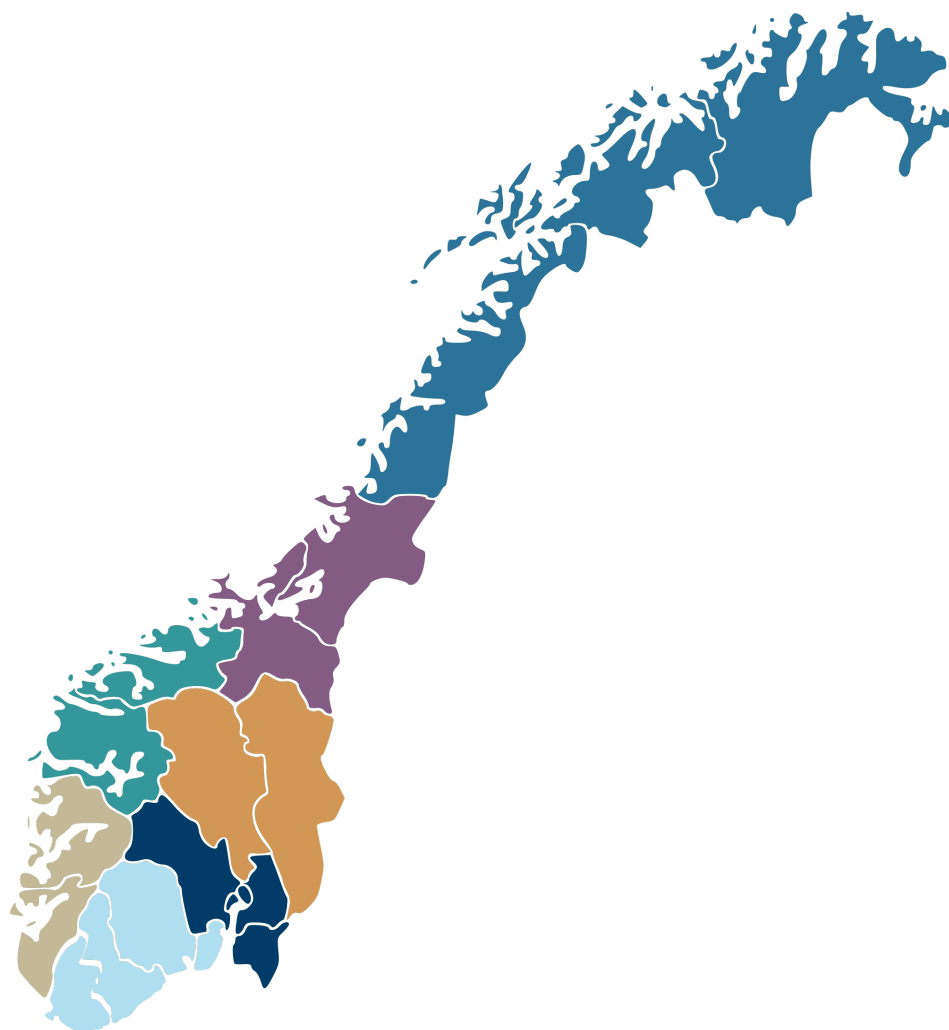


REGIONAL NETWORK

National report

NO. 1 | 2020

INTERVIEWS WERE PRIMARILY CONDUCTED IN THE PERIOD
27 JANUARY – 14 FEBRUARY



NORGES BANK

Growth has slowed further

According to Regional Network contacts, activity growth has continued to decline through winter. Weak demand from export markets, lower residential construction activity and reduced retail sales are having a dampening effect on growth. In addition, the completion of transportation and oil production projects are contributing to lower growth. Enterprises expect growth to continue to drift down in the next six months.

After the ordinary survey, the spread of coronavirus has increased. A second phone survey of a sample of contacts was therefore conducted. The new information from the phone survey is not included in the published figures. The outbreak and the measures to contain it appear to have consequences for large segments of the business sector, inter alia in the form of reduced demand and delays in goods deliveries. Over a third of enterprises participating in the phone survey have revised down their growth outlook in recent weeks.

