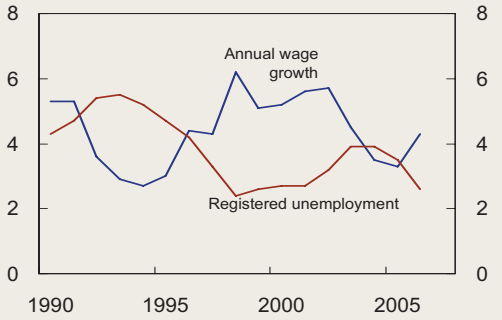
Uncertainty surrounding wage growth ahead

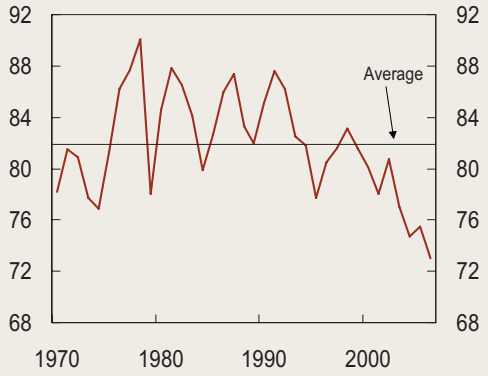
Chart 1 Annual wage growth[1)] and LFS unemployment. Per cent. Annual figures. 1990 – 2006



[1)] Average for all groups. Including estimated costs of increase in number of vacation days and introduction of mandatory occupational pension.

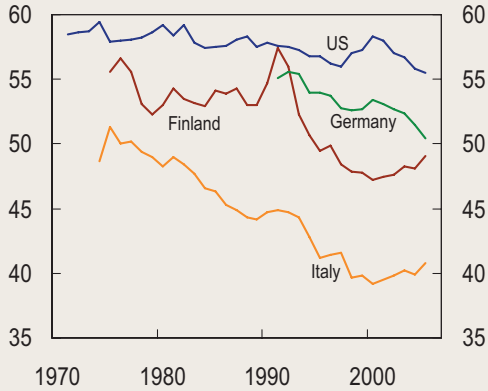
Sources: Technical Reporting Committee on Income Settlements, Norwegian Labour and Welfare Organisation (NAV) and Norges Bank

Chart 2 Labour costs as a share of factor income in manufacturing. Per cent. Annual figures. 1970 – 2006



Sources: Statistics Norway and Norges Bank

Chart 3 Labour costs as a share of GDP. Per cent. Annual figures. 1971 – 2005



Sources: Eurostat and Norges Bank

Moderate wage growth in recent years

The Norwegian economy has expanded sharply over the past three years. Corporate profitability has been solid. Unemployment has declined markedly (see Chart 1). During the expansion, wage growth has nevertheless remained moderate and lower than projected, partly reflecting a later-than-expected increase in employment and the effects of increased globalisation on the labour market and wages.

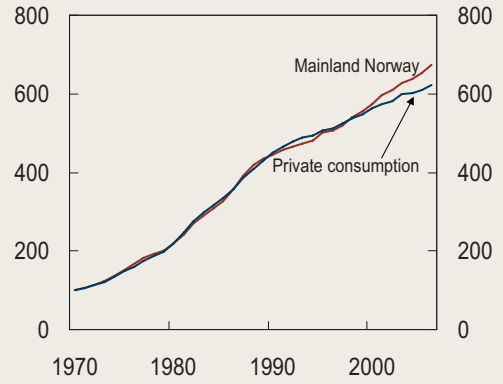
An important force that has held down wage growth is the marked increase in labour inflows from the new EU member states as from 2004. In 2006, the number of persons from EU member states on short-term assignments in Norway was estimated at about 35 000, accounting for about 30% of growth in the total supply of labour in Norway. Inward labour migration delayed the fall in unemployment in this expansion. It has also reduced bottlenecks in the economy and curbed the impact of the fall in unemployment on wage growth. Labour inflows have also had a dampening effect on wage growth, probably because the wage level of foreign workers is somewhat lower than for Norwegian labour.

