

Economic trends

Financial turbulence has again characterised the global economy this spring. In a number of countries, particularly in southern Europe, measures to counteract the financial crisis and effects of automatic stabilisers have weakened the budget balance so much that financial market participants fear defaults on government debt. Market participants perceive government debt as risky, also in countries where the debt is not so large. The rising yield on government bonds is compelling many countries to tighten fiscal policy earlier than the cyclical situation would imply. Thus the financial crisis has become a government level financial crisis. Because of the higher yields on bonds, reducing government debt is more demanding now than it was in the past. If economic growth picks up in the period ahead, it will help to moderate the debt burden. On the other hand, budget cuts may curb growth in the short term, and the events of the last couple of years may have permanently reduced the growth potential in the OECD area. The risk of defaults on government debt has aroused fear of major losses in banks that own this debt, which may lead to a restrictive lending policy among banks and to the public. At worst, we may be heading into a new financial crisis.

For the past few quarters, developments in the real global economy have been characterised by a moderate upswing in output. The upswing is partly a rebound following the fall in output in autumn 2008 and spring 2009. In some countries, growth has taken the form of stock-building consistent with a normalisation of the economy. However, growth has again reached a high level in a number of Asian countries, and this has affected developments in some commodity markets. In the euro area, by contrast, growth has been moderate and only just positive. Now that most countries are tightening their fiscal policy, there is a risk that growth may be weak for a long time to come. We therefore assume that growth among Norway's trading partners will be weak for the next two years, and that the next global cyclical upturn will not come until 2012.

Growth in the Norwegian economy has also been positive, but weak, for the past year. Thus the cyclical downturn is continuing, but at a more moderate pace than just over a year ago. A decline in mainland fixed investment and in housing is pushing growth down, while consumption growth has been quite high. We expect the decline in investment to gradually draw to a halt during the second half of this year. This will contribute to an upswing in GDP growth in 2011, but not really enough to justify talk of a cyclical turnaround before 2012. This is because consumption growth will be somewhat lower and the contribution from the global economy small. Owing to the high cost level and strong krone, internationally exposed enterprises must expect to lose market shares.

A positive aspect of Norwegian developments has been that the increase in unemployment has been relatively moderate under the circumstances. LFS unemployment is now about 3.5 per cent. Taking into account the recent sharp cyclical downturn, the rise in unemployment has been moderate. However, given weak growth for a period ahead, unemployment must be expected to rise from the current level but remain below the level of 4.5 per cent reached during the last contraction (2003-2005). This will curb the rise in domestic costs to some extent. The cyclical downturn and a strengthening of the krone have contributed to underlying inflation, measured by the CPI-ATE, is moderate and likely to remain so for a good while to come.

Continuing cyclical downturn in Norway

Following a cyclical peak in the Norwegian economy in the fourth quarter of 2007, the downturn became gradually more pronounced through 2008 and into 2009. Output measured by mainland GDP continued to grow through the first half of 2008, but more slowly than the underlying growth in the economy. However developments became far more dramatic with the financial crisis from September 2008. In the fourth quarter of 2008 and the first quarter of 2009, mainland output fell by an annual rate of approximately 4 per cent. In the

second half of 2009, mainland GDP began to rise again, but growth has generally been weak and the cyclical downturn in Norway has continued, albeit at a slower pace. A turnaround appears unlikely to occur in 2010.

At the beginning of 2008, the decline in household purchases of consumer durables and housing investment was more than offset by the growth in general government consumption and exports. At the same time, business sector investment levelled off. Demand

Table 1. **Macroeconomic indicators 2008-2009. Growth from previous period unless otherwise noted. Per cent**

	2008*	2009*	Seasonally adjusted			
			09:2	09:3	09:4	10:1
Demand and output						
Consumption in households etc.	1.3	0.1	1.3	1.3	1.3	0.6
General government consumption	4.1	4.8	1.0	1.1	-0.7	1.0
Gross fixed investment	1.4	-7.9	0.1	-5.1	3.0	-11.0
Mainland Norway	1.0	-11.7	1.8	-5.3	5.4	-12.3
Extraction and transport via pipelines	3.7	4.6	-7.2	-7.6	-0.2	2.9
Final domestic demand from Mainland Norway ¹	1.9	-1.1	1.3	0.0	1.5	-1.7
Exports	0.9	-4.0	-4.0	3.6	1.0	-0.2
Crude oil and natural gas	-2.0	-1.2	-5.9	4.6	-1.6	-1.6
Traditional goods	4.3	-7.8	-1.1	8.1	0.0	0.3
Imports	2.2	-10.3	1.7	0.7	0.6	-0.5
Traditional goods	-0.4	-13.2	-1.3	1.5	-0.3	3.1
Gross domestic product	1.8	-1.6	-1.1	0.5	0.1	-0.1
Mainland Norway	2.2	-1.6	0.0	0.3	0.4	0.1
Labour market						
Man-hours worked	3.4	-1.4	-0.3	-0.4	-0.1	-0.4
Employed persons	3.1	-0.4	-0.4	-0.3	0.1	-0.2
Labour force ²	3.4	0.0	0.2	-0.9	0.2	0.4
Unemployment rate, level ²	2.6	3.2	3.1	3.2	3.3	3.5
Prices and wages						
Wages per standard man-year ³	6.0	4.1	4.5	3.5	3.5	3.5
Consumer price index (CPI) ³	3.8	2.1	3.1	1.8	1.4	2.9
CPI adjusted for tax changes and excluding energy products (CPI-ATE) ³	2.6	2.6	3.0	2.4	2.3	2.0
Export prices, traditional goods	2.4	-6.5	-1.4	2.2	-3.7	0.4
Import prices, traditional goods	4.6	-1.2	-2.1	-0.9	-2.6	0.9
Balance of payment						
Current balance, bill. NOK	472.8	337.4	90.5	72.3	101.7	97.6
Memorandum items (unadjusted level)						
Money market rate (3 month NIBOR)	6.2	2.5	2.5	1.9	2.1	2.3
Lending rate, banks ⁴	7.3	4.9	4.4	4.2	4.3	4.4
Crude oil price NOK ⁵	536.4	388.1	386.8	421.2	429.2	452.5
Importweighted krone exchange rate, 44 countries, 1995=100	90.8	93.8	95.1	94.1	90.0	89.3
NOK per euro	8.22	8.73	8.84	8.74	8.39	8.10

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 Period averages.

⁵ Average spot price, Brent Blend.

Source: Statistics Norway and Norges Bank.

for factor inputs for the petroleum industry contributed to dampening the downturn in the Norwegian economy through 2008. When the Norwegian economy was hit in earnest by the global downturn in the fourth quarter of 2008, exports of traditional goods fell in a weak global market and the decline in private domestic demand from the mainland economy intensified as a result of falling investment. The decline in the first quarter of 2009 is mainly due to a continuation of the same factors that affected developments at the end of 2008. The number of man-hours worked fell along with the fall in output. According to Statistics Norway's Labour Force Survey (LFS), both registered unemployment and the number of job-seekers were rising before the actual crisis took hold, but only weakly and from a low level.

With a sombre outlook ahead and falling employment the authorities feared that unemployment would rise substantially and rapidly. This prompted a shift in monetary policy through lower interest rates and special credit policy measures followed by fiscal stimuli. The overall shift in policy substantially dampened the sharp fall in output, and the increase in the labour force also levelled off rapidly. Average hours worked also fell somewhat and as a result unemployment increased far less through 2009 than many had expected.

When the financial crisis took hold and energy prices fell, the rise in the CPI rapidly fell to the inflation target, while the rise in the CPI-ATE did not fall from about 3 per cent to the inflation target until after the summer of 2009. One factor that influenced inflation in Norway compared with the EU countries was the sharp depreciation of the krone in autumn 2008. The import-weighted krone exchange rate depreciated by about 15 per cent from August to December 2008. Despite this – and in contrast to the monetary policy pursued during the Asian crisis in 1998 – Norges Bank reduced its key policy rate. Although the premium between Norges Bank's deposit rate and the 3-month money market rate increased during the financial crisis, the money market rate was approximately halved from the third quarter of 2008 to the first quarter of 2009 and reduced further by the summer of 2009. This contributed to slowing the economic downturn. The krone strengthened again through 2009, and at the end of 2009 the import-weighted exchange rate was back at approximately the same level as before the crisis. This has helped to curb the rise in the CPI-ATE so far this year.

The change to positive growth in the mainland economy is closely linked to the fact that the decline in household consumption came to a halt concurrently with the shift to a more expansionary fiscal policy. On balance, consumption therefore increased strongly through 2009. Exports of traditional goods also recovered again after a sharp fall around year-end 2008/2009, but growth has been very moderate for the last couple of quarters. Growth is currently weak, partly due to a continued fall in mainland business investment and in housing. Preliminary quarterly national accounts

(QNA) figures shows a very moderate GDP growth in the first quarter of 2010. However, there are signs that the decline in housing investment will give way to an upswing, which in isolation will contribute to higher growth in the mainland economy in the period ahead.

On balance, economic policy is continuing to provide a positive stimulus to the Norwegian economy, but this stimulus will gradually abate as policy is shifted to a more neutral stance. In our view, the most important contribution to a halt in the cyclical downturn will be a reversal of the fall in mainland investment to a slight rise in the course of 2011. The weak cyclical recovery from early 2012 will strengthen in 2013, so that towards the end of 2013 we will be approaching a cyclically neutral situation.

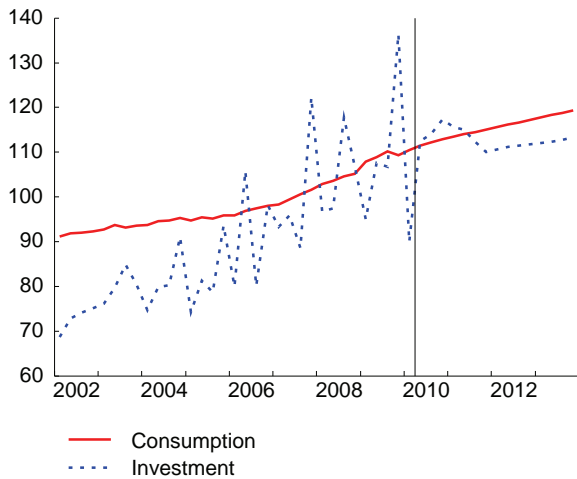
An economic picture of this kind is also dependent on a moderate global upturn that involves traditional Norwegian exports. Developments appear most positive in countries outside the euro area. As mentioned earlier in this report, large budget deficits in Europe are leading to fiscal tightening and increased uncertainty in financial markets. This may curb the weak upturn, not least in the euro countries, resulting in little growth in Norwegian exports in the immediate future. In Norway, new figures and estimates in the Revised National Budget 2010 (RNB) show that fiscal policy does not need to be adjusted as much as was initially estimated in order to revert to the fiscal rule. As a result, Norwegian authorities have freedom of manoeuvre in fiscal policy and, if it should prove necessary, can adjust fiscal policy on the basis of their own assessments of the economic situation. The euro countries have not had this option, and developments in financial markets have compelled them to adjust their policy before they had planned to. According to our projections, however, there will be no fiscal stimulus, measured as deviation from the 4 per cent rule, 2012.

