SVERIGES RIKSBANK

Monetary policy minutes

April 2023

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

Summary

For inflation to fall and stabilise at the target within a reasonable period of time, the Executive Board decided to raise the Riksbank's policy rate by 0.5 percentage points to 3.5 per cent. The forecast indicates that the policy rate will probably be raised by a further 0.25 percentage points in June or September.

The members noted that inflation is still far too high and far from the target of 2 per cent. CPIF inflation has fallen since the monetary policy meeting in February, in line with the Riksbank's forecast, but this is explained entirely by falling energy prices. The members pointed out that inflation excluding volatile energy prices has become significantly higher than expected in recent months, and that the Riksbank's forecast has been revised upwards. Price pressures in early stages of the production chain have declined, which indicates that inflation will fall back, but the members emphasised that there is considerable uncertainty and that there is still a risk that inflation will become entrenched at a too high level. Several members raised the point that a stronger krona would be desirable in this situation.

Confidence in the inflation target among economic agents is essential for strong and sustainable economic growth. The members noted that long-term inflation expectations continue to remain stable close to 2 per cent. Members also stressed that the two-year collective wage agreements signed in the labour market, covering wage increases of 7.4 per cent, create predictability regarding company costs and clearly reduce the risk of a wage-price spiral.

The members also discussed the concern over certain international banks that led to large fluctuations on the financial markets in March and observed that renewed concern could entail tighter financial conditions.

Following the rapid policy rate hikes over the past year, monetary policy has a tightening effect on the economy and the members assess that after the April meeting there will be scope to adjust the policy rate in smaller steps. However, there is still considerable uncertainty and new information regarding the economic outlook and inflation prospects will be decisive for the conduct of monetary policy.

The members were unanimous that monetary policy needs to be tightened further and remain contractionary so that inflation falls back and stabilises at the target within a reasonable period of time. A majority of the members advocated a rate increase of 0.5 percentage points, and a forecast for the policy rate showing that it will probably be raised further by 0.25 percentage points in June or September. Two members instead advocated an increase in the policy rate of 0.25 percentage points and an interest rate path that indicates a high probability of further increases in June and/or September.

MINUTES OF MONETARY POLICY MEETING

Executive Board, No. 2

DATE:	25 April 2023
TIME:	09:00
INFORMATION CLASS:	ÖPPEN
PRESENT:	Erik Thedéen, Chair Anna Breman Per Jansson Martin Flodén Aino Bunge --- Bo Broman, Chair, General Council of the Riksbank Tomas Eneroth, Vice Chair, General Council of the Riksbank --- Mattias Ankarhem Vesna Corbo Charlotta Edler Paul Elger Mattias Erlandsson Anders Gånge Marie Hesselman Christina Håkanson Iida Häkkinen Skans Jens Iversen Henrik Lundvall Pernilla Meyersson Ann-Leena Mikiver Olof Sandstedt Åsa Olli Segendorf Maria Sjödin Ulrika Söderberg --- Robin Ahlén (§ 1-3a)

It was noted that Mattias Ankarhem and Paul Elger would prepare the draft minutes of the monetary policy meeting.

§3 a. Economic developments

Market developments since the last monetary policy meeting

Robin Ahlén from the Markets Department began by presenting the latest developments on financial markets. The period following the monetary policy meeting in February has been marked by high underlying inflation, concern over the banking sector and large shifts in expectations of central banks' policy rates.

The banking turmoil in the United States and Europe in March led to large market movements and lower interest rates, but the measures taken by governments, central banks and other authorities have meant that the market unease has declined and that willingness to take risk has returned, with rising stock markets and reduced credit spreads. On the other hand, expected volatility on the fixed-income market according to options pricing remains elevated, which reflects, for instance, the uncertainty regarding economic developments and monetary policy.

As the banking turmoil has declined, focus has once again shifted towards economic developments and inflation. This has meant that policy rate expectations have risen, primarily in Europe, which has contributed to higher government bond yields.

However, most central banks are expected to be approaching the end of their policy rate hikes and the central banks in Canada and Australia held their policy rates unchanged at their most recent meetings. Central bank members are continuing to emphasise the importance of incoming data.

Inflation has fallen and the labour market in the United States has begun to cool down, but is still tight, and the US central bank raised its policy rate by 0.25 percentage points in March and signalled a further increase before the summer. However, market expectations are not as high as they were prior to the banking turmoil, and the market is expecting interest rate cuts as early as the second half of the year. The United States also risks hitting the debt ceiling at some point during the summer, which has led, for instance, to higher costs to protect against suspension of payments. In Europe, underlying inflation has become higher than expected and the market is expecting further rate increases up to and including the summer in both the euro area and the United Kingdom.

The oil price fell after the outbreak of the banking turmoil, but recovered somewhat after the OPEC+ countries' decision to reduce oil production. All in all, however, the oil price is at similar levels as at the time of the previous monetary policy decision. Market-based measures of long-term inflation expectations in the United States and the euro have on the whole been relatively stable, at around 2.5 per cent.

The US dollar has weakened against the euro in step with, for instance, interest rate spreads relative to Europe declining. The Swedish krona (in KIX terms) is on the whole relatively unchanged since the previous monetary policy meeting.

Prior to the monetary policy decision in April, the analysts are expecting an increase of 0.50 percentage points, which is also in line with what market pricing indicates. After that, a further increase of at least 0.25 percentage points is expected, and market pricing indicates that the policy rate will be raised to around 4 per cent after the summer. No one is expecting any changes to securities sales at the moment. The main reason why the Riksbank is expected to continue raising the policy rate, and by more than was signalled at the February meeting, is that underlying inflation has become higher than expected.

Deputy Governor **Per Jansson** observed that the policy rate's development according to forward pricing had shifted downwards in connection with the banking turmoil, but that pricing since then has gradually shifted upwards again. He therefore wondered whether market expectations had stabilised now or whether there was still volatility in forward pricing.

Robin Ahlén replied that forward pricing has been stable recently.

First Deputy Governor **Anna Breman** mentioned that the Swedish krona had become marginally stronger, measured in terms of KIX, since the February monetary policy meeting. This is to some extent because the Norwegian krone, which has a heavy weighting in KIX, has weakened. Given this, she wondered what was the explanation for the weak Norwegian krone.

Robin Ahlén replied that there has been considerable focus on interest-sensitive economies and that foreign investors possibly regard the Norwegian krone as less liquid. He also noted that the weakening of the Norwegian krone is not explained by interest differentials.

Financial stability - current status and risks

Olof Sandstedt, Head of the Financial Stability Department, described the implications the recent banking turmoil has had on the Swedish financial system, the situation on the housing market, the financing situation for companies and the risks to corporate bond funds. The financial system still faces major challenges and the risks to financial stability in Sweden have increased over the past year.

The bank collapses during March in the United States and Switzerland created considerable uncertainty and increased volatility on the capital markets. However, after large state government measures, the market unease has declined. The Swedish banks were mainly affected through falling equity prices and slightly higher financing costs, but this development was reversed somewhat in April. The resilience of the Swedish banking sector is assessed as good, but the exposure to highly indebted commercial property companies and households still comprises a risk.

