



MONETARY POLICY COMMITTEE REPORT TO PARLIAMENT

2017 • 1

Monetary Policy Committee report to Parliament

7 July 2017

The Act on the Central Bank of Iceland stipulates that the Monetary Policy Committee (MPC) of the Central Bank of Iceland shall submit to Parliament (Althingi) a report on its activities twice a year and that the contents of the report shall be discussed in the Parliamentary committee of the Speaker's choosing.

The Act requires that the MPC meet at least eight times each year. Since the last Report was sent to Parliament, the Committee has held four regular meetings, most recently on 14 June 2017. The following report discusses the work of the Committee between January and June 2017.

Monetary policy formulation

According to the Act on the Central Bank of Iceland, the Central Bank's principal objective is to promote price stability. This objective is further described in the joint declaration issued by the Bank and the Icelandic Government on 27 March 2001 as an inflation target of 2½% in terms of the consumer price index. Furthermore, the Act stipulates that the Central Bank shall promote the implementation of the economic policy of the Government as long as it does not consider this policy inconsistent with its main objective of price stability. The Bank shall also promote financial stability. By law, the MPC takes decisions on the application of the Bank's monetary policy instruments; furthermore, the MPC's decisions shall be based on a thorough and careful assessment of developments and prospects for the economy, monetary policy, and financial stability.

In implementing monetary policy, the MPC bases its decisions in part on an analysis of current economic conditions and the outlook for the economy as presented in the Bank's *Monetary Bulletin*. The MPC's statements and minutes, enclosed with this report, contain the arguments for the Committee's decisions in the first half of 2017.

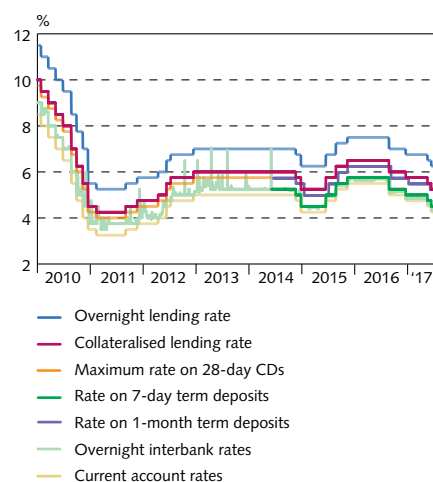
Developments from January to June 2017

The Central Bank's interest rates have been lowered by 0.5 percentage points since the last MPC report was sent to Parliament in January, in addition to a reduction of 0.5 percentage points in the latter half of 2016. At its May meeting, the Committee decided to lower rates by 0.25 percentage points, and in June it lowered them by an additional 0.25 percentage points. At the end of June, the Bank's key interest

Table 1. Central Bank of Iceland interest rates 2017 (%)

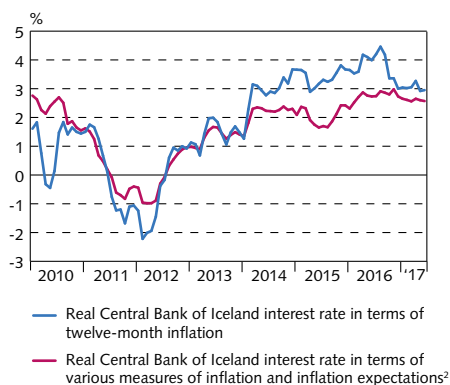
Date	Current accounts	Seven-day term deposits	Collateralised loans	Overnight loans
14 June	4.25	4.50	5.25	6.25
17 May	4.50	4.75	5.50	6.50
15 March	4.75	5.00	5.75	6.75
8 February	4.75	5.00	5.75	6.75

Chart 1
Central Bank of Iceland interest rates and short-term market rates
Daily data 1 January 2010 - 30 June 2017



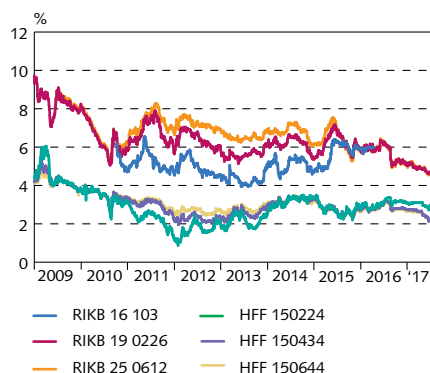
Source: Central Bank of Iceland.

Chart 2
Real Central Bank of Iceland interest rates¹
January 2010 - June 2017



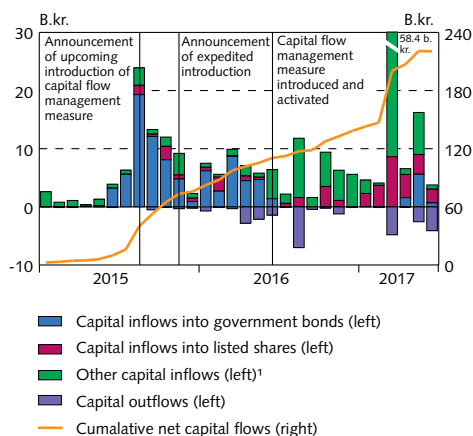
1. From 2010 to May 2014, the nominal policy rate was the average of the current account rate and the maximum rate on 28-day CDs. From May 2014, the policy rate has been the seven-day term deposit rate.
2. Until January 2012, according to twelve-month inflation, one-year business inflation expectations, one-year household inflation expectations, the one-year breakeven inflation rate, and the Central Bank forecast of twelve-month inflation four quarters ahead. From February 2012 onwards, according to the above criteria, plus one-year market inflation expectations based on a quarterly Central Bank survey.
Sources: Gallup, Statistics Iceland, Central Bank of Iceland.

Chart 3
Bond yields
Daily data 2 January 2009 - 30 June 2017



Source: Central Bank of Iceland.

Chart 4
Capital flows due to registered new investments
January 2015- June 2017



1. Other inflows in March 2017 derive almost entirely from non-residents' acquisition of a holding in a domestic commercial bank.
Source: Central Bank of Iceland.

rate – that is, the seven-day term deposit rate – was 4.5%, down from 5.0% at the end of December.¹

In terms of the Central Bank's real interest rate, the monetary stance was virtually unchanged in the first half of the year, in spite of the reduction in the Bank's nominal interest rates. In terms of the average of various measures of inflation and inflation expectations, the Bank's real rate has averaged 2.6% per month in 2017 to date, or 0.1 percentage point less than it was when the last report was sent to Parliament. In terms of twelve-month inflation, the real rate was also broadly unchanged in the first half of the year, at 3%.

Bond market yields developed in line with the Bank's interest rate reductions in the first half of the year. Yields on nominal Treasury bonds fell by 0.2 percentage points in the wake of the Bank's rate cut in May and by up to 0.1 percentage point after the rate cut in June. Yields on the bonds lay in the 4.6-4.7% range at the end of June, or as much as 0.4 percentage points lower than at the end of December. Yields on indexed Treasury and Housing Financing Fund bonds lay in the 2.1-2.9% range at the end of June, or as much as 0.5 percentage points lower than at the end of December. As in the latter half of 2016, the decline in bond yields reflects a reduction in market agents' inflation expectations and their expectations of lower Central Bank rates.

A measure to deter carry trade was in place during the period. It entails imposing a special reserve requirement of 40% for one year at 0% interest on capital inflows invested in listed bonds and high-yielding deposits. Such transactions have been limited since the measure was activated in June 2016. Because of it, monetary policy has been transmitted less through the exchange rate channel than it would have been otherwise, and more through the interest rate channel.

The króna depreciated slightly at the end of 2016 and the beginning of 2017, as a result of the fishermen's strike, and again in March in connection with the step taken towards capital account liberalisation. It began to appreciate again in early April and had strengthened by 12% by mid-June, when it began to weaken again. By 30 June, it had depreciated by roughly 6%. Therefore in trade-weighted terms, it strengthened by 3.7% in the first half of the year, after appreciating by 13.7% in the latter half of 2016. In the first half of 2017, the króna appreciated by 1.1% against the euro, 3.7% against the pound sterling, and 9.2% against the US dollar. As in 2016, the rise in the exchange rate year-to-date mainly reflects developments in economic fundamentals, as can be seen in a trade surplus due to improved terms of trade, growth in exports – tourism in particular – and an improved external debt position.

The main objective of the Central Bank's foreign exchange market intervention policy is to mitigate excess short-term exchange rate volatility. During the run-up to capital account liberalisation, it was also necessary to build up the foreign exchange reserves and to

1. The key rate is the interest rate that is the most important determinant of short-term market rates and therefore is the best measure of the monetary stance. At present, this is the seven-day term deposit rate. Other Central Bank interest rates have been lowered correspondingly, as can be seen in Table 1 and Chart 1.

reduce the risk of a short-term overshooting prior to liberalisation. At its February meeting, after an important step towards liberalisation taken at the beginning of the year, the MPC was of the view that no further build-up of the reserves was necessary and that the risk of a temporary overshooting of the exchange rate prior to full liberalisation had diminished; therefore, there were grounds for somewhat reducing the Bank's intervention in the foreign exchange market. On 14 March 2017, the Bank's new Rules on Foreign Exchange took effect, removing most restrictions on foreign exchange transactions and cross-border movement of capital. Thereafter, the Committee reiterated that the objective of the intervention policy was to mitigate short-term exchange rate volatility and that this entailed not only that the Bank would buy foreign currency, as it had done as a rule since November 2014, but it would also sell foreign currency when conditions warranted it. In the first half of 2017, foreign exchange market flows were more balanced in both directions than in the latter half of 2016. This significantly reduced the appreciation of the króna, and in June the króna weakened slightly. Short-term volatility has increased, however, possibly due to increased movement of capital and to heightened expectations that the exchange rate is close to its peak. Furthermore, the Bank has greatly reduced its foreign exchange market activity. In the first half of 2017, the Bank bought about 75.2 b.kr. in foreign currency from market makers in the foreign exchange market and sold about 5.3 b.kr. Its net purchases in the first half of the year therefore total 69.9 b.kr. The Central Bank's transactions amounted to 32% of total turnover in the foreign exchange market in the first half of the year, as opposed to 57% for the same period in 2016. In March 2017, the Bank sold foreign currency in the market for the first time since November 2014. It sold foreign currency again in June. In all instances, the purpose of the sale was to stop a spiral in the market; i.e., a steep depreciation in which the same small amount was traded like a hot potato among market agents.

Inflation has been below but close to the Central Bank's inflation target for more than three years. Thus far in 2017, it has been broadly as it was in the second half of 2016. Twelve-month inflation in terms of the CPI measured 1.5% in June, down from 1.9% in December 2016. Underlying inflation has subsided considerably year-to-date, however. Most statistical measures of underlying inflation suggest that it was between ½% and 1½% in June, whereas most of the indicators lay in the 2-2.2% range in December (see Chart 6).

The main driver of inflation in the first half of 2017 was the rise in house prices, and the spread between inflation measured with and without the housing component widened significantly. Twelve-month inflation in terms of the CPI excluding housing measured -3.1% in June. Favourable external conditions and the appreciation of the króna have offset the impact of wage costs and domestic demand on inflation, and a tight monetary stance has provided an anchor for inflation expectations. At the same time as local currency import prices have been falling, the rise in domestic prices excluding housing has lost pace. In June, the twelve-month rise measured 0.5%, down from 0.8% in December. The small rise in domestic prices excluding

Chart 5
Exchange rate and volatility of the króna
Daily data 4 January 2010 - 30 June 2017

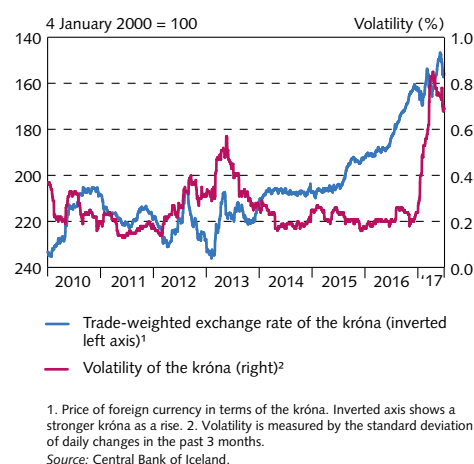


Chart 6
Headline and underlying inflation¹
January 2012 - June 2017

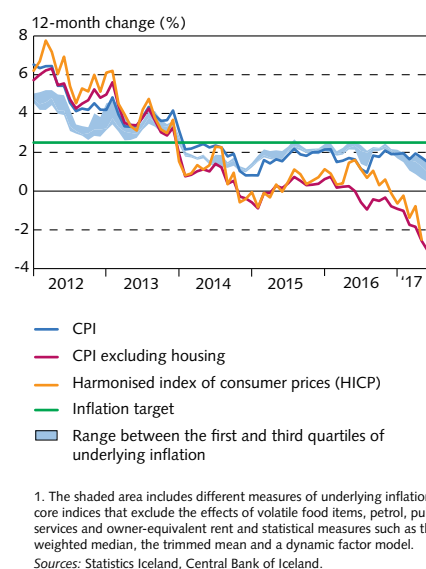


Chart 7
Private services and selected subcomponents of the CPI
January 2012 - June 2017

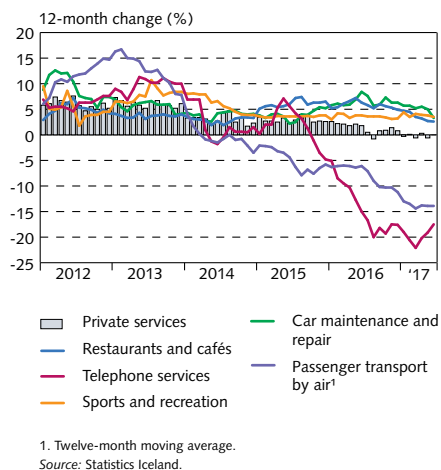
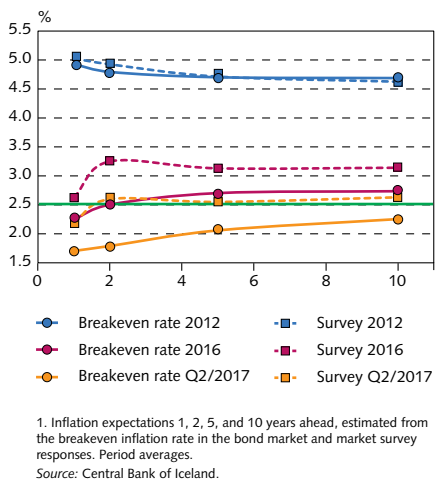


Chart 8
One- to ten-year inflation expectations¹
Period averages



housing is due primarily to a reduction in two private services items: telephone services and airfares. Other labour-intensive items have risen as expected in view of the rise in wage costs, however, the pace of the increase has eased in the past few months (see Chart 7).

According to the Bank's baseline forecast, published in *Monetary Bulletin* on 17 May 2017, inflation will remain in the 2-3% range for the remainder of the forecast horizon, which extends through mid-2020. This reflects the offsetting impact of a rising exchange rate on ISK prices of imports and the impact of domestic inflationary pressures from the real estate and labour markets.

Inflation expectations appear to be even more firmly anchored to the target since the last report was sent to Parliament. Both short- and long-term expectations have subsided and now measure at or slightly below the inflation target. They also withstood increased exchange rate volatility concurrent with the removal of capital controls in mid-March. According to recent surveys, market agents and corporate executives expect inflation to measure at or below 2% in one year's time. Households expect inflation to measure 2.5% after one year. The one-year breakeven inflation rate in the bond market measured 1.6% at the end of June, down from 2.3% in December. Market agents expect inflation to average 2.6% in the next ten years, about 0.2 percentage points lower than they did in November 2016. At the end of June, the five- and ten-year breakeven inflation rate measured 2-2.3%.

Tight monetary policy has anchored inflation expectations, encouraged saving, and contained credit growth. Clear signs of demand pressures in the economy call for a continued tight monetary stance, however, so as to ensure medium-term price stability. The reduction in inflation expectations in May and June led to a rise in the Bank's real rate, however. The increase entailed somewhat tighter stance than the MPC had intended and had considered sufficient to promote price stability. As a result, MPC members agreed to lower nominal interest rates at the May and June meetings. The Committee was of the view that in the coming term, the monetary stance will be determined by economic developments and actions taken in other policy spheres.

Accompanying documents

The following documents are enclosed with this report:

1. Monetary Policy Committee statements from January to June 2017.
2. Minutes of Monetary Policy Committee meetings from January to June 2017.
3. Chief Economist's speech on the economy and monetary policy, delivered at a meeting of the Kópavogur Rotary Club on 21 February 2017.
4. Chief Economist's speech on economic developments and prospects, delivered to the Leftist-Green Party caucus on 27 March 2017.

5. "Everything you wanted to know about the exchange rate of the króna": speech given by the Chief Economist on 16 March 2017, Tourism Day, in Harpa Conference Centre in Reykjavík.
6. Joint declaration by the Government and the Central Bank on inflation targeting, March 2001.

On behalf of the Central Bank of Iceland Monetary Policy Committee,



Már Guðmundsson

*Governor of the Central Bank of Iceland
and Chair of the Monetary Policy Committee*

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Statement of the Monetary Policy Committee 8 February 2017

The Monetary Policy Committee (MPC) of the Central Bank of Iceland has decided to keep the Bank's interest rates unchanged. The Bank's key interest rate – the rate on seven-day term deposits – will therefore remain 5%.

Year-2016 GDP growth is estimated at 6%, a full percentage point above the forecast in the November *Monetary Bulletin*, owing mainly to stronger-than-projected business investment and services exports in the first nine months of the year. Growth is expected to remain rapid, measuring 5⅓% in 2017 and in the 2½-3% range in the two years thereafter. Job creation is strong, unemployment is below 3%, and the labour participation rate has risen above the pre-crisis peak. Even though importation of foreign labour pulls in the opposite direction, demand pressures in the economy are growing and will be stronger than previously projected.

The inflation outlook has improved slightly since the November forecast, in spite of a widening output gap. It is based, however, on the assumption that wage agreements will not be up for negotiation in the near future. This is highly uncertain, however. Domestic inflationary pressures have been offset by low global inflation, the appreciation of the króna during the forecast horizon, and a tight monetary stance. Monetary policy has anchored inflation expectations, contained credit growth, and contributed to more saving than would otherwise have occurred.

The exchange rate of the króna has fallen since the MPC's last meeting, after a steep rise for most of the latter half of 2016. Short-term volatility year-to-date has also been somewhat more pronounced than in the previous two years. The aim is to reduce short-term fluctuations in the near term, in line with the objective of mitigating exchange rate volatility. The Bank's transactions in the foreign exchange market will also take into consideration that there is no longer a need to build up the foreign exchange reserves further and that the risk of a temporary overshooting of the exchange rate during the run-up to capital account liberalisation has diminished in the wake of the recent completion of major milestones in the liberalisation process.

Rapid growth in economic activity and clear signs of growing demand pressures in the economy call for a tight monetary stance to ensure medium-term price stability. A stronger anchor for inflation expectations at target and the appreciation of the króna have enabled the MPC to achieve its legally mandated price stability objective with a lower interest rate than would otherwise have been possible. Strong

growth in demand and unrest in the labour market call for caution in interest rate setting. The monetary stance in the coming term will be determined by economic developments and actions taken in other policy spheres.

Statement of the Monetary Policy Committee 15 March 2017

The Monetary Policy Committee (MPC) of the Central Bank of Iceland has decided to keep the Bank's interest rates unchanged. The Bank's key interest rate – the rate on seven-day term deposits – will therefore remain 5%.

According to national accounts figures from Statistics Iceland, GDP growth measured 7.2% in 2016, a full percentage point more than was projected in the February issue of *Monetary Bulletin*. The deviation from the forecast is attributable largely to stronger-than-projected services exports and private consumption. Indicators imply continued strong growth thus far in 2017. Job creation is strong, unemployment is low, and the labour participation rate has risen above the pre-crisis peak. Even though importation of foreign labour pulls in the opposite direction, demand pressures in the economy are growing.

Inflation measured 1.9% in February, broadly similar to the level in the past six months. As before, the inflation outlook reflects two offsetting forces. GDP growth has turned out stronger than previously forecast, but the exchange rate of the króna is higher. The currency appreciation and low global inflation continue to offset domestic inflationary pressures, and the gap between domestic price developments – housing costs in particular – and external factors has widened. In addition, a tight monetary stance has anchored inflation expectations and contained both credit growth and demand growth.

It is too early to predict the economic impact of the most recent steps in the capital account liberalisation process. It is possible that a better balance will develop between foreign exchange market inflows and outflows, but short-term volatility could increase, as appears to have happened in the past few days. The Central Bank will continue to mitigate short-term volatility when conditions warrant it.

Rapid growth in economic activity and clear signs of demand pressures in the economy call for a tight monetary stance so as to ensure medium-term price stability. On the other hand, uncertainty in the labour market has abated.

A stronger anchor for inflation expectations at target and the appreciation of the króna have enabled the MPC to achieve its legally mandated price stability objective with a lower interest rate than would otherwise have been possible. The monetary stance in the coming term will be determined by economic developments and actions taken in other policy spheres.

Statement of the Monetary Policy Committee 17 May 2017

The Monetary Policy Committee (MPC) of the Central Bank of Iceland has decided to lower the Bank's interest rates by 0.25 percentage points. The Bank's key interest rate – the rate on seven-day term deposits – will therefore be 4.75%.

The outlook is for strong GDP growth this year, as in 2016, with growth for both years exceeding the February forecast. The deviation from the forecast stems mainly from stronger-than-expected growth in tourism, while there is also the prospect of more fiscal easing in 2017 than was previously projected. Demand pressures in the labour market and the general economy have therefore grown despite increased importation of labour and strong productivity growth. This is offset by the appreciation of the króna. The króna has played a key role in the economy's adjustment to positive shocks deriving from improved terms of trade and growth in the tourism sector.

Inflation measured 1.9% in April, broadly similar to the level in the past six months. Underlying inflation appears to have declined in recent months, however. The currency appreciation and low global inflation continue to offset domestic inflationary pressures, and the gap between domestic price developments – housing costs in particular – and external factors has widened even further since the MPC's last meeting. Two opposing forces affect the inflation outlook. Demand pressures in the economy have turned out stronger than previously forecast, but they are offset by the higher exchange rate. The inflation outlook has improved for 2017 and 2018 but has deteriorated further out the forecast horizon.

