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Macro Research

Weekly update 24/2019

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Highlights

The world around us

The Norwegian economy

Market charts & comments

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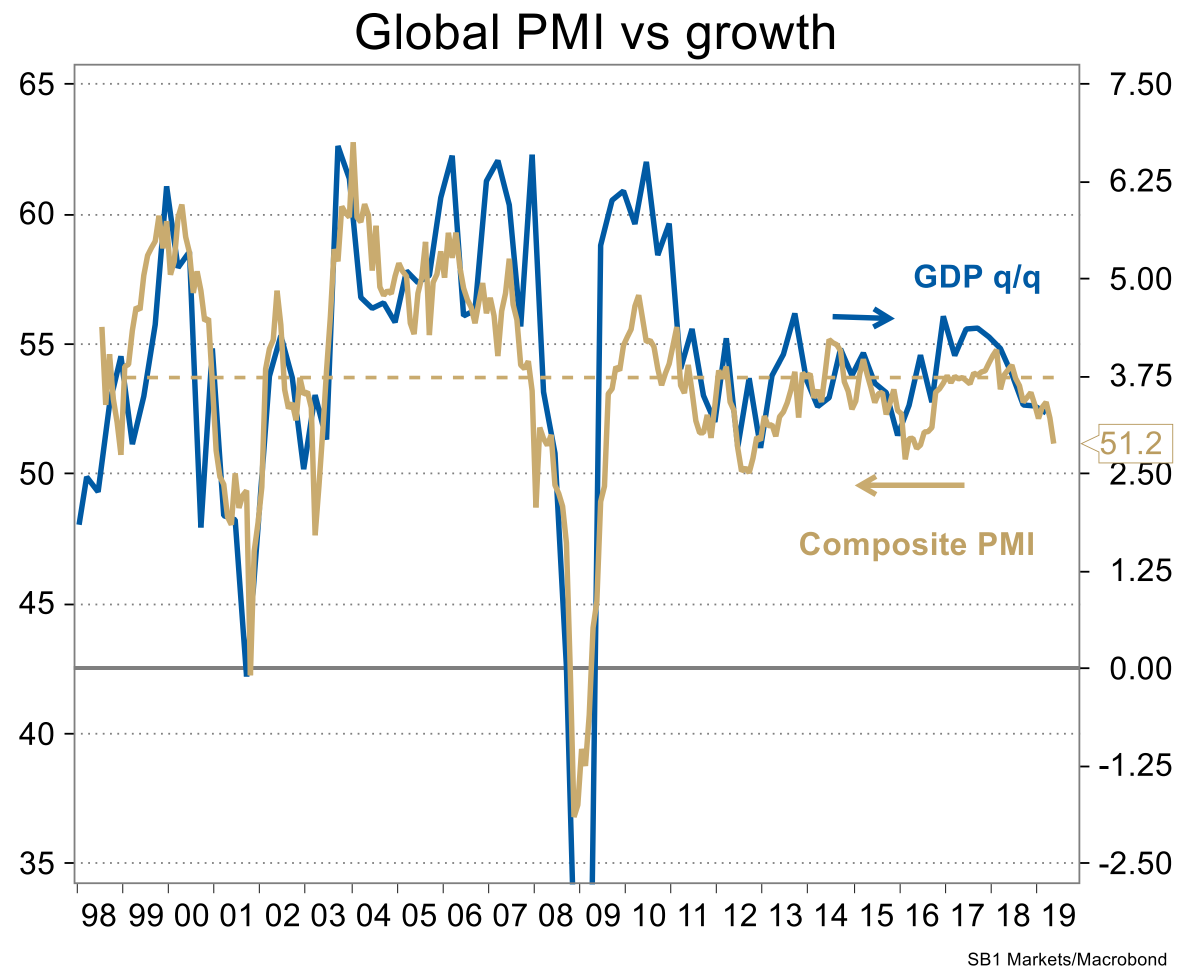
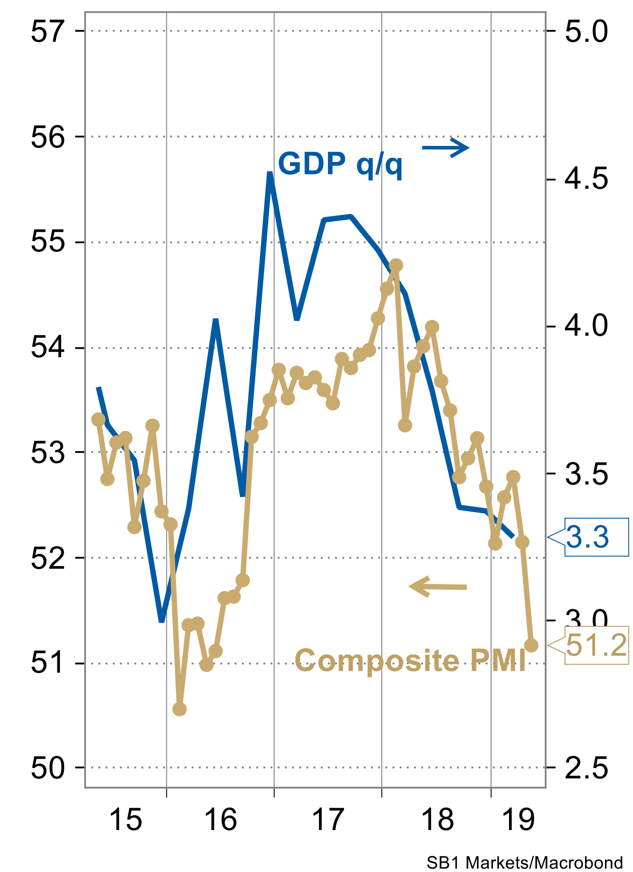
Last week – the main takes

- USA will not impose **tariffs on imports from Mexico now** as Mexico accepted measures in order to curb immigration into US (measures Mexico already may have promised to deliver; a review after 90 days). No positive news on the **US/China debacle**. Trump threatens China with more tariffs if president Xi does not turn up at the G20 in Japan June 29
- **The global composite PMI** dropped by 0.9 p in May, 0.3 p weaker than we f'casted. The PMI at 51.2 is pointing to a noteworthy downtick in global GDP growth, to below 3% (vs 3.6% in Q1). The decline was broad based, both DM and EM noted slower growth, all within the range from 51.1 to 51.5. The steep drop in manufacturing may be spreading to service sectors, which fell 1.2 p in May. **Markit's composite China PMI** softened as services reported easing growth. However, the avg of Markit/NBS at 52.4 is not suggesting any abrupt slowdown. In the **US, the manufacturing ISM** came in below expectations at 52.1, a 0.7% decline. The speed down is worrisome, particularly as Markit's PMI is deteriorating at an even faster pace. On the bright side, the **non-manufacturing ISM** edged up, more than offsetting the decline in manuf. **Eurozone PMIs** remain lackluster, although service sectors are not following manufacturing down. The UK PMI fell sharply as stock-building before the expected Brexit came to an end
- US **auto sales** grew in May, while sales were flat in the EMU following the lift in April. No China data (or a world estimate) yet
- Both **Chinese exports and imports** are trending up from the Q4 trough, at least until May (and the recent tariff hikes)
- **US nonfarm payrolls** rose just 75', vs 175' expected. April was revised down too, but the avg of the two months is not disturbingly weak. The slowdown was broad based. Unemployment was stable at 3.6%, and other labour market indicators do not signal any weakening of the labour market. Still, wage inflation decelerates, leaving Fed an argument for turning dovish. **The Fed's Beige Book** reported a slightly more <u>upbeat</u> economic outlook. **The trade deficit** shrank marginally in April but exports slipped in volume terms, so net trade will probably not contribute to growth in Q2
- **The ECB** took an (unsurprising) dovish turn, is postponing the first interest rate hike at least until H2 2020, and granting banks better conditions than expected in the new lending mechanism (TLTRO). Moreover, the ECB is signaling readiness to act and further expansionary measures were discussed at the meeting. <u>Mixed macro data last week:</u> **The Q1 GDP details** were solid, private consumption and business investments gained speed. **Unemployment** keeps sliding down. **Retail sales** softened but are still on a moderate upward growth path. What is the problem, except global uncertainties?? **Core CPI inflation** slipped 0.5 pp, primarily due to base effects. **Industrial production** is tumbling in Germany, April down 2.3%, adding to signs of a deep downturn. We estimate a 0.6% m/m decline in total EMU production. **Germany exports** fell steeply too, confirming weak surveys and orders
- **Norwegian house prices** rose 0.5% in May, more than we expected, even if the number of unsold homes is soaring; pointing to muted price growth the coming months. **Manufacturing production** surprisingly spiked in April, both sectors gained speed. **Mainland GDP** increased moderately in April, the speed into Q2 is approx. 2%. **Households' savings** increased in Q1 and the cash flow is now marginally positive. In the **Q2 Economic Outlook report,** SSB nudged up the f'cast on 2019 GDP growth to 2.5% (0.2 pp below Norges Bank's March f'cast). The 2020 estimate at 2.2% is well above NoBa's 1.8% f'cast. The upward revision is partly due to higher oil investments, SSB expects 14.5% growth in 2019, from 12.9 in the Q1 report (our estimate is 14%). Wage inflation f'casts at 3.3% in '19 and 3.5% in '20 are consistent with other estimates

Global PMI plunged to 51.2 in May, signals below 3% global GDP growth

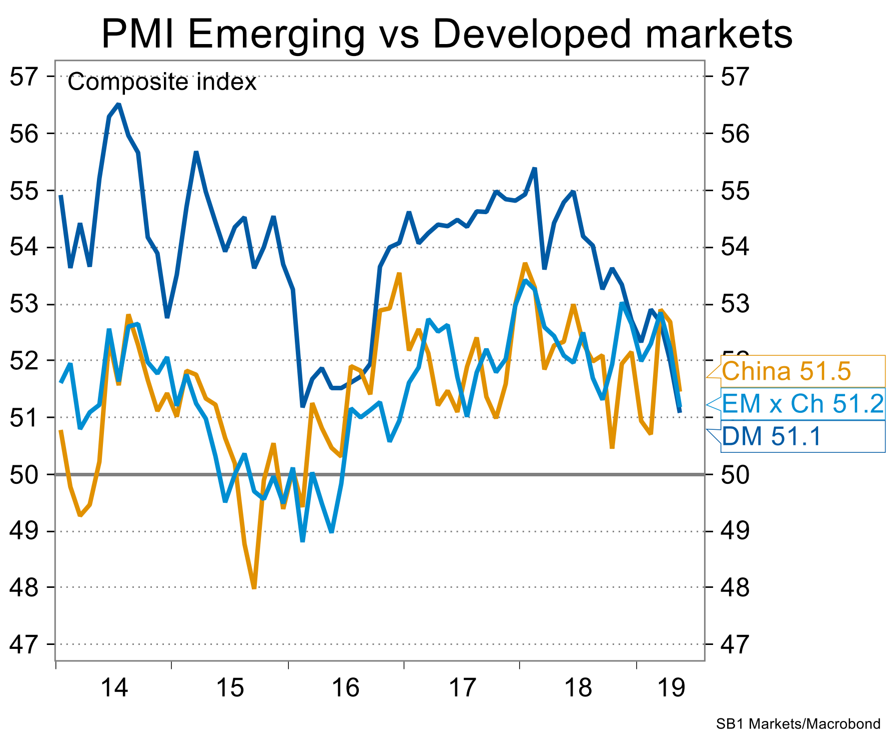
Composite PMI fell by 0.9 p, (we f'casted a 0.6 p drop), growth decelerates to below 3%, from 4+

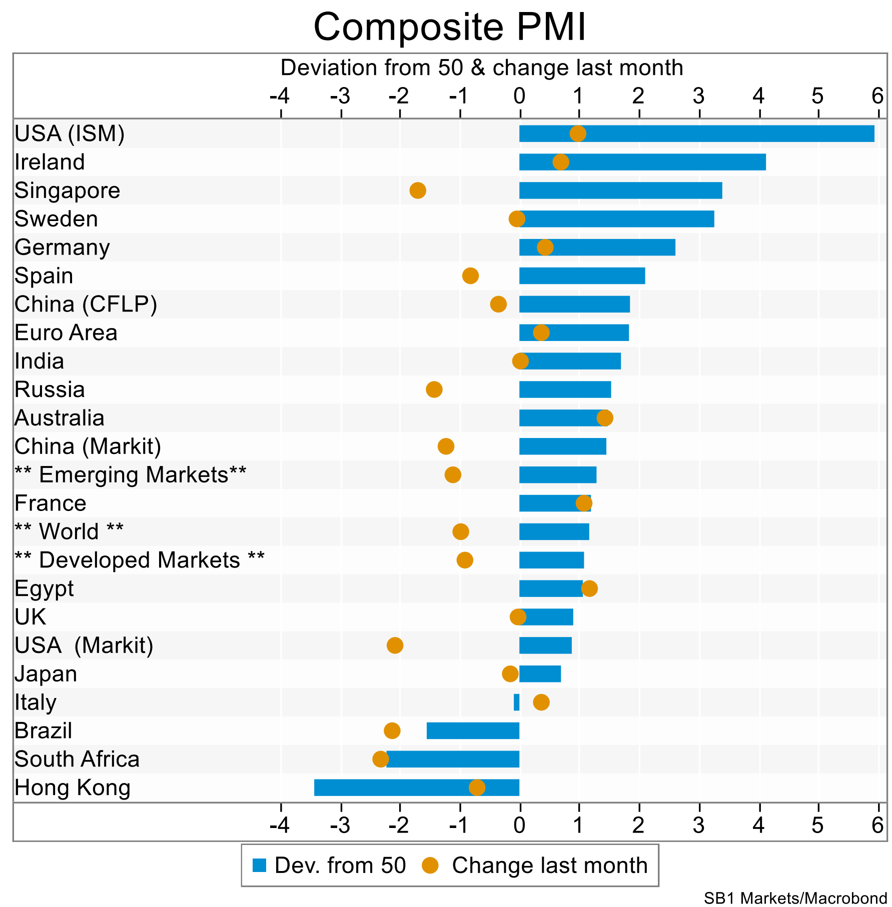




A broad slowdown in May, DM growing at the softest pace in 6 years

Emerging markets are holding up quite well, Developed slows sharply. China down, still trending up?





- Just 8 countries/regions reported that activity expanded at a higher pace in May (9 in April), 13 slowed
- Still just 4 countries below the 50-line (from 2 in April)
- DM average fell 0.9 p to 51.1, signalling slower growth. EM x China down 1.1 p, marginally outpacing DMs. China down to 51.5, still above the Jan/Feb level, and above the past 6 y avg

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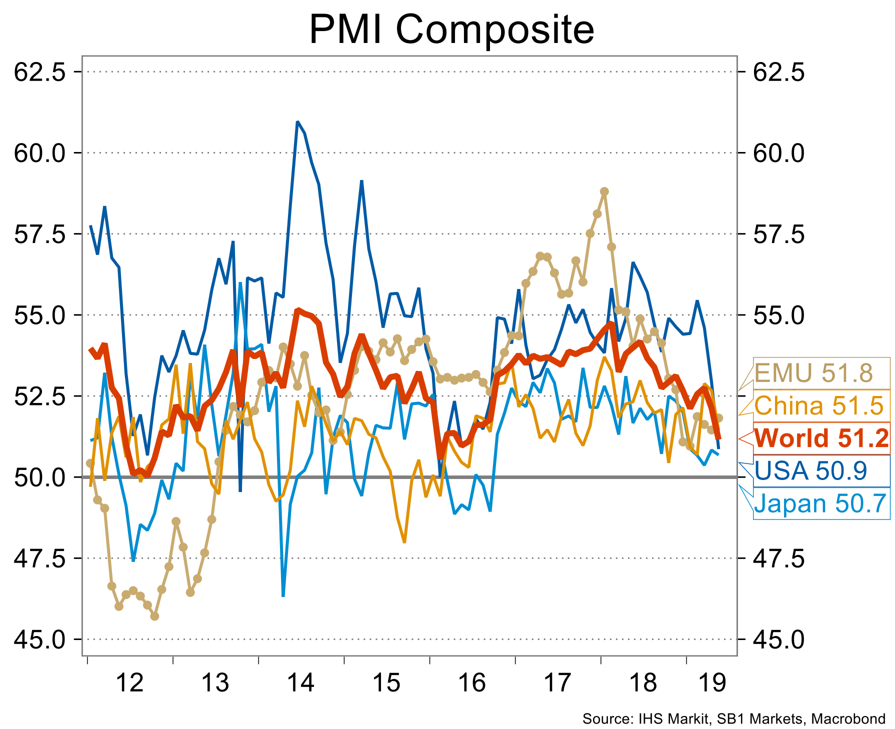
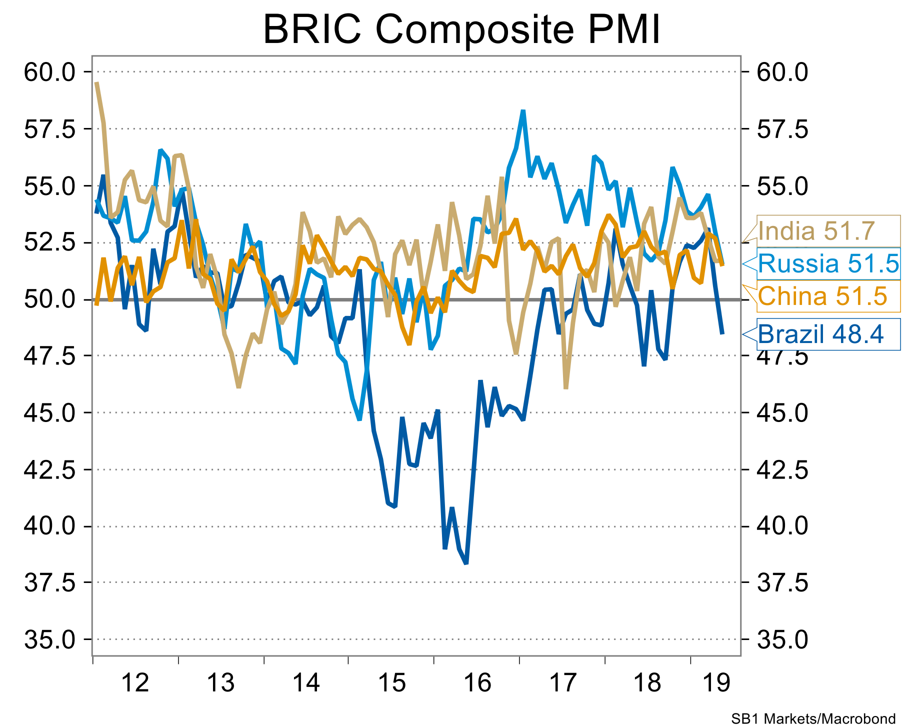
US is slowing rapidly, EMU stable, China a tad weaker in May

BRICs were mostly on the weak side in May, Brazil slipped back below 50

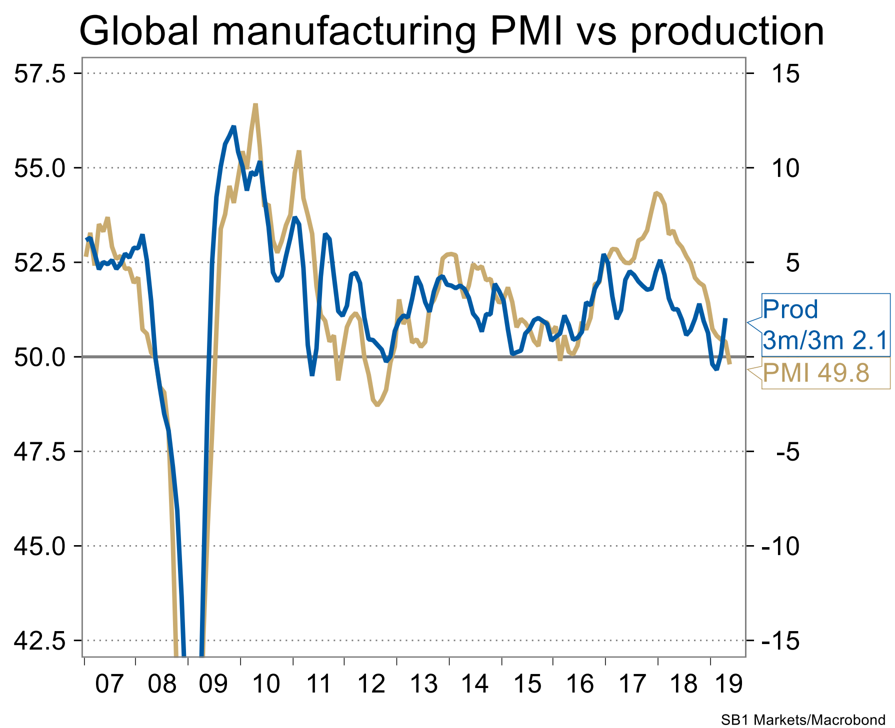


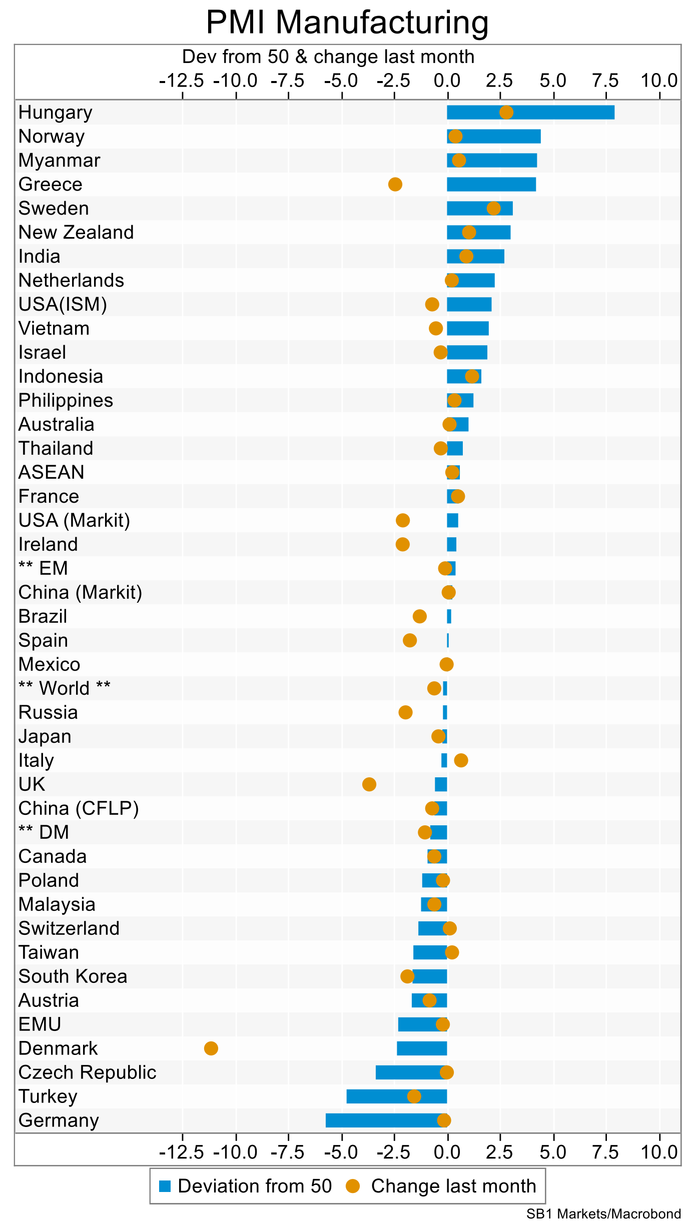


- US Markit's PMI dropped 2.1 p in May, both sectors weakened (however, services ISM improved, taking the ISM avg up)
- Mixed China data; Markit's composite index fell 1.2 p to 51.5, the 'official' NBS PMI fell just marginally. The government stimulus may not be sufficient to bring growth up but PMIs are anyway indicating that activity is expanding at a faster speed than in early 2019
- The EMU PMI improved marginally, is stabilised at a low level (but above the US May level) the past 4 months. However, manufacturing is still tumbling

Manufacturing PMI edged down in May, signals stagnation

The index fell 0.6 p to 49.8, pulled down DM (primarily US, UK)

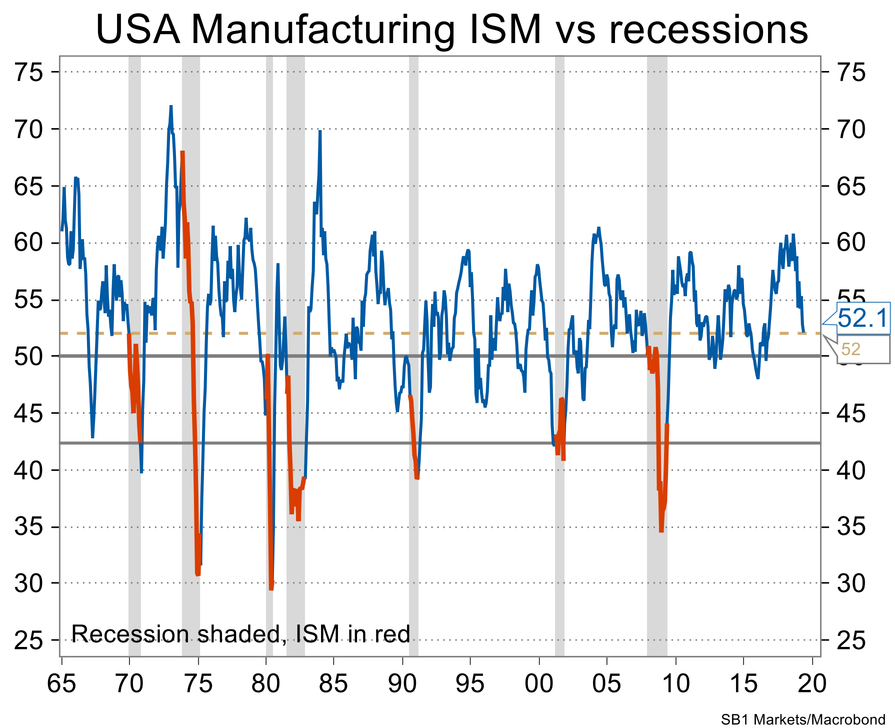


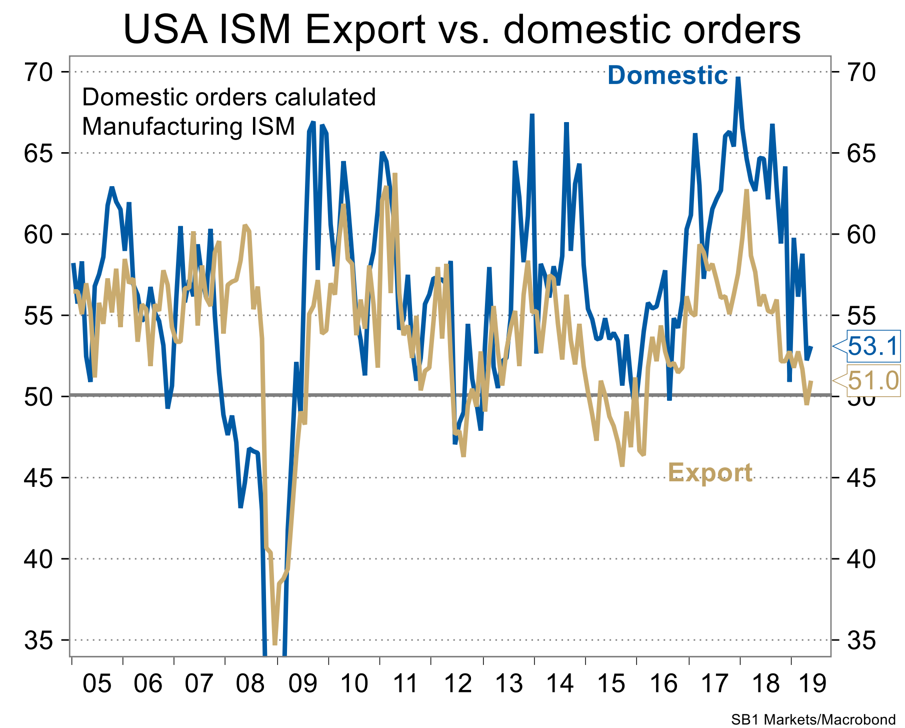


- Global manufacturing PMI fell to 49.8 in May, in line with our estimate. , based on the preliminary results from some countries. **The index has fallen for 13 consecutive months, signals stalling global manufacturing. Production has accelerated somewhat recently, downside risk**
  - 22 (23 in April) countries/regions down in May and 15 up (18)
  - Almost half countries/regions are reporting declining output; 19 countries/regions are below the 50 line. Germany still at the bottom. Norway the 2nd best!
  - Developed Markets fell 1 p in average, Emerging Markets down 0.1 p

Manufacturing ISM another step down in May, below expectations

ISM fell 0.7 p to 52.1, confirming a rapid slowdown. Still, orders are increasing marginally faster

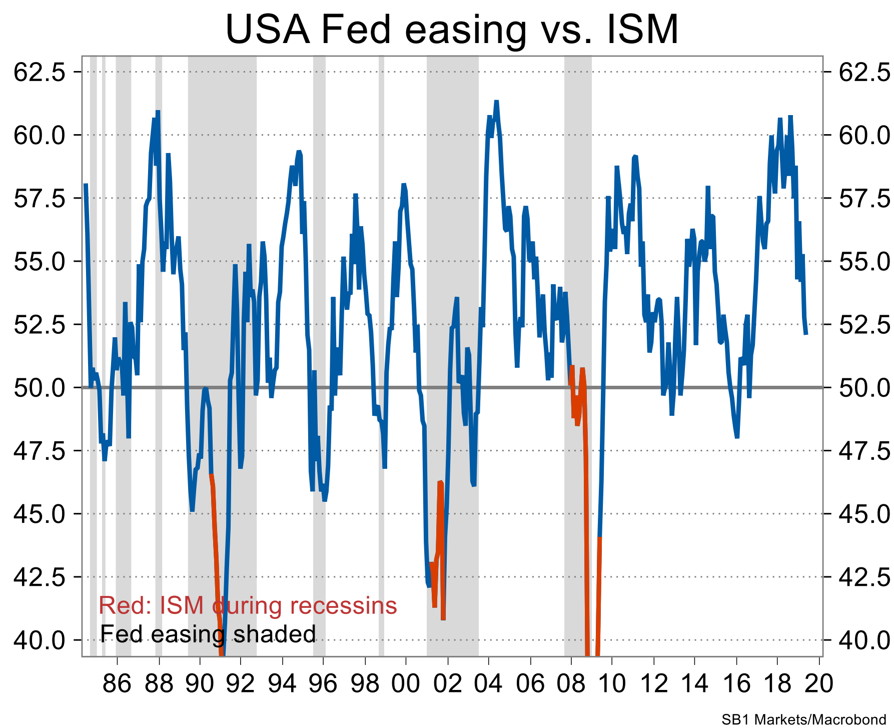


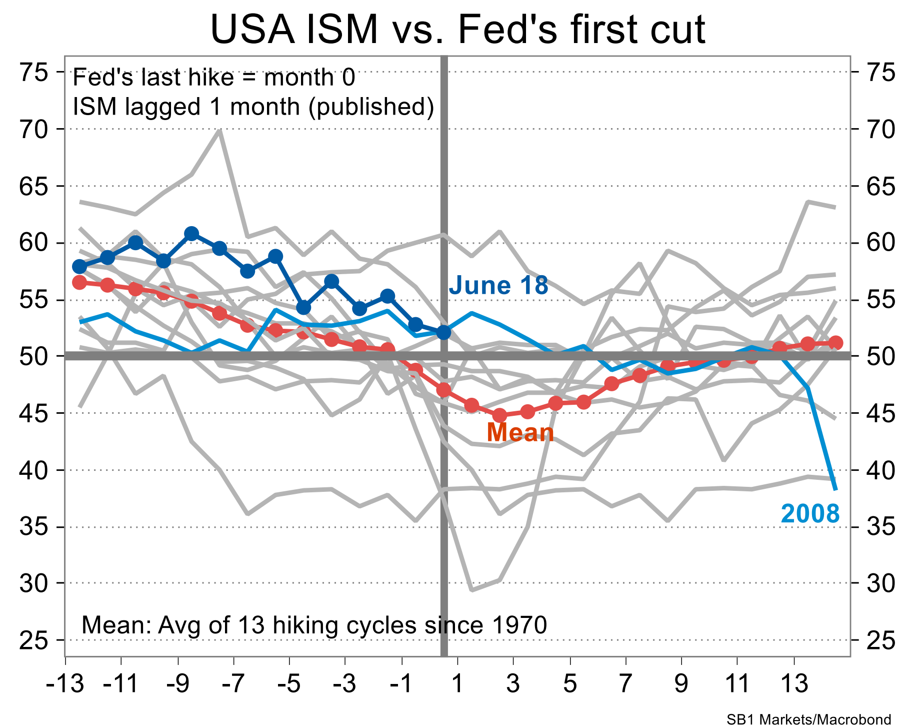


- Manuf. ISM fell to 52.1 in May, was expected up to 53.0, from 52.8. The ISM has nosedived from above 60 last August, and now to the lowest level since Oct 16. The ISM is below the average level (at 52.9) and the speed down is no doubt worrisome, particularly as Markit's PMI slips, too
  - » In the ISM survey, 11 out of 18 manufacturing sectors reported growth (down from 13 in April) and 6 (from 5) sectors reported a contraction
- Businesses reported a marginal acceleration in order inflows (both domestic and exports) and lower inventories, not a weak mix, although the levels are not impressive anymore. Slightly weaker production and faster delivery times, implying weaker demand, pulled the index down
- <u>The really bad news: An ISM at 52 may be an early warning of a recession (in 6 of 20 times, at least). The good news: it usually takes some months</u>

When will the Fed start cutting?

Well, when it believes the economy has slowed (or will slow…) sufficiently





- In average the Fed starts cutting when the manufacturing ISM has fallen below 50 – but has started easing even if the survey is at far higher level – like in Sept 2007 when the (Aug) ISM was at 52.2 (like now, and unemployment still heading down) but when there were some stress in the financial market…
- Fed has engaged in some 13 easing cycles since early 1970, while US has had 'just' six recessions. So, the first hike does not signal a recession

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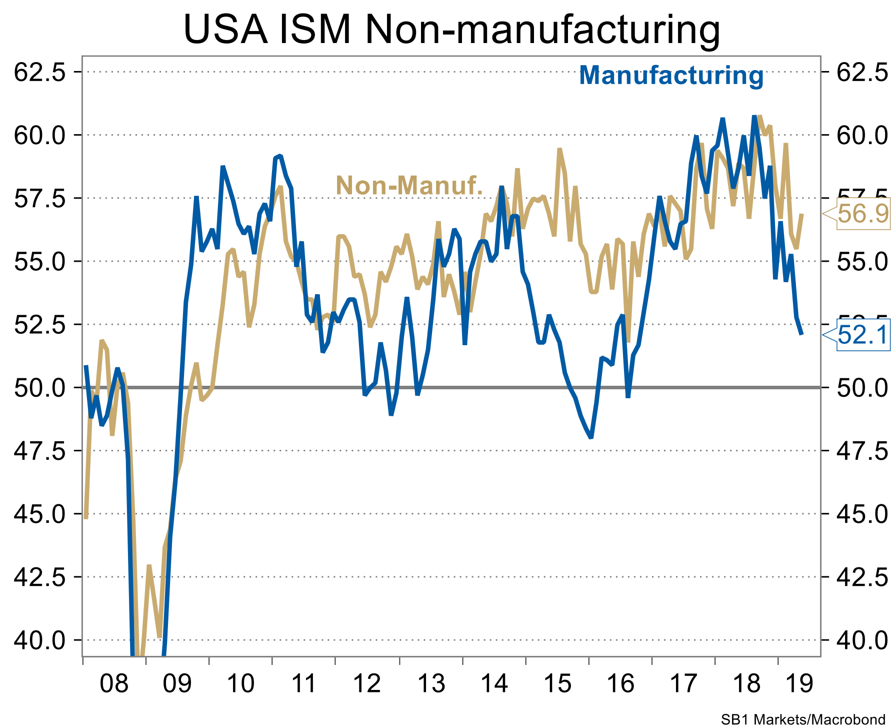
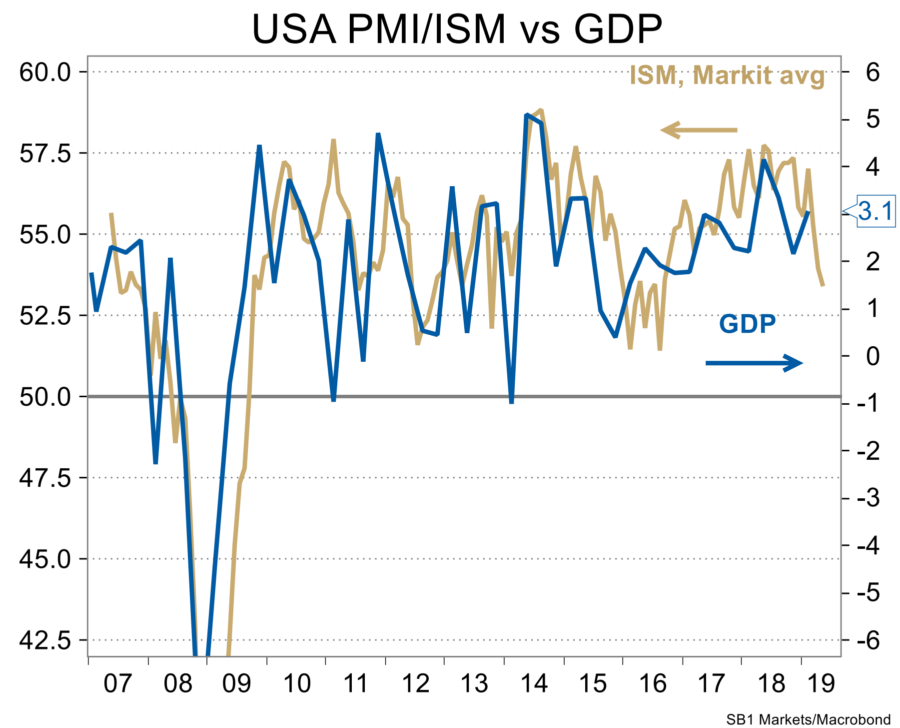
Non-manufacturing ISM gained in May, ‘composite’ ISM ticked up!

Non-manuf. ISM up 1.4 p to 56.9, the avg of Markit/ISM indices signals 1.5% GDP growth

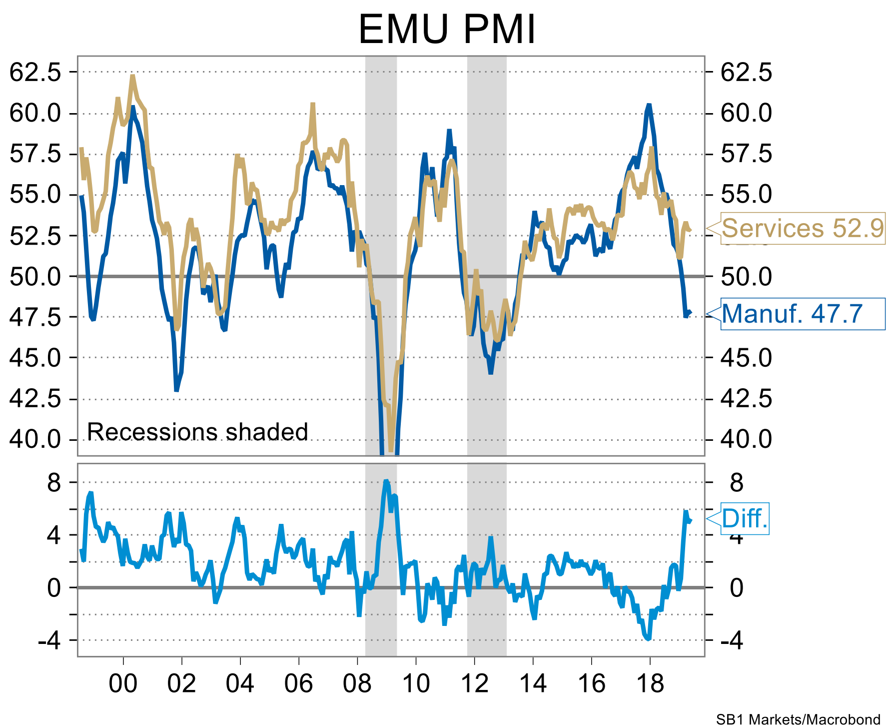


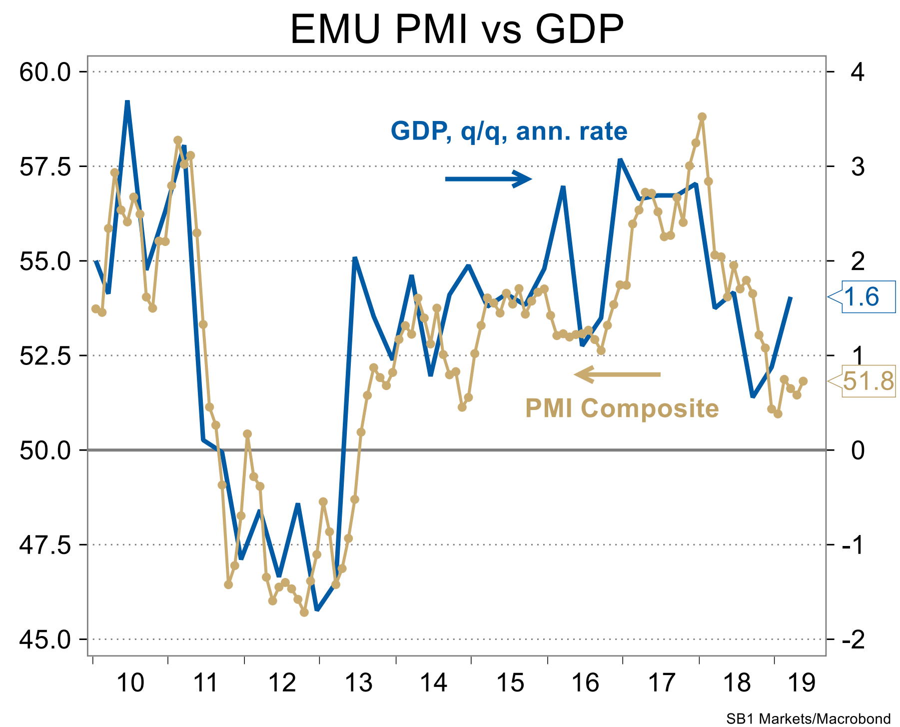


- Non-manuf. ISM came in well above expectations at May, edging up to 56.9. Even with a significant decline the past 6 months, the level way above average. Services are holding up much better than manufacturing, which decreased to 52.1, and the ISM is not confirming the rapid slowdown in service sectors which Markit’s PMI is noting
  - » 16 of 18 non-manufacturing sectors reported growth, just one reported a decrease. Retail trade reported growth, suggesting an upswing in this sector
  - » Composite orders rose marginally to 57.4, thus, orders are still growing at a solid pace – demand is not crumbling
- The ‘composite’ ISM index rose to 55.9, Markit’s composite ISM tumbled to 50.9. Unfortunately, the ISM has been too optimistic vs growth the past couple of years. The avg of the two surveys is pointing to 1.5% GDP growth, just above the nowcasters Q2 f’casts

Final PMI: Composite PMI slides down, services better than first reported

PMI rose 0.3 p in May, 0.2 p above the first est. Manufacturing still weak, services resilient

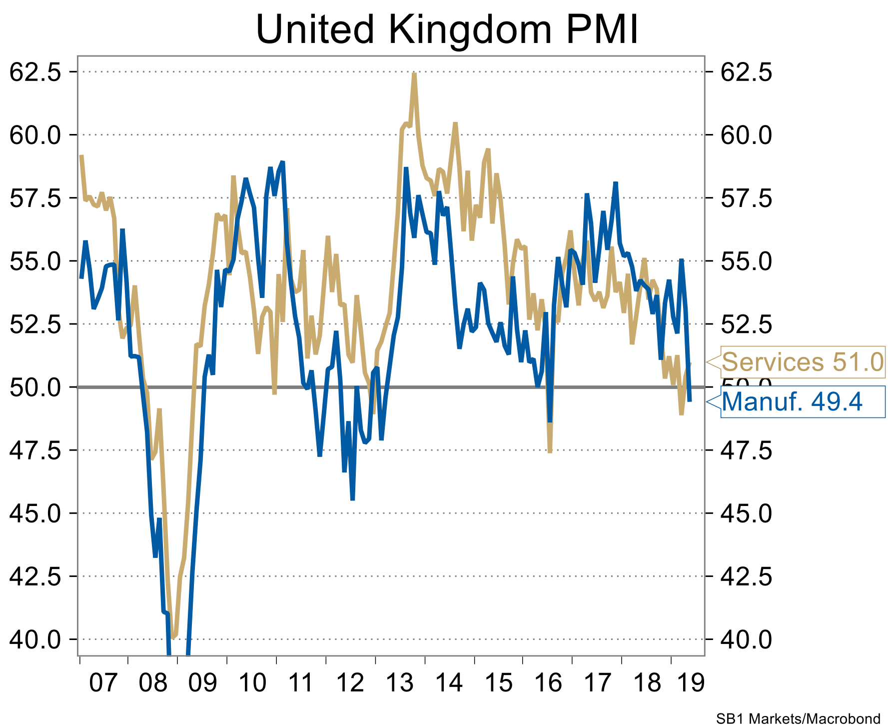


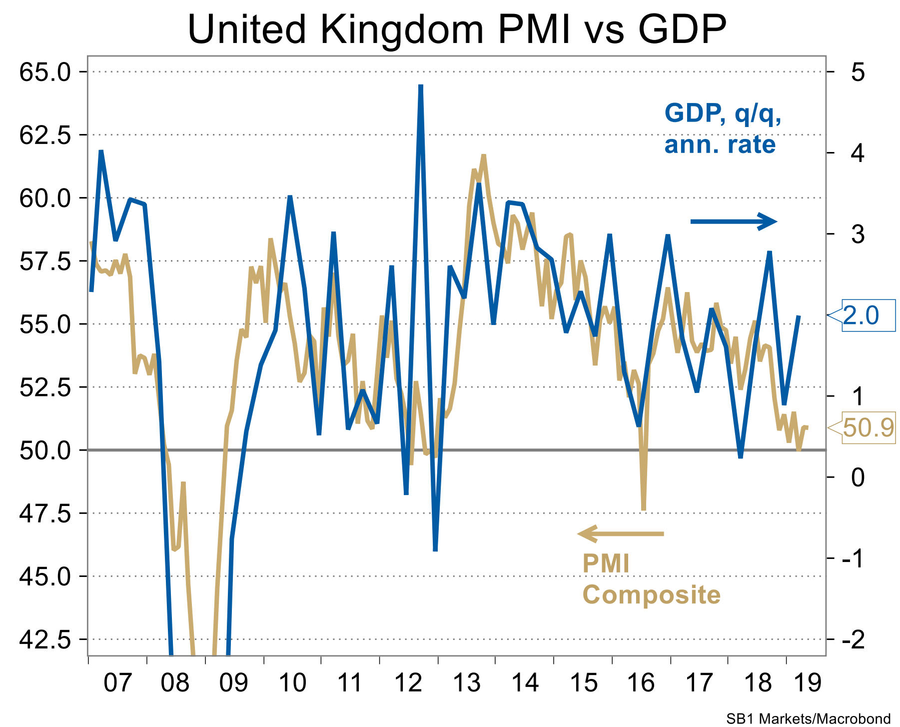


- **The composite index** came in at 51.8 in May, a 0.3 p increase from April, and 0.2 p above the preliminary report. The PMI has stabilised the past 5 months but the survey is no doubt reflecting a substantial slowdown, pointing to some 0.75% growth
  - » Manufacturing PMI at 47.7 is reflecting a continued and sharp contraction, service industries still growing moderately
- **Any hope?** Households are still optimistic, and other fundamentals do not indicate a recession now, and Q1 GDP growth was much stronger than the PMIs were indicating. Unemployment is not record low, wage inflation is still well below 3%, no credit boom recent years. So it may all come down to the trade war, Italy's politicians, Brexit, and France's yellow vests…

Composite PMI still in growth territory, huge downside risk

Manufacturing plunged to 49.4, as businesses are building down pre-Brexit deadline inventories

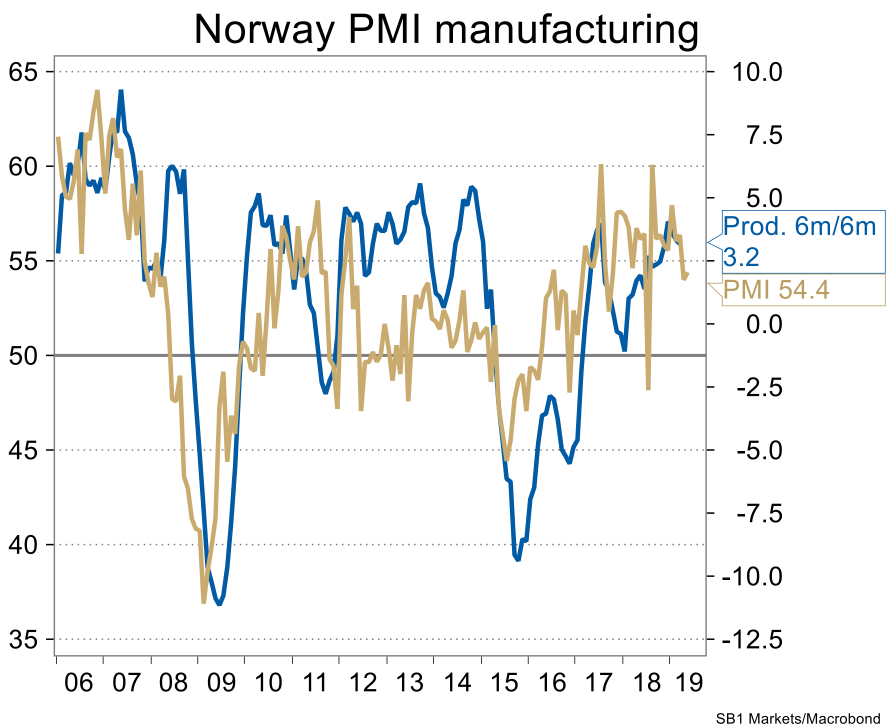


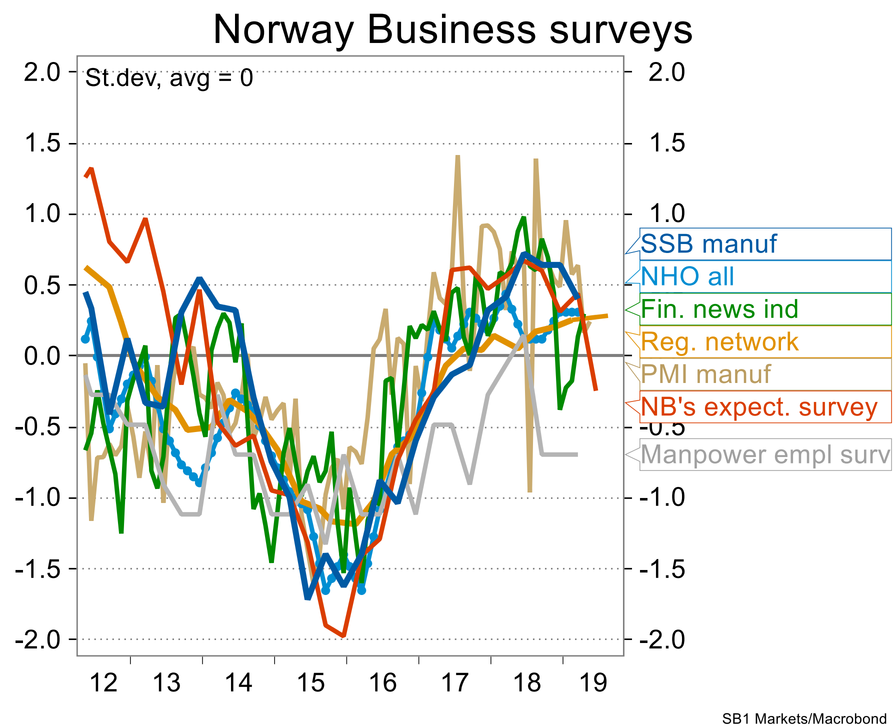


- Manuf. PMI tumbled 3.7 p in May, to the lowest level since the Brexit referendum. Manufacturing activity has been held up by massive efforts to purchase materials ahead of the original Brexit deadline, check the next slide for more. These inventories are now being wound down, contributing negatively to demand
- The service sector PMI rose 0.6 p to 51.0. Businesses have been reporting more or less stagnating activity since November last year, as Brexit uncertainties have been causing postponed/cancelled spending and investment decisions
- The composite PMI at 50.9 is pointing towards just marginal GDP growth

Manufacturing PMI improved in May, indicating moderate growth

PMI ticked up to 54.4, more than 1 p above the avg level. The index is in the mid-range of surveys

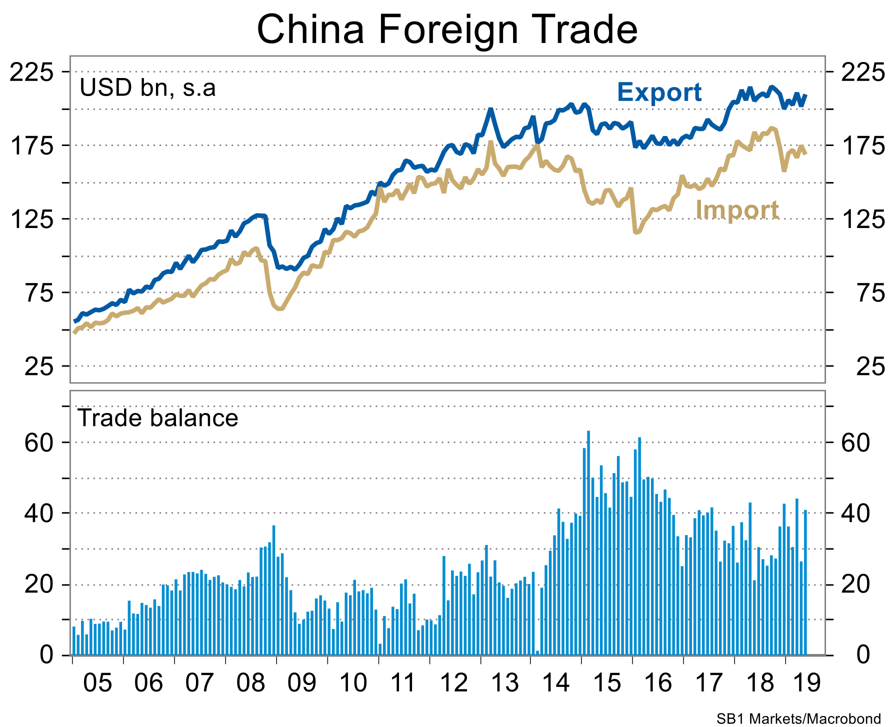




- The PMI rose to 54.4, up 0.4 p from the prior month. The PMI has ticked down recently but is still above the avg level
- In spite a small slowdown, the manuf. index is pointing to moderate growth in manufacturing production, as most other surveys are indicating, too
  - » Manufacturing activity has cooled rapidly in our trading partners, less in Norway, thanks to oil related sectors

Both exports and imports are recovering

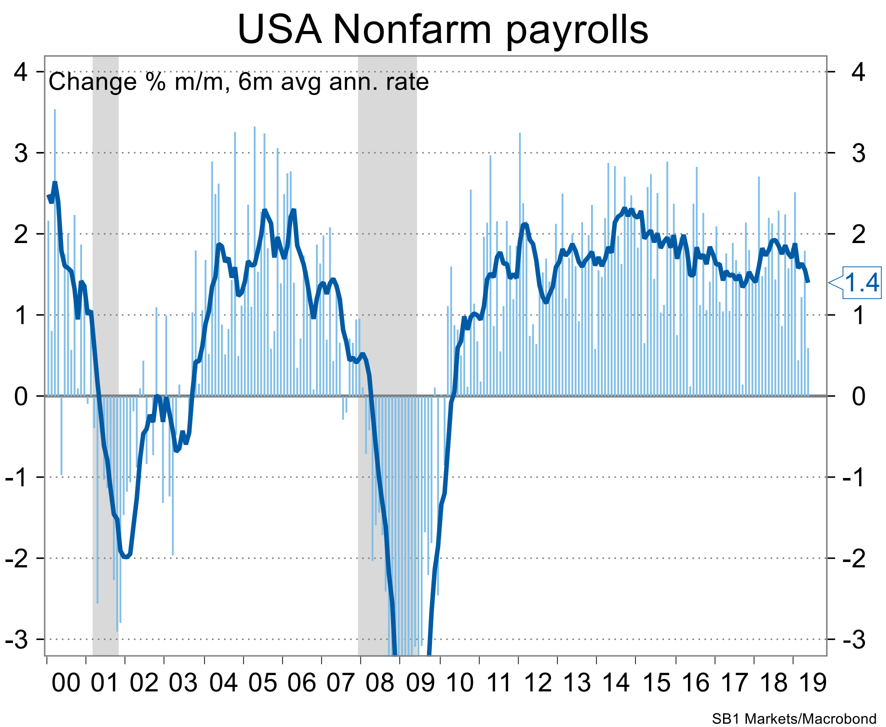
Exports & imports have stabilised after the drop last fall. Exports -6.9% y/y in April, imports +1.1%

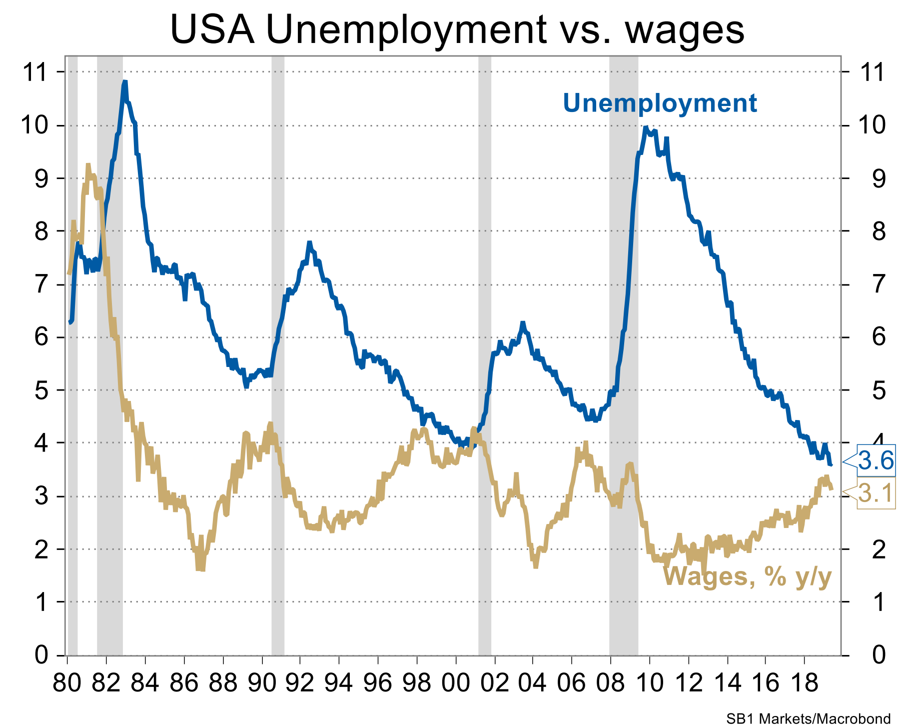


- Exports were reported up 1% y/y in May (in USD), expected down 4%. Exports rose 4% m/m, and is now slowly recovering from the Q4 local through, both in value and volume terms. The trend since early 2018 is close to flat
  - Exports to the US rose in May, but is sharply down y/y, the tariffs hurt exporters. Still total export volumes are flat. Exports to other regions have filled the void. A further escalation of the trade war, which Trump (and then China) decided in May will no doubt dampen Chines exports to the US further.
- Imports are down 8.5% y/y in May (in USD), exp down 4% - and imports fell somewhat m/m. However the trend is slowly up from the weak Q4, even if both value and volumes are down y/y and both are down from the Q3 peak
  - Imports are down from the peak, and are indicating weaker domestic demand
- The trade balance was much stronger than expected, at USD 42 bn, exp 24 bn. The seas. adj. balance is at USD 40, trending roughly flat.

Employment stalled in May and wage growth eased, may be a sign of slowdown

.. But don’t panic, there are no indications of a meltdown at this point. However, at some time…

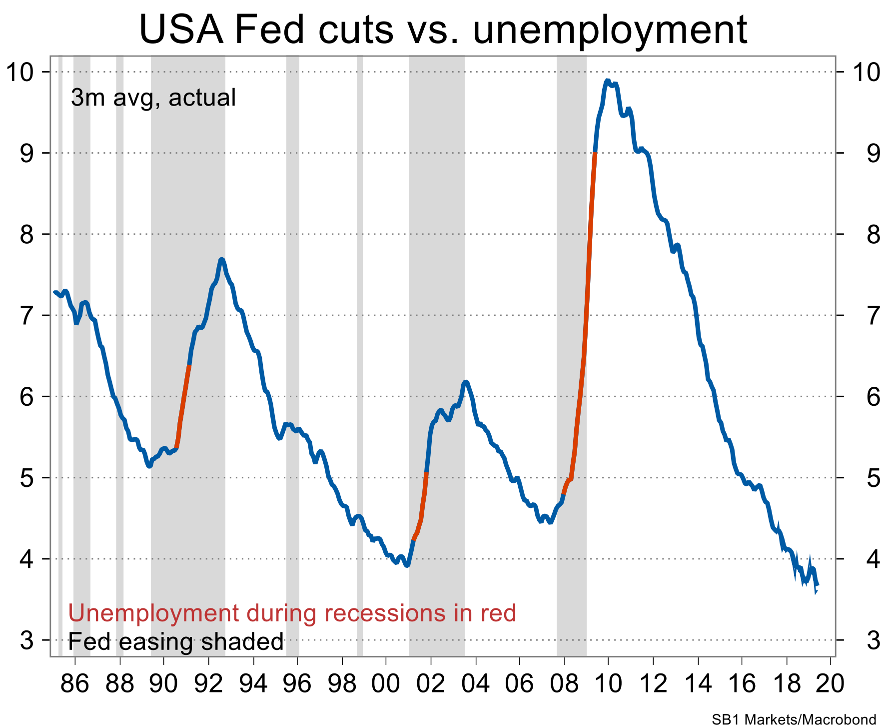


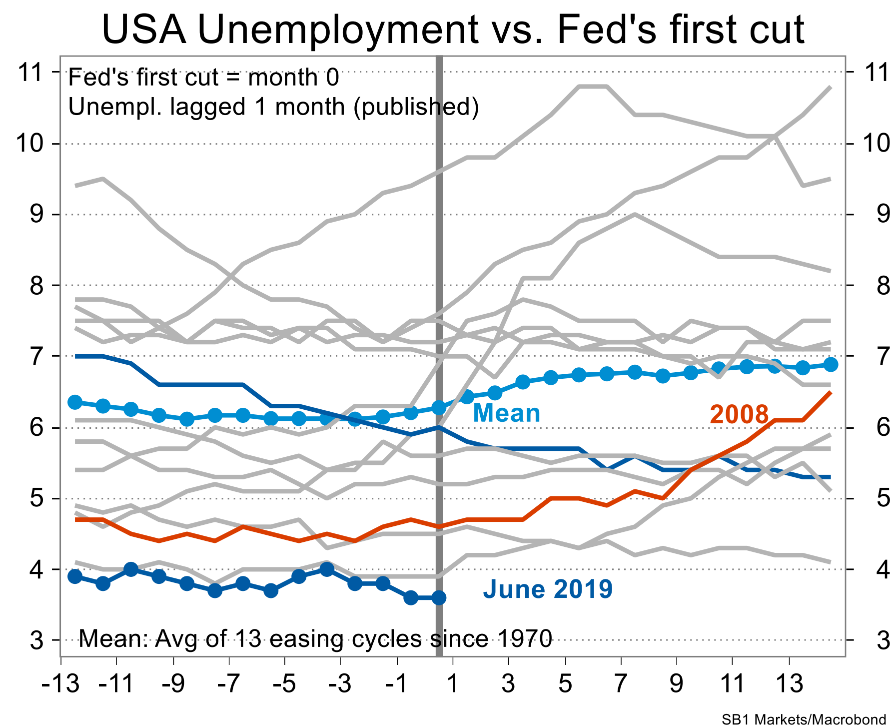


- **Employment** rose by just 75’ in May, 100’ below expectations, which were shifted down as the ADP data pre-warned the slowdown. Moreover, April was revised down by 60’, the avg of the two months is a moderate 140’ rise. The 6m average growth rate has fallen to 1.4% from close to 2%, employment growth is no doubt slowing. Nonetheless, over the past months employment has been expanding at a solid speed, which will not lead to a higher unemployment rate
- **The unemployment rate** held steady at 3.6%, the lowest rate since 1969 – and the trend is still down
- The labour market **participation rate** was unchanged at 62.8%, the upswing late last year into Q1 has completely reversed and the trend is flat. The labour market is tight but the aggregate supply side is not responding. The employment rate held steady at 60.6%, and has been more or less stable recent months
- **Wages** rose just 0.2% m/m in May, 0.1 pp less than expected. The annual rate inched down to 3.1%, wage inflation has eased somewhat recently. Still businesses are reporting lack of labour, like never before
- **These data do not by themselves justify an interest rate cut, and Fed will have to see a more sustained labour market weakness before using the labour market as an easing argument. Wage inflation is not dangerously low**

When can the Fed start cutting: It could, now

In average, Fed waits until uemployment has edged up but often before any weakness is seen

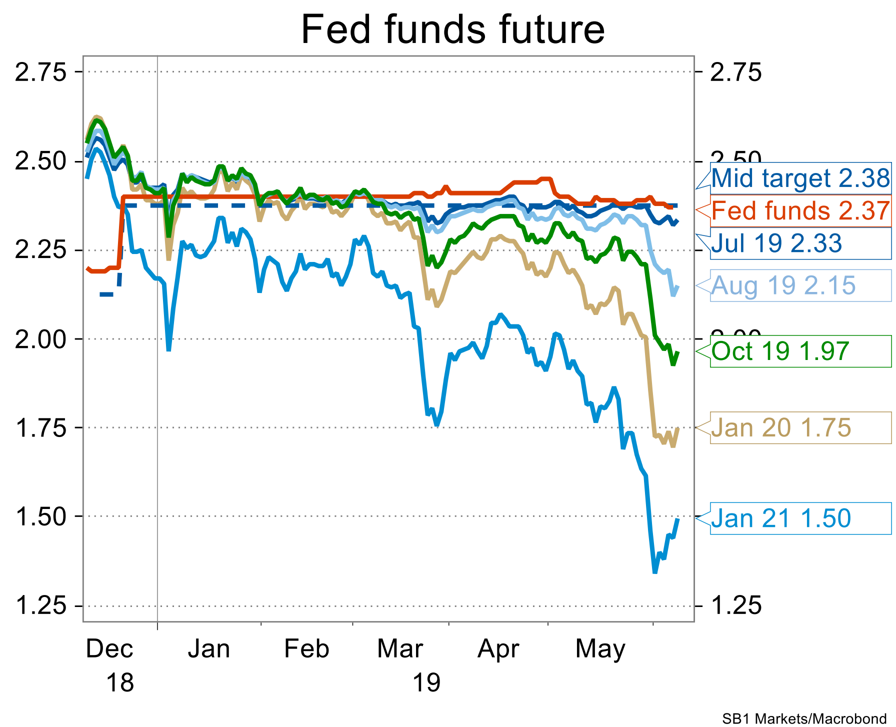




Fed's Beige Book reports slightly higher growth, no support for a Fed cut

Fed's 'regional network' reports tight labour markets but subdued wage inflation in April/May

- Economic activity expanded at a '*modest*' rate in the six weeks up to mid-May, a marginal increase from the '*slight to moderate'* speed in the previous report
- Manufacturing reports were mixed, some reported uncertain outlook, although the overall assessment was positive. Does not confirm the rapid slowdown which some surveys have found
- Household consumption is growing modestly but many Districts reported weaker auto sales
- All districts reported increasing employment, however, employment growth is constrained by widespread labour shortages. Businesses reported some wage pressure but overall wage growth remain modest (strange, given tight markets)
- Prices continued to grow at a 'modest' pace. As in the prior survey, several Districts reported that input prices are rising faster than prices at the consumer level
- **In total, the Beige book noted a somewhat more upbeat outlook than in the previous 2019 reports and does not indicate that the recent weakness in manufacturing and consumption will deteriorate. An argument for a patient Fed!**



Fed Fund market rates have 'collapsed' recent months, recovering somewhat the past days due to the US-Mexico agreement. The market puts a 16% probability for a rate cut at the Fed meeting next week. However, the market assumes a cut before or on the Sept meeting to 92%, most likely down in total of 50 bps (one cut in July and one in Sept)

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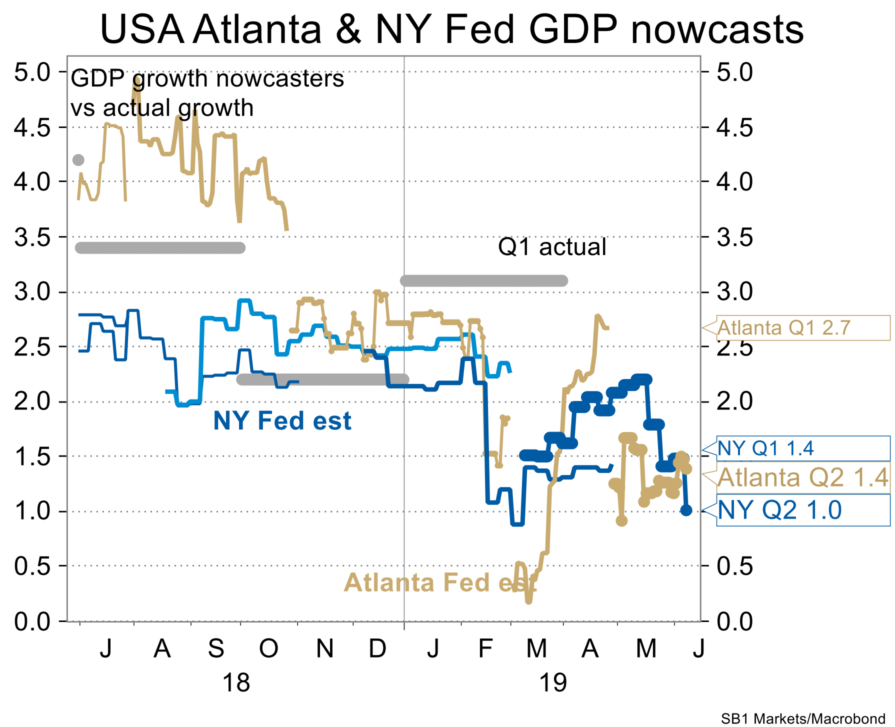
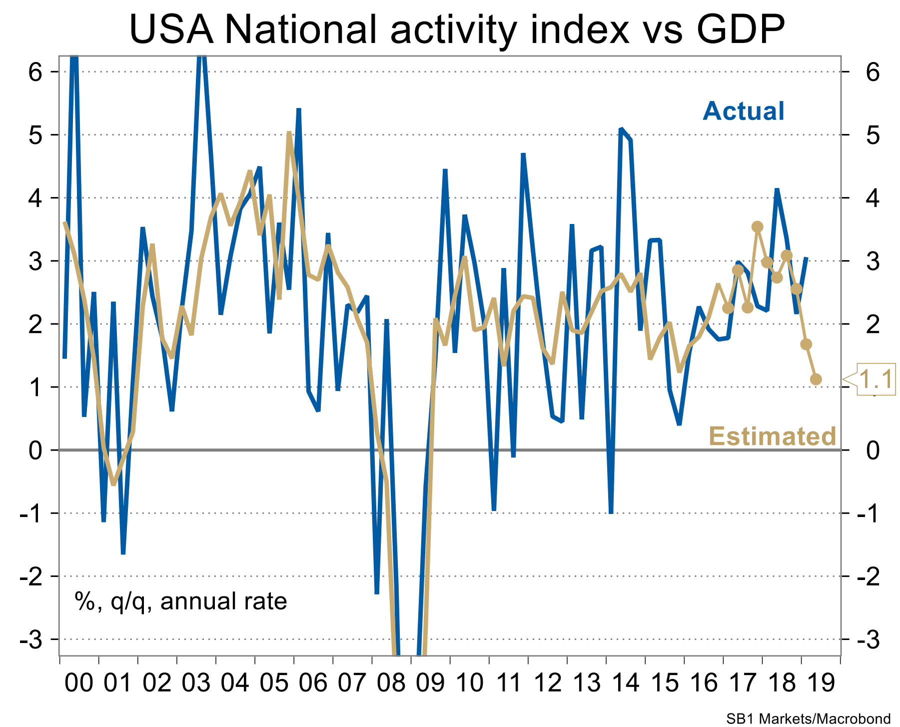
All nowcasters are finding a slowdown in Q2, to 1-1.4%

The nowcaster models are well aligned this time. And they may be right





- The Atlanta Fed nowcasts marginally down last week, the NY Fed model more sharply, 0.4 pp to 1.0%, the lowest estimate so far. The National Activity Index was more downbeat in April, suggesting just 1.1%

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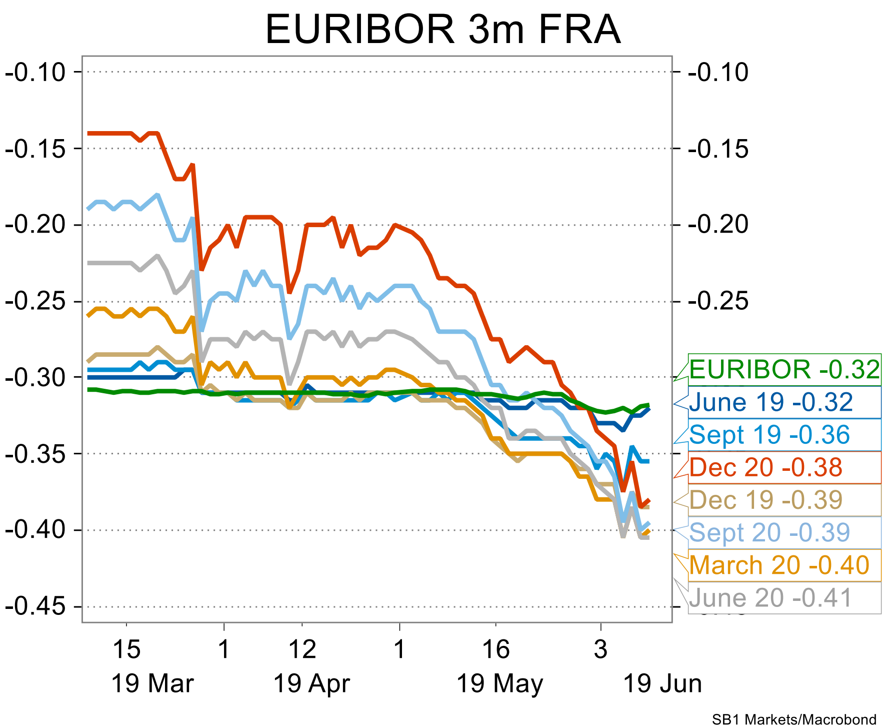
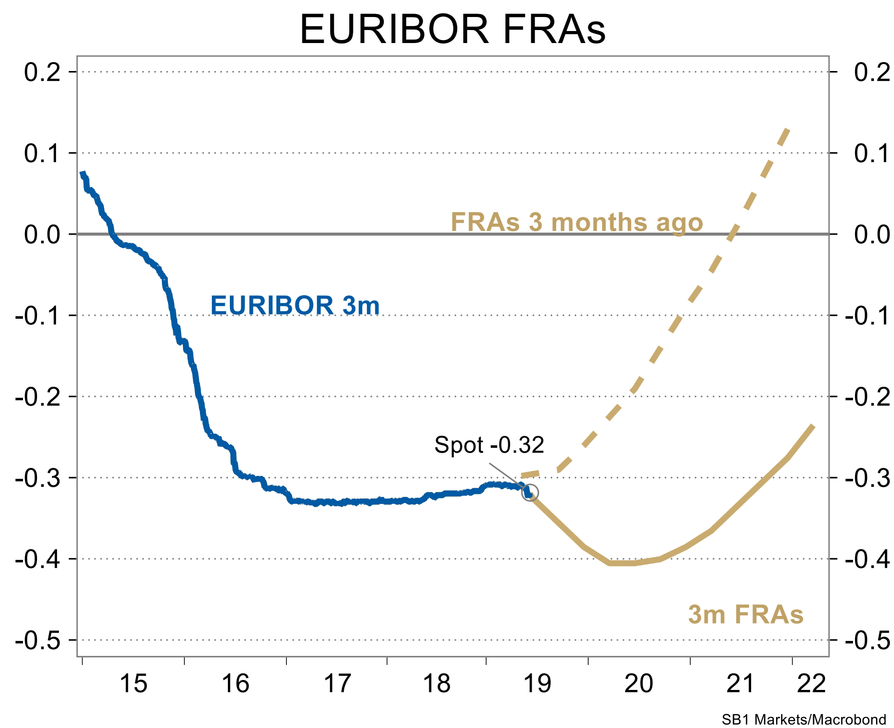
ECB postpones the first hike to H2 2020, stresses readiness to act

The new version of the TLTRO funding vehicle more generous than expected, more bank liquidity





- The soft turn did not surprise markets, which had been starting to consider an interest rate cut (in fact, more was expected, thus, interest rates increased following the announcement) but then fell in sympathy with US rates following the weak US job report. The market is now pricing some 28% probability of a rate cut in '19. The details for the new TLTRO, long term funding for lending for banks was more generous than expected, and banks will most likely utilize the funding vehicle
- Mario Draghi noted that the extension of the current interest rate is a result of acknowledgement of risk due to increased and prolonged uncertainties. At the meeting, several Board members raised possibilities of further expansionary measures such as rate cuts and expansions of QE, and Draghi stressed that the ECB is ready to act if needed.
  - » As expected, the ECB acknowledges that data inflows are on the weak side and indicating a soft Q2. Still, the GDP f'cast for 2019 was nudged up by 0.1 pp (due to higher Q1 growth) and the 2020 f'cast down by 0.2 pp. Core inflation is still expected to pick up

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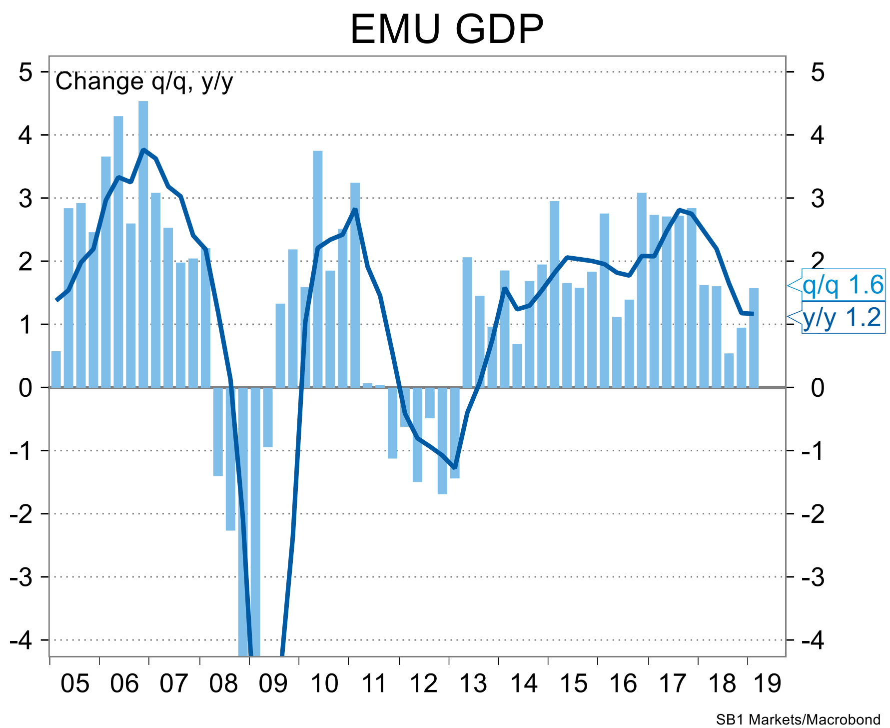
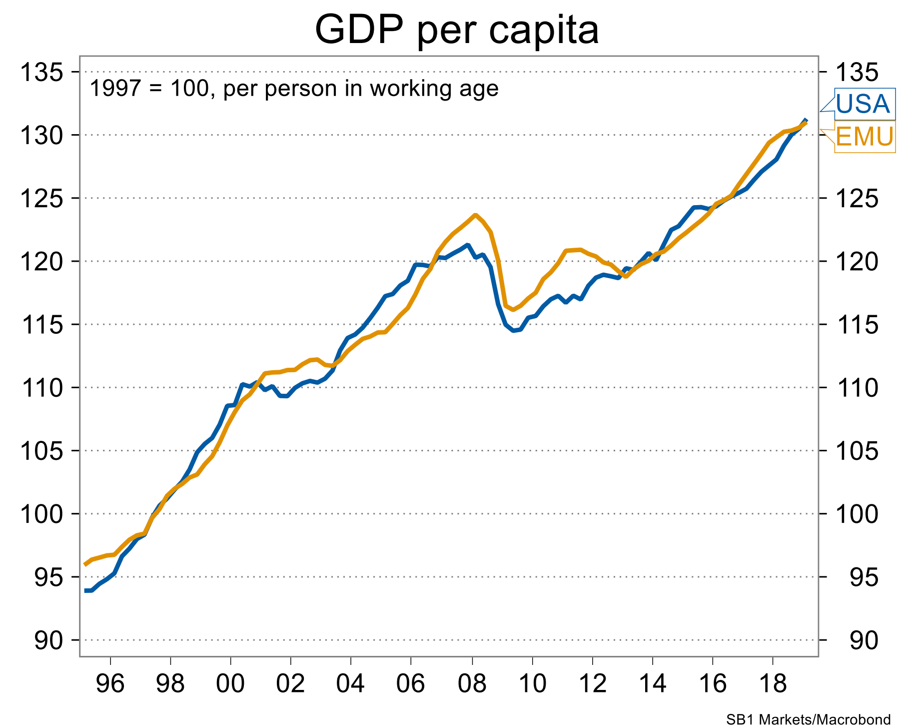
GDP growth confirmed at 1.6%, driven by rising domestic demand

Q1 growth was unchanged in the 3rd release. Fundamentals are solid, just inventories fell

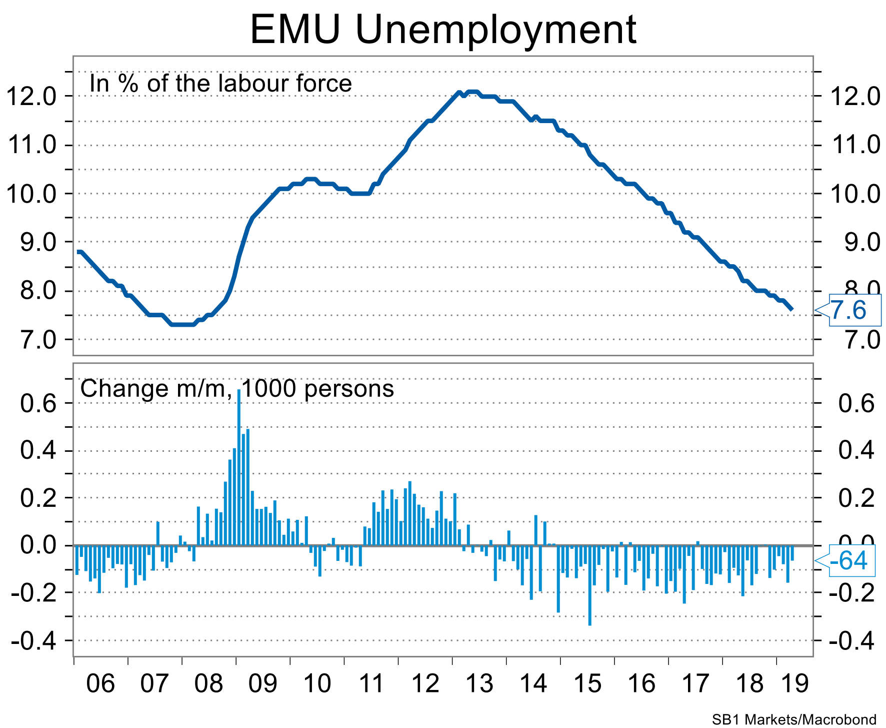


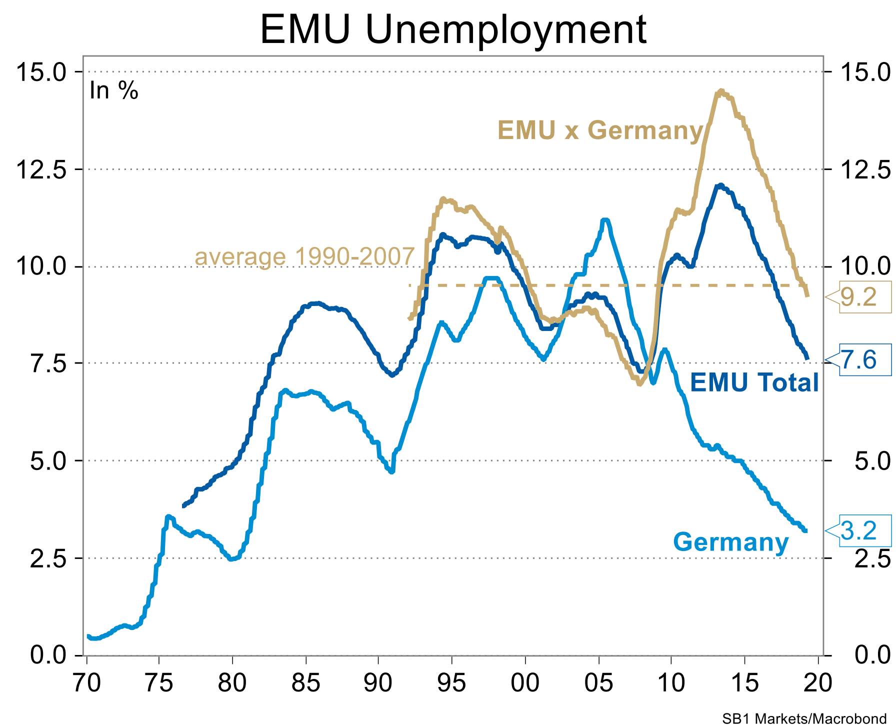


- GDP growth accelerated in Spain, Germany and Italy (which came out of the 'technical recession'), slowed in France
- GDP per capita in working age grew marginally slower in the Eurozone than in the US in Q1. Growth in GDP per capita has been higher in the US than in the EMU two past years, However, if we adjust for the change in the structural budget deficit (the fiscal impulse), the 'real' growth has been far higher in EMU the past years than in the US. Since mid 1990'ies we are not able to spot any material difference. Are you?

