

# Executive Briefing

## Inflation fight continues as China reopens

**Easing pandemic curbs in China, global recession fears and central bank rate hikes continued to drive markets during December.** China stepped up its easing of Covid-19 restrictions on a nationwide basis and a clear shift has taken place in official communication, with emphasis on economic recovery. The reopening in China continues to drive a Covid surge, but some big cities already indicate a peak is close and within a month most of the country has likely peaked. The Chinese reopening happened faster than we expected, and we have revised our China growth outlook upwards (see *China Outlook: Earlier reopening to drive faster rebound*). While the Chinese re-opening is positive from a global growth perspective, it also means China will return as a reflationary force through increased demand for commodities, complicating the inflation fight for central banks.

**Economic data remains overall consistent with our expectation of a mild global recession hitting in 2023.** US leading indicators signalled a further slowdown of the growth momentum at the end of Q4, although data also continues to paint a strong picture of services activity and the US labour market, with high wage inflation. In Europe, economic sentiment rebounded, but remained at subdued levels. With households facing headwinds not only from higher energy bills, but also rising interest rates, we still think a double dip recession is a real risk in the euro area and challenging times lie ahead especially for Germany's economy.

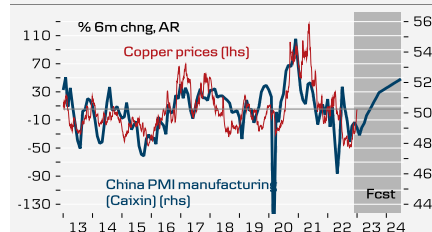
**After months of debate, the EU reached an agreement on a natural gas price cap of EUR/MWh 180, but with a range of caveats.** The cap will take effect from 15 February 2023 and initially apply to Dutch TTF gas contracts traded on all European trading hubs for supplies 1M, 3M and 1Y ahead. Near-term, the inflationary implications of the cap are limited, as natural gas prices currently trade below pre-war levels. However, with the IEA already warning of a 30bn cubic metre shortfall in EU gas supply next year and exchange providers warning about financial stability risks due to more trading moving to unregulated over-the-counter markets, it is not clear that the cap ultimately solves more issues than it creates. With regard to the energy crisis, Europe continues to move on thin ice.

Despite emerging signs of peak inflation on both sides of the Atlantic, global central banks remain firmly in hiking mode. In the US, the Fed hiked policy rates by another 50bp as expected, but Fed Chair Powell also left a door open for more modest rate hikes in the future. We maintain our call for terminal rate at 5.00-5.25%, well in line with the Fed's own new projections (see *Fed review*). The ECB also delivered a 50bp rate hike, but with a clear hawkish message, that further 'significant' rate increases will be needed in 2023 to quell underlying inflation pressures, and we have updated our ECB call to expect a peak of 3.25% for the deposit rate in 2023 (see *ECB review*). Bank of England also joined the 50bp hiking club, but struck a more dovish message on future hikes, in light of the weakening British economy (see *Bank of England review*). With its subdued inflation pressures, Japan has long been an outlier in the global monetary tightening race of 2022. However, during December, Bank of Japan surprised markets by changing its yield curve control policy and despite record bond purchases, a policy rate hike in H1 23 now seems a clear possibility (see *Flash Comment Japan - BoJ tweaks YCC - Global bond market takes a hit*)

### Key points

- The outlook for the Nordic economies in 2023 has worsened somewhat as a consequence of higher inflation and interest rates, see our new *Nordic Outlook* published today.
- Central banks, especially the ECB, maintain a mostly hawkish stance, and will have their efforts to fight inflation complicated by the faster than expected reopening in China.
- December saw higher bond yields and mixed equity markets, while the USD weakened and Danish mortgage bond spreads tightened.

