

# Executive Summary

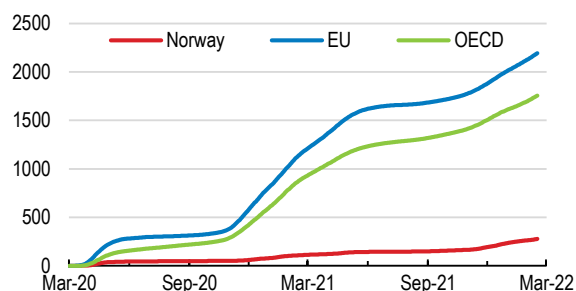
## Consolidating economic recovery

**Spread of the Omicron variant of COVID-19 temporarily damped economic activity, which was hitherto recovering strongly, and led to further fiscal support. In the absence of renewed deterioration in the health and economic situation, fiscal deficit reduction should resume as planned and the withdrawal of monetary stimulus should continue. A close watch on price and cost developments is needed given recent energy-price and wage increases.**

Though the Omicron variant affected Norway more than previous waves of the pandemic, the cumulative cases and fatalities from COVID-19 remain substantially below the OECD average on a per capita basis. A high rate of vaccination has helped limit increase in hospitalisations and fatalities. However, outbreaks and need for further social distancing measures remain a risk.

### Figure 1. Norway's per capita COVID-19 fatalities remain below the OECD average

COVID-19 cumulative deaths per million inhabitants, 7-day moving average



Source: Our World in Data.

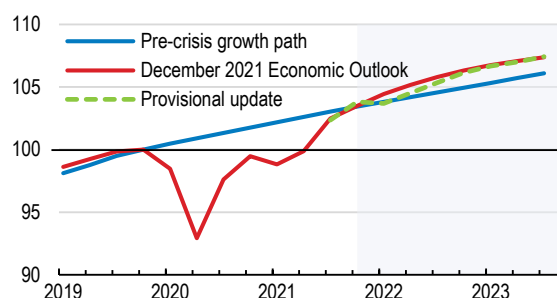
StatLink  <https://stat.link/mwjjezh>

**Following a bounce-back from the phase-out of the latest restrictions, the level of economic output will run slightly above trend over the next two years.** Annual economic growth is expected to turn out at 3.7% in 2022 and 2.2% in 2023. Household consumption will contribute significantly, helped by the pent-up spending power from savings accumulated during the initial phases of the pandemic.

**Strong headline consumer price inflation in recent quarters has been driven by large electricity price increases.** Global supply bottlenecks in computer chips, lumber and shipping are also putting pressure on inflation. Furthermore, there are tentative signs of higher wage inflation. Some of these price and cost rises will most likely ease in the coming quarters. However, there is clear risk that a wage-price spiral could emerge.


### Figure 2. The Omicron wave led to a pause in recovery

Mainland real GDP, index 2019 Q4 = 100, s.a.



Note: The pre-crisis growth path is based on the November 2019 OECD Economic Outlook projection, with linear extrapolation.

Source: OECD Economic Outlook 106 and 110 (databases); and provisional updates.

StatLink  <https://stat.link/0y16v4>

### Table 1. Strong growth in 2022 despite the Omicron wave

(Annual growth rates, unless specified)	2020	2021	2022	2023
<b>Mainland GDP (December 2021)</b>	<b>-2.3</b>	<b>4.2</b>	<b>4.2</b>	<b>1.7</b>
<b>Mainland GDP</b>	<b>-2.3</b>	<b>4.2</b>	<b>3.7</b>	<b>2.2</b>
Private consumption	-6.6	5.0	6.6	3.1
Government consumption	1.8	3.9	2.2	1.2
Gross fixed capital formation	-5.6	-0.3	3.7	3.0
Exports of goods and services	-1.2	4.8	7.2	3.0
Imports of goods and services	-11.9	2.0	8.4	2.7
Unemployment rate (% of labour force)	4.6	4.3	3.5	3.2
<b>Consumer price index (December 2021)</b>	<b>1.3</b>	<b>3.4</b>	<b>2.0</b>	<b>1.4</b>
<b>Consumer price index</b>	<b>1.3</b>	<b>3.5</b>	<b>2.5</b>	<b>1.5</b>

Note: Unless otherwise stated, these projection numbers are from a provisional economic forecast by the OECD in February 2022.

