REGIONAL NETWORK

National report

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NORGES BANK

Weak outlook

According to Regional Network contacts, activity growth has slowed through autumn. Looking ahead, contacts expect lower activity owing to rapidly rising prices and costs, higher interest rates and a decline in new public sector orders. A far smaller share of enterprises now report capacity constraints, and the number of enterprises reporting difficulties in recruiting qualified labour has fallen. Nevertheless, more contacts than normal report capacity constraints and continue to describe the labour market as tight. The rise in prices is unusually high, but more than half of the contacts expect the rise to slow ahead. Contacts expect annual wage growth of 4.0% in 2022 and 4.2% in 2023.

Rapid rise in prices and reduced profitability

Over the past year, contacts have reported rapid and accelerating price increases, which have continued through autumn. In most sectors, prices are rising more than previously. More than half of the contacts expect a slower rise in prices in the coming year, and the share expecting the rise in prices in household-oriented sectors to pick up is the smallest share measured since the start of the time series in 2005. A number of contacts point out that electricity prices and freight rates, for example, have fallen recently. Moreover, some contacts expect that reduced domestic and global demand will curb the rise in prices ahead.

Profitability among contacts is considerably lower than a year ago, and the reduction is the most pronounced since spring 2020 (Chart 1). The decline in profitability is broadly based across sectors. Only oil service contacts report increased margins. Profitability has fallen the most in retail trade and construction.

Prospects for higher wage growth in 2023

Contacts expect annual wage growth in 2022 to be 4.0% (Chart 2), which is in line with the estimate in the previous survey. Contacts expect wage growth to rise to 4.2% in 2023. Oil services and manufacturing expect the strongest wage growth, 4.4%, while retail trade and construction enterprises expect the weakest, 3.9% and 4.0%, respectively. A large share of enterprises expect rapidly rising prices to push up wage growth in 2023, but several enter-

Chart 1. Overall profitability growth

Change in operating margin over the past three months compared to the same three months one year earlier. Percent

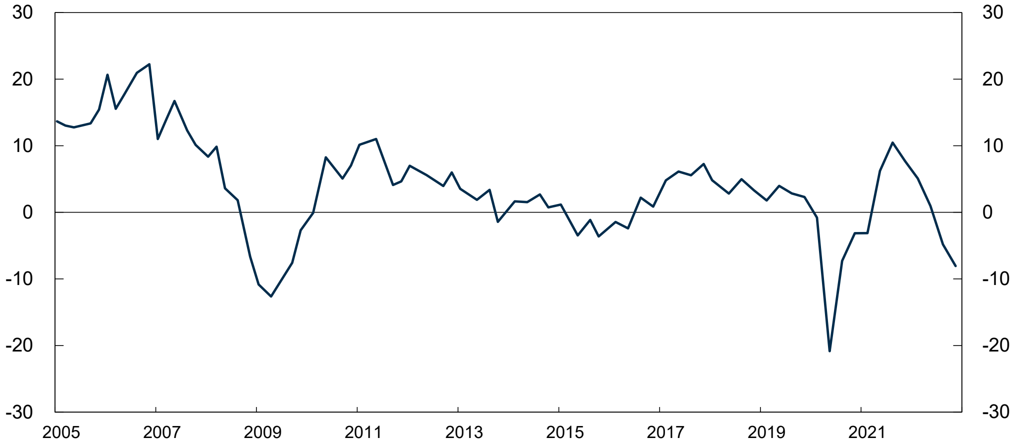
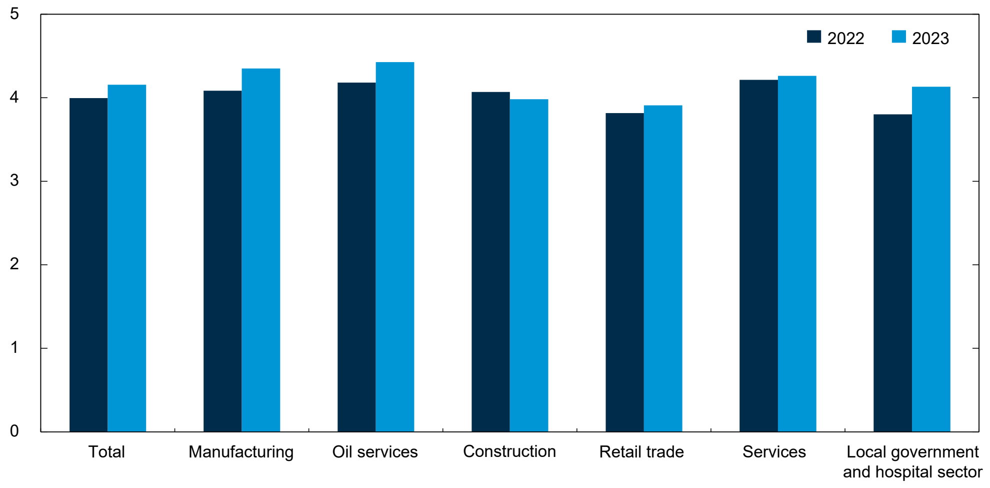


