22 July, 2019

Macro Research

A short summer update

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The headlines are linked to the relevant section in the report
The elements on the the page "In this report" are linked
A top right button will bring you back to the content page

Last week – the main takes

- No good news from **the trade front**, just signs of lack of progress
- **Global auto sales** were flat in June, and weaker than our initial estimate. Sales in EMU were substantially lower than we forecasted. Global sales are down 5% y/y, mostly due to the sharp contraction in auto sales in China. Both **global retail sales and manufacturing production** probably accelerated in June
- (Chinese June & Q2 data were reported in last week's report)
- **Mostly goods news from USA: Manufacturing production** rose further in June and the two first regional Fed **manuf. surveys** surged in early July. **Retail sales** rose more than expected in June, and following a substantial upward revision, sales volumes have more than recovered. **Housing data** were mixed, building permits sharply down but the homebuilders have not seen a sudden stop. **The Fed's Beige book** reports stable growth, and tight labour markets – and does not signal any need for cutting the Fed funds rate. One of **Fed's (too?) many talking heads** (but it was NY Fed's Williams, the Fed 'deputy') referred to research arguing for **deep cuts it rates** were low and the economy needed stimulus – rates nosedived, and the market suddenly though at 50 bps July cut was most likely. New message: He was not referring to research, not to the decision next week. The market yielded**, it will be a 25 bps, no more, no less** (even if some FOMC members still say a cut is not needed, and a majority of them in fact said so in mid June! However, some really want a deep cut, with a thoughtful analysis, in a tweet: '*Because of the faulty thought process we have going for us at the Federal Reserve, we pay much higher interest rates than countries that are no match for us economically.*' DT
- **The ZEW survey** confirmed a sluggish development in Germany
- **UK manufacturing production** remained low in May but **retail sales** are still OK. The **labour market is still tightening, the** unemployment has fallen below 4%, and wage inflation has accelerated to almost 4%; The Phillips curve is not dead, here at least
- **Swedish house prices** rose for the 4th month in row, and the number of transactions has recovered. Prices are still below the early 2017 peak
- **No Norwegian news**

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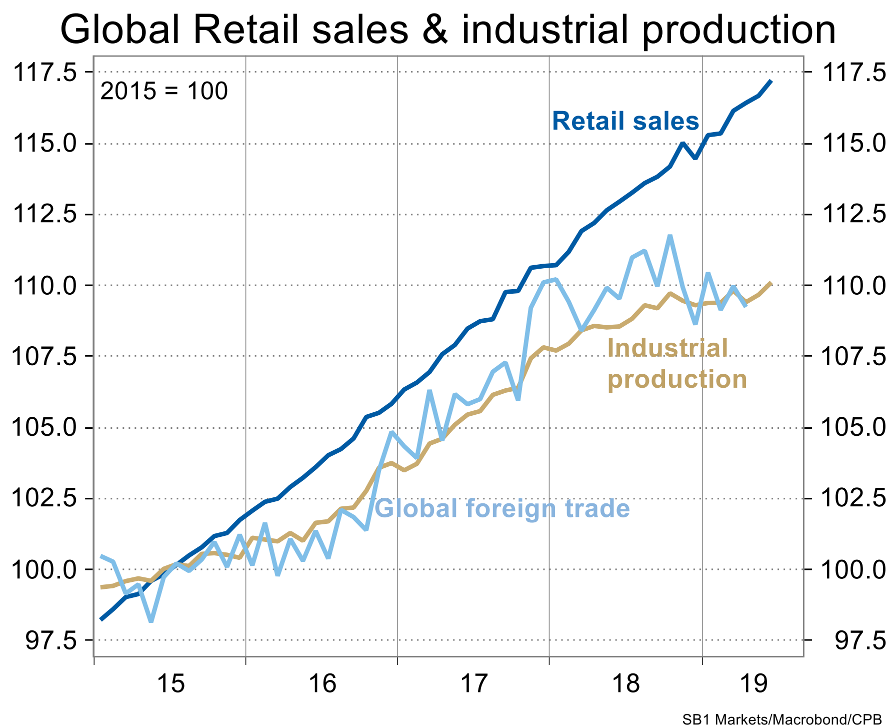
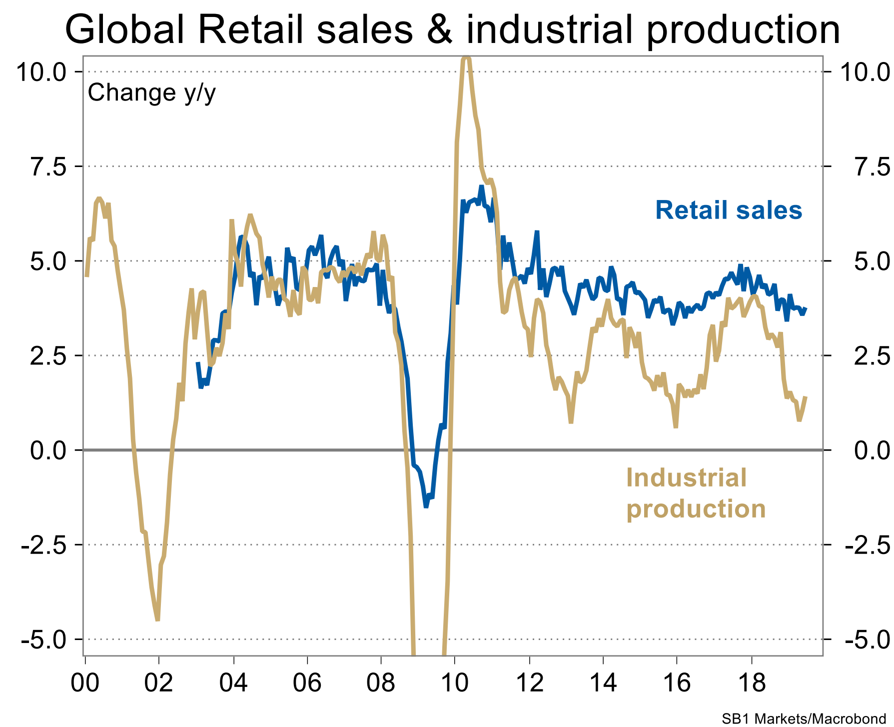
Rays of light? Retail sales, manufacturing production probably OK in June

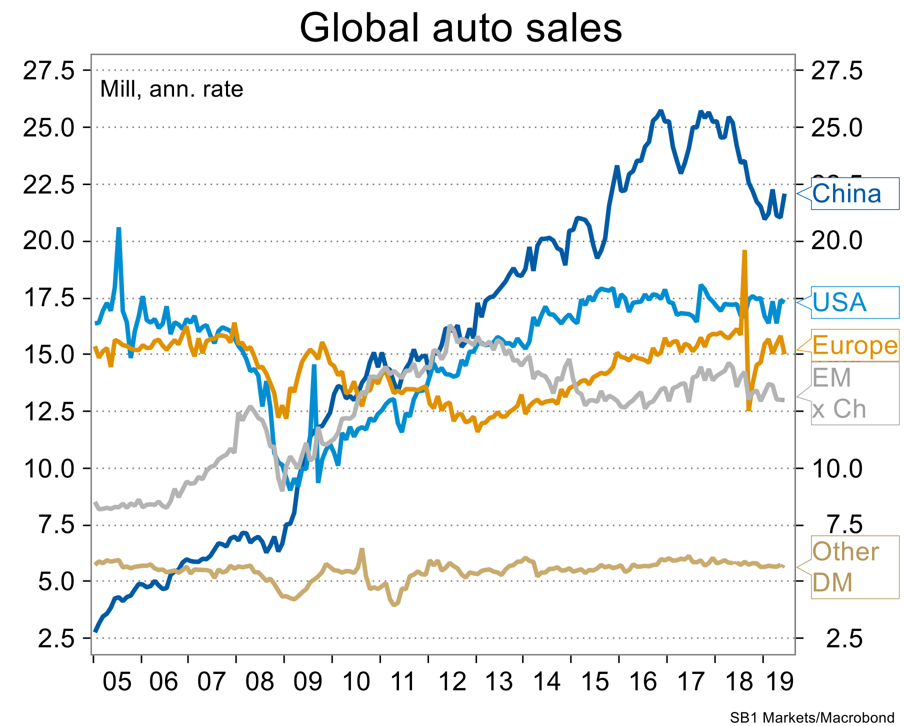


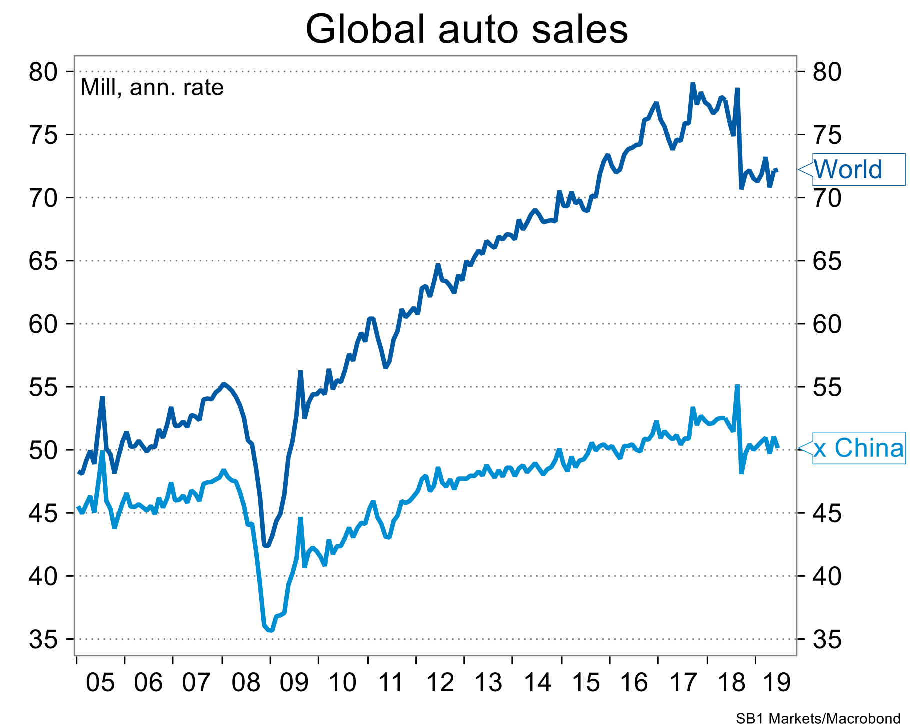


- We still have just some few data point for retail sales and manufacturing production in June but our first estimate implies decent growth from May. Retail sales have slowed somewhat but signals that consumption is still supporting the global economy.
- Global trade volumes fell in April and have stabilised the past 4 months, after retreating in late 2018

Global sales flat in June, weaker than we assumed; EMU sales down

EMU sales 6% below our first estimate



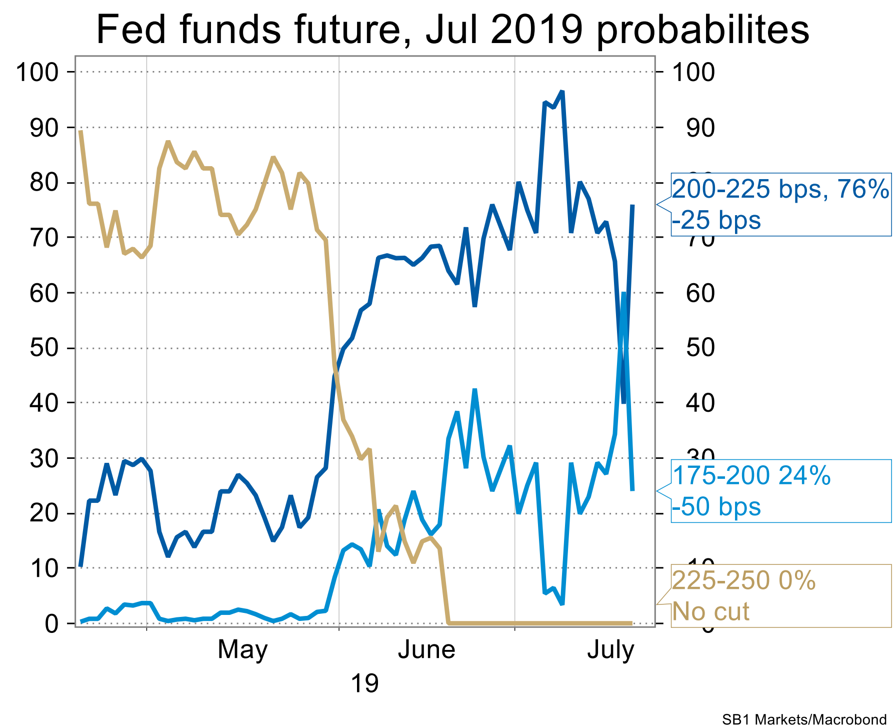


- Global auto sales was flat in June, we assumed a 1% growth, and they are down 5% y/y. Sales ex China fall almost 2%
- Sales in EMU were down 5% y/y, we assumed a 1% increase. Our f'cast model has not missed like this before (some strange data. Sales are still below the level before the emission tightening last august.
- Chines sales rose but probably just due to inventory clearance ahead of the introduction of new emission rules in many cites
- US sales were stable at a 'high' level in June but the trend is most likely slowly down
- Auto sales in EM ex. China is heading down again; mostly due to lower sales in India, Russia, Argentina and Turkey – and Indonesia and Mexico. Just Brazil is heading upwards

Fed's Beige Book confirms an OK economy but Fed will cut anyway

Fed's 'regional network' reports tight labour markets. And a Fed flip flop…

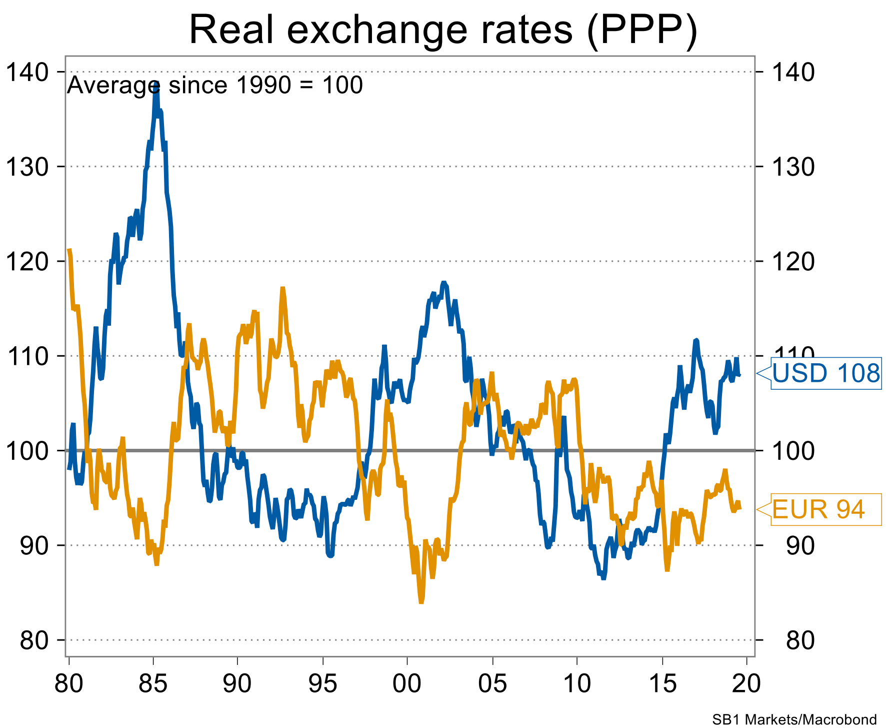
- Economic activity expanded at a '*modest*' rate in the six weeks up to end June, unchanged from the assessment from mid May, according to the respondents to Beige book. The outlook is positive, *despite widespread concerns about the possible negative impact of trade-related uncertainty.* A key-world to be used at the next FOMC meeting? No doubt
- On the demand side
  - » Retail sales are increasing even if auto sales are still flat
  - » Home sales picked up somewhat, home building flat. Other construction still growing
- On the supply side
  - » Manufacturing activity flat but some are reporting a pickup from the May report
  - » Non-financial services still OK, including tourism
- Labour market
  - » Employment growth continues but somewhat slower
  - » The labour market is tight, continued worker shortages and wages are rising but not faster than in May
- Prices
  - » Inflation stable to down slightly, even if costs are increasing as competition was strong
- **In total, the Beige book does <u>not signal any need for cutting the signal rate</u> in order to stimulate demand. The fig leaf is 'trade related/global uncertainty' to legitimise the cut, which the Fed already has 'announced'. Nothing in the report supports a 50 bps gut, of course**

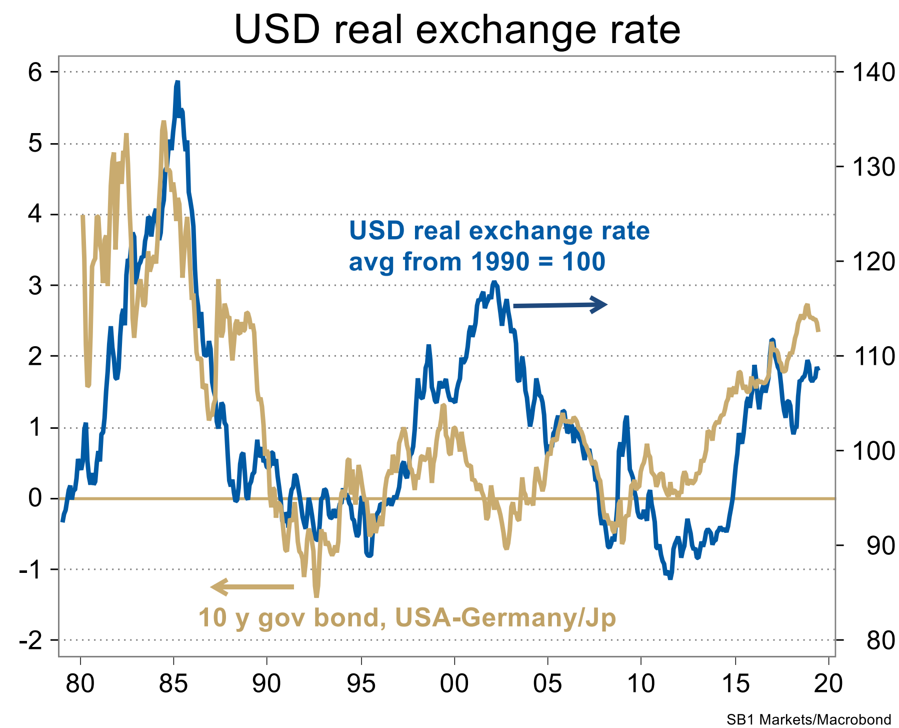


In a speech Thursday, NY Feds governor John Williams said that research had shown that a large cut in interest rates would be best if interest rates were low and the economy needed a stimulus. Did he hint about a 50 bps cut later in July? Interest rates fell sharply (6-8 bps), and the likelihood of a 50 bps cut next week rose to 60% from 34%, an unusual change! Then the NY Fed had to issue a statement to make clear the Williams just had referred to research and had made <u>no reference to the actual situation!</u> Another Fed dove, Bullard, drove the nail in by telling media he now preferred a 25 bps cut. Then market rates fell, and the likelihood of a 50 bps fell back to 24% at Friday! We think it is closer to zero

Currency wars next? The USD is somewhat above average, for a reason

However, the USD is far from record strong

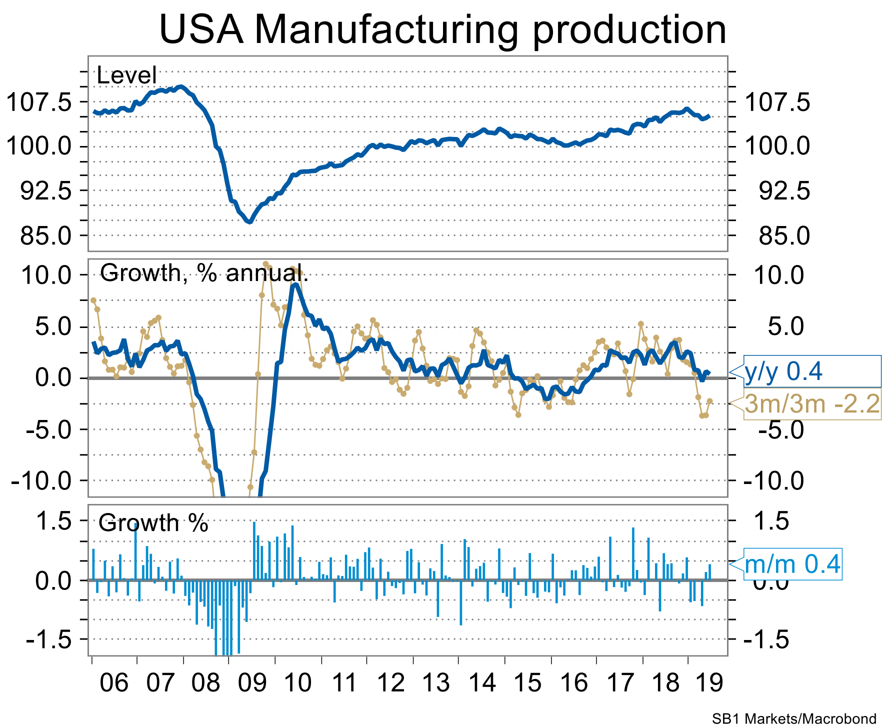


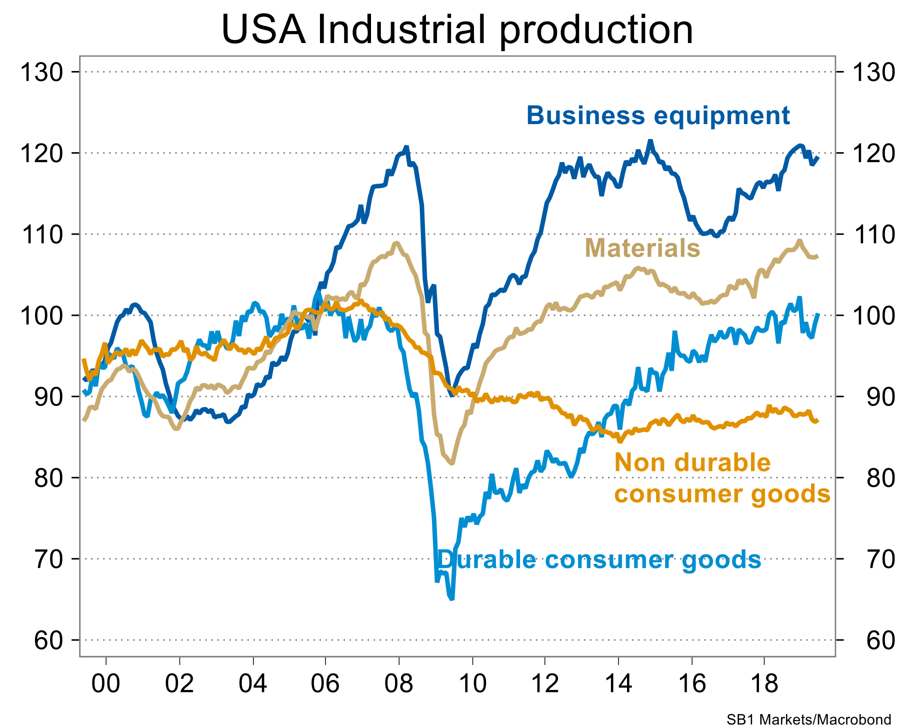


- Is the USD far too strong? Well, the greenback is 8% above average since 1990 (in order to capture two f/x cycles), measured by the real exchange rate (PPP), the same deviation as in Oct 2016, before Trump was elected. It has been up to 40% above the average in 1984 (backward calculated)
  - Higher growth, and higher interest rates in the USA than abroad are good reasons for a somewhat stronger USD than normal
- The EUR is some 5% below the average since 1990 but marginally above the average since 2012

Manufacturing production up in June, still down in Q2

Production rose 0.4% m/m, 0.1 pp more than expected. Q2 down 2.2%. Surveys up in June, still weak

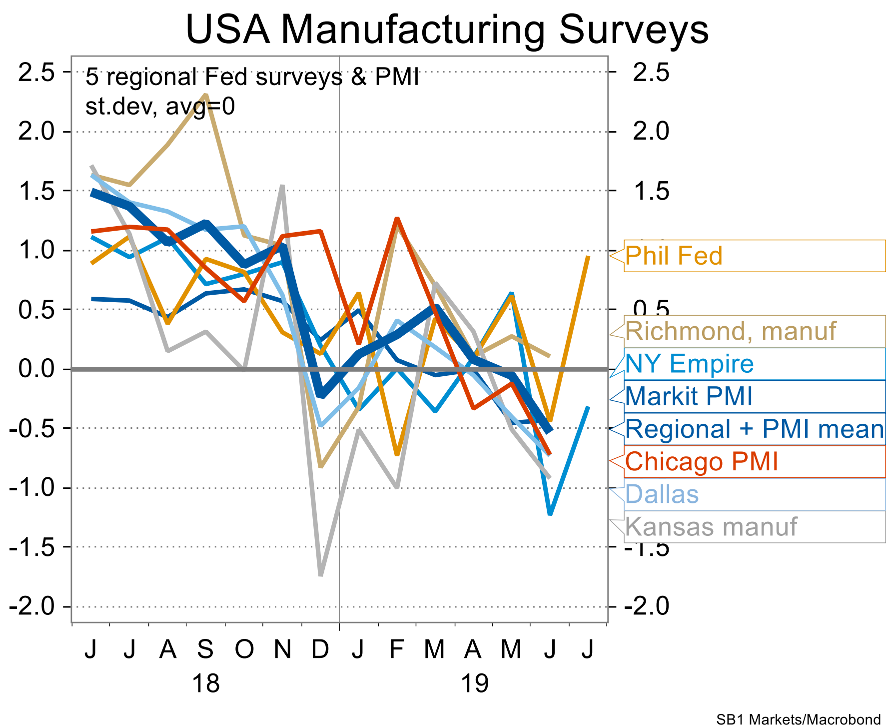


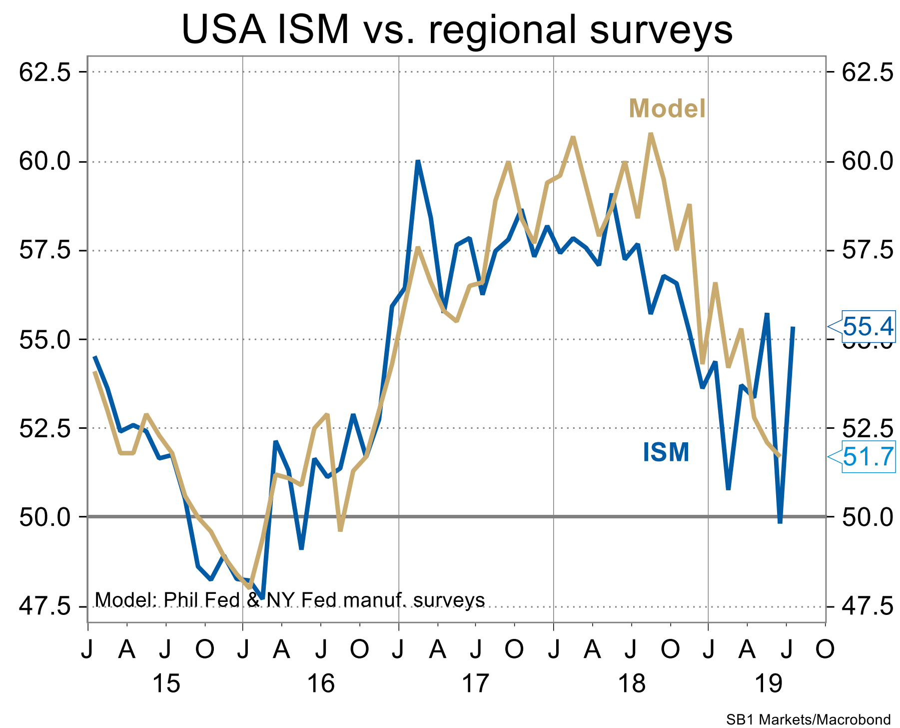


- Manufacturing production rose 0.4% m/m in June, following the 0.2% lift in May, after the 0.7% drop in April revised from -0.5%). Thus, production is still below the March level – and production fell 2.2% in Q2. Production peaked in Dec, and is now down 1.1% - but up 0.4% from June last year.
  - » Total industrial production including energy & mining was unchanged as energy production fell
  - » Durable consumer goods contributed most to the increase
  - » Output has generally not been very impressive recent years (and remains below the 2008 peak) but rose at a 2% pace through 2017/18
- The first July surveys? Check next page!

Finally, some good manufacturing news: Both NY & Phil Fed sharply up in July

Phil Fed index up 1.3 st.dev and highest since last summer! Ny Fed reversed ½ of the June nosedive

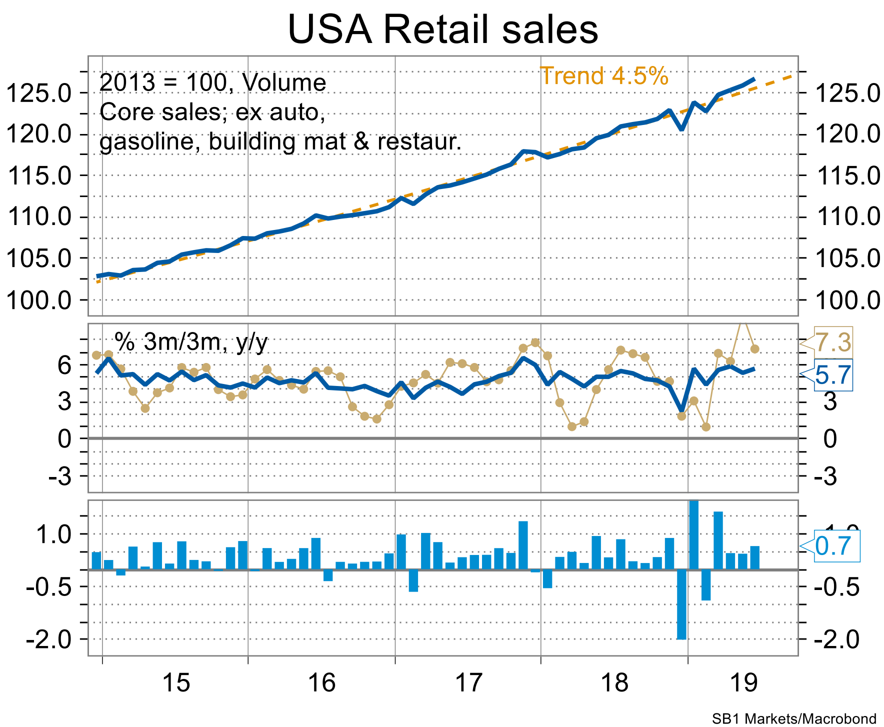


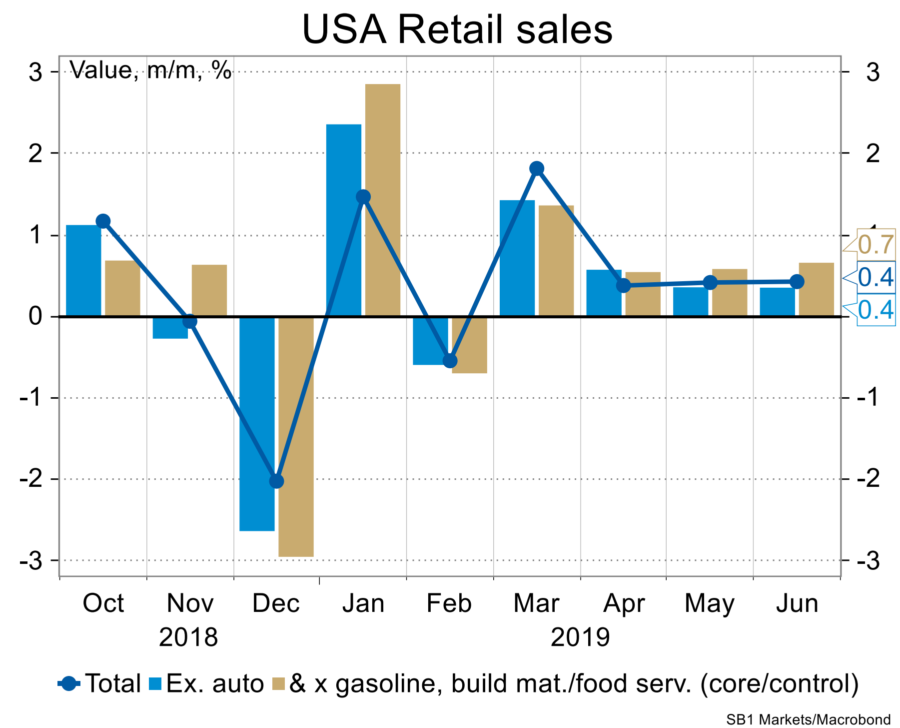


- ‘Something’ has probably happened since first part of June to July, amid some (hopefully) trade war progress and a strong recovery at the stock market; manufacturers are reporting a market change
  - » The order index recovered in both surveys but remain weak in NY Empire stat index
- These two surveys have been extra volatile so far in 2019. Taken face value, they indicate an 5.5 p lift in the ISM, if so the largest increase in 28 years. If we are more modest and let the two surveys indicate the level, a lift from 51.7 to 55.4

Retail sales have fully recovered; June strong, history revised up (again)

Core sales rose 0.7% in June, and the (volume) history revised up, once more, by 1.5%! Cut rates!

