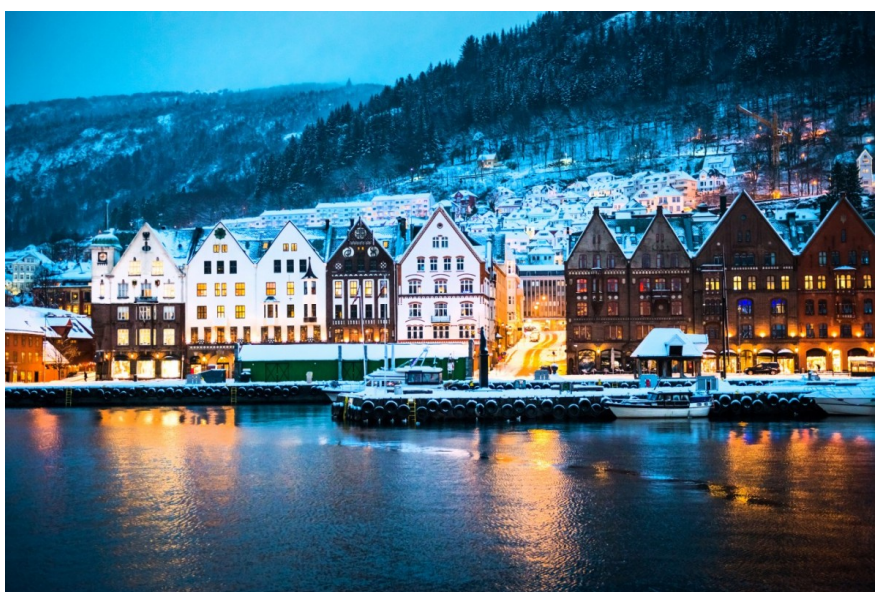


## The battered Scandies

A mix of disappointing domestic data, a stronger EUR and concerns about the local housing market, all suggest the NOK and SEK will remain lower for longer



Source: Shutterstock

The Swedish and Norwegian Krona (SEK and NOK) are going through significant weakness, with both currencies down against the EUR by around 2% over the past two days.

This is due to a mix of disappointing domestic data, a stronger EUR and sharply rising local housing market concerns. The latter in particular and its implications for the central banks' stances suggests lower NOK and SEK for longer versus our current forecasts.

Both NOK and SEK will struggle to fully recover after the sell-off in the upcoming months. Into the year end, we prefer NOK over SEK, given the likely less dovish December Norges Bank meeting versus a more dovish Riksbank meeting.

### EUR strength and disappointing domestic data

The recent EUR strength is indeed a part of the story. The EUR is up against other G10 European currencies as well as CE3 FX (Czech, Hungary and Poland) over the past two days but the bad domestic news underpinned the Scandinavian currencies underperformance. That is largely due to

the disappointing break-down of the Norway Q3 GDP (soft domestic consumption and investment) and lower than expected Swedish CPI. This turned NOK and SEK into the European FX underperformers.

## The housing market conundrum

Adding to this, we observe a theme of falling house prices emerging in both Norway and Sweden, with the October Swedish house price data recording the largest month-on-month decline since 2008. This raises not only macro-prudential risks and concerns about the long observed and well-flagged Scandinavian housing bubble but also has important implications for domestic monetary policy – raising the probability of a further delay in the eventual policy normalisation.

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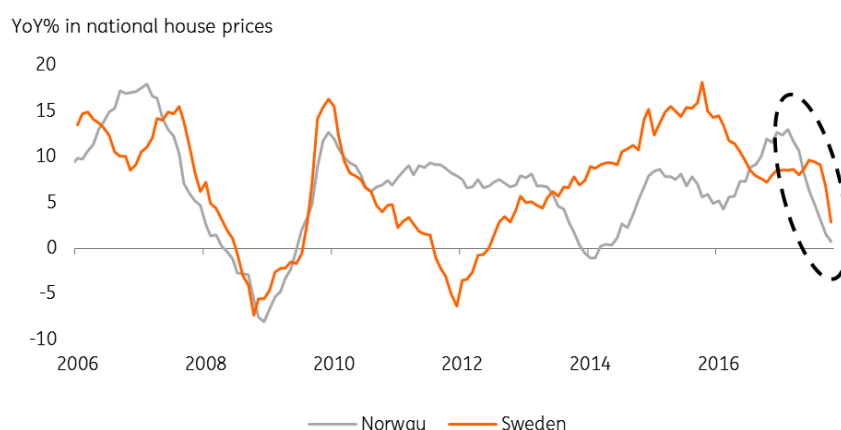
*The main reason for the decline in Sweden and Norway's house prices appears to be the fact that supply has finally caught up with demand*

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Over the past five years, new housing completions have roughly doubled in both markets, and new housing starts are up nearly 300% in Sweden. At the same time, macro-prudential measures are constraining buyers. The Swedish housing market, in particular, looks wobbly, with prices falling nearly 5% in the last two months.

For the Riksbank, and given the lower for longer open-ended European Central Bank QE, this suggests a materially lower likelihood of a deposit rate hike in 2018. In turn, this limits the SEK upside potential as the market will push out expectations for the first rate hike. The lower for longer Riksbank's negative deposit rate means that SEK will retain the cheapest funding cost, after the safe-haven CHF in the G10 FX space, which again does not bode overly well for the currency's prospects.

