

Norges Bank Review

Rate hike and tightening bias

As we expected, Norges Bank (NB) this morning raised the policy rate by 25bp from 1.25% to 1.50%. The rate path was adjusted downward, as global headwinds have lowered global forward rates, even though the weaker currency partly counteracted the effect in the short term. Signs of higher growth in labour supply are considered to increase potential growth, hence pushing the rate path downward. The rate path now suggests a 40% probability of a rate hike in H1 next year, with a high probability of this happening already in Q1. Importantly, this indicates that rates are more likely to rise than fall next year.

The Executive Board stated that: ‘... (the) current assessment of the outlook and balance of risks suggests that the policy rate will most likely remain at this level in the coming period.’

Our interpretation is that this implies unchanged rates within the period of the next monetary policy report, i.e. including December.

The rate path published in the Monetary Policy Report (MPR) was adjusted downward from Q2 20 (Chart 2). Specifically, the rate path suggests a roughly 40% probability of the next hike to be delivered in H1 next year. Further out the rate path signals unchanged rates and then a roughly 30% probability of a rate cut in 2022.

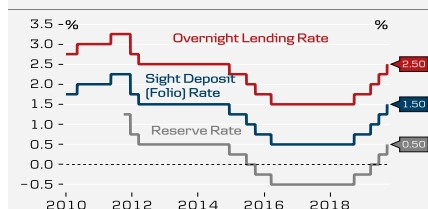
The factors affecting the rate path were broadly in line with our expectations. Global risks and global forward rates pushed the rate path downward. A weaker currency partly counteracted these effects, especially in the short term. There were minor adjustments to the domestic growth outlook. However, NB now considers labour supply to be higher than previously forecasted, which improves potential growth. In isolation, this pushes the rate path downward.

The main takeaway from this meeting is that a rate hike is more likely than a rate cut next year. More precisely, the path suggests a 40% probability of another rate hike in H1 2020. **As we consider the labour market to tighten further, we still expect NB to hike rates again in March 2020.**

FI/Rates. Market interest rates moved up on Norges Bank’s decision - but mainly in the short-end FRAs. NOK 3M DEC19 up from 1.88% just ahead of the decision to 1.94% 15 minutes after. The 2023 fwd interest rate trough is basically unchanged - as the market seems to view Norges Bank as being too hawkish. There should still be upside potential in red FRAs, as we disagree with the market and see a March hike as a real possibility. However, as Norges Bank indicates - and according to our earlier expectations - the target rate will be on hold in December. Any additional upside potential in the DEC19 FRA will be due to FRA-OIS volatility linked to liquidity issues. We disregard this potential and close our DEC19 FRA trade at a profit of 12.5bp.

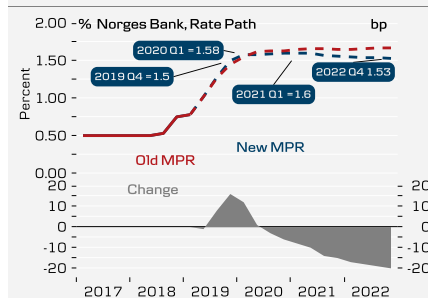
FX. EUR/NOK initially dipped below 9.83 on today’s decision but the move quickly reversed sending the cross back toward 9.87, as it remains difficult for the FX market to buy into marked ECB-NB divergence. NB should eventually provide support for another leg lower in EUR/NOK, but it is unlikely to do so in the very short term, where the NOK is set to remain sensitive to the global environment. EUR/NOK likely to settle marginally lower on the day but to stay above the 9.80 mark.

Chart 1. As expected NB hiked all policy rates by 25bp



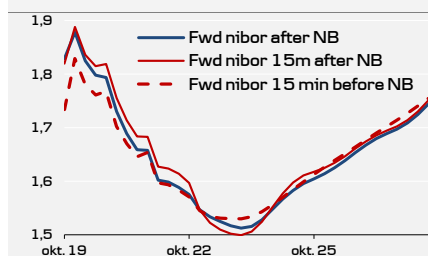
Source: Macrobond Financial, Danske Bank

