The way from the financial crisis and forward – The development of monetary policy

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

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First Deputy Governor

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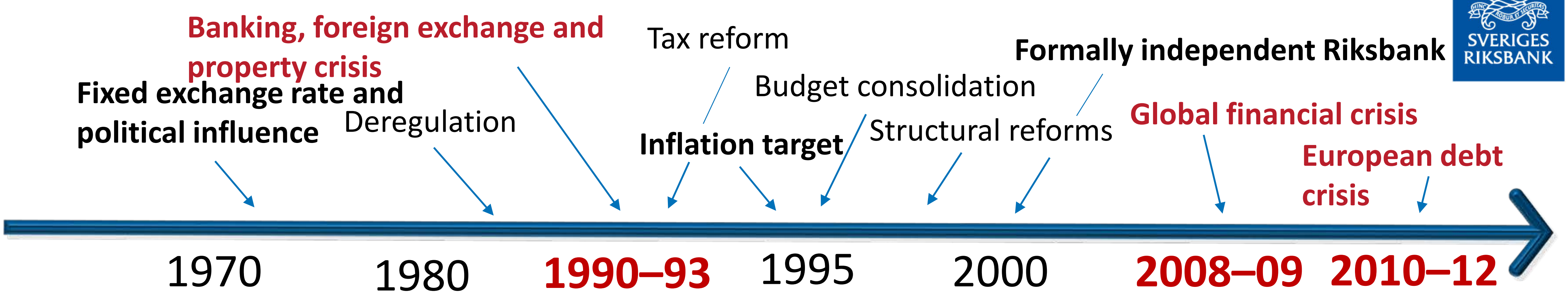
Agenda

- The inflation-targeting regime and its contribution
- From 2008: Global financial crisis, European debt crisis and weak global growth: increasing challenges for monetary policy
- Monetary policy in a low interest rate environment
- Current monetary policy

The inflation-targeting regime and its development



High inflation and low increases in real wages

Low inflation and stable increases in real wages

Recurring devaluations

Low interest rates

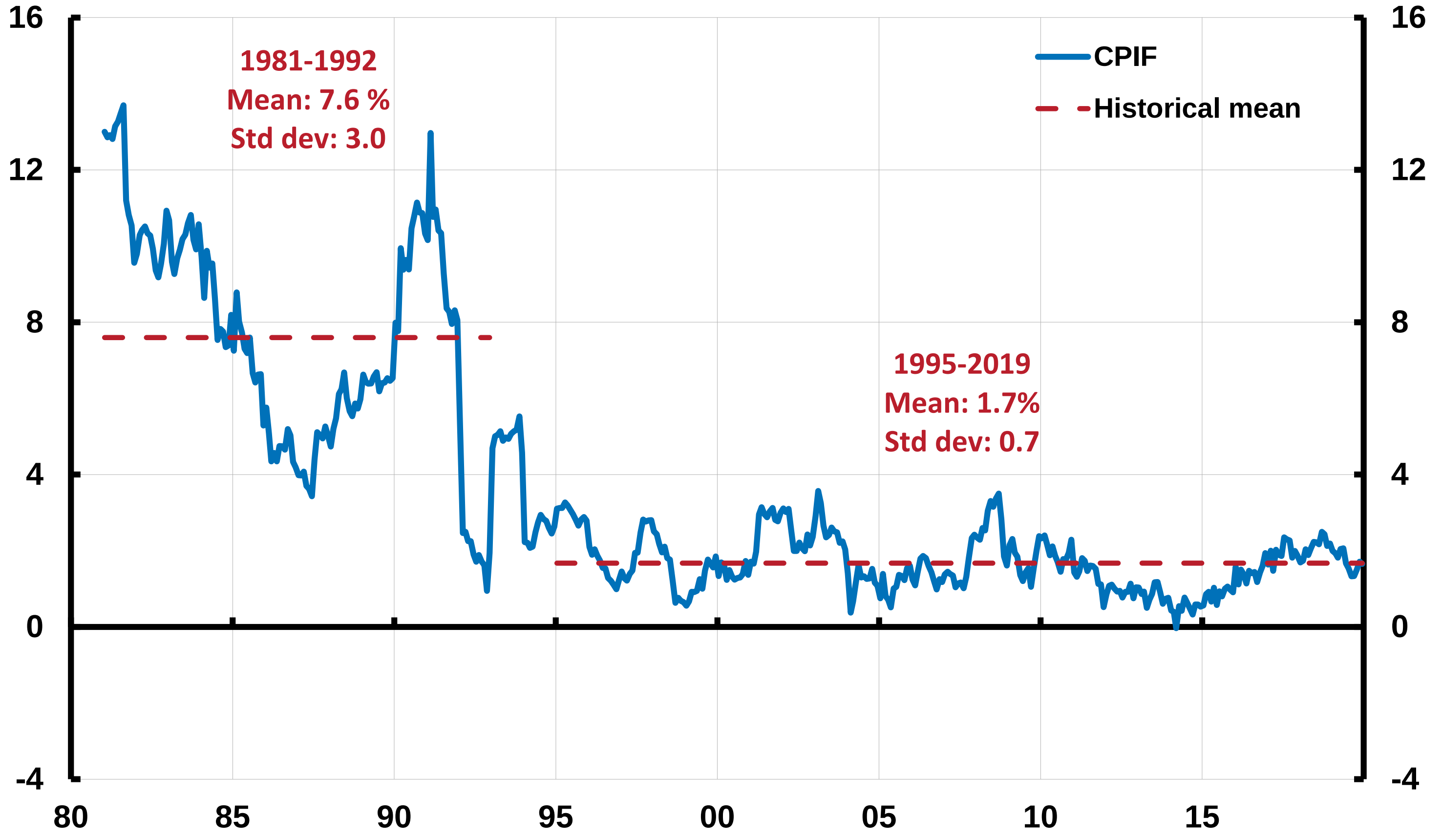
Current account deficit

Current account surplus

Budget deficit and high national debt

Budget surplus and low national debt

A credible inflation target comprises an anchor for the economy

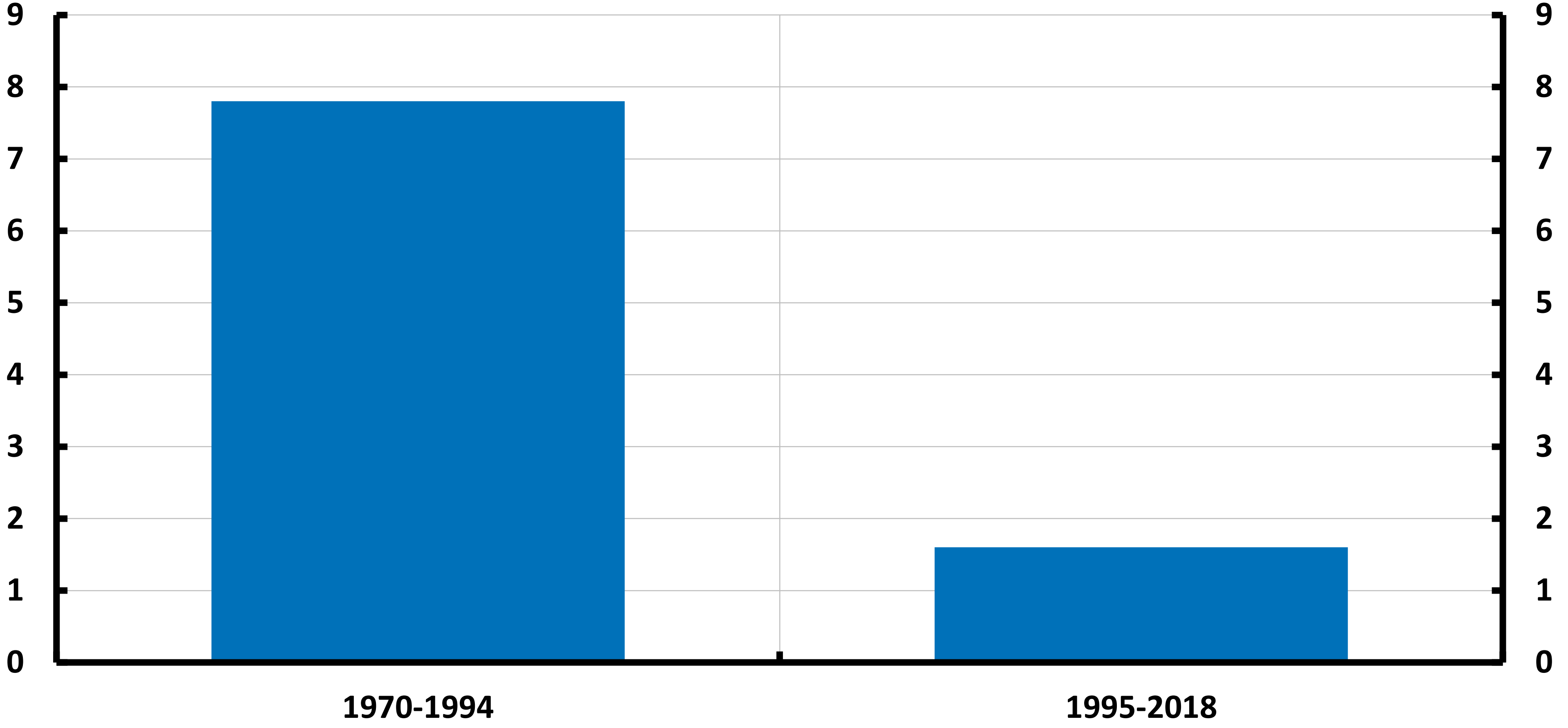


Per cent. Between 1981–1987, the CPI excluding interest was used and, after this, the CPIF.

Source: Statistics Sweden and the Riksbank

Economic growth before and after the crisis of the 1990s

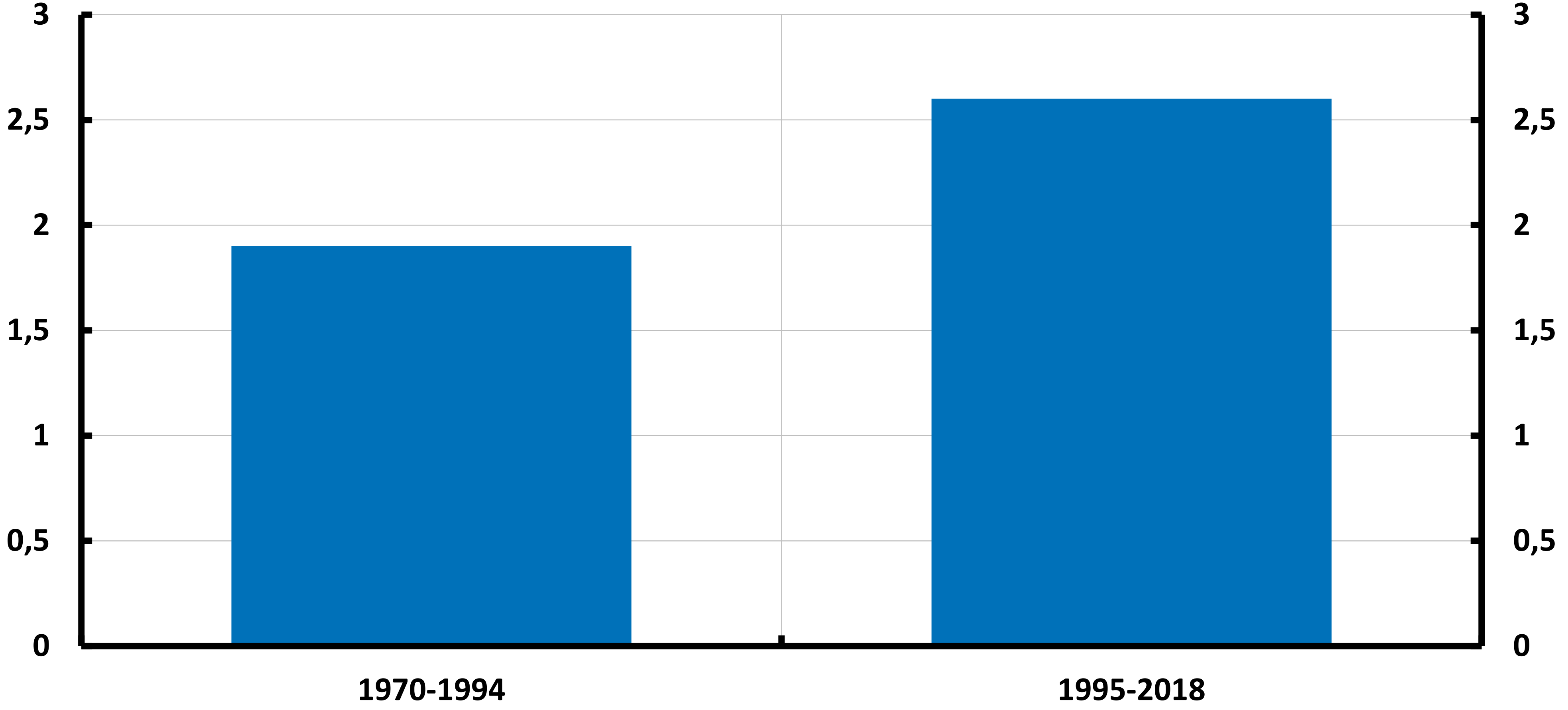
Low and stable inflation after the crisis of the 1990s