### China to turn into an inflationary force again in 2023



Source: Macronand Financial, Danske Bank

**Denmark**

Economic data paints a mixed picture as business sentiment has stabilised but at a low level. We expect a GDP decline of 1% in 2023 and a modest rise in unemployment. Central wage negotiations in the private sector have begun and will be difficult, as workers seek more compensation for high inflation while many businesses are also facing higher costs. There is a risk of strikes during the spring. A left-right majority government has been formed and has signalled that fiscal policy will be broadly in line with the proposal from the old government, which is close to neutral. The Nationalbanken followed ECB's 50bp rate hike but intervened for DKK 5.8bn in December against the DKK, and we expect that Danish rates will be hiked about 10bp less than the ECB's going forward.

**Sweden**

Growth held up better than expected in the third quarter and at the beginning of the fourth quarter and hence have led us to revise up our growth forecast for 2022, but we remain negative about growth in 2023. The labour market has proved very resilient, but we consider it only a matter of time before things take a turn for the worse here as well. We now expect the policy rate to rise by 50bp in February to 3.0%, not because core inflation has surprised to the upside, but more that the ECB has announced a much more aggressive stance than before. Depending on how inflation moves in the first quarter of 2023, we think the Riksbank may then need to hike one last time by 25bp in April, taking the policy rate to 3.25%. Housing prices seem to stabilise somewhat in November and December despite the Riksbank raising its policy rate by a further 75bp during the same period. We expect declines to resume.

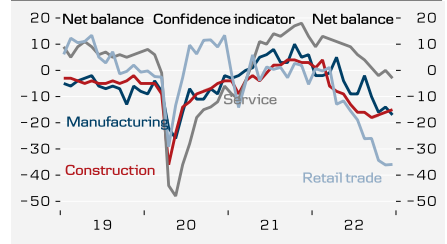
**Norway**

The regional survey points to a clear slowdown going forward. The aggregated output index corresponds to annualised growth of around -1.1% over the next six months. The slowdown is broad-based, with the exception of oil-related industries, and as a result, capacity utilisation is coming down (from high levels). Firms continued to revise down their expectations for employment and investment, although both indicators are still marginally positive, and profitability is still falling sharply. The labour market tightness continues, although unemployment has levelled off. The housing market continues to weaken, with falling prices, lower demand and an inventory build-up, although from very low levels. In terms of GDP growth, we have revised up our estimate for 2022 but lowered the forecast for 2023 to 0.6%.

**Finland**

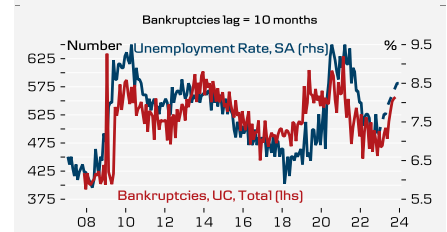
In Finland, economic activity continues to cool down at a moderate pace. Consumer and business confidence indicators have weakened. We expect the GDP to fall 0.7% in 2023. Open job vacancies are still plentiful in many industries, which gives a buffer against the economic adversities. Consumers spend more money in retail trade, but due to high inflation (9.1% in November) less goods have been bought. Inflation and rising interest rates worry consumers. Demand for housing loans has decreased a lot. Housing prices have fallen 5% from the peak in June. Prices are likely to fall slightly more, but there is no pressure for a large price movement. Housing construction outlook has weakened and activity is going to fall. Sanctions and voluntary boycotts have halted most of the foreign trade with Russia. There will be additional investment into domestic energy and national security. Lack of electricity is a worry during this winter, but Olkiluoto 3 nuclear reactor launch should ease the situation in March 2023.

