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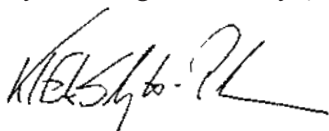
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Preface

This publication contains a summary in English of Norway's National Budget for 2002, presented to the Storting (Parliament) as Report no. 1 (2001-2002) on 11 October 2001. The National Budget presents the Government's programme for the implementation of economic policy and projections for the Norwegian Economy.

The main purpose of this English summary is to give a general picture of the Government's macroeconomic policy (Chapters 1-5), the macroeconomic forecasts (Chapter 7), and a review of some measures aimed at improving the functioning of the economy (Chapter 6).

Royal Norwegian Ministry of Finance



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Minister of Finance
October 2001*



Foto: Linda Cartridge

Introduction

Table 1. Estimates for 2001 and 2002

	Change from previous year, pct.	
	2001	2002
GDP	1.7	3.2
GDP Mainland Norway	1.2	1.9
Unemployment rate	3.4	3.4
Consumer price inflation	3.1	1.9
Current account surplus, NOK billion	196.3	180.7
Fiscal Budget Surplus, NOK billion	259.5	196.4
Structural, non-oil budget balance ¹⁾	-0.1	-0.6
Underlying Fiscal Budget real expenditure	2½	2

¹⁾ Per cent of trend-GDP for Mainland-Norway.

Source: Ministry of Finance.

Following a period of strong expansion from 1993 to 1998, growth in **the Norwegian economy** has been far more moderate the last three years. Despite the slow-down, the economy is still characterised by high capacity utilisation, with a shortage of labour in many sectors and relatively strong cost inflation. With low unemployment and record high labour force participation rates, available labour resources are limited. An increase in the number of vacation days this year and next will restrict the supply of labour further. The growth potential of the economy over the next few years is therefore limited compared with the cyclical upturn through the 1990s.

In recent months growth internationally has slowed considerably. In addition, the terrorist attacks on the US on 11 September have increased the risk of a more pronounced international setback. Reduced growth internationally has contributed to a decline in Norwegian exports in recent months. A more pronounced downturn internationally is expected to result in weaker growth in the export-oriented industries and other industries exposed to international competition. This may have spillover effects on domestic demand and activity. Even if world economic growth turns out to be weaker than assumed, the risk of a pronounced downturn in Norway remains limited.

Norway has abundant natural resources. Petroleum revenues provide us with a scope for manoeuvre enjoyed by few other countries. This enhances possibilities for further economic progress. However, mainland output accounts for about 4/5 of total production in the Norwegian economy, and even a small reduction in growth in the mainland economy could therefore easily exhaust the increased leeway provided by the petroleum revenues. The Government places substantial emphasis

on avoiding a weakening of the growth potential of the Norwegian economy.

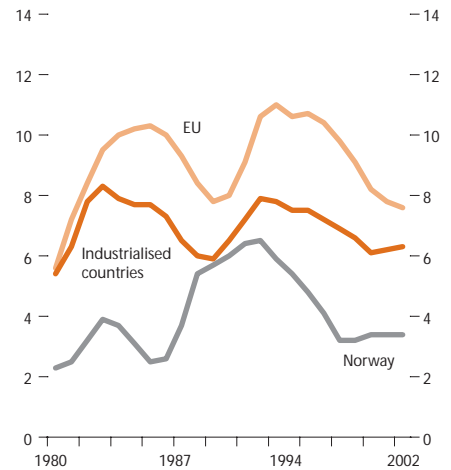
Economic policy must contribute to **stable economic growth**, avoiding excessive cyclical fluctuations. Over the next ten years, Norway will probably record very high government budget surpluses as a result of substantial petroleum revenues. However, petroleum revenues will gradually decline and be accompanied by a sharp rise in expenditures on pensions and health care services as a result of the ageing of the population. In order to address these challenges without having to tighten policy at a later stage, it is necessary to transfer a substantial portion of the high petroleum revenues to the Government Petroleum Fund over the next decade. The Government presented new guidelines for economic policy in Report no. 29 to the Storting (2000-2001) at the end of March 2001¹⁾. The main features of the new guidelines are:

- The structural, non-oil budget deficit shall approximately correspond to the expected real return on the Government Petroleum Fund at the beginning of the fiscal year. The expected real rate of return on the Petroleum Fund is estimated at 4 per cent. The spending rule for oil revenues refers to a situation with normal capacity utilisation in the economy. If the economy is at risk of overheating, fiscal policy restraint should be considered, while in a cyclical downturn a somewhat higher use of petroleum revenues may be required.
- Monetary policy shall aim at stability in the internal and external value of the krone, contributing to a stable exchange rate. At the same time, it shall underpin fiscal policy by contributing to stable developments in output and employment. In accordance with this, the operational implementation of monetary policy shall be oriented towards low and stable inflation, defined as annual consumer price inflation of approximately 2.5 per cent over time. As a main rule, consumer price inflation is expected to remain within an interval of ± 1 percentage point around the inflation target. The conduct of monetary policy shall be forward-looking and should disregard disturbances of a temporary nature that are not considered to have an effect on underlying price and cost inflation.

The Government proposes a 2002 fiscal budget with a structural, non-oil deficit equivalent to the expected real return on the Government Petroleum Fund of NOK 26 billion. This results in a real increase in the use of petroleum revenues over the Fiscal Budget of about NOK

¹⁾ The report is available at www.odin.dep.no/fin/engelsk.

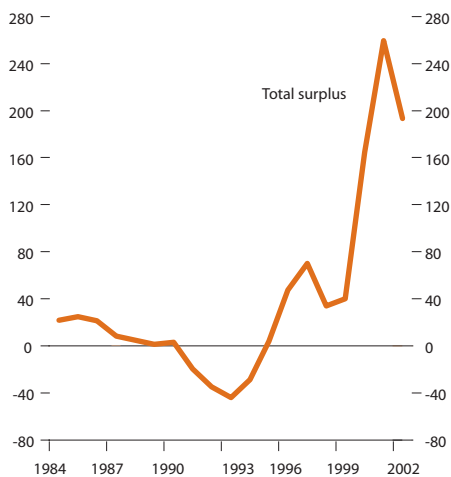
Chart 1. Unemployment



Per cent of labour force

Source: OECD, Statistic Norway and Ministry of Finance.

Chart 2. The Fiscal Budget and the Petroleum Fund



NOK billion

Source: Statistics Norway and Ministry of Finance.

6 billion from 2001 to 2002. A good half of the increased scope for manoeuvre will be used to reduce the level of taxes and excise duties, with particular emphasis on stimulating the supply of labour. The Government has also given priority to measures that can improve productivity and the use of resources in the economy, including measures for improving infrastructure, enhancing the knowledge base and promoting technological advances.

Fiscal Policy

Main Features of Fiscal Policy

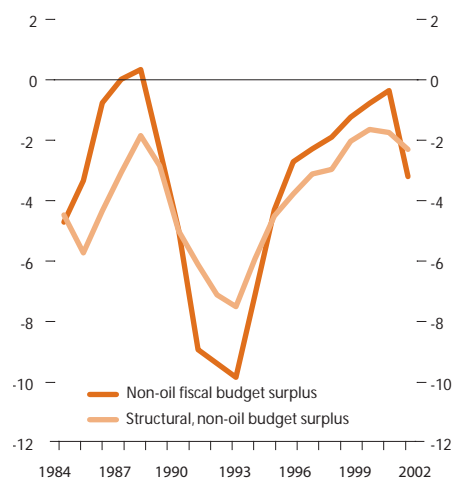
The primary objective of fiscal policy is to allocate resources for public consumption, public investment and transfers to achieve the highest possible welfare over time. Fiscal policy shall also contribute to a stable and sustainable economic development. The fiscal policy for 2002 is based on the new guidelines for economic policy presented in the Government's Long-Term Programme 2002–2005 and in Report no. 29 to the Storting (2000–2001).

Report no. 29 introduced the following guidelines for fiscal policy:

- For each fiscal year, the structural, non-oil budget deficit shall approximately correspond to the expected real return on the Government Petroleum Fund at the beginning of the fiscal year.
- The expected real rate of return on the Petroleum Fund is estimated at 4 per cent.
- The spending rule for oil revenues refers to a situation with normal capacity utilisation in the economy. If the economy is at risk of overheating, fiscal policy restraint should be considered, while in a cyclical downturn a somewhat higher use of petroleum revenues may be required.
- In the event of extraordinary large changes in the Petroleum Fund's capital or in factors behind the structural, non-oil deficit from one year to the next, the corresponding change in the use in of petroleum revenues should be spread over several years on the basis of an estimate of the size of the real return on the Petroleum Fund some years ahead.

The capital in the Petroleum Fund at the beginning of 2002 is estimated at about NOK 650 billion. With an expected real rate of return of 4 per cent, the guidelines

Chart 3. The non-oil fiscal budget surplus and the structural, non-oil budget surplus



Change from previous year. Per cent of trend-GDP for Mainland-Norway

Source: Statistics Norway and Ministry of Finance.

