies in the euro area has fallen substantially over the past year. One cause of the downturn is probably the unease surrounding the ongoing trade conflicts, and the potential risks of these escalating.

The levels of confidence that have now been recorded, and that are below a historical mean value, indicate that growth abroad will be slightly lower than normal in the period ahead. However, Jesper Hansson pointed out that this type of measurement is not a good indicator of longer-term growth. But he also emphasised that how sentiment develops in the period ahead must be closely followed and that any further, significant downturns in key confidence indicators are not compatible with the international forecast described in the draft Monetary Policy Report.

The other issue that has received particular attention during the drafting process is the falling interest rates abroad and in Sweden. Quite a large number of central banks abroad have announced that monetary policy going forward will become more expansionary and decisions on lower policy rates have already been taken in several countries. Government bond yields have also fallen around the world and expectations of future policy rates among investors have been adjusted down significantly. Weaker economic signals, a poorer risk picture and falling inflation expectations are factors that have probably contributed to this development.

The worsened sentiment and lower yields have led to revisions to the proposed forecast in the draft Monetary Policy Report. Growth in the United States and the euro area in the coming quarters is now expected to be somewhat lower compared with the forecast in the Monetary Policy Report in July. However, in the longer term, no revisions have been made to trade-weighted growth abroad. A contributory factor to this is that the weighted average of international policy rates has been written down by between 0.20 and 0.35 percentage points in the years to come, according to the proposed forecast.

Economic activity in Sweden is still considered strong, although it has softened slightly over the past year. Unemployment has previously fallen over many years but recently this development has come to a halt, and in July, seasonally adjusted unemployment rose to 7.1 per cent. However, this comparatively high level is deemed temporary and according to the proposed forecast, unemployment is expected to rise weakly from 6.3 per cent in 2018 to just below 7 per cent in mid-2022.

GDP growth was slightly lower than expected during the second quarter and investments developed weakly. The National Institute of Economic Research's Economic Tendency Indicator has fallen and is now at a level that is slightly lower than the historical average. In the proposed forecast, GDP growth for 2019 is revised down to 1.5 per cent from 1.8 per cent in the July forecast. According to Jesper Hansson's assessment, there is currently no reason to believe that further large falls in confidence among Swedish households and companies will take place. However, even here, there is reason to follow developments closely; the current proposed forecast is based on sentiment stabilising in the period ahead.

Recently, CPIF inflation has fallen slightly, in line with the Riksbank's earlier forecast. In July, annual price growth was 1.5 per cent, but different measures of underlying inflation are closer to 2 per cent. Prices of fuel and electricity are helping to push down CPIF inflation and in September, price growth is expected to fall further. However, according to the proposed forecast, inflation will be higher again towards the end of the year and will be close to 2 per cent in the coming years. High recorded pricing plans among companies in the wholesale and retail sectors and previous depreciations of the krona exchange rate were stated in support of this assessment. In the longer term, slightly higher wage growth is also expected to contribute to higher cost pressures.

In conclusion, Jesper Hansson emphasised that the draft forecast presented is based on the monetary policy that is expected to gain a majority at today's monetary policy meeting. The assumption is that the repo rate is today left unchanged at –0.25 per cent and that the repo rate path indicates a rise at the end of this year or at the beginning of next year. The proposal for the repo rate path implies that the rate will thereafter be raised at a slower pace compared with the forecast in the Monetary Policy Report from July. The most important reasons for this are the worsened sentiment, uncertainty about future economic developments and lower interest rates abroad. Furthermore, the proposed forecast for the economic outlook and inflation prospects is based on the decision taken by the Executive Board in April, according to which the Riksbank will purchase government bonds for a total nominal amount of SEK 45 billion from July 2019 until December 2020.

§3b. The economic situation and monetary policy

Deputy Governor Cecilia Skingsley:

I support the assessments made in the draft Monetary Policy Report, to leave the repo rate unchanged at –0.25 per cent, and the proposed forecast for the repo rate path. In addition, I will make some comments on the international economy, the development of the financial markets and the Swedish economy in those respects that have had the greatest significance for my standpoints.

Both the international and the Swedish economy have entered a calmer growth phase, a development that the Riksbank has been forecasting for some time.

Since the last meeting, the real economy and inflation have developed approximately as expected but sentiment in the form of optimism measured among companies and households has deteriorated, both abroad and in Sweden.

In the business sectors of Sweden's most important trading partners, it is clear that a downward shift is occurring in the manufacturing sector, largely due to the escalated trade conflicts between China and the United States. The increasing risk that the United Kingdom's withdrawal from the EU will take place without an agreement is also weighing down the manufacturing sector abroad. At the same time, it must be borne in mind that activity in the service sector has been relatively unaffected so far. Similar patterns can be found in Swedish surveys.

The financial markets are seeing a tug-of-war between unease over the rising negative effects of the trade conflict between the United States and China on one hand and the more expansionary monetary policies communicated by most central banks on the other.

