

# NHO's Economic Report

Autumn 2007

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## Key Points:

### The NHO's Economic Survey indicates that:

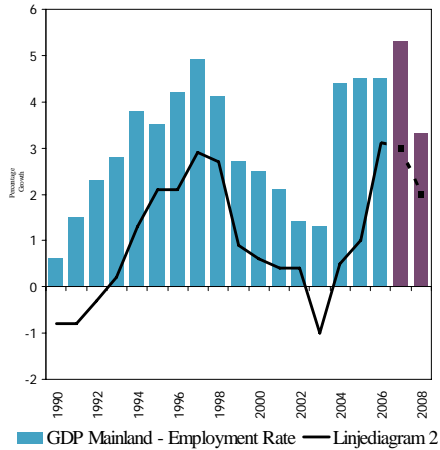
- Fewer NHO member companies have faith in improved market developments for 2008. There is less optimism in the process industry and the building industry with regard to continued growth.
- The growth in labour demand for 2008 is nevertheless estimated to 2.7 percent which is higher than earlier projections.
- The number of unfilled vacancies constitutes approximately 8 percent of the number of employed persons. A year ago the number of unfilled vacancies was 6 percent.
- Two in three enterprises state they use foreign labour. Within ICT and the hospitality industry, more than 80 percent state that they currently are using/will be using foreign labour.
- An increasing percentage of enterprises say that they have invested abroad or that they are planning to invest abroad. Among the enterprises with foreign investments, two in three state that the investment level is higher than that in Norway.
- Within the technology half the enterprises state that they have replaced important Norwegian sub-suppliers with foreign ones during the last year.
- The NHO's profitability and financial statement analysis indicate a clear improvement in 2006. The enterprises expect further improvements for 2007. For 2008, on the other hand, the enterprises are somewhat more uncertain. A stronger exchange rate for the Norwegian krone combined with a weakened US dollar has a negative impact on corporate profitability.
- More than half of the NHO member companies trade in foreign currencies. Of these, two in three state that a strong exchange rate for the krone has a negative effect on business. For the industry, the US dollar is the most important currency while the Euro is the most important currency for the average NHO member company.

### Increased uncertainty and weakened competitiveness

- Upon entering 2008, the Norwegian economy will be venturing into more murky waters. The uncertainty is increasing and the growing pains are expected to intensify.
- The activity level will be high, but the bottlenecks found in the labour market are expected to multiply. Norwegian competitiveness will be severely challenged.
- If the international economic downturn is limited to the US alone, the negative global effect will be minor. But if Europe too enters an economic downturn, the Asian economies as well are expected to be hit by a more extensive decline in exports.
- The decline of the US dollar combined with a strong exchange rate for the Norwegian krone are expected to contribute to poorer competitiveness in parts of the private sector in Norway. With the exception of the oil prices, export prices have already experienced a negative development measured in Norwegian kroner.
- Imports will continue to increase strongly. Norwegian production will be replaced by imports. But short term, strong Norwegian market growth will more than make up for lost market shares.
- Long-term, given a more normal cyclical situation, the underlying cost situation could result in increased unemployment in internationally exposed sectors.
- The increased Norwegian interest rate level is expected to result in a flattening out of housing prices and lead to that fewer new houses are being built. But the capacity within the building industry will be fulfilled by increased activity in relation to the demand for commercial buildings.
- The strong demand for labour should be utilised to increase workforce participation on the labour market. But without increased labour immigration it will be extremely challenging to avoid cost pressure and a decline in competitiveness.

## Prolonged economic upturn serves to weaken Norwegian competitiveness

High activity level also in 2008  
GDP Mainland and employment rate from 1990-2008.



Source Statistics Norway

The Norwegian economy is currently in a phase characterised by a very high activity level and an extremely good market situation. The capacity limits of the labour market in particular are being challenged in several areas in both the public and the private sector. We have now entered the fourth consecutive year characterised by a stronger demand growth than the long-term trend of 2.5 percent. In the second quarter of 2007, a total of 80000 more persons were employed compared to one year before. Never before has Norway seen such high workforce participation.

