2 Economic outlook

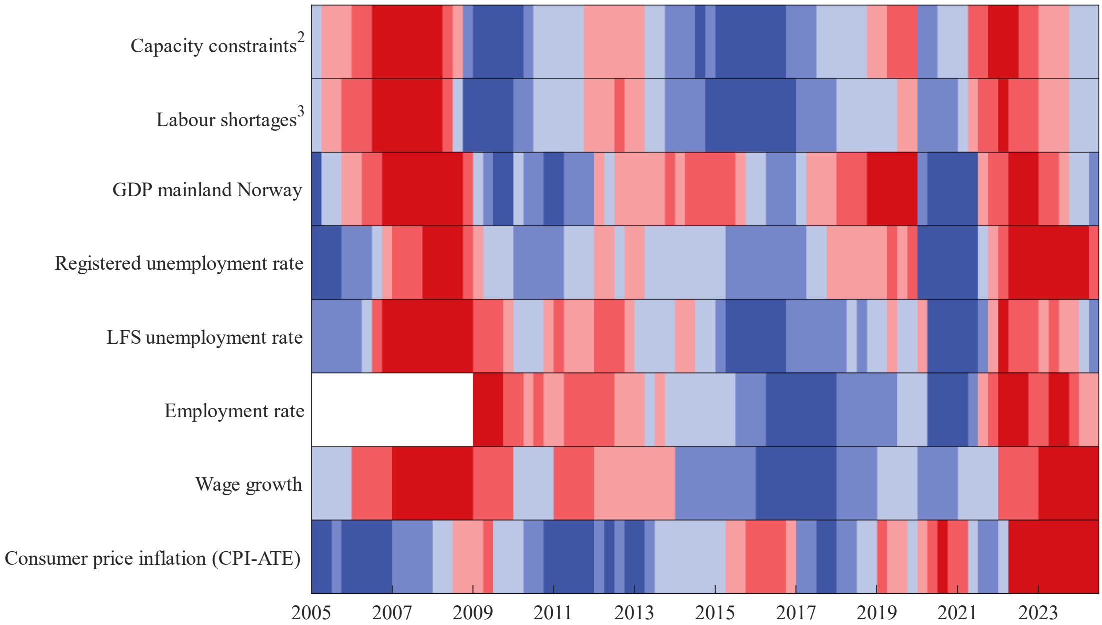
2.1 The Norwegian economy

Following two years of low growth in the Norwegian economy, there are prospects for higher growth next year and continued low unemployment. So far, economic policy appears to have succeeded in allowing inflation to come down without a significant increase in unemployment. Norway has avoided an economic downturn. Norwegian krone depreciation and high wage growth mean that it may nonetheless take some time for inflation to return to target. At the same time, the prospect of wage growth significantly outstripping inflation this year suggests a rebound in household purchasing power. This is expected to boost growth in the Norwegian economy next year. GDP for mainland Norway (non-oil GDP) is projected to increase by 2.3 per cent in 2025, which is well above trend growth.

Stronger growth outlook

Growth as measured by GDP for mainland Norway, has been low for the last two years. This has led capacity utilisation in the economy to return to a more normal level, after being high in the aftermath of the pandemic. The share of businesses reporting capacity constraints and labour shortages in Norges Bank's regional network declined through last year, but there are indications of an upturn this year. The share is currently close to the historical average. There are considerable disparities between industries. The offshore supply industry reports high capacity utilisation and a strong growth outlook. In construction, capacity utilisation is lower than normal and the growth outlook is weak. Capacity utilisation is discussed in more detail in Box 2.1.

Business investment remains at a historically high level, but has declined somewhat over the past year. We project lower business investment and a continued decline in housing investment to dampen economic growth this year, while public sector demand and private sector consumption will have the opposite effect, see **Feil! Fant ikke referansekilden.**. Growth in mainland GDP is projected to pick up in 2025 and 2026, primarily as a result of lower inflation, continued high wage growth and eventually also lower interest rates leading to higher growth in private consumption. Moreover, higher income growth and lower interest rates are expected to boost housing investment from its very low level in 2024. Registered unemployment is projected to remain low, see Figure 2.4.



