FX FOCUS

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Norwegian krone

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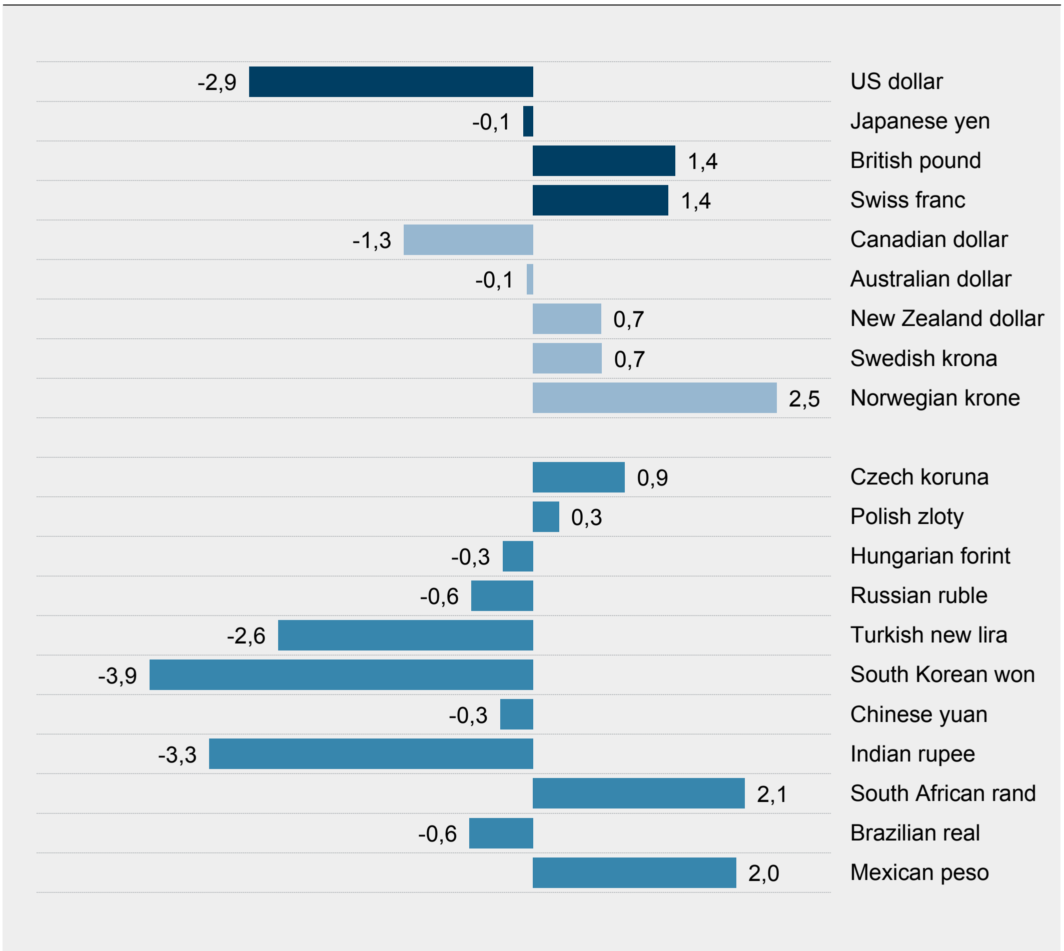
- The US dollar proved the big loser in the currency market most recently. However, a few emerging market currencies were similarly weak. The strongest currency was the Norwegian krone.
- Most recently the Norwegian krone partly made up for the pronounced depreciation from the previous year. A higher oil price and rising yields supported the currency. Since the Norwegian central bank will not carry out its interest rate hikes quite as reticently as the ECB, the interest rate advantage will presumably expand further. Valuation factors also point to a stronger krone, which means that the euro-krone exchange rate should decline markedly over the course of the year.
- Helaba Currency Forecasts

Performance on a month-over-month basis

% vs. euro compared to the previous month (from 01/02 to 01/31/18)



