13 January 2023

Weekly Focus

Markets are rallying but is it premature?

Year 2023 has delivered for risk lovers thus far. Early signs of moderating core price pressures in the US, Chinese reopening and a mild winter in Europe are altogether positive signals for risky assets in short term. The problem is that a premature easing in financial conditions risks upholding underlying price pressures, and central banks are by no means out of the woods as they aim to make sure that the current price pressures are tamed for good. The ECB particularly finds itself in a tricky position as core inflation has kept rising, and soon, pent-up demand from China could create new inflationary concerns. See our *Euro Macro Notes – The China connection: short-term boost, long-term worry*, 12 January.

The sudden change of fortunes has driven a substantial outperformance in European equities vs the US over the last 2-3 months. European equities have gained 13% since the start of November compared to only 3% in the US. Meanwhile, EUR/USD has continued to tick higher, breaching 1.085 this week. We are in the process of updating our EUR/USD forecast, and while we still see fundamentals favouring USD in 6-12 months horizon, it is difficult to pinpoint a trigger for a near term reversal.

This week, US December CPI came out close to our and consensus expectations, but the details suggest underlying price pressures could be starting to moderate. Core services inflation picked up to 0.5% m/m (from 0.4%), but the uptick was driven by higher shelter and health care components, while the most wage-sensitive components showed easing price pressures. We have updated our call and we now expect Fed to hike by 25bp (was 50bp) in February. We continue to think that easing financial conditions, less negative growth outlook and economic recovery in China create persistent inflation risks, and still think the Fed will eventually hike the policy rate to 5.00-5.25% in May (prev. March). See *US Labour Market Monitor*, 11 January and *Global Inflation Watch – Central banks welcome easing inflation*, 13 January, for our latest thoughts on inflation developments.

Next week, we get Q4 GDP data from China on Tuesday morning, which is expected to drop 1% q/q due to the negative lockdown effects in November and covid surge in December. We also get industrial production, retail sales, investments and unemployment for December, which will most likely look very weak. The negative numbers should be followed by a faster-than-expected rebound during H1, though, as the positive reopening effects come through.

In the US, December PPI, retail sales and industrial production data are all released on Wednesday. Retail sales is the most important of the bunch, as it will be the first piece of hard data for December, and will give us a sense of if the sharp slowdown illustrated by the ISM services actually took place. The FOMC blackout will begin on the 21st, and investors will keep an eye on any last minute commentary.

In the euro area, we have ZEW expectations for January due on Tuesday and ECB minutes on Thursday. In the former, it will be interesting to see whether the recent rebound in leading indicators persists into Q1. In the latter, we look out for more details surrounding the upcoming balance sheet normalisation (QT) and how much more 'significant' interest rate increases the Governing Council has in mind in light of the inflation outlook.

Key global views

- Europe in recession during the winter. US recession hits in Q2 23.
- US and euro area headline inflation has peaked and set to come down gradually. Tight labour markets and wage pressures to keep core inflation high for some time.
- The Fed to hike by 25bp in February but still target peak rate at 5.00-5.25% in May. ECB to hike by 50bp in February and March, and by 25bp in May.

Key market movers

- Tuesday: Germany ZEW index, China GDP
- Wednesday: US retail sales
- Thursday: ECB minutes

Selected reading from Danske Bank

- *Global Inflation Watch - Central banks welcome easing wage inflation*, 13 January
- *Euro Macro Notes - The China connection: short-term boost, long-term worry*, 12 January
- *US Labour Market Monitor - Easing wage sum growth suggests Fed is moving in the right direction*, 11 January

Editor

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Scandi market movers

- No scheduled events in **Denmark** next week.
- With a very empty macro calendar in **Sweden** next week, we have wanted to share some thoughts about the Swedish housing market, where prices have fallen 12% s.a. since the peak in February/March. In an international perspective, one can note that the Swedish housing market has evolved in line with New Zeeland but has fallen much more compared to the US, Canada and Norway. Although tumbling prices, the price level is still above pre pandemic prices.

  What is causing the big drop in prices? As in most other countries, the Riksbank has raised the interest in a very fast pace in a response to the sharp increase in inflation, from zero in early 2022 to 2.5% and with more hikes is expected from here. We expect at least 50bp with a risk for an additional hike in April. Markets have for a long time expected much more than that but has during the past two weeks dropped and is now more in line with our risk scenario (75bp from here).