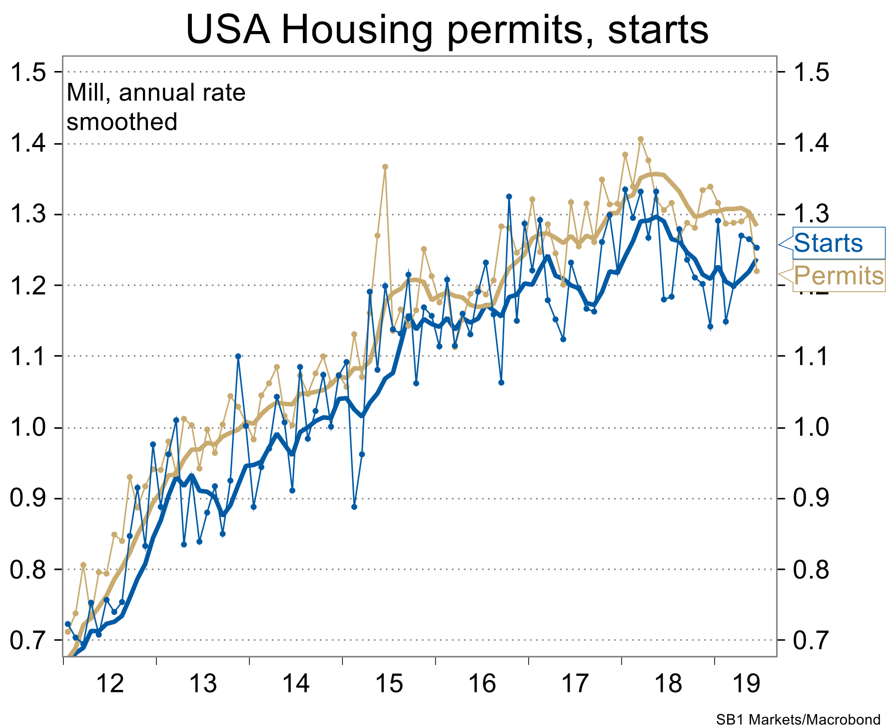


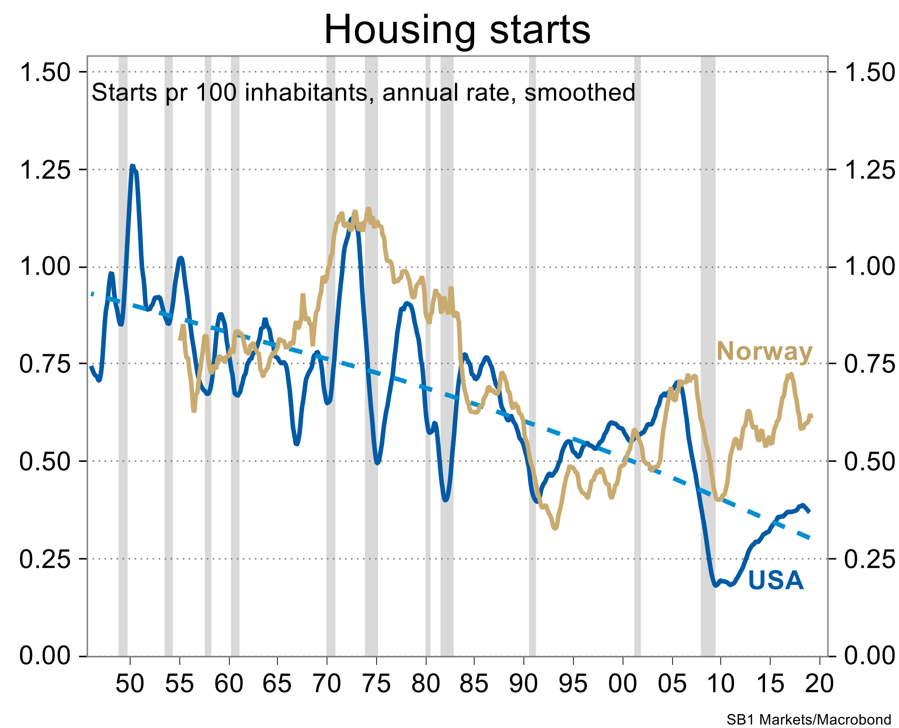


- Core retail sales (ex. auto, gas, building materials & restaurants; control group) increased by 0.7% m/m in nominal terms in June, 0.4 pp above expectations. Moreover, the sales in 2019 (in volume terms) was revised sharply up, all in all buy some 1.5%
- We estimate a 0.6% m/m volume growth in core sales, a marginal increase from the upwardly revised 0.5% in April. Given unch sales in June, core sales will have accelerated 6.6% in Q2, much better than the two previous quarters and total consumption may increase some 3%, contributing significantly to Q2 GDP growth (estimates were revised up by these figures)
  - » Consumer confidence is very strong and income and employment growth is supporting real income (and inflation subsides), and stock markets are recovering. No indications of a sudden slowdown in consumption at this point

Housing permits sharply down, so far just in May. Starts OK, but…

The peak for both was in early 2018 – and is the sharp drop in mortgage rates

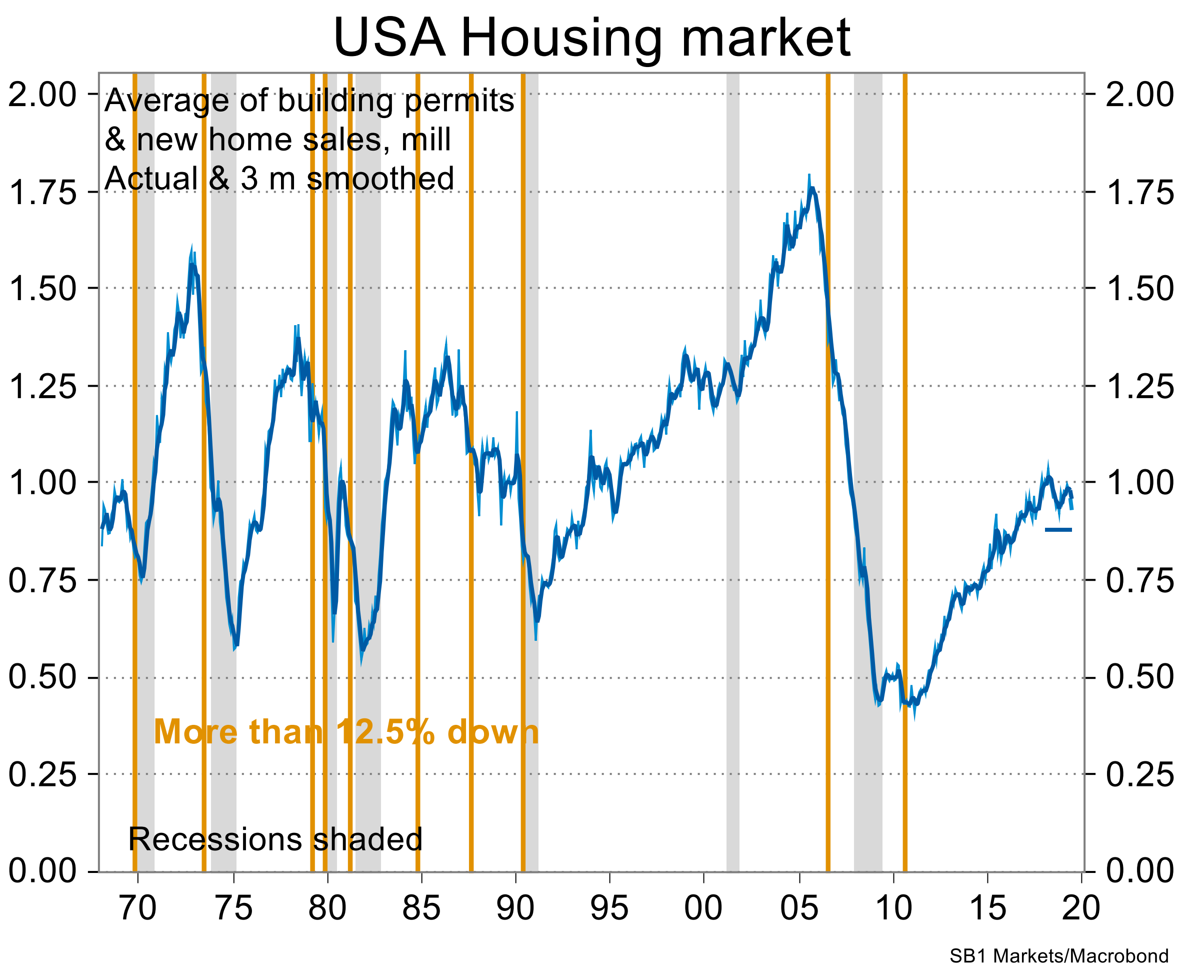


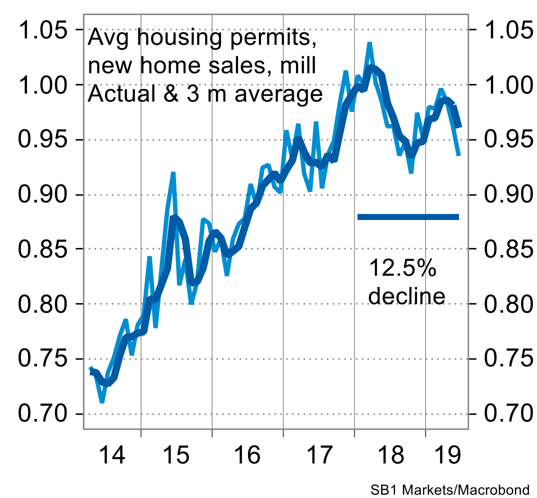


- Housing starts fell 0.9% m/m in May, to 1.253 mill (annual rate) vs expectations at 1.26 mill
- Housing permits are usually a less volatile than actual starts, and are a more useful gauge of the activity in the sector than actual starts – but this time permits fell 6.1% in June, to 1.220, expected unch. The level is the lowest since one weak month in 2016
  - » The June drop is most likely a one-off, as homebuilders have not reported any new weakness in May, June or July
- Still, there is of course a possibility that the June permit figure is correct – and even before that, both permits, starts and new home sales were heading down from the early 2018 peak. Mortgage rates have fallen sharply, and existing home sales have recovered. Is that not sufficient? Luckily, the level of housing starts is quite low, and the home construction downside is not large compared to the fall in 2006-09
  - » *New home sales will be reported this week*

Housing vs recession: Something brewing agian??

Building permits sharply down in June, still not worrisomly weak. But

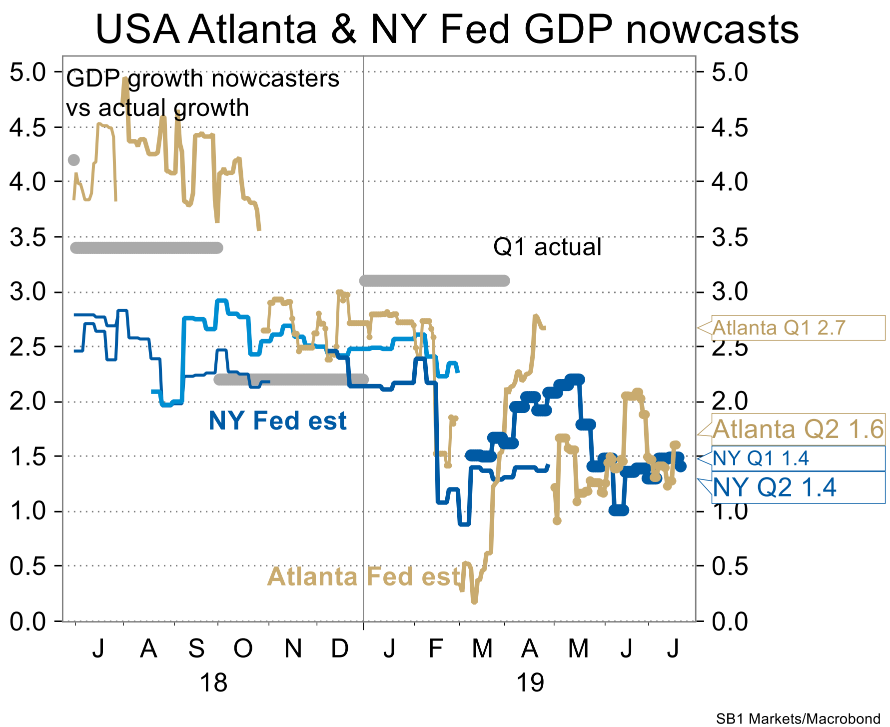


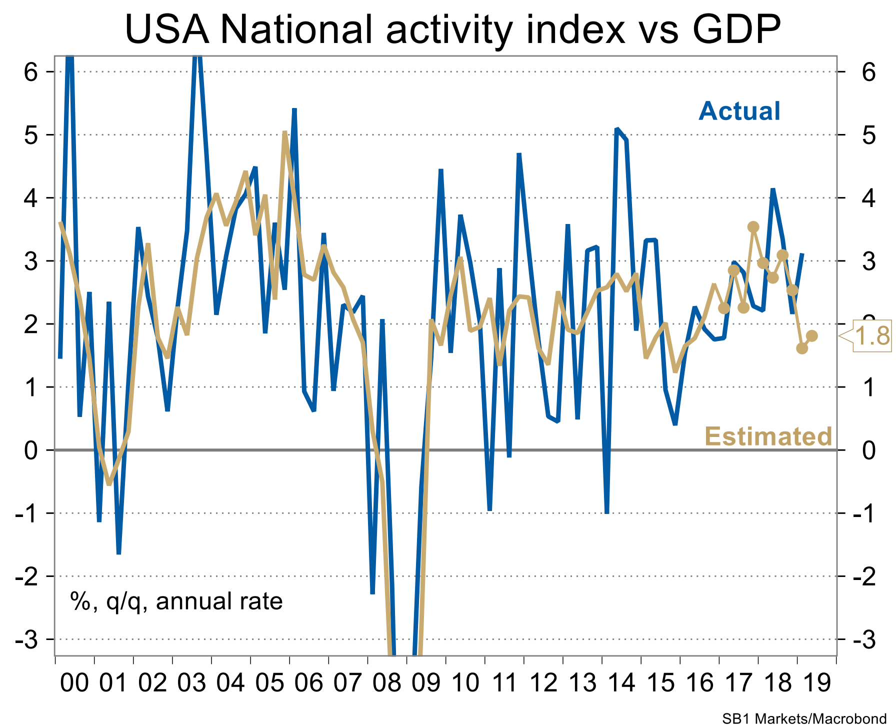


Memo: New Home sales are assumed down to 675' in in April, in line with consensus f'cast

Fed nowcasters say 1.4 – 1.6% in Q2

The National activity index signalled 1.8% Q2 growth in May (up from the 1.1% April est)





- However, a lot of data has still to be reported – and the nowcasters often miss the target (and they change their mind through to the quarter)

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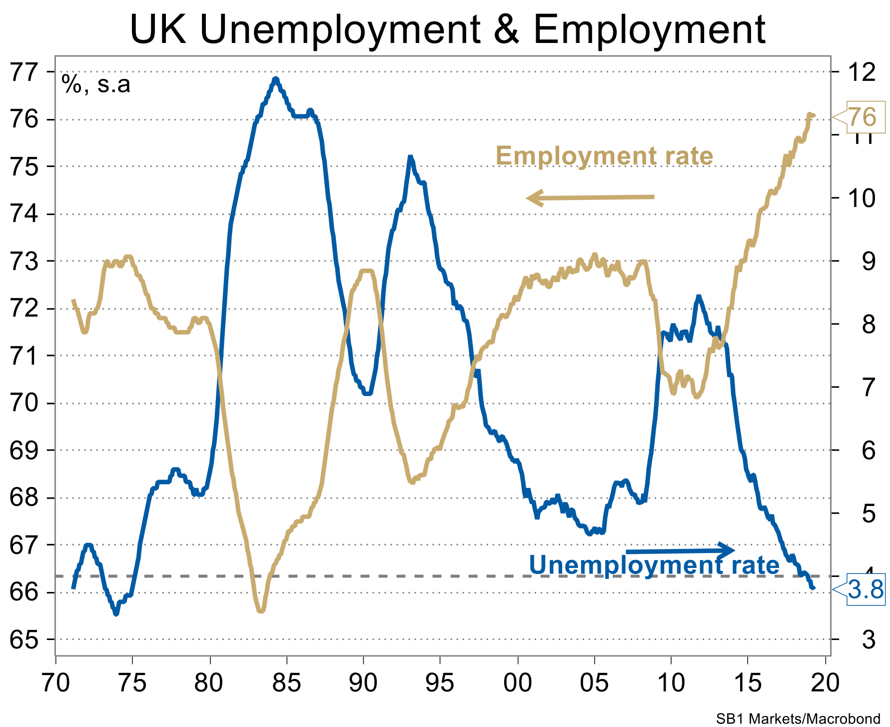
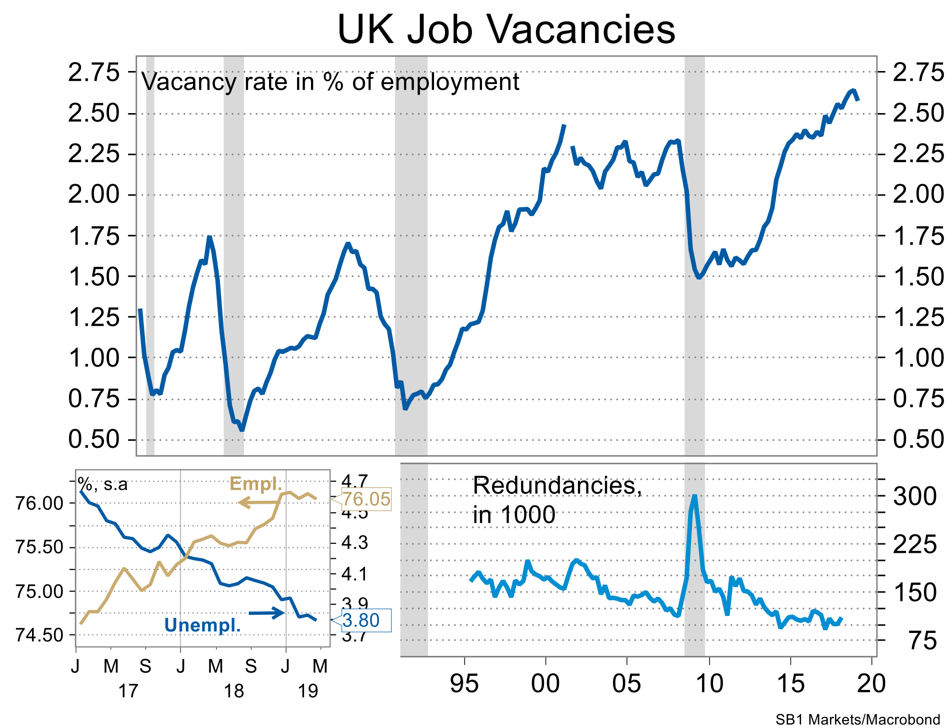
Unemployment flat at 3.8%, employment has been soaring, rising wage growth

Tight labour market; unemployment at 44 y low, high empl. & job vacancies and wages are climbing

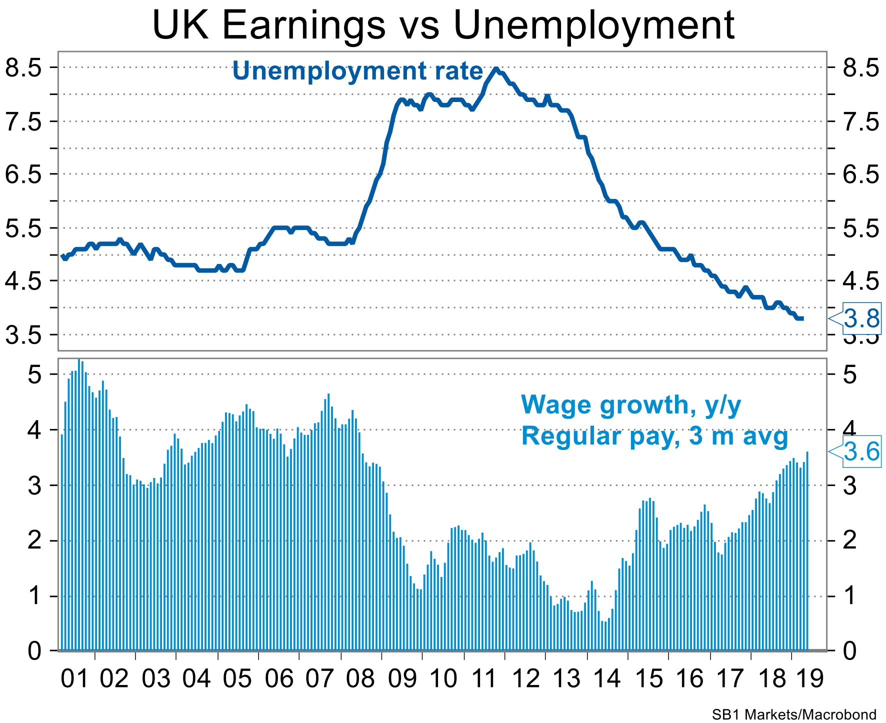


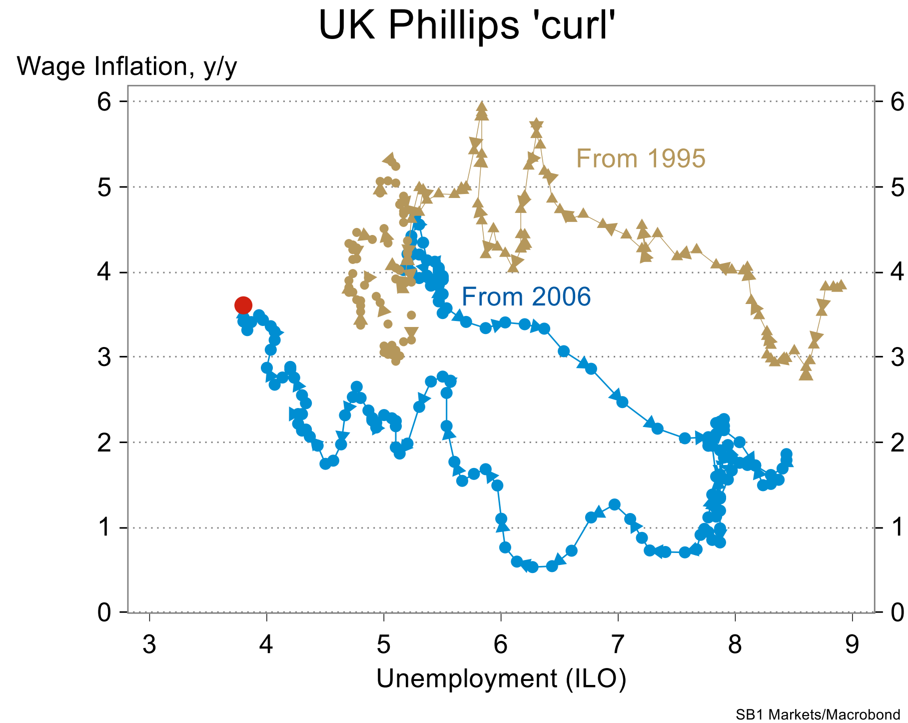


- Unemployment (LFS/ILO) was unchanged at 3.8% in April (avg March-May). The unemployment rate is the lowest since 1975
- The employment rate fell 0.1 pp to 76.0%, from the highest level ever (data back to 1971). The rate has flattened somewhat recently
- The number of job vacancies has fallen marginally recent months but is still close to a record-high level
- No surprise, wage inflation is trending up, and is approaching 4%. Wages are outpacing CPI inflation, total inflation has come down to 2.0%

A tight labour market is boosting wage inflation, now close to 4%

The Phillips curve is not dead, just bit lower/less steep than normal

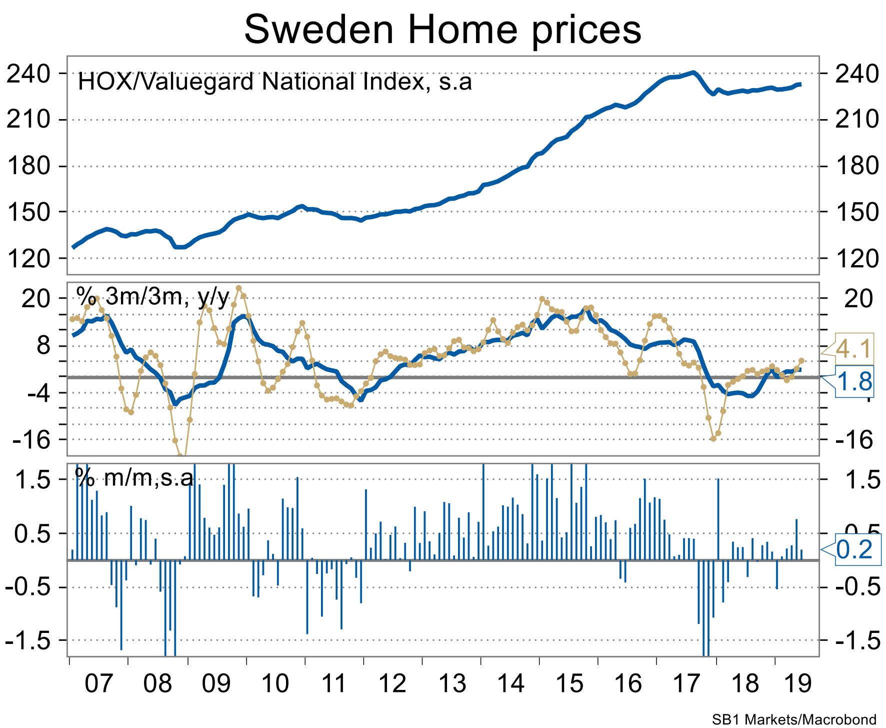


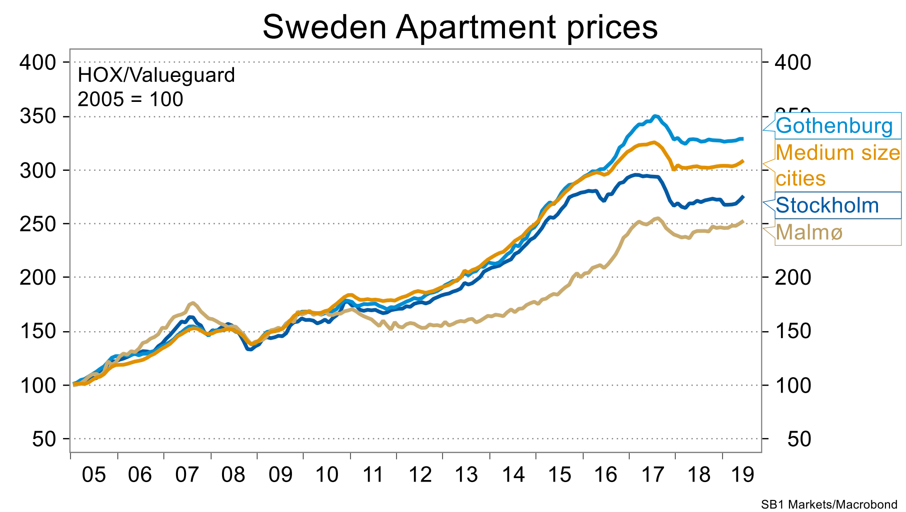


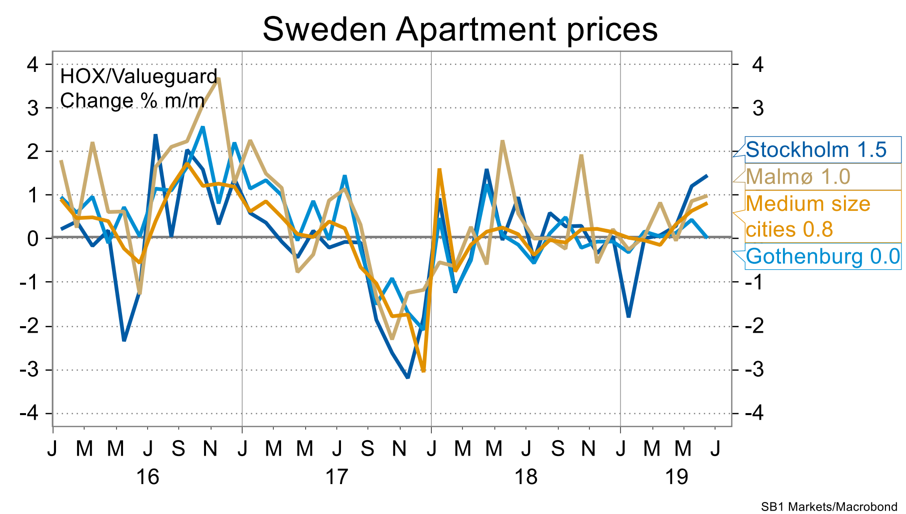
- Wage growth surprisingly surged to 4% y/y (regular pay, revised up from 3.8%), and stayed at 3.8% in June, lifting the 3 m avg to 3.6%, the highest in more than 10 years. (Next month the 3 m average will most likely be even higher, even if underlying growth last months has slowed marginally)
- UK productivity growth is very low, still well below 1%, and unit labour cost inflation is running well above the inflation target. Either will inflation become too high or corporate profits will take a hit

House prices on the way up again

Prices rose ‘just’ 0.2% m/m in May, but prices have recovered recent months







- Home prices rose 0.2% m/m seas. adj. in June, following the 0.8% jump in May. Prices are up 4.1% 3m/3m, and 1.8% y/y. Prices are still low then before the late 2017 setback and real prices are significantly down
  - » Apartment prices in Stockholm rose 1.2% in May, and another 1.5% in June! Still, St.h prices are just up 1.7% y/y. Gothenburg flat m/m in June, and are close to flat y/y too.
- The number of transactions has increased recent months, check next page. The housing market is back on track?

The Calendar

Prelim July PMIs; US GDP, orders, home sales; ECB meeting; SSB manuf. survey

Time	Country	Indicator	Period	Forecast	Prior
Monday July 22					
14:30	US	Chicago Fed Nat Activity Index	Jun	0.1	-0.05
Tuesday July 23					
08:00	NO	SSB Industrial Confidence Survey	2Q	(3)	6.9
08:00	NO	Housing Starts	Jun	(33')	35'
12:00	UK	CBI survey, orders	Jun	-15	-15
16:00	EC	Consumer Confidence	Jul A	-7.2	-7.2
16:00	US	Existing Home Sales	Jun	5.35m	5.34m
Wednesday July 24					
02:30	JN	Manufacturing PMI	Jul P	--	49.3
10:00	EC	Manufacturing PMI	Jul P	47.6	47.6
10:00	EC	Eurozone Composite PMI	Jul P	52.2	52.2
15:45	US	Markit Manufacturing PMI	Jul P	51	50.6
15:45	US	Markit Composite PMI	Jul P	--	51.5
16:00	US	New Home Sales	Jun	659k	626k
Thursday July 25					
08:00	NO	Unemployment Rate LFS	May	3.2 (3.3)	3.2%
09:00	SW	KI survey, tendecy	Jun	97.9	98.1%
09:30	SW	Unemployment Rate LFS	Jun	6.2%	6.4%
10:00	GE	IFO Expectations	Jul	94.0	94.2
13:45	EC	ECB Deposit Facility Rate	Jul-25	-0.4%	-0.4%
14:30	US	Durable Goods Orders	Jun P	0.9%	-1.3%
14:30	US	Cap Goods Orders Nondef. Ex Air	Jun P	0.7%	0.5%
14:30	US	Trade Balance Advance Goods	Jun	-$75.5	-$74.5b
14:30	US	Initial Jobless Claims	Jul-20	219	216
Friday July 26					
14:30	US	GDP Annualized QoQ	2Q A	1.8%	3.1%
14:30	US	Personal Consumption	2Q A	4.0%	0.9%
14:30	US	PCE core deflator	2Q A	2.0%	1.2%

- **The first July PMIs:** Given the lift in two US manufacturing early July surveys, the US manuf. PMI should recover some of its recent losses. In the EMU, the composite PMI was at the best level in 7 months in June, even if the manuf. Sector struggles, far below the 50 line
- **US GDP** most likely slowed significantly in Q2, even if consumption accelerated sharply. Business investments probably rose marginally, while net trade & inventories contributed negatively. Focus at the price deflator too, one of the two 'excuses' used by the Fed to legitimise a July cut. Following mixed housing data last week, **sales of new and existing homes** will provide useful cross checks.
- **The ECB** will leave the signal rate unchanged at -0.4%, and will most likely not formally decide new quantitative measures. However, the communication will be directed towards both, at least vs. more QE
- We expect the **Norwegian LFS unemployment** rate to correct up 0.1 pp to 3.3% in May

Source: Bloomberg. SB1M est. in brackets.
The most important indicators are highlighted

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	Global composite PMI stabilised in June, at 51.2, we expected a 0.4 p decline. The PMI signals just below 3% GDP growth. US and Asia the weakest links now. We think we know why. Global auto sales flat in June
China	The governments' stimulus measures may have stabilised the economy but surveys and data do not point to any swift turn of growth momentum. The invest/GDP ratio is declining rapidly. Debt growth has slowed, and will not accelerate much even if authorities are trying to stimulate credit in order to compensate for the negative impacts from the trade war/previous tightening. Fiscal policy is also activated, strongly. Exports to US (net of interm. imp) approx 2% of GDP, and a (so far) 10% decline here is manageable. However, a full scale tech/trade war will be bad, a deal with US is important	June/Q2 data in line or above expectations albeit partly due to temporary factors
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. CPI inflation is showing signs of some easing as well. No serious overinvestments but most sectors at/above trend. Business investments are probably slowing amid trade war uncertainty. Recent housing and consumption data are OK. Household debt 'low' – and the savings rate is OK, limited consumption risk. Fiscal stimulus continues into '19, but not by much. The deficit is far, far too high, given the low unemployment rate. Recession risk is increasing, but still not overwhelming, short term, and a dovish Fed may give some support. **Risks: Trump/trade/bus investments**	Retail sales back on track, while hosing data are mixed. Manufacturing better than expected in June and the two first July mauf. surveys were much better than expected. Inflation higher than expected, at core CPI above 2%. No signs of weakness in the labour market
EMU	Growth has slowed and manufacturing data are worrying while services remain resilient. 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, still consumption has kept up well. Policy risk: Trade war, populist revolt. Italy 'saved' now, not forever. Even without obvious recession triggers, weak short term data signals a substantial risk for a downturn	Auto sales were weaker than we assumed in July, and they fell from June. Manufacturing production up in May but still weak
Norway	Growth is and will remain above trend – and unemployment declines further. Oil investments have more to go. 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 above target. Electr. prices have fallen sharply, will take the headline CPI further down. Credit growth almost kept at bay just due to regulations. **Risks: Debt, housing.**	Core CPI in line with expectations in June, above target. Headline CPI sharply down due to the 'crash' in electricity prices. May GDP signals OK growth in Q2, and unemployment is anyway still falling

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

- The surprise indices are still in negative territory but less, thanks to the US
- Rays of light? Retail sales, manufacturing production probably OK in June
- Global auto sales flat in June, down 5% y/y, weaker than we assumed; EMU sales fell

USA

- Fed's Beige Book confirms an OK economy but Fed will cut anyway. But most likely 'just 25 bps
- Retail sales back at track, or even better
- Mixed housing date, permits down while builders are still optimistic
- Manufacturing production up in June, still sharply down in Q2
- Finally some good manufacturing news: Both NY & Phil Fed sharply up in June
- Fed nowcasters say 1.4 – 1.6% in Q2

EMU

- The German ZEW survey further down in July

UK

- Unemplyment below 4% and wage inflation is approaching 4%. Phillips is not dead, after all?
- CPI stabilised around 2%
- Retail sales still going strong
- Manufacturing production still weak, before the real destocking starts

Sweden

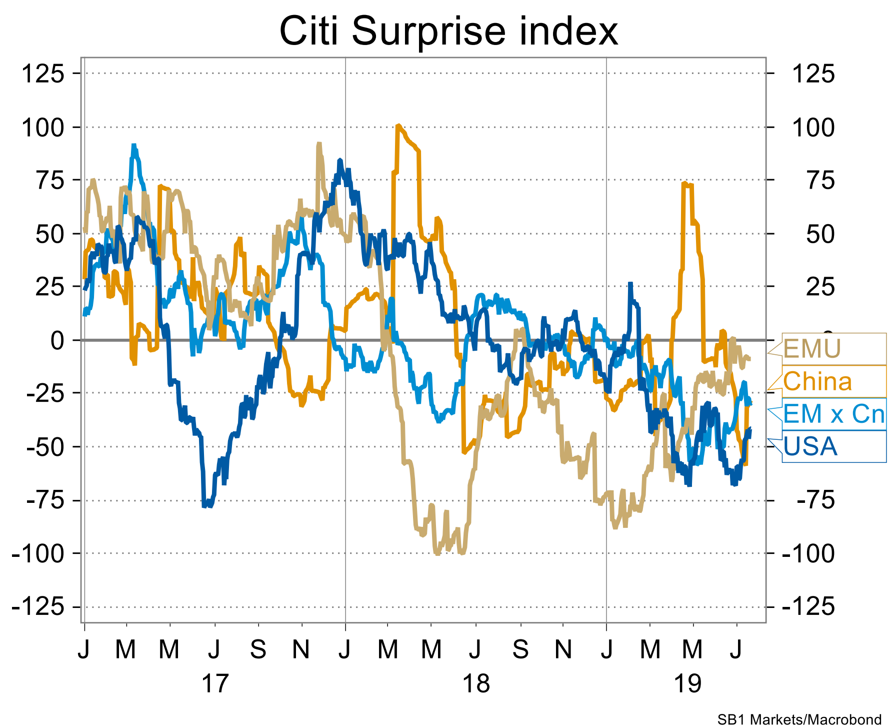
- House prices rose further in June, more transactions. Stockholm in the lead

