Norges Bank Review: January 2022

Executive Summary:

- **Main Policy Rate unchanged at 0.50%, alongside MNI expectations**
- **Bank gave greenlight for next hike in March**
- **Wages, waning infection rates expected to contribute to higher underlying inflation ahead**

Policy statement: https://www.norges-bank.no/en/topics/Monetary-policy/Monetary-policy-meetings/2022/january-2022/

MNI Point of View

The Norges Bank kept the main policy rate unchanged at 0.50% in January, alongside the guidance published in December and inline with market expectations. As was the case at the last meeting, the bank name-checked March as the next most likely rate rise, giving the greenlight to further tightening across this year. This feeds into expectations that the Norges Bank will follow through with a rate hike at each policy report meeting (March, June, September, December) this year, leaving rates at 1.50% at year-end. This suggests there are significant upside risks to the front-end of the path projections going forward.

The bank's policy statement was broadly inline with the communication issued in December last year in identifying COVID as a rolling risk to the policy outlook. Although, the bank acknowledged the omicron variant appears less virulent relative to prior virus waves, and strengthened their language around wage formation and prices. The bank stated that the committee "was also concerned with the risk of a potential rise in domestic price and wage inflation due to capacity constraints and persistent global price pressures."

This small mention of wage inflation will likely be expanded upon materially at March's policy statement, and presents the largest upside risk to their rate path projections. This, twinned with COVID-restriction easing, financial stability risks and a tighter policy outlook among trading partners, all suggest the Norges Bank will retain their position as one of the most hawkish central banks in G10.

January's meeting marked the final appearance of Øystein Olsen as the bank's governor, as he steps down at the end of February. While his successor is yet to be confirmed, the more mechanical and model-based approach to policy-setting at the Norges Bank leaves little risk that the path projections will shift considerably under the leadership of a new governor.

Dates to Watch:

- **N/A –** New Norges Bank governor announced
- **Feb 10th** – January CPI
- **Feb 16th** – Q4 GDP
- **Mar 10th** – February CPI
- **Mar 15th** – RNS Outlook Survey
- **Mar 24th** – Rate decision and Monetary Policy Report

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Analyst Views (Alphabetical Order)

Barclays: To March and beyond

- Judging by recent data and the bank's statement, we think the case for a March hike and beyond has strengthened. Both core and headline inflation have overshot the bank's forecasts, due to supply-side constraints and higher energy prices. Importantly, the bank thinks underlying inflation is now close to target.
- Similarly, a tighter-than-expected labour market should fuel wage inflation and result in some second-round effects.
- We still call for four 25bp hikes this year and for the policy rate to at least revert back to the prepandemic level of 1.5%. We flag a high risk of more hikes beyond 2022, as we expect the bank to revise higher its terminal rate at the March meeting (currently at 1.75% in the December forecast. But we rule out more or bigger hikes this year (eg. 25bp interim meeting hikes or 50bp hikes at quarterly meetings).

ING: Green lights March rate hike

- The Norges Bank have formally given the green light to another rate rise at the March meeting. It made similar statements of intent ahead of both the September and December rate rises last year.
- It's worth remembering that Norges Bank tends to set policy more mechanically than most. And based on pretty much all of the usual factors that feed into the Bank's model, it looks like the next projection due in March will show both a faster pace of rate rises, and potentially a higher terminal rate, too.
- We expect Norges Bank to signal a total of four 2022 rate hikes at its meeting in March, and there's little reason to doubt that will happen.

Morgan Stanley: Hiking in March

- We see three hikes this year, with a risk of the rate path being lifted further in March, signalling action at each of the forecast meetings in 2022. Thursday's statement stressed that while there is still uncertainty around the pandemic, data have been a touch better than expected.
- Norges Bank reiterated, however, that it remains concerned about the upside risks to the inflation outlook stemming from a rise in wage inflation due to capacity constraints and "persistent global price pressures." In short, the Omicron impact was not as severe as projected in December, this pandemic wave is likely to peak in the coming weeks, and inflation risks remain tilted to the upside.
- Norges Bank reiterated its intention to hike in March, and with some of the uncertainty around the virus dissipating and the year-end inflation beats, it is likely to lift its rate path in March, which would then signal two more post-March hikes this year and a high probability of a third move too.

Nordea: Confirmation that key rate will be hiked in March

- The central bank confirmed that the key rate will be hiked in March: "In the Committee's current assessment of the outlook and balance of risks, the policy rate will most likely be raised in March."
- The statement from Norges Bank is mostly tilted to the positive side, noting the better-than-expected developments since December. Unemployment has risen less than Norges Bank's forecast while inflation has risen more and faster than expected and is now close to the target. The central bank notes that omicron is milder.
- The press statement includes some new hawkish tones from the central bank: "The Committee was also concerned with the risk of a potential rise in domestic price and wage inflation due to capacity constraints and persistent global price pressures." We think the central bank is correct in highlighting this risk and foresee a faster pick-up in inflation and wage growth than Norges Bank has done so far. Overall, today's statement from Norges Bank supports our long-held view for four rate hikes this year.

SEB: Confirming a March hike

- The Committee appears to have become less worried about a protracted economic downturn due to the current pandemic situation, while inflation concerns remain high. As such, the risk balance is tipping in favor of a higher rate path but there are yet many data to be released ahead of the March MPR.
- Considering the Committee's guidance and that economic developments (in our view) so far is pointing more towards upside- rather than downside risks a rate hike on Mar 24 is likely.
- We expect three additional hikes this year followed by a final move to 1.75% in 2023, which is broadly in line with current market pricing. Nonetheless, it implies an upward revision of the rate path for this year.

MNI Policy

MNI STATE OF PLAY: Norges Bank Holds But Cites Upside Risks

By David Robinson

Norway's central bank Thursday reaffirmed guidance that its next hike was likely in March and prepared the ground for a possible increase in its projected rate path, citing upside risks from lower-than-expected unemployment and elevated global inflation.

Commentary accompanying the decision by Norges Bank's Monetary Policy and Financial Stability Committee to hold rates as expected in January suggested that inflation pressures are higher than assumed in its December forecast, which was compatible with three hikes this year at most. Some analysts already expect it to increase rates four times in 2022, and they may now find confirmation in the next collective rates projection in March, when Norges indicated it is likely to raise the policy rate another 25 basis points to 0.75%

Despite the cushioning effect on surging energy prices from government support measures, the underlying inflation measure targeted by Norges jumped to 1.8% in December from 1.3% in November, where the Committee had previously assumed it would stay.

--PRICE PRESSURES

Inflation now looks set to increase, at least near term, with the Committee noting elevated price pressures in the UK and the U.S. and rises in rate expectations around the world.

Unemployment could also turn out "somewhat lower than projected," the Committee said, pointing to reduced uncertainty over Omicron and to the limited labour market effect of the hit to service sector spending from restrictions imposed in December to contain the Covid variant, thanks to government measures including a wage support scheme for affected businesses.

The strength of Norwegian public finances has made it easier for Norges to lead the way among global central banks in tightening policy, according to Governor Oystein Olsen, speaking to MNI following December's hike. That month's forecast round had foreseen unemployment at an already-low 2.4% in 2022.

"The policy rate should be raised towards a more normal level. A gradual normalisation of the policy rate is consistent with continued high employment. Higher interest rates will also help counter a build-up of financial imbalances," the Committee said on Thursday.

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