

NHO's Economic Report

Spring 2008

Published 22 May 2008

Table of Contents	
Key Points:	2
An economy in a class of its own	3
Forecasts for 2008 and 2009	7

Key Points:

The NHO's Economic Survey

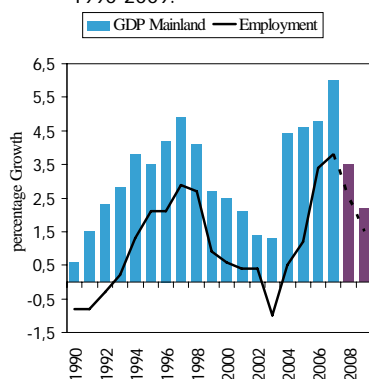
- The current market situation is still regarded as good. ICT enterprises and enterprises belonging to the petroleum cluster are the ones that are the most satisfied. The expectations for 2009 are weaker. In particular the construction industry expects a weaker market in 2009 than in 2008.
- For 2008 the growth in labour demand for the NHO member companies is reduced from 2.7 percent to 2.4 percent for the entire NHO area. For next year, the growth in labour demand is estimated to 1.7 percent. Even the construction industry, where the market outlook is extremely uncertain, reports an increased demand for labour in 2008.
- Fewer enterprises report that a shortage in labour limits their production, but the percentage is still high. The number of unfilled vacancies constitutes 6.4 percent of the number of employed persons. This is somewhat lower than what the responses from last autumn indicate.
- A steadily growing percentage of enterprises use foreign labour. The use of foreign labour increases also in 2009.
- 35 percent of the respondent NHO member companies are negatively or very negatively affected by a stronger Norwegian krone. For the industry sector this percentage constitutes as much as 60 percent.
- The majority of NHO member companies states that a flexible labour market constitutes a very important framework condition. Depreciation rules and removal of the wealth tax are also given high priority. The industry sector points to secure access to energy and a competitive exchange rate for the krone as vital framework conditions.
- Improving employee competencies is the most important long-term challenge for the NHO member companies followed by considerations related to concentrating their efforts on core activities. Upgrading technology is also given high priority.
- Ten percent of the enterprises state that financial market developments create problems for their investments. For the construction and tourism industry, the percentage is even higher.

The Norwegian economy in a class of its own

- Despite the economic cyclical downturn in the US, and in time in Europe, the Norwegian economy continues to grow both in 2008 and in 2009.
- Continued high growth in China and India contributes to that Norwegian export prices for energy are kept up. However, the strong krone still contributes to falling export prices measured in Norwegian kroner.
- The demand for labour will increase both in 2008 and 2009. The labour demand is growing stronger than the domestic workforce.
- If we are to avoid that the pressure on the Norwegian labour market becomes too great, workforce participation for all groups must increase. At the same time, access to foreign labour must be good.
- Despite the decline in the construction of new residential buildings, a labour shortage still exists in the construction industry due to high activity in the construction of commercial buildings.
- A stronger wage growth combined with a strengthened krone serve to create major challenges for the cost-related competitiveness, resulting in an extensive need for restructuring, in particular in the internationally exposed sectors.
- When the petroleum investments on the Norwegian continental shelf fall, industrial employment may stagnate yet again, causing regional pockets of unemployment to emerge.
- Automatic use of the fiscal rule relating to petroleum revenue spending over the state budget, with the high oil prices will provide too strong a stimulus. Increased operational costs will require more labour than expenses for investments.
- The profile of the 2009 state budget should be characterised by the need to stimulate labour supply and the economy's capacity for growth. In particular investments in competence and infrastructure should be granted priority.

An economy in a class of its own

High Activity also in 2008
GDPP mainland and employment growth
1990-2009.



Source:
Statistics
Norway

Based on the responses provided by the enterprises in the NHO's Economic Survey, there is much to indicate that for both 2008 and 2009, we will have a labour market where temperatures will remain high. It may seem like the Norwegian economy will develop differently than the economies of other European countries. The construction activity will remain on an overall high level, even if there is a moderate decline in the construction of new residential buildings. Large accumulated order reserves combined with a shortage of labour serve to create a delay mechanism which will ensure that that the activity level is kept up also in 2009. Moreover, the high oil prices result in strong growth in oil-related sectors. The order situation for shipyards is still good. The income situation for households is developing well and continues to provide strong growth impulses as far as domestic demand is concerned. The financial situation for the state is improving significantly due to high oil prices. Domestic demand is expected to compensate more than adequately for the reduced pulling power from the export markets.

