29 July, 2019

Macro Research

Summer update

Harald Magnus Andreassen
Phone : (+47) 24 13 36 21
Mobile : (+47) 91 14 88 31
E-mail : hma@sb1markets.no

Synne Holbæk-Hanssen
Phone : (+47) 24 13 36 31
Mobile : (+47) 40 49 55 48
E-mail : shh@sb1markets.no

SpareBank 1 Markets
Phone : (+47) 24 14 74 18
Visit address : Olav Vs gate 5, 0161 Oslo
Post address : PostBox 1398 Vika, 0114 Oslo

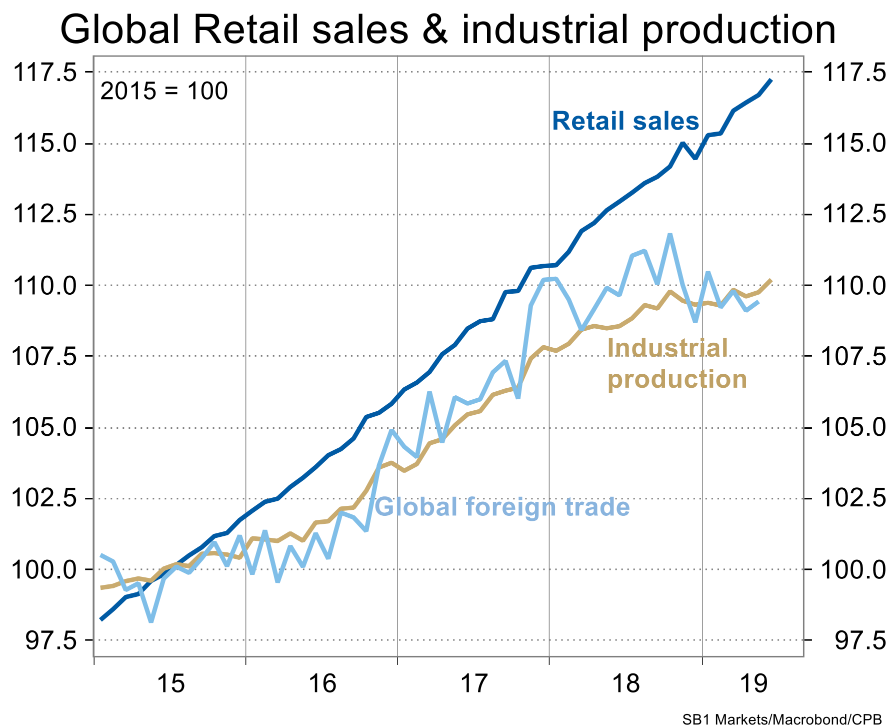
The headlines are linked to the relevant section in the report
The elements on the the page "In this report" are linked
A top right button will bring you back to the content page

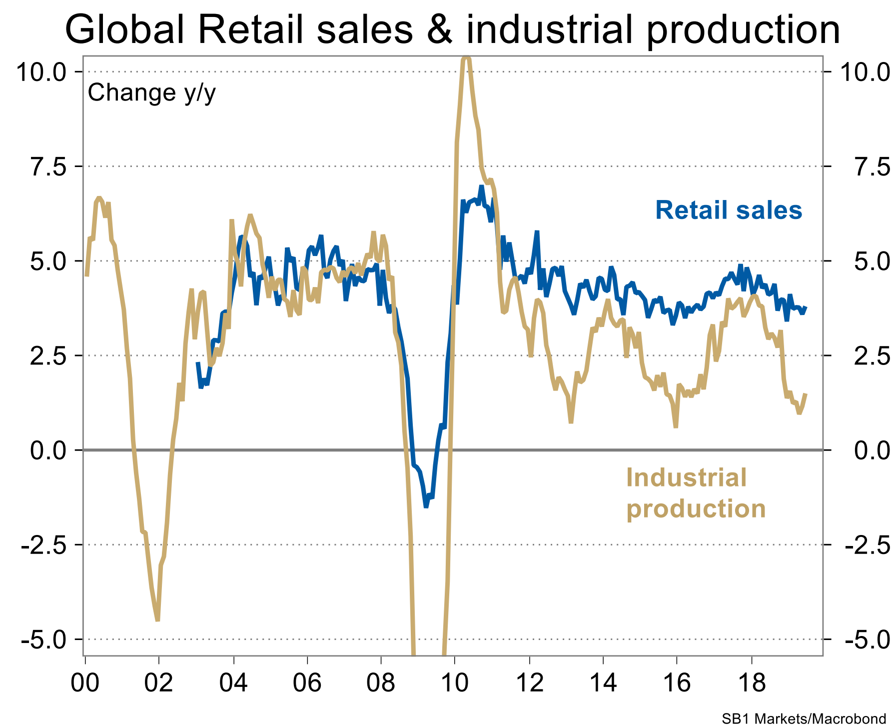
Last week – the main takes

- **Politics & trade:** They (the US trade delegation) are going to Beijing. However, not many other good trade war news. In UK, Boris Johnsen promises to fix everything, Brexit included. Fiscal policy will turn expansionary
- **The global composite PMI** was most likely stable in July, as in June. The manufacturing index fell further below the 50 line, while the service index rose. The US manuf. PMI surprisingly fell to 50, while regional Fed surveys are mixed. The EMU manuf. index fell sharply, and Ifo confirmed that the German manufacturing is struggling
- **US GDP** grew 2.1% in Q2, 0.3 pp more than expected but the history was revised down by 0.4pp, and the annual growth rate was 'just' 2.3%. Household consumption accelerated to above 4%, and government spending rose sharply (5%), while business (and housing) investments fell slightly**. PCE inflation** accelerated but remained below target. **Durable orders** rose in June but do not signal an investment recovery in Q3. Few **jobless claims**, cont. **The debt ceiling** was lifted, and some 0.2% of GDP was added on the expenditure side for the 2019/20 budget year. The fiscal stimulus is less than 0.5% of GDP in 2019, and even given the increased expenditure due to the deal, the budget stimulus will be no more than ¼ % of GDP next year.
- **The ECB** is fully prepared to do whatever it takes. But not now. However, if the inflation outlook does not improve, the Bank will do something, soon. The deck is cleared for a symbolic cut in its signal rates, and more quantitative easing, in September
- **UK manufacturing** companies are reporting a sharp decline in orders, both foreign and domestic
- **Unemployment in Sweden** may have bottomed, and the KI survey fell further in July, now signaling less than 1% growth
- **The Norwegian LFS (AKU) unemployment rate** rose more than expected in May but is still trending down, due to a lower participation rate, not an increased employment rate. **SSB's Norwegian manufacturing survey** confirms a mild slowdown but more companies are reporting lack of labour – and fewer lack of demand

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

Global foreign trade rose in May but has been trending down since Q3 last year

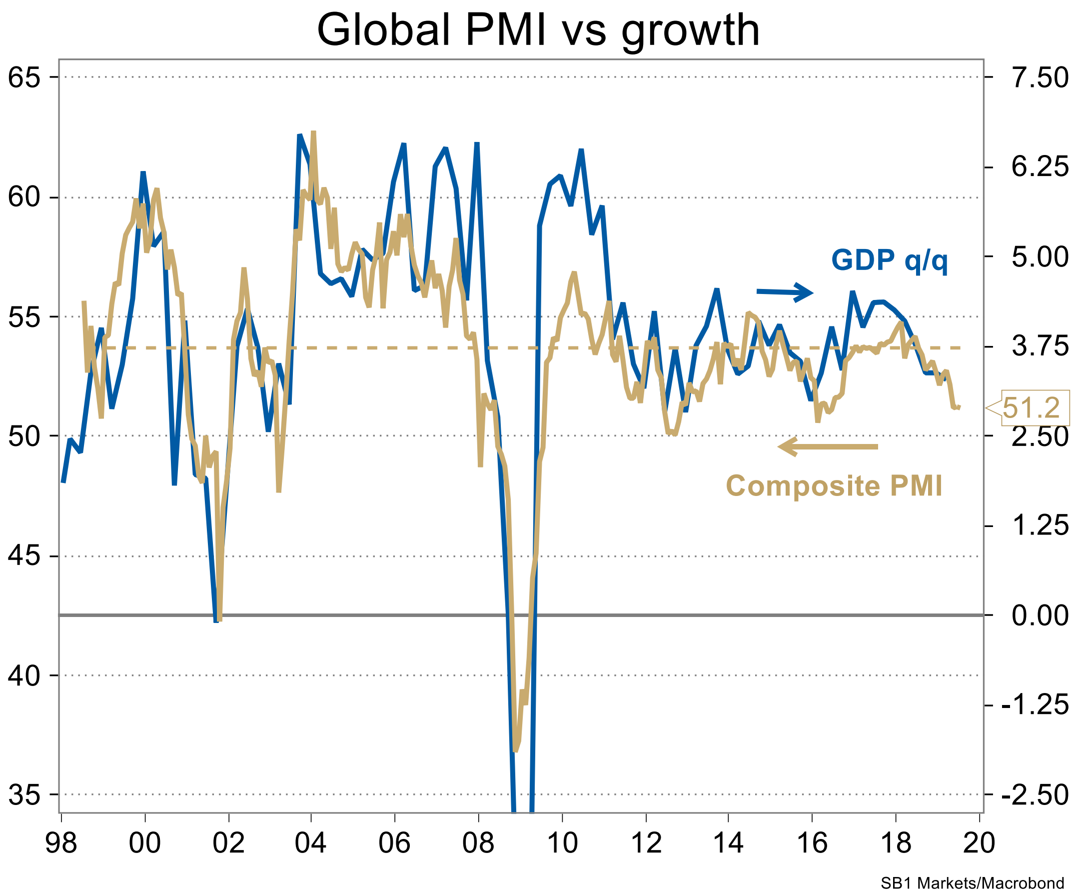


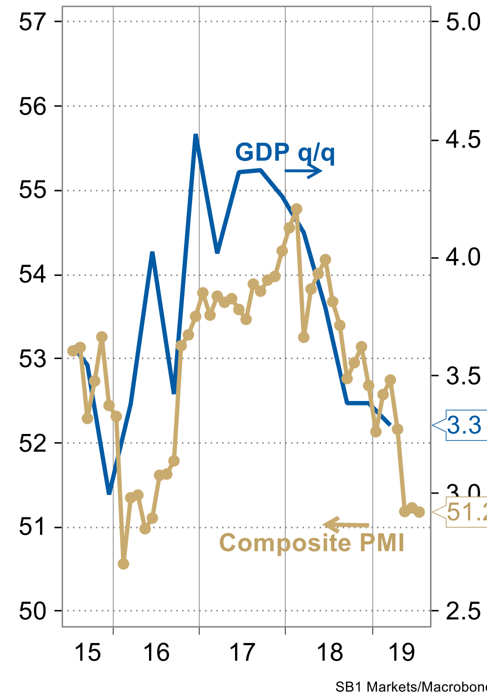


- We still have still too few data point for retail sales and manufacturing production in June but our estimate implies decent growth from May. Retail sales have slowed somewhat but signals that consumption is still supporting the global economy – and sales accelerated in June

Global PMI (probably) probably stable in July too, signals below 3% global growth

The PMI was lower in both 2012 and 16' but the cycle is more mature now, and the PMI trends down



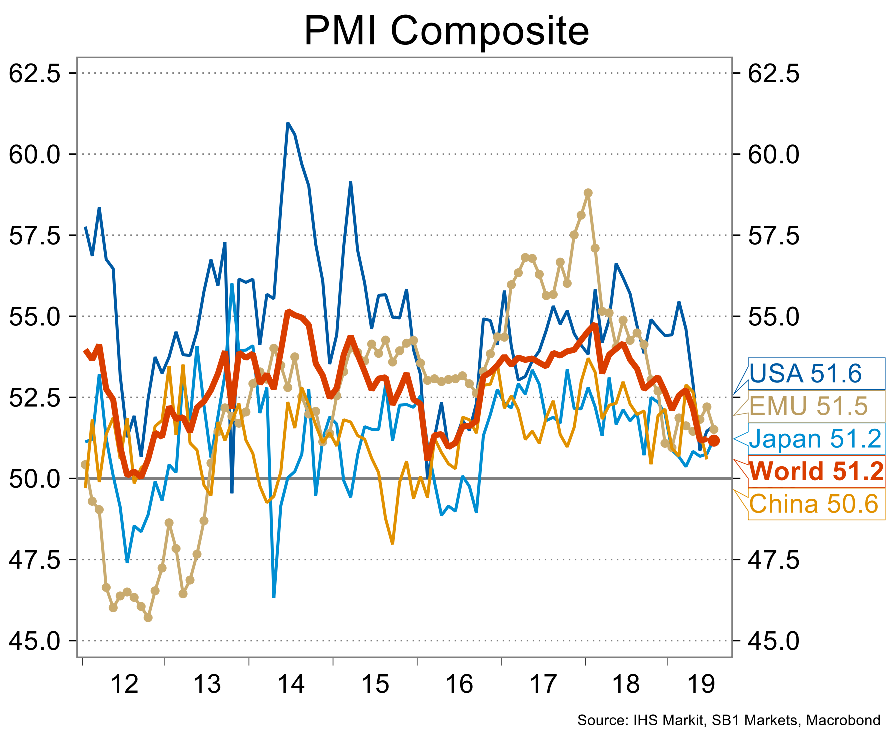


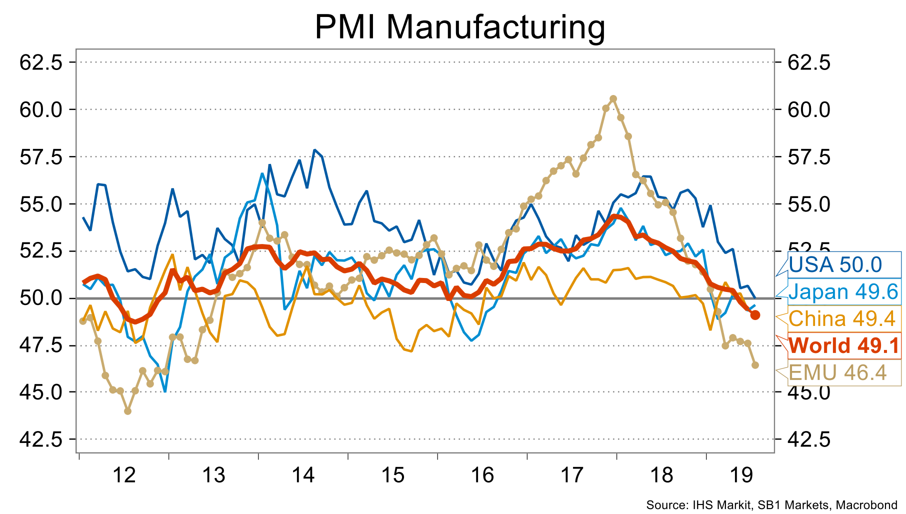
Our estimate is based on the preliminary composite PMIs from EMU, Japan and US,. The estimate is uncertain

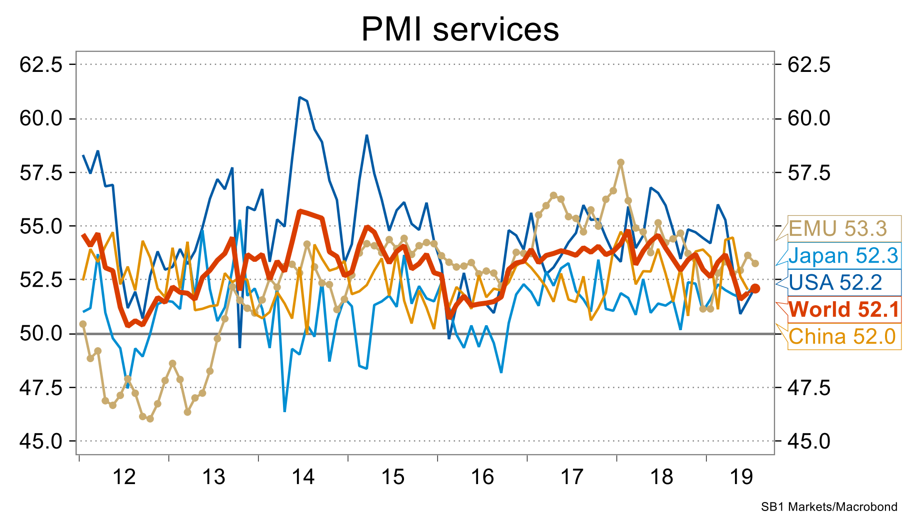
- We estimate a global composite PMI at 51.2 in July, unchanged from June (and May), at the 1st decimal (but marginally down m/m, the lowest level since June 2016
  - » The PMI has fallen by close to 4 points from the Jan 18 local peal, equalling more than a 1 pp slower global GDP growth. The manufacturing PMI signals a 20 pp slowdown in global EPS (earnings per share), down to zero

US and Japan contribute on the upside, EMU at the downside

The global manufacturing further down, weakest since 2012; services probably marginally up



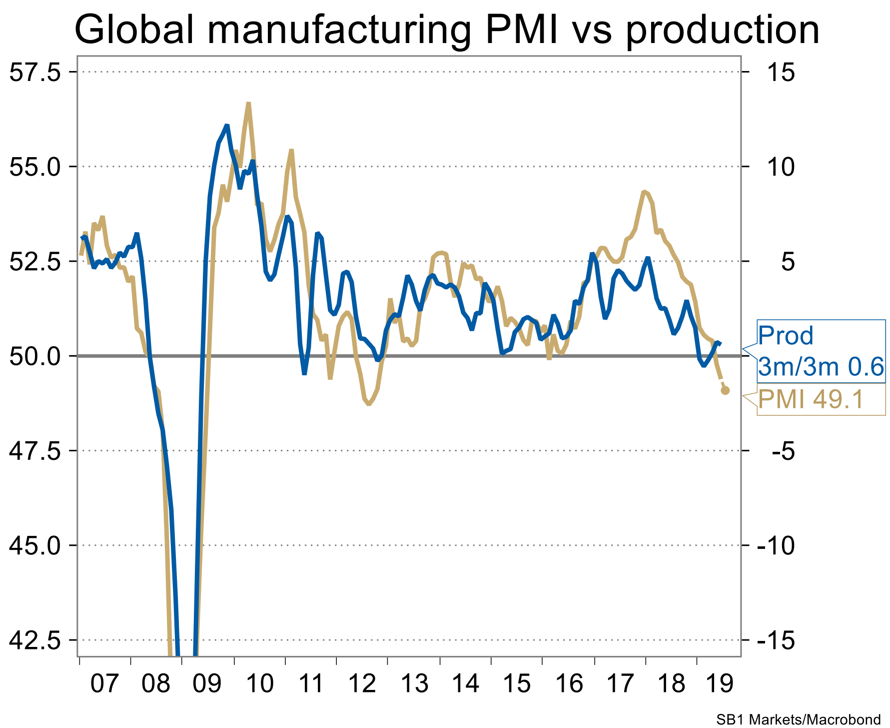




- Memo:
  - » The last obs for world indices for total, manuf. & services PMIs are based on prelim. data from the US, EMU, Japan
  - » The estimate is uncertain,
  - » China has not yet reported any June PMI data

Global manufacturing PMI indicates stagnating production

We estimate a 0.3 p decline in the manuf. PMI in June, to the weakest level since 2012

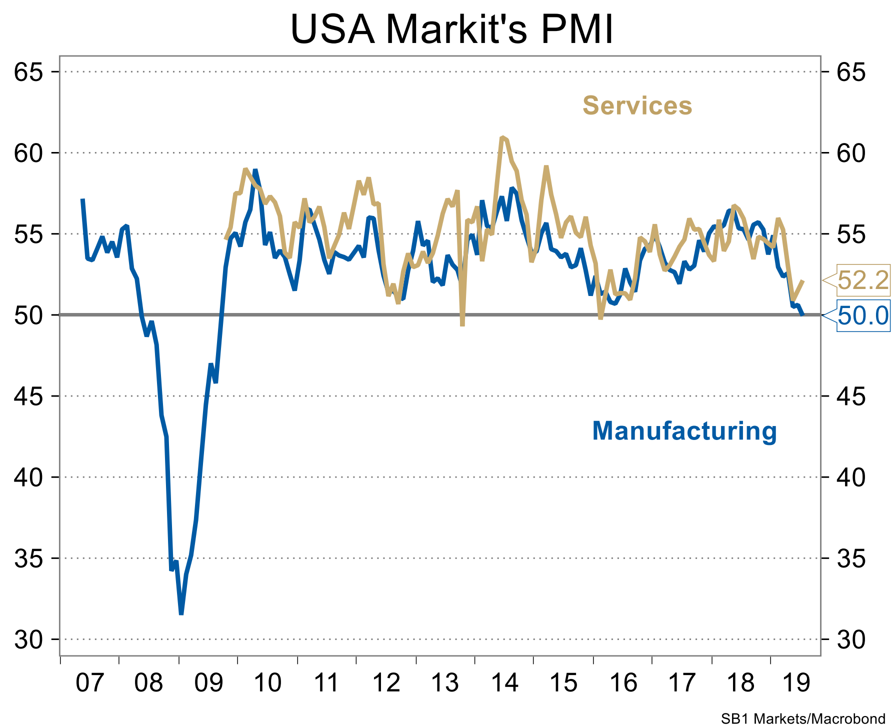


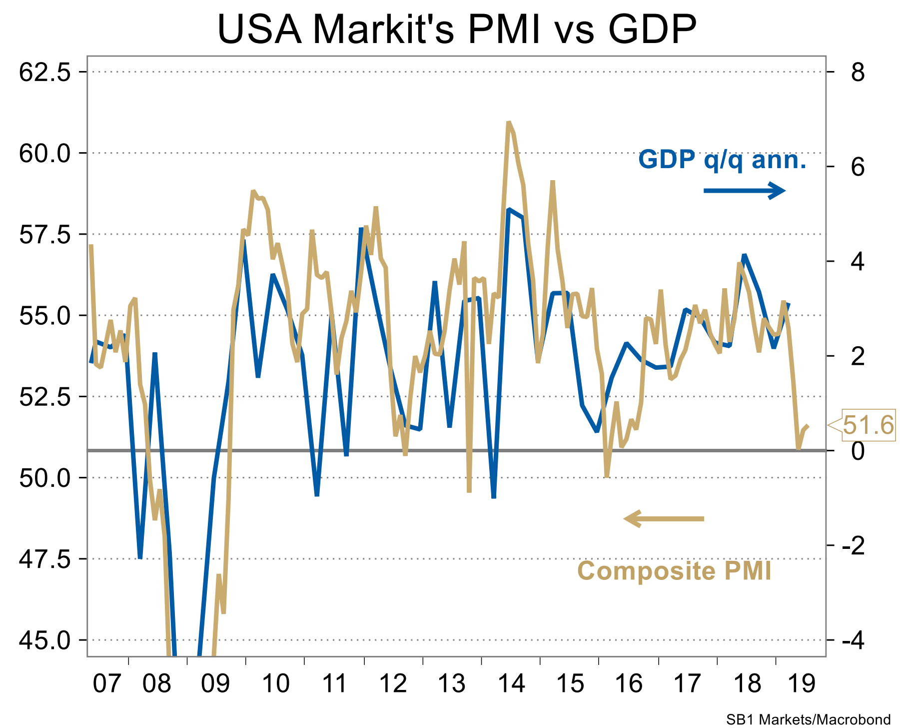
- Signals a 2% pa. decline in global manufacturing production

… And the PMI has been too upbeat the past two years…

Still a below 1% growth message, manufacturing surprisingly down

The further decline in manuf. PMI is surprising given sharp rebounds in early regional Fed surveys



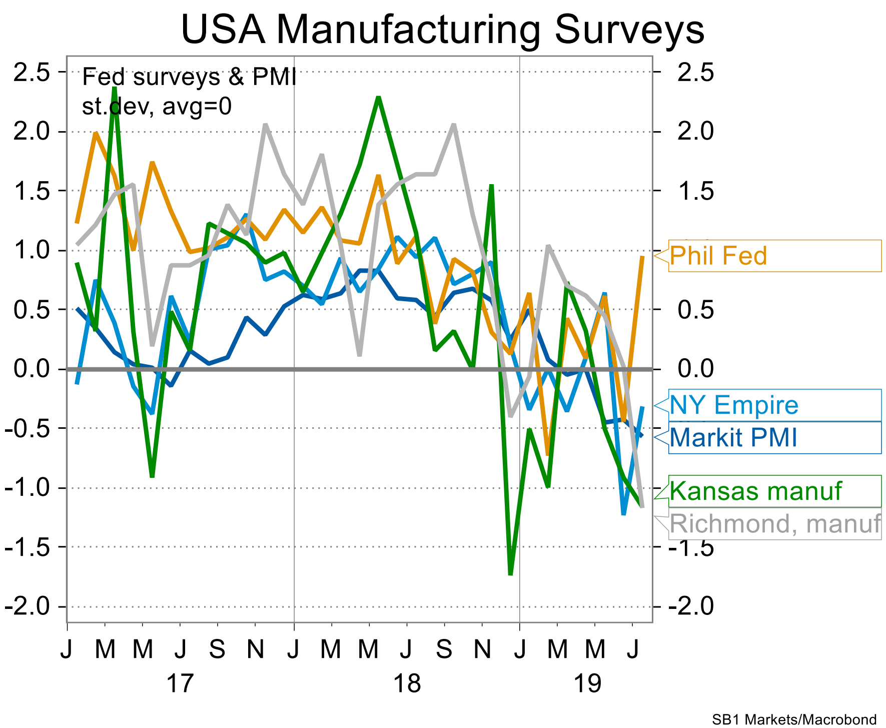


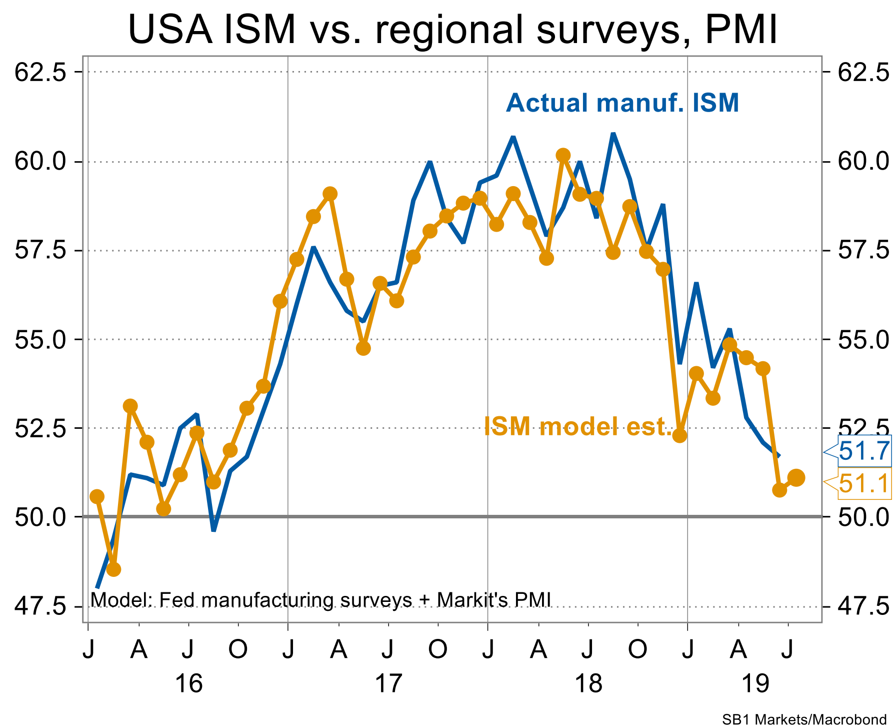
- The manufacturing PMI fell 0.6 p to 50.0 in June, expected up to 51. Given the NY & Philadelphia Fed surveys, the decline was surprising. However, other regional Fed surveys fell in July
- The service sector index rose 0.6 p in July, as in June, to 52.2. The level is the lowest since 2016, and sharply down from 55-level in Q1. The composite strengthened by 0.2 p to 51.6, also the lowest since 2016. The level signals a below 1% GDP growth pace into Q3
- Domestic manufacturing orders grew a tad faster, foreign orders slowed – in July. However, the main contrition to the slowdown recent months has been a lower growth in domestic orders, while the weakening of foreign orders has been much softer – signaling that domestic demand, not problems abroad explains most of the downshift. The GDP report confirmed that business investment was the culprit

SpareBank 1 MARKETS

Two up, three down; ISM marginally up in July??

Highly diverging regional Fed surveys/PMI: In sum slightly up, due to NY & Phil Fed



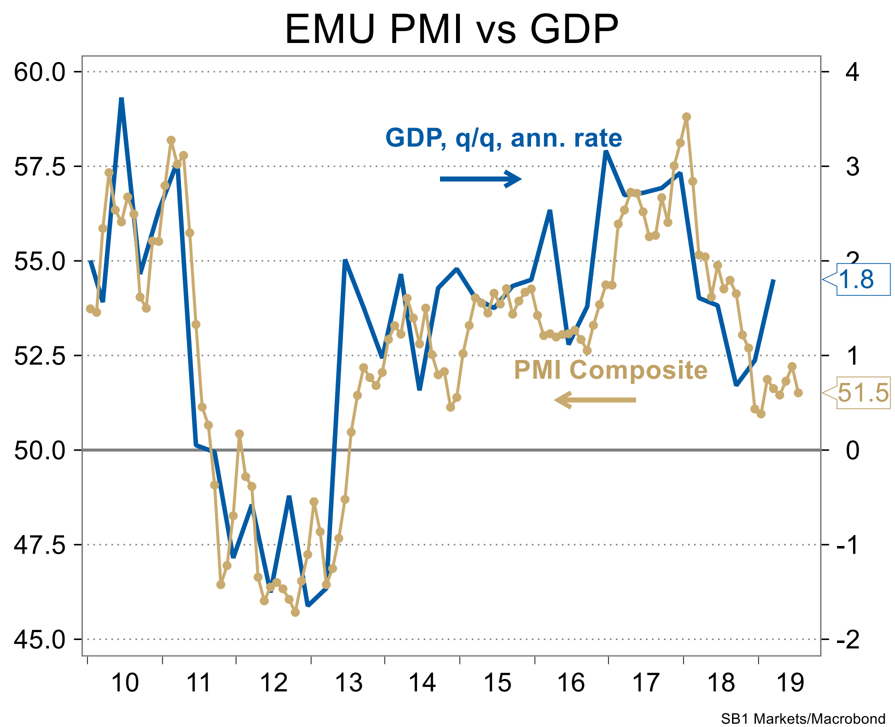


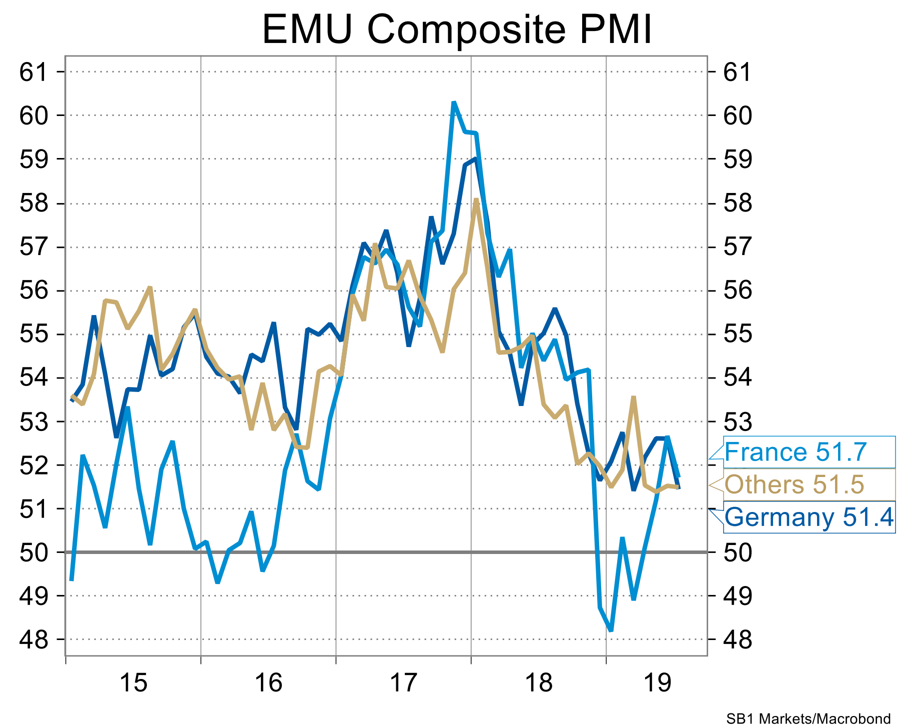
- Phil Fed's manufacturing index rose sharply in July, by almost 1.5 st.dev (a large cycle is 4 st. dev, from peak to trough). NY Fed's index also rose quite a lot but less than the almost 2 st.dev nosedive in June. However, the Kansas and Richmond Feds' surveys fell, as did Markit's PMI
- In sum, our model yields a small uptick in the July manufacturing ISM

SpareBank 1 MARKETS

Eurozone PMI down, more than half of the (very modest) 2019 recovery lost

Services still OK, but the manufacturers are reporting deteriorating conditions

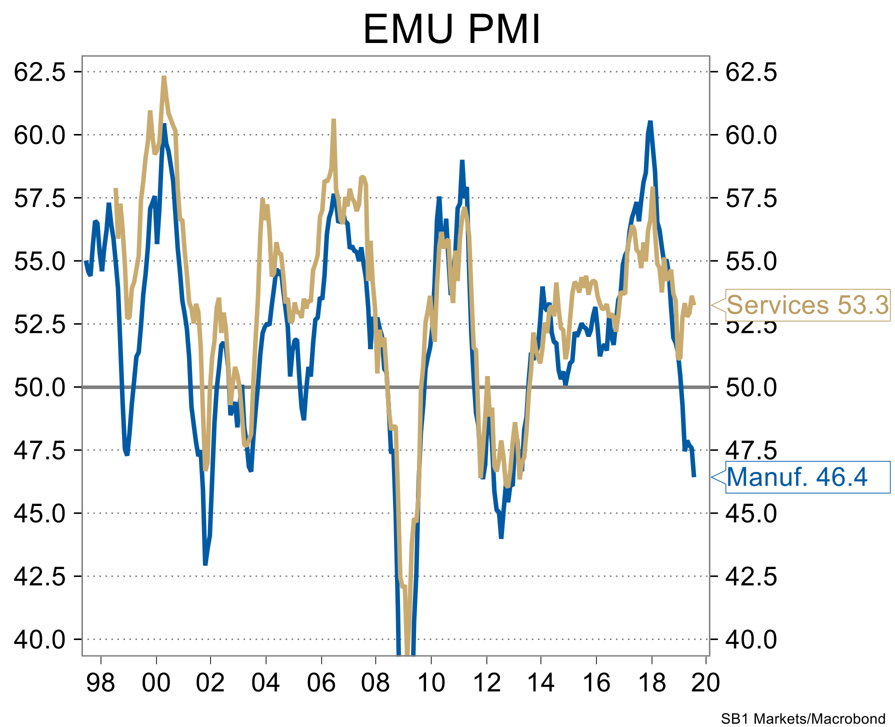


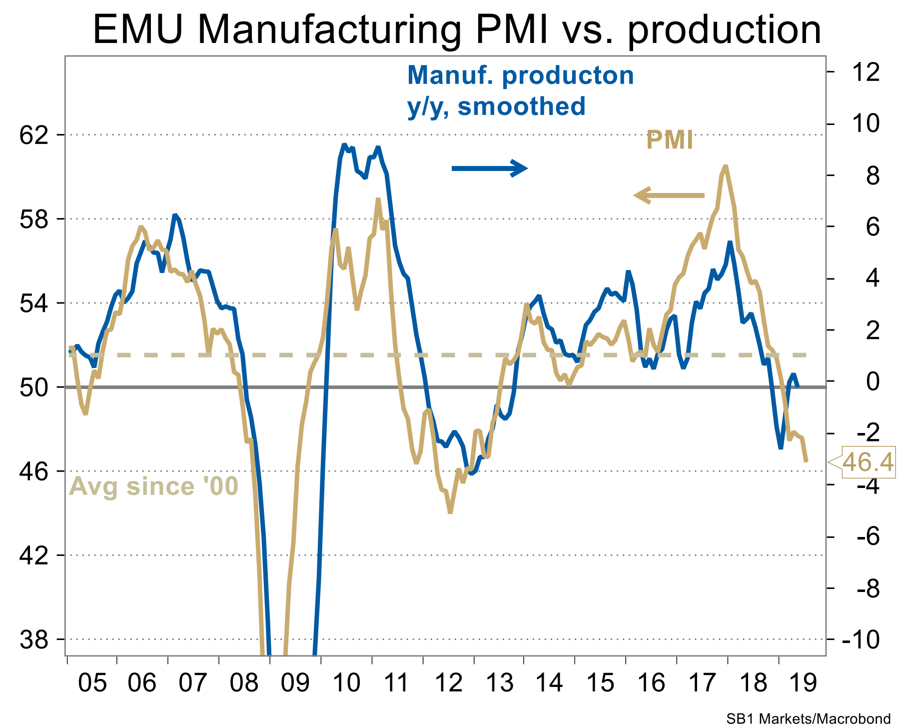


- The preliminary EMU composite declined by 0.7 p to 51.5 in July, expected unchanged. The index is up just 0.5 p from the January local trough. The index signals meagre growth, at some 0.5%
- The PMIs in both France and Germany fell in July, while the implicit estimate for the other countries was flat
- Manufacturing is the weak link in the chain – with Germany as the weakest – the manuf. PMI fell 1.2 p to 46.4, to the lowest print since Dec 2012, during the ' euro crisis', indicating a continued – and faster – decline in production. EMU services are still reporting OK growth, even if the index fell in July

The manufacturing contraction deepens; services remain resilient

The manufacturing PMI almost fell sharply in July, to 46.4 – signalling declining production

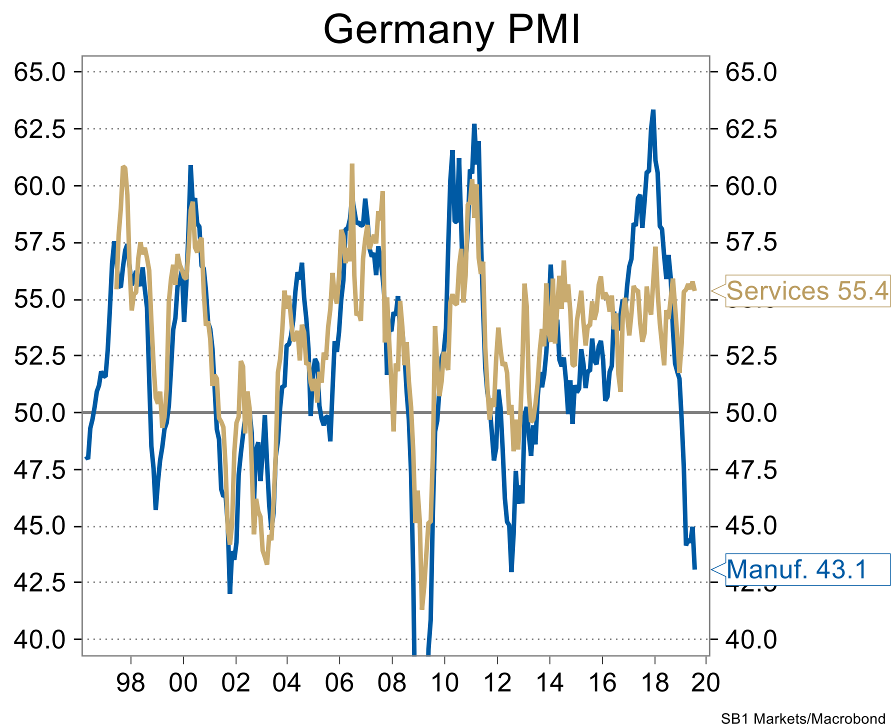


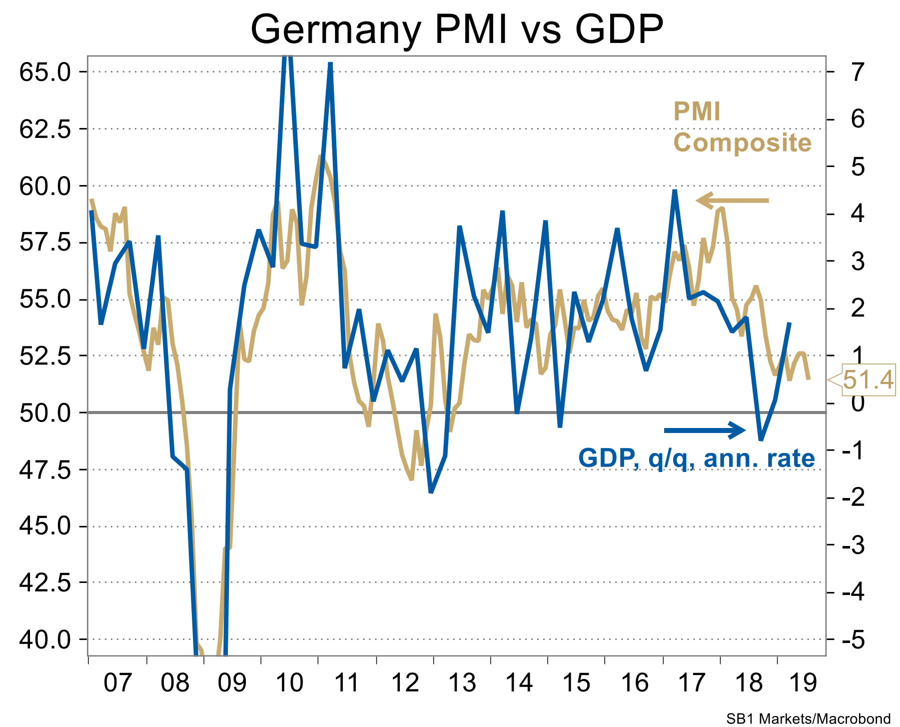


- Manufacturing production stabilised in Q1 (up 3.4% following the Q4 slump), and so far a flat Q2 print is reported (but no June date yet). The PMI indicates a contraction in Q3 (if not already in Q2, if June was weak)

Services still STRONG, the manufacturing PMI even WEAKER in July

The composite surprisingly down 1.2 p to 51.4, indicating 0.5% growth

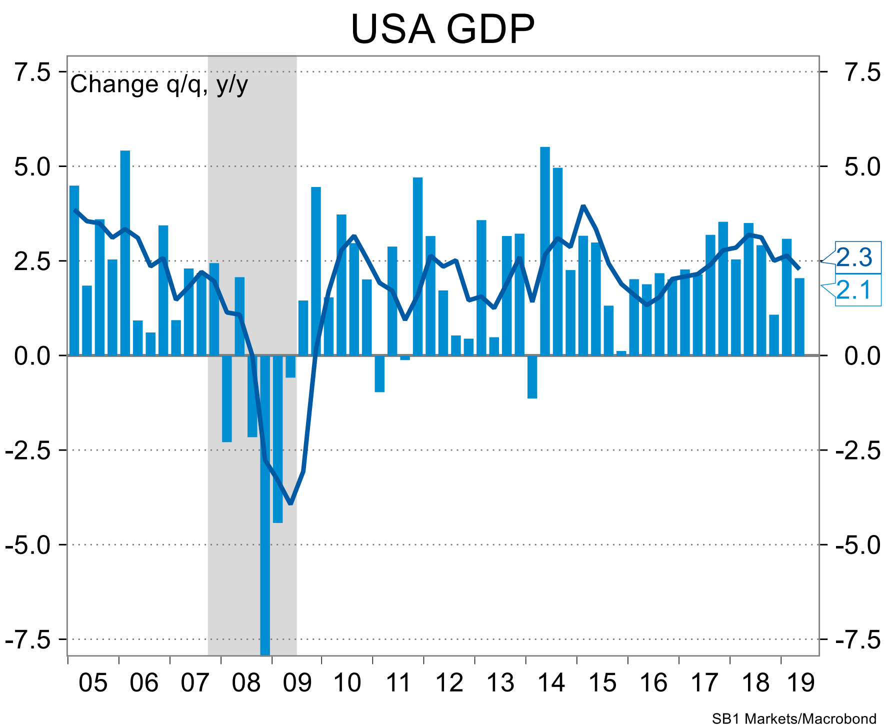


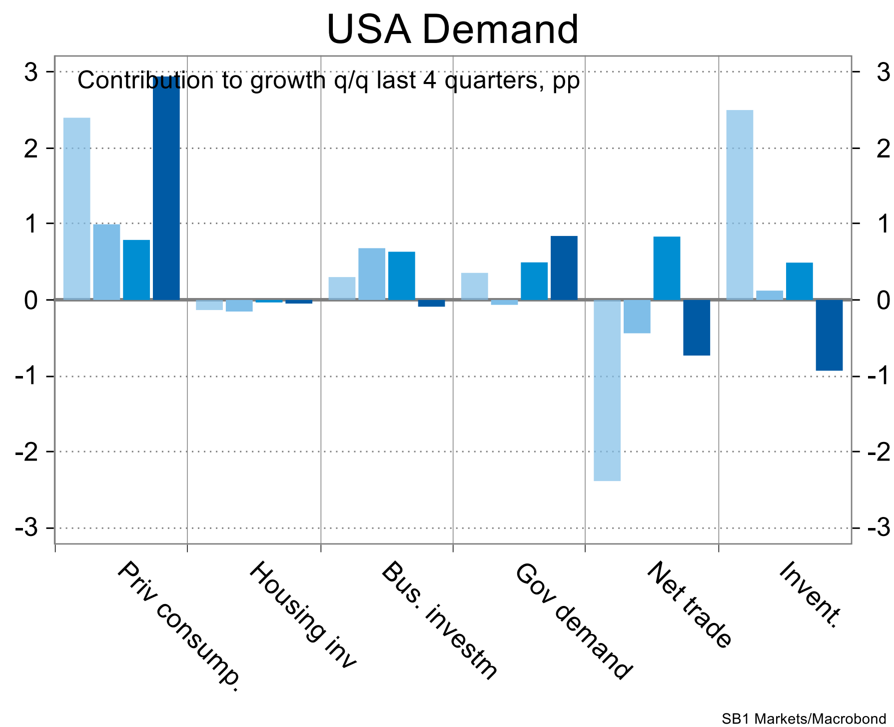


- The manufacturing PMI fell 1.9 p, to 43.1, the lowest level since one month in 2012, during the euro crisis. A smoothed index is at the 3rd lowest level in 20 years (since the German PMI was established)
- The service fell just marginally and continues to note solid growth in services. The discrepancy between services and manufacturing has been larger just during two months in the midst of the Great Financial Crisis. So this is really special!

Q2 growth down but less than exp. – households (and the gov) saved the day

Business (and housing) investments down, a negative drag to GDP from net trade and inventories

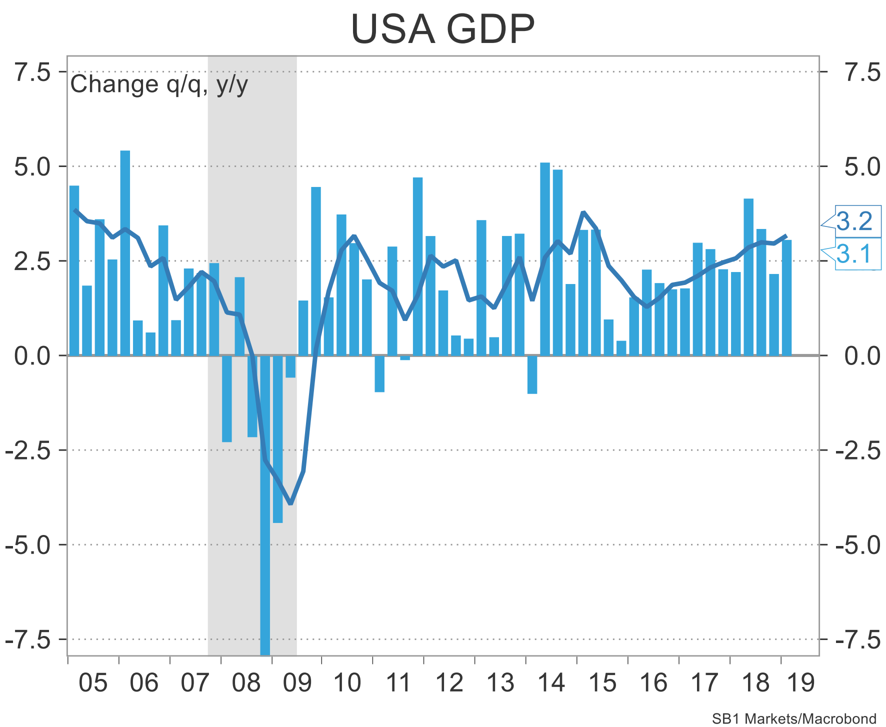




- GDP grew by 2.1% in Q2, better than expected (1.8%), and above NY, Atlanta Fed nowcasters (1.5%-ish). Still, the annual growth rate fell to 2.3%, down from 2.7% in Q1 – which was revised down from 3.2%. The annual revision revealed that growth peaked in Q2 '18, while previously released data showed acceleration through Q1 '19! (check next page)
- Private consumption rose by 4.3%, contributing to 2.9 pp to Q2 growth, a tad better than expected. Government demand grew 5%, lifting GDP by 0.8 pp, highly unusual. Business investments fell marginally, even though immaterial investments continued upwards as construction investments fell sharply (also ex oil investments)
- Total labour costs grew marginally faster than nominal GDP – and core PCE inflation (Fed's price measure) accelerated to 1.8% from 1.2%. Even if growth has slowed, an interest rate cut should normally been far from a done deal given these growth/inflation numbers

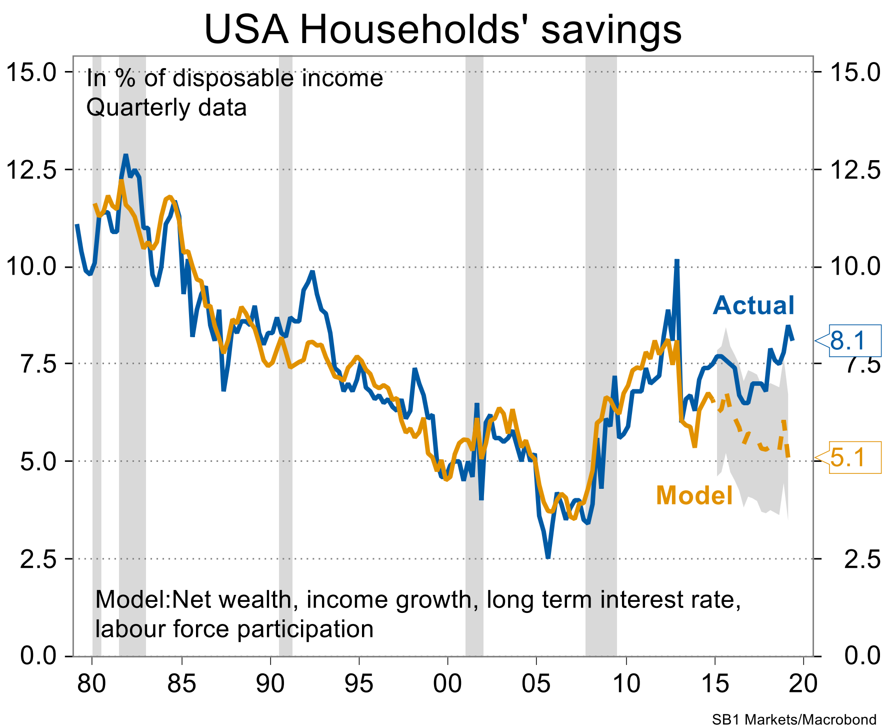
Oops: Wasn't growth at 3%, and accelerating?? Flip back, and check

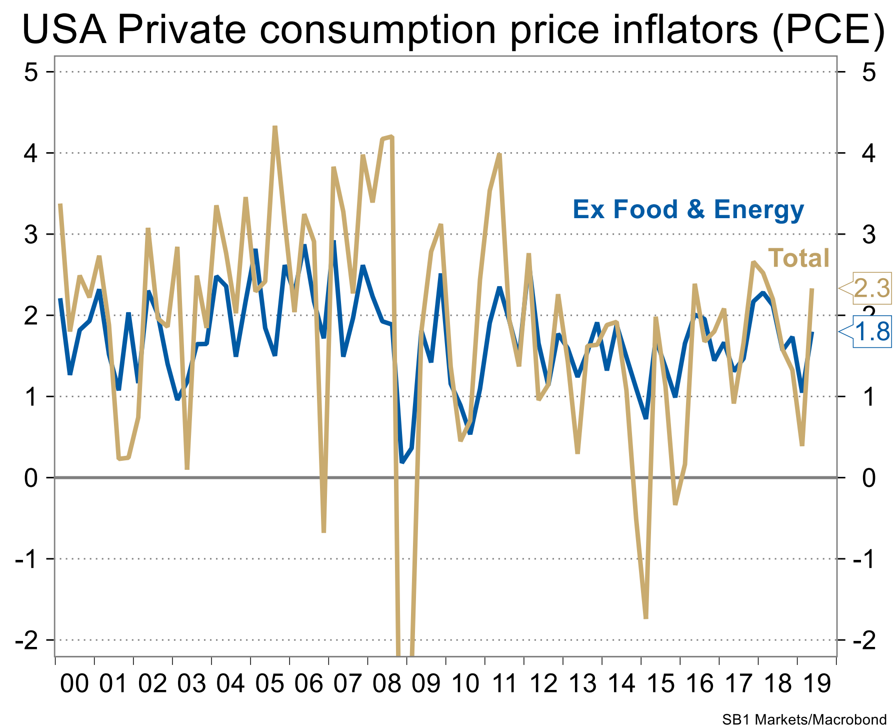
Here is how data looked like before the annual revision, growth had not peaked yet



Another BIG upward revision in the savings rate!