Pricing on the financial markets indicates that market participants expect a significant deterioration of global economic activity and that the response from central banks, particularly in the United States, will be powerful. These expectations are illustrated in Figure 2:1 in the draft Monetary Policy Report. Judging from previous communication and market expectations, some easing can also be expected from the ECB. In my view, market rates in most countries have fallen to an extent that has not been fully reflected by actual economic developments. This view is supported by the downward revision of economic analysts' forecasts in general, albeit not to an extent that could justify the current extremely low interest rates. My interpretation of recent developments on the fixed-income market is that they partly reflect a weakened economic outlook and partly reflect out a negative scenario for surprisingly weak growth. Such a negative scenario would be driven by the trade conflicts and could be exacerbated by global difficulties in reaching agreement on suitable stabilisation measures.

As regards economic activity in Sweden, resource utilisation continues to be higher than normal. Inflation has been near the target of 2 per cent since the start of 2017, which is to say over two years. Since the assessment in July, two outcomes for inflation have been received, which have both been in line with the Riksbank's forecast. Due to lower growth in energy prices, CPIF inflation has fallen and was recorded at 1.5 per cent in July. This was slightly higher than the Riksbank's previous forecast, published at the start of July. The expected downturn, which according to today's forecast will bottom out at 1.3 per cent in September, thereby remaining within the variation band, will not be a problem for monetary policy to deal with, in my opinion. This is because inflation expectations in Sweden are so well anchored that economic agents can be expected to disregard the downturn. Furthermore, the Riksbank's various measures of core inflation indicate that inflationary pressures will stay close to the target of 2 per cent.

However, the identification of an appropriate monetary policy is being complicated by a fairly contradictory picture. The economy is currently favourable in large parts of the world, including Sweden. With inflation close to target, well-anchored inflation expectations and resource utilisation above its normal level, it seems reasonable to continue with gradual rate rises in Sweden, in line with the previous forecast. However, considering the economic outlook and risk outlook, the forecast of future rate rises needs to be adjusted.

Further monetary policy stimulation abroad and low interest rates for a longer time to come form a precondition for the global growth sequence to be able to develop approximately as the Riksbank predicts. For me, it therefore seems reasonable to adjust the repo rate path to reflect a slower pace for future rate rises.

Inflation far below the target of 2 per cent and inflation expectations a good bit below the inflation target would have provided strong reasons to quickly readjust policy and signal an unchanged repo rate for longer or even repo rate cuts. However, this is not the case, so I consider that today's adjustment of the future repo rate is sufficient, and gives us the flexibility to follow the extent to which various risk factors materialise. Swedish monetary policy is not facing the same challenges as the euro area, where inflation expectations according to market-based measures have long been low and have started to fall, and where the monetary policy transmission mechanism needs to be supported in the form of liquidity measures to the banking system.

I expect that today's repo rate decision, when it is published, will be discussed, as it always is. However, reactions may be particularly strong this time, as most analysts have come to expect that there will not be any rate rises for at least the next year. At the same time, differences of opinion are large between different kinds of analyst. Banks and investors expect an unchanged policy rate in the near term and rises later in the forecast period, while prices on the fixed-income market indicate a high probability of cuts. The situation is therefore hard to assess.

With today's decision, I consider that the Riksbank is using the flexibility that comes with target fulfilment for inflation and well-anchored expectations.

To sum up my contribution, economic activity is moving, as expected, into a calmer phase. Inflation is close to target. Consequently, it seems reasonable to maintain the current direction for monetary policy over the next six months and to raise the repo rate towards the end of the year or at the start of next year. However, at the same time, I have the impression that developments abroad will be contingent on a more expansionary monetary policy over a longer period, to which Swedish monetary policy will also need to adjust to some extent.

Deputy Governor Per Jansson:

Since the monetary policy meeting in July, two new outcomes for inflation and inflation expectations have been published. The inflation outcomes refer to June and July. Just as in April and May, the outcomes were close to the Riksbank's forecast. CPIF inflation excluding energy prices, which can be seen as a measure of the longer-term trend, or underlying, inflation rate, was 1.7 per cent in July, which was a slight decline compared with June, when it was just below 1.9 per cent. Including energy prices, the June and July outcomes were 1.7 and 1.5 per cent respectively. Since June, the difference between CPIF inflation with and without energy prices has been negative, which has to do with energy prices contributing less to price development and more underlying inflation gradually rising.

That there is an upward trend in price increases is visible not only in CPIF inflation excluding energy prices but also in the Riksbank's other measures of underlying inflation. So far this year, the average for the median value of the Riksbank's various measures of underlying inflation has been just below 1.9 per cent, compared to 1.6 per cent last year. In July, the median value amounted to 1.8 per cent. The two measures that have been shown in an empirical evaluation to be best at predicting future CPIF inflation, UND24 and CPIFPC, were at 1.8 and 2 per cent respectively in July.[1]

The new outcomes for inflation expectations, as measured in Prospera's monthly and quarterly surveys, consist of the monthly surveys for money market participants in July and August. Here, there are unfortunately some elements that cause concern. The fact that more short-term expectations are falling somewhat is perhaps not so surprising bearing in mind that these tend to closely follow the current development of inflation, which is now weakening. But the fact that five-year inflation expectations have also begun to turn downwards is more worrying. For money market participants, five-year expectations have followed a weak downward trend during the year, with successively greater declines in recent months. Although the figure in August of just over 1.8 per cent is still reasonably close to the inflation target, the tendency of development is not good and means that further downturns can be feared going forward.[2]

Since the monetary policy meeting in July, no new survey of labour market organisations' inflation expectations has been conducted. The latest survey, which is from June, reported five-year expectations at, or just over, 2 per cent for both employers' and employees' organisations. Since it is very important that the labour market organisations make their forthcoming wage bargaining rounds conditional on the Riksbank meeting its inflation target, there is in this situation, as I see it, no room for any substantial decreases in these expectations. The continued development of inflation expectations, and above all of the labour market organisations' more long-term expectations, will play a major role in my monetary policy considerations in the period ahead.

