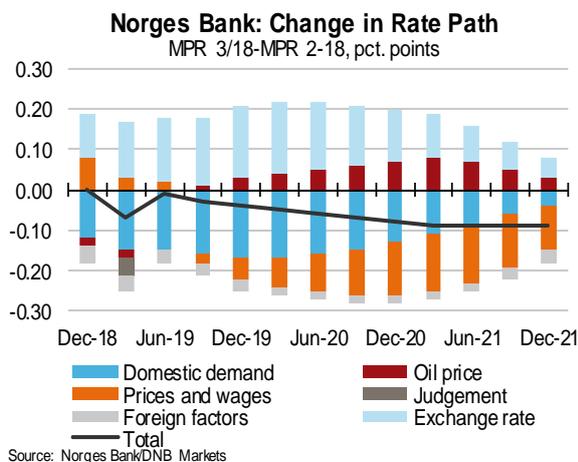


Norges Bank commits to interest rate path

- **Norges Bank precommitted and able to pull off two hikes,...**
- **...before the ECB needs to follow suit.**
- **NOK to trade on the backfoot in H2, but monetary policy normalization will eventually lend support**

By lowering the interest rate path,... Norges Bank hiked the key interest rate by 25bp as widely expected, but against our and market expectations for a higher interest rate path, the path was lowered by up to 9bp. The new interest rate path indicates a rate hike in March and September next year (priced in full), reducing the probability of a January hike by 45pp to 20% (Q1 2019 is the only quarter Norges Bank use their judgement to change the interest rate path). Further out on the curve, the central bank still expects 2 hikes in 2020, while 2021 only fully prices 1 hike.

...Norges Bank commits to the interest rate path. Looking at the interest rate account (see below graph), we struggle to align the central bank's previous modus operandi and changes in fundamentals since the latest MPR in June with the changes in the interest rate path. In particular, the negative contributions from "Domestic demand" and "Prices and Wages" were larger than we expected. While it could be a dovish assessment of the state of the economy, it could be seen in a different context; the central bank is on a predetermined path to normalize policy, while seeing their degrees of freedom limited from interest rate differentials/exchange rate and housing market/household debt concerns. In fact, Governor Olsen at the press conference said "...there are limits to the pace and number of interest rate hikes, given exchange rate considerations". Hiking rates twice without the support from ECB-hikes may be possible without too large an effect on the NOK, but surely the third hike needs to be aligned with the ECB. **Thus, while the interest rate path from June should have been lifted, this may not be the time to conduct monetary policy on a pure 3m delta-approach.**



For now, Norges Bank has its cake and eats it too. We have flagged our expectations for a continued soft risk sentiment to reduce the appetite for NOK. Despite hiking interest rates, Norges Bank is lending this argument support as it flags lower domestic growth momentum, a slower pace of labour market tightening and concerns over protectionism and emerging market concerns. Thus, we expect NOK to trade on the backfoot in H2 and Norges Bank to avoid an appreciating currency lowering the inflation outlook.

However, while fundamentals have done a poor job explaining NOK performance of late, we expect the continued monetary policy normalization to eventually start benefitting the NOK.

Expect EURNOK @ 9.50 in 3 months and 9.30 in 12 months.

DNB Markets Macro Analysis

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