

Monetary policy at the Riksbank and the Phillips curve

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1

Flexible inflation targeting

- Stabilize inflation around the inflation target (2%)
- Stabilize the real economy (resource utilization, output gap)
- Minimize loss function ($\lambda > 0$)

$$L_t = (\pi_t - \pi^*)^2 + \lambda(y_t - \bar{y}_t)^2$$



2

Flexible inflation targeting

- “Forecast targeting:” Choose an instrument-rate path such that the forecast of inflation and resource utilization “looks good”
- “Looks good:” Inflation goes to target and resource utilization goes to normal at appropriate pace
- Publish and motivate instrument-rate path and forecast of inflation and real economy
- “Management of expectations”



3

Decision process

- 6-member Executive Board
- 6 policy decisions per year (3 reports, 3 updates)
- Interaction between staff and EB results in main and alternative combinations of forecasts of repo rate, inflation, and real economy
- At final policy meeting EB discusses and votes on decision and report/update
- Majority decision published day after policy decision
- Named minutes including any dissenting views published 2 weeks after policy decision



4

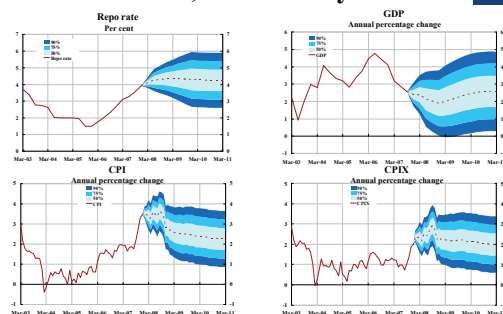
Forecasts

- Forecasts and simulations produced with
 - DSGE model (Ramses, since 2005)
 - Bayesian VAR
 - Other models (indicator, single-equation)
 - Judgment
- Mean forecasts, not mode
- Uncertainty intervals



5

Mean forecasts, uncertainty intervals



6

Ramses, Phillips curves

- Open-economy DSGE model (Adolfson, Laséen, Lindé, Villani)
- Estimated with Bayesian methods
- AS block: New-Keynesian Phillips curves (domestic, consumer-goods import, investment-goods import, export)
- Estimated instrument rule
- Optimal policy (to be implemented)



7

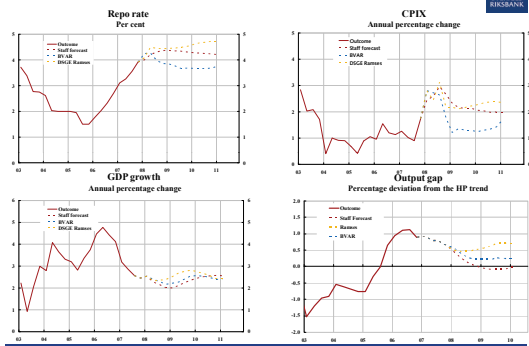
Implications for policy

- Discussion about alternative paths of repo rate, inflation, and real economy
- Discussion more about future repo-rate paths than current repo-rate level
- More medium and longer-term perspective
- More general-equilibrium perspective
- More systematic treatment of alternative assumptions about (scenarios of) of exogenous variables, transmission mechanism, inflation expectations, etc.



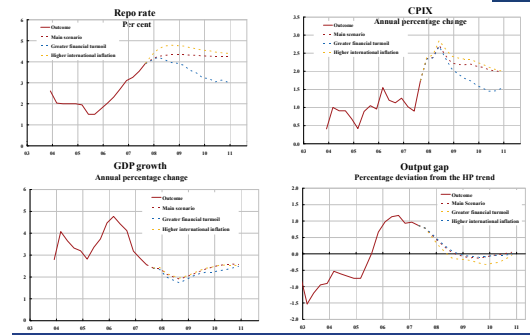
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Model and staff forecasts



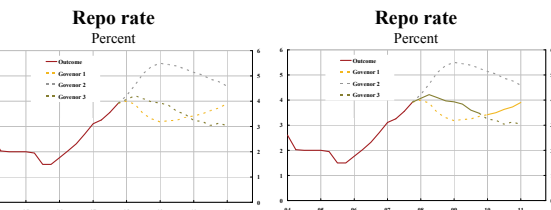
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Alternative scenarios



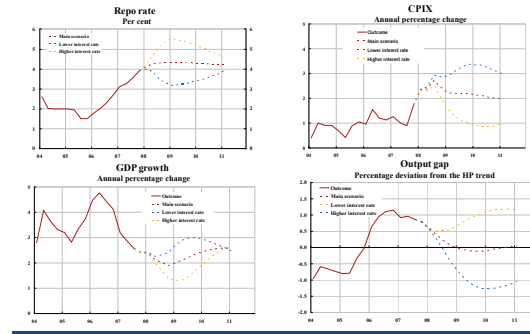
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Deciding on a repo-rate path: Median path?



11

Deciding on a repo-rate path: Just vote among a few alternatives



Decisions

February 2007-April 2008