Given weak GDP growth, there is reason to believe that employment growth will be moderate for the next couple of years and that productivity growth will normalise. Unemployment will probably edge up again after remaining fairly stable for some months. Wage growth is likely to be moderate in the period ahead, but such that real wages increase. Given weak growth abroad, a low rise in prices for imported goods and a moderate rise in domestic costs, inflation in Norway will remain low for a while to come. We believe that the inflation rate will only rise again to the inflation target towards the end of the projection period.

Less expansionary fiscal policy

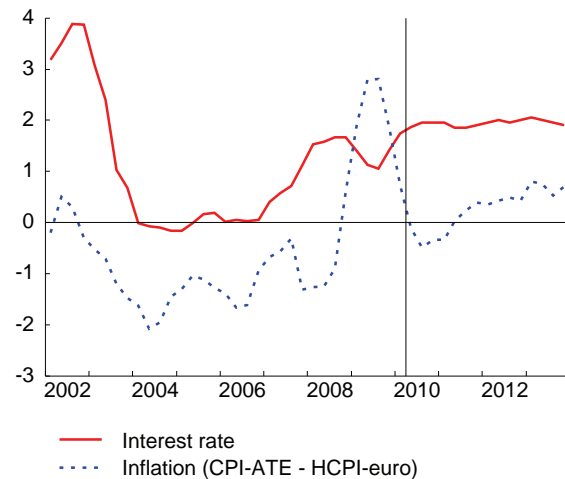
The most recent QNA figures show that the high underlying growth in general government consumption has continued into 2010. However there was a decline in gross general government investment, also after adjustment for incidental fluctuations in investment in defence materials. The national accounts figures for 2009 have been revised somewhat, and growth in general

Figur 1. **General government. Seasonally adjusted volume indices. 2007=100**



Source: Statistics Norway.

Figur 2. **Interest rate and inflation differential between NOK and the euro. Percentage points**



Source: Norges Bank and Statistics Norway.

government consumption has been revised downwards to 4.8 per cent. This growth was fairly evenly divided between central and municipal government, while the figures for the first quarter of 2010 show strongest growth for central government. Gross general government investment has been revised upwards for 2009, as a further frigate was registered as an investment in 2009, which it was previously assumed would not happen until 2010. In addition, one anticipated frigate investment in 2010 has been moved to 2011, so that a slight decline is expected in overall general government investment in 2010. In RNB, underlying real spending growth in the government budget for 2010 is now estimated at 2½ per cent. This is somewhat higher than previously, but the increase is mainly due to the fact that the spending level for 2009 is now lower than previously assumed. Strong growth in transfers to households contributes to pushing up the real growth in overall public expenditure.

Fiscal policy was highly expansionary in 2009, even though the fiscal stimulus was revised down in the RNB compared with previous estimates. In isolation, the downward revision of the 2009 figures increases the expansionary stimulus in the policy for 2010, since the level of spending estimates for 2010 has not been changed to any appreciable extent. Although fiscal policy remains expansionary, the government budget for 2010 provides appreciably less stimulus to the economy than the previous year. Estimates for fiscal policy in 2010 are largely the same as in our previous projection.

One important result of the changes in the estimates in the RNB is that the deviation from the 4 per cent path has been revised down substantially for 2009. Measured in relation to the capital in the Government Pension Fund Global, the structural non-oil budget deficit (SNOBD) was 4.8 per cent in 2009. The SNOBD estimate for 2010 has also been revised down, and is now estimated at 5 per cent of the capital in the fund. This is

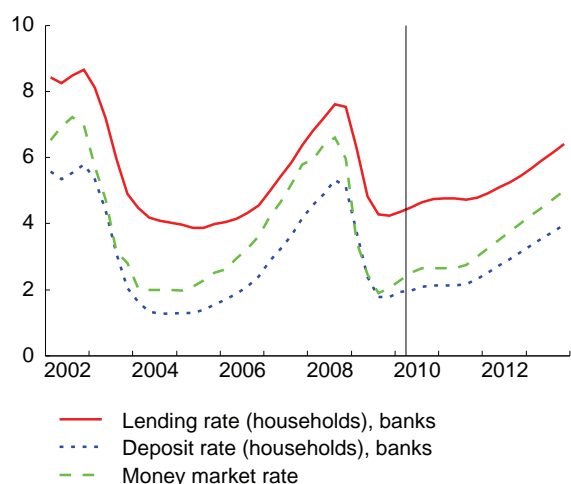
lower than in the period 2001-2005. The Government has indicated that it is aiming for a less expansionary policy from 2011 onwards and a gradual return to the 4 per cent path prescribed by the fiscal rule. This also forms the basis for our projections for the period ahead.

Fiscal policy for 2011 is still assumed to result in a SNOBD that is higher than the 4 per cent path, but we assume that the expansionary stimulus will be reduced compared with 2010 by weaker government spending growth than previously. Growth in public purchases of goods and services is expected to be lower than trend growth in the Norwegian economy. Consumption growth is estimated at 2 per cent, while investment excluding the purchase of frigates is approximately unchanged. Our assumptions are, as usual, based on that direct and indirect taxes are adjusted for inflation. Our projections for 2011 imply that SNOBD will approach the 4 per cent path.

Expansionary impulses from fiscal policy are expected to be somewhat further reduced in 2012 as growth in the economy picks up somewhat. The projections are based on adjustment for inflation of rates in the tax system so that budgetary tightening is achieved through moderate growth in public purchases of goods and services. Increased capital in the Government Pension Fund Global will also contribute to our being approximately on the 4 per cent path in 2012. According to our projections, the Norwegian economy will be in an almost cyclically neutral situation at the end of 2013. This implies that fiscal policy will not deviate substantially from the fiscal rule in 2013 either.

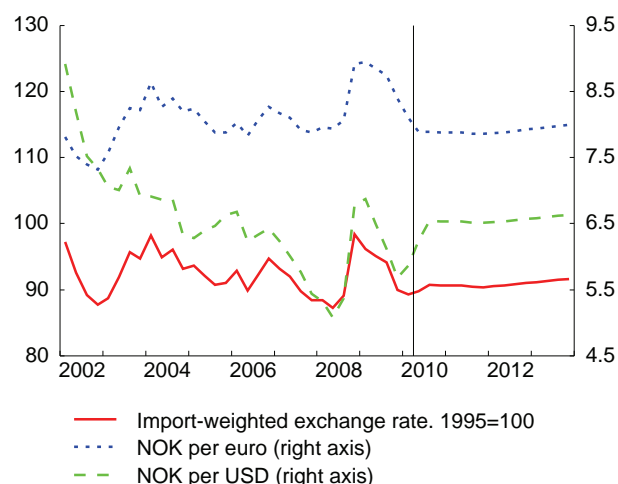
In the years ahead, old age pension expenses will increase substantially because large cohorts born at the end of World War II and subsequent years will reach retirement age. Real growth in old age pensions is therefore assumed to increase by about 0.5 percentage point annually through the projection period. However,

Figur 3. Norwegian interest rates. Per cent



Source: Norges Bank and Statistics Norway.

Figur 4. Exchange rates



Source: Norges Bank.

growth in pension expenses is uncertain because pension system reforms are encouraging older people to postpone retirement partly or wholly. We expect a real decline in sickness absence from 2011. Expenditure on unemployment benefit will peak in real terms in 2012, and then fall back somewhat towards the end of the projection period. We assume that the rise in the number of disability pensioners will abate.

One year without interest rate increases

Norges Bank's setting of interest the key policy rate is aimed at stabilising inflation at 2.5 per cent in the medium term, while promoting stable developments in output and employment. Inflation measured by the 12-month rise in the consumer price index adjusted for tax changes and excluding energy products (CPI-ATE) has fallen somewhat since the beginning of the year and was 1.7 per cent in April.

Prompted by the crisis in financial markets worldwide and the sombre economic outlook, Norges Bank cut the key policy rate by 4.5 percentage points from autumn 2008 and over a nine month period, so that in June 2009 it was 1.25 per cent. Since then, the policy rate has been raised three times, most recently at the beginning of May this year. Each of the interest rate hikes has been 0.25 percentage point, so that the key rate is now 2.0 per cent.

As a result of the financial crisis, the differential between money market rates and the key policy rate widened. Before the financial crisis, money market rates largely shadowed the policy rate with a premium of 0.25 percentage point. Since the summer of 2007, the premium has been substantially larger, and at the end of September 2008 it was over 2 percentage points. Since November 2009, the premium has been around 0.5 percentage point. Money market rates edged up through May 2010, and for the past few weeks have been around 2.6-2.7 per cent.

The authorities introduced measures to reduce the problems in financial markets. The measures involved both supplying liquidity and strengthening banks' equity. These measures were described in more detail in *Economic Survey 1/2010*.

The setting of interest rates also affects credit growth, which is important for the financial stability of the economy. Domestic credit growth, measured by 12-month growth in gross domestic debt of the general public (C2) was 4.0 per cent in April 2010 compared with 14.5 per cent two years earlier. Credit growth in non-financial enterprises has been reduced from just over 20 per cent in July 2008 to -1.5 per cent in April this year. Household debt increased by 6.3 per cent from April 2009 to April 2010. Household debt growth has not been as low for the past 10 years.

The Norwegian krone depreciated strongly against the US dollar and the euro through the second half of 2008. This weakening was largely reversed in the course of 2009. Measured in terms of the import-weighted krone exchange rate, the krone appreciated by over 12 per cent from December 2008 to January 2010. From the beginning of 2010 and up to mid-May this year, there have only been short-term fluctuations in the value of the krone, measured by the import-weighted krone exchange rate, around a relatively stable level. During this period the krone has strengthened against the euro and weakened against the US dollar. From 18-21 May this year the krone depreciated by about 4 per cent, measured by the import-weighted krone exchange rate. Some of this weakening was reversed at the end of May.

Fiscal tightening – made necessary by the high government debt in many countries – will probably mean that the low level of interest rates worldwide will persist for longer than was previously assumed. This points to interest rate hikes being postponed also in Norway. We do not believe that there will be any further increases

Table 2. Household real disposable income. Percentage growth

	2005	2006	2007	2008	2009	2010	2011	2012	2013
Total	7.4	-6.5	6.3	3.1	3.7	3.8	3.0	3.2	3.1
Exclusive dividends	3.4	4.2	5.1	2.7	4.0	3.8	2.8	2.9	2.8

Source: Statistics Norway.