The savings rate fell in Q2, but the level has been revised up by 1.5 pp, signalling more robustness

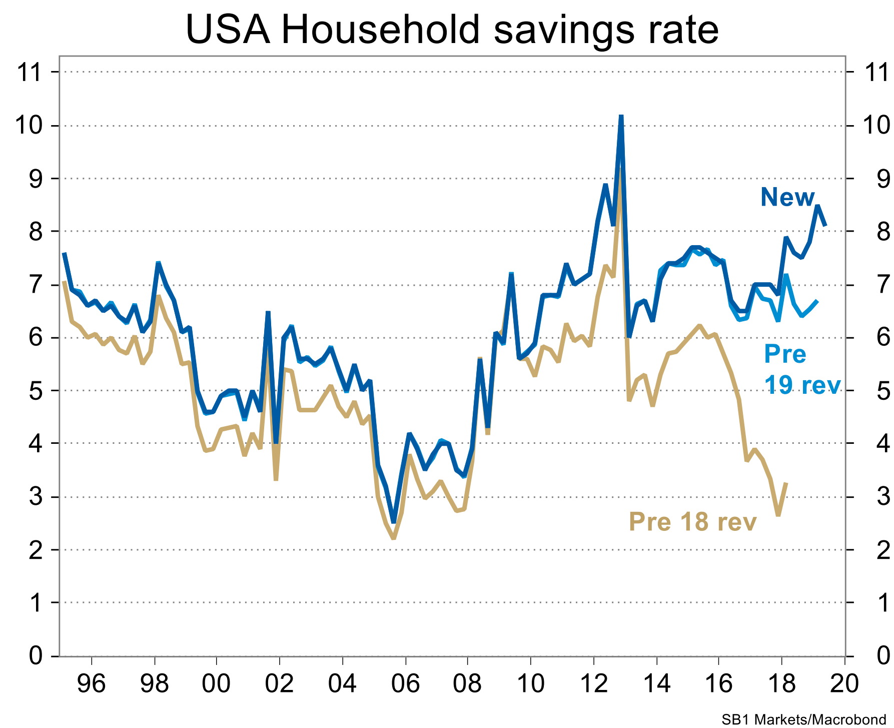


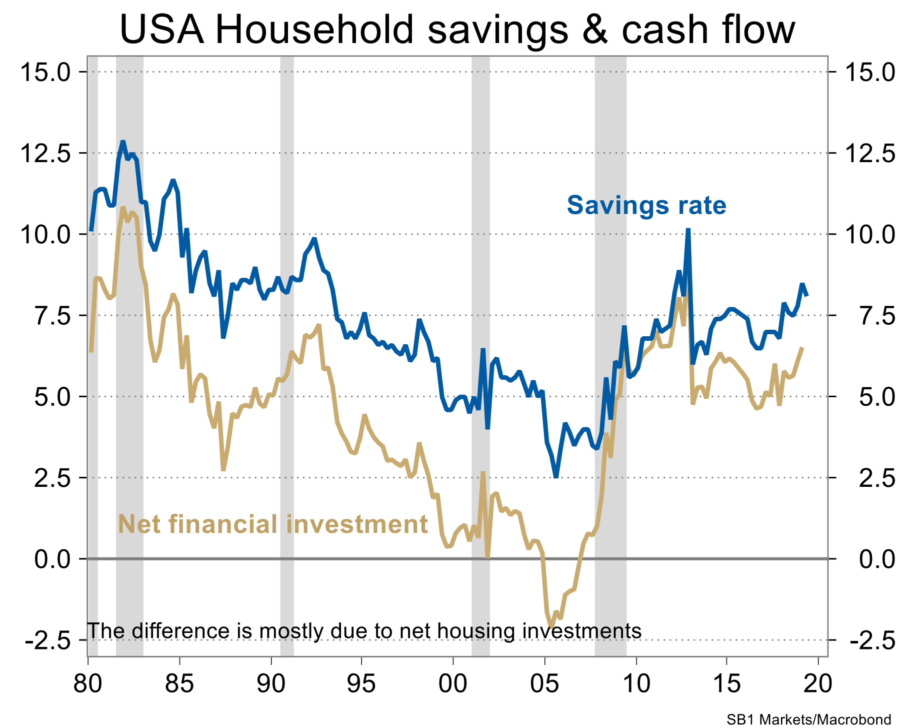


- One year ago the savings rate was revised sharply up due to new (and much higher) estimates of tax evasion. Now the savings rate once more is revised up, by up to 1.5 pp, and it was above 8% in Q2. Check the difference vs. the chart at the next page. Household cash flows are also much stronger than previously assumed. Good news, reduces the risk for a contraction in household spending
- The core PCE price deflator accelerated to 1.8% in Q2 from 1.1%, not that much below the Fed's 2% long term inflation target. The total PCE deflator accelerated to 2.3%

The savings rate has been revised to 8% from 3%, via 6.5%

Savings are the discrepancy between two large numbers – and is a moving target…

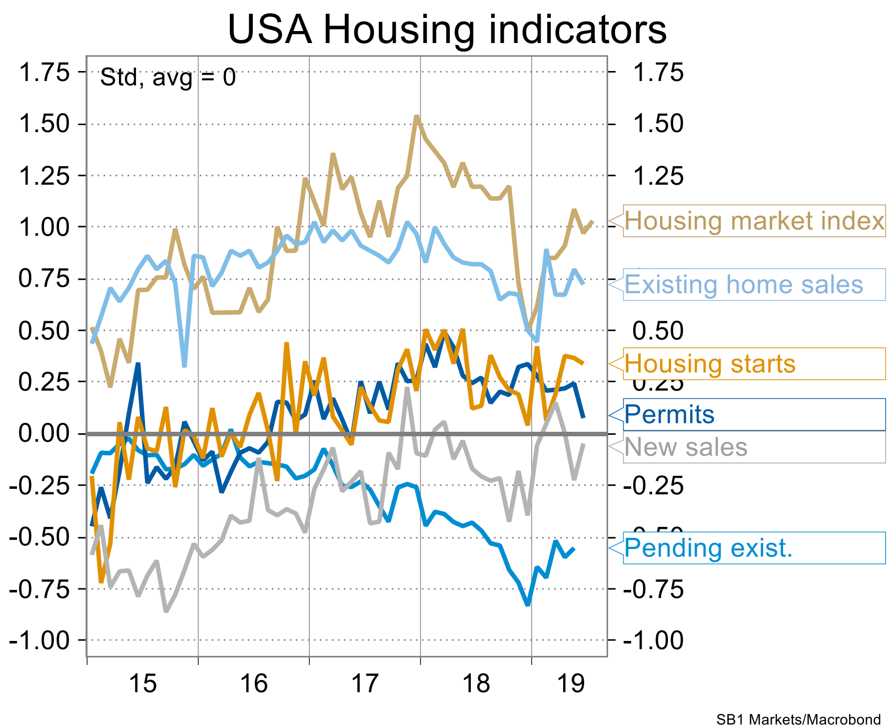




- Household income growth was revised up in the 2019 annual revision, and more than consumption. The savings rate was revised from 6.7% to 8.5%
- More of the tax cuts have been saved – and households are more robust than the previous data indicated; the new savings rate is well above the average of the past decades, at above 8%. The increase in household net financial investment rate explains why the huge increase in the public sector deficit has not sent the current account deficit down the drain

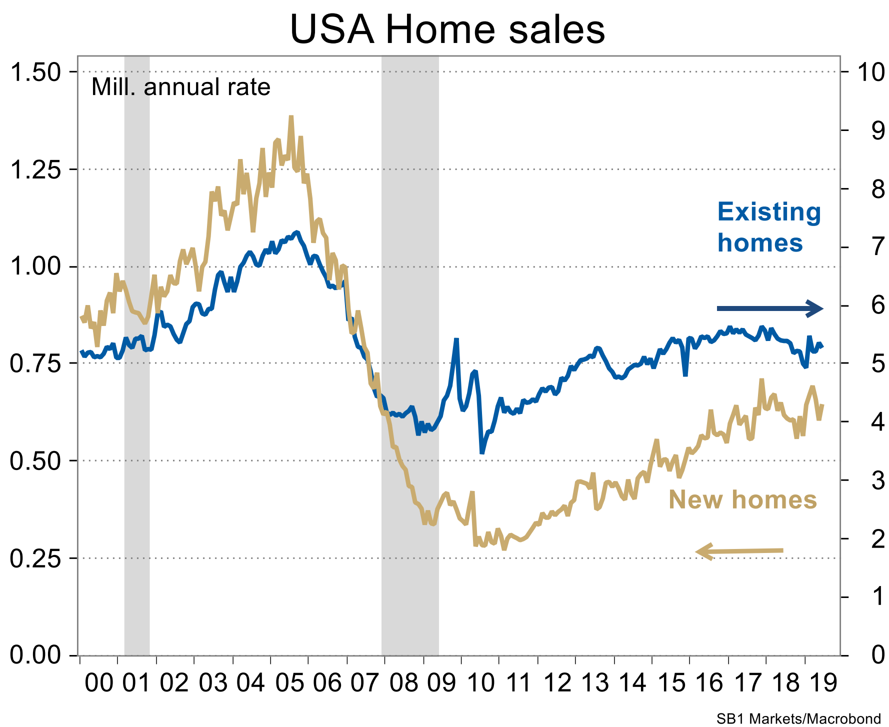
Most housing indicators back to flat to a downward trend

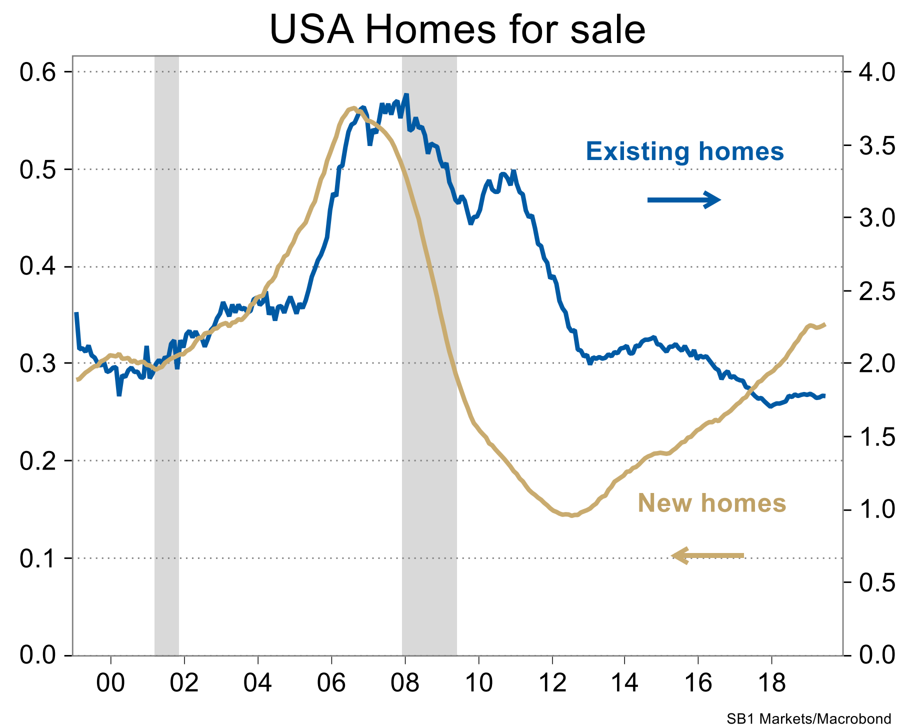
New home sales up, from a downward revised level, existing homes marginally down



New homes sales up in June, from a downward revised May

Trend past two years flat, at best but the level is not that high

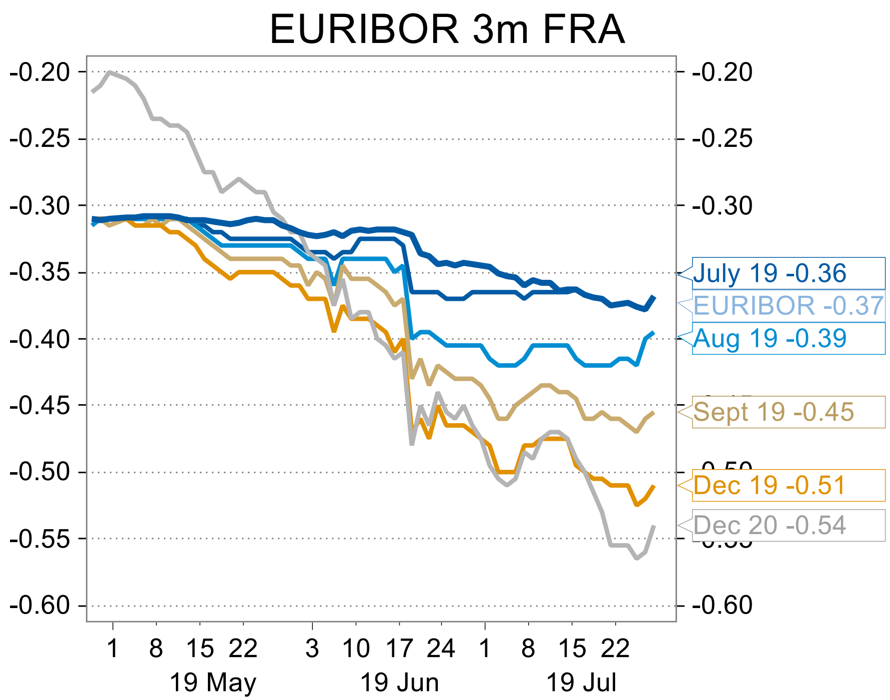


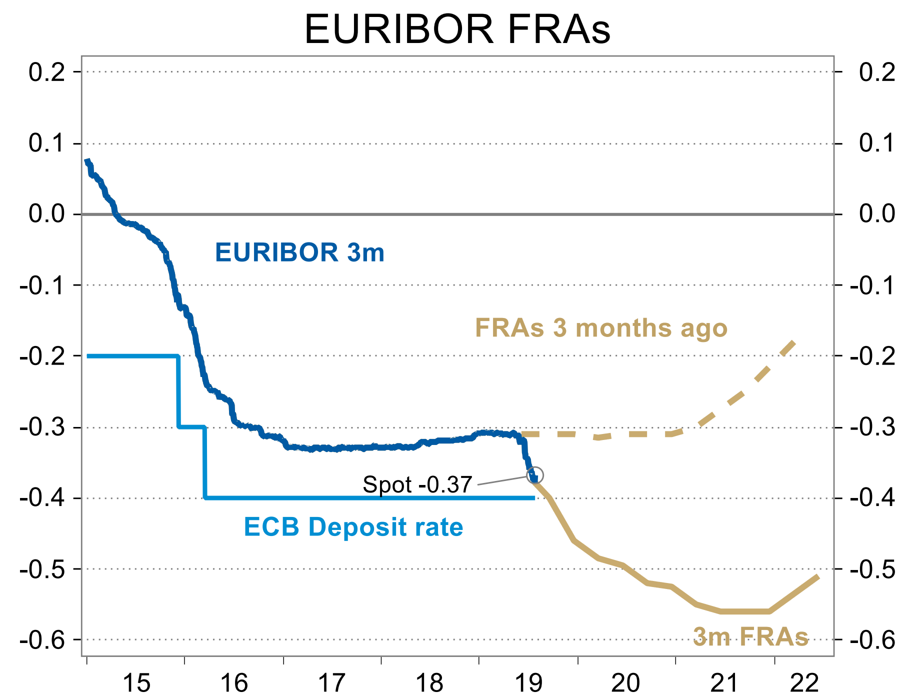


- New home sales rose to 646' in June from 604' in May, expected up to 659' up from prev. reported 629'. In sum 3% lower than expected. Following the decline the two previous months a part of the increase earlier in 2019 is reversed – and the broad trend line over the past two years is flat
  - » The number of unsold homes rose from 2012 until Feb this year but has been since (but rose marginally in June)
- Housing starts/permits are trending slowly down – and permits fell sharply in June (probably a one off but still)
- Existing home sales fell slightly in June, and marginally more homes for sale

ECB ready to act, but not now

Growth, inflation too low. All measures are being considered. Rate at present or lower level in H2-20

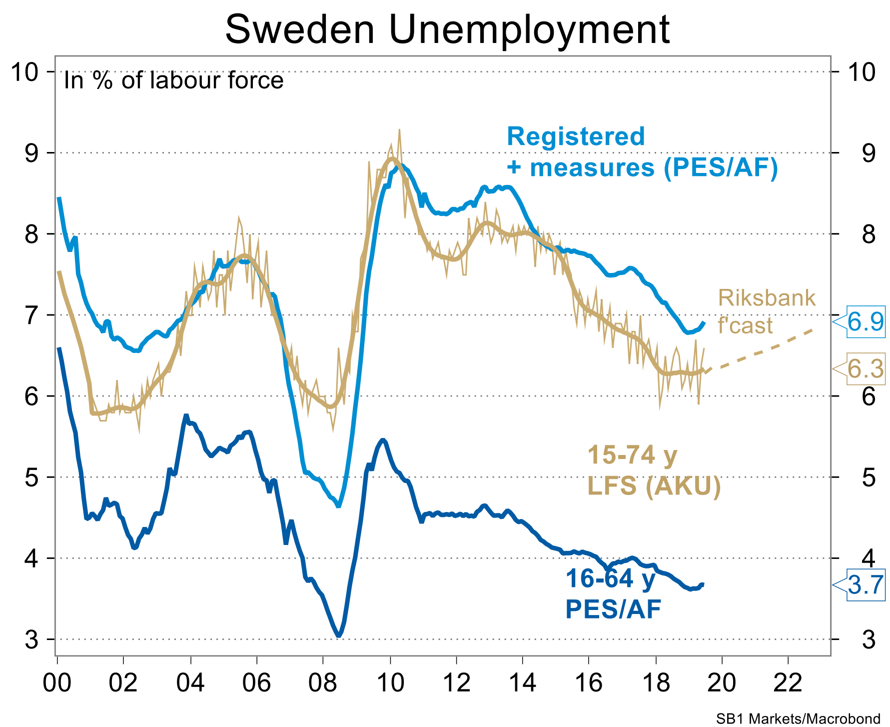


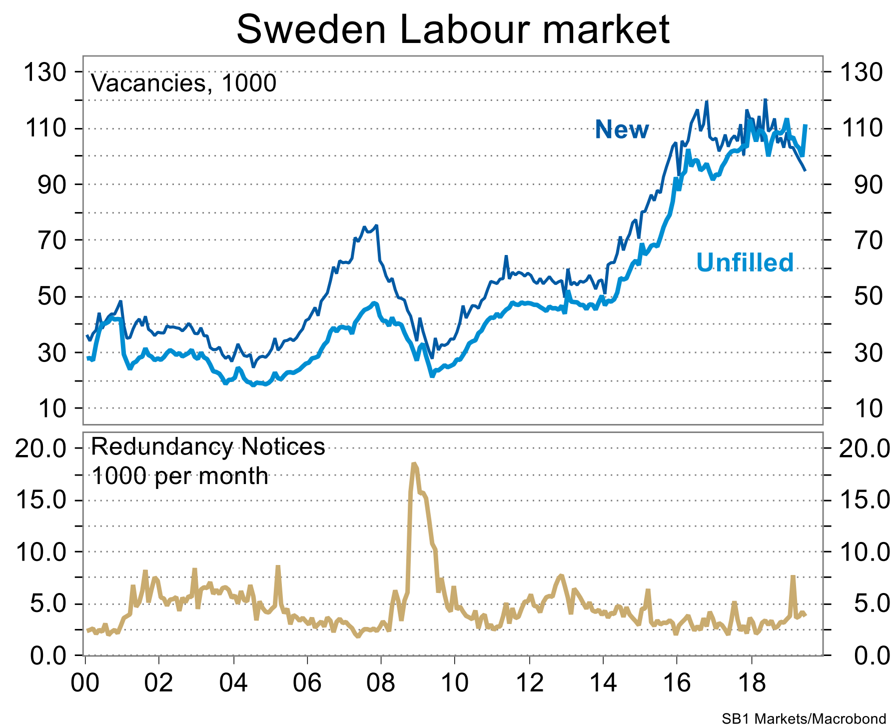


- Some had expected the ECB to act now but that was premature. However, Draghi & co clearly signaled that the bank was worried both about the growth outlook, especially in the manufacturing sector and for the decline in inflation expectations
- The bank is considering all available measures. Rates may be cut, asset buying programs extended.
- Most likely, the Bank will cut its signal rates at Draghi's last meeting, in September. More QE is likely too.
  - » The market is expecting the ECB to cut its deposit rate by 10 bps to -0.5% in September – and further down to approx -0.6%
  - » No doubt, other measures could have larger impact on the economy, than a symbolic cut even further down in negative territory
  - » Expectations for more gov. bond buying has no doubt contributed to the recent decline in bond yields all over Europe

Unemployment turns up?

Both registered and LFS unemployment up but more unfilled vacancies

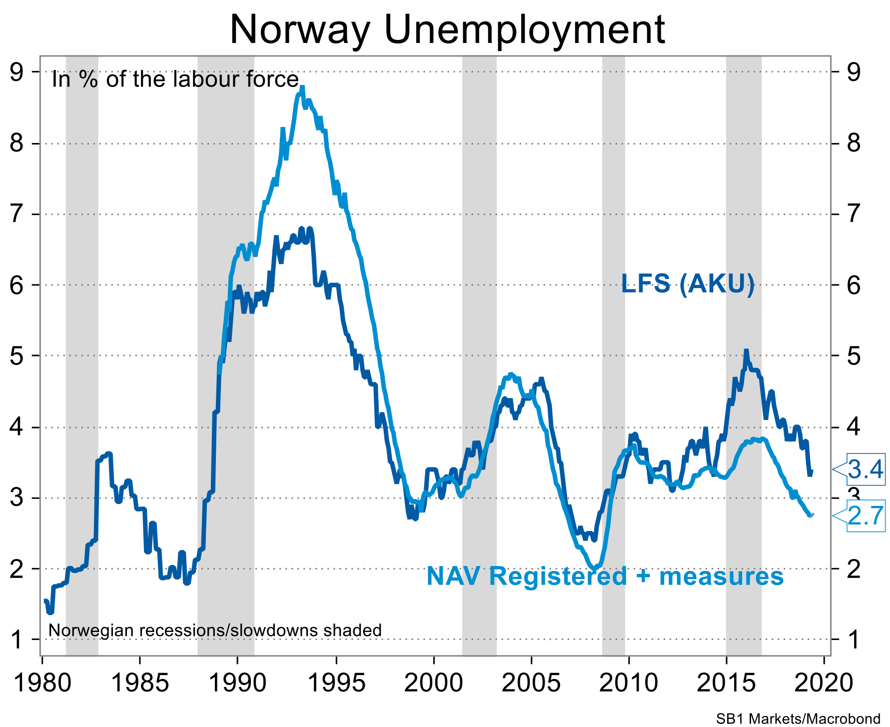


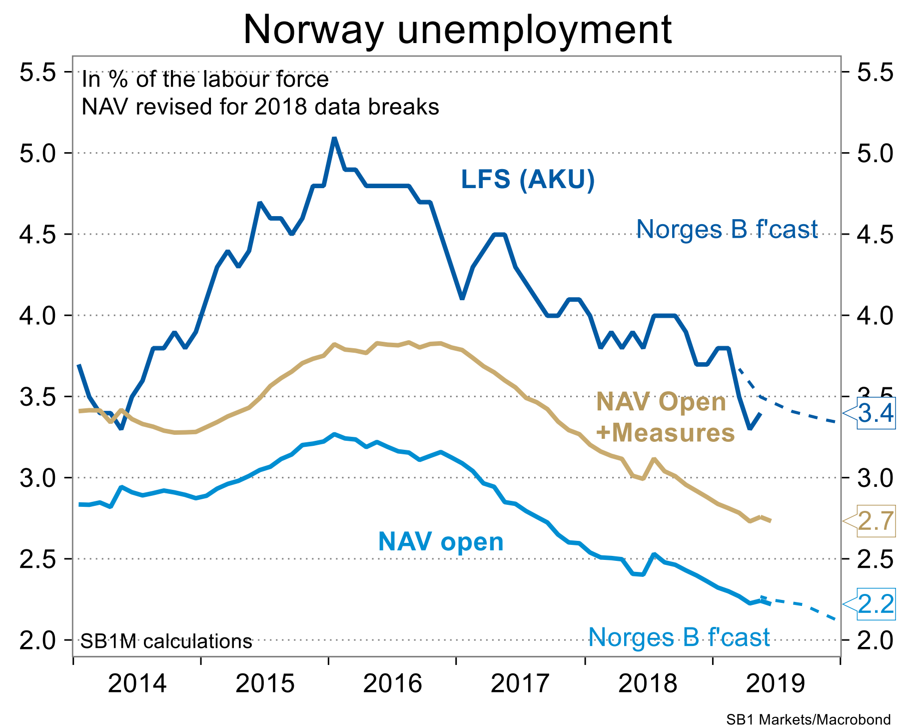


- The LFS unemployment rate rose 0.2 pp to 6.6% in June. The smoothed rate, which we prefer, was unchanged at 6.3%, but it rose slightly at the 2. decimal.
- Employment rose in June but less than the decline previous months, and it is barely up y/y
- PES/AF open (registered) unemployment rate is confirming a weakening labour market; it has turned (very) marginally up recent months
- The number of <u>unfilled</u> vacancies rose sharply in June, while the number of new vacancies continued downwards. We assume the trend is down for both, but leve4ls are still very high. The number of redundancies has fallen back after a temporary spike but may be trending slowly up

LFS unemployment up to 3.4% but still below NoBa est; downward trend intact

April revised 0.1 pp up to 3.3%, and May at 3.4%, exp. 3.3% - down from 3.8% in Q1

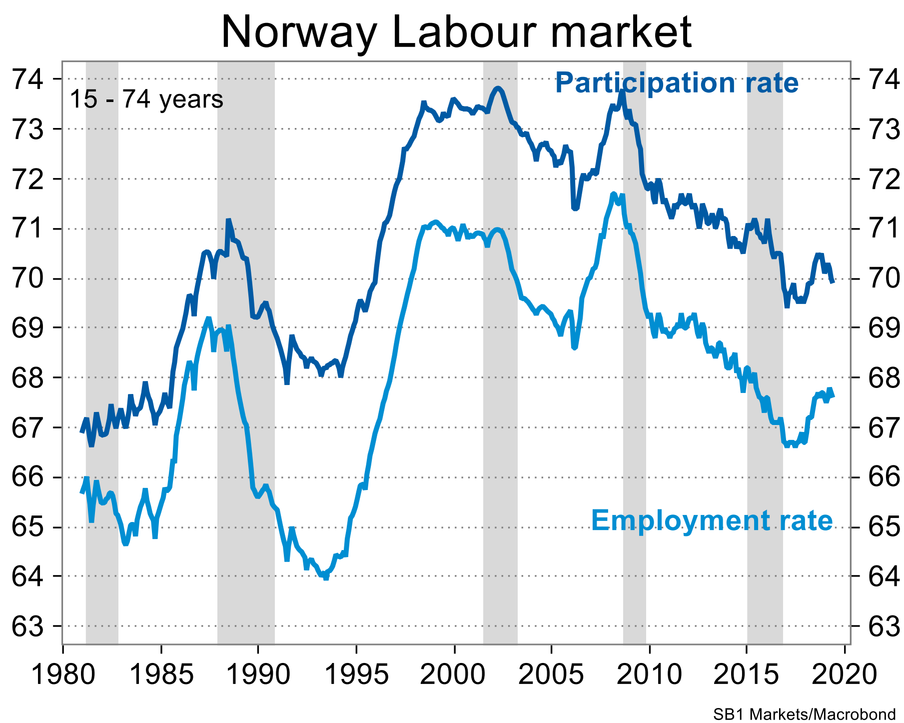


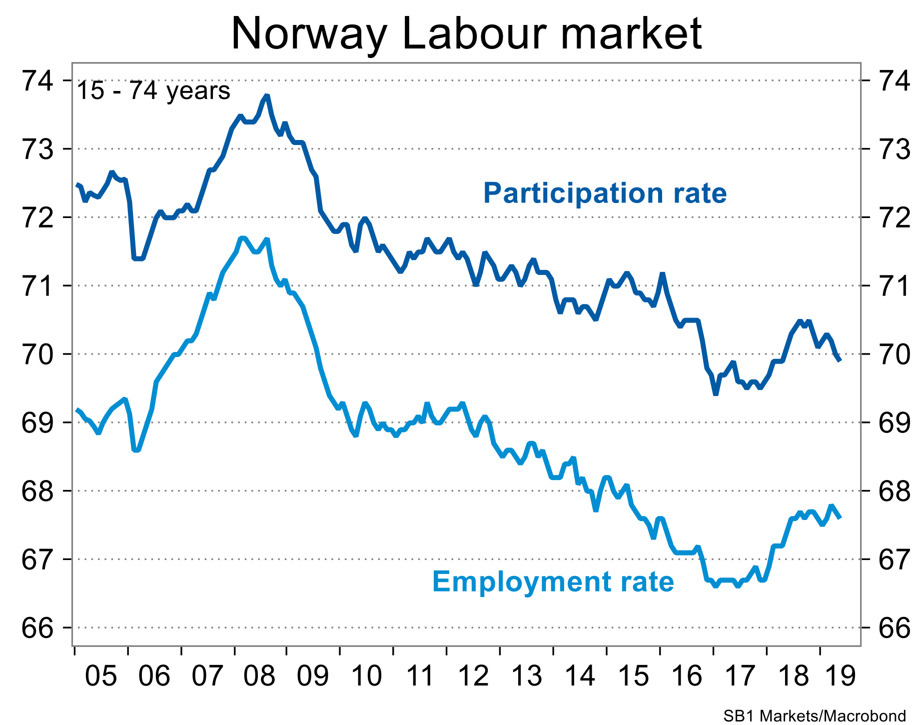


- LFS (AKU) unemployment rose 0.1 pp to 3.4% in May (avg Apr – Jun) from an 0.1 pp upward revised 3.3% in April. Norges Bank assumed a 3.5% unemployment rate in Q2 in the June MPR. Even if the unemployment rate was 0.1 pp above market consensus, the trend is still straight down
  - » Employment fell by 5' m/m in May (3 m avg), and the annual growth rate has fallen to 0.9% from 2.1% in November last year – well below NoBa's f'cast. Labour market participation fell by 8' persons, thus, the entire upswing in the participation rate the past year is reversed! Indicates that supply is 'emptied' and the labour market is becoming tighter, an argument for an aggressive Norges Bank
- The LFS data confirms the steady decline which NAV has been reporting – and the latter is much less volatile

Labour market participation is retreating again! Limited growth potential?

The employment rate has almost flattened, participation is clearly declining

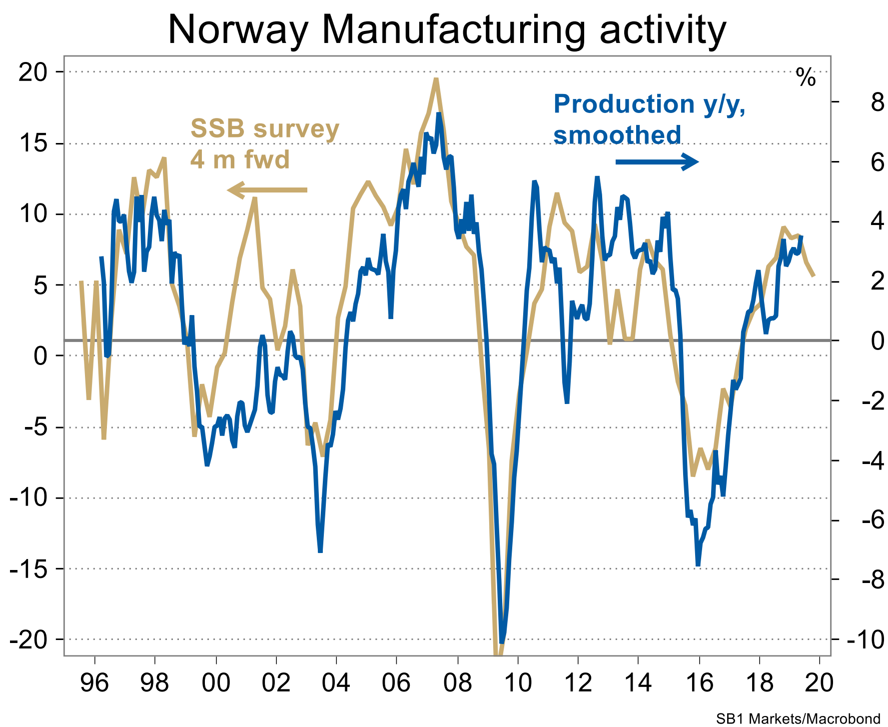


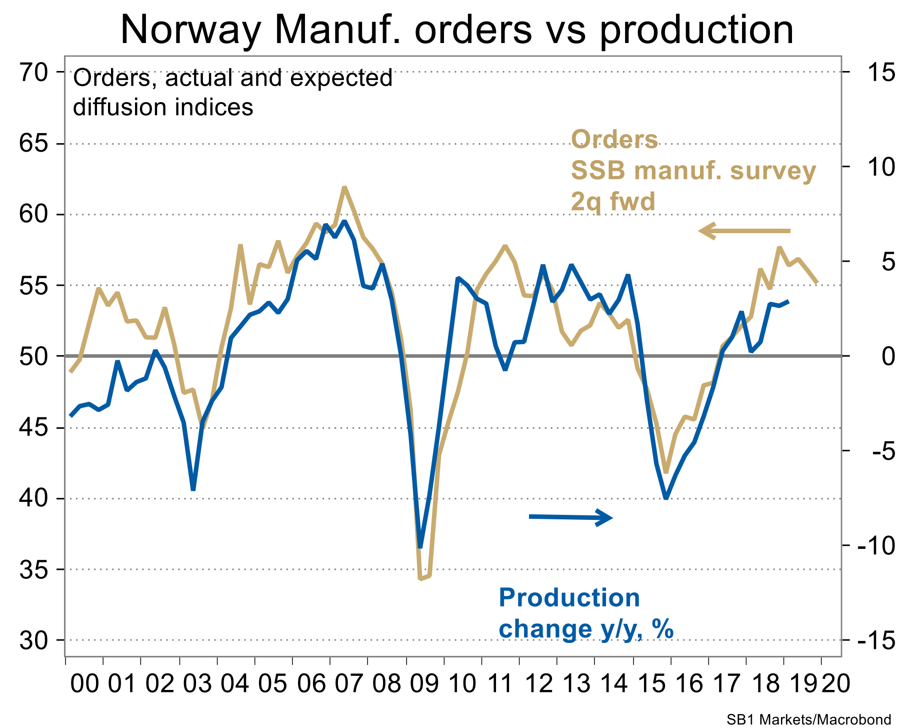


- The long term downturn in the participation rate and employment bottomed one 1½ y ago and both were growing strongly through 2018, up some 1 p.
- However, participation has pulled back for 7 months and fell steeply in April and May, in total by 0.6 pp from the last Oct. peak. The employment rate is down 0.1 pp in the same period – signalling a limited supply; participation is contracting without obvious weakening of demand – and more companies are reporting lack of labour
  - » Wage inflation is picking up, reflecting a strengthening labour market, and more is expected, according to NoBa's expectations survey

SSB's manufacturing confidence a tad down, still points to growth above trend

Slightly softer order inflows, both in oil/non-oil related sectors. Employment plans steeply up



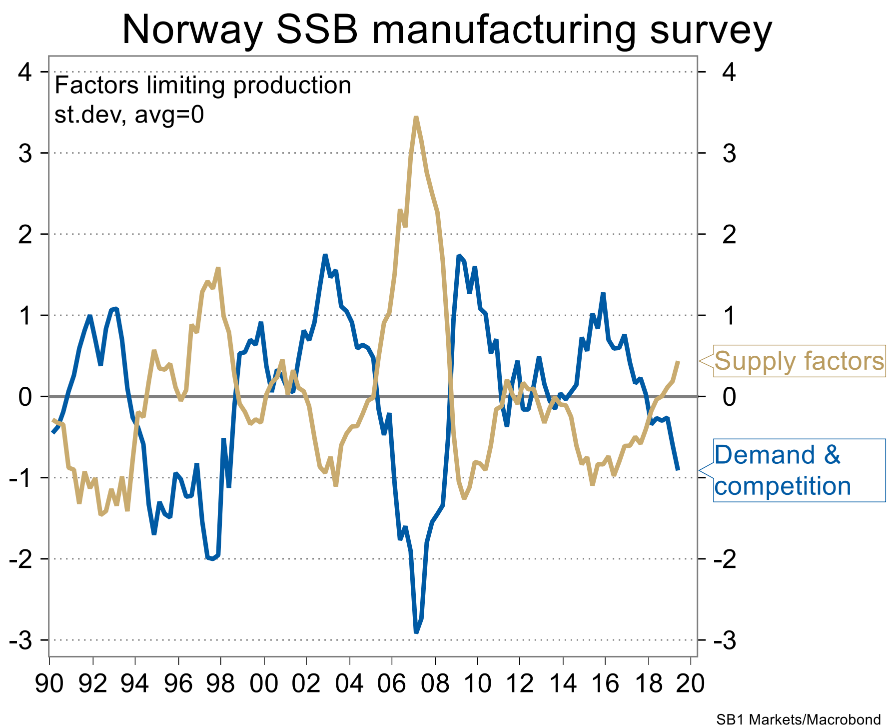


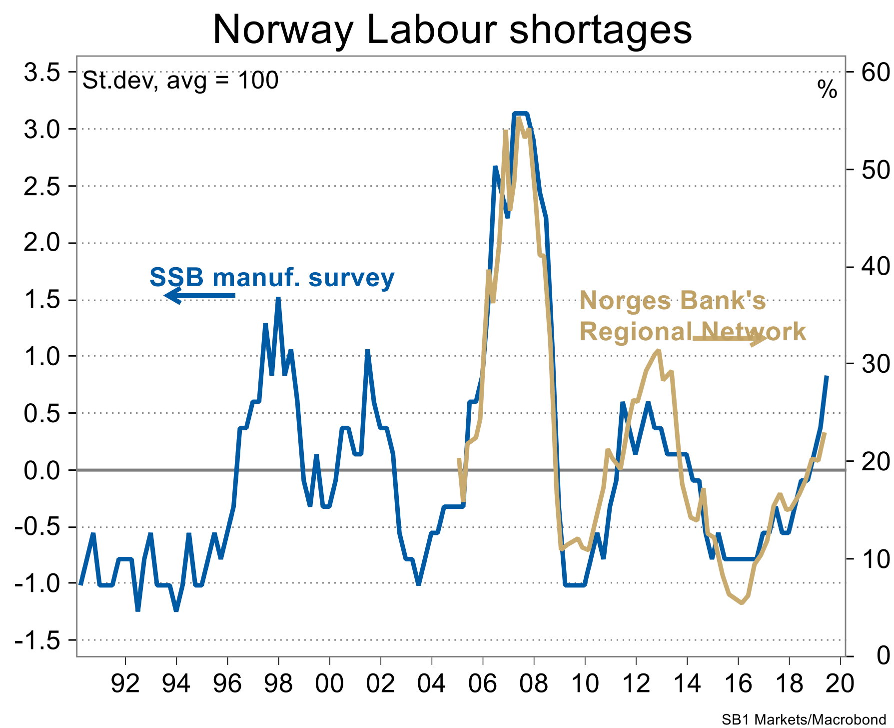
- The composite index in SSB's industrial survey (manuf. index) inched down to 5.6 in Q2, from 6.6, we expected down to 3
  - » The index is well into positive territory (above 0 indicates growth in output) and well above the average at 3.9. Thus, the survey signals growth in manufacturing production above the long term trend rate at 2¼ % and a GDP growth at2 ½ %
- Manufacturing businesses are noting marginally weaker orders (composite index), however, the level is still high
  - » Orders in oil related sectors have held up at a solid level since late 2017, non-oil sectors are somewhat softer

SpareBank 1 MARKETS

Still: Lack of demand less of a problem, more (but not yet serious) lack of labour

The share of businesses reporting labour shortages sharply up, now above the 2011-12 peak





- Fewer companies than normal are reporting lack of demand/too much competition as a constraint; the share has fallen sharply the tow last quarters – and is well above he level in 2011 - 12
- Raw materials are not short in supply (marginally up, and above an average level). Plant capacity constraints are reported at an average level

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 probably remained stable in July too but is signalling less than GDP 3% growth
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. No signs of any breakdown in the economy
USA	Growth has slowed, from well above trend. Employment growth has come down too but is still not too low, and unemployment is trending down while inflation is just marg. below target. No serious overinvestments but most sectors at/above trend. Business investments has slowed amid trade war uncertainty. Recent consumption data are OK, housing mixed. Another substantial upward revision of household savings, limited consumption risk. Fiscal stimulus continues 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**	GDP slightly better than expected in Q2, but the history revised down; growth peaked one year ago – but has remained above trend. PCE inflation up to 1.8%, not far below target (core CPI at 2.1% in June). July manuf. surveys mixed, services up. No signs of weakness in the labour market even if employment growth is slowing
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	Manufacturing PMI further down in July, while services are still reporting growth above trend
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.**	AKU unemployment up in May but is still trending down, now mostly due to a decline in the participation rate. SSB manuf. survey signal somewhat slower growth but not like 'abroad'

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

The Calendar: Global manuf PMI, FOMC -25 bps, US non-farm. NAV, retail here

Time	Country	Indicator	Period	Forecast	Prior
Monday July 29					
Tuesday July 30					
01:30	JN	Jobless Rate	Jun	2.4%	2.4%
01:50	JN	Industrial Production MoM	Jun P	-1.7%	2.0%
08:00	NO	Retail Sales MoM	Jun	0.6%(0.5)	-1.3%
09:30	SW	GDP QoQ	2Q P	0.3%	0.6%
11:00	EC	Economic Confidence	Jul	102.7	103.3
14:30	US	Personal Income	Jun	0.4%	0.5%
14:30	US	Personal Spending	Jun	0.3%	0.4%
14:30	US	PCE Core Deflator YoY	Jun	1.7%	1.6%
15:00	US	CS 20-City House Prices MoM	May	0.2%	0.0%
16:00	US	Pending Home Sales MoM	Jun	0.4%	1.1%
16:00	US	Conf. Board Consumer Confidence	Jul	125	121.5
	JN	BOJ Policy Balance Rate	Jul-30	-0.1%	-0.1%
Wednesday July 31					
03:00	CH	Composite PMI NBS	Jul	--	53
11:00	EC	Unemployment Rate	Jun	7.5%	7.5%
11:00	EC	GDP QoQ	2Q A	0.2%	0.4%
11:00	EC	CPI Core YoY	Jul A	1.0%	1.10%
14:15	US	ADP Employment Change	Jul	150k	102k
14:30	US	Employment Cost Index	2Q	0.7%	0.7%
15:45	US	Chicago PMI	Jul	51.5	49.7
20:00	US	FOMC Rate Decision	Jul-31	2-2.25%	2.25-2.5%
Thursday Aug 1					
03:45	CH	Caixin/Markit Manufacturing PMI	Jul	49.5	49.4
08:30	SW	PMI Manufacturing	Jul	50.3	52
09:00	NO	PMI Manufacturing	Jul	--	51.9
10:00	NO	Oslo OBOS Apartment Prices	Jul		1.4%
10:00	EC	Manufacturing PMI	Jul F	46.4	46.4
10:30	UK	PMI Manufacturing	Jul	47.7	48
13:00	UK	Bank of England + Inflation report	Aug-01	0.75%	0.75%
13:30	US	Challenger Job Cuts YoY	Jul	--	12.8%
14:30	US	Initial Jobless Claims	Jul-27	212k	206
15:45	US	Markit Manufacturing PMI	Jul F	--	50.0
16:00	US	ISM Manufacturing	Jul	52	51.7
17:00	WO	Global Manufacturing PMI	Jul	(49.1)	49.4
	US	Total Vehicle Sales	Jul	16.90m	17.30m
Friday Aug 2					
08:00	NO	Credit Growth	Jul	5.7%	5.6%
10:00	NO	Unemployment Rate, Registered	Jul	2.3%(2.3)	2.1%
11:00	EC	Retail Sales MoM	Jun	0.2%	-0.3%
14:30	US	Change in Nonfarm Payrolls	Jul	169k	224
14:30	US	Unemployment Rate	Jul	3.7%	3.7%
14:30	US	Average Hourly Earnings YoY	Jul	3.1%	3.1%
14:30	US	Trade Balance	Jun	-$54.6b	-$55.5b
Monday Aug 5					
02:30	JN	PMI Composite	Jul	--	50.8
03:45	CH	Caixin/Markit PMI Composite	Jul	--	50.6

- **The global manufacturing PMI** probably fell further in July, by 0.3 p. Both US and EMU reported lower prelim. manuf. PMIs and the level in EMU is just at 46. Other US July surveys are mixed, signals a close to unch manuf. ISM
- **The FOMC** has no choice but cutting the signal rate by 25 bps to 2 – 2.25% at Wednesday? Probably not, since central FOMC members have 'promised' a cut - even if the US economy is still pretty strong, and inflation close to target. A 50 bps cut is quite unlikely. Will the Fed signal further cuts? At least not as many as the market now envisages, the Fed cannot make up a disastrous scenario, now. This is a 'mid meeting', without new economic projections or a new dot plot. **Employment growth** has slowed but unemployment remains record low, and wage inflation is not low – at least until June. July data this week
- **EMU GDP** probably grew in Q2 but probably not at an impressive pace
- **Bank of England** will most likely not signal willingness to cut but rather openness/flexibility in face of an uncertain Brexit process. The bank's chief economist (Haldane) last week argued to be very cautious cutting rates in the current environment
- Back home, we expect a continued decline in **NAV unemployment**, even if the LFS surprised on the upside. **Retail sales** was weaker than expected in May, and even if the trend is up, it is not that impressive. We expect a small uptick in June. **Credit growth** probably accelerated, due to higher growth in corporate borrowing. Data during the summer should not have made Norges Bank to change its mind vs. another hike in Q3 or Q4.

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

In this report

Global + PMIs

- Surprise indices down but just due to EMU, and weak PMIs there
- May/June better for global retail sales, manf. Production, perhaps also foreign trade
- The global composite PMI probably stabilised in July; services and the US up, manufacturing and EMU down

USA

- Q2 growth down but less than expected. Households and the government saved the day.
- History revised down, GDP growth peaked last year?
- Another BIG upward revision in the savings rate!
- Durable goods orders do not signal a business investment setback
- The manufacturing PMI fell to 50 and regional Fed survey are mixed, signals close to unch ISM
- New homes sales weaker than expected, trending down?
- Jobless claims still on the way down

EMU

- The ECB is ready to act, but not now. However, in September…
- The German manufacturing PMI fell to 43.1, and the Ifo survey confirmed that goods production is struggling

UK

- Manufacturing orders straight down, domestic even faster than export orders

Sweden

- Has unemployment turned up?
- The KI surveys further down in July, signals below 1% GDP growth

Norway

- LFS unemployment up but is still trending down, due lower participation rates
- SSB manufacturing survey slightly down, not weak. Much more lack of labour
- Housing 'starts' up or down?

Highlights

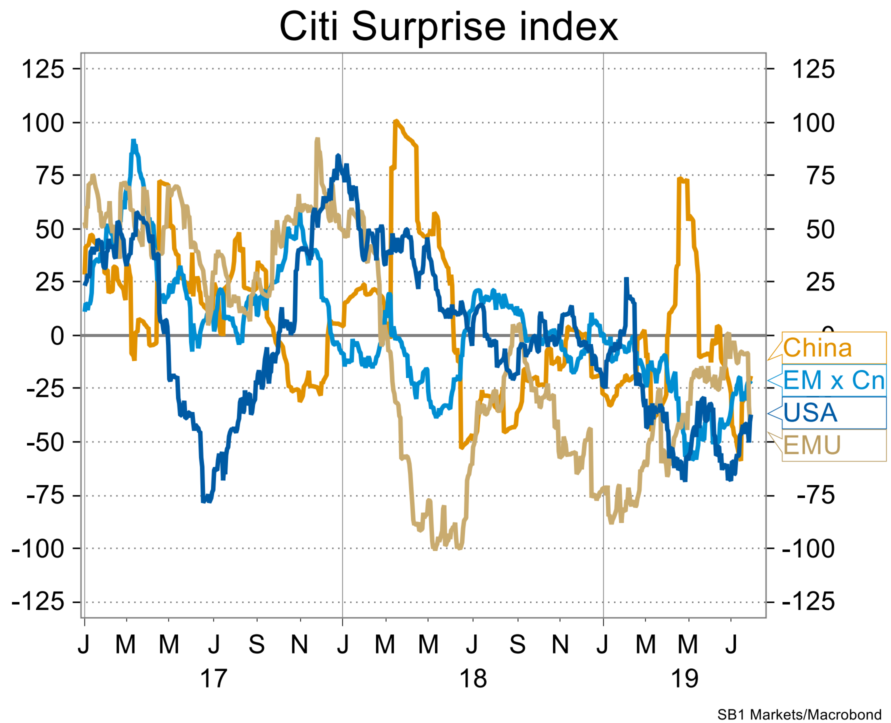
The world around us

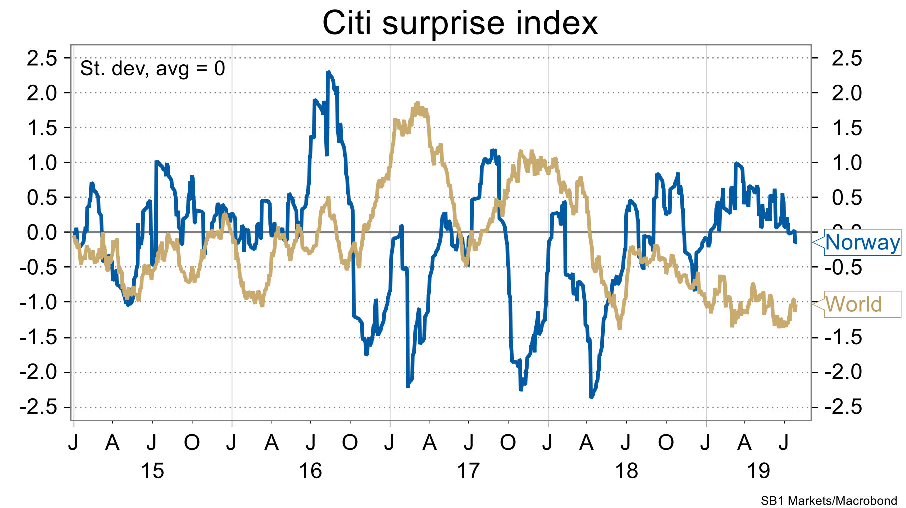
The Norwegian economy

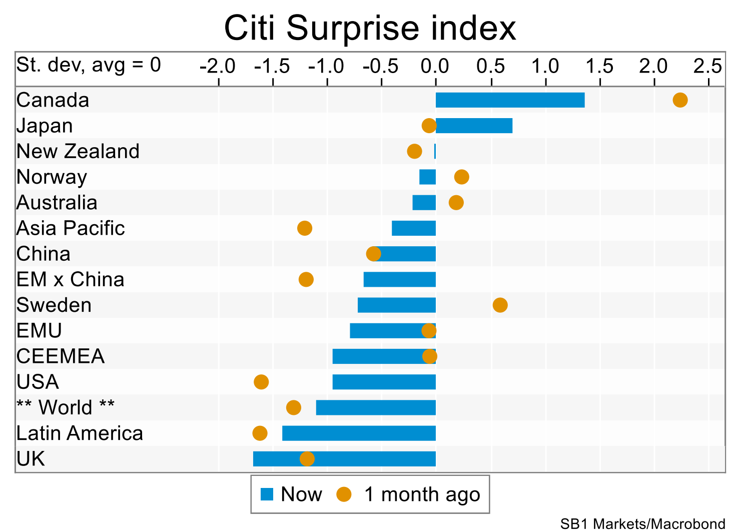
Market charts & comments

The weak EMU PMI sent its surprise index down. US a tad better

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





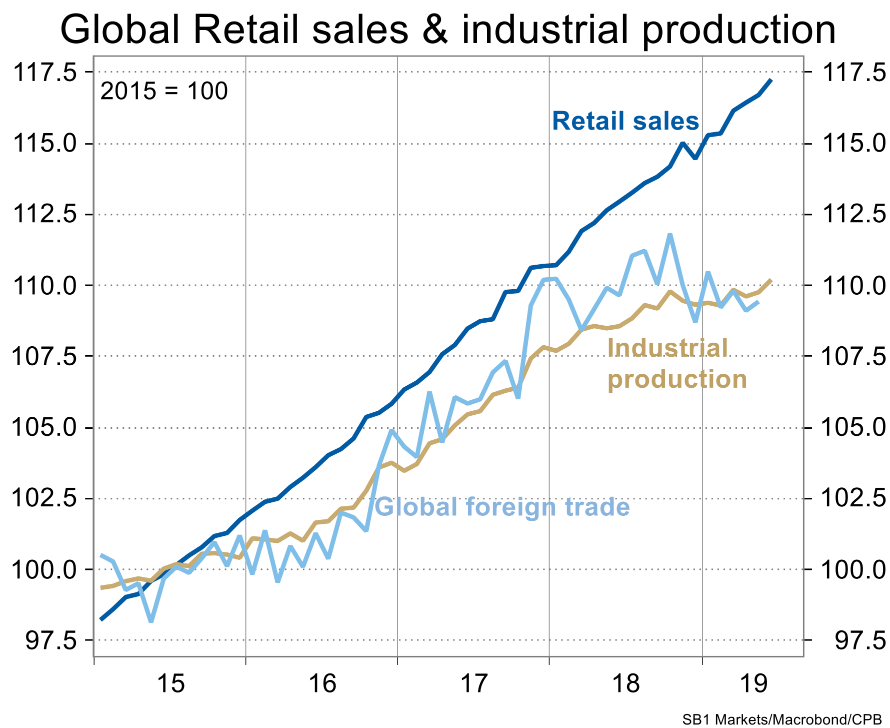


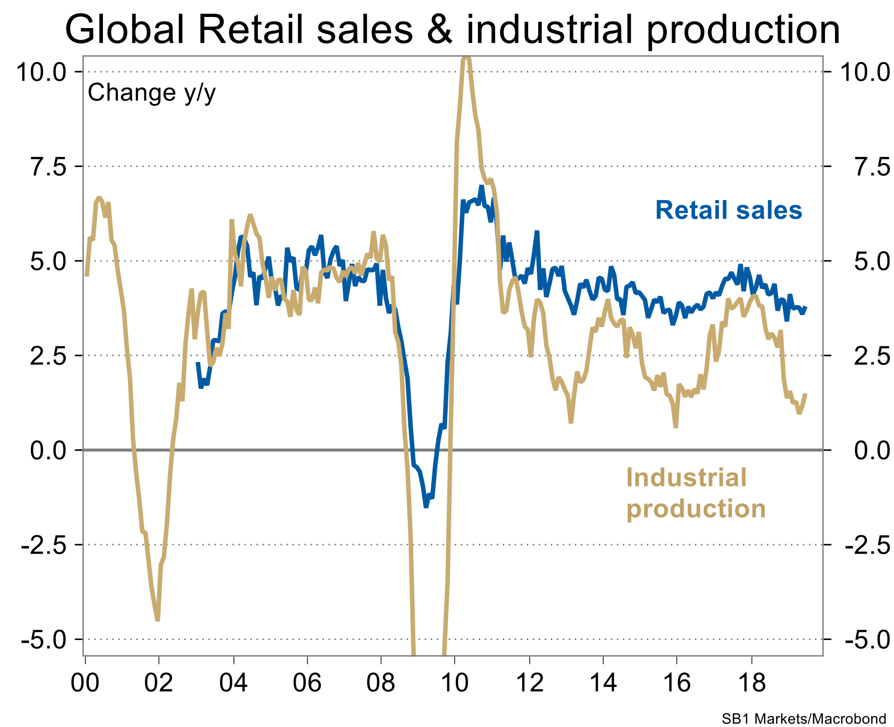
- The global surprise index has been in negative territory since last spring
- The EMU surprise index fell sharply to the decline in the PMI
- The US date still negative over the 3 last months period, but less so last week
- Chinese June/Q2 data better than expected, and surprise index turned up
- EM 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

Global foreign trade rose in May but has been trending down since Q3 last year

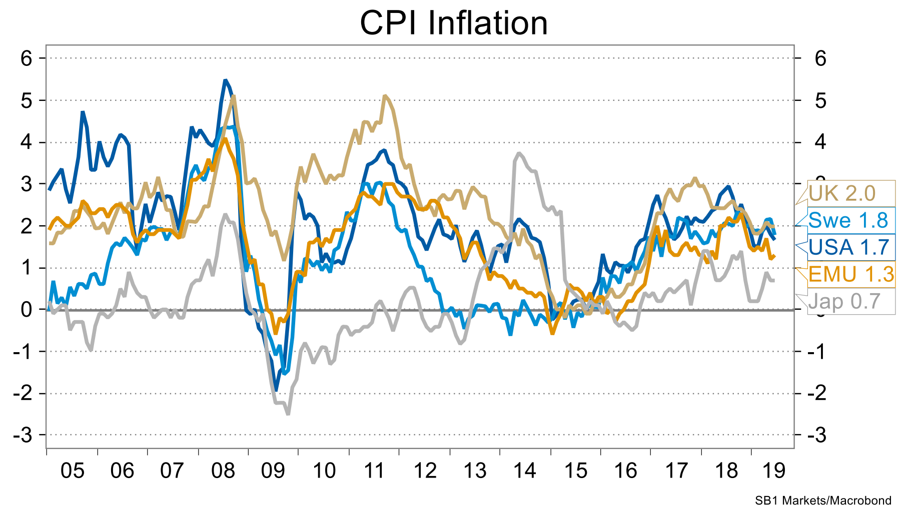


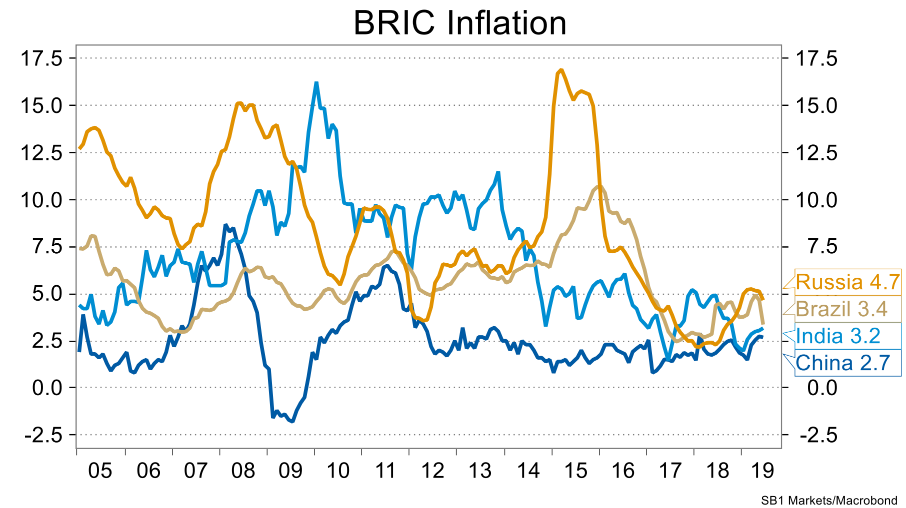


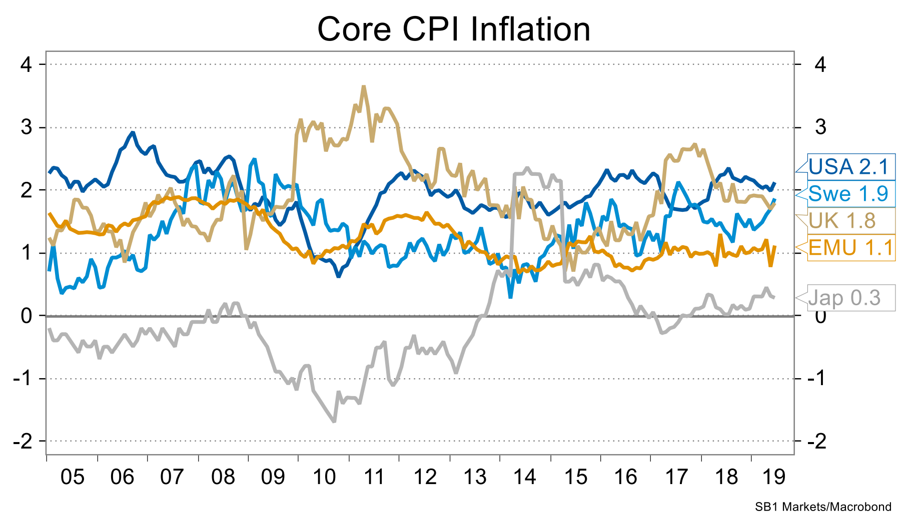
- We still have still too few data point for retail sales and manufacturing production in June but our estimate implies decent growth from May. Retail sales have slowed somewhat but signals that consumption is still supporting the global economy – and sales accelerated in June

