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NORWAY

August 2014

2014 ARTICLE IV CONSULTATION—STAFF REPORT; STAFF SUPPLEMENT; PRESS RELEASE; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR NORWAY

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2014 Article IV consultation with Norway, the following documents have been released and are included in this package:

- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on August 28, 2014, following discussions that ended on May, 23, 2014, with the officials of Norway on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on July 23, 2014.
- An **Informational Annex** prepared by the IMF.
- A **Press Release** summarizing the views of the Executive Board as expressed during its August 28, 2014 consideration of the staff report that concluded the Article IV consultation with Norway.
- A **Statement by the Executive Director** for Norway

The following document has been or will be separately released.

Selected Issues Paper

The publication policy for staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

NORWAY

STAFF REPORT FOR THE 2014 ARTICLE IV CONSULTATION

July 23, 2014

KEY ISSUES

Context: Overheating concerns are fading. Mainland (i.e., non-oil-and-gas) growth slowed to 2 percent and unemployment rose slightly to 3.5 percent in 2013. House prices have been largely unchanged for a year.

Monetary policy: The monetary stance is appropriate. The economy remains roughly at its potential, inflation is roughly at the 2.5 percent target, and moderating growth and the stabilization in the house prices suggest reduced overheating risks.

Financial sector policy: Capital requirements for banks have been strengthened ahead of the Basel III deadlines. Tighter capital standards for mortgage lending by both domestic and foreign banks are being implemented in cooperation with Danish and Swedish parent bank supervisors. With household debt and house prices still high, tighter limits on mortgages should be retained even if the house prices soften further.

Fiscal policy: Fiscal policy has kept the non-oil deficit well within the fiscal rule's limit on spending from the sovereign wealth fund (the Government Pension Fund Global or GPFG). However, there has still been a repeated fiscal stimulus in an economy roughly at capacity. More conservative use of GPFG resources to set a neutral fiscal stance would be preferable so long as the economy remains near potential.

Structural reforms: Improved competitiveness and increasing productivity growth would enhance shift to a non-oil-and-gas growth model. Improved efficiency in local public services and the selection of infrastructure projects, agricultural policy reforms, more neutrality in the tax system, and further reform to pension and sickness and disability systems would all help.

Consultation cycle: The Article IV discussion was conducted on the 12 month cycle in light of the Board's December 2013 decision to place Norway on the list of systemically important financial sector jurisdictions.

Approved By
Mahmood Pradhan and Ranil Salgado

Discussions took place in Oslo during May 13-23, 2014. The staff team was comprised of Mr. Dorsey (head), Mmes. Mircheva, Nowak, and Shirono supported by Mr. Dowling at headquarters (all EUR). Mr. Groenn (Executive Director) joined the discussions. The mission met with Minister of Finance Jensen and ministry staff, Governor Olsen and the staff of the Norges Bank, and the staffs of other key ministries, the Financial Supervisory Authority, Statistics Norway, representatives of the Productivity and Tax Commissions, labor and employer organizations, banks, and academics.

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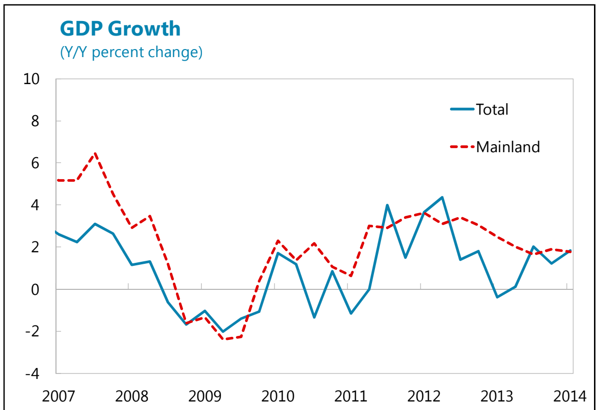
APPENDIX

CONTEXT: OVERHEATING CONCERNS ARE FADING

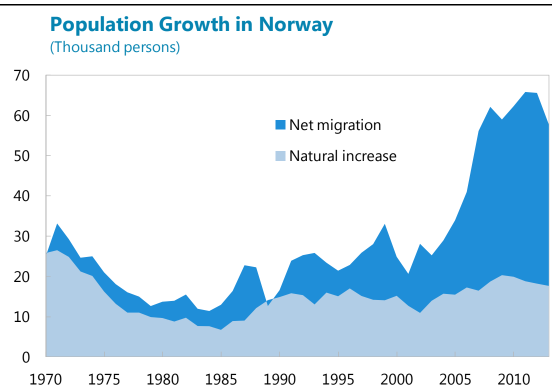
1. **A conservative minority government took office in October 2013, ending eight years of Labor party-led governments.** No major policy shift has taken place so far, but the government's economic policy platform emphasizes lower taxes, more infrastructure investment, greater private ownership, and measures to improve productivity and competitiveness. New challenges are emerging as oil-related investment is peaking and competitiveness concerns are becoming more pressing.

2. **Both mainland and offshore growth slowed in 2013** (Figures 1 and 2). Mainland growth moderated to 2.0 percent in part due to weak private consumption and mainland investment, and lower oil production kept offshore growth down. Households have increased their savings rate significantly in recent years, partly reflecting concerns about elevated debt levels.

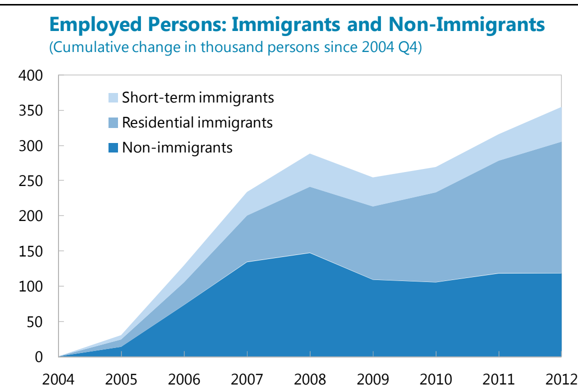


Sources: Statistics Norway and Fund staff calculations.

3. **Unemployment remains low in spite of a growing labor force** (Figure 3). The unemployment rate edged up slightly in the last year, but remains low at around 3.5 percent, notwithstanding net immigration that has added nearly 1 percent annually to the population in recent years and accounted for most of the gains in net employment (see Chapter 1 of the Selected Issues Paper on immigration and potential output).



Sources: Statistics Norway and Fund staff calculations.



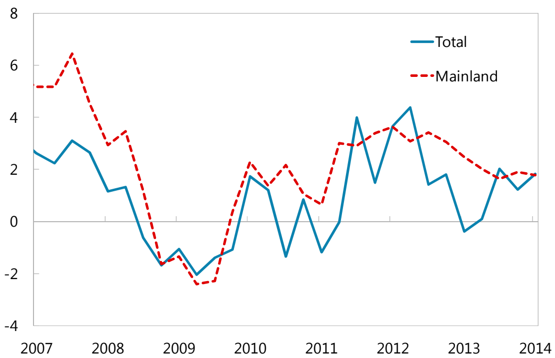
Sources: Ministry of Finance, Statistics Norway and Fund staff calculations.

4. **The housing market has shown signs of cooling.** House prices stabilized in mid-2013 although staff estimates suggest a substantial overvaluation (the average estimate is roughly 40 percent) in spite of a slight reduction in the valuation gap in 2013. A house price

Figure 1. Norway: GDP

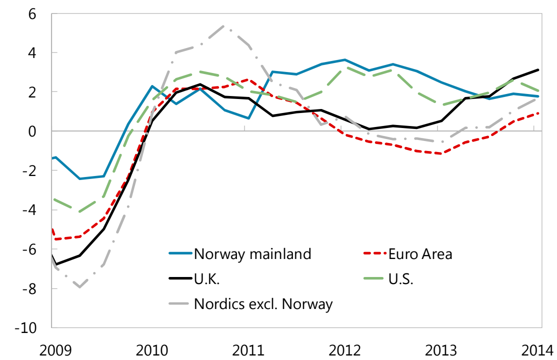
Mainland GDP growth started to slow in mid-2013…

GDP Growth
(Y/Y percent change, seasonally adjusted)



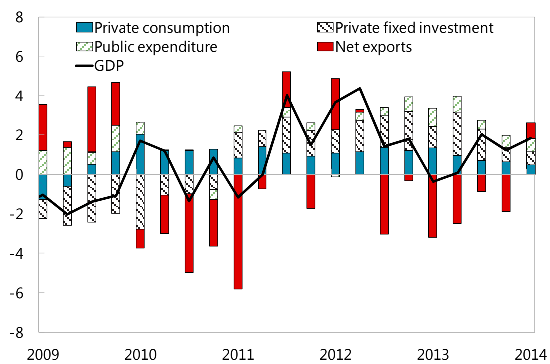
…despite an improving external environment with a pickup in growth of some of the main trade partners.

GDP Growth of Trade Partners
(Y/Y growth)



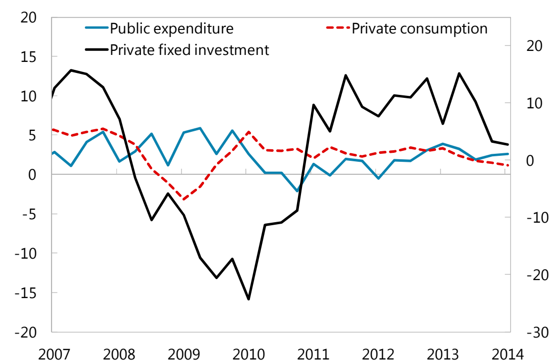
Slower growth in 2013 was due in part to weakening domestic demand.

Contributions to Real GDP Growth
(Y/Y percentage points, seasonally adjusted)



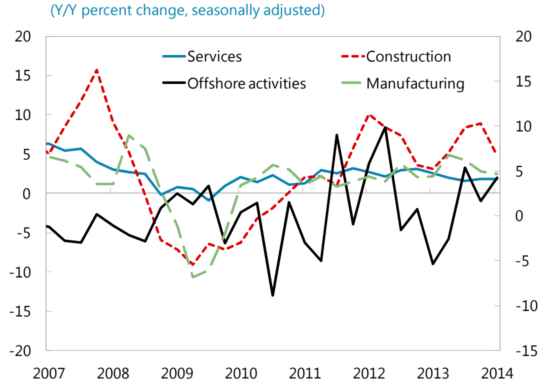
Private investment weakened substantially in mid-2013 with private consumption growth also decelerating.

Real Growth of Domestic Demand
(Y/Y percent change, seasonally adjusted)



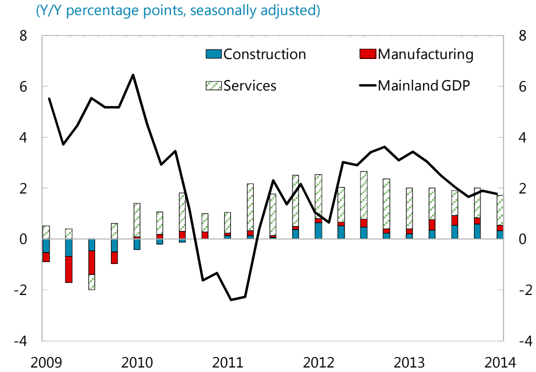
Growth has been mixed across sectors…

Real Growth of Production Side Components
(Y/Y percent change, seasonally adjusted)



…with a more pronounced decline in contribution of services to mainland growth since mid-2013.

Production Side Contributions to Mainland GDP Growth
(Y/Y percentage points, seasonally adjusted)

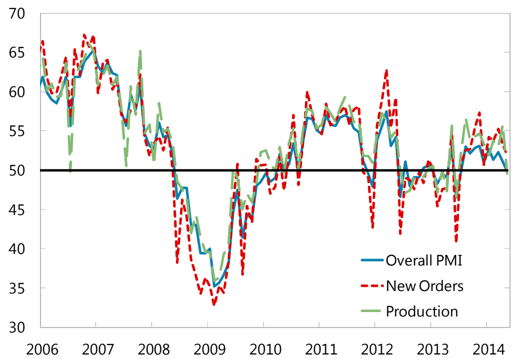


Sources: Haver Analytics and Fund staff calculations.

Figure 2. Norway: Key Activity Indicators

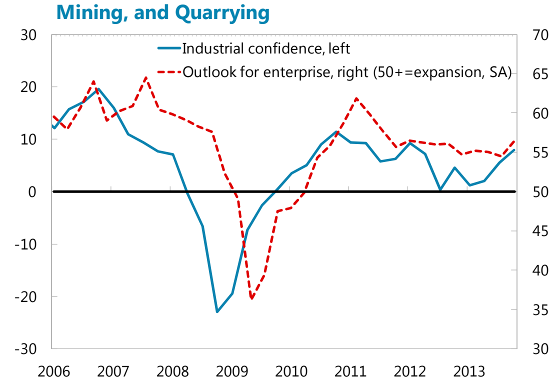
PMI indicators for manufacturing have improved since mid-2013 with the overall index pointing to an expansion.

Purchasing Manager Index
(50+ = expansion, SA)



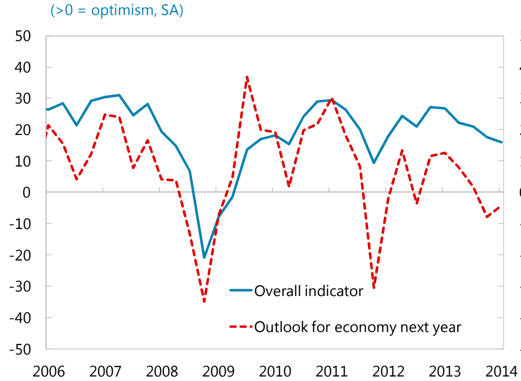
At the same time, confidence indicators improved slightly at the end of 2013.

Business Tendency Survey of Manufacturing, Mining, and Quarrying



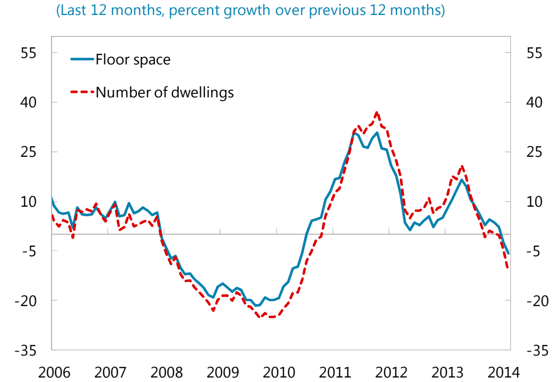
On the other hand, consumer confidence deteriorated significantly in 2013...

Consumer Confidence Indicator
(>0 = optimism, SA)



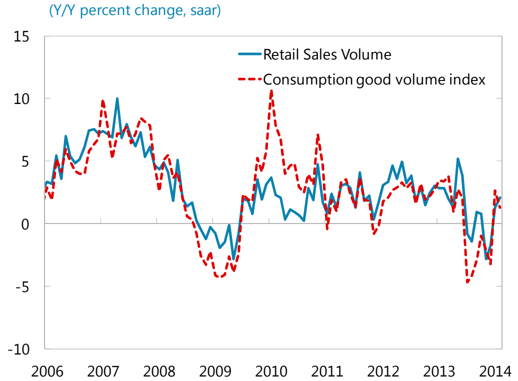
...in part, reflecting the cooling of the housing market with the number of new building starts declining.

New Building Starts
(Last 12 months, percent growth over previous 12 months)



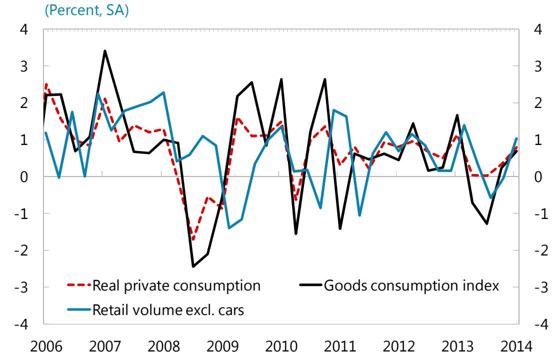
Retail sales dropped substantially in mid-2013...

Retail Activity
(Y/Y percent change, saar)



...with real consumption also weakening.

Real Quarterly Growth in Private Consumption vs. Other Consumption Indicators
(Percent, SA)

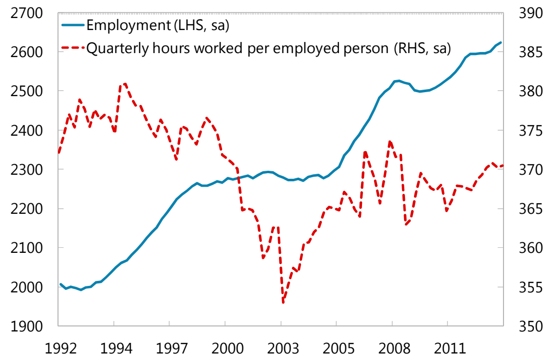


Sources: Haver Analytics and Fund staff calculations.

Figure 3. Norway: Labor Markets

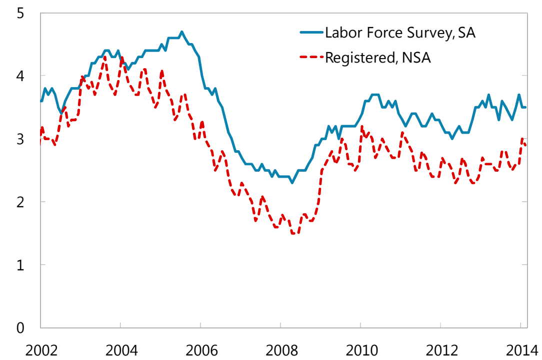
Employment continued to rise…

Employment and Hours
(Thousands, left; hours, right)



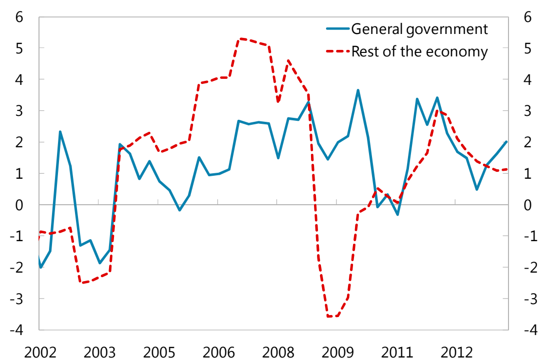
…while the unemployment rate rose slightly in 2013.

