

European Watch

Norges and Riksbank review: diverging

Riksbank and Norges hike 25bp as expected

Norges Bank shifted more hawkish relative to the Riksbank today, in-line with our expectation ([Nordics monthly: diverging 15 Sep 23](#)). This diverging monetary policy outlook reflects the diverging economic outlook. Sweden appears to be entering recession while Norway skirts it. Both central banks hiked 25bp as expected, but Norges raised its forecast policy rate path 23bp at the peak compared to 5bp from the Riksbank. Norges expects to run with higher policy rates than Riksbank until mid-2025, six months later than the previous forecasts. We see the risks skewed towards this Norges-Riksbank gap widening.

Norges expects another hike in December

Norges Bank says "Whether additional tightening will be needed depends on economic developments. There will likely be one additional policy rate hike, most probably in December." We had expected Norges to signal another hike was more-likely-than-not, but this language was a little stronger than we expected. We push back our call for what we see as Norges final hike. We now expect a final 25bp hike in December, compared to November previously. Pushing up Norges policy path was stronger than expected demand, a higher output gap and higher oil prices.

Riksbank focused on exchange rate

The Riksbank faces a more mixed outlook. Domestic inflation pressure appears likely to slow as past rate hikes are driving the economy into mild recession. But the Riksbank's concern about the inflationary consequences of the weak krona seems to remain intense. Balancing these concerns, the Riksbank suggests it is most likely on hold here but expects to retain a hiking bias until the second half of next year. Specifically, the Riksbank's policy rate forecast peaks in 2Q 2024 at 4.1%. In our view the Riksbank is pushing back hard against market expectations that it will shift to cuts relatively soon as growth weakens. In addition to the policy rate forecast the Riksbank presents scenarios in which higher than expected inflation would require immediate further hikes but weaker than expected demand would not require cuts until mid-next year.

Riksbank outlook more challenged

Both central banks are presenting a high-for-long strategy. In our view the Riksbank's outlook is more challenged than Norges. Weaker growth in Sweden will increasingly cut domestic inflationary pressure in our view, whereas Norges faces a more resilient outlook and possibly stronger wage growth. As we say above, the Riksbank seems to be trying to balance supporting the currency to cut upside inflation risks against that growth weakness. We think that argument becomes harder the weaker growth is and we struggle to see Riksbank maintaining that position for a full further year. We look for 3 Riksbank cuts in 2024 compared to two from Norges. We see risks skewed up to the Norges path and down to the Riksbank. A weak currency remains the key upside risk to our Riksbank view (**FX part on the following page**).

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Today's decisions support NOKSEK

Today's decisions support our constructive NOKSEK view. Into today markets (and consensus) assigned a higher chance to Norges pausing (after this week) than to the Riksbank, whereas we saw risks the other way round. This has been because we expect Norway's economy to prove more resilient than Sweden's. To this end, we continue finding the Norges-Riksbank differential priced for end-2024 too tight, and we think NOKSEK stands to benefit if/once markets come to the same conclusion. We look for 1.06 by the end of this year.

For NOK, we continue to expect EURNOK at 11.00 by year-end, on a hawkish Norges Bank, high oil prices, and the resilient, by the European standards, Norwegian economy.

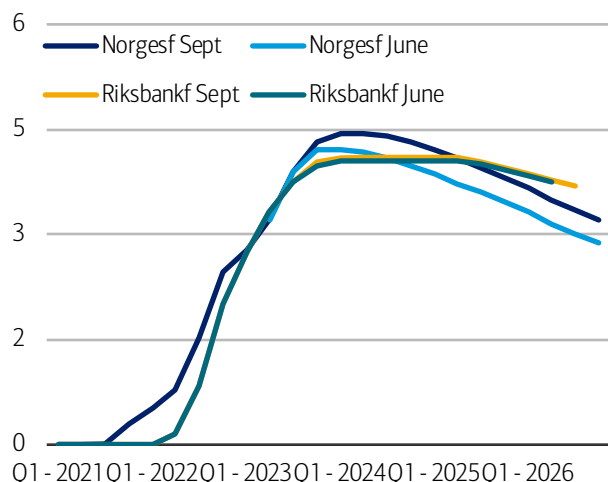
For SEK, we remain cautious, expecting EURSEK to peak at 12.00 in the coming weeks, but we see risks for more and prolonged SEK weakness because we are concerned about a meaningful consumer squeeze and cannot overlook risks around property markets.