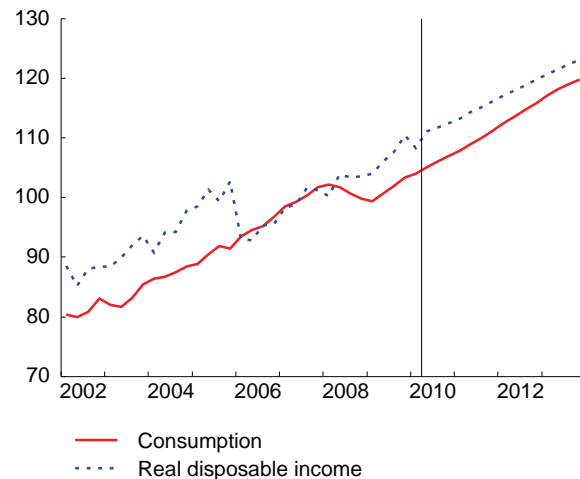
in the key policy rate before next summer. As a result, money market rates will probably remain at the current level for the remainder of 2010 and into 2011. Two or three interest rate hikes in the latter half of 2011 will bring money market rates up to 3-3¼ by the end of 2011 or early 2012. The interest rate level will gradually normalise after a while, and the interest rate is projected to be 5 per cent by the end of 2013. The money market rate is assumed to lie 1¾-2 percentage points higher in Norway than in the euro area throughout the projection period.

Our projections imply small changes in the value of the krone from the current level. We assume that one euro will cost just under NOK 8 throughout the projection period, while the US dollar will be worth around NOK 6.60. This nevertheless represents a substantial strengthening of the krone as an annual average from 2009 to 2010 of 9 per cent against the euro and 4 per cent measured in terms of the import-weighted krone exchange rate. Measured in terms of import weights, the krone will weaken by about 0.5 per cent annually for the remainder of the projection period. The weakening from 2012 is due to the fact that some of the effect of the interest rate differential will then be exhausted.

Slower consumption growth ahead

The most recent seasonally-adjusted QNA figures show that consumption by households and non-profit organisations rose by 0.6 per cent in the first quarter this year compared with the previous quarter. Consumption has accordingly increased for four consecutive quarters. Consumption growth in the first quarter of this year was about half that in the fourth quarter of 2009, however. Car purchases showed sharp growth throughout 2009, which reversed into a slight fall in the first quarter of this year. This contributed to a fall in goods consumption growth from 2 per cent in the fourth quarter of 2009 to 0.4 per cent in the first quarter of this year. The goods consumption index for April shows a seasonally-adjusted decline of 0.2 per cent from March, following a slightly larger decline in March and February. This points to continued slower growth in household consumption in the second quarter of this year. Developments in monthly figures for registered new private cars also point to a levelling off at around the high level of late 2007/early 2008. The sharp fall in registered new private cars throughout 2008 was thus fully made up in the course of 2009. In contrast to goods consumption, consumption of services showed relatively stable developments through the cyclical downturn. In the first quarter of this year, consumption of services increased by 0.6 per cent, approximately on

Figur 5. Income and consumption in households. Volume indices. 2007=100

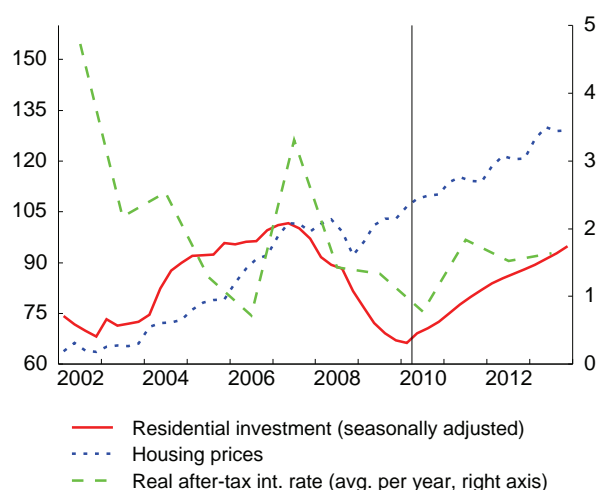


Source: Statistics Norway.

a level with the average growth rate in the period from the second quarter to the fourth quarter of 2009.

Growth in household real disposable income was 3.7 per cent in 2009 compared with 3.1 per cent the previous year, according to preliminary national accounts figures. Substantially lower interest expenses in the wake of the financial crisis and almost a halving of consumer price inflation contributed substantially to the increase in real income growth. Wage income contributed to a more moderate extent to income growth since the cyclical downturn resulted in weaker wage growth and lower employment in 2009 than the previous year. Growth in household real disposable income is expected to moderate through the projection period. Growth in wage income will pick up somewhat, but developments in net interest income will not contribute appreciably to growth in 2010. Housing wealth will probably continue to increase with rising house prices and, aided by low real interest rates, will contribute to consumption growth in 2010 rising to around 4 per cent as an annual average. Although growth in wage income is expected to pick up more markedly with an improved economic situation, somewhat higher interest rates and gradually rising consumer prices will lead to more moderate growth in real disposable income in 2011-2013. Weaker income developments coupled with a somewhat higher interest rate level will contribute to dampening consumption growth in the years after 2010, while increasing housing wealth will have the opposite effect. On balance, annual consumption growth will probably remain at around 4 per cent in the period 2011-2013.

Figur 6. Residential market. Left axis adj. indices. 2007=100. Right axis per cent



Source: Statistics Norway.

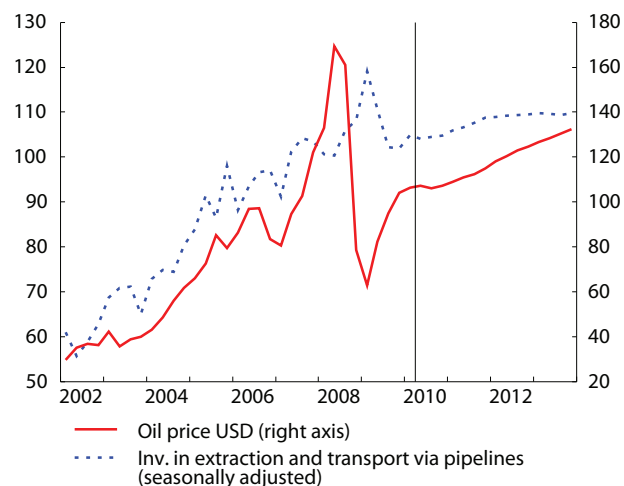
Even with increased real interest rates, the household saving rate (saving as a share of disposable income) is expected to fall from 7.5 per cent in 2009 to around 6.5 per cent this year, and then further down to close to 4 per cent in 2013. This development in the saving ratio must be considered in light of the fact that in isolation the rise in house prices will reduce the need for household financial consolidation. The financial consolidation that followed in the wake of the financial crisis led to a more than doubling of the saving ratio from 2008 to 2009. Net financial investment will fall through the projection period in pace with the fall in saving and rise in housing investment. Households are projected to reduce their net financial investment from a positive NOK 43 billion in 2009 to a negative level of around NOK 12 billion in 2013.

Housing investment is rising

Housing investment continued to fall in the first quarter of this year. According to the seasonally-adjusted QNA figures, housing investment edged down 1.3 per cent from the fourth quarter of 2009 to the first quarter of this year, and has thus fallen for eleven consecutive quarters by a total of around 35 per cent. However the investment level gradually levelled off somewhat through 2009 in pace with the turnaround in housing starts. Prospects of a more favourable economic situation and a continued rise in house prices indicate a further stimulus for housing starts, so that housing investment will probably pick up again in the course of 2010 and for the remainder of the projection period. According to our projections, the level of housing investment in 2013, measured in constant prices, will nonetheless lie about 10 per cent below the peak level in 2007.

According to Statistics Norway's house price index, house prices as a whole fell steeply through the second half of 2008. Prices for detached houses, small houses and flats all dropped by about 10 per cent from the

Figur 7. Oil price and oil investment. 2007=100



Source: Statistics Norway.

second to the fourth quarter of 2008. Prices for all types of housing have since risen sharply and more than compensated for the preceding slump in the wake of the financial crisis. Detached houses and small houses showed the largest price rise from the fourth quarter of 2009 to the first quarter of this year, at 3.9 per cent and 3.7 per cent, respectively, while prices for flats increased by 1.5 per cent. We expect house prices to continue rising, and that they will rise by an annual average of 8 per cent this year. We project a rise in house prices of around 5 per cent annually for the remainder of the projection period, in pace with more moderate income growth and somewhat increasing real interest rates.

High petroleum investment in years ahead

Investment in petroleum activities increased continuously from the end of 2002 up to and including the first quarter of 2009 before falling through the year. The preliminary QNA figures show that the fall in petroleum investment has halted and that investment in oil extraction and pipeline transport increased by 2.9 per cent from the fourth quarter of 2009 to the first quarter of 2010. Investment in platforms, drilling rigs and modules contributed in particular to the fall last year, while investment in drilling and pipelines only showed a moderate decline. The increase in the first quarter of 2010 can be largely attributed to high drilling activity, and particularly production drilling, which increased appreciably. The high drilling activity is largely attributable to the fact that several new fields will commence operations in 2010. However, the completion of platforms through 2009 and initiation of fewer new projects caused investment in platforms and modules to continue falling in the first quarter of 2010.

We are still expecting relatively flat investment developments through 2010. Investment in platforms and modules in particular is being reduced from 2009 to

2010, while production drilling and exploration remain at approximately the same level. This will contribute to reducing petroleum investment by 3.1 per cent from 2009 to 2010. Because of large import shares in investment in platforms compared with other types of investment in the petroleum industry, the demand effect of reduced petroleum investment is less in 2010 than the decline in investment would indicate in isolation.

The initiation of several large projects will cause investment in platforms and modules to increase in 2011. This will lead to a weak rise in overall petroleum investment from 2010 to 2011. Activity is then expected to pick up in most types of investment and contribute to moderate growth in petroleum investment for the remainder of the projection period.

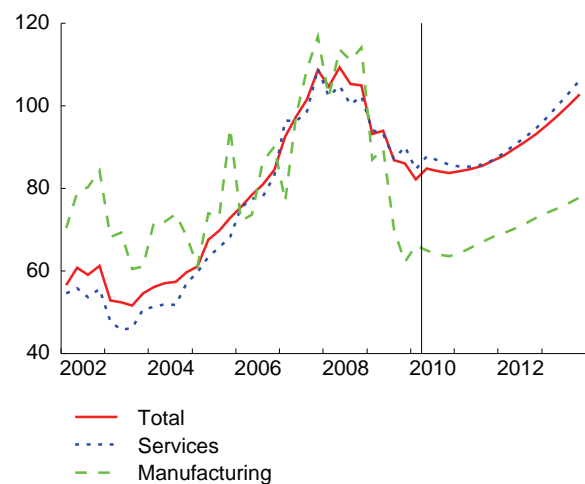
Production of crude oil continued to abate in the first quarter of 2010. The decline in production compared with the same quarter in 2009 was just under 8 per cent. Gas production increased by only 4 per cent, which is somewhat weaker than expected, and has therefore not prevented a fall in overall petroleum production. We expect crude oil production to continue to fall, and that gas production will not grow enough to prevent a further decline in overall petroleum production. In the course of a couple of years, production of gas, measured as oil equivalent, will be greater than production of oil.