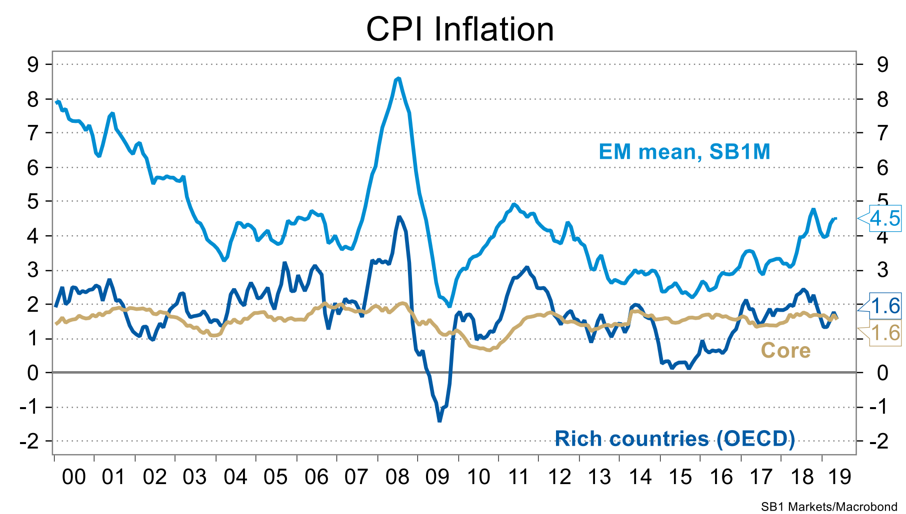
DM to turn south again, with the oil price? Core is sum flattish

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





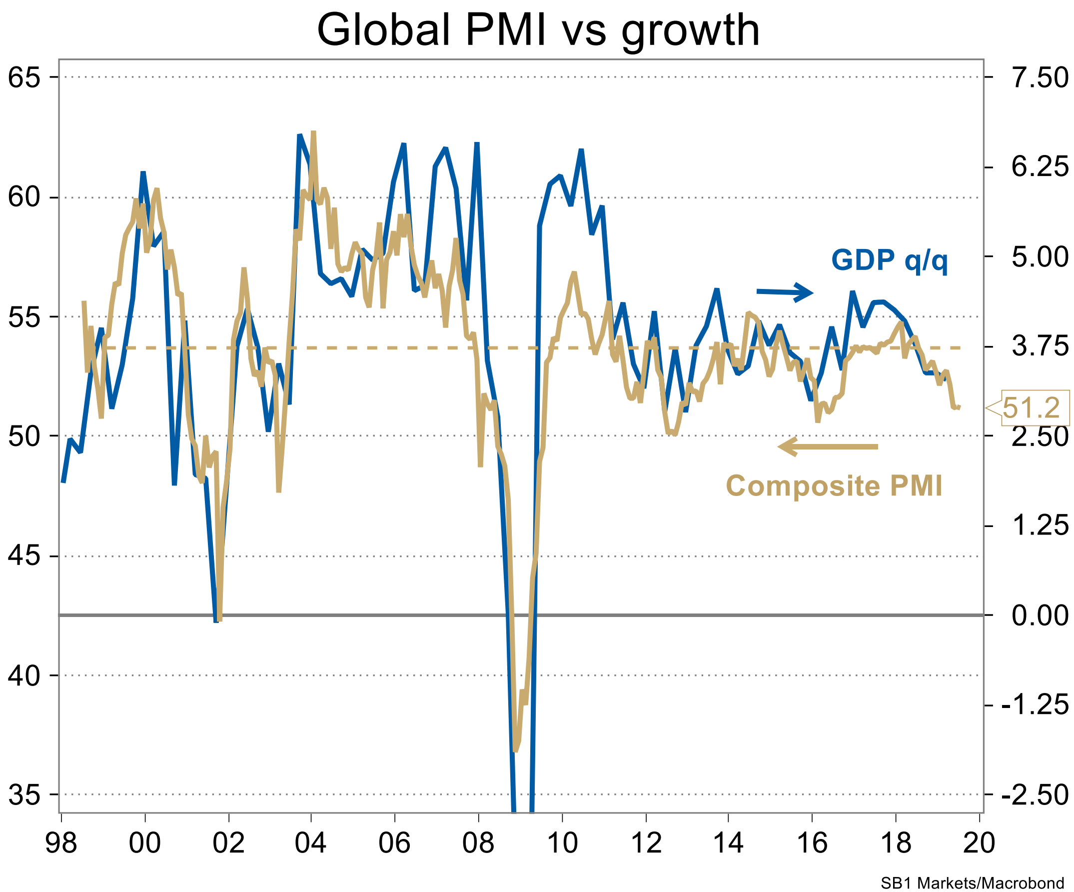


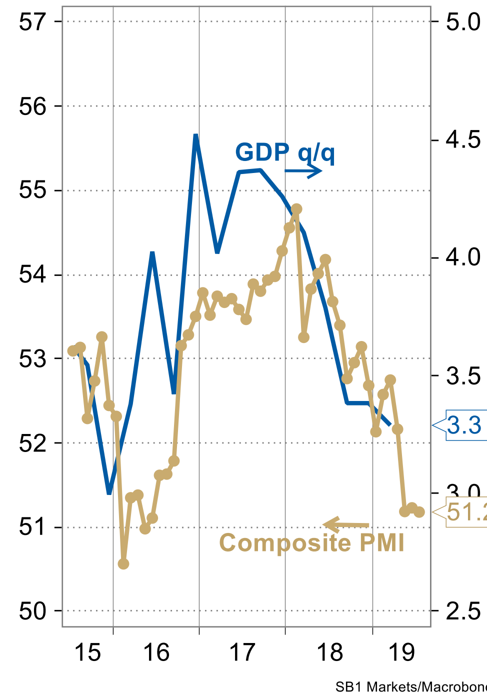


Change in % y/y in all charts. EMU core based on a seasonally adjusted price index

Global PMI (probably) probably stable in July too, signals below 3% global growth

The PMI was lower in both 2012 and 16' but the cycle is more mature now, and the PMI trends down



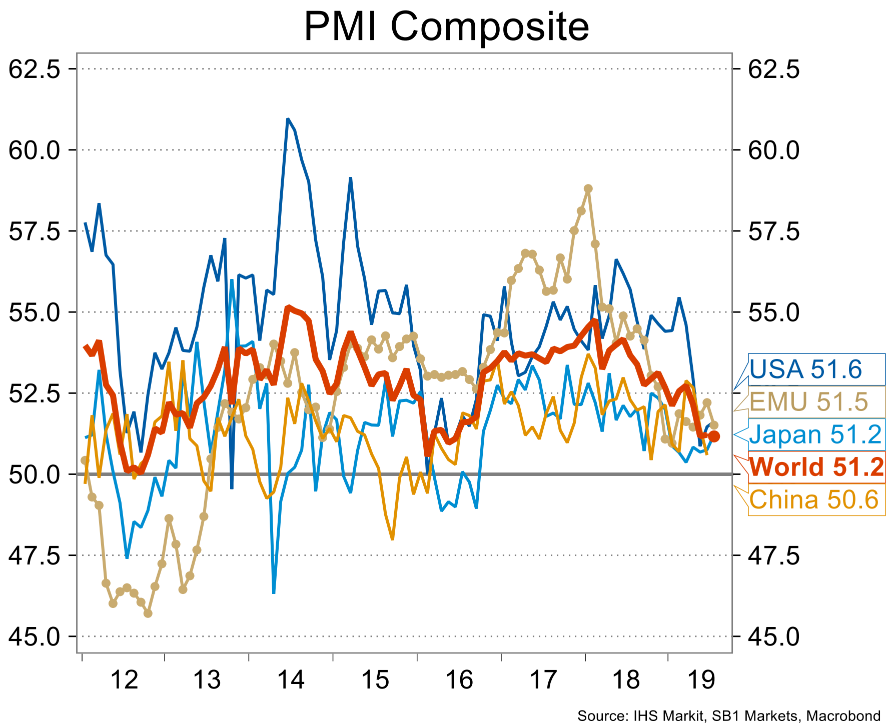


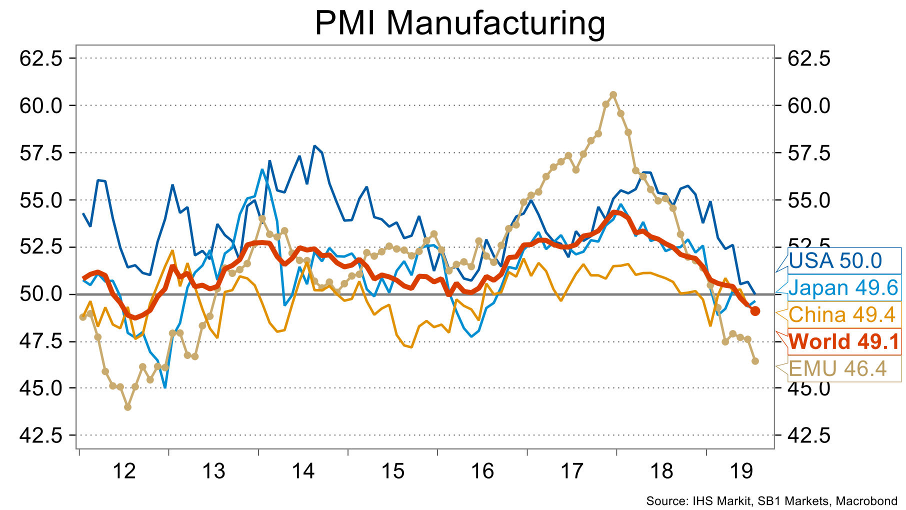
Our estimate is based on the preliminary composite PMIs from EMU, Japan and US,. The estimate is uncertain

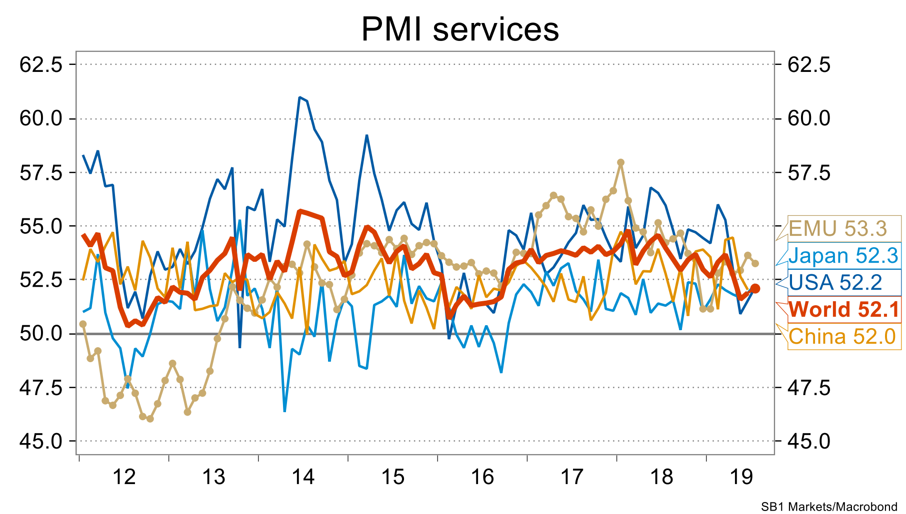
- We estimate a global composite PMI at 51.2 in July, unchanged from June (and May), at the 1st decimal (but marginally down m/m, the lowest level since June 2016
  - » The PMI has fallen by close to 4 points from the Jan 18 local peal, equalling more than a 1 pp slower global GDP growth. The manufacturing PMI signals a 20 pp slowdown in global EPS (earnings per share), down to zero

US and Japan contribute on the upside, EMU at the downside

The global manufacturing further down, weakest since 2012; services probably marginally up



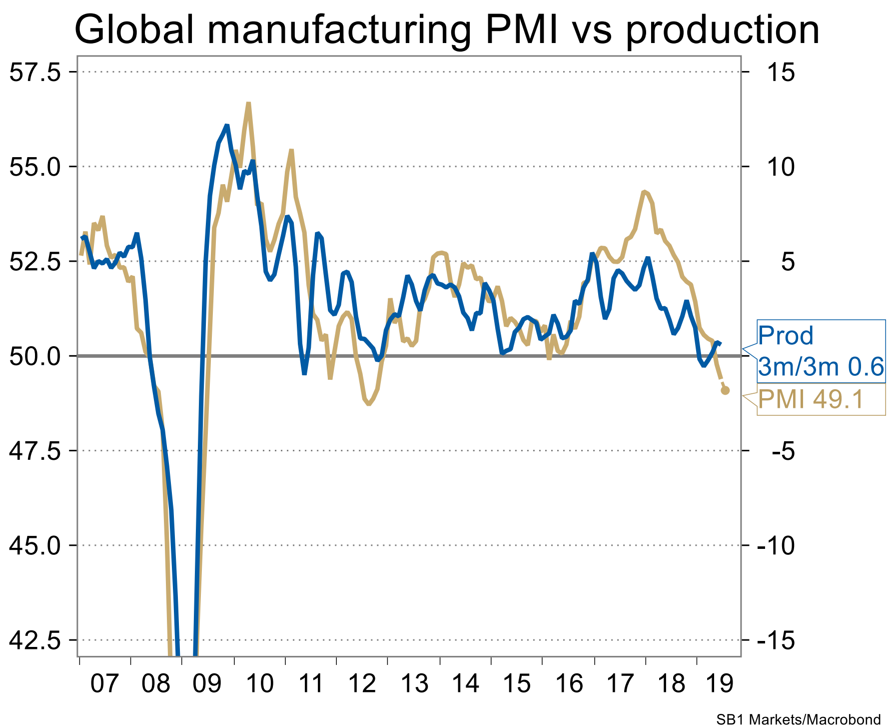




- Memo:
  - » The last obs for world indices for total, manuf. & services PMIs are based on prelim. data from the US, EMU, Japan
  - » The estimate is uncertain,
  - » China has not yet reported any June PMI data

Global manufacturing PMI indicates stagnating production

We estimate a 0.3 p decline in the manuf. PMI in June, to the weakest level since 2012

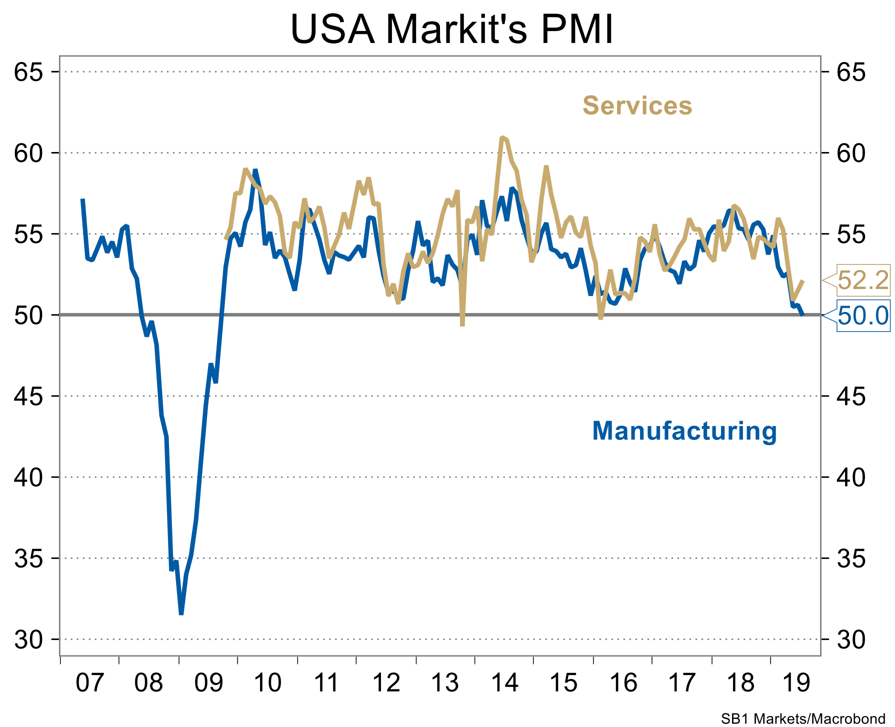


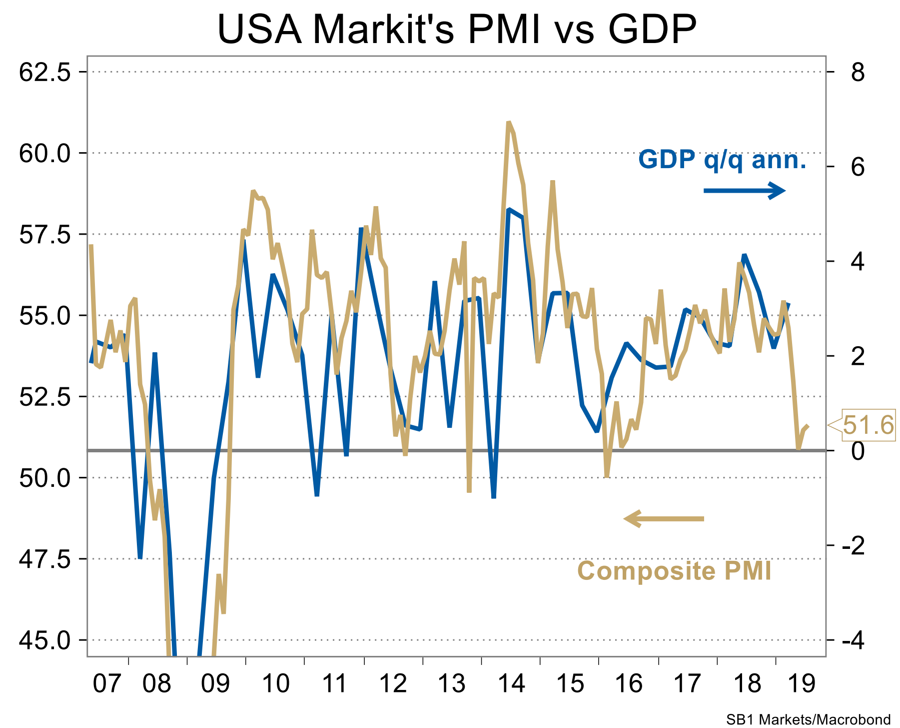
- Signals a 2% pa. decline in global manufacturing production

… And the PMI has been too upbeat the past two years…

Still a below 1% growth message, manufacturing surprisingly down

The further decline in manuf. PMI is surprising given sharp rebounds in early regional Fed surveys

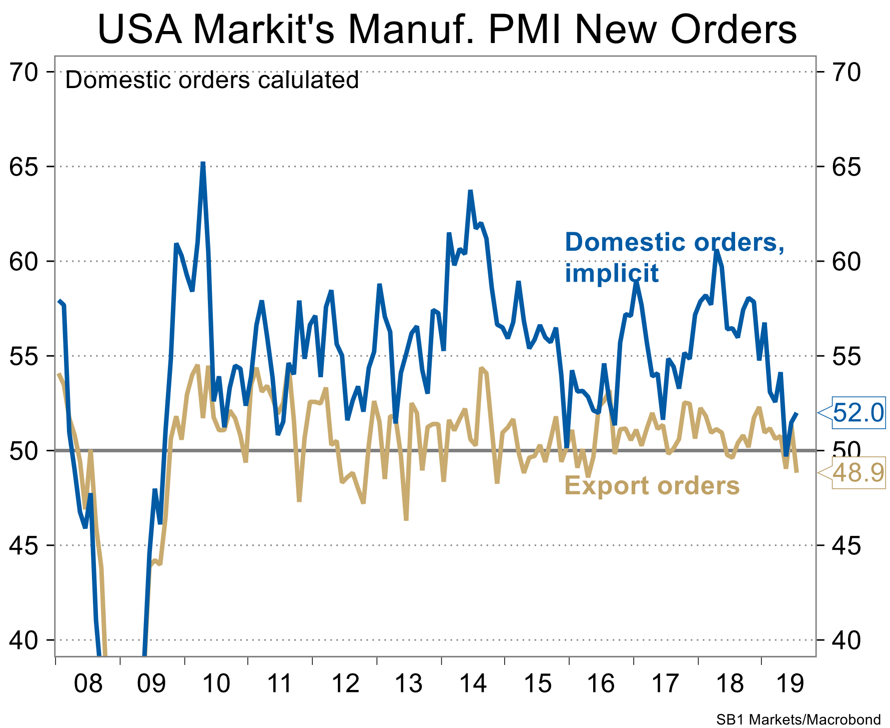


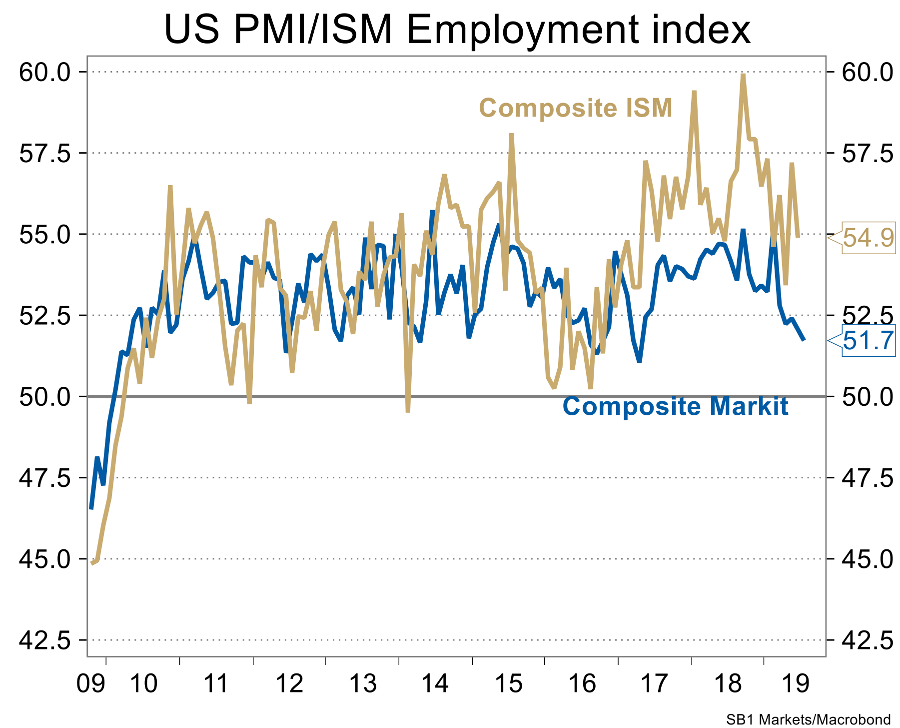


- The manufacturing PMI fell 0.6 p to 50.0 in June, expected up to 51. Given the NY & Philadelphia Fed surveys, the decline was surprising. However, other regional Fed surveys fell in July
- The service sector index rose 0.6 p in July, as in June, to 52.2. The level is the lowest since 2016, and sharply down from 55-level in Q1. The composite strengthened by 0.2 p to 51.6, also the lowest since 2016. The level signals a below 1% GDP growth pace into Q3
- Domestic manufacturing orders grew a tad faster, foreign orders slowed – in July. However, the main contrition to the slowdown recent months has been a lower growth in domestic orders, while the weakening of foreign orders has been much softer – signaling that domestic demand, not problems abroad explains most of the downshift. The GDP report confirmed that business investment was the culprit

Foreign orders down in July, but has been rather stable

Domestic demand has slowed sharply, even if household demand keeps up. Investments to blame?

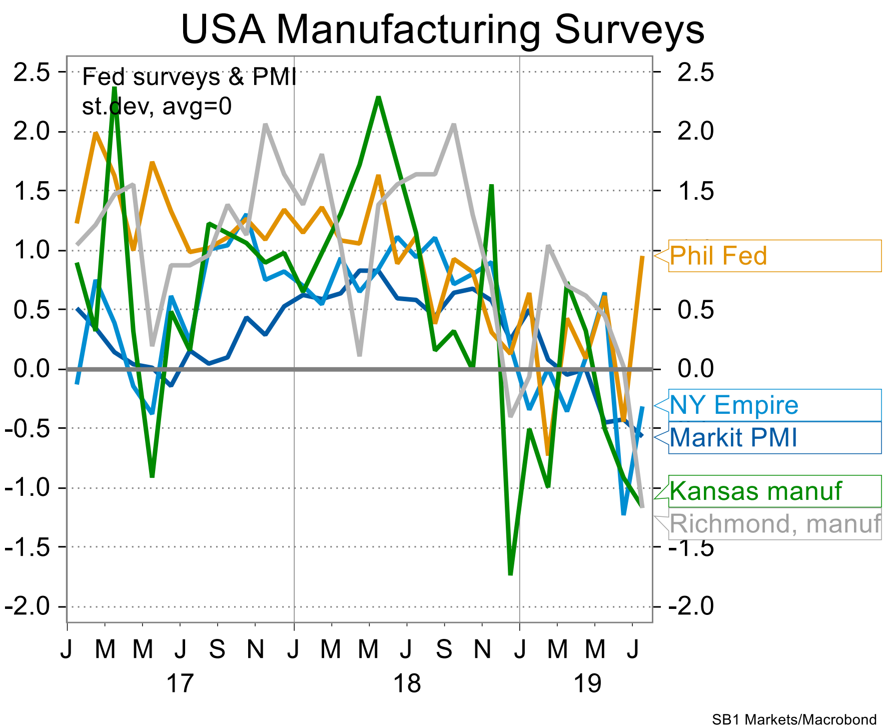


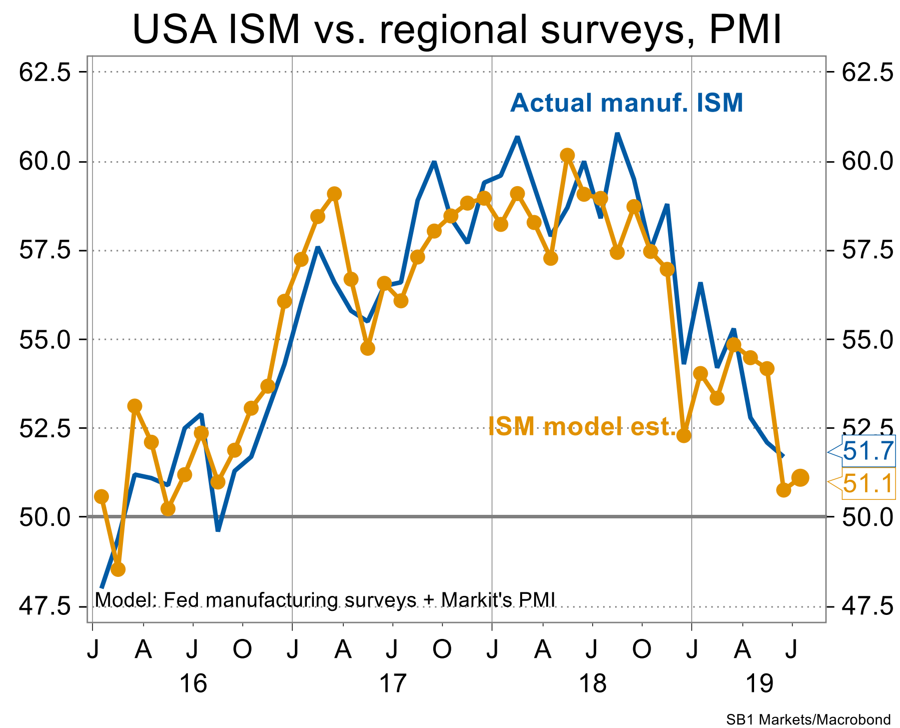


- Since late 2018, manuf. businesses have been reporting a significant downshift in growth in domestic orders. In July, the domestic component rose, while the export order index fell below the 50 line, to the lowest level since 2015. Still, the export order index has remained more or less flattish at normal level the past years and quarters
- The composite PMI employment index (chart to the right) is steady declining but companies are still reporting growth in the headcount

Two up, three down; ISM marginally up in July??

Highly diverging regional Fed surveys/PMI: In sum slightly up, due to NY & Phil Fed

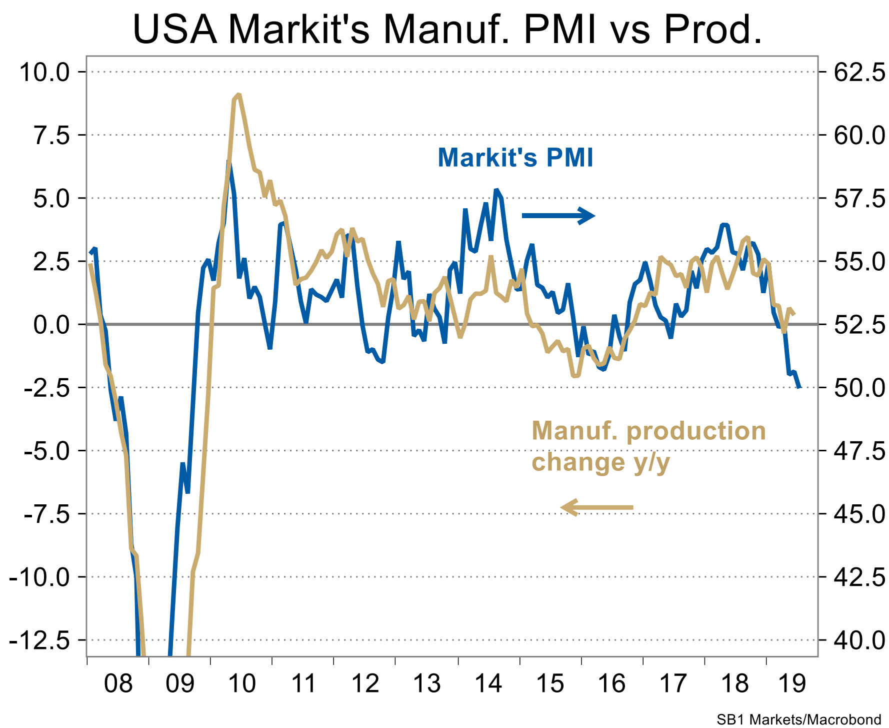


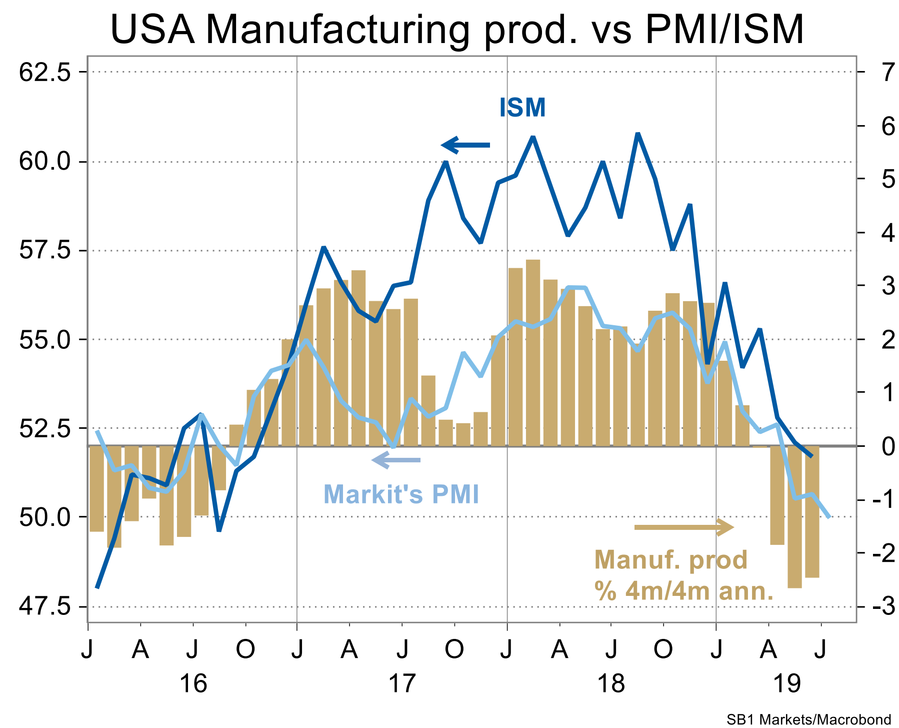


- Phil Fed's manufacturing index rose sharply in July, by almost 1.5 st.dev (a large cycle is 4 st. dev, from peak to trough). NY Fed's index also rose quite a lot but less than the almost 2 st.dev nosedive in June. However, the Kansas and Richmond Feds' surveys fell, as did Markit's PMI
- In sum, our model yields a small uptick in the July manufacturing ISM

Markit's PMI has been closer to the ball vs production than the ISM recently

Now, the PMI is signaling declining manufacturing production (which has fallen so far in '19)

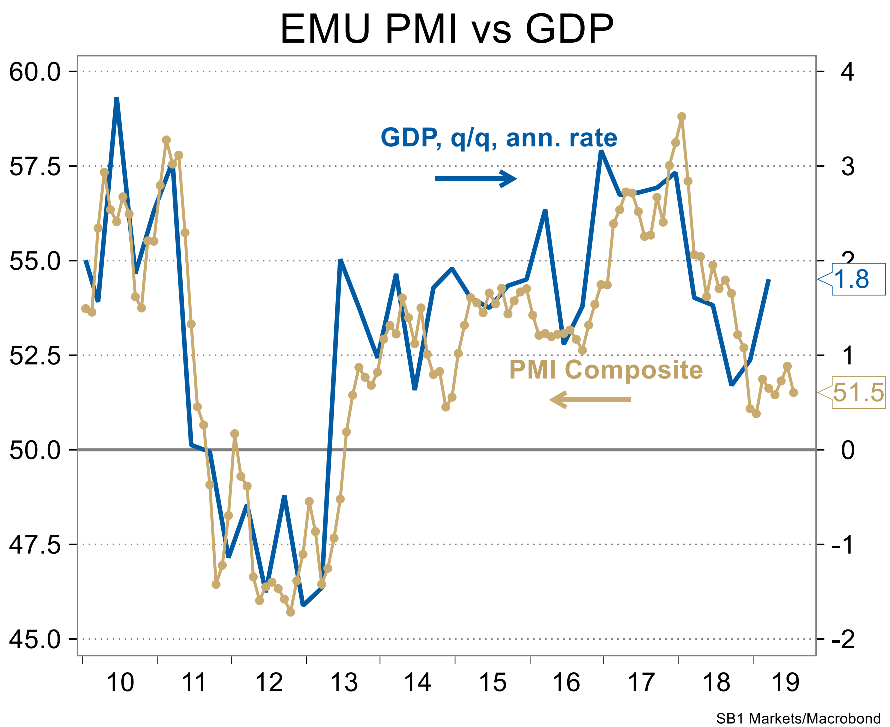


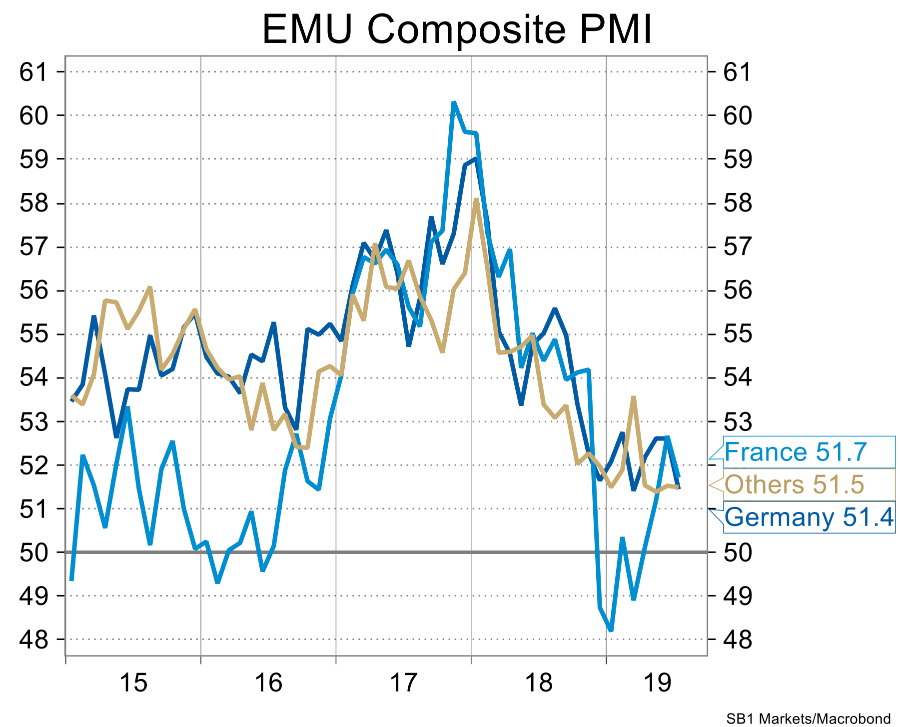


- The past years, Markit's PMI has been more closely correlated to actual manufacturing production than the ISM
  - » The PMI just reaches back to 2007, thus, the ISM a more 'reliable' recession indicator
- ISM has not reported June data yet, flip to the next slide for our f'cast

Eurozone PMI down, more than half of the (very modest) 2019 recovery lost

Services still OK, but the manufacturers are reporting deteriorating conditions

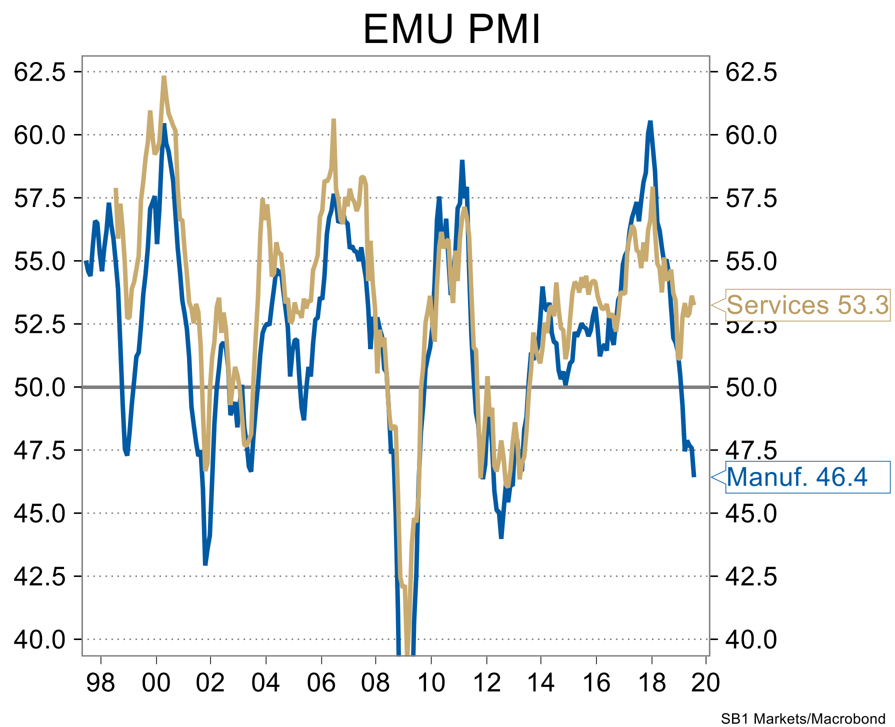


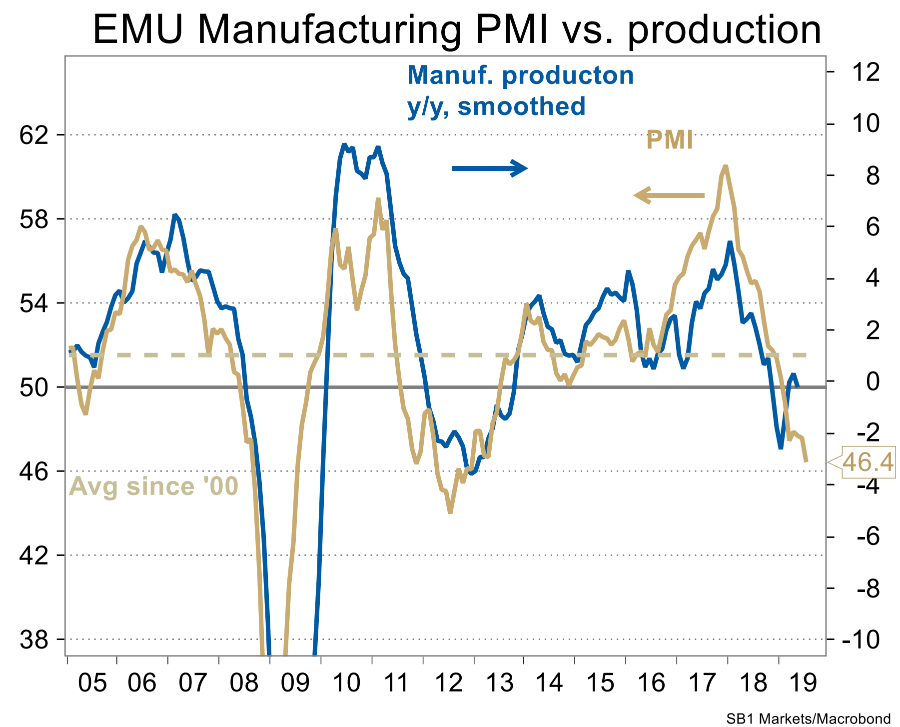


- The preliminary EMU composite declined by 0.7 p to 51.5 in July, expected unchanged. The index is up just 0.5 p from the January local trough. The index signals meagre growth, at some 0.5%
- The PMIs in both France and Germany fell in July, while the implicit estimate for the other countries was flat
- Manufacturing is the weak link in the chain – with Germany as the weakest – the manuf. PMI fell 1.2 p to 46.4, to the lowest print since Dec 2012, during the ‘ euro crisis’, indicating a continued – and faster – decline in production. EMU services are still reporting OK growth, even if the index fell in July

The manufacturing contraction deepens; services remain resilient

The manufacturing PMI almost fell sharply in July, to 46.4 – signalling declining production



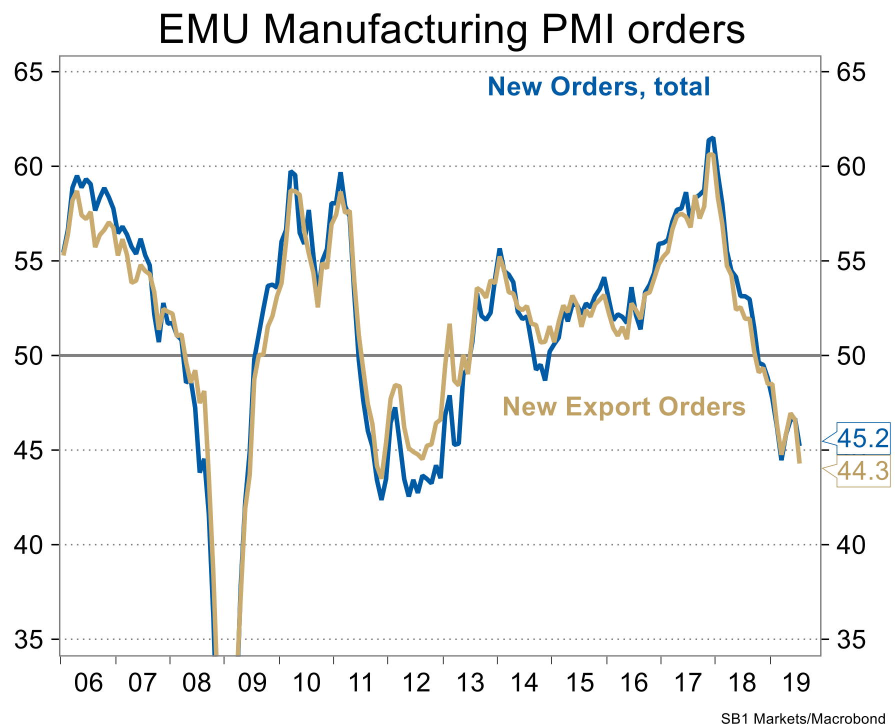


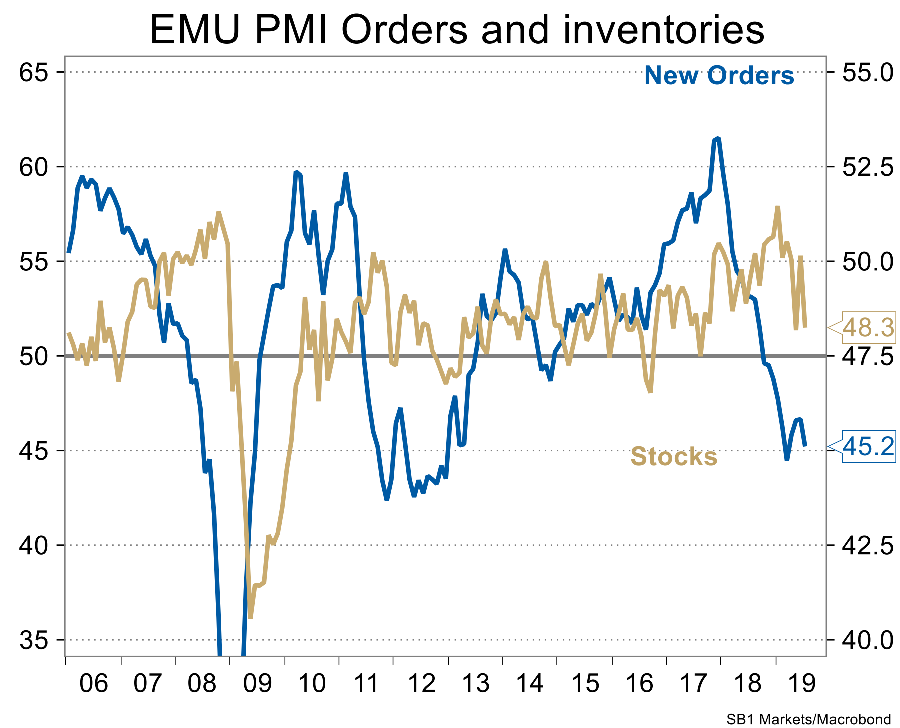
- Manufacturing production stabilised in Q1 (up 3.4% following the Q4 slump), and so far a flat Q2 print is reported (but no June date yet). The PMI indicates a contraction in Q3 (if not already in Q2, if June was weak)

SpareBank 1 MARKETS

The downturn in orders still heavy, no inventory build-down, yet

Manufacturing PMI order indices fell again in July, but has not fallen of a cliff recent months

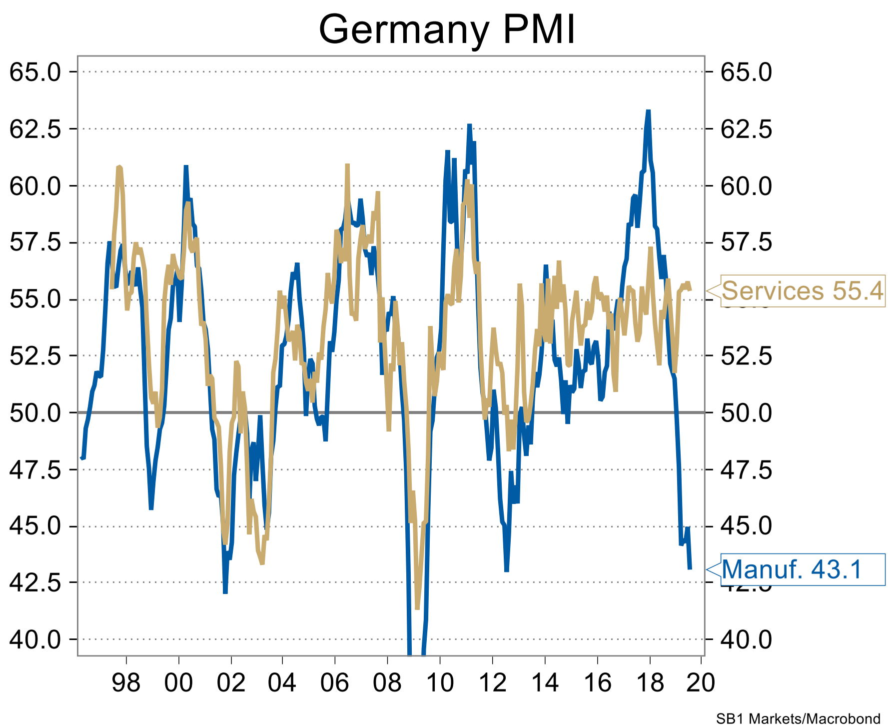


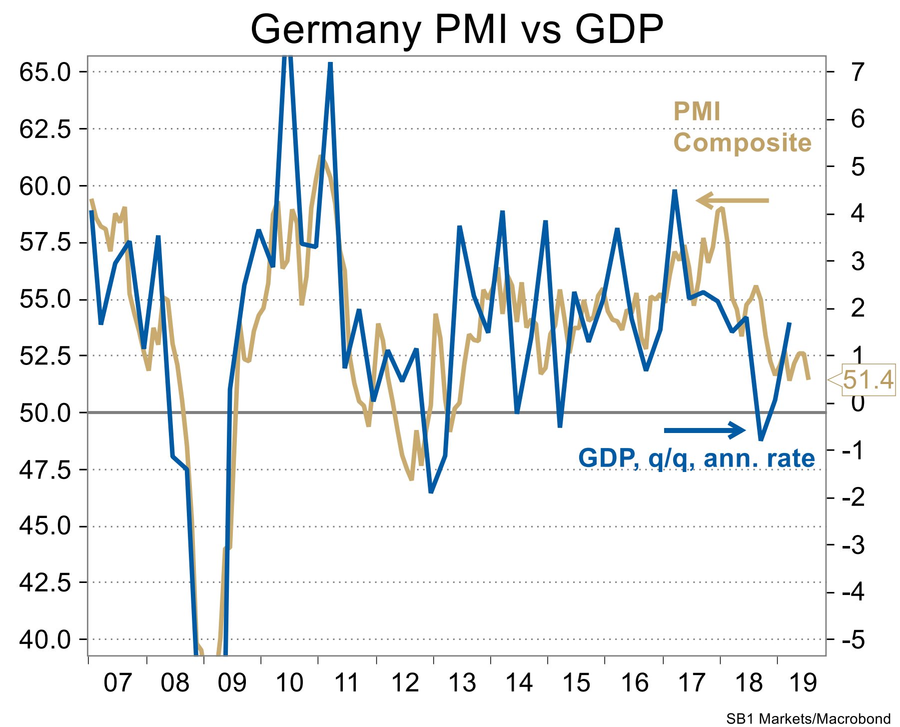


- Businesses reported a further decline, the total orders index fell to 1.4 p to 45.2, following tentative signs of stabilisation. Both domestic and export orders are still contracting (the export index includes intra-area exports and not just out of EMU exports, and is thus pretty useless). Orders are still falling at the fastest pace since the 2012 euro crisis
- The inventories of finished goods index fell in July, back to the level in May. The level is still too high to signal a drawdown of inventories, but they are at least not exploding (anymore)

Services still STRONG, the manufacturing PMI even WEAKER in July

The composite surprisingly down 1.2 p to 51.4, indicating 0.5% growth

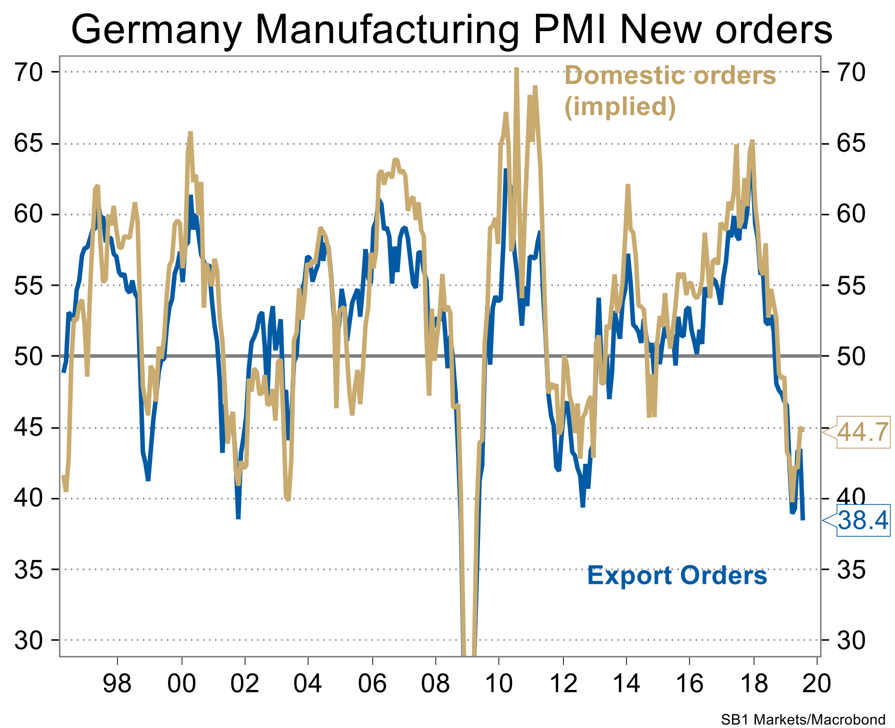


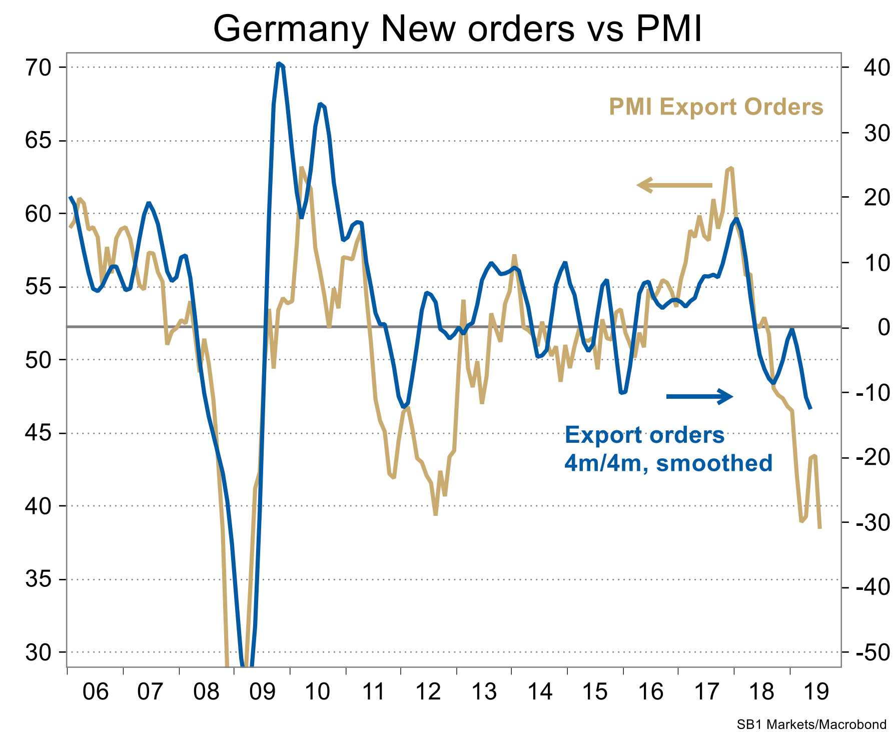


- The manufacturing PMI fell 1.9 p, to 43.1, the lowest level since one month in 2012, during the euro crisis. A smoothed index is at the 3rd lowest level in 20 years (since the German PMI was established)
- The service fell just marginally and continues to note solid growth in services. The discrepancy between services and manufacturing has been larger just during two months in the midst of the Great Financial Crisis. So this is really special!

