21 October, 2019

Macro Research

Weekly update 43/2019

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

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

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

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

- **Brexit?** Most likely. How? Not sure? When? Don't have a clue. Nobody else does either. However, a hard Brexit is even less likely than before, and a (likely) extension will probably increase the probability for a soft Brexit close to the one now on the table. **A USA China trade deal?** Perhaps, but not yet, said the Chinese. They had not recognized the tremendous deal they should have been a part of. Strange? **If that's not enough**, US domestic policies are more paralyzed than ever, led by meltdowners or people that are very sick upstairs

- **Chinese GDP** rose 1.5% q/q (6.1% annualized), in line with expectations. The annual rate fell to 6.0%, the lowest we have seen since 1990 but the slowdown is very slow. Other September data were in sum close to expectations and do not indicate any sudden setback in the Chinese economy. **Manuf. production** recovered more than expected and the slowdown has softened this year. **Retail sales** growth was close to unchanged and has stabilized this year. **Investment growth** is slowing just marginally, and accelerating in volume terms. **Credit growth** is slowly accelerating as monetary policy turns more expansionary

- **US manufacturing production** fell 0.5% m/m in Sept. Production stabilized in Q3 but the outlook is rather bleak, and the first **October surveys** are not shining**. Retail sales** fell modestly in September but Q3 was anyway up at an impressive 7.5% speed. Volume growth is easing somewhat after a steep rise in H1. **The housing market** rebound is gaining strength; housing permits remained elevated in Sept and Homebuilders confidence improved much more than expected in October. **Fed's Beige Book** reports softer growth, dragged down by weaker manufacturing output. Employment growth is slowing due to labour shortages, no argument for another interest rate cut on Oct 30. **The leading index** fell moderately in Aug/Sept

- **Eurozone industrial production** rebounded modestly in August, up 0.4% m/m. The trend is anyway straight down and the PMIs are signaling an even steeper decline. **The German ZEW survey** held steady at a low level in October, at least the expectations component. The view of the current situations drops, as it usually does when a the economy is contracting

- **The Swedish labour market is 'collapsing' - or is it not?** Statistics Sweden admits data flaws running back to 2018, which have resulted in an overestimate of employment figures in early 2019 and an corresponding exaggeration of the downturn the past 3 months. Nonetheless, the labour market is no doubt turning sour, just at a more gradual pace than reported. **House prices** rose briskly in September, up 0.6% m/m and are trending moderately up

- Banks in **Norges Bank lending survey** reports a surprising upturn in household loan demand in Q3 and banks expect a further increase in Q4. Is the moderate housing market upswing and an overall solid economy offsetting the effects of higher interest rates? These data are rather contradictory to actual credit growth, which has been slowing modestly. We doubt that mortgage demand will accelerate the coming months

Growth is slowing but there are some signs of stabilization

September/Q3 broadly in line with expectations, no signs of a sharp slowdown

- **<u>Growth is slowing amid persistent trade war uncertainties and slowing domestic demand – but data are not at all signalling any abrupt setback</u>**
- **GDP** rose by 1.5% q/q (6.1% annualized) in Q3, in line with expectations. Yet, the annual rate came in 0.1 pp weaker than expected, at 6.0%, from 6.2% in Q2. The details were broadly unchanged from Q2; consumption and investments are both slowly slowing, while higher net exports are fuelling growth
- **Industrial production** bounced back in Sept, up 0.7% m/m, following two soft months. The official y/y rate spiked to 5.8%, well above expectations, while our less volatile calculation yields a 6.0% speed (up from 5.7%). Growth is slowly easing, yet at a slower pace this year. PMIs are indicating an upswing
- **Investments** have been expanding steadily and growth is slowing just marginally over the past 2 years. The annual rate has inched down to 5.2% (while the more volatile YTD rate fell to 5.4%). Nominal investments are still growing slower than GDP, real growth is strengthening and has come up to some 3%
- **Retail sales** growth was unchanged at 6.1% according to our volume estimate but growth has slowed during 2019, as during the previous years (excl. 2018). The retail sales data are often revised substantially, yet data at hand do not signal any setback in domestic demand
- **Credit growth** has been slowly accelerating recent months, helped by bank lending. The credit impulse is marginally positive, following the 2018 contraction

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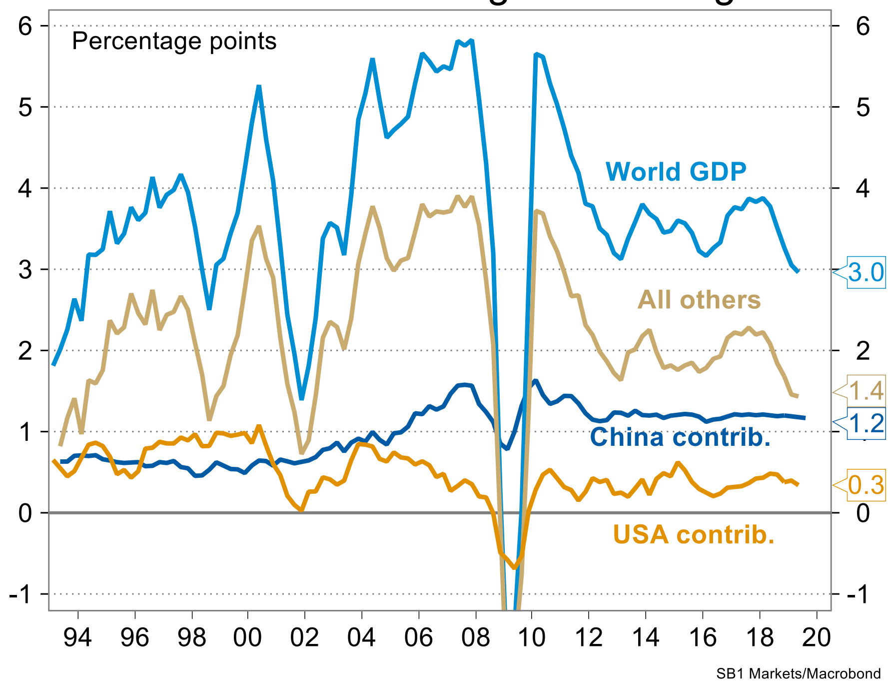
What a Chinese blow to the global economy!

Well, please check the facts too (as usual)

China - Contribution to global GDP growth



Chinese economy

Slowing Chinese growth delivers blow to global economy

Expansion of 6% is worst in three decades due to trade war with US and cooling investment

- European auto stocks in reverse while China's growth disappoints
- Chinese local government funds run out of projects to back
- IMF slashes global growth forecast on trade war fears

Top, front page
Fin Times, Oct 18

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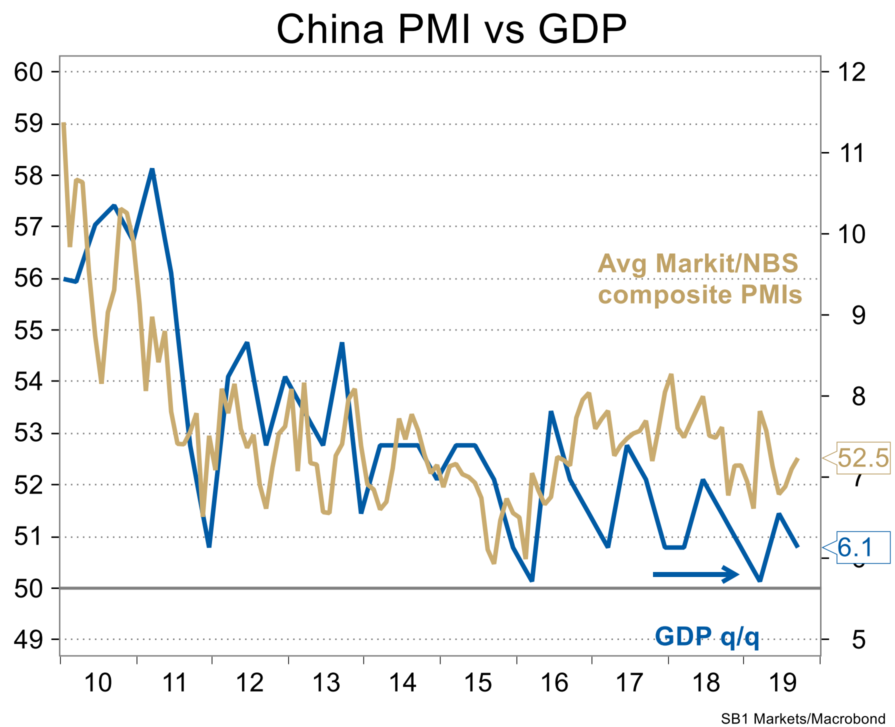
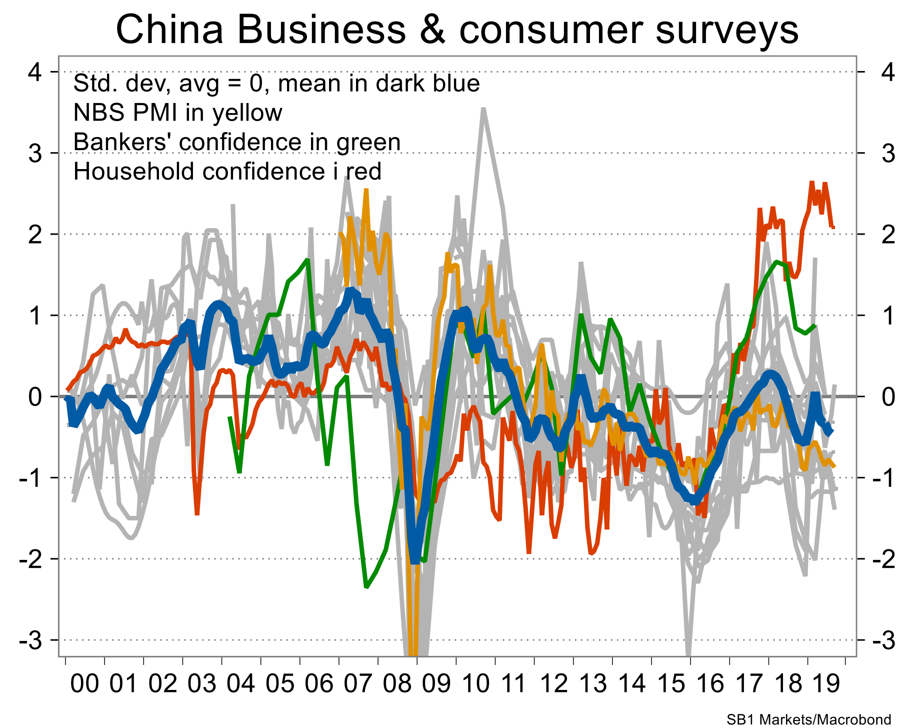
Surveys are not signalling a further growth slowdown

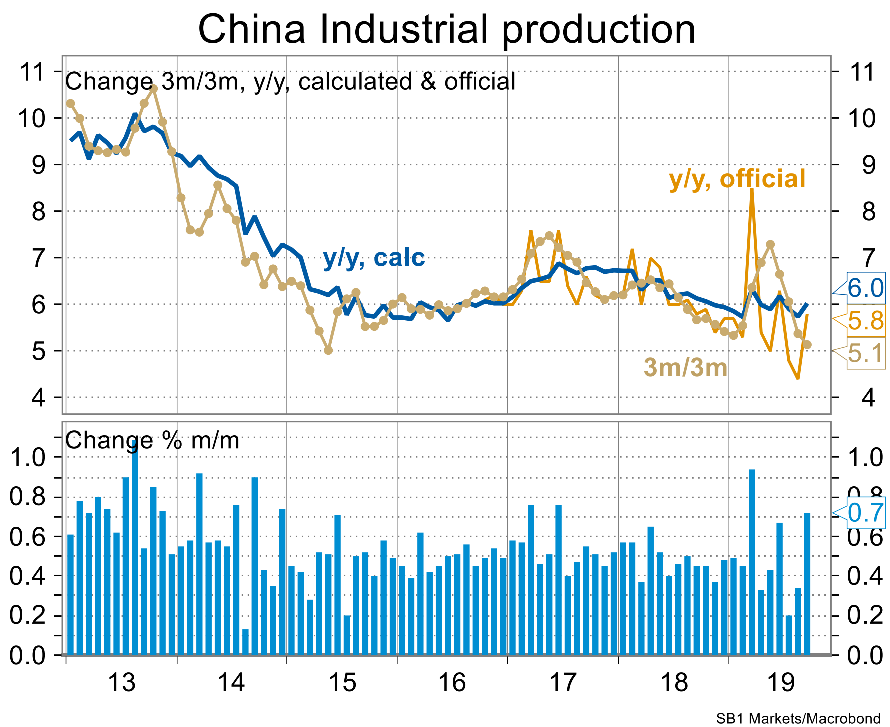
Surveys are in average below par but not by much

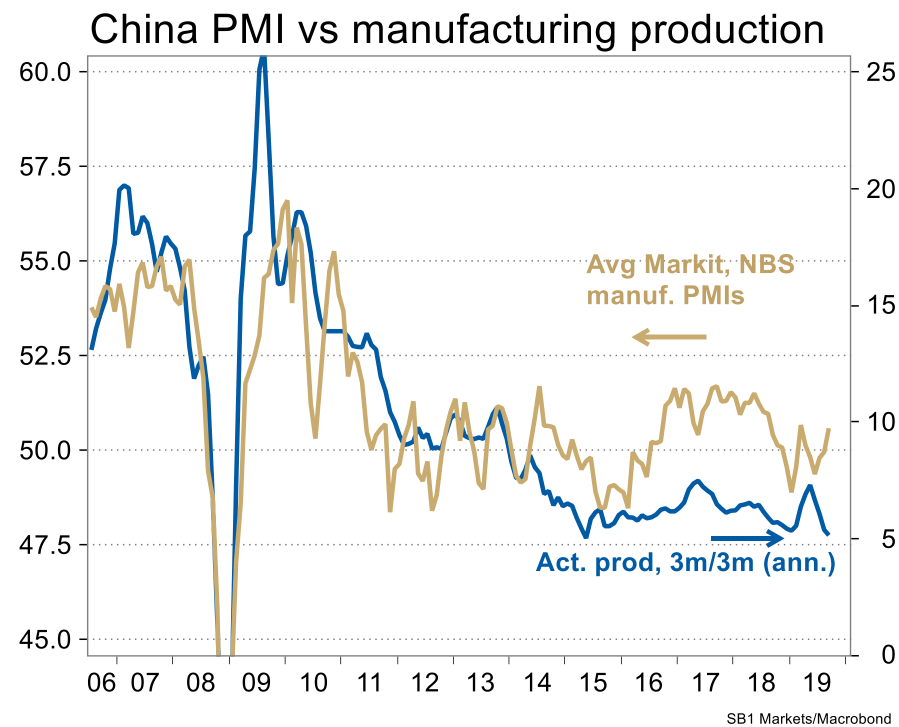




Industrial production bounced back in Sept, trend slowly down

Production jumped 0.7% m/m after two soft months. Our y/y calculation yields 6%, up from 5.7%

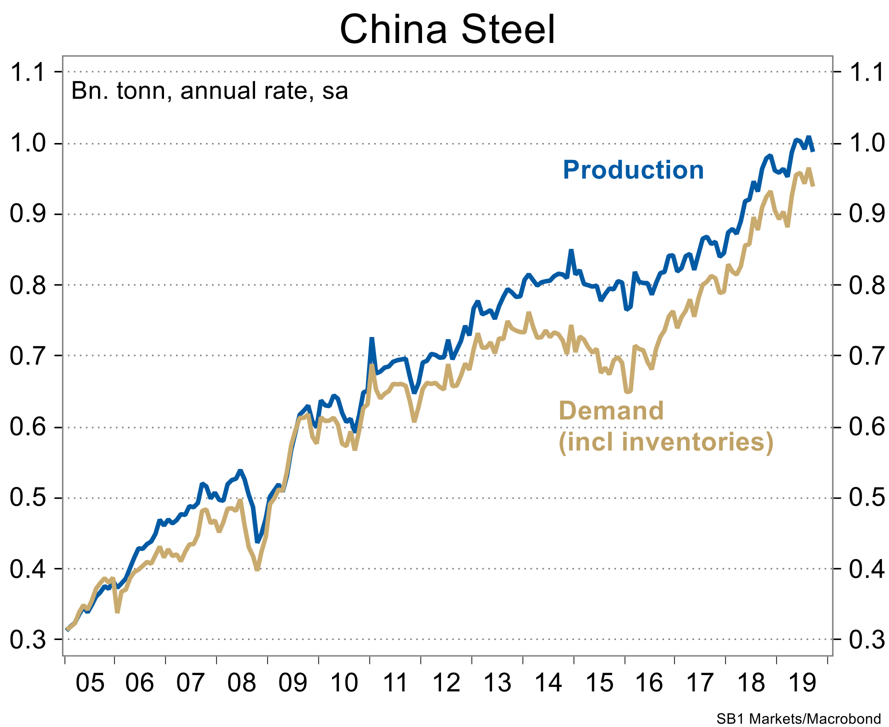




- Production rose 0.7% m/m in September, the highest since March, after muted growth in July/Aug. The 3m average m/m rate is 0.4%, down from 0.5-0.6% in early 2019. Our y/y rate edged up 0.2 pp to 6%, from 5.7%, more or less stabilized since Jan/Feb. Growth slowed in Q3, to 5.1% annualized (vs 6.7% in Q2)
  - » The official y/y growth rate is 'useless', far too volatile as it is not adjusted for holidays or working days. In September, growth soared 1.4 pp (vs our calculated 0.2 pp acceleration) to 5.8% from 4.4% in August (the lowest since 2002) to 5.8%, well above expectations
- PMIs have improved and are pointing to a stabilization in manufacturing activity. Export volumes are trending up and are close a peak levels. China has most likely not been brought to a halt, in fact, the slowdown was more dramatic in 2018 than it has been so far in 2019.

Steel production (and demand) down in Sept, probably still on the way up

Upward trend intact, after both demand and production softened last winter. Reduced overcapacity



- Production is up some 5% y/y (smoothed) and demand is expanding a tad faster, (almost) well explained by the strong growth in construction starts. On the other hand, slowing auto production signals softening steel demand from that sector
- China is still a net steel exporter, but far less than during the 2015-16 setback in domestic demand. Back then, production was cut by far less than domestic demand and net exports soared. Now, net exports are far lower (and domestic demand closer to production

Retail sales volume growth steady in Sept, no collapse in domestic demand

Growth has more or less stabilized the past year, after a setback in 2018. Official y/y rate slides down

- The official value growth rate rose to 7.8% from 7.5% in August, in line with expectations%. Our less volatile value growth estimate (based on monthly seas adj. data) yields 8.1%, up 0.1 pp. Value growth is slowly easing but less so in 2019
- We assume a 0.5% m/m volume growth, the same pace as the prior month. Growth slowed to 5.1% annualized in Q3, dragged down close to zero growth in July. The annual volume rate was unchanged at 6.1%, stabilized since late 2018, even if inflation has accelerated due to the high pork meat prices (which has not lifted the official retail price index, quite strange)
- Consumer confidence is very high and does not point to any demand weakness. Even so, consumption is not thriving, larger tax cuts may be needed to bring consumption growth up

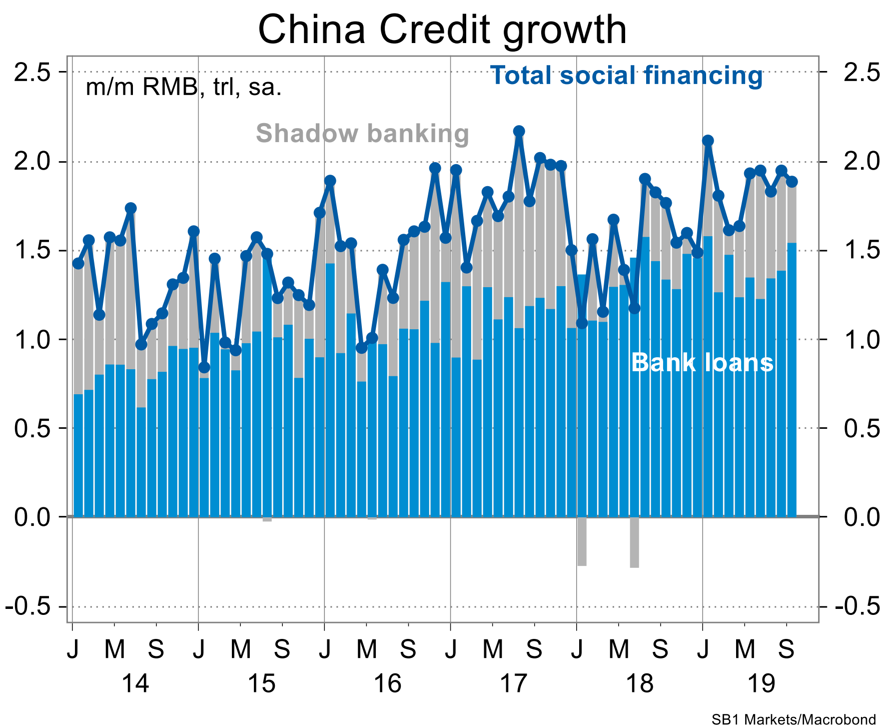
Nominal investments are slowing just marginally

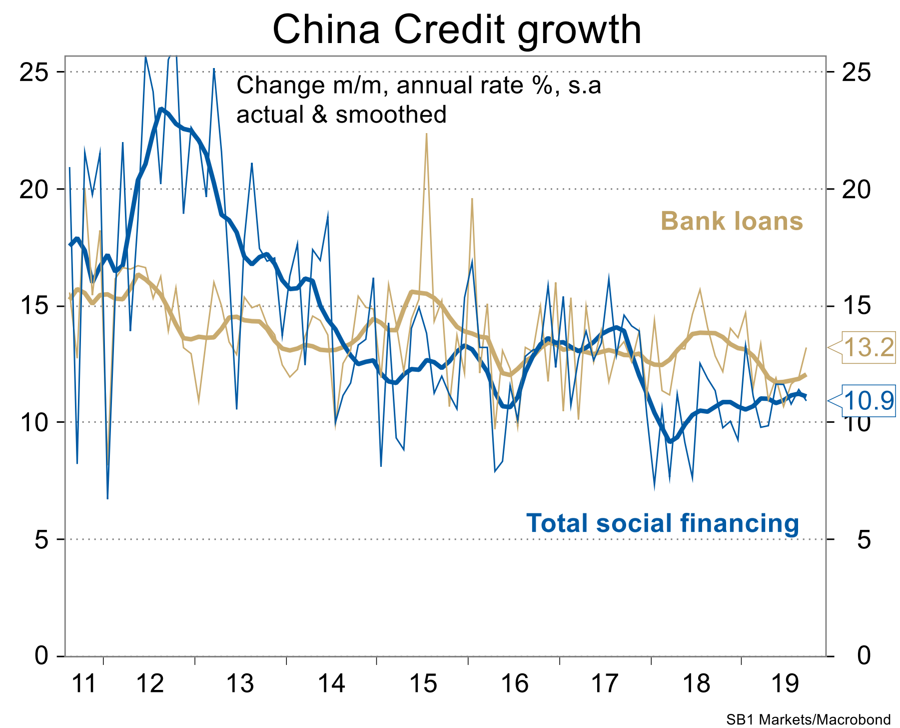
The long term decline in investment growth has halted, at a comfortable, low level

- Urban investments rose 5.4% y/y ytd in September, according to the official data, down from 5.5% in August, expected unchanged. Our calculation yields a 5.2% y/y growth, trending just marginally down. The m/m rate was stable at 0.4%. Monthly growth rates have been stable since late 2017. In real terms, we assume growth has accelerated to some 3%, from close to zero through last year
- Manufacturing investments are still increasing but just marginally. Retail trade investments are sharply down, while real estate is booming
- Long term, nominal investment growth (measured this way) has been on a downward path, from 25-30% before 2009 – but it has now stabilised, well below nominal GDP or income growth

Bank lending gains pace, supported by easing policy?

