Monetary policy minutes

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MONETARY POLICY MINUTES

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Åsa Olli Segendorf
Ulrika Söderberg
Anna Österberg

Joel Birging (§1-3a)

It was noted that Magnus Jonsson and Anna Österberg would prepare the draft monetary policy minutes.

§3a. Economic developments

Market developments since the last monetary policy meeting

Joel Birging from the Markets Department began by presenting the latest developments in the financial markets. The US economy is still performing better than other developed countries and analysts have further revised up their GDP forecasts for 2024. Inflation outcomes during the period are an important reason for why the Federal Reserve is expected to wait before cutting the policy rate and the market is now pricing in just under two cuts this year. The outlook for growth in the euro area has improved, albeit from a low starting point, and the ECB is expected to cut the policy rate in June. Expectations of diverging monetary policy have contributed to a recent increase in interest rate spreads between the euro area and the United States.

The dollar has strengthened on a broad front and been recorded at new annual highs. In addition to a favourable macroeconomic environment, geopolitical uncertainty has also contributed to the strength of the dollar. The volatile geopolitical situation has also been a factor in the new records set by the gold price.

US equity indices have fallen from record-high levels, while equity indices in Europe have mostly moved sideways. Developments have been relatively undramatic and measures of implied volatility are at low levels. Expectations of rate cuts and better growth prospects are contributing to the generally positive sentiment.

Both analysts and the market are leaning towards the Riksbank now cutting the policy rate. The Riksbank's own policy-rate forecast and the inflation outcome for March are raised as arguments in favour of a cut. The krona has weakened since the interest-rate decision in March, and the exchange rate is considered an important reason if the Riksbank chooses to leave the policy rate unchanged.

Financial stability - current situation and risks

Olof Sandstedt, Head of the Financial Stability Department, described the situation in the Swedish financial system. The financial system has so far managed the challenges following the rapid upturn in inflation and interest rates, although both households and businesses have been, and still are, under pressure.

The major banks' large exposure to the highly-indebted real estate companies are still a vulnerability, but the situation for real estate companies has recently improved somewhat. Financing conditions on the bond market are more advantageous and more real estate companies have been able to issue bonds. However, there are risks linked to real estate companies' operations. For instance, office vacancy levels are elevated. If the rental market continues to be weak and interest rates remain at higher levels, it may put further pressure on both financial ratios and real estate values. Many real estate companies therefore need to continue to reduce their risks.

The major Swedish banks are assessed to have a good starting situation and they have margins above the capital requirements. Company bankruptcies have increased, especially in construction, retail, restaurants and domestic services, but so far, this has had a limited impact on the major banks' loan losses. Resilience among mortgagors has been high overall, but the personal finances of many households are strained and the number of payment injunctions is rising. The risk of payment problems increasing is elevated with regard to consumer loans, which can cause problems for institutions that focus on such loans.

The current monetary policy drafting process

Mattias Erlandsson, Deputy Head of 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 a drafting meeting on 29 April. The draft Monetary Policy Update was discussed at a meeting on 2 May.

The forecast in the March Monetary Policy Report was that inflation would meet the target this year, and that there were prospects for monetary policy easing. However, given the very high inflation in recent years and changed pricing behaviour, the Executive Board wanted further confirmation that inflation will stabilise close to the target, prior to a decision to cut the policy rate.

A central issue in the drafting process has thus been how new information has affected the outlook for inflation. The Executive Board has also discussed in detail developments in the US economy and how various scenarios for developments there would affect the conditions for monetary policy in Sweden.

Developments since the report in March provide further confirmation that inflation will stabilise close to the inflation target. In March, CPIF inflation was 2.2 per cent, which was 0.5 percentage points lower than expected. Energy prices are lower than last year and making a negative contribution to inflation, but even excluding energy prices, inflation is falling. The CPIF excluding energy was just below 3 per cent in March. The decline was broad among the sub-groups and prices of goods, services and food increased more slowly than expected. Calculated at a shorter time horizon, such as 3 or 6 months, the price changes for inflation excluding energy are somewhat below 2 per cent.

