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21 May 2010

ECONOMIC AND MONETARY POLICY IN NORWAY – A HISTORICAL PERSPECTIVE



From credit rationing and limited convertibility to capital mobility and inflation targeting

I. 1949 – 1960: Credit rationing and limited convertibility

1944: Bretton Woods system
- Fixed exchange rate
- Capital not freely mobile

1949: NOK follows GBP, and devalue against USD
- 1 USD = 7.14 NOK
- 1 GBP = 20 NOK
- 1 USD = 4 DEM

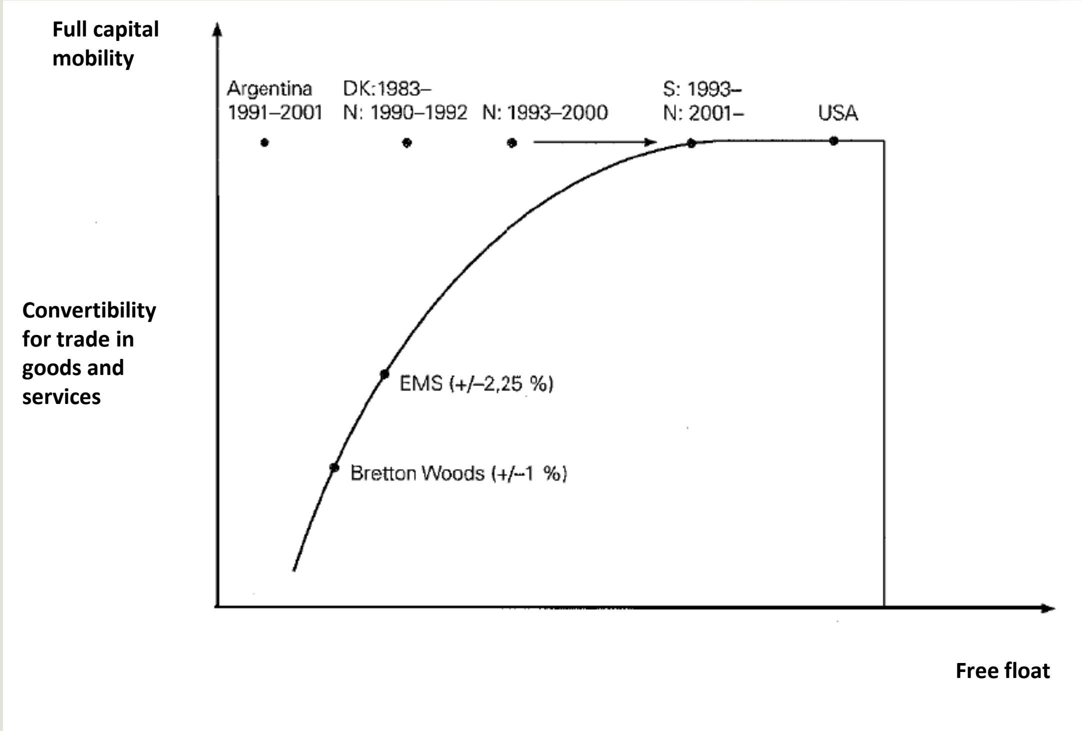


Figure 1

Policy of low interest rate and credit rationing, influencing real investments, cf. China 1998 and 2009

Not until 1959, NOK convertible for transaction on the current account, cf. China 1995

II. 1960 – 1972: Bretton Woods system collapses

August 1971: President Nixon imposes 10% surcharge on all imports

December 1971: Smithsonian Agreement

DEM and JPY revalued against USD

March 1973: Floating

But fixed system within Europe (snake)

