

# 1. The working group's recommendations

In June 2023, the Ministry of Finance appointed a working group composed of experts from Norges Bank (the central bank) and the Ministry of Finance to examine the effects of government transactions on the money market. The working group hereby presents its report.

The working group proposes a number of changes that, if accepted, will have an impact on the fluctuations and the level of structural liquidity in the banking system. The proposal to increase the number of petroleum tax instalments will reduce fluctuations in structural liquidity. In addition, changes are proposed that will ensure that the petroleum fund mechanism has a neutral effect on structural liquidity over time. The working group also proposes that funds accumulated in the government's treasury account as a result of previous deviations from liquidity neutrality in the petroleum fund mechanism should be transferred back to the Government Pension Fund Global (GPFG). The reversal will lead to an increase in the level of structural liquidity. In 2023, outstanding government debt increased less than the borrowing requirement. This implies that government borrowing in the years ahead is expected to drain liquidity from the banking system to account for the supply of liquidity in 2023. This will to some extent counteract the liquidity supply resulting from the transfer of funds from the government treasury account to the GPFG. Finally, the working group proposes that the government ceases to neutralize transfers of interest and dividends from Norges Bank by means of government debt issuance. In principle, structural liquidity will then rise in pace with the government's annual use of transfers from Norges Bank over the budget. The various proposals are described below.

## *Increase in the number of petroleum tax instalments*

The government treasury account is held at Norges Bank, outside of the private banking system. This causes fluctuations in structural liquidity in the banking system due to transactions between the government account and private banks. In recent years, petroleum taxes have fluctuated more and been larger than previously, and in the autumn of 2022 a large petroleum tax payment led to considerable turmoil in the money market. In order to make the system more robust to both fluctuations in petroleum prices and higher prices, the working group recommends that the Ministry of Finance issues for consultation a proposal to increase the number of petroleum tax instalments from six to ten and to distribute each of the two voluntary additional payments over several instalments, so that no single payment becomes very large. The proposal recommends that advance-based instalments be paid on 1 August, 1 September, 1 October, 1 November and 1 December of the fiscal year, while arrears be paid on 1 February, 1 March, 1 April, 2 May and 1 June of the following fiscal year. It is further recommended that the additional payment in the autumn be determined by the petroleum companies by 1 September and distributed equally between the terms of 1 September, 1 October, and 1 November, and likewise by 1 March in the spring, distributed equally between the terms of 1 March, 1 April and 2 May.

In the view of the working group, the proposed measures will reduce fluctuations in structural liquidity both in the event of high levels of petroleum prices and in the event of sharp changes in petroleum prices. The proposal is expected to have minor administrative consequences.

### ***Request to exempt F-loans from the "unwinding mechanism" in the liquidity regulation (LCR)***

The liquidity coverage ratio (LCR) regulation sets out the requirements for banks' liquidity buffers. Under the rules on the unwinding mechanism, banks must take into account all secured borrowing transactions maturing within 30 calendar days when calculating the composition of the liquidity buffer. This may limit banks' ability to participate in Norges Bank's F-loan auctions when structural liquidity falls to very low levels and may have been one of several factors behind the unrest in money markets in autumn 2022. Norges Bank has sent a letter to the Ministry of Finance requesting the Ministry to assess the Norwegian authorities' scope for exempting Norges Bank's F-loans from the rules on the unwinding mechanism. The Ministry of Finance has forwarded the letter to the Financial Supervisory Authority (FSA) and requested an assessment by the end of April 2024. The working group assumes that the Ministry of Finance will take a position on Norges Bank's request based on an assessment of the FSA.

