Macro & FICC Research

Published: 2022-04-19 12:45

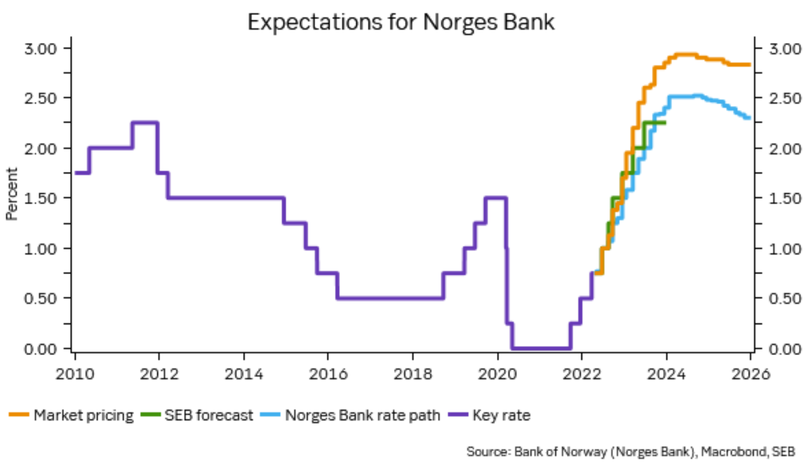
What's up, Norway?

Mixed data keep Norges Bank's course steady

Economic data since the release of the March MPR have been mixed, but the market remains firm on pricing in more aggressive rate hikes than implied by the rate path. Almost four rate hikes are discounted for the remainder of this year and the key rate is seen peaking around 2.90% vs. Norges Bank's 2.50%. We believe pricing is too aggressive. This, combined with other factors, strengthens our belief that we are approaching the time and levels for when the NOK strength will begin to abate.

The market is running ahead of the rate path

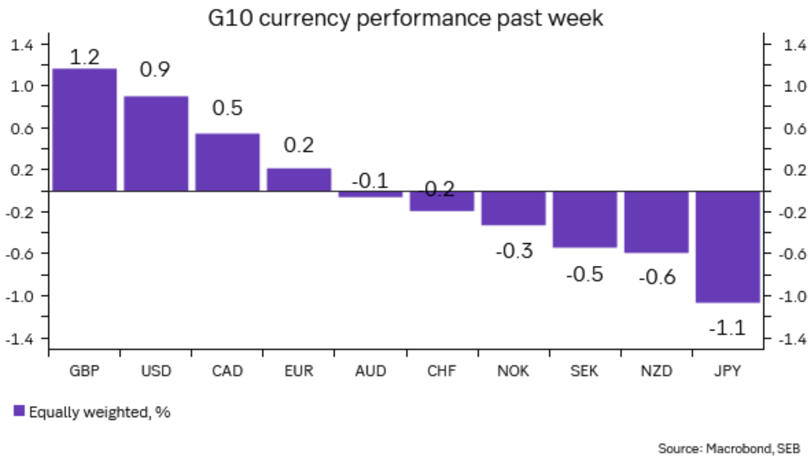
One month has passed since the March rate decision and MPR when Norges Bank restrained the upward revision to the rate path arguing that "Uncertainties relating to the economic outlook and households' response to higher interest rates warrant a gradual rise in the policy rate". The market has taken more notice of the Committee's risk assessment which concluded that "If there are prospects of persistently high inflation, the policy rate may be raised more quickly". The market still discounts a total of just below 100bps of hikes for the remainder of this year, and expectations for 2023 has increased from 80bps to 115bps implying a key rate of approx. 2.85%. While the rate path peaks at 2.50%, the market discounts a peak at 2.95%. We continue to argue that current pricing is too aggressive and believe that the strong transmission mechanism will result in a terminal rate around 2.25-2.50%.



Macro developments since the March MPR have been mixed. Unemployment has surprised on the downside and the wage settlement in the leading manufacturing sector points to upside risk to Norges Bank's estimate for annual economy-wide wage growth of 3.7% this year. Though this should add upside pressure on CPI-ATE, spot inflation surprised by holding steady at 2.1% y/y in March. Monthly volatility can be high, we have revised our CPI-ATE forecast lower though it remains above Norges Bank's trajectory in 2022. The rebound in economic activity from the lifting of pandemic-related restrictions has been more moderate than envisaged; mainland GDP growth increased 0.5% m/m in February vs. Norges Bank's 0.8% m/m estimate. Overall, data so far do not support market's aggressive pricing for Norges Bank. Important data releases ahead of the intermediate rate decision on May 5 are limited and centered on the Business Tendency Survey (Apr 21), household goods consumption (Apr 29) and registered unemployment (Apr 29).

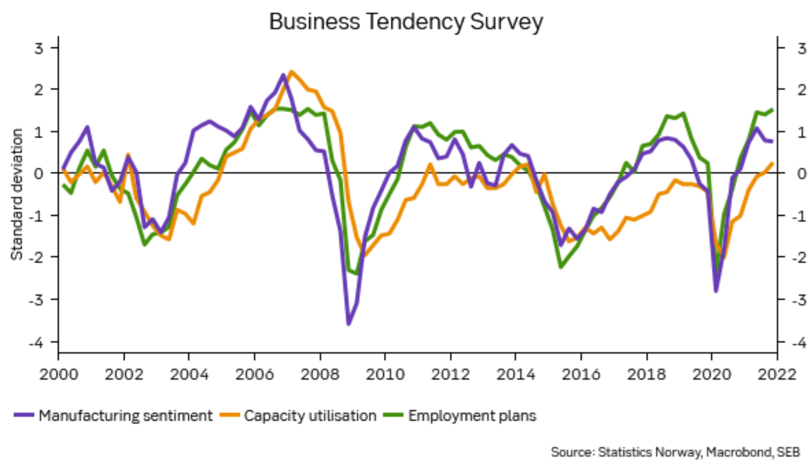
NOK approaching a turnaround, especially versus the SEK

EUR/NOK rose by 0.7% last week which was a period when NOK was among the weaker G10 currencies. The SEK, NZD and JPY were even weaker while GBP and USD were the top performers. We believe that we are approaching the time and levels for when the NOK strength will begin to abate. The seasonal pattern indicates NOK strength foremost the first half of the year and we believe, as introduced in Currency Strategy: "2022 the year of the laggards" in Feb 2022, that the longer we got into this year the more the laggard central banks would come into focus and in turn strengthen their currencies. The ECB at their recent meeting last week did not make any changes so versus the EUR it might be a bit longer before there is a turn, but the SEK still stand a good chance of strengthening versus NOK backed by the Riksbank coming closer to hiking rates. Read more on our NOK/SEK thoughts in What's Up, Sweden? from last week.



A first glance at manufacturing sentiment following the invasion of Ukraine

On Thursday, Statistics Norway publishes its quarterly Business Tendency Survey. The aggregated indicator fell marginally to 8.6 in Q4 2021 but remained in expansionary territory. Supply problems remained a limited factor with manufacturers referring to shortages of raw material, energy and qualified labour. This picture was reinforced in Norges Bank's Regional Network Report published in mid-March. However, the network survey was conducted prior to the invasion of Ukraine. As such, the upcoming Business Tendency Survey will give important input on how the war in Ukraine has impacted manufacturers' assessment of supply problems and price pressures. Norwegian manufacturing PMI tends to be very volatile and thus less reliable but indicates a small decline in sentiment in Q1.



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