Norway joins the snake
→ Need to have inflation at the German level



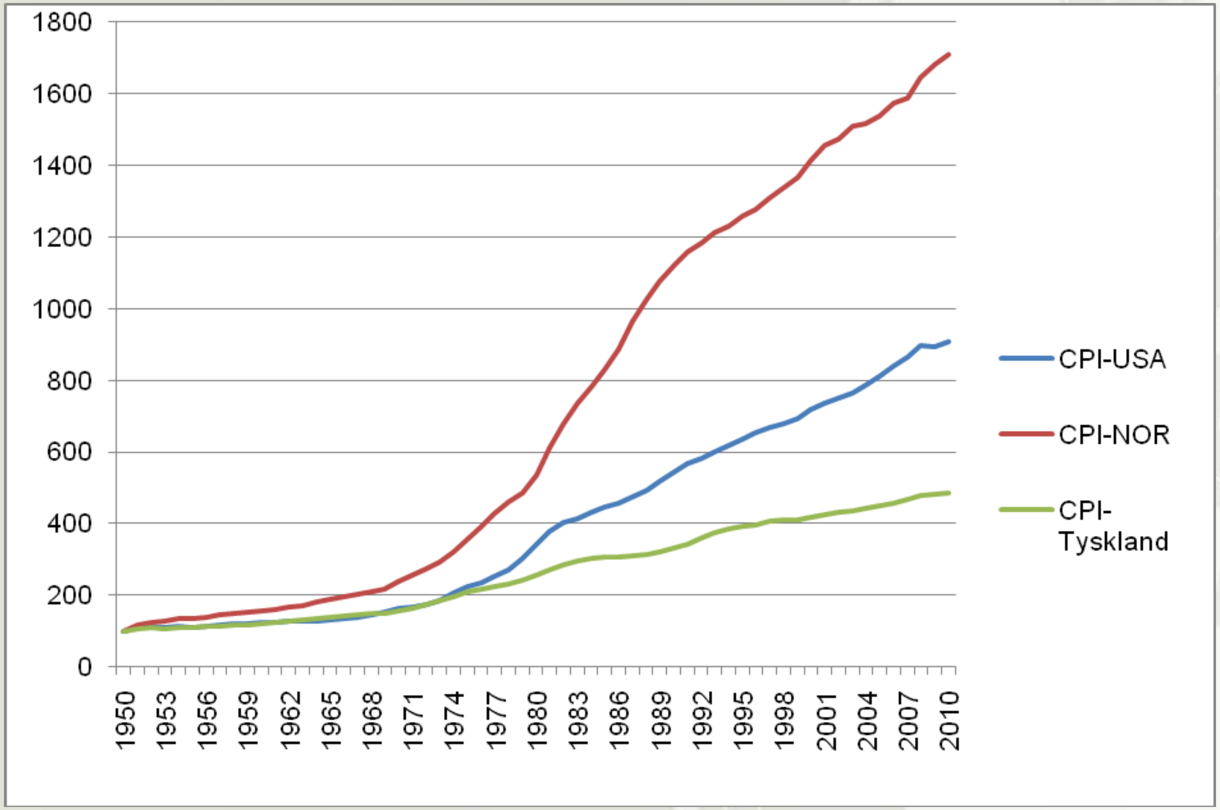

1800
1600
1400
1200
1000
800
600
400
200
0
1950
1953
1956
1959
1962
1965
1968
1971
1974
1977
1980
1983
1986
1989
1992
1995
1998
2001
2004
2007
2010
CPI-USA
CPI-NOR
CPI-Tyskland

