Norges Bank Preview: November 2022

Details:

Monetary policy decision: 0900GMT/1000CET/0500ET, Thursday 3rd Novmber 2022.

- No monetary policy report due, however a press conference is scheduled with governor Ida Wolden Bache at 0930GMT/1030CET/0530ET.

MNI Point of View

The bank signalled with the September monetary policy report that rates will rise further in November with the board likely choosing between another 50bps "double" hike, or a slower pace 25bps step that would mark the end of their front-loading policy bias.

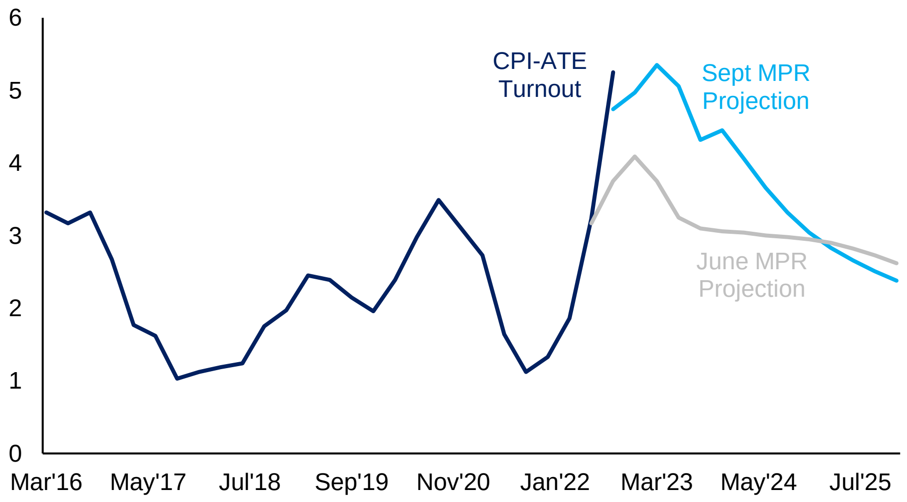
Punchy inflation, higher interest rates among trade partners and a very tight labour market argue for another sizeable 50bps step this month, but slowing real-time economic indicators, eroded household purchasing power and a deposit rate that's already above neutral give the bank space to slow the pace of tightening at this juncture. This makes a 25bps rate hike the most likely outcome in November.

Sell-side analysts are split almost down the middle between a 50bps move or a slower 25bps clip. This has fed directly into market pricing, with FRA spreads indicating a fine balance of expectations between a 2.50% and 2.75% rate for this month.

There are no new rate path projections or economic forecasts to accompany November's decision, although unusually the governor Ida Wolden-Bache will be holding a press conference 30 minutes following the decision. The Bank's schedule show the governor as presenting the Q3 monetary policy report, suggesting no unplanned data or rehashed forecasts will be disclosed. Nonetheless, the press conference gives the bank more opportunity to expand their language in September that "policy is starting to have a tightening effect on the Norwegian economy. This may suggest a more gradual approach to policy rate setting ahead."

A return to gradualism in November (i.e. a 25bps rate step) would keep the bank on track to meet the Q3 assumptions that the policy rate would reach "around 3 percent in […] winter" by turning out a 25bps rate hike in November, December and a third in January.

Figure 1: CPI-ATE has already accelerated to the Bank's projected inflation peak



Source: MNI/Norges Bank

Despite this relatively clear policy message, inflation continues to muddy the outlook. The CPI-ATE measure rose further in September, hitting a new cycle high of 5.3%. This puts core inflation close to what the Norges Bank had projected to be the peak inflation rate for this cycle – albeit ahead of schedule by around 3 months. In isolation, this puts upward pressure on the implied rate path and, twinned with an unemployment rate of just 1.6%, poses problems for wage-setting in 2023.