It is uncertain to what extent new technology for recovering shale gas – thereby creating expectations of an increased supply – will affect gas prices. Prices for gas from the Norwegian continental shelf are strongly linked to movements in the crude oil price. Consequently prices for gas from existing fields will probably be less affected by an increased supply of gas in the short term. In isolation, an increased supply points to lower gas prices in the longer run, but the gas price is affected by a number of factors, and it is not a given that the recovery of shale gas will reduce prices significantly. A larger supply of gas and probably improved delivery reliability, coupled with a clearer focus on environment and climate, may lead to a shift in demand from coal to gas. This may increase demand. We have assumed that Norwegian export prices for gas will rise throughout the projection period, but not as strongly as the export price of oil, which is expected to increase by about 30 per cent from the first half of 2010 to the latter half of 2013. Should the increase in gas prices slow, this may influence investment, but probably not until late in our projection period.

Low investment in 2010 and 2011

Mainland business investment doubled from 2003 to 2008. According to the seasonally-adjusted QNA figures, however, this investment has fallen almost every quarter since the second quarter of 2008. As an annual average, mainland business investment fell by 15 per cent from 2008 to 2009. The first quarter of this

Figur 8. Investment, Mainland Norway. Seasonally adjusted volume indices. 2007=100



Source: Statistics Norway.

year showed a fall of 4.6 per cent compared with the previous quarter.

Investment in manufacturing and mining fell by 30 per cent from 2008 to 2009. The figures for the first quarter of this year show a growth of 6.4 per cent. Investment in other goods production and service industries declined by 17 per cent and 11 per cent, respectively, from 2008 to 2009, and investment in both industry groups fell by a further 6 per cent in the first quarter of this year.

Our investment projection for manufacturing in 2010 is close to what the Statistics Norway's last investment intentions survey indicates. We expect manufacturing firms to further reduce their investment, causing manufacturing investment to fall by about 14 per cent compared with 2009. A more favourable economic situation and normalisation of credit markets are expected to boost manufacturing investment again by over 2.5 per cent in 2011 and 6½-7 per cent in both 2012 and 2013.

Investment in the power supply sector appears likely to increase by as much as 14 per cent this year and a further 25 per cent next year. The investment growth will be partly attributable to a number of large projects associated with the production and distribution of district heating. Another contributory factor is the increased focus on upgrading and development of the electricity grid.

Investment in mainland industry as a whole is expected to fall by 7 per cent this year and to remain approximately unchanged in 2011. This investment will rise again in 2012 and 2013 by 6½ and 9½ per cent, respectively. Pronounced growth in investment in the services industries will contribute to this increase.

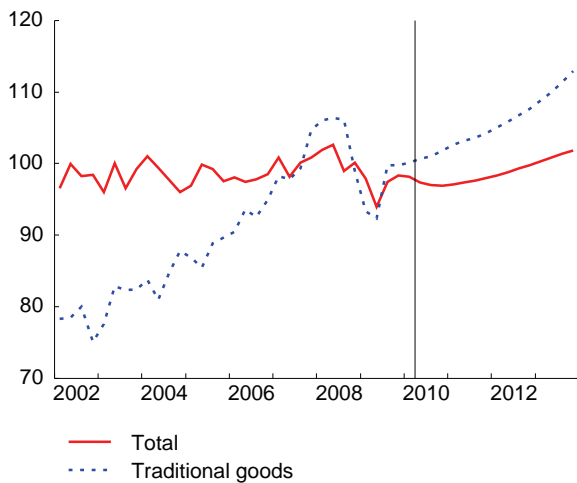
Table 3. Main economic indicators 2009-2013. Accounts and forecasts. Percentage change from previous year unless otherwise noted

	Accounts 2009	Forecasts								
		2010			2011		2012		2013	
		SN	MoF	NB	SN	NB	SN	NB	SN	NB
Demand and output										
Consumption in households etc.	0.1	4.1	4.3	5	3.7	4 1/4	4.3	3	4.0	2 1/2
General government consumption	4.8	2.7	2.4	3	2.1	2 1/4	1.9	..	1.9	..
Gross fixed investment	-7.9	-6.2	-3.6	..	3.4	..	4.7	..	5.9	..
Extraction and transport via pipelines ¹	4.6	-3.1	-2.5	-4 1/2	2.0	-1 1/2	2.4	6 1/2	0.2	2 3/4
Mainland Norway	-11.7	-5.4	-3.5	-2	4.1	8	4.9	..	6.9	..
Industries	-15.1	-7.3	-7.8	..	0.4	..	6.4	..	9.5	..
Housing	-18.9	-3.0	-1.5	..	13.1	..	9.3	..	6.7	..
General government	6.8	-3.0	5.1	..	4.1	..	-2.8	..	1.0	..
Demand from Mainland Norway ²	-1.1	1.9	2.3	3	3.3	4 1/4	3.7	3 1/4	3.9	2 1/4
Stockbuilding ³	-2.2	0.0	..	..	0.0	..	0.0	..	0.0	..
Exports	-4.0	0.1	0.8	..	0.4	..	1.7	..	2.2	..
Crude oil and natural gas	-1.2	-2.5	-3.0	..	-1.6	..	-1.0	..	-0.9	..
Traditional goods ⁴	-7.8	4.6	4.7	5 1/4	2.7	3	2.7	..	4.1	..
Imports	-10.3	1.5	3.7	5	3.6	6	5.1	..	5.3	..
Traditional goods	-13.2	2.6	4.7	..	4.8	..	6.5	..	7.4	..
Gross domestic product	-1.6	0.6	0.9	1 1/4	1.9	1 1/2	2.5	2	2.8	1 1/4
Mainland Norway	-1.6	1.6	2.1	2 1/4	2.7	2 3/4	3.1	2 1/2	3.5	2 1/4
Labour market										
Employed persons	-0.4	-0.2	-0.1	0	0.3	3/4	1.3	1	2.1	1/2
Unemployment rate (level)	3.2	3.5	3.5	3 3/4	3.9	3 3/4	4.0	3 1/2	3.8	3 1/2
Prices and wages										
Annual earnings	4.5	3.4	3 1/4	3 3/4	3.4	4 1/4	3.9	4 3/4	4.7	4 3/4
Consumer price index (CPI)	2.1	2.5	2.2	2 1/2	1.6	1 3/4	2.2	2 1/2	2.7	2 1/2
CPI-ATE ⁵	2.6	1.4	1.3	1 1/2	1.6	2	2.0	2 1/2	2.4	2 1/2
Export prices, traditional goods	-6.5	2.0	1.9	..	2.4	..	3.7	..	4.1	..
Import prices, traditional goods	-1.2	-3.1	-0.4	..	1.4	..	1.0	..	2.1	..
Housing prices	1.9	7.9	..	..	5.0	..	5.3	..	6.8	..
Balance of payment										
Current balance (bill. NOK)	337.4	369.3	385.6	..	363.9	..	422.4	..	442.9	..
Current balance (per cent of GDP)	14.1	14.7	15.2	..	13.7	..	15.0	..	14.7	..
Memorandum items:										
Household savings ratio (level)	7.4	6.5	5.9	..	5.5	..	4.5	..	3.8	..
Money market rate (level)	2.5	2.5	2.7	2.4	2.8	3.3	3.6	4.3	4.6	4.8
Lending rate, banks (level) ⁶	4.9	4.6	..	..	4.8	..	5.2	..	6.0	..
Crude oil price NOK (level) ⁷	388	488	475	..	530	..	578	..	621	..
Export markets indicator	-9.0	5.6	..	..	4.2	..	4.7	..	6.2	..
Importweighted krone exchange rate (44 countries) ⁸	3.3	-4.0	-5.1	-5	0.5	2 1/4	0.3	1	0.7	1

¹ Forecasts from Ministry of Finance incl. service activities incidental to extraction.² Consumption in households and non-profit organizations + general government consumption + gross fixed capital formation in Mainland Norway.³ Change in stockbuilding. Per cent of GDP.⁴ Norges Bank estimates traditional exports, which also includes some services.⁵ CPI adjusted for tax changes and excluding energy products (CPI-ATE).⁶ Yearly average.⁷ Average spot price, Brent Blend.⁸ Increasing index implies depreciation. Ministry of Finance forecasts trade-weighted exchange rate.

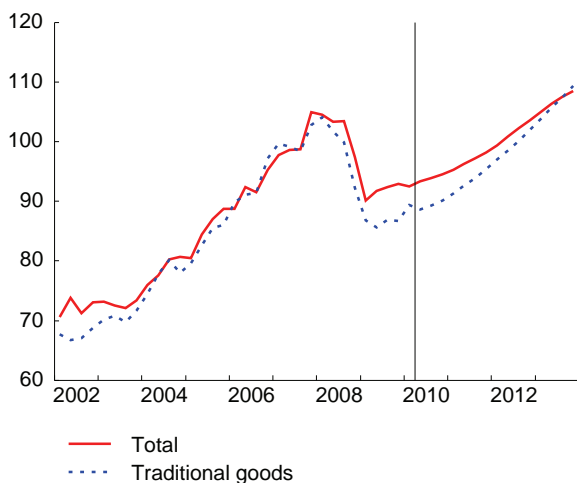
Source: Statistics Norway (SN), Ministry of Finance, St.meld. nr.2 (2009-2010), (MoF), Norges Bank, Pengepolitisk rapport 1/2010 (NB).

Figur 9. Exports. Seasonally adjusted volume indices. 2007=100



Source: Statistics Norway.

Figur 10. Imports. Seasonally adjusted volume indices. 2007=100



Source: Statistics Norway.

Moderate balance-of-payments deficit

The overall volume of Norwegian exports has remained at a relatively stable level over the past decade. Petroleum exports have fallen as a result of a declining trend in crude oil production. However this development has been offset by a rise in exports of other goods and services. Exports of traditional goods – which include large product groups such as engineering products, metals, and chemical and mineral products – increased by over 40 per cent in the course of just over five years before reduced demand from Norway's trading partners brought developments to an abrupt halt in the third quarter of 2008 as a result of the financial crisis. During the year that followed, exports of traditional goods slid by over 13 per cent, and the fall for many product groups was in the range 20-30 per cent. The decline in exports of services was substantially less. A sharp increase in exports of most goods and services through the second half of 2009 slowed the decline

for the year as a whole, so that total exports in 2009 ended up only 4 per cent lower than in 2008. Exports of traditional goods fell by almost 8 per cent. Exports of oil and gas continued their trend decline, at just over 1 per cent. Moving into 2010, developments in exports of traditional goods were almost flat, while exports of services and petroleum have fallen a couple of per cent. Increased sales of used fixed assets contributed to total exports being virtually unchanged in the first quarter compared with the previous quarter.