Unemployment one tick down in April, at 10 ½ y low

Unemployment edged down to 7.6%, below f'casts. A promising sign or a lagging indicator?



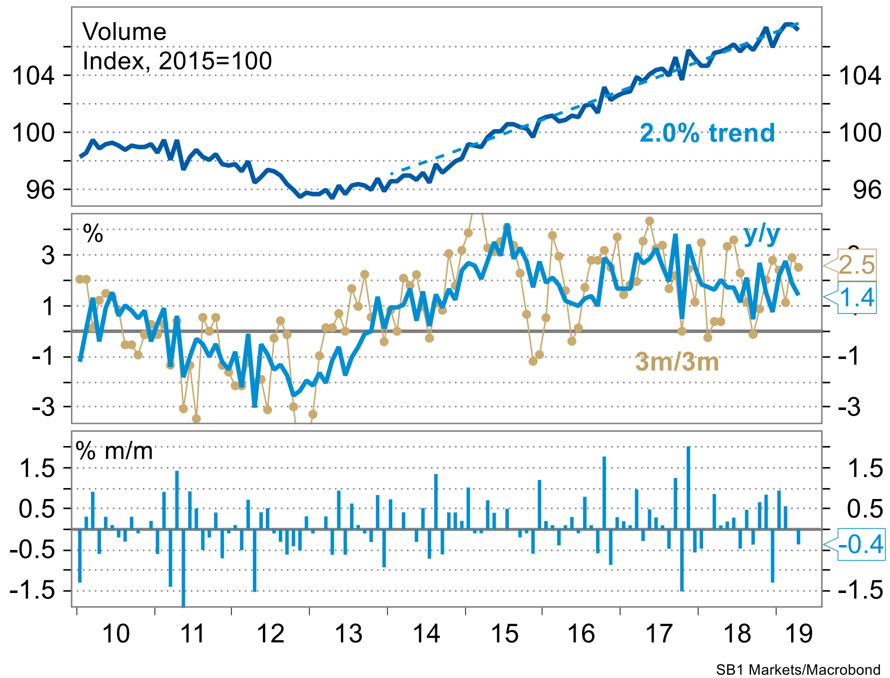


- The unemployment rate fell 0.1 pp in April, was expected unchanged at 7.7%. The number of unemployed fell by 64' persons,a modest decline after a steeper drop the prior month. Thus, there are no indications of a weakening labour market in spite many soft data points. Regrettably, unemployment is not a leading indicator, it is at best a coincident one
- Unemployment in total EMU is well below the 1990-2007 average, and it has fallen just below the average in EMU ex Germany too; Italy & Greece are above avg, the others below pre-2007 avg
- In Germany, the unemployment rate was flat at 3.2% in April, and is at the lowest level in 38 y

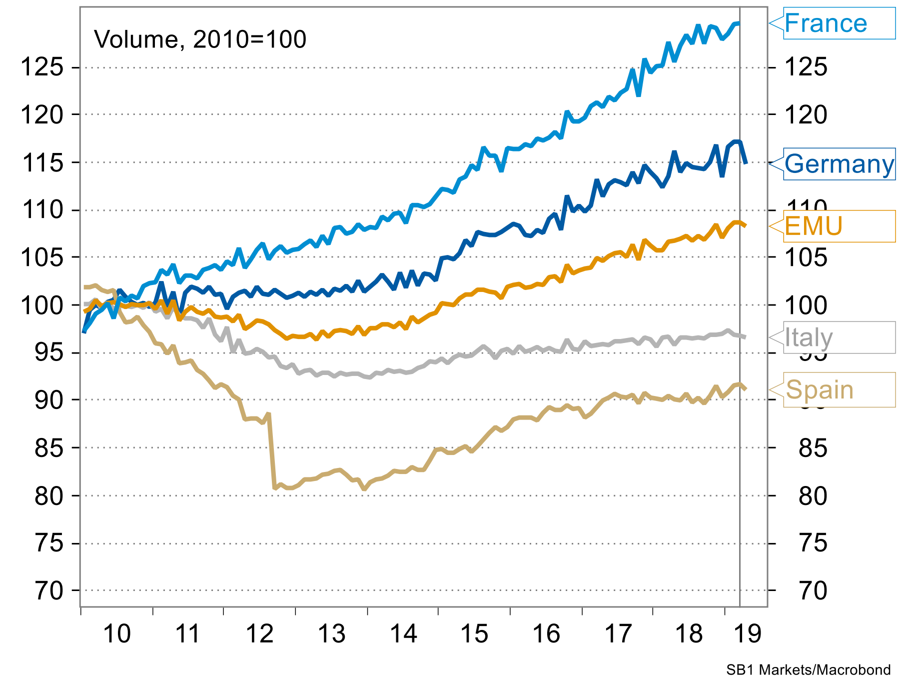
Retail sales down in April, still on a decent growth path

Retail sales down 0.4% in April, the speed into Q2 is not impressive, after a solid Q1

EMU Retail sales



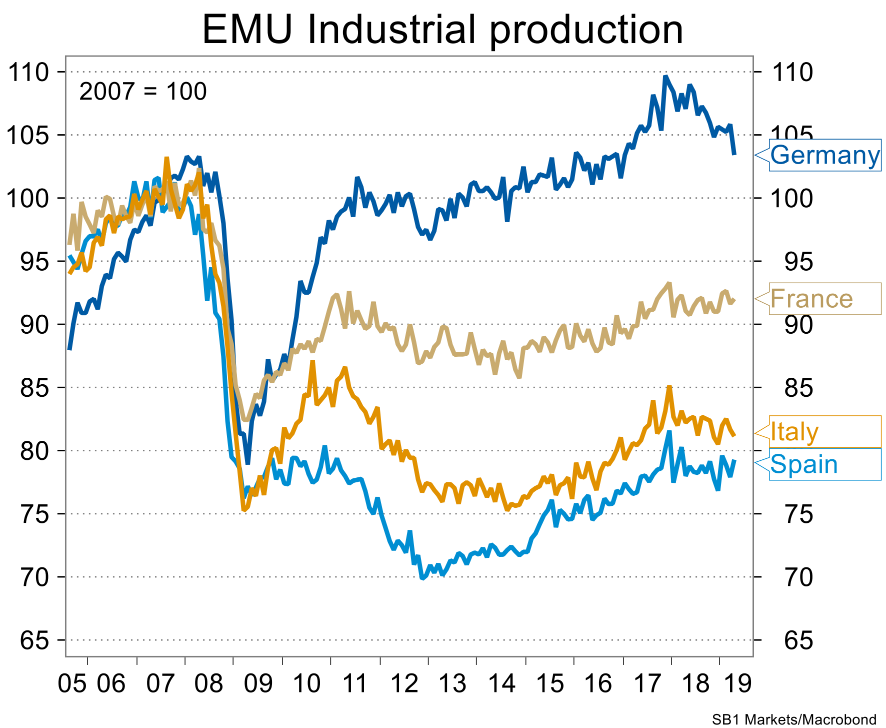
EMU Retail sales

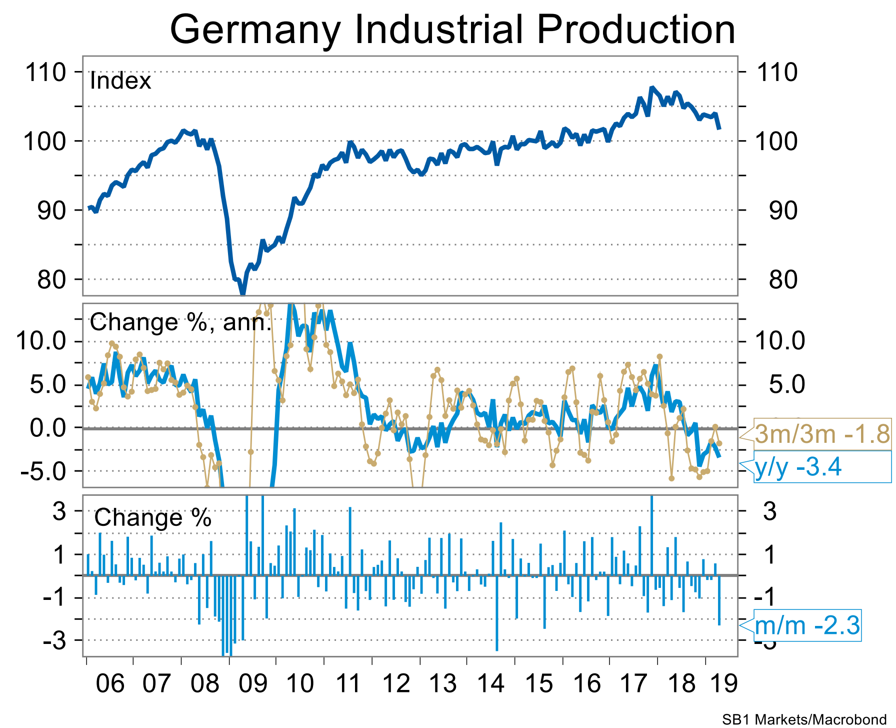


- Retail sales volume ticked down 0.4% m/m, as expected. Underlying growth (3m/3m) slowed to 2.5% and Q2 is off to a soft start, the speed into the quarter is -0.7% annualised, following the 2.9% Q1 growth rate. However, the 2% trend growth is still intact, not bad during these days of acute angst of the European economy
  - » The decline was supported by a slip in German sales. Sales in France have flattened out recently, Spain trending up, Italy not impressive
- Decelerating total inflation as well as retail price growth have helped purchases. Moreover, real wages and employment are increasing and consumer confidence is not weak, signals decent growth in consumption going forward

German industrial production tumbled in April, EMU probably down 0.7% m/m

Production plunged 2.3% in Germany, an upswing in Spain and France can not save total EMU prod.

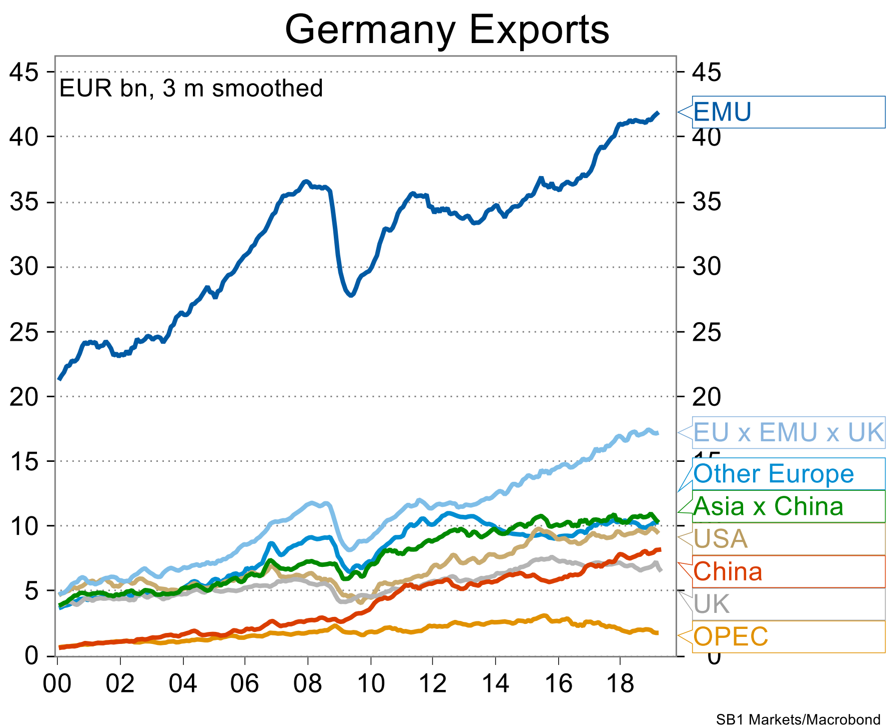


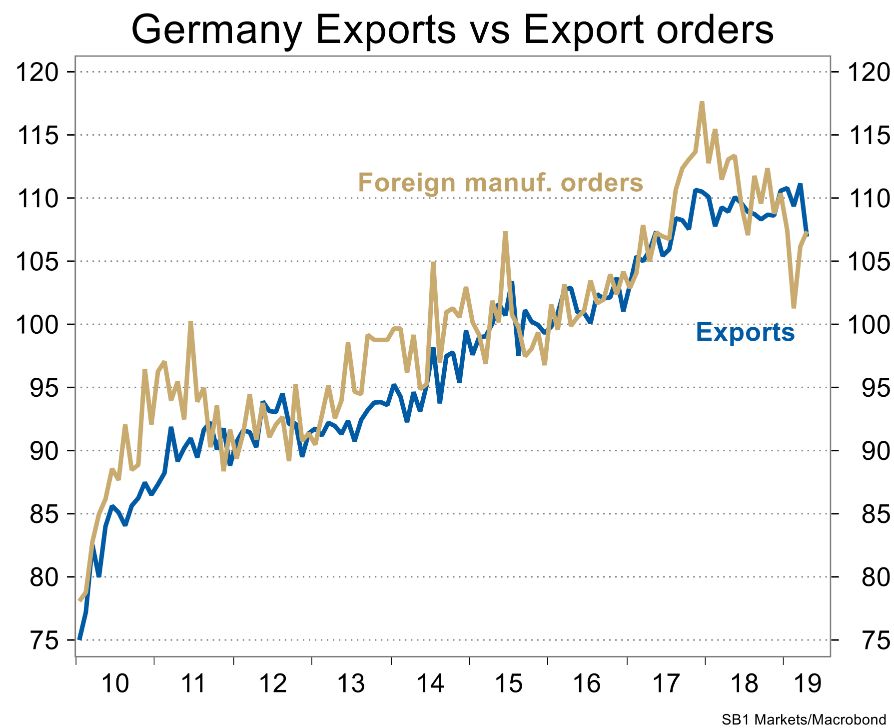


- The contraction in German industrial sectors accelerated in April, the 2.3% drop was much worse than expected. Annual rate down 3.4%. However, manufacturing production (which excludes mining and electricity production) rose 0.1% m/m, though following a huge decline in March, and the 'story' is the same
- Production in France rose modestly at 0.4%, Spain bounced back up (an 1.8% increase), both trending more or less flat. In Italy, production fell again – and the trend is down
- We assume a 0.7% decline in total EMU industrial production (ex construction), based on the data released this far
  - » Unfortunately, PMI and manufacturing orders do not signal any recovery in Eurozone manufacturing, check the next slide for German order inflows

Export data still OK in most directions, China in the lead exports to the UK down

No April data on most countries but UK plunged (Brexit disruptions), others must have fallen too

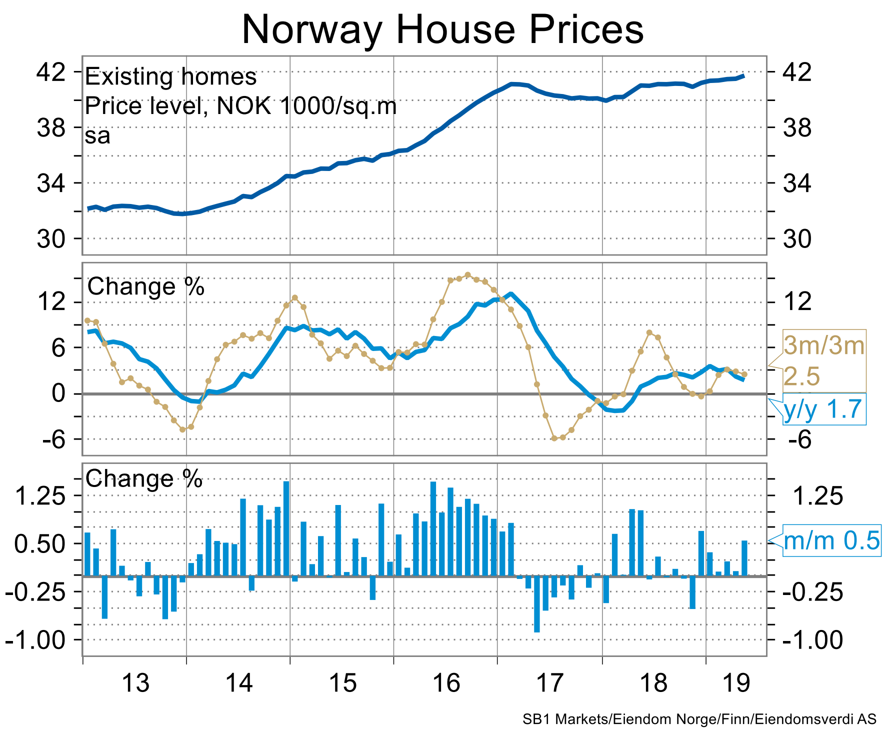


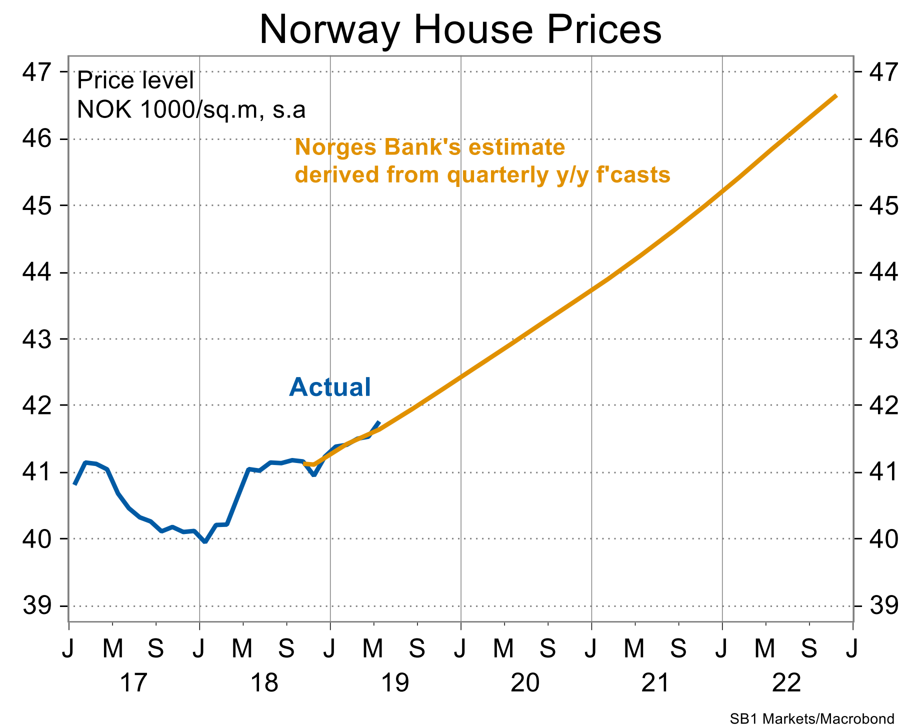


- The direct impacts of the trade war is not easy to find; and German businesses have anyway not been much directly hurt anyway. Surveys/orders are signal than somewhat else have been happening: A retreat in business investments, due to trade war/Brexit uncertainties and probably also a 'normal' mature cycle. Most likely, businesses are holding back their purchases due to increasing global uncertainties
- Exports to UK slipped in April, as businesses there are cutting back purchases after a huge stockpiling ahead of the prior Brexit deadline. Exports to the US is still trending up (no April data), and exports to China are increasing at a fast pace. Exports to other EMU partners have also strengthened recently (no April data), exports to other Europe mixed. Exports to Opec have been the weak link recent two years
- Germany's main export markets: The other EMU countries (38%), other EU countries x UK (16%), Asia x China (10%), Europe x EU (9%), USA (9%), China (7%), UK (6%)

House prices rose more than expected in May, in spite soaring supply

Prices up 0.5% s.a in May, we expected 0.2%. However, market dynamics indicate muted growth



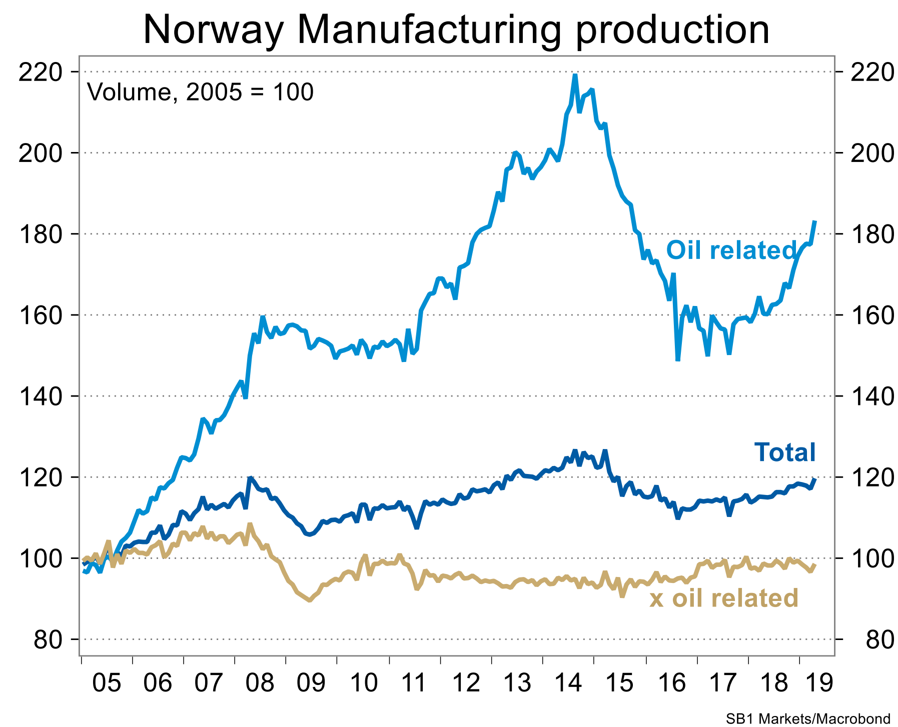


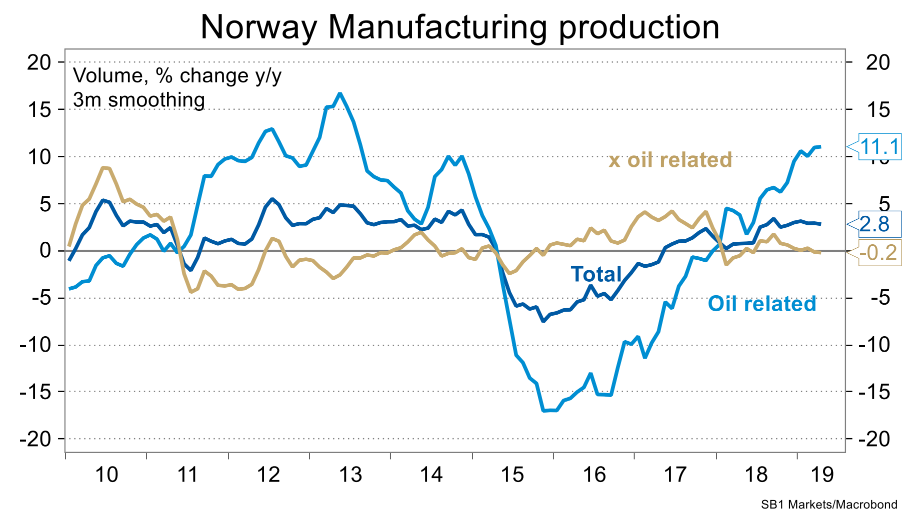
- **House prices** climbed 0.5% m/m seasonally adjusted in May (0.7% unadjusted), 0.3 pp above our f'cast. Underlying growth has flattened out at a 2.5% speed recent months (measured 3m/3m). The annual growth rate fell to 1.7%. Prices are marginally above Norges Bank's path
  - » A broad upswing in May; prices rose m/m in all regions ex Follo. Recent months, prices have fallen in East Norway x Oslo/Akershus, climbing in others
- **The inventory of unsold homes** is soaring, the highest in 10 years. The high inventory is not due to lack of demand but to a steep rise in the number of new listings (of existing homes). The number of transactions is trending steeply upwards, reflecting brisk demand
- **Still, short term dynamics signal slow/zero price growth the coming months. And interest rates are on the way up, limited upside!**

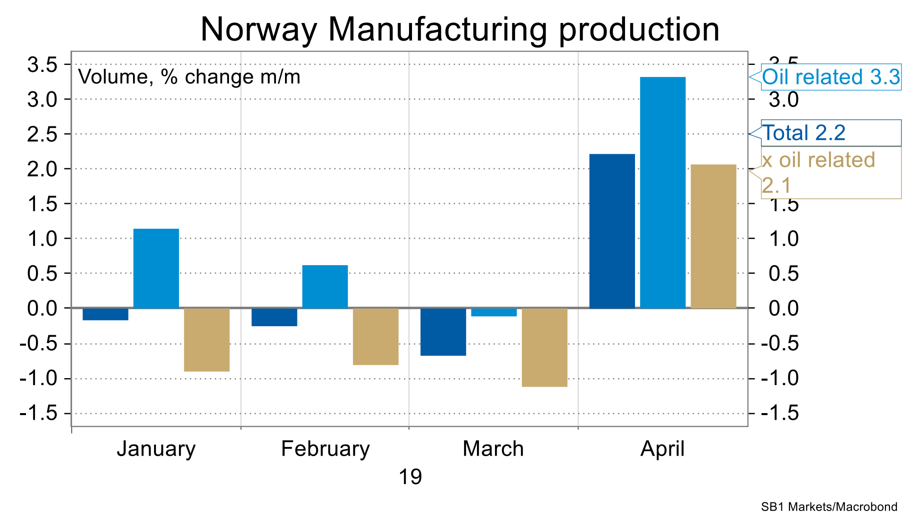
SpareBank 1 MARKETS

Manufacturing production surprisingly spiked in April

Production up 2.2%, strong growth in both oil- and non-oil related sectors. Oil related is soaring



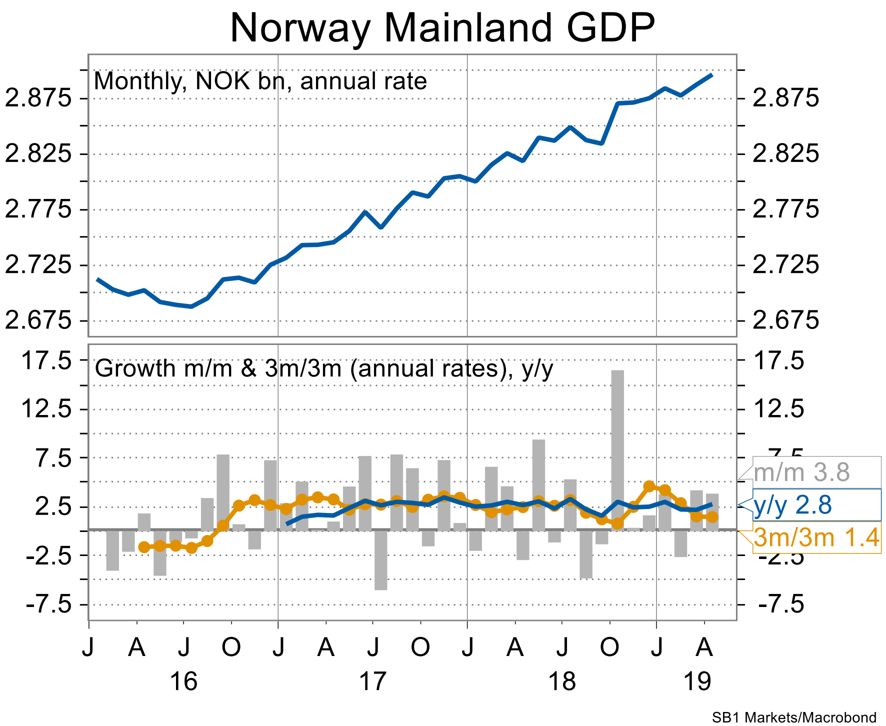




- Total manuf. production surged 2.2% in April, well above f'casts at 0.4%, following some soft months. Production is up 2.8% y/y (smoothed), a solid pace. Surveys indicate that growth may be peaking now
- Oil-related manufacturers reported a 3.3% jump m/m, the highest in 1 ½ years. Oil companies indicate that growth will continue to accelerate in 2019 and into 2020
- Non-oil related sectors noted a solid 2.1% lift, production has been completely flat the past 2 years

Moderate GDP growth in April, the speed into Q2 is some 2%

GDP rose 3.8% annualised in April, underlying growth is so far modest at 1.4%



- Mainland GDP rose 0.3% m/m in April, 3.8% ann. rate
  - » The monthly data are too volatile to give us any useful signals, the more important 3m/3m rate came in at 1.4% annualised, dampened by a weak February
  - » The speed into Q2 is 1.9%, and that is if we assume zero growth in May and June. Most likely, growth will end up higher than this
  - » Norges Bank's March f'cast is a 3.1% annualized speed in Q2
  - » GDP is up 2.8% from April last year
- On the demand side:
  - » Private consumption has gained some speed the past 2 months and is running at a 3% growth rate. The uplift is partly due to a spike in auto sales in March (Teslas) but spending kept up in April
  - » Mainland business investments accelerated in April, after slowing in the first months of 2019
  - » Thus, total private Mainland demand is improving somewhat
  - » Oil investments were revised sharply down in Q1 (as we assumed) but April was much stronger than we expected. Q2 will most likely be very strong!
  - » Housing investments are growing at a modest pace
  - » Mainland net trade is pulling growth down, due to soaring imports
- So what?
  - » Norges Bank's Q2 GDP f'cast at 0.8% q/q is still within reach (if electricity prices normalises), and the Bank anyway does not put much weight on these monthly data. A June hike is a done deal and we expect an upward revision of the interest rate path, primarily in 2020, even if rates are sharply down abroad

The Calendar

In focus: China May data, US inflation, retail, manufacturing, Norges Bank Reg. Network, inflation

Time	Country	Indicator	Period	Forecast	Prior
TBA	CH	Aggregate Financing CNY	May	1410.0b	1360.0b
Tuesday June 11					
08:00	NO	CPI Underlying MoM	May	0.1%(0.1)	0.5%
08:00	NO	CPI Underlying YoY	May	2.6%(2.6)	2.6%
10:00	NO	Norges Bank Regional Network	May	(1.35)	1.46
10:30	UK	Average Weekly Earnings YoY	Apr	3.0%	3.2%
10:30	UK	ILO Unemployment Rate	Apr	3.8%	3.8%
12:00	US	NFIB Small Business Optimism	May	101.8	103.5
14:30	US	PPI Ex Food, Energy, Trade MoM	May	0.2%	0.4%
14:30	US	PPI Ex Food, Energy, Trade YoY	May	--	2.2%
Wednesday June 12					
01:50	JN	Core Machine Orders MoM	Apr	-0.8%	3.8%
03:30	CH	CPI YoY	May	2.7%	2.5%
08:00	NO	New Home Prices	1Q		
10:30	NO	Homebuilders' Survey	May		
14:30	US	CPI Ex Food and Energy MoM	May	0.2%	0.1%
14:30	US	CPI Ex Food and Energy YoY	May	2.1%	2.1%
20:00	US	Monthly Budget Statement	May	--	$160.3b
Thursday June 13					
06:00	SW	PES Unemployment Rate	May	--	3.5%
11:00	EC	Industrial Production MoM	Apr	-0.4%	-0.3%
14:30	US	Initial Jobless Claims	Jun-08	215k	218k
Friday June 14					
04:00	CH	Investments YTD YoY	May	6.1%	6.1%
04:00	CH	Industrial Production YoY	May	5.4%	5.4%
04:00	CH	Retail Sales YoY	May	8.0%	7.2%
09:30	SW	CPIF Excl. Energy YoY	May	1.5%	1.6%
14:30	US	Retail Sales Advance MoM	May	0.7%	-0.2%
14:30	US	Retail Sales Core (Control Group)	May	0.4%	0.0%
15:15	US	Manufacturing Production	May	0.2%	-0.5%
16:00	US	U. of Mich. Sentiment	Jun P	98	100

- **China**
  - Data from China are mixed; **manufacturing production** is slowly accelerating and **investments** are growing steadily, suggesting that the stimulus measures are boosting activity. On the other hand, **retail sales** are softening and **credit growth** have eased the two last months. Both exports and imports are trending up. PMIs noted a slower pace of expansion in May but no rapid downswing. Also, a drop in May last year may help the annual rate on retail sales up this month
- **USA**
  - **CPI inflation** is losing some steam, even if trend was above trend. However, growth is slowing; PMI/ISM price indices have fallen sharply
  - **Retail sales** are slowly recovering from the December slump. Consumer confidence, total disposable income indicate an uplift
  - **Manufacturing production** is cooling, surveys are mixed but in sum pointing to a rather bleak outlook. Downside risks!
- **Eurozone**
  - **Industrial production** is struggling, we f'cast a 0.6% decline m/m
- **Norway**
  - **Norges Bank's Regional Network** will continue to note solid growth and increasing capacity constraints in Q2. Our take is that there is a limited upside from the very upbeat Q1 survey, we expect a small downward adjustment, as some other surveys have signaled. Not even a steep slowdown could Norges Bank from hiking on June 20
  - **Core CPI inflation** accelerates and is well above the price target. We expect an unchanged core annual rate at 2.6%

SpareBank 1 MARKETS

Our main views

	Main scenario	Recent key data points
Global growth cycle	The cycle is maturing, in the real economy, markets. Rich countries (DM) in the lead, more to go in most EM. Unemployment is low, wage inflation on the way up, not low vs. productivity. Most emerging countries (EM) x China are in recovery mode. Some hotspots EM will get burned, as usual – but there are fewer EM imbalances than normal. Barring policy mistakes, the global economy is not yet rigged for a *hard* downturn	<u>Global composite PMI fell 0.9 p to 51.2 in May, 0.3 p weaker than we expected. Signals below 3% growth.</u> The US-China trade negotiations and the Mexican debacle will be in focus the coming weeks too
China	The governments' stimulus measures may have turned the growth momentum, at least that's what some of the data indicate. The invest/GDP ratio is declining rapidly. Debt growth has slowed, and will not accelerate much even if authorities are now, probably successfully, stimulating to counter negative impacts from the trade war/prev. tightening. Fiscal policy is also activated. Exports to US (net of interm. imp) approx 2% of GDP, and a 10% decline here is manageable. However, a full scale tech/trade war will be bad, a deal with US is important	<u>Mixed composite PMIs, Markit's dropped on slower activity in service sectors. The avg of the two composite PMIs do not point to any abrupt downswing Chinese economy. Both exports and imports volumes are trending up from the Q4 slump</u>
USA	Growth is now slowing substantially, from an above trend level. Employment growth has come down too but is still not too low, and unemployment is trending down while wage inflation has slowed. No serious overinvestments but most sectors at/above trend, and housing is still exposed but recent data have been OK. Household debt 'low' – and the savings rate is OK, limited consumption risk. Corporate debt might become a challenge. Fiscal stimulus continues into '19, but not by much. The deficit is far, far too high, given the low unemployment rate. <u>Recession risk is increasing, but still not overwhelming, short term, and a dovish Fed may give some support. **Risk: Trump/trade/bus invest.**</u>	<u>Employment rose much less than expected, up just 75'. Wage inflation eased, unemployment held steady at record low 3.6%. Compensation plans up. Manufacturing ISM is nosediving, non-manuf. was more upbeat but the ISMs are anyway adding to signs of a rapid slowdown. Both imports and exports fell in April.</u>
EMU	Growth has slowed and recent manufacturing data are worrying. The labour market is still tightening, and labour cost infl. back to a normal level. Investment ratios on the way up but are not too high. Credit growth still muted. Household savings are high, and consumption has kept up well. Policy risk: Trade war, populist revolt. Italy 'saved' now, not forever. <u>Even without obvious recession triggers, weak short term data signals a substantial risk for a downturn</u>	<u>Mixed data: Q1 GDP details were strong and unempl. keeps falling. Retail sales fell but are not that weak. The manufacturing contraction is deteriorating, German data are weak. Inflation down. ECB is ready to act</u>
Norway	Growth is and will remain above trend – and unemployment declines further. Oil investments have more to go (we have revised our f'cast up). Mainland business inv. not low anymore, risks balanced. Housing investments have bottomed, for now. The labour market is not tight yet, but wage inflation is accelerating, no reason to expect much lower core CPI infl. Electr. prices will stabilise (at least), headline CPI will come down. Credit growth almost kept at bay just due to regulations.	<u>House prices are rising moderately but the inventory of homes for sale is surging. Manuf. production gained speed in April. PMI is at a decent level. SSB f'casts a continued moderate economic upswing</u>

Colour codes: Green=more to go. Yellow=the cycle is maturing, close to peak. Orange=at peak, downside risk. Red=recession level

In this report

Global PMIs + Auto sales

- The world is more disappointing, due to the US, Emerging Markets
- Global PMI plunged to 51.2 in May, signals below 3% global GDP growth
- A broad slowdown in May, DM growing at the softest pace in 6 years, EM down too
- Composite China PMIs softened, trending up
- US Manufacturing ISM another step down in May, below expectations
- Non-manufacturing ISM gained in May
- Final EMU PMI: Composite PMI slides down
- USA auto sales up in May, marg. down in EMU

China

- Exports were stronger, imports lower but both now trending up again

USA

- Employment stalled in May and wage growth eased, may be a sign of slowdown
- Wage growth is cooling somewhat, the 3rd month of deceleration
- Fed's Beige Book finds slightly higher growth, no support for a Fed cut
- Both exports and imports fell in April, Q2 off to a weak start
- Household credit slows, at a low level, corporate debt growth flat at a high level
- All nowcasters are reporting a slowdown in Q2
- US Indicators: Still no recession signal

EMU

- ECB postpones the first hike to H2 2020, stresses readiness to act, more bank liquidity
- GDP growth confirmed at 1.6%, driven by rising domestic demand
- Unemployment one tick down in April, 10 y low
- Core CPI inflation slumped to 0.8%, partly due to calendar effects
- Retail sales softened in April, still on a decent growth path
- German industrial production tumbled in April, EMU probably down 0.7% m/m
- German manufacturing orders fail to recover
- German exports nosedived in April, confirming weak surveys

UK

- Manufacturing production down 4%, destocking

Norway

- House prices rose more than expected in May, in spite soaring supply
- Households' savings increased in Q1, bottomed out for now?
- Manufacturing production up in April
- Moderate GDP growth in April, the speed into Q2 is some 2%
- Current account surplus inched up in Q1, on higher capital income

SpareBank 1 MARKETS

Highlights

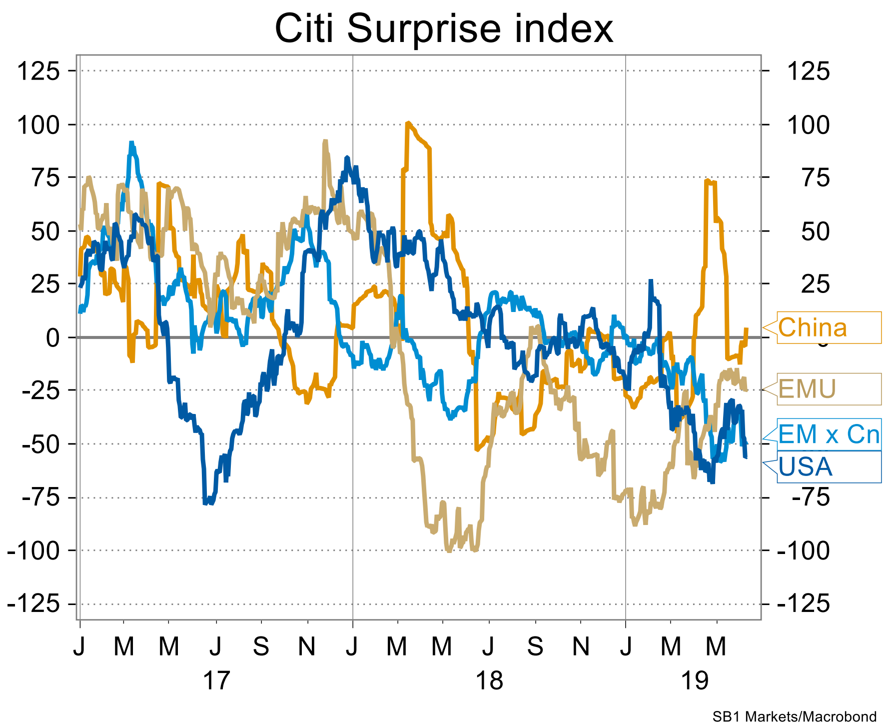
The world around us

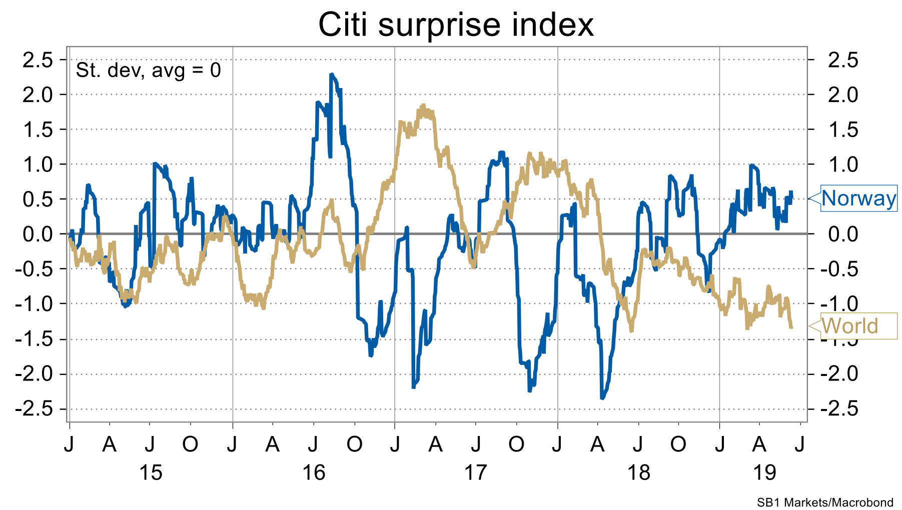
The Norwegian economy

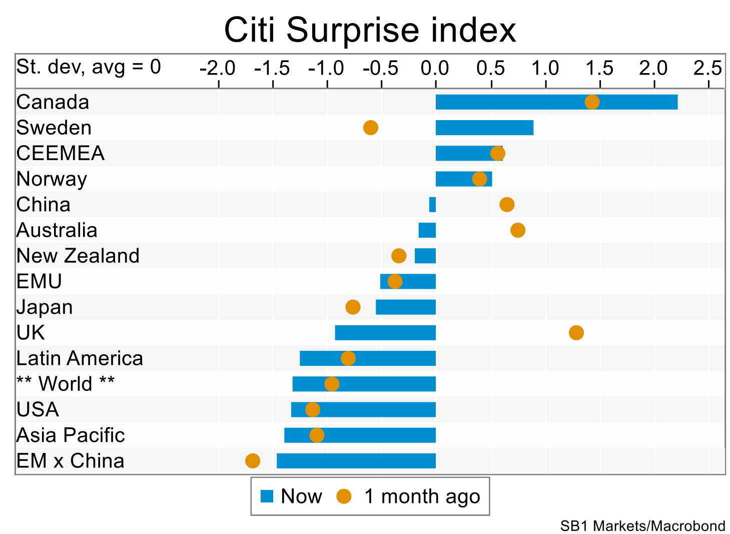
Market charts & comments

The world surprises even more on the downside, due to the US, EM

China close to neutral, EMU stable and not too weak





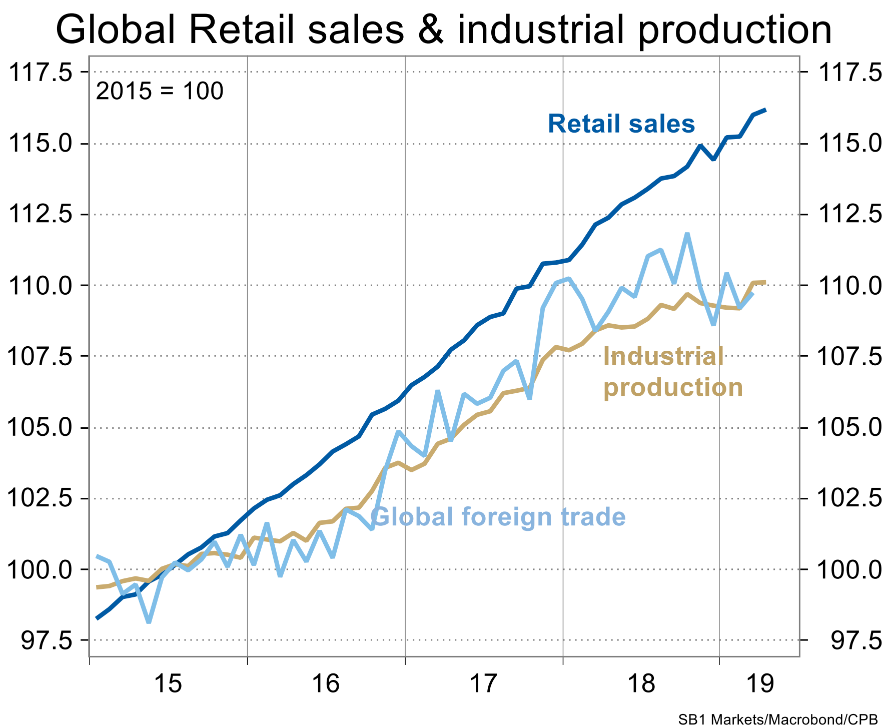


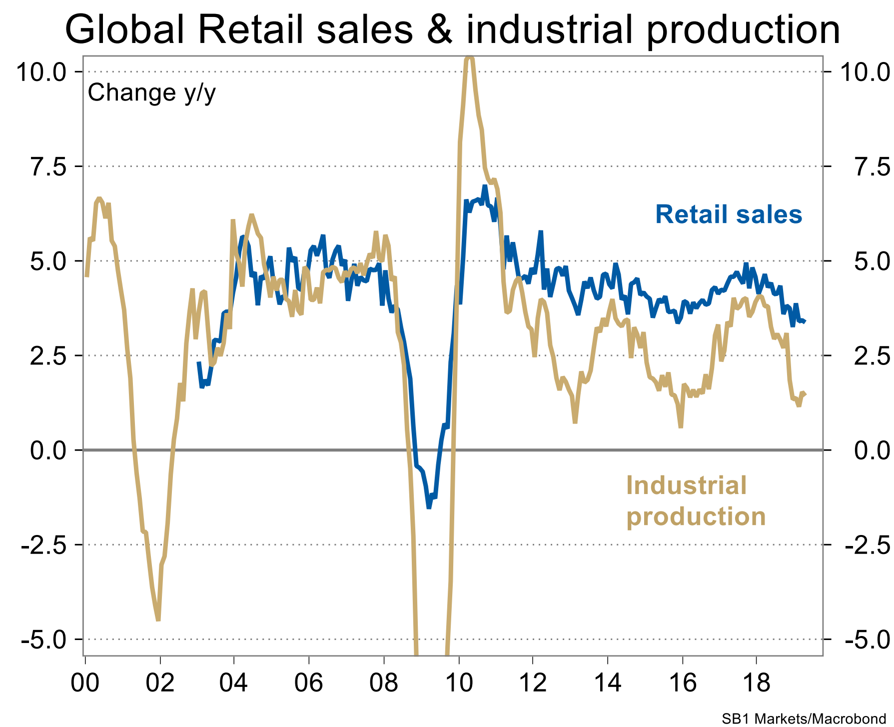
- The global surprise index has been in negative territory since last spring
- The US and EM x China are the most disappointing and both slid down last week, primarily due to weak PMIs/ISMs. Regardless, we do not judge US data to be this weak
- Chinese data are close to neutral territory, following some extreme volatility
- EMU stable vs expectations, data have not deteriorated lately (until Friday)
- Norwegian data further above par, together with Canada, Sweden and UK (!)

Surprise-indices measure the difference between economists' expectations and the actual outcome over a 3 month rolling window

Retail sales still growing but slower, manuf. prod gained speed in March/April

Still, manufacturing production has been flat the previous months. Foreign trade weak too

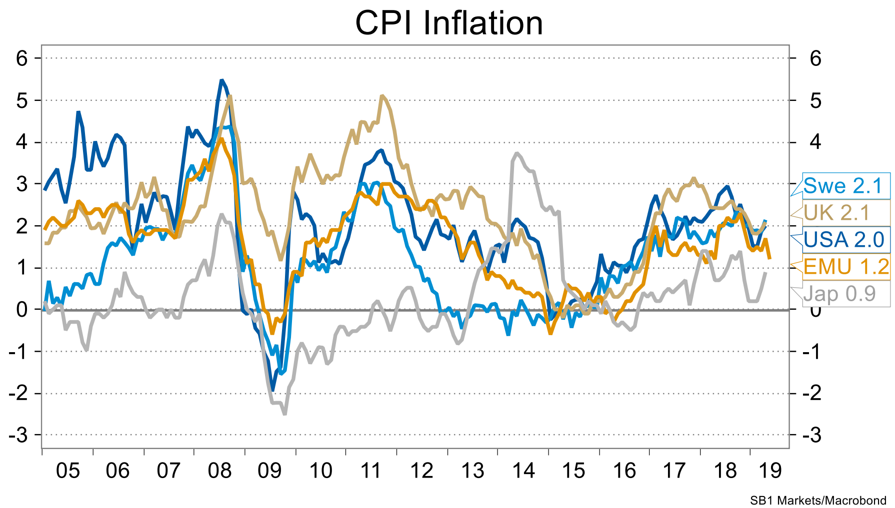


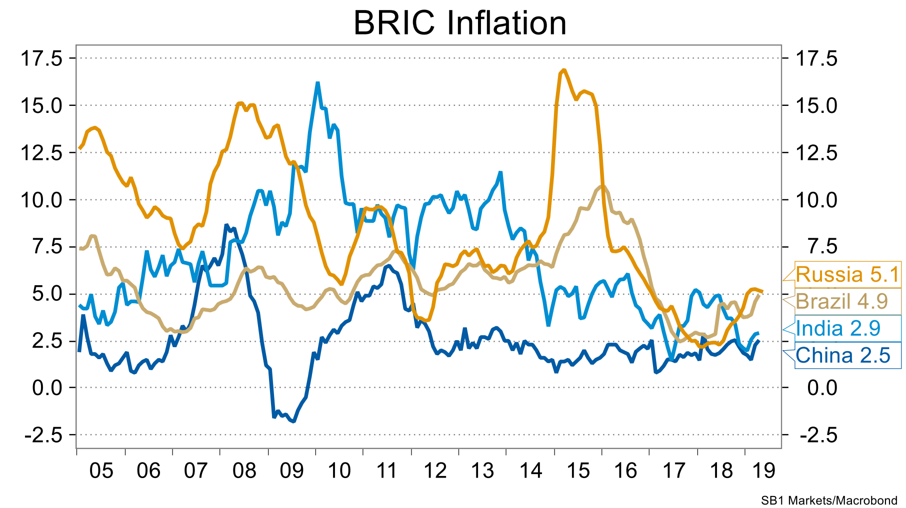


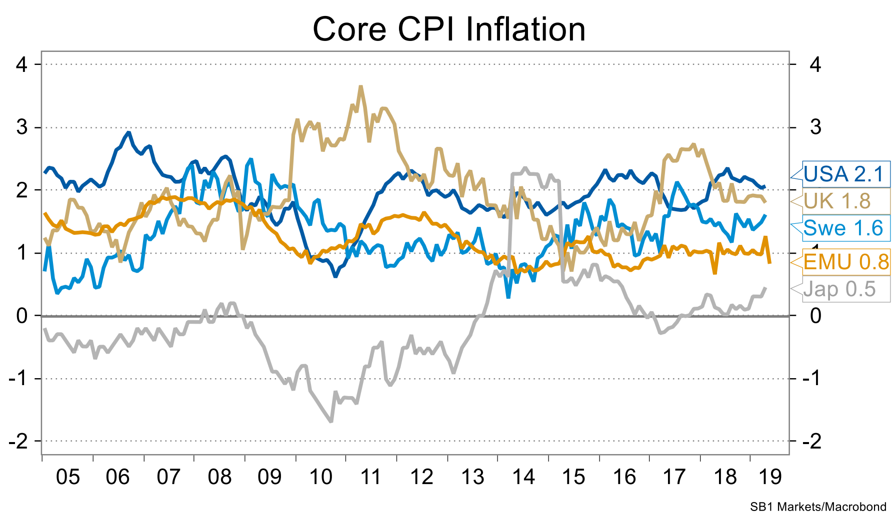
- Manufacturing production has stagnated since last autumn. However, the slowdown has not accelerated recent months, production probably grew marginally in April, after a lift in March. The downturn the past 6 months is due to lower investments and probably destocking following an unwarranted inventory build-up during 2018, stabilising now?
- Retail sales probably increased in April and is still tending up but at a somewhat slower pace
- Global trade volumes improved in March, recovering just slightly the past 3 months. Foreign trade has no doubt slowed, however, the change of pace is so far not dramatic and volumes are up 1.1% y/y (from -1.4% in Dec)

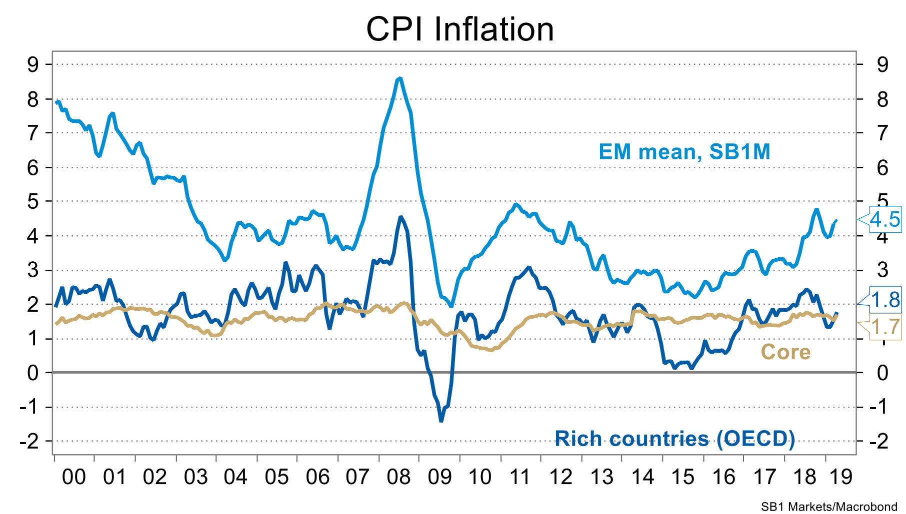
DM inflation is bottoming now? No more oil contribution. Core inflation stable

Core inflation at target in US, UK, below in Sweden and more in EMU. EM inflation will pick up too





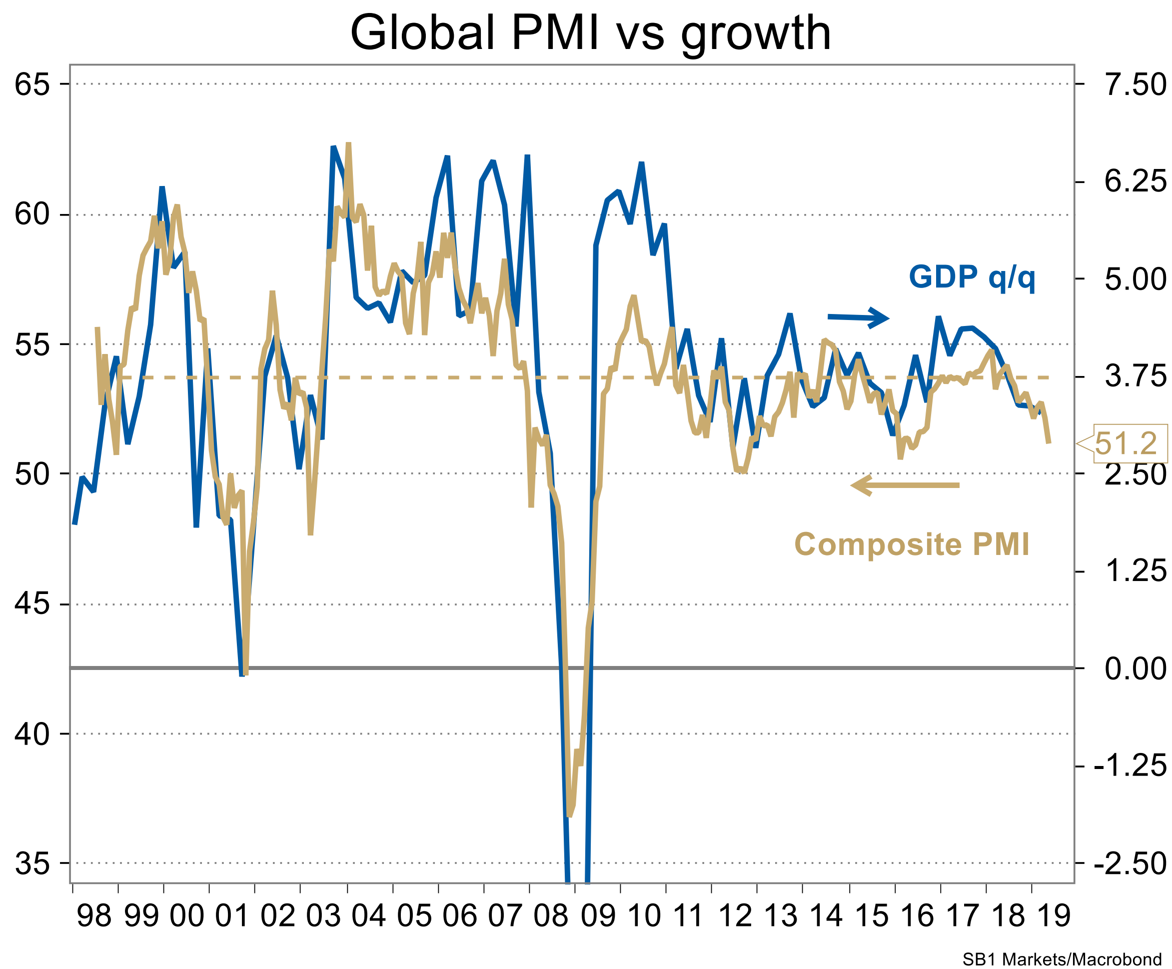


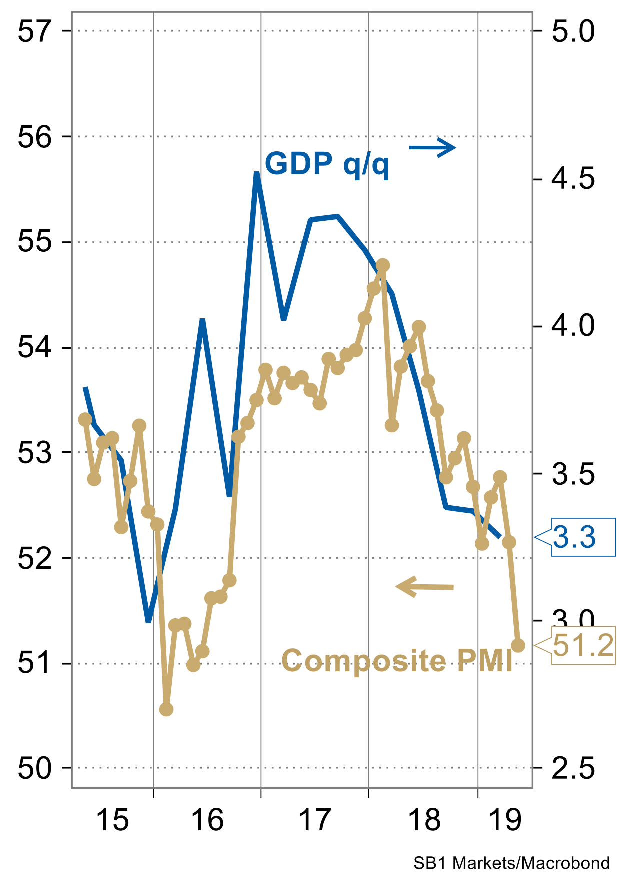


Change in % y/y in all charts. EMU core based on a seasonally adjusted price index

Global PMI plunged to 51.2 in May, signals below 3% global GDP growth

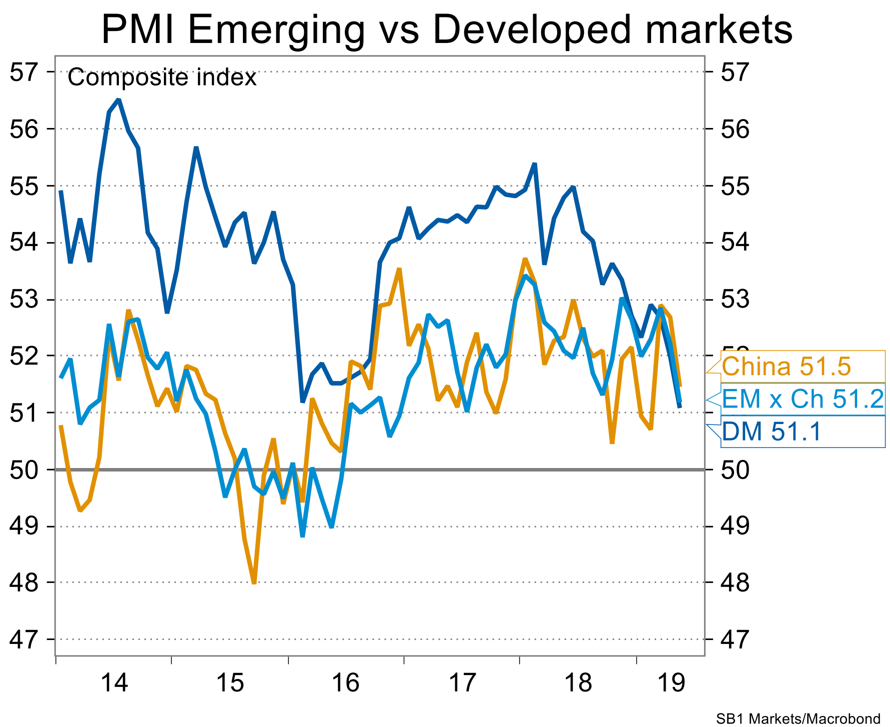
Composite PMI fell by 0.9 p, (we f'casted a 0.6 p drop), growth decelerates to below 3%, from 4+

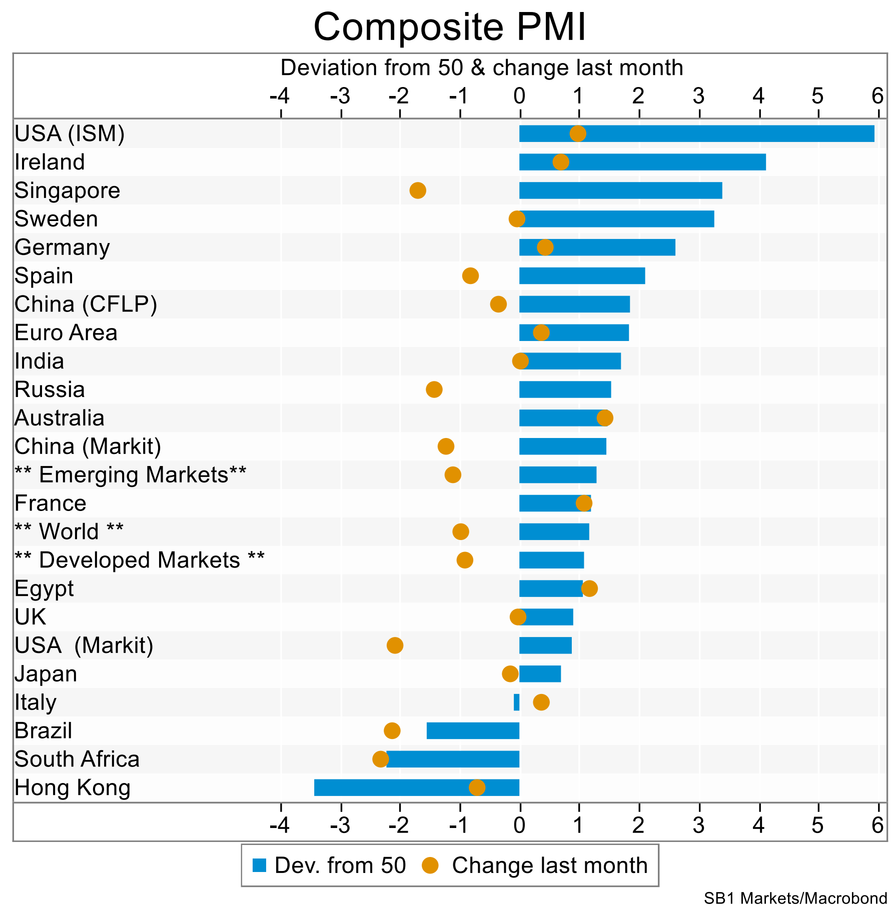




A broad slowdown in May, DM growing at the softest pace in 6 years

Emerging markets are holding up quite well, Developed slows sharply. China down, still trending up?

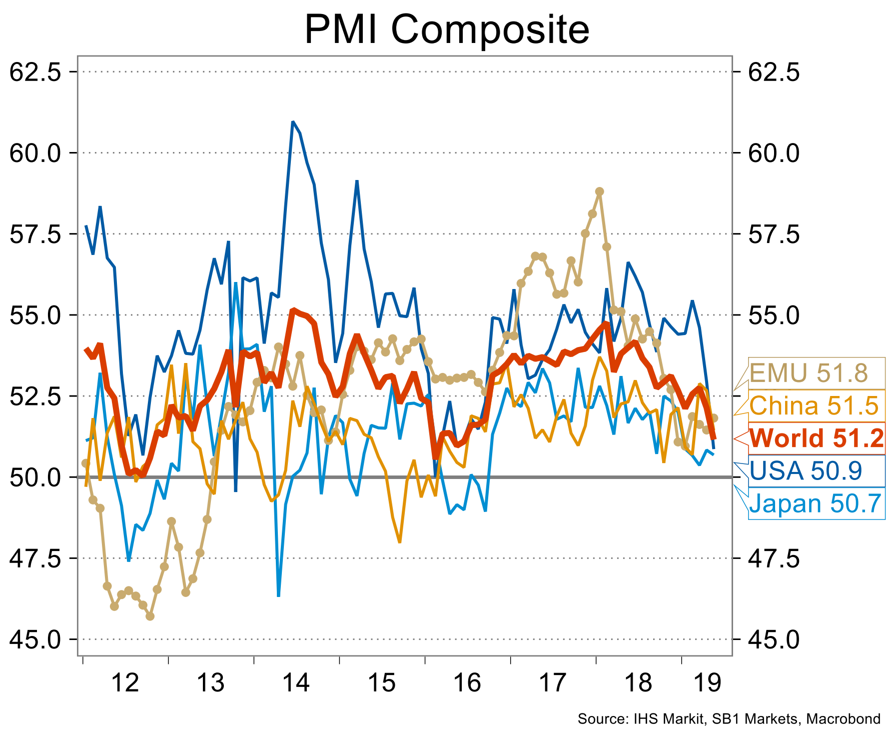


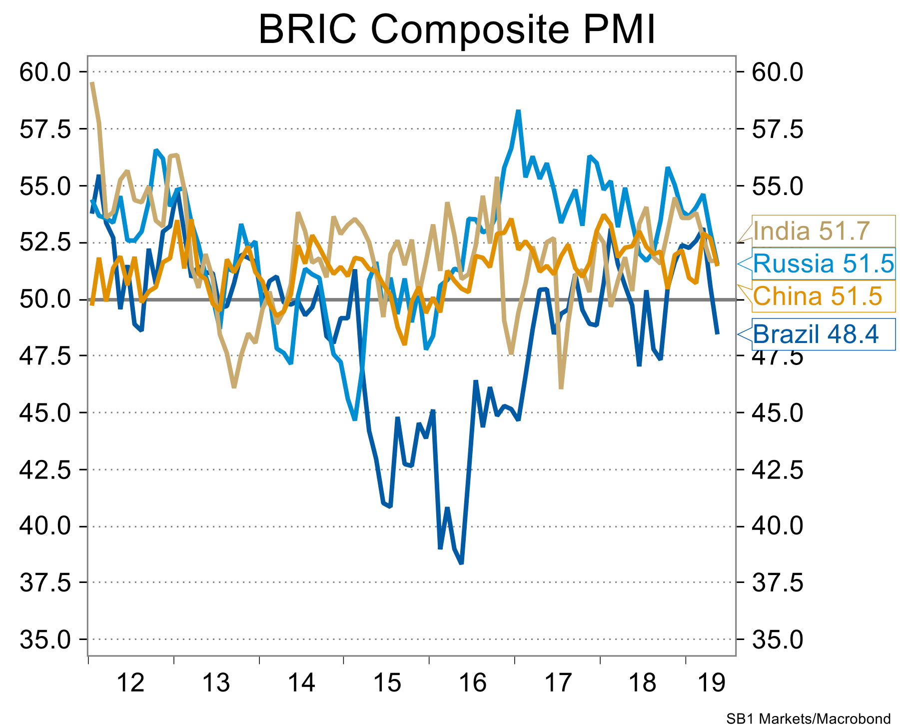


- Just 8 countries/regions reported that activity expanded at a higher pace in May (9 in April), 13 slowed
- Still just 4 countries below the 50-line (from 2 in April)
- DM average fell 0.9 p to 51.1, signalling slower growth. EM x China down 1.1 p, marginally outpacing DMs. China down to 51.5, still above the Jan/Feb level, and above the past 6 y avg

US is slowing rapidly, EMU stable, China a tad weaker in May

BRICs were mostly on the weak side in May, Brazil slipped back below 50

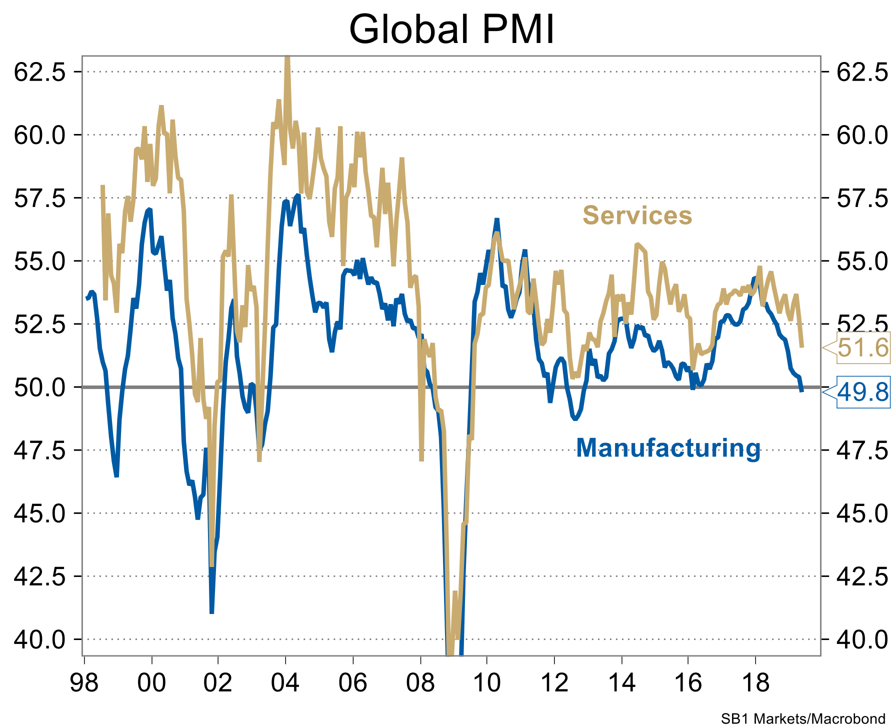


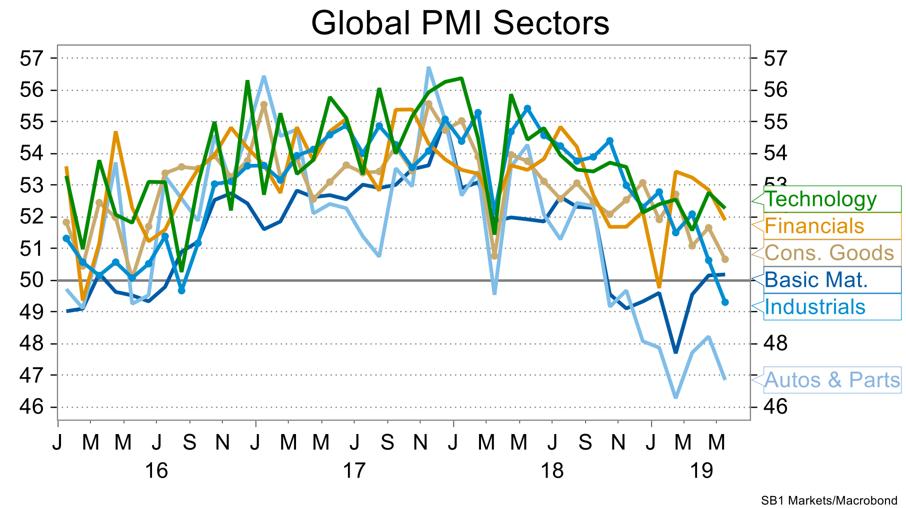


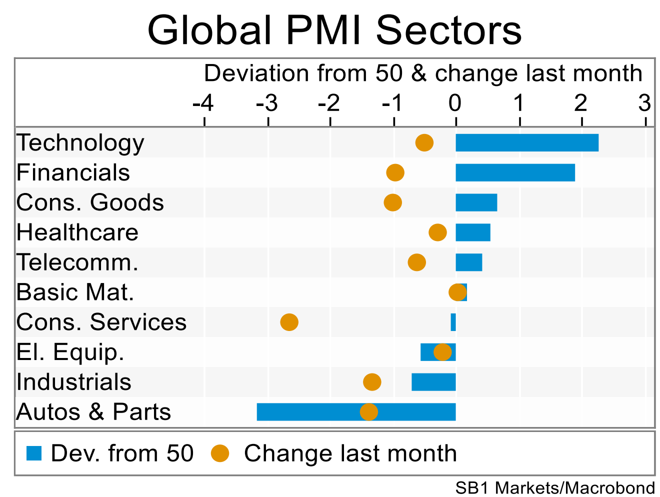
- US Markit's PMI dropped 2.1 p in May, both sectors weakened (however, services ISM improved, taking the ISM avg up)
- Mixed China data; Markit's composite index fell 1.2 p to 51.5, the 'official' NBS PMI fell just marginally. The government stimulus may not be sufficient to bring growth up but PMIs are anyway indicating that activity is expanding at a faster speed than in early 2019
- The EMU PMI improved marginally, is stabilised at a low level (but above the US May level) the past 4 months. However, manufacturing is still tumbling

Sectors: Manufacturing stagnates, services noting a marked slowdown

The auto sector reports a steep drop in activity, most others growing at a slower pace



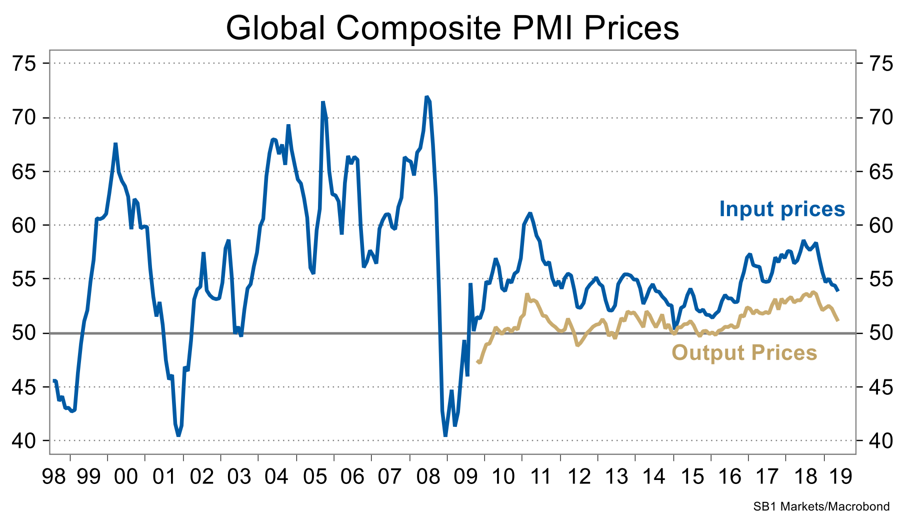


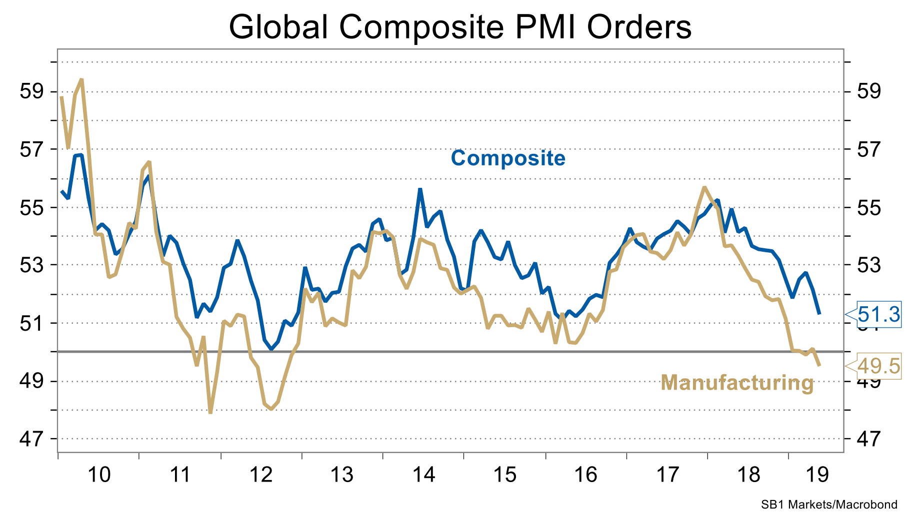


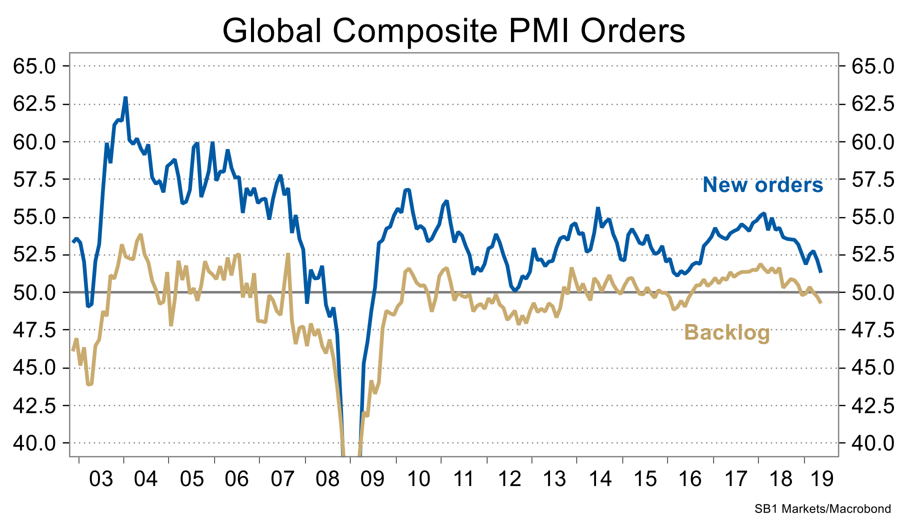
- The auto sector PMI improved somewhat in March/April but the decline deteriorated again in May. No recovery in sight
- Manufacturing has no doubt been hurt by uncertainties caused by the trade war, however, the broad slowdown suggests a widespread loss of demand, too