Activity growth among Regional Network enterprises picked up between spring 2016 and summer 2019 (Chart 1). Growth slowed through autumn and has continued to weaken this winter. Over the past three months, activity increased by an annual rate of 1.8%, down from 2.1% in the previous survey. Growth is slightly weaker than contacts envisaged in November, but close to the average for the period between the financial crisis in 2008 and the present. Growth has slowed most in the export industry, construction and oil services, and turnover volume in retail trade has declined further (Chart 2). The services sector continues to show solid growth.

Overall, enterprises also expect slightly lower growth in the next six months. Oil service and service sector contacts expect growth to slow. Manufacturing and construction contacts expect somewhat higher growth and retail trade enterprises expect turnover to level off.

Employment growth has been high over the past two years, but slowed slightly in the second half of 2019 and has shown little change since November. Oil service and service sector enterprises have increased their workforces most, while the number of employees in retail trade has continued to decline. Enterprises do not expect substantial changes in employment growth through spring.

The ordinary interview period was 27 January to 14 February. A number of contacts then feared a further spread of coronavirus could reduce demand and the supply of goods, but activity had not yet been much affected.

Extraordinary phone survey

In the phone survey conducted in the period 4- 6 March, 82 enterprises were interviewed, and all sectors were represented. The latest information suggests that the virus outbreak will weigh on activity in the Norwegian business sector ahead. Over a third of enterprises participating in the phone survey have revised down their growth outlook in recent weeks. Of these, more than half are already being adversely impacted by the outbreak and the measures to contain it. So far, reduced travel activity and fewer customers in shops are having had the greatest dampening effect on activity, but delayed deliveries

Chart 1

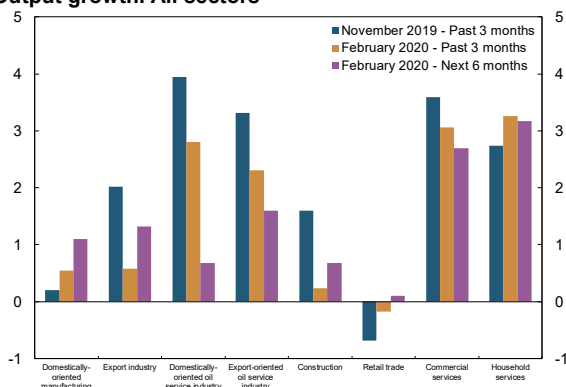
Total output growth



Growth past three months and expected growth next six months. Seasonally adjusted. Annualised. Percent.

Chart 2

Output growth. All sectors



Growth past three months and expected growth next six months. Seasonally adjusted. Annualised. Percent.

are also a growing challenge. Many contact enterprises are worried that higher sickness absence could weaken growth further ahead. The coronavirus outbreak has resulted in higher costs for a number of contacts. For example, reduced transport capacity has led to higher prices for freight. There is considerable uncertainty regarding the duration of the outbreak, and a number of contacts have implemented temporary hiring freezes. Few enterprises are planning workforce reductions, but some mentioned the possibility of layoffs.

A large number of homes and transport development projects have been completed

In *construction*, activity has been solid in recent years, with growth sustained in particular by residential construction and public investment (Chart 3). Growth has slowed from autumn 2019, but enterprises believe it will pick up slightly through spring. Since summer 2019, many transport development projects have been completed, while the launch of large projects such as the Rogaland Fixed Link, the Ringerike Line and the Fornebu Line have been postponed. Moreover, a number of contacts report that the transfer of responsibility from the Norwegian Roads Administration to local government authorities has resulted in postponements and lower levels of activity for many construction contractors. Residential construction activity has slowed, reflecting the large number of housing completions in 2019 and a reduction in housing starts. In the central part of Region East, the shortage of land available for construction is having a dampening effect on housing starts, while the uncertainty regarding the future of the oil sector is influencing the housing market in western Norway. On the other hand, activity in commercial building construction and maintenance is increasing. Public building projects continue to be the main contributors to growth, and hospital construction will be important for activity ahead. In addition, the need for large warehouses with automated solutions is increasing, while investment in brick-and-mortar retail properties is declining. This development reflects the increase in online shopping and the need for greater efficiency in retail trade.

