8 October 2017

Scandi Markets Ahead

Inflation week - pick-up in inflation in Norway and Sweden

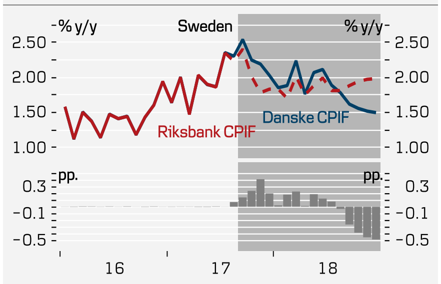
- September inflation is the event of the week in **Sweden**. We expect clothing prices to show a strong but normal rise, giving the biggest contribution to the monthly increase. In addition, Telia's 24% increase in fixed telephony subscriptions is expected to add sizeably as are international airline tickets and to some extent energy. Charter packages remain uncertain, as the new methodology means we are in unchartered waters. No further drop in prices is assumed in our forecast. All in all, September CPIF inflation, hence, is expected to print 2.5% y/y, 0.1 above the Riksbank's forecast.
- Prospera's money market inflation expectations may show some disparity. We would not be surprised to see some downward adjustment to one-year expectations, which should reveal some expectations of base effects. We expect longer horizons to be broadly unchanged.
- We expect EUR/SEK to range-trade for now.
- The main event in **Norway** is Tuesday's inflation numbers for September. Core inflation surprised on the upside over the summer but fell unexpectedly sharply in August on the back of lower food prices. We expect food prices to correct after the drop in August, taking the annual rate of core inflation back up to 1.2% in September. This would be in line with the projections in Norges Bank's latest monetary policy report and so would have a neutral market impact.
- We expect further weakness in the Norwegian housing market.
- In **Denmark**, inflation numbers for September are released on Tuesday. Inflation was surprisingly strong over the summer, due mainly to increases in holiday home rents and package travel prices. We expect the tide to turn in September, however, with inflation down to -0.2% m/m and 1.3% y/y.

See also our *Nordic Outlook*, 5 October 2017.

Financial and macro forecasts for the Nordic area

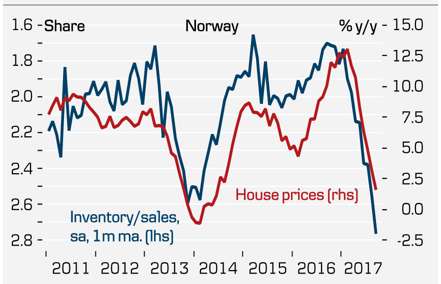
- *See our monthly Yield Outlook that covers Scandi and core markets (September 2017)*
- See *FX Forecast Update* for our latest FX Forecasts (September 2017)
- See *Nordic Outlook* (October 2017) for updated Macro forecasts.

Sweden: Inflation picks-up again



Source: Macrobond Financiel

Norway: further weakness in store for housing market



Source: Macrobond Financial

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Sweden – inflation to come in above Riksbank forecast

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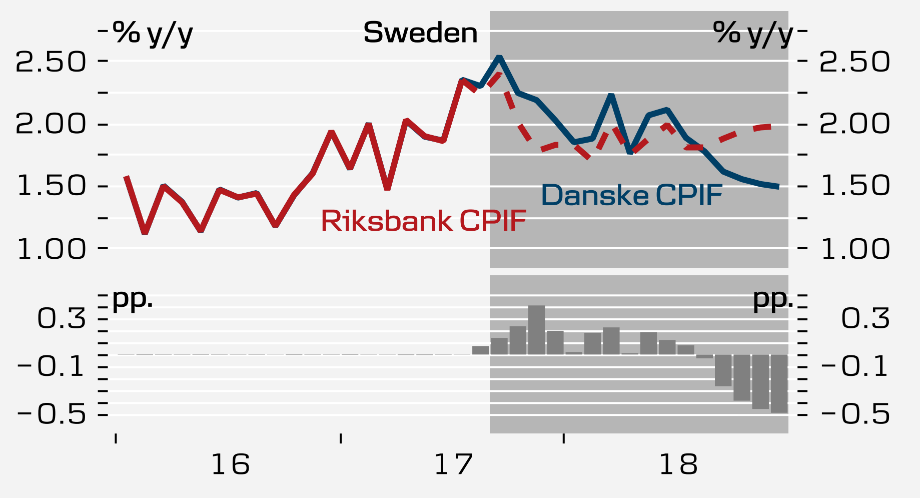
All in all, September CPIF inflation, hence, is expected to print 2.5% y/y, 0.1pp above the Riksbank's forecast.

