TALL SOM FORTELLER

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Economic Survey

2024 / 2

Economic developments in Norway

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Economic developments in Norway

Growth in the Norwegian economy has been modest since mid-2022. High inflation and several interest rate hikes have contributed to curbing demand. At the same time there have been substantial, but declining pressures in the labour market. Unemployment has increased through 2023 and so far in 2024 and is now close to the average for the 2010s. Inflation has been halved since the peak in October 2022. In the period ahead we expect activity in the Norwegian economy to pick up, while inflation continues to fall. Given lower inflation and reduced interest rates among our trading partners, the key policy rate will soon also be cut in Norway. Unemployment is expected to increase slightly next year

Table 1. Main macroeconomic aggregates. Accounts figures. Change from previous period. Percent

	2022	2023	Seasonally adjusted			
			23:2	23:3	23:4	24:1
Demand and output						
Consumption in households etc.	6,2	-0,8	0,6	-0,2	0,3	-0,7
General government consumption	1,1	3,4	1,0	1,0	1,0	0,5
Gross fixed investment	5,2	0,0	0,3	-0,5	0,5	-7,3
Extraction and transport via pipelines	-7,1	10,6	6,6	7,5	8,7	-8,1
Mainland Norway	7,6	-1,2	-0,7	-2,8	-2,5	-5,2
Final domestic demand from Mainland Norway[1]	5,1	0,3	0,4	-0,5	-0,2	-1,4
Exports	4,5	1,4	1,7	-1,4	3,4	0,4
Traditional goods	-2,5	6,1	4,4	-1,5	4,2	2,1
Crude oil and natural gas	1,3	-1,1	0,7	-0,9	3,6	-1,7
Imports	12,5	0,7	2,6	-3,6	-0,3	1,0
Traditional goods	3,4	-3,7	1,4	-3,0	-1,4	1,5
Gross domestic product	3,0	0,5	-0,2	-0,5	1,6	0,2
Mainland Norway	3,7	0,7	0,1	0,1	0,3	0,2
Labour market						
Total hours worked. Mainland Norway	3,9	0,8	0,1	0,2	0,5	0,5
Employed persons	3,9	1,3	0,0	0,1	0,1	0,3
Labour force[2]	1,4	1,3	0,5	0,5	-0,0	0,1
Unemployment rate. level[2]	3,2	3,6	3,4	3,6	3,7	3,9
Prices and wages						
Annual earnings	4,3	5,2	..	..	..	..
Consumer price index (CPI)[3]	5,8	5,5	1,7	0,4	1,2	1,0
CPI adjusted for tax changes and excluding energy products (CPI-ATE)[3]	3,9	6,2	1,7	1,1	1,2	0,8
Export prices. traditional goods	30,2	-0,4	-1,8	-3,5	2,1	-0,6
Import prices. traditional goods	15,6	5,8	1,0	-2,3	4,0	-1,6
Balance of payment						
Current balance. bill. NOK[4]	1 722	917	176	193	243	249
Memorandum items (unadjusted level)						
Money market rate (3 month NIBOR)	1,3	3,5	3,2	3,9	4,3	4,5
Lending rate. credit loans[5]	0,7	1,3	4,8	5,3	5,7	6,0
Crude oil price NOK[6]	951	867	832	897	897	857
Importweighted krone exchange rate. 44 countries. 1995=100	110,0	119,4	122,3	117,7	121,0	118,6
NOK per euro	10,10	11,42	11,66	11,40	11,66	11,41

[1] Consumption in households and non-profit organizations + general government consumption + gross fixed capital formation in Mainland Norway.
[2] According to Statistics Norway's labour force survey (LFS).
[3] Percentage change from the same period the previous year.
[4] Current account not adjusted for saving in pension funds.
[5] Period averages.
[6] Average spot price. Brent Blend.
Source: Statistics Norway and Norges Bank

because of low growth among our trading partners and growing labour market participation by Ukrainians in Norway.

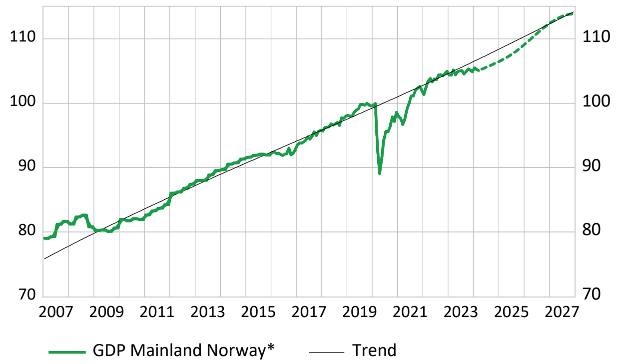
The krone remains weak in a historical perspective. Developments in the krone exchange rate have an important effect on inflation, amongst other things through import prices measured in NOK. Exchange rate movements in the period ahead are shrouded in uncertainty. Research has shown an unchanged exchange rate to be a good prognosis, and we assume that the rate will remain at its mid-June level in the years ahead.

In recent years, consumer price inflation has been very high as a result of global conditions and the depreciation of the krone. Inflation has not been this high since the 1980s. The increase in the annual underlying inflation rate (CPI-ATE) was especially high in the first half of last year, peaking at 7.0 per cent in June. It then slowed gradually to 5.3 per cent in January 2024 and fell further to 4.1 per cent in May. It is primarily developments in prices for imported goods that have pushed down underlying inflation in recent months. We assume a continued stable rise in prices for services through the year, while the rise in prices for goods is expected to fall further, and we expect CPI-ATE inflation to fall from 6.2 per cent in 2023 to 4.1 per cent this year. Energy prices as a whole will increase a little less than underlying inflation this year, bringing the expected rise in the overall consumer price index (CPI) to 3.8 per cent. Low imported inflation and stable developments in energy prices, coupled with lower wage growth, will contribute crucially to inflation falling gradually to the inflation target in 2027.

In December 2023, Norges Bank raised the key policy rate to 4.5 per cent. Norges Bank sets the policy rate primarily to stabilise inflation at around 2 per cent and to ensure financial stability. The central bank also takes into account that a higher interest rate affects activity in the Norwegian economy. We assume that the policy rate will be cut towards the end of 2024. In our projection scenario, the money market rate will come down to 4.0 per cent in 2025 and further down to 3.5 per cent in 2026. Norges Bank has signalled that unforeseen movements in the krone exchange rate could alter the interest rate path. In Box 1 we analyse the relationship between interest rate and krone exchange rate.

Figure 1. GDP Mainland Norway and estimated trend

Seasonally adjusted, index 2021 = 100

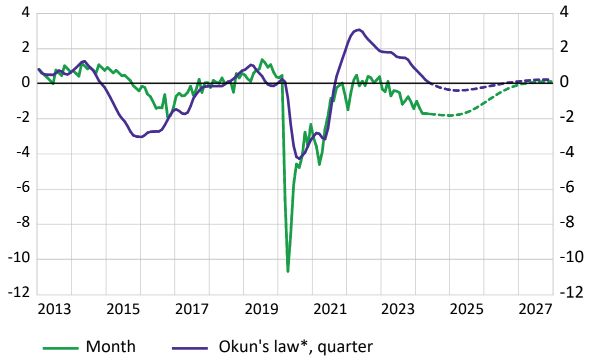


* Quarterly figures before 2016, monthly after. The trend is estimated by an HP-filter (lambda = 40 000 quarterly), but such that the trend is not directly affected by the developement of economic activity in 2020 and 2021.

Source: Statistics Norway

Figure 2. Output gap, Mainland Norway

Deviation form estimated trend GDP in percent, monthly and quarterly frequency



* The series «Okun's law» is based on a one-to-one correspondence between the rate of unemployment and the output gap, cf. box 2.1 i ES 4/2022. The rate of unemployment ris measured relative to the historical average 2010-2020.

Source: Statistics Norway

Fiscal policy features increased scope for manoeuvre and higher investment in defence. Spending of petroleum revenue was increased in the Revised National Budget 2024 (RNB 24), and the budget is regarded as weakly expansionary. The increase in expenditure is largely due to an increase in proposed appropriations for defence as well as for the police, hospitals, the national insurance scheme and support for Ukraine. As a consequence of the sharp increase in the market value of the Government Petroleum Fund Global (the petroleum fund) from the submission of the National Budget last year until the end of the year, the withdrawal rate will remain 2.7 per cent, despite the higher spending of petroleum revenue forecast in RNB 24. The new long-term plan for defence entails substantial investment in defence over the next 12 years. Public investment is expected to grow by around 4 per cent annually up to 2027, while annual growth in consumption is expected to be around 2 per cent. We assume that in the years ahead use of petrole-

Table 2. Growth in GDP Mainland Norway and contributions from demand components[1]. Percentage points. Annual rate

	QNA				Projection			
	2020	2021	2022	2023	2024	2025	2026	2027
GDP Mainland Norway	-2,8	4,5	3,7	0,7	0,5	2,4	2,9	2,9
with contributions from:								
Consumption by households and non-profit organisations	-0,6	1,8	0,8	-0,4	-0,0	0,8	1,2	1,3
General government consumption and investment	-0,2	0,8	0,3	1,0	0,7	0,6	0,7	0,8
Petroleum investment	-0,1	-0,0	-0,3	0,3	0,4	-0,1	-0,1	-0,1
Housing investment	-0,1	0,2	-0,1	-0,8	-0,6	0,2	0,5	0,4
Other mainland investment	-0,3	0,2	1,0	0,3	-0,6	-0,1	0,1	0,1
Exports from mainland Norway[1]	-2,6	2,1	1,4	1,0	1,0	0,7	0,7	0,6
Other factors etc.[1]	1,2	-0,6	0,4	-0,8	-0,4	0,1	-0,0	-0,2

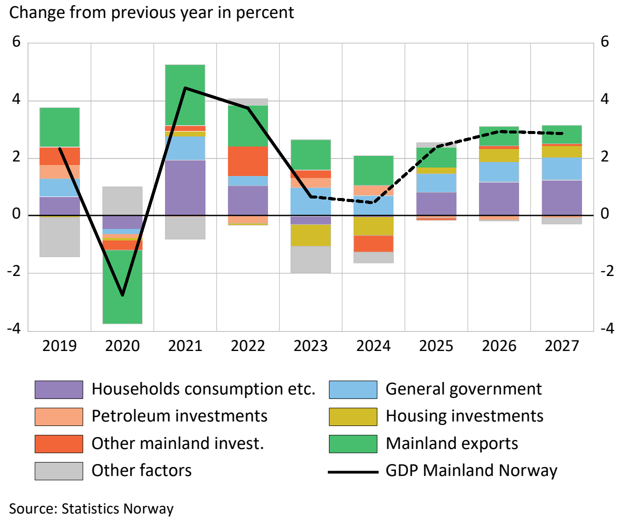
[1] See explanation under Figure 3.
Source: Statistics Norway.

um revenue will remain within the fiscal rule's limit of 3 per cent of the value of the petroleum fund, despite the increased investment in defence.

Household consumption, which accounts for around half of mainland GDP, exhibited weak developments through 2023, dominated by low sales of furniture, white goods and cars. This should be viewed in the light of high sales of these goods during the pandemic, as well as a higher cost of living and higher interest rates. In Q1 this year, consumption fell as a consequence of lower goods consumption, both including and excluding car purchases. However, the goods consumption index for April exhibited a broad-based upswing. Going forward, we expect increasing growth in real disposable income and real wealth to boost consumption. Overall consumption as an annual average is expected to be virtually unchanged in 2024, which implies a clear upswing in consumption through the next three quarters. Consumption growth is forecast to increase further, to almost 4 per cent, in 2026 and 2027. Our projections imply that the saving ratio will then be around 6–7 per cent in the years ahead, which is fairly close to the average for the ten-year period 2010–2019.

Business investment reached a historically high level in 2023 after growth of almost 30 per cent from 2021 Q3 to 2023 Q2. Since then, investment has fallen steadily, and in Q1 this year is around 18 per cent lower than the peak. Overall, business investment accounts for about 13 per cent of mainland GDP, but because it is relatively volatile, it normally contributes more to economic developments than this share would suggest. This year we expect investment to be reduced by an annualised average of 7 per cent. Businesses report lower investment in both manufacturing and services.

Figure 3. Contributions to growth in GDP Mainland Norway, import adjusted



The demand contributions are calculated by finding the change in each variable. extracting the direct and indirect import shares. and then dividing by the mainland GDP level for the previous period. The import shares used are documented in Box 3. All figures are seasonally adjusted and in constant prices.

The export variable is defined as total exports excluding exports of crude oil. gas and shipping.

Other factors are defined as changes in stock and statistical deviations.

One exception is power supply, where a sharp rise in investment is expected this year, particularly in the transmission and distribution of electricity. In isolation, rising real interest rates will push down the investment level going forward, while increased economic activity will push it up. On balance, business investment is expected to remain at the current level in the years up to and including 2027.

