2 September, 2019

Macro Research

Weekly update 36/2019

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The headlines are linked to the relevant section in the report
The elements on the the page "In this report" are linked
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Last week – the main takes

- **Politics:** President Xi is a brilliant leader and trade talks with China are going very well, thank you. Trump once again changed his mind (180 degr), and (most) markets cheered, once again. The long term picture: The trade/tech war is not moving towards a solution. Trump may want a quick fix simple (soya bean) trade deal, others in the US want to stop China now, before China overtakes the US. We think that's too late, but that's not the point, trade/tech tensions <u>may be here to stay</u> and business models must be rewritten (and huge resources reallocated). Elsewhere: **UK's PM Johnson** sent the Parliament on a longer autumn leave than normal (so that a hard, no deal Brexit cannot be blocked by a pro deal Parliament), while **Italy** seems to get a new government, without the Lega party, and without a new election (and the Spread collapsed, as Salvini fell on his own sword)

- **The Chinese PMIs** more up than down in August due to a recovery in Markits' manufacturing PMI (to well above 5y avg). The export indices down in average but no sudden halt to be seen

- **US durable goods orders** and investment orders inched up in July. Orders are pointing to a small decline in business investments into Q3, no sudden setback. **The core PCE price deflator** was flat at 1.6% y/y in July but underlying growth is at target. **Consumption** has been soaring recent months, at a close to 5% speed, of which half is funded by a lower (but still high) savings rate**. Pending home sales** came down in July but the trend is straight up**. House prices** slowed to 1.9% m/m annualised in July (CS index), the softest housing market data at hand? **CB's consumer confidence** index held steady at an elevated level in August, but the **UoM sentiment** survey fell even more the first reported, the largest decline since late '12 (such large declines usually happens only once every 3 – 4 years), and the differential to the CB signals... Guess what?

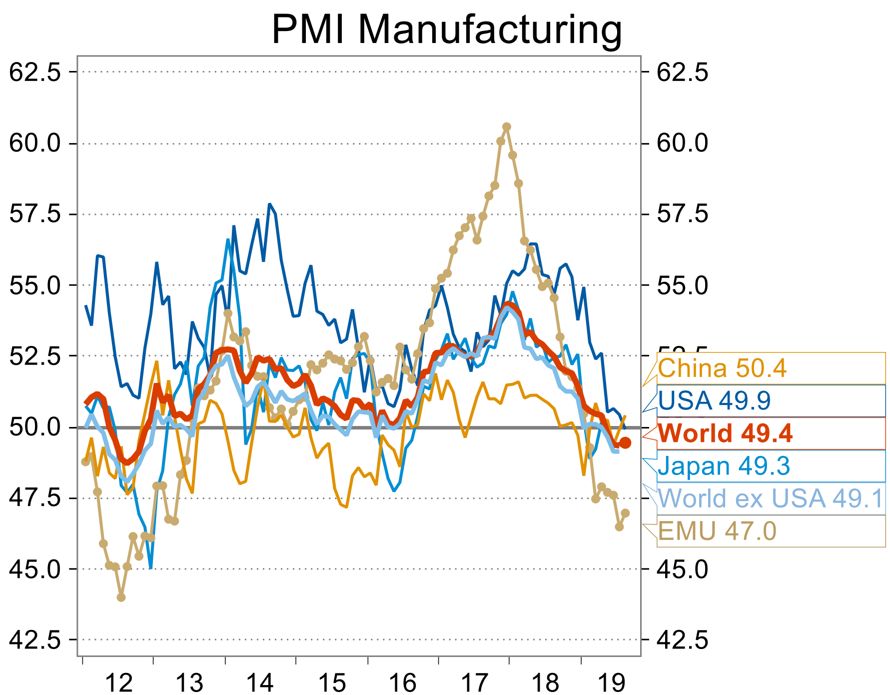
- **Eurozone unemployment** held steady in July, the pace of decline may be slowing amid easing growth. **Core CPI inflation** muted at 1%. **German GDP details** point to a gloomy outlook; household demand was muted and business investments fell. The **Ifo survey** do not signal any recovery either, weakest business expectations since 2009

- **Norwegian Mainland Q2 GDP** grew by 0.7% (2.7% annualized), 0.1 pp below f'casts. Moreover, Q1 was revised up by 0.2 pp. Although the GDP figure reflects an overall solid economy, the demand details were not too strong; public demand, oil investments and private consumption boosted activity in Q2. The two prior will probably not last; our take is that oil investments are peaking now in H2 2019, adding no growth contribution next year. Mainland business investments came in on the soft side, far below our f'casts, and the outlook is not strong. **Registered unemployment** fell by 1.1' persons in August (in total), reversing the recent minor uptick. However, unemployment is declining at a slower pace and other labour market measures are mixed. Brisk growth in **retail sales** in July, up 0.8% m/m, and is trending slowly up. **Credit growth** eased to 5.6% in July, down 0.1 pp. Yet, the slowdown was mostly due to a technical change regarding student loans, there are no indications of a pullback in household loan demand. <u>In sum: We stick to our view that Norges Bank will deliver another hike in September, unless stock markets fall steeply before then, or the Regional Network (Sept 10) notes a marked downswing</u>

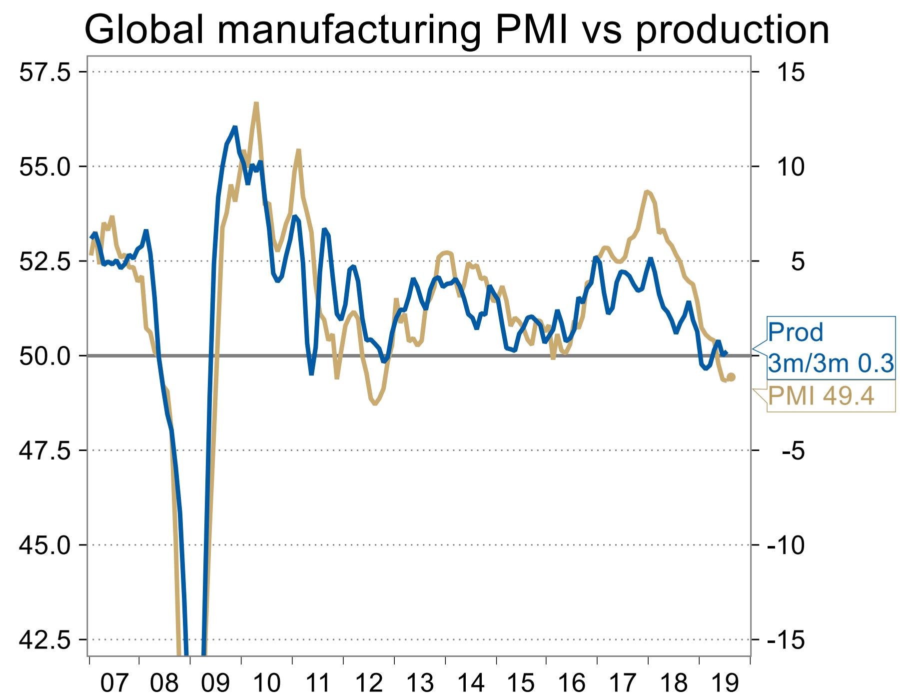
SpareBank 1 MARKETS

Ahead of global manufacturing PMI: Probably a tad up

We expect a 0.1 p lift, and it remains below the 50-line



Source: IHS Markit, SB1 Markets, Macrobond

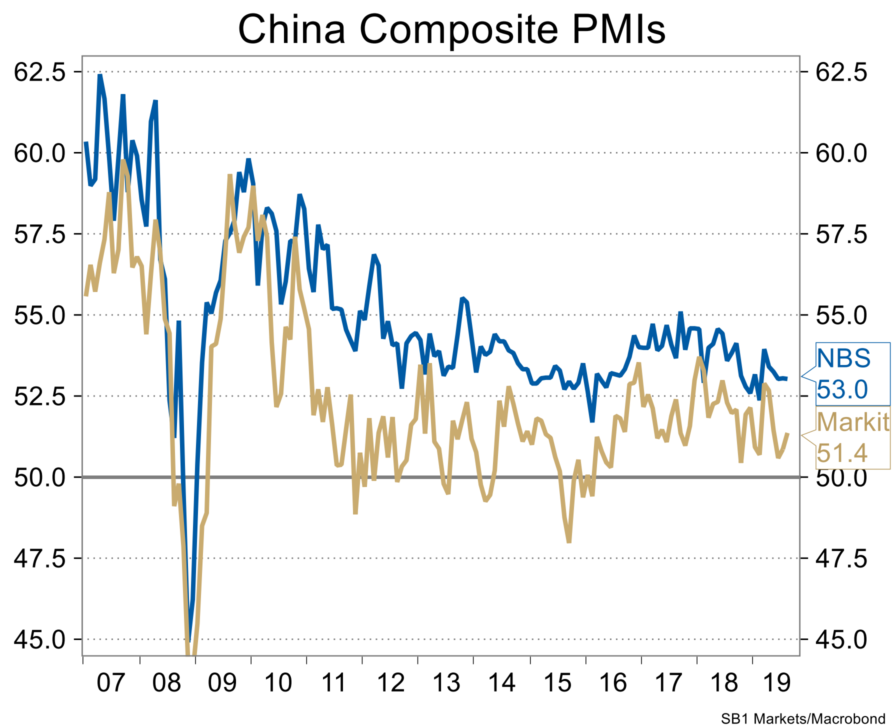


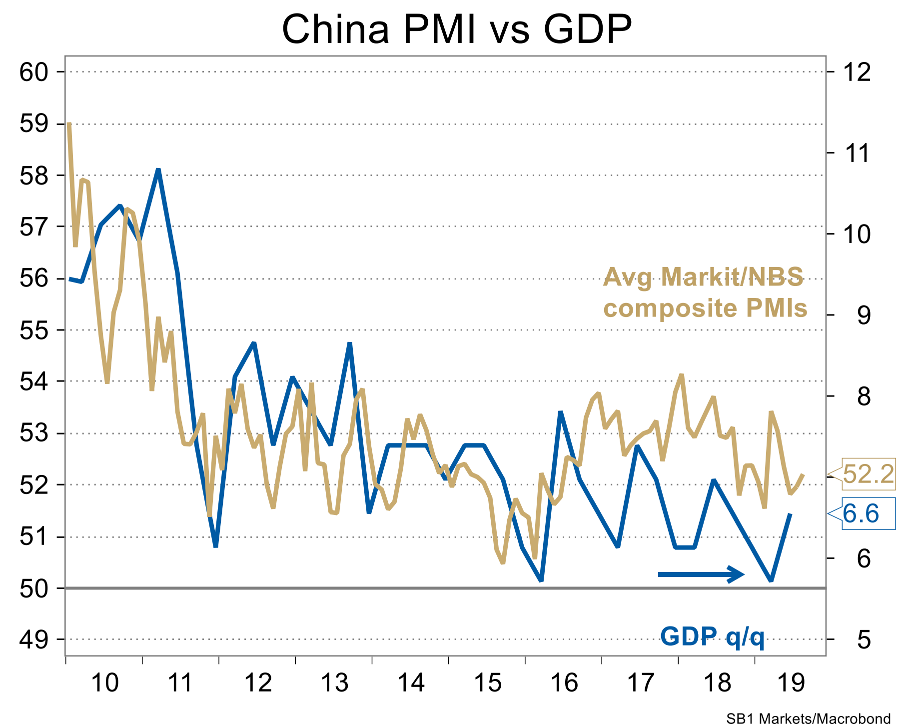
SB1 Markets/Macrobond

SpareBank 1 MARKETS

The PMIs more up than down in August

The NBS composite survey flat, Markit's probably rose

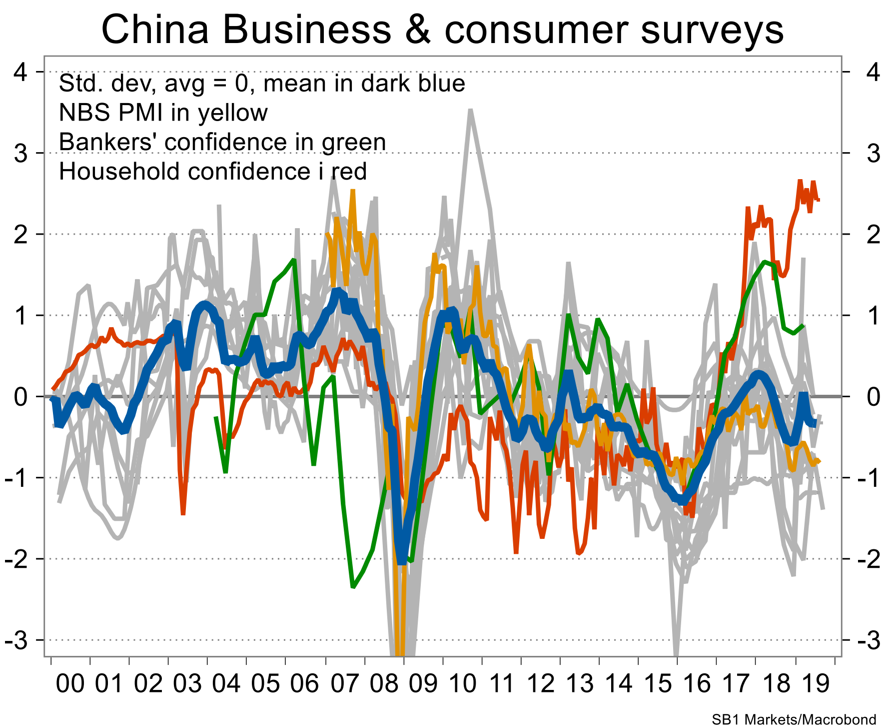


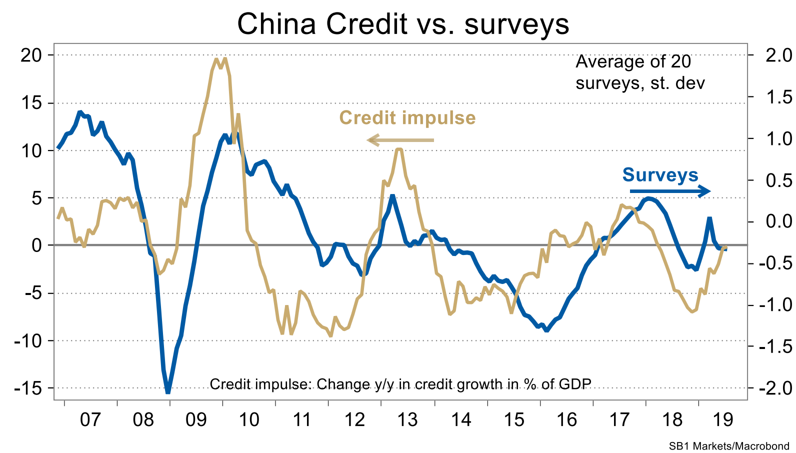


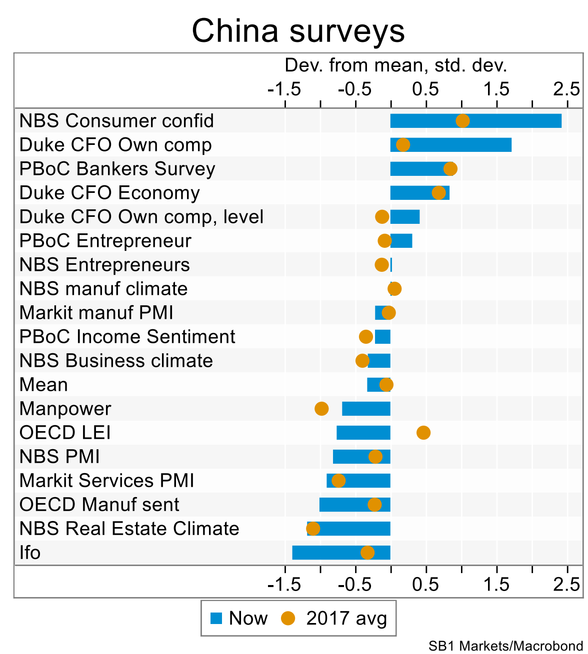
- NBS' composite PMI (CFLP) was stable at 53 in Aug, not too hot/too cold. The manufacturing index declined 0.2 p, stabilising recent months, while service businesses reported a small increase, to 53.8
- Markit's composite PMI probably rose as well, due to the surprising recovery in the manufacturing PMI
- The NBS service sector PMI is approx at the average over the past 5 years but is trending slowly down. Markit's volatile service sector PMI is trending flattish, while the level now is below average (until July, Aug not yet reported)
- The two PMI data are below the avg over the past 3 years but do not at all signal any abrupt halt in the Chinese economy

Most surveys have improved/stabilised as the authorities are stimulating activity

Consumer confidence is still sky-high and businesses sentiment is not weak





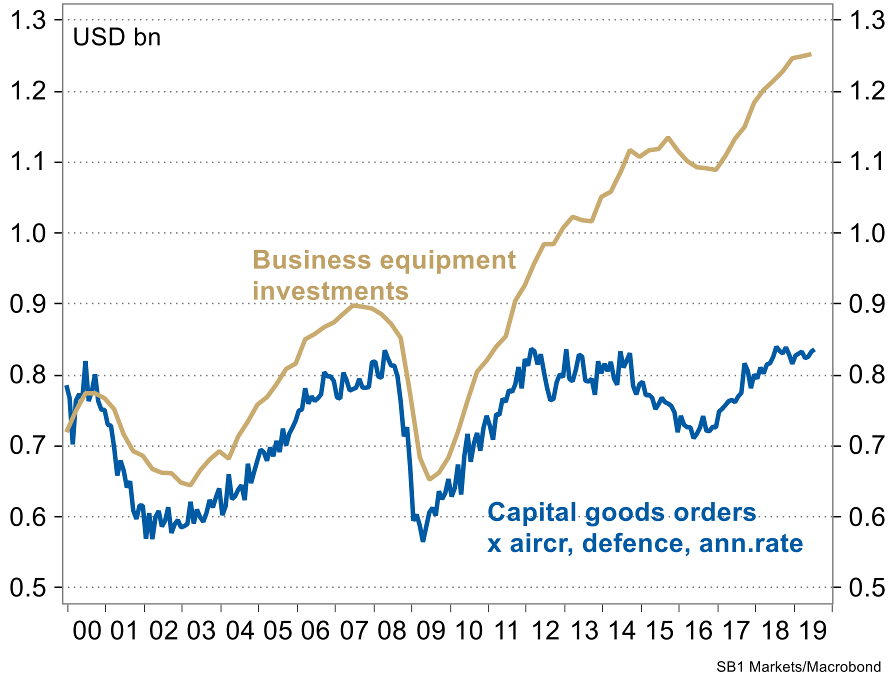


- Trade was worries may explain the slowdown in China through 2018 but the credit tightening in 2017 (especially vs. the shadow banking marked), that dampened credit growth substantially is probably more important. The credit impulse (the 2. derivative) turned negative, and the economy slowed, as usual
- The authorities are pushing the credit accelerator. The credit impulse has turned upwards and is back in neutral. In addition, fiscal policy has been turned expansionary, both by cutting taxes and increasing expenditures, especially in infrastructure (equalling 1% of GDP)

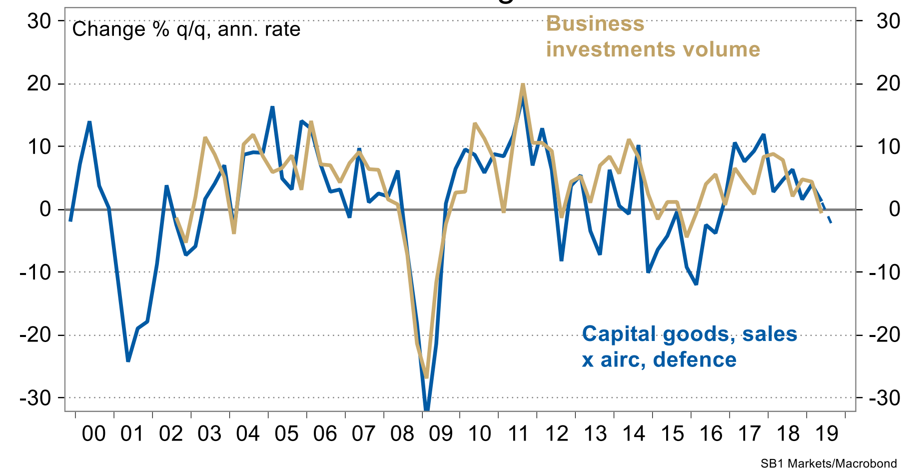
Capital goods orders/sales signal just a mild decline in investments into Q3

Core investment orders rose marginally in July (June revised down), sales edged down

USA Investment goods orders



USA Investment goods sales

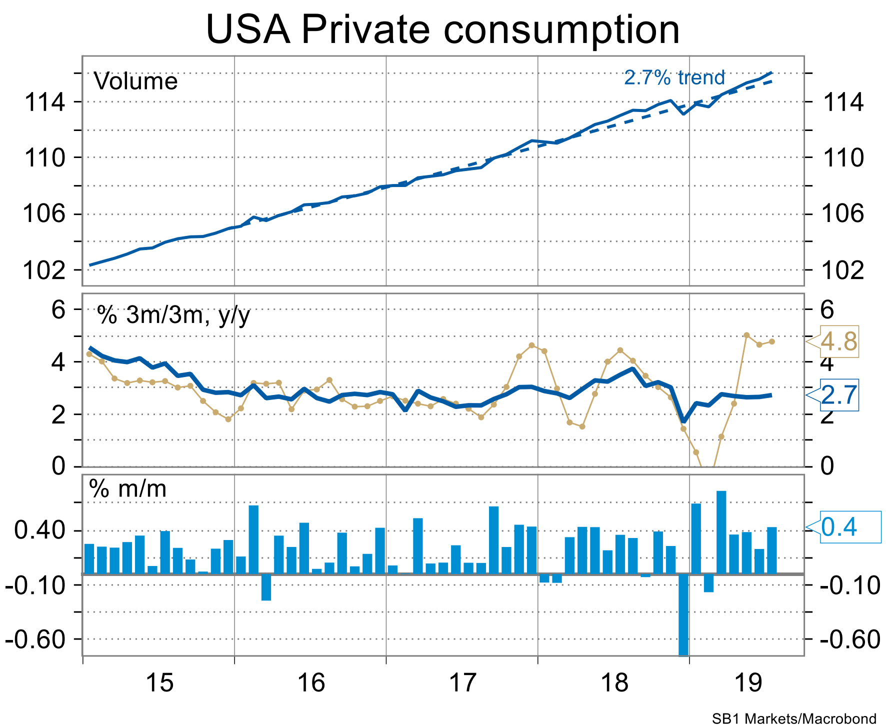


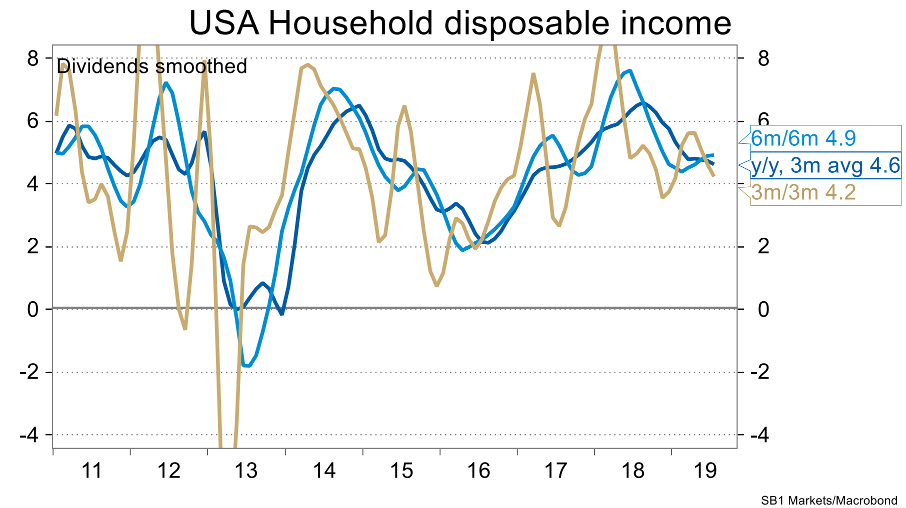
USA Investment goods orders

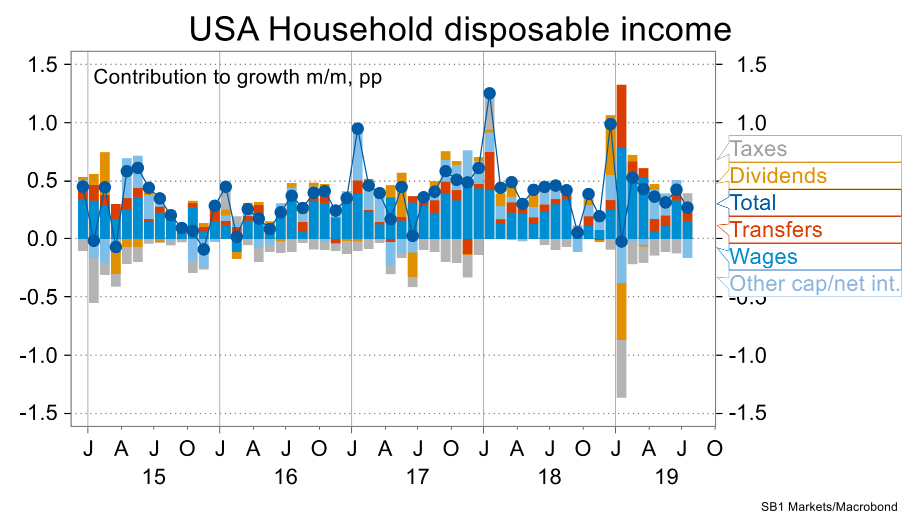
- Investment orders (core) increased by 0.4m/m in July but June was softer than previously reported, 0.9% vs 1.5%. Underlying growth is modest, up 1.3% (3m/3m), and they are flat since last summer
- Sales fell 0.7%, and are probably slowly on the way up, but the July level is below the Q2 average, so far indicating a marginal decline in business investments in Q3 (as did a decline in imports of investment goods in Q2) – but no abrupt setback
- Unfortunately, the PMI is pointing to softer order inflows

Private consumption still going strong into Q3, but income growth is slowing

Consumption rose 0.4% in July, underl. growth close to 5% - above income growth, savings down



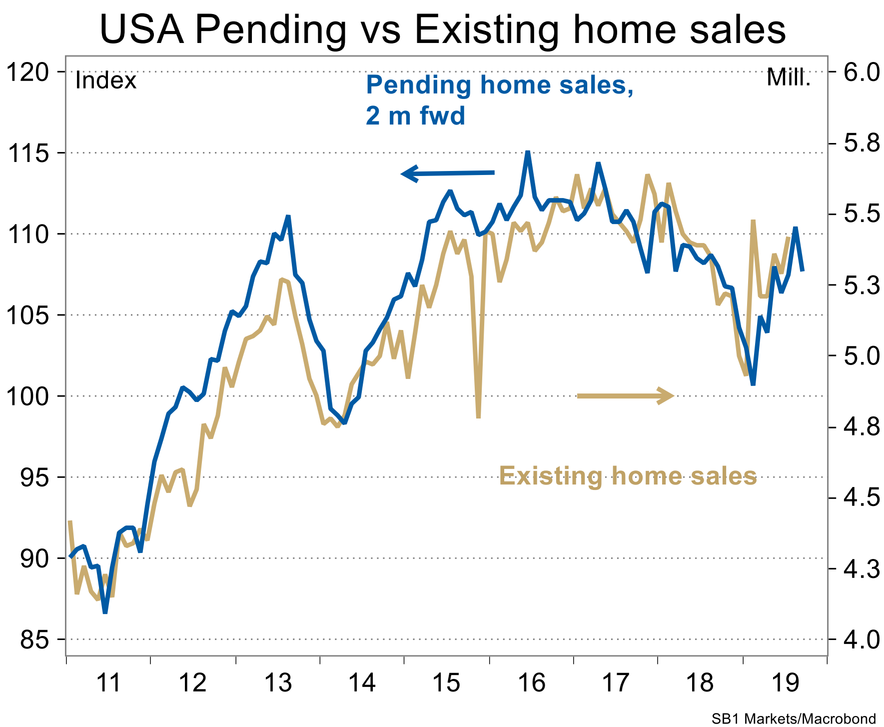


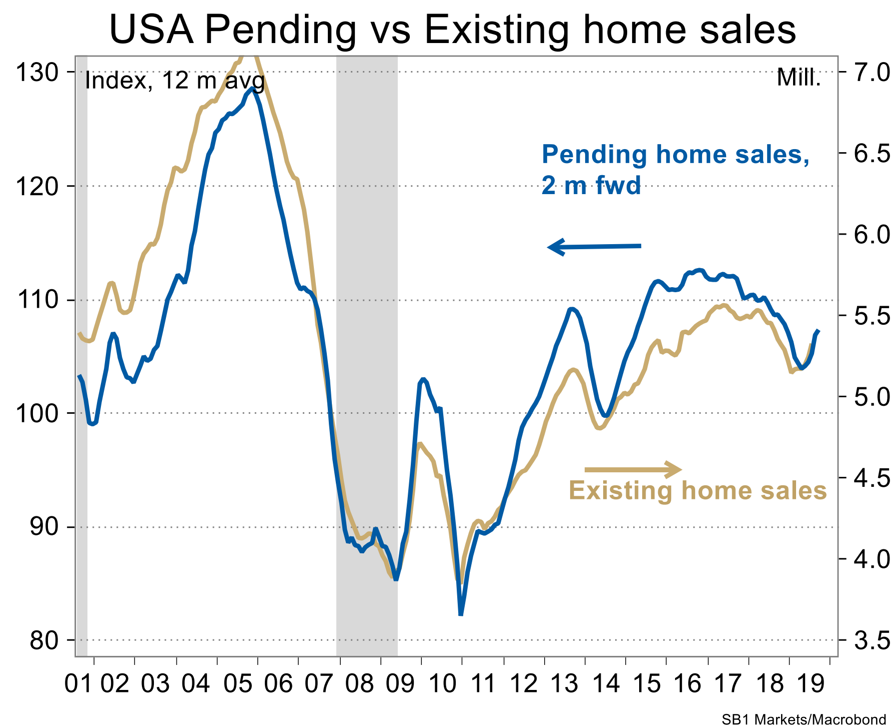


- Private consumption grew 0.4% in July, 0.1 pp weaker than expected. Consumption is up 4.8% 3m/3m, Q3 is off to a solid start, following the 4.7% growth in Q4 (real terms)
- Households' nominal disposable income rose 0.2 m/m, following a strong 0.5% print in June. Underlying growth slowed to 4.2% 3m/3m, annual growth marginally down to 4.6%. Total wage & salary income is up 3.4% (volatile data)
- The savings rate is high but has fallen to 7.7% July from 8.8% in Dec, funding 2 pp growth pace in cons. (more half of total)

Pending home sales down in July but trend is still strong

Pending sales down 2.5% July, are up 7% from the Feb trough – still 5% below the '16/17 level

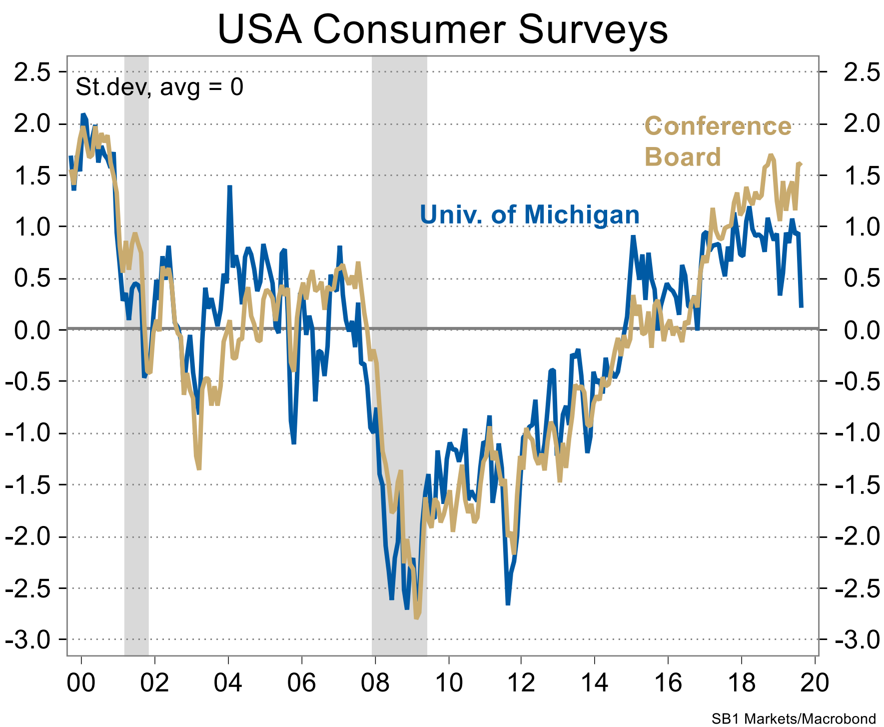


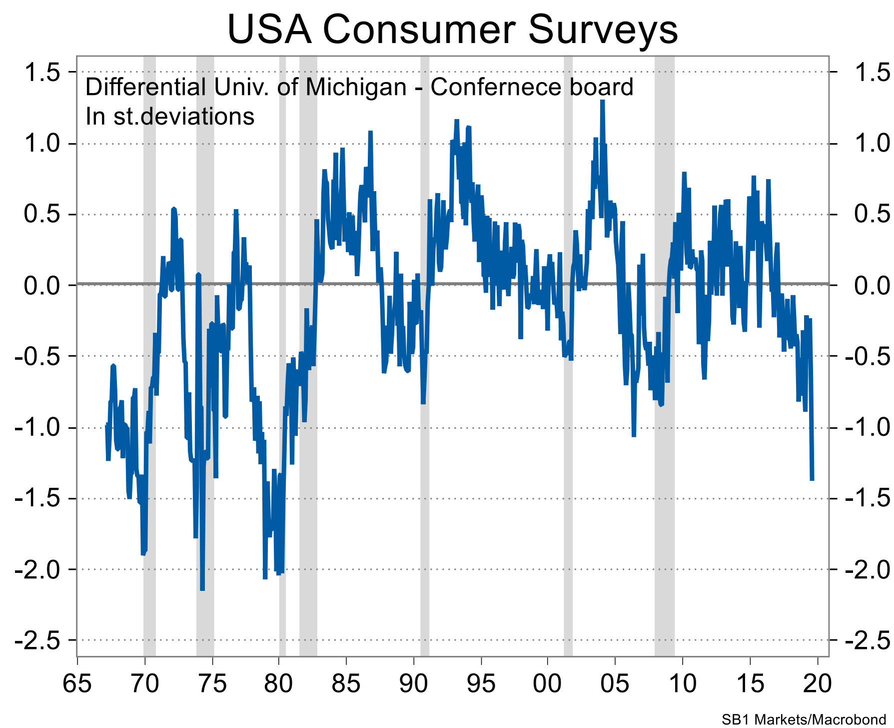


- Pending (existing) home sales were expected unch
- Pending (agreed) and actual sales are usually quite well correlated, with pending leading 1 -2 months on the actual transactions. Both have been recovering so far in 2019
- Most housing market indicators are pointing upwards, probably supported by a steep decline in mortgage rates – and none are pointing down

Mixed consumer surveys, Conf Board's kept up, UoM fell even more than 1st rep.

Conference Board just marg. down, and better than expected. However, U of Mich fell 'dramatically'



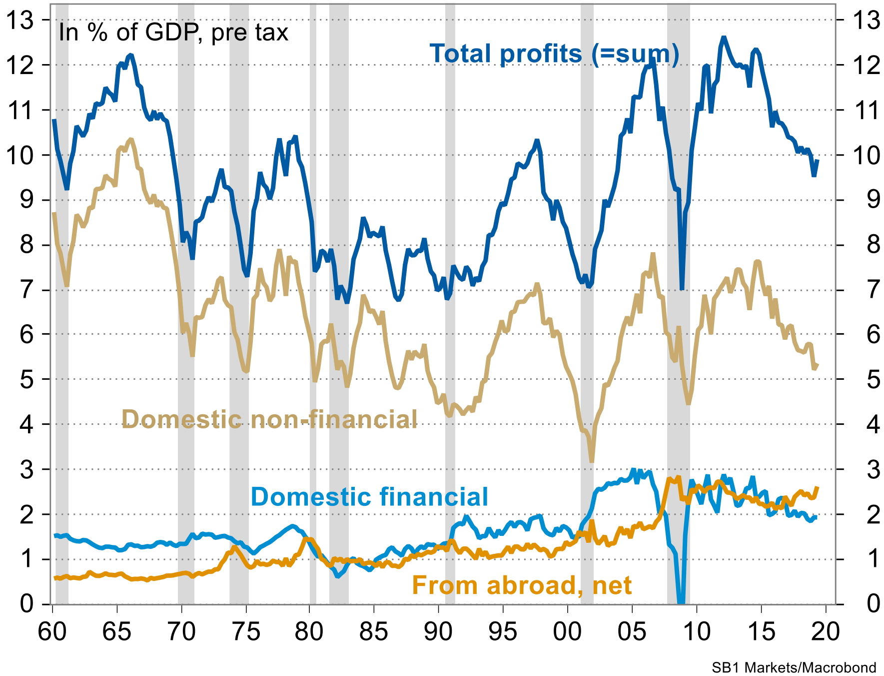


- Conference Board's consumer confidence index fell just marginally (-0.7 p) to 135.1 in August, after soaring in July. The index is at the 5th highest level since 2000, in contradiction to the recessions fears which is spreading across market
- University of Michigan's sentiment survey fell even more than first reported, down to 88.8 vs. the initial estimate at 92.1, down from 98.4 in July, a 0.7 st.dec decline (a 1/6th of a normal cycle). The setback was the largest since Dec 12, and of a size that normally only happens once every 3 – 4 years (the 17th largest since 1960). The differential between the two surveys is unusually large. The UoM index may be more sensitive to downturns in financial markets, and is leading the CB survey somewhat. And 'something' happens when the cycle is maturing and it is heading towards a recession, check the chart on the lhs. As a recession warning, the 'spread' is not that bad
- Still, both surveys are above their long term averages and they do not signal a sudden halt in consumption. But the chart above…

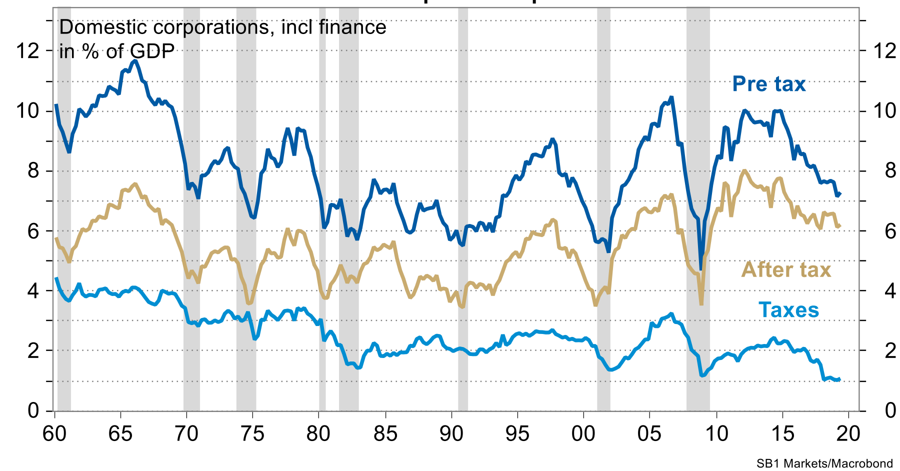
Profits up in Q2 but have flattened – and are falling sharply in % of GDP

Domestic corporate sector after tax profits are still above average, just due to the tax cuts

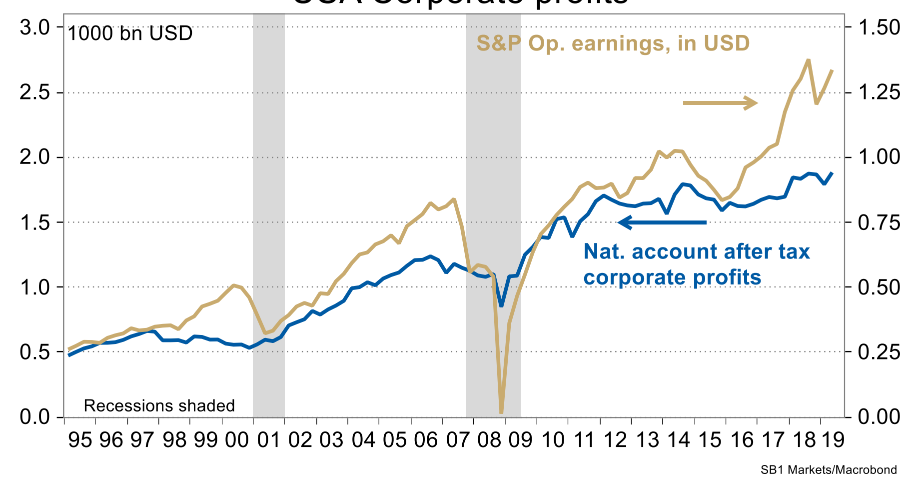
USA Corporate profits



USA Corporate profits



USA Corporate profits



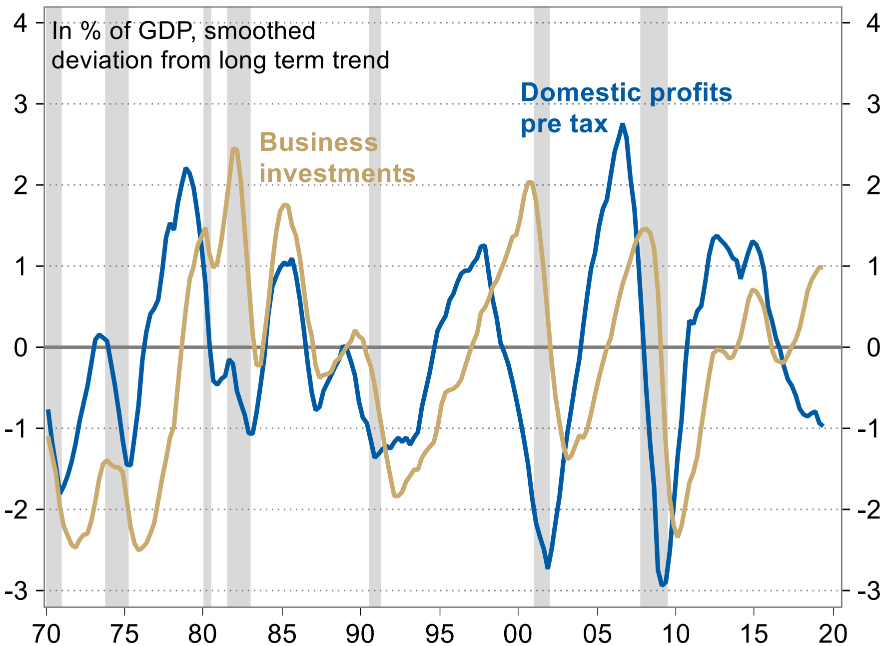
- Corporate profits were revised sharply down in the annual revision of National Accounts
  - » The Q1 total pre tax profit share was revised to 9.5% from 10.8% - and the profit share is trending sharply down. Household income and savings have been rev. up
- Total profits rose 5.3% in Q2, mostly due to higher profits from US companies' activities abroad (minus foreign in the US)
- The after tax profit rate for companies operating in the US ('domestic corporations') is still above average but just because corporate taxes have been cut sharply recent years

S&P 500 companies are reporting much higher growth in earnings than Nat. Acc. are able to detect. We have seen such discrepancies before, and so far S&P profits have yielded the following years, during recessions…

Profits down – and investments will follow suit, as usual?

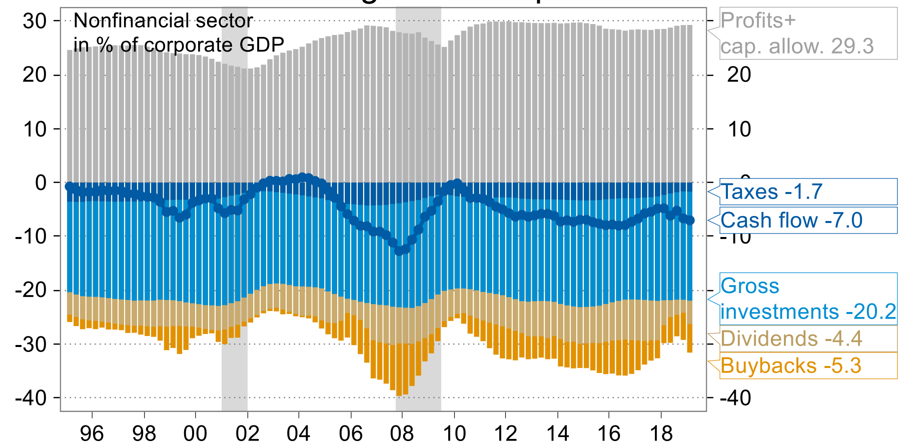
Probably, investments are almost always lagging profits. The cash flow is deep in red, and debt high

USA Profits & investments



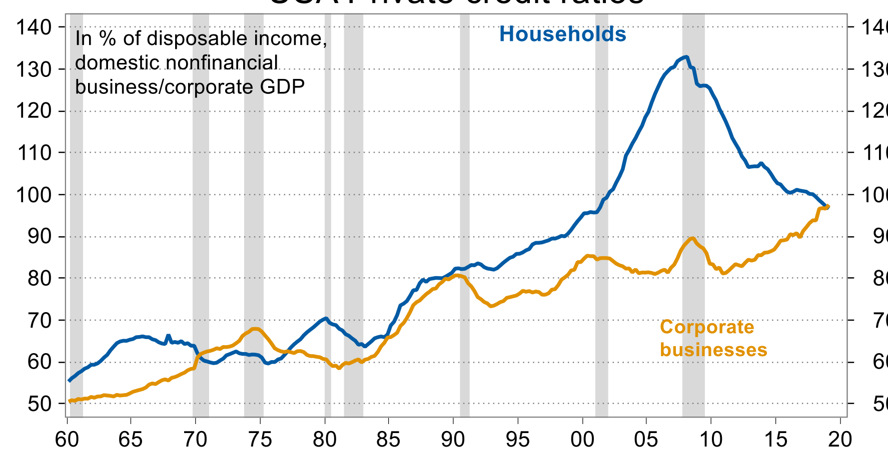
SB1 Markets/Macrobond

USA Funding of the corporate sector



SB1 Markets/Macrobond

USA Private credit ratios



SB1 Markets/Macrobond

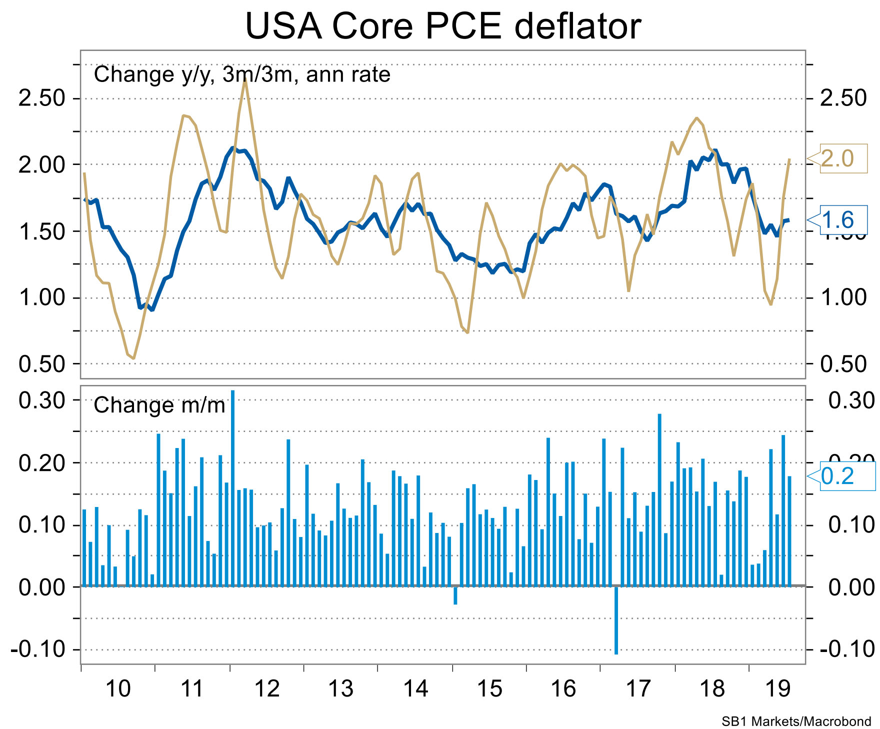
- Business investments are not super high but high, while profits are below a normal level
- The non-financial corporate sector cash flow is negative, by almost the same amount as the companies spend on stock buybacks
- The debt/value added rate has climbed steeply recent year. Without buybacks, the debt ratio would have fallen sharply the past 15 years, to close half the actual level

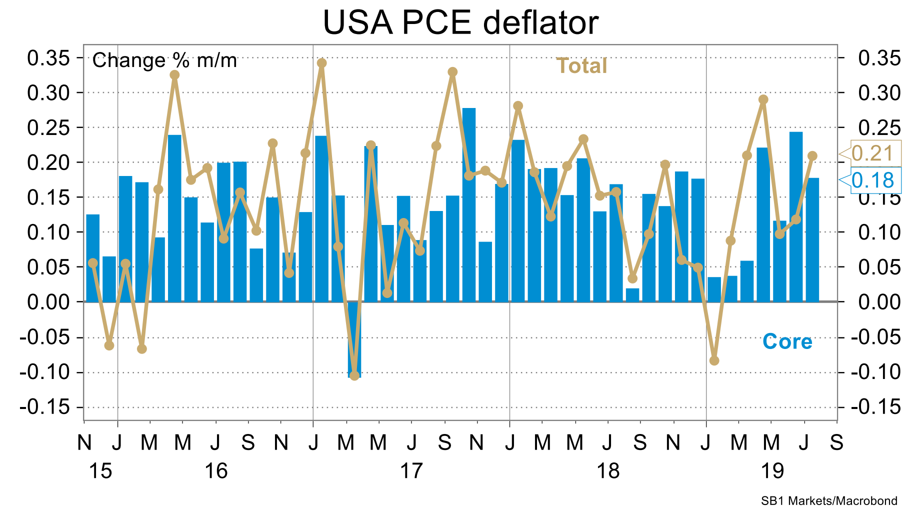
The upper right chart has not incorporated the downward revised corporate profits

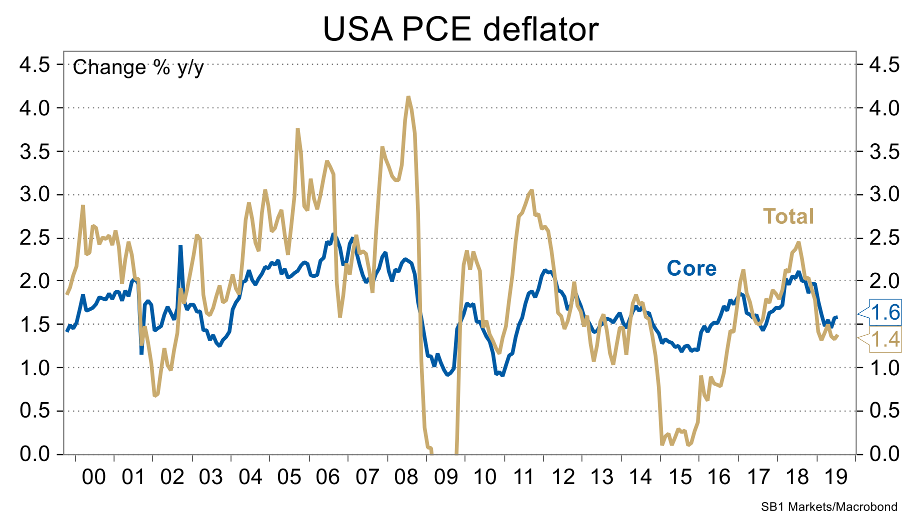
SpareBank 1 MARKETS

Core PCE y/y inflation remains at 1.6, underlying growth picks up

Core PCE deflator flat at 1.6% in July, 0.4 pp below Fed's target. Total PCE inflation at 1.4%



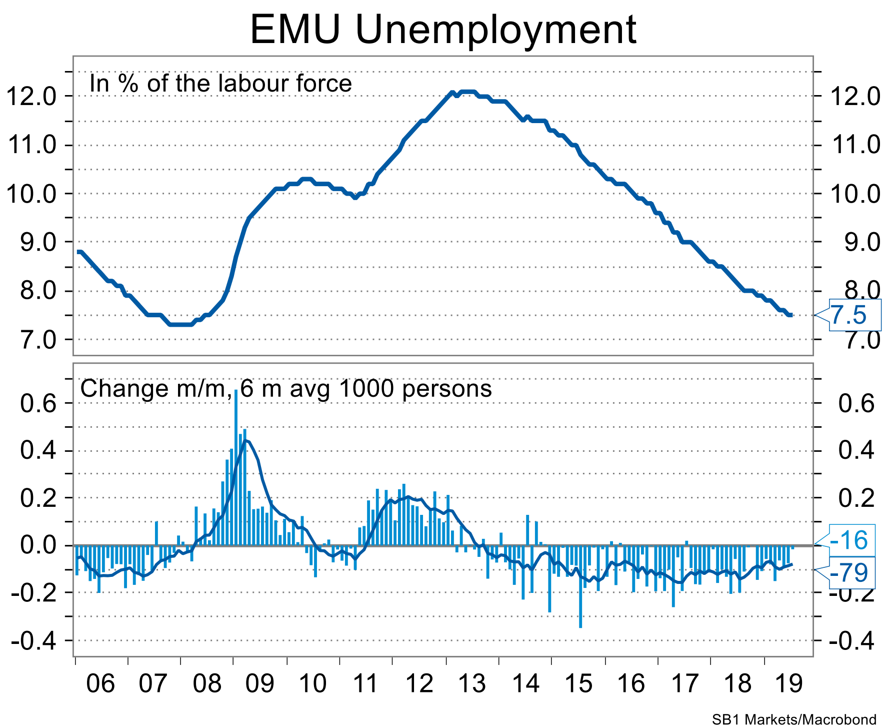


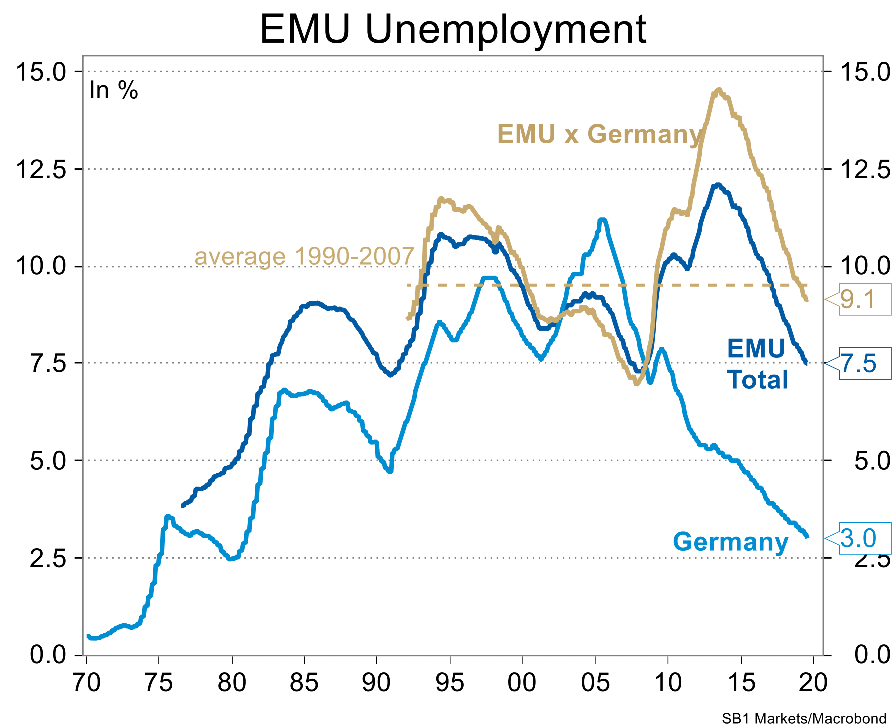


- The core price deflator rose by 0.2% m/m July, as expected. The annual rate was unchanged at 1.6%. Still, underlying growth (measured 3m/3m) accelerated to 2%. The annual rate is low due to low monthly inflation in Dec/Feb
- Total PCE inflation inched up to 1.4% y/y, following a marginal downward revision of June. Total inflation has retreated as energy prices have come down. Good for real income growth
- PCE has been running 'visibly' below Fed's price target at 2% for 6 months. Small changes in inflation has never been important for Fed's rate setting – but it can be used as an 'excuse' for a cut, like now

Unemployment flat in July, the underlying decline may be slowing

Unemployment flat at 7.5% in July, just 16’ less unemployed

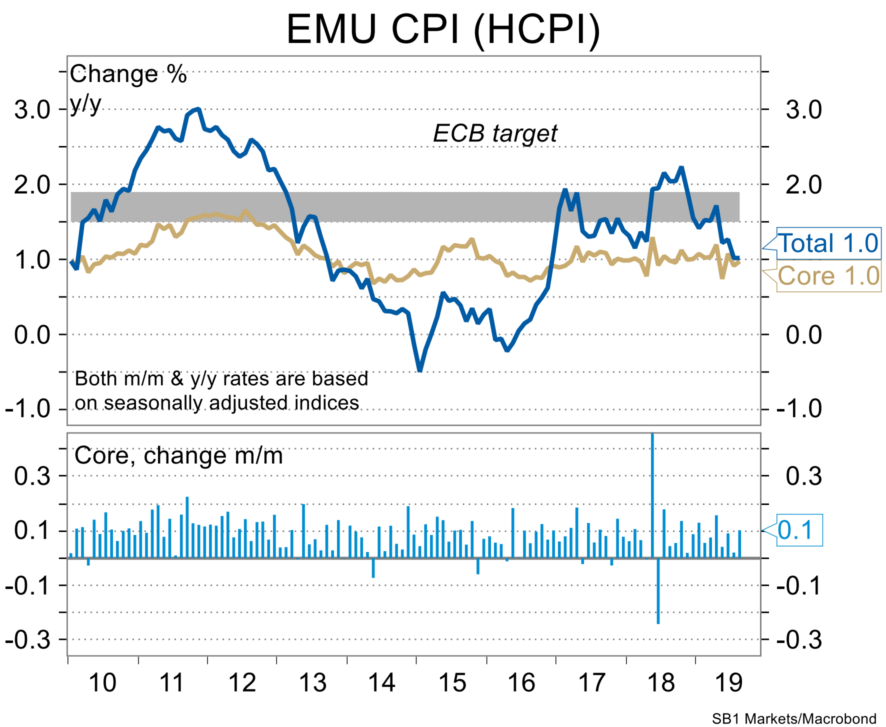


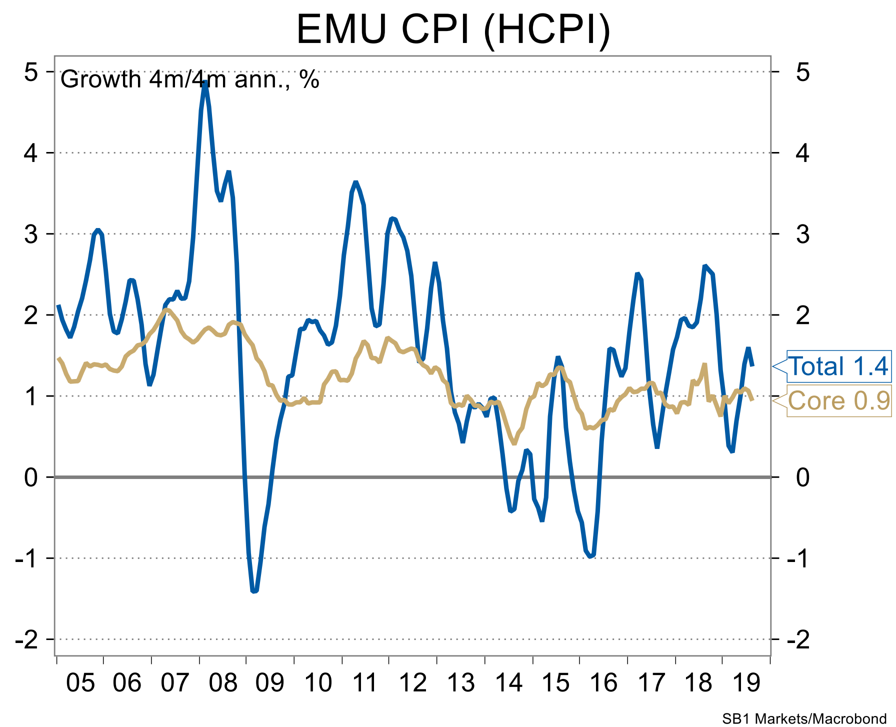


- The unemployment rate was flat at 7.5% in July, in line with expectations. The number of unemployed fell by just 16’ persons, a modest decline vs the 6 m avg at close to 80’. The long term trend is still downwards but the pace has declined somewhat
  - » Unemployment has been declining in spite the soft patch that the Eurozone is in (some sectors, at least). Unfortunately, unemployment is not a leading indicator, it is at best a coincident one. <u>Nonetheless, the decline in unemployment rate during the economic slowdown may also mirror that other sectors so far are persistent to the dip in manufacturing, as the PMIs and some other surveys are reporting</u>
- Unemployment in total EMU is well <u>below</u> the 1990-2007 avg, and it has fallen below the average in EMU ex Germany too
  - » In Germany, the unemployment rate ticked down to 3.0% in July, the lowest level in almost 40 years

Core CPI inflations remains meagre, one inch up to 1.0% in August

Core inflation rose 0.1 p in August, total CPI was flat at 1.0%, bolstering the case for the ECB to act

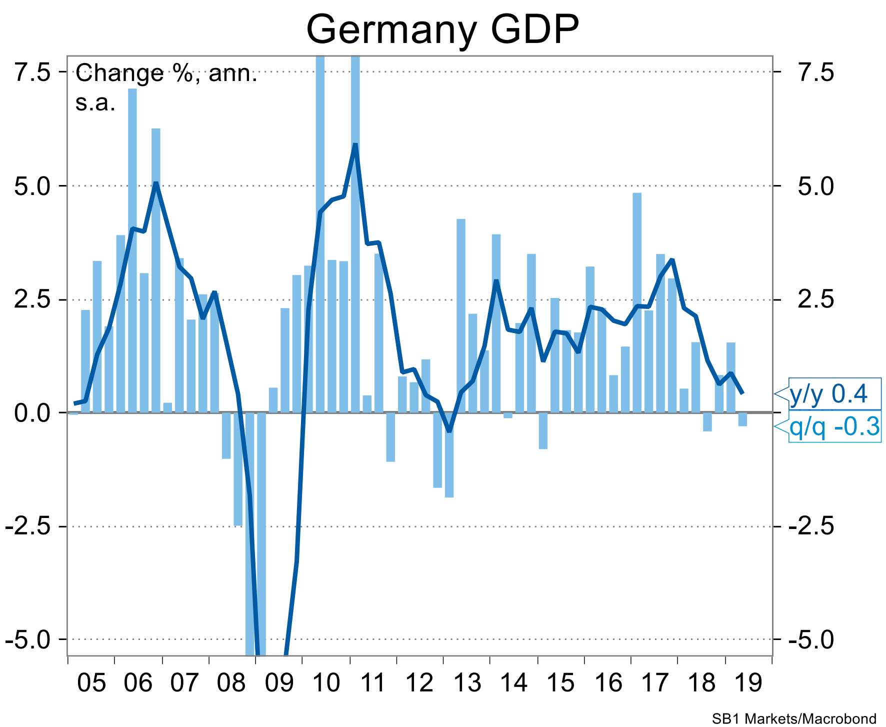


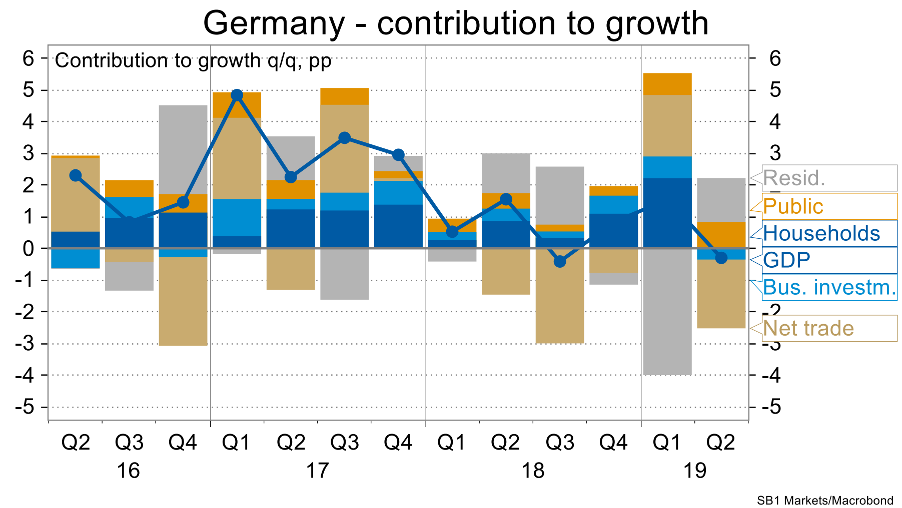


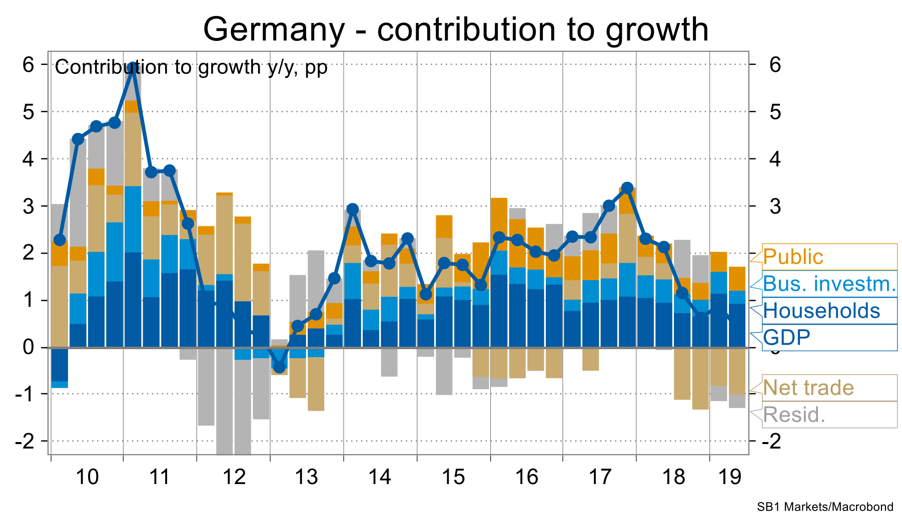
- Core CPI rose 0.1% m/m in August. The annual rate bounced back to 1.0%, up from 0.9% in July and in line with expectations. Core inflation is trending flat (and even downward recent months) and growth measured 4m/4m is low
  - » Subdued inflation is increasing the pressure on ECB to step up support
- Total CPI growth was unchanged at 1.0%. The oil price decline in the spring has sent total inflation down from above 1.5%. We expect headline inflation to decline further the coming months, to well below 1%

Q2 details are not promising; muted household demand, business invest. fell

The major drag in Q2, and last y was exports, and other parts of the economy are just not shining







- GDP fell 0.3% annualised in Q2 (-0.1% not ann.), unchanged from the first report. Growth y/y has slowed to 0.4%, with a negative drag from net trade a 1 pp.
- The details note zero contribution from household consumption/housing inv. from a strong Q1, and a modest decline in business investments. Only public demand and inventories/residual lifted growth! The major drag was exports
- Unfortunately, business surveys do not signal any upswing

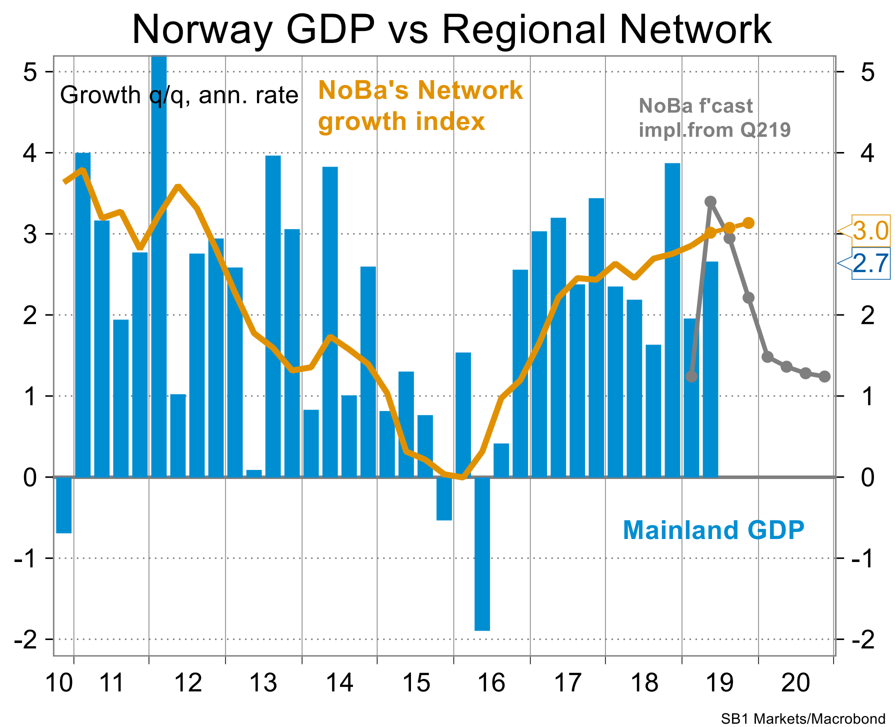
Guess what, German trade is closely correlated to…

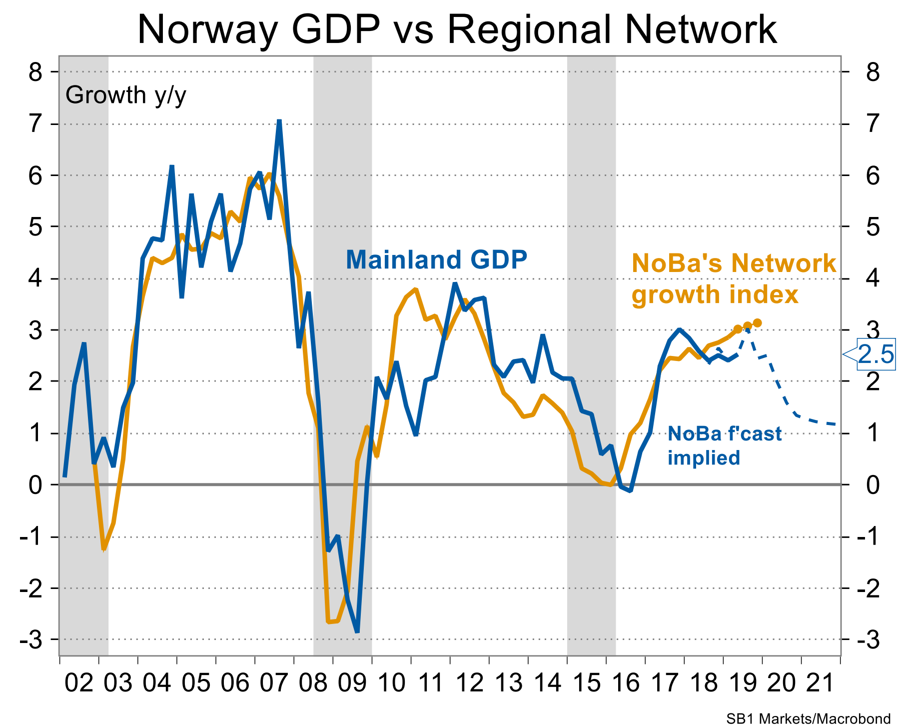
.. global trade. Now, both have stagnated due to trade war/Brexit uncertainties and a mature cycle

- Both German and global trade are highly correlated to German industrial production. Thus, either exports will have to follow production down or production will rebound? The prior is most likely, given signals from PMIs/other surveys

Mainland GDP up 0.7% in Q2 but details do not point to a very bright outlook

GDP rose 2.7% q/q annualised and 2.5% y/y. A tad weaker than expected, not enough to curb NoBa

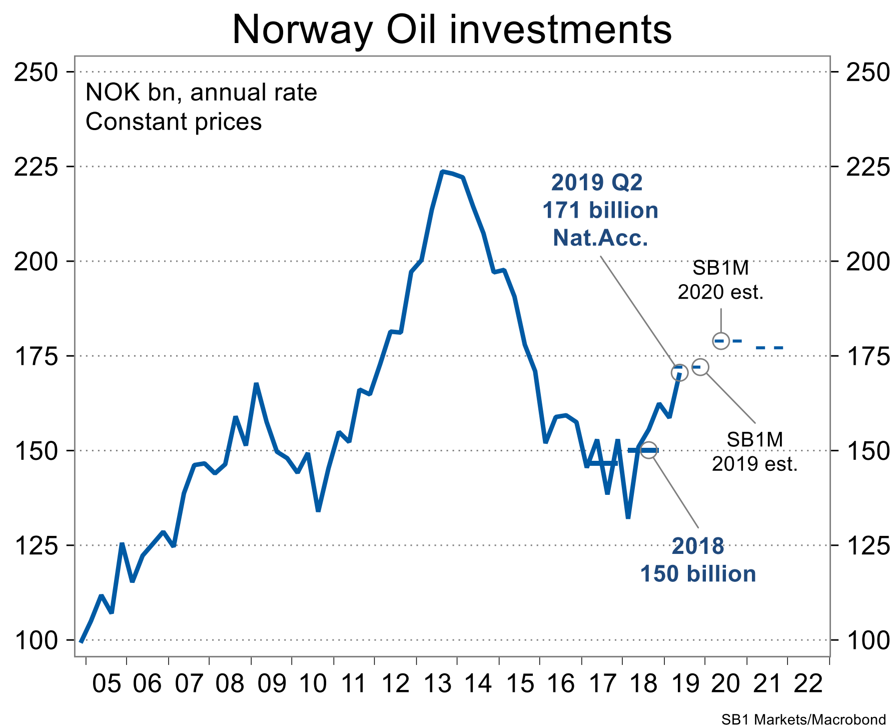


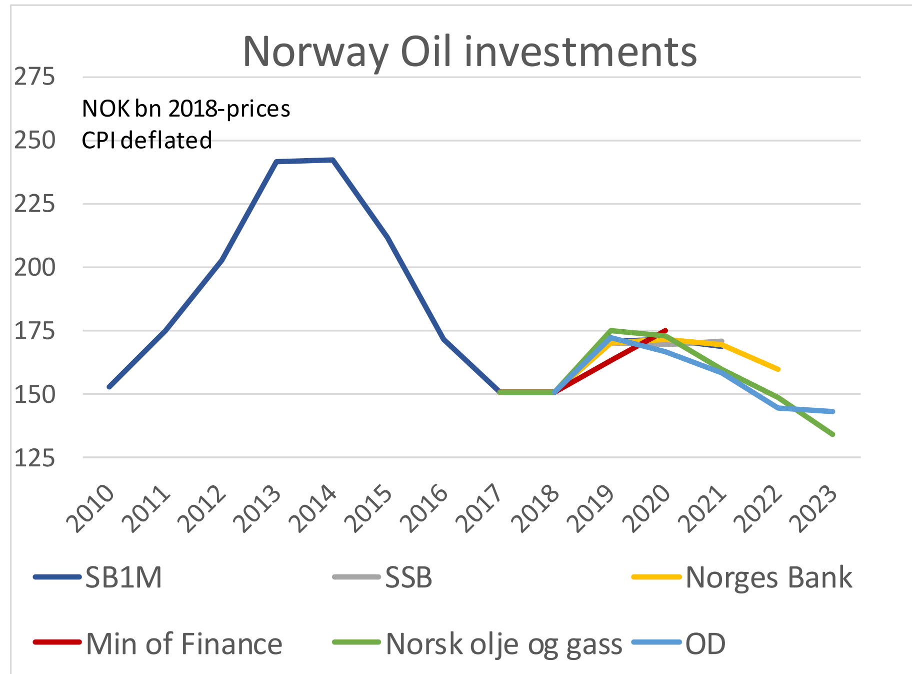


- Mainland GDP rose by 0.7% q/q (2.7% annualised) in Q2, we, consensus and Norges Bank all expected 0.8%. The annual rate inched up to 2.5%. Moreover, Q1 was revised up by 0.2 pp to 0.5%. In spite the solid Q2 figure, the details were not that upbeat;
  - » Private consumption rose moderately, as expected, while Mainland business investments surprisingly dragged growth down (again). Oil investments soared, marginally less than we f'casted. Housing investments rose modestly. However, government demand and inventories were the major growth contributions, will not last. Mainland net exports fell and dampened GDP growth
  - » Solid employment, up 1.7% annualised, while productivity growth is slowly picking up, from a low level (0.9% in Q2). Wage inflation was flat at 3.3%
- Growth is above trend and cost inflation is trending up. The solid GDP figure is an argument for another Norges Bank hike, however, other data (labour market, Regional Network, financial markets and of course the global outlook) are more important. <u>For now, we stick to our view that Norges Bank will hike on September 19, which may be the last one, for a while</u>

Oil investments: The upside is not that large, peak in H2 2019?