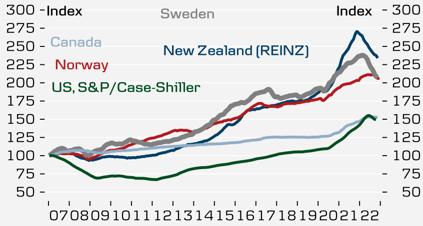
  If all other central banks are hiking policy rates, why are Swedish prices falling more? Swedish households are very rate sensitive due to around 50% being floating rate, with the bulk of the rest with rates fixed for only 1-3 years. This means that Swedish households feel the rate hikes much more quickly than many other countries.

  We estimates that interest costs as a share of disposable income after tax will gradually triple from just over 2% to just over 6%. And if looking at new loans, we estimate that mortgage costs of disposable income will increase to just below 15% from 10% in 2022, which also can be compared to 5% in 2019. In Stockholm, where prices are higher and hence LTVs higher as well, we estimate that the mortgage cost will increase to 19% from earlier 12% (6% in 2019) on new loans.

  Our earlier call is for a drop of 20% in housing prices from the peak imply that there is another 8pp to go from current levels and the risk, as we see it, is for a larger drop than that. Surprisingly, housing prices seem to stabilize somewhat in November and December despite the Riksbank raising its policy rate by a further 75bp during the same period. We think this is only a temporary reprieve, however, partly because these hikes have not yet had their full impact on the economy, and partly because we expect the policy rate to go up at least another 50bp.

  Housing prices will probably not stabilize until late spring, when the focus should have shifted from rate increases to rate cuts, and inflation will have begun to come down.

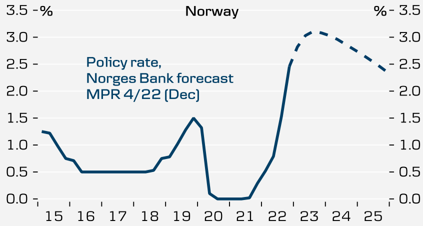
Swedish housing prices in an international perspective



Source: Macrobond

In **Norway**, Norges Bank said at its December rate-setting meeting that “the policy rate will most likely be raised further in the first quarter of next year”. It was clear from both the bank’s projections and especially the press conference that it was thinking here of the March meeting. This was, of course, supported by the absence of a direct reference to “the next meeting”, which would have been natural if the bank had anticipated raising the policy rate in January. This means that the threshold for a rate hike at the January meeting is very high, and we cannot see anything in the data to justify one. The reason why Norges Bank signalled in December that it would leave the policy rate unchanged in January after raising it at five successive meetings was, of course, that “the policy rate has been raised considerably over a short period of time, and monetary policy has started to have a tightening effect on the economy. There are signs that the slowdown may prove somewhat more pronounced than envisaged in September.” This points to a somewhat more cautious approach. We expect the bank to repeat that the policy rate will most likely be raised again in March.

Norges Bank signalling rate hike in March



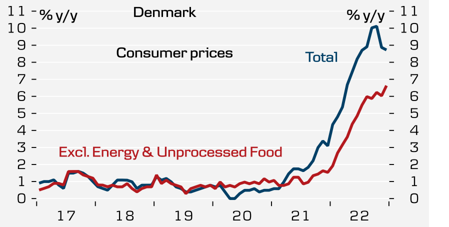
Source: Macrobond, Danske Bank

Scandi update

Denmark – inflation dips, but not out of the woods yet

Inflation declined once again in December, to 8.7% from 8.9% in November, taking inflation for the year overall to 7.7% – the highest since 1982. Electricity and fuel prices were major contributors to the decline, though food prices provided the most surprising fall. Nevertheless, inflation ex. food and energy rose slightly from 6.0% in November to 6.6% in December, underlining that price pressures in the economy remain significant. We expect inflation to fall steadily in 2023, mainly for two reasons. First, we expect the global economy to deteriorate further and central bank rate hikes to begin putting a damper on growth. Second, many prices were already rising in early 2022, so annual growth rates are therefore set to ease in 2023 due to bases effects.

Inflation remains unduly high



Source: Statistics Denmark, Macrobond Financial

Residential property prices continued to tumble in December according to Boligsiden's market index. House prices fell 2.7% nationally between November and December, while apartment prices declined by 1.8%. Taking into account that price growth in December is normally more negative than during the rest of the year, that indicates a 1.9% decrease for house prices and 1.3% for apartments from November to December when seasonally adjusted. Since peaking in April, house prices have shed 8% nationally, and we expect the slide to continue. Sales activity is extremely low, showings have been falling steadily and price discounts have been increasing. Moreover, while long-term interest rates have decreased slightly, short rates still have some upward momentum, in our view.

