17 March 2023

Weekly Focus

ECB holds the course through stormy waters

After a long period of unusually low interest rates, some may have been concerned that when central banks hike interest rates rapidly, eventually something could break. Events unfolding in the past seven days have served as a sharp reminder that there may be a trade-off between central banks' fight against inflation and financial stability. Referring to ECB President Lagarde's press conference this week, they disagree though.

The ECB hiked interest rates by 50bps and repeated their commitment to hike more. As long as the baseline persists i.e. inflation remains sticky and a systemic crisis is avoided, the ECB has '*a lot more room to cover'*. The ECB sees no contradiction in sustaining price and financial stability at the same time, which we consider a signal that the threshold not to hike is high. If necessary, new 'creative' measures can be introduced to address liquidity issues. We keep our call for a 50bp hike in May and a peak policy rate reached in July of 4%, see *Flash ECB Review: 50bp hike but no guidance for May*, 16 March.

Last weekend, the US authorities took control over two banks that had ended in an acute liquidity crisis. The response was stark: All deposits in the two banks would be covered and the Fed set up a new term-funding program where banks could access liquidity against high-quality collateral, valued at par. It is unusual for a central bank not to protect itself from credit losses by imposing haircuts on collateral, and by all measures, the response can be considered impactful. Yet, on Thursday, concerns focused on another US bank, First Republic, until it received a USD 30bn deposit from larger lenders. Fears are also reflected in the swelling of Fed's new lending facility, in a flow of deposits from medium-sized to large US banks and in investors' flight to money market funds.

Worries regarding banking sector health quickly crossed the Atlantic. In Europe, the SNB was forced to step in and provide a liquidity loan to its second largest bank Credit Suisse on Wednesday evening after the share price had plummeted and the CDS market was pricing in a rising risk of default. By Thursday, the share price had started to recover but the CDS was still trading at distressed levels. Some systemic risk indicators have also risen. For example, expected volatility has increased in the stock market and even more in the bond market. Money market risk premia has increased slightly but remains far from the very distressed levels seen during the global financial crisis.

Despite financial stability concerns, inflation woes persist. In the US, February CPI came in close to our expectations but core surprised to the upside. We keep our call for a 25bp hike by the Fed next week (*Global Inflation Watch - Central banks balance inflation and financial stability risks*, 15 March). Also, February CPI in Sweden came in higher than expected, and as a result, we changed our Riksbank call and now expect a peak rate at 4.25% (prev. 3.75%) *Flash Comment: Riksbank to hike 75bp + 50bp from here*, 15 March.

Apart from the obvious market focus on Fed next week, flash PMIs from Europe and the US are likely to attract interest. We pay close attention to whether confidence has been shaken by the recent developments (data has been collected mid-month). We will also follow closely Lagarde's speech on Tuesday for any change in tone. We expect the Bank of England to deliver their final hike next Thursday, bringing the bank rate to 4.25%.

Key global views

- Stagnation and periodic contraction in the US and in Europe in 2023.
- US and euro area headline inflation set to decline further but core inflation likely to stay elevated.
- Rising emphasis on financial stability risks but more rate hikes in store as long as a systemic crisis can be avoided.

Key market movers

- Tuesday: ZEW index
- Wednesday: FOMC meeting
- Thursday. Norges bank meeting, BOE meeting, CBRT meeting
- Friday: Euro area and US PMIs

Selected reading from Danske Bank

- *Flash ECB review – 50bp hike but no guidance for May*, 16 March
- *Research Global: Deglobalisation – is it really happening*, 13 March

Editor

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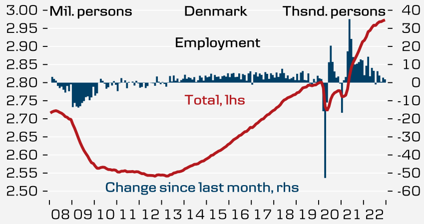
Scandi market movers

- In **Denmark**, we are due to receive January's wage-earner employment figures on Tuesday. Employment rose by 1,800 in December (seasonally adjusted), but we expect employment to decline a little here in 2023 due to higher interest rates and eroded purchasing power hitting consumer demand and given that investment in housing, etc. is likely to fall. Nevertheless, the downturn looks set to be mild and there is still a plentiful supply of vacancies for at least a large share of those who lose their positions in companies that get hit. The question then is whether the slowdown will be too mild to get inflation fully under control in this part of the world. If so, a further downturn could be on the cards for 2024.