Investments rose in Q2 and the level is some 4% below our 2020 estimate



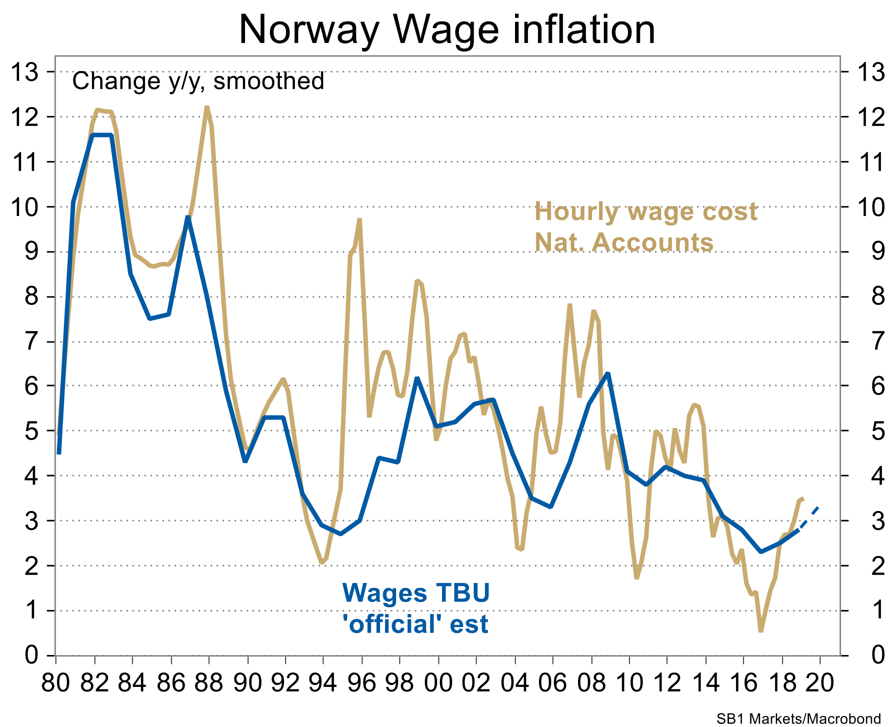


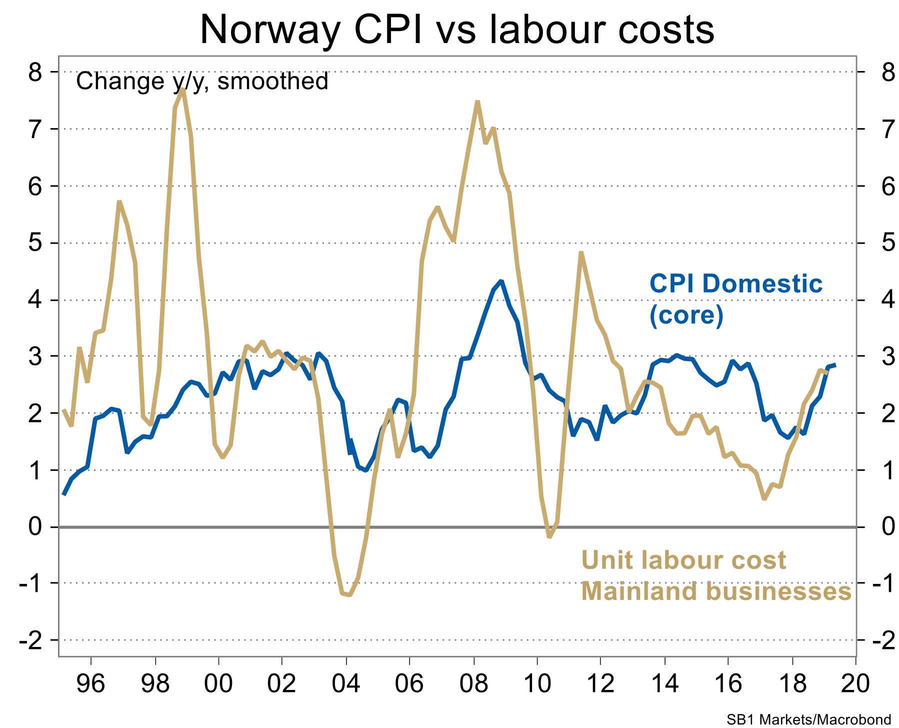
- Oil investments increased by 7.5% q/q in Q2, to NOK 171 bn. Investments are now 14% above the average 2018 level, which is just a fraction below our 14.5% 2019 growth f'cast. The investment level in H2 will be some few per cent above the Q2 level, and the (implied) H2 level is close to our 2020 f'cast (+4% from 2010). **Hence, the surge in oil investments is now (in H2) more or less behind us**
  - » If our assumptions are correct, contribution to growth from the oil investments will be close to zero from Q4
  - » No doubt, the oil price will influence the investment level from 2020 onwards, as more projects may be added

SpareBank 1 MARKETS

Wage inflation and cost inflation on the way up

(Volatile) hourly wage cost up 0.1 pp to 3.5% in Q2, unit labour cost inflation at 2.7%+ (smoothed)



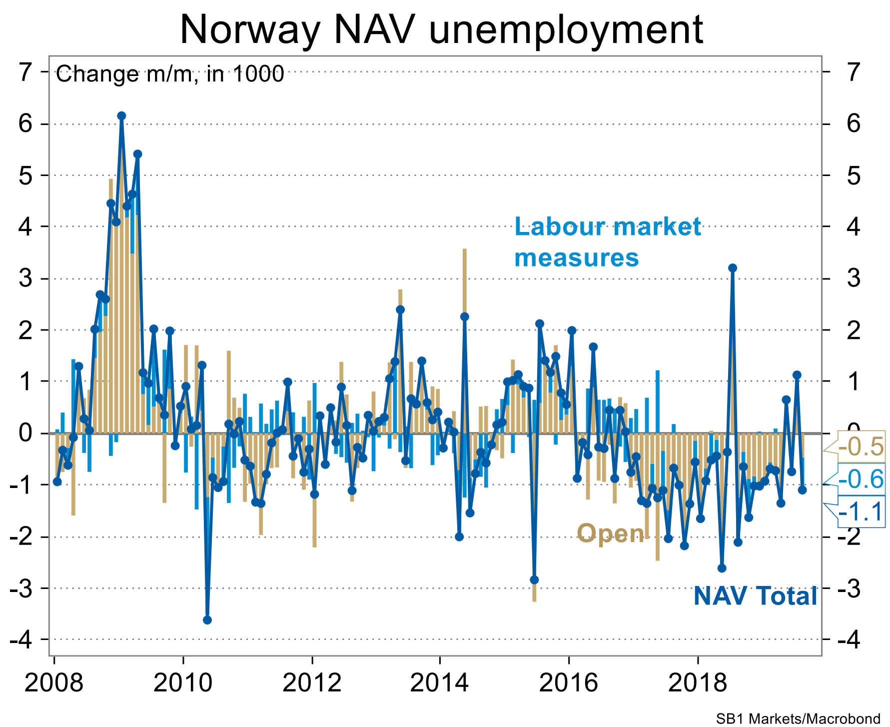


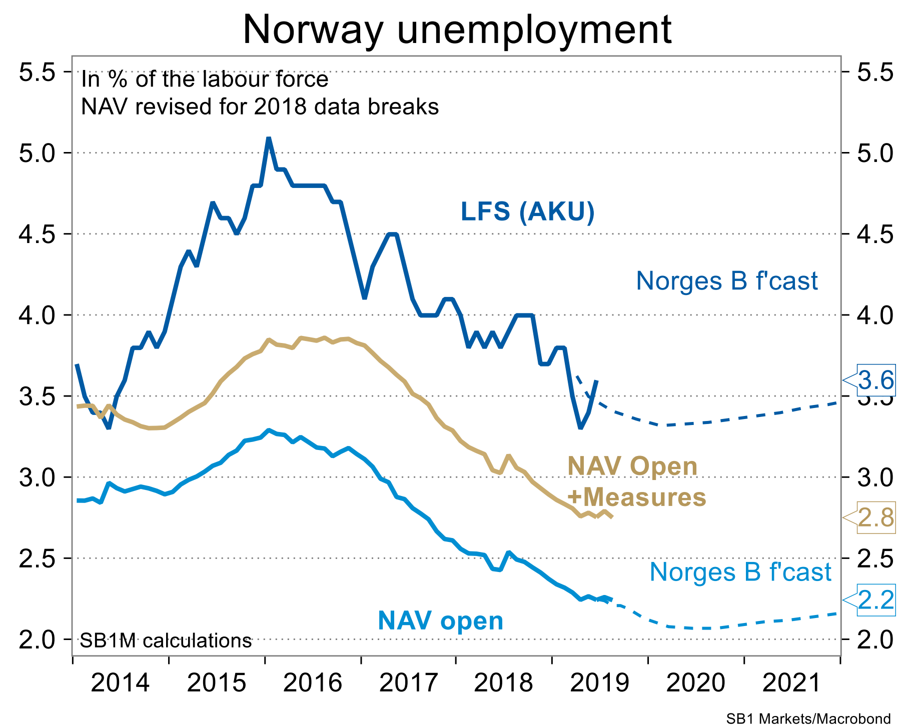
- Hourly wage costs bottomed out in Q2 2017 and are back at the 2014 level, still below ‘normal’ Norwegian wage inflation

SpareBank 1 MARKETS

NAV unemployment down in August, a reassuring sign

NAV total unempl. fell by 1.1' persons, following July uptick. Still, some signs of softer labour market

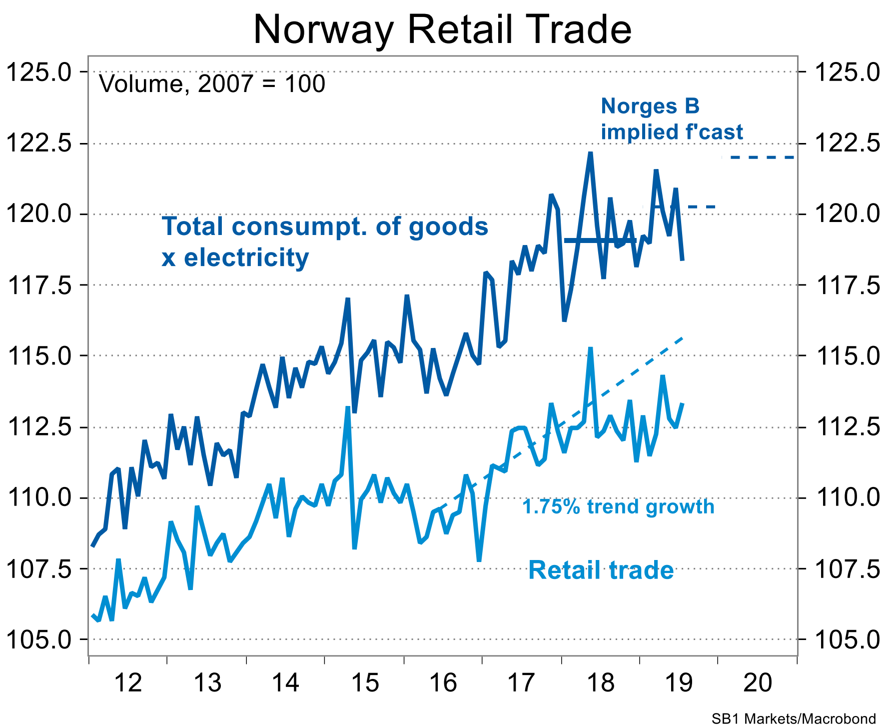


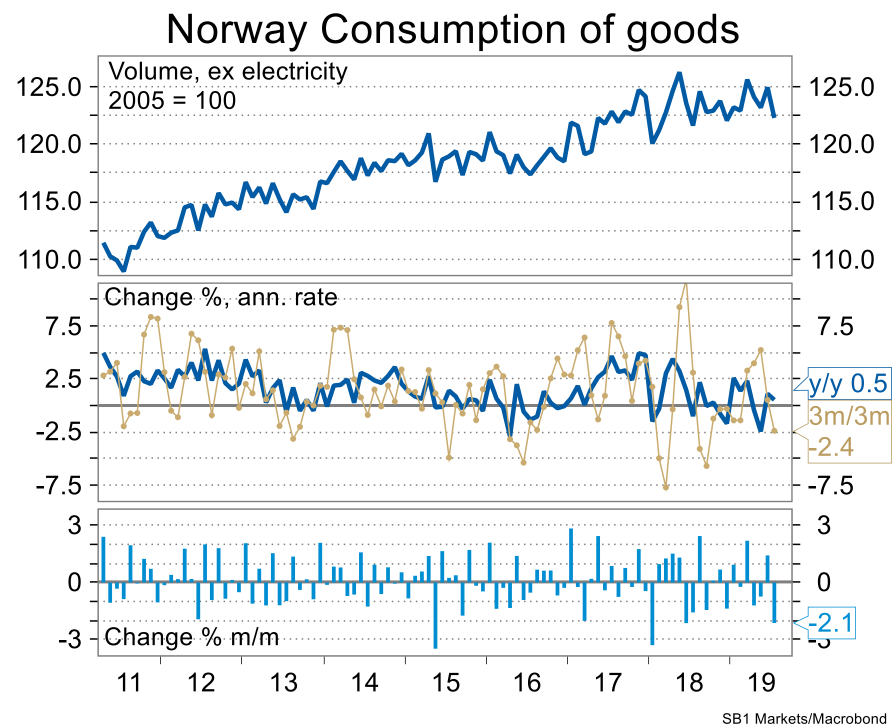


- NAV open unemployment fell by 500 persons in August, total unempl. (incl measures) by 1.100. The decline came after an uptick in July (and May), and the 3 month avg is down by just 240 persons. Unemployment is still declining, although at a softer pace. The open unempl. rate inched down to 2.2%, marginally below NoBa's f'cast (2. decimal). Some other signs of labour market softness:
  - » New jobless claims up in August, a higher no of announced layoffs recent months, and fewer new vacancies
- LFS unemployment is trending down and employment is still growing. We do not expect a sudden shift at the labour market at this point and business do not report any visible weakness. Nonetheless, a gradual softening is expected, by NoBa and us
- We stick with our view that Norges Bank will hike in September

Retail sales improved in July, trending modestly up?

Retail sales rose 0.8%, underlying growth up 0.6%. Auto sales dragged total consumption down

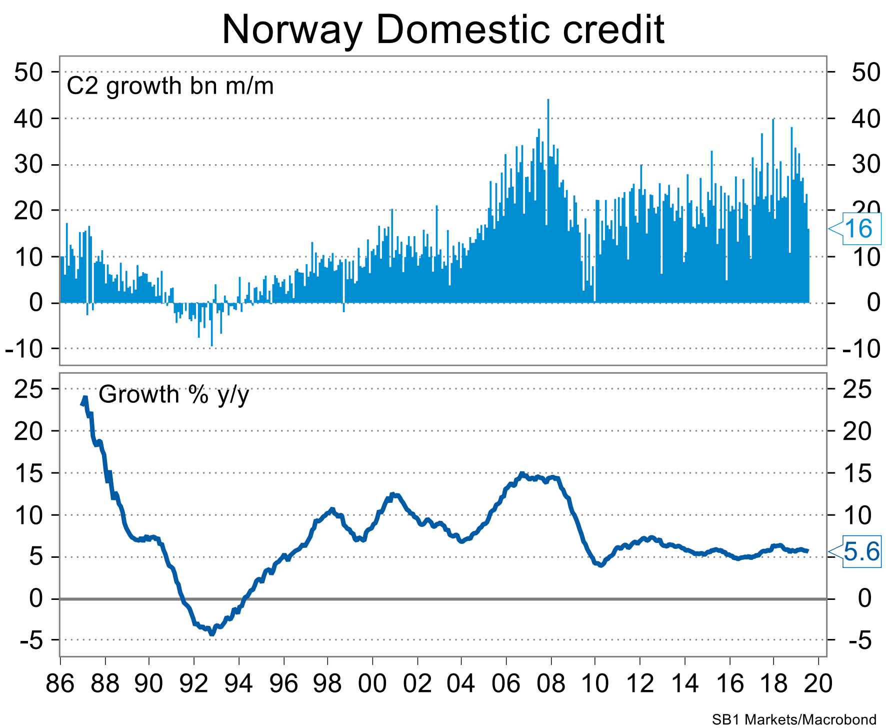


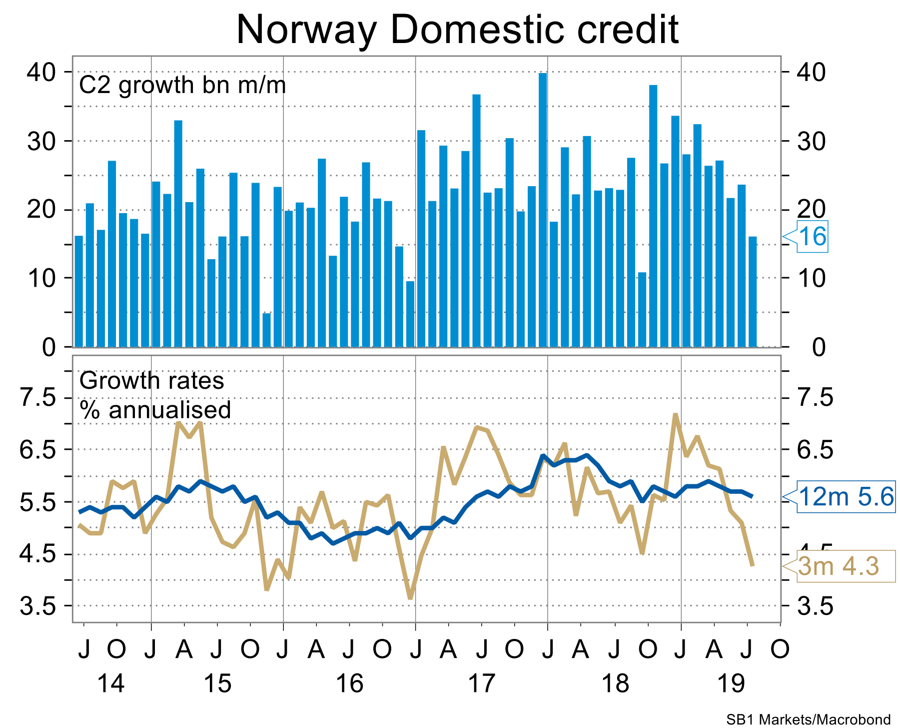


- Retail sales volume (ex auto) increased by 0.8% m/m in July, close to our f'cast at 1.9% (consensus 0.4%). Sales are certainly not thriving, yet, the trend is most likely slightly upwards from the 2018 level. The speed so far into Q3 is 0.6%. The annual rate is modest at 0.9%
- Total consumption of goods (ex electricity) dropped 2.1% m/m, following a strong June. The downswing is solely driven by a retreat in auto sales, which are volatile from month to month. Underlying growth is up 0.7% (measured 3m/3m) but Q3 is off to a weak start. We stick to our expectation that subsiding price inflation will support volume growth the coming months
- Total consumption is anyway at Norges Bank's 2019 (implied) estimate, hence, household's goods demand is no argument for abandoning the hiking plans

Credit growth down to 5.6% in July, due to student loan -> grants

Easing corporate credit is driving total credit growth down (after a spike in '18), households growing steadily





- Total domestic debt (C2) rose by just NOK 16 bn m/m in July, the lowest m/m growth in a year – due to student loans (see below). The annual rate inched down 0.1 pp to 5.6%, we expected up to 5.8%. Average growth over the past 3 months slowed to 4.3%, from 6% some months ago. Still, overall growth has held steady since 2013
- Household credit growth cooled in July and the annual rate fell 0.2 pp to 5.3%. However, the whole decline was due to a changed period for conversion of student loans to grants (usually in Nov, now in July). <u>So far, there are no indications of a pullback in household loan demand following the interest rate hikes</u>
- Corporate credit growth has slowed this year, after a surge in late 2018. The annual rate is steady at 5.8%, below our f'cast

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	Mixed prelim. Aug PMIs, we estimate a 0.2 p decline in the global composite PMI, to 51.5. The PMI points to GDP growth at some 3%. Global manuf. PMI probably rose but remains below 50
China	The governments' stimulus measures may have stabilised the economy, and surveys and data do not point to any swift turn of growth momentum. The invest/GDP ratio is still sliding down. 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. Exports to US approx 2% of GDP, and a (so far) 10 % decline here is manageable. **However, a full scale trade and even more a tech war will hurt the Chinese economy**	The Aug PMIs more up than down, following weak actual data in July (but June was excellent). In sum, China is not collapsing at all
USA	Growth has slowed, from well above trend. The employment rate is still trending up, and unemployment down while inflation is just marg. below target. No serious overinvestments but most sectors at/above trend but corporate debt is high. Business investments has weakened amid weaker growth in profits, and trade war uncertainty. Recent consumption data are solid, halfway funded by s lower (but still unusual high) saving rate). Housing mostly positive. Fiscal stimulus continues in '19/20 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 more support. **Risks: Trump/trade/business investments**	Durable goods orders have flattened out but do not signal an abrupt decline in business investments. Strong consumption in July. Core PCE inflation at 1.6%, below target. Consumer confidence mixed, UoM sharply down. Initial jobless claims still very low. House prices up just 2%
EMU	Growth has slowed and manufacturing data are worrying while services remain resilient. The labour market is still tightening, and labour cost infl. is back to a normal level. Investment ratios on the way up but are not too high, overall. Credit growth is accelerating, but still muted. Household savings are high, still consumption has kept up well. Policy: ECB has turned dovish but has not that much ammunition left, barring a huge QE. Fiscal policy debate has turned. **Risks: Trade war (but less risk for a US/EU war after G7). Italy. Weak short term data signals a substantial further slowdown risk**	EU economic confidence survey a tad up, still 'too' upbeat. Bleak German GDP data and the Ifo survey deteriorates. Unemployment slides down but not further in July. CPI inflation remains low, at 1%
Norway	Growth is still above trend but may soon be peaking. For now, unempl. declines further (some soft data recently, though!). Wage inflation is accelerating. Oil investments are peaking in H2. Mainland business inv. not low anymore, will probably slow in '20. Housing investments have bottomed, for now. Electr. prices have taken the headline CPI down but core still above target. Credit growth still above income growth, is spite of heavy regulations. **Risks: Debt, housing. A harsh global slowdown**	Q2 Mainland GDP came in 0.1 pp below f'casts, at 0.7% q/q. Credit growth is slowly decelerating, households steady recently. NAV unemployment declines. Retail sales rebounding in July, modest growth

The Calendar

In focus: Final PMIs/ISM, China exports & imports, US nonfarm payrolls, Fed's Beige Book

Time	Country	Indicator	Period	Forecast	Prior
Monday Sept 2					
08:30	SW	PMI Manufacturing	Aug	51	52
09:00	NO	PMI Manufacturing	Aug	51.4	48.4
10:00	EC	Manufacturing PMI	Aug F	47	47
10:30	UK	PMI Manufacturing	Aug	48.4	48
Tuesday Sept 3					
08:00	NO	Job Vacancies	2Q		2.5%
15:45	US	Markit Manufacturing PMI	Aug F	50	49.9
16:00	US	ISM Manufacturing	Aug	51.2	51.2
17:00	WO	Global Manufacturing PMI	Aug	(49.3)	49.3
Wednesday Sept 4					
02:30	JN	PMI Composite	Aug F	--	51.7
03:45	CH	PMI Composite Caixin/Markit	Aug	--	50.9
08:00	NO	Households' Savings Rate	2Q		6.8%
08:00	NO	Current Account Balance	2Q	--	67.8b
08:30	SW	PMI Composite	Aug	--	52.2
10:00	EC	Composite PMI	Aug F	51.8	51.8
10:30	UK	Composite PMI	Aug	50.5	50.7
11:00	EC	Retail Sales MoM	Jul	-0.6%	1.1%
14:30	US	Trade Balance	Jul	-$54.3b	-$55.2b
20:00	US	U.S. Federal Reserve Beige Book			
	US	Total Vehicle Sales	Aug	16.90m	16.82m
Thursday Sept 5					
08:00	NO	SSB Economic Outlook	3Q		
08:00	GE	Factory Orders MoM	Jul	-1.5%	2.5%
09:30	SW	Riksbank Interest Rate	Sep-05	-0.25%	-0.25%
13:30	US	Challenger Job Cuts YoY	Aug	--	43.2%
14:15	US	ADP Employment Change	Aug	150k	156k
14:30	US	Nonfarm Productivity	2Q F	2.2%	2.3%
14:30	US	Initial Jobless Claims	Aug-31	215k	215k
15:45	US	Markit US Composite PMI	Aug F	--	50.9
16:00	US	ISM Non-Manufacturing Index	Aug	54	53.7
17:00	WO	Global Composite PMI	Aug	(51.4)	51.7
Friday Sept 6					
08:00	GE	Industrial Production MoM	Jul	0.4%	-1.5%
08:00	NO	Manufacturing Production MoM	Jul	0.4%	-1.0%
11:00	EC	GDP QoQ, Details	2Q F	0.2%	0.2%
14:30	US	Change in Nonfarm Payrolls	Aug	168k	164k
14:30	US	Unemployment Rate	Aug	3.7%	3.7%
14:30	US	Average Hourly Earnings YoY	Aug	3.0%	3.2%
Sunday Sept 8					
	CH	Exports YoY	Aug	2.6%	3.3%

- **PMIs**
  - » **Global composite PMI** probably ticked down in August, we estimate a 0.2 p decline to 51.5, even if the manufacturing PMI rose. The PMIs points to 3% global GDP growth but a decline in manufacturing production. US Markit's PMI slipped, the avg of Markit and regional surveys suggest a marginal decline in the manufacturing ISM
- **China**
  - » **Exports** are still heading up; the Chinese economy has not yet crumbled under the weight of the trade war. Just exports to the US are declining
- **US**
  - » **The labour market** is still going quite strong, although growth is slowing (and growth slowing faster than earlier reported after a substantial annual revision published two weeks ago). Labour shortages are unusual widespread
  - » **Fed's Beige Book** will most likely continue to note an overall solid US economy, barring weakness in manufacturing and business investments. Still, the Fed has 'decided' to deliver the second cut Sept 18
  - » **Trade deficit** is widening marginally as exports have softened
- **EMU**
  - » **Retail sales** soared in June and increased moderately in Q2. The consumer sector is so far resilient to the manufacturing setback
- **Norway**
  - » **Households' savings rate** may have bottomed out, after a decline in the rate has funded ½ of the consumption growth since 2015
  - » **Manufacturing production** is accelerating, boosted by oil related sectors. The oil related upsurge will probably last for some months but the upside on activity is limited, as oil investments

Source: Bloomberg. SB1M est. in brackets. The key data points are highlighted

In this report

Global +PMIs

- The world slightly less disappointing recently, helped by the US, China (!)
- Retail sales still strong, manufacturing production stagnates – exports implodes
- The PMIs stabilised in July, level not impressive but do not signal full stop
- Mixed Chinese PMIs, in sum up due to a stronger Markit manufacturing PMI

USA

- Durable goods orders are sluggish but not subsiding
- Private consumption is accelerating, supported by income growth and even more savings cut
- Core PCE inflation y/y remains soft, underlying growth picks up
- Pending home sales down in July but trend is still strong
- A 2% house price inflation reflects a steady housing market, no take-off
- CB consumer sentiment index steady at an elevated level in August
- Q2 GDP growth marginally revised down, to 2%
- Profits up in Q2 but have flattened, are falling sharply in % of GDP, investments exposed
- The trade deficit shrank marginally in July
- Jobless claims remain very low
- Q3 growth accelerating – or cooling? Reports at 1.4-2.3%

EMU

- Unemployment flat in July trend down, but slower
- Core CPI one inch up to 1% in August, still low
- EU economic sentiment inched up in Aug, level far too upbeat
- German Q2 details are not promising; muted household demand, business invest. fell
- German Ifo survey sinks further

Sweden

- Retail sales still growing at a solid pace
- KI business survey dives, lowest level since ‘13
- Consumer confidence below avg points to softer consumption growth

Japan

- Manufacturing production heading slowly down
- Unemployment further down, employment growth still impressive

Norway

- Mainland GDP up 0.7% in Q2 but details do not point to a very bright outlook
- Oil investments: The upside is not that large, peak in H2 2019?
- Unemployment down in Aug, a reassuring sign but the labour market is slowing?
- Retail sales improved in July, slowly trending up
- Credit growth down to 5.6% in July, due to student loan -> grants
- Consumer confidence slips, according to Opinion’s CCI

Highlights

The world around us

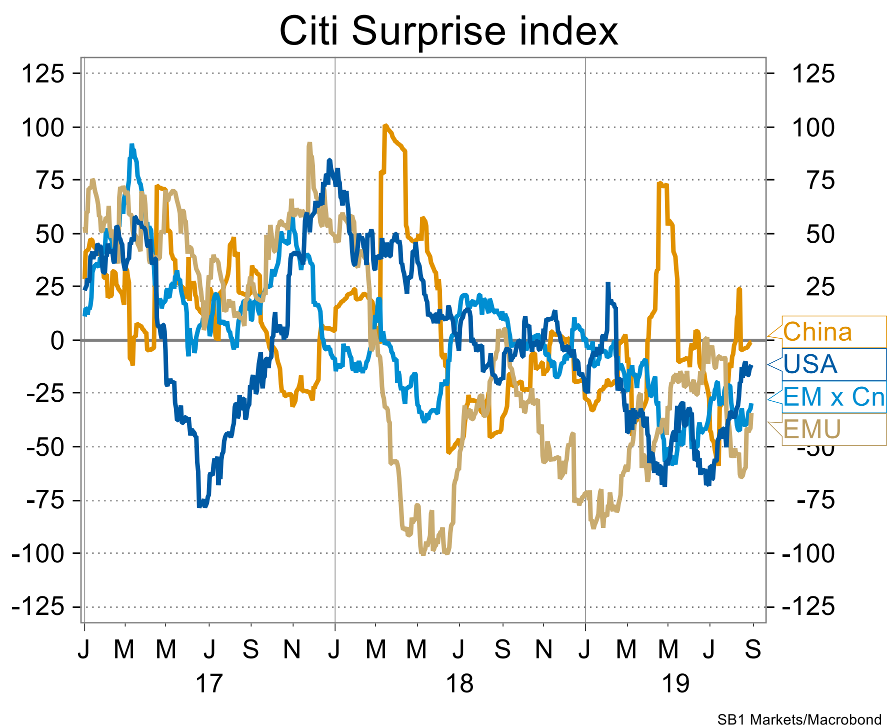
The Norwegian economy

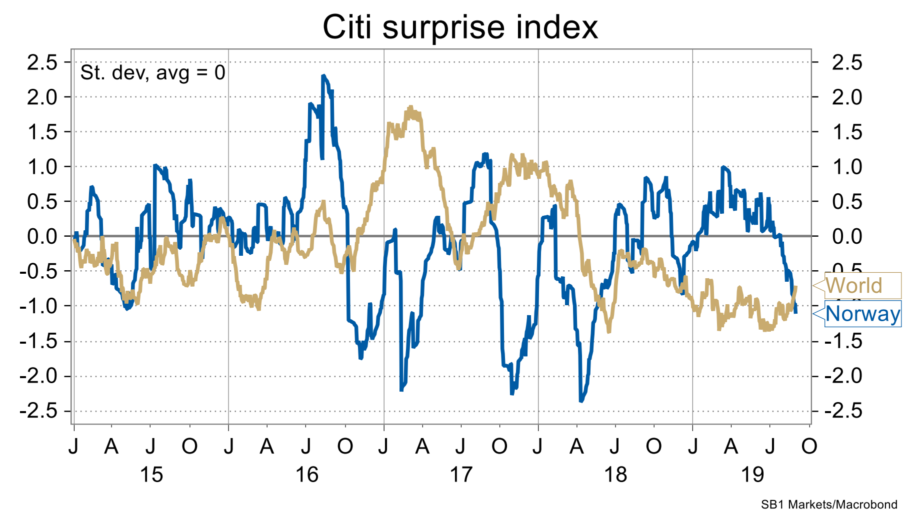
Market charts & comments

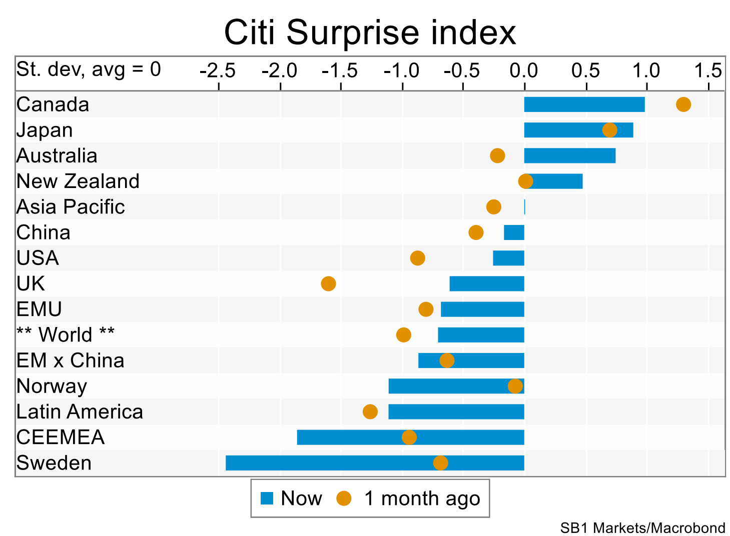
SpareBank 1 MARKETS

The world slightly less disappointing recently, helped by the US, China (!)

All major regions ex China are reporting data below par. EMU less negative. Norway further down







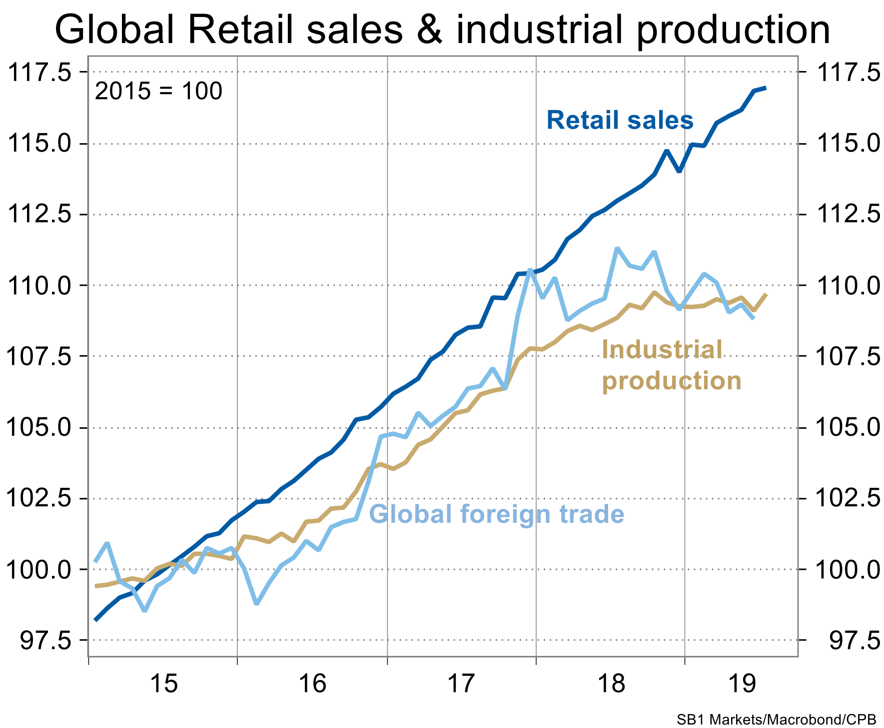
- The global surprise index has been in negative territory since last spring, improving somewhat through July and August
- The EMU surprise index is weak but a tad less so recently as the PMIs were better than feared (but still weak!)
- US data less negative in July & August, mostly due to strength at the consumer side
- Chinese July data in sum neutral, from negative in July
- Norwegian data are disappointing vs expectations, the surprise index reached the weakest level in a year. We are not sure we agree on this assessment, although data are not so bright

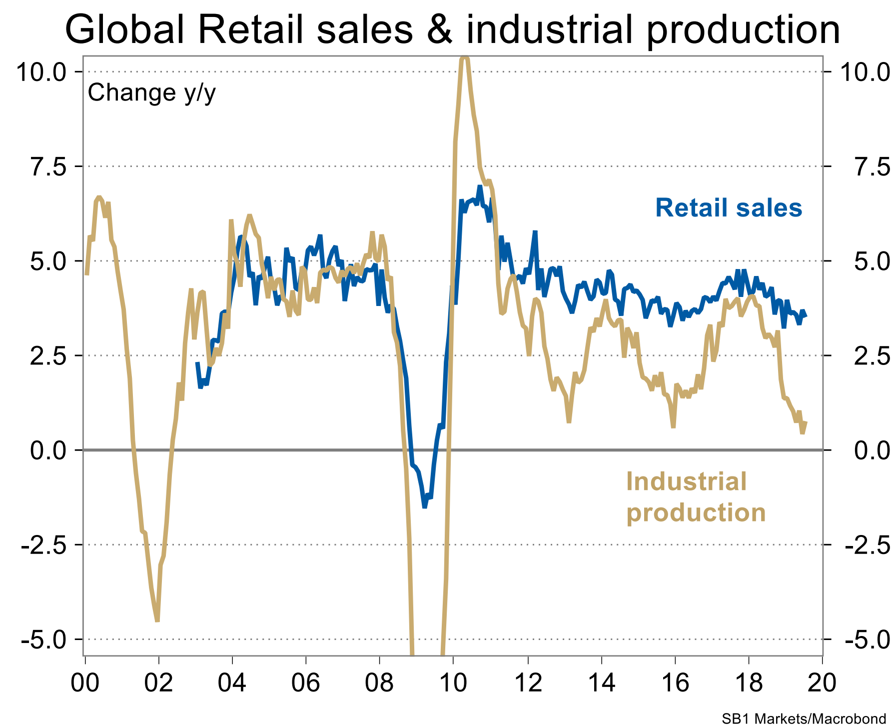
Surprise-indices measure the difference between economists' expectations and the actual outcome over a 3 month rolling window

SpareBank 1 MARKETS

Retail sales still strong, manufacturing production stagnates – exports implodes

Global foreign trade declined in June, trending down since Q3 last year



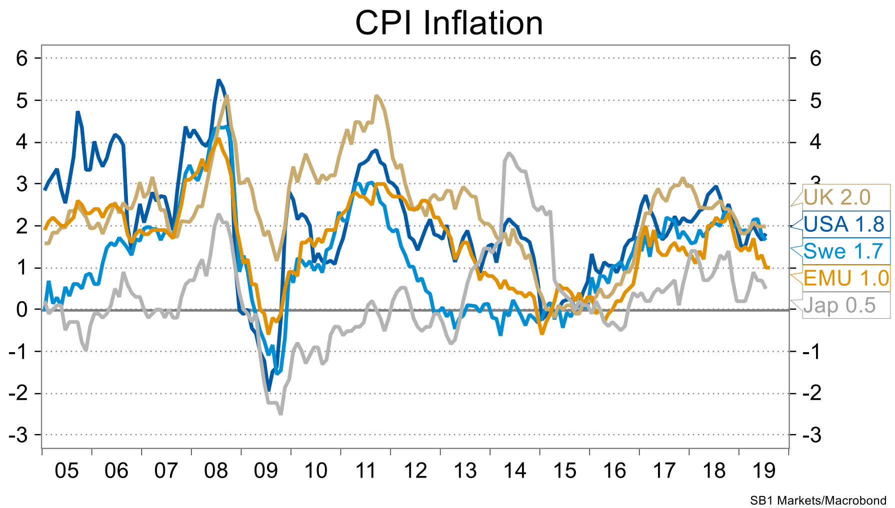


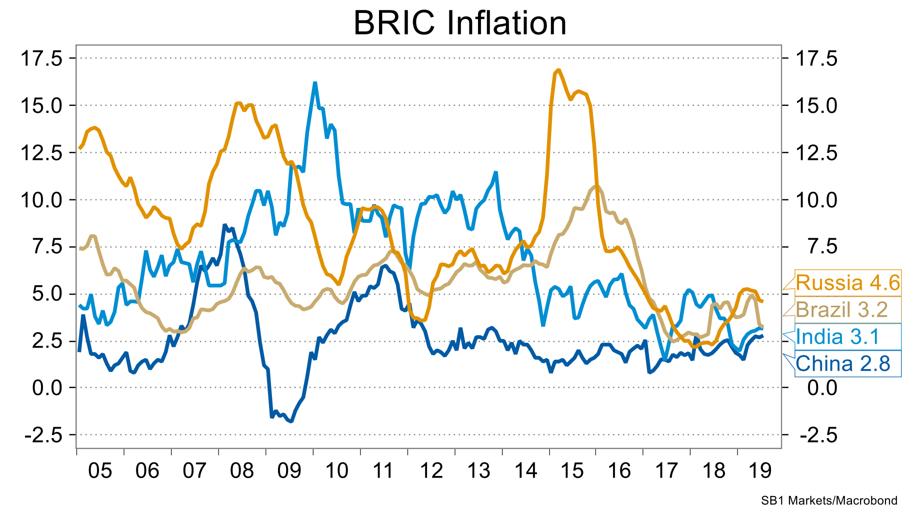
- **Global foreign trade** fell 0.5% m/m in June, and is now trending sharply down. The weakness was rather broad based but Emerging Asia ex China and Lat. Am were the weakest links in the chain (we have massaged the trade data from Netherlands CBP, we reported a 1.4% June decline last week)
- Global **industrial production** probably recovered in July. from the June slump, even if both China and the US have reported weak figures (some EMs fell sharply in June and probably recovered in July). Still, the trend is no more than flat
- **Retail sales** accelerated in June, and even if July might turn out to be somewhat weaker due to China, the trend signals that consumption is still supporting the global economy – even if it has slowed somewhat

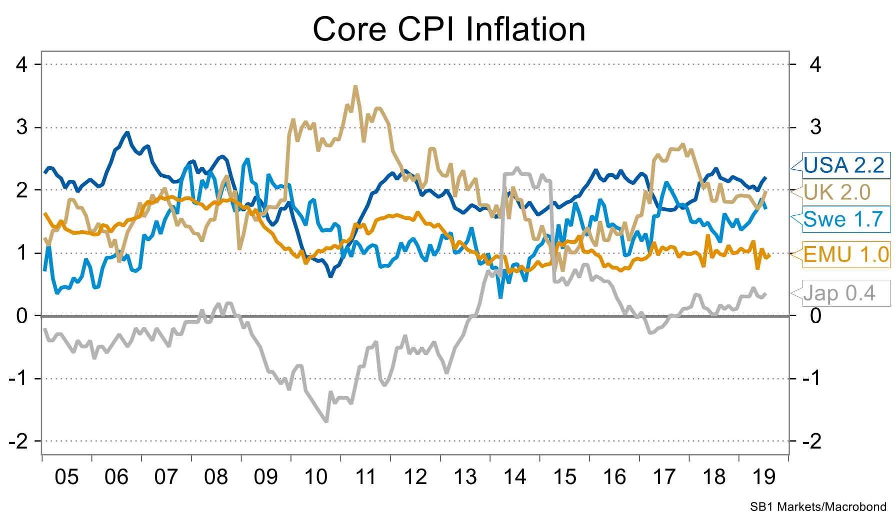
SpareBank 1 MARKETS

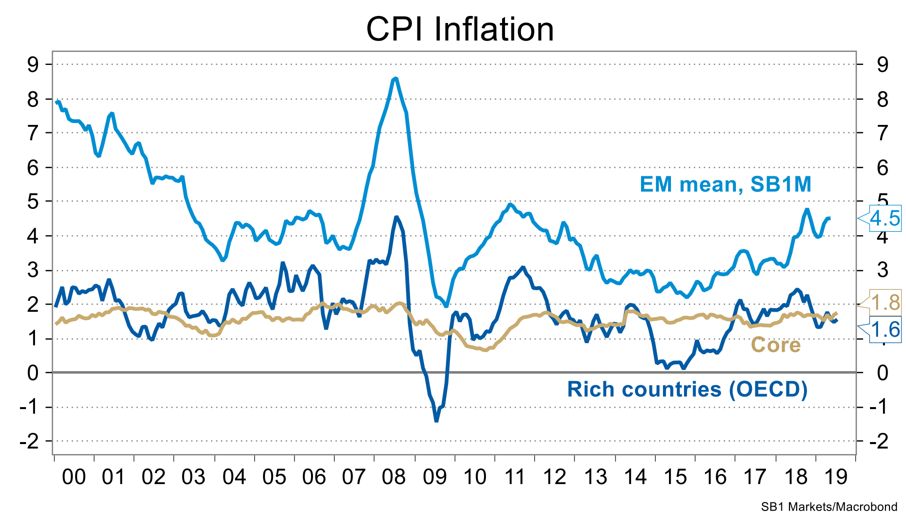
DM CPI has turned south, with the oil price. Core is sum flattish

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





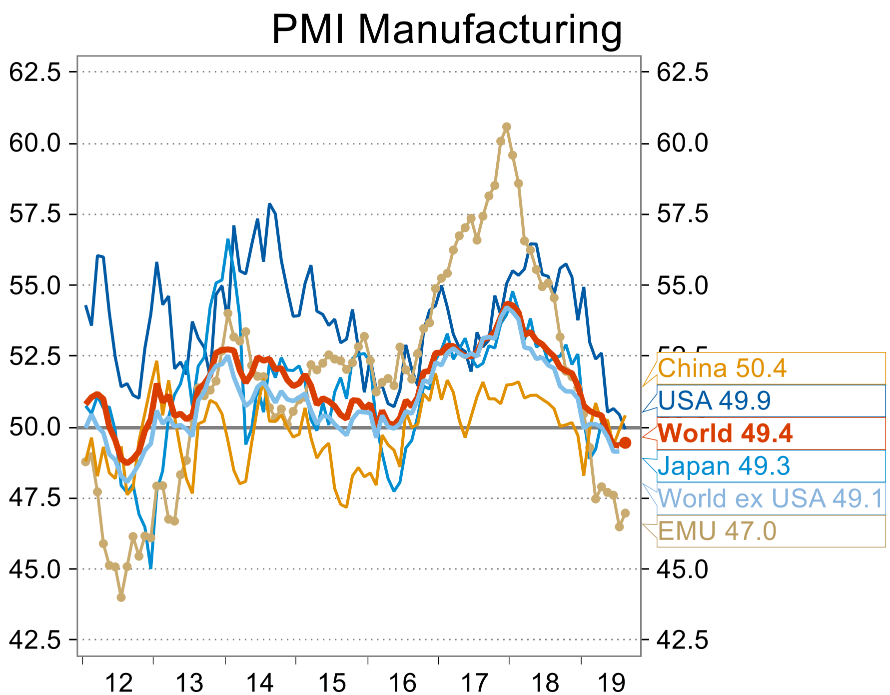




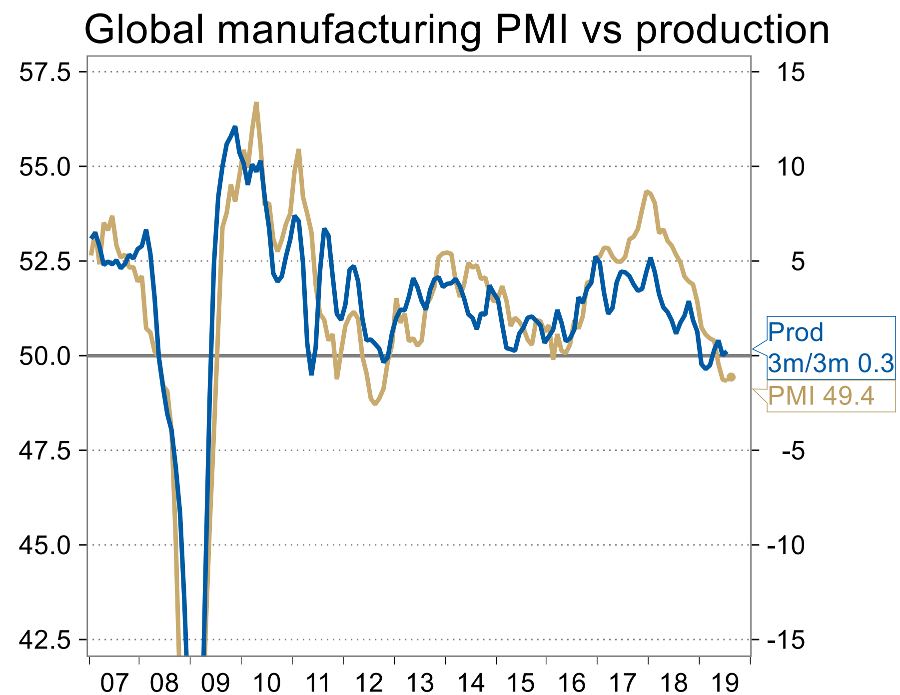
Change in % y/y in all charts. EMU core based on a seasonally adjusted price index

Ahead of global manufacturing PMI: Probably a tad up

We expect a 0.1 p lift, and it remains below the 50-line



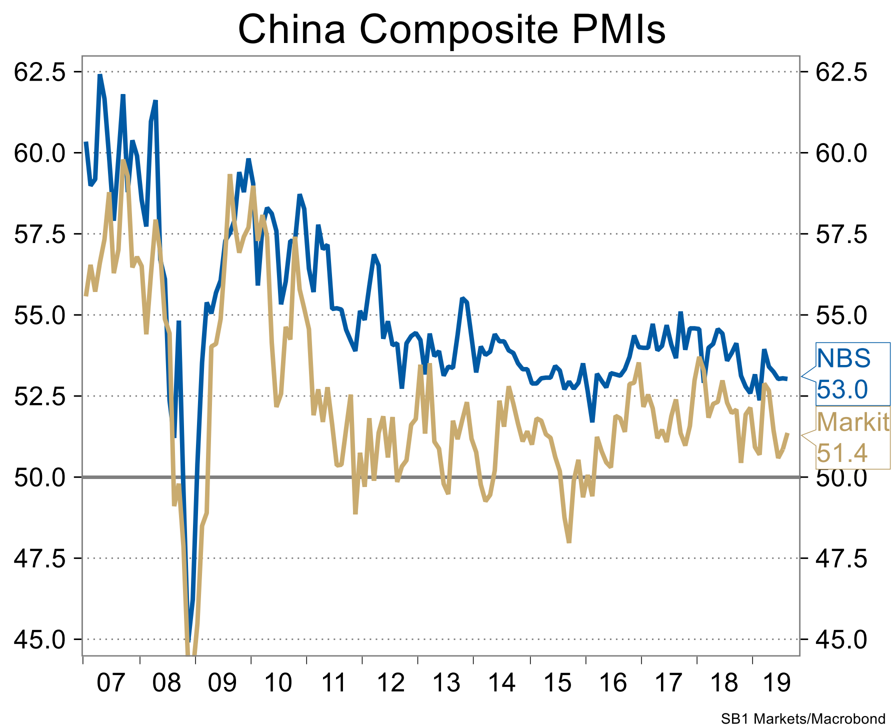
Source: IHS Markit, SB1 Markets, Macrobond

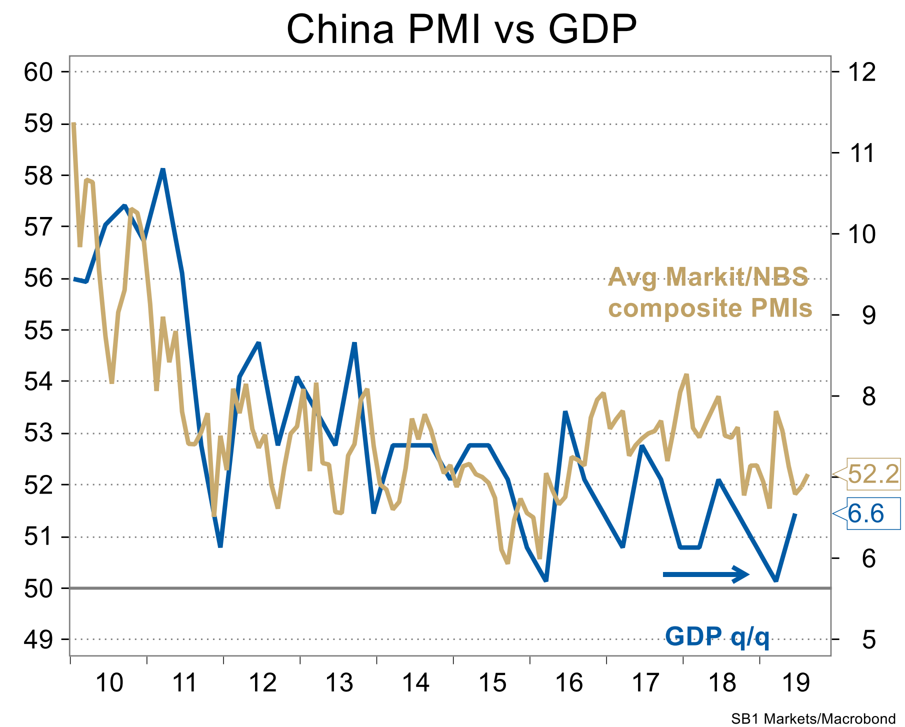


SB1 Markets/Macrobond

The PMIs more up than down in August

The NBS composite survey flat, Markit's probably rose



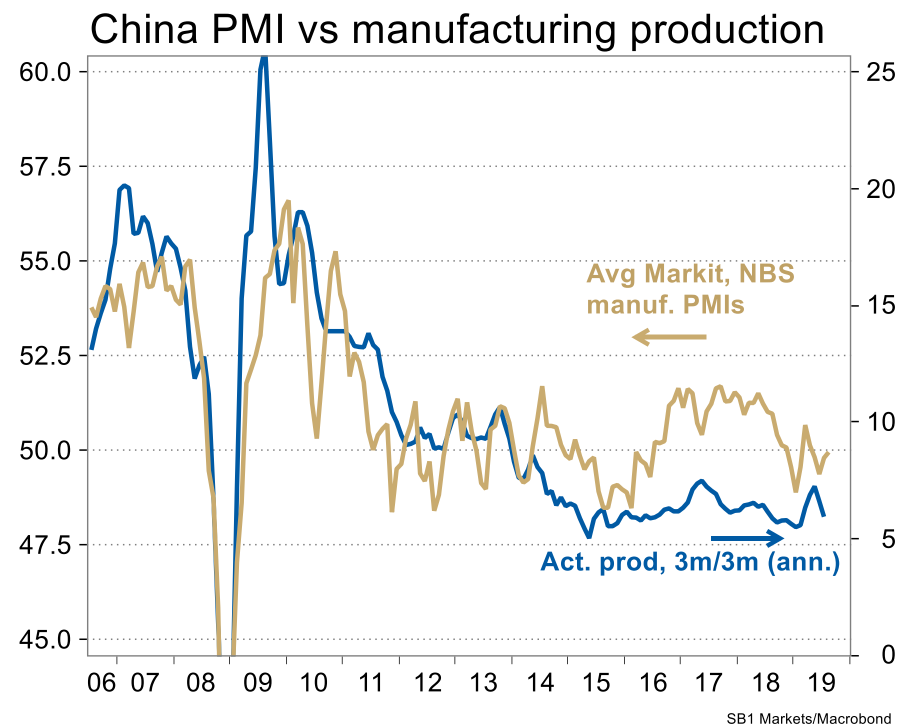


- NBS' composite PMI (CFLP) was stable at 53 in Aug, not too hot/too cold. The manufacturing index declined 0.2 p, stabilising recent months, while service businesses reported a small increase, to 53.8
- Markit's composite PMI probably rose as well, due to the surprising recovery in the manufacturing PMI
- The NBS service sector PMI is approx at the average over the past 5 years but is trending slowly down. Markit's volatile service sector PMI is trending flattish, while the level now is below average (until July, Aug not yet reported)
- The two PMI data are below the avg over the past 3 years but do not at all signal any abrupt halt in the Chinese economy

SpareBank 1 MARKETS

Mixed manufacturing PMIs, Markits up to above 50, NBS remains below

Markit's PMI surprisingly up in August, far above past 5 y avg, NBS/CFLP far below



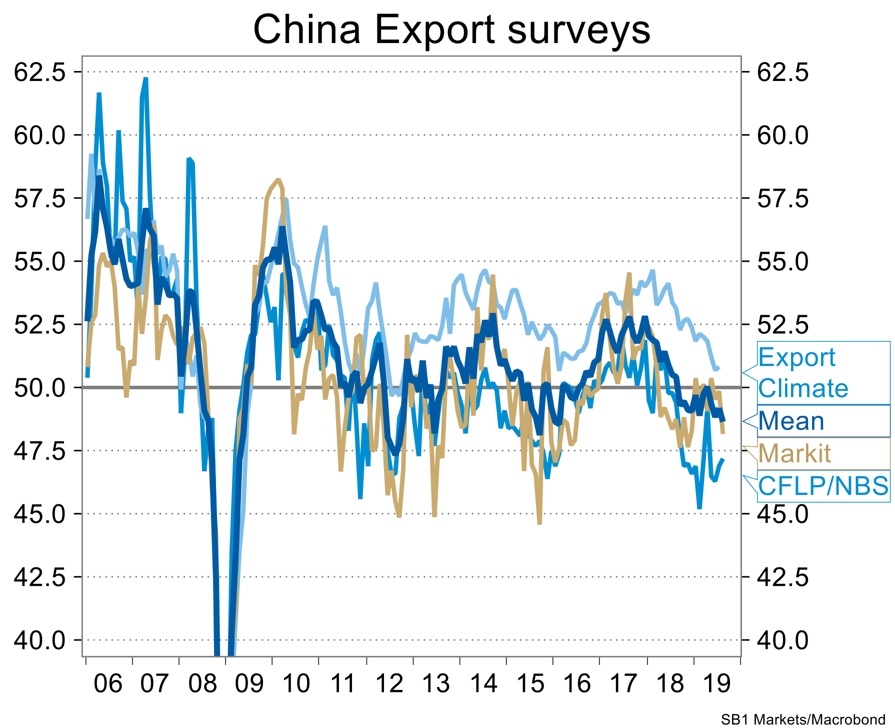
- The NBS/CFLP 'official' manufacturing fell 0.2 p in Aug, expected unch, following the 0.3 p increase in July. This PMI has stabilized recent months but remains below the 50 line, and well below the average past years. Export orders are declining but not faster. Domestic orders are just marginally below the 50 line
- Markit's manufacturing PMI rose to 50.4 from 49.9, expected 0.1 p down. The level is not low at all, check the chart!
  - » The NBS survey is more concentrated vs large state owned companies, Markit's vs 'smaller' privately owned companies
- The avg of the NBS/Markit PMIs is not reflecting any rapid slowdown in manufacturing activity – which by the way has not been weak recent months, even if the July print was weak – following the surge in June

Mixed export order indices, Markit's more down than NBS/CFLP up

Markit's manuf. Export order index fell sharply in Aug but is still above the 2018 level

Export surveys have not collapsed, neither have exports

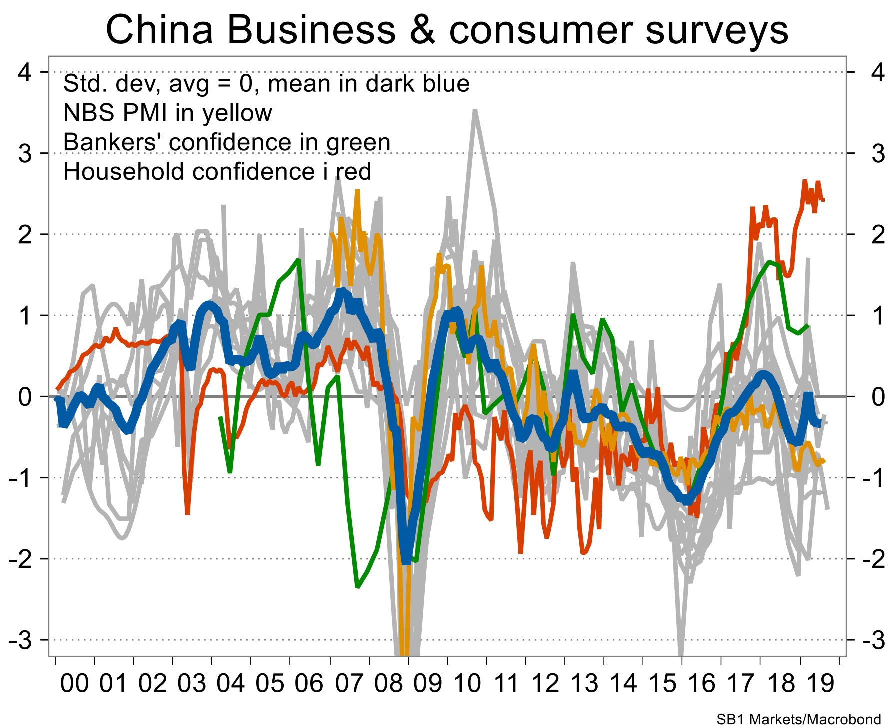
Companies are reporting modestly deteriorating export conditions

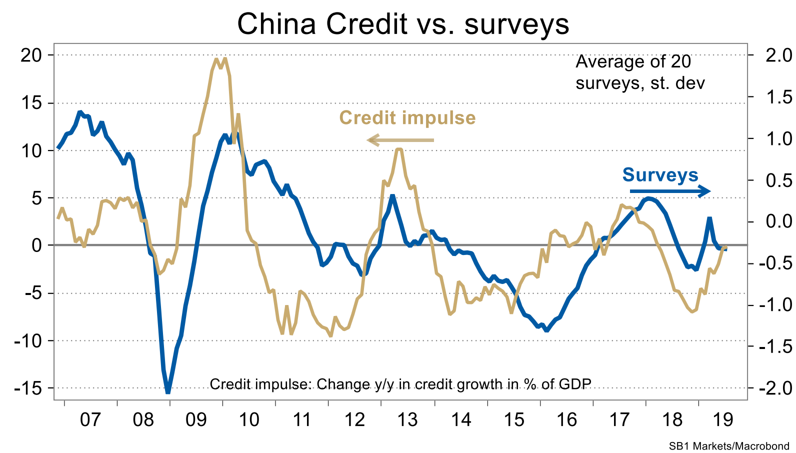


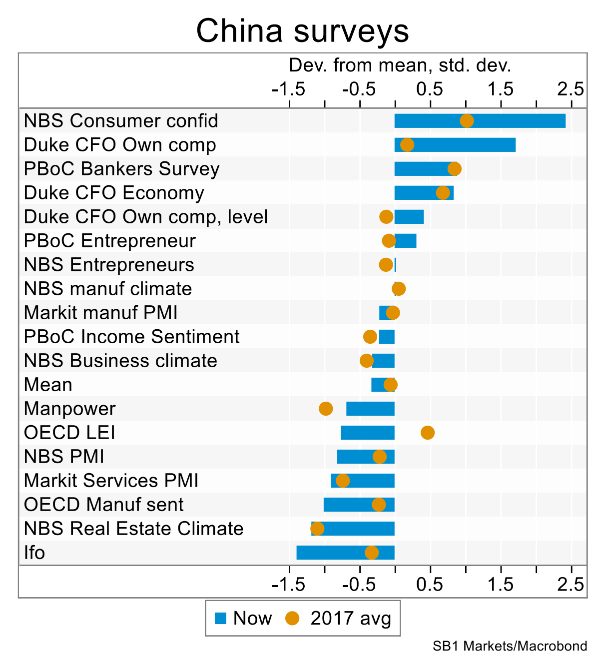
- The surveys we follow are down and below average. Still, the figures are not dramatically weak; the export orders surveys were as weak as now (or weaker) in 2012, 2013 and 2015 and 2016, without any rapid slowdown in the Chinese economy, even if export volumes flattened in 2012, 2013, and 2015/16.
- Export volumes fell in April, but have more or less stabilised so far in 2019, as the export surveys have reported

Most surveys have improved/stabilised as the authorities are stimulating activity

Consumer confidence is still sky-high and businesses sentiment is not weak



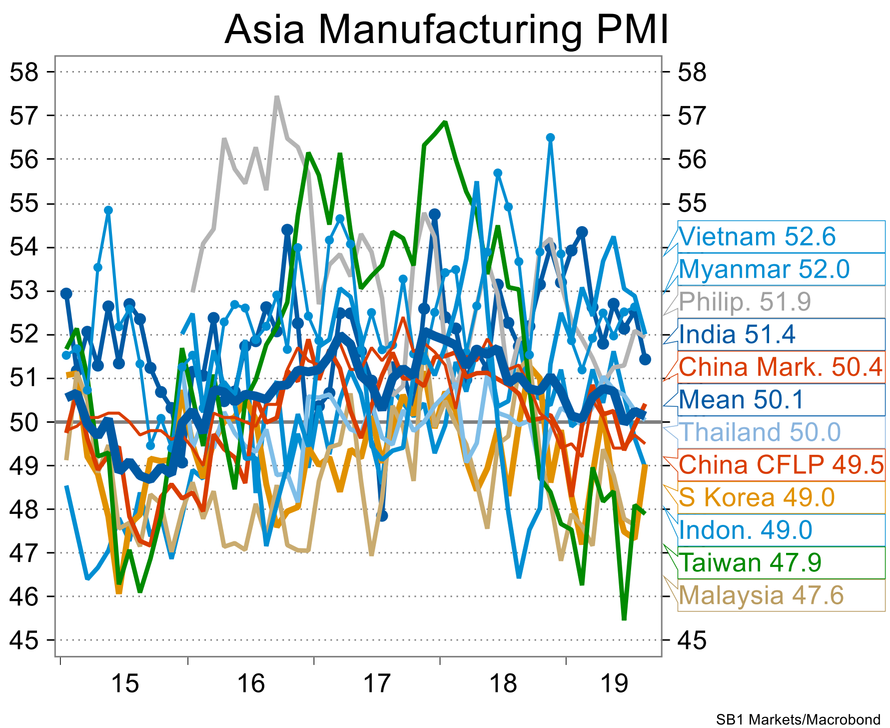


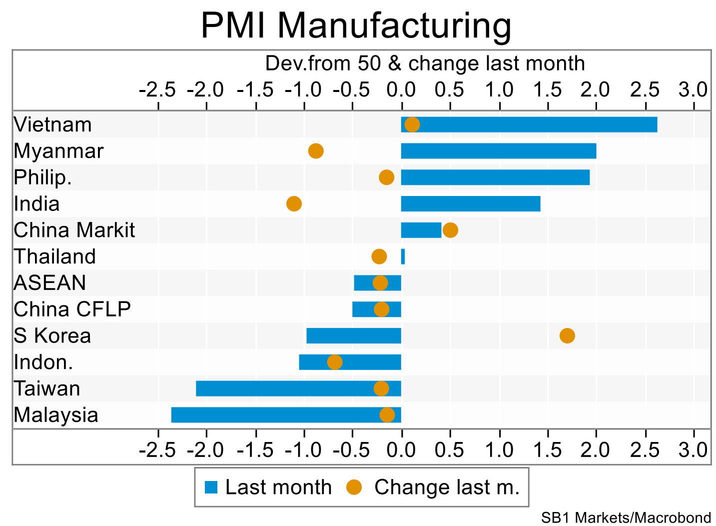


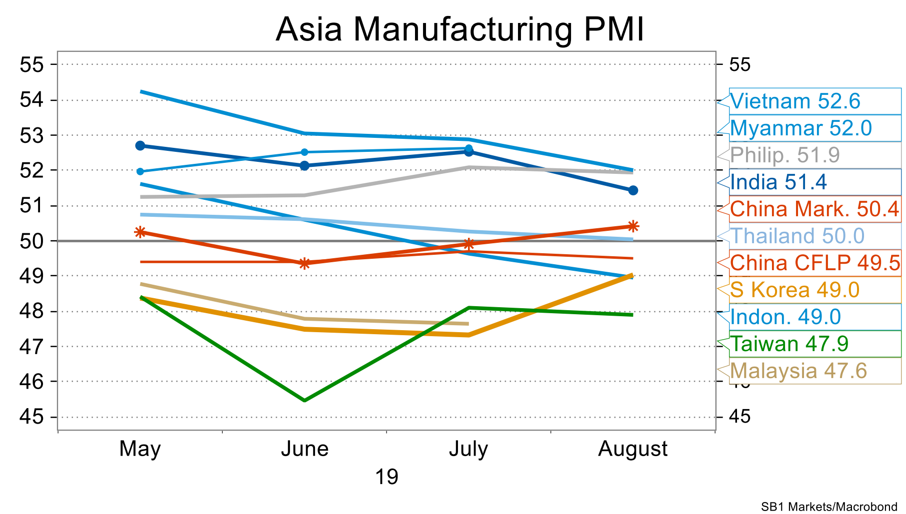
- Trade was worries may explain the slowdown in China through 2018 but the credit tightening in 2017 (especially vs. the shadow banking marked), that dampened credit growth substantially is probably more important. The credit impulse (the 2. derivative) turned negative, and the economy slowed, as usual
- The authorities are pushing the credit accelerator. The credit impulse has turned upwards and is back in neutral. In addition, fiscal policy has been turned expansionary, both by cutting taxes and increasing expenditures, especially in infrastructure (equalling 1% of GDP)