Composite orders and prices are still rising, at a softer pace

New composite orders are slowing, manufacturing deteriorates



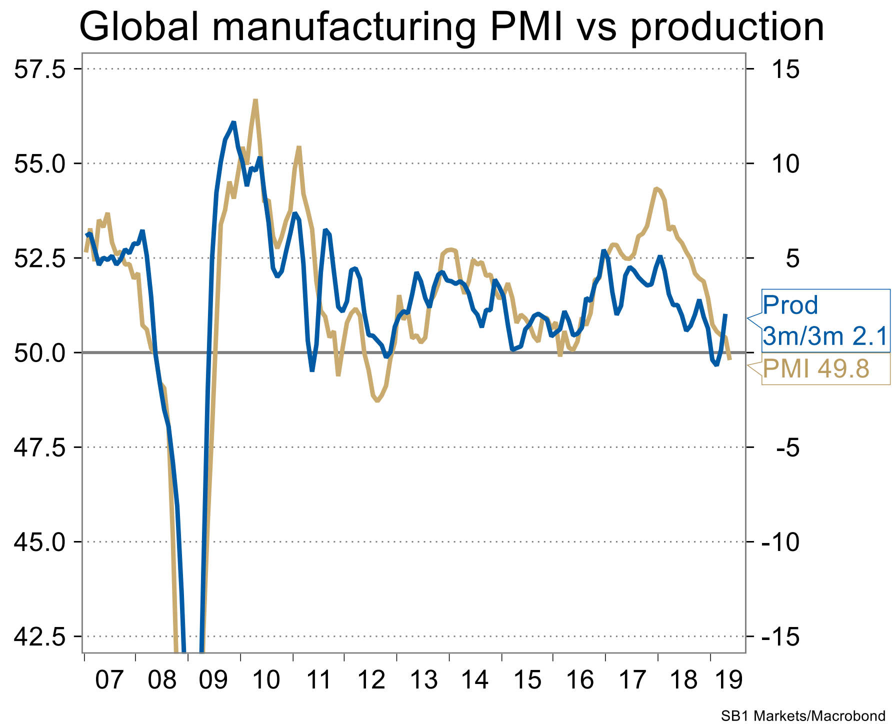


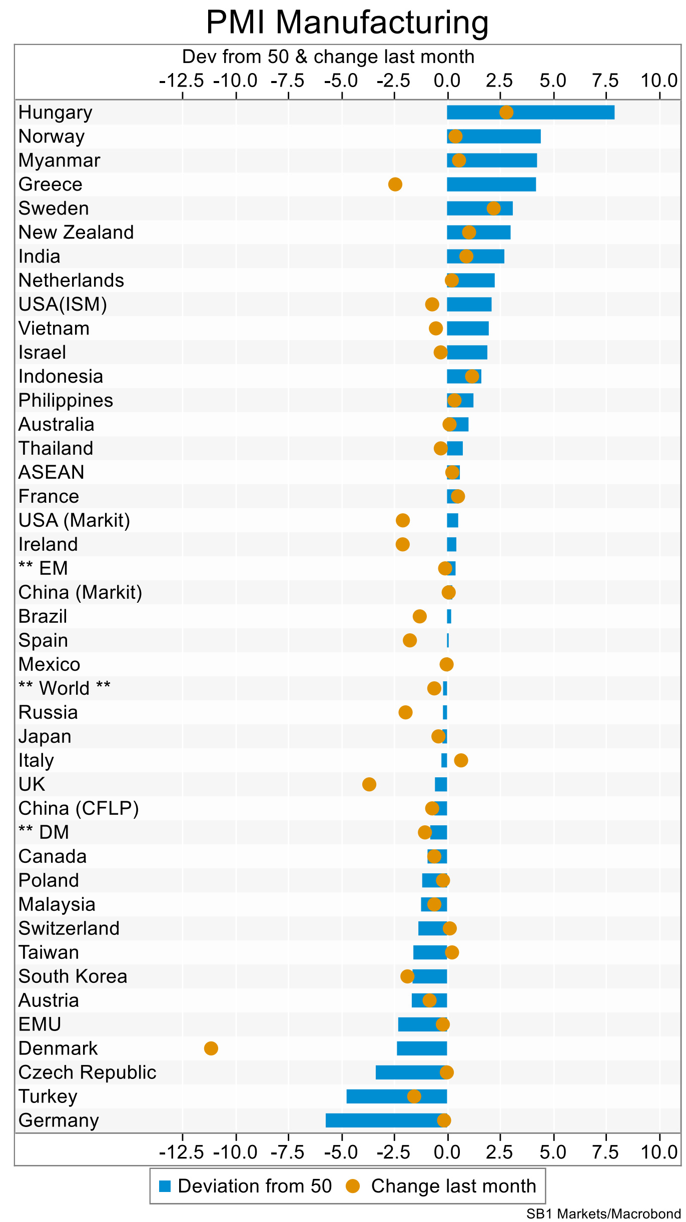


- Manufacturing orders index signals a modest contraction in activity. Service sectors are so far quite resilient to the slump in manufacturing, even as growth has slowed here too
- The global input price index is still at a decent level, at 53.9 but both input and output prices are easing. <u>Signs of a maturing cycle, and not just from the demand side</u>

Manufacturing PMI edged down in May, signals stagnation

The index fell 0.6 p to 49.8, pulled down DM (primarily US, UK)





- Global manufacturing PMI fell to 49.8 in May, in line with our estimate. , based on the preliminary results from some countries. **The index has fallen for 13 consecutive months, signals stalling global manufacturing. Production has accelerated somewhat recently, downside risk**
  - 22 (23 in April) countries/regions down in May and 15 up (18)
  - Almost half countries/regions are reporting declining output; 19 countries/regions are below the 50 line. Germany still at the bottom. Norway the 2nd best!
  - Developed Markets fell 1 p in average, Emerging Markets down 0.1 p

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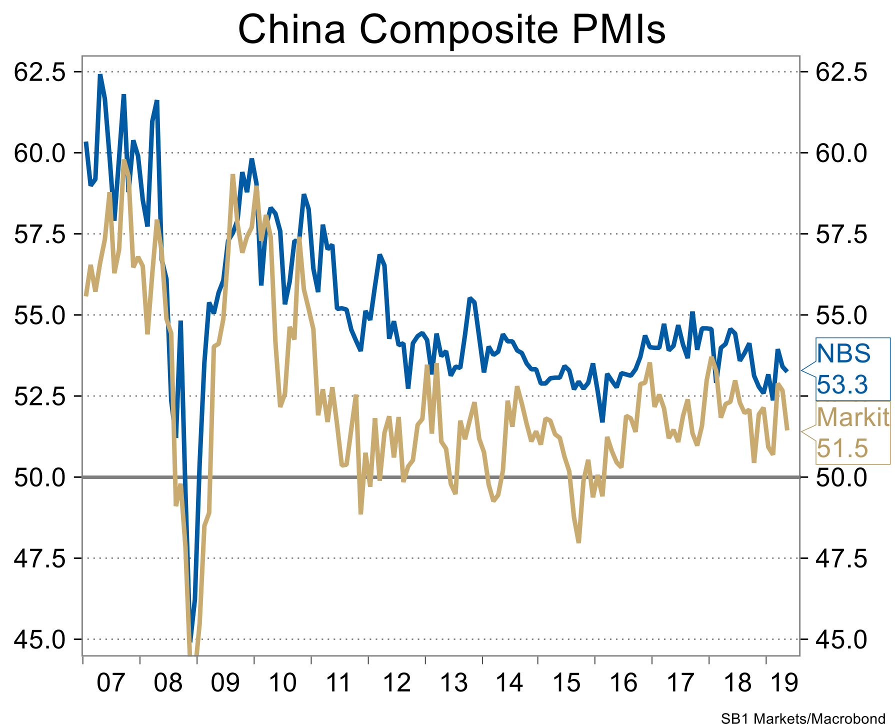
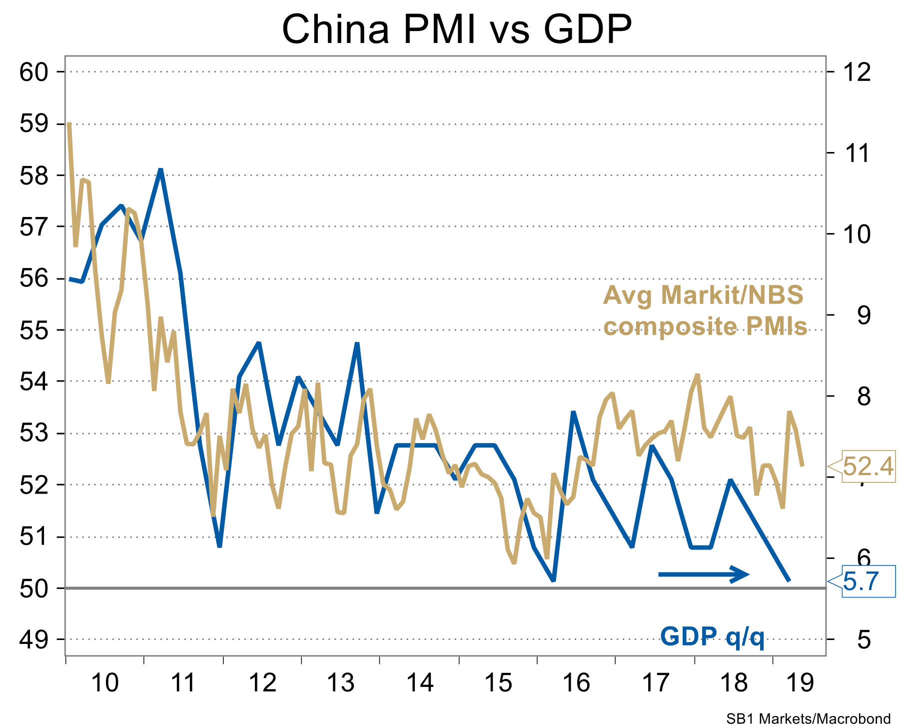
The composite PMIs softened in May, both are trending up recently

One service PMI down, one flat, composited indices do not signal any abrupt slowdown

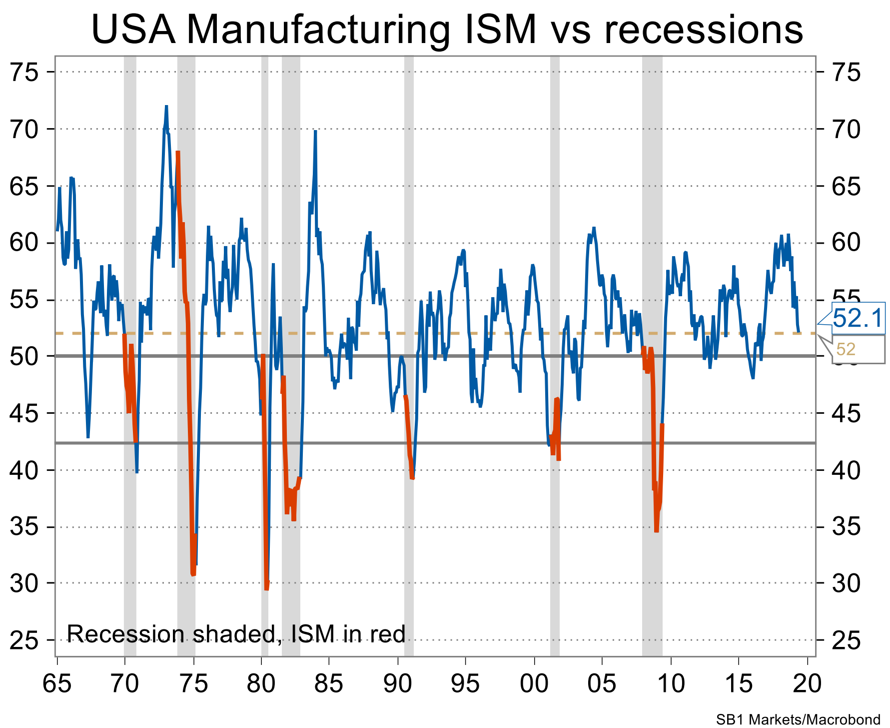


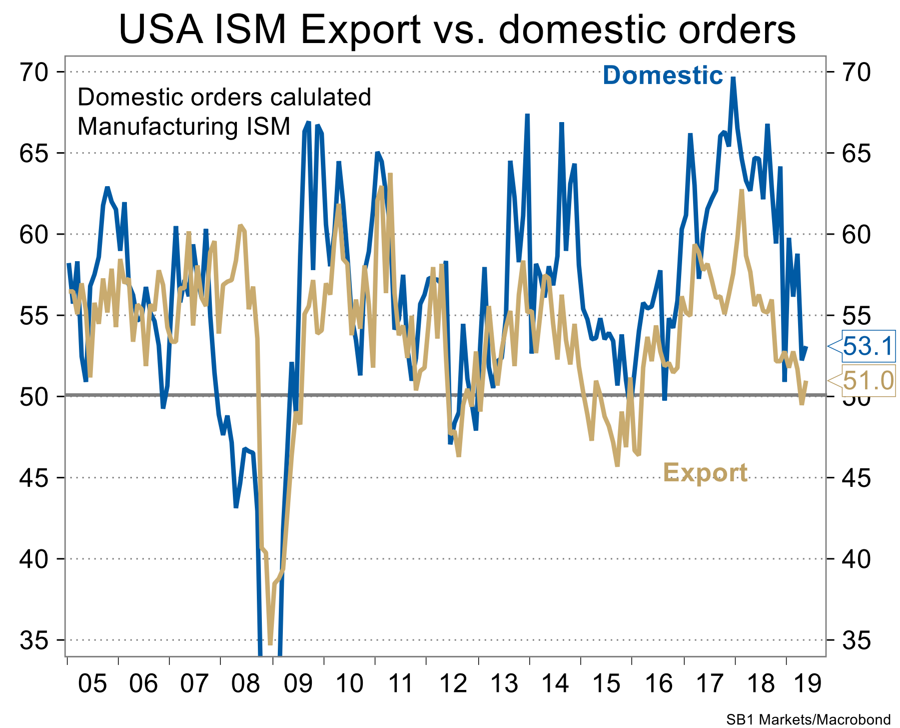


- Markit's PMI composite PMI edged down to 51.5, a 1.2 p decline. Service businesses are still reporting solid growth, although the index fell to 52.7 in May, from 54.5 the prior month. Manufacturing improved marginally to 50.2
- NBS' composite PMI (CFLP) fell 0.1 p to 53.4 in May, not too hot/too cold. The manufacturing index slipped to 49.4, whereas service businesses reported unchanged conditions, index at 54.3, at an average level over the past years
- The two PMI data sets have more or less recovered the losses from late 2018 and into 2019 – and they do not signal any abrupt halt in the Chinese economy

Manufacturing ISM another step down in May, below expectations

ISM fell 0.7 p to 52.1, confirming a rapid slowdown. Still, orders are increasing marginally faster

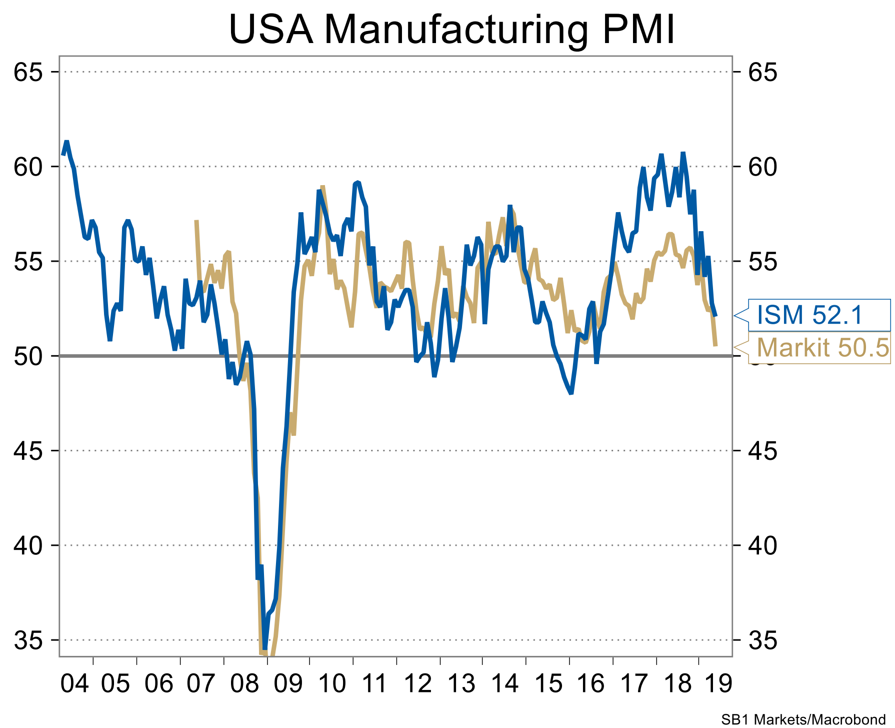


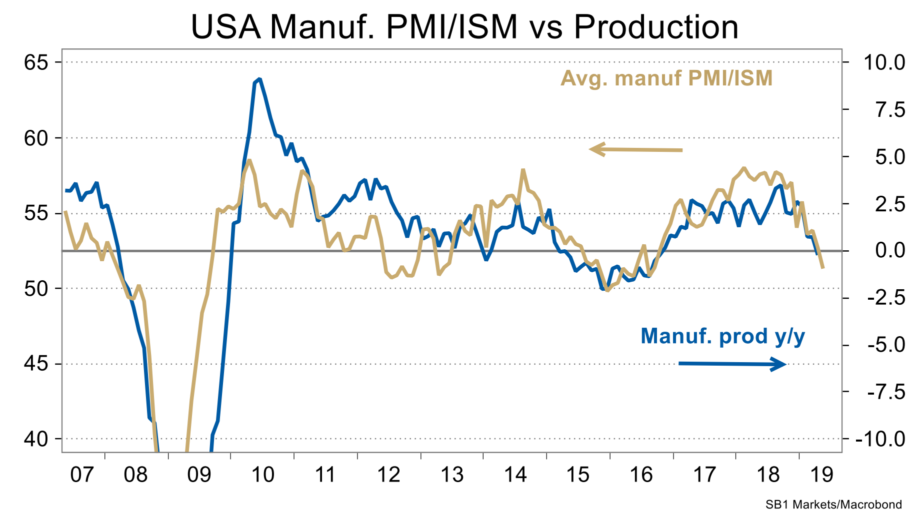


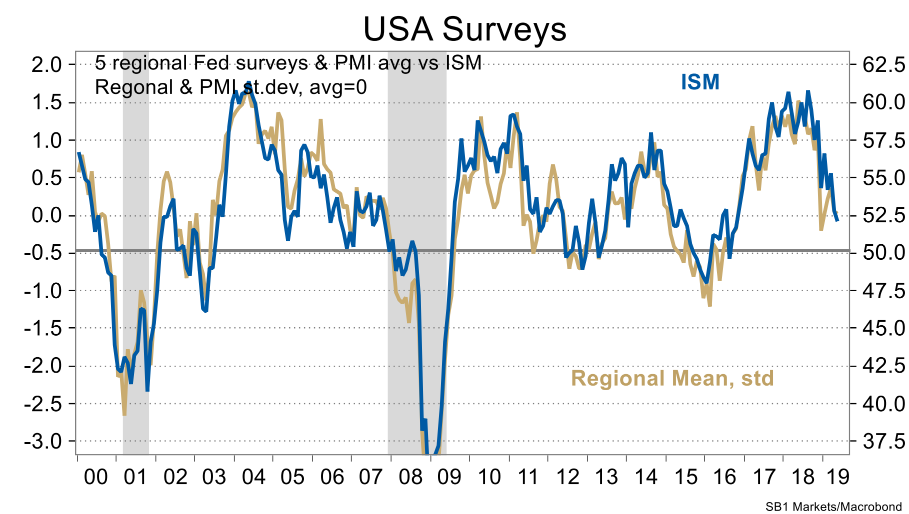
- Manuf. ISM fell to 52.1 in May, was expected up to 53.0, from 52.8. The ISM has nosedived from above 60 last August, and now to the lowest level since Oct 16. The ISM is below the average level (at 52.9) and the speed down is no doubt worrisome, particularly as Markit's PMI slips, too
  - In the ISM survey, 11 out of 18 manufacturing sectors reported growth (down from 13 in April) and 6 (from 5) sectors reported a contraction
- Businesses reported a marginal acceleration in order inflows (both domestic and exports) and lower inventories, not a weak mix, although the levels are not impressive anymore. Slightly weaker production and faster delivery times, implying weaker demand, pulled the index down
- The really bad news: An ISM at 52 may be an early warning of a recession (in 6 of 20 times, at least). The good news: it usually takes some months

ISM and Markit's PMI are suggesting contracting manufacturing output

Markit's PMI plunged to 50.5 (0.1 pp below 1. est), while regional surveys improved somewhat







- An average of other regional surveys and Markit's PMI inched up in May (although the PMI was plummeting), with 3 of 5 regional surveys improving. Markit's manuf. PMI fell 2.1 p vs 2.0 first reported, a rapid decline
- The avg of ISM/PMI are signalling a mild contraction in manufacturing. Actual production has been stalling
- Manufacturing ISM has been much stronger than Markit's PMI the past 2 years but Markit has been closer to the ball vs actual production. Now both are sliding down fast

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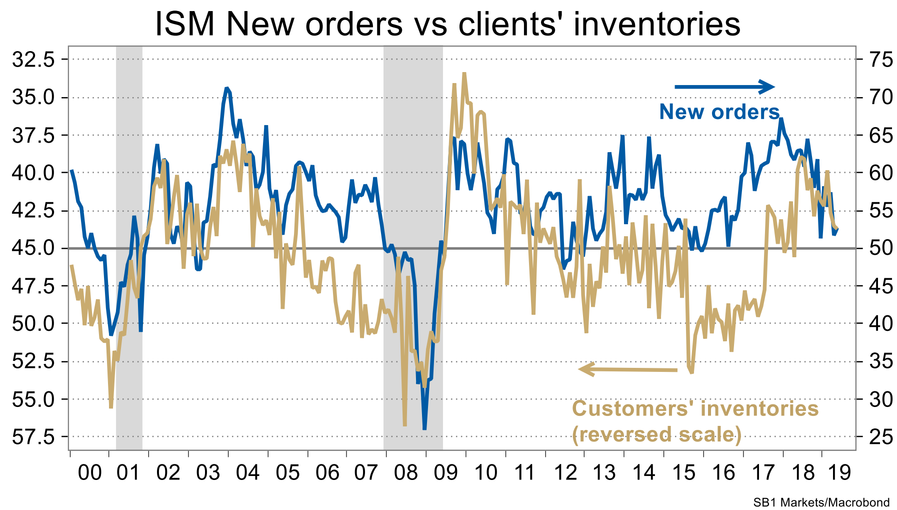
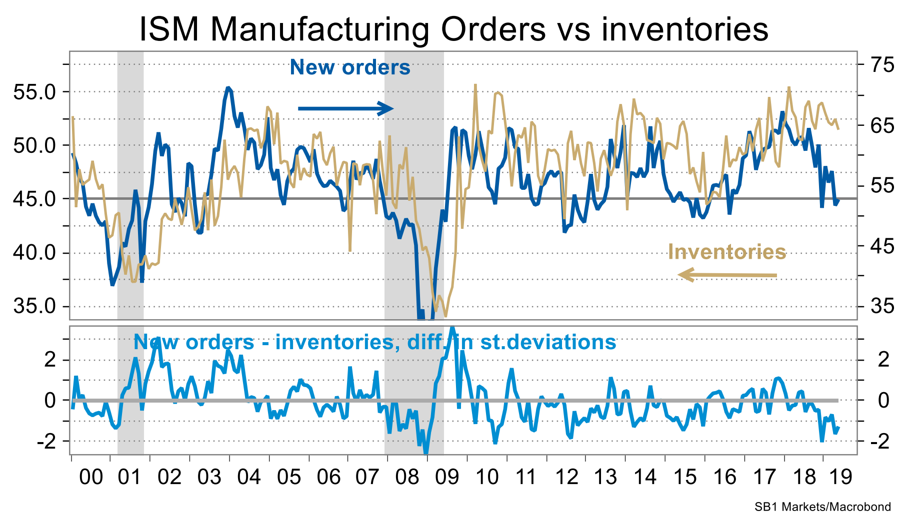
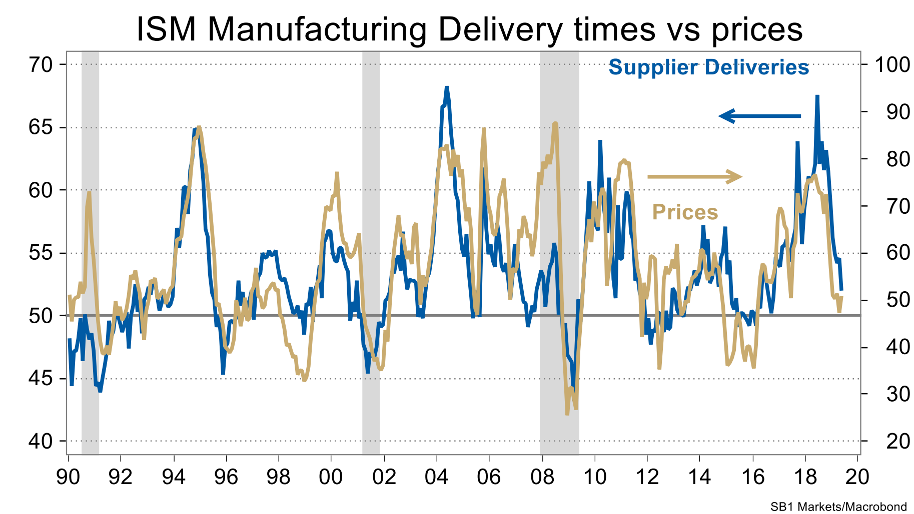
Slowing orders, higher inventories, less capacity constraints, halting prices

Yet, orders improved slightly in May, while delivery times plunged, echoing weaker demand

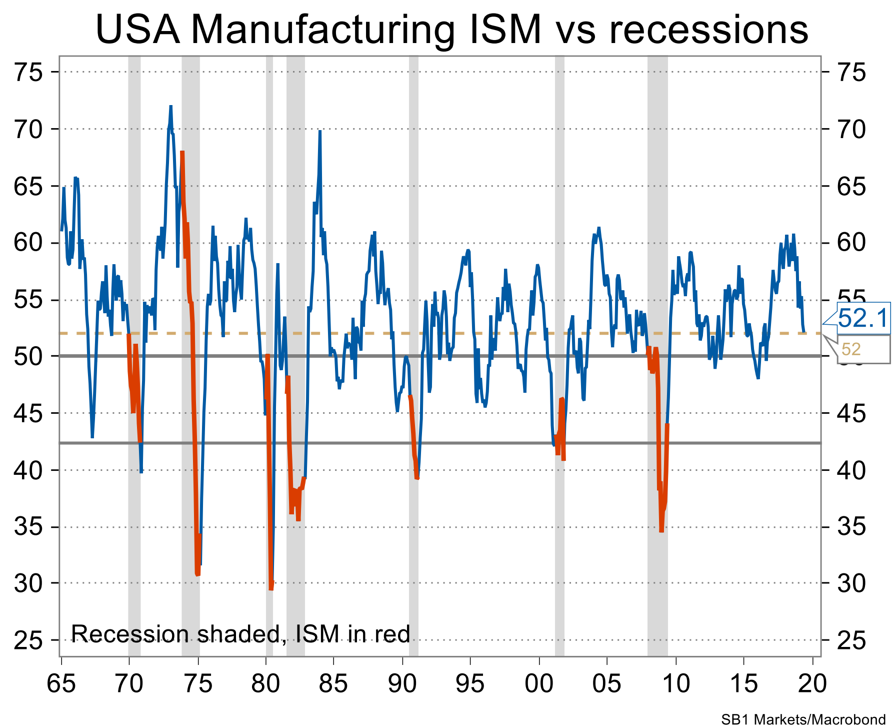


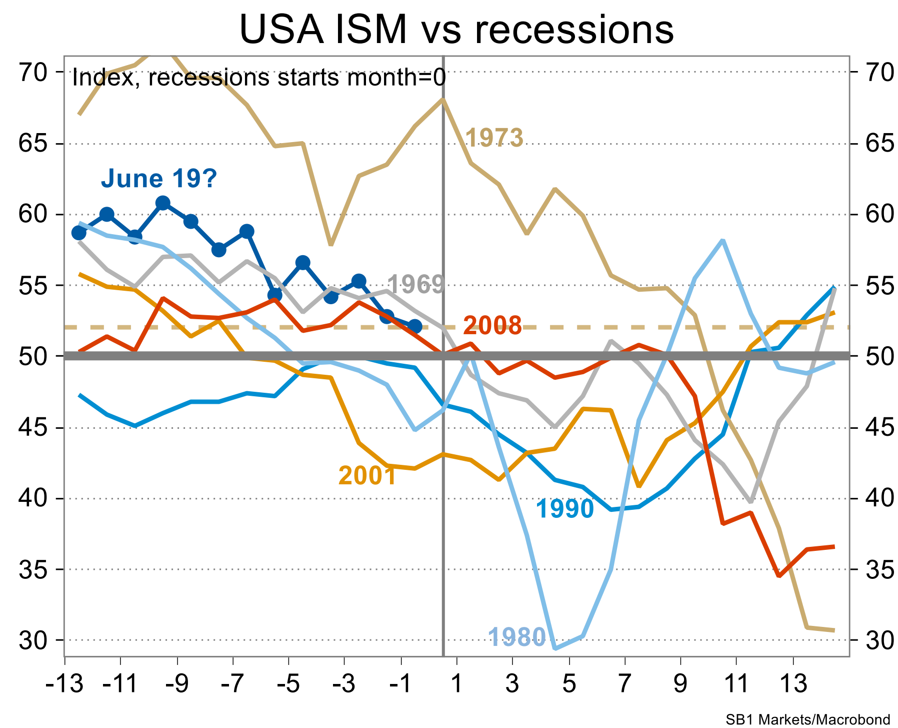




ISM vs recessions: 14 false positives, 6 correct positives, and 1 false negative

What happens if the ISM falls below 52? The ISM is a good cycle indicator but far from perfect.

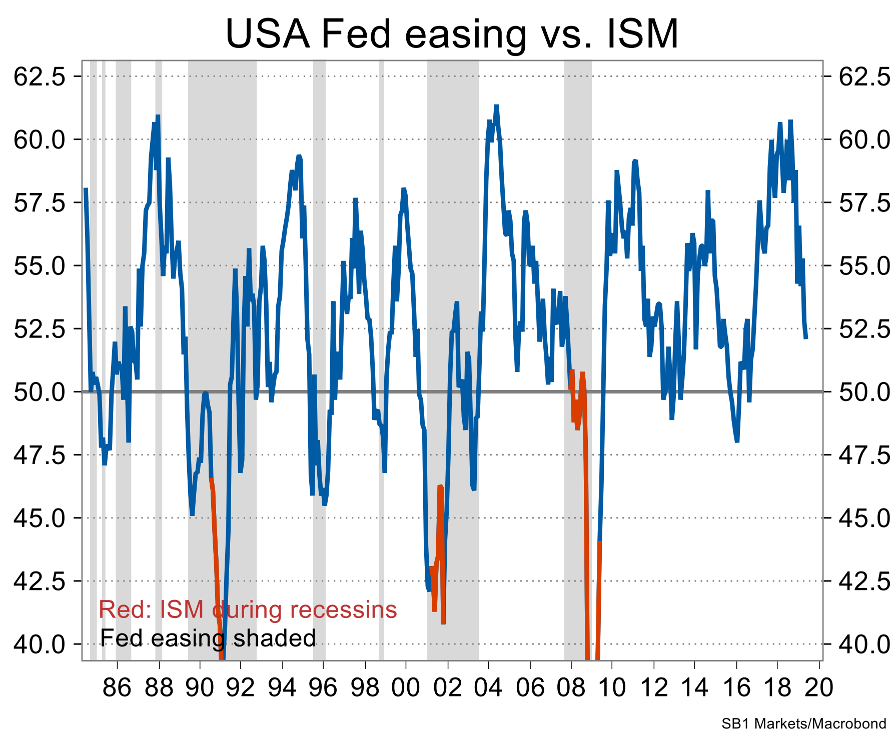


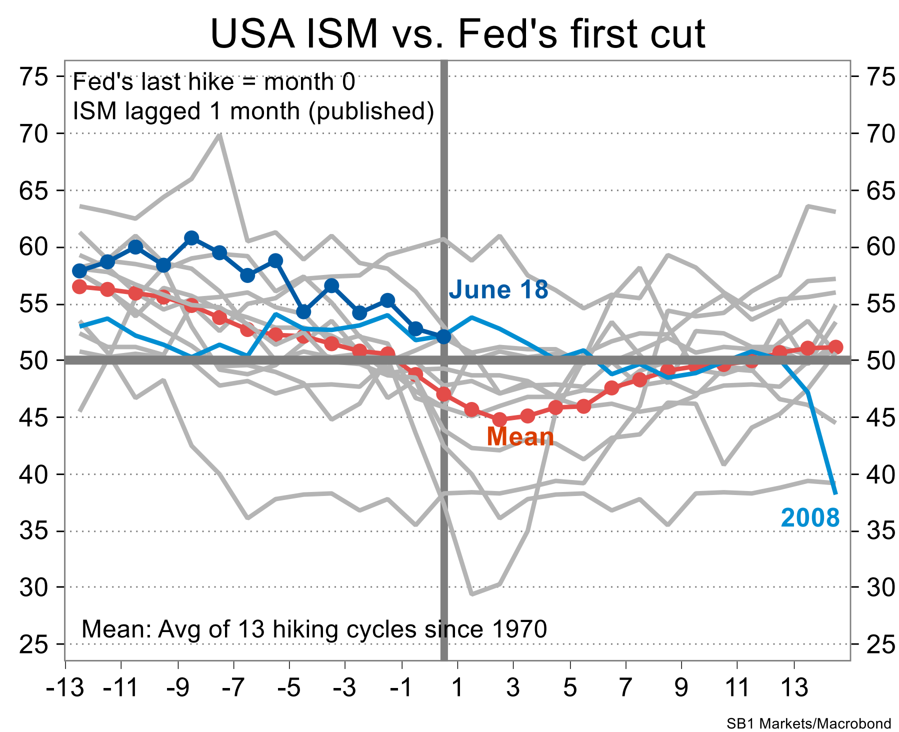


- One recession, in 1973 following the 3 x increase in the oil price, was not flagged by the ISM (1 false negative)
- The ISM fell below 52 in 1969, and below the 50 line five times before the recession hit (6 positive, correct signals)
- However, given a 52 threshold, the ISM has fallen below the line 14 times since 1965 without a recession (14 false positives)
- So, the ISM is not a perfect warning indicator – and a recession is not yet a done deal

When will the Fed start cutting?

Well, when it believes the economy has slowed (or will slow…) sufficiently

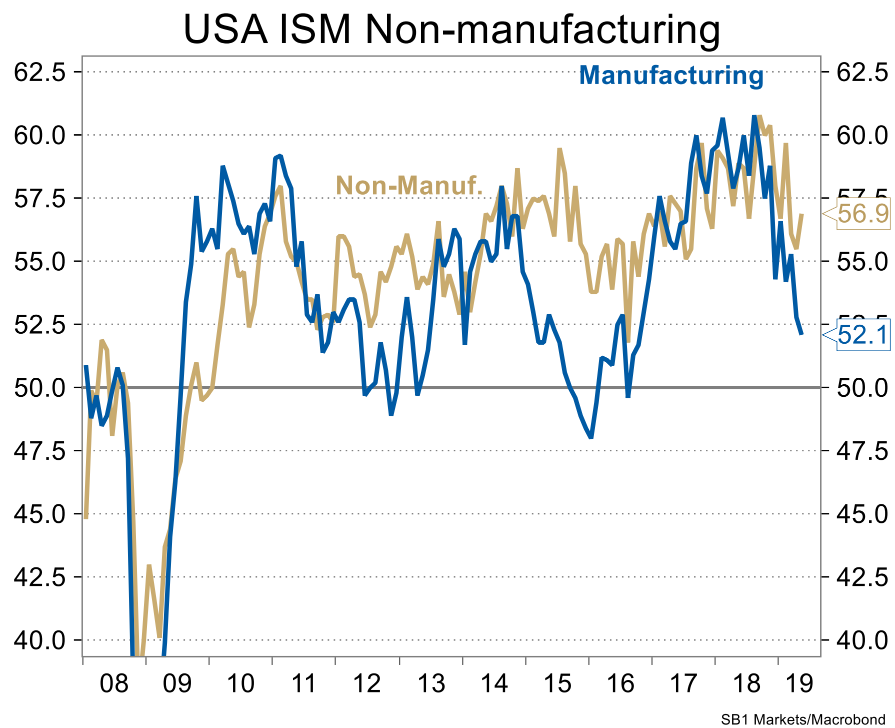


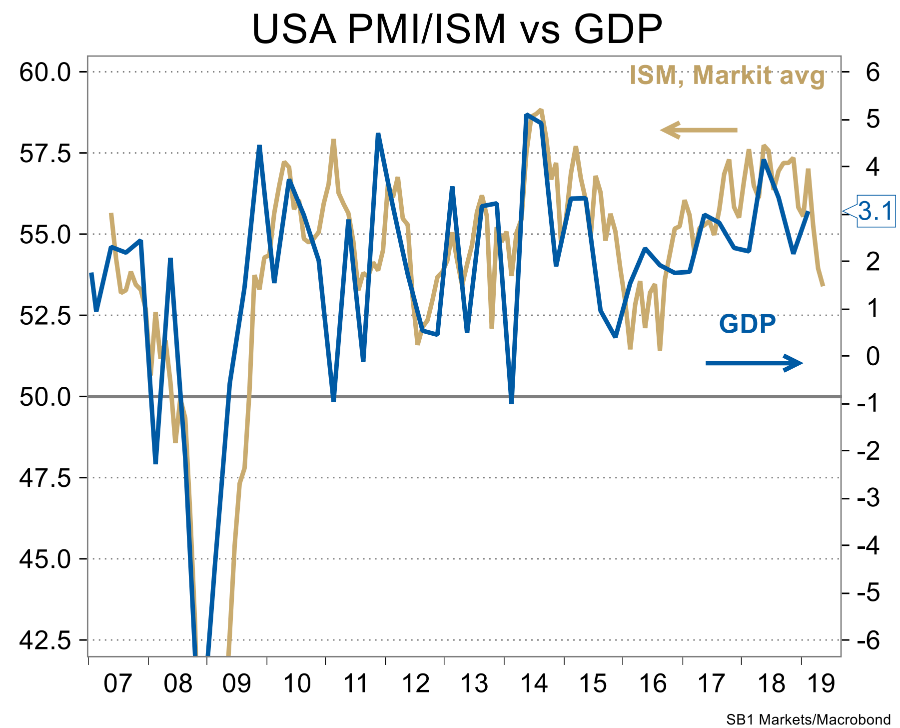


- In average the Fed starts cutting when the manufacturing ISM has fallen below 50 – but has started easing even if the survey is at far higher level – like in Sept 2007 when the (Aug) ISM was at 52.2 (like now, and unemployment still heading down) but when there were some stress in the financial market…
- Fed has engaged in some 13 easing cycles since early 1970, while US has had 'just' six recessions. So, the first hike does not signal a recession

Non-manufacturing ISM gained in May, ‘composite’ ISM ticked up!

Non-manuf. ISM up 1.4 p to 56.9, the avg of Markit/ISM indices signals 1.5% GDP growth

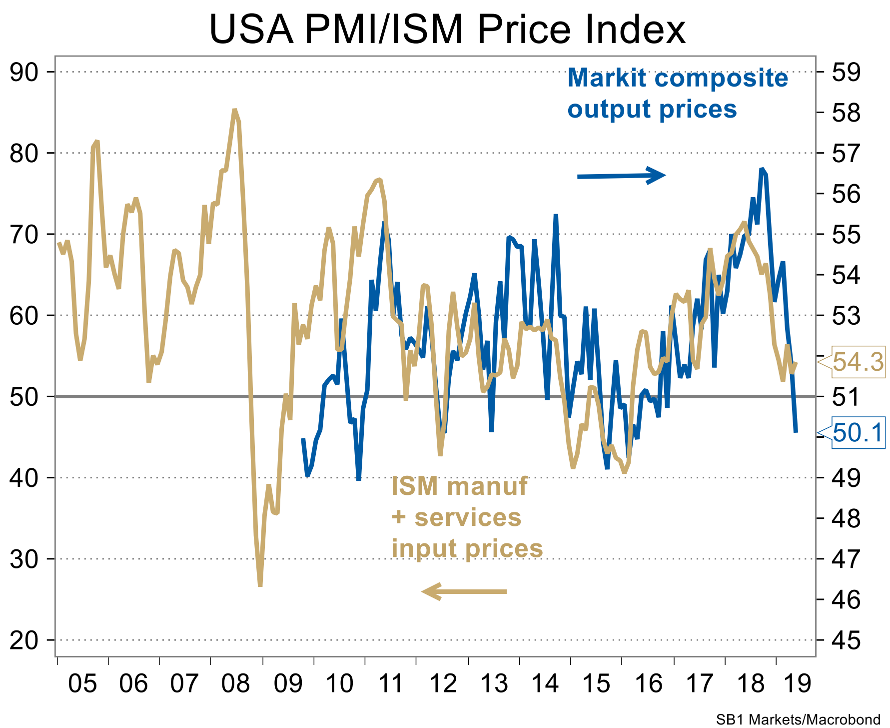


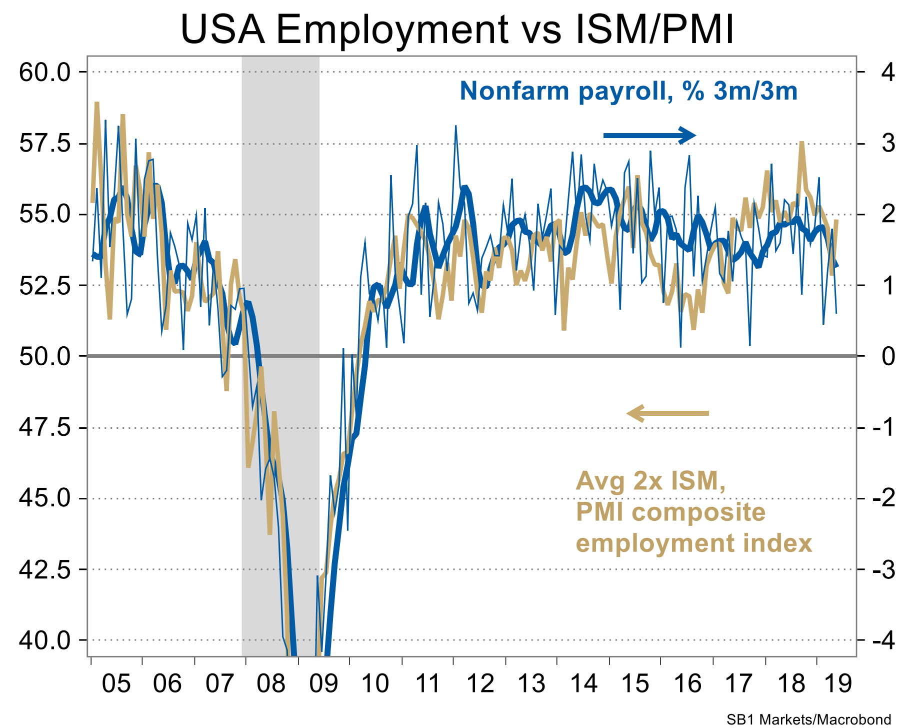


- Non-manuf. ISM came in well above expectations at May, edging up to 56.9. Even with a significant decline the past 6 months, the level way above average. Services are holding up much better than manufacturing, which decreased to 52.1, and the ISM is not confirming the rapid slowdown in service sectors which Markit’s PMI is noting
  - 16 of 18 non-manufacturing sectors reported growth, just one reported a decrease. Retail trade reported growth, suggesting an upswing in this sector
  - Composite orders rose marginally to 57.4, thus, orders are still growing at a solid pace – demand is not crumbling
- The ‘composite’ ISM index rose to 55.9, Markit’s composite ISM tumbled to 50.9. Unfortunately, the ISM has been too optimistic vs growth the past couple of years. The avg of the two surveys is pointing to 1.5% GDP growth, just above the nowcasters Q2 f’casts

PMI/ISM are still suggesting solid growth in employment

However, prices are slowing quite steeply, capacity constraints must be declining

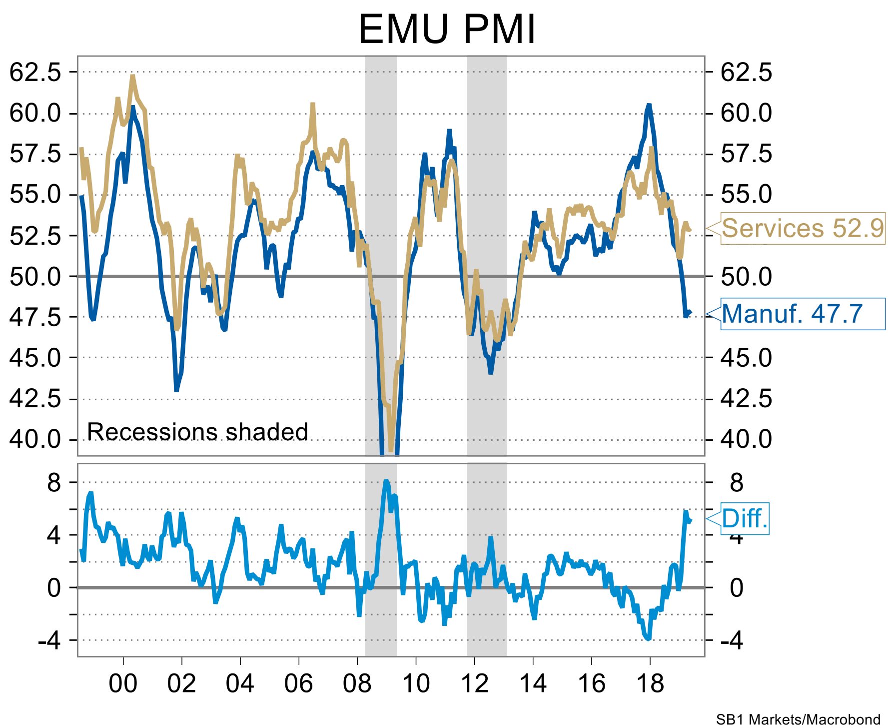


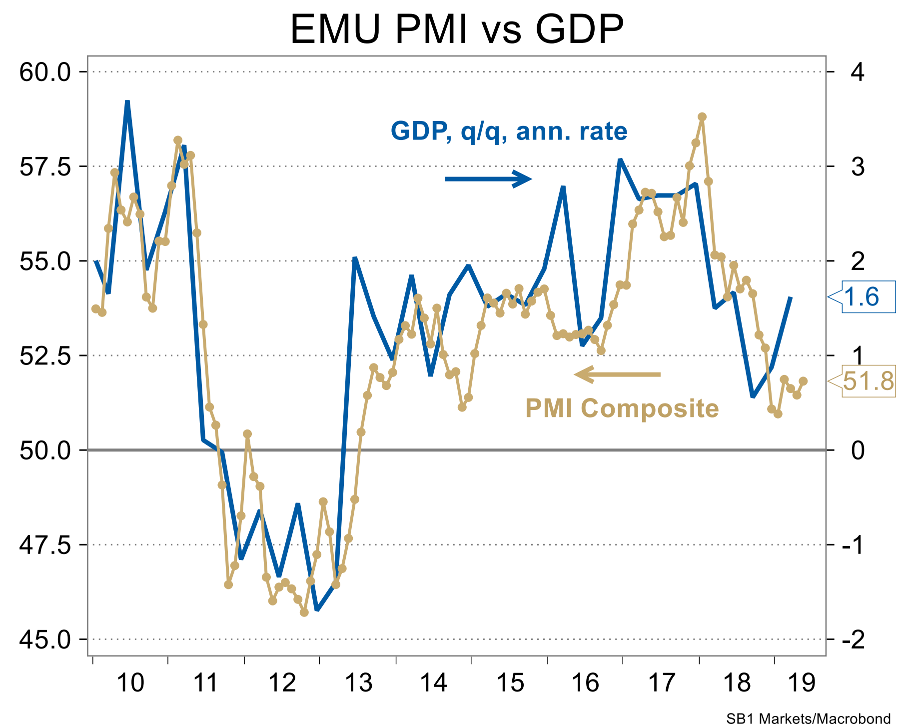


- The avg of the ISM/PMI employment indices increased in May, due to a lift in the non-manufacturing ISM
- Markit is reporting a rapid slowdown in output prices, to a stagnation in May. The composite ISM price index (input prices) has fallen less, stabilizing at +/- 54 the past 3 months

Final PMI: Composite PMI slides down, services better than first reported

PMI rose 0.3 p in May, 0.2 p above the first est. Manufacturing still weak, services resilient

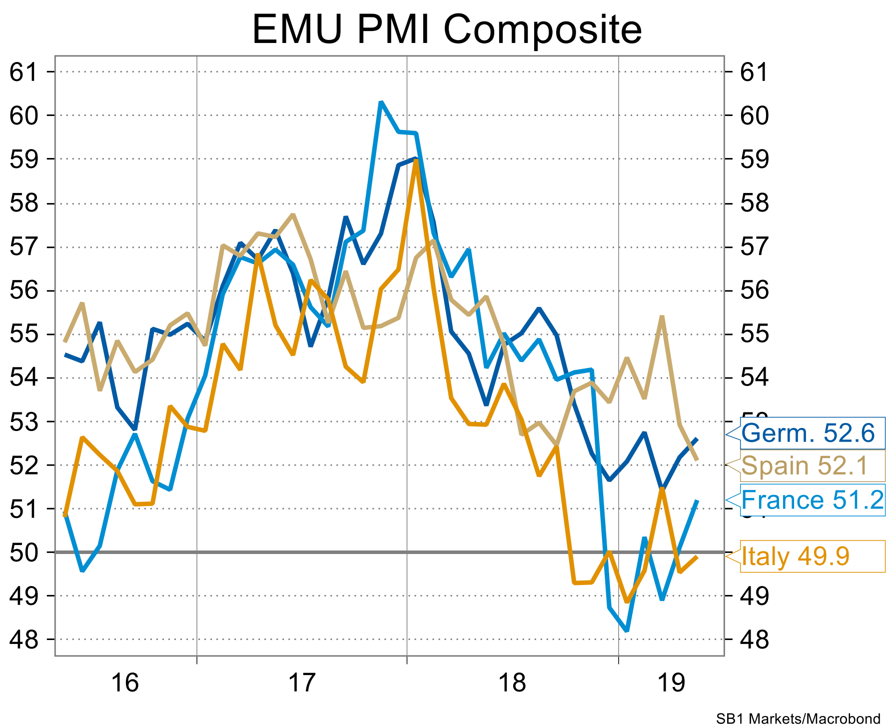


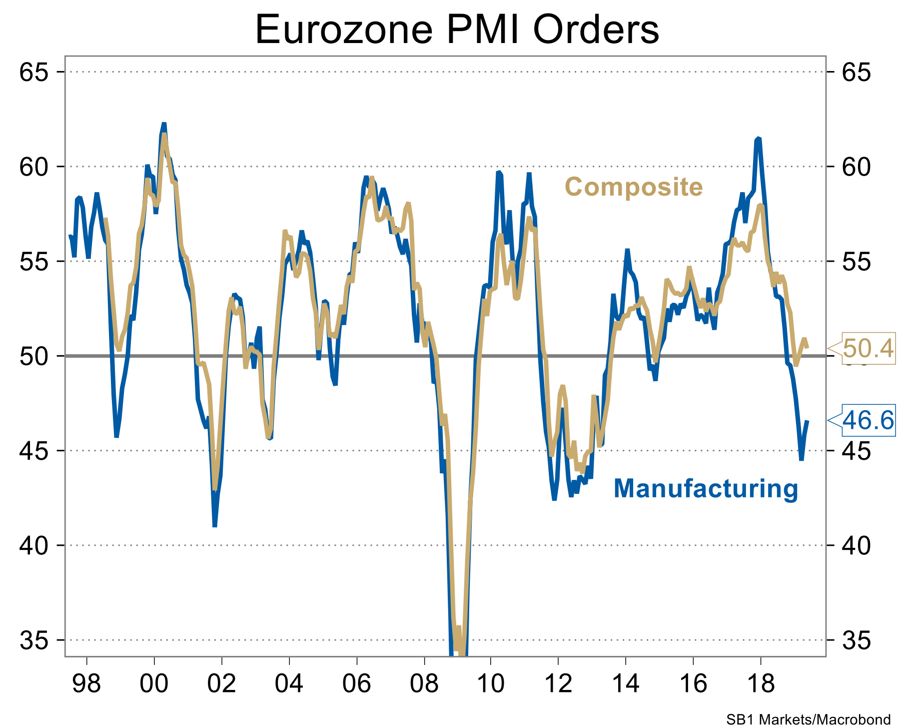


- **The composite index** came in at 51.8 in May, a 0.3 p increase from April, and 0.2 p above the preliminary report. The PMI has stabilised the past 5 months but the survey is no doubt reflecting a substantial slowdown, pointing to some 0.75% growth
  - » Manufacturing PMI at 47.7 is reflecting a continued and sharp contraction, service industries still growing moderately
- **Any hope?** Households are still optimistic, and other fundamentals do not indicate a recession now, and Q1 GDP growth was much stronger than the PMIs were indicating. Unemployment is not record low, wage inflation is still well below 3%, no credit boom recent years. So it may all come down to the trade war, Italy's politicians, Brexit, and France's yellow vests…

France recovering, Germany growing modestly, Spain losing some momentum?

.. And then there is Italy, which has strengthened somewhat but still remains fragile

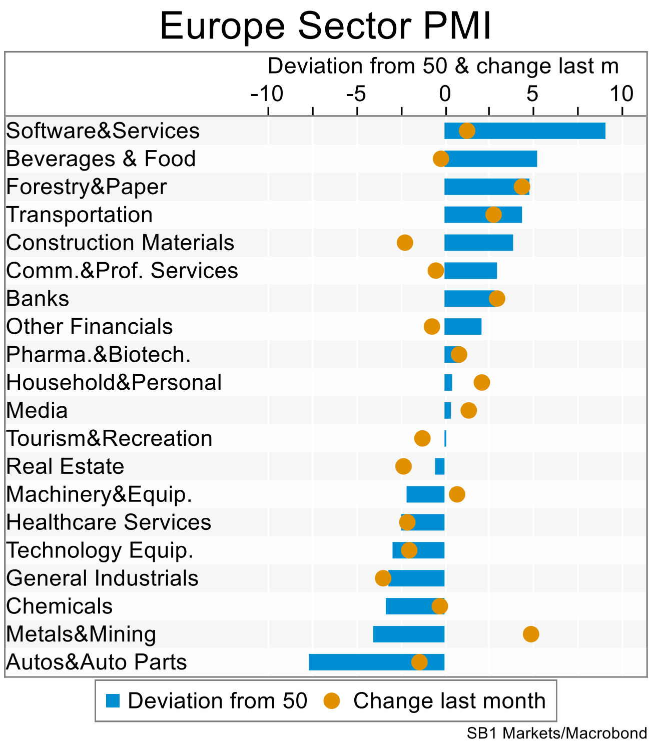


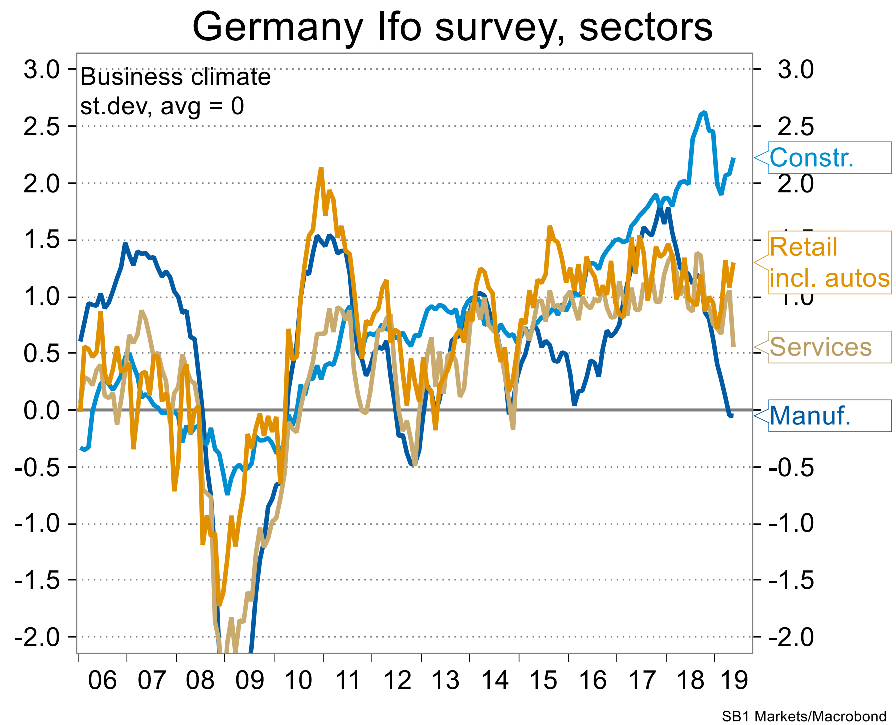


- More up than down in May: France reached the highest level since the protests began, at 51.2. Germany is split; manufacturing tumbles while service sectors remain solid, in sum expanding in May. Spain is reporting a slowdown, after climbing the prior months. Italy is stagnating, a marginal improvement from April
- The manufacturing orders index has recovered somewhat the past 2 months, the 46.6 level is signalling sharply falling order inflows and a rapid downturn in demand. Composite orders are expanding modestly, service orders growing

Sectors: Construction still going strong, retail/services OK, manufacturing slips

.. and the auto sector explains some but not all. Sector details point to a broader cyclical downturn

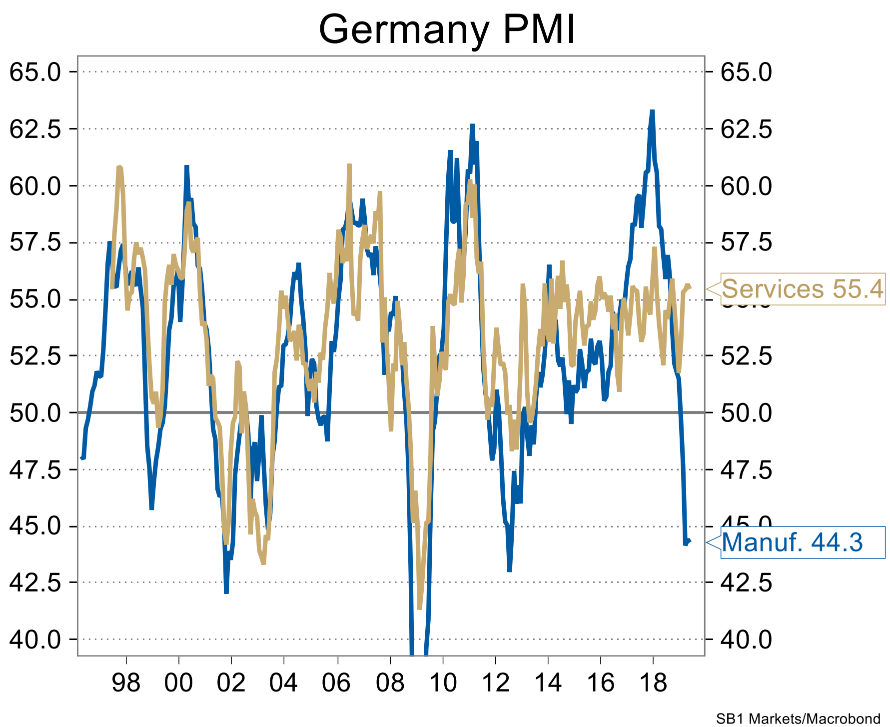


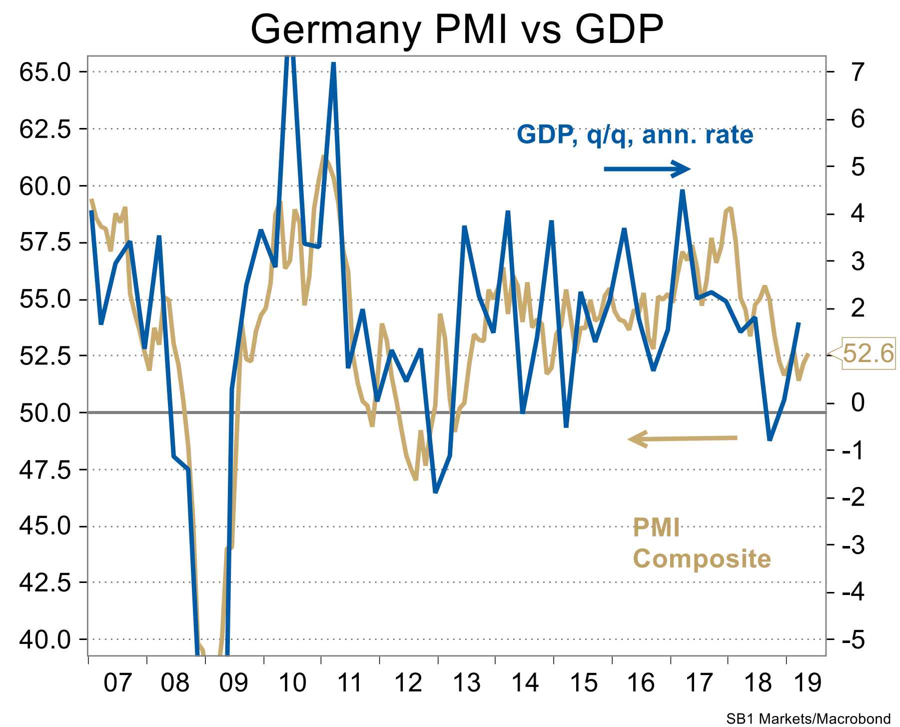


- Both the Europe sector PMI (not Eurozone) and the German Ifo business survey are reporting similar sector patterns (April PMI data, May Ifo)
- More on the outlook in the auto sector on the next slide

Manufacturing PMI signals a deep slowdown, services still strong

Composite PMI inched up, points to below 1% GDP growth. The manuf. sector deteriorates further

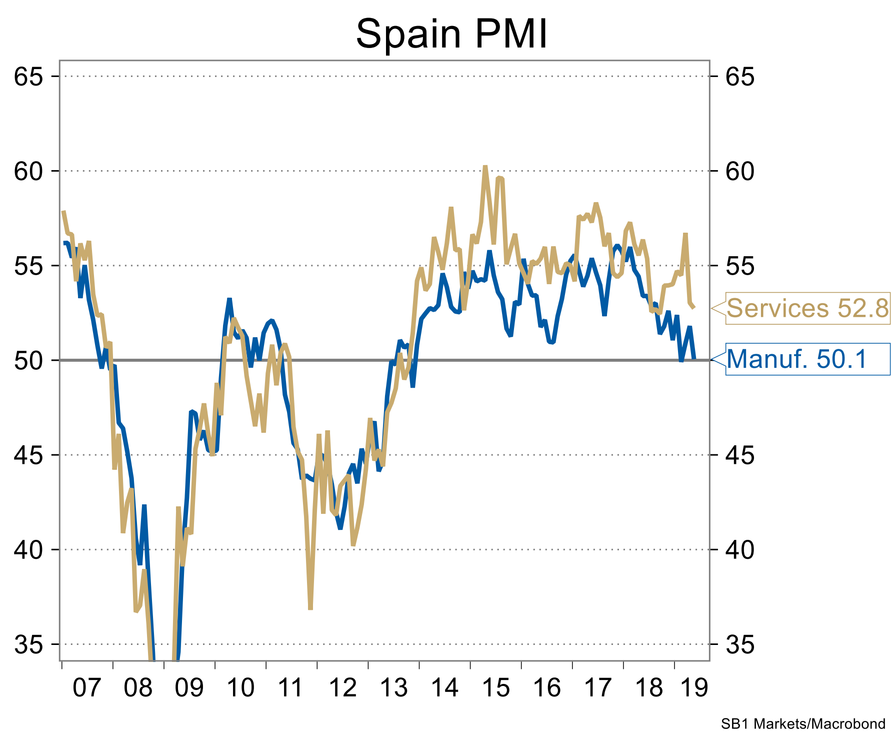


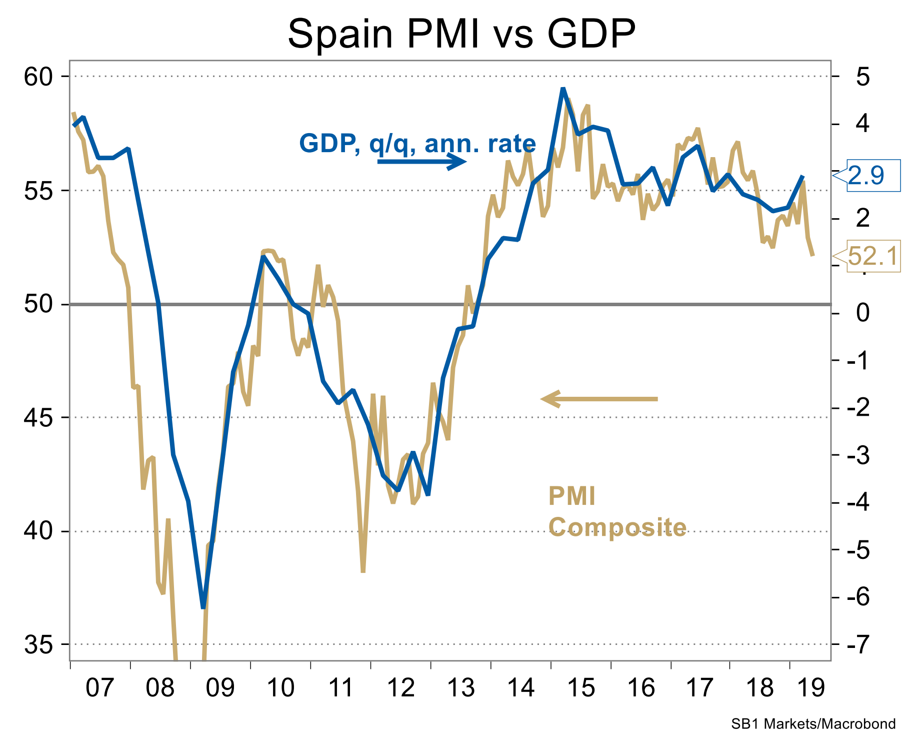


- The manuf. PMI fell marginally to 44.3 in May, just above the March level. The PMI is no doubt signalling a sharp contraction in the manuf. sector. This partly reflects an auto industry which is struggling after the implementation of the WLTP regulations but also a much broader loss of demand, partly due to global uncertainties/trade wars
- The services index is so far fully resilient to the manufacturing turmoil; the index ticked down to 55.4, 0.4 pp above the first report but that's a strong level.
- The composite PMI at 52.6 signals 1% growth in the German economy vs the upswing to 1.7% in Q1

Spain: Both sectors are reporting faltering growth

The composite PMI fell to 51.2, suggesting a slowdown to 1% GDP growth, from 2.9% in Q1

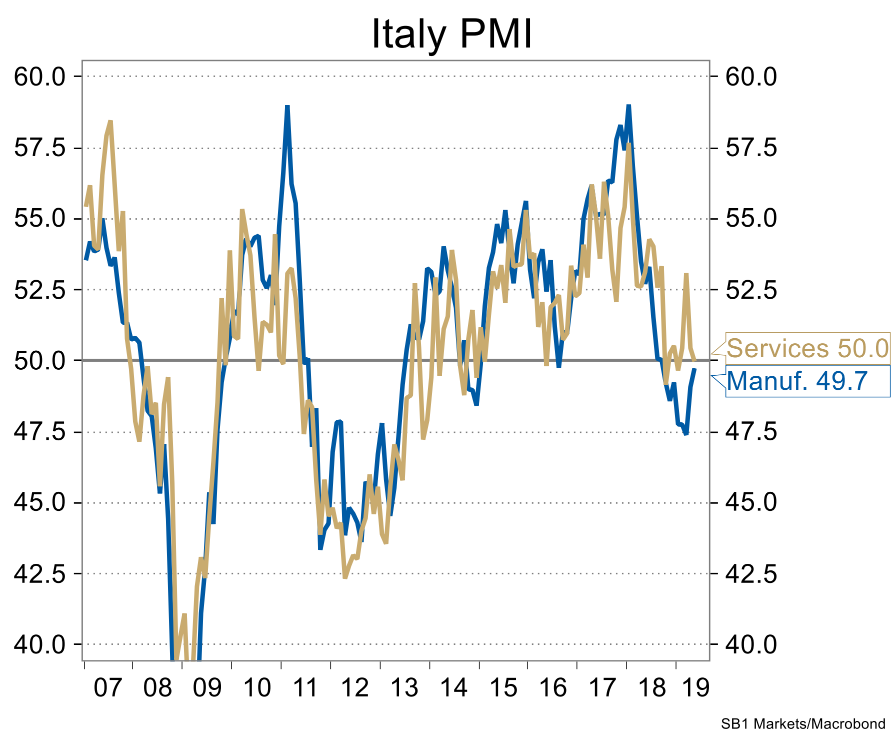


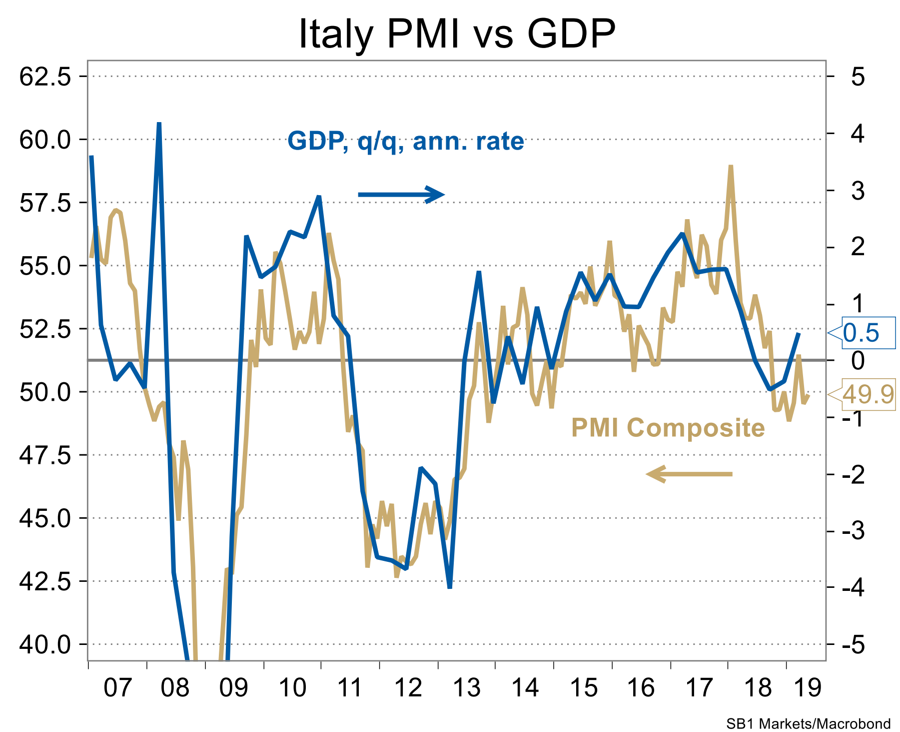


- The composite PMI came another step down in May, after jumping the prior month. Signals slower GDP growth, at just above 1%
- Manufacturing businesses are struggling here too

Italy: Manufacturing recovers, services slows rapidly

Both PMIs are suggesting stagnating activity and the composite index is still pointing to a contraction

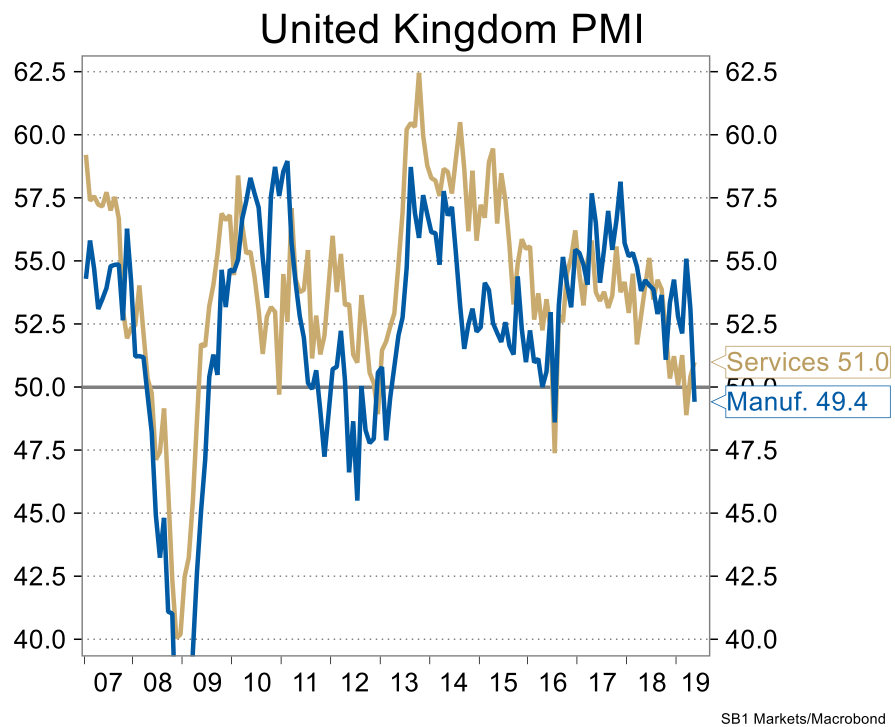


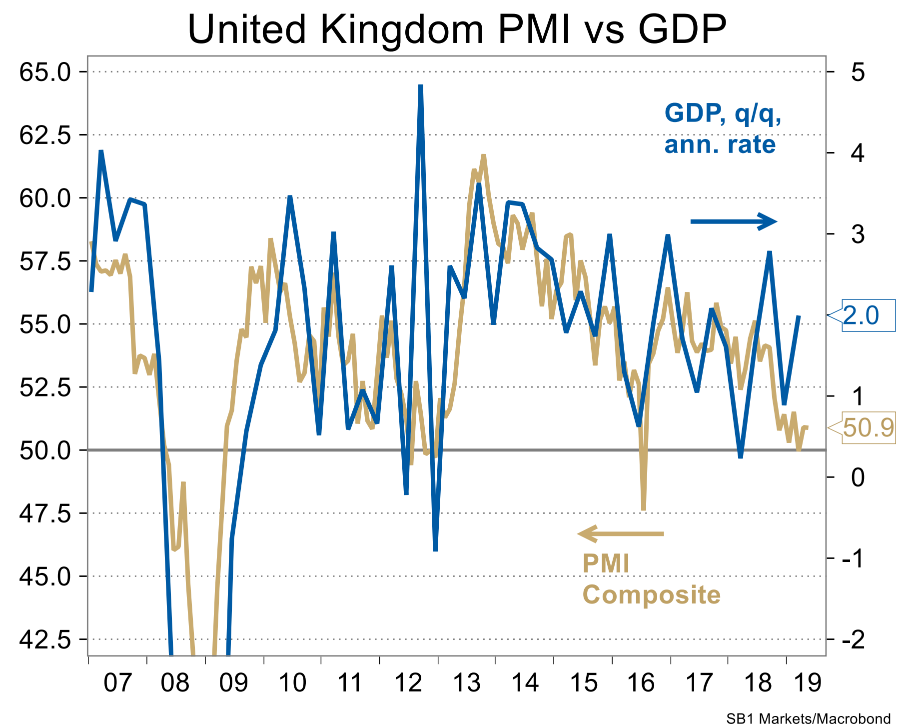


- The composite PMI rose marginally to 49.9 in May. PMI points to a modest contraction in the Italian economy. Actual GDP growth recovered in Q1 after sliding into a technical recession in Q3/Q4. The PMI suggests that the upswing might have been temporary, however, the correlation to actual growth is not that strong in the short term
- The government expects 1.5% growth in 2019, to keep the budget in check. Seems very unlikely at this point

Composite PMI still in growth territory, huge downside risk

Manufacturing plunged to 49.4, as businesses are building down pre-Brexit deadline inventories



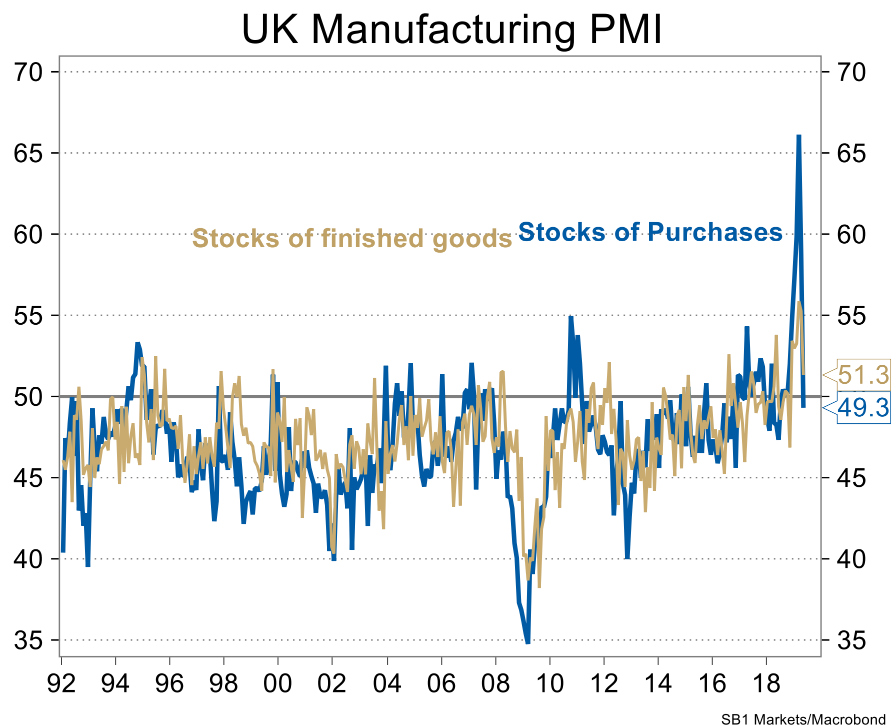


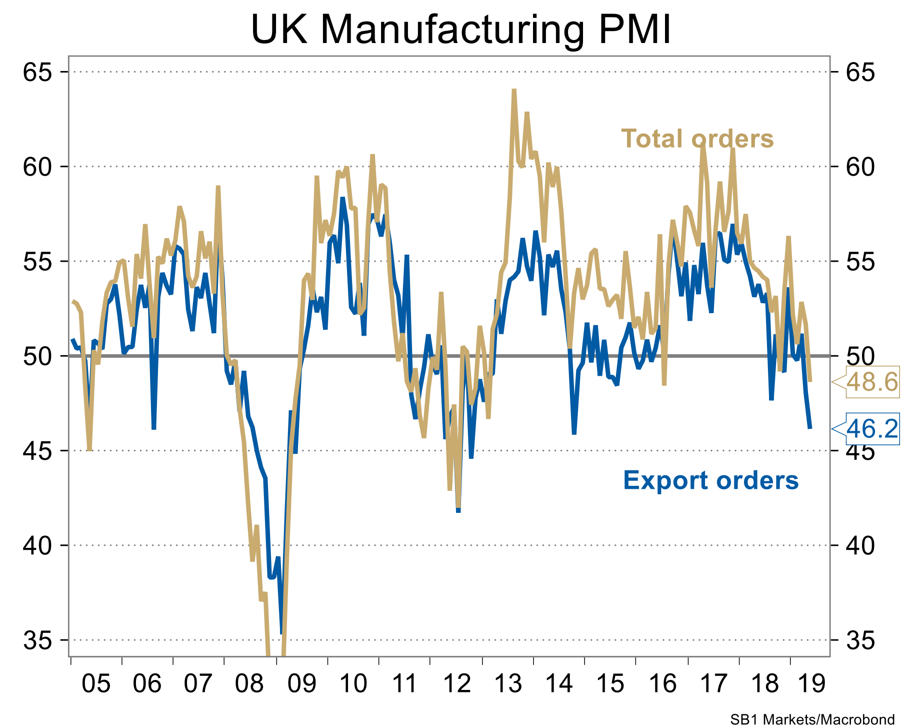
- Manuf. PMI tumbled 3.7 p in May, to the lowest level since the Brexit referendum. Manufacturing activity has been held up by massive efforts to purchase materials ahead of the original Brexit deadline, <u>check the next slide for more.</u> These inventories are now <u>being wound down, contributing negatively to demand</u>
- The service sector PMI rose 0.6 p to 51.0. Businesses have been reporting more or less stagnating activity since November last year, as Brexit uncertainties have been causing postponed/cancelled spending and investment decisions
- The composite PMI at 50.9 is pointing towards just marginal GDP growth

SpareBank 1 MARKETS

Brexit stockpiling eases rapidly and orders are falling; more will come

Businesses were stockpiling ahead of the Brexit deadline, propping up activity. Now..