The summary I make of the developments in inflation and inflation expectations since our meeting in July gives a current inflation picture that is still reasonably encouraging albeit not without problems. But it is worth emphasising that the concerns about inflation expectations are, despite everything, not comparable with those that existed at the end of 2014 and the beginning of 2015. Then, the downturn in long-term expectations was greater, inflation had been well

[1] See the article "Why measures of core inflation?" in Monetary Policy Report, October 2018.

[2] I am focusing here on the expectations for CPI inflation rather than for CPIF inflation, as the response rate for CPIF inflation is very low.

below the inflation target for several years and it was difficult to understand the reasons for the major deviations from the target. Now, inflation has instead been in line with the target for about two and a half years and the recent slide is temporary and has been shaping our forecasts for quite some time. This does not mean we can sound the all-clear as regards the development of inflation expectations. And from what I am saying here, it should also be evident that I am definitely not doing this. But neither is there, in this situation, any reason for immediate panic. The important thing is to follow developments closely and, as I just touched upon, be prepared to act decisively should more serious confidence problems arise.

With this, I now move on to discuss the forecast for inflation. All in all, compared with the Monetary Policy Report in July, the forecast revisions proposed in the draft Monetary Policy Report are minor. This is true of both CPIF inflation and CPIF inflation excluding energy prices. However, it is important to note that the forecasts are now based on an assumption of a lower repo rate than previously. The proposal in the draft report is to adjust down the repo rate path by 0.15 percentage points at the end of 2020, by just under 0.40 percentage points at the end of 2021 and by about 0.50 percentage points at the end of the forecast period. In the short term, however, up until summer next year, the rate path is more or less unchanged. That a more expansionary monetary policy is now required to attain basically the same inflation prospects has to do with a clear deterioration in sentiment, above all in other parts of the world but also to a certain extent in Sweden, which without further stimuli would have led to weaker economic developments. I support the macro forecast in the draft Monetary Policy Report.

I see the proposal in the draft report to lower the repo rate path quite substantially as the right thing to do in the current setting. But in the short term, where the rate path is largely unchanged, the starting point is still that another rate rise could be implemented, towards the end of the year or at the beginning of next year. I have significantly more difficulty with this assumption.

Certainly, our forecasts indicate that it should be fully possible to squeeze in such an increase, inflation is, after all, expected to be in line with the inflation target in the years ahead. But in the near term, inflation is nevertheless expected to remain quite clearly below the target – the average for CPIF inflation during the rest of 2019 is just under 1.6 per cent and during 2020 about 1.7 per cent – and it is hardly the case that there are any particularly worrying upside risks requiring us now to feel stressed. Looking at the inflation forecast, it would have been just as reasonable to refrain from a repo rate rise around the turn of the year and, if the prospects hold up and there is no desire to change the size of the overall rate increase during the forecast period, instead focus on increasing the interest rate a little more later on. Bearing in mind the rapid deterioration in sentiment and in the risk outlook that has occurred since July, I think that such a monetary policy plan is in fact more appealing for a small, trade-dependent economy like Sweden.

One aspect to consider in this context is what the consequences will be of both the Federal Reserve and the ECB increasing their monetary policy stimuli while we in Sweden, if the announced rate increase is implemented, proceed in the opposite direction. I share the opinion expressed by some members of the Executive Board that there are now more degrees of freedom in Swedish monetary policy than previously and that we do not have to follow what the Federal Reserve and the ECB do “on a 1:1 basis”, as I think Stefan put it. But that the Riksbank and the world’s leading central banks are more or less simultaneously changing their monetary policies in completely opposite directions is nevertheless unusual and deserves some reflection and preparedness that it may lead to something which we have not really expected. Of course, one of the questions that will ultimately arise here is how this may affect the Swedish exchange rate.

Despite these problems and concerns, I choose today not to formally enter a reservation against the monetary policy in the draft Monetary Policy Report. That I am not doing so has to do with the facts that the increase of the repo rate has not yet been decided, but is merely a forecast of how we think we will act in a few months’ time, and that I think that the repo rate path otherwise is reasonable.

The new assessment of the repo rate at the end of the forecast period, on average just below 0.4 per cent during the third quarter of 2022, means that the aggregate revision of the policy rate forecasts for Sweden and abroad[3] since April is basically of the same size. The rate path implies a cautiously rising rate during the years to come, with on average just under one rate increase per year once we have reached 0 per cent. If the rise towards the end of the year or at the beginning of next year is not implemented but the end-point for the path is nevertheless still the same, the conclusion is that the rate is instead expected to be increased by on average just over one rise per year. I consider this to be a reasonable plan for monetary policy in the current situation.