The central government structural, non-oil budget balance

The Ministry of Finance has for many years used the change in the non-oil cyclically adjusted budget surplus net of interest payments as an indicator of the fiscal policy stance. In order to assess the use of petroleum revenues over the Government budget, some adjustments have been made to these calculations. These modifications affect the level of the adjusted budget surplus, but not the year to year changes. The new adjusted budget surplus – the structural, non-oil budget balance – can be interpreted as the amount of petroleum revenues that are used over the Government budget. The relation between the non-oil fiscal budget surplus and the structural, non-oil budget balance is shown in table 2.

Table 2. The structural non-oil budget balance. NOK mill.

	2001	2002
Non-oil fiscal budget surplus	-3 766	-36 100
-Transfers from Norges Bank ²⁾	5 473	3 770
-Net interest payments from		
Norges Bank and abroad ²⁾	208	-267
-Extraordinary transfers	2 586	-18 705
-Cyclical corrections	6 709	5 077
=The structural, non-oil budget balance	-18 742	-25 975
In per cent of trend-GDP for		
Mainland-Norway	-1.7	-2.3
Change from previous year in percentage points ¹⁾	-0.1	-0.6

¹⁾ Equivalent to the former budget indicator.

²⁾ In excess of trend.

Source: Ministry of Finance.

imply a use of petroleum revenues of about NOK 26 billion in 2002, as measured by the structural, non-oil budget deficit. The deficit in 2001 is now estimated at NOK 18.7 billion. Overall, these estimates imply that the guidelines for fiscal policy provide room for a real increase in the use of petroleum revenues of about NOK 6 billion from 2001 to 2002, compared with a neutral fiscal stance. This figure is around NOK 2 billion higher than the estimate in the Revised National Budget 2001.

According to the guidelines for fiscal policy, changes in the return on the Petroleum Fund from one year to the next that are attributable to extraordinary large changes in the Fund's capital shall be phased in over several years. In general, the use of oil revenues shall be based on estimates for changes in the expected real return on the Petroleum Fund over a period of years. The revenues from the partial privatisation of Statoil and the disposal of the SDØE (State Direct Financial Interest) units in 2001 are examples of such extraordinary large changes. The expected real return on the Fund is now estimated to increase by about NOK 6 billion on average per year during the period 2003-2005, measured in 2001 prices. This is in line with the estimated room for the increased use of petroleum revenues in 2002.

In keeping with the guidelines, the use of petroleum revenues over the Fiscal Budget must also be considered in the light of the economic outlook. The outlook for the next few years suggests that the labour market may remain relatively tight. Caution should therefore be made with regard to increased spending of petroleum revenues. Should the increased use of petroleum revenues fuel high price and cost inflation in the years ahead, there is a risk that monetary policy will be tightened. This will have a dampening effect on domestic demand, but could also lead to an appreciation of the Norwegian krone. Such a policy could weaken the basis for the exposed industries.

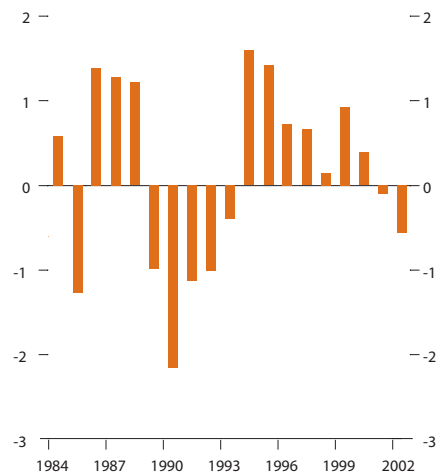
The proposed Fiscal Budget for 2002 implies a structural, non-oil deficit equal to the expected real return on the Petroleum Fund of NOK 26 billion. This implies a real increase in the use of petroleum revenues over the Fiscal Budget of about NOK 6 billion from 2001 to 2002. The Government proposes that a good half of the increased use of petroleum revenues be used to reduce direct and indirect taxes, with a view to stimulating the supply of labour. This is in line with the assumptions in Report no. 29 to the Storting, which was presented at the end of March. On the expenditure side, the Government has placed particular emphasis on maintaining and expanding welfare services. The Government has also given priority to measures that can improve economic efficiency, includ-

ing a reduction in direct and indirect taxes and measures to improve infrastructure, enhance the knowledge base and foster technological advances.

The main features of the Fiscal Budget proposal for 2002 can be summarised as follows:

- A structural, non-oil budget deficit equal to the expected real return on the Petroleum Fund of NOK 26.0 billion, equivalent to 2.3 per cent of mainland trend GDP. The deficit for 2001 is now estimated at NOK 18.7 billion, corresponding to 1.7 per cent of mainland trend GDP. Compared with a neutral fiscal stance, the use of petroleum revenues over the Fiscal Budget will increase by about NOK 6 billion (2001 prices) between 2001 and 2002.
- A real reduction in direct and indirect tax payments of about NOK 3.5 billion between 2001 and 2002. In accrued terms, direct and indirect taxes are reduced by close to NOK 7.7 billion. In the tax proposal for 2002, the Government has placed particular emphasis on measures that can stimulate the supply of labour. In addition, the Government recommends that the removal of the investment tax be postponed by a half year to 1 October 2002. Reference is made to a further discussion on the direct and indirect tax proposal in chapter 5.
- The budget proposal for 2002 implies a real underlying growth in Fiscal Budget expenditures of about 2 per cent, corresponding to a little more than NOK 9 billion. In the calculations of underlying spending growth, Fiscal Budget expenditure on petroleum activities, interest and unemployment benefits are excluded. To render expenditures in 2001 and 2002 comparable, extraordinary changes and some extraordinary accounting elements are also excluded.
- Total local government revenues are proposed to increase in real terms by about NOK 3½ billion, or almost 2 per cent, compared with the revenue level in 2001 as estimated in the Proposition on Local Government Finances. Transfers to the specialist health service are excluded. Compared with the estimates for the accounts for 2001, real growth in total local government revenues is about NOK 1¾ billion, or about 1 per cent.
- The non-oil Fiscal Budget deficit is estimated to increase from NOK 3.8 billion in 2001 to NOK 36.1 billion in 2002. The pronounced increase in the non-oil deficit partly reflects extraordinary repayments of local government debt in connection with the state's acquisition of the specialist health service. NOK 18.7 billion is proposed allocated over the Fiscal Budget for this purpose. Reduced net interest payments and transfers from Norges Bank and a smaller cyclical adjustment also play a part in explaining the fact that the increase in the non-

Chart 4. The structural, non-oil budget surplus



Change from previous year. Per cent of trend-GDP for Mainland-Norway

Source: Statistics Norway and Ministry of Finance.

oil fiscal deficit is larger than the increase in the structural, non-oil budget deficit. The extraordinary repayment of local government debt in connection with the hospital reform will not influence activity in 2002 and is therefore considered to be an accounting adjustment when calculating the structural, non-oil budget deficit.

- Assuming an average oil price of NOK 200 per barrel next year, the state's net cash flow from petroleum activities is estimated at NOK 205.5 billion in 2002.
- Net transfers to the Government Petroleum Fund, excluding transfers to the Fiscal Budget, are estimated at NOK 169.4 billion. Interest and dividends on the accumulated capital in the Petroleum Fund of NOK 24.0 billion come in addition. The overall surplus on the Fiscal Budget and the Government Petroleum Fund, including interest and dividend income, is estimated at NOK 193.4 billion in 2002.

The budget proposals and estimates in this report imply an overall surplus on the Fiscal Budget and the Petroleum Fund of NOK 193.4 billion in 2002, i.e. a reduction of NOK 66 billion compared to the estimates for 2001. The reduction is ascribable to an increase in the non-oil budget deficit of NOK 32.3 billion and an estimated decrease in the state's net cash flow from petroleum activities of NOK 39.4 billion. The decline in net cash flow partly reflects extraordinary income from the sale of SDØE (State Direct Financial Interest) units to Statoil in 2001. In addition, the oil price is assumed to fall from an estimated NOK 230 per barrel in 2001 to an average of NOK 200 per barrel in 2002. Interest and dividend income in the Petroleum Fund is estimated to rise by NOK 5.6 billion to NOK 24.0 billion in 2002. The capital in the Petroleum Fund is estimated at NOK 861 billion at the beginning of 2003, or 57 per cent of GDP.

Estimates for General Government Finances in 2002

Table 4 shows the developments in the general government budget surplus (net lending), using definitions of the national accounts. Net lending corresponds to the surplus concept used in the Maastricht criteria for general government finances. In addition to the Fiscal Budget and the Government Petroleum Fund, this surplus concept comprises other central government and social security accounts, including the National Insurance Fund, the Government Bank Insurance Fund, the Government Bank Investment Fund and other central government funds. The local government sector is also included as a separate administrative level.

Total general government net lending is assumed to decline from NOK 230.1 billion in 2001 to NOK 210.8

Table 3. Key figures for the Fiscal Budget (incl. Social Security) and Government Petroleum Fund. NOK billion.

