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"A lack of understanding of what money is, has given a false understanding of what the oil money is and can be used for." PAGE 12 Arno Mong Daastøl

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"The budget rule" is based on financial misunderstandings, and damage economic growth and employment

The Petroleum Fund and the LO passiveness

Arno Mong Daastøl
IN OTHER WORDS

FACTS:

Debate on the Petroleum Fund:

● Government Pension Fund ("Pension Fund") consists of the state's total oil revenues and the fund's own return. The Ministry of Finance manages the fund using the National Insurance Fund and Norges Bank.

● The debate surrounding the use of oil money suffers from poor understanding of financial logic and international accounting, says Arno Mong Daastøl.

● The use of oil money does not create inflation and pressures in the Norwegian economy, but create jobs for our trading partners and lower Norwegian costs, claim Daastøl.

● He specifically challenges the Trade Unions to demand a strategic plan to ensure wealth creation and employment.

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Norway has recently celebrated 10 year jubilee for “the budget rule", which promotes moderate use of oil money. Finance Minister Sigbjørn Johnson 29 March expresses what a collective media corps, experts and politicians believe, in the article "The budget rule serves us well." But is this really so certain?

If one holds a hammer back-front, it may well be that one gets a nail into the wall, but a little better knowledge could have helped. Action requires that we understand the situation. The budget rule, however, is based on lack of insight into what the oil money is and can be used for.

For decades, Parliament has directed the use of oil money after the belief that heavy use of oil money in the Norwegian economy will overheat the economy and pressures and "Dutch illness" – leading to inflation in labour and property prices, increased interest rates and -currency value. This will weaken the Norwegian industry in international competition, and lead to unemployment and loss of welfare. Therefore, the oil money has been preserved financially abroad, rather than using them on real demand and invest them in long-term Norwegian value creation. The title of Professor Steinar Holden's article (March 31) "Put the money abroad" is illustrative.

This financial-oriented policy for the oil fund were recently criticised by Professor Michael Hudson and Civ. Eng. Øystein Stray Spetalen, who want more real economic- and industrial-oriented policies.

Hudson and Spetalen argument was that healthy investment in infrastructure reduces costs for business and society overall price level. This increases production capacity and -competitiveness over time. Spetalen and Hudson have historical experience on their side - in the UK, USA, Germany, Sweden, Japan, Taiwan, Korea - and now China. - Besides, if the oil money is used for imports that compete with Norwegian products, this may also lead to lower inflation.

"Simple facts about how oil money is actually used has been obscured in the public debate."

In *Aftenposten* 18 March Michael Hudson, was criticised by chief economist of the Trade Union Confederation LO, Stein Reegård. Reegård promotes the afore-mentioned conventional standpoint, claiming that Norway does not have manufacturing capacity to use oil money, for example, to infrastructure. "The budget rule" which restricts the use of oil money, is based on such conventional arguments. It is a misunderstanding, and harms economic growth and employment - both in Norway and among trading partners.

Reegård is in contrast to Hudson, not a weather-beaten expert in international payment balances - since the 1960s. Reegård do not understand that because oil money is foreign currency, they are claims on foreign production - not on Norwegian production. The use of oil money is thus not inhibited by Norwegian production capacity.

The debate surrounding the oil fund is suffering from a lack of understanding of financial logic and international accounting. A lack of understanding of what money is, has given a false understanding of what the oil money is and can be used for. Like all other credit, money and foreign currency are legal terms that symbolise social relationships. They are ideas, not material things - as many economists and politicians give the impression of believing. They are legal claims with a claim on the issuer to supply the bearer with resources and products. Foreign currency is a demand on foreign resources and production.

Hudson and Spetalen thus have yet another argument on their part, because oil is not paid in the Norwegian money. Oil money cannot possibly generate press in Norway, for the simple reason that this currency is a claim on foreign production - and thus only creates demand and inflation pressures abroad - quite the opposite of the official explanation. Increased use of oil money - earned foreign currency - leads to increased demand abroad.

So the use of oil money first and foremost functions as a growth stimulus for our trading partners. Our use of oil money to import, therefore, helps our trade partners to sustain their production and employment. The challenge for us is to use oil money in a way that also creates lasting growth potential at home.

We repeat: Oil money can only be used to import or be given away overseas. Norway exports oil and gas and receives payment - in foreign currency: Norway exports (in order) to import.

Conversely, foreign aid in Norwegian crowns does not increase employment in developing countries, but leads to increased economic pressure in Norway - because it is claims on Norwegian production. The Marshall Plan from the U.S. to Europe (1947-1951) illustrates this: It gave Europe much-needed goods and provided employment in the United States.