Moderate wage growth contributed to reducing labour costs' share of mainland business-sector income, particularly in tradable goods sectors. In manufacturing, the wage share has shown a trend fall since the mid-1990s and the level has been the lowest since 1970 in the past few years (see Chart 2). The wage share has also fallen in many other OECD countries (see Chart 3). Emerging economies' entry into global trade has resulted in a sharp increase in the supply of low-cost labour. This has led to a fall in the global price of labour relative to the return on capital. The wage share equilibrium may therefore have been reduced. The scope for relocating production abroad may have weakened labour's bargaining power and moderated pay demands.

First and foremost, some labour-intensive production is being transferred from industrialised countries to emerging economies so that the capital intensity of the remaining production rises. This will in itself reduce the wage share in industrialised countries.

Moderate wage growth in Norway in recent years also reflects a decline in prices for imported consumer goods. This has increased labour's purchasing power without high nominal pay increases. At the same time, high global demand for commodities and energy products has resulted in higher prices for Norwegian export goods. Norway's terms of trades have increased by about 40% since 2002. The rise in prices for domestically produced goods and services, as measured by the mainland GDP deflator, has been 1% higher than the rise in prices for consumer goods since 2000 (see Chart 4).

Chart 4 Deflator for mainland GDP and private consumption. Index. 1970 = 100. Annual figures. 1970 – 2006



Sources: Statistics Norway and Norges Bank

Wage growth ahead

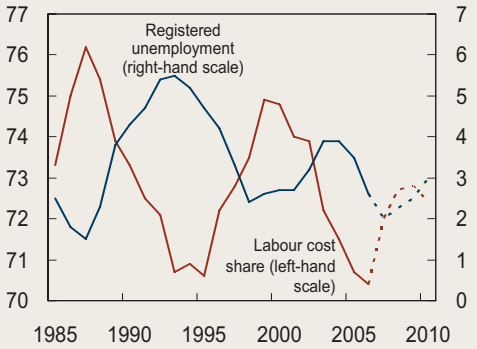
Nominal wage growth is on the rise. Bonus payments have been high in the recent past. Owing to competition for qualified labour, wages are being bid up in some industries, which seems to be generating expectations of higher wages in other industries. The experience of earlier periods of sharp declines in unemployment would indicate that wage growth may pick up fairly quickly.

Capacity constraints have now come into clearer evidence also in industries where labour inflows into Norway have been particularly high, such as the building industry. Foreign labour inflows are expected to continue to rise somewhat ahead, but competition for this labour is intensifying both because the labour market in their home countries is tightening and because several of the old EU countries have relaxed restrictions on labour immigration from the new EU countries. As a result of language barriers and other conditions that require purely Norwegian labour skills, capacity constraints are not as easily overcome in all industries. Against this background, labour inflows are not expected to moderate wage growth to the same extent ahead. The possibilities for transferring parts of production abroad may, on the other hand, contribute to holding down wage growth also in the years ahead, particularly in the internationally exposed sector in Norway. Higher wage growth in more sheltered industries as a result of solid profitability and labour shortages may then exert pressures on wage capacity in enterprises exposed to foreign competition.

The social partners' experience of strong increases in wage growth leading to higher interest rates may also have a moderating effect on pay increases in centralised settlements.

The forces that have influenced wage growth in previous years make the prospects for wage growth highly uncertain. Our projections are based on the mechanism that low unemployment leads to upward pressures on wages, resulting in high real wage growth in 2007 and 2008. This implies an increase in the wage level in relation to our trading partners. The wage share in the mainland economy is expected to show a renewed increase, but as demand in the Norwegian economy slackens and unemployment picks up again, wage growth is expected to slow. The wage share is not expected to be as high as in previous expansions (see Chart 5).

Chart 5 Labour costs as a share of factor income in mainland Norway and registered unemployment. Per cent. Annual figures. 1985 – 2010[1)]



[1)] Projections for 2007 – 2010.

Sources: Statistics Norway, Norwegian Labour and Welfare Organisation (NAV) and Norges Bank