At the same time, forward-looking indicators point to a continued decline in underlying inflation. For instance, the National Institute of Economic Research's Economic Tendency Survey shows that fewer companies are planning to raise their prices. Long-term inflation expectations are well anchored around the target. With regard to the real economy in Sweden, the picture remains largely unchanged since March. The krona has weakened, especially against the dollar, and is weaker than in the March forecast. Overall, this suggests that CPIF inflation may temporarily undershoot the target slightly this year, before stabilising close to the target in the slightly longer term.

International economic developments are fragmented. The US economy is performing well, with higher inflation than expected, while developments in Europe are weaker and more in line with what was expected in the March Monetary Policy Report.

As described in the draft Update, expectations of future policy rates abroad have risen. According to market pricing, approximately two rate cuts of 0.25 percentage points are now expected from the Federal Reserve this year. This can be compared with the expectations of three at the end of March, and six at the beginning of the year. The ECB is expected to cut its rate two or three times this year, starting in the summer. Policy-rate expectations have also risen in Sweden, especially in the longer run, and market expectations are now more in line with the forecast in the March Monetary Policy Report.

The proposal for a monetary policy decision that the Monetary Policy Department judges will gain a majority in the Executive Board at today's meeting is described in Annex A to the minutes. The proposal entails cutting the policy rate by 0.25 percentage points to 3.75 per cent at today’s meeting. If the outlook for inflation stays the same, the policy rate can be cut two more times during the second half of the year, in line with the forecast in March. The Riksbank's asset holdings will continue to decrease through maturities and the sales of government bonds as decided in January.

§3b. The economic situation and monetary policy

First Deputy Governor Anna Breman

I support the proposal to cut the policy rate from 4 to 3.75 per cent. I also support the monetary policy assessments presented in the draft Monetary Policy Update.

Monetary policy has contributed to inflation falling and now approaching the target. Inflation expectations are still well anchored and information we have received since our last meeting reinforces the outlook for inflation being close to the target also in the medium term (see Figures 4 to 8 in the draft Update). As inflation is now starting to stabilise while economic activity is weak, monetary policy can be eased. I therefore support cutting the policy rate at today's meeting and I share the assessment that the policy can probably be cut twice more during the second half of the year, in line with the forecast from the previous meeting.

At today's meeting, I would like to comment on the real economy, the risk outlook and the rate path. I would also like to highlight the risk of major fluctuations in inflation in individual months and what this means for monetary policy.

First, economic activity is weak, but there are still major differences between different sectors in the Swedish economy. Manufacturing and exports are performing strongly while household consumption and housing investment are weak. In addition, the labour market has weakened. As inflation is now approaching the target, conditions are favourable for a recovery in all sectors. Low and stable inflation makes it easier for firms and households to plan ahead, facilitating investments. The fall in inflation is also boosting real wages and strengthening household purchasing power. This will contribute to economic growth and higher employment in the coming years.

Second, the risk outlook for inflation has become more balanced. The risk of setbacks remains, but there is also a risk of inflation undershooting the target. The inflation outcome for March was lower than expected, for both the CPIF and the CPIF excluding energy. The price plans of businesses have continued to fall, bankruptcies are increasing and the labour market has weakened. This could lead to lower inflation going forward. However, geopolitical tensions remain and unexpectedly high inflation in the United States has caused the US dollar to strengthen against many currencies, including the Swedish krona. This can lead to higher import prices via higher inflation abroad and/or via a weaker exchange rate, thereby increasing inflation in Sweden. If the outlook for inflation changes, monetary policy will be adjusted. This brings me on to my third point, the rate path.

My assessment is that our forecast for the policy rate from our previous meeting is holding up well. At the meeting in March, the rate path indicated a cut in May or June and then gradual cuts in the coming years. Forecasts, however, are as always more certain in the near term. If inflation shows signs of increasing, we can hold off with further cuts, and if inflation risks undershooting the inflation target more sustainably, we may need to make more cuts than the current path indicates. However, deviations from the forecast in individual monthly outcomes are not reason enough to change direction. It is an overall assessment of the outlook for inflation in the medium term that guides monetary policy. This includes an assessment of global and Swedish economic activity and other factors that can affect inflation, such as the krona exchange rate.