  Consumer confidence figures for March are due on Thursday. February saw consumer confidence rise to -25.1 after consistently climbing from its low of -37 in October. However, the figures are far from good overall, and Danes still rate the current state of the economy as extremely poor. Consumer confidence figures continuing to move in the right direction despite everything should probably be seen against the fall in energy prices over the winter and the fact that inflation is generally no longer rising. Price growth calming further would also help reduce worries about household finances, while solid growth figures from the end of last year and a just modest deterioration in the labour market could also contribute to a more upbeat view on the Danish economy.

Employment growth slowing

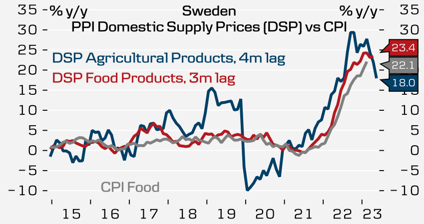


Source: Statistics Denmark, Danske Bank, Macrobond

- Riksbank will remain the center of attention in the coming week. Deputy Governor Breman speaks about monetary policy in the context of financial stability on Tuesday 21st. Hence, she is likely say something about Riksbank priorities when it comes to inflation vs banking worries. Unless there in coming days is mounting evidence that Swedish banks are affected, she is likely to downplay it. Governor Thedéen speaks about technology and climate change the day after, hardly a market mover on the surface but who knows.

  PPI data is usually not in market focus. However, given the heightened attention given to high and soaring food prices in Sweden, it might be interesting to look at the leading food price information that is in PPI domestic supply prices (DSP are weighted the same way as CPI i.e. it is a mix of home market and import prices). The withstanding chart illustrates recent inflation prints for DSP series that are correlated to CPI foods prices. There are already signs that the food inflation peak is within reach.

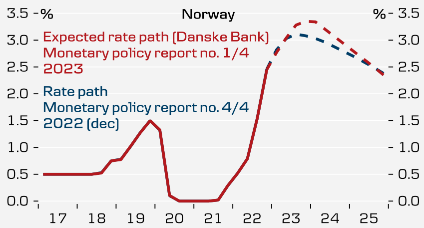
Sweden: A glimpse of hope for food price outlook



Source: SCB

  In **Norway**, we expect Norges Bank to raise its policy rate by 25bp to 3.00% at Thursday's meeting as it has been signalling. We also expect the bank to signal a further increase, probably in June. This will be reflected in the policy rate path in the new monetary policy report, which will probably also show a possibility of a third hike in late summer/autumn. This upward revision of the bank's policy rate expectations since the December report is expected mainly as a result of more aggressive rate expectations in other countries coupled with a clear fall in the NOK. Economic growth also seems to be holding up better than expected, and wage and price inflation will be slightly higher than the bank previously anticipated. Wage and price expectations still seem to be reasonably well anchored, and this year's pay deals look likely to end up around 5%. All of this suggests that Norges Bank can stick to its strategy of raising the policy rate gradually so that it has time to gauge the effects of higher interest rates on growth and inflation. The reaction in global financial markets to the failure of Silicon Valley Bank has clearly introduced a downside risk to future interest rates, but for now we expect Norges Bank to treat it exactly as that, a risk factor.

Policy rate path to be revised up



Source: Macrobond, Danske Bank

Scandi update

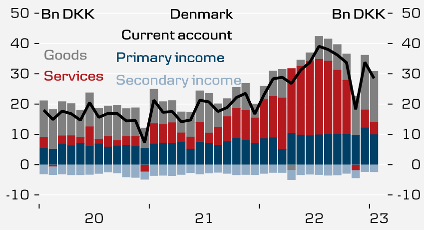
Denmark – Danish central bank hikes rates by half a point

Danmarks Nationalbank has raised its benchmark interest rates by half a percentage point, taking the certificates of deposit rate to 2.6%. The move comes on the heels of the European Central Bank (ECB) also hiking rates by 0.5 percentage points. Interest rates in Denmark have now been increased by 3.2 percentage points over nine months, one of the biggest ever shifts over such a short timeframe and clearly a development that impacts the economy, though the increase in the eurozone has been even greater at 3.5 percentage points. Danmarks Nationalbank has increased the rate spread on several occasions to avoid the robust Danish economy strengthening the Danish krone (DKK) unduly. Mortgage bond markets had essentially already priced in the decisions, so market yields should not change much for now. The dramatic increase in mortgage rates over the past year is clearly mostly due to the rate hikes by the ECB and Danmarks Nationalbank, and these latest decisions are yet another step in that direction.

