



DET KONGELIGE
FINANSDEPARTEMENT

Royal Ministry of Finance

The National Budget 2020

A summary



National Budget 2020

1 Main economic policy features and outlook for the Norwegian economy

The Norwegian economy is performing well. Unemployment is low, and new jobs are created in both rural and urban areas. This contributes to the sustainability of our welfare society. Over the last year, private sector employment has increased by 40,000.

What matters most, for individuals and for the country as a whole, is that as many as possible have a job to go to. Although unemployment is low, there are too many people without job opportunities. The Government is committed to support initiatives that allow more people to learn new skills that enable them to participate in the labour market. The Government is stepping up early intervention in kindergardens and schools to prepare the young for the labour market of the future. The Government prioritises high-quality health services, care for the elderly and assistance for those who need a second chance. It is a priority for this government that families shall be better equipped to look after themselves and their children.

The transition to a greener and more environmentally-friendly society must continue. Research and technological development are key ingredients in efforts to reduce emissions and create new, green jobs. Choosing a greener option must be easy and profitable. The Government is prioritising public transport, as well as other initiatives that provide incentives for making environmentally-friendly choices. Climate policy works. Emissions have been on a downward trend for the last decade and projections show that the reductions are accelerating.

Everyone living in Norway shall be safe. The Government continues to boost the police and the armed forces. To build safe and modern roads is a priority. People and goods must arrive swiftly and safely.

Global political and economic power dynamics are rapidly evolving, and may also give rise to increased uncertainty in Norway. The Government is maintaining its international commitments and is expanding foreign aid.

To overcome the challenges we face we must diversify economic activity, invest for the future, and pursue responsible economic policies. This requires disciplined use of the country's petroleum revenues, with a focus on long-term investment decisions. In the budget for 2020, the Government is proposing to reduce petroleum revenue spending by 0.2 percent of mainland GDP (the non-oil economy). By exercising restraint when the economy is performing well, we avoid putting unnecessary pressure on interest rates and the exchange rate. This will support competitiveness, structural adjustment and private sector growth.

The fiscal budget for 2020 promotes a greener, more modern and safer Norway, resilient and well prepared for the future.

Robust expansion in the Norwegian economy

The Norwegian economy is in its third year of economic expansion. Activity is expanding throughout the country and in most sectors. Employment has increased by more than 50,000 over the last year. Registered unemployment is down to levels last seen in 2008. Many people who were previously outside the labour market are now employed, and the employment rate has increased. At the same time, the number of non-resident employees on short-term visas in Norway has also increased. This may indicate that the labour market is tightening.

The strong performance of the Norwegian economy is expected to continue. Mainland GDP growth is forecast to reach 2.7 percent this year and 2.5 percent next year. This is above the long-term trend both this year and next. Higher real wage growth is boosting private consumption,

and the improvement in competitiveness is contributing to more private sector investment and increased exports. The labour market is expected to continue to improve, with lower unemployment and higher employment.

The growth impulse from the international economy has weakened somewhat recently. Growth has slowed in European countries, but has held up better in the US. Labour markets are nonetheless stronger in many countries than they have been for a long time. Unemployment is on its way down, and wage growth has increased somewhat. For Norway's trading partners as a whole, economic growth is expected to be just below its long-term trend in the near future. The international risk outlook points to increased uncertainty. New barriers to trade pose a threat to global growth. The same applies to the uncertainty relating to the UK's departure from the EU. The uncertainty surrounding economic developments is reflected in financial markets and in weakening business sentiment, especially in manufacturing, and is likely to have a dampening effect on growth in the world economy.

The oil price has recently been around 60 dollars per barrel. This is about 20 dollars less than one year ago, but more than twice the level it reached in January 2016. Futures prices indicate that the oil price will fall slightly from its current level over the next few years. Petroleum investments are still expected to increase significantly this year, and by more than previously expected. Most development projects planned for the Norwegian continental shelf will remain profitable even with oil and gas prices significantly below current levels due to cost reductions and efficiency improvements in the petroleum industry over the last years. Although petroleum investments are expected to gradually decline starting in 2020, they will remain at a high level for many years.

Economic policy has been well-adapted to the state of the economy. When the oil price started to decline in the summer of 2014, fiscal policy turned expansionary in order to boost aggregate demand. Economic growth has picked up considerably since then and unemployment has declined significantly. The Norwegian economy is now in a period of economic expansion and there is therefore no longer need for an expansionary economic policy.

Norges Bank has increased its key policy rate four times over the last year, from 0.5 percent to

1.5 percent. Monetary policy in Norway's trading partners has shifted from rate hikes to rate cuts. Both the Federal Reserve and the European Central Bank have lowered their key policy rates. The Norwegian krone has depreciated by 2.5 pct. since July. This may be linked to the turbulence in international financial markets. Moving forward, Norges Bank has signalled that the key policy rate will remain close to its current level.

Significant improvements in competitiveness over the last few years have paved the way for increased activity in the Norwegian economy. Production is currently expanding throughout the country and in most industries. Businesses are also reporting an increase in investments.

Optimism is widespread across most sectors. Investment and production growth is particularly strong in manufacturing, where many businesses are benefitting from increased demand from the petroleum industry, both in Norway and overseas.

Moderate wage settlements over the last few years have helped consolidate improvements in competitiveness. In line with the outcome of the wage settlement for sectors exposed to international competition, total annual wage growth is estimated at 3.2 pct. this year. Real wage growth is expected to pick up significantly, after turning negative for the 2016-2018 period as a whole. Wage growth is expected to increase further next year, in response to a further tightening of the labour market. At the same time consumer price inflation is expected to decline, further supporting real wage growth.

House prices have increased moderately since last summer. At the same time, activity in the market for existing housing has been high.

Growth in household debt has levelled off somewhat in the last two years, but debt is still at a historically high level and remains a source of vulnerability for the Norwegian economy. When household debt is at a high level, even small changes in interest rates, income or house prices may cause households to cut back on consumption, which would reduce economic growth.

A potential weakening of international growth may also have a negative impact on growth in the Norwegian economy.

The Norwegian economy may also grow faster than projected if, for example, petroleum investments increase more than expected, or if improvements in competitiveness boost exports and