**Business sentiment weakening again**



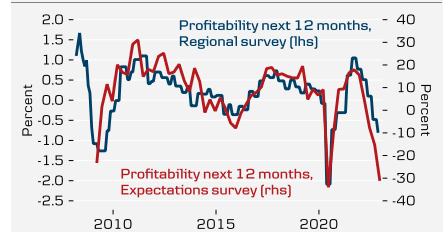
Sources: Statistics Denmark, Macrobond Financial

**More bankruptcies to come**



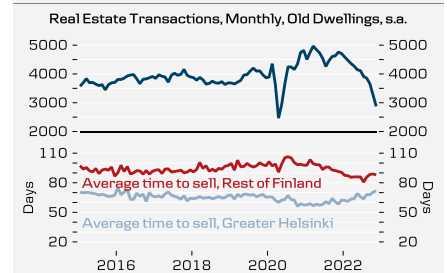
Source: Macrobond Financial

**Profitability under pressure**



Source: Norges Bank, Macrobond Financial

**Housing market slowing down**



Source: Macrobond Financial, Statistics Finland

### Currency markets

The last month in FX markets has generally been characterised by declining volatility and a decline in energy incl. oil and natural gas prices. The Norwegian krone has suffered not only from a weakening energy complex but also from weakening domestic data suggesting that Norges Bank might already have delivered the last rate hike of this cycle. On the other hand, lower energy prices have contributed to lifting HUF, CZK and PLN alongside the JPY which also saw a boost from Bank of Japan’s (surprise) initiating the beginning of the end to its yield-curve-control. The autumn weakness of the USD extended into December amid markets pricing out more rate hikes from the Fed whilst the ECB firmed its hawkish guidance at the December meeting. SEK and GBP were also among the Christmas underperformers while EUR/DKK remains close to historical FX intervention levels from Danmarks Nationalbank, and indeed triggered intervention for DKK 5.8bn.

### Bond markets

During December, most central banks confirmed that they are still tightening policies to rein in the too high inflation pressure, yet slowed the hiking pace. Rates markets sent global yields some 30-50bp higher seen over the month as a whole, but has retraced half of the yield rise at the start of the year. Looking ahead, we see further upside to rates near term driven by aggressive policy tightening, but ultimately lower bond yields on a 12mth horizon in anticipation of weaker economic activity and inflation decline. The Danish central bank has intervened during December to weaken the strong DKK vs. EUR and the speculations regarding less hikes than ECB continue to support the front end of the bond market. Spreads on DGBs vs. Germany remain tight. Mortgage spreads tightened during December but have widened up a bit again after the reinvestment flows from coupons and redemptions from the mortgage market are finished.

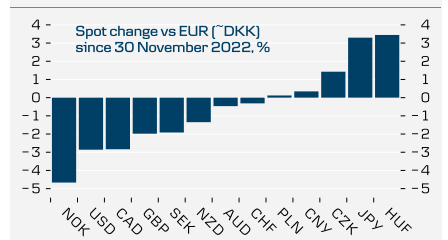
### Credit markets

December was characterized by seasonally very low issuance, with primary market activity coming to a stop after the first week of the month. Spread developments were divergent, with cash bonds tightening slightly during the month while CDS indices lagged somewhat behind and most visibly for iTraxx Crossover, which widened 15bp. The underperformance of CDS indices was driven by significant widening on the 15/16th December where Crossover widened a total of 70bp following the ECB meeting, which weighted more on synthetics than cash bonds. The first couple of days of January have, as usual, been very busy, with mostly financial issuers rushing to the market. Issuance, which has included several AT1 transactions, has in general been very well received.

### Equities

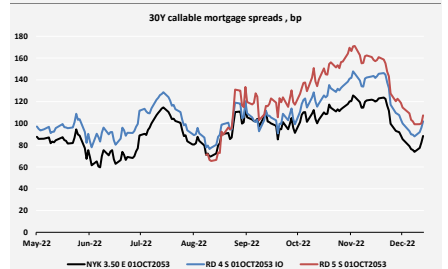
Nordic equities were little changed in December while the US came off its highs, as big tech weighed on performance. After the strong November performance, inflation relief is no longer enough to spark new rallies. Lower inflation is however continuing to shift sector performance in favour of yield sensitive sectors like real estate or medical technology, or companies that have struggled with cost inflation. For the overall market however, short term support for equities from bearish positioning has been emptied out. Therefore, we expect macro data to play a bigger role in the direction for equities, where we see risk of more weakness ahead.