We would not worry about the Riksbank's FX reserves' hedging

Alongside its monetary policy decision, the Riksbank announced it will start hedging part of its FX reserves. While clarifying this is not part of monetary policy, this does not mean this cannot impact FX. We continue to judge the amounts the Riksbank will hedge (USD 8bn and EUR 2bn within 4-6 months) to be not large enough for them to have anything more than a small (positive) and likely temporary impact on SEK (see also What if the Riksbank started hedging its FX reserves? 20 Sep 23).

Exhibit 1: Norges' shifts more hawkish relative to Riksbank

Norges Bank and Riksbank policy rate forecasts

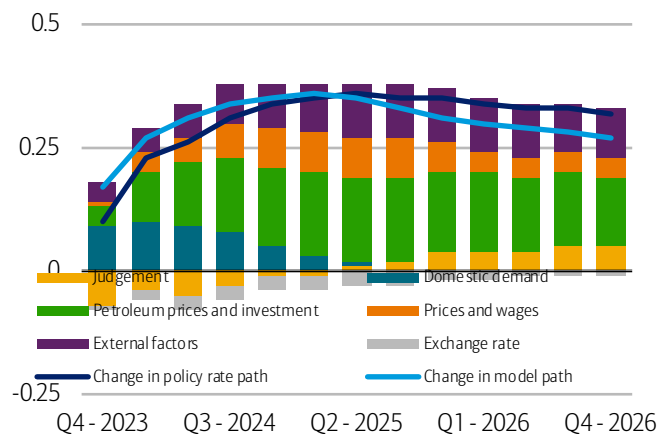


Source: Norges Bank, Riksbank

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Exhibit 2: Decomposition of changes in Norges Bank's rate path

Judgement lowers front end, raises back end

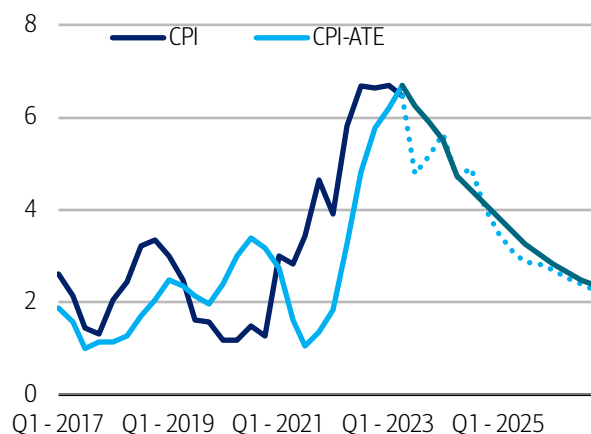


Source: Norges Bank, MPR 3/23, BofA Global Research. Note: Judgment is the difference (residual) between the rate-path changes and the cumulative contribution of the remaining five components.

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Exhibit 3: Norges CPI and CPI-ATE projections, % y/y

Norger expects much more persistent inflation...

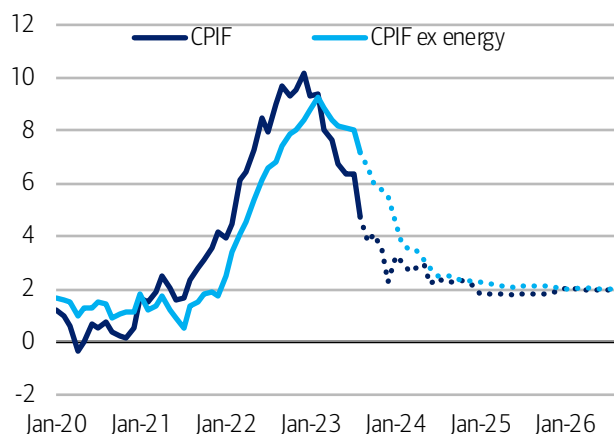


Source: Norges Bank (Monetary Policy Report September 2023). Dotted lines are Norges forecasts.