Households are under pressure from various directions and housing prices have continued to fall during the spring, but at a slightly slower pace than before. The downturn so far (March) is just over 13 per cent from the peak in February 2022 (seasonally-adjusted). In addition, households are interest-rate sensitive and highly indebted. The vast majority of mortgagors are expected to be able to keep up with their debt payments, but some households may have problems paying their mortgages. This applies especially to households with loans for consumption. If costs remain high for a prolonged period, households' resilience will deteriorate, with significant effects on consumption as a result.

Higher costs and lower demand have led to company bankruptcies continuing to increase during 2023. The Riksbank expects this trend to continue. Property companies are particularly vulnerable in the current environment as they have large loans and are interest-rate sensitive. An increasing number of property companies are facing difficulties in refinancing themselves on the bond market and are to a greater extent choosing to finance maturities with extended bank loans from Nordic banks. Rising interest rates mean that the value of properties falls, which has so far taken place in an orderly manner, however. However, the possibility of property values falling faster and substantially cannot be ruled out, if for instance many property companies are forced to sell larger volumes of property or if there is a credit crunch in the Nordic banks. The property companies are taking measures to manage the prevailing market situation, but more will be needed.

The prevailing market situation, with rising interest rates and uncertain growth prospects, can also affect attitudes to risky assets, such as corporate bonds, in the period ahead. Swedish corporate bond funds therefore remain vulnerable to large outflows if risk appetite suddenly changes.

The current monetary policy drafting process – new data and forecasts

Henrik Lundvall, Advisor at the Monetary Policy Department, presented economic developments since the monetary policy meeting on 8 February, and the monetary policy measures that the Monetary Policy Department judged would gain majority support in the Executive Board at today's meeting. The background material for today's decision has been discussed by the Executive Board at meetings on 8 March and then 4, 5 and 17 April. The draft Monetary Policy Report was discussed and tabled at a meeting of the Executive Board on 19 April.

The focus during the drafting process has been on the development of inflation and interest rates in Sweden and abroad. The prospects for inflation in Sweden during the coming year are analysed in an article in the draft report. Another important question has been the turmoil on the financial markets that arose in March in connection with the bank collapses in the United States and Switzerland, and the assessment of how the turmoil has affected, and will affect, credit granting and demand. Considerable attention has also been paid to the collective wage agreement signed in Sweden in March between the social partners in industry and the agreements in other sectors that were signed in April. The consequences of the financial unease and the central wage agreements are an example of factors that have been important when analysing the economic outlook and inflation prospects in Sweden.

Inflation is still high, both in Sweden and abroad, but falling energy prices are slowing down the rate of price increase. In the United States, which is ahead of Europe and Sweden with regard to the development of inflation, the rate of price increase excluding energy prices has fallen somewhat, although it is still high. Underlying inflation in the euro area and Sweden is even higher, and here there are as yet no signs of a clear downturn. In Sweden, prices measured in terms of the CPIF excluding energy rose significantly faster during the first months of the year as compared to the forecast in the February Monetary Policy Report.

As described in the draft report, there are several reasons to expect inflation to fall. In the draft forecast, however, inflation in both the euro area and the United States has been revised up in relation to the forecast made in February. The forecast for the KIX-weighted policy rate abroad has been adjusted up marginally.

The fact that the KIX-weighted policy rate has not been adjusted upwards more is largely due to how the banking turmoil affected economic prospects for the US economy. During the weeks following the monetary policy meeting in February, market expectations of the Federal Reserve's policy rate rose substantially, given the incoming data and the Federal Reserve's communication. This development was more than reversed at the beginning of March, when customers, investors and counterparties lost confidence in a couple of US banks, including the Silicon Valley Bank. As Robin Ahlén has already described, the problems in the US banking sector created considerable uncertainty regarding future interest rates, and the unease on the financial markets also spread to Europe, where for instance the Swiss bank Credit Suisse was in focus. In both the United States and Switzerland, governments, central banks and other authorities concerned acted fast and took far-reaching measures to prevent the turmoil from spreading to other companies in the financial sector. After that, the market's valuation of US and European banking shares also stabilised. All in all, market agents are expecting that the banking turmoil will contribute to the Federal Reserve holding the policy rate somewhat lower than was expected at the beginning of March. Tighter credit conditions in the United States are expected to nevertheless dampen demand somewhat and thus contribute to the downturn in inflation.

The banking turmoil thus affects the assessment of the global economic outlook and so does households' reduced room for consumption. The high inflation is an important factor holding back households' real disposable incomes, and moreover the effects of the monetary policy tightening are gradually become clearer. In the draft forecast, GDP growth abroad is subdued this year, which also affects the economic outlook for Sweden. Following a relatively high level of activity in the Swedish economy last year, when GDP grew by 2.6 per cent, several indicators are now pointing to developments being much weaker this year. In addition to the high inflation, domestic demand is weighed down by weak consumer confidence, increasingly high interest expenditure and a continued weak development of the housing market. The picture of macroeconomic developments in Sweden is not merely gloomy. Exports have grown rapidly and in the draft forecast they continue to provide a positive contribution to GDP growth. Resource utilisation is assessed according to several indicators to currently be somewhat higher than normal. On the labour market too, developments have been unusually strong. However, as GDP falls in the coming quarters, the employment rate is expected to gradually fall and unemployment to rise.

Lower energy prices have contributed to CPIF inflation having fallen back somewhat at the beginning of the year, in line with the Riksbank's forecast from February. However, underlying inflation has remained surprisingly high. CPIF inflation excluding energy was 8.9 per cent in March and so far no clear sign of a downturn is visible in the monthly rates of price increase on goods and services. The surprisingly high underlying inflation shows uncertainty regarding how long the high inflation will last, something that is illustrated by two scenarios in the draft report.

Although there is considerable uncertainty, inflation is expected to fall clearly this year. The reasons for this are discussed and analysed in an article in the draft report. This illustrates, for instance, the developments in a long line of indicators pointing to increasingly subdued price pressures in the producer stage. Declining supply disruptions, tighter monetary policy and lower demand are expected to continue to dampen price pressures going forward. In this context, the collective wage agreements of increases over two years totalling just over 7 per cent signed by the social partners at the end of March should also be mentioned. The agreements do imply a total rate of wage increase that is somewhat higher than the Riksbank's forecast in February. But they also entail less risk of a problematic wage-price spiral arising in the Swedish economy. There are thus, all in all, several reasons to expect that inflation will fall back and the forecast is for CPIF inflation to reach the target of 2 per cent next year. As a result of the low energy prices, CPIF inflation will fall faster than underlying inflation, but CPIF inflation excluding energy will also stabilise close to the target in 2024.

The forecasts are based on the monetary policy that the Monetary Policy Department judges will gain a majority in the Executive Board at today’s meeting. This means that the policy rate is raised from 3.0 per cent to 3.5 per cent at today’s meeting. The draft forecast is for the policy rate to remain at a level somewhat over 3.5 per cent for the remainder of the year and cuts to the rate begin only when underlying inflation has fallen back and been close to the target for a time. At the end of the forecast period, the policy rate is expected to be 3.4 per cent. The draft forecast is also based on the Riksbank's holding of securities continuing to decline through maturities and through the sales of government bonds as decided on in February. On the assumption of sales of government bonds for SEK 3.5 billion every month, and of other bonds being kept until maturity, the asset holdings will amount to just below SEK 200 billion at the end of the forecast period.