An example of this is the strengthening of the US dollar against the krona as market expectations of rate cuts in the United States have changed. It is relatively small deviations in inflation outcomes that have led to significant changes in market expectations of rate cuts. This tends to spill over to expectations in Sweden and can also affect the Swedish economy and the transmission of monetary policy via effects on market rates and the krona exchange rate. This is not a reason to refrain from a rate cut at today's meeting as forward-looking factors indicate low and stable inflation going forward. However, it is important to continue to monitor the krona exchange rate if we see that it affects the outlook for inflation in Sweden.

That said, let me return to domestic factors and the risk of major fluctuations in Swedish inflation in individual months. In the near term, temporary factors such as major entertainment events can affect monthly outcomes. For example, Sweden will host both Eurovision and Taylor Swift concerts in May. This could lead to temporarily higher prices for services. But, there may also be inflation outcomes on the downside. In individual months, CPIF inflation may fall significantly below 2 per cent. Let me therefore reiterate. It is not this type of individual monthly outcome that determines the direction of monetary policy, but it is always an assessment of where inflation is heading in the medium term.

Before I conclude, I would like to comment briefly on our reduced asset holdings. The tapering is both gradual and predictable, which has helped to improve market functionality. In addition, it reduces the risks on the Riksbank's balance sheet. The plan to gradually normalise the balance sheet remains intact. This is made clear in the forecast for the policy rate and the projection of bond holdings in the Monetary Policy Report in March (see Figure 33). We will come back later this year to stipulate an appropriate long-term level of asset holdings.

Allow me to summarise. Inflation is approaching the target and the conditions are favourable for sustainably low and stable inflation also in the medium term. I therefore support the proposal to cut the policy rate and my assessment is that the policy rate may be cut further going forward. However, the risk of setbacks remains. If the outlook for inflation changes, monetary policy will be adjusted. A smooth return to low and stable inflation should not be taken for granted.

Deputy Governor Aino Bunge

I support both the proposal to cut the policy rate by 0.25 percentage points to 3.75 per cent at this meeting and the assessments made in the draft Monetary Policy Update.

In summary, I consider that the prospects are brighter for inflation in Sweden but there remain risks abroad, and the Swedish krona is weaker than in March.

At our last meeting, we communicated that the policy rate could probably be cut in May or June if the inflation outlook continued to be favourable. Inflation is now close to the target. According to the latest outcome in March, it was at 2.2 per cent, measured by our target variable CPIF. The outcome was significantly lower than expected. Measured in terms of the CPIF excluding energy, inflation was 2.9 per cent, which was also lower than expected. Price movements in the shorter term are continuing downwards, as can be seen in Figure 6 in the draft Update.

The Swedish economy has slowed down, largely in line with our forecast. Some “green shoots” can be seen, including in the form of the most recent Economic Tendency Survey. However, this increased optimism is probably also based on expectations of future policy-rate cuts. Moreover, the improvements in several sectors are taking place from a weak starting position. So there is little evidence of any “spring fever” yet. Fortunately, both short-term and long-term inflation expectations are anchored around the target (see Figure 8 in the draft Update).

The labour market showed considerable resilience during the period of rising interest rates. However, it has been weakening for some time and we now see reduced employment and rising unemployment. Outcomes in the most recent quarter were slightly below our forecast (see Figure 4 in the draft Update). Other indicators such as redundancy notices and bankruptcies also indicate rising unemployment in the period ahead.

In my view, one important piece of the inflation assessment puzzle is the continued positive signals we are receiving about companies’ pricing behaviour. According to the Economic Tendency Survey, slightly fewer companies than normal now expect increased sales prices in the retail trade over the next three months (see Figure 7 in the draft update). However, it will be important to monitor developments closely going forward, not least when household demand recovers, as we expect it to.

I consider that all of the factors I have mentioned suggest that monetary policy in Sweden should now be less contractionary. This is to stabilise inflation around the target without simultaneously inflicting unnecessary damage to the real economy and, not least, employment. At the same time, however, several factors clearly call for caution in monetary policy and these factors primarily revolve around international developments.

As described in the draft update, the decline in inflation in the United States seems to have slowed down which is connected to the continued strength of the world’s largest economy. Expectations of fewer rate cuts from the Federal Reserve have further strengthened the dollar and the Swedish krona has also weakened against the euro. The krona exchange rate thus poses a continued upside risk for inflation. However, market expectations of future policy rates and their effect on the krona have been volatile to say the least. This is a reminder of the existing uncertainty and that the path to sustainably low and stable inflation is not necessarily straightforward. To this can be added the ongoing geopolitical risks and associated risks for new supply shocks, which could trigger new inflationary impulses in Sweden.