The number of jobless rose by 2,600 between November and December according to Statistics Denmark's preliminary estimate, while the increase in November was revised up from 1,200 to 3,100. Unemployment rising by 5,700 over two months is not particularly dramatic and the numbers are subject to various uncertainties, but we nevertheless suspect the labour market may have begun to turn. Companies have been reporting plans to cut employee numbers for quite some time, though there has also been a considerable backlog of unfilled positions and labour shortages that have tended to pull unemployment down. While unemployment remains low, we have to conclude that the labour market is now less tight than it has been. That points to lower pay increases in 2023, though the combination of high inflation and the ongoing rounds of collective bargaining will likely pull in the opposite direction so the result is higher wage growth.

Denmark's current account surplus fell by DKK1.4bn in November and was thus DKK6.1bn down on August's peak of DKK37.9bn. We expect the surplus to shrink further on the back of lower freight rates in the shipping industry.

December saw 226 bankruptcies among active companies compared to 269 in November. For 2022 as a whole, the figure was 2,834, the highest since 2012. We very much view this as fallout from the ending of the Covid-19 relief packages – we have yet to experience the full impact of the recession and higher interest rates.

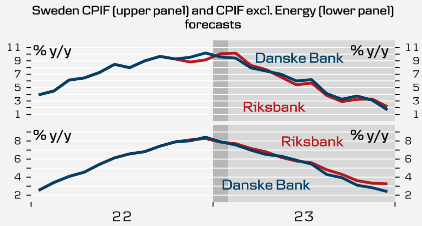
Sweden – Inflation again on the high side

December inflation turned out higher than expectations – ours, the market's and Riksbank's. And the deviation was consistent for all measures i.e. CPI, CPIF and CPIF excl. energy. The difference from Riksbank's forecast was huge for CPIF (10.2 % yoy vs 9.1 % yoy forecast) but less so for CPIF excl. Energy (8.4 % yoy vs 8.3 % yoy).

In our view, this suggests Riksbank will deliver a 50 bp rate hike in February which has been our call for some time. This is 25 bp more than in Riksbank's forecast. Actually, although not our base case, we believe the probability for another 25 bp in April has increased.

Taking a step back, December was probably the inflation peak. This should really not be a surprise as we see these tendency on an international scale. That said, significantly higher energy prices and further aggressive interest hikes from Riksbank may push CPIF and CPI higher yet. Surely, the upside risks for core inflation CPIF excl. Energy also dominates in the near-term. For instance, there is considerable uncertainty about the magnitude of second-round effects from high inflation in the autumn of 2022 that could hit the January outcome.

Sweden: December probably marks peak inflation

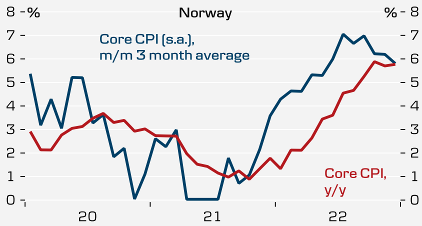


Source: SCB

Norway – Lower inflation risk

It is beginning to look as though core inflation has peaked, although inflationary pressures remain strong. The monthly rate seems to have maxed out in July and has been slowly but surely coming down again. This is partly because cost pressures from commodities, energy, freight rates and so on have eased, but also because it has become harder to pass on cost increases to customers. The latter may mean that firms' profitability gets squeezed, which would normally lead to cost-cutting, including downsizing. On the other hand, mainland GDP grew by 0.2% m/m in November. So while growth is slowing, activity is holding up better than feared given strong cost pressures, rapid inflation, higher interest rates and a global slowdown.

Inflation has peaked



Source: Macrobond, Danske Bank

Calendar

Monday, January 16, 2023				Period	Danske Bank	Consensus	Previous
8:00	NOK	Trade balance	NOK bn	Dec			101.1