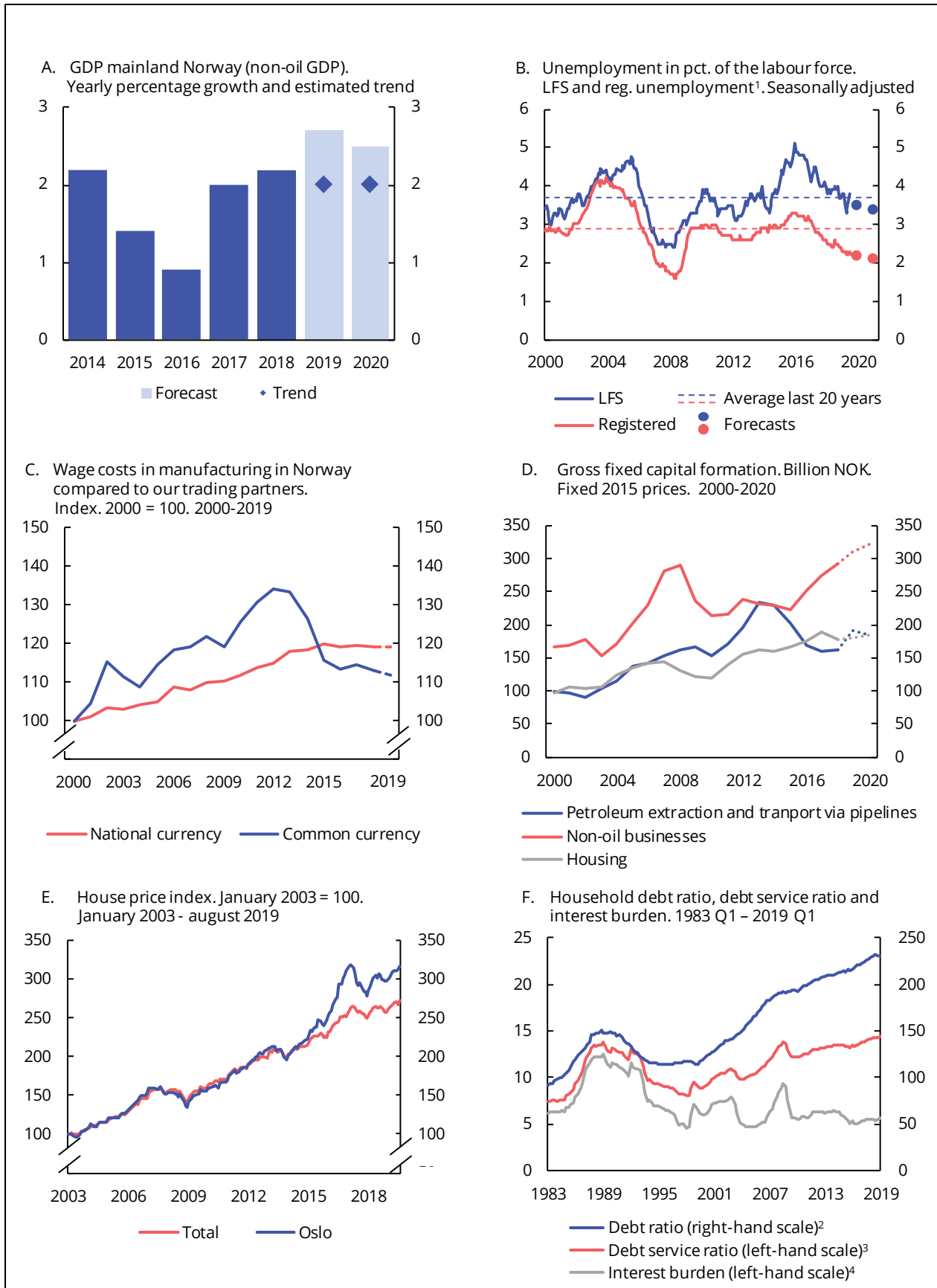


Figure 1 Economic developments

Sources: Macrobond, Statistics Norway, Ministry of Finance, Norges Bank and The Norwegian Technical Calculation Committee for Wage Settlement

Tabell 1 Key figures for the Norwegian economy The National budget 2020

	Billion NOK ¹				
	2018	2018	2019	2020	2021
Private consumption.....	1 533,6	1,9	1,8	2,7	2,9
Public consumption.....	826,8	1,4	1,6	1,7	..
Gross fixed investment	851,5	2,8	6,1	1,2	-0,5
Of which: Petroleum extraction and pipeline transp.	153,4	1,9	17,8	-3,5	-10,4
Business sector Mainland Norway	311,0	6,8	6,2	3,4	2,7
Housing	193,5	-6,2	1,4	2,2	0,8
Public sector	192,7	7,5	1,3	0,3	..
Demand from Mainland Norway ²	3 057,6	2,0	2,1	2,2	2,2
Exports	1 357,3	-0,2	2,3	7,3	3,5
Of which: Crude oil and natural gas	569,4	-4,8	-2,9	14,0	4,6
Goods except oil and gas	411,0	2,0	5,6	5,0	5,1
Services except oil, gas and shipping.....	247,2	4,4	5,3	5,0	1,6
Imports	1 152,2	1,9	5,4	1,8	1,3
Gross domestic product.....	3 530,9	1,3	1,8	3,8	2,3
Of which: Mainland Norway	2 906,9	2,2	2,7	2,5	2,0
Other key figures:					
Employment, 1000 persons.....		1,6	1,6	1,0	0,6
Unemployment rate, LFS (level)		3,8	3,5	3,4	3,4
Unemployment rate, registered (level).....		2,5	2,2	2,1	2,1
Annual wage		2,8	3,2	3,6	..
Consumer price index (CPI)		2,7	2,3	1,9	1,8
Underlying inflation (CPI-ATE).....		1,6	2,4	2,2	2,0
Crude oil price, NOK per barrel (level)		582	538	476	474
Three-month money market rates, pct. ³		1,1	1,6	1,7	1,5
Import-weighted exchange rate (yearly change) ⁴ ...		0,1	2,0	0,5	0,0

¹ Preliminary national accounts in current prices

² Excluding inventory changes

³ Technically calculated using forward prices in September

⁴ Positive number indicates a depreciation of the krone

Sources: Statistics Norway, Norges Bank, Norwegian Labour and Welfare Administration, Reuters and Ministry of Finance

investments more than expected. The optimistic outlook seen in the private sector may increase labour market pressure in a situation of already very low unemployment, accelerating growth in wages and consumption.

A well-adapted economic policy

The Government's Granavolden platform emphasises that petroleum revenue spending shall prioritise investments in research and education and infrastructure, as well as growth-oriented tax reductions, in line with the stated objective of the fiscal rule. This is reflected in a strong and sustained research and development effort, along

with extensive investments in improving roads and expanding public transport services to ease transportation costs. In addition, lower business tax rates and other competitiveness enhancing measures have boosted business investment.

In accordance with the fiscal rule, petroleum revenue spending shall be adapted to the state of the economy. As activity in the Norwegian economy has picked up, the Government has moved to a neutral fiscal policy stance in the last few years, in order to avoid undermining sectors exposed to international competition and to ensure a sustainable development in the Norwegian economy.

When capacity utilisation in the economy is high and interest rates are increasing, fiscal poli-

cy should be restrained. The contribution from the petroleum industry to economic activity in the mainland economy will decline over time. To maintain the competitiveness of the Norwegian economy we must enable new industries to emerge, in order to ensure a diversified economy also in the future. Without a disciplined fiscal policy when the economy is performing well, we could undermine competitiveness, impair labour market mobility and make it difficult for workers to move to sectors exposed to international competition. Such a development would not address the structural challenges facing the Norwegian economy.

With growth in the mainland economy higher than estimated trend growth, and low unemployment, the fiscal stance has been broadly neutral in the last few years' budgets. This path is followed also in the 2020 budget.

In recent years, fiscal policy has entered a new phase. The era of large increases in petroleum revenue spending since the fiscal rule was introduced in 2001 is coming to an end. Petroleum revenue spending as a share of mainland GDP has been kept rather stable in the last few years. Going forward, growth in the Government Pension Fund Global (GPF) is expected to slow. Petroleum revenues will gradually start to decline, and in a decade from now the revenue from the Fund as a share of mainland GDP will most likely be on a downward path. Consequently, the scope for further expanding petroleum revenue spending is severely limited.

As the petroleum reserves have been converted into financial wealth, uncertainty about oil prices has gradually become relatively less important for developments in the GPF, while uncertainty about the market value of the Fund has become more important. How much to transfer from the Fund to the fiscal budget over time is determined by the fiscal rule. The value of the GPF is now about three times the size of the mainland economy, and transfers from the Fund have become an ever more important source of funding for the annual fiscal budgets. A major decline in the capital of the Fund would, when taken in isolation, suggest that petroleum revenue spending should be reduced. The petroleum revenue spending guidelines are flexible exactly in order to handle such developments and to ensure a sustainable development in the Norwegian economy. Petroleum revenue spending should

gradually adapt in the event of major changes (both upward and downward) to the Fund capital or the structural deficit.

The long-term average return on the GPF has been estimated at 3 percent. For 2020, the Government's proposal implies that we are spending 2.6 percent of the Fund capital. This is more than NOK 40 billion less than if we were spending 3 percent. This Government has kept petroleum revenue spending below the long-term fiscal policy guidelines ever since it was first elected – even when faced with the oil price decline in 2014.

If the value of the equities held by the Fund were to decline by 25 percent and petroleum revenue spending remains unchanged at the level proposed in the Government's budget, the spending rate (the withdrawal from GPF) would be 3.1 percent of the Fund capital rather than 2.6. This underlines that the 2020 withdrawal rate is based on prudent economic policies, given that the use of oil revenues, even with a significant decline in the value of the Fund, will be relatively close to the 3-percent path. When we spend less than 3 percent in good times, we are better prepared in the event of a future decline in the value of the Fund or a setback in the economy. When growth in the Fund is levelling off, restraint in good times is a prerequisite for maintaining the fiscal policy flexibility to counter economic setbacks.

While there will be less scope for expanding petroleum revenue spending in coming years, an aging population means gradually higher expenditure on pensions, as well as health care and services for the elderly. Only a small part of these expenditure increases can be funded by increased revenues from the Fund. The pension reform introduced in 2011 is designed to deliver a sustainable pension system over time and to increase labour supply, but is not sufficient to close the gap between central government expenditure and revenues in the long run. New measures will be needed to safeguard the funding of existing welfare schemes in the future. We need to expand economic activity and spend public sector funds more wisely.

