Svein Gjedrem: Monetary policy and the outlook for the Norwegian economy

Speech by Mr Svein Gjedrem, Governor of Norges Bank (Central Bank of Norway), to the Mid-Norway Chamber of Commerce and Industry, Trondheim, 13 November 2003.

The speech is based on the assessments presented at Norges Bank's press conference following the monetary policy meeting on 29 October, Norges Bank's Inflation Report *3/03, the* Report on Monetary Policy 2003 - the first eight months *and on previous speeches.*

The text below may differ slightly from the actual presentation.

The Charts in pdf can be found on the Norges Bank's website.

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I would like to thank the Mid-Norway Chamber of Commerce and Industry for inviting me to speak to you today on monetary policy and the outlook for the Norwegian economy.

The operational target of monetary policy as defined by the Government is inflation of close to 2.5 per cent over time. It is equally important to avoid an inflation rate that is too low as it is to avoid an inflation rate that is too high.

The inflation target provides economic agents with an anchor for their decisions concerning saving, investment, budgets and wages. The inflation target also provides a framework for monetary policy's contribution to stabilising output and employment. This intention is also expressed in the Regulation on Monetary Policy. Normally, Norges Bank sets the interest rate with a view to achieving inflation of 2½ per cent at the two-year horizon. However, it would in general have been possible to attain the inflation target in the nearer term by changing the interest rate more rapidly and more markedly. Hence, in Norges Bank's conduct of monetary policy, emphasis is given to variability in both output and inflation. This is called flexible inflation targeting.

The impact of monetary policy occurs with a lag. The current inflation rate does not therefore provide sufficient information to determine the level at which interest rates should be set now. Our analyses indicate that a substantial share of the effects of an interest rate change will occur within two years.

The choice of a two-year horizon is thus based on striking a balance between inflation stability and output stability and on a perception of how interest rates influence the path of inflation and output.

Activity in the economy moves in waves. This variability can be described by developments in what is known as the output gap. The output gap shows capacity utilisation in the mainland economy measured as the difference between actual GDP and the level indicated by trend growth, estimated at 2½ per cent in Norway. When the output gap is positive, the economy experiences an upturn, and a downturn when the output gap is negative. The output gap increases in value in an upturn and decreases in a downturn.

For the Norwegian economy, the 1980s was a period of relatively wide fluctuations in activity, with periods of high inflation. At the beginning of the 1990s, the Norwegian economy was in a deep recession. Production was far below capacity. The output gap was negative. When growth in the economy picked up, capacity utilisation increased. Around 1996, there was full capacity utilisation, and the output gap, as we normally measure it, closed. The mid-1990s represents a period of stable and solid growth. In contrast to the situation in the two previous decades, inflation was low and stable.

From the mid-1990s, the rise in labour costs and in prices for goods and services produced for the Norwegian market accelerated. The upturn peaked in 1997, with mainland GDP growth approaching five per cent. The economy then shifted from an upturn with high growth rates to an expansion with lower growth but low unemployment, labour shortages in many sectors and strong growth in labour costs.

Since 1998, output growth has been low and the output gap has narrowed. Current capacity utilisation is on a par with the level prevailing in 1995-1997, before cost inflation accelerated. Growth stalled last winter and has been well below capacity in the first half of 2003. Growth is now picking up momentum, however.

Inflation has slowed over the past 12 months and is now considerably below target. Annual CPI-ATE inflation was 0.8 per cent in October. Inflation in 2003 has also been lower than projected in the 2001 and 2002 Inflation Reports.

An account of the reasons for the deviation from the inflation target is included in Norges Bank's *Report on Monetary Policy in 2003 - the first eight months.*

In the years 1998-2002, the Norwegian economy was characterised by substantial labour shortages and a considerably higher rise in labour costs than among its trading partners. Last year was the fifth consecutive year of very high annual growth. Wage growth was substantially higher than the level that over time is consistent with the inflation target and with normal productivity growth. Pay increases varied widely across the different groups. In Norges Bank's view, there was therefore a substantial risk of new wage-wage spirals. Further rounds of such strong wage increases might have led to a considerable decline in output and employment.

Monetary policy was therefore tightened by an interest rate increase last summer. At the one-year horizon, the strong krone would push down inflation to below 2½ per cent, but the effects of strong wage growth would subsequently dominate.

Last year, Norges Bank's Executive Board struck a balance between the consideration of stable inflation developments in the short term and the consideration of stability in output and employment. It was expected that inflation would be low in 2003.