Given the currently strong growth perspective it is fortunately the case that the labour market capacity limits have proven to be more flexible than previously assumed. There are several factors which support this: Firstly the fact that our productivity is increasing as Norwegian enterprises has managed to organise their production in new, ever smarter ways. Secondly, a steadily growing number of people are currently seeking labour market entry. Workforce participation among older people is increasing, and the increased workforce participation among women in particular serves to extend the Norwegian labour market. Thirdly, an increasing number of Norwegian enterprises have chosen to fulfil their increased demand for manpower by using foreign labour.

NHO's Economic Survey shows that a growing number of enterprises in an increasing number of sectors report increased use of foreign labour, especially from the new EU Member States. Both labour immigration with Norwegian employers and so-called imports involving the posting of workers employed with a foreign employer have increased strongly, and stronger than a year ago.

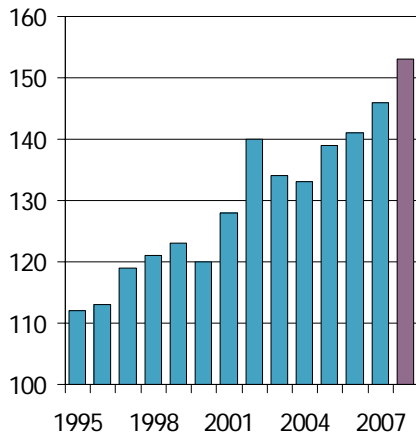
In addition NHO's Economic Survey also shows that enterprises choose to replace Norwegian sub-sub-suppliers with foreign ones. Increased specialisation, a splitting up of value chains and offensive use of the opportunities offered by globalisation has significantly increased the growth potential of the Norwegian private sector, and as a result, the Norwegian economy has gained increased capacity thus enabling it to tackle the extreme demand – so far without negative results such as a cost crack and more expensive goods and services.

The strength and longlivity of the current economic upturn have however lead to that the labour market is currently showing signs of developing bottle necks. The wage growth is going up, and is currently showing a stronger increase than that of our trading partners. In addition to higher cost growth, we have witnessed a significant strengthening of the exchange rate for the Norwegian krone since the publication of NHO's last Economic Report in the spring of 2007. As a result, the cost-related competitiveness has been significantly reduced

The developmental trend in the international arena is characterised

## The cost-related competitiveness severely weakened

Wage costs for industrial workers in Norway. Trading partners = 100



Source: the Norwegian Technical Calculation Committee for Wage Settlements/(TBU)NHO

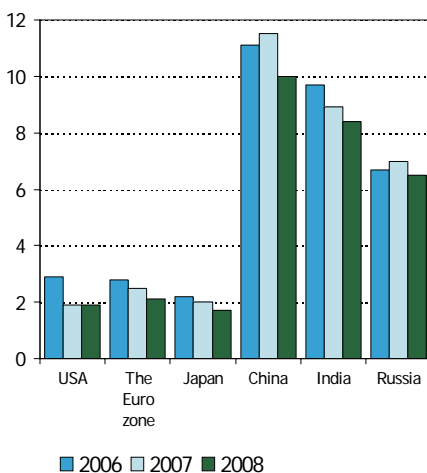
by financial market turmoil. The low savings and high debts of American households now seem to have a negative impact on the are currently witnessing falling housing prices and lower housing wealth. Lower housing wealth means higher risks and greater reluctance among finance institutions. Furthermore this negative wealth effect in the US household sector will yield reduced consumption demand. Traditionally, the US has been regarded as the locomotive of the world economy. Both the prospects of reduced growth in the US economy combined with financial market turmoil increase the likelihood of a reduction in international interest rate levels. The US key interest rate has been cut twice since the publication of the NHO's last Economic Report by a total of ¾ percentage points The prognoses by Consensus point towards falling interest rate levels for the euro zone also. Falling interest rate levels abroad will also serve to reduce the room for manoeuvre which Norway is able to allow itself with regard to increasing the Norwegian interest level if we are to avoid a further decline in competitiveness through an even stronger exchange rate for the krone. In its Monetary Policy Report issued at the end of October 2007 Norges Bank has already reduced the interest rate path for the future key interest rate developments. Given that oil prices remain high combined with falling international interest rate levels, we may see further reductions in the interest rate pate applied to the key interest rate in the next Monetary Policy Report which will be published in March next year.