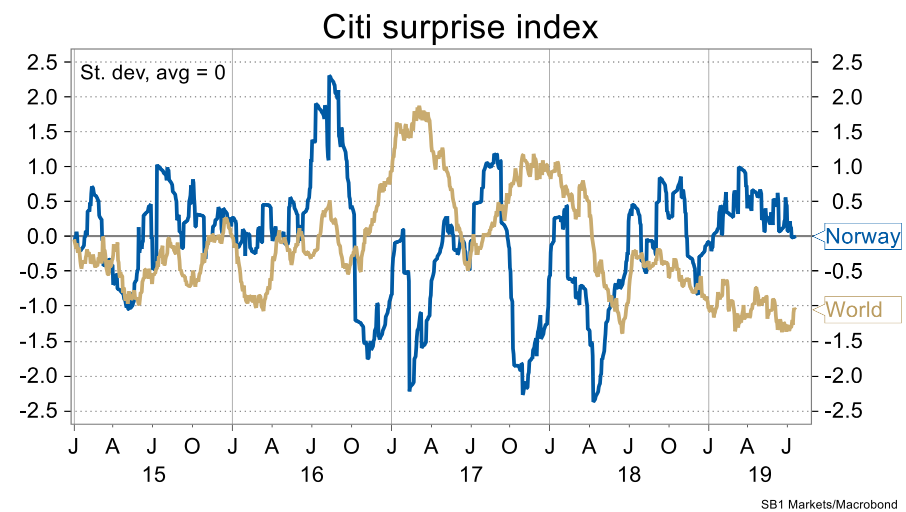
Norway

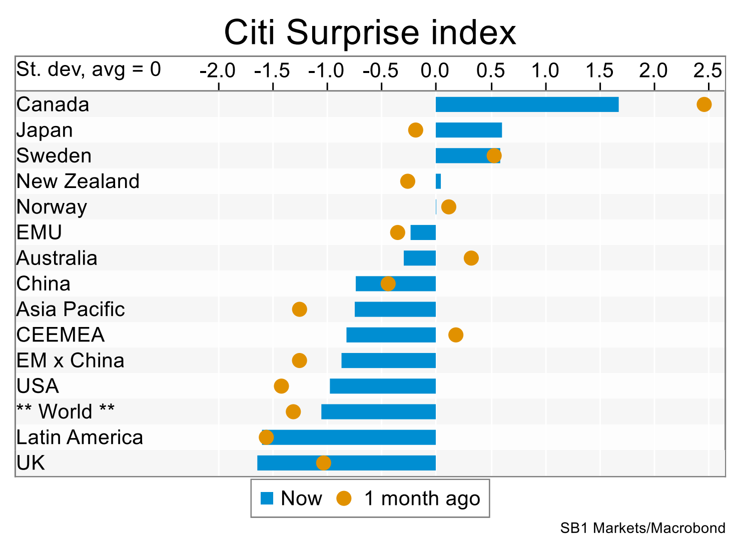
- No important news

Less US (& global) disappointments

All major regions are reporting data below par, and US at the bottom of that league - but less so now



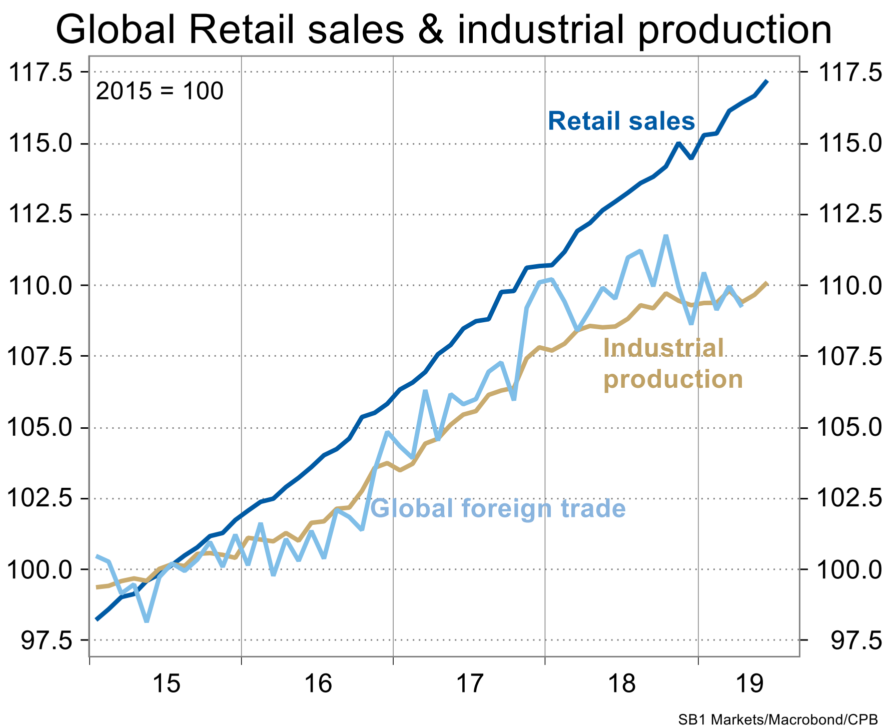


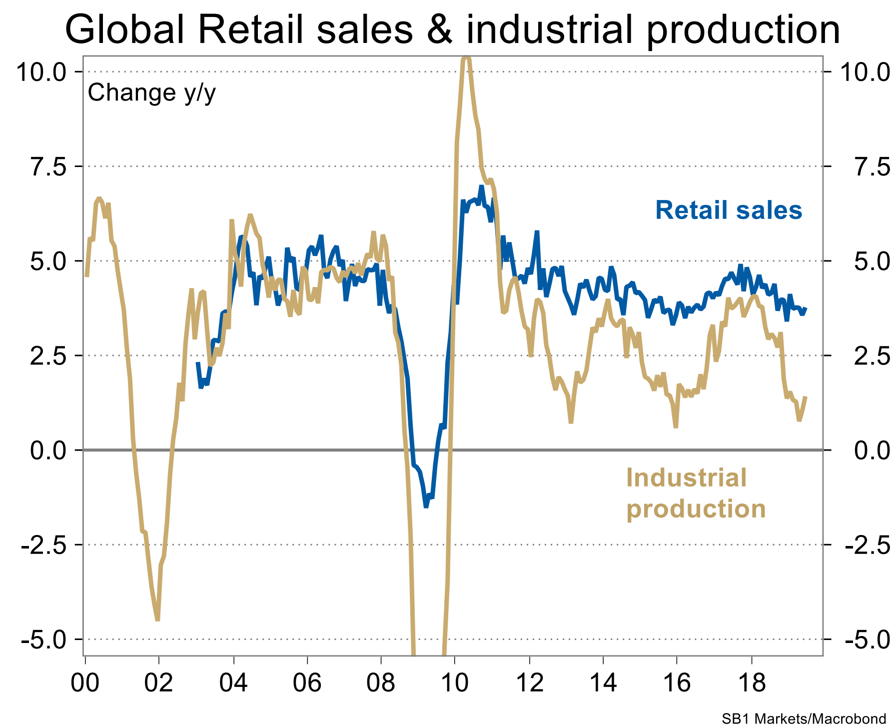


- The global surprise index has been in negative territory since last spring, but less so last week
- The US date still negative over the 3 last months period, but less so last week
- EMU is not far below average vs (lowered) expectations
- Chinese June/Q2 data better than expected, and surprise index turned up
- EM x China less negative recent weeks
- Norwegian data close to neutral. Canada at the top, UK at the bottom.

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

Rays of light? Retail sales, manufacturing production probably OK in June

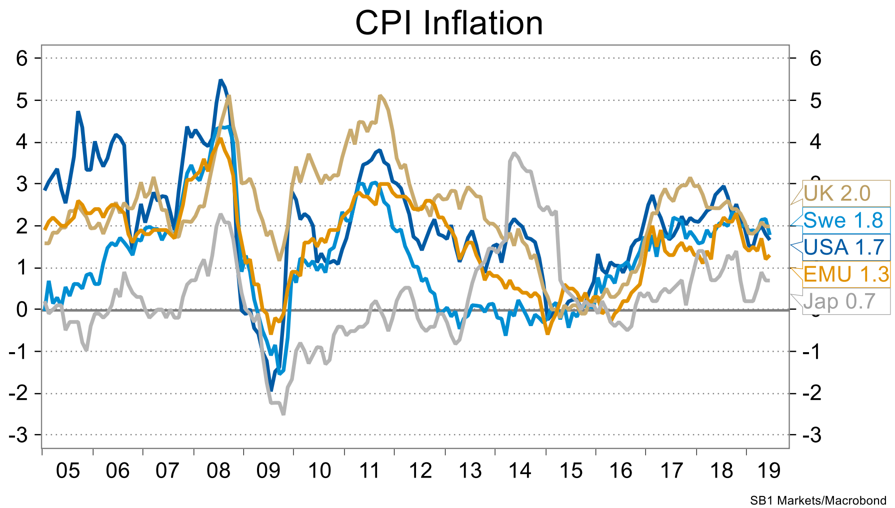


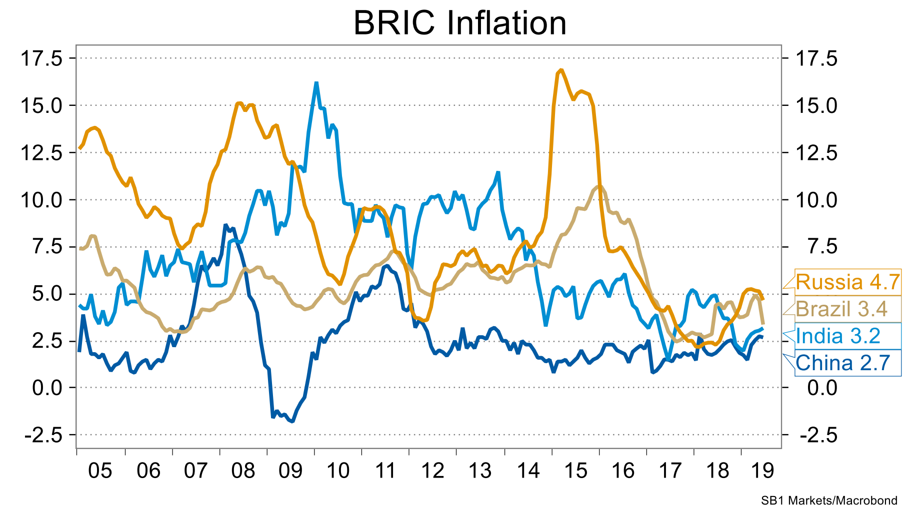


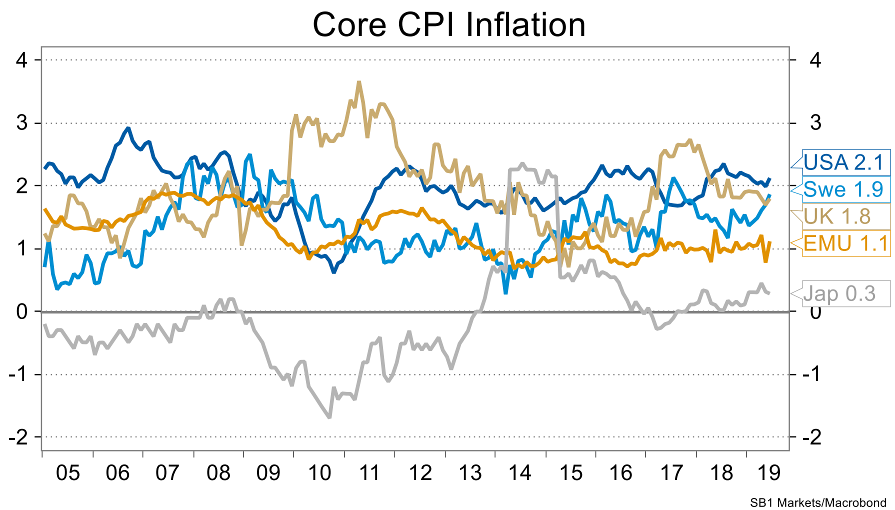
- We still have just some few data point for retail sales and manufacturing production in June but our first estimate implies decent growth from May. Retail sales have slowed somewhat but signals that consumption is still supporting the global economy.
- Global trade volumes fell in April and have stabilised the past 4 months, after retreating in late 2018

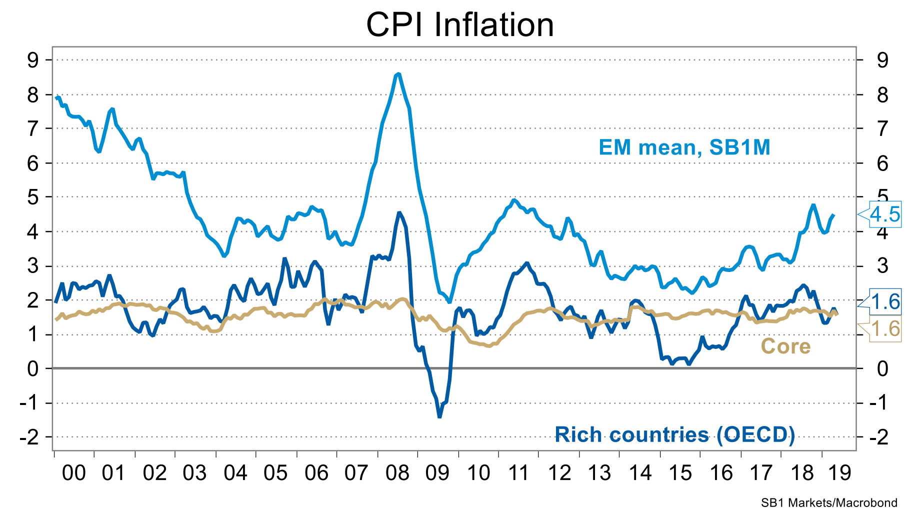
DM to turn south again, with the oil price? Core is sum flattish

Core inflation at target in US, not far below in UK, Sweden. EMU still muted. EM inflation not low





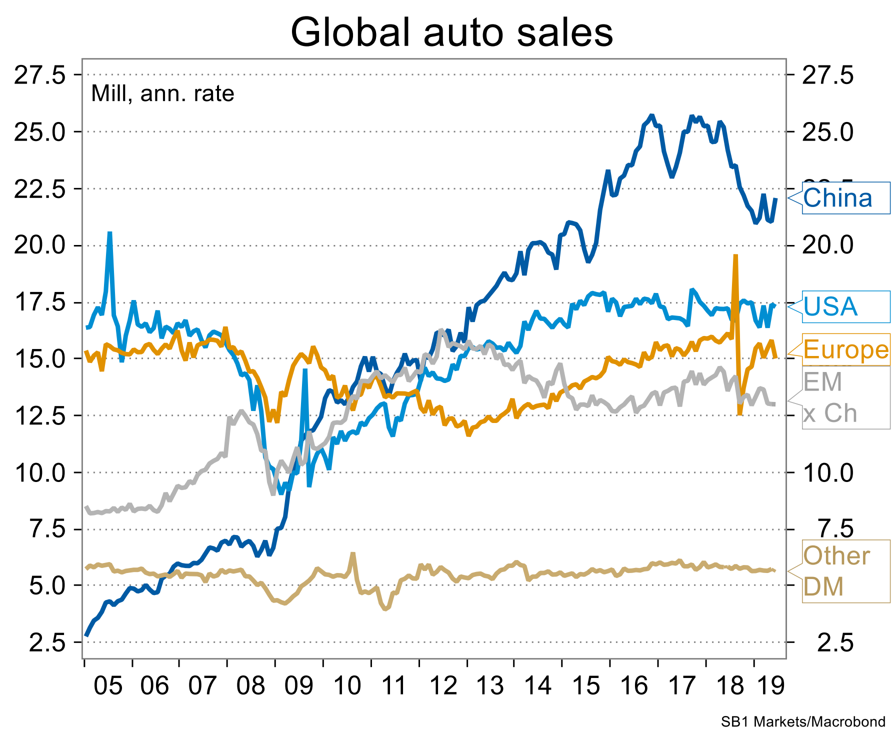


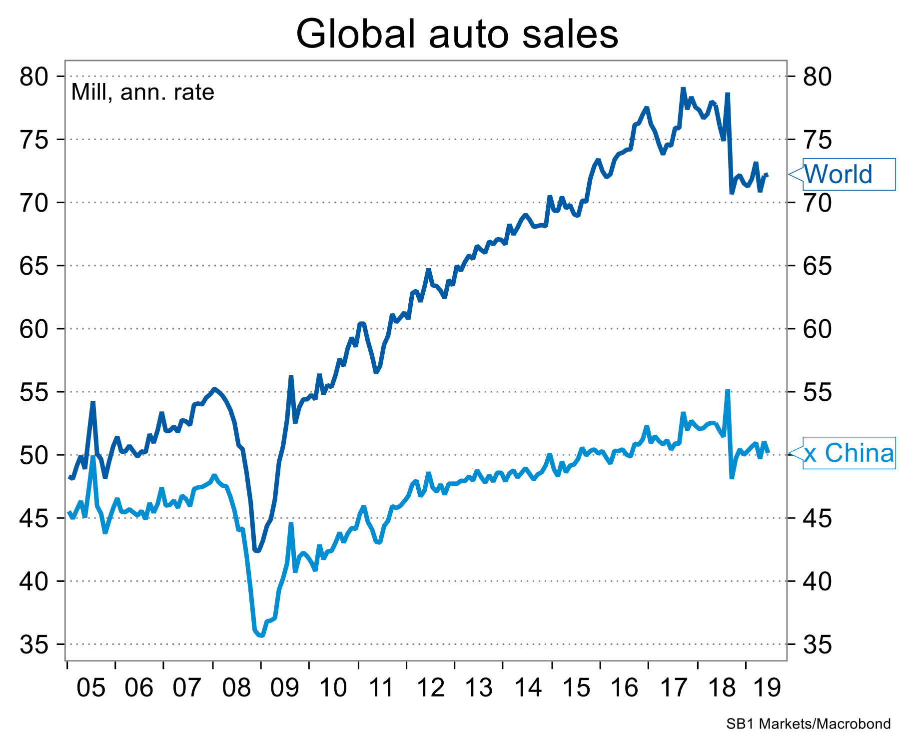


Change in % y/y in all charts. EMU core based on a seasonally adjusted price index

Global sales flat in June, weaker than we assumed; EMU sales fell

EMU sales 6% below our first estimate



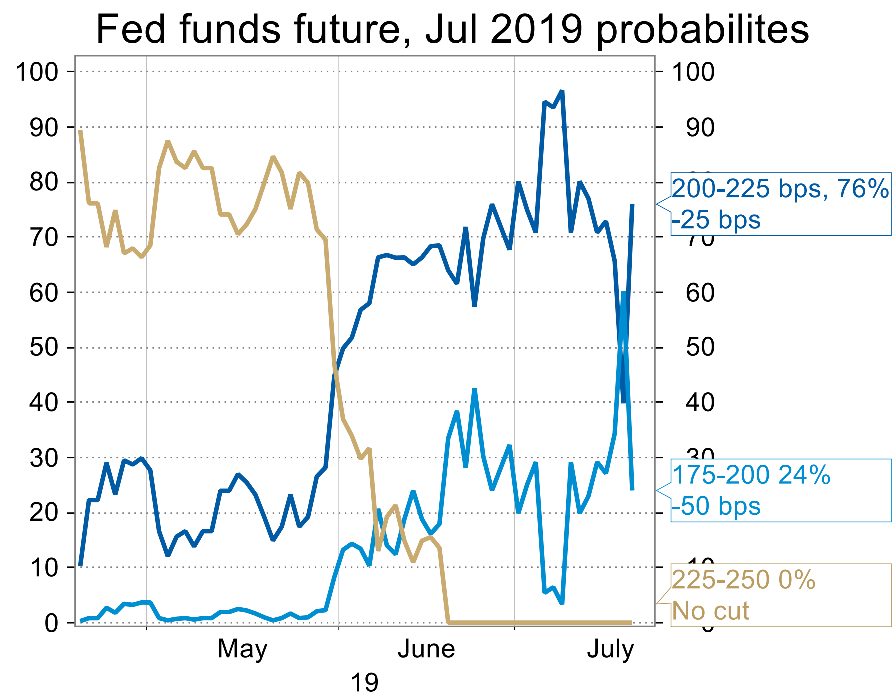


- Global auto sales was flat in June, we assumed a 1% growth, and they are down 5% y/y. Sales ex China fall almost 2%
- Sales in EMU were down 5% y/y, we assumed a 1% increase. Our f'cast model has not missed like this before (some strange data. Sales are still below the level before the emission tightening last august.
- Chines sales rose but probably just due to inventory clearance ahead of the introduction of new emission rules in many cites
- US sales were stable at a 'high' level in June but the trend is most likely slowly down
- Auto sales in EM ex. China is heading down again; mostly due to lower sales in India, Russia, Argentina and Turkey – and Indonesia and Mexico. Just Brazil is heading upwards

Fed's Beige Book confirms an OK economy but Fed will cut anyway

Fed's 'regional network' reports tight labour markets. And a Fed flip flop…

- Economic activity expanded at a '*modest*' rate in the six weeks up to end June, unchanged from the assessment from mid May, according to the respondents to Beige book. The outlook is positive, *despite widespread concerns about the possible negative impact of trade-related uncertainty.* A key-world to be used at the next FOMC meeting? No doubt
- On the demand side
  - Retail sales are increasing even if auto sales are still flat
  - Home sales picked up somewhat, home building flat. Other construction still growing
- On the supply side
  - Manufacturing activity flat but some are reporting a pickup from the May report
  - Non-financial services still OK, including tourism
- Labour market
  - Employment growth continues but somewhat slower
  - The labour market is tight, continued worker shortages and wages are rising but not faster than in May
- Prices
  - Inflation stable to down slightly, even if costs are increasing as competition was strong
- **In total, the Beige book does <u>not signal any need for cutting the signal rate</u> in order to stimulate demand. The fig leaf is 'trade related/global uncertainty' to legitimise the cut, which the Fed already has 'announced'. Nothing in the report supports a 50 bps gut, of course**

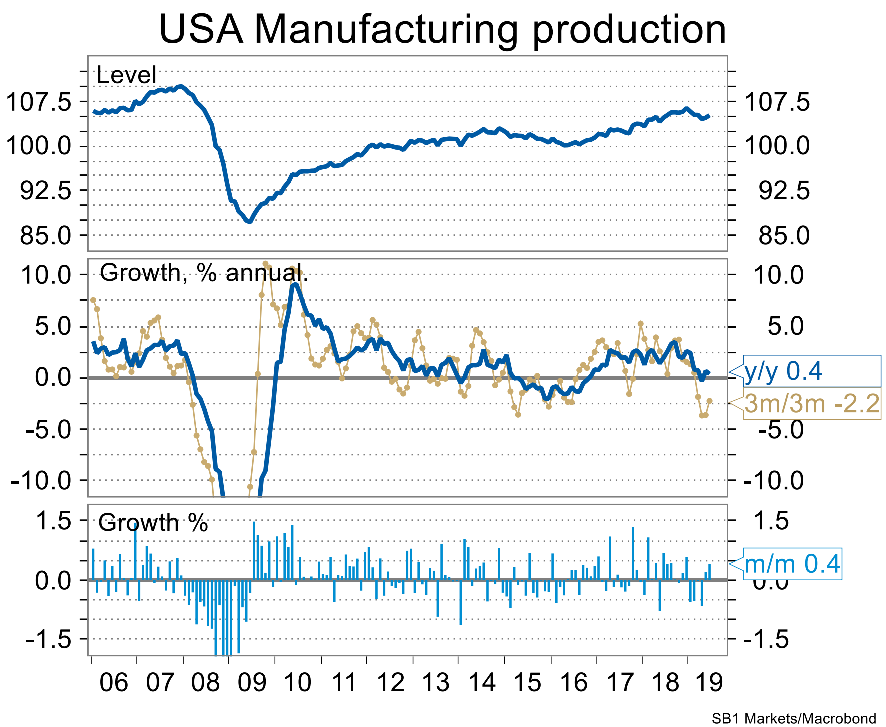


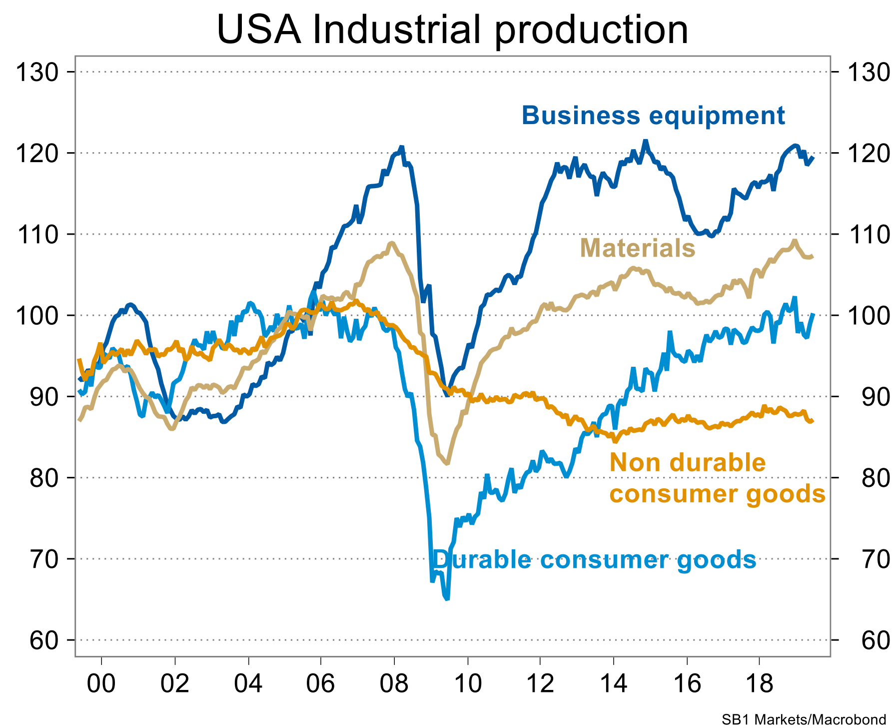
SB1 Markets/Macrobond

In a speech Thursday, NY Feds governor John Williams said that research had shown that a large cut in interest rates would be best if interest rates were low and the economy needed a stimulus. Did he hint about a 50 bps cut later in July? Interest rates fell sharply (6-8 bps), and the likelihood of a 50 bps cut next week rose to 60% from 34%, an unusual change! Then the NY Fed had to issue a statement to make clear the Williams just had referred to research and had made <u>no reference to the actual situation!</u> Another Fed dove, Bullard, drove the nail in by telling media he now preferred a 25 bps cut. Then market rates fell, and the likelihood of a 50 bps fell back to 24% at Friday! We think it is closer to zero

Manufacturing production up in June, still down in Q2

Production rose 0.4% m/m, 0.1 pp more than expected. Q2 down 2.2%. Surveys up in June, still weak

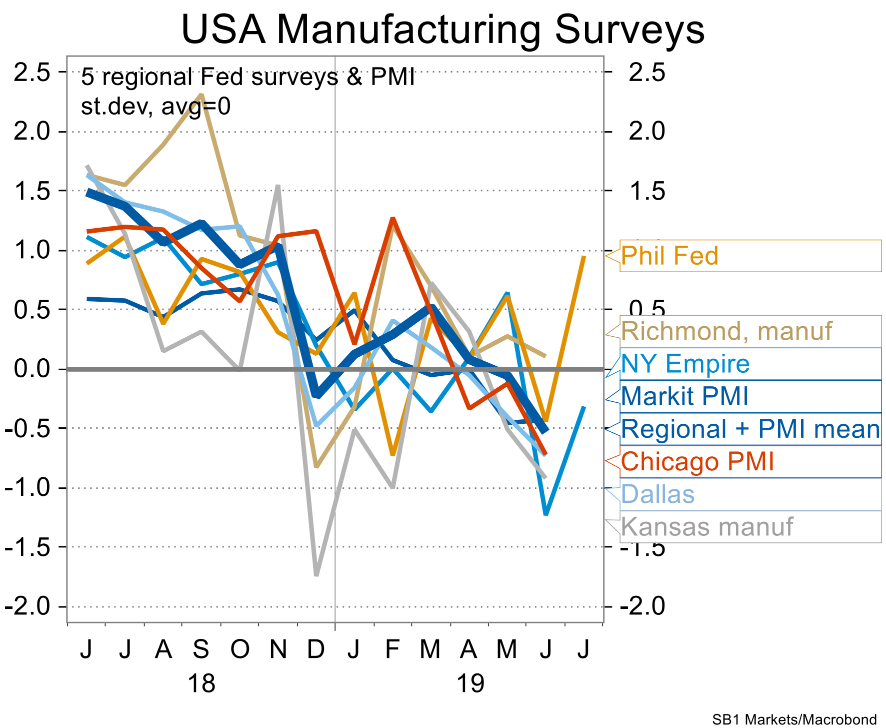


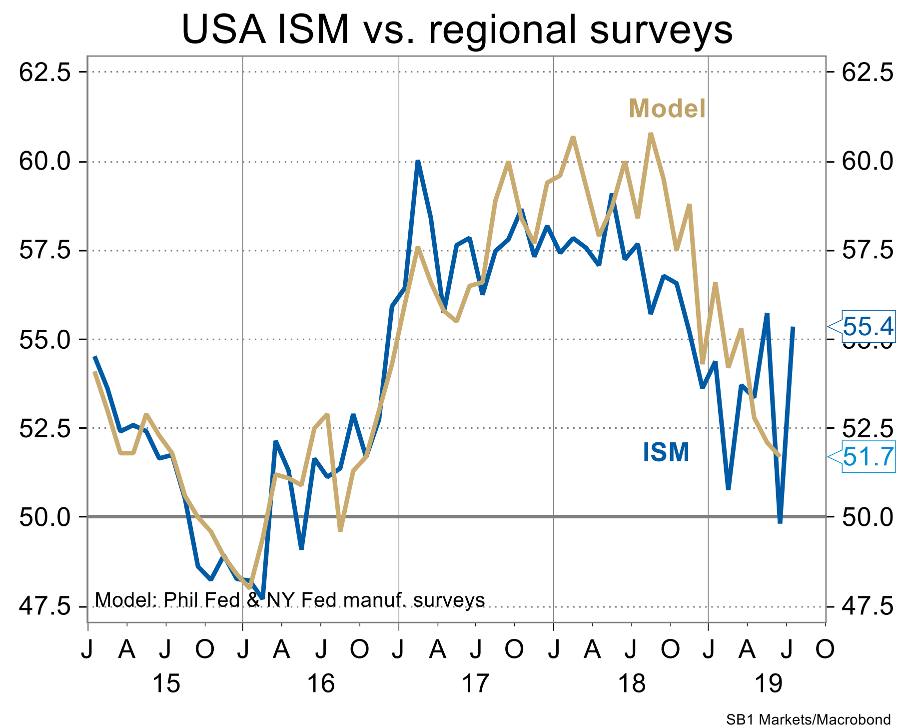


- Manufacturing production rose 0.4% m/m in June, following the 0.2% lift in May, after the 0.7% drop in April revised from -0.5%). Thus, production is still below the March level – and production fell 2.2% in Q2. Production peaked in Dec, and is now down 1.1% - but up 0.4% from June last year.
  - » Total industrial production including energy & mining was unchanged as energy production fell
  - » Durable consumer goods contributed most to the increase
  - » Output has generally not been very impressive recent years (and remains below the 2008 peak) but rose at a 2% pace through 2017/18
- The first July surveys? Check next page!

Finally, some good manufacturing news: Both NY & Phil Fed sharply up in July

Phil Fed index up 1.3 st.dev and highest since last summer! Ny Fed reversed ½ of the June nosedive

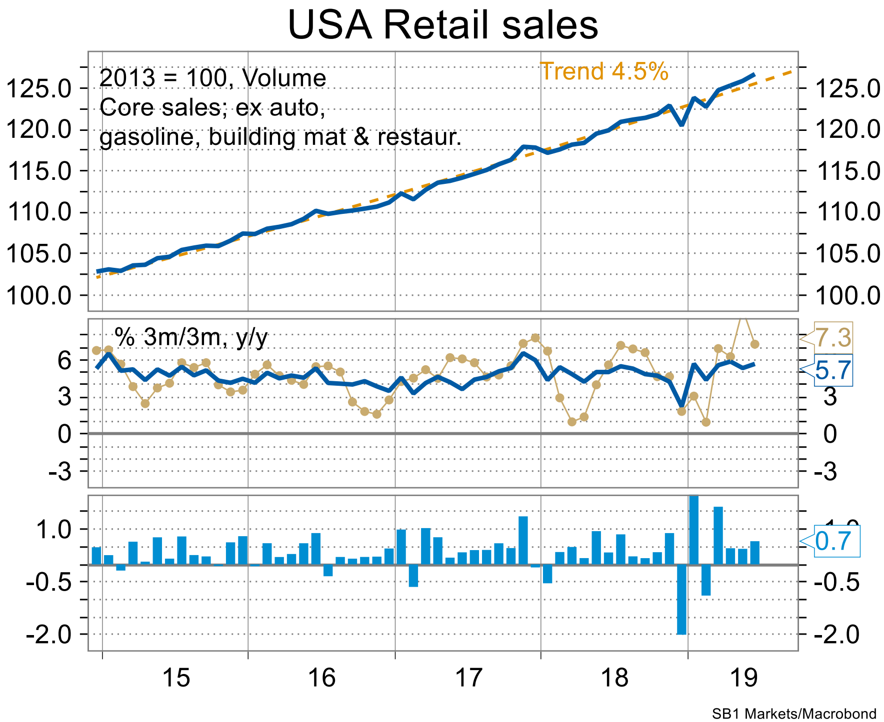


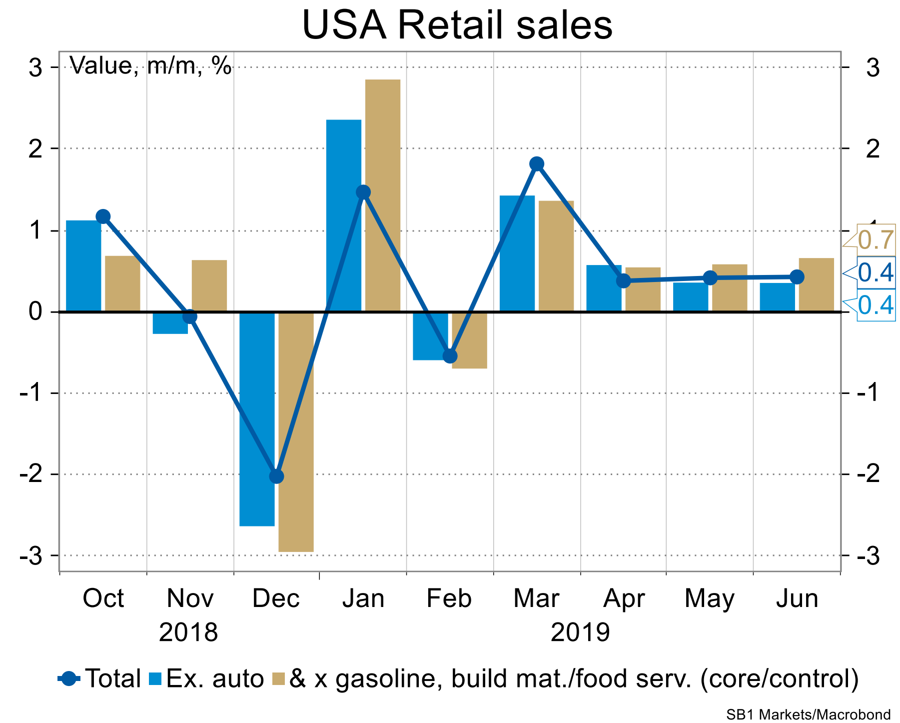


- 'Something' has probably happened since first part of June to July, amid some (hopefully) trade war progress and a strong recovery at the stock market; manufacturers are reporting a market change
  - » The order index recovered in both surveys but remain weak in NY Empire stat index
- These two surveys have been extra volatile so far in 2019. Taken face value, they indicate an 5.5 p lift in the ISM, if so the largest increase in 28 years. If we are more modest and let the two surveys indicate the level, a lift from 51.7 to 55.4

Retail sales have fully recovered; June strong, history revised up (again)

Core sales rose 0.7% in June, and the (volume) history revised up, once more, by 1.5%! Cut rates!