Tuesday, January 17, 2023				Period	Danske Bank	Consensus	Previous
3:00	CNY	Industrial production	y/y	Dec		0.2%	2.2%
3:00	CNY	Retail sales	y/y	Dec		-9.5%	-5.9%
3:00	CNY	Real GDP	q/q|y/y	4th quarter		-1.2%|1.6%	3.9%|3.9%
3:00	CNY	Fixed assets investments	y/y	Dec		5.0%	5.3%
8:00	GBP	Average weekly earnings ex bonuses (3M)	y/y	Nov		6.3%	6.1%
8:00	GBP	Unemployment rate (3M)	%	Nov		3.7%	3.7%
8:00	DEM	HICP, final	m/m|y/y	Dec		-1.2%|9.6%	-1.2%|9.6%
10:00	ITL	HICP, final	m/m|y/y	Dec		...|12.3%	...|12.3%
11:00	DEM	ZEW current situation	Index	Jan		-58.5	-61.4
11:00	DEM	ZEW expectations	Index	Jan		-15.0	-23.3
14:30	USD	Empire Manufacturing PMI	Index	Jan		-8.7	-11.2
14:30	CAD	CPI	m/m|y/y	Dec			...|6.8%
15:00	USD	Fed's George speaks					
21:00	USD	Fed's Williams speaks					

Wednesday, January 18, 2023				Period	Danske Bank	Consensus	Previous
-	JPY	BoJ policy rate	%		-0.1%		-0.1%
5:30	JPY	Industrial production, final	m/m|y/y	Nov			-0.1%|-1.3%
8:00	GBP	CPI	m/m|y/y	Dec	...|10.6%	0.3%|10.5%	0.4%|10.7%
8:00	GBP	CPI core	y/y	Dec		6.3%	6.3%
11:00	EUR	HICP inflation, final	m/m|y/y	Dec	-0.3%|9.2%	-0.3%|9.2%	-0.3%|9.2%
11:00	EUR	HICP - core inflation, final	y/y	Dec	5.2%	5.2%	5.2%
14:30	USD	Retail sales control group	m/m	Dec		-0.5%	-0.2%
14:30	USD	PPI	m/m|y/y	Dec		-0.1%|6.8%	0.3%|7.4%
14:30	USD	PPI core	m/m|y/y	Dec		0.1%|5.4%	0.4%|6.2%
15:00	USD	Fed's Bostic speaks					
15:15	USD	Capacity utilization	%	Dec		79.6%	79.7%
15:15	USD	Industrial production	m/m	Dec		-0.1%	-0.2%
15:15	USD	Manufacturing production	m/m	Dec		-0.2%	-0.6%
16:00	USD	Fed's George speaks					
16:00	USD	NAHB Housing Market Index	Index	Jan		31.0	31.0
18:00	USD	Fed's George speaks					
20:00	USD	Fed's Harker speaks					
22:00	USD	TICS international capital flow, Net inflow	USD bn	Nov			179.9

Thursday, January 19, 2023				Period	Danske Bank	Consensus	Previous
0:50	JPY	Exports	y/y (%)	Dec		0.1	0.2
0:50	JPY	Import	y/y (%)	Dec		0.2	0.3
0:50	JPY	Trade balance, s.a.	JPY bn	Dec		-1630.6	-1732.3
1:01	GBP	RICS house price balance	Index	Dec		-0.3	-0.3
1:30	AUD	Employment change	1000	Dec		22.5	64
8:00	NOK	Industrial confidence (SSB)	Net. bal.	4th quarter			-4.4
10:00	NOK	Norges Banks monetary policy meeting	%		2.8%	2.8%	2.8%
10:00	EUR	Current account	EUR bn	Nov			-0.4
12:00	TRY	Central Bank of Turkey rate decision	%		9.0%	9.0%	9.0%
14:30	USD	Initial jobless claims	1000				205
14:30	USD	Building permits	1000 (m/m)	Dec		1370	1351.0 (-10.6%)
14:30	USD	Housing starts	1000 (m/m)	Dec		1350	1427.0 (-0.5%)
14:30	USD	Philly Fed index	Index	Jan		-10.0	-13.7
17:00	USD	DOE U.S. crude oil inventories	K				18961
19:15	USD	Fed's Brainard speaks					

Friday, January 20, 2023				Period	Danske Bank	Consensus	Previous
-	EUR	Fitch publish Ireland's debt rating					
0:30	JPY	CPI - national	y/y	Dec		4.0%	3.8%
0:30	JPY	CPI - national ex. fresh food	y/y	Dec		4.0%	3.7%
0:35	USD	Fed's Williams speaks					
1:01	GBP	GfK consumer confidence	Index	Jan		-42.0	-42.0
8:00	GBP	Retail sales ex fuels	m/m|y/y	Dec		0.3%|-4.6%	-0.3%|-5.9%
14:30	CAD	Retail sales	m/m	Nov			1.4%
15:00	USD	Fed's Harker speaks					
16:00	USD	Existing home sales	m (m/m)	Dec		3.96	4.09|-0.077
19:00	USD	Fed's Waller speaks					