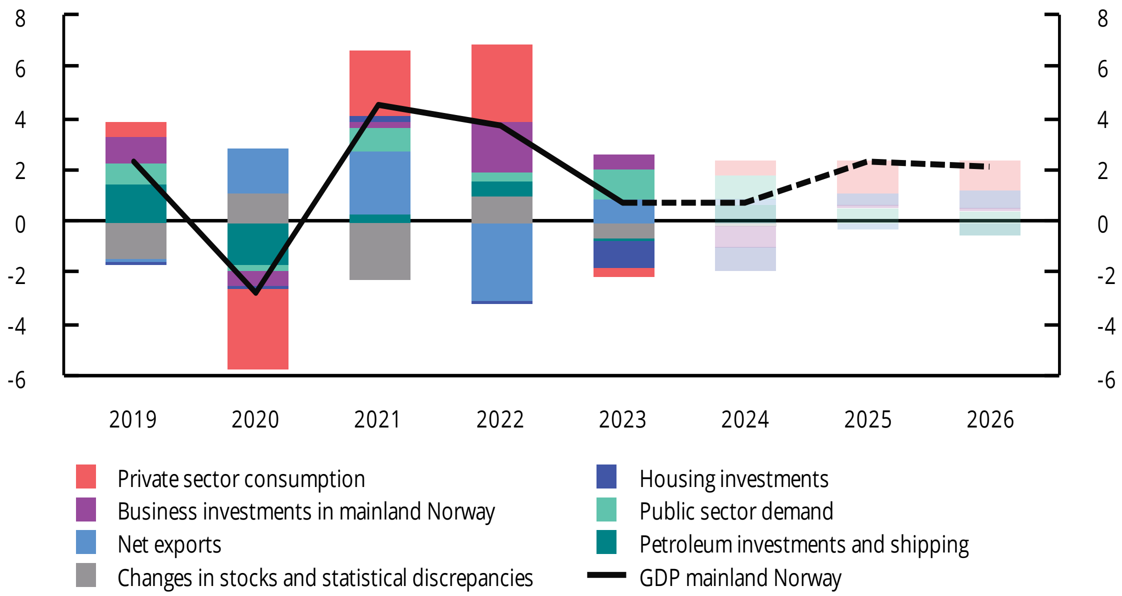
Figur 2.1 Selected indicators of capacity utilisation in the Norwegian economy[1]. Q1 2005 – Q2 2024

[1] Shades of red indicate that the economy is running above full capacity, while shades of blue indicate recession and spare capacity. The colour scale reflects how large the gap, or deviation from the average, is. The darkest colours represent the third of the observations with the largest positive and negative deviation. The indicators are measured as the deviation from the average for the period 2005-2023, with observations from the pandemic years 2020 and 2021 removed from the time series. The exceptions are inflation, which is measured as a deviation from the inflation target, and GDP, which is measured as a deviation from a simple trend, without adjustment for the abnormally low activity development during the pandemic. The trend is estimated using the Hodrick-Prescott filter, where the smoothing parameter is set at 6,400, which corresponds to 400 on an annual basis.

[2] Capacity constraints refer to the share of the contact businesses in Norges Bank's regional network that will have either some or significant problems in increasing production/sales without investing additional resources.

[3] Labour shortages refer to the share of the contact businesses in Norges Bank's regional network reporting that labour shortages are curtailing production/sales.

Sources: Norges Bank, Statistics Norway, Norwegian Labour and Welfare Administration and the Ministry of Finance.



Figur 2.2 Development in mainland Norway by demand component[1]. 2019-2026

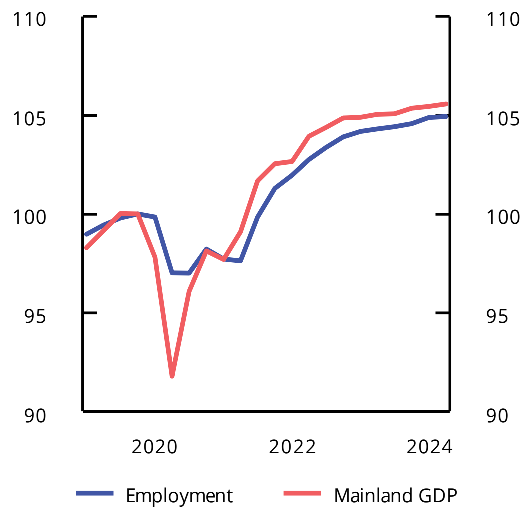
[1] Petroleum investments and shipping refer to demand impulsesfrom these industries to mainland Norway (the non-oil economy).