Export orders are falling even faster – and domestic orders still fast

Actual orders have fallen, but not really bad, and actual exports kept up until April/May

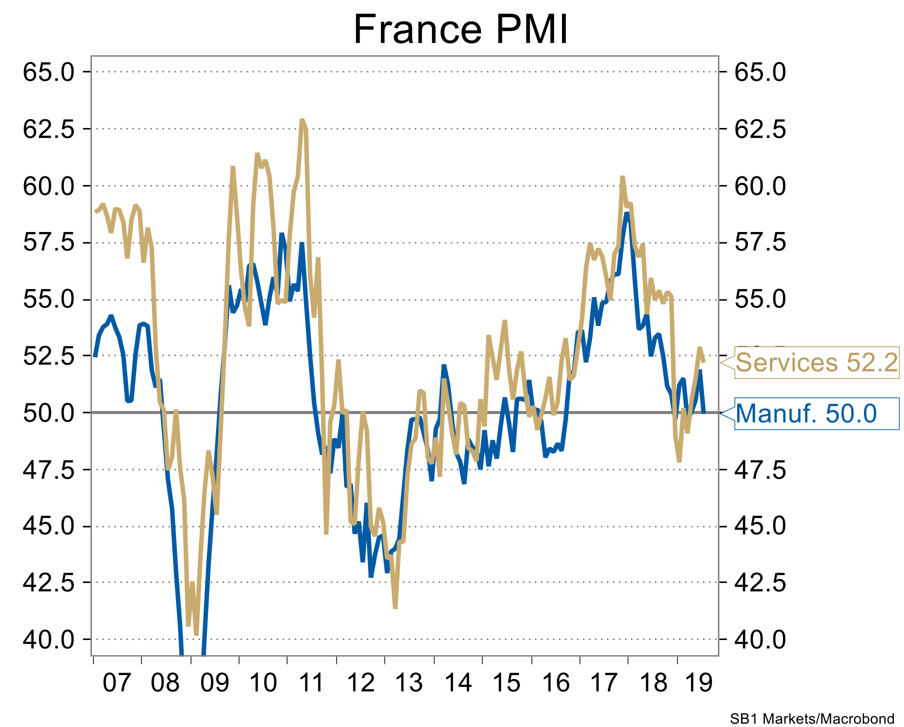


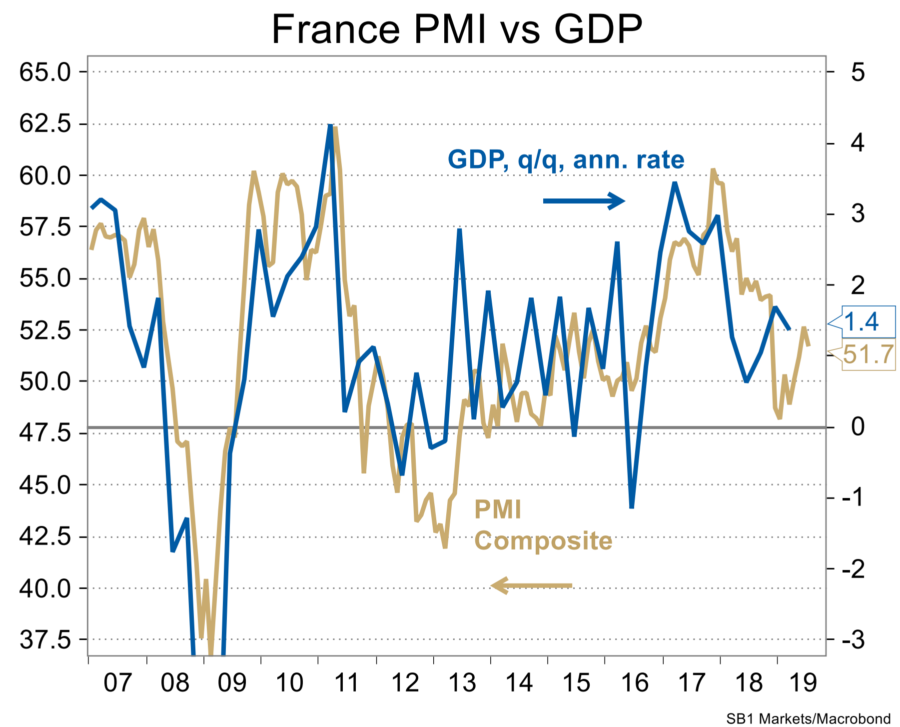


- More on Germany surveys here

PMI down 1 p, signals 1%+ growth, trend still up

The composite rose 1.7 p last month, and the trend is up from the 'yellow vest' through last autumn

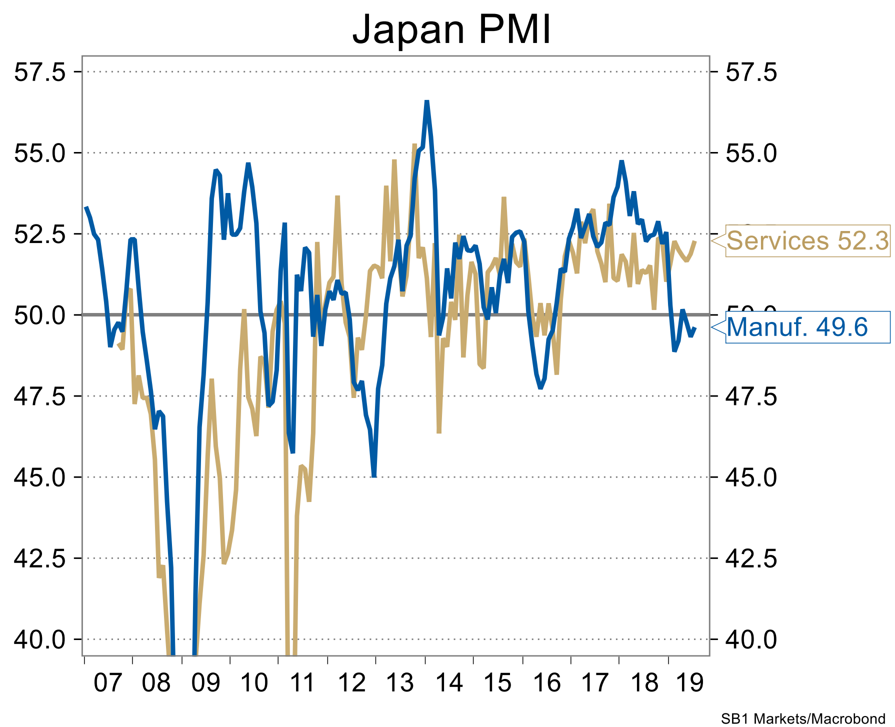


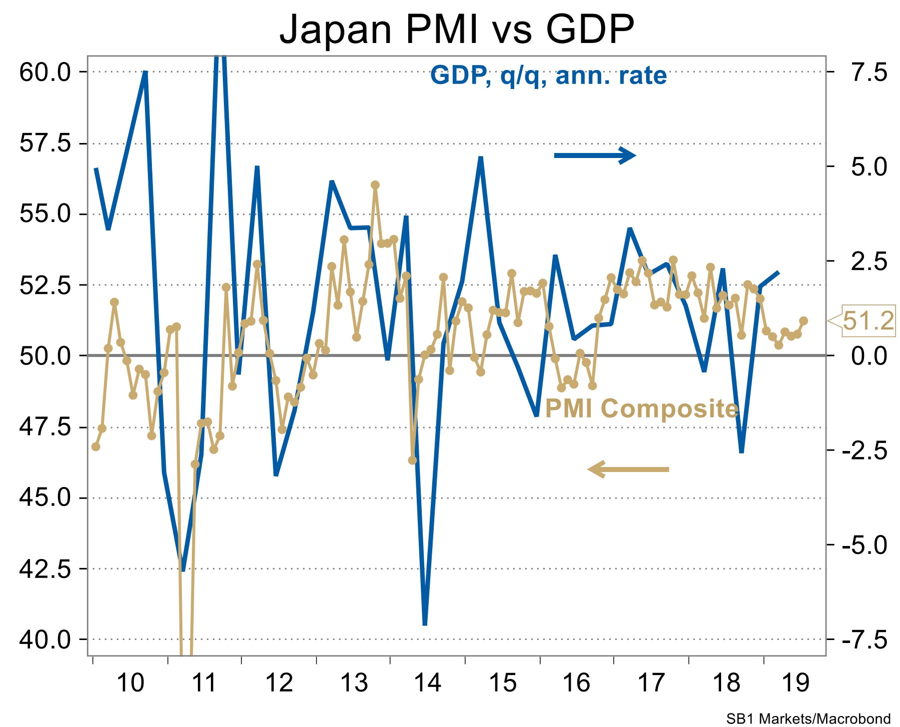


- The manufacturing PMI fell more than the service sector PMI

PMIs up in July, but export order are still weak – and manuf. remains below 50

The service sector index well above an average level (which is not the case for the manuf. Index)

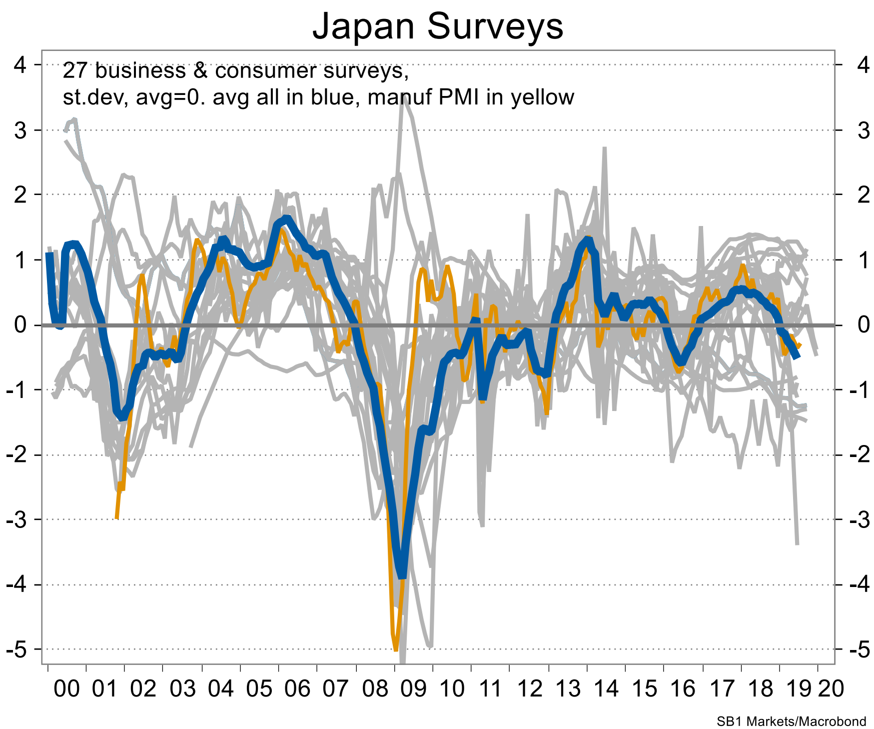




- The composite PMI rose 0.4 p 51,2, trending marginally up since early 2019. However, the level does (if the PMI can be used at all) signal a GDP growth well below 1%
- Other Japanese surveys have softened but are in average not signalling any abrupt slowdown

Other surveys have not collapsed

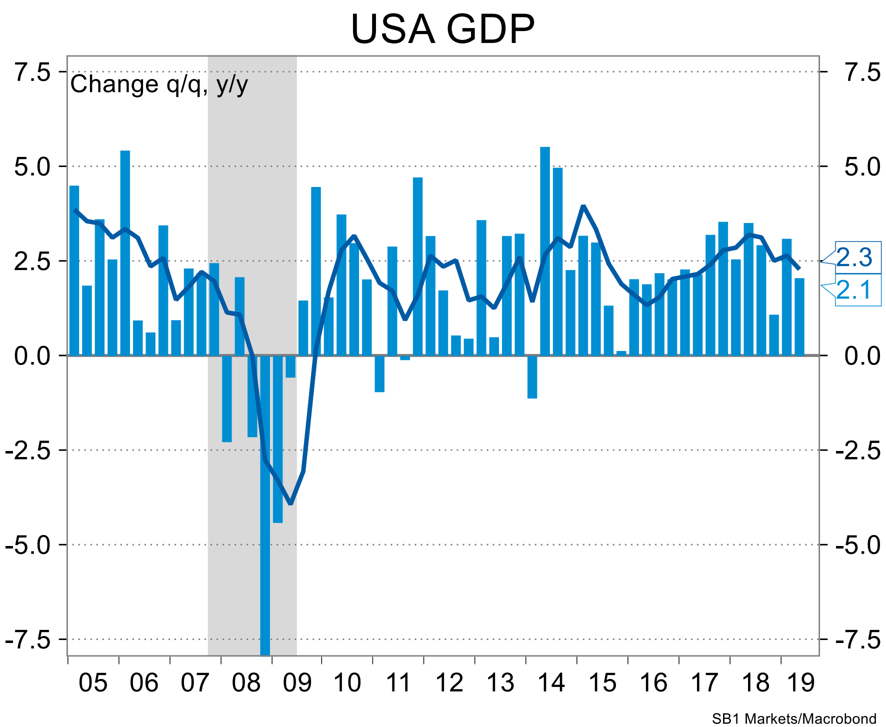
But the direction is down

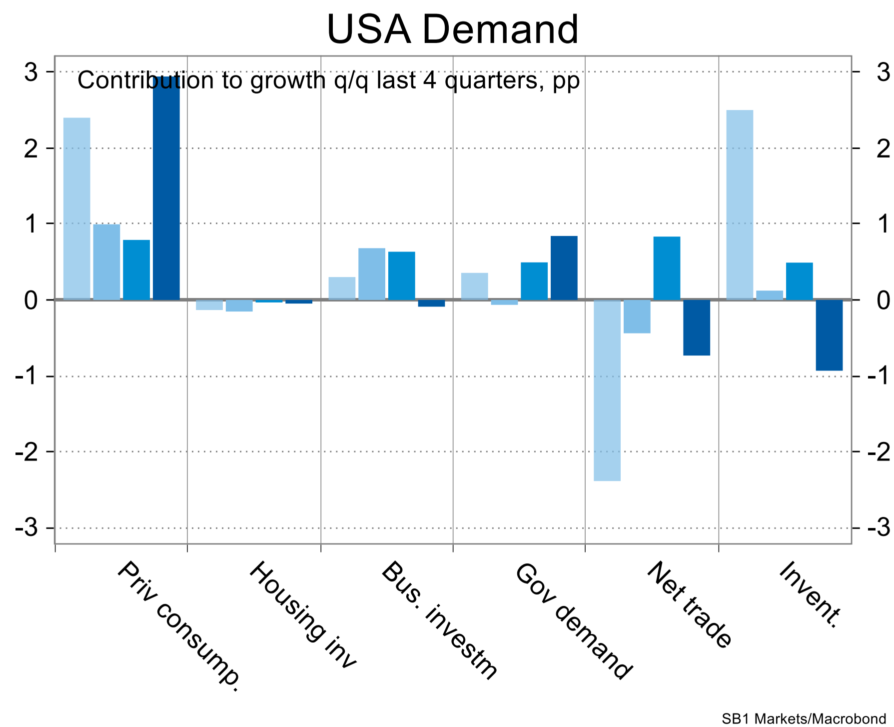


- The outlier on the downside is the Duke index

Q2 growth down but less than exp. – households (and the gov) saved the day

Business (and housing) investments down, a negative drag to GDP from net trade and inventories

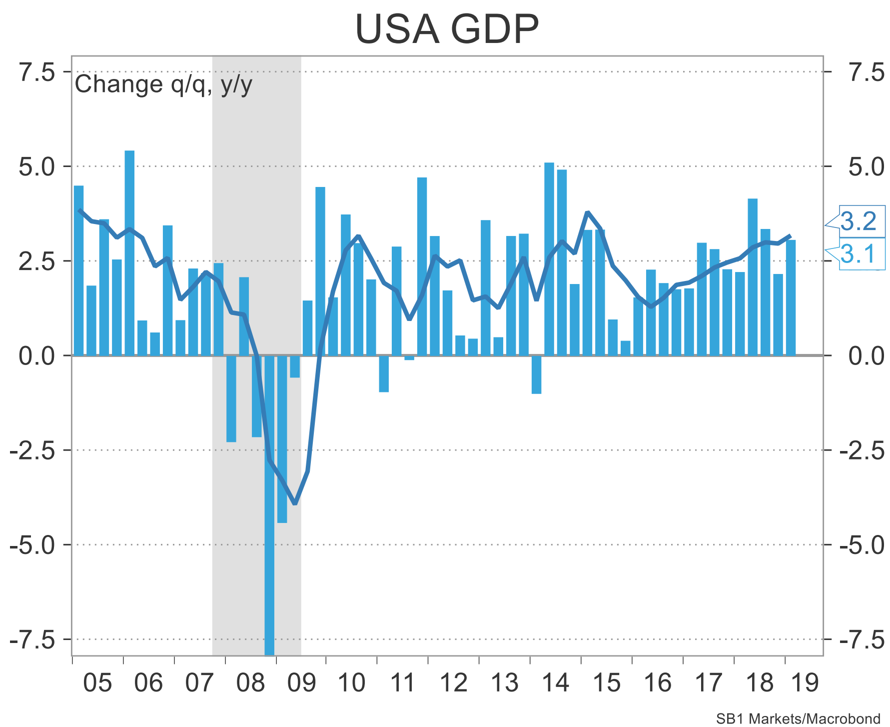




- GDP grew by 2.1% in Q2, better than expected (1.8%), and above NY, Atlanta Fed nowcasters (1.5%-ish). Still, the annual growth rate fell to 2.3%, down from 2.7% in Q1 – which was revised down from 3.2%. The annual revision revealed that growth peaked in Q2 '18, while previously released data showed acceleration through Q1 '19! (check next page)
- Private consumption rose by 4.3%, contributing to 2.9 pp to Q2 growth, a tad better than expected. Government demand grew 5%, lifting GDP by 0.8 pp, highly unusual. Business investments fell marginally, even though immaterial investments continued upwards as construction investments fell sharply (also ex oil investments)
- Total labour costs grew marginally faster than nominal GDP – and core PCE inflation (Fed's price measure) accelerated to 1.8% from 1.2%. Even if growth has slowed, an interest rate cut should normally been far from a done deal given these growth/inflation numbers

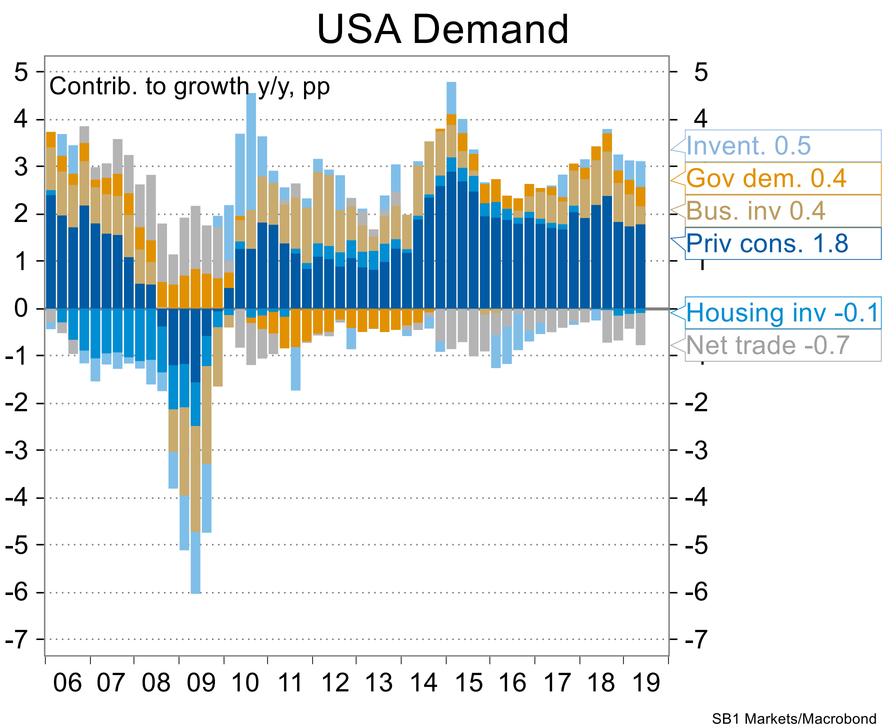
Oops: Wasn't growth at 3%, and accelerating?? Flip back, and check

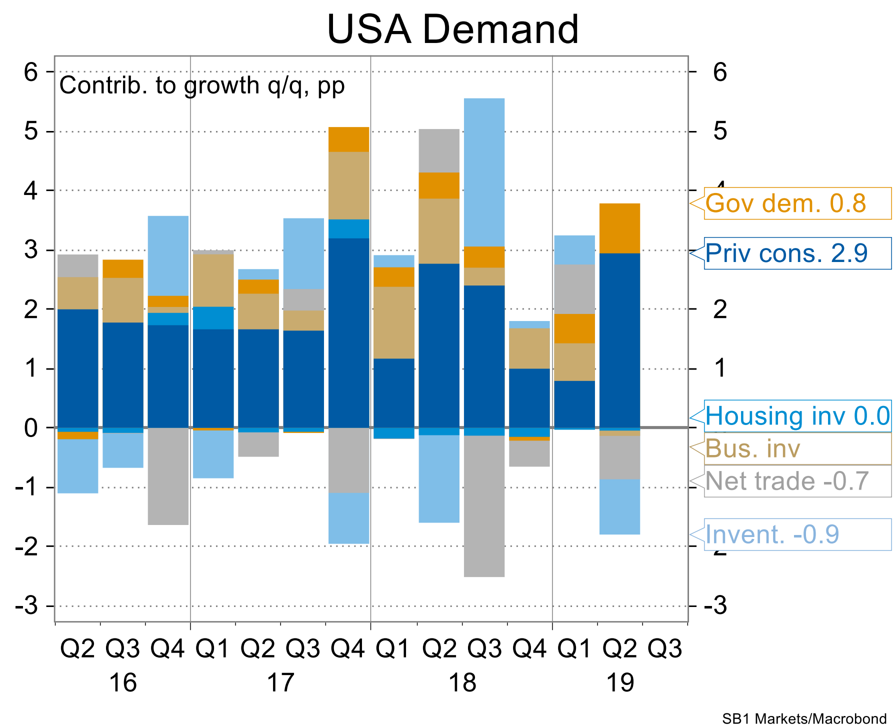
Here is how data looked like before the annual revision, growth had not peaked yet



Private consumption & government spending in the front seat in Q2

Housing, business investments marginally down, while net trade, inventories contributed negatively

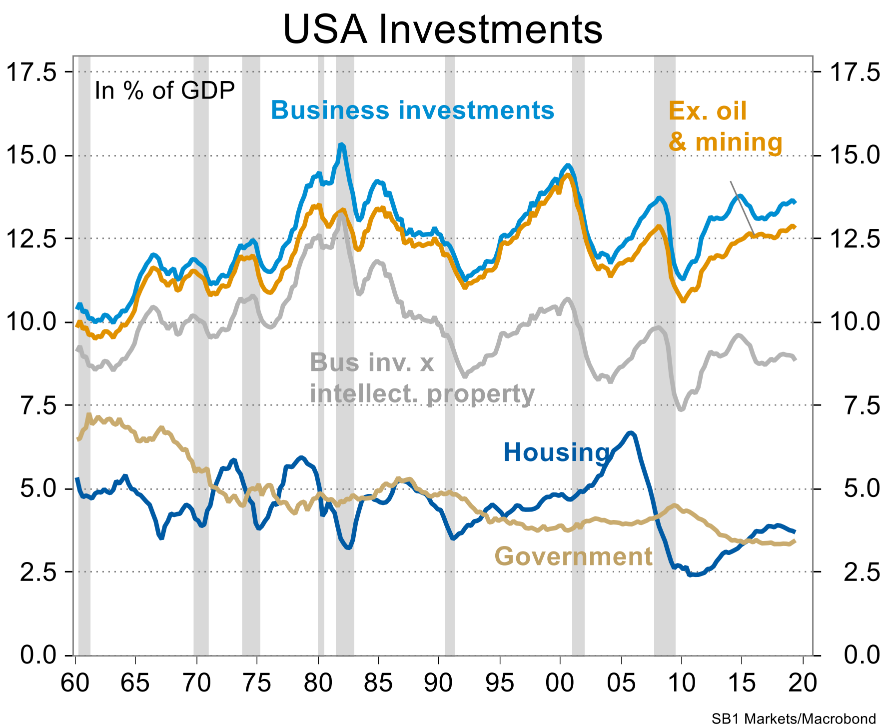


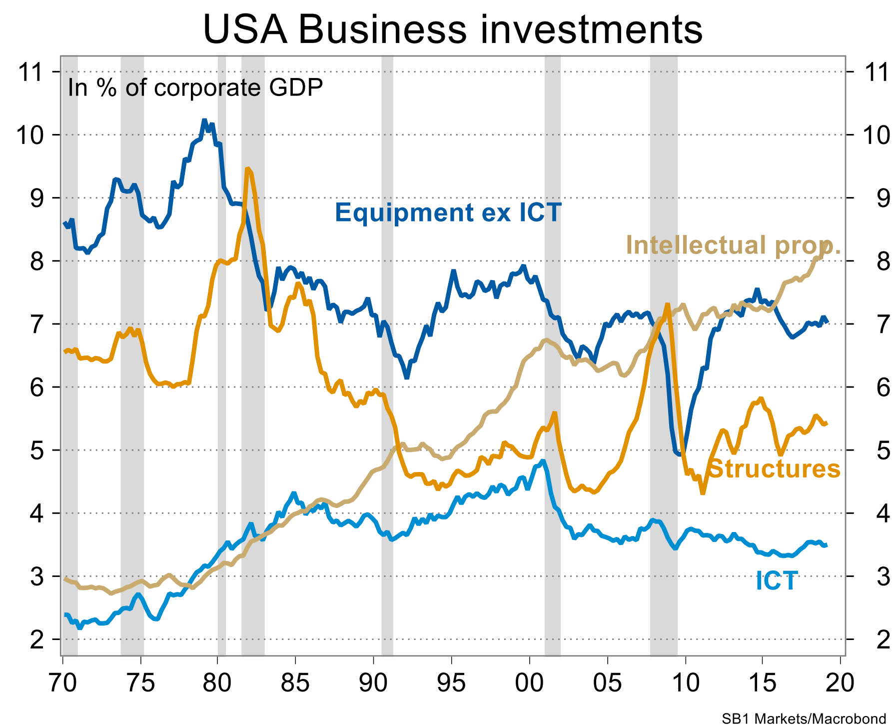


- Private consumption rose more than 4%, yielding a 2.9 pp contribution to growth q/q, and by 1.8 pp y/y (out of total GDP growth at 2.3%. Housing investments dampened growth marginally, as over the past 4 quarters
- Business investments fell 0.8% (-0.1 pp contrib.), but are still up 1.6% over the past year (0.4 pp contrib.)
- Exports fell 5% while exports were flat and net trade deducted 0.7% from GDP growth (from +0.8 pp in Q1) – and by 0.7 pp last year, and the contribution has been negative since 2015 – because domestic demand has been on the strong side
- Government demand made a 0.8 pp contribution, following +0.4 pp in Q1 – and by 0.4 pp last year

Business investments down in Q2, are at a quite high level

Housing investments have peaked. Government investments may have bottomed

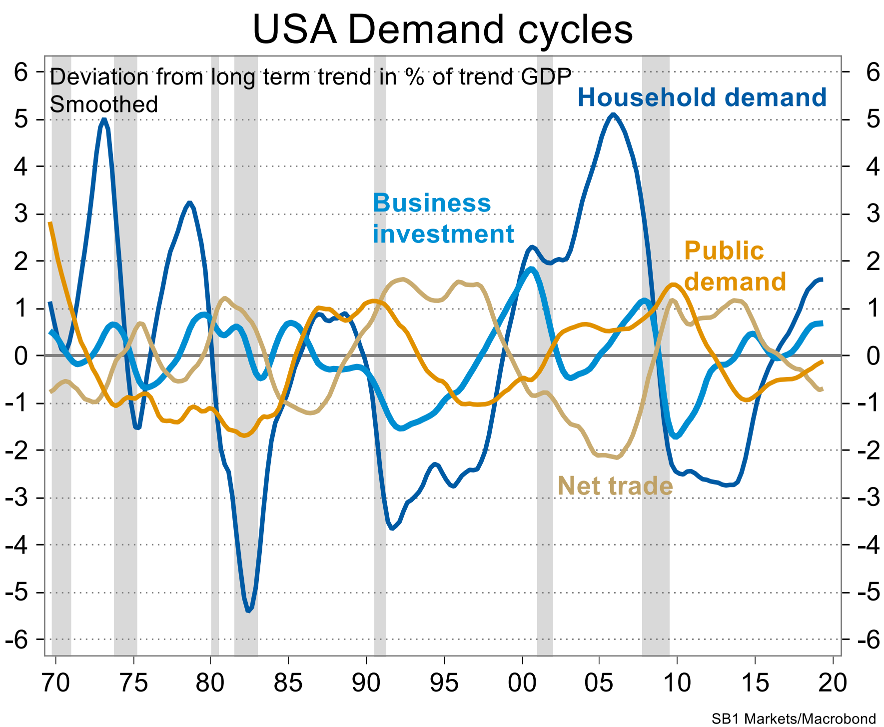


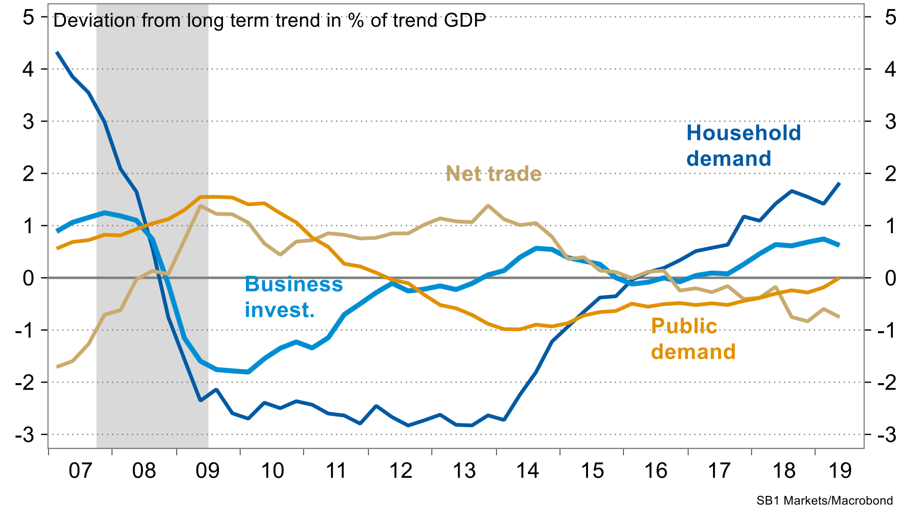


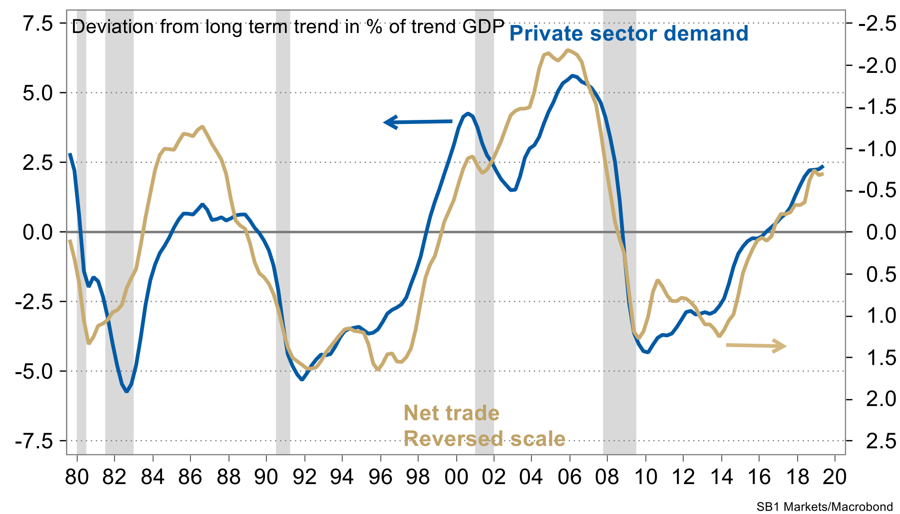
- The decline in total business investments was the first since Q4 '15. Oil investments have been the main driver for higher business investments recent quarters (there too) but have fallen slightly the past 4 quarters. In Q2, bus. investment ex oil fell marginally too
  - » IP/software investments are increasing at a high speed (some 8% y/y), and now constitutes more than 1/3rd of all business investments. These investments have always been less cyclical than investments goods, indicating that cycles in total investments will be less harsh than before. In addition, business investments in structures are not dangerously high, neither are equipment investments.
- Housing investments are slowly declining vs GDP, while the level is not very high – and should the downturn come, it can not impossible be a large one (but several housing recessions have started at approx. the same level of the housing investment/GDP ratio

Households the main demand force, has business investments peaked?

Public demand has recovered. Net trade trending down, due to rising domestic demand



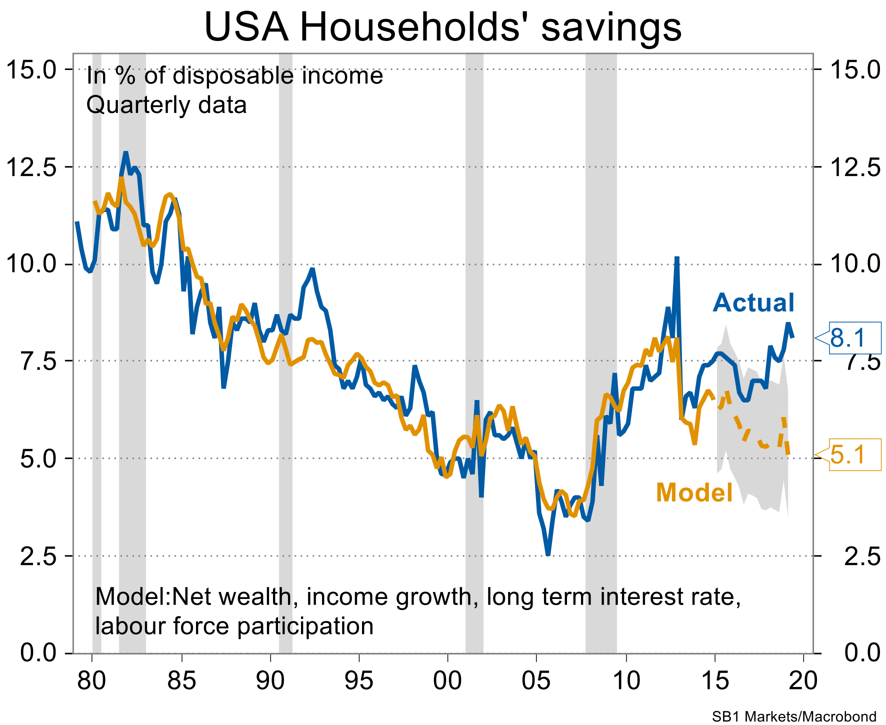


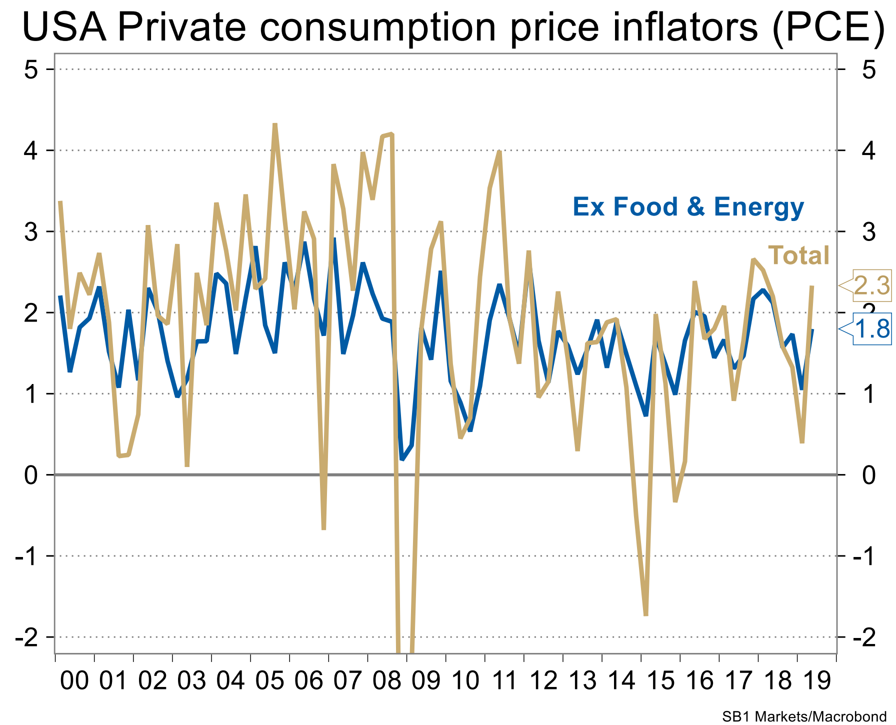


- A strong USD is not to blame for a negative growth contribution from net trade the past years, a strong US is rather a result of strong domestic demand
  - » Net trade correlates close to the activity level in the US, or rather more precise, to private domestic demand in the US
    - Net trade absorbs 1/3 of changes in private domestic demand, the inevitable net trade 'leakage', as domestic production can not take the whole adjustment

Another BIG upward revision in the savings rate!

The savings rate fell in Q2, but the level has been revised up by 1.5 pp, signalling more robustness

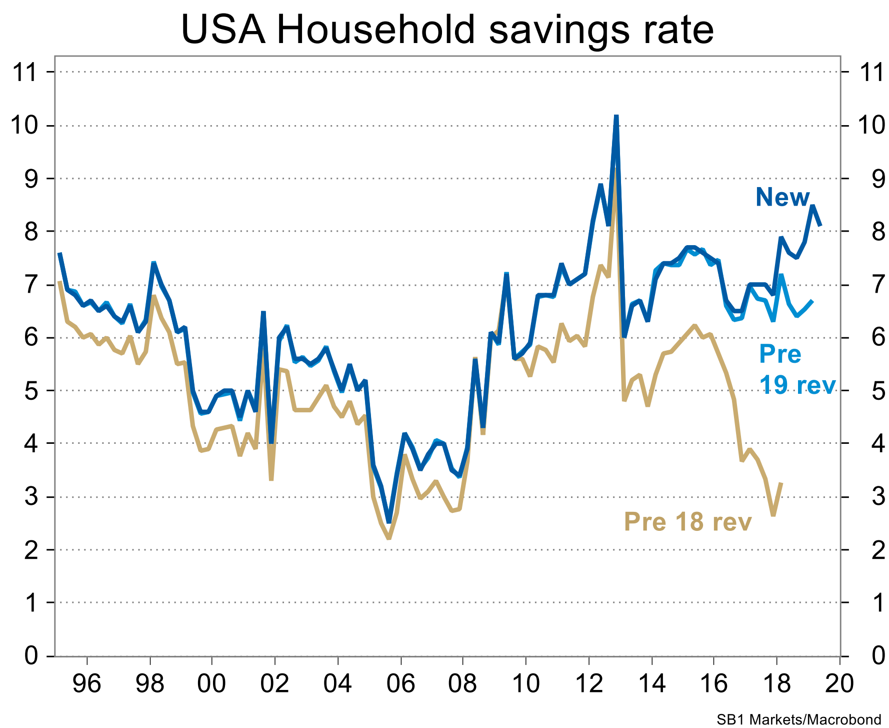


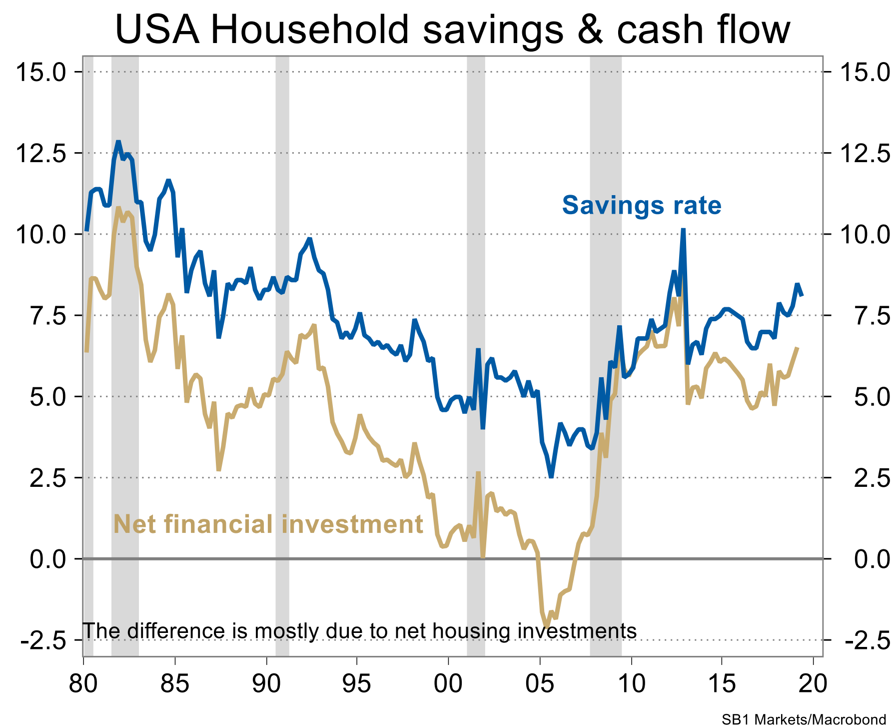


- One year ago the savings rate was revised sharply up due to new (and much higher) estimates of tax evasion. Now the savings rate once more is revised up, by up to 1.5 pp, and it was above 8% in Q2. Check the difference vs. the chart at the next page. Household cash flows are also much stronger than previously assumed. Good news, reduces the risk for a contraction in household spending
- The core PCE price deflator accelerated to 1.8% in Q2 from 1.1%, not that much below the Fed's 2% long term inflation target. The total PCE deflator accelerated to 2.3%

The savings rate has been revised to 8% from 3%, via 6.5%

Savings are the discrepancy between two large numbers – and is a moving target…

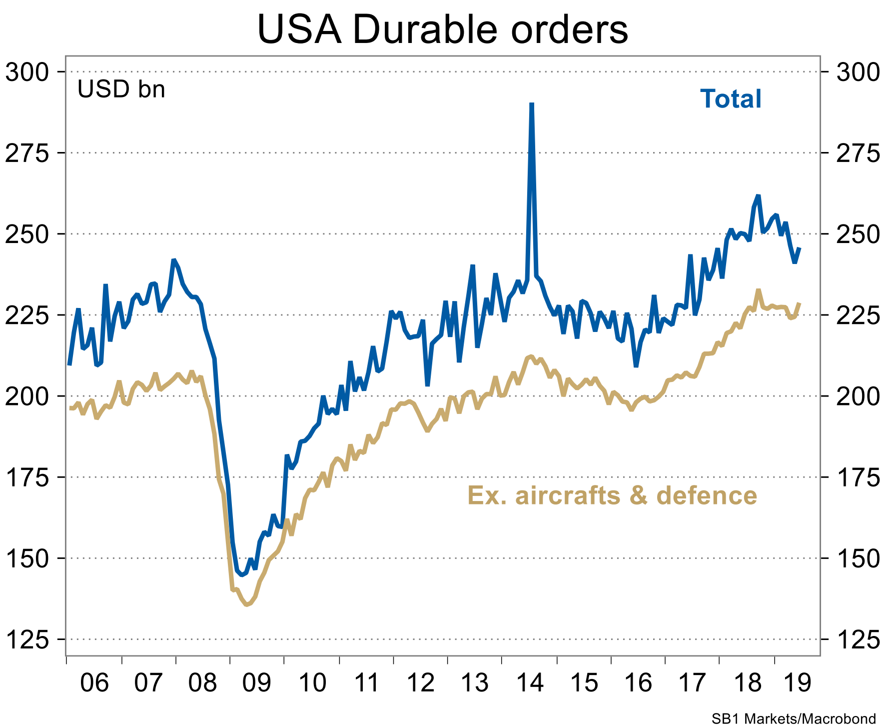


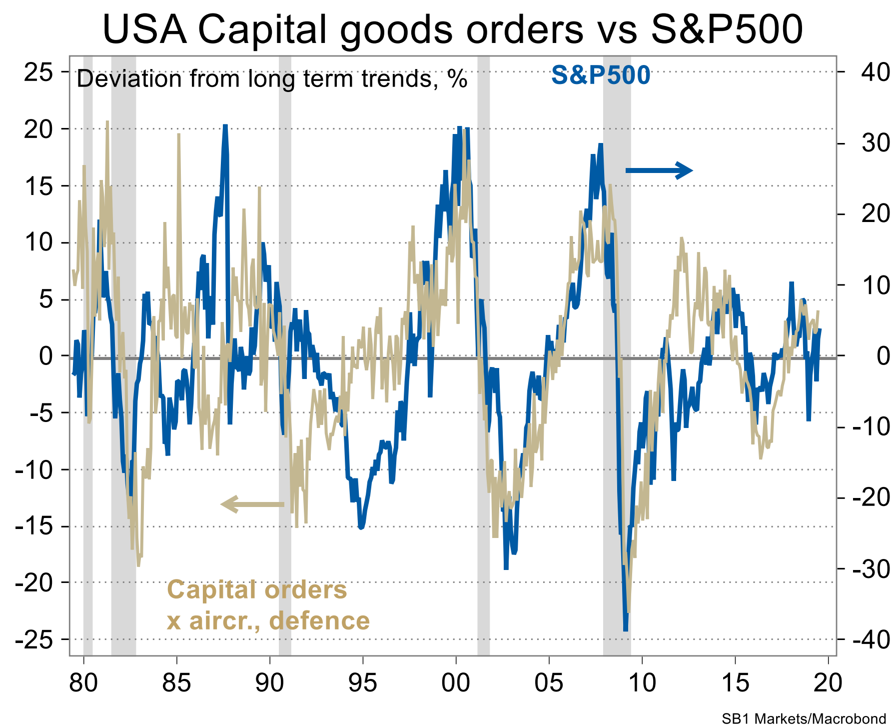


- Household income growth was revised up in the 2019 annual revision, and more than consumption. The savings rate was revised from 6.7% to 8.5%
- More of the tax cuts have been saved – and households are more robust than the previous data indicated; the new savings rate is well above the average of the past decades, at above 8%. The increase in household net financial investment rate explains why the huge increase in the public sector deficit has not sent the current account deficit down the drain

Durable goods orders do not confirm business investment setback

Core durable & investment orders up in June – not strong, but no downturn either

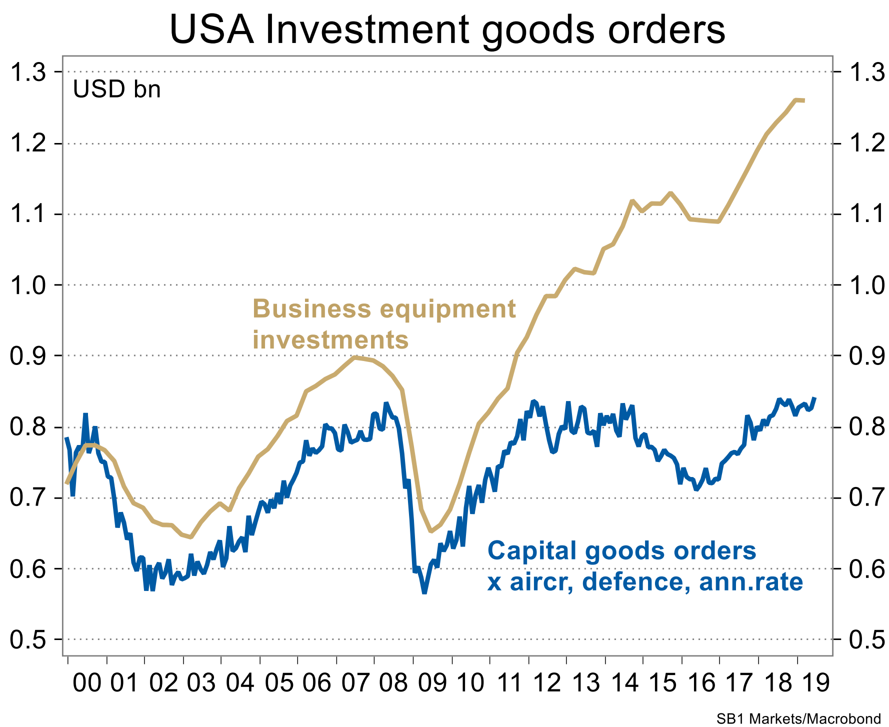


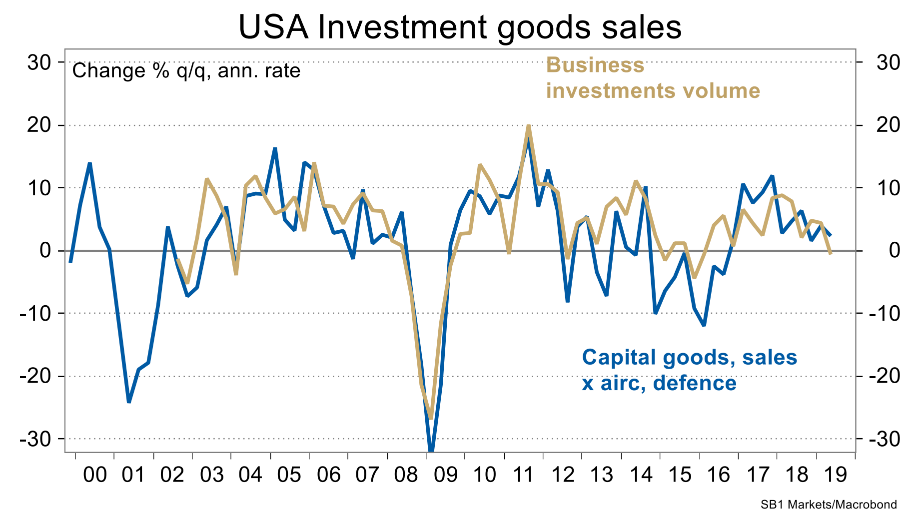


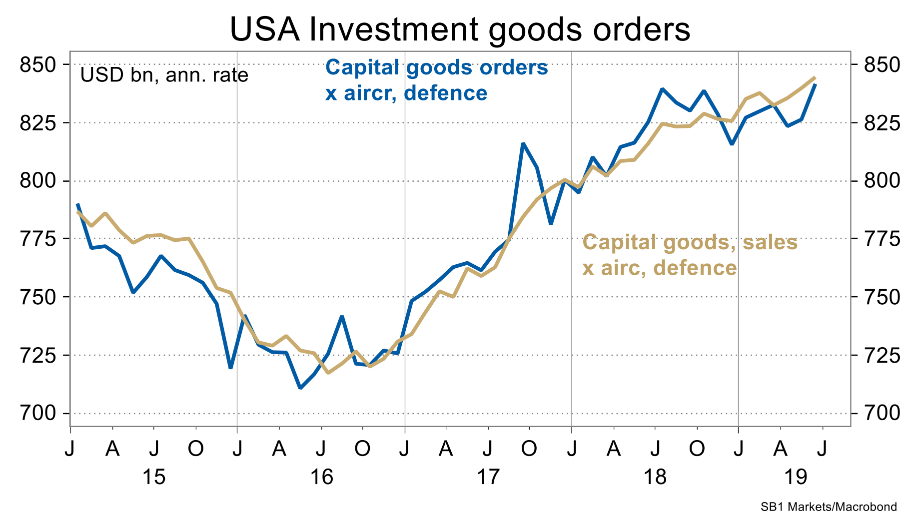
- Total durable orders rose 2% in June, expected 1%, following the 5% decline the previous two months – which partly has been due to troubles with Boeing's Max plane. Core orders (ex aircrafts and defence) rose 1.9% in June, and are marginally above the spring level – but has not grown since last summer
- Core capital orders rose 1.9% too, and sales by 0.6%. The trend is marginally up, signalling weakness but no decline the business investments, which were reported marginally down in Q2 GDP
  - » Deviations in businesses' core capital orders are quite well correlated to the stock market. Slower order inflows indicate a limited upside on the stock market, barring some 'suckers' rallies)

Capital goods orders/sales signal slow growth in business investments into Q3

Core investment orders almost 2% in June but trend remains flattish



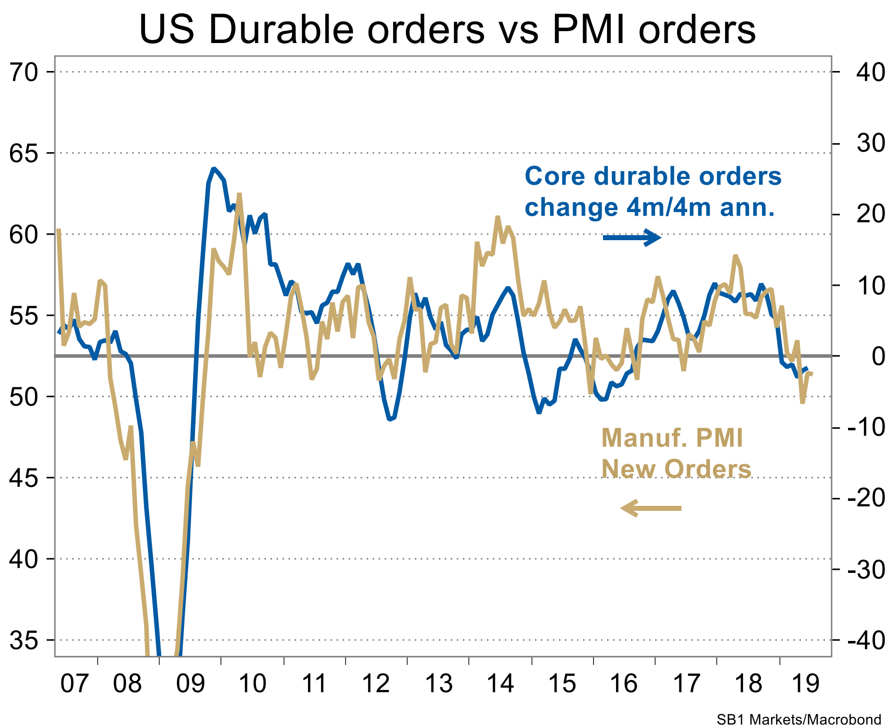


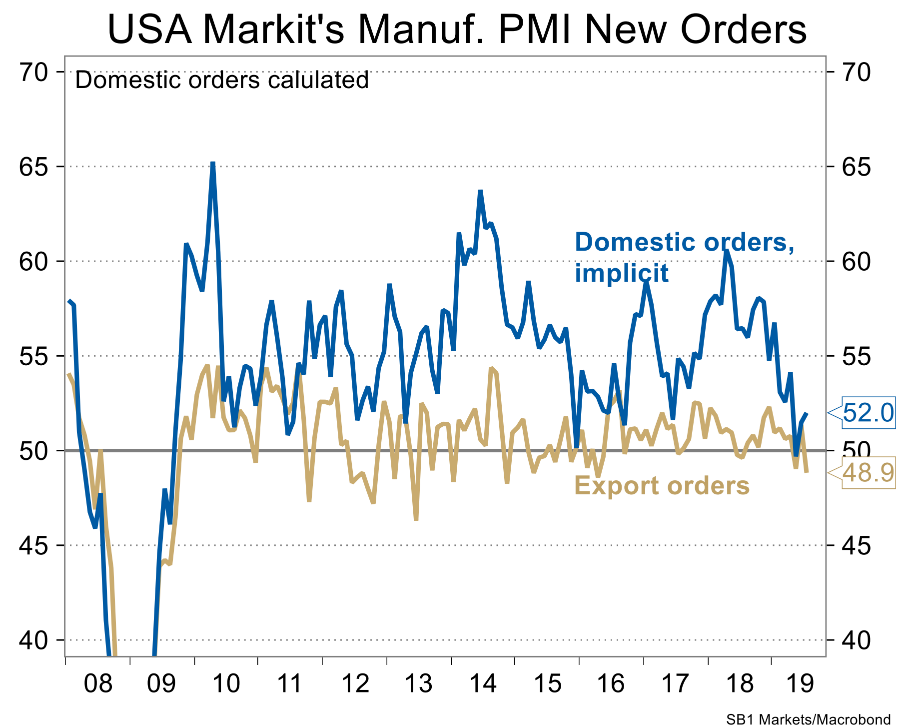


- Investment orders (core) rose 1.9 m/m in May, well above expectations and are up 2.3% 3m/3m (now Q2, annualised)
  - » Sales rose 0.6%, and are slowly on the way up
- Orders/sales are indicating business investments just grew slowly in Q2 but do <u>not signal any abrupt setback</u>. Neither do business investment surveys, check next page

PMIs point to a moderate decline in order inflows

.. and the downturn is primarily driven by weaker domestic demand, <u>not exports…</u>

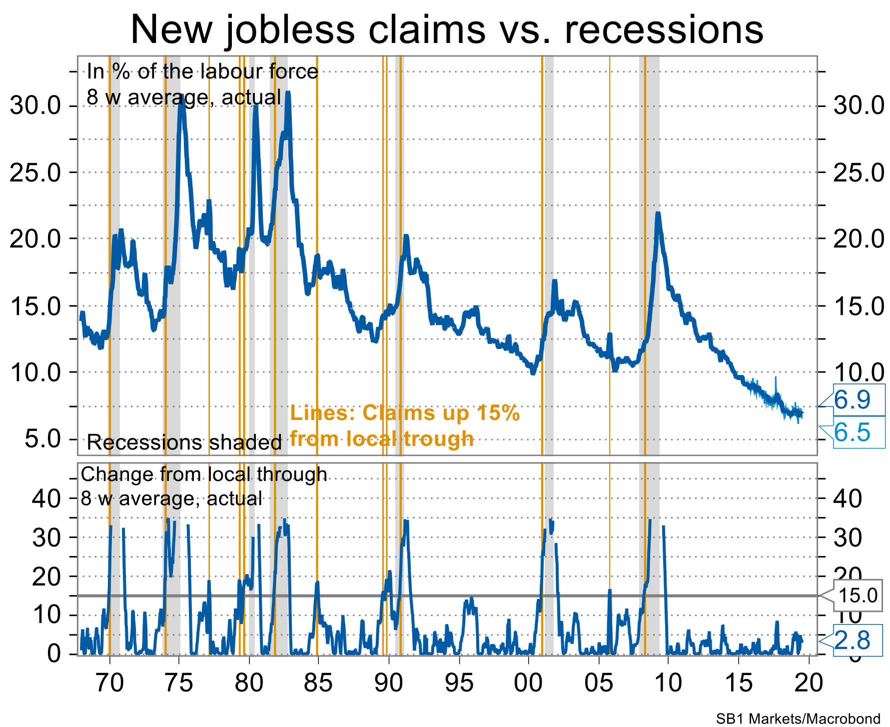


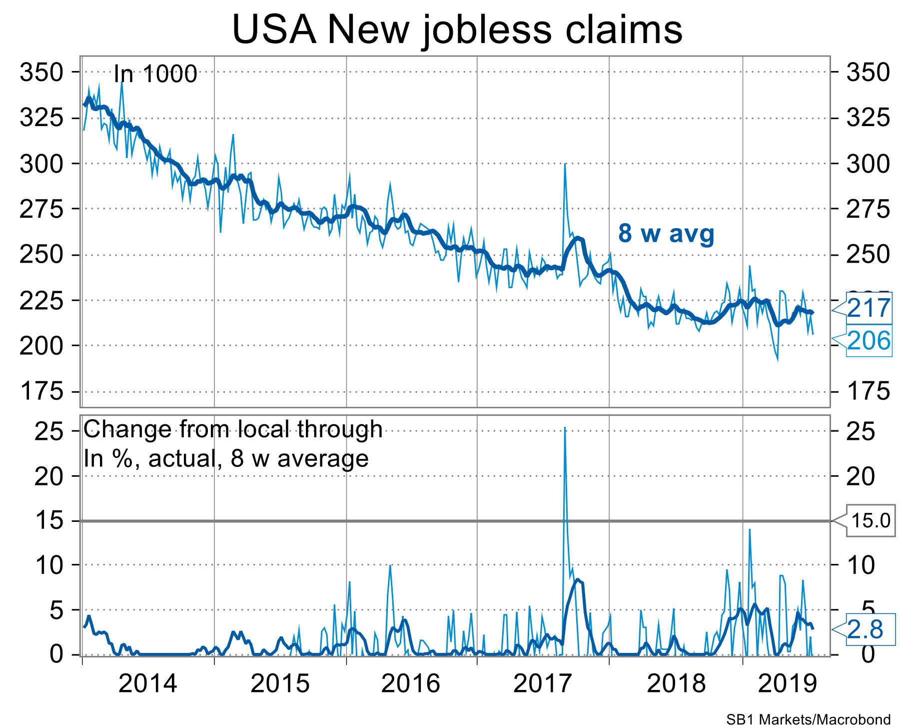


- At least until July, where the export order index in the PMI fell

Jobless claims still on the way down, very low last week

Jobless claims down to 206', lowest since early spring and the 4th lowest in this cycle

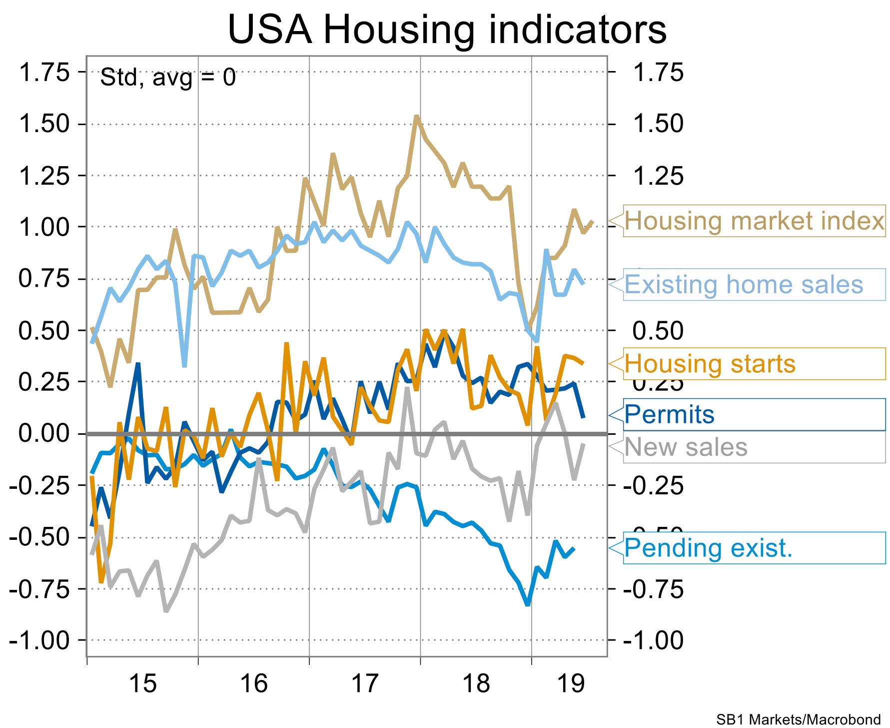




- A more than 15% increase in jobless claims (measured by the 8 week avg) is usually a good indication of a recession, and a yellow 'recession' warning line is to be drawn, check the chart to the left. So, no reason to worry now?