However, price developments are uncertain even 6 months to 1 year ahead. There was thus a possibility that inflation could fall even lower than projected, and be more than 1 percentage point below target. Nevertheless, the deviation from the forecast is unusually large.

This is an indication that the economy was exposed to sizeable unexpected disturbances. The exchange rate appreciated more than projected. After the publication of *Inflation Report* 3/02 in October last year, the krone appreciated further. This was related to unexpectedly weak developments in the global economy resulting in lower interest rates abroad and a wider interest rate differential between Norway and other countries. Negative events such as the accounting scandals in large US companies, fears of terror and war in Iraq and the spread of SARS contributed to weak growth and low inflation in other countries. Developments in the international equity markets and the risk of higher oil prices also contributed to strengthening the krone.

In addition, the Norwegian business sector has clearly felt the effects of the high Norwegian cost level and the strong krone in 2002. Growth in private consumption came to a temporary halt last winter as a result of high electricity prices and general uncertainty. This probably affected profit margins in retail trade, particularly for durable consumer goods. Public entities have also had to make adjustments following last year's wage settlement. Sluggish global and domestic growth has in turn had an impact on the Norwegian labour market.

Inflation in 2003 has been pushed down by the fall in prices for imported consumer goods in particular. The low rise in imported price inflation is a consequence of the appreciation of the krone throughout 2002 and low inflation abroad.

The rise in prices for domestically produced goods and services has also gradually slowed. This is particularly the case for prices for domestically produced goods influenced by world market prices.

The fall in prices for imported consumer goods is not solely attributable to exchange rate developments. Clothing prices have exhibited a falling trend over the past few years. In October 2003, clothing prices were 13.7 per cent lower than in the same month one year earlier, and almost 30 per cent lower than in 1995. In addition to low external price inflation for these goods, lower tariffs for clothing have translated into lower consumer prices. The removal of quota regulations has also led to a shift in clothing imports away from high-cost countries to countries with considerably lower production costs.

The same trend has been observed for the audiovisual industry. Since the mid-1990s, prices for audiovisual equipment have fallen markedly. In October, prices for these goods were 8.5 per cent lower than one year earlier. International producers have moved production to low-cost countries, allowing them to reduce prices charged to Norwegian importers. In addition, new technology and intensified international competition have exerted downward pressure on prices.

Global economic growth has been considerably weaker than expected. Changes in the economic outlook are clearly reflected in interest rate expectations. In the US, these expectations have been adjusted downwards considerably since summer 2002. At that time, market participants expected the key rate in the US to be increased to about 4 per cent towards the end of 2003. Now, interest rates are believed to have reached their lowest level and are expected to remain at 1 per cent until the end of 2003, with only a gradual rise thereafter. Interest rates were also expected to increase markedly in

Europe in summer 2002. Instead, interest rates were also reduced here and expectations were revised downwards substantially.

The lower projections for growth reflect the effect on the world economy of a number of negative shocks, such as the war in Iraq and the SARS outbreak. It may have taken longer than first expected to correct imbalances generated by overoptimism in sectors such as the IT industry. High oil prices may also have contributed to restraining growth.

The combination of low international interest rates and weak cyclical developments contributed to high interest rate differentials against the krone and the strong exchange rate.

Activity in the global economy has picked up from the low level prevailing last winter, primarily reflecting high growth in the US and some Asian economies, including Japan. Recent statistics show that the annual rate of GDP growth in the US was 7.2 per cent in the third quarter of 2003. Strong growth in private consumption and a rise in business investment are evidence of a gradual and broad-based upturn. Employment figures are also showing a positive trend and unemployment is falling.

Following the meetings of the Open Market Committee in August, September and October, the Federal Reserve stated that there is a risk of a further and undesirable fall in inflation, and that it was therefore likely that short-term interest rates in the US will remain low for a considerable period. Interest rates in other countries are also likely to remain low.

In the euro area, developments have been considerably weaker, even though there are now signs that the trough has been reached. Growth among Norway's trading partners as a whole is expected to pick up over the next two years.

The Reserve Bank of Australia and the Bank of England recently raised their key rates.