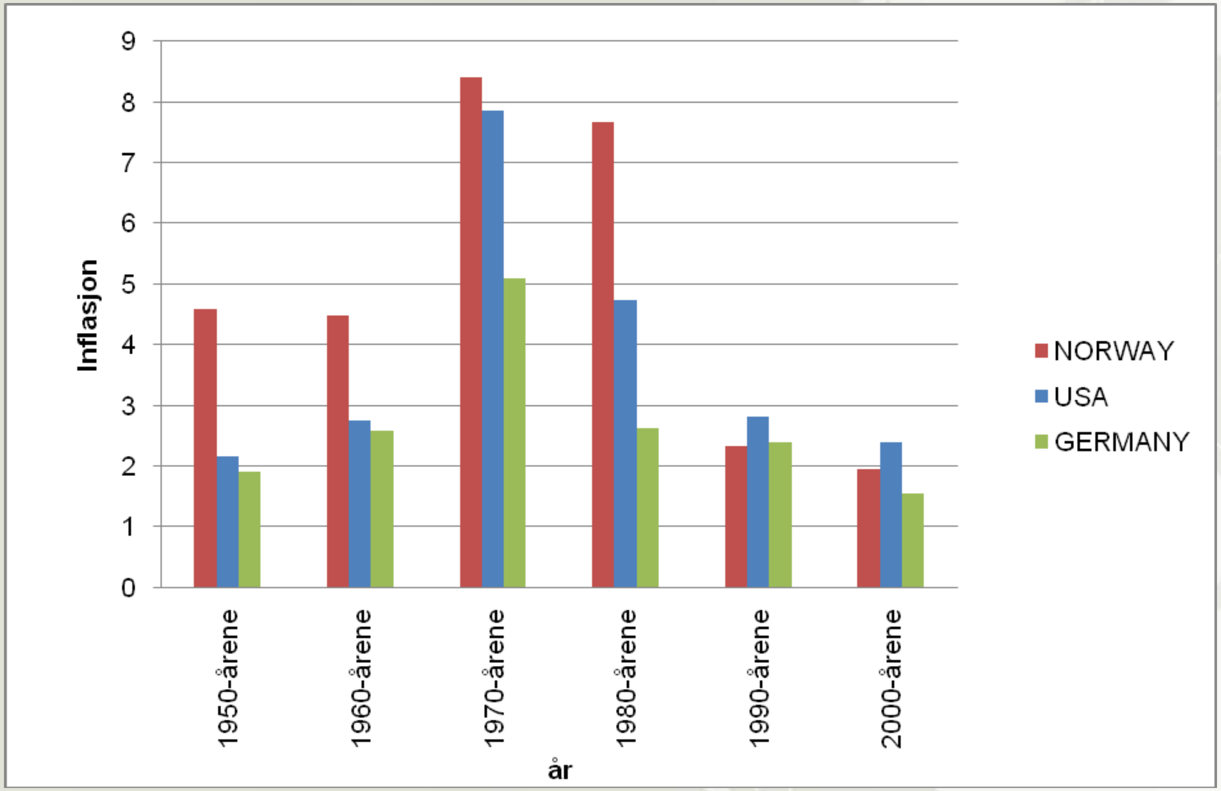
Figure 2

III. 1972 – 1978: Inflation differentials and devaluations are called for

OPEC I 1972-73 and OPEC II 1977-78, met with accomodating monetary policies

- Labor unions succeed in solid pay increases.
- Inflation picks up.
- Norway devalues by 8% in February 1978.
- Leaves the snake in December 1978

15 months wage and price freeze as of September 1978



9
8
7
6
5
4
3
2
1
0
Inflasjon
1950-årene
1960-årene
1970-årene
1980-årene
1990-årene
2000-årene
år
NORWAY
USA
GERMANY