Sources: Bloomberg, Helaba Research

NOK: appreciation potential

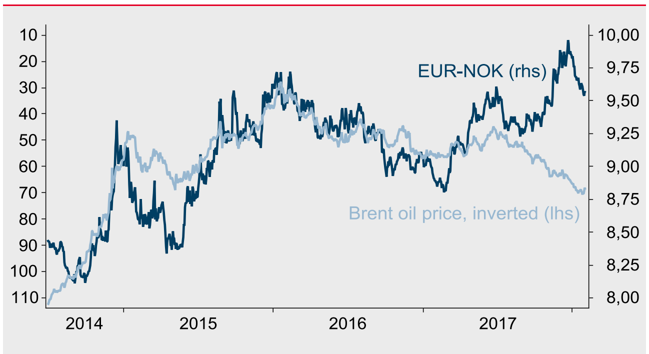
New year, new luck? At the least, the Norwegian krone had a successful start to the new year, since it posted the biggest gain among the leading currencies – even against the super strong euro. What seems at the moment like an unstoppable rise in the euro-dollar exchange rate is grounded less in the euro strength and more in the general dollar weakness. However, the Norwegian krone appreciated in similar fashion in January 2017, though in the end it was clearly among the losers with a minus of nearly 8 % against the euro.

In the pull of the oil price

What explains the good performance of the krone, apart from a growing yield advantage, is the rise in the oil price, the country's most important export commodity. However, that development occurred at times in 2017 without providing the expected, positive impulse to the currency. In principle, the oil price and the Norwegian krone are strongly linked. Thus, the currency came under strong pressure by the slump in the oil price between the middle of 2014 and the beginning of 2016. Lower energy prices led to a contraction not only of export revenues and thus of the current account surplus, but also of investments in the oil and gas sector. However, the energy sector stabilized because of the recovery in oil prices, which is supporting the overall economy. The labour market has overcome its phase of weakness, and the unemployment rate is declining. Moreover, Norway is benefitting from the more robust economy in the euro zone. After expanding by around 2 % last year, Norway's GDP should grow even a little more strongly in 2018 – also beyond the oil-dependent offshore sector. On balance, the higher oil prices suggest a stronger krone.

Higher oil price argues in favor of a stronger krone

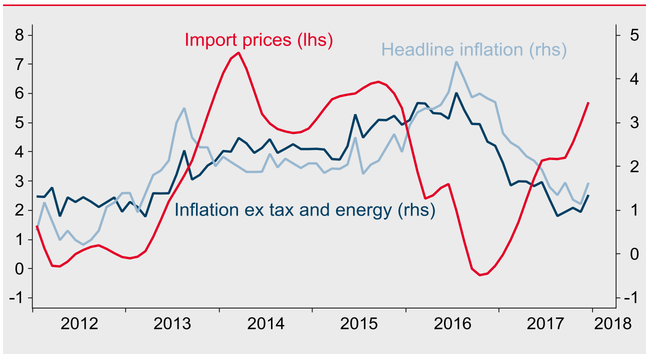
USD/barrel, inverted NOK



Sources: Macrobond, Helaba Research

Inflation with upside risks

% yoy % yoy



Sources: Macrobond, Helaba Research

Interest rate turnaround by Norges Bank still in 2018

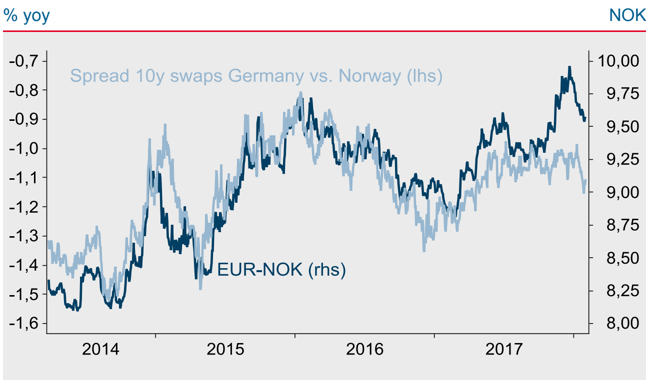
Over the course of 2017, inflation in Norway declined from just under 3 % to 1 %. Moreover, the previously strongly overheated housing market cooled off markedly. As a result, the pressure on the central bank to initiate a change of course on monetary policy eased. Accordingly, Norway's yield advantage against the euro shrank at times, something that explains the depreciation of the krone in part. Now inflation seems to have come off its bottom. The improved economy, higher import prices, and the rise in energy prices argue for a rising inflation. As a result, Norway's central bank should carry out a turnaround in interest rates still this year, something that is already hinted at in its projections. The Norges Bank is likely to still hold off in the coming months, though it will probably begin its interest rate hikes in the second half of the year.