Petroleum investment increased by a whole 10.6 per cent in 2023. This year, too, a substantial increase in investment is expected according to the petroleum companies' reporting to the quarterly survey on investment in oil and gas, manufacturing, mining and power supply (KIS). The fluctuations in petroleum investment are very largely

Table 3. Main economic indicators 2023-2027. Accounts and forecasts.
Percentage change from previous year unless otherwise noted

	Accounts 2023	Forecasts 2024 SN	2024 NB	2024 MoF	2025 SN	2025 NB	2025 MoF	2026 SN	2026 NB	2026 MoF	2027 SN	2027 NB
Demand and output												
Consumption in households etc.	-0,8	0,2	1,0	1,0	2,7	2,1	2,0	3,8	2,1	..	3,8	2,1
General government consumption	3,4	2,2	2,1	2,1	1,8	1,4	..	1,9	1,5	..	2,4	1,2
Gross fixed investment	0,0	-3,5	..	-1,7	1,3	..	0,4	2,9	..	..	2,8	..
Extraction and transport via pipelines	10,6	10,0	10,0	7,3	-2,0	-5,0	-4,0	-4,0	-3,0	..	-2,1	-3,0
Industries	4,0	-8,2	-4,4	-2,6	-1,1	1,9	-3,4	1,6	2,8	..	1,1	3,0
Housing	-15,6	-15,4	-12,5	-16,1	6,7	5,9	13,0	12,7	9,6	..	9,9	9,0
General government	3,0	3,2	..	4,1	4,0	..	..	4,1	..	..	3,9	..
Demand from Mainland Norway[1]	0,3	-0,9	0,0	0,2	2,3	2,0	1,8	3,4	2,3	..	3,4	2,3
Exports	1,4	3,1	..	2,4	3,8	..	4,5	0,8	..	..	1,2	..
Traditional goods[2]	6,1	5,9	2,6	3,6	2,5	1,9	2,9	2,9	1,9	..	3,0	2,7
Crude oil and natural gas	-1,1	1,6	..	-0,2	3,6	..	4,4	-2,1	..	..	-1,3	..
Imports	0,7	0,6	-1,7	2,7	2,5	2,0	2,7	3,2	1,9	..	3,5	2,1
Gross domestic product	0,5	0,8	0,4	0,7	2,7	1,8	2,4	1,9	0,5	..	2,0	0,7
Mainland Norway	0,7	0,5	0,5	0,9	2,4	1,2	1,9	2,9	1,3	..	2,9	1,6
Labour market												
Employed persons	1,3	0,2	0,4	0,5	0,6	0,4	0,5	0,9	0,6	..	0,6	1,0
Unemployment rate (level)	3,6	4,1	..	3,8	4,2	..	3,9	4,1	..	..	4,0	..
Prices and wages												
Annual earnings	5,2	5,2	4,9	5,2	4,6	4,3	..	4,2	3,7	..	3,7	3,4
Consumer price index (CPI)	5,5	3,8	3,8	3,9	3,0	2,7	2,8	2,3	2,6	..	2,1	2,3
CPI-ATE[3]	6,2	4,1	4,1	4,3	3,1	3,2	3,0	2,6	2,7	..	2,2	2,3
Housing prices[4]	-0,5	2,6	1,0	..	3,7	5,1	..	3,7	6,5	..	3,6	..
Balance of payment												
Current balance (bill. NOK)[5]	917	825	..	753	946	..	..	839		..	732	..
Current account (per cent of GDP)	17,9	15,9	..	14,6	17,1	..	..	14,8		..	12,5	..
Memorandum items:												
Money market rate (level)	4,2	4,7	..	4,7	4,0	..	4,2	3,5	..	..	3,5	..
Crude oil price NOK (level)[6]	82	81	..	83	78	..	78	75	..	..	73	..
Import weighted krone exchange rate (44 countries)[7]	8,5	-0,2	-0,6	1,1	0,0	-0,1	0,6	0,0	-0,3	..	0,0	-0,3

[1] Consumption in households and non-profit organizations + general government consumption + gross fixed capital formation in Mainland Norway.
[2] Norges Bank forecasts exports of traditional goods and services from Mainland Norway. Ministry of Finance forecasts exports of goods exclusive of oil and natural gas.
[3] CPI adjusted for tax changes and excluding energy products (CPI-ATE).
[4] Norges Bank forecasts the housing price index published by Eiendom Norge.
[5] Current account not adjusted for saving in pension funds.
[6] Average spot price. Brent Blend.
[7] Increasing index implies depreciation.
Source: Statistics Norway (SN). Ministry of Finance. Nasjonalbudsjettet 2024 (MoF). Norges Bank. Pengepolitisk rapport 1/2024 (NB).

driven by investment in offshore developments. A number of new developments are expected and we forecast, as in our previous report, that growth this year will be around 10 per cent. This implies a further increase through the year. As a consequence of lower investment in ongoing developments, we still expect petroleum investment as a whole to fall over the next few years but to nonetheless leave the level in 2027 approximately the same as in 2019. Although almost half of the deliveries of capital goods for the petroleum industry are imported from abroad, they also imply considerable demand for deliveries from mainland Norway.[1] The reduction in petroleum investment in the years ahead will thus also have a dampening effect on mainland economic growth.

Housing investment fell by as much as 21 per cent through 2023. Such a sharp fall over such a short period has not previously been recorded in the

[1] An overview of import shares in final consumption is provided in *Economic Survey* 1/2024, Box 3.

quarterly national accounts, which go back to 1978. Housing accounts for approximately 20 per cent of mainland investment, and the sharp fall has been a factor in pushing down activity in the Norwegian economy as a whole. The fall continued through Q1 this year, and investment is almost 30 per cent lower than the level two years ago. The most recent figures from the Norwegian Homebuilder Association show that sales of new dwellings, a leading indicator of housing starts, may have reached a turning point. We forecast that housing investment will fall by around an annualised 15 per cent this year, which implies a slight rise in housing investment in the remainder of the year which will then gather pace in the next few years. This increase must be viewed in light of the expectation that house prices will rise in the years ahead. However, projections for developments in house prices are particularly uncertain. Households' expectations of future house prices coupled with possible policy changes are factors that may influence house prices strongly in the short term. In the macroeconomic model we use for our projections, house prices are driven up in the long term by household real disposable income, housing wealth, debt and real interest rates.[2] The rising real interest rates will place a definite damper on the increase in house prices in the years ahead. Box 2 provides an analysis of the significance of the various forces driving developments in house prices in our projections. Given the economic picture we now envisage, house prices will be around 14 per cent higher in 2027 than they were last year.

There was virtually no real wage growth in Norway from 2015 to 2023. Nominal wage growth last year was 5.2 per cent, which meant a slight reduction in real wages. After mediation by the National Mediator of Norway, the Federation of Norwegian Industries (Norsk Industri) and the United Federation of Trade Unions (Fellesforbundet) reached agreement on a norm of 5.2 per cent for annual wage growth in 2024 in overall manufacturing under the Confederation of Norwegian Business and Industry (NHO). The profitability of the wage leader sector is in focus when the social partners negotiate the framework for the wage settlement. The labour share, which is a measure of the share of wealth creation in the economy that accrues to the workers, fell substantially last year as a result of good profitability in some of the activities that make up the wage leader segment. The low labour share is likely to contribute to wage growth remaining high in the years ahead. According to our projections, wage growth will be 5.2 per cent this year, in line with the wage leader norm, before falling to somewhat under 4 per cent towards 2027. Given this scenario, the labour share will pick up and approach the average for the past 20 years. Real wage growth will then be close to 1.5 per cent annually up to 2027.

Unemployment will continue to rise a little. Through 2023, unemployment measured by the trend figure in the Labour Force Survey (LFS) rose from 3.5 per cent at the beginning of the year to 3.8 per cent at year-end. To date in 2024 unemployment has continued to rise, and was 4 per cent in April, close to the average for the 2010s. We expect immigration of asylum-seekers from Ukraine to increase both the labour force and unemployment going forward. It is uncertain how large the increase will be, in terms of both how many come and how many return home in due course. We have based our projections on the national population projections, which indicate that around 20 000 Ukrainians are expected to come to Norway in 2024, followed by a further 10 000 in 2025. The abrupt halt in residential construction is also expected to create more unemployment in the immediate future. According to our projections, unemployment will rise to 4.1 per cent this year and then further to 4.2 per cent in 2025.

The Norwegian economy was characterised by stagnation through the whole of 2023, and the weak tendency has continued so far in 2024. However, there are several factors indicating that economic activity will gradually pick up. Inflation is on the way down, and the policy rate will very likely be cut towards the end of the year. Good profitability in the wage leader segment is pushing up wage and income growth, thereby stimulating household consumption. Public consumption and investment will probably grow markedly in the years ahead, amongst other things because of particularly strong investment in defence. In addition, the fall in housing investment will probably soon reverse into an upturn. Given this scenario, activity in the Norwegian economy is expected to pick up markedly in 2025 and approach what we regard as a cyclically neutral situation from 2026.

[2] See Boug, P., Hungnes, H. & Kurita, T. (2024). The empirical modelling of house prices and debt revisited: a policy-oriented perspective. *Empirical Economics* , 66, 369– 404.

Fiscal policy features increased scope for manoeuvre and higher defence investment

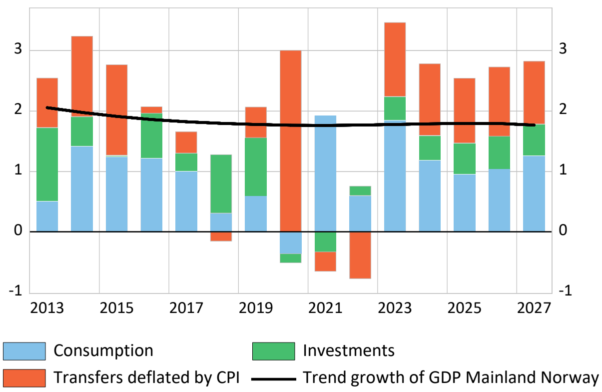
General government spending grew by 0.5 per cent in 2024 Q1. Both central and municipal government spending grew by 0.5 per cent, with defence spending accounting for most of the increase. Gross general government investment fell by 6.0 per cent, but the fall was due mainly to abnormally high investment in the previous quarter. Gross investment in 2024 Q1 was 2.8 per cent higher than in the same quarter the previous year. The level of general government investment is high in a historical perspective.

In RNB 24, spending of petroleum revenue in 2024, measured as the structural, non-oil budget deficit, is forecast to be NOK 418.7 billion. Spending is forecast to be about NOK 9 billion higher than the projections in the National Budget and the Final Budget Bill. Both income and expenditure are forecast to be higher in RNB 24. Revenue from structural taxes and excise is forecast to increase by NOK 10.1 billion. Spending is increasing largely as a consequence of increased appropriations for defence in order to meet the NATO target of spending at least 2 per cent of GDP on defence. It is also increasing as a result of increased appropriations for the police, hospitals, the national insurance scheme and support for Ukraine. The fiscal stimulus, measured as the change in the structural non-oil budget deficit as a share of trend mainland GDP, has been revised up from 0.4 to 0.7 percentage point in RNB 24. The budget for 2024 is expected to have a weakly expansionary effect on the economy in 2024. Budgets from previous years are also expected to have an expansionary effect on economic activity this year. The overall effect thus appears to be a good deal stronger than in previous projections. The RNB also proposes abolishing the extra payroll tax on income in excess of NOK 850 000 from 1 January 2025.

The value of the Government Petroleum Fund Global (petroleum fund) was NOK 15 761 billion at the beginning of 2024, more than NOK 450 billion higher than assumed in the Government's original budget proposal. As a result, the amount withdrawn will remain at 2.7 per cent, despite higher forecast spending of petroleum revenue in RNB. In recent years the value of the fund has increased significantly as a result of favourable developments in global finance markets. The depreciation of the

Figure 4. Contributions to growth in general government

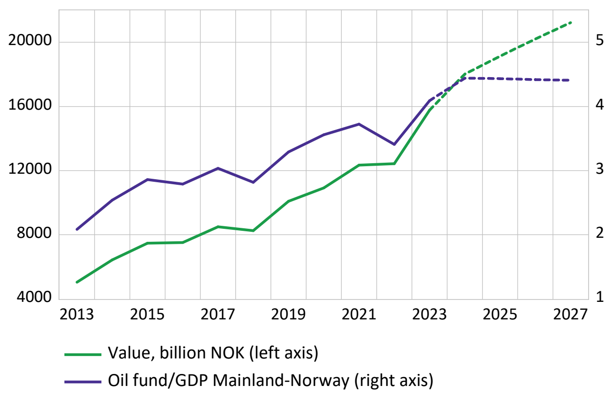
Change from previous year in percent



Source: Statistics Norway

Figure 5. The Norwegian Oil Fund / Government Pension Fund Global

Value, measured in billion NOK and in terms of GDP Mainland-Norway, year



Source: NBIM and Statistics Norway

krone has also contributed to increasing the value of the fund measured in NOK. In addition a large amount of capital has been added to the fund. RNB forecasts that the state's net cash flow from petroleum activities will be NOK 673 billion in 2024.

The fund's value has increased considerably since the beginning of the year, and in mid-June was approximately NOK 17 700 billion. This will increase the fiscal scope for manoeuvre in the period ahead. We expect that the defence programme will entail extensive investment in the projection period. Increased imports of military defence materiel, such as fighter aircraft, will have little impact on activity in the Norwegian economy. However, purchases of defence materiel produced in Norway, as well as investment in and upgrading of the defence infrastructure in Norway, will stimulate economic activity. This stimulus is expected to counter the decline in construction. An increasing need for health and care workers is also expected in the time ahead. We assume that the real return on the fund will be 3 per cent, and that inflows will be based on oil and gas prices that shadow forward prices. We have assumed that spending of petroleum revenue will be kept under the 3 per cent limit, despite the increased investment in defence in the time ahead.

In our previous report, we forecast growth in general government consumption and gross investment of 2.1 and 2.5 per cent, respectively, in 2024. The national budget for 2024 projected growth in general government consumption and gross investment of 1.4 and -0.5 per cent, respectively. RNB 24 forecasts growth of 2.1 and 4.1 per cent, respectively. It is proposed in RNB that military support for Ukraine be increased by NOK 6 billion in 2024, amongst other things by increasing support for air defence systems. Gross investment is defined as new capital less sales of real capital. Donations of heavy defence materiel to Ukraine are regarded as sales of real capital in the national accounts. These donations will thus reduce gross general government investment; see Box 3.2 in Økonomiske Analyser 1/2024 (Norwegian text). However, support for Ukraine through purchases of air defence from other countries will not affect gross investment in Norway.

RNB proposes that NOK 7 billion extra be appropriated to upgrade the Norwegian defence capability. Investment in the Norwegian defence capability will increase gross general government investment. Some of this investment was incorporated in our previous economic report. We now forecast growth in general government gross investment of 3.2 per cent for 2024. This is somewhat higher than the projections in the previous report, where growth in gross investment was revised upward with effect from 2025 as a result of higher defence investment. We are nonetheless making a modest upward revision of these projections as a result of the reacquisition of defence materiel donated to Ukraine as well as decisions by the Storting (Norwegian parliament) on a long-term plan for defence. Public consumption is forecast to grow by about 2 per cent annually further down the projection path, as in our previous economic report. The real value of transfers, measured by the consumer price index, is expected to increase by about 3.5 per cent in subsequent years, as in the previous report.

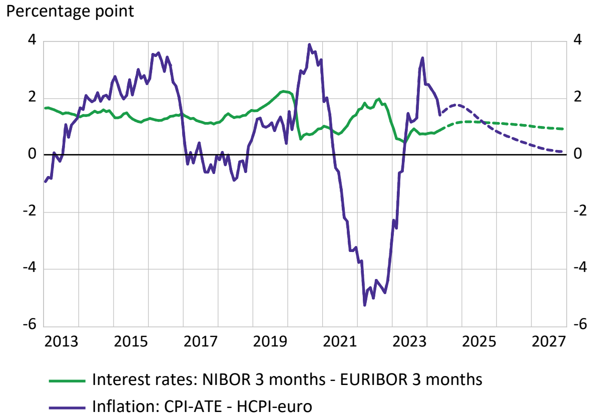
Interest rate cuts postponed

In December 2023, Norges Bank raised the key policy rate to 4.5 per cent. Norges Bank's Monetary Policy and Financial Stability Committee signalled at the same time that it expected to keep "the policy rate at that level for some time ahead". They maintained that signal at the monetary policy meetings in January and March this year. The policy rate path published in the March Monetary Policy Report indicated that the first rate cut will come in September this year at the earliest. At the May monetary policy meeting, the Committee announced that new information indicates "that a tight monetary policy stance may be needed for somewhat longer than previously envisaged." At the same time, the Committee signalled that it would cut the policy rate earlier if "there is a more pronounced slowdown in the Norwegian economy or prospects suggest that inflation will return to target faster".