Clear signs of increased demand pressures in the economy call for a tight monetary stance so as to ensure medium-term price stability. The Central Bank's real rate has risen slightly since the MPC's last meeting. The appreciation of the króna also contains demand.

The Central Bank has scaled down its intervention in the foreign exchange market in view of its strong foreign exchange reserves, as the appreciation of the króna is considered to reflect economic fundamentals. As before, the Bank will intervene in the market in order to mitigate volatility when it considers such intervention warranted.

A stronger anchor for inflation expectations at target and the appreciation of the króna have enabled the MPC to achieve its legally mandated price stability objective with a lower interest rate than would otherwise have been possible. The monetary stance in the coming term will be determined by economic developments and actions taken in other policy spheres.

Statement of the Monetary Policy Committee 14 June 2017

The Monetary Policy Committee (MPC) of the Central Bank of Iceland has decided to lower the Bank's interest rates by 0.25 percentage points. The Bank's key interest rate – the rate on seven-day term deposits – will therefore be 4.5%.

The outlook is for strong GDP growth in 2017, as in recent years. That outlook has changed little from the Bank's last forecast, and GDP growth in Q1 was broadly consistent with the forecast. As before, GDP growth is driven in particular by rapid growth in tourism and private consumption; furthermore, the outlook is for considerable fiscal easing this year.

Inflation is still broadly as it has been over the past half-year, but underlying inflation appears to have subsided in recent months. In addition, both short- and long-term inflation expectations have continued to fall since the MPC's last meeting, and the Bank's real rate has risen. As before, opposing forces affect the inflation outlook, with the appreciation of the króna and low global inflation offsetting domestic inflationary pressures. The gap between domestic price developments – housing costs in particular – and external factors has widened significantly in recent months.

Clear signs of demand pressures in the economy call for a tight monetary stance so as to ensure medium-term price stability. However, the increase in the Bank's real rate since the last MPC meeting entails a somewhat tighter stance than the Committee both had intended and considers sufficient to support price stability.

A stronger anchor for inflation expectations at target and the appreciation of the króna have enabled the MPC to achieve its legally mandated price stability objective with a lower interest rate than would otherwise have been possible. The monetary stance in the coming term will be determined by economic developments and actions taken in other policy spheres.



The Monetary Policy Committee of the Central Bank of Iceland

Minutes of the Monetary Policy Committee meeting, February 2017

Published 22 February 2017

The Act on the Central Bank of Iceland stipulates that it is the role of the Monetary Policy Committee (MPC) to set Central Bank interest rates and apply other monetary policy instruments. Furthermore, the Act states that “[m]inutes of meetings of the Monetary Policy Committee shall be made public, and an account given of the Committee’s decisions and the premises upon which they are based.” In accordance with the Act, the MPC has decided to publish the minutes of its meetings two weeks after each interest rate decision. The votes of individual Committee members will be made public in the Bank’s *Annual Report*.

The following are the minutes of the MPC meeting held on 6 and 7 February 2017, during which the Committee discussed economic and financial market developments, the interest rate decision of 8 February, and the communication of that decision.

I Economic and monetary developments

Before turning to the interest rate decision, members discussed the domestic financial markets, financial stability, the outlook for the global economy and Iceland’s international trade, the domestic economy, and inflation, with emphasis on information that has emerged since the 14 December interest rate decision, as published in the updated forecast in *Monetary Bulletin* 2017/1 on 8 February.

Financial markets

After a protracted appreciation phase, the króna began to weaken in early December and, by end-January, had depreciated by about 5% in trade-weighted terms. It then turned around and, by the time of the February meeting, was 2.3% above the January trough, although it remained 2.5% lower in trade-weighted terms than at the time of the December meeting. Over the same period, it had depreciated by 2.6% against the euro, and 2.1% against the US dollar, whereas it had risen by 0.6% against the pound sterling. The Central Bank’s net foreign currency purchases in the domestic foreign exchange market totalled approximately 186 million euros (roughly 22.3 b.kr.) between meetings, or 34% of total market turnover.

In terms of the Central Bank’s real interest rate, the monetary stance was broadly the same as after the December interest rate reduction. In terms of the average of various measures of inflation and inflation expectations, the Bank’s real rate was unchanged between meetings, at about 2½%.

Interest rates in the interbank market for krónur had developed in line with the Bank's key rate. Yields on nominal Treasury bonds and indexed Treasury and Housing Financing Fund (HFF) bonds were broadly unchanged between meetings but have fallen in the recent term, in line with the Bank's key rate. Most financial institutions' non-indexed deposit and lending rates had fallen in the wake of the December interest rate reduction, while indexed rates remained unchanged.

Risk premia on Treasury foreign obligations were broadly unchanged between meetings, even though Standard & Poor's had upgraded Iceland's sovereign credit rating to A- and Fitch Ratings had changed the outlook on Iceland's sovereign ratings to positive in mid-January. The CDS spread measured about 0.9%, but the spread between the Treasury's foreign currency issues and comparable bonds issued by Germany and the US was 1.1-1.2 percentage points.

Financial institutions' analysts had all projected that the Bank's nominal policy rate would be held unchanged in February, and they agreed that the depreciation of the króna had reduced the likelihood of a rate cut. They also noted that GDP growth had been strong and that uncertainty remained in the labour market. In most analysts' view, the króna would probably appreciate over the course of 2017, which could give cause for further rate cuts during the year.

According to the Central Bank's market expectations survey, conducted at the end of January, respondents expected the Bank's key rate to be lowered by 0.25 percentage points during the first half of 2017 and then raised again to 5% at the beginning of 2018, after which it would remain unchanged for the rest of the forecast horizon. In the survey, market agents were also asked what they considered an appropriate Central Bank key rate at present. Answers ranged between 3.5% and 5.5%, with over half of them in the 4.75-5% range; i.e., at or 0.25 percentage points below the current rate. Just under a fifth of survey participants considered 4.5% appropriate.

Year-on-year growth in M3 accelerated in Q4/2016 in comparison with the previous two quarters but was still below nominal GDP growth. M3 grew by 5.9% year-on-year in Q4/2016, after adjusting for deposits held by deposit institutions in winding-up proceedings. As was the case last year, growth in money holdings is due largely to increased household deposits, although corporate deposits also increased between years.

After adjusting for the Government's debt relief measures, the total stock of credit system loans to resident borrowers grew by just over 2% year-on-year in nominal terms in Q4, and by just under 4% after adjusting for the effects of exchange rate movements on the foreign-denominated credit stock. Growth is attributable to an increase in lending to households and businesses. Pension fund loans to households have increased significantly in the past year, and the pension funds' share of new household lending now exceeds that of deposit institutions. On the other hand, HFF lending has continued to contract. Therefore, credit system lending to households is still modest overall. In Q4/2016, the year-on-year increase measured 2.8%, after adjusting for the Government's debt relief measures.

The Nasdaq OMXI8 index had fallen by 3.8% between meetings and by 9% in 2016. Turnover in the main market was just over 560 b.kr. in 2016, or about 43% more than in 2015. Equity securities prices fluctuated widely shortly before the MPC meeting, after Icelandair published a profit warning.

Global economy and external trade

The global economic outlook was broadly unchanged since the Committee's December meeting, with the new US administration's fiscal and trade policy considered the predominant

uncertainty. According to the International Monetary Fund's January forecast, global GDP growth is projected at 3.4% in 2017 and 3.6% in 2018, which is unchanged from the Fund's October forecast. The forecast for growth in world trade was also unchanged for 2017, whereas the 2018 projection has been revised slightly downwards since October. The inflation outlook for industrialised countries is unchanged as well, with inflation forecast at 1.7% this year and 1.9% in 2018. In emerging and developing countries, however, inflation is expected to be somewhat higher in both 2017 and 2018 than in the October forecast. *Consensus Forecasts'* year-2017 GDP growth and inflation projections for Iceland's main trading partners were unchanged between MPC meetings.

The deficit on goods trade totalled 8.4 b.kr. in December. According to preliminary figures from Statistics Iceland, it measured 6.6 b.kr. in January. The deficit totalled 101.2 b.kr. in 2016 and 33.7 b.kr. in 2015. Import values rose by 8.6% year-on-year in 2016, whereas export values contracted by 4.1%. Import growth in 2016 was due mainly to an increase in imports of transport equipment and consumer goods, while the contraction in exports stemmed mainly from reduced exports of industrial goods.

The listed global market price of aluminium had risen by about 3,1% between MPC meetings, and the average price in January was up about 20.7% year-on-year. This was the largest year-on-year increase since July 2011. In December, foreign currency prices of marine products rose by about 1.1% between months and 6.4% between years. In all, marine product prices rose by nearly 4.3% year-on-year in 2016.

In terms of relative consumer prices, the real exchange rate measured 96.7 points in January, a 2.8% decline from the previous month but a 15.5% increase year-on-year. The rise is due primarily to a 15.7% nominal appreciation of the króna, but in addition, inflation in Iceland was about 0.1 percentage point below the average among its trading partners. In terms of relative consumer prices, the real exchange rate rose by an average of 12.8% in 2016.

The domestic real economy and inflation

According to the 2017 National Budget, the fiscal stance will ease this year, but somewhat less than was projected in the Bank's November forecast. The easing is estimated at 0.5% of GDP, as opposed to an estimate of 0.9% in November. The new Government's fiscal strategy for the upcoming five years was presented at the end of January. Even though it is assumed that the Treasury will be operated at a surplus this year, the fiscal strategy entails some fiscal easing when cyclical adjustments have been made. According to the Bank's February forecast, the 2017 outcome would have needed to be ½% of GDP more favourable than is implied in the strategy in order to maintain the same fiscal stance as in 2016. In 2018, the outcome is expected to improve by ½% of GDP, and if this materialises, the fiscal stance will then be similar to that in 2016.

According to Statistics Iceland's labour force survey (LFS) for Q4/2016, the number of jobs increased year-on-year by 4.6%, much more than was assumed in the Bank's November forecast. The average work week continued to grow shorter, however, and total hours worked increased by 4.1%, in line with the forecast. Total hours worked rose by 3% between yearly averages.

The labour participation rate rose sharply during the year. By Q4/2016 it was above its pre-crisis peak, and the employment rate was very close to its pre-crisis high. The labour participation rate rose by 1 percentage point year-on-year and the employment rate by 1.8 percentage points.

Unemployment was somewhat lower in Q4 than the Bank had forecast in November, at 2.5%, or 2.9% when adjusted for seasonality. The seasonally adjusted unemployment rate is at its lowest since Q3/2008. Measured unemployment was 3% in 2016 as a whole, as opposed to 4% in 2015. Unemployment as measured by the Directorate of Labour (DoL) measured 2.1% in 2015 and had fallen by just over half a percentage point between years.

In 2016, immigrants outnumbered emigrants by just over 4,000, or 2% of the labour force. In 2016, the migration balance among foreign nationals aged 20-59 was positive by 2% of the population aged 20-59, up from 1.3% in 2015.

In Q4/2016, the wage index rose by 1% between quarters and by 9.7% year-on-year. Real wages in terms of the index were 7.7% higher in Q4/2016 than in Q4/2015. Neither nominal nor real wages have ever risen as much in terms of the wage index as they did in 2016, when the index rose by 11.4% real wages by 9.5% between yearly averages.

Key indicators of developments in private consumption in Q4/2016 suggest that year-on-year growth was moderate but somewhat weaker than it had been earlier in the year. This development is in line with the Bank's private consumption growth forecast. Payment card turnover increased by nearly 8% during the quarter and nearly 12½% over the year as a whole. Similar developments can be seen in new motor vehicle registrations, which increased by just over a fifth during the quarter and by 38.5% during the year.

The Gallup Consumer Confidence Index declined between months in both December and January. In January, it declined between years for the first time since 2014 but nonetheless measured 121.6 points, and all of its components measured over 100 points.

The Statistics Iceland's nationwide house price index, published at the end of January, rose by 1.1% month-on-month after adjusting for seasonality, and by 15.2% year-on-year. The capital area real estate price index, calculated by Registers Iceland, rose by 1% month-on-month in December when adjusted for seasonality, and by 15% year-on-year. In 2016, the index rose by an average of 11.1% from the previous year, and the number of registered purchase agreements nationwide rose 7.8% between years. The average time-to-sale for residential property in the greater Reykjavík area declined by just over a month between 2015 and 2016, to just under 2 months.

The CPI rose by 0.14% month-on-month in December and then fell by 0.6% in January. Twelve-month inflation measured 1.9% in January, down from 2.1% at the time of the MPC's December meeting. The CPI excluding the housing component had declined by 0.9% in the past twelve months, however. Most measures of underlying inflation suggested that it had declined in January and lay in the 1.7-2.1% range.

Winter sales were the major determinant of inflation in January, although they were offset by an increase in the cost of owner-occupied housing and in various public levies. Private services prices had fallen by 0.3% year-on-year in January, after having risen in the two preceding months: by 0.8% in December and by 1.4% in November.

According to the Central Bank's survey of market agents' inflation expectations, conducted at the end of January, participants expect inflation to measure 2.5% in one year, an increase of 0.3 percentage points from the previous survey, taken in November 2016. Survey participants' inflation expectations two years ahead had declined, however, from 3% in the last survey to 2.8%. Furthermore, market agents expect inflation to average 2.7% over the next ten years, or 0.1 percentage points less than in the November survey. The ten-year breakeven inflation rate in the bond market had measured in the 2.1-2.5% range during the quarter to date, as opposed to 3% in Q1/2016.

According to the forecast published in *Monetary Bulletin* on 8 February 2017, the inflation outlook has improved since the Bank's November forecast. Domestic inflationary pressures are considerable, however, and stronger than was forecast in November. Pulling in the other direction are low global inflation and the appreciation of the króna. The króna is projected to be stonger during the forecast horizon than was assumed in the November forecast. The inflation outlook has therefore improved slightly, in spite of the prospect of a larger output gap. Inflation is projected to measure about 2% through mid-2017 and then inch upwards, reaching the target in the latter half of 2018. It looks set to rise temporarily above target as the forecast horizon progresses, once the effects of the higher exchange rate subside, but to be close to target by the end of the horizon.

GDP growth is considered to have picked up slightly in leading advanced economies in the latter half of 2016, and there is increased optimism about the global economy. Oil and major commodity prices have risen, and global inflation is on the rise. Increased optimism about the economic outlook and expectations of higher inflation have led to a marked increase in long-term interest rates in the US, with rates in other developed countries following suit.

In spite of the rise in oil and commodity prices, the outlook is for a further improvement in Iceland's terms of trade this year. Indeed, improved terms of trade and rapid growth in tourism have been the main drivers of Iceland's economic recovery. Icelandic exports are estimated to have grown by just over 10% in 2016. Of that total, activity in the tourism industry grew by over 37% in real terms and has nearly quadrupled 2010.

Year-2016 GDP growth is estimated at 6%, a full percentage point more than was assumed in the November *Monetary Bulletin*. The deviation is due primarily to business investment and services exports, both of which were much stronger in the first nine months of the year. Furthermore, GDP growth is expected to be strong again this year, or around 5½%, but to ease towards the 2½-3% range over the next two years. GDP growth both in 2016 and over most of the forecast horizon is somewhat stronger than was forecast in November and will therefore put greater strain on domestic resources and result in a wider output gap. The labour market will be tighter, with rapid job creation and unemployment below 3%. The labour participation rate has also risen above its pre-crisis peak, albeit offset by significant importation of foreign labour. The pay increases provided for in wage agreements have shown in the Statistics Iceland wage index, as was assumed in the Bank's November forecast, and wage drift has been broadly as projected. On the other hand, wages are expected to rise this year by about ½ a percentage point more than was forecast in November, in part because of newly approved wage settlements. Unit labour costs will therefore rise by about 4% this year, on the heels of a 6½-7% increase in the past two years. Unit labour costs are also projected to rise significantly in the next two years, by an average of roughly 5% per year.

According to the forecast, the slack in the economy is considered to have disappeared some time ago and a growing positive output gap has begun to open up. The output gap is estimated to have widened over the course of 2016, to about 2.2% of potential output. The outlook is for it to grow still further this year and become wider than was forecast in November, as GDP growth in 2016 and 2017 is projected to be somewhat stronger than was assumed in the November forecast. As in the Bank's previous forecasts, the output gap is expected to narrow in coming years as GDP growth subsides.

II The interest rate decision

The Governor updated the Committee on developments in connection with capital account liberalisation and on the preparation for the planned review of the monetary policy framework.

The Committee discussed the Bank's foreign exchange market intervention policy. Furthermore, on 23 December, it had held an extraordinary meeting on foreign exchange issues, where members agreed with the Governor's proposal to step up foreign currency purchases if needed so as to lean against the appreciation of the króna just before important steps were taken towards capital account liberalisation at the beginning of 2017. Members considered it timely to review the Bank's intervention policy in the wake of the significant easing of capital controls on individuals and companies at the turn of the year. They agreed that the experience of this had been positive, as no instability had been detected. Capital outflows had not been substantial as yet. This could have played some part in the depreciation of the króna in December and January, but Committee members were of the view that the main causes were the seasonal drop in tourism-generated foreign exchange revenues and the fishermen's strike. Short-term volatility – intraday fluctuations in particular – had been greater year-to-date than in the previous two years. The Committee was also of the view that the risk of a temporary overshooting of the exchange rate prior to full liberalisation had diminished after these steps were taken. Furthermore, there was currently no need to build up the foreign exchange reserves further. Because there was no longer a need to take these temporary factors into account, the MPC decided that the objective of intervention in the foreign exchange market in the near future would be to mitigate short-term volatility. Committee members were of the view that the intervention policy should include not only buying foreign currency, as the Bank had done in the recent past, but also selling it if conditions warranted it. It was emphasised that this must not be interpreted to mean that the Bank was targeting a particular exchange rate. It was pointed out that it was not desirable to disconnect price formation of the króna in the market entirely. The exchange rate must be allowed to move and to play a role in the adjustment of the economy.

The MPC also discussed the findings of a recent working paper that estimated the equilibrium real interest rate in Iceland using different methods. During the discussions at the meeting, Committee members expressed a range of views, both on what the equilibrium real rate could be at present and on the methods used to estimate it. Members agreed, however, that the equilibrium real rate had declined after inflation expectations became more firmly anchored, and that the research findings provided useful input for continued discussion within the Committee.

The MPC also examined the current Central Bank interest rate in relation to a number of different monetary policy rules. The results showed that the current rate was within the range given by different monetary policy rules and various assumptions concerning the equilibrium rate.

The monetary stance had remained unchanged since the December meeting. Committee members discussed whether developments since the previous meeting had changed its assessment of whether the monetary stance was appropriate and whether the outlook had changed. At the December meeting, the MPC had decided to lower the Bank's interest rates by 0.25 percentage points. The majority's arguments for the December decision were that there was scope to lower nominal interest rates, as inflation expectations appeared more firmly anchored to target, and that the appreciation of the króna had tightened the monetary stance

somewhat. However, the minority view was that it was imprudent to lower interest rates further because of the risk of overheating in the economy.

In this context, MPC members took account of the Central Bank's new forecast, published in *Monetary Bulletin* on 8 February, estimating that year-2016 GDP growth had been very strong, and well above the Bank's November forecast, owing mainly to stronger-than-projected business investment and services exports. They also took note of the forecast of continued rapid GDP growth. The MPC also noted the marked tension in the labour market and the outlook for lower unemployment than had previously been forecast. In particular, the Committee considered that the output gap was growing and appeared likely to be wider than previously projected in spite of the offsetting impact of labour importation.

Committee members agreed with the assessment in the forecast that the inflation outlook had improved slightly since the November forecast, even though the output gap was wider. They also observed that domestic inflationary pressures were offset by low global inflation, the appreciation of the króna during the forecast horizon, and a tight monetary stance.

In the MPC's view, uncertainty about the fiscal stance had subsided since the Committee's last meeting because the 2017 National Budget had been approved. According to the budget, the fiscal stance will ease in 2017, but less than had been assumed in the November forecast. The Government's five-year fiscal strategy includes plans to reverse this easing in 2018.

All members considered it appropriate to keep the Bank's interest rates unchanged. In their view, rapid growth in economic activity and clear signs of growing demand pressures in the economy called for a continued tight monetary stance so as to ensure medium-term price stability. Although the November forecast indicated that the inflation outlook had improved somewhat, this assessment was based on the assumption that wage agreements would not be reviewed in the near future, a premise that MPC members agreed was highly uncertain. This uncertainty and strong growth in demand called for caution in setting interest rates.

In view of the discussion, the Governor proposed that the Bank's interest rates be held unchanged. The Bank's key rate (the seven-day term deposit rate) would remain 5%, the current account rate 4.75%, the seven-day collateralised lending rate 5.75%, and the overnight lending rate 6.75%. All Committee members voted in favour of the proposal.

Members were of the view that monetary policy had anchored inflation expectations, contained credit growth, and contributed to more saving than would otherwise have occurred. They agreed that a stronger anchor for inflation expectations at target and the appreciation of the króna had enabled the MPC to achieve its legally mandated price stability objective at a lower interest rate than would otherwise have been possible. This had made it possible for the MPC to lower interest rates in the latter half of 2016. Members agreed that in the coming term, the monetary stance would be determined by economic developments and actions taken in other policy spheres.

The following Committee members were in attendance:

Már Gudmundsson, Governor and Chairman of the Monetary Policy Committee

Arnór Sighvatsson, Deputy Governor

Thórarinn G. Pétursson, Chief Economist

Gylfi Zoëga, Professor, external member

Katrín Ólafsdóttir, Assistant Professor, external member

In addition, a number of Bank staff members attended part of the meeting.

Rannveig Sigurdardóttir wrote the minutes.

The next Statement of the Monetary Policy Committee will be published on Wednesday 15 March 2017.



The Monetary Policy Committee of the Central Bank of Iceland

Minutes of the Monetary Policy Committee meeting, March 2017

Published 29 March 2017

The Act on the Central Bank of Iceland stipulates that it is the role of the Monetary Policy Committee (MPC) to set Central Bank interest rates and apply other monetary policy instruments. Furthermore, the Act states that “[m]inutes of meetings of the Monetary Policy Committee shall be made public, and an account given of the Committee’s decisions and the premises upon which they are based.” In accordance with the Act, the MPC has decided to publish the minutes of its meetings two weeks after each interest rate decision. The votes of individual Committee members will be made public in the Bank’s *Annual Report*.