Denmark's overall current account surplus fell from DKK33.9bn in December 2022 to DKK28.5bn in January 2023, though the surplus for 2022 as a whole was revised up by DKK9.4bn. January's surplus computes to around 12% of GDP, even though it is no longer being pushed up by high shipping rates. We must again conclude that Danish companies, or at least a group of them, are doing extremely well. At the same time, major investments abroad made over the years by pension funds in particular are providing a substantial, regular income for Denmark.

February this year saw 3,381 house and 1,224 apartment sales, a month-on-month increase of 22% for house sales and 27% for apartment sales. However, as February is normally characterised by a jump in home sales, a better comparison is with the same month in previous years. This reveals 2023 to have the lowest house sales in February since 2016, while for apartments it is the lowest number since 2014. Hence, we must conclude that the number of home sales remains low. We see mainly two factors driving the lower level of activity. First, rising interest rates in 2022 have made financing a home purchase much more expensive and, second, soaring sales during the pandemic mean many have recently bought a new home and so are not considering a purchase anytime soon.

Denmark's current account surplus in retreat but still impressive

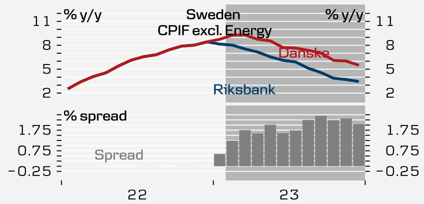


Source: Danske Bank, Statistics Denmark, Macrobond Financial

Sweden – We have changed our Riksbank call to 75bp in April and 50bp in June. Resulting in a peak policy rate of 4.25%

February core inflation rose much more than expected and the 9.3 % yoy outcome was 1.3 percentage points higher than Riksbank's most recent forecast. This was a very bad outcome, both because of the high print and because many components surprised on the upside i.e. inflation continues to be broad-based. Not only food but also clothing, furniture, hotel/restaurant and recreation rose more than expected. Over the past couple of months core inflation has continued to accelerate. Therefore, we have raised our forecast expecting core inflation to remain at 9.3 % yoy in March. Such an outcome would be 1.8 percentage points higher than Riksbank's forecast.

Our underlying inflation forecast vs Riksbank



Source: Danske Bank, Riksbank, Macrobond

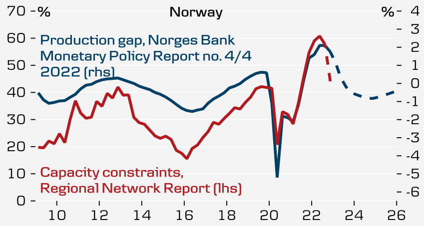
The Riksbank will therefore be forced to deviate from their most recent rate path forecast (indicating 25bp or 50bp hike in April) and deliver a 75bp hike. Especially after Board members already yesterday during the parliamentary hearing delivered a hawkish message, emphasizing the willingness to act accordingly on the back of incoming data. We also lift our June call from 25bp to 50bp as our inflation forecast does not indicate that the Riksbank will have enough positive data to lower the pace to 25bp increments. Hence, we have lifted our estimate for the peak policy rate from 3.75 to 4.25%.

We expect mainly consumers and the housing market to come under intense pressure from soaring interest rates, noting that this applies to many businesses too. Consequently, we will reduce our 2023 forecasts for private consumption and residential property prices. For the latter we now see a 25 % decline from top to bottom vs previously 20 %. Needless to say, the tightening of monetary policy raises the risk for a deeper recession for the economy as a whole.

Norway – Activity levelling off, cost pressures persist

The latest round of Norges Bank's regional network survey shows activity levelling off in the current quarter, while expectations for growth in the coming quarter are appreciably stronger than in December. Only 41% of firms reported operating at full capacity, down from 44% in December, and the share of firms reporting labour shortages as a constraint on production dropped from 35% to 28%. This suggests that the combination of weaker global growth, stronger inflation and higher interest rates is eroding demand, and that the output gap is closing. The expected slowdown is relatively broad-based, with the exception of oil-related industries and the service sector, which now anticipates a moderate acceleration. Wage growth is now expected to be 4.6% this year, just below the 4.7% Norges Bank projected in its December monetary policy report, and then slow to 3.9% next year. Firms anticipate a moderate rise in employment, but a clear upswing in investment next year. Profitability is now expected to improve moderately, but there are big variations between sectors, and firms expect further strong cost inflation.