Chart 2. Annual wage growth
Expected annual wage growth. Percent



prises also point out that higher unemployment and an economic downturn will dampen the rise in wage growth.

Considerable uncertainty surrounding the effects of higher prices and costs
Enterprises report slowing activity growth through autumn (Chart 3). In retail trade and manufacturing, activity has fallen, while the pace of activity growth has picked up among oil service enterprises (Chart 4).

Contacts expect rapidly rising prices and costs, higher interest rates and a decline in new public sector orders to dampen activity through winter. Prospects are the weakest since January 2009. Many contacts describe the market as hesitant, and most describe the uncertainty as unusually high. However, in oil services, growth is expected ahead. In oil and energy, the willingness to invest is strong and order books are filling up.

Chart 3. Total output growth
Growth past three months and expected growth next six months. Seasonally adjusted. Annualised. Percent

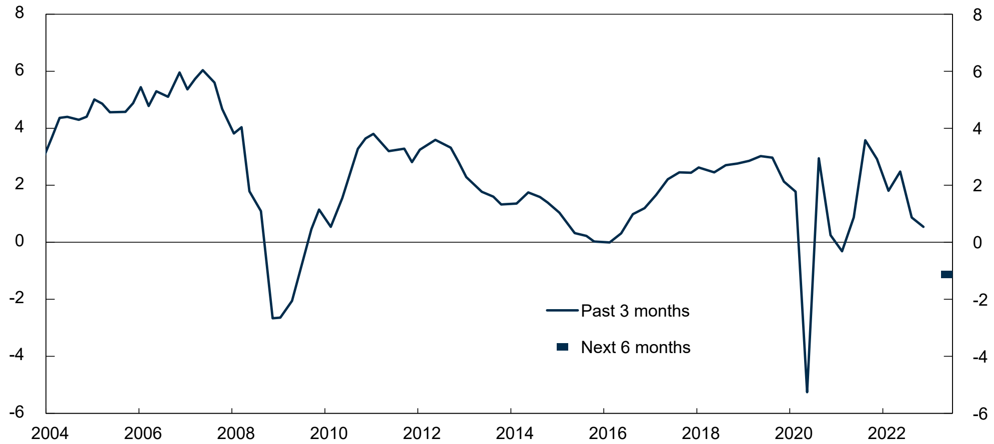
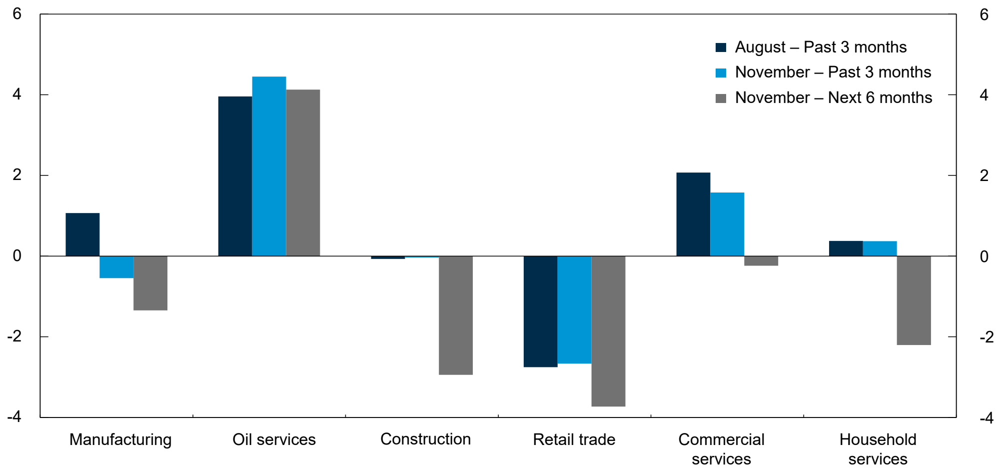