Deputy Governor Martin Flodén:

I support the proposal to hold the repo rate unchanged today, the proposed forecast for the appropriate development of the repo rate in the period ahead and the other forecasts and assessments in the draft Monetary Policy Report.

[3] This refers to the KIX-weighted rate for other countries, that is, the weighted policy rate forecasts for the euro area, the United States, Norway and the United Kingdom.

Since our monetary policy meeting in July, the real economy and inflation abroad have developed approximately in line with the Riksbank's forecast. At the same time, however, the trade conflict between the United States and China has escalated, the risk that the United Kingdom will leave the EU with no withdrawal agreement in place has increased and several international confidence indicators have weakened. International sentiment has clearly deteriorated, inflation expectations have fallen in several countries and expectations of monetary policy have become increasingly expansionary. Market rates have continued to fall and are now much lower than they were one year ago.

In Sweden, GDP growth for the second quarter, according to preliminary calculations, was slightly weaker than in our forecast and the development of unemployment over the summer has also been weaker than expected. On the other hand, inflation has been slightly higher than our forecast. Market rates have continued to fall also in Sweden.

I would like to start by making a few general comments on the economic situation abroad and in Sweden.

First, it is important to point out that weaker economic activity does not necessarily mean that the economy will enter a recession. In Sweden, resource utilisation remains high. The employment rate has increased faster than our forecasts for a number of years and is now very high. There is still a shortage of labour and high vacancy rates in many sectors. Construction is also expected to remain higher than a historical average in the years ahead, despite the slowdown from the peak year of 2017. In our forecast, Swedish resource utilisation remains higher than normal over the next few years.

Second, the signs of falling inflation expectations are, of course, worrying. This applies in particular to the euro area, where inflationary pressures remain problematically weak. The ECB has signalled that further monetary policy stimulation measures can be expected over the autumn. All the indications are, therefore, that international interest rates will remain very low in the period ahead. In Sweden, confidence in the inflation target seems to be a bit stronger and, additionally, the Riksbank's various measures of core inflation show that inflationary pressures have risen in recent years. Swedish monetary policy needs to be formulated with respect to the ever-lower international level of interest rates. However, the inflation problems are no longer as large in Sweden as in the euro area and we do not need to follow every step taken by the ECB.

Third, I consider that planning for a weaker development of inflation should not be the same as planning for weaker economic activity. The Riksbank is responsible for price stability and ensuring confidence in the inflation target. In the event of an economic downturn, however, both an expansionary fiscal policy and an expansionary monetary policy will be needed. Monetary policy still has powerful tools to manage the different market failures that could arise in a recession. However, from today's levels of interest rates, lending and exchange rates, the general economic stimulus from monetary policy could hardly get any stronger.

Fourth, the downturn in both short and long-term market rates has been remarkably large over the last year. It is true that the central banks have simultaneously communicated that monetary policy will become more expansionary than they had previously planned and, in addition, several have cut their policy rates in recent months, but not in a way that corresponds to the changed market pricing. On one hand, the aggressive market pricing means that the financial conditions have become more expansionary, which contributes towards stabilising international economic activity as sentiment deteriorates. On the other hand, there will be increased uncertainty over the development of the economy until the tensions between market pricing and central bank communication are resolved.

Finally, and related to the previous point, it is not only the policy rate the Riksbank sets and the repo rate forecast the Riksbank presents that determine how expansionary monetary policy becomes. The impact on market rates and exchange rates also depends on how credible the Riksbank's communication is and how the market's expectations of future monetary policy develop. Over the year, interest rates have fallen sharply. Pricing on the fixed-income market indicates that a significantly more expansionary monetary policy is expected compared to what has been communicated by the Riksbank. The yield on 10-year government bonds is record low and the yield on shorter government bonds is currently lower than it was a year ago, even though the repo rate has been raised since then. Market pricing now indicates the expectation that the Riksbank will cut, rather than raise, the repo rate over the winter. It is also difficult to reconcile the depreciation of the exchange rate over the last year with how the monetary policy implemented and communicated by the Riksbank relates to monetary policies abroad. During this period, the Riksbank has raised its policy rate once and has signalled that one or a few further increases can be expected, while many other central banks have cut their policy rates and/or indicated that further cuts may lie ahead.

Against the background of these comments, allow me now to discuss some alternatives for our monetary policy.

Shouldn't we start planning for a rate cut instead of holding fast to the plans for a rate rise in the near future? After all, economic activity is now becoming weaker, at the same time as the downside risks are still dominant for inflation and inflation expectations. I consider the arguments against such a monetary policy to be strong. Resource utilisation is still fairly high. Although we expect a slowdown in economic activity, we do not see a recession ahead. In addition, we must ask what we would achieve by cutting the policy rate. When the policy rate is already –0.25 per cent, the impact on lending rates would probably be limited. The dominant effect would instead be a weakening of the exchange rate. However, the krona is already weak. A further depreciation of the krona would lead to unnecessary volatility and uncertainty over the development of the exchange rate and, ultimately, the entire Swedish economy. Such a depreciation of the krona would therefore hardly support economic activity. Neither would it be a sustainable or desirable way of living up to the inflation target. I would consider cutting the repo rate from today's level only if the exchange rate starts to become overvalued at the same time as the inflation development becomes too weak.