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Exhibit 4: Riksbank CPIF and CPIF ex energy projections, % y/y

...than the Riksbank



Source: Riksbank (Monetary Policy Report September 2023). Dotted lines are Riksbank forecasts.

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Exhibit 5: Norges Bank's key forecasts as of Sep-2023 (in brackets changes vs June-23 forecasts)

Norway's outlook remains resilient...

	2022	2023E	2024E	2025E	2026E
CPI	5.8	5.8 (-0.2)	4.8 (0.9)	3.1 (0.2)	2.5 (0.1)
CPI-ATE	3.9	6.3 (0.0)	4.7 (0.1)	3.4 (0.1)	2.6 (0.2)
Annual wages	4.3	5.5 (0.0)	5.2 (0.5)	4.6 (0.3)	3.9 (0.2)
GDP, Mainland Norway	3.7	1.3 (0.1)	0.3 (0.1)	0.8 (-0.1)	1.4 (0.0)
Output gap, mainland Norway (lvl)	1.8	0.8 (0.2)	-0.3 (0.2)	-0.8 (0.0)	-0.7 (0.0)
Unemployment (rate, level)	1.8	1.8 (-0.1)	2.2 (-0.1)	2.4 (0.0)	2.4 (0.0)
Mainland demand	4.9	-0.3 (0.3)	-0.1 (-0.4)	1.8 (0.0)	2.1 (0.2)
Petroleum investment	-6.5	6.0 (1.0)	6.0 (3.0)	2.0 (0.0)	-1.0 (-1.5)
House prices	4.9	-0.3 (-0.6)	0.8 (0.2)	0.8 (0.2)	6.0 (1.1)
Real disposable income excl. dividend income	2.7	-2.1 (0.3)	0.7 (-0.2)	2.3 (0.0)	2.9 (0.1)

Source: Norges Bank, MPR 3/23. Note: Projections show percentage change from the previous year unless otherwise specified. In brackets is the change in projections relative to the June 2023 Monetary Policy Report. GDP figures are working-day adjusted. The output gap denotes the percentage deviation between actual and potential mainland GDP according to Norges Bank's estimates.

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Exhibit 6: Key Riksbank forecasts

...Sweden's outlook much less so

	2021	2022	2023E	2024E	2025E
CPIF	2.4 (2.4)	7.7 (7.7)	5.9 (5.9)	2.5 (2.4)	1.8 (1.8)
CPIF excl. energy	1.4 (1.4)	5.9 (5.9)	7.5 (7.4)	2.9 (2.8)	2.1 (2.0)
GDP	6.1 (6.1)	2.8 (2.8)	-0.8 (-0.5)	-0.1 (0.0)	1.9 (1.8)
Household consumption	6.3 (6.3)	1.9 (1.9)	-2.0 (-2.4)	0.8 (0.7)	1.9 (1.9)
Gross fixed capital formation	7.1 (7.1)	6.2 (6.1)	-2.6 (-2.6)	-2.6 (-3.0)	2.6 (2.2)
Final domestic demand*	5.4 (5.4)	2.4 (2.4)	-1.1 (-1.4)	0.0 (-0.1)	1.8 (1.7)
Employment gap	-1.3 (-1.3)	0.6 (0.6)	1.6 (1.3)	0.2 (0.0)	-0.2 (-0.3)
Hours gap	-2.0 (-2.0)	-0.3 (-0.3)	0.8 (1.2)	-0.8 (-0.8)	-0.7 (-0.8)
GDP gap	0.6 (0.6)	1.8 (1.9)	-0.4 (0.0)	-2.0 (-1.6)	-1.4 (-1.1)

Source: Riksbank (Monetary Policy Report September 2023). Previous forecasts in brackets. Annual % changes for CPIF, GDP and consumption. Final domestic demand refers to its contribution to GDP growth in percentage points. Employment, GDP, and hours gap show percentage deviation from the Riksbank's assessed potential levels.

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