Mostly down in August but both China and South Korea up

More countries are below the 50 line than above



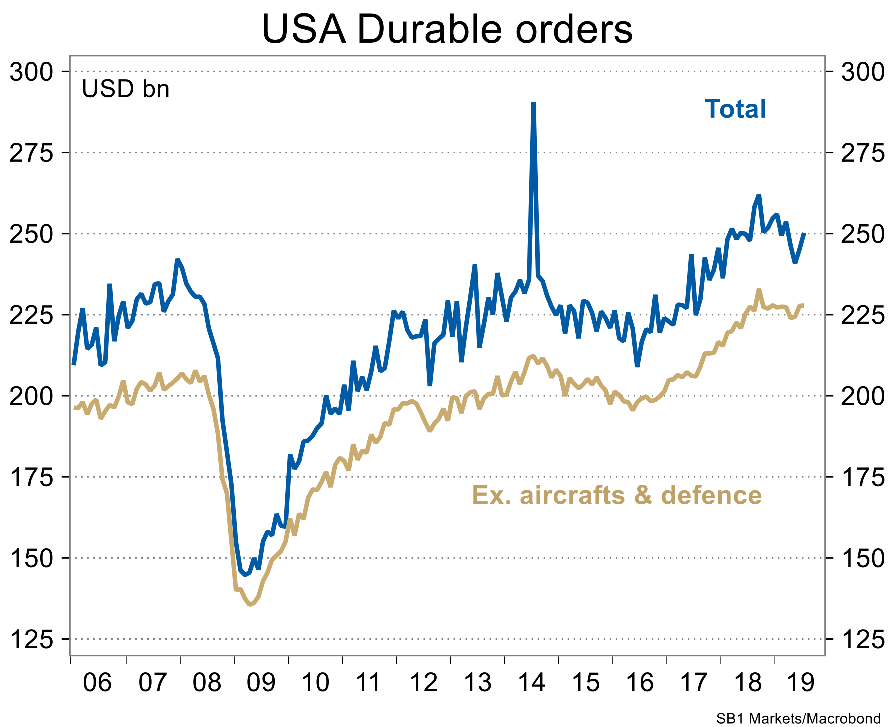


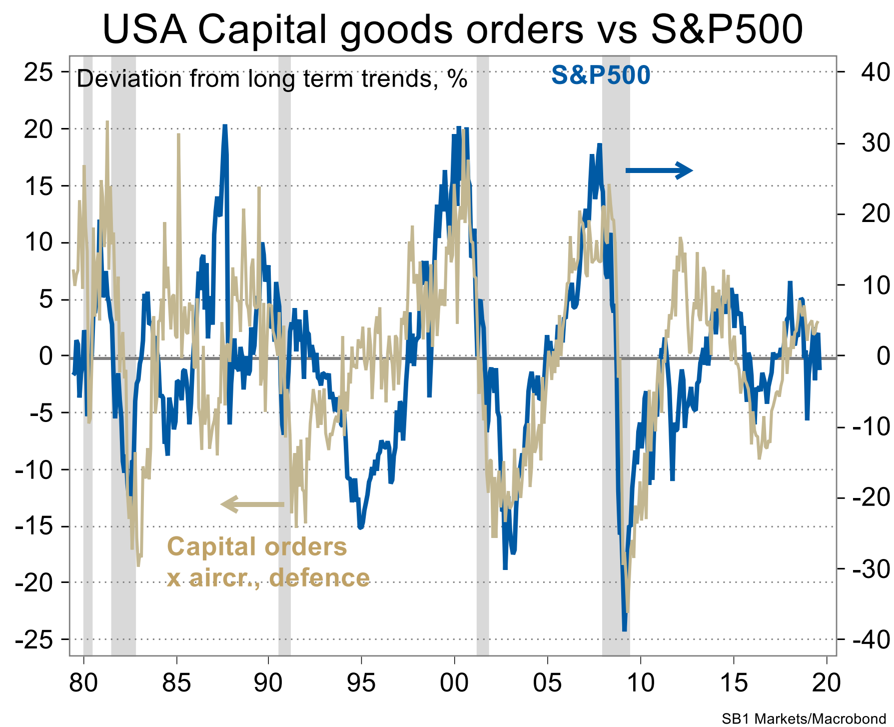


- The Asian PMIs are producing a spaghetti chart like the one above. Take a deep breath before you draw any important conclusion based on any single observation

Durable goods orders are sluggish but core is not subsiding

Core durable & investment orders marginally up in July – do not signal an abrupt investment setback

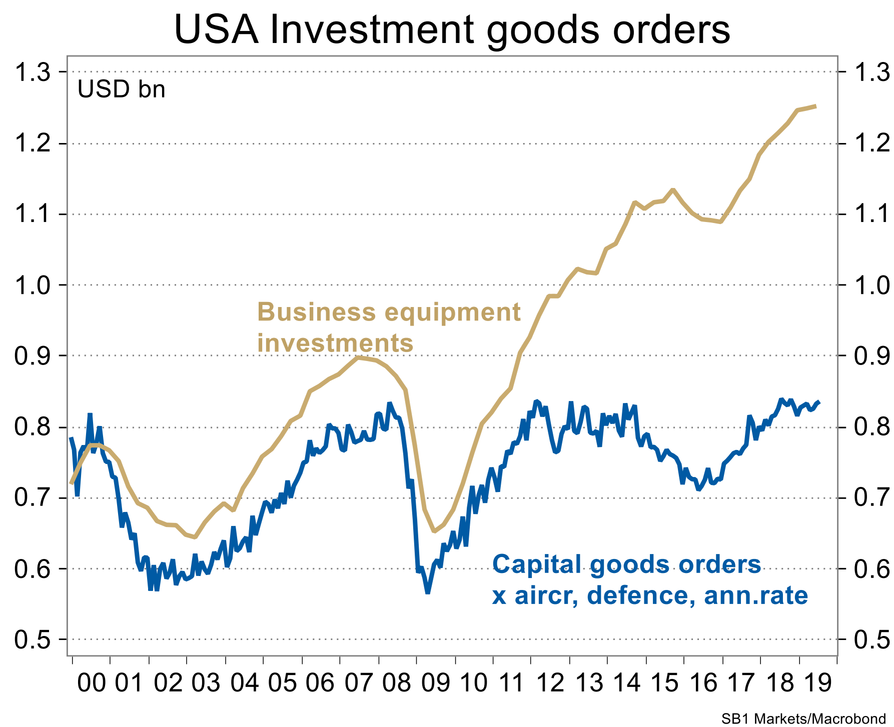


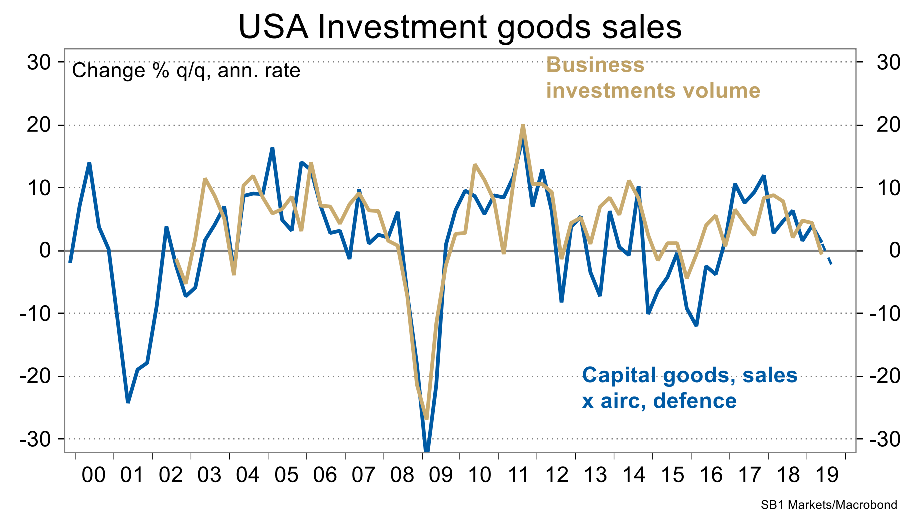


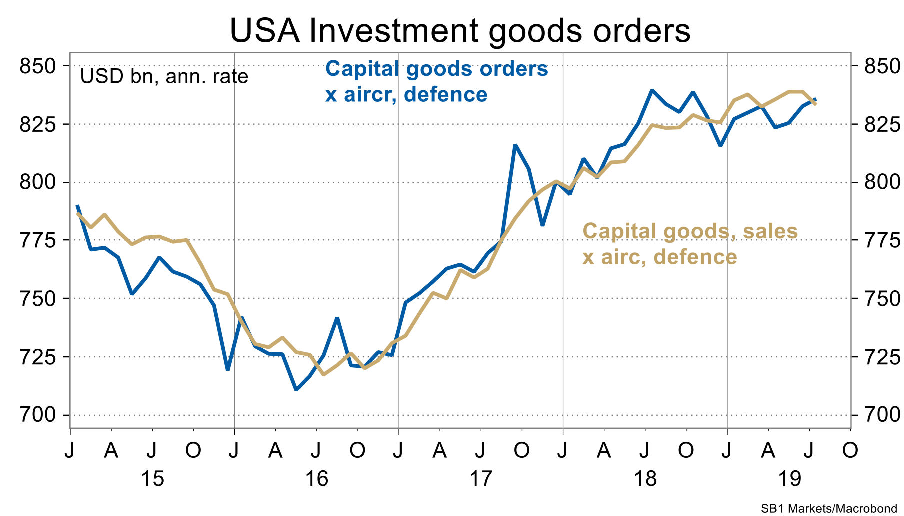
- Total durable orders rose 2.1% in July, boosted by a rebound in aircraft orders. Orders have been sliding down recent months, partly driven by troubles with Boeing's Max plane. Core orders (ex aircrafts and defence) grew by 0.1% m/m in July, and has flattening out the past year. Uncertainties caused by the trade war are probably dampening orders. However, there are no signs of an abrupt decline
- Core capital orders have increased modestly recent months, sales probably inching up too, even if the July level was below the Q2 level. Orders/sales are signalling weakness but no steep decline the business investments, which fell marginally in Q2
  - » 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 just a mild decline in investments into Q3

Core investment orders rose marginally in July (June revised down), sales edged down



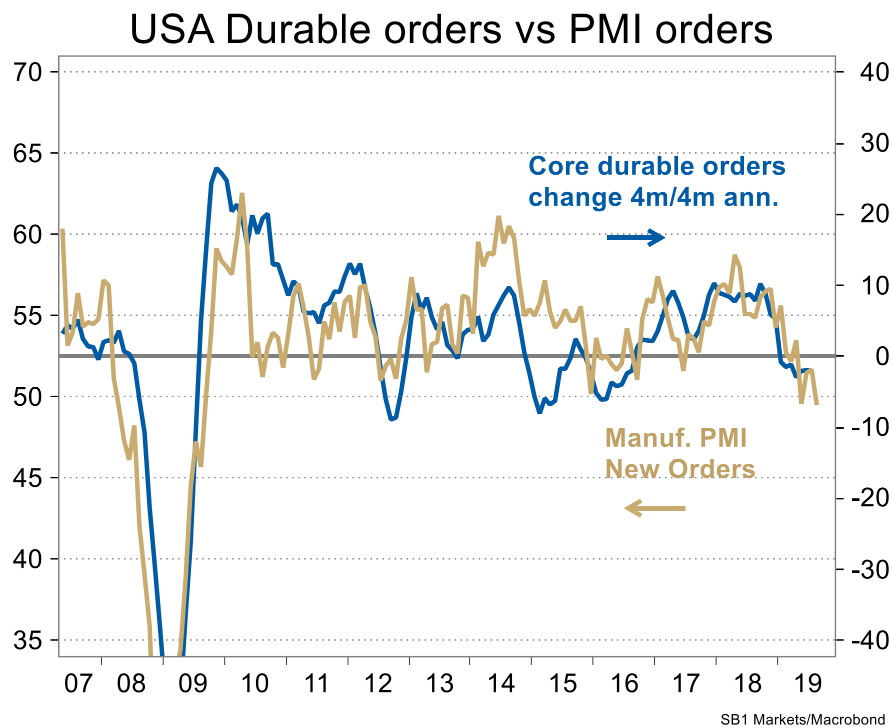


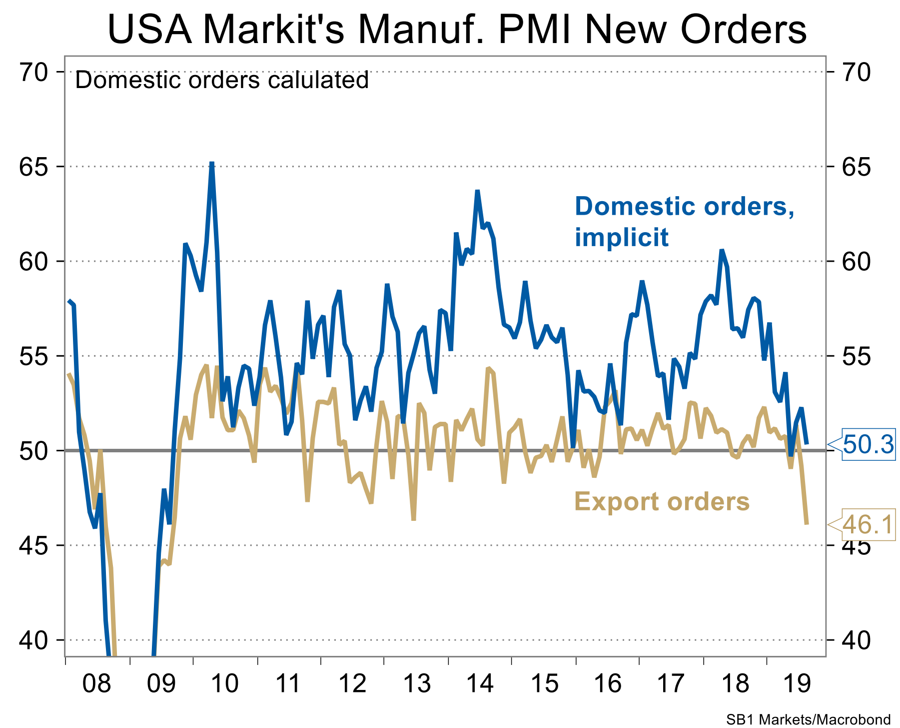


- Investment orders (core) increased by 0.4m/m in July but June was softer than previously reported, 0.9% vs 1.5%. Underlying growth is modest, up 1.3% (3m/3m), and they are flat since last summer
- Sales fell 0.7%, and are probably slowly on the way up, but the July level is below the Q2 average, so far indicating a marginal decline in business investments in Q3 (as did a decline in imports of investment goods in Q2) – but <u>no abrupt setback</u>
- Unfortunately, the PMI is pointing to softer order inflows

PMIs are not promising, signal weaker order inflows

The downturn has been driven by weaker domestic demand, until exports slipped in August

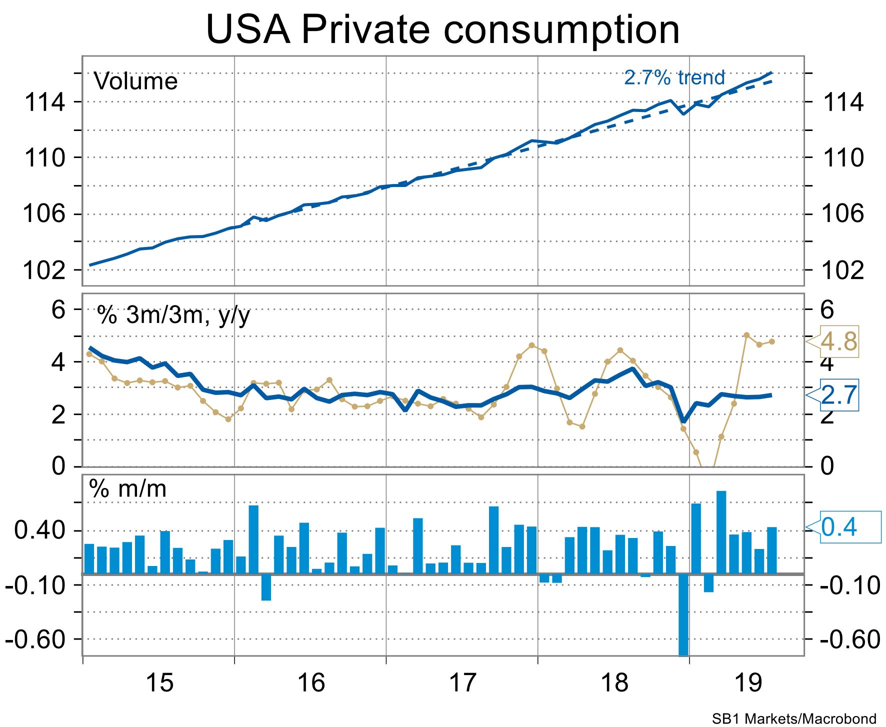


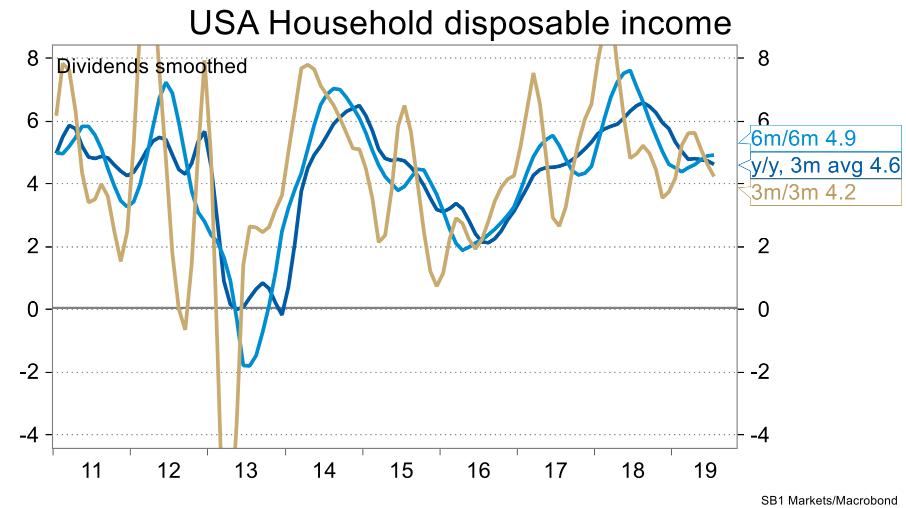


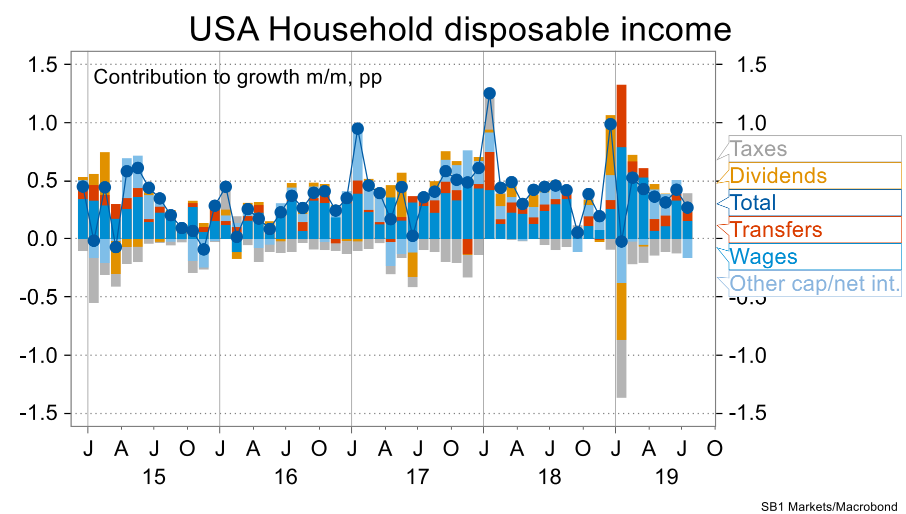
- The manufacturing PMI index is telling the same story as Markit's PMI (but is less precise)

Private consumption still going strong into Q3, but income growth is slowing

Consumption rose 0.4% in July, underl. growth close to 5% - above income growth, savings down





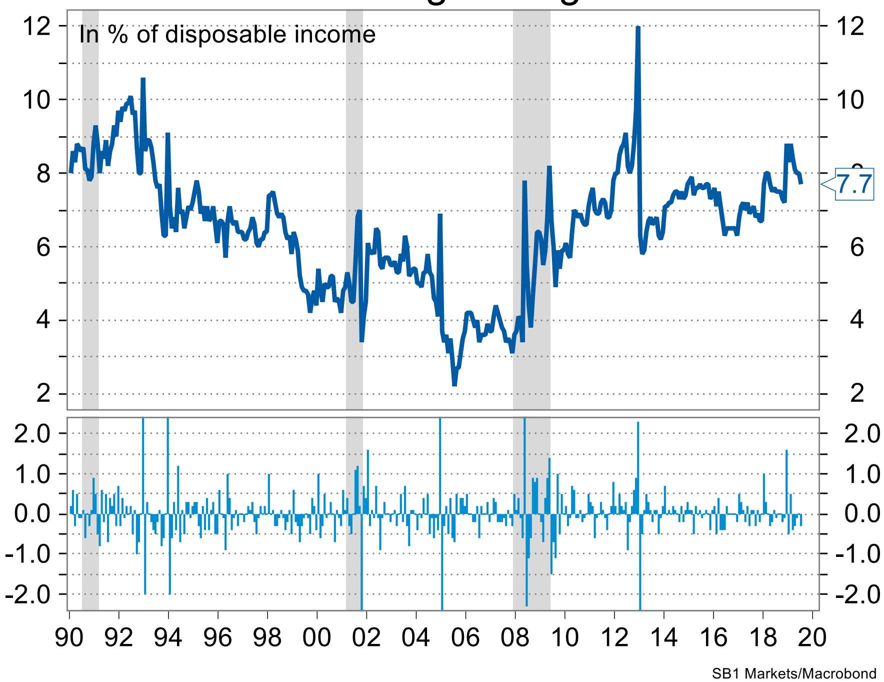


- Private consumption grew 0.4% in July, 0.1 pp weaker than expected. Consumption is up 4.8% 3m/3m, Q3 is off to a solid start, following the 4.7% growth in Q4 (real terms)
- Households' nominal disposable income rose 0.2 m/m, following a strong 0.5% print in June. Underlying growth slowed to 4.2% 3m/3m, annual growth marginally down to 4.6%. Total wage & salary income is up 3.4% (volatile data)
- The savings rate is high but has fallen to 7.7% July from 8.8% in Dec, funding 2 pp growth pace in cons. (more half of total)

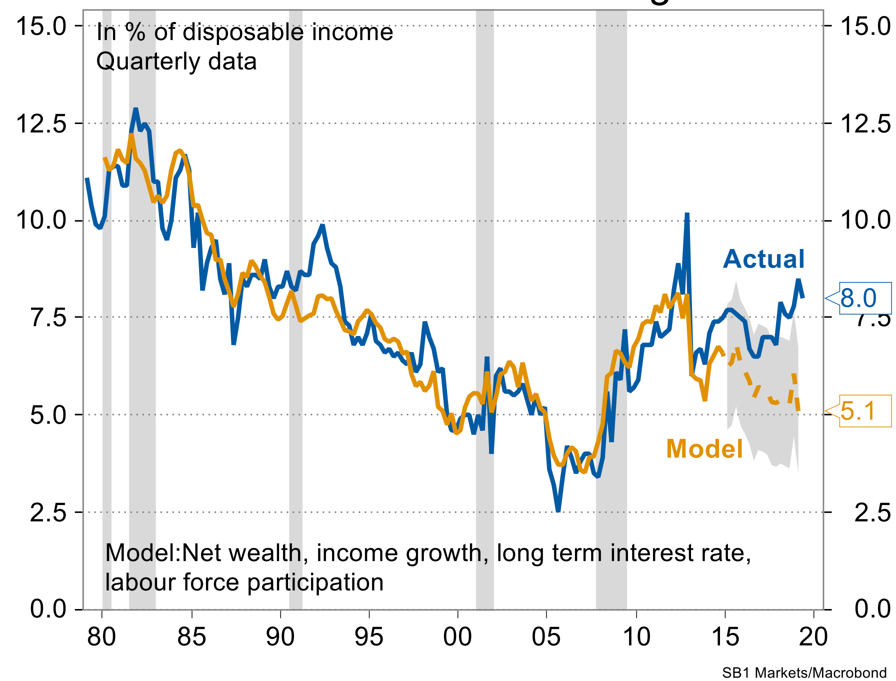
Households savings fell to 7.7% in July, after huge upward revisions

The savings rate inched further down in July, has funded more than ½ of consumption growth in '19

USA Housing savings rate



USA Households' savings

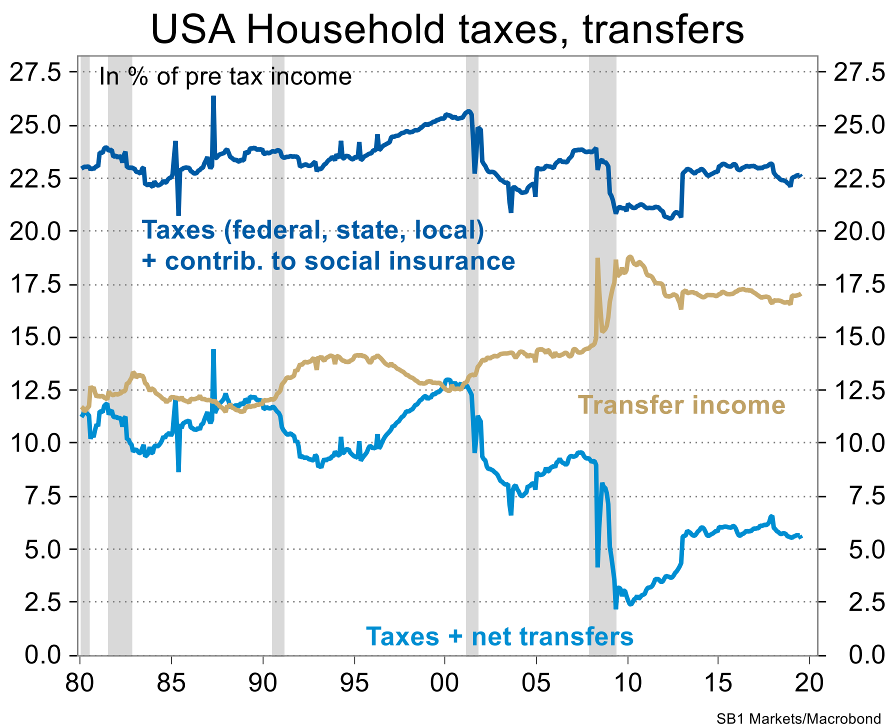


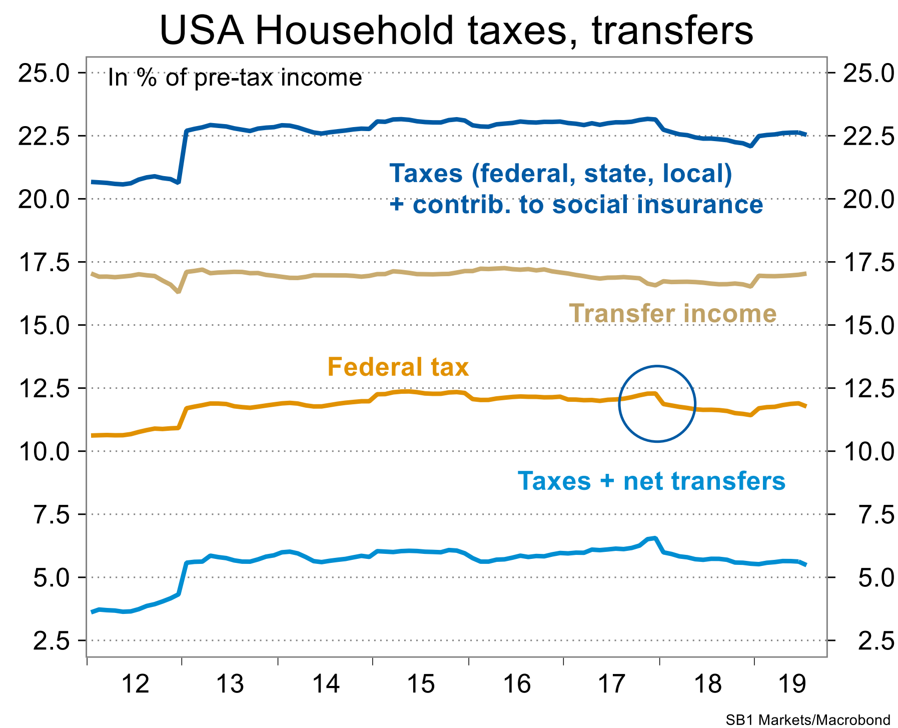
- Household income growth was revised sharply up in the 2019 annual revision, and more than consumption. The Q1 savings rate was revised from 6.7% to 8.5% and Q2 ended at 8.1%
- Following the adjustments, the savings rate is 3 pp above our model forecast! The rise in savings indicate that the tax cuts have largely been saved, and not spent
- Still, the decline in the savings rate so far in 2019 has funded more than half of the brisk growth in consumption. However, as the savings rate is quite high, a further decline is possible

SpareBank 1 MARKETS

The households have received their tax cuts, now they receive more transfers

The tax cuts boosted households' income in early 2018. Now transfers are rising

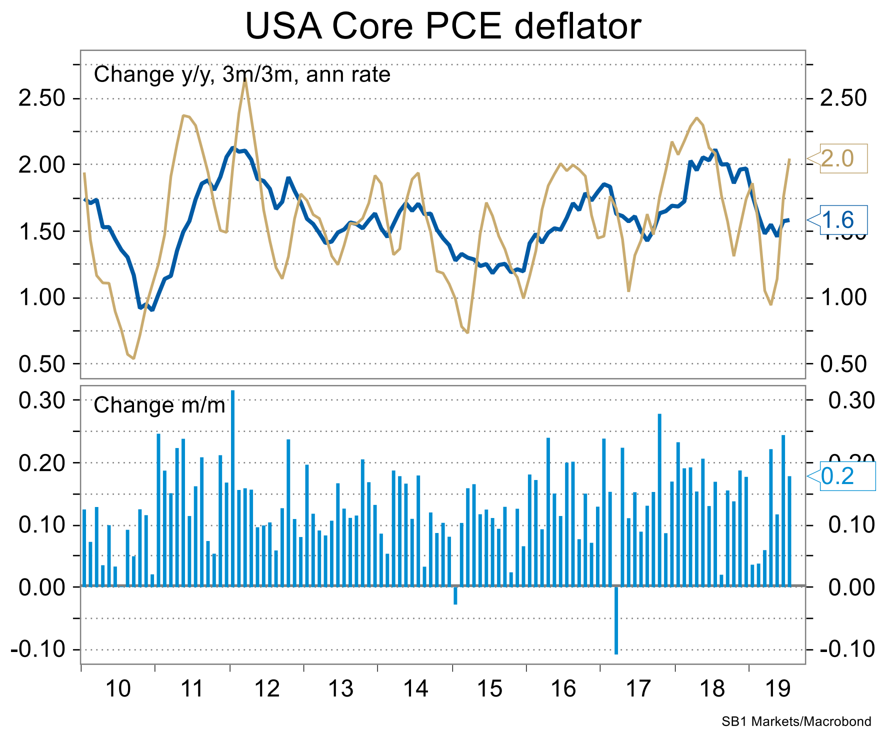


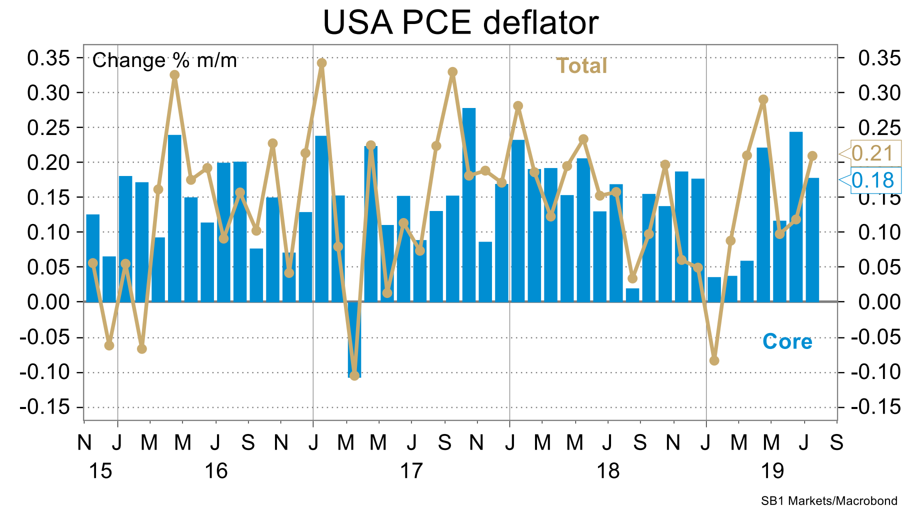


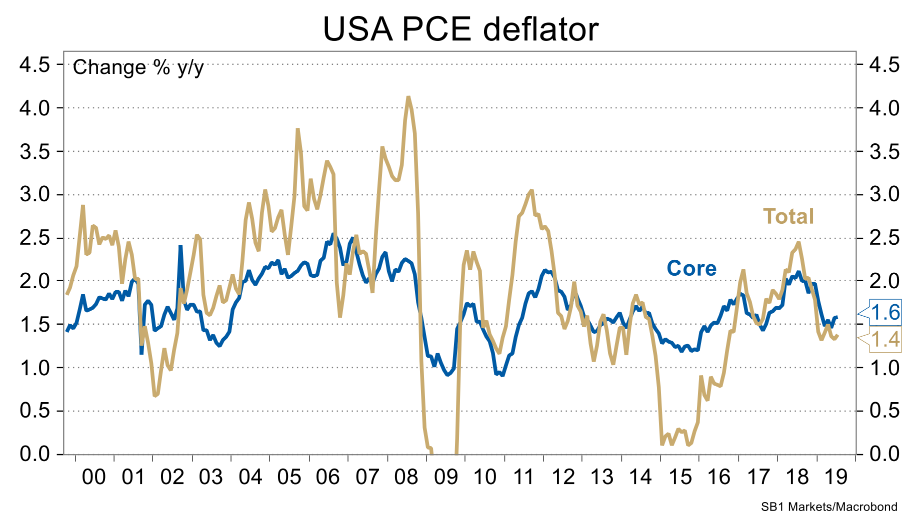
- In sum, household net taxes (taxes – transfers) are down 1% of disposable income since before the tax cuts were implemented. Not that impressive but given a strong economy in the meantime – that usually lifts net taxes substantially – the tax cut is pretty large. In the next recession, net taxes will again fall substantially, contributing to an even higher public sector deficit

Core PCE y/y inflation remains at 1.6, underlying growth picks up

Core PCE deflator flat at 1.6% in July, 0.4 pp below Fed's target. Total PCE inflation at 1.4%



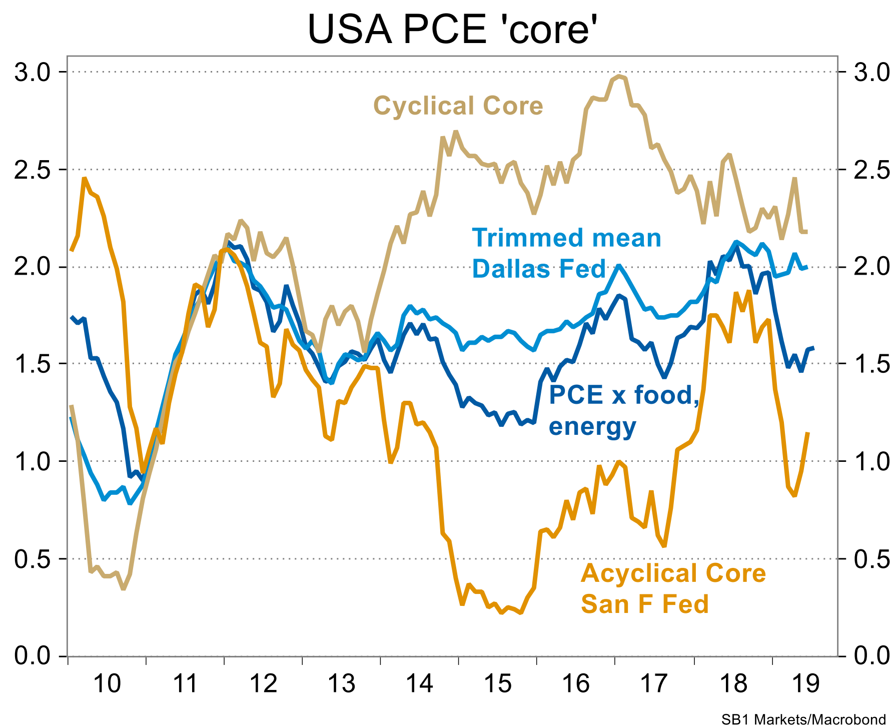


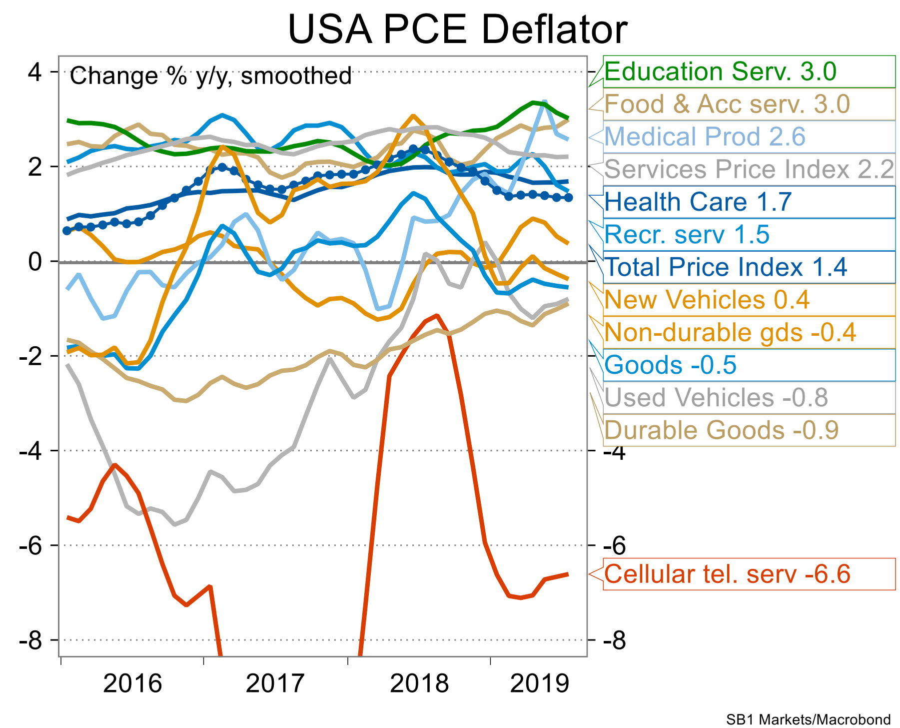


- The core price deflator rose by 0.2% m/m July, as expected. The annual rate was unchanged at 1.6%. Still, underlying growth (measured 3m/3m) accelerated to 2%. The annual rate is low due to low monthly inflation in Dec/Feb
- Total PCE inflation inched up to 1.4% y/y, following a marginal downward revision of June. Total inflation has retreated as energy prices have come down. Good for real income growth
- PCE has been running 'visibly' below Fed's price target at 2% for 6 months. Small changes in inflation has never been important for Fed's rate setting – but it can be used as an 'excuse' for a cut, like now

Is the decline in PCE 'for real'? Well, the cyclical 'PCE' is 2.2% but slowing

Many sectors have flattened/slowed, but the trimmed mean is still at target

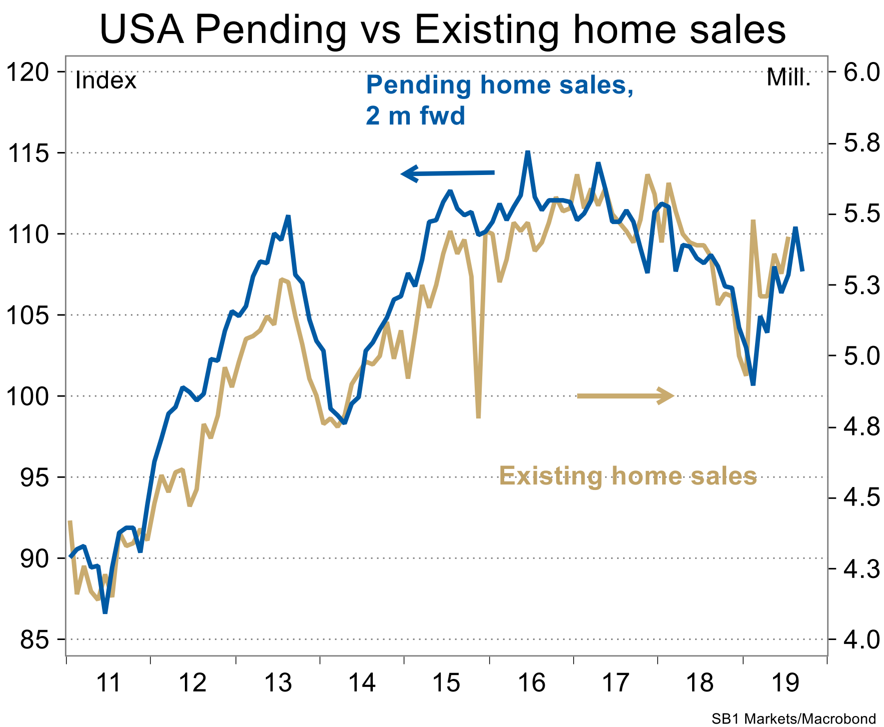


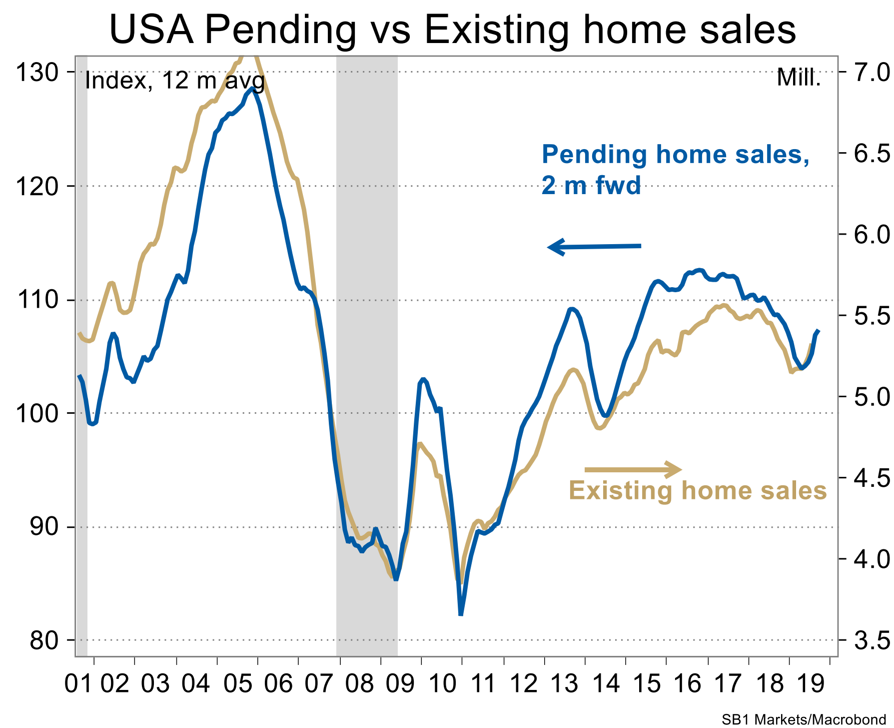


- Durable goods and cell phones and used vehicles are dragging prices down

Pending home sales down in July but trend is still strong

Pending sales down 2.5% July, are up 7% from the Feb trough – still 5% below the ‘16/17 level

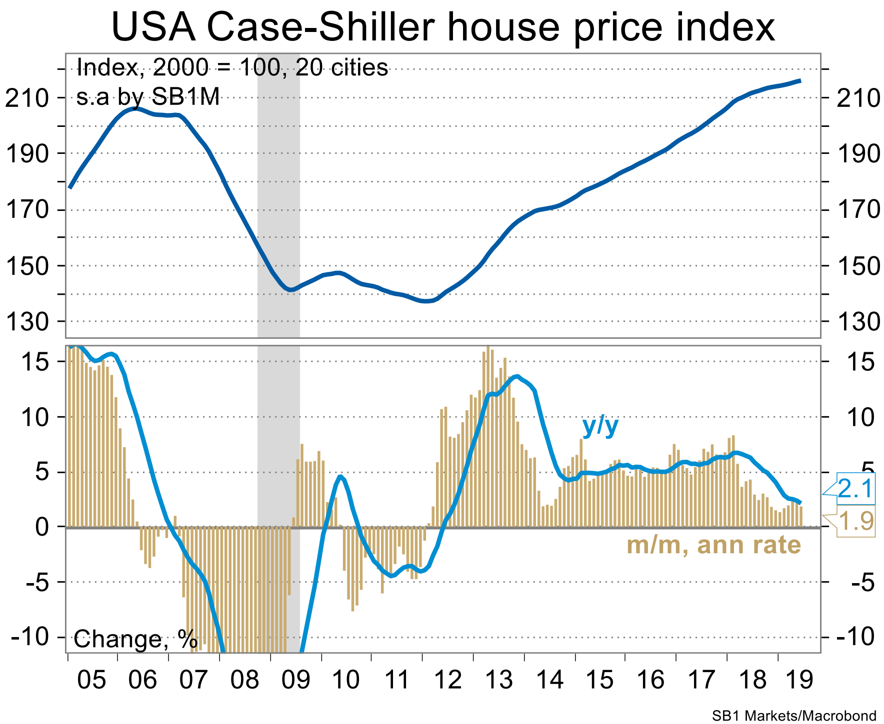


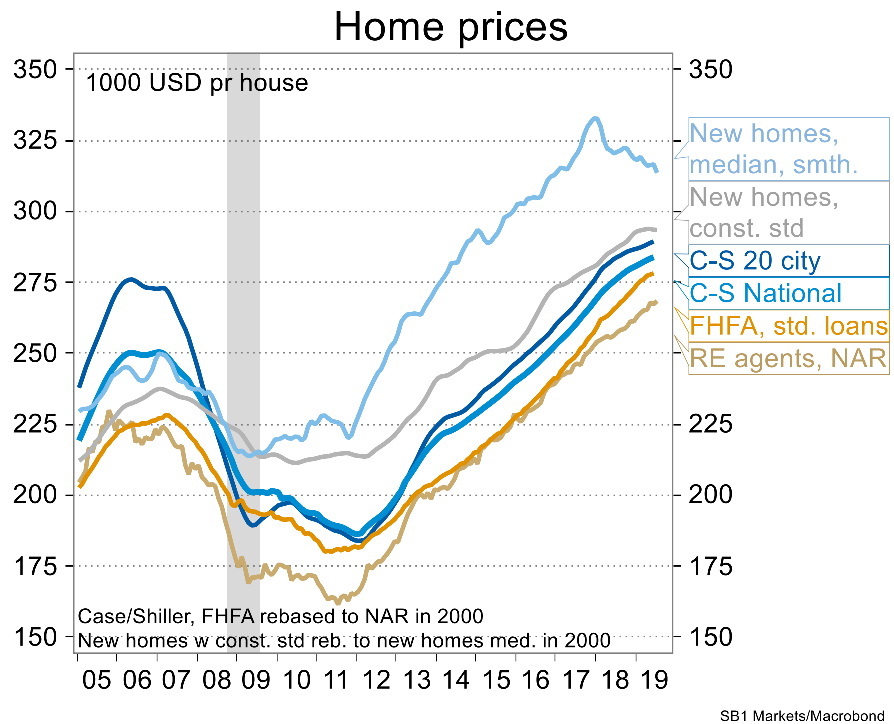


- Pending (existing) home sales were expected unch
- Pending (agreed) and actual sales are usually quite well correlated, with pending leading 1 -2 months on the actual transactions. Both have been recovering so far in 2019
- Most housing market indicators are pointing upwards, probably supported by a steep decline in mortgage rates – and none are pointing down

A 2% house price inflation reflects a steady housing markets but no take-off

C-S house prices rose 1.9% ann. in June, softer than in May. Prices do not signal thriving demand





- The Case-Shiller 20 price index rose by 0.15% m/m (1.9% annualised), a tad stronger than expected. Inflation has turned slowly up since January, following a slowdown in 2018. Annual growth still down to 2.1%, from a 6-7% in early '18
  - » Other house price indices suggest that price inflation has slowed marginally recent months (check next page)
- The CS 20 city (nominal) avg is some 5% above the 2006-peak level. The national avg (including more than the 20 cities) is 13% above the peak (while the real price levels are well below previous peak and much lower vs household income)

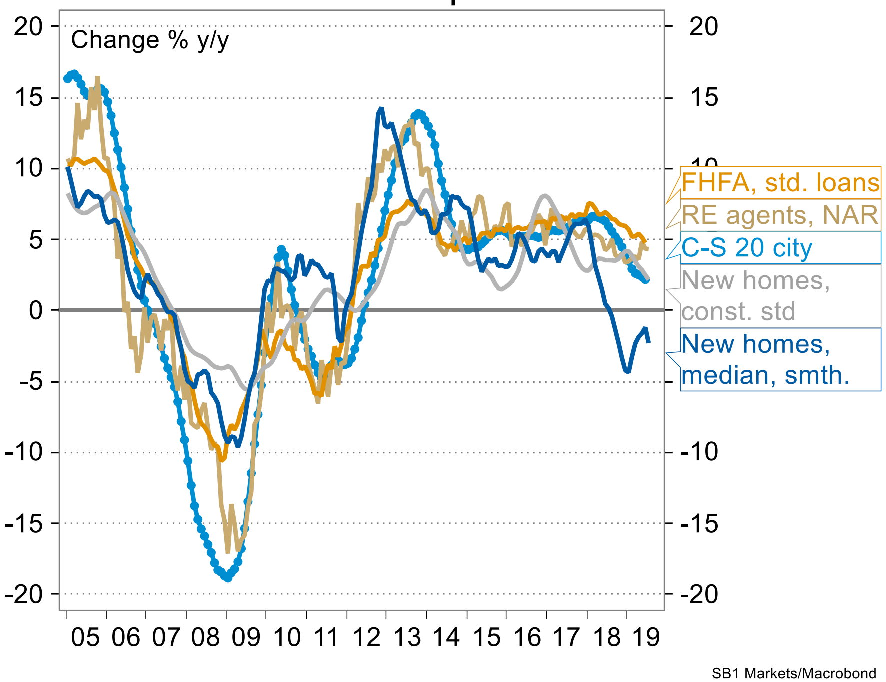
We are making an extra seasonal adjustment of the S&P Core Logic/Case-Shiller price indices as there are a significant seasonality left in the 'official' seasonally adjusted data

SpareBank 1 MARKETS

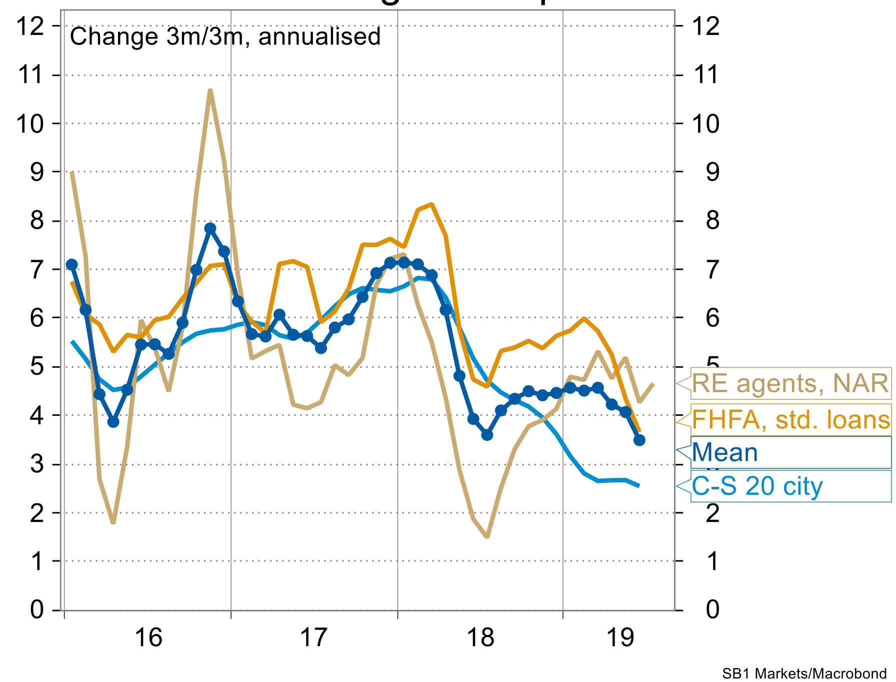
House price inflation is (probably) softening, despite lower mortgage rates

The realtors (NAR) are reporting steady growth, FHFA and C&S indices are weaker

Home prices



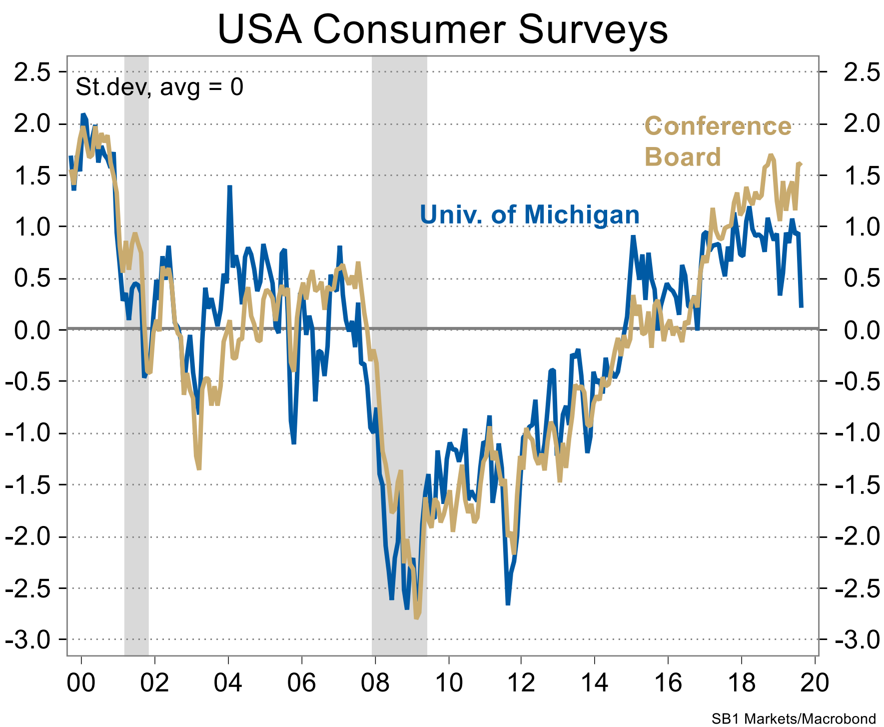
Existing Home prices

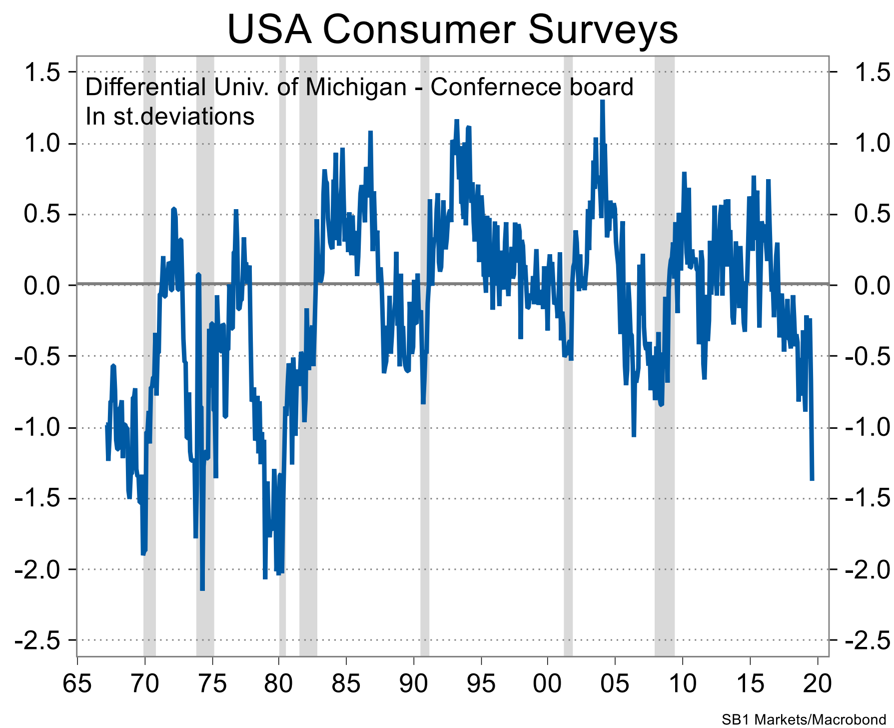


- The FHFA index (for homes financed by state guarantied loans) rose moderately in June, underlying growth (measured 3m/3m) has cooled the past 3-4 months, to below the 2018 trough
- The realtors' index (NAR), which is more volatile, reported solid growth in July, after zig-zagging in May/June. Underlying growth is holding up well, at 4.5% (3m/3m)
- The C&S index is more modest than the others. Keep in mind that the 3m/3m rate above is somewhat lagging
- New home prices have bottomed out, still declining y/y

Mixed consumer surveys, Conf Board's kept up, UoM fell even more than 1st rep.

Conference Board just marg. down, and better than expected. However, U of Mich fell 'dramatically'

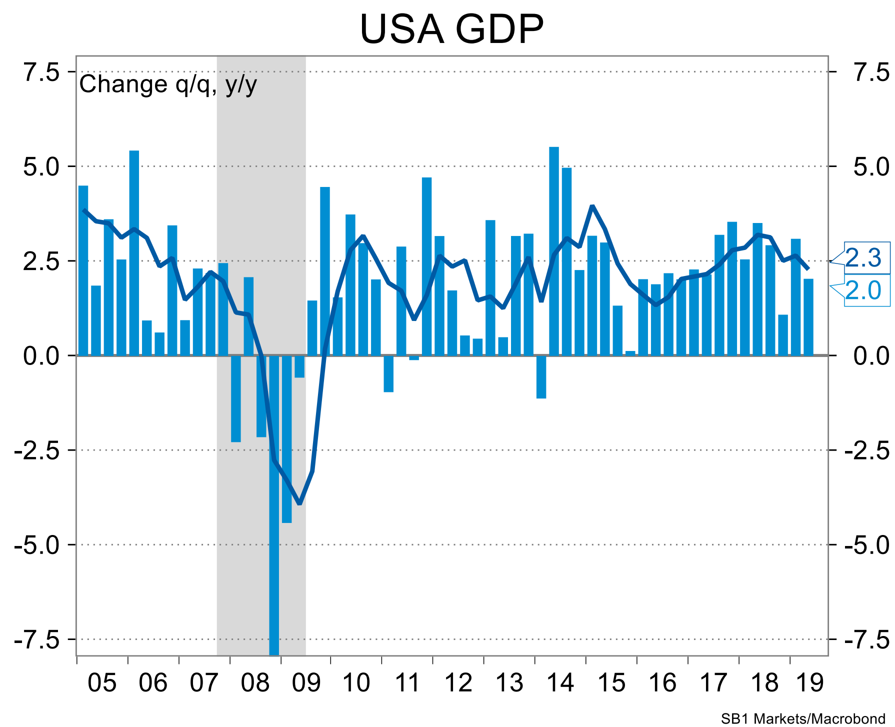


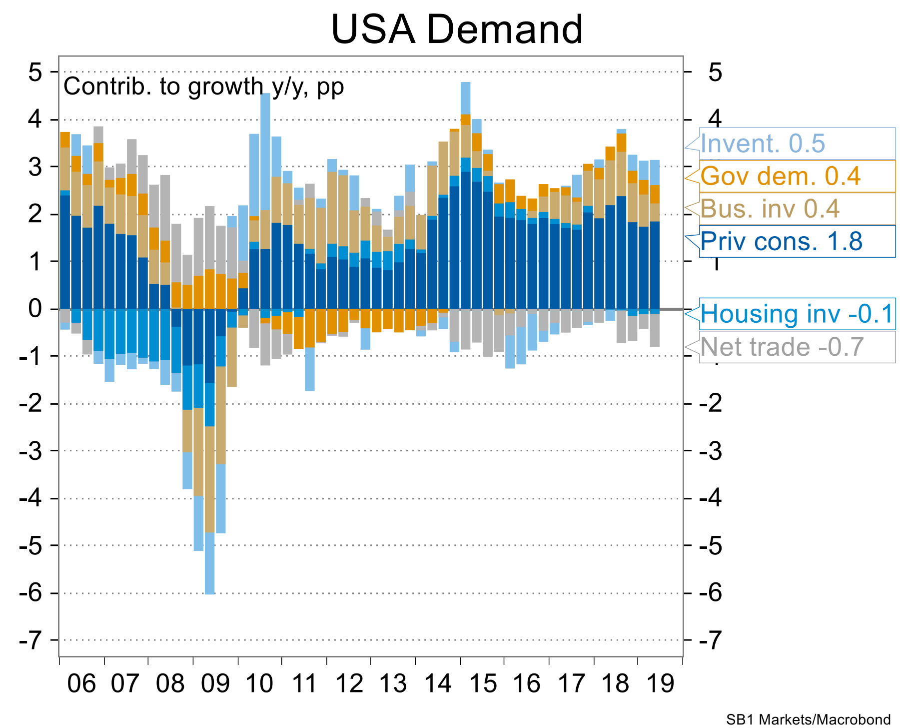


- Conference Board's consumer confidence index fell just marginally (-0.7 p) to 135.1 in August, after soaring in July. The index is at the 5th highest level since 2000, in contradiction to the recessions fears which is spreading across market
- University of Michigan's sentiment survey fell even more than first reported, down to 88.8 vs. the initial estimate at 92.1, down from 98.4 in July, a 0.7 st.dec decline (a 1/6th of a normal cycle). The setback was the largest since Dec 12, and of a size that normally only happens once every 3 – 4 years (the 17th largest since 1960). The differential between the two surveys is unusually large. The UoM index may be more sensitive to downturns in financial markets, and is leading the CB survey somewhat. And 'something' happens when the cycle is maturing and it is heading towards a recession, check the chart on the lhs. As a recession warning, the 'spread' is not that bad
- Still, both surveys are above their long term averages and they do not signal a sudden halt in consumption. But the chart above…

Q2 growth marginally revised down, to 2.0%

GDP growth has slowed (after previous revisions)

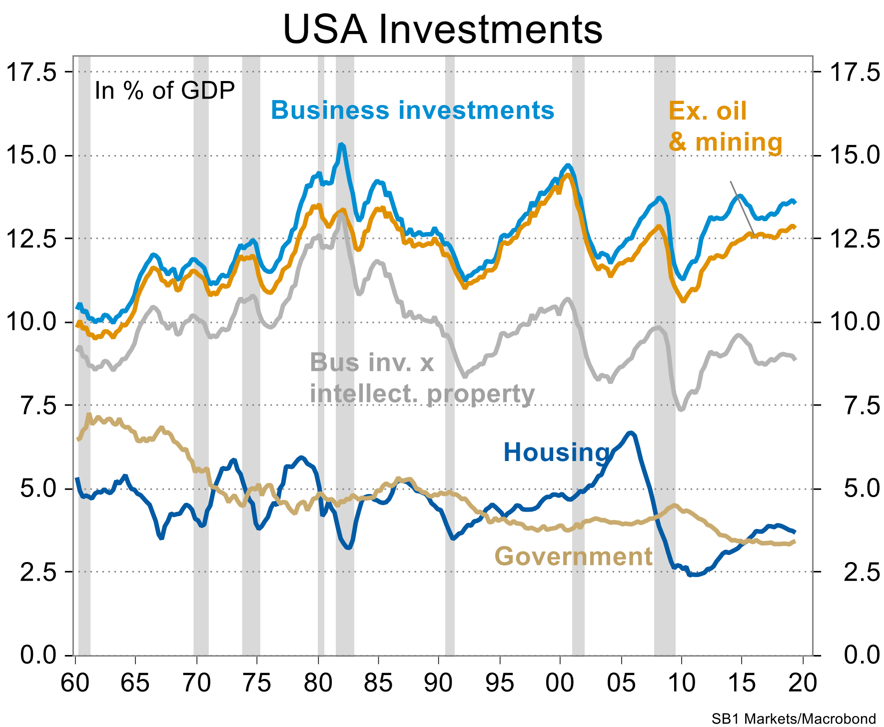


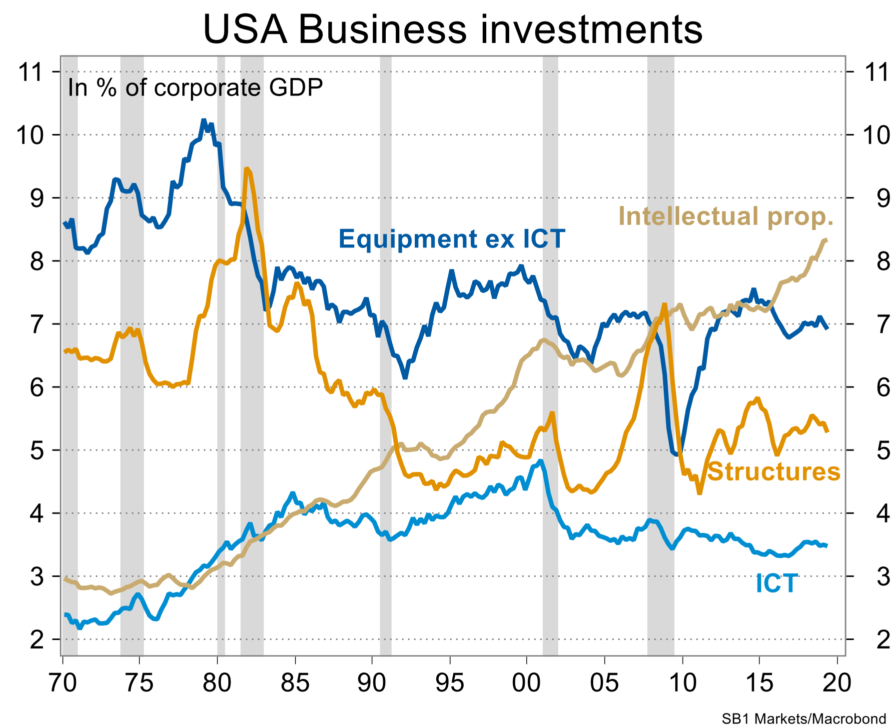


- GDP grew by 2.0% in Q2, a tad below the first estimate at 2.1%. Consumption growth was revised up to a 4.7% pace, public demand was a tad weaker, but still unusually strong. Consumption contributed by 3.2 pp to GDP – and other contributions were in sum negative, most from net trade & inventories

Housing investments marginally down, business investments are peaking?