The following are the minutes of the MPC meeting held on 13 and 14 March 2017, during which the Committee discussed economic and financial market developments, the 15 March interest rate decision, and the communication of that decision.

I Economic and monetary developments

Before turning to the interest rate decision, members discussed the domestic financial markets, financial stability, the outlook for the global economy and Iceland’s international trade, the domestic economy, and inflation, with emphasis on information that has emerged since the 8 February 2017 interest rate decision.

Financial markets

When the liberalisation of capital controls was announced on Sunday 12 March, the exchange rate of the króna had risen by approximately 6.1% in trade-weighted terms since the Committee’s February meeting. The day after, however, the exchange rate fell by 2.7% in trade-weighted terms and by 0.7% on 14 March. Between meetings, the króna therefore appreciated by 2.4% in trade-weighted terms. Over the same period it had risen by 2% against the euro, 1.7% against the US dollar, and 3.8% against the pound sterling.

The Central Bank’s net foreign currency purchases totalled approximately 318 million euros (36.7 b.kr.) between meetings, or 46% of total market turnover. After the announcement of liberalisation measures on Sunday 12 March, there was some volatility in the foreign exchange market, and the Central Bank traded on both buying and selling sides. The Bank had also sold foreign currency on 7 March, but that was the first time since November 2014 that it had sold currency in the interbank foreign exchange market.

In terms of the Central Bank's real interest rate, the monetary stance was broadly unchanged since the MPC's February meeting, and the Bank's real rate was 2.5% in terms of the average of various measures of inflation and inflation expectations.

Interest rates in the interbank market for krónur were virtually unchanged between meetings. Turnover in the market totalled 69 b.kr. and had been considerably greater year-to-date than over the same period in 2016. Yields on Treasury and Housing Financing Fund (HFF) bonds had fallen by up to 0.3 percentage points between meetings. At the time of the MPC meeting, the authorities' announcement on liberalisation had not yet had a significant impact on these yields. Furthermore, financial institutions' deposit and lending rates were virtually unchanged since the February meeting.

Risk premia on Treasury foreign obligations were broadly unchanged between meetings. The CDS spread on the Treasury's five-year US dollar obligations measured 0.9%, and the spread vis-à-vis comparable bonds issued by Germany and the US was 1-1.1 percentage points.

Financial institutions' analysts expected either no change or a 0.25 percentage point interest rate reduction, but all of them agreed that the decision was uncertain. Those expecting a rate cut cited the appreciation of the króna between meetings and the reduced uncertainty in the labour market. Those expecting no change based their projections on the newly published national accounts, which indicated that GDP growth had been much stronger and the output gap much wider in 2016 than had been assumed in the Central Bank's February forecast. Analysts' forecasts were published before the authorities announced the capital account liberalisation measures, but afterwards those who had expected a rate cut said that the likelihood of a reduction had receded.

M3 grew by 3.3% year-on-year in January, after adjusting for deposits held by deposit institutions in winding-up proceedings. This is somewhat weaker growth than in the preceding three months, as financial sector deposits contracted between years and annual growth in households' and businesses' deposits was also somewhat less in January than in the months beforehand.

After adjusting for the Government's debt relief measures, the total stock of credit system loans to resident borrowers grew by about 3% year-on-year in January, and by roughly 4½% after adjusting for the effects of exchange rate movements on the foreign-denominated credit stock. Growth is attributable to an increase in lending to households and businesses. Annual growth in credit system lending to households measured 3% in January after adjusting for the Government's debt relief measures.

The Nasdaq OMXI8 index had risen by 5.2% between meetings and by 0.6% since the beginning of the year. Turnover in the Nasdaq Iceland main market totalled just over 135 b.kr. over the first two months of the year, about 20% more than over the same period in 2016.

Global economy and external trade

Iceland's external goods trade generated a deficit of 19.5 b.kr. for the first two months of the year, as opposed to a deficit of 3.9 b.kr. over the same period in 2016. Export values contracted by 7.2% year-on-year at constant exchange rates, while import values rose 13.3%. The export value of marine products declined by 33% year-on-year, while the export value of industrial goods rose by nearly 9%. Import growth is due in particular to a year-on-year increase of 20% or more in imports of transport equipment, commodities, and operational inputs.

The listed global market price of aluminium had risen by 6% between meetings, and the average February price was up over 20% year-on-year. On the other hand, foreign currency prices of marine products had risen by 1% month-on-month and about 8% year-on-year in January. Oil prices had declined by 9% between meetings, after having held relatively stable since early December.

In terms of relative consumer prices, the real exchange rate measured 99.4 points in February, an increase of 2.5% month-on-month and 18.1% year-on-year. The increase is due primarily to a 17.8% nominal appreciation of the króna, but in addition, inflation in Iceland was about 0.3 percentage points above the average among its trading partners.

The domestic real economy and inflation

According to preliminary figures published by Statistics Iceland in March, GDP growth measured 11.3% in the fourth quarter of 2016. Domestic demand grew 8.4% year-on-year during the quarter. Of that total, consumption and investment grew by a total of 8.2%, and the contribution from inventory changes was slightly positive. Exports grew by about 14%, somewhat outpacing import growth; therefore, the contribution from net trade was positive during the quarter.

For the year as a whole, GDP growth measured 7.2% and was driven mainly by private consumption and business investment. Domestic demand grew by 8.7% during the year, but the contribution from net trade was negative by 0.8 percentage points in spite of strong export growth. GDP growth turned out much stronger than the 6% forecast in the February *Monetary Bulletin*. Domestic demand growth was well in line with the February forecast, however, which assumed 8.4% growth. Private consumption grew more than was forecast, while investment grew less. The main reason for the deviation is that external trade was expected to be a much greater drag on GDP growth than Statistics Iceland's figures indicate. Imports were weaker and exports stronger than was assumed in the February forecast.

The current account balance was positive by 194 b.kr., or 8% of GDP, in 2016. Only once before has Iceland's current account surplus measured as large: in 2009, when it was also 8% of GDP. The surplus on goods and services trade was smaller in 2016 than in 2015; however, the balance on primary and secondary income was considerably more favourable. The forecast in the February *Monetary Bulletin* assumed that the current account surplus would amount to 6.4% of GDP in 2016. The deviation is due to a more favourable balance on services than had been expected, plus greater returns on foreign direct investment, which derives in part from one-off effects from assets held by holding companies established on the foundations of the failed banks' estates.

Indicators of developments in private consumption at the beginning of the year suggests that household demand is still growing rapidly, although it could ease from the level seen in Q4/2016. In February, the Gallup Consumer Confidence Index measured 125.8 points, an increase of a full 4 points from January and 7.3 points from February 2016.

According to the results of Gallup's spring survey, carried out in February among Iceland's 400 largest firms, respondents were somewhat more positive about the current economic situation and the six-month outlook than they had been in the winter survey, taken in November. They were considerably more pessimistic than in the autumn survey, however. About 79% of respondents considered the current situation good, and about 18% considered it neither poor

nor good. Just under 24% of executives were of the view that economic conditions would improve in the next six months, and 63% expected conditions to remain unchanged (i.e., good). Executives in retail and wholesale trade were more upbeat than other executives about the situation six months ahead, while optimism among financial and construction companies had diminished since the winter survey. Optimism was least pronounced among fishing companies. Executives in all sectors were generally more pessimistic than they were a year ago. About 13% of executives were of the opinion that conditions would deteriorate over the next six months.

According to the survey, there was an increase in the number of firms expecting their ratio of profit to turnover to decline year-on-year. The profit index declined by 16 points, to 99, after having remained relatively stable since September 2015. Expectations concerning EBITDA in the next six months had deteriorated also. The investment index had declined from the previous measurement, with the most pronounced change among construction companies.

According to the survey, firms interested in recruiting staff in the next six months outnumbered those planning redundancies by just under one-fourth, adjusted for seasonality. This is a slight decline from the winter survey. The change is due both to a decline in the number interested in adding on staff and an increase in the number of firms considering redundancies. Optimism was greatest among executives in construction and utility companies, where those planning to recruit outnumbered those planning redundancies by some 64 percentage points. Fishing company executives were relatively pessimistic, however, with those planning redundancies outnumbering those planning to recruit by about 16 percentage points. In other sectors, the share of companies planning to recruit was larger than the share planning to lay off staff by 18-37 percentage points.

Adjusted for seasonality, about 40% of respondents considered themselves short-staffed, about the same as during the past year. An all-time high of 93% of construction companies considered themselves understaffed. In other sectors, the share of firms considering themselves short-staffed lay in the 24-59% range.

According to preliminary figures from Statistics Iceland, the wage share (wages and related expenses relative to gross factor income) was 62.4% in 2016, just over a percentage point above the twenty-year average. It rose by 2 percentage points between years, in line with the forecast in the February *Monetary Bulletin*.

Seasonally adjusted unemployment rose by approximately $\frac{1}{2}$ a percentage point month-on-month in January, in terms of both the Statistics Iceland labour force survey and the Directorate of Labour's unemployment register. The increase in registered unemployment was attributable for the most part to the fishermen's strike, as seasonally adjusted unemployment excluding those on strike continued to fall in January.

The wage index rose by 0.1% month-on-month in January and by 8.7% year-on-year. Real wages in terms of the index had risen by 6.7% year-on-year in January.

Statistics Iceland's nationwide house price index, published at the end of February, rose by 1.5% month-on-month, after adjusting for seasonality, and by 16% year-on-year. The capital area house price index, calculated by Registers Iceland, rose by 1.7% month-on-month in January when adjusted for seasonality, and by 16.3% year-on-year. The number of registered purchase agreements nationwide rose 11.5% between years in January. The average time-to-sale for flats

in the greater Reykjavík area was about 1.2 months in January, down from 2.2 months in January 2016.

The CPI rose by 0.7% month-on-month in February. Twelve-month inflation measured 1.9% in February and had been unchanged for three months in a row. The CPI excluding the housing component had declined by 1% year-on-year, however. Most statistical measures of underlying inflation suggested that it had declined in February and lay in the 1.5-2.2% range.

The main drivers of the CPI increase in February were end-of-sale effects and rising house prices. Private services prices had risen by 0.1% between years, and the small increase is largely explained by a decline in telephone services prices and international airfares.

Household inflation expectations were unchanged between surveys, according to Gallup's spring survey, carried out in February. Households' one-year expectations measured 3%, and two-year expectations measured 3.5%. According to Gallup's spring survey among executives, one-year inflation expectations were up by ½ a percentage point from the previous survey, to 2.5%. On the other hand, two-year inflation expectations were unchanged at 3%. Indications of a decline in long-term inflation expectations could be seen in the breakeven inflation rate in the bond market. Since the MPC's last meeting, the ten-year breakeven rate had declined by 0.2 percentage points, to an average of 2.3%.

II The interest rate decision

The Governor updated the Committee on developments in connection with capital account liberalisation and on work in connection with the review of the monetary policy framework. In this context, a presentation was given on the work currently underway with respect to the review of the success of monetary policy in recent years, and a report was given to the Committee on the results of an assessment of developments in the Central Bank's earnings and equity under various scenarios.

The Committee discussed the monetary stance in view of the most recent information on developments in the economy and the fact that the monetary stance had remained broadly unchanged since the MPC's February meeting. Members discussed whether developments since the last meeting had changed their assessment of whether the monetary stance was appropriate in view of the inflation outlook. The Committee had been unanimous in February about its decision to keep the Bank's interest rates unchanged because rapid GDP growth and clear signs of growing demand pressures in the general economy and the labour market had called for a continued tight monetary stance. In particular, consideration had been given to the uncertainty then prevailing in connection with the wage settlement review in the labour market, which, in the Committee's view, also called for caution in interest rate setting.

The MPC discussed the recently published national accounts data, which showed that year-2016 GDP growth had been much stronger than had been projected in the Central Bank's February forecast, and which the Committee had taken into account at the February meeting. Members agreed that, although GDP growth had been export-driven to a considerable degree, it had been well in excess of long-term potential and had begun to strain domestic resources. Indicators also implied continued strong growth thus far in 2017. Job creation had been strong and unemployment low, and the labour participation rate had risen above the pre-crisis peak. Committee members considered it likely that the output gap had widened further than had

been forecast in February and would continue to grow in spite of countervailing effects from labour importation.

Members discussed developments in inflation, which measured 1.9% in February, broadly similar to the level in the past six months. In the Committee's opinion, the appreciation of the króna and low global inflation continued to offset domestic inflationary pressures. Members noted that the gap between domestic price developments – housing costs in particular – and external factors had widened. In addition, a tight monetary stance had anchored inflation expectations and contained both credit growth and demand growth. They also noted that inflation expectations appeared to have withstood significant exchange rate volatility in recent days, as the breakeven inflation rate in the bond market was largely unchanged.

All members considered it appropriate to keep the Bank's interest rates unchanged. They agreed that rapid growth in economic activity and clear signs of demand pressures in the economy called for a tight monetary stance so as to ensure medium-term price stability. In the Committee's opinion, the new national accounts suggested that demand pressures in the economy were stronger than had been assumed in February. On the other hand, the exchange rate of the króna had continued to rise, thereby containing inflation, both by lowering imported inflation and by facilitating labour importation, which eased the tension in the labour market and held back wage drift. Members also noted that strong productivity growth in 2016 had eased domestic inflationary pressures. Doubts were expressed about whether this productivity growth had been as strong as was indicated in Statistics Iceland's preliminary figures, and some members thought it likely that the numbers indicated an underestimation of labour importation.

Members agreed that the virtually complete liberalisation of capital controls had somewhat exacerbated uncertainty about developments in the exchange rate and the general economy in the near term. They considered it too early to predict the economic impact of the liberalisation measures, as the market was still seeking a balance in the wake of the changes. Members considered it possible that a better balance would develop between foreign exchange market in- and outflows, but that short-term volatility could increase while the market was adjusting to the change, as could be seen on the days during which the meeting was held. Committee members agreed that the Central Bank's intervention in the foreign exchange market should continue to focus on mitigating short-term volatility when conditions warranted it. In this context, they considered it appropriate to emphasise that the Bank would not only purchase foreign currency, as had been customary since November 2014, but would also sell currency when conditions called for it, as the Bank had recently demonstrated.

There was some discussion of the appreciation of the króna in recent quarters. MPC members agreed that the appreciation was largely a reflection of economic fundamentals, which could be attributed to improved terms of trade and strong exports – tourism in particular – which delivered a sizeable trade surplus. They agreed that monetary policy neither could nor should try to halt the inevitable adjustment stemming from structural changes in export production and the rise in the equilibrium real exchange rate. On the other hand, there was considerable uncertainty about the equilibrium real exchange rate over the medium term. It was pointed out that the appreciation of the króna was an important factor in the success in keeping inflation at target and that, in view of the strong growth of the tourism industry, appreciation was an unavoidable part of easing the pace of growth in the sector and creating increased scope for it. On the other hand, it could tend to crowd out other export activities to some extent.

During the discussion, it also emerged that Committee members considered it desirable that other economic policy and monetary policy pull in the same direction, particularly if it were

considered beneficial to counteract the rise in the exchange rate. The view was also expressed that it would be possible at the next MPC meeting to make a better assessment of the impact of capital account liberalisation on the exchange rate. A new macroeconomic forecast would also be ready by that time, including a better assessment of the degree to which strong GDP growth in the recent term had led to rising tension in the economy.

In view of the discussion, the Governor proposed that the Bank's interest rates be held unchanged. The Bank's key rate (the seven-day term deposit rate) would remain 5%, the current account rate 4.75%, the seven-day collateralised lending rate 5.75%, and the overnight lending rate 6.75%. All Committee members voted in favour of the proposal.

Members agreed that a stronger anchor for inflation expectations at target and the appreciation of the króna had enabled the MPC to achieve its legally mandated price stability objective at a lower interest rate than would otherwise have been possible. Members agreed that in the coming term, the monetary stance would be determined by economic developments and actions taken in other policy spheres.

The following Committee members were in attendance:

Már Gudmundsson, Governor and Chairman of the Monetary Policy Committee

Arnór Sighvatsson, Deputy Governor

Thórarinn G. Pétursson, Chief Economist

Gylfi Zoëga, Professor, external member

Katrín Ólafsdóttir, Assistant Professor, external member

In addition, a number of Bank staff members attended part of the meeting.

Rannveig Sigurdardóttir wrote the minutes.

The next Statement of the Monetary Policy Committee will be published on Wednesday 17 May 2017.



The Monetary Policy Committee of the Central Bank of Iceland

Minutes of the Monetary Policy Committee meeting, May 2017

Published 31 May 2017

The Act on the Central Bank of Iceland stipulates that it is the role of the Monetary Policy Committee (MPC) to set Central Bank interest rates and apply other monetary policy instruments. Furthermore, the Act states that “[m]inutes of meetings of the Monetary Policy Committee shall be made public, and an account given of the Committee’s decisions and the premises upon which they are based.” In accordance with the Act, the MPC has decided to publish the minutes of its meetings two weeks after each interest rate decision. The votes of individual Committee members will be made public in the Bank’s *Annual Report*.

The following are the minutes of the MPC meeting held on 15 and 16 May 2017, during which the Committee discussed economic and financial market developments, the interest rate decision of 17 May, and the communication of that decision.

I Economic and monetary developments

Before turning to the interest rate decision, members discussed the domestic financial markets, financial stability, the outlook for the global economy and Iceland’s international trade, the domestic economy, and inflation, with emphasis on information that has emerged since the 15 March 2017 interest rate decision, as published in the new forecast and analysis of uncertainties in *Monetary Bulletin 2017/2* on 17 May.

Financial markets

Exchange rate volatility has subsided after a temporary spike after the capital controls were lifted in mid-March. Between meetings, the króna appreciated by 6.2% in trade-weighted terms. Over this period it appreciated by 9.2% against the US dollar, 5.1% against the euro, and 2.7% against the pound sterling. The Central Bank’s net foreign currency purchases in the domestic foreign exchange market totalled approximately 174 million euros (roughly 20.4 b.kr.) between meetings, or 27.4% of total market turnover.

In terms of the Central Bank’s real rate, the monetary stance tightened slightly between meetings, and the Bank’s real rate in terms of the average of various measures of inflation and inflation expectations had risen by 0.2 percentage points, to 2.7%.

Interest rates in the interbank market for krónur were virtually unchanged between meetings. Turnover in the market had been considerably greater year-to-date than over the same period in 2016, totalling almost 101.6 b.kr. Yields on nominal Treasury bonds were broadly

unchanged since the March meeting, and yields on indexed Treasury and Housing Financing Fund (HFF) bonds had fallen by as much as 0.2 percentage points. Furthermore, financial institutions' deposit and lending rates were virtually unchanged since the March meeting.

Risk premia on Treasury foreign obligations had declined by as much as 0.3 percentage points between meetings, after Standard & Poor's upgraded Iceland's sovereign ratings from A- to A. The CDS spread on the Treasury's five-year US dollar obligations measured 0.8% just before the May meeting, and the spread vis-à-vis comparable bonds issued by Germany was 0.8 percentage points.

Financial institutions' analysts expected either no change or a 0.25 percentage point interest rate reduction in May, but they considered the decision uncertain. As grounds for a rate cut, they cited improvements in the short-term inflation outlook and the continued appreciation of the króna despite the removal of most of the capital controls. The main grounds cited for unchanged interest rates pertained to the growing output gap and the situation in the housing and labour markets.

According to the Central Bank's survey of market agents' expectations, carried out in May, respondents expected the Bank's key rate to be lowered by 0.25 percentage points in Q2/2017 to 4.75%, followed by a further reduction in Q4. They expected the key rate to be raised back to 4.75% in Q2/2018, however. In the survey, participants were also asked about near-term developments in house prices. About 60% of respondents expected the year-on-year rise in house prices to be slower in the next six months than it had been in April, when it measured 20%, and 95% of respondents expected the pace to ease in the next twelve months.

M3 grew by about 6% year-on-year in Q1/2017, after adjusting for deposits held by the failed financial institutions. The growth rate is similar to that in the previous quarter but still below nominal GDP growth. As was the case last year, growth in money holdings is due largely to increased household deposits, although corporate deposits also grew between years.

After adjusting for the Government's debt relief measures, the total stock of credit system loans to resident borrowers grew by 3½% year-on-year in Q1, and by just over 4½% after adjusting for the effects of exchange rate movements on the foreign-denominated credit stock. Growth is attributable to an increase in lending to households and businesses. Annual growth in credit system lending to households measured 3.7% in Q1, after adjusting for the Government's debt relief measures.

The Nasdaq OMXI8 index had risen by 9.5% between meetings and by 10.1% since the beginning of the year. Turnover in the Nasdaq Iceland main market totalled 246 b.kr. in the first four months of the year, about 27% more than over the same period in 2016.

Global economy and external trade

According to the forecast published by the International Monetary Fund (IMF) in April, the global GDP growth outlook has improved from the Fund's January forecast, particularly for advanced economies. According to the forecast, global GDP growth will measure 3.5% this year. The Fund's output growth forecast for Iceland's main trading partners is 0.1 percentage points higher this year, or 1.9%. The Fund also expects inflation in advanced and emerging market economies to be higher over the forecast horizon than it projected in January. Among Iceland's main trading partners, inflation is expected to measure 1.9% this year, which is 0.3 percentage points above the IMF's October forecast.

Iceland's external goods trade generated a deficit of 48.3 b.kr. for the first four months of the year, as opposed to a deficit of 28.4 b.kr. over the same period in 2016. Export values contracted by 0.5% year-on-year at constant exchange rates, while import values rose 10.7%. The export value of marine products declined by 16% year-on-year and the export value of industrial products rose by nearly 13%. Import growth is attributable mainly to a 24% increase in imports of commodities and operational inputs, whereas the import value of petrol rose by 29%. In spite of strong growth in passenger car imports, there was a contraction of nearly 13% in the import value of transport equipment, as imports of aircraft were much less this year than over the same period in 2016.

The listed global market price of aluminium was unchanged between MPC meetings, and the average price in April was up by just over a fifth year-on-year. Foreign currency prices of marine products rose by about 1.5% between months in March and by about 5.7% year-on-year.

