



Lessons from a turbulent period

20 December 2023
Carnegie Fonder

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



Erik Thedéen
Governor

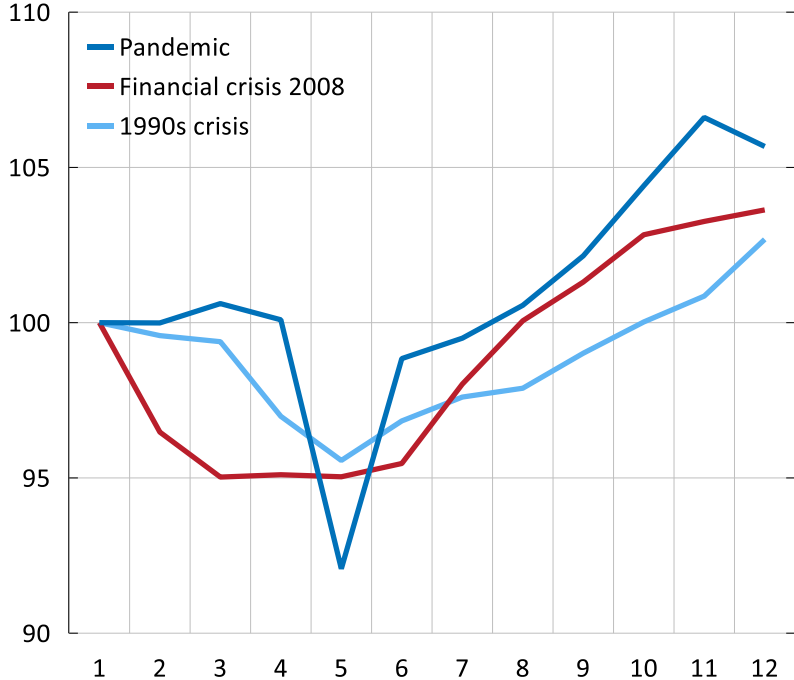
Unusual period with series of global shocks

- The pandemic
 - Dramatic drop in GDP
 - Fast recovery due to vaccine
- War in Ukraine
 - Rising prices for energy and food
 - Reinforced the inflationary trend
- War between Israel and Hamas
 - Limited economic effects so far, but...