We expect unemployment to remain low and employment to remain high

Labour demand remains high, although the labour market is slightly less tight than a year ago. Employment increased significantly in Q1 2024, but has been fairly stable in Q2. Vacancies still remain far higher than in the pre-pandemic years, although the number has declined from the historically high levels of last year.

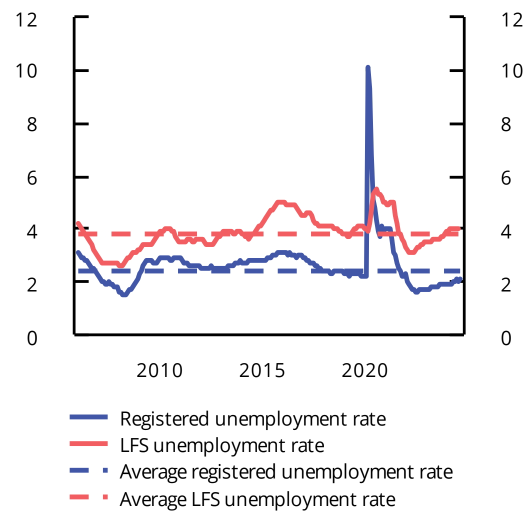
Registered fully unemployed represented 2.1 per cent of the labour force at the end of September. Registered unemployment has increased slightly since the beginning of the year, but is still lower than before the pandemic and well below its 20 years average, see Figure 2.4. Ukrainians account for 40 per cent of the increase in registered unemployment over the past year. Unemployment as measured by the Labour Force Survey (LFS), which also includes jobseekers other than those who register with the Norwegian Labour and Welfare Administration offices (Nav), has also increased. Much of the increase in this unemployment measure over the past two years is due to more students and pupils reporting that they are actively seeking work. LFS-unemployment is now close to its 20 years average.

Employment is projected to continue to increase in the second half of this year and next year. Registered unemployment is also expected to rise slightly during the autumn, partly because more Ukrainians are completing the introduction programme and registering with Nav. However, the significant decline in the number of arrivals since last autumn would indicate that much of the increase in unemployment stemming from displaced Ukrainians has already occurred. Registered unemployment is expected to stabilise at a low level over the next two years.



Figur 2.3 GDP for mainland Norway and employment. Index. Q4 2019=100. Seasonally adjusted. Q1 2019-Q2 2024

Source: Statistics Norway.



Figur 2.4 Unemployment as a percentage of the labour force. Seasonally and trend-adjusted. Jan. 2006-
Sep. 2024

[1] Unemployment figures for 2020 and 2021 have been excluded from the average because the labour market was heavily affected by lockdowns due to infection control measures in these years.

Sources: Norwegian Labour and Welfare Administration and the Ministry of Finance.

The Norwegian krone has depreciated

The Norwegian krone depreciated significantly in the first half of 2023 and has since then fluctuated around a weaker level than previously, see Figure 2.5. The variation over the past year is comparable with previous periods.

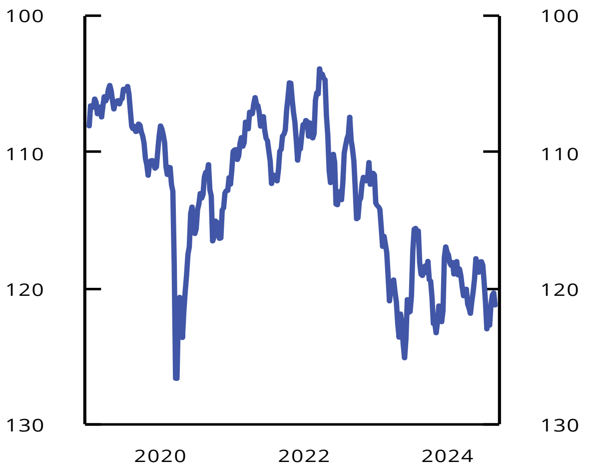
It is difficult to quantify the drivers behind exchange rate fluctuations. A smaller increase in interest rates in Norway than abroad, lower petroleum prices and somewhat weaker productivity growth in Norway than in other countries have been mentioned by market participants and academic scholars as reasons for the Norwegian krone depreciation in recent years. Empirical analyses point to the interest rate differential in relation to other countries, the degree of financial market uncertainty and the oil price as key factors. Events such as the pandemic, wars, high inflation and higher interest rates influence risk appetite. During periods of market turbulence, it is common for investors to move into major currencies, while smaller currencies such as Norwegian krone, the Swedish krone or the New Zealand dollar depreciate.