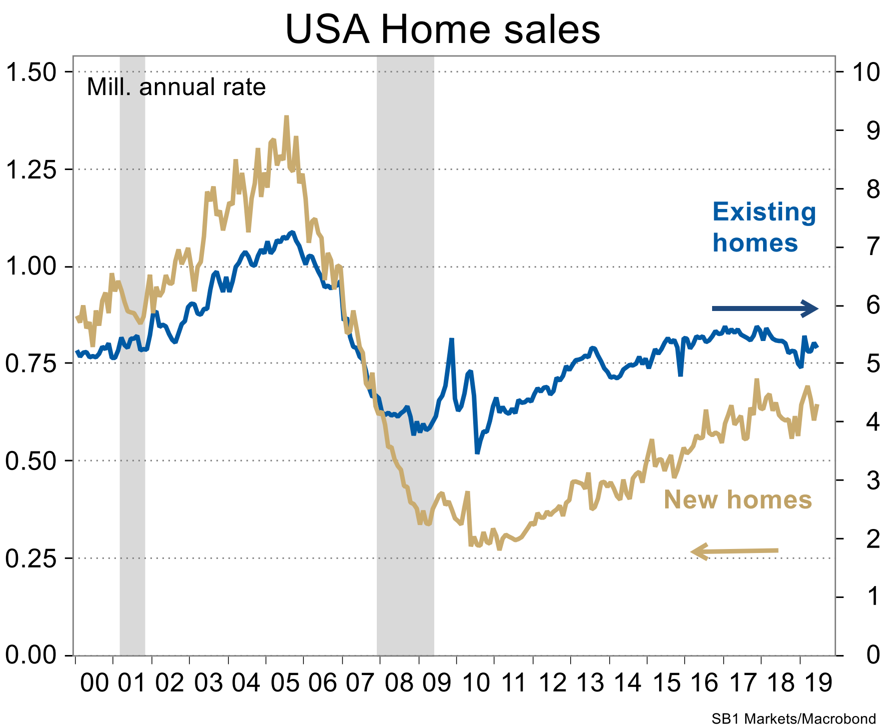
Most housing indicators back to flat to a downward trend

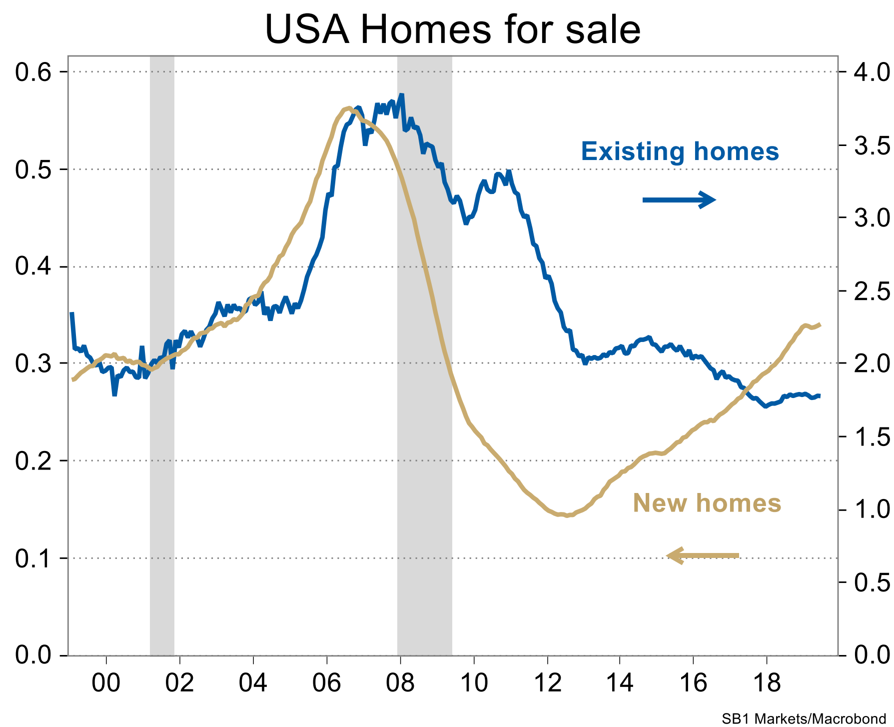
New home sales up, from a downward revised level, existing homes marginally down



New homes sales up in June, from a downward revised May

Trend past two years flat, at best but the level is not that high

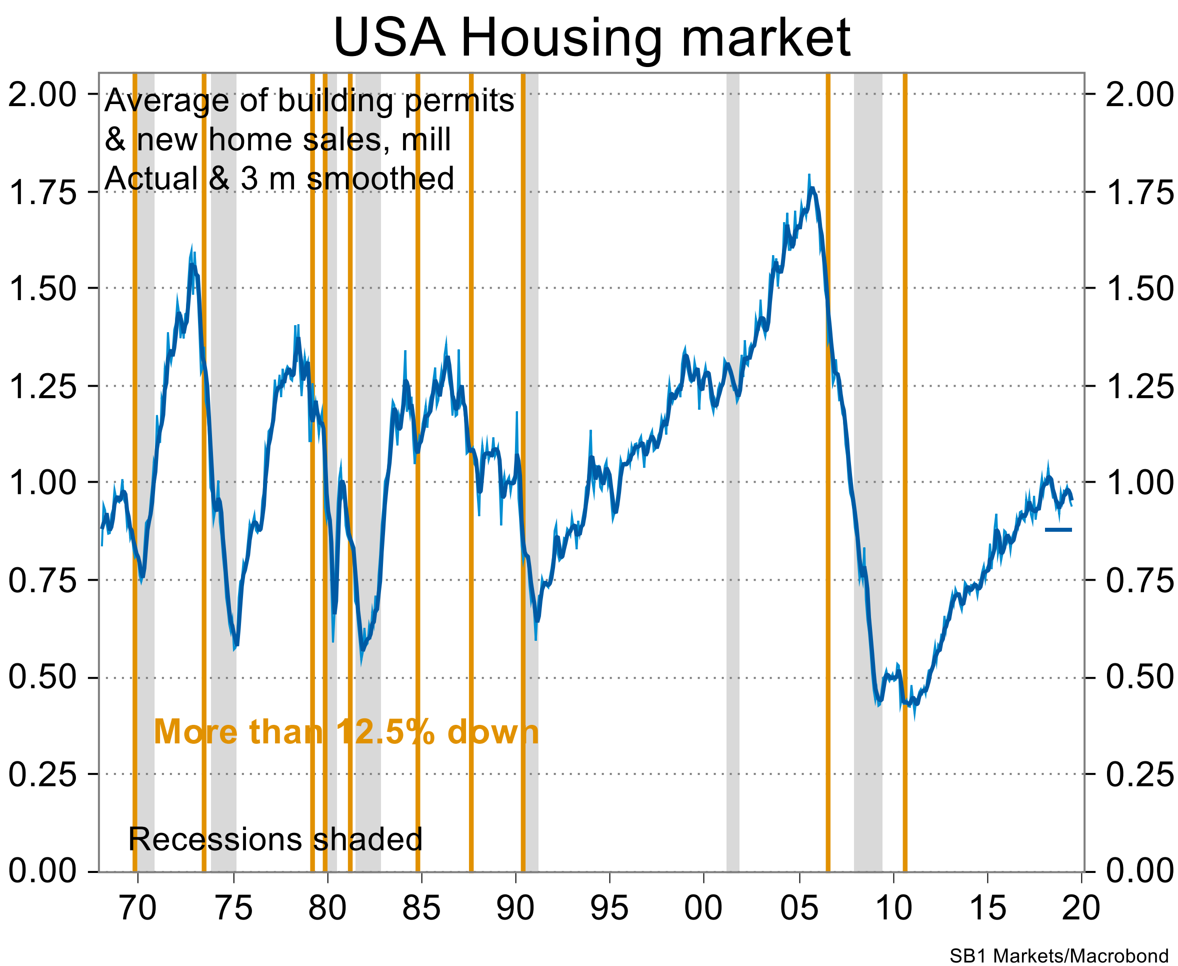


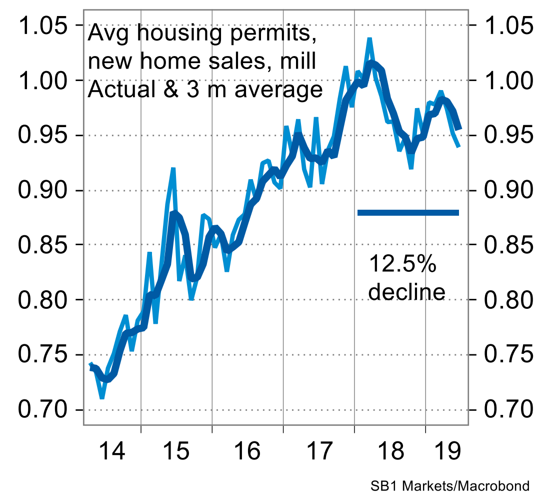


- New home sales rose to 646' in June from 604' in May, expected up to 659' up from prev. reported 629'. In sum 3% lower than expected. Following the decline the two previous months a part of the increase earlier in 2019 is reversed – and the broad trend line over the past two years is flat
  - » The number of unsold homes rose from 2012 until Feb this year but has been since (but rose marginally in June)
- Housing starts/permits are trending slowly down – and permits fell sharply in June (probably a one off but still)
- Existing home sales fell slightly in June, and marginally more homes for sale

Housing vs recession: Not reassuring past months but still no recession in sight

The market recovered in Q4 but has lost speed since

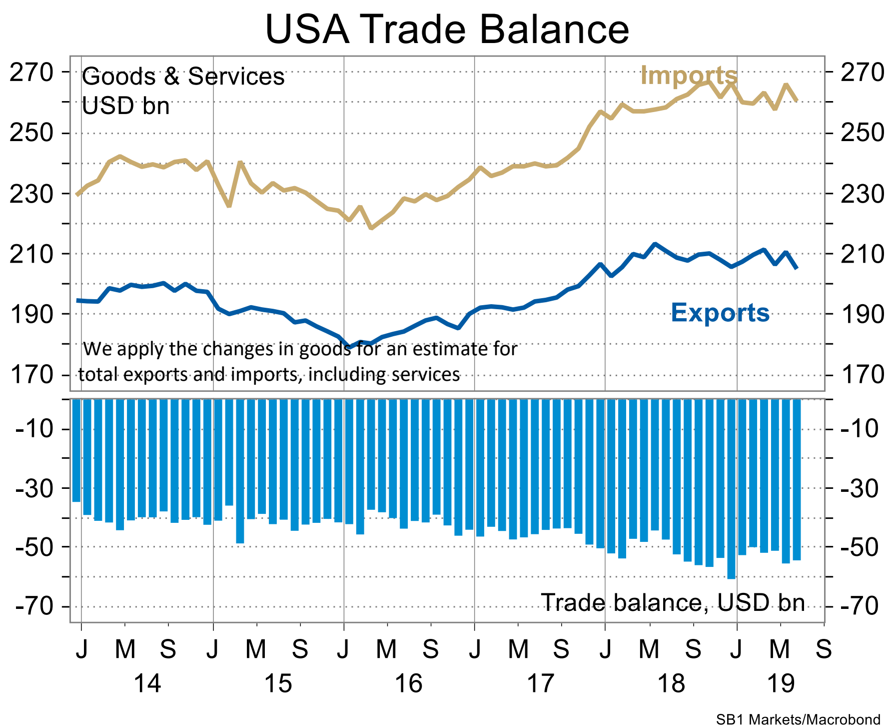


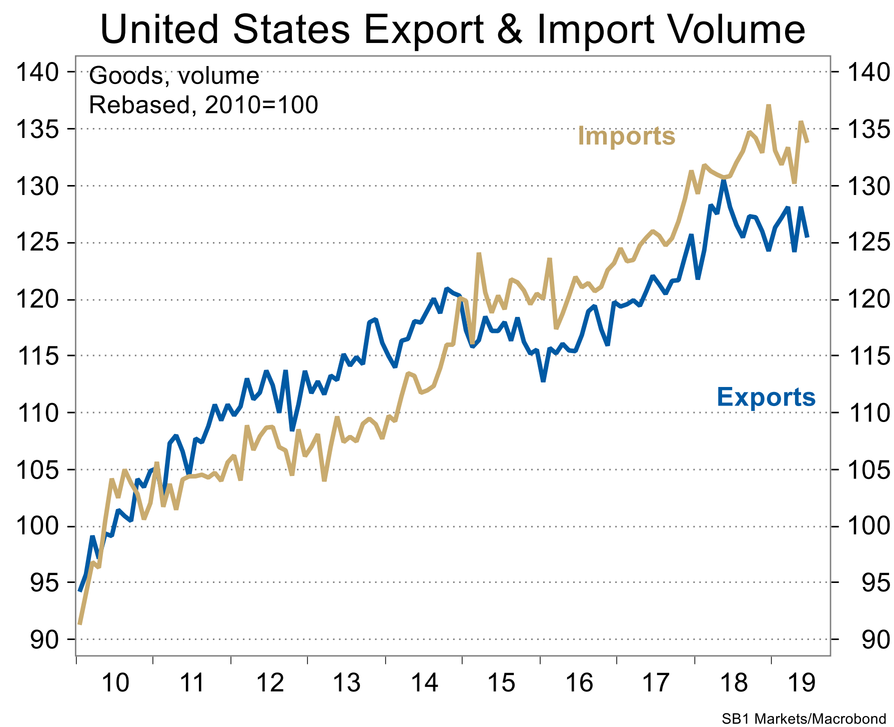


Memo: New Home sales are assumed down to 675' in in April, in line with consensus f'cast

The trade deficit stable in June but trade was a drag on growth in Q2

Both exports and exports fell in June. Both imports and exports are trending slowly down

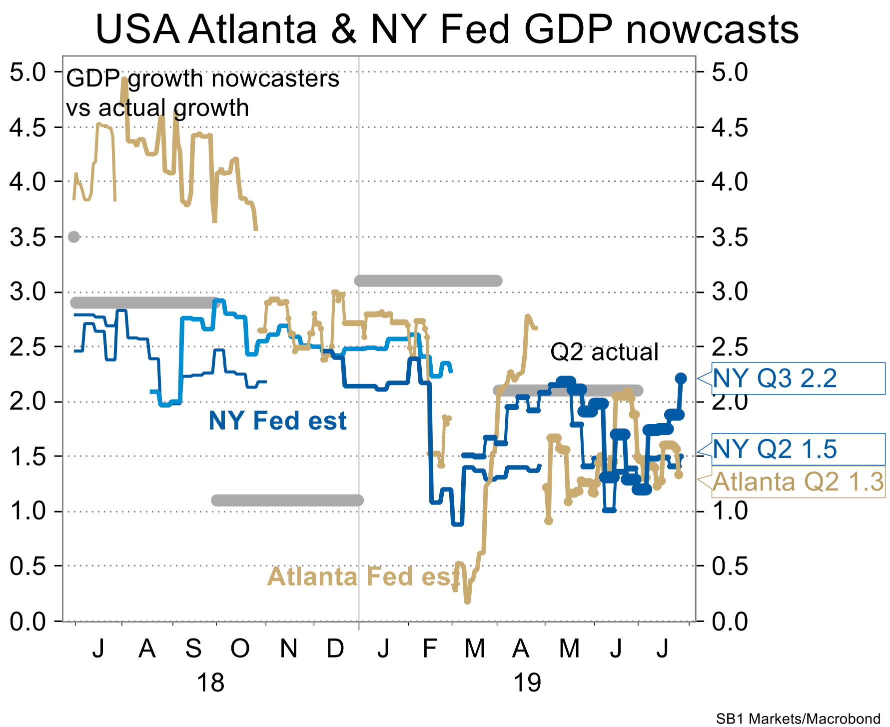


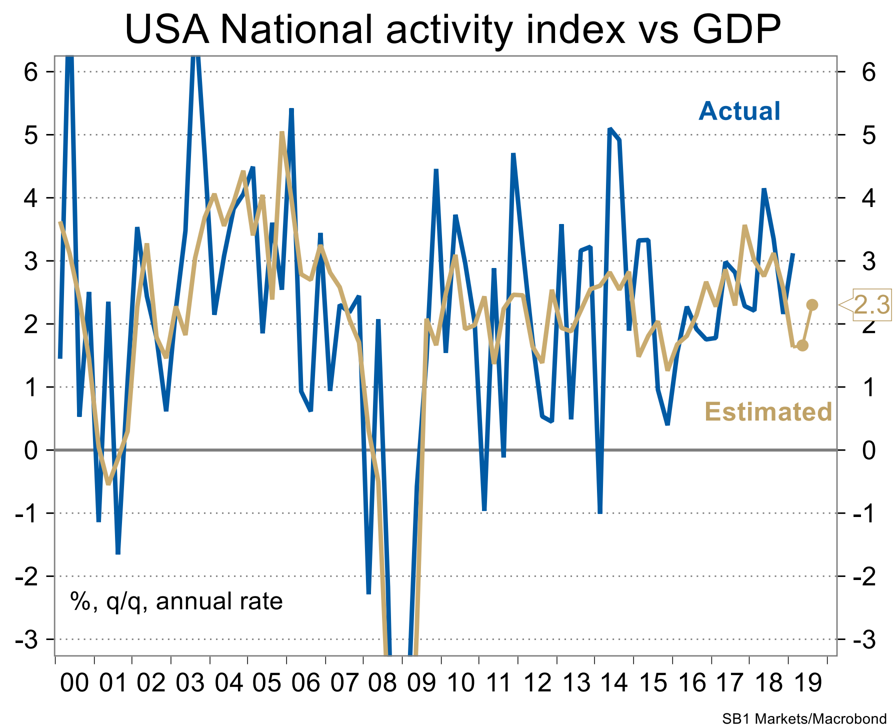


- The advanced trade data (goods only) indicates that the overall trade deficit was marginally slimmer in June, at some USD 54.5 bn
  - » Imports fell both in nominal and volume terms. The trend ins down, at least in value terms. surprisingly spiked 4% m/m in volume terms, the highest monthly rate in 4 years. Possibly due to the escalation of the trade war
  - » Exports fell to, hand is trending down both in value and volume terms – but the decline is not dramatic
  - » Q2 national accounts revealed a negative drag to GDP growth at 0.7 pp q/q, and by 0.4 pp over the past year
- The deficit vs. China is reduced (no May data yet), no doubt due to the trade war, as imports from China is sharply down – but the overall deficit is not cut

Fed nowcasters underestimated (the first) Q2 GDP estimate

Nowcasters said 1.3-1.4%. The first official estimate at 2.1%. NY says 2.2% growth in Q3



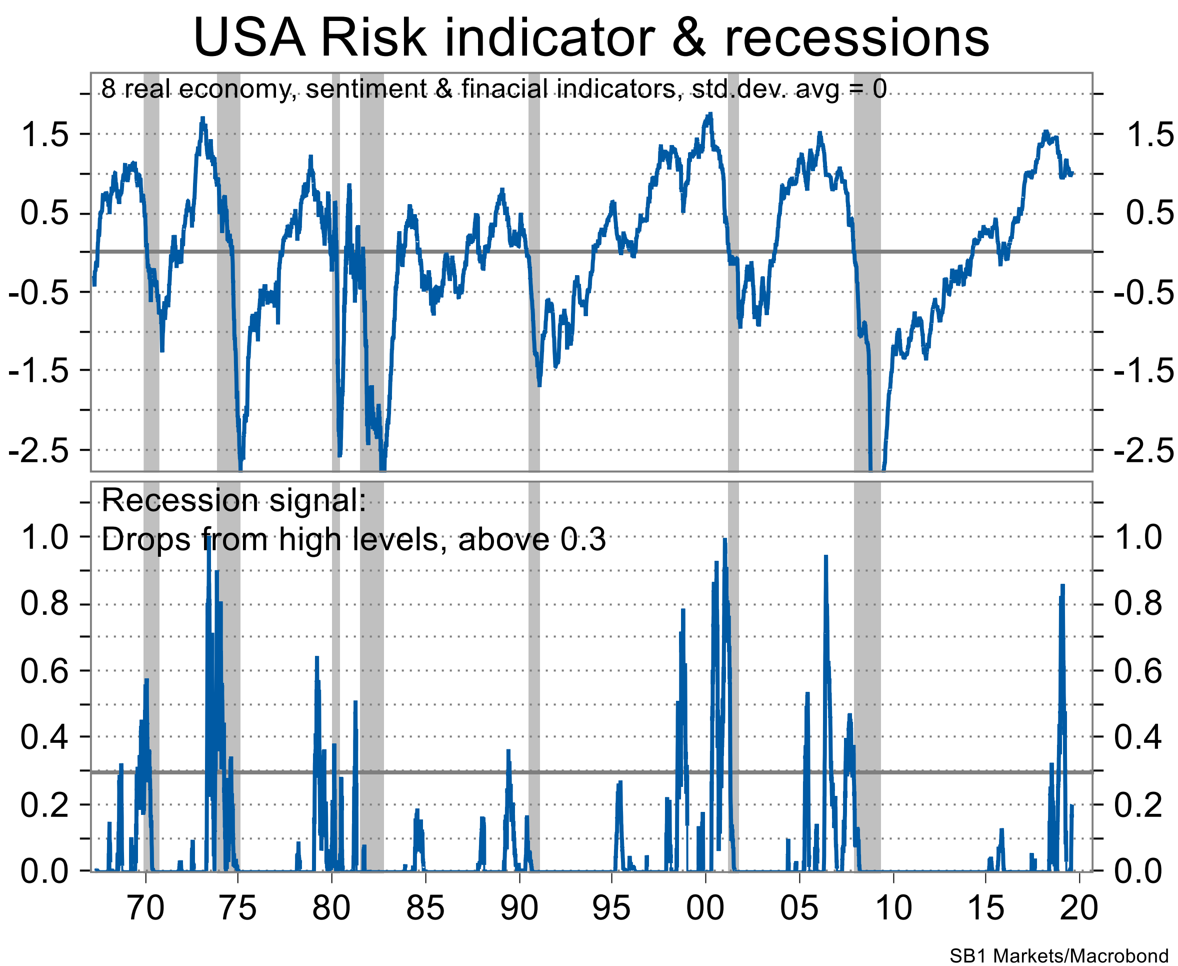


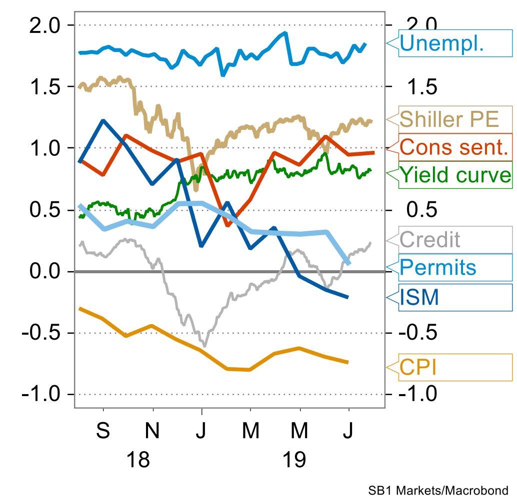
- The National activity reported 1.7% growth in Q2, and a 2.3% speed into Q3

dd

US Indicators: Not a recession warning, now

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

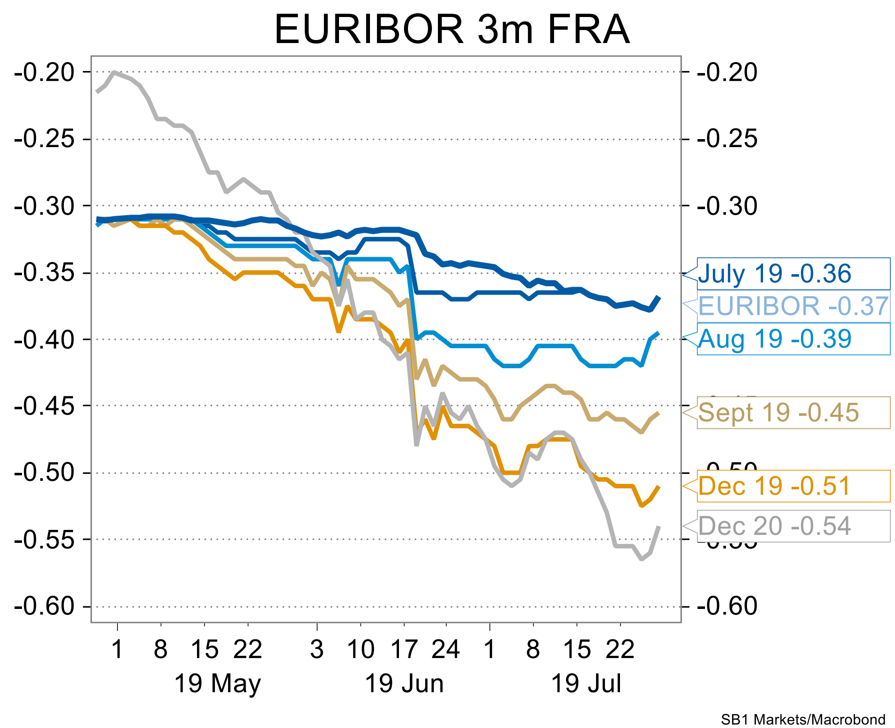


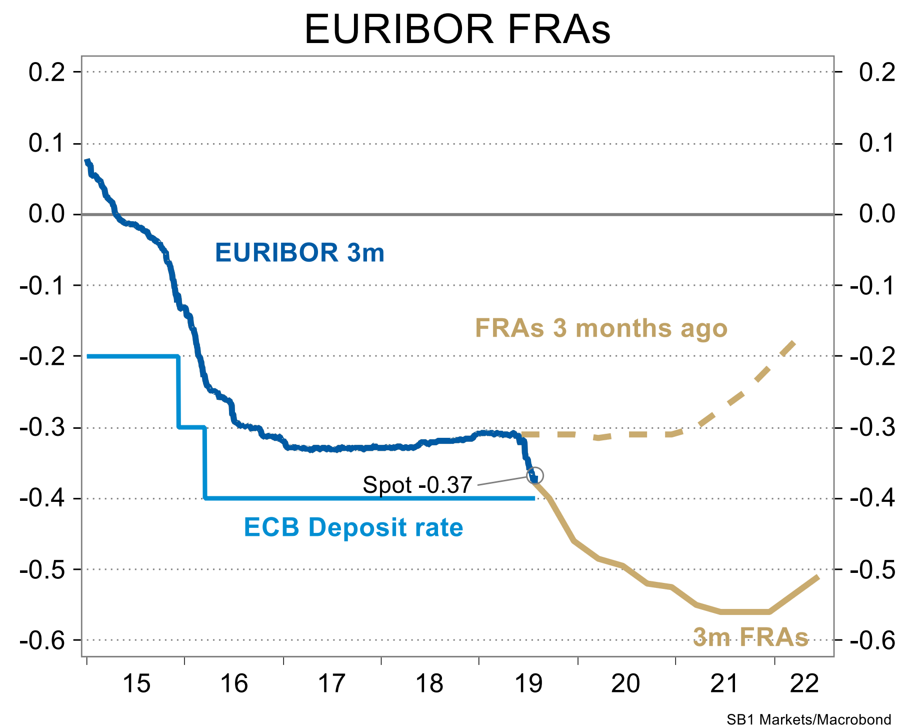


Inspired by Goldman Sachs Bull/Bear indicator. We are using jobless claims instead of unemployment, and have added housing starts, consumer sentiment, and a credit spread. In average, our Risk or Good Times Indicator leads recession starts by 18 months. The lower panel above shows changes in the squared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

ECB ready to act, but not now

Growth, inflation too low. All measures are being considered. Rate at present or lower level in H2-20



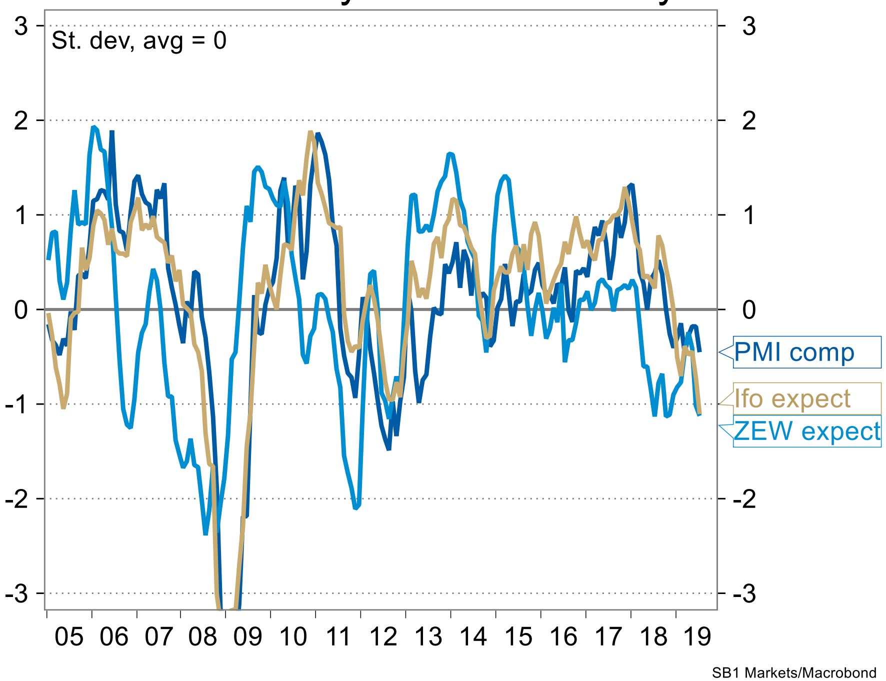


- Some had expected the ECB to act now but that was premature. However, Draghi & co clearly signaled that the bank was worried both about the growth outlook, especially in the manufacturing sector and for the decline in inflation expectations
- The bank is considering all available measures. Rates may be cut, asset buying programs extended.
- Most likely, the Bank will cut its signal rates at Draghi's last meeting, in September. More QE is likely too.
  - » The market is expecting the ECB to cut its deposit rate by 10 bps to -0.5% in September – and further down to approx -0.6%
  - » No doubt, other measures could have larger impact on the economy, than a symbolic cut even further down in negative territory
  - » Expectations for more gov. bond buying has no doubt contributed to the recent decline in bond yields all over Europe

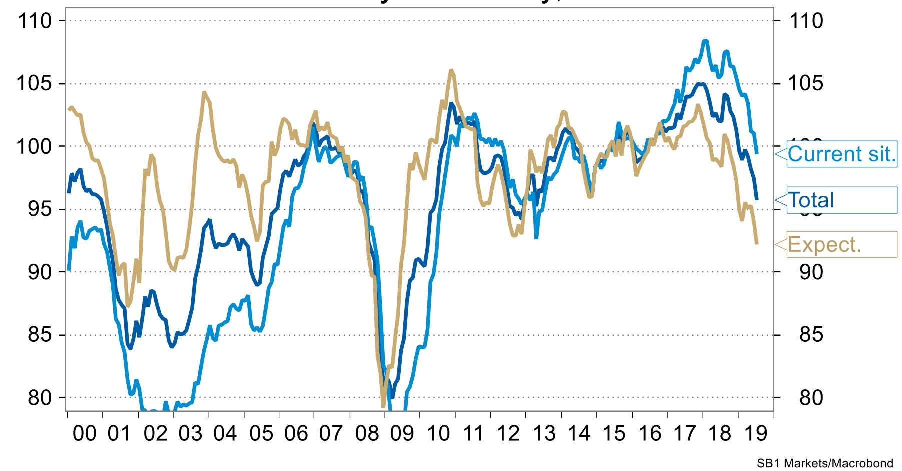
Ifo survey further down, weaker than PMI – signals contraction in GDP

Manufacturing well below average – services (ex retail) approaches an average level

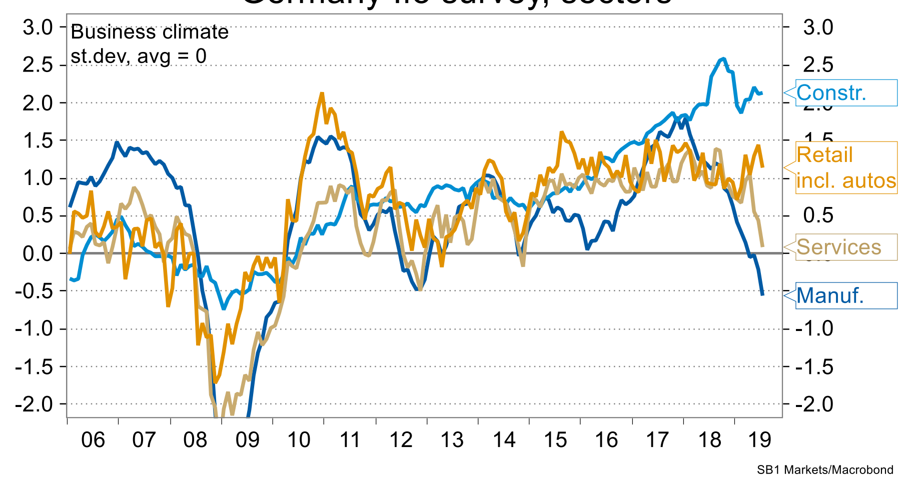
Germany Business surveys



Germay Ifo survey, total



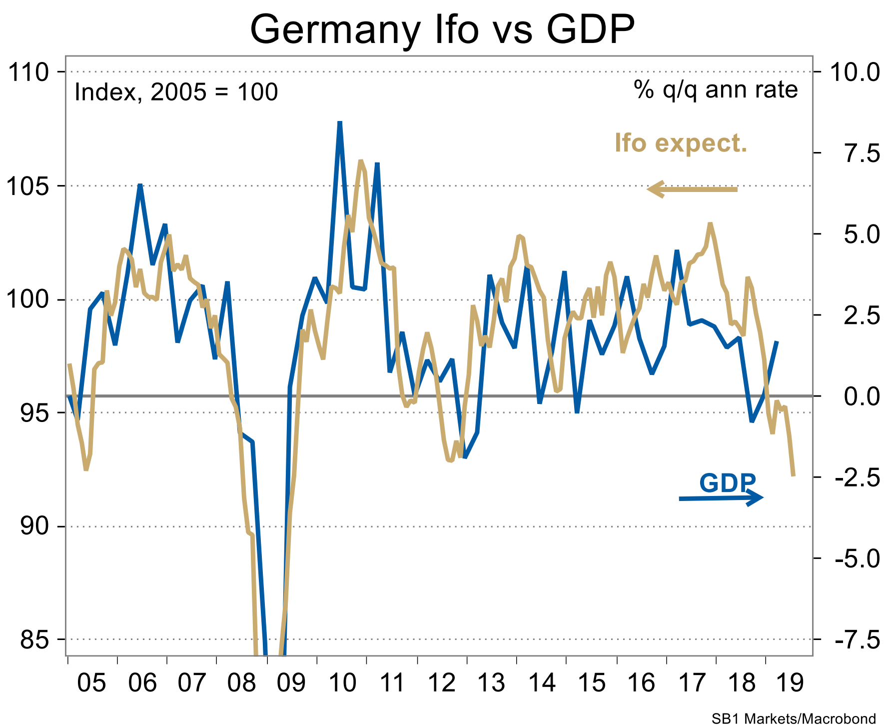
Germany Ifo survey, sectors

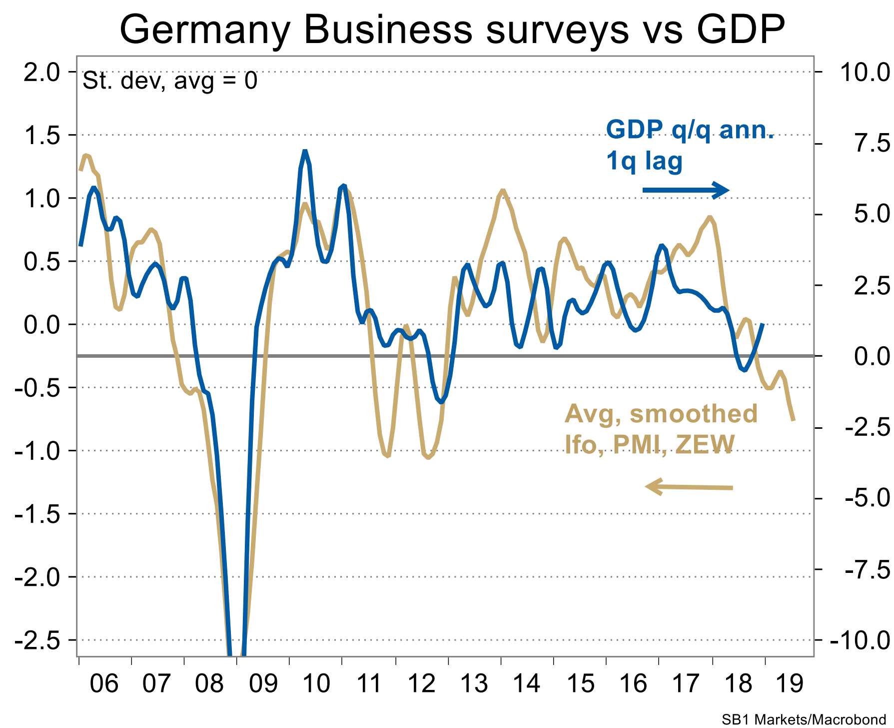


- Both businesses view on both the current situation the outlook weakened further in July. The expectation index is far below a normal level, while the current situation index is well down from the peak but still far above an average level
- The slowdown is driven by struggling manufacturers but according to Ifo, services ex. retail are slowing too, albeit still above an average. while retail and construction are strong and trending up, confirming that important parts of domestic demand remains resilient, even if the manufacturing sector is slowing

Surveys are suggesting a recession

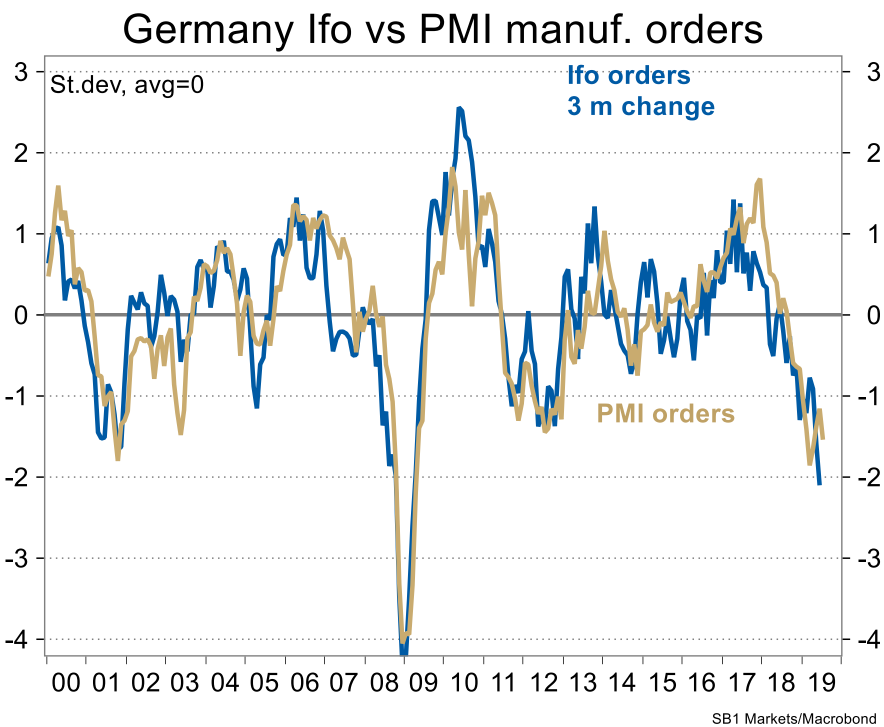
However, the surveys were too downbeat vs actual growth in Q1



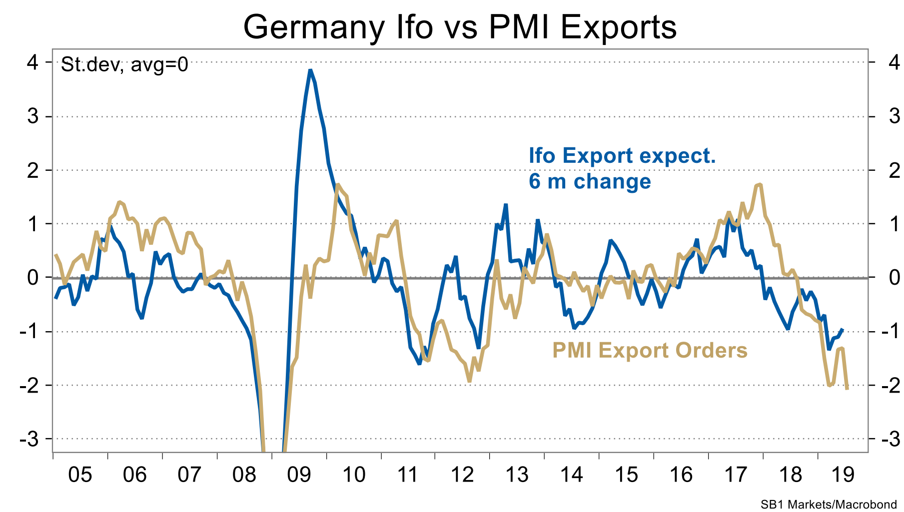


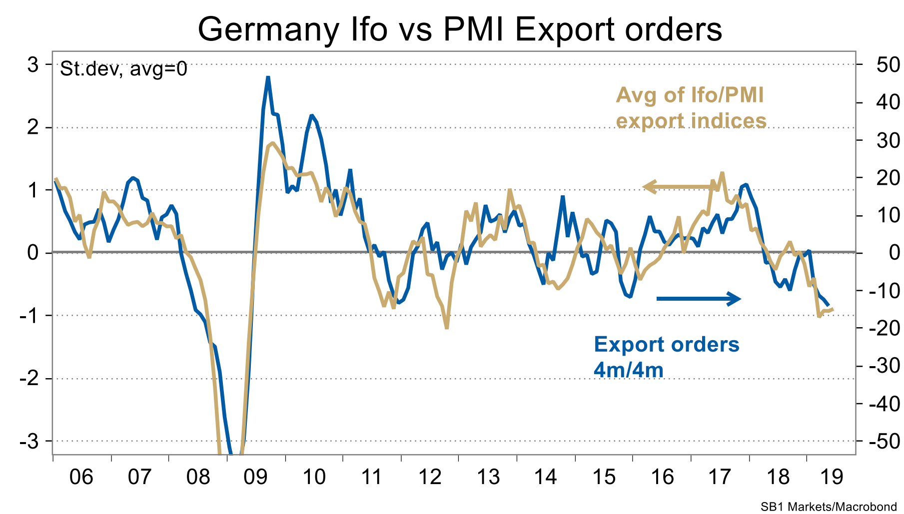
Ifo order assessments deteriorate, both domestic and export related

Underlying growth (3m change) in orders weakest since 2009, certainly not a good sign



- The level of the Ifo order index is far above the PMI. However, the change in Ifo (here a 3 m change), which is closely correlated to – but usually leading – PMI orders, is falling rapidly
- Ifo export expectations fell further in June, in contradiction to the PMI which is slowly recovering. Both are pointing to declining exports. as the PMI, both pointing to a deteriorating decline in export orders

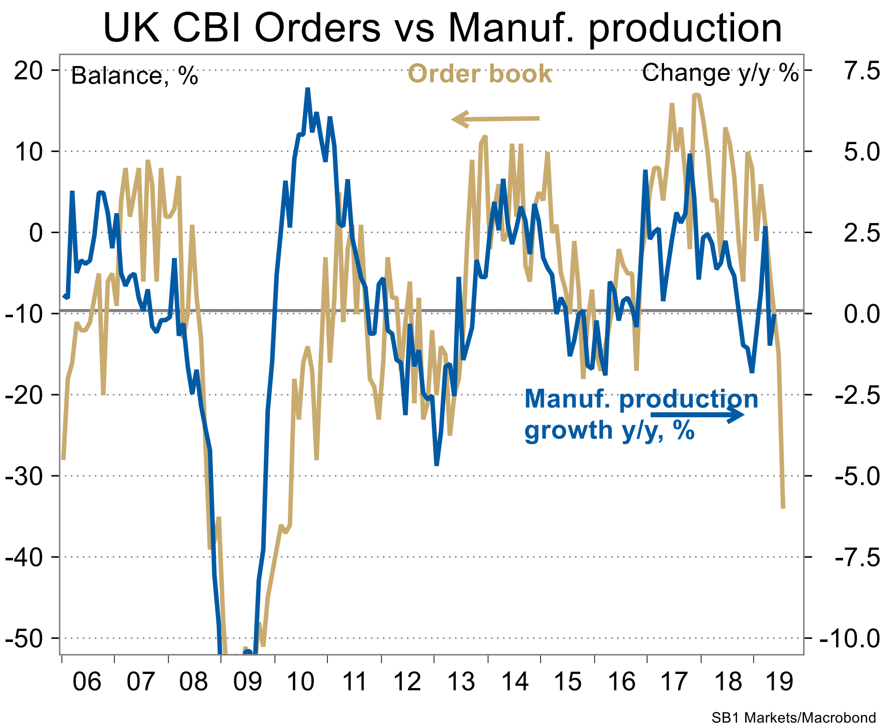


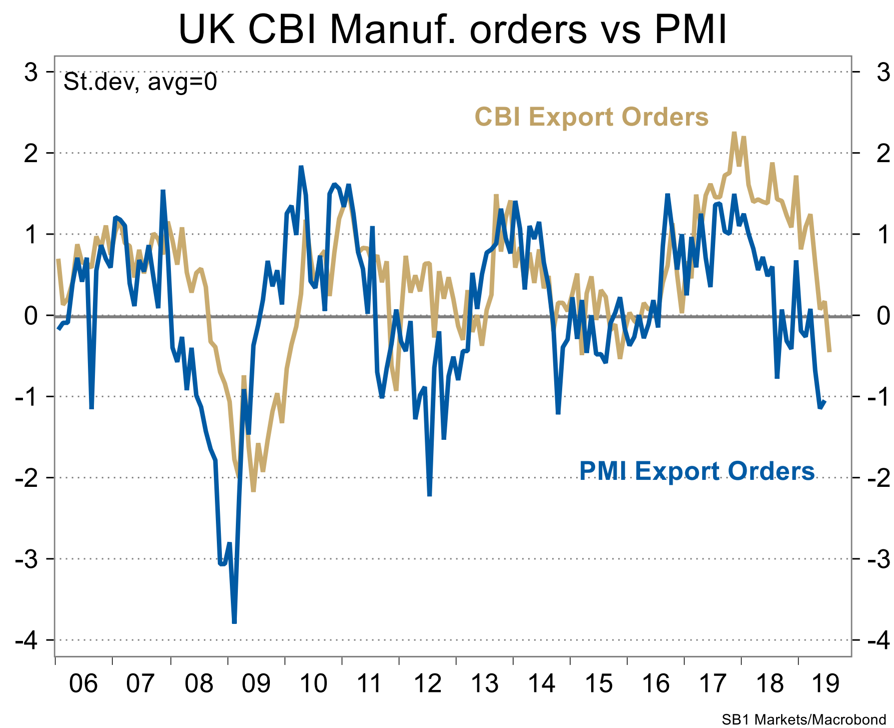


SpareBank 1 MARKETS

Manufacturing orders straight down, domestic even faster than export orders

The CBI survey much weaker than expected, manufacturers are indicating a sharp setback

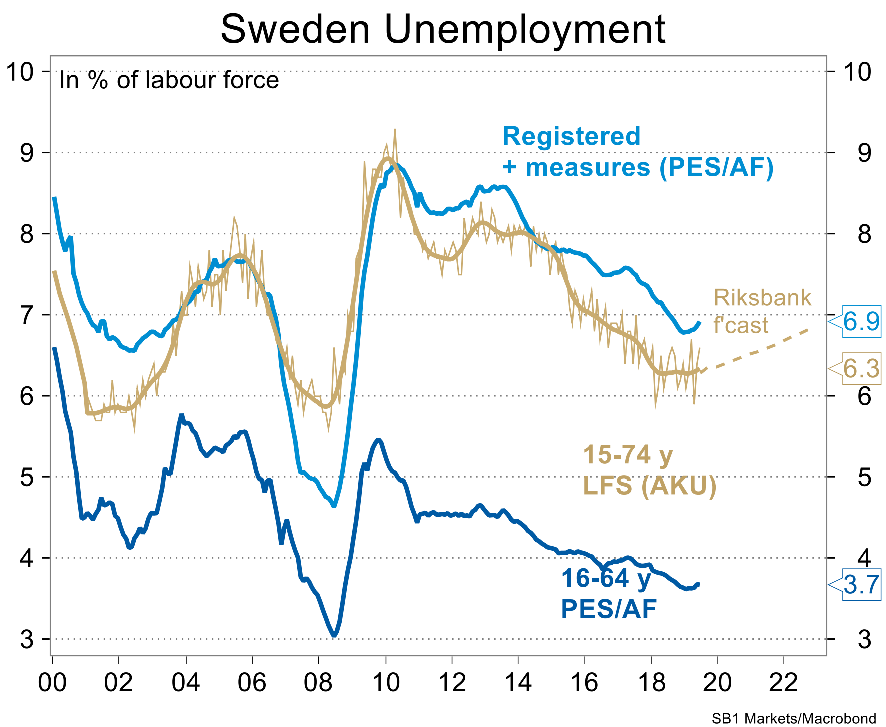


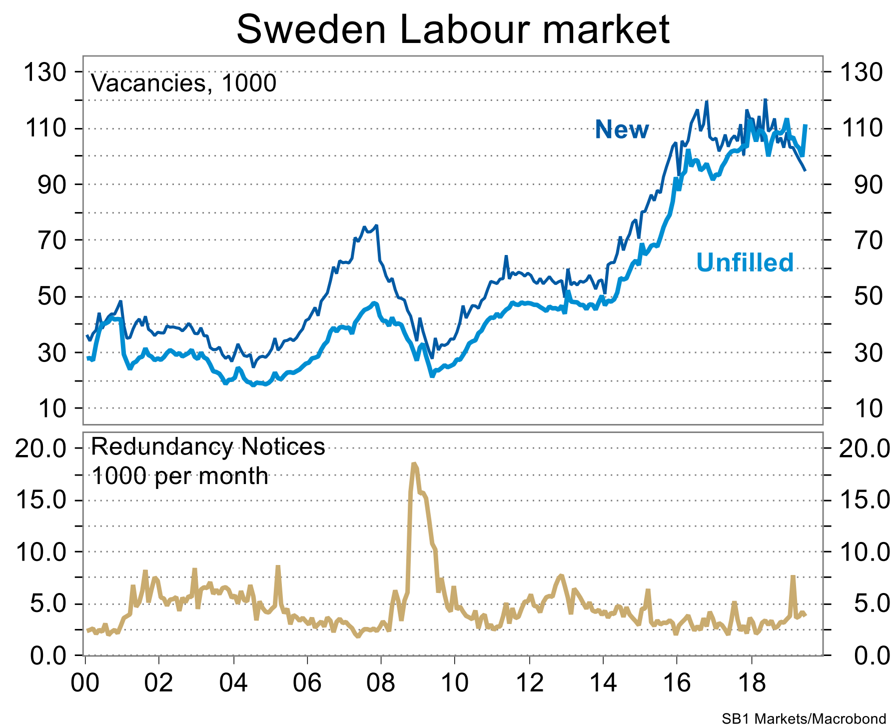


- The CBI order book index fell to -34 in June from -15 in May, expected unch. The level is the lowest since 2008 on the way down, and well above average, signalling a 5% pace of contraction in production.
  - » Earlier this year, demand has been kept up by emergency stockpiling ahead of the (original) Brexit deadline, as businesses have been reporting in the PMI survey. Now, they are probably starting to cut back their inventories, and more will come. It will most likely not be pretty.
  - » The export order index also fell in June but the level is still not far below average. The CBI is less negative than the PMI export order index, which is reporting falling export orders

Unemployment turns up?

