

NORDKINN

— ASSET MANAGEMENT —

Market Review & Outlook

December 2025

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Market overview

Global review

Financial markets ended December broadly unchanged, with global government bond yields rising only modestly overall and the USD weakening slightly. However, this perceived stability masked pronounced intra-month volatility. Early in the month, global rates experienced a sharp sell-off, as stronger-than-expected Canadian labour market data, higher Australian inflation, and hawkish comments from ECB Executive Board Member Isabel Schnabel triggered a rapid repricing across G10 bond markets. Short-term yields rose by around 20 bps and yield curves flattened dramatically over a few days before retracing much of the move later in the month.

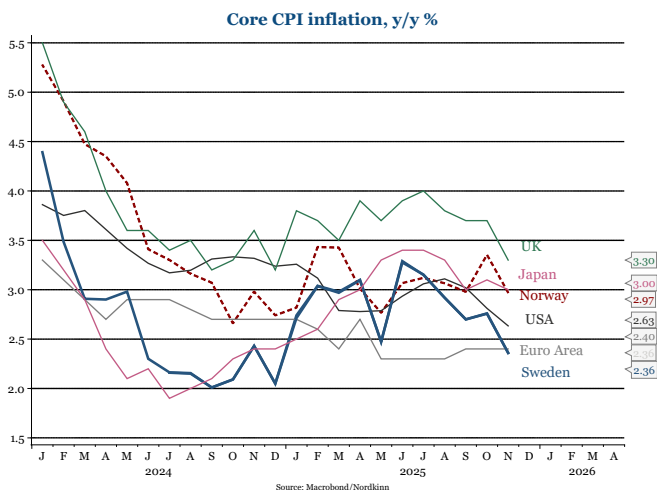
In the U.S., macroeconomic data remained distorted by the government shutdown. A much lower-than-expected CPI print was largely dismissed as a technical anomaly, while unusually large swings in October and November payroll figures were attributed to shutdown-related measurement issues. In contrast, the strong Q3 GDP print reinforced perceptions of continued economic resilience, with consumer spending remaining robust. Nonetheless, the inflationary impact of new tariffs has so far been more muted than feared.

The Fed cut rates by 25 bps at its December 10th meeting, with a divided committee and dissents on both sides. Changes to the dot plots were limited, and the median FOMC participant now signals only one additional rate cut in 2026, underscoring a high bar for further easing.

In the Euro area, the ECB left its policy rates unchanged and emphasised that it is far too early to signal a clear direction of the next move. Earlier optimism around improving European data was tempered by a marked deterioration in German manufacturing sentiment, reinforcing the ECB's cautious and conditional stance.

In the UK, incoming data continued to weaken, and November inflation surprised clearly to the downside, see chart. The Bank of England responded with a 25 bps rate cut, following a finely balanced split-vote of five to four in favour of easing. Despite the close call, markets interpreted the outcome as consistent with a gradual easing cycle.

In Japan, the Bank of Japan raised policy rates by 25 bps to 0.75%. While acknowledging that policy remains accommodative and real rates are still low, the Bank reiterated its intention to normalise gradually after decades of ultra-loose policy. Longer-dated Japanese government bond yields rose following the hike, contributing positively to performance within our *"Sovereign risk premia and fiscal divergence"* theme, offsetting losses from spikes in UK short-term rates earlier in the month.



Nordic review

Swedish interest rate markets in December were shaped by a combination of global repricing pressures, strengthening domestic growth, and a clear moderation in inflation. Early in the month, the sharp increase in rates in Canada, Australia, and parts of Europe spilled over into Swedish markets, which lifted shorter term rates and flattened the Swedish curve. This was later countered by domestic inflation developments: November CPI came in markedly lower than in October and below Riksbank's expectations, reinforcing the view that underlying price pressures are easing after previous month's upside surprise.