§3b. The economic situation and monetary policy

Deputy Governor Aino Bunge:

I support the assessments and forecasts made in the draft Monetary Policy Report, and I support the proposal to raise the policy rate by 0.5 percentage points to 3.5 per cent, as well as the interest rate path.

I concluded my contribution in February by looking forward to this meeting and noted that we are living in uncertain times. But I also noted that, by this date, we would have access to a large amount of important new information, including three inflation outcomes and a new business survey. I also expressed the hope that we would have a clearer view of the wage bargaining rounds. My overall assessment today is that the policy rate needs to be raised further. I have chosen to justify my position by taking the information that has arrived since February as a starting point.

When it comes to inflation, we can note that outcomes for January, February and March for our target variable, the CPIF, were relatively close to our forecast. However, the recent development of inflation is illustrated clearly by Figure 37 in the draft report: for the first time in a long while, energy prices are no longer contributing to CPIF inflation. The figure also makes clear that the contribution made by other factors, particularly services, remains high. The four-quadrant chart in Figure 40 shows that it is precisely the downturn in energy prices that is driving the cooling down of CPIF inflation. In March, inflation measured in terms of the CPIF excluding energy was 1.4 percentage points higher than our forecast in February. My conclusion is thus that inflationary pressures remain very high in the Swedish economy and we have not seen the clear downturn in underlying inflation that we forecast in February.

The Riksbank's Business Surveys also form an important part of our assessments. For example, the survey at the start of last year showed some of the first signs of a clear change in companies' pricing behaviour towards an increased inclination to raise prices.[1] One year later, it is too early to say whether any substantial change in the opposite direction is under way. It is more a question of marginal differences: price increases are continuing, but discounts are becoming increasingly common. The manufacturing sector is significantly more satisfied with the economic situation than the trade sector, and the construction sector is signalling larger problems than other sectors.[2]

We have also got a new Industrial Agreement and benchmark for the wage bargaining rounds. Even though the level is slightly above our forecast, in my view it considerably reduces the risk of a wage-price spiral in the Swedish economy. One important reason for this is that the agreement stretches over two years. However, the agreement also reflects confidence in the inflation target. In general, we can also see that inflation expectations remain close to target in the medium term, which is a vote of confidence that the Riksbank now has to live up to. There will be no return to real wage growth for Swedish wage earners until inflation returns closer to the target.

So far, I have discussed the new information that, at the last meeting, we expected to have received by this point in April. One development that we had not envisaged, however, was the banking turmoil that flared up in March in conjunction with the problems in Silicon Valley Bank. The turmoil rapidly spread to Europe, primarily in the form of problems for the Swiss bank Credit Suisse. Recently, the situation on the global financial markets has become significantly calmer, largely due to forceful interventions by central banks and governments, the long-term effects of which we shall now have to analyse.

Over the last year, the Riksbank has warned of the uncertainty existing over how economic agents are being affected by the rapid rise in interest rates. The banking turmoil is a sign that interest-rate sensitivity may exist in different parts of the economy and financial sector: Silicon Valley Bank and Credit Suisse were essentially very different types of bank that both experienced difficulties. For Sweden's part, the banking sector is comparatively strong with relatively strong

[1] See "I've never before experienced customers accepting price increases so easily", *The Riksbank's Business Survey*, February 2022, Sveriges Riksbank.

[2] See "Price increases continuing, but discounts increasingly common", *Riksbank's Business Survey*, February 2023, Sveriges Riksbank.

capitalisation and large liquidity buffers. At the same time, the contagion effects of the turmoil abroad demonstrate the importance of transparency on risks when it comes to building and maintaining confidence. One risk that both the Riksbank and Finansinspektionen have long highlighted is the highly-leveraged commercial property sector, which requires continued careful monitoring. Overall, I agree with the assessment in the draft report, namely that the banking turmoil has itself led to some tightening but that the signs have been much clearer in the United States than in Sweden. However, as the draft mentions, there exists the risk of greater financial tightening in the event of renewed turmoil.

I shall now share some of my thoughts on future prospects. Over the last year, Swedish household demand and consumption has, if anything, surprised on the upside, even though interest expenditure has increased substantially. One change that may have been more lasting than expected is that travel and restaurant visits, which were restricted during the pandemic, are being prioritised more than previously. The view that households are trying to maintain consumption is confirmed by Statistics Sweden's Financial Accounts, which show that households have cut back on their liquid savings in assets such as deposits, listed shares, mutual fund shares and private insurance savings, with total net withdrawals amounting to SEK 30 billion in the fourth quarter.[3] However, when rate rises have an increasing effect, a reduction of consumption will eventually become more or less unavoidable for many households. Between the second and fourth quarters of last year, consumption fell by about two per cent. The forecast in the draft report of continued falling consumption in the period ahead therefore seems reasonable. But there is considerable uncertainty. At the Riksbank, we have long highlighted the need for statistics over the distribution of savings among households and this is an example of when such statistics would have been useful.

As regards inflation, I believe that there still remains considerable uncertainty over future developments. Apart from factors such as sharply rising energy prices and imbalances between supply and demand after the pandemic, an important additional explanation for last year's rapid rise in inflation is the changed pricing behaviour among companies.[4] There is also great uncertainty over this going forward and it is too early to say whether the problems with inflation are now over. However, as the draft report describes, there exists simultaneously the possibility that pricing behaviour may change again, when demands falters and prices for energy and input goods become lower. Historical data indicates that, in normal times, prices are not cut to any great extent when costs fall. However, the

[3] See Statistics Sweden's statistical news concerning the Financial Accounts, fourth quarter 2022 "Households sold off assets to finance increased costs", Statistics Sweden.

[4] See "Account of Monetary Policy for 2022", March 2023, Sveriges Riksbank.

current situation is far from normal and there are now some signs of cut prices in the food sector and elsewhere.

My overall assessment is that we continue to have inflation that is far too high and that is not showing strong enough tendencies towards cooling off. I therefore consider that further monetary tightening is needed and that the policy rate should be raised by 0.5 percentage points now, with a relatively high probability of a further raise of 0.25 percentage points in June or September. It is really important for confidence in the inflation target that inflation falls clearly this year. There will not be any scope for a possible policy rate cut, as indicated by the interest rate path, until underlying inflation has been close to target for some time. The path also clearly indicates the expectation that this is some way ahead.

Finally, I would like to comment on the Swedish krona and our securities holdings. At the end of February, we decided to sell government bonds with longer maturities and to increase the amount of Riksbank Certificates. Further supplies of Swedish government bonds, together with the increased issuance of Certificates would also increase the supply of safe Swedish assets and could thereby have a strengthening effect on the krona exchange rate. Sales of government bonds started in April and have proceeded according to plan. The planned reduction of the securities holdings should be characterised by predictability and I support keeping it unchanged until further notice. At the same time, it is important to continue to point out that a weak krona has a negative effect on our efforts to fight inflation.

Just like at the last meeting in February, I would like to conclude by looking forward to the next monetary policy meeting, which will take place on 28 June. My hope is that the overall information we have then confirms that inflation has clearly started on its downward path towards the target. But this forecast is being made on the assumption of a tighter monetary policy.