Both registered and LFS unemployment up but more unfilled vacancies

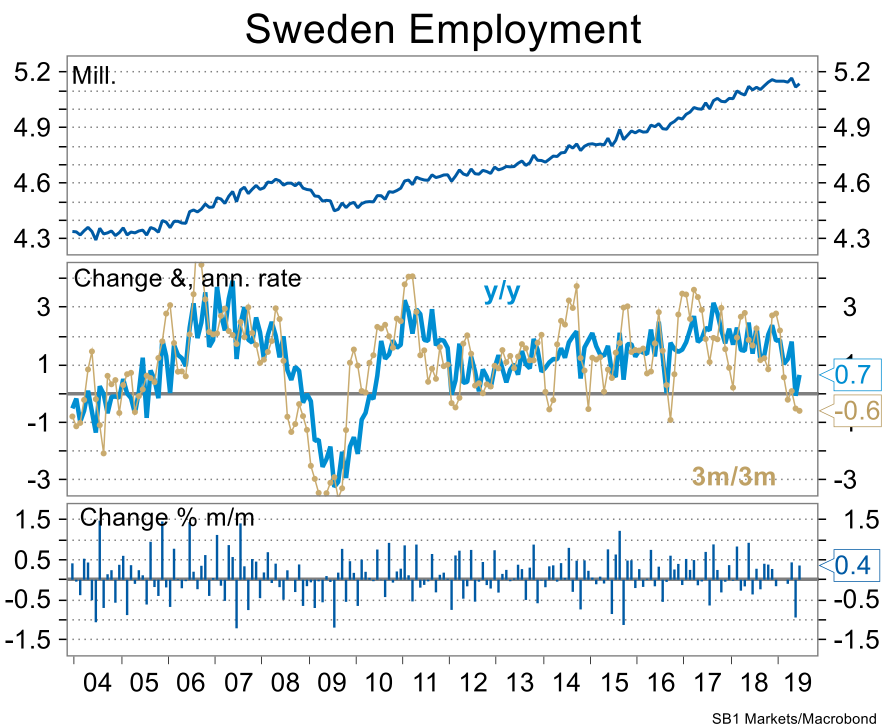


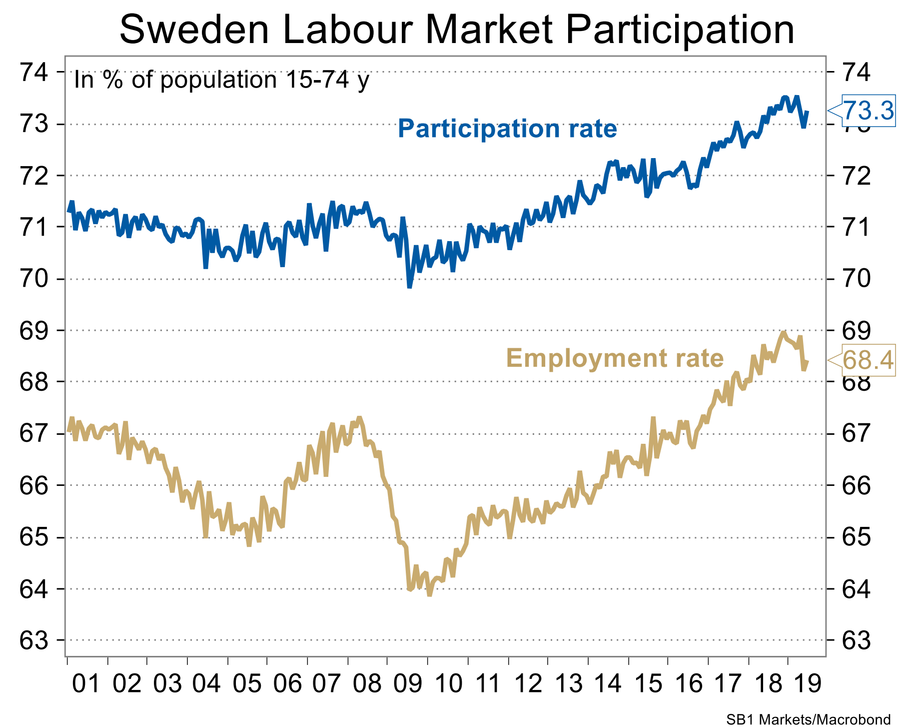


- The LFS unemployment rate rose 0.2 pp to 6.6% in June. The smoothed rate, which we prefer, was unchanged at 6.3%, but it rose slightly at the 2. decimal.
- Employment rose in June but less than the decline previous months, and it is barely up y/y
- PES/AF open (registered) unemployment rate is confirming a weakening labour market; it has turned (very) marginally up recent months
- The number of unfilled vacancies rose sharply in June, while the number of new vacancies continued downwards. We assume the trend is down for both, but leve4ls are still very high. The number of redundancies has fallen back after a temporary spike but may be trending slowly up

Employment up in June but down in Q2

Both participation and employment rates have fallen recent months, and more than 'normal'

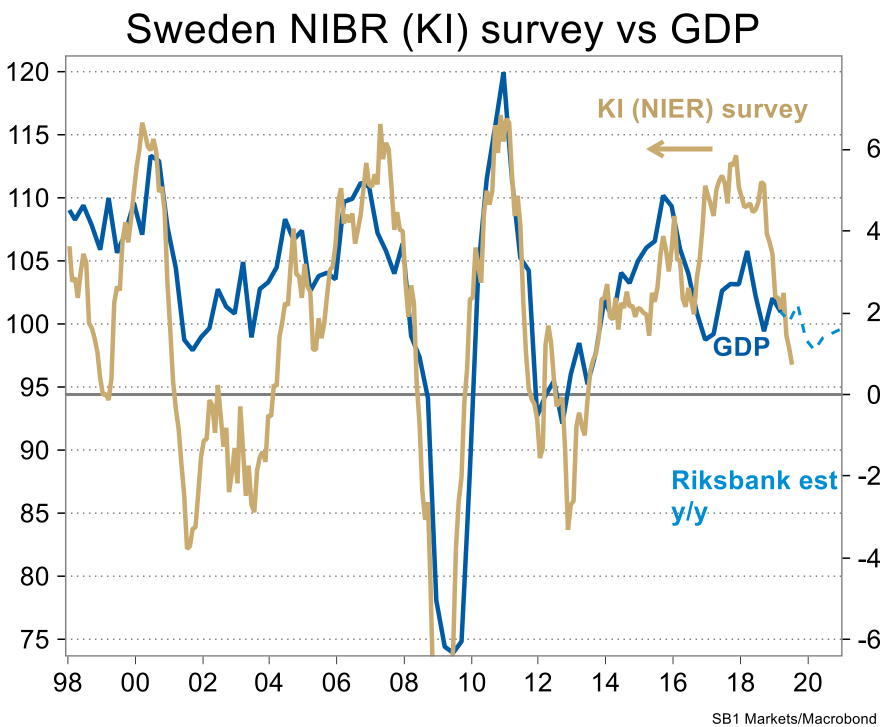


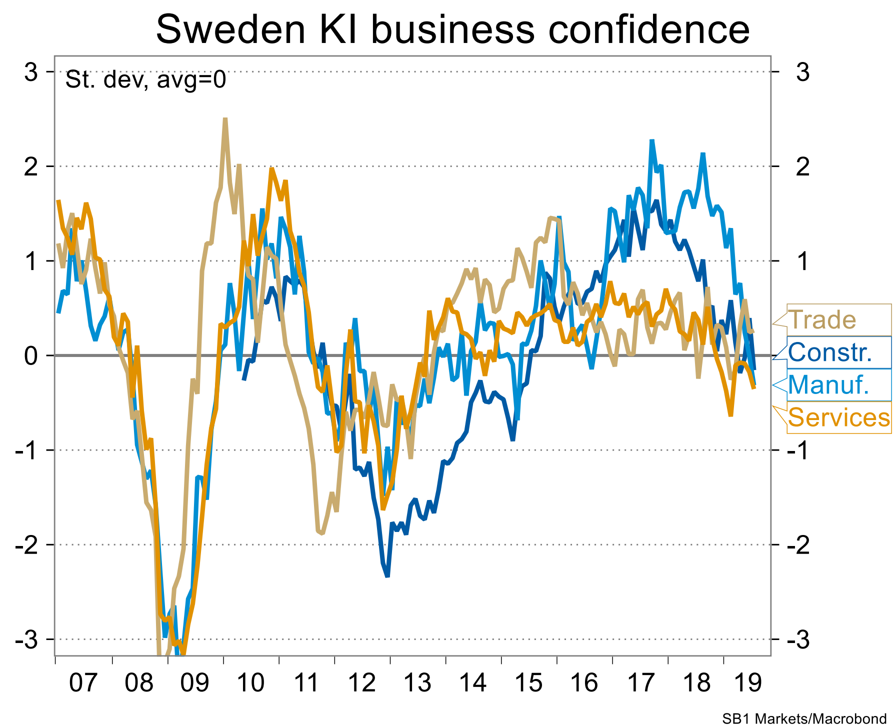


- Employment fell at a 0.6% q/q pace in Q2 following the 0.2% decline in Q1, but is still up 0.8% y/y
- Labour market participation was trending up but has so far in 2019 (almost as much as the employment rate)

The KI business survey another step down in July, to the lowest level since '13

Confidence is falling steeply and broadly. Signals a substantial slowdown in GDP growth



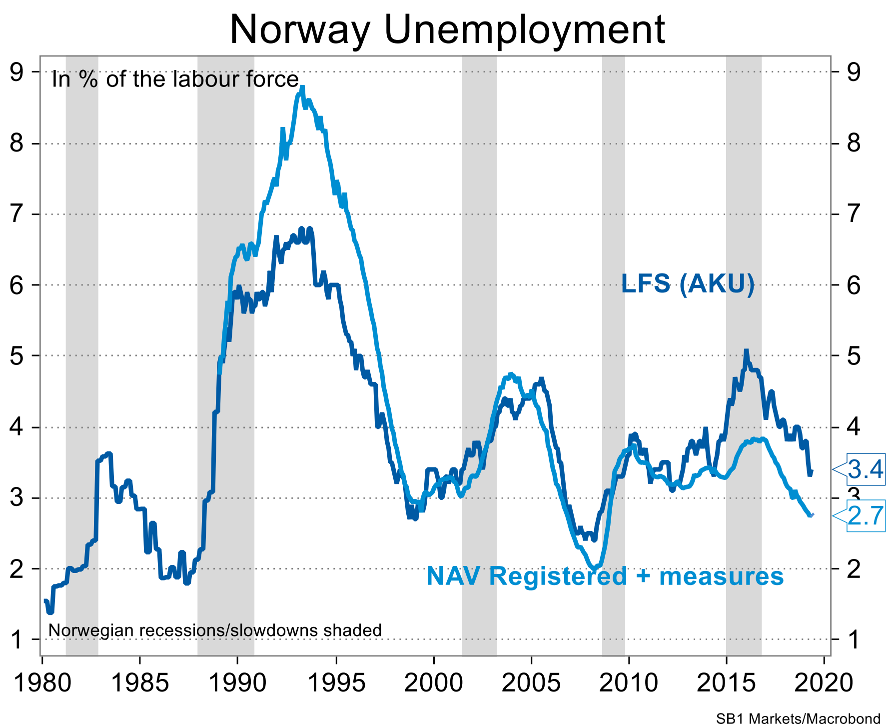


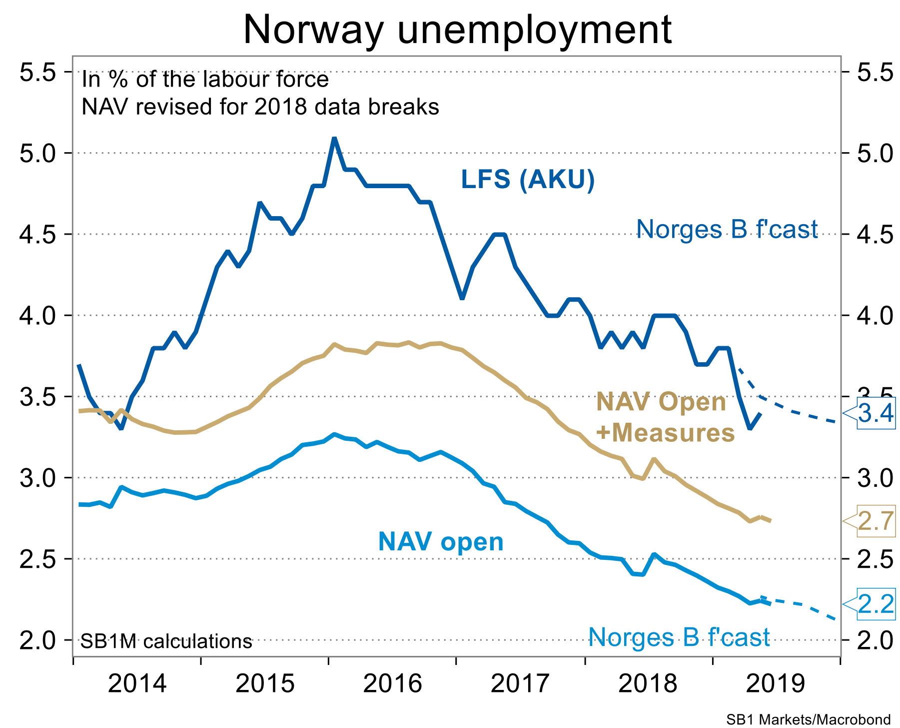
- The KI economic tendency survey, which usually correlates well with GDP growth, were pointing to unusual high growth rates from 2016 and until a couple of months ago. Now, the index has fallen below the 2016 level and is most likely signalling a rapid downswing in GDP growth. All sectors are reporting sagging confidence – but trade not worse than before
  - » From the demand side: Companies are reporting weaker order inflow from both domestic and foreign markets
  - » From the supply side: The best long term reason for expecting growth to slow is that productivity growth has slowed to zero – and it will be close to impossible to keep hours worked growing above 3% for long

- Highlights
- The world around us
- **The Norwegian economy**
- Market charts & comments

LFS unemployment up to 3.4% but still below NoBa est; downward trend intact

April revised 0.1 pp up to 3.3%, and May at 3.4%, exp. 3.3% - down from 3.8% in Q1



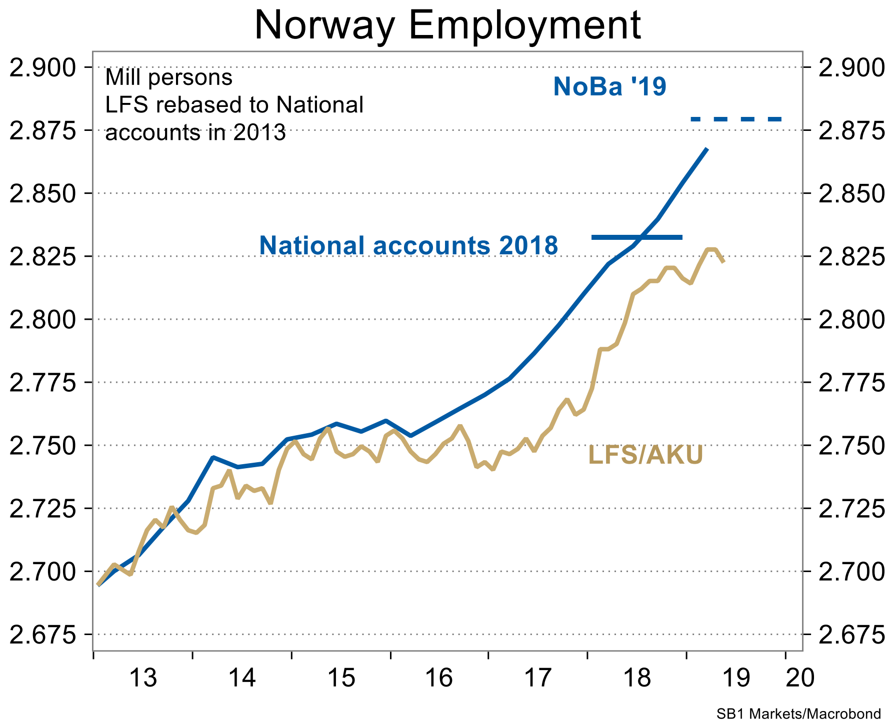


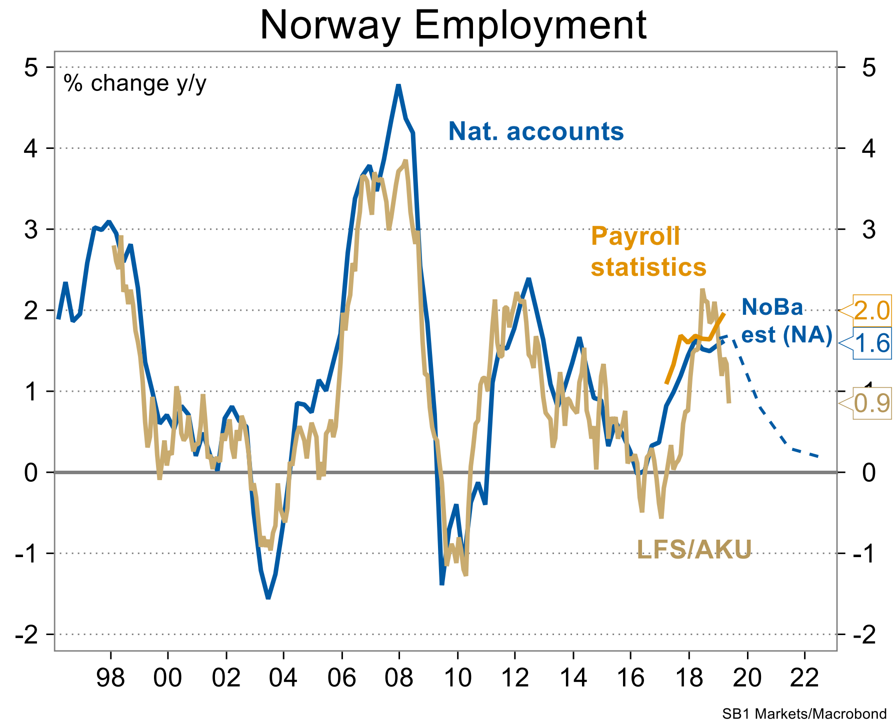
- LFS (AKU) unemployment rose 0.1 pp to 3.4% in May (avg Apr – Jun) from an 0.1 pp upward revised 3.3% in April. Norges Bank assumed a 3.5% unemployment rate in Q2 in the June MPR. Even if the unemployment rate was 0.1 pp above market consensus, the trend is still straight down
  - Employment fell by 5' m/m in May (3 m avg), and the annual growth rate has fallen to 0.9% from 2.1% in November last year – well below NoBa's f'cast. Labour market participation fell by 8' persons, thus, the entire upswing in the participation rate the past year is reversed! Indicates that supply is 'emptied' and the labour market is becoming tighter, an argument for an aggressive Norges Bank
- The LFS data confirms the steady decline which NAV has been reporting – and the latter is much less volatile

SpareBank 1 MARKETS

LFS Employment growth is softening – from above 2% to below 1?

Q2 LFS empl. is up 0.9%% y/y, 0.7 pp below the Q1 Nat. Acc., and 0.7 pp below NoBa's f'cast

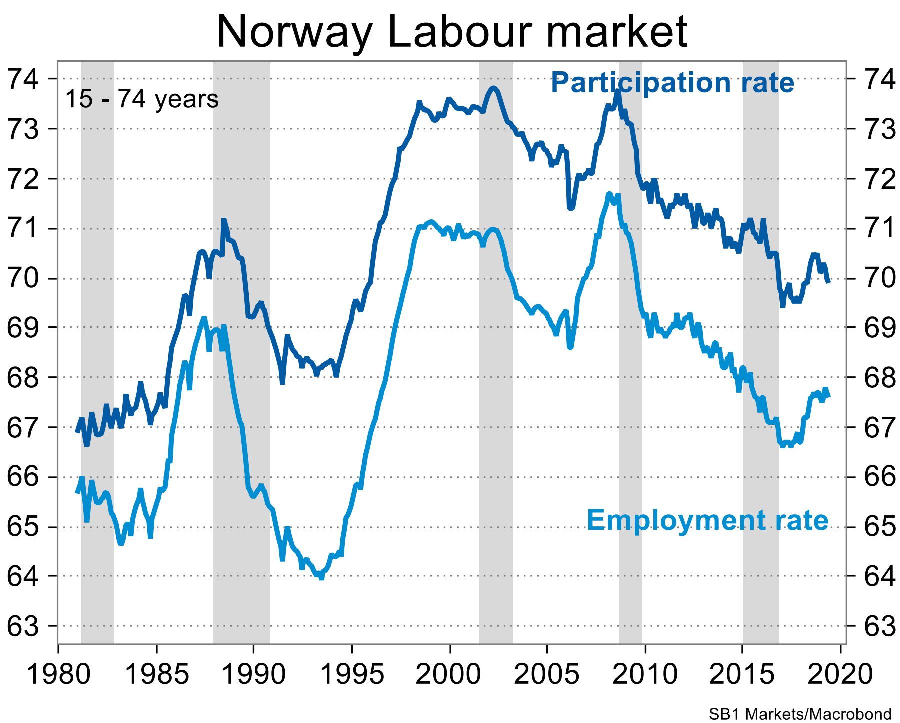


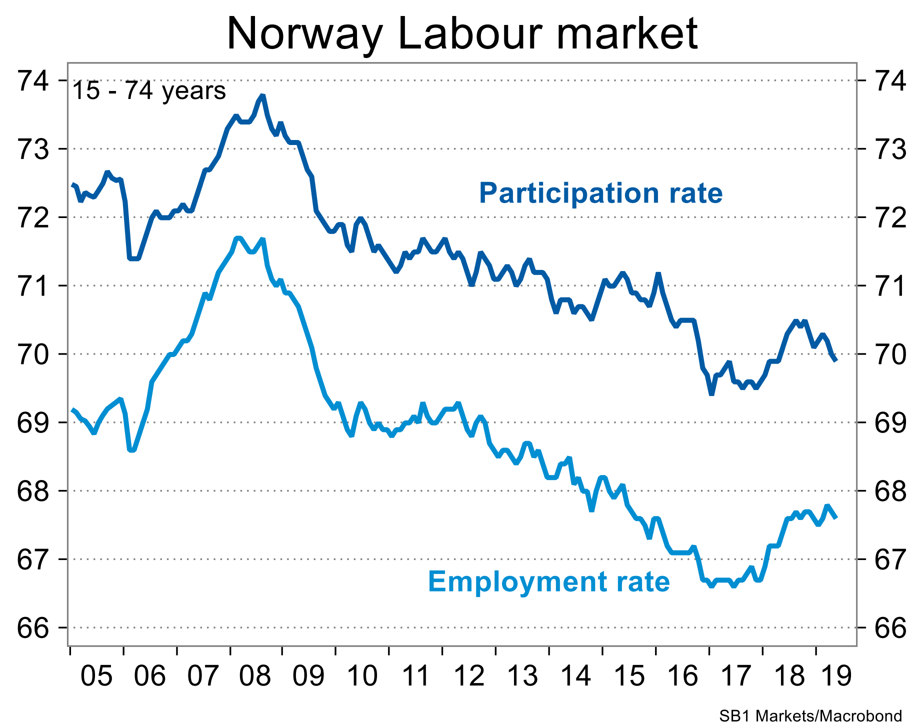


- Employment measured by the LFS accelerated through 2017 and the first half of 2018, to above 2%, has eased somewhat over the past year, and to 0.9% in May (= Q2). However, other data do not yet report such a slowdown. On the other hand, this is the first data point covering Q2 – and both Norges Bank and we expect a substantial slowdown in employment growth mainly due to lack of labour (which manufacturing companies are now reporting)
  - » National accounts' employment figures (and the new quarterly register employee statistics) are no doubt more accurate than the LFS survey data. Nat. Acc. reported a more rapid increase in employment than LFS through 2017, and is noting stable employment growth the past year, to 1.6% in Q1. The LFS figures were probably too high last summer, exaggerating the decline in the annual growth rate due to the base impact
- In the June MPR, Norges Bank nudged up its 2019 employment f'cast by 0.3 pp, to 1.7%
- The working age population growth has slowed to 0.6% y/y, from 1.75% at the peak in 2012. A 1.5% (or 0.9%) employment growth is above trend

Labour market participation is retreating again! Limited growth potential?

The employment rate has almost flattened, participation is clearly declining



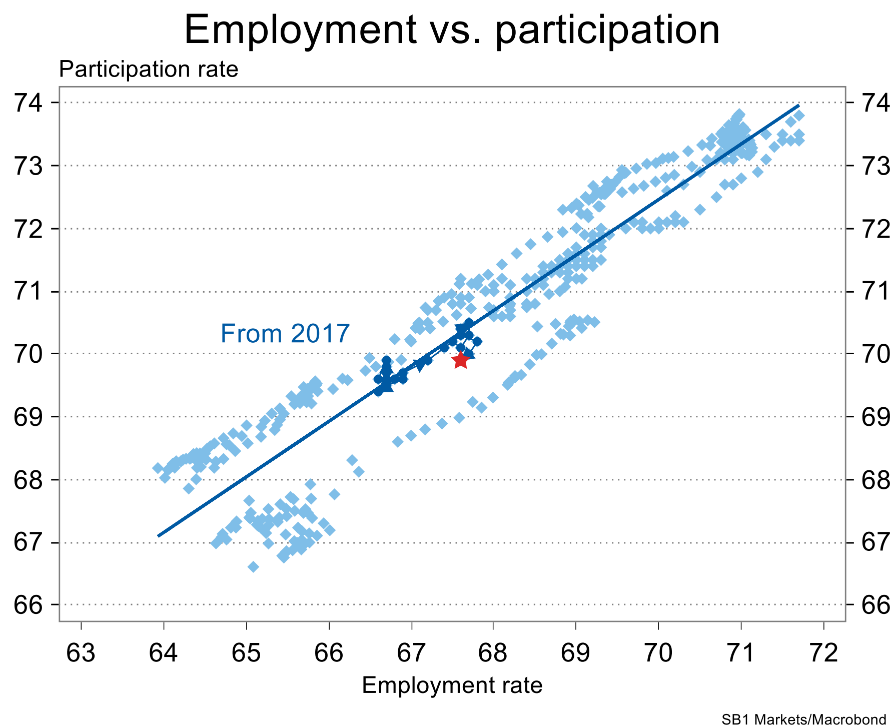


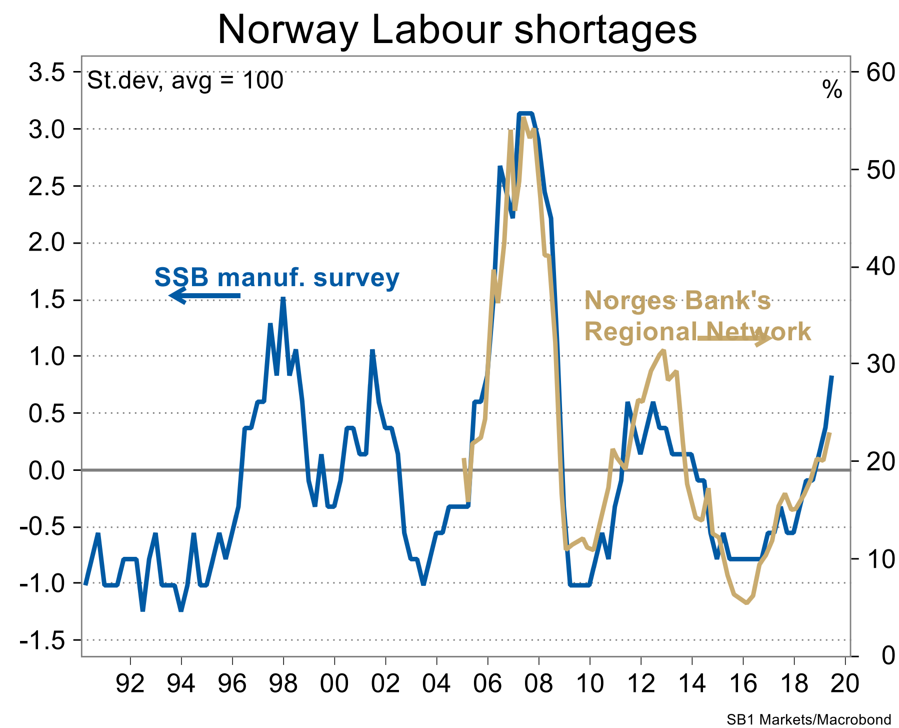
- The long term downturn in the participation rate and employment bottomed one 1½ y ago and both were growing strongly through 2018, up some 1 p.
- However, participation has pulled back for 7 months and fell steeply in April and May, in total by 0.6 pp from the last Oct. peak. The employment rate is down 0.1 pp in the same period – signalling a limited supply; participation is contracting without obvious weakening of demand – and more companies are reporting lack of labour
  - » Wage inflation is picking up, reflecting a strengthening labour market, and more is expected, according to NoBa's expectations survey

SpareBank 1 MARKETS

Participation is sagging vs. employment – signals supply constraints

Participation has fallen 'below the line'

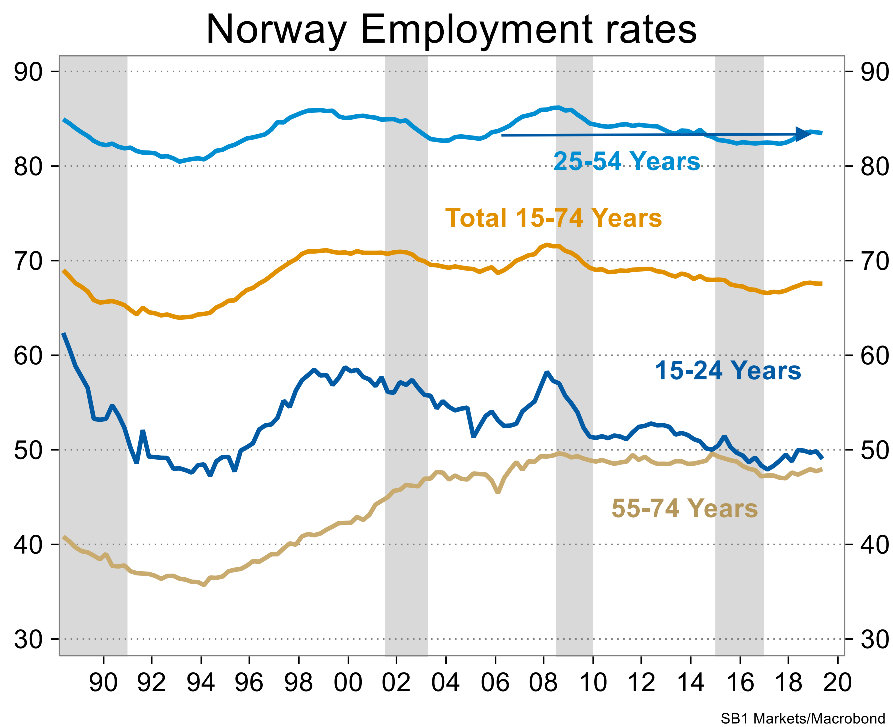


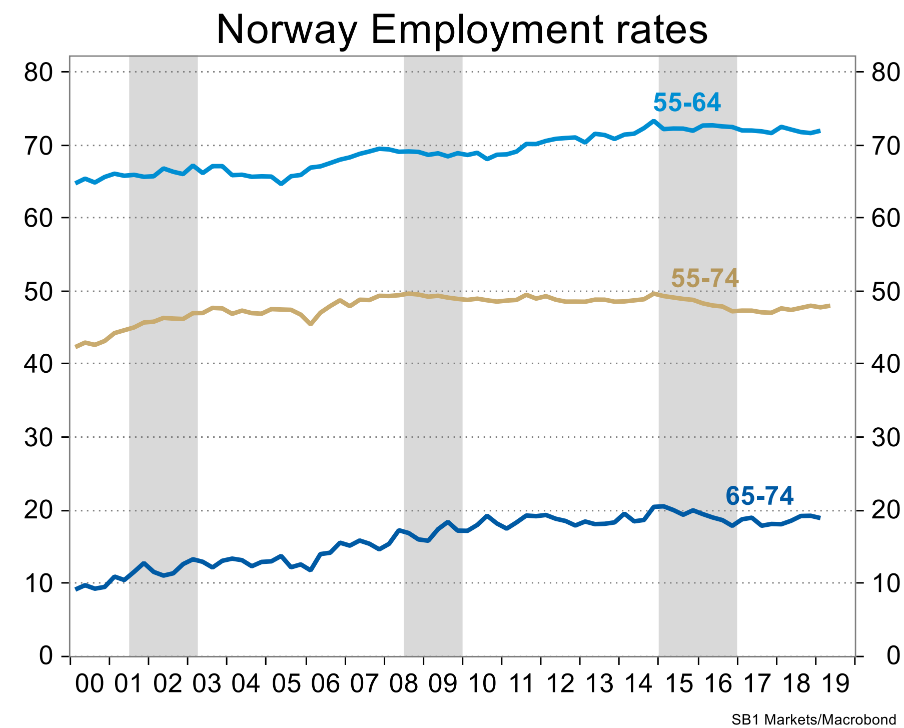


- The Norwegian unemployment rate is quite stable compared to changes in the employment rate – because the participation rate usually is quite responsive to the chances of getting a job; the employment rate. Flexible labour immigration from the EU has also contributed to keep the Norwegian unemployment rate stable
  - » In average since 1980, the labour force participation changes almost 0.9 x the change in the employment rate. Recent years, the response has been somewhat less, say 0.75. However, so far in 2019, the participation rate has declined even if the employment has not fallen, we are moving 'southwards'! Thus, the unemployment rate has become too low vs. the employment level
- Businesses are reporting increasing labour shortages, and the SSB manufacturing Q2 survey well above an average level, more than in 2011 - 12

Employment rates are turning up in all age groups?

Even the oldies may be increasing

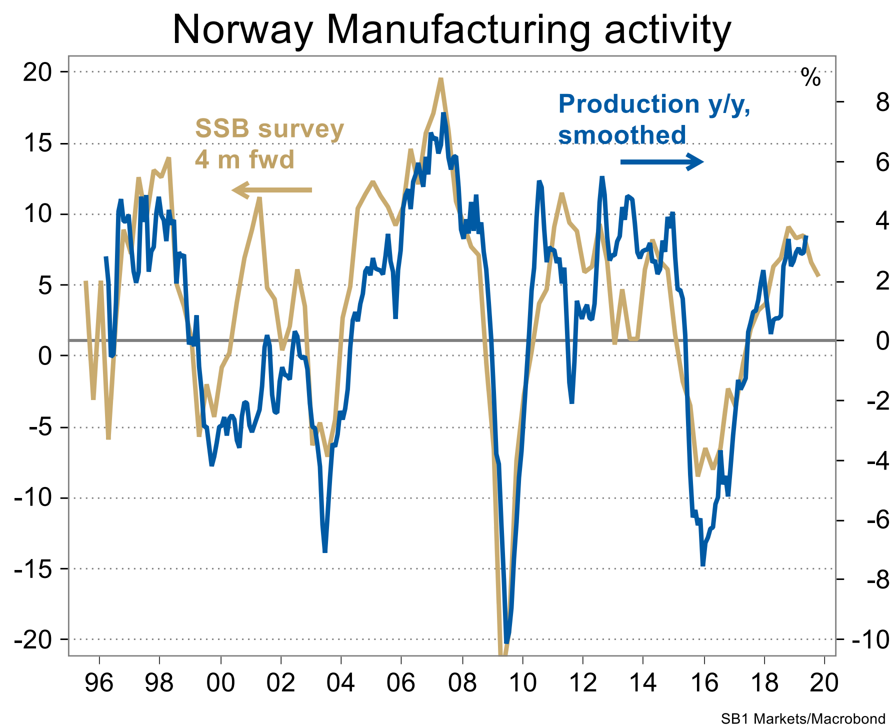


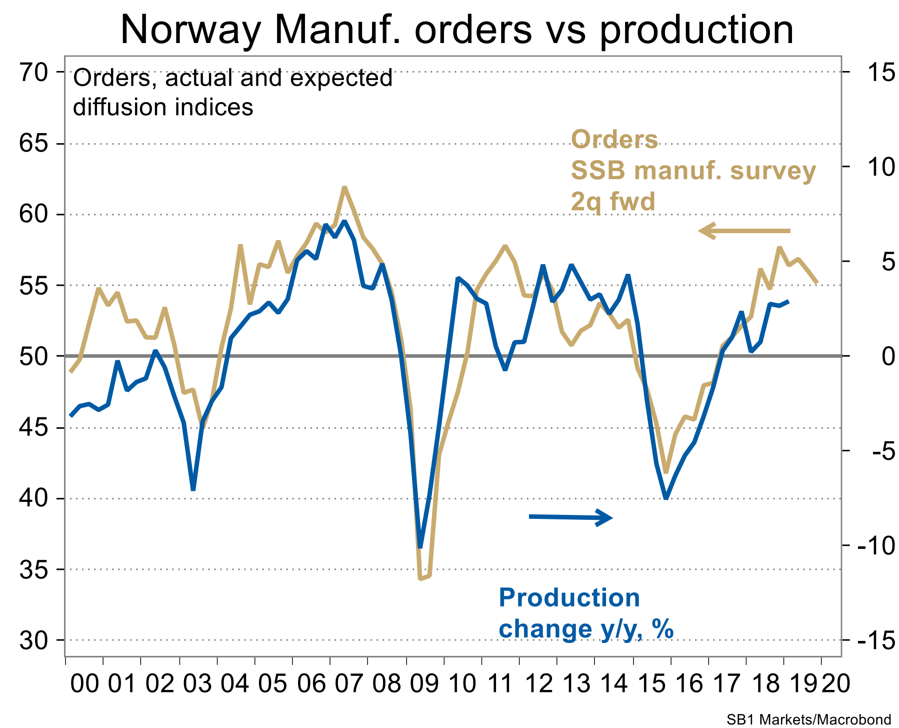


- Employment in the core 25 – 54y group is below the 2008 peak, and has been trending somewhat down since 1998. Still, the level might be close to a mid cycle level, like in 2005/06
- The employment rate in the 15 – 24 age group slowed has fallen marginal. This group trending down long term, due to a higher share in education. We do not think the upside is large
- Employment in the 55y + group has turned slowly up recent quarters and rose in Q3! Over the past three years, the employment rate has fallen marginally, as for the two subgroups; under and above 64 y. Since the core age group has increased its employment share, a cyclical explanation is not reasonable. Bad news

SSB's manufacturing confidence a tad down, still points to growth above trend

Slightly softer order inflows, both in oil/non-oil related sectors. Employment plans steeply up

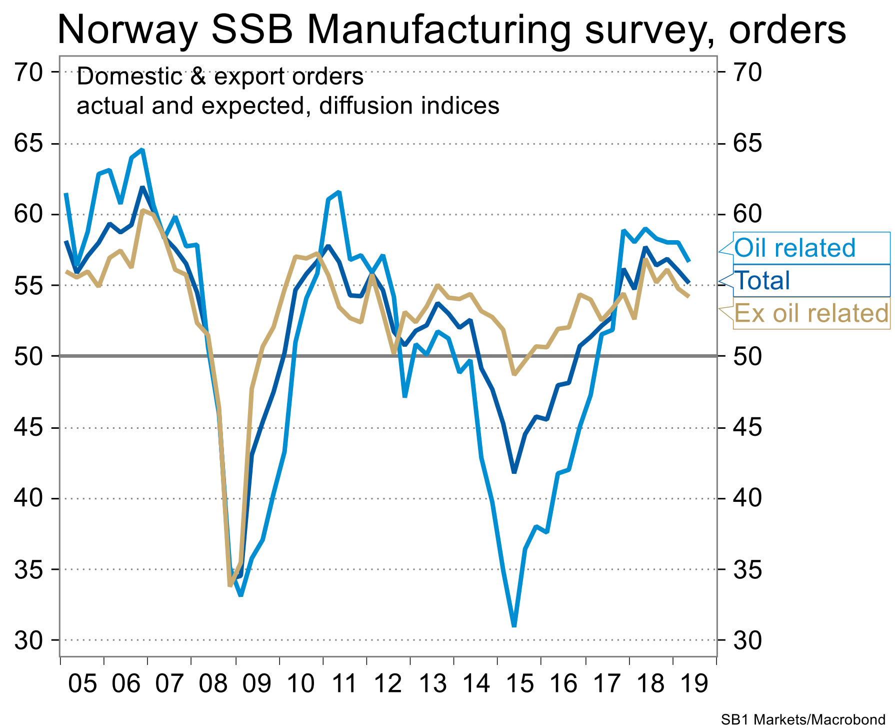


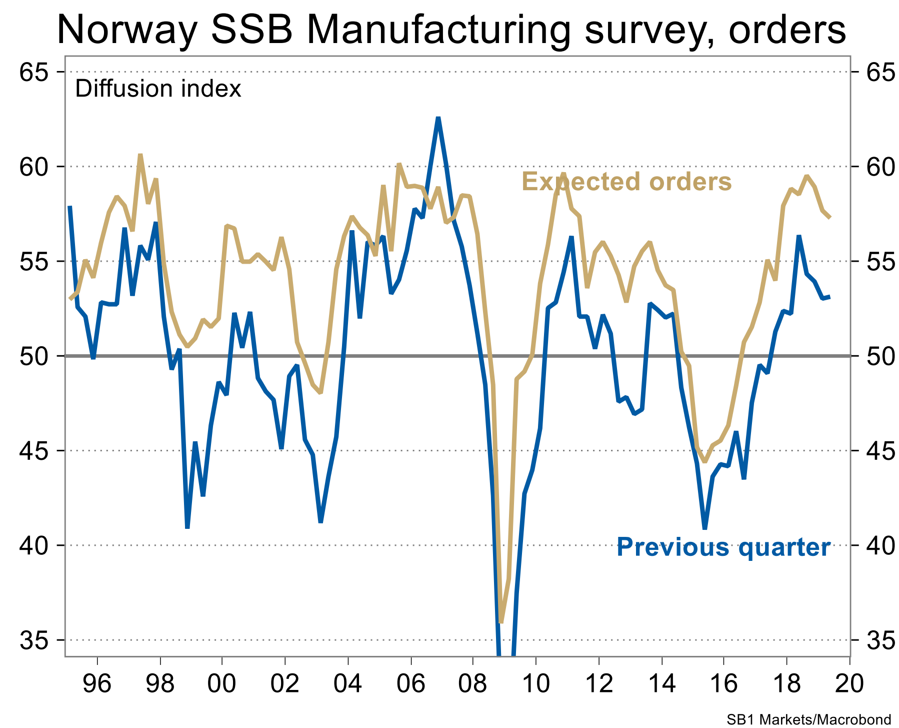


- The composite index in SSB's industrial survey (manuf. index) inched down to 5.6 in Q2, from 6.6, we expected down to 3
  - » The index is well into positive territory (above 0 indicates growth in output) and well above the average at 3.9. Thus, the survey signals growth in manufacturing production above the long term trend rate at 2¼ % and a GDP growth at2 ½ %
- Manufacturing businesses are noting marginally weaker orders (composite index), however, the level is still high
  - » Orders in oil related sectors have held up at a solid level since late 2017, non-oil sectors are somewhat softer

Manufacturing order growth slows marginally, remain quite robust

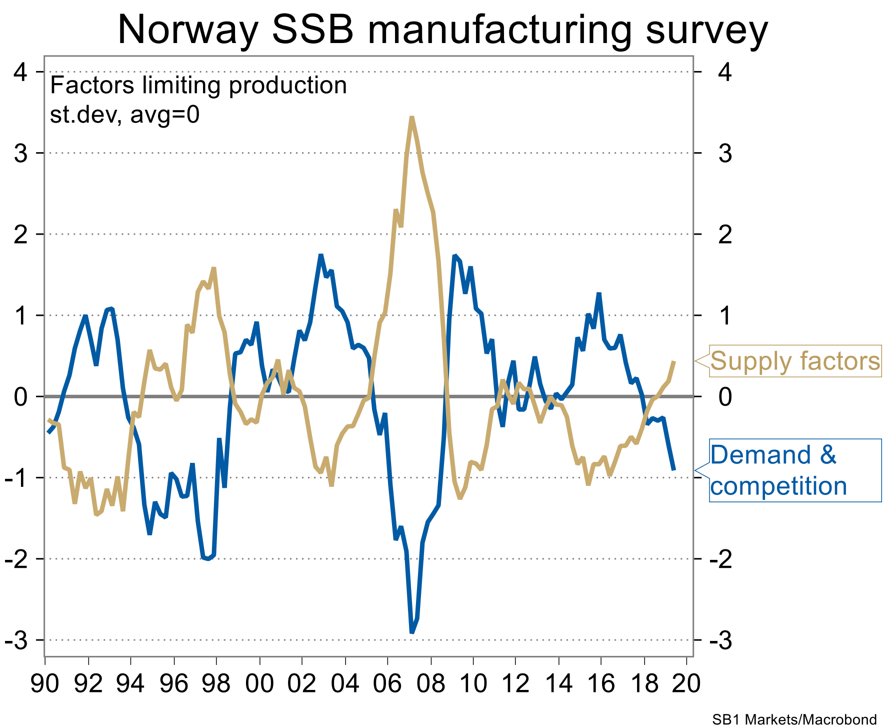
Both reported and expected orders have slowed somewhat recent quarters, from high levels

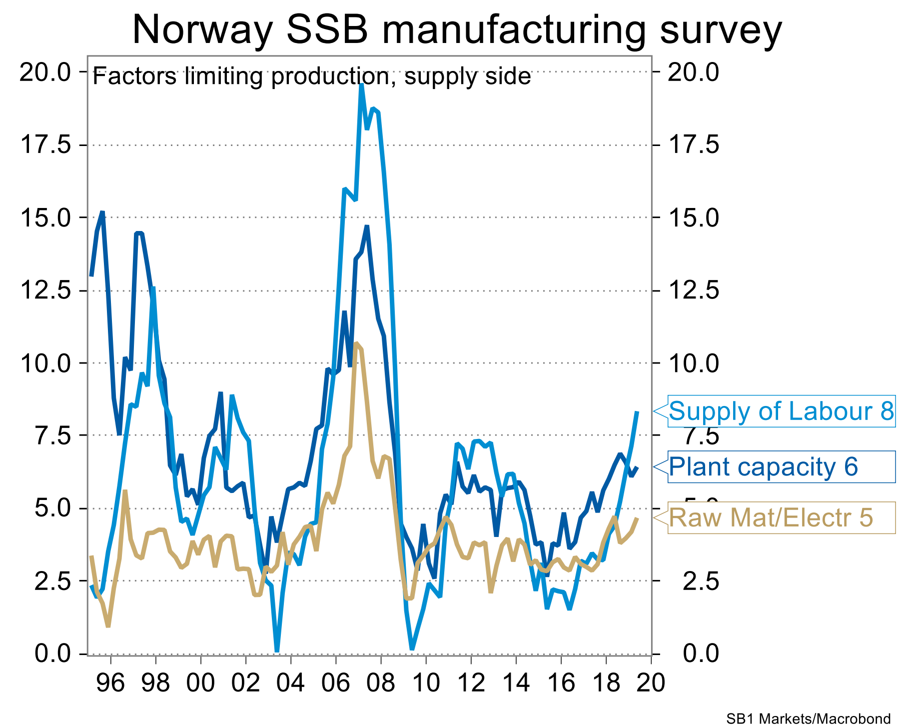




Still: Lack of demand less of a problem, more (but not yet serious) lack of labour

The share of businesses reporting labour shortages sharply up, now above the 2011-12 peak



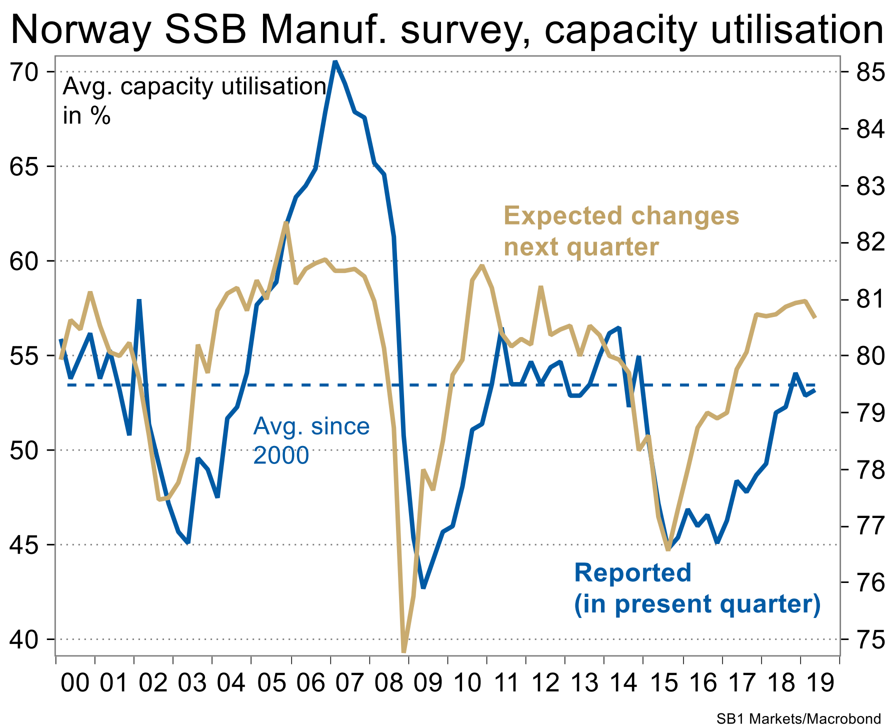


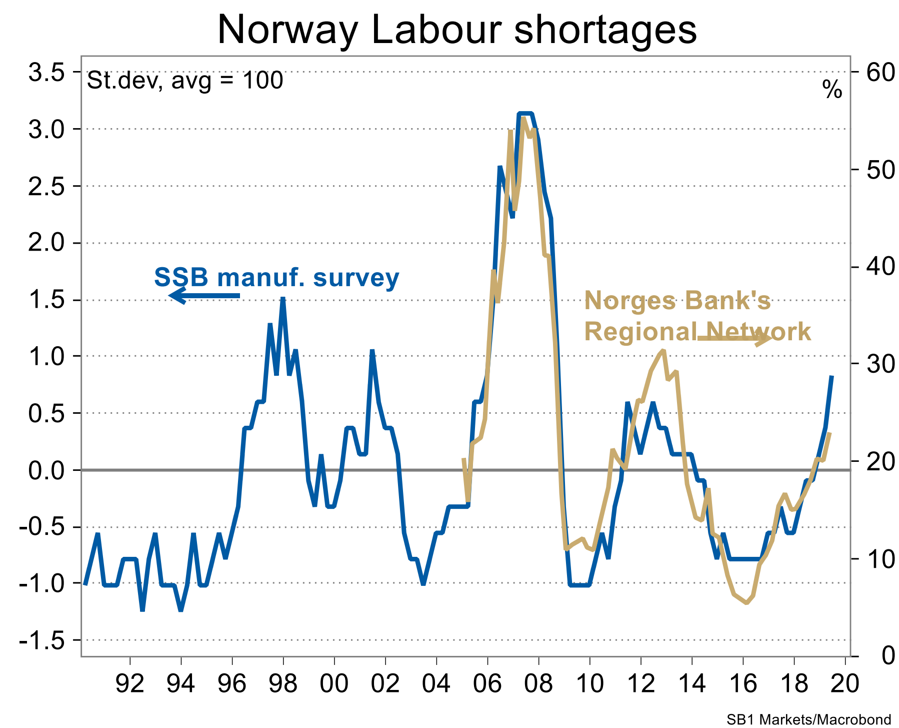
- Fewer companies than normal are reporting lack of demand/too much competition as a constraint; the share has fallen sharply the tow last quarters – and is well above he level in 2011 - 12
- Raw materials are not short in supply (marginally up, and above an average level). Plant capacity constraints are reported at an average level

SpareBank 1 MARKETS

Reported capacity utilisation marginally up in Q2, expected further up

Businesses expect a steep rise in capacity utilisation, which they have since 2015

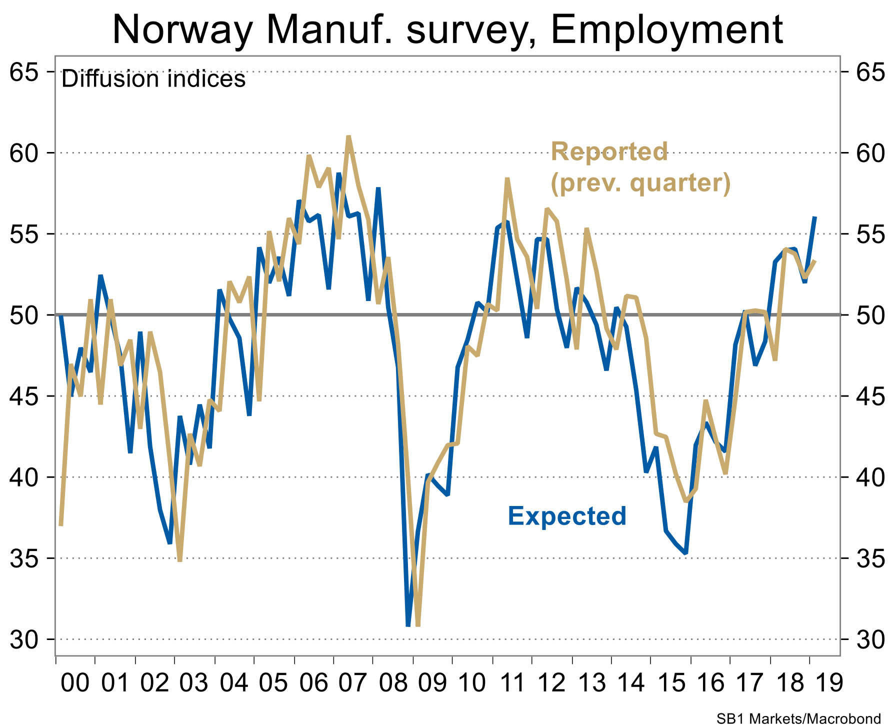


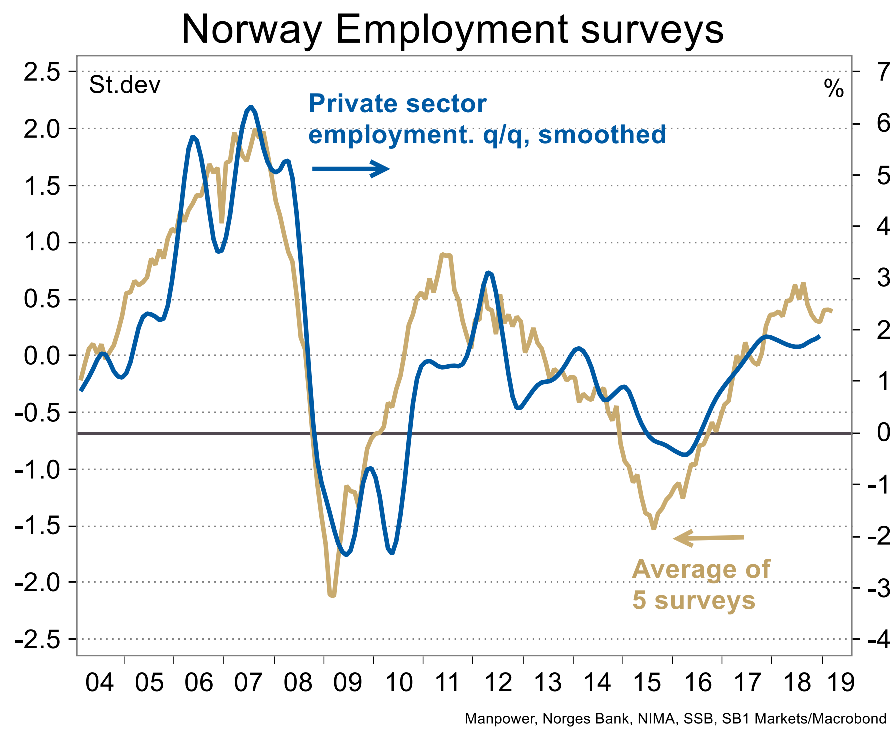


- Both the SSB survey and Norges Banks' Regional Network are reporting increasing labour shortages, and both idices are above their respective averages. However, SSB (manufacturing) is now reporting a tighter labour market than the Regional Network (the whole economy)

Businesses are expecting soaring employment

Avg of employment surveys points to above 2% employment growth, somewhat too optimistic?