The money market rate normally shadows the key rate with an added premium. However, the money market rate did not increase last year in connection with the September and December rate hikes. This may be because part of the increase in the policy rate had already been priced into the money market rate. The premium may also have been reduced. The 3-month money market rate has remained almost unchanged at around 4.7 per cent since the beginning of August last year.

Deposit and lending rates from banks and financial institutions have increased from record low levels in 2021 Q2 and Q3. In the course of less than three years, the average interest rate on loans secured

Figure 6. Interest rate and inflation differential between NOK and euro



Source: Norges Bank and Statistics Norway

Box 1: How much should the interest rate be increased in the face of a weaker krone?

The import-weighted krone exchange rate weakened by 8.6 per cent in 2023. The krone exchange rate affects the Norwegian economy through various channels, and a key question for Norges Bank is how monetary policy should respond to a weaker krone.[1]

The Storting and the Government have defined the central bank's mandate. The primary objective of the mandate is to maintain monetary stability and promote stability in the financial system, while also placing emphasis on the objectives of high and stable output and employment. Given more objectives than instruments, Norges Bank must strike a balance between the different objectives in its implementation of monetary policy. The trade-off between the different objectives is described in Norges Bank's principal model, NEMO, in the form of a loss function.[2] In the loss function, emphasis is placed on stabilising inflation and the activity level. The loss function also takes account of the objective of financial stability, in that the interest rate should not be changed too rapidly, or deviate too much from a normal level.

In this box we analyse the effects of a change in the foreign exchange market, a shock that weakens the krone by 10 per cent through the whole period of the analysis if the interest rate is not raised to counter the depreciation (see Figure 1). The analysis is performed using the KVARTS macroeconomic model.[3] In order to calculate the monetary policy response, we start with the loss function specified in NEMO and use it in KVARTS instead of the interest rate equation that is normally used. Norges Bank places great emphasis on the labour market in its calculations of the output gap; see for example Furlanetto et al. (2023). In our calculations we have therefore assumed that there is a one-to-one relationship between developments in unemployment and the output gap (Okun's law).[4] Fiscal policy is kept unchanged during the calculations.

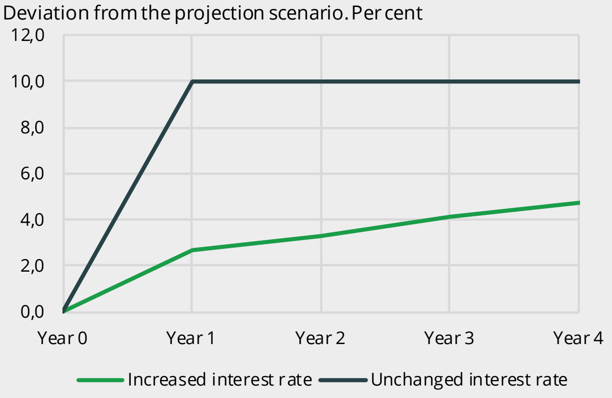
A depreciation of the krone, which we analyse in this box, does not give rise to a conflict between the objectives of stabilising inflation and output. A weaker krone results in higher inflation, in that it becomes more expensive to import goods and services. A weak krone also results in higher economic activity. Although in isolation a weaker krone reduces real disposable income and consumption, which pushes down demand a little, it contributes to a greater extent to boosting activity in export-oriented industries, particularly services. For example, a weaker krone makes it cheaper for foreigners to holiday in Norway. Taking account of both inflation and output therefore points to increasing the interest rate to counter a weaker krone exchange rate.

In the projection, the interest rate is increased by about 1.4 percentage points the first year, before it is reduced a little, such that it is around 0.9 percentage point higher than the baseline scenario after four years; see Figure 2. The interest rate increase neutralises about two thirds of the immediate depreciatory pressure on the krone. The weakening of the krone in the first year will then only be around 3 per cent and not 10 per cent, which would have been the effect in the absence of an interest rate response.

The raising of the interest rate also neutralises the expansionary effects on the labour market, so that unemployment and employment remain at about the same level as prior to the depreciation of the krone. Inflation increases initially by 0.5 percentage point and then remains about 0.3 percentage point higher through the projection period. Even though the nominal annual wage increases as a consequence of higher profitability in the wage leader segment, the rise in prices nonetheless leads to a reduction in real wages. The interest rate hike also causes house prices to fall by around 8 per cent after 4 years. In real terms, house prices fall a little more. Although Norges Bank is not mandated to set the interest rate to fine-tune the housing market, house prices are often used

Figure 1. Exchange rate

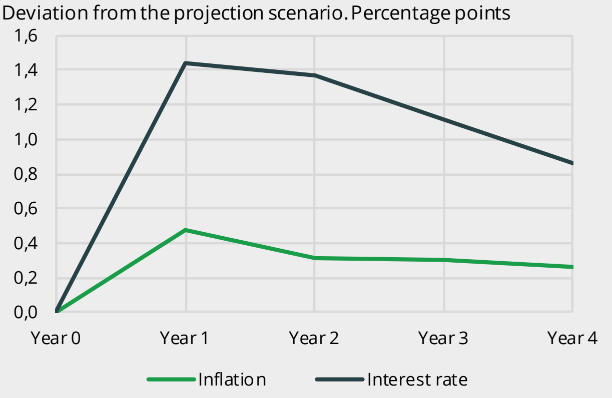
Deviation from the projection scenario. Per cent



Source: Statistics Norway

Figure 2. Inflation and interest rate

Deviation from the projection scenario. Percentage points



Source: Statistics Norway

[1] Norges Bank has responded strongly to changes in the exchange rate compared with other countries; see for example Alstadheim et al. (2021).

[2] The loss function based on that in NEMO is given by: $\sum_{t=0}^{T}\beta^t[\hat{\pi}_t^2+\lambda\hat{y}_t^2+\gamma\hat{\imath}_t^2+\delta\Delta i_t^2]$, where β is a discounting factor for quarterly frequency, $\hat{\pi}_t$ represents inflation measured as deviation from the inflation target in the period t, $\hat{y}_t$ is the output gap, $\hat{\imath}_t$ is the money market rate measured as deviation from a normal interest rate level and Δi_t represents the change in the money market rate from one period to the next. We have used the parameter values specified in NEMO: $\beta = 0{,}99, \lambda = 0{,}3, \gamma = 0{,}02$ and $\delta = 0{,}4$, see Kravik and Mimir (2019, p. 74) and the description in Norges Bank's monetary policy handbook (Norges Bank, 2022, pp. 41–43)

[3] See Boug et al. (2023) for a more detailed description of KVARTS.

[4] Specifically, this means that a 1 per cent increase in the output gap coincides with a 0.3 percentage point reduction in the unemployment gap; see Box 1 in Economic Survey 4/2022 for a more detailed description of this relationship.

nonetheless as an indicator of financial stability, which is a primary objective of monetary policy in Norway. The depreciation of the krone thus creates a conflict between developments in the housing market (financial stability) and general inflationary developments, measured by the CPI. It is because of the considerations of financial stability and developments in the real economy that the interest rate is not increased more in the face of a weakened krone exchange rate. For the central bank to eliminate the effect on inflation, the interest rate would have to be raised by just over 2 percentage points, and not 1.4 percentage points as shown in the calculations in this box.

Model-based analyses of this type are uncertain. First, there is uncertainty associated with how a central bank loss function should be specified. In the analysis, we have used the symmetrical loss function in Norges Bank's NEMO model. However, the economic costs of cyclical fluctuations are probably asymmetric, which Norges Bank attempts to take into account in its setting of interest rates (Norges Bank, 2022, p.22). There is also uncertainty associated with the mechanism of the Norwegian economy and how other economic policy instruments respond. We have excluded a fiscal policy response from our calculations, although a weakening of the krone increases fiscal scope for manoeuvre; see Dyvi (2022). Moreover, KVARTS represents a simplified description of the economy and the model does not necessarily capture all relevant relationships in the Norwegian economy. For example, there is uncertainty as to how the krone responds to interest rate changes, and the extent to which expectations of further price developments play a part in businesses' pricing when inflation is relatively close to the inflation target.[5] The analysis shows the effects on the Norwegian economy of a weaker krone exchange rate, but says nothing about which economic shocks could give rise to such a depreciation. How much the interest rate should be changed to counter a weaker krone will also depend on which other economic disturbances cause the krone to depreciate.

Monetary policy in the face of a weaker krone exchange rate
Deviation from the baseline scenario in per cent unless otherwise indicated

	Year 1	Year 2	Year 3	Year 4
Mainland GDP	-0.1	-0.4	-0.6	-0.6
Consumption by households etc.	-0.6	-1.7	-2.3	-2.4
Business investment	-0.8	-3.1	-3.1	-2.6
Exports excl. oil and gas	0.5	0.8	1.2	1.5
Imports	-0.5	-1.4	-1.8	-1.9
Unemployment rate (percentage points)	0.0	0.0	0.0	0.0
Annual wages	0.1	0.3	0.5	0.8
Number employed	0.0	-0.1	-0.1	-0.1
Household real disposable income	-1.5	-1.9	-1.6	-1.3
House prices	-0.3	-3.6	-6.4	-7.9
Consumer price index (CPI)	0.5	0.8	1.1	1.3
Inflation, CPI (percentage points)	0.5	0.3	0.3	0.3
Money market rate (percentage points)	1.4	1.4	1.1	0.9
Exchange rate, NOK per euro*	2.7	3.3	4.1	4.7

The calculation is based on a shock that weakens the krone by 10 per cent in the absence of a monetary policy response. Monetary policy is calculated using the loss function in Norges Bank's main NEMO model, while fiscal policy is kept unchanged.
* A negative sign means appreciation.
Source: Statistics Norway

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[5] See Benedictow and Hammersland (2023) for a description of the relationship between the exchange rate and the interest rate, and Boug et al. (2017) for an analysis of businesses' pricing in Norway, and the significance of expectations.

on dwellings rose from 2.0 per cent at the end of 2021 Q3 to 6.1 per cent at the end of 2024 Q1. During the same period, the average deposit rate increased by just over 3 percentage points, to 3.4 per cent.

Norges Bank sets the interest rate primarily to stabilise inflation at around 2 per cent and to ensure financial stability. The central bank also takes into account that the setting of the interest rate influences the krone exchange rate, and thereby imported inflation. It also takes into account that the interest rate level affects activity in the Norwegian economy.

Inflation measured by the 12-month rise in the consumer price index (CPI) was 3.0 per cent in May this year. The 12-month rise in the CPI, adjusted for tax changes and excluding energy products (CPI-ATE) was 4.1 per cent in same month, down from 6 per cent in October 2023. Thus inflation is far higher than the inflation target, although it has declined appreciably in the course of just over six months.

The reduction thus far this year in the 12-month rise in the CPI has led us to revise CPI inflation for 2024 as a whole down slightly since our previous economic report. Mainland GDP growth for 2024 has also been revised slightly down since the previous report. In isolation, this points to more rapid interest rate cuts. However, both CPI inflation and activity growth have been revised upwards for next year. As Norges Bank is intended to be forward-looking in its setting of interest rates, this points the opposite way. Our projections for the levels of both activity and prices in 2027 are higher than in our previous report, and on balance this points to postponement of the first interest rate cut.

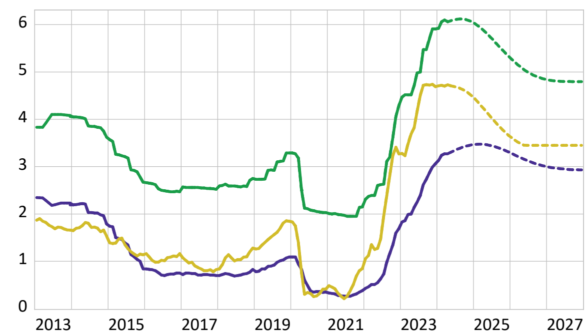
Developments in the krone exchange rate also have an important effect on inflation through import prices measured in NOK. Norges Bank also monitors wage developments. Expectations of a weakened krone may be reflected in higher wage demands, which in turn will weaken the krone. Thus expectations can be self-fulfilling, and contribute to instability.

At the beginning of June a euro was worth NOK 11.50, roughly as in our previous report. The US dollar had strengthened marginally, to NOK 10.60. This means that the krone, measured in terms of the import-weighted exchange rate, has depreciated slightly since the last report. Our projections are based as previously on exchange rates remaining unchanged in the near term.

Norges Bank will probably attempt to prevent a renewed depreciation of the krone. It will therefore probably not begin cutting the interest rate before other countries have cut theirs. The European Central Bank has made the first rate cut. We expect the US to make the first cut in the second half of this year. It now looks as though the cuts in the US will come later than seemed likely in our previous report, so we will probably not see the first cut in

Figure 7. Norwegian interest rates

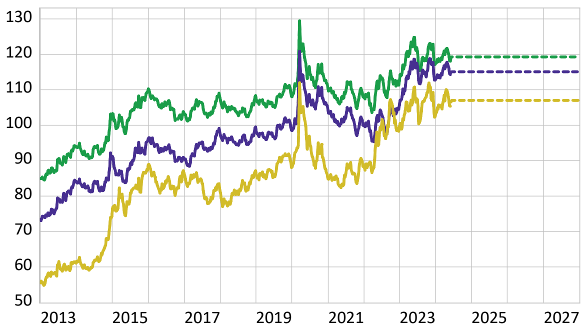
Percent



Banks' lending to households
Households' deposits in banks
Norges Bank's policy rate

Source: Norges Bank and Statistics Norway

Figure 8. Exchange rates



Import-weighted exchange rate index, 1995 = 100 (left axis)
NOK per euro (right axis)
NOK per USD (right axis)

Source: Norges Bank

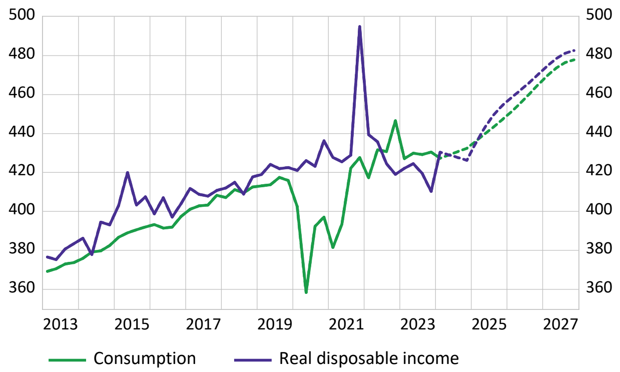
Norway until nearly the end of 2024. We expect cuts in Norway to continue in 2025, but at a slower rate than envisaged previously. In our projection scenario, the money market rate will come down to 3.5 per cent in 2026, which is slightly higher than our projection in March this year. This means four or five interest rate cuts, each of 0.25 percentage point. The interest rate on loans secured on dwellings, forecast to be 6.0 per cent this year, will then fall by just over 1 percentage point by 2027.