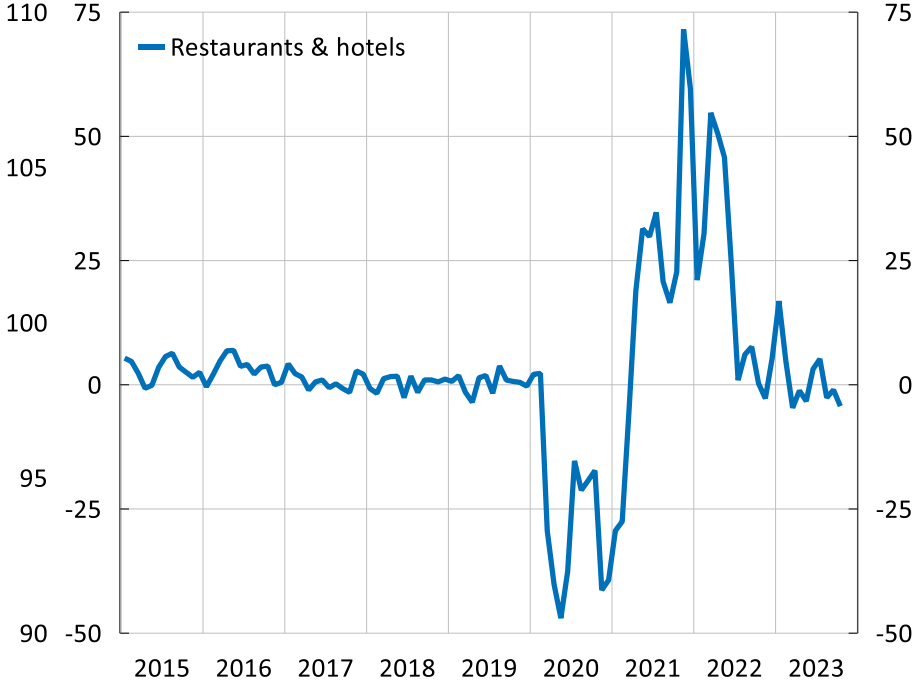


Both demand and supply contributed to the high inflation

Fast recovery after the pandemic



Pent-up demand for consumption

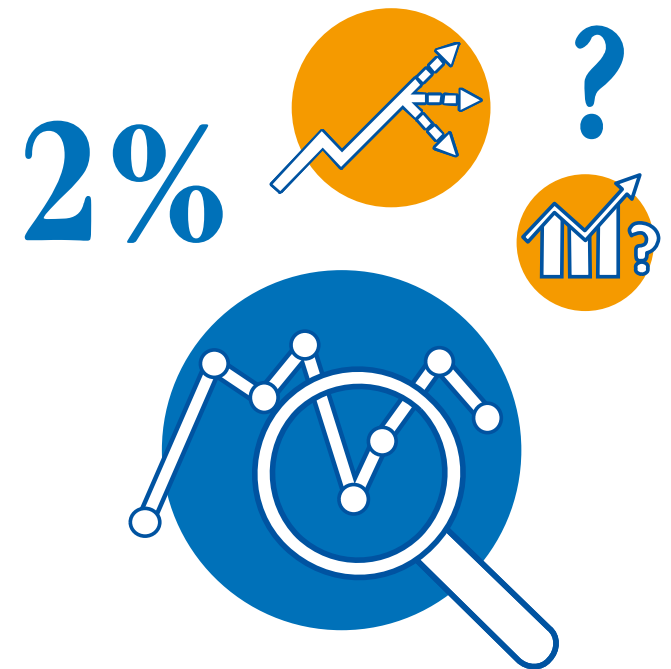


Note. Index=100 five quarters before the bottom of the cycle, the x-axis shows the number of quarters (left). Annual percentage change. Household consumption in fixed prices, seasonally adjusted data. Latest outcome is August 2023. Note that "transport" and "recreation and culture" do not only include consumption of services, but also goods such as leisure goods and vehicles (right).

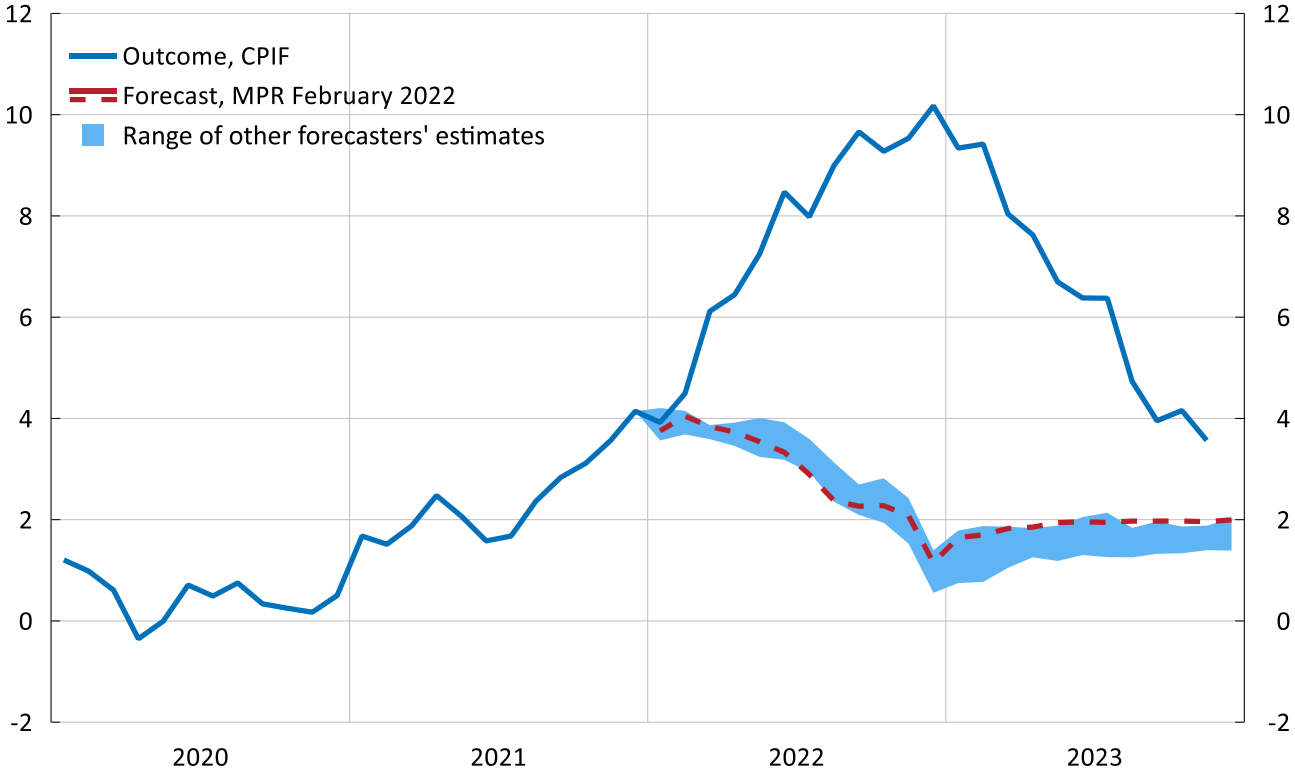
Source: Statistics Sweden.