Per cent

Sources: Statistics Sweden and the Riksbank

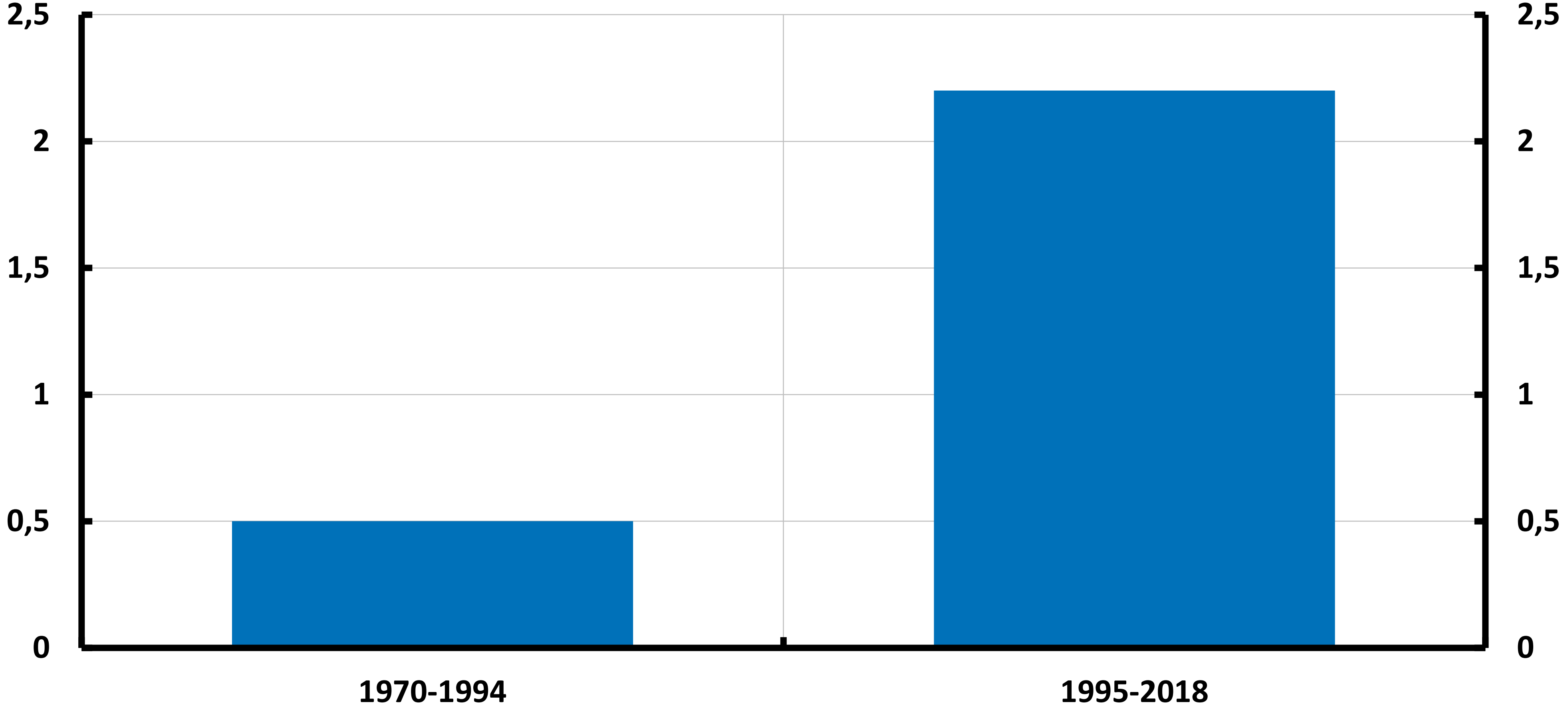
Higher GDP growth after the crisis of the 1990s



Per cent

Sources: OECD, Statistics Sweden and the Riksbank.

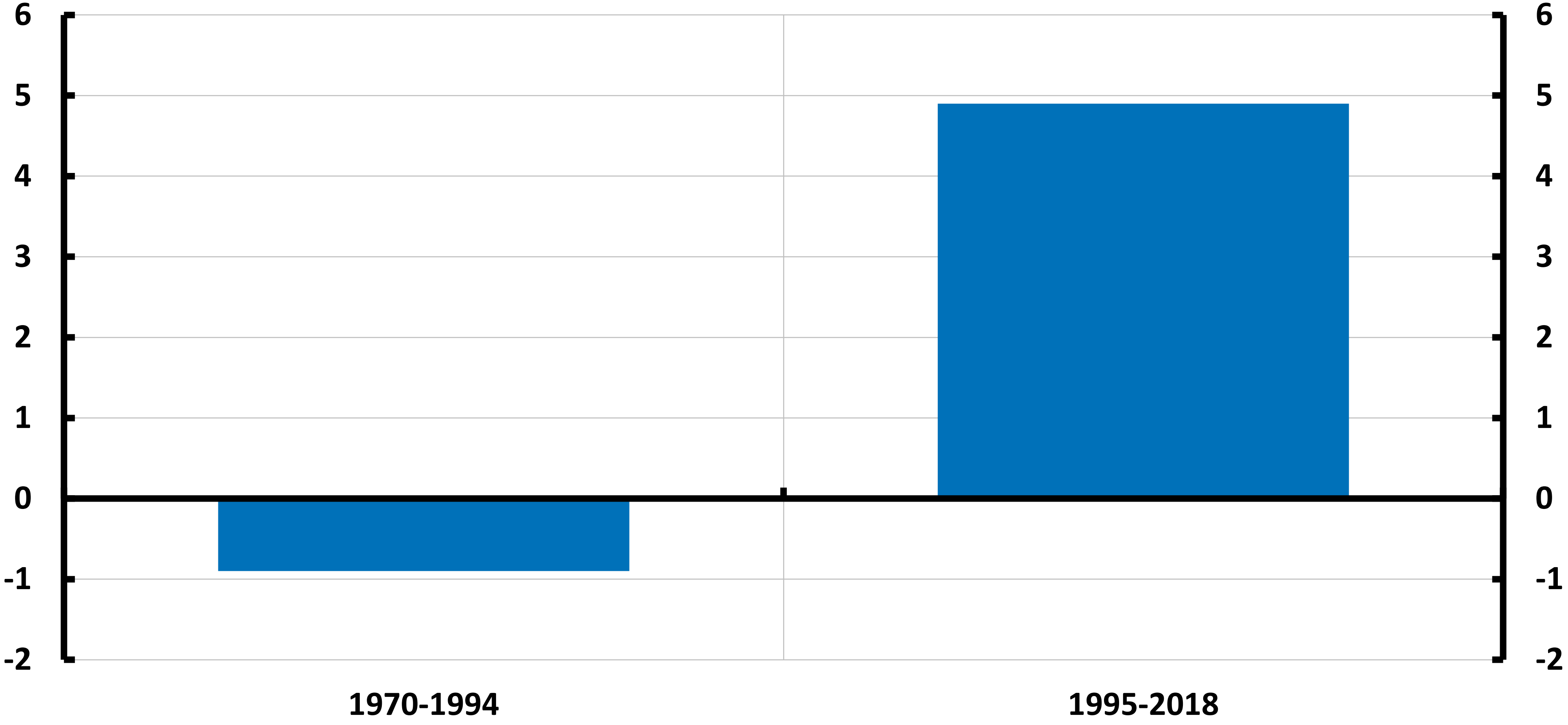
Higher increases in real wages after the crisis of the 1990s



Per cent

Sources: National Mediation Office, Statistics Sweden and Ekonomifakta

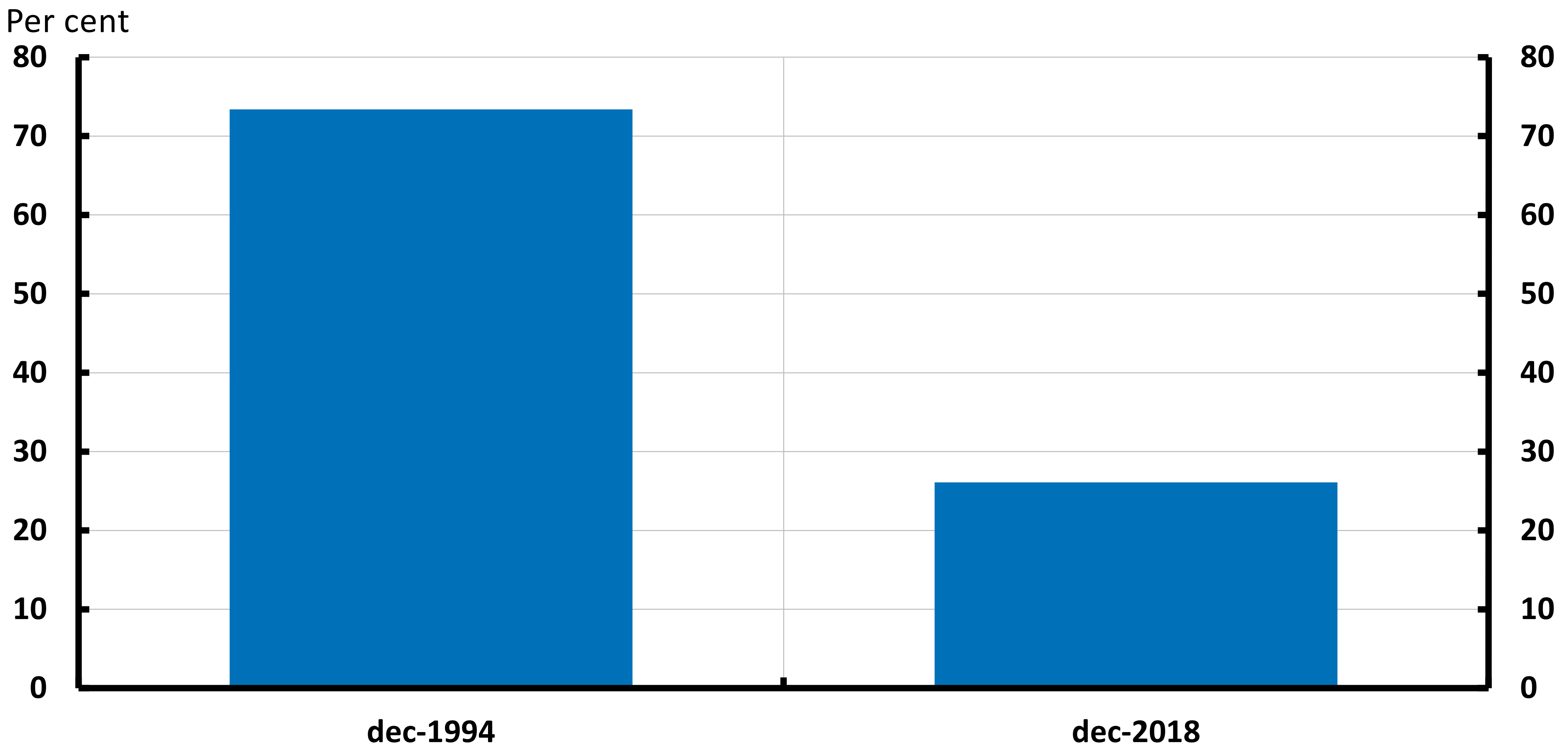
Current account surplus after the 1990s crisis



Per cent. Current account in relation to GDP.