Chart 4. Output growth. All sectors
Growth past three months and expected growth next six months. Seasonally adjusted. Annualised. Percent



Weak order intake in construction

Recently, activity levels in construction have remained fairly stable, supported by large order backlogs. High construction costs and lower new home sales have resulted in project postponements and a fall in residential construction. A number of contacts also point out that fewer public sector projects have been announced. On the other hand, order intake related to the construction and renovation of commercial buildings continues to be solid. Construction enterprises expect activity to fall ahead owing to the overall slow addition of new projects through 2022.

Commercial service enterprises' order books have increased in autumn, but at a slower pace since August. Contacts expect a slight lull ahead. However, expectations vary considerably among contacts. Contacts in real estate, temporary staffing and marketing communication are among the most pessimistic, while contacts in, for example, IT and other types of consultancy services continue to expect fairly strong growth. Among contacts in tourism-related services, there is considerable variation in expected activity ahead.

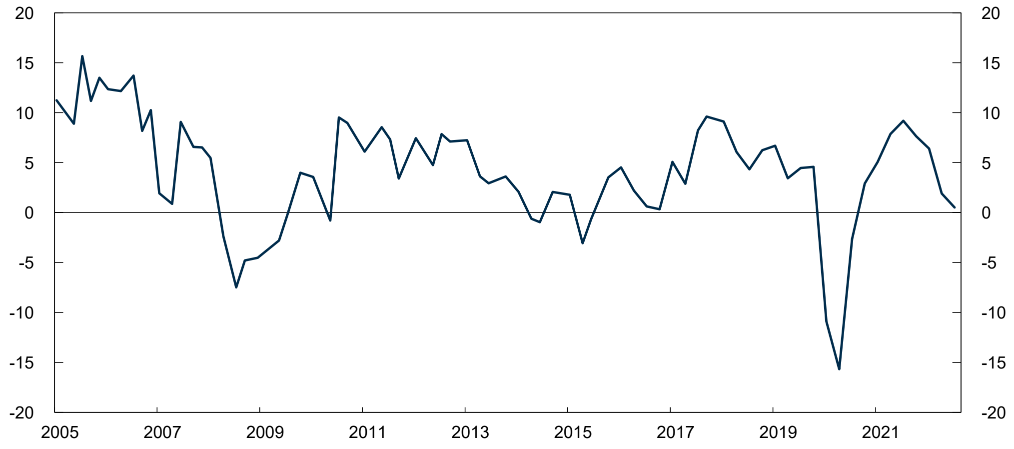
Prospects for lower household demand

Activity among household service enterprises has recently increased slightly, while retail trade turnover has fallen substantially. Households have continued to rotate consumption from goods back to services. Some contacts also pointed to increased cross-border and holiday-related shopping abroad. Moreover, some retail trade segments have observed a shift towards cheaper alternatives. Contacts in both services and retail trade expect lower household purchasing power to reduce demand ahead. A number of contacts do not expect to see the most pronounced effects until after the new year. A majority of retail trade contacts expect lower turnover volume in the next six months and only a few expect higher turnover volume. Services contacts' expectations are more widely dispersed. Some contacts believe that households continue to have pent-up demand for experiences and social events and will therefore tighten goods consumption more than services consumption. Others point out that much of services consumption, such as restaurant dining and travel, is easily forgone when households have to tighten their belts, and that services consumption will therefore be hit harder.

High activity in oil and energy

High oil and energy prices are fuelling substantial willingness to invest in oil and electricity production, which leads to solid growth for oil services and for export industry segments.

Chart 5. Investment growth
Expected growth next 12 months. Percent



Moreover, growth in oil services is being pulled up by the petroleum tax package. Contacts also expect solid growth ahead, but some fear that the proposed tax changes can lead to projects being shelved.