For businesses exposed to international competition, whether for domestic or international customers, the krone depreciation serves to strengthen competitiveness and improve profitability. For businesses that incur costs in foreign currency and earn their income in Norwegian kroner, Norwegian krone depreciation will weaken profitability. Companies that are exposed to exchange rate risk can hedge their positions by entering into fixed-price contracts for currency. Norwegian krone depreciation also serves to increase inflation. This happens directly, by making imported goods more expensive, but also indirectly, by raising the prices of imported intermediate goods. This causes cost increases that businesses are likely to partially pass on to households. Norwegian kroner exchange rate developments will have a major impact on the Norwegian economy in the time to come. This report makes the technical assumption that the krone exchange rate will remain unchanged going forward. This entails that it will depreciate by 1.3 per cent fra 2023 to 2024, but remain stable in 2025 and 2026.

Inflation is declining

Consumer price inflation has come down from the high levels of 2022 and 2023, while underlying inflation is still well above the inflation target. In August, year-on-year growth in the consumer price index (CPI) was 2.6 per cent. Underlying inflation, measured by the CPI adjusted for tax changes and excluding energy products (CPI-ATE), was 3.2 per cent, see Figure 2.6.

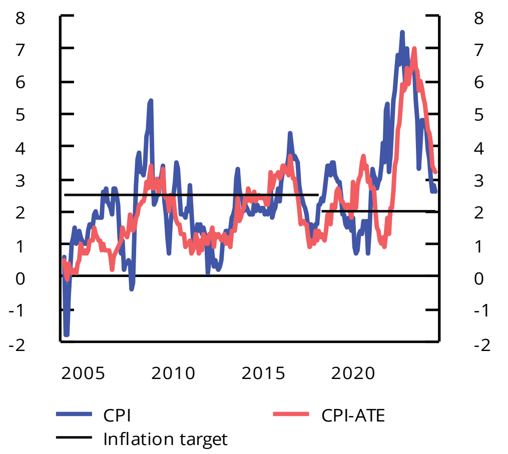
Consumer price inflation has declined more than expected so far this year, partly because electricity prices have come down significantly. The electricity futures market suggests that electricity prices will increase through the winter. Moreover, the Norwegian krone depreciation this summer may lead to higher price growth for imported goods in the time to come. Increased prices for electricity and imported goods may serve to delay a further decline in consumer price inflation. The prospect of high wage growth both this year and next year is also likely to keep inflation up. CPI growth is projected at 3.7 per cent this year and 3.0 per cent next year. CPI-ATE growth is projected at 4.1 per cent this year and 3.2 per cent next year, see Table 2.1.



Figur 2.5 Import-weighted exchange rate index (I-44)[1]. 1995=100. Week 1 2019-week 36 2024

[1] I-44 is a calculated exchange rate index based on exchange rates between NOK and the currencies of Norway's 44 most important trading partners measured by import value. A higher index value means Norwegian kroner depreciation, and the axes are therefore been inverted.

Source: Norges Bank.



Figur 2.6 Year-on-year growth in the consumer price index (CPI)and the consumer price index adjusted for tax changes and excluding energy products (CPI-ATE).
Jan. 2005-Aug. 2024

Source: Statistics Norway.

Tabell 2.1 Key figures for the Norwegian economy. Percentage change from previous year, unless otherwise stated.

	NOK billion[1]				
	2023	2023	2024	2025	2026
Private sector consumption	1,922.9	-0.8	1.2	2.6	2.5
Public sector consumption[2]	1,121.9	3.4	2.2	2.1	1.2
Gross fixed capital formation	1,196.5	0.0	-2.8	1.9	1.8
Of which: Petroleum extraction and pipeline transportation	216.1	10.6	11.0	-1.0	-7.0
Businesses in mainland Norway	499.3	4.0	-6.2	0.9	0.8
Housing	207.7	-15.6	-17.0	12.1	13.7
Public administration	262.0	3.0	3.9	-0.3	2.3
Mainland Norway demand[3]	4,013.8	0.3	-0.2	2.5	2.4
Public sector demand[2]	1,383.8	3.3	2.5	1.6	1.4
Exports	2,419.6	1.4	2.7	2.5	1.0
Of which: Crude oil and natural gas	1,194.1	-1.1	2.7	1.5	-2.3
Goods and services from mainland Norway	1,045.9	6.4	1.4	3.4	4.4
Imports	1,664.4	0.7	1.0	3.0	2.9
Gross domestic product	5,126.5	0.5	1.1	2.1	1.2
Of which: mainland Norway	3,855.4	0.7	0.7	2.3	2.1