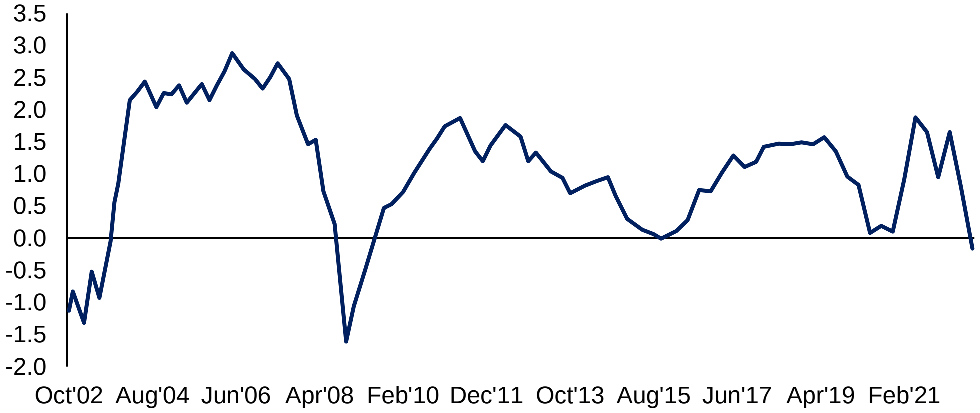
Figure 2: September report saw 50bps of further tightening across November and December decisions

	Jun'22 Report	Sep'22 Report	Change
30/06/2022	0.79	0.79	-
30/09/2022	1.39	1.53	+14bps
31/12/2022	1.99	2.45	+46bps
31/03/2023	2.53	2.82	+29bps
30/06/2023	2.87	3.03	+16bps
30/09/2023	3.04	3.11	+7bps
31/12/2023	3.10	3.10	-
31/03/2024	3.09	3.08	-1bps
30/06/2024	3.08	3.04	-4bps
30/09/2024	3.04	2.99	-5bps
31/12/2024	2.99	2.93	-6bps
31/03/2025	2.93	2.86	-7bps
30/06/2025	2.85	2.76	-9bps
30/09/2025	2.77	2.66	-11bps
31/12/2025	2.68	2.56	-12bps

Source: MNI/Norges Bank

Countering higher near-term inflation are the growing signs that the tightening cycle so far is bedding into household and business activity. The September policy report pointed to "clear signs of a slowdown in the Norwegian economy" which should contribute to curbing inflation going forward. This is reflected in the dire RNS surveys – a key input for Norges Bank policy-setting – which the bank will be expecting to deteriorate further at the December release.

Figure 3: Dire RNS Survey could keep peak of path projections from moving materially higher



Source: MNI/Norges Bank

FRA pricing relative to the interbank rate has fully priced a 25bps move, but only partially priced a 50bps rate hike this month. This makes for a hawkish reaction to any 50bps step, while a rate rise of 25bps would mark the end of front-loading from the G10 central bank that arguably led the global tightening cycle post-COVID.

Analyst Views (Alphabetical Order)

	Nov'22	Dec'22	Jan'22	Peak Rate
Barclays	+50bps	+25bps	+25bps	3.25%
Danske Bank	+25bps	Unch	Unch	2.50%
DNB	+50bps	-	-	-
HSBC	+50bps	+25bps	-	-
ING	+50bps	+25bps	-	3.00%
JP Morgan	+50bps	+25bps	-	3.00%
Nordea	+25bps	+25bps	Unch	2.75%
Scotiabank	+25bps	-	-	-
TD Securities	+25bps	-	-	-
Unicredit	+25bps	+25bps	+25bps	3.00%
SEB	+25bps	+25bps	Unch	2.75%
Swedbank	+50bps	+25bps	Unch	3.00%
Svenska Handelsbanken	+25bps	-	-	-

Barclays: Sees 100bps in further hikes this cycle

- Expects a 50bps hike in November, a further 25bps in December and another 25bps in January, leaving the terminal rate at 3.25%.

Danske Bank: Sees signals consistent with 25bps hike

- Since the last rate decision, inflation has once again surprised on the upside, leading to speculation that NB will deliver yet another 'double hike' of 50bp, despite the signals from September.
- In our view, however, there are at least three factors that differentiate the current situation from July/August – the 150bps in hikes to what NB believes is 50bps above the neutral rate, clear signs of a slowdown in growth and the inflation deviation in September only 0.25pp compared to 1.35pp in July.
- We cannot rule out that NB will deliver 50bp in November, but we consider that the probability is limited to around 20%. At the same time, we believe that NB will signal that policy rate most likely will be hiked again by 25bp in December. However, we still expect a rather strong slowdown, where unemployment is also starting to increase, so we expect NB to be on hold at the December meeting.