Sources: Statistics Sweden and the Riksbank

Lower national debt after the crisis of the 1990s

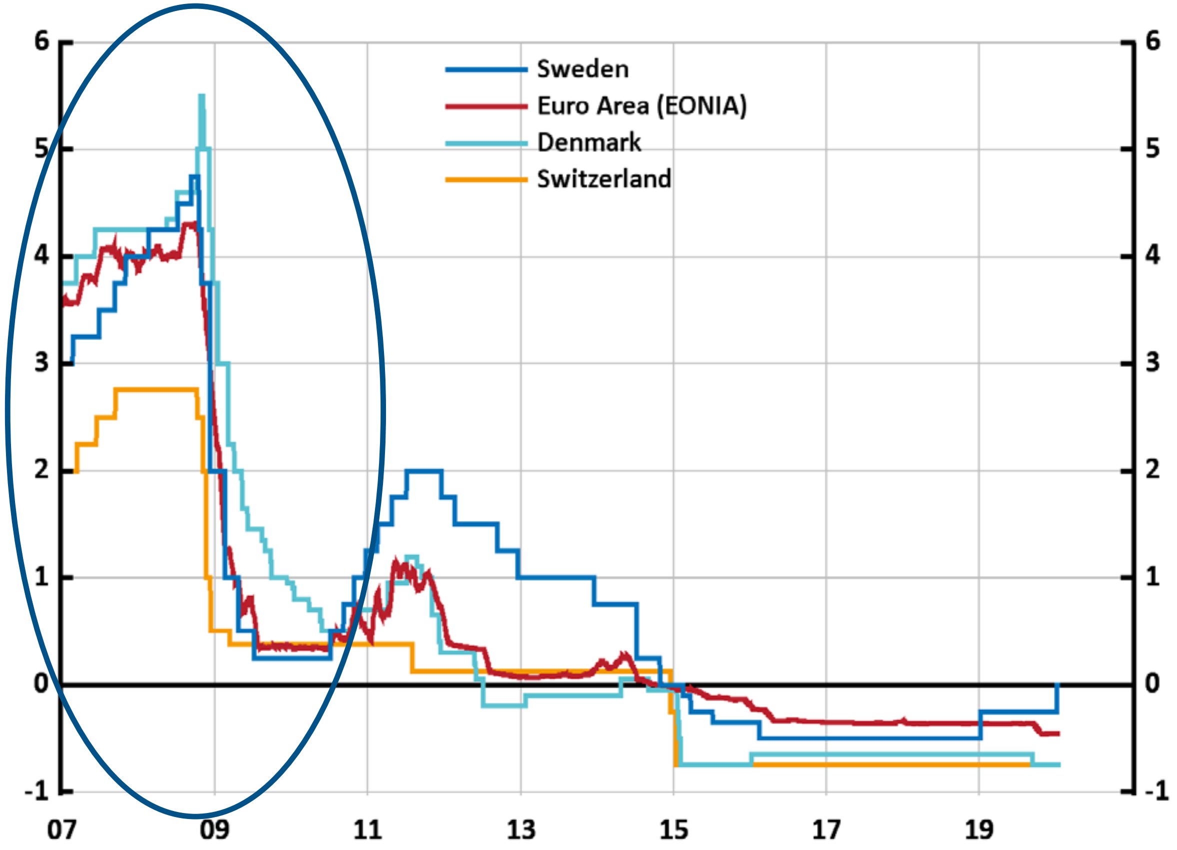


National debt in relation to GDP.

Sources: Swedish National Debt Office and the Riksbank

From 2008: Global financial crisis, European debt crisis and weak global growth: increasing challenges for monetary policy

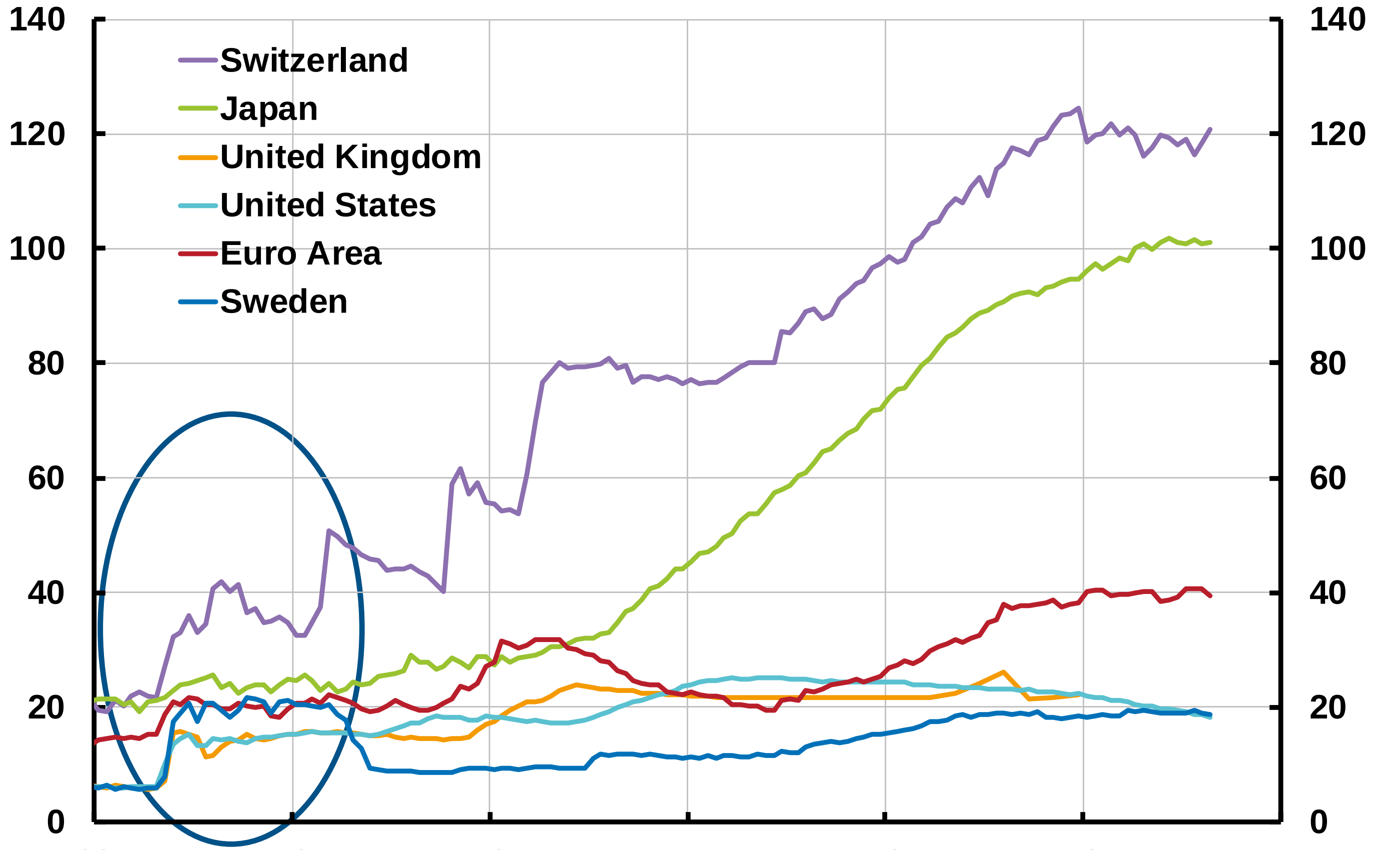
Central banks quickly cut their policy rates to close to zero per cent



Per cent. Euro area refers to EONIA, 30-day rolling average.

Sources: Bank of England, ECB, Federal Reserve Bank of New York and the Riksbank

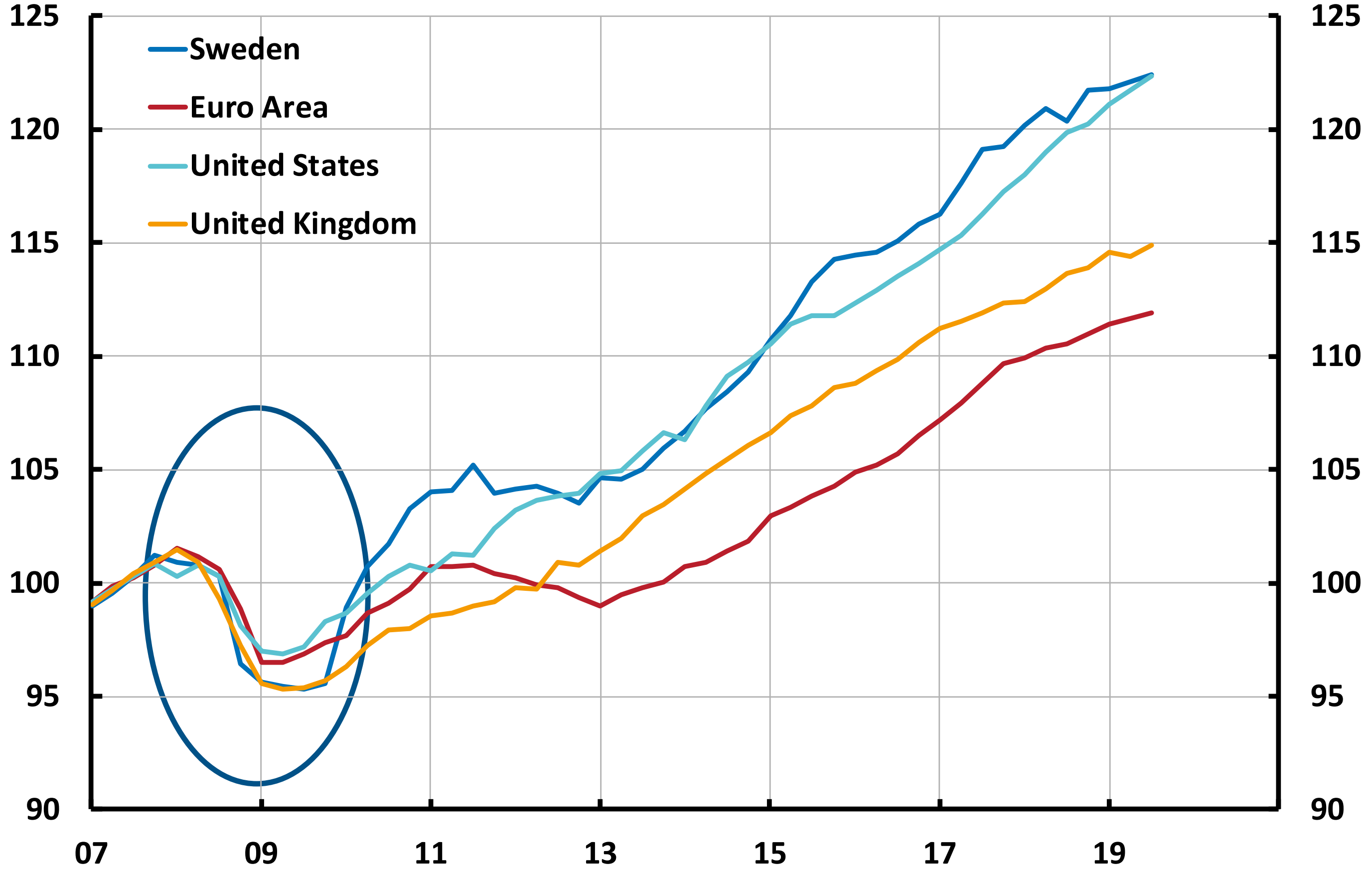
Central banks’ balance sheets grow



Central bank assets as a percentage of GDP.