Prospera's money market inflation expectations may show some disparity. We would not be surprised to see some downward adjustment to one-year expectations, which should reveal some expectations of base effects. We expect longer horizons to be broadly unchanged.

For more details ahead of the inflation release, see *Reading the Markets Sweden,* 4 October 2017.

We expect CPIF to come in just above Riksbank



Source: Riksbank, Macrobond Financial, Danske Bank

EUR/SEK stuck in a range

Note that in *FX research: Inflation could lend support to the SEK*, we underline that "We stick to our tactical view that EUR/SEK is trading in a range of 9.40-9.65 (the downside defined by strong technical support at 9.41). We recommend vol-selling strategies that utilise the fact that implicit volatility still exceeds realised."

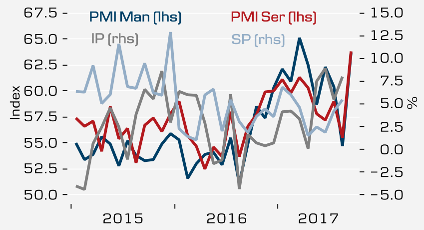
Accelerating business activity

Earlier, we had worries that both manufacturing and services sectors were slowing as evidenced by the decline in PMIs in recent months. This past week, however, September PMI manufacturing and PMI services both rebounded strongly. Manufacturing PMI recorded 63.7, close to the high seen earlier this year. Although we have been quite sceptical about the information content in PMIs, as they have for some time been uncorrelated to hard data, the recent readings are quite in line with industrial production data. The latter showed a growth rate of 7.3% in August. Hence, both these indicators suggest manufacturing is improving markedly right now.

Services show a similar picture. PMI services spiked to 63.8, the highest since December 2010. August service production numbers in addition rose to a healthy 5.2% y/y.

Although it is somewhat premature to draw any strong conclusions, there is a tendency that business activity is growing a little more strongly, in parallel with construction and household spending.

Positive trend in business activity



Source: Konjunkturinstitutet

Norway – small pick-up in inflation expected

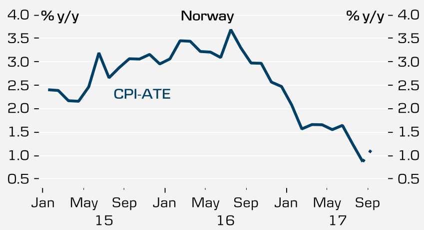
The main event in **Norway** is Tuesday's inflation numbers for September. With 'everyone' now agreed that growth is picking up and that the downside risk is evaporating as oil activity improves, the next step is to gauge when higher capacity utilisation will transmute into higher pressure on wages and prices and, eventually, higher interest rates.

There is currently much uncertainty about the transition from economic growth to inflation. Current inflation numbers can therefore serve as an important crosscheck for whether these driving forces are in the process of reversing.

Core inflation surprised on the upside over the summer but fell unexpectedly sharply in August on the back of lower food prices. It was mainly imported inflation that was lower than expected, while domestic inflation, especially on the service side, appears to have stabilised.

