Norges Bank will hold this week, but a rate cut may follow in June

Norway's central bank has yet to begin its easing cycle. Plans to cut rates in March were thwarted by a spike in inflation: while headline CPI has fallen back, underlying inflation remains sticky, and a cut this week is unlikely. However, mounting growth risks mean Norges Bank may open the way for a June cut. Any negative NOK impact may be temporary though

Norges Bank in Oslo

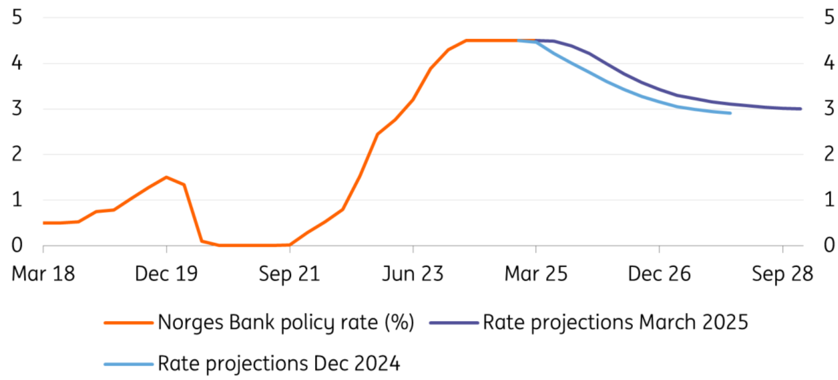
Another hold after March U-turn

Norway's central bank was meant to cut rates in March, but an unexpected spike in inflation forced policymakers to keep rates on hold at 4.50%. As Norges Bank announces its policy again on 8 May, the probability of a cut is low. The Bank's own rate projections, consensus and market pricing are all pointing to a hold this week, although the debate about future moves is more open.

Norges Bank has generally been quite predictable with its forward guidance, but the major jump in domestic inflation and market volatility means the Bank's projections should probably be taken with a pinch of salt. In the March update, the policy rate was projected to stay unchanged at 4.50% until the end of the third quarter, and then decrease to 4.0% by early 2026 and to 3.5% by end-2026. The terminal rate is seen at 3.0%, to be reached around the end of 2027.

But Governor Ida Wolden Bache stressed in March that “the uncertainty surrounding the outlook is greater than normal” – and that was before the "Liberation Day" market shock. Things have changed quite a lot since the March meeting, domestically and externally.

Norges Bank revised its rate path higher in March



Source: Norges Bank, ING

Inflation picture slightly less worrying

First, inflation has come back lower. Following a very surprising jump in February, headline CPI declined by 0.7% month-on-month in March, bringing the YoY rate back from 3.6% to 2.6%. That is a level that would be consistent with Norges Bank rate cuts. But core inflation remains sticky. After jumping from 2.8% to 3.4% in February, underlying CPI stayed at 3.4% YoY in March, with an additional 0.2% MoM acceleration.

New inflation figures are published on Friday, one day after Norges Bank’s meeting. Headline CPI is expected to ease to 2.5%, and underlying inflation to 3.2%. That would be a welcome development, but perhaps not enough by itself to lead to a cut at the 19 June meeting. Other factors may tilt the balance to the dovish side.

Major growth concerns have arisen

Norway’s economic outlook has deteriorated in the past month, with manufacturing PMIs dropping to 46.1 in April, the lowest since 2020. While not hugely exposed directly to US export duties, a slowdown in global trade due to tariffs bodes ill for a country where around 47% of GDP is generated by exports. More importantly, energy products amount to around 66% of total Norwegian exports, and the country’s commodity terms of trade have dropped nearly 15% since the start of April as energy prices plummeted. Our commodities team forecasts Brent will remain below $65/bbl this year and TTF gas below €40/MWh.

Another dovish argument is that other central banks have faced some dovish repricing of rate expectations in the past month: both the USD and EUR two-year swap rates have declined roughly 30bp since late March. The NOK curve has followed, with the two-year swap rate down to 4.05%, 40bp below pre-March meeting levels.

In terms of counterarguments for a dovish shift, in addition to sticky inflation figures, Norges Bank is likely uncomfortable with the 3% drop in the trade-weighted NOK since its latest meeting, as currency weakness can increase imported inflation.

A June cut is possible

We think the risks are finely balanced between the next rate cut coming in June or August. We have a slight preference for June, as two months of re-slowing inflation combined with mounting growth risks call for earlier action.

We then expect another cut in September, but are not convinced about a third cut coming before December, as the growth outlook may have stabilised and some inflation concerns may have resurfaced by then. We stick to our call for a 3.50% terminal rate for Norges Bank, to be reached around mid-2026.

Market implications

In terms of this meeting's market impact, we see the balance of risks skewed to a dovish surprise. While the statement should include plenty of conditionality due to the uncertain outlook, we suspect Wolden Bache may signal rates can be cut in June or August. That would likely prompt markets to increase their bets on a June cut from the current 11bp and drive NOK front-end rates lower.

On the FX side, a dovish Norges Bank may halt NOK's recovery, causing EUR/NOK to stall in the 11.70-11.80 area for some time. That said, given the imbalance in positioning (EUR is overbought) and NOK's big rate advantage, the path should remain to the downside for EUR/NOK moving ahead. We target 11.50 by year-end.

The big caveat is the risk and liquidity conditions in the market. NOK is the least liquid currency, while EUR has grown its value as a safe haven given the recent USD woes. So, EUR/NOK spikes should remain one of the main effects of any new severe risk-off waves in markets.

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