Deputy Governor Martin Flodén:

At our last monetary policy meeting, in February, we raised the policy rate to 3 per cent and indicated that we would increase the rate by another 0.25 or 0.5 percentage points today. Although CPIF inflation has since then developed more or less in line with our forecast, underlying inflation has become much higher than we expected. Measured as the CPIF excluding energy, inflation was 8.9 per cent in March, a full 1.4 percentage points higher than our forecast in February.

In light of inflation being far above our target and of price increases in recent months having been so much higher than our forecast, it would seem natural to raise the policy rate more than we previously indicated. This would indicate a rate increase of at least 0.5 percentage points today.

But I nevertheless advocate that we raise the policy rate only by 0.25 percentage points today. A combination of three main factors lead me to consider this to be the most appropriate decision.

In brief, my argument is that monetary policy needs to continue to be tightened, but that we are probably approaching the endpoint for rate rises. And developments in recent months give us the opportunity, nevertheless, to proceed more cautiously with rate increases. Let me elaborate on this reasoning.

First, we see that domestic demand is weakening rapidly. Our new forecast implies that growth in both household consumption and business investment will be very weak this year and next year. In addition, the forecast for these variables is significantly weaker than our assessment in February. To some extent, this weaker development can be explained by the somewhat tighter monetary policy behind our new forecast, but it is my assessment that the monetary policy I advocate would also lead to weaker development in these variables than in the February forecast.

The forecast for GDP and employment provides a slightly different picture of the economic cycle as the development in both variables has been stronger than expected at the beginning of the year. The weak exchange rate in combination with falling real wages is probably contributing to relatively strong development in the export sector and to high employment. This leads to questions as to which components of GDP have the greatest effect on inflation and how we should interpret measures of resource utilisation based on GDP or employment (like the indicators in Figure 36 in the draft Monetary Policy Report). My assessment is that household consumption in particular but also business investment are of greater significance for inflation than the export industry. And I also assess that the weak development in these variables, even with the monetary policy I advocate, will contribute to a rapid decline in inflation over the coming year.

Let me express this argument in a different way: The most important channel through which monetary policy works is via the effects of the interest rate on consumption and investment. We see signs that inflationary pressures are higher than we previously thought. This means that we need to cool the economy more – that consumption and investment need to be weaker – than we previously judged. We seem to be able to achieve this with a slightly smaller rate hike than the one proposed in the draft report.

Second, we still see, and now even more clearly, that inflation expectations and wage formation are compatible with the inflation target of two per cent. Various measures of long-term inflation expectations are stable at a favourable level. Even more important is that two-year wage agreements in several important sectors have been concluded on levels that are moderate in relation to inflation. In addition, consumers are putting increasing pressure on companies that rapidly increase their prices. Despite the continued strong development in the labour market, I therefore think that the risk of wages in the near time trying to catch up with the rapid price increases over the past year has decreased significantly. With limited wage increases, it will not be sustainable to continue to rapidly increase consumer prices.

One may also think that the gap that has opened up when consumer prices have risen much more rapidly over the past year than nominal wages needs to be closed, and that it is now increasingly likely that this will happen by the prices of certain goods and services that have increased rapidly being adjusted downwards rather than wages starting to rise faster. This argument is reinforced by several commodity and producer prices that have previously risen rapidly having now fallen back significantly.

Third, we need to consider the recent turmoil in international financial markets, linked in particular to problems in certain foreign banks.

We know from before that the Swedish economy is interest-rate sensitive. Both households and companies are highly indebted with short interest-rate fixation periods. The Riksbank's rate hikes therefore mean that cash flows will rapidly deteriorate for many households and companies. Household consumption, housing construction and the commercial property sector are therefore expected to be substantially affected, and more in Sweden than abroad despite the Riksbank’s rate rises being smaller than abroad.

The interest-rate sensitivity of the Swedish economy is a problem for at least two reasons. First, it leads to the Riksbank's monetary policy having an unbalanced impact on the economy. Some sectors are affected very negatively by a monetary policy that needs to be adjusted to the development of the economy as a whole. Second, it leads to the krona depreciating as the Riksbank achieves the same tightening of the real economy with smaller rate rises than in other countries.

But the problems in foreign banks show that other economies are also interest-rate sensitive. The difference is perhaps that it is not always clear where other countries’ interest-rate risk and interest-rate sensitivity are, and where the effects of rate increases will emerge.

Regardless of this interpretation, we now see that the expectations of foreign central banks’ rate rises, particularly those of the Federal Reserve, have fallen.

This also has an effect on the Riksbank's monetary policy. At a given level of the Swedish policy rate, there will be less pressure on the krona exchange rate.

It is also conceivable that the turmoil on financial markets itself is contributing directly to a tightening of the cyclical position via tighter financial conditions, where banks, for example, become more restrictive in their lending. However, in a main scenario, this effect would seem at most to be small in the Swedish economy. Our banks appear to have already taken into account the effect of rate increases on households and commercial real estate companies.

In my view, these three factors together therefore suggest that, despite high inflation outcomes in recent months, we should be content with an increase in the policy rate of 0.25 percentage points today. However, this does not mean I am convinced that the monetary policy proposed in the draft report will be too contractionary. It is not unlikely that this monetary policy will work well and prove to be correctly formulated.

I am advocating a smaller increase today because I also see a certain, not insignificant, probability that in the months up until our next monetary policy meeting, we will see clear signs of underlying inflation having really started to fall rapidly in combination with continued weak domestic demand, and we can then consider a policy rate of 3.25 per cent to be sufficiently high. In this situation, when the risk of a wage-price spiral has abated, there is scope to take smaller steps with our rate increases.

Market expectations are that the rate will be raised by 0.5 percentage points today. An increase of 0.25 percentage points would probably cause the krona to depreciate, at least in the near term. And this would in turn exert more upward pressure on inflation via import prices. I see this as the strongest argument against the monetary policy strategy I am advocating. But it is not obvious that the krona would benefit from larger rate increases if these result in a too rapid slowdown in the Swedish economy.

Pricing in the financial markets indicates that central banks are expected to start to reduce their policy rates already this year or early next year. This is not the path I see for the Riksbank's policy rate, especially not if it is now raised in smaller steps and the krona then depreciates further. It will then be more likely that the rate will need to continue to be raised going forward, or that it will at least take longer before it is appropriate to cut the rate. This understanding should gradually provide some support to the undervalued krona.

Another risk is that an unexpectedly small rate increase could be seen as the Riksbank having changed its policy rule and now attaching less importance than before to fighting inflation. This risk cannot be brushed aside entirely, but with the right communication, I believe it can be managed. Against this background, I wish to point out that fighting inflation is still my number one priority. If developments up until the next monetary policy meeting do not move clearly in the right direction quickly enough, the policy rate will need to be raised further. I therefore advocate a rate path indicating that an additional increase of 0.25 percentage points at the June meeting is probable, but that the rate may also be increased by 0.5 percentage points or not raised at all.

More precisely, I advocate a rate path standing at 3.45 per cent during the third quarter this year and then at 3.5 per cent until this path coincides with the rate path in the draft report.