Unemployment Rate
(Percent)



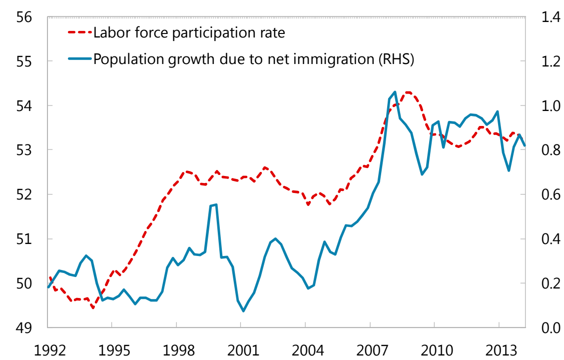
Working hours were rising in 2013 but at a lower rate than in 2012.

Growth in Hours Worked
(Y/Y percent change, seasonally adjusted)



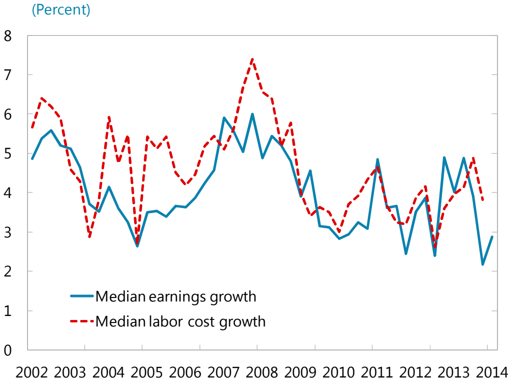
The labor participation rate has been flat while immigration slowed slightly in late-2013.

Labor Force Growth
(Percent of total population, left; 2-quarter annualized growth, right)



Median labor costs across sectors increased further in 2013, in line with higher earnings growth.

Earnings Growth and Labor Costs Across Sectors
(Percent)



At the same time, concerns about labor constraints continued to rise in manufacturing, until recently.

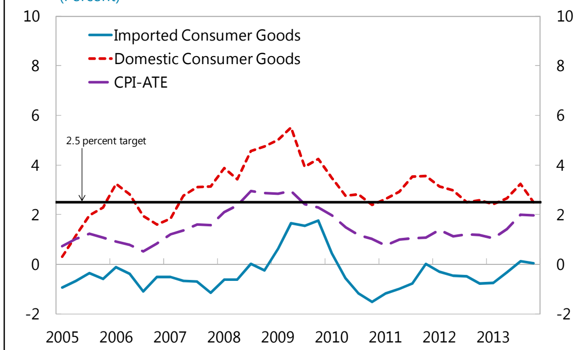
Labor Constraints
(Percent of survey responses)

Sources: Haver Analytics and Fund staff calculations.

correction that would bring house prices back to estimated equilibrium levels would trigger a decline in consumption by 4 percent (See 2013 Nordic Regional Report, Selected Issues).

5. **Inflation rose toward the target partly due to last year's exchange rate depreciation.** The Norwegian krone depreciated by 10 percent in nominal effective terms in 2013, and this pushed the main inflation index (CPI-ATE) to about 2.5 percent early this year after several years below the target (Figures 4).

Annual Inflation of CPI Components
(Percent)

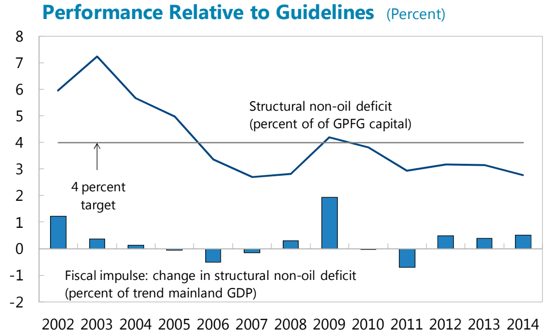


Sources: Norges Bank and Fund staff calculations.

6. **The 2013 fiscal outturn was well within the authorities' fiscal policy rule.** The structural non-oil deficit was 3.1 percent of GPFG assets and 5.1 percent of trend mainland GDP. However, the fiscal impulse (i.e., the change in the structural non-oil deficit as a share of mainland GDP) was slightly positive and lower than expected at 0.2 percent.[1]

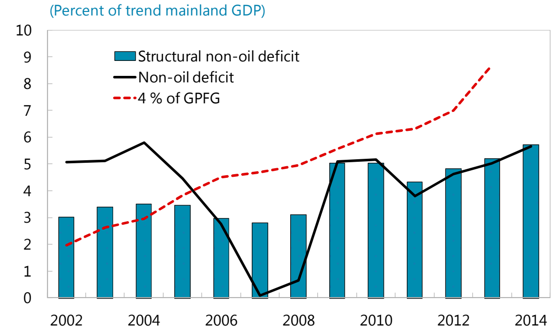
7. **The overall current account surplus remains high at 14 percent of mainland GDP but declined in 2013 partly due to weaker petroleum exports.** The non-oil trade deficit has been gradually rising and worsened further in 2013 (Figure 5). Terms of trade growth, which had been supporting the economy in recent years, also slowed in 2013.

Central Government Fiscal Stance and Performance Relative to Guidelines (Percent)



Sources: IMF World Economic Outlook, Norway Ministry of Finance and Fund staff calculations.

Central Government Balances
(Percent of trend mainland GDP)



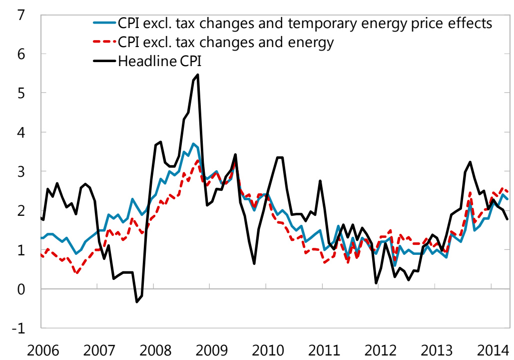
Sources: IMF World Economic Outlook, Norway Ministry of Finance, and Fund staff calculations.

[1] Debt sustainability is not an important consideration; gross public debt is about 30 percent of GDP and net financial assets are above 170 percent of GDP.

Figure 4. Norway: Price Developments

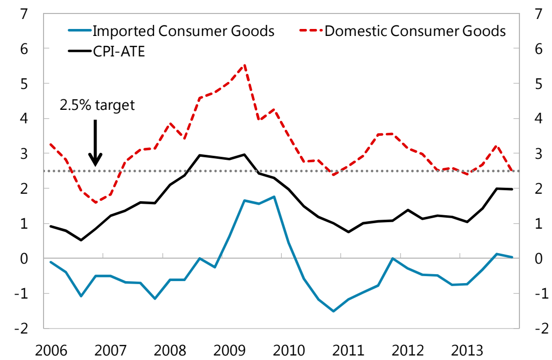
Inflation is rising closer to the 2.5 percent target…

Annual Inflation Rates
(Percent)



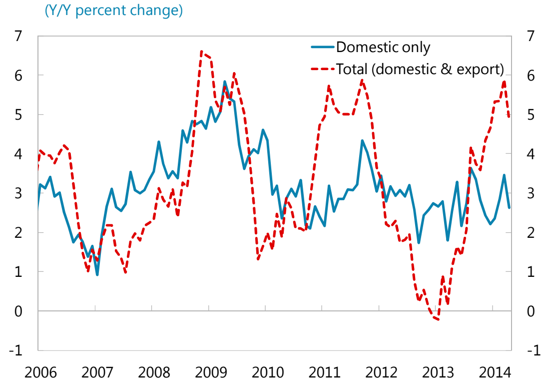
…in part, reflecting increasing pressures from import prices due to depreciation of the Norwegian krone.

Annual Inflation of CPI Components
(Percent)



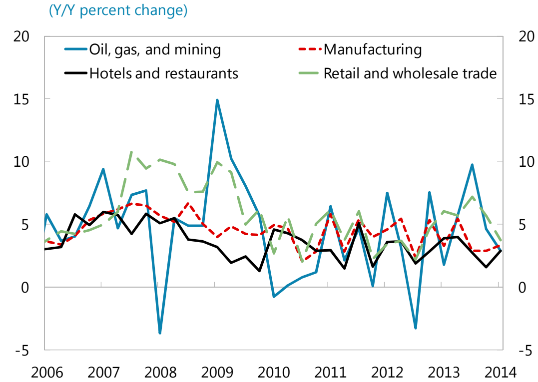
Producer price inflation also increased sharply throughout 2013…

Producer Price Index
(Y/Y percent change)



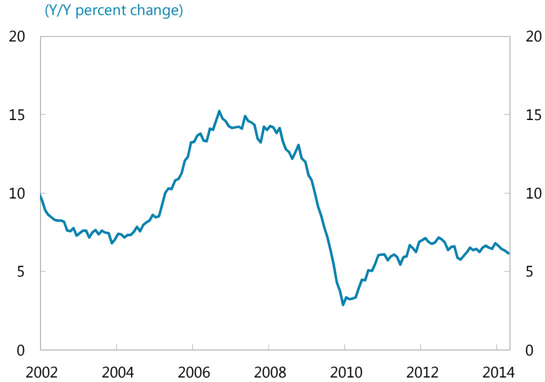
…and wages in the mainland economy continue to rise, most notably in the retail and wholesale sector.

Average Monthly Earnings by Sector
(Y/Y percent change)



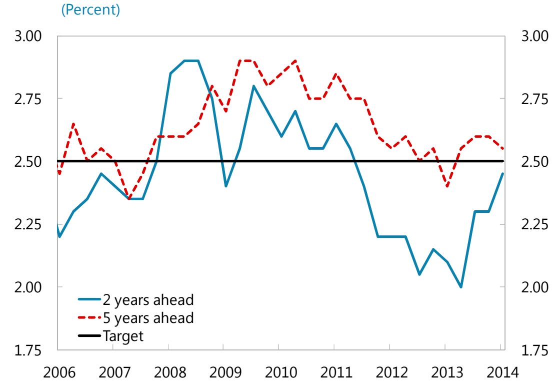
Domestic credit growth remains steady despite some weakness in domestic demand.

Domestic Credit (C2)
(Y/Y percent change)



Near-term inflation expectations are approaching the target while medium-term inflation expectations are well anchored.

Survey Based Inflation Expectations
(Percent)

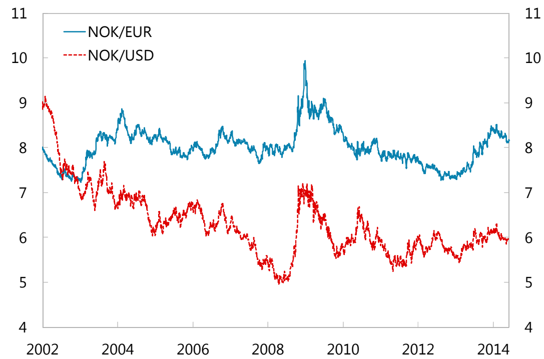


Sources: Haver Analytics, Norges Bank and Fund staff calculations.

Figure 5. Norway: External Developments

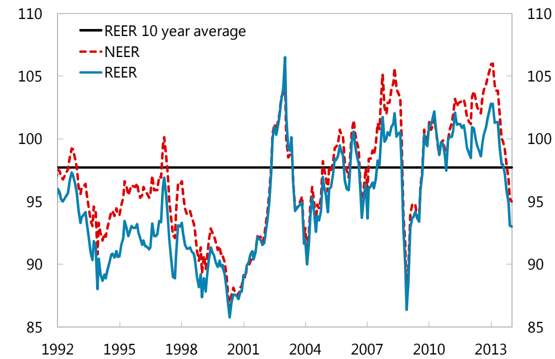
The Norwegian krone depreciated throughout 2013…

Bilateral Exchange Rates
(LCU/foreign)



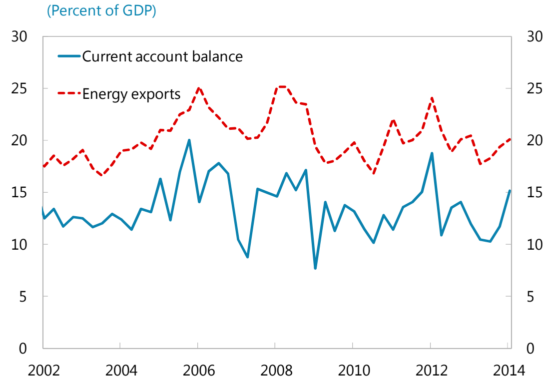
…and the real effective exchange rate is now slightly below its 10-year average.

CPI Based Effective Exchange Rates
(Index, 2005=100; increase indicates appreciation)



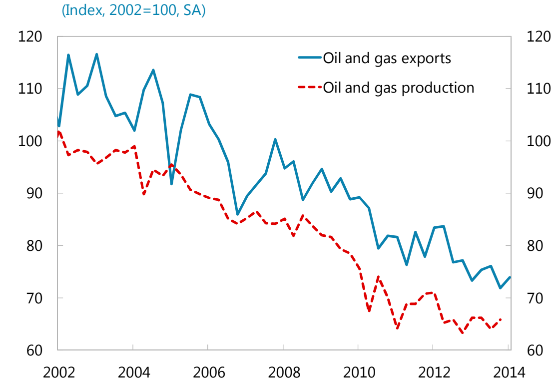
The current account surplus narrowed in 2013, reflecting weaker energy exports…

Current Account Surplus
(Percent of GDP)



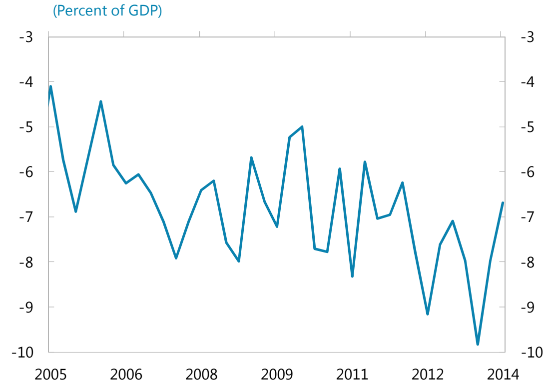
…while energy production continues to decline.

Energy Exports and Production
(Index, 2002=100, SA)



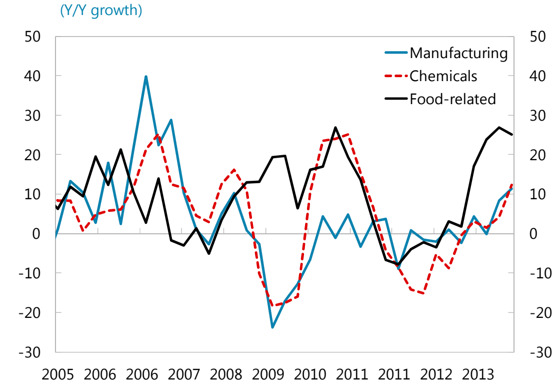
At the same time, the non-energy balance worsened further in 2013…

Non-Energy Exports and Service Trade Balance
(Percent of GDP)



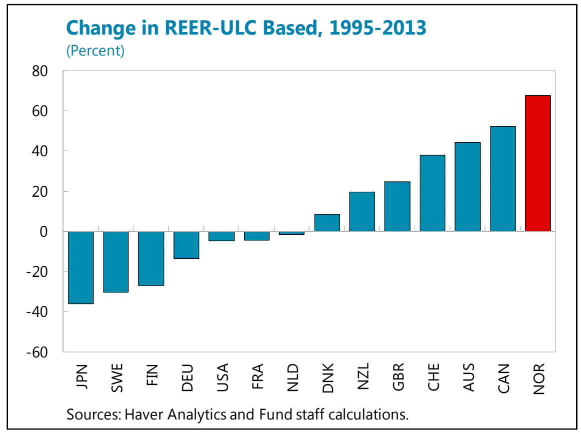
…partly due to very little recovery in manufacturing exports.

Exports of Industry
(Y/Y growth)

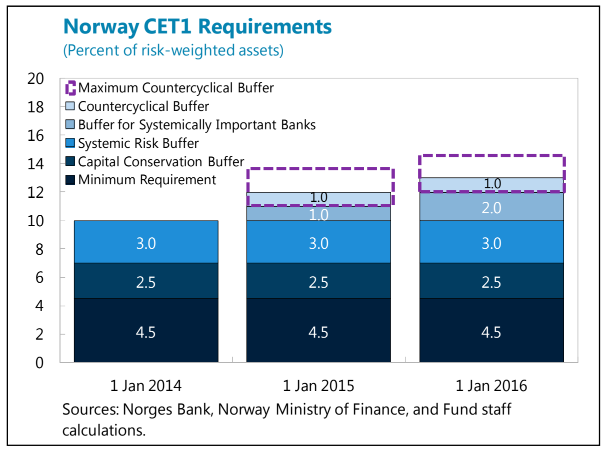


Sources: Haver Analytics, IMF Information System and Fund staff calculations.