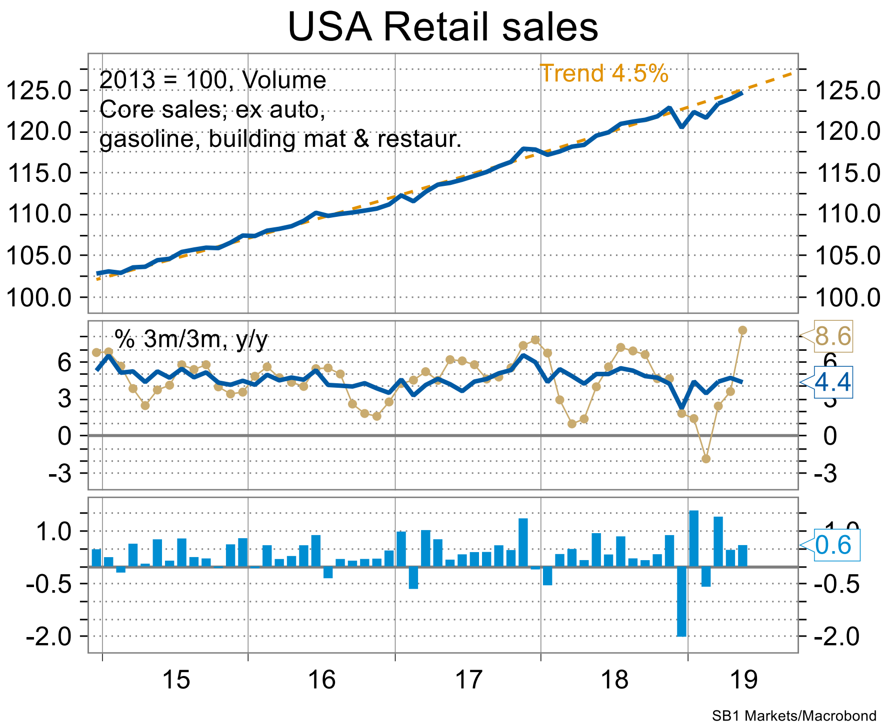




- Core retail sales (ex. auto, gas, building materials & restaurants; control group) increased by 0.7% m/m in nominal terms in June, 0.4 pp above expectations. Moreover, the sales in 2019 (in volume terms) was revised sharply up, all in all buy some 1.5%
- We estimate a 0.6% m/m volume growth in core sales, a marginal increase from the upwardly revised 0.5% in April. Given unch sales in June, core sales will have accelerated 6.6% in Q2, much better than the two previous quarters and total consumption may increase some 3%, contributing significantly to Q2 GDP growth (estimates were revised up by these figures)
  - » Consumer confidence is very strong and income and employment growth is supporting real income (and inflation subsides), and stock markets are recovering. No indications of a sudden slowdown in consumption at this point

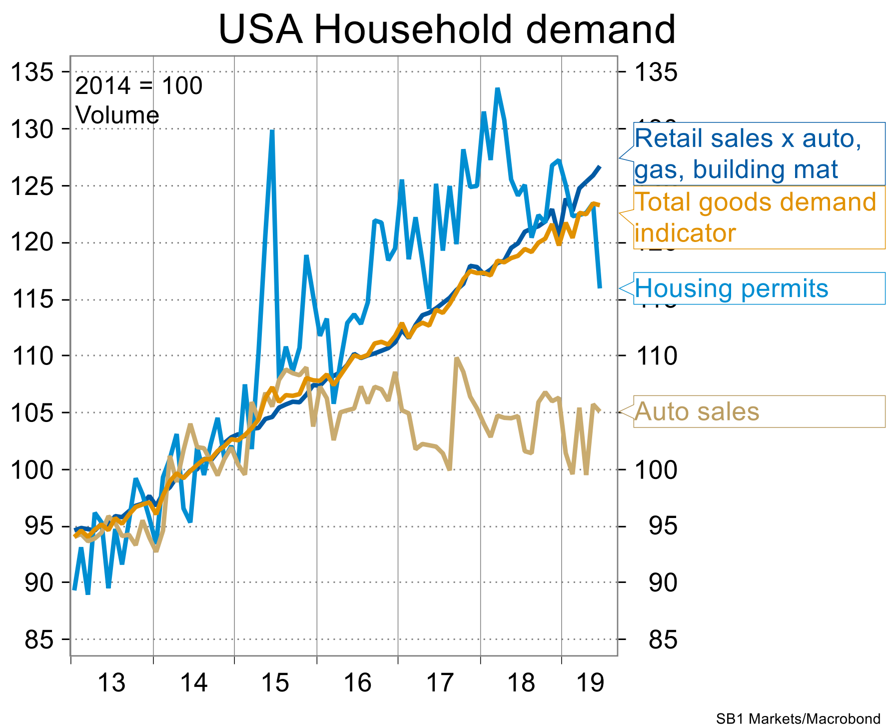
Spot the difference: This is how retail sales looked like one month ago

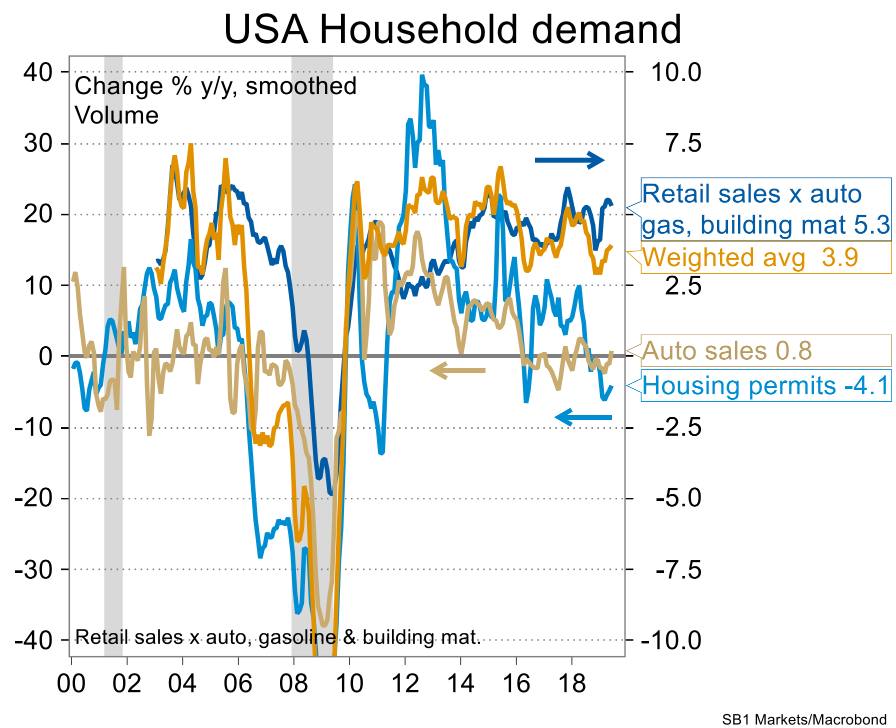
Just flip back and forth



Housing and autos have softened, retail sales not?

Total household goods demand is slowing but not by dramatically



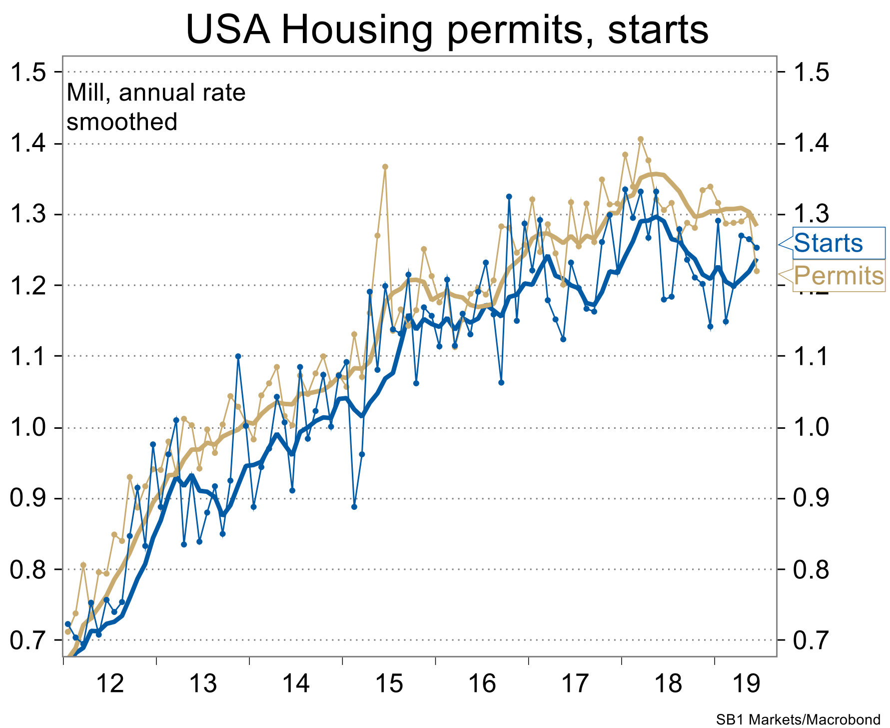


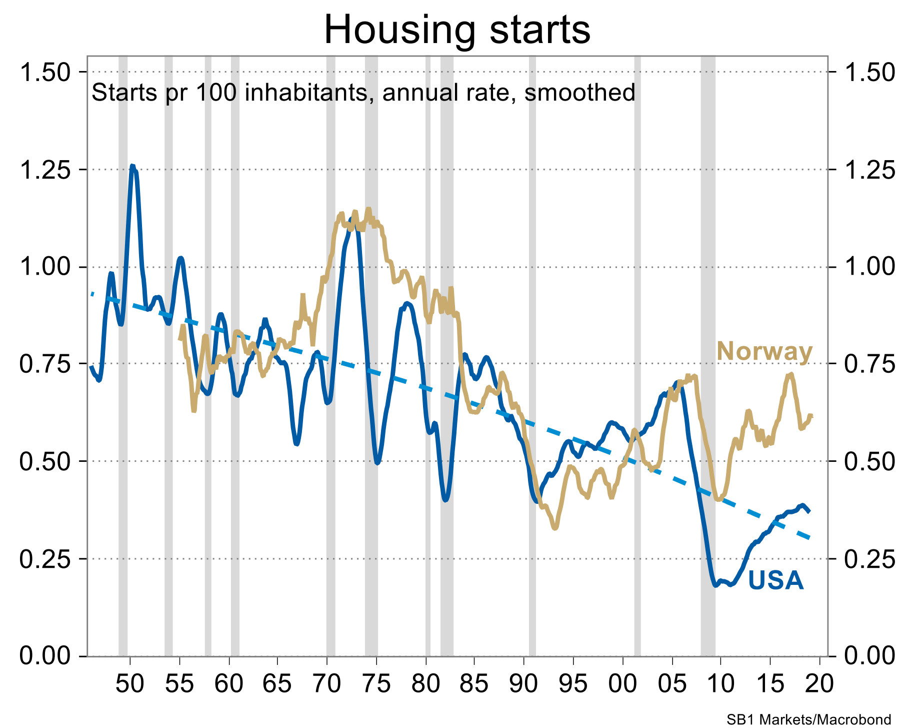
- Unemployment is very low, employment is growing, and wage inflation is above 3%, and together with lower headline inflation (until recently, at least) are generating stronger real income growth. Consumer confidence is still strong, check next page
- Retail sales are still growing a fast pace, while auto sales have flattened or is trending slowly down. The weak spot is housing activity, which peaked earlt is has slowed since e

The total household goods demand weights together core volume retail sales, auto sales & housing permits. Actual housing investments '(activity') are lagging permits/starts by some months

Housing permits sharply down, so far just in May. Starts OK, but…

The peak for both was in early 2018 – and is the sharp drop in mortgage rates



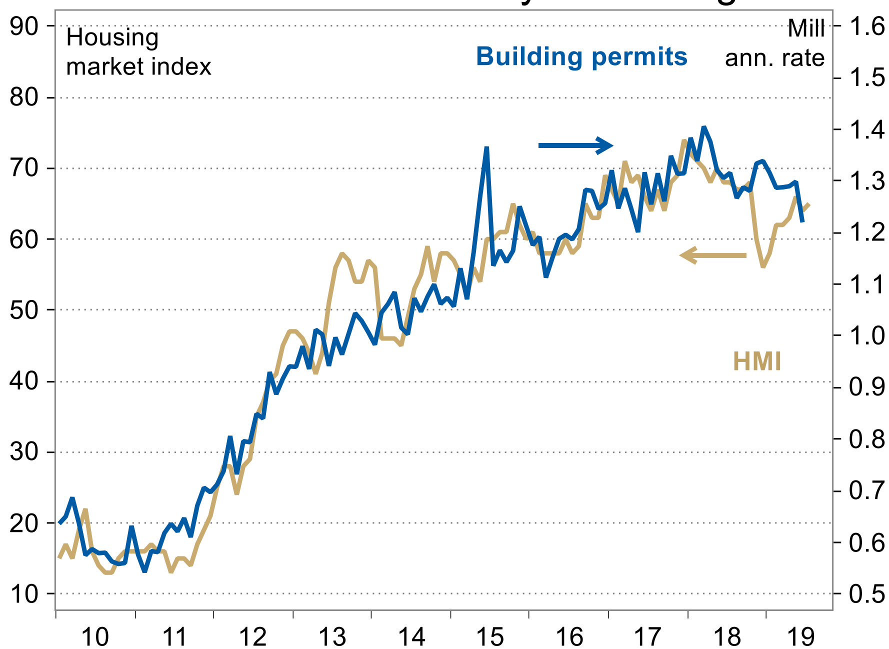


- Housing starts fell 0.9% m/m in May, to 1.253 mill (annual rate) vs expectations at 1.26 mill
- Housing permits are usually a less volatile than actual starts, and are a more useful gauge of the activity in the sector than actual starts – but this time permits fell 6.1% in June, to 1.220, expected unch. The level is the lowest since one weak month in 2016
  - » The June drop is most likely a one-off, as homebuilders have not reported any new weakness in May, June or July
- Still, there is of course a possibility that the June permit figure is correct – and even before that, both permits, starts and new home sales were heading down from the early 2018 peak. Mortgage rates have fallen sharply, and existing home sales have recovered. Is that not sufficient? Luckily, the level of housing starts is quite low, and the home construction downside is not large compared to the fall in 2006-09
  - » *New home sales will be reported this week*

Homebuilders' confidence remain solid in July

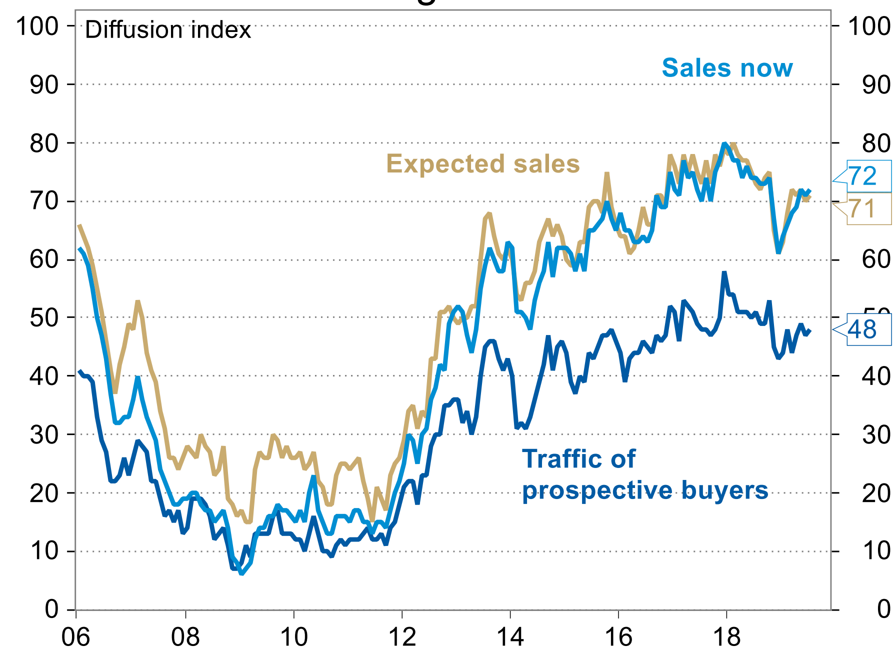
The HMI rose 1 tick in July. The index has been flat for 3 months, after a recovery, but below peak

USA Homebuilders' survey & housing starts



SB1 Markets/Macrobond

US Housing market index



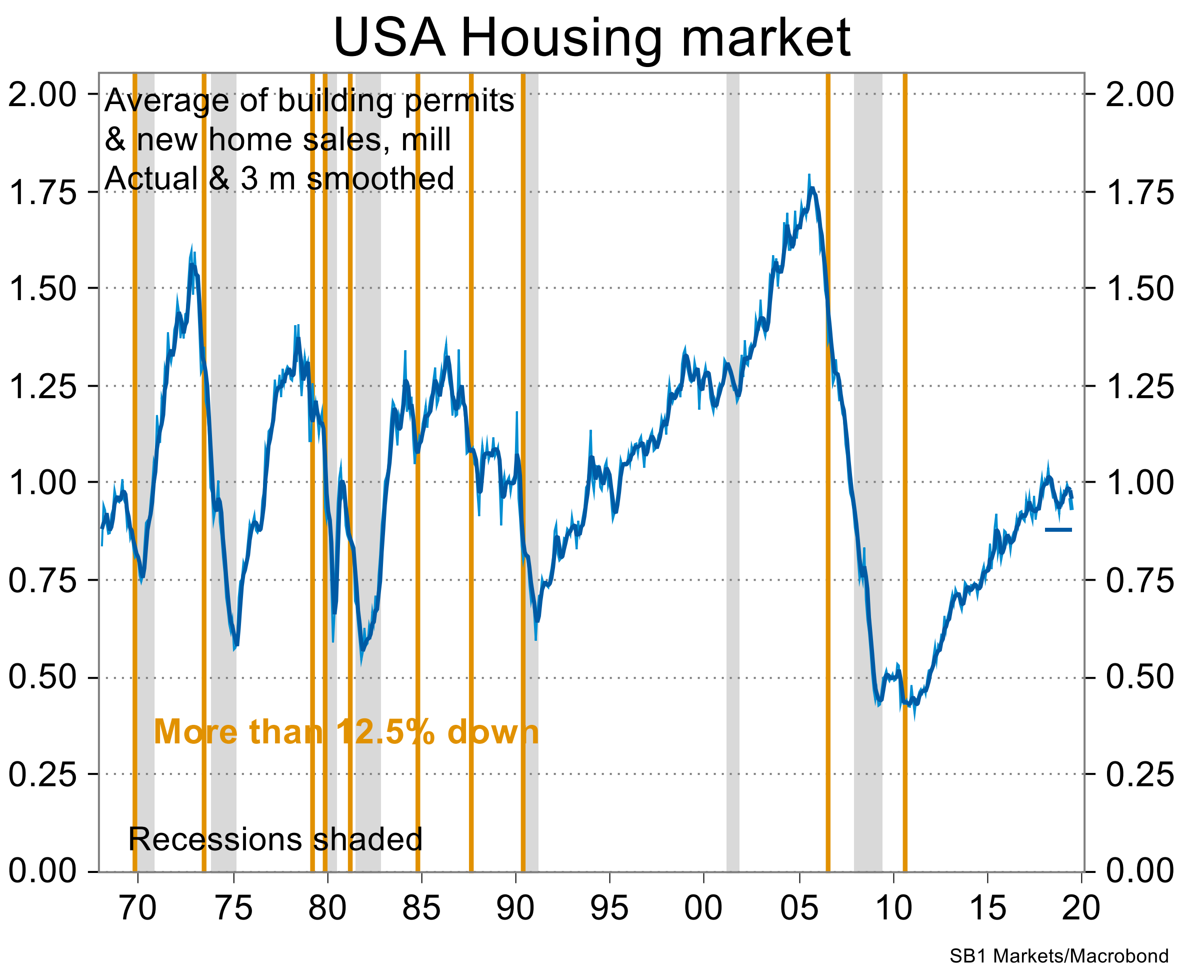
SB1 Markets/Macrobond

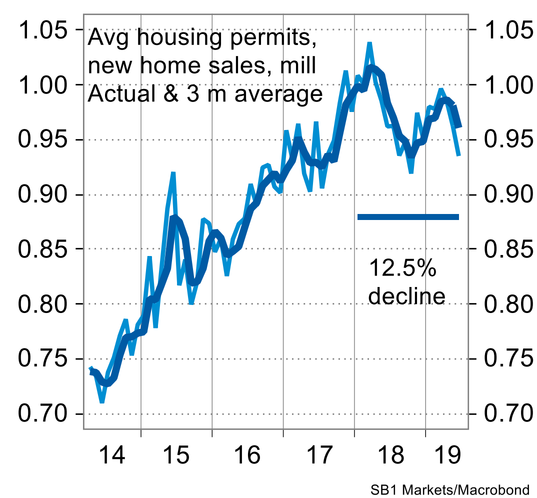
- The housing market index (HMI) rose 1 p to 65 in July, expected unch. The homebuilders have been reporting improved market conditions since January. The index is still 3 p below the Dec 18 level and 8 p below the local peak in Dec 17
  - » HMI still does not suggest any increase in building permits, the survey is pointing to a stabilization
- The homebuilders are reporting that labour shortages and rising material costs are depressing supply. At the same time, they have been noting that fewer (than one year ago) are interested in buying, and that both actual sales and expected sales are below last year's levels. So demand must have slowed during the past 18 months too

HMI is a based on a sentiment survey of US homebuilders, in which the respondents rate housing market conditions at the present time and the next six months. The index ranges from 0 to 100

Housing vs recession: Something brewing agian??

Building permits sharply down in June, still not worrisomly weak. But

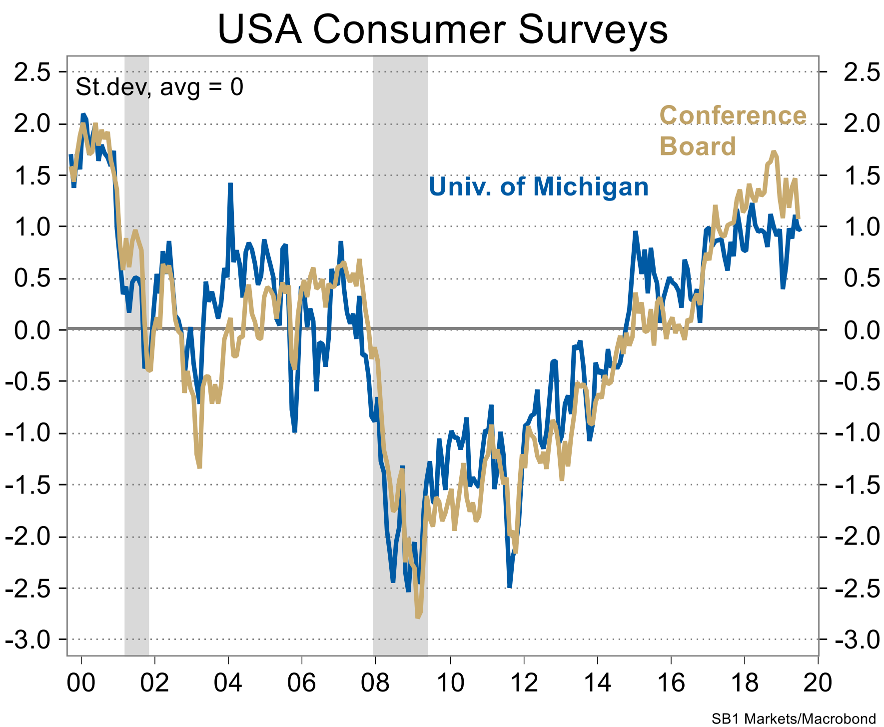


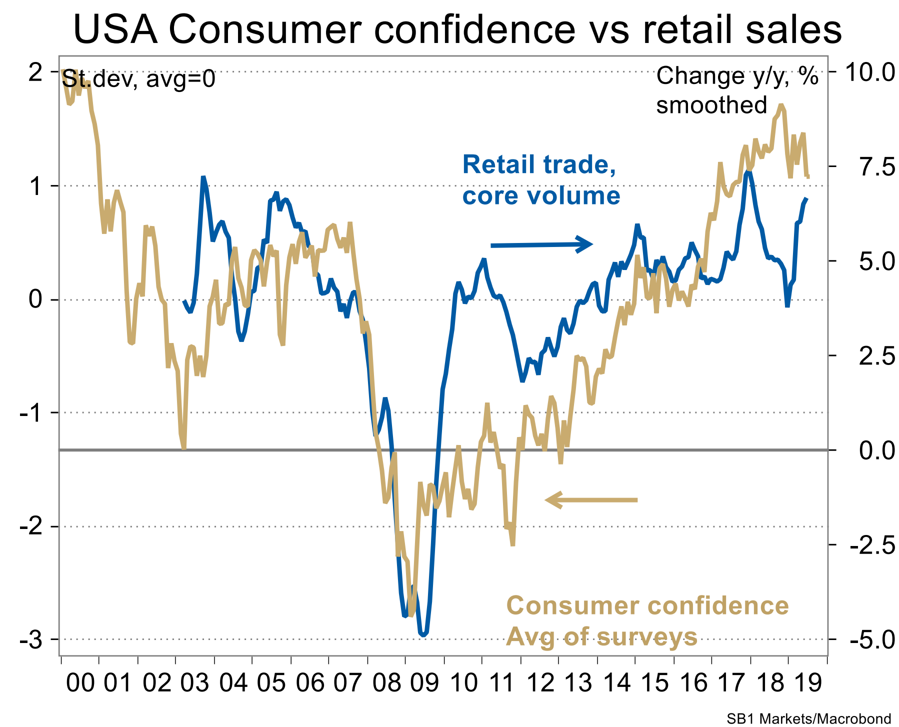


Memo: New Home sales are assumed down to 675’ in in April, in line with consensus f’cast

Michigan sentiment stable in July, level more than OK

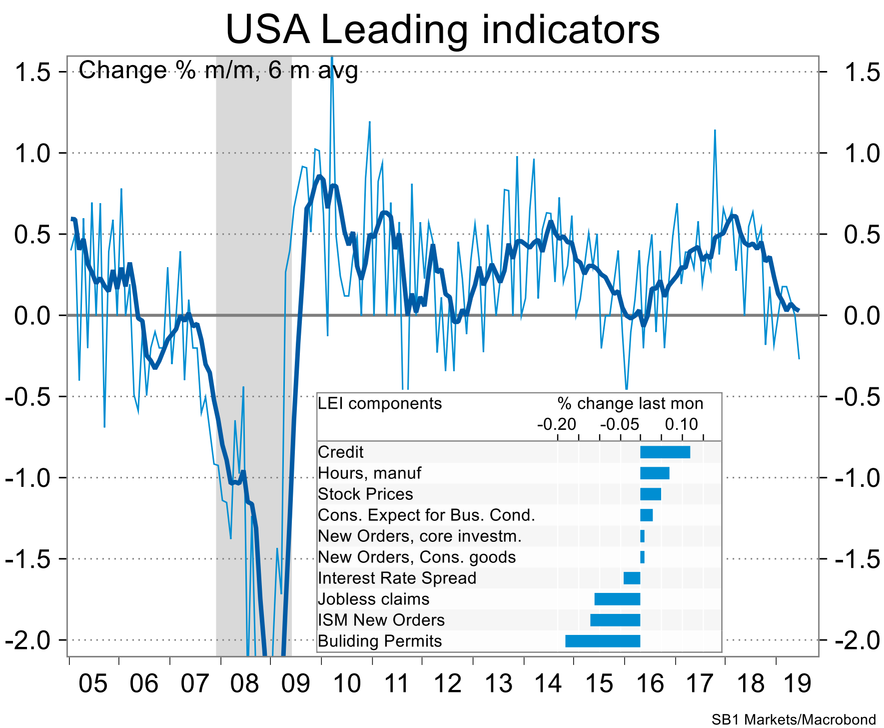
Conf. Board's confidence index fell in June, level OK, here to. Does not indicate weak household dem.

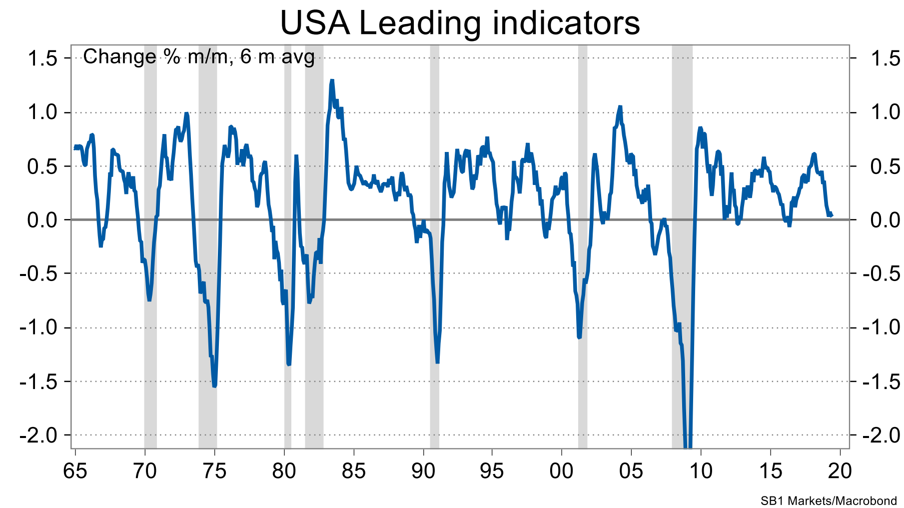


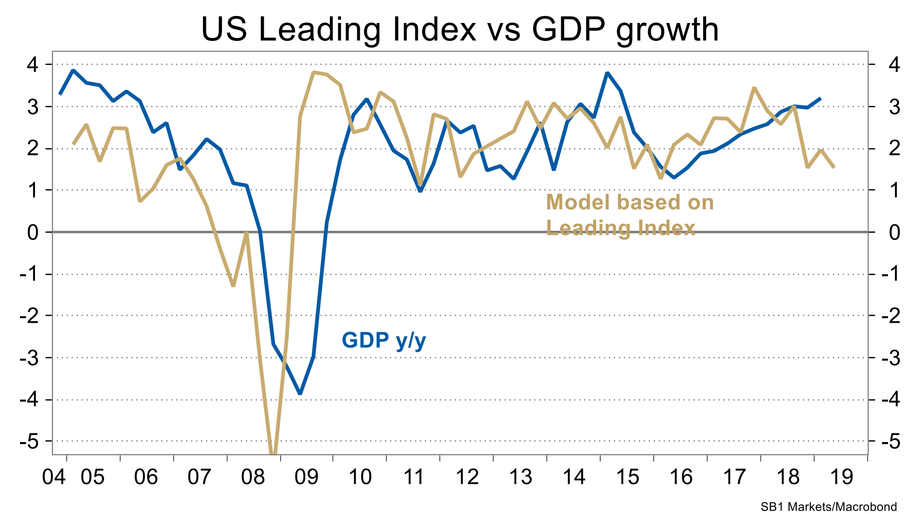


The Leading Index below par, confirms just 1.5% GDP growth

The LEI has indicated a slowdown for a long while <u>but does not signal any recession</u>





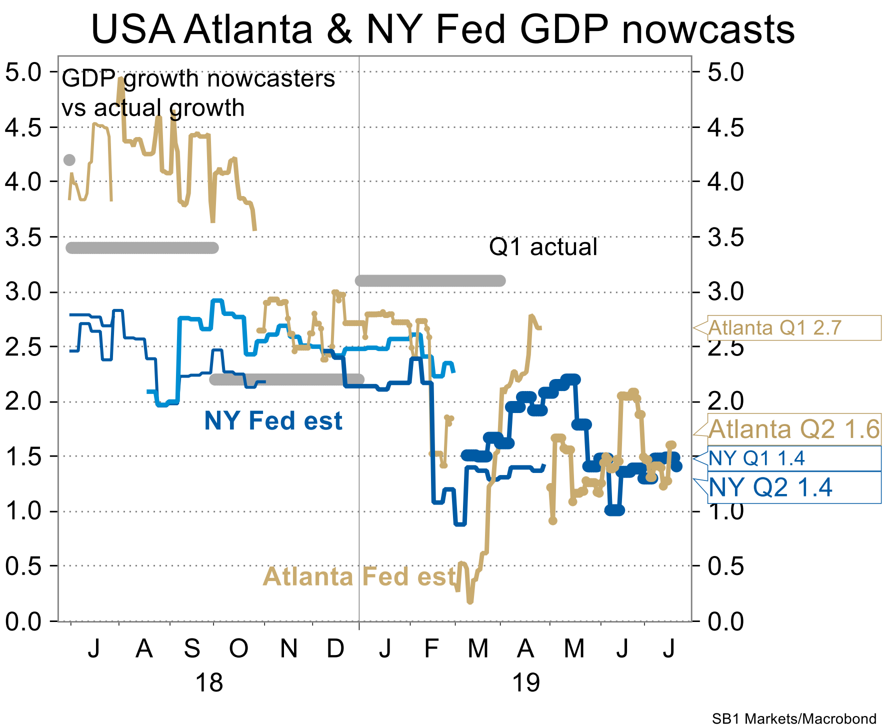


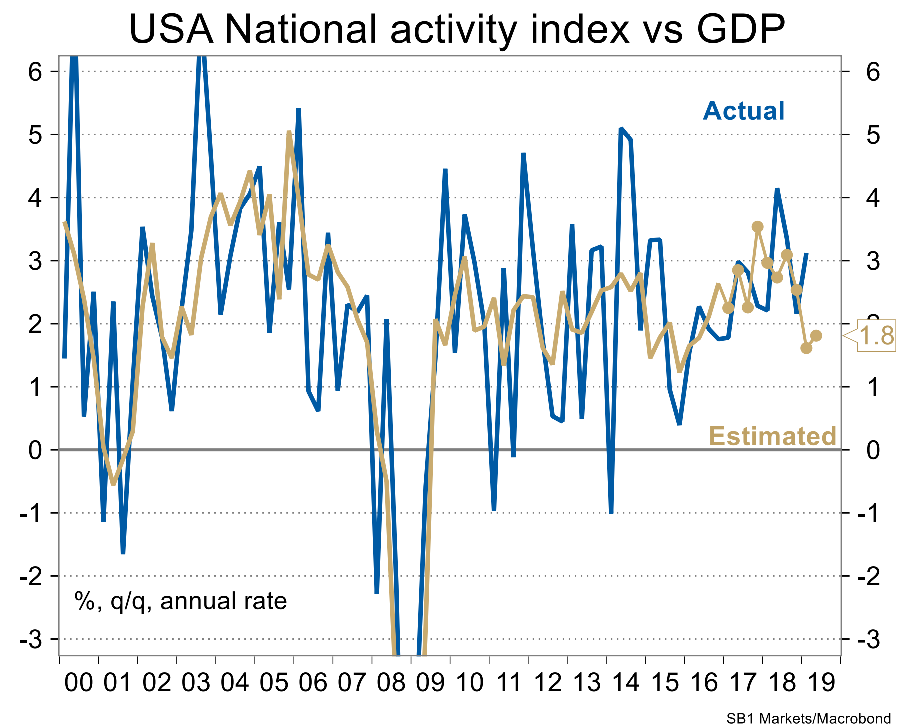
- Conference Board's Leading indicators fell 0.3% in June, expected up was unchanged m/m May, expected up 0.1%. The index has been sliding down since last spring
  - » Building permits and ISM orders contributed most on the downside. Credit spreads, stock market (+manuf hours) on the upside
- The LEI is signaling 1.5% growth, the same levels as the nowcasters are reporting for Q2

Conference Board's Leading Index (LEI) is a composite index based on ten already published leading indicators that are judged to be leading the overall cycle

Fed nowcasters say 1.4 – 1.6% in Q2

The National activity index signalled 1.8% Q2 growth in May (up from the 1.1% April est)