Source: OECD Economic Outlook 110; and OECD calculations.

### Withdrawal of macroeconomic stimulus should continue as the health situation improves.

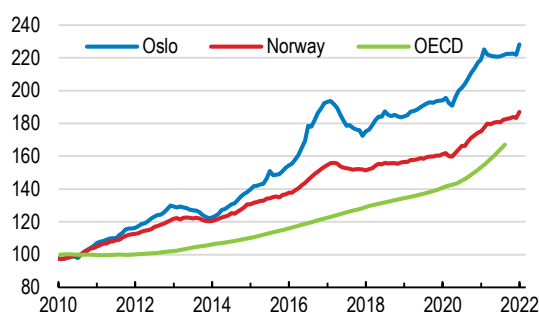
Fiscal revenues have grown and spending on government transfers has diminished since the initial large downturn in economic activity. Norges Bank began raising its key policy rate in September 2021 with an increase from zero to 0.25% and a further increase to 0.50% in December. The Bank forecasts a gradual rise to a rate of 1.75% towards the end of 2024. Thus far, the fiscal and monetary response to changing health and economic conditions has been appropriate.

### House prices and mortgage debt are a concern for financial stability.

Steep rises in house prices in the first year of the pandemic added to past price surges. Steady tightening of monetary policy has contributed to a moderation in price growth. However, prices remain elevated, and this and associated high levels of mortgage borrowing add to risks of a significant house-price correction with impacts on the wider economy.

**Figure 3. House prices surged during the pandemic**

Index 2010 = 100, s.a.



Source: Calculations based on Real Estate Norway (Eiendom Norge) data; OECD (2021), Analytical house prices database.

StatLink  <https://stat.link/akcmjr>

### A decline in the mainland fiscal deficit has been budgeted for 2022.

The central government's core deficit (adjusted for petroleum revenues and oil fund revenues) is estimated at 11.6% of mainland GDP for 2021. For 2022 a deficit of 9.5% was planned, though it is estimated to turn out at 10.4% due to the new COVID measures plus compensation for high electricity prices. This nevertheless continues to represent an

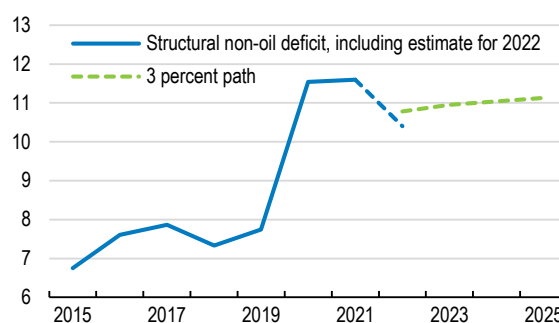
appropriately prudent policy; the budgeted deficit will be below the guideline value according to the fiscal rule.

### Scope for public spending on new policy measures is set to shrink in the coming years due to slower wealth-fund growth, multi-year spending commitments and population ageing.

Unlike in previous years, there will be limited scope within the fiscal rule for new spending initiatives, unless these are accompanied by revenue-raising or cost-saving measures. There will be even less fiscal space if cash flow from petroleum activities or returns to the fund turn out weaker than expected. Public-spending policy needs to focus on strengthening value for money.

**Figure 4. The 2022 deficit has been budgeted to be below the fiscal rule's guideline value**

Projection of the 3% deficit path, % of trend mainland GDP



Note: The mainland structural deficit is the cyclically-adjusted total budget surplus excluding petroleum and oil fund revenues. The "3 percent path" is the deficit implied by the rule for wealth fund spending that stipulates a guideline spending of 3% of the value of the wealth fund.

Source: Ministry of Finance, National Budget 2022.

