NORWAY

The economy is projected to strengthen gradually thanks to stronger growth of private consumption and both petroleum and non-oil investment. Employment growth will pick up and increasing activity will lift consumer price inflation from its current low level.

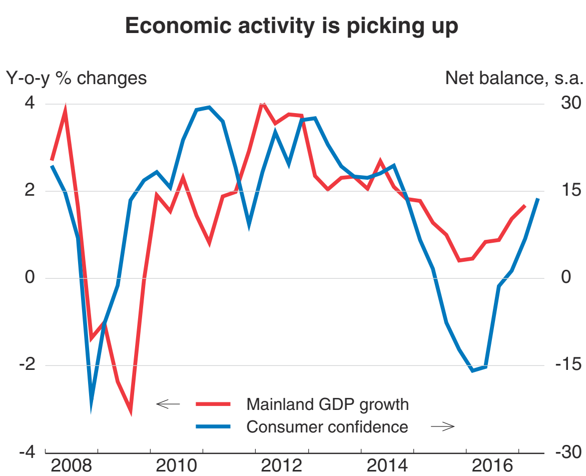
Despite low oil prices, growth has remained positive thanks to accommodative monetary and fiscal policies. The adjusted fiscal rule – budgets should aim for structural deficits at 3% of the value of the oil fund – appropriately implies a broadly neutral fiscal stance going forward. Improving the business environment, stronger competition, and better skills and education are key for raising growth potential and maintaining inclusiveness.

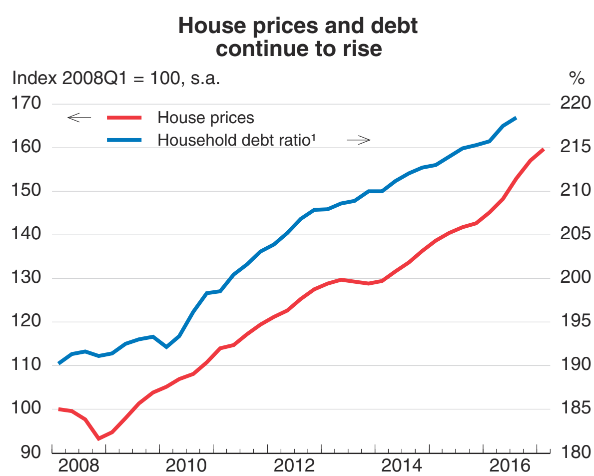
Norway has successfully sustained an egalitarian social and economic model, especially for women and vulnerable families. Comprehensive social programmes have protected Norwegians from the adverse effects of globalisation. However, the model involves substantial public spending and consequently high tax rates, which are a challenge for competitiveness and trade in the global economy. However, Norway has substantial scope for delivering its comprehensive public services and infrastructure investments for less cost, providing room to lower taxes.

Economic activity continues to strengthen

Norway's mainland output growth (that is, abstracting from oil and gas production) has been gradually increasing since early 2016 thanks to supportive macroeconomic policies, less drag from declining petroleum investment, the notch-up in global oil prices, recovering consumer confidence and the comparatively low value of the Norwegian Krone. Consumer price inflation is heading back towards the 2½ per cent target following an uptick due to currency depreciation. However, employment growth has yet to pick up and the rate of unemployment is high by Norwegian standards. Ongoing strong momentum in

Norway





1. Ratio to disposable income.

Source: OECD Economic Outlook 101 database; Thomson Reuters; and Norges Bank.