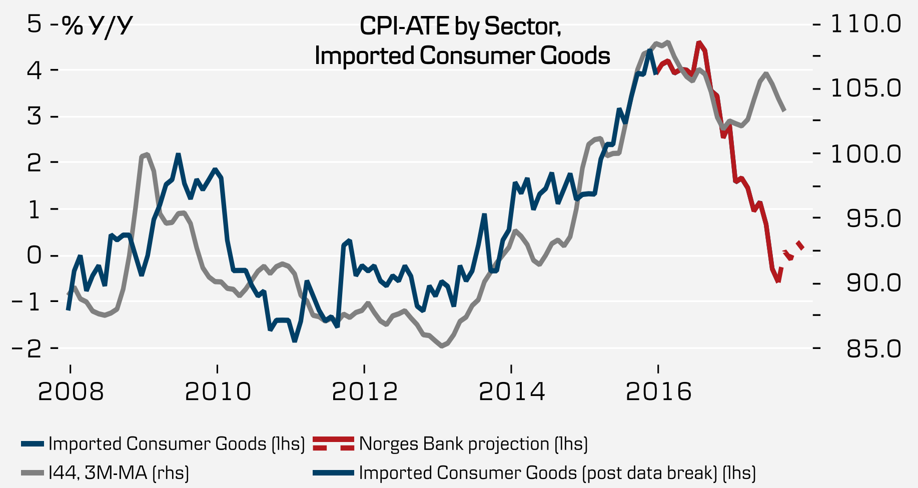
We think this could be a signal that slightly higher wage growth in sheltered industries, combined with strong demand in those industries, is in the process of pushing up inflation. We expect food prices to correct after the drop in August, taking the annual rate of core inflation back up to 1.2% in September. This would be in line with the projections in Norges Bank's latest monetary policy report and so would have a neutral market impact.

Inflation expected to rise again



Source: Macrobond Financial, Danske Bank

Downward pressure on from imported inflation has peaked as NOK weakening now behind us



Source: Macrobond Financial, Danske Bank

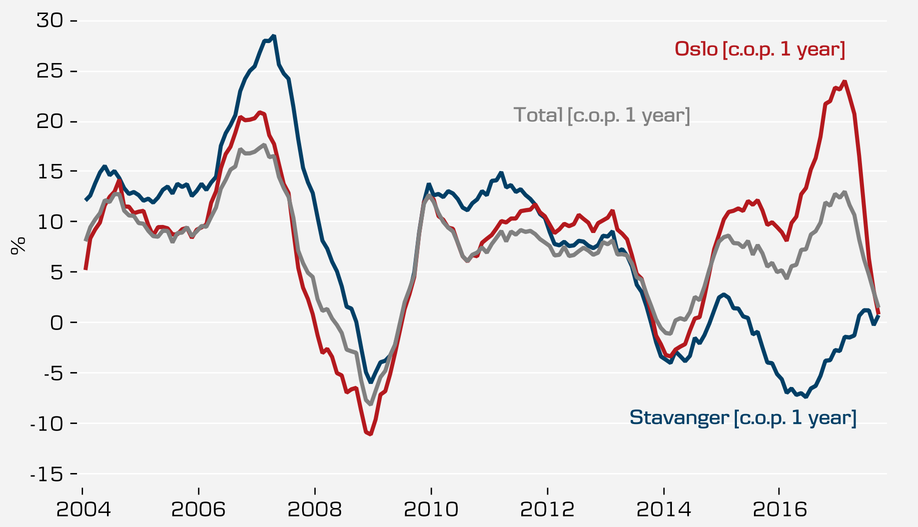
On Thursday, meanwhile, the government is due to unveil its budget for 2018. It is a long time since the budget has been significant news for the market but the growth contribution from fiscal policy will play a greater role in Norges Bank's rate setting as activity normalises. In its latest monetary policy report, the central bank presents an interest rate path based on a fiscal stimulus of just 0.1% of GDP in 2018, or around NOK3bn in constant money. If the budget is more expansionary than this and possibly even more so after the autumn's budget negotiations, this will have a direct impact on the interest rate path for the first time in more than a decade.