	2000	2001	2002
Total revenues	643.6	746.1	738.3
1. Revenues excl. petroleum activities	459.0	484.0	516.4
1.1 Taxes and excises, Mainland Norway	406.7	426.9	465.5
1.2 Other revenues	52.4	57.2	50.9
2. Revenues from petroleum activities	184.6	262.0	221.9
Total expenditures	490.2	505.0	568.9
1. Expenditures excl. petroleum activities	467.0	487.8	552.5
2.1 Purchases of goods and services	106.0	101.4	102.4
2.2 Transfers	360.9	386.4	450.1
2. Expenditures on petroleum activities	23.3	17.2	16.4
Surplus before transfer to the Government Petroleum Fund	153.4	241.1	169.4
- Revenues from petroleum activities	161.4	244.9	205.5
= Non-oil budget surplus	-7.9	-3.8	-36.1
+ Transfer from the Government Petroleum Fund	9.5	3.8	36.1
= Fiscal budget surplus	1.5	0.0	0.0
+ Net transfer to the Government Petroleum Fund	151.9	241.1	169.4
+ Dividends and interest payments on the Government Petroleum Fund	10.9	18.4	24.0
= Fiscal budget surplus and the Government Petroleum Fund	164.3	259.5	193.4

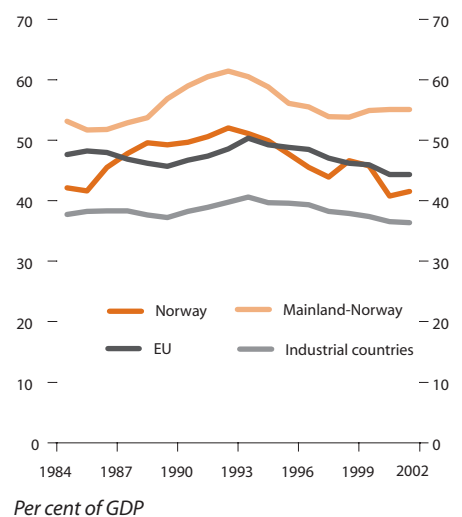
Source: Ministry of Finance.

billion in 2002. General government net assets, including assets in the Petroleum Fund and capital investment in state enterprises, are estimated at about NOK 1180 billion at the end of 2002, or 78 per cent of GDP.

General government expenditures for Norway is compared with that of EU countries and countries in the OECD area in chart 5. The figures for Norway are based on the estimates in this report. The chart shows that general government expenditures fell from around 52 per cent of total GDP in 1992 to 45.8 per cent of GDP in 1999. General government expenditures as a percentage of mainland GDP was reduced from 61.4 per cent of GDP in 1992 to 53.7 per cent in 1998. As a result of slower growth in the mainland economy in recent years, expenditures as a share of mainland GDP is estimated to increase again to 55.9 per cent in 2002.

The general government expenditure level in Norway, measured as a percentage of GDP, has been in line with the average for EU countries in recent years but higher than the average for the OECD area. The relatively low expenditure levels in countries such as the US and Japan contribute to pushing down the average for the OECD area in relation to the average for EU countries. When comparing the level of general government expenditure, it must be taken into account that the countries' debt situ-

Chart 5. Public expenditures



Source: OECD, Statistics Norway and Ministry of Finance.

Table 4. Central and general government net lending. NOK million

	2000	2001 ²⁾	2002 ²⁾
Fiscal Budget surplus	1525	0	0
+ Surplus in Government Petroleum Fund	162 825	259 486	193 370
+ Surplus in other central government and social security accounts	-591	3 728	8 230
+ Definitional differences between central government accounts and national accounts ¹⁾	51 354	8 486	2 437
+ Direct investments in state enterprises	4 101	-38 628	-2 570
= Consolidated central government net lending	219 214	233 072	201 467
+ Local government surplus	-6 507	-2 972	9 286
= General government net lending	212 707	230 100	210 753
Per cent of GDP	14.9	15.6	14.0

¹⁾Including consolidated and central government accrued, unrecorded taxes.

²⁾Estimates

Source: Statistics Norway and Ministry of Finance.

ation may vary widely. For the EU as a whole, high general government debt means that interest expenses account for a substantial share of general government expenditure.

Public Finances in the Medium Term

The new guidelines for economic policy mean that fiscal policy stipulate a use of oil revenues in line with the expected real return on the Petroleum Fund. The estimates for the capital in the Petroleum Fund in the period 2002-2010 are based on two main assumptions:

- A fall in oil prices from the current level together with declining production will contribute to reducing the state's net cash flow from petroleum activities, from an estimated level of NOK 206 billion in 2002 to about NOK 142 billion in 2005 and about NOK 120 billion in 2010.
- A gradual increase in the use of petroleum revenues over the Fiscal Budget approximately in line with to the expected real return on the Petroleum Fund.

Given these assumptions, the Petroleum Fund may increase from 57 per cent of GDP at the end of 2002 to 118 per cent of GDP in 2010. As measured by the structural, non-oil budget deficit, the use of petroleum revenues over the Fiscal Budget will correspond to about 5 per cent of mainland trend GDP in 2010, while the corresponding share is estimated at 1.7 per cent in 2001. Compared with a neutral fiscal stance, the guideline implies an average annual increase in the use of petroleum revenues over the next four years of about 1/2 per cent of mainland trend GDP. The fiscal rule of spending the expected real return on the Petroleum Fund implies a gradual increase in the use of petroleum revenues over the next ten years.

Long-term Fiscal Policy Challenges

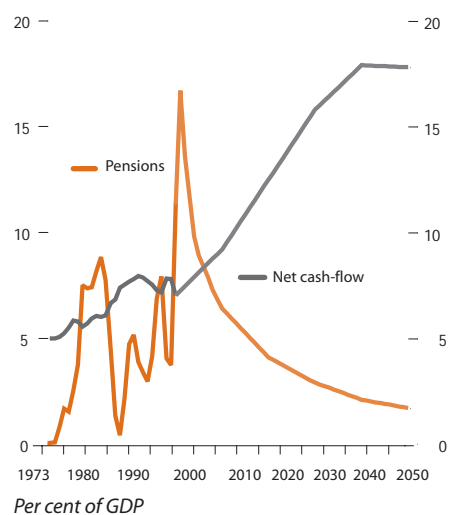
Expectations of substantial general government budget surpluses over the next ten years may create an impression that the issue of the long-term sustainability of fiscal policy is hardly relevant for Norway. However, the large current general government surpluses give a misleading picture of fiscal policy leeway, primarily because of the long-term outlook for petroleum revenues and social security expenditures:

- Owing to the high depletion rate and high oil prices, central government petroleum revenues are today considerably higher than the level expected in the longer run. The accumulation of capital in the Government Petroleum Fund has its counterpart in the reduction in the value of petroleum reserves.
- Old-age and disability pension obligations under the social security scheme are rising sharply. This is not reflected in the annual government budgets. The contingent obligations are estimated at about NOK 3200 billion at the beginning of 2002 and about NOK 3400 billion at the beginning of 2003. Measured in constant 2002 prices, the obligations are estimated to rise by about NOK 120 billion through 2002. Over the next 30 years, old-age and disability pension payments are expected to double as a share of total GDP
- The increase in the number of elderly will eventually require increased resources for nursing and care services. Approved welfare reforms will also increase the need for resources in government services in the years ahead.

Substantial petroleum revenues still provide Norway with a more solid basis than many other countries for addressing the challenges associated with the ageing of the population. However, petroleum revenues are assumed to fall later this century. In periods with high petroleum revenues, substantial capital must be set aside, which is the primary objective of the accumulation of capital in the Government Petroleum Fund.

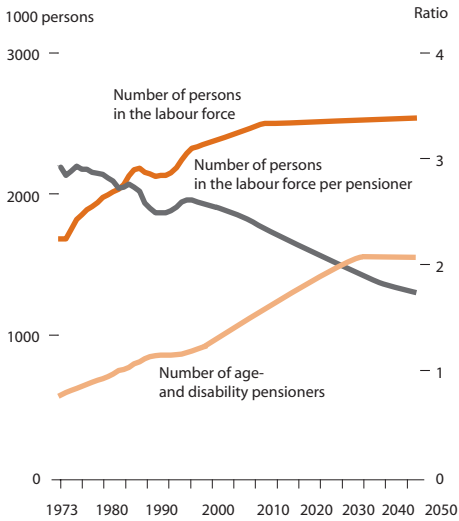
Since 1995, generational accounting estimates have been presented regularly based on the proposed budget. In the National Budget for 2000, the calculations showed a need for tightening in the order of NOK 5-20 billion, while in the National Budget for 2001 and the Revised National Budget for 2001 it was indicated that the budget balance was approximately of an order necessary to avoid passing on burdens to future generations. The calculations were based, among other things, on the assumption that the tax level in 2001 would be maintained. After the Revised National Budget for 2001 was presented, developments have contributed to weakening the generational balance.

Chart 6. Government net cash-flow from petroleum activities and old age and disability pensions



Source: Statistics Norway and Ministry of Finance.

Chart 7. Pensioners and labour force



Source: Statistics Norway and Ministry of Finance.