Nevertheless, my overall assessment is that now is the time to start easing monetary policy. After today's initial cut, we should also be able to cut the policy rate in the autumn, in line with our forecast from March. However, the adjustment of monetary policy will have to be made with caution and with an eye on international developments. Large and rapid rate cuts may also lead to a large increase in demand in Sweden, which, particularly in combination with a weakened currency, may make inflation rise again.

At the same time, now that inflation is again close to the target, it is important not to focus excessively on individual inflation outcomes but to continue to monitor a broad set of indicators to assess inflationary pressures in the period ahead. Our ambition is primarily to stabilise inflation around the target but also to contribute to a favourable development of the real economy.

Deputy Governor Per Jansson

I support the decision to cut the policy rate from 4 to 3.75 per cent. I also support the economic assessments presented in the draft Monetary Policy Update. At our monetary policy meetings on both 31 January and 26 March, I identified two prerequisites for me to support a first policy-rate cut. These were, firstly, that the favourable development of inflation continued and, secondly, that the rate-cutting plans of the major central banks abroad were not significantly postponed. I still assess these prerequisites to be relevant in the current situation, so let me update them one by one.

Looking first at the development of inflation, I already considered at our meeting in March that it probably fulfilled the requirement of being favourable enough to be compatible with a rate cut. Since then, we have received one new inflation outcome, for March, showing that inflation continues to fall, both including and excluding energy prices. And the decline is broad and going faster than expected. CPIF inflation amounted to 2.2 per cent, compared to the projected 2.7 per cent in the Monetary Policy Report in March. For inflation excluding energy prices, the outcome was 2.9 per cent and the forecast 3.3 per cent.

Shorter-term measures of price growth also continue to provide a clear picture of easing inflationary pressures. This applies to different measures of inflation as well as the major consumer-price sub-groups. Annualised, price growth in the shorter term is now often below 2 per cent, or, when it comes to the sub-groups, below the average rate of increase that can be expected to be compatible with the inflation target.

The ever-brighter inflation picture is also apparent in the development of services prices at different frequencies. Here, I mentioned at our March meeting that there was a tendency for these price increases to stick around annual rates of 5 per cent or just slightly lower, which is most likely too high in a long-term perspective. At the same time, I emphasised that a not insignificant part of the rapid rate of increase in services prices had to do with earlier cost increases and certain specific events, that is, drivers that could be expected to be transitory. This now seems to be confirmed by significant declines in both the monthly change in services prices in total and the change in underlying measures of services prices that exclude these presumed temporary effects.

The favourable development in inflation also continues to be supported by increasingly low price plans among companies, inflation expectations close to the inflation target and wages that, considering the circumstances, are increasing at a moderate pace, just over 4 per cent. Adding all this together, I see no obstacles, from an inflation development perspective, to now starting to cut the policy rate. If anything, the risk of inflation being too low for a while has increased. I will return to this risk, which is also emphasised in the draft Update, later on.

I will now turn to the other prerequisite that needs to be in place to be able to cut the rate today, the one related to the monetary policy of the Federal Reserve and the ECB. My view in March was that there was a not inconsiderable risk of delays especially to the rate cuts of the Federal Reserve. And here, I said that it could not 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. All this, I feared, could have rather major negative effects on the Swedish krona exchange rate, and this in a situation where the krona was already at the outset at an unfavourably weak level. The risk I saw with this was of course that it could break the favourable inflation trend that has prevailed since late autumn last year and cause inflation to start rising again.

I think developments since our meeting in March show that there is something in the arguments I put forward then. When we held our March meeting, the markets’ interpretation was that the Federal Reserve would cut its policy rate three times by 0.25 percentage points this year, probably starting in June. The markets have since shifted forward their expectations of a reduced rate in the United States during the year, periodically so that pricing has only reflected a single cut towards the end of the year. Some analysts have even warned that the next rate adjustment from the Federal Reserve may be a hike rather than a cut. Thanks to some favourable data outcomes at the end of last week, the markets’ expectations are just now a little more optimistic again, pricing in slightly less than two rate cuts of 0.25 percentage points, where the first cut is fully reflected in the pricing at the end of October. In parallel with this, the krona exchange rate has continued to depreciate, primarily against the US dollar but also against the euro.

