EXECUTIVE BOARD'S ASSESSMENT

At its meetings on 3 June and 17 June 2015, the Executive Board discussed the monetary policy stance. The starting point for the discussion was the strategy that the Executive Board adopted at its meeting on 18 March 2015 and the analysis in the March 2015 *Monetary Policy Report*. The analysis in the March *Report* implied a key policy rate of around 1% over the coming years. With this path for the key policy rate, there were prospects that inflation would edge up in the coming quarters and thereafter remain a little higher than 2% through the projection period. Capacity utilisation was projected to decline in the coming period, but to move up to a normal level towards the end of the projection period. At the monetary policy meeting on 6 May, the key policy rate was left unchanged. At the same time, the Executive Board was of the view that there were prospects that the key policy rate would be lowered in June.

Global economic developments have so far been slightly weaker than expected in March, but there are still prospects that growth will gain some momentum ahead. In many countries, inflation is very low, partly owing to the fall in oil prices and low wage growth. Policy rates are still close to zero in many of our trading partner countries. Market expectations concerning foreign policy rates in the coming period have shown little change. There have been wide swings in global long-term interest rates in recent months. On the whole, they have risen somewhat since March, but rates are still low. In addition to keeping policy rates at a low level, a number of central banks are buying securities to ease monetary policy further. Monthly bond purchases by the European Central Bank (ECB) have amounted to EUR 60bn since March, and Sveriges Riksbank has increased its purchases of government bonds in recent months.

Foreign exchange markets appear to be reacting more strongly than normal to news about economic developments and monetary policy both in Norway and other countries. So far in Q2, the krone exchange rate has on average been on a par with the March projection, but has weakened in recent weeks.

Oil prices have recently varied between USD 60 and 65 per barrel and are somewhat higher than anticipated in March. Growth in the supply of oil is moderating and there are signs of rising oil demand. At the same time, oil inventories are at historically high levels. Oil futures prices reflect expectations of a further, albeit modest, increase in oil prices.

New information on activity in the Norwegian economy indicates that growth has been a little weaker than projected and that the prospects ahead have weakened somewhat. Consumption remains steady, but business investment has declined. Growth in housing investment has been lower than expected. In May, the enterprises in Norges Bank's regional network reported slower output growth, with expectations of continued weak growth ahead and a weaker outlook than in January. Expectations have in particular weakened in the oil service sector and in the commercial services industry. Further out, there are now prospects that the decline in oil investment will be less pronounced than envisaged in March.

As expected, unemployment has edged up. While registered unemployment has increased in line with the projections in the March *Report*, LFS unemployment has risen to a further extent. A flexible labour supply in Norway is helping to curb the rise in unemployment. There are signs that foreign labour inflows into Norway are declining in pace with slower growth in the Norwegian economy. Unemployment is nonetheless expected to edge up in the period ahead.

This year's wage settlement indicates that wage growth may turn out to be somewhat lower than previously anticipated. A need for restructuring, combined with a relatively high cost level in Norway, may result in moderate wage settlements in the years ahead too.

Consumer price inflation has varied between 2% and 2½% in recent months. Prices for domestically produced goods and services have risen at a slower pace than projected, while prices for imported consumer goods have risen faster than projected in the March *Report*. The pass-through from the krone depreciation in autumn 2014 appears to have occurred a little earlier than expected. The krone depreciation is expected to push up the rise in prices for imported consumer goods further in the period ahead. Lower wage growth and fading effects of a weaker krone will dampen inflation ahead.

Since the beginning of the year, banks have reduced their lending rates a little more than expected in March. At the same time, the premium in the Norwegian money market has increased and been somewhat higher than expected.

House price inflation has moderated in recent months, but there are wide regional variations. Household debt is still rising faster than income. The low interest rate level is contributing to sustaining the rise in house prices and debt. On the other hand, somewhat weaker economic developments in the Norwegian economy and government measures relating to bank lending practices may help curb house price inflation and household debt accumulation.

The Executive Board notes that the analyses in this *Report* show that the outlook for the Norwegian economy is weaker than in March. The effects of lower oil prices and weaker demand from the petroleum industry appear to be somewhat more pronounced than assumed earlier. The analysis implies a key policy rate forecast of a little higher than ¾% in the coming year, followed by a gradual rise.

In its discussion of monetary policy in the period ahead, the Executive Board gave weight to the fact that growth prospects and the forces driving inflation further ahead have weakened. Both the objective of keeping inflation close to target and the aim of sustaining capacity utilisation in the years ahead imply a lower key policy rate. On the other hand, a lower interest rate may fuel house price inflation and debt growth. An overall assessment led the Executive Board to conclude that the key policy rate should now be reduced.

At its meeting on 17 June, the Executive Board decided to lower the key policy rate by 0.25 percentage point to 1.0%. The Executive Board's current assessment of the outlook for the Norwegian economy suggests that the key policy rate may be reduced further in the course of autumn.

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