High labour force participation and productivity are important for both economic growth and the sustainability of public finances. Employment is relatively high in Norway. At the same time, there are many recipients of social security benefits. The proportion of people receiving either sickness or disability benefits is higher in Norway

than in many other countries. Increasing employment is a key objective for the Government. This will also help reduce income inequality.

Last year, the Government launched an inclusion initiative in which the public and private sectors collaborate to bring more people with impaired functioning or gaps in their CVs into ordinary, permanent jobs. The skills reform, which is called “Lifelong learning”, also aims at increasing employment by promoting skill upgrading and helping businesses develop and apply technical innovations.

We also need more immigrants to enter the labour market. The Government has launched an integration initiative and will carry out a comprehensive reform of our integration policies to ensure faster and better results.

Based on the agreement reached with the social partners in March last year, the Government has continued its rollout of the pension reform to public sector employees, providing significantly stronger incentives to keep working for longer.

The term of this Government has been characterised by a strong focus on transport investment and growth-enhancing business tax reductions. Along with improved competitiveness, this has promoted a rise in production throughout the country and in most sectors. Mainland business investment has accelerated considerably.

The favourable labour market developments also indicate that this policy is working. Many people previously outside the workforce have now found jobs. The employment rate has increased. At the same time, labour immigration has also increased. This reflects the current high activity level in the Norwegian economy. Four out of five jobs are now created in the private sector. This reinforces the sustainability of the welfare society.

To maintain more or less the same growth in the standard of living as Norwegians have become accustomed to over the last 40 years, productivity will need to increase more rapidly than in the last 10-12 years. Moreover, public revenues will need to be spent sensibly to secure the long-term funding of welfare schemes. This requires a continuation of targeted reforms in public administration and the rest of the economy. The de-bureaucratisation and efficiency reform (introduced in 2015) provides incentives for a more efficient central government organisation and releases public sector productivity gains, thus opening up space for new fiscal priorities. The Government has also implemented reforms to

improve public sector resource allocation, for example a local government reform, a railway reform, a community police reform and a reform of higher education, as well as establishment of the road company Nye Veier AS. The Norwegian Tax Administration has recently been reorganised, and the Government proposes to shift responsibility for tax collection from municipalities to the Norwegian Tax Administration with effect from 1 June 2020. In addition, a reorganisation of the Norwegian Public Roads Administration is proposed with effect from 1 January 2020.

Digitalisation is one of the key drivers of public sector productivity increases. Responsibility for digitalisation oversight and coordination lies with the Minister of Digitalisation in the Ministry of Local Government and Modernisation. The Government will continue to develop digital solutions based on user needs, across sectors and administrative levels. This is operationalised in the *Public Sector Digitalisation Strategy 2019–2025*, which was launched in June 2019.

Key figures in the budget for 2020

The Government’s budget proposal for 2020 implies petroleum revenue spending of NOK 243.6 billion, as measured by the structural non-oil fiscal deficit. This corresponds to 2.6 percent of the estimated capital of the GPFG at the beginning of the year. Petroleum revenue spending is estimated at 7.6 percent of mainland Norway trend GDP. This is in excess of NOK 45,000 per capita. One eighth of total government spending in the budget is currently financed by withdrawals from the Fund. Real growth in underlying fiscal budget expenditure is estimated at 0.8 percent, which is below estimated growth in the mainland economy.

The budgets for the last two years have adopted a neutral fiscal policy stance, and the same applies to the budget for 2020. Ex-post accounting figures differ from the those in the budget, but seen together, the overall fiscal policy stance is still more or less neutral. The change in the structural non-oil fiscal deficit is often used as a simple yardstick for the effect of the budget on aggregate demand in the economy. The Government is proposing to reduce petroleum revenue spending by NOK 2.6 billion from 2019 to 2020, measured in fixed prices. As a share of mainland GDP, the structural non-oil fiscal deficit is reduced by 0.2 percent in 2020, following a 0.5-

percent increase in 2019 and a 0.4-percent reduction in 2018 according to the revised accounting figures. The change in the timing of emission allowance revenues from 2019 to 2020 has served to lift the fiscal impulse for 2019 and reduce it for 2020.

The fiscal impulse (as measured by the change in the non-oil structural fiscal deficit) is an indicator which does not take into account that different revenue and expenditure items may have different effects on economic activity, or that fiscal policy may influence activity gradually over several years. As an example, revenues from the sale of emission allowances will not, unlike tax revenues and changes in public sector consumption, in themselves influence economic activity in Norway.

Norway’s economy and competitiveness are affected by the amount of petroleum revenues spent, but also by how these are spent. Report No. 29 (2000-2001), a white paper on economic policy guidelines, emphasised that the increase in petroleum revenue spending should be focused on measures likely to improve the productivity, and thus the growth capacity, of the rest of the economy. In their discussion of the white paper on Long-term Perspectives on the Norwegian Economy 2017, the Standing Committee on

Finance and Economic Affairs unanimously noted that the Storting emphasised, in 2001, that petroleum revenues must not become an excuse for avoiding necessary structural reforms. The Standing Committee on Finance and Economic Affairs also endorsed the key priorities outlined in 2001, calling for government spending to be focused on infrastructure, research and education and growth-oriented tax reductions. The Government continues to prioritise these areas in the budget for 2020.

Aggregate investment in research and education and transport, and tax reductions have been significantly higher over the period 2014-2020 than over the period 2006-2013, in line with the objectives of this Government. For the period as a whole, 11 percent of the overall space for new initiatives in the budget has been devoted to tax reductions, while 24 percent has been absorbed by investments in research, education and transport. In addition, 24 percent of the space for new initiatives has been absorbed by increased expenditure in the national insurance scheme, while approximately 23 percent has been allocated to strengthening local governments, including local government investments in research, education and transport.

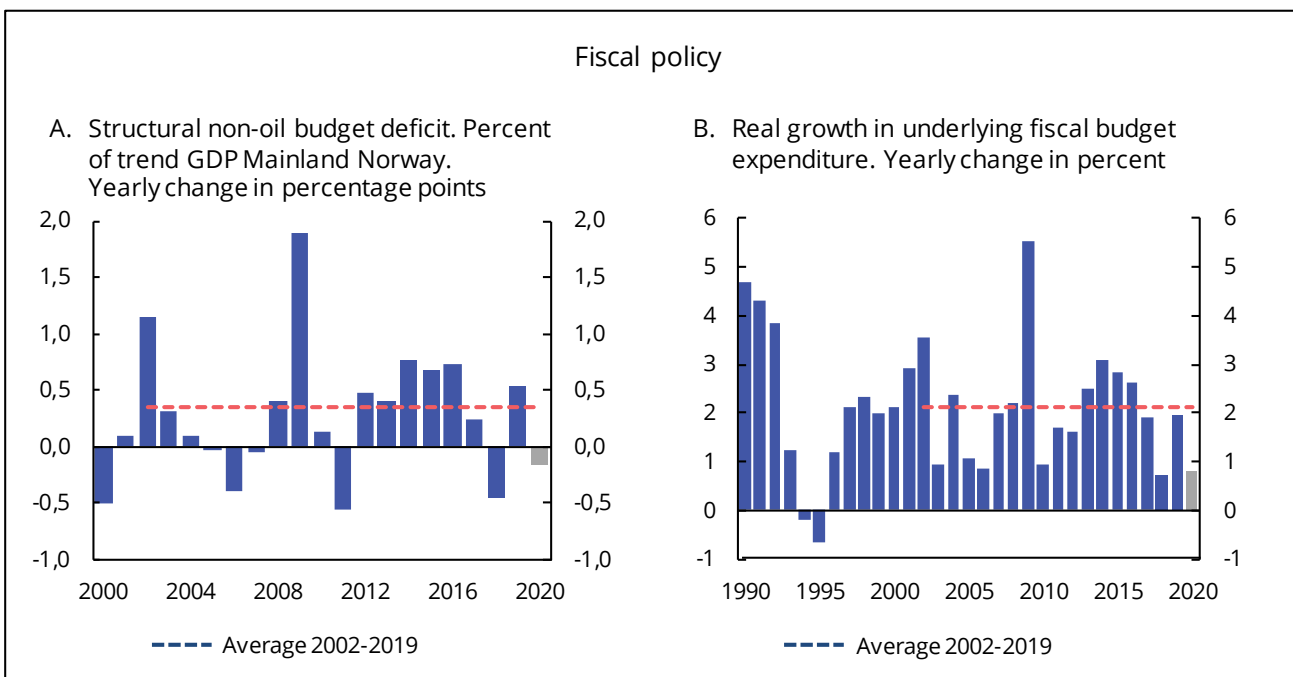


Figure 2 Fiscal policy
Source: Ministry of Finance

Table 2. General government financial balance.¹ NOK million

	2018	2019	2020
Central government financial balance.....	308 447	266 990	276 528
Fiscal Budget surplus and Surplus in Government Pension Fund.....	257 445	242 257	255 167
Non-oil budget surplus.....	-218 513	-232 714	-241 084
Net revenues from petroleum activities.....	250 959	238 271	244 951
Interest and dividends on the Pension Fund.....	224 999	236 700	251 300
Surplus in other central government and social security accounts	-1 936	167	124
Definitional differences between Fiscal Budget and national accounts ² ...	52 938	24 565	21 238
+ Local government financial balance.....	-19 771	-22 012	-27 093
= General government financial balance	288 676	244 977	249 435
In per cent of GDP	8.2	6.7	6.6

¹ Statistics Norway published new data for public finances on 20 September 2019, after the projections on public finances were finalised. The revisions in the latest publication are not included in the National Budget for 2020.