A positive aspect here is that the ECB's plans to cut its policy rate seem not to be influenced by the changed conditions for rate cuts in the United States, at least not so far. In the case of the ECB, the markets expect a first rate cut in June, or possibly July, and pricing reflects overall between two and three cuts during the year.

To sum up, there is still some ambiguity in the timing of rate cuts among the major central banks abroad. This uncertainty comes largely from rapid changes in the markets' expectations of how the Federal Reserve will conduct its monetary policy, where individual data outcomes in a positive or negative direction have the potential of having very large effects. Expectations of the ECB's actions are more stable and continue to indicate a first rate cut during the summer. This, in combination with the very favourable development in Swedish inflation, means that I support the decision to cut the policy rate from 4 to 3.75 per cent at today's meeting. The markets' new-found optimism regarding the conditions for cutting the rate in the United States is also of some importance in the context.

I mentioned earlier that the rapid decline in inflation in Sweden means that the risk of inflation being too low for a while has increased and that this is also something that is highlighted in the draft Update. After about two years of inflation substantially overshooting the inflation target, I must admit that this is not directly something I am currently having sleepless nights over. Furthermore, that this risk increases when inflation falls and starts to approach the target is of course completely inevitable. In addition, I share the view in the draft Update that this is about inflation possibly somewhat undershooting the target temporarily later this year, but that the inflation outlook in the slightly longer term has not been affected. I am also quite sure that several other central banks, in the situation they find themselves in, are somewhat envious of those who already have reason to, so to speak, start getting "worried" about the risks of slightly too low inflation.

That said, the current situation nevertheless provides an opportunity to mention some fundamental aspects that may be good to talk about in advance, before a situation with slightly below-target inflation has already emerged. It is obvious that the sights of monetary policy are not set on undershooting the inflation target. But should such a situation nevertheless emerge, especially after quite some time with far too high inflation and a great sense of responsibility in wage formation, a slightly faster recovery in real wages and other real incomes could be noted as a positive side-effect. This could be favourable for wage formation over time, not least because it should reduce the risk of demands for inflation compensation in wage increases going forward.

Crucial here of course is that the target deviation does not create confidence problems for the inflation target. And this in turn stresses the importance of the deviation being limited, both in size and in time. If this is not the case, monetary policy will not be able to “see through” the deviation but must then be adjusted.

Another positive side-effect of not reacting with monetary policy to these kinds of fairly small target deviations is that it could gradually lead to the establishment of a “more relaxed” view among economic agents in general about deviations from the inflation target. If this is the case, confidence in the target need not deteriorate and above all, the fluctuations in the policy rate could then be smaller than they have been over the last 15 years or so. I believe this would be good for the Swedish economy as a whole.

These are just a few preliminary thoughts that certainly need to be discussed and refined. Time will tell whether it is possible to move in this direction.

Deputy Governor Martin Flodén

I support the proposal to cut the policy rate by 0.25 percentage points to 3.75 per cent. I also support the analyses and considerations presented in the draft Monetary Policy Update.

It is just six weeks since our last monetary policy meeting. During these weeks, the inflation outcome for March has been the most important news affecting our decision today. Inflation was considerably lower than in our forecast, and this applies to services, goods and food alike.

This strengthens the view of Swedish monetary policy having had the intended effect and of inflation now falling rapidly to lower levels. As economic activity is weak and we are starting to bring inflation back under control, it is appropriate for us to start cutting the policy rate to make monetary policy less contractionary.

Monetary policy will remain contractionary even after a policy rate cut to 3.75 per cent. If these developments continue, it will therefore be appropriate to continue to cut the rate by a few more steps. I assess that our rate forecast from the March meeting remains reasonable. This means that more rate cuts will likely be justified this year, but that it will probably not be appropriate to cut the rate again as early as June. However, the uncertainty around this assessment is considerable as it is difficult for several reason to assess both how far and how rapidly the rate should be cut in the coming years.