FX. Sorted spot returns vs EUR



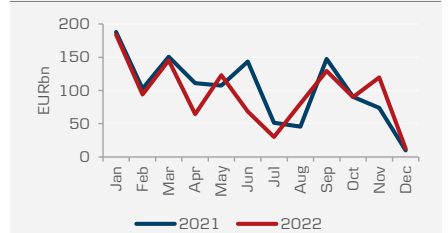
Past performance is not a reliable indicator of current or future results. Source: Macrobond Financial

Tighter mortgage spreads in December



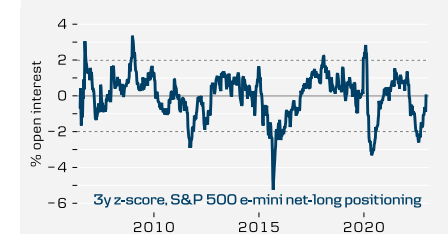
Past performance is not a reliable indicator of current or future results. Source: Danske Bank

January is usually busy for primary market supply



Past performance is not a reliable indicator of current or future results. Source: Bloomberg

Market no longer bearishly positioned



Past performance is not a reliable indicator of current or future results. Source: Refinity

## Names and contact information of analysts

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### Editor:

Las Olsen, <i>Chief Economist</i>	Denmark	+45 45 14 14 94	laso@danskebank.com
Aila Mihr, <i>Senior Analyst</i>	Global	+45 45 14 15 11	amih@danskebank.dk
Michael Grahn, <i>Chief Economist</i>	Sweden	+46 8 568 807 00	mika@danskebank.com
Frank Jullum, <i>Chief Economist</i>	Norway	+47 85 40 65 40	fju@danskebank.com
Pasi Petteri Kuoppamäki, <i>Chief Economist</i>	Finland	+358 10 546 7715	paku@danskebank.com
Kristoffer Lomholt, <i>Chief Analyst</i>	FX Research	+45 45 12 85 29	klom@danskebank.com
Jan Weber Østergaard, <i>Chief Analyst</i>	Fixed Income Research	+45 45 13 07 89	jast@danskebank.com
Mark Thybo Naur, <i>Senior Analyst</i>	Credit Research	+45 45 12 84 30	mnau@danskebank.com
Bjarne Breinholt Thomsen, <i>Senior Equity Strategist</i>	Equities Research	+45 61 22 56 13	bt@danskebank.com

# Macroeconomic forecast

## Macro forecast. Scandinavia

	Year	GDP <sup>1</sup>	Private cons. <sup>1</sup>	Public cons. <sup>1</sup>	Fixed inv. <sup>1</sup>	Ex-ports <sup>1</sup>	Im-ports <sup>1</sup>	Infla-tion <sup>1</sup>	Wage growth <sup>1</sup>	Unem-ploym <sup>3</sup>	Public budget <sup>4</sup>	Public debt <sup>4</sup>	Cu
Denmark	2022	2.9	-2.6	-1.1	4.4	7.4	3.2	7.8	3.5	2.6	1.2	29.7	1
	2023	-1.0	-2.3	0.0	-3.3	1.3	-0.7	4.9	4.1	3.1	1.0	28.1	
	2024	1.0	1.8	0.9	-2.1	1.2	0.4	2.0	4.2	3.4	0.8	27.0	
Sweden	2022	2.6	2.6	-0.2	5.6	4.6	7.9	8.3	2.5	7.5	0.7	31.0	
	2023	-1.2	-1.3	1.1	-3.0	1.3	0.2	8.5	3.2	8.2	-0.9	29.0	
	2024	1.2	2.0	1.2	1.8	2.8	2.6	1.3	2.7	8.1	-0.4	29.0	
Norway	2022	3.7	6.6	0.3	4.0	3.0	12.1	5.8	3.9	1.8	-	-	
	2023	0.6	-0.5	1.3	0.5	3.5	2.5	4.8	4.3	2.2	-	-	
	2024	1.5	0.9	1.5	4.0	2.0	2.0	2.1	3.8	2.4	-	-	