DNB: Expects a further 50bps

- While the central bank could elect for a more gradual rate hike path and raise the policy rate by 25bps, we believe recent data, which indicate even higher capacity utilisation and inflation, will prompt Norges Bank to raise the policy rate into contractive territory more quickly.
- The data released since the September meeting points towards a more aggressive tightening cycle. The labour market is a bit tighter than the central bank assumed in September, mainland GDP was 0.5% higher in August than Norges Bank forecast with these figures indicating that capacity utilisation has slightly exceeded Norges Bank's forecast.
- On inflation, if the core prices have increased in line with the 10-year average in October this year, core inflation would increase to 5.6% YOY in October, versus Norges Bank's forecast of 5.0%. This indicates that Norges Bank risks falling behind the curve if it hikes the policy rate by 25bp rather than 50bp.

HSBC: Sees bank waiting until December to pivot

- In recent meetings, 50bp has become the norm, and with inflation above the central banks' projections and the labour market proving to be tighter, we expect that pace to continue at this meeting.
- However, the central bank's own projection of what it would do at the meeting (from back in September) suggested that a 25bp increase was more likely, and given some of the downside risks for inflation and growth further out that are building, there is a chance that this slower pace of tightening is adopted at this meeting. We think that pivot will wait until December when we expect a 25bp increase.

ING: Sees 75 – 100bps in further hikes this cycle

- Having opted for multiple 50bp rate hikes through the summer, Norway's central bank hinted it could slow the pace back to 25bp for its final few moves. The question week is whether it instead decides to continue to front-load tightening, and we think it will.
- Higher overseas rate expectations and another massive upside surprise on inflation suggest we should expect another 50bp hike on Thursday. However that would take the central bank close to the end of its hiking cycle, and we are pencilling in one (or perhaps two) more 25bp moves before it pauses.

JP Morgan: Expects 50bps rate rise, with material risk of a smaller hike

- Expects a 50bps rate hike, but risk is heavily skewed towards a smaller move. Consensus is leaning towards a 25bp rate hike while markets price in around 38bps.
- We expect governor Bache to say the end of the tightening cycle is near. The outcome of the September meeting widely changed expectations for the upcoming November 3 meeting from a rate hike of 50bp to 25bp. We on the other hand decided to stick to our forecast of a 50bp rate hike in November, with the risk heavily skewed toward 25bp.
- Overall, the data have clearly been better-than-expected, in turn leaving upside risk to Norges Bank´s rate path. A new rate path is not presented at the November meeting, but our calculations suggest a "what-if" rate path would have shown a need to frontload rates and lift the terminal rate from 3.11% to 3.25%.
- Despite the central call for a 50bps rate rise, JPM present four main arguments for why Norges Bank may opt for only a 25bp rate hike: September rate path showed no probability of a 50bp rate hike in November and the change of rhetoric at the September press conference was significant, with the word "gradual" being used a number of times. Thirdly, the policy rate is already above neutral and while key data have been better than expected, leading indicators still point to a slowdown in economic activity.
- Our main expectation is that the governor will say the end of the tightening cycle is near and that rate hikes should be in smaller steps from now on. Beyond the November meeting we only expect a rate hike of 25bp in December, leaving the terminal rate at 3%.

Nordea: Back to 25bp hikes

- We believe Norges Bank will stick to the plan they laid out in September and raise the key rate by 25bp at their November meeting and see the bar for another 50bp hike clearly higher after they frontloaded their planned rate hikes due to higher inflation.
- As such, the September meeting marked a shift towards more moderate rate hikes going forward and a central bank that will use the time to assess the effects of the hikes already delivered.
- We don't think that the press conference will offer real "news". Norges Bank will likely repeat the message from September and go over through the data published since their last meeting as no new forecasts will be made for this meeting.
- Overall, our calculations suggest the rate path in the front end of the curve is broadly unchanged compared to the one from September and only slightly higher further out. In our view, the changes are not significant enough to deviate from the rate plan laid out in September which had a 25 bp hike in November (and December) built in.

- While we don't expect a 50bp rate hike in November and hold our view for 25bp rate hike in December, we cannot totally exclude the probability for a 50bp hike in December. If unemployment continues to stay at very low levels, core inflation continues to surprise on the upside and the NOK weakens significantly, Norges Bank might feel the need to act more forcefully.

Scotiabank: Expect a 25bps rate hike

- After hiking by 50bps at its last meeting on September 22nd, the central bank guided that "Monetary policy is starting to have a tightening effect on the Norwegian economy. This may suggest a more gradual approach to policy rate setting ahead."

TD Securities: Believes bank will follow guidance and slow hikes

- We think Norges Bank will follow through with its guidance from the last meeting and deliver a 25bps hike, despite the substantial upside surprise to the last inflation print and improvements in growth.
- Instead, we expect the Bank to continue to signal that it will respond to the incoming data, and keep the door open to a 50bps hike in December.