Credit growth was substantially higher than expected in September, driven by bank lending





- Total credit rose by 10.9% m/m annualised in Sept, from 11.4% in Aug. In RMB, total credit rose by 2.27 trl, expected 1.9 trl (not seasonally adjusted). The underlying trend is slowly up since the trough in early 2018. The credit impulse is now marginally positive
  » Growth in bank lending accelerated for the third month in row in Sept, after a slowdown in H1 2019. Most likely, the upturn is a result of easing monetary policy; bank's reserve requirement have been cut 6 times, releasing close to 5% increase in lending capacity. Credit supply through the non bank ('shadow') credit market, which drove total credit up in H1, has slowed the past months. Shadow banking now accounts for some 20% of total credit supply
- What's next? Many expect the PBoC to turn more expansionary, and interest rates cuts are quite likely. However, there are good arguments against pushing the credit accelerator even harder. Credit growth is well above growth in nominal GDP, and high debt ratios are climbing further

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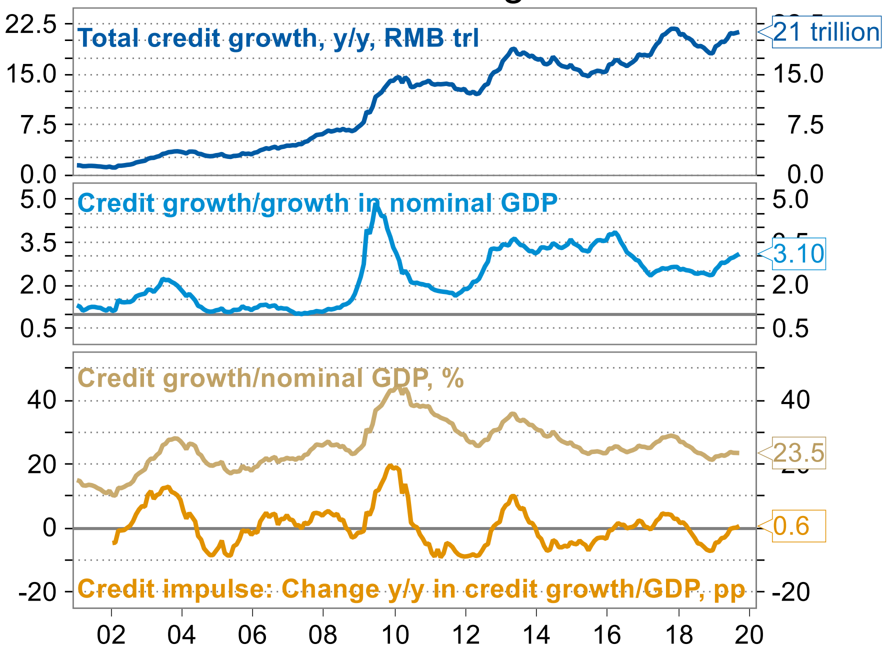
Credit impulse has turned marginally positive, from negative

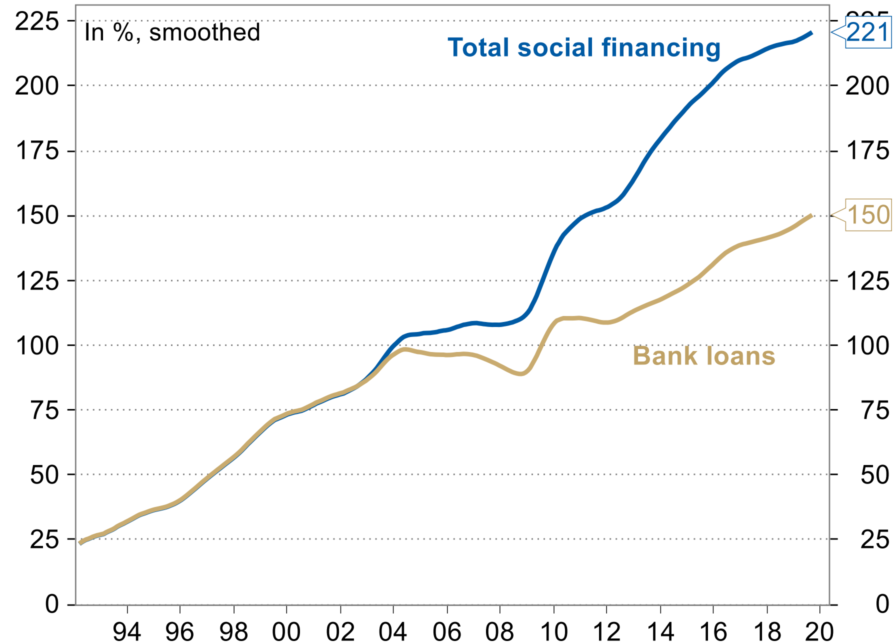
Credit growth is now slowly increasing vs GDP

China Credit growth



SB1 Markets/Macrobond

China Credit/GDP



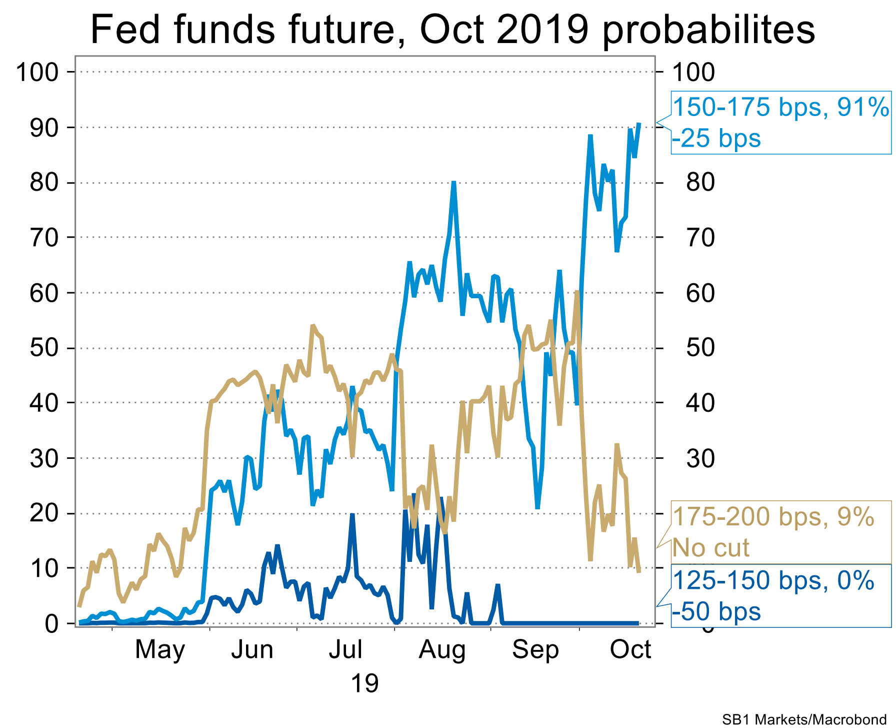
SB1 Markets/Macrobond

- A negative credit impulse implies that the credit growth/GDP ratio is declining (the 2nd derivative)
  - » Indicates credit tightening (or weaker demand)
  - » Has been associated with slowdowns in the Chinese economy
  - » Now, the credit impulse has risen to marginal positive
- We are uncertain how far the authorities are willing or able to bring credit growth back up. The credit/income level is high – and it is still increasing. For every RMB GDP grows, credit increases 3 by RMBs, and each year growth in credit equals more than 20% of GDP. <u>That's not sustainable, neither for lenders or borrowers in the long run, if nominal GDP growth is less than 10%</u>. The Government may succeed in increasing credit supply short (if they dare to, vs long term risks) but the problem may turn out to be demand for credit

Fed's Beige Book reports slower growth but still very tight labour market

Fed's 'regional network' lowered the growth assessment to 'slight to modest', from 'modest'

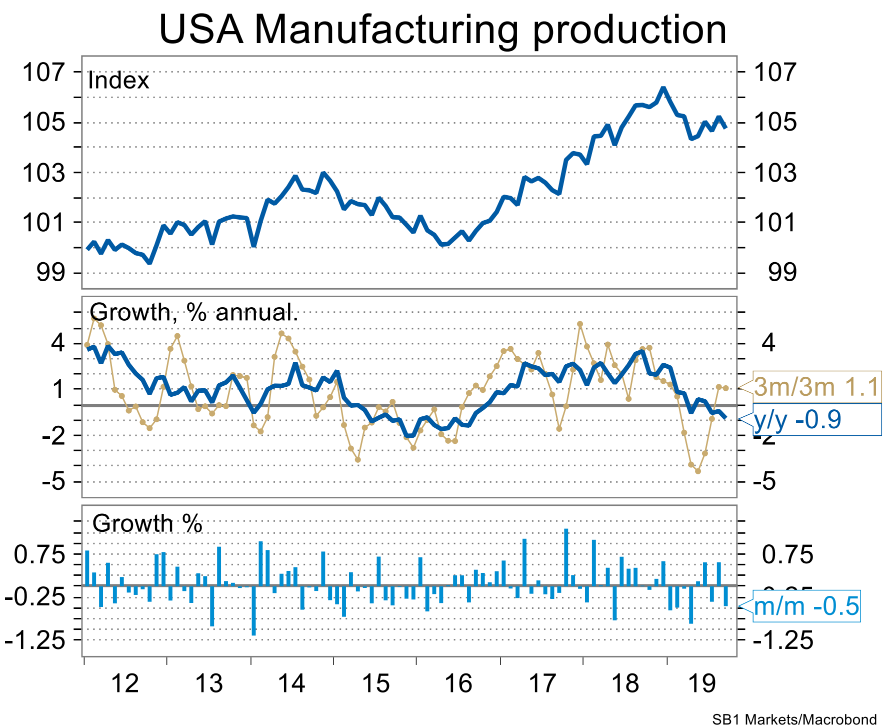
- Economic activity expanded at a '*slight to modest*' rate, according to the respondents to Beige book, downgraded from 'modest' in the September. Many businesses lowered their growth outlooks
- On the demand side
  - » Consumer spending was still solid; robust retail and auto sales
  - » No substantial changes in housing market conditions
- On the supply side
  - » Manufacturing is the major drag on growth, businesses report a further slowdown in manufacturing activity
- Labour market
  - » The assessment of employment growth was changed to 'slight' from 'modest', due to rising labour shortages
  - » <u>Some businesses noted that they reduced working hours rather than staff levels as demand has slowed</u>, due to concerns about future labour shortages (labour hoarding). Wages still rose 'just' moderately
- Prices
  - » Modest inflation and mixed reports on the impact of tariffs
- **In total, the Beige book reflects just a modest slowdown in the US economy, chiefly stemming from global trade uncertainties and labour market tightness. Not an argument for cutting interest rates once again!**

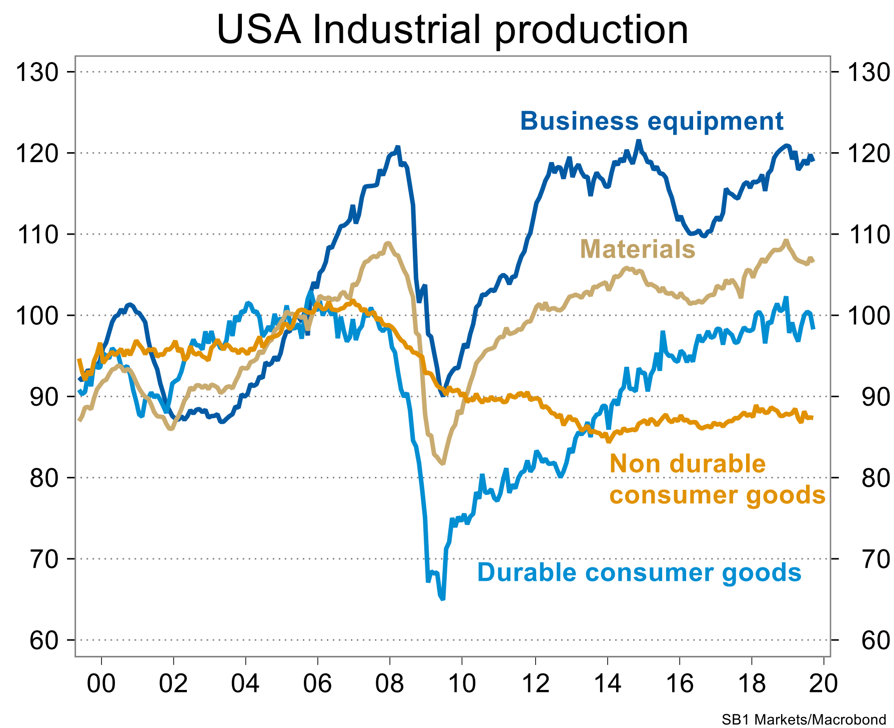


The market is pricing a 25 bps Fed cut on Oct 30 by an 91% probability (and 9% for no cut). We think the probability for a cut is lower, yet still above 50%, even if a cut is not needed and the FOMC was very divided at the Sep. meeting

Manufacturing production stabilized in Q3 but the outlook is gloomy

Production fell 0.5% m/m in September, up 1.1% in Q3. Surveys signals a weaker outlook

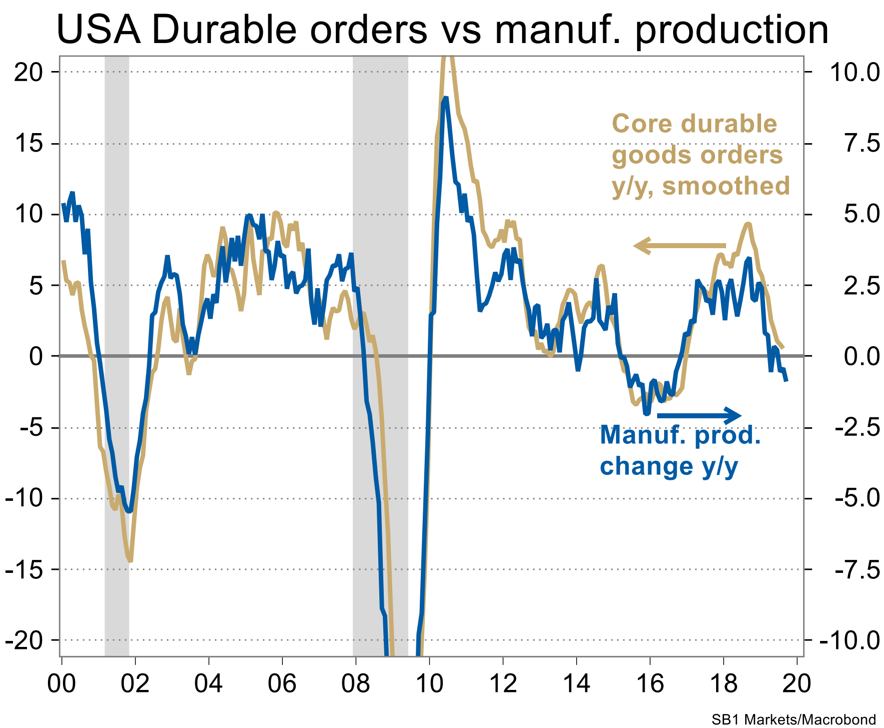


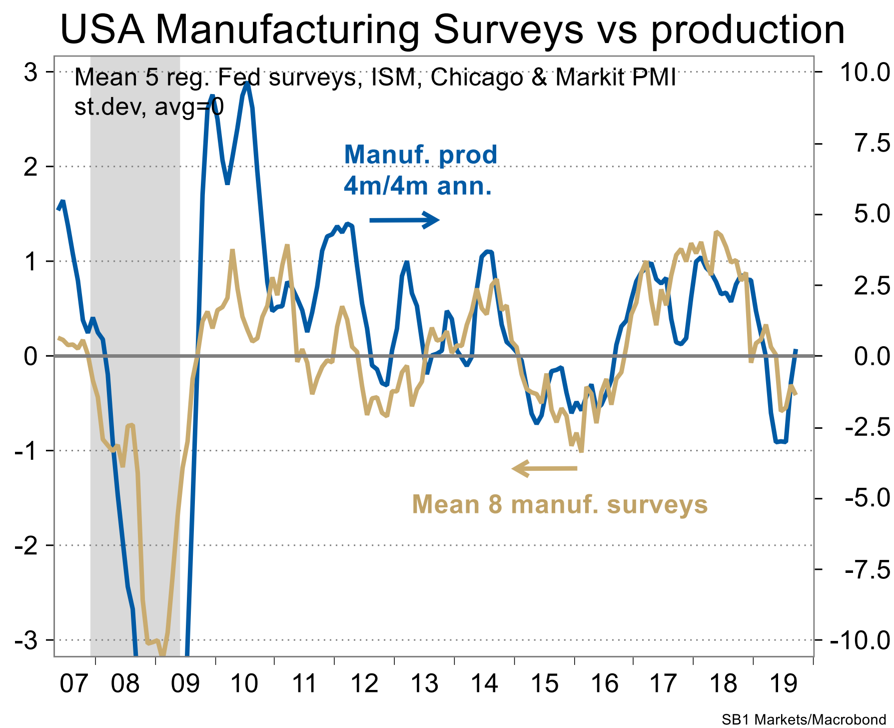


- Manufacturing production declined by 0.5% m/m in September, 0.2 pp below expectations. Still, production has increased marginally the past month and was up 1.1% annualized in Q3, vs the 3.2% drop in Q2. Production is still 1.5% below the Dec '18 local peak and the annual rate is down 0.9%
  - » Total industrial production including energy & mining fell 0.4% and underlying growth is marginally stronger than for manufacturing
  - » Production has slowed in most sectors, the steepest decline has been that of durable consumer goods the past year
- The first October surveys? Check two pages forward!

Unfortunately, orders & surveys do not signal any further recovery

An average of surveys signals a decline in production, orders point to just a stagnation





- <u>Flip to the next slide for more on the surveys</u>

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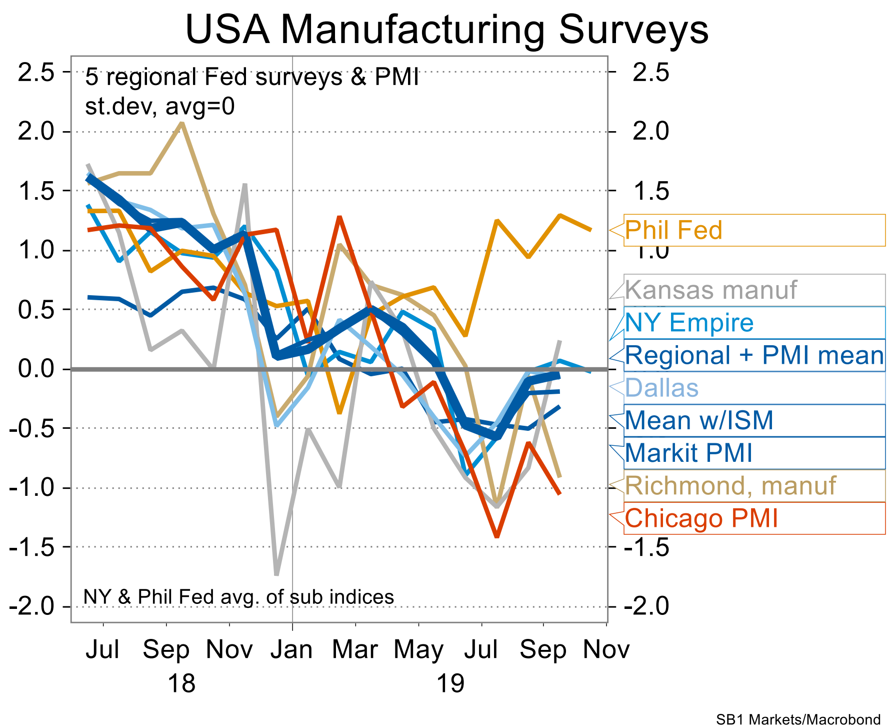
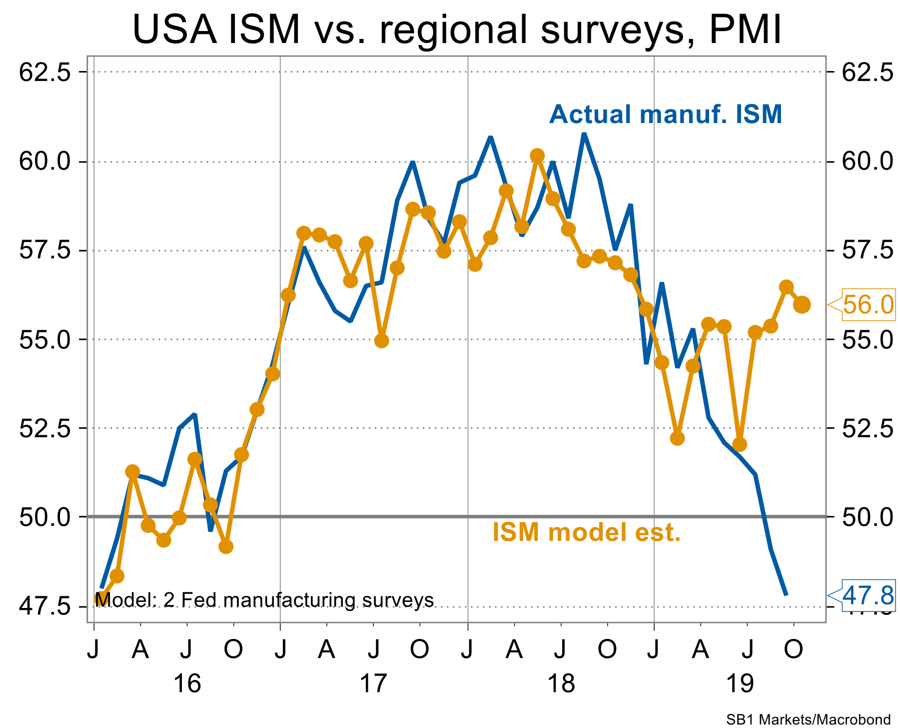
NY Fed's manufacturing index a tad up in Oct, Phil Fed slipped

Phil Fed has been out of line vs other surveys recent months, the NY Fed survey closer to the ball