First and foremost, the new guidelines for fiscal policy result in a real increase in the use of petroleum revenues for the fiscal year 2002 of a good NOK 6 billion. At the same time the petroleum wealth has been revised downwards.

Overall, the generational balance has been weakened by about NOK 10 billion. Updated estimates of the generational accounts now indicate a need for tightening of about NOK 0-20 billion. Still, the generational accounts show that the need for tightening in Norway is moderate compared with that of other European countries (see the Long-Term Programme 2002-2005).

Chapter 3

Monetary Policy

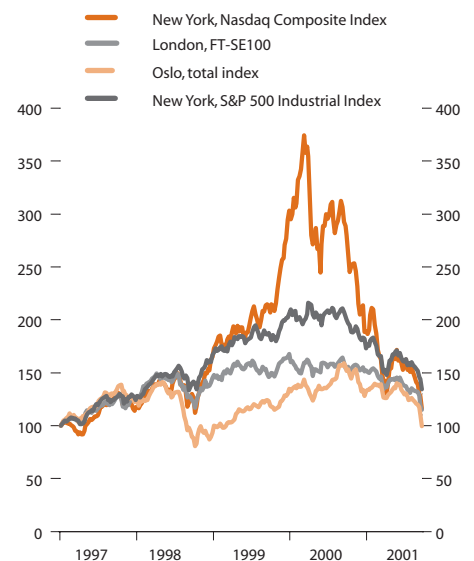
Monetary policy shall aim at stability in the internal and external value of the krone, contributing to a stable exchange rate. At the same time, it shall underpin fiscal policy by contributing to stable developments in output and employment.

In Report no. 29 to the Storting (2000-2001) Guidelines for economic policy, which was presented on 29 March 2001, a new regulation on monetary policy was introduced. In a situation where fiscal policy shall accommodate a gradual and sustainable increase in the use of petroleum revenues in the Norwegian economy, it was necessary to establish a clearer anchoring of monetary policy's role in underpinning economic stability.

§1, first paragraph of the new regulation, reads: "Monetary policy shall be aimed at stability in the Norwegian krone's national and international value, contributing to stable expectations concerning exchange rate developments. At the same time, monetary policy shall underpin fiscal policy by contributing to stable developments in output and employment." Over time there will normally be a clear relationship between developments in the krone's purchasing power in Norway and developments in the value of the krone measured against our trading partners. A stable exchange rate can contribute to expectations of continued low inflation, which in turn influences price and wage setting. Stable economic growth, with moderate price and cost inflation, will also be a precondition for stability in the exchange rate over time.

§1, third paragraph, of the regulation reads: "Norges Bank's implementation of monetary policy shall, in accordance with the first paragraph, be oriented towards low and stable inflation. The operational target of monetary policy shall be annual consumer price inflation of approximately 2.5 per cent over time." As a main

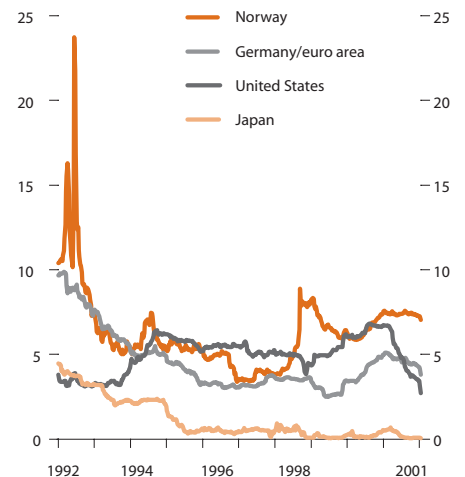
Chart 8. Stock market



Weekly average. Week 1 1997=100

Source: Norges Bank and EcoWin.

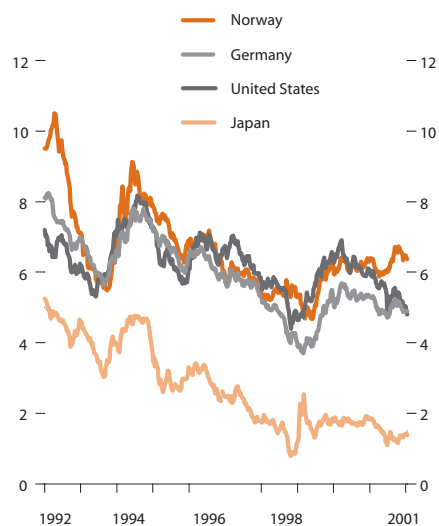
Chart 9. 3-month Euro-rates



Per cent

Source: OECD, Norges Bank and EcoWin.

Chart 10. Government bonds with 10-year residual maturity



Percent

Source: OECD, Norges Bank and EcoWin.

rule, consumer price inflation is expected to remain within an interval of ± 1 percentage point around the inflation target. The provision is to be construed to mean that deviations between actual inflation and the target in a period shall not be compensated for in a later period. If inflation deviates significantly from the target over a period, Norges Bank shall set the interest rate with a view to returning gradually consumer price inflation to the target to avoid unnecessary fluctuations in output and employment.

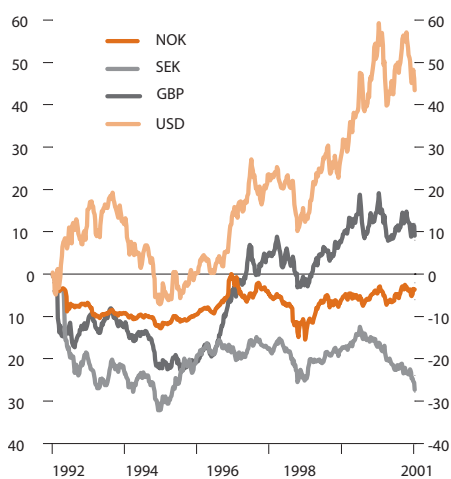
§1, fourth paragraph, of the regulation reads: "In general, the direct effects on consumer prices resulting from changes in interest rates, taxes, excise duties and extraordinary temporary disturbances shall not be taken into account." Norges Bank's interest rate setting shall be forward-looking and take due account of the uncertainty associated with macroeconomic estimates and assessments. It shall take into account that it can take time for policy changes to have an impact, and disregard disturbances of a temporary nature that are not considered to have an effect on underlying price and cost inflation. As a rule, monetary policy shall not react to direct effects on inflation that are due to changes in interest rates, taxes, excise duties and extraordinary temporary disturbances.

In a letter from Norges Bank to the Ministry of Finance of 27 March 2001 Norges Bank writes:

"Monetary policy affects the economy with considerable and variable lags. Consequently, the Bank must be forward-looking in its interest-rate setting. The effects of interest rate changes are uncertain and vary over time. Changes in the interest rate will be made gradually so that the Bank may assess the effects of interest rate changes and other new information on economic developments. If price inflation deviates substantially from the target for a period, Norges Bank will set the interest rate with a view to gradually returning consumer price inflation to the target. Norges Bank will seek to avoid unnecessary fluctuations in output and demand.

Consumer price inflation normally varies from month to month. Substantial changes in the inflation rate may at times occur as a result of extraordinary fluctuations in certain product markets or changes in direct and indirect taxes. In its analyses of different measures of underlying inflation, Norges Bank will assess the effects of changes in the interest rate level, taxes, excise duties and extraordinary temporary disturbances. Deviations between actual and projected underlying inflation will normally be in the interval ± 1 percentage point."

Chart 11. Exchange rates against DEM/euro¹⁾



Percentage change from August 1992

¹⁾ An ascending graph implies a strengthening against DEM/Euro.

Source: OECD, Norges Bank and EcoWin.

In the Ministry's view, the new guidelines lay a sound basis for Norges Bank to continue its conduct of a monetary policy that enjoys the confidence of financial markets and society at large. The new guidelines for monetary policy, combined with the guidelines for fiscal policy provide a solid basis for a stable economic development.

Regulation on Monetary Policy

Established by Royal Decree of 29 March 2001 pursuant to Section 2, third paragraph, and Section 4, second paragraph, of the Act of 24 May 1985 no. 28 on Norges Bank and the Monetary System

I

§ 1.

Monetary policy shall be aimed at stability in the Norwegian krone's national and international value, contributing to stable expectations concerning exchange rate developments. At the same time, monetary policy shall underpin fiscal policy by contributing to stable developments in output and employment.

Norges Bank is responsible for the implementation of monetary policy.

Norges Bank's implementation of monetary policy shall, in accordance with the first paragraph, be oriented towards low and stable inflation. The operational target of monetary policy shall be annual consumer price inflation of approximately 2.5 per cent over time.

In general, the direct effects on consumer prices resulting from changes in interest rates, taxes, excise duties and extraordinary temporary disturbances shall not be taken into account.

§ 2.

Norges Bank shall regularly publish the assessments that form the basis for the implementation of monetary policy.

§ 3.

The international value of the Norwegian krone is determined by the exchange rates in the foreign exchange market.

§ 4.

On behalf of the State, Norges Bank communicates the information concerning the exchange rate system ensuing from its participation in the International Monetary Fund, cf. Section 25, first paragraph, of the Act on Norges Bank and the Monetary System.