Behind us is a period of historically strong growth in the Norwegian economy. During this period, the annual economic growth in the mainland economy has been nearly five percent. Measured in net worth, 200,000 new jobs have been created and the unemployment rate has decreased from 4.5 percent to 2.5 percent. According to preliminary national accounts figures, the employment rate has increased by 3.7 percent in 2007. A more moderate growth is expected both for the current year and for 2009, but even in 2009, the growth in labour demand may seem to increase by 1.5 percent. This is above the growth in the labour force, and thus, the use of foreign labour is expected to increase also in the time ahead.

The Norwegian economy in a class of its own			
	2007	2008	2009
Gross Domestic Product			
Norway	6	3 1/2	2 1/4
The Euro Zone	2,6	1,4	1,2
The US	2,2	0,5	0,6
China	11,4	9,3	9,5
Consumer Prices			
Norway	0,8	3	2 1/2
The Euro Zone	3,1	2,2	1,7
The US	4,1	2	2,1
Unemployment Rate			
Norway	2,5	2 1/4	2 1/4
The Euro Zone	7,4	7,1	7,2
The US	4,6	5,3	5,7

Source IMF,CF, Statistics
Norway; NHO

The correction of the US economy which economists have predicted this year, has been driven by a strong increase in American consumers' loan-financed spending spree. As long as your credit rating is good, there is nothing wrong with taking up a loan, but when housing prices fall resulting in that the value of houses becomes lower than their outstanding debt to an increasing number of families, that's when problems arise. Banks run into losses, which in an almost astonishing way has managed to supplant themselves to all parts of the world's financial markets. Even in Norway, we find that there is a price to pay for taking risks. The money market rate has at times been one percentage point higher than the key interest rate stipulated by Norges Bank.

While the fall of the stock exchange reduces private consumption in other countries, this type of effect will have less of an impact in Norway. Last year, private consumption in Norway increased by nearly 7 percent, and was a major driving force behind the strong growth in the Norwegian economy. The gross domestic product for the Norwegian mainland economy increased by 6 percent from 2006 to 2007 which to a well developed economy constitutes a very strong growth. Behind this

strong figure for private consumption is a strong wage growth of 5.4 percent combined with a price growth of just 0.8 percent. In other words, the purchasing power of Norwegian households experienced a very strong growth, with good help from cheap imports from China, and not least reduced electricity bills due to plentiful water reservoirs. In addition, the number of wage recipients increased by 3.7 percent from 2007 to 2008. Also for this year, the income situation for Norwegian households will be decisive in determining the fate of the Norwegian economy. With a wage bargaining result for the private sector of 5.6 percent in annual wage growth for 2008, an a presumed price increase of 2.5 to 3 percent, the purchasing power for each individual household is set to increase strongly also next year. The employment growth for 2008 however will be somewhat more moderate. The growth in private consumption for 2008 is estimated at approximately 4 percent. Further decline in housing wealth along with the distant after-effect of an increased Norwegian interest rate level may lead to reduced consumption and a greater degree of household pessimism.

There are particularly two questions that come to mind in connection with the US cyclical downturn. How will the spillover effect affect the rest of the world economy, and how-long will it take to restore the balance of both the US economy and the world economy? With regard to the last question, the strong decline in the international value of the US dollar which has already occurred has already provided a significant contribution towards restoring the competitiveness of the US economy. We are likely to see the result of this pretty soon. German BMW has already decided to relocate its car production from Europe to the US. But when regime like China does not allow their currency to reflect the strength of their economy, the picture becomes all wrong. Although the Chinese currency yuan has been somewhat strengthened against the US dollar, compared to the euro for instance, the Chinese currency has been weakened despite the fact that China has a considerable trade surplus vis a vis Europe. Both as a result thereof and due to the fact that Europe is loosing market pacing from the US, there is a risk that the European downturn will be more extensive and long-lived than what forecasts currently indicate. The Consensus Forecasts for May showed a GDP prognosis for 2008 of 1.5 percent for the euro area. As Europe thus is confronted with significant competitive challenges from both the East and the West than what forecast makers currently predict. Neither is it possible to rely on the same pulling bower from the former East European countries whose growth outlook is far weaker. The IMF has estimated the GDP growth for the euro area to 1.2 percent for 2009.