8. **The exchange rate is roughly in line with fundamentals and desirable policies based on EBA results** (Box 1). The CPI-based real effective exchange rate (REER) is about 5 percent below its 10-year historical average, reflecting the recent depreciation of the Norwegian krone (Figure 5). However, REER deflated by unit labor costs (ULC) appreciated significantly over the past decades. The recent depreciation only modestly offsets the erosion of competitiveness, and non-oil export market share continued to decline (Figure 6).



9. **Banks' profitability has improved and capital ratios have strengthened.** All major banks meet the minimum Common Equity Tier 1 (CET1) requirement of 10 percent, although some banks will need to raise capital to meet the overall capital requirement of 13.5 percent in mid-2015 (14.5 percent for systemically-important banks). The return on equity for the largest banking groups rose to 14 percent in 2013 Q3. Banks continue to rely on wholesale funding, mostly in the form of covered bonds, and many banks still have some way to go before meeting the likely Liquidity Coverage Ratio (LCR) requirement. However, many banks still do not meet the Net Stable Funding Requirement (NSFR).



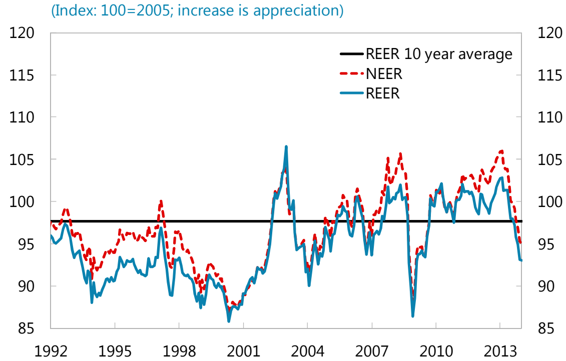
10. **Norway's financial system is part of a tightly integrated Nordic-Baltic system.**[2] Inward links are mainly from Swedish and Danish banks with combined market shares of a quarter to a third. The largest domestically-headquartered bank, DNB, has relatively small external operations concentrated in Nordic and Baltic countries and the shipping industry. More information on these links is in the Nordic Regional Report and the Baltic Cluster Report from 2013 and 2014 respectively and their accompanying selected issues papers.

[2] A Financial Sector Assessment Program mission is planned for late 2014/early 2015 for discussion with the 2015 Article IV consultation. Because Norway's financial sector is considered to be systemically important, subsequent financial stability assessments are expected to take place every five years.

Box 1. External Stability, Competitiveness, and the Real Effective Exchange Rate (REER)

The CPI-based REER appears to be broadly in line with fundamentals. Reflecting recent nominal depreciation, the CPI-based REER is slightly below the 10-year historical average at end-2013. IMF External balance assessment (EBA) estimates vary, but support the view that the real exchange rate is broadly in line with fundamentals and desirable policies: While the real exchange rate approach shows no significant misalignment, the macroeconomic balance approach suggests a mild undervaluation and the external sustainability model points to the opposite.

CPI Based Effective Exchange Rates
(Index: 100=2005; increase is appreciation)



Sources: IMF INS and Fund staff calculations.

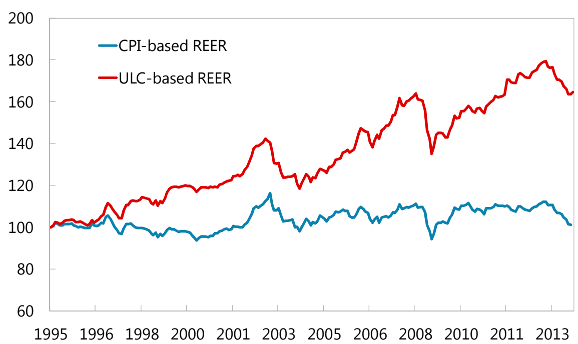
Estimates of Competitiveness Using EBA Methodologies 1/

Methodology	CA gap (percent of GDP)	REER gap (Percent)
Macroeconomic balance (MB) approach	0.6	-2.0
External sustainability (ES) approach	-2.8	9.0
Equilibrium real exchange rate approach	-	0.0

Source: Fund staff calculations.

1/ EBA (External Balance Assessment). CA gaps: minus indicates overvaluation. REER gaps: minus indicates undervaluation. REER deviations between -10 and +10 mean the real exchange rate (RER) is close to balance. EBA estimates are based on data available in April 2014.

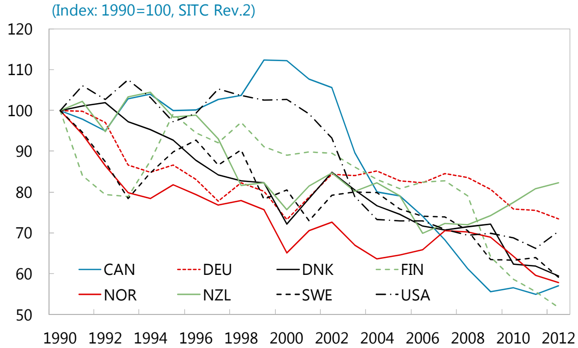
Real Effective Exchange Rates
(Index: 1995=100)



Sources: IMF Institute and Fund staff calculations.

However, the ULC-based REER suggests an erosion of long-term cost competitiveness. Norway's ULC-based REER has appreciated significantly for the past two decades, reflecting strong wage growth, and real ULCs have doubled since 1995. The recent depreciation of the Norwegian krone has reduced the overvaluation at the margin, but the ULC-based REER is still roughly 60 percent higher than the 1995 level. This has been offset by terms of trade gains, but there is no reason to expect these to persist indefinitely.

Non-oil Export Shares
(Index: 1990=100, SITC Rev.2)



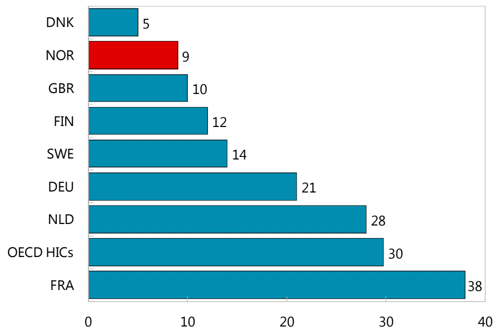
Sources: COMTRADE, World Integrated Trade Solutions and Fund staff calculations.

The declining non-oil export market share also suggests weakening competitiveness. Robust GDP growth driven by high oil prices and large terms of trade gain has masked slowing productivity growth in recent years. Despite the fiscal rule, the insulation from the Dutch disease effects does not seem to have been complete.

Figure 6. Norway: Competitiveness

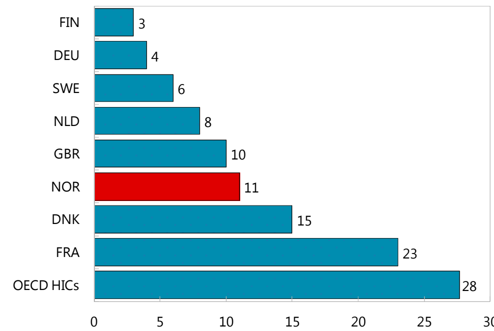
Norway ranks relatively high in the World Bank's Doing Business indicator…

Norway: Ease of Doing Business Overall Rank
(Rank: 1 is highest, 189 is lowest)



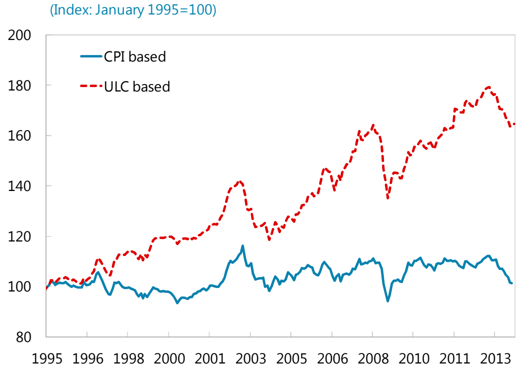
…and on the World Economic Forum's Global Competitiveness Index.

Norway: Global Competitiveness Index
(Rank: 1 is highest, 148 is lowest)



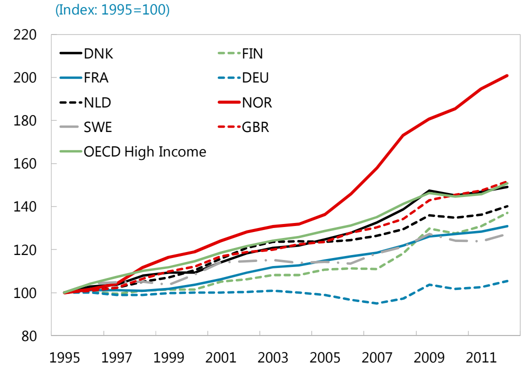
However, the ULC-based REER has appreciated substantially over the past decades, suggesting erosion in competitiveness.

Real Effective Exchange Rates
(Index: January 1995=100)



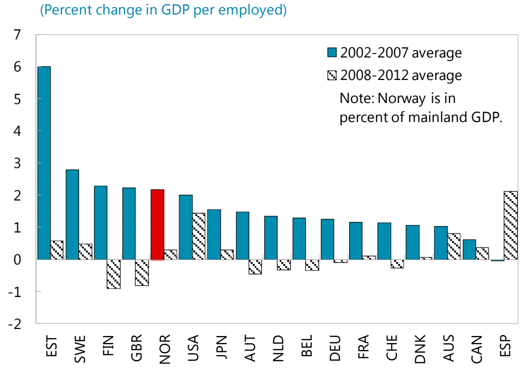
High wage growth in Norway outpaced its peers by a large margin…

Unit Labor Costs
(Index: 1995=100)



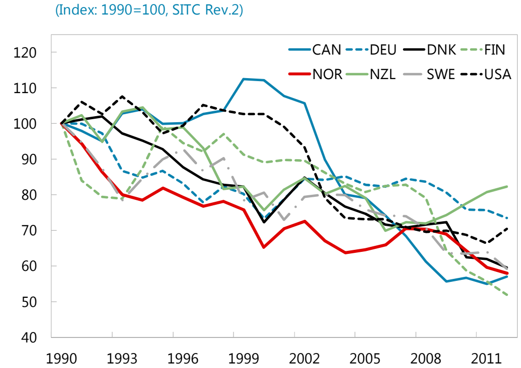
…while productivity growth has declined markedly recently.

Productivity Growth Before and After Crisis
(Percent change in GDP per employed)



At the same time, Norway's non-oil exports continue to lose market shares.

Non-oil Export Shares
(Index: 1990=100, SITC Rev.2)



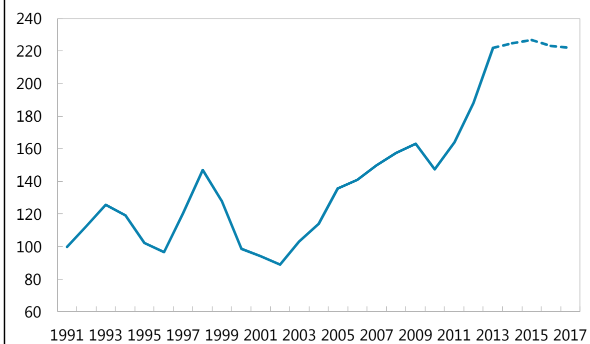
Sources: COMTRADE, OECD, World Bank Doing Business 2014, World Economic Forum Global Competitiveness 2013, World Integrated Trade Soulutions and Fund staff calculations.

OUTLOOK AND RISKS: TAILWINDS FROM OFFSHORE ACTIVITY ARE COMING TO A HALT

11. **The near-term outlook remains stable with moderate growth and inflation.** With the economy roughly at potential, mainland GDP growth is projected to slow to 1.9 percent in 2014 and rebalance as domestic consumption and investment moderate and a modest recovery in trade partners' growth boosts external demand. Inflation is projected to slow to about 2 percent as the effects of the recent depreciation wear off. Unemployment is projected to rise slightly through 2015.

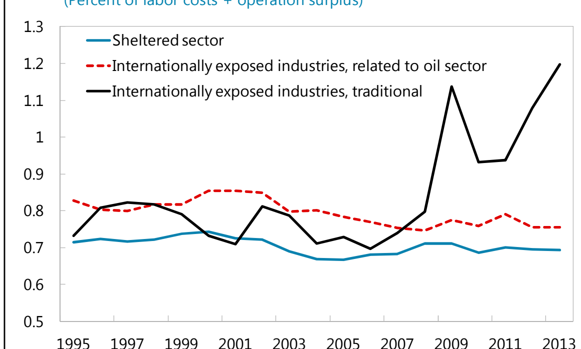
12. **The medium and longer term present new challenges because of the expected slowdown in oil and gas investment.** Steadily increasing oil and gas investment over the last decade culminated in a 17 percent growth rate in 2013. This investment and the provision of other goods and services to the oil and gas sector has provided persistent stimulus to the mainland economy. The increasing role of mainland business in supplying oil and gas sector has boosted growth and provided highly-paid jobs, but it has also pushed up unit labor costs and undercut competitiveness elsewhere in the mainland economy. With this investment expected to flatten out in 2014-15 before beginning a slow decline, new sources of growth are needed. The staff's central forecast is a continuation of growth with only a modest rise in unemployment in the next few years. However, this is based on a scenario in which the sources of growth shift smoothly away from supplying the oil and gas sector to other parts of the economy.

Petroleum Investment
(Index, 1991=100)



Sources: Norges Bank and Fund staff calculations.

Wage Shares
(Percent of labor costs + operation surplus)



Sources: Statistics Norway and Fund staff calculations.

13. **There are risks to this central scenario.**

- ***A sustained decline in oil and gas prices*** triggered by slower global growth or other factors would have widespread effects. The fiscal rule would largely insulate the economy from the direct effects of lower oil revenue. However, a decline in oil and gas prices would undercut growth through a reduction in demand for mainland goods and services, and through a reduction in private demand due to confidence and income effects.

- ***A significant reduction in housing prices*** could be triggered by a reduction of oil prices or other shocks to demand or confidence. While house prices have stabilized recently, it is too early to declare an end to the housing boom or rule out a sustained price decline. A large house price decline would likely reduce household consumption with adverse consequences for retail trade, construction, and commercial real estate and lenders to those sectors.

- ***A more difficult transition to a growth model less dependent on supplying the oil and gas sector*** could result in slower growth and higher unemployment during the shift. The staff's central scenario assumes that the transition will be relatively smooth, but competitiveness challenges from high wage levels could inhibit the transition.

Authorities' views

14. **The authorities generally agreed with the risk assessment.** They noted that global shocks would affect Norway mostly through the channel of oil and gas prices. They agreed that housing prices and related household debt levels presented complex risks. They did not forecast sustained declines in house prices and noted that both bank and households had increased buffers through higher capital and saving respectively. They put considerable emphasis on the risks stemming from the slowdown and eventual reversal of demand from the oil and gas sector.

POLICY DISCUSSIONS: SUPPORTING THE TRANSITION TO A NEW GROWTH MODEL

Norway's medium-term prospects remain favorable, but the economy faces potential challenges from the projected peak in oil-related activity in the mainland economy. Robust oil-related growth in recent years has masked slowing productivity growth in the mainland economy and the erosion of competitiveness. Estimates of output suggest that oil and gas production will pick up over the medium term but start to decline around 2021. However, the decline in investment and other demand from the oil and gas sector is expected to begin in 2015. Actions are needed to ensure that the mainland economy serves as a robust source of growth when offshore activity winds down.

A. Monetary Policy to Meet the Inflation Target

15. **The monetary policy rate has been held at 1.5 percent since March 2012.** Recent tensions among the considerations for setting the policy rate are abating. Inflation is now roughly at its 2.5 percent target, lessening the argument for a rate cut to achieve the inflation objective. At the same time, growth is slowing, unemployment is edging up, and house prices have leveled off (Figure 7). These diminish the argument for a rate increase to offset

overheating pressures. In this context, the staff views the Norges Bank's monetary stance as appropriate. Nevertheless, the policy rate will eventually have to normalize to a level somewhat above the inflation target (Figure 8).

Authorities' views

16. **The authorities agreed on the assessment of the policy stance, as it follows their own assessment.** They agreed that the policy rate would eventually need to normalize, but noted that it would take several years under their current forecasts or market expectations.

B. Fiscal Policy to Stabilize the Economy and Save for the Future

17. **The 2014 revised budget entails an expansionary fiscal stance with a non-oil structural deficit of 5.8 percent of mainland GDP.** This is equivalent to 2.8 percent of the GPFG assets rather than the 4 percent average real return on GPFG assets assumed for the fiscal rule. However, the 2014 fiscal impulse is projected at 0.7 percent, adding stimulus in an economy roughly at capacity.

18. **A neutral fiscal stance would be appropriate with still-low unemployment.** Because GPFG assets are growing more rapidly than the mainland economy, even keeping the non-oil deficit at the current share of assets would imply a growing deficit relative to GDP and a positive fiscal impulse. The government's implementation of the fiscal rule in a manner that keeps the non-oil deficit well below 4 percent of GPFG assets is appropriate, but an even smaller transfer of GPFG resources to the budget to maintain a neutral fiscal stance would be better so long as the economy remains near potential.

19. **The 2014 budget includes some minor tax reductions.** These include: (i) a reduction of the tax rate on personal income from 28 percent to 27 percent; (ii) a reduction of the tax rate on net wealth by 0.1 percentage point to 1 percent; and (iii) elimination of the inheritance tax. These changes reduce taxes by ¼ percent of GDP in 2014 on an accrual basis. Further reforms are planned, and a tax commission is looking into options. Staff argued for a phasing out of tax preferences for housing and eliminating other distortions in capital taxation, and noted that more neutrality in the tax system could help to promote efficiency and support the transition to a new growth model (see Section D).