In terms of relative consumer prices, the real exchange rate measured 99.7 points in April, a decline of 0.9% month-on-month but an increase of 17.6% year-on-year. The rise is due primarily to a 17.5% nominal appreciation of the króna, but in addition, inflation in Iceland was about 0.1 percentage point above the trading partner average.

The domestic real economy and inflation

According to parliamentary resolutions on the five-year fiscal strategy and fiscal plan presented before Parliament in January and at the end of March, the fiscal stance for the period will ease more this year than was assumed in the Bank's February forecast. It is assumed that, after adjusting for one-off items, the Treasury primary surplus will contract from last year's 3.3% of GDP to 2.5% this year. Adjusting for business cycle effects, the primary balance is expected to deteriorate year-on-year by 1.4% of GDP in 2017. It is estimated that the proposed increase in value-added tax (VAT) on tourism will result in consolidation of about 0.7% of GDP in 2018, followed by easing in the amount of 0.2% of GDP in 2019, when the planned reduction of the general VAT rate takes effect.

According to the Statistics Iceland labour force survey (LFS), total hours worked increased by 3.5% in Q1, slightly more than had been assumed in the Bank's February forecast. The increase was due to a 3.9% rise in the number of employed persons, as the average work week continued to grow shorter. In Q1/2017, as in the previous quarter, the seasonally adjusted labour participation rate was 83.8%, which is equal to the pre-crisis peak, although the employment rate is still $\frac{1}{2}$ a percentage point below the previous peak, at 81.6%.

Seasonally adjusted unemployment measured 2.7% in Q1, having declined by 0.4 percentage points between years. This was the lowest unemployment rate since H1/2008.

The wage index rose by 0.8% between quarters in Q1, and by 6.4% year-on-year, and real wages in terms of the index were 4.5% higher in Q1/2017 than in Q1/2016.

Key indicators of developments in private consumption suggest that growth remained strong at the beginning of the year. Payment card turnover was up by nearly 12% year-on-year in the first four months of 2017, and new motor vehicle registrations were up by over a fifth.

The Gallup Consumer Confidence Index measured 126.6 points in April, a full four points less than in April 2016 and 2.6 points less than in March 2017. It is high in historical context, however, indicating significant optimism among households.

Statistics Iceland's nationwide house price index, published at the end of April, rose by 2% month-on-month after adjusting for seasonality, and by 20.4% year-on-year. The capital area real estate price index, calculated by Registers Iceland, rose by 2.4% month-on-month in March when adjusted for seasonality, and by 20.9% year-on-year. The number of registered purchase agreements nationwide rose 12.3% between years in March. The average time-to-sale for residential property in the greater Reykjavík area was about 1.2 months in March, down from 2 months in March 2016.

The CPI rose by 0.5% month-on-month in April, after rising by 0.1% in March. Twelve-month inflation measured 1.9% in April and was unchanged since the Committee's March meeting. The CPI excluding the housing component had declined by 1.8% year-on-year, however. Most measures of underlying inflation suggested that it had declined in April and lay in the 1-2% range.

The main driver of the CPI increase in April was the rise in house prices. International airfares also rose but were offset by the drop in food prices. Private services prices had risen by 0.3% year-on-year. The small increase is explained largely by a decline in two service-related subcomponents of the CPI: telephone services and international airfares.

According to the Central Bank's survey of market agents' inflation expectations, conducted at the beginning of May, participants expect inflation to measure 2.2% in one year. This is 0.3 percentage points less than in the previous survey, taken in February 2017. Survey participants' inflation expectations two years ahead had also declined, from 2.8% in the last survey to 2.6%. Furthermore, market agents expect inflation to average 2.6% over the next ten years, or 0.1 percentage points less than in the February survey. The ten-year breakeven inflation rate in the bond market had measured in the 2.2-2.4% range during the quarter to date, as opposed to 3.1% in Q2/2016.

According to the baseline forecast published in *Monetary Bulletin* on 17 May, inflation will be around 2% well into 2018 and then rise to approximately 3% in mid-2019 before subsiding towards the target. Because of Statistics Iceland's error in measuring the CPI in 2016, inflation was underestimated during the first three quarters of the year. At the turn of the year, excise taxes rose on a number of products, including petrol, alcoholic beverages, and tobacco. The impact of this on the CPI is roughly equal to the aforementioned measurement error. Furthermore, the authorities are planning changes to indirect taxes in the coming term. Once adjustments are made for these factors, the inflation outlook for 2017 is broadly unchanged, whereas the outlook for 2018 is slightly improved. The situation will change at the beginning of 2019, however, when inflation is projected to be $\frac{1}{2}$ a percentage point more than was forecast in February, owing to the prospect of a wider output gap than was assumed then.

According to the baseline forecast, the króna will continue to appreciate until end-2018. If the forecast materialises, the exchange rate will be a full 14½% higher, on average, in 2017 than in 2016 and will rise by an additional 6% in the coming two years. By 2019, the króna would be 3½% stronger than was assumed in February, although these forecasts are highly uncertain. Therefore, according to the forecast, the real exchange rate will rise more than previously anticipated. If this is borne out, the real exchange rate in terms of relative consumer prices will be 11% higher by the end of the forecast horizon than in Q1/2017. In terms of relative unit labour costs, the increase is somewhat larger.

In Q4/2016, global output growth exceeded the forecast in the February *Monetary Bulletin*, and the outlook for this year has improved. GDP growth among Iceland's main trading partners looks set to rise to 1.9% this year, from last year's 1.6%. As in February, trading

partners' GDP growth is assumed to measure about 1.9% per year throughout the forecast horizon.

The ratio of Iceland's export prices to those of trading partner countries rose more at the end of 2016 than had been projected in the last *Monetary Bulletin*. The outlook for developments in marine and aluminium product prices has also improved this year, with relative export prices expected to rise by 4½%, nearly 2 percentage points more than was forecast in February. Nevertheless, a more rapid rise in import prices will cut into this improvement in terms of trade, which is now projected at 1% instead of the 1.9% provided for in the February forecast. The outlook for the next two years is broadly unchanged, however, and no major changes in terms of trade are expected.

It is mainly because of strong growth in services exports that total exports are forecast to grow by 10½% this year, considerably more than was projected in February. The difference is due mainly to the prospect of an even larger increase in tourist arrivals than was previously assumed. Even though marine product exports contracted in Q1/2017 because of the fishermen's strike, they are expected to increase somewhat more this year than was forecast in February, owing to a much stronger capelin fishery than previously anticipated. Aluminium exports are also expected to be stronger this year. As in the Bank's previous forecasts, export growth is expected to ease in the next two years, in line with a rising real exchange rate and relatively weak global export growth.

According to preliminary figures from Statistics Iceland, GDP growth picked up strongly as 2016 progressed, measuring 10.4% in H2 and 7.2% for the year as a whole. This is just over 1 percentage point more than had been assumed in the Bank's February forecast. There are signs that GDP growth eased somewhat in Q1/2017. Clearly, the fishermen's strike early in the year caused a steep drop in marine product exports, causing fisheries to export inventories. Because the impact of the strike was temporary, GDP growth is expected to rally in Q2 and measure 6.3% for 2017 as a whole, 1 percentage point above the February forecast. The changed outlook is due mainly to the prospect of stronger-than-expected export growth, and the greater-than-expected fiscal easing provided for in the new National Budget is a factor as well. Robust export growth also affects the outlook for 2018 GDP growth, which is now projected at 3.5% instead of the 3.1% in the February forecast. As in the February forecast, GDP growth is projected to keep subsiding as the forecast horizon progresses, easing to 2.5% by 2019, close to estimated long-term potential output.

Total hours worked increased by 3% in 2016 and 3.5% in Q1/2017, slightly outpacing the February forecast. Total hours are expected to keep rising through this year, to about 4.1% more than in 2016. The working-age population grew by about 2% year-on-year, owing in part to significant importation of foreign labour. The labour participation rate is also on the rise and will be some ¾ of a percentage point higher this year than in 2016.

Unemployment continued to decline as well, to a seasonally adjusted rate of 2.7% in Q1. It is expected to measure 2.6% for the year as a whole, as was forecast in February. As in previous forecasts, it is projected to rise gradually to the level deemed consistent with low and stable inflation. It is forecast to average 3% in 2018 and 3½% in 2019.

Wages have risen steeply in the recent term, offsetting imported deflation and the appreciation of the króna. This year's pay rises will be large as well, nearly 7%, but the pace will then ease in 2018 and 2019. Offsetting these hefty pay increases is last year's unusually strong productivity growth and the prospect of the same this year. It is possible, however, that productivity growth has been overestimated – for instance, because of an underestimation of the increase in foreign labour. In 2017-2019, unit labour costs are forecast to rise by about the

same as in 2016, or an average of nearly 5% per year. If the forecast materialises, there will be significant inflationary pressures from the labour market during the forecast horizon.

Strong demand growth and job creation have caused a persistent shortage of workers in spite of increased labour importation, and representatives of a steadily growing number of firms indicate that they are operating at or above capacity. As a result, the output gap appears to be growing. It is estimated to measure $3\frac{1}{3}\%$ of potential output at the end of this year. It will therefore grow more rapidly than was assumed in February and will be nearly 1 percentage point more during the forecast horizon, at just under 1% of potential output by mid-2020, the end of the forecast horizon.

The baseline forecast reflects the assessment of the most likely economic developments during the forecast horizon. It is based on forecasts and assumptions concerning developments in the external environment of the Icelandic economy, as well as assessments of the effectiveness of specific markets and on the transmission of monetary policy to the real economy. All of these factors are subject to uncertainty. Changes in key assumptions could lead to developments different from those provided for in the baseline forecast.

The inflation outlook could turn out poorer than in the forecast if domestic demand is underestimated or the flexibility of the supply side of the economy is overestimated. Furthermore, a number of wage agreements are up for negotiation soon, and the resulting pay rises could prove larger than is assumed in the baseline forecast. The tension in the labour market could also generate more wage drift than the forecast provides for. Furthermore, the scope for domestic companies to absorb further cost increases could be exhausted – particularly in the tradable sector, where firms' competitive position has been eroded significantly by the rising real exchange rate. The imbalances in the housing market could also be underestimated, which could kindle even more demand pressures and exacerbate the risk of a hard landing later on. Moreover, if the fiscal stance eases more than is currently expected, demand pressures could be underestimated. All of this could test the newly established anchor for inflation expectations.

The inflation outlook presented in the baseline forecast could be overly pessimistic, however. The outlook is for sustained large current account surpluses and a continued improvement in Iceland's external position. The equilibrium exchange rate of the króna could therefore rise more than is assumed in the forecast, pulling the nominal exchange rate upwards even further than is currently projected. Weaker GDP growth among Iceland's main trading partners and a more sluggish recovery of global oil and commodity prices could also cut into domestic economic activity and prolong the impact of imported deflation, which has helped keep inflation low in Iceland. The effects of increased global competition on domestic retailers' pricing decisions could also be underestimated. And finally, the cyclical expansion of potential output could still be underestimated.

II The interest rate decision

The Governor reported to the MPC on the Icelandic mission's meetings with representatives of the International Monetary Fund (IMF) and its meetings with other central bankers, rating agencies, and financial institutions at the IMF's spring meetings in Washington, DC. In this context, he also reported on discussions of the capital flow management measure.

Committee members discussed the Bank's most recent *Financial Stability* report; they also discussed financial institutions' position and risks to the financial system.

The MPC discussed the monetary stance in view of the most recent information on the economy and the slight rise in the Bank's real rate between meetings. Members discussed whether this had changed their assessment of whether the monetary stance was appropriate in view of the inflation outlook, as the Committee had been unanimous in March about its decision to keep the Bank's interest rates unchanged, owing to rapid growth in economic activity and clear signs of growing demand pressures in the economy, which, in MPC members' view, called for a tight monetary stance. The Committee had also considered, at its March meeting, that the virtually complete liberalisation of capital controls had somewhat exacerbated uncertainty about developments in the exchange rate and the general economy.

In this context, members took account of the Central Bank's new forecast, published in *Monetary Bulletin* on 17 May, which indicated that GDP growth would be strong in 2017, as it had been in 2016, and that growth would exceed the February forecast in both years. Members noted that the deviation from the February forecast stems mainly from stronger-than-expected growth in tourism, although the outlook was also for more fiscal easing in 2017 than was previously projected. In particular, the MPC noted that demand pressures in the labour market and the general economy had grown despite increased importation of labour and strong productivity growth. The appreciation of the króna offset the increased tension, and members agreed that it had played a key role in the economy's adjustment to the positive shocks attributable to improved terms of trade and growth in the tourism sector.

The Committee discussed developments in inflation since the last meeting; inflation had measured 1.9% in April, broadly similar to the level in the previous six months. As at previous meetings, members agreed that the currency appreciation and low global inflation offset domestic inflationary pressures.

In particular, they discussed different measures of inflation, as the gap between domestic price developments – housing costs in particular – and external factors had widened even further since the last MPC meeting. Members noted that underlying inflation appeared to have tapered off in recent months. They also observed that underlying the recent developments in inflation were wide fluctuations in relative prices, with the housing component one of the main drivers of inflation. It was not appropriate to ignore the housing component, however, because house prices were an indicator of future inflation just as they had been during the pre-crisis period, when different measures of inflation also diverged. It was also mentioned that the small rise in domestic prices excluding housing was due primarily to a decline in two items falling under private services. Other labour-intensive items had risen as could have been expected given the rise in wage costs.

Members also took account of the inflation forecast published in *Monetary Bulletin*, which shows that the inflation outlook for 2017 and 2018 has improved since the February forecast, while the outlook further out the forecast horizon has deteriorated. Committee members agreed that two opposing forces were at work and were affecting the outlook. One was the demand pressures in the economy, which had proven stronger than had been projected in

February, and the other, offsetting domestic inflationary pressures, was the impact of a higher exchange rate.

The Committee discussed recent exchange rate developments, as the króna had appreciated somewhat since the March meeting. The MPC considered it positive that short-term exchange rate volatility had receded since the beginning of April. As before, members agreed that the appreciation of the króna was largely a reflection of economic fundamentals, which could be attributed to improved terms of trade and strong exports – tourism in particular – which delivered a sizeable trade surplus. They were of the view that monetary policy neither could nor should try to halt the resulting adjustment of the real exchange rate, which was inevitable. It was pointed out that the alternative scenario published in *Monetary Bulletin* illustrated clearly the impact of the exchange rate on the adjustment of the economy to positive shocks. Nevertheless, Committee members agreed that the Bank should continue to intervene in the foreign exchange market in order to mitigate volatility when it considered such intervention warranted.

In the Committee's opinion, there were grounds for keeping interest rates unchanged and for lowering them by 0.25 percentage points. All members agreed that the main rationale for keeping interest rates unchanged was the rapid growth in economic activity and the clear signs of demand pressures in the economy, which called for a tight monetary stance in order to ensure medium-term price stability. It was therefore difficult to see how the current situation and near-term outlook called for monetary easing. By the same token, it was necessary to take into account that the fiscal stance provided for considerable easing; therefore, it was difficult to see where a tight stance should come from if not from monetary policy.

The main argument in favour of a rate reduction that was expressed at the meeting was that the Bank's real rate had risen since the Committee's last meeting. At the same time, the appreciation of the króna had also contained demand and economic activity. These two factors created the scope for a rate reduction. There was some discussion of how much tightening the higher exchange rate entailed, with some members considering it to be significant. It was mentioned that the rise in the exchange rate and the proposed increase in VAT on tourism had already begun to affect tourism companies' investment plans. Committee members agreed that the exchange rate uncertainty associated with capital account liberalisation, which they had taken into account at the last meeting, was no longer a factor. Some members emphasised that inflation was due entirely to increased housing costs. They considered it likely that the rise in house prices in excess of the general price level and wages would reverse within a few years or at least halt earlier than currently expected, once housing supply had caught up with demand, as property prices were close to a historical high. If this should occur without a reversal of the recent appreciation of the króna, the combined developments in house prices and the exchange rate could lead to rapid disinflation. These members were of the view that such a scenario was no less probable than a scenario involving a less favourable interaction between exchange rate and house prices. It was therefore appropriate to continue lowering interest rates cautiously, provided that credit growth did not accelerate.

It was also mentioned that the supply side of the economy was more flexible than before. More importation of labour, together with growth in investment and productivity, had increased potential output well in excess of the long-term trend growth rate. As a result, it could grow more rapidly without significant wage drift or excessive demand pressures. Furthermore, it was pointed out that the near-term inflation outlook was better than had been anticipated at the previous meeting. Consequently, some members were of the view that a

small interest rate reduction would not pose a risk as regarded future inflation, and one member thought it possible that the scope for a rate cut was underestimated. It was pointed out that a tight monetary stance had anchored inflation expectations more firmly at target and that it was therefore safe to lower the Bank's key rate despite the strength of the economy, as such a move would not bring the Bank's real rate below the level just before the March meeting.

In view of the discussion, the Governor proposed that the Bank's interest rates be lowered by 0.25 percentage points, which would lower the key rate (the seven-day term deposit rate) to 4.75%, deposit rates (current account rates) to 4.5%, the seven-day collateralised lending rate to 5.5%, and the overnight rate to 6.5%. All Committee members voted in favour of the proposal.

Members agreed that a stronger anchor for inflation expectations at target and the appreciation of the króna had enabled the MPC to achieve its legally mandated price stability objective with a lower interest rate than would otherwise have been possible. Members agreed that in the coming term, the monetary stance would be determined by economic developments and actions taken in other policy spheres.

The following Committee members were in attendance:

Már Gudmundsson, Governor and Chairman of the Monetary Policy Committee

Arnór Sighvatsson, Deputy Governor

Thórarinn G. Pétursson, Chief Economist

Gylfi Zoëga, Professor, external member

Katrín Ólafsdóttir, Assistant Professor, external member

In addition, a number of Bank staff members attended part of the meeting.

Rannveig Sigurdardóttir wrote the minutes.

The next Statement of the Monetary Policy Committee will be published on Wednesday 14 June 2017.



The Monetary Policy Committee of the Central Bank of Iceland

Minutes of the Monetary Policy Committee meeting, June 2017

Published 28 June 2017

The Act on the Central Bank of Iceland stipulates that it is the role of the Monetary Policy Committee (MPC) to set Central Bank interest rates and apply other monetary policy instruments. Furthermore, the Act states that “[m]inutes of meetings of the Monetary Policy Committee shall be made public, and an account given of the Committee’s decisions and the premises upon which they are based.” In accordance with the Act, the MPC has decided to publish the minutes of its meetings two weeks after each interest rate decision. The votes of individual Committee members will be made public in the Bank’s *Annual Report*.

The following are the minutes of the MPC meeting held on 12 and 13 June 2017, during which the Committee discussed economic and financial market developments, the interest rate decision of 14 June, and the communication of that decision.

I Economic and monetary developments

Before turning to the interest rate decision, members discussed the domestic financial markets, financial stability, the outlook for the global economy and Iceland’s international trade, the domestic economy, and inflation, with emphasis on information that has emerged since the 17 May 2017 interest rate decision.

Financial markets

Between meetings, the króna appreciated by 1.1% in trade-weighted terms. Over this period it appreciated by 1.8% against the US dollar, 0.4% against the euro, and 3.1% against the pound sterling. The Central Bank’s net foreign currency purchases in the domestic foreign exchange market totalled approximately 54 million euros (roughly 6.03 b.kr.) between meetings, or 22% of total market turnover.

In terms of the Central Bank’s real rate, the monetary stance tightened slightly between meetings. The Bank’s real rate in terms of the average of various measures of inflation and inflation expectations had risen by 0.3 percentage points since just after the Bank’s rate reduction in May, to 2.7%.

Interest rates in the interbank market for krónur had developed in line with the Bank’s key rate between meetings. Turnover in the market had been considerably greater year-to-date than over the same period in 2016, totalling 111.6 b.kr.

Yields on nominal Treasury bonds had fallen by up to 0.4 percentage points following the reduction in the Bank's key rate and the publication of the minutes of the last MPC meeting.

Yields on indexed Treasury and Housing Financing Fund (HFF) bonds declined by up to 0.2 percentage points between meetings.

The commercial banks' nominal deposit and lending rates fell by 0.1-0.3 percentage points, in line with the Bank's rate cut in May, whereas the pension funds' nominal lending rates remained unchanged between meetings. The pension funds' indexed lending rates declined marginally between meetings, in line with yields on indexed Treasury and HFF bonds, but the commercial banks' indexed lending rates were unchanged.

Risk premia on Treasury foreign obligations were broadly unchanged between meetings. The CDS spread on the Treasury's five-year US dollar obligations was unchanged since the May meeting, at 0.8%, while the spread between the Treasury's eurobonds and comparable bonds issued by Germany rose slightly, to 1 percentage point.

Financial institutions' analysts expected either no change or a rate reduction of 0.25 or 0.5 percentage points in June. As grounds for a rate cut, they cited improvement in the inflation outlook because of the appreciation of the króna and signs of a slower rise in house prices in the near future, as well as the rise in the real rate between MPC meetings. The main grounds cited in favour of an unchanged key rate were the tight labour market, the strength of the economy, and the accommodative fiscal stance.

Growth in money holdings has picked up in the past two months. Annual growth in M3 was almost 9% in March and 7½% in April, after adjusting for deposits held by the failed financial institutions. As in 2016, annual growth is due primarily to an increase in household deposits. The quicker pace of growth in money holdings in the past two months is also due to a larger year-on-year increase in corporate and financial sector deposits than in previous months.

After adjusting for the Government's debt relief measures, the total stock of credit system loans to resident borrowers grew by nearly 3½% year-on-year in April, and by just under 4½% after adjusting for the effects of exchange rate movements on the foreign-denominated credit stock. Growth is attributable to an increase in lending to households and businesses. Annual growth in credit system lending to households measured nearly 4% in April after adjusting for the Government's debt relief measures.

The Nasdaq OMXI8 index had fallen by 2.7% between meetings but had risen by 7.2% since the beginning of the year. Turnover in the Nasdaq Iceland main market totalled almost 318 b.kr. in the first five months of the year, about 26% more than over the same period in 2016.