² Includes central government accrued but not recorded taxes. Direct investments in state enterprises, including government petroleum activities, is defined as financial investments in the national accounts.

Sources: Statistics Norway and Ministry of Finance.

The Government's priorities

In the budget for 2020, the Government prioritises policy initiatives that were outlined in the Granavolden platform. The platform identified four key challenges facing the Norwegian economy. The policy initiatives to address these challenges are adapted to the state of the economy, in accordance with the fiscal rule.

Sustainable welfare society

The Government aims to create a sustainable welfare society by readjusting the economy, promoting economic growth and job creation, expanding infrastructure across the country, and promoting the green economy. What matters most, for individuals and for the country as a whole, is that as many as possible have a job to go to. Due to improved competitiveness and the Government's policies, new jobs are being created throughout the country. Four out of five new jobs are created in the private sector. This reinforces the sustainability of the welfare society, and the Government is committed to safeguard the security this provides. The Government wants to make it easier for those currently out of work to find a job. In light of this, we must invest for the future, restructure where needed, and make responsible policy choices. In the 2020 budget, the Government is proposing to reduce petroleum revenue spending by 0.2 percent of mainland GDP. By exercising restraint when the economy is perform-

ing well, we avoid putting unnecessary pressure on interest rates and the krone exchange rate. This will support competitiveness, structural adjustment and private sector growth.

It is a positive development that people live longer, but the sustainability of our welfare schemes depend on us increasing employment. The key elements of the pension reform are improved financial sustainability and stronger incentives to work. In the spring of 2019, the Government proposed a new public sector occupational pension scheme. The proposal, which builds on the agreement with the social partners from March 3, 2018, was adopted by the Storting in June 2019. These changes will increase the incentives for public sector employees to work longer. In collaboration with the social partners, the Government has embarked on the process of adapting the system of occupation-specific retirement ages to the new pension system.

We need to improve the integration of immigrants and ensure that immigrants gain employment in a more timely manner. This calls for an inclusive workplace. The proposed new Integration Act is being circulated for public consultation. The aim of the legislative proposal is that more immigrants obtain formal competencies and enter the labour force. The Government is proposing to refocus part of the integration grant to measures that boost education and formal certification. Immigrants from outside the European

Table 3. Key figures for the central government. The National budget 2020

	2018	2019	2020
Non-oil deficit, NOK billion	218,5	232,7	241,1
Structural non-oil fiscal deficit, NOK billion	214,1	239,0	243,6
Per cent of capital in the Government Pension Fund Global ¹	2,5	2,9	2,6
Per cent of trend GDP mainland Norway	7,2	7,8	7,6
Fiscal impulse.....	-0,4	0,5	-0,2
Real underlying expenditure growth, per cent.....	0,7	2,0	0,8

¹ At the beginning of the year

Sources: Ministry of Finance.

Economic Area (EEA) are prioritised recipients of support through labour market programmes.

High employment and low unemployment are key economic policy objectives for the Government and are of decisive importance for ensuring a sustainable welfare society and an equal distribution of income. Employment and income policies are discussed in more detail at the end of this chapter.

Technological developments create opportunities for new jobs, empowering people and increasing efficiency, but also challenge certain existing jobs and necessitate new skills. The Government proposes to increase budgetary allocations to the skill reform and to set up a skill development programme. Changes are proposed to the financial support scheme for education in order to make it easier to combine education and training with work. The Government will also establish 100 new vocational school places and bolster flexible on-the-job training opportunities.

Research and higher education are important for maintaining welfare levels and for developing a sustainable society. The Government is continuing its initiatives focused on technology, the quality of higher education, and R&D for structural adjustment and business revitalization, as outlined in the *Long-Term Plan for Research and Higher Education 2019-2028*. Furthermore the Government is expanding its support for research on structural adjustment to a low-emission society, technological development to facilitate the transition to a green economy and successful climate change adaptation.

The Government will continue to improve the transport network. Better opportunities for quick and efficient transport support growth and economic renewal, while also making everyday journeys easier for people and businesses. Including

the current budget proposal, the transport budget will have increased by more than 80 percent in nominal terms since 2013. 102 kilometres of dual-carriage motorways will be opened in 2019. This is more than the length of the motorway network in 1990, which only spanned 73 kilometres in total. For 2020, the government proposes NOK 69,3 billion in appropriations to follow up on initiatives in the National Transport Plan (NTP). This is an increase of NOK 2.9 billion in real terms from 2019. The budget proposal facilitates reduced road tolls, increased grants for public transport in urban areas, development of road projects all over the country, as well as improved rail services. The Government is making a targeted effort to increase the return on transport investments. Nye Veier AS, a limited company which oversees new motorways, shall give priority to projects with the largest social return. Allowing competition between railway operators will reduce the need for subsidies and improve quality. The Norwegian Public Roads Administration is being reorganised to improve efficiency.

The Government is proposing several new digitalisation initiatives aimed at increasing efficiency, simplifying access to, and improving the quality of, public services, and enhanced IT security.

Ambitious climate policy

Climate change is one of the key challenges of our time and can only be solved through global cooperation. An ambitious climate policy is necessary to achieve ecological sustainability so that future generations have the same opportunities that we have. We must meet Norway's climate commitments and accept our part of the responsibility for resolving the climate challenges. Tomorrow's workplace must be green, smart and innova-

tive. We need to adopt and develop new green technologies, ensure that the polluter pays, and develop markets for zero-emission solutions. The Government will meet the 2030 commitment of reducing emissions by at least 40 percent in 2030 compared to 1990 in cooperation with the EU.

Climate policy works. Emissions have been on a downward trend for the past decade and projections show that reductions are accelerating. For 2020, the Government is proposing measures to further reduce greenhouse gas emissions in both the short and the long run. The Government is proposing to increase the CO₂ tax on mineral products and other taxes on greenhouse gas emissions by 5 percent on top of the adjustment for inflation. In addition, it is proposed to abolish reduced rates and exemptions from the CO₂ tax. This gives incentives to lower emissions in all sectors and promotes more equal pricing of greenhouse gas emissions across sectors. This makes climate policy more cost effective.

The Government aims to reduce non-EU ETS emissions by 45 percent in 2030 compared to 2005. Norwegian non-EU ETS emissions primarily originate from transport and agriculture. A significant climate-friendly transport initiative is therefore proposed. The preferential treatment of electric cars is maintained. Increased budgetary transfers to the Zero-Emission Fund (under Enova) shall prioritise initiatives to reduce emissions from commercial transport. The Government also proposes initiatives to stimulate increased uptake of zero- and low-emissions solutions in shipping. Furthermore, the Government proposes the appropriation of NOK 700 million in new investment capital for the sovereign climate investment company Nysnø Klima- investeringer AS. This is close to a doubling of the company's investment capital.

The Government proposes to increase spending on public transport. In particular, rail services will be improved. The Government proposes to start construction of double-track railway between Kleverud and Sørli, which is part of the InterCity project on the Dovrebanen line. The Government also proposes to start construction of a railway electrification system on parts of the Trønderbanen and Meråkerbanen lines. Moreover, the Government proposes to increase central government spending on key public transport projects in the four largest urban areas, as well as to reduce ticket prices for public transport in the main cities.