Figure 3

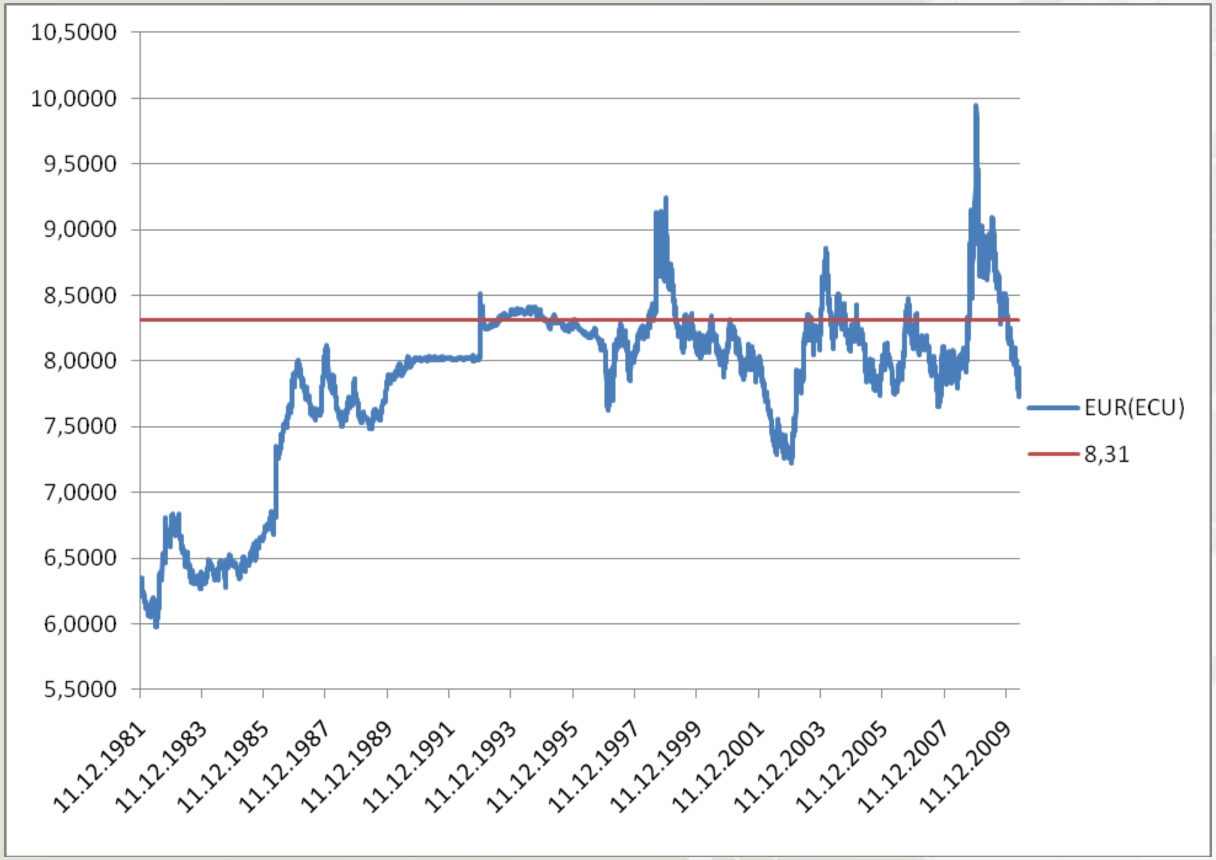
IV. 1978 – 1992: Capital mobility and floating exchange rate

Norway devalues several times

May 1986, Gro Harlem Brundtland:
”This is our last devaluation (12%)”

Stabilizes NOK against ECU (which later became euro) at

7.994 NOK = 1 ECU


10,5000
10,0000
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11.12.1981
11.12.1983
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11.12.1993
11.12.1995
11.12.1997
11.12.1999
11.12.2001
11.12.2003
11.12.2005
11.12.2007
11.12.2009
EUR(ECU)
8,31

Figure 4

1990: Opens up for full convertibility on the capital account
→ December 1992: Floating exchange rate

