

Norges Bank Review: August 2020

Executive Summary:

- As expected, the Norges Bank kept its key policy rate unchanged at 0% in a unanimous decision.
- The decision and accompanying statement did nothing to change analysts' views on future Norges Bank policy, with broad expectation that rates will be on hold for the foreseeable future, with the next move being a hike, either in 2021 or 2022.
- Market reaction was muted, given that the decision was well-anticipated.

Links:

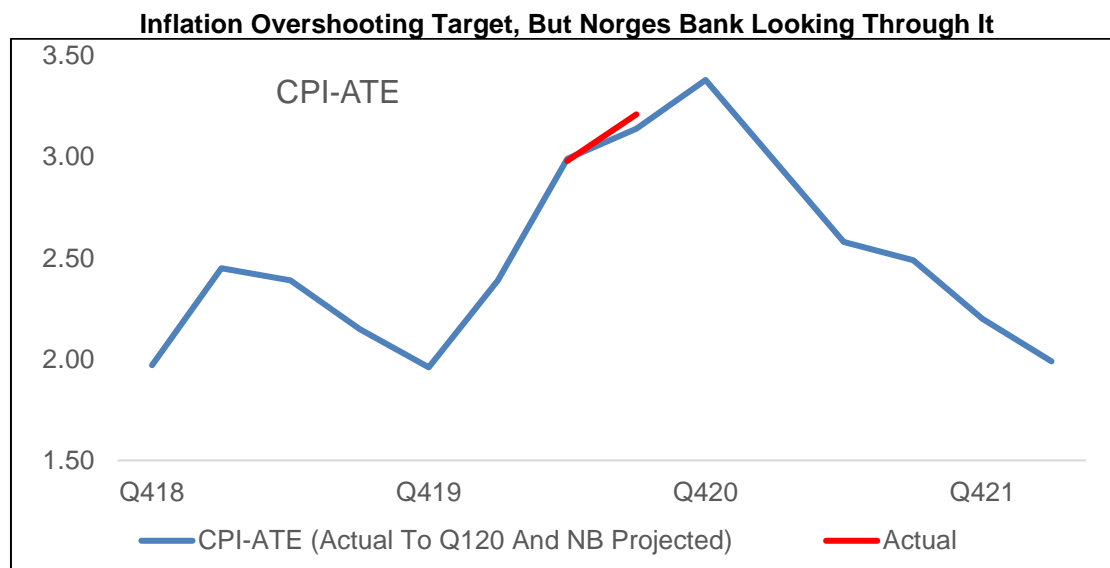
- **Monetary Policy Statement:** <https://www.norges-bank.no/en/topics/Monetary-policy/Monetary-policy-meetings/2020/august-2020/>
- **Monetary Policy Assessment:** <https://www.norges-bank.no/en/topics/Monetary-policy/Monetary-policy-meetings/2020/august-2020/?tab=111258>

Key Takeaways:

The Norges Bank left policy rates unchanged in a unanimous decision in which they stated that the "New information largely confirms the picture of the economic developments presented in the June Report."

The Norges Bank did not release new forecasts, just gave updates in relation to the June MPR stating "Economic activity overall appears to have picked up broadly as projected in the June Report."

On inflation: "Overall inflation is low. At the same time, underlying inflation has risen and is higher than the inflation target. The krone appreciation and prospects for low wage growth suggest that inflation will moderate further out."



Source: Norges Bank Jun Projections, Statistics Norway, MNI

The forward guidance removes the explicit reference to rate hikes except in response to the June forecasts. It now reads: "The Committee's assessment of the outlook and balance of risks suggests that the policy rate will most likely remain at today's level for some time ahead." In June it said: "The policy rate forecast implies a rate at the current level over the next couple of years, followed by a gradual rise as economic conditions normalise."

On the balance of risks: "The Committee gave weight to the considerable uncertainty surrounding the further economic recovery. Recently, the spread of Covid-19 has increased, and some containment measures have been reintroduced. The Committee also focused on housing market developments. Persistently high house price inflation may result in accumulating financial imbalances."

Dates to Watch:

August 27th – July Retail Sales

September 1st – August Manufacturing PMI

September 3rd – August House Prices

September 24th – Norges Bank Rate Decision (with Monetary Policy Report and new projections)

Analyst Views (Alphabetical Order):

Barclays: Constructive But Cautious

- The committee struck a constructive but cautious tone, and emphasised five points:
- No significant changes in outlook from the June meeting; willing to look through recent inflation overshoots; cautious on the domestic econ outlook given COVID uncertainty; mixed global conditions; and futures prices indicating only a modest rise in prices in the years ahead.
- We remain medium-term constructive on NOK, but believe material near-term normalisation of NOK vs EUR and SEK is predicated on supportive risk sentiment and higher oil prices, and we are not there.