### ***Transfer of funds from the government's treasury account to the Government Pension Fund Global and a new correction mechanism to ensure liquidity neutrality of the petroleum fund mechanism***

The petroleum fund mechanism channels government revenues from petroleum activities either to savings in the Government Pension Fund Global (GPFG) or to spending over the central government budget. The mechanism shall, in principle, have a neutral effect on liquidity in the banking system. However, the realized non-oil budget deficit has tended to be lower than projected in the budget. As a result, more funds have been transferred from the GPFG than necessary to cover the realized non-oil deficit. Because there is no mechanism to correct for such discrepancies, these funds have remained in the government's treasury account in Norges Bank. This has led to an increase in the government's cash holdings and a corresponding reduction in structural liquidity in the banking system. In the view of the working group, it is unfortunate that funds that should have been allocated to the GPFG for saving for future generations accumulate in the government's treasury account. The working group also considers that it is unfortunate if deviations from liquidity neutrality in government transactions contribute to uncertainty for banks in their liquidity management. The working group therefore recommends that the Ministry of Finance outline a proposal for an annual correction mechanism in connection with the revised national budget for 2024, which is proposed in the central government budget (Yellow Book) for 2025. The working group also recommends that the Ministry of Finance at the same time propose a transfer from the government's treasury account to the GPFG of the funds accumulated in the government's account as a result of the petroleum fund mechanism not being neutral. The working group estimates that the need for reversal is NOK 82.1 billion. The working group's proposal implies that NOK 82.1 billion will be exchanged from NOK to foreign currency for savings in the GPFG. If so, this will be included as part of the government's foreign currency need in 2025. The total foreign currency need in 2025 depends on a number of factors that are not known today. All else being equal, the proposal implies that the level of structural liquidity at the end of 2025 will be NOK 82.1 billion higher than without such a reversal.

In recent years, government borrowing has been somewhat lower than implied by borrowing requirements. This is because some of the estimated borrowing requirements have been financed by drawing on the government's cash holdings. Current practice in government debt management implies that Norges Bank may, if necessary, adjust borrowing so that loan transactions are liquidity neutral over time. All else being equal, this implies that government debt management will drain liquidity in the years ahead to take account of the liquidity supply in 2023. At the same time, this should be seen in the context of the need for predictability in borrowing from year to year and consideration for the government bond market in general.

***The practice of issuing government debt to neutralize transfers of interest and dividends from Norges Bank is being discontinued***

The government has its treasury account in Norwegian kroner in the central bank and owns Norges Bank. Norges Bank therefore pays interest and dividends to the government. The transfers of interest and dividends differ from other revenues in the central government budget in that the government receives “new” kroner created by Norges Bank. Transfers from Norges Bank to the government therefore do not affect liquidity in the banking system, unlike other payments to the government, which reduce liquidity in the banking system. When the government spends the transfers from Norges Bank over the budget, net liquidity is therefore supplied to the banking system. In order to neutralize this liquidity supply, the government issues government debt that drains liquidity from the banking system equivalent to total transfers.

Under the current practice for transfers and subsequent neutralization, the government's cash holdings increase annually corresponding to transfers of interest and dividends from Norges Bank, with a corresponding contribution to growth in outstanding government debt. The result is an increase in government debt and government cash holdings that the working group does not consider sustainable over time. Higher government debt and borrowing requirements may increase government bond yields and lead to higher government borrowing costs. The increased cash holdings cannot be utilized without supplying substantial liquidity to the banking system. The working group is of the view that it is not the government's use of transfers of interest and dividends from Norges Bank over the government budget that results in liquidity supply to the banking system, but rather the way in which Norges Bank conducts the transfer of funds in the first place. The working group's assessment is therefore that it is not incumbent on the government to neutralize this liquidity supply. The working group recommends that the government no longer neutralize transfers from Norges Bank, starting from the fiscal year 2025. Such a change will, in isolation, lead to a reduction in the estimated borrowing requirement from 2025 onwards. As a result, structural liquidity will increase as the transfer from Norges Bank is used over the central government budget. The transfers of interest and dividends from Norges Bank will partly depend on the balance on the government's account and the associated interest rate, as well as the return on Norges Bank's assets. The estimate for transfers of dividends and interest from Norges Bank to the government in 2024 is about NOK 35 billion.