IP investments are still rising sharply, masking a decline in equipment/structures

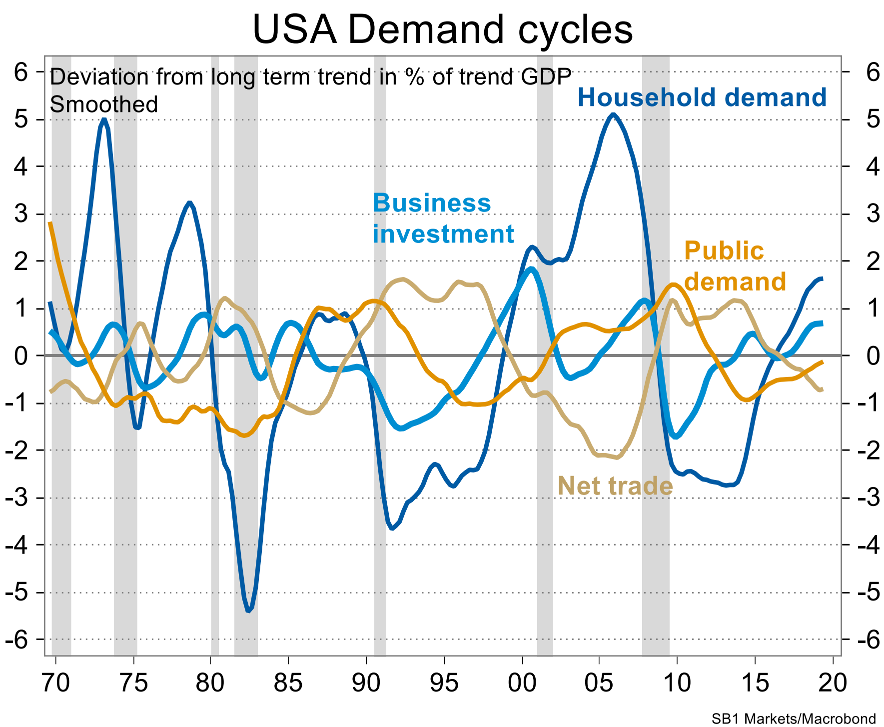


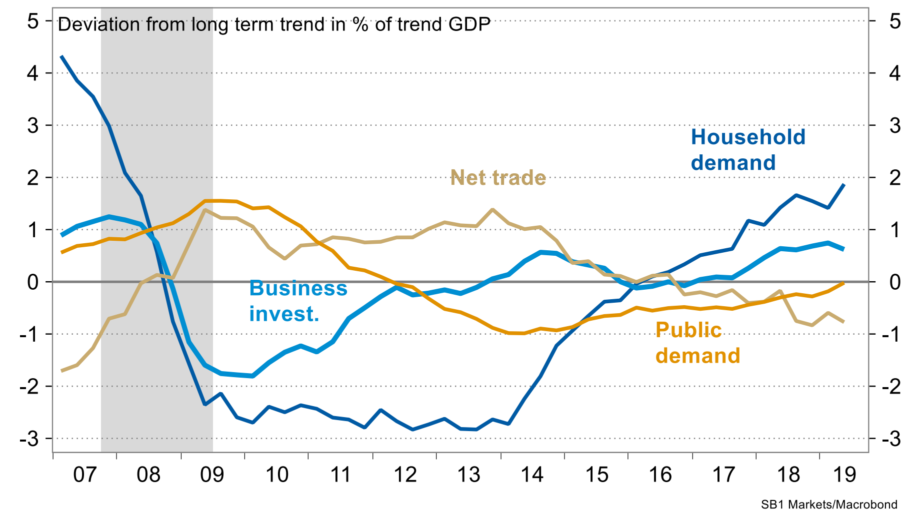


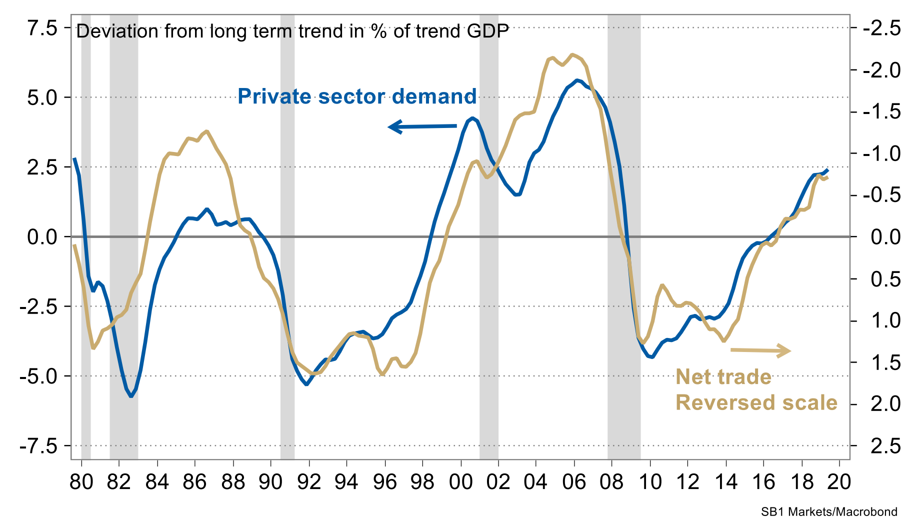
- The decline in total business investments was the first since Q4 '15. Oil investments have been the main driver for higher business investments recent quarters (there too) but have fallen slightly the past 4 quarters. In Q2, bus. investment ex oil fell marginally too
  - » IP/software investments are 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 possibly be a large one (but several housing recessions have started at approx. the same level of the housing investment/GDP ratio)

Households have been the main demand force

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





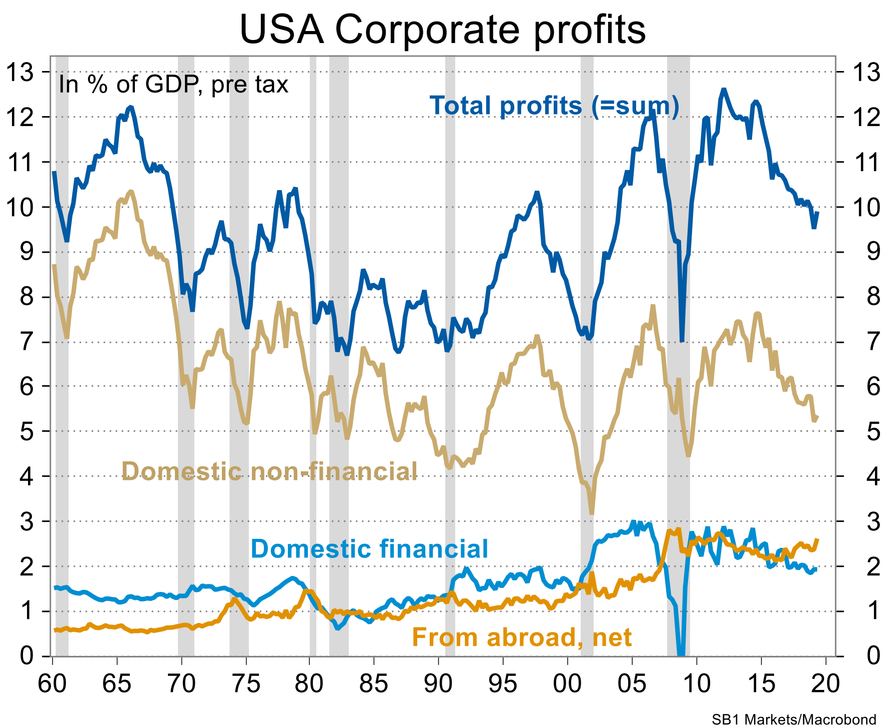


- A strong USD is not to blame for a negative growth contribution from net trade the past years, a strong US is rather a result of strong domestic demand
  - » Net trade correlates close to the activity level in the US, or rather more precise, to private domestic demand in the US
    - Net trade absorbs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

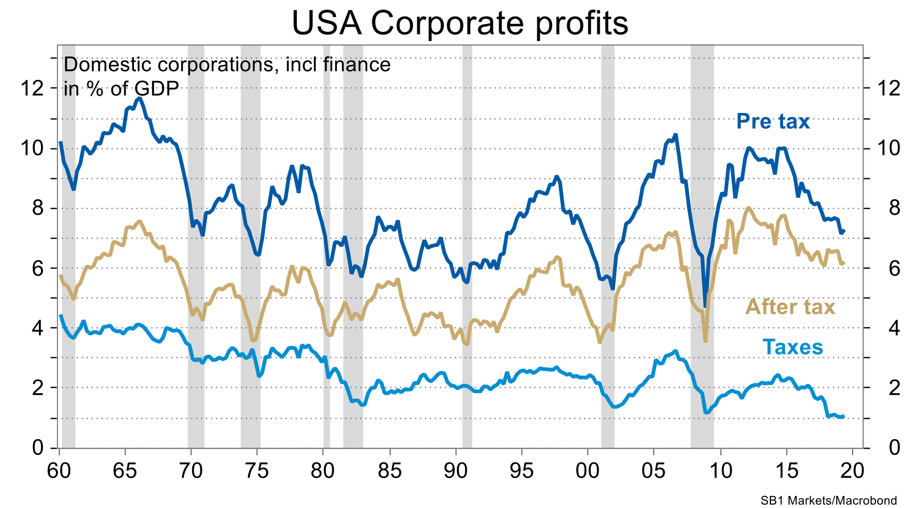
SpareBank 1 MARKETS

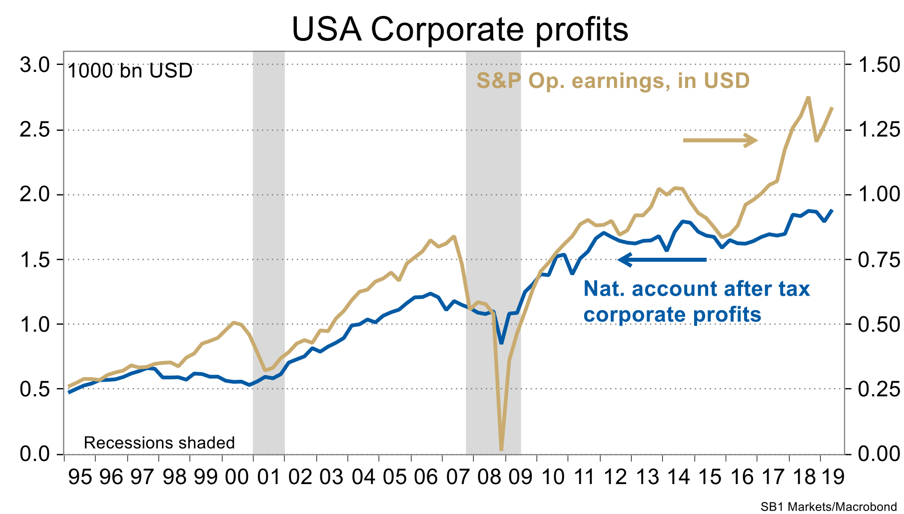
Profits up in Q2 but have flattened – and are falling sharply in % of GDP

Domestic corporate sector after tax profits are still above average, just due to the tax cuts



- Corporate profits were revised sharply down in the annual revision of National Accounts
  - » The Q1 total pre tax profit share was revised to 9.5% from 10.8% - and the profit share is trending sharply down. Household income and savings have been rev. up
- Total profits rose 5.3% in Q2, mostly due to higher profits from US companies' activities abroad (minus foreign in the US)
- The after tax profit rate for companies operating in the US ('domestic corporations') is still above average but just because corporate taxes have been cut sharply recent years

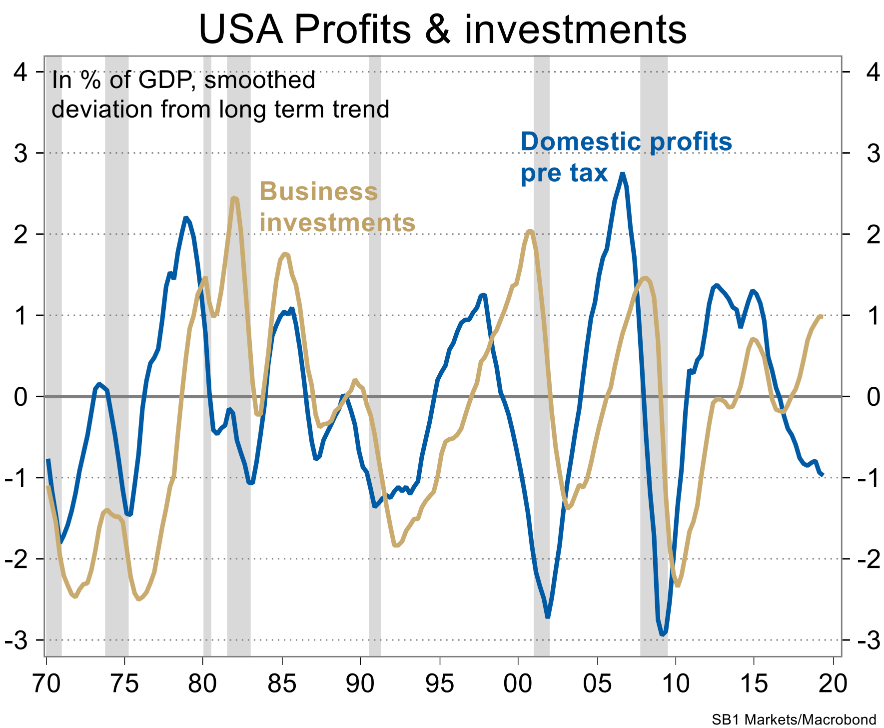


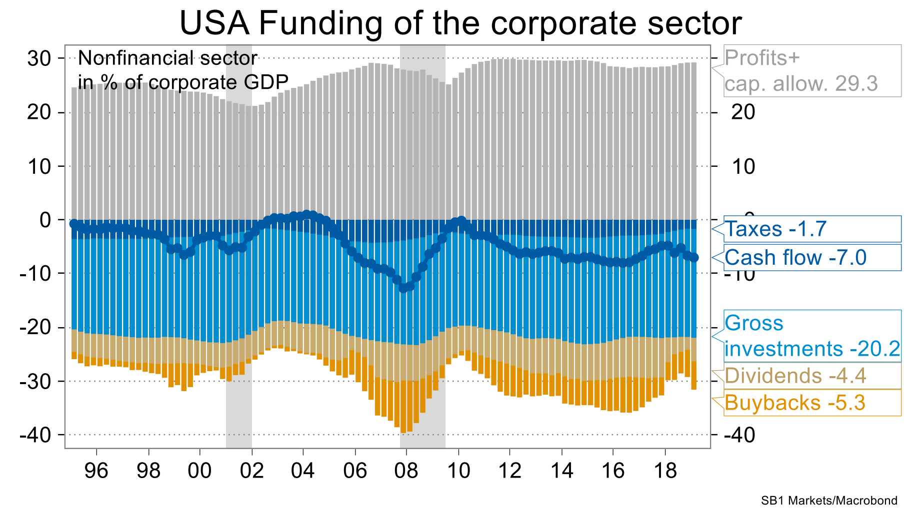


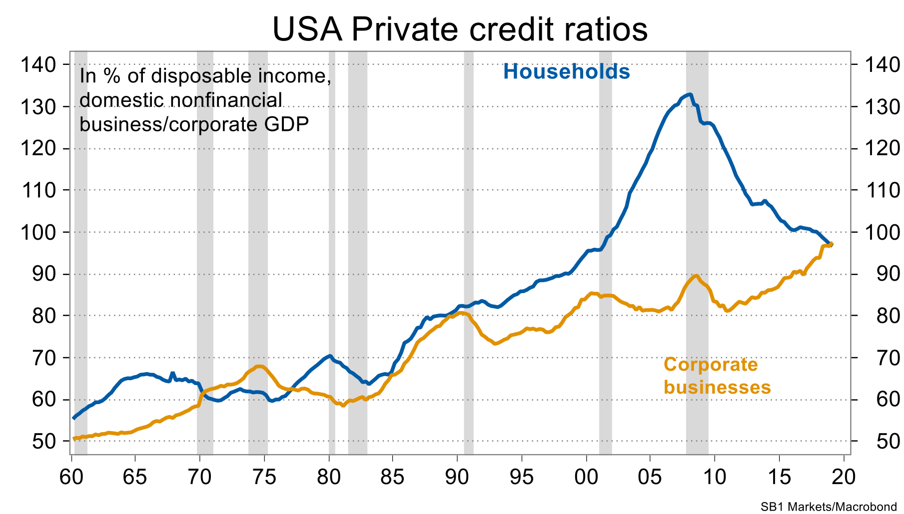
S&P 500 companies are reporting much higher growth in earnings than Nat. Acc. are able to detect. We have seen such discrepancies before, and so far S&P profits have yielded the following years, during recessions…

Profits down – and investments will follow suit, as usual?

Probably, investments are almost always lagging profits. The cash flow is deep in red, and debt high





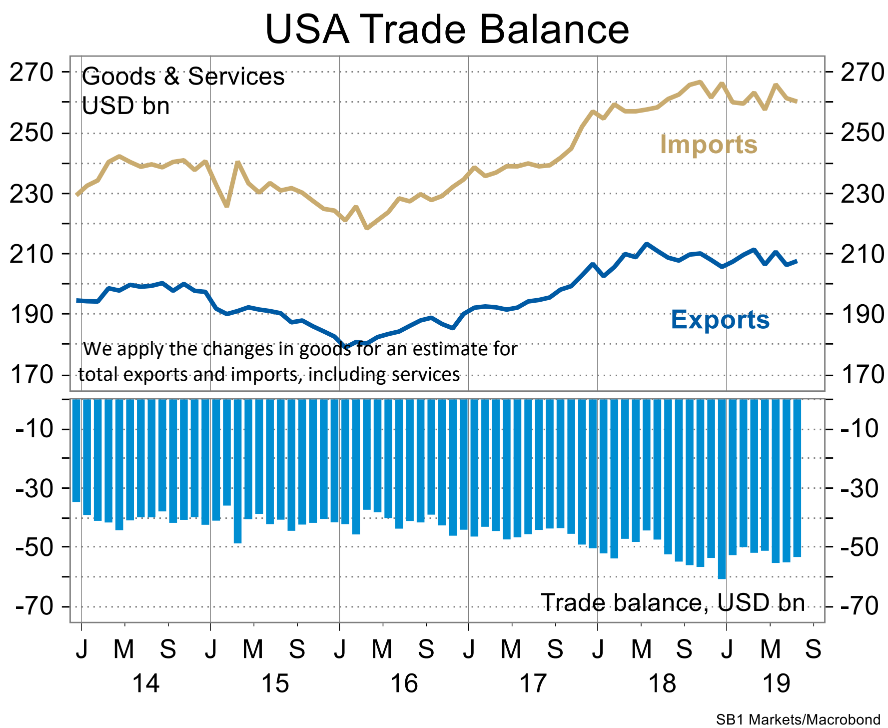


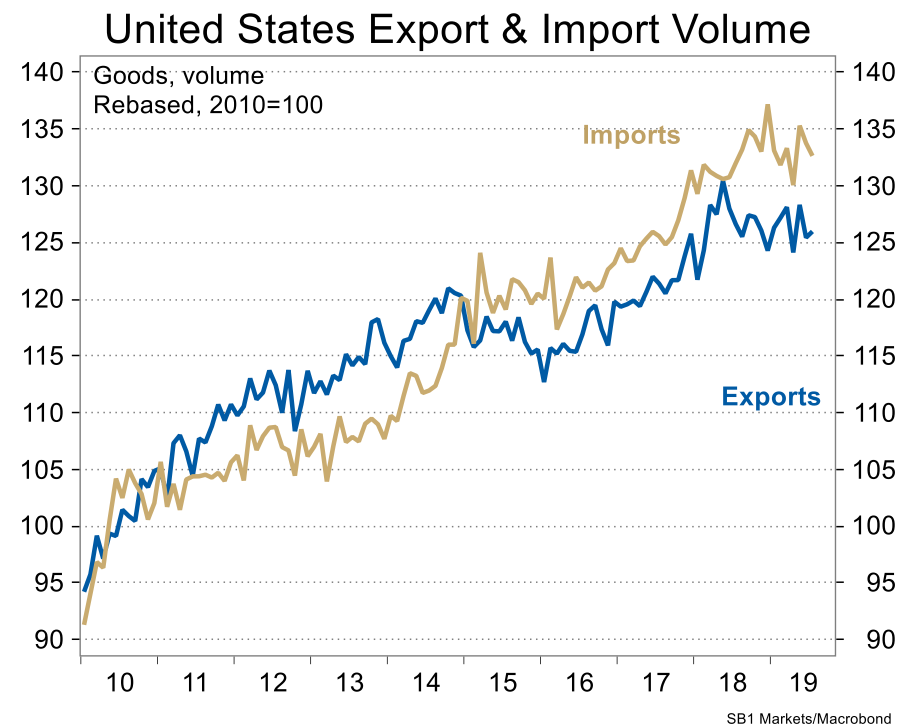
- Business investments are not super high but high, while profits are below a normal level
- The non-financial corporate sector cash flow is negative, by almost the same amount as the companies spend on stock buybacks
- The debt/value added rate has climbed steeply recent year. Without buybacks, the debt ratio would have fallen sharply the past 15 years, to close half the actual level

The upper right chart has not incorporated the downward revised corporate profits

The trade deficit shrank marginally in July

Both imports and exports are trending slowly down, no dramatic trade war impacts

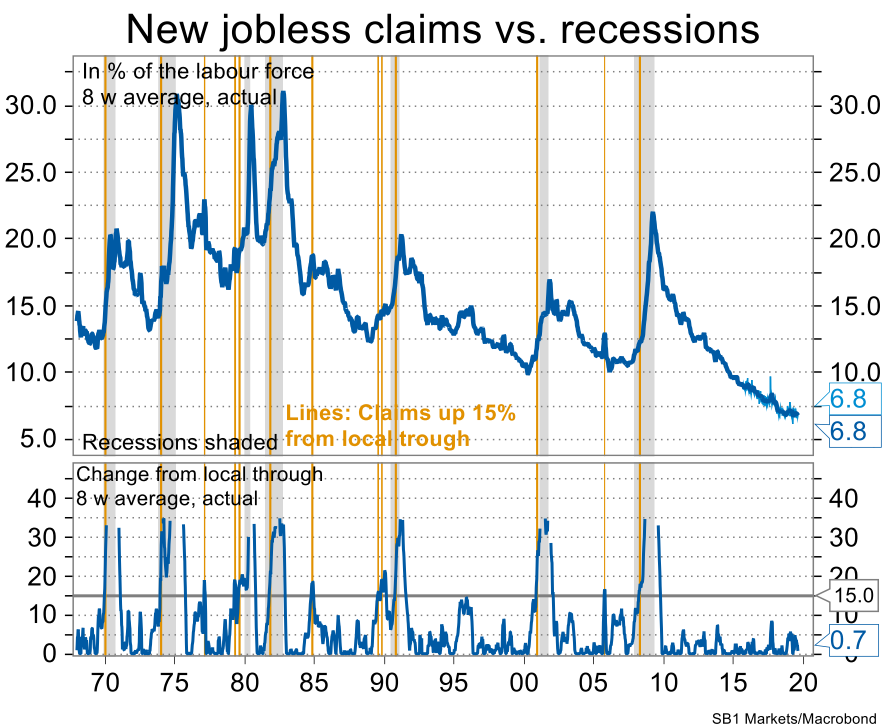


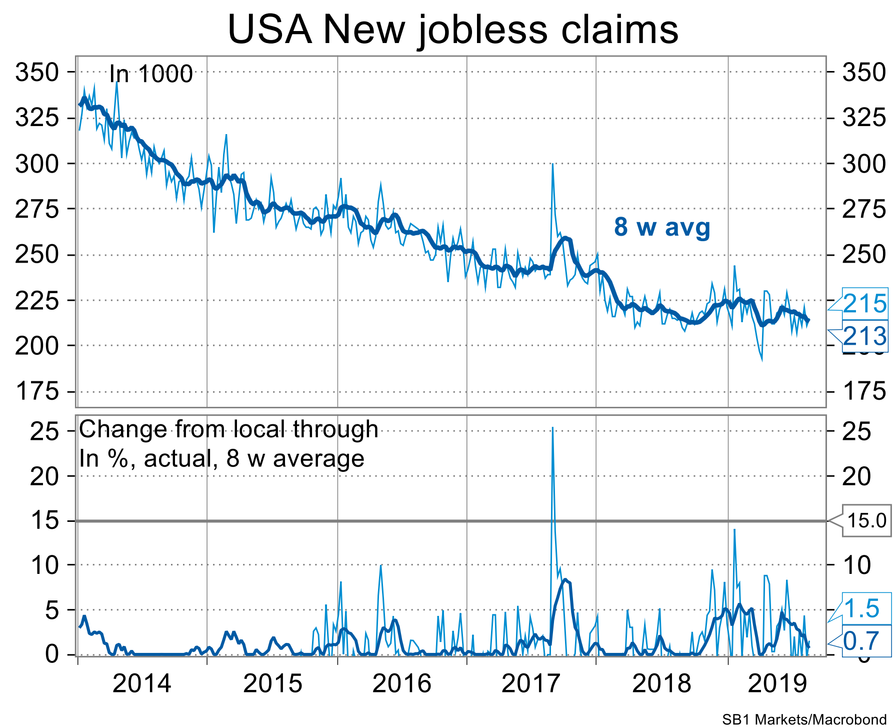


- The advanced trade data (goods only) indicates that the overall trade deficit was marginally slimmer in July, at some USD 53.5 bn
  - » Imports fell both in nominal and volume terms. The trend is down, at least in value terms. Possibly due to the escalation of the trade war
  - » Exports rose marginally, have been heading down since mid-2018, both in value and volume terms – but just marginally
  - » In Q2, net exports were a negative drag to GDP growth at 0.8 pp q/q. Data into Q3 indicate a close to zero contribution
- The deficit vs. China is reduced (no July data), no doubt due to the trade war, as imports from China is sharply down. However, the deficits vs most other countries are widening, thus, the overall deficit is widening

Jobless claims remain very low, no signs of weakness

Jobless claims edged up to 215', the 8 w average is very low, at 213'. The labour market is tight

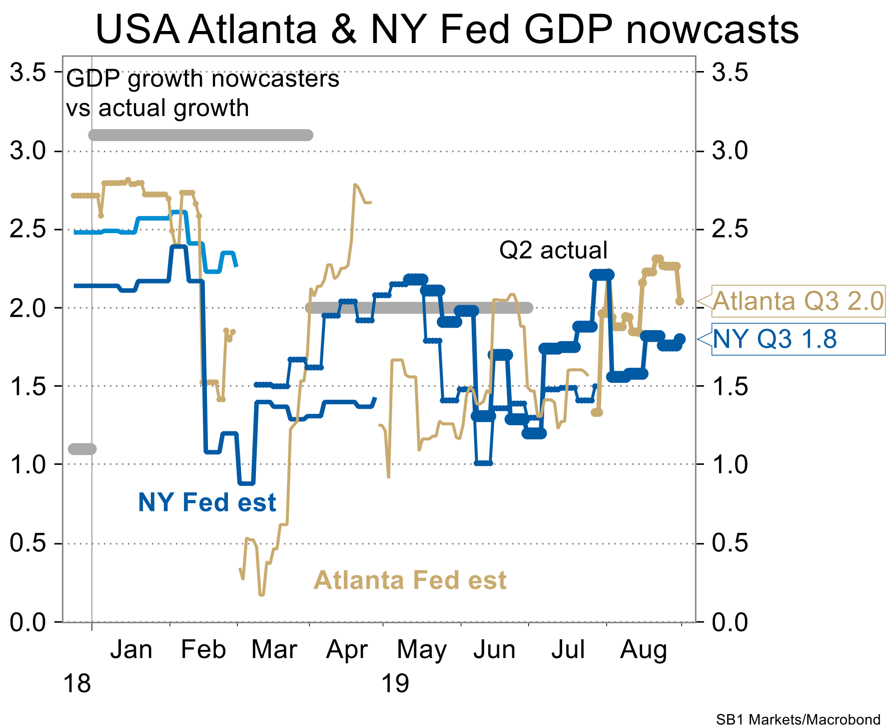


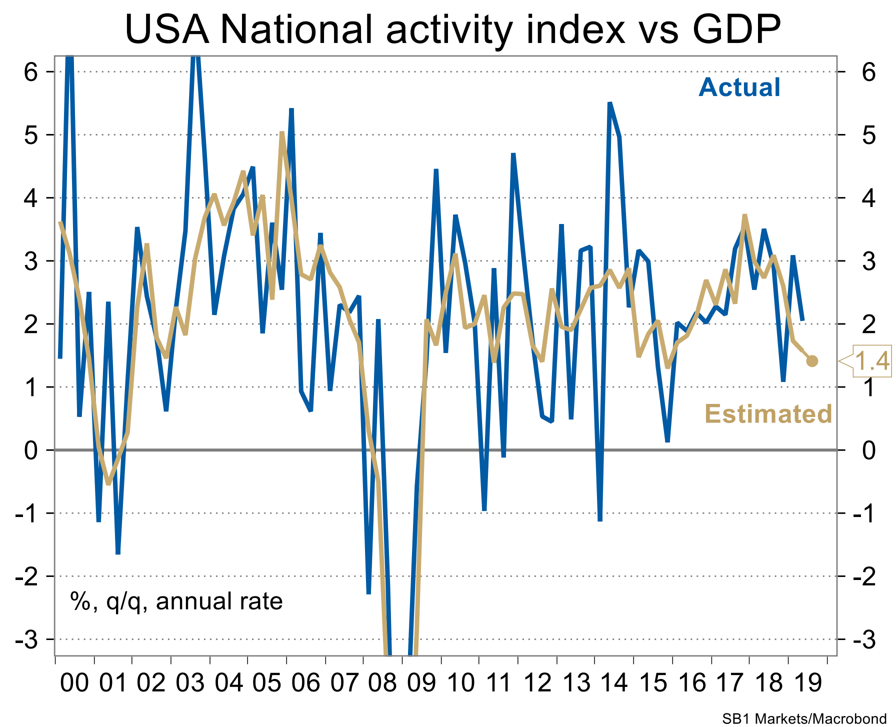


- A more than 15% increase in jobless claims (measured by the 8 week avg) is usually a good indication of a recession, and a yellow 'recession' warning line is to be drawn, check the chart to the left. So, no reason to worry now?

Q3 growth close to 2% - or below

The nowcasters are noting 1.8-2.0% GDP growth in Q3, the National Activity index at 1.4%



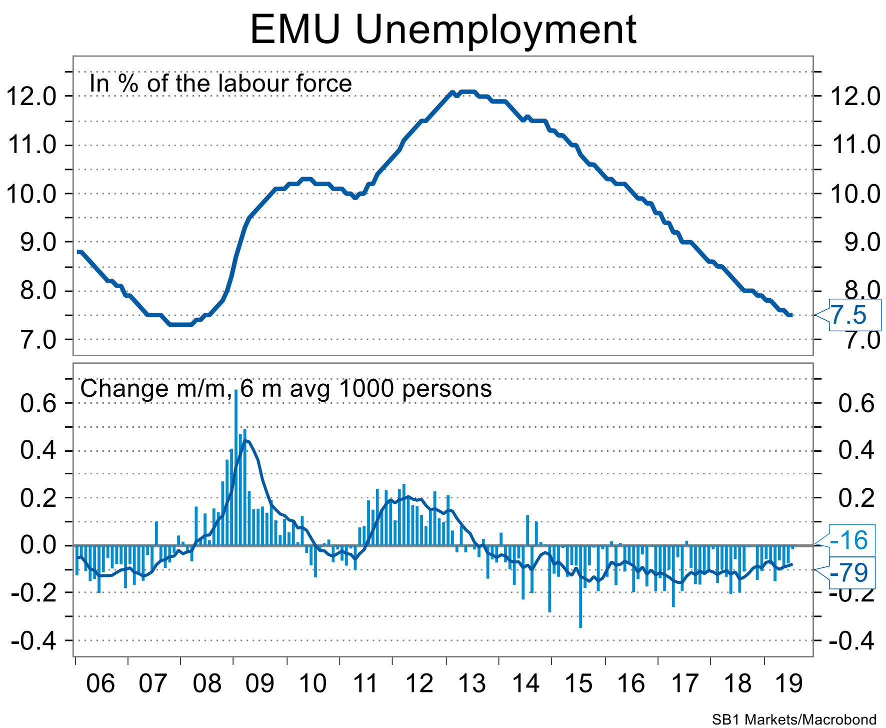


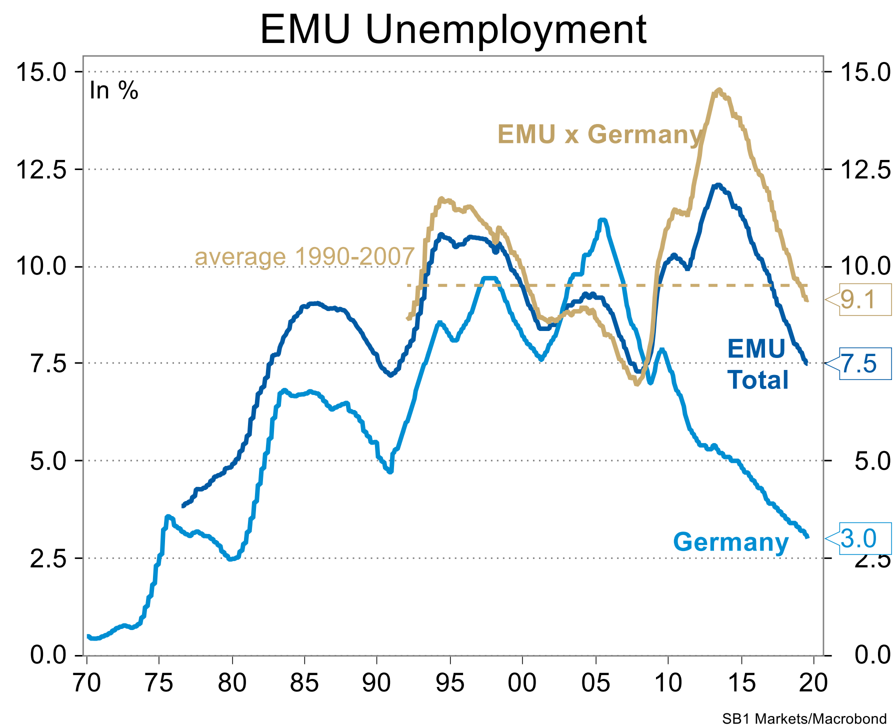
- The National activity reports 1.4% GDP growth in Q3 vs the 2.1% in Q2 (However, the index was too downbeat, at 1.7%)

SpareBank 1 MARKETS

Unemployment flat in July, the underlying decline may be slowing

Unemployment flat at 7.5% in July, just 16' less unemployed





- The unemployment rate was flat at 7.5% in July, in line with expectations. The number of unemployed fell by just 16' persons, a modest decline vs the 6 m avg at close to 80'. The long term trend is still downwards but the pace has declined somewhat
  - » Unemployment has been declining in spite the soft patch that the Eurozone is in (some sectors, at least). Unfortunately, unemployment is not a leading indicator, it is at best a coincident one. Nonetheless, the decline in unemployment rate during the economic slowdown may also mirror that other sectors so far are persistent to the dip in manufacturing, as the PMIs and some other surveys are reporting
- Unemployment in total EMU is well below the 1990-2007 avg, and it has fallen below the average in EMU ex Germany too
  - » In Germany, the unemployment rate ticked down to 3.0% in July, the lowest level in almost 40 years

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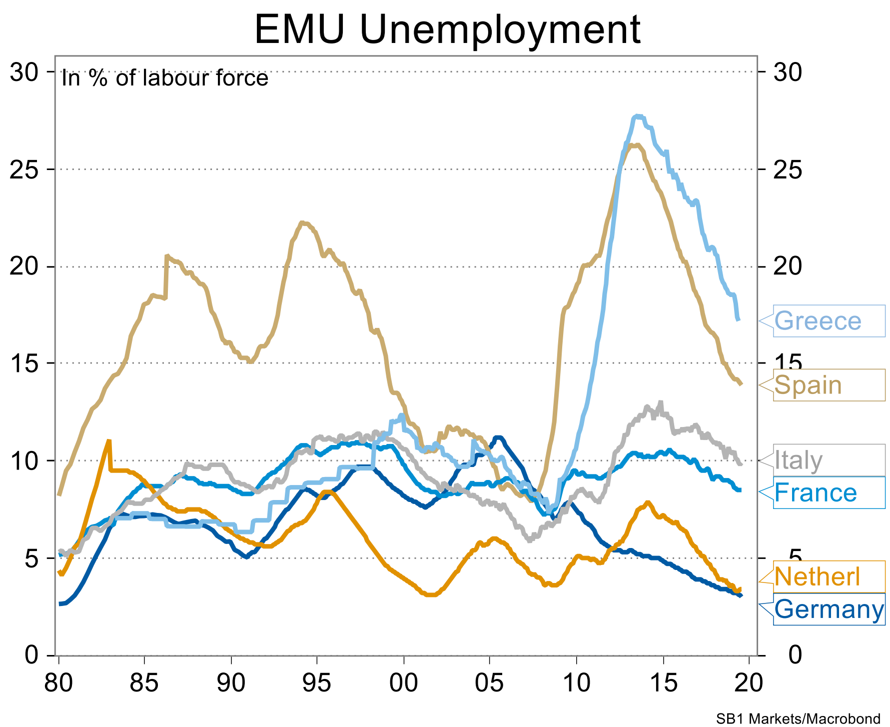
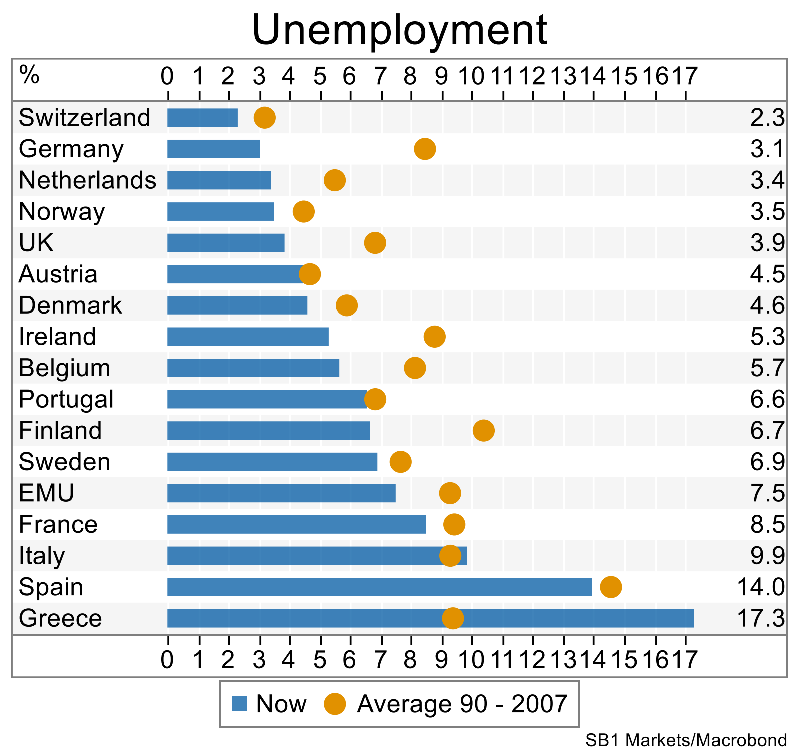
Unemployment is heading down everywhere

Unempl. is higher than 'normal' (avg 1990 – 2007) only in Greece (and marginally in Italy)

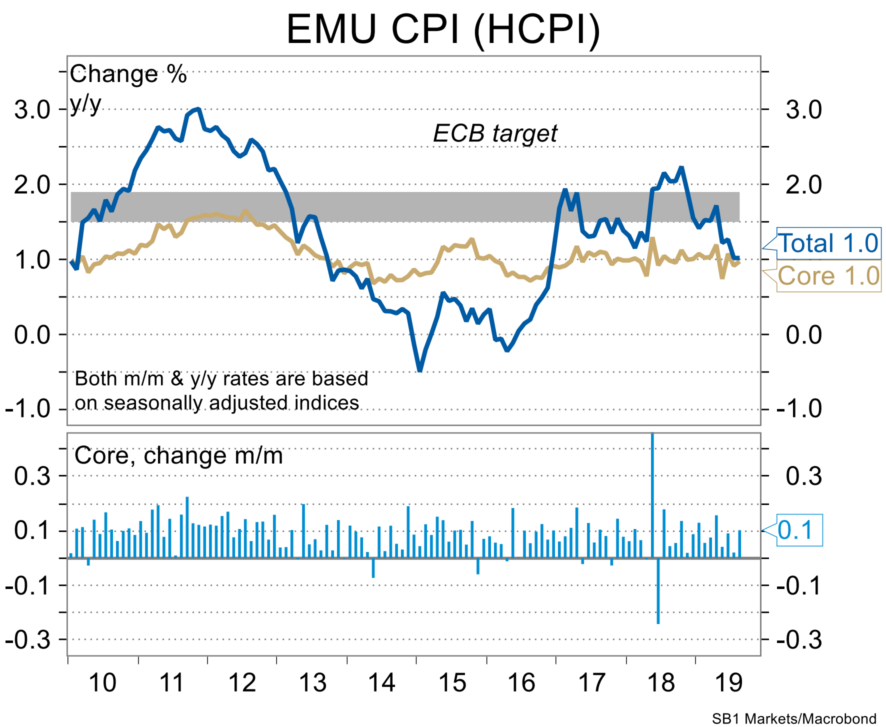


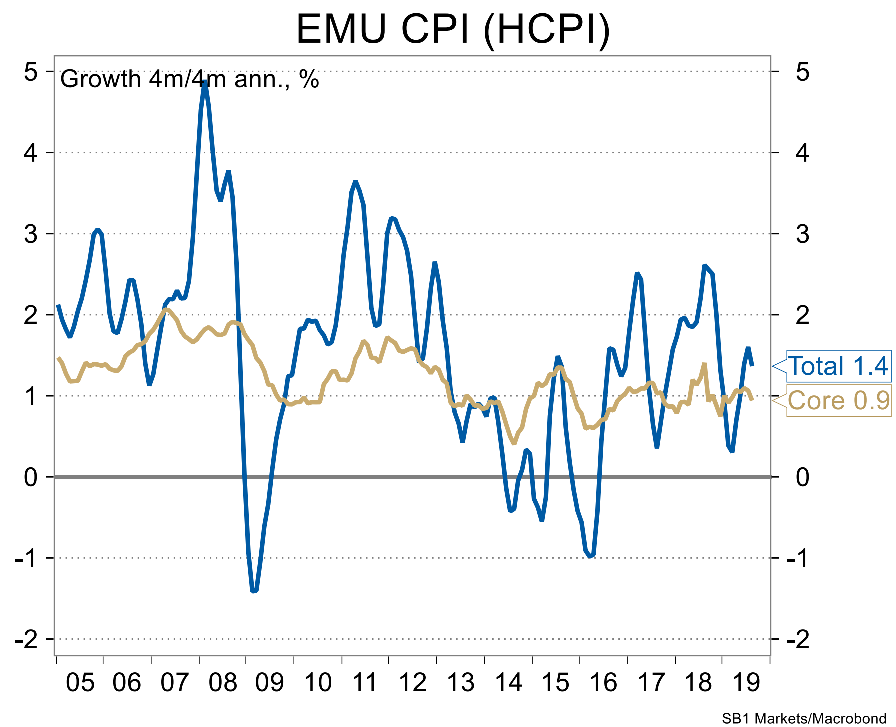


- Unemployment rates in Greece and Spain have fallen sharply since 2013, from awfully high levels. Unemployment is still very high in Greece, at 17% (down from 28% in 2013!). Spain down from 26% to 14%
- Unemployment in Germany and the Netherlands have fallen to very low levels, limited downside potential!
- Employment rates are in general high – but lower than before the GFC in Greece, Spain and France (but not in Italy)

Core CPI inflations remains meagre, one inch up to 1.0% in August

Core inflation rose 0.1 p in August, total CPI was flat at 1.0%, bolstering the case for the ECB to act





- Core CPI rose 0.1% m/m in August. The annual rate bounced back to 1.0%, up from 0.9% in July and in line with expectations. Core inflation is trending flat (and even downward recent months) and growth measured 4m/4m is low
  - » Subdued inflation is increasing the pressure on ECB to step up support
- Total CPI growth was unchanged at 1.0%. The oil price decline in the spring has sent total inflation down from above 1.5%. We expect headline inflation to decline further the coming months, to well below 1%

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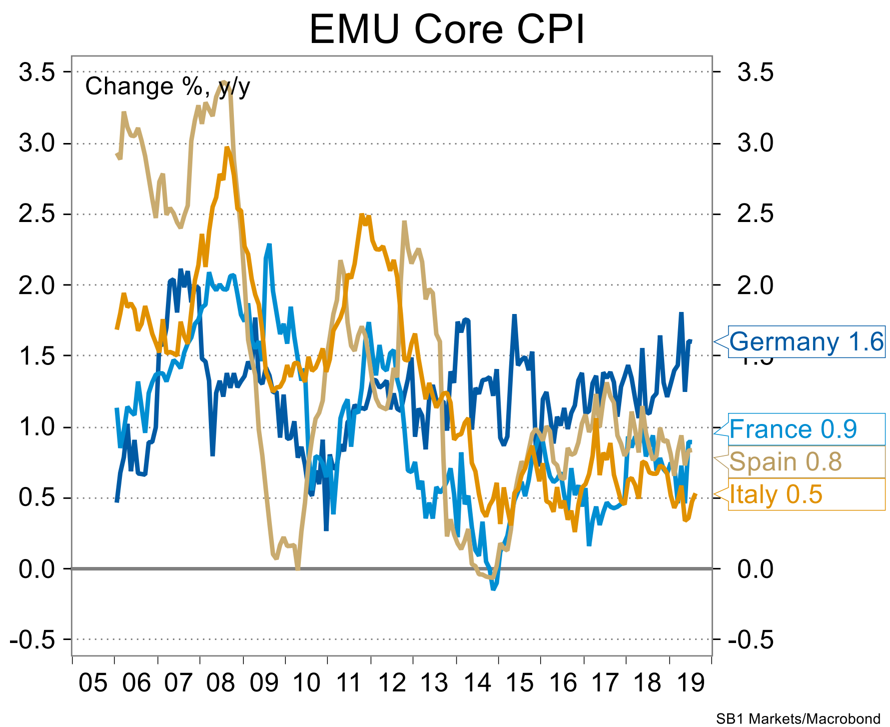
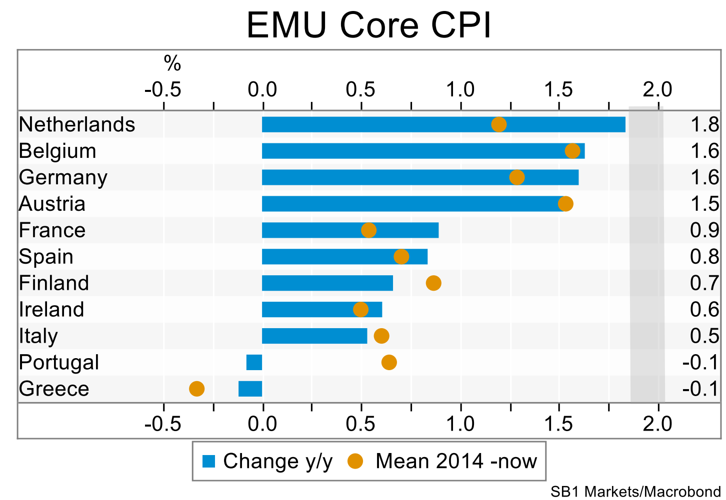
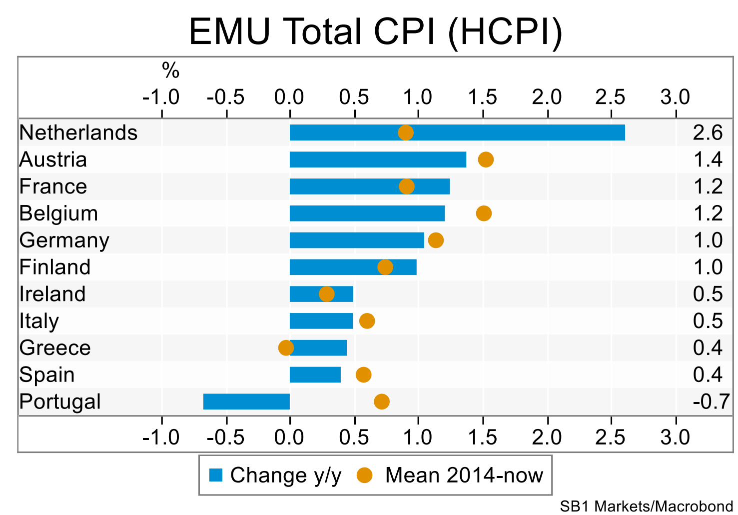
Core inflation below target almost everywhere

Inflation is lower than 'normal' just in Italy, Portugal, Greece and Finland. Germany heading up



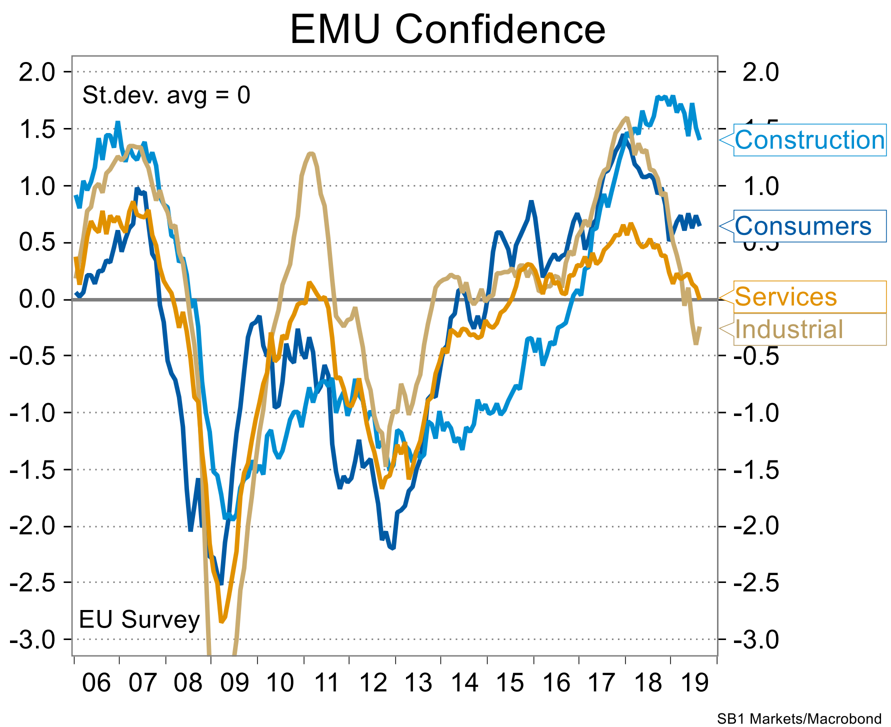
- Core inflation in Germany is up some 1.6% y/y (in July), and has no doubt accelerated
- In France, inflation is meagre at 0.9%
- In the other major countries core inflation has slowed
  - » Only the Netherlands is at/close to the ECB's price target at just below 2%

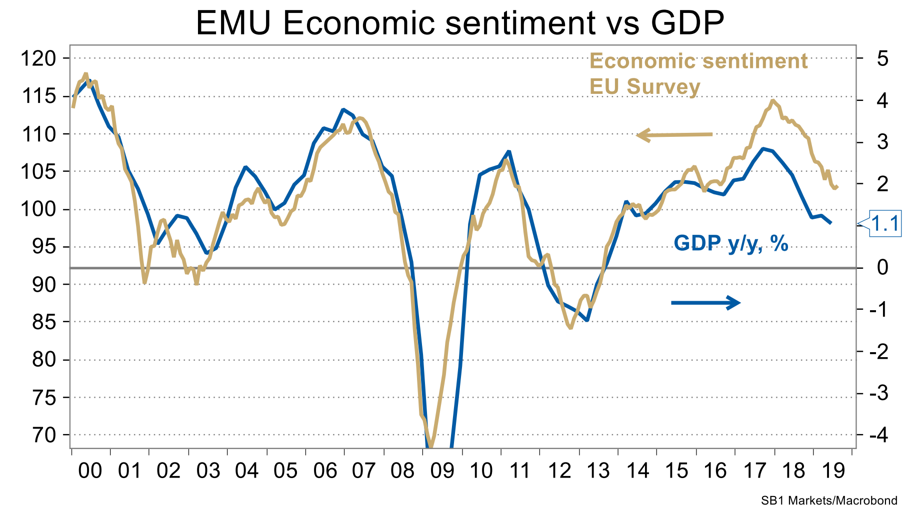


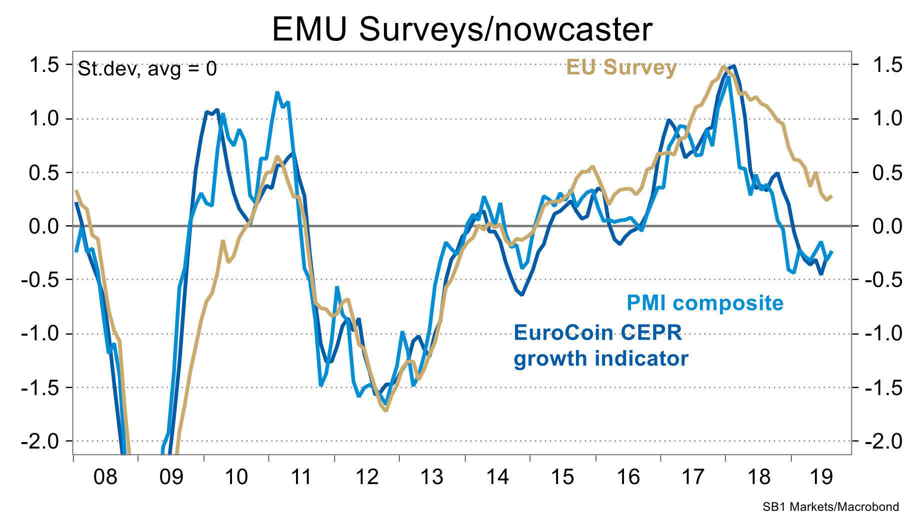


EU economic sentiment inched up in August, level far too upbeat

Surveys do not signal deteriorating conditions. However, the ECI is probably too optimistic







- Total sentiment rose marginally to 103.1 in August. The survey is still above the average level, however, it has been far too optimistic vs growth the past two years; the direction is probably more essential
  - » The survey is usually lagging the PMI and CERP
- Both the PMI and CERP have stabilized at low levels recent months, do not signal a deteriorating downturn in the Eurozone
- Huge sector deviations; manufacturing is plummeting and services are not strong either, while construction is still elevated. Consumer confidence is stable and not weak, well above avg level

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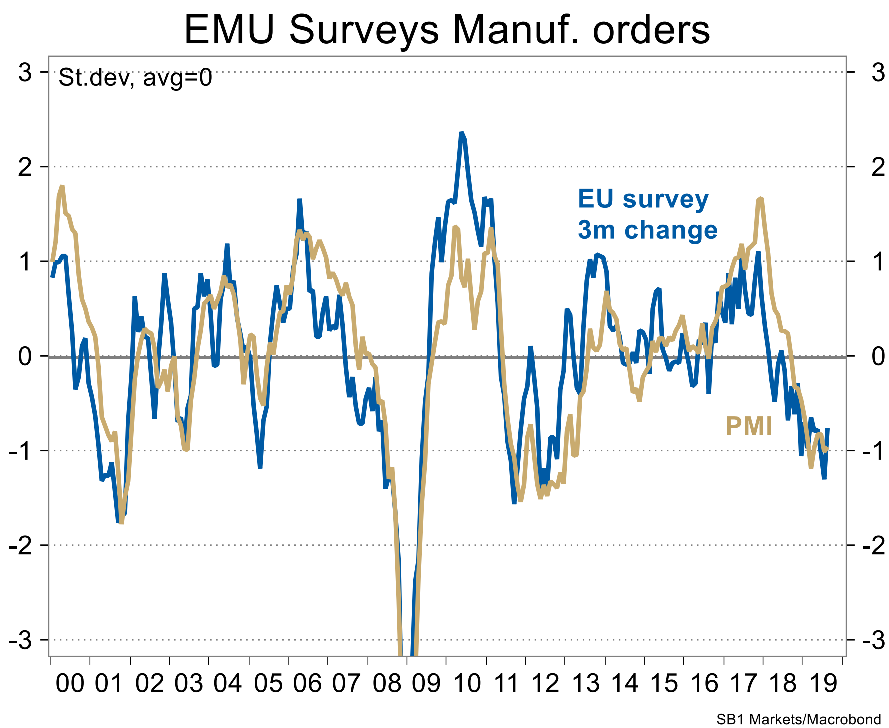
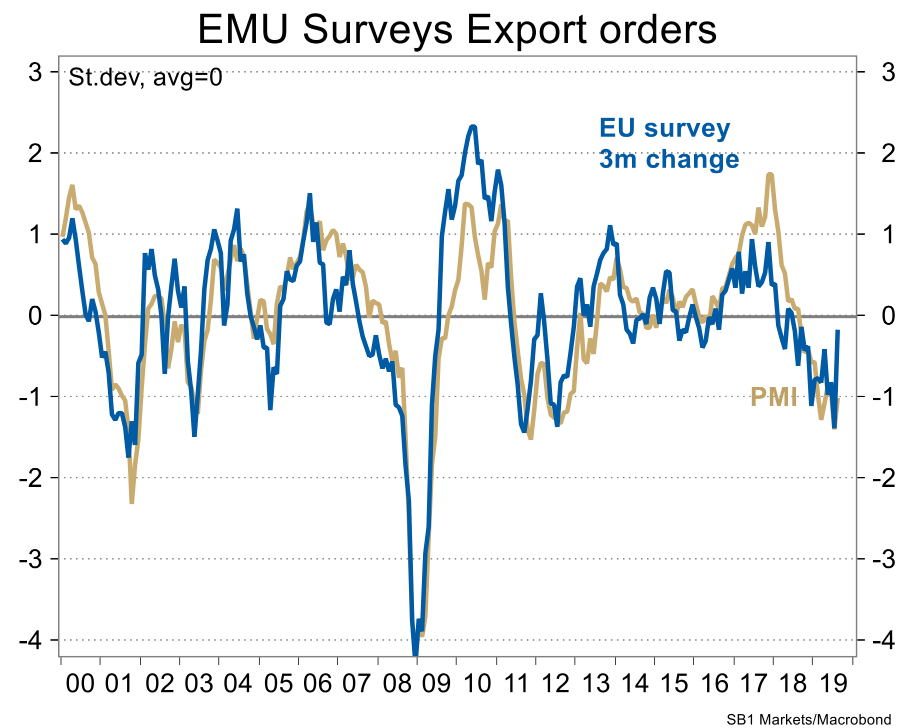
EU survey reports declining manufacturing orders but export orders less weak

Both PMI and the EU survey are at the weakest levels since the 2012 euro crisis

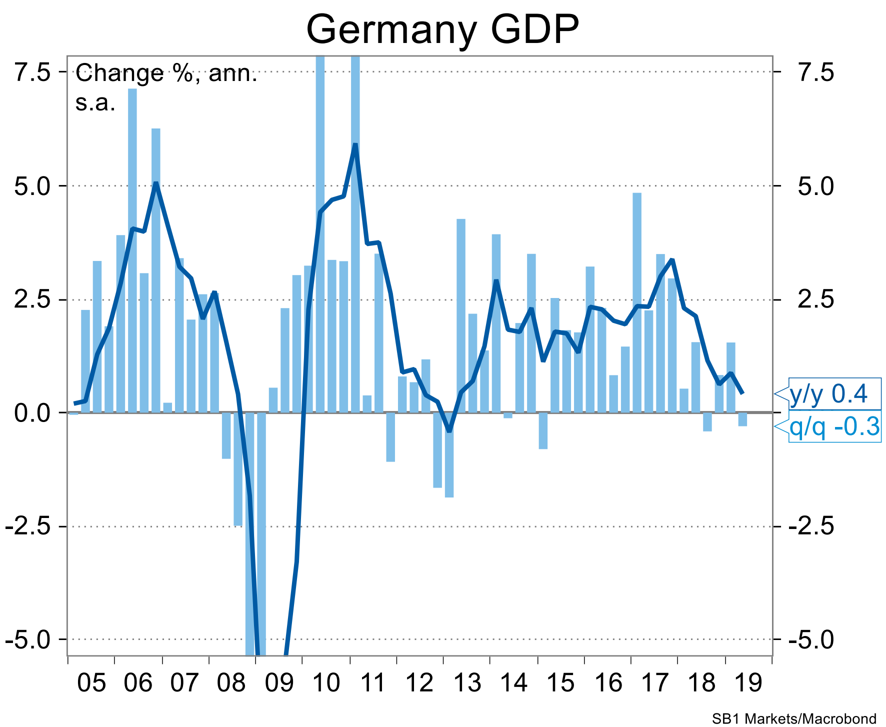


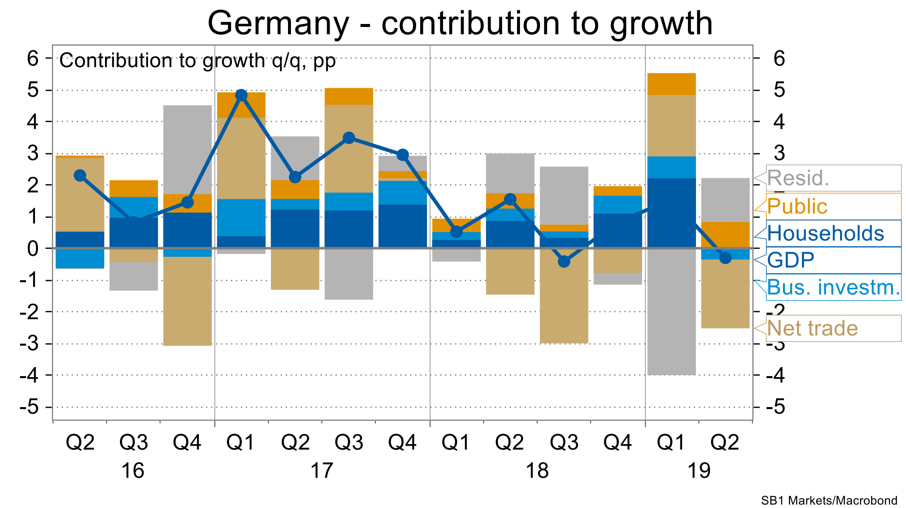


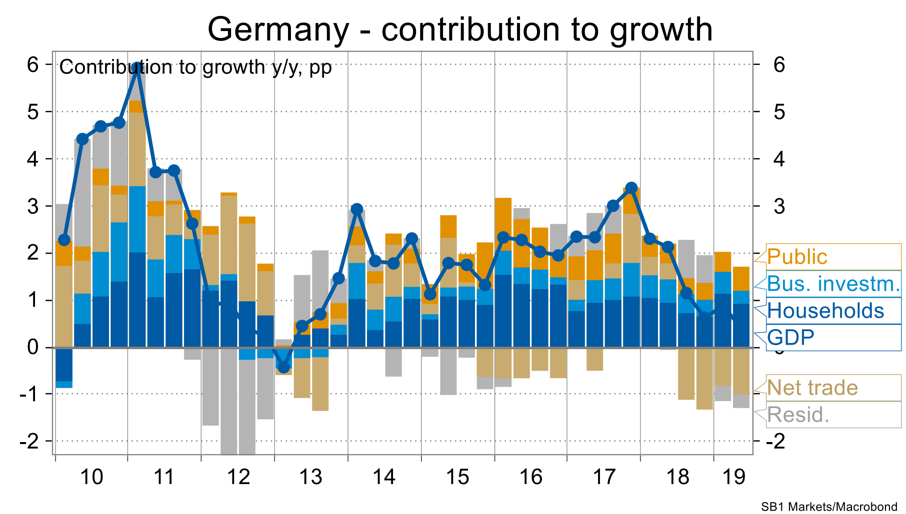
- Both total and foreign manufacturing orders have slipped. In August, the EU survey reported improved export conditions and the PMI noted a small uptick, signs of a stabilization?
- At the charts above, we compare the 3 m <u>change</u> in the EU order index to the PMI

Q2 details are not promising; muted household demand, business invest. fell

The major drag in Q2, and last y was exports, and other parts of the economy are just not shining



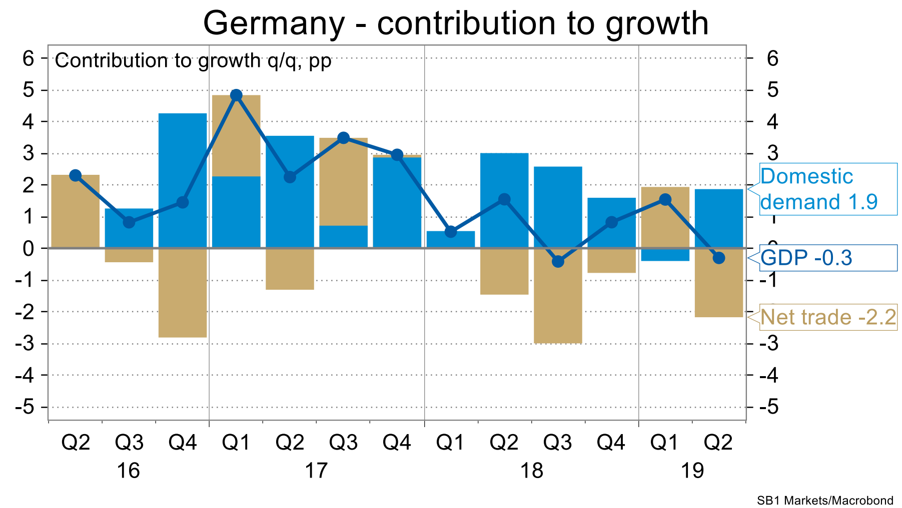


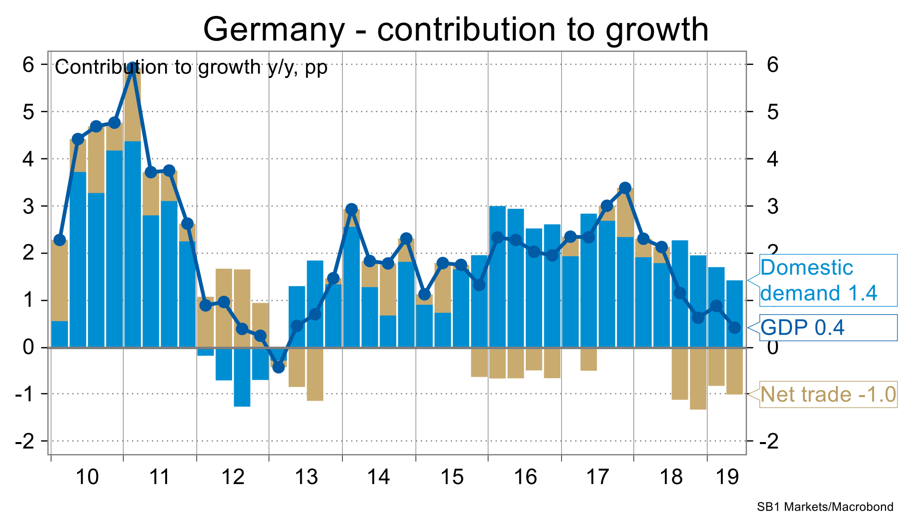


- GDP fell 0.3% annualised in Q2 (-0.1% not ann.), unchanged from the first report. Growth y/y has slowed to 0.4%, with a negative drag from net trade a 1 pp.
- The details note zero contribution from household consumption/housing inv. from a strong Q1, and a modest decline in business investments. Only public demand and inventories/residual lifted growth! The major drag was exports
- Unfortunately, business surveys do not signal any upswing

Net trade has contributed with a -1 pp swing, so has domestic demand

It's not just trade, domestic demand has slowed too

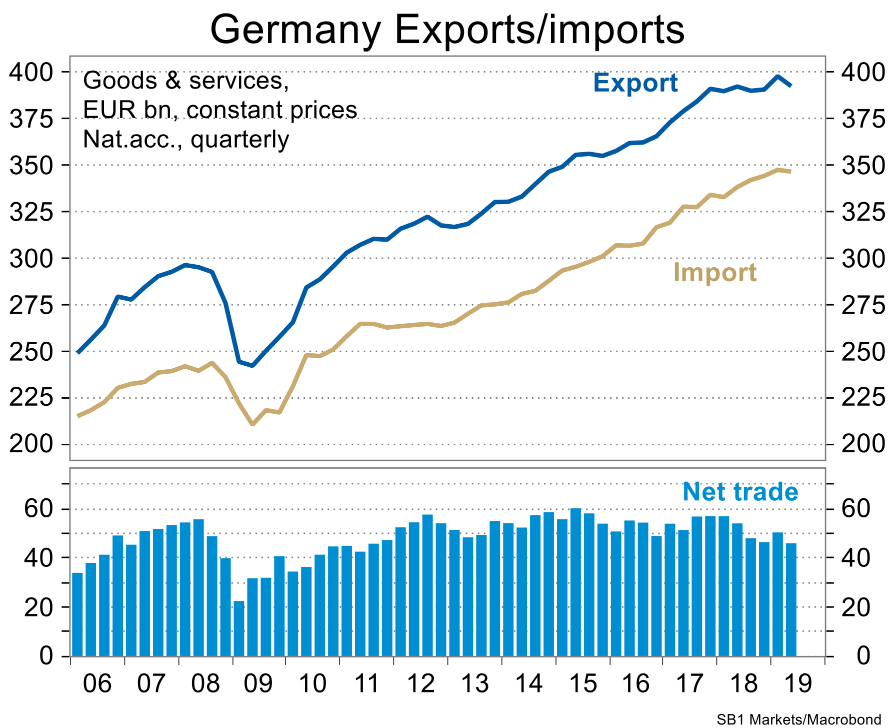


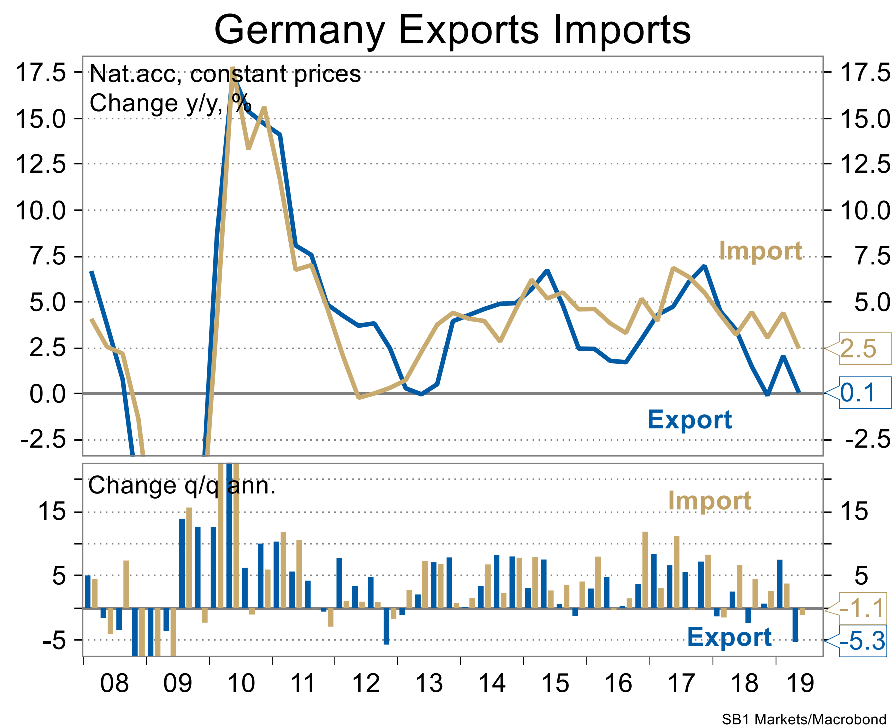


- Changes in inventories are included in domestic demand in the charts for aggregated demand

Q2 exports hit by less exports the UK but trend growth has slowed markedly

Exports have flattened out since Q1 2018, annual rate up just 0.1% - and slipped 5.3% q/q in Q2

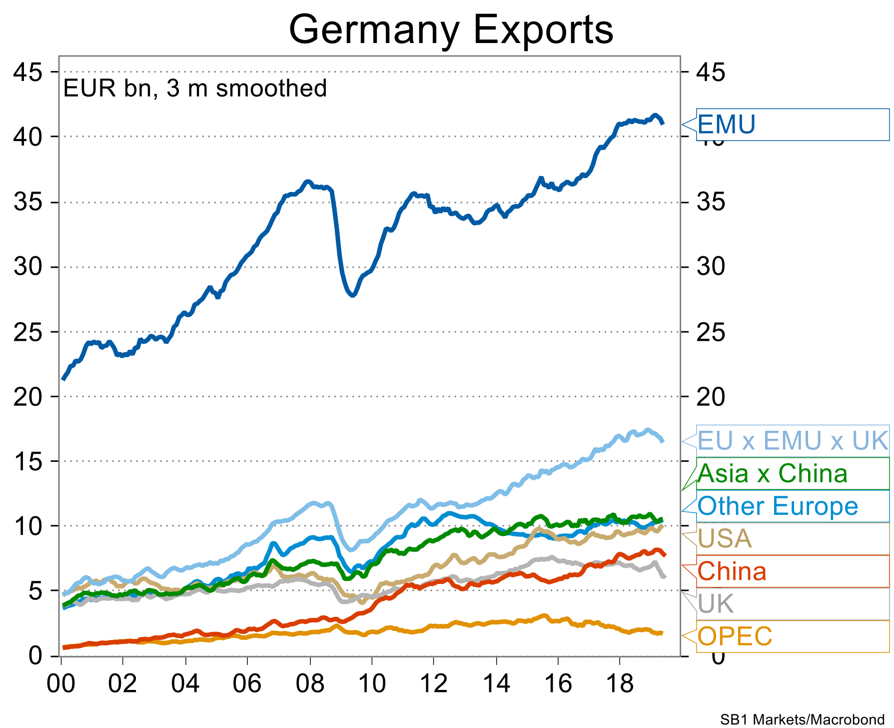


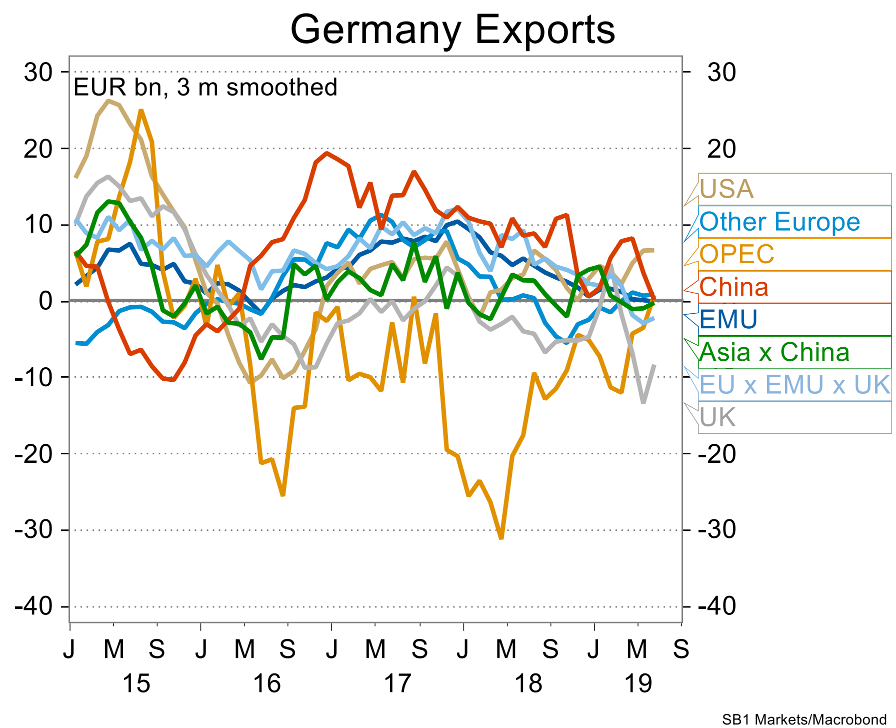


- Exports to the UK plunged in Q2 as the pre-Brexit stockpiling in Q1 was being reversed. The decline in UK exports explain almost 70% of the total Q2 decline. Exports to China fell moderately, but has been trending up until now. Check the next slide for country details
- Imports are still growing moderately, although somewhat slower than 2-3 years ago. Up 2.5% y/y (in volume terms)

Exports to most countries have cooled, ex the US. Exports to UK sharply down

Exports to EU x Germ. are down recent months too. China and EMU have stagnated, US still growing

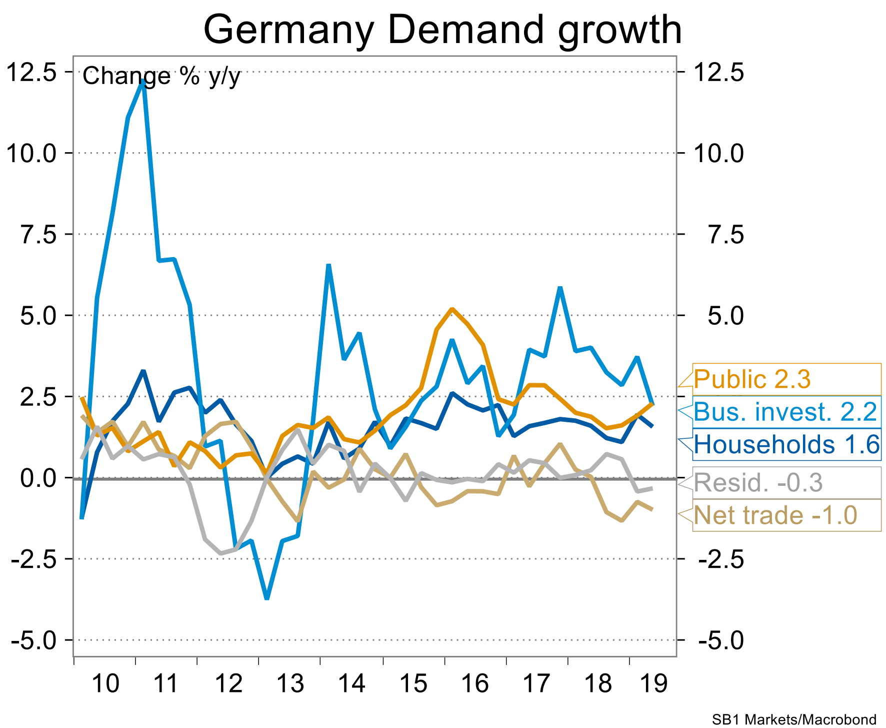


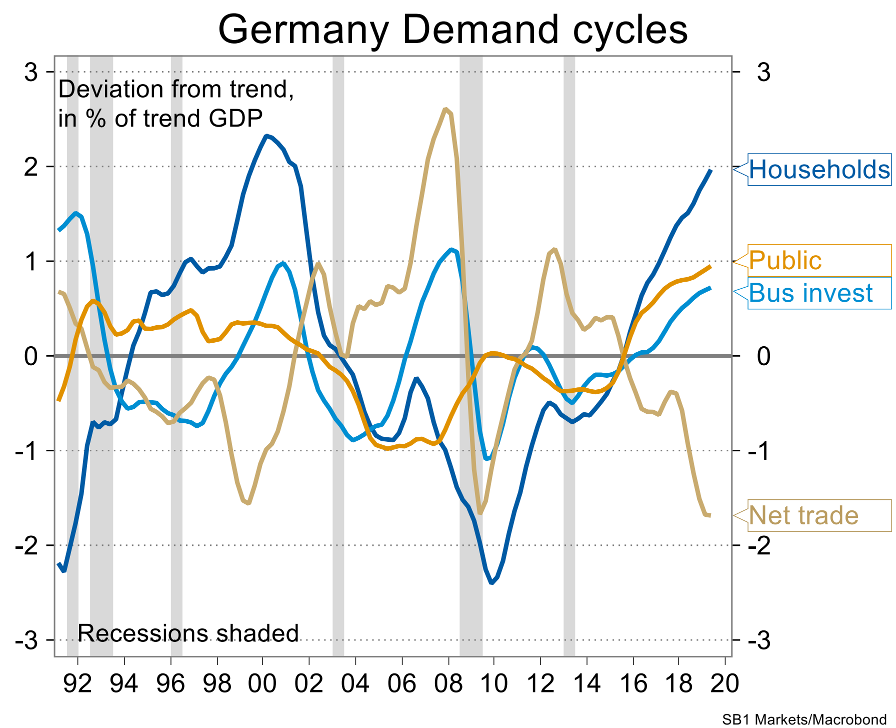


- No signs of a collapse in German exports but the trade war and Brexit uncertainties are no doubt dampening global trade
- Exports to China fell in May and June – and the annual rate slowed to +0.1% (3m smoothed). Exports to other EMU countries, and Asia x China have stagnated too. Exports to the US are still heading up
- UK demand is falling rapidly, as businesses there are cutting back purchases after a huge stockpiling ahead of the prior Brexit deadline in the spring. Exports to other EU countries x EMU is declining too
- Germany's main export markets: The other EMU countries (37%), other EU countries x UK (15%), Asia x China (10%), Europe x EU (10%), USA (9%), China (7%), UK (6%)

Them long term big picture: Net trade the really weak spot

Solid growth in business & public investment. Households the risk now? And business investments?