StatLink  <https://stat.link/e19a2b>

### Strengthening sustainable productivity and employment

**Business-sector productivity growth has been picking up but remains below historical levels. The employment rate is no longer among those of top-ranking countries.**

**Policy needs to ensure good conditions for business innovation and technology adoption. It also needs to address the opportunities and challenges of green transition.** Financial

pressure on businesses during the pandemic has underscored the important role of insolvency procedures in giving struggling businesses a chance to turn around. Resources need to be reallocated to more promising sectors and firms, including those related to faster digitalisation and green transition. Meanwhile, some areas of business support require reform, notably there is a need to reorient agricultural support away from economically distorting subsidies.

**Norway's generous sick leave and disability compensation systems, in addition to the pension system, remain major challenges for labour participation.** Sick leave compensation remains more generous than necessary and disability pension systems could do more to facilitate return to work. Though good progress has been made on pension reform, there remains scope to improve linkage to life expectancy and there are challenges in some occupational pensions in the public sector.

### Ensuring enough affordable housing

*Rising house prices during the pandemic have further reduced housing affordability for first-time homebuyers. Deteriorating accessibility of homeownership and high rent burdens underscore the need for structural reforms to lift new housing supply and temper demand for home buying.*

**Altering regulation affecting land use, and more efficient planning processes around residential construction are key to making housing supply more responsive.** More leeway is needed for the construction sector to respond to housing demand while retaining high standards on other fronts. Scope for adjustment lies in land-use rules, building standards, and planning processes, especially in the largest cities.

**Tax concessions for homeowners remain unusually generous compared with other OECD countries.** These boost demand for housing, divert resources from more productive investments and inflate house prices, particularly in supply-constrained cities. The tax subsidies also favour current owners at the cost of new homebuyers.

**Social-housing shortages have emerged in high-cost cities, while households in private rental dwellings face heavy housing-cost burdens.** Beyond targeted assistance for low-income homebuyers, support needs to be bolstered for renters. Increased investment in social rental housing can alleviate cost pressures for disadvantaged households, backed with means-tested allowances for private rental accommodation.

**Housing affordability could be improved by reducing labour income tax on low income.** Raising disposable income through tax cuts can broadly help households tackle housing affordability. It can also help resolve the welfare issues emerging from other cost increases, for instance those related to climate change measures. Lighter labour taxes can also strengthen labour supply.

### Tackling climate change

*Norway's CO<sub>2</sub> emissions are low but are generated in sectors where cutting them is challenging. Norway has raised its ambition on emission reduction and is combining market-based instruments with regulation and support for green technology.*

There has been a welcome proposal to increase the price of carbon as part of a new climate action plan. Nevertheless, gaps in the coverage of carbon taxation remain, mainly on emissions of nitrous oxide and methane from the agricultural sector.

**Norway is making good progress in the adoption and development of green technologies.** Electric vehicle adoption has matured to a point where tax concessions and other advantages can gradually be withdrawn. Substantial green-technology initiatives are underway, notably a flagship carbon-capture and storage programme (*Longship*). However, there is more ground to cover, including clearing regulatory obstacles to greater materials recycling and extending the service life of residential and other buildings.