## Synchronised decline in house prices



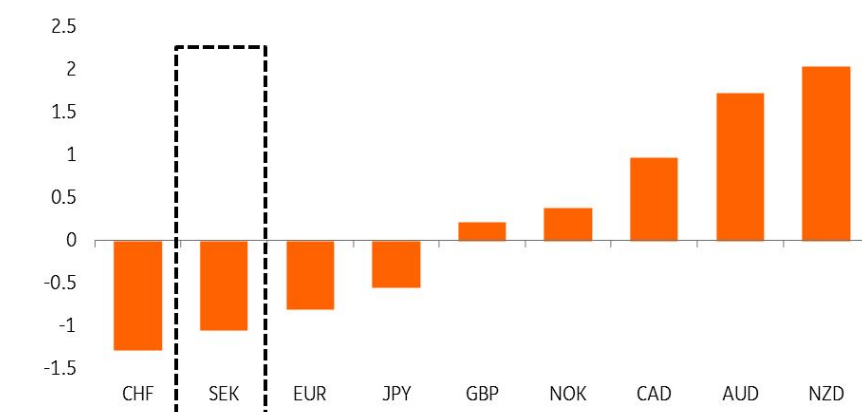
Source: Macrobond

## Concerns in place, but Scandies look to have overshoot

As we write our 2018 FX Outlook, we put our Scandinavian FX forecasts under revision following the recent moves. While at this point further weakness cannot be ruled out we don't want to pencil in further and persistent SEK and NOK declines.

This is partly because the scale of the recent fall looks like an overshoot, suggesting a fair degree of bad news already priced. As shown below, EUR/SEK is now trading meaningfully above the levels deemed as fair by our short-term financial fair value model. In terms of NOK, the cross materially decoupled from the oil price.

## Attractive SEK funding costs



Source: Bloomberg, ING

## SEK and NOK outlook: Lower for longer

Given the central banks, are unlikely to provide a catalyst for a monetary policy induced FX strength while the current concerns about the local housing market should remain in place, the scope for a meaningful SEK rebound over the next six months may be limited. The cross looks unlikely to break below 9.70 level this year, particularly if the Riksbank further flattens out its interest rate forecast at the December meeting and delays the start of the hiking cycle. The EUR/SEK 9.50 level should act as a solid and persistent support for most of 2018.

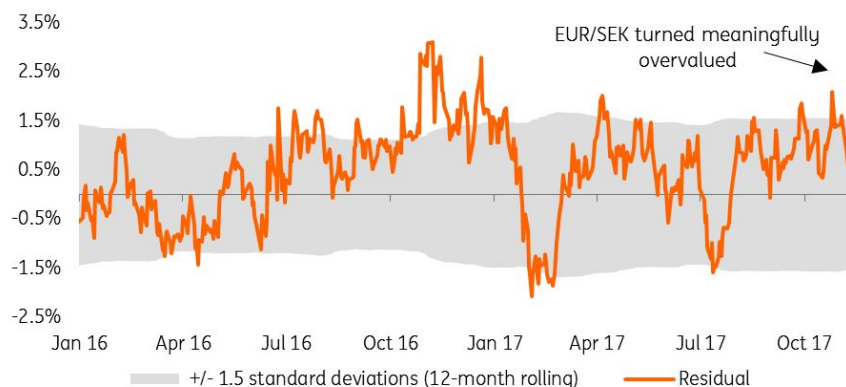
For NOK, our commodities' team view a limited upside to the oil price from here and some scope for a decline following the oil price rally of the past two months. This means that any pricing out of the EUR/NOK risk premia may be somewhat shallow, suggesting that the eventual post sell-off stability levels will be higher compared to the pre-sell-off starting point. The below EUR/NOK 9.00 levels of 1Q17 seems off the table, and EUR/NOK will most likely struggle to move below 9.20 during 1H18.

In line with the ECB lower for longer QE, both NOK and SEK, even after the likely correction higher, following the recent somewhat exaggerated sell-off, should remain low for longer (vs our current under-revision forecasts) reflecting the rise of concerns about the housing market and the idiosyncratic factors (persistently dovish Riksbank and the risk of some modest decline in the oil price in coming weeks). To be sure, we will be actively looking for short EUR/NOK and EUR/SEK entry points (as the recent sell-off looks overdone) but the target levels will be higher compared to our previous expectations.

[Read what's next for the Riksbank?](#)

## EUR/SEK looks to have overshoot

Percentage residual between EUR/SEK fair value and spot - a gauge for risk premium



Source: ING, Bloomberg

### Favouring NOK over SEK

On a relative basis, we see more upside to NOK during the remainder of the year as the 14th December, Norges Bank meeting is likely to deliver an upward revision to the current interest rate forecast due to the mix of NOK weakness and higher oil price.

In contrast, the Riksbank should further flatten out its interest rate forecast at the 20th December meeting, due to lower CPI and the housing market concerns.

The non-negligible likelihood of another QE extension in December should also limit the scope for SEK recovery (vs NOK). The relative NOK vs SEK outperformance should be supported by the somewhat better housing market in Norway vs Sweden – there may well be more bad news to come in Sweden, while the decline in Norwegian prices has been gentler and concentrated in the Oslo market.

We expect NOK/SEK to re-test the November high of 1.0354.

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