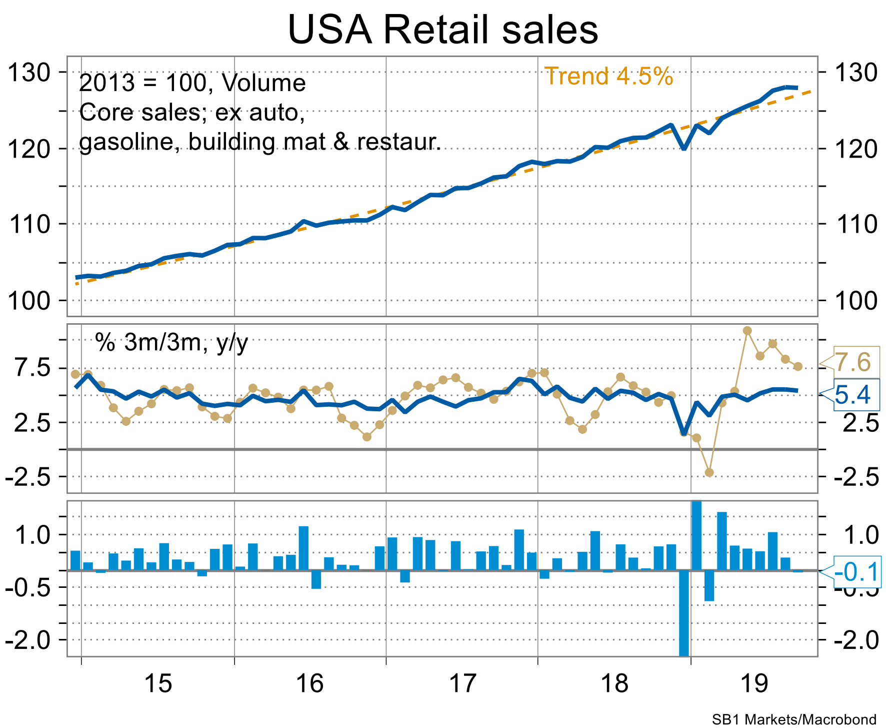


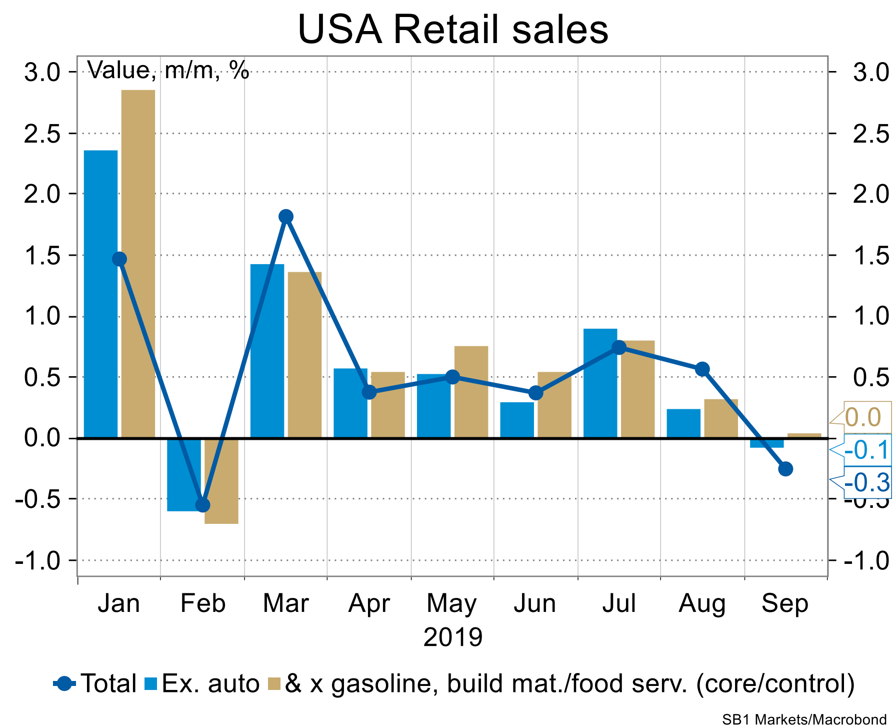


- The Philadelphia Fed index fell more than expected in Oct, to 5.6 (from 12). When calculated as the average between relevant sub indices, like the total ISM and PMI are calculated, the index also fell but the level is still well above average
- The NY Empire is more in line with others, the headline improved marginally in Oct, better than expected – while the average of the sub-indices fell marginally
- Taken face value, these indices signals a small decline in the manufacturing ISM. However, if we let the two surveys indicate the level, they signal a 'crazy level, at 56 (compared to actual ISM at 47.8 in Sept. However, these to regional surveys have been far too to strong compared to other surveys – and actual manufacturing production

Retail sales soared in Q3 but growth is slowly losing steam

Core sales volume fell -0.1% in Sept (our est), underlying growth is still solid

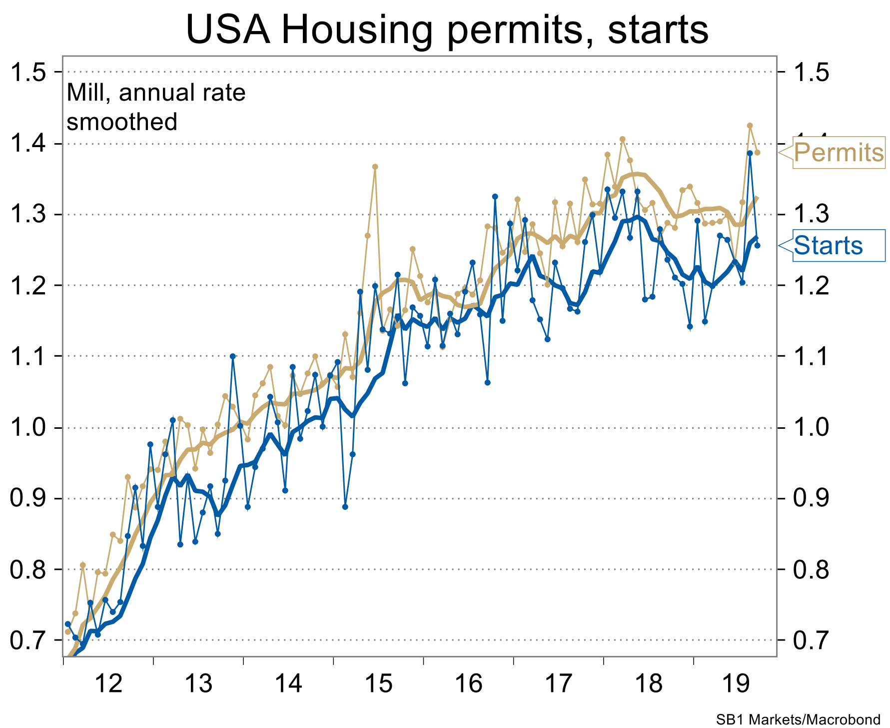


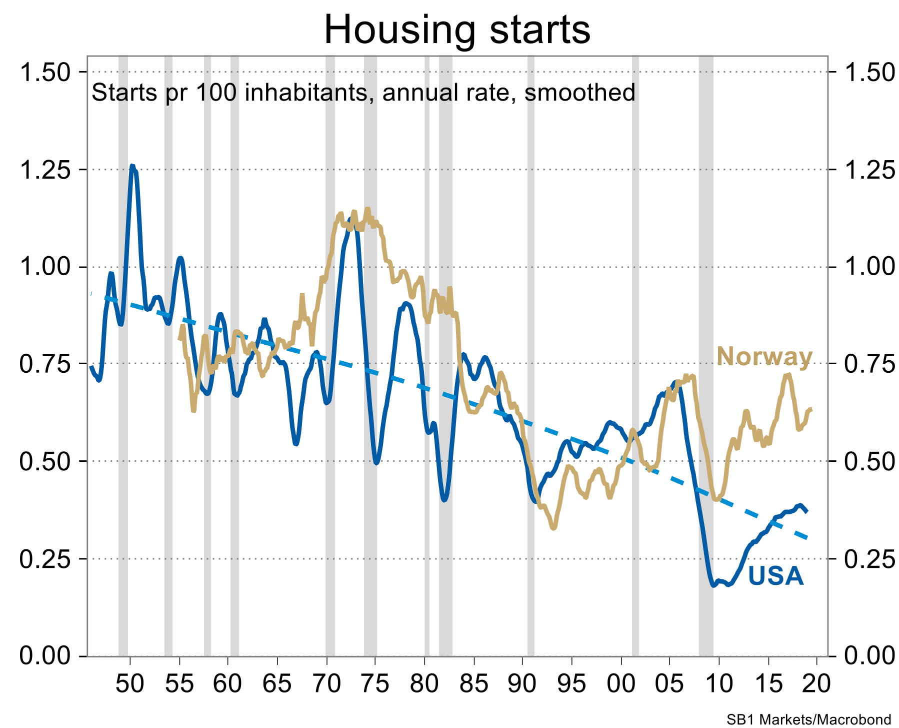


- Core retail sales (ex. auto, gas, building materials & restaurants; control group) were flat m/m in nominal terms in September, 0.3 pp weaker than expected. Total retail sales fell 0.3%, even as auto sales increased marginally
- We estimate a 0.1% m/m decline in core sales volume, following strong growth the prior months. Growth has eased somewhat, after accelerating in H1. Regardless, the 3m/3m speed at 7.6% is still rather impressive, and the annual rate is solid at 5.4%
  - » The slowdown the two past months may still be an early indication that the manufacturing led slowdown is now spreading to the consumer side
  - » Income growth has slowed somewhat, and consumer confidence is mixed – the risks are now skewed to the downside. However, we have no indication of an abrupt slowdown (even if declining savings have been funding half of the growth in consumption so far in 2019…)

Housing permits remained very strong, volatile starts back to a ‘normal’ level

Permits fell just marginally in Sept after Aug spike, both starts and permits trending moderately up





- Housing starts fell 9.4% m/m in Sept while permits fell 2.7%, thus, reversing just a small share of the surprising Aug jump. Permits were reported at an annual rate of 1.39 mill in Sept, vs expectations at 1.35 mill
- Housing permits are usually less volatile than actual starts, thus, a more useful gauge of the activity in the sector than actual starts. Permits have climbed steeply recent months and are back at the 2018 peak level, however, the smoothed rate is still 2.4% below the peak. Starts have increased more than permits the past months
- Housing starts/permits reflect a solid housing market, boosted by low mortgage rates. Upbeat Homebuilders’ confirm a moderate upswing, so do home sales. The level of housing starts is still quite low, and the home construction downside is not large compared to the downturn in 2006-09

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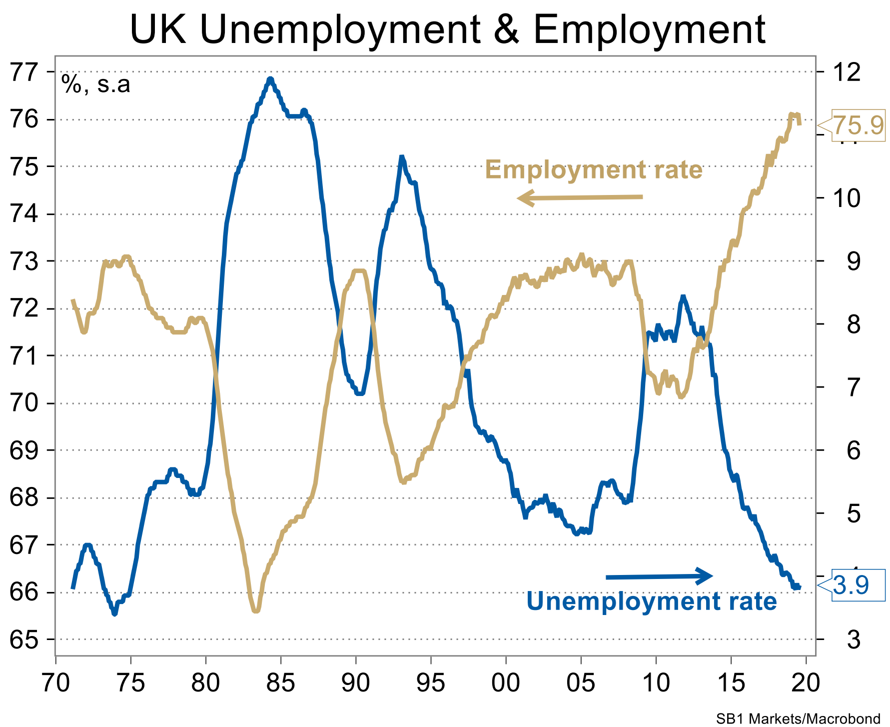
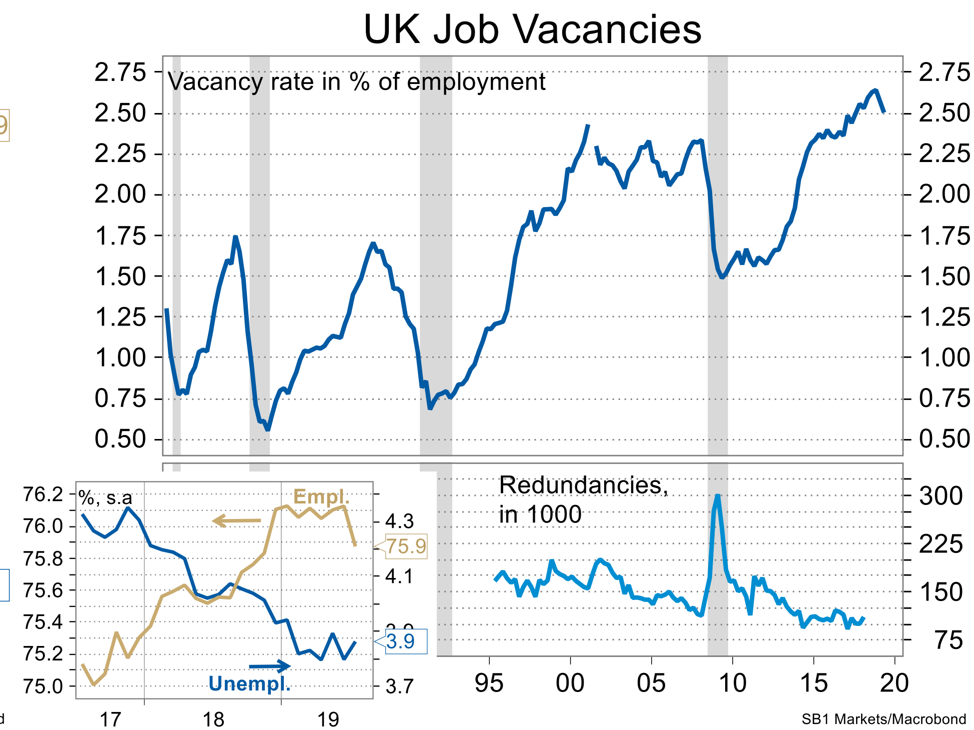
Unemployment rose, employm. fell; Brexit slowdown hitting the labour market?

Unemployment edged up 0.1 pp and employment dropped 0.2 pp. And wage growth flattens out

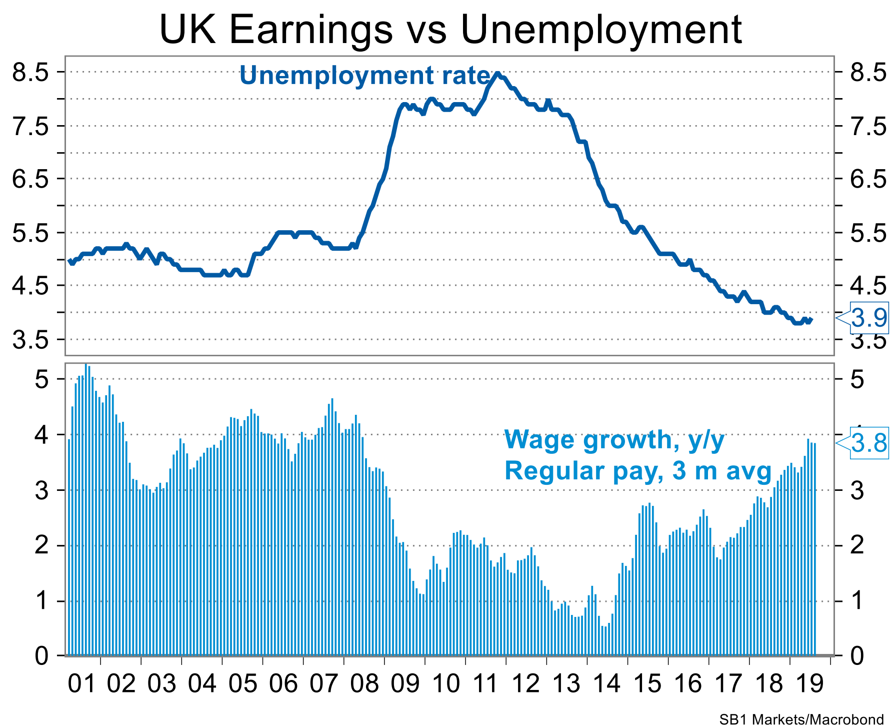


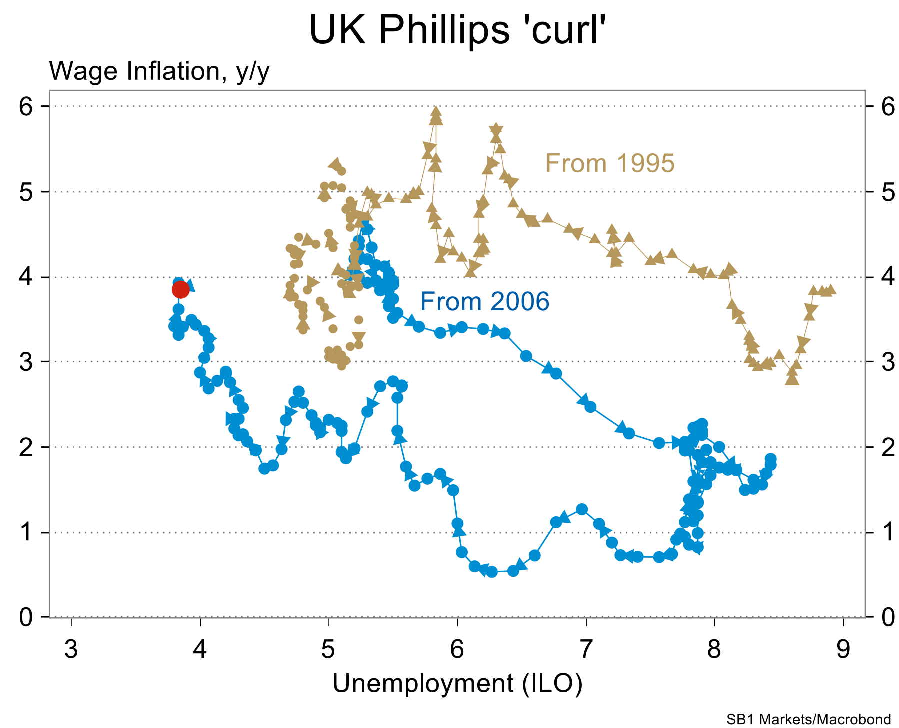


- Unemployment (LFS/ILO) ticked up to 3.9% in July (avg June-Aug), expected unchanged at 3.8%. Unemployment has flattened out since early 2019, at the lowest level since 1974
- The employment rate fell to 75.9%, a 0.2 pp decline. This is the largest monthly decline since 2009. May be a one off but the employment rate has anyway flattened out since January, due to supply constraints or lack of demand? The vacancy ratio is just slightly down from a record high level (Q2 data). Wage inflation is approaching 4% (check next page)
- In sum: these data may signal that the labour market is now at a turning point, probably triggered by Brexit troubles

Wage inflation was accelerating; unchanged at 11 y high the past 3 months

A tight labour market has been boosting wage inflation, at peak now?

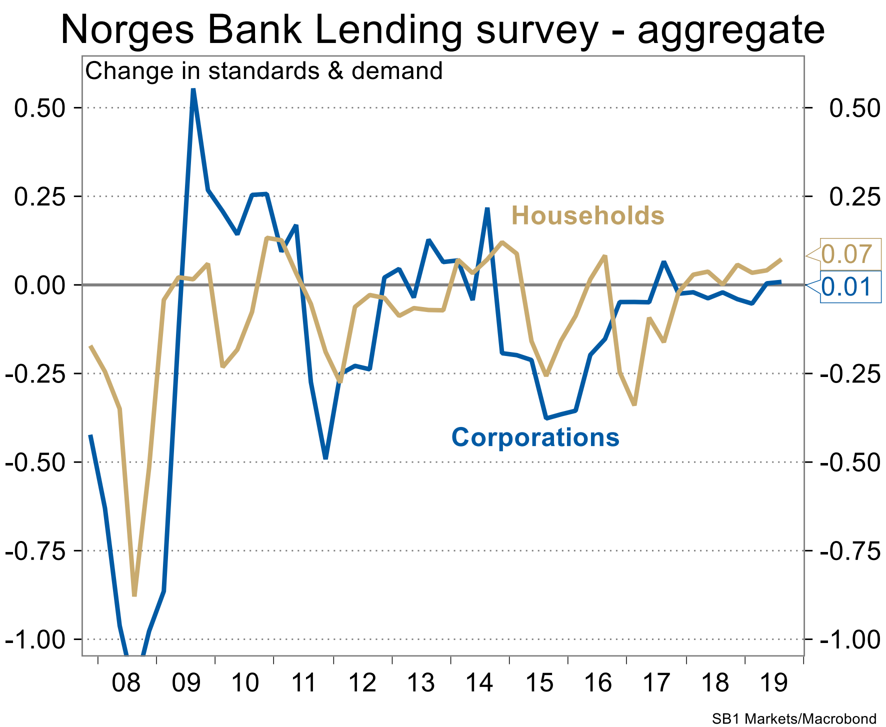


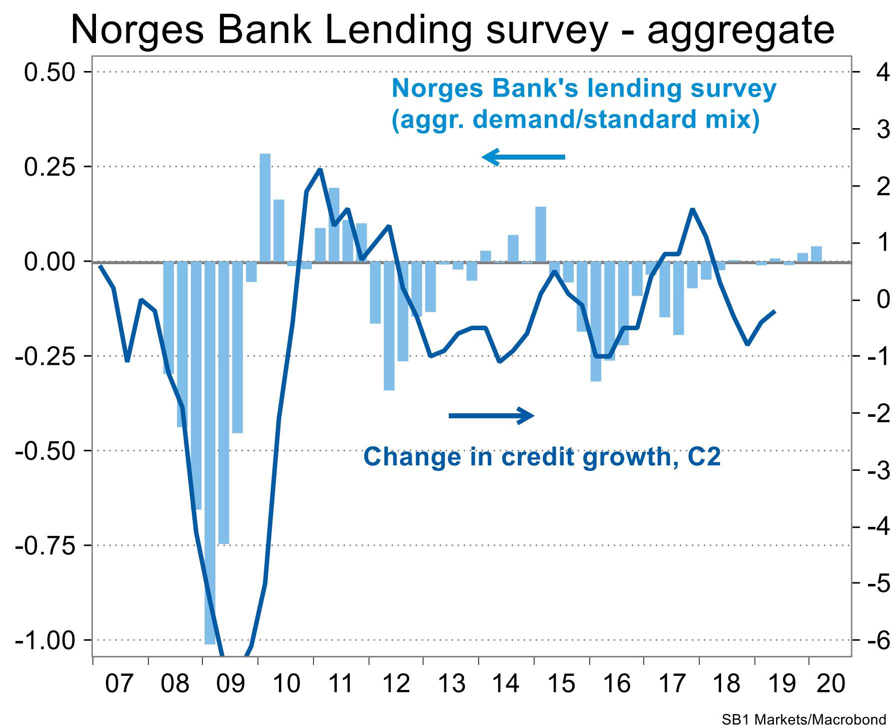


- Wage growth (regular pay) was flat at 3.8% y/y in August, or down 0.1 pp after adding a 3 m smoothing. Wage inflation was heading straight up but it has not accelerated further the past 3-4 months
- UK productivity growth is still well below 1%, and unit labour cost inflation was running at 2% in Q1. Cost pressure is not muted!