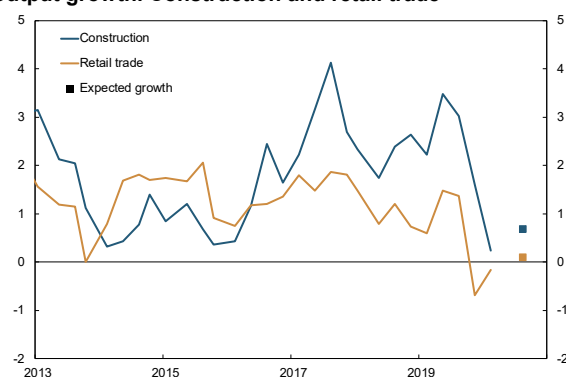
Lower demand in retail trade

In autumn 2019, turnover in *retail trade* fell for the first time in over ten years (Chart 3). Through winter, it fell slightly further, but higher car sales following the turn of the year cushioned the decline. New emissions standards for European car manufacturers led to postponements of a number of electric vehicle deliveries between 2019 and 2020. Recycling and border trade are growing challenges for many retail trade enterprises. Moreover, the mild winter has reduced sales of seasonal goods such as sporting goods and clothing, but it has also had a positive impact on turnover of certain goods for indoor use, such as electronics and furniture. None of the enterprises interviewed in the ordinary survey had noticed any consequences of the coronavirus, although a number of contacts expressed concern regarding the availability of goods in the event the virus spreads further.

In *commercial services*, growth has been strong over the past years, but slowed slightly through autumn 2019 (Chart 4). Growth continued to slow in recent

Chart 3

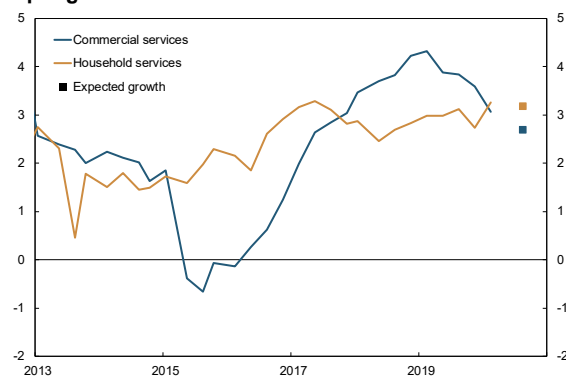
Output growth. Construction and retail trade



Growth past three months and expected growth next six months. Seasonally adjusted. Annualised. Percent.

Chart 4

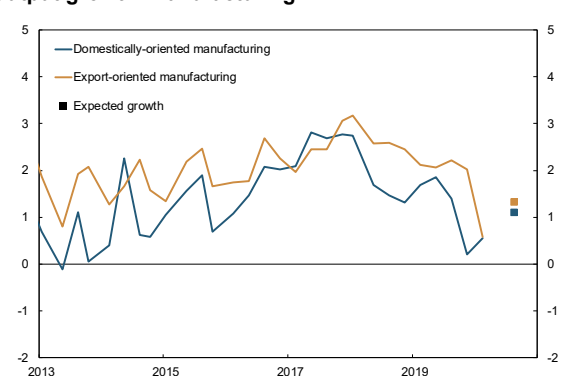
Output growth. Services



Growth past three months and expected growth next six months. Seasonally adjusted. Annualised. Percent.

Chart 5

Output growth. Manufacturing



Growth past three months and expected growth next six months. Seasonally adjusted. Annualised. Percent.

months and enterprises also expect weaker growth ahead. Substantial changes, such as digitalisation and addressing climate issues, continue to increase the need for consulting services. At the same time, lower levels of activity in transport development and residential construction have a dampening effect on demand for construction-related services. A number of contacts also point out that some Norwegian enterprises have become more cost-conscious and cautious about purchasing services. This also amplifies the trend of offshoring certain tasks. At the time of the interviews, most contacts felt little effect of the corona outbreak, although some expressed concern that consequences of the virus could be substantial through spring. This pertained especially to contacts in the travel and transport industries.

