EXECUTIVE BOARD'S ASSESSMENT

At its meetings on 3 September and 17 September 2014, the Executive Board discussed the monetary policy strategy. The starting point for the discussion was the strategy that the Executive Board adopted at its meeting on 18 June 2014 and the analysis in the June 2014 *Monetary Policy Report*. The analysis in the June 2014 *Report* implied a key policy rate of 1.5% in the period to end-2015, followed by a gradual rise. With this path for the key policy rate, there were prospects that inflation would lie somewhat below, but close to, 2.5% throughout the projection period. Capacity utilisation was projected to edge down in the coming year, but to move up again to close to a normal level towards the end of the projection period.

In its discussion at the meetings on 3 September and 17 September, the Executive Board placed emphasis on the following developments:

- Growth among Norway's trading partners combined has been slightly lower than expected, and prospects are now somewhat weaker than envisaged in the June *Report*. For trading partners as a whole, growth is projected to pick up from 2% in 2014 to 2½% in the coming years.

- Key policy rates are close to zero in many trading partner countries. In Sweden, the Riksbank reduced its policy rate to 0.25% in July. The European Central Bank lowered its policy rate to 0.05% at the beginning of September and at the same time announced that it will take additional monetary policy measures. Market expectations indicate that an increase in interest rates abroad has again been pushed further out.

- The krone has depreciated. The krone, as measured by the import-weighted exchange rate (I-44), has so far in Q3 been about 1¾% weaker than projected in the June *Report*.

- Bank lending rates have been broadly in line with expectations. Lending rates facing households and enterprises are still considerably higher than the key policy rate.

- Growth in the Norwegian economy was stronger than expected in Q2, as measured in the quarterly national accounts. However, the enterprises in Norges Bank's regional network reported in August that output growth remained moderate. Registered unemployment has been relatively stable and a little lower than expected. Capacity utilisation in the Norwegian economy is still projected to be close to a normal level, and has likely declined a little less than anticipated earlier.

- House prices have picked up broadly in line with that projected in the June *Report*. Household debt accumulation has moderated and been lower than expected earlier.

- Inflation has been higher than projected. Consumer price inflation adjusted for tax changes and excluding energy products (CPI-ATE) was 2.2% in August. Underlying inflation is estimated to run between 2% and 2½%.

The point of departure for the Executive Board's assessment of monetary policy is that the key policy rate is set with a view to keeping inflation close to 2.5% over time. The objective of low and stable inflation is weighed against the objective of stable developments in output and employment. Monetary policy should be robust. There is uncertainty surrounding economic driving forces and the functioning of the economy. This normally suggests a gradual approach in interest rate setting. At the same time, monetary policy takes into account the risk of a build-up of financial imbalances.

The Executive Board noted that the analysis in this *Report* implies little change in the outlook for inflation and output. The analysis implies a key policy rate at the present level in the period to end-2015, followed by a gradual rise. With this path for the key policy rate, inflation will be somewhat below, but close to, 2.5% throughout the projection period. Capacity utilisation may edge down in the coming year, but is expected to increase again to close to a normal level towards the end of the projection period.

The Executive Board pointed to the uncertainty surrounding the growth rate in the Norwegian economy. Growth gained considerable momentum in Q2, but some of the momentum is likely ascribable to temporary conditions, such as unusually high production of electricity and fish. It was noted that the enterprises in Norges Bank's regional network reported moderate growth in production. Petroleum investment is still expected to show a pronounced decline in 2015, and the magnitude of the spillover on the wider economy is uncertain. Moreover, somewhat weaker growth prospects abroad and the conflict between Russia and Ukraine entail greater uncertainty concerning the outlook for Norwegian exporters.

Consumer prices have been somewhat higher than expected. Fluctuations in food prices have resulted in wider-than-normal movements in the CPI through summer. It was pointed out that changes in the calculation methodology may have altered CPI seasonality. Wide monthly variations in inflation increase the uncertainty linked to short-term price developments.

The Executive Board also discussed housing market developments. Turnover in the housing market has increased, with a decline in the number of unsold homes. Residential construction is on the rise. At the same time, it was pointed out that the price rise so far this year may be a case of prices catching up after the weak developments in the housing market through autumn 2013. If financial imbalances build up further, it will be appropriate to assess the level of the countercyclical capital buffer requirement for banks.

In its assessment of monetary policy in the coming period, the Executive Board gave weight to the fact that the outlook for the Norwegian economy remains broadly unchanged. The forces driving inflation and output ahead are expected to remain moderate. The Executive Board's overall assessment is that the key policy rate should remain at today's level in the coming period.

At its meeting on 17 September, the Executive Board decided to keep the key policy rate unchanged at 1.5%. At the same meeting, the Executive Board decided that the key policy rate should be in the interval 1%-2% in the period to the publication of the next *Report* on 11 December 2014, unless the Norwegian economy is exposed to new major shocks.

Øystein Olsen
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