As everyone realises and has noticed recently, it is uncertain how the policy rate will develop from meeting to meeting. Over the past year, we have consistently been surprised by both the power of the inflation upturn and the resilience of the economy to the combination of rate hikes and rapidly rising energy prices, and we have had to adjust monetary policy to this. Even going forward, we need to adjust monetary policy to new information on how interest-rate sensitive the economy is, how rapidly demand softens and how inflationary pressures are then affected.

And the forecast for the policy rate several years ahead is of course associated with even greater uncertainty than the short-term forecast. If confidence in the inflation target remains, the interest-rate trend will in the longer term be determined mainly by global, and difficult-to-assess, drivers of saving and investment. The important message conveyed by the rate path is that the Riksbank's monetary policy tightening will need to be sustained. Despite inflation being projected to fall rapidly this year, we expect it to remain at unusually high levels for some time, even measured at monthly rates (see Figure 47 in the draft report). Monetary policy needs to remain contractionary until we are convinced that inflationary pressures and companies' price-setting behaviour are compatible with inflation sustainably close to the target.

In conclusion, I would like to return to my reasoning about economic activity. For inflationary pressures to ease substantially and quickly enough, economic activity must be held back. We are already seeing clear signs that this has started to happen, and our assessment is that domestic demand will continue to weaken. I judge that the monetary policy I am advocating would also lead to a development where GDP growth becomes lower in Sweden than abroad, and that domestic demand will be even weaker than GDP. One may therefore argue that monetary policy is more contractionary in Sweden than in, for example, the euro area despite us having set policy rates at approximately the same level. If our picture of the economy proves to be too pessimistic, it is likely that inflationary pressures going forward will remain at a high level too long and that we will then need to set a higher policy rate than the one I have advocated today.

First Deputy Governor Anna Breman:

In the space of a year, we have raised the policy rate from zero to three per cent. We have also started quantitative tightening through the sale of government securities and by completely ceasing reinvestment of maturing bonds. Monetary policy is now significantly contractionary and we can see it starting to have an effect on the Swedish economy and inflation.

Inflation measured using the CPIF, our target variable, has fallen by over 2 percentage points since the last monetary policy meeting. It is important that this downturn continues and that underlying inflation also falls. The prospects for this are good. Swedish companies are now faced with a fall in prices of many input goods (see, for example, Figures 41 and 45 in the draft Monetary Policy Report). The wage bargaining rounds have been marked by responsibility and restraint. Long-term inflation expectations are still firmly anchored close to the target. However, these good prospects should be weighed against the facts that inflation remains far from target and underlying inflation has been significantly above our last forecast.

In light of this, I support raising the policy rate but I do not support raising it by 0.5 percentage points. Instead, I advocate an increase of 0.25 percentage points and a path that indicates further gradual increases in June and/or September. This would allow us to keep our options open for other courses of action later in the year, including the possibility of a return to larger increases if inflation should become entrenched on a high level. At the same time, a gradual approach to further tightening would reduce the risk of negative side-effects. This is my overall assessment of the appropriate monetary policy stance, which I also deem compatible with the principle of proportionality in the Sveriges Riksbank Act.

At today's meeting, I would like to focus on two questions that will help clarify my stance. What have we learnt about the transmission of monetary policy over the last year? And what, in turn, does this mean for monetary policy in Sweden as we go forward? I will conclude with some remarks on the global banking turmoil and the effects it may have.

Let me start with the lessons learned from the last year. First, inflationary pressures have been more powerful and more sustained than expected, not just in Sweden but worldwide. Central banks around the world have tightened monetary policy rapidly and resolutely. This is impacting global demand and contributing to a substantial easing of the factors that triggered the rising inflation, such as pandemic-related supply and demand imbalances and high energy prices following Russia's invasion of Ukraine. Lower global inflationary pressures benefit Sweden by restraining import prices. At the same time, as most other central banks are also raising their policy rates, we are not being supported by a krona appreciation in our efforts to bring inflation down. Over the past year, front-loaded increases have been a good strategy for restraining domestic demand, keeping inflation expectations well anchored and simultaneously countering an excessively strong krona depreciation. But this does not automatically mean that we have to continue to make increases in large steps. Now that the policy rate is at a contractionary level and is being supplemented by the sale of bonds, the most important thing is to keep monetary policy contractionary for a significant period until monetary policy has had its full impact. This will reduce the risk of negative side-effects and leave us prepared with a margin of manoeuvre to act on new information.

Second, we have seen a wide and rapid pass-through of rate rises to households (see Figure 18 in the draft report). Swedish households are highly interest rate sensitive but their high savings seem to have acted as a buffer. We know that not only have household debts increased sharply since the 1990s but so have household assets. In addition, saving was particularly high during the pandemic. What we do not know and cannot fully analyse is how long this will counteract a downturn in demand because we do not have data that matches debts against assets on the household level. However, we are now seeing a clear slowdown in the Swedish economy and have revised our forecast for domestic demand downwards - and it is domestic demand that is most important for inflation. The largest policy rate hikes were made last autumn and this will gradually have an increasing impact on demand and inflation over the course of this year.

Third, companies' pricing behaviour seems to have changed. It has been easy for many (not all) companies to pass their cost increases on to consumers.[5] For example, the indirect effects of high energy prices on other price categories have been greater than historical correlations would lead us to expect. Now that energy prices and global food prices are falling, consumers should be facing lower price increases. However, if competition is weak in certain sectors and if companies expect the policy rate to be cut in the near term, there is a risk that these companies will continue to raise prices too fast and too much. It is therefore important that monetary policy remains contractionary for a significant time. In addition, research shows that temporary increases of the policy rate risk only having minor effects on inflation.[6]

This leads me into my final point concerning lessons from the last year's monetary policy tightening and what this will mean going forward. We need to communicate more clearly that it would be problematic if a deviation from

[5] See, for example, "I've never before experienced customers accepting price increases so easily", *Riksbank's Business Survey*, February 2022, Sveriges Riksbank.

[6] See, for example, S. Laséen, J. Lindé and U. Söderström, "How much is inflation affected by monetary policy?", *Economic Commentary no. 13* 2022, Sveriges Riksbank.

forecast were to lead to a certain monetary policy response being expected.[7] A well-balanced monetary policy should always be forward looking. It should be based on an overall view of where the Swedish economy and inflation are headed in one to two years. Forward-looking information must be weighed in even when backward-looking outcomes are unfavourable.

Let me take the interpretation of outcomes for underlying inflation as an example. Inflation measured as the CPIF excluding energy was higher than in the February forecast, but this can be explained by two factors in particular: very high food prices and a change in the CPI basket. The weight for service prices has increased. This means that the upturn in service prices at the start of this year is a basket effect that reflects the strong demand for services last year (see page 10 of the draft report). In addition, global food prices have fallen and real-time data such as that from the food price monitoring company Matpriskollen indicate that the large price rises in food prices are now behind us. In addition, inflation adjusted for food and energy acts as a better guide for monetary policy and many countries exclude both food and energy from measures of core inflation as these are more volatile.[8]

Having said this, the road back to sustainably low and stable inflation will be a long one. If inflation becomes entrenched on a high level, I will not hesitate to continue gradual increases longer than the path indicates and/or to resume increases in larger steps than 0.25 percentage points. In addition, we can use all our tools, including adjusting the pace of quantitative tightening. Our sales of government bonds have worked well. We are not taking a new decision on this today but I would still like to stress that I support reducing the asset holdings by about SEK 200 billion a year, in line with earlier decisions (see Figure 3 in the draft report). All else being equal, I would prefer to see faster tapering rather than slower. This would have a positive side-effect in that it would supply liquidity to the market. Over the long term, this should provide some support to the Swedish krona. The krona has strengthened marginally (in KIX terms) since the last monetary policy meeting and it would be desirable for this trend to continue.