Global economy and external trade

According to the Organisation for Economic Co-operation and Development's (OECD) June forecast, GDP growth will be somewhat stronger in 2016 and 2017 than in the OECD's November forecast. Global GDP growth is expected to increase from last year's rate of 3% to 3.5%, some 0.2 percentage points more than was forecast in November. Global GDP growth is forecast at 3.6% in 2018. The outlook for world trade in 2017-2018 has also improved. The OECD forecast for 2017 GDP growth among Iceland's main trading partners is about 0.2 percentage points higher than was expected in November, or 2%. Trading partner inflation is projected at 1.9% this year, or 0.3 percentage points higher than was assumed in the November forecast, owing to the recent rise in commodity prices.

Iceland's external goods trade generated a deficit of 61 b.kr. for the first five months of the year, as opposed to a deficit of 41 b.kr. over the same period in 2016. Export values rose by 7% year-on-year at constant exchange rates, while import values rose 15%. The export value of industrial goods rose by 18% year-on-year, while the export value of marine products contracted nearly 6%. Import growth is attributable in particular to a rise of roughly one-fourth in the value of imported commodities and operational inputs and a 40% rise in the value of imported fuels and lubricants.

The listed global market price of aluminium was unchanged between MPC meetings, and in the first week of June the average price was up by nearly one-fifth year-on-year. Foreign currency prices of marine products rose by about 2.5% between months in April and had by 7.9% year-on-year.

In terms of relative consumer prices, the real exchange rate had risen 5.6% month-on-month in May, to 105.2 points. In the first five months of 2017, it was up 18.8% year-on-year, owing to a corresponding rise in the nominal exchange rate, as inflation was the same as the trading partner average.

The domestic real economy and inflation

According to preliminary figures published by Statistics Iceland in June, annual GDP growth measured 5% in Q1/2017, somewhat below the H2/2016 growth rate. This was due mainly to the effects of the fishermen's strike in Q1, which showed in a contraction in good exports and explains in part the negative contribution from inventory changes. In addition, investment growth slowed markedly, mainly due to reduced investment in ships and aircraft. Domestic demand grew 3.2% year-on-year during the quarter. Of that total, consumption and investment grew by a total of 4.7%, with the difference reflecting the negative contribution from inventory changes. In spite of the impact of the fishermen's strike on exports, the contribution from net trade was positive during the quarter, as exports grew by 5.4% and imports by 3.1%.

GDP growth in Q1/2017 measured marginally below the forecast in the May issue of *Monetary Bulletin*. Investment was somewhat weaker than forecast, owing almost entirely to less residential investment than was reported in Statistics Iceland's figures. Private consumption growth was stronger, however, and the negative contribution from inventory changes was expected to be greater than Statistics Iceland's figures indicate. Growth in domestic demand turned out broadly as had been forecast. Growth in services exports was strong during the quarter but less than had been projected. The contribution from net trade was therefore smaller than had been assumed in the forecast in *Monetary Bulletin*.

The current account balance was positive by 11.1 b.kr., or 1.9% of GDP, in Q1/2017. This is a considerably smaller surplus than in the previous quarter and somewhat smaller than in Q1/2016, when it measured 2.6% of GDP. The surplus for this year was due to a 43.1 b.kr. surplus on services trade and a 3.1 b.kr. surplus on primary and secondary income, which were offset by a 35.1 b.kr. deficit on goods trade.

Indicators of developments in private consumption at the beginning of the quarter suggest that household demand growth is still robust but may have eased from the Q1/2017 measurement. The Gallup Consumer Confidence Index measured 123.6 points in May, a full 3 points lower than in April and about 12 points lower than in May 2016. Even though the index has fallen, it still indicates that households are optimistic, however.

According to the results of Gallup's summer survey, conducted in May among Iceland's 400 largest firms, respondents were very upbeat about the current economic situation but slightly more pessimistic about the outlook six months ahead than they were in the spring survey, conducted in March. They were slightly more optimistic than they were in the winter survey, however. About 80% of respondents considered the current situation good, and about 14% considered it neither poor nor good. Just under 19% of executives were of the view that economic conditions would improve in the next six months, and 65% expected conditions to remain unchanged (i.e., good). Executives in the construction and fishing industries were more pessimistic than other about the situation six months ahead, while optimism among companies in retail and wholesale trade diminished most in comparison with the spring survey. Executives in all sectors were more pessimistic than they were a year ago. About 16% of respondents expected conditions to be worse in six months' time, as opposed to 8% a year earlier. There was considerable optimism about domestic and foreign demand, albeit somewhat less than in the last survey.

According to the survey, firms interested in recruiting staff in the next six months outnumbered those planning redundancies by about 22 percentage points, after adjusting for seasonality. This is broadly similar to the percentage in the spring survey but lower than in the survey taken a year ago. The most positive executives were those in the financial and insurance sector, where firms planning to recruit outnumbered those planning redundancies by 38 percentage points. The most pronounced change was in the fishing industry, where firms planning to recruit outnumbered those planning redundancies by 14 percentage points in the summer survey, whereas in the spring survey the opposite was true: firms planning redundancies outnumbered those planning to add staff by 16 percentage points. In other sectors, the ratio lay in the range of 15-35 percentage points.

Adjusted for seasonality, 41% of firms considered themselves short-staffed, broadly the same as in the past year or so. The percentage of firms that considered themselves understaffed was highest in the financial and insurance sector, at 48%, and lowest in transport, transit, and tourism, at 31%. In other sectors it ranged between 35% and 45%.

The wage index rose by 0.2% month-on-month in April and by 4.9% year-on-year. Real wages in terms of the index had risen by 2.9% year-on-year in April.

Statistics Iceland's nationwide house price index, published at the end of May, rose 2.6% month-on-month after adjusting for seasonality, and by 22.5% year-on-year. The capital area real estate price index, calculated by Registers Iceland, rose by 2.7% month-on-month in April when adjusted for seasonality, and by 22.7% year-on-year. The number of purchase agreements registered nationwide in the first four months of 2017 were unchanged between years. The average time-to-sale for residential property in the greater Reykjavík area was about 1.4 months in the first four months of 2017, as opposed to 2 months during the same period in 2016.

The CPI rose by 0.2% month-on-month in May. Twelve-month inflation measured 1.7% in May and had tapered off since the MPC's March meeting. The CPI excluding the housing component had declined by 2.6% year-on-year, however. Most measures of underlying inflation suggested that it had declined even further in May and lay in the 0.6-1.7% range.

As before, the main driver of the CPI increase in May was the rise in house prices. Offsetting this was the seasonal decline in international airfares, although a reduction in the price of motor vehicle tyres also had a significant downward impact on the index. Private services

prices fell by 0.6% year-on-year, mainly because of reductions in telephone services prices and international airfares, although rises in other services prices have also subsided recently.

According to Gallup's summer survey, conducted in May, household inflation expectations declined between surveys, to 2.5% one year ahead and 3% two years ahead. Corporate executives' expectations also fell between surveys, to an all-time low of 1.8% one year ahead.

II The interest rate decision

The Governor reported to the Committee on the Executive Board of the International Monetary Fund's (IMF) Article IV discussion about the current situation and future prospects for the Icelandic economy. The Chief Economist reported on a discussion of the same topic at a meeting at the OECD in connection with the OECD's report on Iceland in which he had participated on behalf of the Bank. At both meetings, the capital flow management measure was discussed in particular.

The MPC discussed the monetary stance in view of the most recent information on the economy and the rise in the Bank's real rate between meetings. Members discussed whether this changed their assessment of whether the monetary stance was appropriate in view of the inflation outlook, as the Committee had been unanimous in May about its decision to lower the Bank's key rate by 0.25 percentage points, because the real rate had risen between meetings and the appreciation of the króna had contained demand.

Only a short time had passed since the previous meeting, and the information published in the interim largely supported the Committee's previous assessment of the economy. Members discussed the newly published national accounts figures for Q1/2017, which they considered to show that the outlook was broadly unchanged from the Bank's last forecast. GDP growth was weaker in Q1 than it had been in H2/2016, although it was in line with the forecast in the May issue of *Monetary Bulletin*. The GDP growth outlook for 2017 as a whole was therefore broadly unchanged. The national accounts figures showed that, as before, GDP growth was driven in particular by tourism and private consumption. The MPC also considered that the outlook was for significant fiscal easing in 2017, in addition to the easing in the previous two years.

Members noted that inflation was broadly as it had been over the past half-year but that underlying inflation appeared to have subsided in recent months. The gap between domestic price developments – housing costs in particular – and external factors had also widened significantly in recent months. As before, the MPC was of the view that opposing forces affected the inflation outlook, with the appreciation of the króna and low global inflation offsetting domestic inflationary pressures.

In addition, members noted that both short- and long-term inflation expectations had continued to fall since the last meeting and the Bank's real rate had therefore risen. Inflation expectations had been relatively stable in spite of exchange rate movements, indicating, in the Committee's opinion, that monetary policy had anchored them more securely.

The Committee discussed whether to keep interest rates unchanged or lower them. All members agreed that clear signs of demand pressures in the economy called for a continued tight monetary stance so as to ensure medium-term price stability. However, they were of the view that the increase in the Bank's real rate since the last MPC meeting entailed a somewhat tighter stance than the Committee had intended and considered sufficient to support price

stability. As a result, there were grounds for a nominal rate cut so that the Bank's real rate would remain unchanged from the previous meeting.

Committee members did not agree, however, on whether other factors warranted a further reduction in interest rates. One member preferred to take a larger step because real rates on loans to borrowers outside the real estate market were very high as a result of deflation as measured by the CPI excluding housing. Deflation by that measure had accelerated by 0.8 percentage points since the May meeting. Furthermore, this member was of the view that the strength of the króna dampened demand and gradually eroded exporters' equity, particularly in the case of exporters with króna-denominated debt. An interest rate reduction could therefore be seen as a measure to counterbalance the high and rising exchange rate. He also pointed out that increased competition in the goods market could lead to lower mark-ups, which would deliver higher real incomes and reduce the level of unemployment consistent with stable inflation.

The view was expressed that although the króna had not appreciated substantially between meetings, the accumulated appreciation over a longer period of time had already exerted considerable restraint, as did the strong króna. In addition to the effect on export sectors, there was probably some impact on the labour market as well. The rise in the exchange rate made it more economical for firms to import workers and mitigated outward migration. This had already resulted in less wage drift than could have been expected given the demand pressures in the labour market; furthermore, it could result in wage increases more in line with the inflation target and productivity growth in the coming round of wage negotiations.

Some members thought the probability that the rise in house prices in excess of the general price level and wages would reverse without also reversing the recent appreciation of the króna was no less than the probability of a less favourable interaction between house prices and the exchange rate. This warranted a continued cautious reduction in nominal interest rates, provided that credit growth did not accelerate too much.

One member pointed out that it was difficult to see how the current situation and near-term outlook called for monetary easing and that it was therefore only appropriate to reverse the increase in the real rate that had occurred between meetings. The fiscal stance had eased significantly; therefore, it was difficult to see where a tight stance would come from if not from monetary policy. This member also pointed out that the purpose of a tight monetary stance had indeed been to slow down economic activity, and that this purpose was being achieved. Furthermore, this member pointed out that with monetary policy stabilising inflation including housing, it was inevitable that inflation excluding housing would be very low or even negative when house prices rose steeply.

In view of the discussion, the Governor proposed that the Bank's interest rates be lowered by 0.25 percentage points, which would lower the key rate (the seven-day term deposit rate) to 4.5%, deposit rates (current account rates) to 4.25%, the seven-day collateralised lending rate to 5.25%, and the overnight rate to 6.25%. All Committee members voted in favour of the proposal. Two of them would have preferred to lower rates by 0.5 percentage points but were nonetheless willing to vote in favour of the Governor's proposal.

Members agreed that a stronger anchor for inflation expectations at target and the appreciation of the króna had enabled the MPC to achieve its legally mandated price stability objective with a lower interest rate than would otherwise have been possible. Members

agreed that in the coming term, the monetary stance would be determined by economic developments and actions taken in other policy spheres.

The following Committee members were in attendance:

Már Gudmundsson, Governor and Chairman of the Monetary Policy Committee

Arnór Sighvatsson, Deputy Governor

Thórarinn G. Pétursson, Chief Economist

Gylfi Zoëga, Professor, external member

Katrín Ólafsdóttir, Assistant Professor, external member

In addition, a number of Bank staff members attended part of the meeting.

Rannveig Sigurdardóttir wrote the minutes.

The next Statement of the Monetary Policy Committee will be published on Wednesday 23 August 2017.

Staða efnahagsmála og peningastefnan



Fyrirlestur hjá Rótarýklúbbi Kópavogs
21. febrúar 2017

Þórarinn G. Pétursson
Aðalhafgræðingur Seðlabanka Íslands

Þær skoðanir sem hér koma fram þurfa ekki að endurspeglar skoðanir annarra nefndarmanna Peningastefnunefndar

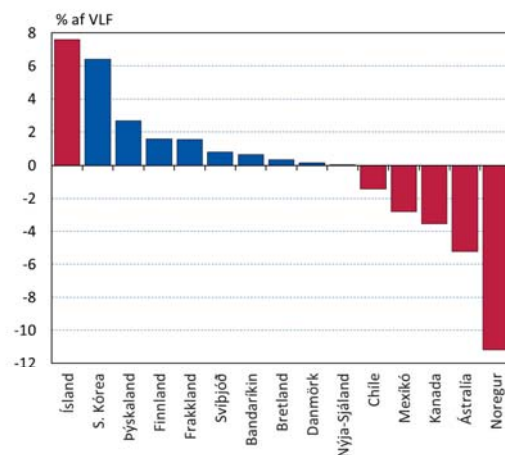
Tveir stórir búhnykkir: viðskiptakjarabati

- Útflutningsverð Íslands hækkaði um 17% 2014-16 í hlutfalli við útflutningsverð helstu viðskiptalanda sem er óvenjulegt í ljósi hægs hagvaxtar í viðskiptalöndum
- Viðskiptakjör hafa því batnað um 13½% – mun meiri bati en meðal annarra OECD-ríkja, sérstaklega meðal hrávöruútflytjenda

Útflutningsverð 1990-2016¹



Viðskiptakjaraáhrif í 15 OECD-ríkjum 2014-2016²



1. Útflutningsverð Íslands í hlutfalli við útflutningsverð helstu viðskiptalanda (fært í sama gjaldmiðli með vísitölu meðalgengis). Skyggða svæðið sýnir ár þar sem heimshagvöxtur er undir 25 ára meðaltali (1992-2016). Spáin fyrir heimshagvöxt 2016 er spá Alþjóðagjaldeyrissjóðsins (*World Economic Outlook*, október 2016). 2. Mismunur kaupmáttar útflutnings og útflutningsmagns í hlutfalli af VLF fyrra árs. Samtals áhrif fyrir árin 2014-2016. Þau lönd sem eru flokkuð sem hrávöruútflytjendur miðað við vægi hrávöru í hreinum útflutningi eru táknuð með rauðlitum súlum.

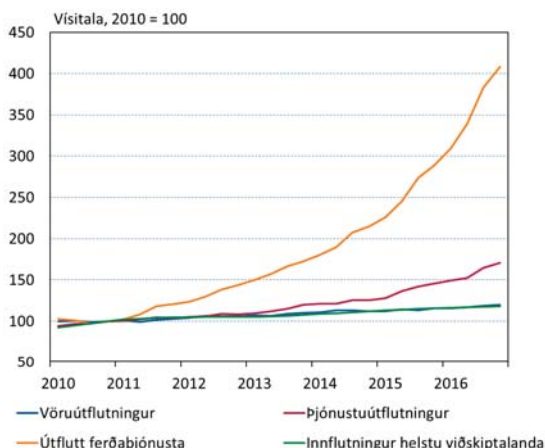
Heimildir: Alþjóðagjaldeyrissjóðurinn, Hagstofa Íslands, Macrobond, OECD, Sameinuðu þjóðirnar (UNCTAD), Seðlabanki Íslands.

Tveir stórir búhnykkir: vöxtur ferðapjónustu

- Útflutningsvöxtur hefur verið mikill undanfarið þrátt fyrir veikburða vöxt alþjóðaumsvifa: drifin áfram af gríðarlegum vexti ferðapjónustu sem óx um 37% í fyrra og hefur fjórfaldast síðan 2010 ...
- ... var, ásamt viðskiptakjarabata, meginástæða mikillar hækkunar gengis krónunnar í fyrra

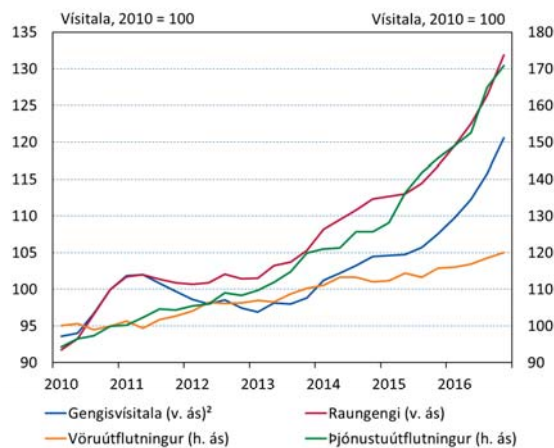
Útflutningur og alþjóðleg eftirspurn¹

1. ársfj. 2010 - 4. ársfj. 2016



Gengi krónunnar og útflutningur¹

1. ársfj. 2010 - 4. ársfj. 2016



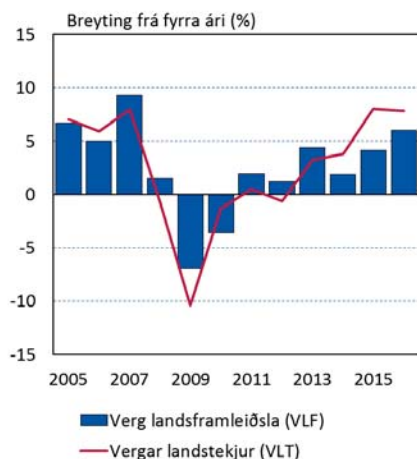
1. Fjögurra ársfjórðunga hreyfanlegt meðaltal. Útflutningstölur fyrir 4. ársfjórðung 2016 byggjast á grunnsþá *Peningamála* 2017/1. 2. Gengisvísitala sýnd þannig að hækkun vísitölu endurspeglar hækkun gengis krónunnar gagnvart erlendum gjaldmiðlum.

Heimildir: Hagstofa Íslands, Seðlabanki Íslands.

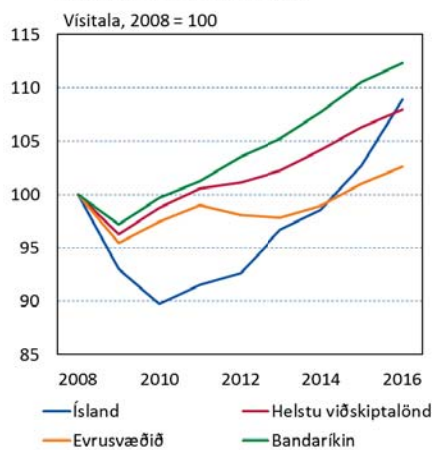
Efnahagsumsvif vaxa hratt en ytra jafnvægi betra ...

- Hagvöxtur áætlaður 6% í fyrra og kemur í kjölfar 4% hagvaxtar 2015 – tekjur hafa vaxið enn meira (8% hvort ár) ... mun meiri hagvöxtur en í öðrum þróuðum hagkerfum og samdráttur í kjölfar kreppu að fullu endurheimtur
- Ólíkt fyrri uppsveiflu er töluverður afgangur á viðskiptum við útlönd, vaxandi sparnaður og hrein skuldastaða orðin jákvæð

Hagvöxtur og tekjur 2005-2016^{1,3}



VLF á Íslandi og í helstu viðskiptalöndum 2008-2016³



Viðskiptajöfnuður og hrein erlend staða 2005-2016^{2,3}



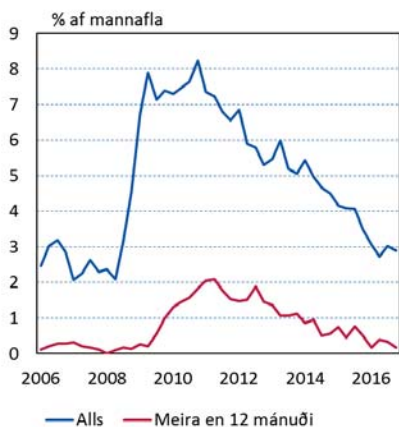
1. Vergar landstekjur (VLT) er verg landsframleiðsla (VLF) að viðbættum viðskiptakjaraáhrifum. 2. Undirliggjandi viðskiptajöfnuður og erlend staða (p.e. þar sem leiðrétt er fyrir áhrifum uppgjörs slitabúa fallinna fjármálfyrirtækja) fyrir árin 2008-2015. 3. Tölur fyrir 2016 byggjast á grunnsþá *Peningamála* 2017/1 nema að erlend staða er staðan á þriðja ársfjórðungi 2016.

Heimildir: Hagstofa Íslands, Macrobond, Seðlabanki Íslands.