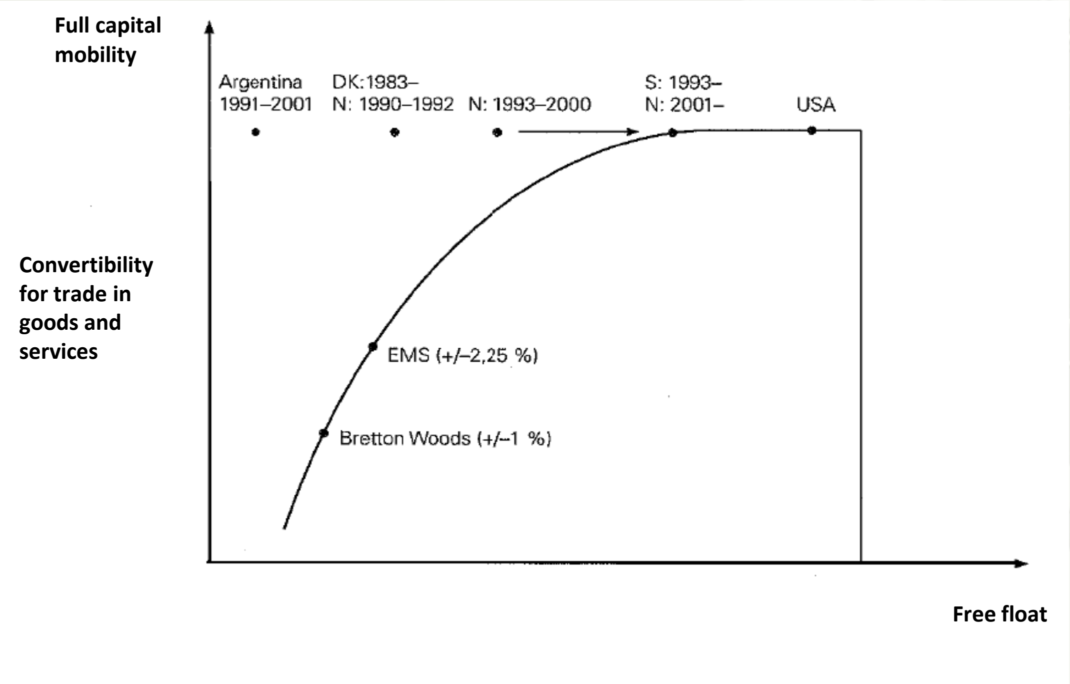

Figure 1

1992: Banking crisis, which is cleverly handled by the Ministry of Finance

V. 1992 – 2001: Restoration rule

In mid-1990s, Norway announces a restoration rule for the exchange rate: floating rate, but in the long run, try to achieve 8.31 NOK = 1 ECU

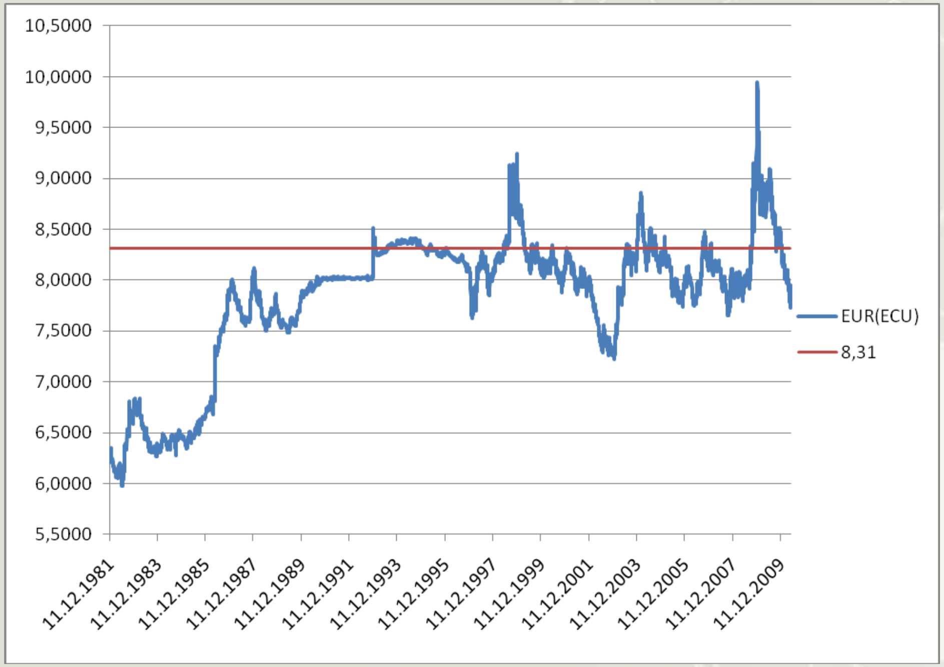

Figure 4

1999: Svein Gjedrem new governor of Norges Bank

To have a stable exchange rate against the euro, we need to have the same rate of inflation

March 2001: Inflation target adopted and also 4% rule for use of money in the State Petroleum Fund

VI. 2001 – : Inflation targeting in practice

Norges Bank ”educating” the organizations in the labor market

Raises the rate of interest in July 2002. Because of too high wage increase being negotiated in the spring