Other key figures:				
Employment	1.3	0.5	0.7	0.6
Unemployment rate, registered (level)	1.8	2.0	2.2	2.2
Unemployment rate, LFS (level)	3.6	4.0	4.1	4.1
Annual wages	5.2	5.2	4.5	4.3
CPI	5.5	3.7	3.0	2.5
CPI-ATE	6.2	4.1	3.2	2.7
Crude oil price, USD per barrel (current prices)	82	83	79	75
Gas price, USD per MMBtu (current prices)	13.6	10.3	11.5	9.7
Three-month money market rate (level).	4.2	4.7	4.3	3.5
Import-weighted Norwegian krone exchange rate[4]	7.9	1.0	1.3	0.0

[1] Provisional national accounts figures for 2023 in current prices. Growth rates from this level are stated in volumes.

[2] For 2026, the public sector consumption and gross capital formation projections are based on demographic trends, as well as the long-term plan for the Norwegian Armed Forces published in spring 2024.

[3] Excluding inventory changes.

[4] A positive number indicates Norwegian kroner depreciation.

Sources: Statistics Norway, Norges Bank, Norwegian Labour and Welfare Administration, Reuters, ICE, Macrobond and the Ministry of Finance.

Prospects for real wage growth

Continued high wage growth combined with lower inflation offers the prospect of significant real wage growth both this year and next year after a decline in 2022 and 2023. The Norwegian wage bargaining model is based on the manufacturing industry negotiating first, with the outcome from these negotations serving as a norm for subsequent wage settlements. High commodity prices and a weaker currency have resulted in strong profitability in parts of the economy, and the labour share of income in manufacturing has declined. When considered in isolation, high profitability in manufacturing should provide a basis for wage growth to remain high in the time to come. However, the social partners usually place little emphasis on the effects on profitability of short-term exchange rate fluctuations. Wage growth has remained high thus far in 2024. Data from the wage reporting system show that average basic monthly wages increased by 5.4 per cent from Q2 2023 to Q2 2024, after growth of 6.1 per cent from Q1 2023 to Q1 2024. Basic monthly wages have also increased by 5 per cent or more in almost all industries over the past year. We project annual wage growth of 5.2 per cent this year, in line with the manufacturing income settlement. For next year, projected annual wage growth is 4.5 per cent.

Higher consumption growth going forward

High inflation and high interest rates have held back growth in private sector consumption over the past couple of years. Last year, consumption declined for the first time since the 1980s. Car purchases in particular after an increase towards the end of 2022. This development is likely related to the introduction of a new weight-based tax on electric cars that came into effect on 1 January 2023. Excluding car purchases, there was a slight increase in consumption from 2022 to 2023.

Consumption has proved relatively resilient to decreased household real disposable income. High savings during the pandemic have helped many households to maintain consumption despite inflation surpassing income growth.

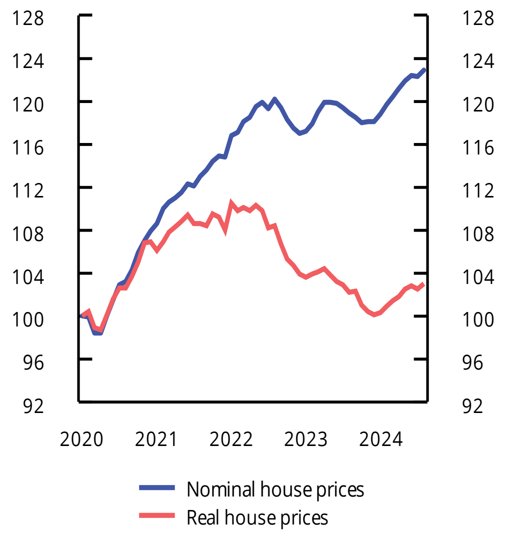
Significantly higher income growth this year and next year than in the preceding years will increase purchasing power and is expected both to boost consumption and provide scope for increased savings. In the first half of 2024, household consumption of goods and services increased by 0.6 per cent compared with the same period last year. Consumption is expected to growth further at a rate of 1.2 per cent this year and 2.6 per cent next year.