Several of the uncertainty factors I listed at our last monetary policy meeting remain at least as noticeable today. In the United States, the economy has shown surprising resilience and inflation has repeatedly been higher than expected over the last six months. This can affect Swedish monetary policy, partly via the strong dollar exchange rate and partly via the emergence of expectations of similar inflation dynamics in Europe and Sweden.

Such interpretations are also indicated by the expectations that can be inferred from pricing in the financial markets. Despite the very positive inflation outcome in March, pricing indicates that market participants now expect fewer rate cuts from the Riksbank this year than they expected at our last monetary policy meeting.

At the last monetary policy meeting, I also mentioned that the effects on demand in the economy can be considerable when the Riksbank cuts the rate for the first time in more than eight years. I also mentioned that we already saw signs of such effects as a consequence of rate cuts being discussed. The signs of this have become increasingly clear in recent weeks. For example, the National Institute of Economic Research's Economic Tendency Survey for April indicated an increase for all sectors.

A rate cut today will probably reinforce this trend. In that case, it will be important going forward to monitor how rapidly increasing optimism affects demand in the economy and ultimately the scope of companies to raise their prices.

At the last monetary policy meeting, I also mentioned the significance of fiscal policy for the design of monetary policy going forward. For a long time, fiscal policy has played a rather inconspicuous role in our monetary policy analysis. When inflation was worryingly low and the policy rate was close to its lower bound, changes in fiscal policy did not lead to instant monetary policy reactions. And when inflation later increased, fiscal policy was restrained so as not to disturb the Riksbank's fight against inflation.

We are now approaching a more normal state, where monetary policy needs to react to changes in how expansionary or contractionary fiscal policy is. If fiscal policy becomes more expansionary, monetary policy will, all else being equal, need to become more contractionary, for example via the rate being cut at a slower pace. When inflation is close to target and the rate is clearly above its lower bound, such monetary policy reactions are therefore a completely normal element in stabilisation policy.

Another uncertainty factor I wish to mention relates to the changes in relative prices that have occurred in recent years. Consumer prices have risen more than wages. Energy and commodity prices have at times been very high, which has also pushed up various consumer prices. However, energy and commodity prices have since fallen back. The exchange rate has weakened. And prices have risen significantly more for some consumer goods than for others.

Certain changes in the economy will likely be permanent. In that case, it is justified that certain changes in relative prices will also be permanent. But many of the shocks in recent years have been temporary and should not lead to permanent changes in relative prices. It is then unclear how the adjustment will take place. Will it mostly happen via prices that have previously risen rapidly being reduced or increased unusually slowly in the coming years? Or will it mostly happen via other prices increasing unusually rapidly? Uncertainty surrounding these issues makes it difficult to assess current inflationary pressures, which is perhaps also reflected in the major forecasting error for inflation in March.

After the broad decline in inflation in March, it is likely that inflation outcomes in the second half of the year will be below 2 per cent on several occasions. However, both the increasing optimism in the Swedish economy and the weak exchange rate suggest that subsequent inflationary pressures will be at least as high as our assessment at the monetary policy meeting in March. I still see the monetary policy plan we formulated then as reasonable, but it is of course a plan that continuously needs to be adapted to new information.

Governor Erik Thedéen

I support the proposal to cut the policy rate by 0.25 percentage points to 3.75 per cent, and I support the assessments made in the draft Monetary Policy Update. In March, we communicated that the policy rate could probably be cut in May or June if the inflation outlook continued to be favourable. Today we can observe that we have received confirmation of such favourable developments. There are – as always – risks to take into account, and I will return to these shortly. However, I nevertheless feel that we are now as sure as we can reasonably be that inflation will remain low. It is therefore appropriate for us to begin gradual monetary policy easing.

Although developments in the United States are raising some questions, the global inflation outlook nevertheless continues to be favourable overall. This is despite ongoing war, geopolitical tensions and changes in global trade patterns. Energy and commodity prices are relatively stable and inflation is continuing to fall in most countries. However, in the United States, inflation in the last quarter has been higher than many people had hoped and expected. Together with some unexpectedly strong indicators of economic activity in the United States, this has led to a substantial change of scene in global financial markets. Pricing indicates that market participants now expect the rate cuts in the United States to come much later, compared with the situation at the end of last year, and in many countries, long market rates have shifted upwards quite considerably. For instance, the yield on a US ten-year government bond has risen by around 0.6 percentage points since the turn of the year, and in Germany and Sweden the corresponding yields have risen by 0.4 and 0.3 percentage points respectively. Meanwhile, the krona exchange rate has weakened.