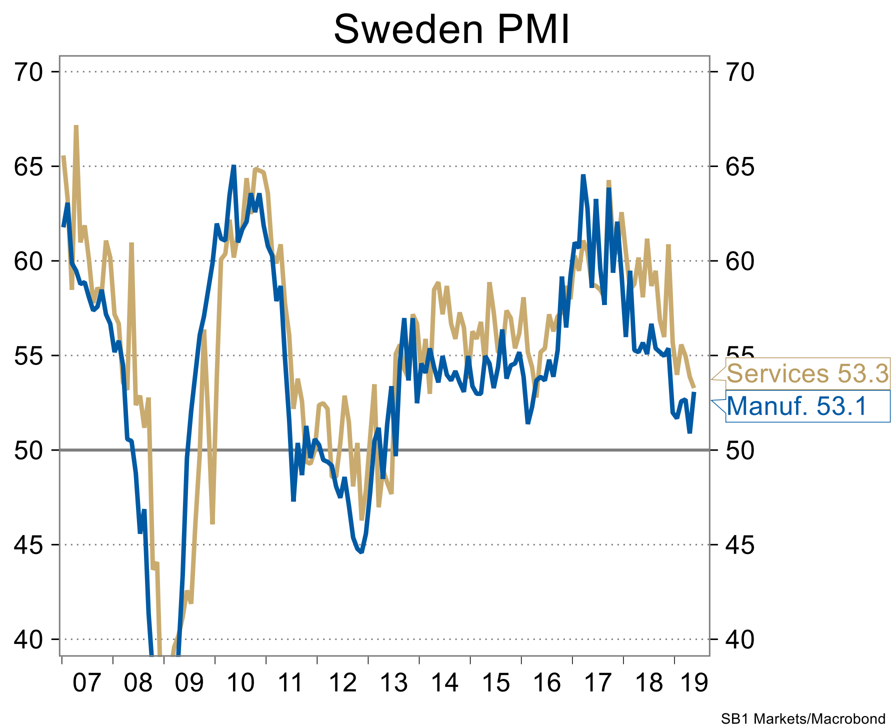


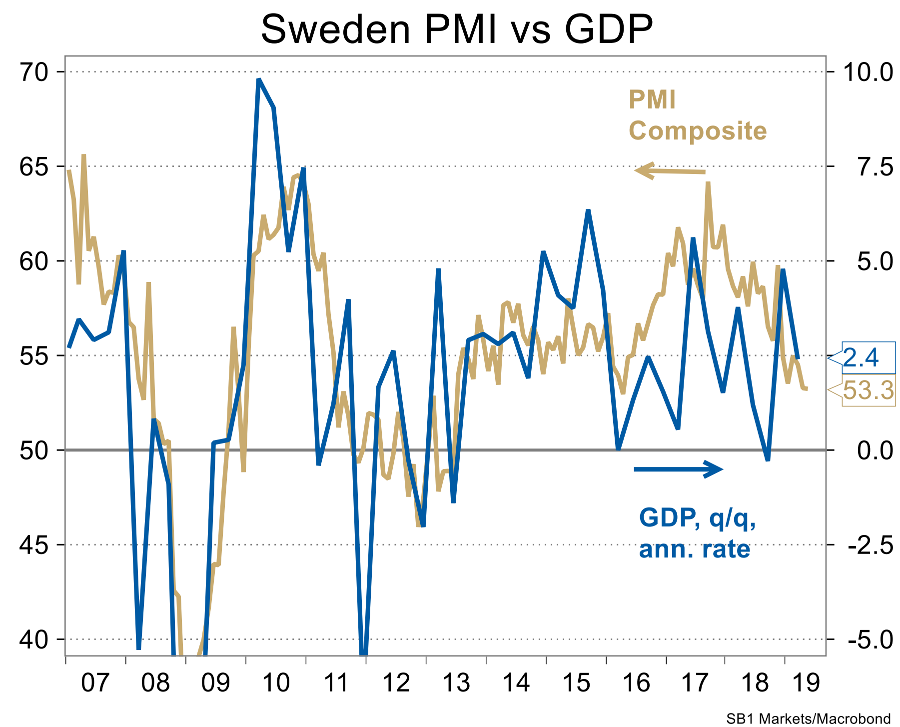


- Businesses are reporting a 3.1 p drop in the total orders index, echoing decreasing order inflows. Both export and total orders fell, implying a rapid slowdown in domestic orders. Export orders are most likely pulling back as foreigners may be starting to find new supply chain routes amid Brexit uncertainties. If so, the outlook is bleak
- Massive stockpiling ahead of the original Brexit deadline have helped support growth in orders and production recent months. The stocks of purchases index fell sharply in May but is not signaling a cut in inventories. Stocks of finished goods are still rising, albeit slower than in April. Still significant downside risk; the major inventories built up since Jan will have to be to built down, and both inventory indices are above a neutral level

Manufacturing gains, services PMI another step down

Both sectors are noting modest growth, pointing to a noteworthy slowdown

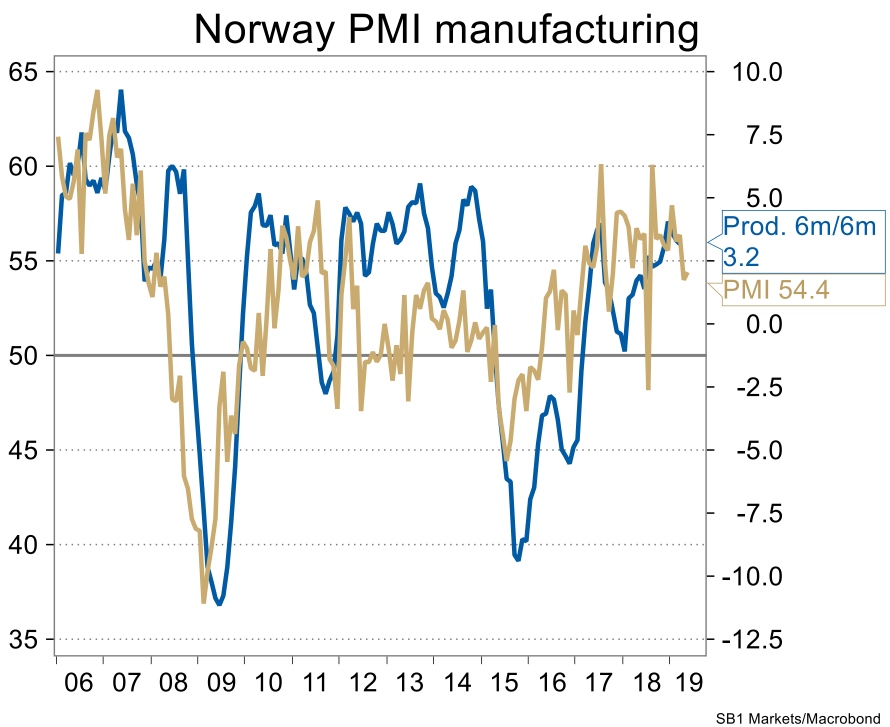


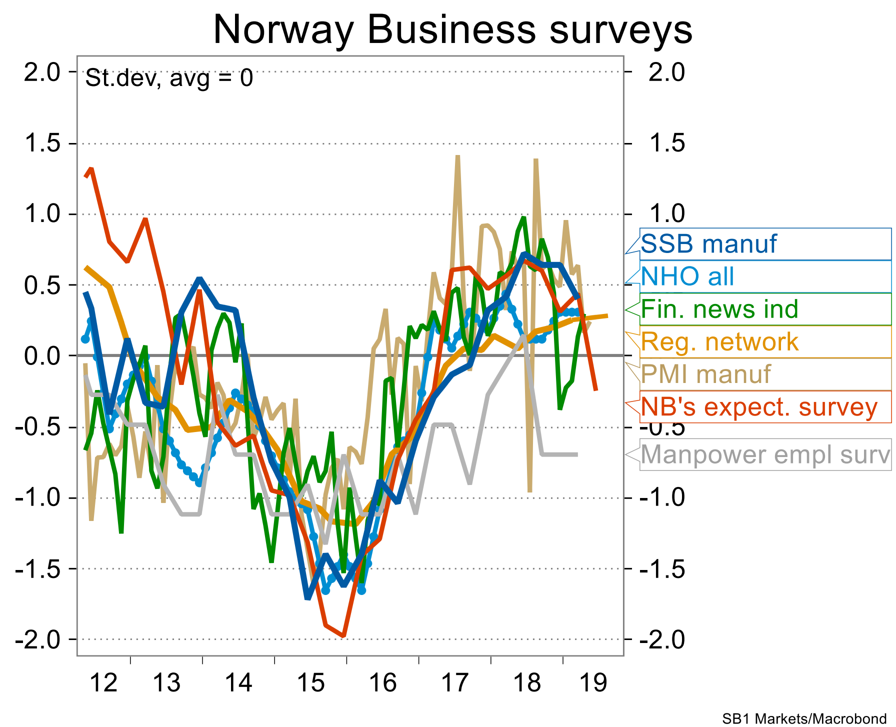


- The composite PMI fell marginally to 53.3, points to moderate GDP growth. Also, the PMI has been too optimistic vs actual growth the past 2-3 years and is now signalling growth well below the 2.4% in Q1

Manufacturing PMI improved in May, indicating moderate growth

PMI ticked up to 54.4, more than 1 p above the avg level. The index is in the mid-range of surveys

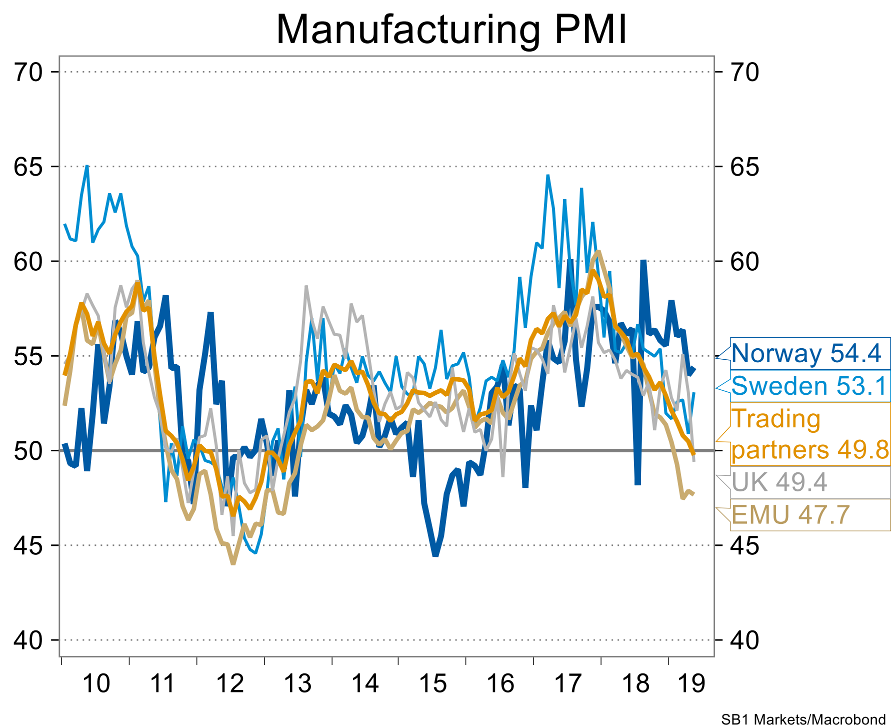


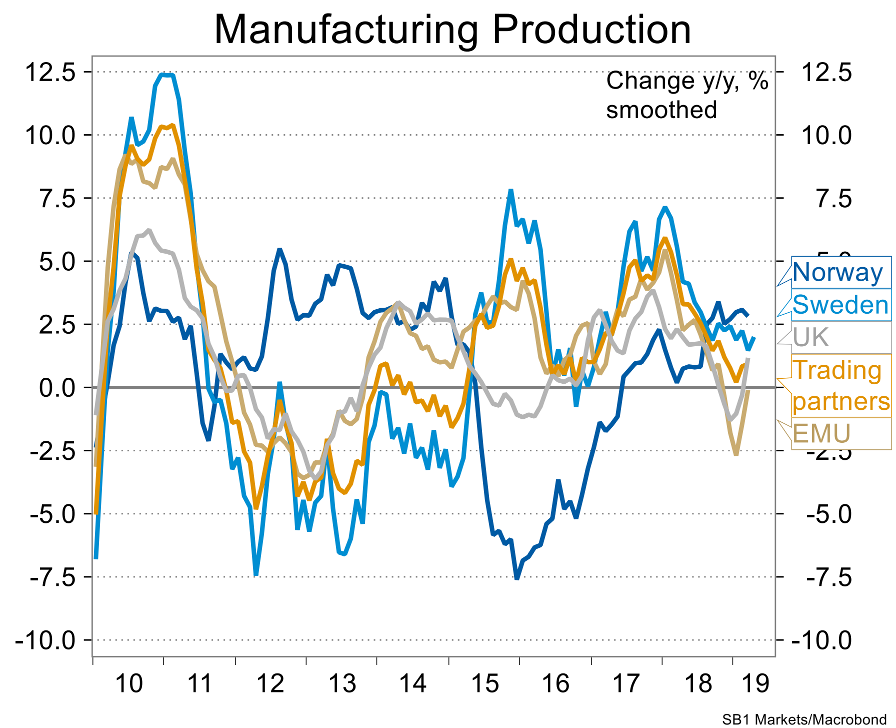


- The PMI rose to 54.4, up 0.4 p from the prior month. The PMI has ticked down recently but is still above the avg level
- In spite a small slowdown, the manuf. index is pointing to moderate growth in manufacturing production, as most other surveys are indicating, too
  - » Manufacturing activity has cooled rapidly in our trading partners, less in Norway, thanks to oil related sectors

Manufacturing activity is holding up better than among our trading partners

Norway still the winner, Norwegian manufacturers have been 'saved' by oil related sectors

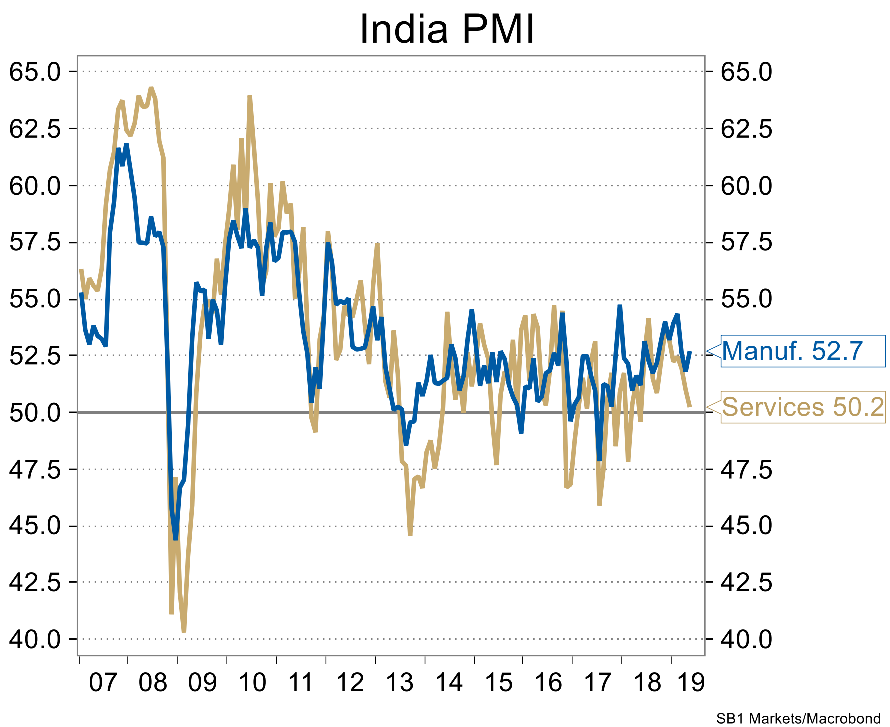


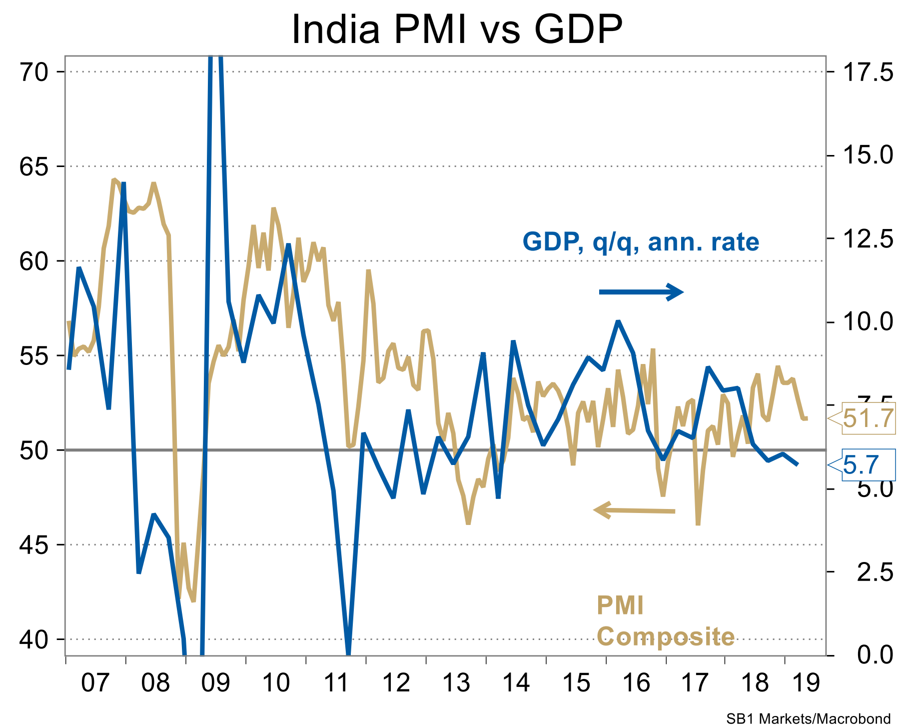


- .. Just as Norwegian companies were hurt by the oil downturn in 2015/16
- Norway has not been in sync with the rest of the world recent years

Composite PMI signals softer GDP growth (and growth has been rev. down)

Service sectors are struggling, manufacturing not that weak

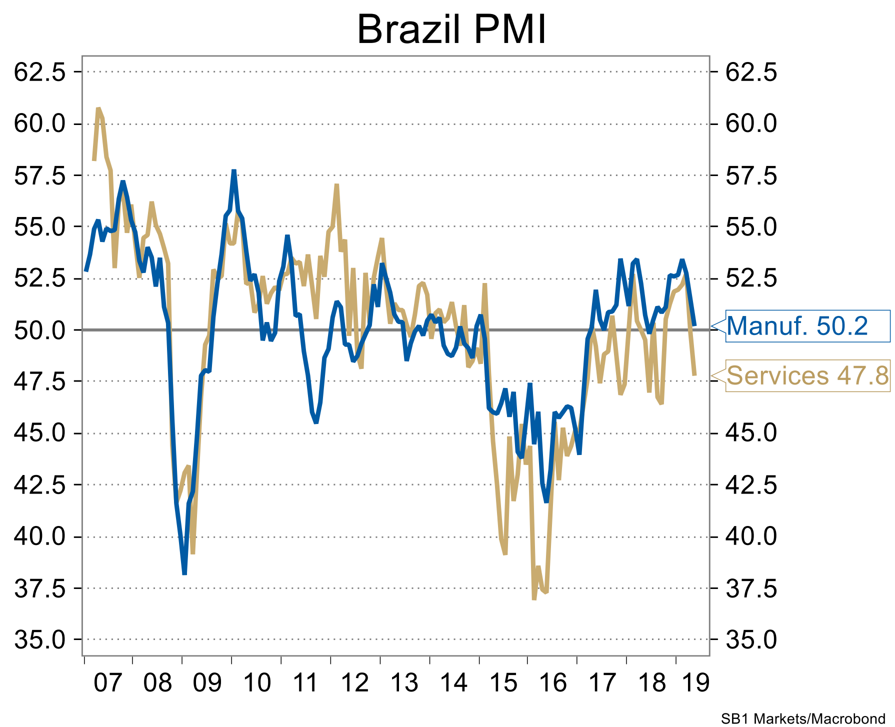


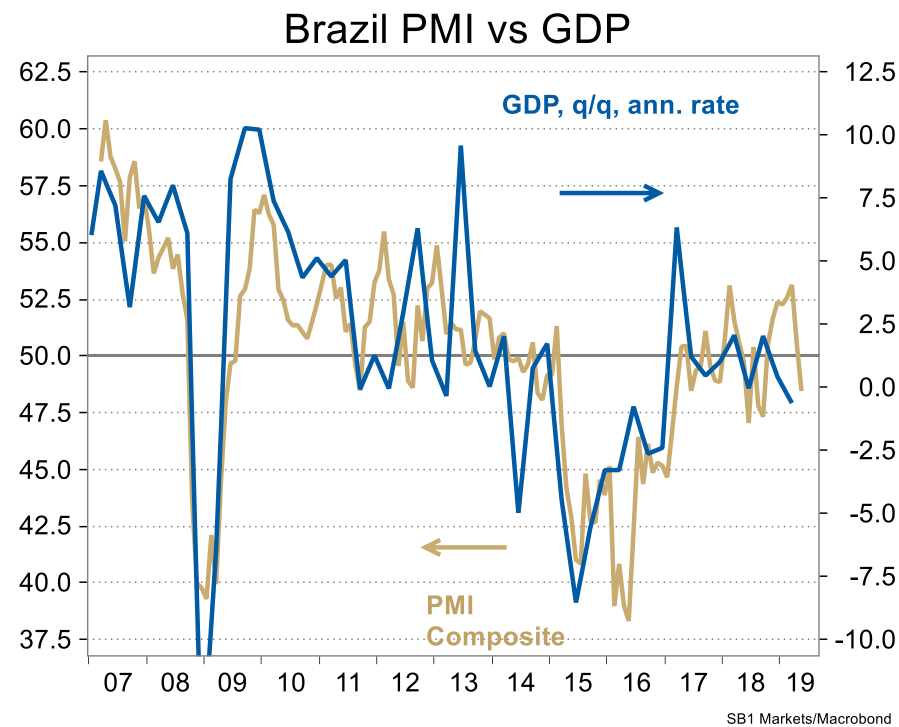


- The correlation between PMI and GDP is not very close but the PMI indicates growth at below 5%, well below the 8% growth rate recorded in Q1
- Indian GDP growth has been substantially revised down the two previous quarter, in Q1 t0 5.7% from 8.0%, which led to a downward revision even in our global GDP estimate

PMI down the drain again, mainly due to services

The PMIs do not signal that the Brazilian economy will pick up speed, composite down to 48.4

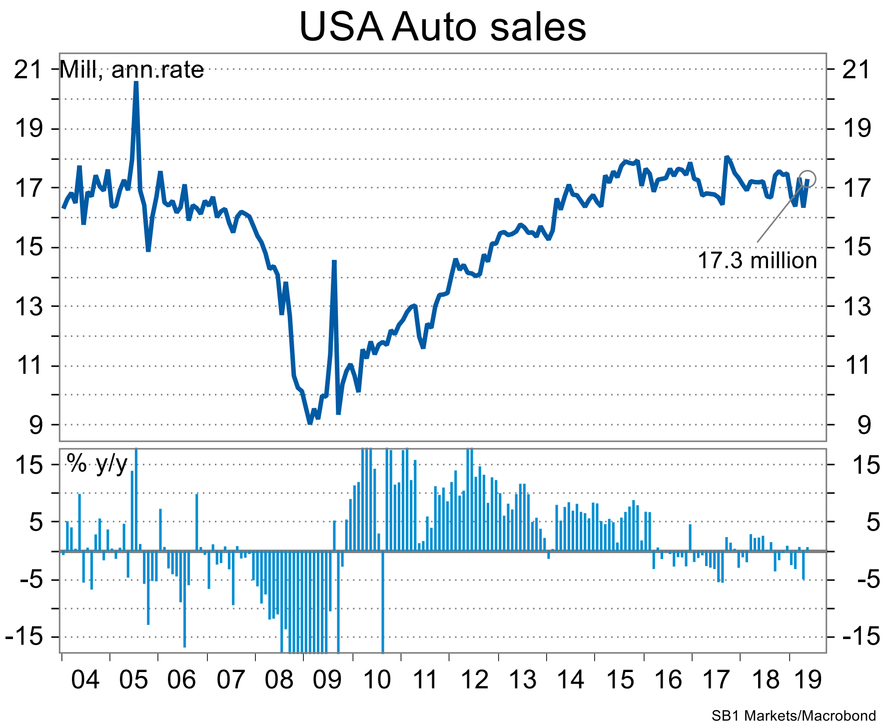


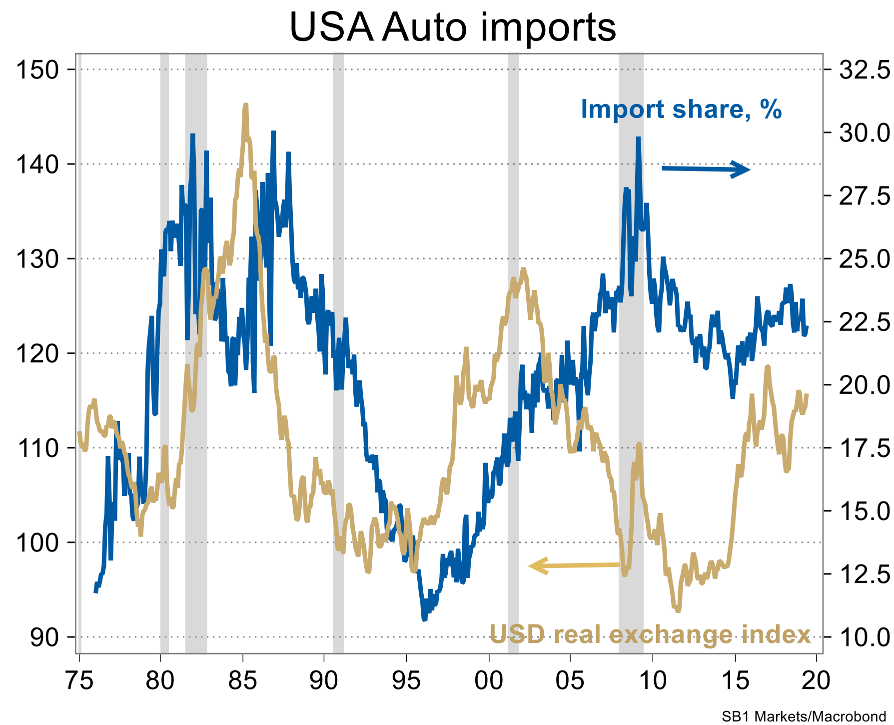


- GDP growth fell 0.6% q/q (ann. rate) in Q1, the Brazilian economy has been troubled by political and financial challenges. The PMI is signalling subdued growth, no recovery in sight

Auto sales bounced back up in May, trend slowly downward?

Sales recovered more than expected from the April slump, up to 17.3 mill (annualised)





- Sales were not strong in Q1 and will not thrive in Q2 either, if June does not surprise on the upside. The trend is flat, at best
- The import share rose marginally in May. The share has increased somewhat past 3 years, and is above the long term average – but it has been far higher several times before. The sharp USD appreciation to 2017 from 2012 may explain the increase
- No signals yet from the White House on (Trump has said 25%) auto tariffs based on 'national security' analysis produced by the Commerce dept. However, the Mexico tariffs, if imposed, will hurt auto industries (and US consumers)

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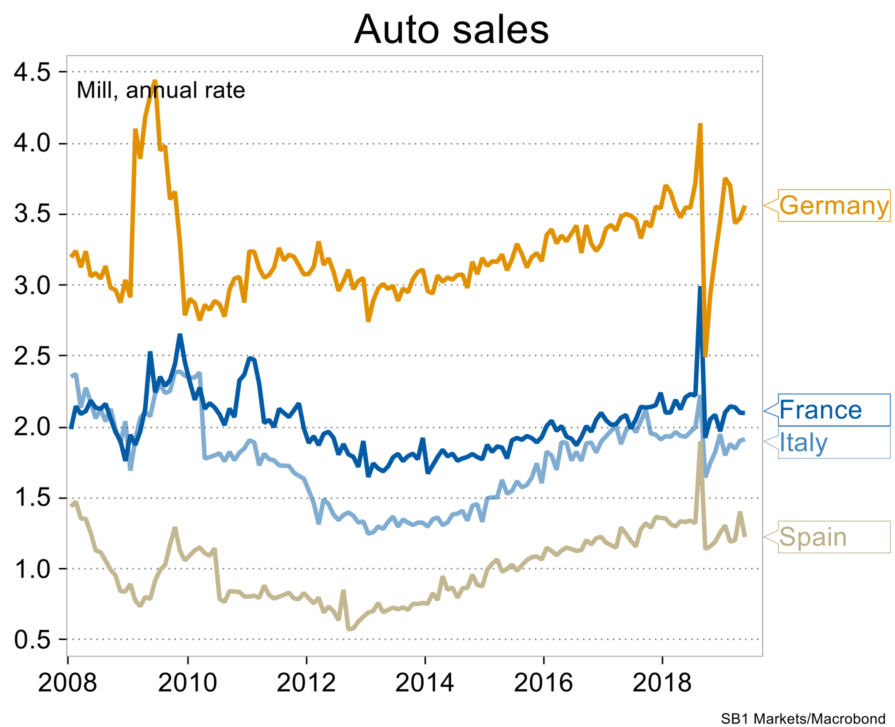
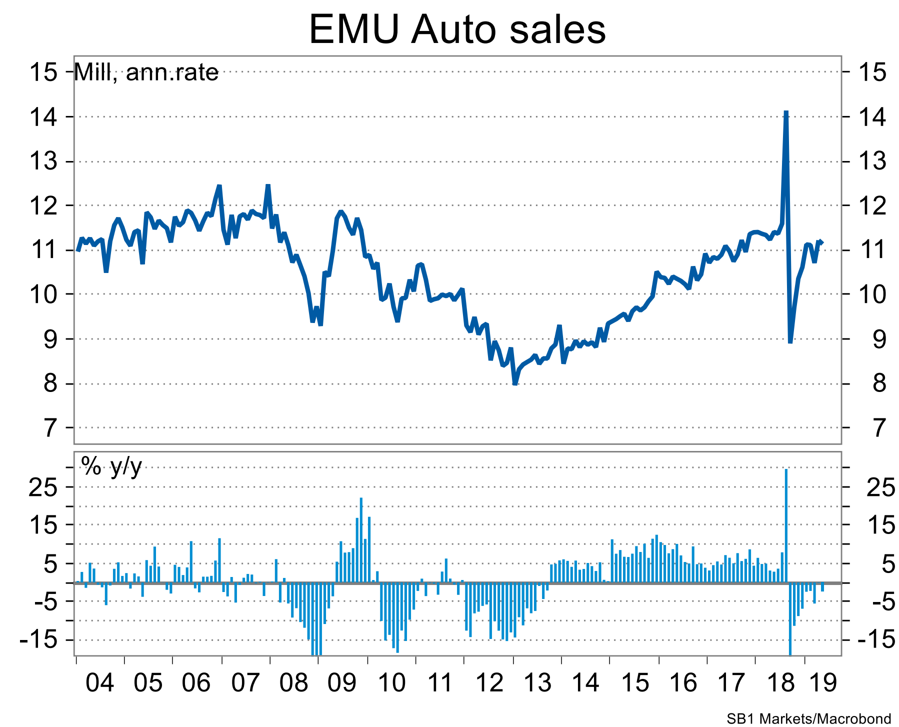
EMU: Auto sales probably marginally down in May

Sales up in Germany, France & Italy flat, Spain down. All are below pre-Sept levels

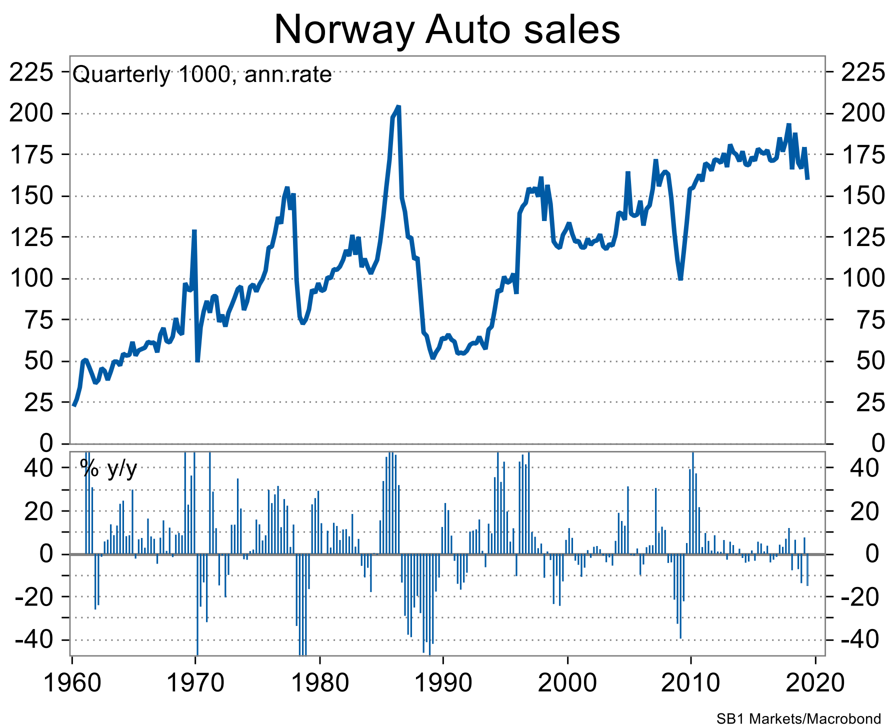


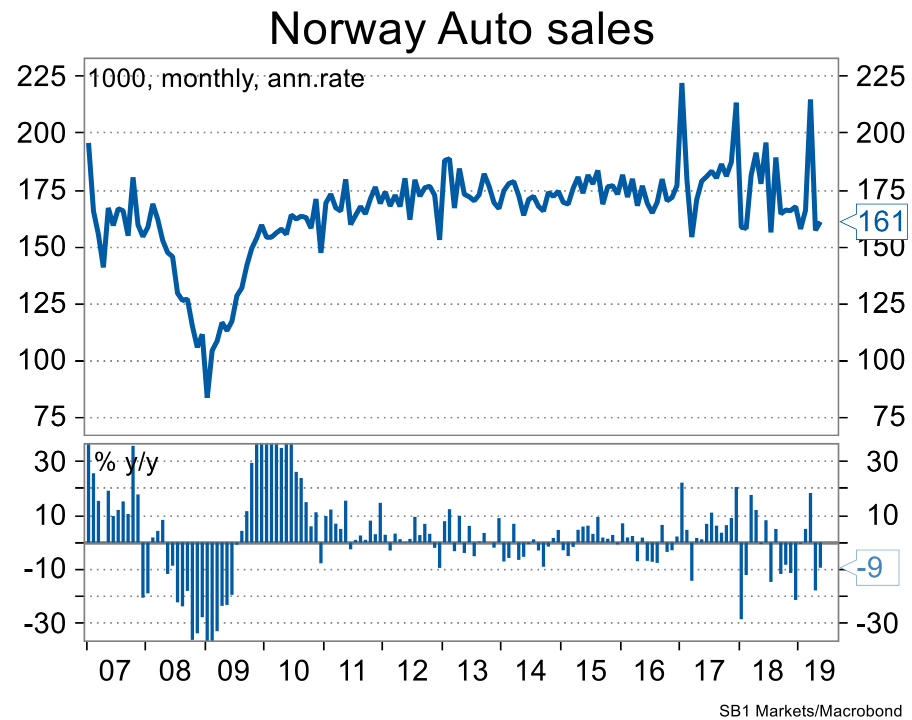


- For EMU total, we assume sales fell some 0.7 % in May, due to the 15% decline in Spain
- EMU sales are some 4% below the level before the new emission regulations hit. German auto production is still almost 20% below the pre-regulation level. Incredible!

'Tesla' effect reversed, auto sales back to a 'normal' level

Sales rose marginally to 161' in May, vs 200'+ in March. The trend is most likely down the past year

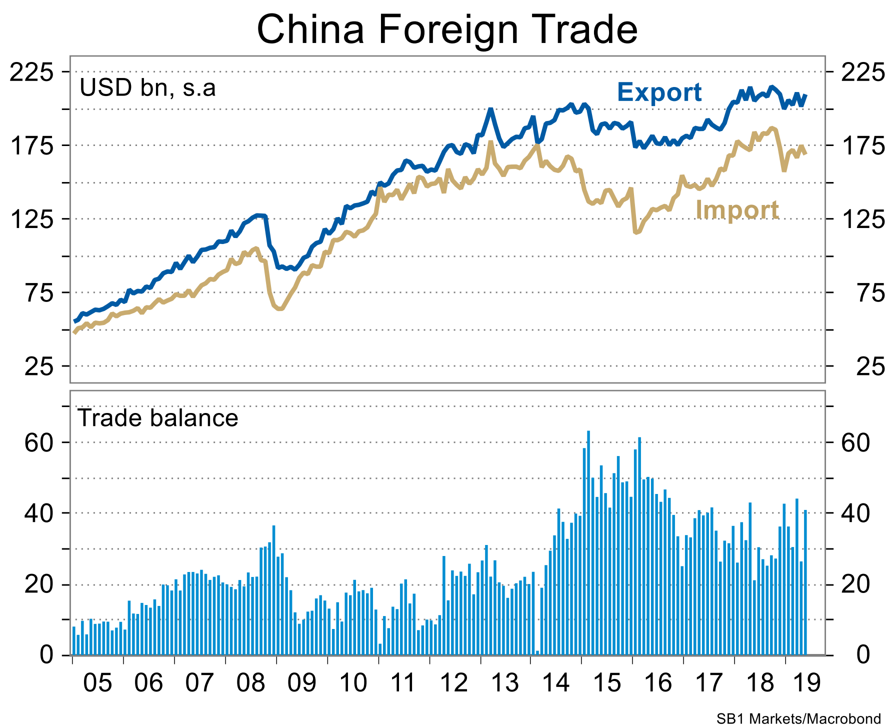




- The spike in March was due to deliveries of 5000 Teslas (60' in annual rate)
- There are still long waiting lists for many popular electrical vehicles, and the actual level of new registrations may still be lower than the actual sales rate – at least there are many cars to be delivered coming months
- Still, the trend in sales are pointing slowly down?

Both exports and imports are recovering

Exports & imports have stabilised after the drop last fall. Exports -6.9% y/y in April, imports +1.1%



- Exports were reported up 1% y/y in May (in USD), expected down 4%. Exports rose 4% m/m, and is now slowly recovering from the Q4 local through, both in value and volume terms. The trend since early 2018 is close to flat
  - » Exports to the US rose in May, but is sharply down y/y, the tariffs hurt exporters. Still total export volumes are flat. Exports to other regions have filled the void. A further escalation of the trade war, which Trump (and then China) decided in May will no doubt dampen Chines exports to the US further.
- Imports are down 8.5% y/y in May (in USD), exp down 4% - and imports fell somewhat m/m. However the trend is slowly up from the weak Q4, even if both value and volumes are down y/y and both are down from the Q3 peak
  - » Imports are down from the peak, and are indicating weaker domestic demand
- The trade balance was much stronger than expected, at USD 42 bn, exp 24 bn. The seas. adj. balance is at USD 40, trending roughly flat.

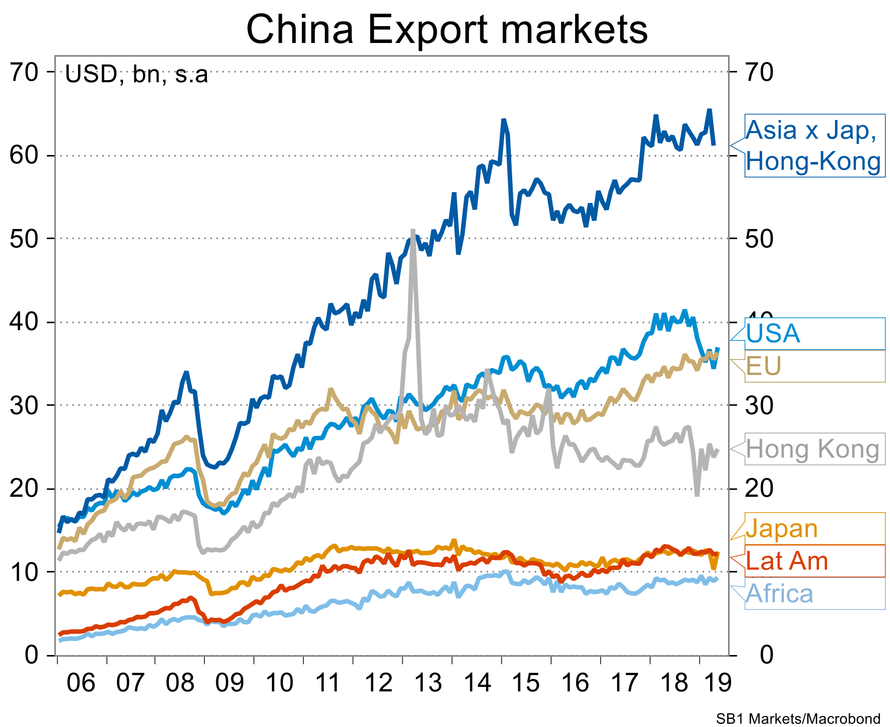
Export surveys are signalling stalling exports but no collapse

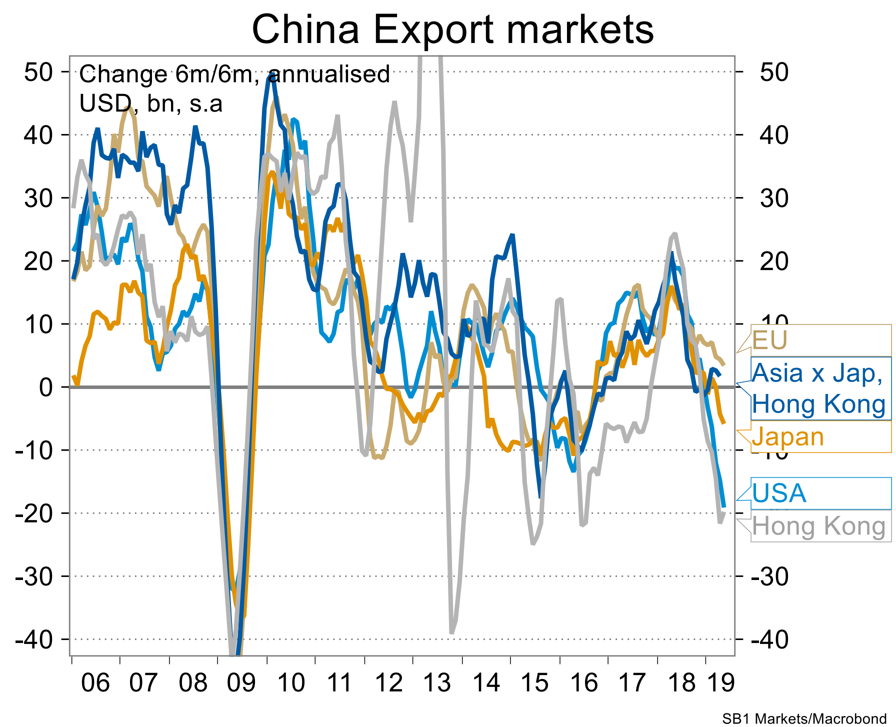
A slowdown/marginal decline has been signalled, as in 2011, ’12, ‘13, and ‘15

- .. And actual export volumes fell in 11/12, were flat in 13 and fell in 2015 – <u>without creating huge problems in the Chinese economy</u>
- Now, exports are close to flat y/y

Exports to the US down 12%

Exports to the US rose sharply in May, but well down from the level before tariffs were implemented

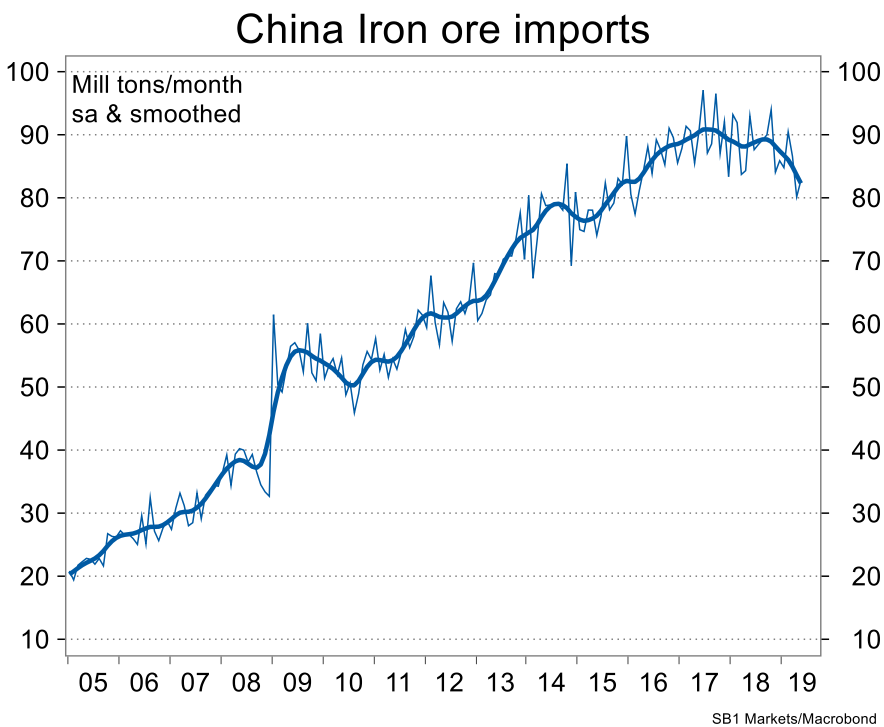


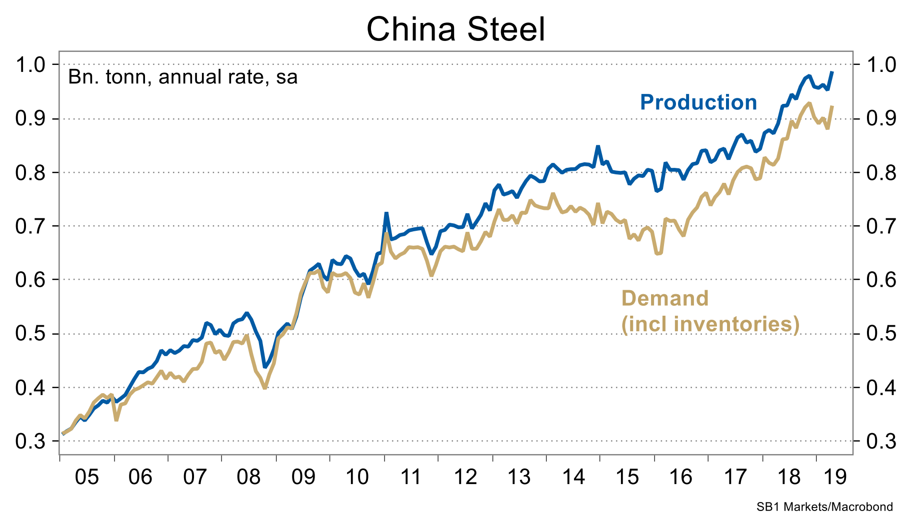


- Exports to the US is very likely hurt by the tariffs, now down some 12% since last autumn. The increase in tariffs to 25% from 10% on USD 200 bn of imports from China will no doubt lower Chines exports to the US further
  - Exports to the US equalled 18% of total Chinese goods exports (and exports to EU 16%, rest of Asia 48%, all before US tariffs)
    - Total exports equal some 20% of GDP, exports to the US 3.6% of GDP – now down 12%, shaving a gross 0.4% from GDP growth (however, dampened by lower need for imports as inputs for these exports). The total trade surplus in volume terms is up, as imports have fallen – and net trade is supporting Chinese growth
    - The real economic risk for China & elsewhere: Trade rule uncertainty may hurt investments as companies may postpone investment decisions until the dust settles – and both Chinese and foreign company may reallocate to other countries. The tech war will of course increase the risk Some households may become worried too
- Exports to Asia ex Japan & H-K fell in April (no May data)

Iron ore imports are trending down, less imports from Brazil

Net steel exports further down in May, but are still too high? Domestic demand up

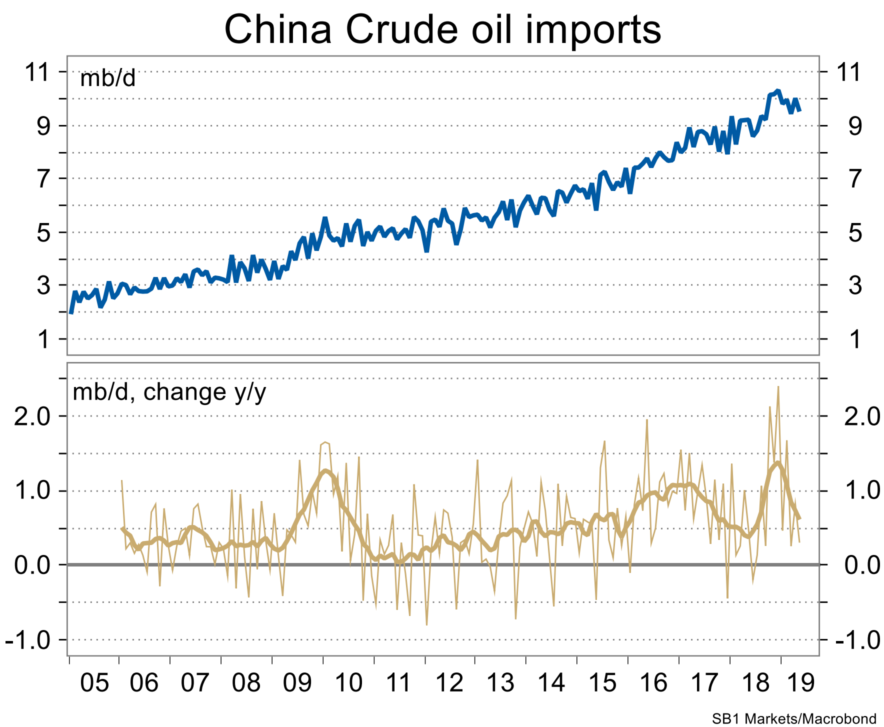


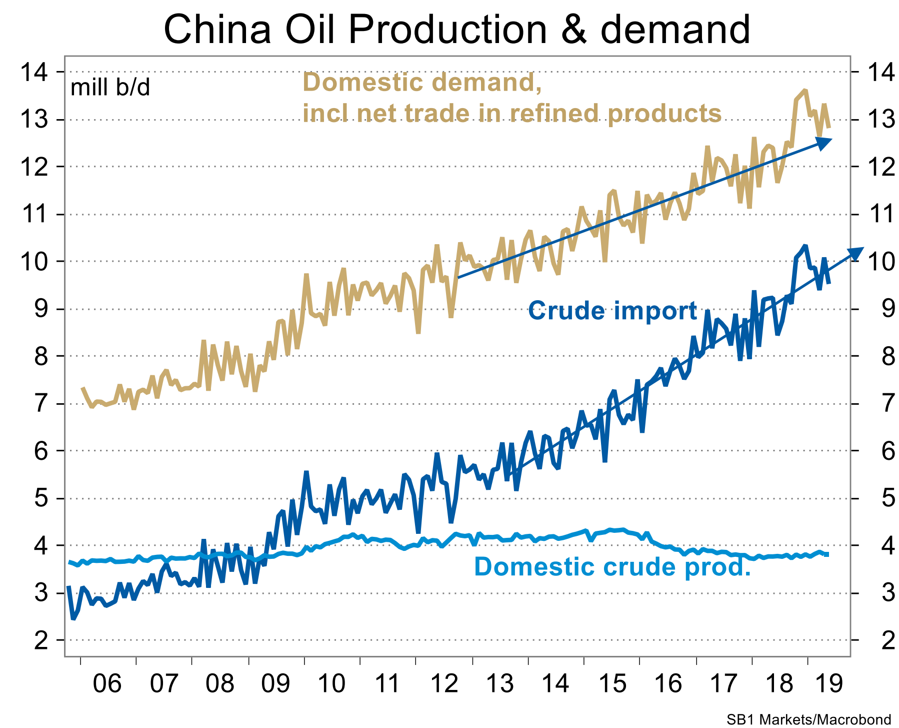


- Chinese steel production rose in April (no May data), as did domestic apparent demand. Iron ore inventories in China are probably declining
- Net steel exports equals some 6% of Rest of World production, and is trending up again – most likely not sustainable

Oil imports (and demand) down to the old growth path

Crude imports soared last autumn, and have fallen so far in ’19 – still at normal level (at least)

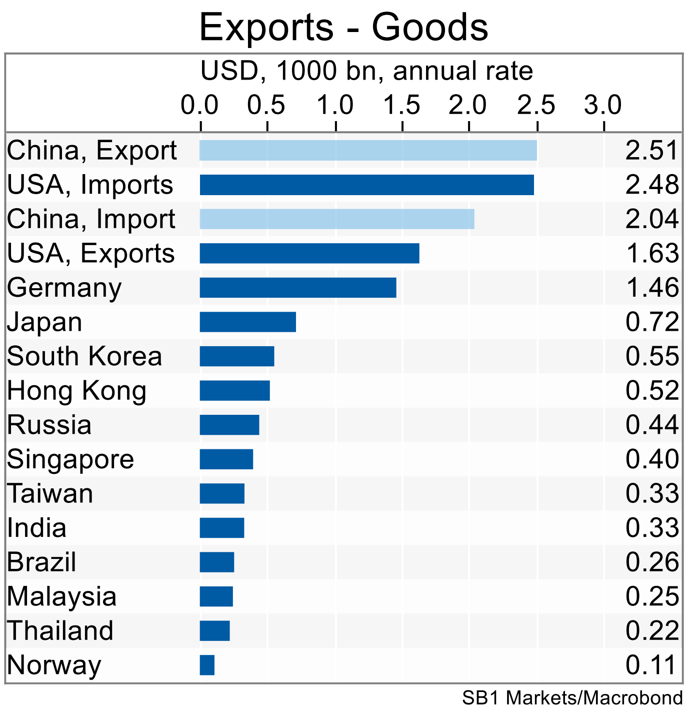


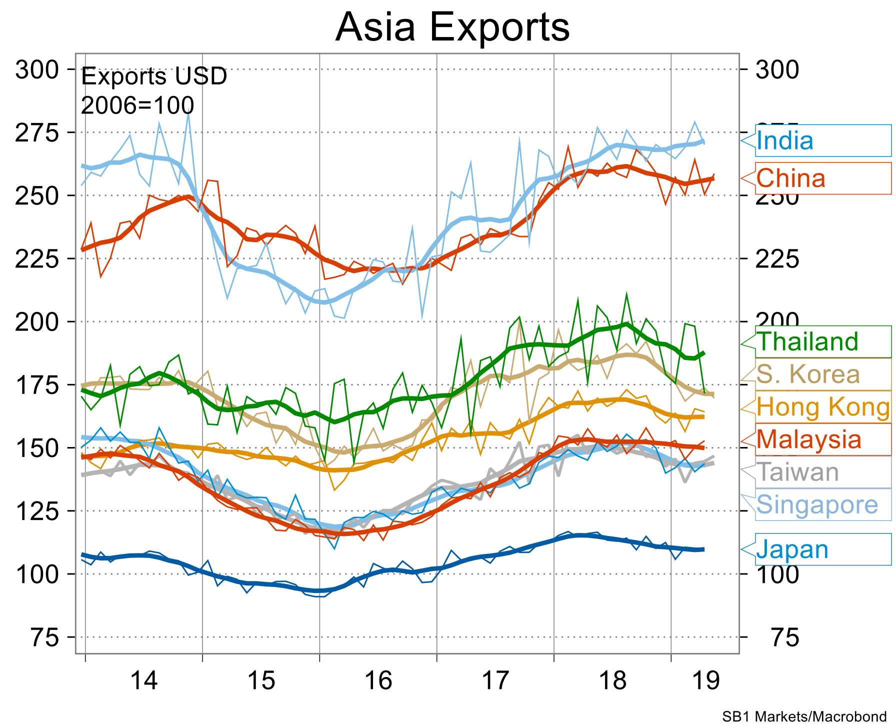


- Chinese crude oil imports were up 0.3 mill b/d y/y in May, have fallen from incredibly high growth rates last autumn, at 1.5 mill (and even higher) b/d.
- Beside reporting errors, just an aggressive stock rebuilding can explain the unprecedented increase in imports through 2018; it is highly unlikely that end-user demand could have been that strong. If so, the recent slowdown in imports does not signal a weakening of final demand for oil in China

Asian exports turning south again?

Some better data points earlier this spring – but now most arrows are pointing down

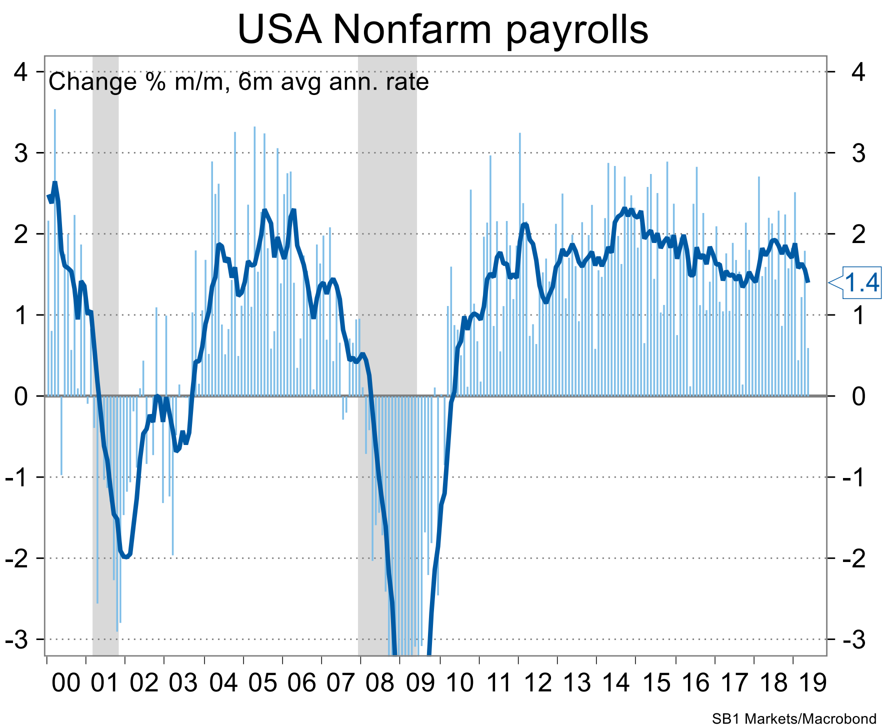


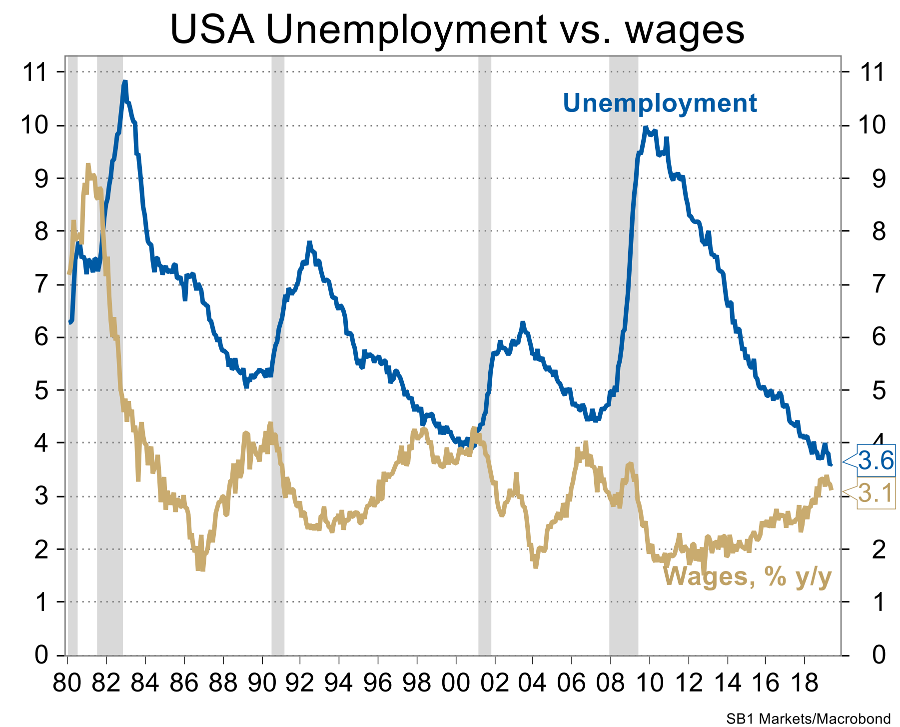


- China is of course the world's biggest exporter country (50% larger than the US!) – and the 2nd biggest importer
  - » China will take the pole position in imports too, in some few years time

Employment stalled in May and wage growth eased, may be a sign of slowdown

.. But don't panic, there are no indications of a meltdown at this point. However, at some time…

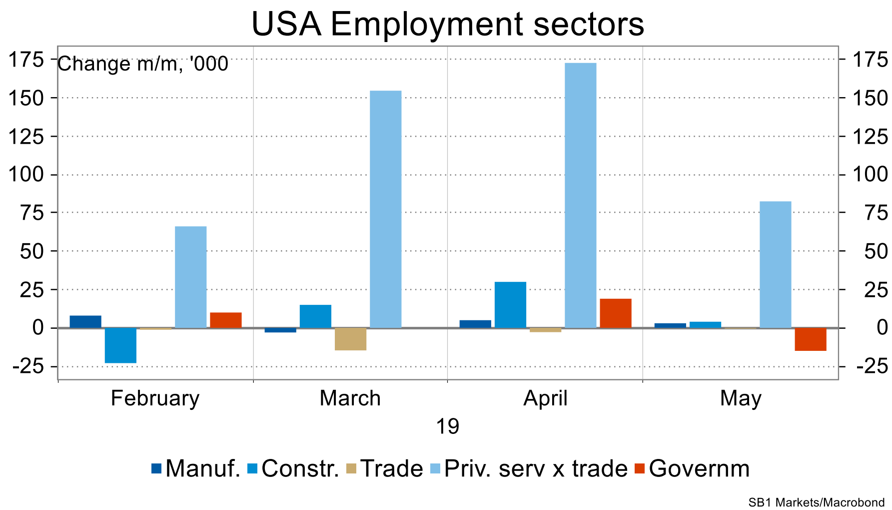


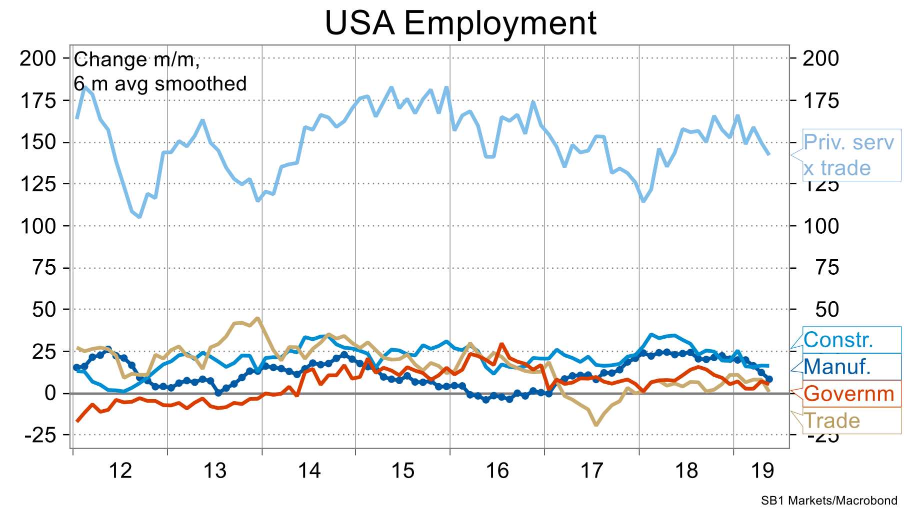


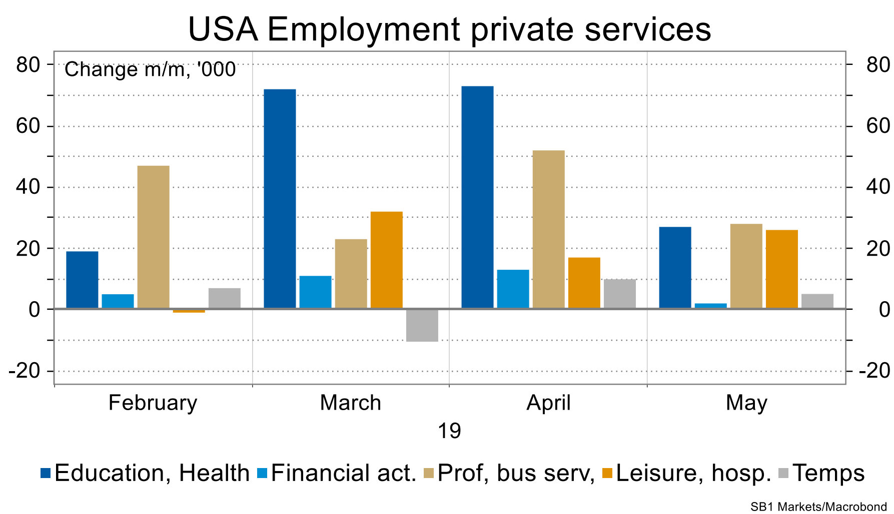
- **Employment** rose by just 75' in May, 100' below expectations, which were shifted down as the ADP data pre-warned the slowdown. Moreover, April was revised down by 60', the avg of the two months is a moderate 140' rise. The 6m average growth rate has fallen to 1.4% from close to 2%, employment growth is no doubt slowing. Nonetheless, over the past months employment has been expanding at a solid speed, which will not lead to a higher unemployment rate
- **The unemployment rate** held steady at 3.6%, the lowest rate since 1969 – and the trend is still down
- The labour market **participation rate** was unchanged at 62.8%, the upswing late last year into Q1 has completely reversed and the trend is flat. The labour market is tight but the aggregate supply side is not responding. The employment rate held steady at 60.6%, and has been more or less stable recent months
- **Wages** rose just 0.2% m/m in May, 0.1 pp less than expected. The annual rate inched down to 3.1%, wage inflation has eased somewhat recently. Still businesses are reporting lack of labour, like never before
- **These data do not by themselves justify an interest rate cut, and Fed will have to see a more sustained labour market weakness before using the labour market as an easing argument. Wage inflation is not dangerously low**

Broad slowdown in private sector employment, the government cuts

Private services delivered some small gains



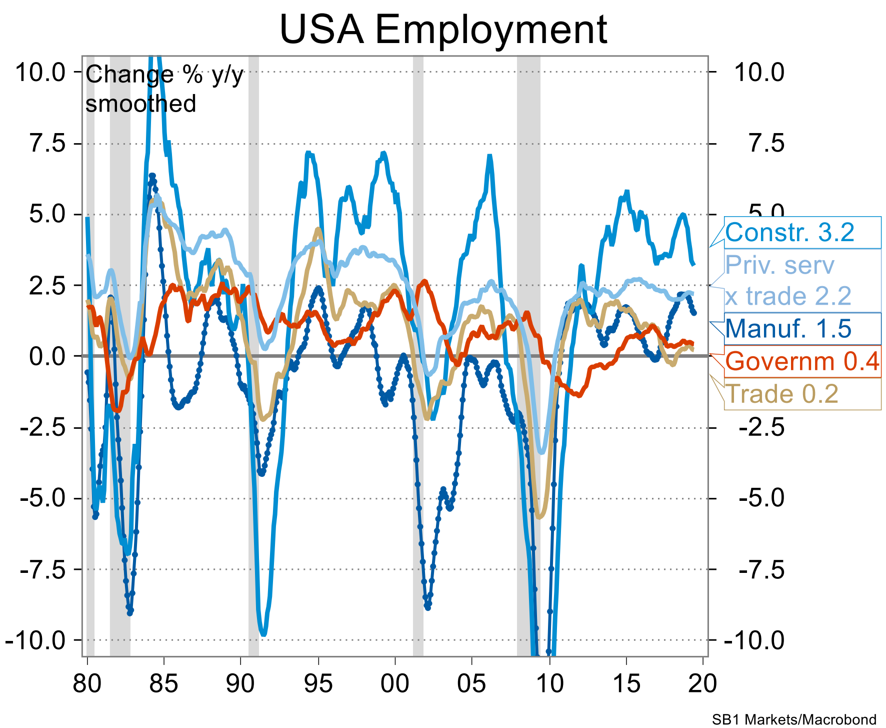


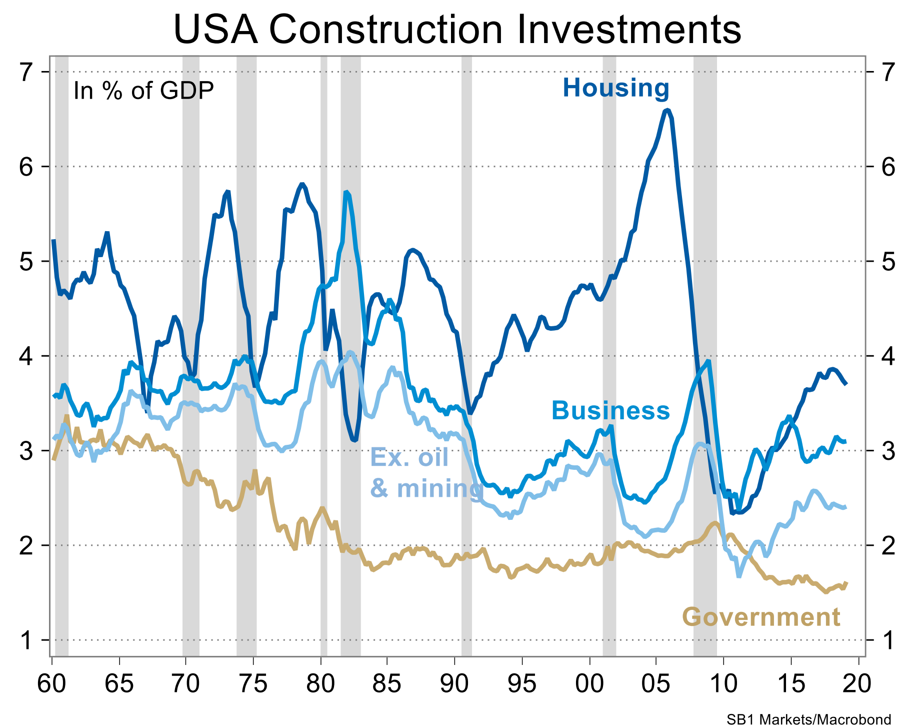


- **In May:** Manufacturing and construction noted just marginal employment growth and retail sectors stalled. Just private services up but much less than normal, only leisure/hospitality reported normal growth, while government employment declined
- **Recent months:** Employment is still growing in all sectors but trade, which is stagnating. Both manufacturing and private services have slowed, construction is easing somewhat too. Government stable
- **Big picture:** Manufacturing, construction both peaked in H1 ’18, but construction is still growing faster than normal. Private services x trade recovered last year but is now slowing again? Trade has been week since 2006 Government still below par

Construction is still the fastest growing sector (in %). For how long?

Housing investments have most likely peaked, just oil has kept business construction invest. up…





- Public construction is probably too low, but will most likely remain low – as long as nobody will pay taxes to pay for them
  - » … and growth in government employment is not that impressive either

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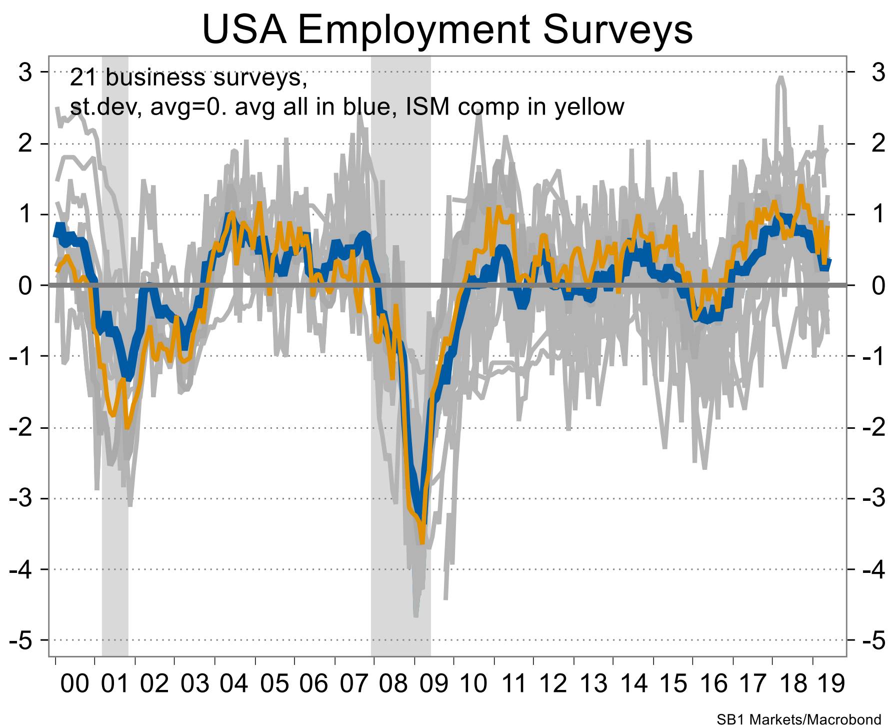
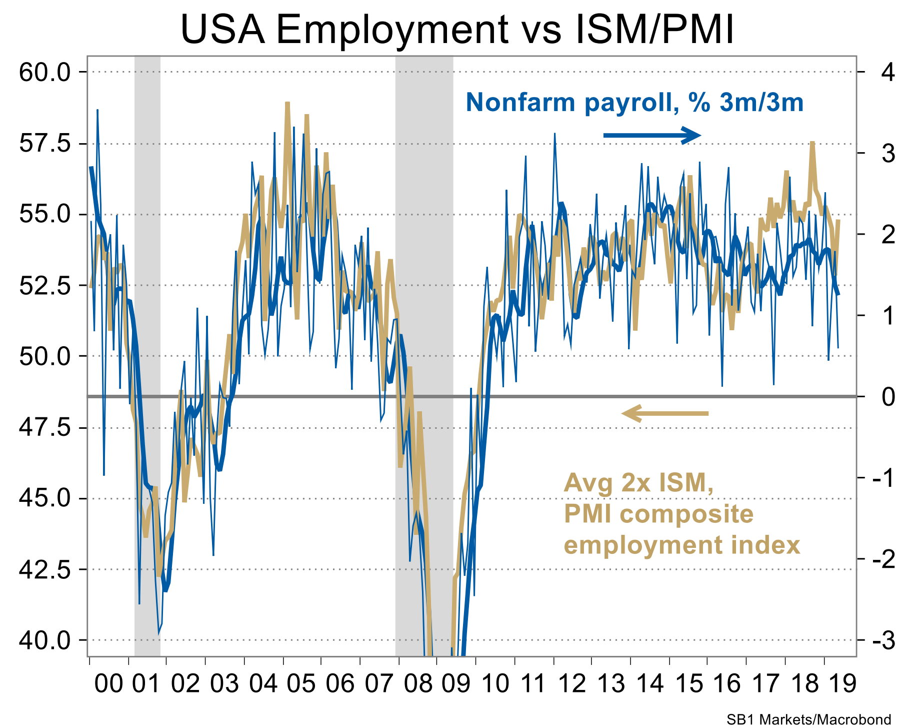
Employment surveys down but still well above average

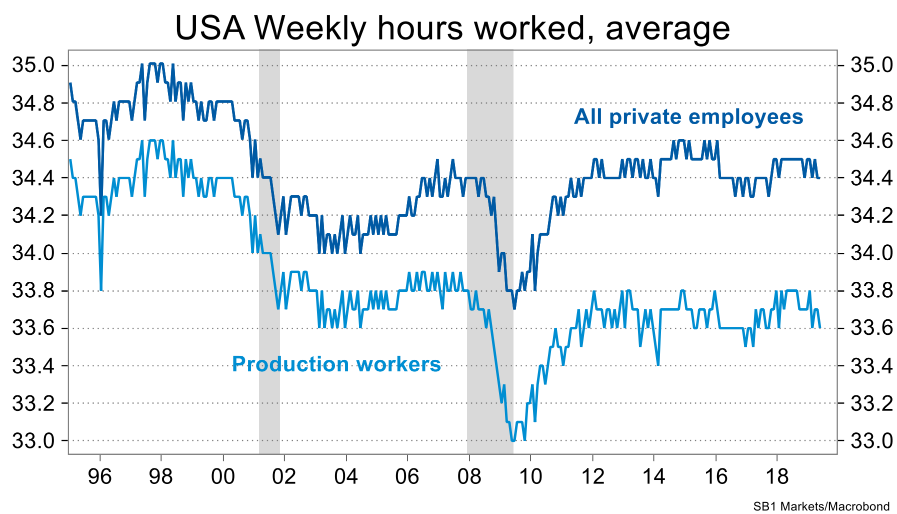
… and they are still signaling employment growth above average

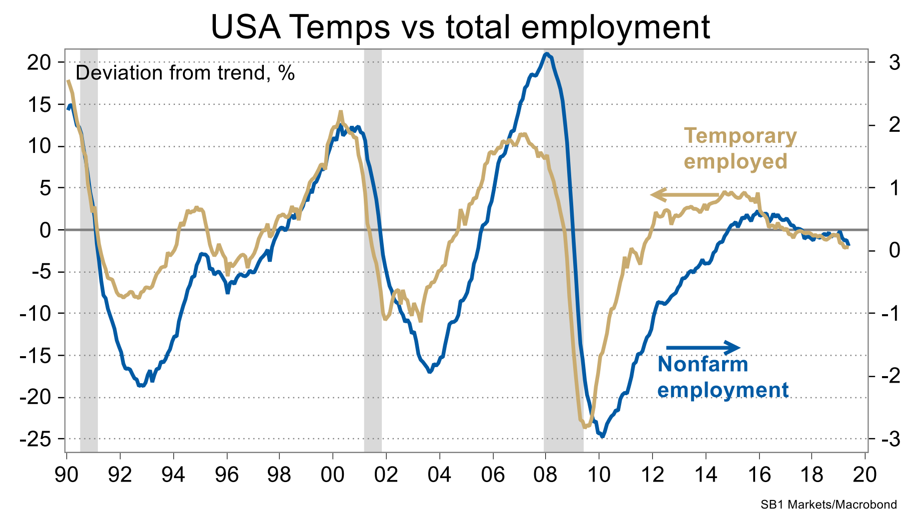


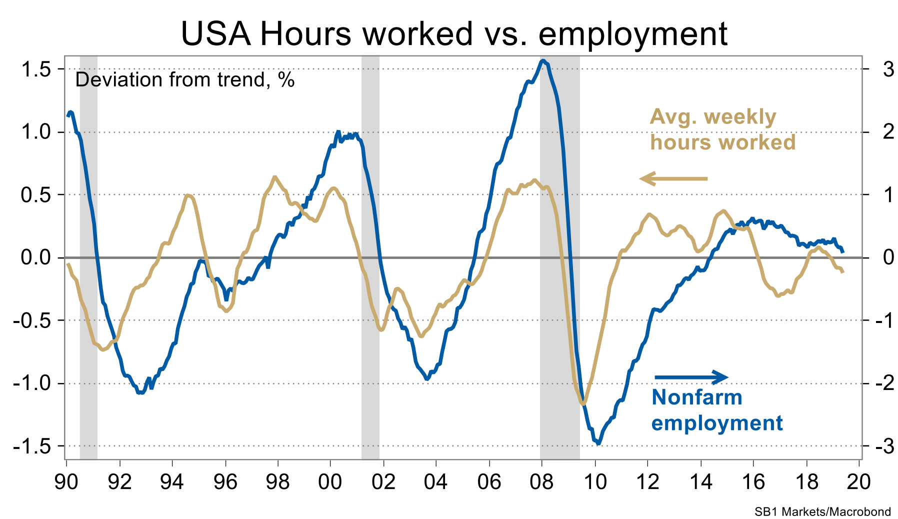


Weekly average hours unchanged in May, slightly down recent months

The long term trend (from 2012) is quite flat



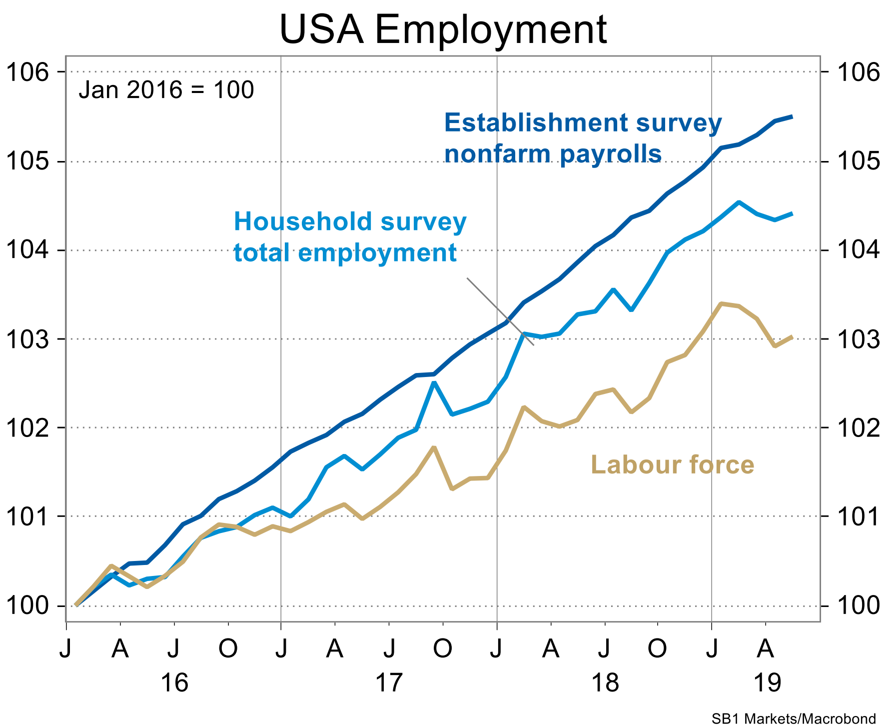




- Average weekly hours worked have slowed since last summer and is now growing just below trend
- Total hours worked rose by 1.3% in Q1, productivity accelerated to 1.9%, higher than the 'normal' rate recent years, in which productivity has been muted
- The number of temporary is waning, usually a leading indicator for future slower total employment growth

Household survey confirms slower employment growth. Participation weak

Total employment rose by 113' according to the Household survey, losing some steam the past 3 m

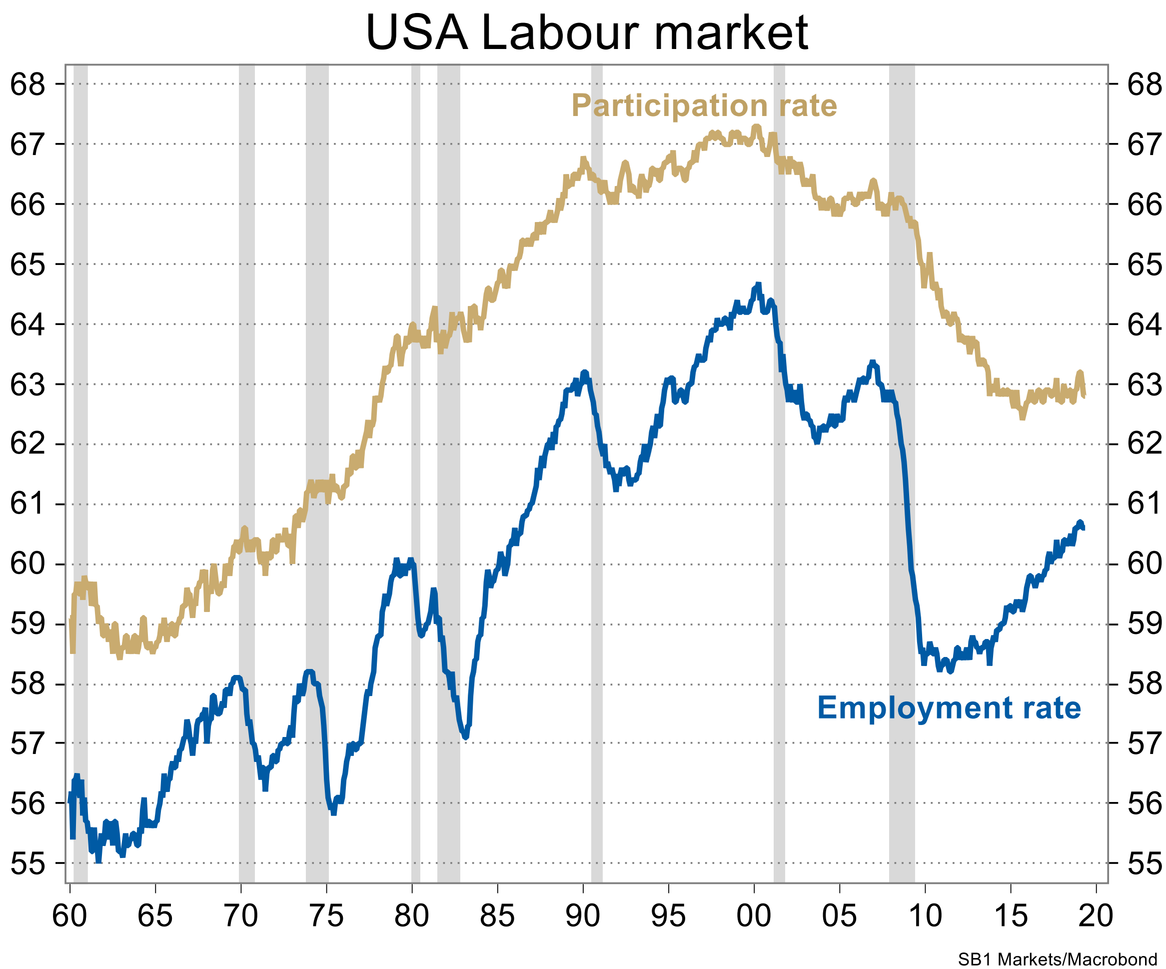


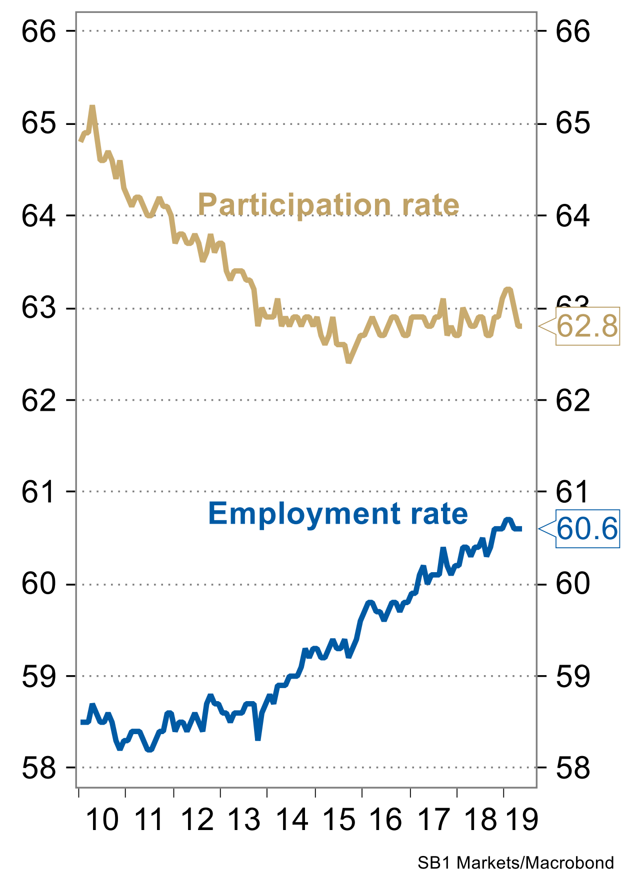
- Household data have reported a marginally slower growth in employment than payrolls, but growth has not slowed dramatically, if smoothed somewhat
  - » Total employment grew by 113' according to the LFS ('AKU'), while employment defined as the payroll report fell by 166' but this segment has been 'too much' up over the previous months
- The labour force rose in May, after falling the prior 3 months. The participation rate has fallen back to a normal level, check next page
- Monthly household survey employment data are more volatile than nonfarm payrolls data, and not useful from month to month (and in some months the payrolls data are not representative either!)