The turbulence in global financial markets weakened the krone exchange rate severely in the fourth quarter of 2008. In isolation, this provides a positive stimulus to exports. The global cyclical downturn had a negative impact on Norwegian export prices, nevertheless. The oil price was roughly halved in the fourth quarter of 2008, while the seasonally-adjusted price index for exports of traditional goods fell by approximately 10 per cent from the third quarter of 2008 to the second quarter of 2009. The rise in oil prices through the last three quarters of 2009 contributed to reversing developments in the price index for overall exports from declining to rising through 2009, but was nevertheless unable to prevent Norwegian exports as a whole experiencing an annualised average price fall in 2009 of a full 14 per cent compared with the previous year. Prices for traditional export goods fell by 6.5 per cent. The price index for service exports was approximately unchanged. Seasonally-adjusted QNA figures for the first quarter of 2010 indicate a slight rise in prices for goods exports, while prices for service exports dipped.

We have assumed that the economic situation of our most important trading partners through 2010 and the next few years will be weak. We expect total exports this year and next to remain at approximately the same level as in 2009. Growth in exports excluding oil and gas is estimated at about two per cent for the next two years, with somewhat higher growth in exports of services and traditional goods. Exports of petroleum products are expected to continue their trend decline throughout the projection period. In 2012 and 2013 we expect the global cyclical recovery to lift exports on a broad front. Because of the high cost level in Norway, growth in exports of traditional goods is unlikely to keep pace with growth in international demand. In other words, Norwegian export firms will probably lose market shares. However, demand growth is expected to be strong enough for exports of traditional goods to contribute positively to growth in mainland GDP nonetheless. We have assumed that oil prices will rise through the projection period, with the result that export prices as a whole will rise substantially. A high rise in prices is expected for all product groups in 2012 and 2013.

Imports of goods and of services have followed roughly the same growth path for the past decade, and grown somewhat faster than traditional goods exports. The cyclical downturn in Norway started early in 2008.

Approximately 20 per cent of total demand is met by imports (see Box 3 in *Economic Surveys* 1/2010). As a result of the decline in demand, traditional imports fell almost 17 per cent in the second quarter of 2009 compared with the volume in the same quarter the previous year. On balance, the volume of imports in 2009 was 10 per cent lower than in 2008. Imports of traditional goods showed the largest decline by a clear margin, but imports of services also fell. Marked changes in the composition of demand due to sharply reduced investment and car purchases contributed to the decline. Imports, like exports, show virtually zero growth in volume in the beginning of 2010 after adjustment for seasonal fluctuations. Import prices rose in the first quarter of 2010, slightly for goods and considerably for services.

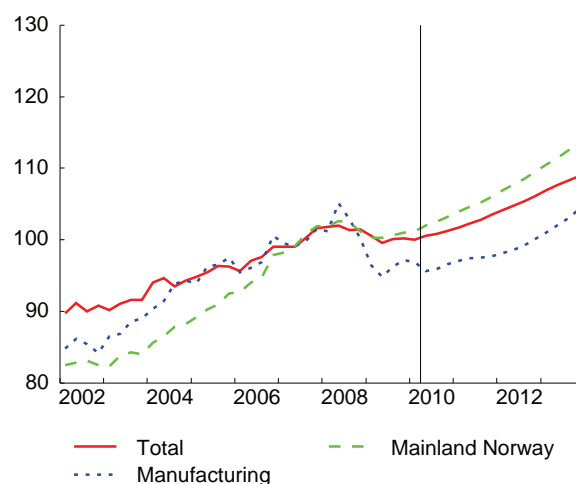
In the period 2010-2013 we expect imports to receive a particularly positive impetus from investment growth, which will pick up sharply from 2011 after a couple of weak years. Investment has a high import share, and the investment growth will therefore stimulate imports considerably. This year the Armed Forces will be importing two Hercules aircraft and two helicopters. A further twelve helicopters are expected to be delivered in 2011-2013, about four each year. The last of four frigates will be delivered in 2011. Imports of military material can have a strong effect on import figures but have no significant effects on the Norwegian economy. The rise in import prices is expected to pick up from the low or negative rates in 2009, and most strongly for traditional imports of goods and services. We expect a terms of trade gain each year of the projection period nonetheless, since the rise in import prices is expected to remain lower than the rise in export prices, even when oil and gas are excluded.

The trade surplus fell from NOK 487 billion in 2008 to NOK 352 billion in 2009. The 28 per cent slump can be explained by a terms of trade loss. Prices for oil and gas and traditional Norwegian export goods fell far more than prices for Norwegian import products. In terms of volume, the fall in exports was substantially less than the fall in imports, which in isolation improved the trade balance. Rising oil prices will contribute strongly to pushing up the trade surplus during the projection period. Projections indicate that the surplus may exceed NOK 440 billion in 2012 and 2013. Continued growth of the Government Pension Fund Global and its disbursements is expected to reduce the income and current transfers deficit. The current account surplus could accordingly be equivalent to 14-15 per cent of GDP in the projection period.

End of four years of cyclical downturn in 2011

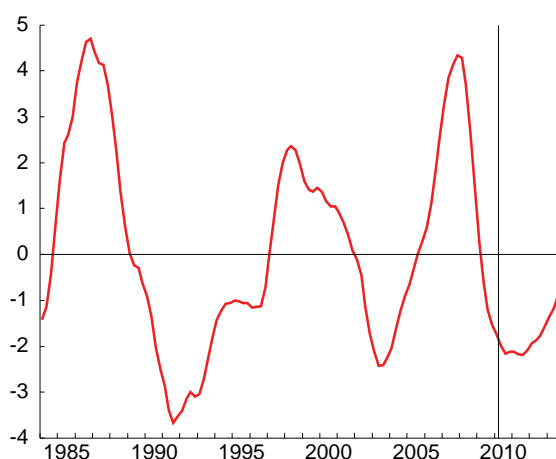
The Norwegian economy is still in a cyclical downturn that is primarily due to weak developments in domestic demand and in Norwegian export markets. Norway's cost-competitiveness has also deteriorated since late 2008/early 2009. Seasonally-adjusted QNA figures

Figur 11. **Gross domestic product. Seasonally adjusted volume indices. 2007=100**



Source: Statistics Norway.

Figur 12. **Output gap, Mainland Norway. Deviation from trend, per cent**



Source: Statistics Norway.

show mainland GDP growth of only 0.1 per cent in the first quarter of 2010 compared with the previous quarter, after slightly higher growth through the previous half year. As a result of the slump in activity in the mainland economy in the winter of 2008/2009 in the wake of the financial crisis, mainland GDP was nonetheless 1.4 per cent lower in the first quarter of 2010 than in the second quarter of 2008. If general government is excluded, the decline in the period was 2.4 per cent. Since summer 2009, general government production growth has been just a little higher than business sector production growth, so the difference stems from developments in the period when the activity level fell in the private sector.

Activity developments vary considerably from one industry to the next. After a certain decline through the second half of last year, mainland-based service industries experienced a definite upswing and recorded

1.0 per cent growth in value added in the first quarter of 2010. Positive and in some cases high growth was recorded in all major industries except transport. On balance, production in the service industries has followed a far more stable course through the downturn than goods-producing industries.

The financial crisis hit the export-oriented part of manufacturing hard. After the situation in large sectors of the world economy stabilised, and the strong growth in Asia continued, many manufacturing industries experienced a sharp recoil through the second half of last year. This effect was less pronounced in the first quarter, while developments in manufacturing production aimed at the petroleum industry remained weak. Overall, there was a slight decline in value added in manufacturing and mining in the first quarter of this year of 0.3 per cent following an increase of 2.4 per cent through the second half of 2009.

The largest negative contribution to manufacturing growth came in the first quarter from ship- and platform-building. Activities in this industry have developed in a fairly atypical manner, since there was still strong growth in the winter of 2009, but subsequently a decline. The first quarter of 2010 was down 1.8 per cent on the previous quarter and a full 6 per cent lower than the same quarter of the previous year. Deliveries of investment goods from this industry to the petroleum industry are affected by changes in the framework conditions for petroleum activities with a considerable time lag. The choice of development solutions is of great importance, and activity in the industry may be characterised by individual projects. The direct significance for manufacturing as a whole is moderate since the industry accounted for just under 15 per cent of value added in manufacturing in 2009. A separate article on how the demand from the petroleum industry affects the Norwegian economy in *Økonomiske analyser* (Norwegian text), that concludes that petroleum investment, direct and indirect, is of importance to the great majority of Norwegian industries.

The machinery industry, which accounts for over a third of manufacturing value added, records some increase in activity through the past half year. However, the strongest contributions to growth in the first quarter of this year come from production of chemicals. Owing to increased capacity, production in this industry has never been at a higher level. Production has also increased recently in other commodity-based manufacturing excluding the refining industry.

According to the preliminary QNA figures, value added in other goods production declined by more than 2 per cent in the first quarter after developments in power supply and primary industries provided a sharp boost through the second half of 2009. The building and construction industry recorded by far the largest decline in the first quarter. The decline in value added of more than 4 per cent followed an overall fall of the

same magnitude through the previous one and a half year. Since the publication of the QNA figures, however, the production index for building and construction has been revised sharply upwards for the whole of 2009. The effect in isolation of the revision is an upward adjustment in activity growth in the industry estimated at an annualised 4 percentage points for 2009. This is equivalent to 0.3 percentage point of mainland GDP growth. The production index for the first quarter also showed a distinctly less pronounced decline than that forming the basis for the QNA estimates. In isolation, the effect on GDP growth in the first quarter was an increase of 0.1 percentage point for mainland GDP and an approximate halving of the decline in the building and construction industry.

The decline in the building and construction industry in the first quarter appears to have been large regardless, and may be partly attributable to the particularly cold winter. On the demand side, the fall in housing investment has gradually slowed, but there is a stronger decline in mainland business investment in addition to a pronounced decline in public sector investment. Developments in the power sector also contributed to the first quarter fall in value added in "other goods production". However, precipitation is the underlying cause in this case. Despite high prices, production declined. In the primary industries, by contrast, growth through the second half of last year continued in the first quarter of 2010. Value added in fishing and fish-farming has increased by almost 30 per cent in volume in the course of a year and a half.