- Long term Germany most likely has to accept a lower trade surplus – and as that happens, the country will be more dependent on domestic demand for growth
- Household demand has been growing well above trend recent years – and is now at a high level? Possibly. Luckily, the savings rate has been stable – and a high level, 10%

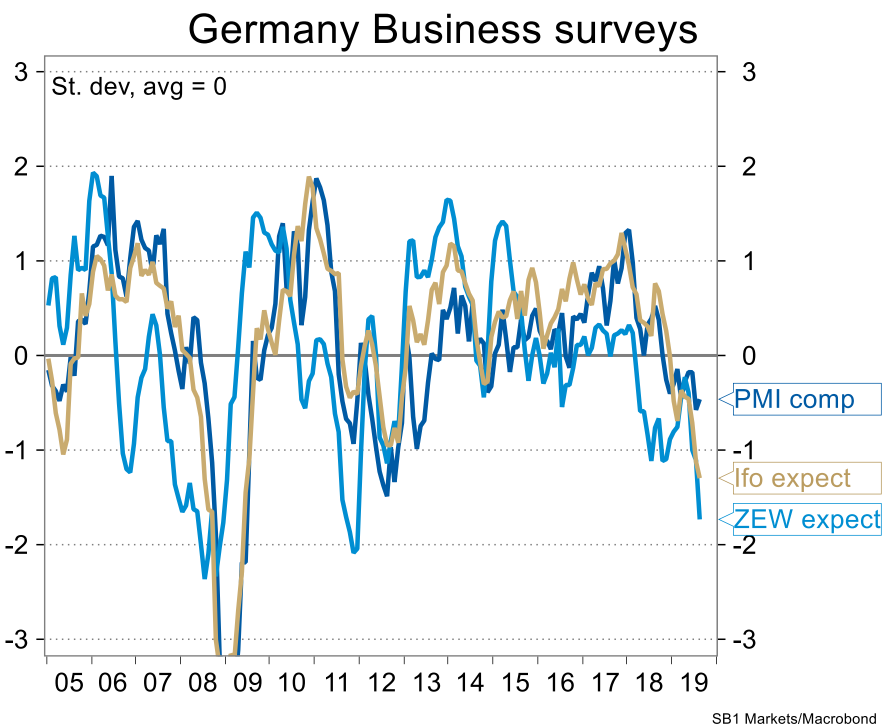
Guess what, German trade is closely correlated to…

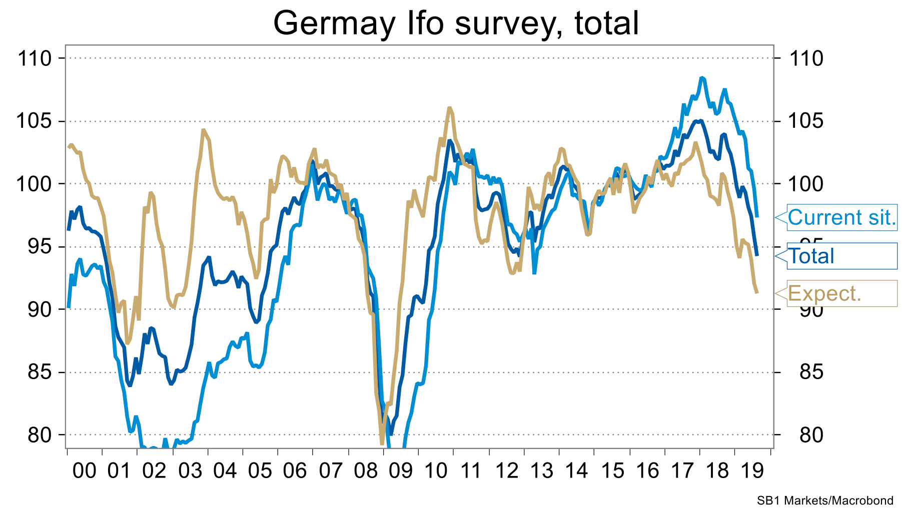
.. global trade. Now, both have stagnated due to trade war/Brexit uncertainties and a mature cycle

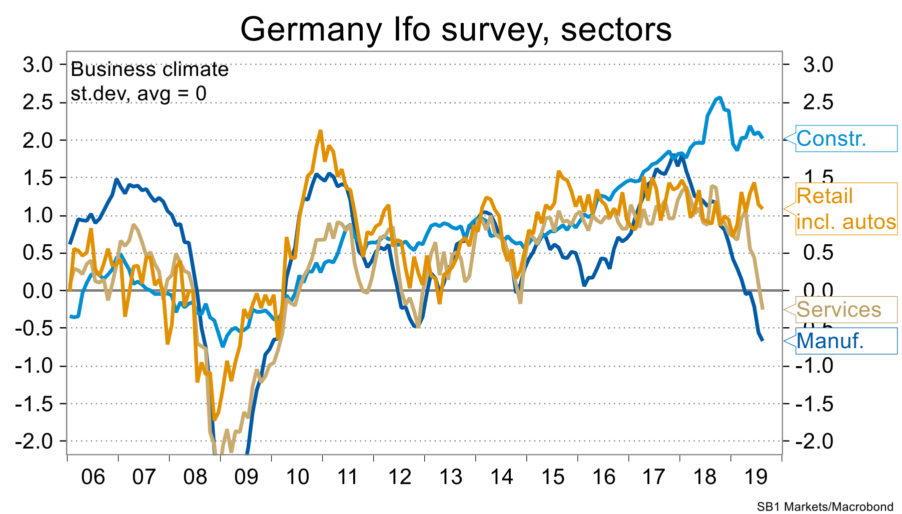
- Both German and global trade are highly correlated to German industrial production. Thus, either exports will have to follow production down or production will rebound? The prior is most likely, given signals from PMIs/other surveys

Ifo survey sinks further, weakest since 2009 and far softer than the PMI

Services (x retail) have followed manufacturing down, retail & construction still well above avg



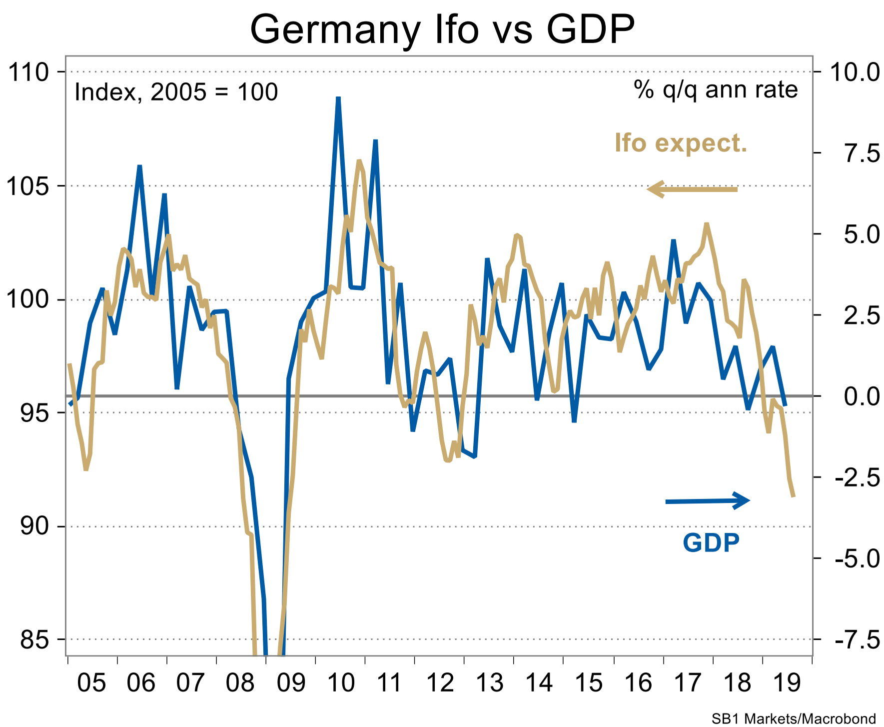


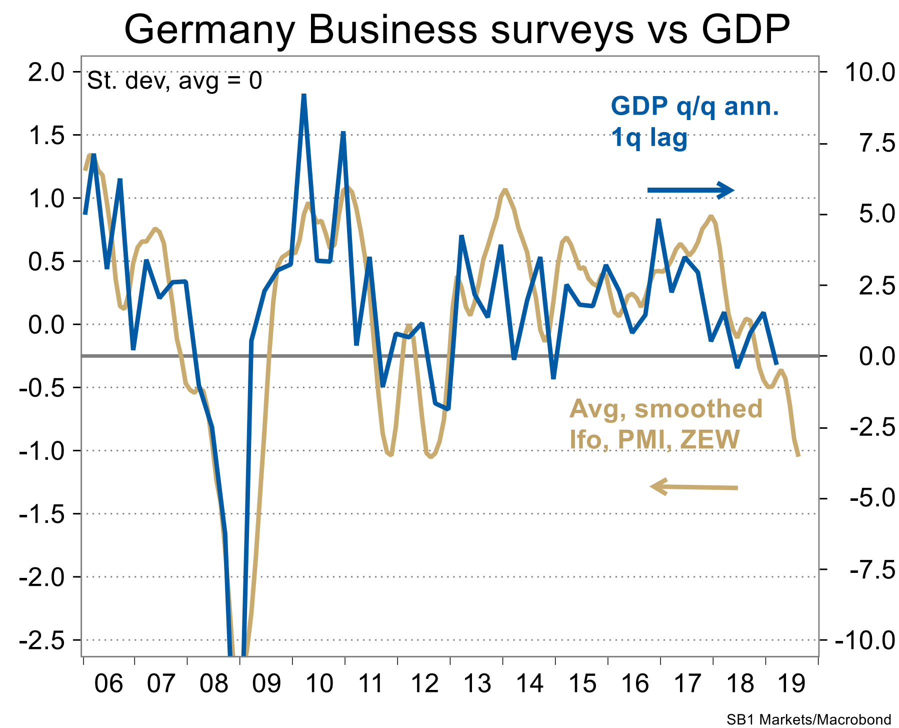


- Both businesses view on both the current situation the outlook weakened once again in August, softer than expected. The expectation index is far below a normal level, at the lowest since the financial crisis. The current situation index is well down from the peak but still above an average level (however, the expectations index is leading)
- The slowdown is driven by manufacturers but according to Ifo, services ex. retail are now slowing rapidly. Retail and construction are still going strong, confirming that important parts of domestic demand remain resilient to the contraction in manufacturing

Surveys (in avg) are suggesting a German recession

However, the surveys were too downbeat vs actual growth in both Q1 and Q2





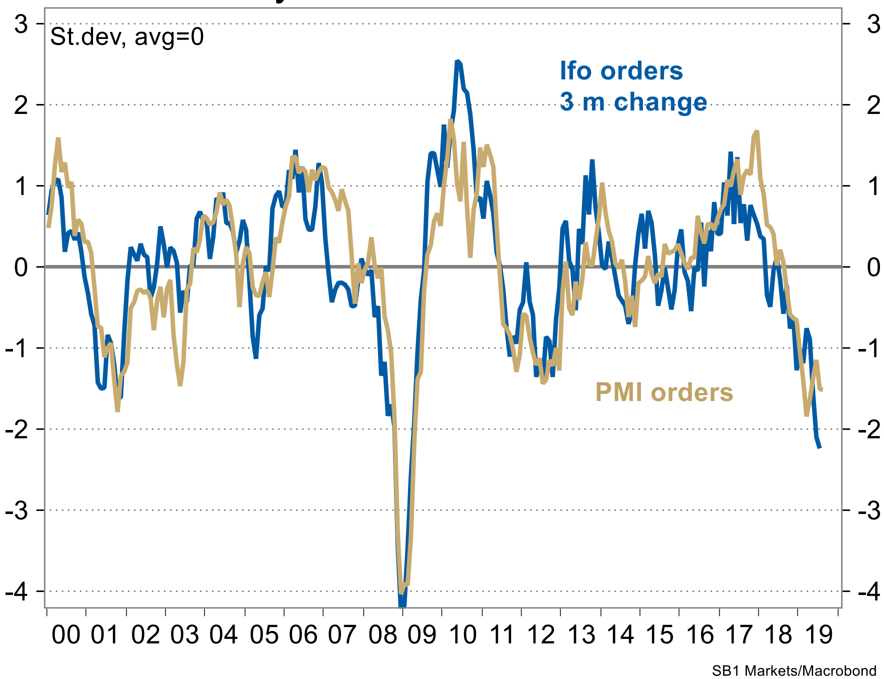
.. And the correlation is anyway not very strong, short term

- The surveys are not in unison, the composite PMI still points to positive GDP growth (although just some 0.5% annualised), while both Ifo and ZEW are suggesting a contraction

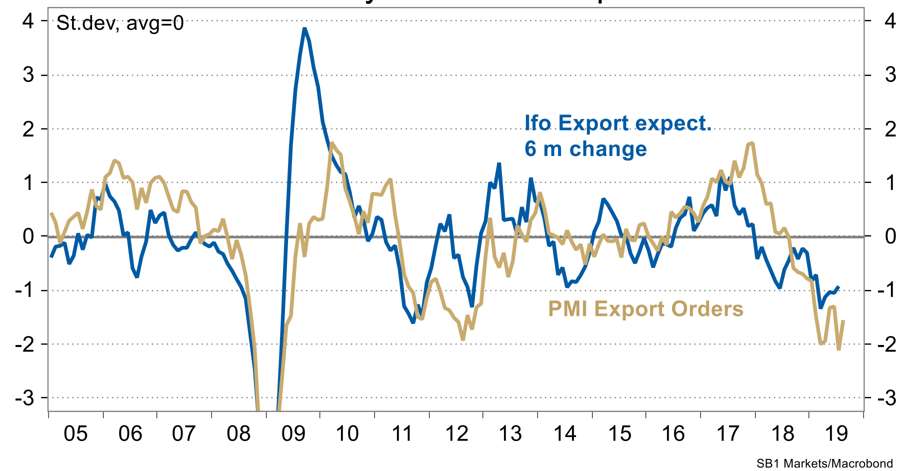
Ifo order setback deteriorates, both domestic and export related

Underlying growth (3m change) in orders weakest since 2009, pointing to a gloomy outlook

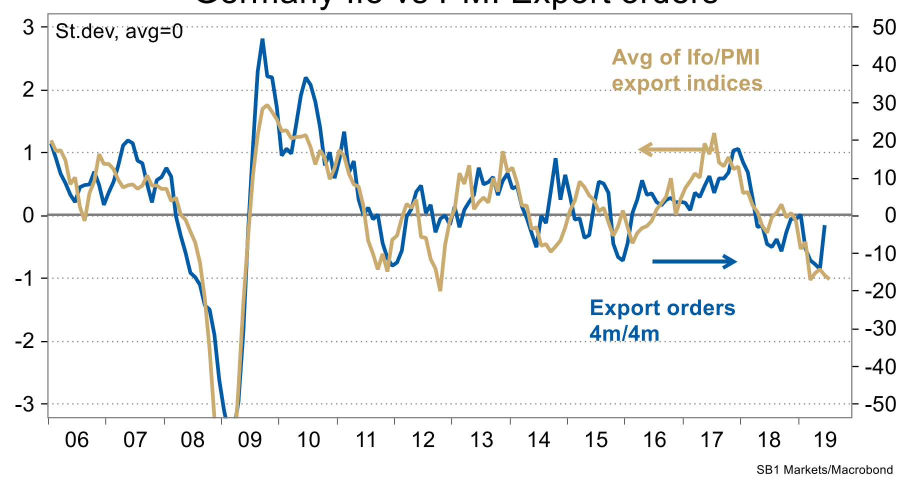
Germany Ifo vs PMI manuf. orders



Germany Ifo vs PMI Exports



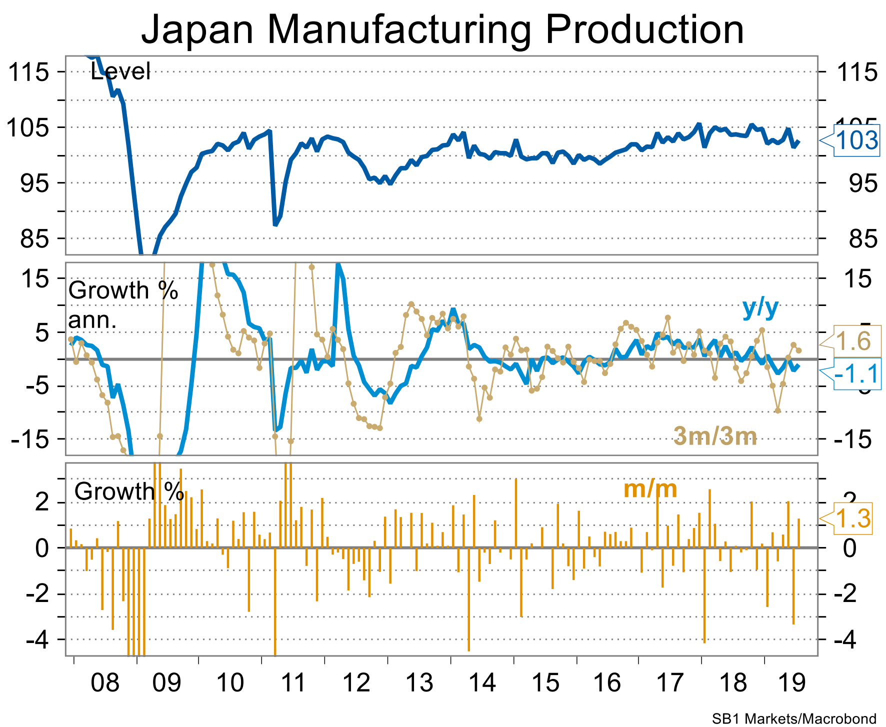
Germany Ifo vs PMI Export orders

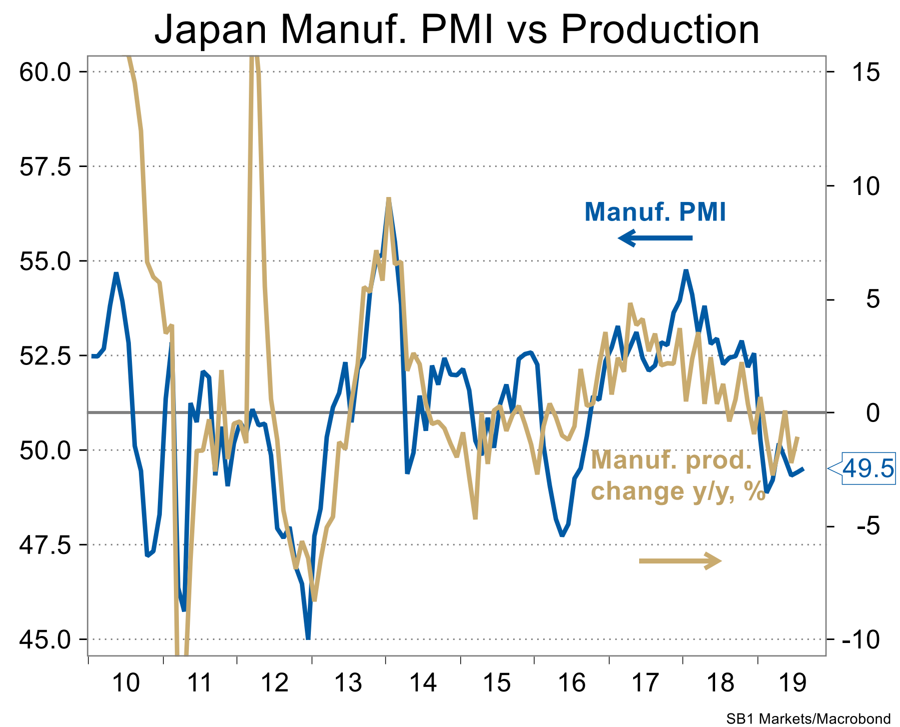


- The level of the Ifo order index is far above the PMI. However, the change in Ifo (here a 3 m change), which is closely correlated to – but usually leading – PMI orders, is falling rapidly
- Ifo export expectations fell again in July, but the decline has not gained speed recently (6m change). An avg of Ifo and PMI is pointing to a deteriorating decline in export orders

Manufacturing production heading slowly down, as PMIs have noted

Production recovered some of the June loss – and the trend is still downwards

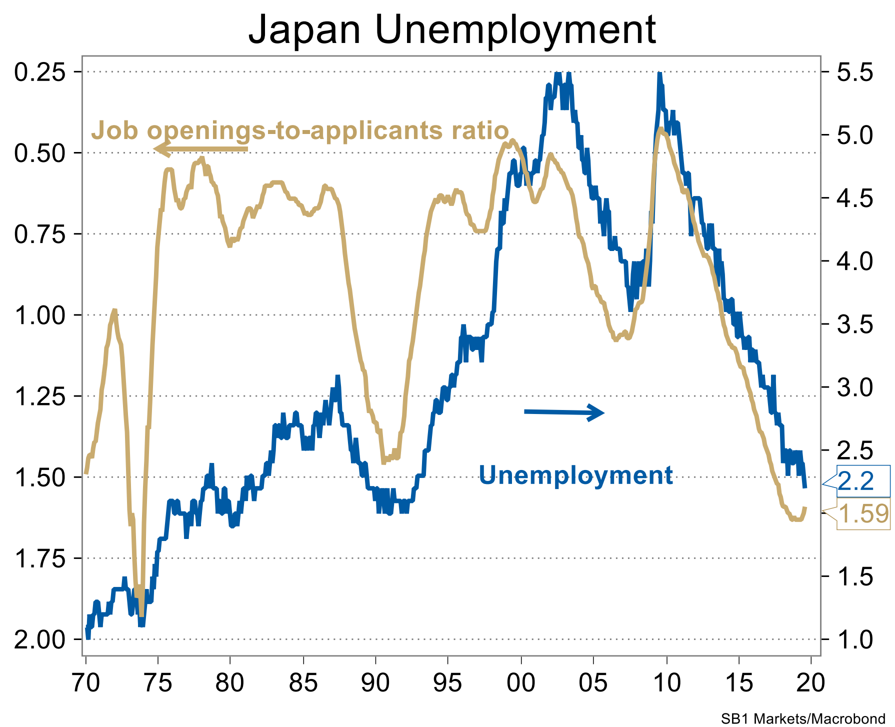


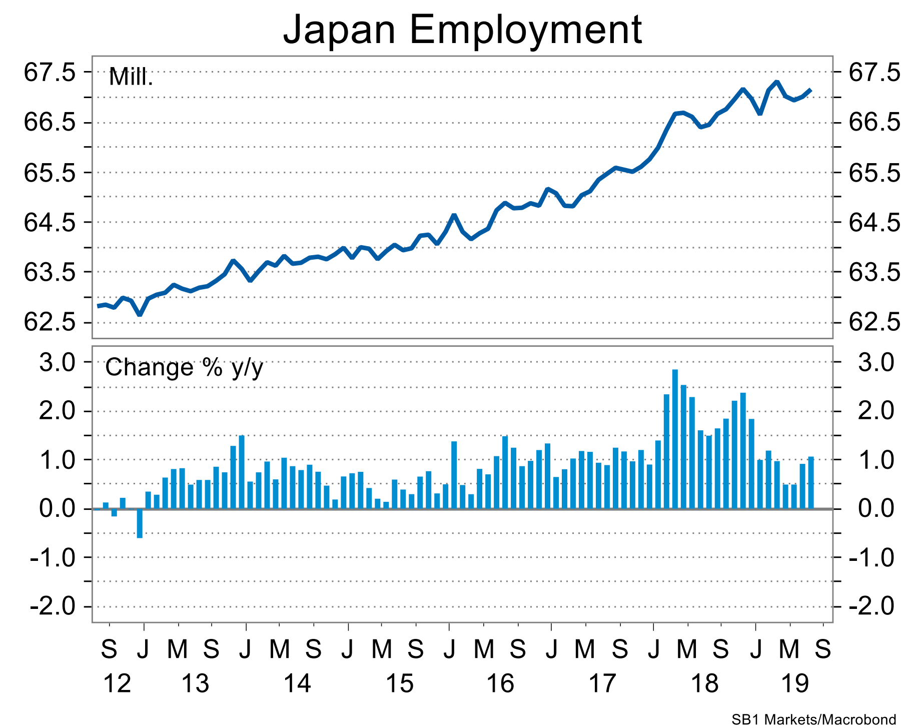


- Manufacturing production rose 1.3% m/m in July following the 3.5% drop in June. Production is down 1.1% y/y
- Neither surveys nor orders are signalling any recovery in the Japanese manufacturing sector. Export orders and export volumes have fallen sharply – while domestic orders have kept up somewhat better

Unemployment further down, employment growth at 1%

Unemployment inched down to 2.2%, to the lowest level in 27 years!

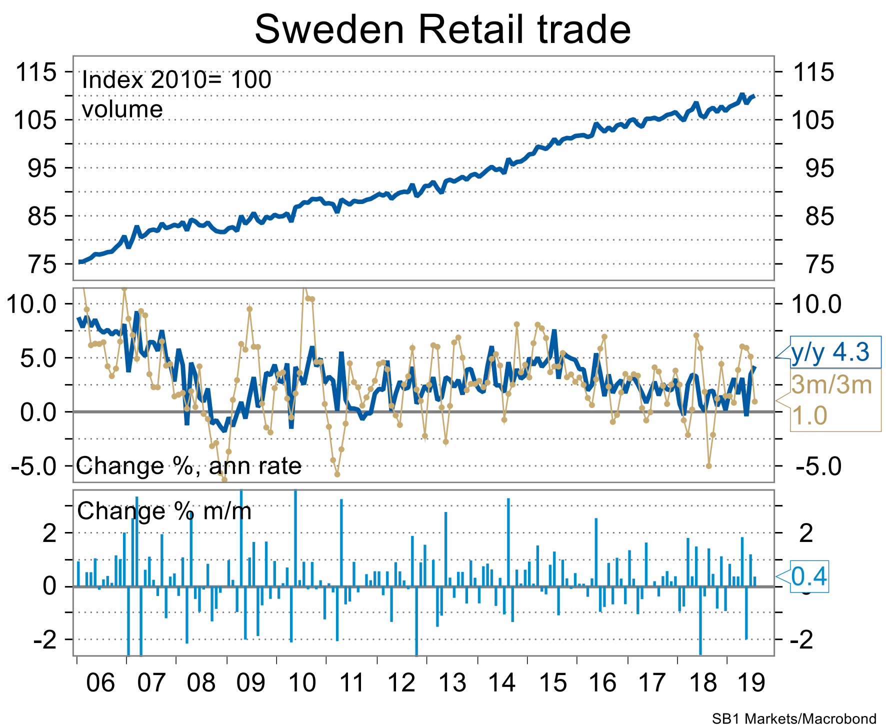




- Unemployment has been more or less flat over the past year, at the lowest level in 27 years. In July, unempl. fell 0.1 pp, to 2.2%
  - » The job openings-to-application ratio may have turned down, signalling some weakness? On the other hand, level is the highest since the 1970'ies
- Employment growth ticked up in June and July, at a slower pace than in 2018. Employment rates have been soaring, and are at record high levels for all ages/genders, with those over 55 y in the lead. And of course, participation rates straight up too
- Wage inflation has fallen recent months
- Barring the high corporate savings rate (partly offset by the public sector deficit – Japan is running a huge current account surplus) - what's really the Japanese problem – when employment is 'more than full'

Retail sales still growing at a solid pace

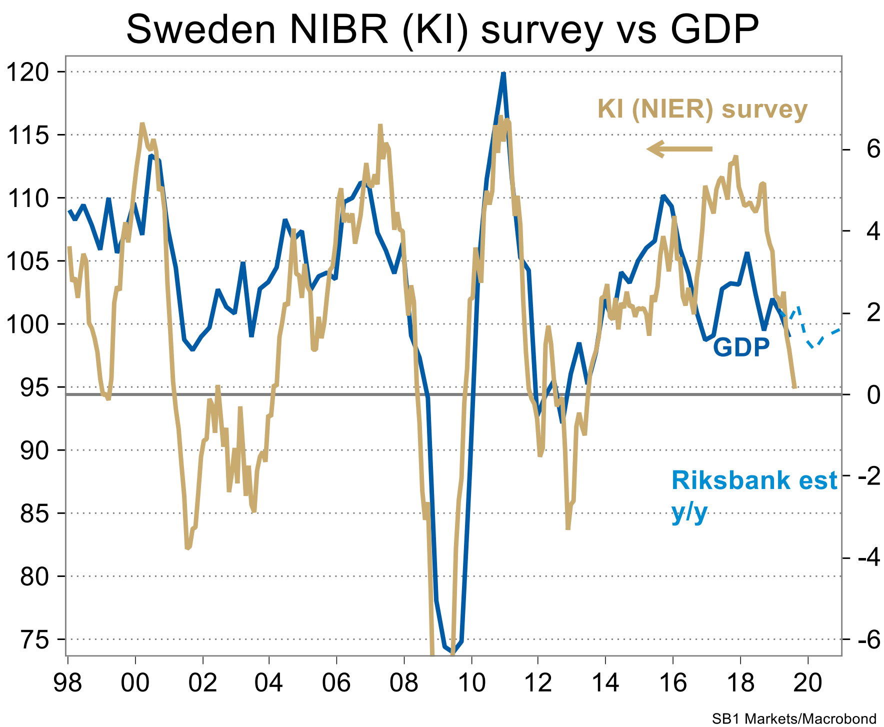
Sales rose 0.4% in July and are up 4.3% y/y. A 2.2% trend path is intact

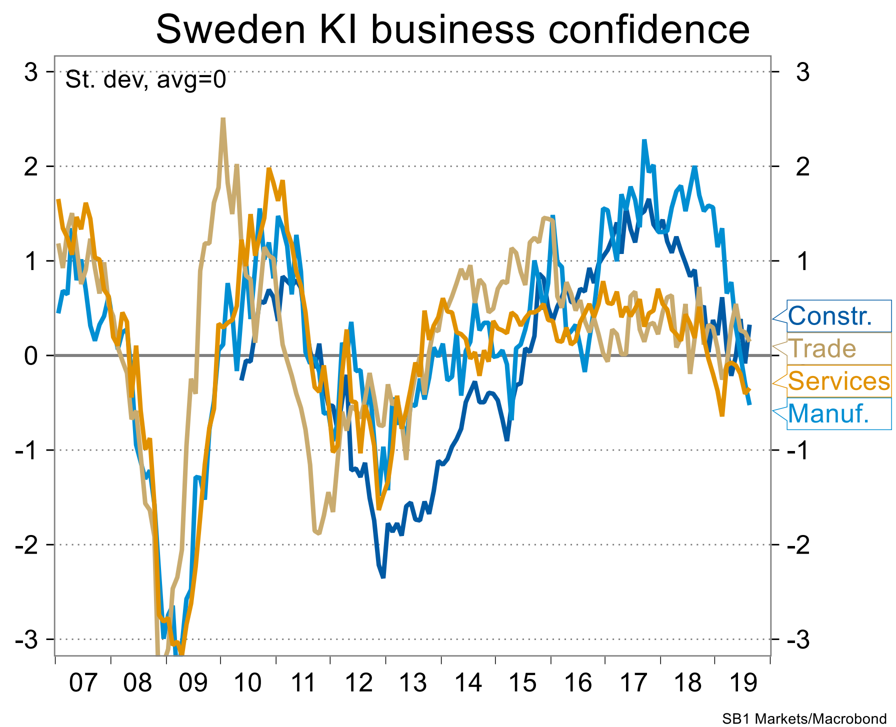


- Retail sales volume increased by 0.4% m/m in July, close to expectations. The annual rate rose to 4.3% and sales are trending steadily up (even if our 3m/3m is weaker, due to a Easter sales hike). Growth is stronger than in Norway, where retail sales have more or less stagnated, strange…
  - » Modest price inflation is supporting volume growth. However, price inflation is now increasing, limited upside?
- Employment has fallen sharply recent months, according to the LFS, consumer confidence is less upbeat (although above average in July) and modest house price inflation do not signal strong consumer demand going forward

The KI business survey dives, lowest level since '13

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

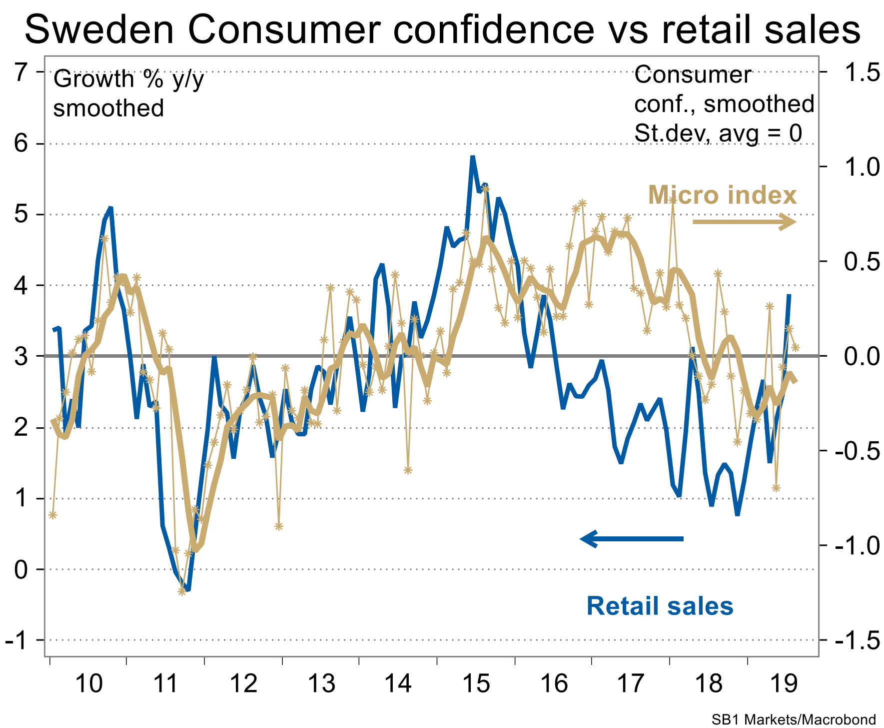


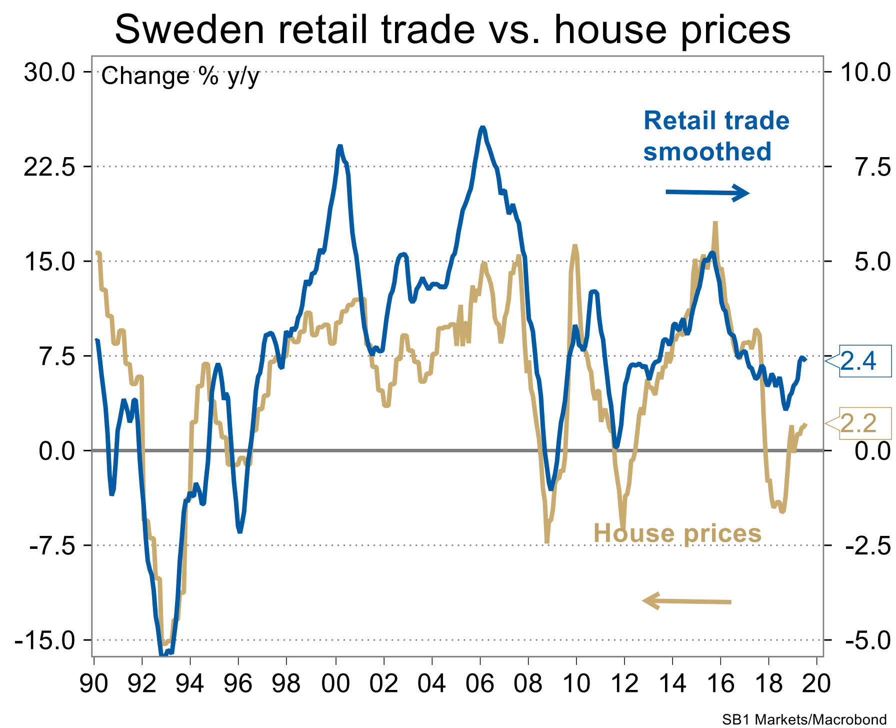


- The KI economic tendency survey, which usually correlates well with GDP growth, were pointing to unusual high growth rates from 2016 and until a few months ago. Now, the index has fallen below the 2016 level and is most likely signalling a rapid downswing in GDP growth. All sectors are reporting sagging confidence – with manufacturing in the lead (down)
  - 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

Consumer confidence below avg points to softer consumption growth

The volatile confidence index inched down in Aug, may have stabilised after a steady decline

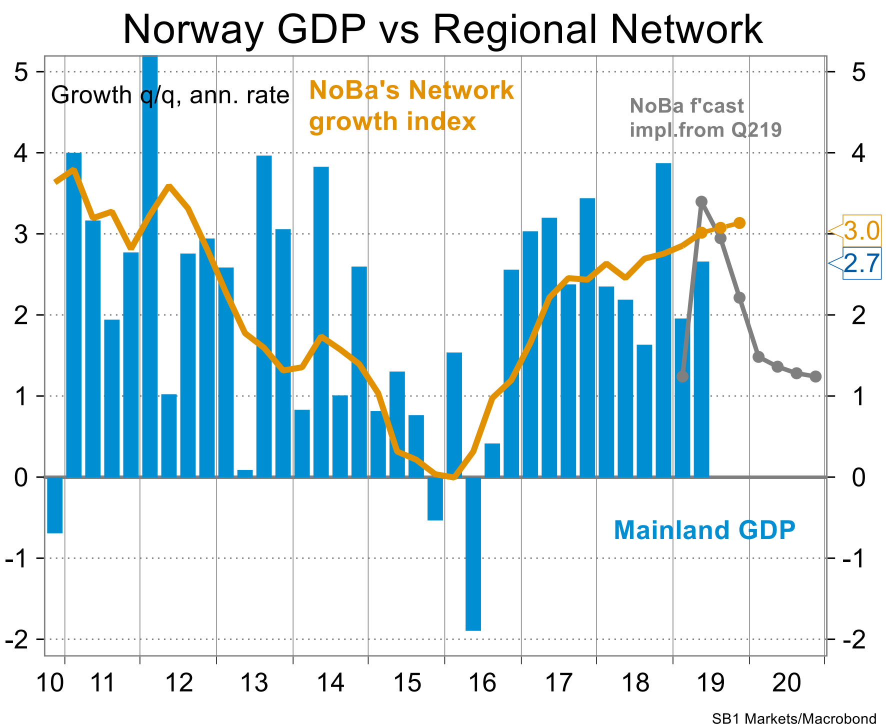


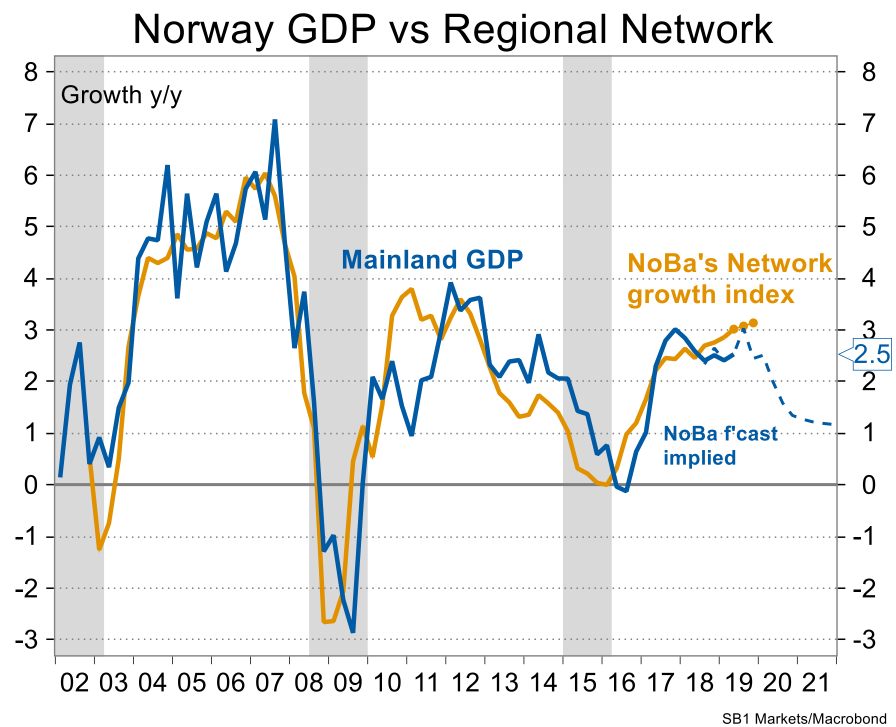


- The consumer confidence survey is volatile, and recent months have been zig zagging too much to give any useful signals. However, confidence is below avg and may still be trending down. The survey has been too optimistic vs actual consumption the past 2 years (vs the normal correlation to and the correlation is anyway not very strong
- House prices and retail sales are often quite closely correlated. Consumption did not follow house prices down in late 2017/early 2018 and now house prices have stabilised, and real wages are on the rise. On the other hand, a weakening labour market is not a good sign.

Mainland GDP up 0.7% in Q2 but details do not point to a very bright outlook

GDP rose 2.7% q/q annualised and 2.5% y/y. A tad weaker than expected, not enough to curb NoBa

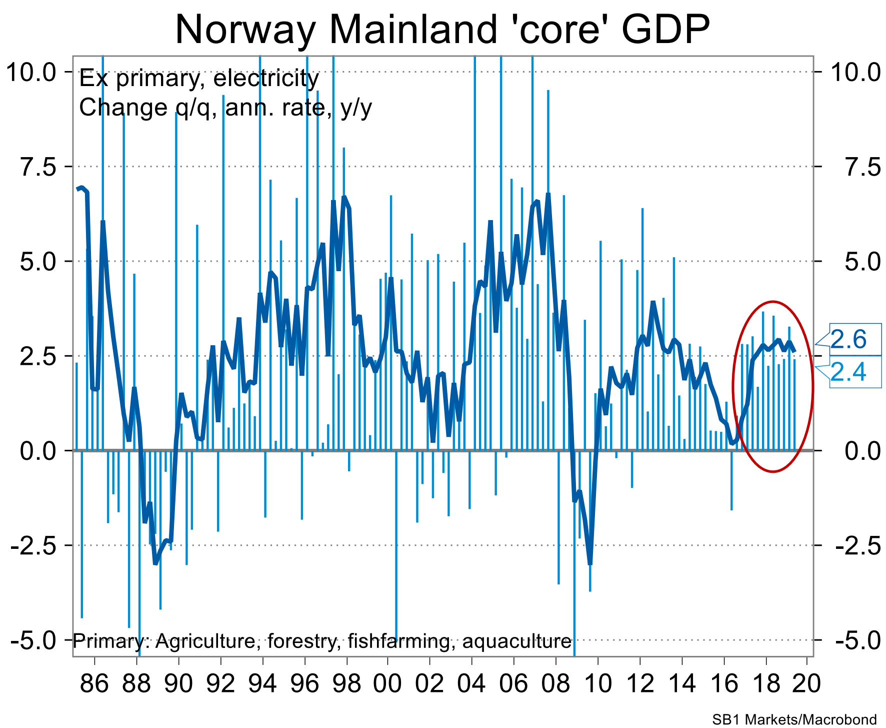


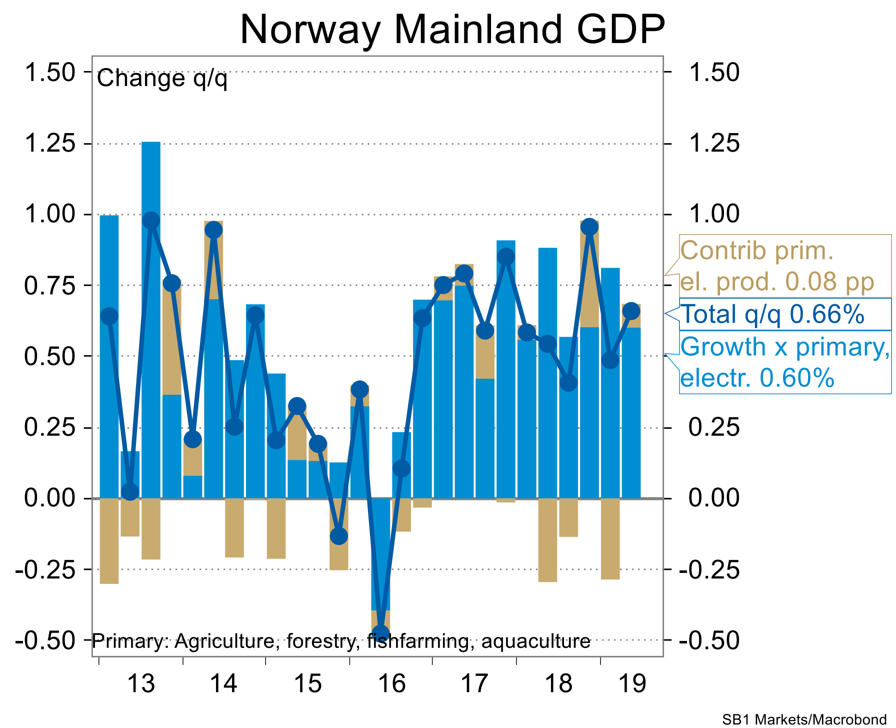


- Mainland GDP rose by 0.7% q/q (2.7% annualised) in Q2, we, consensus and Norges Bank all expected 0.8%. The annual rate inched up to 2.5%. Moreover, Q1 was revised up by 0.2 pp to 0.5%. In spite the solid Q2 figure, the details were not that upbeat;
  - » Private consumption rose moderately, as expected, while Mainland business investments surprisingly dragged growth down (again). Oil investments soared, marginally less than we f'casted. Housing investments rose modestly. However, government demand and inventories were the major growth contributions, will not last. Mainland net exports fell and dampened GDP growth
  - » Solid employment, up 1.7% annualised, while productivity growth is slowly picking up, from a low level (0.9% in Q2). Wage inflation was flat at 3.3%
- Growth is above trend and cost inflation is trending up. The solid GDP figure is an argument for another Norges Bank hike, however, other data (labour market, Regional Network, financial markets and of course the global outlook) are more important. <u>For now, we stick to our view that Norges Bank will hike on September 19, which may be the last one, for a while</u>

Growth ex. electricity production & primary sectors at 0.6% in Q2

'Core' GDP growth has been unusually stable since end of 2016, at 0.5-0.8%

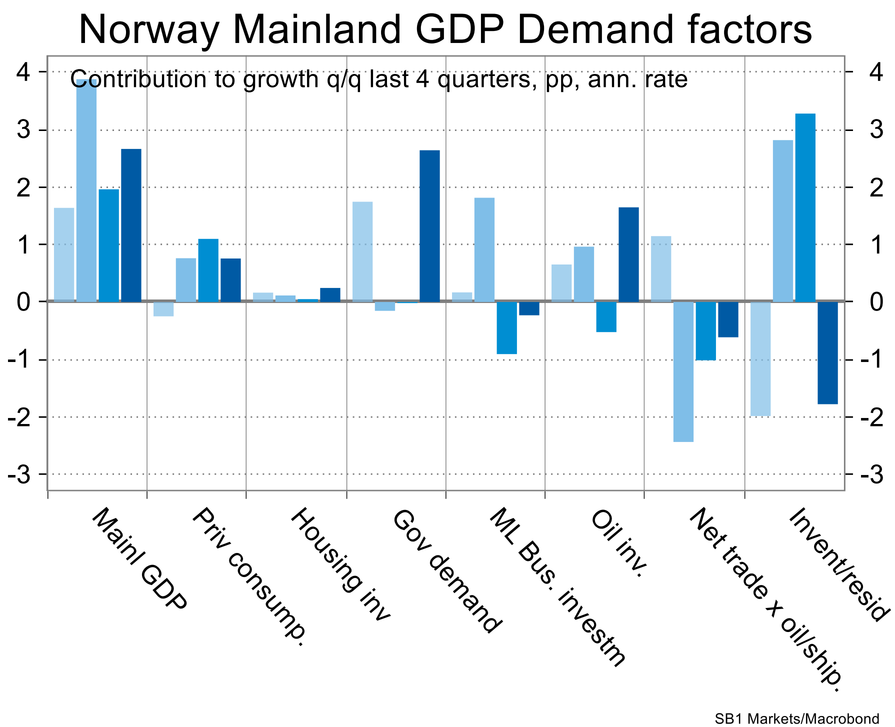




- Weather conditions affect the Norwegian economy in many ways, primary & electricity production are particularly exposed
- Increased production of electricity, agriculture and fishing boosted growth by 0.1 pp, barring these sectors; Mainland GDP ex these sectors rose 0.6% q/q
  - » Electricity production was unchanged q/q in Q2, agriculture & fishing fell 1.2%, while fishing & aquaculture surged 6.1% q/q
- Since end of 2016, when the Norwegian economy entered the post oil downturn recovery, the 'core' quarterly growth rates have been among the more stable we have ever seen, check the graphs above

GDP expenditure components not that impressive in Q2

Public demand, oil investments and private consumption lifted growth, soft business investments



- Private consumption rose moderately in Q2, up 1.4% annualised, lifting growth by 0.8 pp. Consumption has been expanding steadily recent quarters
  - » Higher auto sales lifted consumption, retail sales weaker
- Housing investments climbed 3.8% ann., the highest growth rate since 2017, confirming that housing investments have turned up from the bottom. However, our take is that the upside is limited
- Mainland business investments fell 2.1% q/q annualised, following an 8% slip in Q1, and much weaker than we expected
- Oil investments are accelerating, up 33% annualised (7.5% q/q not annualised) and boosted growth by 1.6 pp. Yet, the increase was somewhat softer than we expected. Still, we expect H2 2019 to be (close to) the investment peak. Hence, <u>a crucial growth engine will most likely subside in 2020</u>
- Government demand spiked in Q2, up 7.9% and lifted GDP growth by some 2.6 pp. Most likely a one off
- Net exports fell and deducted some 0.6 pp of Q2 growth, as total Mainland exports stalled while imports increased. In goods, both exports and imports declined

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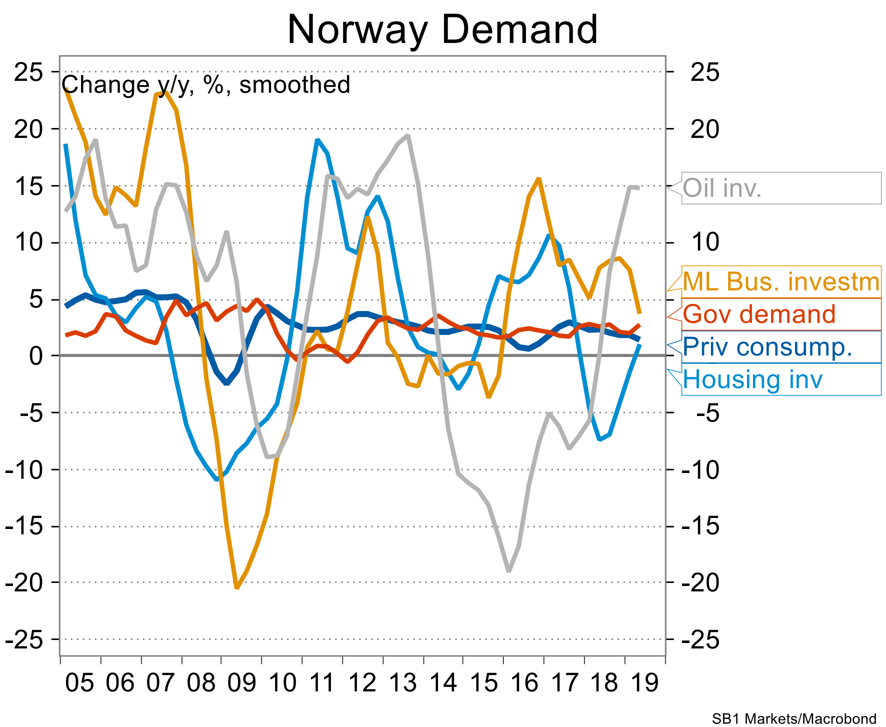
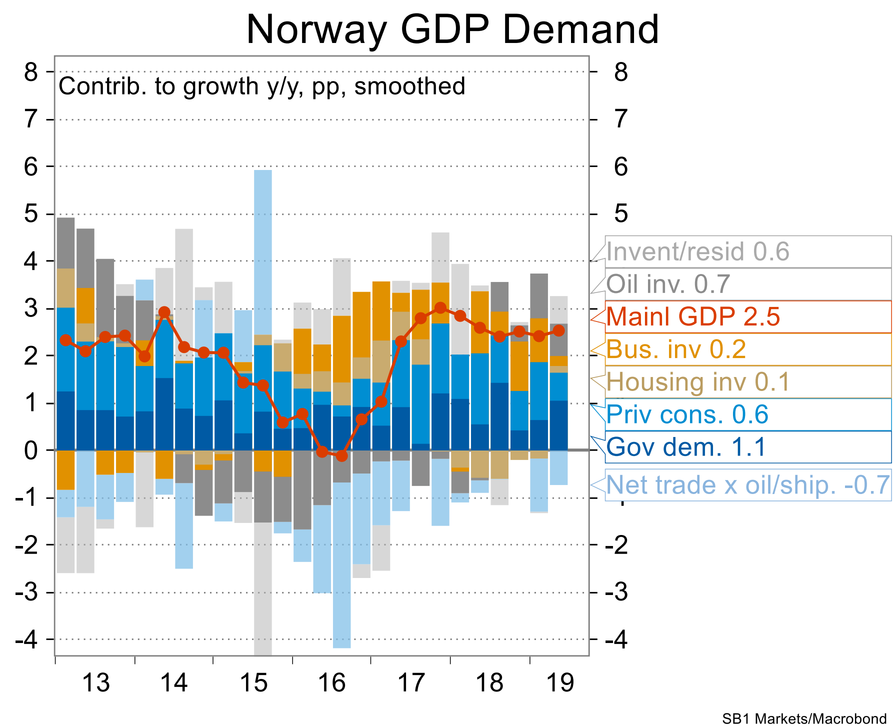
The big demand picture: Higher oil investment, public demand, the rest weaker

Consumption, Mainland bus investment growth has slowed, housing has stabilised

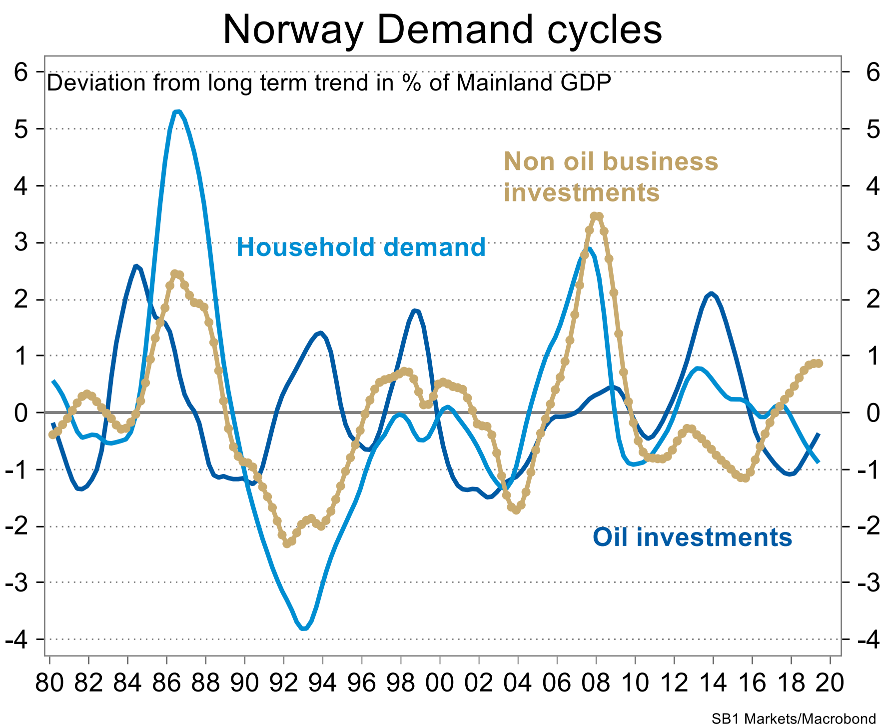


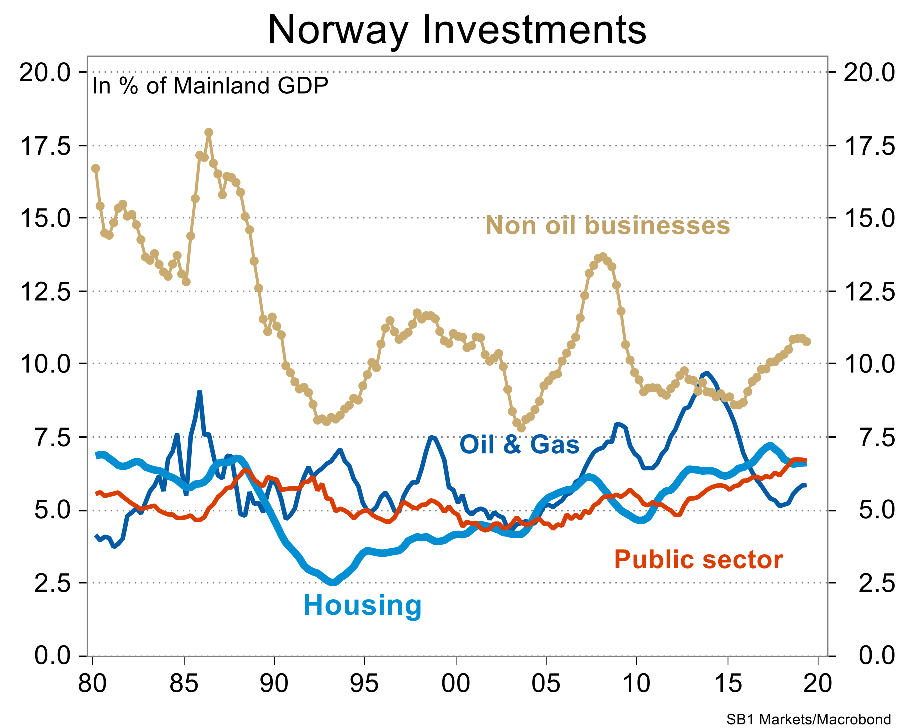


- Mainland business investments are growing at a moderate pace, up some 3.7% y/y in Q2 (smoothed). However, investments have slowed this year and the y/y growth contribution at 0.2 pp in Q2 is not impressive
- Oil investments are soaring, up 15% y/y, the Q1 investment level was revised down. More on the oil investment outlook here
- Housing investments are not decreasing anymore, up 1% y/y smoothed in Q2, up from -7% in 2018

Household demand slows, mainland bus. invest. have peaked, oil invest. close to

Mainland business investments may have peaked, but not at a dangerously high level

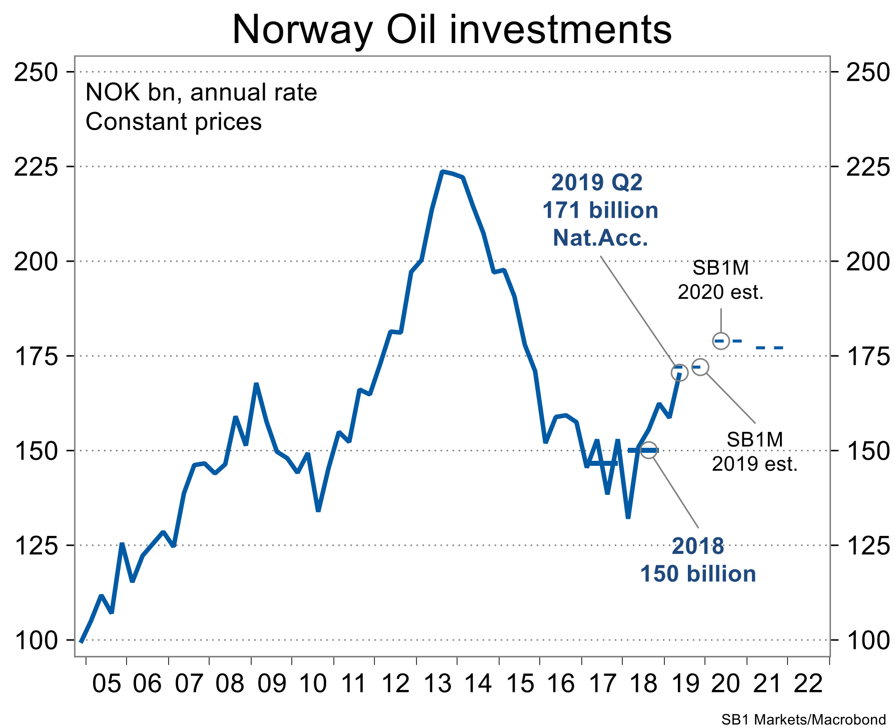


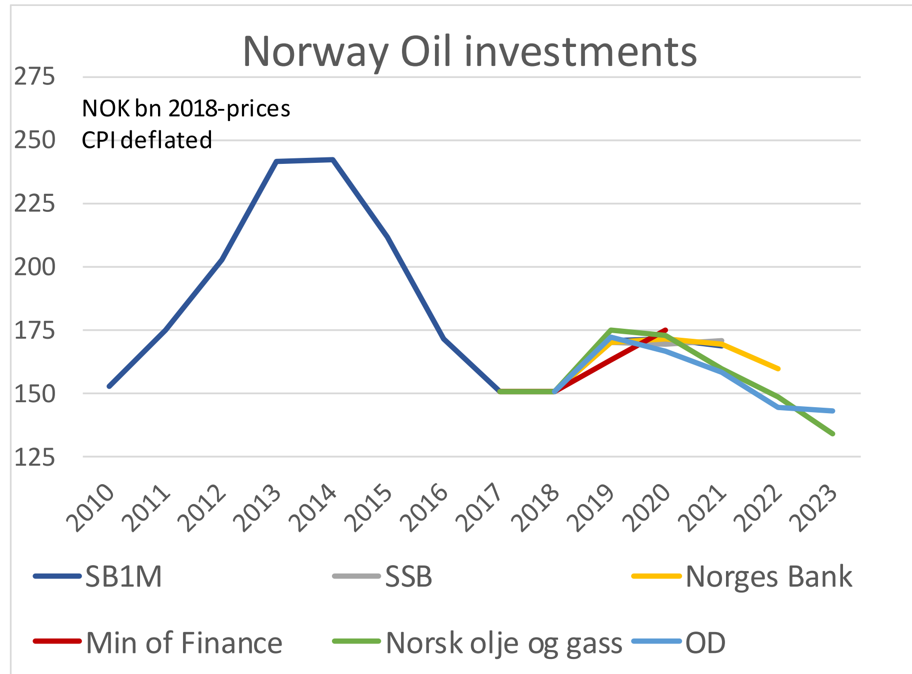


- Both manufacturing and power supply are reporting declining investments in 2020, according to SSB surveys
- Housing investments are at high level vs GDP but is not increasing anymore (flat, following the '17/18 mild setback)

Oil investments: The upside is not that large, peak in H2 2019?