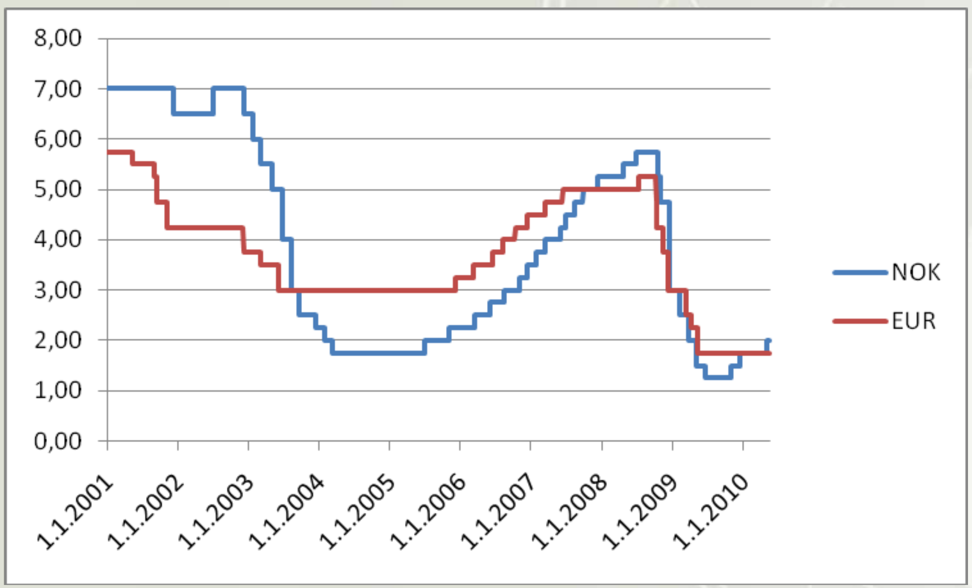

Figure 5

The NOK appreciates to 7.25 NOK/EUR in February 2003

June 2003: Norges Bank starts lowering the interest rate aggresively

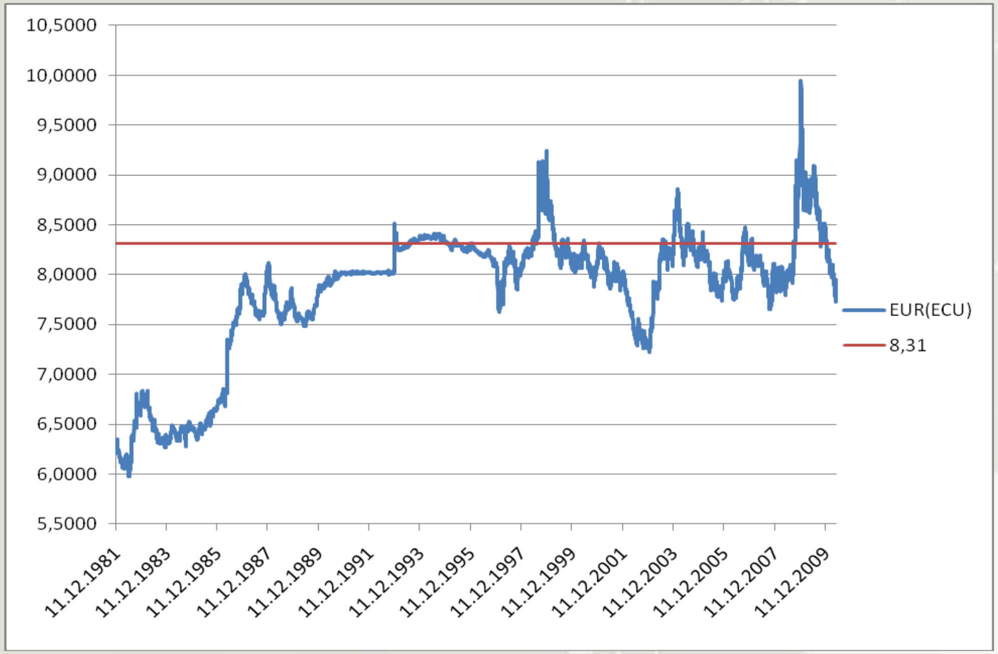

Figure 4

2008: Hit by the international financial crisis.
But banks had learned a lesson in 1992-94.

VII. Some concluding observations

- Hard to get rid of inflation. More generally, hard to get rid of bad habits, cf. current problems in EMU.
- Norges Bank and Ministry of Finance: Clever civil servants
- Responsible Labor unions and Employee Federations

→ They all had to learn the name of the game.
Difficult when the game sometimes changes

- Oil wealth – a mixed blessing
- Government – successful in devising and keeping the 4% rule
- Good luck part of the picture

    China’s rise and Norway enjoys terms of trade improvement