Consumption will pick up

According to the preliminary non-financial sector accounts, the real disposable income of households and non-profit organisations, both including and excluding share dividends, fell by around 2.5 per cent in 2023. The fall is about 1 percentage point larger than published previously, and is mainly due to an upward revision of annualised net interest expenses of around NOK 15 billion last

Figure 9. Income and consumption in households

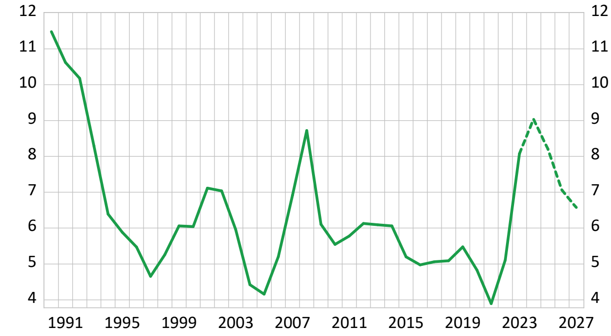
Seasonally adjusted, billion 2021 NOK, quarter



Source: Statistics Norway

Figure 10. Household interest burden

Interest expenses after tax as a share of disposable income in percent, year



Source: Statistics Norway

year.[3] Developments in real disposable income in 2023 were driven by higher wage income due to growth in wages and employment, increased public transfers partly due to higher disbursements of old-age pensions, higher net interest expenses due to higher borrowing rates, and increases in prices for a number of goods and services. In 2024 Q1 real disposable income, also adjusted for share dividends, picked up markedly from a low level the previous quarter. Benefits from various funds as well as public transfers and pensions contributed substantially to this upswing.

According to the preliminary national accounts, total consumption by households and non-profit organisations decreased by close to 1 per cent in 2023, following growth of just over 6 per cent in 2022. The weak developments in consumption through 2023 were dominated by low sales of furniture, white goods and cars. This must be viewed in light of the higher cost of living and higher interest rates, coupled with high sales of these goods during the Covid pandemic. The low level of car purchases must also be viewed in light of the introduction of taxes on electric cars in January 2023, which brought planned car purchases forward to 2022. Overall consumption dipped a further 0.7 per cent in Q1 this year despite a clear rise in income in the same period. Goods consumption fell by 2.2 per cent, while consumption of services edged up 0.2 per cent. The decline in goods consumption was broad-based. A sharp fall in car purchases pushed down consumption most, indicating that households continued to cut down on major long-duration purchases in Q1 of this year. With car purchases excluded, the decline in goods consumption would have been 0.8 per cent. While consumption in Norway exhibited weak developments in Q1, Norwegians' purchases abroad and foreigners' purchases in Norway increased by 4.2 and 3.1 per cent, respectively.

Measured in current prices, consumption in the second half of 2022 and in much of 2023 was clearly higher than disposable income. The saving ratio, measured as saving as a share of disposable income, fell from a record level of around 14 per cent in 2021 to around 5 per cent in 2022.[4, 5] The ratio excluding share dividends shrank from around 5.5 per cent to around 0.5 per cent in the same period. From 2022 to 2023 the saving ratio, both including and excluding share dividends, fell by just short of a further 1 percentage point. As income showed a clear increase and consumption fell somewhat in Q1 this year, the saving ratio both including and excluding share dividends increased in the same period to levels of around 6.5 and 2.5 per cent, respectively.

We now forecast that real disposable income, both including and excluding share dividends, will increase by around 2.5 per cent this year. This is a substantial upward revision compared with our previous report, and is mainly attributable to a downward revision of the level of real income in the non-financial sector accounts, and to inflation this year likely being lower than previously forecast. For the years 2025–2027, growth in real disposable income as an annual average will rise

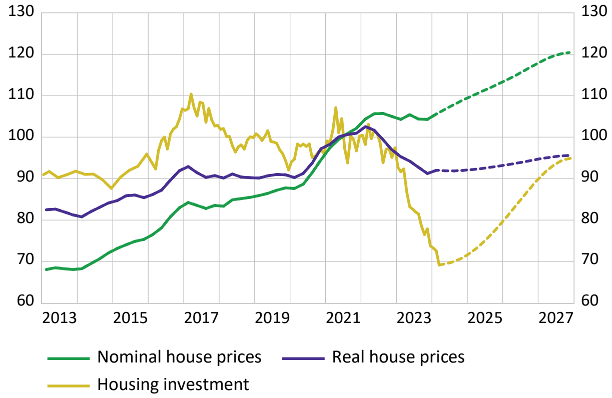
[3] Further details of the revision can be found in the article [Økt sparing i husholdningene [Increased household saving]].

[4] Household saving includes saving in collective pension funds. Thus household saving has been positive, despite consumption being higher than disposable income.

[5] The high level of the saving ratio in late 2021 is due to large share dividend disbursements prior to an increase in taxation of these dividends.

further to close to 4 per cent. In isolation, the real value of both wage income and public transfers will increase, given lower inflation going forward. A fall in net interest expenses will also contribute to income growth as mortgage rates are reduced due to cuts in the policy rate. The level of the household interest burden, measured as interest expenses after tax as a share of disposable income, is projected to rise from around 8 per cent in 2023 to around 9 per cent in 2024. The interest burden will fall gradually from 2024 to 2027, to around 6.5 per cent. By way of comparison, the average annual interest burden was 5.5 per cent in the 10-year period 2010–2019.

Figure 11. Housing market
Seasonally adjusted, index, 2021 = 100



Source: Statistics Norway

We forecast zero growth in total consumption in 2024, roughly half a percentage point less than published previously. The downward revision is mainly attributable to considerably weaker developments in consumption in Q1 than assumed previously. Nonetheless, the projection for annual growth in 2024 implies a clear rise in consumption through the next three quarters. The goods consumption index for April this year showed broad-based seasonally adjusted growth of just over 4 per cent. Consumption growth will gradually pick up to close to 4 per cent in both 2026 and 2027. The upswing in overall consumption through the years 2024–2027 is being driven by increasing growth in real disposable income and real wealth, but constrained by higher real interest rates.

Given our projections for income and consumption coupled with forecasts for saving in collective pension funds, the saving ratio level including and excluding share dividends will be around 6–7 per cent and around 2–3 cent, respectively, in the projection period. Our figures mean that the saving ratio, both including and excluding share dividends, will then be fairly close to its average annual level in the period 2010–2019.

Higher rise in house prices in the years ahead

According to Statistics Norway's resale home price index, house prices rose by 1.2 per cent from 2023 Q4 to 2024 Q1. The positive growth was not evenly distributed geographically, being several percentage points higher in Western Norway and the Trøndelag region than in Eastern and Northern Norway. The rise in prices has been far higher than we envisaged before the end of 2023. Despite the high household interest burden, signals that interest rates have probably peaked have reduced uncertainty and boosted activity in the resale homes market. However, real house prices fell by 0.5 per cent in the same period. Supply side developments in the new homes market in recent years, viewed in light of more positive economic prospects for households, could result in higher house prices, but to what extent is uncertain.

Real Estate Norway's monthly house price statistics show that house prices rose through Q1 and into Q2. In each of the first five months of 2024, house prices increased 0.6–0.7 per cent on prices the previous month. Because of the early Easter, sales volumes in March were a good deal lower than usual, while volumes in April were higher than usual. The turnover time is still longer than in previous years. In May, conversely, a record number of sales were registered, the turnover time was somewhat reduced and the number of new homes put up for sale rose markedly towards the end of the month. The Bidding War Index published by Housing Lab measures the share of housing transactions in which sales are preceded by bidding wars, defined as auctions with at least three bidders. The index shows that the share of bidding war transactions in Oslo was 35 per cent in April this year. Such a high share has not been observed since spring 2022, and may indicate that expectations of future interest rate increases have subsided.

In Economic Survey 4/2023 we investigated the significance of the seasonal adjustment of Real Estate Norway and Statistics Norway's house prices indices. In estimating the seasonal effects, greatest weight is placed on the most recent years.

In January 2022 and 2023 changes were made in the regulations to the Sale of Real Property Act and the Mortgage Lending Regulations, respectively. Both may have made positive, non-seasonal contributions to the rise in house prices in the first halves of these years. This makes the seasonal adjustment of the indices in 2024 somewhat uncertain. In 2024 Real Estate Norway changed its method for making seasonal adjustments. Changes of this nature illustrate the uncertainty of house price statistics. In isolation, Real Estate Norway's change in method could imply an increase in the annual price rise of around half a percentage point this year.[6]

Housing investment fell sharply through 2023, and the fall continued into 2024. According to preliminary quarterly national accounts figures, investment fell 5.8 per cent from 2023 Q4 to 2024 Q1. Following the dramatic fall in new housing project starts through 2023, the number for 2024 Q1 is the lowest recorded for the past 25 years. Housing starts are now 22 per cent lower than in 2023 Q1. Since housing starts are a leading indicator of housing investment, we can therefore expect that housing investment as measured in the national accounts will be negatively affected this year and next. The construction industry itself reports little activity in the near term, and it is not very likely that the authorities will offer support measures.

The most recent figures from the Norwegian Homebuilder Association may indicate a turning point. Up until April this year, sales of new homes, a leading indicator for housing project starts, were 6 per cent higher than for the same period last year. However, this is due to high sales figures in April. According to Statistics Norway's price index for new dwellings, the 12-month price rise was down to 2.1 per cent in Q1. Considering only the sub-index for multi-unit residential buildings, i.e. properties with five or more non-subdivided units, prices for these newbuild properties fell by 1.6 per cent. During the same period resale home prices rose by 1.2 per cent. If this tendency continues, sales of new dwellings may pick up further as new dwellings become relatively less expensive. However, it is reported that developments in new housing project starts up to and including April were marginally lower this year than in the same period last year. According to Statistics Norway's construction cost index for residential buildings, the 12-month rise in prices for construction materials rose to 4.6 per cent in April. This, coupled with the fact that access to credit for home builders is limited by the weak sales of new dwellings, causes us to adhere to our previous projection for housing investment this year, namely a fall of about 15 per cent. We envisage that the rate of housing starts will follow sales of new homes and generate growth in housing investment next year already.

In our forecasting of resale home prices, we place special emphasis on expected developments in households' debt growth, interest burden and real disposable income, and the interest rate level. We have revised up our projections for debt growth and income somewhat further on in the projection period. These factors point to an upward adjustment of our projection for resale home prices. However, the policy rate is expected to remain high for a good while yet, and real interest rates are expected to increase. The increasing real interest rates will place a definite damper on the rise in house prices. In addition there has been an upward revision of net interest expenses, as mentioned above. As a result, the household interest burden has been revised up further compared with the previous report, and in isolation points to weaker movements in house prices. According to the Consumer Confidence Indicator published by Finance Norway, households are now more optimistic about the future. The housing market barometer of the Norwegian Federation of Cooperative Housing Associations (NBBL) also shows record-high belief among Norwegian households that house prices will rise. Almost 70 per cent of those asked believe that house prices will go up, which is the highest survey result since February 2022. According to the Norwegian Homebuilder Association's forecasts of housing needs, the historically low rate of residential construction will lead to a shortage of dwellings in the years ahead, particularly in central areas. Any renewal of the Mortgage Lending Regulations must take place before the end of 2024, and any amendments with effect from January 2025, such as relaxation of the equity requirements, may be reflected in the demand side of the housing market.

[6] Using Real Estate Norway's new method, an unchanged price level from June and for the remainder of the year results in an annual price rise in 2024 of 2.3 per cent, whereas the annual rise based on the previous seasonal adjustment method will be 1.7 per cent.

Box 2: How do we explain house prices?

The rise in house prices has recently exceeded the figures in our earlier projections. The historically high household interest burden combined with the fall in real wages in recent years has had a surprisingly small impact on house prices. Whereas house prices fell 0.5 per cent in 2023, the overall rise in prices compared with 2021 has been 5.6 per cent according to Statistics Norway's house price index up to and including Q1 this year. In the period to 2027 we expect the price rise to increase by up to 20 per cent, measured in relation to 2021.

This box considers house price developments since 2021 and shows how fundamentals such as disposable income and debt, the domestic price level, interest rates and housing investment have affected developments. The analysis also shows how these factors are expected to contribute to movements in house prices through the projection period. The analysis was performed with the aid of the KVARTS macroeconomic model; see Boug et al. (2023). The theoretical and empirical properties of the KVARTS housing module are based on Anundsen and Jansen (2013) and Boug et al. (2024). In order to consider the effects of these factors in isolation, we assume that the krone exchange rate, fiscal policy and developments in the global economy remain unchanged.

The figure shows historical and projected house price developments from 2021 to 2027 (yellow line), and how these developments can be decomposed into four main factors: household disposable income and debt (green columns), consumer prices (grey), interest rates (dark blue), and housing investment (red).[1] The black line shows the combined net contribution of the four main factors.

House prices are determined by the interplay between demand for and supply of dwellings. As with other goods and services, household's ability to pay will influence housing demand. Ability to pay is largely determined by disposable income and access to loans secured on dwellings. Historically, productivity growth and terms of trade gains have resulted in higher income and a higher debt level for Norwegian households, which has contributed to maintaining a positive house price trend.

The green columns in the figure show that a gradual increase in household disposable income and mortgage loans compared to the 2021 level is reflected in a similar gradual increase in house prices. The income effect increases over time, as we expect strong growth in disposable income as a consequence of high wage growth and lower interest rates in the years ahead. The increase in disposable income, as the figure shows, is the primary driver of rising house prices.[2]

The general rise in prices for consumer goods and services also influences house prices. When prices for consumer goods increase, housing becomes relatively cheaper. At the same time, higher inflation may lead to an upward adjustment of household expectations regarding future price increases. As buyers wish to secure a dwelling before prices rise, this may lead to increased willingness to pay. In periods with lower mortgage rates than inflation, such as in 2022 and 2023, borrowers have an economic benefit: the gain on repaying the loan with money that is worth less exceeds the cost of the interest. All else being equal, these factors will push up demand in the housing market in the short term.

