1. Summary

The Covid-19 pandemic, infection control measures, fiscal and monetary countermeasures and international economic developments will shape the Norwegian economy towards 2025. The Government has requested the Commission «Norway towards 2025» to examine the implications for the Norwegian economy, along with relevant measures. The Commission is chaired by Jon Gunnar Pedersen. It will submit its final report in the first quarter of 2021 and will also submit interim reports along the way in order that its findings may, inter alia, be reflected in the National Budget 2021.

Covid-19 and the attendant countermeasures, domestically and abroad, caused a sharp downturn in the Norwegian economy in the first quarter. The economy quickly bottomed out, and this was followed by an upturn in parts of the economy. Production and employment levels remain significantly lower than would have been expected in the absence of Covid-19. Prevention measures will continue to guide economic policy for some time to come. In this first interim report, the Commission identifies potential effects of Covid-19 on the Norwegian economy over the next few years. The main report contents are outlined below.

Norwegian economic history over several decades suggests that the impact of an economic crisis on economic output, employment and government budgets, is shaped by domestic factors, even when triggered by circumstances outside the borders of Norway. Robust government finances, a strong public sector, a finely meshed social security net for individuals, responsible tripartite labour market collaboration, powerful automatic macroeconomic stabilisers, floating exchange rates, as well as tailored regulation and supervision – especially of the financial sector – are some of the factors that serve to reduce the impact of negative impulses on the Norwegian economy.

The capacity of the authorities to evaluate, launch, calibrate and roll back emergency measures is of significance to how a crisis will unfold. Measures may shorten a crisis and make it less severe. Measures may also influence how the negative repercussions of a crisis affect various parts of the population. Experience from previous crisis management in Norway suggests that insufficient weight may be attached to long-term effects of emergency measures, possibly because of strong government finances. Norway is facing considerable structural challenges in its economy, relating to productivity, industrial structure, demography and climate, which need to be addressed. These challenges increase the importance of the long-term effects of current crisis management.

The Covid-19 crisis is different from earlier crises in some respects. The effects in the first phase were severe and unpredictable. Considerable uncertainty held back household demand and business investment, especially in the first phase of the crisis. Measures had to be designed without much relevant experience, from previous crises or from other countries, of how these worked. This lack of experience affected all parts of society, including households, businesses and government agencies, but the population demonstrated considerable ability and willingness to change in a complex and fluid situation. Covid-19 was also a new challenge for academic institutions in their quest to develop and structure knowledge.

Covid-19 triggered exceptionally extensive government measures, which roughly can be grouped into two categories. Those are the infection control measures; and the measures to counter the economic effects of the outbreak and said infection control measures. These two

categories of government measures differed in their impact on the Norwegian economy. The infection control measures served to slow down production and employment. The economic measures have stimulated production and employment, whilst seeking to spread the income shortfall more evenly. Many people are nonetheless worse off, whilst large groups have not yet suffered any major negative impact from the crisis.

The balance between these government measures applying the «brake and accelerator», respectively, has changed over time. The most comprehensive infection control measures that were introduced on 12 March, were rolled back in the second half of April. The economic countermeasures were launched swiftly. These measures have not yet been scaled back significantly. An exception is the compensation scheme for businesses suffering large sales reductions, which was discontinued at the end of August. The economic measures have been exceptionally powerful, which contributed to the economy bottoming out already in April. The subsequent period has been characterised by a faster rebound than would normally be experienced in times of deep economic crisis, although the activity level remains significantly lower than at the beginning of the crisis.

The crisis has reduced economic output. Measured by mainland Norway production shortfall, this loss amounted to about NOK 14,700 per capita over the period from February to July. Said production shortfall is reflected in lower wage income for private sector employees, as well as lower business profits. Automatic stabilisers and government economic measures reduce the loss of income for wage earners and businesses, thereby shifting a major portion of the financial cost to the State.