The interest rate in Norway has been lowered substantially. The interest rate cuts must be seen in connection with the change in the inflation outlook, which has occurred as a result of weaker global economic developments and low international interest rates. The key rate has been reduced with a view to bringing inflation back to target at the two-year horizon. Moderate pay increases in this year's wage settlements and prospects for wage growth falling to a more sustainable level for a prolonged period have been an important factor behind the considerable easing of monetary policy. An interest rate as low as 2½ per cent, however, largely reflects a long period of low interest rates abroad with little prospect of an increase in the near future in the largest economies. Weaker developments both abroad and at home have had an impact on the Norwegian labour market. Unemployment has increased.

Decisions concerning saving and investment are affected by the real interest rate, that is the nominal rate minus expected inflation. The real interest rate is also low.

An enterprise investing in productive capital will typically apply a longer perspective than a household buying durable consumer goods. Enterprises' cost estimates will be based on the interest rate and expected inflation in the long term, while short-term interest rates and expectations will be more important to households.

Monetary policy influences inflation indirectly via domestic demand for goods and services and via its effect on the exchange rate. Because changes in the economy take time to feed through, monetary policy functions with a lag. It will therefore take time for all the effects of the substantial changes in the interest rate since December 2002 to come into evidence.

When interest rates fall, consumption rises both because disposable income increases and because it is less profitable for households to save. Borrowing also becomes less costly, with an associated rise in investment. Higher demand leads to higher employment.

Another important mechanism is that lower interest rates make it less attractive to invest in NOK. Lower interest rates will therefore normally lead to lower capital inflows and a weaker krone. Imported goods thereby become more expensive and inflation can rise relatively rapidly. The time lag in product markets can, however, delay this effect somewhat, as was the case when the krone appreciated in 2001 and 2002. In addition, a weaker krone increases activity, profitability and the capacity to pay in the Norwegian business sector.

Higher demand and wage growth may lead to higher inflation through enterprises' price-setting. In the long run, wages must be commensurate with the value added that is generated by workers. Real wage growth is thus determined over time by developments in labour productivity in all sectors of the economy. With productivity growth at the historical level of about 2 per cent, wage growth of about

4½ per cent over time will be consistent with Norway's inflation target of 2½ per cent. Wage growth that is lower than 4½ per cent will boost employment and wage growth that is higher will reduce employment.

Through 2003, the differential between Norwegian and foreign interest rates has narrowed considerably. This has also contributed to a substantial depreciation of the krone. The depreciation of the krone will make imported consumer goods more expensive, but will also improve competitiveness for Norwegian enterprises.

Interest rate differentials are also affected by cyclical developments abroad. Subdued economic growth internationally, high levels of activity and a sharp rise in labour costs in Norway resulted in a wide interest rate differential between Norway and its trading partners in 2001 and 2002. This made it profitable to invest in NOK, and the krone appreciated. The appreciation of the krone and high wage growth led to a considerable deterioration in the competitiveness of Norwegian enterprises - and made imported consumer goods cheaper.

Norges Bank has no set target for the level of the exchange rate. Developments in the krone exchange rate are nevertheless important in interest rate setting. The response to a change in the exchange rate will depend on its expected impact on inflation. This requires an evaluation of the reasons for and the duration of the change. Short-term fluctuations in the krone exchange rate tend to have very limited effects on economic developments, while long-lasting changes can have an impact.

High wage growth over several years has eroded the competitiveness of the Norwegian business sector. Last year, the effects of high wage growth on export industries were amplified by the changes in the krone exchange rate. The krone has now reverted to around the level prevailing in the mid-1990s, while labour costs in manufacturing have increased by almost 15 per cent more than among our trading partners in the same period. The appreciation of the krone proved to be reversible, but the loss of competitiveness and jobs caused by relatively high domestic wage growth is difficult to recoup. A precondition for a considerable improvement in competitiveness is that real wage growth is lower than productivity growth in the business sector for a period. Experience shows that this only occurs in periods with low resource utilisation. This is also an indication that changes in competitiveness over time depend on real economic factors and aspects of wage formation and cannot be controlled by monetary policy.

Household demand will probably be the most important driving force in the Norwegian economy in the period ahead. Private consumption has a considerable impact on overall demand and activity and accounts for 60 per cent of mainland GDP.

There are prospects of strong growth in private consumption. The interest rate reductions are contributing to strong growth in disposable income. When households' interest-bearing debt is substantially larger than their interest-bearing assets, a fall in interest rates will reduce household interest expenses. The magnitude of this effect depends on the impact of the key rate on deposit and lending rates to households and on the proportion of the debt that is tied to floating rate loan agreements. If we base our assumptions on Norges Bank's figures for household net lending for 2002, interest expenses could be reduced by NOK 12-15 billion on an annual basis. This corresponds to a rise in disposable income of just below 2 per cent. Because the fall in interest rates has occurred gradually through 2003, some of this effect will become evident in 2004 if interest rates remain low. Long-term interest rates are also historically low, enabling households to fix their borrowing rate for a few years at a level that is relatively low compared with the interest rate a few years ago.