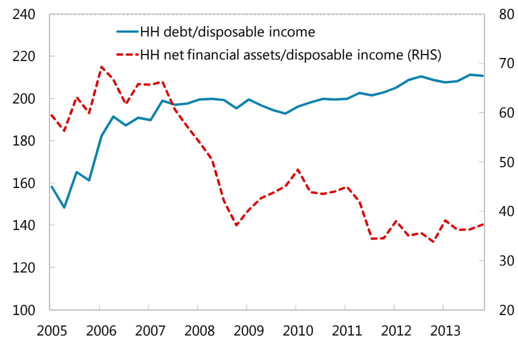
Authorities' views

20. **The authorities recognize the risk of excessive fiscal stimulus from spending too large a fraction of GPFG assets, and this is reflected in their 2014 budget.** However, they placed greater emphasis on reducing the overall tax burden as a means of promoting competitiveness. In their view, the most effective means of doing this is to simplify the tax code and reduce overall rates, particularly on corporate income taxes, and improve the efficiency of public expenditures without reducing services.

Figure 7. Norway: Household and Corporate Sector

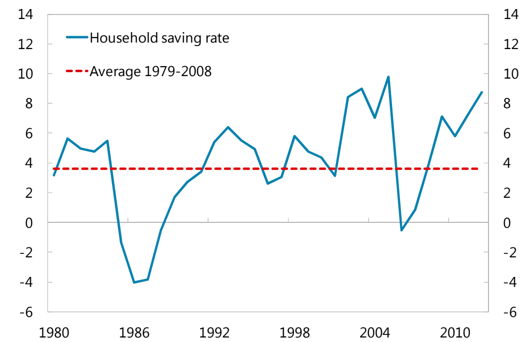
Household debt continues to be elevated while net financial assets remain below pre-crisis levels.

Household Financial Position
(Percent of disposable income)



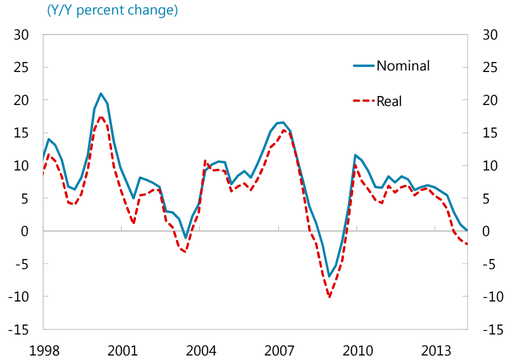
On the other hand, the household savings rate is on the rise, partly reflecting concerns about elevated debt levels.

Household Savings Rate
(Percent of disposable income)



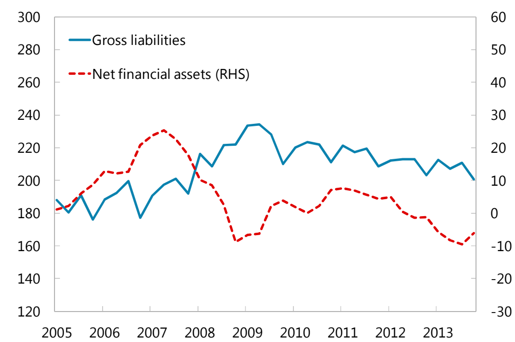
The housing market is showing signs of cooling with real house prices falling in 2013.

House Prices
(Y/Y percent change)



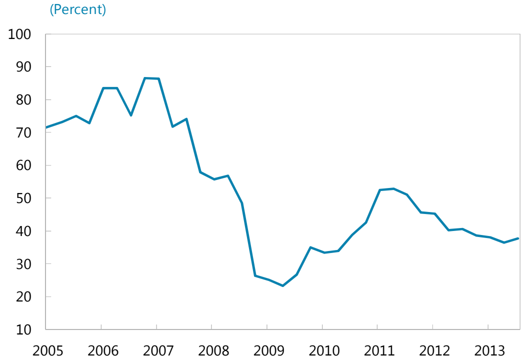
Net financial assets of non-financial corporations (NFCs) have been declining recently...

Nonfinancial Corporation Financial Position
(Percent of mainland GDP)



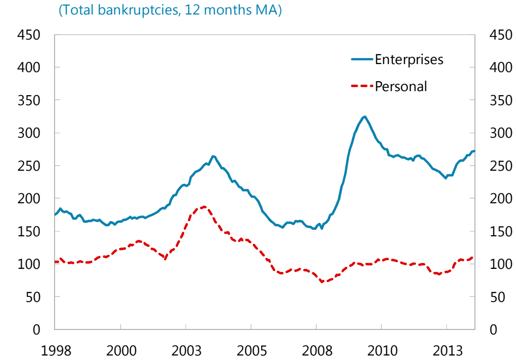
...and the debt-service capacity of NFCs has also fallen, suggesting a possible future rise in bank losses.

Debt-Service Capacity of Listed Enterprises 1/
(Percent)



At the same time, the number of bankruptcies has picked up while remaining higher than the pre-crisis period.

Number of Bankruptcies
(Total bankruptcies, 12 months MA)



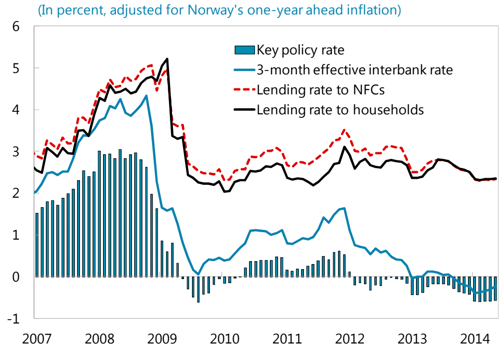
Sources: Haver Analytics, Norges Bank, Statistics Norway and Fund staff calcuations.

1/ Pre-tax profit plus depreciastion and amortisation for the previous 4 quarters as a percent of interest-bearing debt for non-financial enterprises included in the OBX index, excluding Statoil.

Figure 8. Norway: Credit Developments

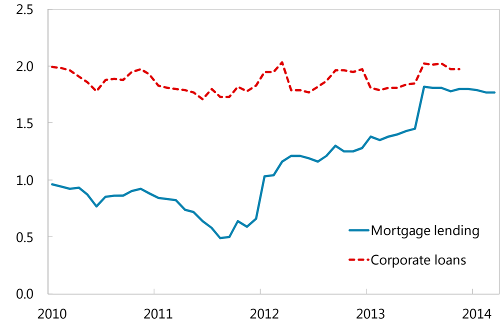
Recently, Norges Bank's monetary easing has been effectively transmitted into domestic lending rates…

Real Interest Rates
(In percent, adjusted for Norway's one-year ahead inflation)



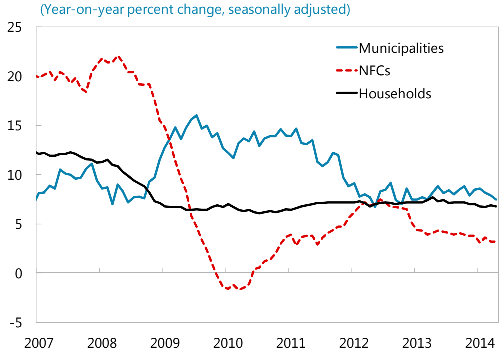
…while bank margins on mortgage lending are at a three-year high.

Margins on Private Sector Lending[1]
(Percent)



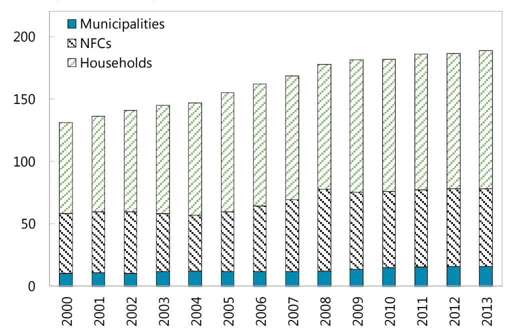
Lending to the private sector has continued to grow moderately in recent years…

Growth in Domestic Credit
(Year-on-year percent change, seasonally adjusted)



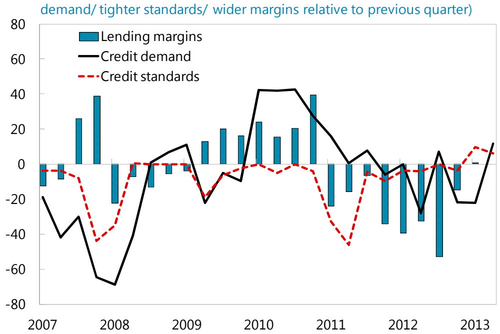
…broadly in line with the growth in the mainland economy while the ratio of debt to GDP has stayed at roughly the same high level since 2011.

Domestic Credit
(Percent of GDP)



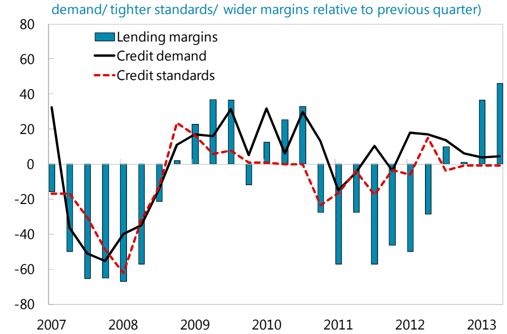
In late 2013, banks modestly relaxed loan standards for households as credit demand slowed, in part reflecting wider lending margins…

Household Loans: Demand and Credit Standards
(In percent of responses, negative net percentage balances indicate lower demand/ tighter standards/ wider margins relative to previous quarter)



…whereas corporate credit demand remained broadly unchanged, even though credit standards and margins on lending to enterprises have softened.

Corporate Loans: Demand and Credit Standards
(In percent of responses, negative net percentage balances indicate lower demand/ tighter standards/ wider margins relative to previous quarter)



Sources: Consensus Economics, Haver Analytics, Statistics Norway and Fund staff calculations.

C. Macroprudential Policies to Insure Against Banking Crises

21. **Implementation of the CRD IV/Basel III requirements is moving well ahead of the schedule required by Basel III** (Figure 9).

- All large Norwegian banks already meet the CET1 capital requirement, effective from July 2014.
- Counter-cyclical capital buffers will go into effect from end-June 2015 (see Box 2).
- Three financial institutions have been designated as domestic systemically important banks. These banks account for more than 45 percent of lending, and they will be subject to an additional capital surcharge of one percent in mid-2015 that will rise to 2 percent one year later.
- While DNB and other larger commercial banks meet the likely LCR requirement as of 2013 Q3, many savings banks still have some way to go to meet the LCR in its current form.

22. **Changes in risk weights for mortgages are also underway.**

- The government raised the minimum loss-given-default (LGD) risk model parameter from 10 percent to 20 percent in October 2013. The risk weights for residential mortgages ranged from 10-15 percent before, and a minimum LGD requirement of 20 percent is expected to increase the average risk weighting of residential mortgage loans to about 20 percent.
- The same capital requirements for mortgages are expected to apply to branches of Danish and Swedish banks through agreements among the Nordic authorities, however the details of how this will be done are still being worked out. This should result in these foreign branches lending in line with the regulatory framework in Norway.
- Staff supported tighter capital standards for mortgage lending for both domestic and foreign banks and the efforts to harmonize prudential standards among Nordic countries.

23. **Nevertheless, vulnerabilities in the financial system remain.** Stricter capital requirements and tightening of loan-to-value (LTV) limits seem to have helped contain the increase in house prices, but valuations are still high (Box 3). Banks continue to rely on wholesale funding, and the deposit-to-loan ratio has not improved much. In this context, tighter capital standards and LTV limits on mortgages should be maintained even if house prices weaken further, and tighter limits on interest-only mortgage loans should be considered.

Figure 9. Norway: Banking Sector Developments

Capital positions of Norwegian banks have strengthened by 4.4 percentage points since 2008…

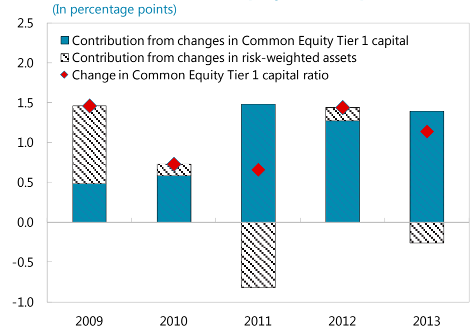
Common Equity Tier 1 Capital Ratio[1]

(In percent of risk weighted assets)

…mostly due to profit retention and equity issuance.

Evolution of Common Equity Tier 1 Capital Ratio[2]

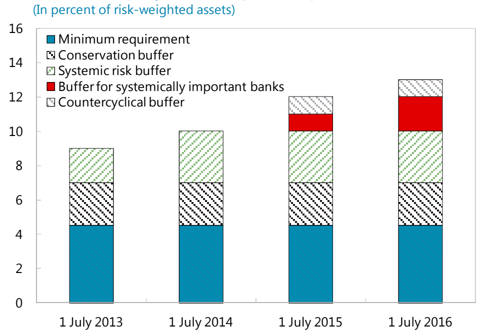
(In percentage points)



However, systemically important banks will need to raise more capital due to Basel III requirements, which are being phased in Norway ahead of the EU CRD IV schedule…

Common Equity Tier 1 Capital Requirements, 2013– 16

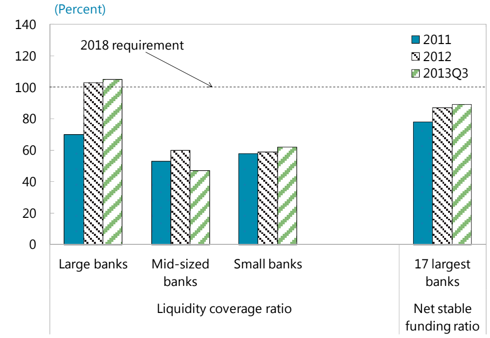
(In percent of risk-weighted assets)



…and many new banks still have some way to go before meeting the new liquidity requirements.

Liquidity Coverage and Net Stable Funding Ratios

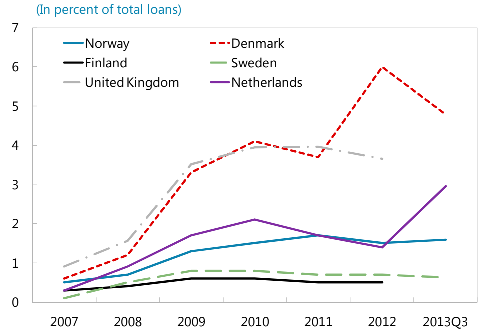
(Percent)



The ratio of impaired loans to gross loans remains relatively low compared to other countries…

Nonperforming Loans

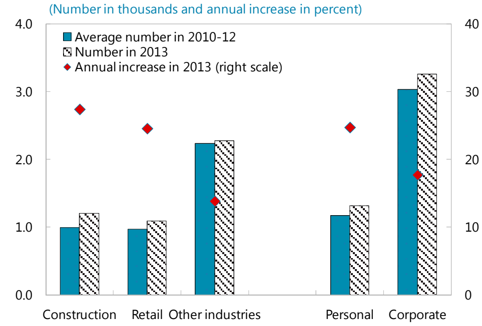
(In percent of total loans)



…but the bankruptcies have increased considerably in 2013.

Bankruptcies

(Number in thousands and annual increase in percent)



Sources: Norges Bank, Statistics Norway and Fund staff calculations.

[1] End-2013 data for the 6 largest Norwegian banking groups: DNB Bank, Nordea Bank Norge, SpareBank1 SR-Bank, SpareBanken Vest, SpareBank 1 SMN and SpareBank 1 Nord-Norge.

[2] Calculated as the weighted average for the 6 largest Norwegian banking groups at end-2013: DNB Bank, Nordea Bank Norge, SpaeBank 1 SR-Bank, Sparebanken Vest, SpareBank 1 SMN and SpareBank 1 Nord-Norge.

Box 2. Counter-cyclical Capital Buffers[1]

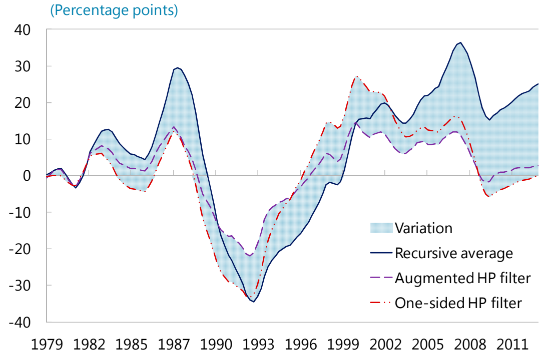
The Norges Bank is responsible under current regulations for providing advice to the Government, on the use of the countercyclical capital buffer in consultation with the FSA. The Ministry of Finance sets the level of the countercyclical capital buffer on a quarterly basis. The buffer will be set at between 0 and 2.5 percent of banks' risk-weighted assets.

The Norges Bank issued its first advice on the countercyclical capital buffer in December 2013. Subsequently, the Ministry of Finance set the buffer at 1 percent in line with Norges Bank's recommendation. It will become effective from end-June 2015. The counter cyclical capital buffer will eventually apply to all banks operating in Norway, but it will apply to branches of foreign banks after 2016.

The Norges Bank formulates its advice mostly based on four indicators: (i) the ratio of total credit to mainland GDP; (ii) the wholesale funding ratio of Norwegian credit institutions; (iii) the ratio of house prices to household disposable income; and (iv) commercial property prices. These indicators are compared with their historical trends, which are estimated with various methods, and the difference between indicators and trends is used as a measure of financial imbalances. These indicators gave a buffer guide of ¼ to 1¾ percent in mid-2013. The Norges Bank's final recommendation of 1 percent took into account other regulatory changes being implemented at the same time, the fact that imbalances were no longer building up, and the somehow slower growth in the Norwegian economy.