Some lessons learned (so far)

- Difficult to make forecasts
 - Inflation was underestimated



Difficult to forecast inflation

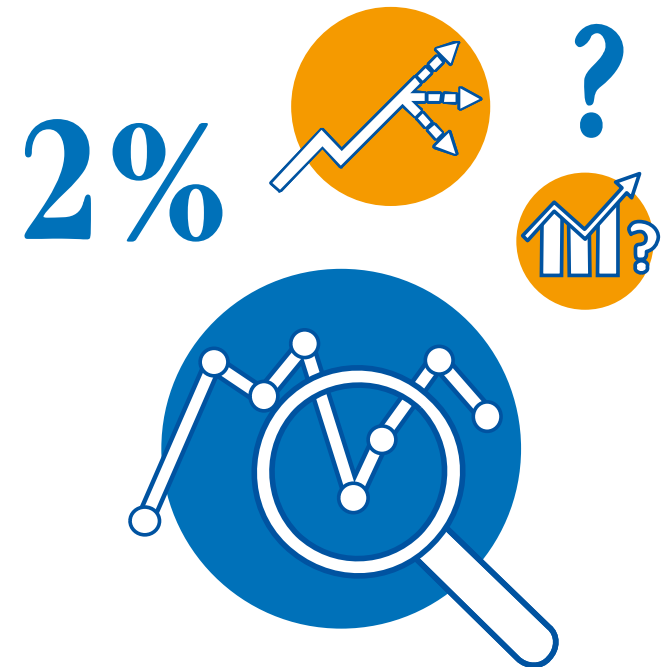


Note. Annual percentage change. Refers to forecasts based on outcomes for CPIF up to and including December 2021. The range shows the spread between the highest and lowest forecast made by other forecasters

Sources: Statistics Sweden, individual forecasters and the Riksbank.

Some lessons learned (so far)

- Difficult to make forecasts
 - Inflation was underestimated
 - Alternative scenarios
- Easy to get caught up in the zeitgeist
 - Inflation was not "dead"
- Stable economic relationships can change
 - Easier to pass on cost increases
 - Important with indications of changes (ongoing project)



Inflation Is Dead and It's Not Coming Back

"I praktiken, för ett land som Sverige, är inflationen död under överblickbar tid. För en kontinent som Europa är inflationen död"

Inflation is dead: It's below 1 percent in the U.S., U.K., Europe, China, and Japan

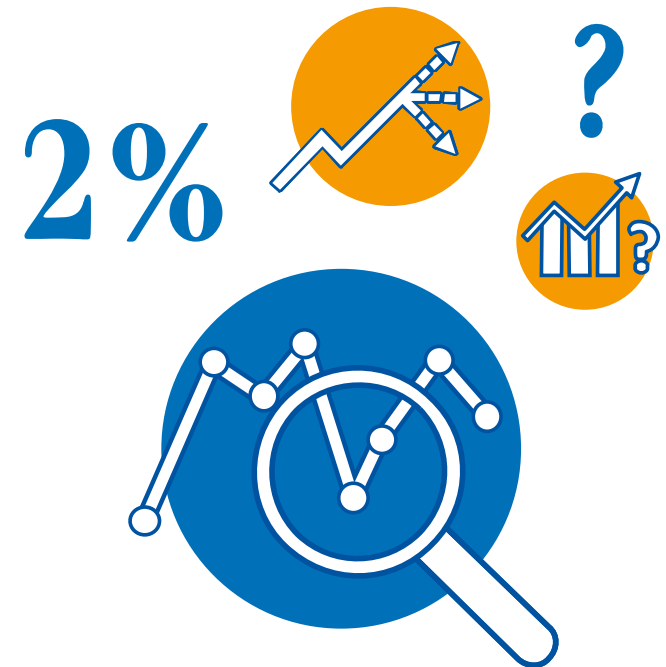
"Low inflation presents challenges for the economy"