The Government seeks to achieve a cost-effective solution for a full-scale CO₂ capture and storage facility in Norway. For 2020, appropriations are proposed for further planning, including a CO₂ storage exploration well. The Government is aiming to make an investment decision in 2020/2021.

The Government also contributes to reducing emissions in other countries, and proposes to appropriate just over NOK 7 billion for foreign aid-related renewable energy, climate, environment and ocean initiatives; an increase of NOK 200 million from 2019.

The Government is following up on the recommendations of the Climate Risk Commission. Flood and landslide prevention is given priority via mapping, zoning, monitoring, warning and protection measures. A special appropriation is proposed under the Norwegian Water Resources and Energy Directorate for expenditure on disaster and emergency measures in connection with flood and landslide events.

Social sustainability and opportunities for all

Social sustainability is characterised by low levels of inequality, trust among people, and low poverty. Social exclusion can prevent people from living rich and fulfilling lives. Good schools and a quality education are critical if we are to create opportunities for all. Strong social cohesion requires poverty reduction, concerted integration efforts and a society that enables people to live free and independent lives.

The Government is stepping up early intervention in kindergartens and schools to help children who need support. A white paper on early intervention and social inclusion will be published in the autumn of 2019. NOK 400 million of the proposed increase in unrestricted revenues for the local government sector is made with reference to the importance of early intervention in schools. Appropriations that can be used to expand the number of teaching positions, as a result of the teacher density norm, are maintained at about the same level as in 2019.

Good schools with up-to-date curricula and skilled teachers are prerequisites for successful learning. The Government is renewing the national curriculum for primary and secondary education and will continue to devote resources to strengthening qualifications and on-the-job training for teachers and school managers. The Gov-

ernment will also continue its initiatives to enhance the quality of kindergartens.

The Government will remove financial barriers to child and youth participation in the educational and social environment. Two-year olds from low-income families are included in the free of charge core time kindergarten scheme from the autumn of 2019. From 2020, it is proposed to offer full-time kindergarten free of charge to two- and three-year olds in asylum seeker reception centres. Furthermore, the Government is proposing means-testing of parent payments for the after-school recreational programme (SFO) for 1st and 2nd graders and to offer SFO free of charge to 5th – 7th graders with special needs.

The Government proposes to increase the child benefit grant for all children up to the age of six years by NOK 300 per month from 1 September 2020. The increase will improve the financial situation of all parents with young children, especially those with low incomes. In addition, the Government is proposing a leisure card trial scheme for children over the age of six, to pay for participation in leisure activities.

Well-designed welfare schemes help reduce inequality and play an important role in enabling individuals to lead rich and fulfilling lives, irrespective of background and health. Well-designed welfare schemes also enhance the structural adjustment capacity of the labour force. Welfare schemes need to encourage people to work, while at the same time ensuring an income for those who are unable to work.

The Government's budget proposal is aimed at improving welfare services. The Government is giving priority to strong hospital finances, hospital building investment and eHealth, as well as enhancing care service quality and capacity. The budget allows for a 1.5 percent increase in hospital activity in 2020, which exceeds the 1.3-percent increase arising purely from demographic developments. New hospital investments are facilitated, inter alia, by an investment loan of more than NOK 29 billion for the new Oslo University Hospital. The Government propose to boost national eHealth development through investment in the health analysis platform and the establishment of a "standardised language" for eHealth solutions. Measures are taken to address recruitment challenges under the regular general practitioner scheme and the need for consultant physicians.

The local government sector, which provides

key welfare services, will see real growth of NOK 1.3 billion in unrestricted revenues under the budget proposal. This enables municipal and county administrations to keep providing more and better services. The budget allows for investment grants for 2,000 municipal assisted living facility spaces. The Government is following up on the senior citizen reform *A full life – all your life* by increasing the maximum grant size under the grant scheme for decentralized kitchen services in nursing homes and assisted living facilities. The Government will continue and expand ongoing trials of central government funding of care services. We are following up the anti-substance abuse plan, and aggregate appropriations for the plan exceed NOK 2.4 billion, which was the amount originally proposed, over the period 2016-2020.

The Government will take advantage of the positive labour market developments to include as many people as possible in the labour market. The inclusion initiative aims to bring more people with impaired functioning or gaps in their CVs into ordinary jobs. Labour market programmes are important tools under the inclusion initiative. For 2020, the Government is proposing to increase appropriations for individual job placement support, the mentoring programme and assistance in ensuring a disability-accessible workplace.

International migration is unpredictable and may rapidly change. We must be prepared for such changes, and at the same time pursue a restrictive and responsible immigration policy premised on the rule of law.

When setting the settlement refugee quota, the number of asylum seekers and other immigration and integration challenges facing Norway should be taken into consideration. The Government proposes to maintain the resettlement refugee quota of 3,000 places in 2020, as the number of asylum seeker arrivals to Norway is expected to be low.

The Government believes that Norway needs suitable and adequate benefit schemes for those who are granted a residence permit, but such schemes must be fair, sustainable and serve their purpose. The benefit schemes need to stimulate work. We therefore propose to abolish the special refugee provisions under the national insurance scheme, and to increase the residence period requirement under the national insurance scheme from three to five years.

Security

Security is a prerequisite for freedom. Crime breeds insecurity. The population therefore needs to be protected by the rule of law, a strong and effective police force and a credible defence capability.

This is reflected in the budget for 2020 with a NOK 2.5 billion increase in defence sector appropriations for, inter alia, investments in new submarines, maritime patrol aircraft and artillery for the Norwegian Armed Forces. We are preparing for an increase in military activity and strengthened emergency response preparedness. This meets the targets the Government has set in the 2017-2020 long-term plan for the defence sector, and will expand the defence budget by more than NOK 8 billion in real terms over the period covered in the long-term plan.

The Government is planning for a continued increase in police presence. The budget proposal allows for the recruitment of graduates from the Norwegian Police University College in 2020. In addition, appropriations are increased to cover the full-year effect of the recruitment of graduates in 2019. More funds for the police will strengthen the capacity of police districts to prevent, investigate and prosecute crime.

It is proposed to provide the police and the Norwegian Directorate of Immigration with funds in order to enable the implementation of new Schengen systems for border control and monitoring. These systems will improve capacity for detecting and preventing crime, ID fraud and illegal migration.

To facilitate follow-up of the Security Act, the Government is proposing to increase appropriations for the Norwegian National Security Authority (NSM). The proposal facilitates digitalisation and improved efficiency and quality in the security clearance of personnel. Moreover, the Government proposes initiatives to improve the ability to prevent, detect and manage security incidents in emergency preparedness communications.

To facilitate an increased rescue preparedness in Northern Norway, the Government intends to establish a new base for rescue - helicopters in Tromsø from 2022. Such a base will also be able to meet the preparedness needs of the police. In order to meet these needs in the short run, when the Bell 412 helicopters of the Armed Forces are relocated from Bardufoss to Rygge, the Government is proposing a temporary solution based on

renting civilian sector stand-by helicopter capacity. Furthermore, it is proposed to establish high frequency (HF) coverage in the northernmost ocean areas, which will provide improved emergency communications.

The Government's priorities are discussed in further detail in the proposal for the state budget. The Government is in the budget for 2020 taking important steps to meet the key challenges facing the Norwegian economy, while at the same time continuing and supporting new structural adjustment efforts and reforms with a longer horizon.

The tax proposal

Since 2013, a responsible fiscal policy and an ambitious tax policy with broad tax reductions for businesses and individuals have yielded results.

When the television licence fee is abolished on 1 January 2020, the Norwegian Broadcasting Corporation (NRK) will be funded via the fiscal budget. For 2020, the restructuring is funded by reducing the personal allowance in the income tax, but this tax increase amounts to less than the abolishment of the NRK licence fee. The Government proposes, at the same time, to increase the tax credit for pensioners to ensure that those receiving the minimum national insurance pension will continue to pay no tax.

The Government also proposes to make it more attractive for small start-up companies to use share options to attract and retain key personnel. It is proposed to expand the current scheme to include companies with a maximum of 12 employees. The maximum share option benefit per employee will be increased from NOK 500,000 to NOK 1 million. In addition, certain improvements are proposed for the Skattefunn research and development tax incentive scheme. These include, inter alia, increasing the maximum hourly wage rate for internal R&D from NOK 600 to NOK 700. The Government also proposes to abolish the special provisions on the valuation of shares of newly-incorporated companies for net wealth tax purposes. It shall no longer be possible to reduce the taxable valuation of unlisted companies via simple changes to the company structure.

