Euler Hermes Economic Research

Country Report

Norway

Lower oil prices bite

General Information

GDP	USD500.103bn (World ranking 27, World Bank 2014)
Population	5.14mn (World ranking 117, World Bank 2014)
Form of state	Constitutional Monarchy
Head of government	Erna SOLBERG
Next elections	2017, legislative

Strengths

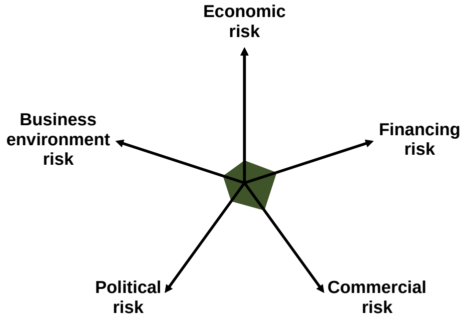
- Solid banking system
- Significant natural resources
- Strong business environment
- Second highest per capita income in Europe after Luxembourg
- Highly skilled and educated workforce

Weaknesses

- Very high household debt burden
- Loss in competitiveness
- High dependency on oil prices
- Low diversification of the economy

Country Rating

AA1



Source: Euler Hermes

Trade Structure

By destination/origin (% of total)

Exports		Rank		Imports
United Kingdom	19%	1	16%	Sweden
Netherlands	12%	2	13%	Germany
Germany	10%	3	8%	China
Belgium	9%	4	7%	Denmark
Sweden	8%	5	6%	United Kingdom

By product (% of total)

Exports		Rank		Imports
Crude Oil	36%	1	6%	Cars And Cycles
Natural Gas	26%	2	5%	Miscellaneous Hardware
Meat	6%	3	5%	Refined Petroleum Products
Refined Petroleum Products	5%	4	4%	Electrical Apparatus
Non Ferrous Metals	4%	5	4%	Non Ferrous Ores

Source: Chelem (2013)

Economic Overview

Declining oil investment is having a clear negative impact on the economy

GDP growth has grown by +3% on average over the past decade thanks to the rise in oil prices and to the rise of households' wealth on the back of rising property prices. Thus, Norway has been one of the strongest growing economies of the developed ones over the past decade. However, the pace of GDP growth has been halved since 2011, growing by only 1.5% on average mainly given the fall in the oil sector output. Over the past months, the strong fall in oil prices (-57% from its mid-2014 high) started to have visible negative effects on the economy. GDP fell for the first time since Q4 2013 (-0.1% q/q). Household consumption slowed down to +0.5% q/q and investment fell for the third consecutive quarter (-1.3% q/q), mainly driven by falling spending in oil-related industries, but also by lower investment in construction. Net exports added +0.4pp to GDP growth, but both export and imports have contracted.

Looking ahead, there is scope for growth to disappoint even further. EH expects oil prices to remain low in the coming months, at 55 USD/barrel on average in 2015 and 60 USD/barrel on average in 2016. Thus, prospects for energy investment have deteriorated considerably (see Chart 2) and could continue to do so in the coming months. Overall, GDP should increase by +1.2% in 2015, almost half the pace form 2014.

Low oil prices led to record low interest rates and exchange rate depreciation

Inflation has trended lower since August 2013 and is expected to be at 2% on average in 2015, below the Central Bank official target of 2.5%. This supports real purchasing power of households while record low interest rates (at 1%, but still the highest within the Nordics) boost loans to consumers that are mainly based on floating interest rates. Further, households' savings remain high. All this supports the housing market. House prices briefly leveled out in late 2013 but started to rise again since the start of 2014 (+10% between Q1 2014 and Q1 2015). The Central Bank would need to be very cautious when normalizing financing conditions and the impact that this might have on house prices given the record high household debt (220% of disposable income). The IMF estimates that a 10% decline in real house prices could reduce private consumption by 0.9%.

The lower oil prices and a more accommodative monetary policy stance triggered a downside adjustment of the krone. This has led to a -17% fall in the real effective exchange rate since its 2013 highs (see Chart 3) and helped get back some of the lost competitiveness of the Norwegian companies, which suffered from deteriorating unit labour costs over the past years.

