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Recent Economic Developments in Sweden,
May - August 1963

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Economic Developments in Sweden: May - August 1963

Summary

Swedish expansion, which was underway as the economy emerged from the severe winter, quickened and also became more broadly based this summer.^{1/} The stimulus of reviving export demand has significantly improved the outlook in some industrial branches--timber and pulp, iron ore mining, steel, the engineering branches and shipbuilding--which still displayed weakness earlier this year. Meanwhile, economic activity has continued at high levels in previously dynamic sectors such as public and private consumption and, especially, construction.

The authorities are now concerned over mounting signs of inflationary pressure, particularly in the building sector. Anticyclical building programs adopted in 1962 and the rush to complete projects delayed by the bad weather have combined to produce labor shortages and to encourage wage increases in excess of contractual limits. So far, these rising costs and continued high spending levels have not been reflected in Swedish price indices, which have increased very moderately. However, in order to reduce strains in the building sector, the central government recently reached agreement with communal and regional authorities to cut down building activity of local authorities.

On the monetary front, economic policy is aimed at curbing inflationary tendencies. This spring witnessed a switch from liberal to restrictive credit policies, which culminated in the discount rate increase from 3-1/2 to 4 per cent on June 14. Nevertheless, the money market has been under strain as bank credit expansion continued unabated. The resulting squeeze on bank liquidity--with some

^{1/} The earlier stages of the Swedish business expansion are discussed in "Economic Developments in Sweden: January - May 1963," July 2, 1963.

banks hard pressed to maintain prescribed liquidity quotas--and an unusually heavy volume of commercial bank borrowing at the central bank led the Bank of Sweden in mid-August to issue a strong warning on the dangers of continued rapid credit expansion.

Swedish exports have been rising from the depressed first quarter level, but the effects of the severe winter on outbound shipments and a rising volume of imports resulted in a trade deficit of \$183 million in the first seven months, more than doubling the deficit of \$79 million in the comparable January-July period of 1962. However, Sweden is now in the period of seasonal balance of payments strength, and export prospects are favorable. The decline in Sweden's gold and foreign exchange holdings which set in last November continued through June. Reserves fell by \$82 million in this eight-month period, with most of the loss sustained in the first quarter of this year. Reserves rose modestly (by \$29 million) in July, but declined (by \$9 million) in August.

Economic expansion broadens

The improved tone displayed by the Swedish economy as it emerged from the exceptionally severe winter has been more definitely confirmed this summer.

Industrial production has increased modestly but steadily. On a seasonally adjusted basis, the index shows a continuing improvement in the first two quarters this year, by comparison with the corresponding periods in 1962. (See Table 1.) The sector breakdown--which is not seasonally adjusted--shows a continuation of the earlier pattern, with virtually the entire gain in output concentrated in the consumer goods sector. While over-all industrial production increased by about 2 per cent in the first six months of this year, capital goods output was unchanged and consumer goods production rose by about 6 per cent.

Table 1. Sweden: Industrial Production, 1961-63.
(quarterly averages of seasonally adjusted monthly data, 1935=100)

<u>Quarter</u>	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>Index of Change</u> (1962=100)
I	286	288	296	102.8
II	280	286	300	104.9
III	281	295	-	-
IV	289	297	-	-

Sources: Affärsvärlden; Bank of Sweden, Ur tidningarna (daily press releases).

The rather mixed trends observable within some industrial branches earlier this year have evened out somewhat, as the general upswing in Europe is providing an impetus to the Swedish expansion. In July the Swedish Labor Market Board noted rising levels of activity in machine-building and engineering, the timber, paper and pulp branches and in Swedish shipyards as evidence that the recession was over in these sectors. The Board pointed to a successive improvement in new orders (especially for export) during the spring, concluding that the new order books guaranteed high levels of employment in these branches through the first half of 1964.

Sectors of trade serving the consumer have continued strong. The latest retail sales figures (March) show that first quarter retail trade turnover was 10 per cent higher than in January-March 1962. New car sales have been setting records in each month this year, and through August were 18 per cent higher than total new car sales in January-August 1962.

Labor market tightens

Swedish labor market developments since the spring provide clear evidence of the broad character of the current economic expansion. Unemployment was, of course, relatively high last winter. By April, rising levels of economic activity had made substantial inroads into the idle labor force, and by May unemployment reached a record low for this time of year. (See Table 2.)

The rather speedy reduction in unemployment as the weather improved and general business activity picked up was accompanied by signs of increasing labor market tightness, as indicated by the data on total vacancies shown in Table 2. Labor market shortages developed earliest--and have been most pronounced--in the construction sector, where high levels of activity reflect the effects of anticyclical building programs adopted in 1962 as well as the rush to complete building projects delayed as a result of the severe winter.