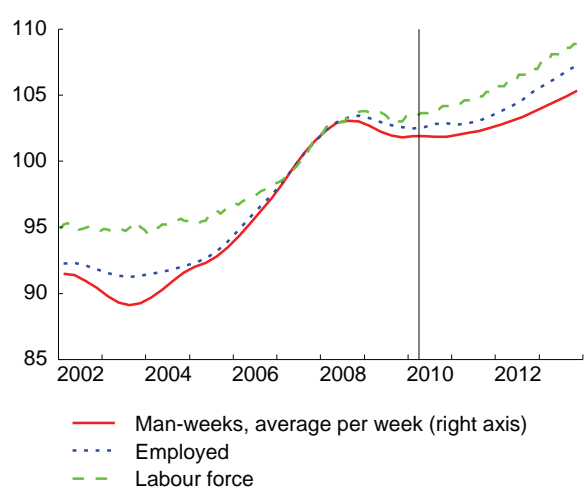
Growth in private domestic demand is expected to pick up slightly in the period ahead. However, growth in Norwegian export markets, which was relatively high through the winter of 2009-2010, is expected to decline somewhat over the next two years. Higher Norwegian costs as a result of relatively high wage growth and a stronger krone will dampen growth in output.

Manufacturing output is therefore expected to grow moderately over the next couple of years, and more strongly in 2013. Activity in building and construction, on the other hand, will probably pick up gradually. Mainland-based service production is largely focused on the domestic market and activity is expected to increase, but not as strongly as in the first quarter. On an annual basis, we expect the growth rate to gather pace gradually in the years ahead.

As private sector activity picks up, the increase in general government value added is expected to account for a considerably smaller share of overall activity growth in the period ahead. Public sector production growth will be appreciably reduced from 2009 to 2010. In subsequent years it will be further reduced due to a tighter fiscal policy.

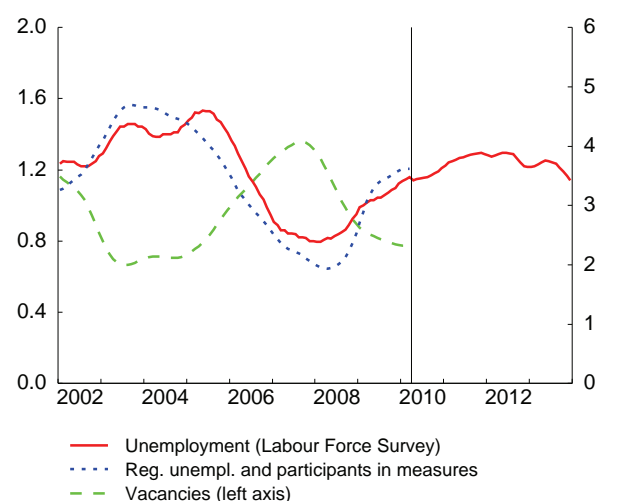
Growth in mainland GDP will increase gradually but moderately going forward. It will be possible to

Figur 13. Labour force, employment and number of manhours. Seasonally adjusted and smoothed indices. 2007=100



Source: Statistics Norway.

Figur 14. Unemployment and number of vacancies. Seasonally adjusted and smoothed. Per cent of labour force



Source: The Norwegian Labour and Welfare Service and Statistics Norway.

describe the remainder of 2010 and probably also 2011 as a moderate cyclical downturn as growth in mainland GDP will remain somewhat lower than trend on balance. We expect mainland GDP as an annual average to rise by 1.6 per cent in 2010 and 2.7 per cent in 2011. In 2012 we forecast that the economic situation in Norway will turn around into a moderate recovery. Growth may then reach over 3 per cent in 2012 and be slightly higher the following year. However, the turnaround is not expected to be strong enough to prevent the level of mainland GDP remaining slightly below trend in 2013 as well, so that Norway will remain in a moderate recession.

Unemployment still rising

In the first quarter of 2010, seasonally-adjusted employment fell by 4 300 persons, or 0.2 per cent. The slight rise of just over 2 000 persons in the previous quarter thus proved to be temporary. Public sector employment increased less in the first quarter than in any quarter last year, and cutbacks took place in both the service industries and manufacturing. Developments have nonetheless been weakest in building and construction. The decline of over 4 000 persons in the first quarter of 2010 is equivalent to 2.3 per cent of employment in this industry. However, order backlogs in building and construction climbed by 9 per cent in the first quarter of 2010 after remaining at a stable, low level since the fourth quarter of 2008. This may indicate that the decline is slowing to a halt.

While unemployment registered with the Norwegian Labour and Welfare Organisation (NAV) increased by 3-4 000 persons monthly from October 2008 to May 2009, on the whole unemployment has increased by less than 1 000 persons monthly for the past year. There was also a decline in unemployment in some of the months, and in May this year registered unemployment fell by 1 600 persons. This is the highest decline in unemployment recorded since May 2007. Almost 74

000 were registered as unemployed in May, while some 90 000 were either unemployed or on labour market programmes. Unadjusted registered unemployment figures for different job-seeker durations show a decline in the number of short-term unemployed, while long-term unemployment continues to rise. This may indicate that fewer have become unemployed, but that it is still difficult to find work.

The Labour Market Survey (LFS) publishes statistics on the number unemployed as a three-month moving average. In the first half of 2009, LFS unemployment was fairly stable at just under 80 000, but since June last year unemployment has risen steadily to just over 90 000 in March this year. This accounted for 3.5 per cent of the labour force.

In isolation, growth in the working age population will increase the supply of labour in Norway in the period ahead. As a result of high immigration, the population of men aged from 25 to 61 is growing particularly fast. Since this age group has a high labour force participation rate, in isolation this increases the average labour force participation rate. The increase in the population aged over 67 has the opposite effect. In addition we find that some people, particularly in the younger age groups, are now withdrawing from the labour market as unemployment rises. Many of them take further education. On balance we estimate labour supply growth in 2010 at about 6 000 persons, or 0.2 per cent, and that growth will rise from 0.9 per cent in 2011 to 2.0 per cent in 2013.

We anticipate that rising production will gradually be reflected in increased man-hours worked, but that it will take time before this is clearly reflected in a rise in employment. Since fiscal policy is assumed to be less expansionary in the next few years, general government employment will increase at a slower pace than in recent years. At the same time, employment in

manufacturing and building and construction will not fall as much as in 2009. Service industry employment is expected to fall somewhat this year but then to rise through the projection period. On balance, employment is expected to fall somewhat this year and then grow moderately for the next few years.

Since the labour force is growing faster than employment, unemployment is assumed to increase in the period ahead. Unemployment in 2010 is estimated at 3.5 per cent, increasing to about 4 per cent in the years 2011 to 2013. LFS unemployment will then be just over 100 000.

Low wage growth and improved profitability

Annual wage growth in 2009 was revised up by 0.4 percentage point to 4.5 per cent in connection with the publication of the QNA for the first quarter of this year. Wage growth in 2008 was 6.3 per cent. Over half of last year's wage growth was the full-year effect of the pay increases granted through 2008. The pay increases in last year's wage settlement only contributed about 0.5 percentage point. The slowing wage growth is partly attributable to the steep decline in output and weaker profitability of Norwegian manufacturing enterprises coupled with rising unemployment. These factors have also affected this year's wage settlements, which appear to be ending up with frameworks estimated by the parties themselves as annual wage growth in 2010 of around 3-3½ per cent.

Although real wage growth in Norway in the 2000s has been unusually high, Norwegian manufacturing enterprises as a whole have enjoyed very solid profitability in the same period. Even after the global financial crisis and a considerable decline in demand in international markets, Norwegian manufacturers have maintained relatively satisfactory profitability. This can be attributed to high petroleum investment and the fact that product prices have fallen from a very high level. Seasonally-adjusted QNA figures for the first quarter of this year show that value added in manufacturing has fallen by about 8 per cent compared with the second quarter of 2008, thereby reverting to the level in 2006 in both constant and current prices. In 2006, labour costs in Norwegian manufacturing measured as a share of factor income also touched a historic low. We estimate the labour cost share in 2010 at approximately 70 per cent, which is 6 percentage points higher than in 2006, but still low in a historical perspective.

The global decline in demand has impacted the manufacturing production of many of Norway's trading partners harder than Norwegian production. Norwegian manufacturing produces mainly semi-finished goods, for which there is steadily increasing demand from the Chinese manufacturing industry, among others. Many European countries and the USA are increasingly manufacturing consumer goods in competition with China. Thus there is reason to believe that growth in

manufacturing wages in other countries will be very low in the wake of the financial crisis. Moreover, high government debt in many countries has resulted in wage cuts among public sector employees, which will probably also have spillover effects for the wage level in the private sector. The low cost level abroad will probably spread to enterprises in competition with Norwegian manufacturing enterprises, causing downward pressure on Norwegian wages as well.

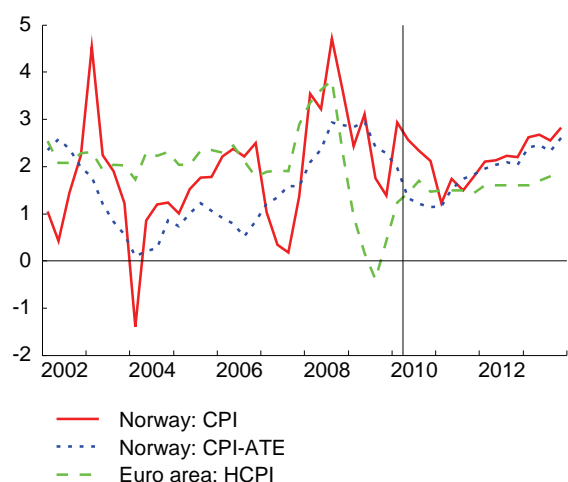
We estimate that wage growth in Norway will be 3.4 per cent this year and in 2011 and will pick up thereafter. The projections are based on the fact that manufacturing enterprises and the competitiveness of internationally exposed Norwegian industry will continue to set the framework for settlements. This factor, coupled with developments in the Norwegian and global economy generally, leads us to believe that this wage growth is sufficiently low to prevent a further deterioration in the profitability of Norwegian manufacturing enterprises. There is reason to believe that increased productivity growth and higher export prices will contribute to improving profitability somewhat when demand begins to pick up worldwide – albeit not up to the level in 2006.

The issue of pay increases to achieve equality, i.e. special pay increases to bring women's pay up to the level of men's in occupations dominated by women in the public sector, has sparked a number of strikes in connection with the 2010 settlement. Employer representatives have held the view that such a pay increase must be made within the frameworks set by the settlement in manufacturing industry. This means that public sector occupations dominated by men must get lower pay increases than in manufacturing. This was the background to the requirement from public sector unions that an increase to bring about gender wage equality must be additional to the frameworks set by manufacturing. The demand from the unions was not met in this year's negotiations. In our projections for the years ahead we have not assumed special gender equality pay increases in the public sector over and above the frameworks set by manufacturing. However, our projections do not exclude the possibility that there redistribution may take place within these frameworks.