Banks expect higher household loan demand in spite interest rate hikes

Banks report a surprising acceleration in mortgage demand in Q3 and expect even more in Q4

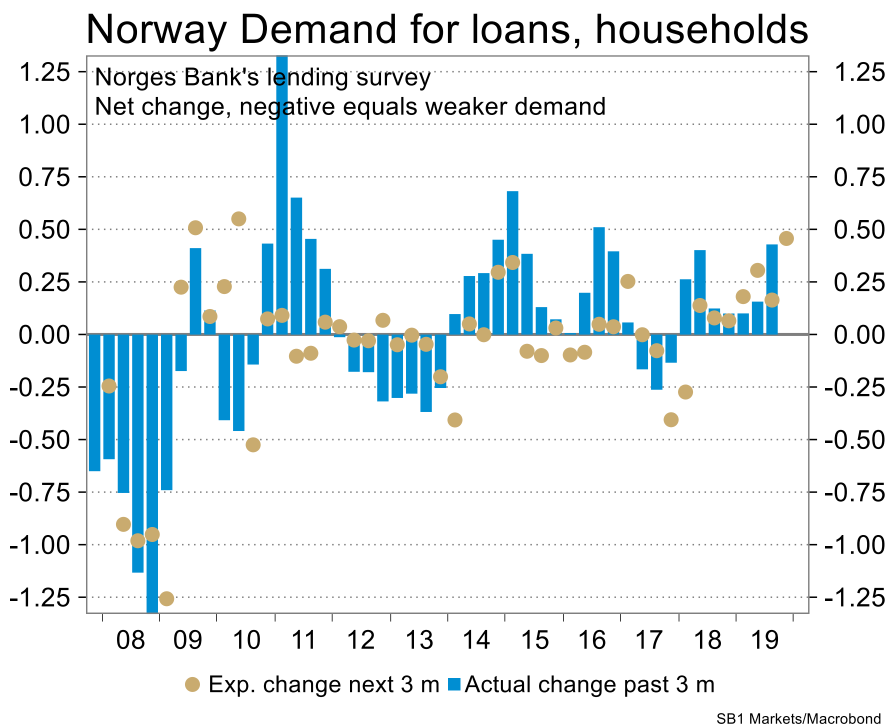


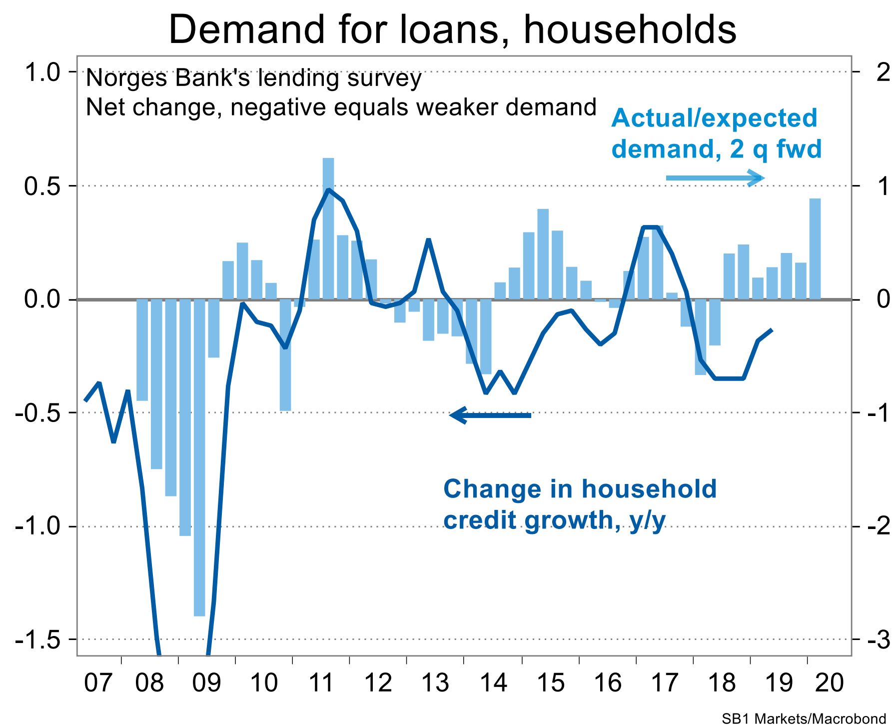


- Banks in Norges Bank's Q3 Lending Survey reports somewhat higher credit demand from households and unchanged demand from the corporate sectors. Our aggregate lending survey indicator (demand + standards reported in Q3 and Q4 expectations, both sectors) has inched up the past 2 quarters, reflecting slightly higher credit demand
  - Banks report a lift in mortgage demand in Q3, in contradiction to the modest slowdown in actual household credit growth
  - Credit demand from corporations was unchanged and banks project no changes the coming quarter

If the banks' projections are correct, credit growth will turn up (we doubt so)

Banks report accelerating household loan demand, while actual credit is slowly softening

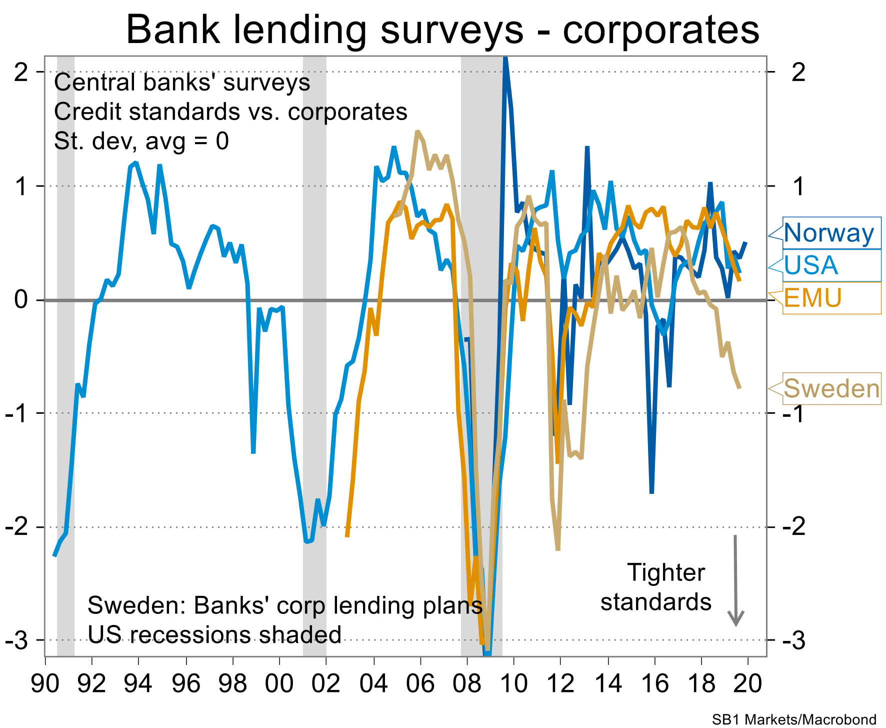


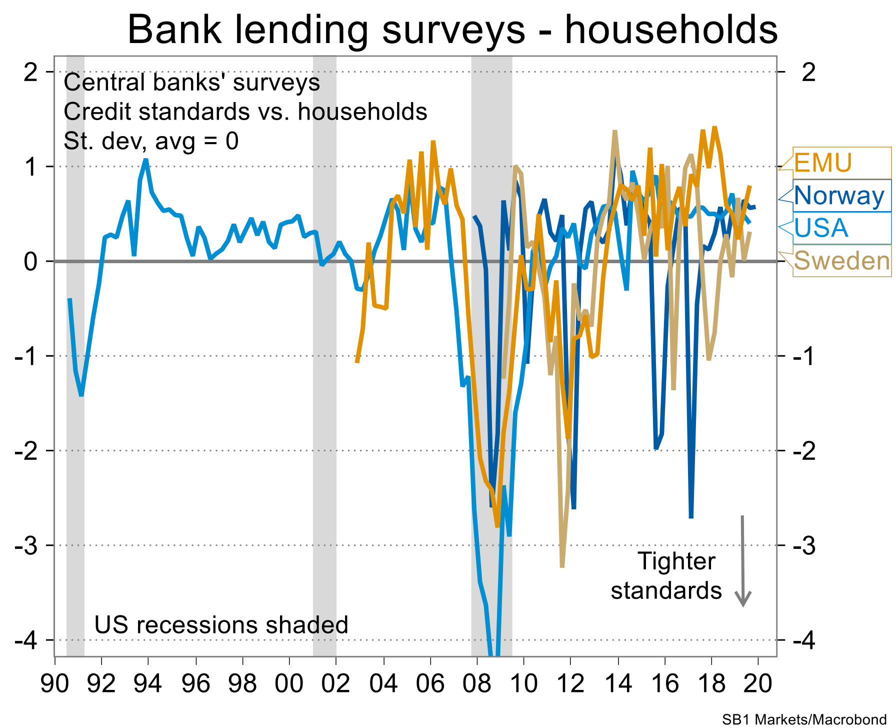


- Banks reported close to unchanged loan demand in Q2, slightly weaker than they expected in the previous report. Moreover, banks expect marginally higher demand in Q3, regardless of climbing interest rates
  - » A moderate upswing in the housing market, low unemployment and an overall solid economy are probably offsetting the negative effects on demand from higher interest rates. Effects from the Sept hike have not materialized in mortgage rates yet, though many banks have announced hikes
- Actual credit growth from households is sliding slowly down and m/m growth was softer than 'usual' in July/August (no Sept data yet). The lending survey pointing to an upturn in credit growth, however, the precision is not impressive. We highly doubt credit will accelerate now,

Global view: Credit easing most places vs both corporates & households

But banks are becoming a tad less upbeat vs. the corporate sector, and Swedish banks to cut lending?

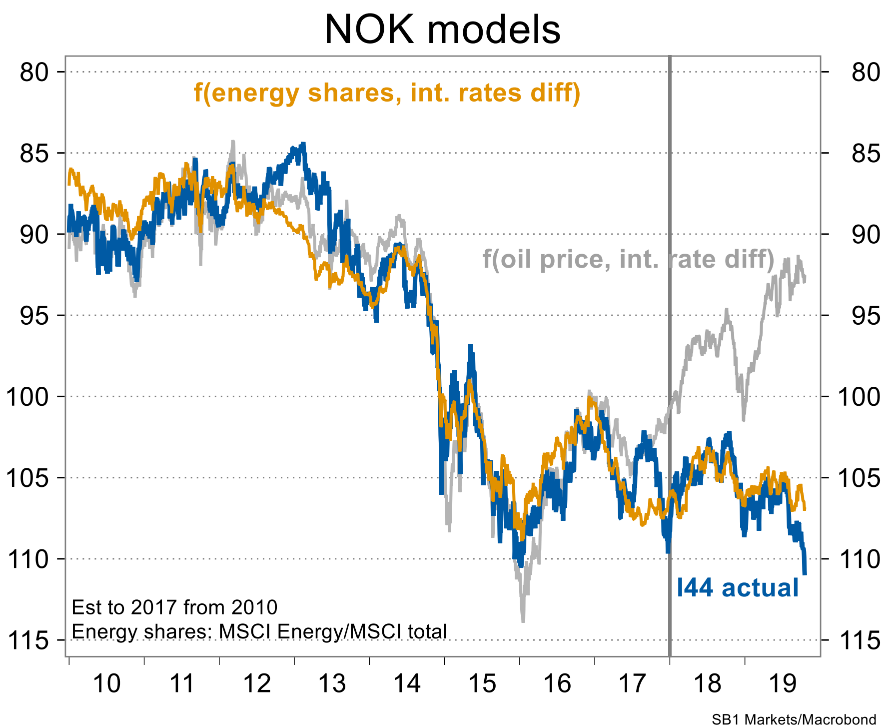


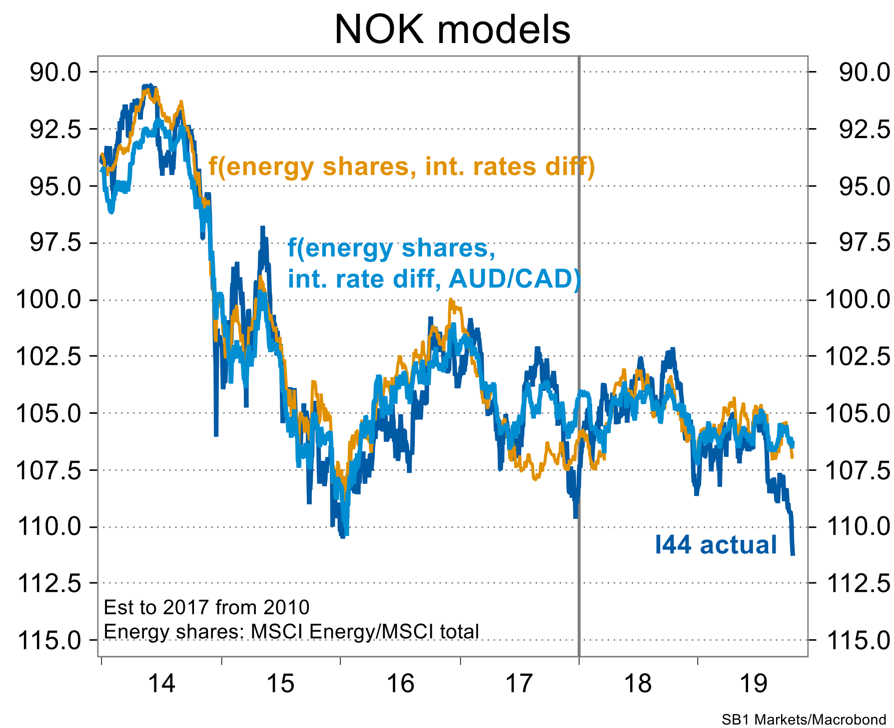


- Credit standards implemented on corporates have eased most places, although standards on both US and Eurozone corporations are less loose than they were in 2018. Norwegian banks have been loosening standards vs corporations the past year. Swedish banks are planning to pull back lending (not standards)
- Banks are reporting easing credit standards vs households in both the US and the Eurozone, and marginally in Sweden. Standards in Norway have eased too, after the implementations of new mortgage regulations in 2017

NOK hit by the green wave, like the oil industry?

Our old short term behavioural f/x model has not worked well past two years. Why? The green shift?

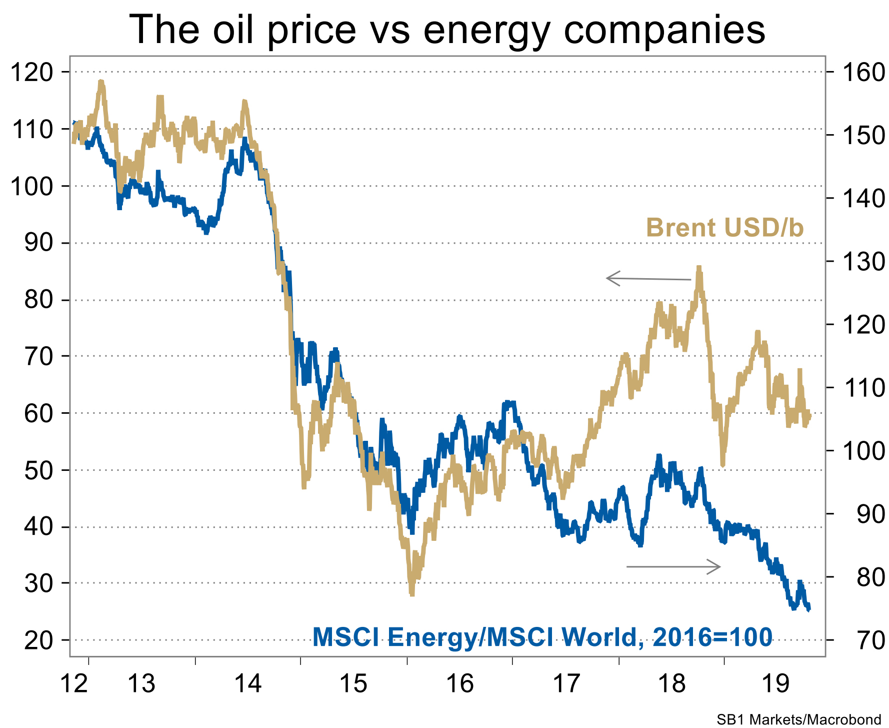


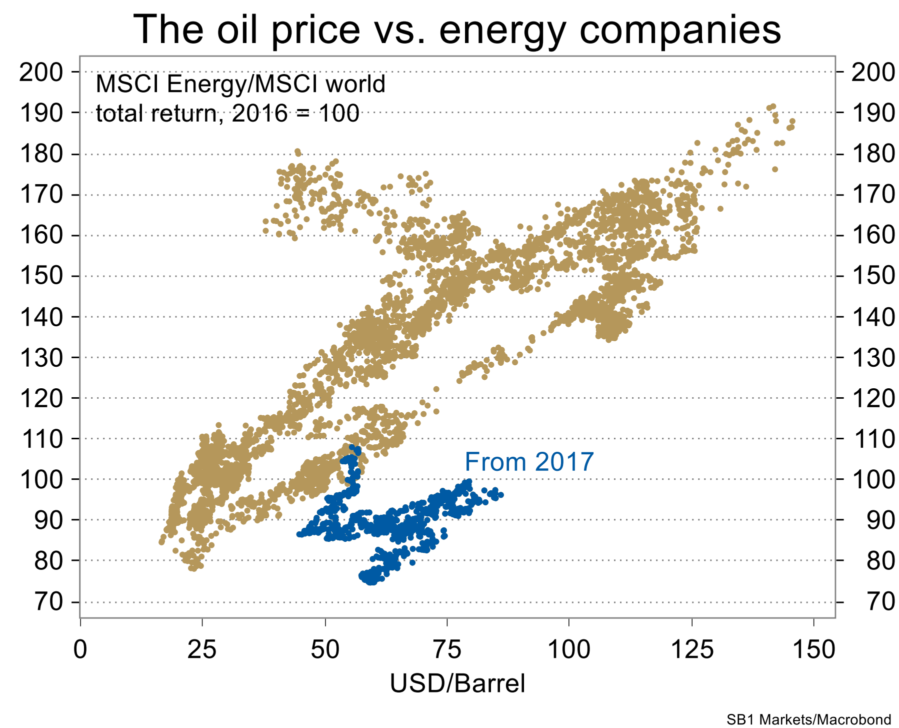


- The first step: We have swapped the oil price with the market's pricing of oil assets, measured by the relative return for energy shares vs the total market in the NOK f/x model. Until 2017 it did not matter which 'oil' variable we applied, they explained the NOK equally well. When forecasting the NOK, by using the model parameters estimated 2010 – 2017 (including the 2y interest swap rate spread vs. trading partners), the deviation is startling. The energy share model explains the actual NOK way better than the oil price model. The residual is 4%, compared to the 15% gap vs. a simple oil price model (or 10% in our augmented oil price model). The market judges the Norwegian economy as it judges oil companies, and has lost the long term confidence in both. And not because of greenwashing, but out of real concerns for the future for oil/gas producers. We think the market puts too much weight on the oil sector's importance on the oil sector, but that's another debate. *Check next page for energy companies vs. the oil price*
- If we include AUD and CAD in the model, the forecast model works even better. Both Australia and Canada are energy net exporters (Aust. coal, Canada oil/gas). Their energy exports equals some 5% of their GDPs vs 12-15% for Norway. Even a NOK model with just AUD and CAD (and SEK, but just to please our neighbours) as explanatory variables, works far better over the past 2 years than the oil price/int. rate differential model
  - » However, both the model with the relative return of energy shares and the one including AUD and CAD fail to explain the NOK weakness since late July. NOK is 4% too weak

ESG: Oil companies have fallen out of favour – and are cheap vs. the oil price

The relative pricing of oil companies have been quite closely correlated to the oil price

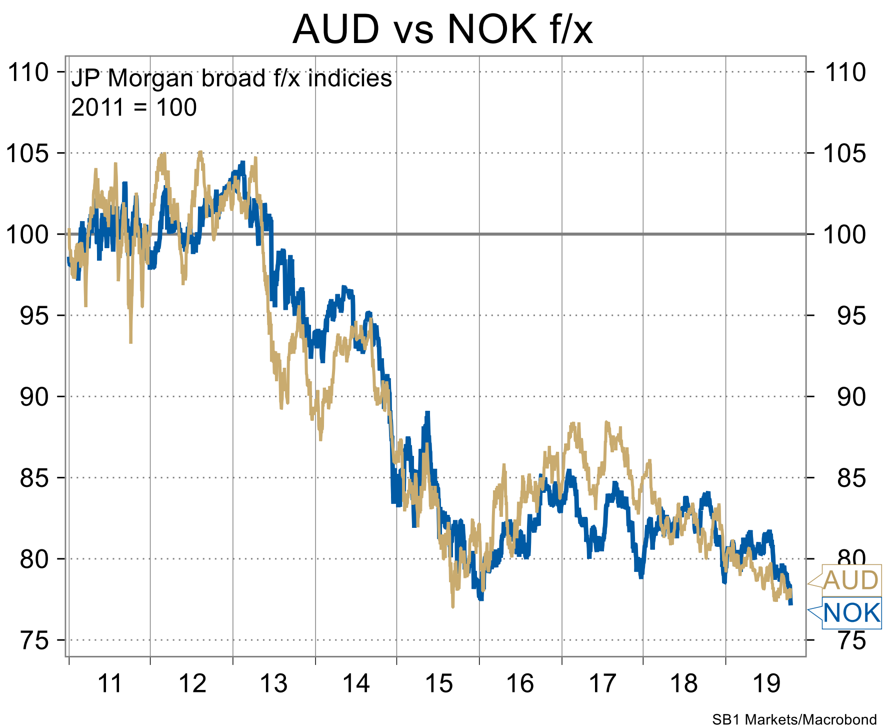


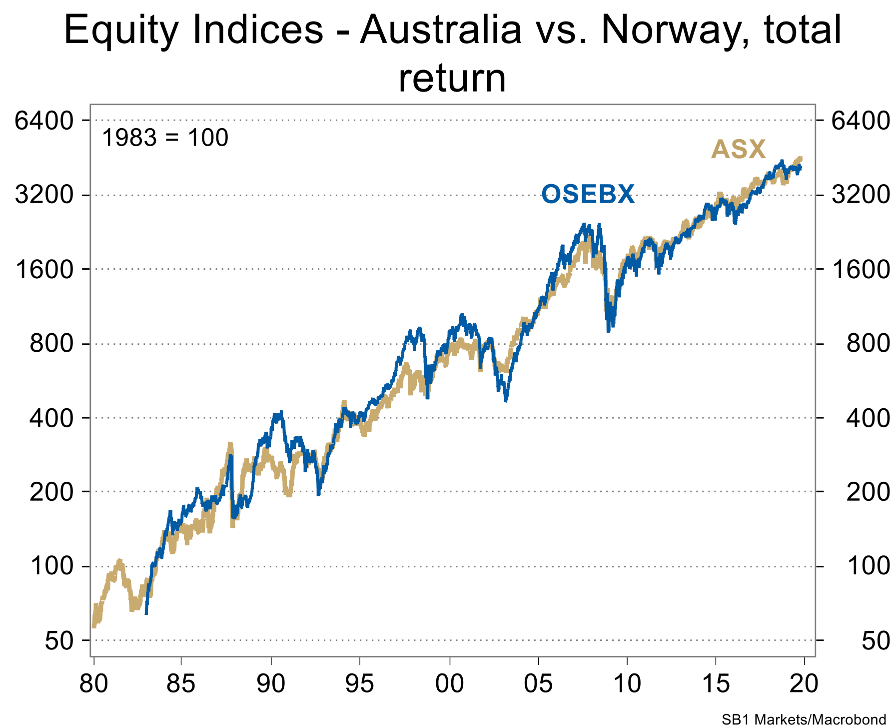


- They still are, but just after a shift down in the pricing of oil companies vs. the oil price during 2017 and ‘18, down approx 30% vs rest of the stock market

.. Or make it even simpler: Just check NOK vs the Aussie!