II

This regulation comes into force immediately. Regulation no. 0331 of 6 May 1994 on the exchange rate system for the Norwegian krone is repealed from the same date.

The Government Petroleum Fund

Table 5. Investment of the Fund

Benchmark portfolio	
Equities ¹⁾	40 %
America	30 %
Europe	50 %
Asia/Oceania	20 %
Bonds ²⁾	60 %
America	30 %
Europe	50 %
Asia/Oceania	20 %

¹⁾ The equity portfolio is distributed between countries according to market capitalisation weights.

²⁾ The bond portfolio has until now been distributed between countries according to GDP weights. From 2002, bonds will be distributed between countries according to market capitalisation weights.

Source: Ministry of Finance.

The Government Petroleum Fund was established in 1990 when the Storting adopted the Petroleum Fund Act. The Fund's income is defined under the Act as the central government's net cash flow from petroleum activities, income from the sale of shares in Statoil and the return on the Fund's investments. The Fund's expenditure includes an annual transfer to the Fiscal Budget by virtue of a Storting resolution, equivalent to the non-oil Fiscal budget deficit.

Norges Bank manages the Government Petroleum Fund in accordance with the guidelines provided by the Ministry of Finance. The capital in the Petroleum Fund is invested in equities and fixed-income instruments abroad. The equity share in the Fund is limited to 30-50 per cent. The Fund may today be invested in 28 different countries¹⁾.

The value of the Government Petroleum Fund came to NOK 522.6 billion at end-June 2001. The Fund is estimated to increase to NOK 650 billion at the end of 2001 and NOK 861 billion at the end of 2002. Since the beginning of 1998, the Petroleum Fund's total cumulative return has been 23.8 per cent. This corresponds to an average annual real return of 4.7 per cent in the period.

An Environmental Fund was established on 31 January 2001 with a capital of NOK 1 billion. The Fund should be invested in companies that are considered to have little negative impact on the environment and in companies that satisfy defined criteria with respect to environmental reporting and certification.

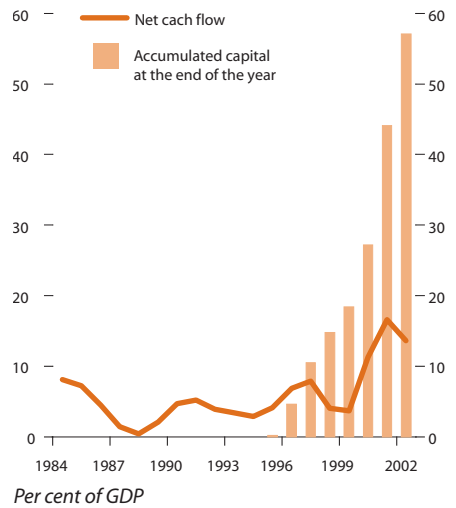
1) The countries are: Belgium, Denmark, Finland, France, Greece, Ireland, Italy, the Netherlands, Portugal, Spain, the United Kingdom, Switzerland, Sweden, Turkey (equity only), Germany and Austria in Europe, Brazil (equity only), Canada, Mexico (equity only) and USA in America and Australia, Hong Kong, Japan, New Zealand, Singapore, South-Korea (equity only), Taiwan (equity only) and Thailand (equity only) in Asia and Oceania.

The Government will establish an exclusion mechanism for the Petroleum Fund, whereby the Ministry may exclude companies from the Fund's investment universe if investments in such companies are contrary to Norway's commitments under international law. The framework and procedures for such a mechanism are laid down in the Regulation for the Management of the Petroleum Fund. The Regulation was amended on 28 September 2001.

In the Revised National Budget for 2001, the Government decided to include non-government-guaranteed bonds in the benchmark portfolio as from the first quarter of 2002. This change will make the benchmark index more representative of international bond markets. The Lehman Global Aggregate will be used as a benchmark for the bond portfolio. After a period of build-up of non-government-guaranteed bonds, these are estimated to account for about 30-40 per cent of the Petroleum Fund's bond portfolio. The portfolio will primarily include non-government-guaranteed bonds with medium to low credit risk, rated by the credit rating agencies Moody's and Standard and Poors.

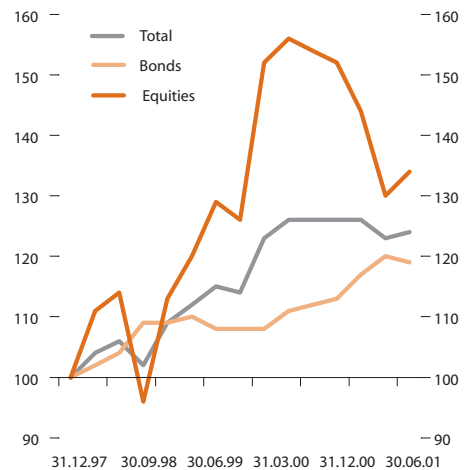
Currently, the weights to regional equities and bonds are brought back to the long-term strategic weights at the end of each calendar quarter. In order to reduce transaction costs the Government suggests to rebalance the benchmark only if the weights to certain regions and markets move outside a specified trigger point. In addition the benchmark will be rebalanced as far as possible back towards the strategic weights each month, taking account of the actual monthly cash transfer to the Fund. Norges Bank has estimated that this may reduce transactions costs by NOK 700 million over a five-year period.

Chart 12. Government net cash-flow from the petroleum activities and accumulated capital in the Government Petroleum Fund



Source: OECD, Statistics Norway and Ministry of Finance.

Chart 13. Accumulated returns on the Petroleum Fund

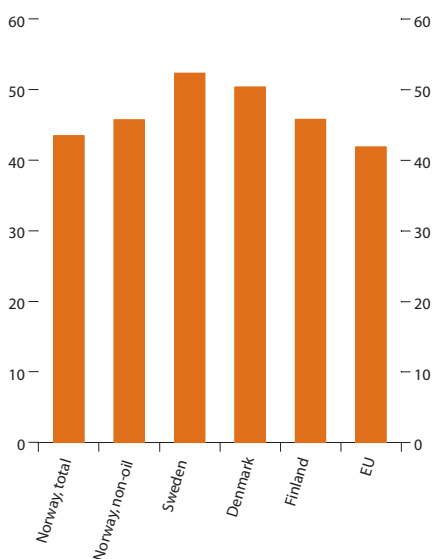


Indicies 31 December 1997=100

Source: Norges Bank.

Tax Policy

Chart 14. Taxes in per cent of GDP



Source: OECD, Statistics Norway and Ministry of Finance.

The tax system shall finance the government expenditures and contribute to an equitable distribution of income as well as an efficient use of resources. The Government emphasises that the tax system should be based on broad tax bases and relatively low rates, since this will reduce the efficiency costs of taxation. The Government is also seeking to simplify the tax rules, reduce the number of tax loopholes and ensure a fair distributional profile.

The new guidelines for fiscal policy imply an increase in the structural, non-oil budget deficit of about NOK 6 billion a year in the period 2002 to 2005 (see section 2). The Government proposes to use a good half of this increased fiscal leeway in 2002 to reduce taxes, partly because lower direct and indirect taxes may have favourable effects on the growth potential of the economy.

The Government proposes a reduction in the overall tax level, excluding changes in the child benefit scheme, of about NOK 3.5 billion from 2001 to 2002, while accrued taxes will decrease by almost NOK 7.7 billion. The reductions in real terms in the child benefit scheme amount to about NOK 635 million.

The Government's proposal to increase the upper limit of the standard allowance and the threshold for the surtax on higher labour and pension income will reduce marginal taxes for taxpayers with low and medium income. The proposal means that employees with an average labour income will not pay the surtax. In order to keep the tax proposal within a responsible budget balance, the Government proposes to postpone the removal of the investment tax by six months, to 1 October 2002.

The main features of the Government's tax proposal for 2002 are:

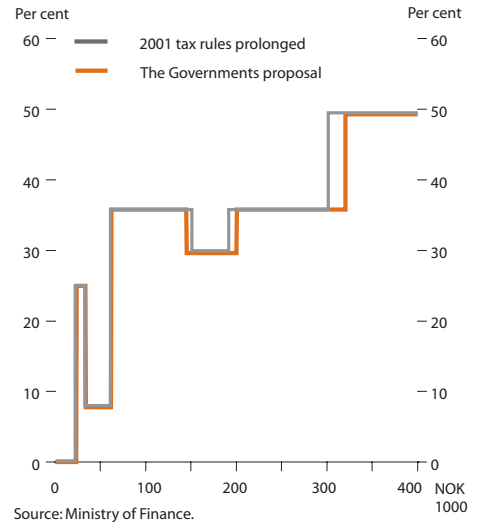
- An increase in the threshold for the surtax on higher incomes by 10.7 per cent, to NOK 320 000.
- An increase in the upper limit of the standard allowance by 6.7 per cent, to NOK 43 000.
- An increase in the allowance for trade union fees etc. by 100 per cent, to NOK 1800.
- Stricter rules for the taxation of private use of company-owned cars and mileage allowance
- An increase of 5 per cent in assessed tax values for real property
- An increase in depreciation rates for some business assets
- An introduction of a tax allowance for corporate R&D
- A removal of the investment tax with effect from 1 October 2002
- A reduction of 1 øre per kWh in electricity taxes, to 9.30 øre per kWh, with effect from 1 July 2002
- A removal of the import tariffs for many groups of manufactured goods
- A removal of the sulphur tax on coal, coke and refinery plants

The Government follows up the Storting's decision to introduce a maximum value in the taxation of housing by allowing the maximum assessed tax value to be set at 30 per cent of market value.