Chart 2. Rate path marginally revised down



Source: NB, Macrobond Financial, Danske Bank

Chart 3. Market interest rates moved mainly in the very short end



Source: Macrobond Financial, Danske Bank

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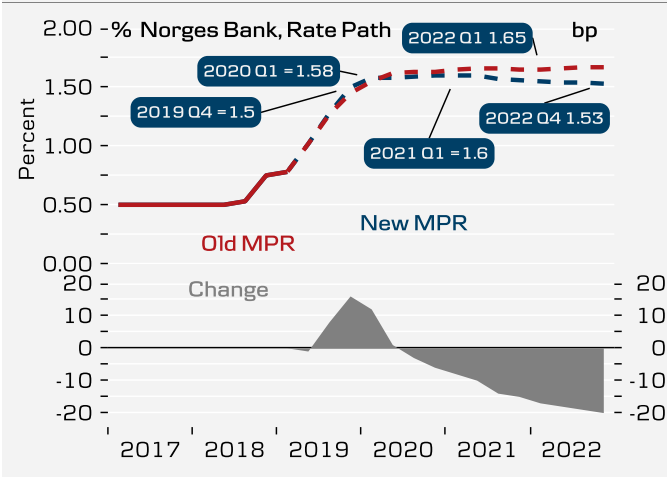
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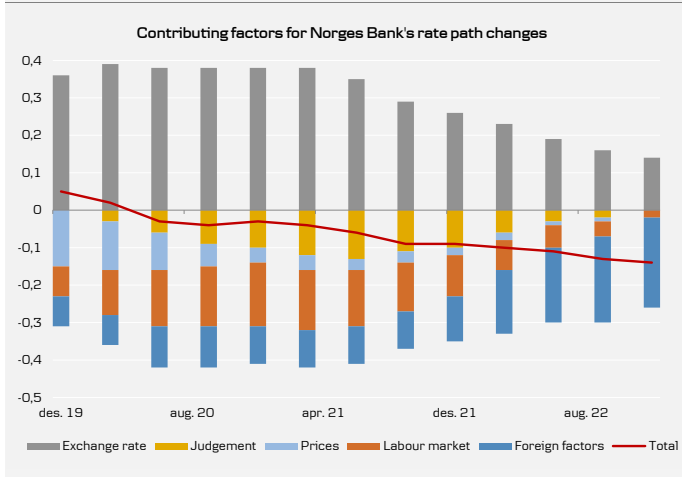
Appendix chart pack

Chart 4. Forward curve marginally revised down - 14bp in the long end



Source: NB, Macrobond Financial, Danske Bank

Chart 5. International factors push the rate path down compared to MPR II - weak NOK pushes the path up



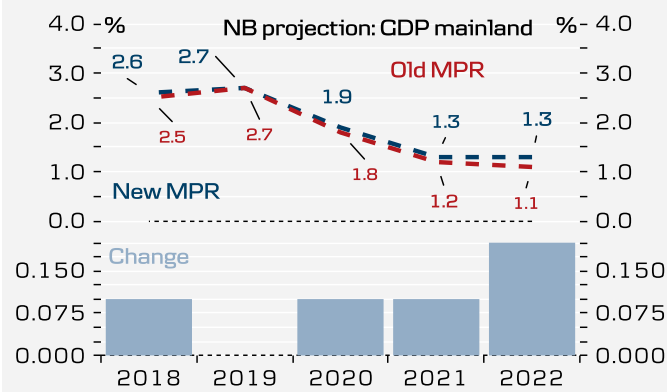
Source: NB, Macrobond Financial, Danske Bank

Table 1. Contributing factors to changes in the rate path in table format

	Contributing factors for rate path changes (pp)					Total
	Labour market	Prices	Judgement	Foreign factors	Exchange rate	
31.12.2019	-0,08	-0,15	0,00	-0,08	0,36	0,05
31.03.2020	-0,12	-0,13	-0,03	-0,08	0,39	0,02
30.06.2020	-0,15	-0,10	-0,06	-0,11	0,38	-0,03
30.09.2020	-0,16	-0,06	-0,09	-0,11	0,38	-0,04
31.12.2020	-0,17	-0,04	-0,10	-0,10	0,38	-0,03
31.03.2021	-0,16	-0,04	-0,12	-0,10	0,38	-0,04
30.06.2021	-0,15	-0,03	-0,13	-0,10	0,35	-0,06
30.09.2021	-0,13	-0,03	-0,11	-0,10	0,29	-0,09
31.12.2021	-0,11	-0,02	-0,10	-0,12	0,26	-0,09
31.03.2022	-0,08	-0,02	-0,06	-0,17	0,23	-0,10
30.06.2022	-0,06	-0,01	-0,03	-0,20	0,19	-0,11
30.09.2022	-0,04	-0,01	-0,02	-0,23	0,16	-0,13
31.12.2022	-0,02	0,00	0,00	-0,24	0,14	-0,14