The interest rate reductions may also result in a sharper rise in house prices, leading to stronger growth in household wealth. Historically, a larger share of household income has, in this situation, been used for consumption.

Lower real interest rates make it less profitable for households to invest in financial instruments and they will be more inclined to make purchases - for example of durable consumer goods - now, rather than wait until later. On the other hand, many households probably expect that the interest rate will not remain as low as it is now and will avoid allowing higher consumption to become entrenched. The fall in interest rates may provide an opportunity for households with large loans to make extra debt repayments. We nonetheless expect a fall in the saving ratio.

Lower interest rates may also increase the need for allocations to pension funds. Companies account for a substantial share of the allocations to pension funds, and their ability to pay will be reduced as a result.

In light of these prospects, a large majority of households have a positive view of their own future financial position. According to TNS Gallup's confidence survey for Q3 2003, confidence in the country's economy has also improved considerably from a low level earlier this year.

Companies are facing a different situation, however. While household income has risen sharply, earnings in the enterprise sector have been low with an associated low level of investment activity.

The difference in credit growth between households and non-financial enterprises is a good illustration of Norway's dual economy. Over the past few years, credit growth has been far higher for households than for enterprises. The level of household credit growth has remained high recently in spite of increased unemployment and a downward revision of the prospects for economic growth. An important reason for this is the sharp rise in house prices in recent years. Low investment demand is reflected in credit to non-financial enterprises, which has declined to a very low level. Developments in prices for commercial property compared to house prices also indicate that the situation is better for households. The current level of vacancy in commercial premises is very high. Although lower interest rates will, in isolation, stimulate investment, a substantial share of the vacant premises will probably have to be filled before renewed growth can be expected.

Developments in mainland enterprises have been characterised by low output growth, falling investment and declining profitability in many industries. In order to boost returns on invested capital, enterprises have taken steps to reduce costs, primarily by reducing their workforce or relocating parts of their production abroad.

There are some positive impulses, however. Interest rates are low, and equity prices have increased sharply since the trough in February 2003. The krone has depreciated and there are signs of a global upturn. Wage growth has moderated and cost inflation is likely to be lower than in the years from 1998 to 2002. Given the high level of costs and excess capacity in a number of sectors, we expect, however, that it will take some time for employment and investment in the business sector to pick up. On balance, we expect investment by mainland enterprises to make only a marginal contribution to growth in the Norwegian economy in 2004. Renewed growth is not expected until 2005 and 2006.

Investment in the petroleum sector, however, is expected to increase markedly both in 2003 and 2004. Even though the share of imports is high, these investments will contribute to holding up activity in oil-related industries. The current low level of exploration activity on the Norwegian continental shelf points to a relatively sharp fall in investment looking further ahead. Demand is also being sustained by investment to keep mature fields in operation and by the scrapping of old platforms.

Another important factor influencing overall demand in the economy is fiscal policy. In recent years, expenditure growth in the government budget has increased at a faster pace than growth in mainland GDP. Nominal expenditure growth was particularly strong in 2002, but slowed markedly in 2003. In the central government budget for 2004, the Government proposes a 5.4 per cent increase in expenditure, or slightly more than estimated trend growth in nominal mainland GDP. The level of taxes remains virtually unchanged in real terms.

Fiscal policy has stimulated economic activity, also when adjusted for cyclical fluctuations. This is reflected in the increase in the structural, non-oil budget deficit since 2001. The Government has included a further increase in the deficit, measured as above, in the National Budget for 2004. However, the budget balance figures are influenced by transactions that have little effect on demand. For 2003 and 2004 as a whole, fiscal policy will probably generate some stimulus to activity in the Norwegian economy. As cyclical developments will probably stabilise, our forecast is based on the technical assumption that the structural deficit will not increase in 2005 and 2006. This would also seem to be consistent with the practical application of the fiscal rule, cf. the discussion by the Ministry of Finance in the National Budget for 2004.