The same goes for the Oslo Stock Exchange vs Sydney, of course





- Australia has cut rates, Norway has hiked. Does not matter at all, it seems like, vs their currencies

Our main views

	Main scenario	Recent key data points
Global growth cycle	The cycle is maturing, in the real economy, markets, and the trade conflict is now doubt a factor behind the recent slowdown, especially in the manufacturing sector. 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 EMs 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. Investment rates are not far too high, few debt bubbles this time. **Still, growth has slowed to 3% from 4%, and we expect a further slowdown to 2.5% in 2020, even if trade conflicts are 'solved'. If ramped up, more downside risk**	The global composite PMI inched down just 0.1 p in Sept, to 51.2. The level points to some 3% GDP growth, as during the previous quarters. Global manuf. PMI has stabilised but remains weak and actual prod. remains sluggish while retail sales are slowly cooling
China	The governments' stimulus measures may have stabilised the economy, and surveys and data do not point to a hard downturn (rather, a stabilization recent months). 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/world hegemony war will hurt the Chinese economy**	Sept data in sum OK. Q3 GDP rose 6.1% q/q ann, as f'casted, growth is slowing but very slowly. Manuf. production rose more than expected, retail in line with exp, both have more or less stabilized recently. Investments are slowing just marginally. Housing starts up
USA	Growth has slowed, from well above trend. The employment rate is still trending up, and unemployment down, but wage growth is not accelerating. Price inflation is just marg. below target. No serious overinvestments but most sectors at/above trend and corporate debt is high. Business investments have weakened amid weaker growth in profits and trade war uncertainty. Recent consumption data are solid but may now be softening (and partly funded by lower, although still high savings). Housing mostly positive. Fiscal stimulus continues but not by much. The deficit is far, far too high, given the low unemployment rate. Recession risk is increasing, but still not overwhelming, short term. **Risks: Trump/trade/business investments**	Upbeat housing market data, both starts and the HMI are climbing. Retail sales fell in Sept, Q3 was anyway solid. Manufacturing production has stabilized, surveys point to a decline. Fed's Beige Book notes a weaker growth momentum but still very tight labour markets
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 are above trend. Credit growth is accelerating, but still muted. Household savings are high, still consumption has kept up well. Policy: ECB has turned dovish but does not have that much ammunition left, barring a huge QE, and the ECB policy makers are split. 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**	Industrial production recovered softly in Aug, up 0,4%. Production is anyway contracting, led by Germany, and the outlook is bleak. Weak German ZEW survey in October
Norway	Growth is still above trend but may soon be peaking. Unempl. is still declining, although at a slower pace. Wage inflation is accelerating. Oil investments are peaking in H2. Mainland business inv. not low anymore, will probably slow in '20. Mixed signals from the housing market, starts probably slowing. Electr. prices have taken the headline CPI down but core still slightly above target. Credit growth slowing (households) still above income growth, is spite of heavy regulations. **Risks: Debt, housing. A harsh global slowdown**	Norges Bank's lending survey notes an uptick in household loan demand, in spite higher interest rates. We doubt growth will accelerate. The trade deficit widened in Sept, will most likely be a drag on Q3 GDP growth

SpareBank 1 MARKETS

The Calendar

In focus: The first October PMIs, US housing market, ECB and Riksbank monetary policy meetings

Time	Country	Indicator	Period	Forecast	Prior
TBA	US	Monthly Budget Statement	Sep	$83.0b	$119.1b
Monday Oct 21					
03:30	CH	New Home Prices MoM	Sep	--	0.6%
03:30	CH	1-Year Loan Prime Rate	Oct	4.15%	4.20%
06:30	JN	All Industry Activity Index MoM	Aug	0.1%	0.2%
08:00	NO	SSB Industrial Confidence Survey	3Q	--	5.6
08:00	NO	Housing Permits	Sep		32'
10:00	NO	Homebuilders' Survey	Sep		17'
Tuesday Oct 22					
12:00	UK	CBI Trends Total Orders	Oct	-25	-28
16:00	US	Existing Home Sales	Sep	5.45m	5.49m
Wednesday Oct 23					
16:00	EC	Consumer Confidence	Oct A	-6.7	-6.5
Thursday Oct 24					
02:30	JN	PMI Composite	Oct P	--	51.5
08:00	NO	Unemployment Rate, LFS	Aug	(3.7%)3.7	3.8%
09:30	SW	Riksbank Interest Rate	Oct-24	-0.25%	-0.25%
10:00	NO	Norges Bank Interest Rate	Oct-24	(1.5)1.5%	1.50%
10:00	EC	Manufacturing PMI	Oct P	46	45.7
10:00	EC	Services PMI	Oct P	51.9	51.6
10:00	EC	Composite PMI	Oct P	50.4	50.1
13:45	EC	ECB Deposit Facility Rate	Oct-24	-0.5%	-0.5%
14:30	US	Durable Goods Orders	Sep P	-0.5%	0.2%
14:30	US	Capital Goods Orders Core	Sep P	-0.1%	-0.4%
14:30	US	Initial Jobless Claims	Oct-19	216k	214k
15:45	US	Markit Manufacturing PMI	Oct P	50.7	51.1
15:45	US	Markit Services PMI	Oct P	51	50.9
15:45	US	Markit Composite PMI	Oct P	--	51
16:00	US	New Home Sales	Sep	710k	713k
Friday Oct 25					
09:30	SW	Retail Sales MoM	Sep	0.5%	0.0%
10:00	GE	IFO Expectations	Oct	91	90.8
16:00	US	UoM Consumer Sentiment	Oct F	96	96

- **Preliminary October PMIs (US, EMU, Japan)**
  - **The global PMI** has stabilized at just above 51 since early summer, confirming that the global economy has lost momentum, however, the downturn has not accelerated recent months. In Sept, there were some signs that the manufacturing weakness may now be spilling over to the service sector
- **US**
  - Both **new home sales** and **existing home sales** are soaring, buoyed by low mortgage rates. Still, the risks are now skewed to the downside, if not in Sept
  - **Durable goods orders** and **capital orders** are sluggish and point to a slight decline in business investments in Q3, as in Q2
- **EMU**
  - Mario Draghi leaves a deeply divided **ECB** at his last monetary policy meeting. We expect no changes following the massive stimulus package announced in Sept. Christine Lagarde will probably largely follow the course set by Draghi
  - **Consumer confidence** remains elevated, stressing the persistent divergence between manufacturing and services
- **Sweden**
  - In Sept, the **Riksbank** surprised by sticking to its plans to hike the interest rate to 0 in Q4/Q1. Our take is that labour market weakness, inflation below target and persistent global uncertainties will scupper the bank's hiking plans
- **Norway**
  - **LFS unemployment** has ticked up due to a lift in labour market participation. We expect unemployment to edged back down the coming months
  - **SSB's industrial confidence** slides slowly down, with other business surveys
  - **Housing starts** are most likely turning down from the peak, although data are somewhat conflicting. We f'cast SSB's starts to follow the Homebuilders down

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

SpareBank 1 MARKETS

In this report

Global

- Global macro data somewhat more downbeat
- Retail sales, manufacturing production slows; global trade declines

China

- GDP growth is slowing but quite slowly
- Industrial production bounced back in Sept, trend slowly down
- Retail sales volume growth steady in Sept, no collapse in domestic demand
- Nominal investments are slowing just marginally
- Bank lending gains pace, supported by easing policy?
- Total inflation accelerated to 3%, core CPI steady

USA

- Fed's Beige Book reports slower growth but still very tight labour market
- Manufacturing production stabilized in Q3 but the outlook is gloomy
- Retail sales soared in Q3 but growth is slowly losing steam
- Housing permits remained very strong, volatile starts back to a 'normal' level
- Jobless claims another remains very low, no signs of weakness yet
- The Leading indicators retreated in August, following July spike
- Nowcasters are signalling some 2% growth in Q3 as well

EMU

- Industrial production rebounds softly in August, trend straight down
- ZEW survey expectations steady in October, view of the current sit. weakens

UK

- Core CPI inflation recovered but just to 1.7%, trend tilting downwards?
- Unemployment rose, employm. fell; Brexit slowdown hitting the labour market?
- Retail sales still growing above trend

Sweden

- Unemployment is soaring but the upturn has been overestimated
- Employment is no doubt slowing but not as steeply as reported
- House prices jumped in Sept, trending moderately upwards

Japan

- Core CPI inflation is turning very slowly up

Norway

- Banks expect higher household loan demand in spite interest rate hikes
- Imports soared in Sept, net trade most likely a drag on Q3 growth

Highlights

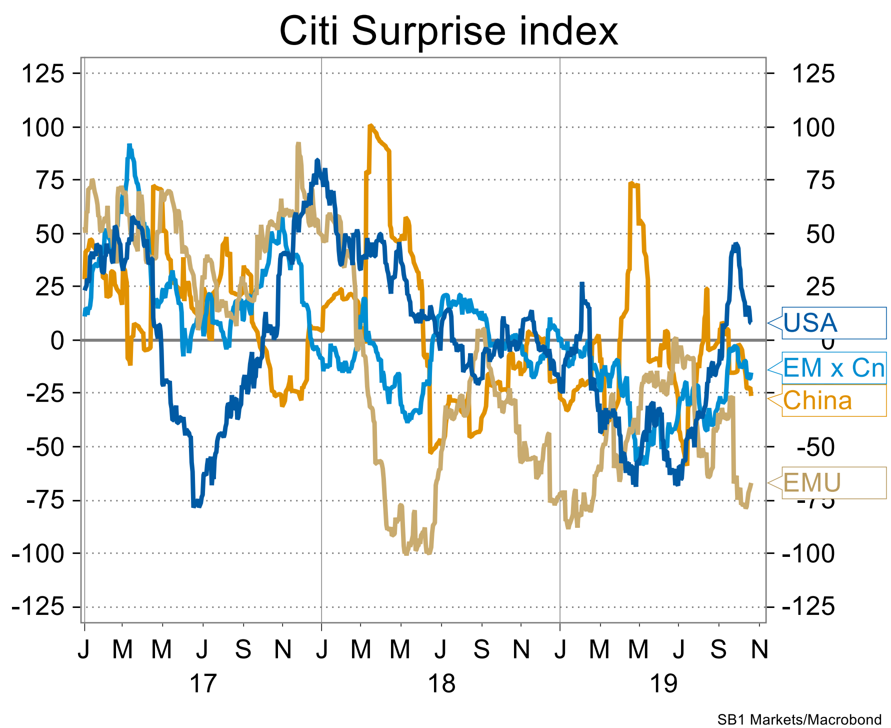
The world around us

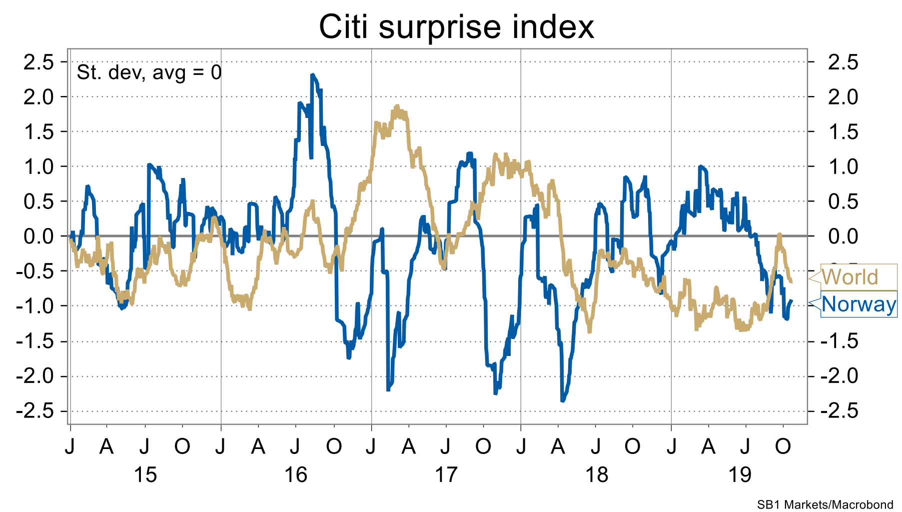
The Norwegian economy

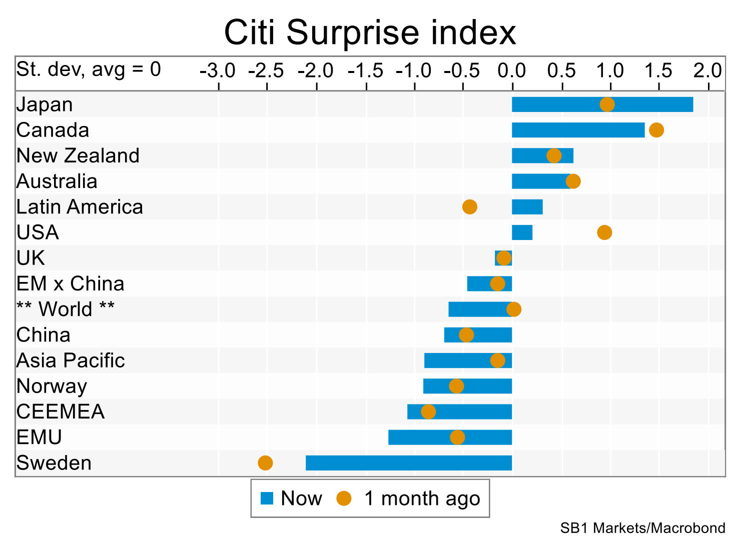
Market charts & comments

Global macro data somewhat more downbeat, again

Less positive news from US and weak EMU data have sent the global index down from 'neutral'







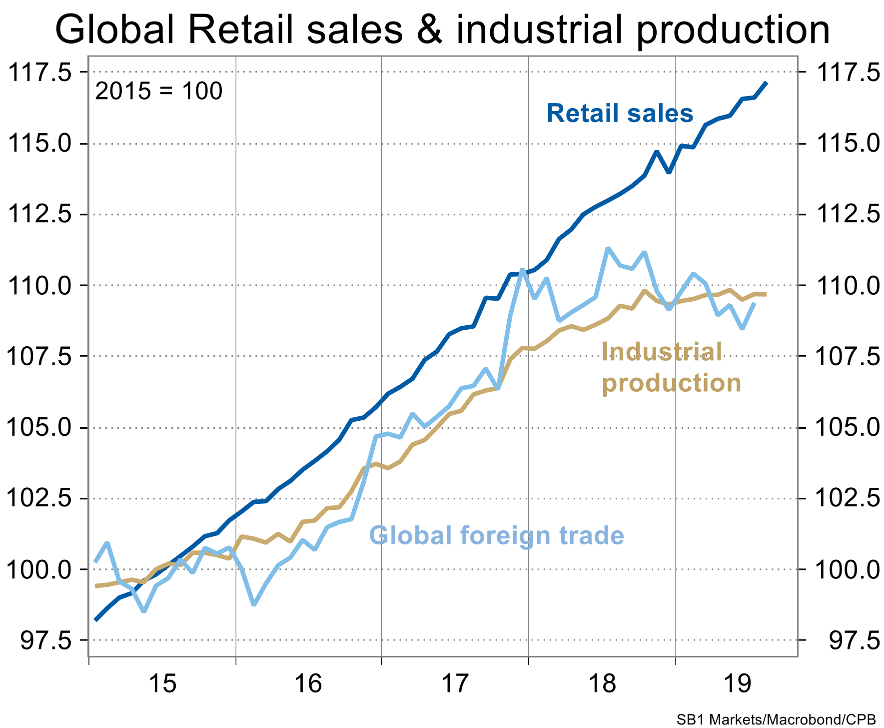
- The global surprise index climbed to a 'neutral' level for the first time this year in mid-Sept. Since then, data have been slightly more disappointing, in sum
- US data flows have been beating expectations the past month, however, much less the past 3 months. ISM, retail sales, job openings and PPI inflation have sent the index down
- EMU data have been most disappointing since early 2019, pulled down by weak PMIs
- China sliding down again, along with other EMs
- Norwegian data are slightly more disappointing than the world in general, we are not sure we agree

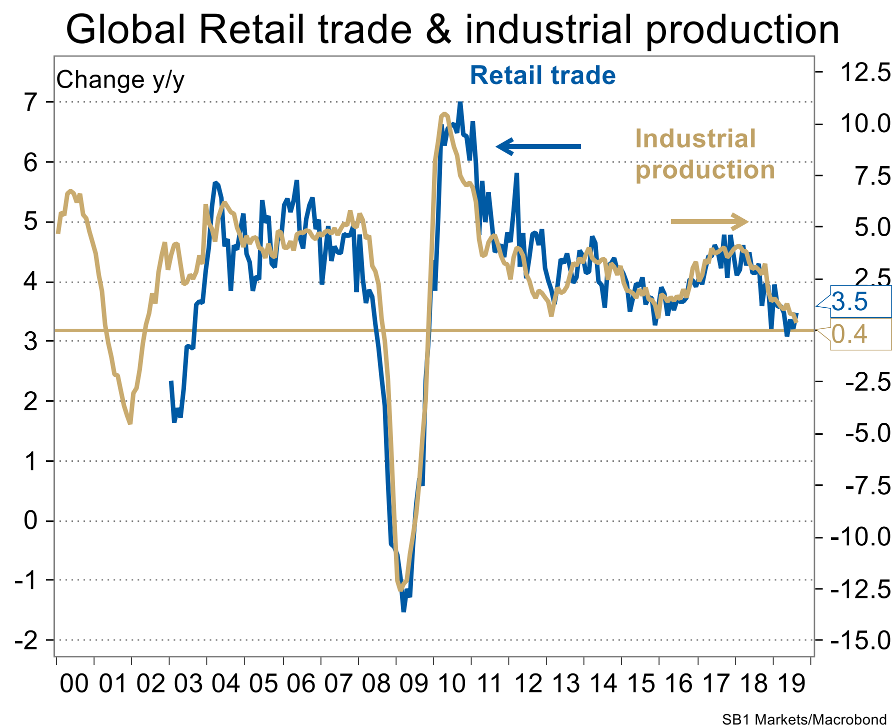
Surprise-indices measure the difference between economists' expectations and the actual outcome over a 3 month rolling window

SpareBank 1 MARKETS

Retail sales, manufacturing production slows; global trade declines

Global trade flows rose in July but are no doubt heading down. Manufacturing production stalls





- **Global industrial production** most likely inched up some 0.1% m/m in Aug (our prelim. estimate). The overall trend is no better than just marginally upwards, growth has slowed substantially. Global business surveys signal a modest decline
- **Retail sales** increased by 0.5% m/m in August, based on our estimate. Growth has come down, more or less in tandem with manufacturing production (given the normal correlation between the two, retail sales are less volatile than retail sales). Even so, consumption is still supporting the global economy
- **Global foreign trade** increased by 0.9% m/m in July (with our seasonal adjustment) but the decline in June was more abrupt than previously reported, down 0.8% m/m vs 0.5%. Trade flows are trending down, at a 2% pace since last summer, as trade uncertainties curb demand. The slowdown is rather broad based, Emerging Asia ex China and Lat. Am and Africa are the weakest links in the chain

Growth is slowing but there are some signs of stabilization

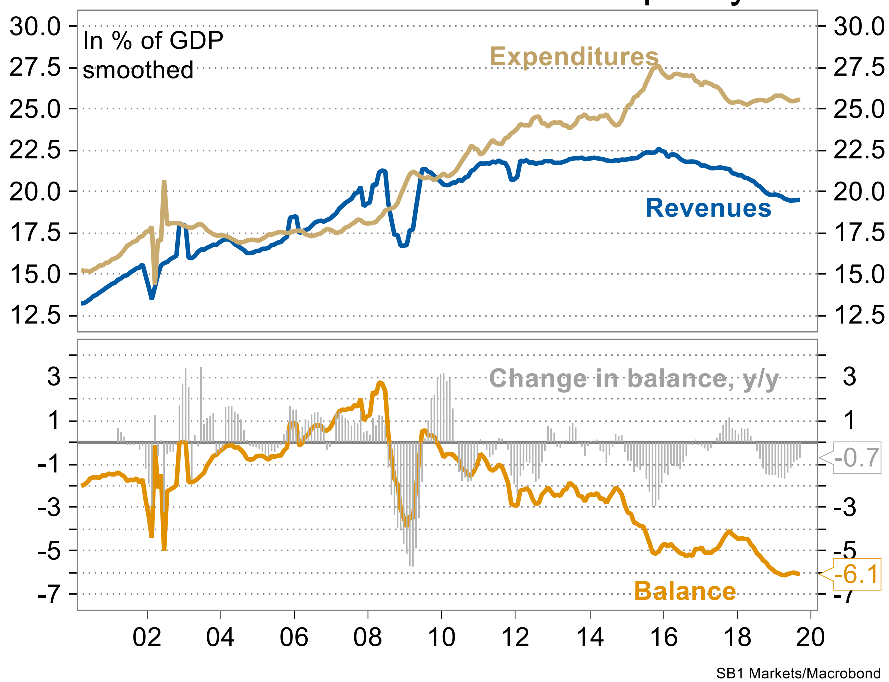
September/Q3 broadly in line with expectations, no signs of a sharp slowdown

- **Growth is slowing amid persistent trade war uncertainties and slowing domestic demand – but data are not at all signalling any abrupt setback**
- **GDP** rose by 1.5% q/q (6.1% annualized) in Q3, in line with expectations. Yet, the annual rate came in 0.1 pp weaker than expected, at 6.0%, from 6.2% in Q2. The details were broadly unchanged from Q2; consumption and investments are both slowly slowing, while higher net exports are fuelling growth
- **Industrial production** bounced back in Sept, up 0.7% m/m, following two soft months. The official y/y rate spiked to 5.8%, well above expectations, while our less volatile calculation yields a 6.0% speed (up from 5.7%). Growth is slowly easing, yet at a slower pace this year. PMIs are indicating an upswing
- **Investments** have been expanding steadily and growth is slowing just marginally over the past 2 years. The annual rate has inched down to 5.2% (while the more volatile YTD rate fell to 5.4%). Nominal investments are still growing slower than GDP, real growth is strengthening and has come up to some 3%
- **Retail sales** growth was unchanged at 6.1% according to our volume estimate but growth has slowed during 2019, as during the previous years (excl. 2018). The retail sales data are often revised substantially, yet data at hand do not signal any setback in domestic demand
- **Credit growth** has been slowly accelerating recent months, helped by bank lending. The credit impulse is marginally positive, following the 2018 contraction

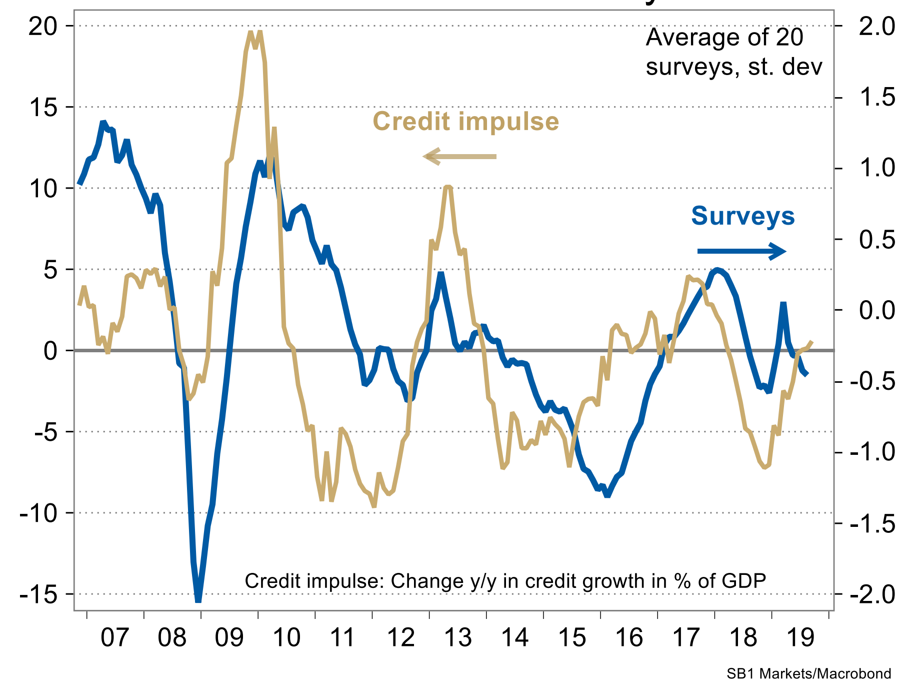
Growth is gradually slowing even if policies try to stimulate

Budget deficit at 6.1% of GDP, +0.7 pp last year. In addition: A modest credit turnaround