Pressures easing



Source: Macrobond, Danske Bank

Calendar

Monday, March 20, 2023				Period	Danske Bank	Consensus	Previous
11:00	EUR	Trade balance	EUR bn	Jan			-18.1
Tuesday, March 21, 2023				Period	Danske Bank	Consensus	Previous
11:00	DEM	ZEW current situation	Index	Mar		-48.0	-45.1
11:00	DEM	ZEW expectations	Index	Mar		20.0	28.1
13:30	CAD	CPI	m/m|y/y	Feb			...|5.9%
15:00	USD	Existing home sales	m (m/m)	Feb		4.15	4.00|-0.7%
Wednesday, March 22, 2023				Period	Danske Bank	Consensus	Previous
8:00	GBP	CPI	m/m|y/y	Feb		0.6%|9.8%	-0.6%|10.1%
8:00	GBP	CPI core	y/y	Feb		5.7%	5.8%
10:00	EUR	Current account	EUR bn	Jan			15.9
15:30	USD	DOE U.S. crude oil inventories	K				1550
19:00	USD	FOMC meeting	%		5.0%	5.0%	4.8%
Thursday, March 23, 2023				Period	Danske Bank	Consensus	Previous
8:00	DKK	Consumer confidence	Net. bal.	Mar	-23		-25.1
9:30	CHF	SNB policy rate	%		1.5%	1.5%	1.0%
10:00	NOK	Norges Banks monetary policy meeting	%		3.0%	3.0%	2.8%
12:00	TRY	Central Bank of Turkey rate decision	%			8.5%	8.5%
13:00	GBP	BoE minutes					
13:00	GBP	BoE Bank rate	%		4.25%	4.25%	4.0%
13:30	USD	Current account	USD bn	4th quarter		-213.2	-217.1
13:30	USD	Initial jobless claims	1000				192
15:00	USD	New home sales	1000 (m/m)	Feb		650	670.0 (7.2%)
16:00	EUR	Consumer confidence, preliminary	Net bal.	Mar		-18.5	-19.0
Friday, March 24, 2023				Period	Danske Bank	Consensus	Previous
-	EUR	S&P may publish Germany's debt rating					
0:30	JPY	CPI - national ex. fresh food	y/y	Feb		3.1%	4.2%
0:30	JPY	CPI - national	y/y	Feb		3.3%	4.3%
1:01	GBP	GfK consumer confidence	Index	Mar		-35.0	-38.0
1:30	JPY	Nikkei Manufacturing PMI, preliminary	Index	Mar			47.7
1:30	JPY	Markit PMI services, preliminary	Index	Mar			54.0
8:00	SEK	PPI	m/m|y/y	Feb			-5.2%|11.8%
8:00	NOK	Credit indicator (C2)	y/y	Feb			5.3%
8:00	GBP	Retail sales ex fuels	m/m|y/y	Feb		0.2%|-4.9%	0.4%|-5.3%
9:00	ESP	GDP, final	q/q|y/y	4th quarter		0.2%|2.7%	0.2%|2.7%
9:15	FRF	PMI manufacturing, preliminary	Index	Mar		48.0	47.4
9:15	FRF	PMI services, preliminary	Index	Mar		52.0	53.1
9:30	DEM	PMI manufacturing, preliminary	Index	Mar		47.0	46.3
9:30	DEM	PMI services, preliminary	Index	Mar		51.1	50.9
10:00	EUR	PMI manufacturing, preliminary	Index	Mar		48.9	48.5
10:00	EUR	PMI composite, preliminary	Index	Mar		51.8	52.0
10:00	EUR	PMI services, preliminary	Index	Mar		52.5	52.7
10:30	GBP	PMI manufacturing, preliminary	Index	Mar		50.0	49.3
10:30	GBP	PMI services, preliminary	Index	Mar		53.0	53.5
13:30	CAD	Retail sales	m/m	Jan			0.5%
13:30	USD	Core capital goods orders, preliminary	%	Feb			0.8%
14:45	USD	Markit PMI manufacturing, preliminary	Index	Mar		47.3	47.3
14:45	USD	Markit PMI service, preliminary	Index	Mar		50.3	50.6