Four years of very strong growth in the Norwegian economy have their background in the fact Norway as a producer of raw materials and intermediate goods whose prices are being determined by the world market, has profited greatly from globalisation. China's and India's entry into the international trade in goods and services have resulted in cheap imports for all countries. But Norway is particularly fortunate since the strong growth in these countries has contributed strongly to that the demand for energy and other raw materials has been given a major boost. These are all areas in which Norway is a major supplier. Moreover, globalisation has also resulted in a considerable need for transport, which is also an area in which Norway plays an important private sector role. Globalisation has meant good times for the shipping industry and shipping-related industries.

Increased raw material prices naturally also imply increased costs for some Norwegian sectors. The building and construction industry along with the transport sector are examples of sectors where costs are increasing rapidly partly due to a high economic activity level outside Norway and partly due to the high oil price.

Increased export prices coupled with moderate import prices have increased Norway's disposable revenues considerably. This development has given Norwegian households a particular boost with regard to their purchasing power. The enterprises have been given a boost with regard to their profitability and their investment ability whereas the Norwegian State has been given a room for manoeuvre with regard to finances that is unique and has no parallel in other countries. All these three factors combined have served to

Slower international growth in 2008  
Projected GDP growth in selected countries



Source: IMF

give the Norwegian economy strong growth impulses.

Oil prices seem to continue to remain at a very high level, while there seems to be more uncertainty linked to other export prices. The strong exchange rate for the krone and especially the weak US dollar has contributed to a weakening of Norway's favoured position as a global winner. The terms of trade were negative for mainland Norway in the third quarter of this year as export prices showed a decline compared to the previous year, while import prices increased rather strongly.

## Forecasts for 2007 and 2008

	2007				2008			
	SSB	NB	Findep	NHO	SSB	NB	Findep	NHO
Private Consumption	6.3	6	6	6	3.7	3.5	3.5	4
Public Consumption	2.7	3	3.1	3 ½	3.2	2.75	2.3	3 ½
Gross Fixed Investments	7.8		9.9	9 ½	6.6		1.3	5
Petroleum Activities	6.3	7.5	15	10	9.9	7.5	0	5
Mainland Norway	7.6	8.75	8.8	9	6	3.25	1.8	5
-Enterprises	8.9		10.7	12	8.2		4	8
-Housing	6.8		6	5	3.1		-1.8	0
- Public	5.7		8.6	8	5.1		2	6
Demand from Mainland Norway	5.6	5.75	5.7	6	4	3.25	2.9	4

Exports	2.9		1.6	1 ½	4.6		5.1	4 ¼
- Oil and Gas	-2.5		-5.8	-5	7.4		5.4	5
- Traditional Goods	7.8	6.5	8	7	3.9	4	4.3	4
Imports	8.7	7.75	8.3	8 ¾	6.1	4.75	3.8	5 ¾
- Traditional Goods	8.8		9	8 ¾	5.8		3.3	6

GDP in Total	3.5	3.25	3.5	3 ¼	3.7	3.75	3.1	3 ½
GDP Mainland	5.1	5.25	5	5 ¼	3.1	2.75	2.8	3 ½
Industry	3.4			4	2			2

Employed Persons	3.1	3.5	3.5	3 ½	1.3	1.25	1	2
Unemployment Rate	2.6	2.5	2.5	2 ½	2.5	2.5	2.5	2 ¼
Annual Wages	5.6	5.5	5	..	5.9	5.75	5	..
Consumer Prices	0.8	0.75	0.5	½	2.7	3.25	2.5	2 ½
CPI ATE*	1.4	1.5	1.5	1 ½	1.8	1.75	2	1 ½
Money Market Rate	4.8	..	..	4 ¼	5.5	..	..	5 ¼

Export price- Traditional goods	3.6	..	..	4	-6	..	..	-5
Current Account Balance in Billion NOK	335.9	..	..	..	359.3	..	..	..
Current Account Balance in % of GDP	14.9	..	13	14	15.1	..	11.4	14