China Government - fiscal policy



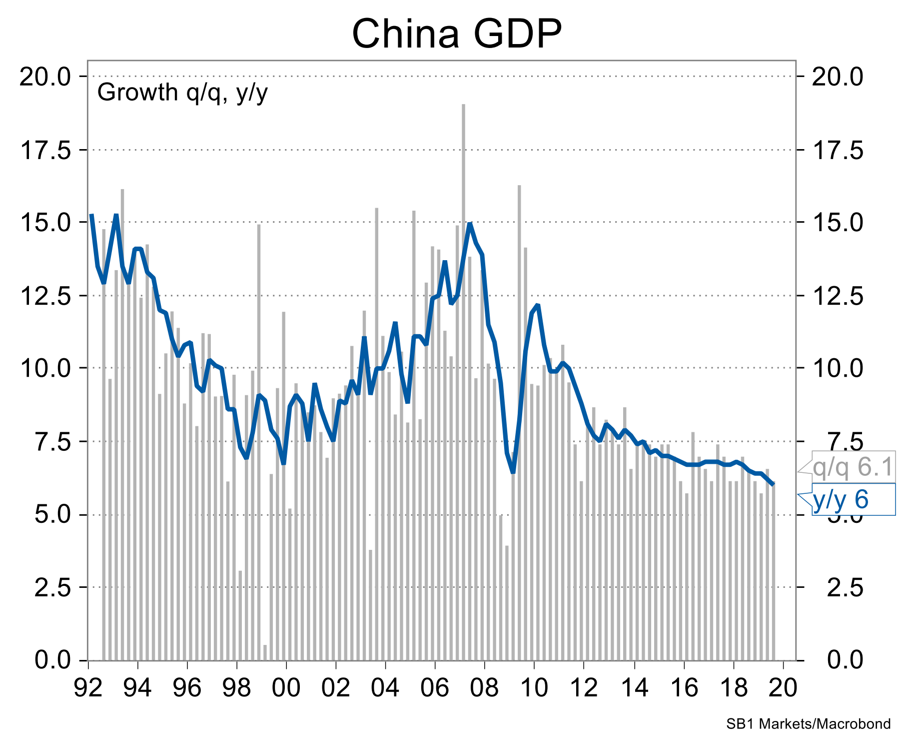
China Credit vs. surveys



- Fiscal policy: Taxes are cut, spending programs decided. Over the past year, the deficit has increased by 0.7% of GDP, a substantial fiscal expansion – but it is slowly petering out, as spending declining marginally (in % of GDP). The deficit has increased to 6.1% of GDP, according to our calculations
- Credit growth is slowly accelerating (more here), and the credit impulse has turned marginally positive (measured y/y, positive 'now'), from sharply negative
- CNY has depreciated 10% since 2015, of which 5% since May (and 2.5 % since early August)

GDP growth is slowing but quite slowly

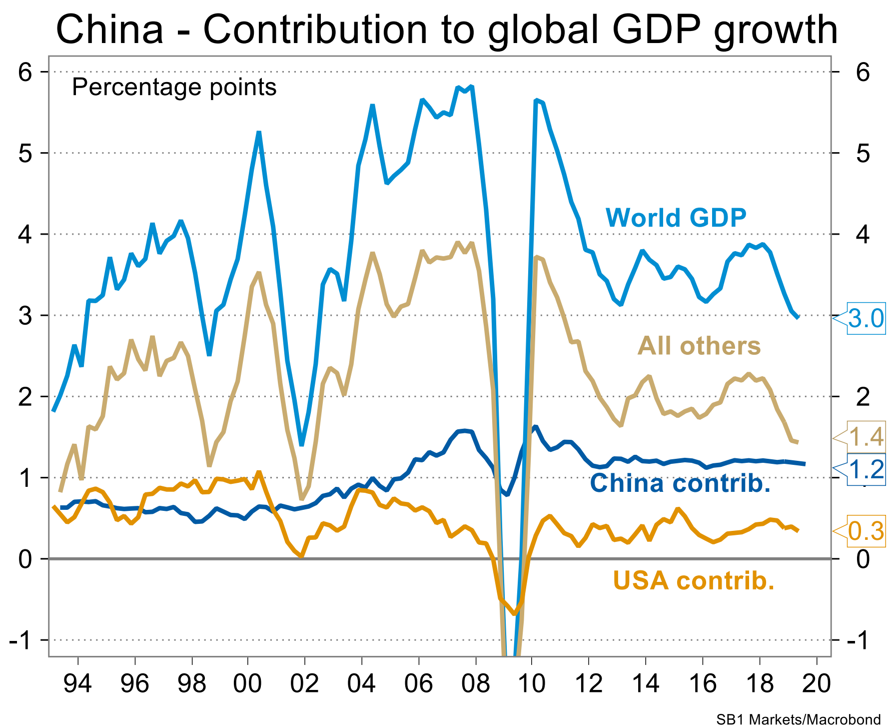
Growth is slowing a tad faster than over the previous years, now by 0.5 pp per year



- GDP grew 6.0% y/y in Q3, down 0.2% from Q2, 0.1 pp weaker than expected. The annual growth rate has fallen from 6.8% in Q1 last year, and is the lowest y/y growth rate on record (quarterly data back to 1992).
  - » GDP grew 1.5% (6.1% annualised) in Q3, down from 1.7% (6.6%) in Q2, as expected. (Quarterly data do not add up to annual growth rates, but that's another story)
- Big picture: Growth is slowing but at a modest pace. The authorities' 2019 growth target is 6 - 6½%. If annual growth slows to 5.9% in Q4, average 2019 growth will 6.1%, close to the lower range. Nominal growth is slowing faster than real growth
- Are the official GDP reliable? Goods research suggests that growth is some 2pp lower than reported, mostly due to a much slower growth in investments

What a Chinese blow to the global economy!

Well, please check the facts too (as usual)



Chinese economy

Slowing Chinese growth delivers blow to global economy

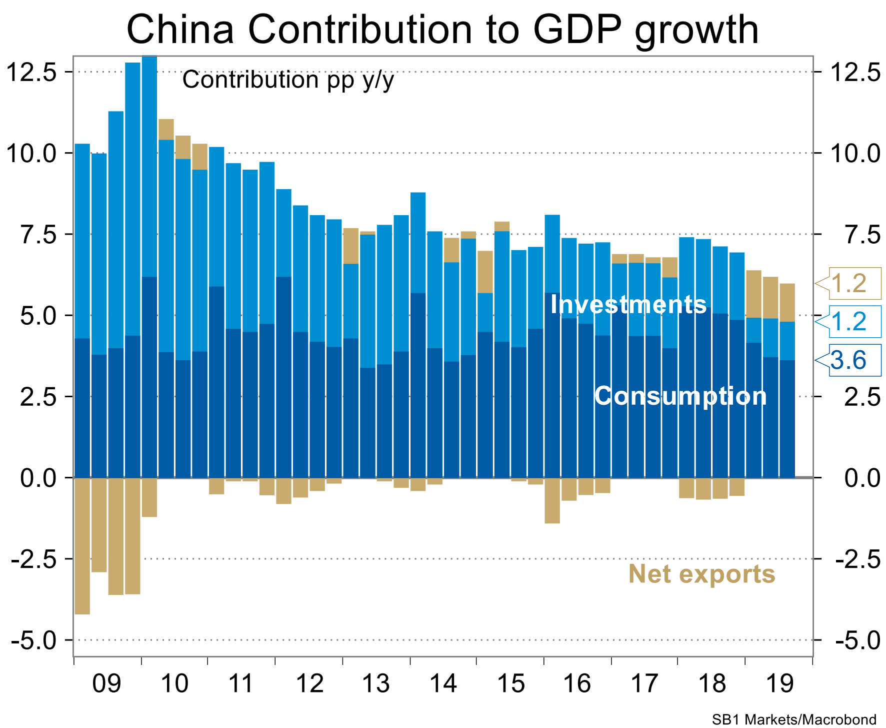
Expansion of 6% is worst in three decades due to trade war with US and cooling investment

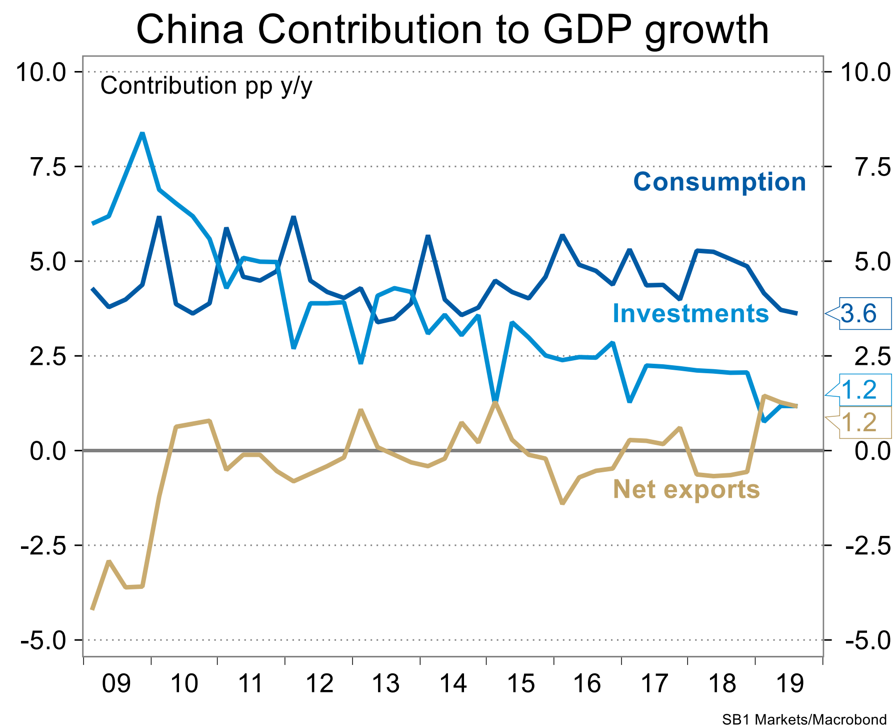
- European auto stocks in reverse while China's growth disappoints
- Chinese local government funds run out of projects to back
- IMF slashes global growth forecast on trade war fears

Top, front page
Fin Times, Oct 18

Growth in investments contributes less and less - consumption too

.. But not further in Q3. Net exports contributed positively in Q3, as in Q1/Q2

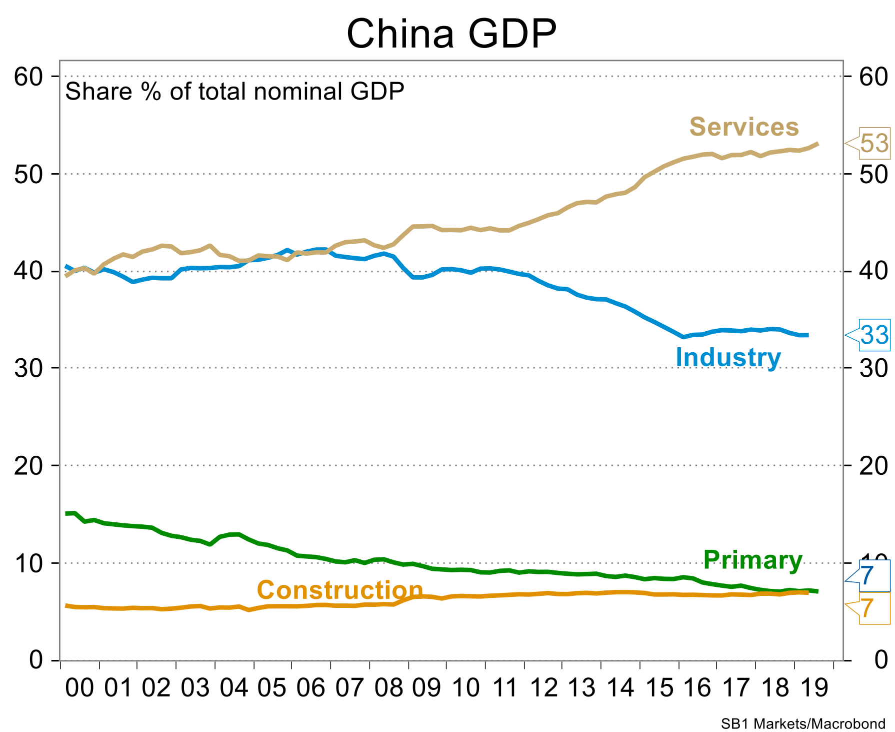




- In the Nat. accounts, net exports contributed to 1.2 pp GDP growth from Q3 last year. Net trade has in average been marginally negative since 2011. Not easy to identify any direct impact of the trade war. The slowdown in GDP growth is domestically driven
  - According to trade data (our volume calc), exports rose 2% q/q in 3Q (annualised) in while imports fell 3%
- Consumption (private & public) contributed to 3.6 pp growth in Q3, a tad lower than in Q3 but sharply down from 2018 (above 5%)
- Growth in investments (private & public) is slowing, measured as contribution to growth according to Nat. Accounts, now just supporting GDP growth by 1.2% (implying a growth rate at some 3%, down from 5% two years ago – and much higher some years ago. However the slowdown is very gradual, and we assume in line with the authorities' ambitions in order to get the investment ratio further down to reduce the risk for heavy overinvestments (which still is a substantial risk!) The continued gradual slowdown may now of course be due to the trade war reducing investment appetite

Services are slowing too but less than industry

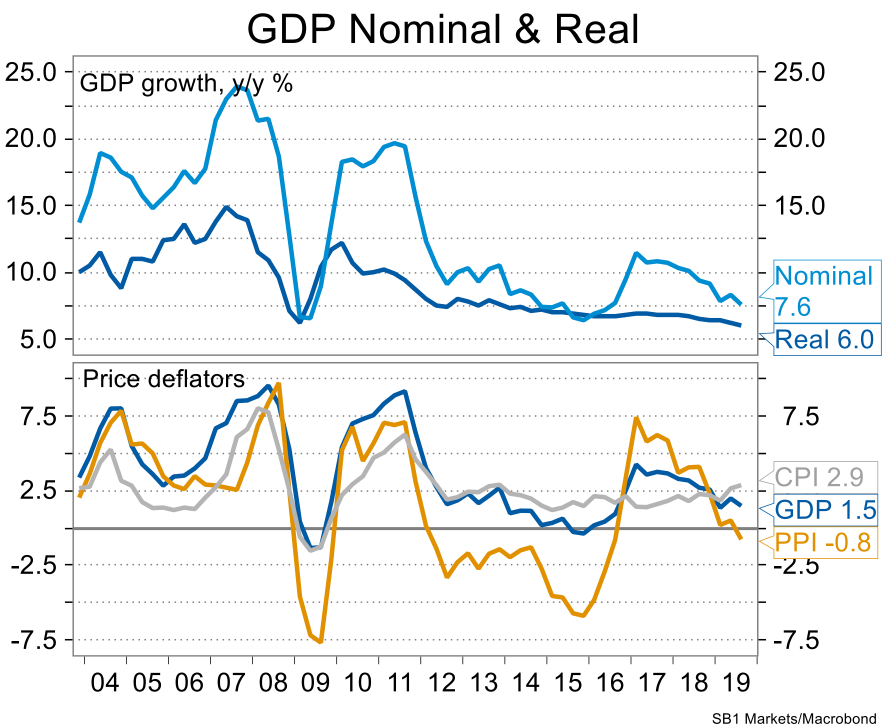
Nominal growth has slowed in the main production sectors



- Services are now contributing to more than 50% of GDP
- No Q3 data for construction, industry

GDP price deflator +1.5%, nominal GDP 7.6 %, both are trending down

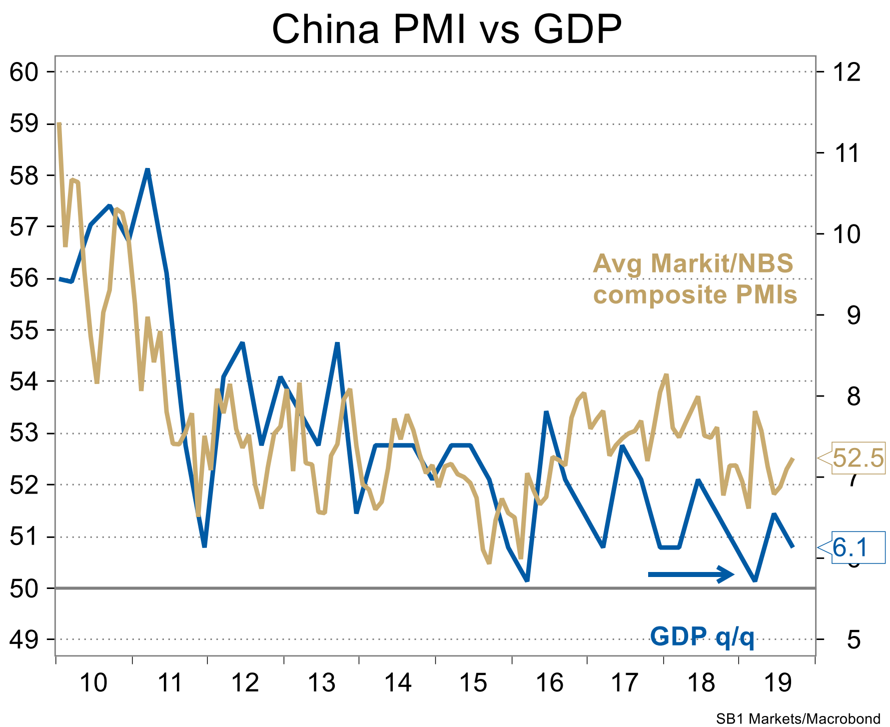
Nominal income growth is still higher than in 2015

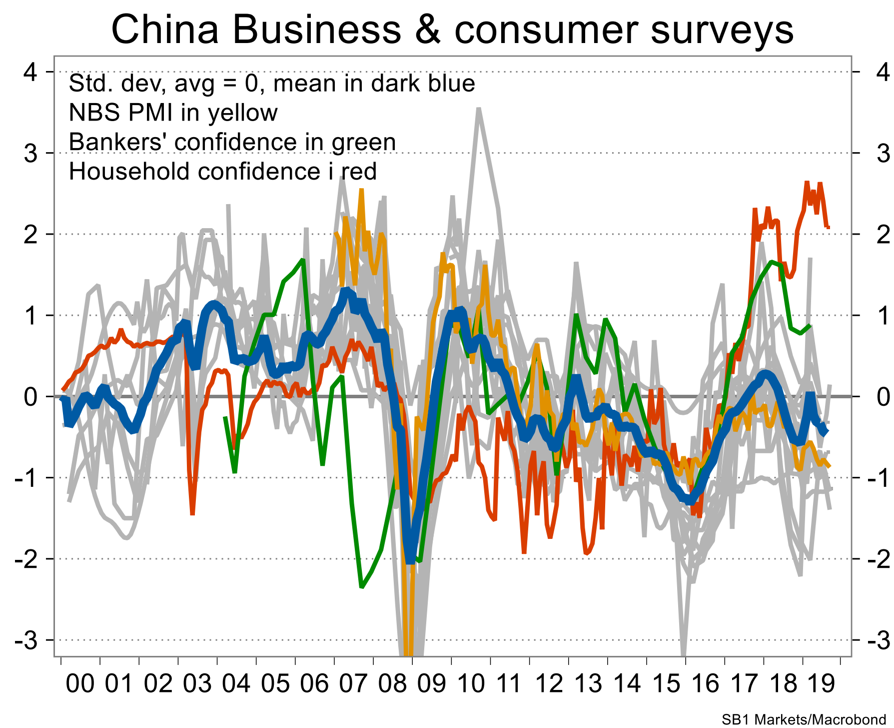


- Manufacturing producer prices (PPI) are down 0.8% y/y, down from above 7% (!) less than 2 years ago. CPI up 2.9% in Q2 in average, up from 1.8% in Q1 – entirely due to higher pork meat prices caused by the serious swine flu

Surveys are not signalling a further growth slowdown

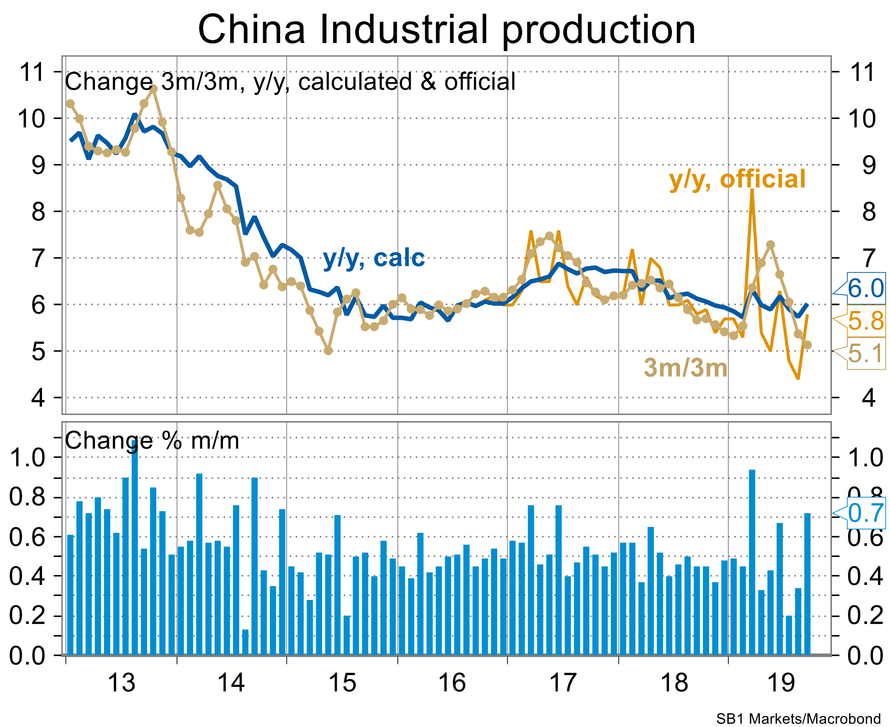
Surveys are in average below par but not by much

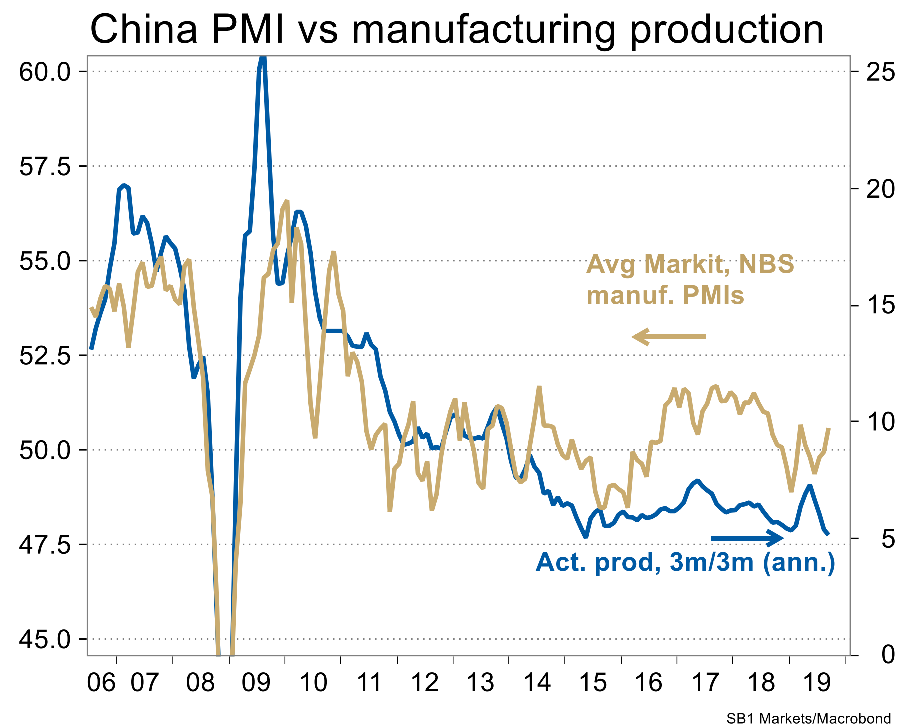




Industrial production bounced back in Sept, trend slowly down

Production jumped 0.7% m/m after two soft months. Our y/y calculation yields 6%, up from 5.7%

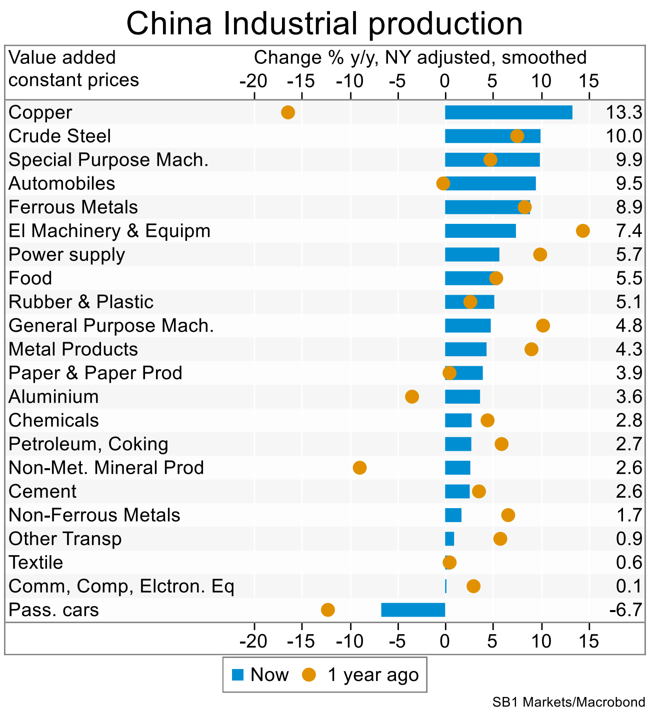




- Production rose 0.7% m/m in September, the highest since March, after muted growth in July/Aug. The 3m average m/m rate is 0.4%, down from 0.5-0.6% in early 2019. Our y/y rate edged up 0.2 pp to 6%, from 5.7%, more or less stabilized since Jan/Feb. Growth slowed in Q3, to 5.1% annualized (vs 6.7% in Q2)
  - » The official y/y growth rate is 'useless', far too volatile as it is not adjusted for holidays or working days. In September, growth soared 1.4 pp (vs our calculated 0.2 pp acceleration) to 5.8% from 4.4% in August (the lowest since 2002) to 5.8%, well above expectations
- PMIs have improved and are pointing to a stabilization in manufacturing activity. Export volumes are trending up and are close a peak levels. China has most likely not been brought to a halt, in fact, the slowdown was more dramatic in 2018 than it has been so far in 2019.

