Norges Bank to keep its powder dry this week

We expect Norway's central bank to keep its powder dry this week but we still think it is too early to rule out some further tightening in 2020. We continue to expect the Norwegian krone to outperform in the coming months

Interim meeting likely to be a non-event

The Norwegian central bank is unlikely to rock the boat at its interim meeting this Thursday - after all there won't be a monetary policy report or press conference. Expect policymakers to reiterate that '*the policy rate will most likely remain at this level in the coming period*' – any deviation from that communication would be interpreted as a rather strong hawkish shift.

1.50% Current deposit rate

The main factors that the Norges Bank (NB) will be mulling this week include:

1. Oil: Prices have slipped slightly since December, and in isolation that would normally translate into a marginally lower interest rate projection from the NB.

2. Macro-economic outlook: Recent activity data points to more subdued growth in 2020. Leading surveys from the Norges Bank point to a more moderate level of output and retail trade while Monday's industrial confidence survey reached its lowest level since the fourth quarter of 2016. However, while December inflation came in below the consensus estimate, it is still expected to pick up in 2020, and move above target, which could build the case for another hike.

3. FX: The case for further tightening may well hinge on the Norwegian krone. While the import-weighted krone index is currently slightly stronger than the Norges Bank forecasted, the difference isn't large enough to faze the Norges Bank.

4. Global growth: US-China trade tensions have tentatively calmed down, but this will need to translate into a rebound in global activity to convince the Norges Bank to increase rates again. Don't forget there is also the latent risk of a flare-up in Europe-US trade tensions.

Putting all of this together, we suspect policymakers will be comfortable with their on-hold stance for now. We still wouldn't completely rule out further tightening this year. Currently, the Norges Bank's rate projection implies there's a possibility of a hike around the second quarter (roughly a 40% chance). We're still loosely pencilling in a rate increase in the middle of this year, although this does rely upon a more pronounced global recovery, and one that isn't coupled with sizable NOK appreciation.

NOK: little impact from the NB, but still supportive outlook

We expect the NB meeting to have a fairly neutral impact on the krone. The bank is likely to reiterate its view from the December meeting (flat rates for 2020, with a bias for a potential hike) suggesting little impact on NOK.

We expect NOK to continue to do well in coming months. From a seasonality point of view, NOK tends do well in January and February. On a valuation basis, NOK remains one of the cheapest currencies in the G10 FX space. From a carry prospective, the currency offers the highest nominal yield in the developed market FX world. The non-negligible probability of a NB rate hike later this year also favours NOK. We expect EUR/NOK to reach the 9.80 level in coming weeks.

Author

James Smith
Developed Markets Economist, UK
james.smith@ing.com

Disclaimer