Shouldn't we at least adjust the repo rate path to communicate that the next repo rate rise will come a few quarters later than we had previously planned? This alternative does not appeal to me either. Our forecasts indicate slightly calmer Swedish and international growth in the next few years. Nothing today indicates that a rate rise in, for example, April next year would be more appropriate than a rate rise in December this year. And market participants also realise this. Communicating that a rise will come a few months later than we had previously planned would probably be interpreted as meaning that the policy rate will remain at –0.25 per cent for several years to come.

It is then easier for me to see the argument for a very flat interest rate path. Such an interest rate path would indicate that the repo rate will be held at today's level until we can see clear signs that economic activity and/or inflationary pressures are strengthening again. This alternative would bring our interest rate path close to the one priced by the market. However, the interest rate path would be significantly lower than the one we have previously communicated and I suspect that the market's expectations and pricing would shift further downwards in reaction to such a communication from us. As I mentioned previously, the Riksbank's monetary policy has had a greater impact on the financial conditions than we intended or desired given the development of economic activity and inflation. I therefore deem that this alternative would unnecessarily strengthen the market's already aggressive pricing.

I instead advocate the interest rate path included in the draft Monetary Policy Report. This path indicates that the repo rate will be raised towards the end of the year or possibly at the start of next year, but that the rate will subsequently only be raised once or twice over the course of the following three years. The first rate rise is justifiable as otherwise monetary policy would be unnecessarily expansionary in a way that would not benefit the Swedish economy. Confidence in the inflation target was seriously threatened in 2014–2016, as inflation had been well below target for many years, inflation expectations were at worryingly low levels and there was a risk that the krona would become too strong. Inflation has now been close to the target of 2 per cent for almost three years, confidence in monetary policy has been strengthened and there is nothing to indicate that the krona will become overvalued. The conditions for Swedish monetary policy are therefore better today. In December last year, we raised the repo rate from its lowest point of –0.50 per cent. My assessment is thus that conditions are in place to take a further step away from the very lowest interest rate levels soon. However, after this increase, I think that it will be appropriate to hold the rate steady until we see clear signs that economic activity and/or inflationary pressures have strengthened again.

First Deputy Governor Kerstin af Jochnick:

I support the assessments and forecasts in the draft Monetary Policy Report, and I support the proposal to hold the repo rate unchanged at –0.25 per cent. Moreover, I support the proposed forecast for the repo rate path, which entails that the next increase can be expected towards the end of this year or start of next year, but that subsequent increases will be made at a slower rate than in the previous forecast.

At the monetary policy meeting in July, we were able to note that the real economy and inflation in Sweden had largely developed in accordance with our forecasts. However, perhaps the most important issue was that of how uncertainty abroad could affect the assessments we made of developments over the coming years. The conclusion we then reached was to leave monetary policy unchanged.

Now, two months later, when we again are discussing the development of the economy and monetary policy, we can again note that the real economy and inflation, both in Sweden and abroad, have largely developed in line with our forecasts. However, in my opinion, the main difference from July is that uncertainty over global developments has become so much greater.

The escalated trade conflict between the United States and China is creating a substantial risk that the development of global growth will be significantly worse than we expect in our main scenario. It can be noted that indicators of developments in Germany, for example, are already pointing to a clear slowdown. It is difficult, however, to estimate the effects on trade patterns in the slightly longer term. To a certain extent, the trade taking place between China and the United States up until now can probably take new paths, which could dampen the negative effects on global trade and growth.

The likelihood of the United Kingdom leaving the EU without a withdrawal agreement has also increased since the monetary policy meeting in July. The new government in the United Kingdom seems to have no hesitation over leaving the EU on 31 October, even if this would be without an agreement. In the short term, such a scenario would probably have a major negative effect on growth in the United Kingdom. As far as Sweden is concerned, the direct effects on trade are not so large. However, indirect effects via other European countries' trade with the United Kingdom, such as Germany, and increased unease on the financial markets mean that the negative effects on growth could nevertheless be significant for Sweden.

Pricing on the financial markets has reflected increasingly pessimistic views of economic development in the period ahead. Over the summer, long-term bond yields have continued to fall to very low levels, reflecting expectations of lower future policy rates. The Federal Reserve cut its policy rate in July, while the ECB has communicated over the summer that monetary policy may be made more expansionary in the period ahead.

As far as I am concerned, one important question to consider at this meeting is whether, despite greater uncertainty and lower interest rates abroad, we deem that the repo rate can be raised towards the end of the year or at the start of next year. Another important question concerns the development of the repo rate over a slightly longer time frame, beyond the next six months – how rapidly do we deem that the repo rate should rise in the uncertain environment in which we find ourselves? I feel more certain answering the first of these questions than the second. Allow me to explain why.