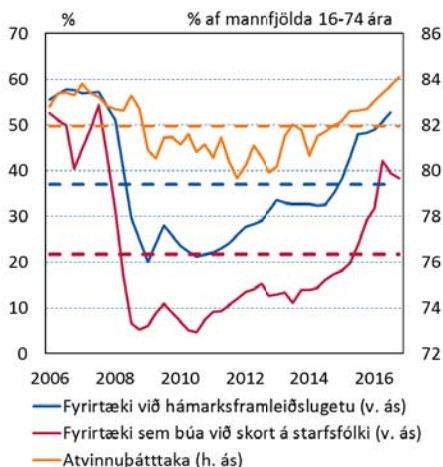
... en farið að reyna á þanþol þjóðarbúskaparins

- Vaxandi spenna í þjóðarbúinu: atvinnuleysi minnkað mikið og langtímaatvinnuleysi horfið ... vaxandi skortur á starfsfólki og æ fleiri fyrirtæki starfa við fulla framleiðslugetu ... atvinnuþátttaka eykst hratt og er orðin meiri en hún var mest fyrir kreppu
- Mikilli eftirspurn eftir vinnuafli mætt með innflutningi vinnuafis sem léttir að hluta á spennunni í þjóðarbúinu

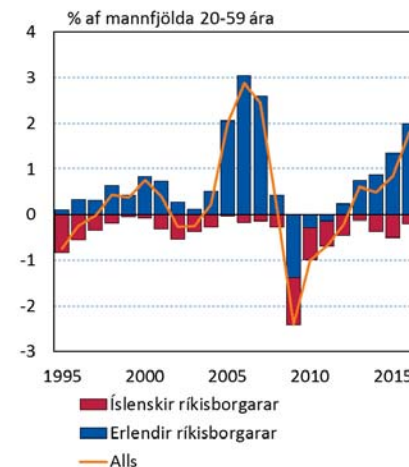
Atvinnuleysi 2006-2016¹



Nýting framleiðsluþátta og atvinnuþátttaka 2006-2016²



Aðfluttir umfram brottflutta 1995-2016³



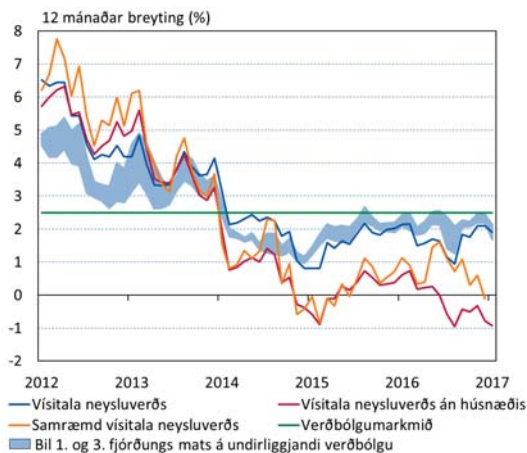
1. Árstíðarleiddar tölur fyrir 1. ársfj. 2006 - 4. ársfj. 2016. 2. Mælikvarðar á nýtingu framleiðsluþátta eru úr viðhorfskönnun Gallup meðal 400 stærstu fyrirtækja landsins en atvinnuþátttaka samkvæmt vinnuþátttökunni Hagstofunnar. Árstíðarleiddar tölur fyrir 1. ársfj. 2006 - 4. ársfj. 2016. Brotalínur sýna meðalhúlföll tímabilsins. 3. Búferlafutningar fólks á aldrinum 20-59 ára. Heimildir: Gallup, Hagstofa Íslands, Seðlabanki Íslands.

Mæld og undirliggjandi verðbólga nálægt markmiði

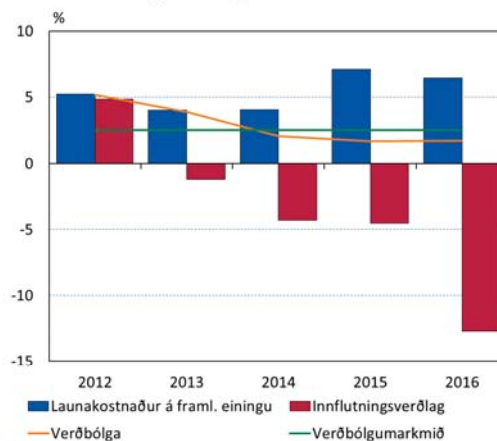
- Verðbólga var 1,9% í janúar – áþekkt því sem hún var í lok 2016 og á sama tíma í fyrra ... undirliggjandi verðbólga svipuð en verðbólga án húsnæðis mun minni: VNV án húsnæðis var -0,9% í janúar og HICP -0,1% í desember
- Vegast á áhrif 20% lækkunar innflutningsverðs 2014-16 og 19% hækkunar launakostnaðar á framleidda einingu yfir sama tíma

Mæld og undirliggjandi verðbólga¹

Janúar 2012 - janúar 2017



Verðbólga, launakostnaður og innflutningsverðlag 2012-2016²



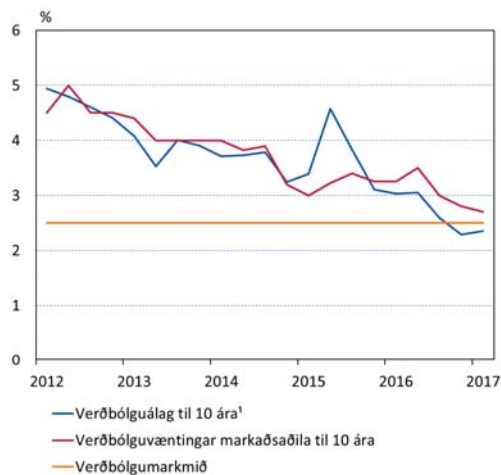
1. Skyggða svæðið inniheldur bil 1. og 3. fjórðungs mats á undirliggjandi verðbólgu þar sem hún er mæld með kjarnvísitölum sem horfa fram hjá áhrifum skattabreytinga, sveiflukenndra matvöruleiða, bensins, opinberrar þjónustu og reiknaðrar húsnæðis og með tölfraðilegum mælikvörðum eins og vagnu miðgildi, klipptum meðaltölum og kviku þáttalkani. 2. Launakostnaður á framleidda einingu er hlutfall launakostnaðar og framleiðni vinnuafis. Innflutningsverðlag er verðvísitala innflutnings vöru og þjónustu. Tölur fyrir 2016 byggjast á grunnspá *Peningamála* 2017/1. Heimildir: Hagstofa Íslands, Seðlabanki Íslands.

Peningastefnan hefur náð árangri ...

- Verðbólguvæntingar hafa smám saman lækkað í átt að markmiði eftir að hafa verið vel fyrir ofan það um langa hríð ...
- ... hættu virtist þó á að nýfengin kjölfesta þeirra brysti í kjölfar kjarasamninga vorið 2015
- Peningastefnunefnd brást við með hækkun vaxta og skilaboðum um frekari hækkanir ef með þurfti ... það dugði til að koma þeim smám saman aftur í markmið sem gerði nefndinni kleift að lækka vexti á ný

Langtímaverðbólguvæntingar

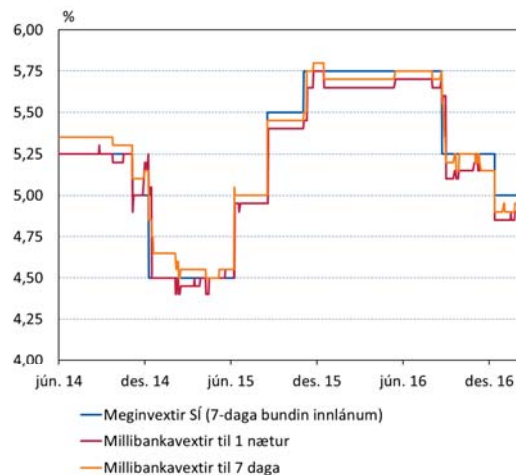
1. ársfj. 2012 - 1. ársfj. 2017



1. Tala fyrir 1. ársfjórðung 2017 er meðaltal það sem af er fjórðungnum.
Heimild: Seðlabanki Íslands.

Meginvextir Seðlabanka Íslands

1. júní 2014 - 31. janúar 2017

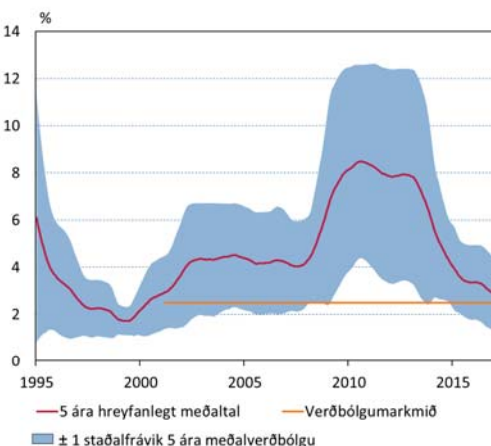


... en fullnaðarsigur ekki í höfn

- Þrátt fyrir að peningastefnan hafi náð nokkrum árangri við að auka efnahagslegan stöðugleika undanfarið er enn nokkuð í land við að tryggja varanleika þessa árangurs ... því þarf að fara varlega og vera viðbúin bakslagi
- Samanburður við Noreg sýnir þetta ágætlega: Norska seðlabankanum hefur tekist að halda verðlagi stöðugu yfir mun lengri tíma sem eykur trúverðuleika bankans og eykur sveigjanleika hans við mótun peningastefnunnar

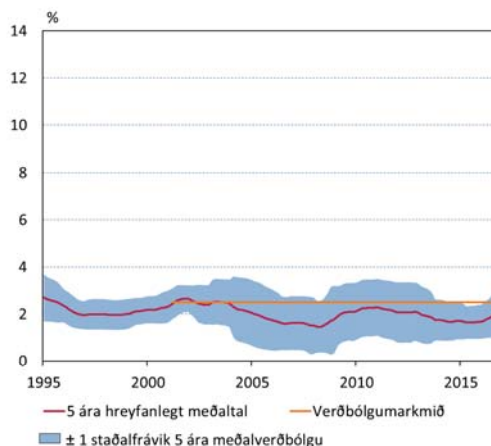
5 ára meðalverðbólga á Íslandi

Janúar 1995 - desember 2016



5 ára meðalverðbólga í Noregi

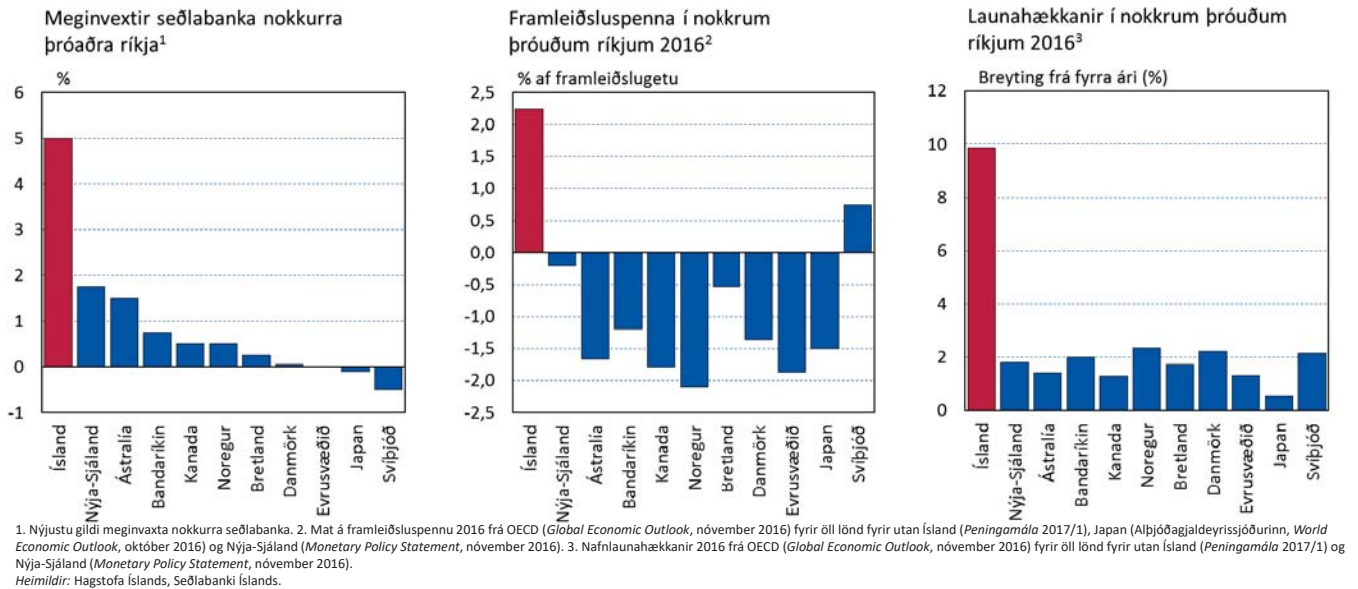
Janúar 1995 - desember 2016



Heimildir: Hagstofa Íslands, Noregsbanki, OECD, Seðlabanki Íslands.

Efnahagsaðstæður einnig ólíkar hér á landi

- Við samanburð á vöxtum hér á landi og í nágrennaríkjunum þarf ekki einungis að hafa í huga hvað saga verðstöðugleika er í raun stutt hér á landi ...
- ... einnig að hér er mikill hagvöxtur og vaxandi spenna en þrálátur slaki og hæggangur í hinum ríkjunum



Breytingar á ramma peningastefnunnar?

Hávær umræða um að breyta þurfi ramma peningastefnunnar

- Eðlilegt að fara reglulega yfir reynsluna og skoða mögulegar umbætur ...
- ... en ekki er ljóst hvað það er sem kallar á róttækar breytingar á rammanum – sérstaklega í ljósi árangurs undanfarið

Þegar verið gerðar miklar breytingar

- Fjölskipuð peningastefnunefnd og stórukið gagnsæi
- Viðbótarstjórntæki: inngrip á gjaldeyrismarkaði, þjóðhagsvarúð og fjárstreymistæki

Öllum útfærslum peningastefnu fylgja kostir og gallar

- Mismunandi fyrirkomulagi fastgengis fylgja einnig gallar ...
- ... og gæti verið feigðarflan ef framkvæmd stefnunnar í ríkisfjármálum er ekki bætt og ekki eru gerðar veigamiklar breytingar á skipulagi vinnumarkaðar

Ástand og horfur í efnahagsmálum



Þingflokkur Vinstri Grænna
27. mars 2017

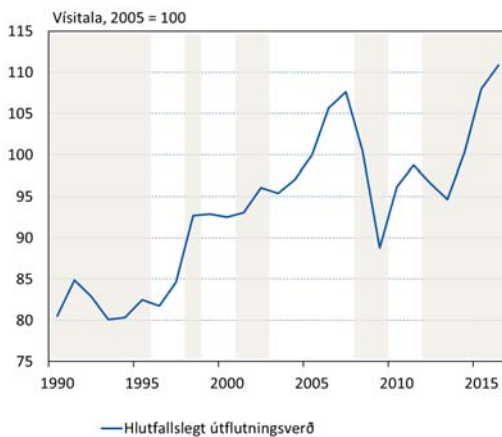
Þórarinn G. Pétursson
Aðalhogfræðingur Seðlabanka Íslands

Þær skoðanir sem hér koma fram þurfa ekki að endurspeglja skoðanir annarra nefndarmanna peningastefnunefndar

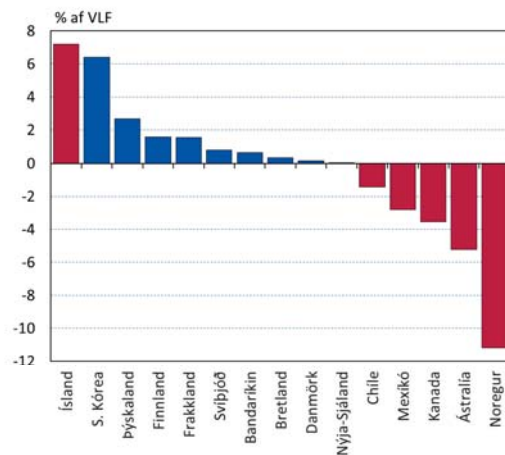
Tveir stórir búhnykkir: viðskiptakjarabati

- Útflutningsverð Íslands hækkaði um 17% 2014-16 í hlutfalli við útflutningsverð helstu viðskiptalanda sem er óvenjulegt í ljósi hægs hagvaxtar í viðskiptalöndum
- Viðskiptakjör hafa því batnað um 13% – mun meiri bati en meðal annarra OECD-ríkja, sérstaklega meðal hrávöruútflytjenda

Útflutningsverð 1990-2016¹



Viðskiptakjaraáhrif í 15 OECD-ríkjum 2014-2016²



1. Útflutningsverð Íslands í hlutfalli við útflutningsverð helstu viðskiptalanda (fært í sama gjaldmiðli með vísitölu meðalgengis). Skyggða svæðið sýnir ár þar sem heimshagvöxtur er undir 25 ára meðaltali (1992-2016). Spáin fyrir heimshagvöxt 2016 er spá Alþjóðagjaldeyrissjóðsins (*World Economic Outlook*, október 2016). 2. Mismunur kaupmáttar útflutnings og útflutningsmagns í hlutfalli af VLF fyrra árs. Samtals áhrif fyrir árin 2014-2016. Þau lönd sem eru flokkuð sem hrávöruútflytjendur miðað við vægi hrávöru í hreinum útflutningi eru táknuð með rauðlitum súlum.

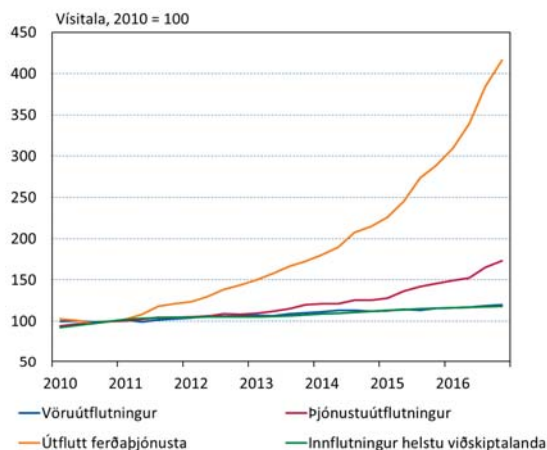
Heimildir: Alþjóðagjaldeyrissjóðurinn, Hagstofa Íslands, Macrobond, OECD, Sameinuðu þjóðirnar (UNCTAD), Seðlabanki Íslands.

Tveir stórir búhnykkir: vöxtur ferðapjónustu

- Útflutningsvöxtur hefur verið mikill undanfarið þrátt fyrir veikburða vöxt alþjóðaumsvifa: drifin áfram af gríðarlegum vexti ferðapjónustu sem óx um 44% í fyrra og hefur ríflega fjórfaldast síðan 2010 ...
- ... skýrir um ⅓ af 10% meðalvexti útflutnings undanfarinna 2 ára

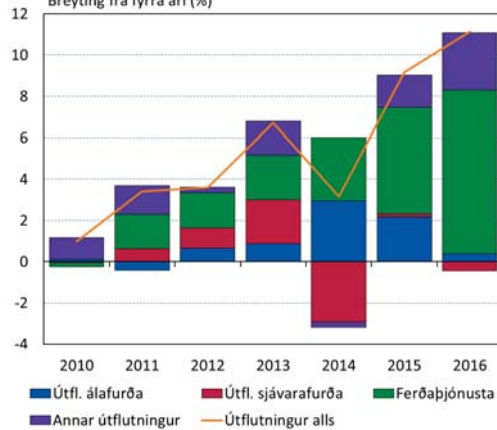
Útflutningur og alþjóðleg eftirspurn¹

1. ársfj. 2010 - 4. ársfj. 2016



Útflutningur og framlag undirliða 2010-2016²

Breyting frá fyrra ári (%)

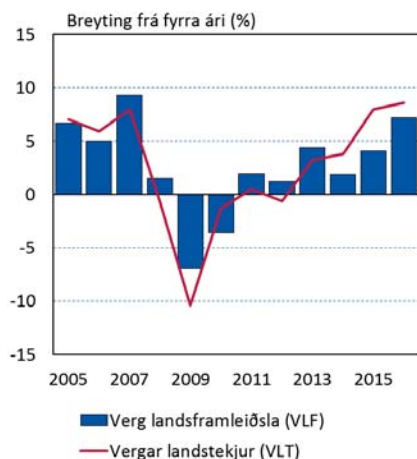


1. Fjögurra ársfjórðunga hreyfanlegt meðaltal. 2. Útflutningur álafurða samkvæmt þjóðhagsreikningum. Heimildir: Hagstofa Íslands, Macrobond, Seðlabanki Íslands.

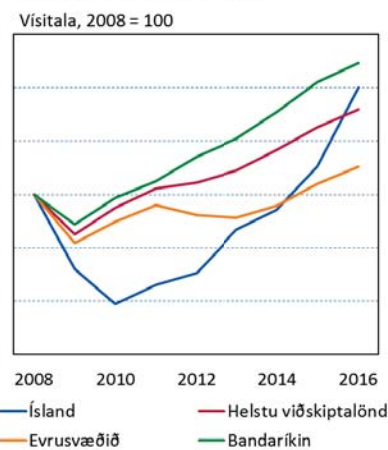
Efnahagsumsvif vaxa hratt en ytra jafnvægi betra ...

- Hagvöxtur mældist 7,2% í fyrra og kemur í kjölfar 4,1% hagvaxtar 2015 – tekjur hafa vaxið enn meira (yfir 8% hvort ár) ... mun meiri hagvöxtur en í öðrum þróuðum hagkerfum og samdráttur í kjölfar kreppu að fullu endurheimtur
- Ólíkt fyrri uppsveiflu er töluverður afgangur á viðskiptum við útlönd, vaxandi sparnaður og hrein skuldastaða orðin jákvæð

Hagvöxtur og tekjur 2005-2016¹



VLF á Íslandi og í helstu viðskiptalöndum 2008-2016



Viðskiptajöfnuður og hrein erlend staða 2005-2016²

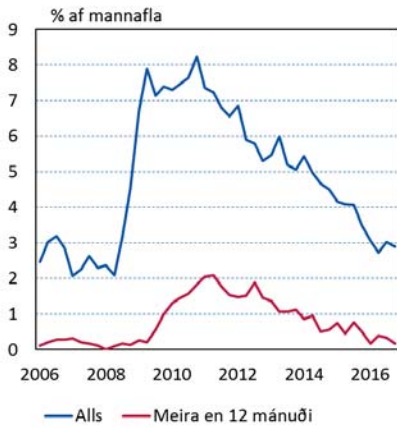


1. Vergar landstekjur (VLT) eru verg landsframleiðsla (VLF) að viðbættum viðskiptakjaraáhrifum. 2. Undirliggjandi viðskiptajöfnuður og erlend staða (þ.e. þar sem leiðrétt er fyrir áhrifum uppgjörs slitabúa fallinna fjármálafyrirtækja) fyrir árin 2008-2015. Heimildir: Hagstofa Íslands, Macrobond, Seðlabanki Íslands.

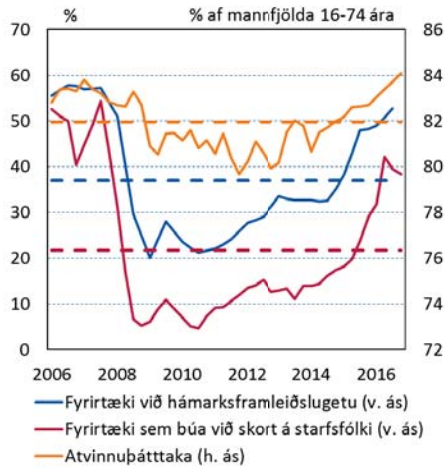
... en farið að reyna á þanþol þjóðarbúskaparins ...