Production is slowing in many sectors but just autos are down y/y

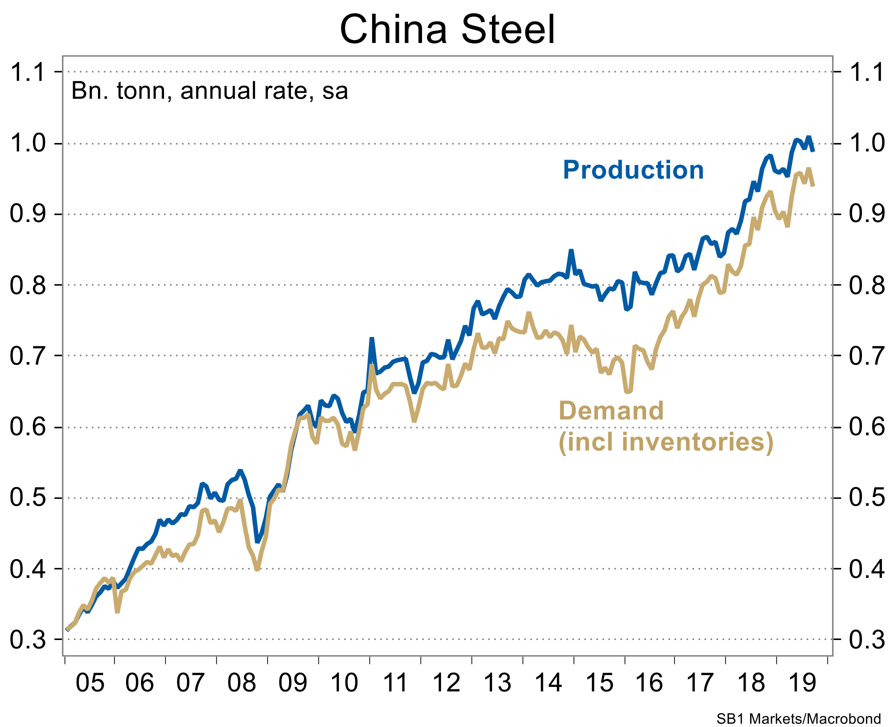
Details are not that weak; 8 sectors are accelerating (vs 1 y ago), 10 are slowing. Auto prod. is falling



- Crude steel production fell in September, and has flattened recent months but is still probably trending up, up 5.4% y/y (3 m smoothed)
- Aluminium production is recovering steadily from the downturn in 2017 and is increasing by 5.2% y/y
- Cement production is slowly climbing, up just 4.8% y/y
- Copper production has recovered sharply in 2019, and is up 13.7% y/y (in August)
- Auto production (valued added) has been hurt by weaker sales and is down 6.7% y/y. Auto sales have fallen steeply, down 20% from the peak. Still, sales have stabilized recent months and are falling 'just' 7.1% y/y (smoothed)

Steel production (and demand) down in Sept, probably still on the way up

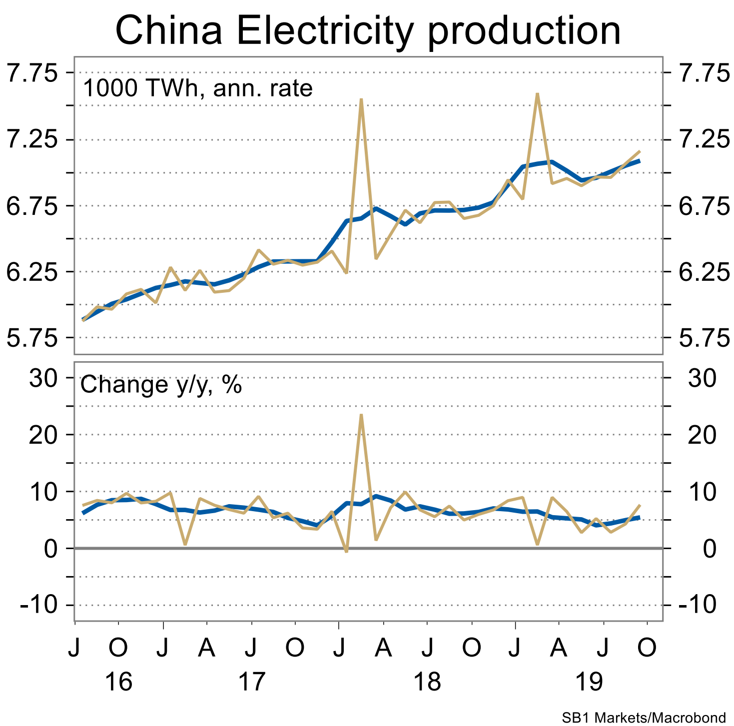
Upward trend intact, after both demand and production softened last winter. Reduced overcapacity

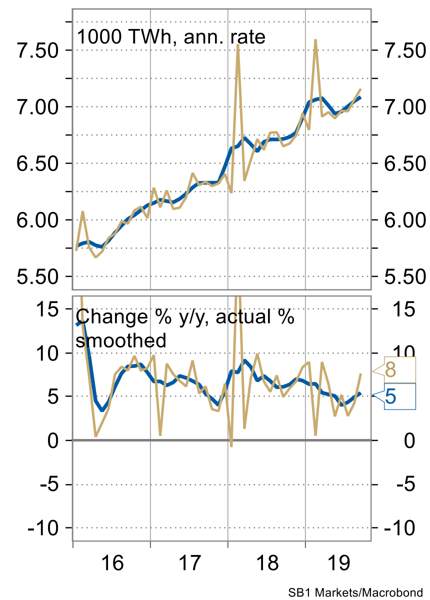


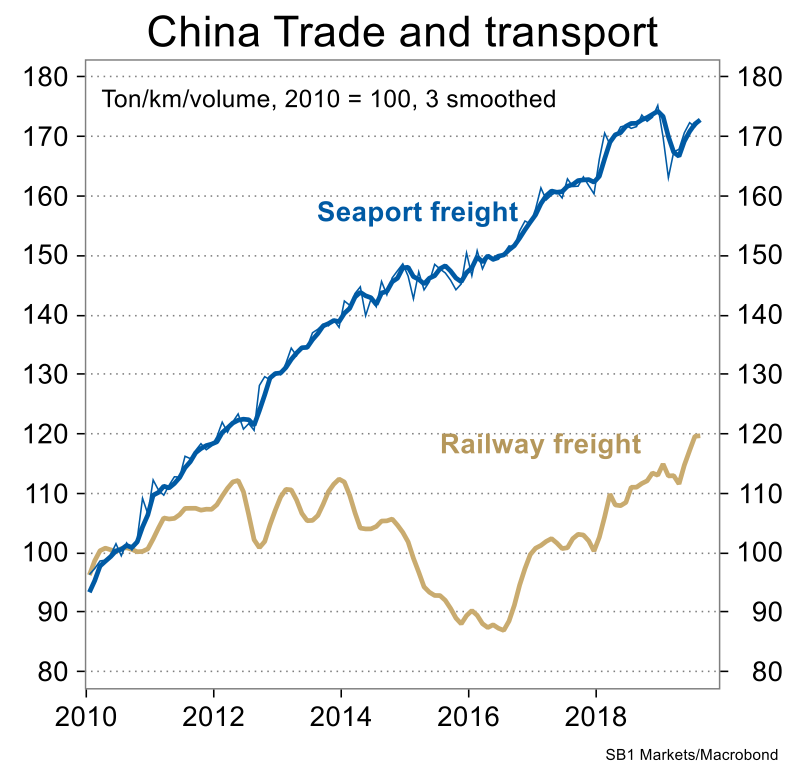
- Production is up some 5% y/y (smoothed) and demand is expanding a tad faster, (almost) well explained by the strong growth in construction starts. On the other hand, slowing auto production signals softening steel demand from that sector
- China is still a net steel exporter, but far less than during the 2015-16 setback in domestic demand. Back then, production was cut by far less than domestic demand and net exports soared. Now, net exports are far lower (and domestic demand closer to production

Electricity production has slowed but up again recent months

Electricity prod. has gained some speed after a slowdown in the spring, trend up, at a 5% y/y pace







- Transport activity (seaports & railway) has recovered recent months, following a setback earlier in 2019

Retail sales volume growth steady in Sept, no collapse in domestic demand

Growth has more or less stabilized the past year, after a setback in 2018. Official y/y rate slides down

- The official value growth rate rose to 7.8% from 7.5% in August, in line with expectations%. Our less volatile value growth estimate (based on monthly seas adj. data) yields 8.1%, up 0.1 pp. Value growth is slowly easing but less so in 2019
- We assume a 0.5% m/m volume growth, the same pace as the prior month. Growth slowed to 5.1% annualized in Q3, dragged down close to zero growth in July. The annual volume rate was unchanged at 6.1%, stabilized since late 2018, even if inflation has accelerated due to the high pork meat prices (which has not lifted the official retail price index, quite strange)
- Consumer confidence is very high and does not point to any demand weakness. Even so, consumption is not thriving, larger tax cuts may be needed to bring consumption growth up

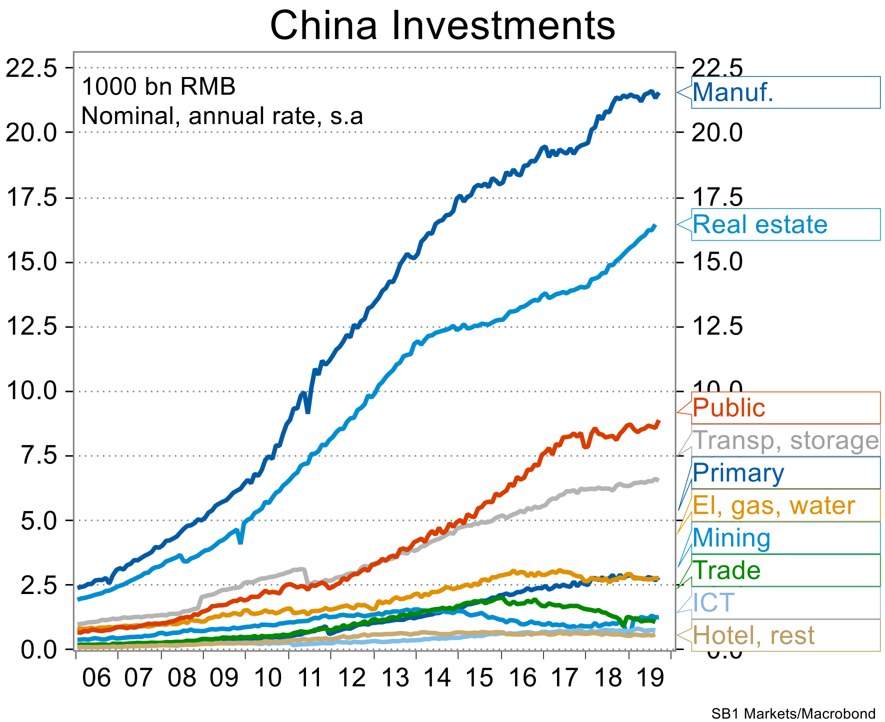
Nominal investments are slowing just marginally

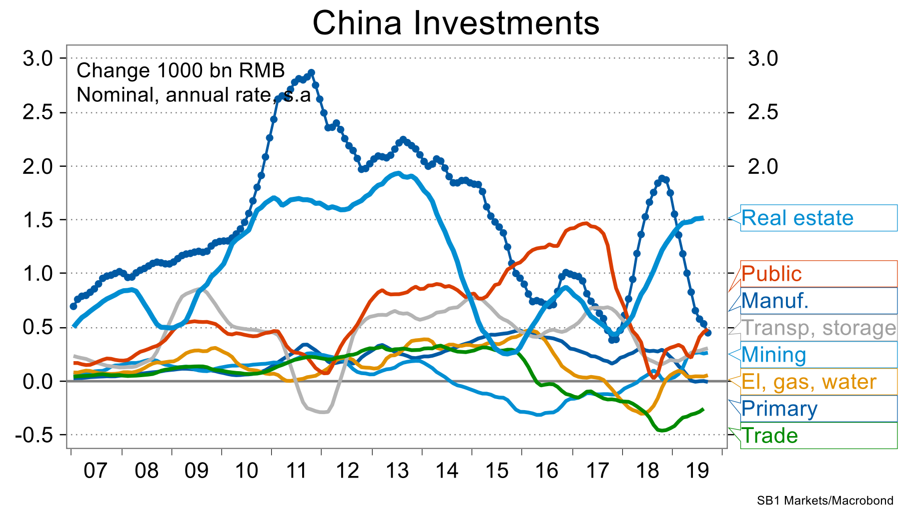
The long term decline in investment growth has halted, at a comfortable, low level

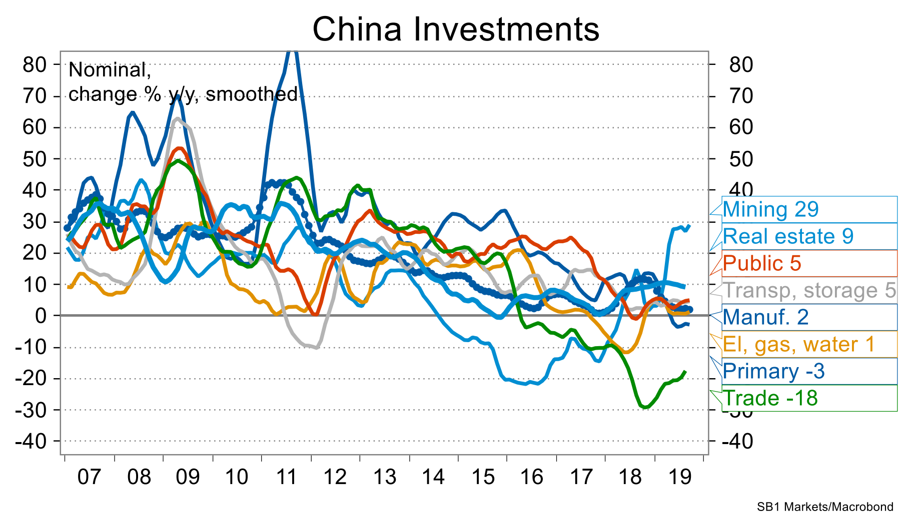
- Urban investments rose 5.4% y/y ytd in September, according to the official data, down from 5.5% in August, expected unchanged. Our calculation yields a 5.2% y/y growth, trending just marginally down. The m/m rate was stable at 0.4%. Monthly growth rates have been stable since late 2017. In real terms, we assume growth has accelerated to some 3%, from close to zero through last year
- Manufacturing investments are still increasing but just marginally. Retail trade investments are sharply down, while real estate is booming
- Long term, nominal investment growth (measured this way) has been on a downward path, from 25-30% before 2009 – but it has now stabilised, well below nominal GDP or income growth

Manufacturing investments are slowing, public investments gain some pace

Retail trade invest. down 18%, have bottomed, primary marginally down. Others are still growing







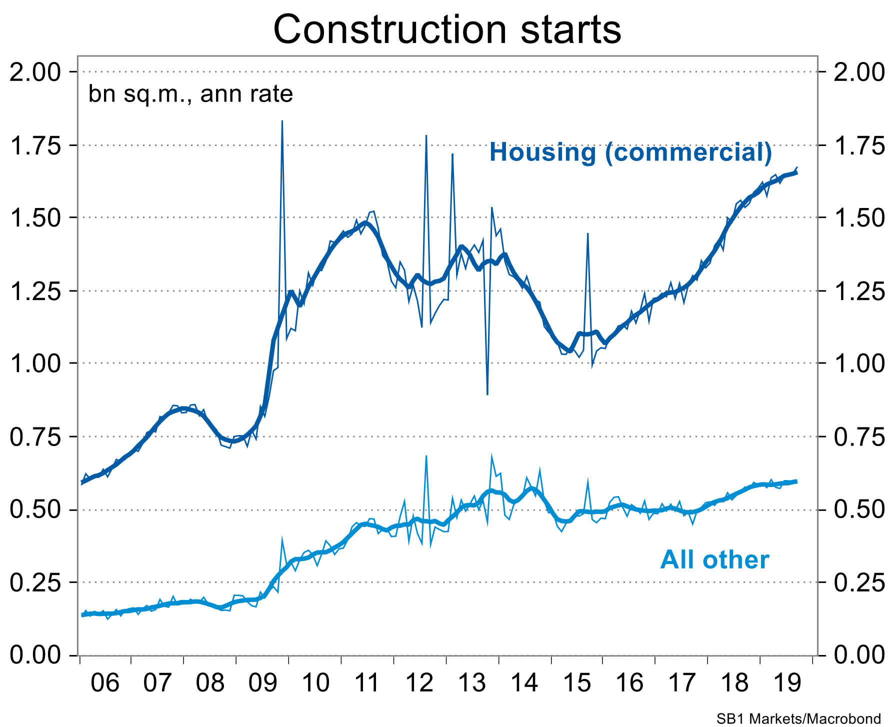
- Manufacturing investments are still slowly on the way up but just by 2% y/y, down from 12% y/y one year ago! Most likely due to the escalating trade/tech war
- Weak retail sales through 2018 brought investments in trade sharply down; -18% y/y - while the level is stabilising now
- Real estate investments and are now the main growth engine
- Public sector investments slowed in 2017 and most of 18, have picked up to a 5% speed now, from below 3% in the spring. **Still, there are no signs of any substantial fiscal stimulus**

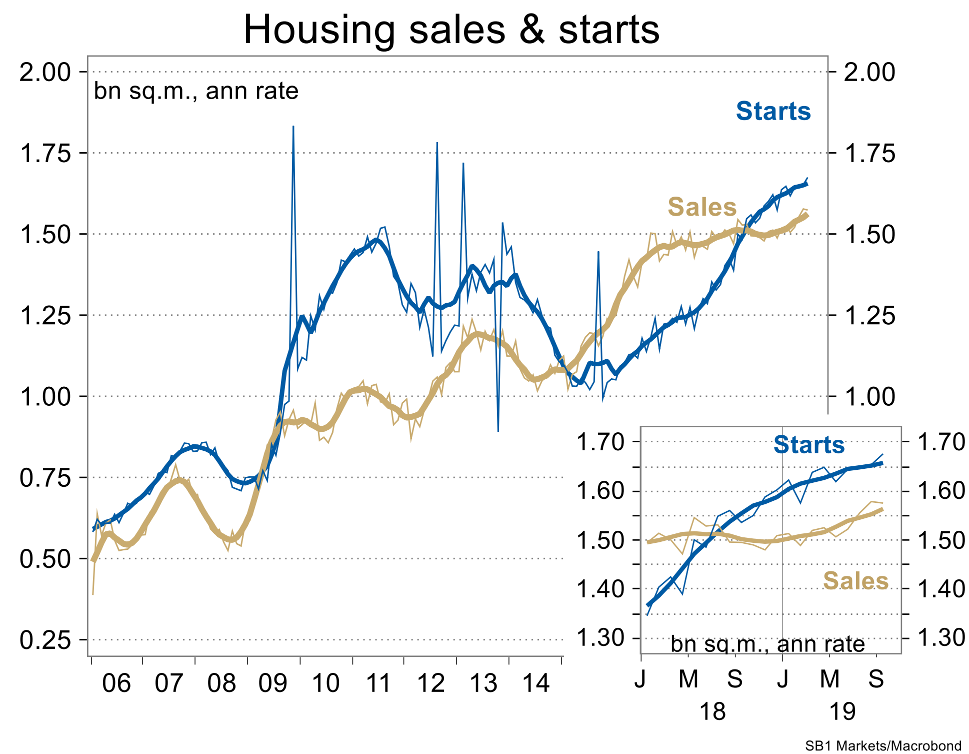
Not all sectors have reported data for the last month

SpareBank 1 MARKETS

New home starts are slowing somewhat, sales are accelerating softly

Both housing starts and other construction are at record high levels, close to peak?