Conversely, in the longer term consumer price inflation will reduce real disposable income. Ability to pay will be reduced and housing demand will therefore be lower. The grey columns in the figure show that the increased consumer price level is expected to push housing growth down in the years ahead.[3]

The interest rate level is another important factor that plays a large part in house price developments. An increase in interest rates reduces house prices by raising borrowing costs and by reducing household disposable income. Depending on the model and the period forming the basis, the estimated decline in house prices as a consequence of a persistent 1 percentage point increase in the interest rate level varies between 10 and 15 per cent, all else being equal; see Anundsen and Jansen (2013), Anundsen (2019) and Boug et al. (2024). This effect is somewhat higher than in other countries, probably due to higher aggregate household debt with floating interest rates in Norway, which makes Norwegian house prices more sensitive to interest rate increases.[4]

After reducing the key policy rate to 0 per cent during the pandemic, Norges Bank has increased the policy rate by 4.5 percentage points since 2021 to combat the high inflation. The average mortgage rate has increased correspondingly, and in mid-June this year was over 6 per cent. Going forward, we expect the policy rate to be gradually reduced, and that mortgage rates will be under 5 per cent in 2027. At the same time, we assume that real interest rates will remain well over the average for the past 10 years. Frequent interest rate changes, coupled with the fact that the impact of the interest rate on the economy comes with a time lag, makes it difficult to quantify the effects of monetary policy on house prices.

However, the dark blue columns indicate that interest rate changes in isolation will push down house prices in 2027 by 30 per cent relative to the 2021 level. Mortgages rate will then be 2.4 per percentage points higher than at the end of 2021.

Like prices for other goods and services, house prices will depend on both demand and supply. A special feature of the housing market is that the supply is virtually non-elastic in the short term.[5] The housing stock today is determined by decisions made several years ago, and housing investment in a year only accounts for around 5 per cent of total housing wealth.

[1] In order to estimate the isolated effects, we calculated different combinations of these factors and the contributions of each combination by allowing the level of the variables associated with each factor to remain unchanged from the 2021 level. With a total of 24 combinations based on four factors (disposable income and debt, consumer prices, interest rates and housing investment), we derived the magnitude of the composition effects and the unique contributions from each individual factor. We distributed the composition effects equally among the four contributory factors. In combinations where the interest rate is not set equal to the level in 2021, we assume that developments in the interest rate are the same as in the projection scenario.

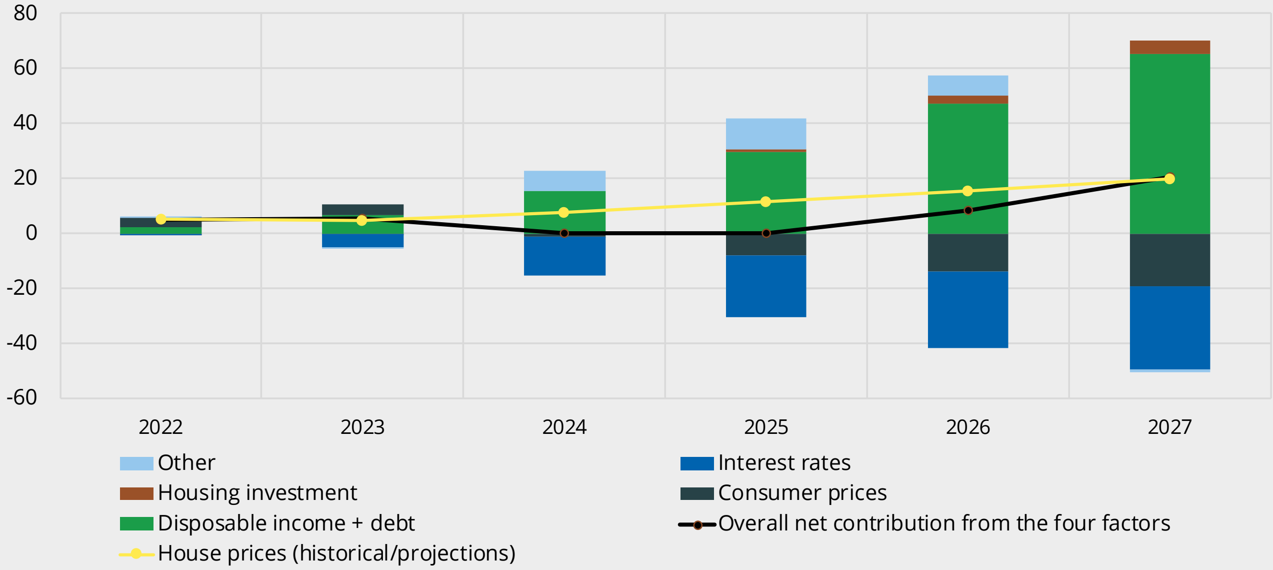
[2] Towards the end of the projection scenario, changes in disposable income will account for 60 per cent of the increase in house prices. This must be viewed in light of an increase in disposable income in the projection scenario of around 35 per cent from 2021 to 2027, and the fact that in the longer term income elasticity lies in the range 1.5–4; see Jacobsen and Naug (2005) and Boug et al. (2024).

[3] Higher inflation will also cause wage growth to increase. The effect of this on house prices is part of the changes in disposable income, shown by green columns in the figure. Grey columns show the effect that can be attributed solely to the increase in consumer prices.

[4] Aastveit et al. (2023) estimate that for the US, a 1 percentage point increase in the interest rate leads to a 5–10 per cent fall in house prices, depending on the period considered.

[5] Anundsen and Jansen (2013) argue that housing stock adapts slowly and can therefore be regarded as constant in the short term. In a panel study of OECD countries, Caldera and Johansson (2013) show that in most countries house prices are unaffected by the housing stock in the short term.

Decomposition of contributions to house price developments
Deviation from 2021 level in percent



Source: Statistics Norway

Since 2022 there has been a marked reduction in the number of housing project starts, which may be attributed to both higher construction costs and lower demand for new dwellings. Although the fall in housing investment was record high through 2023, it has thus had relatively little impact on total capital stocks, and it takes time for lower capital stocks to be reflected in higher house prices. This is illustrated by the red columns, which show that the fall in housing investment will first have an effect on house prices in 2025. In the longer term, however, higher house prices could provide a stimulus for more new housing projects, which in turn might dampen the rise in prices.

Although household disposable income, inflation, interest rates and the supply side of the housing market may explain much of house price developments, other factors also contribute (light blue columns). Regulation of the housing market, changes in lending regulations, moving patterns and household expectations are factors that influence house price movements. For example, communication from Norges Bank on future interest rate changes could influence households' evaluation of their own financial situation and future financial room for manoeuvre, even before interest rates change. This may affect decisions on the purchase and sale of dwellings. Expectations may also be based on incomplete information, and be influenced by what appears in the media.[6, 7]

Changes in expectations, regulations and moving patterns mean that housing market forecasts are particularly uncertain in the short term. Although house price movements from month to month and from year to year often provide surprises, a large part of trend developments can nonetheless be explained by a few fundamental factors. The projections in this report are based on the assumption that historical relationships will continue to apply in the years ahead.

[6] Shiller and Thomson (2022) show that household expectations regarding future house prices can be largely explained by current house price movements. Using the same data, Aastveit et al. (2023) show that the formation of household expectations is different when house prices rise from when they fall. In periods with rising prices, households expect prices to continue increasing. The authors show furthermore that when house prices fall, households also expect them to rise.

[7] See Larsen et al. (2021) for a study of the significance of the media for household expectations.

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Many forecasting institutions have revised up their house price projections recently, to a level somewhat higher than ours. Expectations of higher prices may stimulate demand for homes in the current market, which in turn may lead to higher prices. However, taking account of factors of this nature in our model projections is challenging, and there is therefore great uncertainty associated with house price projections. We have allowed our modelling of the housing market in our KVARTS model to play a large part in our forecasting. Box 2 provides a decomposition of house price drivers since 2021.

We are revising up the projections for 2024 and 2025 to around 2.5 and 3.5 per cent, respectively. In the last two years of the projection period we forecast a total rise in house prices of about 7 per cent. Our projections imply a rise in real house prices next year already.

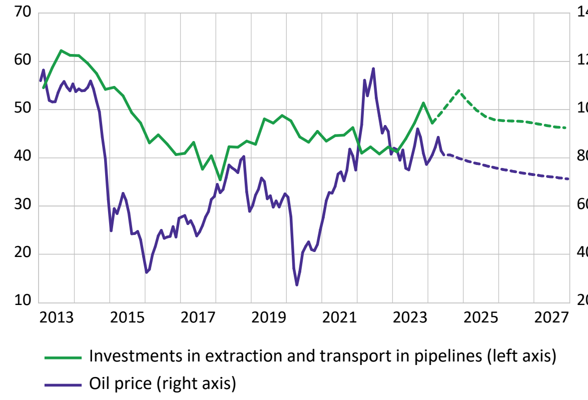
Growth in petroleum investment this year and a moderate decline the next two years

Following 14.3 per cent growth in 2019, petroleum investment fell for the three following years. In 2023 this reversed into an investment upturn of as much as 10.6 per cent. After three consecutive quarters of clear growth, investment in 2024 Q1 fell by 8.1 per cent, more sharply than forecast in our previous report.

Investment in Q1 this year was 14.6 per cent higher than in Q1 last year. The upswing was driven by higher investment in production platforms, rigs and modules. Investment prices increased by 7.1 per cent in Q1 compared with the same quarter last year. This is a decline compared 2023 Q4, when investment prices increased by 9.7 per cent.

The fluctuations in petroleum investment are very largely driven by investment in offshore developments. The other main categories have either exhibited more stable development or investment levels are too small for variations from year to year to significantly affect aggregate petroleum investment. The Storting package of tax measures that was adopted in June 2020 to help the industry cope with the sharp fall in the oil price early in the Covid pandemic, coupled with high oil and gas prices, has triggered a very large number of new developments on the Norwegian continental shelf. This led to marked growth in investment through 2023. We assume that the level of activity stemming from these developments will remain high through 2024 as well. The carry-over from last year will therefore ensure clear annualised growth this year too. Following a lower than normal addition of new developments in 2023 and this year, growth is expected to pick up more in subsequent years. The fall in investment expected for the next few years, a consequence of declining investment activity in existing projects, will be slowed by these new additions.

Figure 12. Petroleum investments and oil price
Seasonally adjusted. Left axis: billion 2021 NOK, quarter
Right axis: USD per barrel



Source: Statistics Norway

The petroleum companies' investment plans for the current year and next year are surveyed in [Statistics Norway's quarterly investment intentions survey (KIS).](#) In the most recent survey, from May, the nominal projection for 2024 is NOK 247 billion, which is marginally higher than the projection in the previous survey in February. A new development project has been added since the previous survey. The projection for 2024 is 25 per cent higher than the corresponding one made for 2023.

Investment in 2023 ended up a full 8.8 per cent higher than the projection for 2023 published a year ago, with which we now compare the current projection for 2024. Historical figures from the last 21 years show that the projection for the year published in May of the investment year has on average been 2.4 per cent lower than the final figure, and in none of those years, apart from 2023, has the final figure been as much as 8.8 per cent higher than the projection published in May.

We assume that there will be moderate investment in 2024 in projects for which PDOs have not yet been submitted, and which are therefore not yet included in the survey. Previous experience indicates that there is a risk of some of the ongoing developments incurring somewhat higher costs than those in the current investment plans. On the other hand, there is also a risk of not all the investments planned for this year being completed, and having to be postponed until next year. The surprisingly low investment in Q1 this year increases this risk, as the investments planned for Q1 have now been rolled over onto the projections for the remaining quarters of 2024. Overall, investment looks set to increase by a nominal 16 per cent this year. Assuming a price rise of 6 per cent, this will result in a 10 per cent growth in volume. We are revising down the growth in volume by 1 percentage point, mainly because the Q1 figures were weaker than expected.

The projection in the most recent survey for total investment in oil and gas activities in 2025 is NOK 216 billion, which is about 5 per cent higher than the projection published in February. It is a full 19 per cent higher than the corresponding projection for 2024 published a year ago. The projection for 2024 has increased by as much as 36 per cent from the projection for this year published in 2023 Q2 to the figure published in this survey. Such an increase from a projection published in May prior to the investment year to May of the investment year has not been seen since 2008 with the exception of 2023, when the increase in the growth projection was a whole 51 per cent. However, the increase in the 2023 projection was artificially high because the projection published in May prior to the investment year did not include figures for the many developments that were not included until 2023 Q1. There are no such artificial grounds for the strong growth in the projection for 2024. The increase is related to the high inflation through 2023, largely as a result of the depreciation of the krone. Planned investment has also increased because some developments were brought forward. There has also been a cost increase over and above the rise in prices, for example because projects have required more investment activity than planned previously. The reasons for the strong increase in the projection in the survey for 2024 do not appear to exist to the same degree for 2025. The rise in prices for intermediate inputs looks likely to be lower this year than last. Nor is there any reason to expect any bringing forward of investments other than those reported last year. It is also necessary to take into account cost increases for individual projects, but probably not as much as for the 2024 projections.

We assume that there will be some investment in 2025 related to developments for which PDOs have not yet been submitted, and which are therefore not included in the survey. Investment in 2025 in some of the other categories, particularly fields in operation, is assumed to be higher than the figures in the last survey. All in all, it is assumed that the projections for 2025 will increase less than was the case in the survey for 2024. We forecast that investment in 2025 will fall by 2 per cent, about one percentage point less than in our previous report. As we have reduced growth this year by 1 percentage point, the forecast investment level for 2025 is approximately as in the previous report.

Falls of 4 and 2 per cent are forecast for 2026 and 2027, as in our previous report. We assume that the large Wisting development project will be included from the end of 2026, and hence contribute to dampening the decline in 2027. This would bring the investment level in 2027 back to roughly the same level as in 2019.

In Q1 this year, oil and gas extraction was 3.7 per cent higher than in the same period last year. Liquid production increased by 2.8 per cent, while gas production increased by 4.5 per cent compared with 2023 Q1. The Norwegian Offshore Directorate forecasts that extraction this year will be at about the same level as last year. Petroleum production is expected to increase by 4.2 per cent in 2025 before falling gradually through the remainder of this decade.