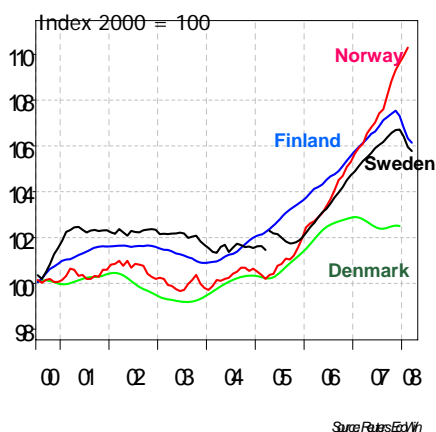
During the last four to five years, Norway has profited hugely on globalisation. The strong growth in China, India and the former Eastern Europe has resulted in an extra price boost for energy, semi-finished products and raw materials. In addition we have mostly enjoyed the benefits and not so much the competition resulting from Chinas massive mobilisation of labour in the battle for the world's labour-intensive goods production. Increased export prices along with in part, falling import prices have increased Norway's disposable income considerable in recent years. The development trend has given Norwegian households a particular boost in purchasing power, but also corporate investment capacity has risen significantly due to good results. The

Norwegian state finances have been given a particularly strong boost due to high oil prices. Interest rate increases do not have the same bite when the income effects on the economy are this strong. There is a good chance that export prices for Norwegian export of goods and services will remain high. The IMF predicts that the growth in China will remain high with an approximate GDP growth of 9 percent for both 2008 and 2009. Correspondingly, India is expected to grow by approximately 8 percent both years. There is much to indicate that world market prices for energy and raw material will remain at high levels also in 2008 and 2009. In addition increased need for transport and in particular sea transport results in good rates within the shipping industry and a good order situation for both Norwegian shipyards and for producers of ship equipment. It may look like the Norwegian economy won't be as severely affected by the world economic turmoil as the rest of Europe.

The pro-longed high temperature of the Norwegian economy has resulted in a record-high growth in labour demand. In November of 2007, the number of unfilled vacancies equalled 8 percent of the positions in the NHO member companies. There are currently fewer enterprises which report that labour shortages limit their production. The number of unfilled vacancies has decreased somewhat since the last survey, but nonetheless equals 6.4 percent of the employment among NHO member companies. The demand for labour has also been adjusted downwards for 2008, but only marginally from a growth of 2.7 percent to 2.4 percent. Also for 2009 the enterprises expect that they will need to increase their staff. Even the construction industry where next year's market outlook is being characterised as very uncertain reports of increased recruitment needs also for 2009.

For a long time, the Norwegian wage growth was relatively moderate in an early phase of this cyclical upturn. But last year, the annual wage growth in Norway was 5.4 percent, or one percentage point higher than what the LO and the NHO had envisioned during the wage adjustments in the spring of 2007. In 2007, the annual wage costs for the Norwegian industrial worker were 41 percent higher than those of their competitor countries. In 2004 the Norwegian cost disadvantage equalled 30 percent. This development trend serves to illustrate that the prolonged economic upturn has provided the Norwegian private sector with a challenge in relation to costs vis a vis the outside world which may turn out to be challenging to handle when the competition heats up in the event of a possible cyclical downturn towards the end of 2009 and in 2010.

An economy in a class of its own
The development trend for employment for the Nordic countries

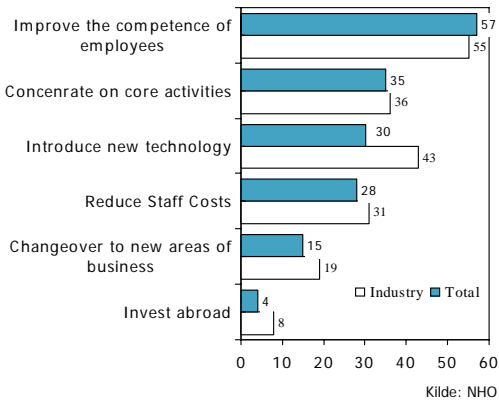


With an adopted wage settlement proposal for the private sector of 5.6 percent for 2008, the Norwegian competitiveness will be further weakened from 2007 to 2008. Based on the technical assumption that the exchange rates we had in April 2008 remain constant for the remainder of the year, the hourly wage costs for workers will be almost 50 percent higher than those of our trading partners on average for 2008. Handling a situation given the strong pressure on the exchange rate for the krone as we have had for parts of this year will be very demanding. Given the bright outlook as regards continuous high oil prices, it is important to avoid increased interest rate differentials

between Norway and other countries.