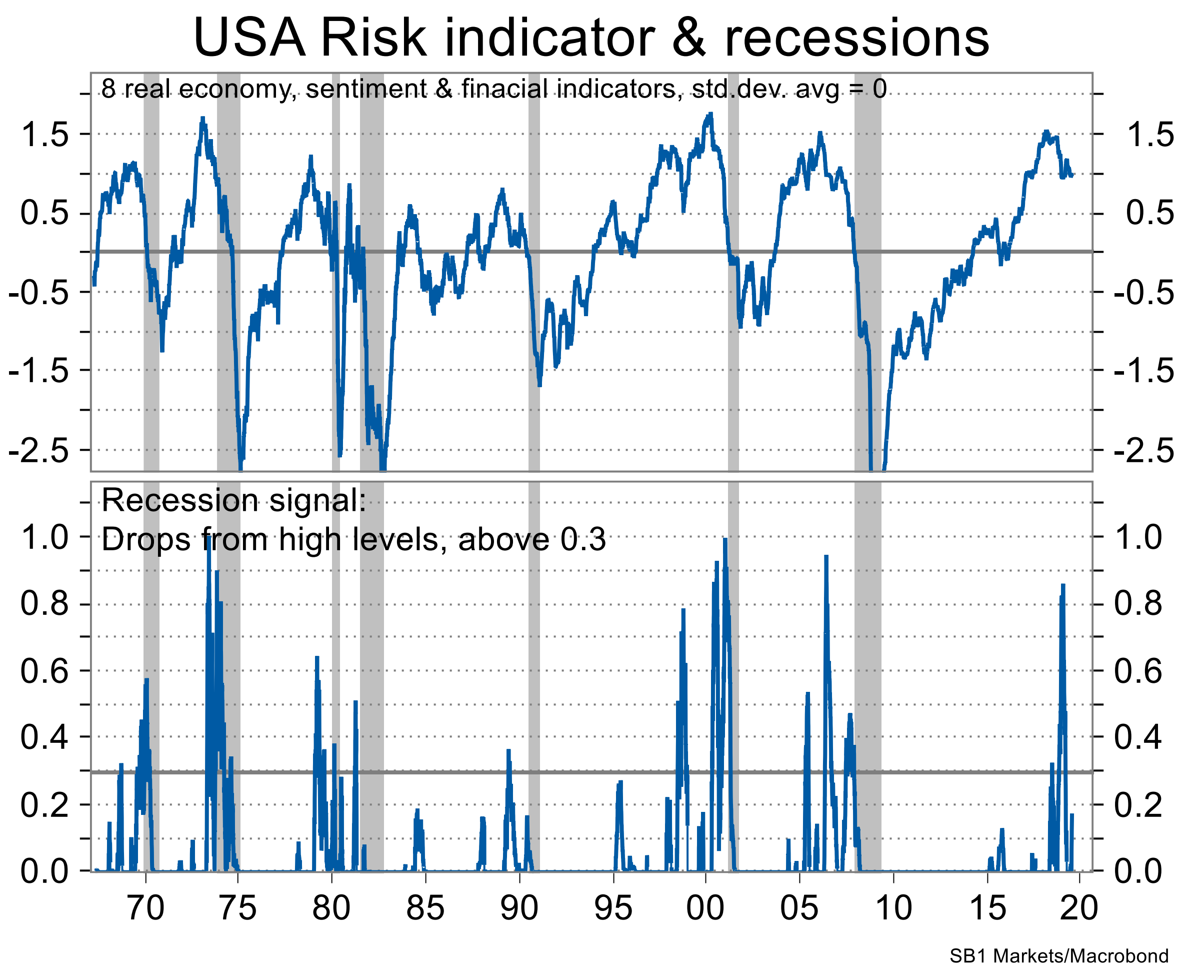


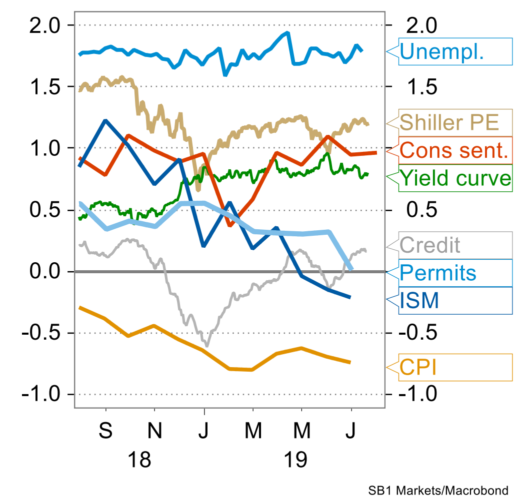
- However, a lot of data has still to be reported – and the nowcasters often miss the target (and they change their mind through to the quarter)

dd

US Indicators: Not a recession warning, now

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

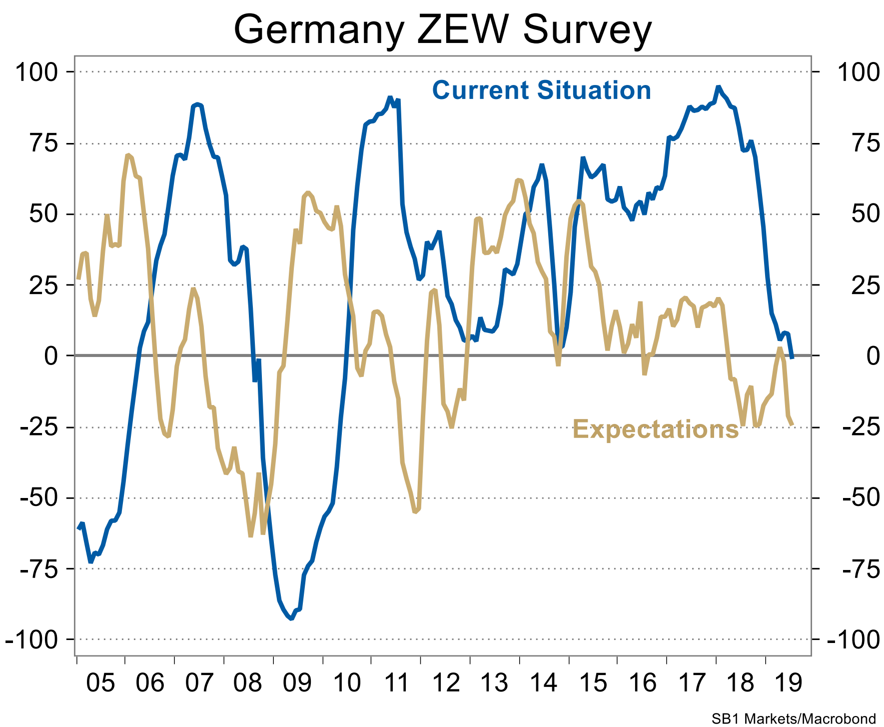


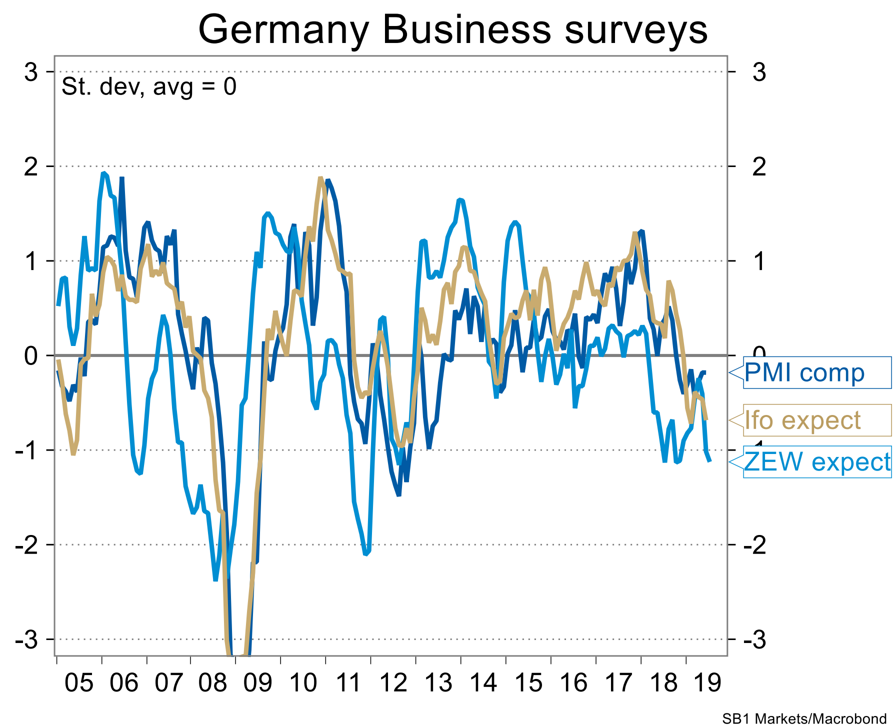


Inspired by Goldman Sachs Bull/Bear indicator. We are using jobless claims instead of unemployment, and have added housing starts, consumer sentiment, and a credit spread. In average, our Risk or Good Times Indicator leads recession starts by 18 months. The lower panel above shows changes in the squared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

ZEW survey expectations further down, current situation weaker too

The subpar domestic data flow and the intensified trade dispute darken the economic outlook



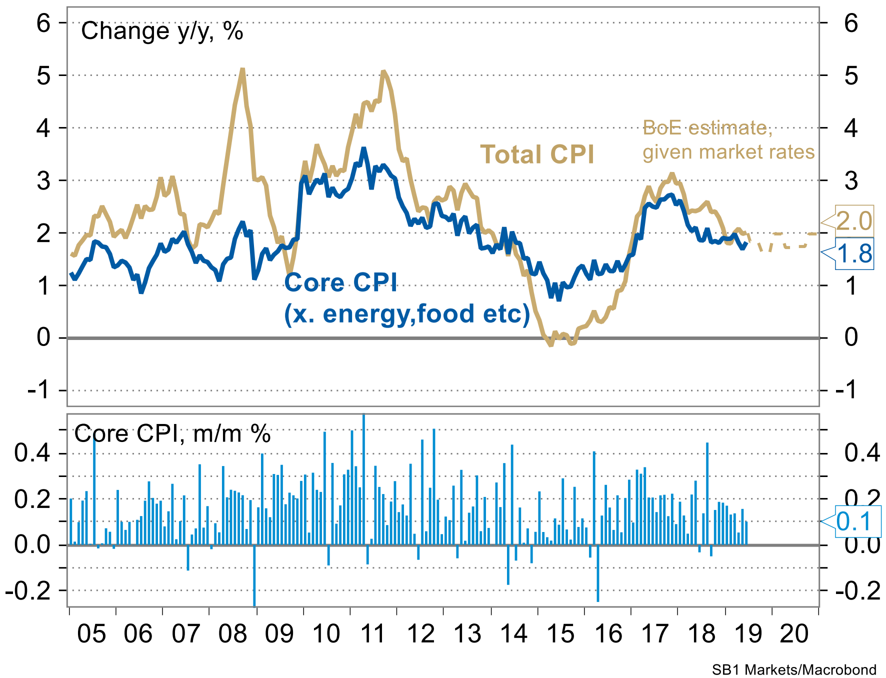


- Expectations in the German ZEW survey fell further 3 p following the large 19 p drop in June, and the level is far below average (but still not lower than some slack months last year). The assessment of the current situation fell too, down to an average level.
  - » The ZEW survey points grim Q2 growth. The ZEW is a sentiment survey among economists and analysts, not a business survey, and is usually leading the Ifo and PMI by a wide margin – however with a rather weak correlation
- All German surveys are pointing to a rather bleak outlook. The ZEW sentiment survey has been the weakest recently, we prefer the PMI and Ifo, as these are business surveys and better correlated to actual growth

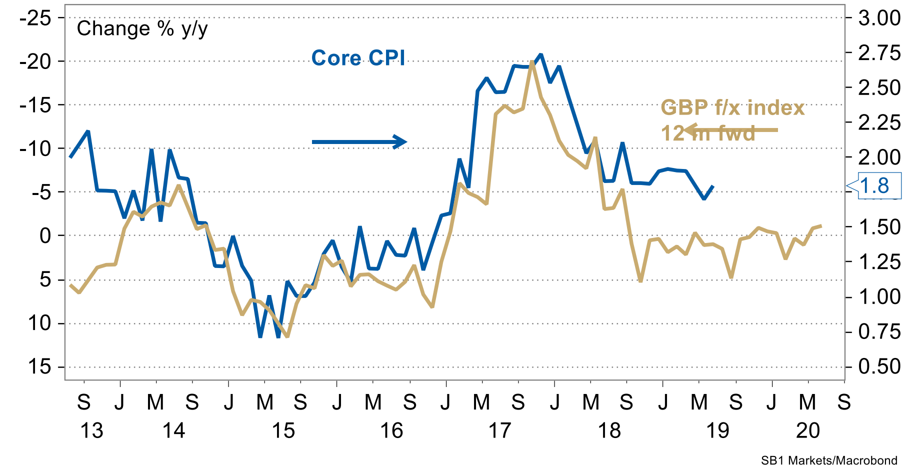
Core CPI inflation ticked up to 1.8%, total inflation have probably bottomed

The GBP impact is probably soon taken out, core inflation close to target

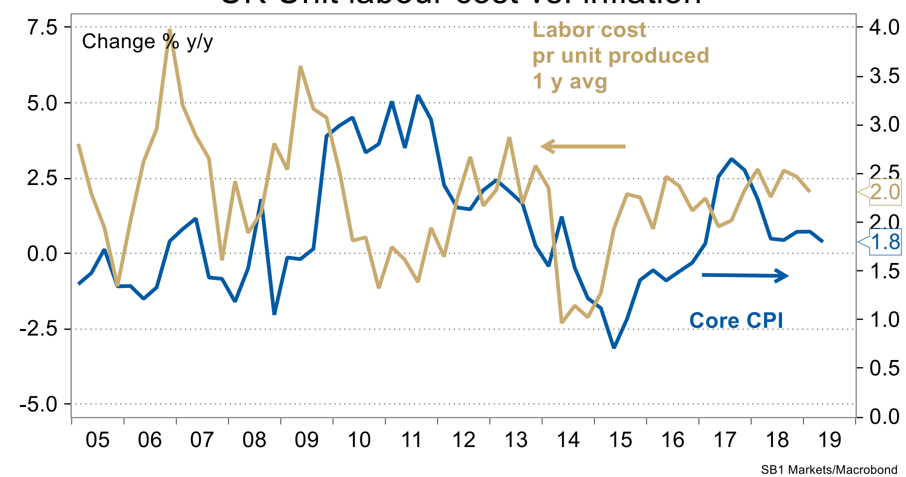
UK CPI



UK CPI vs. GBP



UK Unit labour cost vs. inflation

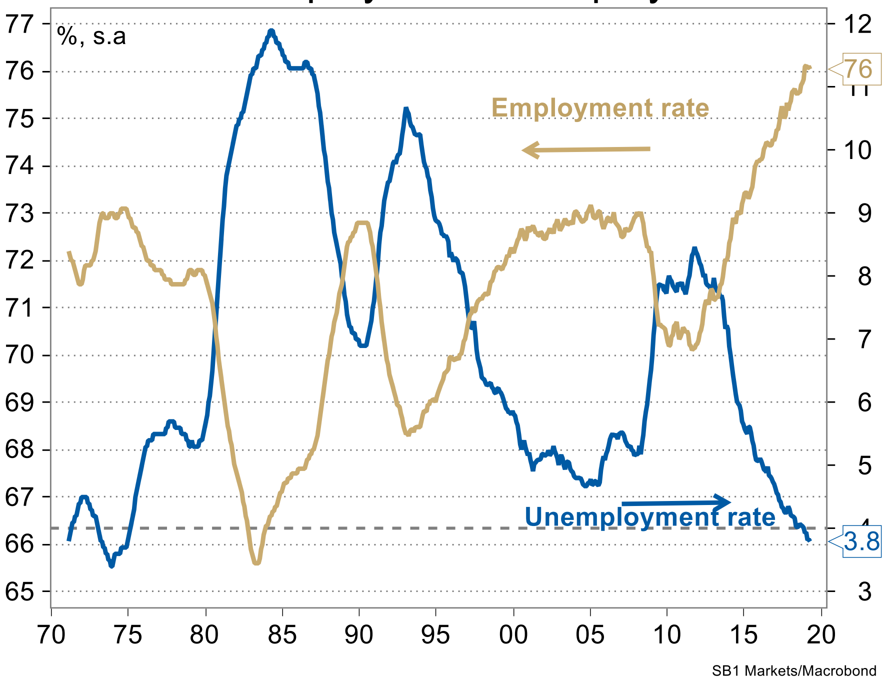


- Core CPI inflation +0.1 p up to 1.8% in June. Core inflation may still be trending slowly down but is not far from BoE's price target of 2%. Total inflation flat at 2.0%, stabilising the past 4 months
- Inflation came down through 2018, as the upward pressure from the GBP depreciation in 2016 changed sign. Our simple f/x based model still may still point to lower CPI inflation. However, <u>domestic costs are are not low, and wage inflation has climbed to close to 4%</u>

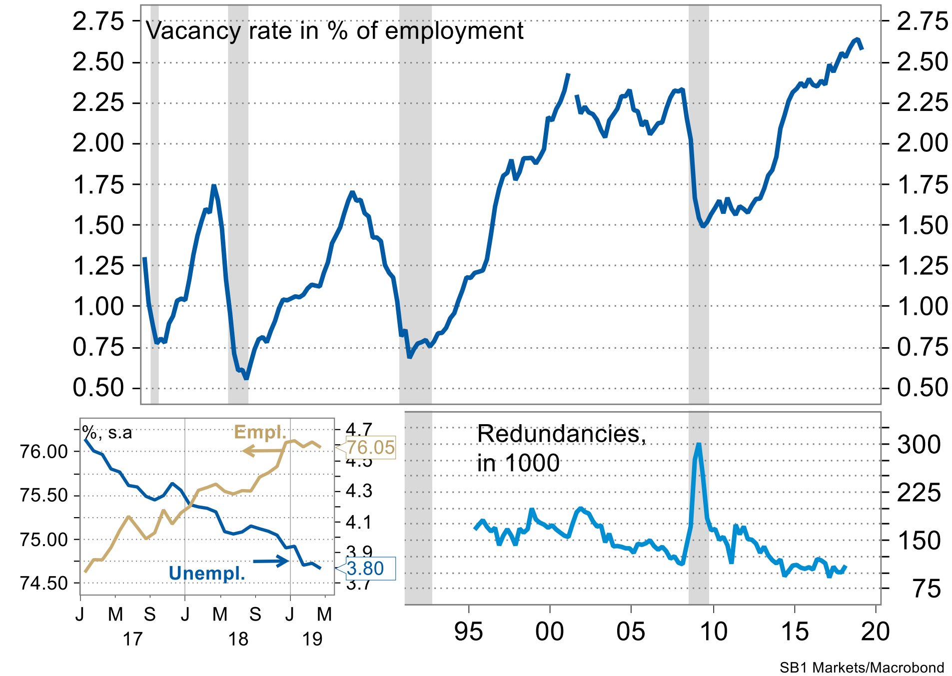
Unemployment flat at 3.8%, employment has been soaring, rising wage growth

Tight labour market; unemployment at 44 y low, high empl. & job vacancies and wages are climbing

UK Unemployment & Employment



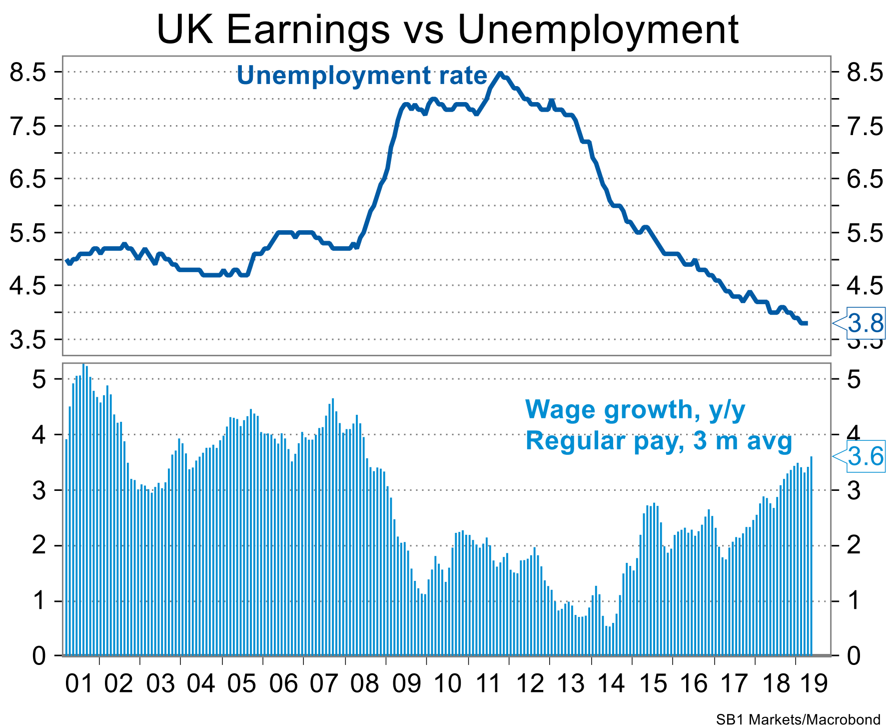
UK Job Vacancies

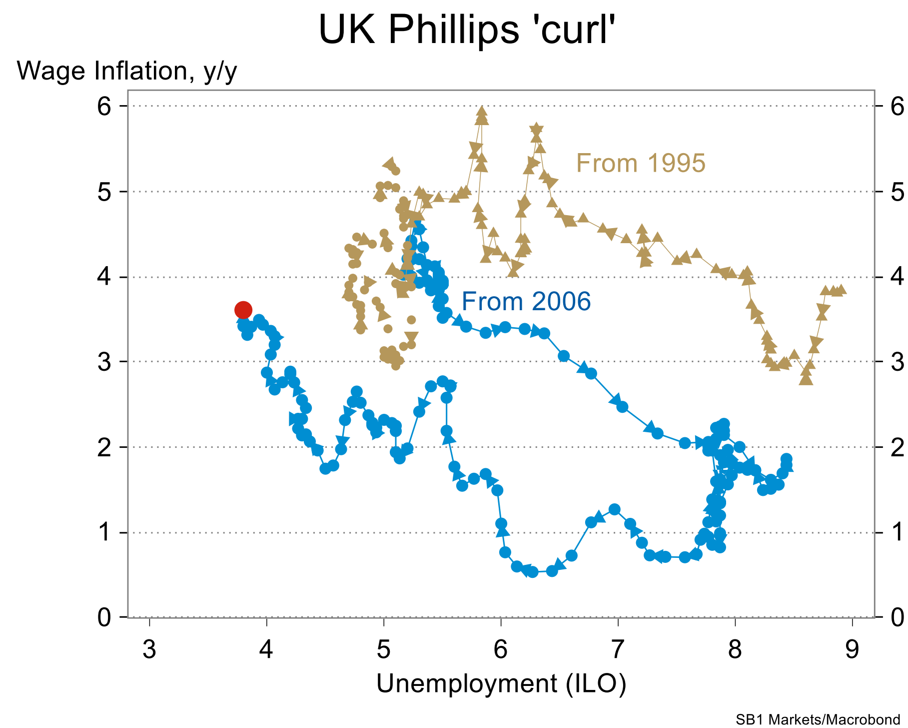


- Unemployment (LFS/ILO) was unchanged at 3.8% in April (avg March-May). The unemployment rate is the lowest since 1975
- The employment rate fell 0.1 pp to 76.0%, from the highest level ever (data back to 1971). The rate has flattened somewhat recently
- The number of job vacancies has fallen marginally recent months but is still close to a record-high level
- No surprise, wage inflation is trending up, and is approaching 4%. Wages are outpacing CPI inflation, total inflation has come down to 2.0%

A tight labour market is boosting wage inflation, now close to 4%

The Phillips curve is not dead, just bit lower/less steep than normal

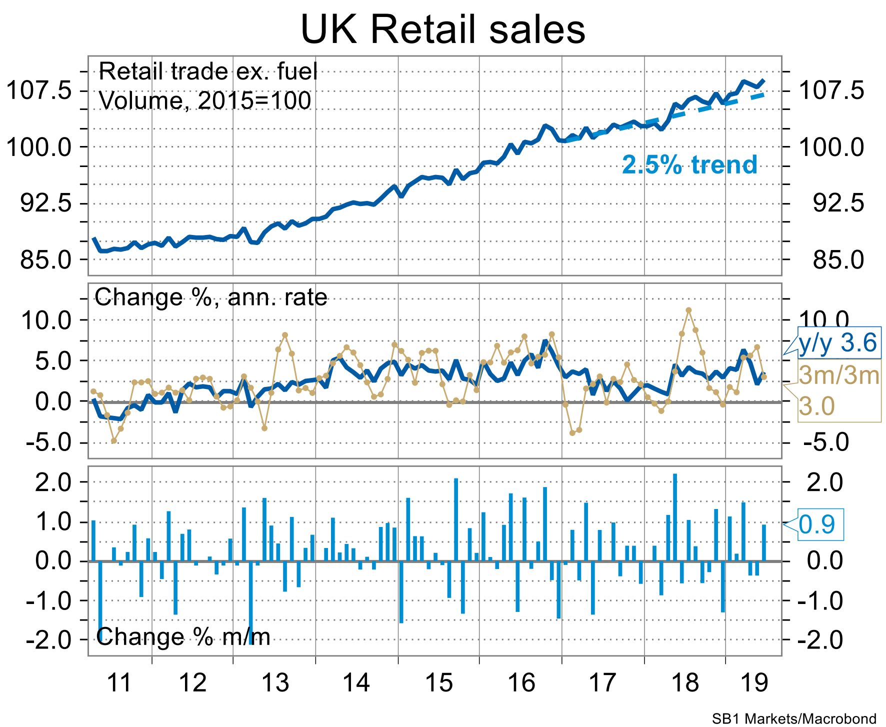


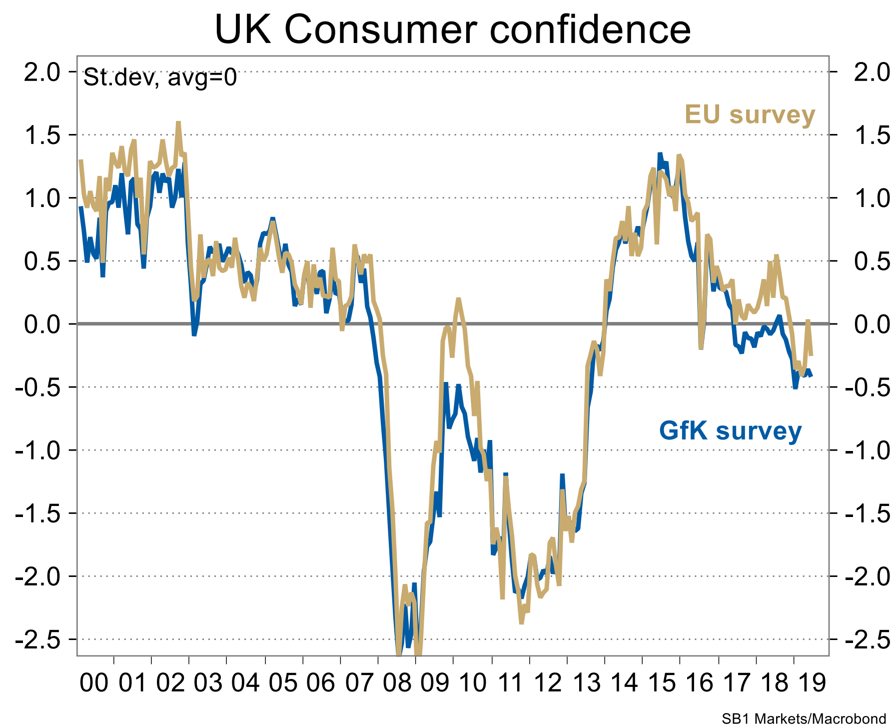


- Wage growth surprisingly surged to 4% y/y (regular pay, revised up from 3.8%), and stayed at 3.8% in June, lifting the 3 m avg to 3.6%, the highest in more than 10 years. (Next month the 3 m average will most likely be even higher, even if underlying growth last months has slowed marginally)
- UK productivity growth is very low, still well below 1%, and unit labour cost inflation is running well above the inflation target. Either will inflation become too high or corporate profits will take a hit

Retail sales are still strong

Sales up 0.9% in June, much better than expected amid falling consumer confidence

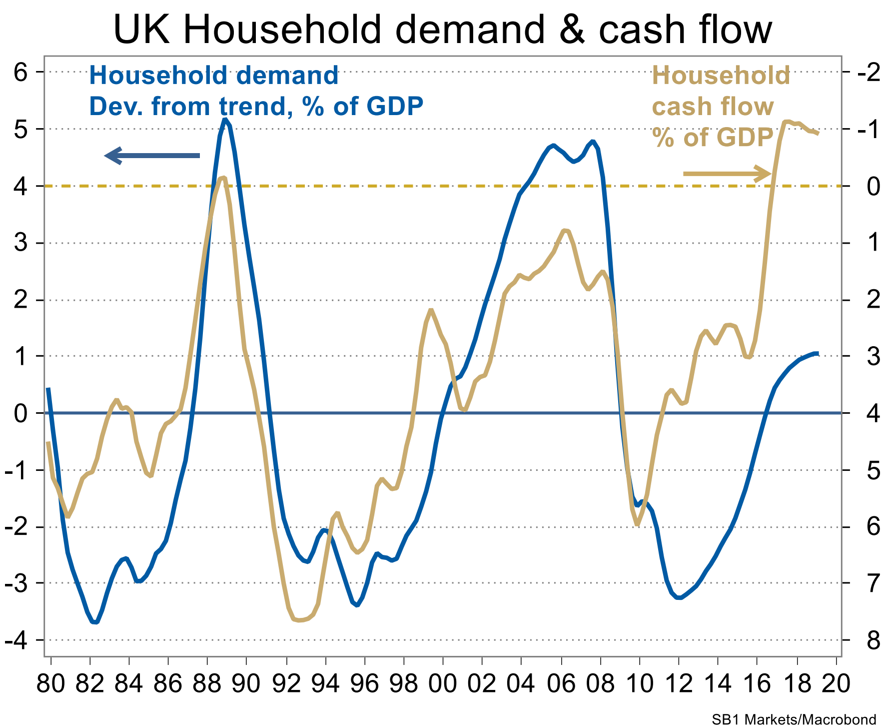


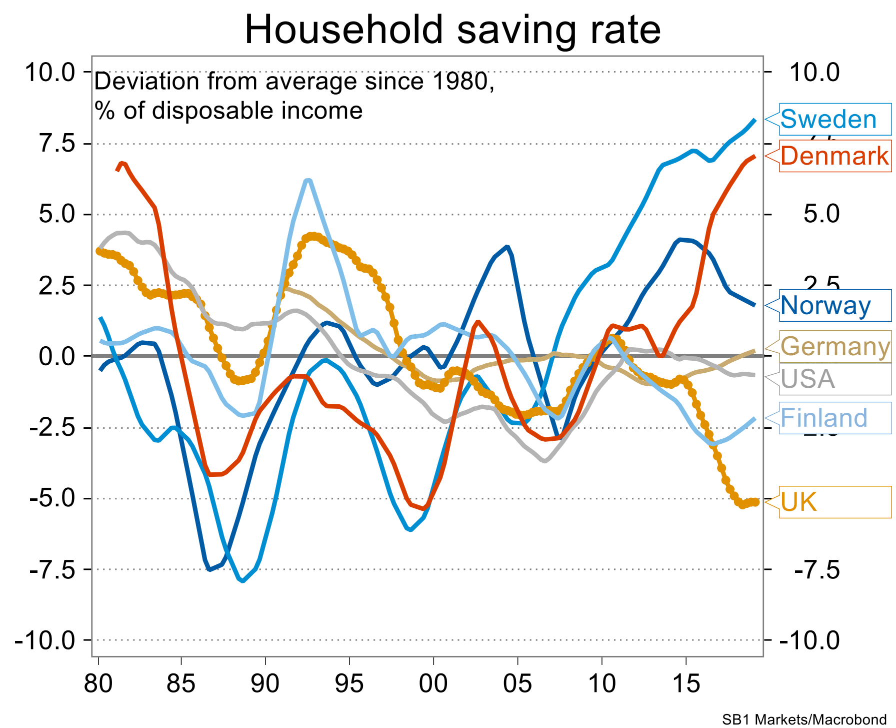


- Sales fell inn both April and May but the February level was high and June sales are well above the 2.5% trend path, with Q2 growth at 3% and 3.6% y/y in June . Still, GDP growth was probably weak in Q2, partly due to less sockbuilding
- Record high employment and rising real wages are helpful. However, over the recent years, consumption has been fuelled by a sharp decline in household savings. Given the drop in savings, the risk is on the downside
- Consumer confidence surveys have fallen substantially, which is no surprise, given the Brexit turmoil. Both the GfK survey and the EU survey are well below par but have stabilised recent months

Households are not saving anymore, even without any huge demand boom…

The UK saving trend is bad, savings have fallen sharply recent years, and the cash flow is now negative



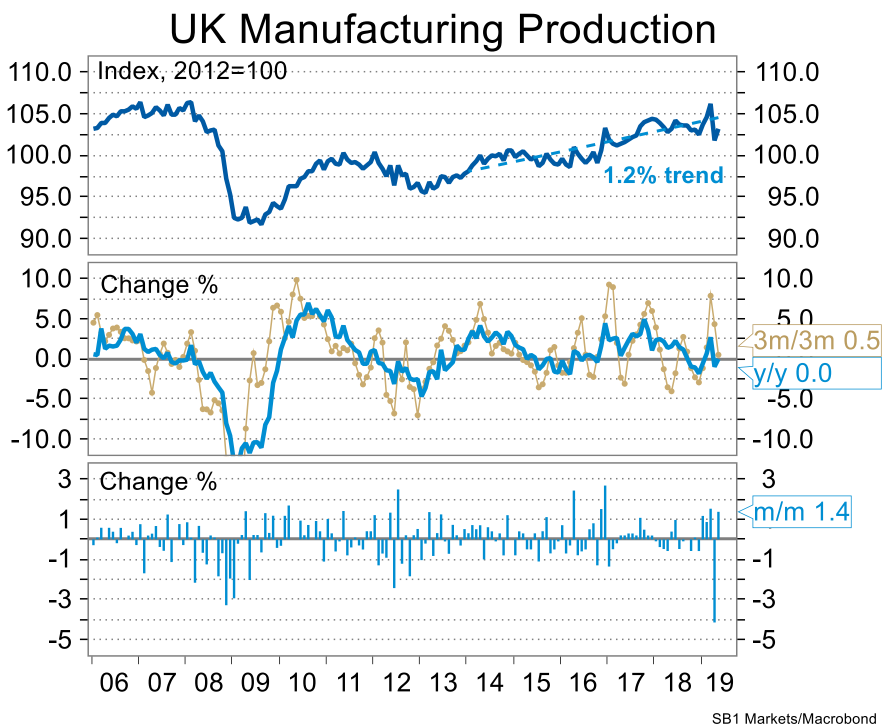


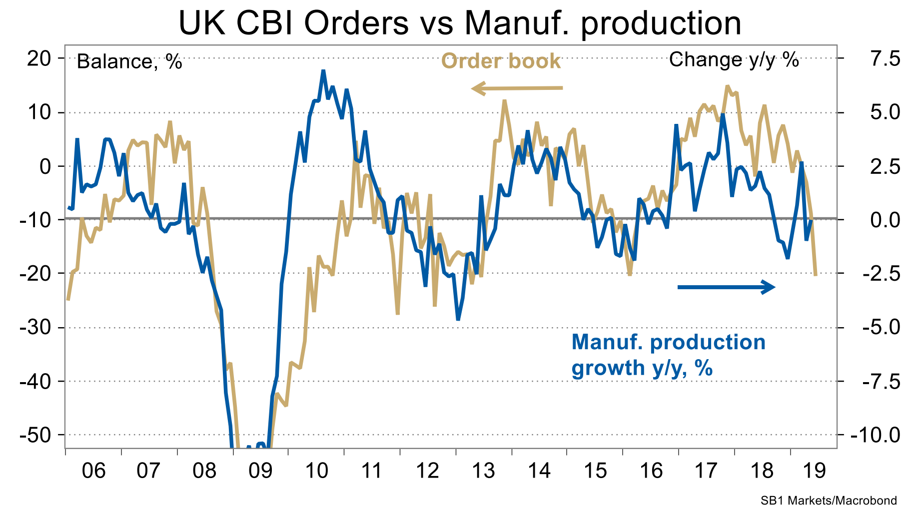
A rather scary picture, both short and long term. Short term: A substantial risk for a savings shock, sending the UK into recession

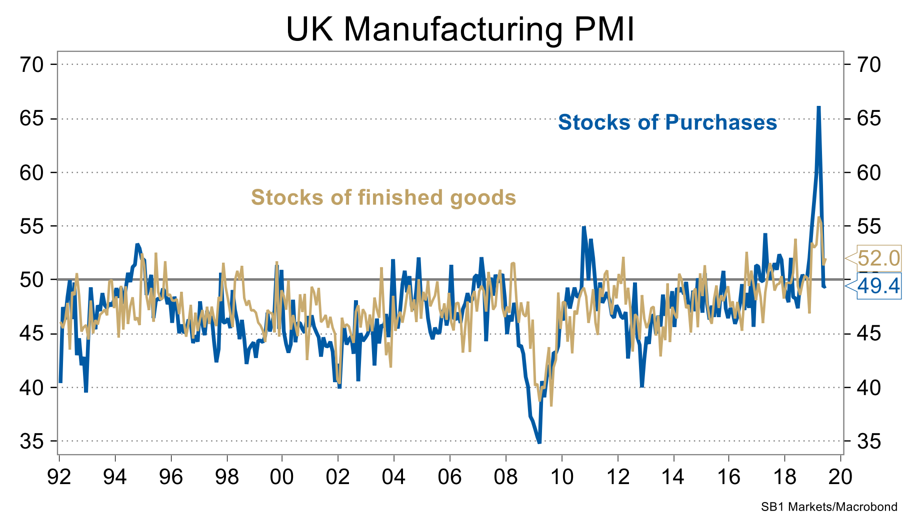
- The savings rate has fallen 4 pp since late 2015. The brits have compensated slow income growth by cutting savings in order to keep consumption up – which have 'saved' the British economy, demand wise, recent years
- The household sector's cash flow has fallen into negative territory, for the first time since 1988, this time without any huge spending boom, just a small one. This illustrates the mush slower income generation capacity in the UK economy, due to very low productivity growth. Employment growth has been decent, and the employment ratio is record high but that has still not been enough to fund spending.