- Vaxandi spenna í þjóðarbúinu: atvinnuleysi minnkað mikið og langtímaatvinnuleysi horfið ... vaxandi skortur á starfsfólki og æ fleiri fyrirtæki starfa við fulla framleiðslugetu ... atvinnuþátttaka eykst hratt og er orðin meiri en hún var mest fyrir kreppu
- Mikilli eftirspurn eftir vinnuafli mætt með innflutningi vinnuafis sem léttir að hluta á spennunni í þjóðarbúinu

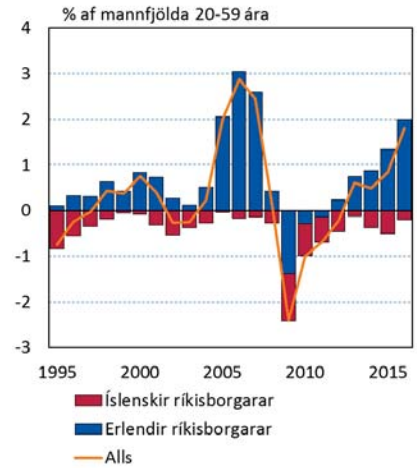
Atvinnuleysi 2006-2016¹



Nýting framleiðsluþátta og atvinnuþátttaka 2006-2016²



Aðfluttur umfram brottflutta 1995-2016³

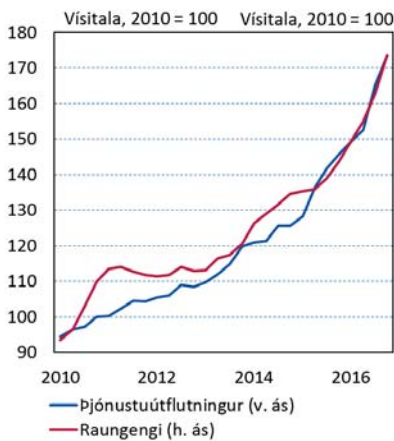


1. Árstoðarleiddar tölur fyrir 1. ársfj. 2006 - 4. ársfj. 2016. 2. Mælikvarðar á nýtingu framleiðsluþátta eru úr viðhorfskönnun Gallup meðal 400 stærstu fyrirtækja landsins en atvinnuþátttaka samkvæmt vinnuþátttöku Hagstofunnar. Árstoðarleiddar tölur fyrir 1. ársfj. 2006 - 4. ársfj. 2016. Brotalínur sýna meðalhluftöll tímabilsins. 3. Búferlaflutningar fólks á aldrinum 20-59 ára. Heimildir: Gallup, Hagstofa Íslands, Seðlabanki Íslands.

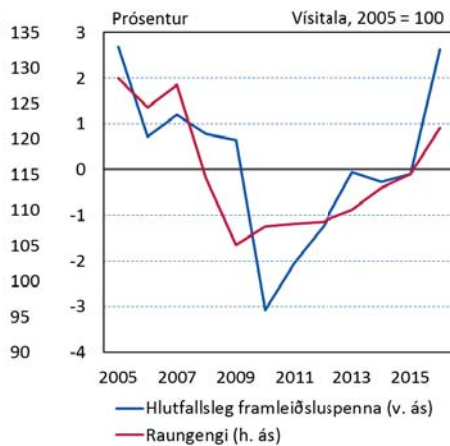
... og hefur leitt til mikillar gengishækkunar ...

- Þessi mikli vöxtur ferðapjónustu hefur reynt á innlenda framleiðsluþætti og kallað á verulega aðlögun í þjóðarbúskapnum ... sem birtist m.a. í því að hinn nýi útflutningsgeiri ryður í burt annarri útflutningsstarfsemi með því að þrýsta upp genginu
- Gengispróunin í ágætu samræmi við það sem vænta má í ljósi þróunar efnahagssumsvifa hér á landi og erlendis

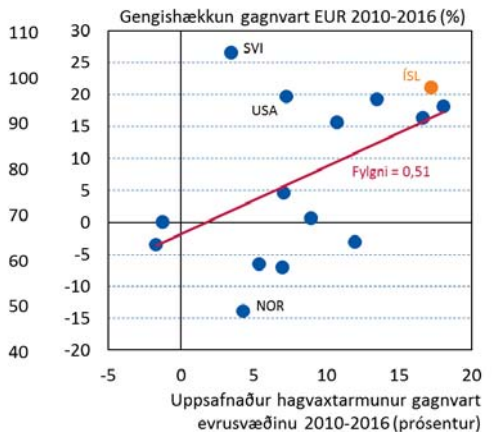
Gengi krónunnar og útflutningur¹
1. ársfj. 2010 - 4. ársfj. 2016



Hagsveiflan og raungengið 2005-2016²



Hagvöxtur og gengi í 15 iðnríkjum 2010-2016³

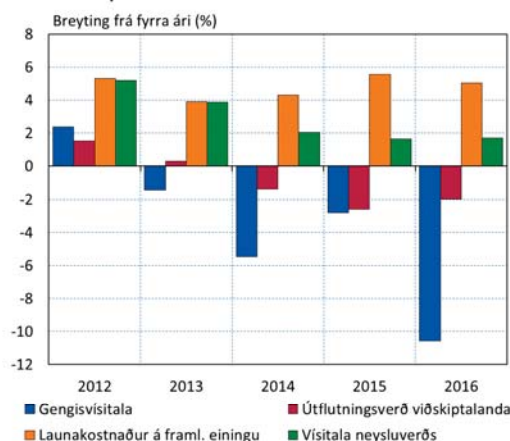


1. Fjögurra ársfjórðunga hreyfanlegt meðaltal. 2. Mismunur framleiðsluþátttöku á Íslandi og í helstu viðskiptalöndum. Matíð á framleiðsluþátttöku á Íslandi byggir á frávikum VLF frá framleiðslugetu út frá framleiðslufalli þjóðhagslíkans Seðlabankans. Framleiðsluþátttöku í helstu viðskiptalöndum er metin út frá frávikum VLF í helstu viðskiptalöndum frá Hodrick-Prescott-leitniferli (með $\lambda = 1.600$). Raungengi er miðað við hlutfallslegt neysluverðlag. 3. Uppsafnaður hagvaxtarmunur er mismunur breytingar VLF frá 2010 til 2016 fyrir hvert land og fyrir evrusvæðið. Breyting á gengi gjaldmiðla gagnvart EUR er breyting milli ársmeðaltala 2010 og 2016. Hækkun táknar hækkun gjaldmiðils gagnvart EUR. Heimildir: Hagstofa Íslands, Macrobond, Seðlabanki Íslands.

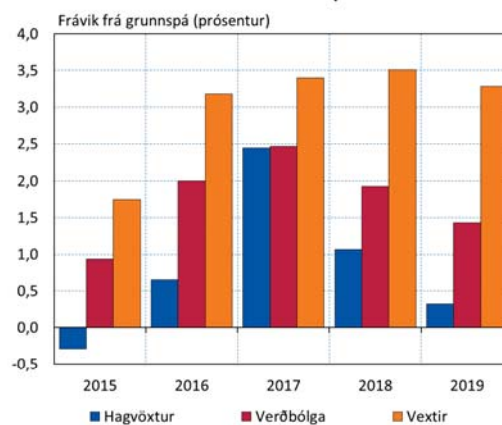
... sem er mikilvægur hluti efnahagsaðlögunarinnar

- Gengishækkunin hefur, ásamt lítilli alþjóðlegri verðbólgu, vegið á móti miklum innlendum verðbólguþrýstingi: 2014-16 lækkaði innflutningsverð um 20% en launakostnaður á framleidda einingu lækkaði um 16%
- Án gengisaðlögunarinnar væri ójafnvægið meira og verðbólguþrýstingur meiri og vextir þyrftu að öðru óbreyttu að vera hærri

Verðbólga og innlendir og alþjóðlegir áhrifaþættir 2012-2016¹



Hagvöxtur, verðbólga og vextir ef gengi krónunnar hefði verið óbreytt frá 2014¹



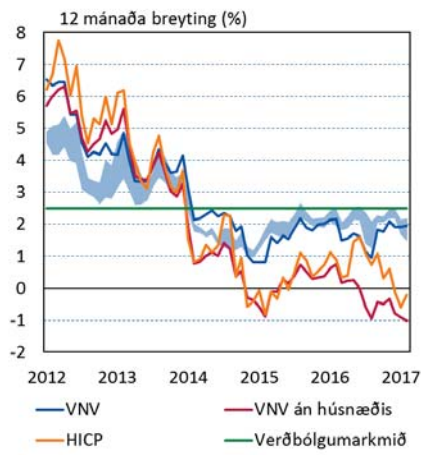
1. Hækkun gengisvísitölu endurspeglar lækkaði gengi krónunnar gagnvart meðaltali annarra gjaldmiðla. Launakostnaður á framleidda einingu er hlutfall launakostnaður og framleiðni vinnuafis. 2. Samanburður á grunnspá PM 2017/1 og hermun með þjóðhagslíkani Seðlabankans þar sem gengisvísitalan helst óbreytt í um 207 stigum frá 2014 og út spátímann. Heimildir: Hagstofa Íslands, Seðlabanki Íslands.

Verðstöðugleiki og traustari kjölfesta væntinga ...

- Verðbólga var 1,9% í febrúar – áþekk því sem hún hefur verið undanfarið hálf tölur ... undirliggjandi verðbólga svipuð en verðbólga án húsnæðis mun minni: VNV án húsnæðis -1% og HICP -0,2%
- Verðbólguvæntingar hafa smám saman lækkað í átt að markmiði eftir að hafa verið vel fyrir ofan það um langa hríð

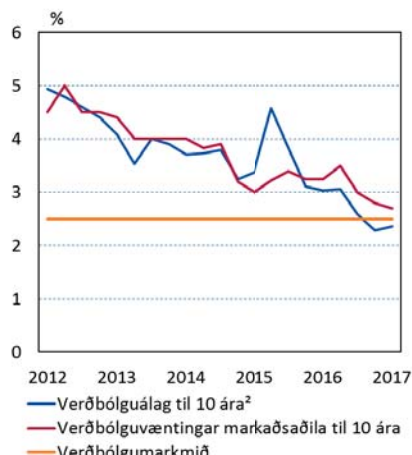
Mæld og undirliggjandi verðbólga¹

Janúar 2012 - febrúar 2017



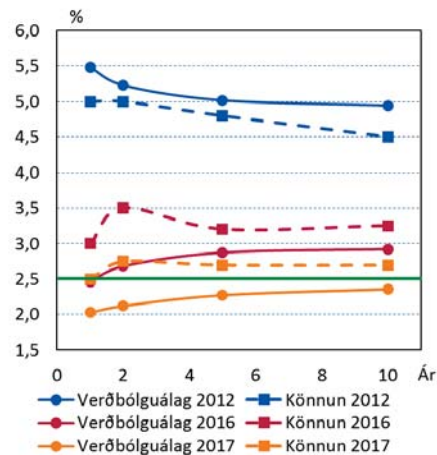
Langtíma-verðbólguvæntingar

1. ársfj. 2012 - 1. ársfj. 2017



Verðbólguvæntingar til 1-10 ára³

Mælingar á 1. ársfj. 2012, 2016 og 2017

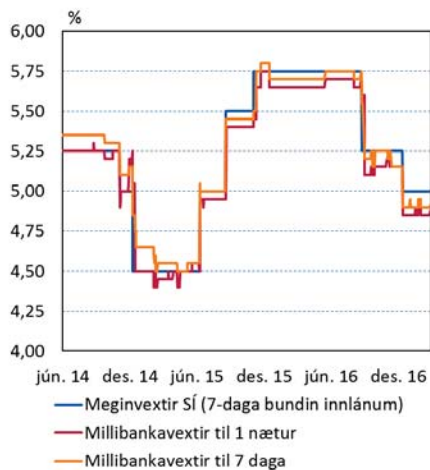


1. Skyggða svæðið inniheldur bil 1. og 3. fjórðungs mats á undirliggjandi verðbólgu þar sem hún er mæld með kjarnavísitölu sem horfa fram hjá áhrifum skattabreytinga, sveiflukenndra matvörulíða, bensins, opinberra þjónustu og reiknaðar húsaleigu og með tölræðilegum mælikvörðum eins og vagnu miðgildi, klipptum meðaltölum og kviku þáttalkani. 2. Talan fyrir 1. ársfjórðung 2017 er meðaltal það sem af er fjórðungnum. 3. Verðbólguvæntingar til 1, 2, 5 og 10 ára út frá verðbólguálagi á skuldabréfamarkaði (ársfjórðungsleg meðaltöl) og könnun meðal markaðsaðila. Heimildir: Hagstofa Íslands, Seðlabanki Íslands.

... fyrir tilstuðlan aðhaldssamrar peningastefnu ...

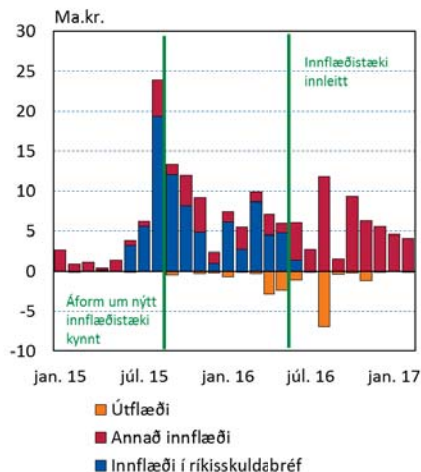
- Vextir bankans voru teknir að lækka en voru hækkaðir skarpt í kjölfar kjarasamninga 2015 til að ná aftur tókum á verðbólguvæntingum ... þegar það tókst tóku þeir að lækka á ný – þannig stuðlar peningastefnan að langtíma verðstöðugleika
- Önnur stjórnþæki: fjárstreymistæki og inngrip á gjaldeyrismarkaði – notuð til að ná öðrum markmiðum

Fjármagnsflæði vegna nýfjárfestinga
1. júní 2014 - 28. febrúar 2017

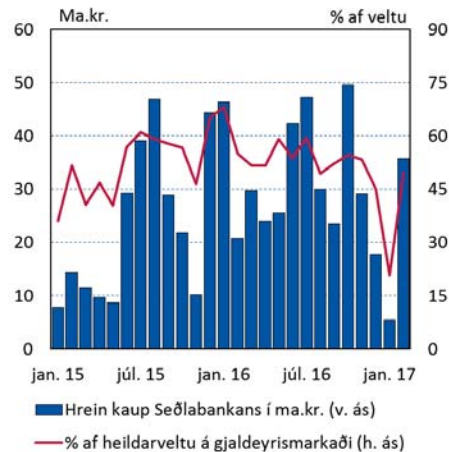


1. Fjármagnsflæði vegna skráðra nýfjárfestinga.
Heimild: Seðlabanki Íslands.

Fjármagnsflæði vegna nýfjárfestinga¹
Janúar 2015 - febrúar 2017



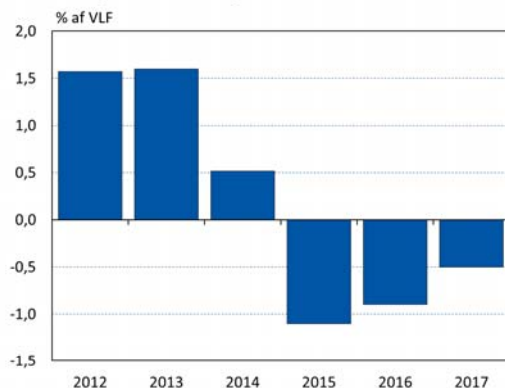
Gjaldeyriskaup Seðlabankans
Janúar 2015 - febrúar 2017



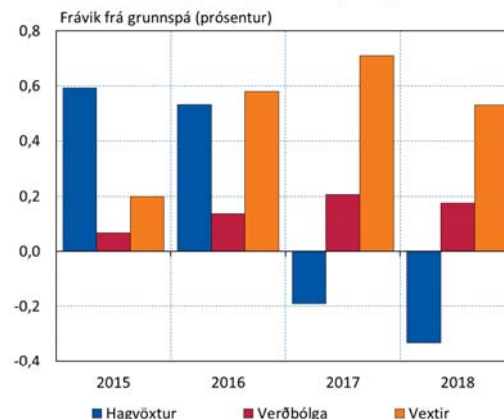
... en á sama tíma slaknar á aðhaldi ríkisfjármála

- Vaxandi spenna í þjóðarþúinu hefur kallað á aðhaldssama peningastefnu – en á sama tíma hefur slaknað á aðhaldi opinberra fjármála: slökunin um 2% af VLF 2015-2016 – og nýleg fjárlög benda til tæplega ½% viðbótarslökunar í ár
- Slökunin hefur aukið á eftirspurn og þenslu, þrýst enn frekar á gengi krónunnar og kallað á hærri vexti en ella

Breyting á hagsveifluleiðréttum
frumjöfnuði ríkissjóðs 2012-2017¹



Áhrif slökunar á aðhaldsstigi ríkisfjármála
2015-16 á hagvöxt, verðbólgu og vexti¹

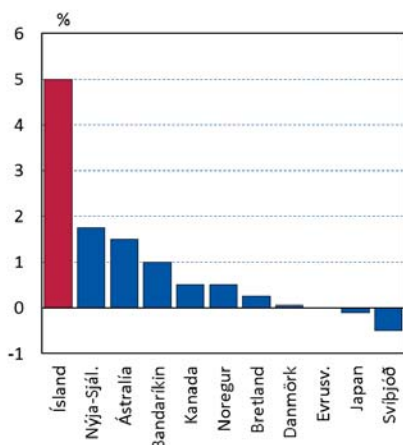


1. Frumjöfnuður er leiðréttur fyrir einkisþekjum og gjöldum (t.d. stöðugleikaframlögum og flýtingu niðurgreiðslu verðtryggðra húsnæðislána). Um er að ræða uppfært mat á breytingunni á hagsveifluleiðréttum frumjöfnuði ríkissjóðs frá PM 2016/4. Tekið hefur verið tillit til nýs mats á framleiðsluspennunni á tímabilinu í samræmi við PM 2017/1 auk þess sem sá hluti samgönguáætlunar sem er umfram fjárlög ársins 2017 og fjármálaáætlun hefur verið felldur út. 2. Mat á áhrifum slökunar á aðhaldsstigi ríkisfjármála 2015-2016 um 2½% af VLF út frá hermun með þjóðhagslíkani Seðlabankans (sjá nánar umfjöllun í PM 2016/2).
Heimildir: Fjármála- og efnahagsráðuneytið, Seðlabanki Íslands.

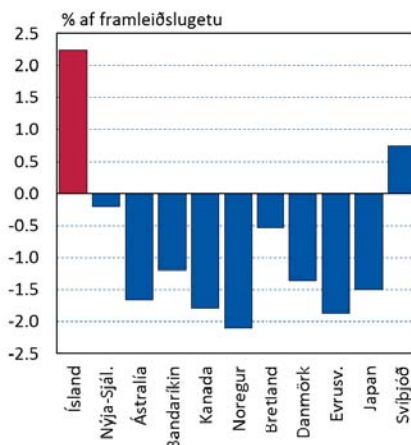
Af hverju eru vextir hærri hér en í öðrum iðnríkjum?

- Afar takmarkað hvað peningastefnan getur gert við kerfisbreytingu á samsetningu útflutnings og hækkun jafnvægisgengis – hennar verkefni er að tryggja verðstöðugleika sem hefur tekist undanfarin ár ... þrátt fyrir mikla spennu í þjóðarbúskapnum
- Allt aðrar aðstæður en í nágrennaríkjunum þar sem enn er mikill slaki og verðbólguvæntingar hafa leitað undir markmið

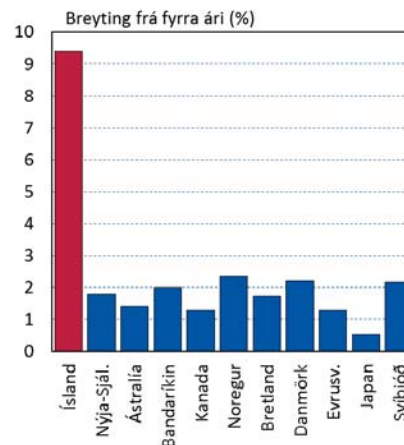
Meginvextir seðlabanka nokkurra þróaðra ríkja¹



Framleiðsluspenna í nokkrum þróuðum ríkjum 2016²



Launahækkunir í nokkrum þróuðum ríkjum 2016³



1. Nýjstu gildi meginvaxta nokkurra seðlabanka. 2. Mat á framleiðsluspennu 2016 frá OECD (*Global Economic Outlook*, nóvember 2016) fyrir öll lönd fyrir utan Ísland (*Peningamála* 2017/1), Japan (*Alþjóðagjaldeyrissjóðurinn, World Economic Outlook*, október 2016) og Nýja-Sjáláland (*Monetary Policy Statement*, nóvember 2016). 3. Nafnlaunahækkunir 2016 frá OECD (*Global Economic Outlook*, nóvember 2016) fyrir öll lönd fyrir utan Ísland og Nýja-Sjáláland (*Monetary Policy Statement*, nóvember 2016).
 Heimildir: Alþjóðagjaldeyrissjóðurinn, Hagstofa Íslands, OECD, Seðlabanki Nýja-Sjálálands, Seðlabanki Íslands.

Allt sem þú vildir vita um gengi krónunnar (en þóðir ekki að spyrja)



Ferðapjónustudagur
16. mars 2017

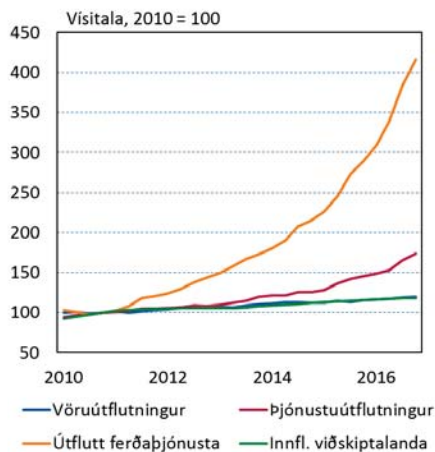
Þórarinn G. Pétursson
Aðalhogfræðingur Seðlabanka Íslands

Þær skoðanir sem hér koma fram þurfa ekki að endurspeglar skoðanir annarra nefndarmanna peningastefnufndar

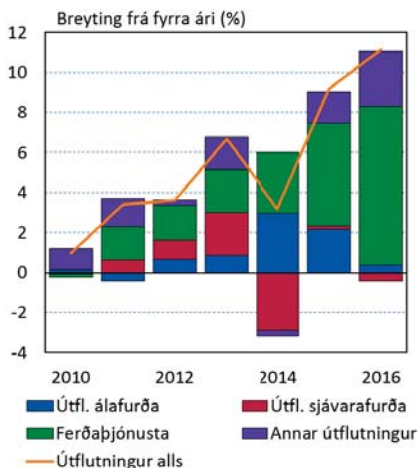
Hraður vöxtur útflutnings og efnahagsumsvifa ...