## Macro forecast. Euroland

	Year	GDP <sup>1</sup>	Private cons. <sup>1</sup>	Public cons. <sup>1</sup>	Fixed inv. <sup>1</sup>	Ex-ports <sup>1</sup>	Im-ports <sup>1</sup>	Infla-tion <sup>1</sup>	Wage growth <sup>1</sup>	Unem-ploym <sup>3</sup>	Public budget <sup>4</sup>	Public debt <sup>4</sup>	Cu
Euro area	2022	3.3	3.9	1.1	4.4	7.4	8.6	8.4	4.2	6.7	-3.9	93.7	
	2023	-0.9	-1.6	1.3	0.7	2.9	4.5	6.8	4.9	7.4	-4.0	92.5	
	2024	0.0	0.7	1.7	-0.1	1.3	2.7	2.9	3.6	8.3	-3.5	91.6	
Germany	2022	1.8	4.6	1.6	0.4	3.2	6.7	8.6	4.1	3.0	-2.3	67.4	
	2023	-1.4	-2.1	1.9	-1.2	2.4	3.7	7.9	5.4	3.8	-2.7	65.5	
	2024	-0.5	0.9	2.3	0.2	-0.1	3.0	3.9	4.3	4.2	-1.9	66.2	
Finland	2022	1.8	2.3	2.5	4.5	1.5	7.0	7.2	2.6	6.8	-1.8	70.7	
	2023	-0.7	-0.3	1.5	-1.0	-1.5	-2.0	4.8	4.0	7.3	-2.5	71.0	
	2024	0.5	0.4	1.0	0.5	1.5	1.0	2.2	3.5	7.2	-2.0	71.7	

## Macro forecast. Global

	Year	GDP <sup>1</sup>	Private cons. <sup>1</sup>	Public cons. <sup>1</sup>	Fixed inv. <sup>1</sup>	Ex-ports <sup>1</sup>	Im-ports <sup>1</sup>	Infla-tion <sup>1</sup>	Wage growth <sup>1</sup>	Unem-ploym <sup>3</sup>	Public budget <sup>4</sup>	Public debt <sup>4</sup>	Cu
USA	2022	1.9	2.6	-0.9	-0.4	7.9	8.5	8.0	5.2	3.6	-4.2	124.0	
	2023	-0.2	-0.2	1.1	-5.4	1.1	-4.4	3.3	4.4	4.0	-3.8	121.0	
	2024	0.5	0.4	1.3	0.6	-0.1	0.5	1.7	2.1	5.6	-3.9	120.5	
China	2022	3.3	2.8	-	4.5	-	-	2.0	3.0	-	-8.9	76.9	
	2023	4.9	5.1	-	5.2	-	-	2.2	5.0	-	-7.2	84.1	
	2024	5.3	5.5	-	5.5	-	-	2.5	5.5	-	-7.5	89.8	
UK	2022	4.2	-	-	-	-	-	8.9	-	3.8	-	-	
	2023	-0.7	-	-	-	-	-	6.2	-	4.4	-	-	
	2024	0.8	-	-	-	-	-	2.6	-	5.0	-	-	
Japan	2022	1.4	3.0	1.6	-0.8	4.7	8.0	2.2	-	2.6	-	-	
	2023	0.7	0.9	0.6	1.3	2.5	3.2	2.4	-	2.8	-	-	
	2024	0.9	0.8	0.5	0.6	1.5	0.5	1.4	-	2.8	-	-	

Source: OECD and Danske Bank. 1) % y/y. 2) % contribution to GDP growth. 3) % of labour force. 4) % of GDP.