The higher interest rates, as I said, are linked to changed inflation prospects in the United States. Some indicators point to growth there still being robust, and inflation is continuing to surprise on the upside. It is possible that demand and inflationary pressures in the United States will quite simply decline at a slower pace, compared with the forecasts made at the end of last year, and that the US policy rate will nevertheless be cut relatively soon. The data on the US labour market that we received last Friday has probably reinforced this picture. However, various indicators point in different directions and it is difficult to interpret the situation at present. Another conceivable alternative is that developments in the United States will continue to surprise us and other analysts and that the US central bank will not cut the policy rate as expected. This could have an increasingly large impact on economic activity in Europe, too, with stronger economic activity, higher inflationary pressures and even higher interest rates. When there are signs that the world's largest economy is changing direction, and when forecasts for its growth and inflation shift upwards, there is reason for vigilance. Swedish monetary policy will continue to be based on developments in the Swedish economy and inflation, but it will not be unaffected by developments in the United States.

It is already clear that the higher international interest rates, through their effects on the krona exchange rate, pose a risk to the inflation outlook here in Sweden. This risk is reinforced by the uncertainty prevailing with regard to the pass-through of the exchange rate to consumer prices. When inflation was very high earlier, there was reason to believe that the pass-through to inflation was higher than normal and we also saw indications that CPIF inflation was affected more than usual by the weak exchange rate. It is conceivable that the pass-through has been dampened again, as inflation has fallen back, but this is not something we can count on. The continued weakening of the krona thus comprises a risk that may affect how quickly monetary policy can be eased.

We also need to continuously monitor and evaluate the effects of the interest rate cuts we are now starting. A risk that I have mentioned earlier, and which gains further relevance after today’s decision, is the uncertainty over how Swedish households and companies will react when the policy rate is cut. One possibility is that demand will rise more, compared with the assumption in our March forecast, and that it will be aimed at sectors that have difficulty increasing their production at a rapid pace or where a lack of competition means that companies can increase their price mark-ups. During the pandemic, it became clear that the composition of demand can shift considerably and rapidly. When household purchasing power increases again going forward, it is possible that unexpected inflationary impulses will arise again. The uncertainty also applies to developments in the housing market and in the construction sector, where we have seen considerable interest-rate sensitivity. Our endeavour with today's policy rate cut, and the coming gradual reductions we see ahead of us, is to contribute to increasing demand without driving up inflation. We shall thus welcome an economic recovery, but be vigilant that this occurs without prices going in the wrong direction.

There are, of course, further uncertainty factors that can affect the inflation outlook in Sweden. Now that we are emerging from a situation with too high inflation, there is a risk that we could underestimate the probability of inflation undershooting the target of 2 per cent going forward. It will therefore be important to clearly illustrate in coming Monetary Policy Reports the risks of inflation being too low.

I will now describe the reasons why I consider it is now appropriate to make monetary policy less contractionary.

In Sweden, the outcomes and forward-looking indicators published in recent weeks have largely confirmed the picture of the economic outlook and inflation prospects outlined in the March Monetary Policy Report. Economic activity is still subdued, weighed down by weak household consumption and by a low level of residential construction. The slowdown in the labour market has continued in recent months, with rising unemployment and continued elevated redundancy figures. At the same time, employment is still high and according to the National Institute of Economic Research's Economic Tendency Survey, companies' recruitment plans have stabilised. Several forward-looking indicators are also pointing to stronger developments in coming quarters, which supports the forecast in our March Report. In addition, there are early signs that the housing market has strengthened somewhat, for instance, turnover is increasing.

In March, inflation fell more than expected, which confirms the picture from some months ago that inflation is now slowing down and moving towards the target, and several indicators point to continued low inflationary pressures in the coming months. One example is producer prices, which remain low. Another is companies' price plans, where the responses from companies in the retail sector indicate unusually low price plans in the coming three months. The fact that inflation expectations are anchored at the target, at the same time as economic activity is subdued, also means, on a more general level, that the prospects for inflation remaining low also in the slightly longer term are favourable. Overall, this means that inflation prospects have continued to improve since the monetary policy meeting in March, and that the risks of persistently high inflation have been further reduced.