Sources: National central banks and accounts

Large downturn in GDP – Sweden copes relatively well

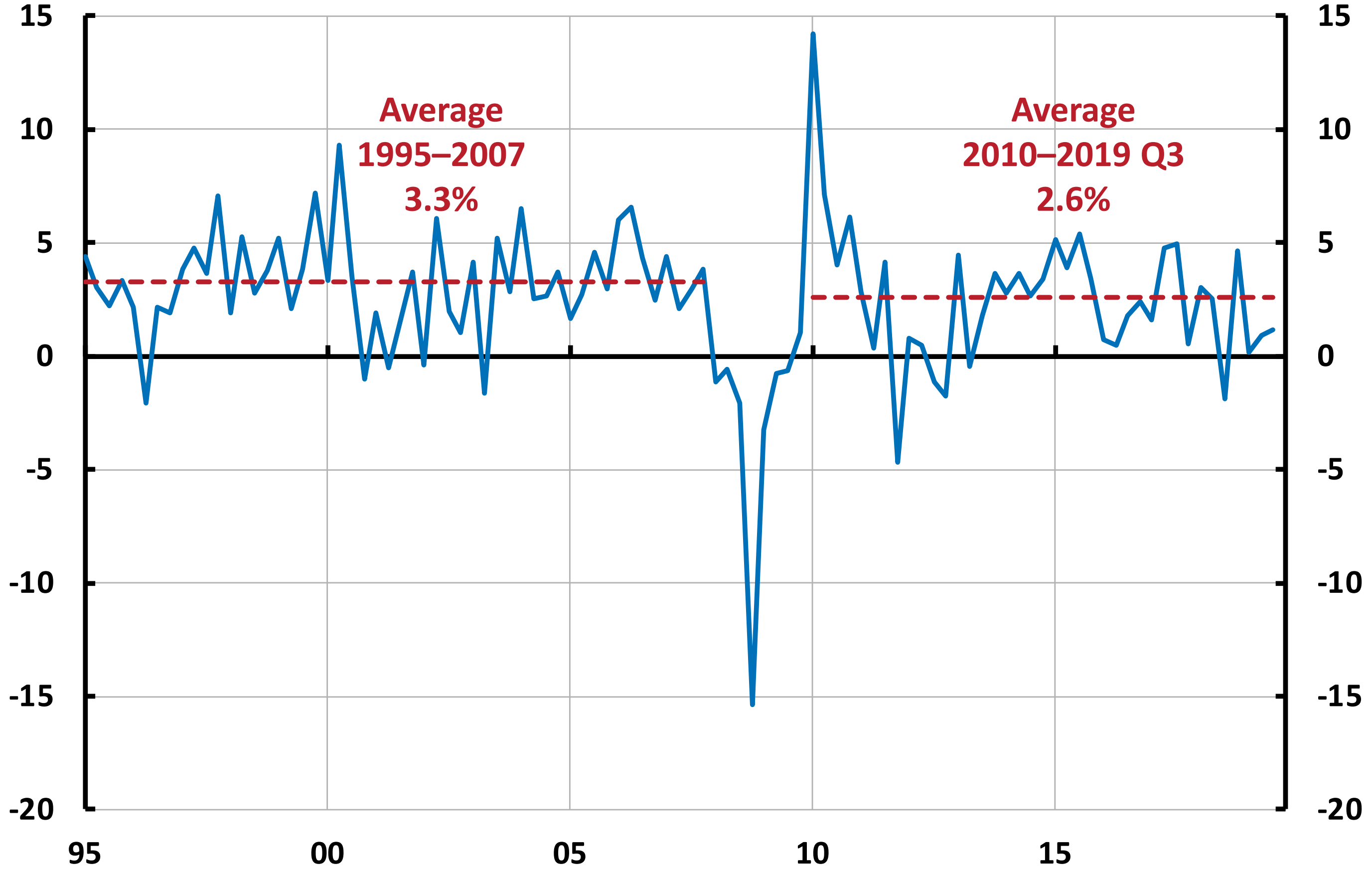


Index: 2007=100 GDP in constant prices.

Sources: Bureau of Economic Analysis, Eurostat, UK Office for National Statistics and Statistics Sweden

Economic growth before and after the financial crisis

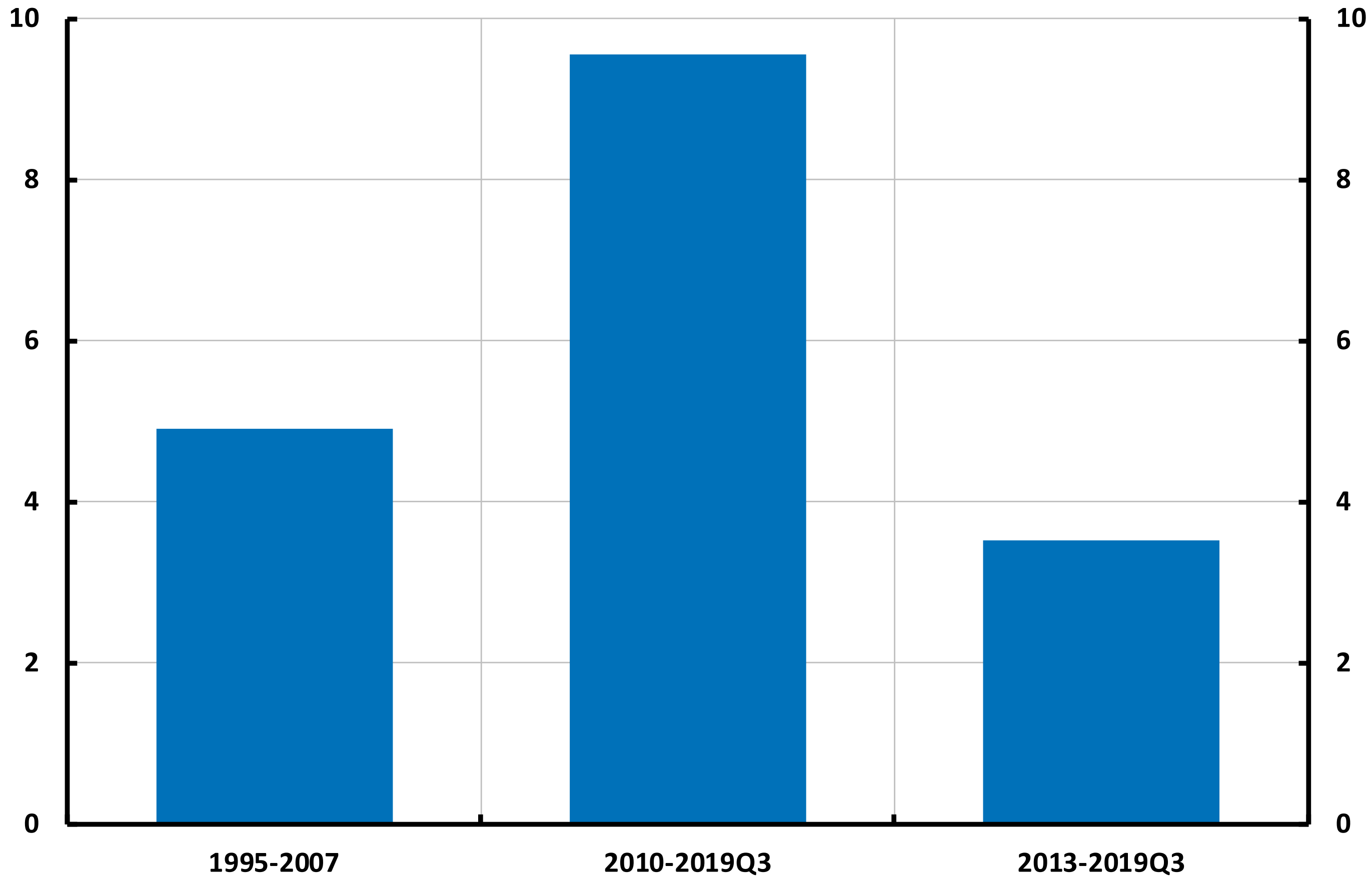
Lower average GDP growth after the financial crisis



Per cent. Quarterly growth calculated as an annual rate.

Source: Statistics Sweden

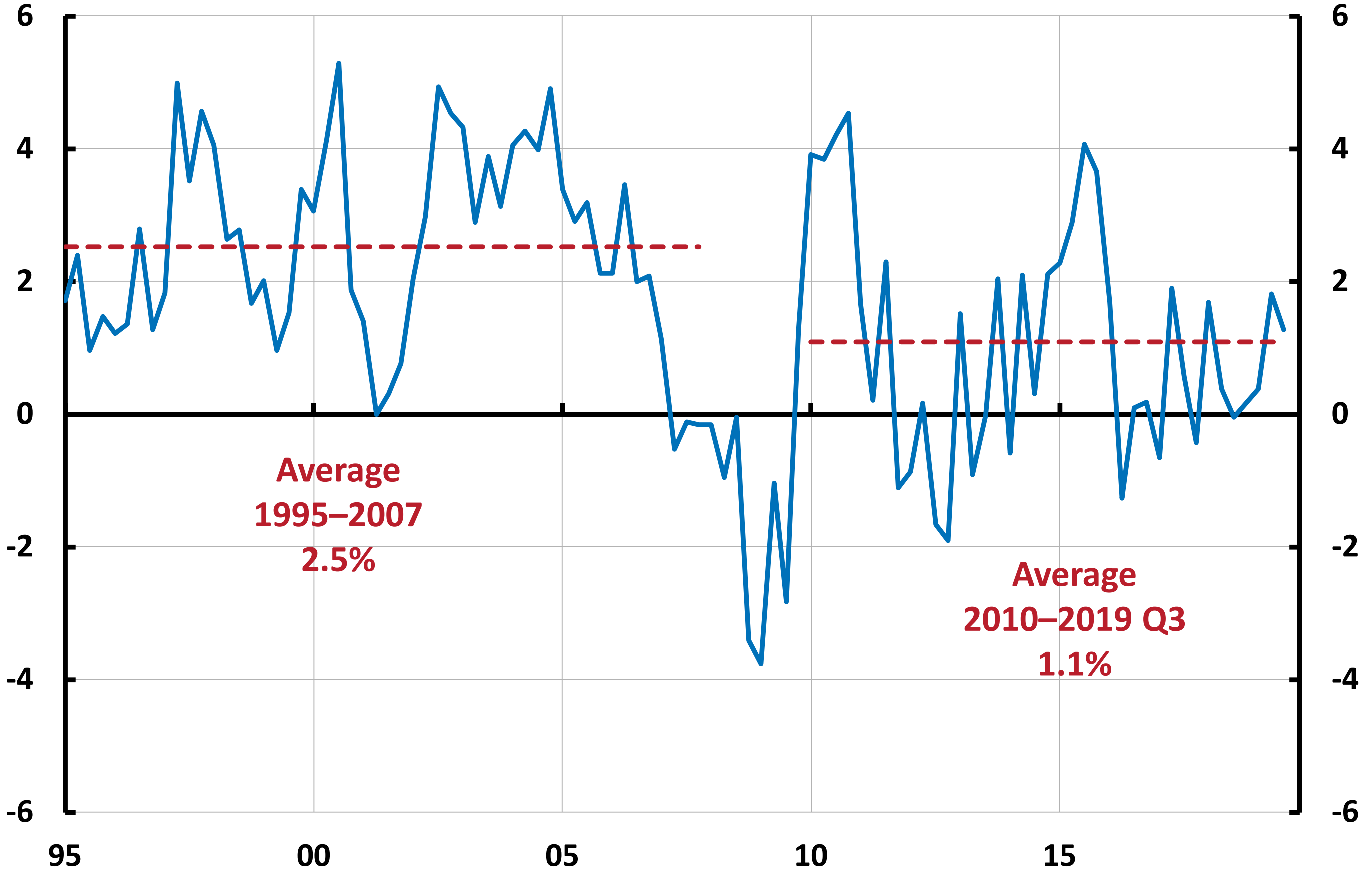
Smaller fluctuations in GDP after the debt crisis