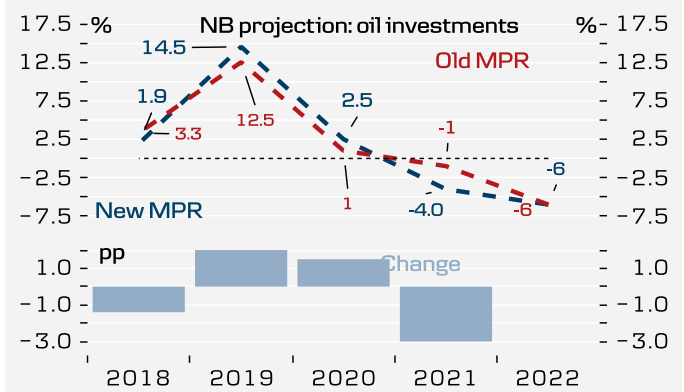
Source: NB, Danske Bank

Chart 6. Mainland GDP forecasts - marginal adjustment of forecasts



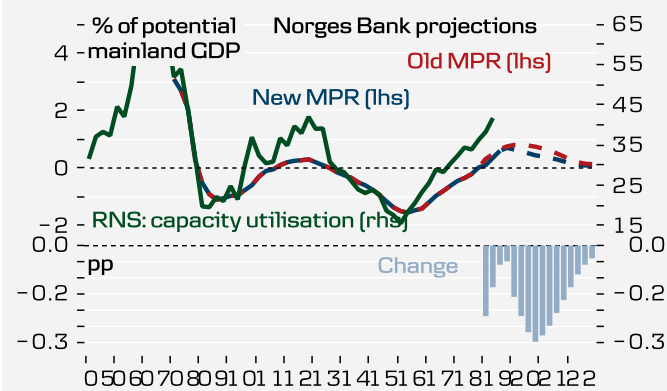
Source: Macrobond Financial, Bloomberg, Danske Bank

Chart 7. Petroleum investments - higher short term, then lower



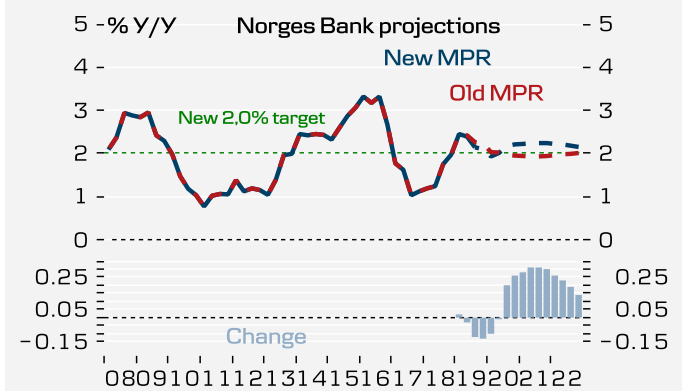
Source: NB, Macrobond Financial, Danske Bank

Chart 8. Moderately downward adjustment in output gap projections



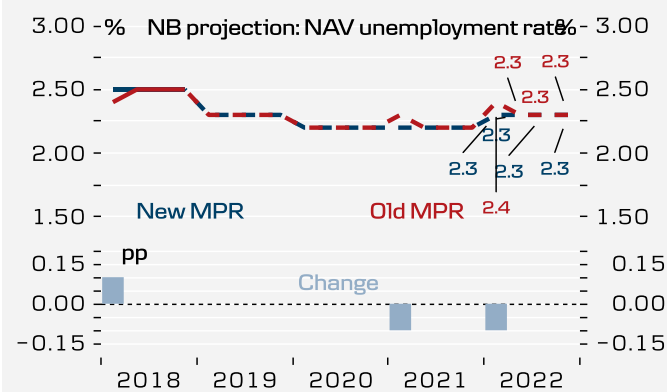
Source: Ministry of Finance, Macrobond Financial, Bloomberg, Danske Bank

Chart 9. Core inflation projections (quarterly) raised



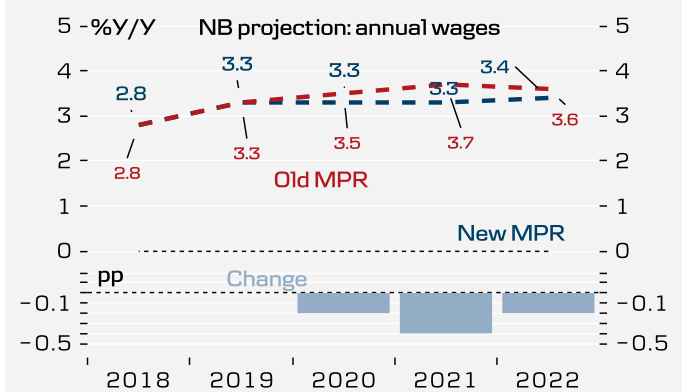
Source: SSB, Macrobond Financial, Bloomberg, Danske Bank

Chart 10. NAV unemployment rate forecast



Source: Ministry of Finance, Macrobond Financial, Bloomberg, Danske Bank

Chart 11. Wage growth projections lowered slightly



Source: SSB, Macrobond Financial, Bloomberg, Danske Bank

Disclosures

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None.

Date of first publication

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