

NOK flow update

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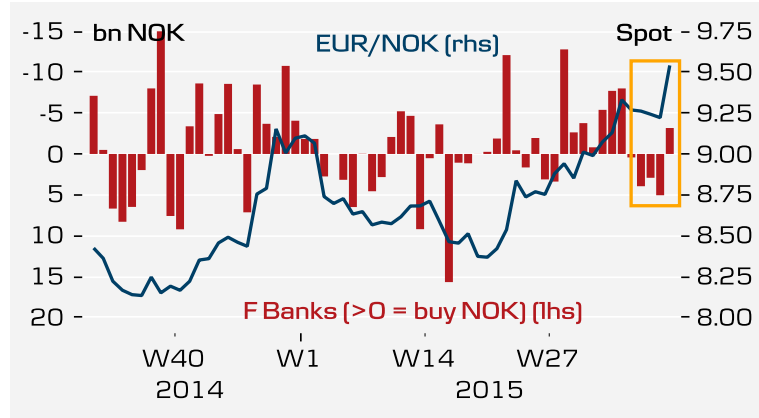
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NOK flow update – ‘Norges Bank uncertainty premium’ visible

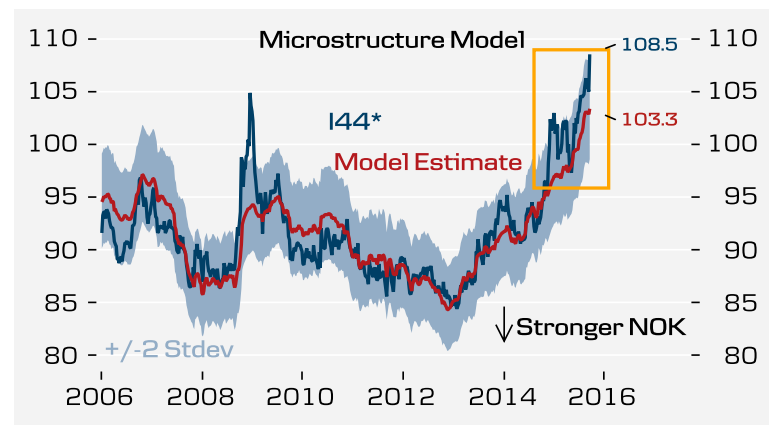
- Norges Bank FX transactions statistics released today show that **foreign banks (proxy for speculative flows) net sold NOK 3.2bn in the Norwegian currency last week**. The net selling primarily reflects how Norges Bank surprised markets on 24 September by cutting the sight deposit rate by 25bp to 0.75% whilst signalling a high probability of another cut (for more details see [Norges Bank Review: a 25bp cut and an easing bias](#)). As figure 1 shows, it was the first time in five weeks that banks net sold the Norwegian currency after a post-summer period of short covering.
- Importantly, the chart shows that, **while the NOK weakened significantly on the Norges Bank’s announcement, the net selling was actually very limited from a historical perspective (chart 1)**. Indeed, according to our microstructure model on FX flows, the weakening of the NOK was considerably greater than what a historical/statistical relationship would suggest (chart 2). According to the model, the import-weighted NOK (the index Norges Bank projects) should have weakened by just 1% due to the selling pressure during the week and not by the actual 3%.
- In our view, the move higher in the I44 reflects further considerable widening of the NOK liquidity- and risk-premium as **markets have priced a ‘Norges Bank uncertainty’ premium into the NOK**. This has contributed to sending the I44 index to the highest level ever recorded (since 1989). While a tightening of this risk premium together with overall stretched short speculative positioning should eventually become a NOK positive when the business cycle turns, we still expect the NOK to trade around the current weak levels in the months ahead. **We target EUR/NOK at 9.40 in 1M, 9.40 in 3M, 9.25 in 6M and 8.80 in 12M.**

Chart 1. Last week’s net NOK selling was actually fairly limited relative to the actual spot movement



Source: Norges Bank, Danske Bank Markets

Chart 2. Increase in NOK risk premium is reflected in our microstructure model



*The I44 is the NOK index that Norges Bank forecasts, and currently the EUR (34%), SEK (13%), CNY (10%), GBP (7%), DKK (6%) and USD (6%) make up the majority of the index.

Source: Norges Bank, Danske Bank Markets

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