Unicredit: Balance now tilting towards GDP prospects, leaning toward smaller 25bps hike

- Highly likely to stick to its plan to increase its policy rate to 2.50% (from 2.25%) and signal that the next rate hike will come in December.
- Beyond November, we expect the NB to deliver two more interest-rate hikes, by 25bp each, over the course of winter, taking the policy rate to a peak of 3% in this cycle.
- At the time of the policy-rate decision in September, Governor Bache said that monetary policy is starting to have a tightening effect on the Norwegian economy. This was confirmed by the last regional survey, which highlighted that the sharp rise in firms' selling prices, due mainly to higher costs for electricity, and higher interest rates are starting to have a dampening effect on demand, particularly on household spending and the construction sector.
- We think that the balance is now gradually tilting towards GDP prospects. This is likely to lead the NB to continue its sequence of policy-rate hikes, although at a slower pace than the 50bp delivered in September.

SEB: A close call, but Norges Bank to remain calm

- Though capacity utilization appears to be higher than envisaged, sentiment indicators still point to a sharp slowdown ahead. We believe the latter will convince Norges Bank to stick to its cautious approach. Though it is a close call we expect the Committee to deliver a 25bps hike to 2.50%, in line with its guidance.
- Recent developments lend upside risk, suggesting close to a 50/50 call to whether the bank will deliver a 25bps or 50bps hike. We stick to our call for a 25bps increase to 2.50%, in line with consensus, but the market discounts approx. a 70% chance for a larger hike.
- Data published since the September MPR has mainly surprised on the upside, supporting the market's expectation of a high chance for a 50bps hike, however the September MPR showed that Norges Bank is becoming more growth-oriented in its policy deliberations, suggesting that underlying drivers for inflation (rather than spot inflation) are becoming increasingly important for the policy outlook.
- Hence, the outlook for growth, the assessment of the output gap and the labour market will be highly important in the assessment of long-term inflation risks. Should inflation continue to surprise on the upside, and economic activity not show signs of weakening, a 50bps hike may be justified at the following Dec 15 decision when new projections are being released. As of now, our policy rate forecast implies a final 25bps increase to 2.75%.

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Swedbank: Expects 75bps in further hikes, with a 50bps step in November

- Our expectation is for Norges Bank to end its hiking campaign at 3.00% by this year's end, and to refrain from hiking rates next year. We expect a 50 bps hike at the meeting in November and 25 bps in December. We expect Norges Bank to start cutting rates in September 2023.
- Inflation has yet again surprised on the upside since the latest Norges Bank projections and two monthly releases of the NAV unemployment data has surprised on the downside, suggesting tighter labour markets than Norges Bank projected.
- While most of the inflation surge is stemming from global supply elements, Norges Bank's fear is to see price-wage spirals starting off on the back of the tightest labour market conditions since before the financial crisis. Higher wage growth will result in higher inflation and will make Norges Bank's job harder. So if they do not hike rates now, they might be forced to hike even faster at a later stage.
- The risks of a starting price-wage spiral are prominent. What is important is to avoid seeing high inflation feed into secondary wage effects. As higher mortgage rates feed through the economy, the outlook is becoming even bleaker and the real value of household bank deposits (liquid part of savings) are soon back to pre-pandemic trend.
- We are very shortly approaching a 'peak hawkishness' pivot from several central banks – and Norges Bank should be part of that. Possibly indicating more explicitly that they will hike by 'only' 25 bps in December.

Svenska Handelsbanken: Expects a rate hike of 25bps to 2.50%

- We assume that Norges Bank will stick to the plan this time, and thus raise the interest rate by 25bps, to 2.50%. We cannot, however, ignore the possibility of another double increase.
- Looking at the backdrop, both the real economy and (not least) core inflation have continued to surprise on the upside. Core inflation has surprised Norges Bank on the upside again and the deviation is also significant. All told, it boils down to whether slightly lower unemployment, coupled with even higher core inflation, will cause Norges Bank to deviate yet again from its own strategy and carry out yet another double interest rate increase.
- We still expect Norges Bank to stick to its strategy from September, and lift rates by a more cautious 25bps. The background to this is that we are now in a situation where the interest rate is already slightly elevated. It is no longer correct to claim that interest rates are only normalising after the pandemic.
- We believe that Norges Bank will tone down the fact that the key figures have surprised on the upside recently, especially considering that it also takes time before interest rate increases have their full impact on the economy.