Manufacturing production remained at a low level in May

Production rose just 1.4% m/m, following the 4.1% cut in April (from a high level in March, though)



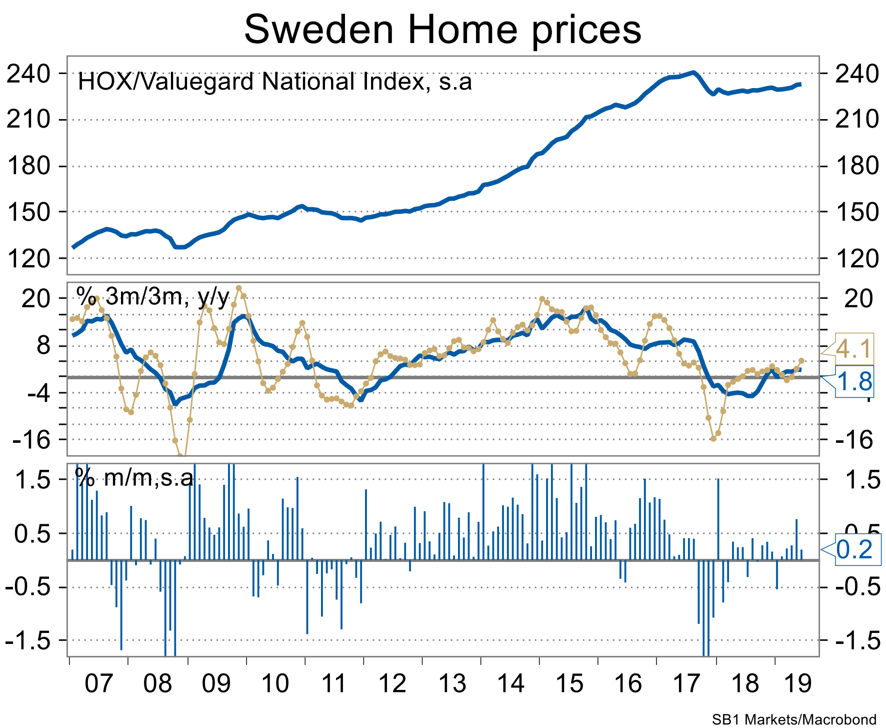


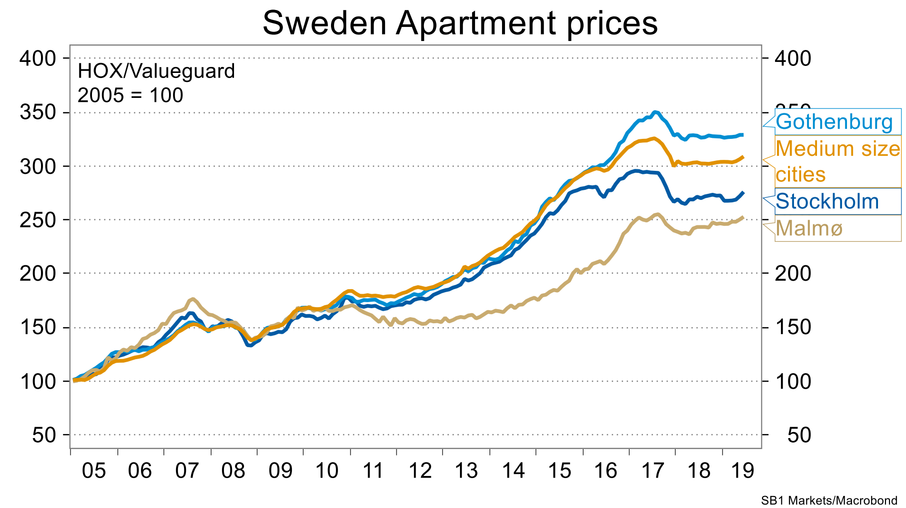


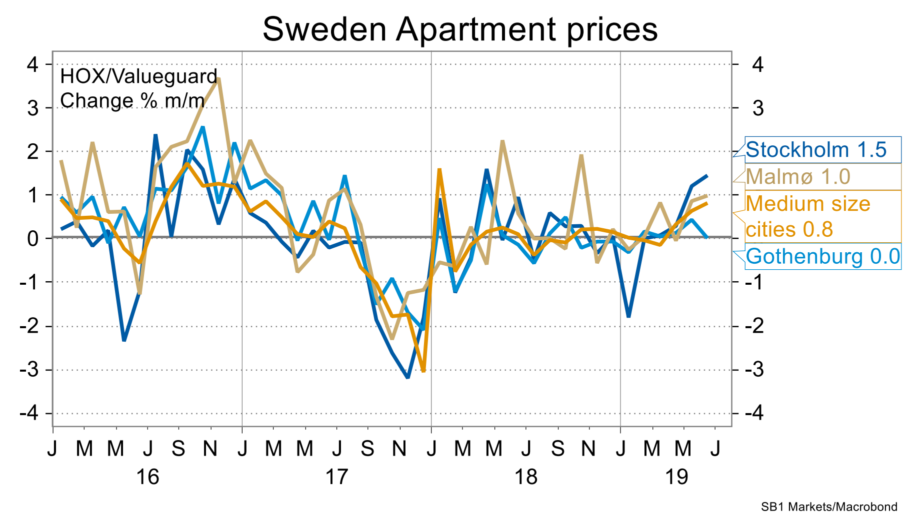
- Production was 'artificially' high in March, before the assumed Brexit date, March 30. Inventories were build sharply up. Production is now flat y/y
- Inventories are probably not yet cut (according to PMI, the inventory indices were still above average, in June, but growth has surely slowed sharply (thus, inventories will be a large drag on growth in Q2, following the unprecedented positive contribution in Q1)
- All activity surveys have turned south recent months, and the production outlook is bleak, as it is many other places

House prices on the way up again

Prices rose ‘just’ 0.2% m/m in May, but prices have recovered recent months



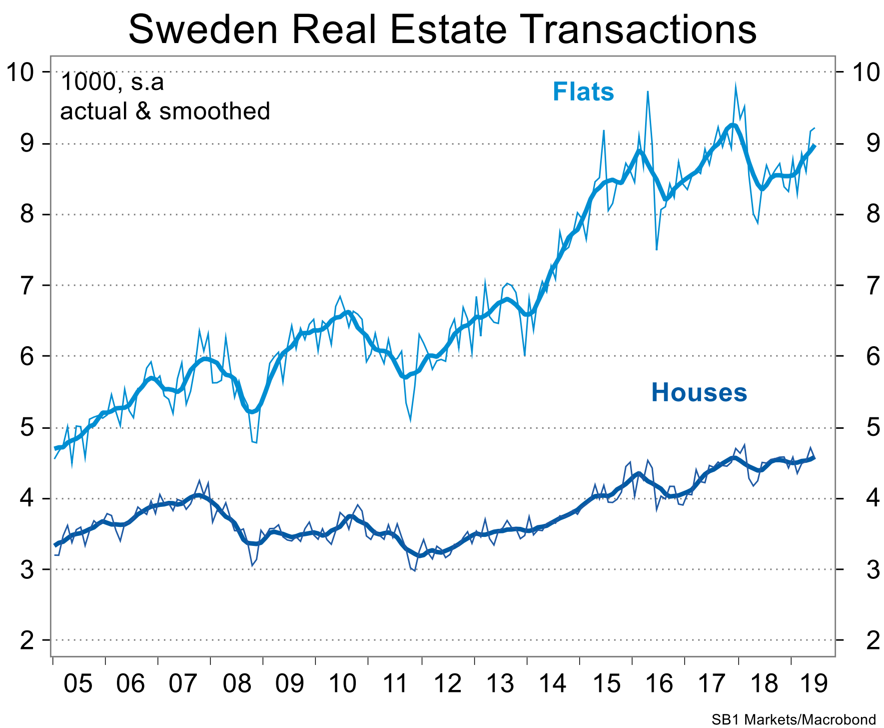


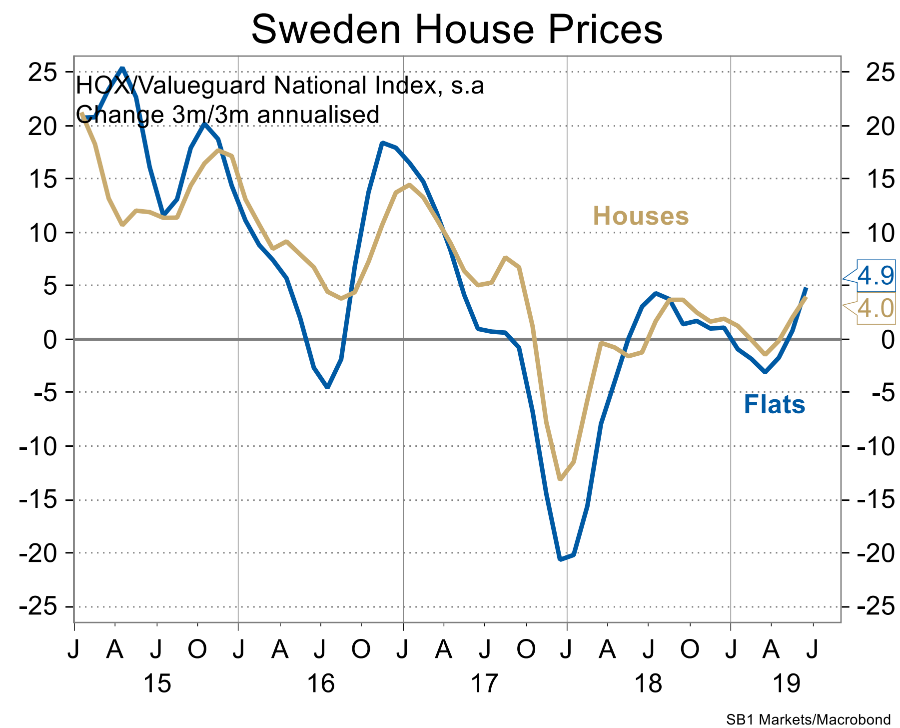


- Home prices rose 0.2% m/m seas. adj. in June, following the 0.8% jump in May. Prices are up 4.1% 3m/3m, and 1.8% y/y. Prices are still low then before the late 2017 setback and real prices are significantly down
  - » Apartment prices in Stockholm rose 1.2% in May, and another 1.5% in June! Still, St.h prices are just up 1.7% y/y. Gothenburg flat m/m in June, and are close to flat y/y too.
- The number of transactions has increased recent months, check next page. The housing market is back on track?

Apartment sales have recovered too

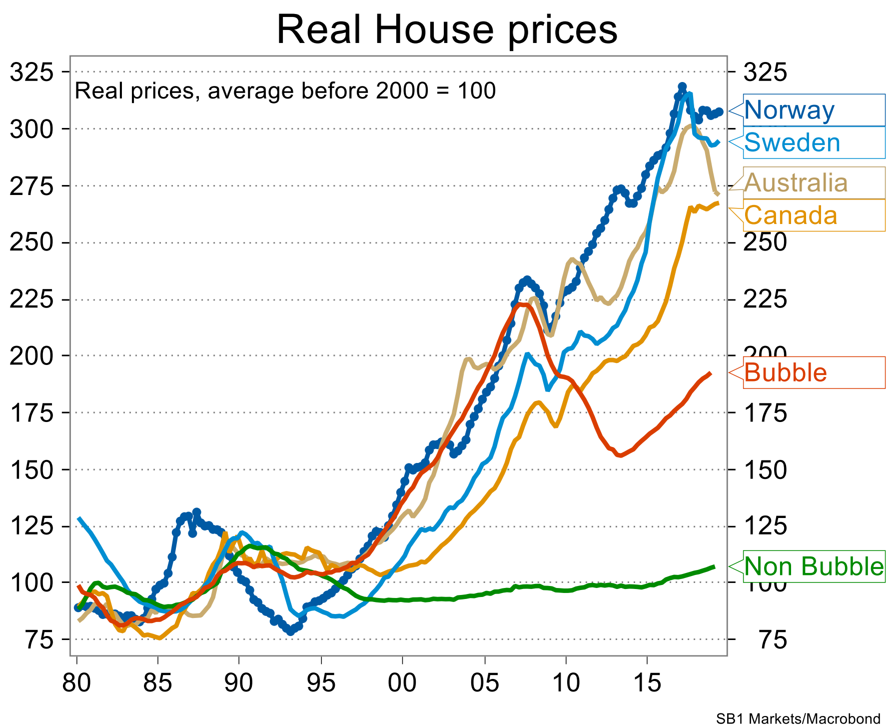
Sales fell last year, have recovered most of the decline now. House sales flattish, record high

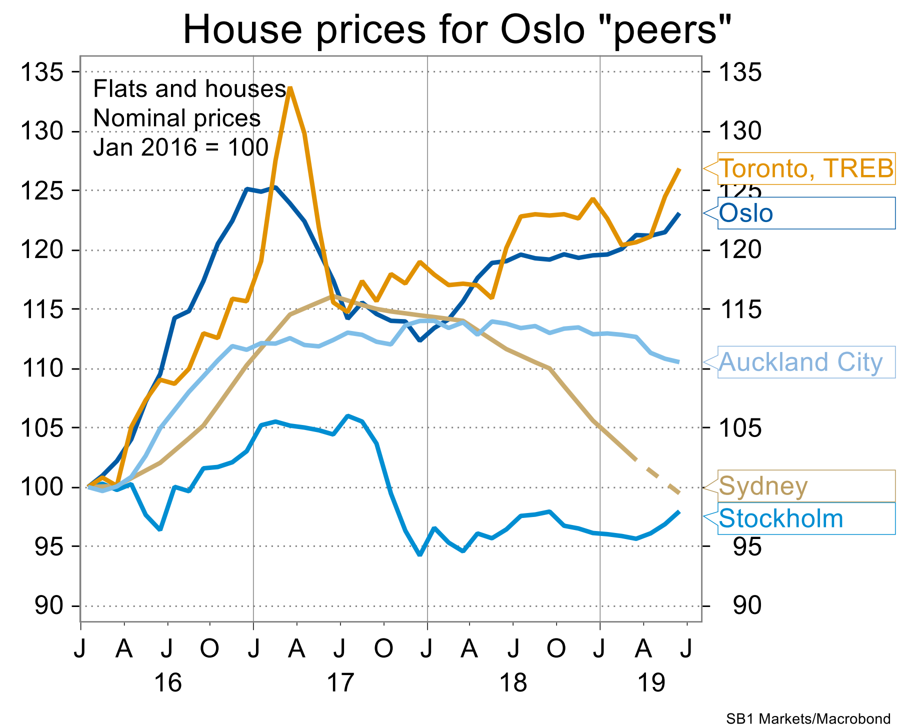




Real home prices have fallen/flattened out in all supercycle countries

Sweden down 7% in real terms, Norway 4% and Australia 10%, Canada flat





- Mixed among the super cycle guys recently: Oslo is slowly on the way up again, Stockholm flat (and slightly up most recently), Toronto more or less flat, after a comeback in May. Auckland is trending down and Sydney is falling steeply, down 12% from the peak in Q2 2017, in nominal terms!
- 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

SpareBank 1 MARKETS

Highlights

The world around us

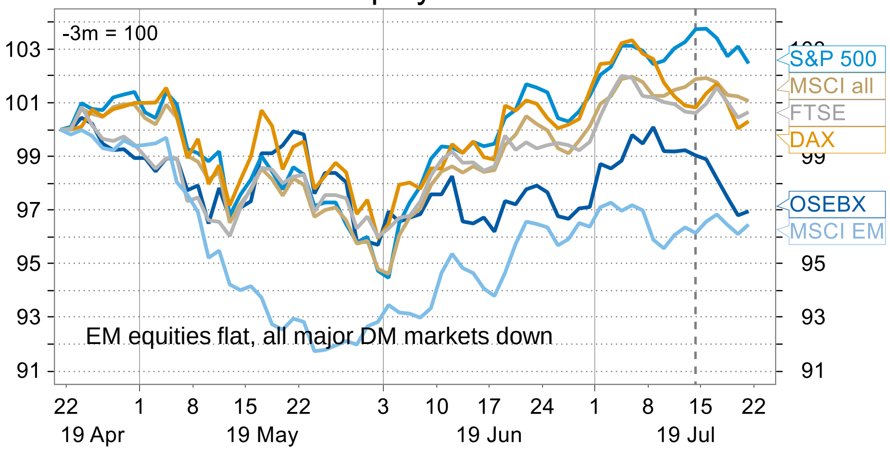
The Norwegian economy

Market charts & comments

Stock markets down, yields down, oil down. Metal prices are trending up

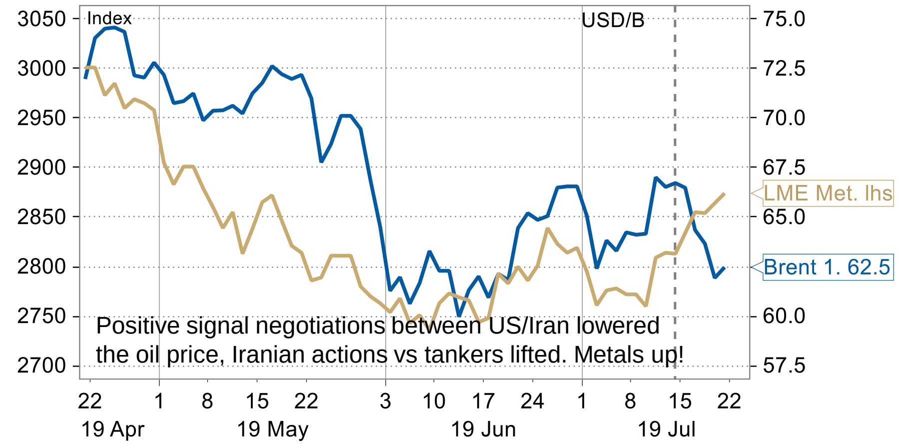
Broad decline in bond yields last week but all ar up from the local trough early July

Equity Indices



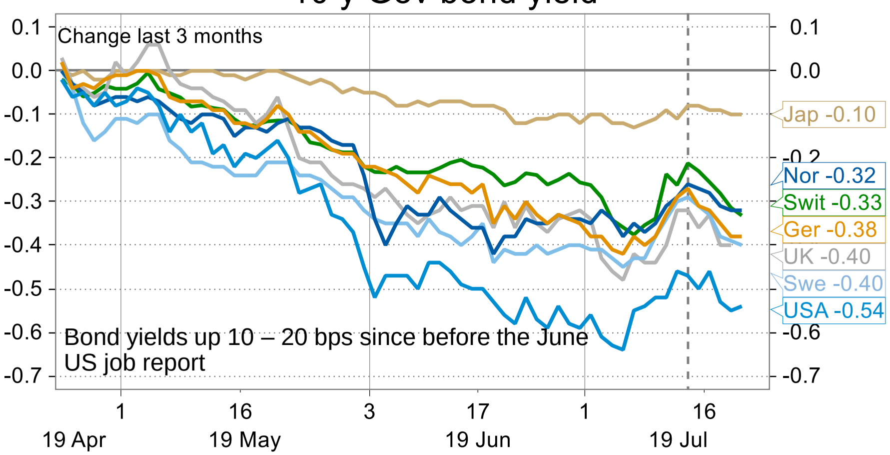
SB1 Markets/Macrobond

Oil vs. metals



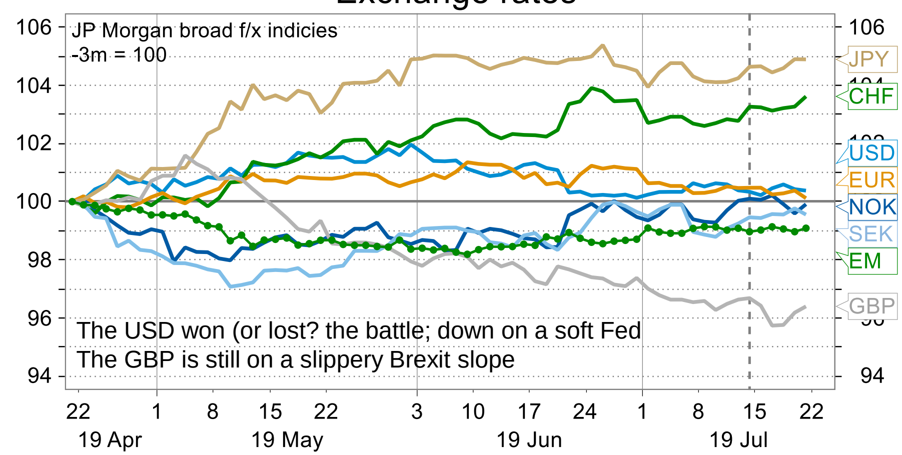
SB1 Markets/Macrobond

10 y Gov bond yield



SB1 Markets/Macrobond

Exchange rates



SB1 Markets/Macrobond

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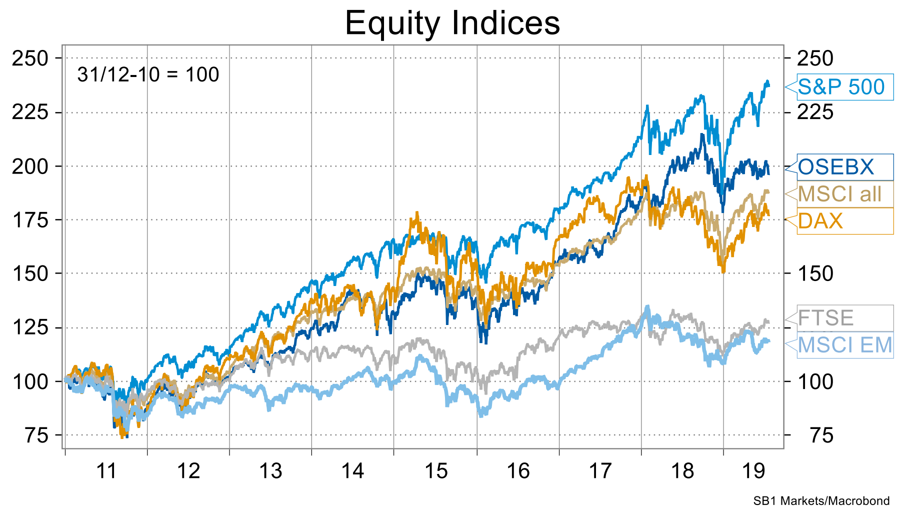
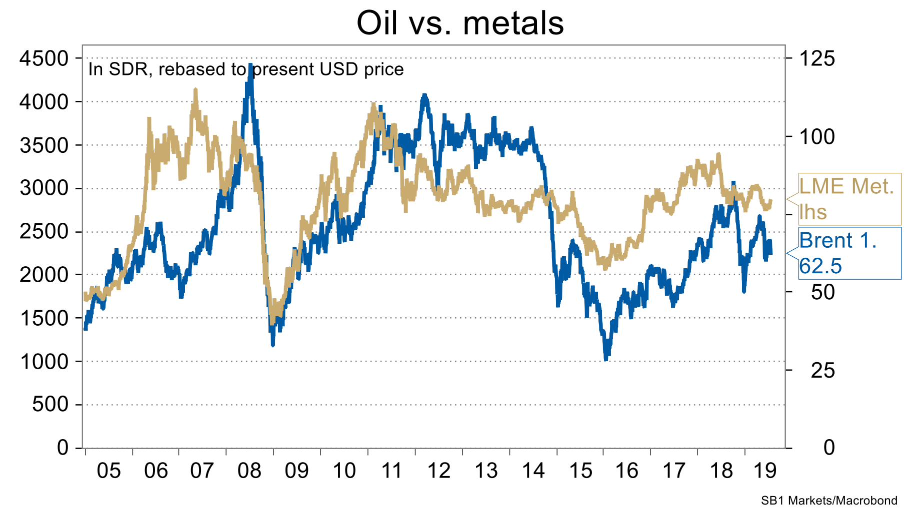
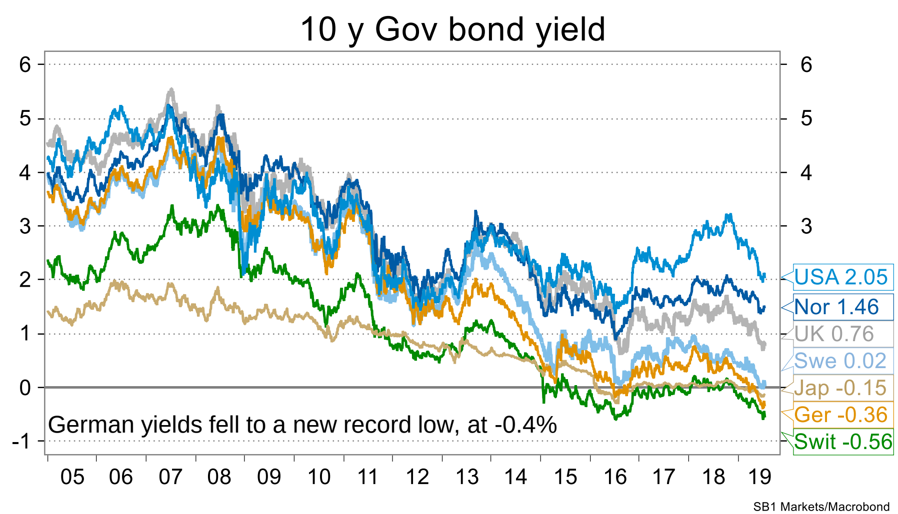
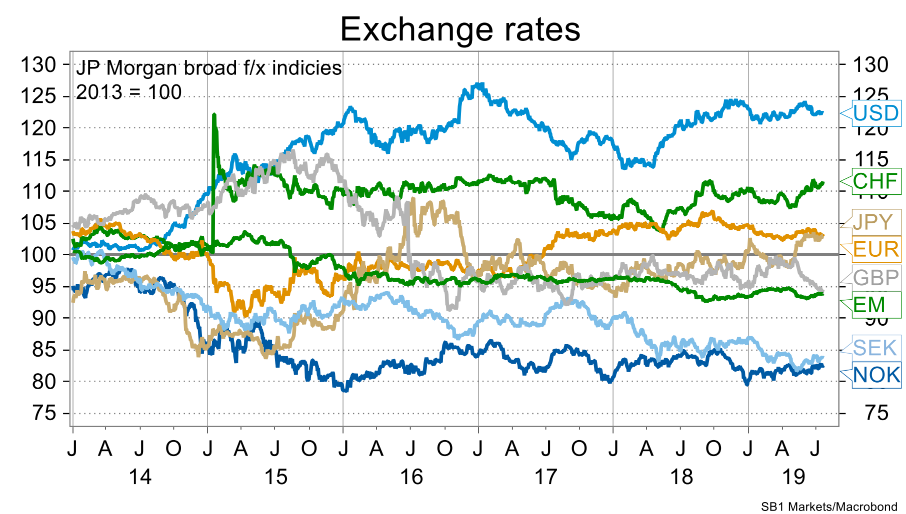
No major risk setback. For how long will low interest rates be good news?



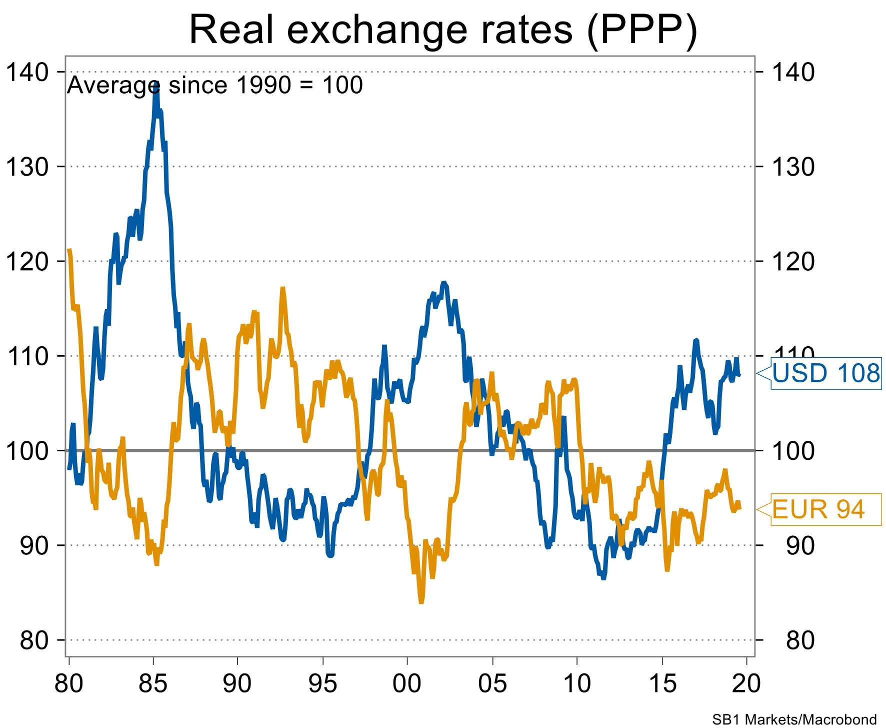


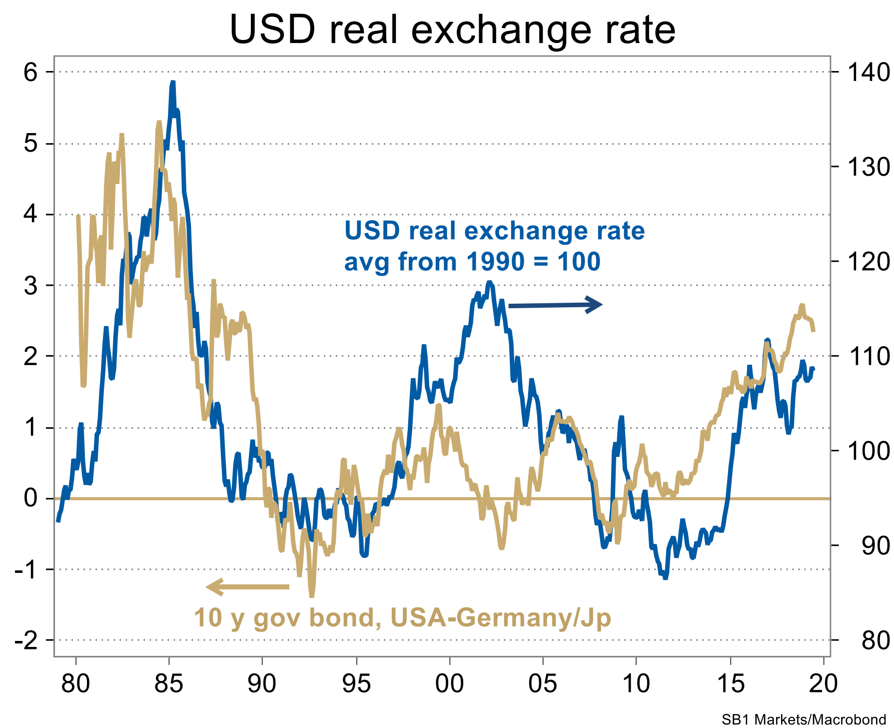




Currency wars next? The USD is somewhat above average, for a reason

However, the USD is far from record strong

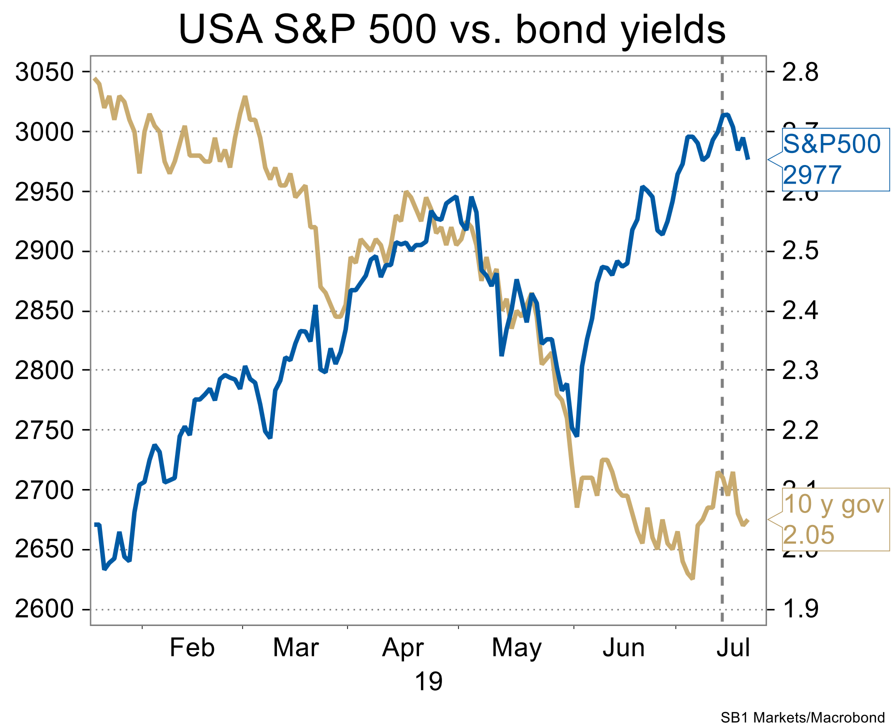


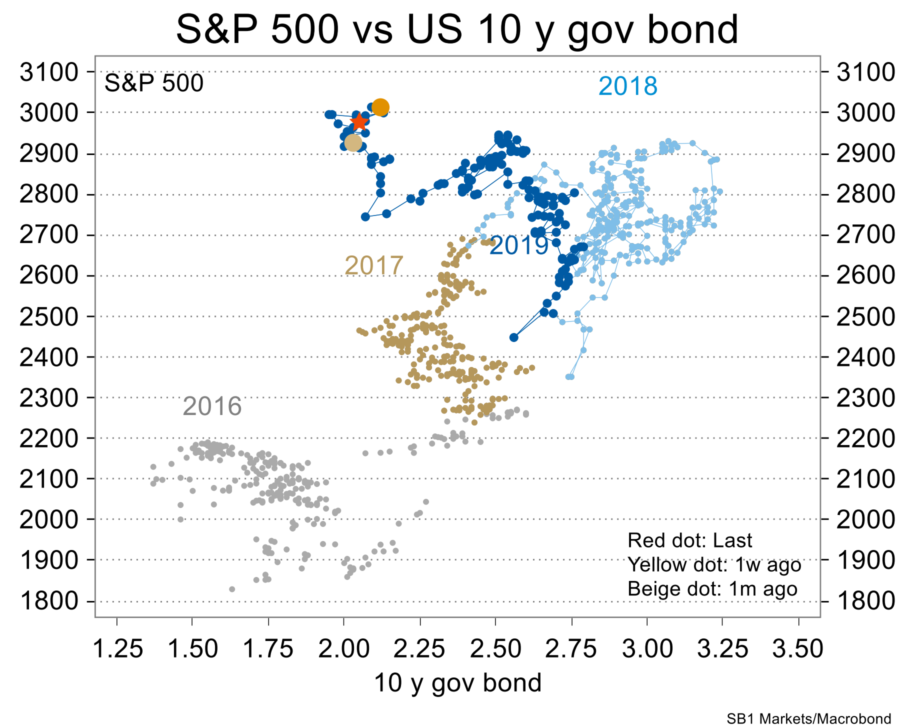


- Is the USD far too strong? Well, the greenback is 8% above average since 1990 (in order to capture two f/x cycles), measured by the real exchange rate (PPP), the <u>same deviation as in Oct 2016, before Trump was elected</u>. It has been up to 40% above the average in 1984 (backward calculated)
  - » Higher growth, and higher interest rates in the USA than abroad are good reasons for a somewhat stronger USD than normal
- The EUR is some 5% below the average since 1990 but marginally above the average since 2012

Higher bond yields, and another S&P500 ATH

Bond yields down 7 bps, to 2.05%. S&P500 up to ATH, still ended down 1.2%; earnings disappoint

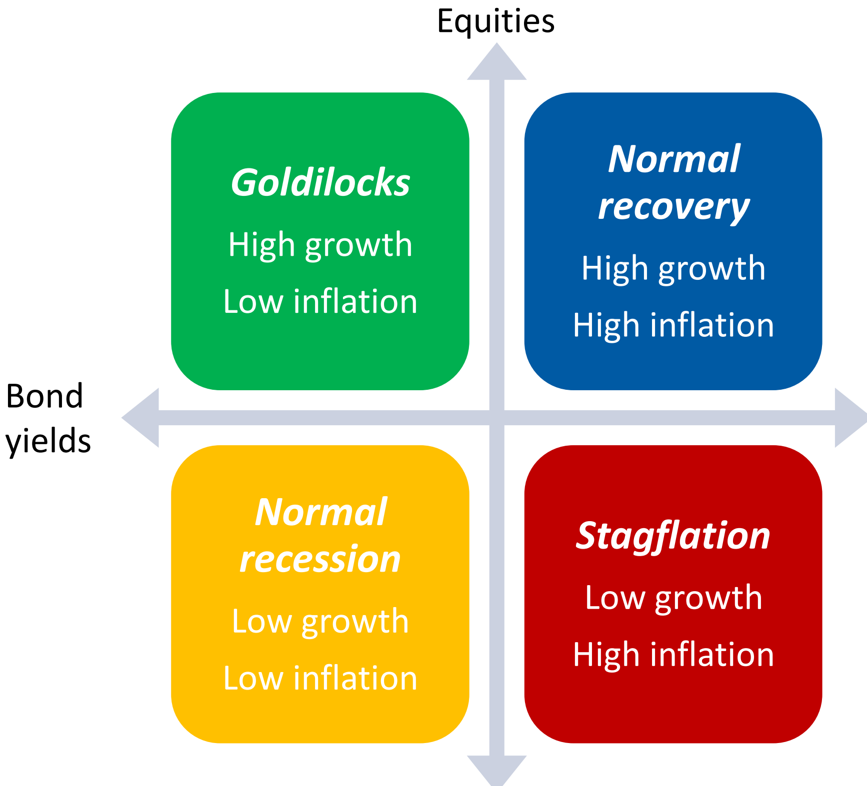




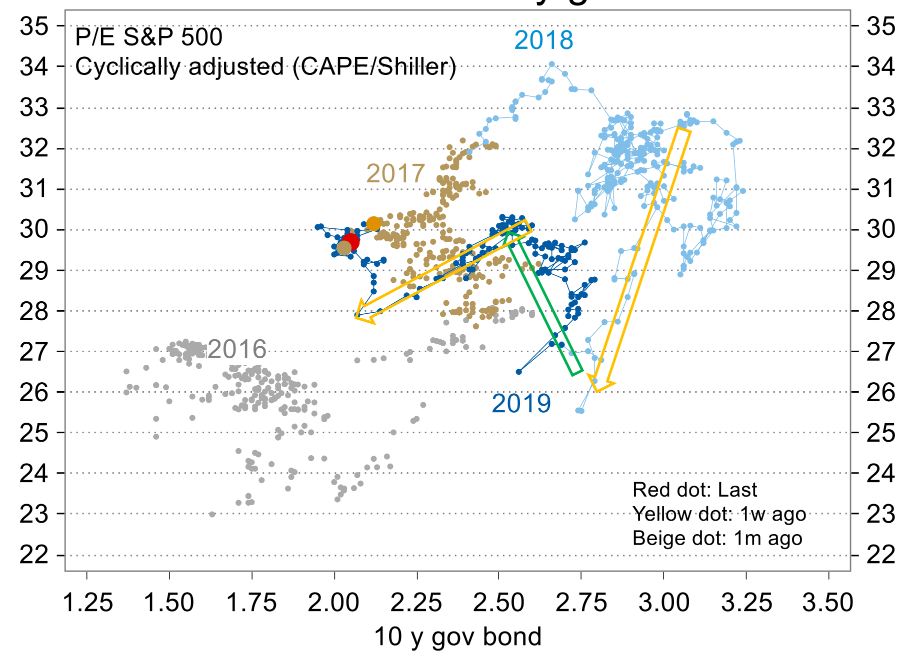
- For more on the relation between stocks and bonds, check next page

Markets towards ‘normal recovery’ last week too: Yields, equities up

The move in the Goldilocks’ direction is done for now? Only a huge Fed surprise can repeat the trick?