According to the fiscal policy guideline, the use of petroleum revenues over the central government budget shall over time correspond to the expected real return on the Government Petroleum Fund. At the same time, fiscal policy shall contribute to smoothing fluctuations in output and employment. Since the introduction of the fiscal policy guideline in spring 2001, the scope for manoeuvre in fiscal policy has been reduced. The projection for the Petroleum Fund's expected real return has been revised down substantially since the Revised National Budget for 2001.

Wage growth in the years 1998-2003 indicates that the degree of labour shortages in all sectors of the labour market plays an important role in wage formation. The low pay increases in this year's wage settlement may indicate that the social partners are placing more emphasis on the negative effects of large pay increases on future developments in interest rates, the krone exchange rate and employment. We expect that in the light of the experience gained in 2002, public entities will exercise more caution in future wage settlements. Expectations of moderate wage growth are supported by the labour market outlook.

The monetary policy easing since last December will boost demand, primarily through private consumption and gradually through business investment. The increase in petroleum investment will also contribute to higher demand for Norwegian products and services. As global demand picks up and excess capacity in service industries is reduced, demand for labour may rise in other sectors of the economy. Unemployment is expected to edge down again.

The aim of monetary policy in the period ahead is to achieve a higher level of inflation. The key rate has been reduced with a view to bringing inflation back to target at the two-year horizon. Analyses in the October Inflation Report indicate that inflation will move up and stabilise around the inflation target at the two-year horizon. The real economy is projected to be approximately in balance, with an output gap, as we measure it, that is slightly positive.

The analyses are based on the technical assumption that the interest rate will move in line with expectations in financial and foreign exchange markets, implying that the interest rate will remain at the current level well into 2004. Thereafter, the interest rate in Norway is assumed to rise gradually in pace with interest rates in other countries. The forward exchange rate implies a moderate depreciation of the krone through the projection period. Such interest rate and exchange rate developments would be consistent with the monetary policy objective and would probably also contribute to keeping inflation expectations at around 2½ per cent.

Overall, growth in mainland GDP is projected at ¾ per cent in 2003. Growth was about zero in the first half of the year, but is projected to pick up in the latter half of the year and be high in 2004. Mainland GDP growth is projected at 3 per cent in 2004 and 2¾ per cent in 2005. In 2006, mainland output is expected to grow below but close to trend, which we estimate at 2½ per cent.

As the fall in the krone exchange rate feeds through in the economy, inflation will gradually rise. As early as next year, inflation will probably be considerably higher than the current level.

The inflation projections are uncertain. The uncertainty may be illustrated by intervals calculated on the basis of historical deviations in actual price developments in relation to projections. Inflation may move on a different path than projected for several reasons.

The interest rate reductions and the fall in the krone exchange rate imply that inflation will gradually increase and will be considerably higher than the current level as early as next spring. After such a period of very low inflation as we have now witnessed, it is appropriate to be particularly vigilant in monetary policy in the event that inflation does not increase as projected.

We have little experience concerning the effects of such considerable monetary policy easing as that seen over the past year. It is uncertain how economic agents will adapt to a real interest rate that is as low as it is now. Activity in the Norwegian economy may pick up more swiftly than expected. Excess capacity may be reduced more rapidly and unemployment may fall to a greater extent than we have projected. If new pressures arise in the Norwegian economy, inflation may be higher than projected.

Growth in household borrowing, which has slowed since spring 2002, may accelerate again. A renewed rise in house prices and the debt burden may provide the basis for new imbalances in the economy. On the other hand, growth in corporate borrowing has remained very low.

The projections are based on the assumption that wage growth is primarily determined by overall conditions in the labour market. It cannot be ruled out, however, that profitability in internationally exposed industries will again play a more prominent role in wage formation than has been the case in recent years. Overall wage growth may then be lower than projected and provide the basis for an easing of monetary policy.

The global economy appears to be vulnerable to new disturbances. Since summer 2002, international financial market developments have been marked by increased optimism concerning the growth outlook. Equity prices and long-term interest rates have risen. The increase has been uneven, however, and there have been wide fluctuations between major currencies. This may be a reflection of the uncertainty about the strength of the global economic recovery.

Developments in the krone exchange rate represent a source of considerable uncertainty. The relationship between the krone exchange rate and the interest rate differential against other countries is not necessarily stable over time. Themes in international financial markets shift. We may not yet have seen the full effects of the interest rate reductions on the krone exchange rate.

Even though Norges Bank is forward-looking in its conduct of monetary policy, thorough knowledge of the current economic situation is extremely important. An up-to-date and correct picture of the current situation is necessary to make accurate projections for the period ahead.