Housing prices to fall further as inventory goes up

Housing prices were down for a sixth successive month in September, falling 0.5% from August. The decline is still strongest in the big cities, but also reasonably clear elsewhere in the country. At the same time, turnover is holding up well, including in Oslo. This tells us that the drop in prices is mainly a matter of supply, with strong growth in homebuilding in recent years having dramatically increased the overall housing stock. Slightly lower population growth and the new mortgage regulations have also put a damper on demand growth. Although turnover is holding up, the greater number of properties on the market means that the stock-to-sales ratio is continuing to climb. As can be seen from the chart, this is a clear sign that prices are set to fall further.

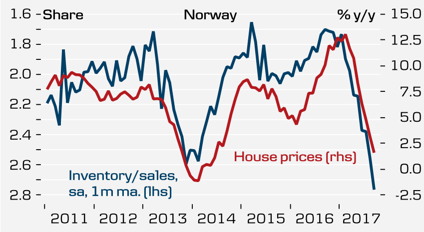
There was one slight ray of light, with the number of homes for sale in Oslo seeming to slow up a little, which could be a first sign of the market stabilising.

Divergent development in the housing markets



Source: Macrobond Financial, Danske Bank

Supply surplus continues to grow



Source: Macrobond Financial, Danske Bank

Denmark – inflation to drop

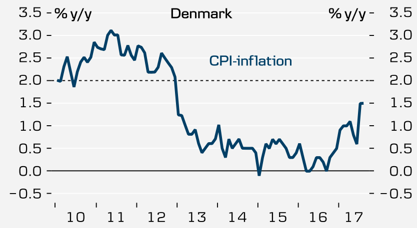
In **Denmark**, inflation numbers for September are released on Tuesday. Inflation was surprisingly strong over the summer, due mainly to increases in holiday home rents and package travel prices. We expect the tide to turn in September, however, with inflation down to -0.2% m/m and 1.3% y/y.

Foreign trade and balance of payments data for August are due out on Monday. The current account surplus shrank slightly to DKK14.6bn in July, due mainly to a drop in exports of goods, so it will be interesting to see whether exports, which have looked a bit weak so far this year, picked up in August.

Statistics Denmark releases unemployment figures for August on Thursday.

Finally, Tuesday brings the autumn report of the Danish Economic Councils with a special focus on long-term welfare dependency and on industrial restructuring and the growth outlook.

Inflation expected to fall after a surprisingly strong summer

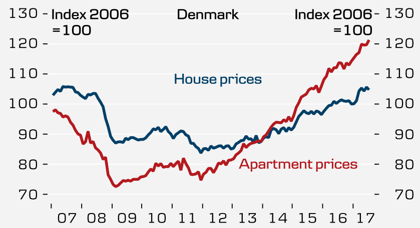


Source: Statistics Denmark

Further housing market improvement ahead

The past week has brought a variety of housing market news. House prices fell 0.9% in July, while apartment prices climbed 1.3%. Housing prices do have a tendency to fluctuate from month to month, so we should not read too much into a single set of data. We still expect there to be further improvements in the housing market, given that fundamentals such as unemployment and interest rates are still favourable. This was underlined by the number of repossessions in September, which remained well below the levels of the financial crisis despite a slight increase m/m. Nor do interest rates look like rising for now. The Nationalbank certainly saw no need to intervene in the currency market in September to defend the krone, and so had no need to touch interest rates either. The week also brought figures for bankruptcies, which increased by 21 m/m to 219 in September but remain low, continuing the recent trend.

Housing prices have trended up ever since late 2011



Source: Statistics Denmark

Disclosure

This research report has been prepared by Danske Bank A/S ('Danske Bank'). The author of this research report is Arne Lohmann Rasmussen, Chief Analyst.

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