The Government also intends to present a report to the Storting on the taxation of business and capital income.

All in all, the tax proposal will contribute to increasing household purchasing power, on average providing a relief for all major income levels.

Chart 15. Marginal tax rates on wage income



Measures to Improve the Functioning of the Economy

Measures to improve the functioning of the economy shall contribute to achieving an efficient use of resources, thereby strengthening the growth potential of the economy.

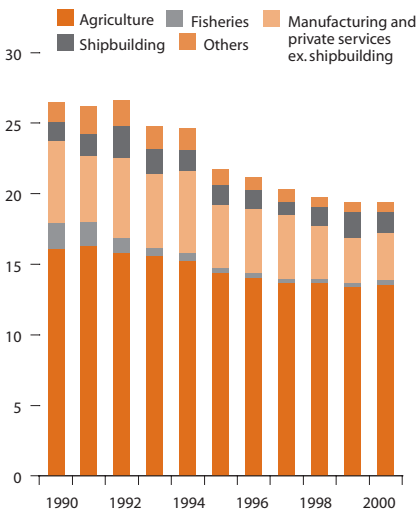
The **budgetary support** to industries is estimated at NOK 19.4 billion in 2000, a slight increase from the level in 1999, measured at constant prices. During the 1990s, annual budgetary support payments to industries were reduced by about 27 per cent in real terms. As a percentage of GDP, support to industries fell from 2.6 per cent in 1990 to 1.4 per cent in 2000.

In the period 1990-2000, the budgetary support to the **agricultural sector** was reduced, but by far less than the overall support to industries. Agricultural support accounted for almost 70 per cent of total budgetary support in 2000.

Support payments to the **fisheries sector** are estimated at NOK 427 million in 2000. Transfers through the fisheries agreement represent a substantial portion of support to this sector. Transfers through this agreement were reduced sharply in the first half of the 1990s.

Support to **manufacturing, mining and private services** amounted to about NOK 4.8 billion in 2000, which is a reduction in real terms of 3.9 per cent from 1999. The total support to the sector was reduced by more than 30 per cent during the 1990s. However, support to the shipbuilding industry remained high throughout the 1990s, with an annual average of NOK 1.5 billion (2000 prices). This level was maintained in 2000. As a result of the EEA regulations applying to the shipbuilding industry, all support for contracts concluded after 1 January 2001 is discontinued.

Chart 16. Budgetary support to industries



NOK billion in 2000-prices

Source: Ministry of Finance

Research is a high-priority area. The Government's objective is that by 2005 research activities in Norway shall as a minimum correspond to the average OECD level, measured as a percentage of GDP. The Government will make a contribution both by proposing substantial increases in appropriations to research the next few years and by proposing measures to encourage the business sector to invest more in R & D. Moreover, the Government will initiate measures to increase the quality of Norwegian research and strengthen recruitment to research.

As a result of the EEA Agreement, two sets of **competition rules** have existed since 1994: the national Competition Act and the competition rules under the EEA Agreement. The purpose of both sets of rules is to ensure that commercial undertakings do not restrict or distort competition. The Norwegian authorities have appointed an official committee that is to review Norwegian competition legislation and table proposals for new rules by November 2002. The committee has submitted its first report, which proposes giving the Norwegian authorities responsibility for fully enforcing Article 53 of the EEA Agreement prohibiting anti-competitive practices and Article 54 prohibiting an abuse of a dominant position. Moreover, the committee recommends that a new Norwegian competition act should be drawn up on the basis of the model set out in the EEA Agreement's competition rules.

Public sector ownership in the Norwegian business sector is somewhat higher than in most other OECD countries and relatively concentrated on certain companies or industries. A large portion of government ownership is related to the use of natural resources, natural monopolies or regional policy considerations. In recent years, a number of companies have been converted to ordinary limited companies, partially privatised, listed on the stock exchange and, in some cases, fully privatised. Following the partial privatisation of Statoil and Telenor, the proportion of companies that are partially owned by the public sector is becoming far greater than the proportion of wholly owned state companies. In the Long-Term Programme 2002-2005, the Government presented several measures to clarify and enhance the state's role as owner in entities that shall remain in public ownership. This is followed up in the National Budget 2002 through a more precise formulation of the management of government ownership interests with regard to, for example, the use of required returns, dividend policy, the valuation of unlisted companies and the evaluation and composition of boards.

Extensive changes took place in the **electricity market** in the 1990s. As a result of the Energy Act of 1990, the

electricity supply sector was changed from a sector that focused on meeting local/regional demand for electricity to a market where prices are determined by supply and demand. The opportunity to switch from one supplier to another has steadily improved for end-users. In recent years, there has been a tendency towards increased cooperation and mergers between energy plants as well as acquisitions of distribution companies and customer portfolios in electricity turnover. Statkraft SF is by far the largest production company in Norway. In spring 2001, the Storting decided to transfer NOK 6 billion in new capital to the company and gave the Ministry of Petroleum and Energy authority to expand Statkraft's loan and guarantee limit by up to NOK 10 billion.

In the **telecommunications sector**, Norway has generally adhered to the schedule for deregulation laid down in the EEA Agreement. With effect from 1 January 1998, the remaining exclusive rights pertaining to general telecommunications infrastructure and speech telephony in the established transmission line network were removed. So far, Telenor AS has maintained a strong market position in most market segments. Except for the market for GSM mobile telephony, competitors have only won small market shares in the market for private customers, while competition is somewhat stronger in the market for corporate customers.

In December 2000, four nationwide licences were awarded for the establishment and operation of a third-generation mobile communication system in Norway. One of the licences was revoked after the owner was declared bankrupt in August 2001. The Ministry of Transport and Communications, in cooperation with the Norwegian Post and Telecommunications Authority, will work on a reallocation of the available licence.

In recent years, the Norwegian **civil aviation market** has shifted from a market based on exclusive right to a regulated competitive market, albeit with fairly dominant operators. SAS and Braathens are the only airlines that have a large scheduled network for domestic flights that are trafficked by competing companies. On 21 May 2001, SAS concluded an agreement with the largest owners of Braathens concerning the purchase of the company. The Norwegian Competition Authority, however, has announced that it is evaluating intervention to prohibit the purchase. The case is still being considered.

The **taxi industry** has traditionally been heavily regulated. Municipalities regulate market entry by allocating licences. Moreover, the Norwegian Competition Authority has regulated prices in the market by setting maxi-

imum taxi rates. With effect from 1 May 2000, the Competition Authority is no longer responsible for regulating taxi rates in areas with two or more taxi exchanges and where conditions are otherwise conducive to competition. According to the Competition Authority, the deregulation has resulted in an improvement in the relationship between the supply of taxi services and demand in the areas involved.

The Norwegian market for **pharmaceuticals** continues to feature extensive regulations. A new Pharmacy Act entered into force on 1 March 2001, setting out less restrictive entry requirements. According to the new Act, pharmacies will continue to have exclusive rights for selling non-prescription pharmaceuticals. When the new Act has been in force for a period, the authorities will evaluate whether some non-prescription pharmaceuticals can also be sold outside pharmacies. The practice of setting maximum prices for prescription pharmaceuticals was changed with effect from 1 July 2000. According to the new regulation, maximum prices are generally set on the basis of selling prices in countries within the EEA, but with the exception of southern European countries. As a main rule, the price is set at the average of the three cheapest comparison countries. The change in the way prices are set has probably resulted in lower pharmaceutical prices.

A special feature of the **fisheries industry** is the extensive set of rules relating to activities in the industry. The regulations contribute to maintaining sustainable stocks and to a better adaptation of fleet capacity, thereby increasing value added in the industry. The formulation of some regulations, however, may result in lower value added in the traditional fisheries sector than would otherwise have been the case. The fish farming industry is also regulated with regard to establishment, ownership and fish farming installations.

The fisheries industry exports more than 90 per cent of its production. It is therefore in Norway's best interest to reduce trade barriers that limit exports of seafood. The Government will use the opportunity provided by the round of negotiations in the World Trade Organisation to secure improved trading conditions for the fisheries industry.