I do not consider that inflation prospects over the short term are any different to the assessment made in July. Inflation retreated slightly over the summer months of June and July, but this was completely expected, as the contribution made by the previously high rate of increase in energy prices drops off. I consider that this is illustrated very well by Figure 1:4 in the draft Monetary Policy Report. Our assessment is that inflation will again rise over the autumn to just below 2 per cent. The rising rate of increase in producer prices, among other reasons due to the weak krona, as well as price plans in the wholesale and retail sectors, are factors supporting this assessment.

Inflation expectations are at around 2 per cent when we look at all participants in Prospera's survey. Assuming that the Swedish economy develops in accordance with our forecasts over the autumn, the conditions will be in place, in my opinion, to raise the repo rate at some point around the end of the year.

A more difficult question, in my opinion, is assessing the development of the repo rate further on. In one sense, this is not at all strange, as all forecasts become more uncertain in the longer run, as illustrated by the fan charts in the Monetary Policy Report. However, as regards the assessment of economic activity in the future, I consider that uncertainty is unusually great this time. Economic developments differing from those we see ahead of us could have substantial implications for the assessment of inflation and monetary policy further ahead.

In addition to the risk of less favourable developments abroad, which I have already addressed, I consider that a number of doubts are also present over the strength of domestic demand. According to the Tendency Survey of the National Institute of Economic Research, Swedish households have shown decreased confidence in economic development for a time. The downturn, compared with the peak of the upswing, can probably be explained by the slowdown of prices on the housing market, although households may also possibly have been affected by general reporting of increased risks abroad. Our forecast of Swedish households' consumption entails an annual rate of increase of 1.8–2 per cent over 2020–2021. This forecast is based on households having confidence in economic developments. If this is not the case, the risk is obvious for a weaker development of their consumption than in our forecast. On the other hand, unemployment continues to be relatively low, despite everything, and households' earlier unease over the development of the housing market should reasonably have eased now that housing prices have stabilised and are now rising at a modest pace.

This rising uncertainty makes it seem reasonable to proceed cautiously in monetary policy going forward, just as the proposed repo rate path indicates. All in all, I consider that the monetary policy described in the draft Monetary Policy Report strikes a reasonable balance.

At many monetary policy meetings and in several of my speeches, I have raised the issue of problems on the Swedish housing market and the risks associated with households' high indebtedness. The stabilisation of housing prices with the moderate rates of increase we are now observing is therefore very welcome. Compared with the earlier situation, this entails a kind of 'slow puncture' that, if we are lucky, will lead to more sustainable development in the period ahead. Having said this, the housing market continues to suffer from a number of structural problems that need to be focused on. Metropolitan areas need homes that can be rented, bought and transferred without decisive obstacles to efficiency. I consider that we must improve the possibilities for people from different parts of Sweden or the world to find a home in the metropolitan regions at a reasonable price; otherwise the housing market risks becoming an obstacle to growth and the positive development of society in a wider sense.

Finally, this has been my 49th and final monetary policy meeting. It has been a very exciting and interesting period in which to be a member of the Riksbank's Executive Board. I would like to take the opportunity to express my great gratitude to my colleagues at the Riksbank for this time!

Deputy Governor Henry Ohlsson:

To begin with, I would like to say that I support the proposal to leave the repo rate unchanged at –0.25 per cent. I also support the repo rate path showing a repo rate rise towards the end of this year or start of next year.

Annual growth abroad, KIX-weighted, is expected to amount to 2.0 per cent in 2019 according to the draft Monetary Policy Report. The forecast is unchanged since the monetary policy report in July. For 2020 and 2021, the forecast for both years is also 2.0 per cent. According to the draft Monetary Policy Report, KIX-weighted inflation is expected to be 1.8 per cent in 2019. The forecasts for 2020 and 2021 are 1.9 per cent and 2.0 per cent respectively. The two latter forecasts are unchanged compared with the Monetary Policy Report in July.

According to the draft Monetary Policy Report, the weighted average of international policy rates is expected to be 0.1 per cent in 2019. For 2020 and 2021, the forecast in the draft Monetary Policy Report is that the weighted average of international policy rates will be 0.0 per cent. This is not an inconsiderable change compared with the forecast in the July Monetary Policy Report. At the same time as the forecasts for the real economy abroad are almost unchanged, pricing on the financial markets has undergone major changes. Market rates have fallen significantly and monetary policy has become more expansionary, or is expected to become more expansionary, in many countries.

The CPIF has been the target variable for monetary policy since 2017. The most recent inflation figure in July showed an annual rate of increase in the CPIF of 1.5 per cent. I see this as an individual event. CPIF inflation has been around the inflation target for a long time. The two measures of core inflation that have demonstrated the best characteristics in a Riksbank Study are close to 2 per cent.[4] I also note that the moving average over twelve months for CPIF inflation is just over 2 per cent. Target achievement remains good! Even if inflation expectations have fallen somewhat in the latest measurements, I consider that they are still well anchored.

According to the most recent labour force survey (LFS), unemployment was 6.9 per cent (not seasonally adjusted) in July. This is higher than the corresponding month one year earlier, when LFS unemployment was 6.0 per cent. The Monetary Policy Reports have long forecast that LFS unemployment was about to bottom out. This has now happened. However, this should come as no surprise, indeed it has been expected.