Wage and price movements moderately upward

Rising levels of economic activity and tighter labor market conditions are evidently pushing up wages, although comprehensive data on wage movements lag considerably. Through May, the latest month for which partial statistics are available, the upward movement was still rather moderate. Between February and May this year hourly wages of adult male industrial workers increased by 2 per cent, which is about in line with earlier predictions. However, wage increases are apparently exceeding this moderate pace in branches in which shortages of skilled workers are reportedly most serious; and in the building sector upward wage movements for some skills are evidently exceeding contractual margins. New wage negotiations will take place this fall; late in August, the Minister of Finance expressed concern at this year's quite substantial upward wage "drift," which thus far has averaged 3 per cent.

Table 2. Sweden: Labor Market Indicators, January-June 1962-63

<u>Year and Month</u>	<u>Total</u> ^{1/}	<u>Unemployment</u>			<u>Vacancies (thousands)</u>
		<u>Total</u>	<u>Percentages</u> ^{2/}		
			<u>Industry</u>	<u>Construction</u>	
1962 Jan.	35112	2.1	1.1	8.5	108.1
Feb.	34440	2.2	1.0	9.1	102.8
Mar.	31732	2.0	1.0	8.4	117.0
Apr.	29790	1.9	0.9	6.8	115.1
May	21591	1.3	0.7	3.7	144.5
June	16280	0.8	0.6	2.1	137.9
1963 Jan.	56621	3.6	1.5	17.2	107.8
Feb.	40695	2.5	1.3	9.8	103.5
Mar.	32448	1.9	1.1	6.8	118.6
Apr.	30091	1.8	1.0	5.1	125.7
May	19395	1.1	0.7	2.7	153.1
June	14636	0.7	0.6	1.6	n. a.

^{1/} Registered unemployed.

^{2/} Percentages of insured workers.

Source: Monthly Digest of Swedish Statistics, July 1963;
Bank of Sweden, Ur tidningarna.

These rising wage costs and continued high levels of consumer spending have not yet been reflected in Swedish price indices, which have edged up only moderately so far this year. In the first six months, the cost of living rose by 1.7 per cent--much less than the 4.3 per cent increase between December 1961 and June 1962. The rise in wholesale prices was equally moderate, the index recording an increase of 1.9 per cent in the first half of 1963. (See Table 3.) In this period, however, import prices increased by about 3 per cent while export prices moved up only marginally. The resulting deterioration in Sweden's terms of trade contributed, albeit not significantly, to the larger trade deficit in the first half of the year. (See below.)

Table 3. Sweden: Price Movements, 1961-63.
(1949=100)

<u>Item</u>	1961 <u>Dec.</u>	1962		1963		<u>Percentage Changes</u>	
		<u>June</u>	<u>Dec.</u>	<u>Mar.</u>	<u>June</u>	<u>Dec. '62</u> to <u>June '63</u>	<u>June '62</u> to <u>June '63</u>
Cost of living	164	171	172	174	175	+1.7	+2.3
Wholesale prices	152	154	156	157	159	+1.9	+3.2
Export prices	144	143	142	142	143	+0.7	-
Import prices	125	125	124	126	128	+3.2	+2.4
Terms of trade <u>1/</u>	115	114	115	113	112	-	-

1/ Ratio of export prices to import prices.

Source: Monthly Digest of Swedish Statistics, July 1963.

Countercyclical fiscal policy moves

Since the beginning of this year, the Swedish authorities have gradually dismantled the expansionary fiscal programs adopted to ease the employment effects

of the 1962 recession.^{1/} The authority to spend investment funds expired at the end of April. As residential construction activity increased with the end of the winter weather, the authorities gradually allowed relief projects to taper off, and by mid-year had released most workers to the private building sector.

Nevertheless, the authorities, greatly concerned at signs of overheating in the construction sector, recently moved to reduce the strain on manpower resources and the wage level. At a conference of local government representatives held at the end of August, the central authorities obtained agreement on a voluntary curtailment of public building activity. The agreement provides for postponement, until next June, of public building projects costing over 300,000 kronor. However, construction of residential units was exempted because of the persistent need for more housing.

The authorities are not planning any restrictions on private investment activity, which shows signs of reviving after a two-year period of sluggishness. But they will attempt to hold down the over-all level of government expenditures, particularly since the deficit estimated for the current fiscal year (ending June 30, 1964) will exert an expansionary effect. So far, however, the government accounts have continued to reduce liquidity in the economy. The combined surplus reported for the fiscal year that closed on June 30 was Skr. 513 million, as compared with surpluses of Skr. 300 and 381 million, respectively, in the preceding two fiscal years.