Housing investment will decline further this year

The housing market has been impacted by high interest rates and uncertainty for the past two years. Both sales of new homes and housing starts have slumped. Inflation adjusted figures show that the strong growth in prices of existing dwellings during the pandemic has been reversed, see Figure 2.7. Nonetheless, the impact of interest rate increases on the market for existing dwellings has been smaller than expected, with nominal house prices having increased markedly so far this year. In August, far more existing dwellings were both sold and put up for sale than normal. Sales of new dwellings have also picked up somewhat so far this year, but the level still remains very low. Housing starts are projected to remain low in 2024 and to increase sharply in 2025. The rebound in housing investment is now expected to come somewhat later than previously anticipated, in line with signals from businesses in Norges Bank's regional network. Repair and renovation of existing dwellings are expected to dampen the declinein housing investmentsomewhat.

Business investment expected to fall back somewhat

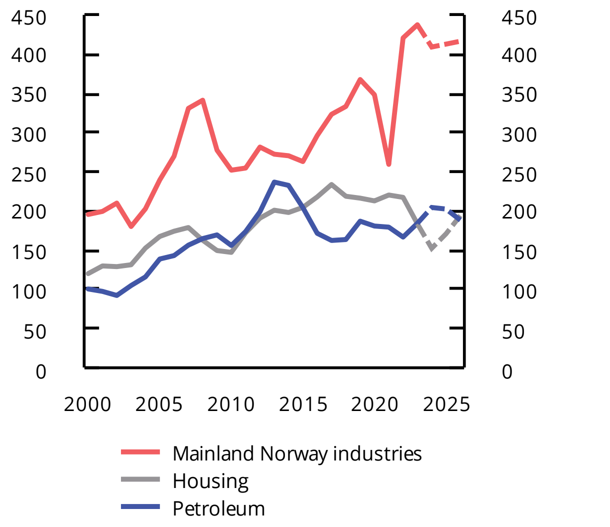
Mainland business investment was record high in 2023, while growth was particularly high in 2022, see Figure 2.8. Investment appears to be tapering off slightly this year, but this decline is far from offsetting the strong growth of the preceding two years. Investment in services and manufacturing are set to decline this year, while investment in power supply is expected to increase. A slight investment upturn is expected next year, fuelled by the climate and energy transition in manufacturing industry and power supply.



Figur 2.7 Prices of existing dwellings[1]. January 2020=100. Seasonally adjusted. Jan. 2020-Aug. 2024

[1] Real house prices are calculated by deflating Real Estate Norway's seasonally adjusted price series for existing dwellings with the seasonally adjusted consumer price index (CPI).

Sources: Real Estate Norway, Eiendomsverdi, Finn.no, Statistics Norway and the Ministry of Finance.



Figur 2.8 Gross fixed capital formation. Mainland businesses, housing and petroleum. NOK billion at 2020 prices. 2000-2023. Projections 2024-2026.

Sources: Statistics Norway, the Ministry of Energy, the Norwegian Offshore Directorate and the Ministry of Finance.

Demand from the petroleum sector has helped sustain growth over the past year. Petroleum investment increased sharply last year, after declining for three consecutive years. The increase should be viewed in the context of both high petroleum prices and the temporary tax rules for the petroleum sector that were introduced in spring 2020. The temporary tax rules contributed to a major increase in planned field developments, which will result in high investment growth also this year. Next year, investment is expected to taper off somewhat, but the level will still remain high.

Public sector demand

Total public sector demand for goods and services grew strongly last year compared with the last decade. One reason was that activity growth in the local government sector was higher than expected in the balanced budget.

Public sector consumption growth this year and next is projected to be close to the average for the last decade. The forecast for this year is unchanged from the revised national budget. Large defence investments will contribute to the high public sector investment growth this year and will also boost public investment next year. Overall, growth in public sector demand is estimated to be in line with the revised budget.

Public sector investment is nevertheless projected to be to decline somewhat next year. This is due to an anticipated decrease in investments in the health and care sector, which have been high in recent years. Overall, public demand for goods and services this year and next year is estimated to grow roughly in line with the historical average.For 2026, the public sector consumption and investment projections are based on demographic trends and the long-term plan for the Norwegian Armed Forces.