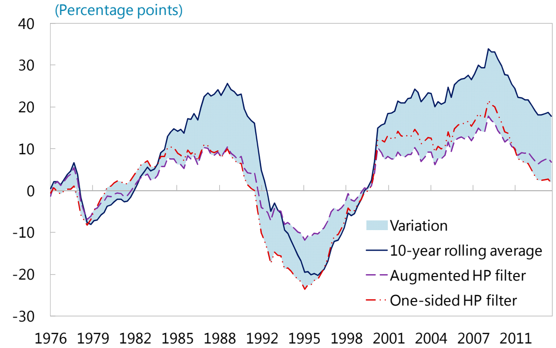
The current set of indicators is expected to be expanded over time as more experience is gained. The Norges Bank's advices will also take account of EU recommendations from the European Systemic Rick Board.

House Price Gap
(Percentage points)



Sources: Norges Bank and Fund staff calculations.

Credit Gap
(Percentage points)



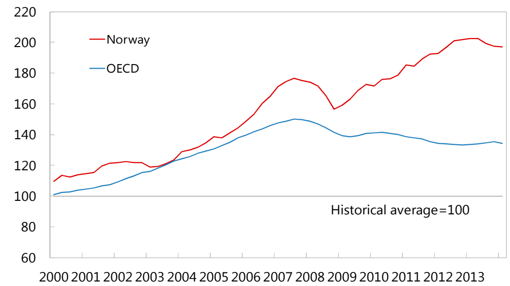
Sources: Norges Bank and Fund staff calculations.

[1] See also Norges Bank's *Monetary Policy Report with financial stability assessment 4/13.*

Box 3. House Prices and Prudential Policies

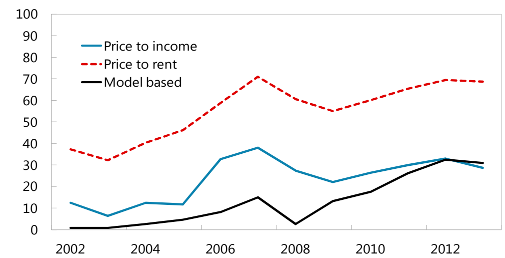
House prices in Norway rose strongly in recent years but stabilized in late 2012. Various factors have been contributing to rising house prices, including high income and wage growth, immigrant inflows, and supply constraints. Nevertheless, there are signs of overvaluation with a sustained increase in the price-to-income ratio and a large deviation in the price-to-rent ratio from its historical average. Staff's updated estimates on house price valuation gaps, based on the three measures of valuation used in the background papers for the 2013 Nordic Regional Report and Norway Article IV report, suggest a slight correction in the degree of overvaluation in 2013, but prices remain above equilibrium by varying degrees according to different estimates.

Real House Prices in Norway and OECD Average
(Index: historical average over 1970-2014Q1=100)



Sources: OECD and Fund staff calculations.

Estimated House Price Valuation Gaps in Norway*
(Percent)

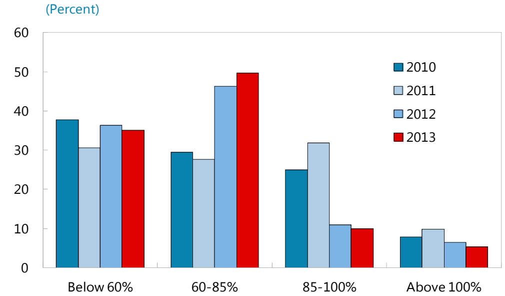


Sources: OECD and Fund staff calculations.
*Based on the methodologies as in the 2013 NRR and 2013 Norway Article IV Selected Issues.

The authorities have taken various measures to contain increases in house prices in recent years. The FSA introduced guidelines in March 2010 that set recommended limits on loan-to-value (LTV) and loan-to-income (LTI) ratios for mortgages. The FSA further lowered the cap on the LTV ratio on mortgages to 85 percent in December 2011, along with other tightening measures. Higher risk-weights on mortgage lending are also being implemented. In October 2013, the Ministry of Finance raised the minimum loss-given-default (LGD) risk model parameter from 10 percent to 20 percent. The risk weights for residential mortgages have on average ranged from 10–15 percent before. A minimum LGD requirement of 20 percent is expected to increase the average risk weighting of residential mortgage loans to about 20 percent. Additional requirements for IRB-models are also being considered.

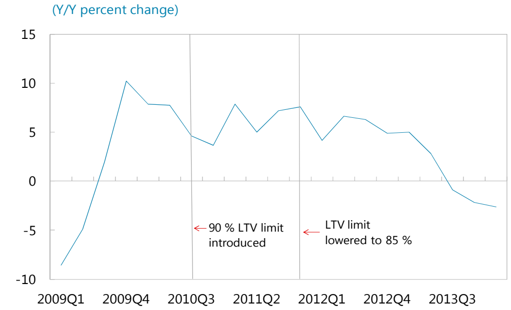
While it is difficult to disentangle the impact of prudential measures on house prices from other factors, these measures may have helped to dampen house price growth. For example, new loans exceeding the FSA-recommended 85 percent LTV limit fell to 17 percent in 2012 in spite of robust income growth and falling unemployment, suggesting that the LTV cap may have started to have some impact.

Distribution of LTV for New Loans 1/
(Percent)



Sources: Norway FSA and IMF staff calculations.
1/Based on FSA's annual survey.

Real House Price Growth Rate
(Y/Y percent change)



Sources: OECD and Fund staff calculations.

Authorities' views

24. **The authorities generally agreed with staff's assessment.** New capital adequacy regulation for banks adopted by the parliament in June 2013 contains a set of macroprudential tools and powers, which are already in place to increase capital levels for Norwegian banks. Nevertheless it is still important to follow up Norwegian banks' capital adequacy, to ensure that they are well prepared to meet downturns in the economy. The Nordic cooperation will continue, including the efforts to improve comparability among Nordic banks and facilitate transparency and market discipline.

D. Structural Reforms to Promote a New Growth Model

25. **Competitiveness concerns are becoming more pressing.** Robust growth driven by high offshore activity and large terms of trade gains has masked a decline in wage competitiveness relative to peer countries. With demand from the offshore economy peaking, the mainland economy has to shift to a growth model less dependent on supply the oil and gas sector. Staff welcomed the authorities' initiatives in this area, including setting up a productivity commission to propose specific policies and starting a process to reassess the extent of state ownership. These issues are explored in more detail in Chapters 2 and 3 of the Selected Issues Paper.

26. **There are clear areas for competitiveness and productivity enhancing reforms.**

- **Public services provided at the local level could be improved and made more efficient.** Small municipalities struggle to achieve economies of scale, and there is scope to both improve services and save resources through consolidation guided by cost-benefit and quality of service assessments.

- **Many public investment projects have social and economic benefits that are below their costs, particularly in transportation.** There is scope for greater efficiency by making more use of cost-benefit analysis in the selection of the projects.

- **Agricultural policy is constraining productivity**. Norway's high trade restrictions and subsidies are diverting private and public resources away from more productive sectors and raising the cost of living, particularly for lower-income groups.

- **Greater differentiation in wage formation could facilitate the adjustment towards a new growth model.** Norway has a tradition of labor agreements that result in highly similar wage growth rates across sectors and therefore a reliance on economy-wide wage restraint to maintain competitiveness. However, wage formation may need to allow for greater differentiation in compensation across sectors to better align wage developments with productivity in the private sector, particularly if the transition costs in terms of lower growth and higher unemployment turn our to be greater than anticipated.

Competitiveness and efficiency could also be improved by relaxing the restrictions on working hours and schedules.

27. **More neutrality in the tax system could also help to promote efficiency and growth.** A reduction in the extent to which the personal income tax system promotes housing rather than productive investment would help redeploy new investment toward the exposed industries that will need to replace oil and gas suppliers as an engine of growth. This could include less preferential treatment for both residential and commercial real estate. More generally, a simpler tax system with fewer exemptions and preferences (e.g., equalizing VAT taxes on services and removing exemptions for high-value electric cars) could create fiscal space for a reduction in overall tax rates, including the corporate income tax. Chapter 4 of the Selected Issues Paper explores tax policy reforms for the mainland economy in greater detail.

28. **Further reform to pension and sickness and disability benefits would help labor force participation.** Private sector employment of persons over 62 has risen as a result of the recent pension reform, but incentives for early retirement still remain in the public sector. Staff urged the authorities to complete the pension reform by fully aligning the rules for public sector pensions with the principles used in private sector pensions. Further reform to sickness and disability benefits would likely improve the efficiency and competitiveness of the economy and contribute to growth and employment.

Authorities' views

29. **The authorities strongly agreed on the need for improvements to competitiveness and productivity in the transition away from oil and gas supported demand in the mainland economy.** They noted that reforms in the corporate and personal income tax system, support and protection for agriculture, and the provision of local public services were under review. Some adjustments of labor market regulations were considered, but authorities were more cautious on reductions to the tax preferences for housing.

STAFF APPRAISAL

30. **Norway's near-term outlook remains stable with moderate growth and inflation and low unemployment.**

31. **Monetary policy is appropriate in terms of the authorities' inflation targeting framework**. Tensions among the considerations for monetary policy have abated in the last year. Specifically, the economy roughly at potential output, inflation at about the target, and stabilizing house prices. However, the policy rate will eventually have to normalize to a level somewhat above the inflation target. The exchange rate is broadly in line with fundamentals, although high unit labor costs may become an obstacle to a shift toward a non-oil based growth model.

32. **The government's fiscal policy has been prudent, but it has entailed repeated fiscal stimulus for an economy roughly at capacity.** While the non-oil deficit has been maintained well below 4 percent of GPFG assets, the rapid growth of the GPFG has still allowed a rising non-oil deficit as a share of GDP. The recent policy of keeping the non-oil deficit well below 4 percent of GPFG assets lessens overheating pressures, but a more neutral fiscal stance would be appropriate so long as the economy remains near capacity.

33. **The stronger capital requirements for banks are welcome, in particular the higher capital requirements for mortgage lending.** These increased capital requirements are still in their early stages, and they may need to be adapted in line with experience as implementation proceeds to ensure that they are sufficient. The agreement among Nordic authorities on aligning capital requirements for mortgage lending by branches as well as subsidiaries to Norwegian conditions is commendable. These tighter capital standards and loan-to-value limits on mortgages should be maintained in light of the vulnerabilities stemming from high house prices and household debt even if the housing market softens further. However, implementation challenges remain for this as well as in the broader process of integrating the existing Nordic-Baltic agreements with the Banking Union and European institutions.

34. **The transition to a growth model less reliant on oil and gas-related demand could be eased by structural reforms.** A simpler income tax system and one that is less skewed toward promoting housing rather than productive investment would help productivity and remove disincentives toward investment in those parts of the productive economy that will need to replace oil and gas as a source of growth. Aligning public sector pensions with recent private sector reforms as well as reforms to sickness and disability pensions could increase output through greater labor force participation. There is also scope for efficiency gains in the better provision of public services, the improved use of cost-benefit analysis in the selection of infrastructure projects, removing labor market rigidities, and lower protection and subsidies in agriculture.

35. It is proposed that the next Article IV consultation with Norway be held on the standard 12-month cycle.

Norway: Risk Assessment Matrix[1]

Source of Risks and Relative Likelihood (High, medium, or low)	Expected Impact if Risk is Realized (High, medium, or low)
High **Protracted period of slower growth in advanced and emerging economies:** • **Advanced economies:** Lower-than-anticipated potential growth and persistently low inflation due to a failure to fully address legacies of the financial crisis, leading to secular stagnation. • **Emerging markets:** Maturing of the cycle, misallocation of investment, and incomplete structural reforms leading to prolonged slower growth.	**Medium/High** • Slower growth in advanced economies and emerging markets, particularly China, for an extended time period would affect Norway, through weaker non-oil exports and lower oil prices. • Lower asset prices elsewhere would have negative impacts on the rate of return on GPFG.
Medium **Sustained decline in commodity prices** triggered by deceleration of global demand and coming-on-stream of excess capacity (medium-term).	**High** • A large and prolonged reduction in oil prices would reduce growth through a reduction in oil-related demand for mainland goods and services, and indirectly through a possible reduction in demand for housing due to confidence effects or a reversal of immigrant inflows.
Medium **Significant reduction in house prices:** • Even if house price growth has slowed, the level if historically very high. Therefore, a risk of overvaluation remains. • Household debt continues to stay elevated at around 200 percent of household disposable income.	**High** • A decline in house price in the context of high level of household debt may cause households to cut consumption and residential investment sharply, leading to slower growth and an increase in NPLs in construction, commercial real estate, and retail.
Medium **A more difficult transition to a growth model less dependent on supplying the oil and gas sector:** • Competitiveness challenges from high wage levels compared to trading partners could make it more difficult to shift to a new growth model.	**Medium** • This could result in slower growth and higher unemployment during the transition, particularly if real wage adjustments do not facilitate labor movements between sectors.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability of 30 percent or more). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly.

Authorities' Response to Past IMF Policy Recommendations

Fund Policy Advice from 2013 Consultation	Authorities' Actions
Macroprudential Policy: The Executive Board supported: • increased capital requirements for banks; • tighter macroprudential policies and reduction of the relative tax advantages of housing investments, including tighter limits on loan-to-value ratios and interest-only mortgages; and • greater cross-border coordination on macroprudential measures to ensure that branches of foreign banks lend in line with economic conditions in Norway.	The authorities have made progress in implementing the CRD IV/Basel III requirements well ahead of the required schedule. Tighter capital requirements are in place, including counter-cyclical capital buffers. Higher capital standards for mortgage lending expected to increase the average risk weighting of residential mortgages loans to about 20 percent. There have been no new measures on loan-to-value ratios or interest only mortgages, and tax preferences for real estate are largely unchanged. The Norwegian, Danish, and Swedish authorities agreed that branches of Danish and Swedish banks in Norway would apply similar capital requirements on mortgages.
Fiscal Policy: The Board considered that wage pressures and eroding competitiveness in the non-oil sector argued for a slower rate of spending in 2014 and beyond than 4 percent of GPRG assets.	The 2013 fiscal outturn and 2014 budget are well below 4 percent of GPFG assets (3.1 and 2.8 percent respectively). However, the fiscal impulse was positive in 2013 outturn and it is projected to be 0.7 percent of GDP in 2014.
Structural Reforms to Boost Competitiveness: Directors agreed that structural reforms are needed to enhance the competitiveness of the mainland economy through labor market, pensions, trade in agriculture products, and public sector services. Sickness and disability benefits could be further reformed to improve efficiency and help contain future pressures on government spending.	No changes to sickness and disability benefits in 2013, but some changes will be implemented for disability benefits in 2015. Other policies including state ownership, efficiency of local public services, and agricultural policy are under review, including by the Productivity Commission.

Table 1. Norway: Selected Economic and Social Indicators, 2008-15

Population (2013): 5.1 million
Per capita GDP (2013, USD): $100,318 — Quota (1883.7 mil. SDR/0.79 percent of total)
Main products and exports: Oil, natural gas, fish (primarily salmon) — Literacy: 100 percent

							Projections	
	2008	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**
Real economy (change in percent)								
Real GDP 1/	0.0	-1.4	0.6	1.1	2.8	0.7	1.6	1.9
Real mainland GDP	1.5	-1.4	1.7	2.5	3.3	2.0	1.9	2.4
Domestic demand	1.1	-4.0	3.6	3.2	3.4	3.3	2.1	2.4
Private consumption	2.0	-0.1	3.7	2.6	3.0	2.2	1.8	2.3
Private mainland fixed investment	-2.3	-18.4	-4.1	7.7	5.9	2.9	2.9	4.8
Government consumption	2.4	4.5	1.2	1.1	1.8	1.8	2.1	2.1
Unemployment rate (percent of labor force)	2.6	3.2	3.6	3.3	3.2	3.5	3.7	3.8
Output gap (mainland economy, - implies output below potential)	1.2	-1.1	-1.3	-0.9	0.2	-0.1	-0.3	-0.3
CPI (average)	3.8	2.2	2.4	1.3	0.7	2.1	2.0	2.0
CPI (end of period)	2.1	2.0	2.8	0.2	1.4	2.0	2.0	2.0
Gross national saving (percent of GDP)	40.4	34.0	35.2	37.3	39.2	37.5	37.0	36.8
Gross domestic investment (percent of GDP)	24.5	22.3	23.3	23.8	24.9	26.4	26.8	27.4
Public finance								
Central government (fiscal accounts basis)								
Overall balance (percent of mainland GDP) 2/	21.7	9.8	8.6	13.1	13.4	9.9	7.4	...
Structural non-oil balance (percent of mainland trend GDP) 3/	-3.2	-5.1	-5.1	-4.4	-4.9	-5.1	-5.8	...
in percent of Pension Fund Global capital 4/	-2.9	-4.3	-3.9	-3.0	-3.3	-3.1	-2.8	...
General government (national accounts basis)								
Overall balance (percent of mainland GDP)	25.8	13.4	14.2	18.0	18.5	14.5	14.0	12.3
Net financial assets (percent of mainland GDP)	177.8	202.3	215.9	216.0	228.9	269.4	275.9	276.8
of which: capital of Government Pension Fund Global (GPFG)	122.0	140.6	154.7	159.5	174.1	217.6	226.3	229.6
Money and credit (end of period, 12-month percent change)								
Broad money, M2	3.8	2.4	5.2	6.2	3.8	6.0	...	...
Domestic credit, C2	12.0	2.9	6.1	6.9	5.9	6.8	...	...
Interest rates (year average, in percent)								
Three-month interbank rate	6.2	2.5	2.5	2.9	2.2	1.8	...	...
Ten-year government bond yield	4.5	4.0	3.5	3.1	2.1	2.6	...	...
Balance of payments (percent of mainland GDP)								
Current account balance	21.9	14.9	15.3	17.9	19.0	14.4	13.2	12.0
Balance of goods and services	23.7	15.6	15.3	18.1	17.7	14.0	13.6	11.7
Mainland trade balance of goods	-7.8	-6.5	-6.8	-7.5	-8.0	-8.0	-9.4	-9.1
Offshore trade balance of goods	31.4	21.7	22.0	26.0	26.4	24.8	24.1	21.7
Exports of goods and services (volume change in percent)	0.7	-3.7	0.1	-1.4	1.1	-3.3	1.2	1.3
Imports of goods and services (volume change in percent)	4.1	-12.7	9.3	3.6	2.2	2.7	2.4	2.7
Terms of trade (change in percent)	13.1	-17.3	7.2	9.9	1.2	0.8	...	...
International reserves (end of period, in billions of US dollars)	50.9	48.9	52.8	49.4	51.9	58.5	...	...
Fund position								
Holdings of currency (percent of quota)	88.4	80.6	76.6	71.4	71.1	78.2	...	...
Holdings of SDR (percent of allocation)	169.0	102.4	102.0	97.5	96.1	95.1	...	...
Quota (SDR millions)	1,672	1,672	1,672	1,884	1,884	1,884	...	...
Exchange rates (end of period)								
Exchange rate regime				Floating				
Bilateral rate (NOK/USD), end-of-period	7.0	6.2	5.8	5.7	5.8	5.9	...	...
Nominal effective rate (2005=100)	87.5	99.8	99.9	101.4	105.4	95.3	...	...
Real effective rate (2005=100)	86.4	99.4	99.9	98.9	102.3	93.1	...	...