It is against this backdrop that I assess that we are now as sure as we can reasonably be that inflation will remain low. It is therefore appropriate for us to begin a gradual monetary policy easing. I also think that the policy rate path for the coming quarters published in the March Monetary Policy Report is still a reasonable forecast. Given the information we have today, it should be appropriate to cut the policy rate around two more times this year, following today's decision.

The uncertainty over how policy rate cuts will affect the economic outlook and inflation prospects justifies making the cuts gradually, and regularly evaluating the need for further easing. In doing this, we need to consider international developments, which affect the Swedish economy via several different channels, including the exchange rate. But, as I have stated earlier, it is inflationary pressures and the outlook for inflation here in Sweden that are decisive factors in our decision.

It is an important step we are taking today, when the Riksbank decides to cut the policy rate for the first time since 2016. Following a period with substantial global inflationary impulses, price growth in Sweden of around 10 per cent and considerable uncertainty over inflation prospects, we are now back in a situation where CPIF inflation is close to the target of 2 per cent and where the prospects for continued low inflation are favourable.

During the period with high inflation, Sweden's framework for monetary policy and wage formation has demonstrated its strength. It is easy to forget that the way the Riksbank and other agents have managed the upturn in inflation is perhaps the first time the system had been really tested since the framework was properly established, at the end of the 1990s. We and others should therefore thoroughly evaluate this period. But my assessment is that the inflation-targeting policy has this time managed the test well, as far as we can now see. Firmly anchored inflation expectations, responsible outcomes from last year's wage bargaining rounds and tight monetary policy have all contributed to inflation falling back rapidly. The low public debt has also meant that the higher interest rates only had limited impact on public finances. As inflation is now close to the target of 2 per cent, inflationary pressures are comparatively low and the risks of persistently high inflation have declined significantly, it is also possible to conduct monetary policy in a more forward-looking manner than we had scope to do last year. Then, we had repeatedly underestimated inflationary pressures and at times saw a need for monetary policy to react significantly to new inflation readings. Individual CPIF readings that will be published in the coming quarters and years will sometimes be higher than expected, and sometimes lower. However, if CPIF inflation overshoots or undershoots the target by one or a couple of tenths of a percentage point in individual months, this should not in itself affect our plans for conducting monetary policy. In this respect, it is important that we and other agents have realistic expectations of what monetary policy can achieve. The Riksbank does not have the ability to control with precision the inflation outcomes for individual months. The strength of the inflation-targeting regime instead lies in its ability to steer inflation one or a couple of years ahead to the target of 2 per cent, even after substantial disruptions.

The fact that there is reason to see beyond individual surprises in price growth does not mean that monetary policy is being put on autopilot. We will continue to adjust the policy rate and our forecasts in the light of new information. The point is that the risks to the credibility of the inflation target have been reduced considerably in the past year. This means that there is now greater scope to adjust the pace at which inflation is brought back to the target so that monetary policy can contribute to a balanced development of production and employment.

In conclusion, the whole Executive Board and I would like to thank Martin Flodén for his excellent and important efforts on behalf of the Riksbank during your 11 years as deputy governor. You have been an important colleague, and we will all miss you, a lot. Your complete commitment, tremendous knowledge and great team spirit have been very much appreciated by us on the Executive Board and all the Riksbank staff. We wish you the best of luck in your future work at the university and anywhere else you may be employed.

In conclusion, Deputy Governor **Aino Bunge** added: I share Anna Breman's view that the tapering of our asset holdings shall be gradual and predictable, as this helps to improve market functionality and reduce the risks on the Riksbank's balance sheet. The plan to gradually normalise the balance sheet therefore remains intact.

§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 3.75 per cent, which means that it is cut by 0.25 percentage points,
- to establish the Monetary Policy Update according to the proposal, Annex B to the minutes Monetary Policy Update,

- to publish the monetary policy decision in a press release at 09.30 on Wednesday 8 May 2024,
- to publish the minutes from today's meeting at 09.30 on Wednesday 15 May 2024.

This paragraph was confirmed immediately.

Minutes taken by

Magnus Jonsson Anna Österberg

Verified by

Erik Thedéen Anna Breman Per Jansson

Martin Flodén Aino Bunge

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