Household survey data are adjusted for the 800.000 downward revision of the 16+ year population from Jan. 2019 (due to lower immigration than assumed)

Participation has pulled back, supply is not responding at all?

The participation rate was turning up, now all of it is reversed! Unchanged at 62.8% in May

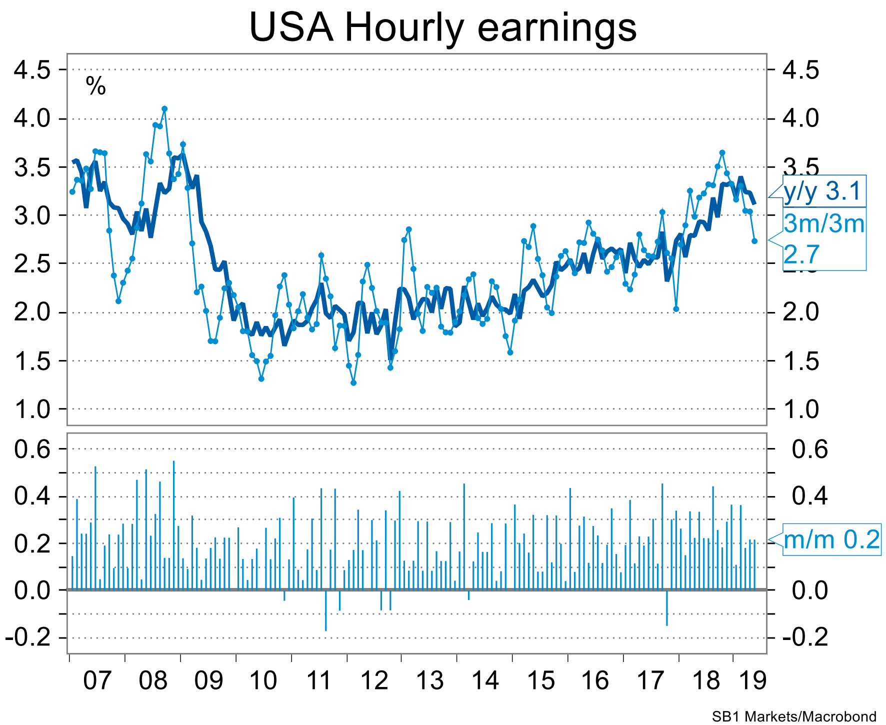




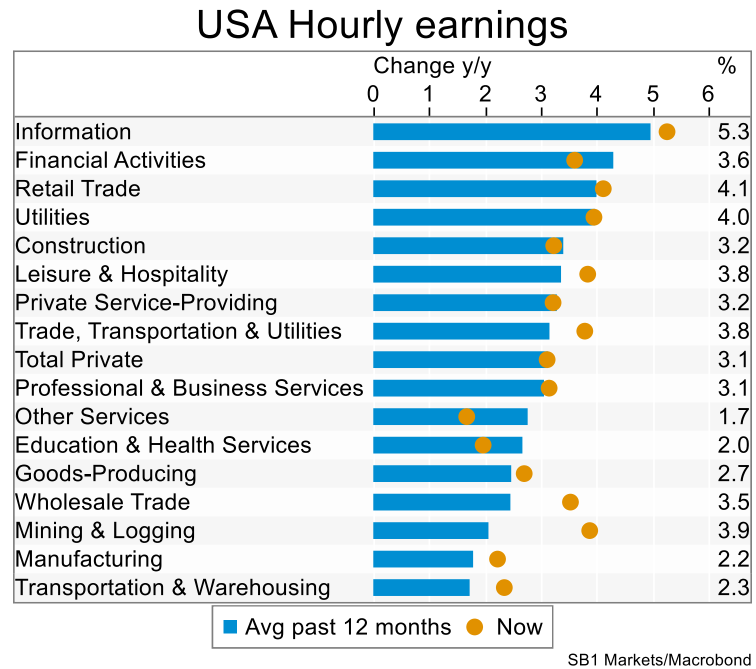
The employment rate has been unchanged at 60.6% the past 3 months. The level is well below the pre-financial crisis levels

Wage growth is cooling somewhat, the 3rd month of deceleration

Wages rose 0.2% m/m, 0.1 pp below expectations and the annual rate inched down to 3.1%



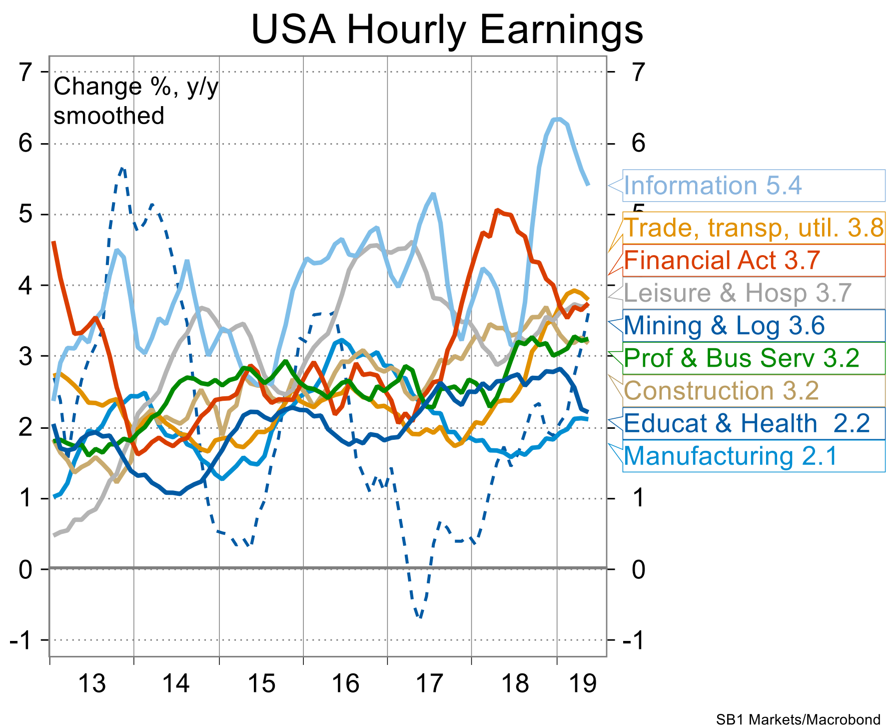
- Wage inflation is not high vs historical standards but it is not low vs. underlying CPI inflation and probably not vs productivity growth, see three pages further out. In addition, companies are not reporting slower wage growth to surveys

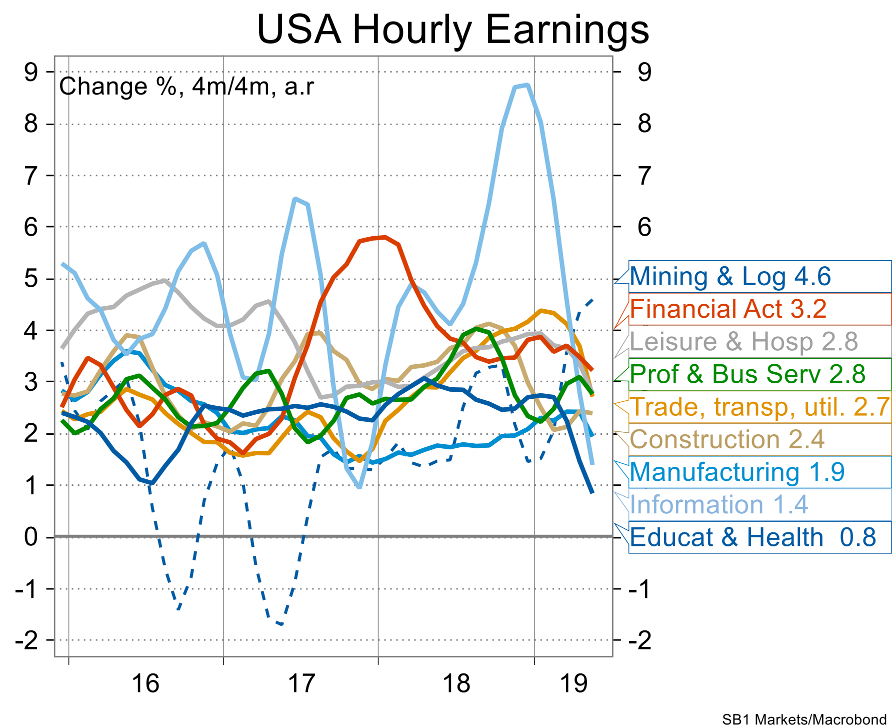


- Measured by the 3m/3m, wage growth has cooled to 2.7%, the lowest in more than a year, and down from a 9 y high at 3.7% in October
- Annual wage inflation is accelerating vs. a year ago in 8 sectors and declining in just 3 sectors. Wages are still increasing the most in information and financial activities

Annual wage inflation trending up but weakness in most sectors recently

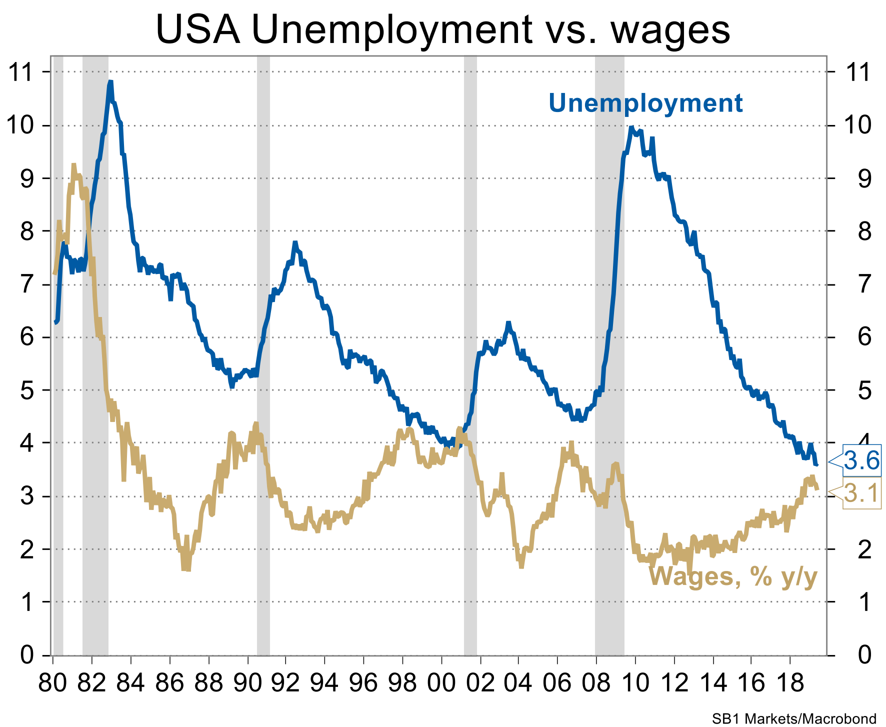
Monthly wage inflation has slowed in <u>all sectors </u>ex mining & lodging

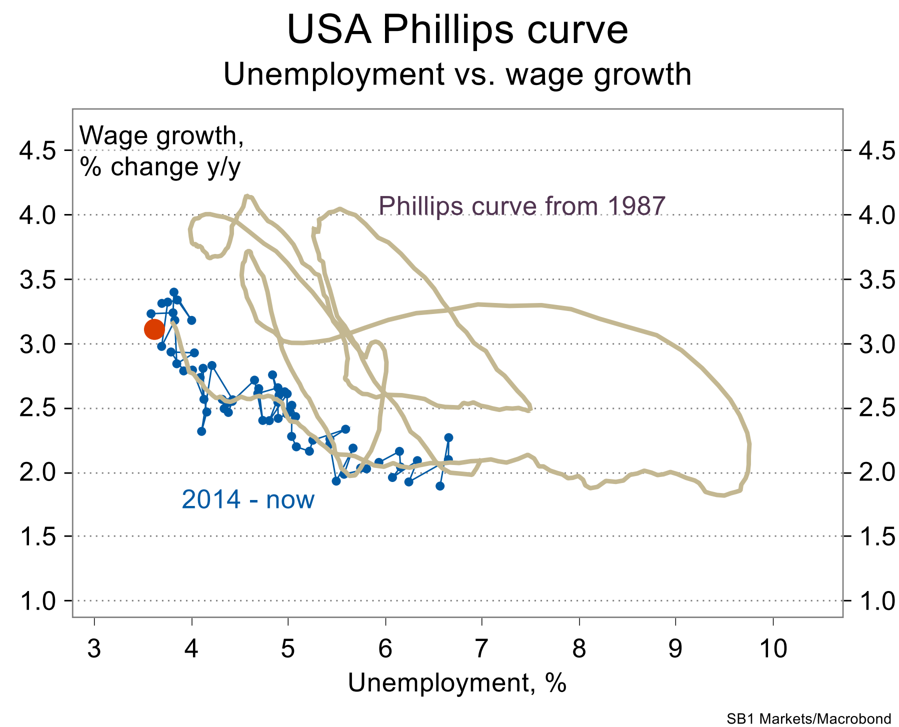




Wage inflation still somewhat lower than 'usual' vs. the unemployment rate

Even if the Phillips curve is flatter than before <u>it is definitely not flat</u>

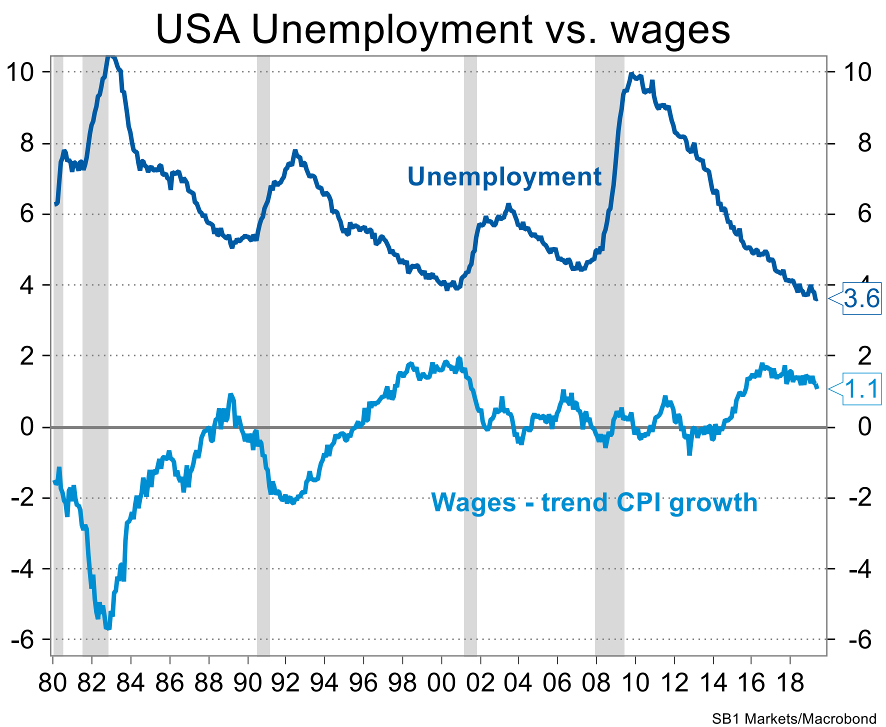


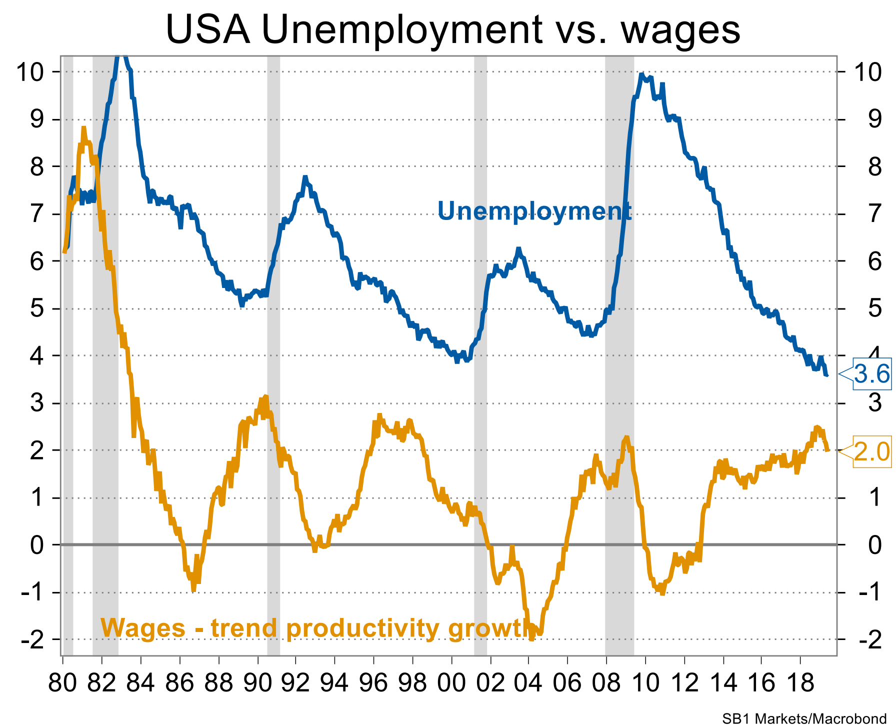


- However, we would not have guessed a wage growth at 3.1% y/y if we were told 6 m ago that the unemployment rate should decline to 3.6% in May
- On the other hand, if we calculate the Phillips curve using the employment rate, or the core (25-55y) employment rate, the Phillips curve is either far to the 'right' (and not to the 'left' as at the chart above) or normal

Wage inflation is not low vs. prices or productivity

In fact, real wages are increasing faster than normal, and more than normal vs. productivity

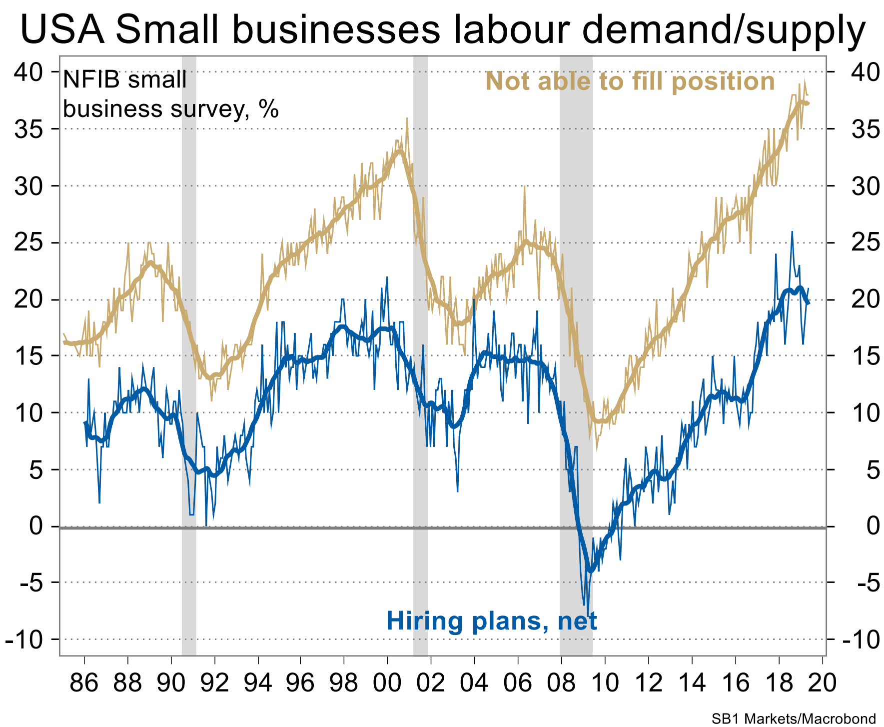


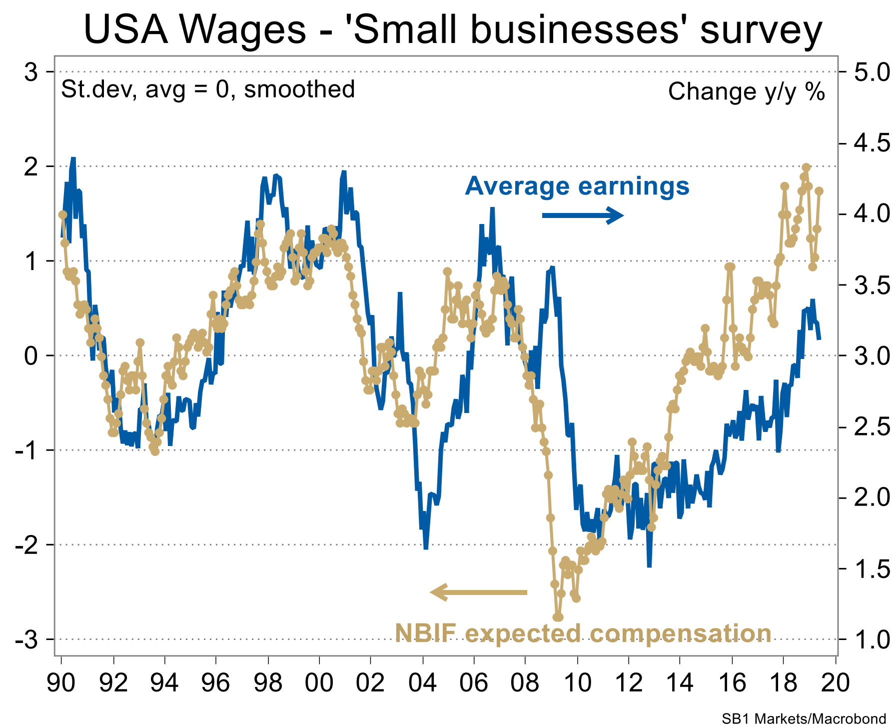


- In Q1, the wage – productivity gap, or labour cost per unit produced (ULC, unit labour cost, using the monthly wage data) fell to 2.0% y/y, as wage inflation has slowed marginally productivity growth has picked up (we here use a 3 y average productivity growth). Less price pressure?

Small companies are reporting tight labour market, rising compensation plans

Hiring plans have stagnated at a high level the past 6 m but businesses still unable to fill vacancies

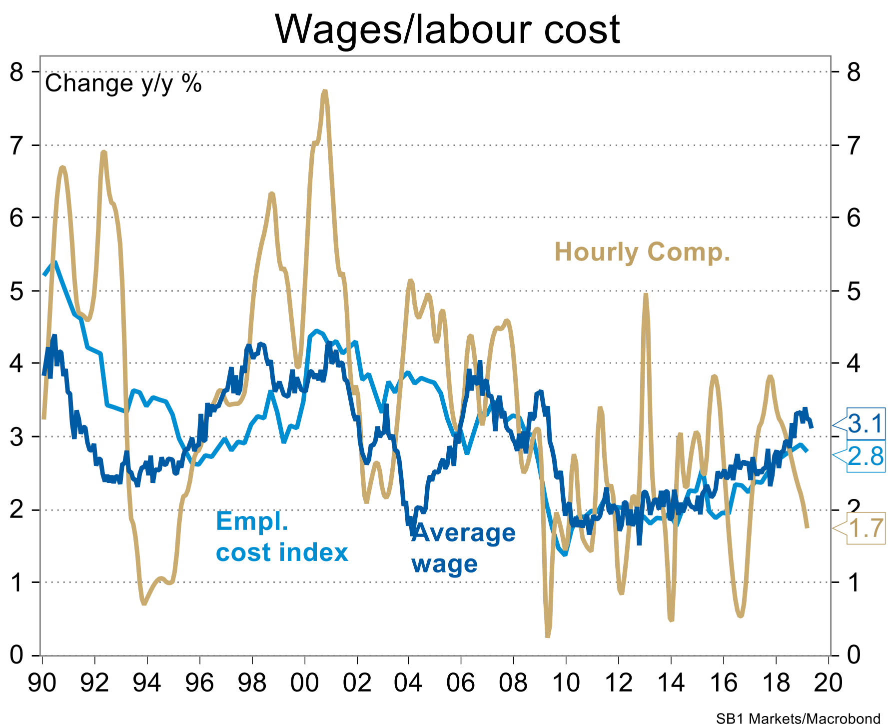


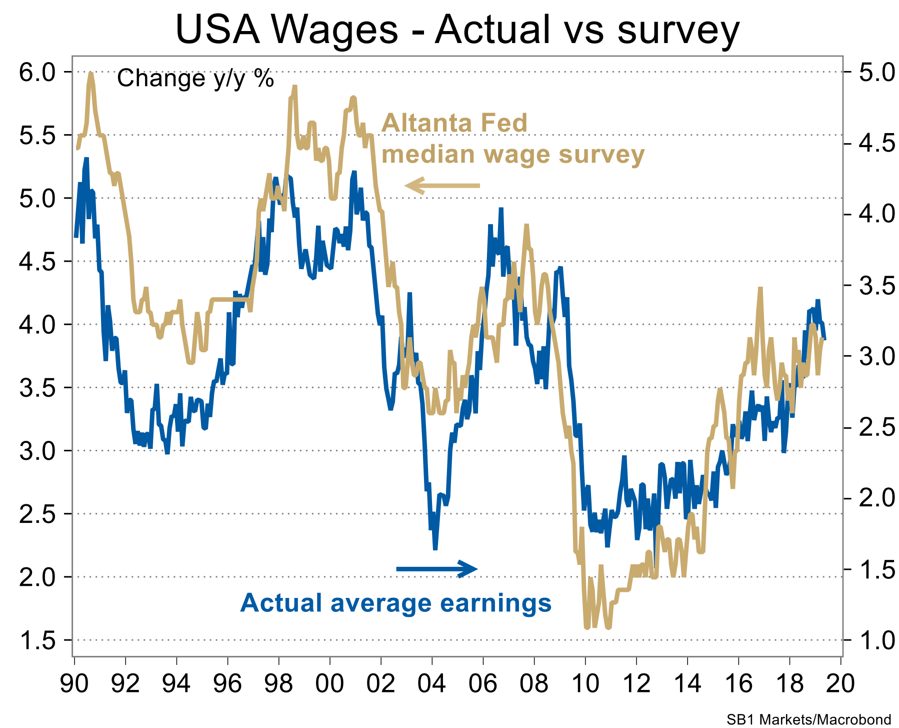


- SME companies have been reporting marginally less aggressive hiring plans so far this year, compared to the late 2018 levels. Early sign of demand weakness or just temporarily? These data are volatile – and the level is still close to ATH
  - » Most likely, companies will scale back their hiring plans before they start reporting that it's easier to fill vacancies and the unemployment will turn up – some months before the US economy really slows (or worse)
- The companies are still not able to fill their vacancies, which may be a reason for less aggressive hiring plans. An increasingly uncertain outlook have probably contributed as well. Compensation plans were shifted up in May, echoing a very tight labour market. A signal of accelerating wage growth the coming months

The long term view: Wage growth has been rising, according to all measures

Still, wage inflation has not accelerated the most recent months

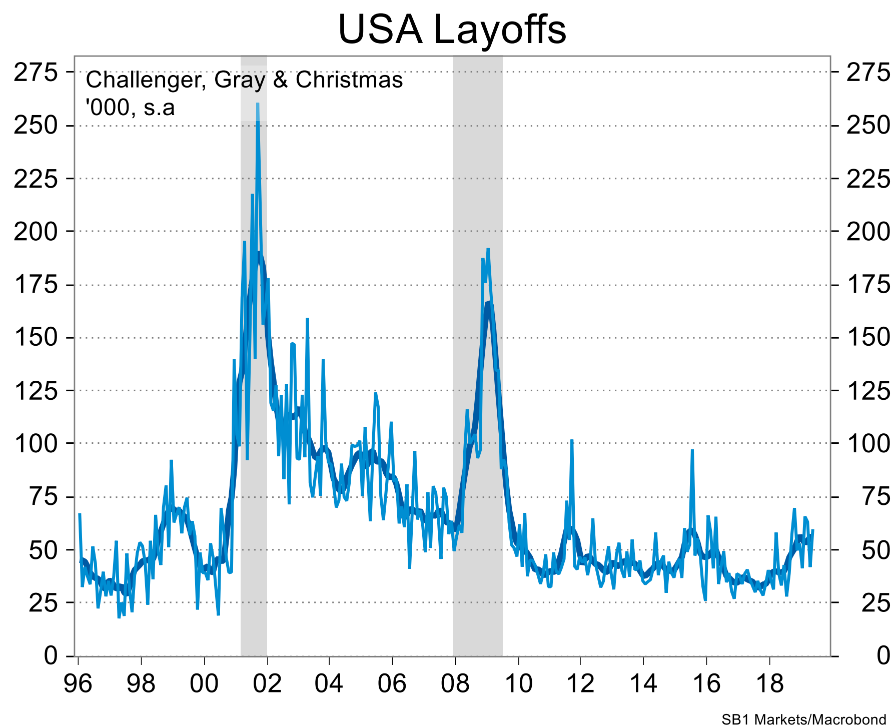


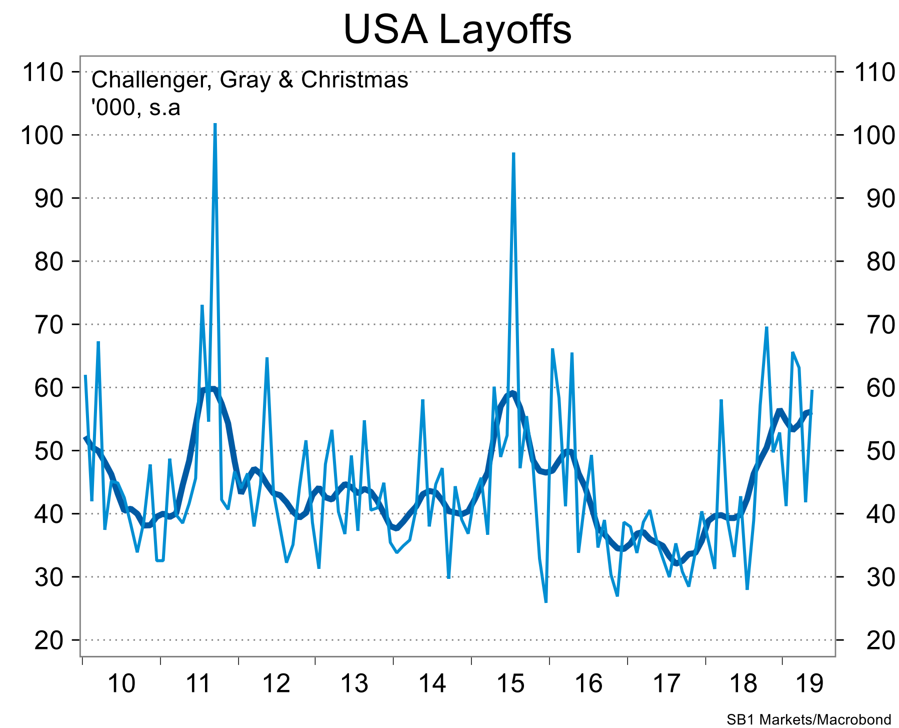


- The monthly employment cost index reports 3.1% y/y wage growth
- The Employment cost index rose 3.0% q/q annualised in Q1, up from 2.7% in Q4 and was up 2.8% y/y – is clearly accelerating
- Hourly compensation (from National Accounts) is the final assessment of all sorts of labour compensation. It is much more volatile than other labour cost measures. It rose 1.7% q/q in Q1 (from 3.9% in Q4) and the same speed y/y
- Atlanta Fed's wage survey reports 3.9% median wage growth, which normally equals the present growth in actual wages

Oobs: More layoffs in May, trending up

Layoffs have stabilised recent months but is still on an upward trend since early 2018

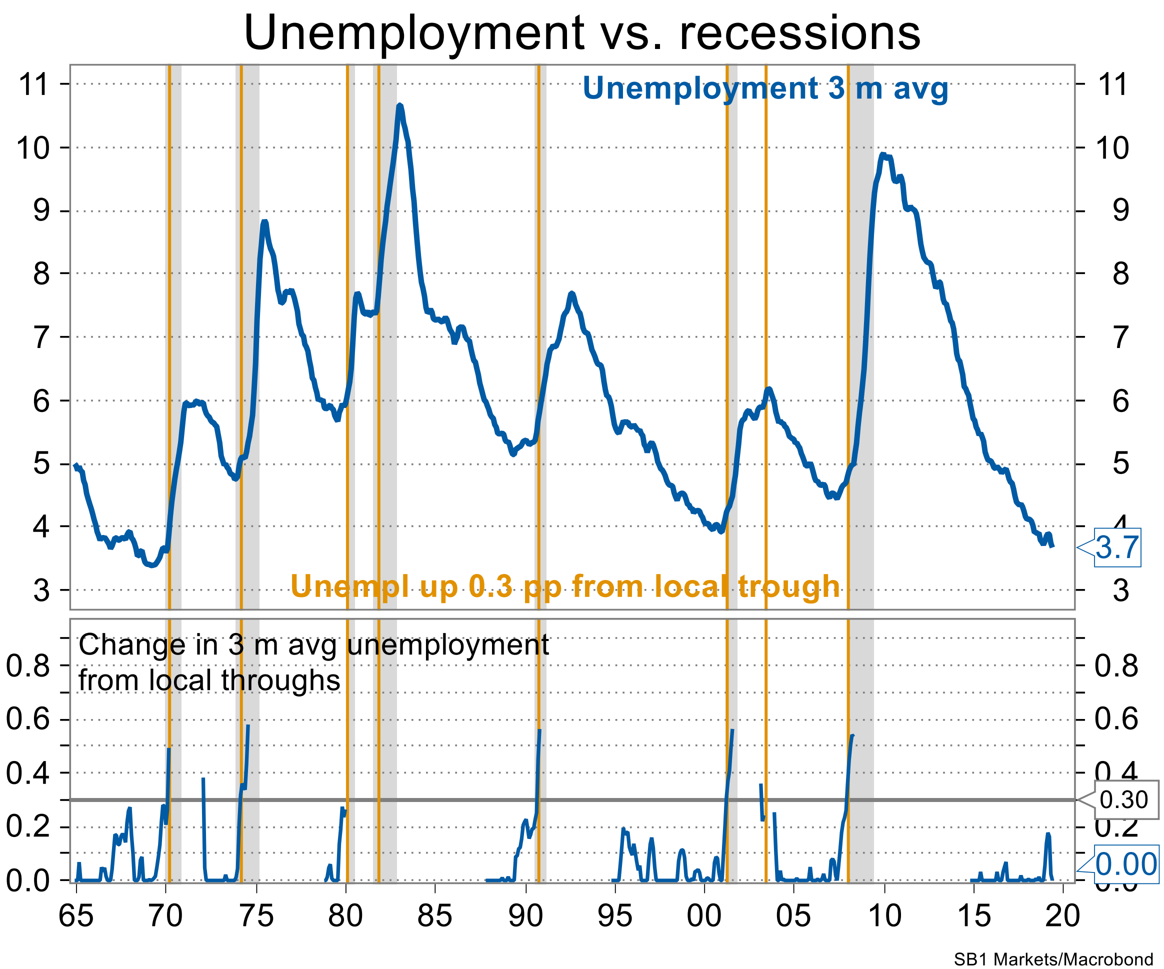




- The number of announced layoffs has been increasing since early 2018, flattening out the past 5-6 months. The levels is not very high but could signal some weakness in the labour market. However, the indicator is not consistently leading; in 2008 layoffs started to increase after the recessions started (but it was not yet declared)
- <u>Layoffs turned up in both 2011 and 2015, both times up 50-60%. Now, we are up almost 70% from the trough – and there not many other recession signals, although data have weakened recently</u>

Unemployment not up yet, no recession now?

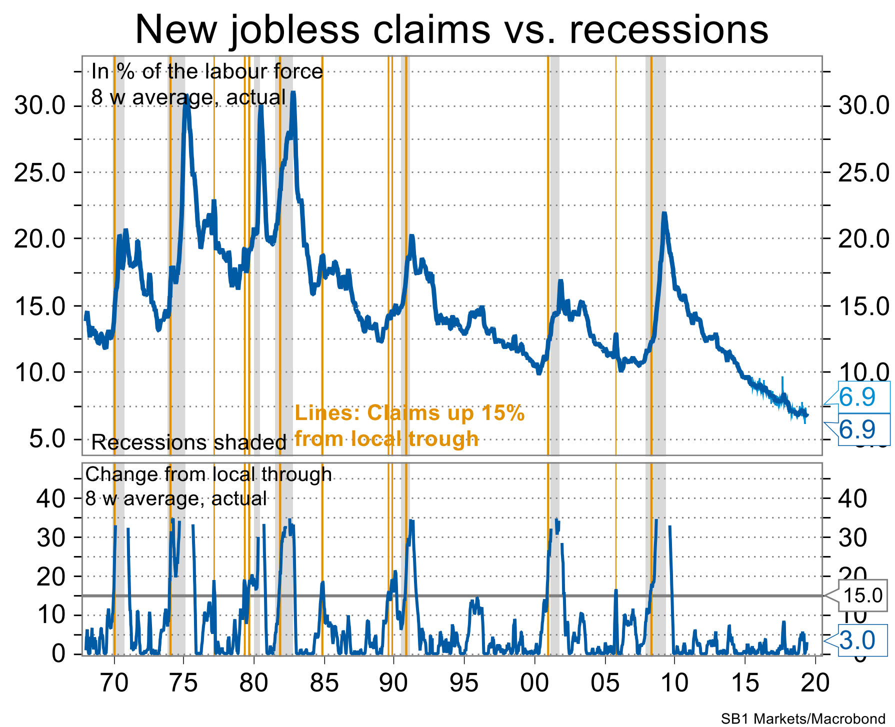
Unempolyment usually turns up slightly before or at the same time as the recession hits

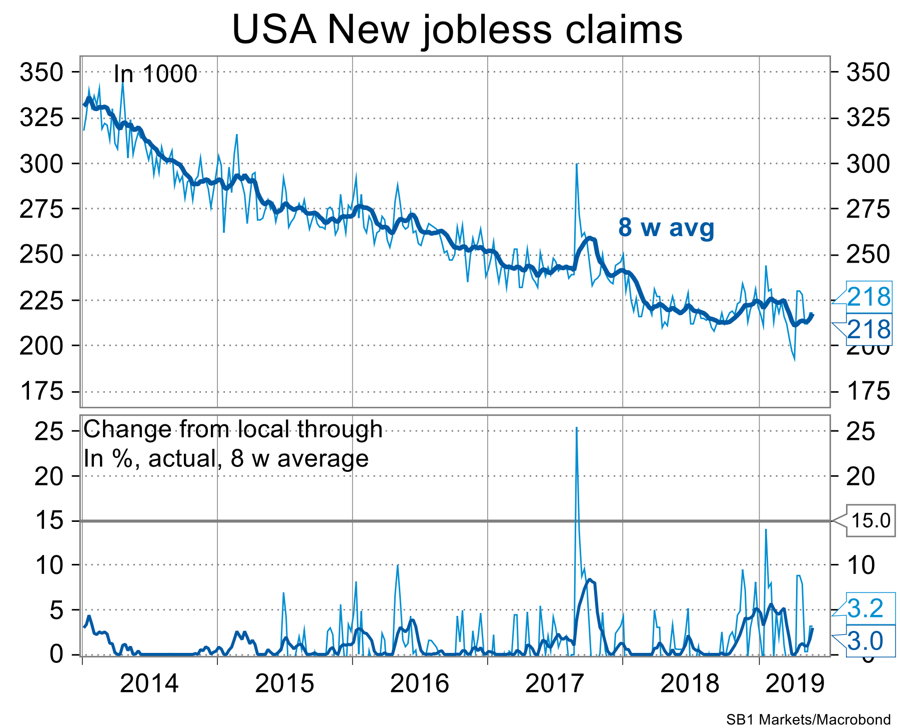


- A 0.3 pp increase in the 3 m avg unemployment rate has been a quite safe recession signal, but has not been a good recession pre-warning
  - » Unemployment always increases substantially during recessions
  - » The often used threshold for signalling a recession is a 0.3 pp increase in the 3 month moving average of the unemployment rate
    - Just once since 1965, in 2003, unemployment rose more than 0.3% without a recession underway. The 7 recessions were detected
  - » However, the 'signal' have always come too late to warn for a coming recession, at the best it has been coincident, rising 0.3 pp from a local trough at the same time as the recession starts
    - That's not that bad, as recessions are often recognised long after the fact.
  - » Other transformations of the change in the unemployment yield the same result.
    - Sure, unemployment increases marginally before recessions, but unemployment increases quite often, without any recession around, creating many false signals if not smoothed somewhat
  - » New jobless claims is marginally better as at recession warning indicator but not by much

Jobless claims marginally up last week, no signs of labour market weakness

Jobless claims (2 m avg) have been record low lately, reflecting a tight labour market

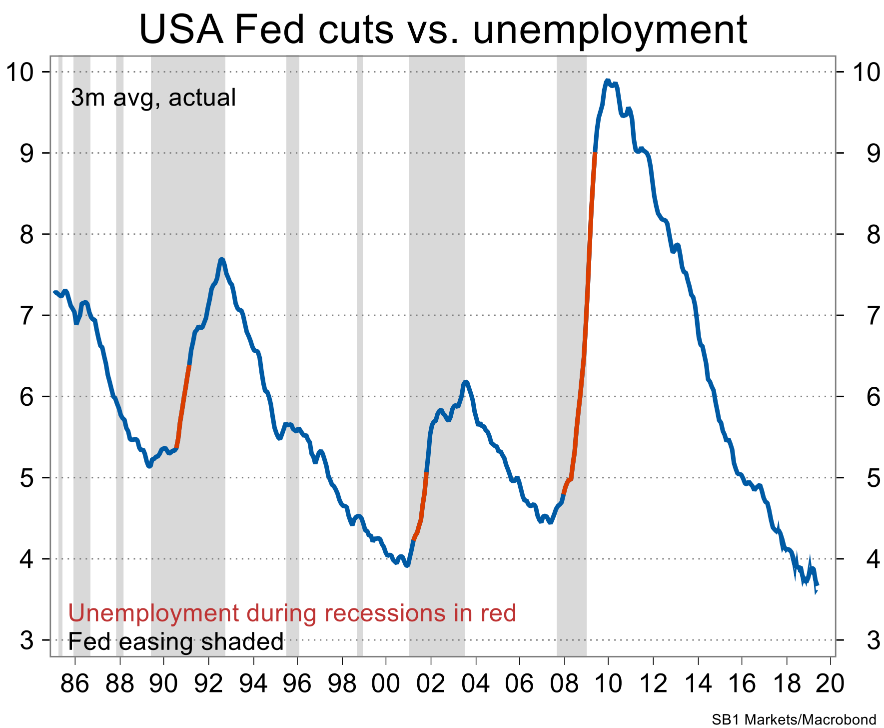


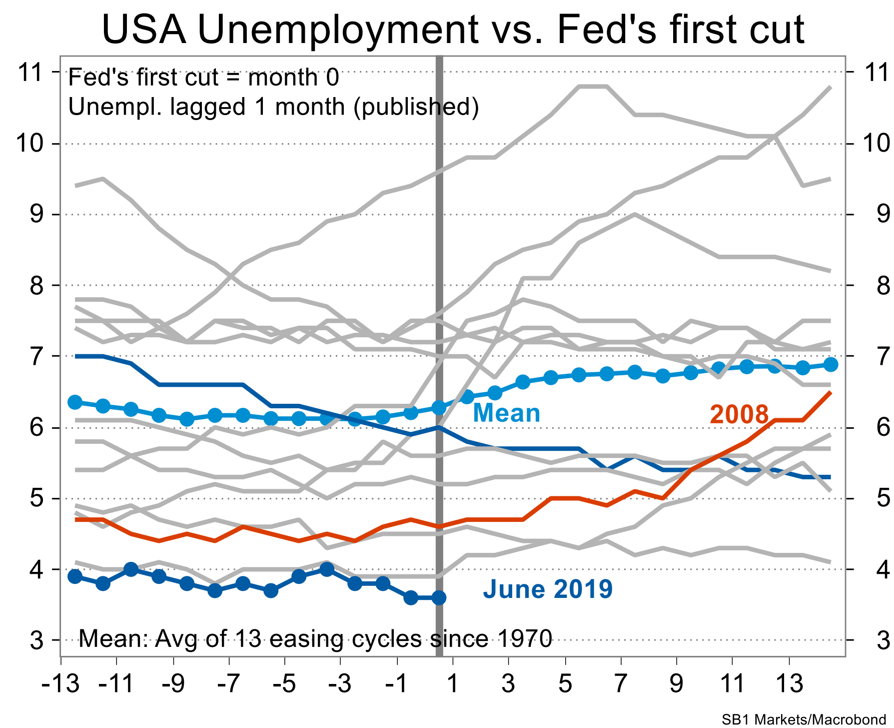


- Last week, jobless claims rose to 218’, from 211’ the prior week and up just slightly from the bottom at 193’in mid-April (the lowest since 1969!) The 8 week average is still very low, at 218’
- A more than 15% increase in jobless claims (measured by the 8 week avg) is usually a good indication of a recession, and a yellow ‘recession’ warning line is to be drawn, check the chart to the left. So, no reason to worry now?

When can the Fed start cutting: It could, now

In average, Fed waits until uemployment has edged up but often before any weakness is seen



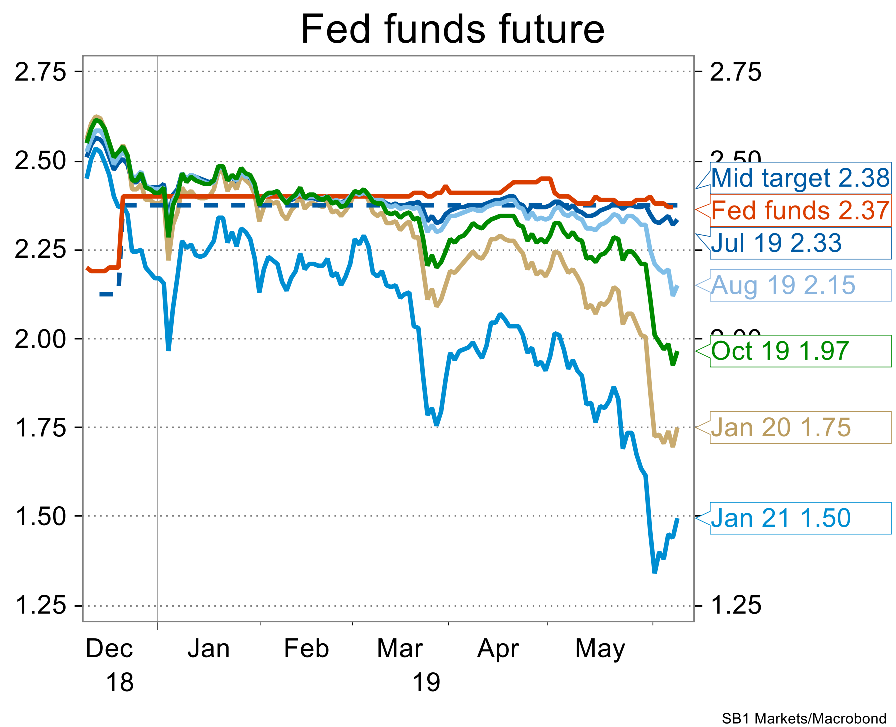


SpareBank 1 MARKETS

Fed’s Beige Book reports slightly <u>higher</u> growth, no support for a Fed cut

Fed’s ‘regional network’ reports tight labour markets but subdued wage inflation in April/May

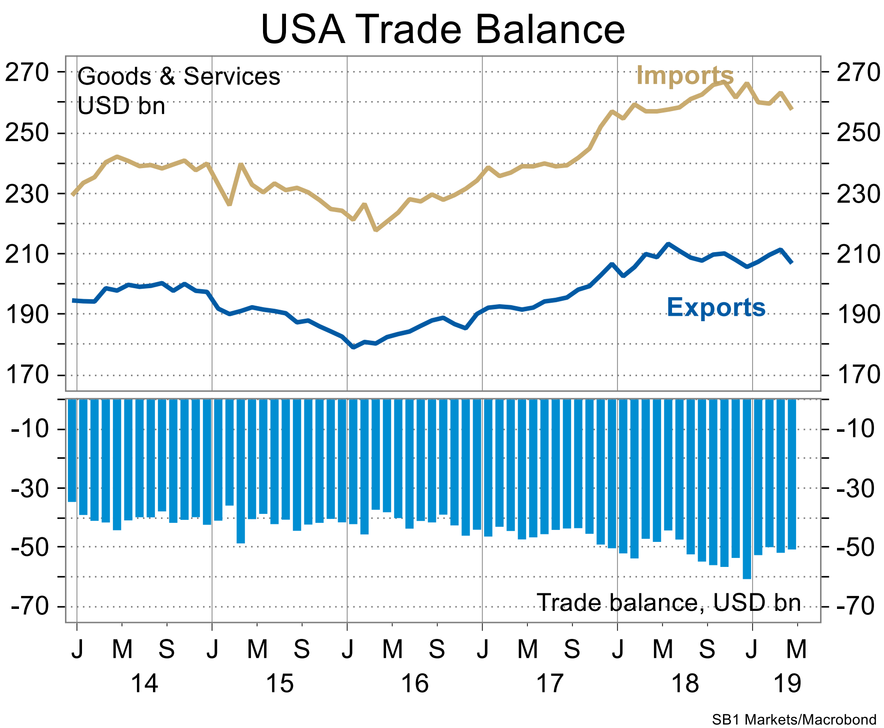
- Economic activity expanded at a ‘*modest*’ rate in the six weeks up to mid-May, a marginal increase from the ‘*slight to moderate’* speed in the previous report
- Manufacturing reports were mixed, some reported uncertain outlook, although the overall assessment was positive. Does not confirm the rapid slowdown which some surveys have found
- Household consumption is growing modestly but many Districts reported weaker auto sales
- All districts reported increasing employment, however, employment growth is constrained by widespread labour shortages. Businesses reported some wage pressure but overall wage growth remain modest (strange, given tight markets)
- Prices continued to grow at a ‘modest’ pace. <u>As in the prior survey, several Districts reported that input prices are rising faster than prices at the consumer level</u>
- **In total, the Beige book noted a somewhat more upbeat outlook than in the previous 2019 reports and does not indicate that the recent weakness in manufacturing and consumption will deteriorate. An argument for a patient Fed!**

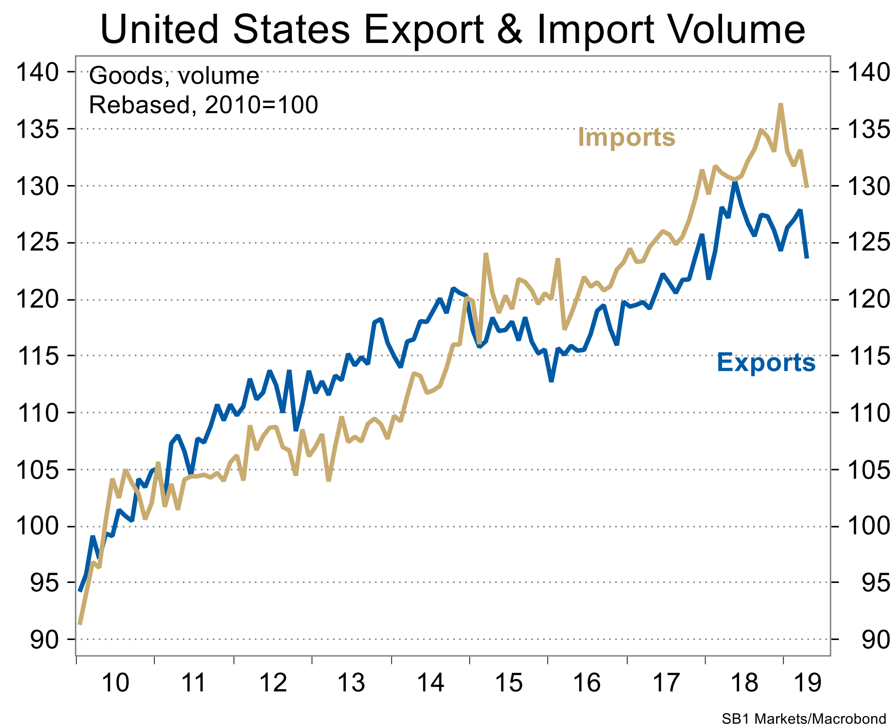


Fed Fund market rates have ‘collapsed’ recent months, recovering somewhat the past days due to the US-Mexico agreement. The market puts a 16% probability for a rate cut at the Fed meeting next week. However, the market assumes a cut before or on the Sept meeting to 92%, most likely down in total of 50 bps (one cut in July and one in Sept)

Both exports and imports fell in April, Q2 off to a weak start

The trade deficit shrank marginally in USD but exports fell more than imports in volume terms

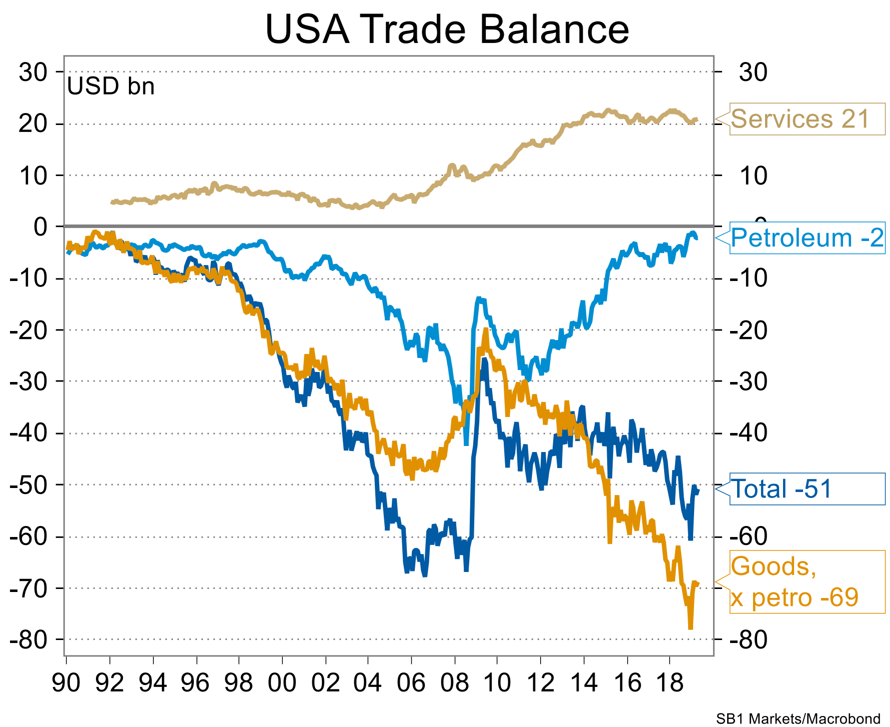


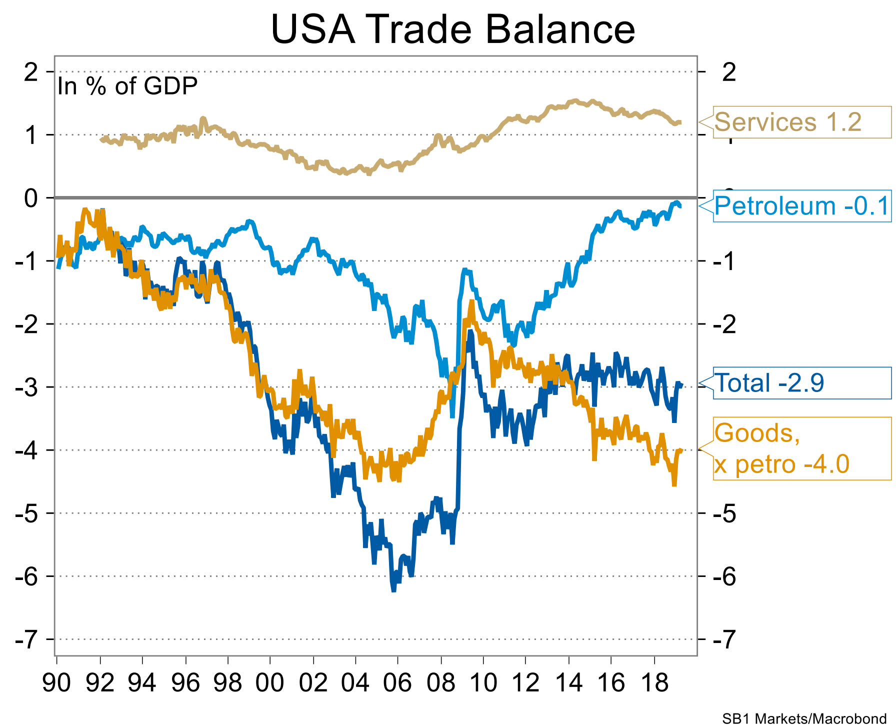


- The overall trade deficit (goods & services) shrank marginally to USD 50.8 bn in April
  - » Exports slowed rapidly in both value and volume, goods down 3.4% m/m in volume terms and is sliding slowly down the past year. The trade war has certainty not boosted US exports!
  - » Imports fell slightly less than exports in volume in April, and Q1 is off to a rather weak start, no positive growth contribution, so far
- The deficit vs. China is reduced, no doubt due to the trade war (imports from China is sharply down) – but the overall deficit is not cut

If not for petroleum, a 'catastrophe', but total deficit just 2.9% of GDP, was 6

The goods deficit ex petroleum is still very large, was the largest ever in December (vs GDP)

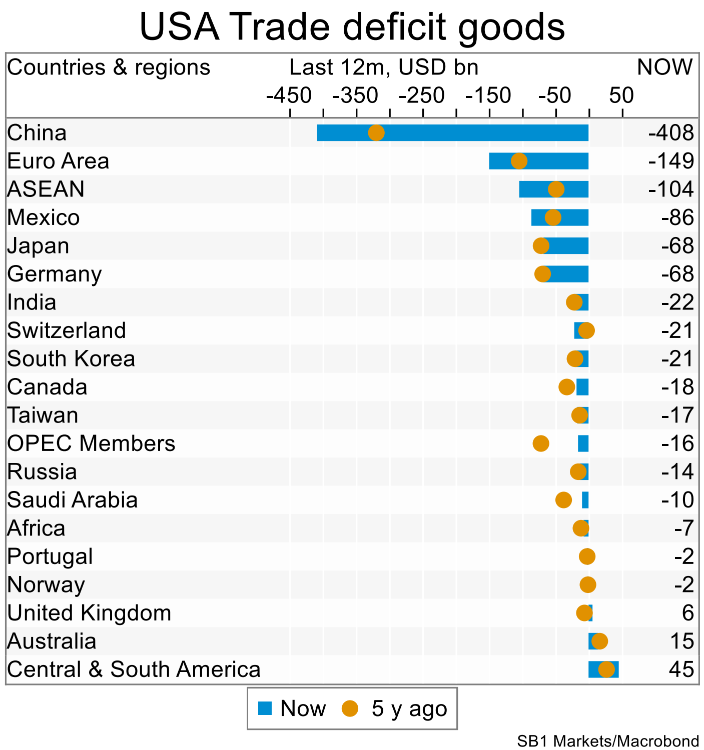


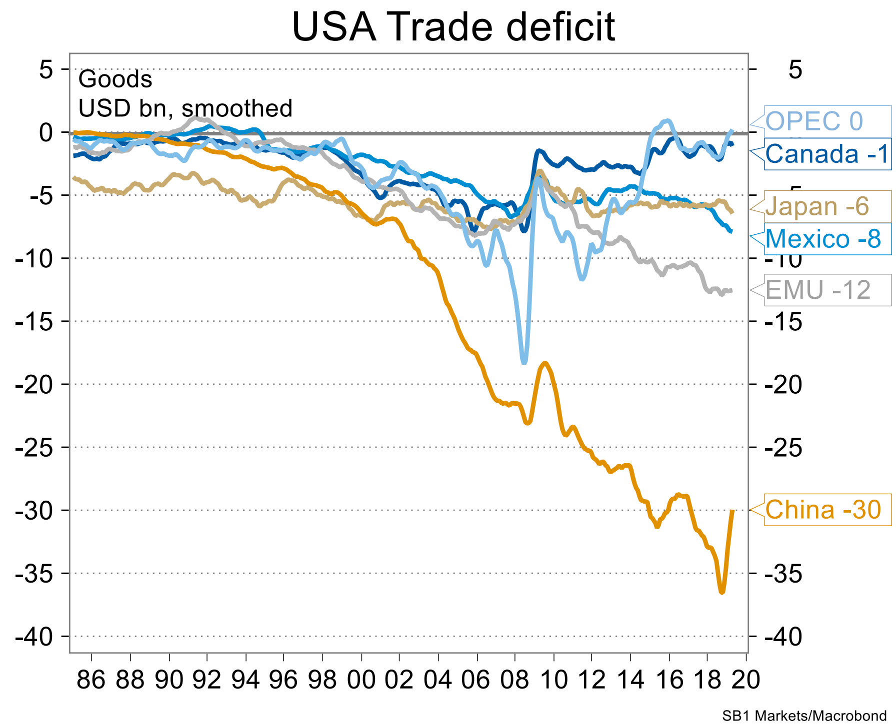


- In April, the goods deficit was unchanged at USD -69 bn, or 4% of GDP, after reaching an ATH in Dec '18 (data from '90)
- The deficit in petroleum trade is shrinking, USD -2 bn is the lowest in many decades (was 40 bn in one month in 2008!)
- The US has a surplus in services at USD 21 bn, equalling 1.2% of GDP (but it is now trending slowly down)

The deficit vs. China has narrowed, due to lower imports from China

Imports from China are falling. The deficit vs Mexico is rising and vs EMU it is trending out

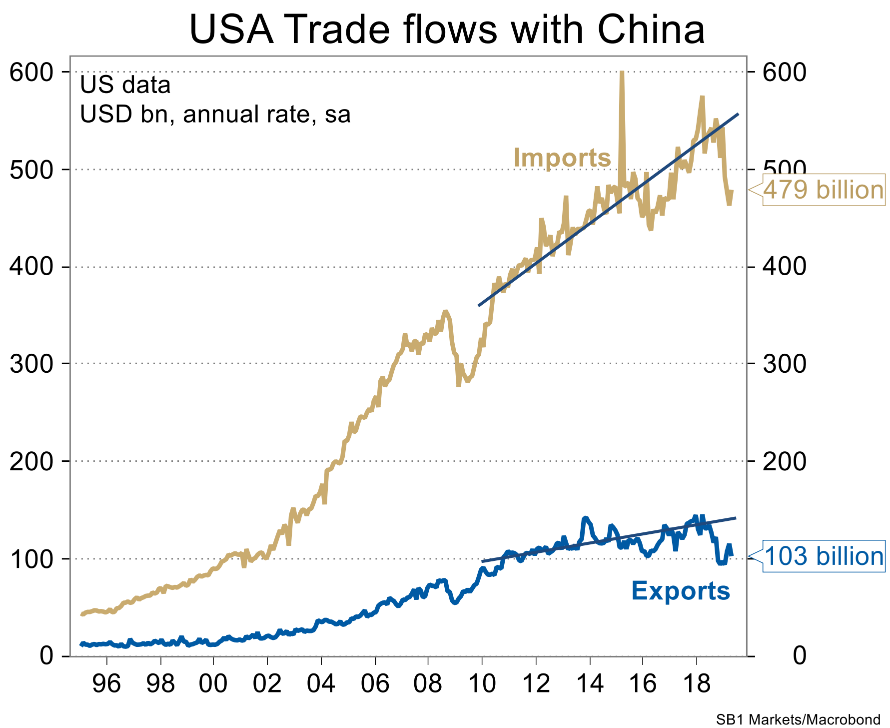


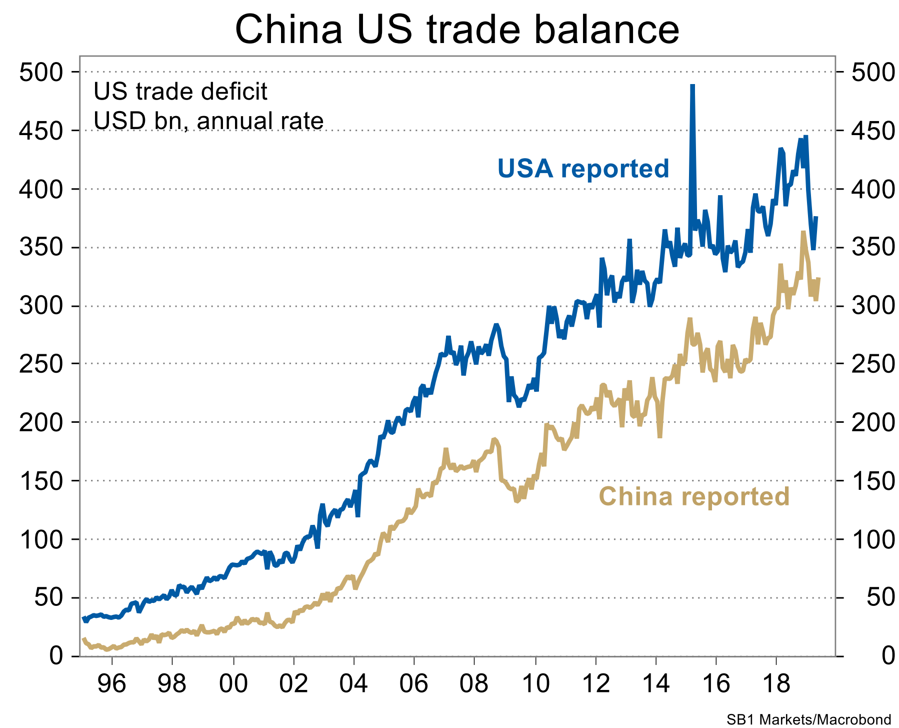


- The US deficit vs. China still equals 43% of the total deficit in goods
- The deficit vs. Mexico has widened markedly, vs EMU it slowly trending out
- Deficits vs OPEC & Canada close to balance

US imports from China have fallen more than exports to China (in billions)

Tariffs have hurt bilateral trade significantly, and China more than US

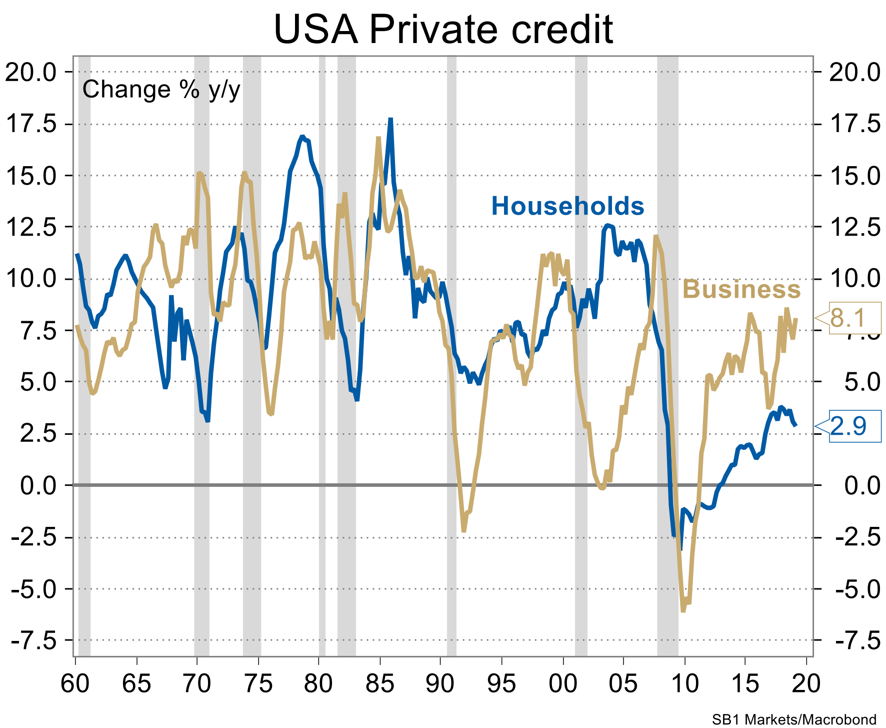


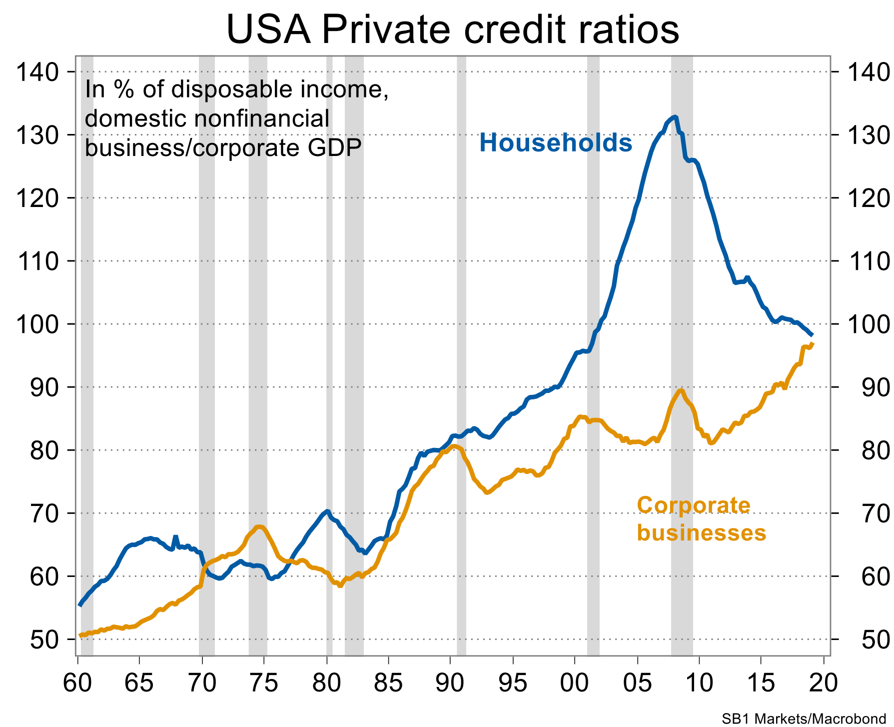


- The Chinese are reporting a smaller decline in the surplus vs. US, than US reported decline in deficit vs. China. FOB exports vs. CIF exports explains some of the difference between the two measures of 'the same'

Household credit slows, at a low level, corporate debt growth flat at a high level

Household debt slowed to up 2.9% y/y in Q1, corporate debt growth ticked up to 8.1%

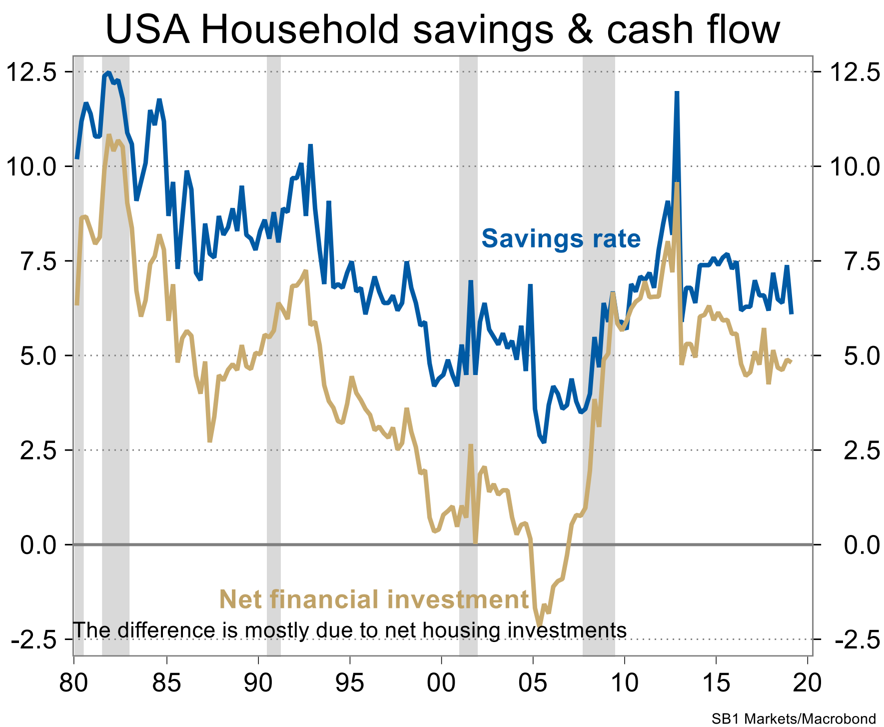


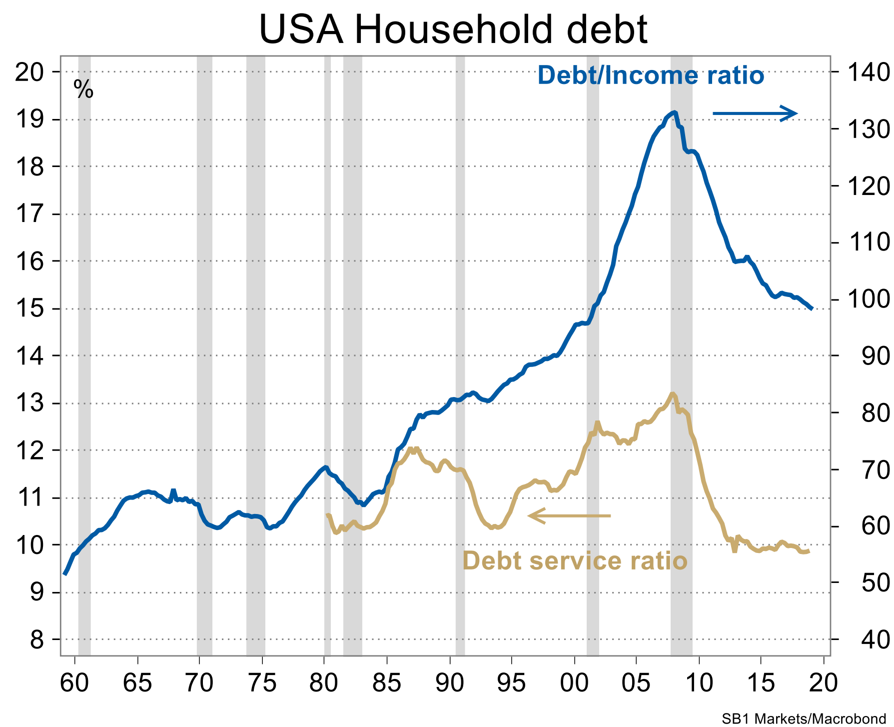


- Household debt inflation fell in Q1, and is still increasing slower than household income. The debt/income ratio has fallen to below 100%, down from 133% in 2007! The largest deleveraging ever in the US. And unemployment has fallen most of the time!
- Corporate credit growth accelerated to 8.1% in Q1, well above growth in corporate value added. Growth in corporate credit has been far higher than growth in corporate GDP, and corporate debt equals 97% of corporate GDP. That is way above previous peaks, and high above any reasonable trend line. If not for equity buybacks past 10 years the debt ratio would have been in the 50'ies, lowest 'ever'!