Danske: Little To Report

- NB, as we expected, recognised that both private consumption and the housing market had developed better than expected, and that inflation had been higher. On the other side, NB stressed that the 'Committee gave weight to the considerable uncertainty surrounding the further economic recovery'.
- Overall, NB concluded that 'New information largely confirms the picture of the economic developments presented in the June Report'. So, no new signals today.
- Market reaction in FI and FX markets was limited (rates marginally lower which might reflect that some market participants had been expecting a more upbeat rhetoric), but as we believe NB will be more upbeat at its September meeting, where we see a good chance of a new upward revision to the rate path, we still see upside for the 5y segment of the curve and keep our positive NOK view.

ING: Cautiously Optimistic Stance

- While the short statement emphasised there are plenty of unknowns in the outlook, the reality is that there's not a great deal more policymakers can add in terms of support.
- Don't expect rates to move in either direction any time soon.
- The statement emphasises that the recent data flow has largely backed up Norges Bank's cautiously optimistic outlook.
- Norges Bank is loosely pencilling in a rate hike for 2022, although clearly a lot can change between now and then.

Nordea: No New Signals

- Overall, we see today's statement as fairly neutral. Norges Bank will continue to monitor developments until its September meeting.
- Their conclusion is that "the policy rate will most likely remain at today's level for some time ahead", the same as in June.
- In terms of risks, the bank noted uncertainty about the economic recovery due to the rise in new COVID cases both in Norway and abroad, while developments in the housing market (stronger than expected) may lead to financial imbalances down the road.

SEB: A Balanced Message

- Considering that economic developments have been broadly as expected, while financial stability risks have increased, one may conclude that this points to a higher rate path. However, uncertainty to the economic outlook has increased which may be balancing the path – for now. There are lots of important data releases in the coming month that will give decisive input on the risk outlook for the economy.
- These include Q2 national account data / July GDP and the Regional Network Report.
- The Committee concluded that "the outlook and balance of risks suggests that the policy rate will most likely remain at today's level for some time ahead". The only difference from the June MPR being "some time ahead" instead of "in the coming period".
- However, the rate path from June does not signal a rate hike until year-end 2022 and in our opinion the conclusion is thus validating the June path (which implied a total of three rate hikes until end-2023).
- While CPI-ATE inflation is running above Norges Bank's trajectory, the June trajectory implies that CPI-ATE will be below target in both 2022 and 2023. Hence, temporarily high inflation is not influencing the monetary policy stance.
- Despite the bank's flexible inflation target, it considers financial stability, and we believe accelerating home price growth due to the record-low interest rates is likely to justify a rate hike in H2 2022 despite the output gap remaining negative.

Swedbank: Rate Increase Coming In 2021

- As expected little new. But in the details we find two interesting remarks about the risk picture: On the one hand, the COVID increase is mentioned: "Recently, the spread of Covid-19 has increased, and some containment measures have been reintroduced." This poses a downside risk.
- On the other hand, and more interestingly, Norges Bank found it appropriate to mention housing market and credit in particular: "The Committee also focused on housing market developments. Persistently high house price inflation may result in accumulating financial imbalances."
- We read this as follows: If virus outbreaks are brought under control again (as we expect, and it may well be clear even before the September meeting) and the housing market continues to grow strongly (with extremely low interest rates and good access to credit to households this seems very likely) then Norges Bank on the margin tends to raise the interest rate path further in September.
- This is our main case going forward, and we maintain our bullish view of Norges Bank for the coming year. Expect the first interest rate rise in 2021!

MNI POLICY

Norges Bank On Hold; No Word On Tightening

- Governor Olsen Says Balance Of Risks Suggests Rates At Current Level For Some Time

The Norges Bank left policy unchanged in August, keeping the benchmark policy rate at a record low 0%, with the Monetary Policy and Financial Stability Committee seeing the economy evolving broadly in line with its latest quarterly projections, published in June. But policymakers did not repeat explicitly June's line that rates were likely to rise towards the forecast horizon.

The Committee's June projections were based on a collective rate path that showed the policy rate holding at zero for a couple of years before edging up in 2022 and reaching 0.5% in 2023, at the end of the forecast period.

In its policy announcement Thursday, the committee said nothing about future tightening.

--UNCHANGED FOR SOME TIME

"The Committee's assessment of the outlook and balance of risks suggests that the policy rate will most likely remain at today's level for some time ahead", Governor Oystein Olsen said.

No new economic projections was issued in August and while the committee said that "new information largely confirms the picture of the economic developments presented in the June Report," it did identify some downside risks.

While output picked up in line with its projections, with May data showing a 2.4% rise, the labour market was weaker than expected. The committee also cited concerns about a pick-up in Covid-19 infection rates, which have been low by international standards in Norway.

Inflation on the target measure, CPI-ATE, was stronger than forecast, hitting 3.5% in July. The committee said that the strengthening of the krone, which plunged in March as the Covid pandemic roiled global markets but has since rallied on its I-44 import weighted measure back to pre-pandemic levels, should bring inflation back down.

"The krone appreciation and prospects for low wage growth suggest that inflation will moderate further out," the committee said.