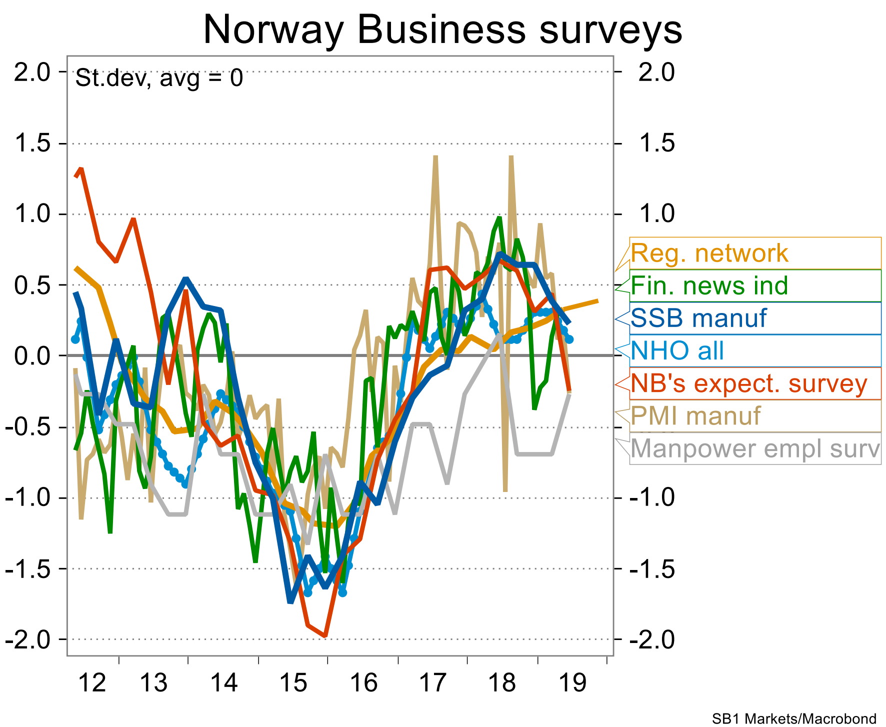


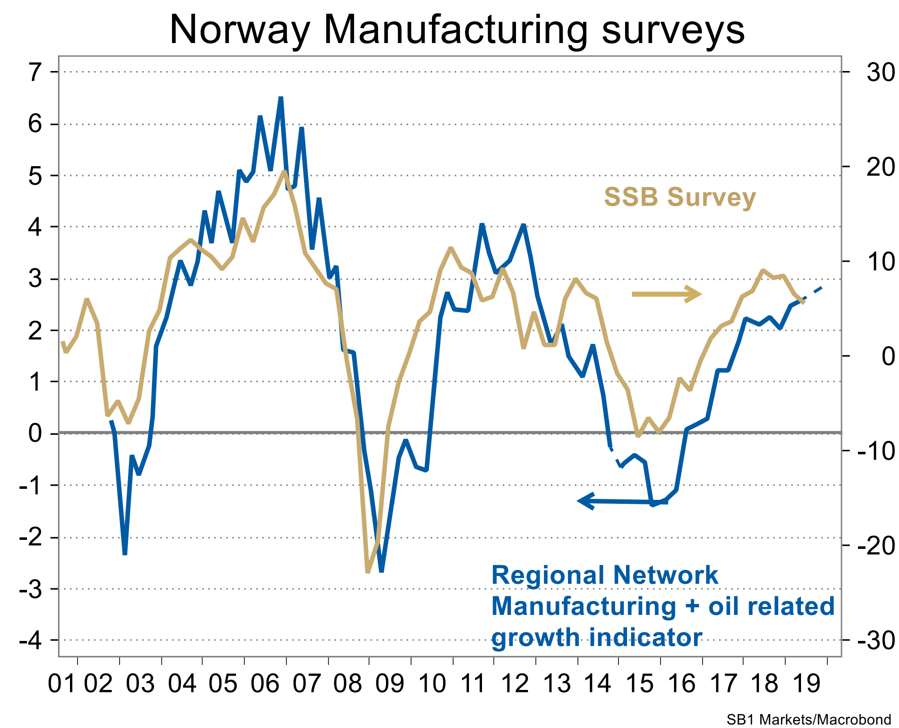


- Manufacturing businesses reported a slight increase in employment growth but they expect an accelerating, index at 11 y high!!

Most business surveys are heading downwards, except NoBa's Regional Netw.

The majority (4 out of 6) are above average, reporting growth above trend

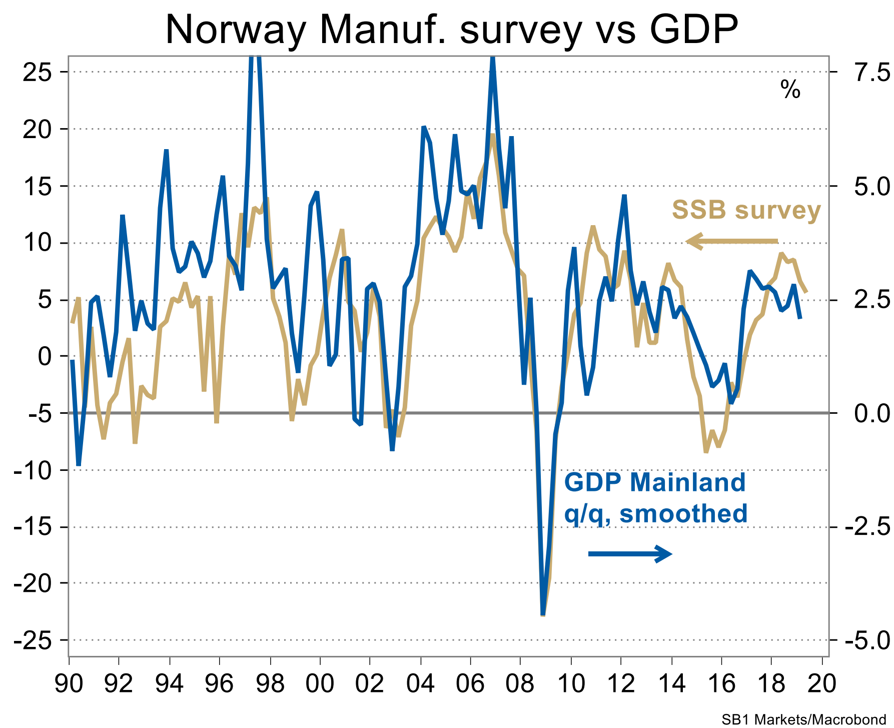


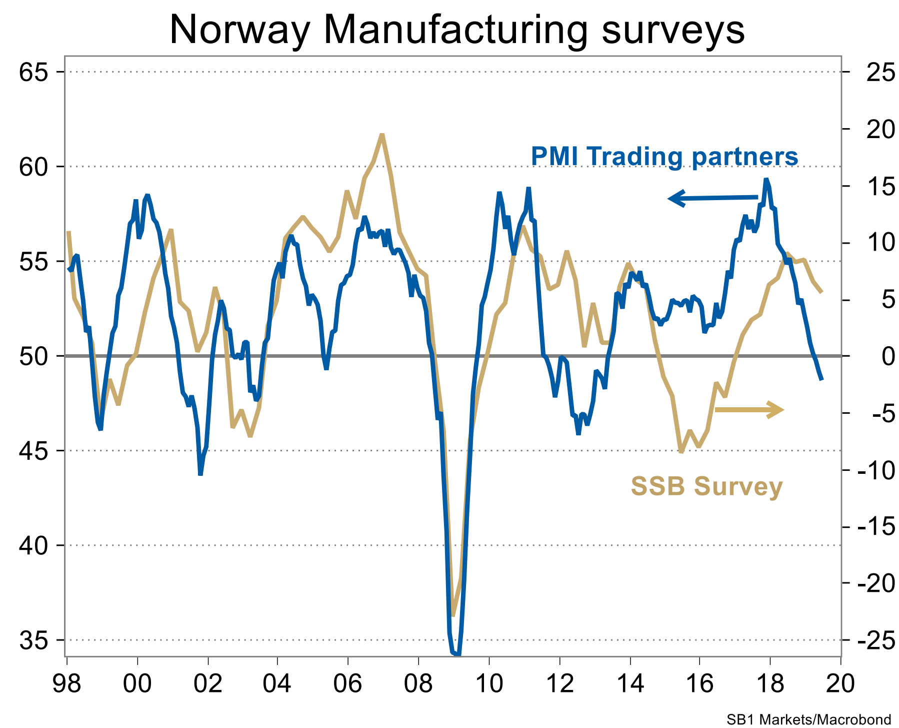


- The Network is the only survey signalling stronger growth – and it's the survey that is indicating the highest growth rate

2.5% Mainland GDP growth confirmed. And Norway is still ahead of the pack…

But the SSB survey is heading south too

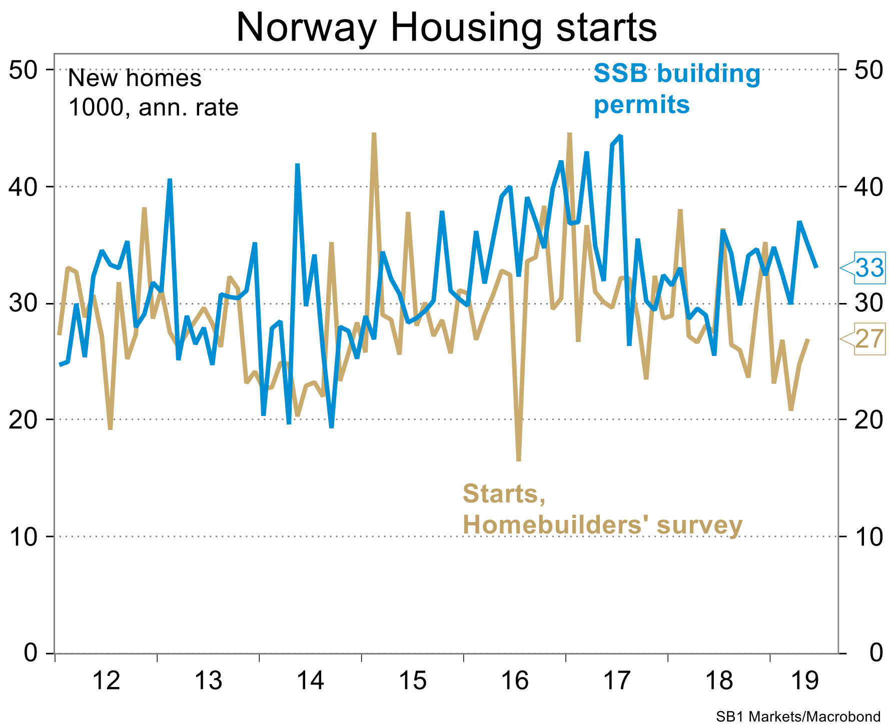


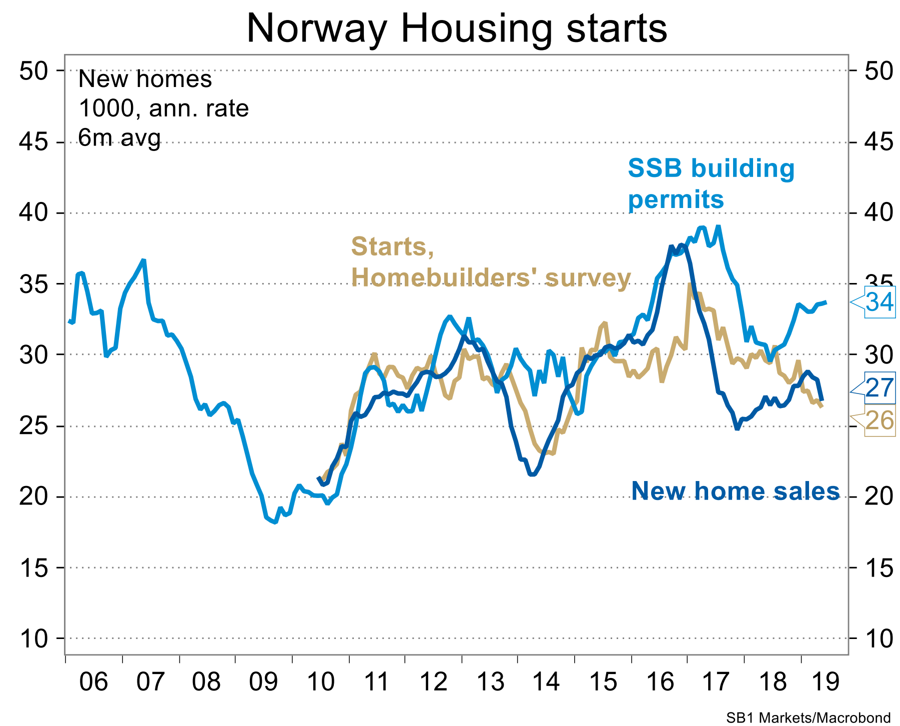


- The SSB survey signals a 2½ % Mainland GDP growth

Housing 'starts' up or down?

Building permits ticked down to 33' in June, trend still marginally up. Homebuilders are not so sure

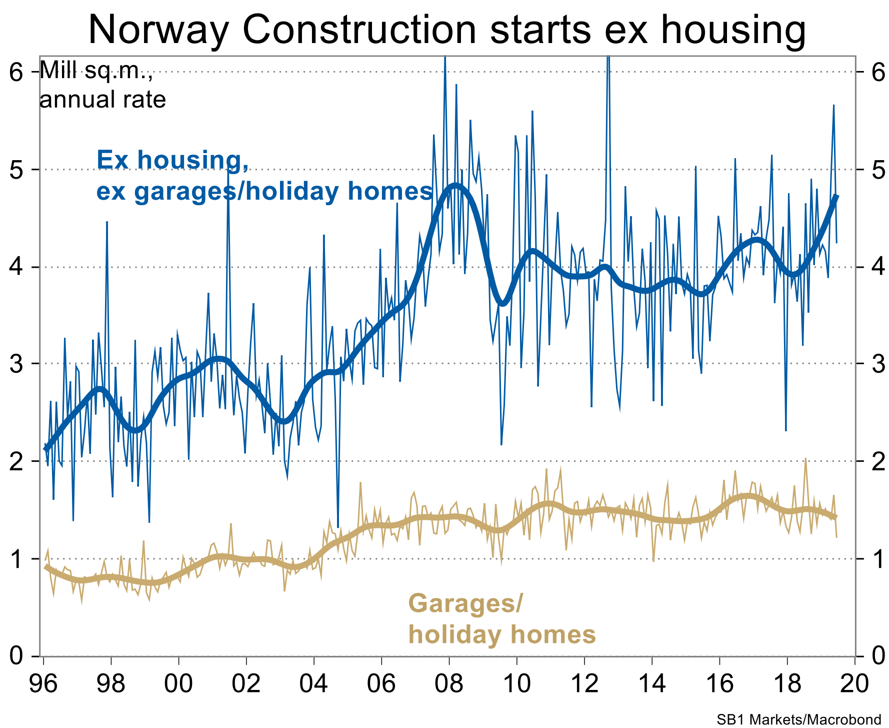


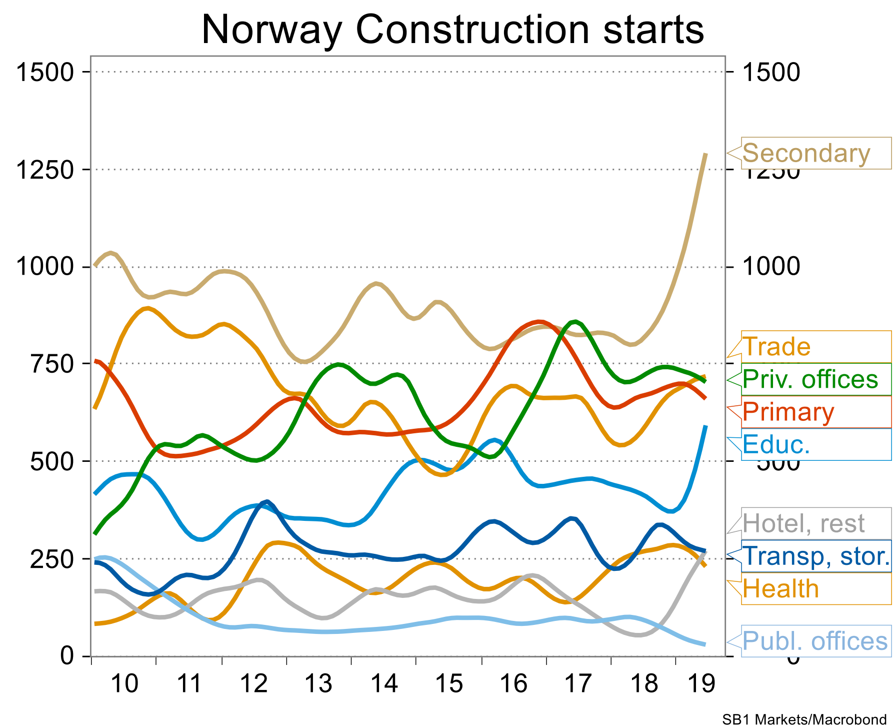


- SSB reported housing starts (building permits) at 33' annually in June, down from 35' in May. Starts may be trending slowly up
  - Mixed signals; the Homebuilders' are still reporting declining housing starts (and weaker sales). The Homebuilders are usually reporting a lower level of starts than SSB, not all projects are included. New home sales have slowed somewhat and is not signalling a further rise in starts
- The level of housing starts is not low, although we are still well below the 2016-2017 peak. Housing starts are above the average since 2000, and approx. at the per capita average (with low population growth and real income growth much below what we have been used too). Moreover, the level is still high vs most other countries, check this page

Construction ex. housing is surging, back at 2008 peak level

May upswing is probably partly transitory, as electricity supply construction spiked. Trend up anyway

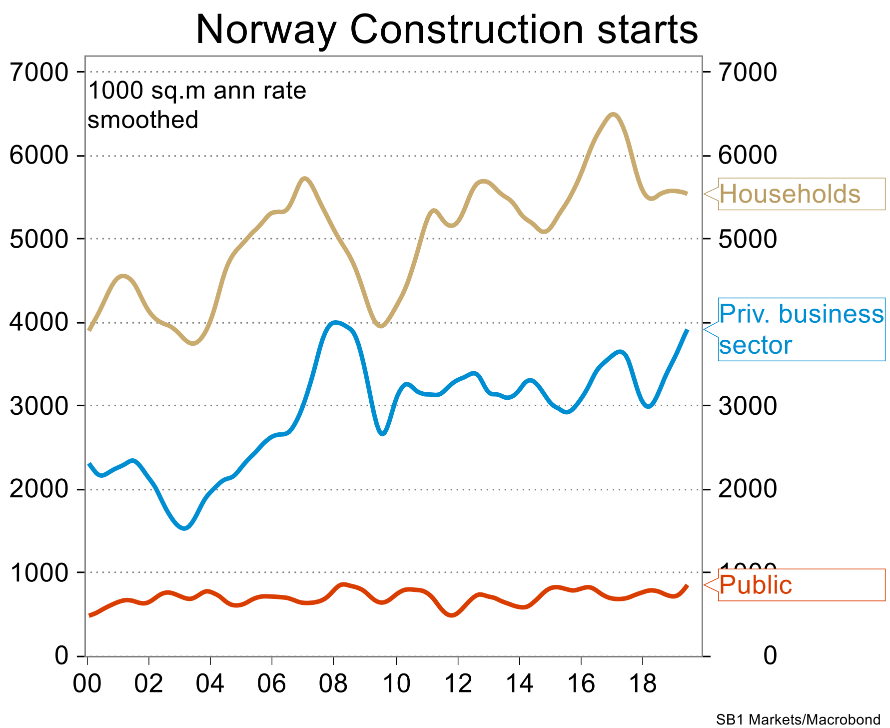


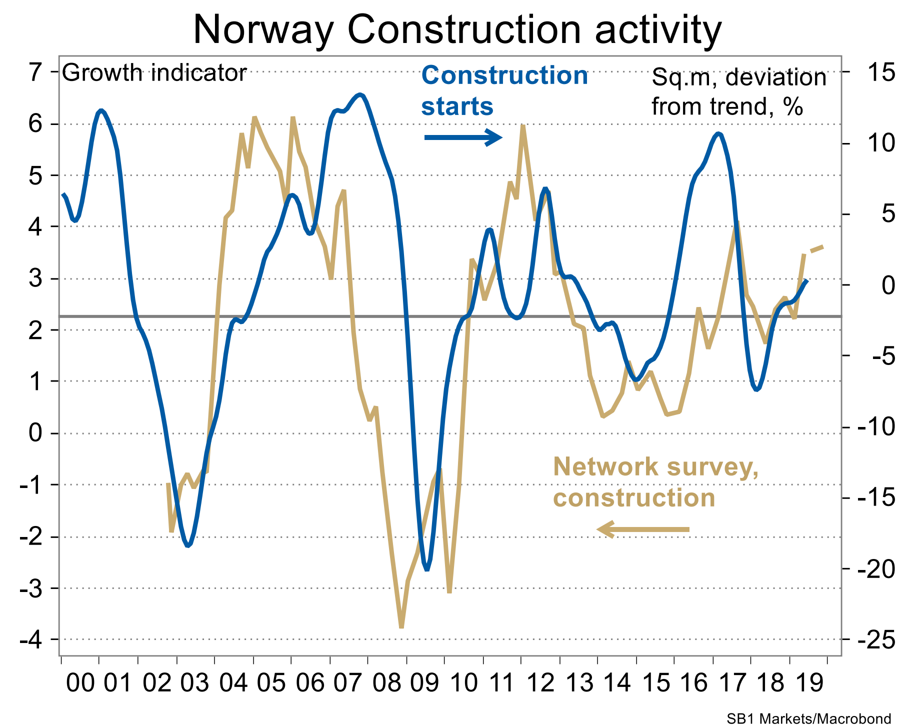


- Construction ex housing, garages/cabins is increasing rapidly, even if the May spike was partly reversed in June
  - » The upswing is driven by secondary (industry) sectors. Electricity supply construction soared in May and will most likely be reversed the coming months. Nonetheless, manufacturing construction is soaring too, industrial sector construction is no doubt trending up
  - » Hotels/restaurants, health and trade, primary and health sectors are increasing too. The upswing in trade is surprising, given the weakness in retail sales (particularly physical sales). Construction within the education sector is falling, along with transport
  - » Public sector offices starts are heading slowly down, private offices stable
- Construction starts of cabins/garages are holding steady, after a mild downturn in 2017

Regional Network expects construction growth slightly above trend

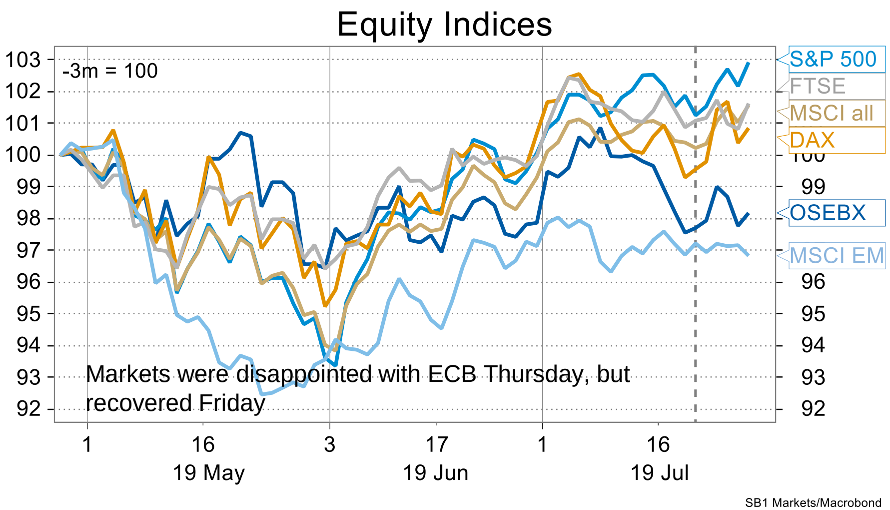
Total construction lifted by business construction, which is rising much more than housing

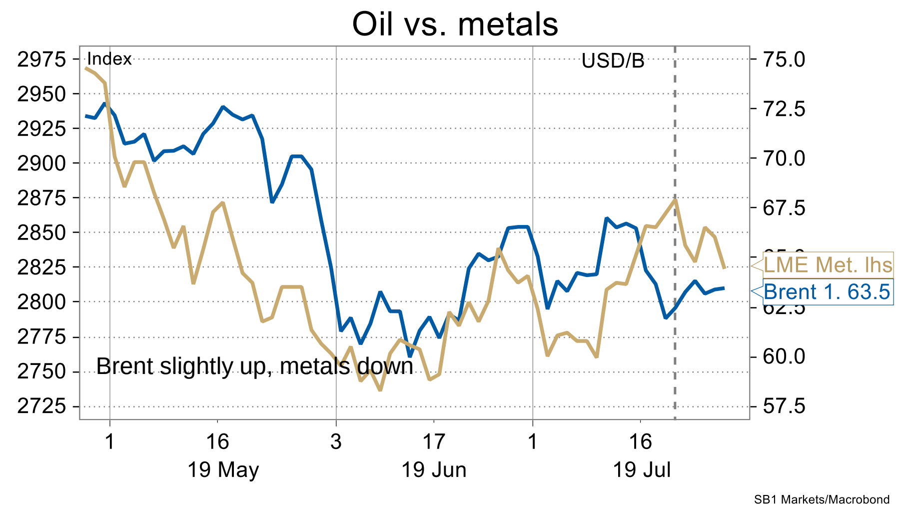


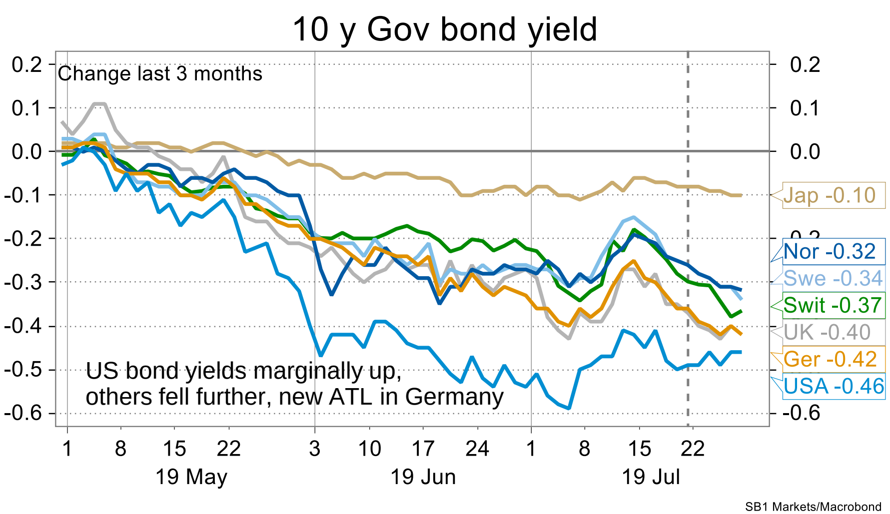


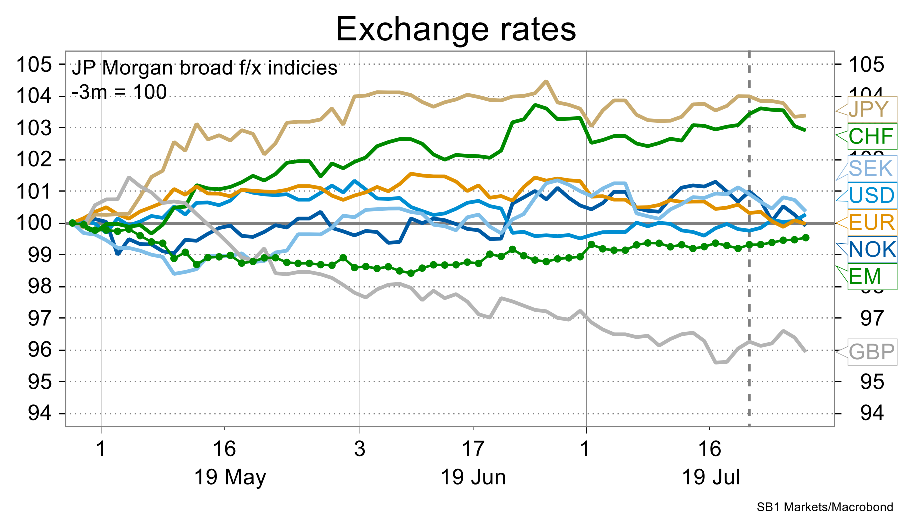
Public on the chart to the left: Construction starts in public administration, education and health

Stock markets up, S&P 500 ATH at Friday, US bond yields up, others down

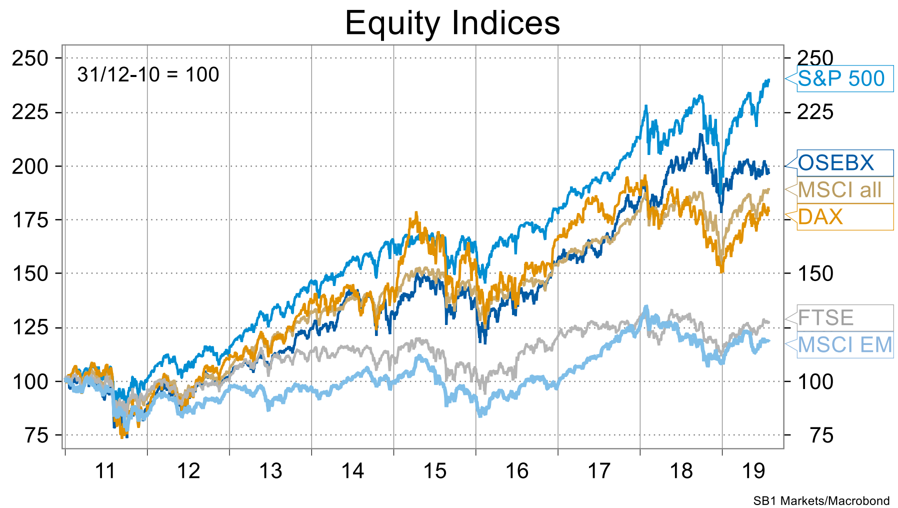


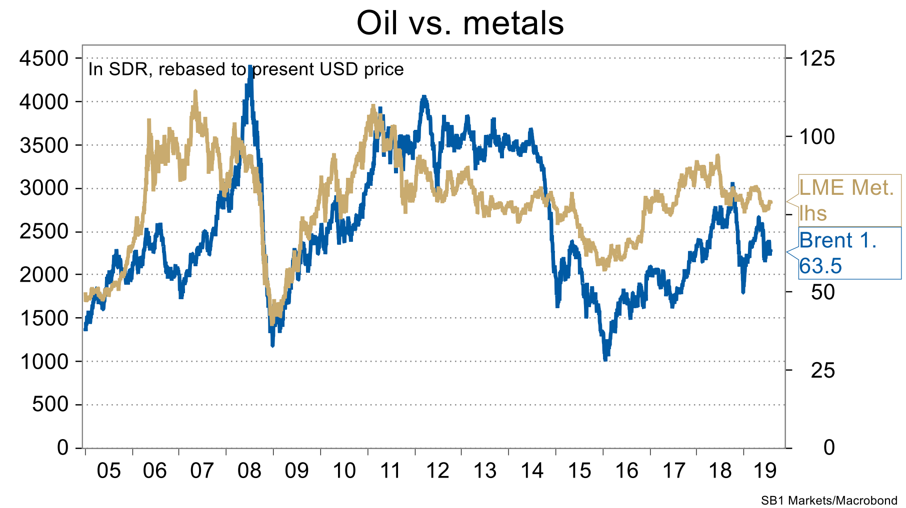


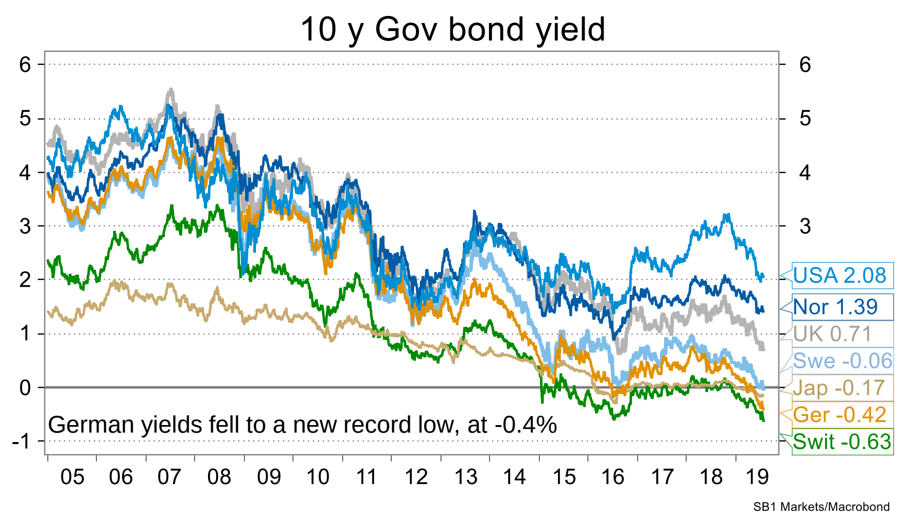


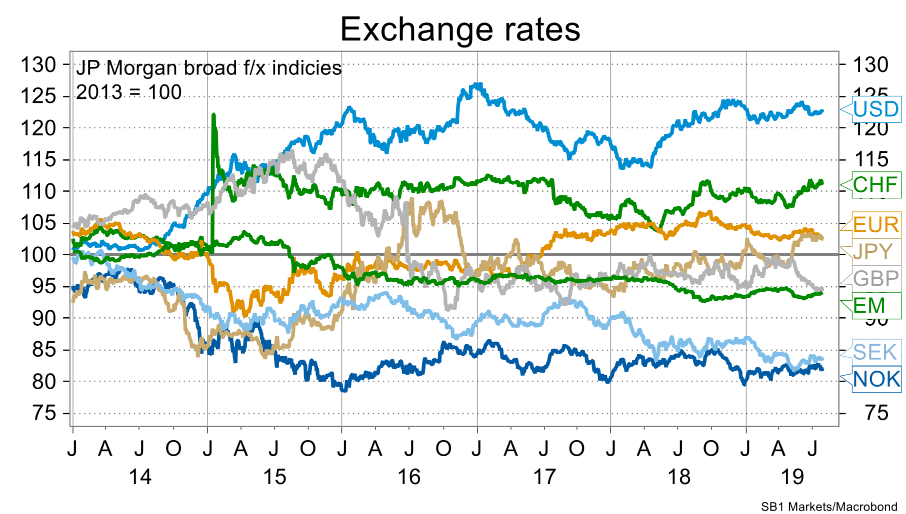


German bunds at new ATL, stock markets are mostly trending up



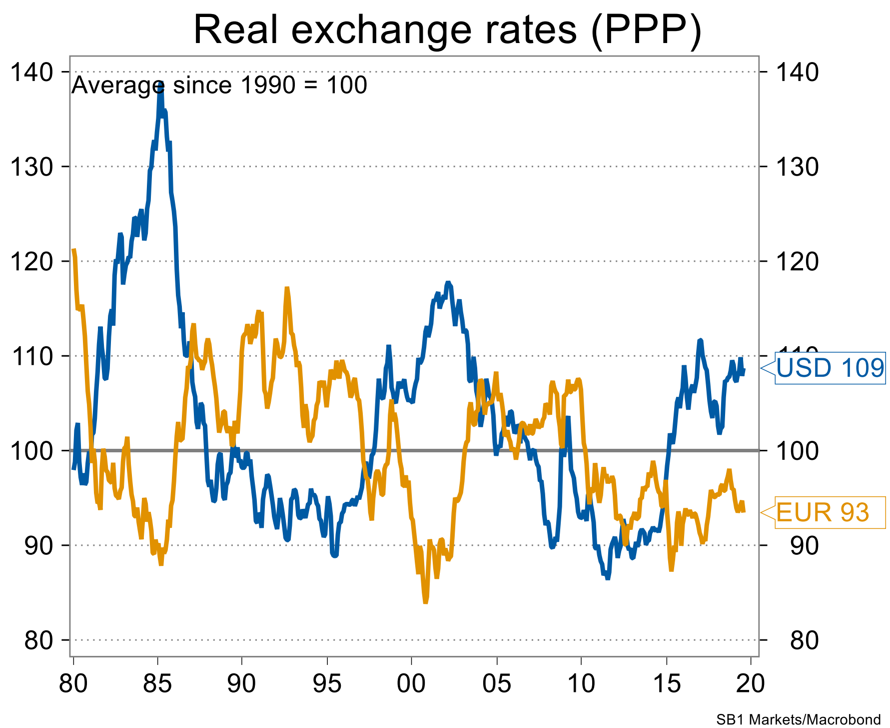


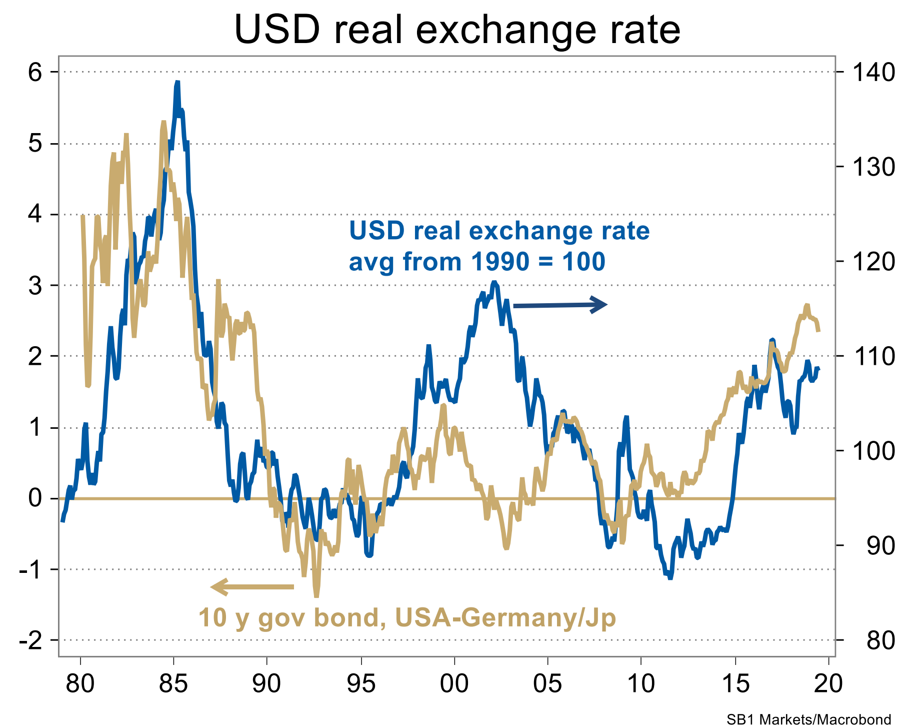




Currency wars next? The USD is somewhat above average, for a reason

However, the USD is far from record strong



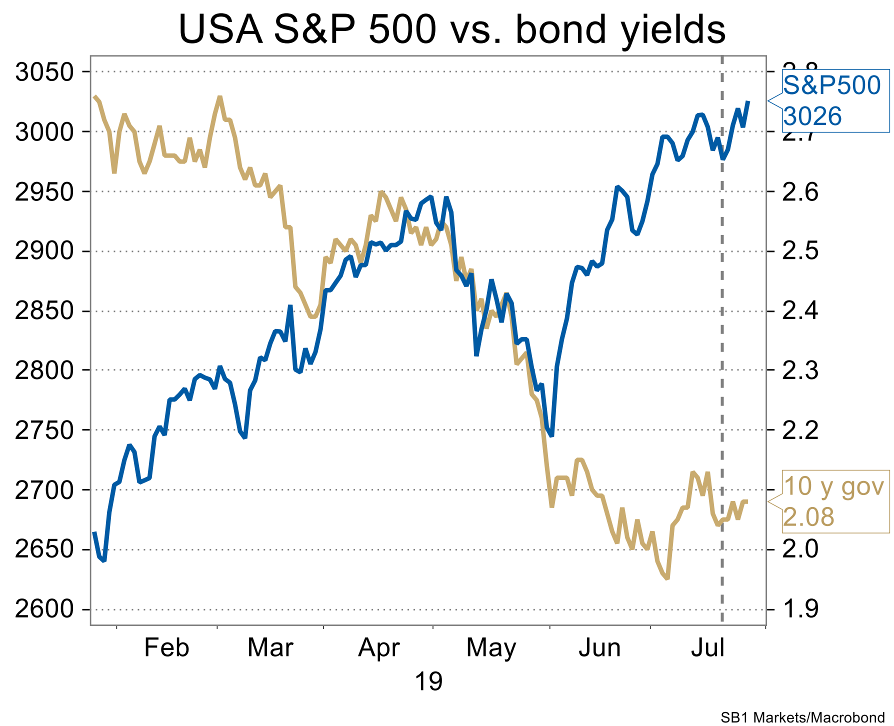


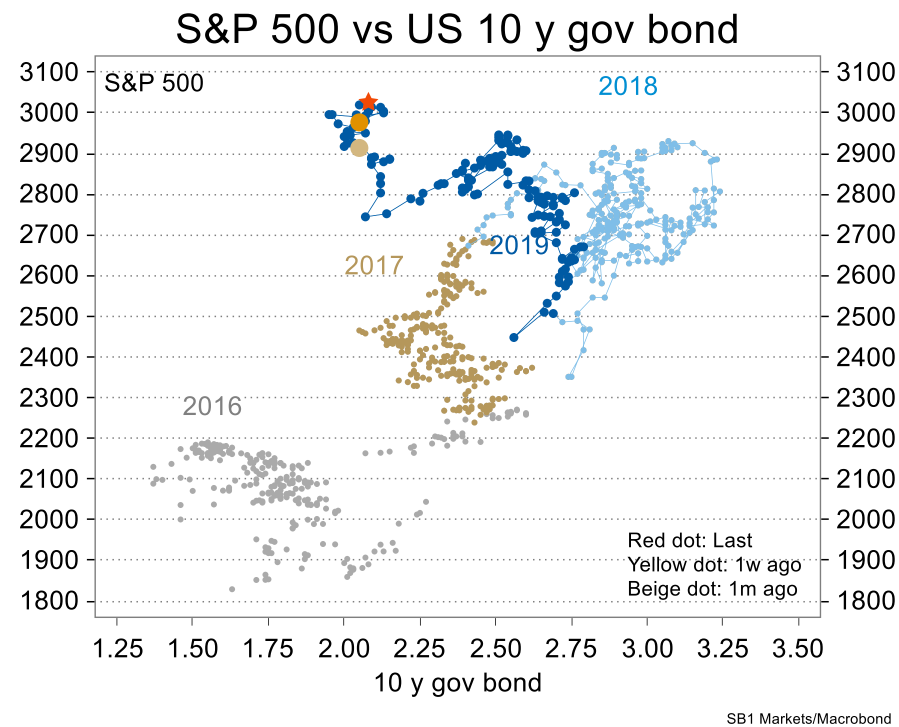
- Is the USD far too strong? Well, the greenback is 8% above average since 1990 (in order to capture two f/x cycles), measured by the real exchange rate (PPP), the same deviation as in Oct 2016, before Trump was elected. It has been up to 40% above the average in 1984 (backward calculated)
  - Higher 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

SpareBank 1 MARKETS

US: Higher bond yields, and another S&P500 ATH

Bond yields up 3 bps, to 2.08%. S&P500 up to ATH as earnings disappointed less last week

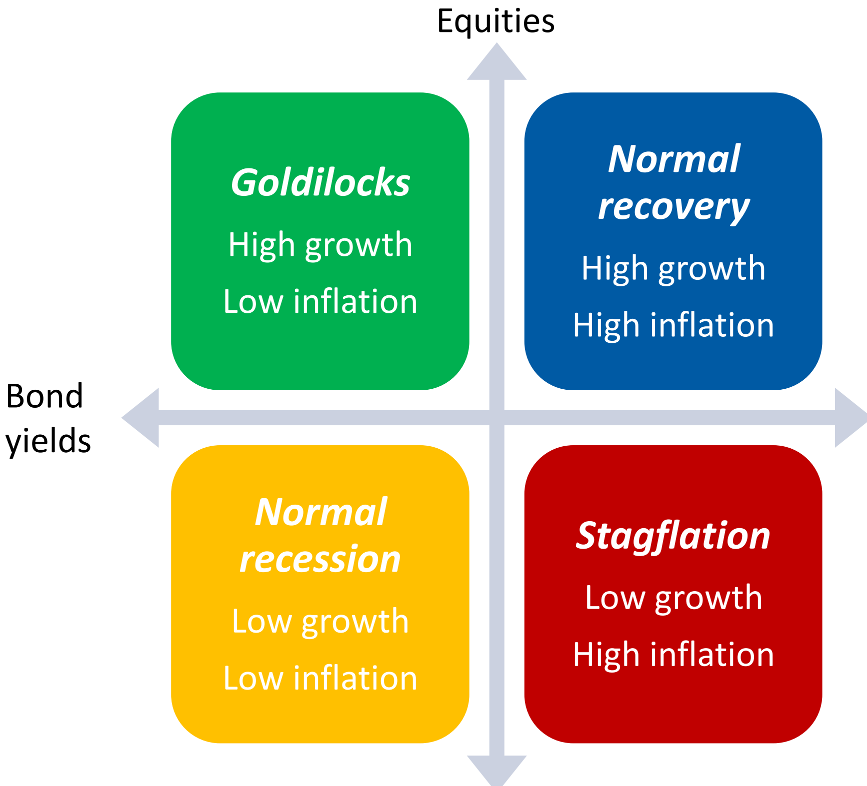


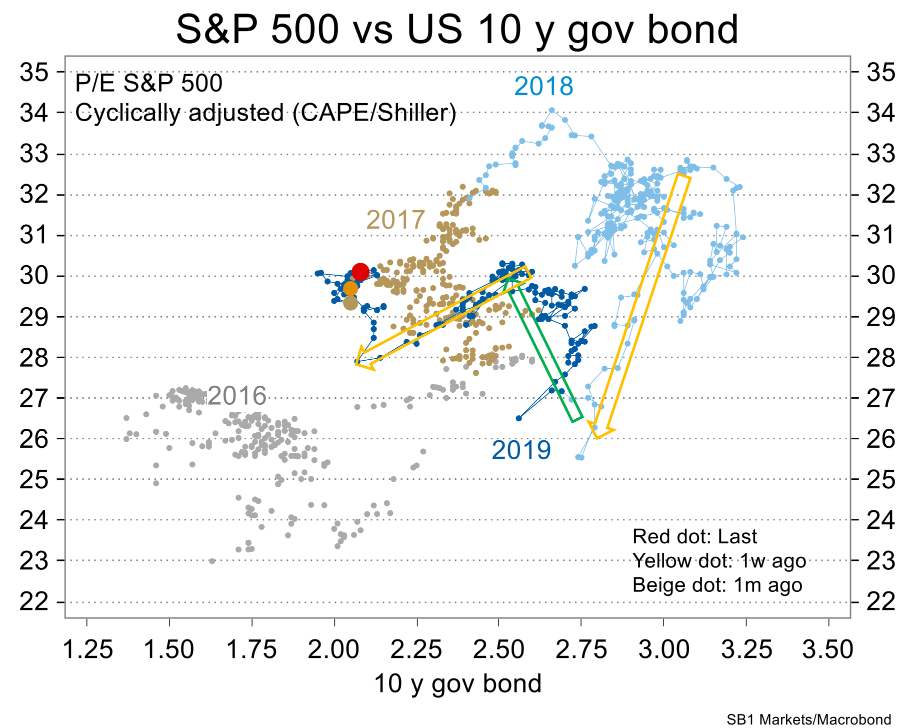


- For more on the relation between stocks and bonds, check next page

USA markets towards 'normal recovery' last week: Yields, equities up

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

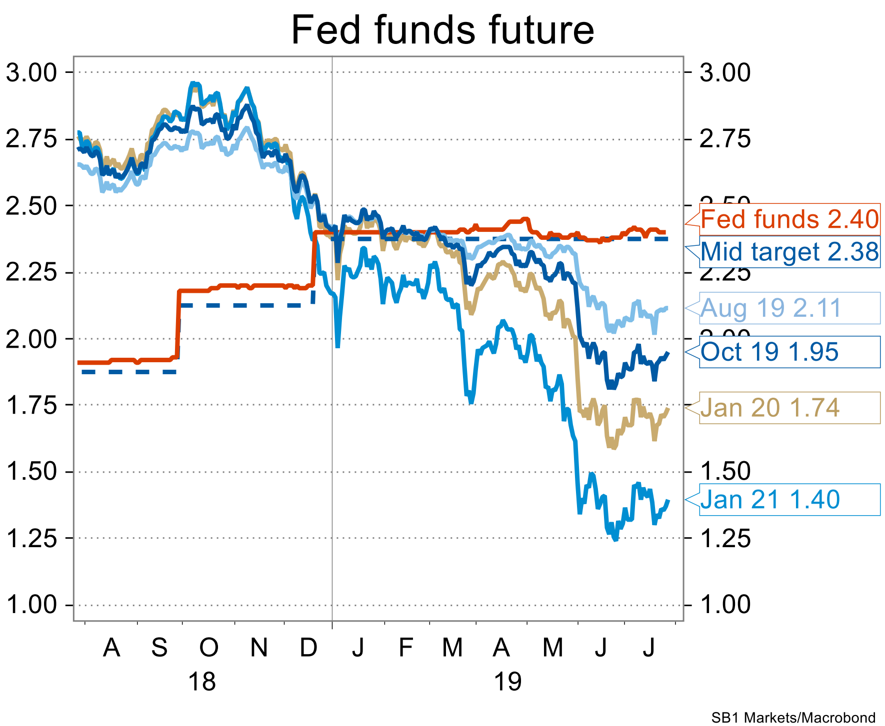


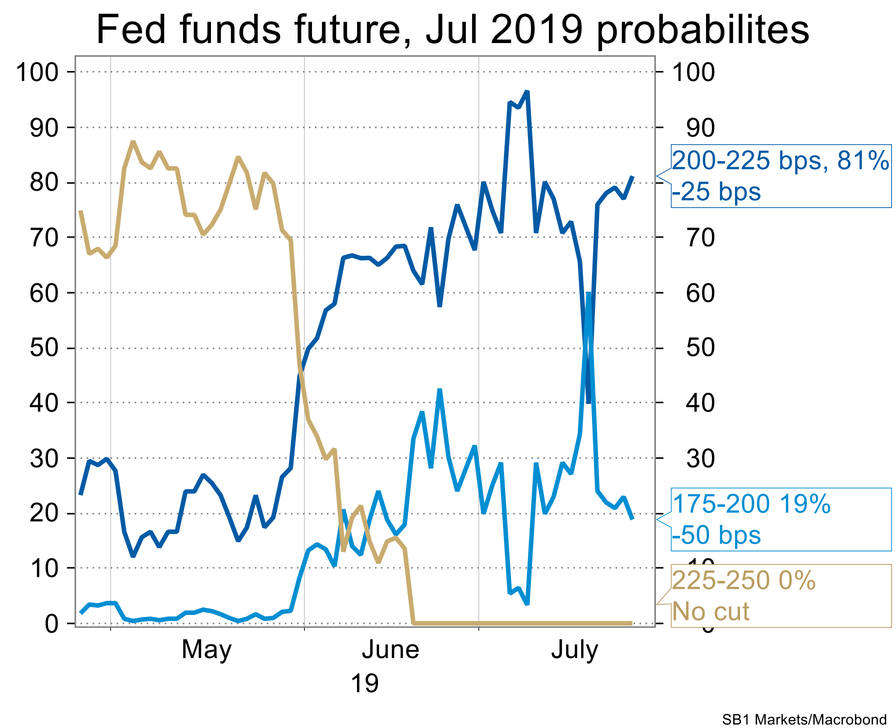


- During May, both stocks and bond yields fell sharply, towards the 'normal recession' (yellow) corner. The 'yielding' signals from the Fed (and other central banks) during June then pushed bond yields further down, and stock markets up – in the Goldilocks direction.
- <u>We still think 'normal' axis, driven by growth, and with inflation (or at least interest rates) over time following growth up or down (the yellow/blue axis)</u>
- 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

A 25 bps cut a done deal. Still market puts a 19% probability of a 50 bps cut

Well, Fed's communication will be much more important. Given present data, how gloomy can it be?

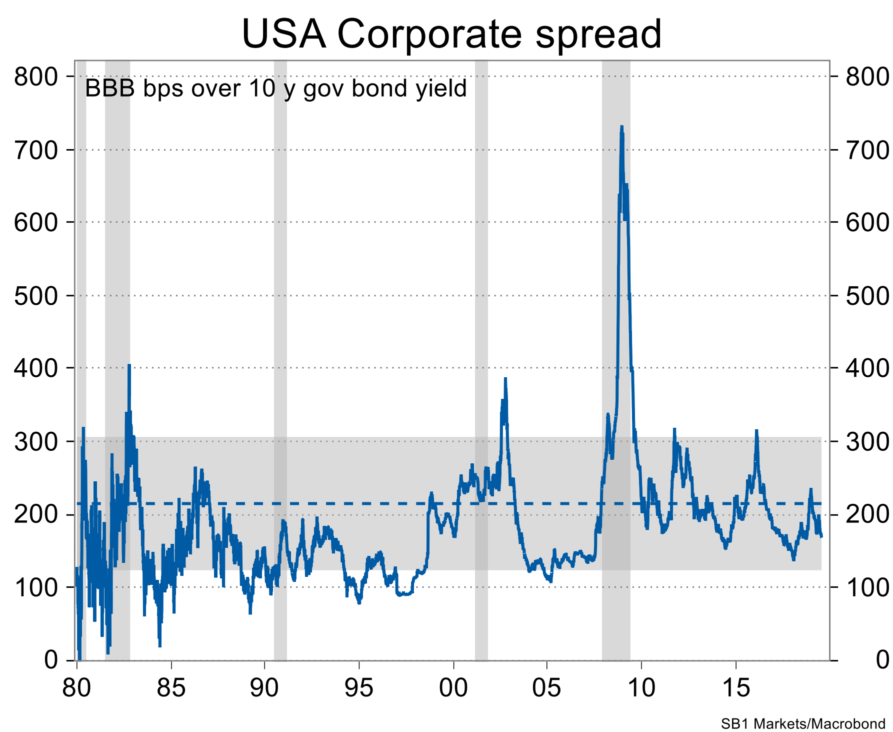


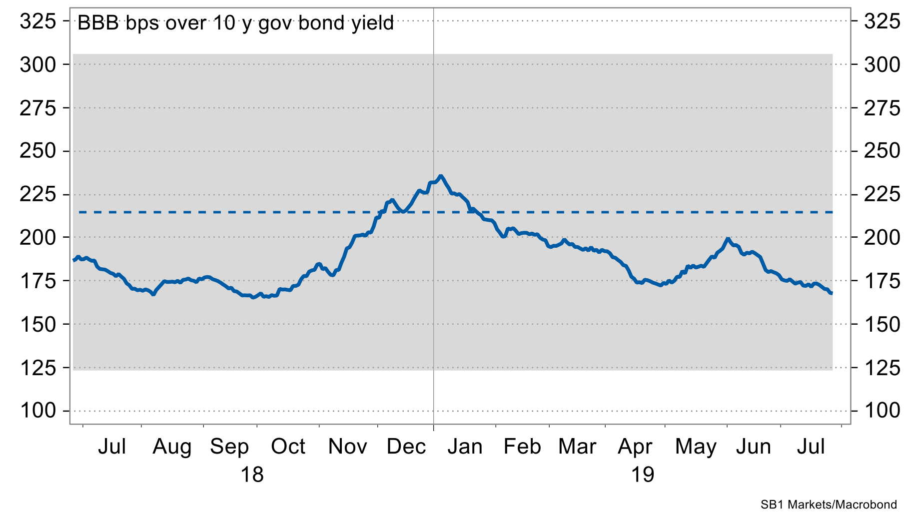


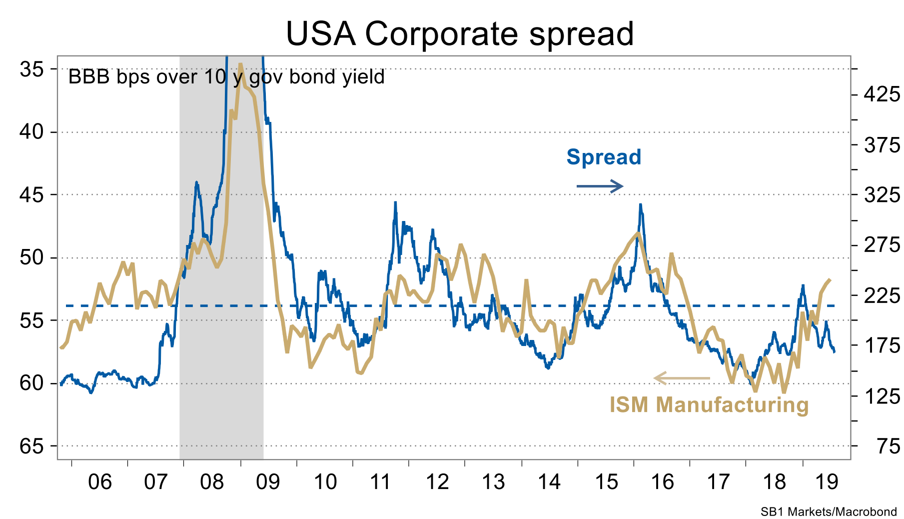
- US GDP growth has slowed slightly but it is still above or at trend, supported by growth in consumption. Inflation is not far below the target. The real Fed funds rate is just above zero. Yes, there are clouds at the horizon but is still not raining. The USD is stronger than normal but not by that much. In June, most FOMC members expected the Fed funds rate to be kept unchanged trough H2.
- Since then, trade news have been at the positive side and risk markets have recovered substantially. The S&P 500 is at all time high, and credit spreads are low. So therefore, at Fed has no choice but cutting the signal rate…

Credit spreads are narrowing marginally again

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

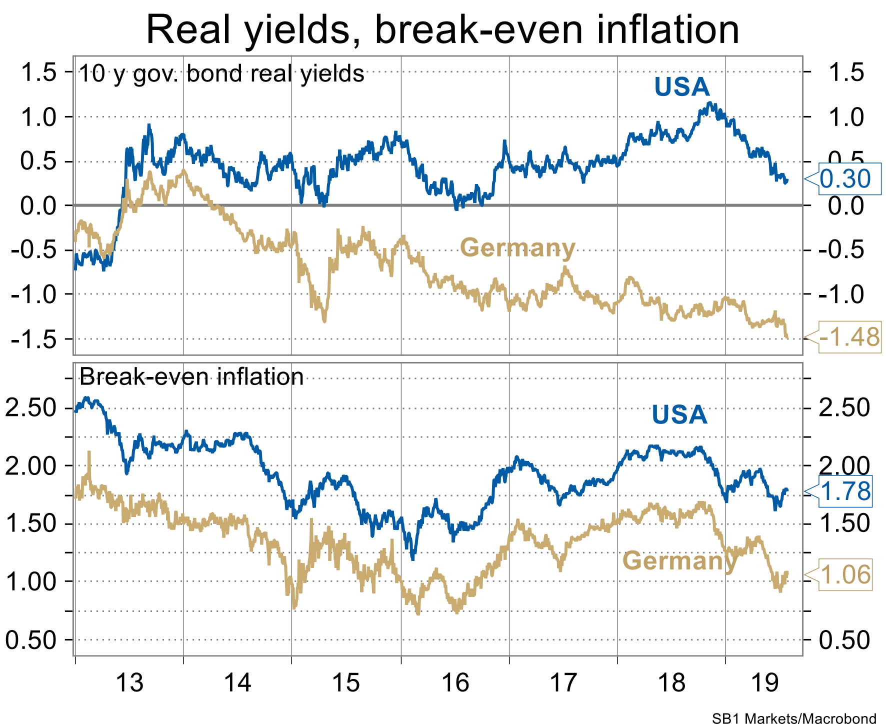


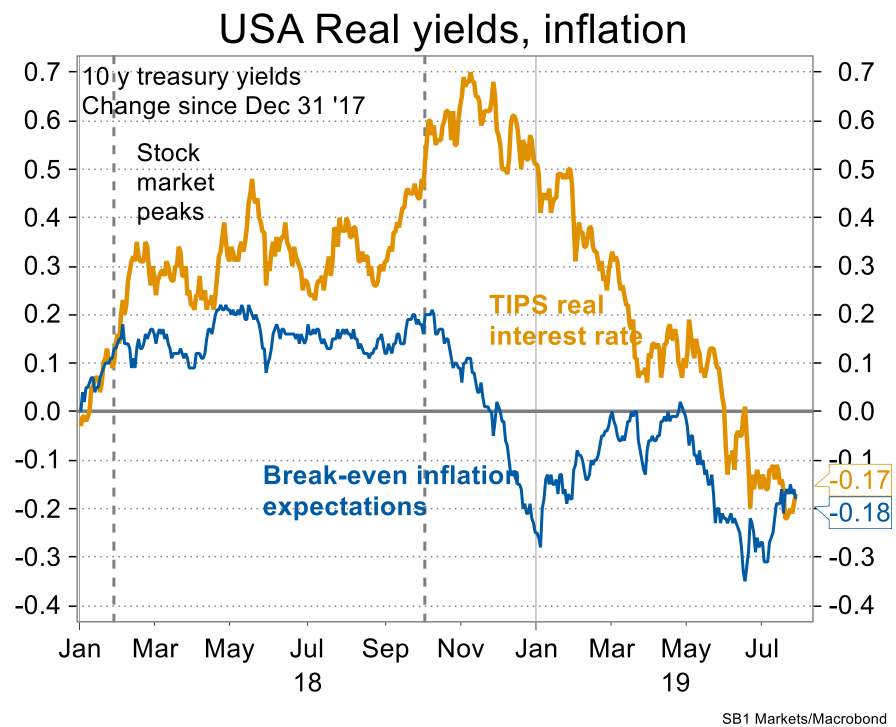




German inflation expectations up, real rates down; the other way in the US

German 10 y real rate down to -1.48%, per year, a new ATL!!!