Enterprises participating directly or indirectly in the international market competition have developed a pressing need for increasing their competitiveness in other ways than competing on the basis of high Norwegian hourly wage costs. The cost disadvantage will for instance be reduced by opting for a changeover to highly skilled labour. The knowledge worker is not as expensive in Norway compared to other countries as less competent labour. Increased knowledge content therefore serves to improve competitiveness. The responses provided in the NHO's Economic Survey show that a clear majority holds the opinion that improving the competence of their employees is the most important long-term challenge for enterprises. But upgrading technology is also seen as an issue to which the enterprises themselves find important to grant priority in a time of strongly increasing hourly wage costs.

The most important challenges in relation to restructuring – as enterprises see it
– % who see it as very important



Given the labour market situation outlined in this report is necessary for the Norwegian fiscal policy to have a dampening effect on Norwegian demand also in 2009. Automatic use of the fiscal rule for petroleum revenue spending over the state budget, with the high oil prices we have had and probably will continue to have, will provide far to strong a stimulus to the economy. Increased public operating costs will require more labour than expenses for investment according to the Research Department at Statistics Norway. In a situation characterised by a shortage of labour petroleum revenue spending should therefore be directed towards investment rather than operating costs. The state budget profile for 2009 should be characterised by the need to stimulate to increased labour supply and increased growth capacity for the economy.

Forecasts for 2008 and 2009

	2007	2008				2009		
	SSB	SSB	NB	Fin	NHO	SSB	NB	NHO
Private Consumption	6,4	3,9	3 1/2	3,7	4	3,2	1 3/4	3 1/4
Public Consumption	3,2	3,2	2 3/4	3,2	3 1/2	3	3 1/4	3 1/4
Gross Fixed Investments	9,6	3,5	..	4,8	4 1/2	1,1	..	1 3/4
Petroleum Activities	6,6	7,6	7 1/2	10	5	6,3	5	5
Mainland Norway	9,2	2,6	5 1/4	3,4	4 1/2	-0,5	3/4	1
Enterprises	13,2	6	..	7	8	0,5	..	3
Housing	6,3	-2,7	..	-4	-2	-4,5	..	-5
Public	4,1	1,9	..	5,4	6	2,5	..	4
Demand from Mainland Norway	6,1	3,5	3 3/4	3,5	4	2,5	2	2 3/4
Exports	3,2	0,4	..	2,4	1 1/2	1,2	..	1
oil and gas	-2,4	-3,4	..	-0,2	0	1,4	..	2
traditional goods	9	4,8	5	4,3	4	0,9	1 1/4	-1
Imports	8,6	4,7	5 1/4	6	5 1/2	3,8	2 1/4	4
traditional goods	8,2	5,2	..	6,1	6	3,1	..	4 1/4
GDP in Total	3,5	1,8	3	2,4	2 1/2	1,6	2 1/4	2
Mainland Norway	6	2,8	3 1/2	3,2	3 1/2	1,5	2	2 1/4
Industry	4,6	1		0,1	..	
Employed Persons	3,8	1,3	2 1/4	2,4	2 1/2	1	1/4	1 1/2
Unemployment Rate	2,5	2,7	2 1/2	2,4	2 1/4	2,8	3	2 1/2
Annual Wages	5,6	6	6	5,5	..	4,7	5 1/2	..
	0,8	3,5	3	3,2	3	1,5	2 3/4	2 1/2
CPIJATE*	1,4	2,2	2 1/4	2,4	2 1/2	1,5	2 1/4	2
Money Market Rate	5	5,7	6 1/4	5,1	..	5 1/2
Export Price Traditional Goods	2,4	-6,3	..	-1,5	-5	-3,5	..	0
Current Account Balance in Billion NOK	390,6	406,2	..	429,4		343,5	..	
Current Account Balance in % of GDP	17	16,6	..	17,2		13,9	..	