Investments rose in Q2 and the level is some 4% below our 2020 estimate

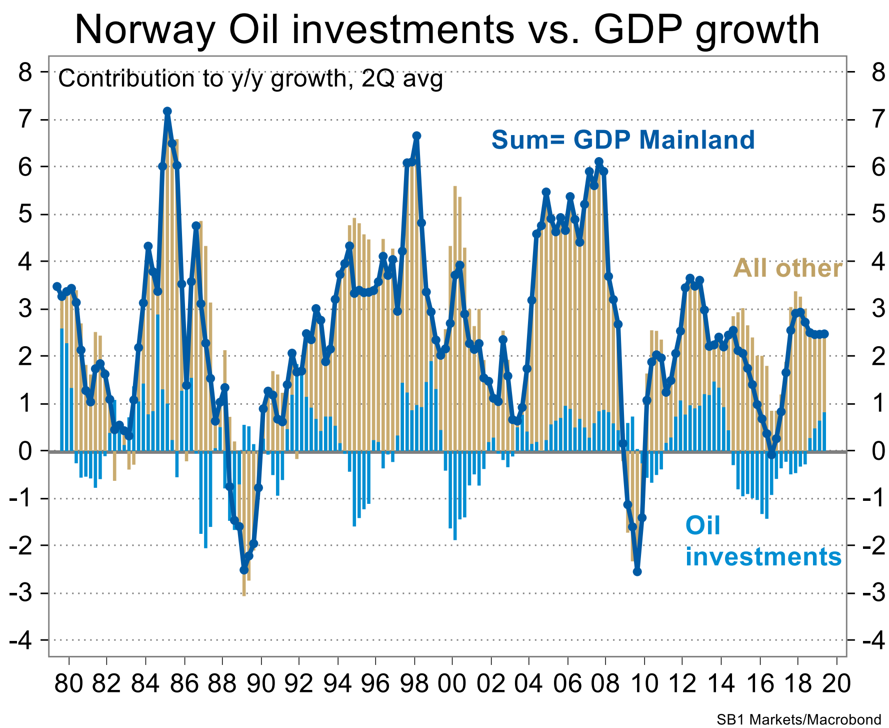




- Oil investments increased by 7.5% q/q in Q2, to NOK 171 bn. Investments are now 14% above the average 2018 level, which is just a fraction below our 14.5% 2019 growth f'cast. The investment level in H2 will be some few per cent above the Q2 level, and the (implied) H2 level is close to our 2020 f'cast (+4% from 2010). **Hence, the surge in oil investments is now (in H2) more or less behind us**
  - If our assumptions are correct, contribution to growth from the oil investments will be close to zero from Q4
  - No doubt, the oil price will influence the investment level from 2020 onwards, as more projects may be added

The 'oil boom' was not that large – but has given a decent GDP support

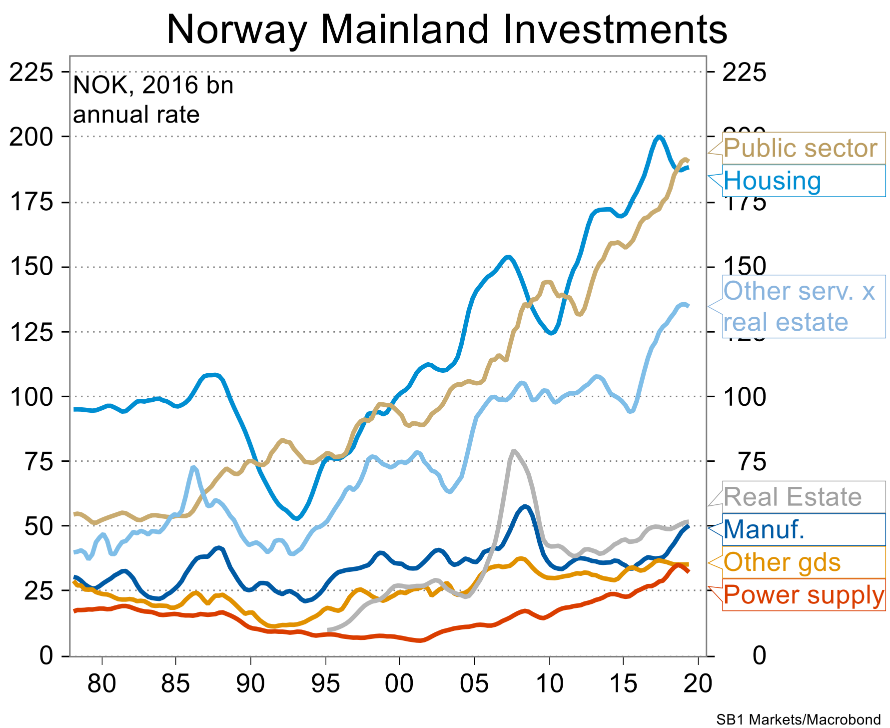
The contribution will rapidly decline towards zero, from some 0.7 pp now



- The contribution on the chart is not adjusted for direct and indirect import to oil sector investments – the net impact is less than the gross contribution

Public investments straight up, private services have been soaring

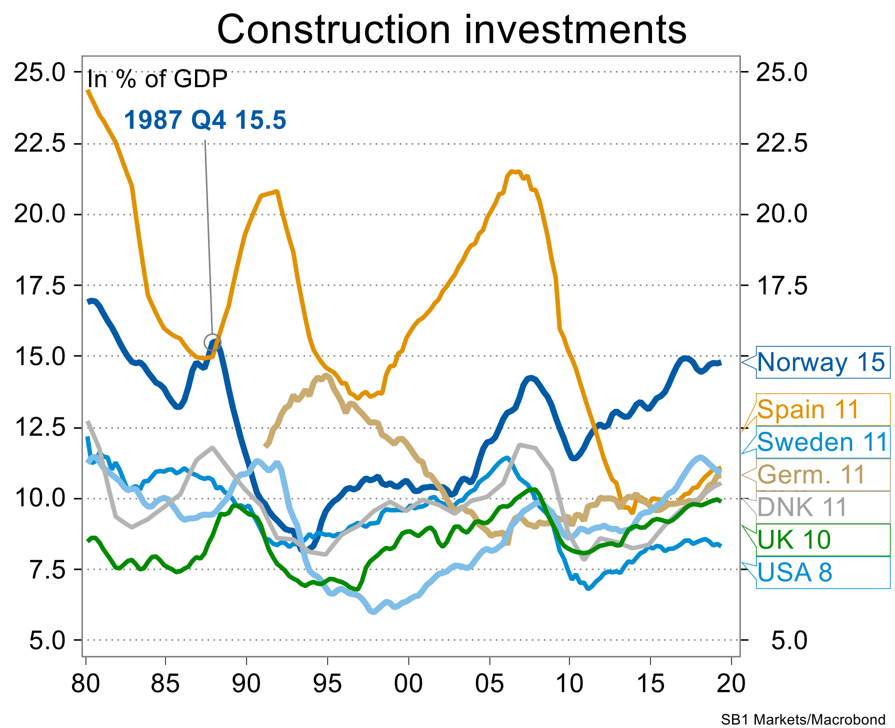
Housing investments down from the peak but is stabilising. Manufacturing soon peaking

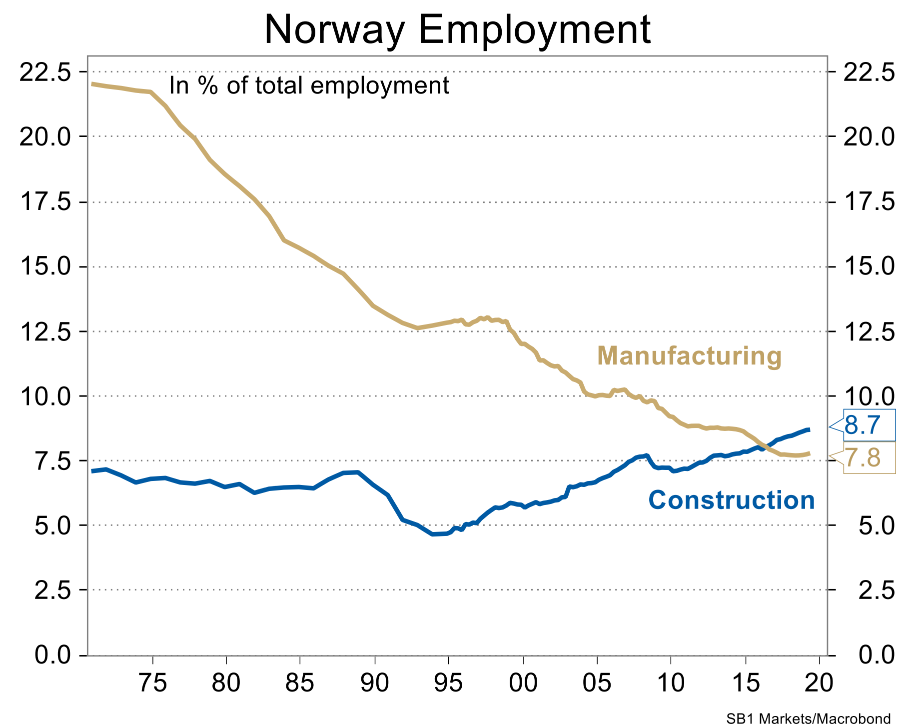


- Private service investments soared in 2016-2017, flattening out recent quarters – and is probably well above a reasonable long term level
- Manufacturing investments are on the way up, but SSBs investment survey suggests a steep decline next year,
- … as is the case for investments in power supply
- Real estate as is real estate (at a slower pace)

Construction investments on the way up, the level is very high

We are quite confident: Construction activity is higher than needed, long term

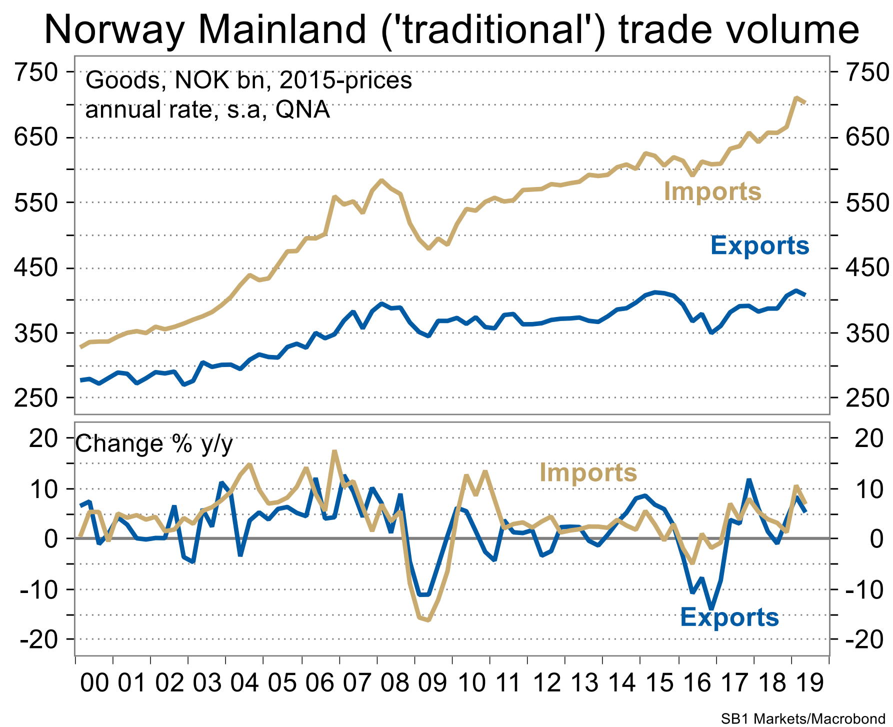


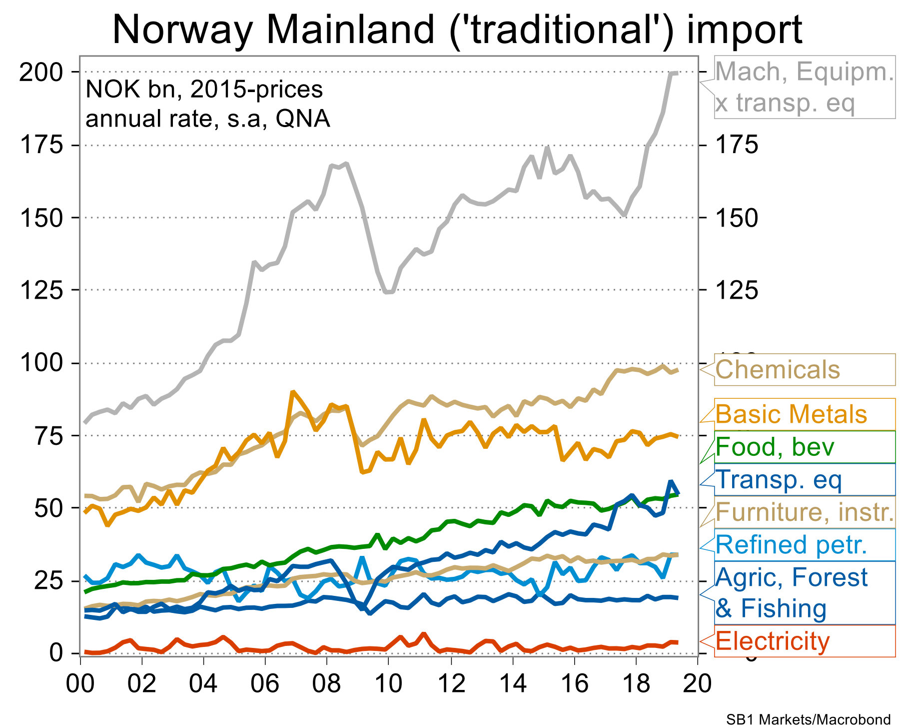


- Construction investments/GDP climbed through 2018 and is back at the same level as in 2017
  - We could have added the long term (assumed permanent) income from the Petroleum fund to GDP (in order to measure demand vs income), but the ratio would still have been very high, and much higher than in other countries
- Construction employment now equals 8.7% of total employment, much higher than anytime before
  - Construction is larger than manufacturing industries, employment wise, probably for the first time in a civilised country (except Spain and Ireland)

Goods imports are trending up, exports are following

Imports of machinery/equipment are surging, most other sectors are slowly increasing

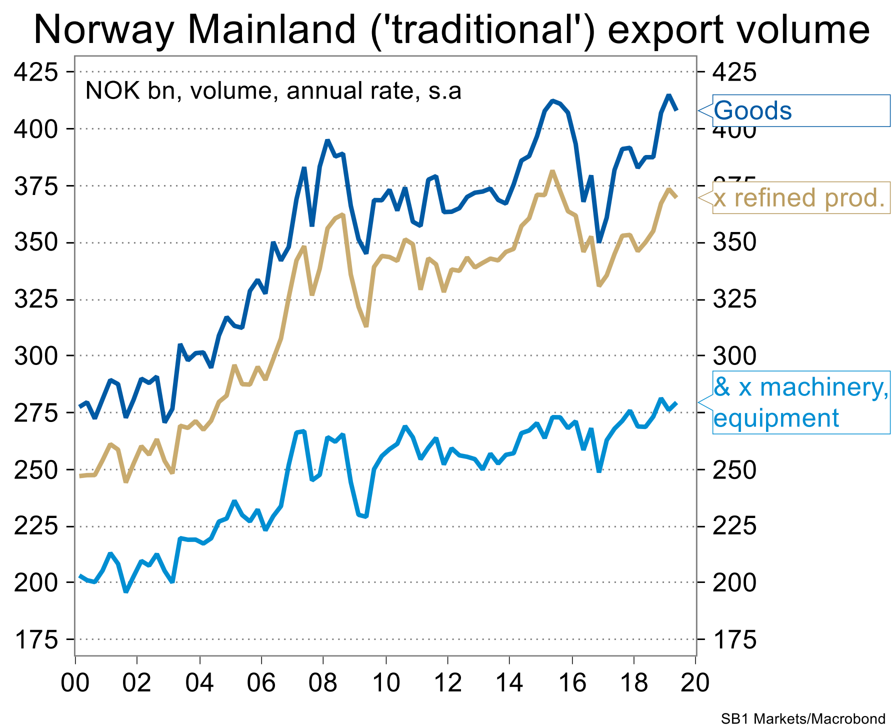


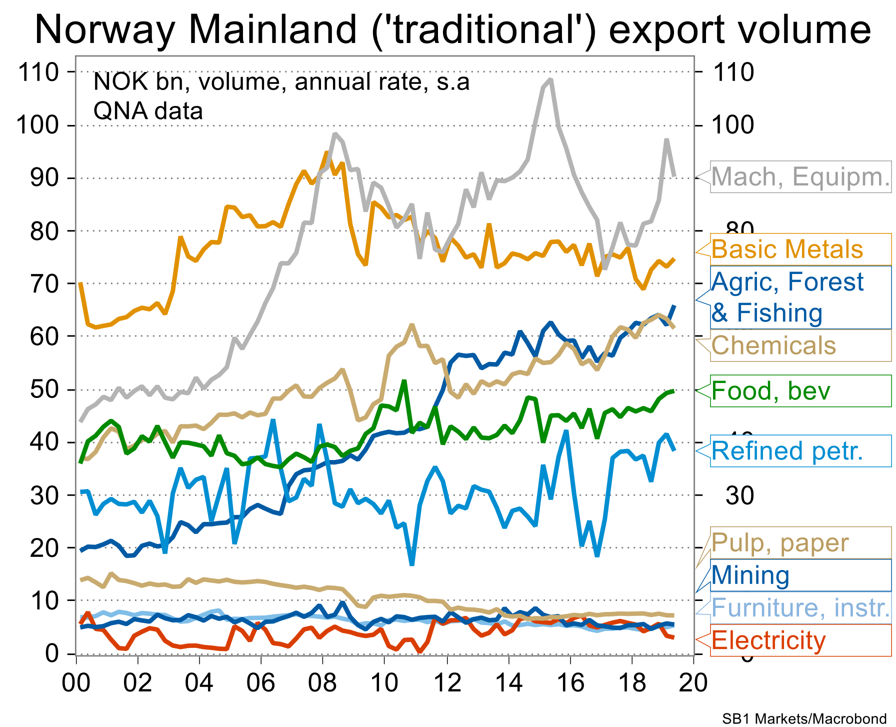


- Higher imports of machinery reflect higher oil investment demand

Mainland good exports are soaring, boosted by oil related goods

Oil related exports are thriving: Machinery/equipment exports and refined petroleum up

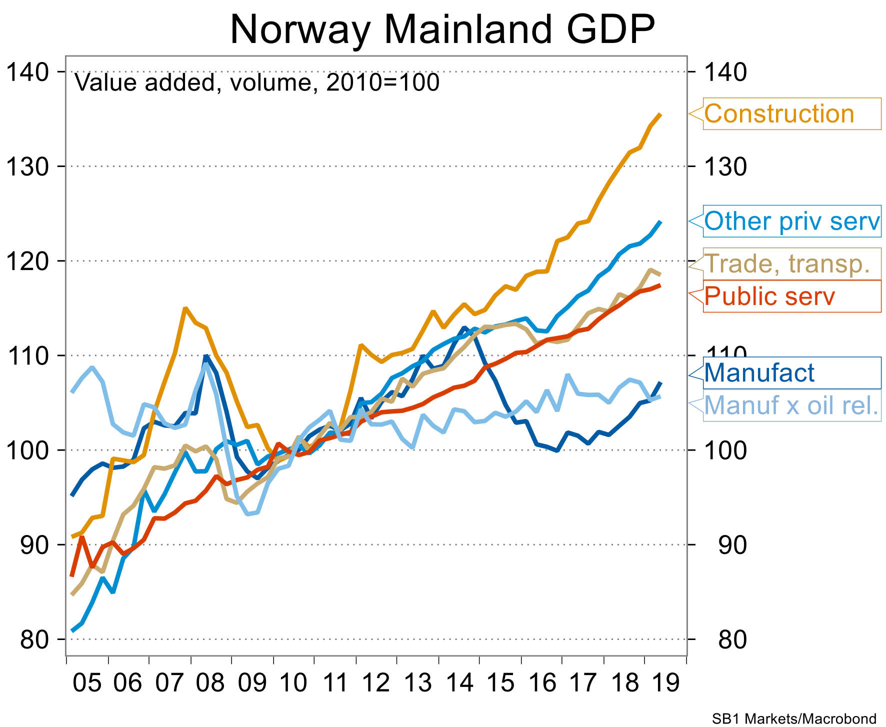


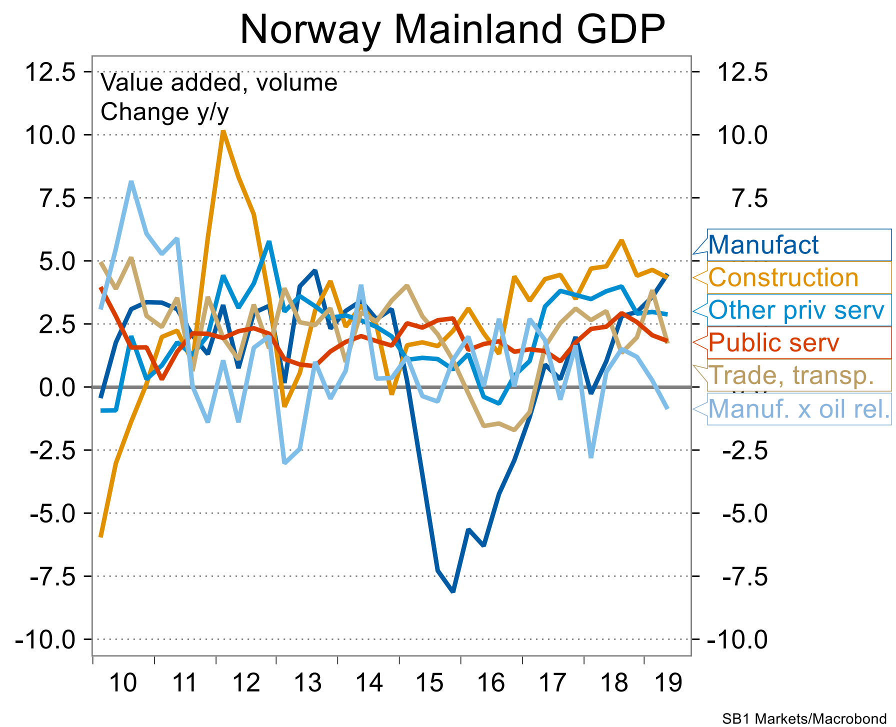


- Mainland exports ex refined petro. and machinery equipment inched down in Q2 but are trending up
- Chemicals are steadily increasing, as is fish exports (although fish exports was much stronger in Q2). Food exports gaining pace, other sectors not that impressive

Production: Broad based growth; a construction boom forever?

Manufacturing production is accelerating, just due to oil related, ex oil is now declining y/y

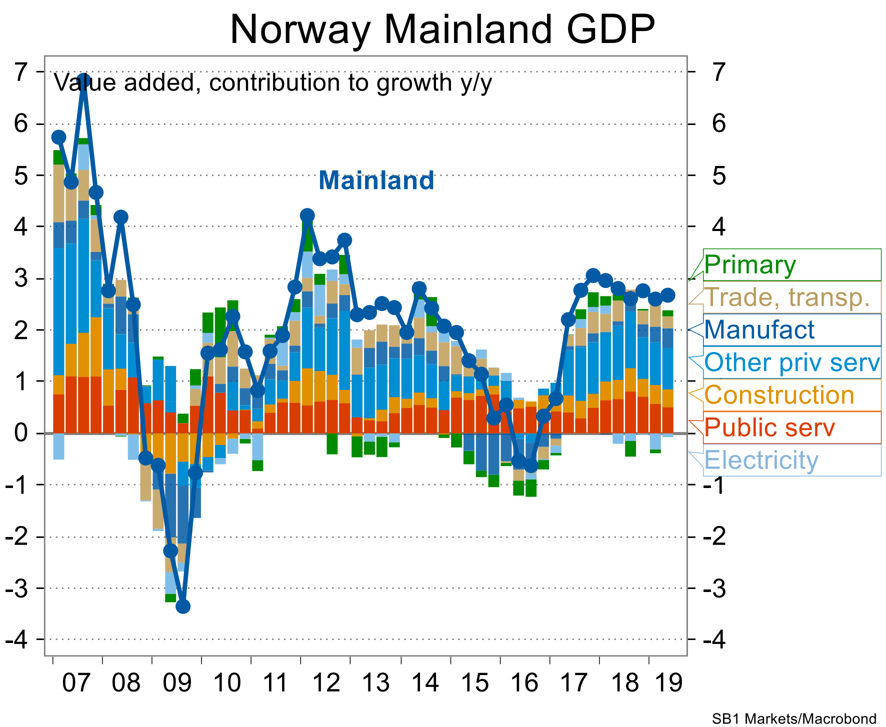


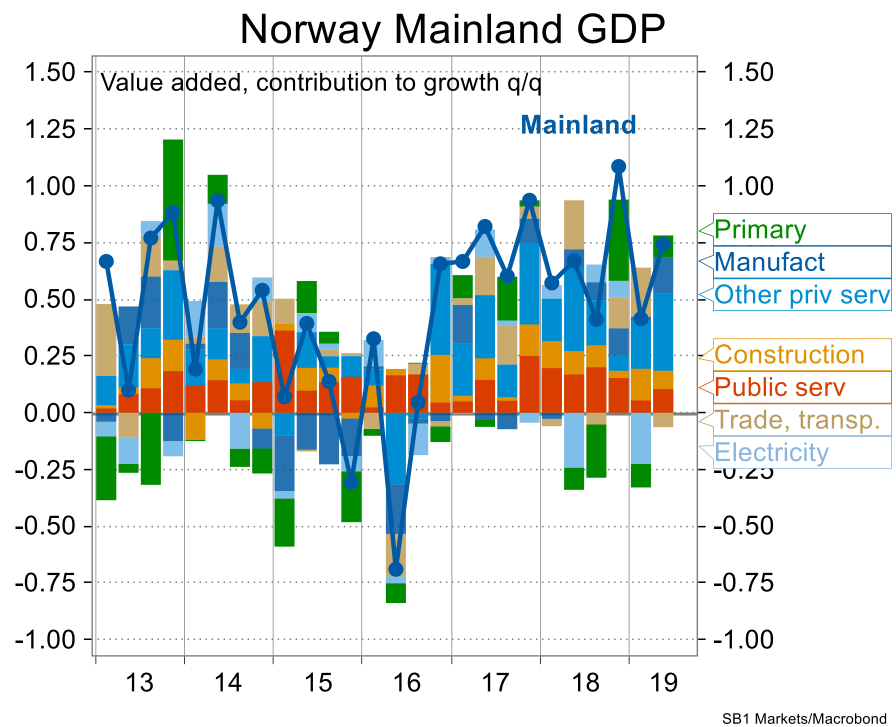


- Growth in private services has been hoovering around 3% recent quarters
- Construction production is up 4.3% y/y, slowly decelerating the past 2 years, from above 5% in mid-2017
- Manufacturing is surging, up 4.3% y/y in Q2, the highest since 2013 (with no help from x oil related sectors)
- Production in retail trade and transport fell to 1.7%. Not surprising, given sluggish retail sales

Production: A broad upswing in Q2, boosted by private services

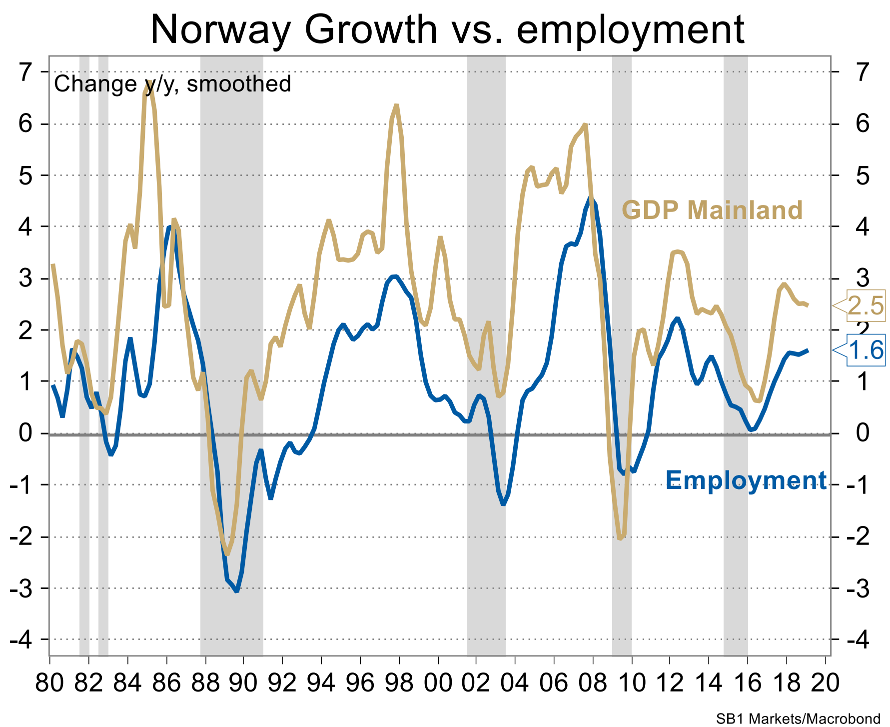
Just trade and transport dampened q/q growth marginally

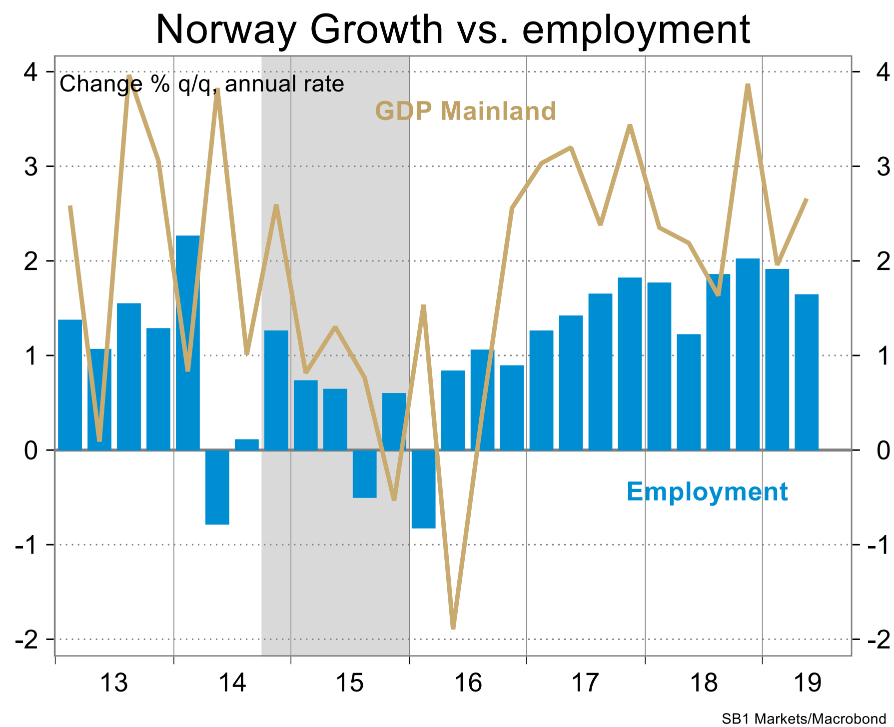




A tad softer but still solid growth in employment, up 1.7% q/q

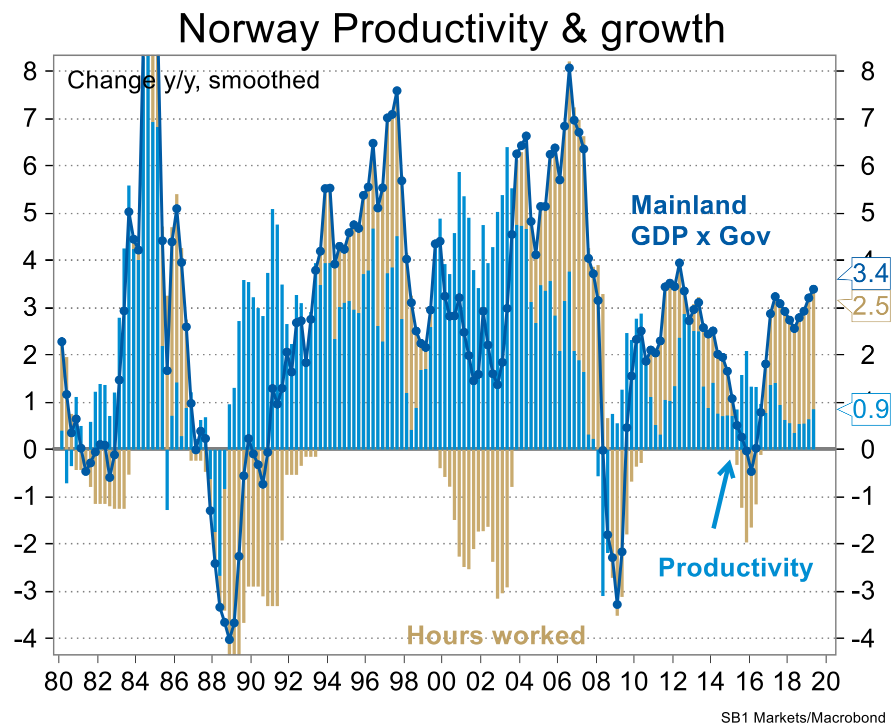
Annual growth accelerated to 1.9%, or a smoothed rate at 1.6%

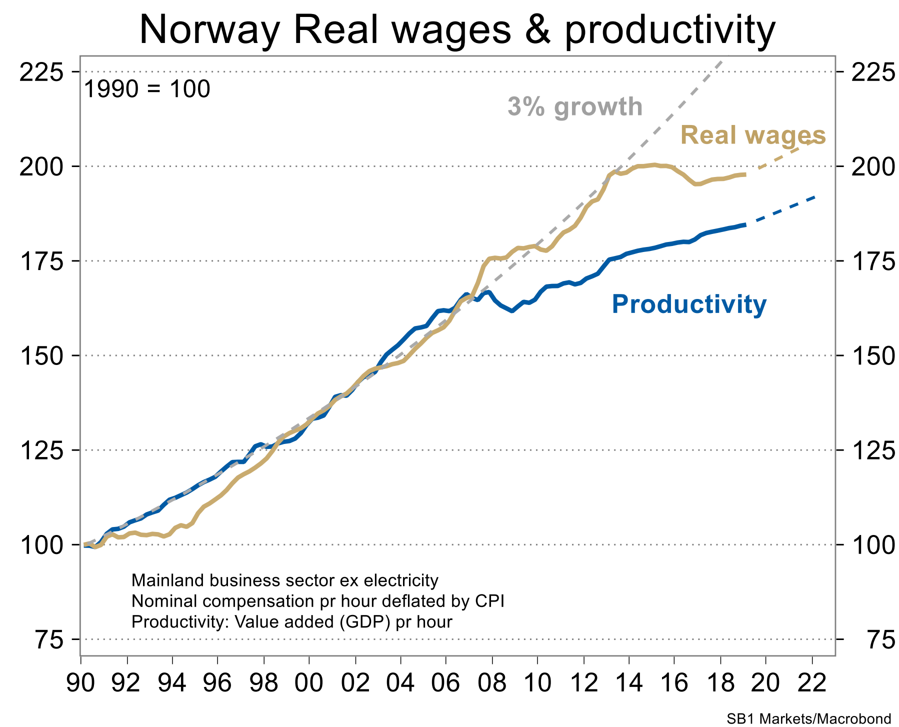




Productivity growth slowly turning up – real wage growth still modest

Total Mainland productivity growth fell to 0.4% y/y in Q2, a smoothed rate yields a slight upswing

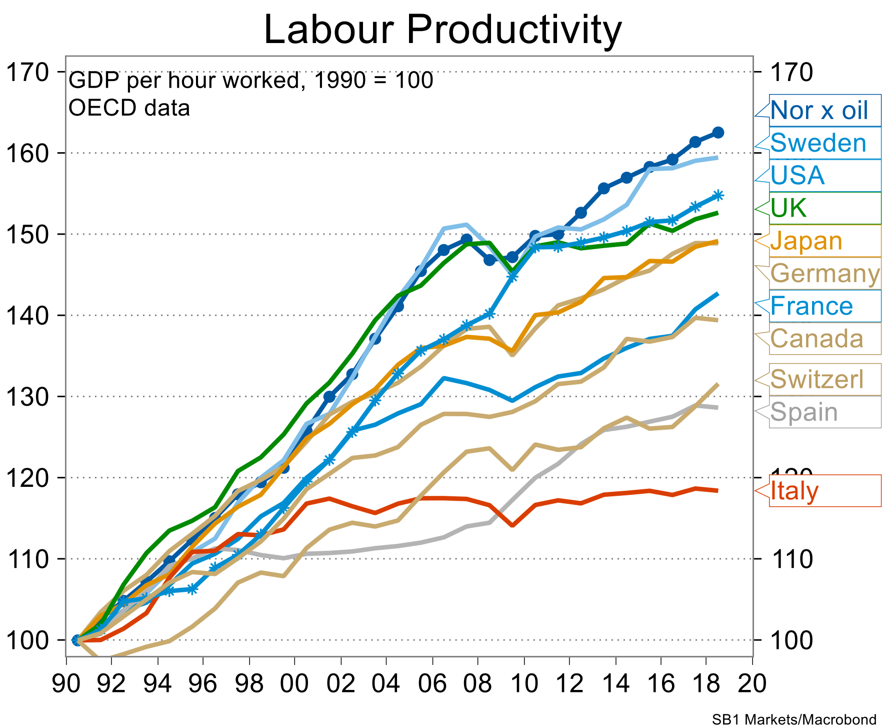


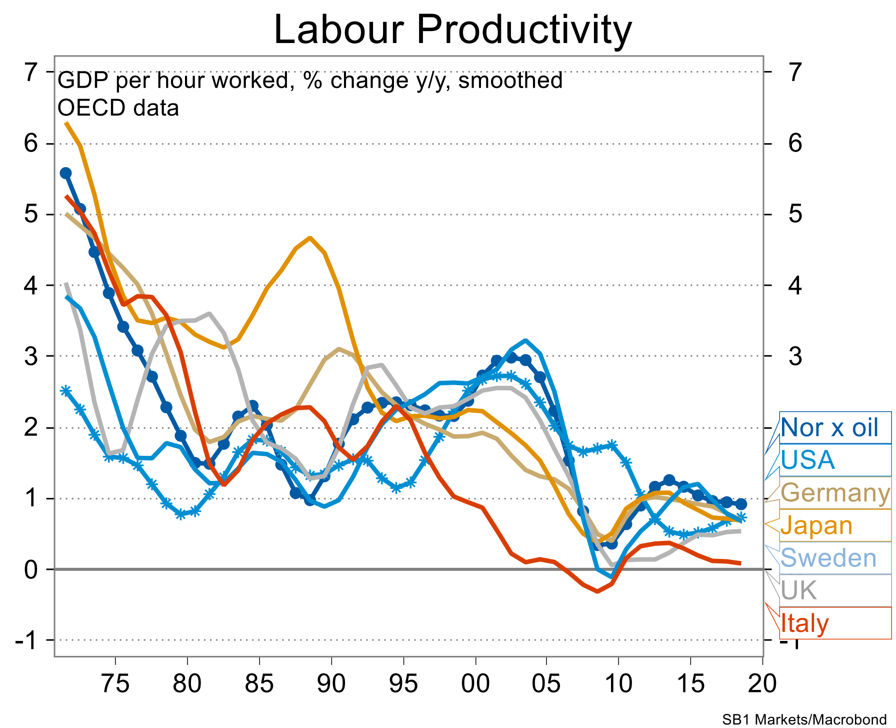


- Underlying productivity growth remains muted, at below 1%, and the past 4-5 quarters were revised down
- Hours worked explains 2.5 pp of the 3.1% growth in Mainland x government GDP (1 y smoothed)
- Real wages are slowly increasing, following the decline in 2016 but are still <u>lower than 5 years ago</u>!
- We expect just modest growth in real wages – as long as the underlying productivity growth is this slow

No specific Norwegian productivity slowdown

If anything, the opposite

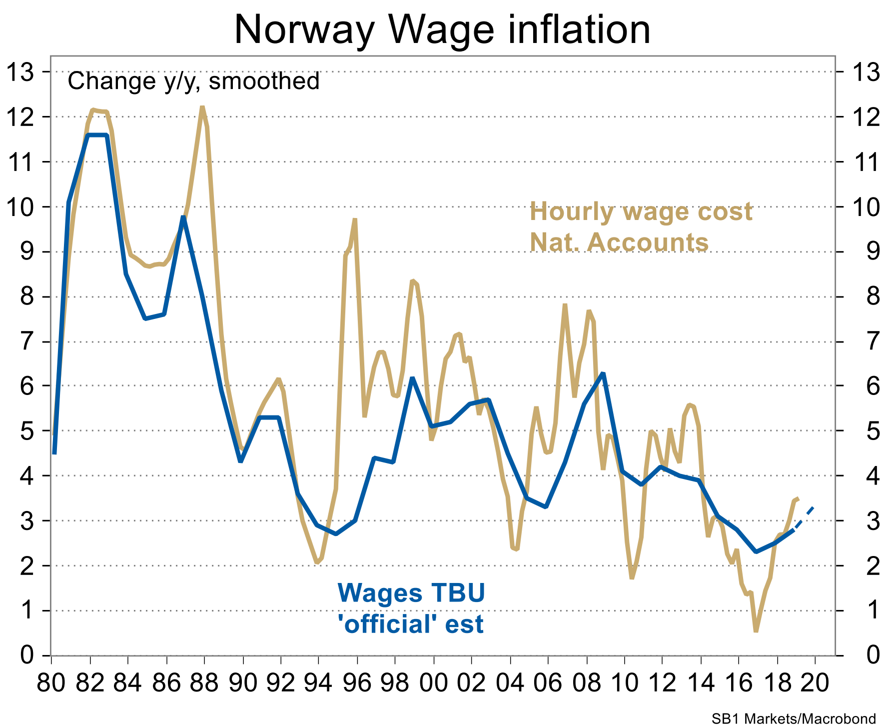


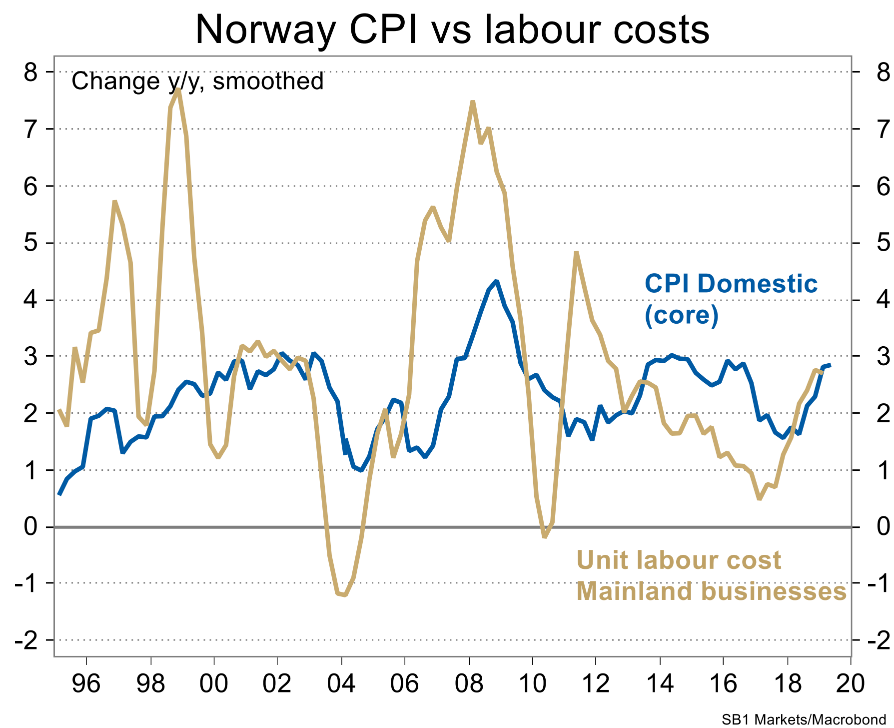


- Annual data compiled by OECD, last year is 2018

Wage inflation and cost inflation on the way up

(Volatile) hourly wage cost up 0.1 pp to 3.5% in Q2, unit labour cost inflation at 2.7%+ (smoothed)





- Hourly wage costs bottomed out in Q2 2017 and are back at the 2014 level, still below 'normal' Norwegian wage inflation

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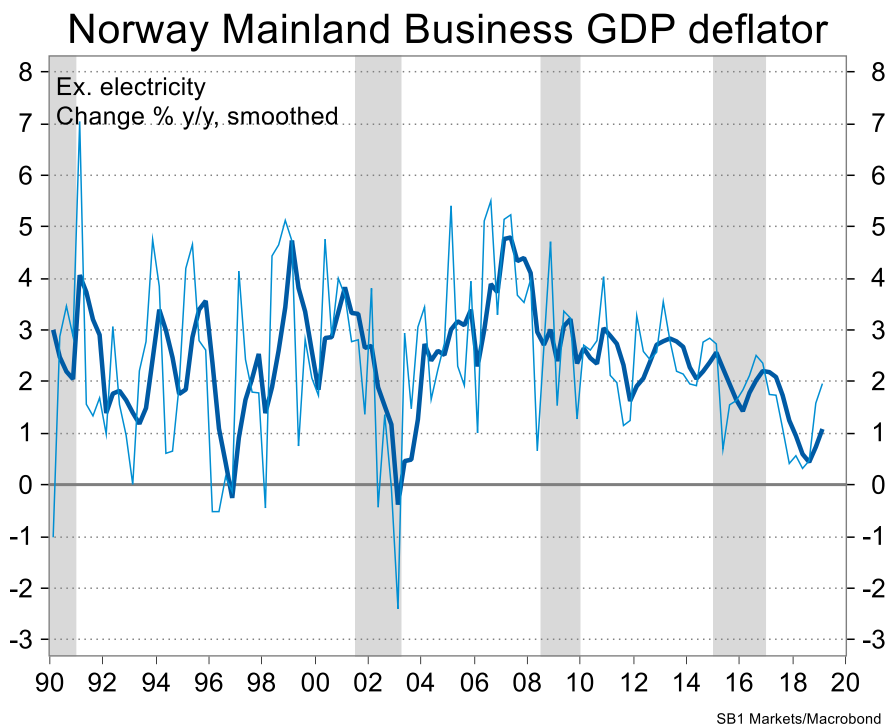
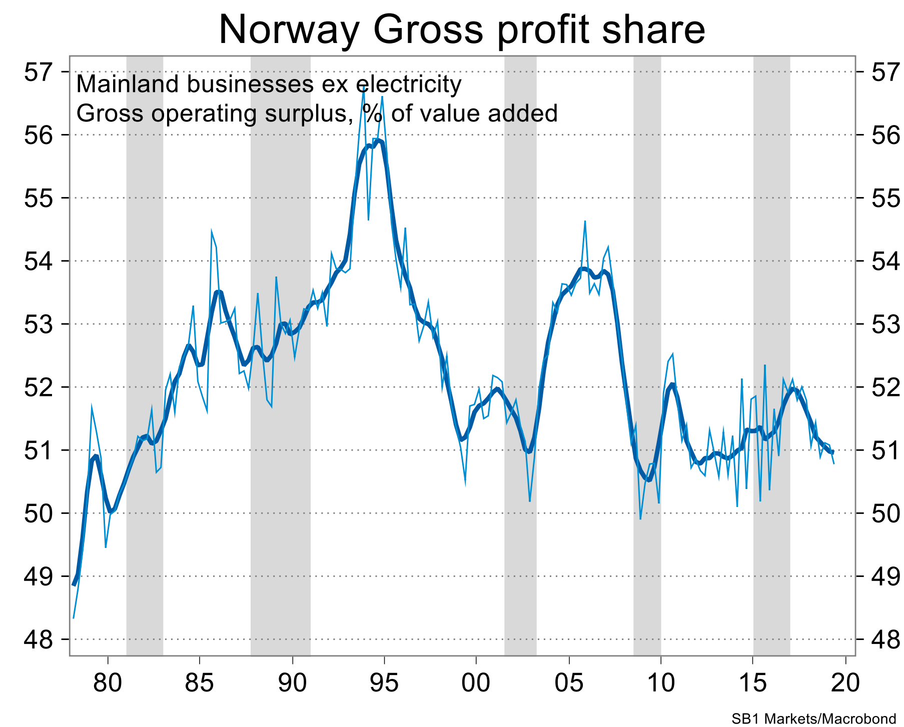
The profit share is under pressure – but less than previously assumed

GDP price deflator is growing (past years revised up) but still well below unit labour cost growth

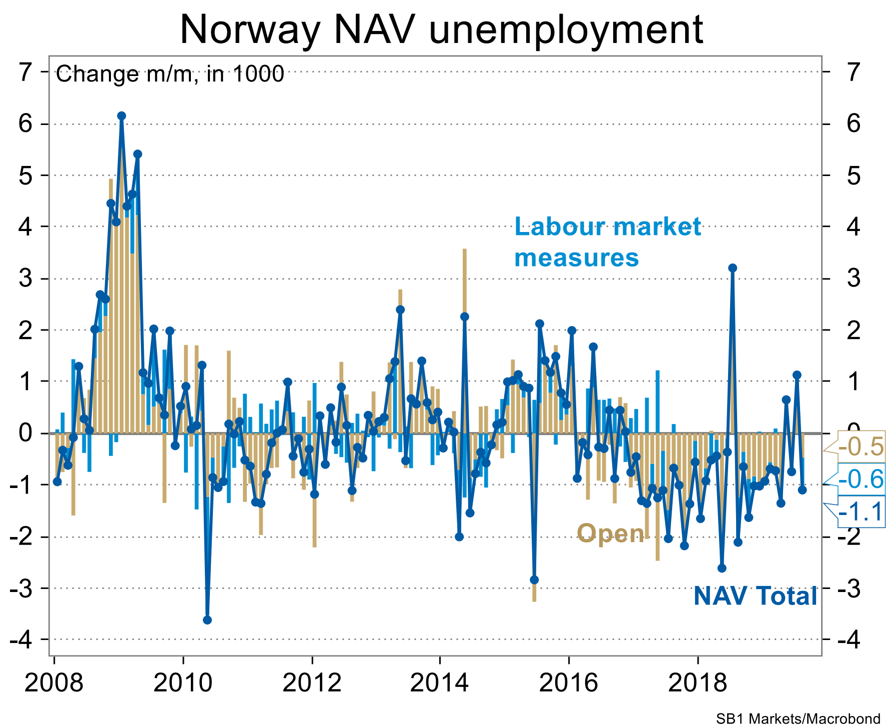


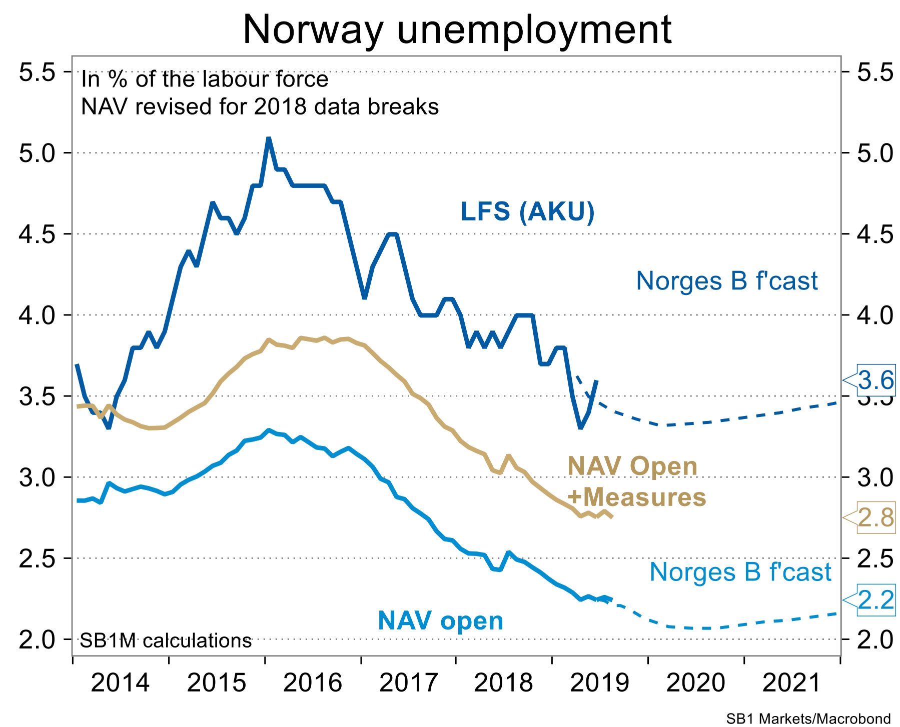


- The Mainland business GDP price deflator (ex the volatile electricity sector) rose to 2% in Q2 (not smoothed). Recent years were revised up, by some 0.5 pp – but the average growth recent quarters at 1% is not impressive
- As prices are rising slower than production costs (unit labour cost), the profit share in Mainland businesses is declining – as has been the case recent quarters – and the profit share is probably too low

NAV unemployment down in August, a reassuring sign

NAV total unempl. fell by 1.1' persons, following July uptick. Still, some signs of softer labour market





- NAV open unemployment fell by 500 persons in August, total unempl. (incl measures) by 1.100. The decline came after an uptick in July (and May), and the 3 month avg is down by just 240 persons. Unemployment is still declining, although at a softer pace. The open unempl. rate inched down to 2.2%, marginally below NoBa's f'cast (2. decimal). Some other signs of labour market softness:
  - » New jobless claims up in August, a higher no of announced layoffs recent months, and fewer new vacancies
- LFS unemployment is trending down and employment is still growing. We do not expect a sudden shift at the labour market at this point and business do not report any visible weakness. Nonetheless, a gradual softening is expected, by NoBa and us
- We stick with our view that Norges Bank will hike in September

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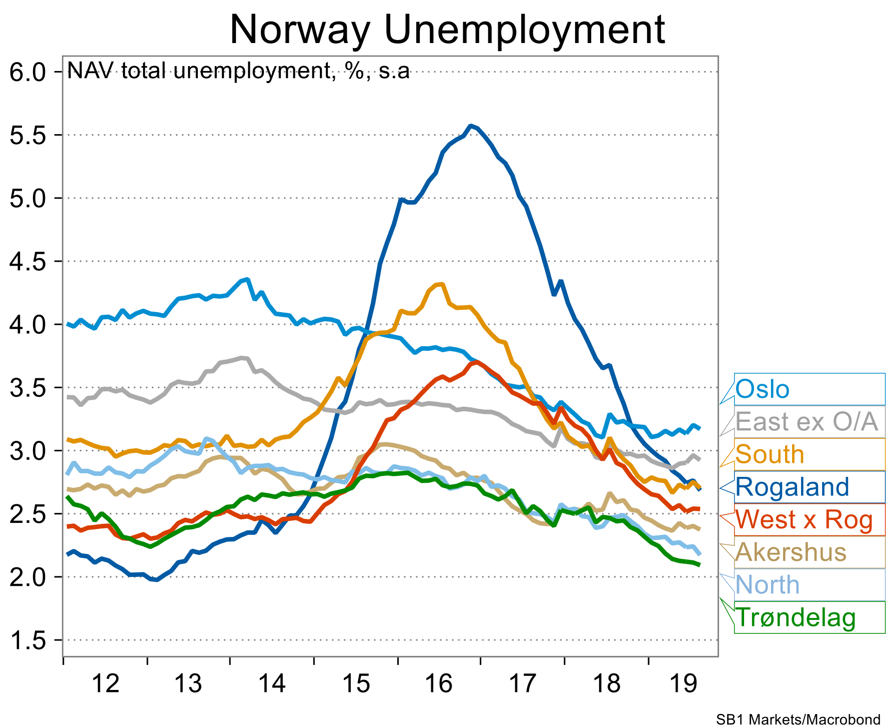
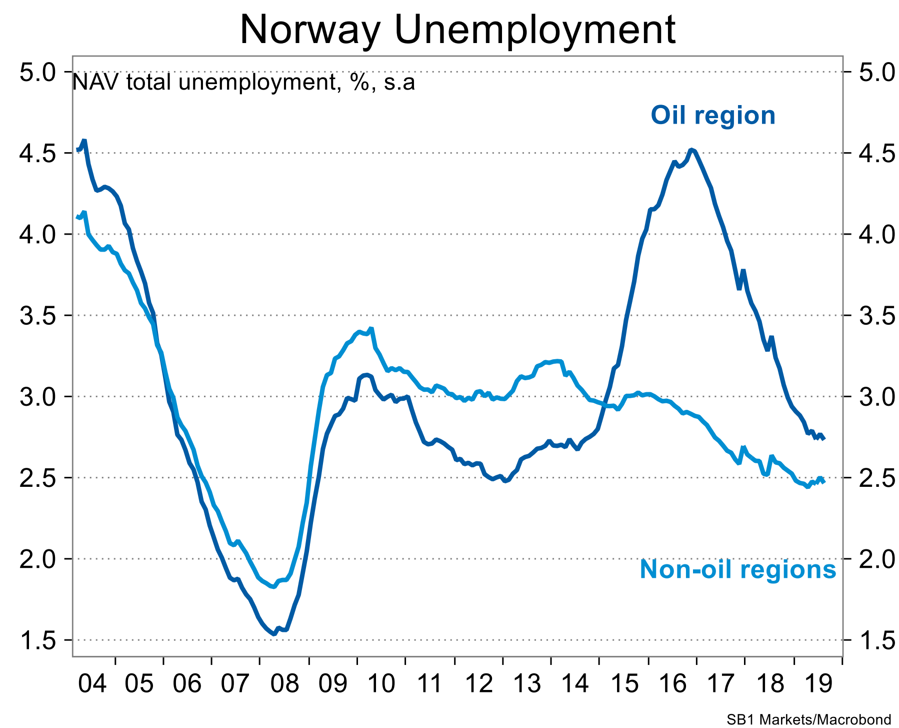
Soft spots in some regions recent months – mostly in non-oil regions

Unempl. marginally up in Oslo, other East, and South? Rogaland still heading steeply down



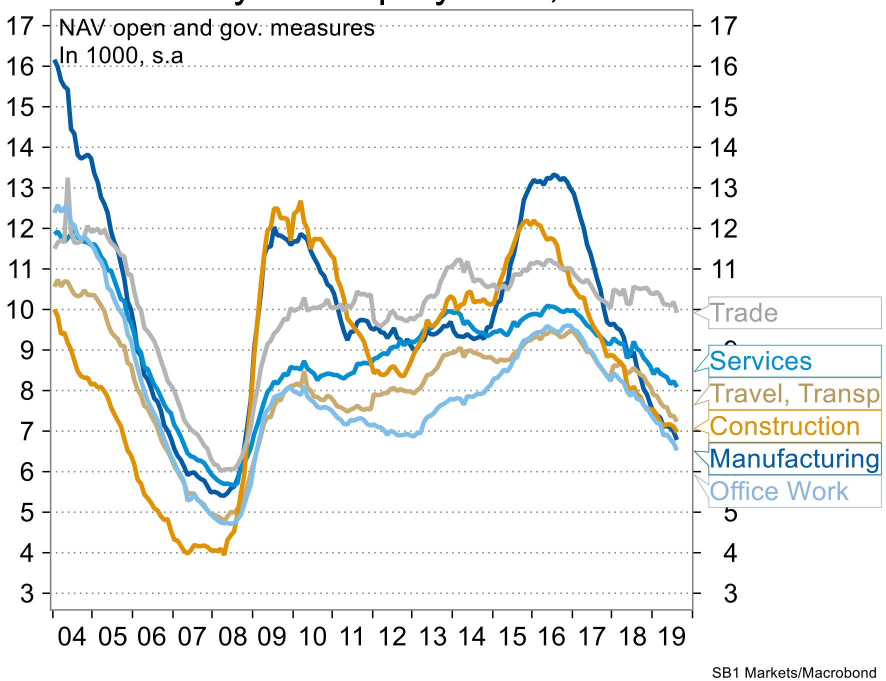


- Unemployment rates have flattened out/inched up in Oslo and Eastern counties. Some weakness in the South too
- Unempl. in Rogaland and the rest of the Western (oil) coast is still decreasing. Trøndelag and North sliding down
- The unemployment rate in the ‘oil region’ (Agder, Rogaland, Hordaland, Sogn & Fjordane, Møre & Romsdal) has dropped to 2.7%, from 4.5% in late 2016 and is just 0.2 pp above the non-oil regions

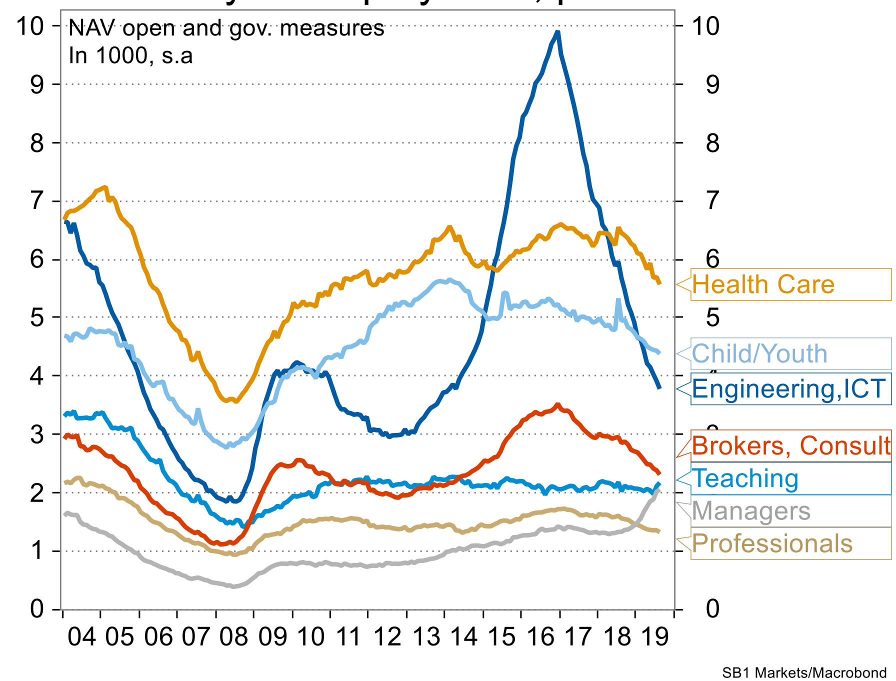
Unemployment is falling among most occupancies, even in retail trade?

Engineering, manufacturing, construction are dropping. Managers, teaching are heading up

Norway Unemployment, blue collar



Norway unemployment, professionals

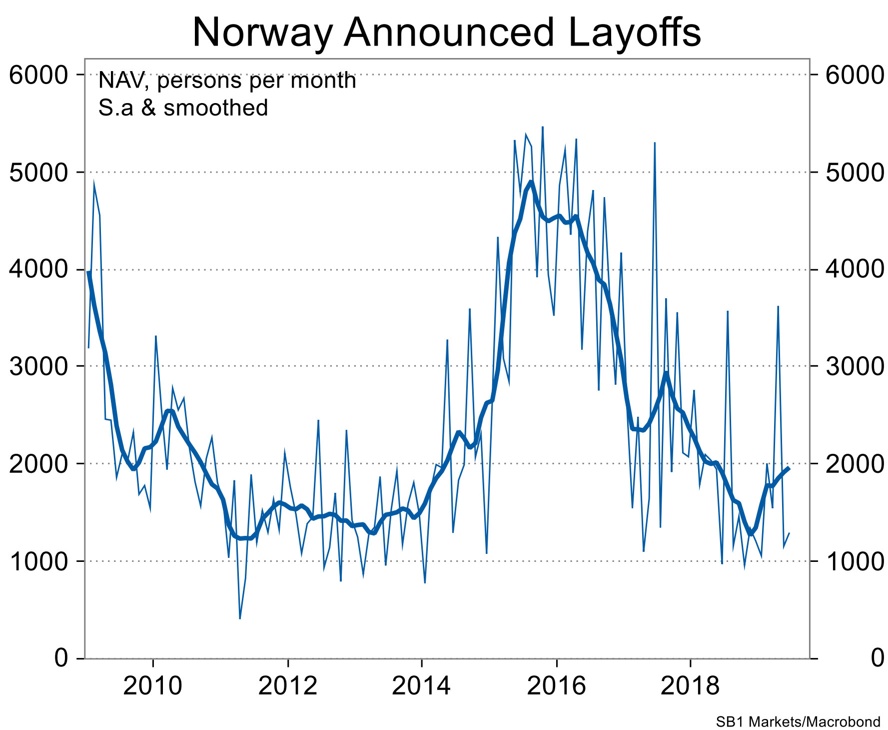


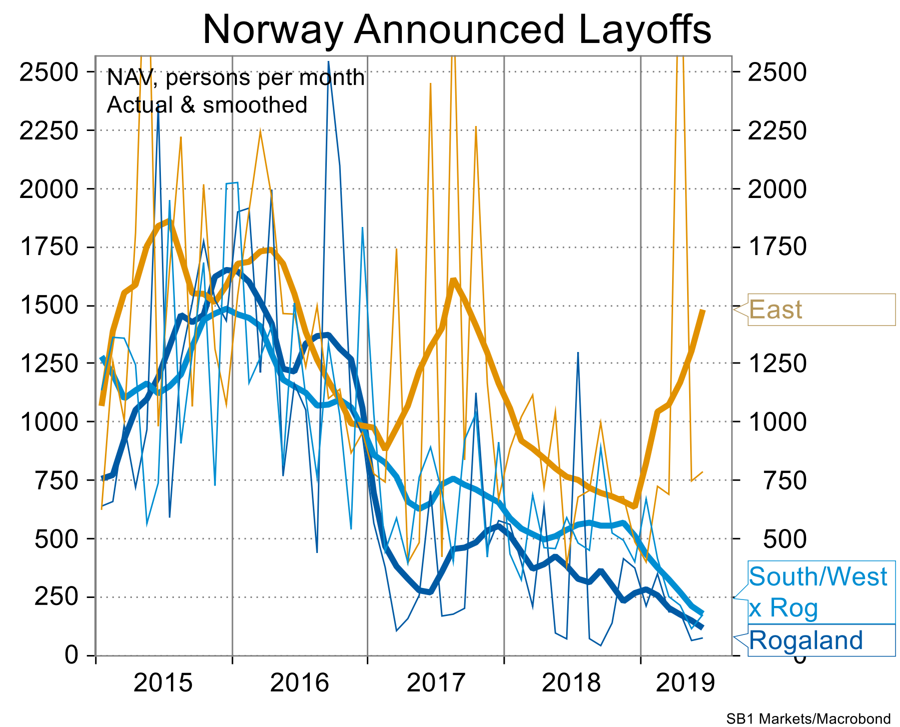
- Unemployment in engineering & ICT sectors and manufacturing is falling rapidly
- Most other sectors are heading down, ex teaching. And what is going on among managers? A change in definitions probably explains most of the increase among managers
- Retail trade has been the soft spot, no surprise given sluggish sales the past year. Unemployment is now inching down
- Unemployment in other ‘blue collar’ occupancies have dropped since 2015/2016, services somewhat slower than the others

Occupancy unemployment series are not fully adjusted for 2018 changes in NAV unemployment data collection methods

A low level of layoffs, but…

… the number of layoffs is heading slowly up from the late 2018 bottom, due to the East

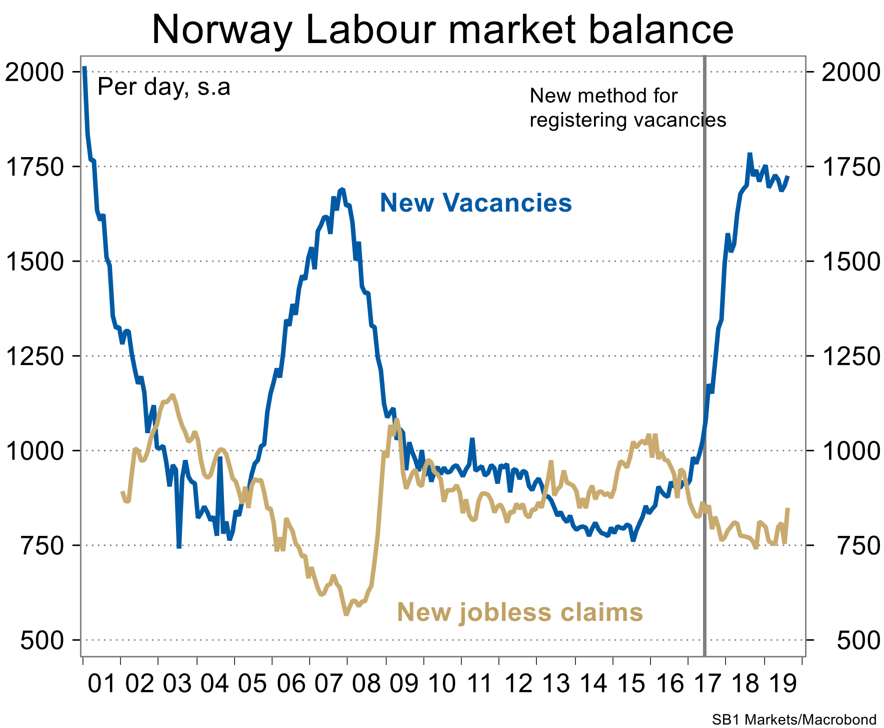


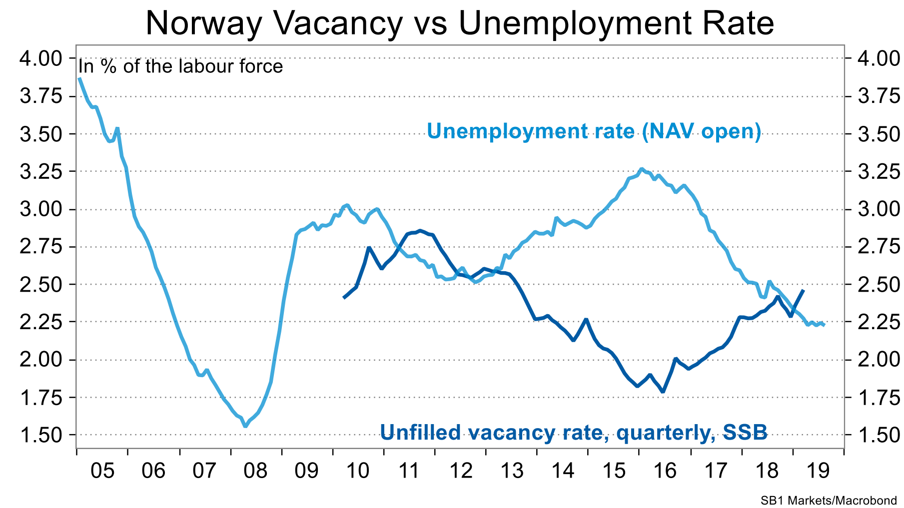


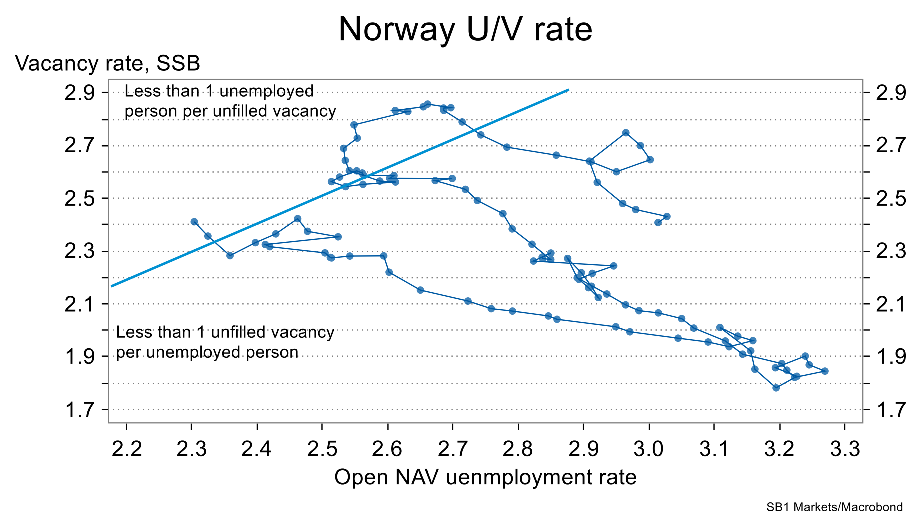
- These monthly data are very volatile and should not be taken too literally from one month to the next. The average of the past months is marginally up (incl the May hike though)

New jobless claims edging up? Fewer (but far from few) new vacancies

May be signs of a somewhat calmer labour market. SSB reported more unfilled vacancies, in Q1



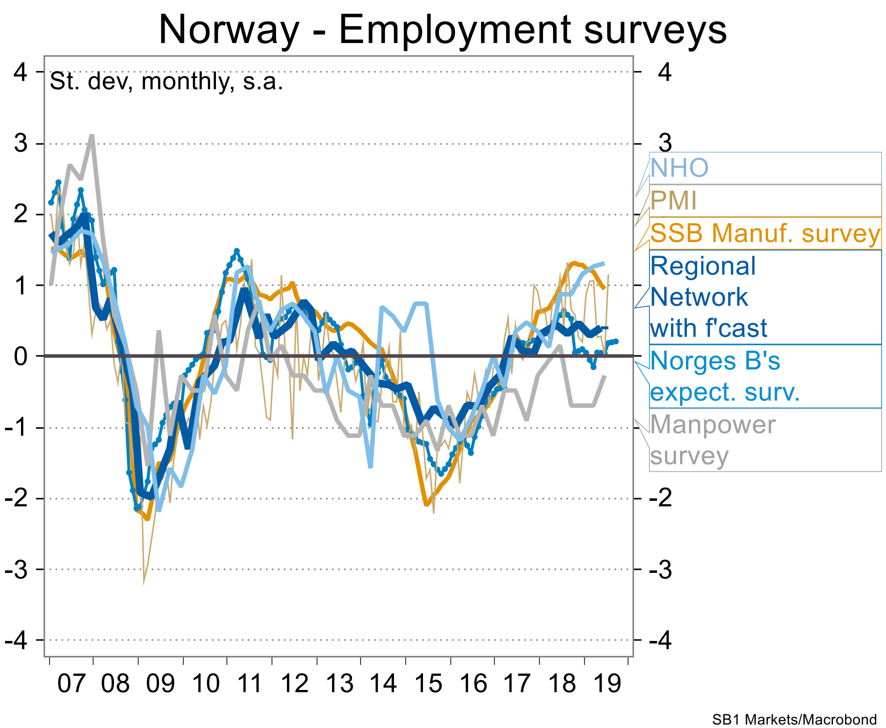


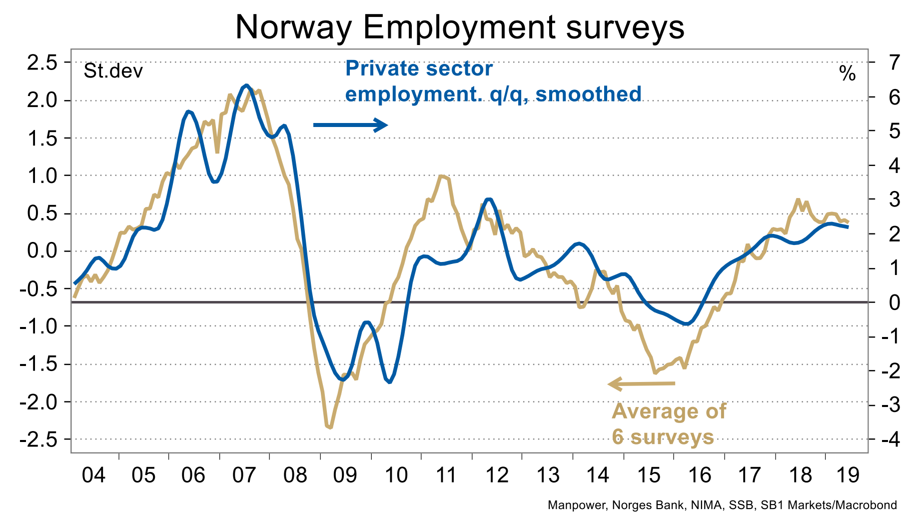


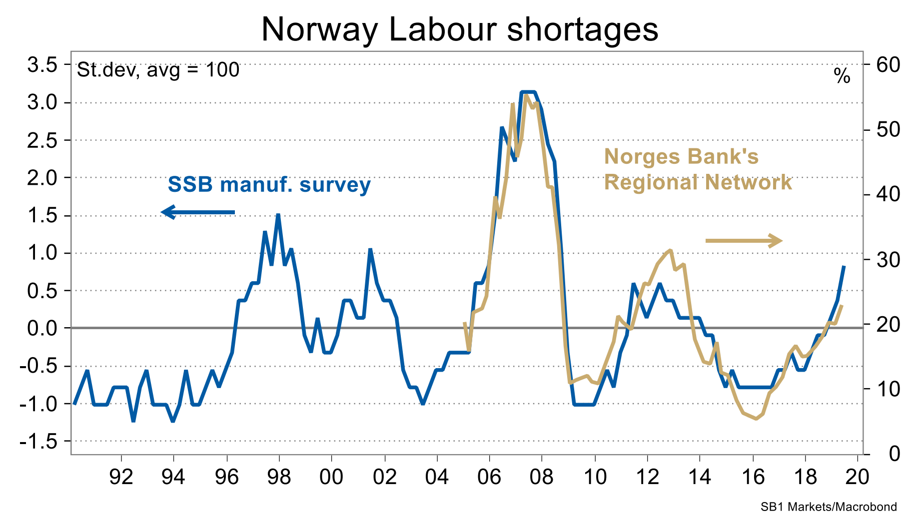
- New jobless claim spiked in August, to 850/day. New claims have flattened out the past year, <u>and the trend is not down anymore – and is may now be heading slowly up</u>
- NAV is reporting a soft decline in the <u>number of new vacancies,</u> as it has since the peak last August. Due to new collection methods, the level is not comparable to old data – but the decline is so far probably marginal
- On the other hand: SSB reported an increase in the no of unfilled vacancies in Q1 (no Q2 data yet), indicating a tighter labour market

Surveys report more lack of labour, not lower demand

Employment surveys have flattened out, signaling steady growth in demand

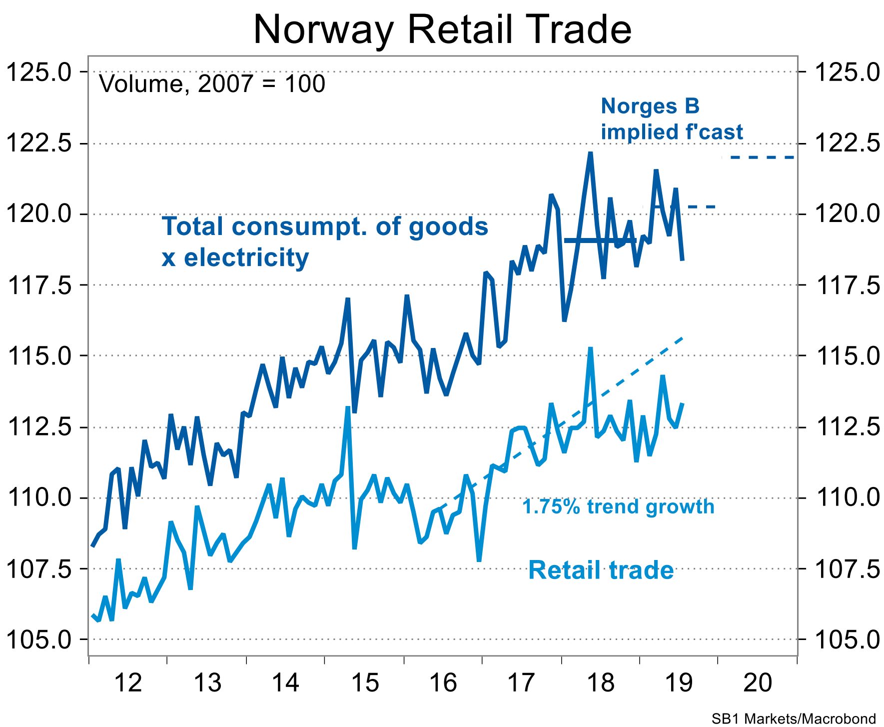


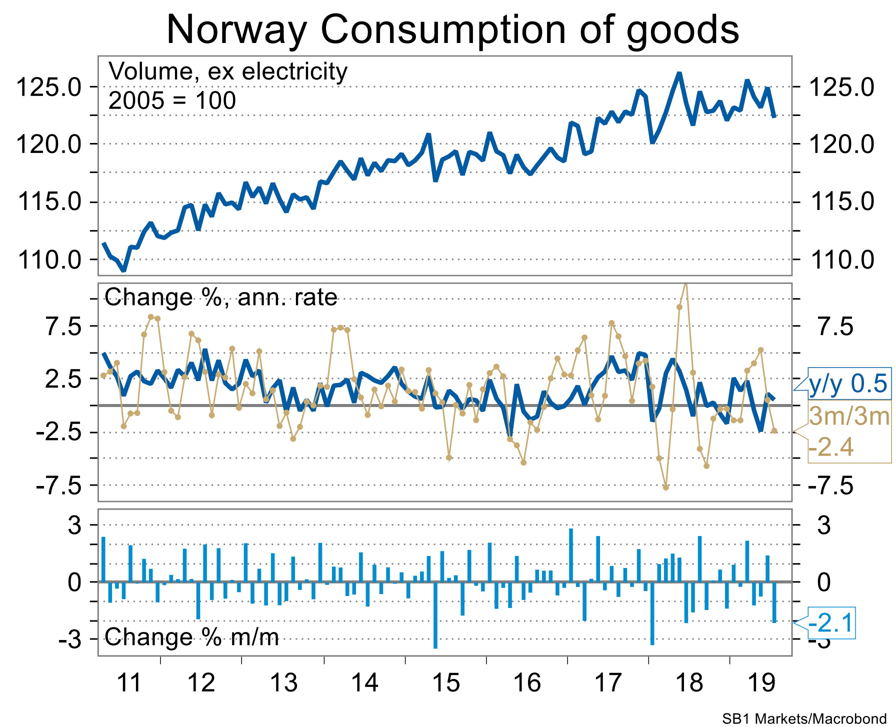




Retail sales improved in July, trending modestly up?