Low inflation is a global phenomenon with global causes

Riksbanken måste sänka inflationsmålet

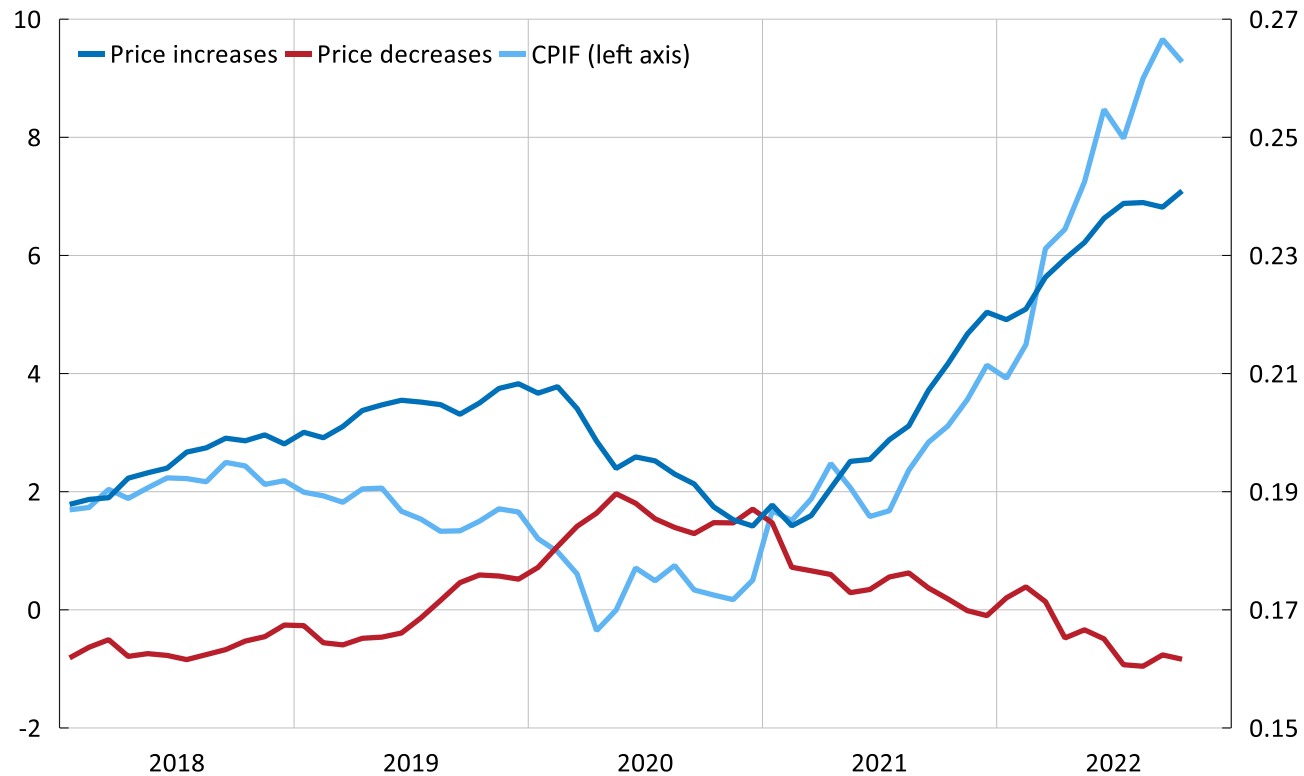
Some lessons learned (so far)

- Difficult to make forecasts
 - Inflation was underestimated
 - Alternative scenarios
- Easy to get caught up in the zeitgeist
 - Inflation was not "dead"
- Stable economic relationships can change
 - Easier to pass on cost increases
 - Important with indications of changes (ongoing project)



The frequency of price changes most important

CPI, price change frequency. CPIF annual percentage change.