Most recently, bond yields have risen nearly all around the world. In fact, in Norway the interest rates moved up even more than they did for Bunds, with the result that the yield advantage expanded. Experience teaches us that the Norwegian krone – outside of euro debt crises – benefits from rising bond yields. Not least because Norwegian interest rate then move up more robustly. Even if the central bank will surely pay attention to the ECB and the exchange rate, there is reason to believe that its cycle of interest rate hikes will proceed more quickly – or better: not quite as slowly – as that of the ECB. A rising interest rate advantage makes the Norwegian krone accordingly more attractive.

Fundamental tail wind for the krone

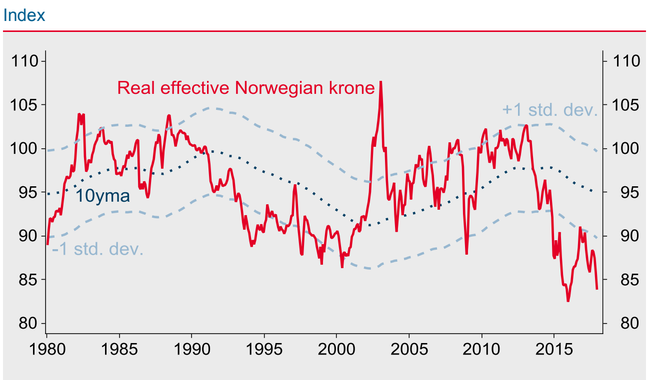
As it is, the current yield advantage – much like the oil price – already argues for a stronger krone. Likewise, long-term valuation indicators support the Norwegian currency. Thus, in December the real, trade-weighted index of the krone stood at its lowest value in the last forty years. In the face of the easing of the European sovereign debt crisis, other factors have receded into the background. In this regard the Norwegian government can shine. Thanks to the pension fund (filled with oil earnings) valued at around 870 billion euro, the country has a gigantic net wealth instead of debts. Should the nervousness increase noticeably in the financial markets, this should hardly weigh on the krone over the medium term, especially since Norway is running a smaller, but still significant current account surplus.

Norway's yield advantage growing again



Sources: Macrobond, Helaba Research

Norwegian krone very favourably valued



Sources: Macrobond, Helaba Research

Attractive risk-reward ratio

Several factors signal a noticeably lower euro-krone exchange rate. However, that was at times also true last year, without the Norwegian currency moving up in a sustained way. To be sure, a robust correction in the oil price or another postponement in Norway's turnaround on interest rates cannot be ruled out. However, in such an environment the euro will presumably weaken, too. A slump in real estate prices in Norway is considered a risk factor. However, the most recent data points instead to a stabilization of prices. With that, the opportunities for the Norwegian currency are higher overall than the risks. The euro-krone exchange rate should fall over the course of the year from most recently just under 9.6 to below 9.0.

Helaba Currency Forecasts

	Performance year to date	1 month	current*	Forecast horizon at end ... Q1/2018	Q2/2018	Q3/2018	Q4/2018
vs. Euro	(vs. Euro, %)						
US dollar	-3,3	-2,9	1,24	1,10	1,15	1,15	1,20
Japanese yen	-0,2	-0,1	136	127	125	125	128
British pound	1,5	1,4	0,87	0,85	0,90	0,90	0,85
Swiss franc	1,2	1,4	1,16	1,12	1,15	1,17	1,15
Canadian dollar	-1,3	-1,3	1,53	1,44	1,50	1,47	1,51
Australian dollar	-0,2	-0,1	1,54	1,47	1,49	1,47	1,50
Swedish krona	0,5	0,7	9,78	9,50	9,40	9,20	9,00
Norwegian krone	2,9	2,5	9,57	9,10	9,00	8,90	8,80
Chinese yuan	-0,5	-0,3	7,84	7,48	7,88	7,88	8,16
vs. US-Dollar	(vs. USD, %)						
Japanese yen	3,2	2,8	109	115	109	109	107
Swiss franc	4,6	4,3	0,93	1,02	1,00	1,02	0,96
Canadian dollar	2,1	1,6	1,23	1,31	1,30	1,28	1,26
Swedish krona	3,9	3,7	7,88	8,64	8,17	8,00	7,50
Norwegian krone	6,4	5,4	7,71	8,27	7,83	7,74	7,33
Chinese yuan	3,5	3,2	6,29	6,80	6,85	6,85	6,80
US-Dollar vs. ...	(vs. USD, %)						
British pound	5,0	4,4	1,42	1,29	1,28	1,28	1,41
Australian dollar	3,2	2,9	0,81	0,75	0,77	0,78	0,80

*31.01.2018

Sources: Bloomberg, Helaba Research ■