NORWAY

TO ADDRESS INFLATION, A COORDINATED TIGHTENING OF THE POLICY MIX

After being severely hit by the Omicron variant, economic activity picked up again as of February, and the recovery is expected to continue with growth reaching 4% in 2022. Through no fault of its own, Norway is one of the big winners of the Russia-Ukraine conflict thanks to a substantial increase in oil and gas revenues, which are expected to reach NOK 1,500 bn in 2022 (about EUR 143 bn). Although inflation is milder than in the other European countries, the Norwegian central bank has expressed its determination to tighten monetary conditions as much as necessary to break the inflationary momentum. To bring inflation within its target range, NorgesBank plans to gradually raise its key deposit rate to 2.5% by the end of 2023.

Norway was severely hit by the Omicron variant despite preventative health restrictions introduced in late 2021. Business slumped under these restrictions and mainland GDP (excluding oil and gas activities) declined by 1% m/m in January, before picking up again in February and March (+0.6% m/m and +1.2%, respectively). For the full quarter, Q1 2022 GDP contracted 0.6% q/q, but is still 2.7% higher than the pre-pandemic level. As a major energy producer (the world's 8th and 15th largest producer of natural gas and oil, respectively), Norway is not very dependent on Russia (less than 8% of energy consumption) and consequently, is not hurt much by the Russia-Ukraine war. Through no fault of its own, the country is even one of the big winners of the conflict because it benefits from both higher energy prices and new orders from countries seeking to diversify their supply sources. Nordea Bank estimates that oil and gas revenues will reach nearly NOK 1,500 bn in 2022 (about EUR 143 bn).

Compared to the other European countries, Norway has not been hit as hard by rising inflation (+6.2% in May 2022 y/y, compared to a Eurozone average of 8.1%). Despite more moderate inflation, the government has introduced several measures to boost purchasing power: direct subsidies, electrical power tax cuts, and higher housing allowances. The total cost of these measures should near NOK 9 bn (EUR 860 m). Moreover, Norway's unemployment rate has fallen to a very low level (2.9% in March 2022) and the number of job vacancies has risen significantly (+41.4% y/y in Q1), increasing the bargaining power of workers. Labour unions and corporate management are anticipating wage increases of 4% in 2022 according to the NorgesBank quarterly survey for Q2 2022. Thanks to the limited erosion of purchasing power, household consumption is holding up well (+0.6% m/m in April) and largely surpasses the pre-pandemic level (by 4.8% compared to year-end 2019).

In the face of inflationary pressures, NorgesBank was one of the first central banks to begin normalising its monetary policy. After holding at 0% through September 2021, the key rate was raised by 25 basis points (bp) on three occasions. Yet with prices accelerating more rapidly than expected, the national statistics institute (SSB) foresees an exceptionally big 50bp rate increase at the end of June, which would be the biggest rate increase in a decade. To bring policy in line with its price stability target, i.e. core inflation of close to 2% in the medium term, the central bank has already announced that the deposit rate could rise to 2.5% by year-end 2023. At the same time, the government declared that it would do its part to fight inflation by limiting increases in public expenditure. This will entail the suspension of several construction projects. Norway thus stands apart for the co-ordination of the monetary and fiscal policy mix at a time when most of the other European countries are still pursuing support measures.

GROWTH & INFLATION

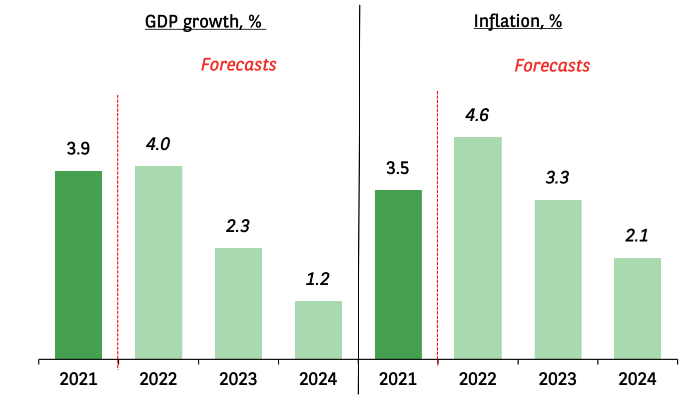

CHART 1 SOURCE: OECD, BNP PARIBAS

NORWAY: ACTIVITY INDICATORS

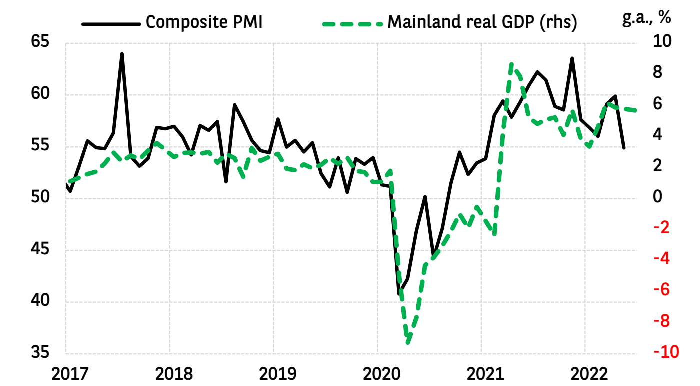

CHART 2 SOURCE: NIMA/DNB MARKETS, STATISTICS NORWAY, BNP PARIBAS

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