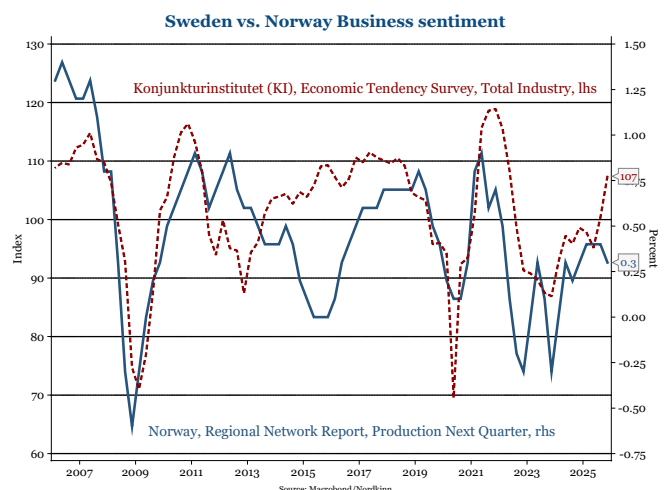
At the same time, the macroeconomic outlook for Sweden strengthened further. Survey data, including the Economic Tendency Indicator, pointed to stronger-than-normal economic growth, underscoring resilient demand and improving activity momentum, see chart. Against this backdrop, the Riksbank decided on December 18th to keep its policy rate unchanged at 1.75 %, as widely expected, with guidance signalling rates on hold for an extended period.

The combination of strong growth, falling inflation, stable policy rates and higher global rate expectations led to a pronounced steepening of the Swedish money market curve. This benefitted our theme *"Sweden: Road to recovery"* offsetting marginal losses from our *"Return of the inflation hedge"* theme.

In Norway, as our price survey models had projected, inflation fell more than expected in October. Changes largely reflected aggressive Black Friday discounting, as we highlighted in the previous monthly report. The Regional Network pointed to slightly weaker economic growth and lower capacity utilisation, see chart. As expected, Norges Bank left its key policy rate unchanged at 4.00% at its December 18th meeting, while revising the policy rate path modestly lower, signalling one to two rate cuts in 2026.

Notably, Norges Bank emphasised that further depreciation of the NOK could delay policy easing. With EUR/NOK trading above 12.0 and NOK/SEK close to 0.91 ahead of the meeting, the communication clearly signalled discomfort with currency weakness. Short-end rates rose and the NOK strengthened modestly following the decision.

Overall, despite notable intra-month volatility driven by global yields, domestic data, and a relatively hawkish Norges Bank, the impact on our Norwegian investment themes was contained. However, our long NOK FX exposure in the *"Tactical risk reward trading"* theme experienced negative performance during December.



Outlook

Global outlook

The ongoing U.S. government shutdown will continue to impair the quality and availability of data into 2026, with gaps in CPI reporting likely taking several months to normalise. In addition, the risk of another shutdown remains elevated, as current funding expires at the end of January 2026. This backdrop will complicate policy assessment and increase the risk of market volatility around incomplete or distorted data.

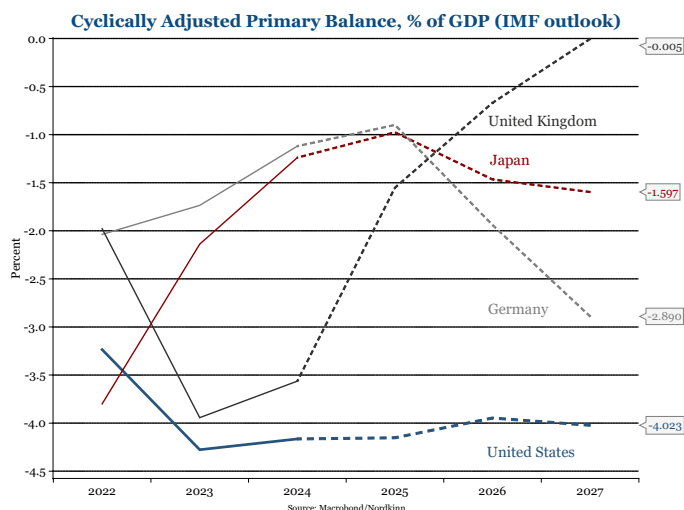
Beyond data noise, the U.S. outlook remains characterised by internal divergence. Aggregate activity is supported by strong AI-related investments and continued spending by higher-income households, while labour demand remains subdued — particularly for younger workers — and delinquencies are rising among lower-income households. Inflation remains above target, but tariff-related price pressures have so far been more limited than feared.

We believe this uneven equilibrium can persist through 2026. Fiscal policy is likely to remain supportive, with Big Beautiful Bill-related tax cuts and transfers providing additional stimulus. Under the current Fed leadership, the bar for further rate cuts appears high. However, political pressure and the shift of Fed Chair in May could reopen the door to further easing. Nonetheless, with markets already discounting some 50 bps of easing, we prefer trading front-end U.S. yields from the short side, while longer-dated yields remain sensitive to growth expectations, equity-market performance and a continued challenging fiscal outlook.

