

Norges Bank hikes rates and signals several more to come

Thursday's rate hike in Norway will likely be followed by more in December and March, and at least one more next year. Given Norges Bank's history of going against the wider G10 central bank trend, there's no reason to doubt this hawkish outlook for now. We expect NOK to emerge as a key outperformer in risk-on periods thanks to its attractive yield profile

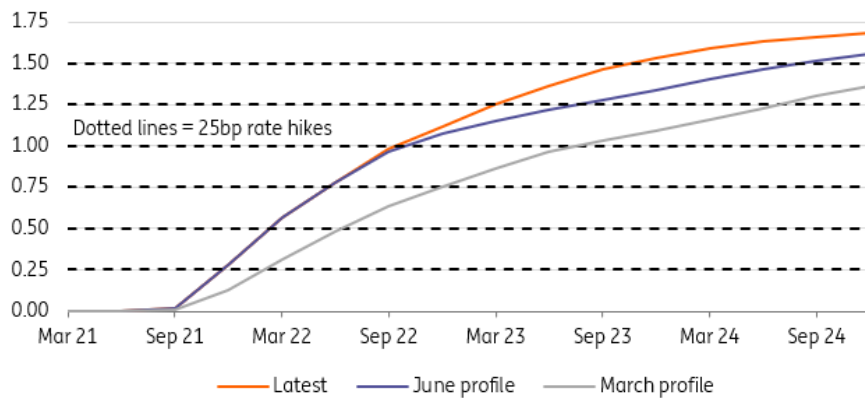


Norges Bank fires the starting gun on a run of hikes

Norway's central bank has fired the starting gun on what is likely to be a fairly rapid set of rate hikes over the coming 18 months. Thursday's hike, taking the deposit rate to 0.25%, was well telegraphed both in the June interest rate projection, and also verbally in the August meeting statement.

But the bigger focus as always is on what comes next, and importantly the latest interest rate projections imply a further three or four rate hikes by the end of 2022. That's fairly similar to what the central bank had predicted in June, though the bigger difference is that policymakers are factoring in around 20bp more tightening during 2023.

Norges Bank interest rate projections compared over time



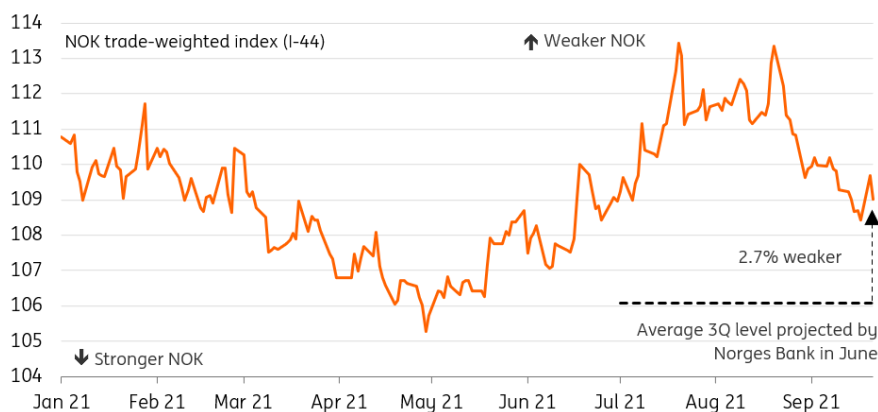
Source: Norges Bank

Again this isn't a huge surprise – NOK is tracking roughly 3% weaker than the central bank had been forecasting for the 3Q on average, while oil prices have bounced back to roughly where they were around the time of the last meeting. All else equal, that requires a higher level of interest rates.

Still, this profile is undoubtedly punchy, and puts Norges Bank in a very different setting to other G10 central banks. But then again it reflects the different structure of Norway's economy – and indeed the more formulaic nature of Norges Bank's policy decisions. So there's little reason to doubt the rough trajectory of the bank's projections at this stage. After all Norway saw several interest rate rises in 2019, at a time where the Fed was cutting.

Barring any further unwelcome surprises on Covid-19, we expect another rate hike in both December and March 2022. The jury's out on whether we see an additional one or two moves in the latter half of next year.

NOK has been trading weaker than Norges Bank had expected



Source: Macrobond, ING

NOK set to benefit from attractive yield profile

The 25bp rate hike today was not at all a surprise to markets, and it was likely the announcement that another hike will likely come in December – and an upgrade in longer-term rate projections –

that generated some lift on NOK, as EUR/NOK broke decisively below 10.1000 after the policy decision release. Incidentally, today's statement is likely reinforcing the degree of trust among investors that Norges Bank will not underdeliver when it comes to following their projected tightening plan.

All this is ultimately cementing expectations that NOK will be tied with NZD as the highest yielding currency in G10 for the foreseeable future. While the current choppy risk environment may keep preventing a sustained revamp in carry trades, the dissipation of some tail risks for global sentiment in the longer run may leave room for those currencies backed by tightening cycles to emerge as outperformers.

We expect to see EUR/NOK back at the 10.00 level by the end of the year, and also expect to see it trade consistently below the 10.00 mark in 2022. We think such a gradual appreciation profile for NOK will not tamper with the Norges Bank monetary tightening plans.

Authors

James Smith

Developed Markets Economist, UK

james.smith@ing.com

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.