Trade conflicts are dampening growth

Growth in the *export industry* has been solid in recent years. Growth remained elevated through most of 2019 but in the past three months has been at its weakest since autumn 2009 (Chart 5). A number of export enterprises have been adversely affected by tariff barriers and weaker growth among many trading partners. Several also cite the potential for growth to weaken further if measures to contain the spread of the coronavirus curb demand from important export markets or limit the supply of intermediate goods. Nevertheless, export enterprises expect growth to edge up again in the next six months. Enterprises that are focused on the green transition or digitalisation are the most optimistic.

In *domestically-oriented manufacturing*, growth has picked up slightly but remains weak. The mild winter has curbed growth in the output of seasonal goods. Enterprises continue to cite weaker demand from parts of the construction sector, while higher activity in residential and commercial building renovation pulls in the opposite direction. Some contacts are also experiencing greater demand for domestically produced goods owing to greater focus on sustainability.

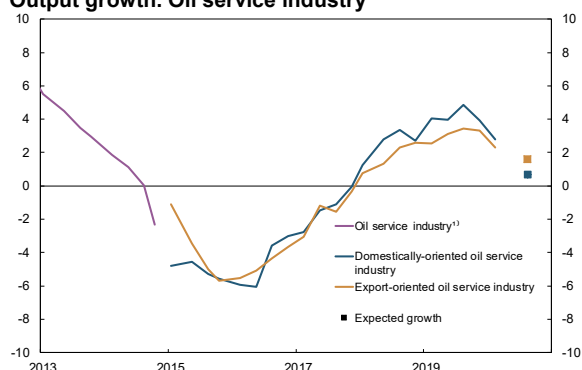
Over the past two years, the *oil service sector* experienced sharp growth (Chart 6), but since autumn 2019, growth has slowed in both domestic and export markets. The completion of large construction projects is weakening growth in the domestic market, but at the same time, increasing drilling activity entails a greater need for maintenance and modification. In the export market, subsea development activity is increasing. On the other hand, the low number of new rigs and offshore ships is having a dampening effect on growth. The market remains characterised by considerable surplus capacity and a large number of laid-up vessels. Some contacts are experiencing growth specifically related to the renovation of older ships and rigs.

Stable capacity utilisation

The indicator for enterprises' capacity utilisation shows the share reporting the inability to increase sales or output without committing additional resources such as labour or machinery. The indicator rose gradually from the cyclical trough in 2016 but has shown little change since spring 2019 (Chart 7). The most pronounced capacity constraint is the shortage of labour, which has amplified over the past year.

Chart 6

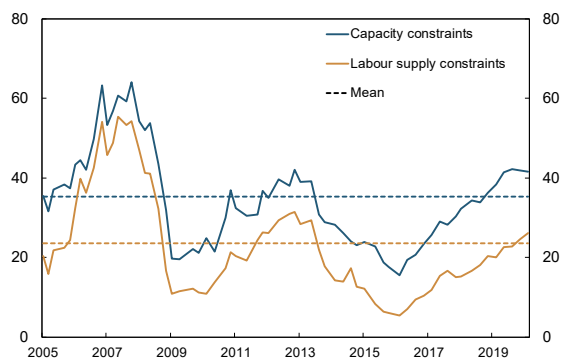
Output growth. Oil service industry



Growth past three months and expected growth next six months. Seasonally adjusted. Annualised. Percent. 1) Terminated series (2003-2014).