Households' net cash flow at a 'normal' level, sliding slowly down

Households are saving – and paying down debt (relative to income), debt service cost record low

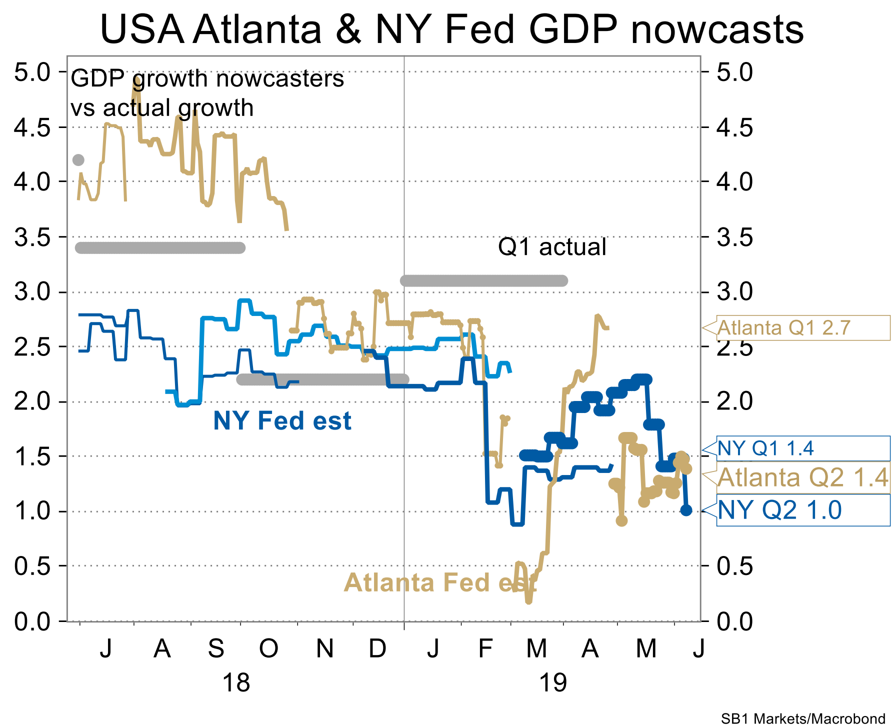


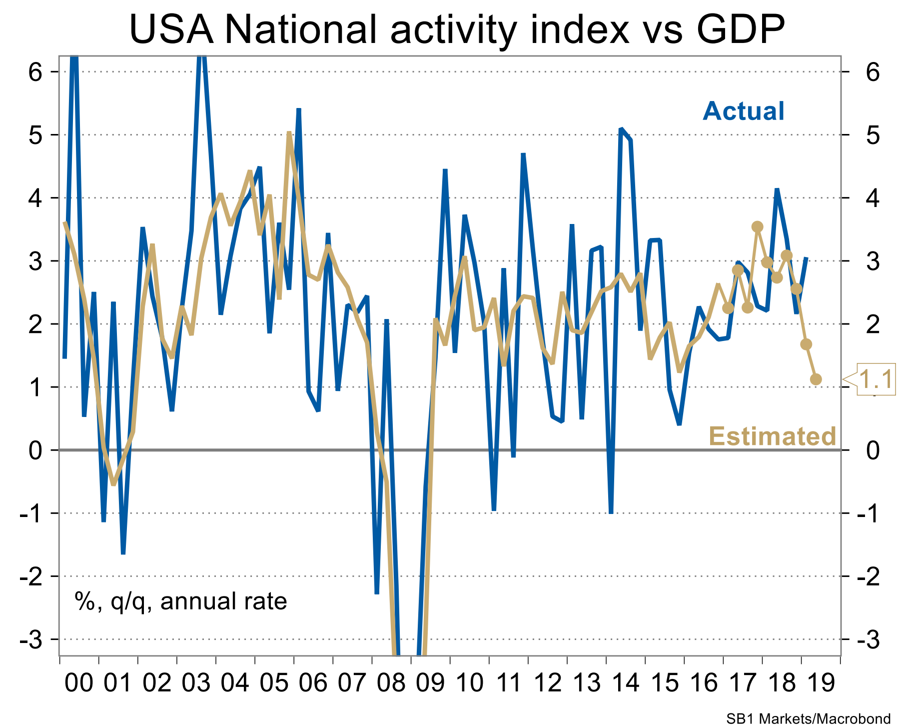


- Households are running a cash surplus at 4.8% in Q1, marginally lower than in Q4, at a rather high level
  - » Cash balance (net financial investments) = Savings – net (of depreciation) investments in fixed real capital (mostly housing)
  - » The savings rate fell to 6.1% of disp. income in Q1, the lowest since 2013 but the trend is more or less flat
- Households' debt ratio is much lower than 10 years ago and is still sliding down, almost back to a the year 2000 level
  - » There are few signs of financial stress, at least barring student loans

All nowcasters are finding a slowdown in Q2, to 1-1.4%

The nowcaster models are well aligned this time. And they may be right

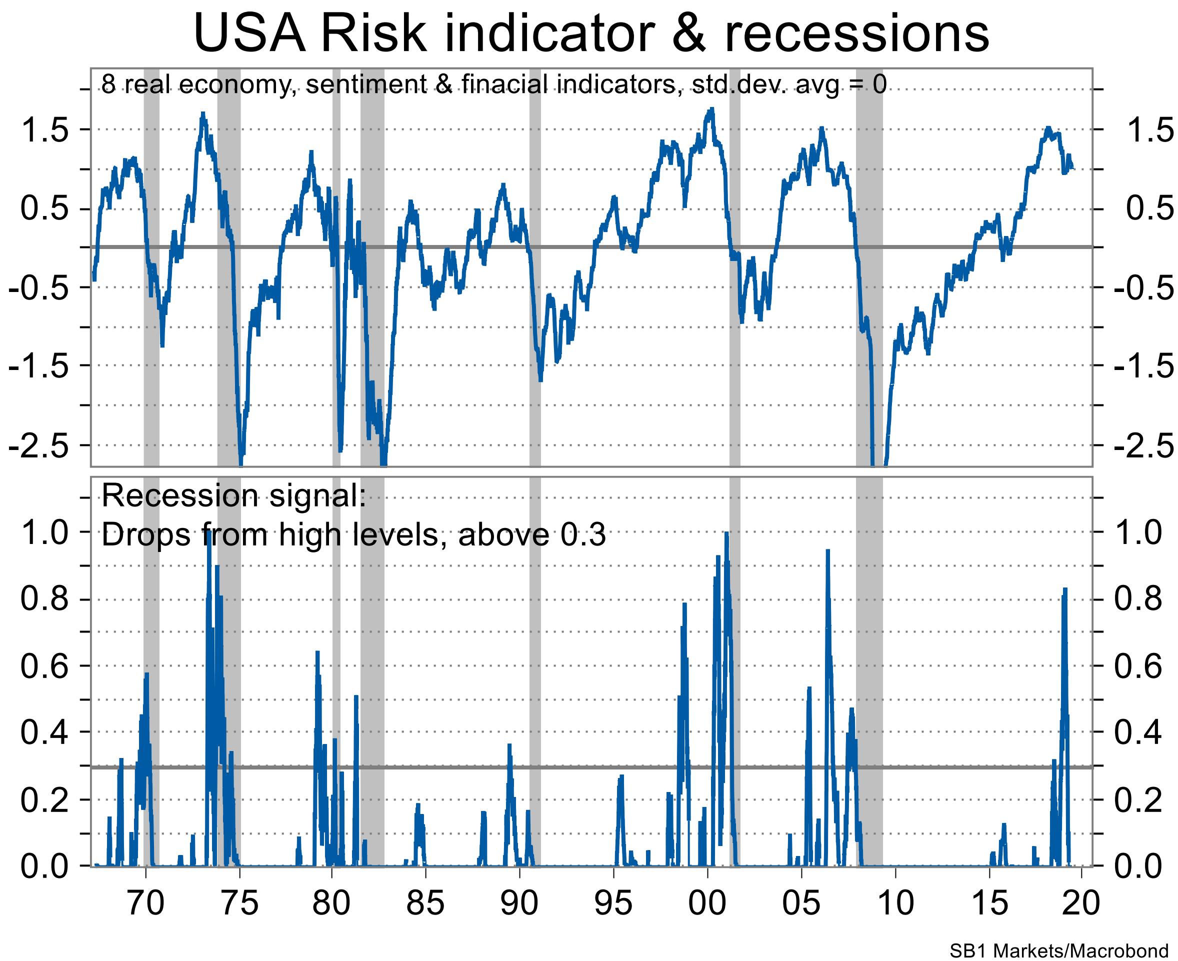


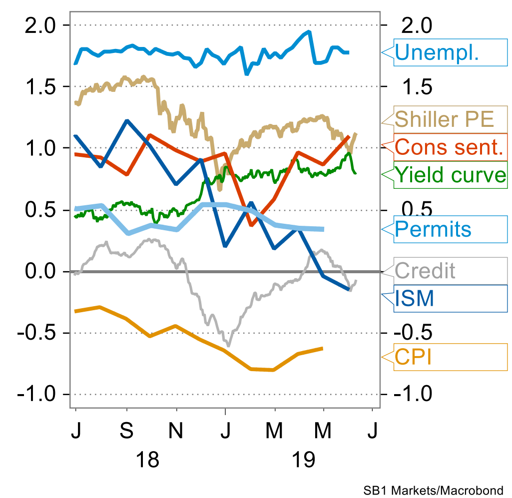


- The Atlanta Fed nowcasts marginally down last week, the NY Fed model more sharply, 0.4 pp to 1.0%, the lowest estimate so far. The National Activity Index was more downbeat in April, suggesting just 1.1%

US Indicators: Not a recession warning, now

… but data are deteriorating, barring the labour market and housing. To be continued



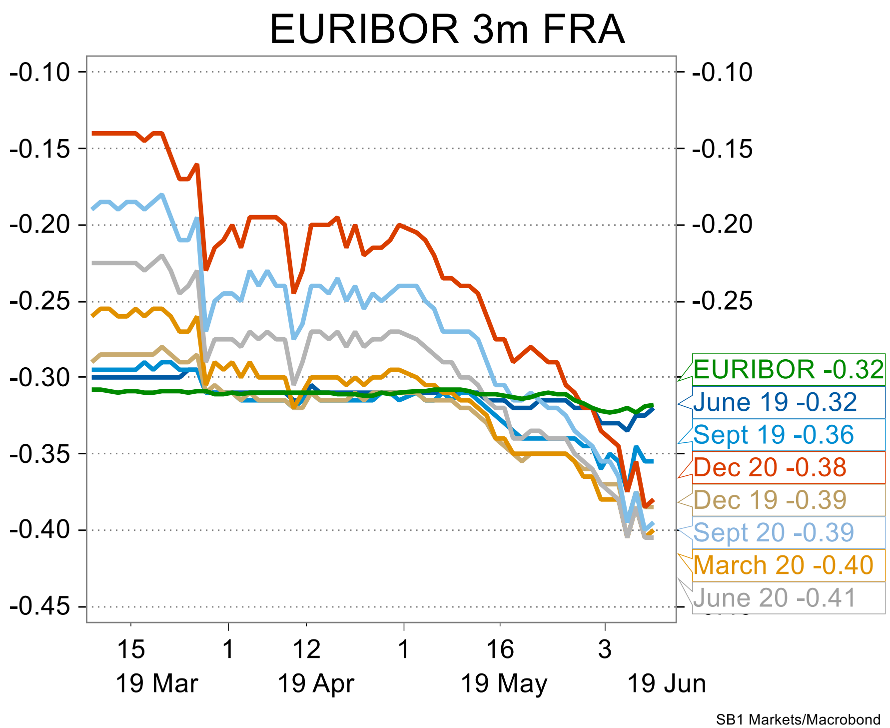


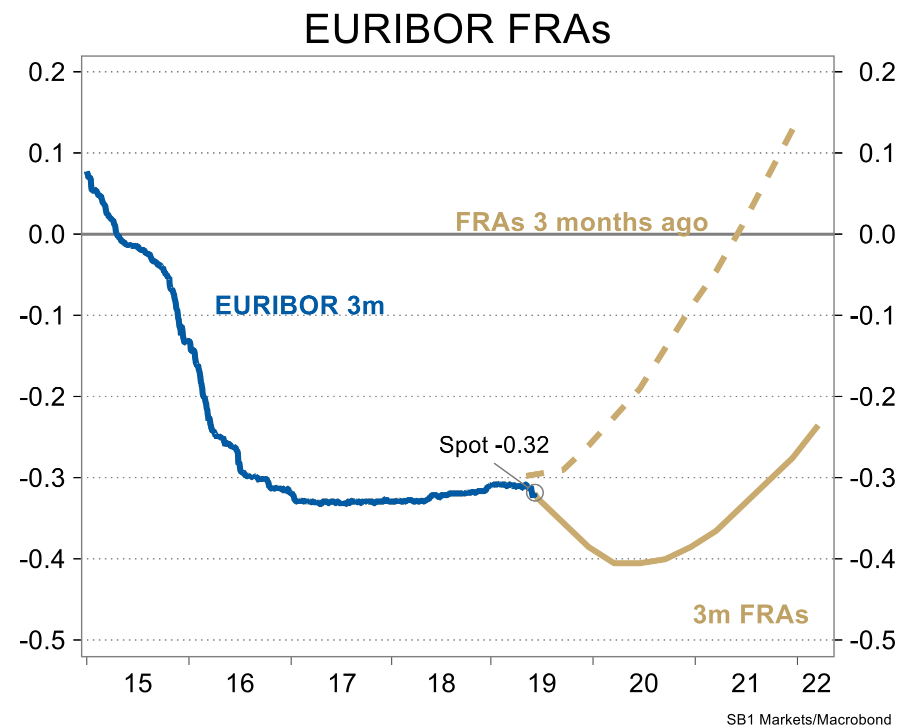
Inspired by Goldman Sachs Bull/Bear indicator. We are using jobless claims instead of unemployment, and have added housing starts, consumer sentiment, and a credit spread. In average, our Risk or Good Times Indicator leads recession starts by 18 months. The lower panel above shows changes in the squared index (if index >0) to accentuate the dangerous declines from high levels

SpareBank 1 MARKETS

ECB postpones the first hike to H2 2020, stresses readiness to act

The new version of the TLTRO funding vehicle more generous than expected, more bank liquidity

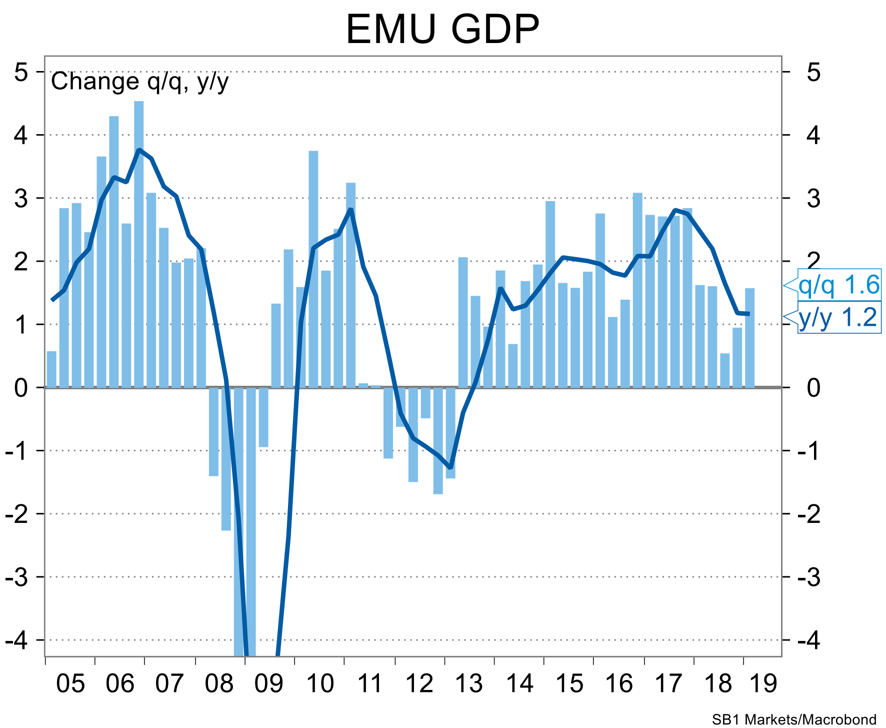


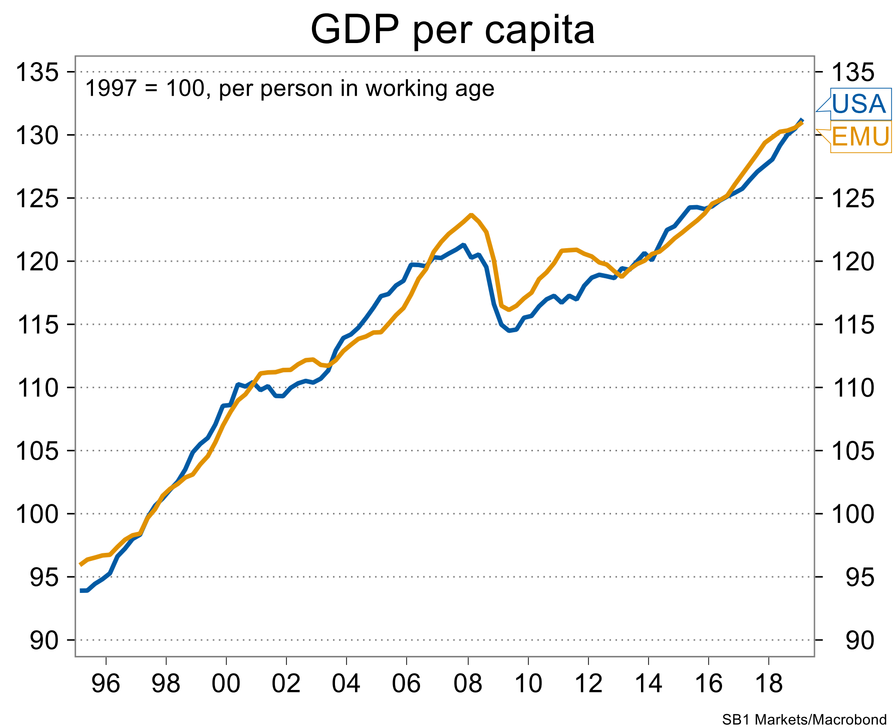


- The soft turn did not surprise markets, which had been starting to consider an interest rate cut (in fact, more was expected, thus, interest rates increased following the announcement) but then fell in sympathy with US rates following the weak US job report. The market is now pricing some 28% probability of a rate cut in '19. The details for the new TLTRO, long term funding for lending for banks was more generous than expected, and banks will most likely utilize the funding vehicle
- Mario Draghi noted that the extension of the current interest rate is a result of acknowledgement of risk due to increased and prolonged uncertainties. At the meeting, several Board members raised possibilities of further expansionary measures such as rate cuts and expansions of QE, and Draghi stressed that the ECB is ready to act if needed.
  - As expected, the ECB acknowledges that data inflows are on the weak side and indicating a soft Q2. Still, the GDP f'cast for 2019 was nudged up by 0.1 pp (due to higher Q1 growth) and the 2020 f'cast down by 0.2 pp. Core inflation is still expected to pick up

GDP growth confirmed at 1.6%, driven by rising domestic demand

Q1 growth was unchanged in the 3rd release. Fundamentals are solid, just inventories fell

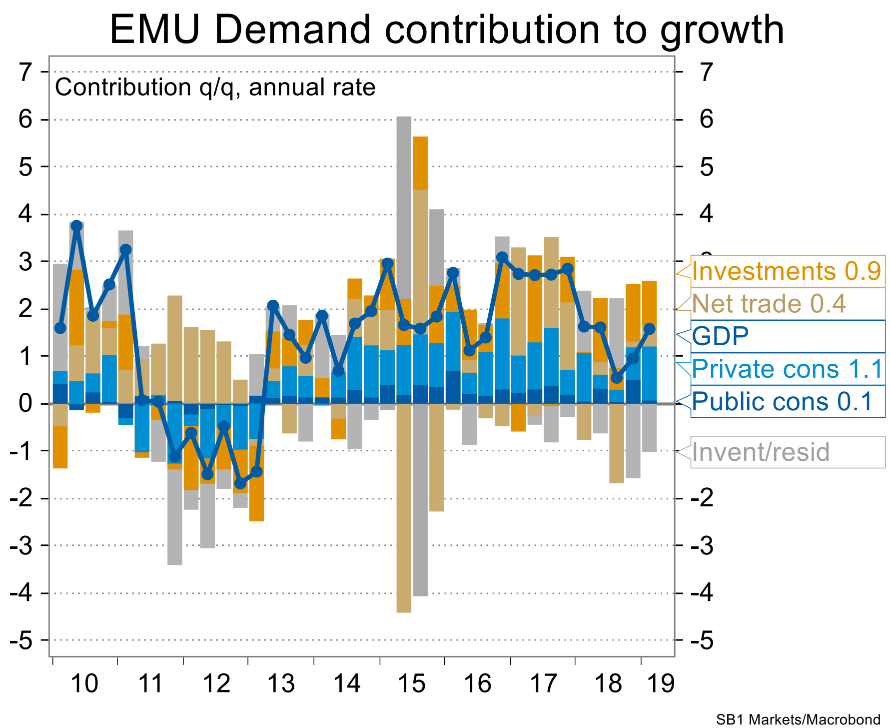


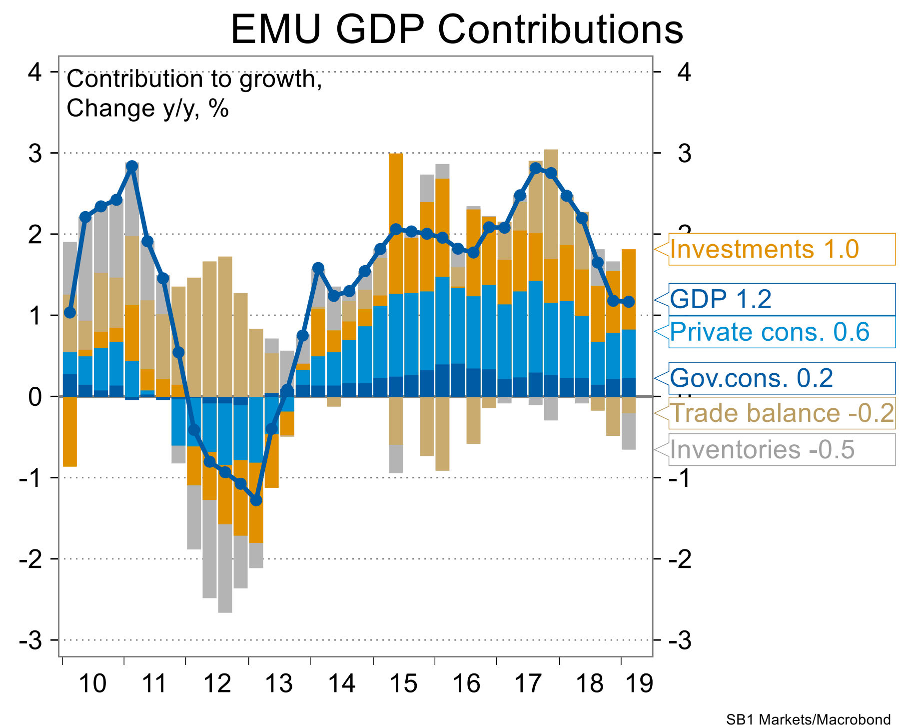


- GDP growth accelerated in Spain, Germany and Italy (which came out of the 'technical recession'), slowed in France
- GDP per capita in working age grew marginally slower in the Eurozone than in the US in Q1. Growth in GDP per capita has been higher in the US than in the EMU two past years, However, if we adjust for the change in the structural budget deficit (the fiscal impulse), the 'real' growth has been far higher in EMU the past years than in the US. Since mid 1990'ies we are not able to spot any material difference. Are you?

Solid growth in household consumption and business investments

A reduction of (auto?) inventories drove GDP growth down too, better days ahead?

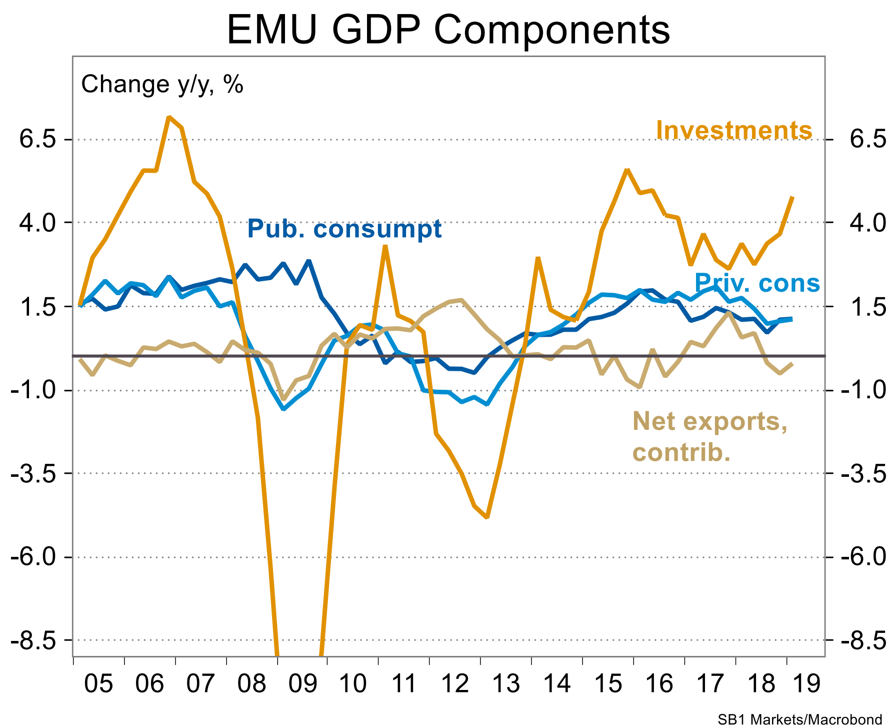


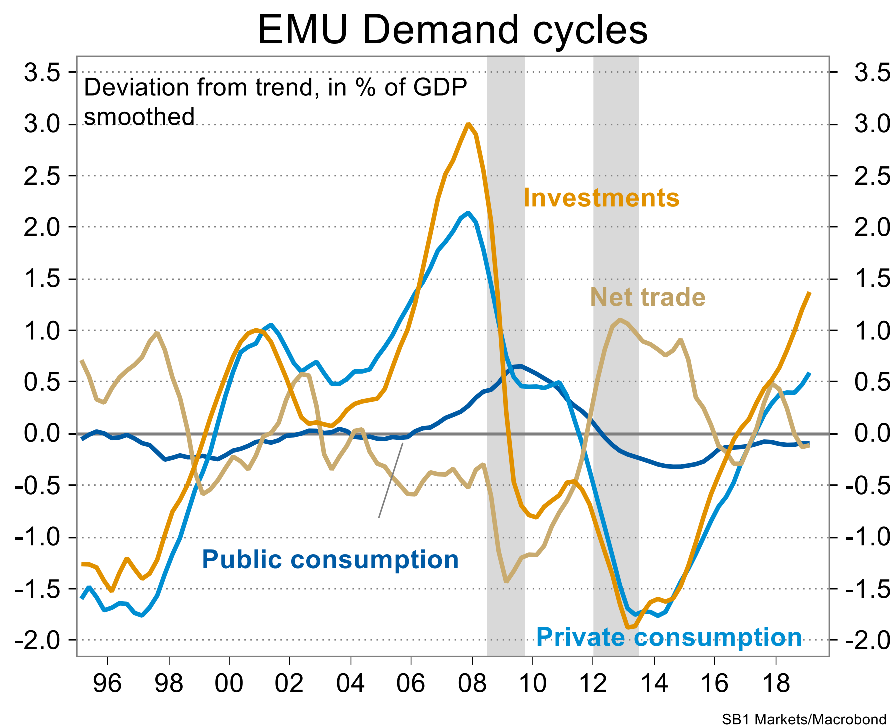


- Private consumption was the main growth driver in Q1, following some soft quarters. Consumption lifted q/q growth by 1.1% annualised, slightly higher than 'normal' the past 2-3 years
- Investments expanded at a decent rate too, and made a 0.9 pp contribution - and 1 pp y/y
- Net trade up in Q1 but slightly down y/y – but has even so contributed to the declin in the growt rate since 2017, when net trade contributed positively
- Inventories are still being trimmed, partly due to lower (German) auto inventories (In Q3 last year, auto inventories spiked as auto sales nosedived). Since then, production is cut and sales are slowly turning up, thus, inventories are trimmed

Investments are the main growth engine, private consumption above trend too

Just net exports is halting – and public consumption grows modestly

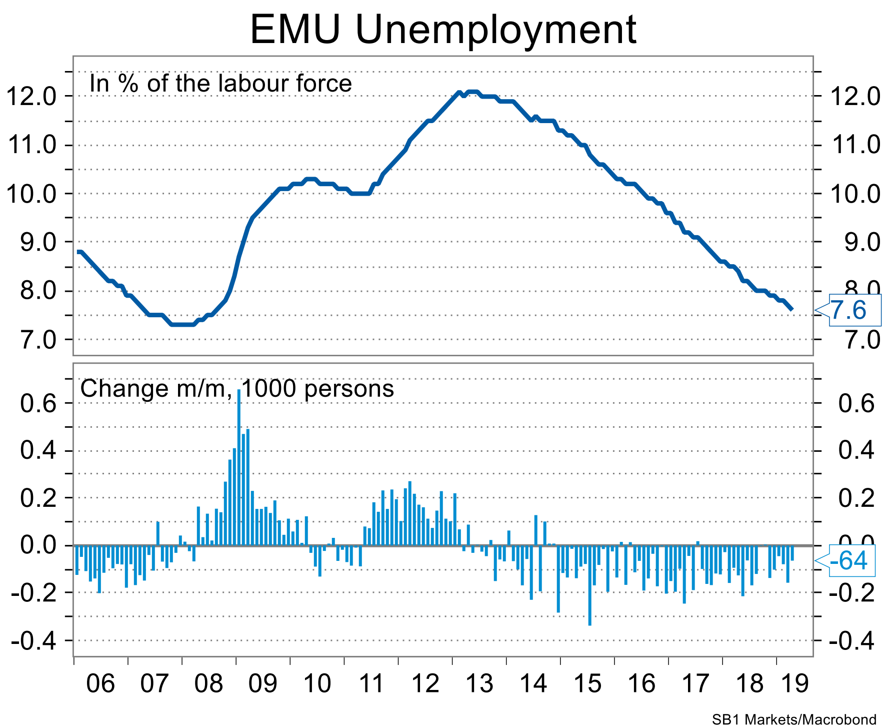


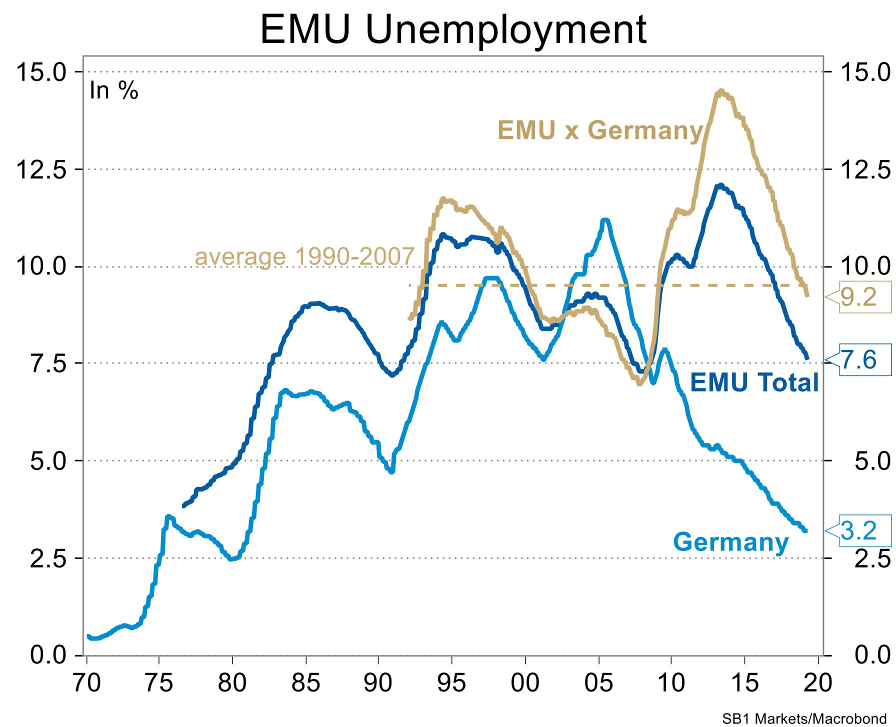


- Investments are far above trend, an obvious downward risk the coming quarters

Unemployment one tick down in April, at 10 ½ y low

Unemployment edged down to 7.6%, below f’casts. A promising sign or a lagging indicator?

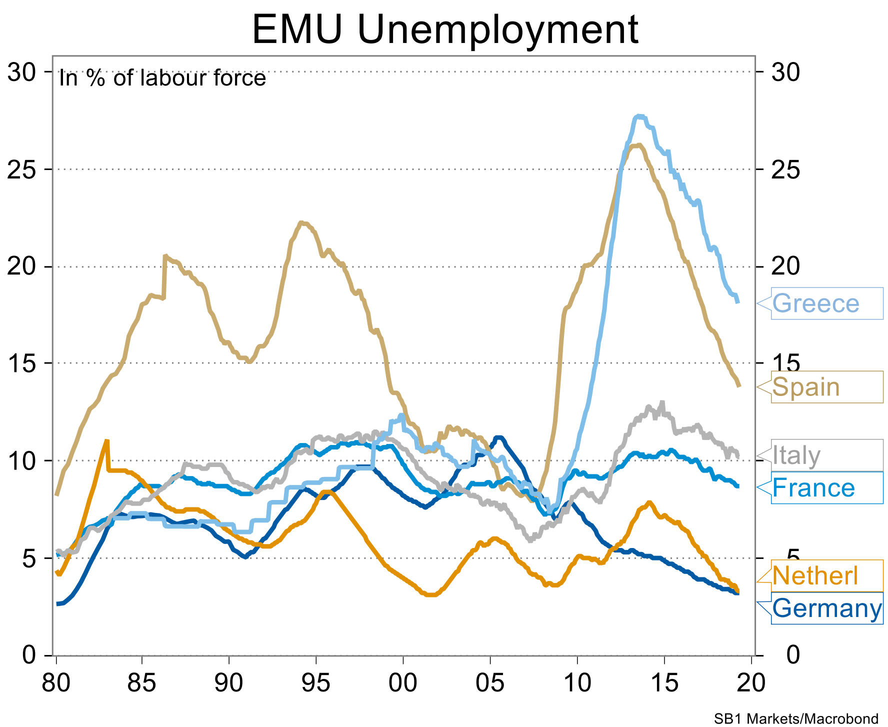


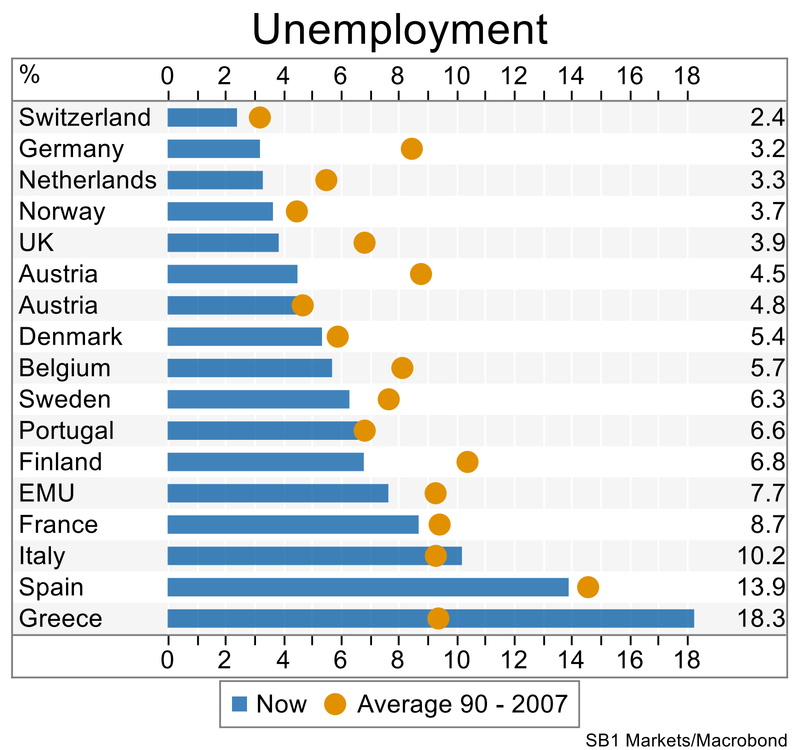


- The unemployment rate fell 0.1 pp in April, was expected unchanged at 7.7%. The number of unemployed fell by 64’ persons,a modest decline after a steeper drop the prior month. Thus, there are no indications of a weakening labour market in spite many soft data points. Regrettably, unemployment is not a leading indicator, it is at best a coincident one
- Unemployment in total EMU is well below the 1990-2007 average, and it has fallen just below the average in EMU ex Germany too; Italy & Greece are above avg, the others below pre-2007 avg
- In Germany, the unemployment rate was flat at 3.2% in April, and is at the lowest level in 38 y

Unemployment is declining everywhere

Higher than 'normal' (avg 1990 – 2007) only in Greece and slightly in Italy

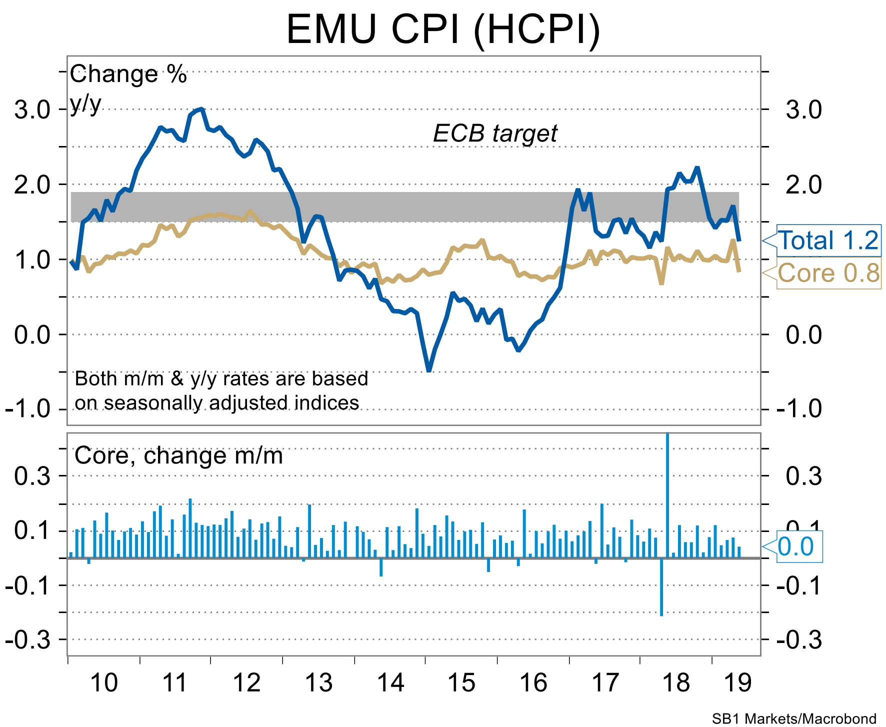


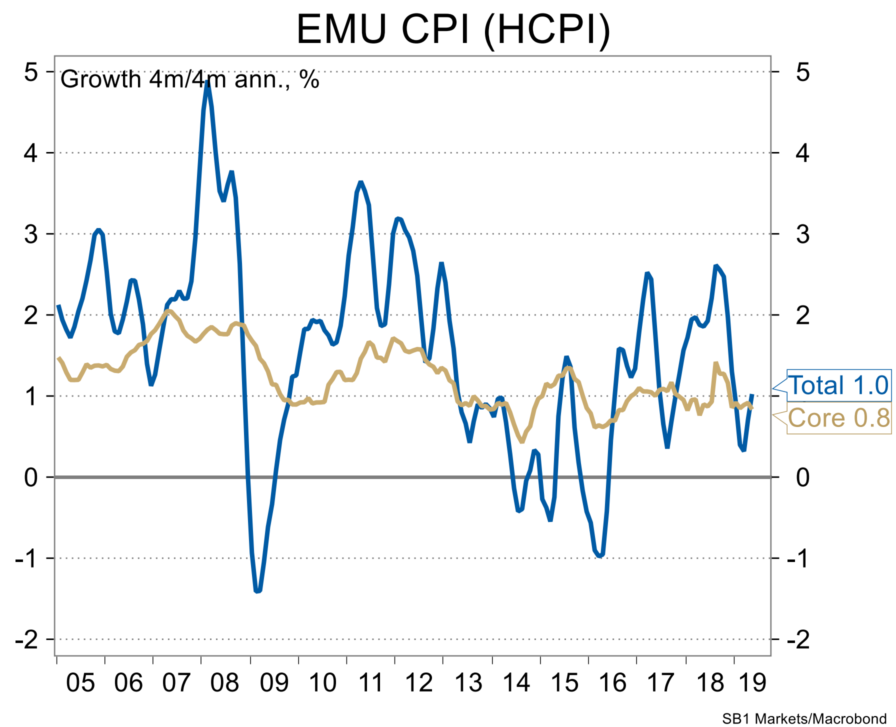


- Unemployment rates in Greece and Spain have fallen sharply since 2013, from awfully high levels. Unemployment is still very high in Greece, at 18.6% (down from 28% in 2013!). Spain down from 26% to 14%
- Soft spot: Italy may have flattened out, at 10%
- Unemployment in Germany and the Netherlands have fallen to very low levels, limited downside potential!

Core CPI inflation slumped to 0.8%, partly due to calendar effects

The 0.5 pp decline was partly a reversal of the jump in May last year, but m/m growth was subdued



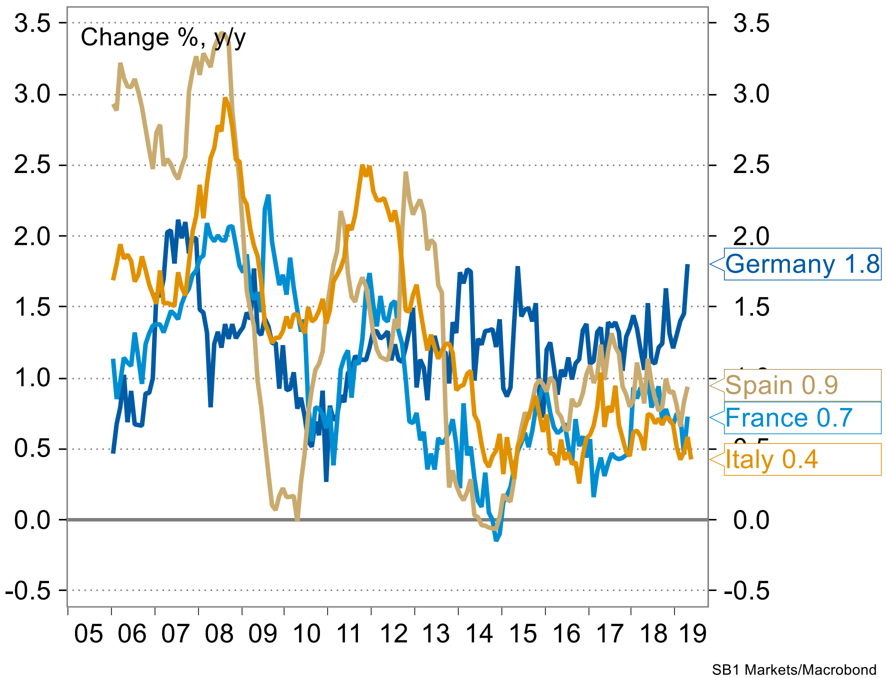


- Core CPI were close to flat m/m in May. In May last year, prices jumped 0.5%, after a slip during Easter (even after a seasonal & Easter adjustment, these months are challenging to adjust). The official annual rate dropped to 0.8%, from 1.3% in April, a decline to 1% was expected (our calculation, seasonal and Easter adjusted, reports a decline to 0.8% from 1.2% in April).
  - » We expect the core CPI y/y to accelerate marginally in June but to decline again the during the summer, increasing the pressure on ECB to act
- Total CPI growth slowed 0.5 pp to 1.2% in May. If the oil price stabilises at the present level, the headline CPI will decline further the coming months – and substantially, to well below 1%

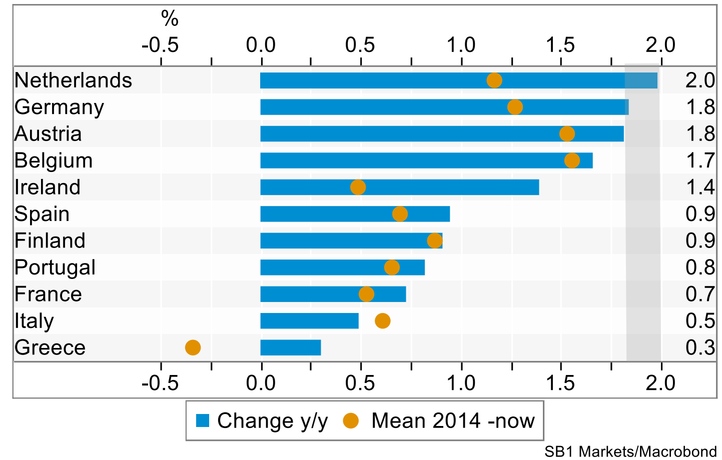
Core inflation below target almost everywhere (but not in Germany, finally)

But it's trending down everywhere, ex Germany (but is still above the avg since '14 everywhere, x It)

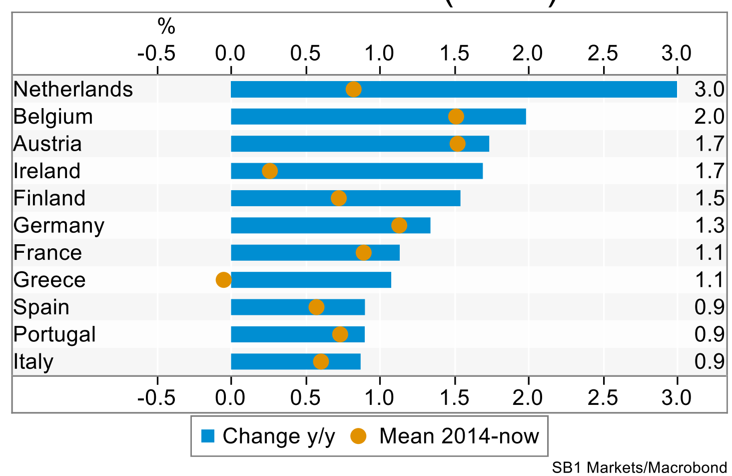
EMU Core CPI



EMU Core CPI



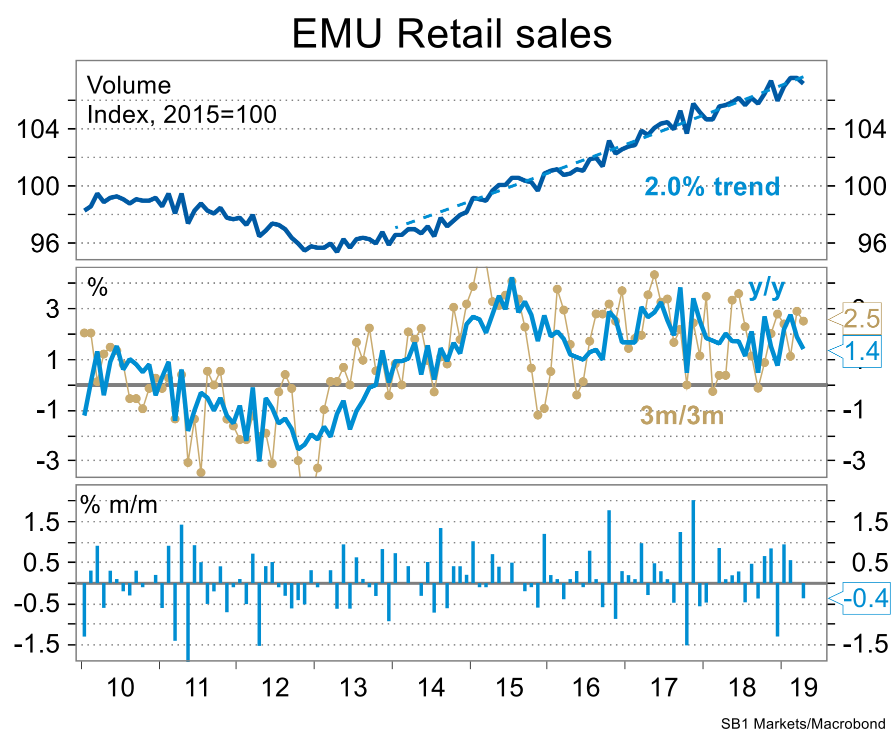
EMU Total CPI (HCPI)

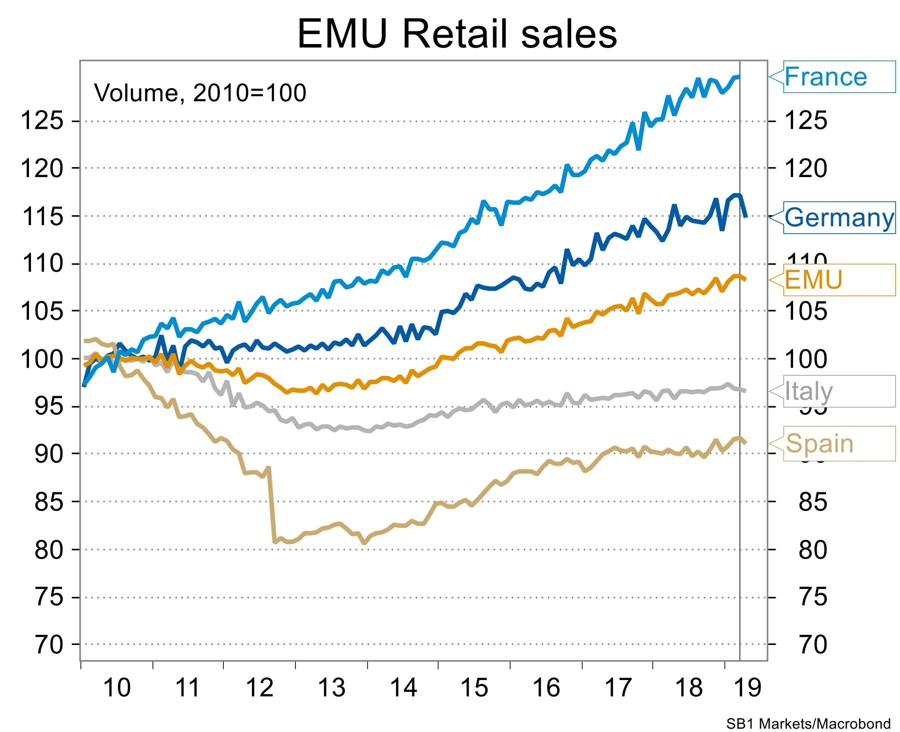


- Core inflation in Germany jumped to 1.8% in April, from 1.1% in March, due to the Easter base effects but the core has been trending up. In other major 4 countries, core CPI is now declining
- Mixed in other countries, most heading down recently

Retail sales down in April, still on a decent growth path

Retail sales down 0.4% in April, the speed into Q2 is not impressive, after a solid Q1

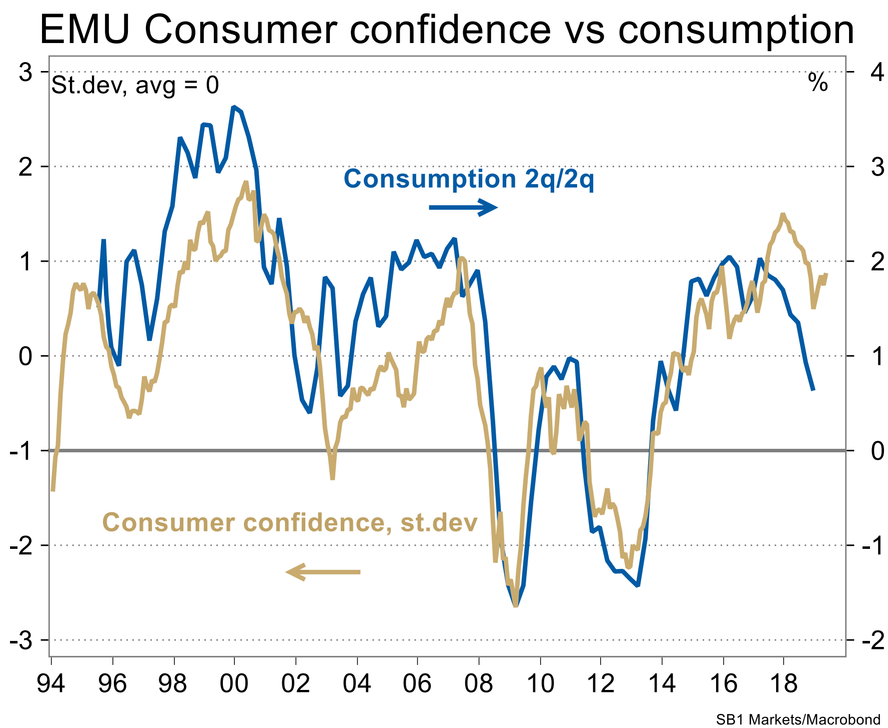


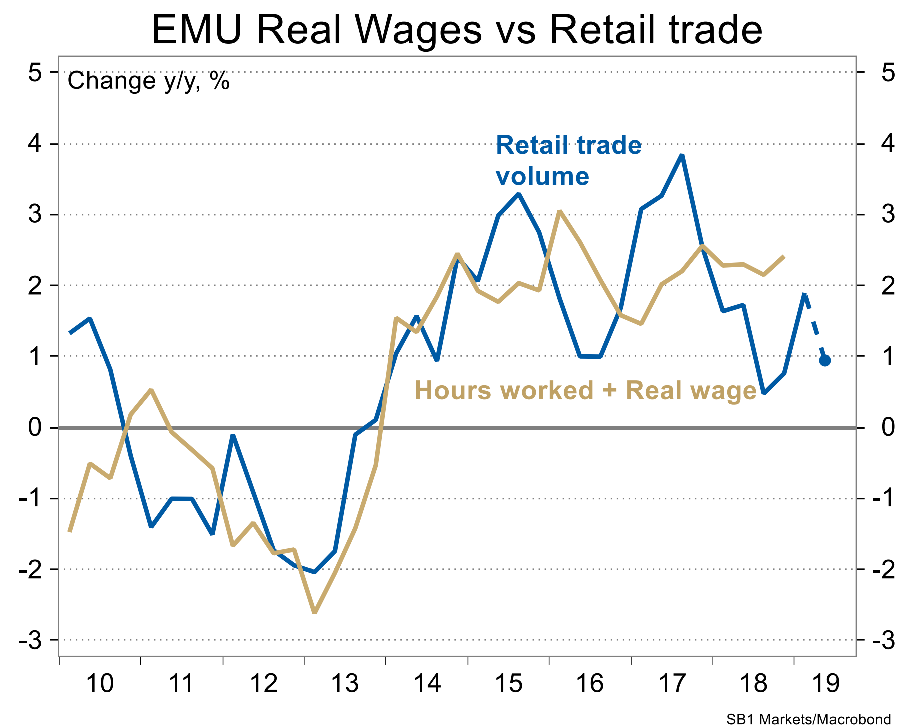


- Retail sales volume ticked down 0.4% m/m, as expected. Underlying growth (3m/3m) slowed to 2.5% and Q2 is off to a soft start, the speed into the quarter is -0.7% annualised, following the 2.9% Q1 growth rate. However, the 2% trend growth is still intact, not bad during these days of acute angst of the European economy
  - » The decline was supported by a slip in German sales. Sales in France have flattened out recently, Spain trending up, Italy not impressive
- Decelerating total inflation as well as retail price growth have helped purchases. Moreover, real wages and employment are increasing and consumer confidence is not weak, signals decent growth in consumption going forward

Consumer confidence, income do not signal stagnating consumption

.. The upside is probably limited but a moderate growth pace should be within reach

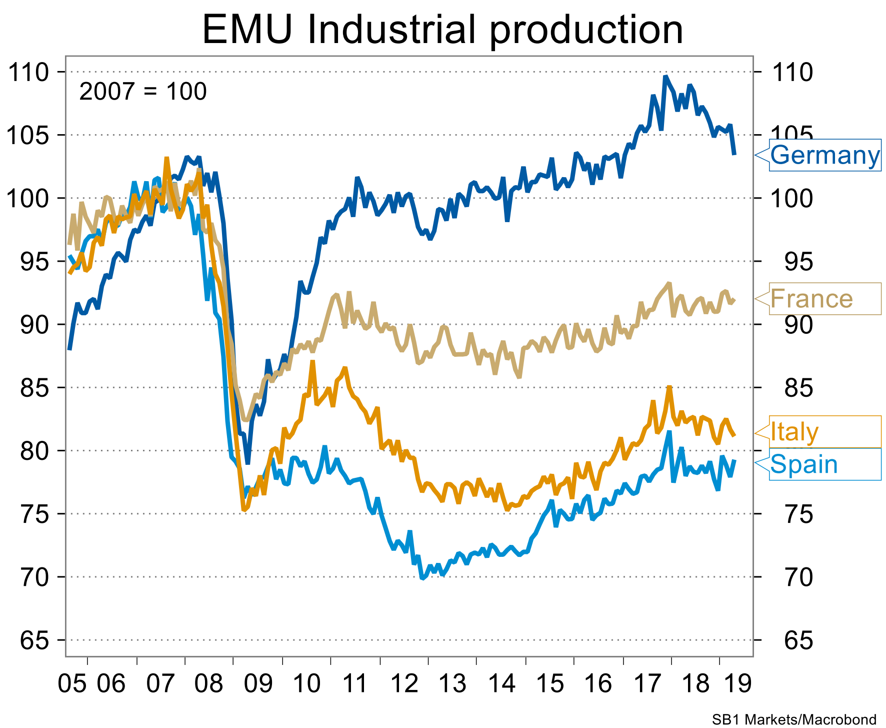


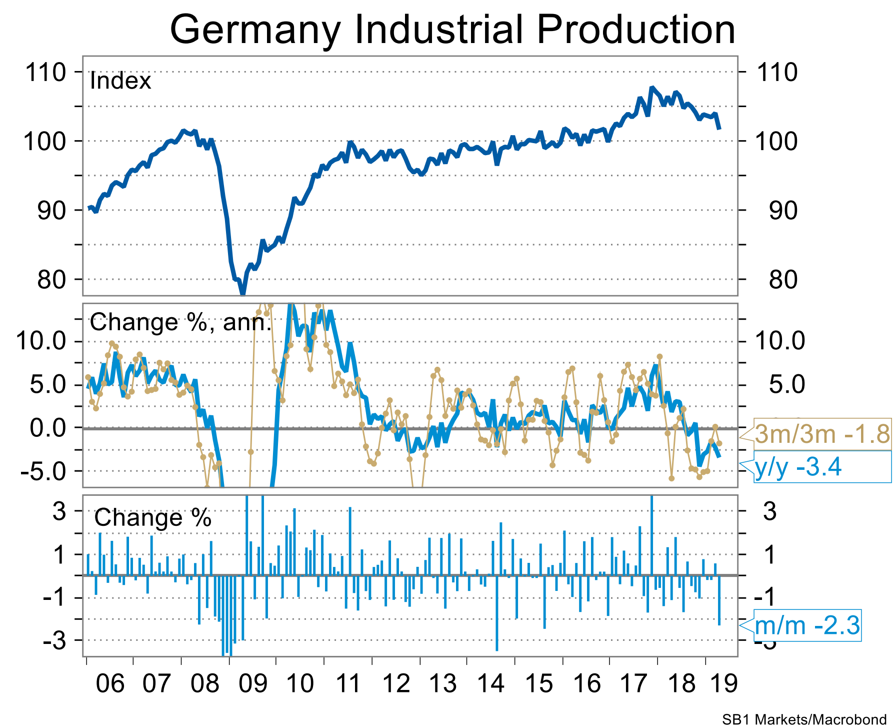


- Consumer confidence has improved and the level is not low, even if the index fell rapidly through 2018
- Real wages + hours worked, a good proxy of total disposable income is expanding faster than retail sales

German industrial production tumbled in April, EMU probably down 0.7% m/m

Production plunged 2.3% in Germany, an upswing in Spain and France can not save total EMU prod.

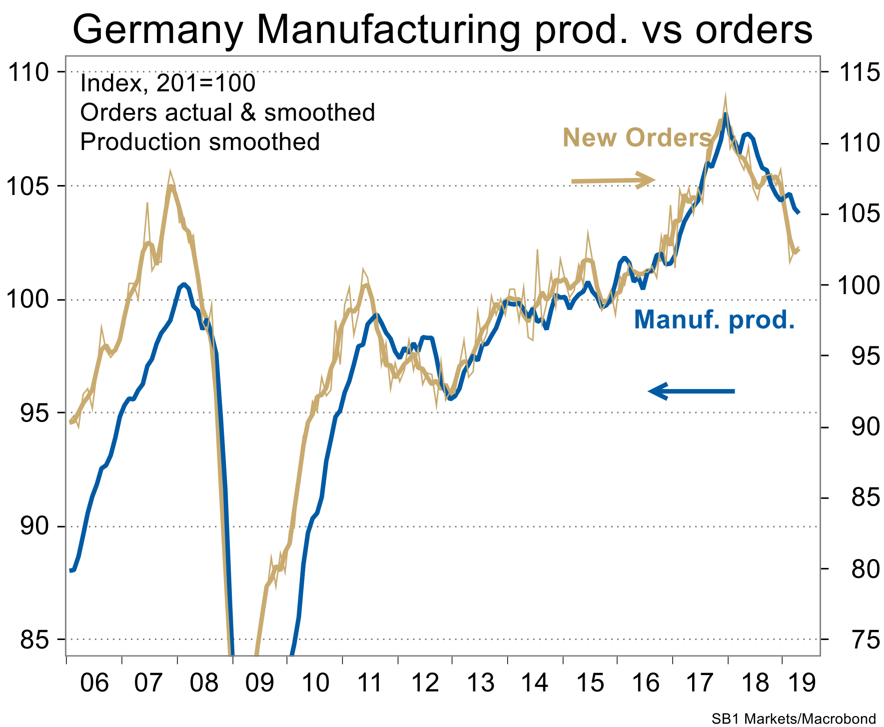


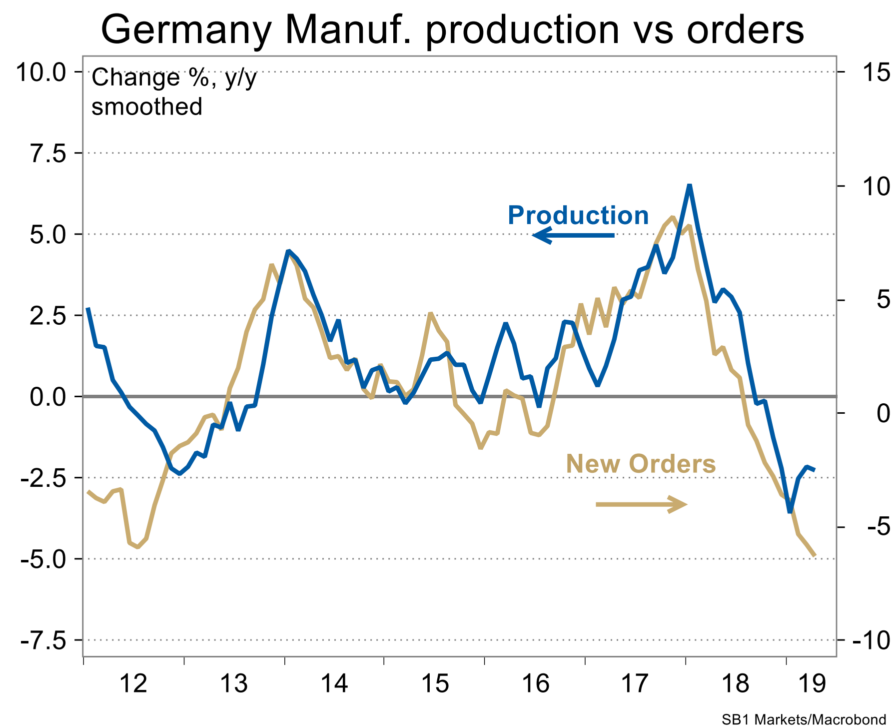


- The contraction in German industrial sectors accelerated in April, the 2.3% drop was much worse than expected. Annual rate down 3.4%. However, manufacturing production (which excludes mining and electricity production) rose 0.1% m/m, though following a huge decline in March, and the 'story' is the same
- Production in France rose modestly at 0.4%, Spain bounced back up (an 1.8% increase), both trending more or less flat. In Italy, production fell again – and the trend is down
- We assume a 0.7% decline in total EMU industrial production (ex construction), based on the data released this far
  - » Unfortunately, PMI and manufacturing orders do not signal any recovery in Eurozone manufacturing, check the next slide for German order inflows

Manufacturing orders fail to recover, bleak outlook

New orders have inched up in March/April, still pointing to deteriorating production

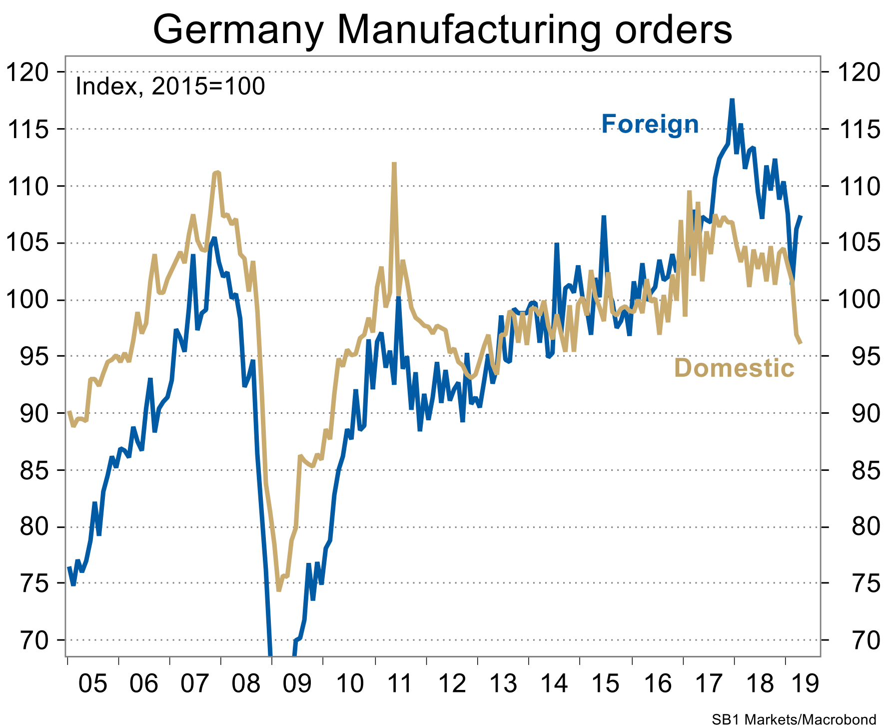


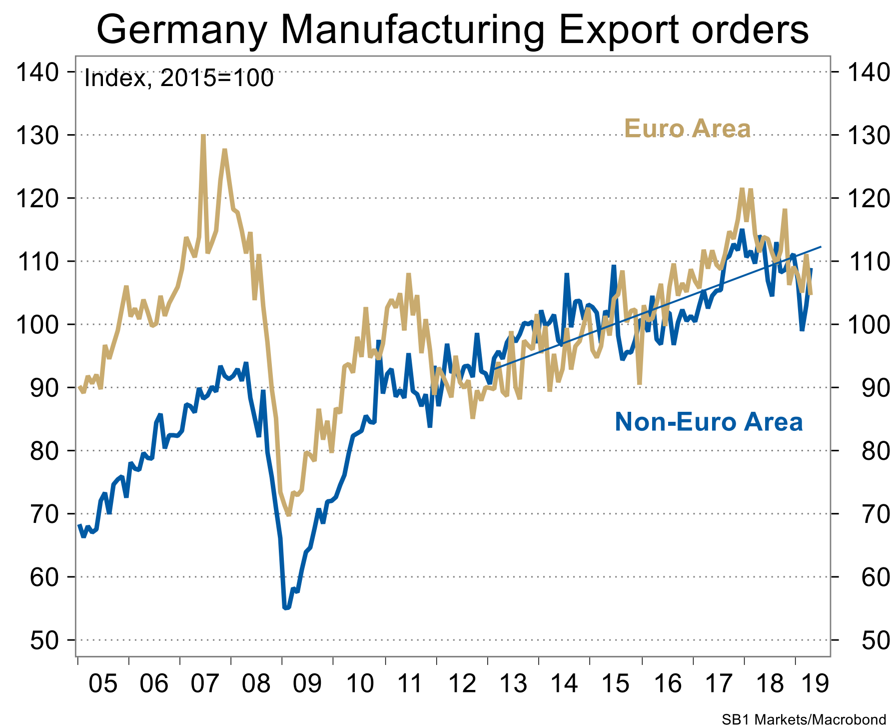


- Total manufacturing orders up 0.3% m/m in April. Orders are down 6.2% y/y (smoothed rate), the steepest decline since 2009, pointing to a deeper downturn in manufacturing output
- The German manufacturing sector have been hit by a slump in foreign orders, primarily non-EU orders. However, recent months, export orders have recovered whereas domestic orders are nosediving. Thus, the weakness cannot merely be attributed to global uncertainties and trade wars, there must be a domestic problem too

Domestic demand is tumbling, foreigners' orders stabilized

Orders from within Germany are plummeting, what is the problem??

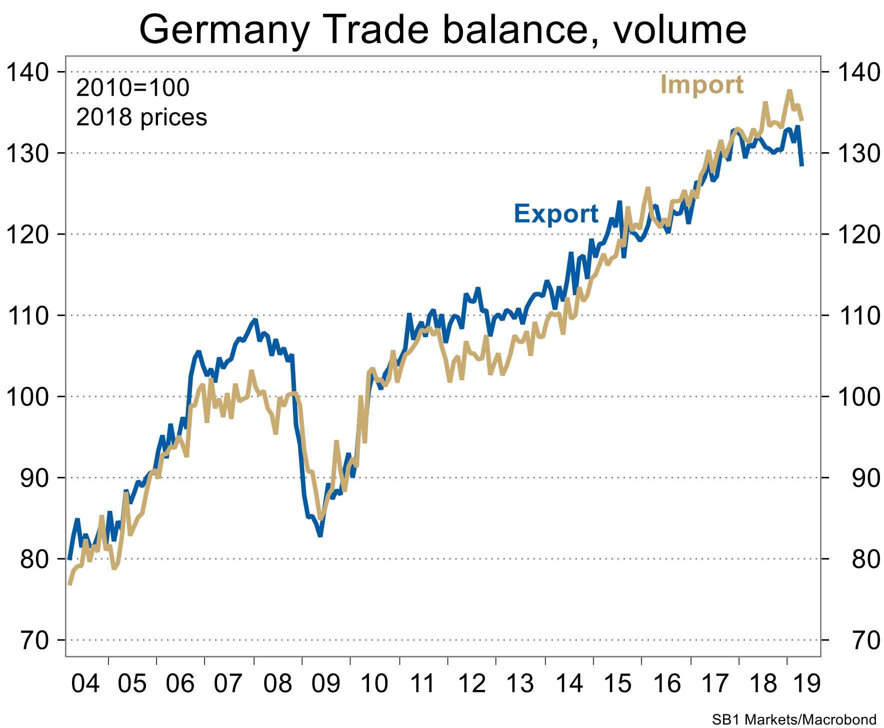


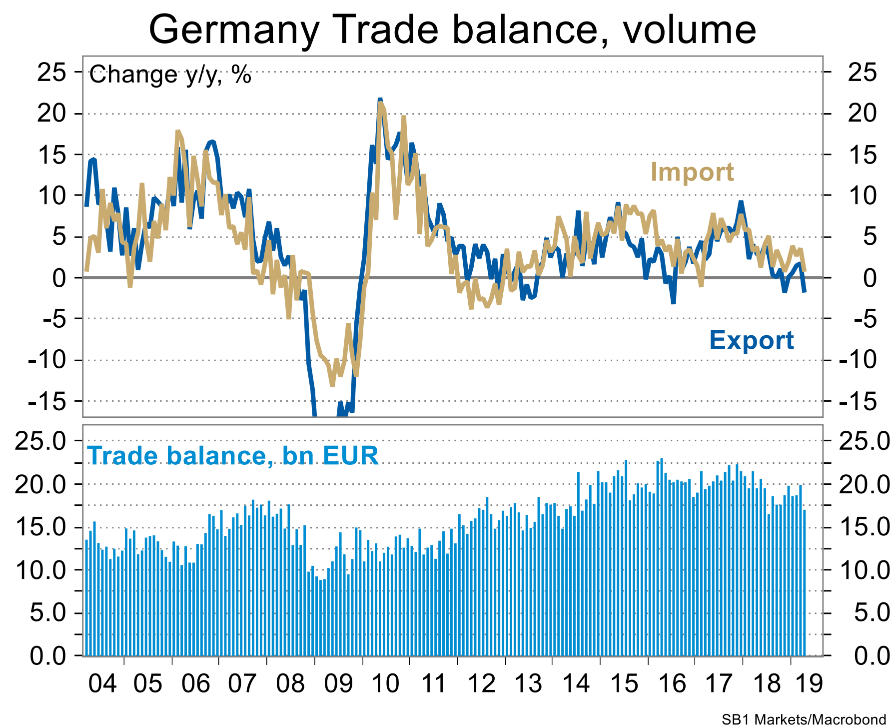


- German data are quite contradictory these days; manufacturing surveys and orders are pointing to a deep downturn, production has slowed markedly to. However, Q1 GDP revealed that domestic demand is expanding at solid rates, both business investments and private consumption increased. Barring the trouble in the auto industry, why is domestic demand waning?

Exports nosedived in April, confirming weak surveys

Exports are down 1.8% y/y to the weakest level in almost 2 years, imports still expanding marginally

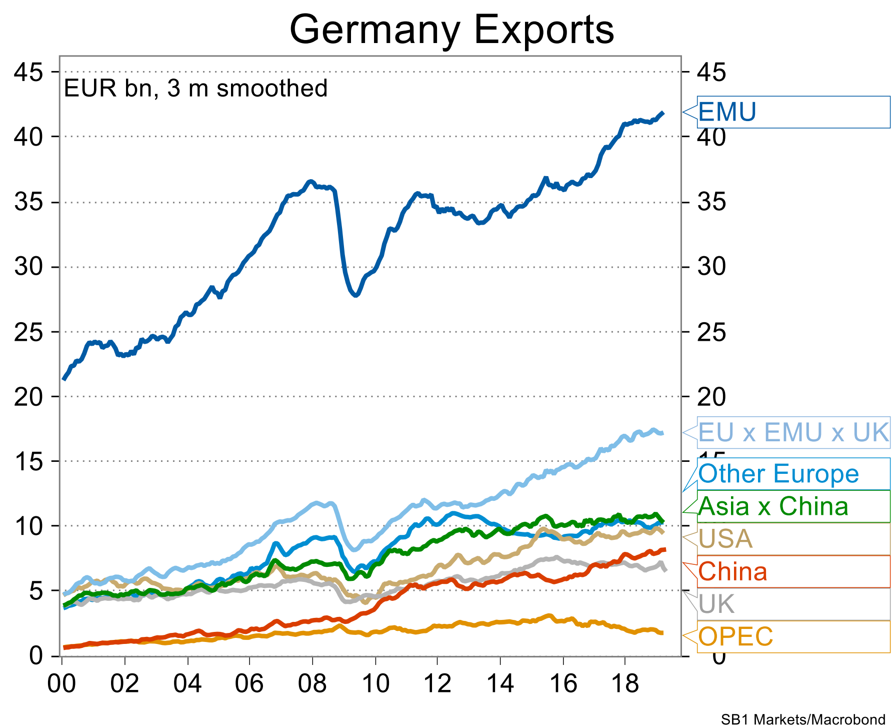


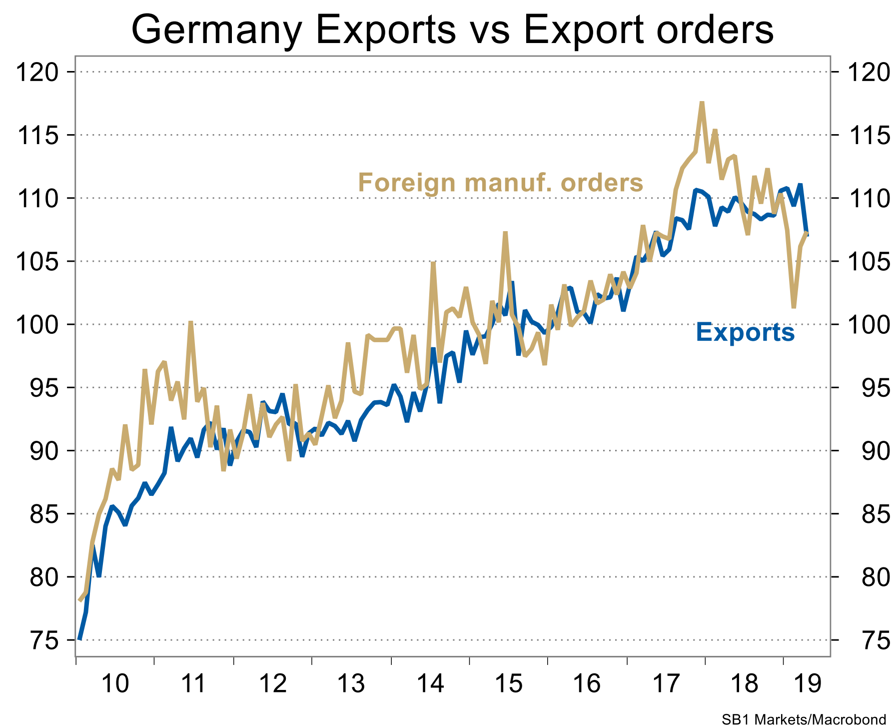


- Export volumes dropped in April, we assume down 1.8% m/m in volume (-3.7% nominal). Exports have kept up better than PMIs and export orders have been indicating recently, the April slip confirms that Germany is struggling with global headwinds (as well as domestic).
  - » Export orders have improved somewhat in March/April but the export order PMI points to a steep downturn
- Import volumes are still trending up, although at a slower pace the past year
- The German trade surplus is slowly shrinking, it fell to 4% of GDP in April (6% the prior months), from 8% in 2016

Export data still OK in most directions, China in the lead exports to the UK down

No April data on most countries but UK plunged (Brexit disruptions), others must have fallen too

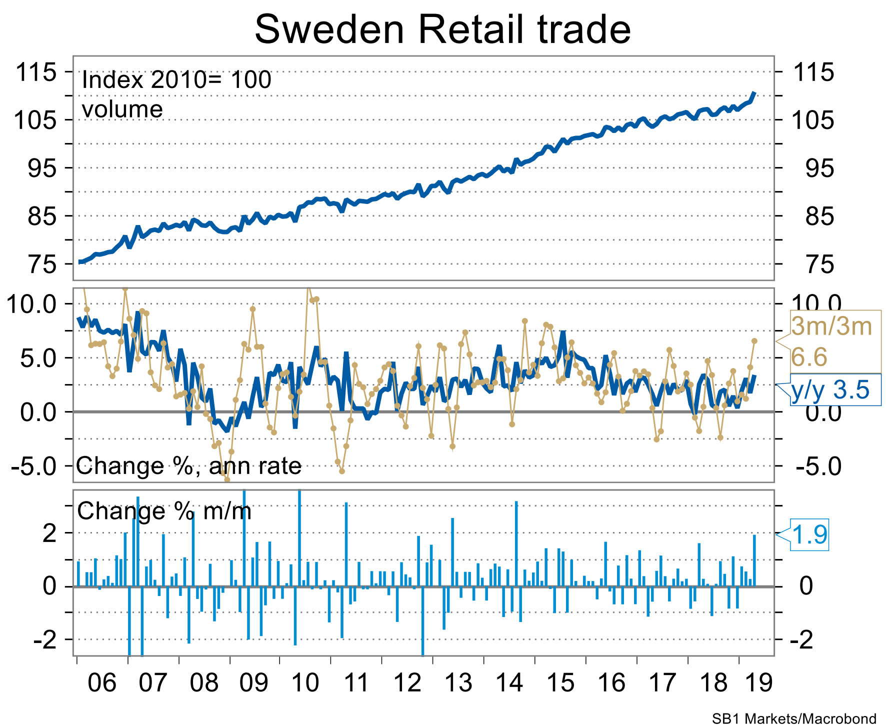




- The direct impacts of the trade war is not easy to find; and German businesses have anyway not been much directly hurt anyway. Surveys/orders are signal than somewhat else have been happening: A retreat in business investments, due to trade war/Brexit uncertainties and probably also a ‘normal' mature cycle. Most likely, businesses are holding back their purchases due to increasing global uncertainties
- Exports to UK slipped in April, as businesses there are cutting back purchases after a huge stockpiling ahead of the prior Brexit deadline. Exports to the US is still trending up (no April data), and exports to China are increasing at a fast pace. Exports to other EMU partners have also strengthened recently (no April data), exports to other Europe mixed. Exports to Opec have been the weak link recent two years
- Germany's main export markets: The other EMU countries (38%), other EU countries x UK (16%), Asia x China (10%), Europe x EU (9%), USA (9%), China (7%), UK (6%)

Retail sales spiked 1.9% in April, Easter effects??