As far as indirect taxes are concerned, the Government is proposing to abolish CO₂ tax exemptions and low rates, as well as to increase the general rate by 5 percent. This will result in more equal pricing of CO₂ emissions and a more cost-

effective climate policy. The CO₂ tax on petroleum activities and domestic EU ETS aviation will also be increased by 5 percent. The road transport biofuel sales requirement will be increased from 12 to 20 percent in 2020. It is proposed, in line with the Granavolden platform, to reduce the road usage tax to compensate for the increased CO₂ tax and an increased biofuel sales requirement. New emission values (WLTP) are introduced in the CO₂ component of the motor vehicle registration tax.

The Government is also proposing to abolish the NOK 350 duty-free allowance on goods imports. At the same time, a simplified arrangement for the payment of value added tax from non-Norwegian platforms is proposed with effect from 1 April 2020.

The Government aims to reduce the maximum rate of property tax on residential properties and holiday homes from 0.5 to 0.4 percent from 2021, and will come back to this as part of a comprehensive local government finance proposal in connection with the local government proposition for 2021.

Total new tax reductions in 2020 as the result of the Government's proposals are about NOK 0.5 billion on an accrual basis.

Monetary policy

The long-term role of monetary policy is to maintain monetary stability. Ensuring price stability in the form of low and stable inflation is the best contribution monetary policy can make to promoting a high level of welfare, high employment and economic growth over time.

Norges Bank is responsible for the operational implementation of monetary policy based on guidelines set by the Government. The operational target of monetary policy is annual consumer price inflation of close to 2 percent over time. Inflation targeting shall be forward-looking and flexible so that it can contribute to high and stable output and employment and counteract the build-up of financial imbalances.

Over the last year, Norges Bank has increased the key policy rate four times. The first time was in September last year, when the rate was increased from a historically low level of 0.5 percent. The rate was thereafter increased to 1.0 percent in March this year, 1.25 percent in June and 1.5 percent in September. The analysis in Monetary Policy Report 3/2019 suggest that the

rate will most likely remain at this level in the coming period.

On 17 June this year, the Storting enacted a new Central Bank Act, which will enter into effect on 1 January 2020. The Act includes a new provision regarding the purpose of the central bank. The Act also outlines the duties, the organisation, and the supervision of Norges Bank. Once the Act enters into effect, a Monetary Policy and Financial Stability Committee will be established. The committee will be responsible for Norges Bank's role as the executive and advisory monetary policy authority, and will also contribute to the promotion of financial stability. The Committee will be one of the three top governing bodies of the Bank, along with the Executive Board, which will have the responsibility of the Government Pension Fund Global, and the Supervisory Council.

Vulnerabilities in the Norwegian financial system

Experience shows that the economic costs of financial instability can be high and persistent. In particular, the interaction between the banking sector and the rest of the economy may give rise to an accumulation of financial imbalances, and trigger severe turbulence and deep economic setbacks.

Sustained increases in the household debt burden indicate that financial imbalances have accumulated and represent a vulnerability to the Norwegian economy. The Government has over the last few years adopted a number of measures to contribute to more sustainable housing market developments, reduce household vulnerabilities and make the financial system more robust. The Housing Mortgage Regulations will contribute to a more sustainable housing mortgage market. These are temporary regulations scheduled to expire on 31 December 2019. The Government is now contemplating whether to extend the regulations and, if so, in what form. Regulations stipulating lending practice requirements for consumer loans were adopted in February. These provide, together with the Housing Mortgage Regulations, a unified regulation of banks' household lending practices.

In the wake of the financial crisis, Norway was among the first countries to introduce new and improved solvency requirements for banks, including a countercyclical capital buffer requirement. The countercyclical capital buffer require-

ment has been increased gradually, and was further increased to 2.5 percent in December 2018 with effect from the end of 2019. The Ministry of Finance has recently been circulating for consultation a proposal to increase the systemic risk buffer requirement for banks to maintain actual capital requirements at a level commensurate with risk in the Norwegian economy. The background to this is that implementation of the EU capital requirements framework, CRR/CRD IV, will reduce requirements for many Norwegian banks in real terms, since the introduction of the so-called SME discount will reduce capital requirements for lending to small and medium-sized enterprises, whilst abolition of the Basel I floor may reduce requirements for banks that use the internal ratings-based approach.

Favourable developments in the Norwegian economy have enabled banks to enjoy several years of low loan losses, easy access to funding and strong earnings. This has continued thus far in 2019. Market funding allows banks to engage in more flexible liquidity management, but also makes them vulnerable to market turbulence. A somewhat higher proportion of the market funding has become longer term in the last few years, thereby reducing the vulnerability of banks to market fluctuations.

Employment and income policy

Employment policy shall, together with other economic policies, support high economic growth and high labour force participation. High employment and low unemployment are key economic policy objectives for the Government and are of decisive importance for ensuring a sustainable welfare society and an equal distribution of income.

The Government will take advantage of the positive labour market developments to include as many people as possible in the labor market. The Government has launched an inclusion initiative in cooperation with the social partners. The intention is to lower the threshold for labour market entry and make it easier for employers to hire individuals who are currently outside the labour force. Recruitment assistance for employers has been strengthened. The wage subsidy scheme, which is an important tool for getting more people with uncertain or variable productivity into work, has been modified to make it easier for employers

to use the scheme. The Government will also expand programmes for job seekers with impaired work capacity, mental disorders or substance abuse in order to get more people into work. The Government has also improved the opportunities for job seekers with gaps in their CVs or who have not completed secondary education to complete training that results in formally-approved competencies.

The letter of intent on a more inclusive work-life (the IA Agreement) plays a key role in the Government's efforts to reduce social exclusion. The IA Agreement was renewed on December 18, 2018 until late 2022. The overarching objective of the IA cooperation is to create a worklife that caters to all by preventing sickness absence and people dropping out of the workforce. The IA Agreement aims to reduce the incidence of sickness absence by 10 percent from 2018.

It is important to offer assistance to those who may have difficulties in obtaining employment unassisted. Labour market programmes are key tools for getting more people who are unemployed into work and preventing groups with weak qualifications from permanently dropping out of the labour market. Labour market programmes are focused on people who are unemployed and people with impaired work capacity. An improved labour market outlook for 2020 implies that labour market programmes can be scaled back somewhat. The appropriation is nonetheless sufficient for the continuation of well-funded programmes for people with impaired work capacity and other vulnerable groups. In addition to people with impaired work capacity, youth, non-EEA immigrants and people who have been out of work for long periods of time are given special priority for participation in labour market programmes. Moreover, the Government proposes to maintain the increase of 300 places for people participating in permanently adapted work that was proposed in the Revised Budget for 2019.

Since the year 2000 there has been a more than 50 per cent increase in the proportion of the population aged 18-29 years that receives work assessment allowances (WAA) or disability benefits. For young people, WAA can in many cases be the first step on the way to permanent social exclusion. It has been noted by the Employment Commission that many young people receiving the minimum WAA have an income that is above

the average income of people in the same age group who do not receive any social security benefits. This may create a poverty trap. The Government aims to pave the way for more people to make the move from passive schemes to income-generating work. The Government is therefore proposing to follow-up young WAA recipients more closely, while at the same time reducing the minimum benefit and abolishing the disabled youth supplement for WAA recipients. The minimum benefit for new WAA recipients under the age of 25 years will thereby be at the same level as the minimum benefit for young recipients of introduction benefits and qualification benefits.

Wage bargaining is the responsibility of the social partners. Wage bargaining is coordinated, with key industries in sectors exposed to interna-

tional competition being the first to bargain. This helps keep wage developments within limits that are sustainable over time for businesses exposed to international competition. The authorities are responsible for ensuring that laws and regulations facilitate an efficient and flexible labour market. Income policy cooperation helps the social partners and the authorities to develop a common understanding of the situation in the Norwegian economy and the challenges facing it.

Based on the wage settlements concluded thus far this year and assessments of economic developments, annual wage growth in 2019 is estimated at 3.2 percent. The National Budget 2019 assumed annual wage growth of 3¼ percent this year.

Appendix 1

Norway's fiscal policy framework

Norway has as most countries a framework that governs the fiscal balance. Norway's fiscal framework is especially designed for our situation as a large petroleum producer.