S&P 500 vs US 10 y gov bond

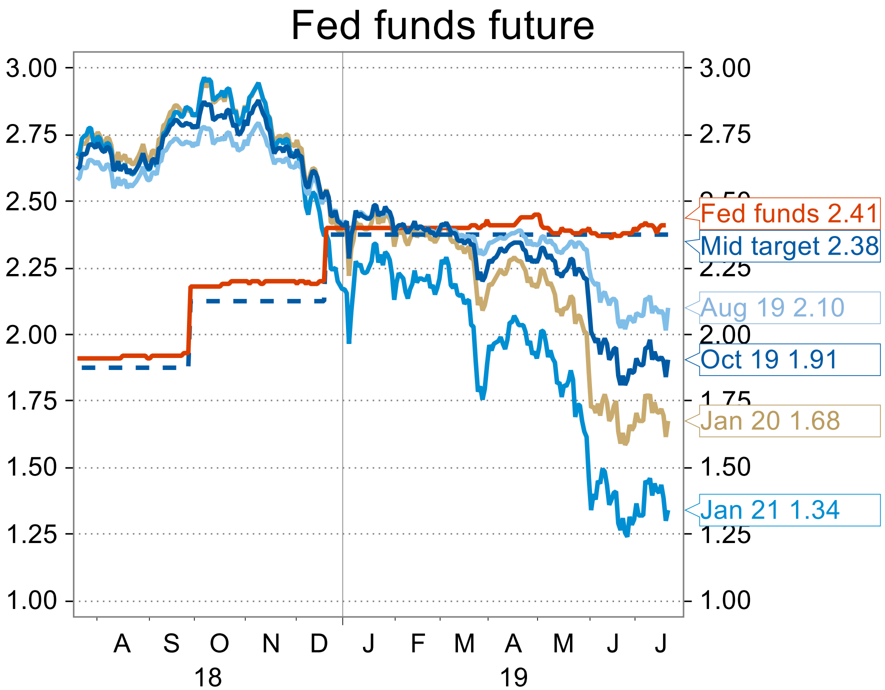


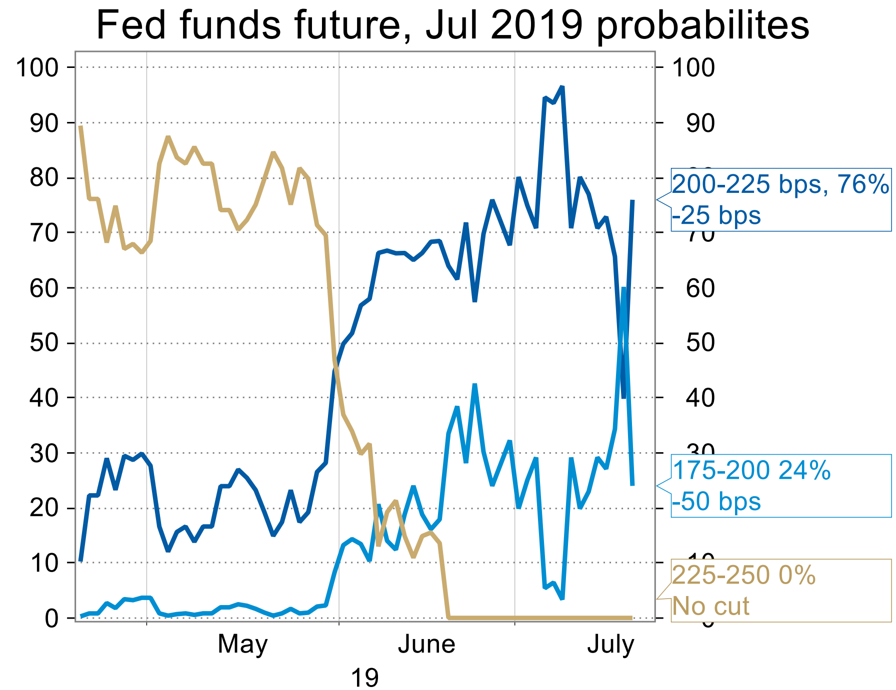
SB1 Markets/Macrobond

- During May, both stocks and bond yields fell sharply, towards the ‘normal recession’ (yellow) corner. The ‘yielding’ signals from the Fed (and other central banks) during June then pushed bond yields further down, and stock markets up – in the Goldilocks direction.
- We still think ‘normal’ axis, driven by growth, and with inflation (or at least interest rates) over time following growth up or down (the yellow/blue axis)
- Limited movements past weeks – last week both yields and equities fell – back to the level one moth ago (when S&P500 is devided by 10y avg real earnings, CAPE)
- We are – longer term – not that worried for the ‘Stagflation’ corner, 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

Oobs, too many talking head, some were misunderstood. In the end: -25 bps

NY Fed's Williams referred to pro 'big cut research', that turned out to not be relevant now





- In a speech Thursday, NY Feds governor John Williams said that research had shown that a large cut in interest rates would be best if interest rates were low and the economy needed a stimulus. Did he hint about a 50 bps cut later in July? Interest rates fell sharply (6-8 bps), and the likelihood of a 50 bps cut next week rose to 60% from 34%, an unusual daily (or hourly) change!
- Then the NY Fed had to issue a statement to make clear the Williams just had referred to research, and that he had made no reference to the actual situation! Another Fed dove, Bullard, drove the nail in, by telling media he now preferred a 25 bps cut. Then market rates fell, and the likelihood of a 50 bps fell back to 24% at Friday! We think it is closer to zero
- Two more cuts are priced in before Christmas. Not impossible – but that requires a much weaker economy than the present

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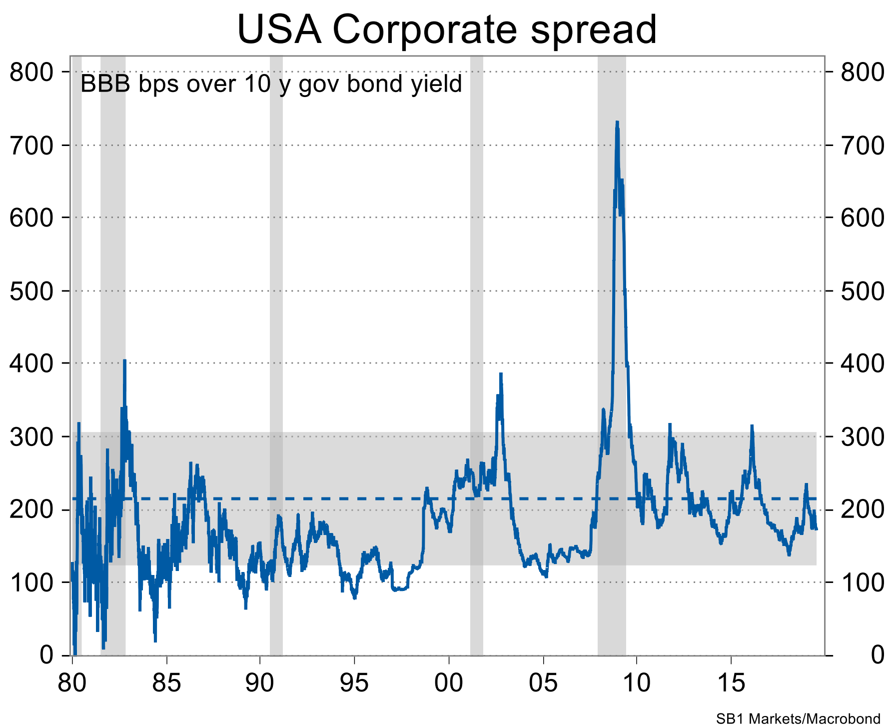
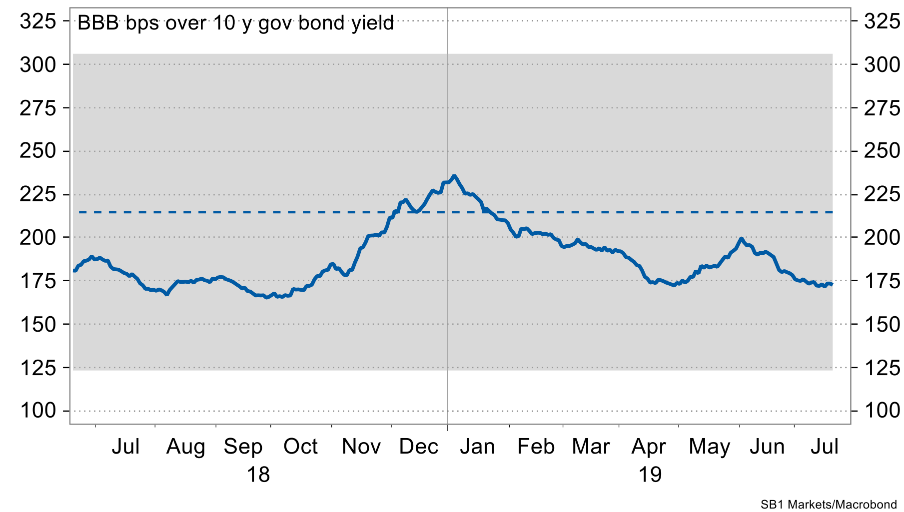
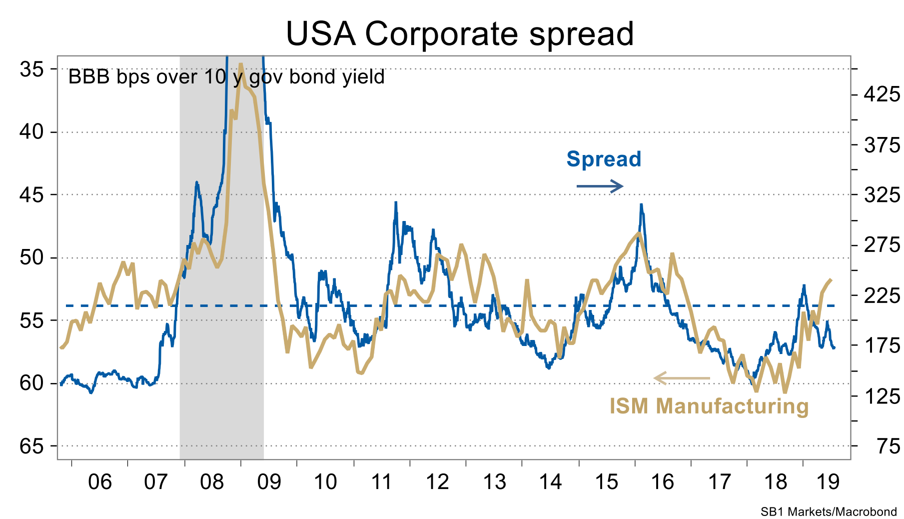
Credit spreads marginally out last week but still low

However, spreads are too low if the ISM and (most) other surveys are correct; <u>if growth is slowing</u>

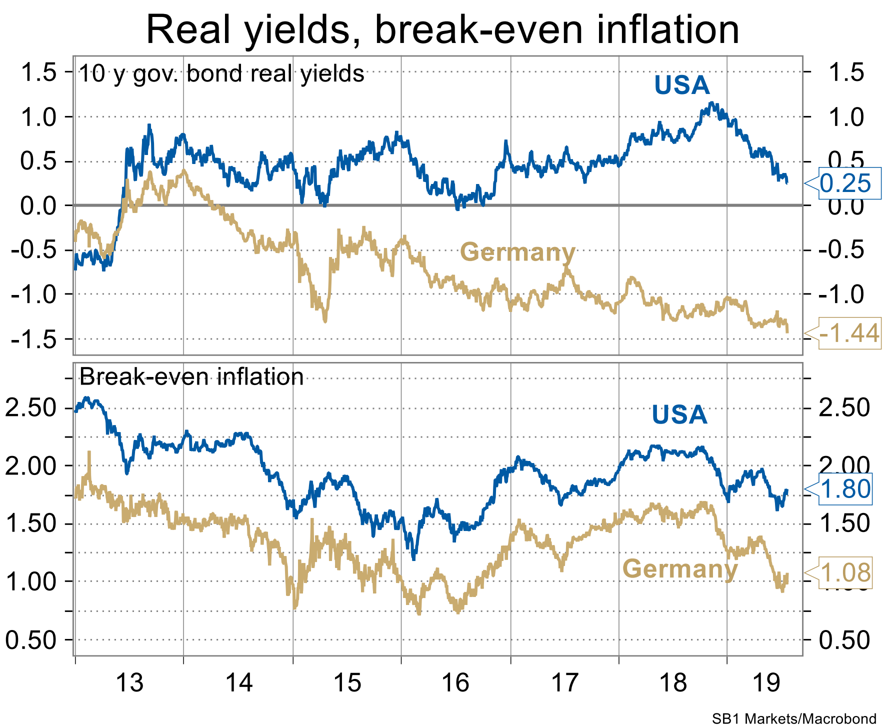


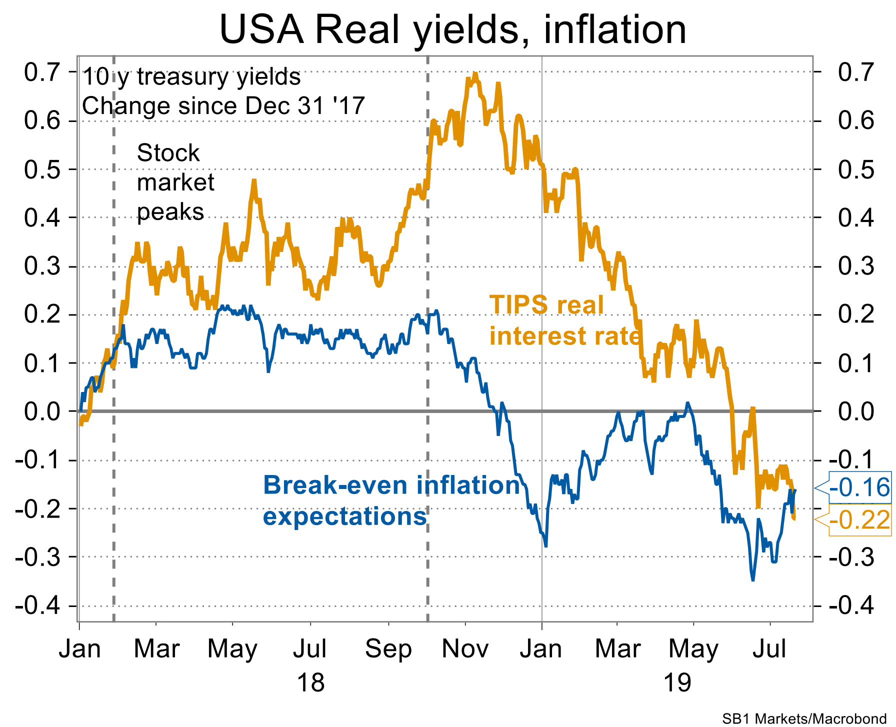




Inflation expectations up, real rates down, both in US, Germany

German 10 y real rate down to -1.44%, per year, a new ATL!!!





- US 10 y real rate at 0.25% (down 10 bps, has not been lower since 2016 , inflation expectations (measured by CPI) at 1.80%
- German real rates down 17 bps, to -1.44%, in credible. Inflation expectations up but still low, at 1.08%

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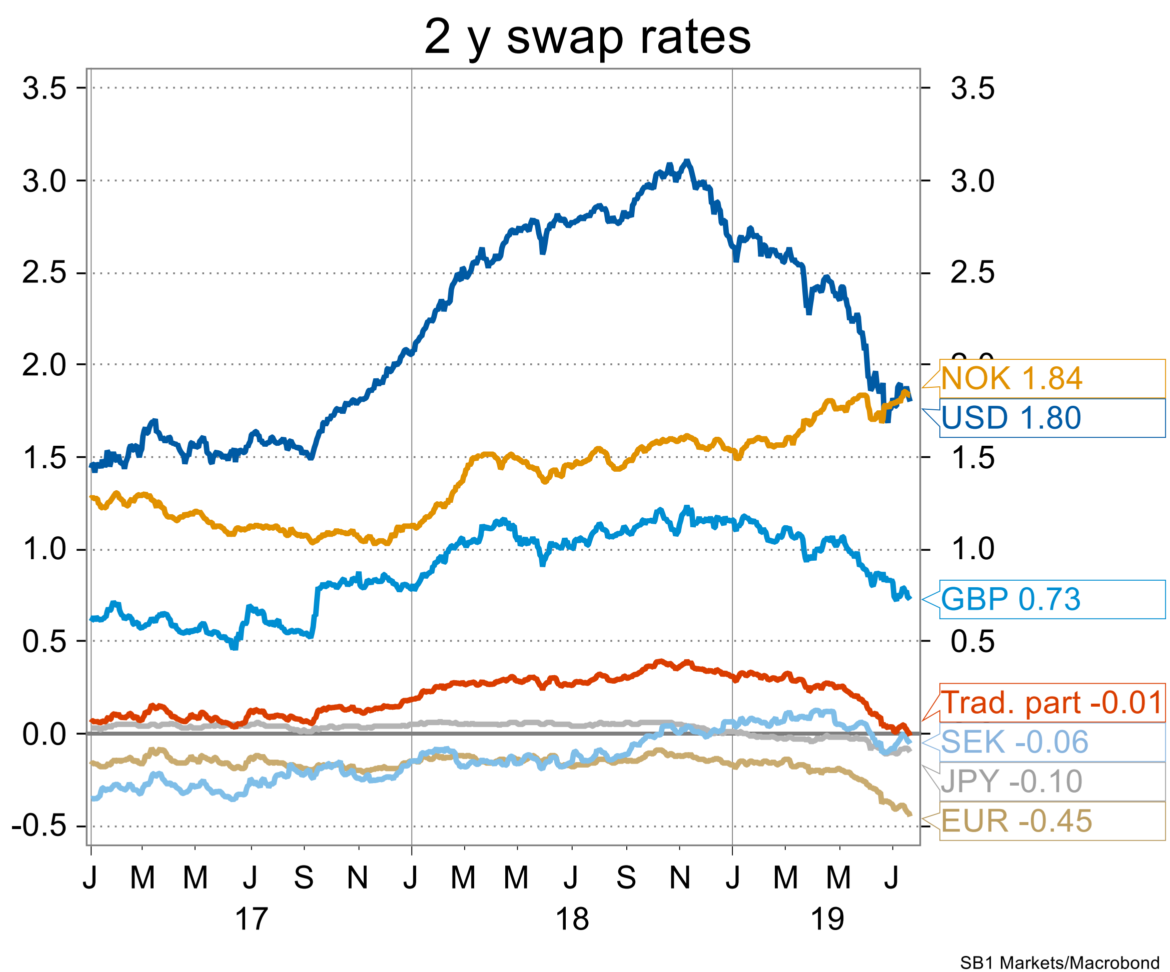
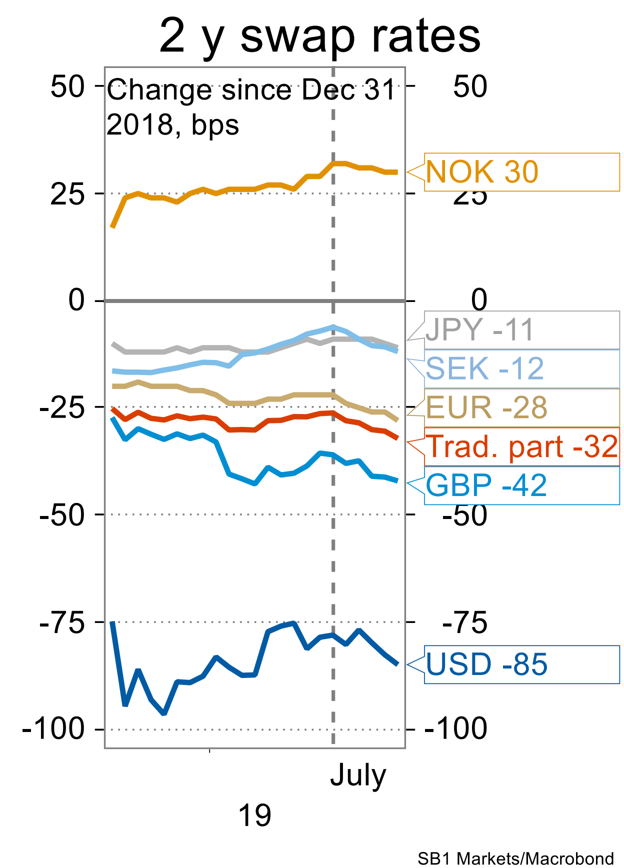
Short term rate down everywhere

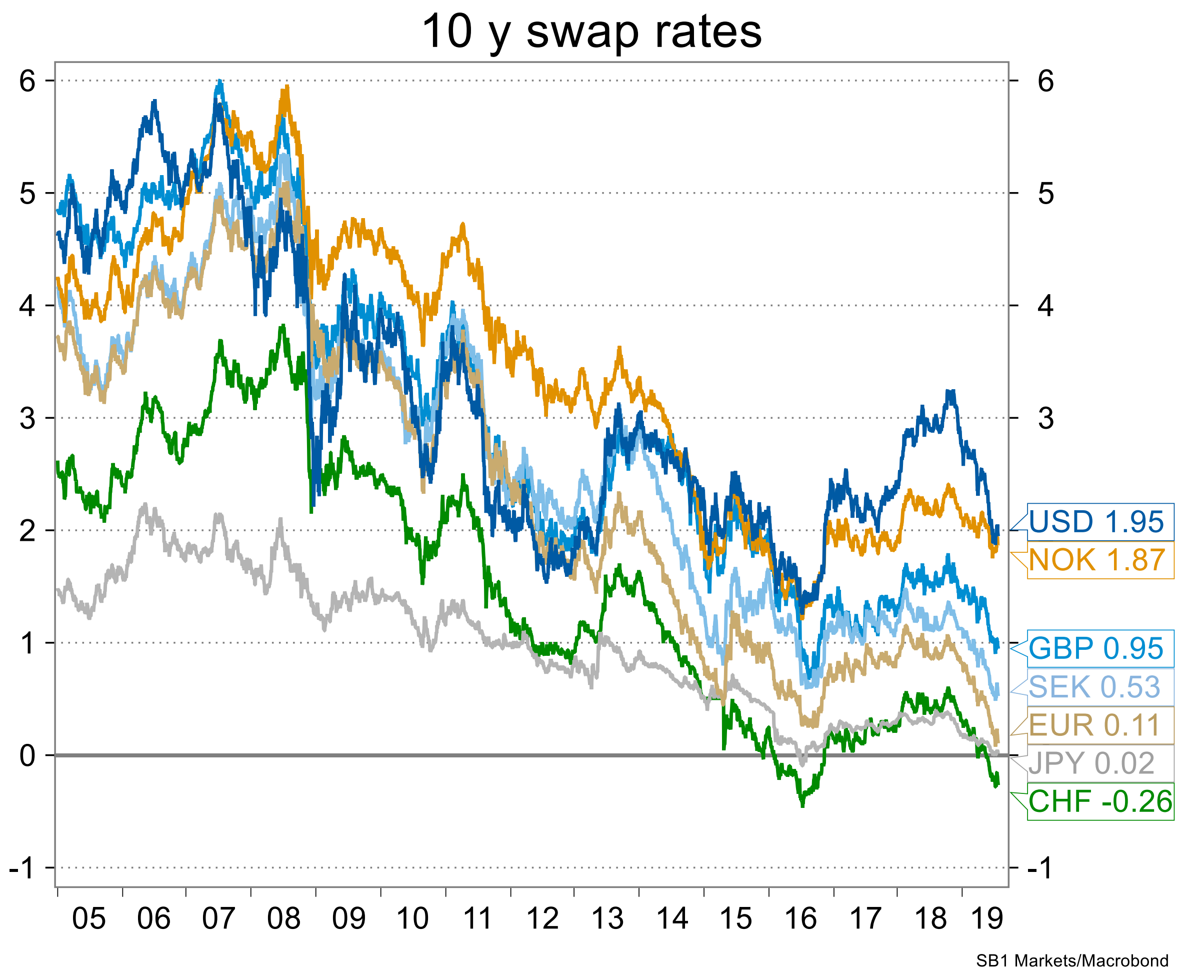
And new ATLs day after day in EMU. The ECB has to tell a story this week… NOK rates high, vs others

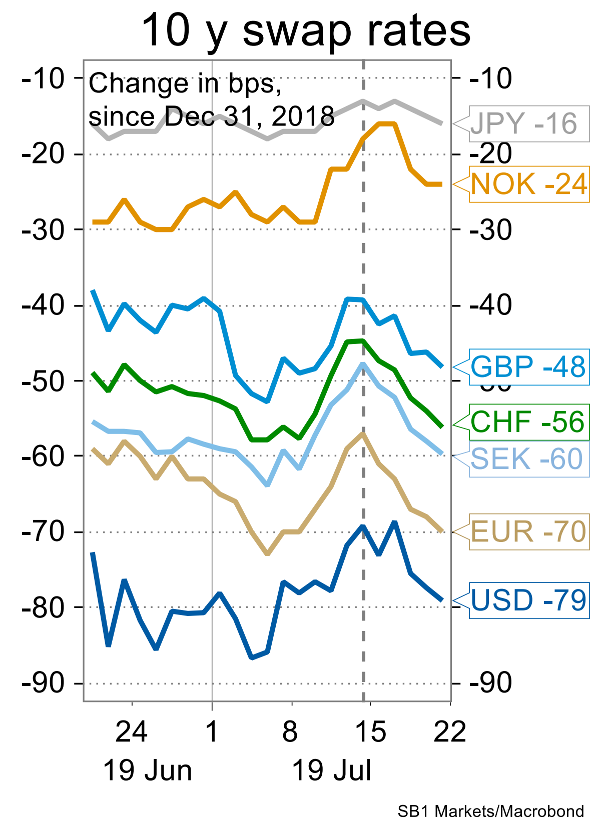




Long term swap rates down everywhere last week…

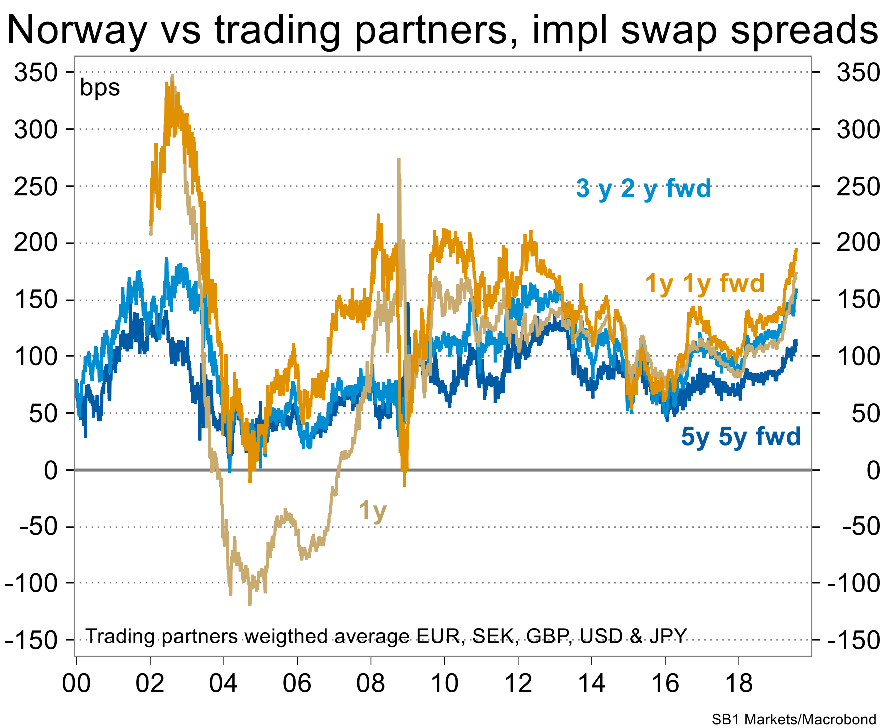
And the trend is straight down

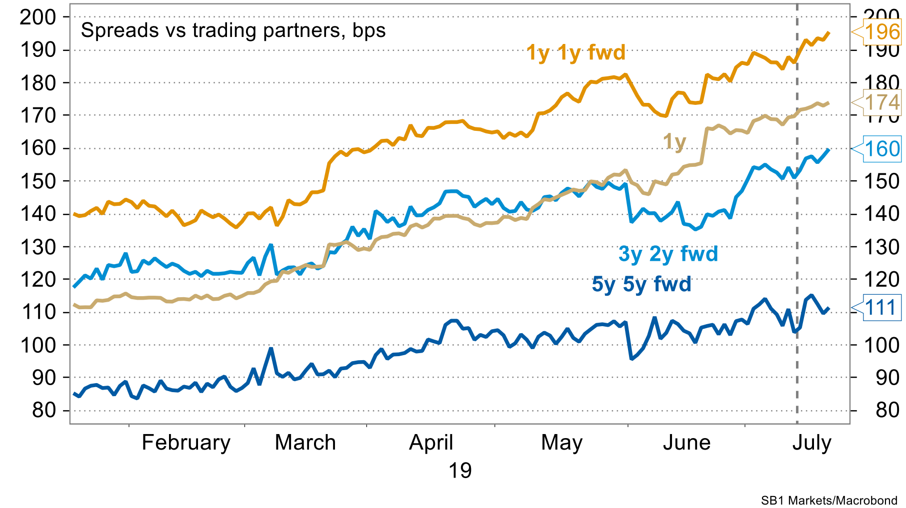


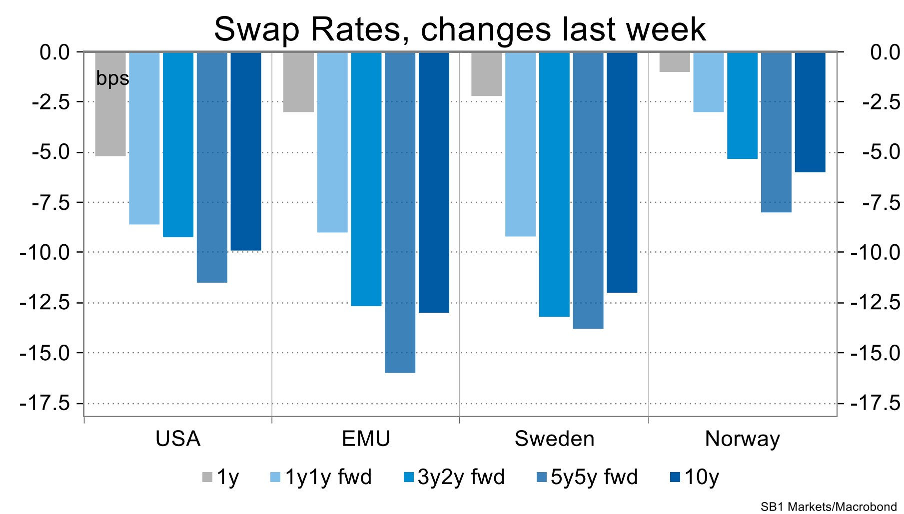


NOK swap spreads vs trading partners up all over the curve, again

NOK rates down all over the curve but less than abroad



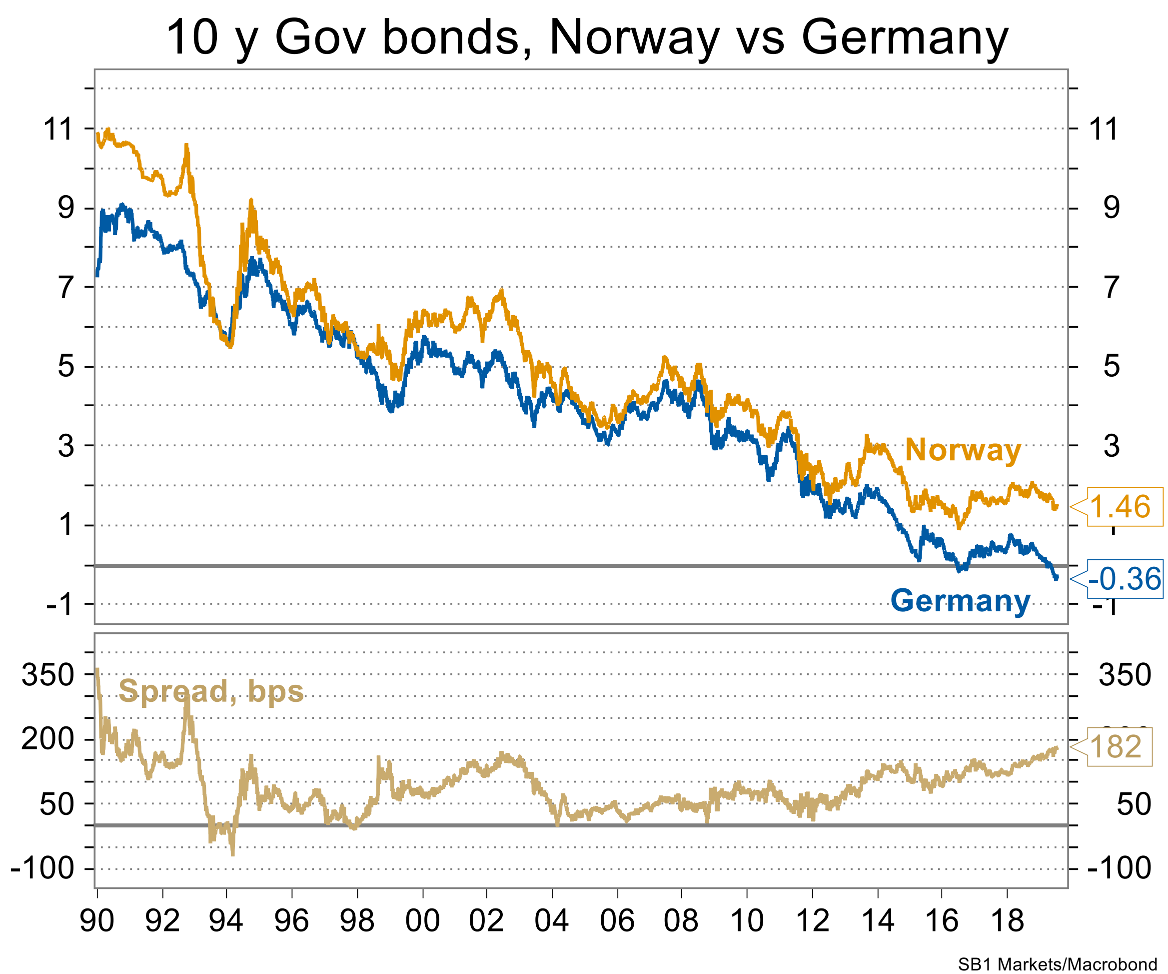


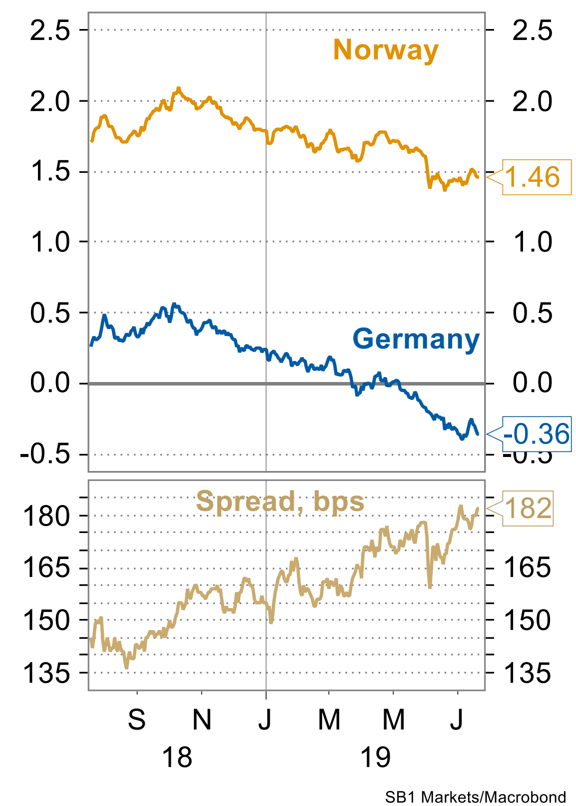


- A high spread is reasonable, given NoBa's stance vs Fed, ECB and the Riksbank (which is due to solid Norwegian data, not a really hawkish bank..)
- Although the short term spread is well explained, we have been surprised by the wide spread in the long end of the curve of the since March