Even if the jump was due to the Easter, sales are anyway back at the old, moderate trend growth



- Retail sales spiked 1.9% m/m in April, a 4 year high. Easter effects probably contributed, like in Norway. Still, sales have been slowly improving recent months and are more or less back at the 2.2% growth path, following a soft slowdown
- Price inflation is subsiding, supporting volume growth. More to go?
- On the other hand, consumer confidence is weakening and is not pointing to a consumption upswing. A soft housing market is not indicating brisk demand either. However, households' disposable income is rising and employment is still growing, not arguments for a slowdown in consumption

Highlights

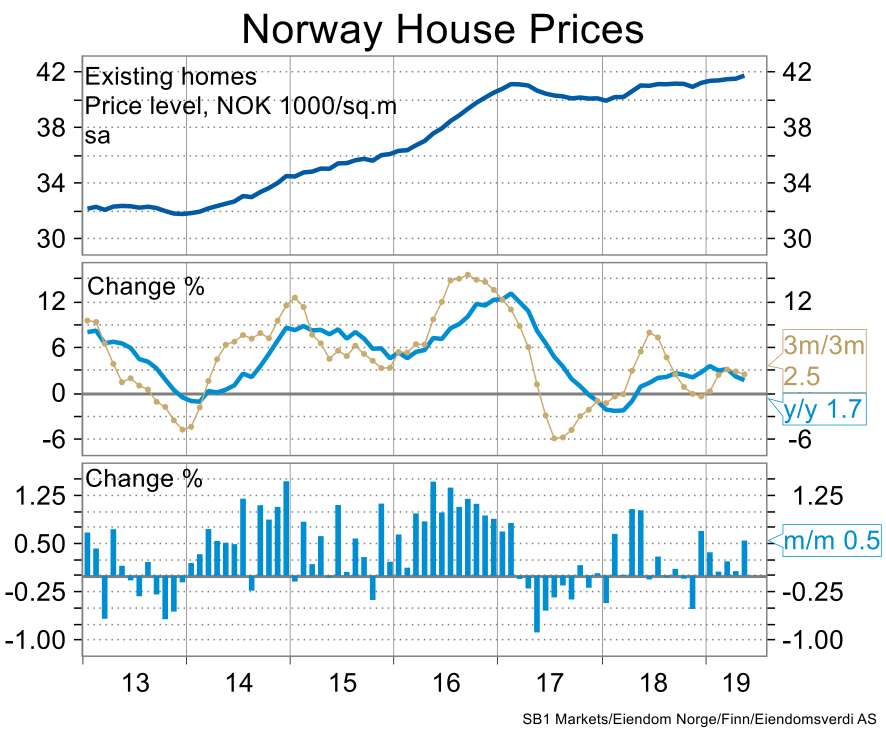
The world around us

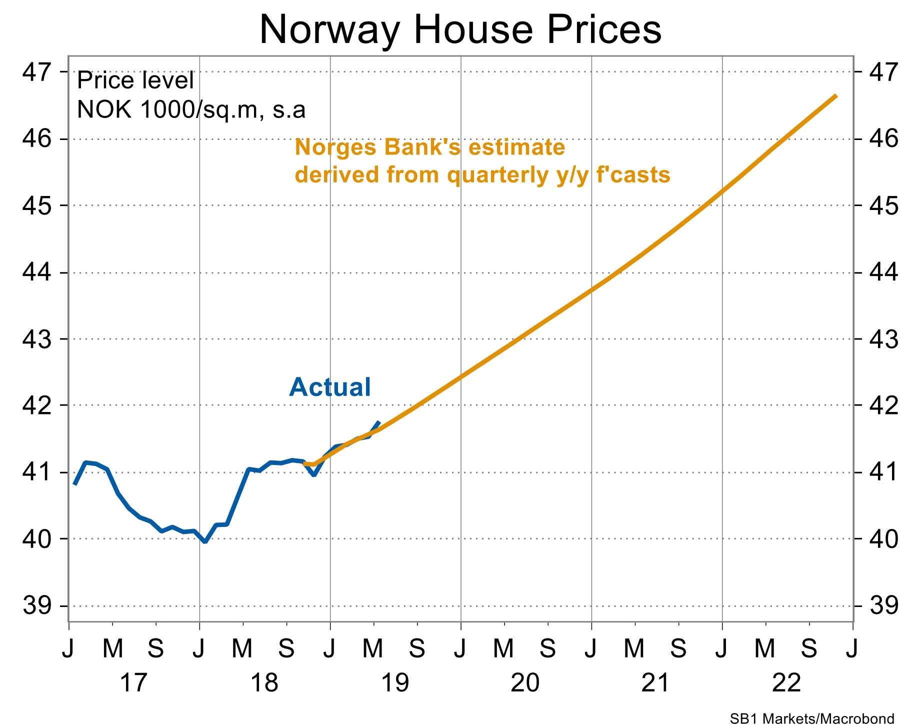
The Norwegian economy

Market charts & comments

House prices rose more than expected in May, in spite soaring supply

Prices up 0.5% s.a in May, we expected 0.2%. However, market dynamics indicate muted growth

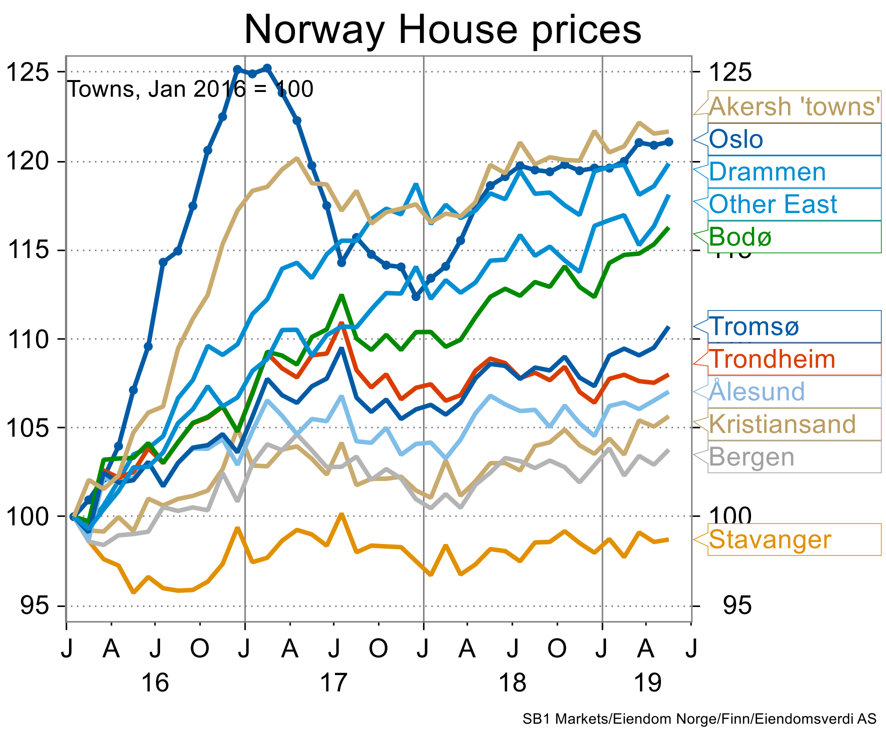


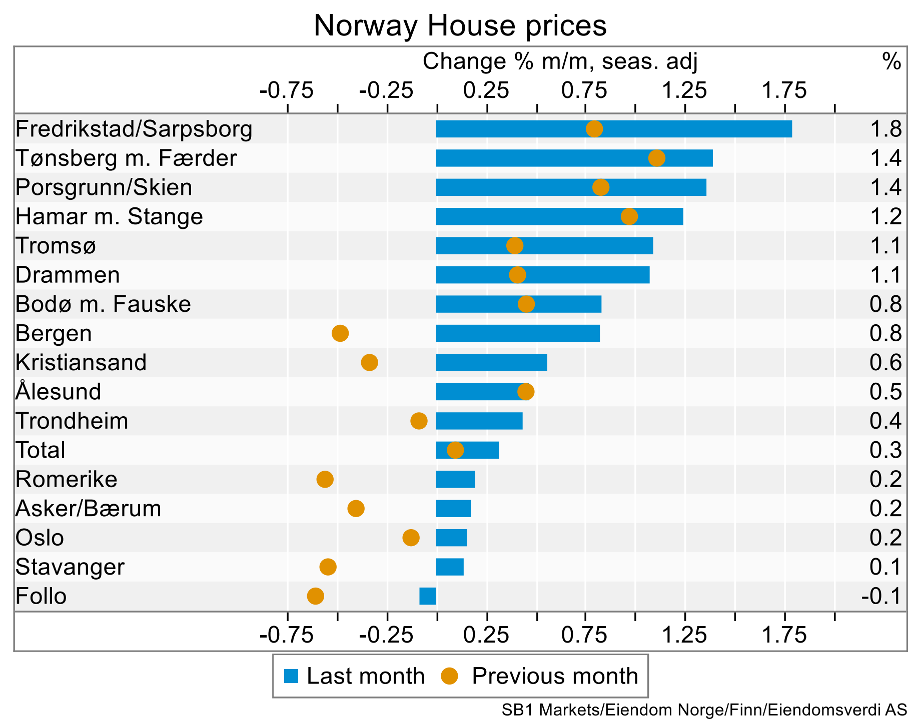


- **House prices** climbed 0.5% m/m seasonally adjusted in May (0.7% unadjusted), 0.3 pp above our f'cast. Underlying growth has flattened out at a 2.5% speed recent months (measured 3m/3m). The annual growth rate fell to 1.7%. Prices are marginally above Norges Bank's path
  - » A broad upswing in May; prices rose m/m in all regions ex Follo. Recent months, prices have fallen in East Norway x Oslo/Akershus, climbing in others
- **The inventory of unsold homes** is soaring, the highest in 10 years. The high inventory is not due to lack of demand but to a steep rise in the number of new listings (of existing homes). The number of transactions is trending steeply upwards, reflecting brisk demand
- **Still, short term dynamics signal slow/zero price growth the coming months. And interest rates are on the way up, limited upside!**

Prices rose almost everywhere in May, just Follo down

Prices are zig-zagging on a monthly basis, just noise

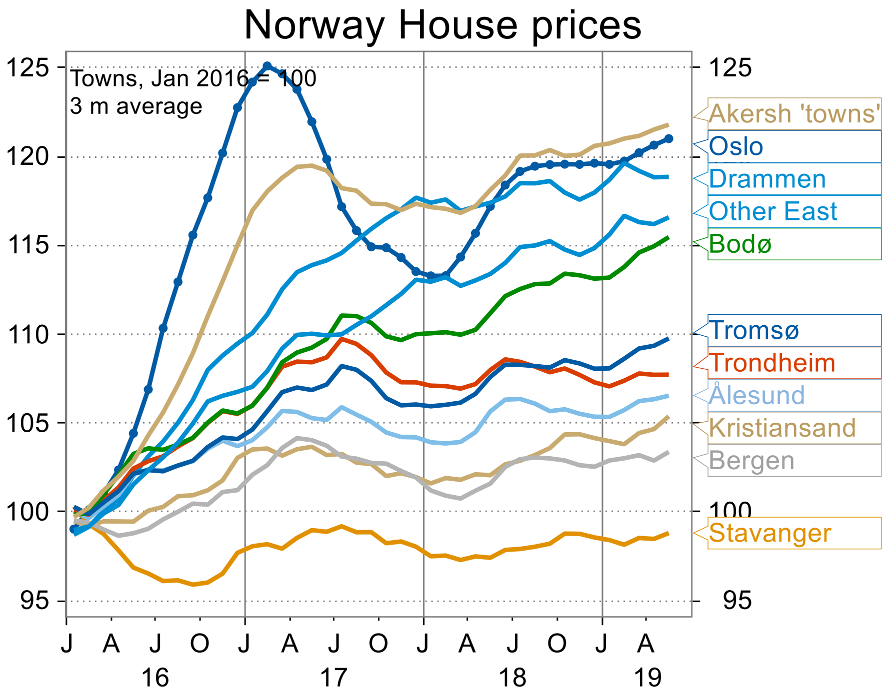




- The monthly data are too volatile, check the much more ‘relevant’ 3 month averages next page

Recent months: Broad upswing, prices are climbing in all cities, just East falling

Prices are accelerating in 8 cities, slowing in 3 and declining in just 4



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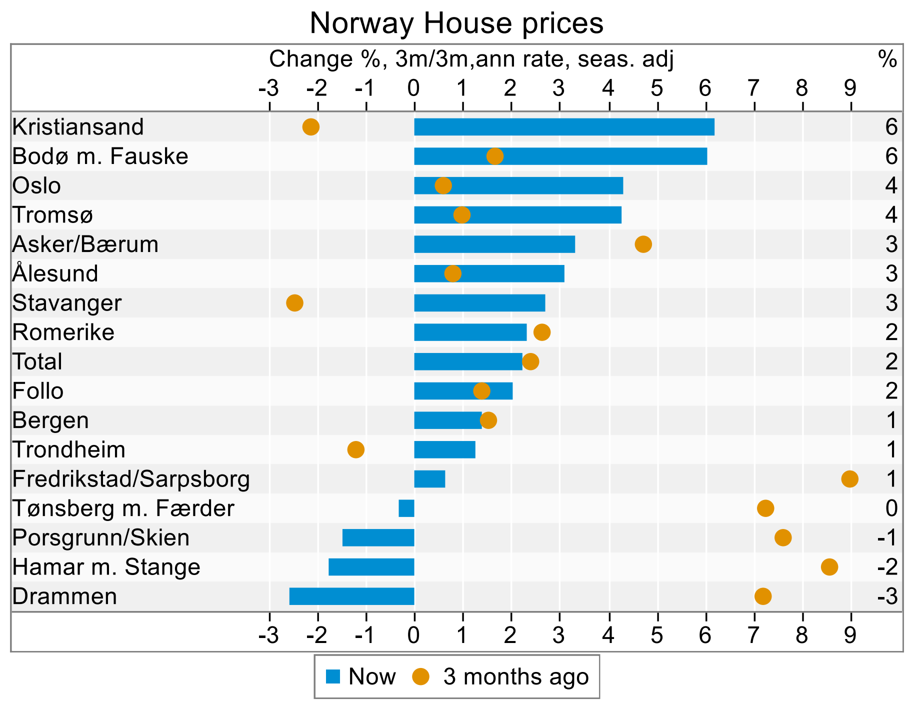


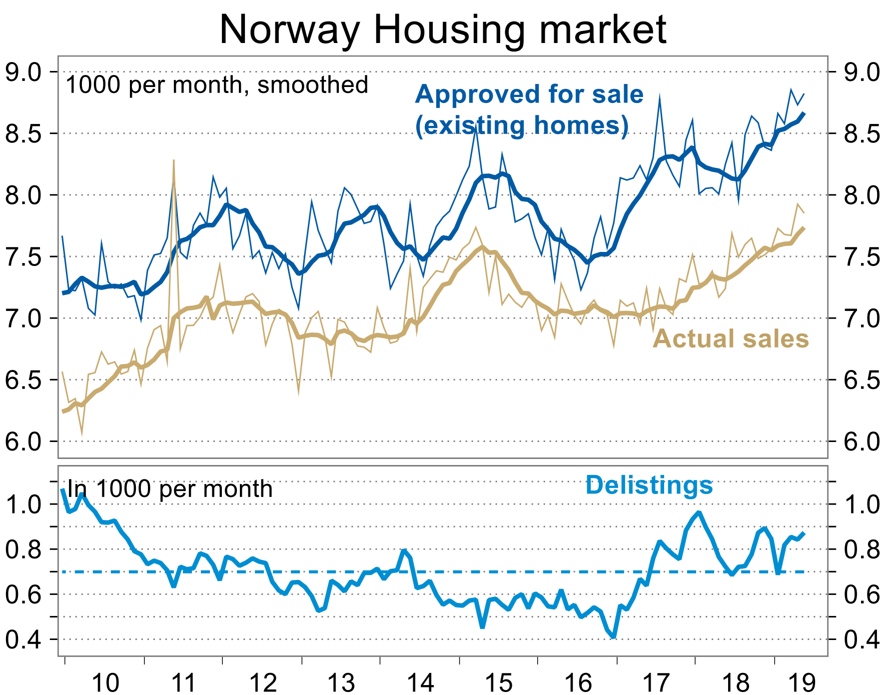
SB1 Markets/Eiendom Norge/Finn/Eiendomsverdi AS

- Measured 3m/3m annualised, prices are now rising in all cities expect Drammen, Hamar, and other Eastern cities ex Oslo/Akershus. In these towns, prices increased in late 2018/early 2019 and have been retreating the past 3-4 months. Kristiansand and Bodø have really gained speed recently, Oslo is accelerating too, up at a 4 - 6% pace
  - » Compared to 3 months ago, prices are accelerating in 8 cities, slowing in 3 and declining in 4
  - » Prices in most cities are now above the local 2017 peak level. Oslo is still some 3 % below the peak, Trondheim, Bergen are below too. And Stavanger flat vs the 17 peak but is down 11% from the June 2013 peak (btw, one year before the oil prices collapsed)

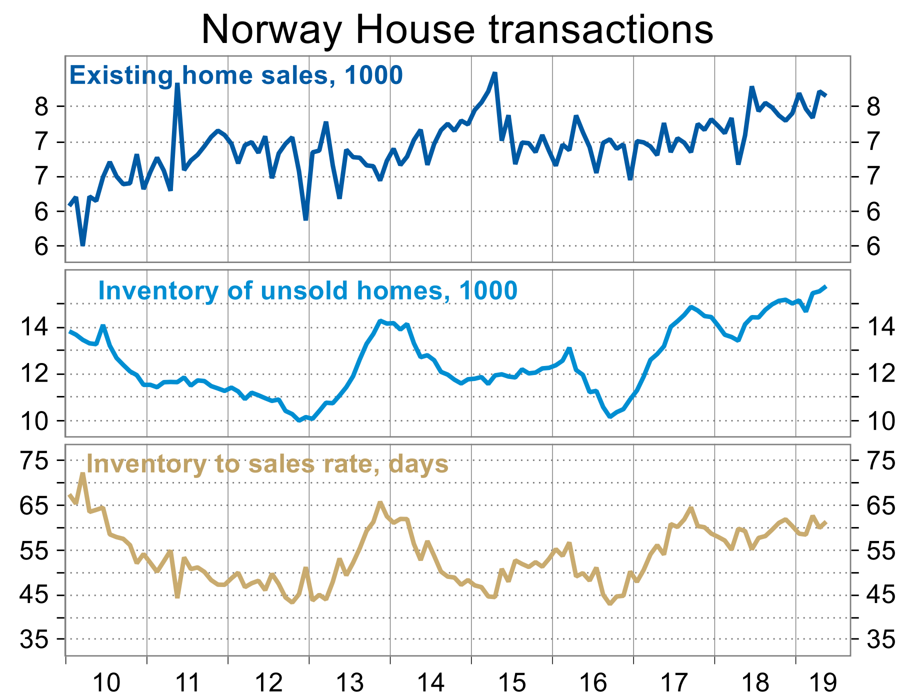
SpareBank 1 MARKETS

A buyers' market? New listings are soaring, very high no of unsold homes

Not demand weakness but many homes approved for sale is lifting the inventory



SB1 Markets/Macrobond

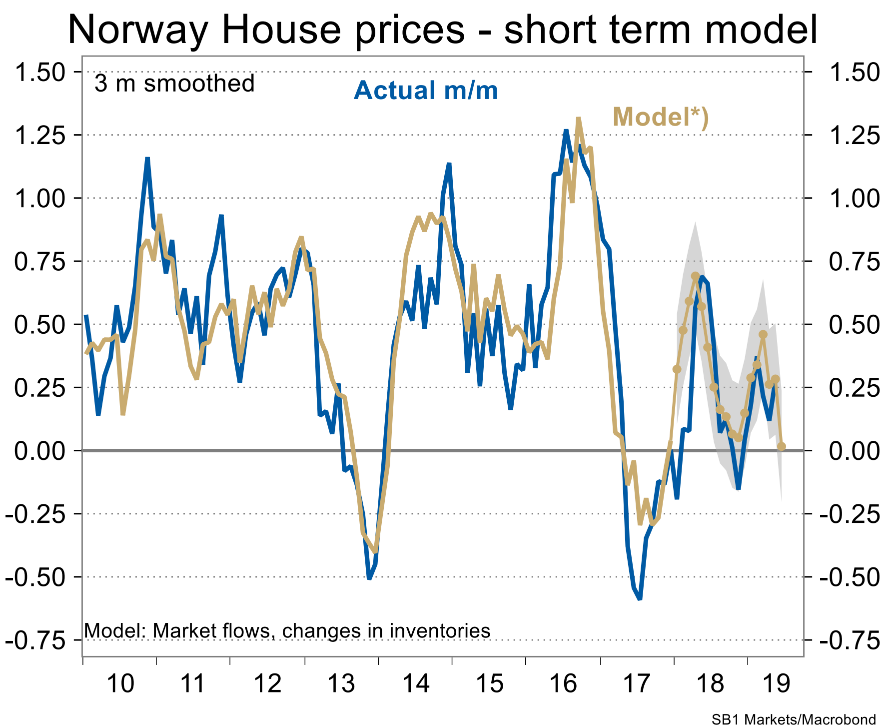


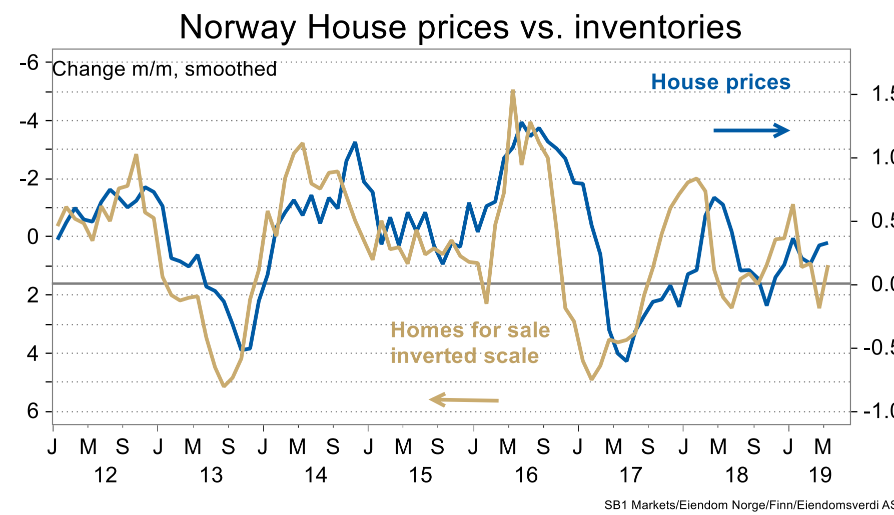
SB1 Markets/Eiendom Norge/Finn/Eiendomsverdi AS

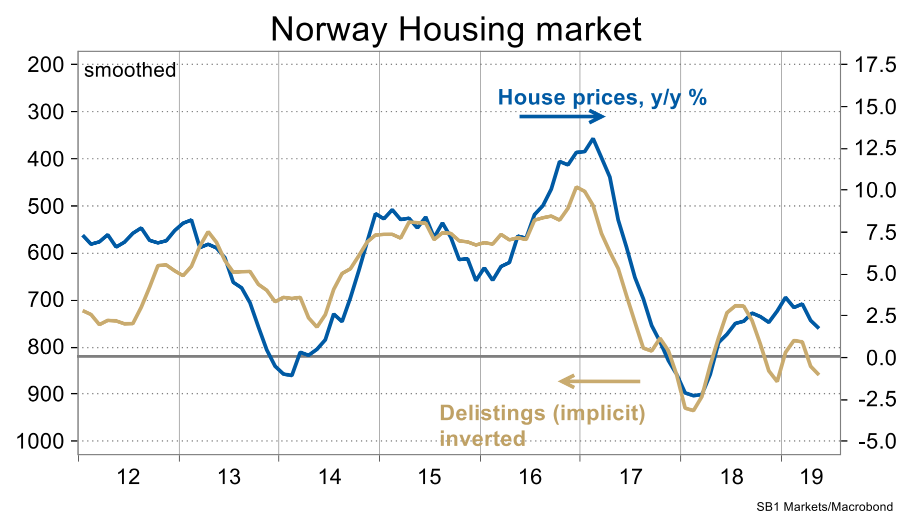
- **New listings of existing homes** increased in May and is trending steeply up. It will most likely remain high for some time.
- **The number of sales** inched down but has been climbing the past year, reflecting strong demand. However, demand is not sufficient to absorb the surging supply of homes; thus, the **number of homes for sale (inventory) is rising**. The inventory edged up to another 10 year high, dampening price inflation. The inventory is flat measured against the number of transactions, and the inventory to sales rate is flat – but average avg. The number of delistings is quite high too, may reflect some mismatch between actual prices and price expectations
- The flow balance on the housing market indicates modest to zero price growth the coming months, check next page

Market flows signal muted price growth the coming months

High inventories and delistings are not indicating strong growth (and interest rates are coming up)



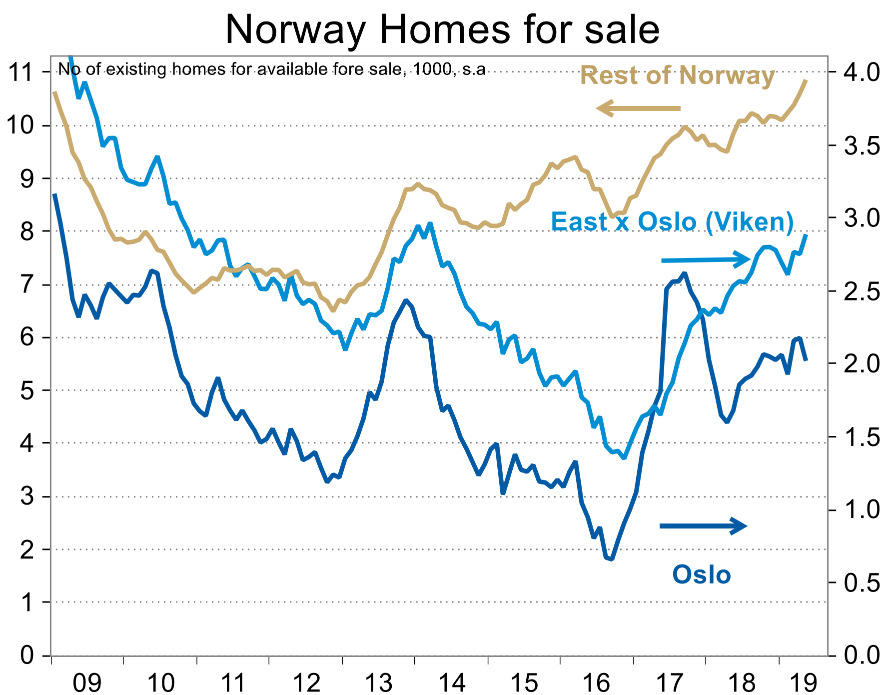




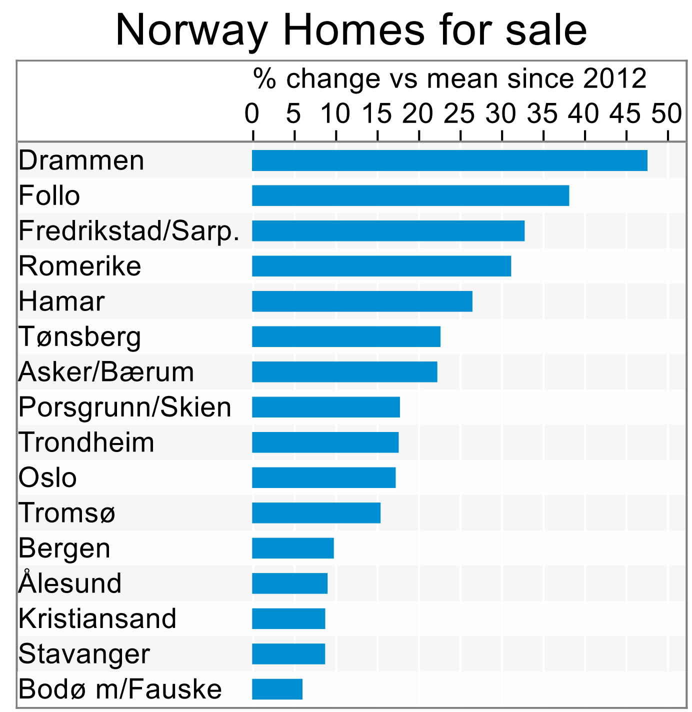
- A somewhat weaker mix for the short term dynamics, signals soft to zero growth the coming months
- *This is not a long term price model, just a short term price model based on flows of approved and actual sales, and changes in the inventory of unsold homes (taking account of delistings)*

The number of homes for sale is higher than ‘normal’ in all cities

… even as inventories in Oslo are still well below the 2017 level. Rest of Norway is soaring!



SB1 Markets/Eiendom Norge/Finn/Eiendomsverdi AS

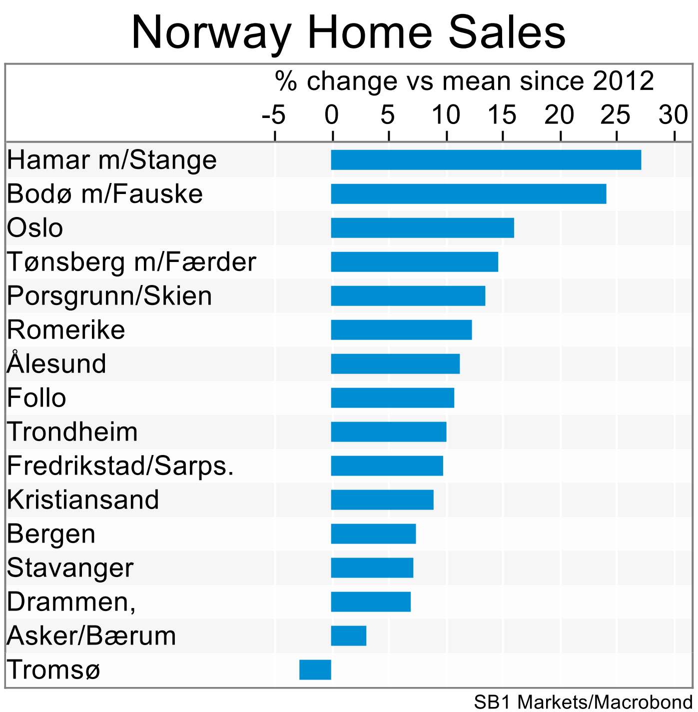


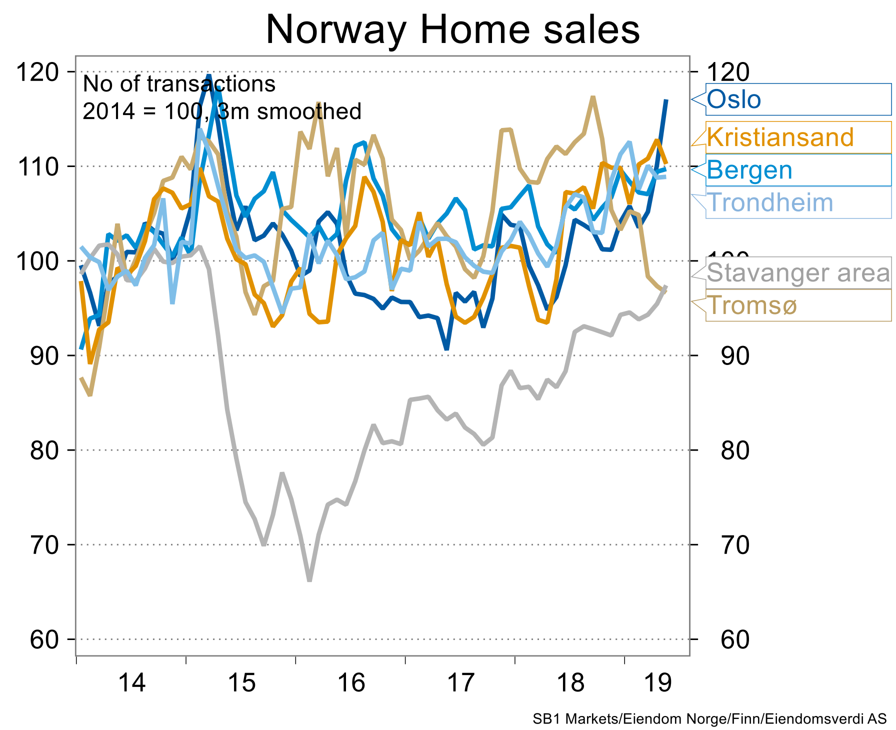
SB1 Markets/Macrobond

- The number of homes for sale have been increasing all regions recent years, higher than the avg since 2012 (some revisions of data, the big picture is not altered)
- Norway outside Viken (Akershus, Buskerud, Østfold; or East x Oslo) & Oslo report record high number for existing homes for sale (data from 2009). The inventory in Viken is increasing too, at the highest level since 2014. Drammen, Follo, Fredrikstad are at the top of the listings list
- Oslo inventories are rising but are still far below the 2017 levels

Sales are surging in Oslo, waning in Tromsø?

The number of transactions are higher than the avg since 2012 in all regions ex Tromsø



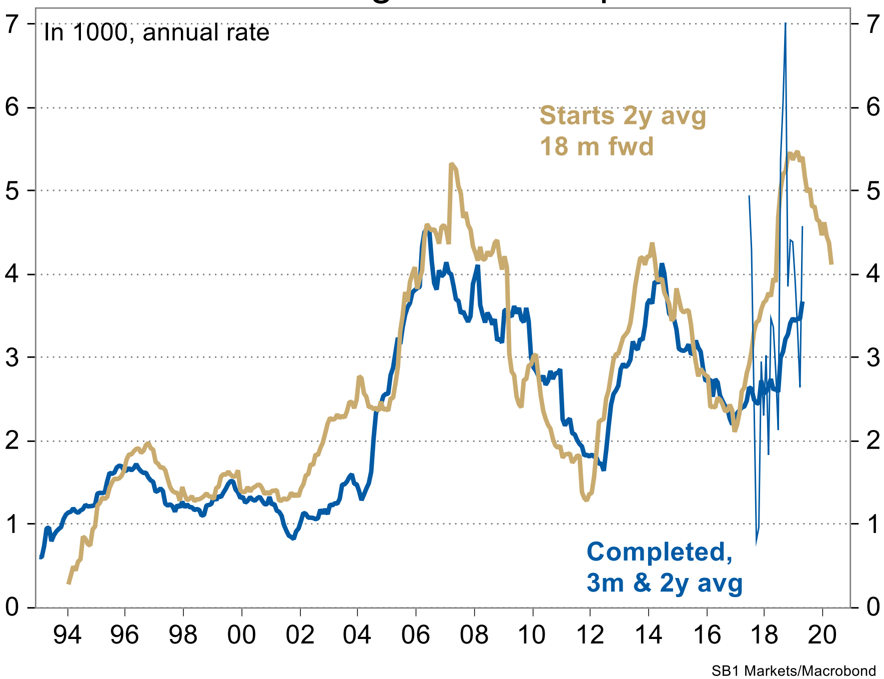


- Even with declining sales and rising supply of homes for sale, Tromsø prices are up 4% 3m/3m (annualized) and 2% y/y
- Oslo demand must be strong (even as the supply is even higher thus, the number of homes for sale is rising)

Still a lot of new homes to be filled up yet supply may be peaking now

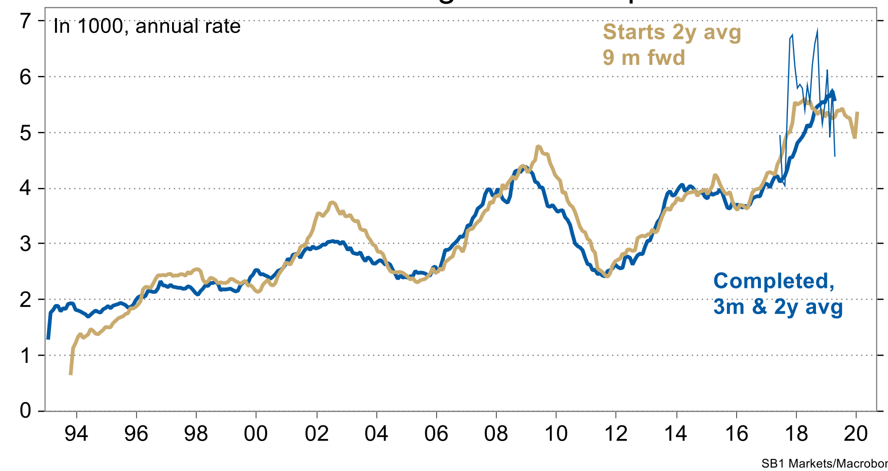
The no of completed homes will remain high in Oslo, probably not much upside elsewhere

Oslo Housing starts/completions

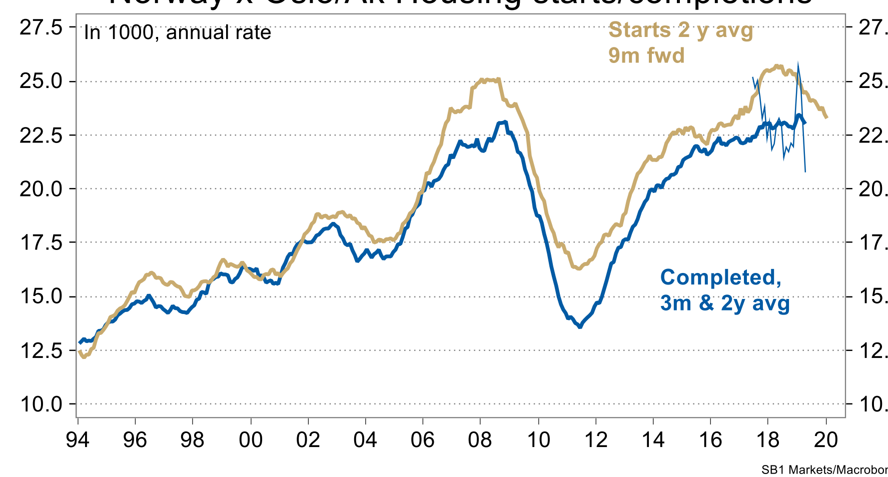


- Due to a high level of housing starts in Oslo in 2016–17, the number of completions has increased rapidly and will stay at a high level the coming year or more
  - » Supply have probably peaked Akershus but the coming deliveries in Oslo are larger than a marginal decline in Akershus
- Supply of completed houses in Norway x Oslo/Akershus is slowly rising but will soon peak. However, the level is still unusually high at the same time is population growth has slowed, income growth muted, and interest rates are coming up… Interesting

Akershus Housing starts/completions

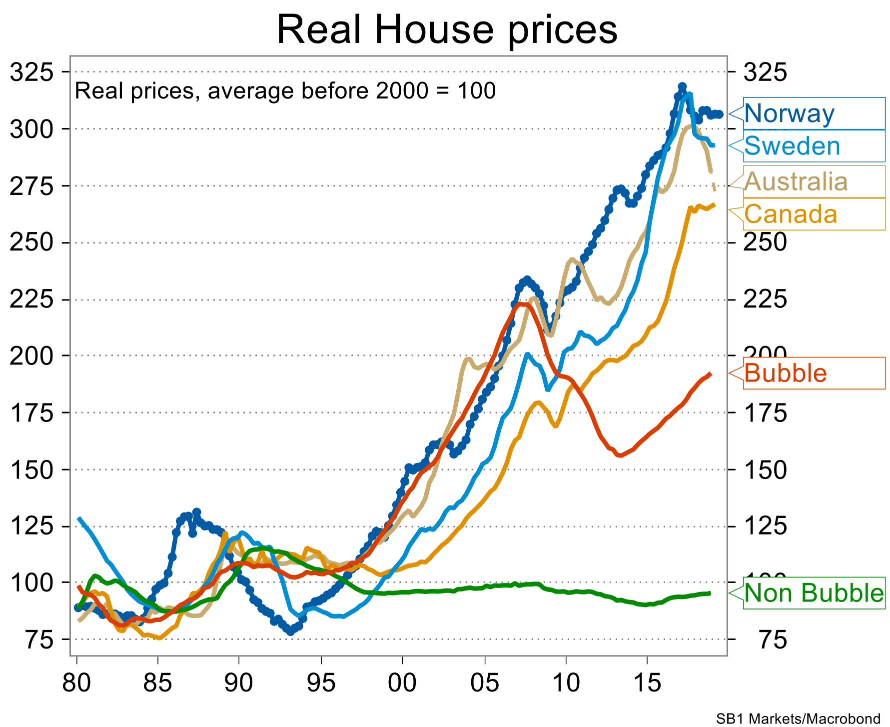


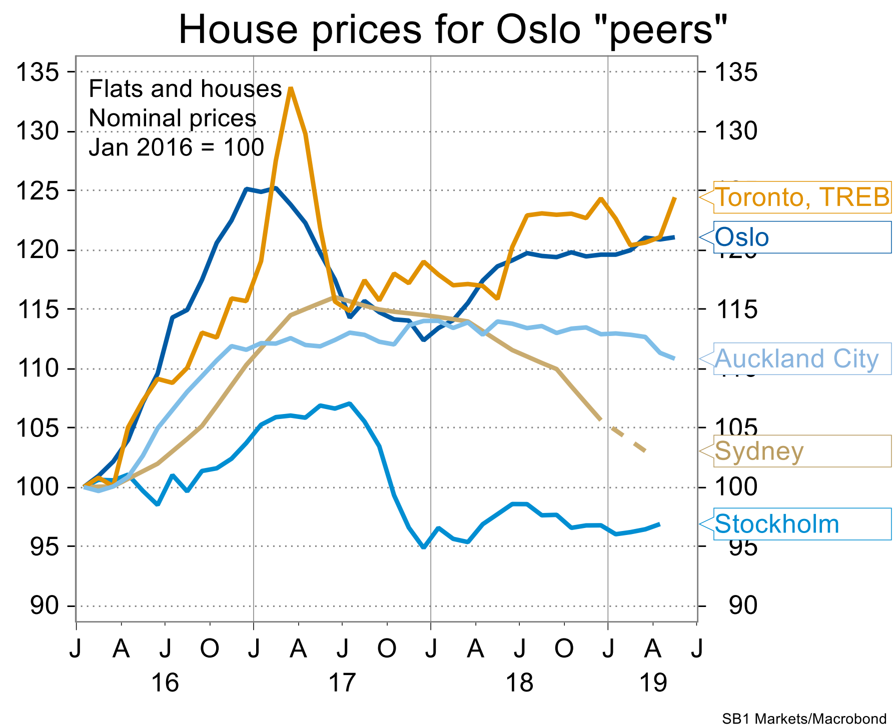
Norway x Oslo/Ak Housing starts/completions



Some housing weakness in other 'super cycle' countries too

Real prices in Norway, Sweden and Canada have fallen, Canada flattening

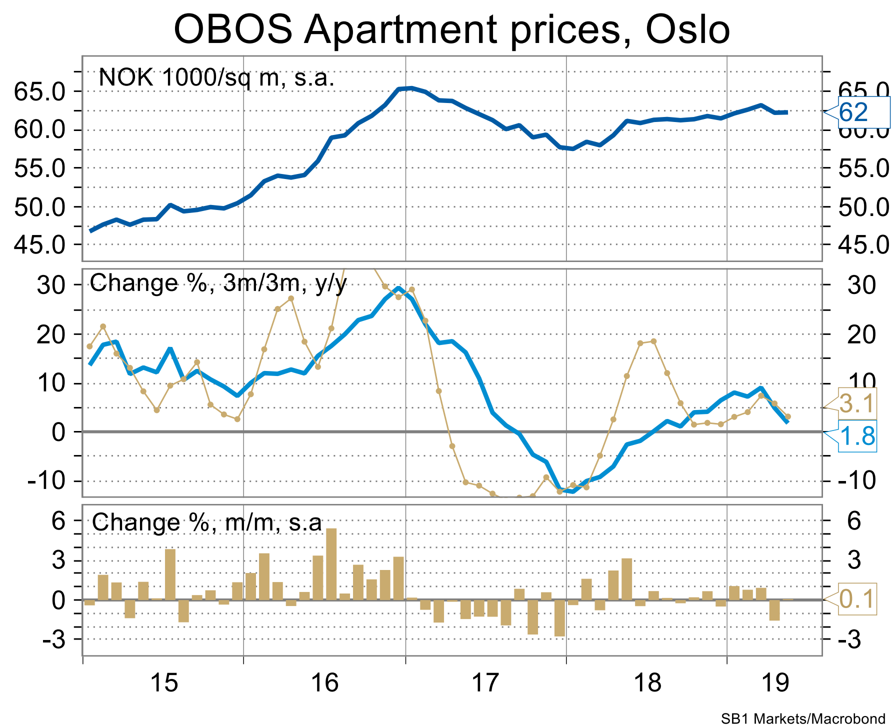


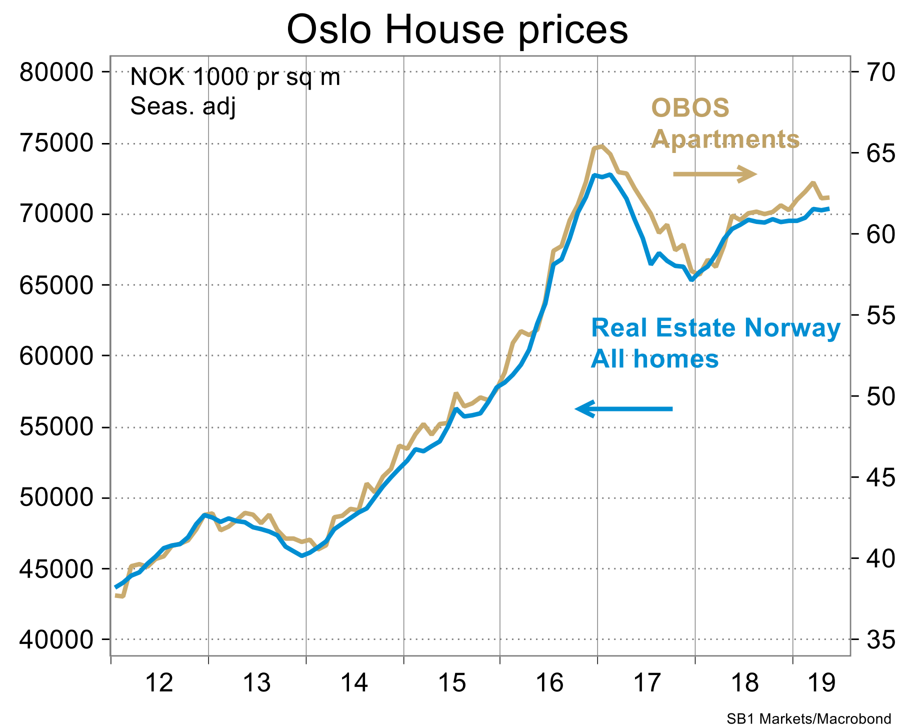


- However, mixed among the super guys recently: Oslo slowly on the way up again, Stockholm has flattened (apartments & detached homes avg). Auckland is trending slowly down while Sydney is falling sharply, down 11% from the peak in Q2 2017, in nominal terms! Toronto has gained some pace
- New housing market/debt regulations (foreigner buying restrictions, LTV/LTI/mandatory amortisation) – and in Canada higher interest rates – may have created 'some turbulence' – prices have slowed/declined since 2017
- No surprise, household debt is high and rising in these countries, with Norway in the lead, at some 240% of disp. income (it has nothing to do with low interest rates, right??)

OBOS Oslo apartment price growth muted in May, underlying growth cools

OBOS prices rose just 0.1% m/m in May after declining in April, flat since January

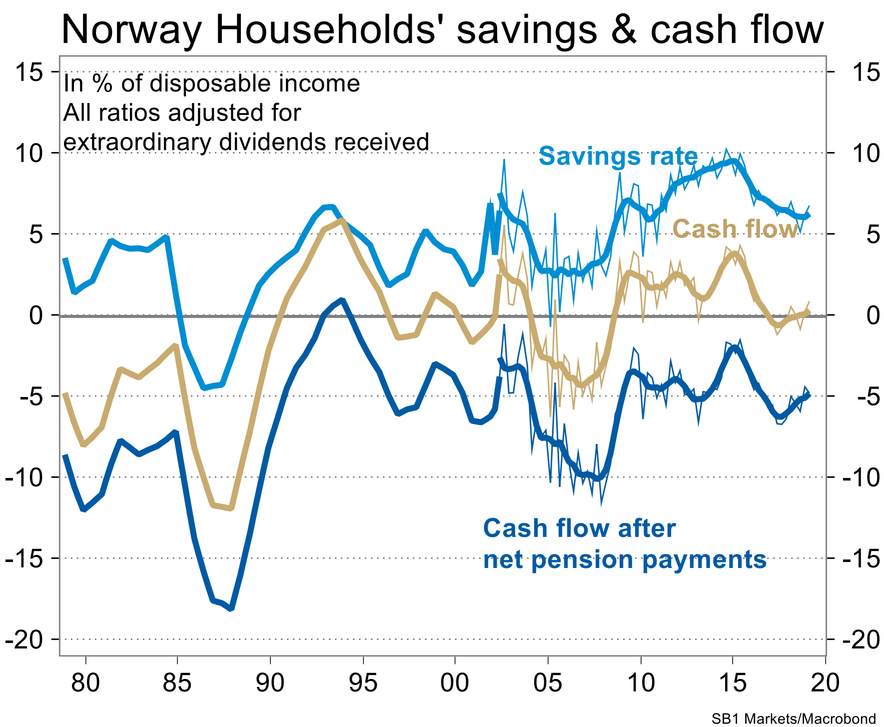


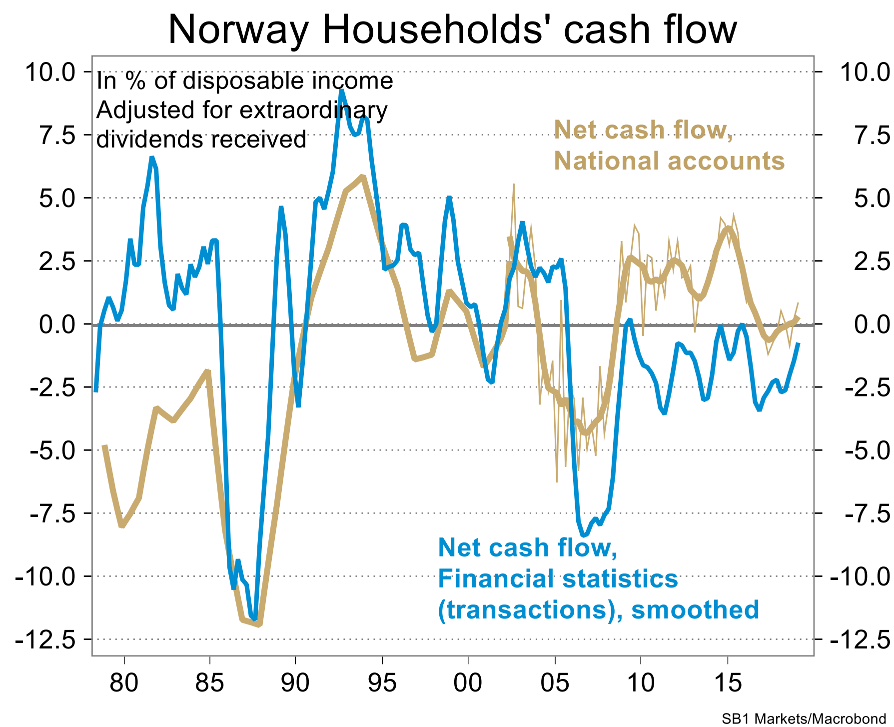


- OBOS Oslo apartment prices rose just marginally m/m in May(seasonally adjusted, +0.7% unadjusted). Prices have turned slowly up since last spring, decelerating the past 2 months. Signs of softness?
  - » Prices are up 1.8 % from May last year but still some 3% below the ATH in January 2017
- OBOS' monthly data are more volatile than Real Estate Norway. RE's Oslo prices (all houses, not just apartments) have been somewhat more sluggish than OBOS the past year and reported a 0.2% m/m increase in May

Households' savings increased in Q1, bottomed out for now?

The cash flow is tilting upwards but the level is not that impressive; upside risk (downside vs. econ)

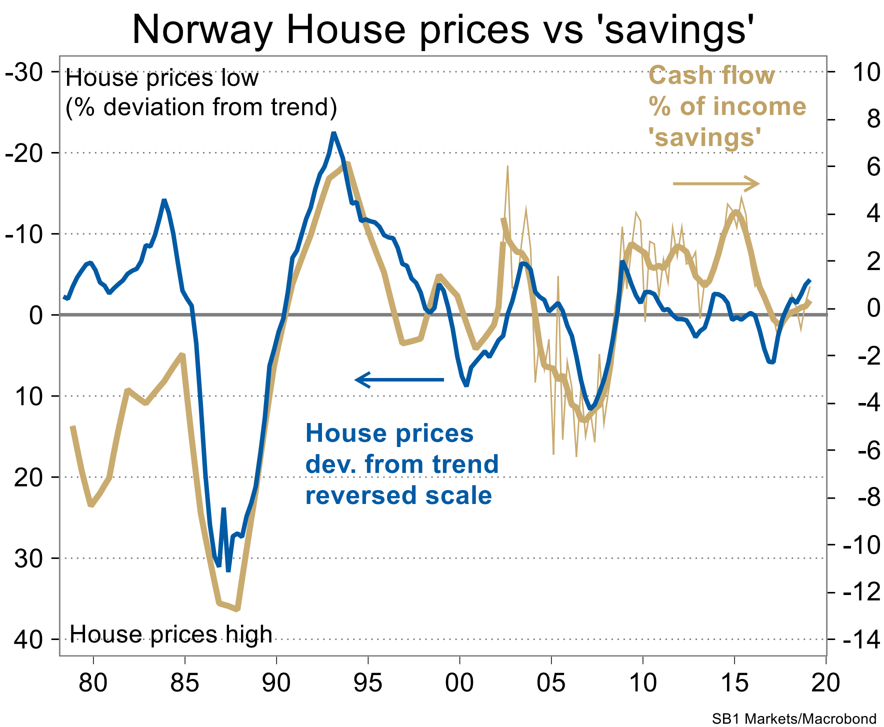




- The savings rate rose 0.4 pp to 6.8% of disposable income in Q1 (trend in dividends adjusted, total up to 7.0%). Savings were sliding down since 2015, but have turned up the two past quarters. Consumption rose 0.8% q/q in value terms in Q1, while disposable income adjusted for savings in pensions fund rose 1.4% (4.4% y/y)
  - » The savings rate has fallen 3 pp from 2015. Consumption is up almost 6% in the same period. Hence, the cut in savings have funded some 1/2 of cons. growth since 2015
- After deducting for still high housing investments, net financial investments are just marginally positive – and well into red if net pension savings (which are not visible or at least not available for households) are deducted too
- Financial accounts reported a negative cash flow (incl. pensions) at -0.7% of disp. income in Q1, up from -1.4% in Q4 (revised up from -2.5%), lower than National Accounts at +0.1%. The gap between the Financial Accounts and National accounts has been wide since 2010, as SSB has not been able to 'find' the households' money in banks, funds etc which the National accounts report they have saved. Now, the gap between the reports is closing

House prices and savings are usually correlated

Now, a soft housing market may signal increasing savings

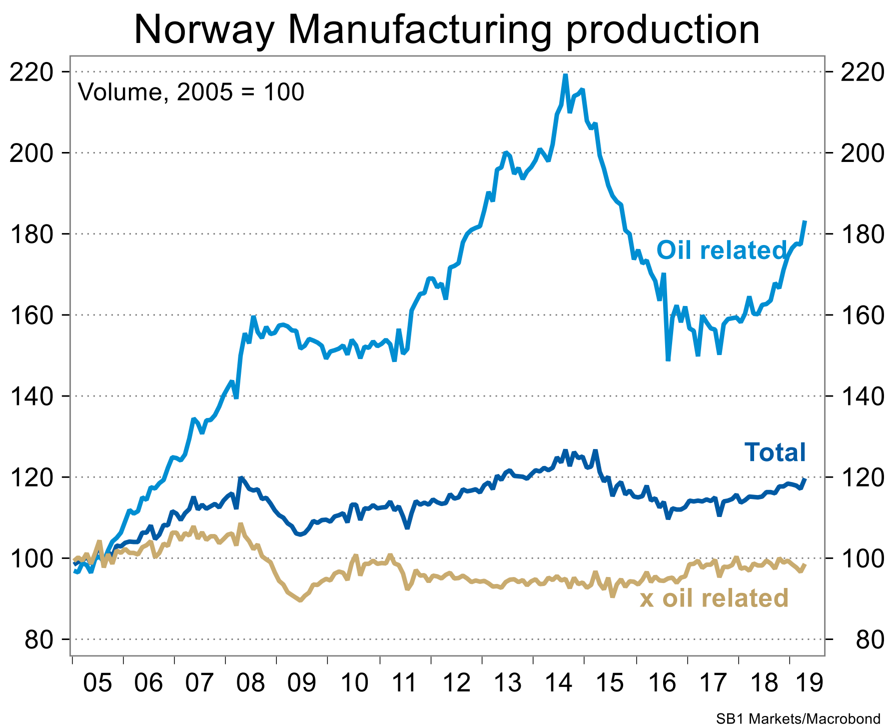


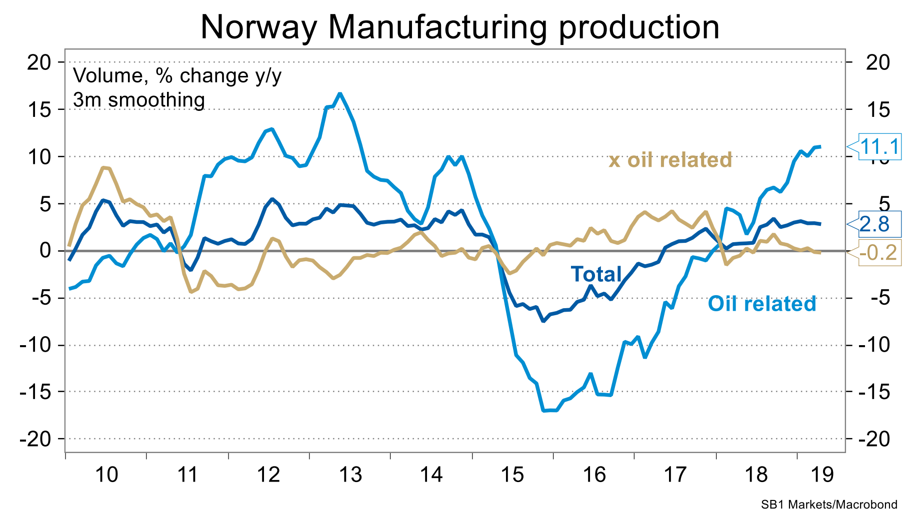
- House prices usually impacts
  - » The savings rate
    - You normally spend less and saves more when your net wealth falls – but that did not happen when house prices fell through 2017 (and the savings rate fell further)
  - » Housing investments
    - It is less profitable to build/buy a new home when house prices are low. Housing starts fall when house prices declines
- Now, house prices have more or less flattened out, some upside risk on savings? Consumption growth is low, even as savings have been falling, not a good sign

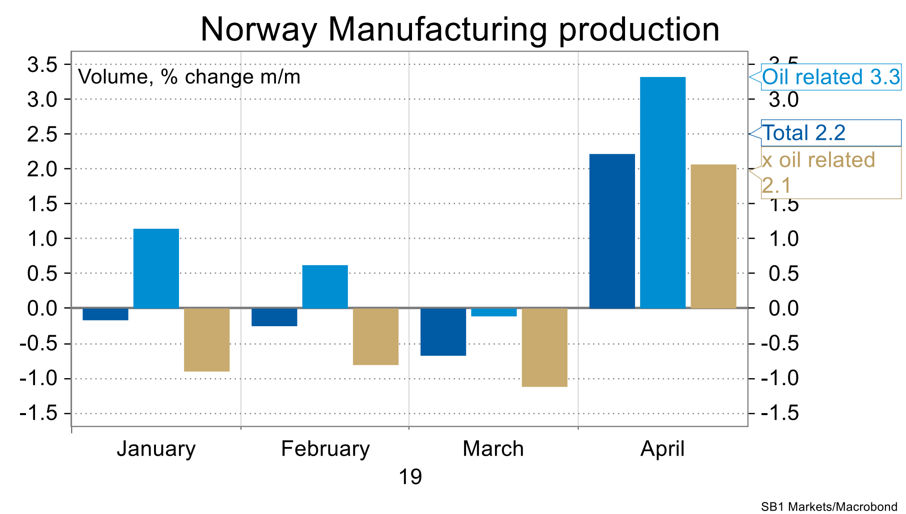
SpareBank 1 MARKETS

Manufacturing production surprisingly spiked in April

Production up 2.2%, strong growth in both oil- and non-oil related sectors. Oil related is soaring



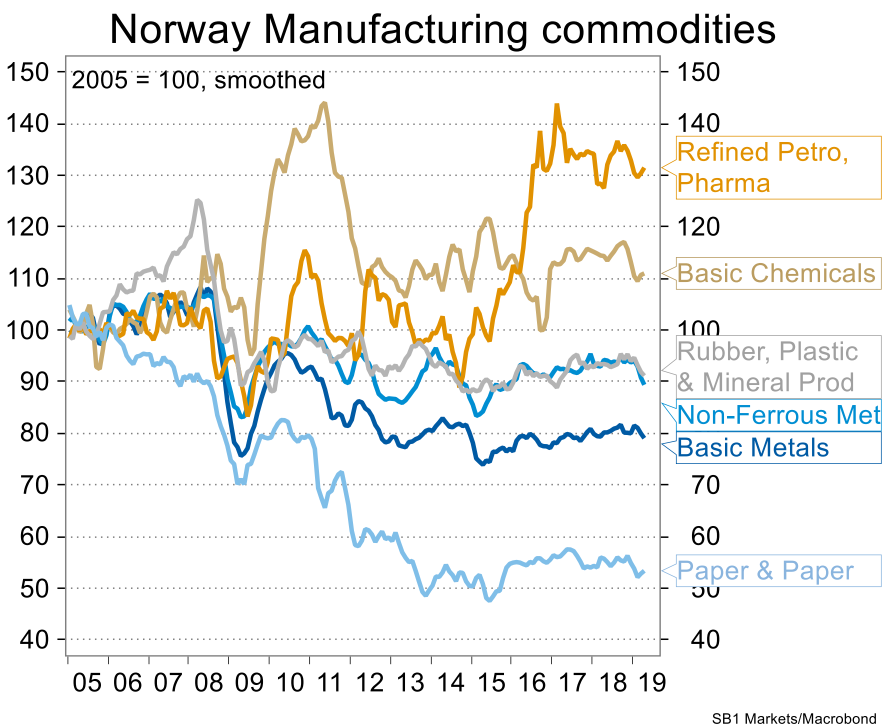


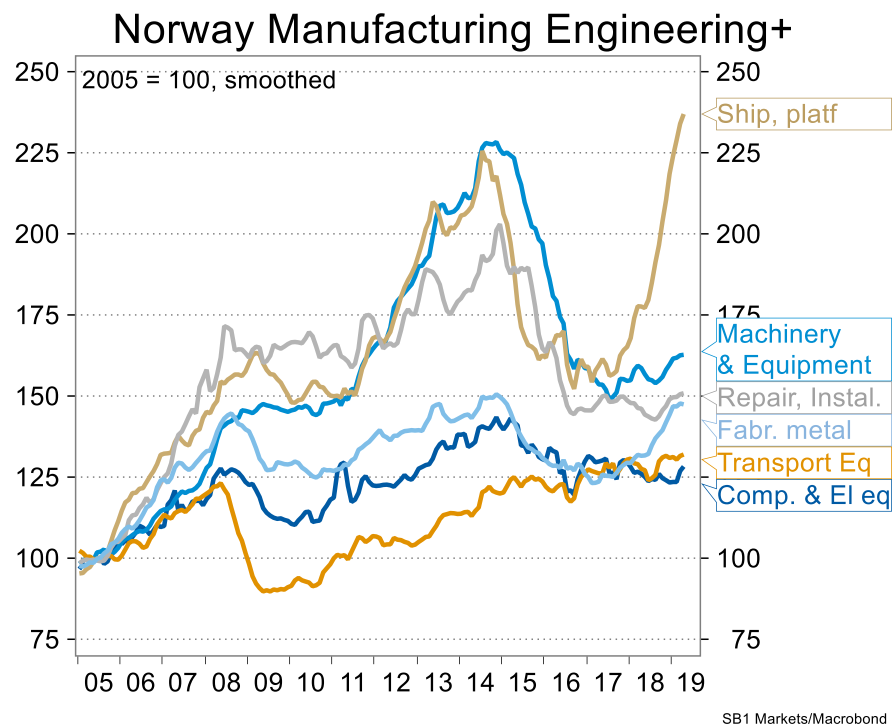


- Total manuf. production surged 2.2% in April, well above f'casts at 0.4%, following some soft months. Production is up 2.8% y/y (smoothed), a solid pace. Surveys indicate that growth may be peaking now
- Oil-related manufacturers reported a 3.3% jump m/m, the highest in 1 ½ years. Oil companies indicate that growth will continue to accelerate in 2019 and into 2020
- Non-oil related sectors noted a solid 2.1% lift, production has been completely flat the past 2 years

Production of ships & platforms is soaring, commodity sectors not impressive

Most commodities have lost steam the past 6 months, engineering sectors are thriving

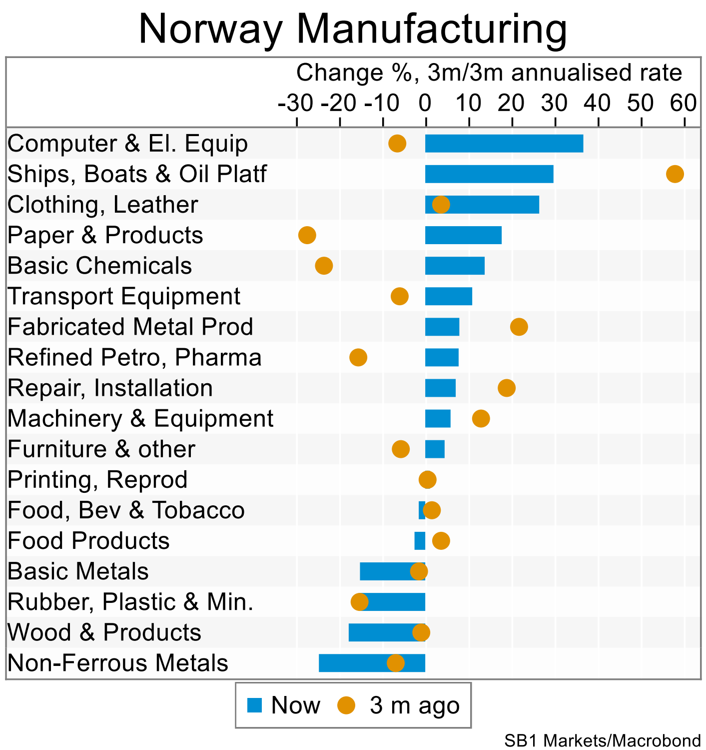


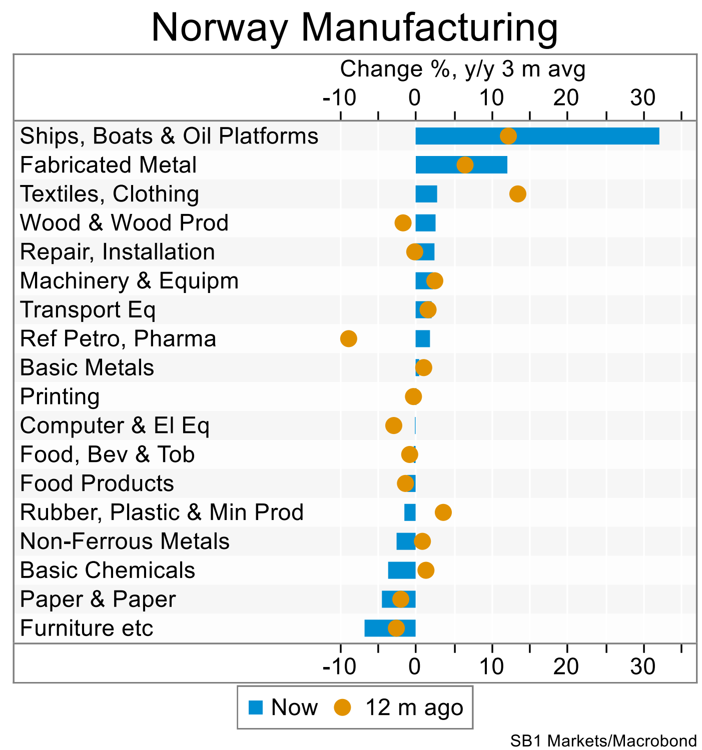


- Engineering sectors: ships & platforms are surging, followed by other partly oil-related sectors; both fabricated metals, machinery & equipment and repair & installation are accelerating. The only weak sector is computers etc,
- Commodities: All sectors ex basic metals have declined recently (although refined petro & pharmaceuticals and basic chemicals improved in April). Metal production may still be trending very slowly up

Ships & platforms production is boosting growth

Production is increasing in 11 and accelerating in most of them, just 4 declining considerably



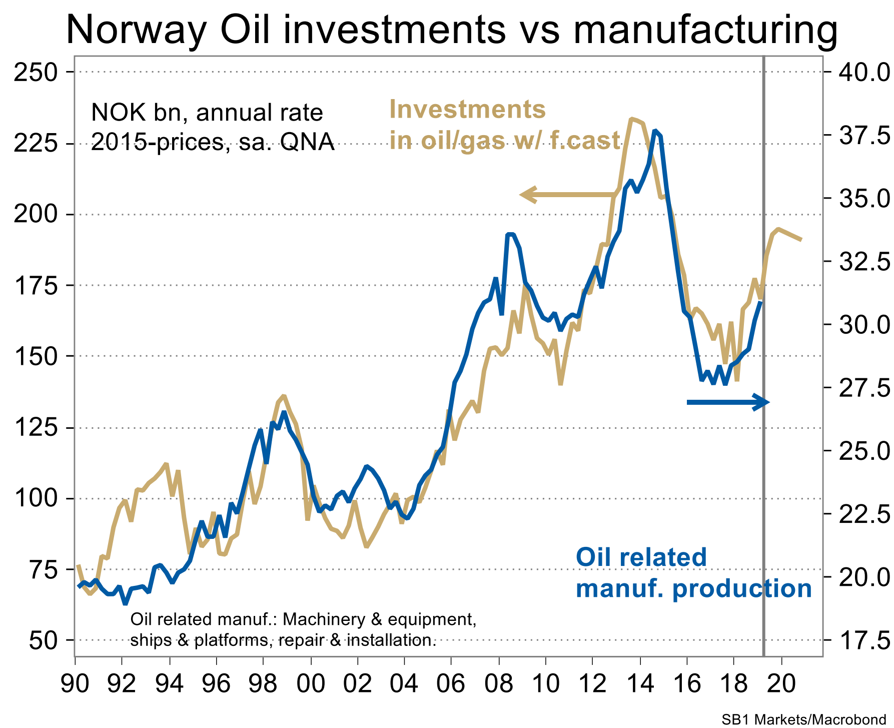


- Ships/platforms production is up 32% y/y (smoothed), an acceleration from 10% one year ago. However, underlying growth has slowed significantly (measured 3m/3m) the past months. Still more to go??
- Not that impressive in other oil related sectors; machinery +2.3% y/y, repair & installation up 2.5%
- Production of furniture, paper, basic chemicals and non-ferrous metals are declining y/y

SpareBank 1 MARKETS

How large is the upside in oil related industries? We assume some 5% in '19

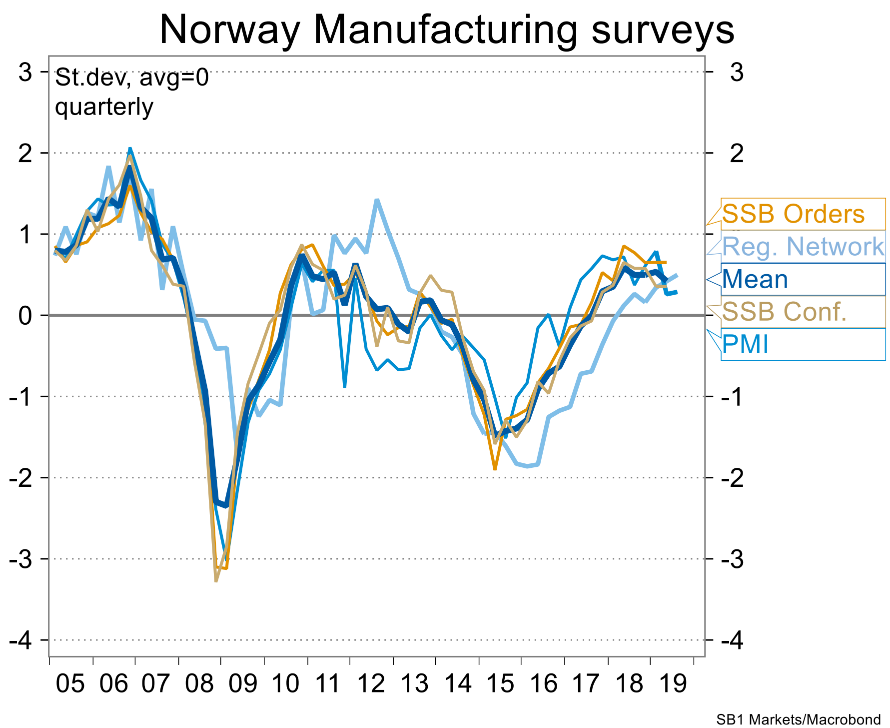
Oil companies have revised up their 2019 & 2020 investment plans, still some upside left

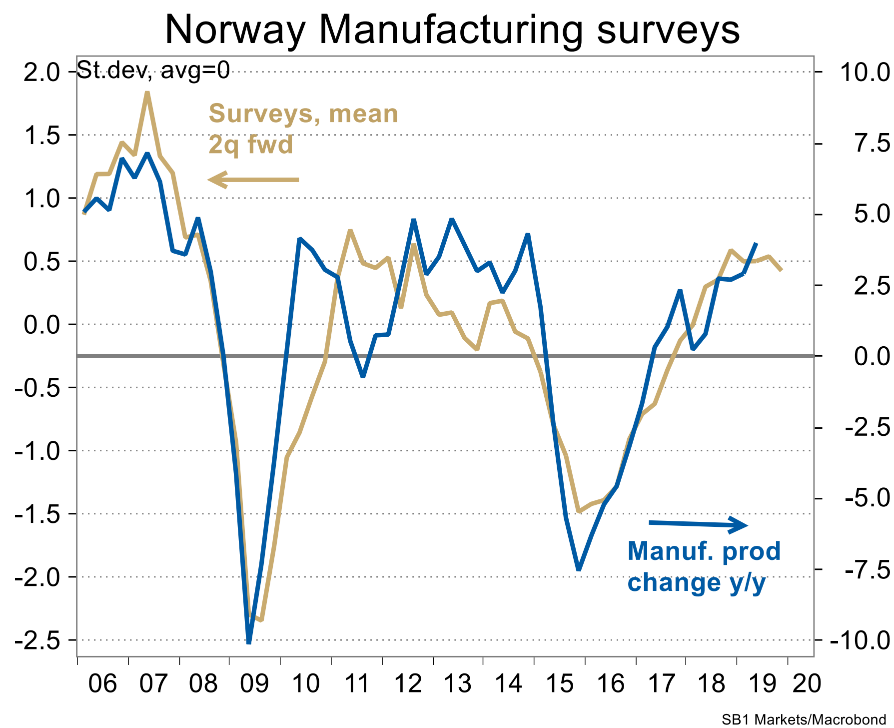


- Oil companies revised their 2019 & '20 forecasts up more than we expected in the Q2 oil & gas investment survey. Thus, the <u>upside</u> from the National Accounts Q1 investment level (which was – as we signalled – revised sharply down in the monthly statement Friday), <u>is substantially larger than we until now have assumed</u>. We assume the investment peak (later in 2019) is some 15% above the downward revised Q1 calculated level
- If so, there is some upside on oil related manufacturing production as well, we assume

Manufacturing surveys do not signal an overall acceleration

Both SSB's confidence survey, orders and the PMI have softened somewhat

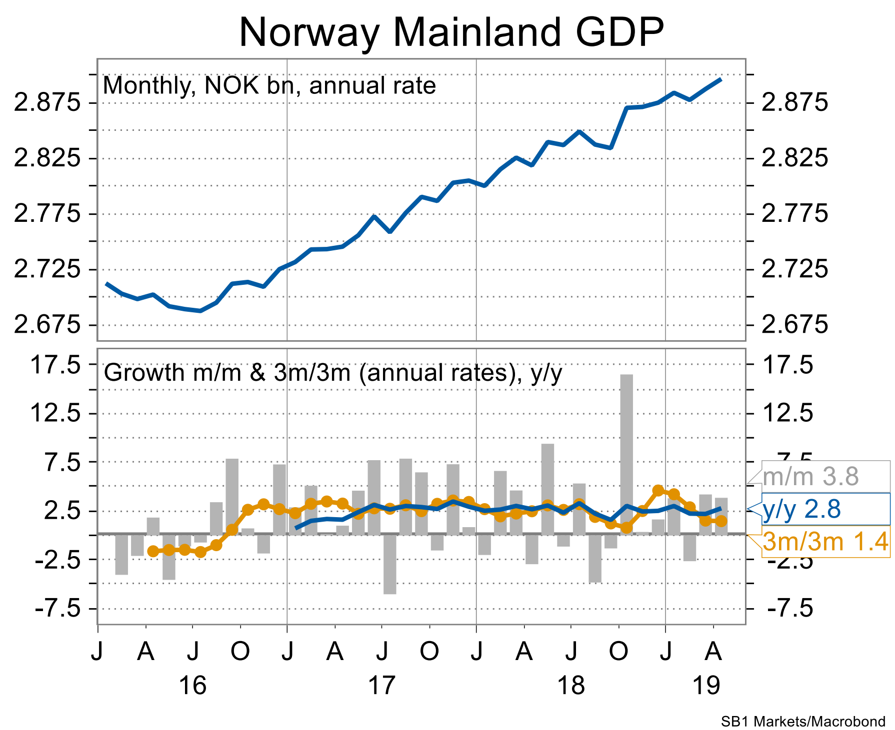




- The PMI is the weakest of the survey but all are above their respective averages, signalling solid growth
- Norges Bank's Q2 Regional Network is released at 08.00 today

Moderate GDP growth in April, the speed into Q2 is some 2%

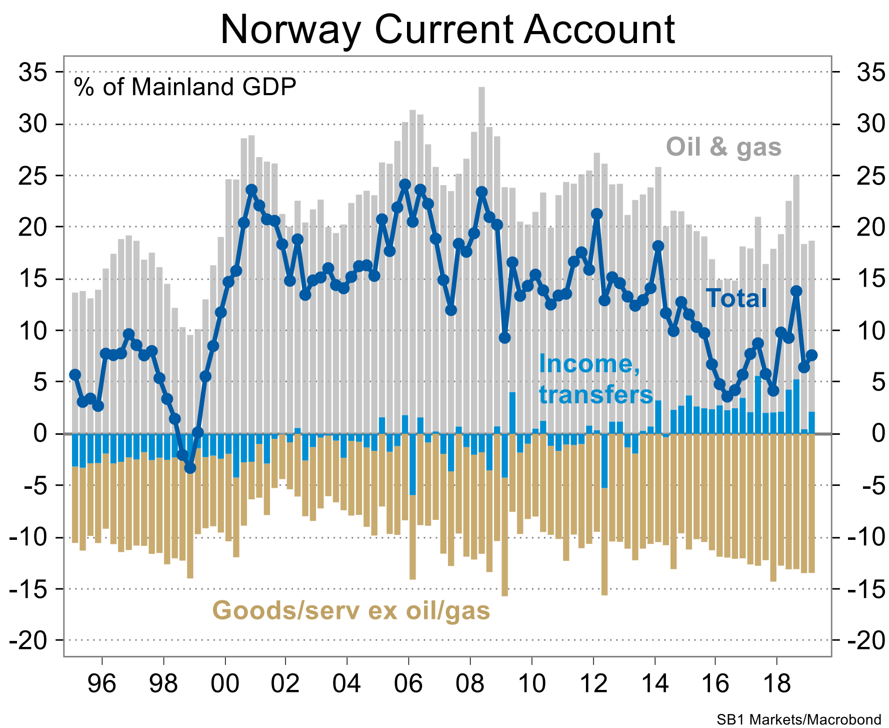
GDP rose 3.8% annualised in April, underlying growth is so far modest at 1.4%

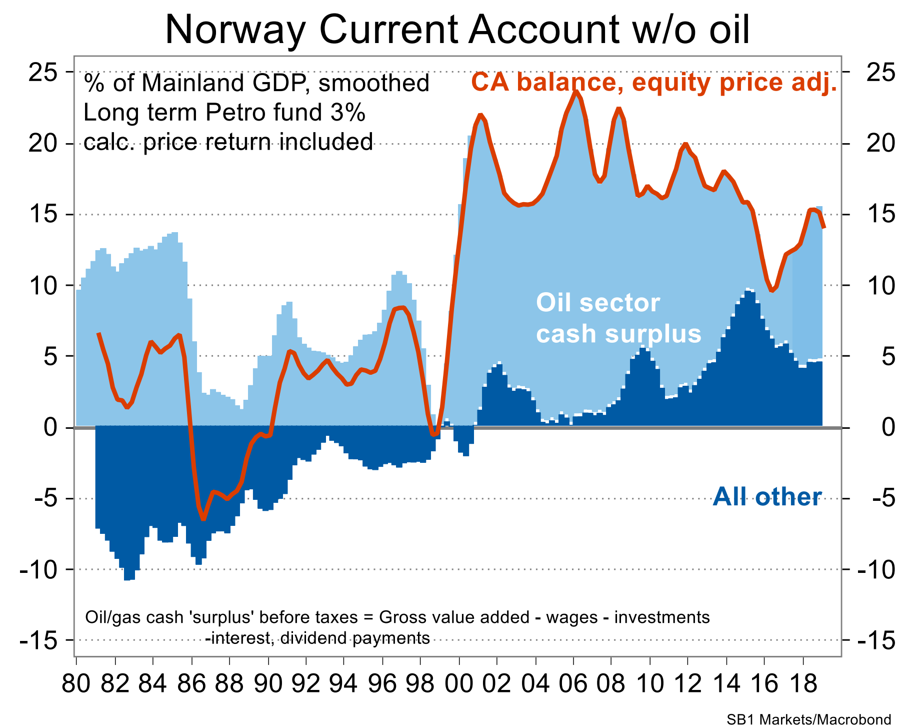


- Mainland GDP rose 0.3% m/m in April, 3.8% ann. rate
  - » The monthly data are too volatile to give us any useful signals, the more important 3m/3m rate came in at 1.4% annualised, dampened by a weak February
  - » The speed into Q2 is 1.9%, and that is if we assume zero growth in May and June. Most likely, growth will end up higher than this
  - » Norges Bank's March f'cast is a 3.1% annualized speed in Q2
  - » GDP is up 2.8% from April last year
- On the demand side:
  - » Private consumption has gained some speed the past 2 months and is running at a 3% growth rate. The uplift is partly due to a spike in auto sales in March (Teslas) but spending kept up in April
  - » Mainland business investments accelerated in April, after slowing in the first months of 2019
  - » Thus, total private Mainland demand is improving somewhat
  - » Oil investments were revised sharply down in Q1 (as we assumed) but April was much stronger than we expected. Q2 will most likely be very strong!
  - » Housing investments are growing at a modest pace
  - » Mainland net trade is pulling growth down, due to soaring imports
- So what?
  - » Norges Bank's Q2 GDP f'cast at 0.8% q/q is still within reach (if electricity prices normalises), and the Bank anyway does not put much weight on these monthly data. A June hike is a done deal and we expect an upward revision of the interest rate path, primarily in 2020, even if rates are sharply down abroad

Current account surplus inched up in Q1, on higher capital income

Oil & gas exports stabilised in Q1, the balance of income/transfers back up to a 'normal' level





- The trade balance ex oil & gas has gradually weakened recent years (but it almost at the same level vs Mainland GDP as in 1998!). In Q1, the trade balance was marginally lower than in Q4. Oil & gas exports decreased rapidly in Q4, when the oil price fell, and stabilised in Q1
- The balance of income/transfers has been trending up mostly due to higher capital income from the Oil fund. The income surplus came back up in Q1 after a setback in Q4
- We have tried to illustrate the non-oil balance: The oil sector is running a large cash surplus, more than 10% of GDP, almost equalling the overall surplus at the current account. However, capital gains in the oil fund are not included in the current account, just the income (interest, dividends). If we add a 3% price appreciation on equities long term, Norway is running a 5%+ of GDP surplus at the current account, before any revenues from the oil sector (but included deliveries – exports – from the Mainland to the oil and gas sector)

Highlights

The world around us

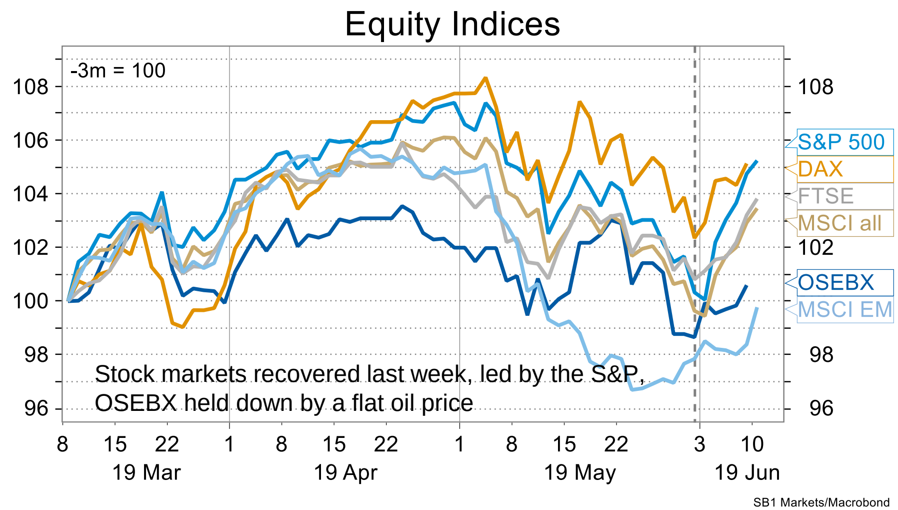
The Norwegian economy

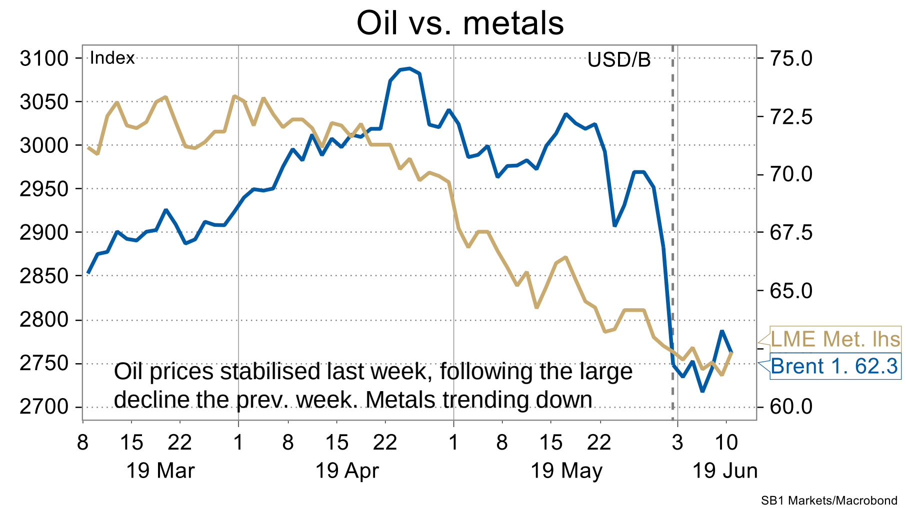
Market charts & comments

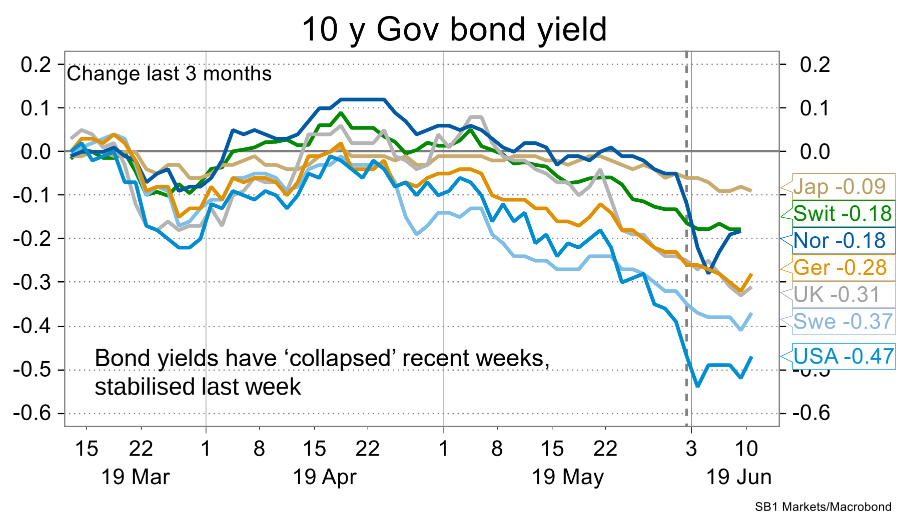
SpareBank 1 MARKETS

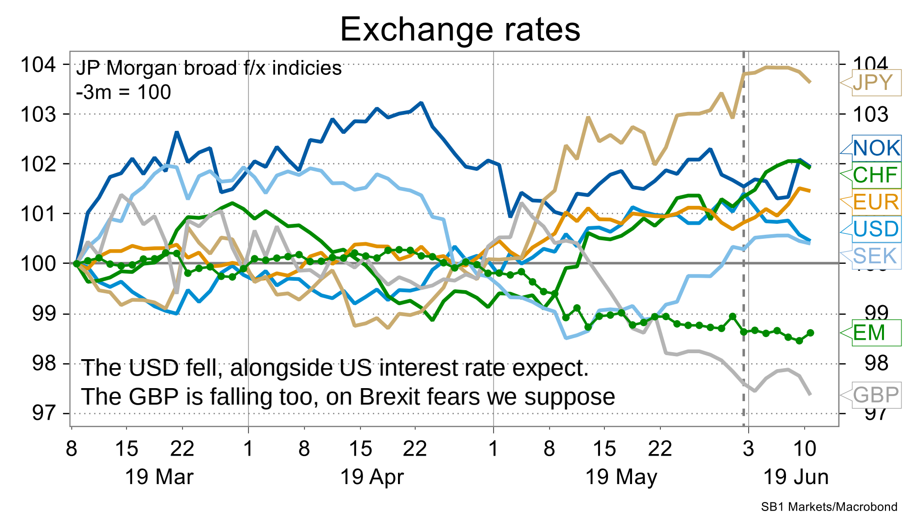
Risk markets shrugged off trade/growth fears, helped by Fed/ECB, US/Mex deal

Stock markets rebounded last week, bond yields finally stabilised







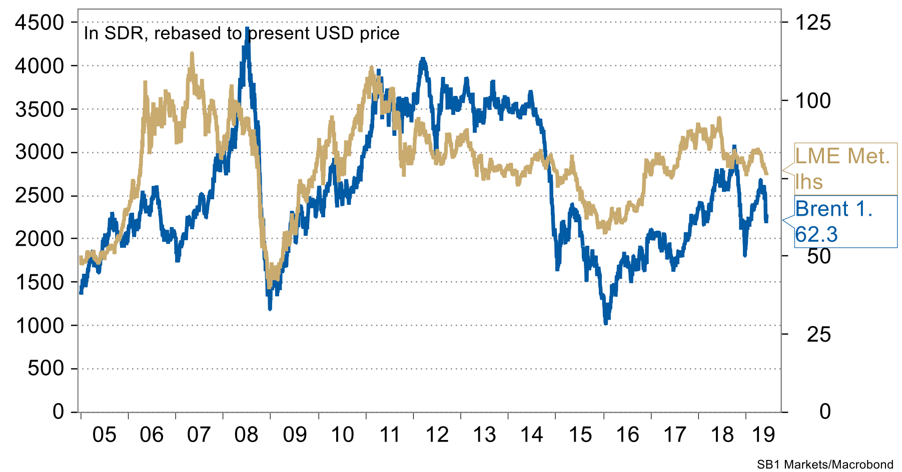


The trade war may trigger a stock market crash. Or the economy..

