NORWAY

Mainland output growth will remain robust in the first half of 2018, boosted by the increase in the global oil price but held back by a slowdown in housing construction. Output growth will then moderate. The unemployment rate will decrease further, while price and wage inflation will rise.

The switch from an expansionary to a neutral fiscal stance as implied by the adjusted fiscal rule is appropriate given the economy's cyclical position. Achieving the switch will bolster policy credibility. The central bank has signalled that it will increase the policy rate in autumn this year, which is appropriate. Structural reforms should remain focused on improving the business environment, including lighter taxation financed by greater public-spending efficiency.

The pick-up in activity continues, except for housing

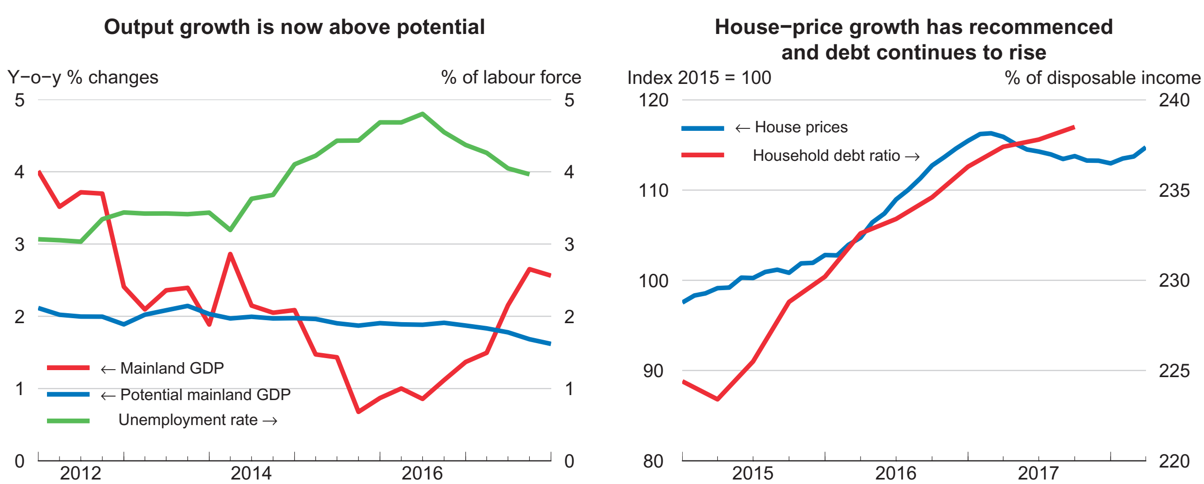
Mainland output growth (that is, growth abstracting from oil and gas production) continues to gather momentum. Monetary and fiscal policy support and currency depreciation have been bolstering demand. Also, the oil-price pick-up has encouraged resource-related activity. Employment growth is increasing and the unemployment rate continues to decline. Consumer-price inflation remains low and the negotiated benchmark wage increase for 2018 is moderate, at 2.8%.

A house-price correction began in early 2017 and construction activity has started shrinking. Past macro-prudential measures curtailing housing credit growth, and adjustment of banks' safety margins via the counter-cyclical capital buffer, assisted the housing-market cooldown. Recent data, however, show a country-wide resurgence in prices, suggesting that the price correction may be over.

Fiscal and monetary support is set to lessen

Finalisation of the government budget for 2018 saw welcome retention of a move towards a neutral stance, reflecting improved economic growth and the adjustment to the

Norway



Source: OECD Economic Outlook 103 database; Statistics Norway; and Real Estate Norway (Eiendom Norge).

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Norway: **Demand, output and prices**

	2014	2015	2016	2017	2018	2019
	Current prices NOK billion	Percentage changes, volume (2015 prices)				
Mainland GDP at market prices[1]	2 539.6	1.4	1.0	1.9	2.5	2.1
Total GDP at market prices	3 146.7	2.0	1.1	1.9	1.8	1.6
Private consumption	1 288.4	2.6	1.5	2.5	2.3	2.0
Government consumption	692.0	2.4	2.1	2.2	2.1	2.0
Gross fixed capital formation	749.5	-4.0	-0.2	4.9	-0.8	3.2
Final domestic demand	2 729.8	0.7	1.2	3.0	1.5	2.3
Stockbuilding[2]	133.7	0.0	1.4	-0.3	1.1	0.0
Total domestic demand	2 863.5	0.7	2.7	2.5	2.5	2.2
Exports of goods and services	1 220.4	4.7	-1.8	1.1	-0.1	1.4
Imports of goods and services	937.2	1.6	2.3	2.8	2.0	3.0
Net exports[2]	283.2	1.3	-1.4	-0.6	-0.7	-0.5
Memorandum items						
GDP deflator	_	-2.8	-1.1	3.8	3.2	2.1
Consumer price index	_	2.1	3.6	1.9	1.9	1.9
Core inflation index[3]	_	2.6	3.3	1.7	0.9	2.0
Unemployment rate (% of labour force)	_	4.3	4.7	4.2	3.7	3.6
Household saving ratio, net (% of disposable income)	_	10.3	7.1	7.3	8.0	8.3
General government financial balance (% of GDP)	_	6.1	4.0	4.4	4.9	5.1
General government gross debt (% of GDP)	_	38.9	42.8	42.4	50.9	52.1
Current account balance (% of GDP)	_	8.0	4.9	5.1	5.9	5.7

1. GDP excluding oil and shipping.
2. Contributions to changes in real GDP, actual amount in the first column.
3. Consumer price index excluding food and energy.

Source: OECD Economic Outlook 103 database.

StatLink http://dx.doi.org/10.1787/888933731358

fiscal rule – that the structural deficit over time should equal 3% (previously 4%) of the value of the oil fund (the Government Pension Fund Global). In March, Norges Bank's inflation target was reduced from 2.5% to 2%, on the basis that this aligns better with targets elsewhere. The Bank's policy-rate forecasts have been signalling a start to policy tightening, projecting an increase from the current rate of 0.5% in autumn this year.

The switch to a more neutral fiscal stance increases the importance of improving value-for-money in public spending while retaining the comprehensive welfare support and public services that are integral to Norway's socio-economic model. A recent OECD assessment points to cost-efficiency issues in transportation infrastructure, for instance. Greater public-spending efficiency can also help accommodate tax reform, such as the proposed reduction from 24% to 23% in the “ordinary” rate of taxthat applies to both household and business incomes.

Norway's high-cost, high-tax economy means business competitiveness relies on strong attributes in other dimensions of the business environment. In this regard, the priority given to strengthening the education system and reducing red-tape exemplify good policy direction. Agreement to reduce early-retirement bias in the public sector will help to reduce the drain on the skills pool. Similarly, renegotiation of the tripartite "inclusiveness agreement" this year provides an opportunity to better contain early retirement via sick-leave and disability-benefit systems.

Strong output growth will continue

Mainland output will follow a similar trajectory to most other Nordic economies, with 2.5% growth projected for 2018. Growth will moderate somewhat in 2019 as capacity constraints begin to bite. Oil-related investment will return to growth, accompanied by expanding non-oil investment and robust household consumption growth. Employment growth will gather strength, lowering the unemployment rate further. Consumer price inflation and wage growth will gradually increase as spare capacity diminishes. A critical uncertainty is whether the recent housing market adjustment will prove sufficient to avoid a larger correction in the future that brings substantial consequences for the economy. Global oil price developments pose both upside and downside risks to the economy.