The outlook is uncertain

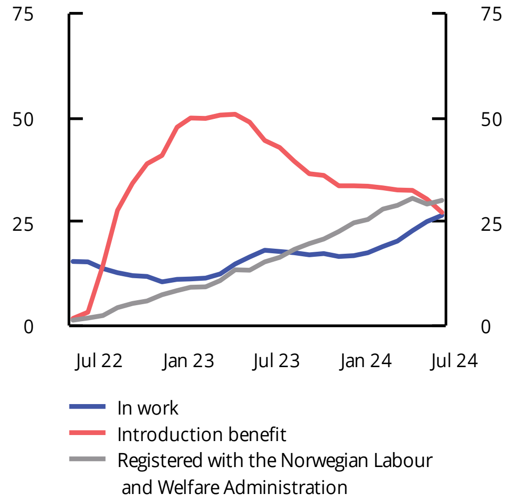
The Norwegian economy is approaching an inflection point where growth is expected to accelerate from a low level and eventually lead to increased capacity utilisation , with price growth continuing to decline towards the inflation target.. Risks to the outlook include factors that could cause the turning point to be brought forward or deferred. Continued Norwegian krone depreciation could be one such a factor. Unexpectedly high wage growth could be another. Both could contribute to prolonging the period of price growth above the target and cause interest rates to remain high for longer. This could delay the inflection point, which could have a particularly negative impact on the construction industry. There is also uncertain about how households might adapt to the prospect of a persistently higher interest rate level. Employment may grow faster than projected and cause higher income growth. This would enable households to increase consumption or housing investment more rapidly than projected. Geopolitical tensions provide significant uncertainty and could lead to supply side shocks, which would also affect the Norwegian economy.

Boks 2.1 The labour market situation for displaced Ukrainians and a comparison with Denmark

Since Russia invaded Ukraine in February 2022, more than 80,000 displaced people have been granted temporary collective protection in Norway. The resettlement of displaced Ukrainians has been rapid, and about 70,000 displaced Ukrainians had been resettled by August of this year. Of these, 45,000 were in the 20-66 age group[1]. Most people in this age group attend the introduction programme during the initial period after resettlement, and it therefore takes some time for them to enter employment and education. As illustrated in Figure 2.9, around half of those resettled received introduction benefits during the first half of last year. This share subsequently declined as more people completed the programme. In parallel with this, an increasing number of displaced Ukrainians have found work or registered with NAV. In August, 12,000 Ukrainians were in work, corresponding to 27 per cent of resettled displaced Ukrainians between 20 and 66 years old. Seven out of ten in this group work more than 30 hours per week. The share of people working is higher among men than women and increases with the length of time since resettlement. In June, the share who were in work two years after resettlement was more than 50 per cent for men and more than 40 per cent for women, see Figure 2.10. The share of displaced people in work varies greatly between counties, and employment is highest in the three northernmost counties. Particularities of the regional labour markets are probably an important explanation for these differences. A large and unmet need for labour in some counties, especially the three northernmost counties, may make it easier for displaced Ukrainians to find work.

The majority of displaced Ukrainians have completed higher education, which probably contributes to them being integrated into the labour market more rapidly than other refugees who have been resettled for the same length of time. Data from Statistics Norway[2] show that only one fifth of immigrants aged 20-66 from Afghanistan, Eritrea and Syria were in work two years after resettlement. Nonetheless, there are barriers to finding work quickly, even for displaced Ukrainians with higher education. In addition to a lack of language skills, many lack professional experience matching their educational background and feedback from the NAV offices indicates that there is often a mismatch between displaced people's skillsets and labour market demand.[3] Although close to half of those who complete the introduction programme enter work or education, many of them need additional training through NAV. Participation in labour market programmes in this group has increased sharply over the past year. Close to one in ten displaced Ukrainians in the 20-66 age group participate in labour market schemes, see Figure 2.11.

