Executive Board's assessment

Norges Bank's Executive Board has decided to keep the policy rate unchanged at 0.75%. The Executive Board's current assessment of the outlook and balance of risks suggests that the policy rate will most likely be increased in March 2019.

The expansion among Norway's trading partners has been solid in recent years. Unemployment has fallen, and wage growth has begun to rise. Economic growth now appears to be slowing. Since the September 2018 *Monetary Policy Report*, activity indicators have moved down, and there has been a broad decline in global equity markets. The projections for growth ahead have been revised down somewhat. Forward rates indicate a very gradual global interest rate rise, and policy rate expectations have fallen since September.

Growth in the Norwegian economy has been solid since autumn 2016, and the labour market has improved. The global upturn, higher oil prices and low interest rates have contributed to driving growth. There are prospects that the upturn in the Norwegian economy will continue, but slower growth abroad and a flattening of petroleum investment later in the projection period will likely pull down growth further out.

Growth in the mainland economy slowed in 2018 Q3 and was lower than expected. Much of the decline reflects a fall in agricultural production after the dry summer. Since the September *Report*, labour market developments have been broadly as projected. There has been strong growth in both employment and the labour force. Oil prices have fallen in recent months, with futures prices also lower than assumed in September. Lower oil prices reduce oil industry profitability, but there are still prospects for solid growth in investment on the Norwegian shelf in the coming year.

Consumer price inflation has risen over the past year. A substantial increase in electricity prices has contributed to the rise. Underlying inflation has also moved higher, driven in part by a pick-up in wage growth. Tighter labour market conditions suggest that wage growth will increase further.

Inflation has risen and been higher than projected in the September *Report*. In November, the 12-month rise in the consumer price index (CPI) was 3.5%. Adjusted for tax changes and excluding energy products (CPI-ATE), inflation was 2.2%. The krone exchange rate has depreciated and is weaker than expected. This will contribute to underpinning inflation in the near term. On the other hand, wage growth in 2018 appears to have been slightly lower than assumed in the September *Report*. The fall in oil prices suggests that wage growth may also be lower than projected in the period ahead.

Persistently high debt growth has increased household vulnerability. Household debt growth has abated somewhat in recent years, but remains higher than growth in disposable income. In recent months, house prices have fallen a little.

In its discussion of the risk outlook, the Executive Board focused in particular on global economic prospects. Through 2018, rising protectionism and political uncertainty have weakened growth prospects. Persistent trade conflicts and turbulence surrounding political processes in Europe may dampen growth among trading partners more than projected. If the UK exits the EU without a withdrawal agreement, financial market turbulence may increase. At the same time, the krone may remain weaker than envisaged should global uncertainty persist.

The target for monetary policy is annual consumer price inflation of close to 2% over time. Inflation targeting shall be forward-looking and flexible so that it can contribute to high and stable output and employment and to counteracting the build-up of financial imbalances.

In its assessment of monetary policy, the Executive Board gives weight to evidence of a continuing upturn in the Norwegian economy. Spare capacity has gradually diminished, and capacity utilisation now seems to be close to a normal level. Underlying inflation is close to the inflation target.

If the policy rate is kept at the current level for a long time, price and wage inflation may accelerate and financial imbalances build up. That would increase the risk of a sharp economic downturn further out. Raising the policy rate rapidly ahead could stifle the upturn and lead to higher unemployment and inflation that is too low. Uncertainty surrounding the effects of higher interest rates suggests a cautious approach to interest rate setting.

Overall, the outlook and the balance of risks imply a gradual interest rate increase in the years ahead. The policy rate forecast is little changed, but the fall in oil prices and weaker global growth prospects imply a slightly slower rate rise than in the September *Report*. Inflation is projected to remain close to target in the coming years, at the same time as unemployment remains low. The policy rate path will be adjusted in response to changes in economic prospects.

The Executive Board decided to keep the policy rate unchanged at 0.75%. The Executive Board's current assessment of the outlook and balance of risks suggests that the policy rate will most likely be raised in March 2019. The decision was unanimous.

Øystein Olsen
12 December 2018