Variance in GDP growth.

Source: Statistics Sweden

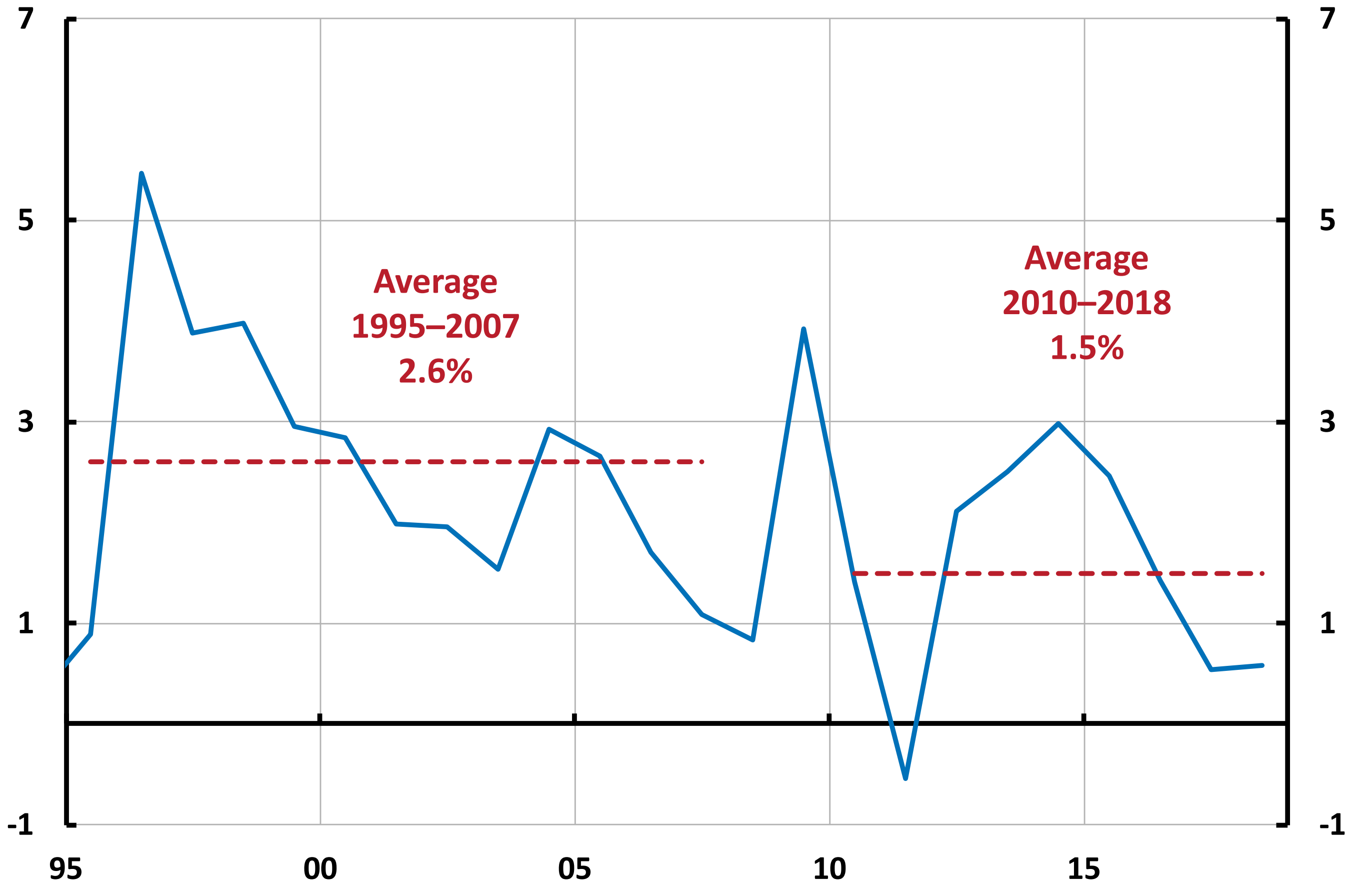
Lower average labour productivity after the financial crisis



Per cent. GDP in relation to hours worked.

Sources: Statistics Sweden and the Riksbank

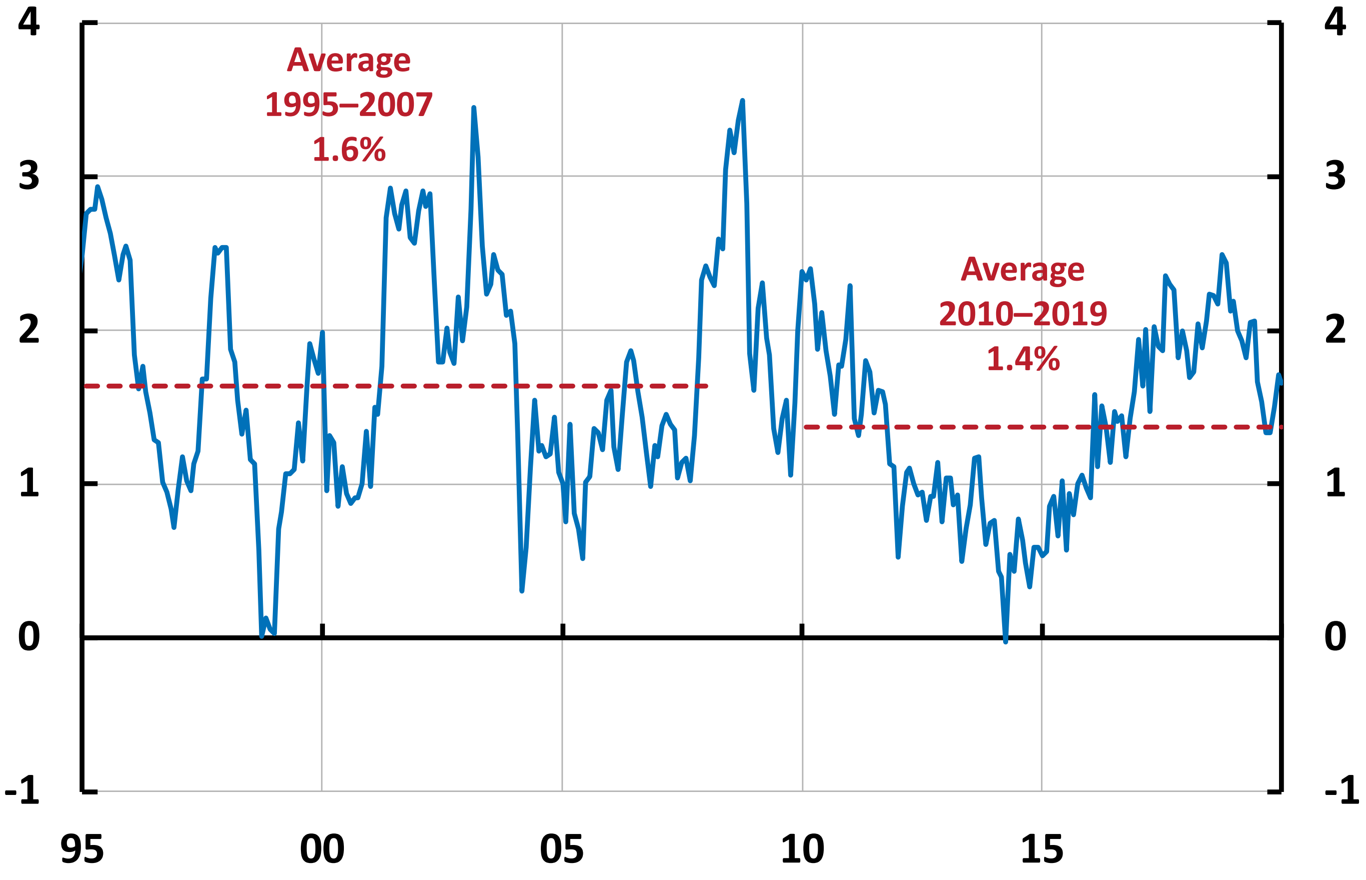
Lower average real wages after the financial crisis



Per cent. Real wages are calculated as the difference between the annual percentage change of nominal wages and the annual percentage change in the CPIF.