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	3.6	-2.6	-2.8	8.4	7.9	3.8	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	4.3	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	3.8	6.8	0.1	4.4	5.9	9.3	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	3.5	4.3	1.1	3.8	7.2	8.0	8.4	4.2	6.7	-3.9	93.7	1.5
	2023	0.1	-0.3	0.8	1.7	3.5	5.2	6.1	4.9	6.9	-4.0	92.5	1.9
	2024	0.3	0.9	1.0	0.0	3.6	4.6	2.6	3.6	7.0	-3.5	91.6	2.4
Germany	2022	1.9	4.4	1.2	0.6	3.0	6.1	8.7	4.1	3.1	-2.3	67.4	3.7
	2023	-0.4	-0.6	0.9	-0.7	3.3	4.4	6.6	5.4	3.3	-2.7	65.5	4.6
	2024	0.1	0.8	1.2	0.0	3.2	4.6	2.6	4.3	3.5	-1.9	66.2	4.9
Finland	2022	2.1	2.1	2.9	5.0	1.7	7.5	7.1	2.6	6.8	-1.8	73.0	-3.9
	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	2.1	2.8	-0.6	-0.2	7.2	8.2	8.0	5.2	3.6	-4.2	124.0	-3.9
	2023	0.3	0.3	1.5	-5.2	1.0	-5.7	4.2	4.0	4.0	-3.8	121.0	-3.1
	2024	0.9	0.8	1.3	1.5	1.2	1.7	1.7	2.1	5.6	-3.9	120.5	-2.8
China	2022	3	2.8	-	4.5	-	-	2.0	3.0	-	-8.9	76.9	1.6
	2023	5.5	5.1	-	5.2	-	-	2.2	5.0	-	-7.2	84.1	1.0
	2024	5.2	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	17-Mar	4.75	4.91	4.44	3.60	106.6	-	698.6	1069.7	1045.7
	+3m	5.25	5.40	5.10	3.85	104.0	-	715.6	1019.2	1057.7
	+6m	5.25	5.40	4.90	3.65	102.0	-	729.9	1019.6	1098.0
	+12m	5.25	5.00	4.70	3.45	102.0	-	730.4	1000.0	1098.0
EUR	17-Mar	3.00	2.65	3.38	2.96	-	106.6	744.7	1140.4	1114.8
	+3m	3.75	4.08	3.45	3.25	-	104.0	744.3	1060.0	1100.0
	+6m	4.00	4.16	3.20	3.10	-	102.0	744.5	1040.0	1120.0
	+12m	4.00	4.13	3.00	2.90	-	102.0	745.0	1020.0	1120.0
JPY	17-Mar	-0.10	-0.03	-	-	120.5	133.0	6.18	9.46	9.25
	+3m	-0.10	-	-	-	130.0	125.0	5.73	8.15	8.46
	+6m	-0.10	-	-	-	127.5	125.0	5.84	8.16	8.78
	+12m	-0.10	-	-	-	127.5	125.0	5.84	8.00	8.78
GBP*	17-Mar	4.00	-	4.16	3.44	87.7	121.6	849.4	1300.7	1271.5
	+3m	4.25		4.10	3.40	87.0	119.5	855.5	1218.4	1264.4
	+6m	4.25		4.10	3.40	85.0	120.0	875.9	1223.5	1317.6
	+12m	4.00		3.90	3.30	85.0	120.0	876.5	1200.0	1317.6
CHF*	17-Mar	1.00	-	1.51	1.64	98.7	92.6	754.7	1155.6	1129.7
	+3m	1.50	-	-	-	98.0	94.2	759.4	1081.6	1122.4
	+6m	1.50	-	-	-	97.0	95.1	767.5	1072.2	1154.6
	+12m	1.50	-	-	-	97.0	95.1	768.0	1051.5	1154.6
DKK	17-Mar	2.60	2.95	3.49	3.07	744.71	698.55	-	153.13	149.70
	+3m	3.35	3.77	3.60	3.40	744.25	715.63	-	142.43	147.80
	+6m	3.60	3.85	3.35	3.25	744.50	729.90	-	139.69	150.44
	+12m	3.60	3.84	3.15	3.05	745.00	730.39	-	136.91	150.34
SEK	17-Mar	3.00	3.26	3.55	2.86	1114.8	1045.7	66.8	102.3	100.0
	+3m	3.75	4.15	3.65	3.00	1100.0	1057.7	67.7	96.4	-
	+6m	4.25	4.40	3.30	2.80	1120.0	1098.0	66.5	92.9	-
	+12m	4.00	4.00	3.00	2.75	1120.0	1098.0	66.5	91.1	-
NOK	17-Mar	2.75	3.36	3.27	3.00	1140.4	1069.7	65.3	100.0	97.8
	+3m	3.25	3.45	3.45	3.15	1060.0	1019.2	70.2	-	103.8
	+6m	3.25	3.36	3.20	2.85	1040.0	1019.6	71.6	-	107.7
	+12m	3.00	3.20	3.05	2.80	1020.0	1000.0	73.0	-	109.8

*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	
	17-Mar	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2022	2023
ICE Brent	75	98	112	105	100	95	95	95	95	104	95

Source Danske Bank

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