Sources: Ministry of Finance, Norges Bank, Statistics Norway, International Financial Statistics, United Nations Development Programme 2011, and IMF staff calculations.

1/ Based on market prices which include "taxes on products, including VAT, less subsidies on products".
2/ Projections based on authorities's 2014 budget.
3/ Authorities' key fiscal policy variable; excludes oil-related revenue and expenditure, GPFG income, as well as cyclical effects.
4/ Over-the-cycle deficit target: 4 percent.

Table 2. Norway: Medium-Term Indicators, 2012–19

(Annual percent change, unless otherwise noted)

			Projections					
	2012	2013	2014	2015	2016	2017	2018	2019
Real GDP	2.8	0.7	1.6	1.9	2.0	2.1	2.1	2.1
Real mainland GDP	3.3	2.0	1.9	2.4	2.5	2.6	2.6	2.6
Real Domestic Demand	3.4	3.3	2.1	2.4	2.6	2.6	2.6	2.6
Public consumption	1.8	1.8	2.1	2.1	2.1	2.0	2.0	2.0
Private consumption	3.0	2.2	1.8	2.3	2.7	2.8	2.8	2.8
Gross fixed investment	8.2	8.4	2.9	3.1	3.1	3.1	3.2	3.2
Public	-0.3	10.1	2.5	2.1	2.1	2.1	2.1	2.1
Private mainland	5.9	2.9	2.9	4.8	4.8	4.8	4.8	4.8
Private offshore	16.9	16.5	3.0	1.0	1.0	1.0	1.0	1.0
Final domestic demand	3.9	3.6	2.2	2.5	2.7	2.7	2.7	2.7
Stockbuilding (contribution to growth)	-0.3	-0.2	0.0	0.0	0.0	0.0	0.0	0.0
Trade balance of goods and services (contribution to growth)	-0.2	-2.1	-0.2	-0.3	-0.3	-0.3	-0.3	-0.3
Exports of goods and services	1.1	-3.3	1.2	1.3	1.4	1.4	1.5	1.5
Mainland good exports	1.7	0.3	2.6	2.8	2.8	2.8	2.8	2.8
Offshore good exports	0.0	-7.4	-0.3	-0.3	-0.2	-0.2	-0.2	-0.2
Imports of goods and services	2.2	2.7	2.4	2.7	2.9	2.8	2.8	2.8
Potential GDP	1.7	1.0	1.8	1.9	1.9	1.9	2.1	2.1
Potential mainland GDP	2.2	2.3	2.1	2.4	2.4	2.4	2.6	2.6
Output Gap (percent of potential)	0.2	-0.1	-0.3	-0.3	-0.2	0.0	0.0	0.0
Labor Market								
Employment	1.9	0.7	0.7	0.8	0.9	0.9	1.0	1.0
Unemployment rate LFS (percent)	3.2	3.5	3.7	3.8	3.8	3.8	3.7	3.7
Prices and Wages								
GDP deflator	2.9	2.8	2.5	1.3	1.9	2.2	2.5	2.7
Consumer prices (avg)	0.7	2.1	2.0	2.0	2.2	2.3	2.5	2.5
Consumer prices (eop)	1.4	2.0	2.0	2.0	2.0	2.3	2.5	2.5
Manufacturing wages								
Hourly compensation	4.7	4.0	...	...	...	...	...	...
Productivity	2.4	1.5	...	...	...	...	...	...
Unit labor costs	2.2	2.4	...	...	...	...	...	...
Fiscal Indicators								
General government fiscal balance (percent of GDP)	13.9	11.1	10.8	9.6	8.7	7.8	7.0	6.3
of which: nonoil balance (percent of mainland GDP)	-5.0	-5.4	-5.3	-5.1	-4.9	-4.9	-4.9	-4.9
External Sector								
Current account balance (percent GDP)	14.3	11.1	10.2	9.4	9.4	8.7	8.6	8.2
Balance of goods and services (percent of GDP)	13.3	10.7	10.5	9.2	8.2	7.4	6.9	6.4
Mainland balance of goods 1/	-8.0	-8.0	-9.4	-9.1	-8.8	-8.4	-8.0	-7.7

Source: Statistics Norway, Ministry of Finance, and IMF staff estimates.
1/ Percent of mainland GDP.

Table 3. Norway: External Indicators, 2012-19

	2012	2013	2014	2015	2016	2017	2018	2019
			Projections 1/					
				(Billions of USD)				
Current account balance	71.7	56.8	53.5	51.4	52.5	50.6	52.5	52.3
Balance of goods and services	66.6	55.0	55.2	50.1	45.8	43.4	41.9	41.0
Balance of goods	69.2	59.5	59.5	54.1	49.3	46.1	43.8	42.1
Mainland balance of goods	-30.2	-31.7	-37.9	-38.8	-39.3	-39.7	-40.2	-40.6
Balance of services	-2.5	-4.6	-4.4	-4.0	-3.4	-2.8	-2.0	-1.1
Exports	204.5	199.3	204.0	208.7	212.2	218.6	227.3	237.1
Goods	159.8	153.5	155.9	156.6	156.5	158.8	162.8	167.6
of which oil and natural gas	105.0	97.1	96.9	92.4	88.0	85.3	83.6	82.2
Services	44.7	45.8	48.0	52.2	55.7	59.7	64.5	69.5
Imports	137.9	144.3	148.8	158.6	166.4	175.2	185.5	196.0
Goods	90.6	93.9	96.4	102.4	107.3	112.7	119.0	125.5
Services	47.3	50.4	52.4	56.2	59.1	62.5	66.5	70.6
Balance of factor payments	5.1	1.8	-1.7	1.2	6.6	7.2	10.6	11.2
Capital account balance	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3
Financial account balance	-71.4	-56.5	-53.2	-51.1	-52.2	-50.3	-52.2	-52.0
Net direct investment	-3.1	-14.1	-14.5	-15.0	-15.5	-16.0	-16.8	-17.6
Net portfolio investment	-73.4	-56.6	-24.1	-20.9	-21.3	-18.3	-18.9	-23.7
Net other investment	6.2	17.2	-11.7	-12.2	-12.6	-13.0	-13.6	-7.9
Change in reserves (- implies an increase)	-1.1	-3.0	-2.9	-3.0	-2.9	-2.9	-2.9	-2.9
Net errors and omissions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
				(Percent of Mainland GDP)				
Current account balance	19.0	14.4	13.2	12.0	11.7	10.7	10.5	9.9
Balance of goods and services	17.7	14.0	13.6	11.7	10.2	9.2	8.4	7.7
Balance of goods	18.4	15.1	14.7	12.6	11.0	9.8	8.8	7.9
Mainland balance of goods	-8.0	-8.0	-9.4	-9.1	-8.8	-8.4	-8.0	-7.7
Services balance	-0.7	-1.2	-1.1	-0.9	-0.8	-0.6	-0.4	-0.2
Exports	54.3	50.6	50.4	48.7	47.4	46.3	45.4	44.7
Goods	42.4	39.0	38.5	36.5	34.9	33.7	32.6	31.6
of which oil and natural gas	27.9	24.7	23.9	21.6	19.6	18.1	16.7	15.5
Services	11.9	11.6	11.9	12.2	12.4	12.7	12.9	13.1
Imports	36.6	36.6	36.8	37.0	37.1	37.2	37.1	37.0
Goods	24.1	23.8	23.8	23.9	23.9	23.9	23.8	23.7
Services	12.6	12.8	13.0	13.1	13.2	13.3	13.3	13.3
Balance of factor payments	1.4	0.5	-0.4	0.3	1.5	1.5	2.1	2.1
Capital account balance	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	0.0
Financial account balance	-19.0	-14.3	-13.2	-11.9	-11.7	-10.7	-10.4	-9.8
Change in reserves (- implies an increase)	-0.3	-0.8	-0.7	-0.7	-0.7	-0.6	-0.6	-0.5
Net errors and omissions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
				(Percent of GDP)				
Stock of net foreign assets (IIP)	99.5	...	...	...	...	...	...	...
Direct investment, net	4.7	...	...	...	...	...	...	...
Portolio investment, net	95.8	...	...	...	...	...	...	...
Other investment, net	-11.6	...	...	...	...	...	...	...
Official reserves, assets	10.6	...	...	...	...	...	...	...
Government Pension Fund Global, percent of mainland GDP 2/	174.6	217.5	226.3	...	...	...	...	...

Sources: Statistics Norway; Ministry of Finance; and IMF staff estimates.
1/ IMF staff projections as of March 2014.
2/ Projections from the 2014 National Budget.

Table 4. Norway: Key Fiscal Indicators, 2007-14

(Percent of mainland GDP, unless otherwise indicated)

	2007	2008	2009	2010	2011	2012	Projections 2013	2014
Central Government 1/								
Revenue	58.6	63.5	56.1	53.6	59.0	58.9	55.8	54.0
Oil revenue	19.2	23.5	16.2	14.9	17.9	19.2	16.4	15.1
Non-oil revenue	39.4	40.0	39.8	38.7	41.0	39.7	39.5	38.9
Expenditure	40.7	41.8	46.3	44.9	45.9	45.5	45.9	46.5
Oil Expenditures	1.2	1.2	1.3	1.0	1.0	1.2	1.5	1.6
Non-oil expenditures	39.5	40.6	45.0	43.9	44.8	44.3	44.5	45.0
Balance	17.9	21.7	9.8	8.6	13.1	13.4	9.9	7.4
Non-oil balance	-0.1	-0.6	-5.1	-5.2	-3.8	-4.6	-5.0	-6.0
Structural nonoil balance 2/	-2.8	-3.1	-5.2	-5.2	-4.5	-4.9	-5.1	-5.8
In percent of Pension Fund Global capital 3/	-2.8	-2.9	-4.3	-3.9	-3.0	-3.3	-3.1	-2.8
In percent of trend mainland GDP 4/	-2.9	-3.3	-5.2	-5.2	-4.4	-4.9	-5.1	-5.8
Fiscal impulse 5/	-0.1	0.3	1.9	0.0	-0.8	0.5	0.2	0.7
General Government 6/								
Revenue	75.5	80.3	71.7	71.7	75.9	75.5	71.9	71.3
Oil revenue	22.6	28.3	19.0	19.4	22.8	23.4	19.9	19.3
Non-oil revenue	52.9	52.0	52.7	52.3	53.1	52.1	52.1	52.0
Expenditure	52.8	54.5	58.3	57.5	57.9	57.1	57.5	57.3
Oil expenditures 7/	0.1	0.1	0.1	0.1	0.0	0.0	0.0	0.0
Non-oil expenditures	52.7	54.4	58.3	57.4	57.9	57.1	57.5	57.3
Balance	22.7	25.8	13.4	14.2	18.0	18.5	14.5	14.0
Non-oil balance	0.2	-2.4	-5.6	-5.1	-4.8	-5.0	-5.4	-5.3

Sources: Statistics Norway, Ministry of Finance and IMF staff estimates.

1/ Budget definition; excludes Pension Fund Global. Projections are based on the 2014 budget.

2/ Estimated by the Ministry of Finance.

3/ Key policy indicator under Norway's fiscal guidelines, which set an over-the-cycle target for the structural nonoil deficit of 4 percent.

4/ Trend output is based on the estimates by the Ministry of Finance.

5/ Annual change in the structural balance as a percentage of trend mainland GDP

6/ National accounts definition. In addition to central government, includes also Government Pension Fund, other social security and central government accounts, state enterprises, and local government.

7/ Differently from the budget definition, investments in State Direct Financial Interest are considered as net lending, and not as expenditures.

Table 5. Norway: General Government Accounts, 2007-2012
(Percent of mainland GDP)

	2007	2008	2009	2010	2011	2012
Revenue	75.5	80.3	71.7	71.6	75.9	75.5
Taxes	44.6	45.7	40.8	42.2	44.1	43.3
Social contributions	11.8	12.2	12.5	12.3	12.6	12.7
Other	19.1	22.4	18.4	17.2	19.2	42.5
Expense	51.2	52.8	56.5	56.1	56.4	56.0
Compensation of employees	16.1	16.6	17.6	17.5	17.8	17.9
Use of goods and services	7.5	7.6	8.4	8.2	8.0	7.9
Consumption of fixed capital	2.4	2.5	2.6	2.6	2.7	2.7
Interest	1.7	2.0	1.8	1.6	1.5	1.2
Subsidies	2.3	2.4	2.6	2.6	2.6	2.5
Grants	1.3	1.3	1.5	1.6	1.5	1.3
Social benefits	18.4	18.6	20.2	20.2	20.5	20.5
Other	1.6	1.7	1.8	1.8	1.8	1.9
Gross operating balance	26.7	30.0	17.8	18.2	22.2	22.3
Net operating balance	24.3	27.5	15.2	15.6	19.5	19.5
Net acquisition of nonfinancial assets	1.6	1.7	1.8	1.4	1.4	1.2
			Net financing			
Net lending/borrowing	22.7	25.8	13.4	14.2	18.1	18.0
Net acquisition of financial assets	27.2	14.7	4.7	18.4	2.2	21.4
Currency and deposits	0.0	-0.9	-0.8	0.5	-2.4	2.9
Securities other than shares	3.3	10.8	-17.8	9.0	0.7	7.2
Loans	8.0	-27.6	5.7	3.3	-10.0	1.4
Shares and other equity	14.7	30.0	18.2	4.4	12.1	10.7
Insurance technical reserves	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts receivable	1.2	2.4	-0.6	1.2	1.9	-0.8
Monetary gold and SDRs	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	4.8	-11.7	-8.3	4.1	-15.9	3.4
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0
Securities other than shares	-0.8	3.7	11.1	1.1	-3.9	2.6
Loans	3.8	-15.1	-19.4	2.3	-11.0	0.7
Shares and other equity	0.0	0.0	0.0	0.0	0.0	0.0
Insurance technical reserves	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts receivable	1.8	-0.2	0.0	0.6	-1.0	0.2
			Balance sheet			
Net financial worth	182.2	169.9	196.5	209.5	211.2	221.2
Financial assets	256.5	245.7	258.7	272.5	255.9	267.3
Currency and deposits	13.3	12.1	11.1	11.0	8.1	10.6
Securities other than shares	67.0	90.0	62.7	67.5	68.3	70.1
Loans	53.7	32.6	37.5	38.6	27.1	27.5
Shares and other equity	106.6	95.8	133.3	140.7	136.8	146.2
Insurance technical reserves	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts receivable	16.0	15.3	14.2	14.6	15.6	12.9
Monetary gold and SDRs	0.0	0.0	0.0	0.0	0.0	0.0
Financial liabilites	74.3	75.8	62.2	62.9	44.6	46.1
Currency and deposits	0.0	0.0	0.0	0.0	0.0	0.0
Securities other than shares	13.4	16.8	27.5	27.3	22.6	23.7
Loans	52.9	50.0	27.4	28.1	15.9	16.0
Shares and other equity	0.0	0.0	0.0	0.0	0.0	0.0
Insurance technical reserves	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts receivable	8.0	9.0	7.3	7.5	6.2	6.3

Source: IMF *Government Finance Statistics.*

Table 6. Norway: Financial System Structure, 2007-12
(Percent of assets, unless otherwise noted)

	2007	2008	2009	2010	2011	2012	2013
Assets of all financial institutions (billions of NOK)	5,004	6,112	5,201	6,424	7,042	7,351	7,746
Share of assets owned by							
Banks	62.4	62.5	71.1	56.7	56.1	55.1	55.1
Mortgage companies	12.4	16.4	21.6	21.5	22.9	23.3	22.6
Finance companies	2.8	2.5	2.8	1.7	1.7	1.7	1.7
State lending institutions	4.2	3.7	4.5	3.8	3.7	3.7	3.8
Life insurance companies	14.9	12.1	15.2	13.4	12.9	13.5	14.1
Non-life insurance companies	3.3	2.9	3.5	2.9	2.7	2.7	2.8
Balance sheet structure							
Banks excluding foreign subsidiaries							
Assets							
Cash and deposits	8.0	11.6	9.9	8.5	14.2	13.7	10.9
Securities (current assets)	10.8	11.6	19.3	19.7	17.8	19.0	18.7
Lending to households, municip. and non-finan. firms	68.6	59.5	53.7	53.7	50.3	48.5	47.8
Other lending	9.8	11.3	10.0	10.7	10.5	11.8	14.9
Loan loss provisions	-0.3	-0.3	-0.4	-0.5	-0.4	-0.4	-0.4
Fixed assets and other assets	3.0	6.4	7.5	7.8	7.7	7.3	8.1
Equity and liabilities							
Customer deposits	43.2	43.4	43.1	46.6	45.7	46.8	47.4
Deposits/loans from domestic credit institutions	4.7	2.9	3.1	3.0	2.6	1.9	1.3
Deposits/loans from foreign credit institutions	11.0	12.9	15.2	12.2	17.1	16.7	17.2
Deposits/loans from Norges Bank	1.2	1.8	1.6	1.3	0.7	0.2	0.0
Other deposits/loans	2.9	1.2	6.3	6.1	3.8	2.9	1.9
Notes and short-term paper debt	5.1	5.4	3.1	3.4	3.9	4.6	3.4
Bond debt	18.3	19.0	15.5	14.7	12.7	13.2	12.4
Other liabilities	5.3	5.5	3.9	3.9	4.9	4.8	7.0
Subordinated loan capital	2.2	2.5	2.3	2.2	1.7	1.5	1.8
Equity	6.0	5.4	5.9	6.7	6.8	7.3	7.5
Covered bond companies							
Assets							
Cash and deposits	3.7	3.6	3.2	1.6	1.5	2.3	2.0
Securities (current assets)	1.4	8.4	2.4	3.2	4.3	5.1	5.7
Gross lending	94.7	87.5	93.6	94.7	93.6	92.1	91.8
Loan loss provisions	0.0	0.0	0.0	0.0	0.0	0.1	0.1
Fixed assets and other assets	0.3	0.5	0.7	0.4	0.5	0.5	0.5
Equity and liabilities							
Notes and short-term paper debt	2.6	0.2	0.1	0.1	0.5	0.5	0.3
Bond debt	44.7	59.0	66.6	70.0	73.3	70.0	73.4
Loans	46.2	37.0	27.1	22.2	19.0	21.1	18.9
Other liabilities	1.6	0.1	1.1	2.7	2.4	3.4	1.7
Subordinated loan capital	1.0	0.7	0.6	0.5	0.4	0.3	0.6
Equity	4.0	2.9	4.5	4.5	4.4	4.7	5.1

Sources: Norges Bank and Statistics Norway.