Flat developments in business investment despite power supply gathering pace

According to preliminary national accounts figures, business investment rose by a full 17.1 per cent in 2022 and 4 per cent in 2023, to a historically high level. Growth was particularly strong in manufacturing and in mining and quarrying, at 15.2 and 16 per cent in those two years. However, the trend reversed in mid-2023, and the sector as a whole reported negative growth in 2024 Q1. Investment in manufacturing, mining and quarrying fell by 7.3 per cent, while other goods production and other services dipped 3.8 per cent.

Businesses in manufacturing, mining and quarrying, power supply and oil and gas report regularly to Statistics Norway's investment intentions survey on planned and completed investment. The most recent projections for 2024 and 2025 show that investment in power supply will increase substantially, as was also pointed out in our previous report. The main cause of the strong growth is an unusually high level of investment in the transmission and distribution of electricity. Going forward, large offshore wind projects with government support may help to maintain the investment level high in the years ahead as well.

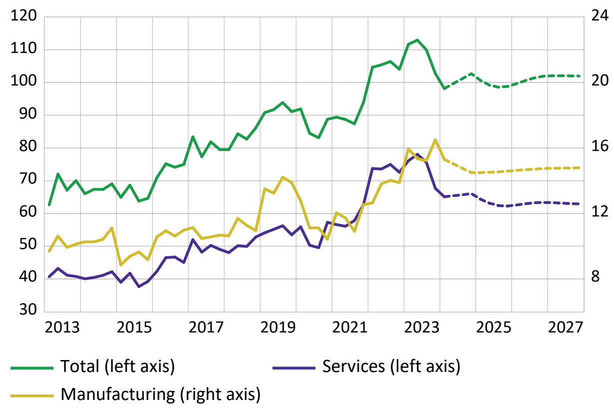
Businesses' forecasts for investment in manufacturing, mining and quarrying still indicate an annualised average decline in 2024. Although the projection indicates a decline, the investment level will still be high in a historical perspective, following the strong growth in the two previous years. Businesses forecast an upturn in 2025, which may indicate that major investment projects will not start until next year. This can be viewed in light of the fact that a number of businesses that report to Norges Bank's survey of business prospects (Norges Bank's Regional Network) indicate that they are postponing investment decisions because of high investment and financing costs.

Norges Bank's report also shows that service providers and wholesale and retail trade report reduced investment this year and investment at about the same level next year. The high interest rate level, expectations of lower prices for investment products and weaker demand are factors underlying the postponement of investment decisions.

According to our projections, overall business investment will fall by about 8 per cent this year, i.e. somewhat more than forecast in our previous report. We forecast a sharper fall than previously because several industries reported weaker Q1 developments than we foresaw in our previous report. We have revised down our projection for manufacturing, mining and quarrying for this year by around 2 percentage points, to a decline of just over 5 per cent, but reduced the forecast decline in 2025 by around 3 percentage points, to just over 2 per cent. In light of the reported growth in power supply investment, we are revising the projection for this industry up somewhat, for both this year

Figure 13. Investments Mainland Norway

Seasonally adjusted, billion 2021 NOK, quarter



Source: Statistics Norway

and next year. In isolation, rising real interest rates will depress the investment level going forward, while increased economic activity will exert upward pressure on it. On balance, business investment is expected to remain at the current level in the years up to and including 2027.

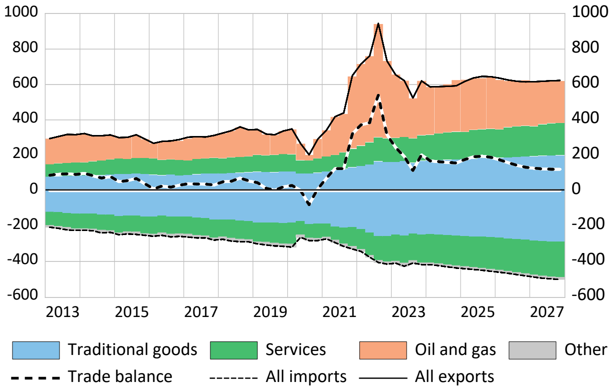
Oil and gas exports will keep the trade surplus large

Following a strong fourth quarter in 2023, the external account faltered in Q1 this year, because oil and gas exports declined in both volume and price. 2024 Q1, excluding trade in oil and gas, was more positive. Both the volume and the export value of traditional goods and services increased a little, while the value of imported goods and services remained more or less unchanged. A small increase in the volume of imports was offset by a slight price reduction. Mainland Norway thereby reduced its trade deficit. But the weakening of oil and gas exports meant that the surplus on all foreign trade was reduced by about NOK 34 billion in 2024 Q1.

In traditional goods and services, high-value subgroups have grown most in terms of both overall volume and the price index. An over 15 per cent increase in exports of basic metals contributed most, adding about 2 per cent of growth to exports of traditional goods. Service exports increased by 1.7 per cent. The largest contribution came from shipping, which grew by 6.7 per cent. The decline in prices for basic metal exports and for shipping contributed substantially to the small decline we saw in the price indices for traditional goods exports and overall service exports.

Figure 14. Foreign trade

Exports (positive axis), imports (negative axis) and balance of trade
Value (current prices), seasonally adjusted, billion NOK, quarter



Source: Statistics Norway

There were small changes in volume and price for overall imports of traditional goods and services in Q1 this year. Imports of basic metals fell sharply, while imports of basic chemicals and chemical and mineral products increased considerably. For several years, Norwegians' consumption abroad has been more than twice as large as foreigners' consumption in Norway. Both continued to grow in Q1.

We expect no major changes in the balance of trade in the years 2024–2027 compared to our March projection. A weak Norwegian krone will contribute to a lower rise in prices for mainland exports than for imports, thereby strengthening competitiveness. This effect is estimated to be somewhat lower now than in our previous report, as the import-weighted krone has strengthened a little since March. We expect higher growth in mainland exports than is forecast for our trading partners this year and next, which will mean that Norway wins market shares. Exports of oil and gas are expected to increase in pace with production for the first two years before slacking off somewhat.

Whereas mainland Norway has an increasing trade deficit, exports of oil and gas ensure a large trade surplus. This surplus may be reduced in the years ahead if oil and gas prices fall (see Box 1.1 in Økonomiske analyser 2/2024 while Norwegian production and export volumes do not increase, but nonetheless remain at a high level. A growing petroleum fund will add to the income and current transfers surplus. When this surplus is added to the trade surplus, the total – estimated as a share of GDP – is expected to be in the area of 12–18 per cent in the years 2024–2027.

The standstill in the Norwegian economy will soon be at an end

The national accounts showed that mainland GDP growth from 2022 to 2023 was only 1 per cent. The weak growth continued into 2024, with growth of 0.2 per cent from 2023 Q4 to 2024 Q1. Mainland GDP in 2024 Q1 was 0.6 per cent higher than in the same quarter in 2023. Price and interest rate increases have contributed to the relatively weak growth this past year.

Growth in overall GDP, including petroleum production and shipping, was 0.6 per cent from 2022 to 2023 and 0.3 per cent from 2023 Q4 to 2024 Q1. However, prices for oil and gas fell in Q1. This led to overall GDP and exports falling by 1.5 and 5.5 per cent, respectively, measured in current prices.

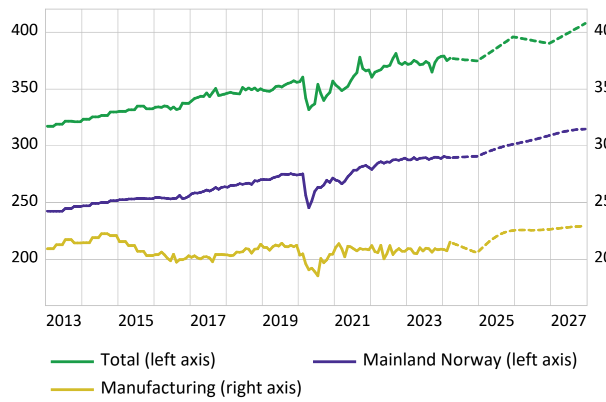
Favourable tax conditions and high oil and gas prices led to the submission of many new applications for field developments in 2022. This has given oil-related manufacturing and services many new assignments in 2023 and 2024. In particular, services associated with oil and gas extraction increased markedly, with growth in 2024 Q1 of 3.4 per cent compared with 2023 Q4 and of 5.4 per cent compared with 2023 Q1.

Manufacturing grew by 1 per cent in 2024 Q1 compared with the previous quarter. Production of metal goods, electrical equipment and machinery increased by 1.2 per cent, shipbuilding and other transport equipment by 2.6 per cent and repair and installation of machinery by 2.3 per cent.

Health and care services and wholesale and retail trade grew by 0.9 per cent and 0.5 per cent, respectively, from 2023 Q4 to 2024 Q1. These are large industries which contributed significantly to pushing up total Q1 growth. The accommodation and food services industry is smaller, but contributed growth of 1.6 per cent.

Value added in in the construction sector fell for the fourth consecutive quarter, with a decline of 0.3 per cent in 2024 Q1 compared with the previous quarter. This is still a relatively moderate decline, bearing in mind the fall in new residential construction, and is attributable to activity in other types of construction remaining fairly buoyant. Value added in fishing and aquaculture fell too, by as much as 4.4 per cent. This is attributable to

Figure 15. Gross domestic product
Seasonally adjusted, billion 2021 NOK, month



Source: Statistics Norway

the decline in the industry due to poor fish health, among other things.

The national accounts figures show that value added in administrative and support services, which includes recruitment agencies, increased by 0.7 per cent in 2024 Q1 after falling sharply through 2023. This is nonetheless 4 per cent lower than in 2023 Q1. The decline may be partly attributable to the rules for labour recruitment being tightened from 1 April 2023.

In the March publication of the survey from Norges Bank's Regional Network it is reported that businesses expect activity to remain virtually unchanged in the first half of the year. The prospects are thus somewhat better than indicated by the previous survey, but there are large differences across industries. Suppliers to the petroleum industry and service providers expect an upswing, while businesses in the other industries foresee a fall in activity. Statistics Norway's business tendency survey for manufacturing, mining and quarrying also reveals expectations of little or no growth in the immediate future. The composite indicator for manufacturing showed no change in Q1. The general assessment of producers of capital and consumer goods regarding prospects for Q2 is positive, while the majority of producers of intermediate products expect the situation to remain unchanged.

The Norwegian economy has been at almost a standstill through the whole of 2023, and this weak tendency has continued so far in 2024. According to our projections, mainland GDP will rise by 0.5 per cent this year, a little lower than forecast in our previous report. However we expect activity will pick up going forward, such that the economy is close to cyclically neutral from 2026.

Unemployment will increase moderately

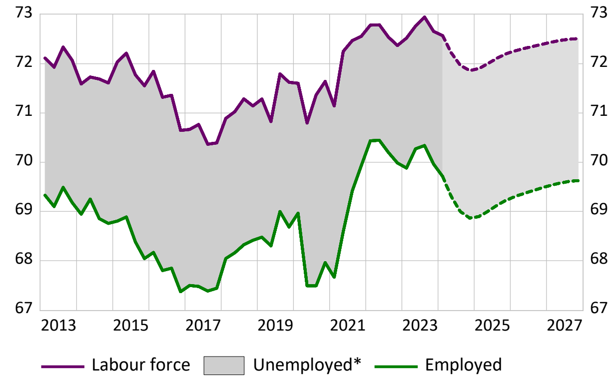
In the past year and a half, unemployment has risen from a low level to one fairly close to the average for the 2010s. Labour force participation is high, but the level has been falling somewhat for the past half year. In the near term, we expect unemployment to rise to a slightly higher level than the current one because of the virtual standstill in economic activity last year and this year. The labour force as a share of the population will fall somewhat going forward, but the share will remain high. Immigration of refugees from Ukraine will increase both the labour force and unemployment, but it is uncertain how strong the increase will be going forward.

According to the Labour Force Survey (LFS), seasonally adjusted unemployment rose from 3.7 per cent in 2023 Q4 to 3.9 per cent in 2024 Q1. This is approximately the same level as before the Covid crisis struck. Unemployment increased weakly through 2023 after lying at a historically low level. According to the LFS trend figure, unemployment increased from 3.6 per cent in autumn 2023 to 4.0 per cent in April. The seasonally adjusted 3-month moving average also exhibited a weak increase during this period, but to a somewhat lower level for the 3-month period February–April. Like the trend figures, this was an increase on the autumn of 2023, but unchanged compared with the previous 3-month period (November–January). The trend figures represent long-term developments, and the greatest uncertainty is associated with the figures at the end of the time series.

The increase in LFS unemployment from 2023 Q4 to 2024 Q1 occurred mainly among persons aged 25 and over. The unemployed in this group accounted for 2.7 per cent of the labour force in 2024 Q1. That too is consistent with the average unemployment rate for this group in the 2010s. In 2024 Q1 LFS unemployment among persons aged 15–24 was 11.4 per cent, and thus roughly unchanged from 2023 Q4. Whereas the unemployment level for this group is normal, employment and labour force participation are at historically high levels.

Figure 16. Labour market status

Percent of population in working age, LFS

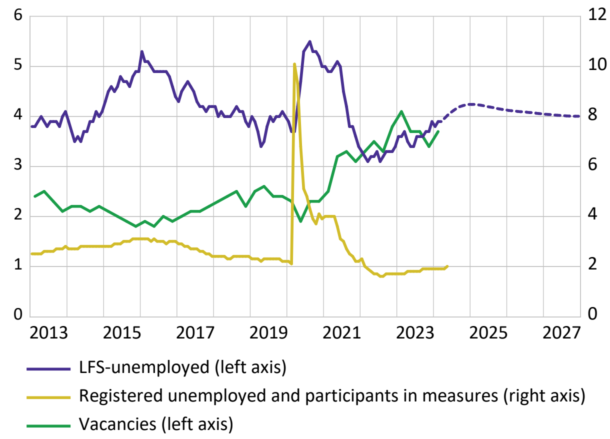


* Unemployment is measured as share of population in working age

Source: Statistics Norway

Figure 17. Unemployed and number of vacancies

Percent of labour force and of the sum of occupied and vacant positions, seasonally adjusted and smoothed



Source: The Norwegian Labour and Welfare Administration and Statistics Norway

Seasonally adjusted registered unemployment as published by the Norwegian Labour and Welfare Organisation (NAV) increased to 2.0 per cent in May after lying at 1.9 per cent for the previous eight months. The NAV figures are based on a total count of all those registered as fully unemployed by NAV, while LFS figures are based on responses to an interview with a sample of the population. The same underlying criteria form the basis for the definition of being unemployed in the two sets of statistics. Some individuals who are registered with NAV as fully unemployed are not classified as LFS unemployed because they do not state that they are looking for work. Conversely, the LFS picks up unemployed who do not register with NAV, for example because they do not have a right to unemployment benefit. The difference in developments between registered and LFS unemployment recently is probably attributable to unemployment increasing in groups with low incentives to report themselves to NAV as unemployed.

