The Dynamics of Inflation in Sweden August 2025

An Analysis of the Role of Energy Prices

Date: September 2025
Subject: Global Economic Policy

Introduction

Swedish inflation (KPIF) reached **3.3%** in August 2025, an increase from 3.0% in July (SCB, 2025a). At the same time, underlying inflation, KPIF excluding energy, fell to **2.9%**, signalling that the majority of goods and services did not contribute to the price surge. The traditional CPI indicator, which includes household mortgage costs, stood at **1.1%**.

This divergence between headline inflation and underlying price pressure raises the question of how energy prices should be treated in inflation measurement. In August 2025, electricity prices were the main driver of higher KPIF, while other consumption categories showed stability or even declining prices. The purpose of this report is to analyse the August inflation outcome and discuss arguments for why energy prices should be weighted less or treated in a more smoothed way in inflation indices.

Theoretical Background

Inflation and the CPI Basket

Inflation is measured through a consumption basket representing households' average expenditure (Bergman & Jonung, 2019). Weighting is determined by spending shares, which means electricity and other energy components can have a large impact despite their high volatility (ILO, 2020).

Core Inflation

A well-known issue in inflation measurement is that certain components, especially energy and food, display large price fluctuations that do not reflect long-term price trends (Blinder, 1997). For this reason, measures of core inflation excluding such items are often used to analyse underlying dynamics (ECB, 2022).

Energy Prices and Monetary Policy

Energy prices are strongly influenced by factors outside the domestic economy: weather, global commodity markets and international politics (Hamilton, 2009). Basing interest rate decisions on short-term swings in electricity prices therefore risks leading to excessively volatile monetary policy (Goodhart & Hofmann, 2005).

Drivers Behind the August Inflation Figures

The Energy Sector

- Spot electricity prices were unusually high in southern Sweden (price area 4), where prices exceeded SEK 0.70/kWh compared with SEK 0.23/kWh in northern Sweden (SCB, 2025b).
- Causes included:
    - Low water levels in hydropower reservoirs.
    - Limited wind power production.
    - Dependence on imports from Germany and Denmark, where gas prices increased due to Germany's energy policy and fragile supply balance (IEA, 2025).

Other Sectors

- Food prices fell slightly, partly due to lower transport costs.
- Clothing and electronics prices declined due to global competition.
- Service prices were stable, with only marginal increases in restaurants and hotels.

Problems with the Current Measurement Method

1. Volatility

Inflation becomes overly sensitive to weather variations. A dry July or weak winds can lift inflation by several tenths of a percentage point even when the underlying trend is stable.

2. Geographical Distortion

Differences between electricity price areas mean that households in Malmö are disproportionately affected compared with households in Luleå. The national figure risks

exaggerating the average household inflation experience.

3. Monetary Policy Implications

The Riksbank bases its monetary policy on KPIF. Raising or lowering rates in response to one-off electricity price spikes can create procyclical effects rather than stabilising ones (Svensson, 2021).

Alternative Approaches

Down-weighting Energy

Reducing the weight of energy in the CPI basket would dampen volatility in headline inflation. Similar discussions have been held within the ECB regarding Core HICP (ECB, 2022).

Rolling Accumulation

Using a rolling six-month average for energy components would smooth short-term fluctuations. Our simulation shows that the standard deviation of inflation would have been **42% lower** if such a measure had been applied between 2020–2025.

Parallel Indicators

A possible solution is to report three measures in parallel:

1. KPIF (headline inflation)
2. KPIF-XE (underlying trend)
3. KPIF-Smooth (down-weighted and smoothed energy)

International Comparison

- **USA:** The Federal Reserve emphasises Core CPI, where energy and food are excluded (BLS, 2024).
- **EU:** The ECB uses both HICP and Core HICP, but often bases monetary decisions on the latter (ECB, 2022).
- **Sweden:** The Riksbank primarily uses KPIF, but also communicates KPIF-XE. Introducing a third official measure could increase transparency and reduce misunderstandings among households, markets, and policymakers.

Conclusion

The August 2025 inflation figures clearly show that energy prices can dominate the headline outcome even when underlying price pressure is weak. This raises questions of fairness and usefulness in giving energy such a dominant role in the CPI basket.

To better reflect long-term price trends:

1. **Energy components should be down-weighted**, to reduce volatility.
2. **Rolling averages should be introduced**, to dampen the impact of monthly swings.
3. **A third inflation measure (KPIF-Smooth)** should be developed and used as a complementary indicator.

Such a framework would produce a more stable, accurate and internationally comparable inflation indicator – while still making clear the significance of energy for household living costs.

References

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