Low inflation

There has been a clear falling tendency in underlying inflation through the past year. The 12-month rise in the consumer price index adjusted for tax changes and excluding energy products (CPI-ATE) has been 1.7 per cent for the past two months, down from 3.3 per cent in June 2009. During this period there has been a falling tendency for the majority of product groups. Seasonally-adjusted figures show that the rise in the CPI-ATE through the first four months of the year was only an annualised 1.0 per cent. Almost the whole increase took place from December last year to January this year.

Figur 15. Consumer price indices. Percentage growth from the same quarter previous year



Source: Statistics Norway.

A breakdown of the CPI-ATE by supplier sector shows slower year-on-year inflation for all main groups since the summer of 2009. A slower rise in prices for imported consumer goods accounted for almost half of the decline in inflation from June last year to April this year.

The depreciation of the krone in the wake of the financial crisis in autumn 2008 contributed to an accelerating rise in prices for imported consumer goods through 2009. The krone strengthened through 2009 and into 2010, which slowed inflation. Changes in the exchange rate affect prices to households for both imported and domestically produced goods. Imported goods are factor inputs in Norwegian production, and experience shows that it takes a good while before the effects of changes in the exchange rate on Norwegian consumer prices are exhausted. The global downturn and slower rise in labour costs have also contributed to curbing underlying inflation in Norway.

The slower rise in Norwegian labour costs, higher productivity growth and the appreciation of the krone that have already taken place will contribute to curbing underlying inflation for a while to come. In recent weeks, exchange rates have fluctuated so widely that price impulses from abroad now appear more uncertain than when the previous *Economic Survey* was published. The most probable scenario appears to be that in the short term the krone will become somewhat weaker than previously assumed, and thereafter strengthen a little through 2011. In our projections, a certain weakening of the krone will then push inflation up slightly in 2013.

We expect trade with low-cost countries to continue increasing throughout the projection period. In isolation, this will contribute to a continued low rise in import prices. A slow business cycle recovery is expected to cause productivity growth to pick up throughout the

period. With prospects of wage growth that is low by Norwegian standards coupled with moderate global inflation, Norwegian inflation will probably also be relatively low. CPI-ATE inflation is projected to come down to an annualised average of 1.4 per cent for 2010. The indirect effects of higher energy prices and reduced negative price impulses from imported consumer goods will then contribute to the rise in the CPI-ATE gradually increasing to 2.4 per cent in 2013.

The movements of the CPI-ATE provide information about underlying price inflation. However, it is developments in the consumer price index (CPI) that are relevant for actual developments in household purchasing power. Energy prices and electricity prices in particular often impart strong direct impulses to the CPI. Developments in electricity prices brought the year-on-year rise in the CPI in October last year down to 0.6 per cent, i.e. 1.5 percentage points lower than the rise in the CPI-ATE. Five months later, in March this year, the situation was completely reversed. During this period, electricity prices rose by almost 50 per cent. CPI inflation rose to 3.4 per cent, 1.7 percentage points higher than CPI-ATE inflation. Following a very tight electricity market this past winter, electricity prices have begun to fall. Average electricity prices to households showed a moderate decline from March to April, and CPI inflation in April was measured at 3.3 per cent.

No major changes in electricity prices appear to be imminent. On the basis of Nordpool futures prices at the end of May, electricity prices, as they are measured in the CPI, are projected to be 22 per cent higher as an annual average this year than last. A moderate price fall is then expected next year and approximately unchanged prices in 2012. In 2013, electricity prices are expected to rise more in pace with the general rise in prices.

We assume that there will be no changes in indirect taxes other than those that have now been decided on for 2010 and which were mainly adjusted for inflation. However, both oil and electricity prices are expected to increase more than inflation generally this year. This means that the projected CPI rise of 2.5 per cent will be distinctly higher than the rise in the CPI-ATE in 2010.

For subsequent years we assume, as usual, that indirect taxes will be adjusted for inflation. Oil prices are assumed to increase throughout the projection period. With real prices for oil and electricity moving in opposite directions, the CPI is expected to rise in much the same way as the CPI-ATE in 2011. Electricity prices will rise somewhat after a while and cause the CPI to increase somewhat more than underlying inflation and to rise to over 2.5 per cent towards the end of the projection period.

Table 4. National accounts: Final expenditure and gross domestic product. At constant 2007 prices. Million kroner

	Unadjusted		Seasonally adjusted							
	2008	2009	08.2	08.3	08.4	09.1	09.2	09.3	09.4	10.1
Final consumption expenditure of households and NPISHs	951 832	953 102	239 399	236 876	234 692	233 688	236 770	239 867	243 080	244 605
Household final consumption expenditure	913 602	913 604	229 760	227 292	225 192	223 997	226 972	229 944	232 973	234 620
Goods	467 414	466 170	118 340	115 780	114 069	112 916	115 240	117 830	120 145	120 567
Services	413 072	416 484	103 180	103 340	103 560	103 297	103 961	104 513	104 830	105 457
Direct purchases abroad by resident households	59 614	55 604	14 968	14 626	14 186	13 829	13 816	13 633	14 538	14 896
Direct purchases by non-residents	-26 499	-24 654	-6 728	-6 453	-6 623	-6 046	-6 045	-6 032	-6 539	-6 300
Final consumption expenditure of NPISHs	38 230	39 498	9 639	9 584	9 500	9 692	9 799	9 923	10 107	9 985
Final consumption expenditure of general government	464 633	487 058	115 666	116 726	117 388	120 400	121 589	122 963	122 052	123 325
Final consumption expenditure of central government	240 672	252 693	59 871	60 352	60 947	62 525	63 075	63 409	63 663	63 907
Central government, civilian	208 565	220 402	51 822	52 329	52 770	54 481	54 762	55 320	55 817	55 945
Central government, defence	32 107	32 291	8 049	8 023	8 177	8 043	8 313	8 089	7 846	7 962
Final consumption expenditure of local government	223 961	234 365	55 795	56 374	56 440	57 875	58 513	59 554	58 389	59 418
Gross fixed capital formation	510 898	470 445	127 736	129 848	127 016	119 687	119 770	113 707	117 094	104 224
Extraction and transport via pipelines	112 247	117 386	27 156	28 650	29 269	32 250	29 932	27 656	27 595	28 402
Service activities incidental to extraction	-421	-179	-25	-233	-174	-198	-76	217	-122	-279
Ocean transport	19 961	18 379	5 071	4 554	4 901	3 926	4 738	5 145	4 554	1 538
Mainland Norway	379 112	334 859	95 535	96 877	93 020	83 709	85 177	80 688	85 067	74 563
Mainland Norway excluding general government	304 497	255 177	78 160	75 870	73 992	66 765	66 000	61 656	60 754	58 525
Industries	216 226	183 580	55 694	53 662	53 464	47 475	47 851	44 260	43 871	41 860
Manufacturing and mining	34 165	23 894	8 818	8 614	8 854	6 748	6 946	5 428	4 821	5 132
Production of other goods	38 217	31 675	10 090	9 843	8 715	7 735	8 207	8 265	7 461	7 011
Services	143 844	128 011	36 787	35 204	35 895	32 992	32 698	30 568	31 588	29 717
Dwellings (households)	88 270	71 597	22 466	22 209	20 529	19 290	18 150	17 396	16 883	16 666
General government	74 615	79 681	17 375	21 007	19 028	16 944	19 176	19 032	24 313	16 037
Changes in stocks and statistical discrepancies	43 185	-9 194	8 517	14 101	5 853	-743	1 737	-1 248	-7 761	1 305
Gross capital formation	554 083	461 251	136 254	143 950	132 869	118 944	121 507	112 459	109 333	105 529
Final domestic use of goods and services	1 970 547	1 901 410	491 319	497 552	484 948	473 032	479 866	475 289	474 464	473 458
Final demand from Mainland Norway	1 795 576	1 775 018	450 600	450 479	445 100	437 797	443 536	443 518	450 199	442 492
Final demand from general government	539 248	566 739	133 041	137 733	136 415	137 344	140 765	141 995	146 365	139 362
Total exports	1 049 134	1 007 185	266 558	256 911	259 956	254 273	244 059	252 893	255 375	254 765
Traditional goods	315 309	290 675	80 302	80 044	74 691	70 437	69 659	75 272	75 306	75 545
Crude oil and natural gas	470 254	464 732	118 342	112 289	119 610	119 297	112 290	117 453	115 604	113 709
Ships, oil platforms and planes	14 215	14 057	3 361	4 700	3 646	4 934	3 333	2 789	3 002	5 452
Services	249 356	237 722	64 553	59 878	62 009	59 605	58 776	57 379	61 464	60 059
Total use of goods and services	3 019 681	2 908 595	757 877	754 464	744 905	727 304	723 925	728 182	729 840	728 224
Total imports	706 843	633 740	178 499	178 714	168 413	155 781	158 418	159 587	160 587	159 749
Traditional goods	456 080	396 060	116 449	114 369	105 575	99 301	98 055	99 537	99 225	102 320
Crude oil and natural gas	3 685	4 830	749	652	1 658	636	842	1 893	1 483	814
Ships, oil platforms and planes	28 969	26 495	6 845	9 030	6 617	4 542	6 571	5 588	9 795	5 164
Services	218 109	206 354	54 456	54 663	54 564	51 302	52 950	52 569	50 084	51 451
Gross domestic product (market prices)	2 312 838	2 274 856	579 378	575 749	576 491	571 523	565 507	568 594	569 252	568 474
Gross domestic product Mainland Norway (market prices)	1 762 458	1 734 223	442 482	441 791	436 066	432 266	432 403	433 853	435 604	436 252
Petroleum activities and ocean transport	550 380	540 633	136 896	133 958	140 426	139 257	133 104	134 741	133 649	132 222
Mainland Norway (basic prices)	1 504 957	1 485 082	377 302	378 133	373 891	370 053	370 387	371 363	373 179	374 114
Mainland Norway excluding general government	1 172 909	1 143 870	295 154	294 674	290 237	285 400	285 279	285 833	287 223	287 965
Manufacturing and mining	214 001	201 287	54 965	53 764	52 368	50 413	49 596	50 314	50 807	50 660
Production of other goods	174 377	166 026	44 055	44 229	42 577	41 617	40 241	41 824	42 399	41 439
Services incl. dwellings (households)	784 531	776 557	196 134	196 680	195 293	193 370	195 441	193 696	194 017	195 866
General government	332 048	341 212	82 148	83 460	83 654	84 653	85 108	85 530	85 956	86 149
Taxes and subsidies products	257 501	249 141	65 180	63 658	62 174	62 213	62 016	62 490	62 424	62 138

Source: Statistics Norway.