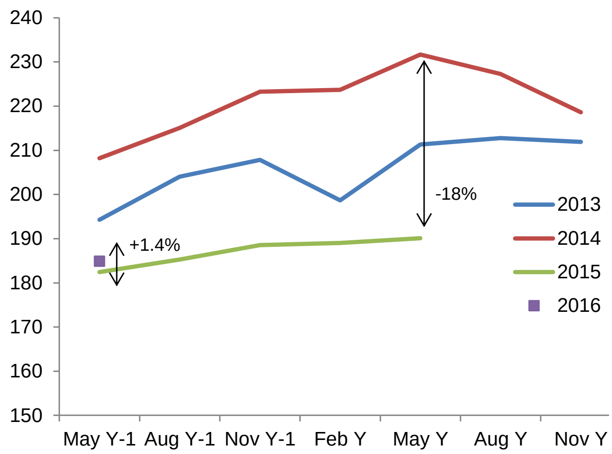
Table 1 Key economic forecasts

Norway		share	2013	2014	2015	2016
GDP		100%	**0.8**	**2.2**	**1.2**	**1.5**
Consumer Spending		40%	**2.0**	**2.0**	**2.8**	**2.7**
Public Spending		21%	**1.7**	**2.7**	**2.0**	**2.4**
Investment		22%	**6.9**	**0.7**	**-4.2**	**-0.9**
Stocks	*	4%	**0.5**	**0.2**	**1.6**	**0.1**
Exports		41%	**-3.0**	**2.6**	**-0.1**	**1.4**
Imports		28%	**4.2**	**2.0**	**3.3**	**2.1**
Net exports	*	13%	**-2.4**	**0.5**	**-1.0**	**-0.1**
Current account	**		**308**	**297**	**255**	**280**
Current account (% of GDP)			*10.0*	*9.4*	*8.1*	*8.6*
Employment			**0.7**	**1.1**	**0.8**	**1.6**
Unemployment rate			**3.5**	**3.5**	**4.1**	**3.7**
Wages			**3.6**	**2.6**	**2.3**	**2.6**
Inflation			**2.1**	**2.0**	**1.9**	**2.0**
General government balance	**		**337**	**334**	**315**	**310**
General government balance (% of GDP)			*11.0*	*10.6*	*10.0*	*9.5*
Public debt (% of GDP)			*29.7*	*28.9*	*30.0*	*30.5*
Nominal GDP	**		3 068	3 150	3 153	3 266

Change over the period, unless otherwise indicated:
*contribution to GDP growth
**NOK bn

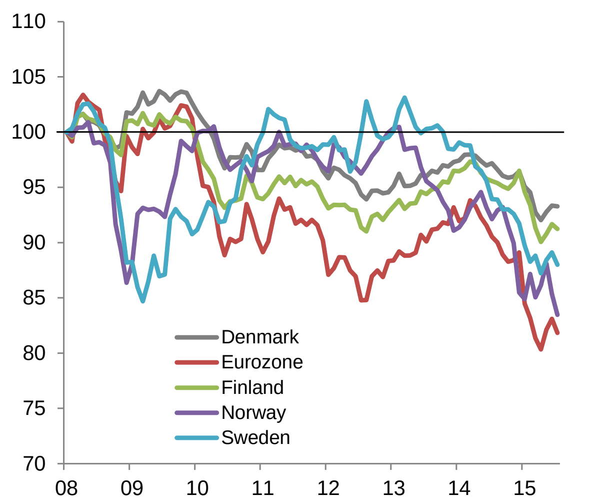
Sources: National sources, IHS, Euler Hermes

Chart 2 Investment costs - oil and gas activity (NOKbn)



Sources: National sources, IHS, Euler Hermes

Chart 3 Real effective exchange rate, Q1 2008 = 100



Sources: National sources, IHS, Euler Hermes

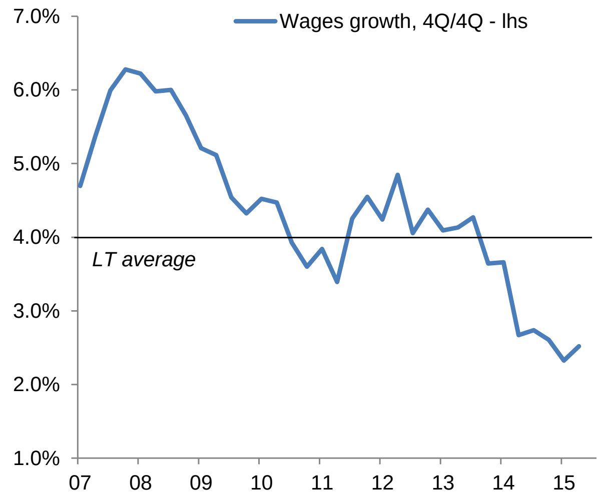
Current account surplus is softening quite fast, but remains one of the highest in Europe

Although the outlook for exports has deteriorated given the fall in oil and gas prices, and that the trade deficit on services and goods (excl. oil) has also widened, the current account surplus still remain large. Indeed, Norway would continue to enjoy solid demand for hydrocarbons (7th world biggest exporter) and electricity that would support the current account surplus, expected to reach +8.1% of GDP in 2015 and +8.6% of GDP in 2016 – see Table 1. This is undeniably far below the +13% average between 2007 and 2013, but still the external position remains very comfortable.

Business insolvencies remain close to 2009 highs

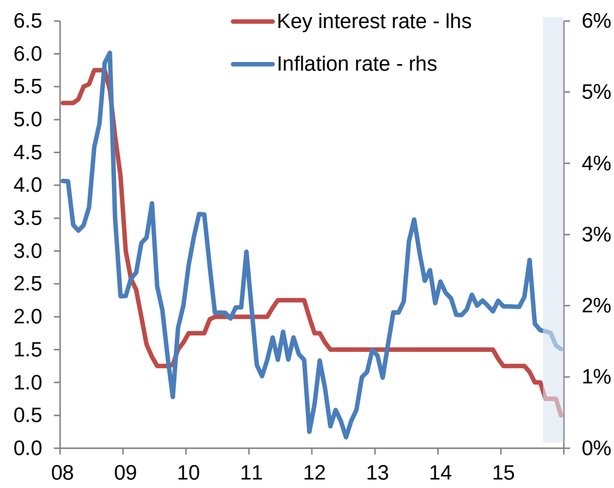
After two years of strong rises, business insolvencies are expected to stabilize at a high level in 2015 (4,800 cases). Prospects remain dampened by the fall in oil prices and the deteriorating outlook for external demand (notably within the emerging markets). However, now that wages slow down (see Chart 4) given the increased flexibility of the collective bargaining system (nominal increase in the national negotiations of only 0.3%) improving companies' competitiveness and that inflation outlook remains subdued, leaving the door open for further rate cuts later this year (see Chart 5), prospects look slightly better. We expect business insolvencies to fall by -3% in 2016, but to remain 69% above the 2007 level and close to 2009 high of 5,013 cases.

Chart 4 Wages – manufacturing sector



Sources: IHS, Euler Hermes

Chart 5 Inflation vs key interest rate



Sources: Central Bank, Euler Hermes

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