Sources: The National Mediation Office and Statistics Sweden

Inflation (CPIF) slightly lower after the financial and debt crises

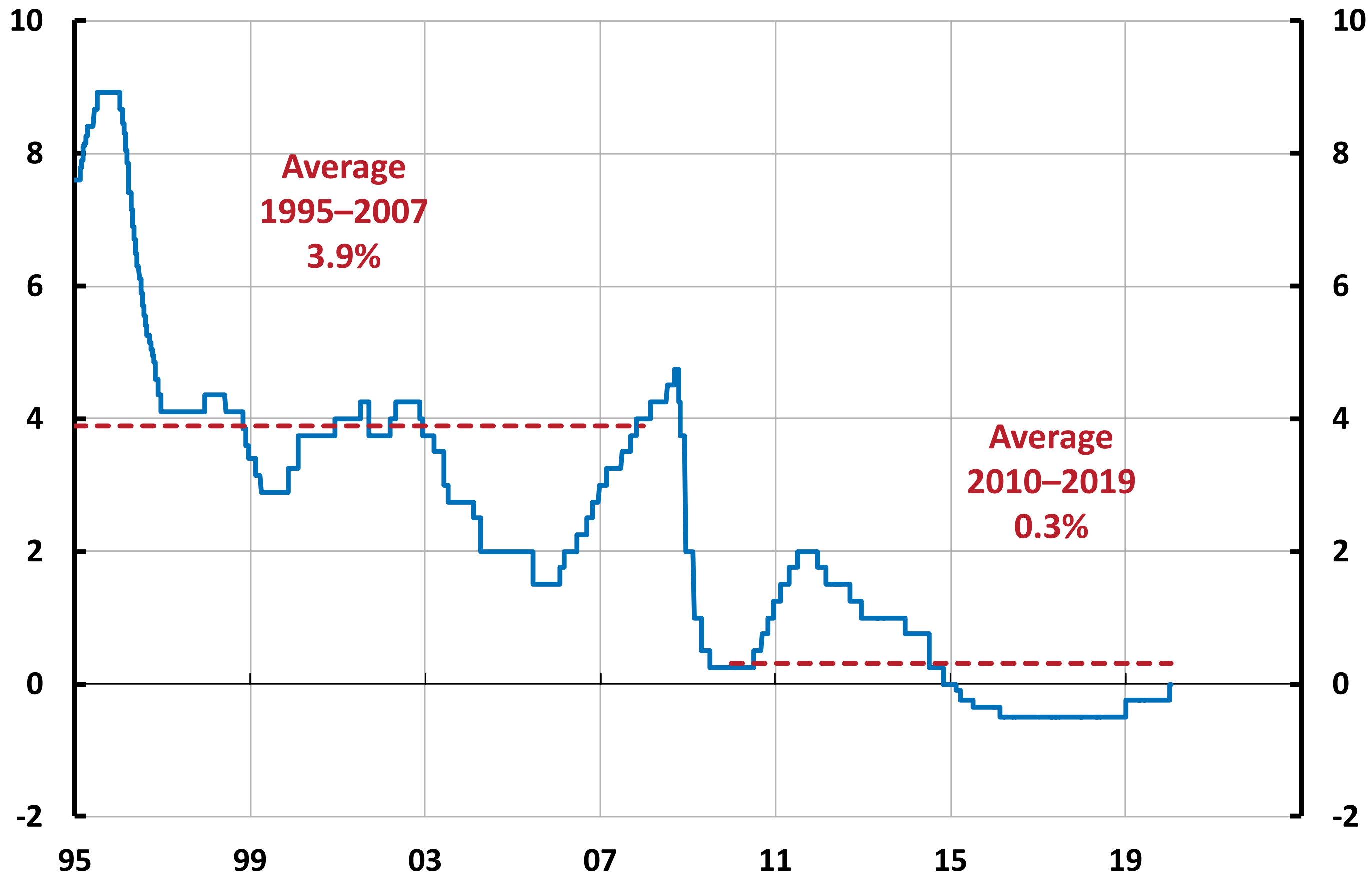


Per cent.

Sources: Statistics Sweden and the Riksbank

Monetary policy in a low interest rate environment

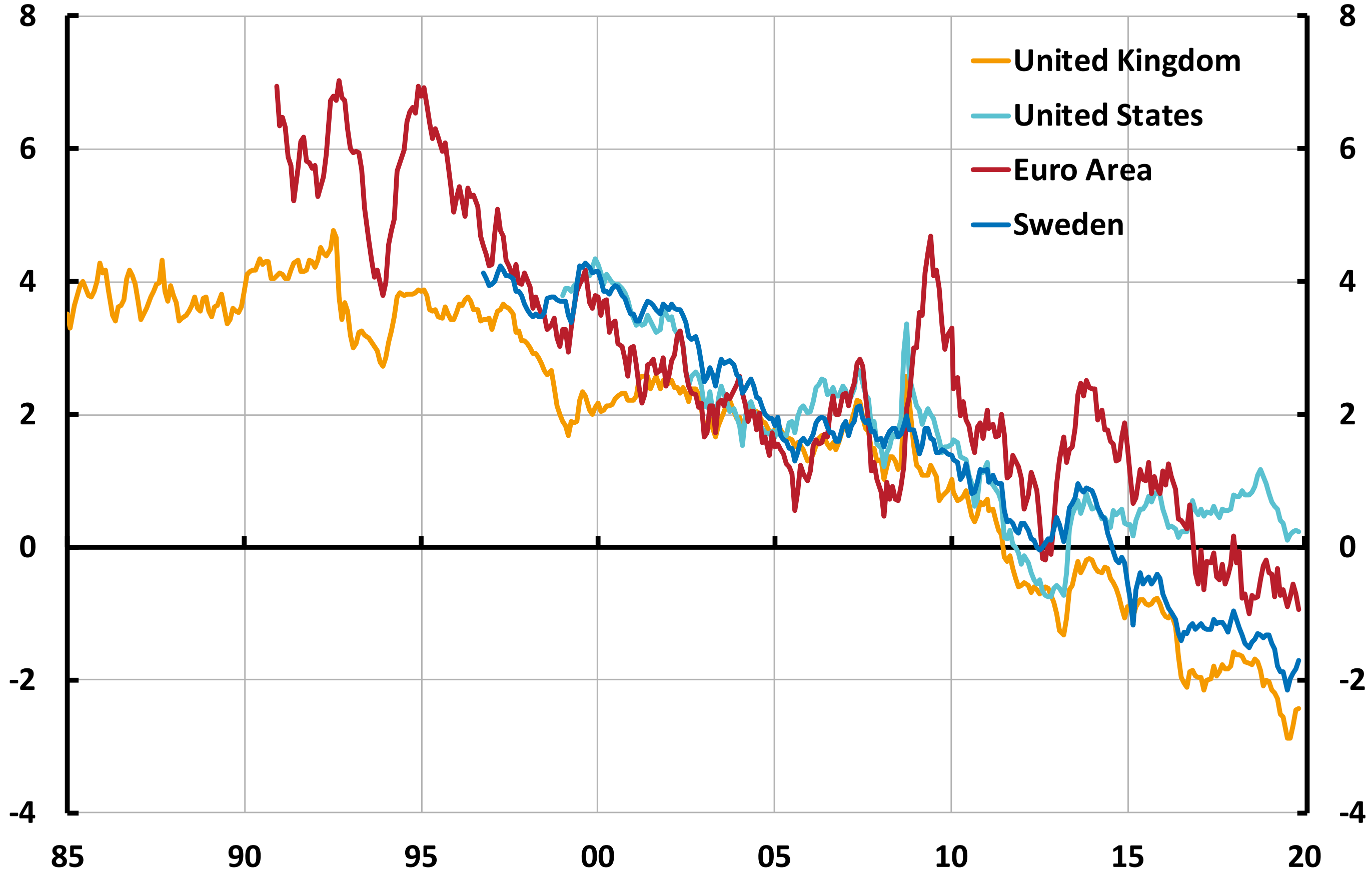
Policy rate still on low levels after the financial crisis...



Per cent.

Source: The Riksbank

...partly due to low long-term real interest rates

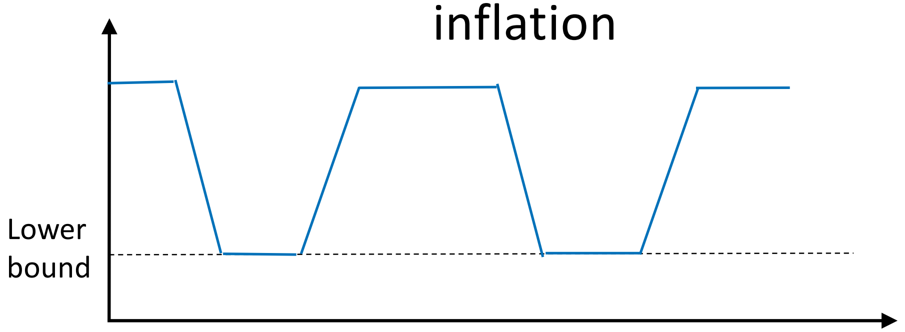


Per cent. 10-year real government bond yields.

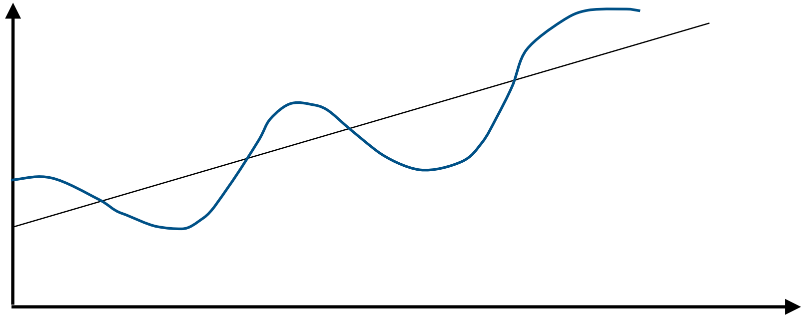
Sources: Bank of England, ECB, Federal Reserve and the Riksbank.

Low long-term policy rate and inflation are making it more difficult to counteract recessions

Normal policy rate and two per cent inflation



Economic development



Low long-term policy rate and inflation

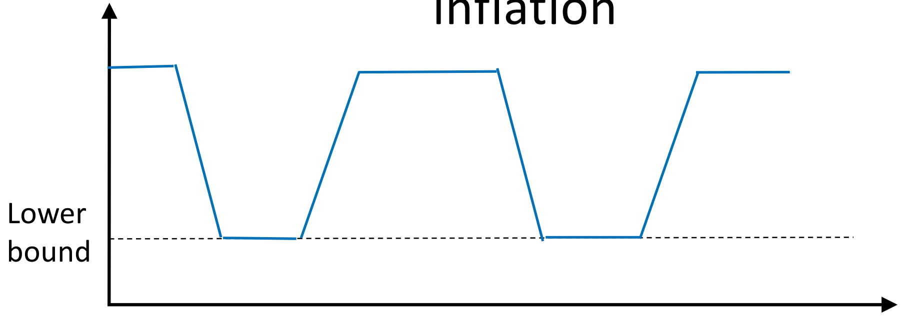
Economic development

Schematic illustration.

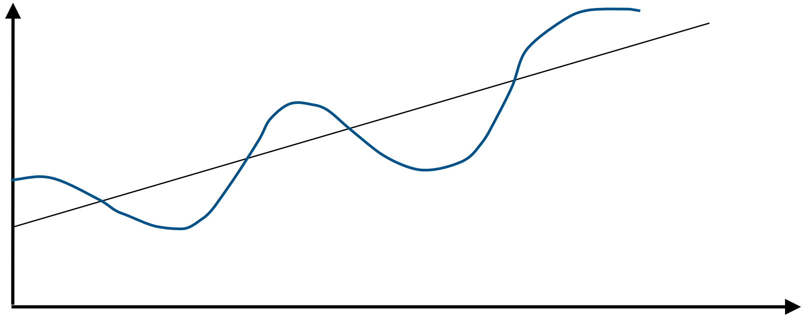
Source: The Riksbank

Low long-term policy rate and inflation are making it more difficult to counteract recessions

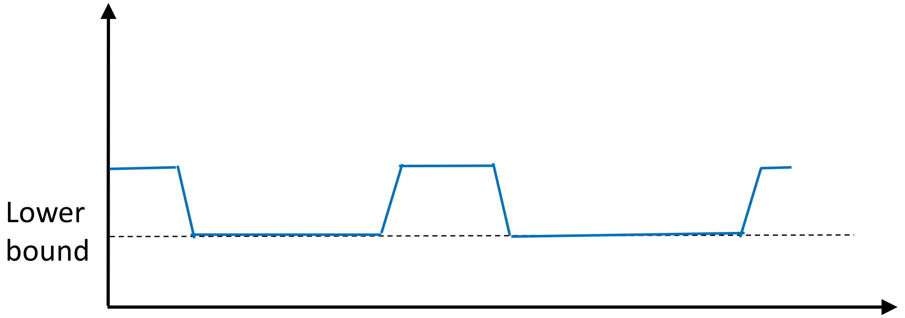
Normal policy rate and two per cent inflation



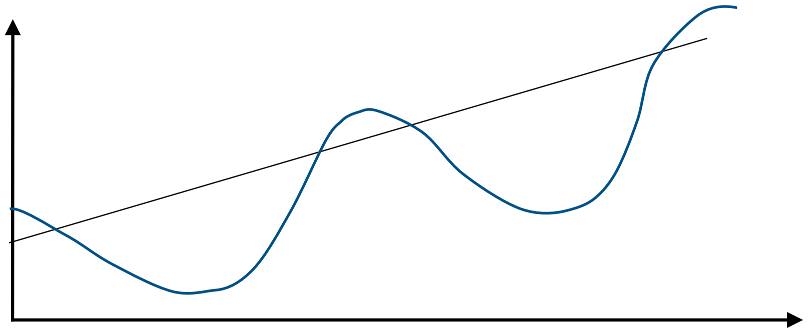
Economic development



Low long-term policy rate and inflation



Economic development



Schematic illustration.

