Monetary policy in a changing world

Kommuninvest, Örebro
13 November 2019

Martin Flodén
Deputy Governor
Agenda

- The economy is changing
- How large is the monetary policy toolbox?
- Can the Riksbank contribute towards more sustainable development?
The economy is changing

- Globalisation has taken a step back
- China is increasingly important
- Ageing population, lower population growth
- Digitalisation
- Climate change
Globalisation has taken a step back

World trade is not growing like before

Global value chains are breaking up

Exports and imports as a proportion of global GDP, per cent, and proportion of exports linked to global value chains, per cent, respectively.

Sources: World Bank, OECD, IMF, Riksbank and UNCTAD-Eora.
China is increasingly important

China:
• Share of global GDP increased from 3 to 16 per cent between 1980 and 2018
• Saving ratio increased from 32 to 45 per cent

G7 countries:
• Saving ratio decreased from 23 to 21 per cent

Global saving ratio, per cent of GDP, and contributions from China and the G7 countries, respectively. Source: IMF WEO.
Demography entails lower interest rates and growth

- Lower population growth
  - ... lower willingness to invest
  - ... lower GDP growth
- We are living longer
  - ... want to save more for retirement
  - ... increased dependency ratio

Growth in G7 countries’ population, 25–29 years, annual percentage.

Source: UN.
Productivity has grown more slowly

Lower productivity growth

... lower willingness to invest
... lower GDP growth
... lower interest rates

Growth in OECD countries’ labour productivity, annual percentage. Source: OECD EO.
The economy is changing

- Willingness to invest↓
- Need to save↑
- Lower productivity growth?
- Lower inflationary pressures?
- Low interest rates
- Low growth
Many indications of continuing low real interest rates

Yield on 10-year real government bonds, per cent, 12 month moving average.

How large is the monetary policy toolbox?
The Riksbank’s toolbox

The interest rate can be cut

- But the interest rate is close to its *effective* lower bound

Purchase more Swedish government bonds?

- Term premiums are already very low
- No credit risk for Swedish government securities
- The Riksbank already owns a large share

‘Unconventional’ monetary policy

- Other asset purchases, helicopter money, …
- Could work but is *fiscal policy*
- Sweden’s public finances are strong; it is the Government’s task to conduct fiscal policy
Can the Riksbank contribute towards more sustainable development?
Climate change affects the economy

**New risks**
- Physical risk & transition risk
- Adequate supervision and regulation are needed
- Primarily Finansinspektionen’s responsibility, but also the Riksbank’s

**The functioning of the economy is changing**
- Economic relationships are changing
- More noise in the data?

**Can the Riksbank contribute to better sustainability?**
- Asset purchases (QE)?
- Managing the foreign exchange reserve?
Can the Riksbank contribute to better sustainability?

Asset purchases
- Swedish government bonds
- The central government is the Riksbank’s principal
- Not appropriate for the Riksbank to attempt to affect the Government’s climate work
- The Riksbank should not select among government bonds

Managing the foreign exchange reserve
- The reserve must consist of safe and liquid assets
- There is some scope for considering climate change
- New risk and investment policy
Greenhouse gas emissions

Direct greenhouse gas emissions, excluding uptake and emission of greenhouse gases from land use, GHG (kt CO2e)/GDP (mn USD).

Sources: UNFCCC, OEDCD, Climate watch.
The Riksbank rejects issuers with a large climate footprint

Direct greenhouse gas emissions, excluding uptake and emission of greenhouse gases from land use, GHG (kt CO2e)/GDP (mn USD).

The economy is changing
- What will normal levels be for interest rates and productivity and GDP growth in the period ahead?

The Riksbank must understand structural changes
- Economic correlations are changing, new risks are emerging
- However, monetary policy has little ability to affect these structural changes

Fiscal policy is playing a larger role in stabilisation policy
- The policy rate is close to its effective lower bound
- Fiscal policy can be made more expansionary if necessary

The Riksbank shall not conduct fiscal or climate policy
- But the Riksbank can take some consideration of climate change in its management of the foreign exchange reserves
Thank you!