Appendix I. Debt Sustainability Analysis

Norway Public Sector Debt Sustainability Analysis (DSA) - Baseline Scenario

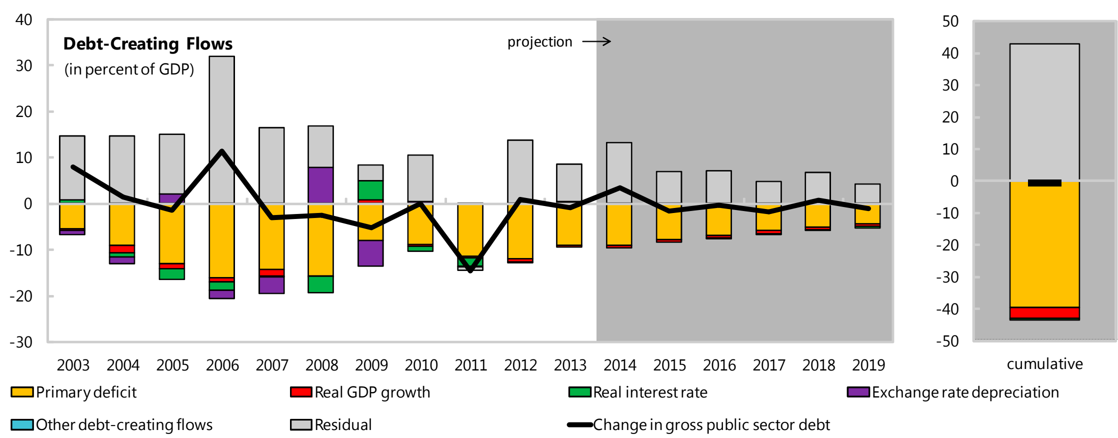
(in percent of GDP unless otherwise indicated)

Debt, Economic and Market Indicators [1/]

	Actual			Projections						As of March 10, 2014		
	2003-2011 [2/]	2012	2013	2014	2015	2016	2017	2018	2019	Sovereign Spreads		
Nominal gross public debt	44.0	29.3	28.4	31.9	30.3	29.9	28.1	28.9	27.9	EMBIG (bp) 3/		133
Public gross financing needs	-8.4	-12.9	-9.8	-9.9	-3.9	-4.3	-1.9	-3.6	-0.9	5Y CDS (bp)		180
Real GDP growth (in percent)	1.4	2.8	0.8	1.8	1.9	2.0	2.0	2.1	2.1	Ratings	Foreign	Local
Inflation (GDP deflator, in percent)	5.3	2.9	2.5	3.0	1.2	1.7	2.2	2.5	2.7	Moody's	Aaa	Aaa
Nominal GDP growth (in percent)	6.9	5.7	3.3	4.9	3.1	3.7	4.2	4.7	4.8	S&Ps	AAA	AAA
Effective interest rate (in percent) [4/]	3.4	3.4	3.1	3.2	1.4	1.7	1.8	1.6	1.8	Fitch	AAA	AAA

Contribution to Changes in Public Debt

	Actual			Projections							
	2003-2011	2012	2013	2014	2015	2016	2017	2018	2019	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	-0.7	0.9	-0.9	3.5	-1.6	-0.4	-1.8	0.8	-1.0	-0.5	
Identified debt-creating flows	-13.1	-12.8	-9.0	-9.7	-8.4	-7.5	-6.6	-6.0	-5.3	-43.5	
Primary deficit	-11.4	-12.0	-9.2	-9.2	-7.9	-6.9	-5.9	-5.1	-4.4	-39.5	-0.8
Primary (noninterest) revenue and gra	53.2	54.1	52.3	52.2	51.7	51.3	51.1	50.9	50.8	307.9	
Primary (noninterest) expenditure	41.8	42.1	43.1	43.0	43.7	44.4	45.1	45.8	46.4	268.4	
Automatic debt dynamics [5/]	-1.7	-0.8	0.2	-0.5	-0.5	-0.6	-0.7	-0.8	-0.8	-3.9	
Interest rate/growth differential [6/]	-1.3	-0.6	0.0	-0.5	-0.5	-0.6	-0.7	-0.8	-0.8	-3.9	
Of which: real interest rate	-0.8	0.1	0.2	0.0	0.0	0.0	-0.1	-0.3	-0.3	-0.6	
Of which: real GDP growth	-0.6	-0.8	-0.2	-0.5	-0.6	-0.6	-0.6	-0.6	-0.6	-3.4	
Exchange rate depreciation [7/]	-0.3	-0.1	0.2	...	...	...	...	...	...	...	
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
General government net privatizatio	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Please specify (2) (e.g., ESM and Euro	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8/]	12.4	13.7	8.1	13.1	6.9	7.1	4.8	6.8	4.3	43.0	



Source: IMF staff.

1/ Public sector is defined as general government.

2/ Based on available data.

3/ Long-term bond spread over German bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

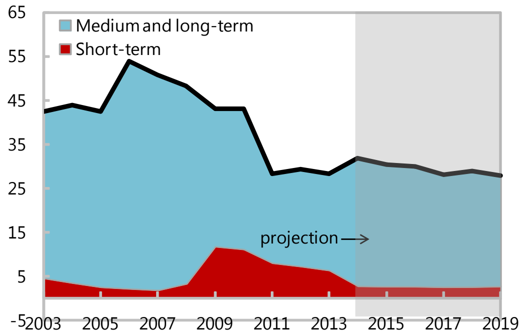
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Norway Public DSA - Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

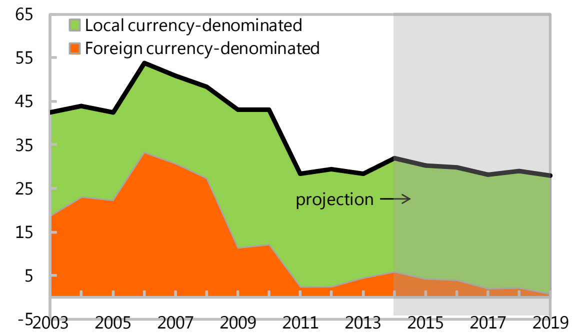
By Maturity

(in percent of GDP)



By Currency

(in percent of GDP)

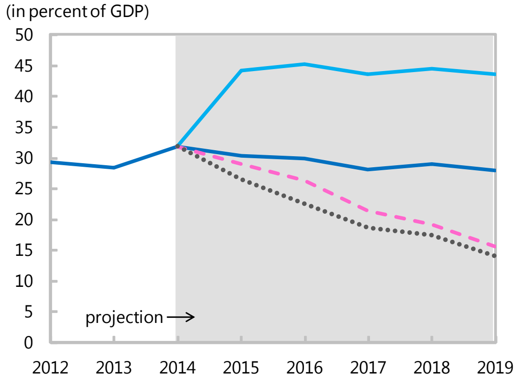


Alternative Scenarios

Baseline
Contingent Liability Shock
Historical
Constant Primary Balance

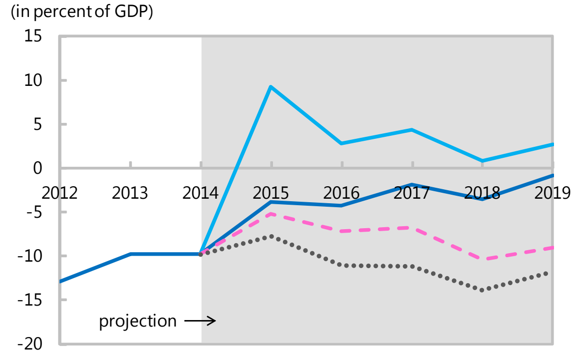
Gross Nominal Public Debt

(in percent of GDP)



Public Gross Financing Needs

(in percent of GDP)



Underlying Assumptions

(in percent)

Baseline Scenario	2014	2015	2016	2017	2018	2019
Real GDP growth	1.8	1.9	2.0	2.0	2.1	2.1
Inflation	3.0	1.2	1.7	2.2	2.5	2.7
Primary Balance	9.2	7.9	6.9	5.9	5.1	4.4
Effective interest rate	3.2	1.4	1.7	1.8	1.6	1.8
Constant Primary Balance Scenario						
Real GDP growth	1.8	1.9	2.0	2.0	2.1	2.1
Inflation	3.0	1.2	1.7	2.2	2.5	2.7
Primary Balance	9.2	9.2	9.2	9.2	9.2	9.2
Effective interest rate	3.2	1.4	1.7	1.8	1.4	1.5

Historical Scenario	2014	2015	2016	2017	2018	2019
Real GDP growth	1.8	1.5	1.5	1.5	1.5	1.5
Inflation	3.0	1.2	1.7	2.2	2.5	2.7
Primary Balance	9.2	11.8	11.8	11.8	11.8	11.8
Effective interest rate	3.2	1.4	1.6	1.7	1.2	1.3
Contingent Liability Shock						
Real GDP growth	1.8	0.3	0.4	2.0	2.1	2.1
Inflation	3.0	0.8	1.3	2.2	2.5	2.7
Primary Balance	9.2	-5.1	6.9	5.9	5.1	4.4
Effective interest rate	3.2	1.6	2.8	2.7	2.4	2.5

Source: IMF staff.

INTERNATIONAL MONETARY FUND

NORWAY

STAFF REPORT FOR THE 2014 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

July 23, 2014

Prepared By

European Department
(In consultation with other departments)

CONTENTS

FUND RELATIONS

(As of May 31, 2014)

Membership Status

Joined: December 27, 1945; Article VIII

General Resources Account SDR Percent Million Quota

	SDR Millions	Percent Quota
Quota	1,883.70	100.00
Fund holdings of currency	1,515.80	80.47
Reserves tranche position	367.92	19.53
Lending to the Fund		
New Arrangements to Borrow	511.09	

SDR Department	**SDR Millions**	**Percent Allocation**
Net cumulative allocations	1,563.07	100.00
Holdings	1486.09	95.08

Outstanding Purchases and Loans

None

Latest Financial Arrangements

None

Projected Payments to the Fund

(SDR Million; based on existing use of resources and present holdings of SDRs)

	Forthcoming				
	2014	2015	2016	2017	2018
Principal					
Charges/Interest	0.04	0.09	0.09	0.09	0.09
Total	0.04	0.09	0.09	0.09	0.09

Implementation of HIPC Initiative

Not applicable

Implementation of Multilateral Debt Relief Initiative

Not applicable

Implementation of Post-Catastrophe Debt Relief

Not applicable

Exchange Arrangements

The de jure and de facto exchange rate arrangements in Norway are classified as freely floating. The exchange system is free of restrictions on the making of payments and transfers for current international transactions other than restrictions notified to the Fund in accordance with Decision No. 144-(52/51).

Article IV Consultation

Norway is on the 12-month consultation cycle.

FSAP Participation

A review under the Financial Sector Assessment Program (FSAP) was completed in 2005.

Technical Assistance

None

Resident Representative

None

STATISTICAL ISSUES

Norway—STATISTICAL ISSUES APPENDIX (As of June 6, 2014)	
I. Assessment of Data Adequacy for Surveillance	
General: Data provision is adequate for surveillance.	
National Accounts: Breakdowns for oil-related parts of the mainland economy and other traditional sectors would be useful, in light of growing needs to better understand the impact of oil and gas activity on the mainland economy. Work is under way in this area, and the authorities are looking into this issue.	
II. Data Standards and Quality	
Subscriber to the Fund's Special Data Dissemination Standard (SDDS) since 1996. Uses SDDS flexibility options on the timeliness of the general government operations and central government debt. SDSS metadata are posted on the Dissemination Standard Bulletin Board (DSBB).	Data ROSC completed in 2003 is publicly available.

Norway: Table of Common Indicators Required for Surveillance
(As of June 6, 2014)

	Date of latest observation (For all dates in table, please use format dd/mm/yy)	Date received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of Publication[7]	Memo Items:[8]	
						Data Quality – Methodological soundness[9]	Data Quality – Accuracy and reliability[10]
Exchange Rates	June 2014	June 2014	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	May 2014	May 2014	M	M	M		
Reserve/Base Money	April 2014	April 2014	M	M	M	O, O,O, LO	O, O, O, O, O
Broad Money	April 2014	April 2014	M	M	M		
Central Bank Balance Sheet	April 2014	May 2014	M	M	M		
Consolidated Balance Sheet of the Banking System	30/09/11	07/11/11	M	M	M		
Interest Rates[2]	June 2014	June 2014	Q	Q	Q		
Consumer Price Index	April 2014	April 2014	M	M	M	O, O, O, O	O, O, O, O, O
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	Apr. 2014	May 2014	A	A	A	LO, LNO, O, O	LO, O, O, O, LO
Revenue, Expenditure, Balance and Composition of Financing[3] – Central Government	Apr. 2014	May 2014	M	M	M		
Stocks of Central Government and Central Government-Guaranteed Debt[5]	Q1 2014	2013	A	A	A		
External Current Account Balance	Q1 2014	May 2014	Q	Q	Q	O, O, O, O	LO, O, O, O, LO
Exports and Imports of Goods and Services	Q1 2014	May 2014	Q	Q	Q		
GDP/GNP	Q1 2014	May 2014	Q	Q	Q	O, O, O, O	O, O, O, O, LO
Gross External Debt	Q4 2014	2014	Q	Q	Q		
International Investment Position[6]	2012	2012	A	A	A		

[1] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

[3] Foreign, domestic bank, and domestic nonbank financing.

[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

[5] Including currency and maturity composition.

[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

[7] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).

[8] These columns should only be included for countries for which Data ROSC (or a Substantive Update) has been published.

[9] This reflects the assessment provided in the data ROSC or the Substantive Update (published on ..., and based on the findings of the mission that took place during...) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O); largely observed (LO); largely not observed (LNO); not observed (NO); and not available (NA).

[10] Same as footnote 7, except referring to international standards concerning (respectively) source data, assessment of source data, statistical techniques, assessment and validation of intermediate data and statistical outputs, and revision studies.

INTERNATIONAL MONETARY FUND

COMMUNICATIONS DEPARTMENT

Press Release No.14/406
FOR IMMEDIATE RELEASE
August 29, 2014

International Monetary Fund
700 19th Street, NW
Washington, D.C. 20431 USA

IMF Executive Board Concludes 2014 Article IV Consultation with Norway

On August 28, 2014 the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Norway.[1]

The Norwegian economy slowed in 2013 with both mainland (i.e. non-oil) and offshore growth below the 2012 pace. Mainland growth moderated to 2.1 percent in part due to weak private consumption and mainland investment, while lower oil production kept offshore growth down. The unemployment remains low, at around 3.5 percent, in spite of a growing labor force due to immigration. House prices stabilized in mid-2013 although at high levels and the housing market shows signs of cooling. Inflation rose to about the inflation target, 2.5 percent, partly due to last year's exchange rate depreciation. The structural non-oil deficit was 3.1 percent of Government Pension Fund Global (GPFG) assets and 5.1 percent of trend mainland GDP. This is below the deficit permitted under the authorities' fiscal policy rule, but it still implies a positive fiscal impulse due to the strong growth in GPFG assets. The overall current account surplus remains high at 14 percent of mainland GDP but declined in 2013 partly due to weaker petroleum exports.

Banks' profitability has improved and capital ratios have strengthened. Banks continue to rely on wholesale funding, mostly in the form of covered bonds, and many banks still have some way to go before meeting the Liquidity Coverage Ratio (LCR) requirement. Norway's financial system is part of a tightly integrated Nordic-Baltic system. Inward links are mainly from Swedish and Danish banks with a combined market share of a quarter to a third. Outward links are relatively modest and concentrated in Nordic and Baltic countries and the shipping industry.