Such simple and logical facts have for decades been misunderstood by Norwegian economists and politicians. This has led to long and totally unnecessary debates and a lot of wasted time and resources that should have been spent on real problems. It is sad that such things can happen - after expensive advice from so many experts.

Simple facts about how oil money is actually used has been obscured in the public debate. The fact is that oil companies in Norway exchanges some of its foreign currency income in Norges Bank to pay the oil tax in Norwegian crowns. These Norwegian crowns then go into the state budget, and do not differ from other tax money. When politicians talk about the use of oil money, it is therefore these Norwegian kroner they are talking about - NOK issued by Norges Bank.

What then happened to the foreign currency that oil companies redeemed? It went into the Norges Bank's so-called "petro buffer portfolio, which is part of the foreign exchange reserves.

The misguided use of oil money is the reason that the governing economists and politicians may argue that increased use of oil revenues increase pressures in the economy. Apparently, currently used oil money on an equal footing with other tax dollars, while they really ensures that we have on going surplus on our balance of payments with foreign countries.

A small digression: - If we assume that we have a 50% import leakage, and the government claims to have used such as "10 billion extra oil money" directly (from the state budget), it has actually only spent 5 billion indirectly (through tapping the foreign exchange reserves).

The relationship is as follows: As long as the state budget is directed to a demand for Norwegian goods and services, the oil money in foreign currency remains unused. But insofar as the state budget results in increased imports this drains Norges Bank's foreign exchange reserves accordingly. The currency "left over" will be invested abroad, and increases the Oil Fund.

A NEW DRIVE?
Norway needs a national plan for import and development with priority investments. Norway has neglected this for 40 years - and instead used a dangerous saving policy writes Arno Mong Daastøl.
ILLUSTRATION: Labour Party Poster from the 1945 Campaign ARBARK

The use of oil money is a question of what Norway will buy abroad. To increase future value creation Norway should buy overseas competence, in terms of research and education. Moreover, one should invest in the maintenance and improvement of infrastructure, which includes education, research, health, energy, transport and communication. This provides common services that all industries rely on, and it is up to individual companies to take advantage of these improvements.

It is essential to combine these fields, so that e.g. construction of transportation also promote innovation, own research, bureaucratic competence, health and environmental protection. PRT or “taxitracks” is one such example - automated electric cars on elevated tracks, well suited to Norwegian terrain. In 2010 Sweden certified these for public transport and the government declared them a national priority. Is Norway also sleeping here?

Since Norway depends most of all on her neighbours, it is important to support development of these, for example through the development of Nordic infrastructure. There will also benefit ourselves, through better export opportunities. Besides, we might learn to make long-term and coherent plans in place of today's splash show improvements.

The experience we gain by controlling development in neighbouring areas, we in turn pass on to the world. We can learn from the Kuwait Development Fund and China, which for decades has helped many underdeveloped countries to build their country.

Almost any degree of risk of loss and unprofitability on projects in infrastructure cannot possibly be worse than the oil fund's losses of 800 billion during the recent financial crash, however much they claim that such “burned” money can be revived later on.

Experience shows that more major economic crashes, and natural and political upheavals will come ... So if Norway were to secure her assets abroad, Norway would had become a political player abroad, in the old imperial tradition. This is neither possible nor desirable. The Petroleum Fund's foreign assets are therefore totally at the mercy of international events, which we hardly may influence.

When Norway pours thousands of billions into the already established financial papers, this inflates their prices and contributes to unstable bubbles. Additionally, as means of payment are removed from the real sector, this creates underconsumption and unemployment. The Parliament's petroleum fund policy will thus contribute to international instability, underconsumption and unemployment. Nothing constructive is thus done with Norway and the world's problems, on the contrary.

Taking into consideration both ourselves and the outside world - and for ethical reasons above all - it is high time to go from such a unilateral passive and risky financial positioning of oil wealth, and rather to include an active industrial and productive use of oil money.

Increased use of oil money does not cause inflationary pressures in the Norwegian economy, because they are claims on foreign output - and therefore rather increases the demand abroad. The use of oil revenues are not constrained by production capacity at home, but on the contrary, extend it and increase Norwegian competitiveness - if you invest in infrastructure in the broadest sense. A wise strategy for import of capital goods and knowledge will push prices down at home, and increase the competitiveness of Norwegian and value creation - in addition to providing our trading partners jobs.

In order to receive productive imports on a large scale, this will require a national import- and development plan with prioritised investments - preferably in infrastructure in the broadest sense. Norway has neglected this for 40 years - and instead followed a harmful savings policy.

The LO is completely passive regarding this important issue, and thus fail to use the oil fund to promote the long-term interests of her members - in the LO and in sister organisations abroad. As chief economist of the LO, Reegård should require such a development, which can ensure long-term wealth creation and jobs.

Arno Mong Daastøl