Ida Wolden Bache: Soon appropriate to begin easing monetary policy

Introductory statement by Ms Ida Wolden Bache, Governor of Norges Bank (Central Bank of Norway), at the press conference following Norway's announcement of the policy rate, Oslo, 19 December 2024.

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Presentation accompanying the speech

Chart 1: Policy rate kept unchanged at 4.5 percent

The Monetary Policy and Financial Stability Committee has decided to keep the policy rate unchanged at 4.5 percent.

Norges Bank is tasked with keeping inflation low and stable. The operational target is inflation of close to 2 percent over time. We are also mandated to help keep employment as high as possible and to promote economic stability.

In recent years, we have raised the policy rate significantly to tackle high inflation. Since December last year, the policy rate has been held at 4.5 percent. The interest rate has contributed to cooling down the economy and to dampening inflation. Inflation has fallen markedly and moved closer to target but is not expected to fall as fast ahead. If the policy rate is lowered too quickly, inflation could remain above target for too long. At the same time, the Committee does not want to restrict the economy more than needed to bring inflation down to target within a reasonable time horizon.

Since the previous forecasts presented in September, economic activity has been a little higher than expected, while inflation pressures appear to have been slightly lower.

The Committee judges that a restrictive monetary policy is still needed, but that the time to begin easing monetary policy is soon approaching. If developments turn out as we now envisage, the Committee will reduce the policy rate in March next year.

Chart 2: Policy rate will likely be reduced in March

The Committee projects a gradual reduction in the policy rate in the years ahead. The policy rate forecast presented today is consistent with a reduction in the policy rate to 4.25 percent in March, with a further decline to 3.75 percent by the end of 2025.

Even though the time is soon approaching to begin easing monetary policy, we must be prepared for a higher interest rate level than we had been accustomed to over the past decade. Given the current policy rate path, the average interest rate on housing loans is projected to decline from 5.6 percent today to just below 4.5 percent in 2027.

I want to emphasise that a forecast is not a promise. There is a large degree of uncertainty around the economic outlook. We are likely to see a period of increased trade barriers ahead as the incoming US administration has announced higher tariffs on imports from China among other countries. Increased tariffs will likely dampen global growth, but their impact will depend on the scale of potential increases in import tariffs and countervailing measures. The implications for price prospects, and hence for interest rate prospects, in Norway are uncertain. Domestic conditions may also lead to a different path for the Norwegian economy than we now foresee. If the outlook changes, the policy rate path may also be adjusted.

Let me say a few words about the background for the policy rate decision and the Committee's assessment.

Chart 3 Growth in the Norwegian economy has picked up slightly

Growth in the Norwegian economy was weak through last year but has picked up slightly this year. Activity is primarily being lifted by high public demand and large investments in the petroleum industry. At the same time, construction activity has shown a sharp decline. Unemployment has risen somewhat since its lowest level a couple of years ago, but in recent months unemployment has changed little.

Growth in the Norwegian economy is projected to be a little higher in the coming years than in 2024, partly owing to faster growth in private consumption. Housing construction is expected to start picking up through spring next year, but it will likely take a long time for construction activity to return to more normal levels.

Chart 4: Inflation has fallen markedly from its peak

Inflation among trading partners has moved down towards their inflation targets, and many central banks have cut their policy rates. Financial markets expect further rate cuts internationally ahead.

Inflation in Norway has also fallen markedly from its peak and faster than projected. The main factor that has pulled down inflation is the fall in prices for imported goods. The strong krone depreciation up to summer last year has restrained the decline in inflation. Inflation is still not right on the target. Over the past year, consumer prices have risen by 2.4 percent. Excluding energy prices, which fluctuate widely, inflation stands at around 3 percent.

Wage growth has accelerated in recent years. Wages rose by 5.2 percent last year and are expected to increase at the same rate this year. Wage growth is projected to slow ahead, but will still be high relative to productivity growth, which means continued high growth in business costs. This will restrain further disinflation ahead.

Chart 5. Inflation back to target without a large rise in unemployment

Given the current projections, there are prospects that wages will rise faster than prices, and most people will see their budgets stretch further. Consumer price inflation is projected to slow in the coming years and run slightly above 2 percent at the end of 2027. Unemployment is projected to increase a little, albeit slightly less than we envisaged in September.