Retail sales rose 0.8%, underlying growth up 0.6%. Auto sales dragged total consumption down





- Retail sales volume (ex auto) increased by 0.8% m/m in July, close to our f'cast at 1.9% (consensus 0.4%). Sales are certainly not thriving, yet, the trend is most likely slightly upwards from the 2018 level. The speed so far into Q3 is 0.6%. The annual rate is modest at 0.9%
- Total consumption of goods (ex electricity) dropped 2.1% m/m, following a strong June. The downswing is solely driven by a retreat in auto sales, which are volatile from month to month. Underlying growth is up 0.7% (measured 3m/3m) but Q3 is off to a weak start. We stick to our expectation that subsiding price inflation will support volume growth the coming months
- Total consumption is anyway at Norges Bank's 2019 (implied) estimate, hence, household's goods demand is no argument for abandoning the hiking plans

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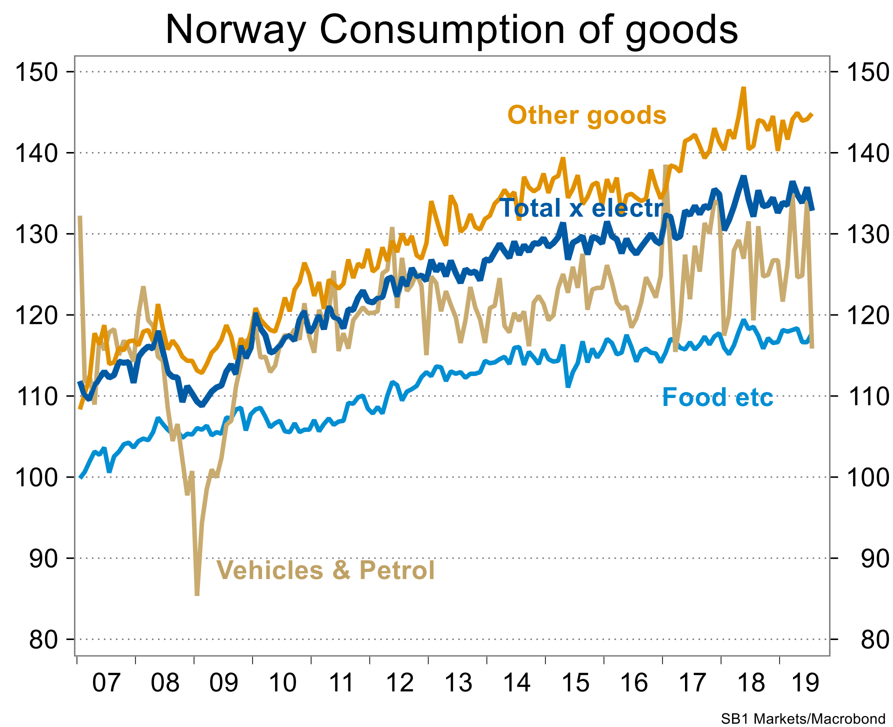
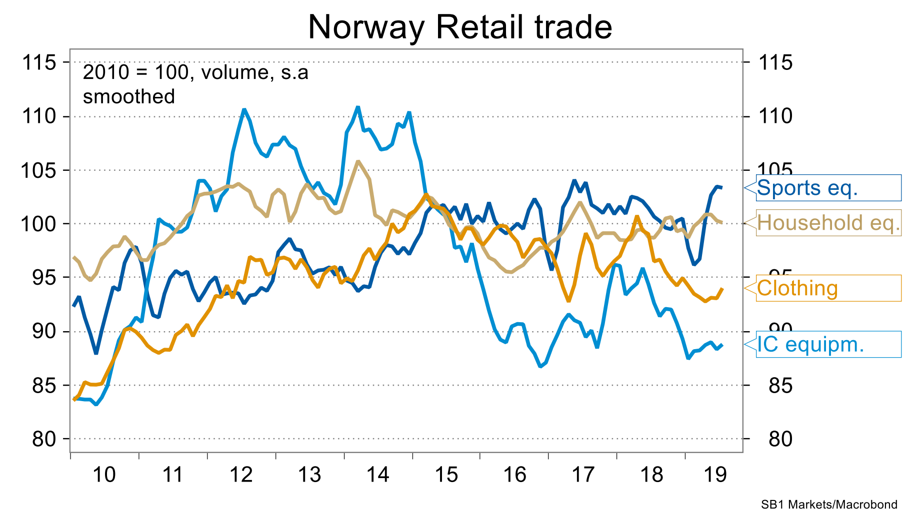
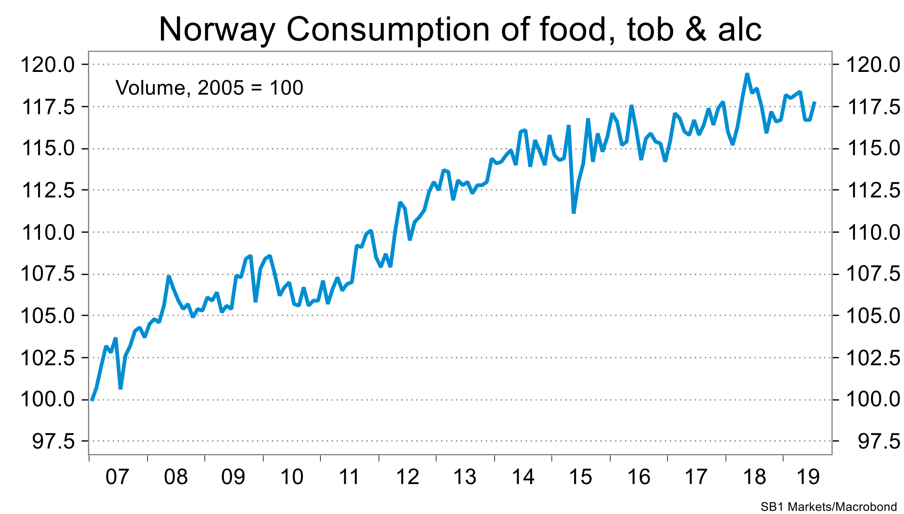
Consumers are buying more sports equipment, household equip.

Auto sales steeply down, trend softly down? Food sales more or less flat, short term



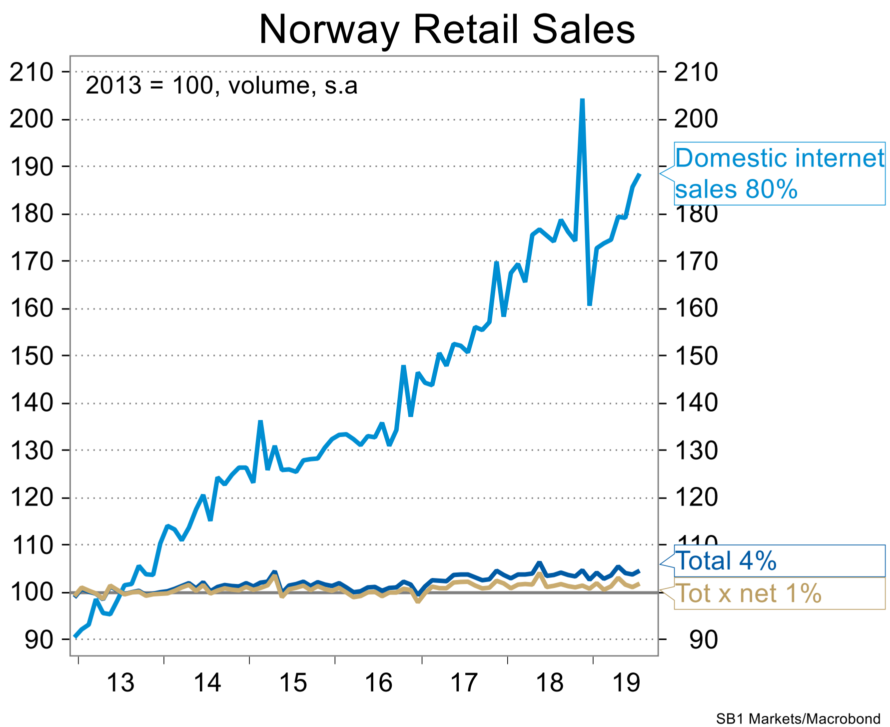


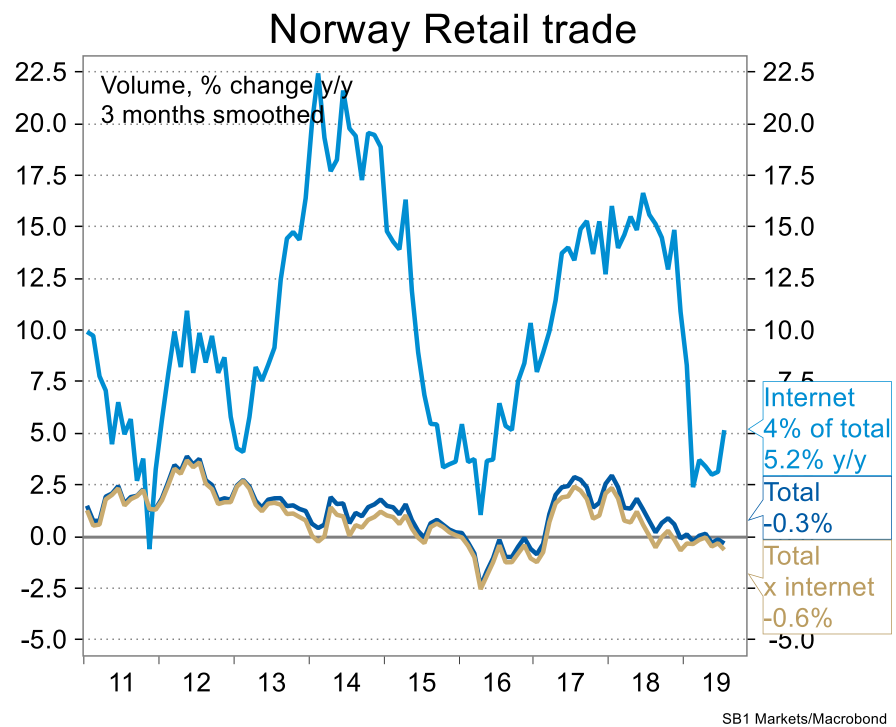


- Auto & gas sales slipped in July. Due to supply bottlenecks, particularly for electrical vehicles, the monthly data are ridiculously volatile. Trend flat/softly down
- Food consumption increased in July but the short term trend is flat, long term up
- Other consumer goods are not very impressive, clothing and IC equipment have fallen

Internet sales (domestic) picking up but growth is much lower than 'usual'

Still, over the past 6 years, almost no growth in sales from the 'old' physical outlets

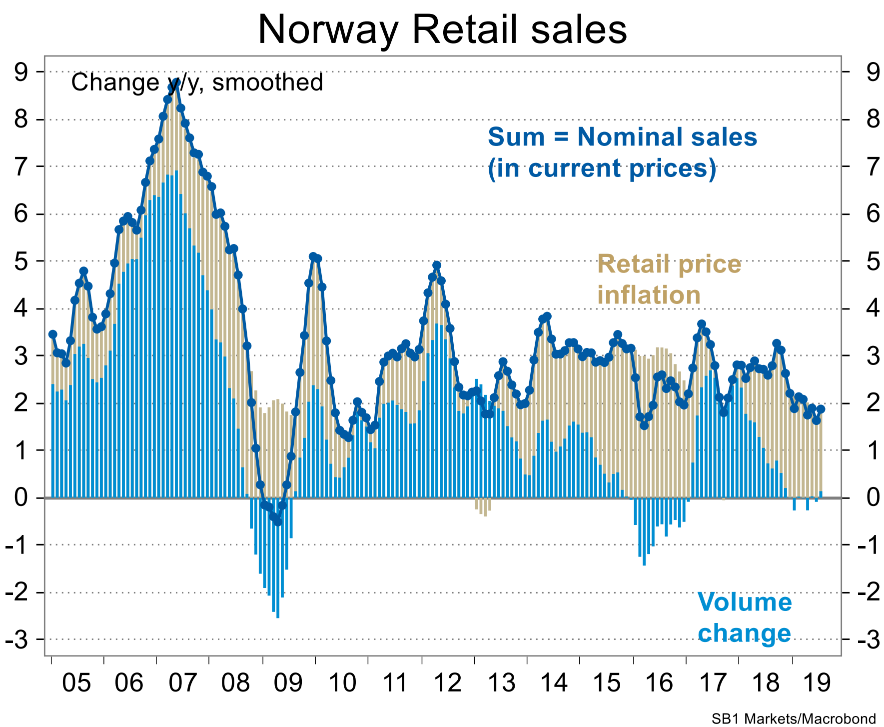


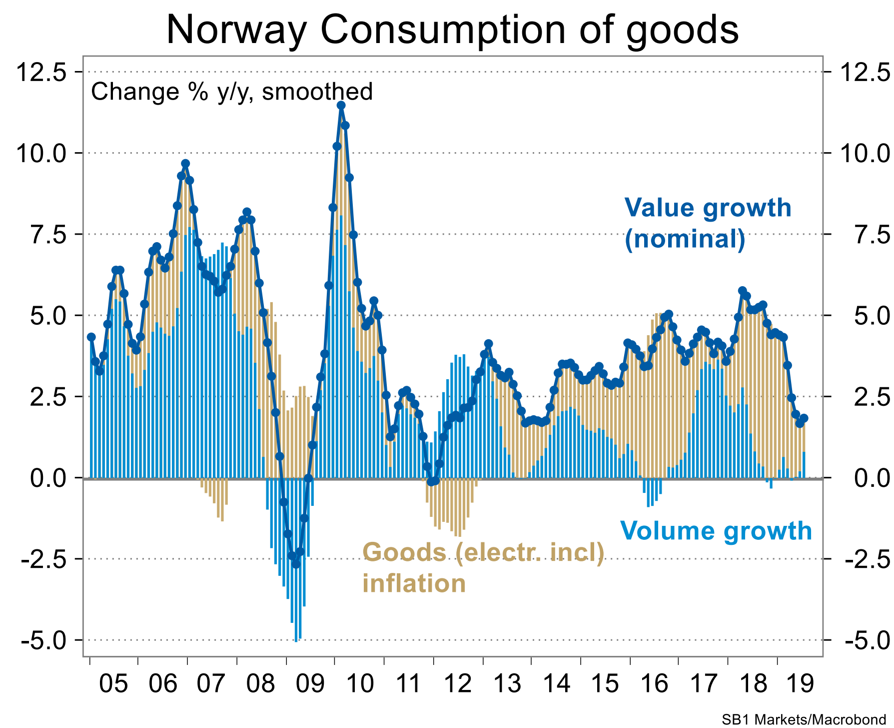


- The retail trade data cover only sales statistics from domestic outlets, not imports. From 2018, SSB included internet sales from abroad in the total consumption index but these figures are just estimates based on domestic internet sales
- SSB estimates that internet shopping from foreign sources (both services and goods) equalled NOK 40 bn in 2017, of which goods constitute the half, some NOK 20 bn. Internet import of goods have doubled past 5 years, more or less like sales from Norwegian outlets
  - If so: 'Direct' imports have increased by NOK 10 bn since 2013, equalling more than 2% of domestic retail sales since 2013
  - Domestic sales (in volume terms) is up 4% since 2013. If we add on an 2 pp contribution from internet sales from abroad, the total is up 6%.
  - Out of these 6%, 1 pp is sold in ordinary shops domestically, 2.5% via domestic net outlets, and 2.5% via foreign sites

Retreating price inflation but still modest volume growth

Total goods inflation has slowed to just 1%, from 5%, the cash impact is probably limited, so far

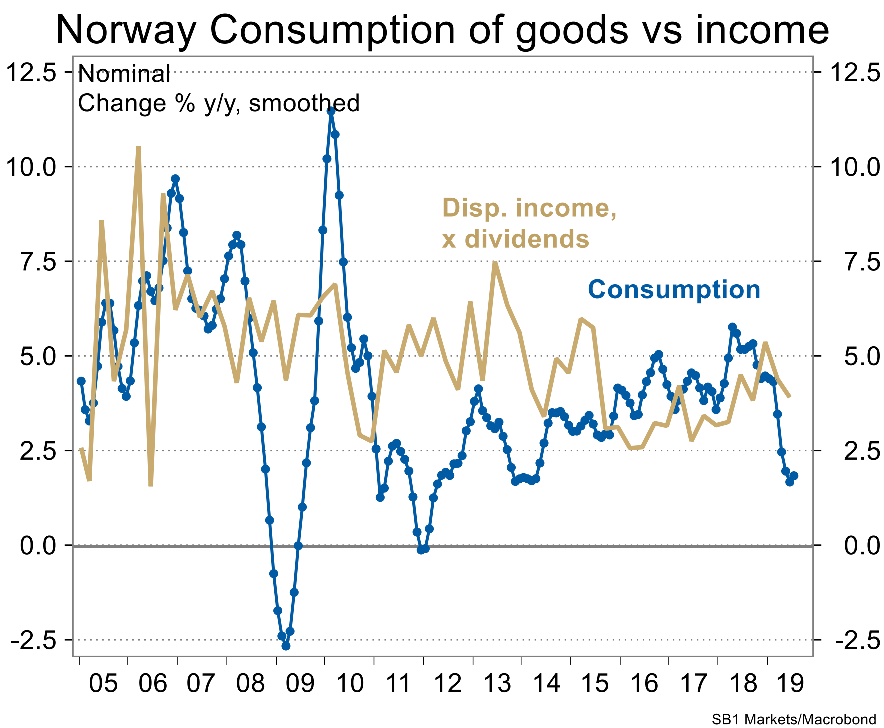


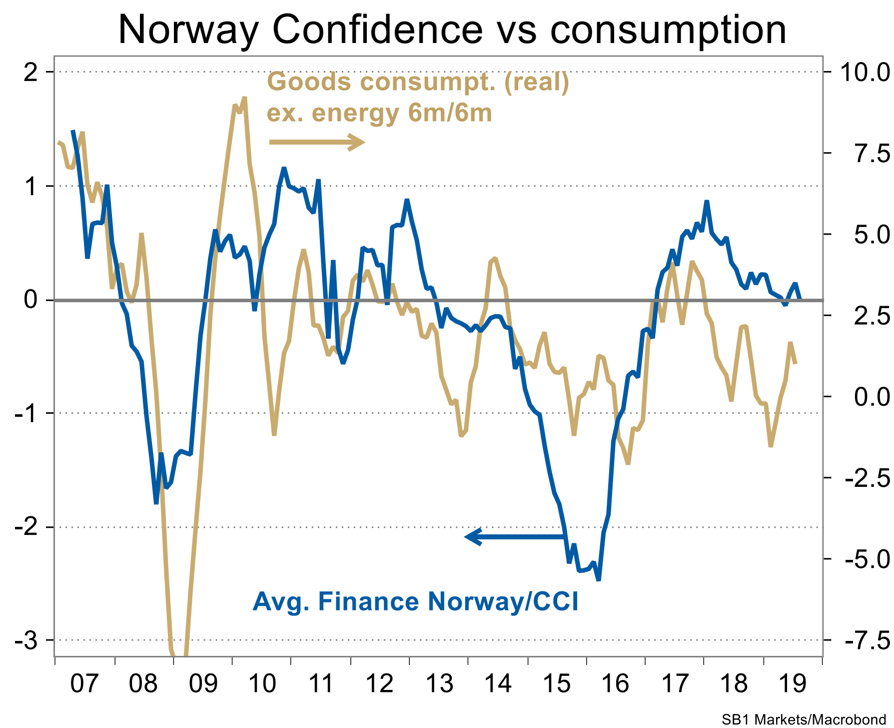


- Growth in nominal total consumption of goods has slowed sharply, to 1.8% y/y in July. The downswing is driven by retreating price inflation, primarily due to a sharp decline in electricity prices. Volume growth may now be heading up, at 0.8% y/y in July
  - » The decline in electricity prices have probably not yet been fully felt by consumers due to the lag between changes in prices, and households' actual payments which anyway are mostly done automatically, through their bank accounts. Thus it will take time for consumers to recognise the gain – and start spending the money saved on the electricity bill
- The annual growth in nominal retail sales is 1.9%. Volume growth remains muted in spite the decline in price inflation

Household income and confidence do not signal a rapid consumption slowdown

Both disposable income growth and confidence are pointing to somewhat higher consump. growth

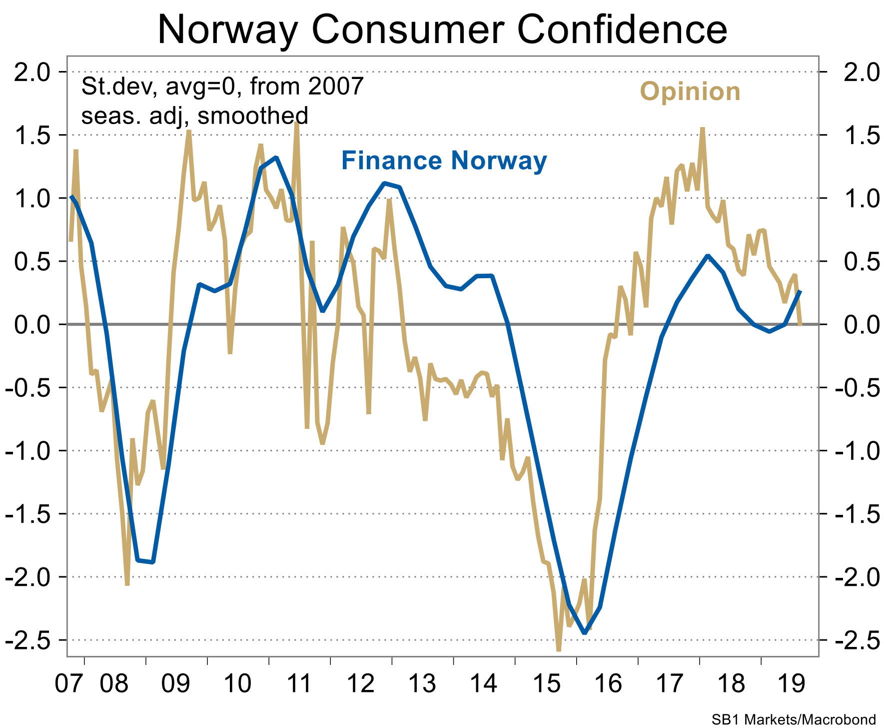




- Disposable income ex dividends was up 3.9 y/y in Q2 (our est), and the savings rate is now slowly increasing slowly again and it probably grew marginally in Q2
- Consumer confidence has softened, the average of Finance Norway survey (which rose in Q3) and Opinion's consumer sentiment survey (which fell sharply in August, check next page) are on the average level since 2007, and does not signal weaker consumption

Consumer confidence slips, according to Opinion's CCI

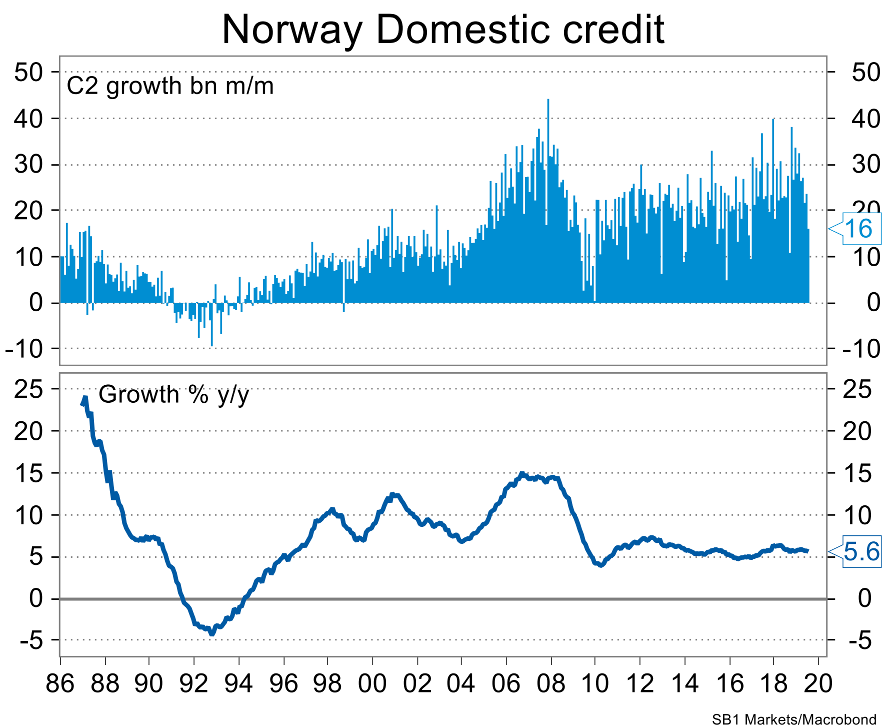
Opinion reports the weakens sentiment since 2016. Mixed surveys, Finance Norway turned up in Q3

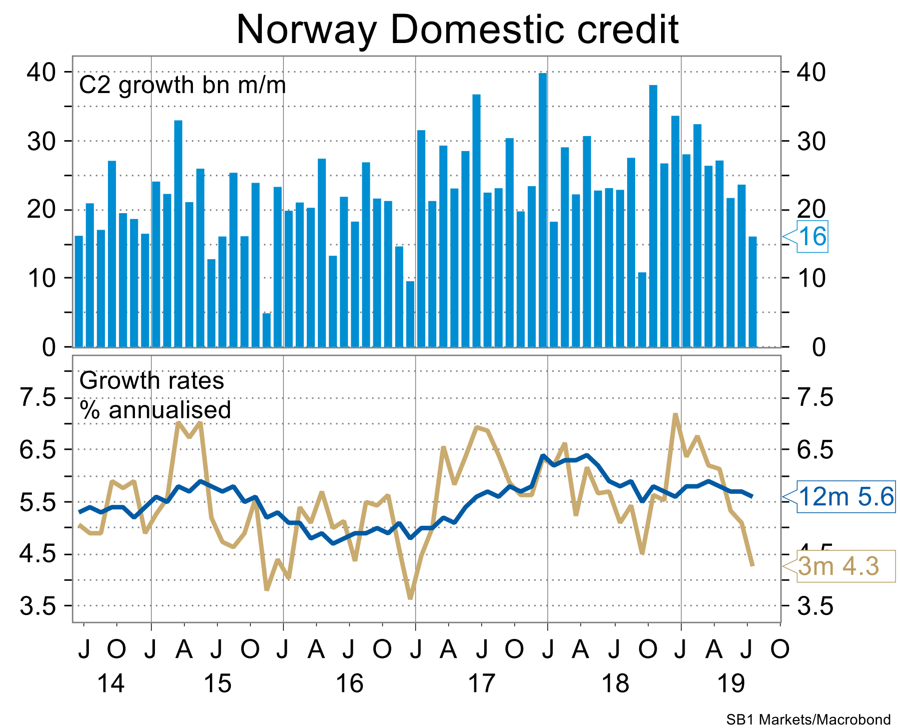


- Opinion's index fell sharply, and down to an average level in August, after inching up in June and July. The trend is steady down
- Finance Norway's consumer conf. index rose 17 in Q3 from 14 in Q2 (revised from 12). Confidence weakened through 2018 but has recovered in Q2 and Q3. Consumers are far more optimistic than during the oil downturn (2015-2017), but less than in average (since 1994, but above the avg since 2007, shown on the chart above)

Credit growth down to 5.6% in July, due to student loan -> grants

Easing corporate credit is driving total credit growth down (after a spike in ‘18), households growing steadily

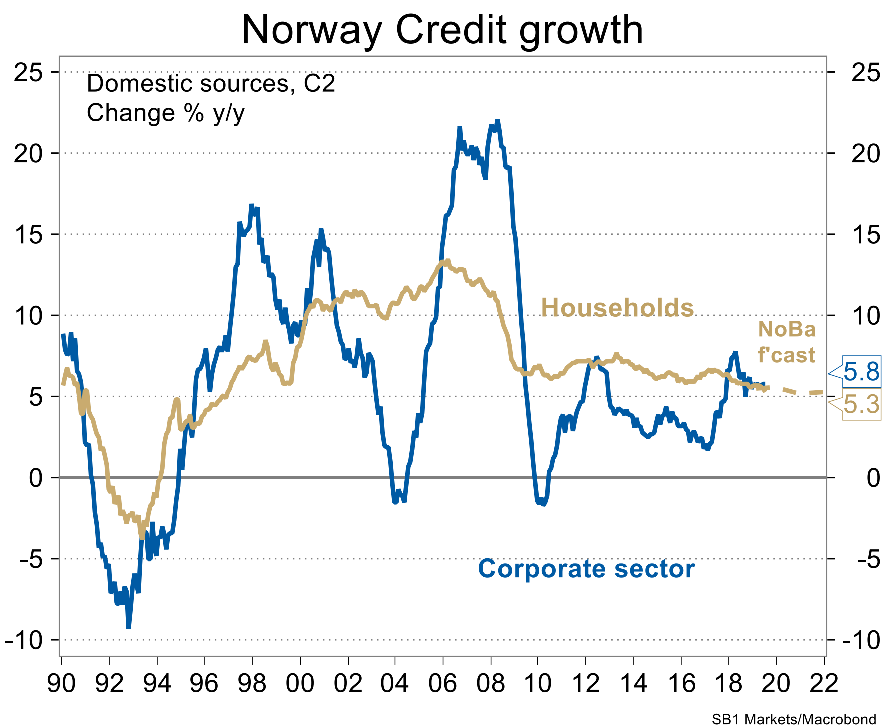


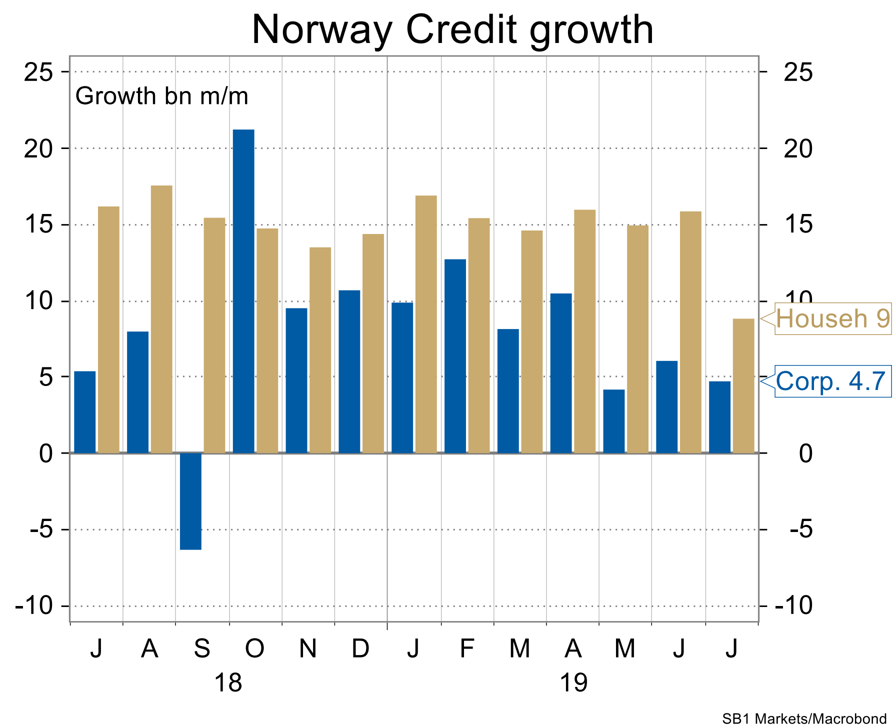


- Total domestic debt (C2) rose by just NOK 16 bn m/m in July, the lowest m/m growth in a year – due to student loans (see below). The annual rate inched down 0.1 pp to 5.6%, we expected up to 5.8%. Average growth over the past 3 months slowed to 4.3%, from 6% some months ago. Still, overall growth has held steady since 2013
- Household credit growth cooled in July and the annual rate fell 0.2 pp to 5.3%. However, the whole decline was due to a changed period for conversion of student loans to grants (usually in Nov, now in July). So far, there are no indications of a pullback in household loan demand following the interest rate hikes
- Corporate credit growth has slowed this year, after a surge in late 2018. The annual rate is steady at 5.8%, below our f’cast

Household credit appetite survives the interest rate hikes?

No signs of curbing household credit growth, the July slowdown was just technically



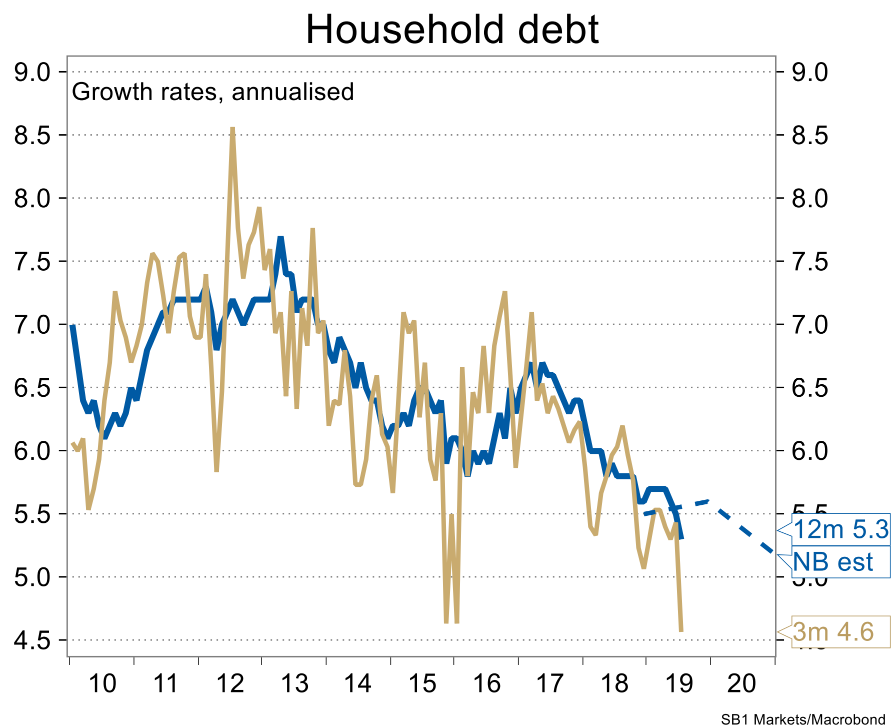


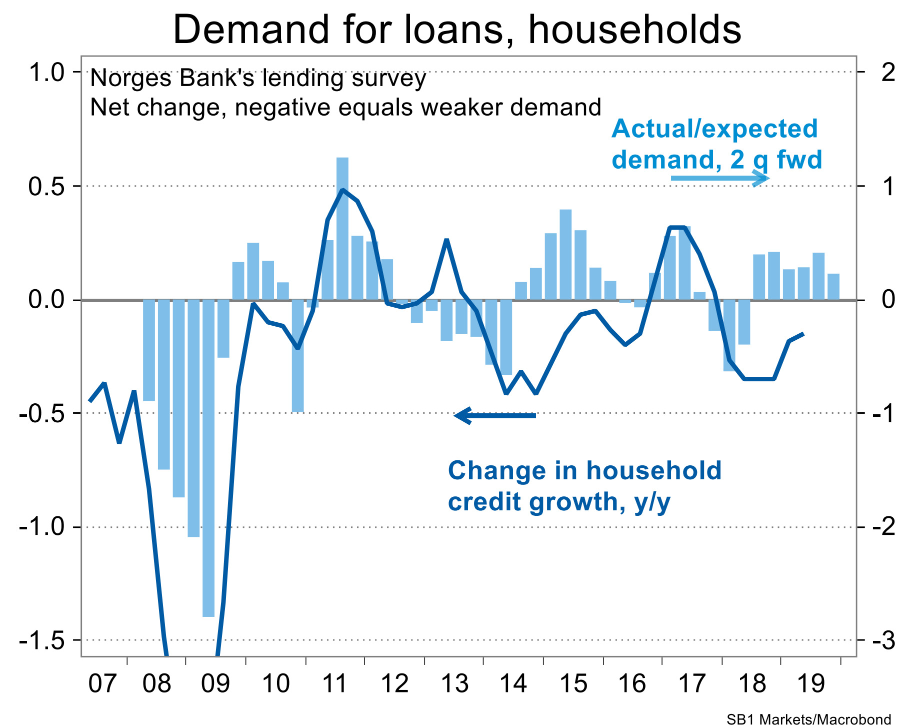
- Households' credit growth slowed to NOK 9 bn in July, from a +/- 15 bn speed the past 6-7 months. The y/y rate edged down to 5.3%, a 0.2 pp decline. The July dip was a change of the timing for the annual conversion of student loans to grants was changed from November to July. According to our calculations, this adjustment explains more or less the entire NOK 6 bn m/m slowdown in July, the 0.2 pp drop in the annual household debt growth rate, as well as the 0.1 pp decline in overall credit growth
  - Household credit growth has been trending slowly down since 2017 but the Sept18/March19 hikes have not lowered credit growth visibly. The jury is still out whether the June hike and most likely a 4th hike in H2 will have any impact on households' demand for credit. Banks lifted mortgage rates by an avg of 18 bps in August, following NoBa's June hike, more than we expected, and rates are up some 45 bps since before NoBa started hiking (in total 75 bps)
- Corporate credit growth (in C2, domestic lending) fell to NOK 4.7 bn, the third month of a visible slowdown. Still, corporate demand for credit has not overall been weakening, the annual rate held steady at 5.8%

SpareBank 1 MARKETS

Household credit growth is slowing, so far at a modest pace (barring July)

Given rising interest rates and a modest rise in house prices, the risks are tilted to the downside

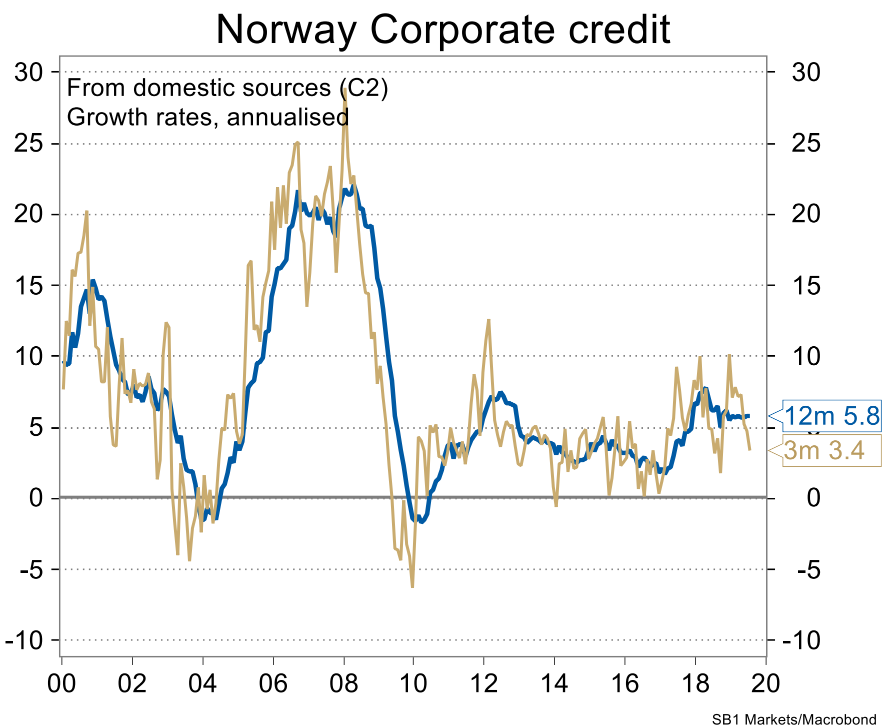


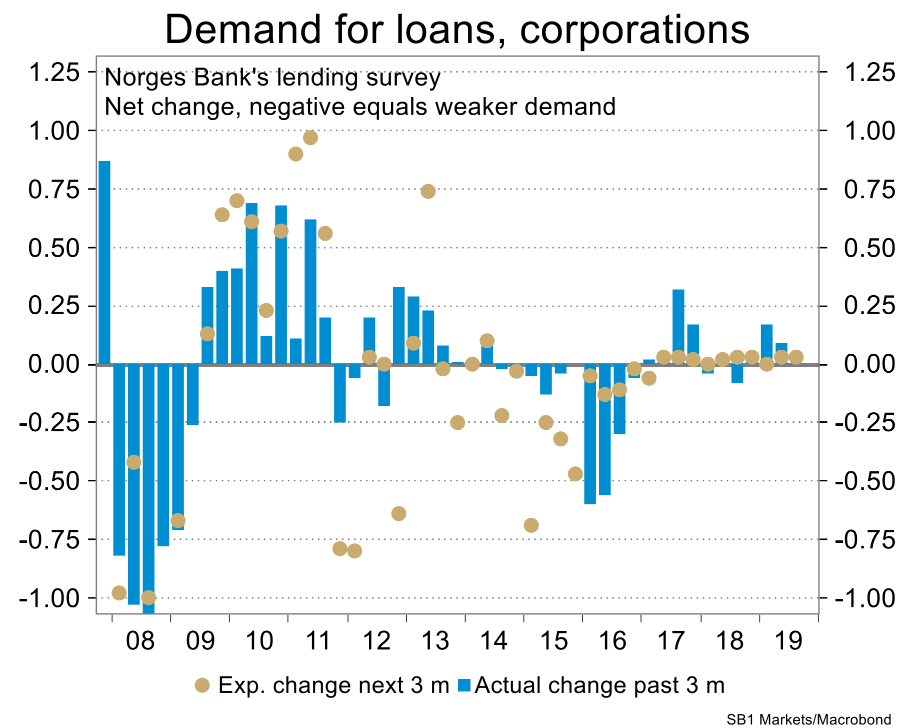


- In the longer term, household credit growth is slowing, from above 7% in 2012-2013 to some 5½% now
  - » Even as household credit is slowly easing, credit growth is still (marginally) above income growth – and the debt/income ratio is still inching upwards, as Norges Bank expects it to do the coming years. Norw. households have the highest debt ratio in the world
- Banks have not reported any downshift in household demand for credit, <u>they even expect a small uplift in Q3</u>
- Higher existing home sales could keep growth up, while higher interest rates and soft house prices may dampen debt

Corporate credit growth quite stable below 6%

Annual rate steady at 5.5-6%, well above the 2013-2017 level (yet far below prior peaks)

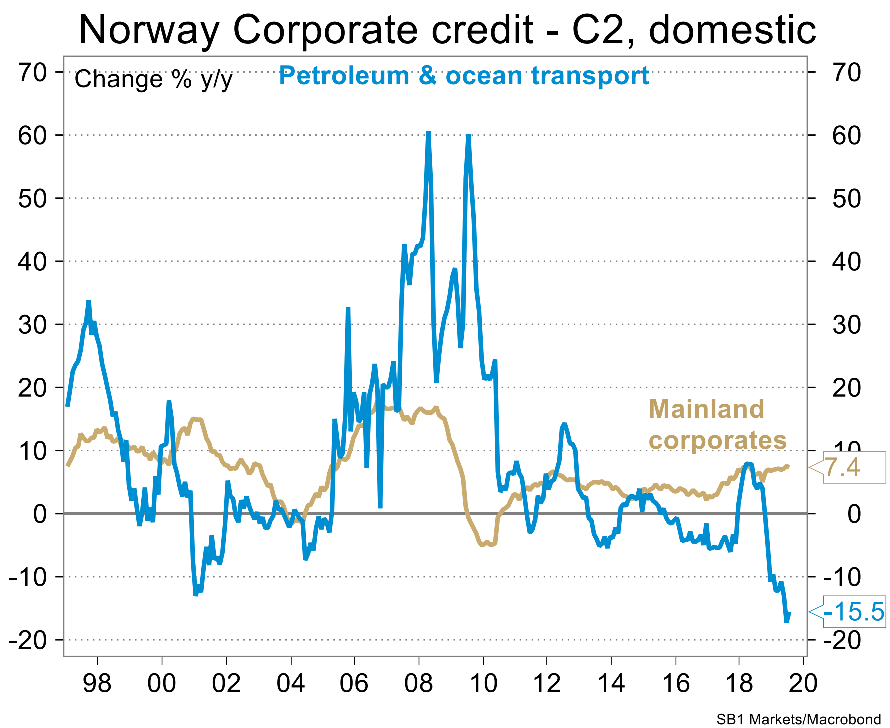


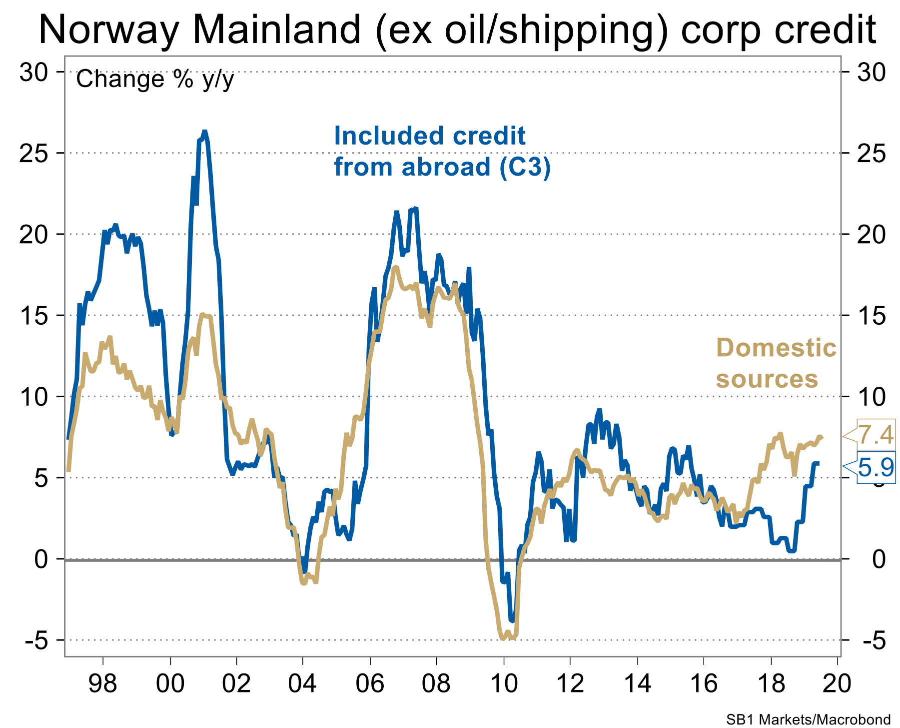


- The underlying growth rate (3m) fell to 4.9% in June, following a strong rebound in early 2019
- The annual rate rose to 5.8%, down from 7-8% growth rates in early 2017. The lift through 2017 might have been 'too rapid', thus, businesses pulled back demand through early 2018. Business investments are still growing

The petroleum sector is still reducing the debt level

.. And non-oil companies are borrowing more, at least at home

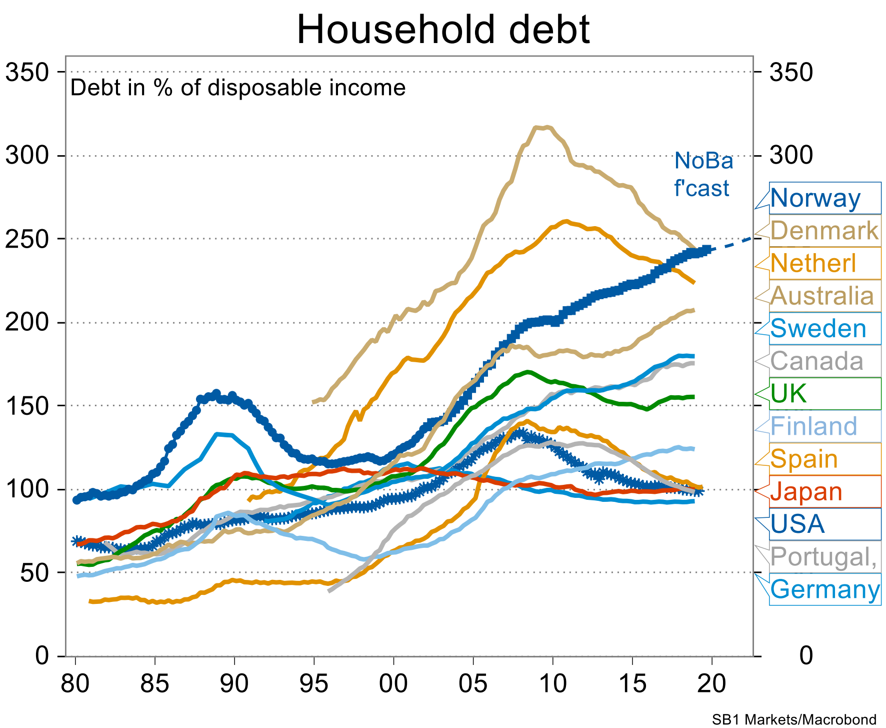


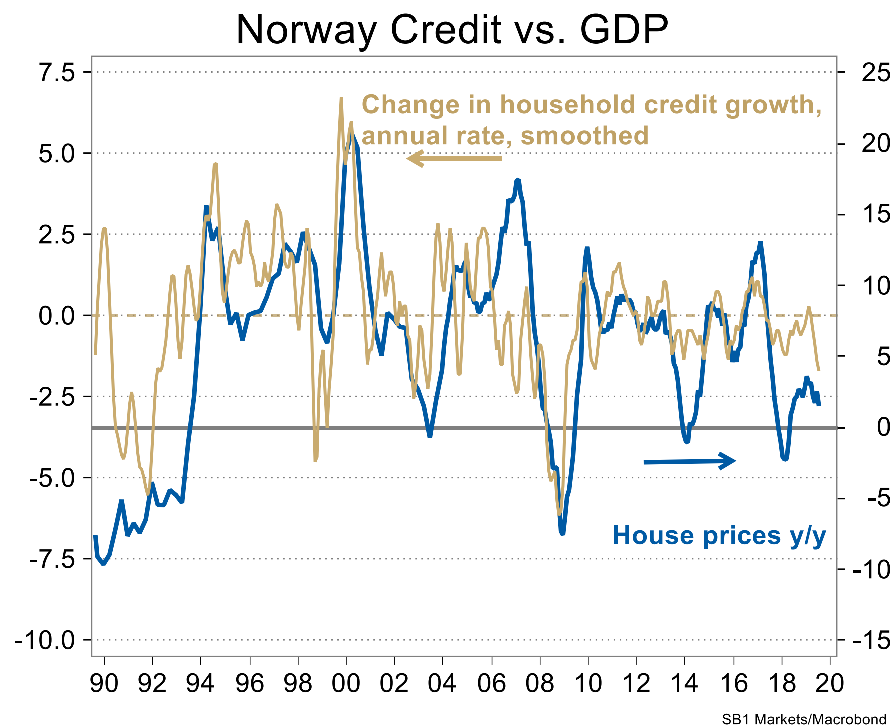


- Credit aggregates are influenced by balance adjustments in international corporations (both Norwegian and foreign owned, operating in Mainland Norway, and then categorized as Mainland corporations).
- The slow growth in Mainland corporate credit growth when borrowing from abroad is included, is probably not a ‘real’ figure but may be influenced by tax adjustments etc

The credit ratio will keep climbing, even with the current interest rate path

The credit ratio rises, Norway in the lead! Shouldn't credit growth outpace income growth forever??





- Household debt is still growing faster than income growth, hence, the debt ratio is increasing
- Norges Bank expects a 5.6% household credit growth rate in 2019. <u>The Bank's estimate implies a further increase in the the debt/income ratio to keep climbing, to almost 250% in 2022,even as the bank is slowly pressing the brake pedal. Stronger brakes are needed to stabilise the credit ratio?</u>
- A slow retreat will be healthy in the long run, but it might hurt short term
- *Changes* in credit growth is usually correlated to economic growth and asset markets – and the housing market. A soft housing market now points to a limited upside on credit growth

Highlights

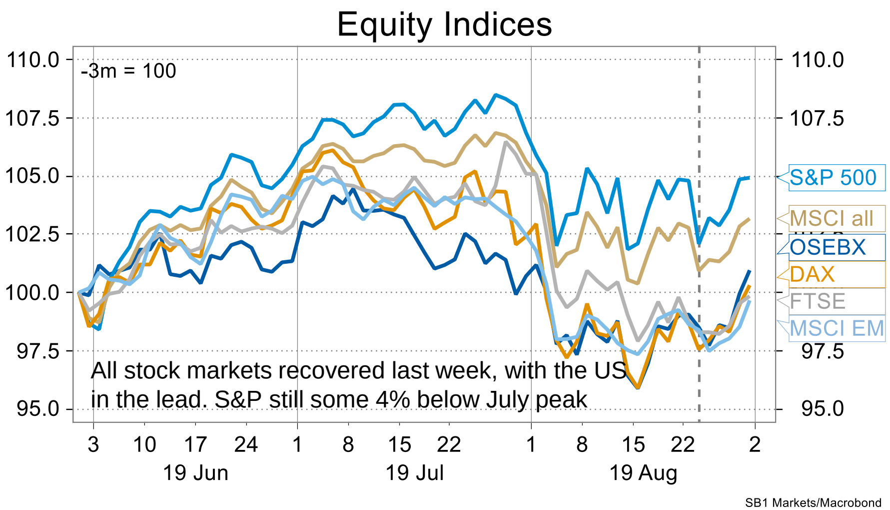
The world around us

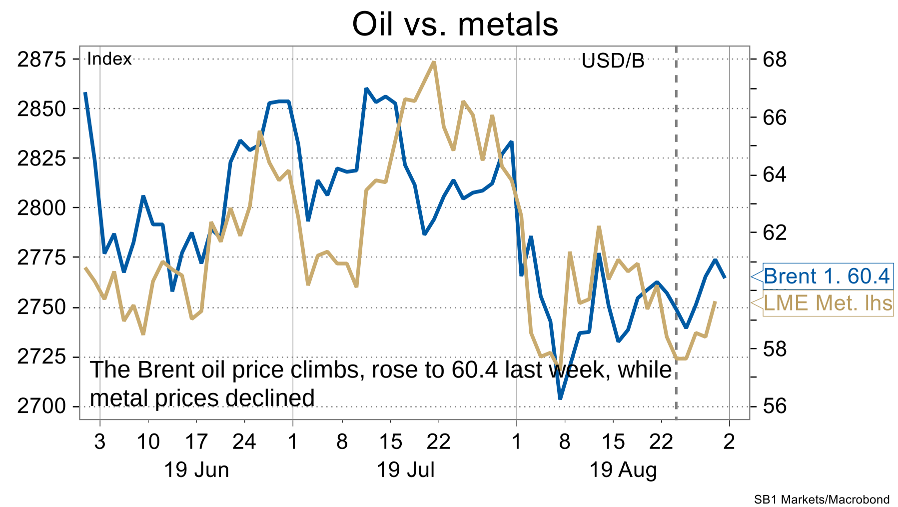
The Norwegian economy

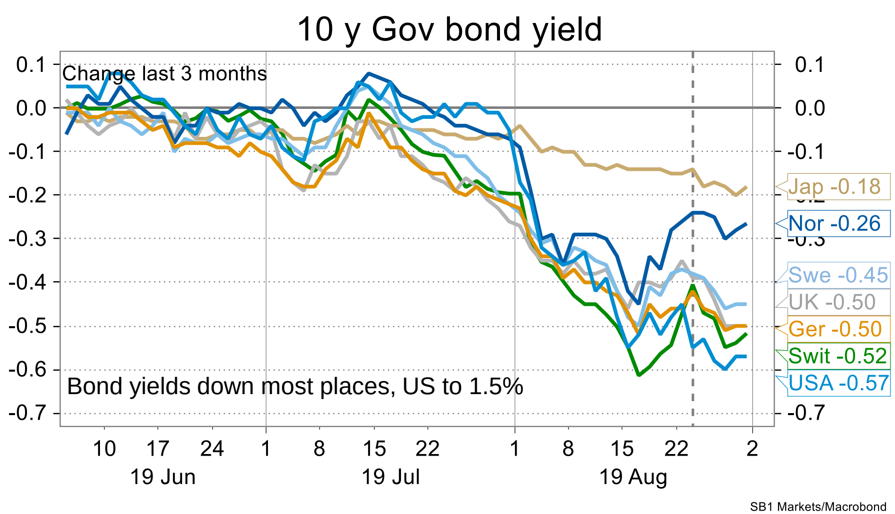
Market charts & comments

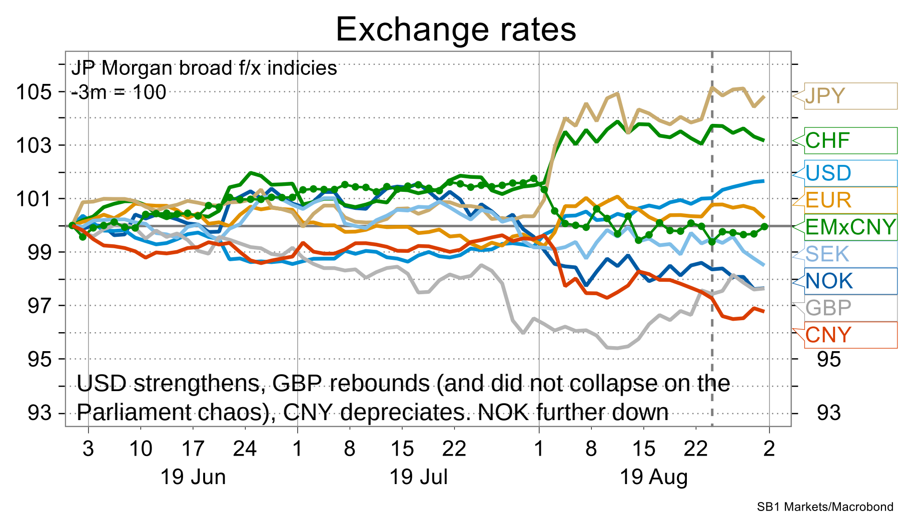
Stock markets recover from the trade war shock, bond yields still heading lower

The trade war triggered risk markets volatility through August. Stocks, oil turned up last week, yields down









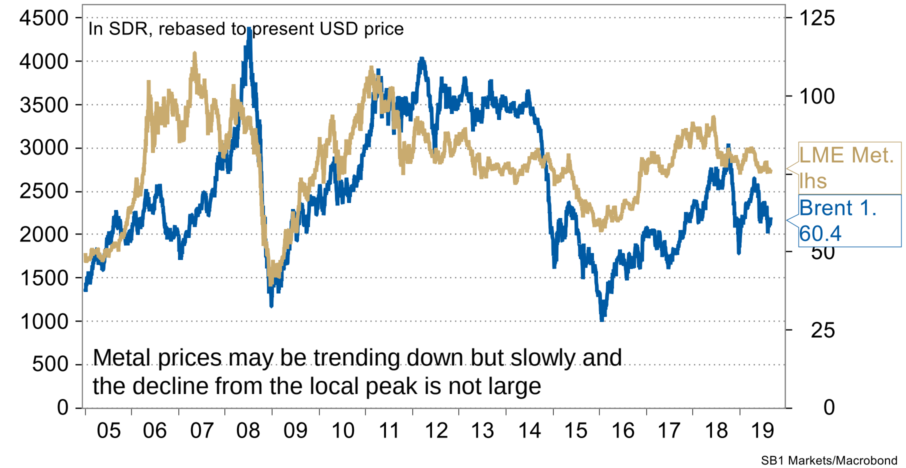
SpareBank 1 MARKETS

German bunds to a new ATL at -0.71%, S&P down some 4% from July peak

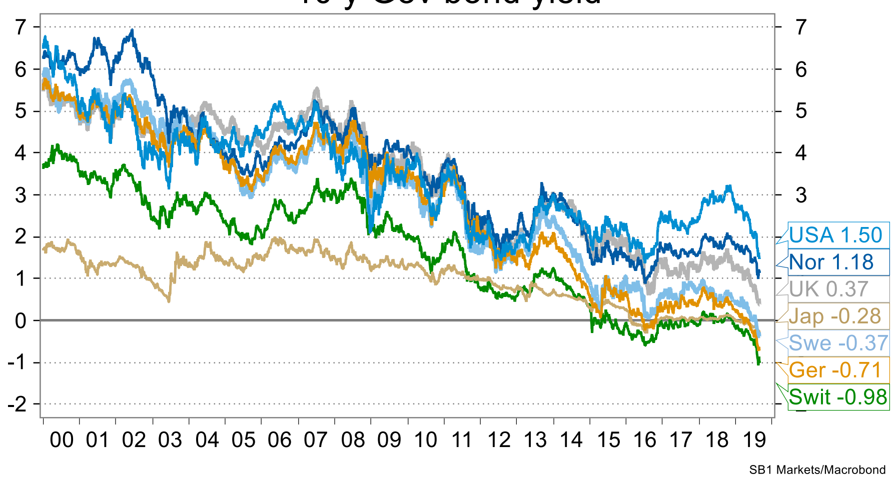
The trade war rules. And then some economic data. Increasing volatility is probably here to stay

Equity Indices

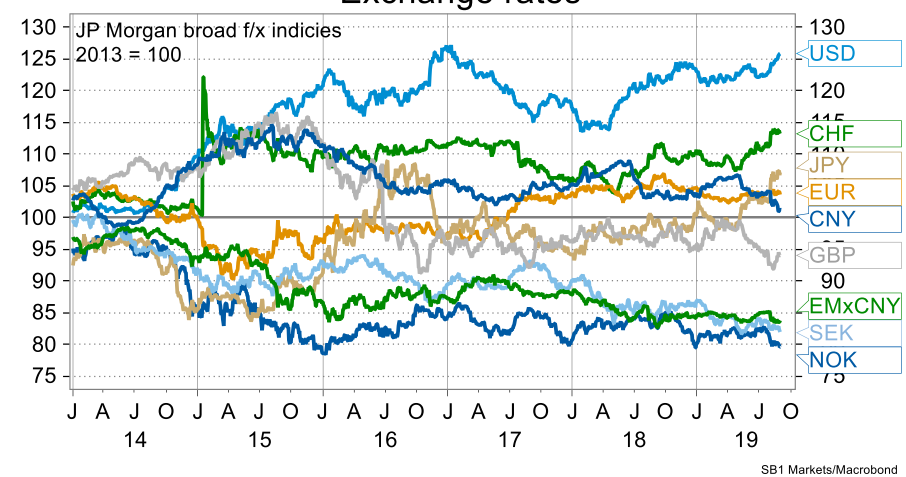
Oil vs. metals



10 y Gov bond yield



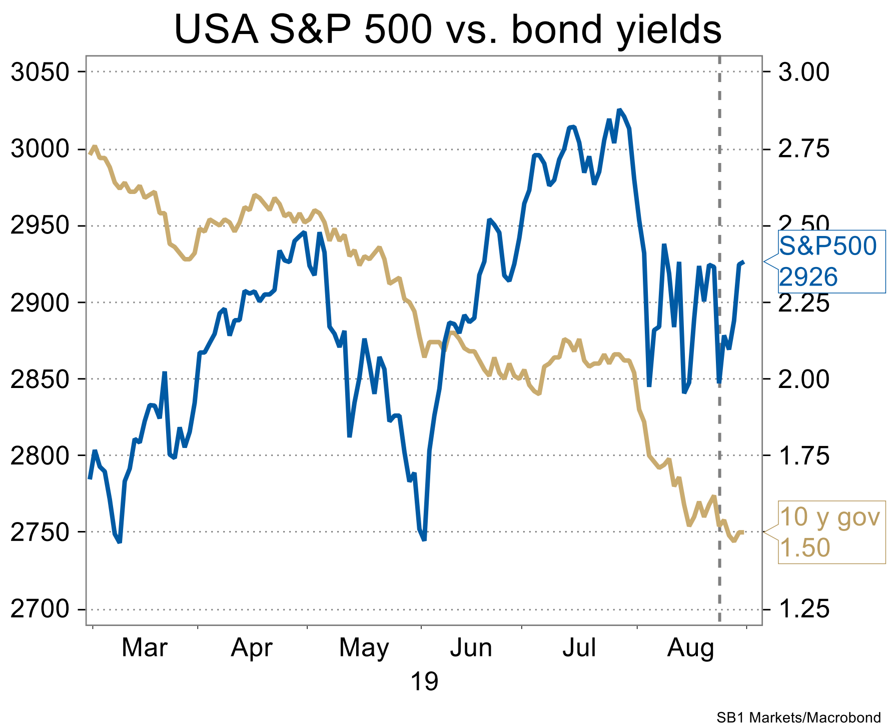
Exchange rates

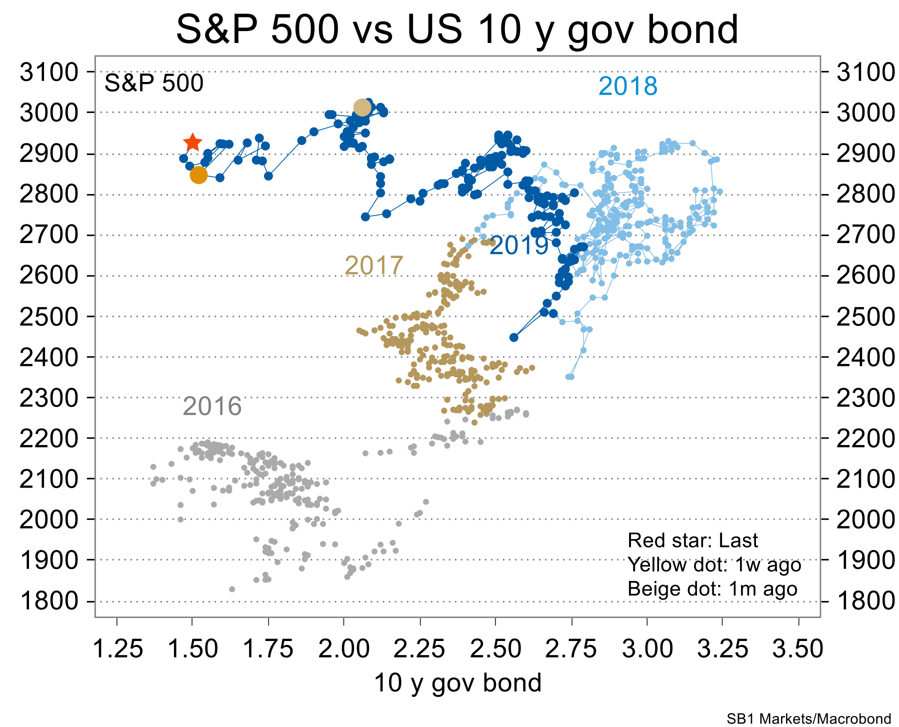


SpareBank 1 MARKETS

US: Stocks recovered mildly, bond yields down the drain

10 y gov at 1.50%, soon at ATL? Stock markets cheered softer trade rhetoric from Trump on China

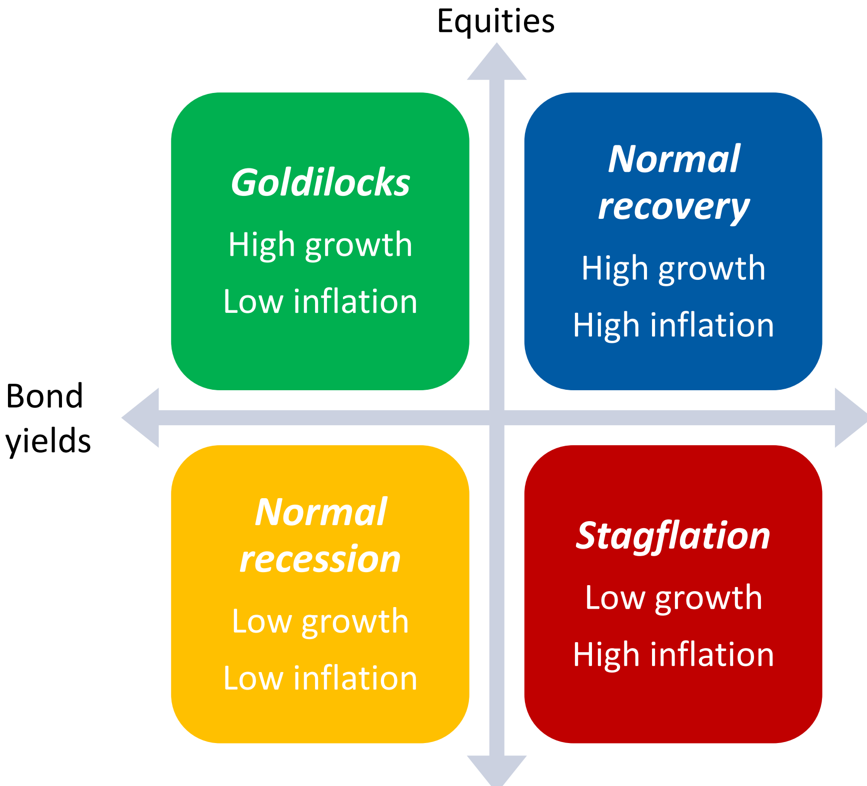


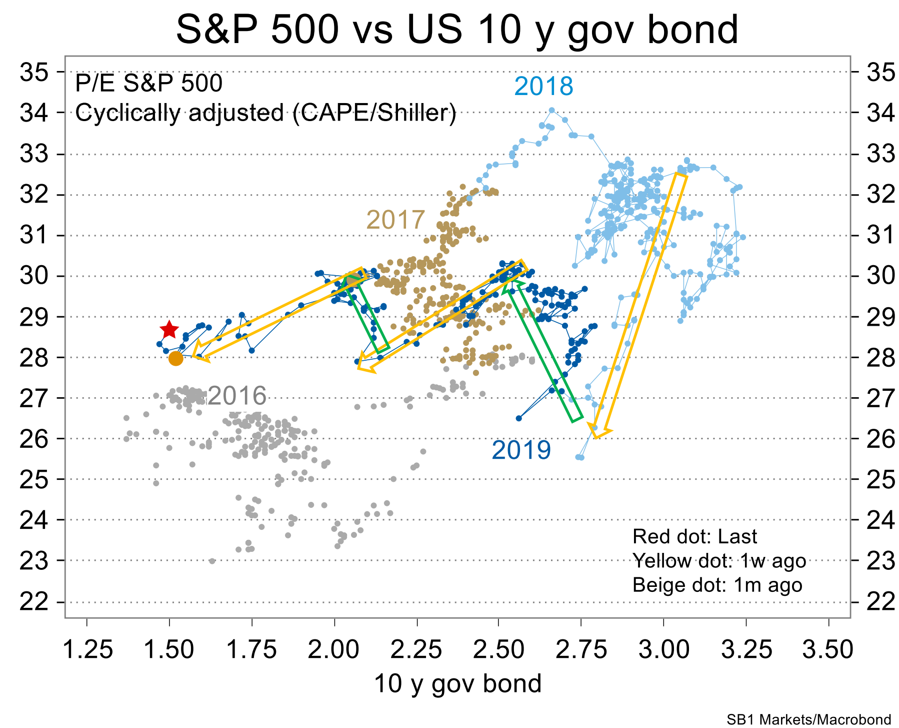


- Stock markets turned up last week, after Trump changed his mind and said he wanted a trade deal with China
- Bond yields fell to 1.47% on Wednesday and stabilized at the end of the week, at 1.50%
- For more on the relation between stocks and bonds, check next page

US markets have been moving towards the recession corner

Normally, markets move in either the 'normal' recession or recovery corner. Last week: Goldilocks?