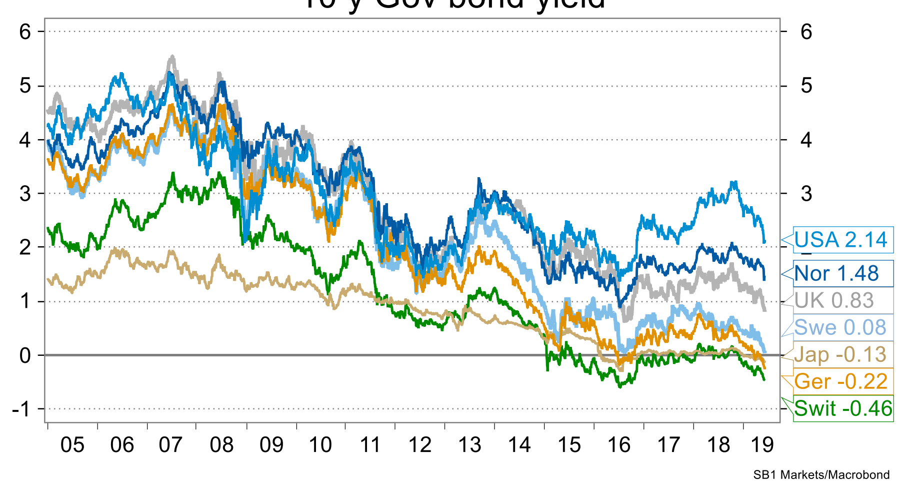
Economic data are now extremely important, risk markets are vulnerable. The trade war is key

Equity Indices

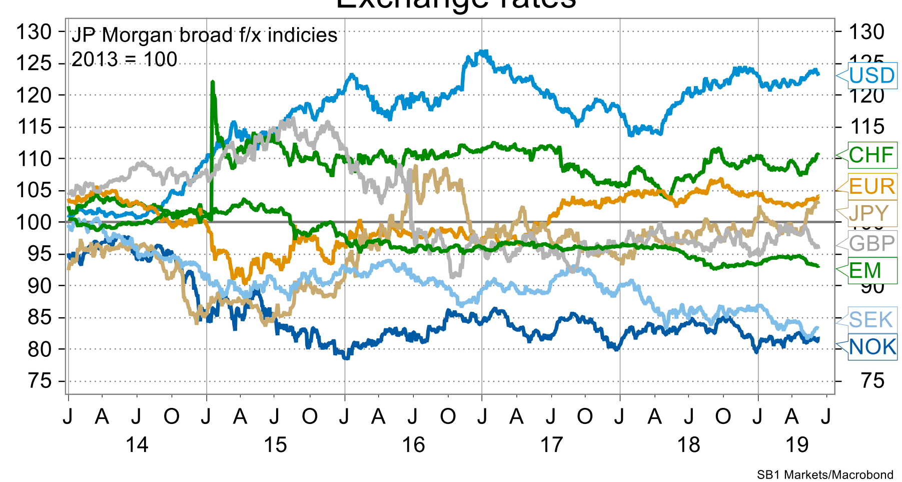
Oil vs. metals



10 y Gov bond yield



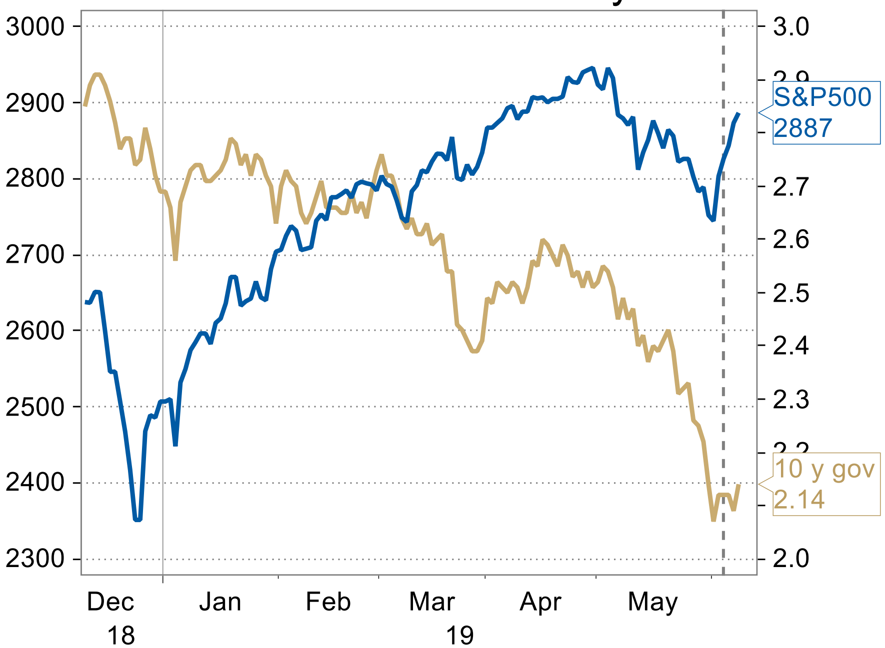
Exchange rates



Fed's Powell sparked a stock market rebound, bond yields rose modestly too

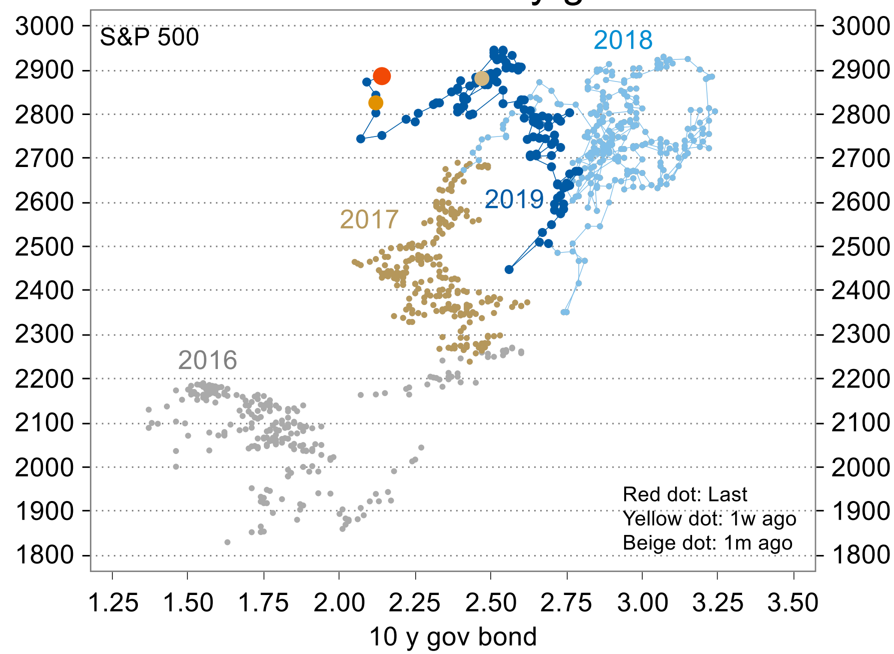
Ironically, Powell opening the door for cutting rates sent yields slightly up as growth fears eased

USA S&P 500 vs. bond yields



SB1 Markets/Macrobond

S&P 500 vs US 10 y gov bond

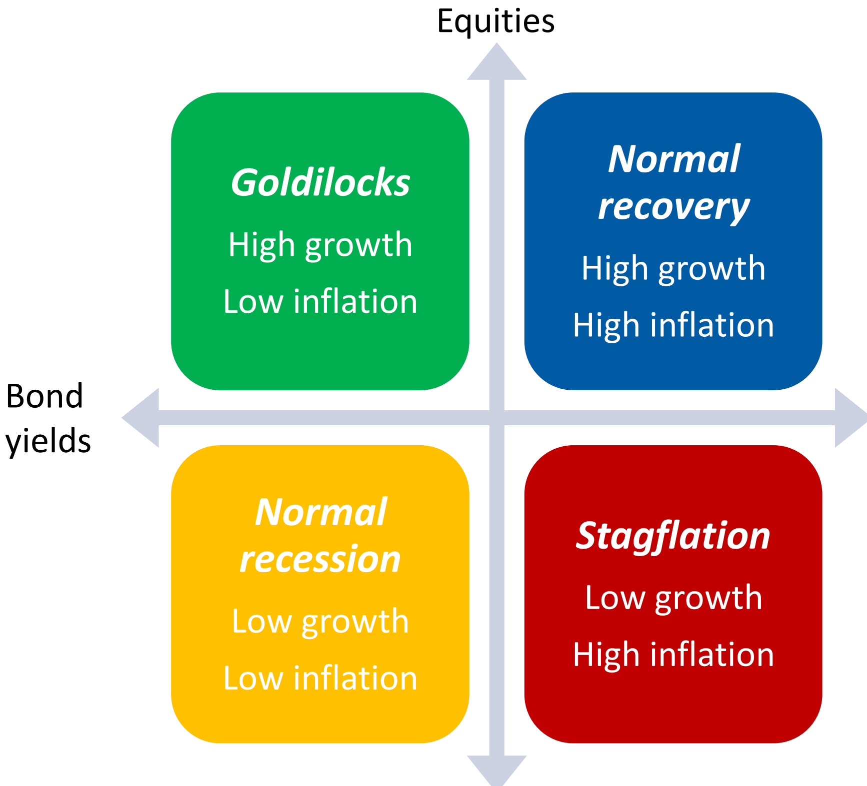


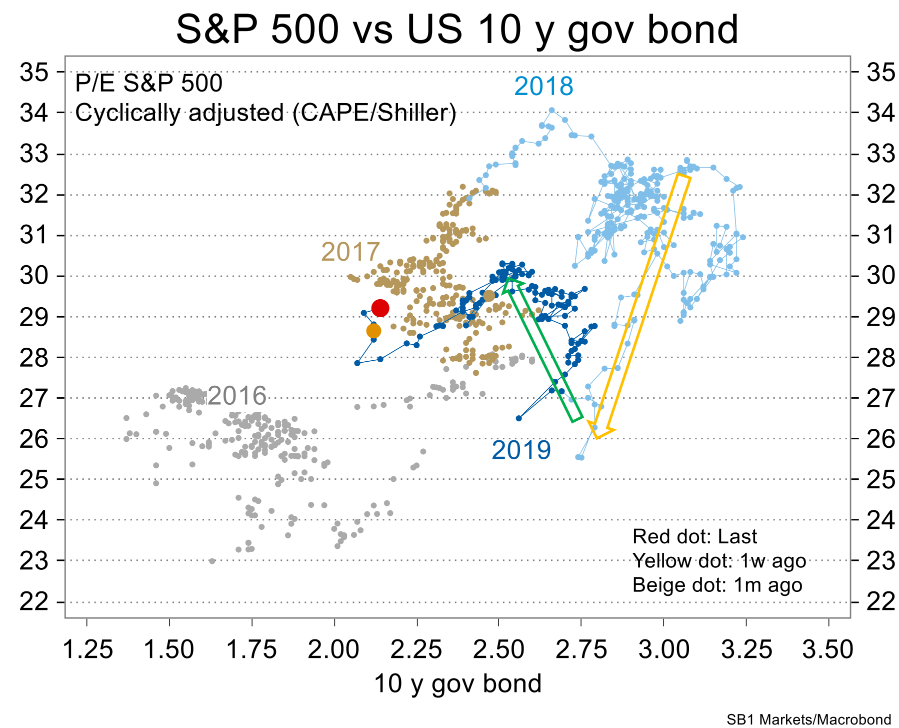
SB1 Markets/Macrobond

- S&P has recovered some 4.9% since last Friday, after sliding down close to 6% in May – and is not far below ATH. The upswing came after Fed's Powell said in a speech on Tuesday that the Fed would respond 'as appropriate' to the risks posed by the trade war and global uncertainties. Powell's signals that the Fed was opening the door for an interest rate cut comforted markets and sent S&P up 2.1% on the day. In addition, US will not impose tariffs on Mexican imports as a deal was reached
- The stock market upturn send bond yields up 5 bps on the same day. The fact that bond yields edged up as the Fed signalled a possible interest cut reflects how far ahead of the Fed the market pricing has gone. Yields came back down 4 bps after the soft nonfarm payrolls report – and rose yesterday as the US and Mexico reached a deal
- For more on the relation between stocks and bonds, check next page

Markets are moving rapidly towards the normal recession corner

Last week: North, stocks markets rebounding, yields rose just slightly (in the end)

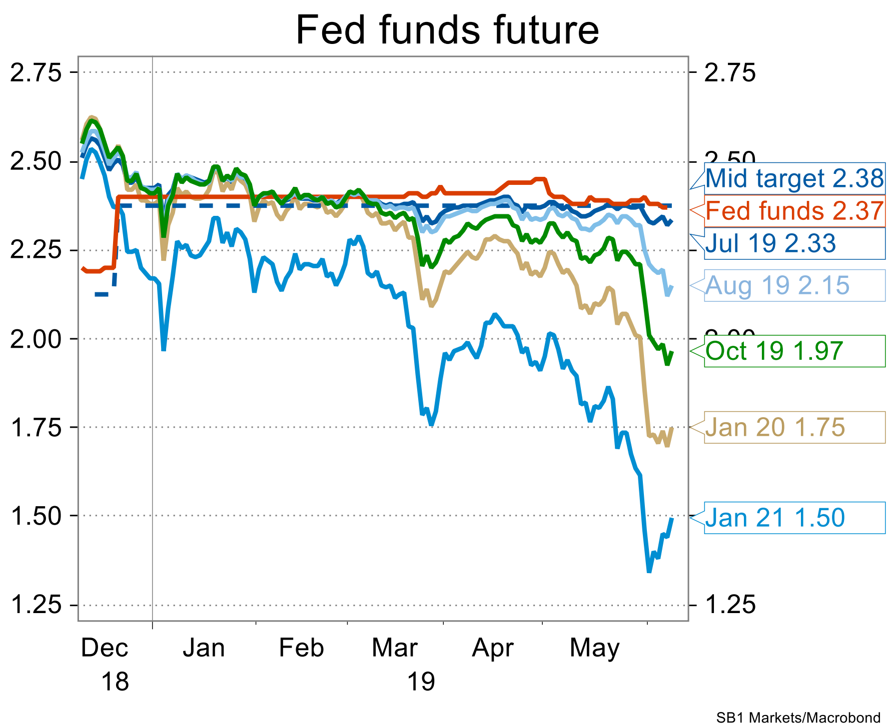


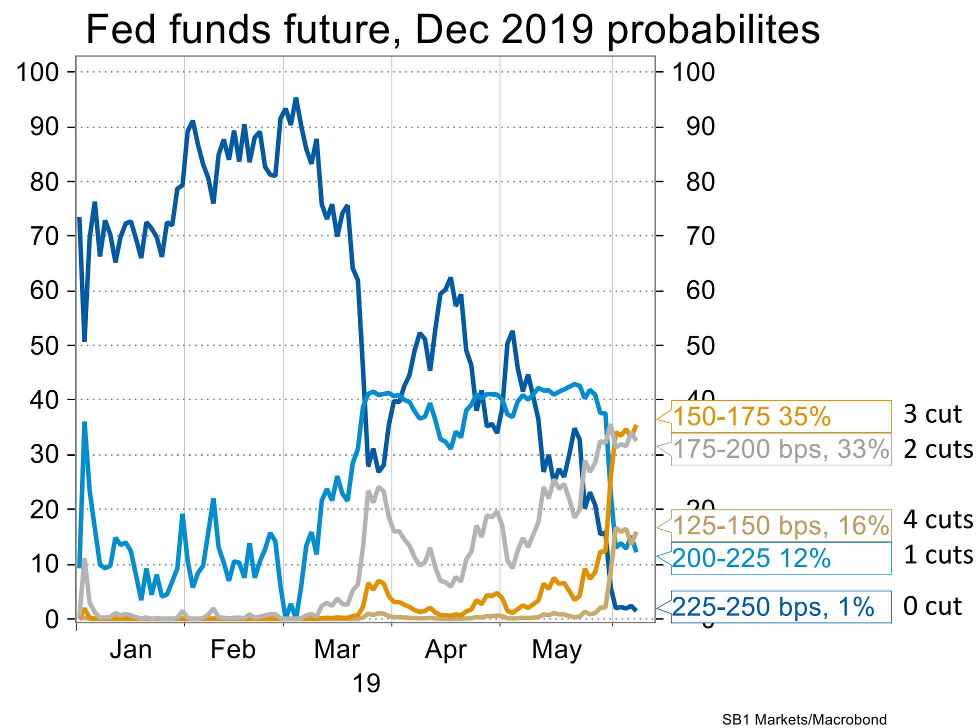


- Until last week both stocks and bond yields fell sharply, towards the 'normal recession' corner
- Before the trade war escalated and sent risk markets down, markets were on the march to the 'Goldilocks' scenario, check the green arrow
- We are not that worried for 'Stagflation', a take off in inflation will happen only if central banks make serious policy mistakes, over time. Trump want the Fed to do just that but we doubt he will succeed
- We stick to our 'normal' axis, driven by growth, and with inflation (or at least interest rates) over time following growth up or down. The risks of a slide in the recession direction has increased significantly past weeks, primarily due to trade war escalation

Fed funds futures are pricing at more than 50% prob. of at least 3 cuts this year

... and the first in July. Just 1% for no '19 cut. Still, just the very short end of the curve down last w.



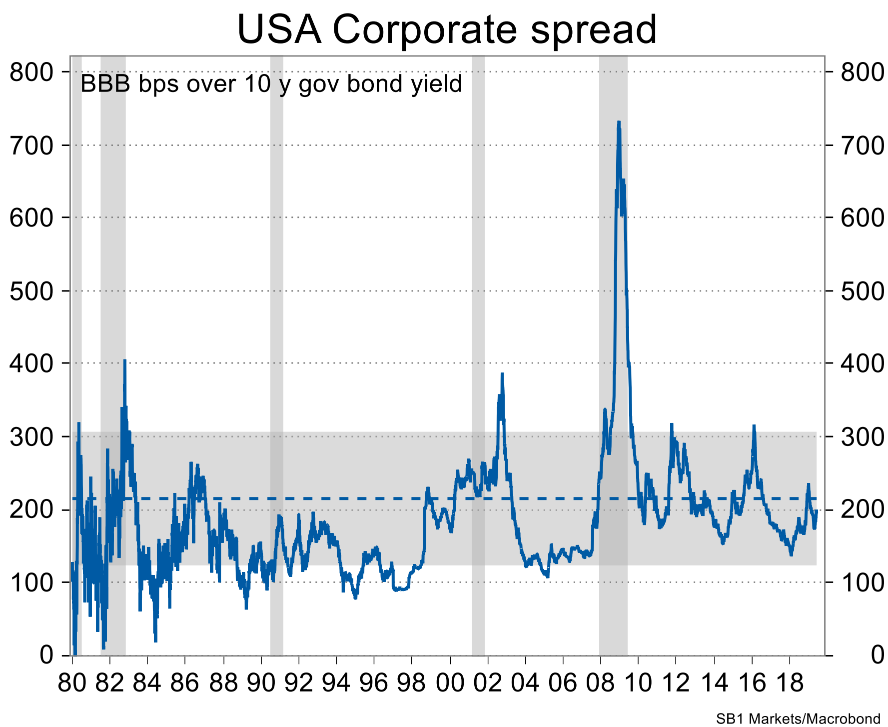


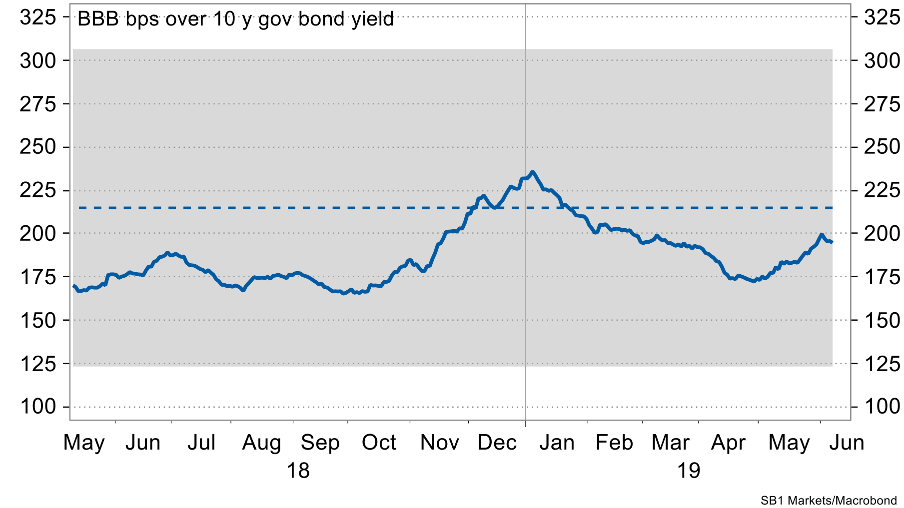
- Soft signals from Powell & co lowered the curve further. No cut is expected at the June meeting but a July cut is a 'done deal'. Further out on the FRA curve, rate expectations rose, yesterday also due to the US/Mexico deal on tariffs/immigration
  - The market now expects at least one cut in 2019 with a 99% probability; 12% for one cut, 33% for two cuts, and 35% for 3 cuts, and 16% for 4! (25 bps per cut)
  - The Aug FRA at 2.15 implies that the market is fully expecting a cut at the July meeting
- **At the June meeting, the Fed may well signal that it plans to cut the signal rate in H2 as a precautionary measure to fend off possible impacts from the trade war. However, even if employment growth has slowed, the economic situation down does not warrant any cut**

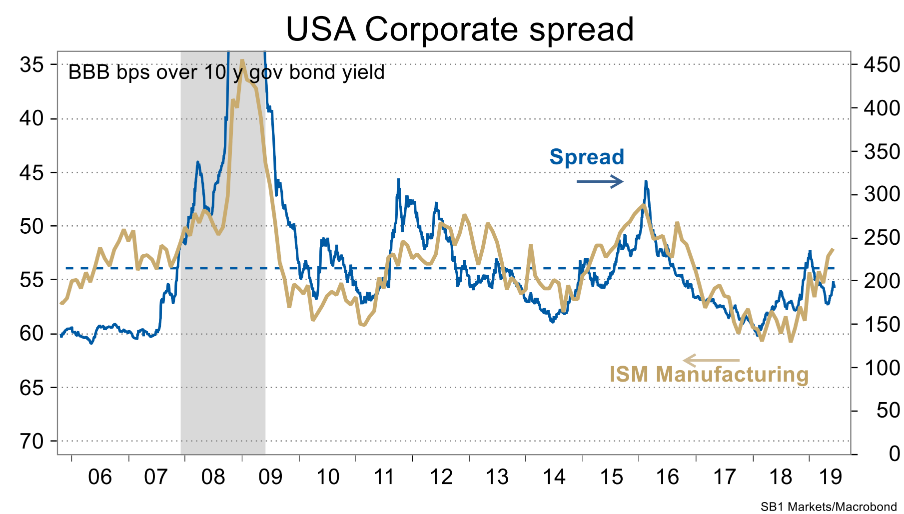
SpareBank 1 MARKETS

Credit spreads marginally lower last week

Spreads are too low if the ISM and (most) other surveys are correct; if growth is slowing

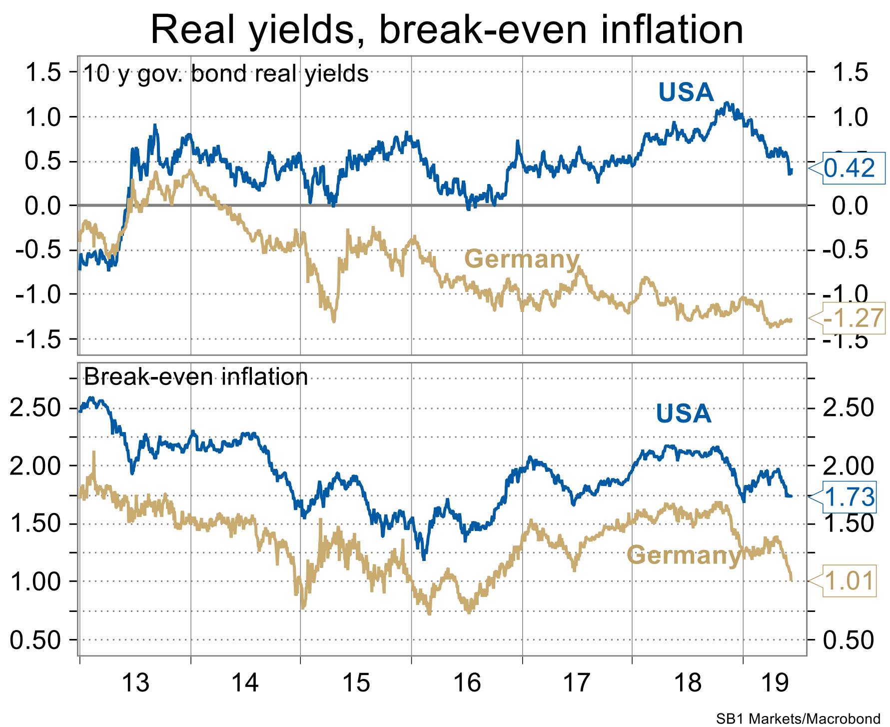


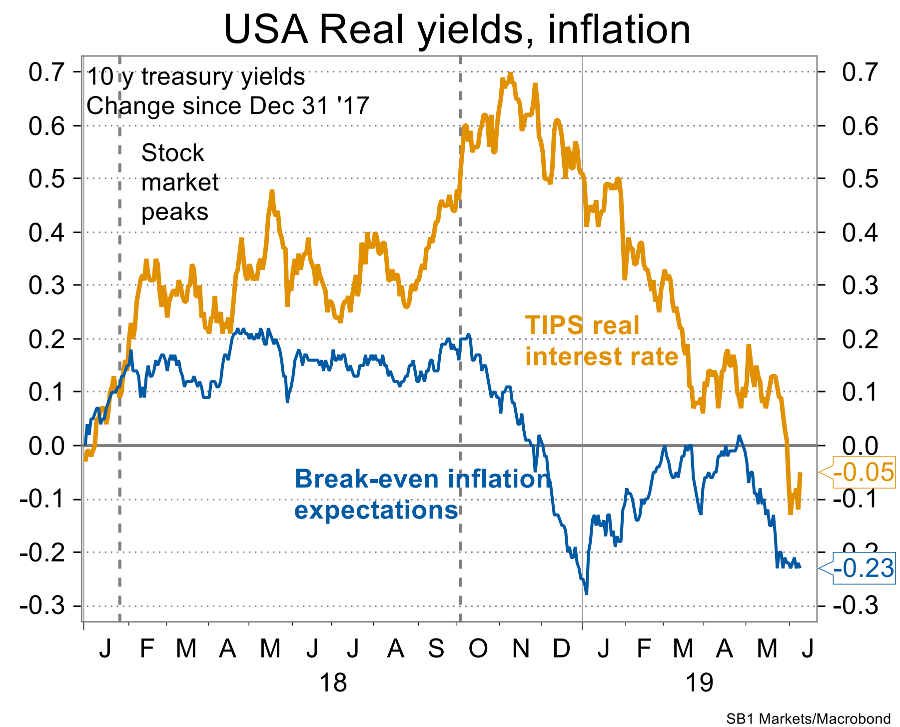




US real rates have 'collapsed', on trade tension and growth concerns

The decline took a break last week, markets were comforted. Inflation expectations stable past 2 w

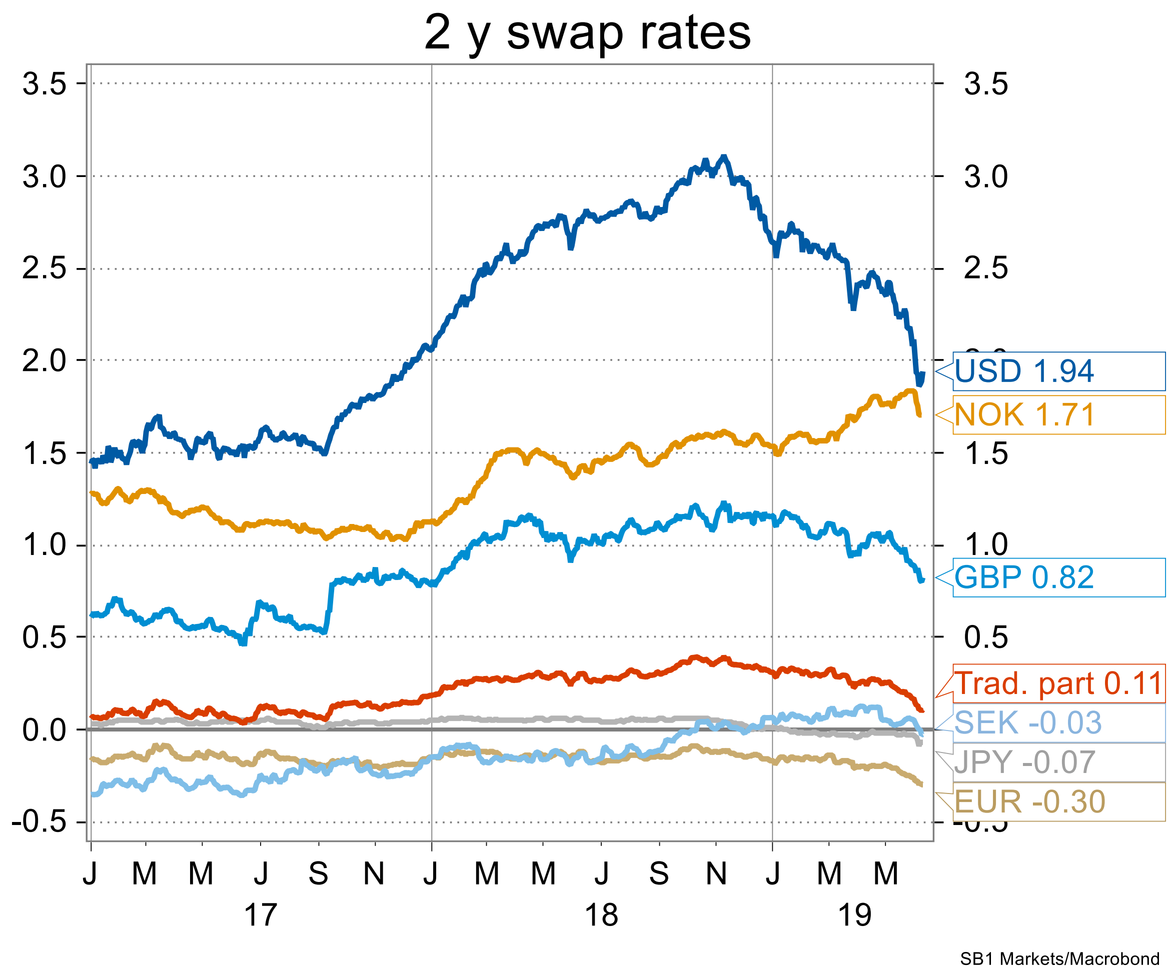


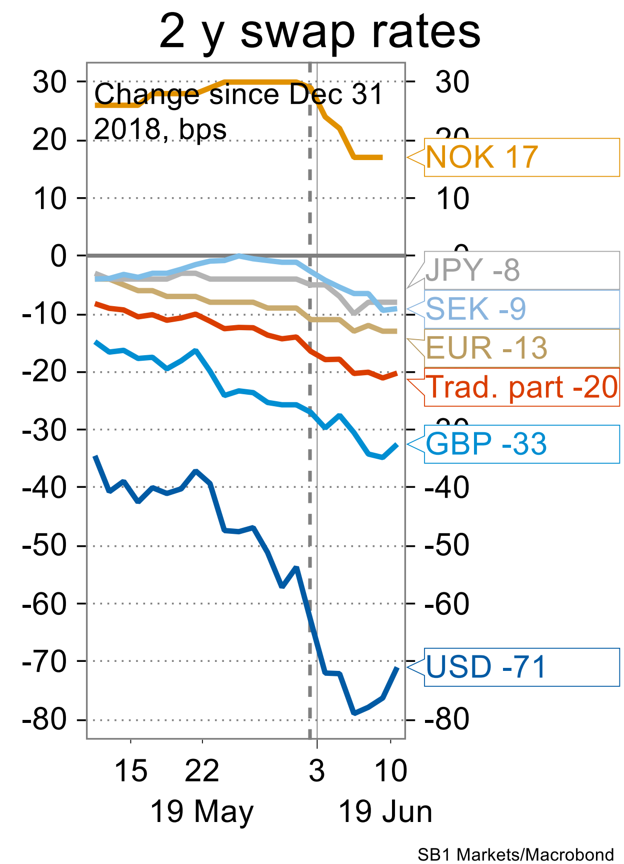


- The 10y US real rate came up last Tuesday, along with stock markets, after the Fed signalised that it will act in order to sustain the economic expansion if trade war headwinds hampered the economy. The stabilisation was reversed by Friday, when a soft labour market report frightened markets, before the Mexico-US deal sent real rates up yesterday
- Inflation expectations are stabilised the 2 past weeks. A CPI inflation expectation at 1.73% is well below the Fed's 2% PCE deflator target
- German real rates climbed last Friday, even with disturbingly weak German data, to -1.27%, per year, the next 10 years…
  10 y inflation expectations are falling steeply, to 1.01%, the lowest since 2016. The nominal bond yields dropped to -0.26% last week

Short term rates are plummeting all over, NOK rates (finally) yielded

NOK rates have followed others down in June, without any weak domestic data

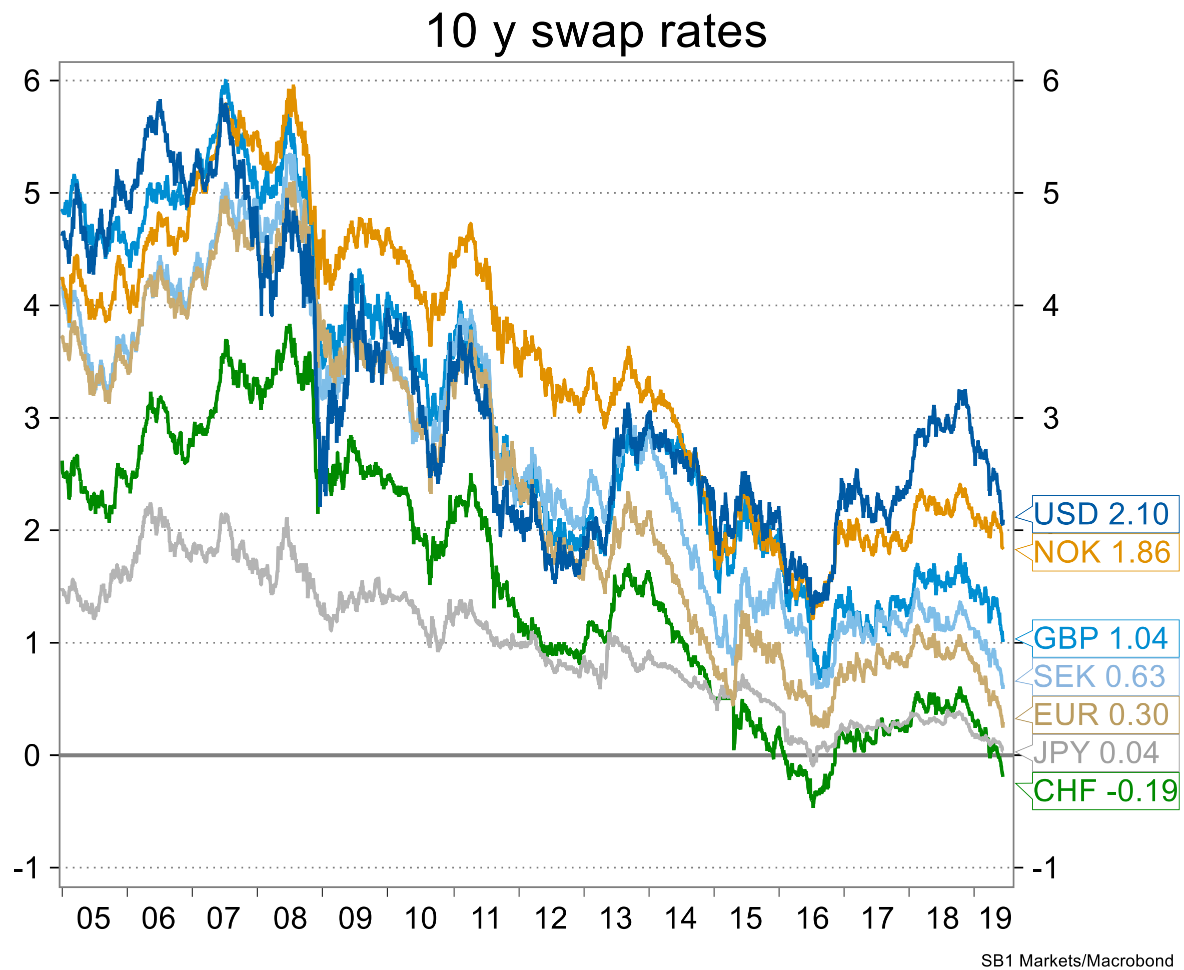


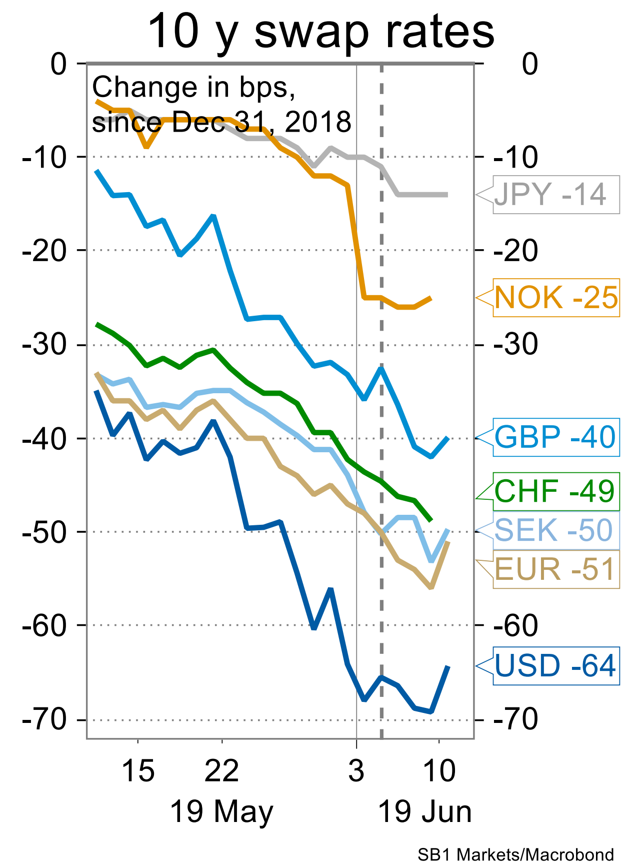


SpareBank 1 MARKETS

Long term rates are falling all over, triggered by the trade wars

The fixed rate in Japan is declining the least, with the Norwegian

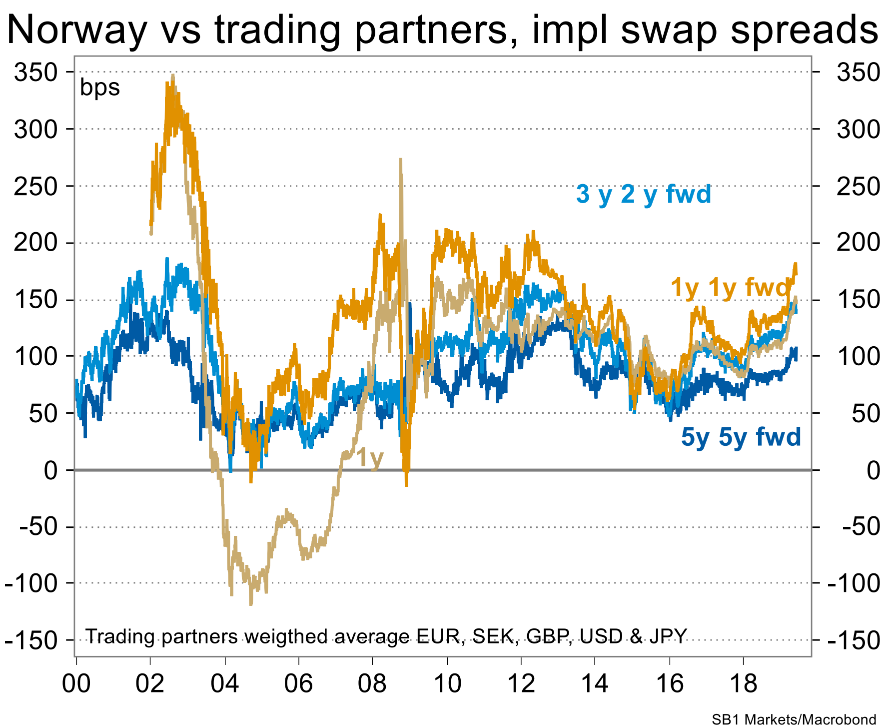


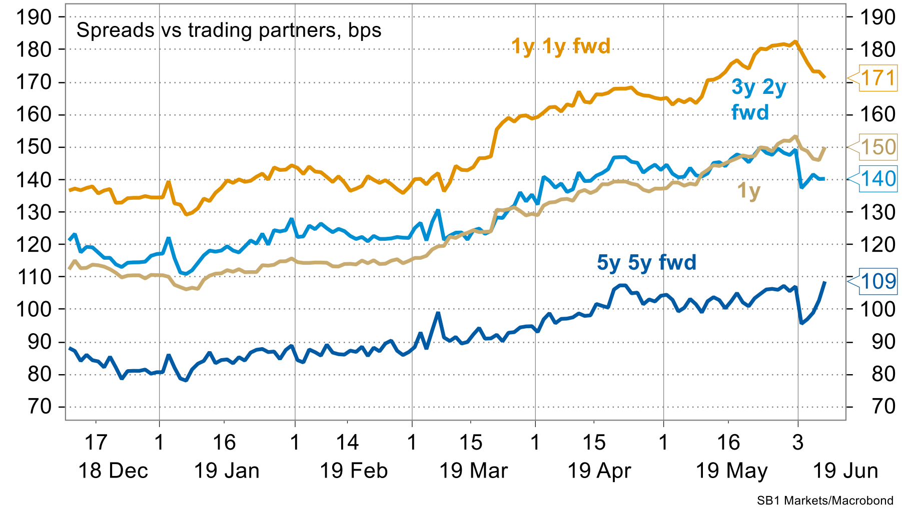


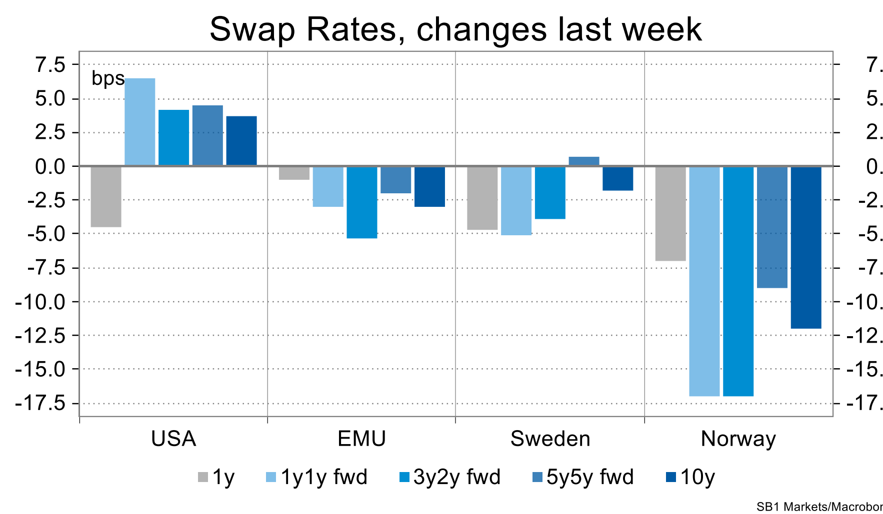
SpareBank 1 MARKETS

Swap spreads vs our trading partners came in, enough for now?

Swap rates are falling among all maturities, NOK (finally) yielded last week, helped by the oil price



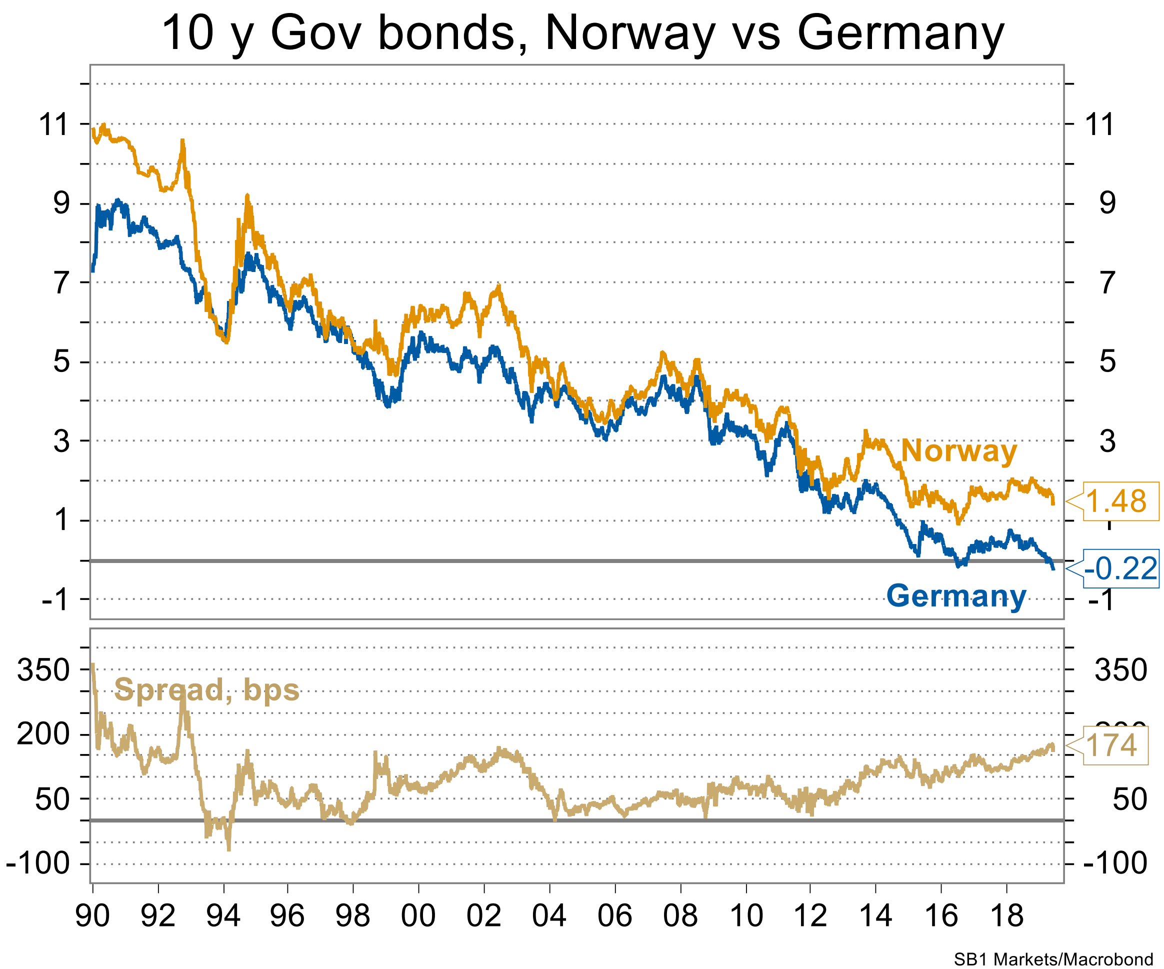


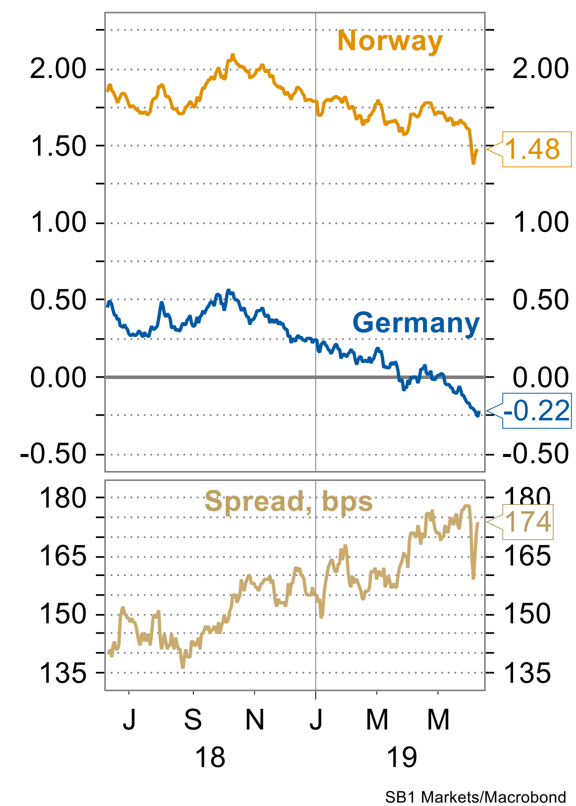


- NOK short term spreads vs trading partners finally yielded last week, after climbing substantially since March. A high spread is reasonable, given NoBa's stance and solid Norwegian data. However, the short term upside for the spreads is rather limited
- We have been more surprised by the wide spread in the long end of the curve recently – and the spread rose again last week (no Whit Monday data)

German Bund down to -0.26% at Friday, the lowest ever

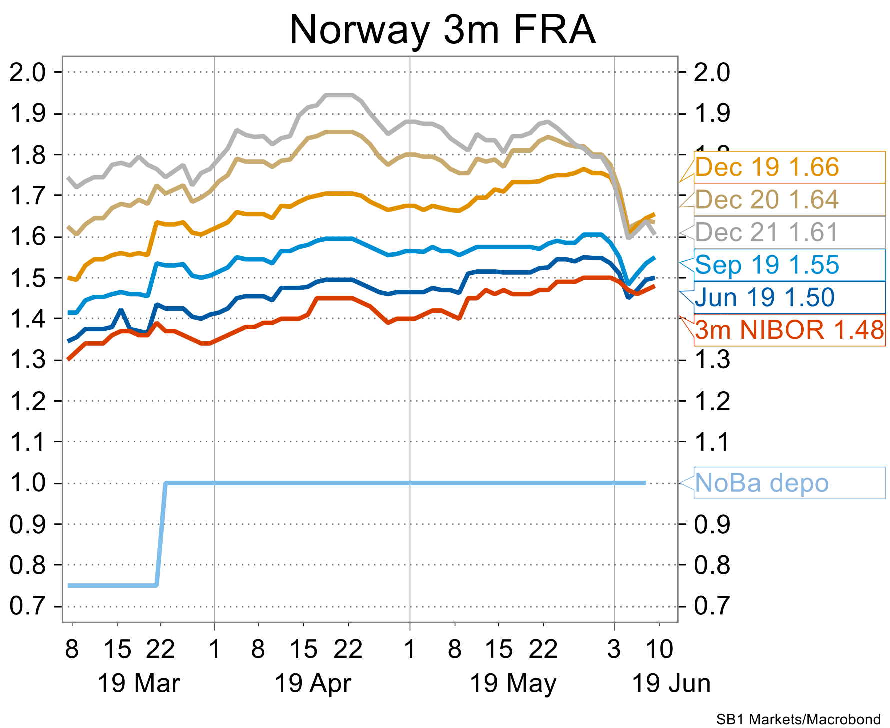
The 10 y gov spread came in to 174 bps, as Norwegian rates fell. The spread is far too rich long term

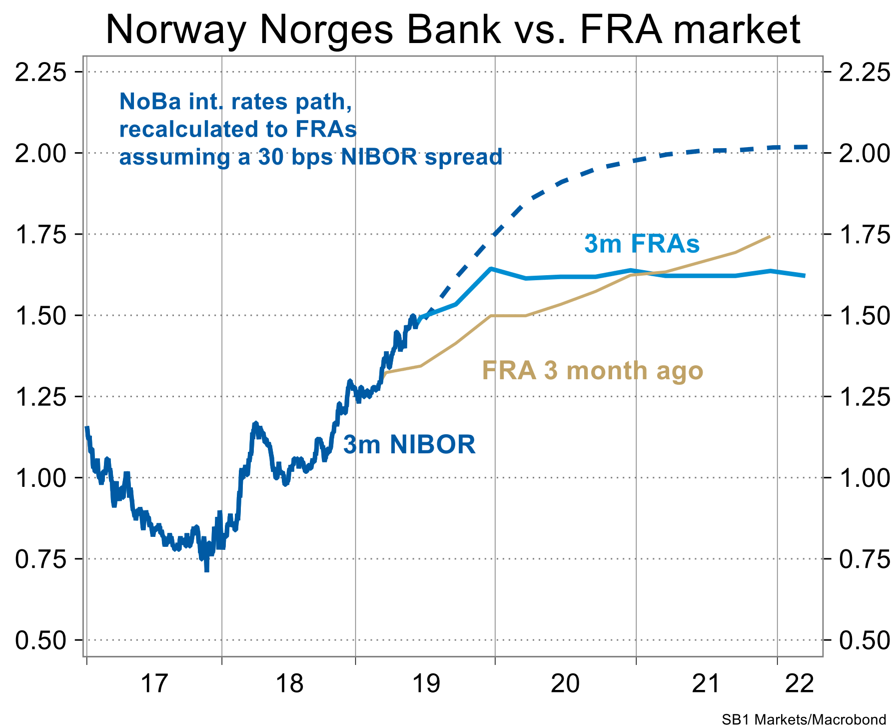




The FRA curve is tilting down; starting to doubt a second hike?

FRAs have fallen recently, still 80% probability of a June hike but a second in Dec is reduced to 45%



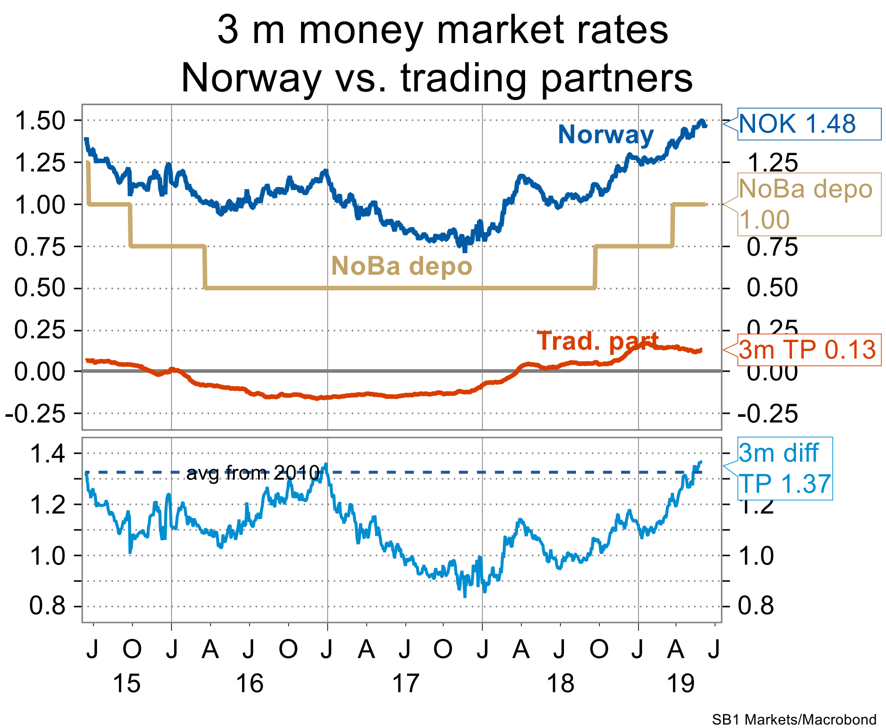


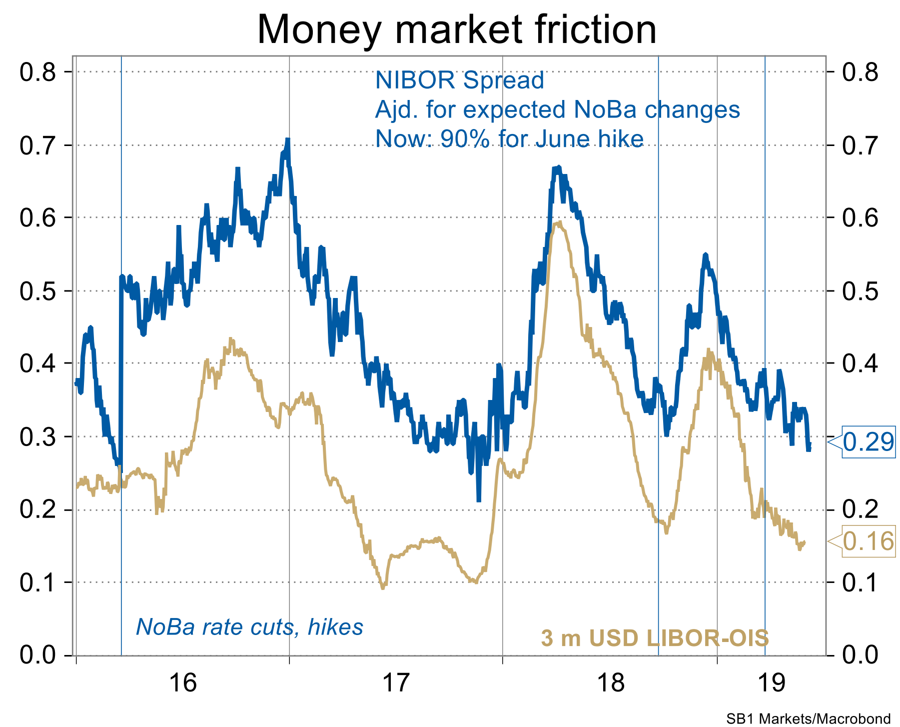
- The June 3m FRA lost fell 4 bps to 1.50 last week, after climbing the prior months as markets started to fully accept the June hike. We have revised our estimate of the NIBOR spread down to 30 bps, from 35 (and 40 before that). If we are right, a June hike is still expected by some 80% probability, down from 100% the prior week. (A fully priced hike: 1.25% + 30 bps = 1.55%). With a 35 bps spread, the probability is 60%
- The Dec 19 FRA contract has fallen 9 bps to 1.66% so far in June, thus, the probability of second hike in December is lowered substantially. We estimate some 45% probability, from 80% one week before. FRAs further out on the curve have lost more than 10 bps, of course influenced by the sharp decrease in rates abroad

SpareBank 1 MARKETS

LIBOR OIS spread flat. 3m NIBOR down 2 bps to 1.48%

The (unobservable) NIBOR (forward) spread has probably not widened recent weeks

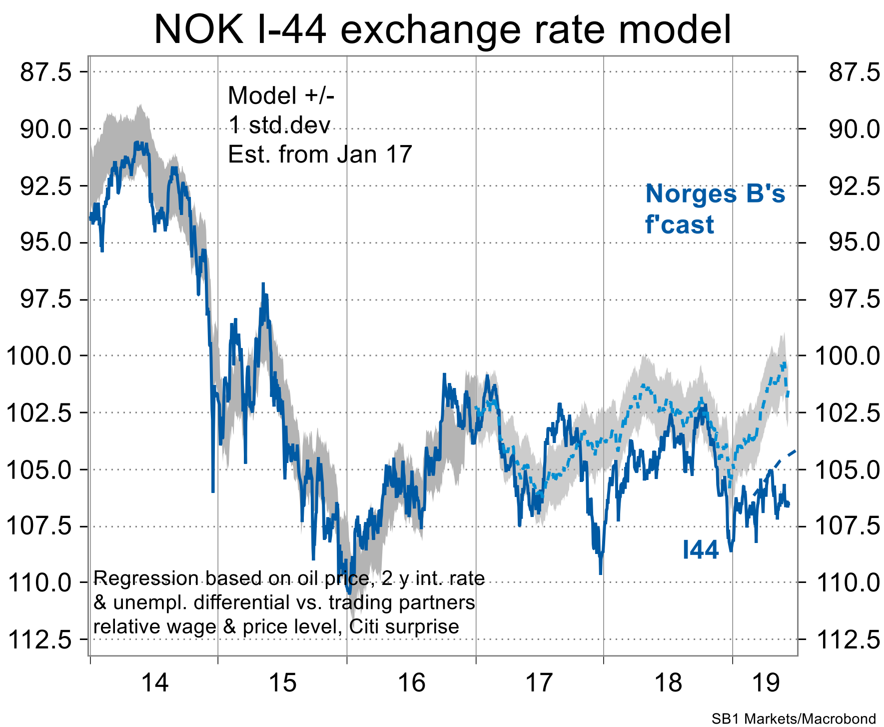


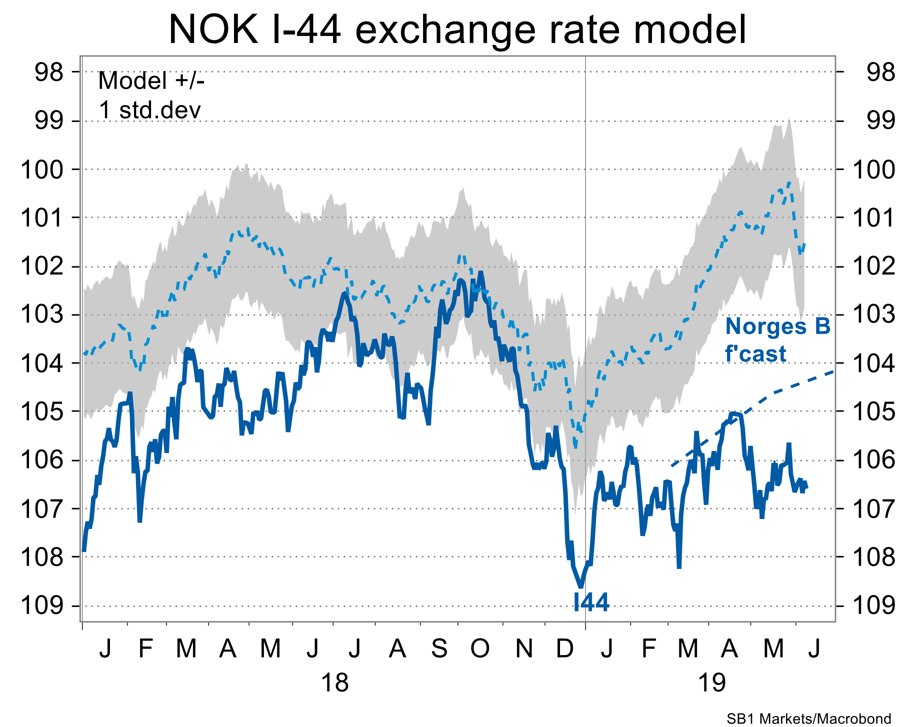


- The spread between NOK and trading partners’ 3 m money market rates at 1.37 bps is up some 50 bps since December 2017 and is now slightly above the 10 past year’s average – without sending the NOK into the orbit
- The US LIBOR-OIS spread has narrowed to 16 bps, and the NIBOR spread may have followed suit. In the rhs chart, we have technically assumed a 90% probably for a June hike
  - » The spread between NOK 3 m treasury bills and 3 m NIBOR has widened somewhat, might indicate some friction in the Norwegian money market, and a higher NIBOR – NoBa signal rate spread

NOK stabilized, is down less than the oil price implies the past 2 weeks

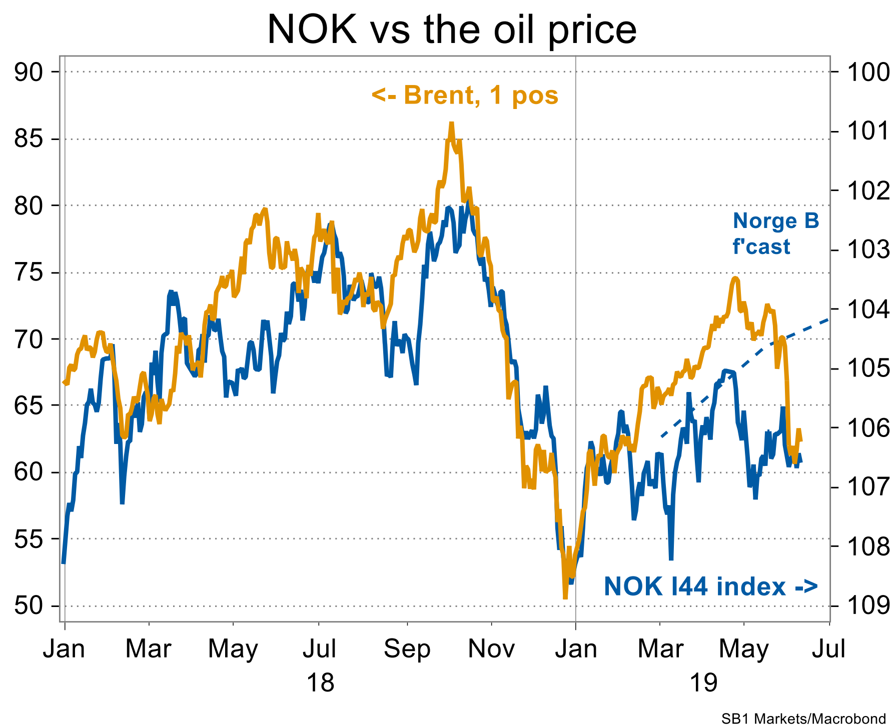
NOK held steady last week and the gap vs the model decreased to 4.9%. Still far too wide, of course

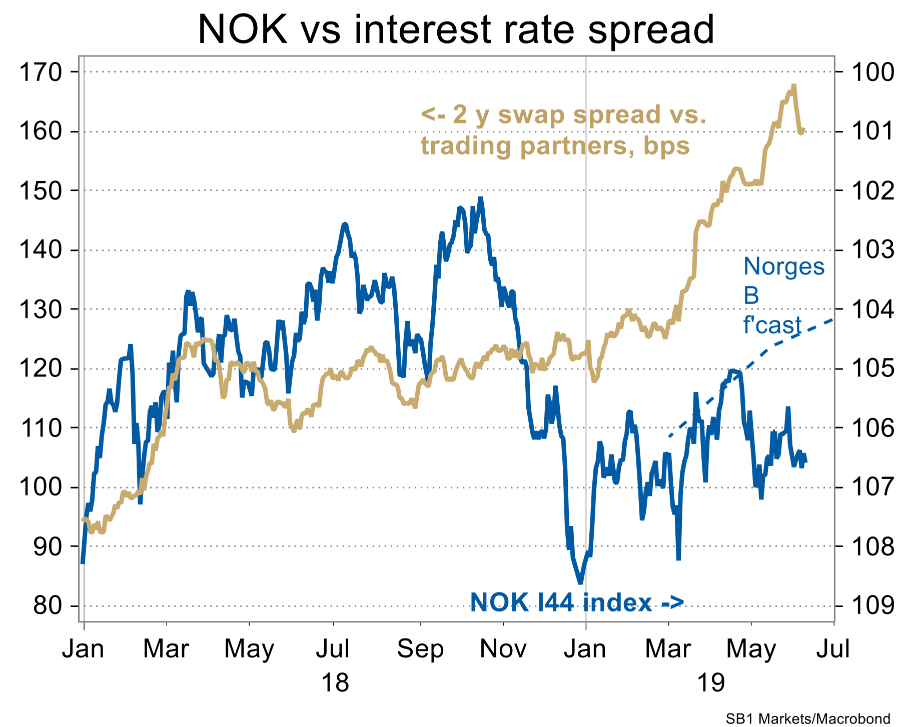




- Our model estimate has fallen sharply since late May, due to a lower oil price. The NOK depreciated somewhat less than indicated by the model but is still 5% below the model f'cast (the main drivers are the oil price and the 2 interest rate swap spread), the second highest deviation since 2010. What explains the weakness?
  - » No really weak Norwegian macro data, on the contrary, most data have been upbeat
  - » Risk aversion? Perhaps, yet EM currencies have not collapsed (even as many depreciated when the trade war escalated)
  - » Weakness in other supercycle currencies may be an explanation. NOK followed the SEK down after a dovish Riksbank, AUD & CAD are weak too, although stable recent weeks
- We do not have any other recommendation than **Buy NOK**

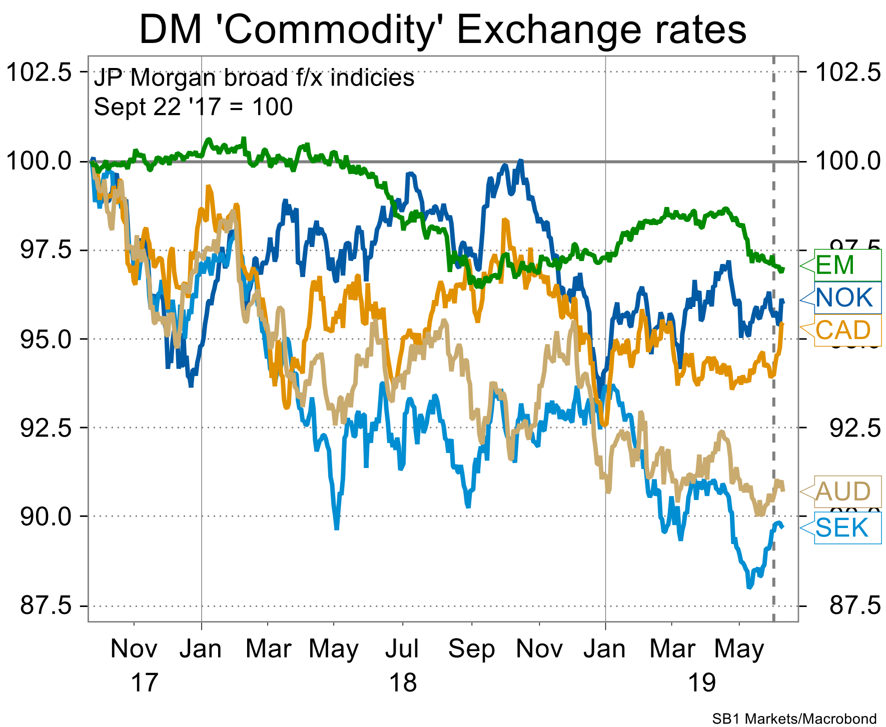
NOK fell 'less' than the oil price, as the interest rate spreads shrank

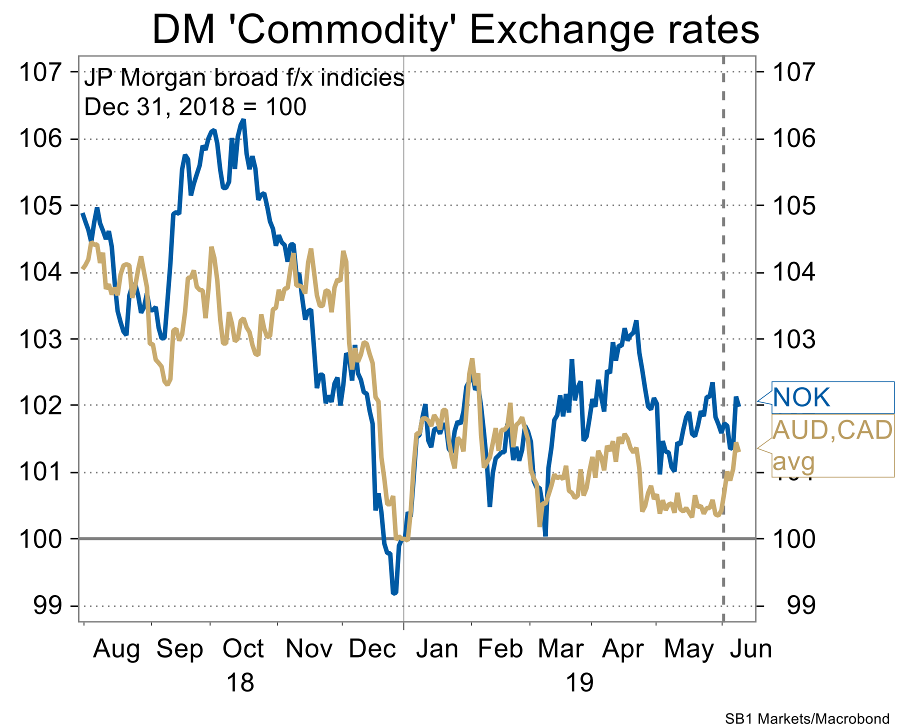




NOK saved by the super cycle friends recently?

SEK, AUD and CAD recovered somewhat, may have supported the NOK when the oil price dropped

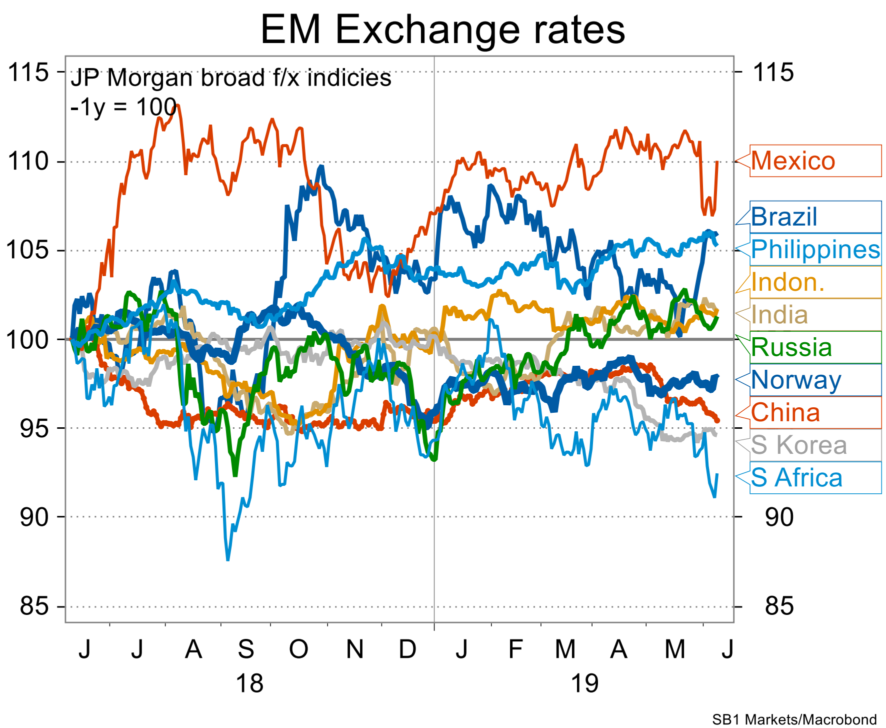


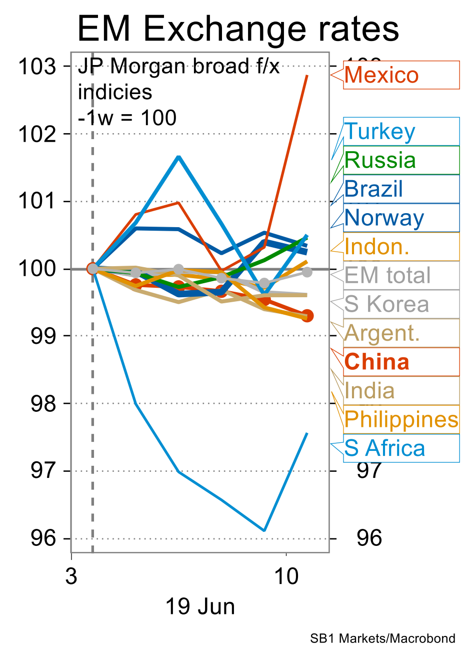


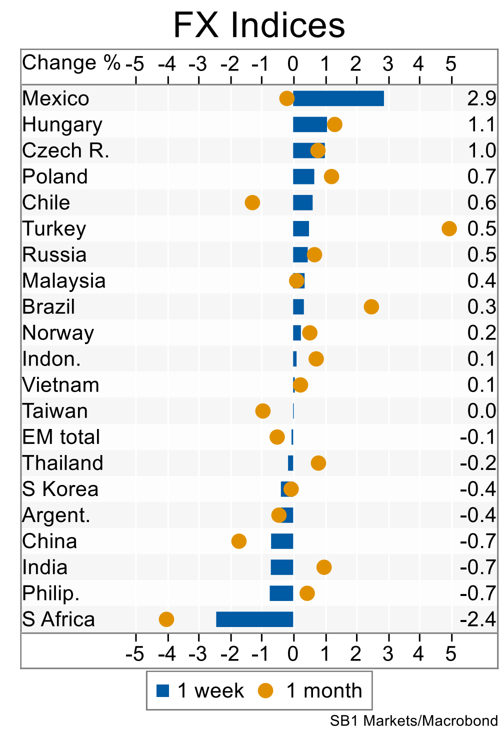
- NOK is more closely correlated to AUD, than to CAD and SEK, over time. Weak 'super cycle' currencies are perhaps the best explanation for the large deviation between the NOK and its fundamental drivers the past year
  - » Global risk appetite can often but not regularly explain the trajectory of these 'commodity' currencies. Some housing market trouble, debt concerns as well??

EM f/x a few steps down, due to South Africa, China. But the Mexican peso up!

The CNY is taking a beating as the trade war angst intensifies, while the peso recovered due to deal







- The Mexican peso depreciated after Trump's surprising tariff threat – and appreciated 2.5% yesterday as at deal between US and Mexico was reached
- The Brazilian real has been volatile recently, sharply up recent weeks
- The South African rand tumbles amid weak macro data (Q1 GDP noted a 0.8% q/q decline) and a political squabble between the Central Bank and the ANC, which is bringing the banks independence into question

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