Long gov bond yields down, more in Germany than in Norway

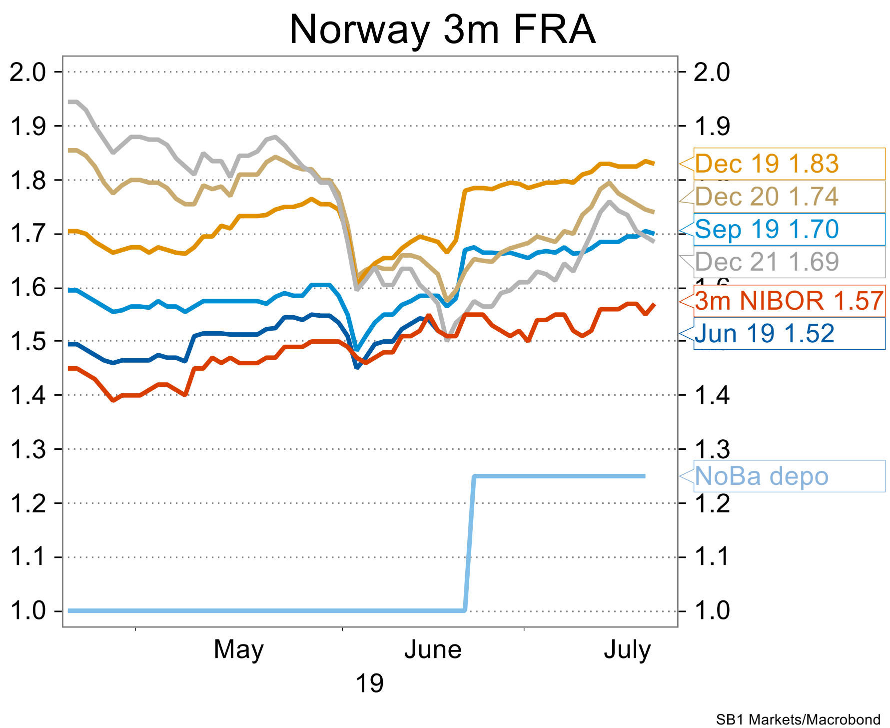
NOK 10 y gov down 6 bps to 1.46% - the spread vs the Ger. bund at 177 bp is far too rich, long term

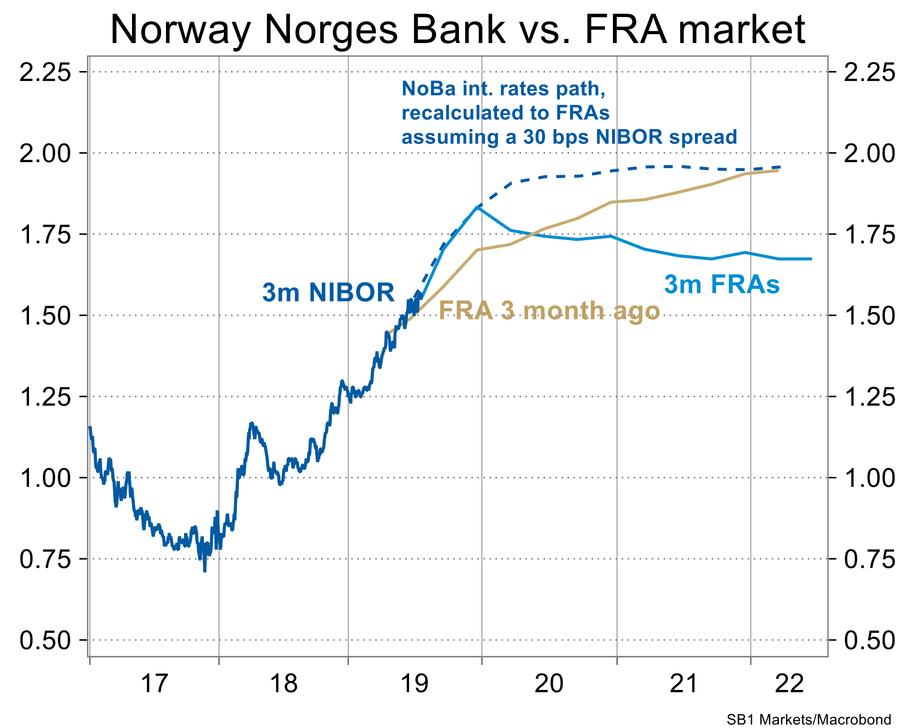




Norwegian short FRAs climb, longer FRAs follow foreign rates down

The NIBOR spread may have widened somewhat, but market puts at least 50% prob. for a Sept hike

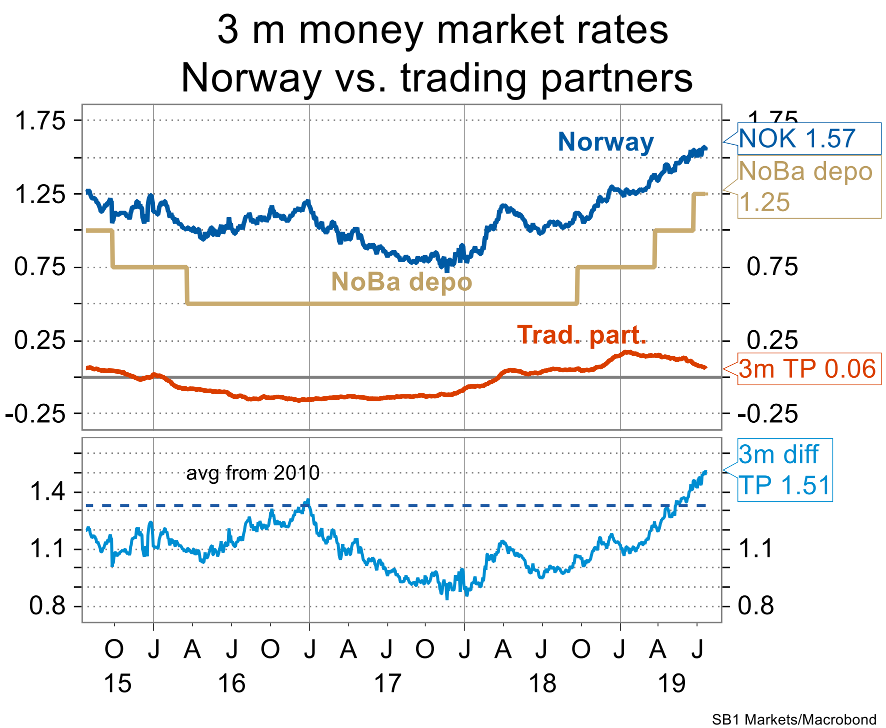


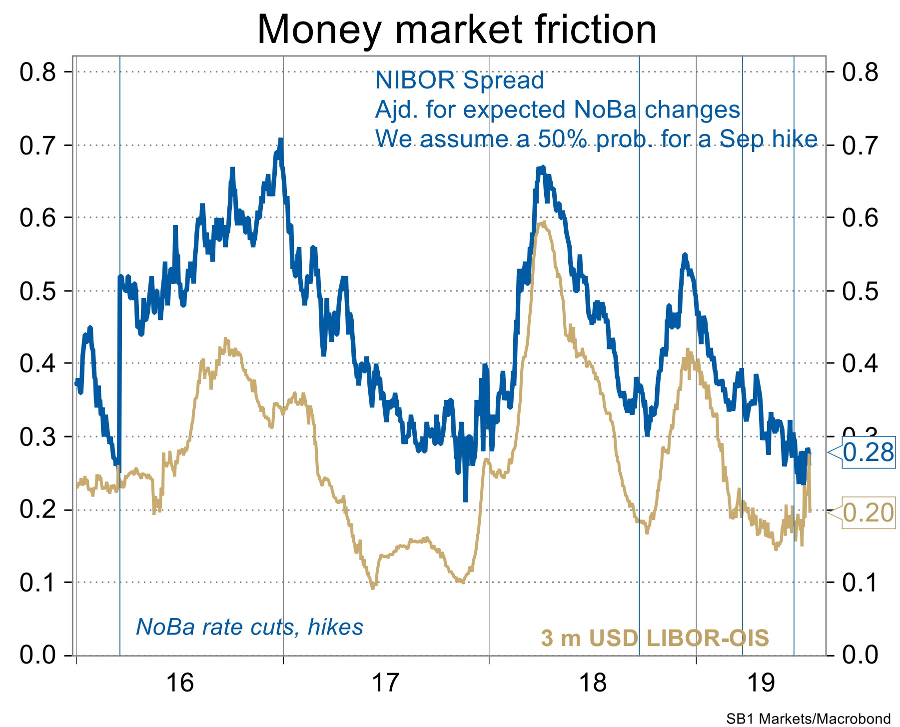


- The NIBOR Dec '19 FRA at 1.83%, signals either that at NIBOR spread has increased (we have until now assumed 30 bps) or that the market is puts some probability for a hike both in Sept and Dec (if so up to signal rate at 1.75, and a NIBOR at 2.05). We think a spread widening is most likely
- The FRA curve is inverted from Dec 19 onwards, the market does not expect any hikes after 2019 (NoBa plans 1 in '20)

3m NIBOR up to 1.57%, as the market warming up to a Sept hike

Warning: The US 3m OIS (as the TED) widended the prev. week; then fell back last week

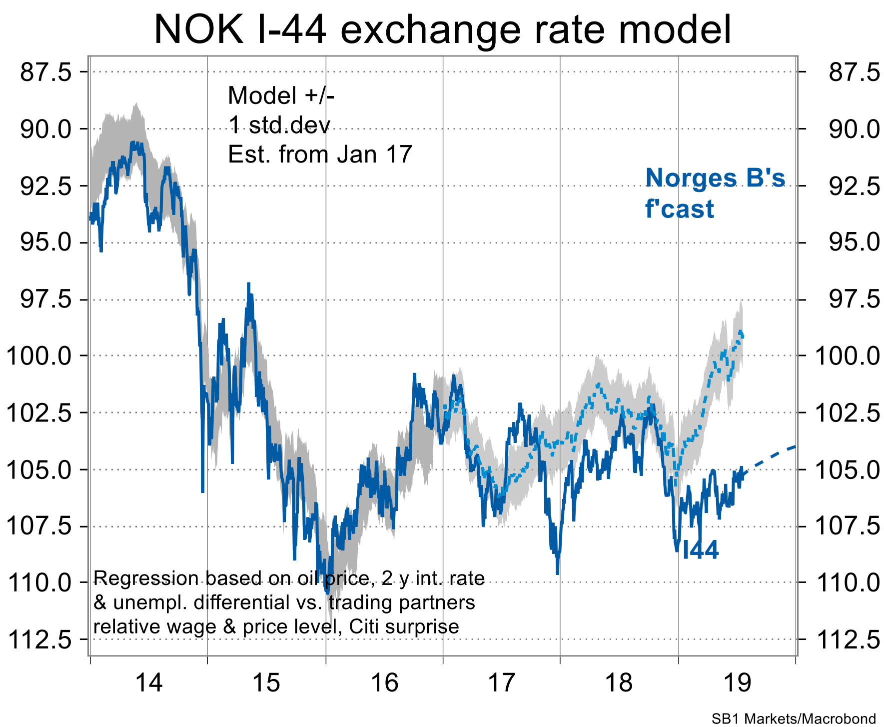


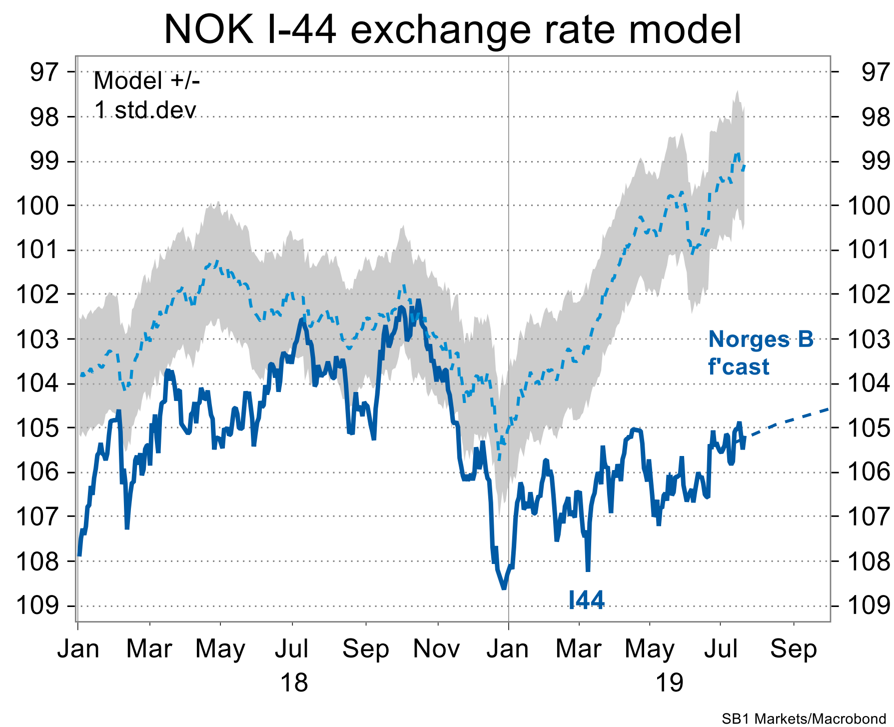


- Still, the spread has widened over the recent weeks and the NIBOR spread may have widened too. If so, it's the spread that's pushing the NIBOR and FRA's up, not more probability for a September hike
- The spread between NOK and trading partners' 3 m money market rates at 1.51 bps is up 60 bps since December 2017 and is 20 bps above the 10 past year's average – without sending the NOK into the orbit

NOK marginally down last week, like the model said. But…

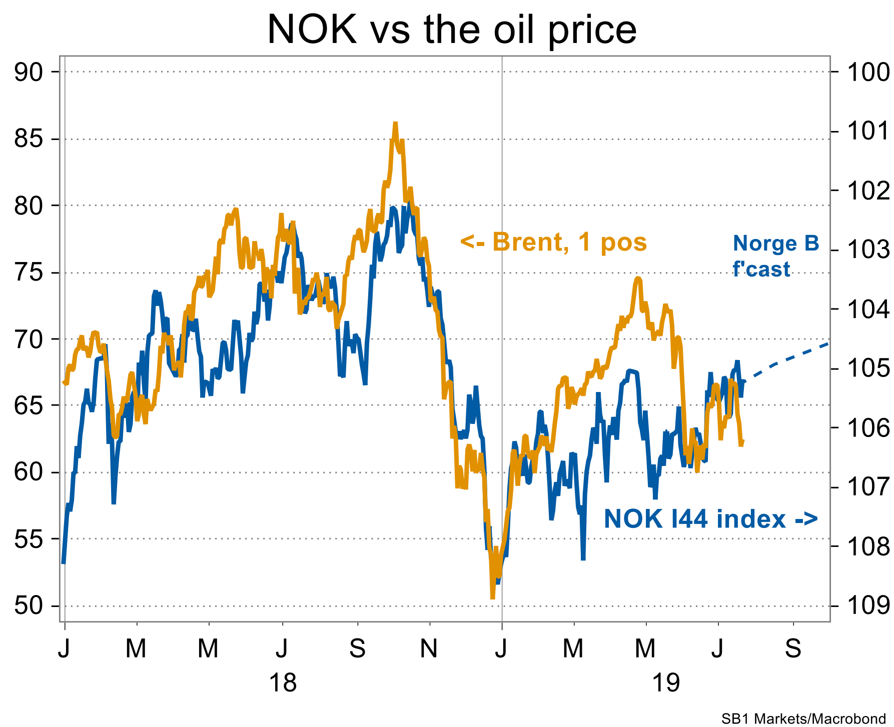
The NOK is still more than 6% below our model's f'cast

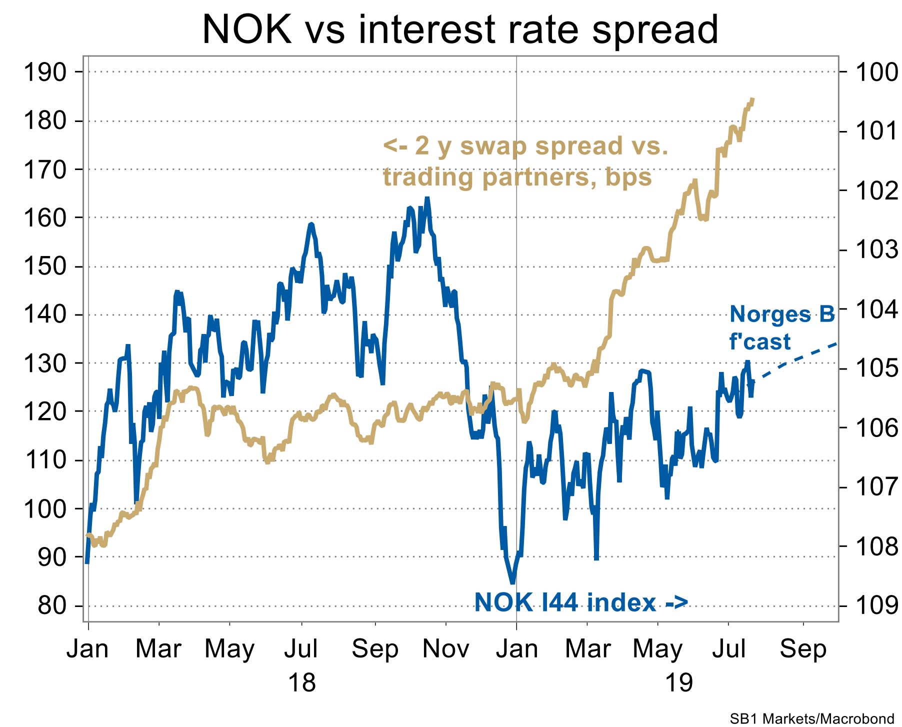




- The model forecast down 0.3% with a lower oil price countered by the impact of a higher interest rate spread
- What explains the (extra) weakness vs the model estimate since March?
  - » No really weak Norwegian macro data, on the contrary, most data have been upbeat
  - » Risk aversion? Perhaps, yet EM currencies have not collapsed (even as many depreciated when the trade war escalated)
  - » Weakness in other supercycle currencies may be an explanation. A NOK model based on AUD, CAD & SEK, that has worked very well over time, explains the recent 'flattishness' very well – which our standard model does not
- We do not have any other recommendation than **Buy NOK**

NOK marginally up last week, but less than oil, interest rate spreads suggested





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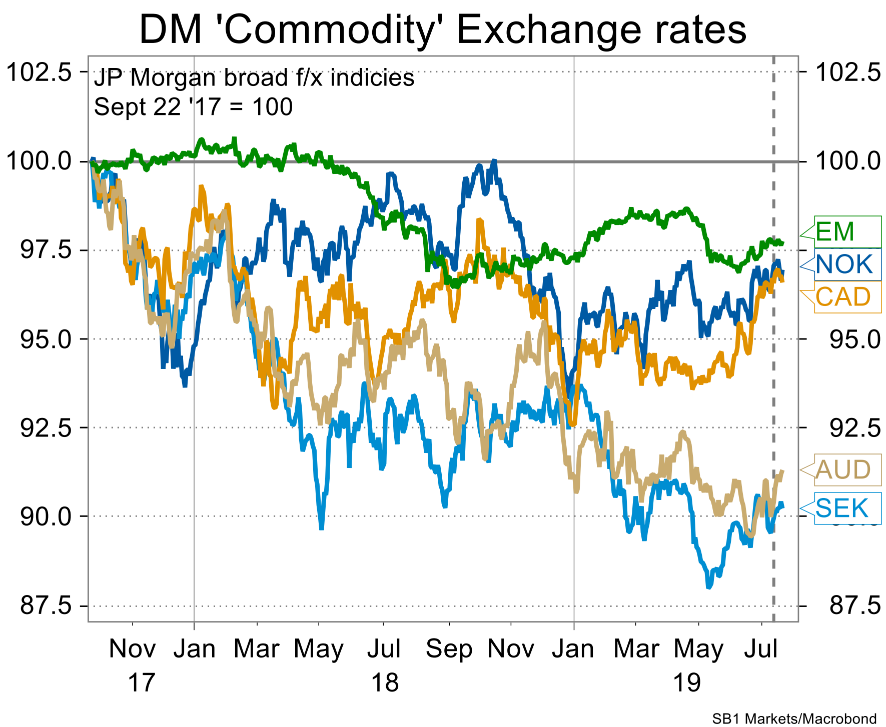
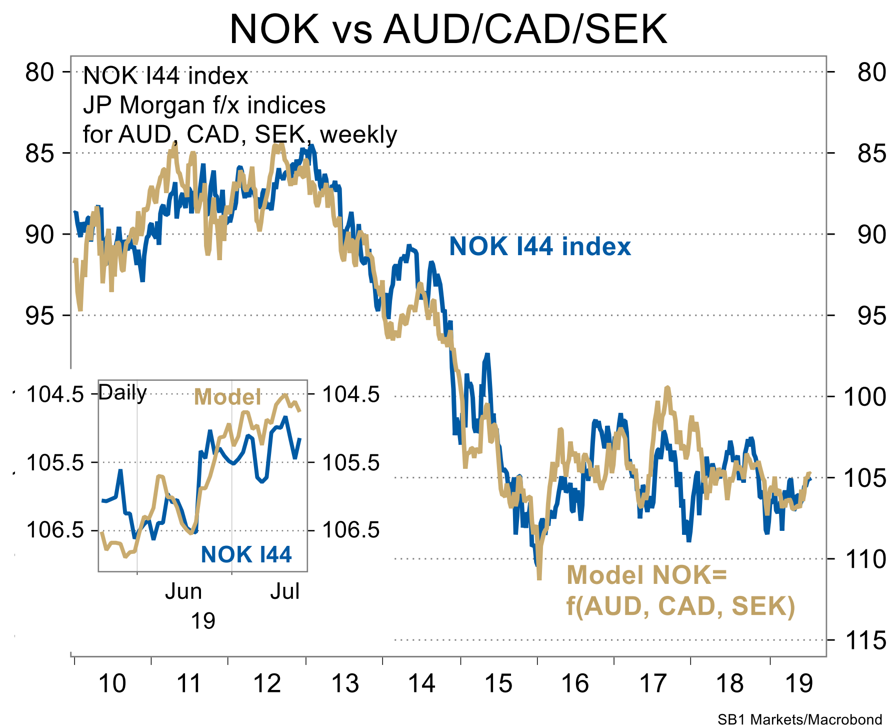
NOK follows our supercycle pals pretty well over time – and now

Forget oil, NOK interest rates and all the other factors. Just look at AUD, CAD (& SEK, but not needed)

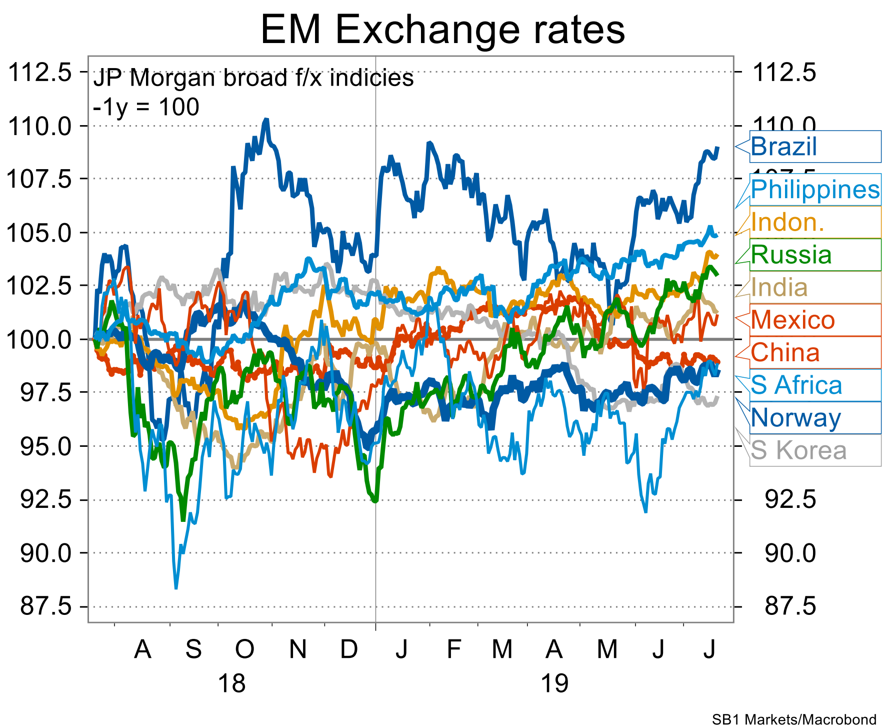


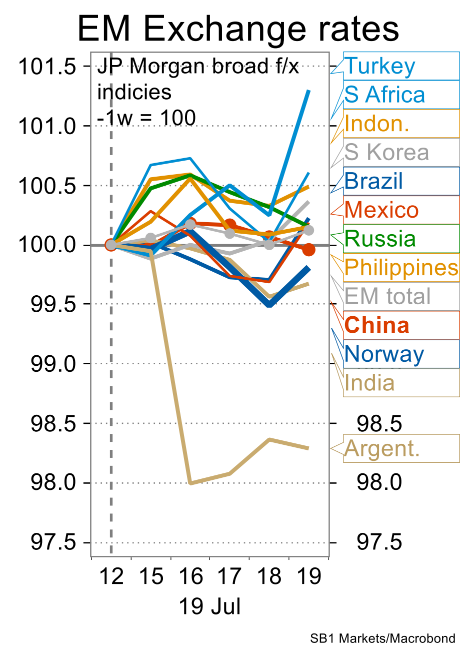


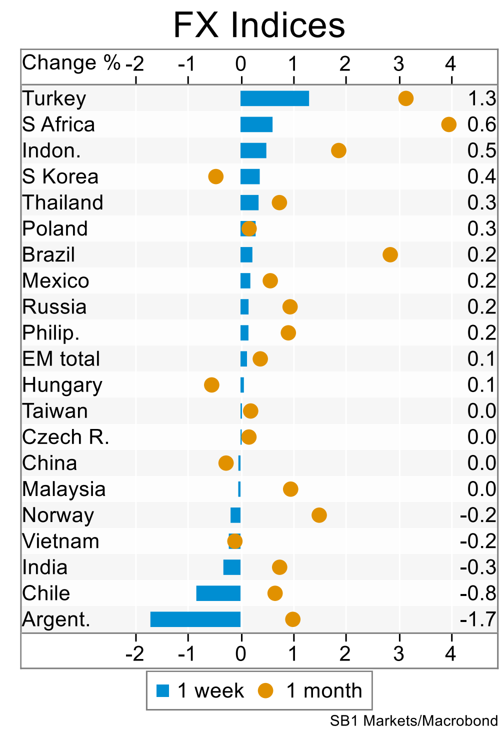
- NOK is much weaker than our workhorse model predicts, and much lower than others' models suggests (NoBa's model miss is almost twice as large as our model's residual)
- If we just model NOK as a function of AUD, CAD and SEK indices, the 'new' NOK weakness since 2017 is much better explained. It was the supercyclicals that fell out of favour – not the NOK (except for some extra NOK weakness late 2017)
- What is the common factor for these currencies? It could be raw material prices, but they do not explain it. Quite similar bubble economies w/ debt & housing risk? China risk?

EM f/x: More up than down last week

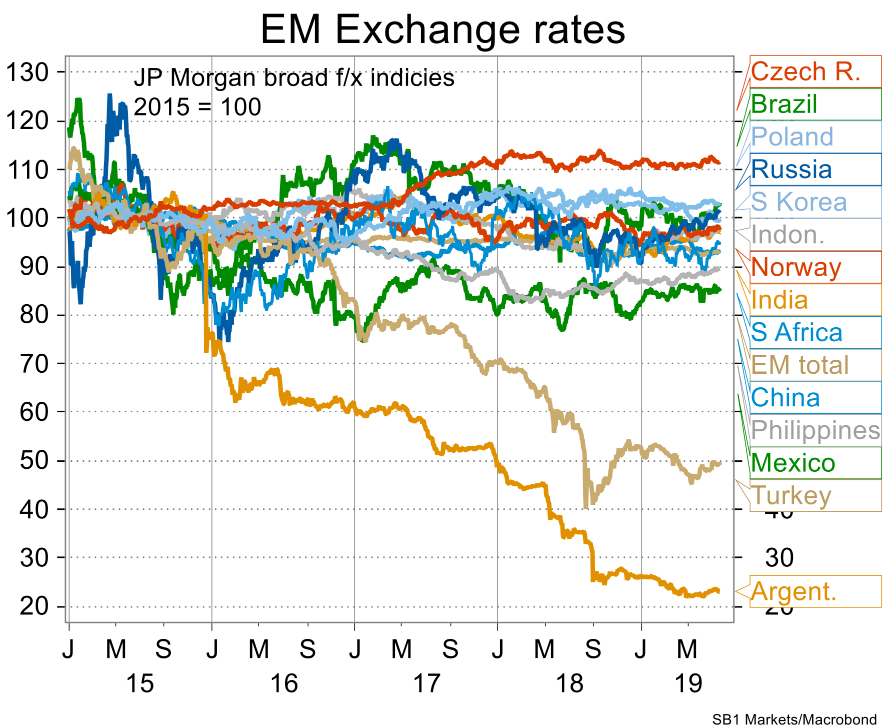
The CNY marginally down, the Argentinian peso much more (but may have stabilised, like the TRY)

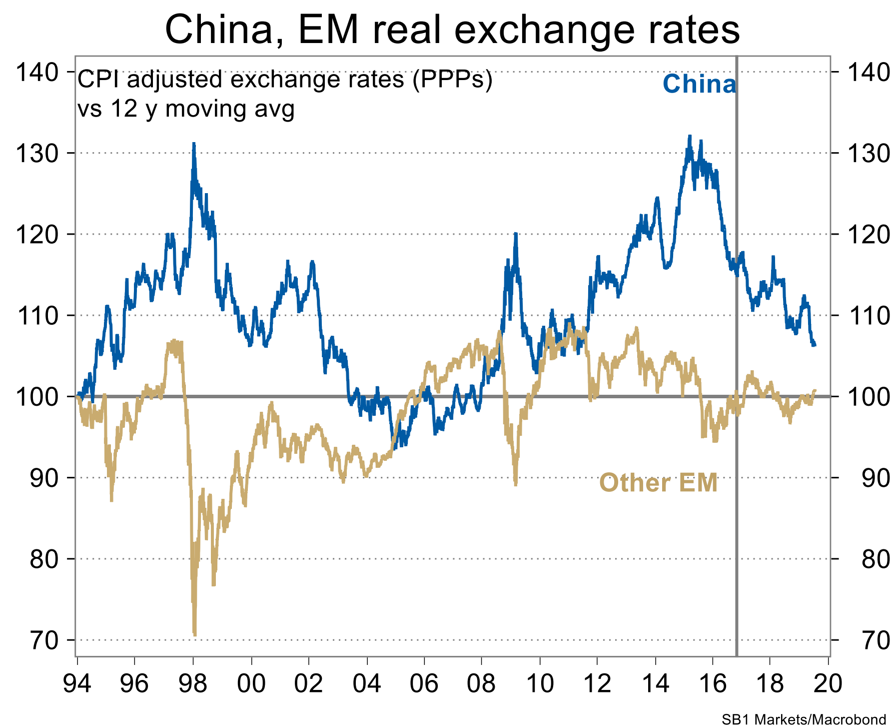






EM f/x, a long term view: Not that exiting, now





- The real CNY exchange rate was (too) strong in 2015/16, most likely contributing to the slowdown in the Chinese economy. China had a huge surplus at the current account 10 years ago (10%+). Now the C/A is close to balance; goods are still in surplus, while there is deficit at the service balance
- Other EM currencies have in average been quite stable the recent years, even if some have run into problems, like always. This time Argentina and Turkey have struggled, for good reasons. They have both stabilised recent months

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