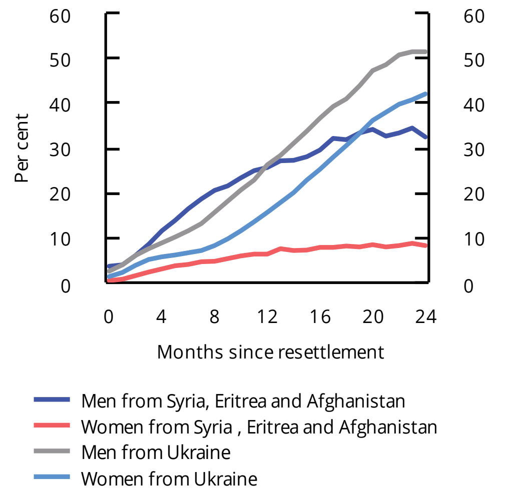
Although the share of displaced people in work has increased over time, the share remains much lower than in Denmark, see Figure 2.12**Feil! Fant ikke referansekilden.**. Part of the explanation for this difference may be that Denmark has placed more emphasis on rapid entry of displaced people into work, while Norway has placed more emphasis on qualifications and language training in the initial period after resettlement. Far more displaced people arrived to Norway in 2023 and so far in 2024 than to Denmark. Their average time since resettlement is therefore much shorter in Norway. This contributes to reducing the share in work and may explain part of the difference between the countries. Nonetheless, the share of displaced people in work two years after resettlement in Norway is still lower than the share of displaced people in work in Denmark. One explanation may be that there were more Ukrainians in Denmark than in Norway prior to February 2022. This may have made it easier for Ukrainians in Denmark to use established networks to find work. Different labour markets, different benefit levels and different schemes for displaced people may also contribute to differences.



Figur 2.9 Labour market status[1] for displaced Ukrainians. 20-66 years of age.
July 2022-August 2024

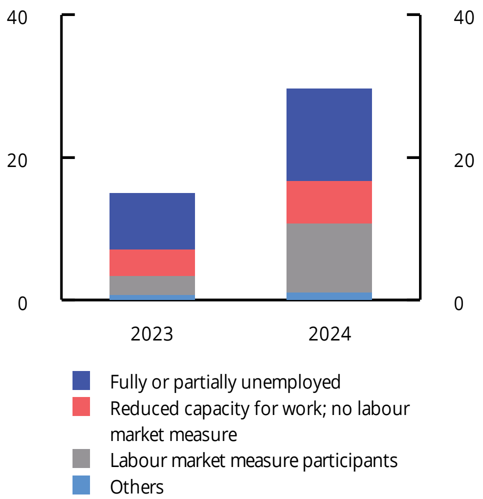
[1] A person may have more than one status at any given time

Source: Norwegian Labour and Welfare Administration.



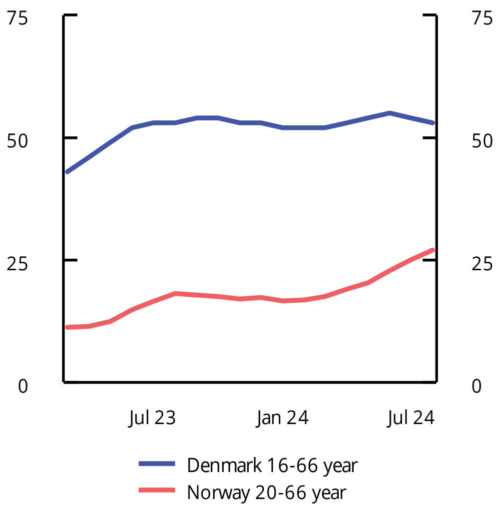
Figur 2.10 Share in work by time since resettlement, country of birth and gender. Immigrants arriving from January 2022 onwards. 20-66 years of age. As of June 2024. Per cent

Source: Statistics Norway.



Figur 2.11 Number of displaced Ukrainians registered with the Norwegian Labour and Welfare Administration. Percentage of the population aged 20-66. As of August

Source: Norwegian Labour and Welfare Administration.



Figur 2.12 Percentage of displaced Ukrainians in work. March 2023-August 2024

Sources: Norwegian Labour and Welfare Administration and jobindsats.dk.

[1] Both Statistics Norway and the Norwegian Labour and Welfare Administration prepare statistics on employment among displaced Ukrainians. The numbers differ somewhat. Numbers from the Norwegian Labour and Welfare Administration are generally used in the box, unless otherwise stated.

[2] Statistics Norway (2024). *One third of Ukrainians are in work.* Article published on ssb.no on 12 September [numbers retrieved on 17 September].

[3] Norwegian Labour and Welfare Administration offices' experiences with the labour market integration of displaced Ukrainians. Norwegian Labour and Welfare Administration report. May 2024.