A big petroleum industry has certain characteristics that may prove challenging for fiscal policy's ability to ensure a stable economic development. From a public finance point of view, tax revenues from petroleum extraction are large, vary considerably from year to year, and will eventually end. For many resource-rich countries, the temporary large revenues has led to relatively short-lived booms followed by long-lived and painful adjustments as production and revenues diminish. A common pitfall is excessive spending, which destabilizes the economy and fails to benefit future generations.

The Government Pension Fund Global (hereafter, fund) and the fiscal rule for the use of oil and fund revenues support a stable economic development in both the short and long term. The State's net cash flow from the petroleum industry is transferred in full to the fund, in addition to the direct returns from the fund itself. The fiscal rule specifies that the transfers back from the fund to the central government budget shall over time equal the expected real return on the fund, estimated at 3 per cent.

The framework *delinks the earning from the use of petroleum revenue*, a key feature, which is necessary in securing a sound macroeconomic management. In particular, the framework shields the fiscal budget from petroleum price volatility and lessens the risk of overspending by providing policy makers a fiscal policy guideline in their decision making. The fund is invested abroad. This protect the krone exchange rate against large, varying foreign exchange earnings, and lays a foundation for more stable expectations in the currency market.

The fiscal rule is a long-term guide for the use of the money in the fund. It also puts emphasis on evening out economic fluctuations to contribute to good capacity utilisation and low unemployment. Several mechanisms have an effect in this regard. Spending of petroleum income is measured by

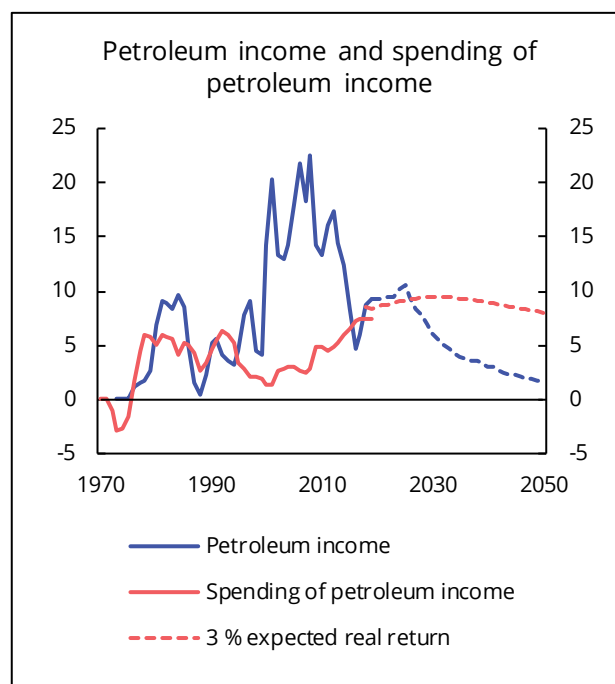


Figure A.1 The State's net cash flow from the petroleum sector, the structural non-oil fiscal deficit and 3 per cent real return on the Government Pension Fund Global. Per cent of trend-GDP for mainland Norway

Sources: Ministry of Finance and Statistics Norway.

the non-oil structural fiscal deficit. This means that the fiscal rule allows automatic stabilisers to play out in full (see appendix 2). The automatic stabilisers in the budget are estimated to be stronger in Norway than in many other countries due to Norway's comprehensive welfare systems. The fiscal rule also allows budget policy to be used actively to stabilise production and employment. Still, monetary policy is the first line of defence in stabilising the economy.

Figure A1 shows how the spending rule helps Norway convert substantial, yet temporary and fluctuating income from the petroleum industry into more stable spending over public budgets. Following a decline in the second half of the 1990s, the spending of petroleum revenue has increased again after 2001, but have been kept rather stable the latest years, measured as a share of mainland trend-GDP, see figure A1. The level is not much higher now than in the 1980s and

early 1990s, measured as a share of mainland trend-GDP, and is now also based on the expected real return of a large fund.

The fund has grown rapidly in recent years and is now estimated to be about three times the size of the mainland economy. Over time, the inflow of new petroleum revenues will decline, as will the growth of the fund. Consequently, the volatility of the fund's investment portfolio will

affect the fund's value more than the ups and downs of petroleum prices. The fiscal framework needs to take into account the risk of a large drop in the value of the fund. The framework states that fluctuations in the fund shall be evened out over several years. A permanent, large drop may make it necessary to reduce the transfer from the fund to the budget. This calls for prudence in our macroeconomic management.

Appendix 2

Calculation of the structural non-oil budget balance

The general government budget surplus can vary considerably from year to year without this being the result of structural changes in the budget. To get a better picture of the underlying development of fiscal policy, it is sensible to examine the development of the budget balance excluding petroleum-industry revenue and expenditure. It is also useful to correct for factors such as the effects of economic fluctuations on direct and indirect taxes and unemployment benefit, see table A.1.

The classification of public revenues and expenditure into a cyclical and a structural part cannot be based on direct observations, but needs to be estimated on the basis of analyses of accounting figures, economic statistics and projections for coming years. The distinction between cyclical and structural changes is usually made on the basis of estimated trend levels for the relevant variables. The findings may be influenced by new economic development data, and are subject to

revision even after the national accounts for each year have been finalised.

The calculation of structural direct and indirect taxes is based on data on actual revenues recognised in the national accounts, as well as forecasts for the projection period. The calculations also include taxes on income and wealth payable to municipalities, and essentially cover the period 1960–2018, extended to 2030 using forecasts. The projection period is based on the Ministry of Finance's medium-term projections and the continuation of the proposed tax programme for 2019. The assumptions may be summarised as follows:

- *Taxes on labour.* This category includes employers' social security contributions and personal taxes, including net wealth tax levied on individuals. The development in the number of normal man-years employed is an important indicator of developments in employers' social security contributions and total personal tax-

Table A.1 The structural non-oil fiscal deficit. NOK million

	2018	2019	2020
Non-oil fiscal deficit.....	218 513	232 714	241 084
+ Net interest payments and transfers from Norges Bank.			
Deviation from trend.....	4 934	5 847	3 774
+ Accounting technicalities	680	3 547	-730
+ Taxes and unemployment benefits. ¹ Deviation from trend.....	-10 073	-3 119	-502
= Structural non-oil fiscal deficit	214 054	238 989	243 627
Measured in pct. of trend-GDP for mainland Norway	7,2	7,8	7,6
Change from previous year in percentage points (fiscal impulse) ²	-0,4	0,5	-0,2
Memo:			
Income from investments in The Government Pension Fund Global.			
Estimated trend.....	215 806	229 434	243 281
Structural non-oil fiscal deficit, including income from investments..	-1 752	9 555	346
Measured in pct. of trend-GDP for mainland Norway	-0,1	0,3	0,0

¹The corrections are influenced by adjustments to the tax reform.

²Positive figures indicate that the budget has an expansionary impact. The fiscal impulse does not take into account that different income and expenditure items may impact economic activity differently.

Source: Ministry of Finance.

es. The projections are based on a growth in normal man-years employed of 1.6 pct. in 2019 and 1.0 pct. in 2020. The estimates are based on population projections from Statistics Norway.

- *Taxes on capital.* This category includes taxes paid in arrears by companies and other non-individual taxpayers outside the petroleum industry and excluding withholding tax. It is assumed that taxes from enterprises outside

the petroleum industry will remain approximately unchanged as a proportion of non-oil GDP after 2020.

- *Indirect taxes.* This category includes value added tax, motor vehicle registration tax and other excise duties, and other indirect taxes including stamp duty and miscellaneous sectoral taxes. Private consumption developments are an important influence on indirect taxes.