Table 5. National accounts: Final expenditure and gross domestic product. At constant 2007 prices. Percentage change from the previous period

	Unadjusted		Seasonally adjusted							
	2008	2009	08.2	08.3	08.4	09.1	09.2	09.3	09.4	10.1
Final consumption expenditure of households and NPISHs	1.3	0.1	-0.4	-1.1	-0.9	-0.4	1.3	1.3	1.3	0.6
Household final consumption expenditure	1.2	0.0	-0.4	-1.1	-0.9	-0.5	1.3	1.3	1.3	0.7
Goods	-0.2	-0.3	-0.1	-2.2	-1.5	-1.0	2.1	2.2	2.0	0.4
Services	2.0	0.8	0.2	0.2	0.2	-0.3	0.6	0.5	0.3	0.6
Direct purchases abroad by resident households	6.3	-6.7	-6.5	-2.3	-3.0	-2.5	-0.1	-1.3	6.6	2.5
Direct purchases by non-residents	0.0	-7.0	0.6	-4.1	2.6	-8.7	0.0	-0.2	8.4	-3.7
Final consumption expenditure of NPISHs	3.0	3.3	1.2	-0.6	-0.9	2.0	1.1	1.3	1.9	-1.2
Final consumption expenditure of general government	4.1	4.8	0.8	0.9	0.6	2.6	1.0	1.1	-0.7	1.0
Final consumption expenditure of central government	3.3	5.0	0.7	0.8	1.0	2.6	0.9	0.5	0.4	0.4
Central government, civilian	3.4	5.7	0.4	1.0	0.8	3.2	0.5	1.0	0.9	0.2
Central government, defence	2.8	0.6	2.2	-0.3	1.9	-1.6	3.4	-2.7	-3.0	1.5
Final consumption expenditure of local government	4.8	4.6	0.9	1.0	0.1	2.5	1.1	1.8	-2.0	1.8
Gross fixed capital formation	1.4	-7.9	1.2	1.7	-2.2	-5.8	0.1	-5.1	3.0	-11.0
Extraction and transport via pipelines	3.7	4.6	-0.3	5.5	2.2	10.2	-7.2	-7.6	-0.2	2.9
Service activities incidental to extraction	-108.9	-57.4	-320.9	819.7	-25.3	13.9	-61.4	-383.8	-156.1	128.9
Ocean transport	29.3	-7.9	-6.2	-10.2	7.6	-19.9	20.7	8.6	-11.5	-66.2
Mainland Norway	1.0	-11.7	2.1	1.4	-4.0	-10.0	1.8	-5.3	5.4	-12.3
Mainland Norway excluding general government	0.1	-16.2	2.3	-2.9	-2.5	-9.8	-1.1	-6.6	-1.5	-3.7
Industries	6.1	-15.1	4.4	-3.6	-0.4	-11.2	0.8	-7.5	-0.9	-4.6
Manufacturing and mining	10.2	-30.1	11.2	-2.3	2.8	-23.8	2.9	-21.9	-11.2	6.4
Production of other goods	17.3	-17.1	6.1	-2.4	-11.5	-11.2	6.1	0.7	-9.7	-6.0
Services	2.5	-11.0	2.5	-4.3	2.0	-8.1	-0.9	-6.5	3.3	-5.9
Dwellings (households)	-12.1	-18.9	-2.5	-1.1	-7.6	-6.0	-5.9	-4.2	-2.9	-1.3
General government	4.7	6.8	0.8	20.9	-9.4	-11.0	13.2	-0.8	27.7	-34.0
Changes in stocks and statistical discrepancies	31.8	-121.3	-34.5	65.6	-58.5	-112.7	-333.6	-171.8	522.0	-116.8
Gross capital formation	3.2	-16.8	-2.2	5.6	-7.7	-10.5	2.2	-7.4	-2.8	-3.5
Final domestic use of goods and services	2.5	-3.5	-0.6	1.3	-2.5	-2.5	1.4	-1.0	-0.2	-0.2
Final demand from Mainland Norway	1.9	-1.1	0.4	0.0	-1.2	-1.6	1.3	0.0	1.5	-1.7
Final demand from general government	4.1	5.1	0.8	3.5	-1.0	0.7	2.5	0.9	3.1	-4.8
Total exports	0.9	-4.0	0.8	-3.6	1.2	-2.2	-4.0	3.6	1.0	-0.2
Traditional goods	4.3	-7.8	0.4	-0.3	-6.7	-5.7	-1.1	8.1	0.0	0.3
Crude oil and natural gas	-2.0	-1.2	-1.0	-5.1	6.5	-0.3	-5.9	4.6	-1.6	-1.6
Ships, oil platforms and planes	11.5	-1.1	34.1	39.8	-22.4	35.3	-32.4	-16.3	7.6	81.6
Services	1.9	-4.7	3.3	-7.2	3.6	-3.9	-1.4	-2.4	7.1	-2.3
Total use of goods and services	1.9	-3.7	-0.1	-0.5	-1.3	-2.4	-0.5	0.6	0.2	-0.2
Total imports	2.2	-10.3	-1.1	0.1	-5.8	-7.5	1.7	0.7	0.6	-0.5
Traditional goods	-0.4	-13.2	-2.2	-1.8	-7.7	-5.9	-1.3	1.5	-0.3	3.1
Crude oil and natural gas	-36.0	31.1	21.2	-12.9	154.1	-61.7	32.5	124.8	-21.7	-45.1
Ships, oil platforms and planes	47.0	-8.5	5.7	31.9	-26.7	-31.4	44.7	-15.0	75.3	-47.3
Services	4.9	-5.4	0.2	0.4	-0.2	-6.0	3.2	-0.7	-4.7	2.7
Gross domestic product (market prices)	1.8	-1.6	0.2	-0.6	0.1	-0.9	-1.1	0.5	0.1	-0.1
Gross domestic product Mainland Norway (market prices)	2.2	-1.6	0.7	-0.2	-1.3	-0.9	0.0	0.3	0.4	0.1
Petroleum activities and ocean transport	0.6	-1.8	-1.4	-2.1	4.8	-0.8	-4.4	1.2	-0.8	-1.1
Mainland Norway (basic prices)	2.7	-1.3	0.8	0.2	-1.1	-1.0	0.1	0.3	0.5	0.3
Mainland Norway excluding general government	2.5	-2.5	1.2	-0.2	-1.5	-1.7	0.0	0.2	0.5	0.3
Manufacturing and mining	2.3	-5.9	3.9	-2.2	-2.6	-3.7	-1.6	1.4	1.0	-0.3
Production of other goods	3.4	-4.8	1.8	0.4	-3.7	-2.3	-3.3	3.9	1.4	-2.3
Services incl. dwellings (households)	2.4	-1.0	0.3	0.3	-0.7	-1.0	1.1	-0.9	0.2	1.0
General government	3.5	2.8	-0.4	1.6	0.2	1.2	0.5	0.5	0.5	0.2
Taxes and subsidies products	-0.7	-3.2	-0.1	-2.3	-2.3	0.1	-0.3	0.8	-0.1	-0.5

Source: Statistics Norway.

Table 6. National accounts: Final expenditure and gross domestic product. Price indices. 2007=100

	Unadjusted		Seasonally adjusted							
	2008	2009	08.2	08.3	08.4	09.1	09.2	09.3	09.4	10.1
Final consumption expenditure of households and NPISHs	103.7	106.3	102.7	104.2	105.8	105.9	106.2	106.5	106.4	109.0
Final consumption expenditure of general government	105.9	109.5	104.4	106.8	109.2	108.6	109.2	109.8	110.3	111.4
Gross fixed capital formation	106.1	109.4	105.0	106.9	109.5	108.3	109.4	111.1	109.0	112.3
Mainland Norway	105.1	107.8	104.1	105.7	107.6	106.8	107.9	108.7	108.3	108.5
Final domestic use of goods and services	104.3	107.7	102.8	105.7	106.2	107.9	106.9	108.2	107.5	110.4
Final demand from Mainland Norway	104.6	107.5	103.4	105.2	107.1	106.8	107.3	107.8	107.8	109.6
Total exports	116.5	100.2	120.8	120.0	112.9	101.9	99.6	98.4	100.1	101.2
Traditional goods	102.4	95.7	100.8	106.4	105.1	96.7	95.4	97.5	93.9	94.3
Total use of goods and services	108.6	105.1	109.1	110.5	108.5	105.8	104.5	104.8	104.9	107.1
Total imports	104.0	103.6	102.8	104.6	107.5	104.9	104.4	103.8	101.1	104.0
Traditional goods	104.6	103.3	103.4	105.4	108.4	106.2	103.9	103.0	100.3	101.2
Gross domestic product (market prices)	110.0	105.5	111.1	112.4	108.8	106.0	104.5	105.1	106.0	108.0
Gross domestic product Mainland Norway (market prices)	103.2	106.5	102.1	104.3	105.1	105.4	106.4	107.1	107.3	108.1

Source: Statistics Norway.

Table 7. National accounts: Final expenditure and gross domestic product. Price indices. Percentage change from previous period

	Unadjusted		Seasonally adjusted							
	2008	2009	08.2	08.3	08.4	09.1	09.2	09.3	09.4	10.1
Final consumption expenditure of households and NPISHs	3.7	2.5	0.5	1.4	1.5	0.1	0.3	0.2	-0.1	2.5
Final consumption expenditure of general government	5.9	3.4	1.3	2.3	2.3	-0.6	0.6	0.5	0.4	1.0
Gross fixed capital formation	6.1	3.1	2.2	1.8	2.4	-1.1	1.1	1.5	-1.9	3.1
Mainland Norway	5.1	2.6	1.4	1.5	1.8	-0.7	1.0	0.8	-0.3	0.2
Final domestic use of goods and services	4.3	3.2	-0.9	2.8	0.5	1.6	-0.8	1.2	-0.7	2.6
Final demand from Mainland Norway	4.6	2.8	0.9	1.7	1.8	-0.3	0.5	0.4	0.0	1.7
Total exports	16.5	-14.0	7.8	-0.7	-5.9	-9.7	-2.3	-1.2	1.7	1.1
Traditional goods	2.4	-6.5	3.7	5.5	-1.3	-8.0	-1.4	2.2	-3.7	0.4
Total use of goods and services	8.6	-3.2	2.4	1.3	-1.8	-2.5	-1.2	0.3	0.1	2.1
Total imports	4.0	-0.4	1.2	1.8	2.8	-2.5	-0.4	-0.6	-2.6	2.9
Traditional goods	4.6	-1.2	2.0	1.9	2.8	-2.1	-2.1	-0.9	-2.6	0.9
Gross domestic product (market prices)	10.0	-4.0	2.7	1.2	-3.2	-2.6	-1.4	0.6	0.8	1.9
Gross domestic product Mainland Norway (market prices)	3.2	3.3	0.5	2.1	0.8	0.3	1.0	0.6	0.2	0.8

Source: Statistics Norway.