The near-term outlook remains stable with moderate growth and inflation. However, the medium and longer term present new challenges and uncertainties, particularly because of

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summing up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

expected slowdown in oil and gas investment. Steadily increasing oil and gas investment over the last decade culminated in a 17 percent growth rate in 2013. With this investment expected to flatten out in 2014-15 before beginning a slow decline, new sources of growth are needed. Staff's central forecast is a continuation of growth with only a modest rise in unemployment in the next few years and inflation gradually rising back toward the target. However, this is based on a scenario in which the sources of growth shift away from supplying the oil and gas sector and toward other sectors of the economy or exports of oil-related goods and services.

There are risks to this scenario. A substantial decline in oil and gas prices could undercut growth through a reduction in demand for mainland goods and services, and through a reduction in private demand due to confidence and income effects. A significant reduction in housing process would likely reduce household consumption with adverse consequences for retail trade, construction, and commercial real estate and lenders to those sectors. Also, a more difficult transition to a growth model less dependent on supplying the oil and gas sector could result in slower growth and higher unemployment during the shift.

Executive Board Assessment[2]

Executive Directors commended Norway's continued steady economic growth, moderate inflation, low unemployment, and large current account and fiscal surpluses. Nevertheless, challenges remain. Directors agreed that policy priorities and structural reforms should be geared towards preserving financial stability, supporting the transition to an economy less dependent on oil and gas, and improving productivity and competitiveness.

Directors concurred that the current stance of monetary policy, under the authorities' inflation-targeting framework, is appropriate. Given that the economy is roughly at its potential, inflation is close to target, and house prices are stabilizing, the argument for a rate increase has diminished for now. Directors noted that the policy rate might eventually have to normalize to a level above the inflation target to meet the objectives of monetary policy, and to mitigate risks of overheating, particularly, in the real estate market.

Directors welcomed the authorities' prudent fiscal policy, in particular the decision to keep the spending of oil revenues well below 4 percent specified under the fiscal rule. While acknowledging the availability of resources for additional investments, most Directors saw merit in a more neutral fiscal policy stance as long as the economy remains near capacity. Directors welcomed the stronger capital requirements for banks ahead of the Basel III deadlines, in particular the higher capital requirements for mortgage lending. Given that these

[2] At the conclusion of the discussion, the Managing Director, as a Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summing up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

requirements are still in their early stages, they may need to be adapted as implementation proceeds. Directors commended the agreement among Nordic authorities on aligning capital requirements for mortgage lending by branches and subsidiaries to local economic conditions. They agreed that tighter capital standards and loan-to-value limits on mortgages should be maintained given the vulnerabilities stemming from high house prices and household debt and banks' reliance on wholesale funding, even if the housing market softens further.

Directors emphasized the importance of further structural reforms to improve productivity and competitiveness, and to promote the non-oil economy, and they looked forward to the report of the Productivity Commission. Priorities include further reforms of the labor market, pensions and public services, greater wage differentiation across sectors, and reducing protection and subsidies in agriculture. Directors also recommended increased use of cost-benefit analysis in the selection of infrastructure projects, and a simpler income tax system with fewer incentives for promoting housing to encourage productive investment.

Norway: Selected Economic and Social Indicators, 2008–15

Population (2013): 5.1 million
Per capita GDP (2013, USD): $100,318 — Quota (1883.7 mil. SDR/0.79 percent of total)
Main products and exports: Oil, natural gas, fish (primarily salmon) — Literacy: 100 percent

							Projections	
	2008	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**
Real economy (change in percent)								
Real GDP 1/	0.0	-1.4	0.6	1.1	2.8	0.7	1.6	1.9
Real mainland GDP	1.5	-1.4	1.7	2.5	3.3	2.0	1.9	2.4
Domestic demand	1.1	-4.0	3.6	3.2	3.4	3.3	2.1	2.4
Private consumption	2.0	-0.1	3.7	2.6	3.0	2.2	1.8	2.3
Private mainland fixed investment	-2.3	-18.4	-4.1	7.7	5.9	2.9	2.9	4.8
Government consumption	2.4	4.5	1.2	1.1	1.8	1.8	2.1	2.1
Unemployment rate (percent of labor force)	2.6	3.2	3.6	3.3	3.2	3.5	3.7	3.8
Output gap (mainland economy, - implies output below potential)	1.2	-1.1	-1.3	-0.9	0.2	-0.1	-0.3	-0.3
CPI (average)	3.8	2.2	2.4	1.3	0.7	2.1	2.0	2.0
CPI (end of period)	2.1	2.0	2.8	0.2	1.4	2.0	2.0	2.0
Gross national saving (percent of GDP)	40.4	34.0	35.2	37.3	39.2	37.5	37.3	37.5
Gross domestic investment (percent of GDP)	24.5	22.3	23.3	23.8	24.9	26.4	26.6	27.2
Public finance								
Central government (fiscal accounts basis)								
Overall balance (percent of mainland GDP) 2/	21.7	9.8	8.6	13.1	13.4	9.9	7.4	...
Structural non-oil balance (percent of mainland trend GDP) 3/	-3.2	-5.1	-5.1	-4.4	-4.9	-5.1	-5.8	...
in percent of Pension Fund Global capital 4/	-2.9	-4.3	-3.9	-3.0	-3.3	-3.1	-2.8	...
General government (national accounts basis)								
Overall balance (percent of mainland GDP)	25.8	13.4	14.2	18.0	18.5	14.1	14.3	12.9
Net financial assets (percent of mainland GDP)	177.8	202.3	215.9	216.0	228.9	269.4	275.8	277.5
of which: capital of Government Pension Fund Global (GPFG)	122.0	140.6	154.7	159.5	174.1	217.6	226.3	230.4
Money and credit (end of period, 12-month percent change)								
Broad money, M2	3.8	2.4	5.2	6.2	3.8	6.0	...	...
Domestic credit, C2	12.0	2.9	6.1	6.9	5.9	6.8	...	...
Interest rates (year average, in percent)								
Three-month interbank rate	6.2	2.5	2.5	2.9	2.2	1.8	...	...
Ten-year government bond yield	4.5	4.0	3.5	3.1	2.1	2.6	...	...
Balance of payments (percent of mainland GDP)								
Current account balance	21.9	14.9	15.3	17.9	19.0	14.4	14.0	13.3
Balance of goods and services	23.7	15.6	15.3	18.1	17.7	14.0	14.4	12.9
Mainland trade balance of goods	-7.8	-6.5	-6.8	-7.5	-8.0	-8.0	-9.4	-9.1
Offshore trade balance of goods	31.4	21.7	22.0	26.0	26.4	24.8	24.9	22.9
Exports of goods and services (volume change in percent)	0.7	-3.7	0.1	-1.4	1.1	-3.3	1.2	1.3
Imports of goods and services (volume change in percent)	4.1	-12.7	9.3	3.6	2.2	2.7	2.4	2.7
Terms of trade (change in percent)	13.1	-17.3	7.2	9.9	1.2	0.8	...	...
International reserves (end of period, in billions of US dollars)	50.9	48.9	52.8	49.4	51.9	58.3	...	...
Fund position								
Holdings of currency (percent of quota)	88.4	80.6	76.6	71.4	71.1	78.2	...	...
Holdings of SDR (percent of allocation)	169.0	102.4	102.0	97.5	96.1	95.1	...	...
Quota (SDR millions)	1,672	1,672	1,672	1,884	1,884	1,884	...	...
Exchange rates (end of period)								
Exchange rate regime				Floating				
Bilateral rate (NOK/USD), end-of-period	7.0	6.2	5.8	5.7	5.8	6.0	...	...
Nominal effective rate (2005=100)	87.5	99.8	99.9	101.4	105.4	95.3	...	...
Real effective rate (2005=100)	86.4	99.4	99.9	98.9	102.4	93.2	...	...

Sources: Ministry of Finance, Norges Bank, Statistics Norway, International Financial Statistics, United Nations Development Programme 2011, and IMF staff calculations.

1/ Based on market prices which include "taxes on products, including VAT, less subsidies on products".

2/ Projections based on authorities's 2014 budget.

3/ Authorities' key fiscal policy variable; excludes oil-related revenue and expenditure, GPFG income, as well as cyclical effects.

4/ Over-the-cycle deficit target: 4 percent.

Statement by Audun Groenn, Executive Director for Norway
August 28, 2014

On behalf of my Norwegian authorities, I would like to thank staff for a very well-written report on the Norwegian economy. My authorities broadly agree with staff's findings and analysis in the report, and welcome the recommendations.

Economic Developments and Main Challenges

The analysis of current economic conditions and the forecasts in the staff report are broadly in line with those of my authorities. The status of the Norwegian economy is favorable and the prospects for a balanced development in the medium term are good. However, my authorities recognize that the economy faces some challenges, and the outlook is subject to some key risks. These risks are clearly stated in the risk matrix on page 26.

Since the year 2000, the Norwegian economy has experienced significant terms of trade gains. The oil price has increased substantially, whereas prices on imports have been more stable. The high oil price has spurred a rapid increase in oil and gas investments, providing persistent demand stimulus to the Mainland economy. High income growth and low real interest rates have supported growth in household demand.

In 2013, Mainland GDP growth slowed to a level below its historical average. Despite the slowdown there are signs that the economy is operating close to full capacity. The unemployment rate has been fairly stable at a level well below the average for the last 25 years. Moreover, almost all of the net employment growth over the past five years can be accounted for by net immigration.

Looking ahead, the Norwegian economy faces some challenges. As pointed out in the staff report, demand from the petroleum sector will commence on a downward trajectory in the coming years. This implies that an important growth engine for the Norwegian economy will lose its speed, and eventually be set in reverse. The latest investment survey indicates a decline in petroleum investments already next year. Even if investment may increase somewhat again over the next years, Norwegian businesses must adapt to the new situation in order to maintain growth. High unit labor costs in Norway may make this transition even harder, especially in a situation where productivity growth has slowed down compared with historical trends.

Another challenge facing the Norwegian economy is the high house prices and the high debt level among households. This makes some households vulnerable to shocks, and poses a risk to financial stability. As pointed out by the staff report, a fall in the oil price or other shocks to demand or confidence could lead to significant reduction in house prices, which would amplify the negative impact on the Mainland economy. Solid banks and prudent lending practices are crucial elements for maintaining financial stability.

Monetary policy

My authorities generally concur with staff's assessment of monetary policy.
In the baseline outlook of Norges Bank's June 2014 Monetary Policy Report, inflation is expected to be somewhat below, but close to, 2.5 percent throughout the projection period to 2017. Capacity utilization may edge down in the coming year, but is expected to increase towards a normal level at the end of the projection period. Both the objective of keeping inflation close to target and the objective of sustaining capacity utilization in the years ahead could, ceteris paribus, imply a somewhat lower key policy rate. A lower key policy rate today may on the other hand increase the risk that financial imbalances build up again. Norges Bank's overall assessment in June was that the key policy rate should remain at today's level for a period ahead.

Fiscal policy

Norway's fiscal framework, including the Government Pension Fund Global, is designed to support a stable development of the economy in both the short and medium term. In addition, it makes sure that the petroleum wealth also benefits future generations. The public revenues from petroleum are large, volatile and temporary. A key feature of the framework is that it delinks the earning of petroleum revenues from its use. This reduces the costs of future structural changes and the risk of a sharp decline in industries exposed to international competition.

On the *earning* side, Norway's oil tax system and the state's direct ownership in the oil production are set up to capture the resource rents from the industry, to make sure they benefit the entire Norwegian population. The government's net cash flow from the petroleum industry is transferred to the Government Pension Fund Global. This Fund is invested abroad. This insulates the government budget from volatility in petroleum revenues, and helps protect the krone against fluctuations in export income.

On the *utilisation* side, Norway has a fiscal rule for gradually phasing oil and gas income into the fiscal budget. The fiscal rule was adopted in 2001 and received broad political support. The design of the rule reflected that the issue was not *whether* more petroleum revenues should be used in public budgets, but rather *when* and *how quickly* this should happen.

The fiscal rule specifies that the expected real return of the Fund, estimated at 4 percent, over time shall be transferred to the central government's budget. The rule is also intended to even out economic fluctuations and support low unemployment. The spending of petroleum revenues in a particular year must therefore be adjusted to the macroeconomic situation.

In a period with steep growth in the Fund's capital, as is presently the case, to spend oil revenues in line with the expected return on the Fund (the four-percent path) would have provided the economy with a very strong boost in the short term. Therefore, spending of oil revenues is at present held well below the four-percent path of expected return (with current spending being at 2.8 percent of the Fund).

As long as the Fund's capital increases relative to mainland GDP, the fiscal framework implies an expansionary fiscal stance. Since the guidelines were introduced in 2001, the structural non-oil budget deficit has increased from 1¾ to 5¾ percent of trend-GDP Mainland Norway, or on average by 0.3 percentage points a year. While the fiscal impulse is estimated to be above this average in 2014, this partly reflects that spending was lower than anticipated in 2013. The Fund's capital is expected to reach a peak at around 2 ½ times of Mainland GDP sometime in the period 2020-2030. Once the peak has passed, the impulse from fiscal policy to aggregate demand is expected to be negative.

The staff report suggests that a neutral fiscal stance would be preferable so long as the economy remains near potential. How quickly petroleum revenue should be phased into the economy is an important and legitimate question. In the view of my authorities, however, to completely stop phasing in petroleum revenues in an economy performing near trend could be seen as out of line with a framework that so far has served the country well and enjoyed broad political support.

The government has emphasized the need to strengthen the growth capacity of the Norwegian non-oil economy. This has bearings for the government's budget priorities. Lower taxes can improve competitiveness. Likewise, investments in infrastructure and knowledge can support productivity. In the 2014 budget the government has started to redirect the use of oil revenues along these lines.

A tax commission is currently reviewing the corporate tax system. Increasing taxes on housing as a balancing measure to reduced corporate taxes is not a prioritized issue.

Financial sector issues

Norwegian banks have strengthened their solvency significantly in recent years, due to both new capital requirements and demands from lenders and other financial markets participants. Loan losses are low, but the banks must be prepared for the possibility of increased losses in the next few years. Banks' financial position strengthened in 2013, but Norwegian banks need to further bolster their equity capital position to tackle economic uncertainty and forthcoming regulatory requirements.

My authorities generally concur with staff's assessment of the risks and vulnerabilities associated with households' indebtedness, a possible house price reversal and financial institutions' reliance on wholesale funding. Uncertainty is a key feature in the international

economy, still being affected by financial imbalances. Banks must therefore continue to strengthen their capital base, and assure more robust funding and improved liquidity.
A new capital adequacy regulation for banks adopted by the Norwegian parliament in June 2013 contains a set of macroprudential tools and powers. These are already in place to increase capital levels in Norwegian banks. The counter-cyclical capital buffer, the buffer for systemically important banks, and minimum floors for mortgage risk weights, are important elements of the new capital adequacy regulation.

My authorities are pleased to note that staff recognizes one of the most important financial sector policy issues for Norway. This is the need for tighter capital risk weights on mortgage lending for both domestic and foreign banks, and the efforts to harmonize prudential standards among Nordic countries through reciprocity. My Norwegian authorities believe that different national circumstances may require different prudential policy responses, and that a greater degree of host country regulation will contribute to securing financial stability and leveling the playing field in national credit markets.

Structural policy

The Norwegian authorities welcome the emphasis on structural policy in the staff report. Large terms of trade gains and rapidly increasing demand from offshore activities may have masked the consequences of a decline in wage competitiveness relative to peer countries. As demand from the petroleum sector will diminish at some stage, the Mainland economy needs to shift to a growth model less dependent on the oil and gas sector. This calls for stronger emphasis on structural policies and productivity growth.

In this context, the government has already introduced several structural policy measures. The government has published a consultation paper on reforming the municipality structure with the aim to increase the size of municipalities and make them more robust. Also, some measures to increase efficiency in the agricultural sector are already taken. In order to reduce costs and shorten the planning process in the construction sector, the government has proposed changes in building and planning regulations. Furthermore, the government recently published a consultation paper with proposals to soften labor market regulations on working hours in order to increase labor market flexibility. In addition, a commission has been appointed to explore how the regulations on working hours can be relaxed in order to better mobilize labor resources without infringing upon important rights to health and welfare. Measures to increase efficiency in road construction are also a main task for the government.

As noted in the staff report, a Productivity Commission was appointed soon after the present government took office. The Commission’s first report is to be presented in February 2015. The government will consider all initiatives to increase productivity in the Norwegian economy.

As mentioned above, a main strategy for the government to achieve a more growth-friendly policy for Mainland businesses is to reduce taxes and to direct government spending towards transport, research and development, and education. The bulk of future increases in spending of oil revenues will therefore be on tax reductions, in combination with a broadening of the tax base, and the mentioned expenditures items.

The Norwegian government wants to reduce taxes, especially taxes that hamper productivity and economic growth. Several tax cuts have already been introduced in that regard, most notably a cut in the personal and corporate income tax rate from 2014. My authorities concur with the staff report that a simpler tax system would underpin productivity. Growth-enhancing tax cuts in combination with simplifications and a broadening of the tax base will be prioritized in the coming years. The relatively high corporate tax rate is an area of particular concern.

In recent years, Norway has implemented comprehensive reforms of the old age pension in the social security system, and of the early retirement scheme in the private sector. Benefits can already be seen in the form of an increase in already high labor market participation rates among elderly. However, as pointed out in the staff report, still there remains a need to reform occupational pensions in the public sector, and more must be done to reduce the high level of disability and sickness.