Source: The Riksbank

The Riksbank does not lack tools

The policy rate can be cut

- But the policy rate is close to its **effective** lower bound
- Probably difficult to gain acceptance for negative rate on households' bank accounts

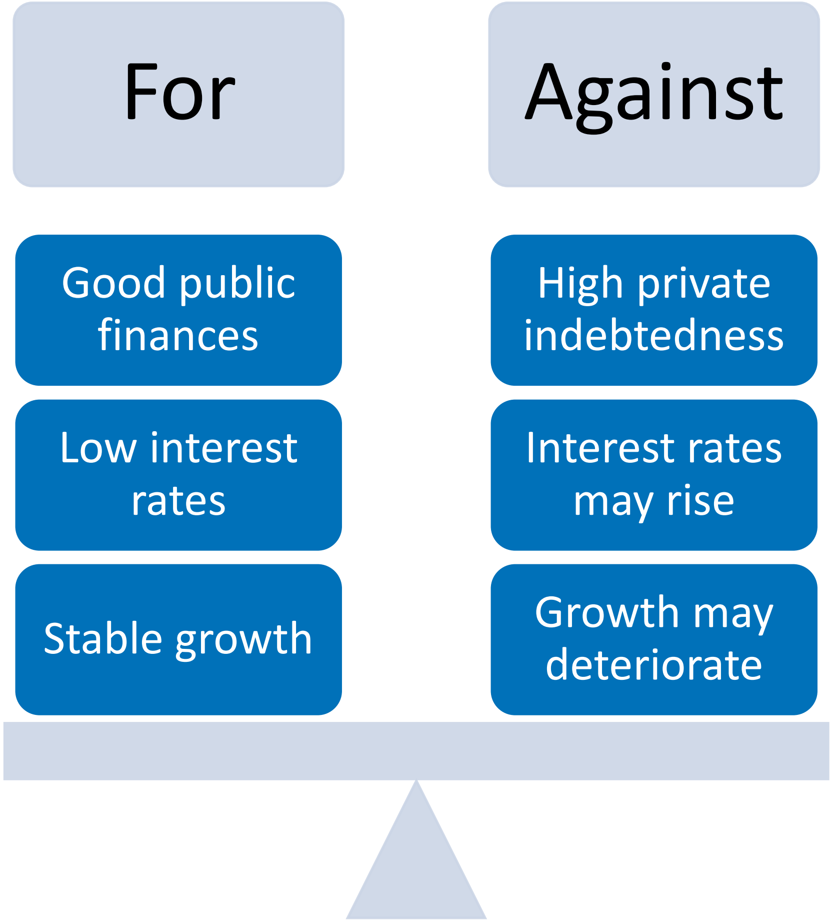
Purchases of financial assets

- **Government bonds:** But the Riksbank already owns a large share
- **Commercial papers** (mortgage and corporate bonds): But most effective for problems on a specific (systemically important) market

Affects expectations of future policy rates

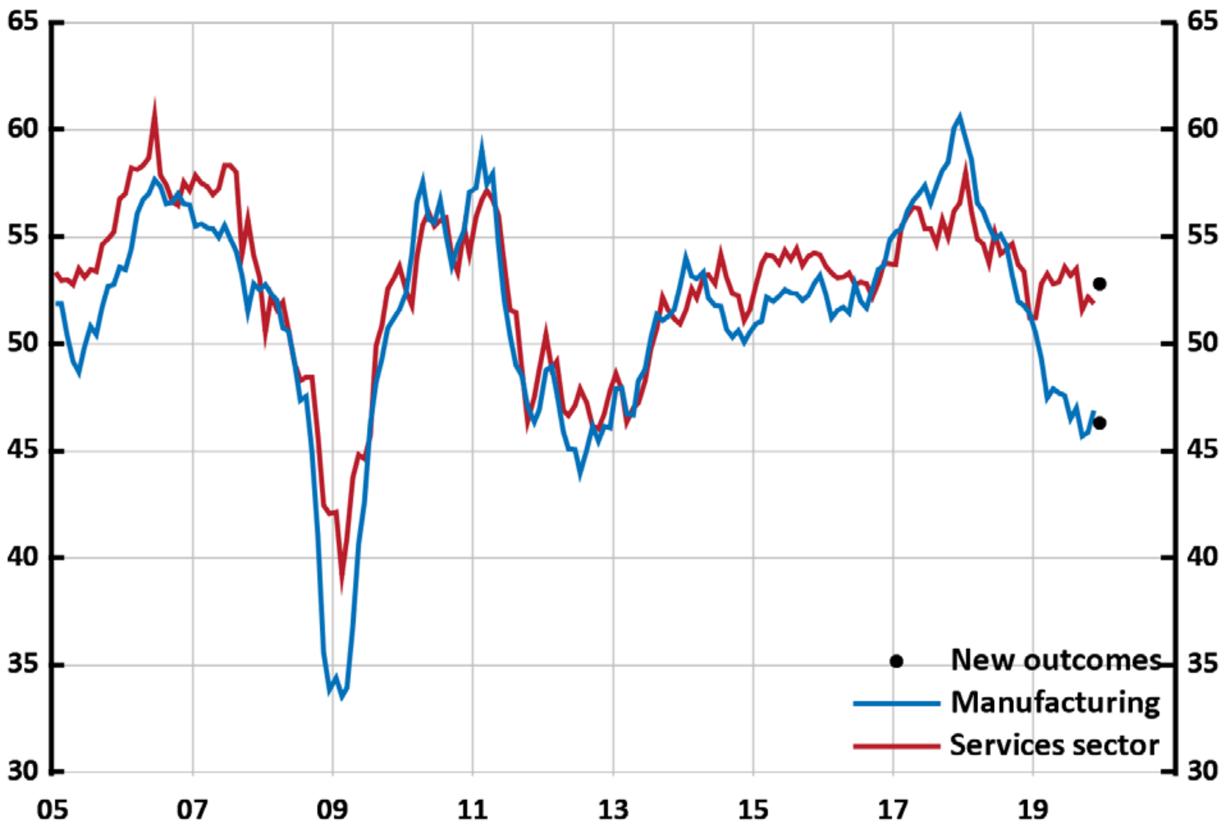
- The policy rate can remain at its lower bound longer

Larger role for – discretionary – fiscal policy?



Current monetary policy

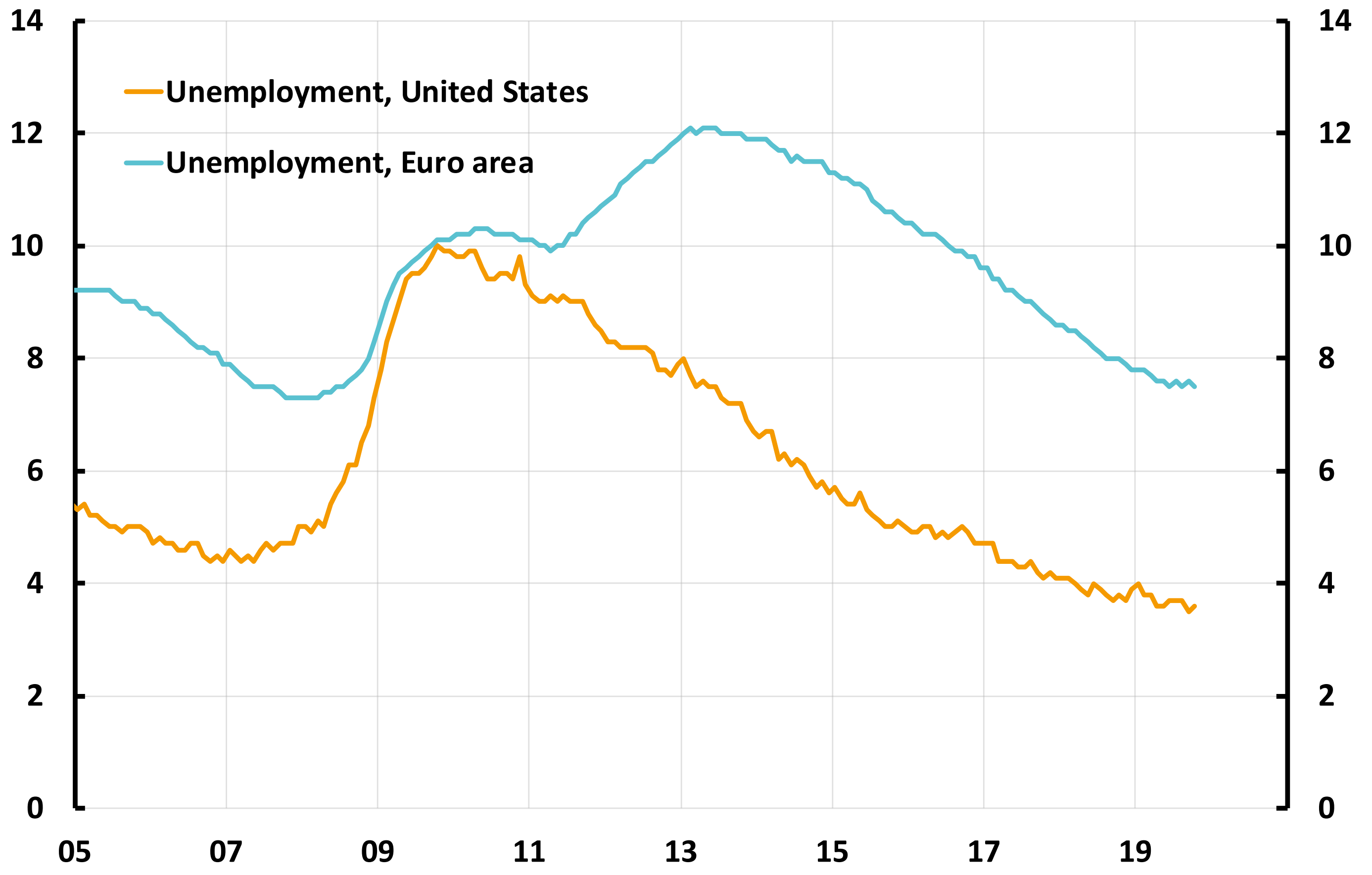
Global economic activity as expected in a calmer phase



Purchasing Managers' Index in the euro area.