Before summing up, I would like to comment briefly on the recent banking turmoil. The situation has stabilised due to the quick actions of several central banks, governments and supervisory authorities in various countries. However, the appearance of new vulnerabilities in the financial system, triggering renewed global turmoil, cannot be ruled out. Such a scenario could, in retrospect, make today's decision look like a bad call, with the better decision having been to pause

[7] In this context, I would like to stress the importance of not regarding the alternative scenarios in the Monetary Policy Reports as simple rules of action. New global shocks can quickly change the conditions for a rapid return to the inflation target.

[8] For a more detailed discussion of the advantages and disadvantages of this, see speech by A. Breman (2022), 23 March 2022, Sveriges Riksbank, Inflation and monetary policy in the shadow of war.

further rate hikes. That said, with current information available, I support the analysis in the Monetary Policy Report: financial stability in Sweden is not currently threatened and the global banking turmoil does not justify refraining from a rate hike at today's meeting.

Allow me to summarise. Inflation measured with the CPIF target variable has started to turn downwards. It is important that this trend continues and that underlying inflation also falls. I do not support an increase of 0.5 percentage points at today's meeting but instead advocate a rate rise of 0.25 percentage points and a policy rate path that indicates subsequent continued increases. The economic gains from a return to sustainably low and stable inflation are substantial. This would create the conditions for robust economic growth, a strong labour market and a return to real wage growth.

Governor **Erik Thedéen** asked Anna to clarify her view of the policy rate path.

First Deputy Governor **Anna Breman** responded as follows. Martin and I have the same proposal for an alternative interest rate path, "a path that indicates further gradual increases in June and/or September". Note that this says "in June and/or September". Earlier in my contribution, I emphasised that "if inflation becomes entrenched on a high level, I will not hesitate to continue gradual increases longer than the path indicates and/or to resume increases in larger steps than 0.25 percentage points". I still see upside risks for inflation in the medium term and I would like to have room to make further increases later on in the autumn. I can easily see a path that peaks at over 3.75 per cent. Moving gradually forward with increases in smaller steps would create space for larger increases later on, if this is what would be needed to bring inflation sustainably back to a low and stable level.

Deputy Governor Per Jansson:

Since our last monetary policy meeting in February, three new inflation outcomes have been published, for January, February and March. Irrespective of whether price increases are measured including or excluding energy prices, inflation continues to be much too high and far above the inflation target.

It is indeed positive that inflation including energy prices has fallen by a couple of percentage points since our meeting in February and that this development is well in line with the forecasts we made at that time. Under the surface, however, the development is being driven by an unexpectedly large decline in the rate of increase in energy prices while other prices are rising faster than anticipated. Inflation excluding energy prices has therefore risen significantly higher than expected, 8.9 per cent in March, compared with a forecast of 7.5 per cent. As inflation adjusted for volatile energy prices can be assumed to provide a better picture of more genuine, underlying inflationary pressures, this development is of course clearly worrying.

However, everything is not doom and gloom when it comes to the indicators of underlying inflation. The median of our measures of underlying inflation fell in March for the first time in twenty months, from 8.8 per cent in February to 8.3 per cent. Even compared with the calculation based on data up until the end of December in conjunction with our last meeting, the median is now a little lower, around a tenth of one percentage point. The lowest measure of underlying inflation has also fallen slightly since our last meeting, from 7.3 to 7.2 per cent. These are not of course major improvements but after many meetings with very sharp increases in the measures of underlying inflation, it is nevertheless a bright spot that I think is worth highlighting.

An excellent article in the draft Monetary Policy Report discusses the conditions needed for inflationary pressures to ease more generally.[9] It states that price pressures at relatively early stages of the production chain have recently abated significantly but that there is still a way to go before this is visible in consumer prices. Monthly seasonally adjusted price changes, which in comparison with annual percentages rates of increase provide a more up-to-date picture of price developments, are still elevated. They imply, if we freeze the monthly changes for inflation excluding energy prices from now on, a price increase in annual percentage change for this inflation measure of just under 5 per cent.

One aspect I think deserves to be highlighted, however, is that the monthly change in inflation stripped of energy prices declined quite significantly in March compared with the three previous months, which moreover showed gradually rising outcomes. Monthly price changes are very volatile, even when seasonally adjusted. So one should obviously be careful when drawing long-term conclusions from this. But it is nevertheless positive and could constitute the start of an improving trend.

Another aspect that gives cause for some optimism is the outlook for the development of food prices. The monthly change in these prices has also decreased substantially in March after a couple of months of really poor outcomes, with monthly increases at an annual rate of over 25 per cent. In addition, there are now signs that the positive development in food prices has continued in April, for example according to weekly data from the food-price monitoring company Matpriskollen. Furthermore, food retailer ICA Sweden reduced its prices on over 300 articles by between 5 and 25 per cent on 11 April, saying that this will apply for at least two months.

[9] See the article “How quickly will inflation fall?”.

Looking at a few more fundamental determinants of inflation – inflation expectations, wage formation and fiscal policy – the situation remains stable, tilting towards becoming brighter. Fiscal policy has clearly internalised the existing inflation problems. The unfunded expenses totalling SEK 4 billion announced in the spring budget on 17 April do not significantly affect the inflation prospects.

On 31 March, the social partners in the manufacturing sector signed a two-year agreement providing wage increases of 4.1 per cent in the first year and 3.3 per cent in the second year. Additional agreements concluded after the agreement in the manufacturing sector are in line with this so-called benchmark. Although the deal implies a slight upward revision in the forecast for wage growth in the draft report, this is undoubtedly good news. Compared with many other countries, wage growth in Sweden is moderate and the fact that the agreement is over two years signals a high level of confidence in inflation falling and being back close to target in 2024.

That our labour-market organisations have confidence in the inflation target is also evident from Kantar Prospera's new readings of inflation expectations. In the larger quarterly survey in March, the employer organisations' five-year inflation expectations were just below 2 per cent, which is unchanged from the previous survey in December.[10] For the employee organisations, expectations even decreased slightly, from 2.3 to 2.2 per cent. For money-market participants, where there is also a reading for April, the corresponding expectations have varied between 2.1 and 2.2 per cent, one to two tenths of a percentage point lower than in the new outcomes we had access to at our February meeting.

Although there is some positive news in the inflation picture since February, sharp upward revisions of the forecast in the near term are proposed for both CPIF inflation and CPIF excluding energy prices in the draft report. The assumption for the rate of increase in energy prices going forward has been revised down overall, so the upward forecast revision for inflation excluding energy prices is significantly larger than the corresponding revision for inflation including energy prices. Including energy prices, the assessment has been revised up by about half a percentage point, or slightly more than that, some way into 2024, after which it gradually falls back towards the previous forecast from February. Regarding inflation excluding energy prices, the largest upward forecast revision is during summer and autumn this year, where the new assessment exceeds the earlier forecast by just over one and a half percentage points. From early spring 2024, the deviations from the previous forecast are small.