Source: Danske Bank

Macroeconomic forecast

Macro forecast. Scandinavia

	Year	GDP [1]	Private cons.[1]	Public cons.[1]	Fixed inv.[1]	Ex-ports[1]	Im-ports[1]	Infla-tion[1]	Wage growth[1]	Unem-ploym[3]	Public budget[4]	Public debt[4]	Current acc.[4]
Denmark	2022	2.9	-2.6	-1.1	4.4	7.4	3.2	7.7	3.5	2.6	1.2	29.7	11.8
	2023	-1.0	-2.3	0.0	-3.3	1.3	-0.7	4.9	4.1	3.1	1.0	28.1	9.5
	2024	1.0	1.8	0.9	-2.1	1.2	0.4	2.0	4.2	3.4	0.8	27.0	9.5
Sweden	2022	2.6	2.6	-0.2	5.6	4.6	7.9	8.4	2.5	7.5	0.7	31.0	3.9
	2023	-1.2	-1.3	1.1	-3.0	1.3	0.2	8.5	3.2	8.2	-0.9	29.0	4.4
	2024	1.2	2.0	1.2	1.8	2.8	2.6	1.3	2.7	8.1	-0.4	29.0	4.5
Norway	2022	3.7	6.6	0.3	4.0	3.0	12.1	5.8	3.9	1.8	-	-	-
	2023	0.6	-0.5	1.3	0.5	3.5	2.5	4.8	4.3	2.2	-	-	-
	2024	1.5	0.9	1.5	4.0	2.0	2.0	2.1	3.8	2.4	-	-	-

Macro forecast. Euroland

	Year	GDP [1]	Private cons.[1]	Public cons.[1]	Fixed inv.[1]	Ex-ports[1]	Im-ports[1]	Infla-tion[1]	Wage growth[1]	Unem-ploym[3]	Public budget[4]	Public debt[4]	Current acc.[4]
Euro area	2022	3.3	3.9	1.1	4.4	7.4	8.6	8.4	4.2	6.7	-3.9	93.7	1.5
	2023	-0.9	-1.6	1.3	0.7	2.9	4.5	6.7	4.9	7.4	-4.0	92.5	1.9
	2024	0.0	0.7	1.7	-0.1	1.3	2.7	2.9	3.6	8.3	-3.5	91.6	2.4
Germany	2022	1.8	4.6	1.6	0.4	3.2	6.7	8.6	4.1	3.0	-2.3	67.4	3.7
	2023	-1.4	-2.1	1.9	-1.2	2.4	3.7	7.9	5.4	3.8	-2.7	65.5	4.6
	2024	-0.5	0.9	2.3	0.2	-0.1	3.0	3.9	4.3	4.2	-1.9	66.2	4.9
Finland	2022	1.8	2.3	2.5	4.5	1.5	7.0	7.1	2.6	6.8	-1.8	70.7	-3.3
	2023	-0.7	-0.3	1.5	-1.0	-1.5	-2.0	4.8	4.0	7.3	-2.5	71.0	-2.7
	2024	0.5	0.4	1.0	0.5	1.5	1.0	2.2	3.5	7.2	-2.0	71.7	-2.1

Macro forecast. Global

	Year	GDP [1]	Private cons.[1]	Public cons.[1]	Fixed inv.[1]	Ex-ports[1]	Im-ports[1]	Infla-tion[1]	Wage growth[1]	Unem-ploym[3]	Public budget[4]	Public debt[4]	Current acc.[4]
USA	2022	1.9	2.6	-0.9	-0.4	7.9	8.5	8.0	5.2	3.6	-4.2	124.0	-3.9
	2023	-0.2	-0.2	1.1	-5.4	1.1	-4.4	3.1	4.4	4.0	-3.8	121.0	-3.1
	2024	0.5	0.4	1.3	0.6	-0.1	0.5	1.7	2.1	5.6	-3.9	120.5	-2.8
China	2022	2.8	2.8	-	4.5	-	-	2.0	3.0	-	-8.9	76.9	1.6
	2023	4.6	5.1	-	5.2	-	-	2.2	5.0	-	-7.2	84.1	1.0
	2024	6.0	5.5	-	5.5	-	-	2.5	5.5	-	-7.5	89.8	0.8
UK	2022	4.2	-	-	-	-	-	8.9	-	3.8	-	-	-
	2023	-0.7	-	-	-	-	-	6.2	-	4.4	-	-	-
	2024	0.8	-	-	-	-	-	2.6	-	5.0	-	-	-
Japan	2022	1.4	3.0	1.6	-0.8	4.7	8.0	2.2	-	2.6	-	-	-
	2023	0.7	0.9	0.6	1.3	2.5	3.2	2.4	-	2.8	-	-	-
	2024	0.9	0.8	0.5	0.6	1.5	0.5	1.4	-	2.8	-	-	-

Source: OECD and Danske Bank. 1) % y/y. 2) % contribution to GDP growth. 3) % of labour force. 4) % of GDP.