Reforming the public sector is an important part of economic policy. Since Norway has a relatively large public sector, productivity developments in this sector is of vital importance to the overall economic efficiency. The Government is in the process of implementing or initiating a number of extensive reforms in the **public sector**:

- A hospital reform, which consists of a state take-over of the specialist health service
- A defence reform, which means that the defence sector shall be modernised and adapted to new challenges
- An education reform, which includes a new structure for degrees and a renewal of the content and structure of studies. At the same time, the study period in higher education will be reduced
- A police reform, which means that fewer police officers will be used for management and administration and a greater number for active police work
- 24-hour public services shall provide increased accessibility to the public sector, more flexible and individually tailored services for users and a more efficient use of resources in the public sector

Chapter 7

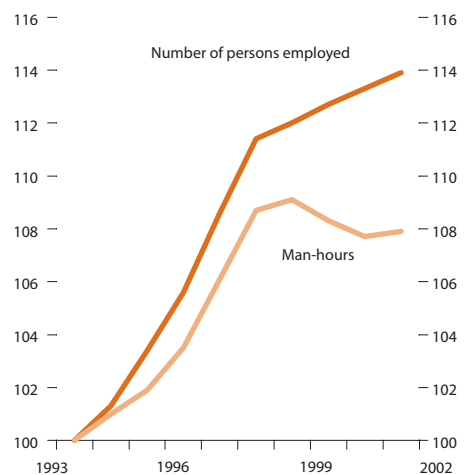
Economic Prospects

In spite of moderate growth over the past few years, the Norwegian economy is still characterised by high capacity utilisation, labour shortages in many sectors and relatively high cost inflation. This is also reflected in a high interest rate level. Since the upswing in the Norwegian economy started in 1993, employment has increased by almost 260 000 persons, corresponding to an average annual growth of $1\frac{3}{4}$ per cent. At the same time, unemployment has declined to a low level. Low unemployment and record-high labour force participation rates are setting limits to the potential increase in labour supply. The increase in the number of vacation days this year and next will further restrict the supply of labour. The growth potential of the economy over the next few years is therefore limited compared with the strong growth through the 1990s.

Economic growth internationally has slowed markedly over the past year, and the world economy may grow at the lowest rate recorded since the beginning of the 1990s. At the same time the outlook is more uncertain than it has been for a long time. Growth in the US economy has slowed substantially since the summer of 2000. The terror attacks on the US in September 2001 resulted in the loss of several thousands human lives and severe material damages. The impact on consumer and business confidence in the future is highly uncertain as a result of these events, and has intensified the uncertainty regarding the timing of a rebound in economic growth.

In the first six months of 2001, growth in Norway's mainland economy picked up moderately after a seasonally adjusted decline towards the end of last year. Increased consumption in the household and public sector has made a positive contribution to growth so far this year. However, mainland investment showed a seasonally adjusted decline both in the first and second

Chart 17. Employment



Per cent of labour force

Source: Statistics Norway and Ministry of Finance.

quarter, primarily as a result of lower business investment. In the first half of 2001, mainland GDP expanded by only 0.8 per cent compared to the same period last year. Current economic data suggest that the economy has continued to expand at a moderate pace in the third quarter. The value of traditional merchandise exports fell, seasonally adjusted, both in July and August. Consumer spending has exhibited moderate growth over the last few months, and Norway, like most other countries, has seen a dramatic decline in equity prices. On the other hand, activity in the housing market is high, which is reflected in strong credit growth. New orders in the construction industry indicate that residential construction will remain at a high level in the period ahead.

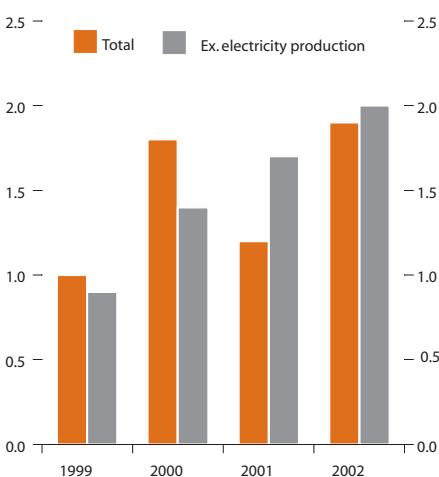
Norges Bank has left the key rate unchanged at 7 per cent since September of last year, after increases totalling 1½ percentage points in 2000. **Three-month money market rates** have been reduced to 7.1 per cent following the terrorist attacks on the USA 11 September, after remaining fairly stable at around 7.4 per cent over the past year. In response to signs of weaker growth in the global economy, many central banks have reduced their key rates. As a result, the interest rate differential between Norway and abroad has widened.

The effective krone exchange rate has appreciated over the last year, and is now about 4 per cent stronger than at the beginning of the year. The strengthening of the krone must be seen in the light of the marked depreciation of the Swedish krona. The krone has remained fairly stable against the euro at around 8.0.

Mainland GDP growth is now projected at 1.2 per cent in 2001 and 1.9 per cent in 2002, compared with 1.8 per cent in 2000. The growth estimate for this year must be seen in connection with developments in electricity production. As a result of heavy rainfall, electricity production rose to a very high level in 2000. Excluding electricity, mainland economic growth is projected to pick up between 1999 and 2002 (see chart 17).

The **labour market** is tight. In 2000, the labour force participation rate for the age group 16-64 was 80.7 per cent. On an international scale, only Switzerland and Iceland have a higher labour force participation rate than Norway. All in all, there is probably limited room for further growth in the labour force other than the potential implied by demographic changes. Total **employment** has increased moderately so far this year. Employment has continued to rise in the service sector and in the construction industry. On an annual basis, growth in the

Chart 18. GDP for Mainland-Norway



Growth in per cent from previous year

Source: Statistics Norway and Ministry of Finance.

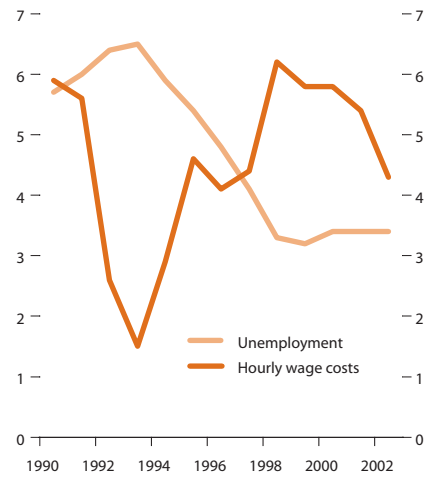
number of employed is now projected at about 1/2 per cent both in 2001 and 2002.

Unemployment (Labour force survey) remained stable at 3.4 per cent of the labour force both in the first and second quarter of this year. In the three months to end-July, unemployment rose to 3.6 per cent, but this must be seen against the background of the considerable uncertainty associated with the seasonally adjusted monthly LFS figures. Unemployment is projected at 3.4 per cent in 2001 and 2002.

After peaking in 1998, growth in labour costs has slowed somewhat over the last few years. Average **annual wage growth** is estimated at 4 1/2 per cent in 2001 and 4 1/4 per cent annually in the period 2002-2005. The estimate for this year is based on the assumption that wage drift will be approximately the same as the average for the 1990s. The contractual increase in the number of vacation days this year and next entails increased provisions for holiday pay for enterprises in 2000 and 2001. As a result, the increase in enterprises' labour costs will be approximately 3/4 percentage points higher than the annual wage growth in 2001.

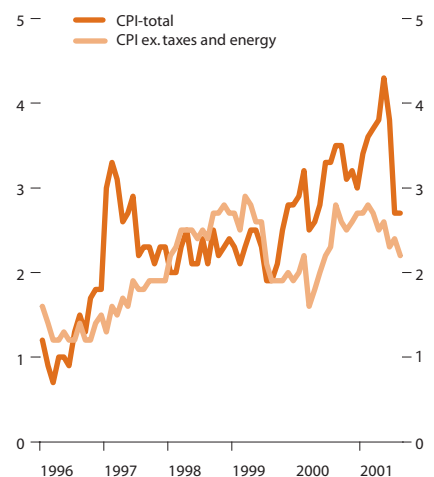
Consumer price inflation has been heavily influenced by changes in indirect taxes and the increase in electricity prices this year. Electricity prices rose in the first six months of this year, while they normally fall during the spring. Electricity prices have thus contributed to pushing up consumer price inflation, and in August the year-on-year rise in electricity prices was higher than 40 per cent. Even though the indirect tax programme for this year will only have a limited impact on average price inflation from 2000 to 2001, the impact over the year will be considerable. While the average rise in prices in the first half of the year was 3.8 per cent, the halving of VAT on food as from 1 July will push down the year-on-year rise in consumer prices markedly in the latter half of the year. Consumer price inflation fell in line with this to 2.7 per cent in July and August. Excluding changes in excise duties and energy prices, consumer price inflation has slowed somewhat in recent months. Consumer price inflation is now projected at 3.1 per cent from 2000 to 2001 and about 2 per cent in 2002. This is based on the assumption that the halving of VAT on food as from 1 July this year will contribute to reducing price inflation by about 1/2 percentage point from 2001 to 2002. Excluding changes in excise duties and energy prices, consumer price inflation is projected at 2 1/2 per cent both in 2001 and 2002.