[10] I am focusing as usual on the expectations for CPI inflation rather than for CPIF inflation, as the response rate for CPIF inflation is often lower. As we are now in a rate-hike cycle, it may become more important going forward to follow and emphasise the expectations for CPIF inflation. For five-year inflation expectations, however, the differences between the two measures are currently small.

That the proposed forecast adjustments are so sizeable is to a large extent due to inflation adjusted for energy prices having surprised substantially on the upside since the monetary policy meeting in February. The development indicates quite simply that the inflation propensity in the Swedish economy is higher than expected, which will cause inflation to remain at a high level a little longer than we have previous thought. A tendency towards higher inflation propensity has also been noted in many other countries, so this seems to be a general phenomenon that central banks need to closely monitor. I support the forecasts for inflation and other economic variables in the draft report.

To contribute to a development of inflation in accordance with these forecasts, the assumption in the draft report is that the Riksbank will increase the policy rate by 0.5 percentage points at today's meeting and then slightly more at the June or September meetings. The forecast for the policy rate now peaks at 3.65 per cent, compared with 3.33 per cent in February. Another difference compared with the assessments in February is that the policy-rate forecast starts to fall slightly in the second half of 2025. This is a consequence of the policy-rate rises now being larger and that it then quite simply becomes more likely that the rate can be reduced somewhat again in the coming years. However, it is worth emphasising that the uncertainty around the development of the policy rate in the slightly longer term continues to be very considerable and that neither larger nor smaller rate rises can be ruled out in this time perspective.

I have already mentioned that, despite the major negative forecast surprises for inflation excluding energy prices, there are a number of bright spots in the inflation picture. These include different indicators pointing to favourable conditions for inflationary pressures to ease quite soon, positive outcomes in wage negotiations and fiscal policy, and inflation expectations that continue to be close to the inflation target in the slightly longer term. If it was not for these positive elements, I would certainly have considered the adjustment of monetary policy proposed in the draft report to be insufficient. After all, the inflation forecast has been adjusted upwards substantially even considering that the policy rate is higher than in February.

A circumstance I think is particularly troublesome in the context is that it this time in the forecast takes longer for inflation to stabilise close to the target. A firmer monetary policy than is now assumed in the draft report could possibly have changed this. Although it takes some time for monetary policy to impact inflation via demand effects, other parts of the monetary-policy transmission mechanism can affect price developments more rapidly. This is true, for example, of effects that go via the krona exchange rate or are more directly reflected in price- and wage-setting decisions.

If target achievement were seriously delayed, the social partners may feel let down, especially as they now have negotiated responsible nominal wage increases with an expectation that the Riksbank will do all it can to bring down inflation in the fairly near future so that real wages can begin to rise again. All things considered, however, the delay in target achievement is not actually that large. It is mostly a question of inflation being expected to be slightly higher for a few months in early 2024. The crucial thing in this situation is not really during which month next year inflation is exactly 2 per cent but that we very soon start to substantially reduce the far-too-high rate of price increase, to a level that does not deviate too much from the inflation target. Against this backdrop, I support the monetary-policy assumptions in the draft report. But I wish to stress that I am doing this with some hesitation and I am fully prepared to support both faster and larger policy-rate rises than those assumed in this forecast, if it proved necessary.

I would like to finish my contribution with a comment on how I, in a Swedish monetary-policy context, see the banking turmoil and market stress that affected us during the first half of March. The turmoil began in the United States but also spread to a couple of European banks. It was rapidly countered by powerful measures from central banks, governments and authorities, which helped to stabilise financial markets. Swedish banks are profitable and have ample capital and liquidity, which probably explains why market moves were more limited here in Sweden than in many other countries. However, such events do not just pass by without leaving a trace and there is in all likelihood some residual unease in financial markets, even here in Sweden. Another lasting effect is that markets have reduced their expectations of central bank policy-rate rises, especially in the United States. Neither can it be ruled out that the events may lead to some tightening of the regulatory frameworks for banks and financial markets further ahead. But they have so far not been of any direct, concrete significance for my view of Swedish monetary policy.

Governor Erik Thedéen:

Let me begin by saying that I support the proposal to raise the policy rate by 0.5 percentage points to 3.5 per cent. And I support the path for the policy rate indicating that there is some likelihood it will be increased by a further 0.25 percentage points in June or September. Finally, I also support the forecasts presented in the draft Monetary Policy Report. I also think that we should continue with the government bond sales that we decided on at our previous meeting. The volume and other terms and conditions should remain unchanged, unless important new information is received.

The period since the previous monetary policy meeting has been very eventful, with among other things three new outcomes for the CPI, which has given us plenty of new information on how inflation is developing. We have also had a period of turmoil in the banking sectors in the United States and Europe in March.

International growth is entering a calmer phase in 2023. Developments in the United States have been surprisingly positive, including a strong labour market. China’s economy is also expected to be stronger after the Covid restrictions are lifted. Inflation will fall at a global level in line with the effects of earlier supply limits declining and demand slowing down, partly as a result of tighter monetary policy. Inflation is still high in most developed economies.

Economic developments in Sweden are weakening in 2023 following relatively strong growth in 2022. Growth has been somewhat stronger than expected at the beginning of 2023. This is partly connected to international economic growth having been relatively robust, which has had a positive effect on exports. But we have also seen that consumption of private services has been maintained in an unexpected manner. The labour market has also developed better than expected; the employment rate is continuing to rise. Indicators such as the recruitment plans in the Economic Tendency Survey point to a continued strong labour market, although the picture differs from one sector to another. There are labour shortages in several parts of the economy.

Signs of some stabilisation can also be seen in the housing market. It is possible that further price falls will occur when more households feel the effects of rising mortgage rates. But it could also be the case that demand for housing is stronger than the Riksbank and many other analysts have assumed. In that case, there is less risk of private demand being even weaker.

All in all, economic developments in Sweden in 2023 look to be slightly less weak than was indicated in our February report. Our forecast is still that GDP will fall, but somewhat less than was assumed in February. My assessment is that there is some upside risk in our forecast. However, the Swedish economy is sensitive to interest rates and it will still be important to monitor private consumption to assess how it reacts when an increasing number of households are hit by rising interest expenditure.

Since the previous monetary policy meeting, the development of inflation has given cause for concern. Three new outcomes for the CPI have been published since the February report, and they have all been higher than the forecasts we made then. According to the most recent outcome, which refers to March, the annual rate of change in the CPIF was 8.0 per cent and the figure for CPIFxe was 8.9 per cent.

With regard to the outcome for the CPIF, the deviation in the March outcome was not so large, 0.2 percentage points. However, the CPIFxe, which is inflation excluding the falling energy component, was a good 1.4 percentage points higher than our assessment in February. The outcomes show that we are still in a period of very high underlying inflation. At this meeting, too, we will have to adjust the inflation forecast for 2023 and 2024 upwards.

One important question is whether we can discern a turning point for inflation. Figure 47 in the draft report shows the monthly changes in the CPIFxe. The figure shows that inflation has not yet shown any clear turning point. It is possible that the recent monthly outcomes give some hope, but this is only individual outcomes. But there are also signs of food prices slowing down.