In Europe, hopes for a recovery driven by higher investments remain intact, but realised effects have so far been modest. German manufacturing continues to face structural headwinds and infrastructure spending is progressing slowly. With subdued growth and limited inflationary pressure, the ECB is unlikely to consider rate hikes in 2026. This suggests low front-end yields and relatively steep yield curves.

The UK outlook appears more challenging. Despite a less restrictive-than-feared 2026 budget, fiscal tightening is likely to weigh on an already fragile economy, see chart. As activity softens, we expect wage and price pressures to ease, allowing the Bank of England to continue cutting rates toward 3% in 2026. This favours lower UK yields relative to the U.S. and Euro area, though fiscal uncertainty is likely to keep term premia volatile.

Japan remains an outlier. Inflation is still elevated, and a more expansionary fiscal stance under the new government, combined with persistent currency weakness, support further policy normalisation. We expect the Bank of Japan to continue raising rates gradually in 2026, with Japanese government bond yields trending higher and reinforcing an attractive cross-market divergence versus Europe and the UK.



Nordic outlook

The Swedish economy is entering 2026 with a markedly improved macro backdrop. After several years characterised by aggressive monetary tightening, weak demand, and elevated inflation volatility, the economy has transitioned into a phase of recovering growth and easing inflation pressures — a combination that is particularly supportive for interest-rate and curve-steepening strategies.

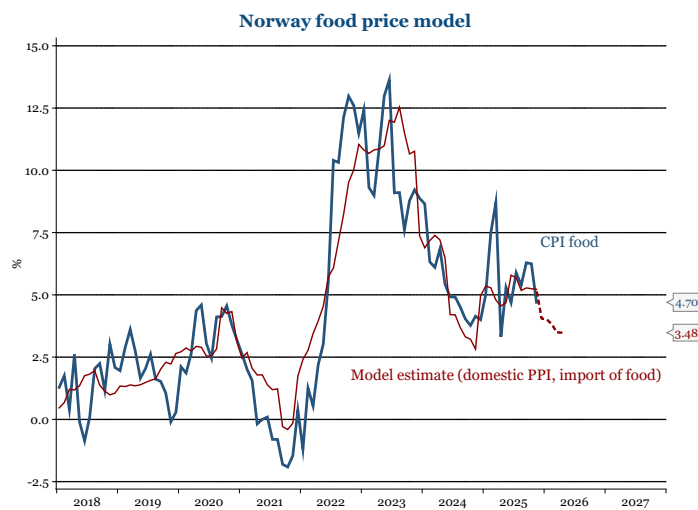
With significant labour market slack still in place and the government's VAT cut in April set to take effect, we expect wage and price inflation to remain subdued through 2026. This should leave the Riksbank well positioned to keep its key policy rate on hold at 1.75% for an extended period, at least through year-end. Against a backdrop of improving growth and rising global term premia, this creates favourable conditions for steeper yield curves. In addition, elevated government bond supply is likely to exert persistent pressure on Swedish government bond valuations, particularly at the long end of the curve. As a result, we see further scope for Swedish bonds to cheapen — relative to swaps, on a cross-market basis, and relative to shorter maturities.

In Norway, the outlook is more nuanced but remains constructive. Inflation has moderated but still runs around 100 bps above target. While domestic demand remains relatively resilient, overall economic activity appears to be operating slightly below normal capacity, suggesting that underlying wage and price pressures should gradually ease.

That said, with wage growth still elevated and monetary policy being sensitive to exchange-rate developments, as at current we expect Norges Bank to remain patient and keep its policy rate unchanged at 4.00% until June, broadly in line with the Bank's projections.

The timing and extent of further policy easing will however hinge critically on continued progress toward the 2.0% inflation target. We currently see three forces supporting such progress. First, lagged effects from lower commodity prices and softer international price pressures should dampen imported inflation, particularly for food, see chart. Second, oil-fund-related FX flows, where Norges Bank has moved from being a net seller to net buyer of NOK, will support NOK in 2026, keeping import prices contained. Third, lower capacity utilisation should help restrain domestic wage and price pressures in the months to come.

Overall, the Nordic outlook is characterised by meaningful differences in growth trajectories, bond supply dynamics, and monetary policy reaction functions. This divergence creates scope for cross-market relative value opportunities, both within the Nordic region and relative to Europe and the U.S.



About Nordkinn

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Our focus is to generate stable absolute returns that exhibit low correlation to other assets. Our Nordkinn Fixed Income Macro Fund was launched in 2013.

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