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## Financial forecast

Bond and money markets										
		Key interest rate	3m interest rate	2-yr swap yield	10-yr swap yield	Currency vs EUR	Currency vs USD	Currency vs DKK	Currency vs NOK	Currency vs SEK
USD	05-Jan	4.50	4.78	4.68	3.65	106.1	-	701.3	1010.9	1054.4
	+3m	5.25	5.40	5.20	4.05	102.0	-	729.4	1019.6	1078.4
	+6m	5.25	5.40	5.10	4.05	98.0	-	759.7	1040.8	1142.9
	+12m	5.25	5.24	4.80	3.65	98.0	-	760.2	1020.4	1122.4
EUR	05-Jan	2.00	2.18	3.26	2.93	-	106.1	743.7	1072.0	1118.3
	+3m	3.00	3.36	3.35	3.00	-	102.0	744.0	1040.0	1100.0
	+6m	3.25	3.41	3.20	2.85	-	98.0	744.5	1020.0	1120.0
	+12m	3.25	3.39	2.90	2.55	-	98.0	745.0	1000.0	1100.0
JPY	05-Jan	-0.10	-0.03	0.33	0.91	120.5	132.9	6.17	8.90	9.28
	+3m	-0.10	-	-	-	141.8	139.0	5.25	7.34	7.76
	+6m	-0.10	-	-	-	132.3	135.0	5.63	7.71	8.47
	+12m	-0.10	-	-	-	125.4	128.0	5.94	7.97	8.77
GBP*	05-Jan	3.50	-	4.31	3.56	88.3	120.1	842.3	1214.1	1266.5
	+3m	3.75	-	4.20	3.50	86.0	118.6	865.1	1209.3	1279.1
	+6m	3.75	-	4.20	3.50	85.0	115.3	875.9	1200.0	1317.6
	+12m	3.75	-	4.00	3.30	85.0	115.3	876.5	1176.5	1294.1
CHF*	05-Jan	1.00	-	1.50	1.85	98.4	92.8	755.5	1089.1	1136.1
	+3m	1.00	-	-	-	97.0	95.1	767.0	1072.2	1134.0
	+6m	1.50	-	-	-	96.0	98.0	775.5	1062.5	1166.7
	+12m	1.50	-	-	-	96.0	98.0	776.0	1041.7	1145.8
DKK	05-Jan	1.75	2.53	3.42	3.08	743.72	701.28	-	144.14	150.37
	+3m	2.65	3.45	3.55	3.20	744.00	729.41	-	139.78	147.85
	+6m	2.90	3.50	3.40	3.05	744.50	759.69	-	137.00	150.44
	+12m	2.90	3.50	3.10	2.75	745.00	760.20	-	134.23	147.65
SEK	05-Jan	2.50	2.79	3.35	2.92	1118.3	1054.4	66.5	95.9	100.0
	+3m	3.00	3.05	3.35	2.95	1100.0	1078.4	67.6	94.5	-
	+6m	3.00	3.10	3.15	2.85	1120.0	1142.9	66.5	91.1	-
	+12m	3.00	3.10	2.85	2.55	1100.0	1122.4	67.7	90.9	-
NOK	05-Jan	2.75	3.28	3.56	3.23	1072.0	1010.9	69.4	100.0	104.3
	+3m	2.75	2.95	3.45	3.15	1040.0	1019.6	71.5	-	105.8
	+6m	2.75	2.95	3.20	2.80	1020.0	1040.8	73.0	-	109.8
	+12m	2.50	2.95	3.05	2.70	1000.0	1020.4	74.5	-	110.0

\*Notes: GBP swaps are SONIA and CHF swaps are SHARON.

We have updated our Norges Bank forecasts after yesterday's Norges Bank meeting but not yet our Norwegian yield outlook

## Commodities

	05-Jan	2022				2023				Average	
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2022	2023
ICE Brent	79	98	112	105	100	95	95	95	95	104	95

Source Danske Bank

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