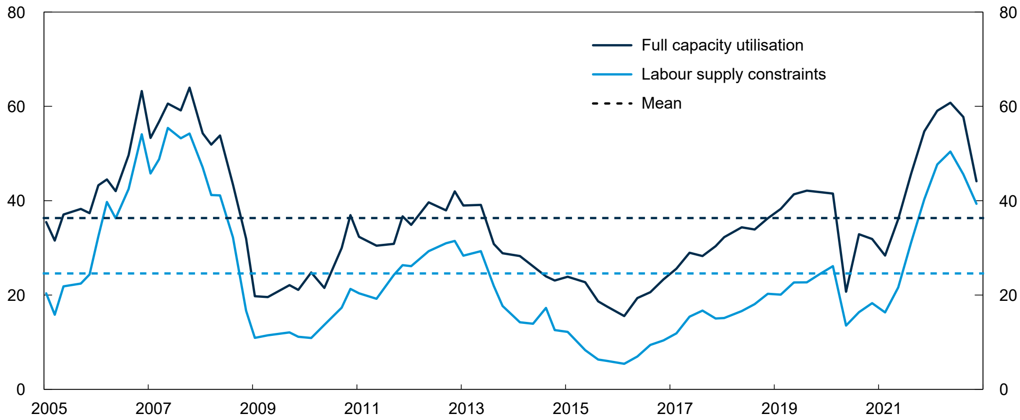
Contacts report declining manufacturing output. Developments are weakest in domestically oriented manufacturing, which particularly reflects reduced demand for building materials and a shift towards cheaper food. In addition, providers of services to the aquaculture sector report that a number of clients have postponed projects citing the new resource rent tax. A number of contacts expect elevated global inflation and the energy shortage in Europe to lead to an economic downturn in important export markets, which they expect will result in fewer orders for their own business too.

Stable investment levels ahead
Since the beginning of 2021, contacts have planned to increase investment in the coming 12 months (Chart 5). In this survey, contacts expect growth ahead to level off, reflecting the large investments already made by many enterprises over the past year. In addition, a number of enterprises have postponed investment plans citing uncertainty related to the rise in construction costs and developments in demand ahead. Oil service and manufacturing contacts are planning for increased investment ahead, while other sectors are planning for lower investment.

Lower capacity utilisation
Over the past year, high demand and supply problems have resulted in capacity constraints among an unusually high number of contacts (Chart 6). In spring, the share of contacts that reported capacity constraints reached the highest level since 2007, but declined somewhat in the previous survey. Over the course of autumn, the share has declined substantially, and fewer than half of contacts now report full capacity utilisation. The decline is broadly based across sectors and regions, but the share has declined most in construction (Chart 7). Only a few contacts now report difficulty obtaining intermediate goods, and a large share has increased capacity by augmenting their workforces over the past year. At the same time, a number of contacts are facing weaker demand growth. Even though the share of contacts reporting high capacity utilisation fell in autumn, the share is still higher than the historical average.

Fewer contacts are experiencing recruitment difficulties than reported in August, but the labour market continues to be tight. There is a substantial shortage of, for example, technical expertise and health workers, and recruitment difficulties are most pronounced in oil

Chart 6. Capacity utilisation[1] and labour supply constraints[2]
Percentage shares.

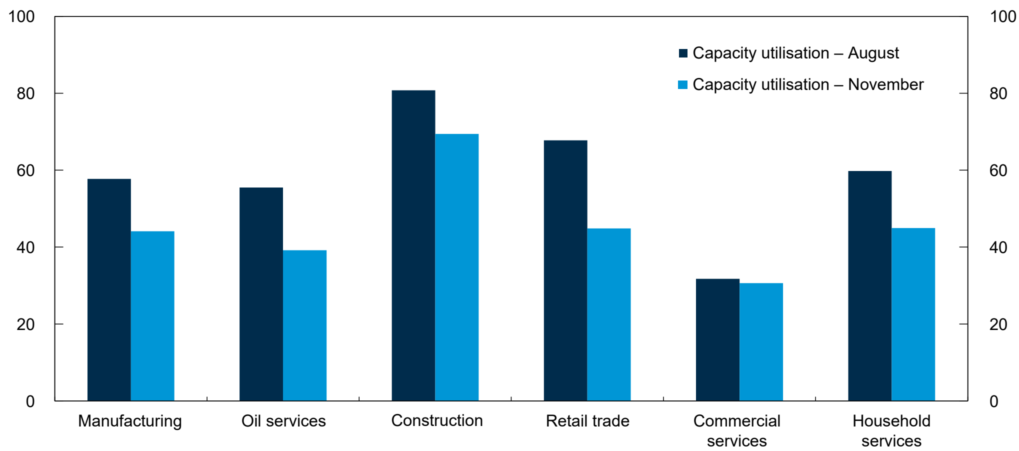


1) Share of contacts that will face some or considerable difficulty increasing output/sales without committing additional resources such as labour or machinery. 2) Share of contacts citing shortage of labour as a constraint on production/sales. The question about labour is asked only of the enterprises reporting full capacity utilisation, but the series shows the share of all contacts included in the interview period. The local government and hospital sector is omitted from the capacity utilisation series, but is, however, included in the labour force series.