Chart 19. Hourly wage costs and unemployment



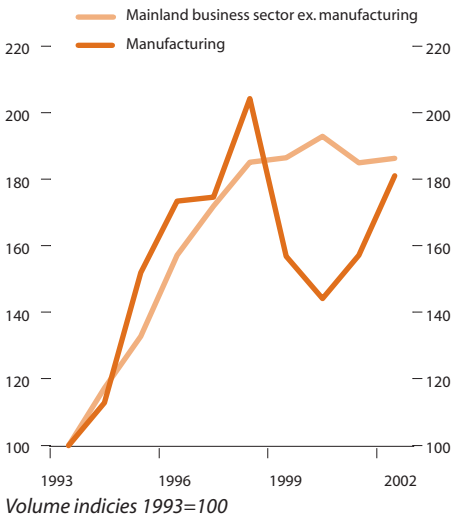
Growth in per cent from previous year and per cent
Source: Statistics Norway and Ministry of Finance.

Chart 20. Consumer price inflation



Growth in per cent from previous year
Source: Statistics Norway and Ministry of Finance.

Chart 21. Mainland fixed business investments

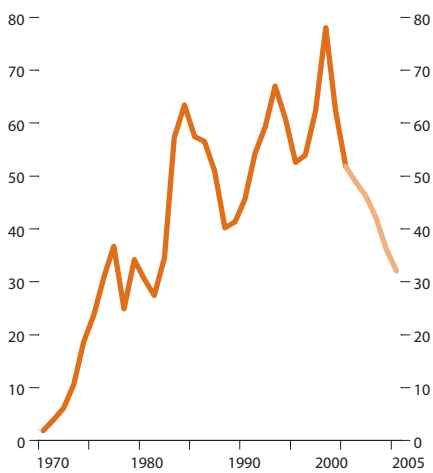


Source: Statistics Norway and Ministry of Finance.

Table 6 provides a summary of the macroeconomic projections for 2001 and 2002. The estimates are based on the following assessments:

- The outlook for export-oriented industries has deteriorated in recent months as a result of signs of weaker international growth, and the estimate for **traditional merchandise exports** has been revised downwards somewhat for this year. As a result of an expected pick-up in economic growth among our trading partners next year, growth in traditional merchandise exports is assumed to be stronger next year. Several years of a marked deterioration in cost competitiveness implies, however, that export growth may be lower than market growth.
- **Mainland business investment** is estimated to fall by 2½ per cent this year, followed by an increase of the same order next year. Manufacturing investment is pushed up by large investment projects in the metal industry. With an estimated increase of 9 and 15 per cent in 2001 and 2002, respectively, manufacturing investment will again reach a high level following the decline over the last few years. Investment in the service sector has expanded at a considerably slower rate than expected so far this year, and investment in this industry is now projected to decline somewhat both this year and next.
- **Petroleum investment** is projected to contract by about 5 per cent in 2001 and 2002. The estimates for 2001 and 2002 have been revised downwards somewhat compared with the figures in the Revised National Budget. The projected decline will contribute to curbing activity in mainland industries that supply the petroleum industry. Experience shows, however, that the estimates for petroleum investment tend to be highly uncertain.
- **Private consumption** is projected to increase by 2 per cent from 2000 to 2001, against 2.4 per cent in 2000. The moderate growth rate reflects the increases in interest rates last year and a relatively moderate growth in household real disposable income this year. However, growth in household real disposable income is expected to show a pronounced increase next year, partly as a result of the projected slower growth in consumer prices. With relatively stable household saving, this implies a consumption growth of 2¾ per cent next year.
- **Housing starts** have picked up markedly the last two years, reaching a level of about 26 000 new dwellings this year. This is the highest level recorded since 1988. Against the background of the sharp increase in housing starts, housing investment is now projected to rise by 7½ per cent between 2000 and 2001. In 2002, hous-

Chart 22. Investments in petroleum activities



NOK billion

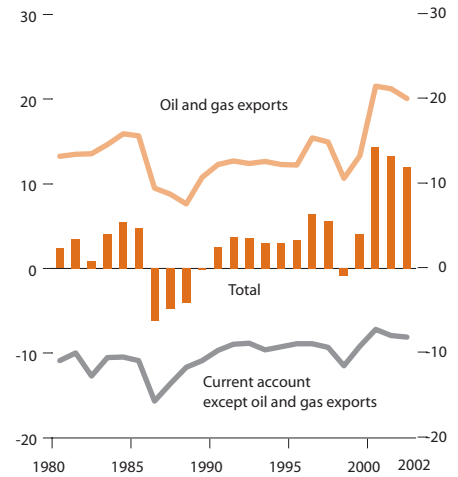
Source: Statistics Norway and Ministry of Finance.

ing investment is estimated to remain high, but is not expected to move up from the level in 2001.

- In line with the new guideline for **fiscal policy**, it is assumed that the use of petroleum revenues will increase in the years ahead. The Government budget bill for 2002 implies that about half of the increase in fiscal leeway will be used to increase expenditure and the remainder to reduce direct and indirect taxes.
- Our calculations are based on the technical assumption that short-term interest rates will move in line with implied forward rates as reflected in the yield curve for the money and bond markets. On 10 September, forward rates implied that three-month rates will decline from 7.2 per cent to 6.5 per cent towards the end of next year. As a technical assumption, the manufacturing industry's effective krone exchange rate is assumed to remain approximately unchanged ahead.
- **Oil prices** have averaged NOK 236 per barrel so far this year, compared with NOK 251 per barrel in 2000 as a whole. The average oil price is assumed to be NOK 230 per barrel this year and NOK 200 per barrel in 2002.
- **Petroleum production on the Norwegian continental shelf** is assumed to reach NOK 256 million sm³ o.e. in 2001, i.e. an increase of 5 per cent on the previous year. In 2002, production is expected to rise by a further 9 per cent. Combined with the other assumptions, this implies a **current account** surplus of NOK 196 billion in 2001, or 13 per cent of GDP. In 2002, the surplus is expected to fall to NOK 181 billion, or 12 per cent of GDP.

The main element of **uncertainty** surrounding the macroeconomic projections relates to developments in the international economy. The terrorist attacks on the USA 11 September have increased the risk of a more severe international setback. A more pronounced downturn will result in weaker growth for Norwegian export industries and other industries exposed to international competition. This may have spillover effects on domestic demand and activity. Even if world economic growth turns out to be weaker than assumed, the risk of a pronounced downturn in Norway remains limited. The Norwegian economy is well balanced. Unlike the situation following the upswing in the mid-1980s, the financial position of households is solid. As a result, a strong financial consolidation of the household sector will not be required to the same extent as at that time, should the economy weaken. Moreover, the high activity level in the North Sea will not be influenced by the first-round effects of the international slowdown. However, if oil prices fall and remain at a substantially lower level, the effects on the Norwegian economy may be stronger.

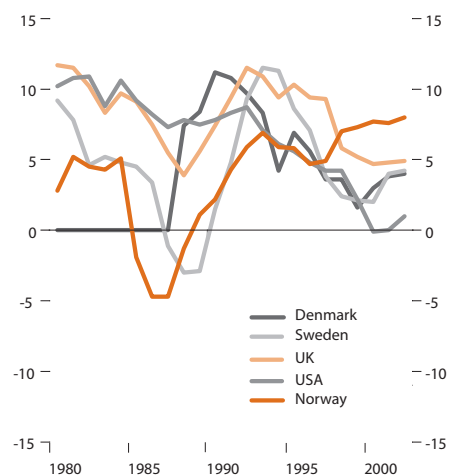
Chart 23. Current account of the balance of payment



Per cent of GDP

Source: Statistics Norway and Ministry of Finance

Chart 24. Household savings rate



Per cent of disposable income

Source: OECD, Statistics Norway and Ministry of Finance.

On the other hand, with a continued tight labour market, nominal wage growth may be higher than assumed in the years ahead. Household consumption may then increase further, particularly in the light of the historically high saving ratio recorded in recent years.

Table 6. Key figures

	NOK billion	Change from previous year, pct.	
	2000	2001	2002
Private consumption	608.0	2.0	2.7
Public consumption	271.0	2.1	1.5
Gross fixed capital formation	282.1	-1.0	1.4
Oil activities	58.9	-5.9	-5.0
Shipping	16.9	9.3	4.7
Mainland business sector	128.8	-2.5	2.8
Residential construction	37.1	7.6	0.8
Public sector	40.4	-1.6	4.8
Total domestic demand, incl. stockbuilding	1193.8	1.1	2.1
Exports	663.6	4.4	5.4
Of which: Traditional goods	212.1	4.0	3.6
Imports	433.5	3.3	3.0
Of which: Traditional goods	274.4	4.5	3.4
Gross Domestic Product	1423.9	1.7	3.2
Of which: Mainland Norway	1054.5	1.2	1.9
<i>Memorandum items:</i>			
Gross product manufacturing sector	130.2	1.2	1.1
Consumer price inflation	..	3.1	1.9
Wage growth	..	4½	4¼
Employment (persons)	..	0.5	0.6
Unemployment rate (per cent of labour force)	..	3.4	3.4
Current account surplus, NOK billion	203.6	196.3	180.7
Per cent of GDP	14.3	13.3	12.0
Net external assets, NOK billion	327.6	510.1	690.9
Per cent of GDP	23.0	34.6	45.8

Source: Statistics Norway and Ministry of Finance.