MAIN FINDINGS	KEY RECOMMENDATIONS
<b>Handling post-recovery challenges</b>	
<p>Following a short downturn due to the Omicron wave, the level of economic output will run slightly above trend over the next two years. Economic recovery is well-advanced and vaccination rates are high. However, as the Omicron wave demonstrated, risk of renewed outbreaks and social distancing measures remains. Recent strong price and cost increases will most likely ease in the coming quarters but there is a risk of sustained higher inflation. Vulnerabilities stemming from property markets remain a risk.</p>	<p>Maintain a close watch on price and wage inflation and continue to normalise monetary and fiscal conditions.</p> <p>Stand ready to tighten macroprudential tools if strong house-price growth resumes.</p>
<p>The deficit for 2022 is expected to turn out below the long-term guideline value under the fiscal rule, despite new temporary COVID measures and compensation for high electricity prices. Fiscal space will narrow in the coming years due to slower wealth-fund growth, multi-year spending commitments and population ageing.</p>	<p>Retain a prudent approach to fiscal budgeting in the coming years.</p> <p>Use more productivity enhancing measures in public services, including spending reviews. Use cost-benefit analysis more extensively in public investment and retain the pruning of budget allocations through “efficiency dividends”.</p>
<b>Strengthening productivity and employment</b>	
<p>Post-pandemic, policy should nurture stronger business-sector productivity. One strand should be to ensure businesses are easy to establish and have good paths to recovery when running into financial difficulty. Another strand should be to ensure sectoral business support encourages long-term economic and environmental sustainability, notably in agriculture.</p>	<p>Improve insolvency procedures through better routes to recovery for businesses in difficulty, including lighter penalties for failed entrepreneurs.</p> <p>Continue to tackle weak points in business efficiency including through re-orienting agriculture support away from the most economically distorting forms of support, including import tariffs.</p>
<p>The pandemic demonstrated the value of comprehensive sick leave compensation and disability support, but nevertheless reforms are needed to enhance labour-force attachment. Norway has a record high incidence of sick leave compared to other countries.</p>	<p>Strengthen incentives to reduce sick-leave absences, including through lowering sick-leave compensation and by extending employers’ participation in funding.</p> <p>In disability benefits, in addition to retraining and other support, apply eligibility rules more strictly and strengthen treatment and rehabilitation requirements.</p>
<p>Ensuring the pension system adjusts as people live longer is important to ensure balanced retirement decisions. Special pensions provisions for some public occupations mean early retirement remains common and pension provisions do not appropriately adjust payouts when individuals decide to retire early.</p>	<p>Index age dimensions of the pension system to life expectancy, such as the retirement-age range of 62 to 75 years.</p> <p>Continue to align special pension provisions for groups such as nurses, national defence and the police with the mainstream pension system.</p>
<b>Ensuring enough affordable housing</b>	
<p>Concessions on the taxation of owner-occupied dwellings are inefficient and contribute to wealth inequality and higher housing prices.</p>	<p>Gradually phase in imputed rents to owner-occupied dwellings in income tax or gradually phase out mortgage-interest deductibility.</p> <p>Introduce tax on capital gains from sales of owner-occupied dwellings, eliminating exemptions based on periods of ownership and occupancy.</p> <p>Reduce disparities in wealth-tax discount rates applied to owner-occupied homes and other assets.</p>
<p>Social-housing shortages have emerged in high-cost cities.</p>	<p>Increase loans for building social rental housing, particularly in cities such as Oslo with currently constrained supply.</p> <p>Consider reducing labour income tax on low-income households, as a broad means of addressing housing affordability and other cost-of-living issues.</p>
<p>The residential construction sector requires more leeway to respond swiftly to housing demand while retaining high standards on other fronts. Shorter, cheaper and more predictable planning processes would improve the scale and responsiveness of housing supply, especially in the largest cities.</p>	<p>Ease national restrictions on land use.</p> <p>Allow more small apartments in inner-city neighbourhoods.</p> <p>Enable streamlined approval processes for small urban-infill projects.</p>
<b>Tackling climate change</b>	
<p>Norway has initiated a schedule of carbon-price increases and has recently launched large-scale publicly-supported projects for carbon-capture and storage. Achieving greenhouse gas emission goals in Norway requires reducing gross domestic emissions from the current 50 million tonnes of CO<sub>2</sub> equivalent to around 25 million tonnes in 2030 and close to zero by 2050 (90-95% reduction).</p>	<p>Ensure continued follow through on the schedule of carbon-price increases. Augment this with additional greenhouse-gas reduction measures via regulation and investment, in particular in transport and agriculture.</p> <p>Develop carbon pricing on emissions of methane and nitrous oxide in the agricultural sector.</p> <p>Make electric vehicles gradually subject to VAT and the motor vehicle registration tax.</p>
<p>Measures for more efficient use and re-use of CO<sub>2</sub>-intensive building materials, such as steel and concrete, can significantly reduce greenhouse gas emissions associated with the construction and replacement of dwellings.</p>	<p>Push ahead with proposals to remove regulatory impediments to increased use of second-hand building materials.</p>



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