In 2024 Q1, 69.7 per cent of the population was employed, down from 69.9 per cent in 2023 Q4. This is high in a ten-year perspective, nonetheless. Seasonally adjusted LFS figures show that the number employed edged down by 0.1 per cent from 2023 Q4 to 2024 Q1, after a similar decline from Q3 to Q4 in 2023. For most of 2023, the LFS figures showed an increase in the number employed. There was a 0.7 per cent increase in the number employed from 2023 Q1 to 2024 Q1.

Employment has increased in recent years among immigrants, i.e. residents born abroad with foreign parents and grandparents. From 2023 Q1 to the same quarter in 2024, the number of employees classified as immigrants increased by 4.0 per cent. By way of comparison, the number of registered resident wage-earners not classified as immigrants increased by 0.2 per cent in the same period.

In 2023, 33 100 Ukrainian citizens immigrated to Norway. Immigration figures are expected to be slightly lower in 2024, but there is great uncertainty associated with the projections. Roughly a third of the immigrants from Ukraine were under 20 years old. According to figures from Statistics Norway's statistics on number of jobs and earnings, 8 400 immigrants from Ukraine who immigrated after the outbreak of the war in 2022 were in work and received wages in April 2024. They accounted for approximately 20.8 per cent of Ukrainians aged between 20 and 66 who have immigrated since the outbreak of the war. The low participation rate is partly due to the fact that many take part in the introduction programme for newly arrived refugees before they look for work. NAV reports that over half of those registered as fully unemployed or job-seekers on NAV programmes at the end of May have immigrant backgrounds, and that Ukrainians (7 100 persons) now make up the biggest group. It takes some time before the immigration from Ukraine is reflected in the LFS figures, because refugees who live in asylum reception centres or other forms of non-private households are not included in the survey.

The national accounts show growth in both employment and hours worked. Employment increased by 0.3 per cent from 2023 Q4 to 2024 Q1, while hours worked increased by 0.5 per cent. The increase in employment was slightly larger than in the previous three quarters, but lower than through 2022. Employment in Q1 this year was 0.6 per cent higher than in the same quarter of 2023. Hours worked were 3.0 per cent lower, however, but this is attributable to Easter occurring in March, and thus in the first quarter of 2024.

Hours worked in administrative and support services increased by 0.4 per cent from 2023 Q4 to 2024 Q1 after falling through the whole of 2023. Hours worked in construction fell by 0.3 per cent in the same period, but are still at a markedly higher level than in 2019. Whereas residential construction has fallen, other construction segments have remained buoyant. Administrative and support services include recruitment of labour for other industries, such as construction. The labour recruitment rules were tightened in April 2023, but it is unclear how much effect this has had. It is clear, however, that it has affected recruitment in clerical and blue collar occupations. The new rules may have resulted in workers moving from administrative and support service activities to construction work.

The number of foreign commuters (non-resident wage-earners) fell by 5.8 per cent from 2023 Q1 to the same quarter in 2024, to 79 000 persons. This level is still higher than the average for Q1 of the years 2016–2019. The number who commute to work in Norway is influenced by the economic situation in Norway and in the countries they come from. Wage-earners from the countries that have joined the EU since 2004 have been and remain the dominant group of foreign commuters since 2014.

According to seasonally adjusted LFS figures, the number of persons in the labour force increased through most of 2023 to a historically high level, whereas since 2023 Q3 there have only been small changes from one quarter to the next. The labour force measured as a percentage of the population, i.e. the labour force participation rate, was 72.5 per cent in 2024 Q1. This is down somewhat compared with the latter half of 2023, but high in a historical perspective.

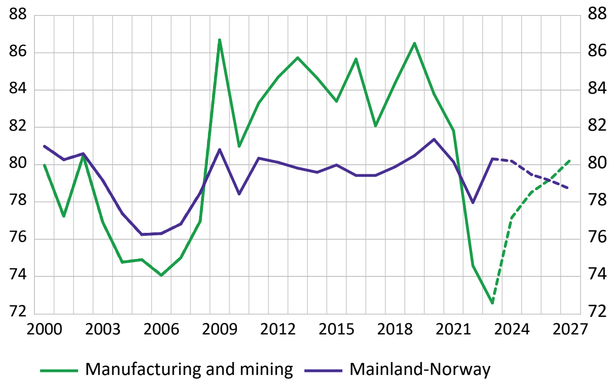
Demand for labour was high in 2021 and 2022, but fell through 2023. According to Statistics Norway's survey on job vacancies, the level in 2024 Q1 was slightly higher than in 2023 Q4, but the same as in Q2 and Q3 that year. Statistics Norway publishes figures on the stock of job vacancies, while NAV publishes figures on new vacancies. According to seasonally adjusted NAV figures, the number of new vacancies has fallen somewhat so far this year, but the addition of new vacancies is still higher than the average for 2023.

The labour market has been tight through 2022 and 2023. We forecast almost unchanged employment growth in 2024. An expected increase in labour productivity from an abnormally low level will contribute to keeping employment growth low for the remainder of the projection period, up to and including 2027. We expect immigration of asylum-seekers from Ukraine to add to both the labour force and unemployment in the projection period. How pronounced the increase will be is uncertain, with respect to both how many new immigrants will come and how many will return home in due course. We have used Statistics Norway's population projections as a basis, and hence assumed that about 20 000 Ukrainians will come to Norway in the course of 2024 followed by a further 10 000 in 2025. Employment will not keep pace with the increase in the working age population, with the result that the employment rate will fall a little. We expect unemployment to continue increasing somewhat, particularly in construction. We forecast that unemployment will end at 4.1 per cent in 2024. We then expect it to rise a little further in 2025 before edging down again and remaining at close to 4 per cent up to 2027. The labour force will grow weakly in 2024 and through the remainder of the projection period.

Real wage growth going forward

After mediation by the National Mediator of Norway, the Federation of Norwegian Industries (Norsk Industri) and the United Federation of Trade Unions (Fellesforbundet) reached agreement on a norm of 5.2 per cent for annual wage growth in 2024 in overall manufacturing under the Confederation of Norwegian Business and Industry (NHO). For manufacturing workers, who account for over half of full-time equivalents in businesses under the NHO, the wage carry-over into 2024 will contribute 1.6 percentage points, while for clerical employees in manufacturing it will contribute 1.8 percentage points. The centrally negotiated pay increases for manufacturing workers are estimated

Figure 18. Wage share
Calculations based on factor income adjusted for income of self-employed, percent



Source: Statistics Norway

to contribute 2.2 percentage points, while the majority of clerical workers in manufacturing will only receive locally negotiated pay increases. The remainder of the projected annual wage growth in manufacturing is wage drift, defined as the sum of all factors that influence annual wages other than the contributions from carry-over and pay increases, including the outcome of local wage negotiations.

Growth in average monthly basic earnings in 2024 Q1 compared with the same quarter last year was 6.1 per cent, while wage growth for persons with the same job the previous year was 6.8 per cent in the same quarter. Following high growth in 2023 Q3, growth in average monthly basic earnings has thus slowed somewhat.[7] Of the major industries, administrative and support services and education pushed up average growth in 2024 Q1, with growth of 8.2 per cent and 7.0 per cent, respectively. However, Q1 growth figures for average monthly basic earnings in wholesale and retail trade and manufacturing were 5.6 and 5.3 per cent, respectively, thereby pushing down the average growth rate.

The high growth in education sector pay in 2024 Q1 must be viewed in light of weak growth in 2023 Q1 as a consequence of the wage settlement for 2022 for many wage-earners in education not being included in the statistics until 2023 Q2.[8] This accordingly resulted in similarly high growth in average monthly basic earnings for the education sector in 2024 Q1. The level of wage growth in administrative and support service activities can be viewed against the backdrop of a reduction in the number of wage-earners in the temporary employment sector because of new rules for the use of contract labour applying from 1 April 2023.[9] The change in the composition of wage-earners in this industry may have helped to push up wage growth for administrative and support services in 2024 Q1.

For the past two years, the labour costs share, which is a measure of the percentage of value creation in the economy that accrues to the workers, has been less than the average of 82.2 per cent in the period 2009–2021 for manufacturing. According to the preliminary national accounts, the labour share for manufacturing is estimated to be 71.6 per cent in 2023. We forecast that it will pick up to about 77 per cent in 2024 and up further to around 80 per cent at the end of the projection period. The upward revision since the last economic report is due to both higher forecast growth in disbursed wages than previously and a downward adjustment of forecast operating results in the near term.

We maintain our projection for annual wage growth for 2024 at 5.2 per cent, as in the previous report, and then expect nominal wage growth to fall somewhat in the years ahead. There is uncertainty associated with the projections. The low labour cost share is a factor pushing up wage growth, while rising unemployment is reducing the pressure on wages. The unchanged projection for annual wage growth this year and downward revision of the projection for CPI inflation mean that real wages are estimated to be somewhat higher than in the previous report. In the near term, we expect a gradual reduction in CPI inflation to 2 per cent and hence growth in average real wages of just over 1.5 per cent leading up to 2027.

Inflation is slowing

The annual rise in the consumer price index adjusted for tax changes and excluding energy products (CPI-ATE) rose almost continuously from 1.3 per cent in January 2022 to a peak of 7.0 per cent in June 2023. The rise in prices has slowed since this peak, and came down to 5.3 per cent in January. Since then it has gradually declined further to 4.1 per cent in May. The path of underly-

[7] See Skjæveland, M. H. and Bye, K. S. (2024): Lavere vekst i månedslønnen [Lower growth in monthly pay].
[8] See discussion in *Economic Survey* 3/2023.

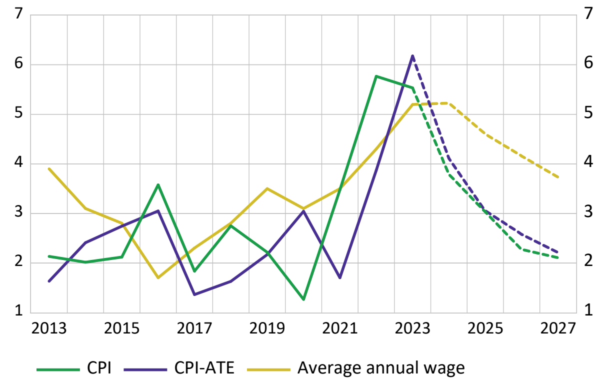
[9] See Berge, C. and Edelmann, F. S. (2023): Færre lønnstakere i utleie av arbeidskraft [Fewer wage-earners in temporary employment activities].

ing inflation in recent years is largely attributable to the global market situation. Global inflation escalated after the pandemic. The outbreak of war in Ukraine in February 2022 accelerated the rise in prices in global commodity markets. Whereas global consumer price growth fell markedly last year, a pronounced depreciation of the krone in spring 2023 was reflected in Norwegian inflation. The krone strengthened again after the especially weak period in spring 2023, and contributed to a limited rise in the overall price level through the second half of 2023. This led to the 12-month rise in the CPI-ATE slowing for the remainder of the year. Businesses price changes into their underlying costs over time, and there are considerable time lags before changes in import prices, wages and energy costs feed fully through into consumer prices. Prices in the first half of the year were expected to increase less this year than last, and contribute to a continued slowing of the 12-month rise in the CPI-ATE. Inflation has nonetheless been lower in recent months than expected earlier this year, which is why we are now revising down the projection for annual CPI-ATE inflation for 2024 by an annualised 0.2 percentage point.

Energy prices have developed approximately as expected in the previous report. The May thaw led to a sharp increase in unregulated power production, and spot prices on the NordPool power exchange fell markedly. Except in Northern Norway, the thaw also led to reservoirs at the beginning of June reaching record levels for this time of year. However, the warm weather in May brought the energy content of the snow reservoirs down to almost the minimum level for the last 20 years, so that at the beginning of June the overall hydrological balance was weaker than last year. In the forward market, electricity futures contracts in the Nordic market exhibit a relatively steady rise in price from the summer and into the winter. The market does not price in a repeat of the extreme weather in autumn 2023, when extreme quantities of precipitation and a lot of wind led to high unregulatable power production and very low electricity prices. We assume that the electricity price including grid charges will be a good deal higher this coming autumn than it was last year, and that in isolation this will add more to annual CPI inflation than to CPI-ATE inflation in these months. So far this year the 12-month development in energy prices has been negative, leading to annualised CPI inflation being lower than

Figure 19. Consumer price indices and annual wage

Change from previous year in percent



Source: Statistics Norway

CPI-ATE inflation. The 12-month rise in the CPI was 4.7 per cent in January and as low as 3.0 per cent in May, when household electricity prices, including grid charges, fell by a full 24 per cent compared with May 2023. Overall, energy prices reduced inflation by 1.1 percentage points last month. The price developments that form the basis for energy prices in this report imply a weak fall in prices for energy products as a whole as an annual average. As in our previous report, we forecast that energy products will reduce CPI inflation in 2024 by 0.3 percentage point. In our March economic report, CPI and CPI-ATE inflation were projected to be 4.0 and 4.3 per cent, respectively, for 2024. The downward revision of CPI-ATE inflation is also reflected in lower CPI inflation, so that the projections for both measures of inflation are revised down by 0.2 percentage point. In this report, we forecast that CPI and CPI-ATE inflation will increase by 3.8 and 4.1 per cent, respectively, in 2024.

According to the consumer price index (CPI), prices for food and non-alcoholic beverages rose rapidly from January up to and including July 2023. After peaking in July, they then fell in the second half of 2023. In January 2024, the price level was still lower than the peak in July 2023. A surprising fall in prices for food and non-alcoholic beverages from January to February this year was followed by a further sharp fall in March in connection with special Easter offers. In recent months prices have risen again, but not until May did they again reach the level in July last year. The year-on-year rise in prices has remained high because of the relatively low price level for the product group at the beginning of last year. The rise was 8.7 per cent in January, and in May had fallen to 5.4 per cent. Given an expected moderate rise in prices for food and non-alcoholic beverages up to the summer, the year-on-year rise for this product group is likely to decrease further up to July.

