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Economics Group

Special Commentary

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Norges Bank, the Lone G10 Hawk?

Executive Summary

- The Norges Bank caught markets off guard today with its fourth interest rate increase within the last year. While the hike today contrasts sharply with most other central banks globally, the Norges Bank's guidance suggested this may be the end of the tightening cycle for now.
- The Norges Bank's executive board decided to raise its key policy rate 25 bps to 1.50%, the highest level in almost five years, and cited "solid" domestic growth. However, the board's current assessment suggests that the policy rate will most likely remain at its current level over the forecast horizon.

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The Norges Bank's "Dovish Hike"

The Norges Bank's decision to raise its deposit rate 25 bps to 1.50% today was not a complete shock, as the central bank had previously signaled near-term tightening, and the decision was expected by 11 out of 26 economists in a Bloomberg survey. The Norwegian krone initially gained sharply against the euro and the U.S. dollar following the decision, as most were looking for rates to remain steady at today's meeting. However, krone gains were likely limited by dovish signals from the Norges Bank around the rate path going forward.

Figure 1

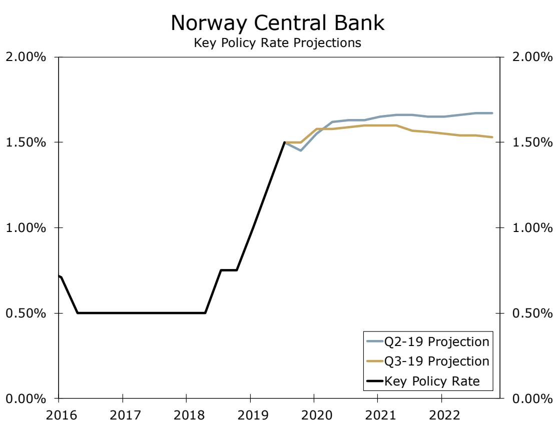
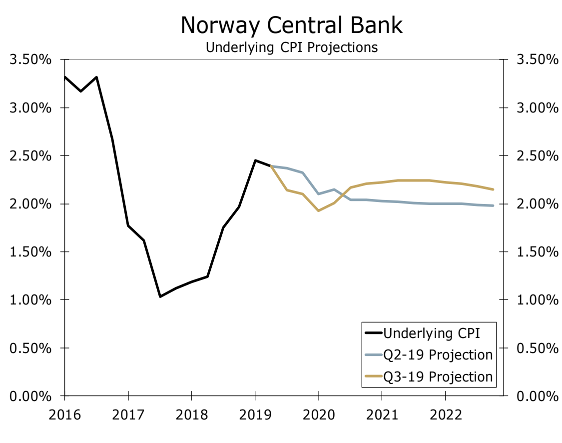


Figure 2



Source: Norges Bank and Wells Fargo Securities

Indeed, the central bank lowered its longer-term projections for the policy rate, and now is signaling that it may not raise rates further over the forecast horizon (Figure 1). In its policy report, the board noted that weaker growth prospects and lower interest rates abroad, combined with slightly lower inflation and a somewhat "less tight" domestic labor market, have contributed to the downward revision in the policy path. Meanwhile, the central bank lowered its near-term inflation forecasts but raised its longer-term projections, such that underlying inflation is projected to remain close to the central bank's 2% target across the forecast horizon (Figure 2).

The central bank is now signaling that it may not raise rates further over the forecast horizon.

Together we'll go far

Mainland GDP growth was upwardly revised in 2019 to 2.7% from 2.6%. However, in the years ahead, growth is expected to slow somewhat.

Hawk No More

We believe the Norges Bank will be on hold for the foreseeable future.

The Norges Bank's main objective is to ensure low and stable inflation around the 2% target. Despite price pressures easing in August, the Norges Bank's decision to hike rates today suggests the central bank was able to look through short-term swings in CPI inflation. The central bank has been raising interest rates in an attempt to cool its economy, while has benefitted from generally buoyant oil prices and withstood the global slowdown and uncertainty surrounding global trade tensions and Brexit. However, the board's current assessment of the Norwegian economy suggests that the policy rate will most likely remain at its current level over the forecast horizon. As of now, we share the same view as the board and believe the Norges Bank will be on hold for the foreseeable future.

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