- Útflutningsvöxtur hefur verið mikill undanfarið þrátt fyrir hægna vöxt alþjóðaviðskipta: drifin áfram af gríðarlegum vexti ferðapjónustu sem óx um 44% í fyrra og hefur fjórfaldast síðan 2010: skýrir um ¾ af 10% meðalvexti útflutnings sl. 2 ára
- Hagvöxtur hefur verið mikill og tekjur vaxið enn meira – hagvöxtur langt umfram hagvaxtargetu og hagvöxt viðskiptalanda

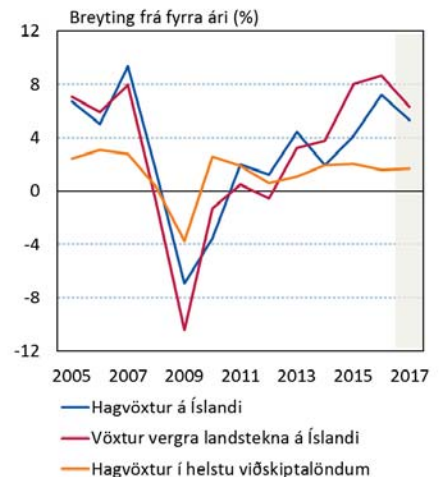
Útflutningur og alþjóðleg eftirspurn¹
1. ársfj. 2010 - 4. ársfj. 2016



Útflutningur og framlag undirliða
2010-2016²



Hag- og tekjuvöxtur 2005-2017³

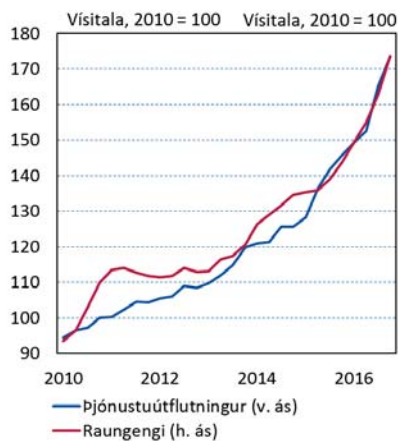


1. Fjögurra ársfjórðunga hreyfanlegt meðaltal. 2. Útflutningur álafurða skv. þjóðhagsreikningum. 3. Vergar landstekjur eru verg landsframleiðsla leiðrétt fyrir viðskiptakjaraáhrifum. Skyggt svæði sýnir grunnspá PM 2017/1 fyrir 2017.
Heimildir: Hagstofa Íslands, Macrobond, Seðlabanki Íslands.

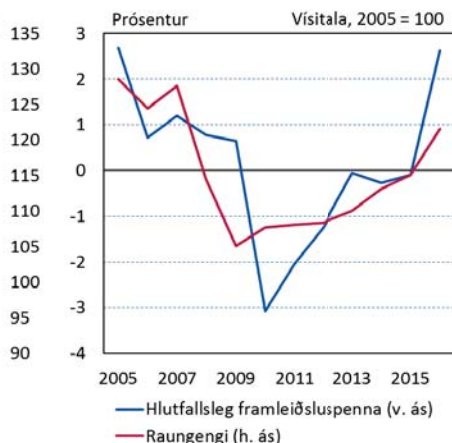
... hefur leitt til mikillar gengishækkunar ...

- Þessi mikli vöxtur ferðapjónustu hefur reynt á innlenda framleiðsluþætti og kallað á verulega aðlögun í þjóðarbúskapnum ... sem birtist m.a. í því að hinn nýi útflutningsgeiri ryður í burt annarri útflutningsstarfsemi með því að þrýsta upp genginu
- Gengisþróunin í ágætu samræmi við það sem vænta má í ljósi þróunar efnahagssumsvifa hér á landi og erlendis

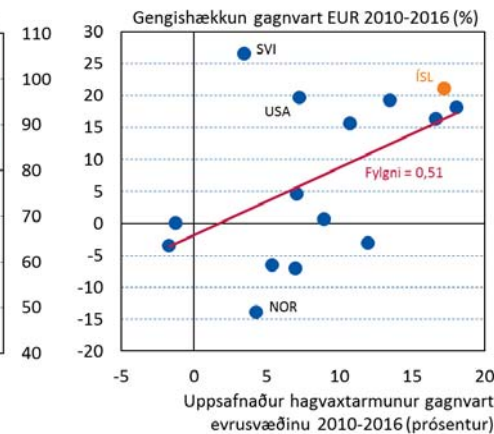
Gengi krónunnar og útflutningur¹
1. ársfj. 2010 - 4. ársfj. 2016



Hagsveiflan og raungengið 2005-2016²



Hagvöxtur og gengi í 15 iðnríkjum 2010-2016³

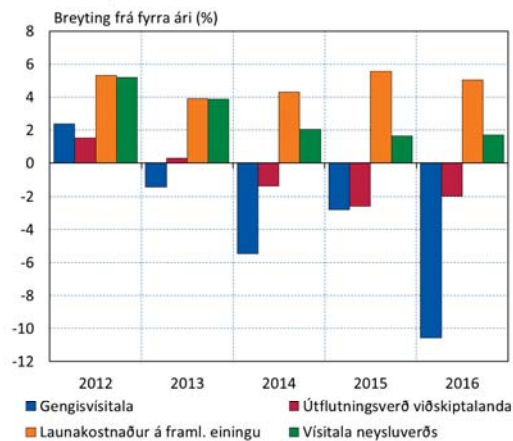


1. Fjögurra ársfjórðunga hreyfanlegt meðaltal. 2. Mismunur framleiðsluspennu á Íslandi og í helstu viðskiptalöndum. Matíð á framleiðsluspennu á Íslandi byggir á frávikum VLF frá framleiðslugetu út frá framleiðslufalli þjóðhagslíkans Seðlabankans. Framleiðsluspenna í helstu viðskiptalöndum er metin út frá frávikum VLF í helstu viðskiptalöndum frá Hodrick-Prescott-leitniferli (með $\lambda = 1.600$). Raungengi er miðað við hlutfallslegt neysluverðlag. 3. Uppsafnaður hagvaxtarmunur er mismunur breytingar VLF frá 2010 til 2016 fyrir hvert land og fyrir evrusvæðið. Breyting á gengi gjaldmiðla gagnvart EUR er breyting milli ársmeðaltala 2010 og 2016. Hækkun táknar hækkun gjaldmiðils gagnvart EUR.
Heimildir: Hagstofa Íslands, Macrobond, Seðlabanki Íslands.

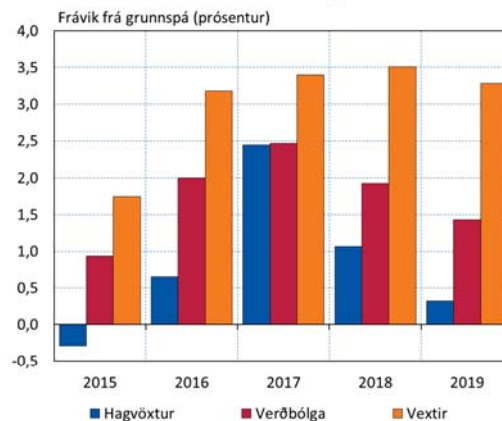
... sem er mikilvægur hluti efnahagsaðlögunarinnar

- Gengishækkunin hefur, ásamt lítilli alþjóðlegri verðbólgu, vegið á móti miklum innlendum verðbólguþrýstingi: 2014-16 lækkaði innflutningsverð um 20% en launakostnaður á framleidda einingu hækkaði um 16%
- Án gengisaðlögunarinnar væri ójafnvægið meira og verðbólguþrýstingur meiri og vextir þyrftu að öðru óbreyttu að vera hærri

Verðbólga og innlendir og alþjóðlegir áhrifaþættir 2012-2016¹



Hagvöxtur, verðbólga og vextir ef gengi krónunnar hefði verið óbreytt frá 2014¹

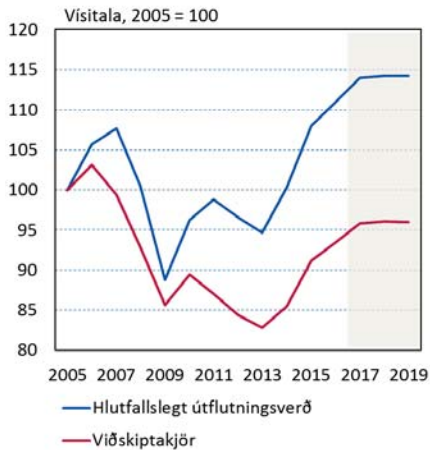


1. Hækkun gengisvísitölu endurspeglar lækkanði gengi krónunnar gagnvart meðaltali annarra gjaldmiðla. Launakostnaður á framleidda einingu er hlutfall launakostnaður og framleiðni vinnuafli. 2. Samanburður á grunnspá PM 2017/1 og hermun með þjóðhagslíkani Seðlabankans þar sem gengisvísitalan helst óbreytt í um 207 stigum frá 2014 og út spáttímann.
Heimildir: Hagstofa Íslands, Seðlabanki Íslands.

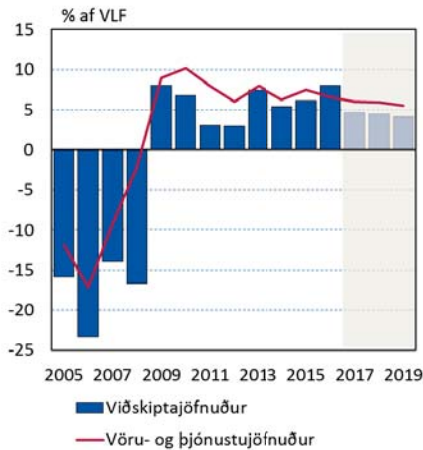
Hefur gengi krónunnar ofrисиð?

- Gengið hefur vissulega hækkað mikið og sett útflutningsáttugreinar í vanda – en er hækkunin óeðlilega mikil?
- Ekki augljóst að svo sé: virðist ljóst að jafnvægisgengi krónunnar hafi hækkað mikið: viðskiptakjör hafa batnað verulega, búið að vera töluverður viðskiptaafgangur í 8 ár samfelt og gríðarleg breyting hefur orðið á hreinni skuldastöðu þjóðarbúsins

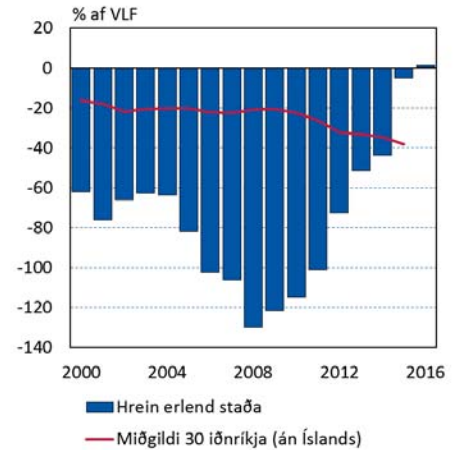
Útflutningsverð og viðskiptakjör 2005-2019¹



Viðskiptajöfnuður 2005-2019²



Hrein erlend staða 2000-2016³

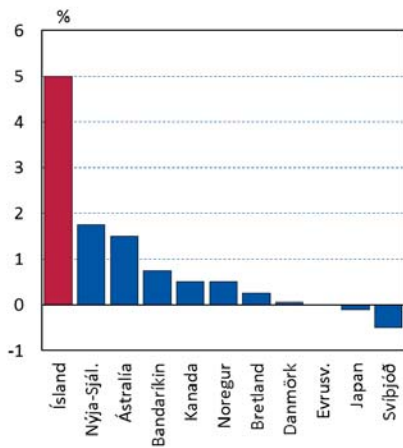


1. Hlutfallslegt útflutningsverð er útflutningsverð Íslands í hlutfalli við útflutningsverð helstu viðskiptalanda (fært í sama gjaldmiðli með vísitölu meðalgengis). 2. Undirliggjandi viðskiptajöfnuður fyrir árin 2008-2015. 3. Undirliggjandi erlend staða fyrir Ísland 2008-2014. Alþjóðleg gögn um erlenda stöðu úr gagnagrunni Lane og Milesi-Ferretti fyrir tímabilið 2000-2011 en gögn þeirra eru framflengt til ársins 2015 miðað við þróun skv. IFS-gagnagrunni Alþjóðgjaldeyrissjóðsins (sjá rammagrein 4 í PM 2016/2). Skyggt svæði sýnir grunnspá PM 2017/1 fyrir 2017-2019. Heimildir: Alþjóðgjaldeyrissjóðurinn, Hagstofa Íslands, Lane og Milesi-Ferretti (2007), Macrobond, Seðlabanki Íslands.

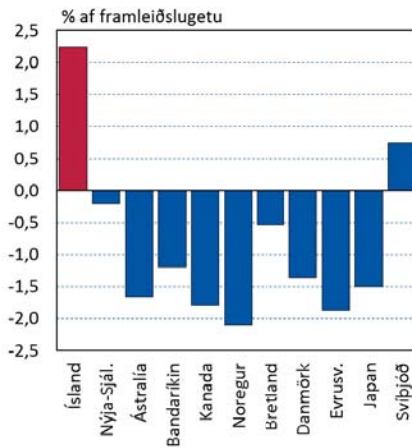
Hvað með peningastefnuna?

- Afar takmarkað hvað peningastefnan getur gert við kerfisbreytingu á samsetningu útflutnings og hækkun jafnvægisgengis – hennar verkefni er að tryggja verðstöðugleika sem hefur tekist undanfarin ár ... þrátt fyrir mikla spennu í þjóðarbúskapnum
- Allt aðrar aðstæður en í nágrannaríkjunum þar sem enn er mikill slaki og verðbólguvæntingar hafa leitað undir markmið

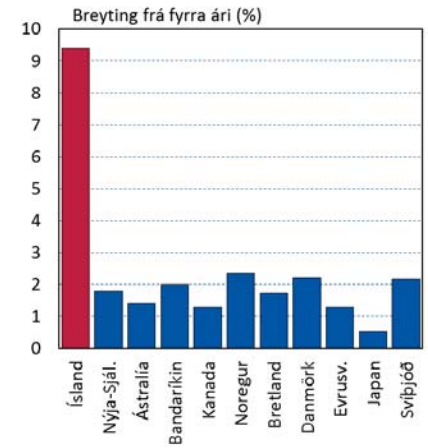
Meginvextir seðlabanka nokkurra þróaðra ríkja¹



Framleiðsluspenna í nokkrum þróuðum ríkjum 2016²



Launahækkunir í nokkrum þróuðum ríkjum 2016³

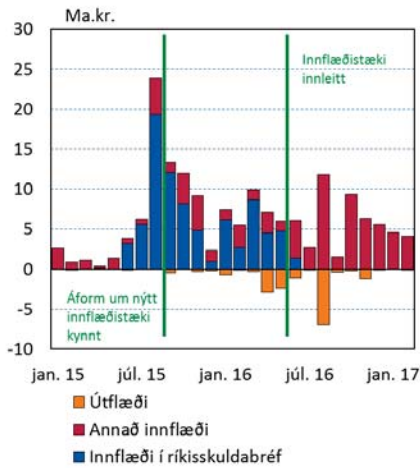


1. Nýjstu gildi meginvaxta nokkurra seðlabanka. 2. Mat á framleiðsluspennu 2016 frá OECD (*Global Economic Outlook*, nóvember 2016) fyrir öll lönd fyrir utan Ísland (*Peningamála* 2017/1), Japan (Alþjóðgjaldeyrissjóðurinn, *World Economic Outlook*, október 2016) og Nýja-Sjáláland (*Monetary Policy Statement*, nóvember 2016). 3. Nafnlaunahækkunir 2016 frá OECD (*Global Economic Outlook*, nóvember 2016) fyrir öll lönd fyrir utan Ísland og Nýja-Sjáláland (*Monetary Policy Statement*, nóvember 2016). Heimildir: Alþjóðgjaldeyrissjóðurinn, Hagstofa Íslands, OECD, Seðlabanki Nýja-Sjálálands, Seðlabanki Íslands.

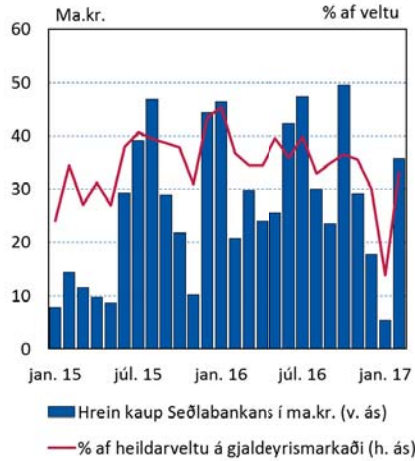
Hvað með peningastefnuna? (frh.)

- Ekki merki um að óstöðugt fjármagnsinnflæði í formi vaxtamunaviðskipta hafi þrýst upp gengi krónunnar
- Seðlabankinn hefur þar að auki lagt gegn gengishækkun með verulegum gjaldeyriskaupum
- Og bara að lokum: raungengi getur líka hækkað mikið án þess að það tengist innlendri peningastefnu – sbr. reynsla frá 2001-07

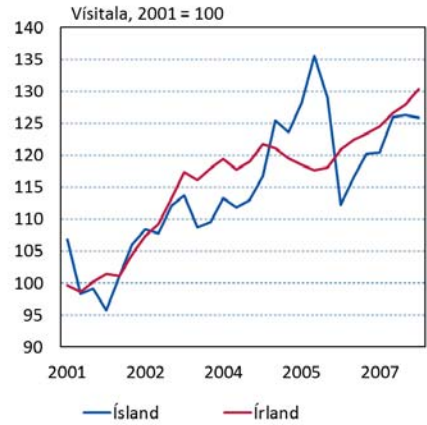
Fjármagnsflæði vegna nýfjárfestinga¹
Janúar 2015 - febrúar 2017



Gjaldeyriskaup Seðlabankans
Janúar 2015 - febrúar 2017



Raungengisþróun á Íslandi og Írlandi
1. ársfj. 2001 - 4. ársfj. 2007



1. Fjármagnsflæði vegna skráðra nýfjárfestinga.
Heimildir: Alþjóðagreiðslubankinn í Basel, Seðlabanki Íslands.



March 27, 2001

Declaration on inflation target and a change in the exchange rate policy

(From March 27, 2001 – as amended by agreement between the Prime Minister of Iceland and the Board of Governors of the Central Bank of Iceland on November 11, 2005, cf. Press release no. 35/2005)

On March 27, 2001 the Prime Minister and the Governors of the Central Bank of Iceland signed a declaration on changes in the framework of monetary policy in Iceland. The declaration is as follows:

The Government of Iceland and the Central Bank of Iceland have decided the following changes in the framework of monetary policy in Iceland, effective March 28, 2001:

- (1) The main target of monetary policy will be price stability as defined below. The Central Bank shall also promote financial stability and the main objectives of the economic policy of the Government as long as it does not deem it inconsistent with the Bank's main objective of price stability.
- (2) Rather than basing monetary policy on keeping the exchange rate within a fluctuation band, the Central Bank will aim at keeping inflation within defined limits as specified below.
- (3) The change described above implies that the fluctuation limits for the króna are abolished. Nevertheless, the exchange rate will continue to be an important indicator in the conduct of monetary policy.
- (4) The Government grants full authority to the Central Bank to use its instruments in order to attain the inflation target.
- (5) Later this week, the Government will submit to Parliament a bill on a new Central Bank Act which, once enacted, will legally confirm the decisions described above on making price stability the main objective of monetary policy and on the independence of the Central Bank to use its instruments.
- (6) The inflation target of the Central Bank will be based on 12-month changes in the consumer price index as calculated by Statistics Iceland. Statistics Iceland will also be asked to calculate one or more indices which may be used to assess the underlying rate of inflation, as will be further agreed between the Central Bank and Statistics Iceland. The Central Bank will take note of such indices in its assessment of inflation and in the implementation of monetary policy.

(7) The Central Bank will aim at an annual inflation rate of about 2½ per cent.

(8) If inflation deviates by more than 1½ percentage point from the target, the Central Bank

shall bring it inside that range as quickly as possible. In such circumstances, the Bank will be obliged to submit a report to the Government explaining the reasons for the deviations from the target, how the Bank intends to react and how long it will take to reach the inflation target again in the Bank's assessment. The report of the Bank shall be made public.

(9) The Central Bank shall aim at attaining the inflation target of 2½ percent not later than by the end of 2003. In the year 2001, the upper Declaration on inflation target and a change in the exchange rate policy limit for inflation shall be 3½ percentage points above the inflation target but 2 percentage points above it in the year 2002. The lower limit for inflation will always be 1½ percentage point below the inflation target. Should inflation move outside the target range in 2001 and 2002, the Bank shall respond as set out in item 8 above.

(10) Despite the elimination of the fluctuation limits for the króna, the Central Bank will intervene in the foreign exchange market if it deems such action necessary in order to promote the inflation objective described above or if it thinks that exchange rate fluctuations might undermine financial stability.

(11) The Central Bank shall publish inflation forecasts, projecting inflation at least two years into the future. Forecasts shall be published in the Bank's Monetary Bulletin. This shall also contain the Bank's assessment of the main uncertainties pertaining to the inflation forecast. The Bank shall also publish its assessment of the current economic situation and outlook.

[Amended text by agreement between the Prime Minister of Iceland and the Board of Governors of the Central Bank of Iceland on November 11, 2005]

(12) The Central Bank shall in its publications explain how successful it is in implementing the inflation target policy. The Governors will also report to the Minister, the Government and committees of the Parliament on the policy of the Bank and its assessment of current economic trends and prospects.