At the same time, I think it is important also to look at other measures of unemployment when interpreting the LFS. Unemployment insurance fund members can be considered to have a relatively strong position on the labour market. In July 2019, the percentage of openly unemployed fund members was 2.9 per cent. This is higher than in the same month one year previously, when the proportion was 2.6 per cent. The downward trend that we have seen for several years has now been broken. The break in the trend emphasises that unemployment has bottomed out.

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[4] Jesper Johansson, Mårten Löf, Oliver Sigrist and Oskar Tysklind, 2018, "Measures of core inflation in Sweden", Economic Commentaries No. 11 2018, Sveriges Riksbank.

However, in my view, unemployment is too high and the increase we are now seeing is not desirable. But today it is primarily a matter of bringing down unemployment among foreign-born persons. And this is primarily a question of labour market policy measures to strengthen the human capital of unemployed persons and cut the cost of employing them. General demand side policies can provide support but cannot take primary responsibility.

Against the backdrop of this reasoning, I would now like to move on to my monetary policy considerations: My starting point is that monetary policy cannot be governed by inflation varying a few tenths of a percentage point around 2 per cent in individual months. Inflation has now been around the target of 2 per cent for quite a long period of time, both with regard to outcomes and expectations. This was the decisive argument for me in December 2018 that it was time to start raising the repo rate.

The draft Monetary Policy Report predicts a slowdown both in Sweden and internationally, but this has been incorporated into the forecasts for some time now. And uncertainty factors such as trade wars, the United Kingdom's withdrawal from the EU, the Italian economy etc. are not new. At every monetary policy meeting, there will always be phenomena that give rise to uncertainty. I cannot imagine a situation where the future is certain in all respects. Uncertainty is something economic policy always needs to live with.

However, the fact that market rates have fallen considerably around the world cannot be avoided. In addition, monetary policy has become more expansionary in a number of places. At the same time, the real economy is continuing to develop well despite the slowdown.

In light of this reasoning, I therefore consider it to be appropriate at this monetary policy meeting to leave the repo rate unchanged. Furthermore, I consider that it will be appropriate to stick to the forecast, over the short term, that the next rate rise will come at the end of this year or start of the next one. The Swedish economy is continuing to demonstrate a high level of activity, higher than in the euro area, for example. Inflation is on target. In Sweden, we can conduct our own monetary policy and there are good reasons at present to take advantage of this possibility.

At the same time, there is no avoiding that, in the slightly longer term, there is reason not to push on as rapidly with the approaching rate rises that previously adopted repo rate paths have indicated.

This time, I can support the economic picture and the forecasts in the draft Monetary Policy Report.

To summarise, I support the proposal to hold the repo rate unchanged at –0.25 per cent. I also support the repo rate path showing a repo rate rise towards the end of this year or start of next year.

Governor Stefan Ingves:

I support the proposal to hold the repo rate unchanged at –0.25 per cent. I also support the forecasts for and assessments of economic developments in Sweden and the rest of the world as described in the draft Monetary Policy Report. Our forecast for the repo rate – the repo rate path – indicates that an increase in the repo rate may occur later this year or at the beginning of 2020, which is in line with our view at the last monetary policy meeting. Further ahead, the repo rate path is revised quite substantially downwards, which is linked in part to the increased unease that we see in the global economy. I will return to this issue a little later on. Our government bond purchases are also part of monetary policy. In this respect, our strategy remains fixed, so I will not touch upon this aspect of monetary policy today.

The assessments of real economic developments abroad and in Sweden made in the draft Monetary Policy Report coincide quite well with the assessments made in July. This means that we are expecting more modest developments both in the global economy and at home.

The global economy has grown rapidly in recent years, and, as expected, is now entering a phase of lower growth. We expect growth of around 2 per cent in the coming years, if we look at the countries included in the KIX index, and around 3.5 per cent if we consider the world as a whole. Inflationary pressures abroad have been moderate in recent years, particularly in the euro area, but are expected to rise during the forecast period. A rising inflation rate abroad is an important starting-point for Swedish inflation to continue developing in line with the target.

As I noted, the changes in most of our forecasts are not so substantial. The exception is market rates and expectations on central banks internationally, which have fallen in an unexpected way since the July meeting. Our forecasts for international rates have therefore been revised down. At the same time, I think it is difficult to see how these expectations of significantly more expansionary monetary policy in the major currency areas could be realised, given the prevailing view of economic developments. Market pricing seems to point towards a rapid deterioration in global economic activity. Our forecasts, and those of many other analysts, imply softer development in the period ahead, but not an immediate recession. Both cannot be correct, so this friction and uncertainty remain.

One reason for the large movements in market rates is that the risk outlook for global economic activity continues to look uncertain. In my opinion, the risk outlook has deteriorated since the monetary policy meeting in July. The trade conflict between the United States and China is continuing with undiminished strength, Argentina is again facing a difficult situation, despite an extensive IMF programme, and here in Europe, there is still a lack of clarity regarding the United Kingdom's exit from the EU. The uncertainty surrounding developments in Italy continues, with political divisions and an incapacity to manage the risks linked to Italian banks. In other words, there is a number of major risks that may have a significant effect on economic developments.