Given their weight of about 12 per cent in the consumer price index, developments in prices for food and non-alcoholic beverages have a strong bearing on developments in the CPI. The weak rise in prices so far this year is thus a factor contributing to our downward revision of general inflation projections for 2024. Norwegian agriculture is sheltered, but the shelter has lessened over time. Trade with the EU has gradually expanded through the EEA Agreement, and duty-free quotas have increased markedly since 1990. Both Norwegian and international conditions have a strong bearing on further movements in food prices. The Government has reached agreement with the farmers' unions on a new agricultural agreement for the coming year. The agreement implies an overall increase in potential income for 2024 and 2025 of just over NOK 3 billion, with NOK 627 million covered through increases in target prices. The remainder of the income frame is expected to be met largely through higher transfers over the government budget, which will not be reflected in the rise in prices. According to the final records from the negotiations meeting between government and farmers' unions, the isolated impact of increased commodity prices reflected in consumer prices, including the forecast for goods without a target price, is 0.5 percentage point of the price index for food and non-alcoholic beverages. This implies an increase in the overall CPI of a bare 0.1 percentage point, which is in line with the calculated inflationary effects of last year's agricultural settlement. Through the EEA Agreement, developments in prices for food products in Europe and the price of the euro are important factors in inflationary developments. Naturally occurring factors also play a part. Last year's crop yields were lower than in a normal year in both Norway and Europe. Southern Europe was hit by drought, while in Northern Europe there was heavy precipitation during the harvest period. The global price of fertiliser has fallen by a further 30 per cent in a year, thereby lessening the cost rise in agriculture. A lower rise in packaging prices globally has curbed the increase in costs in the food industry. It is difficult to forecast inflation going forward. Wage growth affects production costs in the food industry, wholesale and retail trade and transport. The fall in prices for packaging and electricity has now probably been largely passed through into end-user prices. In our projections, we have assumed that the annual rise in prices for food and non-alcoholic beverages will reach a temporary trough this summer, and that we will not experience the same fall in prices as in the second half of last year. The 12-month rise in prices will then pick up again somewhat towards the end of the year.

Developments in prices for the group alcoholic beverages and tobacco products are far more stable than for food. AS Vinmonopolet revised its prices by 0.2 per cent from 1 May, which was described as unusually low. After falling from April to May, the 12-month price rise for this product group was lower last month than at the beginning of the year. The year-on-year price rise in May was 4.0 per cent, and we have based our projections on a stable rise in prices for the product group alcoholic beverages and tobacco products for the remainder of the year. Special taxes make a large contribution to dampening the fluctuations in underlying producer prices for this product group, which has a weight of 4 per cent in the CPI.

According to the CPI-ATE by supplier sector, it is developments in prices for goods that have pushed down underlying inflation in the past three months, while the rise in prices for services has been stable since February, with a year-on-year rise in the range 4.5–4.7 per cent. Prices for imported goods, with a weighting of 35 per cent in the CPI-ATE, have made a particular contribution to the reduction. We assume a continued stable rise in prices for services through the year, while the rise in goods prices is forecast to slow further.

Furniture and household equipment are a consumer group with a large import content which saw a high rise in prices in both 2022 and 2023. This was due to a high rise in prices in commodity markets globally coupled with a weakening of the exchange rate, and this was passed through into end-user prices. The rise in prices for this product group was very high in 2023 Q1, but has been low since April 2023. The 12-month rise fell from 7.0 per cent in January 2024 to 2.7 per cent in May, while the price level changed little in this period. We assume generally that the year-on-year rise in prices for import goods will be far more stable in the second half of 2024 than in the first half, when the falling rates largely reflect the high rise in prices through the first half of 2023.

According to the CPI-ATE, the rise in the rental index has been stable at a high level, with a 12-month rise in the period January-May in the range 4.3–4.6 per cent. Given increased interest rates, high population growth and high demand for rental housing, the rise in rents as an annual average is expected to increase further compared with last year. In the CPI, actual rent paid by tenants is derived from the rent survey. The rent survey aims to capture price changes in connection with entry into new rental contracts, while prices in existing contracts are largely adjusted according to the CPI. Imputed rent for owner-occupiers is derived from developments in the rental market adjusted for the geographical composition of the housing stock. In our projections, we assume that the rate of the increase in rents will remain high through the current year. Given lower CPI inflation and a fall in interest rates, the rise in rents may slow. A continued shortage of rentals has a countering effect. Overall, rents account for more than 20 per cent by weight of the CPI-ATE. The rise in rental prices will probably have to slow if inflation is to come down towards the inflation target in the medium term. We have made this assumption the basis for our projections, with rents largely mirroring CPI inflation.

Developments in prices for other services largely follow movements in domestic costs, with wage growth one of the key cost components. Price movements are adjusted for special factors, such as the Storting decision that the maximum price for parents’ contribution to day-care centres is to be changed from 1 August 2024. The monthly rates for parents’ contribution will be cut from this date, slightly reducing the rise in the CPI-ATE for this service group.

In the financial market, annual contracts for Nordic power for the years 2025–2027 have risen somewhat since our last report. At the beginning of June, annual contracts for 2025 were priced at about 46 EUR/MWh, which is an increase of about 6 EUR/MWh since March. The increase is related to higher forward prices for gas and climate quotas in the European market (see Box 1.1 in Økonomiske analyser 2/2024). This has led to a rise in German forward prices that has spilled over into Nordic prices. We make developments in prices for Nordic power contracts the basis for developments in the Nordic System Price for the coming years, and adjust for deviations from the System Price in the various price areas. In our projections, we have assumed that the current schemes with reduced excise in the months January– March and energy support based on hour-to-hour prices will be extended through the projection period, and that both the excise duty on electricity and the threshold for receiving energy support will be adjusted up in line with general inflation. The income framework for grid charges is determined by the Norwegian Energy Regulatory Authority (RME) at the beginning of each year, and depends on factors such as spot prices and interest rates. Given an assumed decline in interest rates and low spot prices, we assume that the distribution companies’ cost rise will be moderate, and we also adjust grid charges upward in pace with general inflation. In our projections for energy prices, fuel prices largely shadow crude oil prices in NOK with a premium consisting of special taxes. On balance, we assume that the annual rise in energy prices will increase roughly in line with general inflation in 2025, and a little less than underlying inflation in the years 2026–2027. We have adjusted the special tax rates for inflation for the years 2025– 2027 and expect them to have a neutral effect on CPI inflation.

The inflation projections for the years ahead are broadly in line with those in our previous economic report in March. The key factors driving inflation have undergone little change. As usual, the exchange rate is fixed at the current level in the projections, which means that the rise in import prices for typical consumer goods falls to 2 per cent in the medium term and is consistent with the projections for global inflation. Since 1 January this year, the maritime sector has been included in the EU Emission Trading System (ETS), a quota system for emissions of climate gases, and this resulted in a considerable increase in fuel costs in the shipping sector. As a general rule, however, the transport capacity of a freighter is so large that the freight costs per item of goods carried has little effect on the product’s underlying import price. Low imported inflation and stable developments in energy prices will contribute crucially to inflation gradually falling toward the target in 2026. Productivity growth is forecast to be low this year. In the current year, growth in real wages is largely being driven by lower imported inflation. Given the stable developments in import prices forming the basis for the medium term projections, increased productivity growth will be the chief factor leading to real wage growth. We assume that productivity growth will pick up in the years ahead, with more effective utilisation of real capital and innovations in information technology expected to make major contributions.

CPI-ATE inflation is expected to fall to 3.1 per cent in 2025, and then to slow gradually to 2.2 per cent in 2027. Household energy prices are expected to increase roughly in line with underlying inflation next year, and CPI inflation is forecast to be 3.0 per cent in 2025. A moderate expected reduction in energy prices will lead to CPI inflation being slightly lower than CPI-ATE inflation in 2026.

Table 4. Main economic indicators 2015-2027. Accounts and forecasts[1, 2]

										Forecasts			
	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
Demand and output													
Consumption in households etc.	2,7	1,1	2,2	1,4	1,0	-6,2	5,1	6,2	-0,8	0,2	2,7	3,8	3,8
General government consumption	2,4	2,3	1,9	0,6	1,1	-0,5	3,6	1,1	3,4	2,2	1,8	1,9	2,4
Gross fixed investment	-4,0	3,9	2,6	2,2	9,5	-4,1	0,7	5,2	0,0	-3,5	1,3	2,9	2,8
Extraction and transport via pipelines	-12,2	-16,0	-5,4	0,7	14,3	-3,3	-0,9	-7,1	10,6	10,0	-2,0	-4,0	-2,1
Mainland Norway	-0,2	9,0	6,8	1,5	6,3	-3,1	1,6	7,6	-1,2	-6,7	1,9	4,6	3,9
Industries	-2,8	12,6	9,2	3,1	10,3	-5,3	3,2	17,1	4,0	-8,2	-1,1	1,6	1,1
Housing	3,2	6,6	7,3	-6,5	-1,1	-1,6	3,5	-1,4	-15,6	-15,4	6,7	12,7	9,9
General government	0,2	6,4	2,6	8,1	7,5	-1,1	-2,5	1,3	3,0	3,2	4,0	4,1	3,9
Demand from Mainland Norway[3]	2,0	3,1	3,1	1,2	2,3	-3,9	3,9	5,1	0,3	-0,9	2,3	3,4	3,4
Exports	3,9	0,4	1,6	-1,5	2,1	-2,3	6,1	4,5	1,4	3,1	3,8	0,8	1,2
Traditional goods	6,5	-11,2	0,9	2,0	5,1	-0,8	6,7	-2,5	6,1	5,9	2,5	2,9	3,0
Crude oil and natural gas	1,3	5,4	5,2	-4,6	-2,9	10,5	0,2	1,3	-1,1	1,6	3,6	-2,1	-1,3
Imports	1,9	1,9	1,8	1,4	5,3	-9,9	1,8	12,5	0,7	0,6	2,5	3,2	3,5
Traditional goods	2,7	-1,4	3,5	2,8	6,2	-2,7	5,4	3,4	-3,7	0,0	2,0	3,5	3,9
Gross domestic product	1,9	1,2	2,5	0,8	1,1	-1,3	3,9	3,0	0,5	0,8	2,7	1,9	2,0
Mainland Norway	1,4	0,9	2,2	1,9	2,3	-2,8	4,5	3,7	0,7	0,5	2,4	2,9	2,9
Manufacturing	-4,4	-4,1	-0,1	1,6	2,1	-5,7	5,6	-0,5	0,2	0,8	4,2	3,5	1,6
GDP in current prices (NOK billion)	3 130	3 116	3 323	3 577	3 597	3 462	4 324	5 708	5 127	5 186	5 545	5 680	5 832
Labour market													
Total hours worked. Mainland Norway	0,6	0,6	0,5	1,6	1,5	-2,1	2,4	3,9	0,8	0,5	1,1	1,7	1,8
Employed persons	0,4	0,3	1,1	1,6	1,6	-1,5	1,1	3,9	1,3	0,2	0,6	0,9	0,6
Labor force	1,5	0,2	-0,2	1,4	1,0	0,4	2,2	1,4	1,3	0,8	0,5	0,8	0,6
Participation rate (level)	71,0	70,4	69,7	70,2	70,5	70,4	72,1	72,6	72,8	72,2	72,1	72,4	72,5
Unemployment rate (level)	4,5	4,7	4,2	3,8	3,7	4,6	4,4	3,2	3,6	4,1	4,2	4,1	4,0
Prices and wages													
Wages per standard man-year	2,8	1,7	2,3	2,8	3,5	3,1	3,5	4,3	5,2	5,2	4,6	4,2	3,7
Consumer price index (CPI)	2,1	3,6	1,8	2,7	2,2	1,3	3,5	5,8	5,5	3,8	3,0	2,3	2,1
CPI-ATE[4]	2,7	3,0	1,4	1,6	2,2	3,0	1,7	3,9	6,2	4,1	3,1	2,6	2,2
Export prices, traditional goods	2,6	4,5	4,7	5,1	0,1	-3,5	12,6	30,2	-0,4	0,1	2,2	1,3	1,7
Import prices, traditional goods	5,0	2,5	3,2	4,1	2,5	4,3	5,0	15,6	5,8	1,0	1,7	1,4	1,6
House prices	6,1	7,0	5,0	1,4	2,5	4,3	10,5	5,2	-0,5	2,6	3,7	3,7	3,6
Income, interest rates and excange rate													
Household real disposable income	5,3	-1,6	2,0	0,9	2,0	1,1	4,1	-3,3	-2,5	2,2	4,0	4,2	3,2
Household saving ratio (level)	9,8	6,9	6,6	5,9	7,1	12,9	13,8	4,9	4,1	5,7	7,0	7,2	6,7
Money market rate (3 month NIBOR) (level)	1,3	1,1	0,9	1,1	1,6	0,7	0,5	2,1	4,2	4,7	4,0	3,5	3,5
Lending rate, credit loans (level)[5]	3,2	2,6	2,6	2,7	3,0	2,6	2,1	2,9	5,0	6,0	5,6	5,0	4,8
Real after-tax lending rate, banks (level)	0,1	-1,6	0,1	-0,7	0,2	0,7	-1,8	-3,3	-1,5	-0,2	-0,5	-1,1	-1,2
Importweighted krone exchange rate (44 countries)[6]	10,5	1,8	-0,8	0,1	2,9	6,7	-5,3	1,2	8,5	-0,2	0,0	0,0	0,0
NOK per euro (level)	8,95	9,29	9,33	9,60	9,85	10,72	10,16	10,10	11,42	11,51	11,51	11,51	11,51
Current account													
Current balance (bill. NOK)[7]	282	163	210	320	136	38	644	1722	917	825	946	839	732
Current account (per cent of GDP)	9,0	5,2	6,3	9,0	3,8	1,1	14,9	30,2	17,9	15,9	17,1	14,8	12,5
International indicators													
Exports markets indicator	5,3	3,9	5,5	4,3	3,4	-8,2	10,5	8,2	1,6	1,0	2,4	3,8	3,9
Consumer price index, euro-area	0,2	0,2	1,5	1,8	1,2	0,3	2,6	8,4	5,4	2,3	1,8	2,0	2,0
Money market rate, euro (level)	0,0	-0,3	-0,3	-0,3	-0,4	-0,4	-0,5	0,3	3,4	3,7	2,9	2,4	2,5
Crude oil price US dollar (level)[8]	53	45	55	72	64	43	71	99	82	81	78	75	73
Crude oil price NOK (level)[8]	431	379	452	583	564	407	609	951	867	857	828	800	779

[1] Percentage change from previous year unless otherwise noted.
[2] Some time series may have been revised after the publication of the Economic Survey.
[3] Consumption in households and non-profit organizations + general government consumption + gross fixed capital formation in mainland Norway.
[4] CPI adjusted for tax changes and excluding energy products.
[5] Yearly average. Credit lines. secured on dwellings.
[6] Increasing index implies depreciation.
[7] Current account not adjusted for saving in pension funds.
[8] Average spot price Brent Blend.
Source: Statistics Norway. The cut-off date for information was 12 June 2024.