Sources: Markit Economics

Low unemployment maintaining international demand



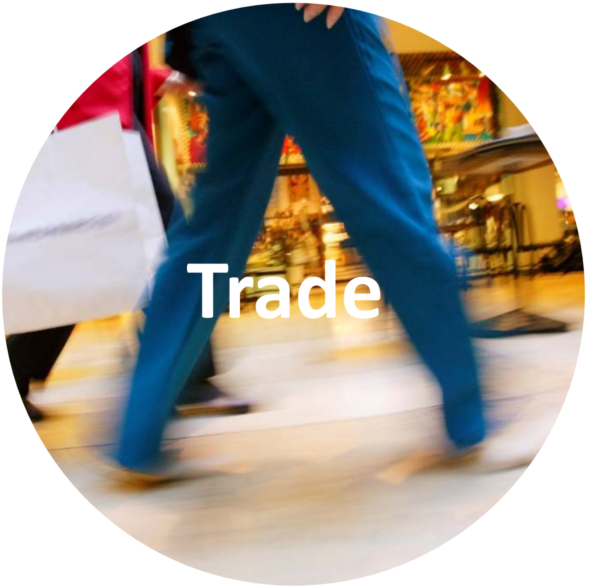
Per cent of labour force.

Sources: Bureau of Labor Statistics and Eurostat

Major Swedish companies on economic situation

“So far, we don’t expect any sharp economic downturn”

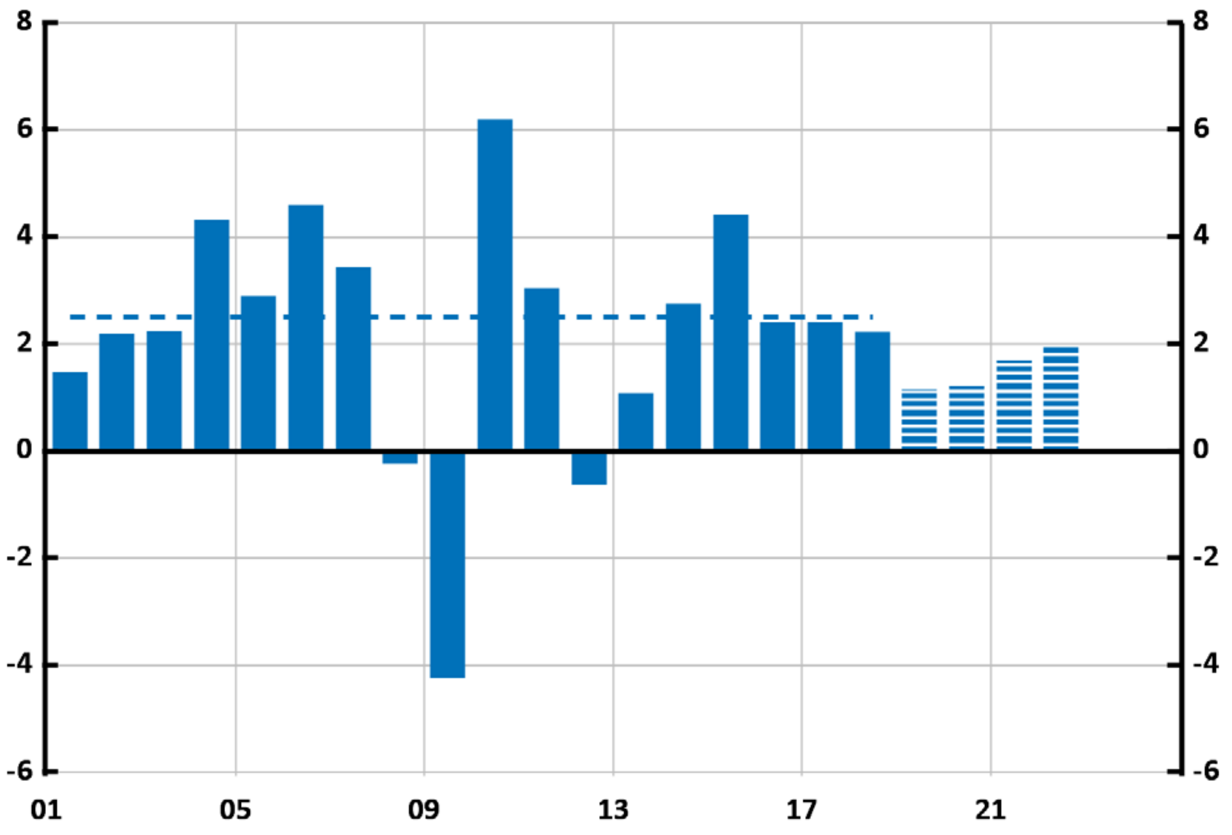
“It is not bad but not the same frantic pressure as before”



“More difficult than ever before to judge where things are heading”.

Quotes from the Riksbank’s Business Survey, November 2019

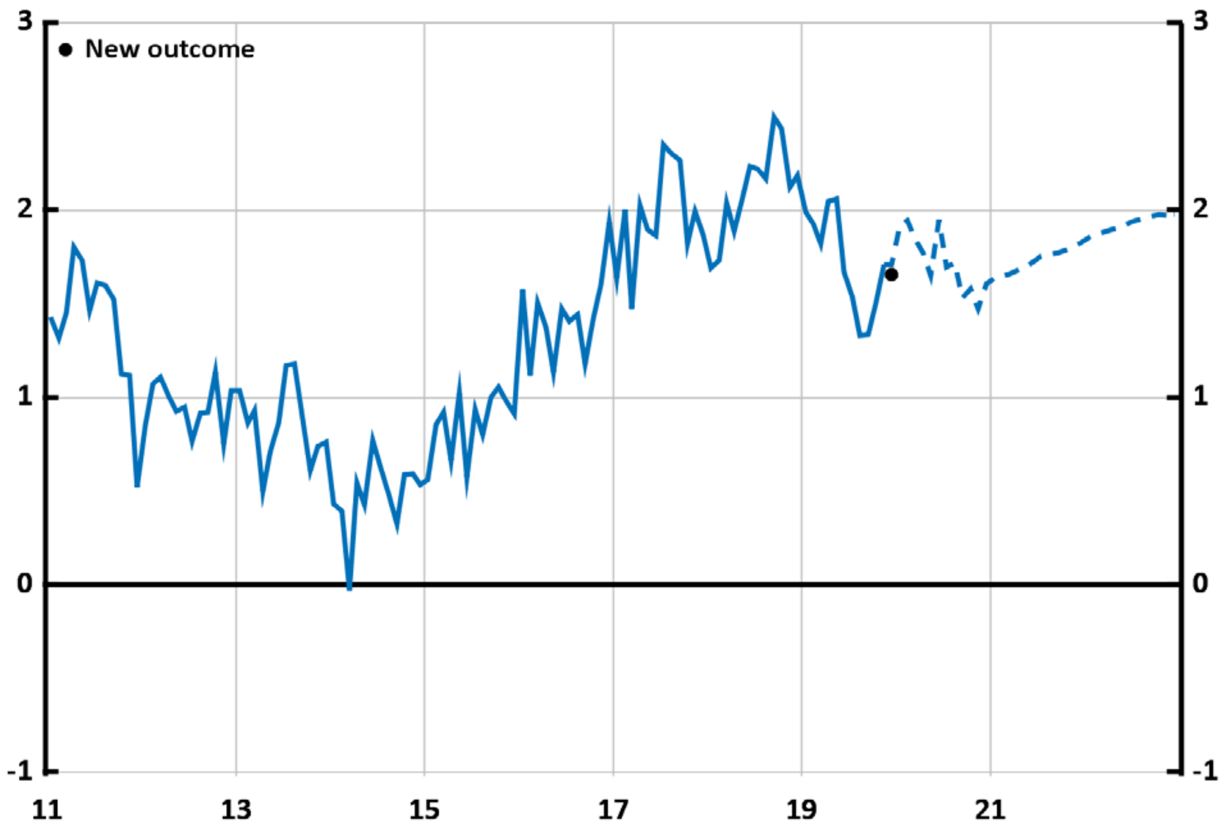
More normal economic situation – calmer growth



Annual percentage change.

Source: Statistics Sweden and the Riksbank

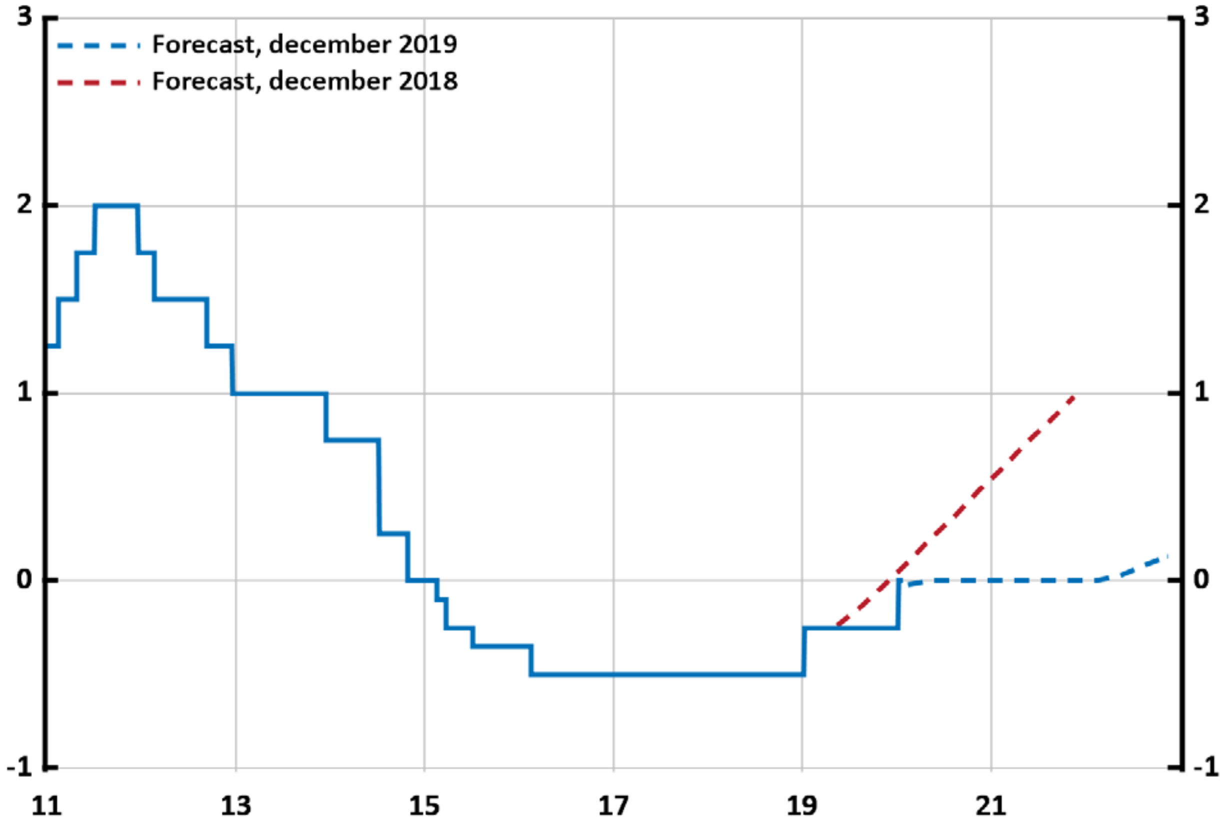
The inflation forecast from December still holds



Per cent. The broken line shows the Riksbank's forecast in December.

Sources: Statistics Sweden and the Riksbank

Monetary policy needs to proceed cautiously



Per cent.

Source: The Riksbank

Summary

- Inflation targeting regime still dominates globally. Lack of obvious alternatives.
- With limited ability to make an impact, the Riksbank needs access to a complete toolbox, including negative interest rate, bond purchases and direct lending to companies.
- Monetary policy cannot do the job alone.
  - Overall economic policy affects structural conditions for potential growth.
  - Micro and macroprudential policy prevent financial vulnerabilities.

Thank you!