services, local governments and hospitals. The indicator for labour shortages has therefore fallen less than the indicator for capacity utilisation, and the difference between them is the smallest measured since the start of the time series in 2005.

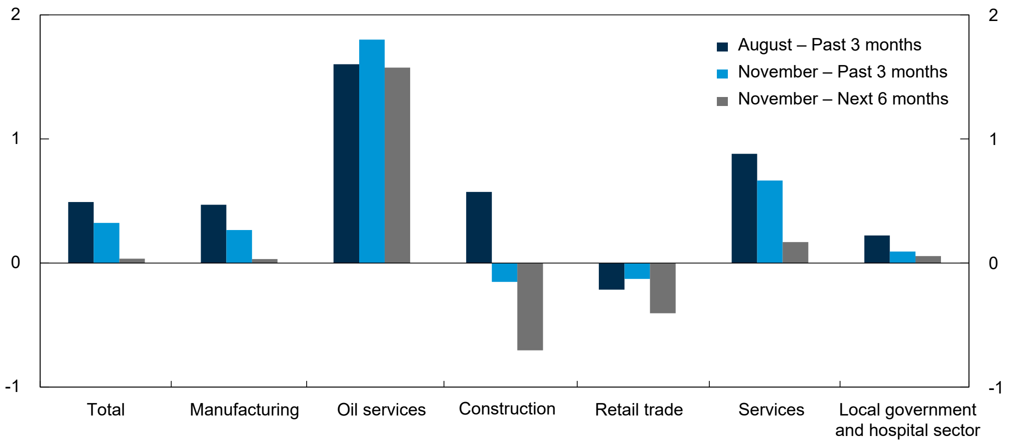
Contacts report that they have increased employment substantially since the beginning of 2021, and the increase in staffing has continued recently (Chart 8). Growth has slowed since the previous survey. High employment growth among oil service and service sector contacts is pulling up overall growth. In construction and retail trade, however, contacts have reduced their workforces. Retail trade and construction contacts are planning further downsizing, while oil service contacts are planning to further increase employment substantially. Overall, enterprises expect growth to level off over the next three months. Many enterprises report that they will assess the economic situation in the new year and only then decide whether they will have to reduce staffing.

Chart 7. Capacity utilisation[1]
Percentage shares.



1) Share of contacts that will face some or considerable difficulty increasing output/sales without committing additional resources such as labour or machinery.

Chart 8. Employment growth
Growth past three months and expected growth next three months. Seasonally adjusted. Percent



	This survey	Previous survey
OUTPUT AND DEMAND		
Output growth past three months (annualised percentage growth)		
Total	0.5	0.9
Domestically-oriented manufacturing	-1.6	0.4
Export-oriented manufacturing	1.0	2.1
Domestically-oriented oil service industry	4.4	3.9
Export-oriented oil service industry	4.5	4.1
Construction	0.0	-0.1
Retail trade	-2.7	-2.8
Commercial services	1.6	2.1
Household services	0.4	0.4
Expected output growth next six months (annualised percentage growth)		
Total	-1.1	-0.3
Domestically-oriented manufacturing	-2.3	-1.5
Export-oriented manufacturing	0.1	3.0
Domestically-oriented oil service industry	4.2	3.6
Export-oriented oil service industry	3.9	3.6
Construction	-2.9	-3.3
Retail trade	-3.7	-3.6
Commercial services	-0.2	1.1
Household services	-2.2	-0.7
LABOUR MARKET AND OUTPUT GAP		
Employment growth past three months	0.3	0.5
Expected employment growth next three months	0.0	0.2
Labour supply constraints	39.3	45.6
Full capacity utilisation	44.1	57.7
COSTS AND PRICES		
Estimated annual wage growth for current calendar year (percent)	4.0	4.0
Estimated annual wage growth for next calendar year (percent)	4.2	