Financial forecast

Bond and money markets

		Key interest rate	3m interest rate	2-yr swap yield	10-yr swap yield	Currency vs EUR	Currency vs USD	Currency vs DKK	Currency vs NOK	Currency vs SEK
USD	13-Jan	4.50	4.82	4.42	3.44	108.3	-	686.8	987.7	1038.7
	+3m	5.25	5.40	5.20	4.05	102.0	-	729.4	1019.6	1078.4
	+6m	5.25	5.40	5.10	4.05	98.0	-	759.7	1040.8	1142.9
	+12m	5.25	5.24	4.80	3.65	98.0	-	760.2	1020.4	1122.4
EUR	13-Jan	2.00	2.33	3.13	2.68	-	108.3	743.9	1069.8	1125.0
	+3m	3.00	3.36	3.35	3.00	-	102.0	744.0	1040.0	1100.0
	+6m	3.25	3.41	3.20	2.85	-	98.0	744.5	1020.0	1120.0
	+12m	3.25	3.39	2.90	2.55	-	98.0	745.0	1000.0	1100.0
JPY	13-Jan	-0.10	-0.03	0.32	1.05	120.5	128.4	6.17	8.88	9.34
	+3m	-0.10	-	-	-	141.8	139.0	5.25	7.34	7.76
	+6m	-0.10	-	-	-	132.3	135.0	5.63	7.71	8.47
	+12m	-0.10	-	-	-	125.4	128.0	5.94	7.97	8.77
GBP*	13-Jan	3.50	-	4.07	3.34	88.7	122.2	839.1	1206.6	1268.9
	+3m	3.75		4.20	3.50	86.0	118.6	865.1	1209.3	1279.1
	+6m	3.75		4.20	3.50	85.0	115.3	875.9	1200.0	1317.6
	+12m	3.75		4.00	3.30	85.0	115.3	876.5	1176.5	1294.1
CHF*	13-Jan	1.00	-	1.30	1.53	100.4	92.8	740.6	1065.1	1120.1
	+3m	1.50	-	-	-	97.0	95.1	767.0	1072.2	1134.0
	+6m	1.50	-	-	-	96.0	98.0	775.5	1062.5	1166.7
	+12m	1.50	-	-	-	96.0	98.0	776.0	1041.7	1145.8
DKK	13-Jan	1.75	2.59	3.27	2.82	743.91	686.84	-	143.81	151.23
	+3m	2.65	3.45	3.50	3.15	744.00	729.41	-	139.78	147.85
	+6m	2.90	3.50	3.35	3.00	744.50	759.69	-	137.00	150.44
	+12m	2.90	3.50	3.05	2.70	745.00	760.20	-	134.23	147.65
SEK	13-Jan	2.50	2.81	3.18	2.63	1125.0	1038.7	66.1	95.1	100.0
	+3m	3.00	3.05	3.35	2.95	1100.0	1078.4	67.6	94.5	-
	+6m	3.00	3.10	3.15	2.85	1120.0	1142.9	66.5	91.1	-
	+12m	3.00	3.10	2.85	2.55	1100.0	1122.4	67.7	90.9	-
NOK	13-Jan	2.75	3.29	3.44	2.99	1069.8	987.7	69.5	100.0	105.2
	+3m	2.75	2.95	3.45	3.15	1040.0	1019.6	71.5	-	105.8
	+6m	2.75	2.95	3.20	2.80	1020.0	1040.8	73.0	-	109.8
	+12m	2.50	2.95	3.05	2.70	1000.0	1020.4	74.5	-	110.0

*Notes: GBP swaps are SONIA and CHF swaps are SHARON.
We have updated our Norges Bank forecasts after yesterday's Norges Bank meeting but not yet our Norwegian yield outlook

Commodities

		2022				2023				Average	
	13-Jan	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2022	2023
ICE Brent	85	98	112	105	100	95	95	95	95	104	95

Source Danske Bank

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