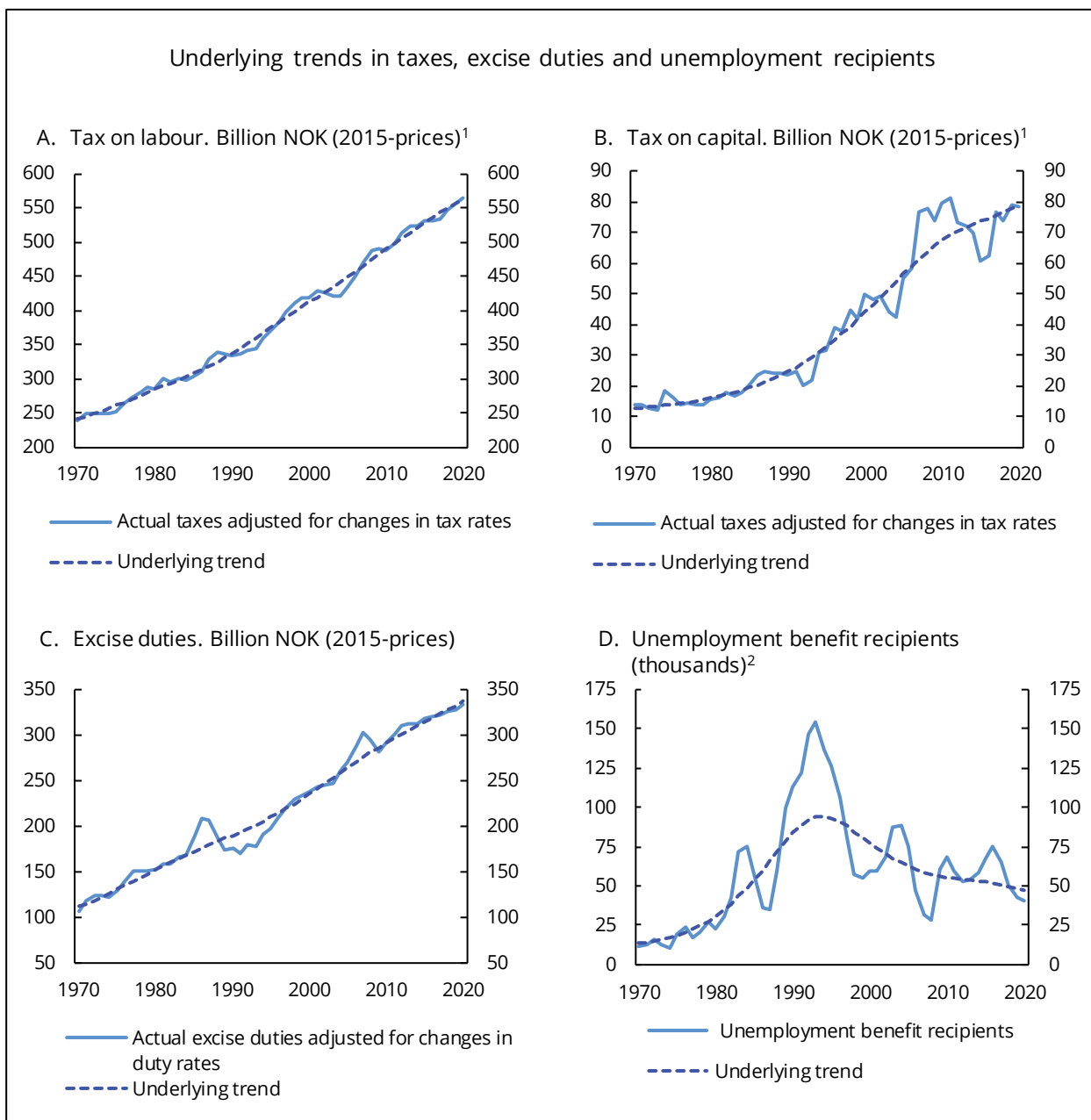


Figure A.2 Underlying trends in direct and indirect taxes and the number of unemployment benefit recipients

¹ For years up to and including 2018, actual taxes as per the national accounts are shown adjusted for changes in tax rates and the tax base and converted into fixed 2015 prices.

² A correction is made to take into account that unemployment benefit recipients may be partly unemployed, by converting the number of recipients into full-time equivalents.

Sources: Ministry of Finance and The Norwegian Labour and Welfare Administration.

On the expenditure side of the budget, a cyclical correction is made to unemployment benefit expenditure based on estimated trend deviations for the number of unemployment benefit recipients.

The described methods for calculating the structural budget balance deviate somewhat from methods used by international organizations such as the OECD, IMF and the EU Commission. The Ministry of Finance has access to detailed information about developments in the Norwegian economy and important tax bases, which allows a detailed methodology. OECD, IMF and the EU Commission uses a more aggregate approach, due to their need of a uniform methodology across countries and a more limited access to detailed information from each country.

Developments in the three main groups of direct and indirect taxes and the number of unemployment benefit recipients are shown in Figures A.2A to A.2D. Labour, capital and indirect taxes are all projected to be near their trend level. The number of unemployment benefit recipients is expected to be lower than the trend.

Developments in the non-oil and the structural non-oil fiscal surplus are shown in Figure A.3. As regards the surpluses in the years 1987–1988 and the small deficits in 2001 and 2007, it is important to note that these years marked the ends of lengthy, strong cyclical upturns. With the exception of these years, fiscal budgets since 1975 have generally registered significant running deficits when revenues and expenditure relating to the petroleum industry are excluded, although there have been major variations during the period. Spending of petroleum income, measured by the structural non-oil fiscal deficit, increased gradually up until 2017. In recent years, it has hovered around 7.5 percent of trend GDP for the mainland economy.

The fluctuations in the structural non-oil deficit are related to the fact that the budget has at times been used actively to stabilise production and employment trends. Figure A3 shows that the fluctuations in the non-oil deficit are considerably larger than the fluctuations in the structural non-oil deficit. This is due to the objective of allowing the automatic stabilisers in the budget to function so that cyclical fluctuations in direct and indirect tax revenues, as well as in unemployment benefits, do not influence the expenditure side of the budget.

Experience shows that it is difficult to distinguish the impact of economic cycles from the underlying tax revenue trend. The estimated structural non-oil deficit may thus be revised considerably on the bases of new information.

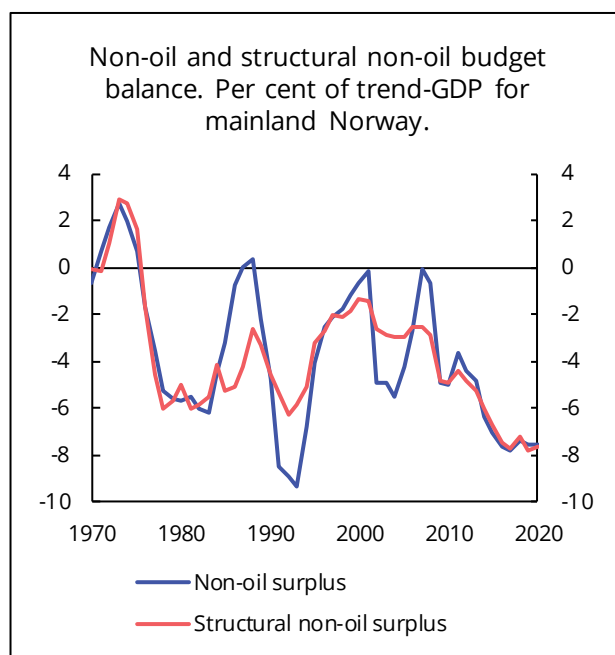


Figure A.3 Non-oil and structural non-oil budget balance. Per cent of trend-GDP for mainland Norway.

Source: Ministry of Finance.

Appendix 3

The role of the petroleum sector in the Norwegian economy

Through its demand for goods and services, the petroleum industry contributes considerably to activity and employment in the Norwegian mainland economy. The tax system and the State's Direct Financial Interest (SDØE) ensure that most of the net extraction revenues accrue to the State. Such revenues make a major contribution to the funding of the welfare state and the strengthening of public finances. The State's net cash flow from petroleum activities has represented 26 per cent of the State's total income since 2000. The management of the Norwegian petroleum wealth is discussed in Appendix 1.

Growth in aggregate demand from the petroleum sector (the sum of investments, intermediate products and wage costs) was particularly steep from the mid-1970s to the mid-1980s. Subsequently, demand from the sector fluctuated around a stable level as a percentage of mainland GDP, before picking up significantly again over the period 2005-2013. In 2014, this trend stopped, and the next couple of years the demand from the petroleum sector fell sharply, mostly due to

lower investment activity after the decline in the oil price. Last year the aggregate demand from the petroleum sector picked up slightly. The forecast for 2019 is for oil investments to increase significantly, see table 2.

Productivity in the petroleum industry is high. Even though the industry directly employs only about 1 per cent of all employees in Norway, in 2018 it accounted for 17 percent of Norway's GDP.

Development of petroleum activities has given rise to a large Norwegian supply industry. According to estimates from Statistics Norway, about 6.1 percent of total employment was directly or indirectly attached to the petroleum sector in 2017, down from about 9 percent in 2013. The highest concentration of such employment is in areas on the southwest coast, but there are supply enterprises in all parts of the country. Moreover, petroleum revenue spending via the fiscal budget also affects employment, in particular in the public sector.