Restrictive monetary policies strengthened

With the reversal from easy to restrictive monetary policies earlier this year, and the discount rate increase from 3-1/2 to 4 per cent on June 14, domestic money markets have been under continued strain. Bank lending has been

^{1/} These measures are discussed in "Economic Developments in Sweden: January-May 1963," July 2, 1963.

at high levels this year, with the expansion in almost every month exceeding comparable levels recorded in the last five years. From January through August, commercial bank lending rose by 17 per cent, as compared with increases of 3.7 and 6.9 per cent in the corresponding periods in 1961 and 1962. A very large part of this increased lending--almost the entirety in some months this year--was accounted for by the extension of building credits. The remainder reflects higher levels of bank lending to support increased business activity and also, to some extent, the continuing trend toward greater business dependence on bank credit owing to industry's reduced capacity for internal financing.

The expansion of bank credit has been made possible by a reduction in bank holdings of securities and by an unusually heavy volume of borrowing from the central bank. Average bank liquidity has apparently been maintained--though reportedly strained--but some banks are said to be hard pressed to maintain prescribed liquidity quotas. In mid-August the Bank of Sweden issued a strong warning against the dangers of continued rapid credit expansion. The central bank could be expected to take more vigorous anti-inflationary measures if its recent warning to curb excessive bank credit expansion goes unheeded.

Trade gap widens, exchange reserves fall

Although Sweden's external position is basically strong, the trade deficit widened significantly as imports rose while favorable export performance was seriously impeded by the severe icing conditions during the winter. Owing to the slow start, Swedish exports were in fact almost unchanged in value in the first six months of this year, by comparison with January-June 1962, although rapid improvement was made from April onward. However, Swedish exports increased by only 2.3 per cent in the first seven months while imports rose by 8.2 per cent. As a result, Sweden's trade deficit more than doubled, increasing, as mentioned

earlier, from Skr. 409 million (\$79 million) in January-July 1962 to Skr. 947 million (\$183 million) in the first seven months of this year. (See Table 4.)

A small part of this deterioration was due to a slight worsening in Sweden's terms of trade, but the basic explanation lies in rising imports, especially of consumer goods, and in the effects of bad weather on the movement of Swedish exports early in 1963.

Sweden's external position should improve in the months ahead as receipts from exports, tourist travel, and shipping increase seasonally.

The deterioration in Sweden's trade position was reflected in a continuation of the decline in foreign exchange reserves which set in late last year. From a peak level of \$855 million at the end of October 1962, Sweden's gold and foreign exchange holdings had fallen \$82 million by the end of June. Virtually all of this fall in reserves took place in the first quarter of 1963. (See Table 5.) In July, reserves increased for the first time this year, but in August gold and foreign exchange holdings of the Bank of Sweden and the commercial banks declined by \$9 million.

Transactions with U. S. Treasury

In mid-July the Bank of Sweden purchased a \$25 million U. S. Treasury Note (denominated in dollars), maturing in October 1965 but, at the option of the holder, cashable on two-days notice.

Table 4. Sweden: Foreign Trade, 1962-63
(millions of Swedish kronor)

<u>Month or period</u>	<u>Imports</u>		<u>Exports</u>		<u>Trade Surplus (+) or Deficit (-)</u>	
	<u>1962</u>	<u>1963</u>	<u>1962</u>	<u>1963</u>	<u>1962</u>	<u>1963</u>
January	1,415	1,476	1,252	1,370	-163	-106
February	1,220	1,212	1,127	966	- 93	-245
March	1,448	1,337	1,155	1,077	-292	-260
April	1,191	1,527	1,216	1,234	+ 25	-293
May	1,372	1,582	1,388	1,365	+ 16	-217
June	1,234	1,318	1,316	1,467	+ 81	+149
July	1,149	1,312	1,170	1,337	+ 21	+ 25
January-July	9,027	9,764	8,619	8,817	-409	-947

Sources: Monthly Digest of Swedish Statistics, July 1963; Bank of Sweden, Ur tidningarna (daily press releases). Data are not adjusted for seasonal variation.

Table 5. Sweden: Net Reserve Position, 1961-63

	<u>Riksbank</u>	<u>Commercial Banks</u>	<u>Total</u>	<u>Change</u>	
				<u>(in millions of Swedish kronor)</u>	<u>(mill. Kr.)</u>
1961 Dec.	3,318	472	3,790	--	--
1962 June	3,701	474	4,175	+385	+74.4
Oct. <u>1/</u>	3,891	532	4,423	+248	+47.9
Dec.	3,869	492	4,361	- 62	-12.0
1963 Mar.	3,871	147	4,018	-343	-66.3
June	3,809	191	4,000	- 18	- 3.5
July <u>2/</u>	3,826	326	4,152	+152	+29.4
Aug. <u>2/</u>	3,800	304	4,104	- 48	- 9.3

1/ Peak level.

2/ Preliminary; end of July and August data, from Bank of Sweden press releases, differ slightly from classification of other end of month data given in Monthly Digest of Swedish Statistics; the latter are believed to include a small net position in bilateral (nonconvertible) currencies.

Sources: Monthly Digest of Swedish Statistics, July 1963; Bank of Sweden, Ur tidningarna.