As the most restrictive infection control measures have been lifted, locked-down industries have to some extent been able to resume their operations. Some sectors nonetheless remain severely affected. This applies, in particular, to the culture sector, as well as aviation and the travel industry, especially with regard to travel between Norway and other countries. Besides, export businesses are affected by low activity on the part of Norway’s trading partners.

We are now in the second phase of Covid-19 in which we are learning to live with the disease. The prevalence of infection has at times accelerated in localised areas. Outbreaks have been met by local countermeasures, as well as travel restrictions. Effective systems for testing, tracing, quarantining and isolation (infection tracking) are important to limit and stop local surges in infection rates. However, experience with infection tracking in other countries and geographic areas in Norway suggests that it is difficult to keep infection rates under control over time through infection tracking alone, especially in less than strict of compliance with basic infection control rules. Quarantine may be a costly measure if many people are infected, and infection imports from abroad may happen even if infection rates are kept low in Norway.

A third phase will ensue when the infection risk has for all practical purposes been eliminated, for example through vaccination. In Norway, this third phase may perhaps be reached over the course of the next year, but it may also take significantly longer. We are dependent on effective vaccines being developed outside Norway. Globally – and especially in poor countries – there is considerable uncertainty as to when such a third phase will be reached. Conditions in other countries may prolong the need for economic measures in Norway.

The Commission will through the autumn be gathering experience and assessments, both domestically and internationally, on restructuring needs, the distribution of negative effects and the design of policy measures. The Commission will focus, in particular, on charting and examining how measures should be oriented to avert unwanted effects and contribute to solving some of the major structural economic challenges facing Norway:

- An expansionary fiscal policy stance during the crisis involves intergenerational redistribution. Future challenges as the result of, inter alia, aging may be further exacerbated if fiscal policy does not revert to a more neutral stance in response to the upturn. Expansionary policy in a subsequent recovery phase may entail persistent structural effects. One potential structural effect could be a transfer of resources from the export industries currently suffering from lower international demand to industries that devote such resources to meeting domestic needs. This will add to the challenges posed by the transition away from petroleum-based exports.
- Temporarily supporting businesses that have suffered a loss of earnings and expanding the scope of furloughing rules may inhibit restructuring of the economy. Such measures should be discontinued fairly early in a recovery phase, and earlier than measures that may improve the capacity for restructuring and growth. The public sector's role in income support for households should not be replicated vis-à-vis businesses.
- Behavioural changes during the crisis have had a positive impact on the environment and the climate, although through a steep decline in production and employment. The Commission will examine whether some of the behavioural changes during the crisis may turn out to be permanent, and how to sustain positive effects by according priority to initiatives that offer the highest possible cost-benefit ratio.
- The low employment level during the crisis increases the risk that individuals will drop permanently out of the labour market. This risk is highest for young employees with a weak labour market affiliation. Government-funded demand and low interest rates may bring down unemployment and reduce the number of businesses folding, but offer no guarantee of long-term jobs. The Commission will also examine more targeted measures for preventing jobseekers from dropping permanently out of the labour force.
- The crisis has reinforced the trends towards more pervasive digitalisation of society. The Commission will examine the implications of this for growth and emergency preparedness. These may include benefitting from demand having reached a critical mass during the crisis. Besides, public infrastructure investment may be better targeted to reinforce the positive effects of digitalisation. Moreover, public funds allocated to risk sharing with the private sector may be channelled to industries offering a sustainable growth potential.
- A well-designed tax system may support growth as we chart a course out of the crisis. The Commission will reflect on whether any specific changes might have a particularly beneficial effect on labour force participation, business solvency and sustainability as we set out to put the crisis behind us.
- International value chains were put to a serious test during the pandemic. It appears that many of these passed that test with flying colours. The vulnerabilities revealed may still bring about changes to the trade-off between efficient production and emergency preparedness measures. Vulnerabilities may cause geographical changes to value chains and increase the focus on national ownership of strategic industries. The

commission will reflect on whether formal collaboration with same-minded countries may strengthen Norway’s security of supply in preparation for future global crises.