In autumn 2002, Norges Bank established a regional network as a tool to gauge the level of activity in the Norwegian economy.

Official statistics and evaluations of developments in financial markets will continue to be the main basis for our assessments, but due to the time lag and revisions of such statistics, supplementary information is useful.

The regional network provides up-to-date information on the state of the Norwegian economy. Regular communication with local contacts in Norway's business and community life provides us with information that supplements available official statistics. It also provides us with supplementary information about areas not covered by official statistical sources, and we learn which issues are of particular concern to enterprises.

The network consists of companies, organisations and municipalities throughout Norway. In six rounds of talks each year, we engage in discussions with business and community leaders on financial developments in their enterprises and industries, with about 200 visits in each round. The selection of contacts represents the production side of the economy, both industry-wise and geographically. The network will comprise about 1000 contacts in the course of 2003, who will be contacted once or twice a year. Allforsk in Trondheim is responsible for the contact meetings in Central Norway.

The industry structure in Central Norway is not substantially different from the rest of Norway. The public sector and some private service segments are important for employment in Central Norway. Primary industries are relatively more important in this part of the country.

A large share of the workforce in Central Norway is employed in the public sector, in part because there is substantial research and development activity in this region. Focusing on knowledge is very important for the economy's long-term production capacity, both for the nation and for the region. A study from Rogalandsforskning[1] shows that there are more newly established businesses in the Trondheim area than in any other urban centres in the country. The business sector in Trondheim is technologically highly advanced.

Norges Bank's regional network reports firm growth in the retail sector and the household service sector. Both manufacturing and corporate services report that the trough has been reached or passed. Activity in the construction industry has also stabilised and the number of new orders is edging up. There is considerable uncertainty about the strength and duration of the upturn.

The decline in employment is slowing, but few in the public or private sector report plans to increase employment. The supply of qualified labour is still good and is increasing somewhat in all sectors.

The regional network also reports that cost reductions in the business sector, especially in services, are now generating results in the form of improved profitability. The focus appears to have shifted to some extent from cost cutting to strategies for boosting income. Both the public and private sectors appear to be somewhat more positive about investment plans, but are still not signalling significant growth in investment over the next year.

Lower interest rates have contributed to more positive expectations concerning future developments. Few market participants believe that there has been any real impact yet, but many expect an improvement in the near future.

Contacts in the regional network in Central Norway believe that a rise in retail trade and household services is contributing somewhat to growth in the region, as is the case in the rest of the country. Growth now appears to be strong enough to hold up the level of employment. Manufacturing output increased slightly in the previous quarter. There is continued growth in retail trade.

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1 Gjelsvik, M and T. Høyvarde Clausen. (2003). Verdiskapingsevnen i norske storbyregioner. Rapport 2003/144. Rogalandsforskning.

The construction industry continues to report some growth in Central Norway. Increased activity in rural districts has reduced the previous differences between urban and rural areas. House sales are on the increase and there has been an appreciable rise in house prices. A rise in the number of new orders in manufacturing and the construction industry is generating expectations that growth will continue.

Most markets report intensified competition. This is partly a result of a rise in imports in some industries and increased capacity in retail trade. Margins are being reduced.

In Central Norway, as in the rest of the country, lower interest rates have contributed to more positive expectations concerning future developments.

There are wide regional variations in unemployment. At the end of October, 3.9 per cent of the labour force in Central Norway was registered as unemployed. This is slightly higher than the national average of 3.8 per cent.

All regions of the country have reported an increase in unemployment in the past year, although in Central Norway the increase has been relatively low. This is probably related to the industry structure with a relatively high share of employees in the public service sector. Reports from the regional network indicate that employment in the public sector will remain more or less constant in the period ahead, while there are indications of growth in some private business sectors. The start-up of Rica Nidelven Hotel generated 100 new jobs but also keener competition in Trondheim’s hotel industry.

As I mentioned earlier, this snapshot report on the current situation in this part of the country and similar reports from the other regions provide information that is important to interest rate setting.

Interest rates were left unchanged at Norges Bank’s Executive Board meeting on 29 October. The sight deposit rate therefore remains at 2.5 per cent. According to Norges Bank’s assessment, with an interest rate of 2.5 per cent, the probability that inflation two years ahead will be higher than 2½ per cent is the same as the probability that it will be lower.

By using a time horizon of two years when we set interest rates, monetary policy contributes to stabilising output. The choice of this horizon prevents monetary policy from contributing to unnecessary volatility in the economy.