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Norway: **Demand, output and prices**

	2013	2014	2015	2016	2017	2018
	Current prices NOK billion	Percentage changes, volume (2014 prices)				
GDP at market prices	3 071.1	1.9	1.6	1.1	1.3	1.5
Private consumption	1 232.9	1.9	2.1	1.6	2.0	2.2
Government consumption	652.3	2.7	2.1	2.3	2.1	1.6
Gross fixed capital formation	717.1	-0.7	-3.8	0.3	2.3	2.2
Final domestic demand	2 602.4	1.4	0.5	1.4	2.1	2.1
Stockbuilding[1]	140.6	0.2	0.2	0.3	-0.2	0.0
Total domestic demand	2 742.9	1.6	0.7	1.8	1.7	2.0
Exports of goods and services	1 203.7	3.1	3.7	-0.5	1.4	1.2
Imports of goods and services	875.5	2.4	1.6	0.8	2.9	2.6
Net exports[1]	328.2	0.5	1.0	-0.4	-0.5	-0.4
Memorandum items						
Mainland GDP at market prices[2]	_	2.2	1.1	0.9	1.7	2.1
GDP deflator	_	0.3	-2.3	-1.2	4.9	1.6
Consumer price index	_	2.0	2.2	3.5	1.9	1.8
Private consumption deflator	_	2.2	2.3	3.3	1.8	1.8
Unemployment rate	_	3.5	4.3	4.7	4.4	4.2
Household saving ratio, net[3]	_	8.2	10.4	7.1	6.1	5.8
General government financial balance[4]	_	8.8	6.0	3.1	4.1	4.5
General government gross debt[4]	_	33.4	39.2	42.7	55.5	59.4
General government net debt[4]	_	-249.4	-284.4	-289.0	-276.1	-272.3
Current account balance[4]	_	12.1	8.7	4.9	8.5	8.8

1. Contributions to changes in real GDP, actual amount in the first column.
2. GDP excluding oil and shipping.
3. As a percentage of disposable income.
4. As a percentage of GDP.

Source: OECD Economic Outlook 101 database.

StatLink http://dx.doi.org/10.1787/888933506037

house price growth (particularly in Oslo) and household borrowing is supporting consumption and construction activity, but has led to increasing concern about debt levels and housing market stability.

Monetary policy looks set to remain supportive. Norges Bank has maintained the policy rate at 0.5% since early 2016 and has been signalling continuation of a low-interest environment through its policy-rate forecasts. However, house prices and household debt have been rising rapidly for some time, fuelled at least in part by persistently low interest rates. The authorities introduced new macro-prudential rules on housing credit in January and are adjusting safety margins via the counter-cyclical buffer mechanism.

The fiscal rule has been altered

Fiscal policy has for many years been guided by a fiscal rule stipulating that the structural deficit over time should be equal to the expected real rate of return on the oil fund (the Government Pension Fund Global). The expected real return was reduced from 4% to 3% in March 2017. At the moment, the rule implies a broadly neutral fiscal stance in coming years, as the structural deficit is close to the new limit and the Fund is expected to grow in line with mainland GDP. A neutral stance is broadly appropriate given the macroeconomic outlook. As before, the rule allows for deviations in the event of extraordinary circumstances, and there is ample fiscal room to use this flexibility in the unlikely event of a sharp fall in output growth.

Welcome initiatives are underway that will help businesses better tap into globalisation. Cuts in the corporate tax rate and red tape continue, as do measures to improve skills and education. However, there remains substantial opportunity for more effective public spending (and consequently a reduced tax burden). The ongoing surge in public infrastructure investment has brought to the fore issues in project selection and there are longstanding issues of spending efficiency in other areas.

Activity is projected to strengthen further

Mainland output growth is projected to gain strength and reach just over 2% in 2018. Oil-related investment will become positive and be accompanied by growing non-oil investment and household consumption. Employment growth is expected to turn up, putting the rate of unemployment on a downward trend. Consumer price inflation will fall further in the near term as currency-depreciation effects wane, but then gradually increase as spare capacity diminishes.

Uncertainty about the global oil price, as always, remains a key source of upside and downside risks. Risks for non-oil export demand remain heightened by political and economic uncertainty elsewhere, particularly regarding the Brexit process. Domestically, the housing market and related credit concerns are a key risk. A market downturn could significantly dent consumption demand as wealth effects go into reverse.