This also includes the fundamental trade-off we need to manage; most indications are that inflation will fall, and even that it will fall quickly and substantially over the coming year, but inflation is so far still at a very high level and cannot be said to have shown a clear downward turn. We must therefore both consider that inflation will probably fall relatively much going forward and at the same time note that there is considerable uncertainty and that we have been repeatedly had negative surprises.

A good illustration of the inflation dynamic can be found in an article in the draft report. This contains a review of the various indicators for cost and price pressures in various stages of production in the form of a heat map. The heat map illustrates clearly that much lower price and cost pressures are now in the pipeline, which indicates a clearly lower rate of inflation in the consumer stage for the remainder of this year and during next year. However, at the same time, the heat map shows that the more consumer-related inflationary pressures, in the form of pricing plans in the retail trade, for instance, are still high. This means that the inflation dynamic is still uncertain. The fact that inflation is falling is relatively certain, but by how much and to what level is still very uncertain.

What is new since the previous monetary policy meeting is that important steps have been taken in the collective wage bargaining rounds. The agreements signed so far do entail a rate of wage increase that is somewhat higher than our earlier forecast, but they mean that the risk of future price and wage spirals has declined. And this indicates that inflation expectations may remain stable, even if individual monthly outcomes for inflation were to be more negative than expected; monetary policy can assume on the basis of these wage agreements that there is now less risk of a really bad development in inflation going forward. I think that we can regard to the design of the collective wage agreements as a sign of good confidence in the Riksbank's actions to safeguard the inflation target. If the social partners are to continue to trust the Riksbank, we must continue to act to bring down inflation within a reasonable period of time. Only then can wage-earners experience real increases in their salaries.

I would also like to say a few words about the financial turmoil that arose in March, and what this could mean for Sweden. In March, some major question marks were raised regarding some smaller banks in the United States. This development was very rapid and the Silicon Valley Bank went from having a good external credit rating to being on the brink of bankruptcy in one week, after very rapid and large outflows. Other banks with similar business concepts and customers were hit by the same mistrust. The US authorities implements powerful measures, and the situation calmed down after a couple of weeks. In Europe, Credit Suisse also suffered a confidence crisis. We faced the risk of a global systemically important bank being put into resolution for the first time since the new regulations came into force. This didn't happen, however, and the situation calmed down after powerful measures by the government and authorities in Switzerland.

There are other important lessons that can be learned from these events. One concerns the global economy and the international financial markets being in a period of major change. We have gone from a long period with low interest rates and good access to liquidity, to a new financial environment with rising interest rates and competition for liquidity. During such a transition, financial institutions and other companies and households, which have not made allowances for the change, are also affected, as we saw in March. The important thing is to understand that the transition is not over yet. The IMF, for instance, points in its most recent forecast to the risk of new periods of financial unease, and that this can have a negative effect on credit granting and economic growth. There is thus reason for increased vigilance regarding developments on the financial markets going forward, as higher interest rates affect several parts of the economy. Moreover, there is reason to consider whether regulations need to be changed as a result of the recent events in the United States and Switzerland. A discussion on this has already begun, which I welcome.

Swedish banks were not affected to any great extent by the bank stress in March, which is probably due to their strong financial position and good earnings capacity. However, equity prices fell and borrowing costs rose for Swedish banks, too. The situation at the time of today's decision indicates that the banking crisis at the beginning of March has relatively limited significance for inflation in Sweden, and thus for monetary policy. My assessment is nevertheless that we cannot disregard the events in March. They showed examples of risks in the financial system that are difficult to identify in advance. And the large falls in policy rate expectations that occurred then reflect the potentially large negative effects that the banking unease is thought to be able to have on the economy as a whole. Although the situation has calmed, I see some, albeit limited, risk that the events in March could have a negative effect on investment decisions and credit granting.

The value of the krona has varied considerably since the previous meeting, and is now at roughly the same level as then. I addressed the long-term development of the krona at the previous monetary policy meeting, and my view is the same now as then. That is, that there are several factors indicating a stronger Swedish exchange rate, for instance given the large Swedish savings surplus in relation to other countries and the stable economic policy framework. If the krona continues to weaken, which in turn affects inflation, we need to take this into account in monetary policy. A stronger krona would be welcome, and is also included in our forecasts, as it would make it easier for us to attain the target of 2 per cent inflation.

Let me summarise my monetary policy deliberations in connection with today's decision. As I have said, a lot of new information has been received since the previous monetary policy meeting, both information indicating we need a tighter monetary policy and information indicating a more positive development in inflation going forward, which reduces the need to raise the policy rate.

What does indicate a need for monetary policy tightening is the high rate of inflation, which is moreover reinforced by unexpectedly high outcomes since our February meeting. Underlying inflation is currently further from our target than we anticipated in February. Moreover, many companies still have pricing plans that indicate inflation will remain high. I would also like to add that economic developments, perhaps particularly on the labour market, have been somewhat stronger than expected. Forward-looking economic indicators have been somewhat stronger than most analysts were expecting. So although demand in the economy is falling, it may be to a lesser extent than we and others fear.

There are several factors pointing in the other direction. The most important is that we see clear conditions for inflation to fall during 2023. Falling price and cost pressures in earlier stage should gradually spill over into lower prices in the consumer stage, too. Inflation expectations in the longer term are in line with the inflation target, and the fact that the collective wage negotiations delivered agreements that are assessed as compatible with the inflation target reduces the risk of high and lasting inflation in the long term; the risk of a really bad development in inflation has declined as a result of the agreements signed in the Swedish labour market. Nevertheless, there is still uncertainty over how quickly and how much inflation is falling.

To summarise, I think there is reason today to raise the policy rate by 0.5 percentage points to 3.5 per cent. I also think that now, despite the very high inflation we are still registering, it is appropriate to reduce the pace of the increases and adopt a somewhat more open stance. It will still be important to closely monitor new economic information, including the development of the krona, to take a stance on whether the inflation forecast in the draft report will prove accurate. But if the information about Swedish inflation and economic developments points towards increased or prolonged inflationary pressures, I will advocate a higher policy rate than is indicated in our interest rate path. The aim of bringing inflation to two per cent within a reasonable period of time will of course continue to guide me.

In conclusion, Deputy Governor **Aino Bunge** added: I share the view that some light can be seen regarding the future inflation trend, not least the wage bargaining rounds and inflation expectations, which will make the risk outlook more symmetric in the period ahead. But this will be from a significantly less favourable inflation situation than we expected in February. Without this light, I would consider, like Per Jansson, that the interest rate would have had to be raised further.

§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 policy rate will be raised by 0.5 percentage points to 3.5 per cent and this decision will apply from Wednesday, 3 May 2023,
- to establish the Monetary Policy Report according to the proposal, Annex B to the minutes Monetary Policy Report,
- to publish the monetary policy decision with the motivation for it in a press release at 09.30 on Thursday 26 April 2023,
- to publish the minutes from today's meeting at 09.30 on Tuesday 9 May 2023.

This paragraph was confirmed immediately.

Minutes taken by

Mattias Ankarhem   Paul Elger

Verified by

Erik Thedéen   Anna Breman   Aino Bunge

Martin Flodén   Per Jansson

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