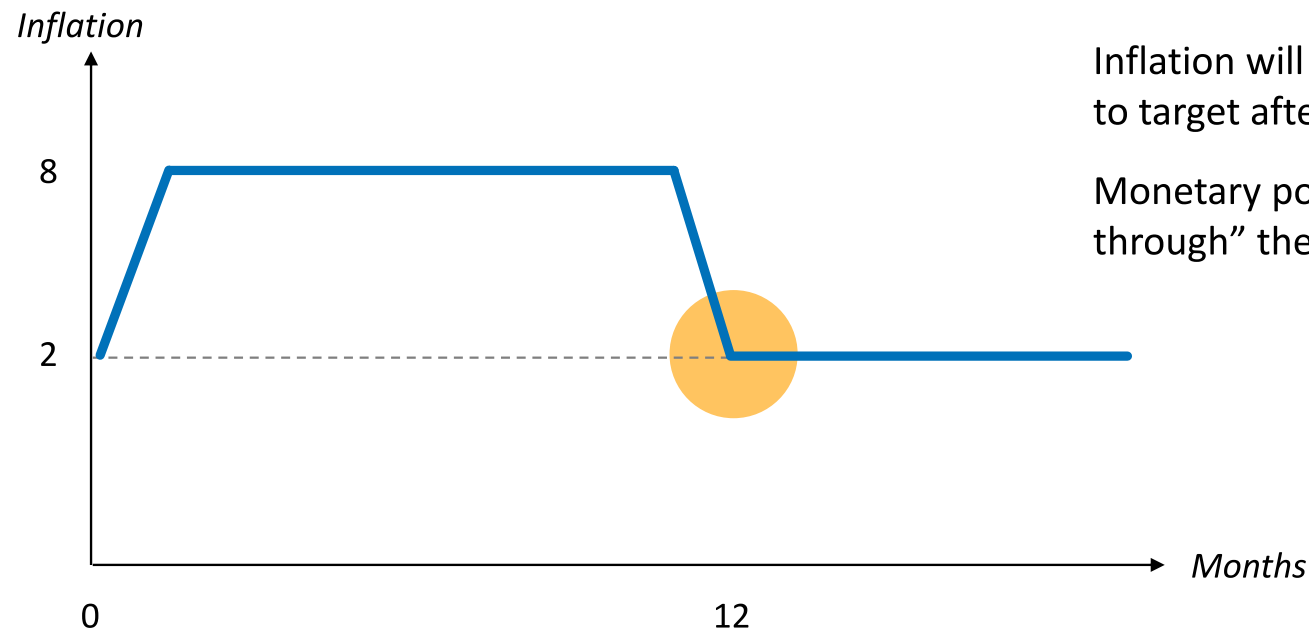


References: Montag, Hugh, & Daniel Villar (2023), "Price-Setting During the Covid Era", FEDS Notes, Board of Governors of the Federal Reserve System. Cavallo, Alberto, Francesco Lippi & Ken Miyahara (2023), "Large Shocks Travel Fast", NBER Working Paper No. 31659.

Debate about how much the policy rate has had to be raised

”Inflation is demand-driven”

Effect on inflation of a one-off increase in energy prices



Inflation will automatically return to target after 12 months

Monetary policy can “look through” the supply shock

But more complex in practice

- Both supply *and* demand have played a role
- Spillover effects also from supply impulses
 - Pricing more generally – “it has rarely been so easy to raise prices”
 - Wages – next wage round?
 - Expectations – anchored, but based on the Riksbank actually reacting
- Evaluation of monetary policy 2022 (Hassler et al., 2023):
The Riksbank should have raised earlier and more resolutely
- Matter of judgement how much the policy rate needs to be increased
 - “Policy rate hikes don’t affect supply-driven inflation” too simple



Negative supply shocks more common in the future?



Climate change

More frequent natural disasters, lack of certain foods, etc.?

Deglobalisation

Problems due to less international integration?

Climate transition

Problems when switching to other energy sources, etc.?

Monetary policy more difficult

Even more important with anchored inflation expectations

We are not at the finishing line – there are still lessons to be learned

- The final conclusions from the episode of high inflation still to be drawn
- “Soft landing” the ambition – permanently back on target with a mild slowdown
- “Last mile problem”
- New information and how it affects the economic and inflation outlook determines monetary policy





THANK YOU!

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