Chart 7

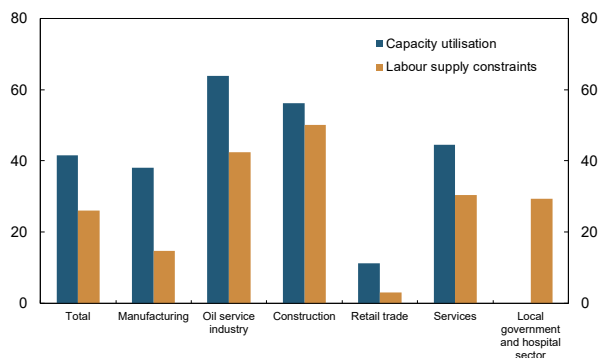
Capacity utilisation¹⁾ and labour supply constraints²⁾



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.

Chart 8

Capacity utilisation¹⁾ and labour supply constraints²⁾ All sectors



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.

Capacity utilisation remains highest among oil services and construction contacts (Chart 8). Capacity utilisation in the oil service sector picked up through 2019 but has fallen slightly in recent months. Owing to weaker growth and lower order intake among many oil service contacts, the need for new hiring has recently declined slightly. Enterprises are nevertheless concerned that uncertain future prospects are making it difficult for the sector to recruit, particularly among youth.

Capacity utilisation in construction has remained stable at a high level since spring 2019. Enterprises report a slightly greater shortage of labour in recent months and that difficulty recruiting experienced project managers and those with vocational training remains the main challenge. Some enterprises also report that the weak krone may have made it less attractive for foreign construction workers to work in Norway.

The shortage of IT skills continues to restrain growth among enterprises, particularly in services. For many enterprises, it is also a restraint on efficiency and business development.

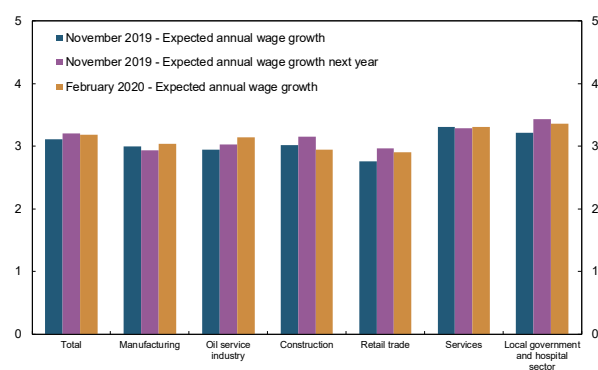
Unchanged wage expectations

Tighter labour market conditions in recent years have boosted wage growth among contacts. In 2020, contacts believe wage growth will be around 3.2% (Chart 9), unchanged on their estimate from November.

In retail trade, the rise in prices has shown little change in recent months. Over the past year, there have been substantial krone exchange rate movements that resulted in higher purchasing costs for most retail trade enterprises. However, strong competition makes it difficult to raise prices. This has resulted in reduced profitability for many, and a majority of enterprises will therefore increase prices further in the coming year. In household services, the rise in prices has picked up slightly since autumn, but enterprises do not expect any substantial change in the rise in prices ahead.

Chart 9

Expected annual wage growth



Expected annual wage growth. Percent

TABLE 1 Economic Indicators

	This survey	Previous survey
Output and demand		
Output growth past three months (annualised percentage growth)		
Total	1.8	2.1
Domestically-oriented manufacturing	0.6	0.2
Export industry	0.6	2.0
Domestically-oriented oil service industry	2.8	3.9
Export-oriented oil service industry	2.3	3.3
Construction	0.2	1.6
Retail trade	-0.2	-0.7
Commercial services	3.1	3.6
Household services	3.3	2.7
Expected output growth next six months (annualised percentage growth)		
Total	1.7	1.9
Domestically-oriented manufacturing	1.1	1.2
Export industry	1.3	1.6
Domestically-oriented oil service industry	0.7	2.6
Export-oriented oil service industry	1.6	2.9
Construction	0.7	0.1
Retail trade	0.1	-0.3
Commercial services	2.7	3.3
Household services	3.2	2.9
Labour market and output gap		
Employment growth past three months	0.3	0.3
Expected employment growth next three months	0.3	0.2
Labour supply constraints	26.1	24.5
Capacity constraints	41.5	41.8
Costs and prices		
Estimated annual wage growth for 2020	3.2	3.2