However, the risks are very difficult to quantify, they will be incorporated into our forecasts only once they materialise, and were already there before albeit to a lesser extent.

Turning to developments in Sweden, it can be noted that economic growth in the second quarter of this year was weaker than expected, which has affected our forecasts for the quarters ahead. The forecast for GDP growth in 2019 is now 1.5 per cent, a downward revision of 0.3 percentage points compared with the assessment in July. The revisions for 2020-2021 are smaller, and towards the end of the forecast period, we expect growth of somewhat lower than 2 per cent, approximately the same as the assessment in July. However, the forecast revisions are relatively minor. We are now entering a period of softer growth, but economic activity is still high.

We have received two inflation outcomes since the last monetary policy meeting, and they have been slightly higher than the forecasts in the July report. The most recent observation concerns inflation for July, when the annual percentage change in the CPIF was 1.5 per cent. For the rest of the year, inflation is expected to rise to 2 per cent again, due in part to a weak krona and the fact that energy prices will stop pulling down inflation. Thus, inflation continues to develop in line with the target and target attainment is good. Long-term inflation expectations also continue to remain around 2 per cent, which is obviously good.

Sweden has had good economic development for several years. If we look at different measures of resource utilisation, such as the GDP or employment gap, and also consider the forecasts in the draft Monetary Policy Report, Sweden will have had a positive gap for six to seven years. In recent years, the labour market has developed strongly, with high employment levels and unemployment that last year fell to its lowest level in ten years. A contributory factor to this good development is the very expansionary monetary policy. The aim was to bring up inflation to the target, and we have also succeeded in doing so – inflation has developed in line with the target for several years now. A negative interest rate and substantial bond purchases may seem odd but generally speaking, Sweden has experienced good times and monetary policy has contributed to this.

The very expansionary monetary policy was never intended to last forever. Now when inflation is around 2 per cent, monetary policy is slowly going in a less expansionary direction, with a rate rise late last year, and another late this year or early next year. Sweden is a small, open economy with free capital movement and a floating exchange rate. However, this does not mean that we as monetary policy-makers can act completely independently of developments in the world's major economies. If we look at Swedish monetary policy in a slightly longer time perspective, we can say that Swedish rates should often be between those in Europe and those in the United States, and most often closer to those in Europe due to its greater significance for the Swedish economy. And if we look at the forecasts in the draft Monetary Policy Report, it is just such a monetary policy that is being proposed in the period ahead.

However, there is a risk outlook, as I mentioned earlier. If global growth were to be affected more negatively by, for example, the trade conflict between the United States and China, or by the United Kingdom's withdrawal from the EU, the major central banks may make monetary policy even more expansionary. If this were to be the case, we will have to decide at forthcoming monetary policy meetings what it means for Swedish monetary policy. It is too early to draw any conclusions, but as I said earlier, it can be noted that, when the ECB, for instance, made its monetary policy more expansionary in 2014 and 2015, Sweden was in a different situation, with low inflation and low inflation expectations. We are in a better place now, and therefore it is reasonable to assume that the degrees of freedom are greater.

A question that many economists have asked themselves in recent years is why real interest rates have been so low for so long, even substantially negative. The real repo rate, for example, has been negative since 2012, and is also expected to be so for the rest of the forecast period. If the forecast is accurate, this means over ten years with a negative real repo rate. Negative real interest rates are a global phenomenon, and also not a new one. In the 1970s, real interest rates in several of the world's major economies were negative. The difference now is that inflation is low, which means that nominal rates are also very low, or even negative. For our own understanding of where general interest rates are heading in the longer term, we are following this international debate, which has been inspired in part by ideas launched by Knut Wicksell. But there is certainly more to be done, for example, in order to determine where our repo rate is heading in the longer term. This is exactly how it should be – a central bank should occupy itself intensively with interest rates and exchange rates.

In conclusion, I would again like to point out that the Swedish housing market is characterised by a number of structural problems. This creates both risks, in the form of high indebtedness among households, and economic inefficiency in that it will be more difficult for people to move in connection with finding a new job. In order to address these risks and the structural problems on the Swedish housing market, a number of measures within housing and tax policy are required.

Kerstin, if with a little help I have calculated correctly, this is your 49th monetary policy meeting, and it is your last. I would like to thank you for the time and effort you have put in together with the rest of us to devise a Swedish monetary policy and not least often under difficult circumstances. Many thanks from all of us and good luck in your future work at the ECB and the Single Supervisory Mechanism.

§4. Monetary policy decision

The Executive Board decided

- to hold the repo rate unchanged at –0.25 per cent and that this decision shall apply with effect from Wednesday 11 September 2019.
- to adopt the Monetary Policy Report according to the proposal, Annex A to the minutes.
- to publish the monetary policy decision and the Monetary Policy Report with the motivation and wording contained in a press release at 09.30 on Thursday 5 September 2019.
- to publish the minutes from today's meeting at 09.30 on Tuesday 17 September 2019.

This paragraph was verified immediately.

Minutes taken by

Maria Kindborg

Verified:

Stefan Ingves	Kerstin af Jochnick	Martin Flodén
Per Jansson	Henry Ohlsson	Cecilia Skingsley

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