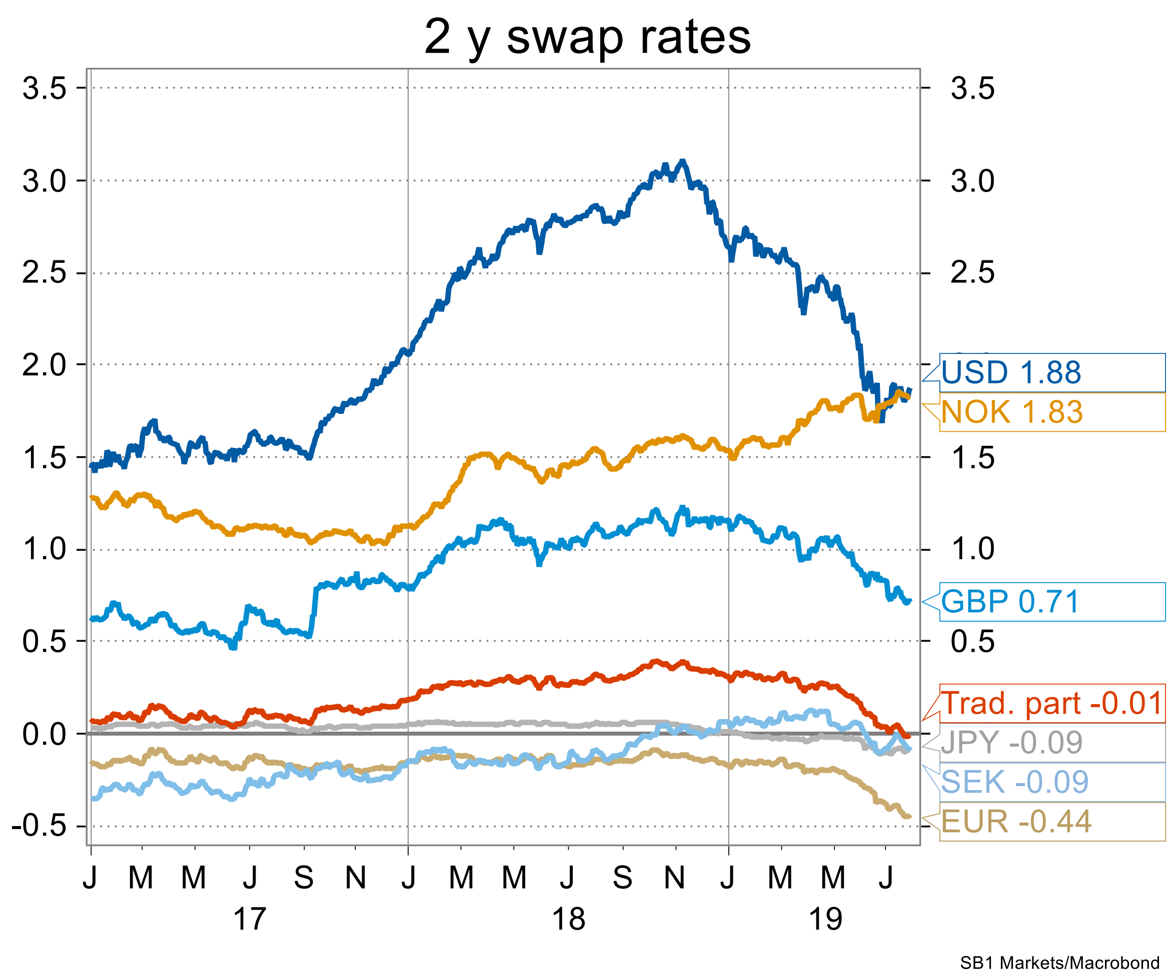


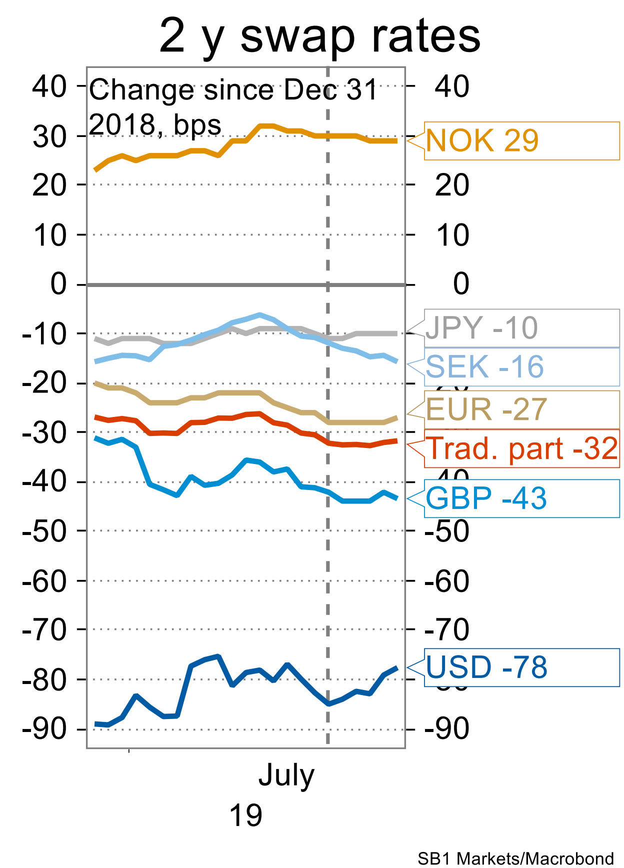


- US 10 y real rate at 0.30% (+5 bps), inflation expectations (measured by CPI) at 1.78%
- German real rates further down 4 bps, to -1.48%, incredible. Inflation expectations at 1.06%

Short term rate down in Sweden, flattish elsewhere

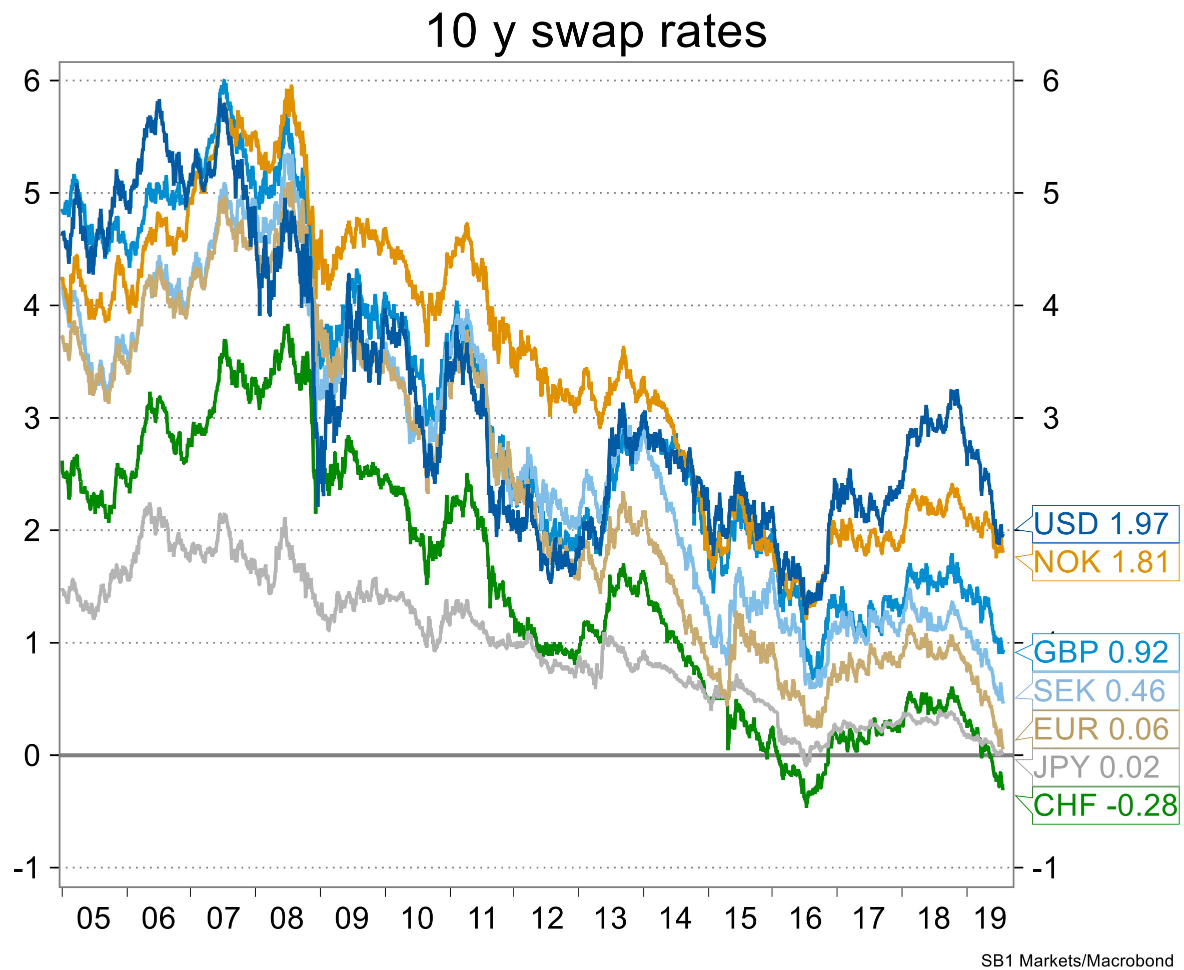
And new ATLs day after day in EMU. The ECB has to tell a story this week… NOK rates high, vs others

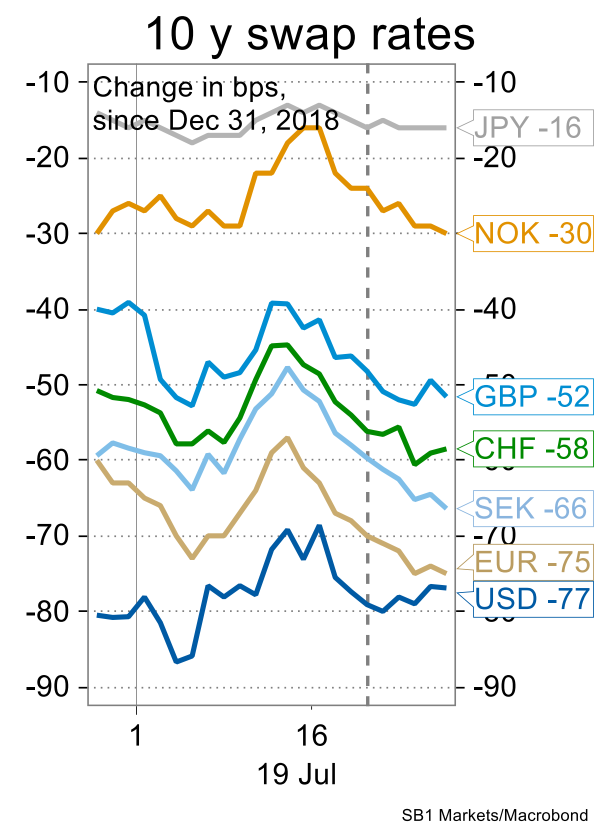




Long term swap rates down everywhere but in US last week

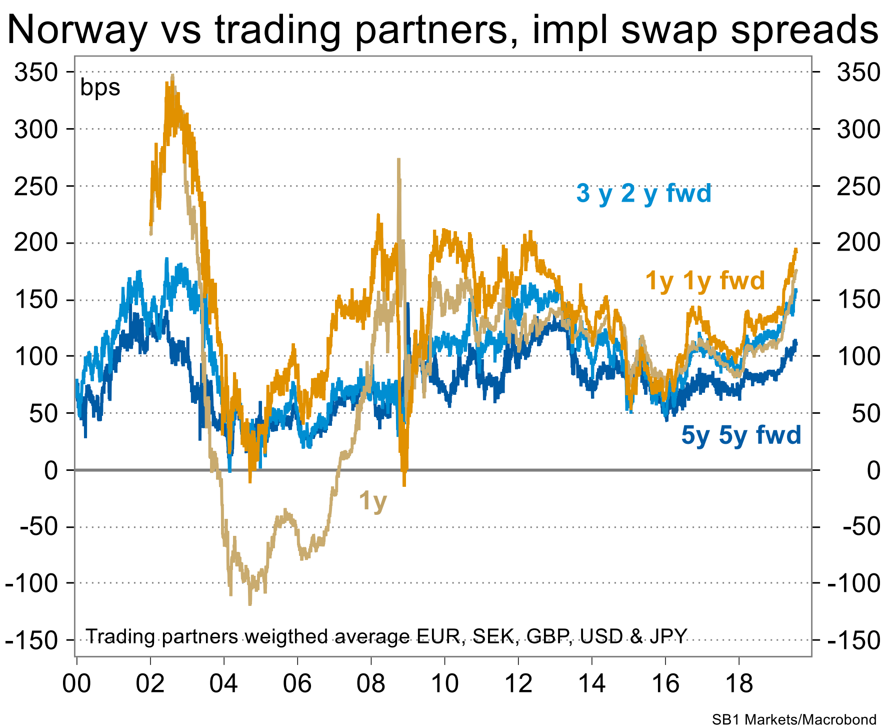
And the trend is straight down, everywhere

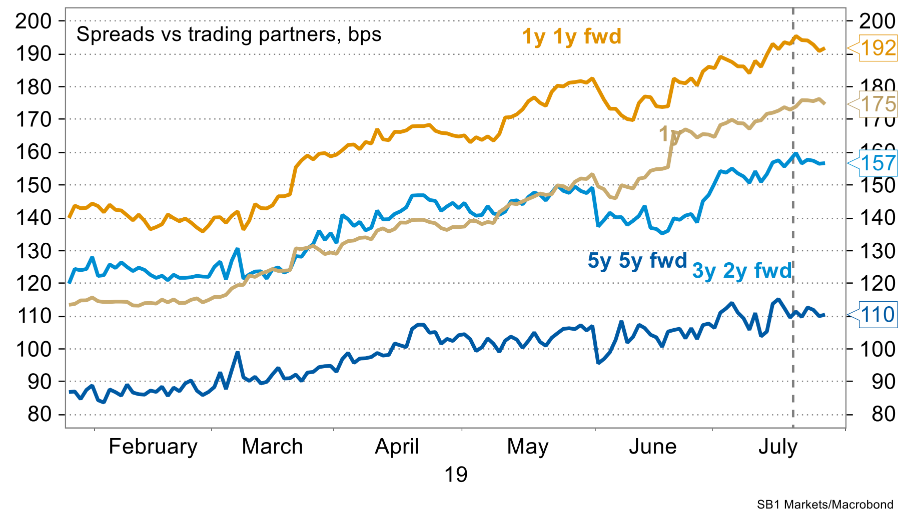


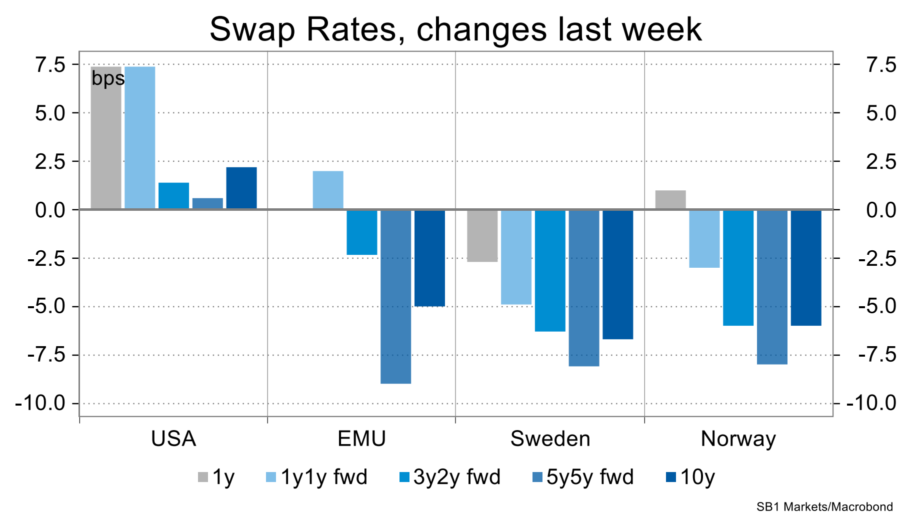


SpareBank 1 MARKETS

NOK swap spreads vs trading partners close to flat last week



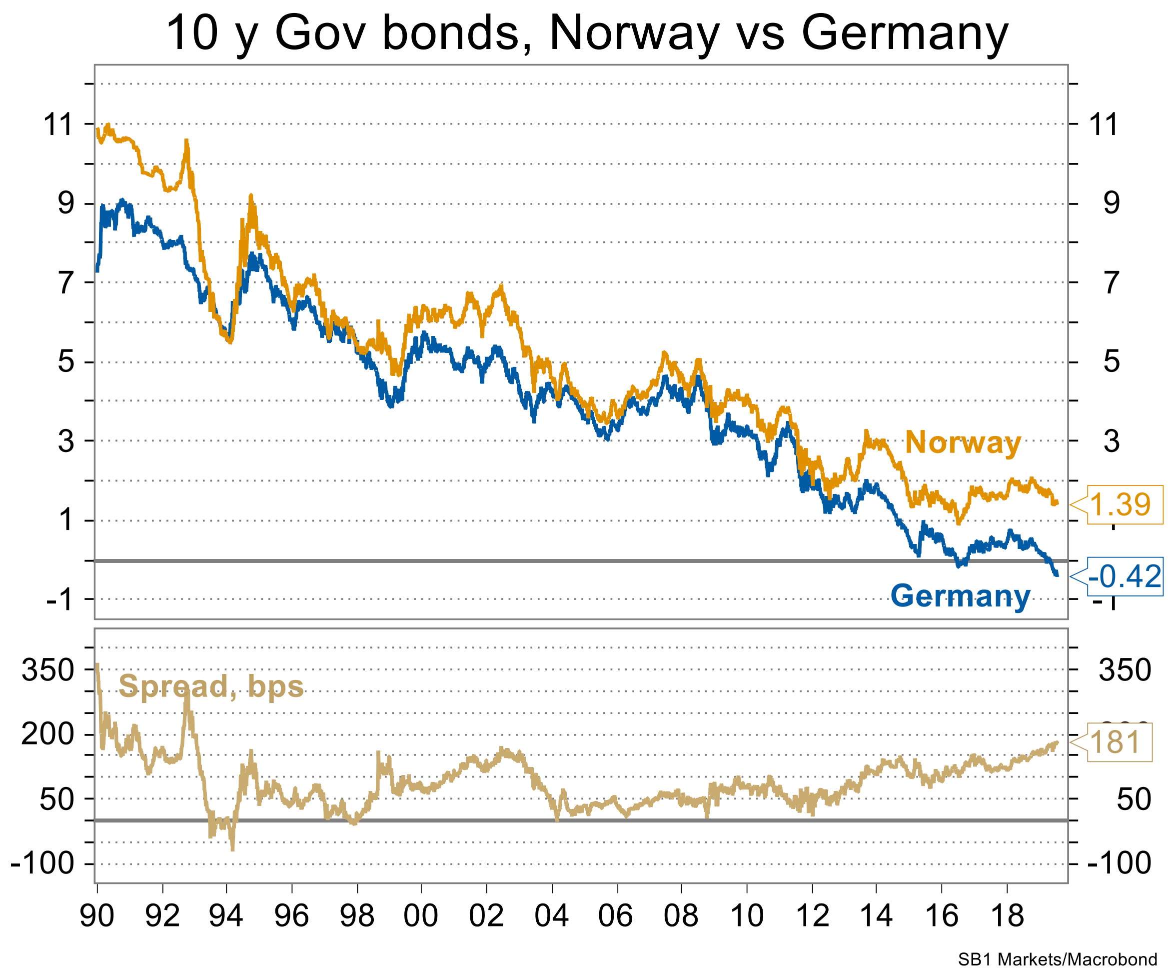


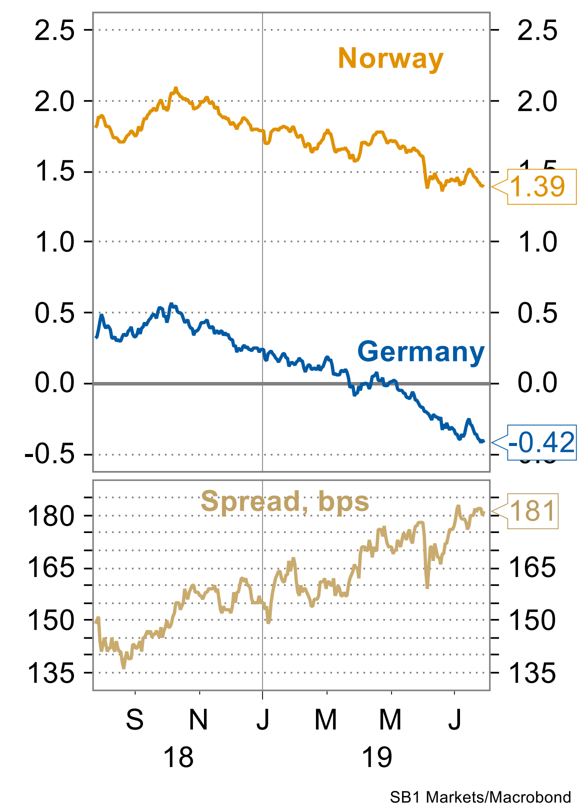


- A high spread is reasonable, given NoBa’s stance vs Fed, ECB and the Riksbank (which is due to solid Norwegian data, not a really hawkish bank..)
- Although the short term spread is well explained, we have been surprised by the wide spread in the long end of the curve of the since March

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

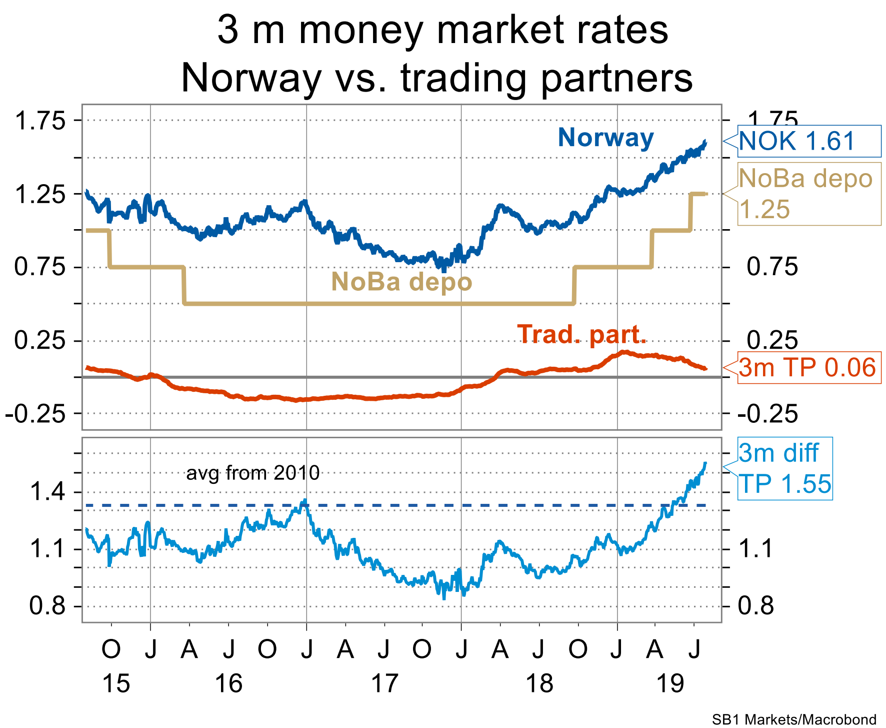
NOK 10 y gov down 7 bps to 1.39% - the spread vs the Ger. bund at 181 bp is far too rich, long term

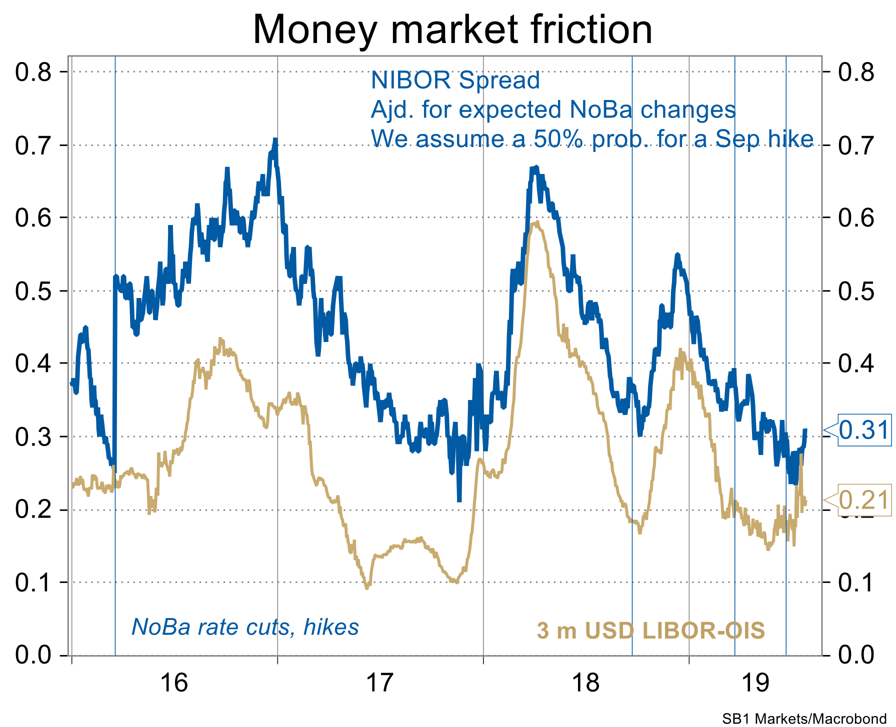




3m NIBOR up to 1.61%, now mostly due to higher spreads?

Warning: The US 3m OIS (as the TED) has widended – probably the NIBOR spread too

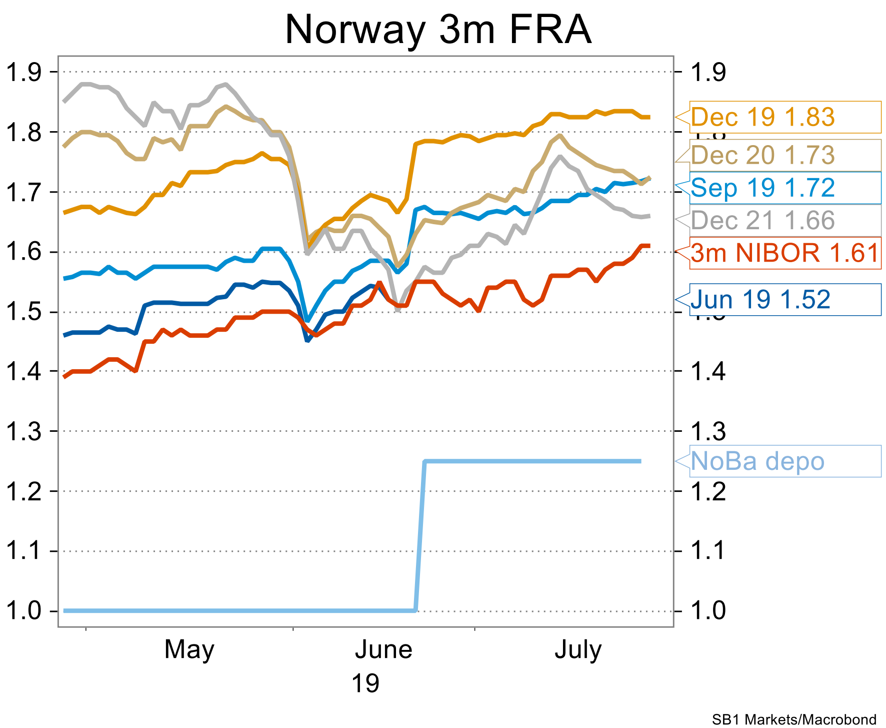


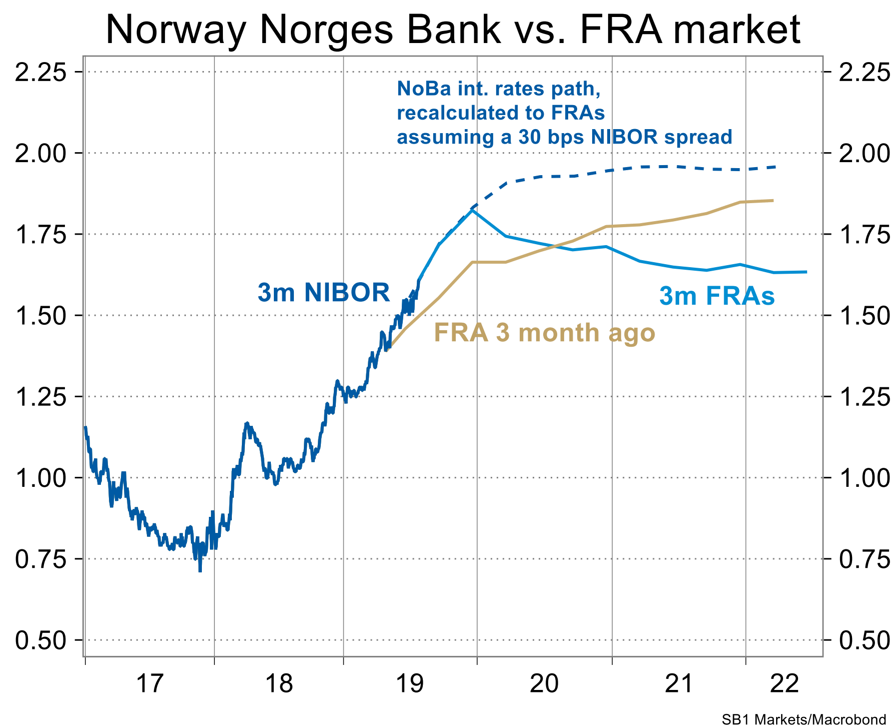


- IF the market believes a Sept hike is a done deal, the 3 NIBOR spread vs the signal rate the next 3 months is now at 26 bps. IF the market disregards any chance for a hike, the spread is 36 bps. We still think the market is pricing some 50% probability, and the 'real' NIBOR spread is just above 30 bps (more next page).
- The spread between NOK and trading partners' 3 m money market rates at 1.55 bps, above the 130 bps avg since 2010 – without sending the NOK into the orbit

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

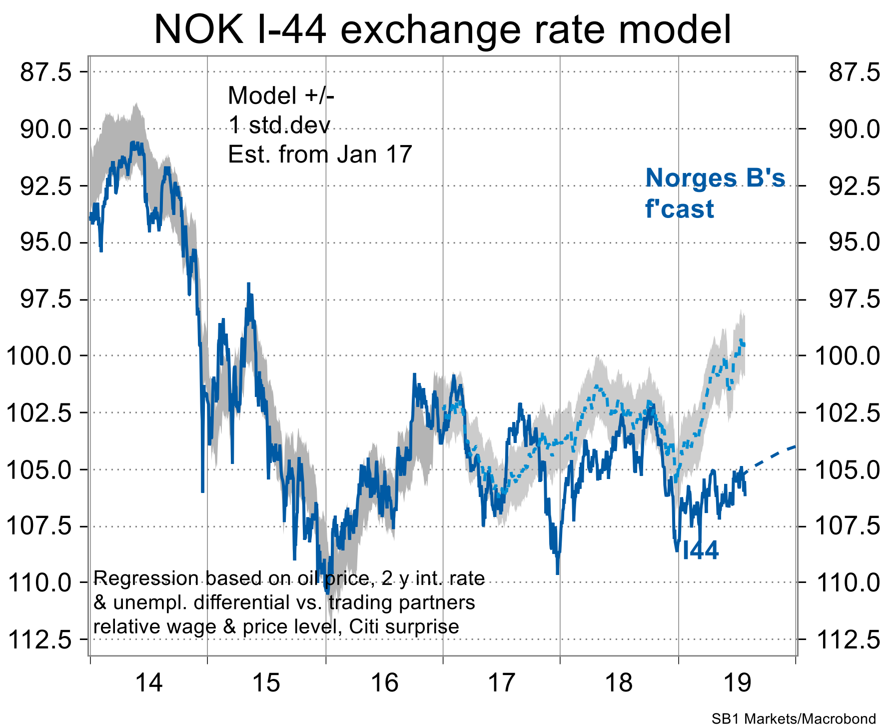


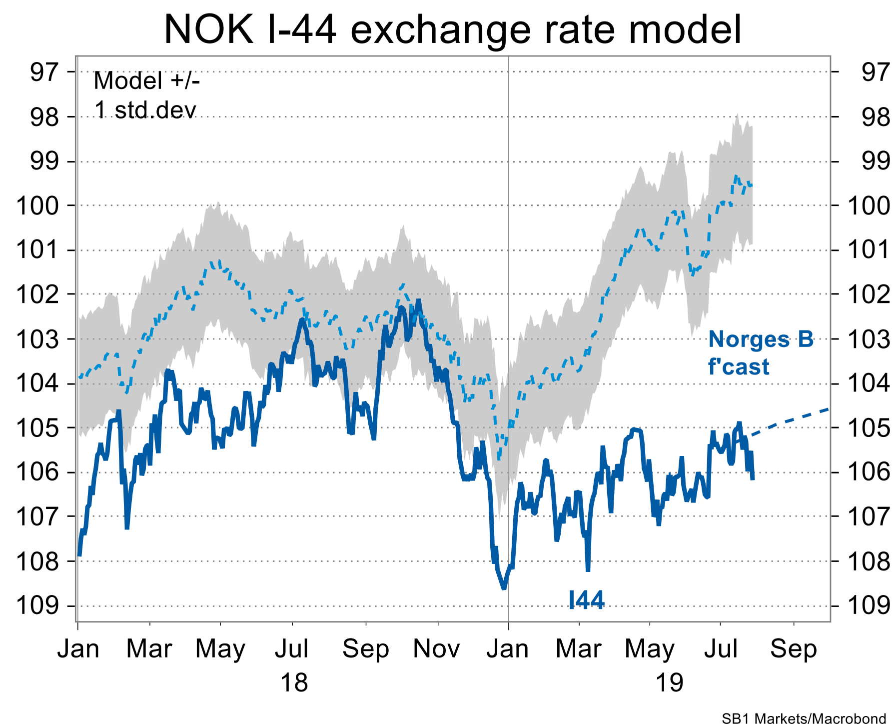


- The NIBOR Dec '19 FRA at 1.83%, signals either that at NIBOR spread has increased (we have until now assumed 30 bps) or that the market is puts some probability for a hike both in Sept and Dec (if so up to signal rate at 1.75, and a NIBOR at 2.05). We think a spread widening is most likely
- The FRA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

NOK down 1% last week, for no good reason

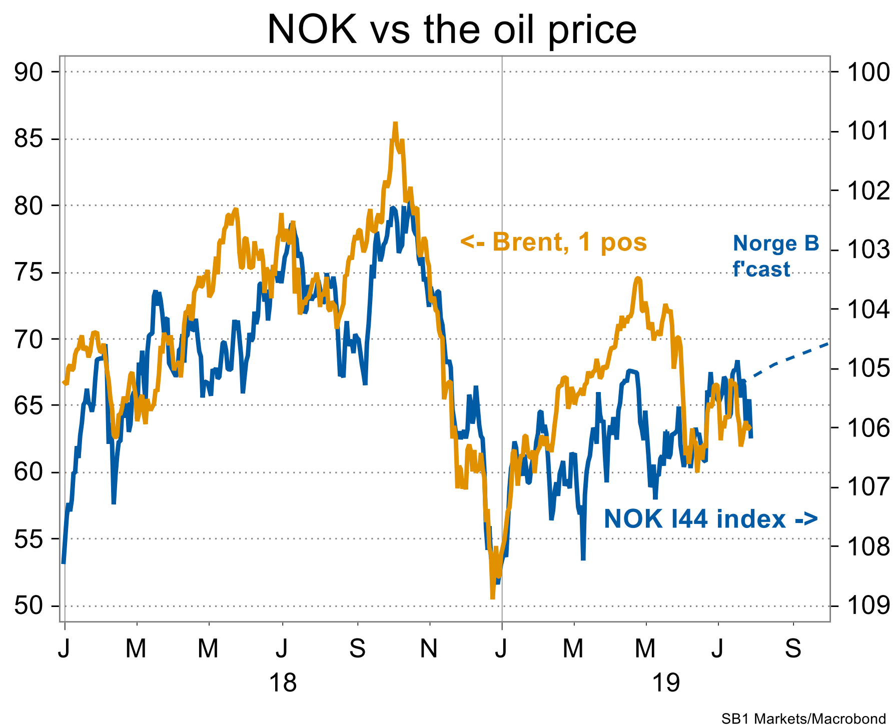
The NOK is still more than 6% below our model's f'cast

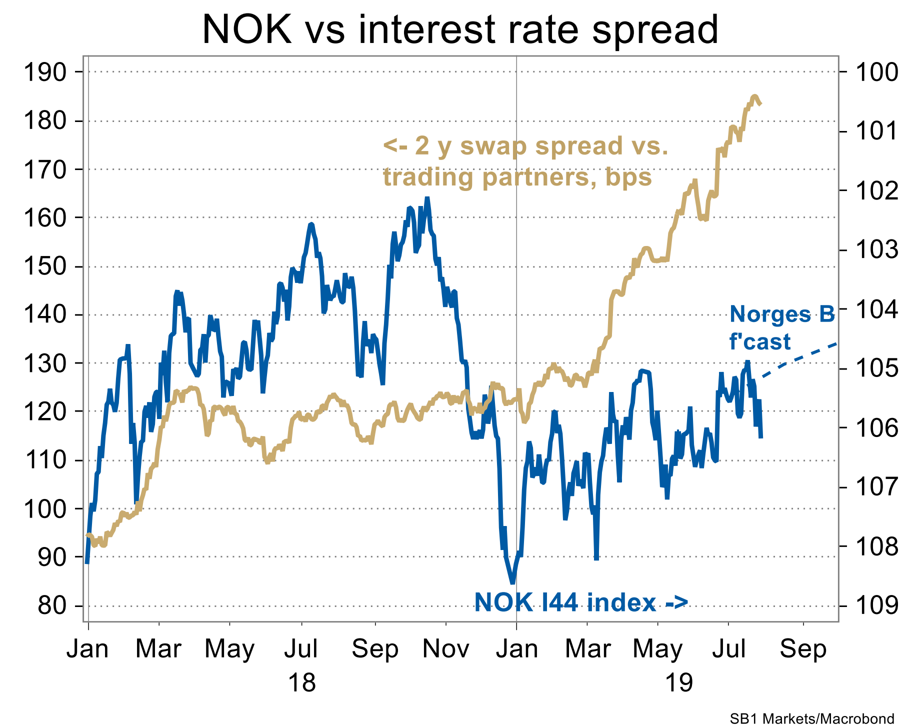




- The model forecast close to unch; the oil price fell but other elements contributed on the other side
- What explains the (extra) weakness vs the model estimate since March?
  - » No really weak Norwegian macro data, on the contrary, most data have been upbeat
  - » Risk aversion? Perhaps, yet EM currencies 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**

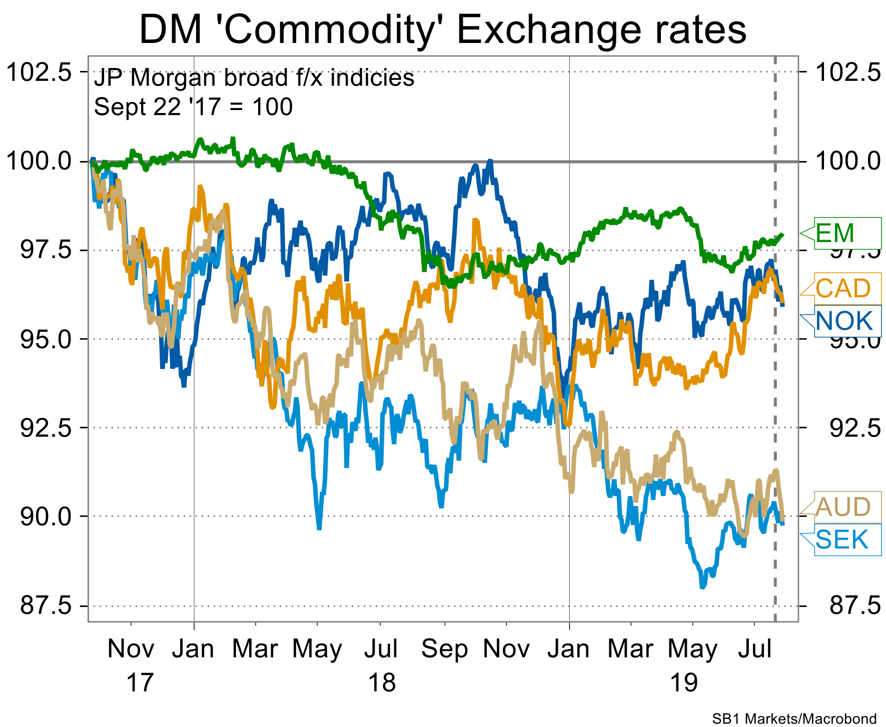
NOK down with the oil price last week

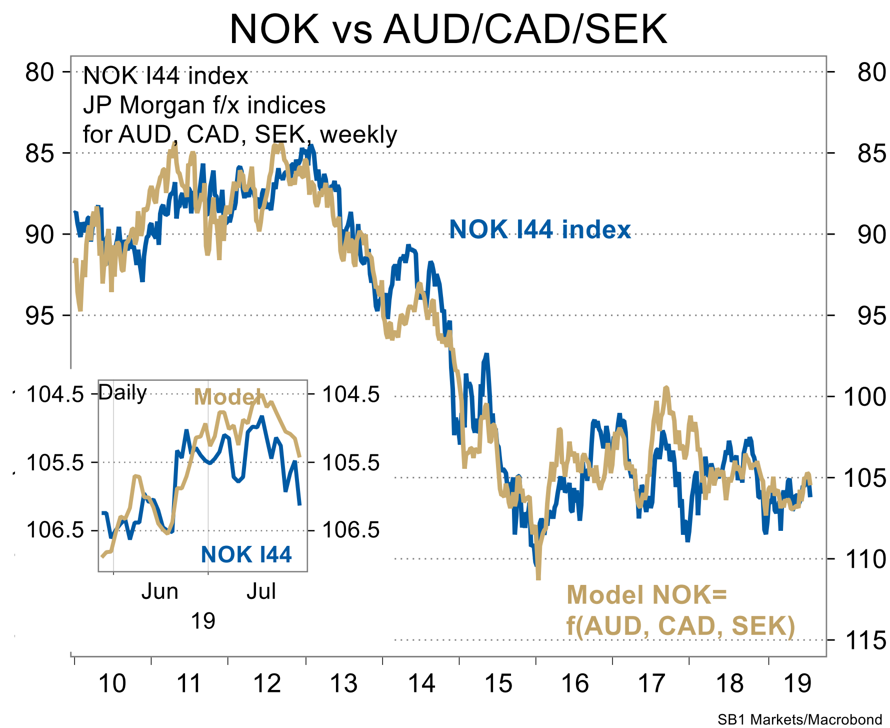




NOK follows our supercycle pals pretty well over time – and now

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

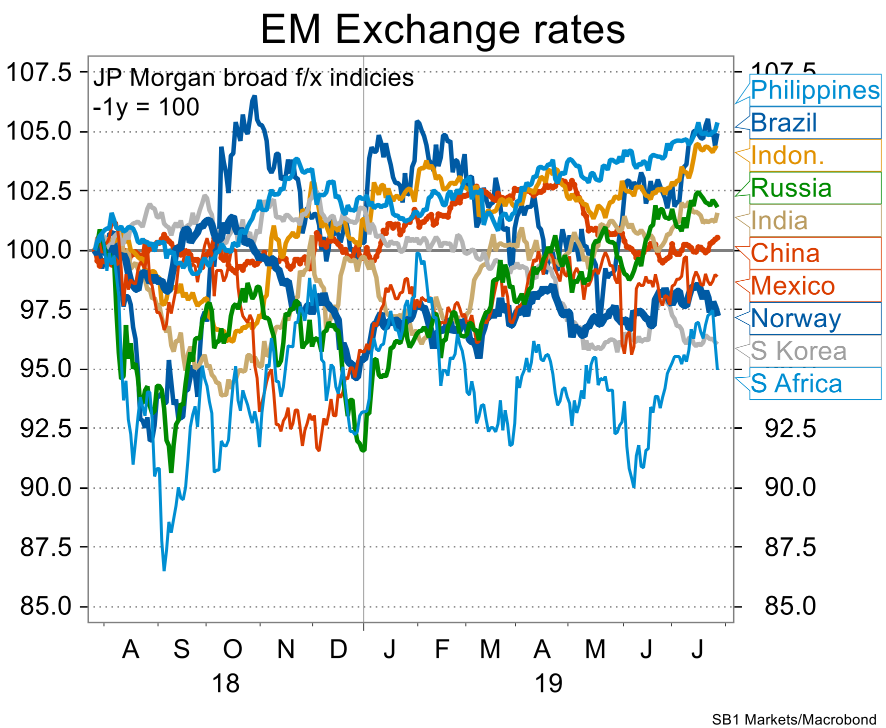


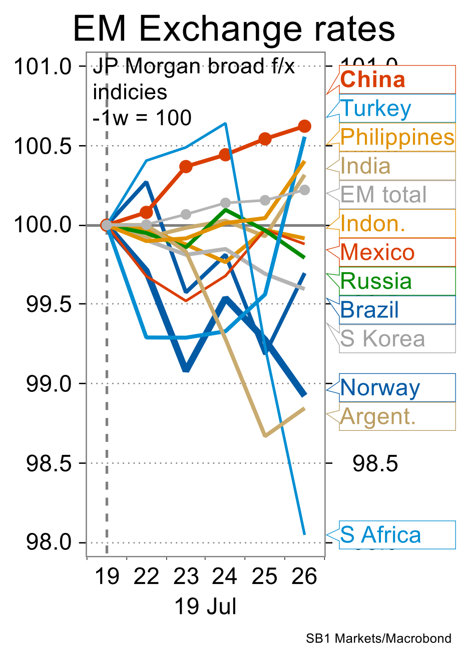


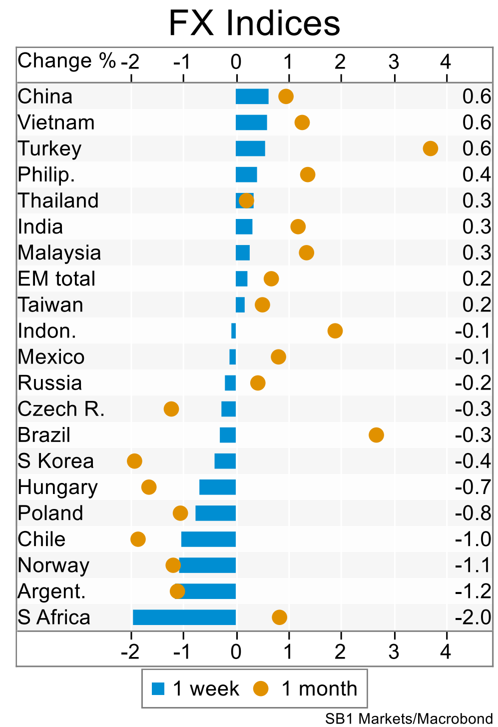
- NOK is much weaker than our workhorse model predicts, and much lower than others' models suggests (NoBa's model miss is almost twice as large as our model's residual)
- If we just model NOK as a function of AUD, CAD and SEK indices, the 'new' NOK weakness since 2017 is much better explained. It was 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: China's CNY lifted the EM segment – mixed among the rest

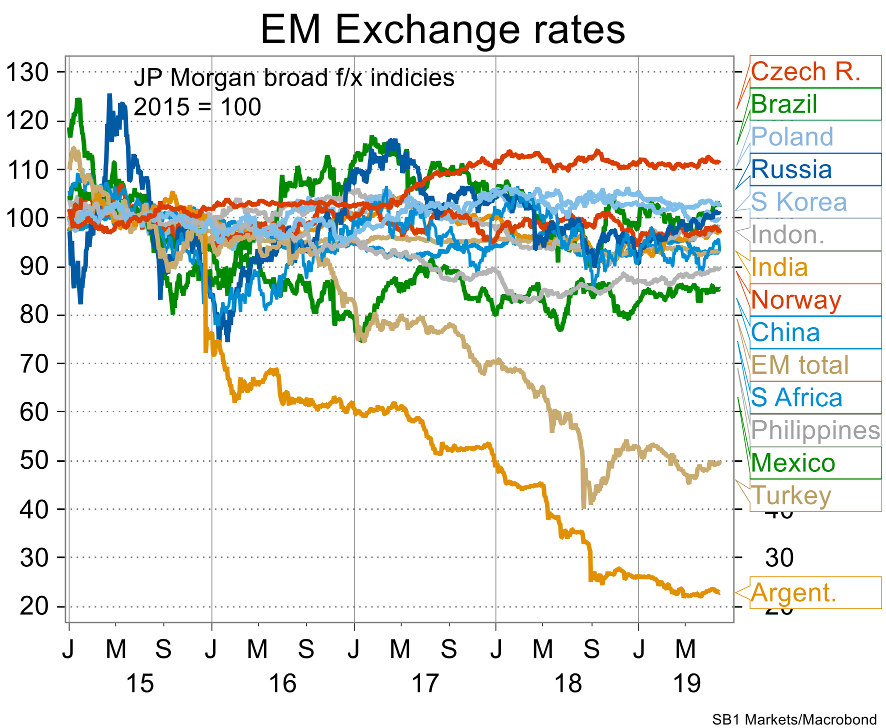
The CNY appreciated before the news about US trade reps going to Bejing this week

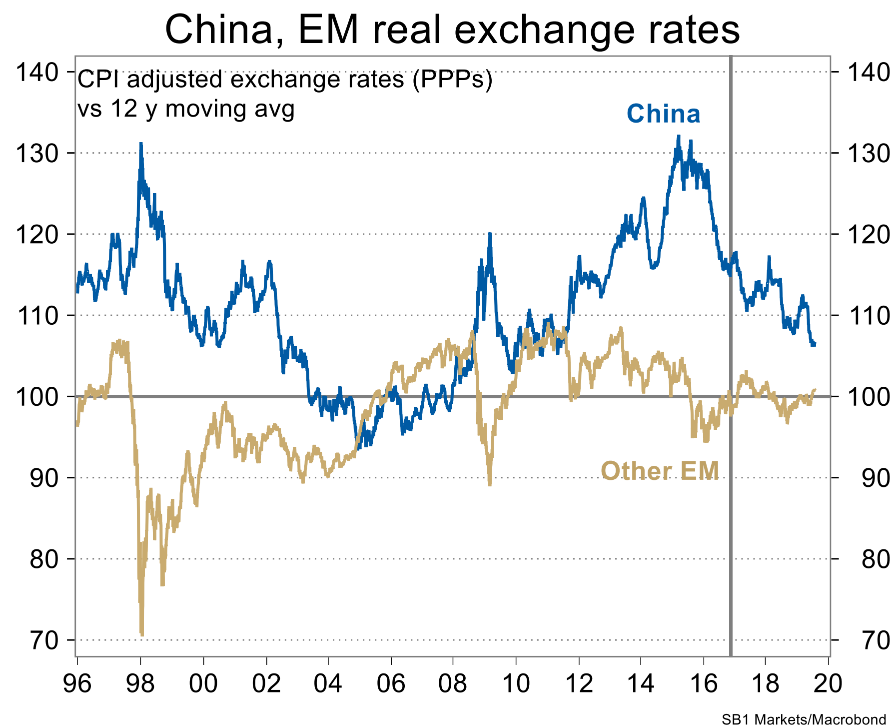






EM f/x, a long term view: Not that exciting, now





- 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 – but the lira has lost 50% of its value and the peso 75% since 2015

DISCLAIMER

DISCLAIMER

SpareBank 1 Markets AS ("SB1 Markets")

This report originates from SB1 Markets' research department. SB1 Markets is a limited liability company subject to the supervision of The Financial Supervisory Authority of Norway (Finanstilsynet). SB1 Markets complies with the standards issued by the Norwegian Securities Dealers Association (VPFF) and the Norwegian Society of Financial Analysts.

No investment recommendation

Any views and opinions relating to securities mentioned in this report should be interpreted as general market commentary, and not as investment recommendations within the meaning of section 3-10 of the Norwegian Securities Trading Act.

No personal recommendation

The information contained in this publication is general and should not be construed as a personal recommendation within the meaning of the Norwegian Securities Trading Act, section 2-3 (4). It does not provide individually tailored investment advice regarding a particular financial situation, investment experience, risk profile or preferences of the persons who may receive this report. For tailored investment advice regarding stocks mentioned in this publication, please consult our brokerage desk or your individual investment advisor.

Research for the purposes of unbundling

This report is deemed to constitute a minor non-monetary benefit for the purposes of the inducement rules under MiFID II. The report is publicly available on our website (no log-in required).

Conflicts of interest

SB1 Markets, affiliates and staff may perform services for, solicit business from, hold long or short positions in, or otherwise be interested in the investments (including derivatives) in any stock mentioned in this publication. To mitigate possible conflicts of interest and counter the abuse of confidential information and insider knowledge, SB1 Markets has set up effective information barriers between divisions in possession of material, non-public information and other divisions of the firm. Our research team is well versed in the handling of confidential information and unpublished research material, contact with other divisions, and restrictions on personal account dealing. The views expressed in this report accurately reflect the analyst's personal views about the companies and the securities that are subject of the report, and no part of the research analyst's compensation is related to the specific recommendations or views expressed in this report.

Accuracy of sources

All opinions and statements in this publication are, regardless of source, given in good faith, and may only be valid as of the stated date of this publication and may be subject to change without notice. SB1 Markets has taken all reasonable steps to ensure that the information contained in this report is true and not misleading. Notwithstanding such efforts, we make no guarantee as to its accuracy or completeness.

Risk information

Return on investments is inherently exposed to risks. The value of an investment position may both rise and fall during the investment period. If the return on investments is positive at one time, there is no guarantee that it will remain such in future. In certain cases, losses may exceed the sum of the original investment.

Limitation of liability

Any use of information contained in this report is at your own individual risk. SB1 Markets assumes no liability for any losses caused by relaying on the information contained in this report, including investment decision taken on the basis of this report.

Limitation on distribution

This publication is not intended for, and must not be distributed to, individuals or entities in jurisdictions where such distribution is unlawful.