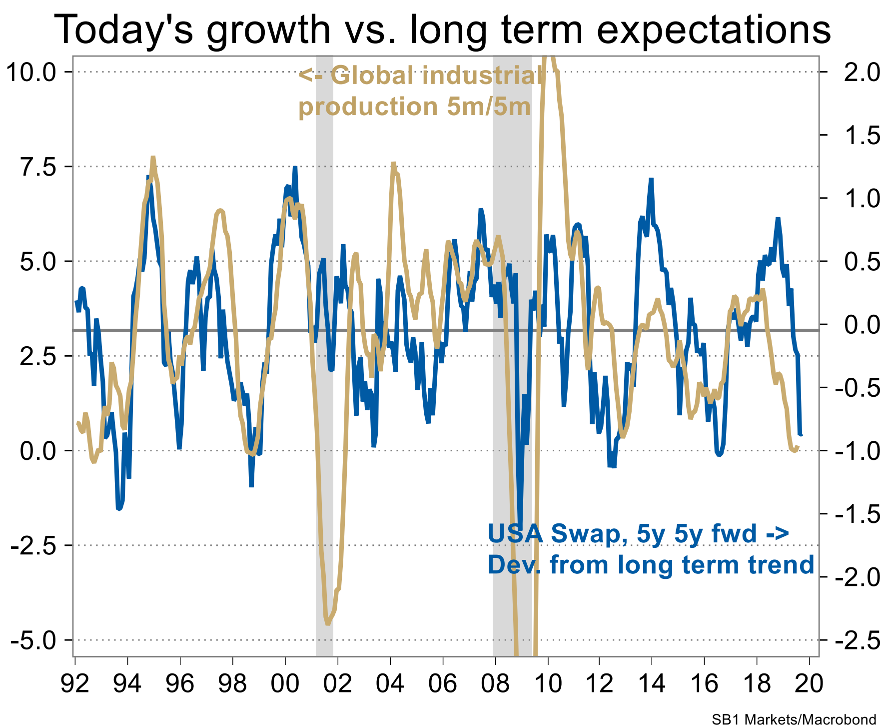




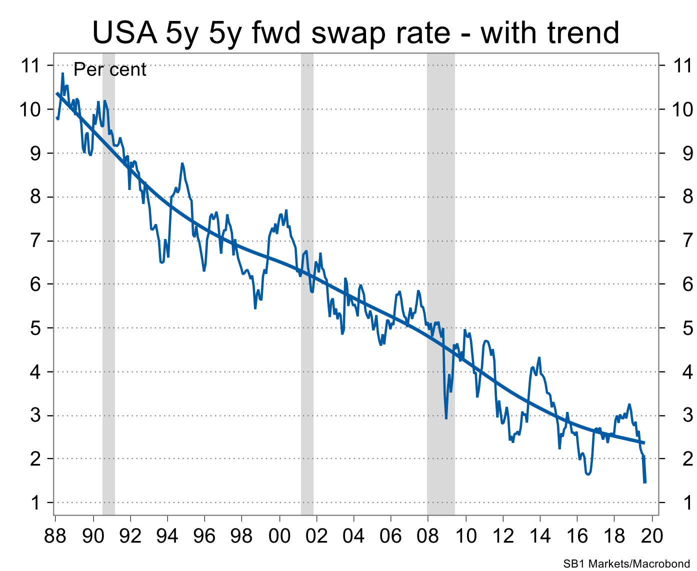
- During May, both stocks and bond yields fell sharply, towards the 'normal recession' (yellow) corner. The 'yielding' signals from the Fed (and other central banks) during June then pushed bond yields further down, and stock markets up – in the Goldilocks direction. In July, the market fluctuated mostly along the normal recession/normal recovery axis.
- So far in August, markets have moved towards the recession corner following the bad trade policy news. Last week the stock market rose margially, while bond yields also declined (marginally) – in the Goldilocks direction
- We still do not think a long term Goldilocks scenario is likely. If yields decline substantially form here, it will be due to really weak economic news, which will not be good news for the equity markets. We are not that worried for the 'Stagflation' corner either; a take off in inflation will happen only if central banks make serious policy mistakes, over time. Trump wants the Fed to do just that but we doubt he will succeed. So, the normal recession/recovery axis is the most likely – and now we are heading towards the recession corner

Long term interest rates are driven by the short term business cycle

… just like the short term cycle is driving most long term expectations…



- USD 5y 5y swap is down more than 150 bps since last autumn
- This is the normal decline if the business cycle slows, like we have seen since last autumn, as growth in global manufacturing production has slowed to zero, from 4%
  - » The global manufacturing PMI and other surveys are signalling a marginal a small decline in production but not by much
- Sure, interest rates may decline further short term but the bet is not 'obvious' anymore, given the 'normal' decline recent monhts

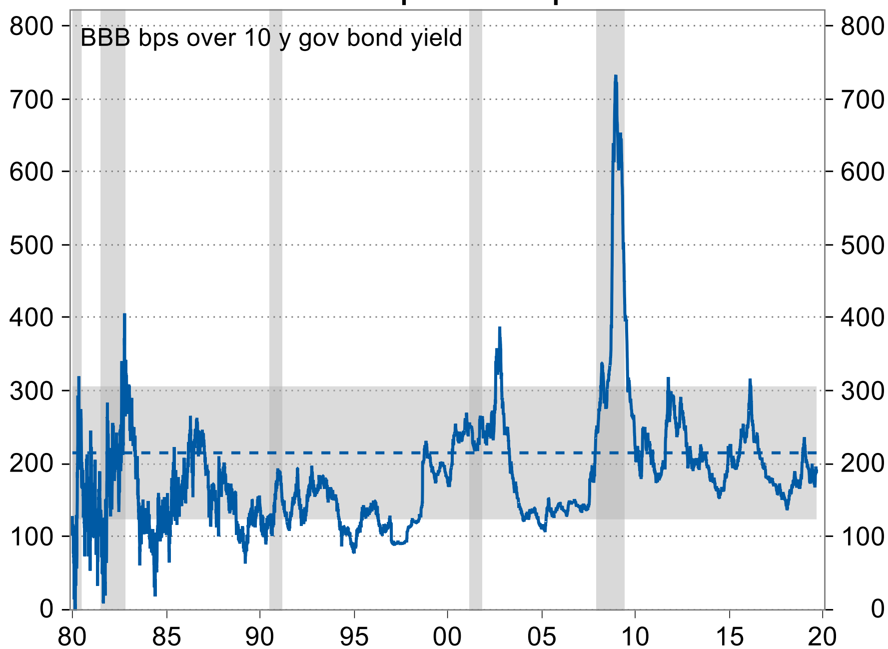


- We decompose the past 20 y USD 5y 5y in two components, the long term trend (approx -0.4 pp per year), and a short term cyclical component
- The cyclical component (the difference between the actual obs. and the trend on the chart to the right) is compared withe the short term business cycle at the chart above. There are some similarities… The biggest miss: Long term rates fell less than they 'should' during the 2001 recession – and long term rates were 'too stable' during the financial crisis vs the huge down/upturn in the global manufacturing cycle

Credit spreads are ‘too’ low given the current ISM level

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

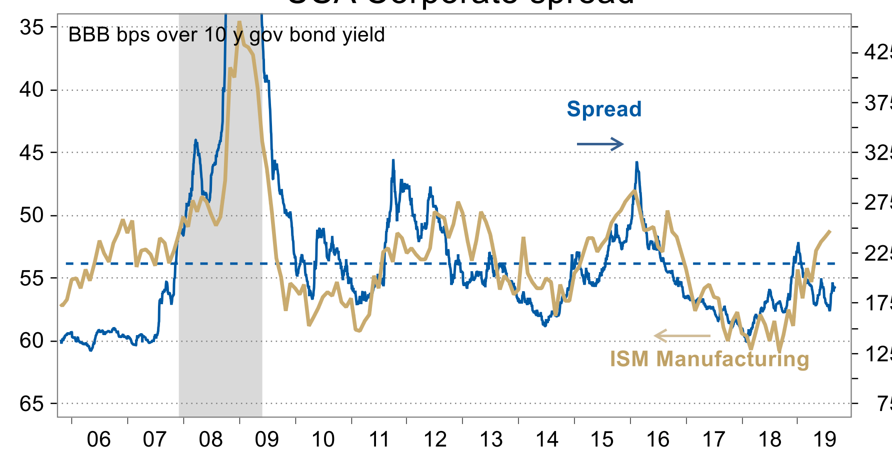
USA Corporate spread



SB1 Markets/Macrobond

SB1 Markets/Macrobond

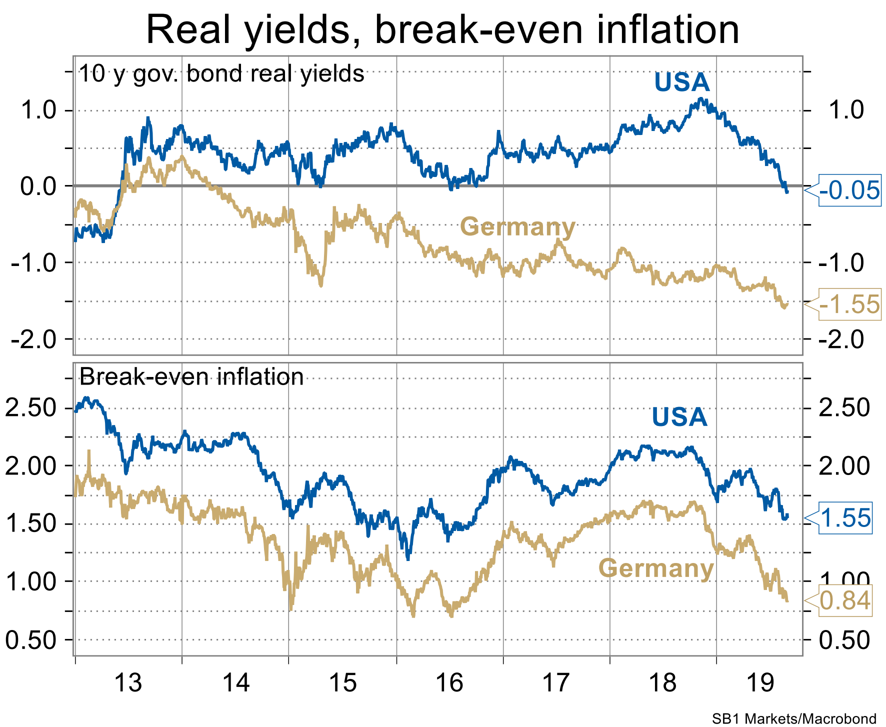
USA Corporate spread

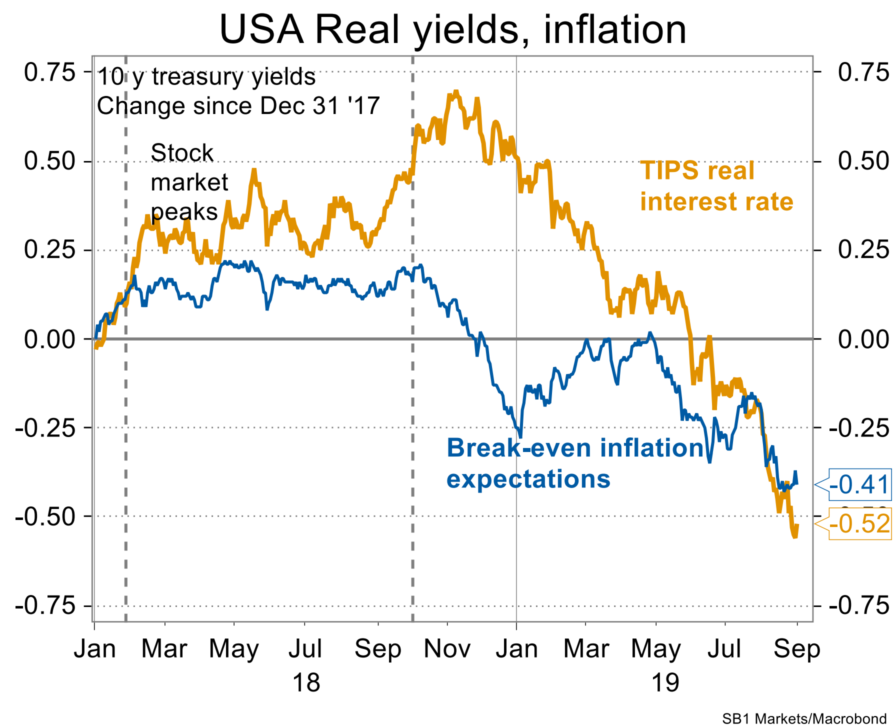


SB1 Markets/Macrobond

US real rates tumble, inflation expectations stabilized

US real rates fell to -0.05% last week, lowest since ‘13. German real rates steady, inflation exp. drops

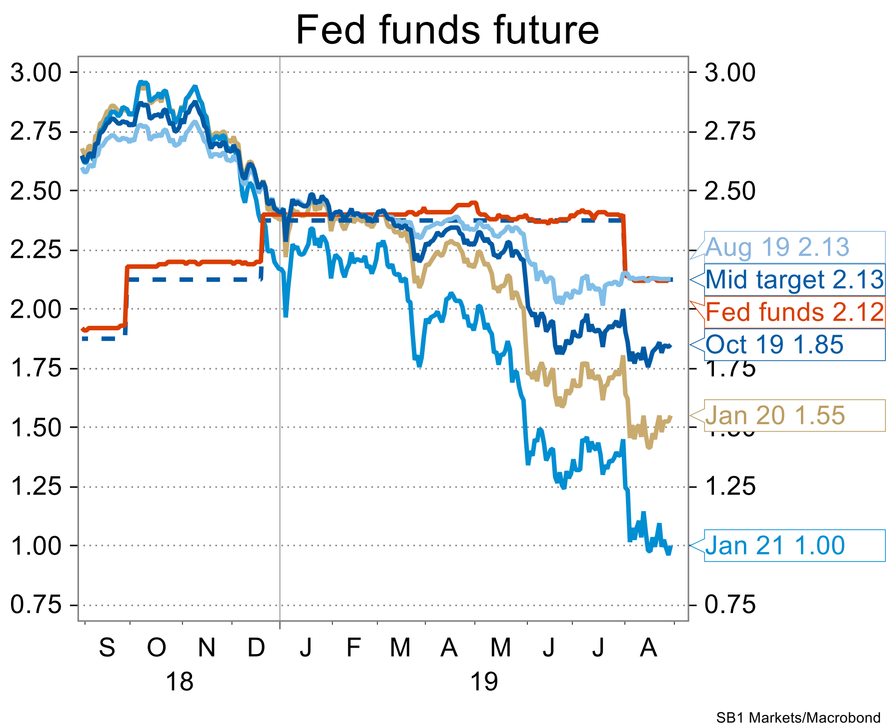


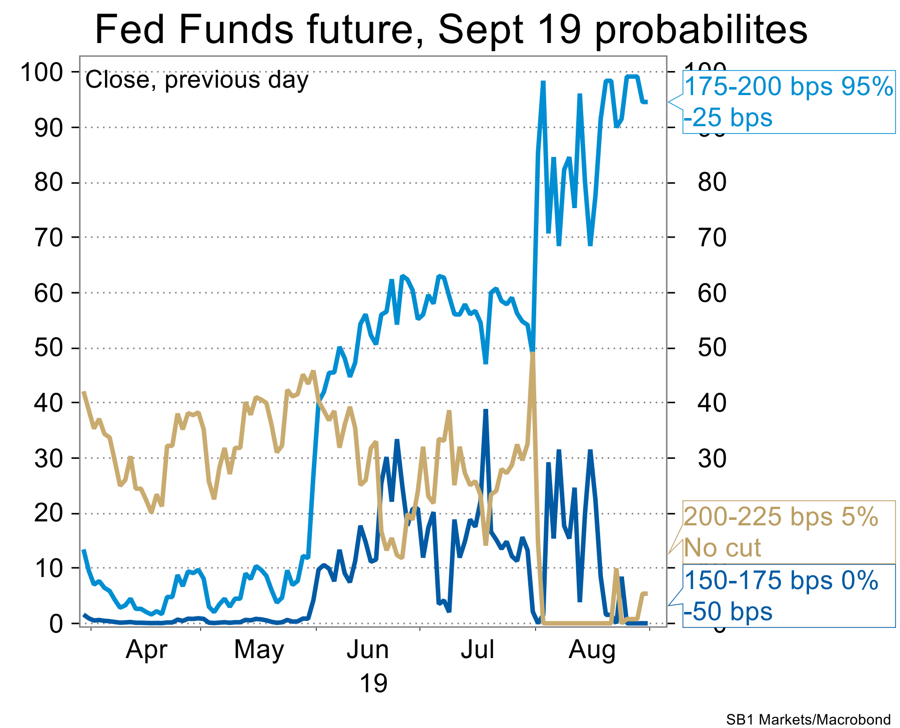


- Both real rates and break even inflation have been sliding sharply down in both countries
- German real rates record low, at -1.55% last week
- Inflation expectations stabilised at some 1.59% in the US, fell to 0.84% in Germany

Fed fund futures edge up, 'everybody' is expecting a 25 bps cut in Sept

A Sept cut is fully priced, the probability of 50 bps cut has fallen to 5%, from 30%

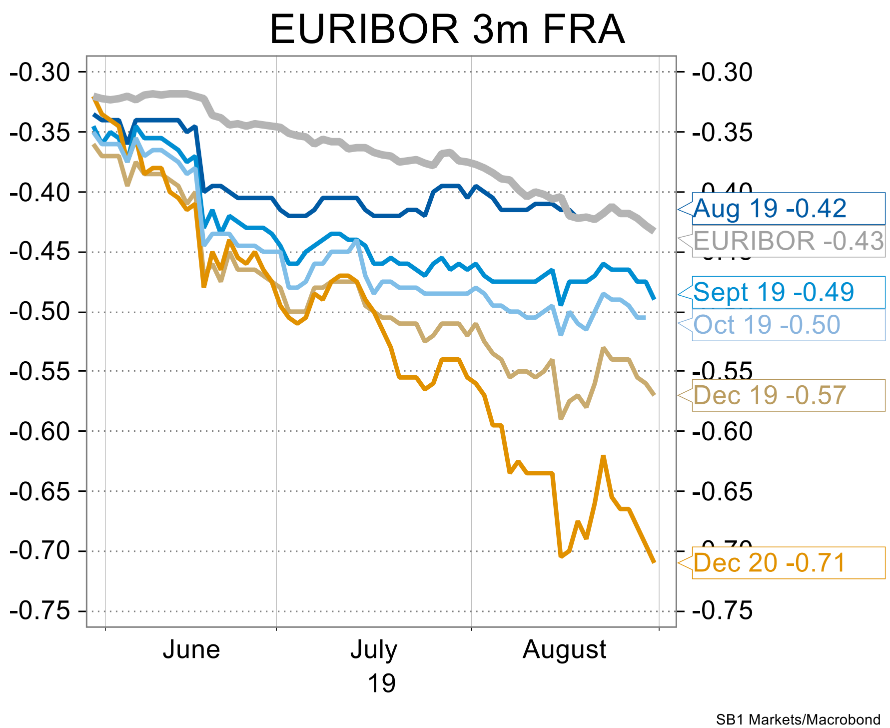


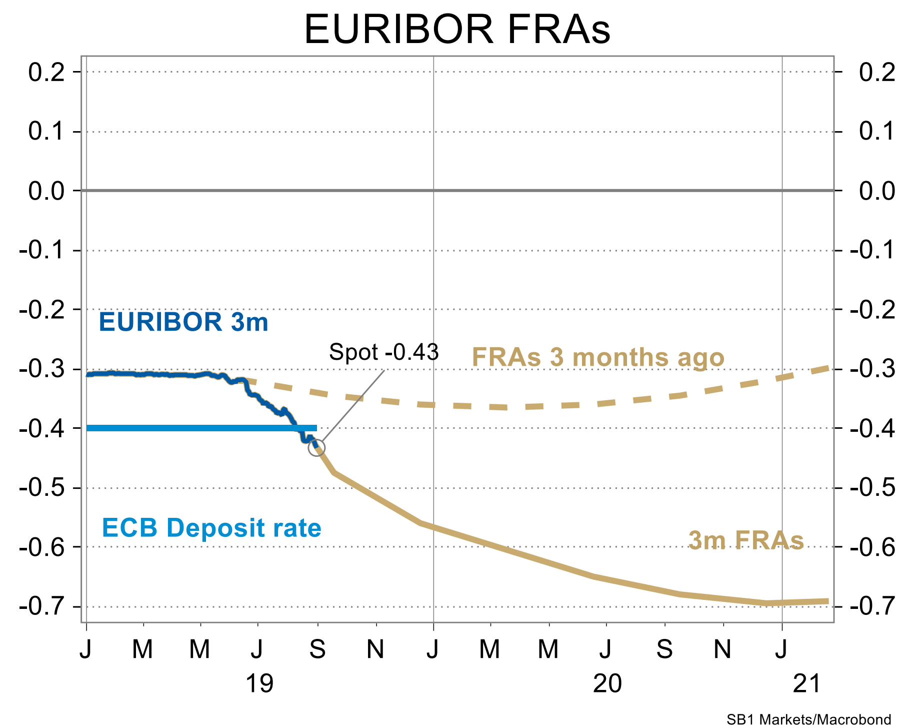


- The trade war escalation and growth concerns, triggered by the yields curve inversion, have taken the Fed fund futures steeply down. The past two weeks, the shorter FRAs have been rebounding, the Oct '19 contract is 9 bps above the bottom
- The probability of a 50 bps cut is zero, and 5% for no cut. Market is pricing in 2 cuts before Jan and 4-5 cuts by the end of 2020
- US growth is slowing but it is still above or at trend. Inflation is not far below the target. Yes, there are clouds at the horizon but is still not raining. The USD is stronger than normal but not by that much. The economy is not justifying another interest rate cut in Sept, but another 'precautionary' 25 bps cut is very likely to be delivered, as Powell indicated at Jackson Hole

The EUR curve further down, signals some belief in a 20 bps cut again

The market is pricing some 60% prob. of a 10 bps cut in Sept and 40% for 20 bps (from 0 last week)



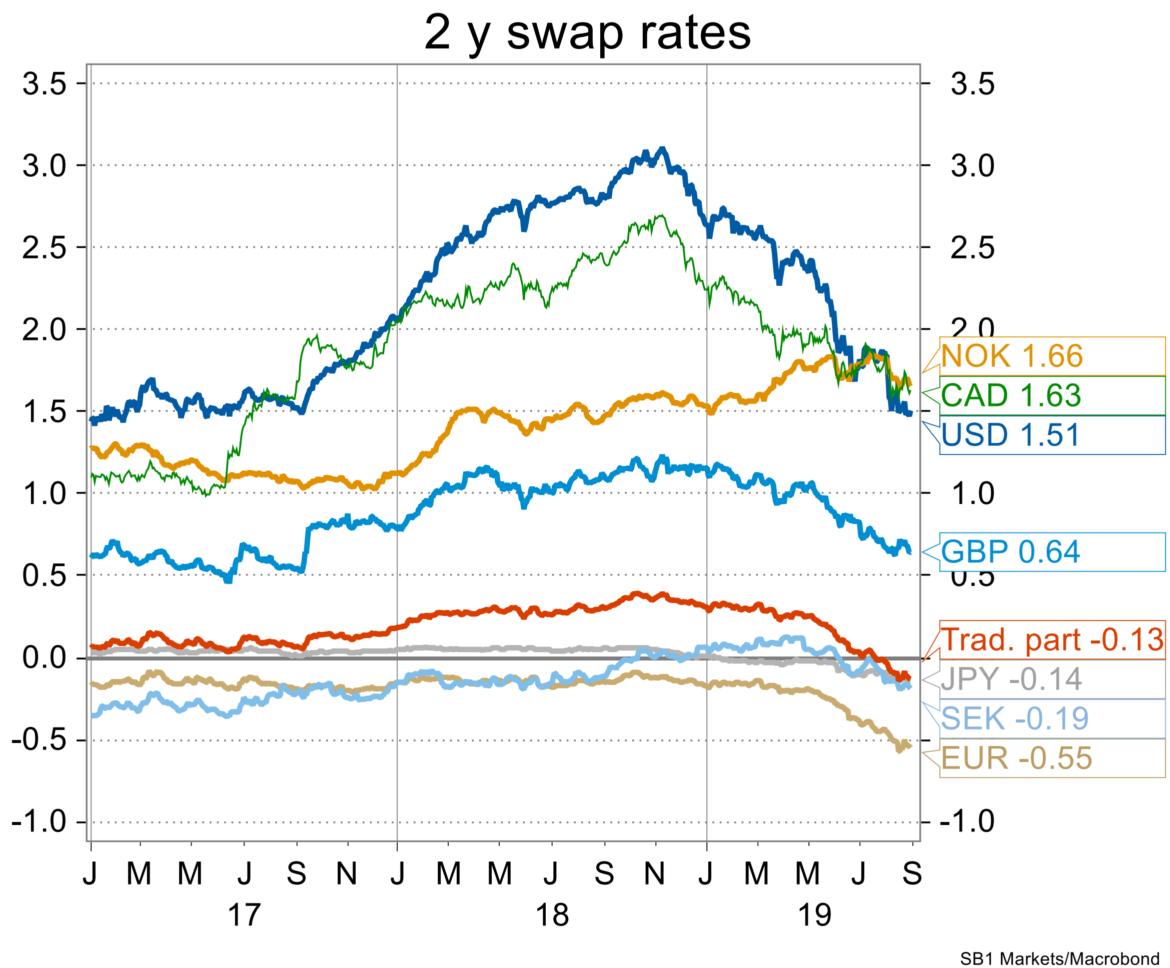


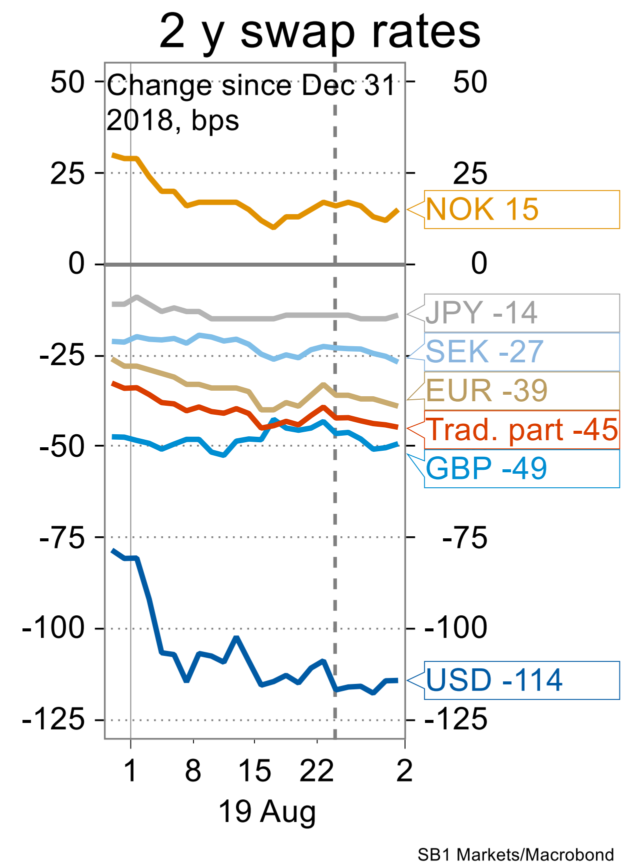
- In July, the ECB hinted of a more accommodative monetary policy, if the economic/inflation outlook did not strengthen. A board member Olli Rehn said in Aug that bank was prepared to cut rates and introduce aggressive QE measures
  - The German finance minister suggested that massive fiscal stimulus will be imposed, if necessary (50 billion EUR, he said) More debates on fiscal policy other places too – reducing the need for aggressive monetary stimulus?
- The market is pricing 60% probability for a 25 cut at the September meeting, and the probability of 20 bps increased to 40% last week (from zero the prior week). No one is expecting an unchanged rate. More QE will be announced too
- Unlike in the US, a more expansive monetary stance can be justified by weak data and muted inflation

SpareBank 1 MARKETS

Short term rates mostly down last week, NOK rate still elevated vs others

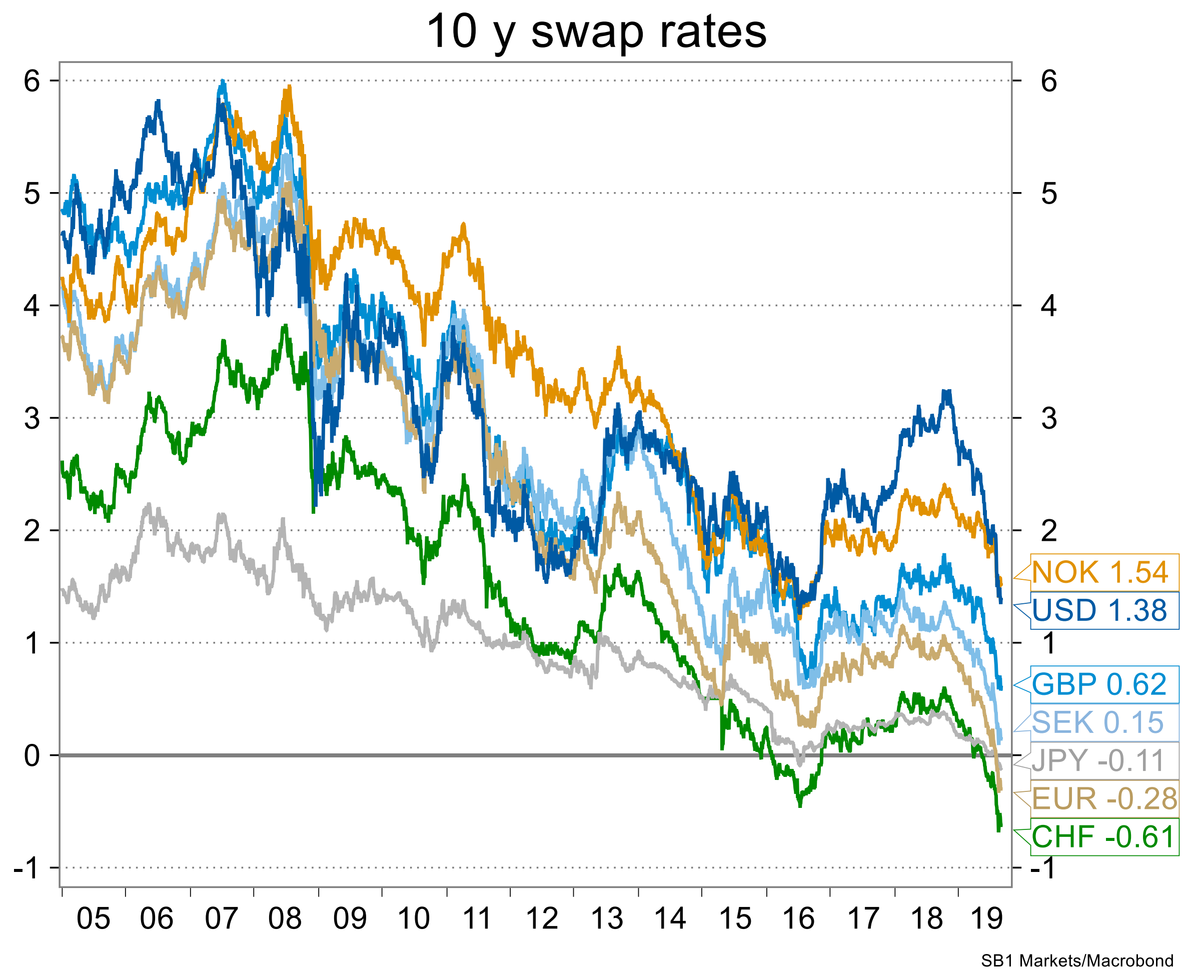
Short term rates everywhere have followed the US down after the trade war escalation on Aug 1

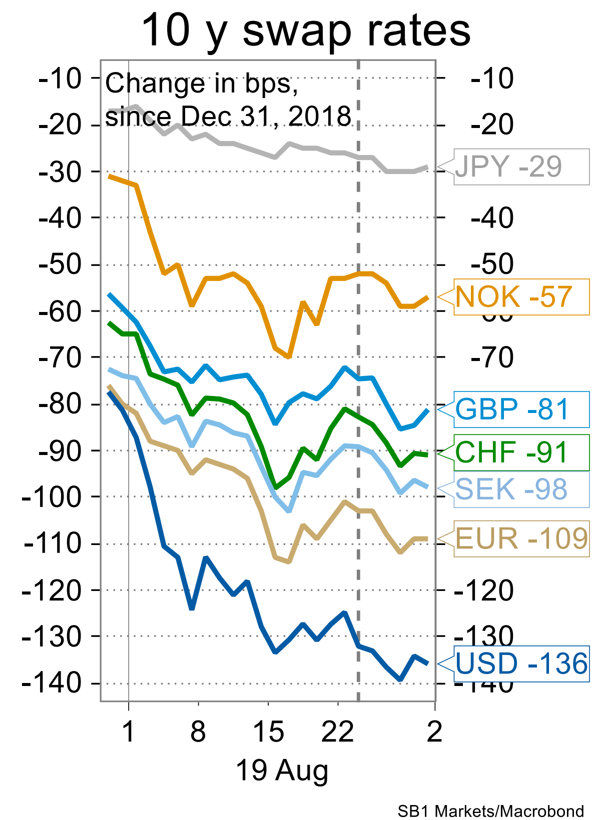




Long term swap down last week too, in spite of some ‘risk on’

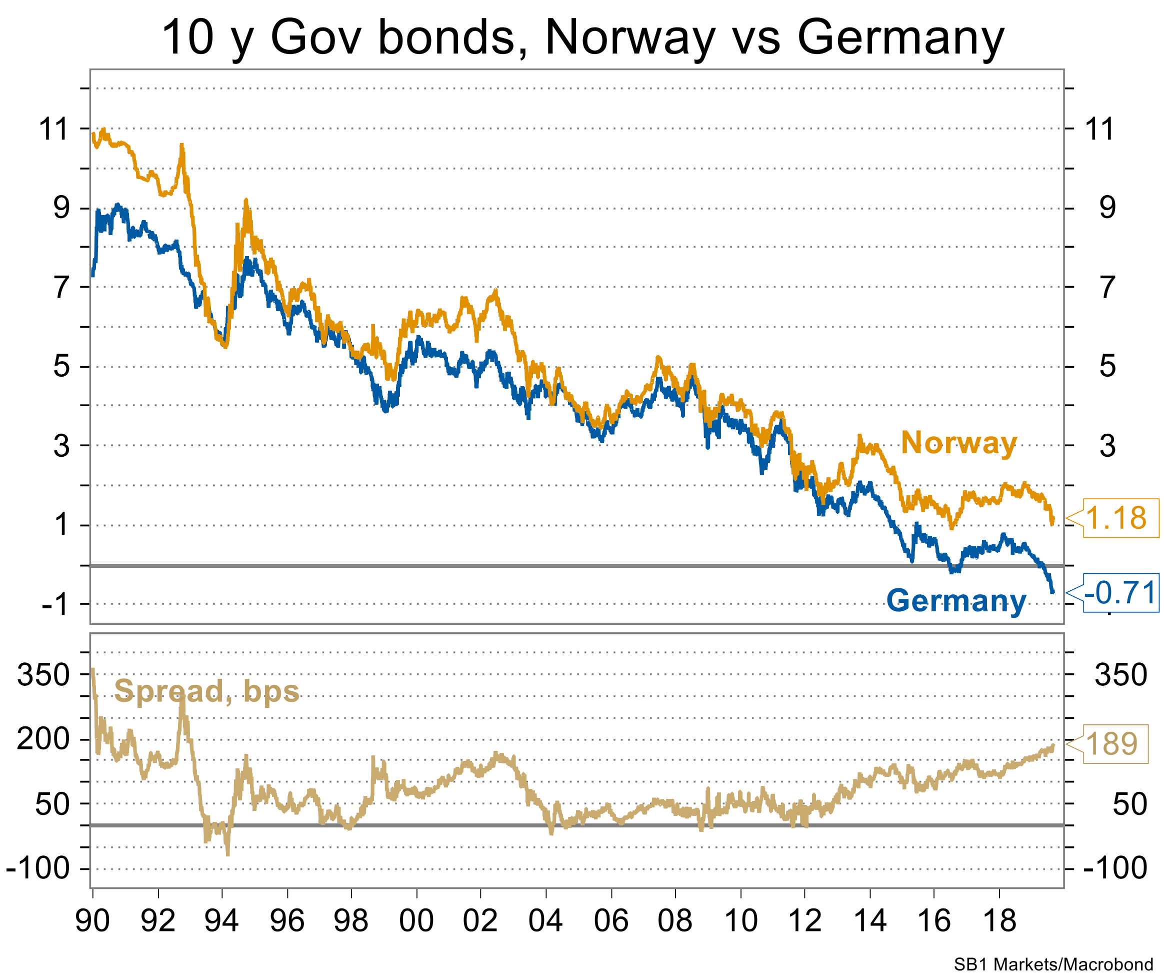
10 y swap rates at ATLs in the EMU, UK, Sweden, Japan – and soon in the US and Norway?

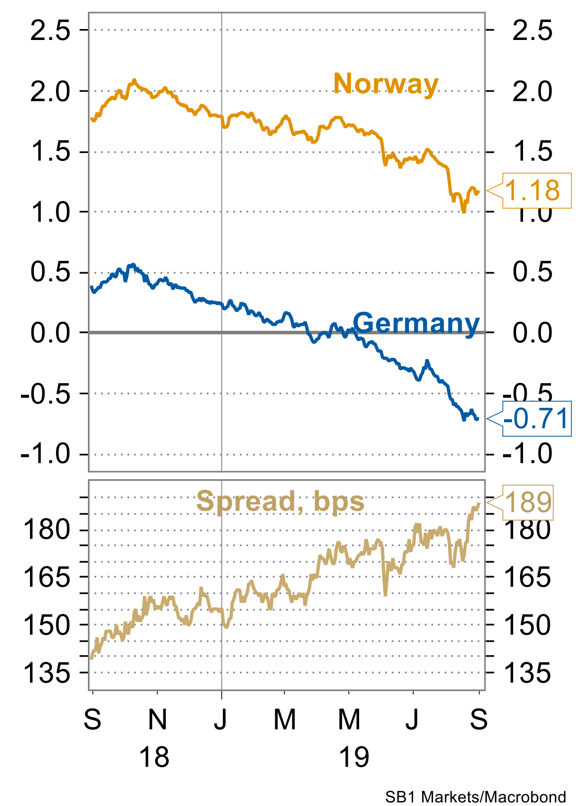




NOK 10 y gov has recovered more than German bund, highest spread since '93!

NO 10 y gov up 16 bps the past two weeks, German bund up 2 bps (but it fell 8 bps last week)





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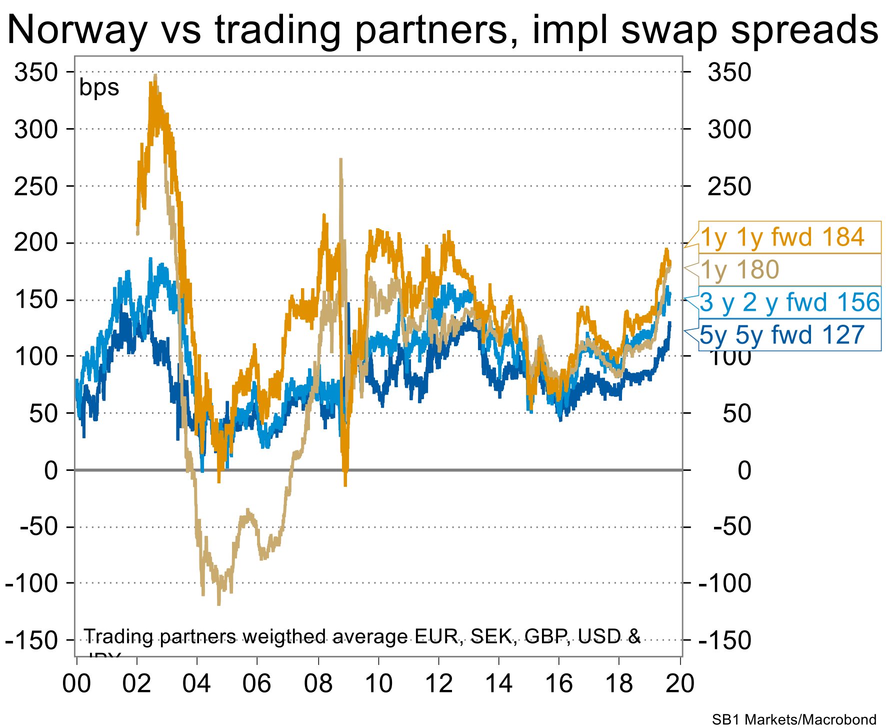
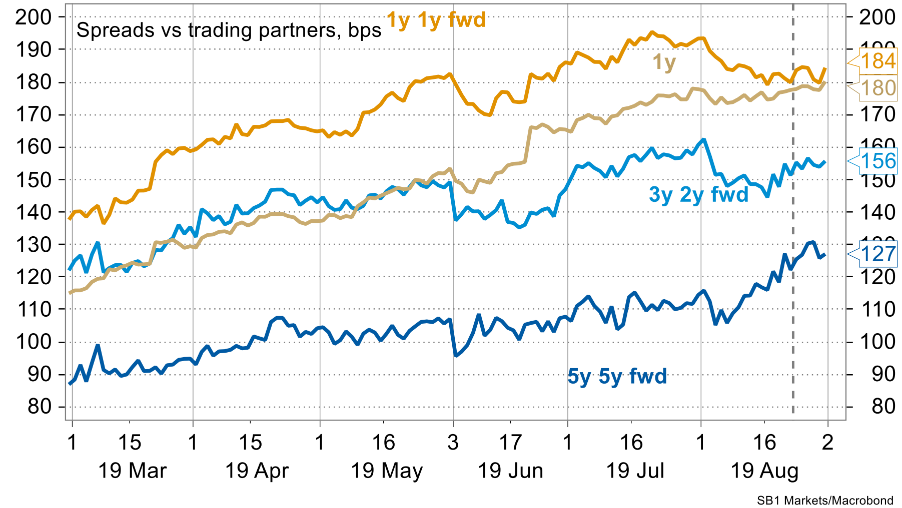
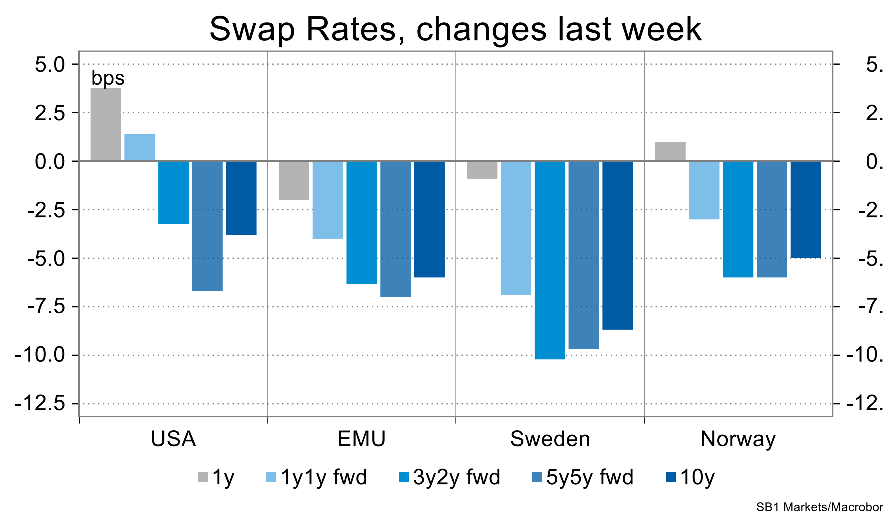
Spreads vs trading partners narrow in the short end, widens in the long end

The spread has widened steeply in the long end of the curve, strange (and it is too high, long term!)







- Swap spreads between NOK rates and our trading partners narrowed in the short term through late July and the first half of August. Spreads have flattened out the past two weeks
- 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, which rose further last week. It must be 'too' high?

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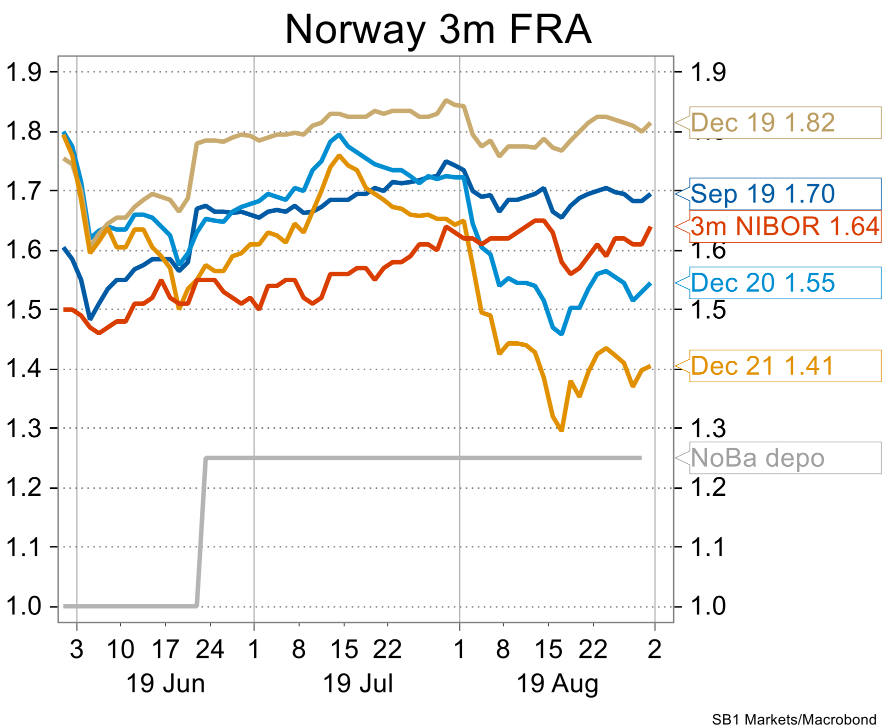
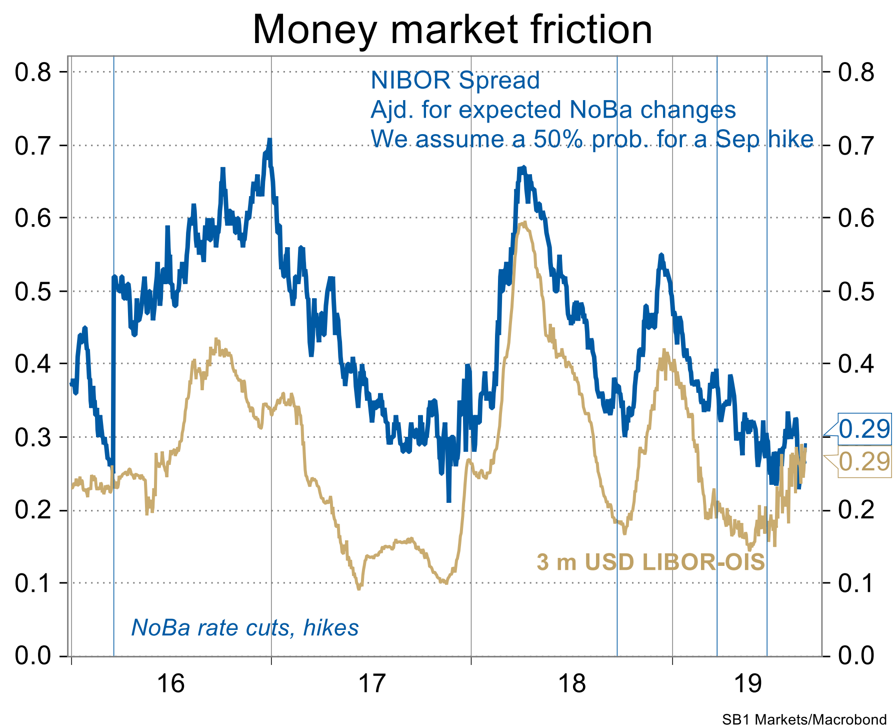
FRAs flat to marg. Up last week, the Sept FRA implies some 30-50% for a hike

Strange movements in the 3m NIBOR vs the Sept contract recently, liquidity effects?

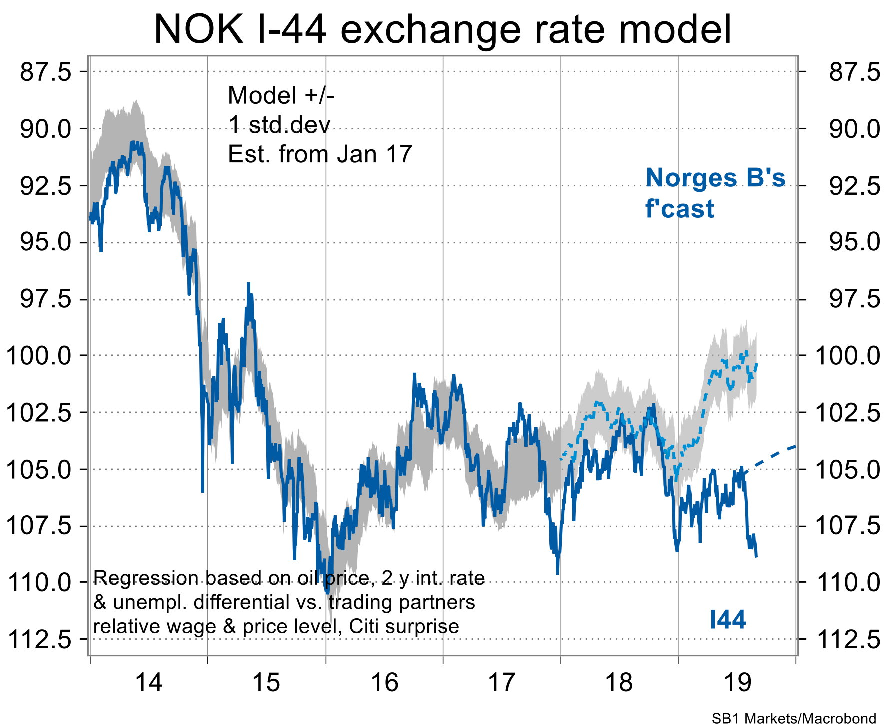


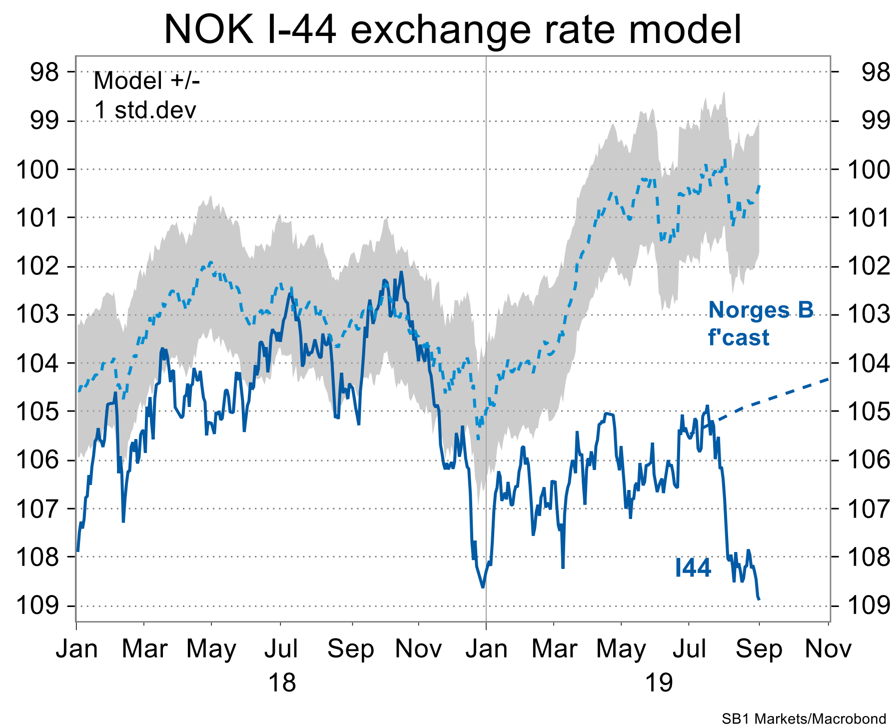


- We have been waiting for the difference between the 3m NIBOR, and the SEP 3m FRA contract to narrow as the differential has been far too high for two weeks (implying a very low NIBOR before Sept 19 and a high rate thereafter, more than a 100% probability for a NoBa sept hike could explain). The 6 bps gap is still elevated, one of them will have to yield soon (and we assume the 3m NIBOR)
- The Sept 3 m FRA at 1.70% implies a 30% - 50% probability of a NoBa hike in September depending on the NIBOR spread assumption. The LIBOR-OIS spread has widened recently, signalling a higher NIBOR spread too. However, a 3m NIBOR, stretching more than 2 months into the Sept FRA, signals a much lower spread
  - » The market is pricing a hike by the end of the year by more than 80% (depending on the spread expectation). From Dec 19 and onwards, the curve is inverted. The market expects a Norges Bank cut in 2020. In June, NoBa planned (almost) one more hike in '20

NOK is plummeting, -0.6% last week. More than 8% gap to our old f/x model

The model said +0.4%. NOK is unusually weak vs the model or other 'supercycles' too





- It did not help that the oil price rose, and that the interest rate spread climbed again; the NOK index is at the lowest since Dec 2017 – and not that far from All Time Low
- Even our super-cycle f/x model has not explained the NOK weakness since late July, although both AUD and SEK fell with the NOK last week
  - We have tested our models with global risk etc., without success
- Long term, we stick to our long term **buy NOK** recommendation

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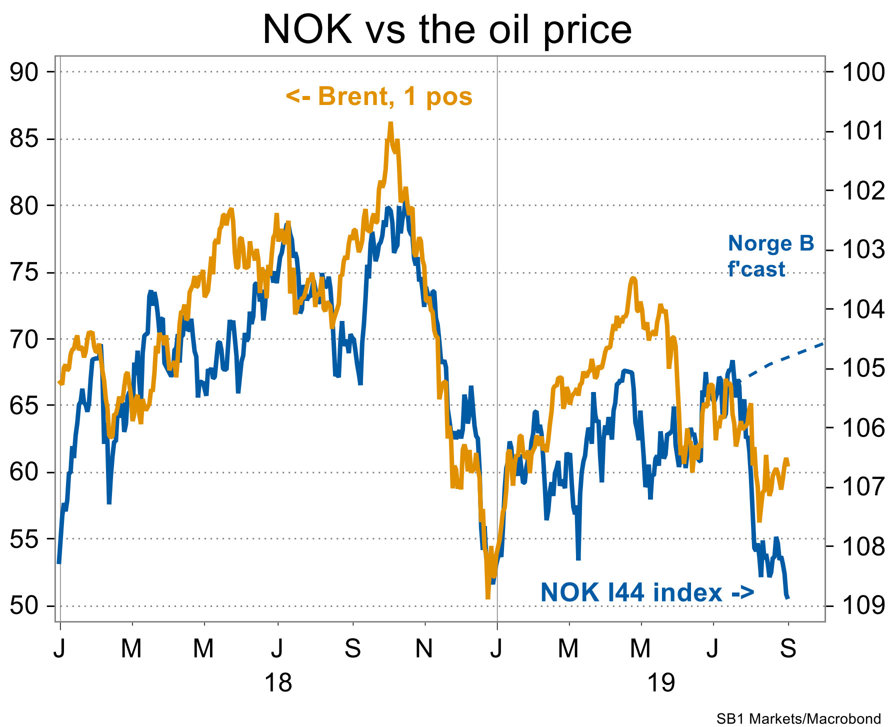
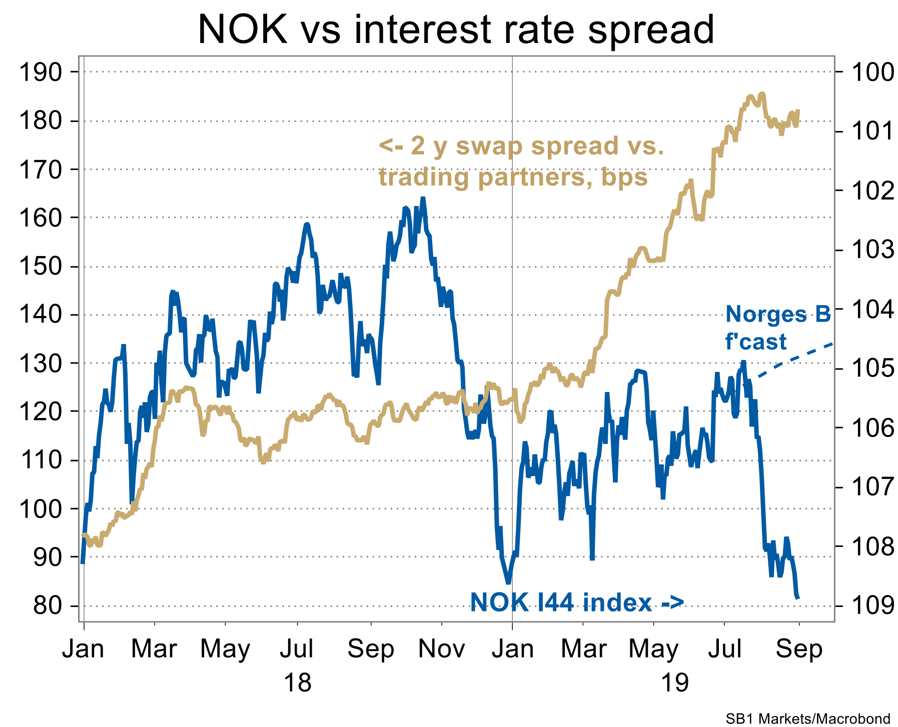
The NOK is weak vs. oil & the interest rate spread

The oil price rose, and the interest rate spread vs trading partners increased; the NOK weakened





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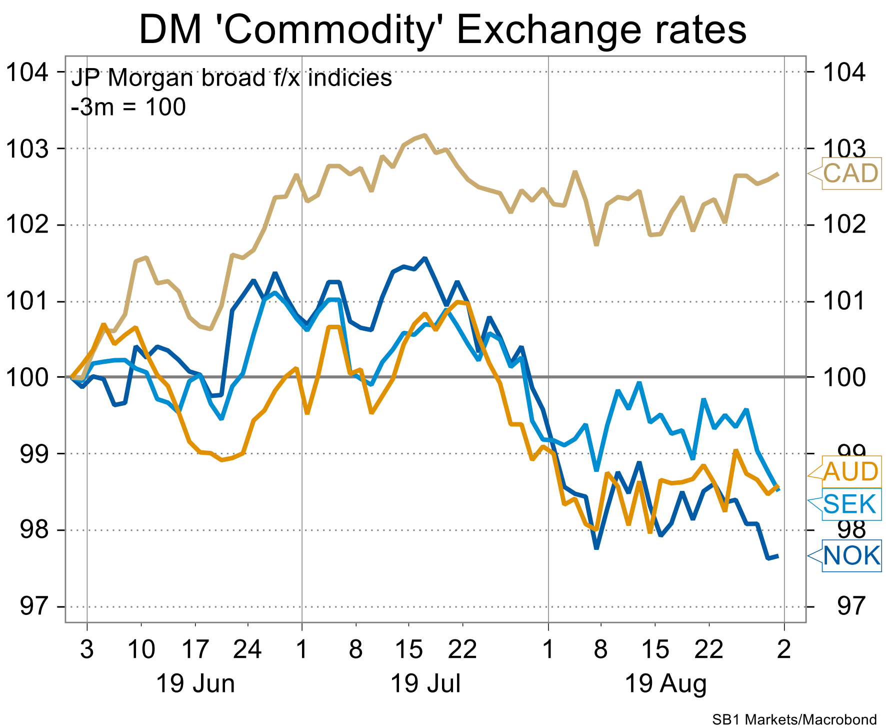
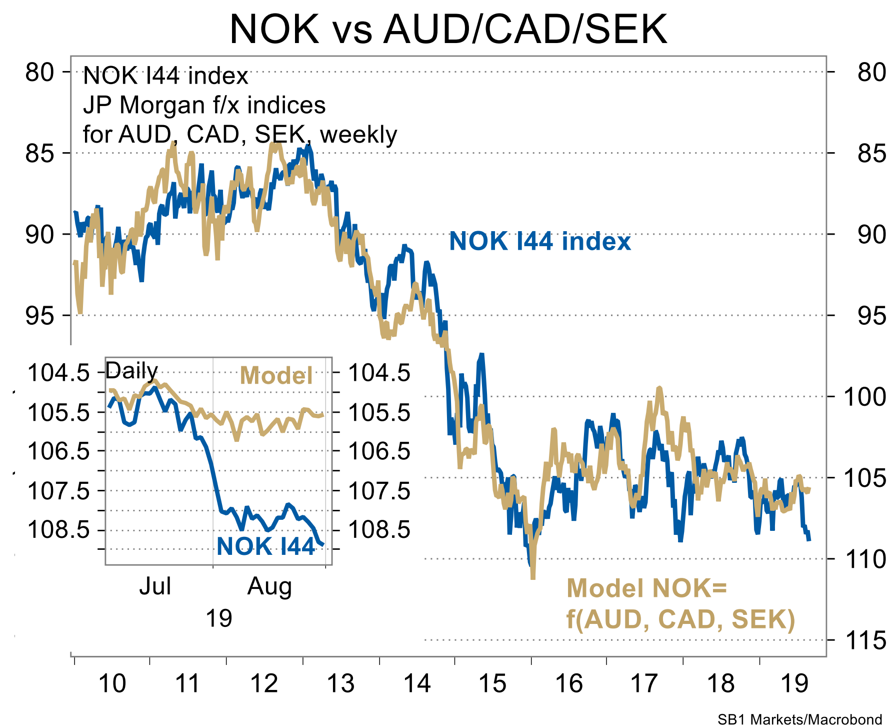
NOK weak vs the ‘supercyclicals’, CAD has not followed NOK; AUD, SEK just partly

Last week, both SEK and AUD fell with the NOK, while CAD appreciated. NOK 3.5% too low???





- Together, the other supercyclicals cannot ‘explain’ the recent NOK setback. The NOK has lost 3.5% vs. the the supercycle f/x model estimate over the past weeks. That’s not unusual but not something that happens often either
- SEK has fallen 1% less than the NOK since early Aug, but has still been more closely correlated than normal
  - » There could have been better arguments for a weaker SEK, given Swedish labour market data, and surveys
  - » The CAD is normally closer correlated to the NOK than SEK

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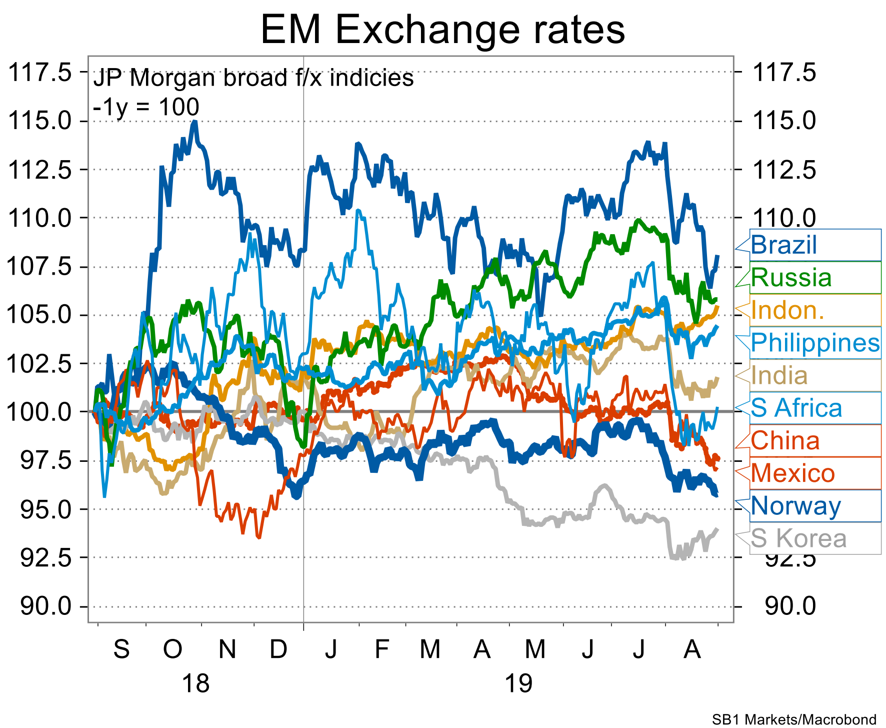
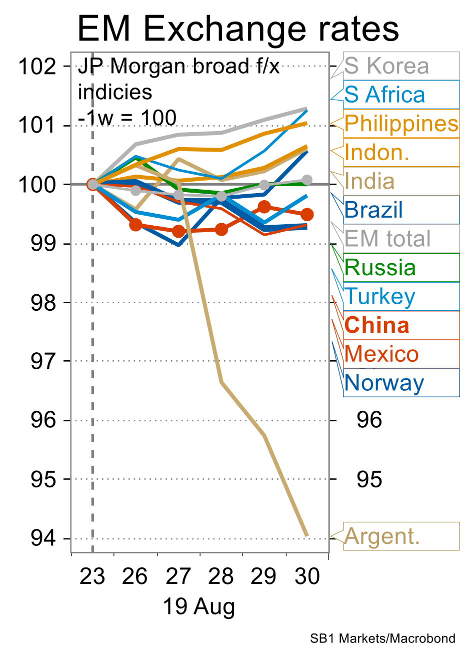
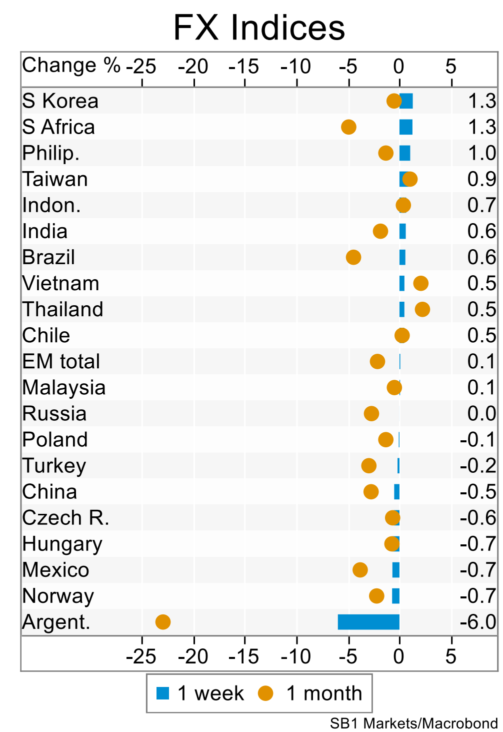
EM f/x: CNY depreciates but is just 3% weaker than before the 'new' tariff round

Mixed among other EMs weakened last week, Argentina still struggles







- Most EM currencies are down last month but no drama
- Argentina another leg downwards last week

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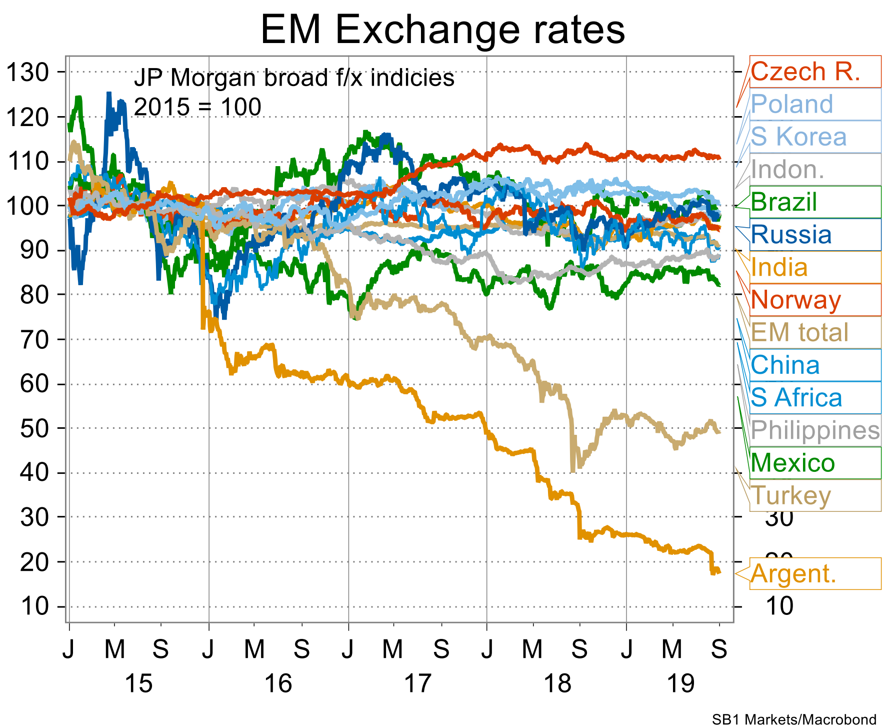
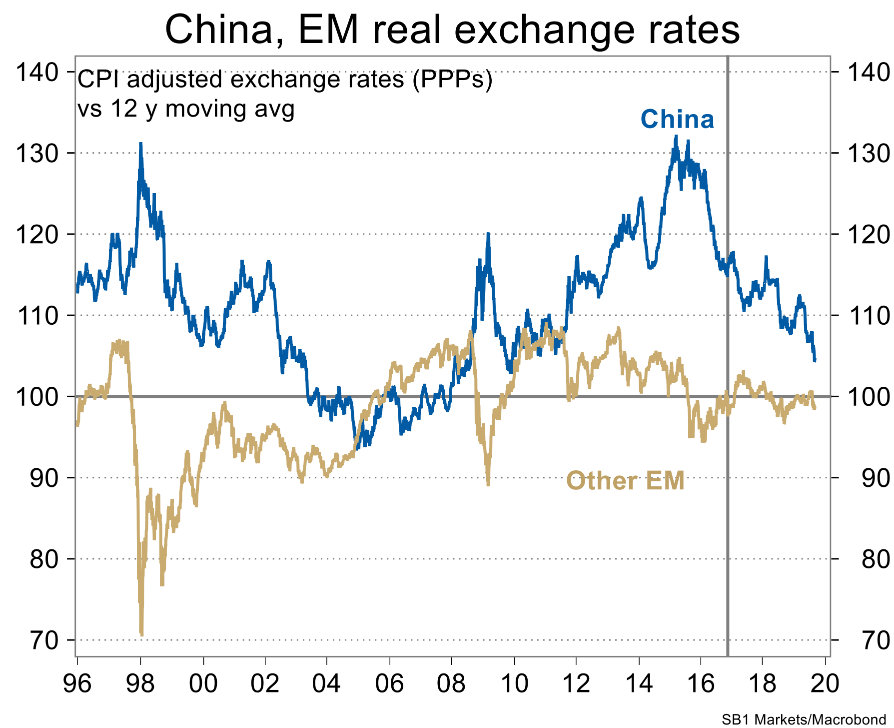
EM f/x, a long term view: Not that exciting, now

With a (normal) couple of notable exceptions, EM currencies have been unusual stable recent years





- 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, countered by a deficit at the service balance. The CNY real exchange rate has fallen by 10% since 2015 (of which 3% since early 2019) but is still 5% above its 12 y average
- Other EM currencies have in average been quite stable the recent years, even if some have run into problems, like always. Argentina and Turkey struggled last year, and Argentina once more now, for good reasons. The lira is down 50%, Argentina 82% (from 2015)

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