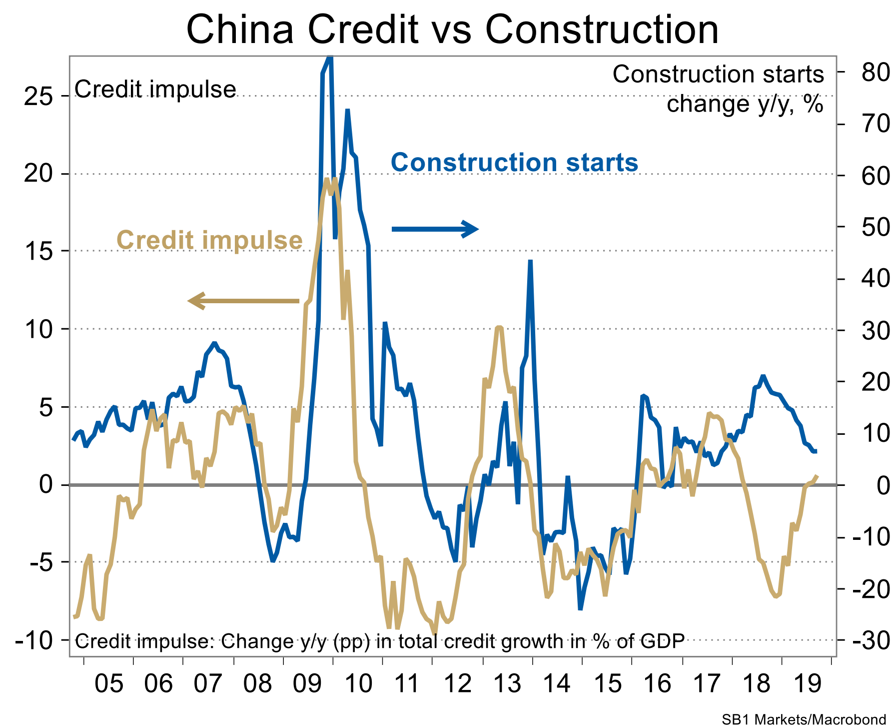




- Sales of new homes have accelerated through the summer, and are not that far below housing starts
- Starts rose in Sept to a record high level but growth has slowed somewhat so far in 2019. Starts are up more than 50% from the 2015 trough, and are up 7.5% y/y (smoothed) – and are now slowing. The downside risk is still there. Sales are below starts – implying an increasing inventory – yet we are not that worried, given the large inventory drawdown from 2014 – 2018.
- Other construction starts have been flattening since late 2018 but are still up 4.5% y/y (down from 20% in late 2018). These starts have reached a new ATH too, although the level is not that much higher than 5 years ago. The cycles in non residential construction have been and still is very close to the cycle in residential construction

Credit and construction have moved in opposite directions recently

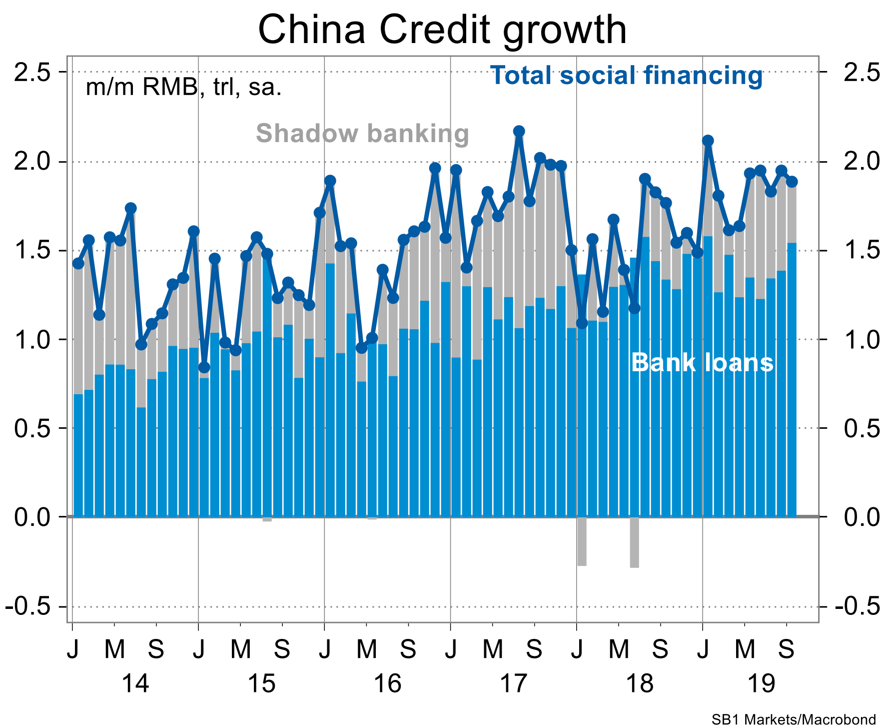
Usually, credit growth and construction starts are correlated

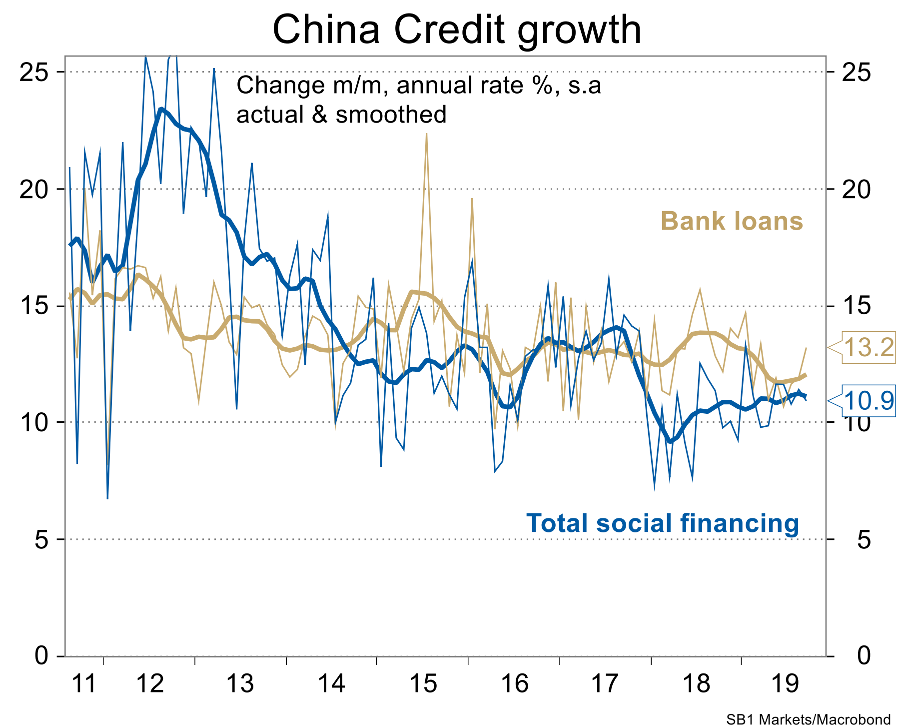


- During 2017/18 credit was tightened but construction activity accelerated – now, credit is no longer contracting while growth in construction is slowing

Bank lending gains pace, supported by easing policy?

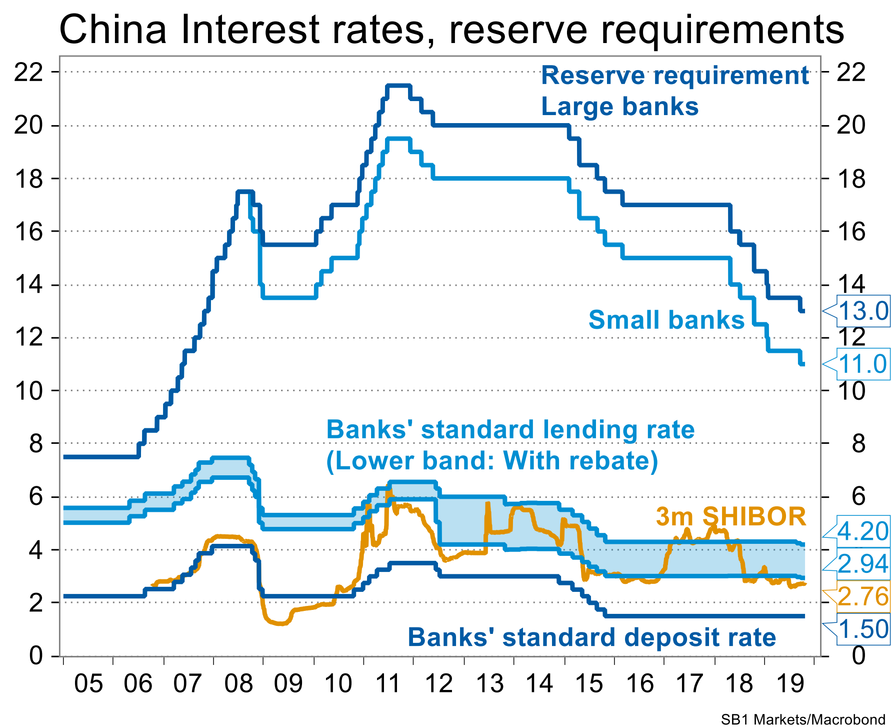
Credit growth was substantially higher than expected in September, driven by bank lending

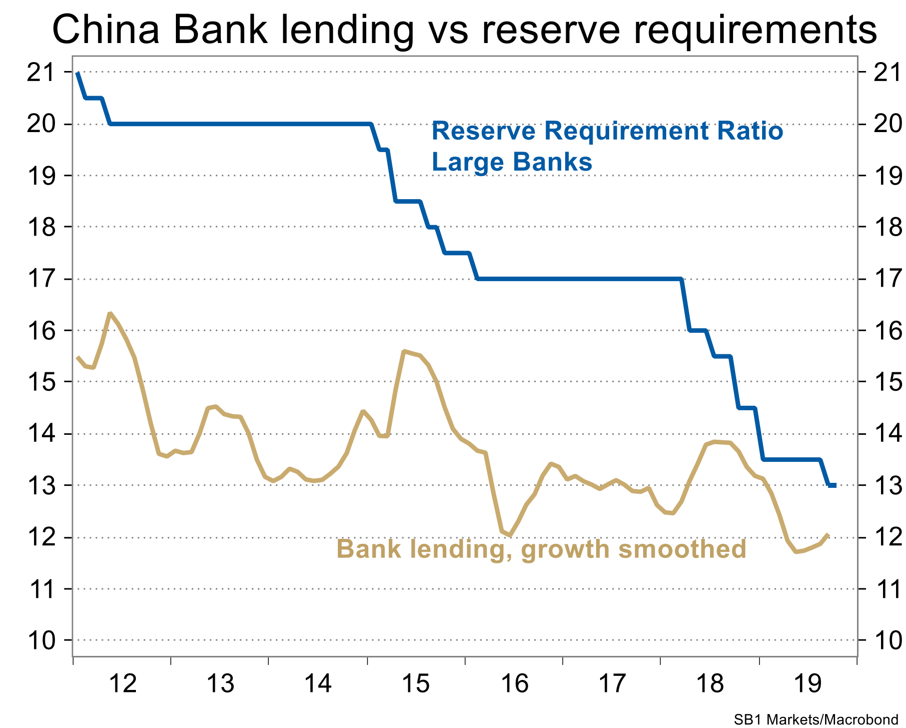




- Total credit rose by 10.9% m/m annualised in Sept, from 11.4% in Aug. In RMB, total credit rose by 2.27 trl, expected 1.9 trl (not seasonally adjusted). The underlying trend is slowly up since the trough in early 2018. The credit impulse is now marginally positive
  - » Growth in bank lending accelerated for the third month in row in Sept, after a slowdown in H1 2019. Most likely, the upturn is a result of easing monetary policy; bank's reserve requirement have been cut 6 times, releasing close to 5% increase in lending capacity. Credit supply through the non bank ('shadow') credit market, which drove total credit up in H1, has slowed the past months. Shadow banking now accounts for some 20% of total credit supply
- What's next? Many expect the PBoC to turn more expansionary, and interest rates cuts are quite likely. However, there are good arguments against pushing the credit accelerator even harder. Credit growth is well above growth in nominal GDP, and high debt ratios are climbing further

Rates just marginally cut so far but reserve requirements are slashed



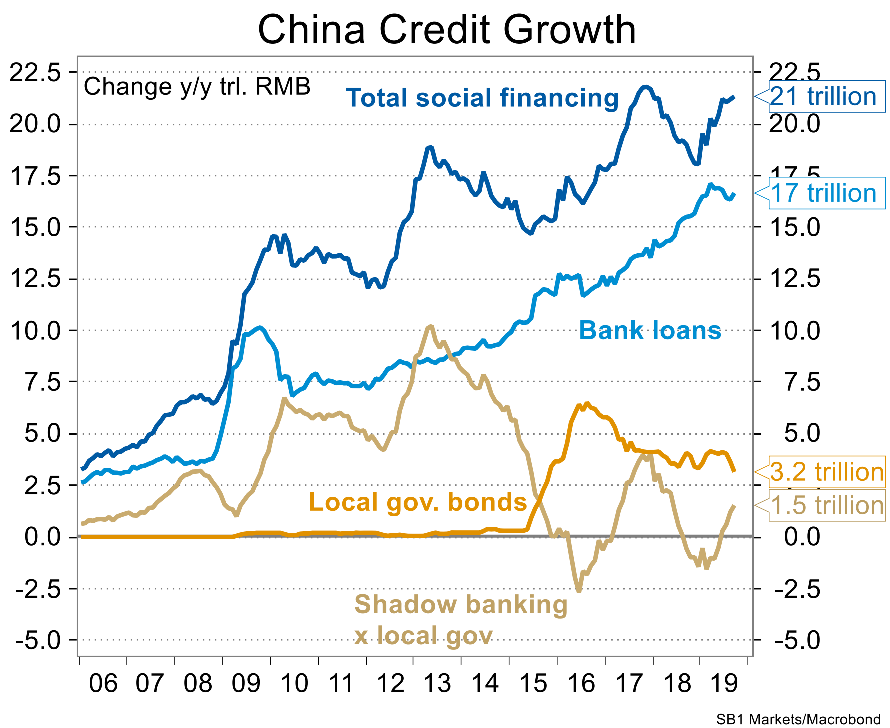


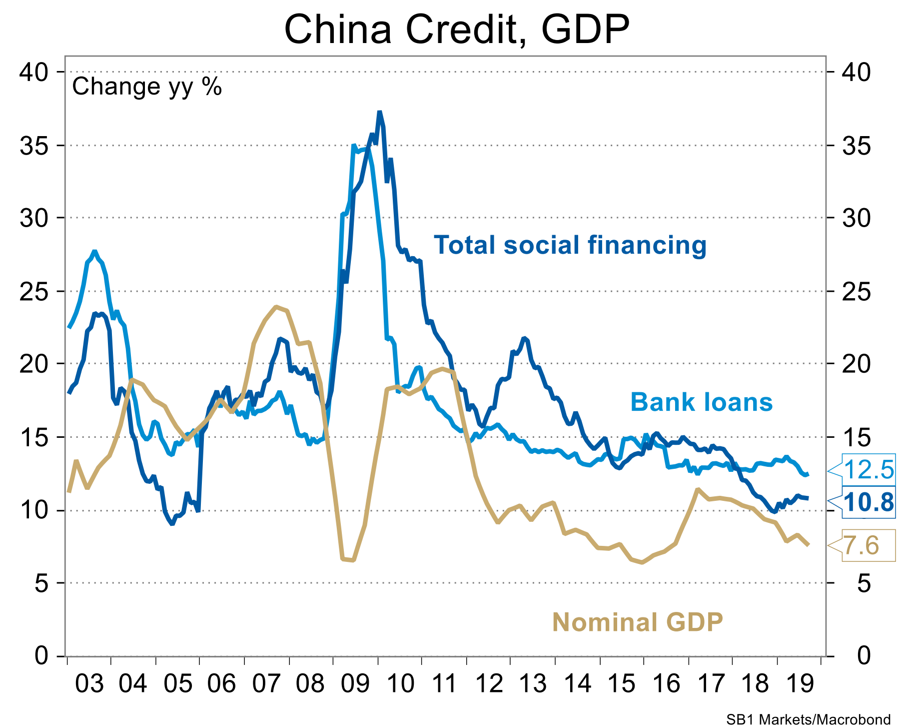
- Last week, the PBoC announced a CNY 200 bn cash injection into the banking system to ease lending conditions. This amount equals just 1/10th of one month's increase in bank lending, and cannot have any significant impact on credit condition
- This morning, the one year loan prime rate was unexpectedly kept unchanged at 4.2% (expected at 4.15%)

SpareBank 1 MARKETS

Credit growth has accelerated slowly over the past year

Banks have been slowing somewhat, while the shadow banking market (ex local gov) filled the void

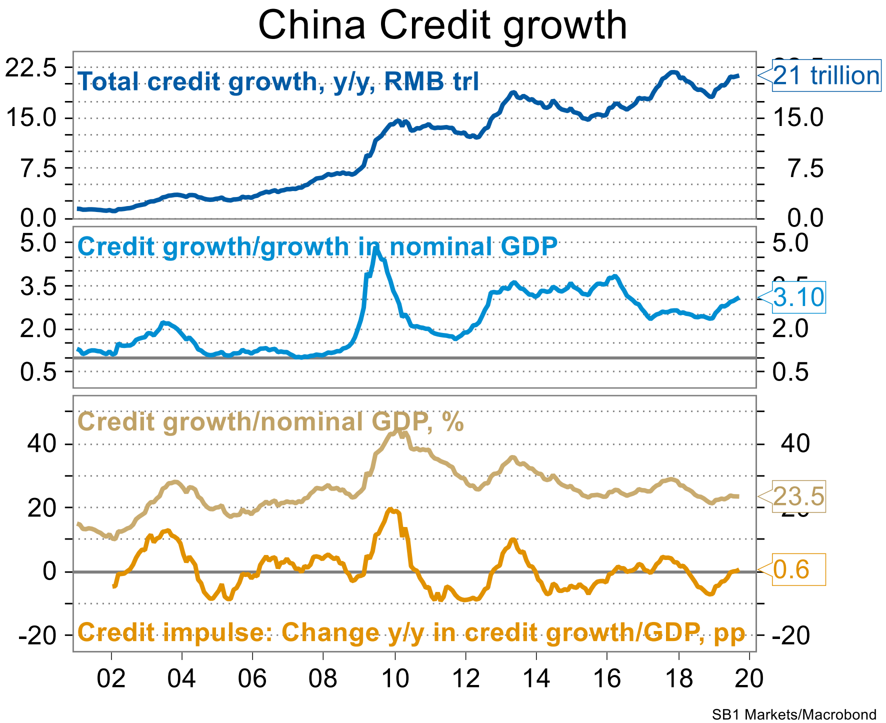


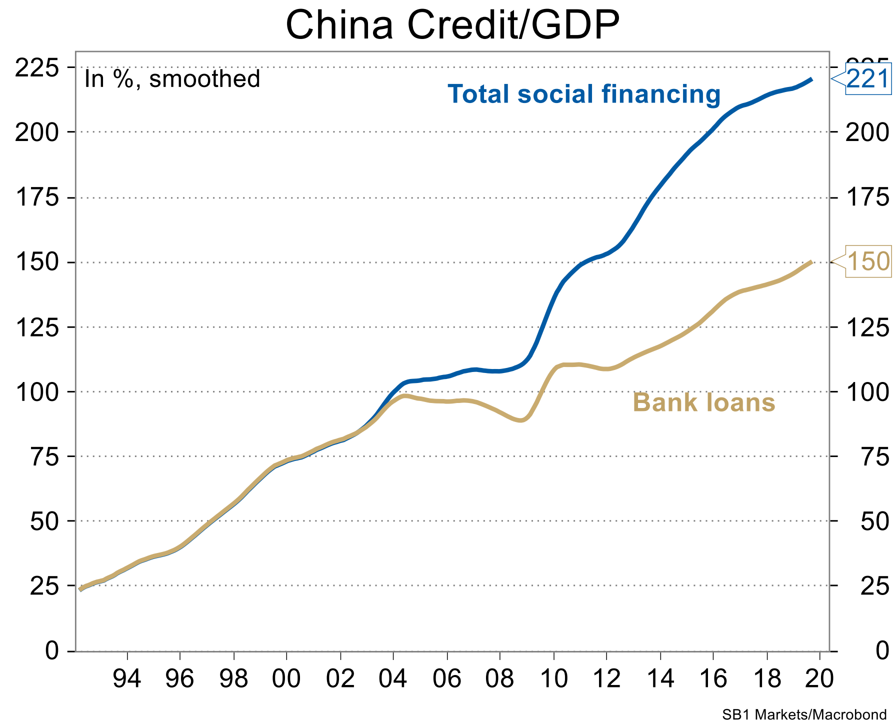


- Over the past 12 months, total credit has grown by CNY 21 trl, equalling 23% of GDP. The annual rate bottomed out in Dec
- Banks supplied CNY 17 trl of the y/y increase in Sept, from 16 trl in Aug, equalling 80% of the total rise in credit volume
- Local governments borrowed CNY 3.2 trl in the bond market, slowing recent months
- Other credit – via the shadow credit market x gov bonds – are up 1.5 trl, from a negative drag over the previous year
- Total credit growth at 10.8% is well above growth in nominal GDP at 7.6% in Q3, and debt/income is still on the way up

Credit impulse has turned marginally positive, from negative

Credit growth is now slowly increasing vs GDP



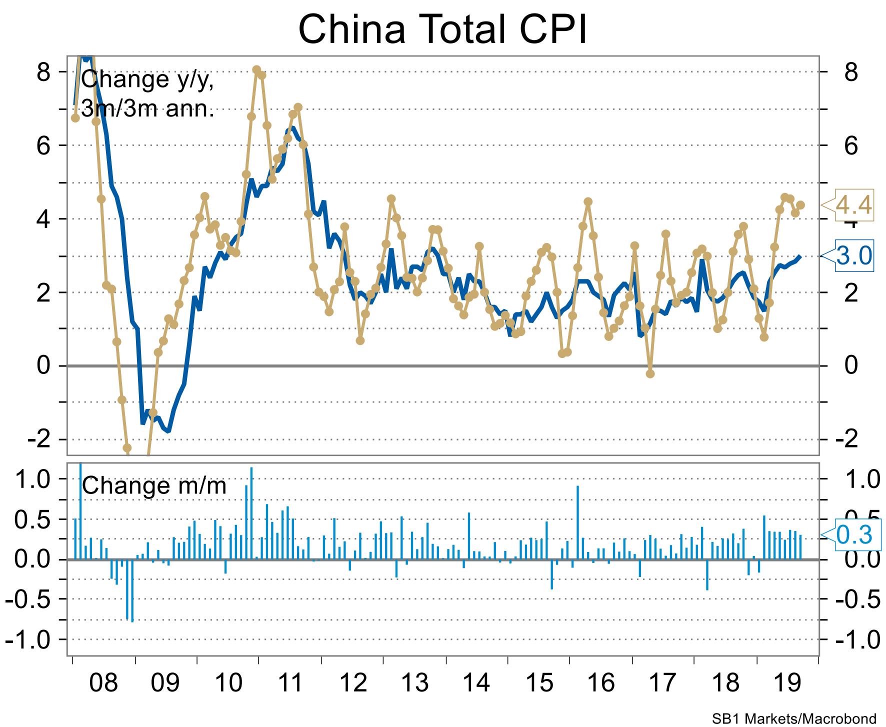


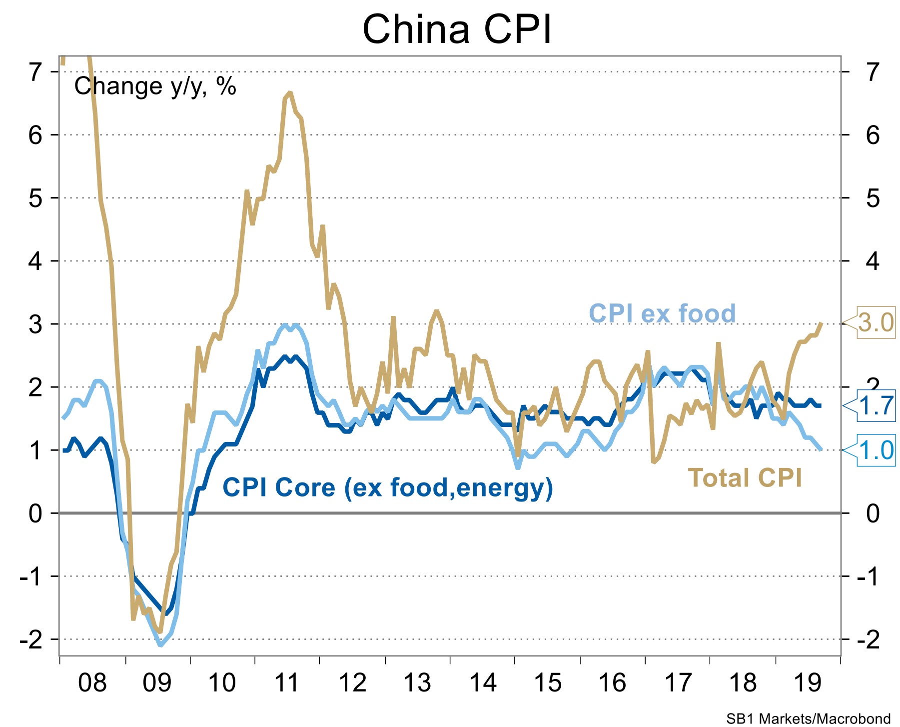
- A negative credit impulse implies that the credit growth/GDP ratio is declining (the 2nd derivative)
  - » Indicates credit tightening (or weaker demand)
  - » Has been associated with slowdowns in the Chinese economy
  - » Now, the credit impulse has risen to marginal positive
- We are uncertain how far the authorities are willing or able to bring credit growth back up. The credit/income level is high – and it is still increasing. For every RMB GDP grows, credit increases 3 by RMBs, and each year growth in credit equals more than 20% of GDP. That's not sustainable, neither for lenders or borrowers in the long run, if nominal GDP growth is less than 10%. The Government may succeed in increasing credit supply short (if they dare to, vs long term risks) but the problem may turn out to be demand for credit

SpareBank 1 MARKETS

Total inflation accelerated to 3%, core CPI steady at 1.7%

Total inflation climbs on a rapid increase in pork prices, core inflation holds steady



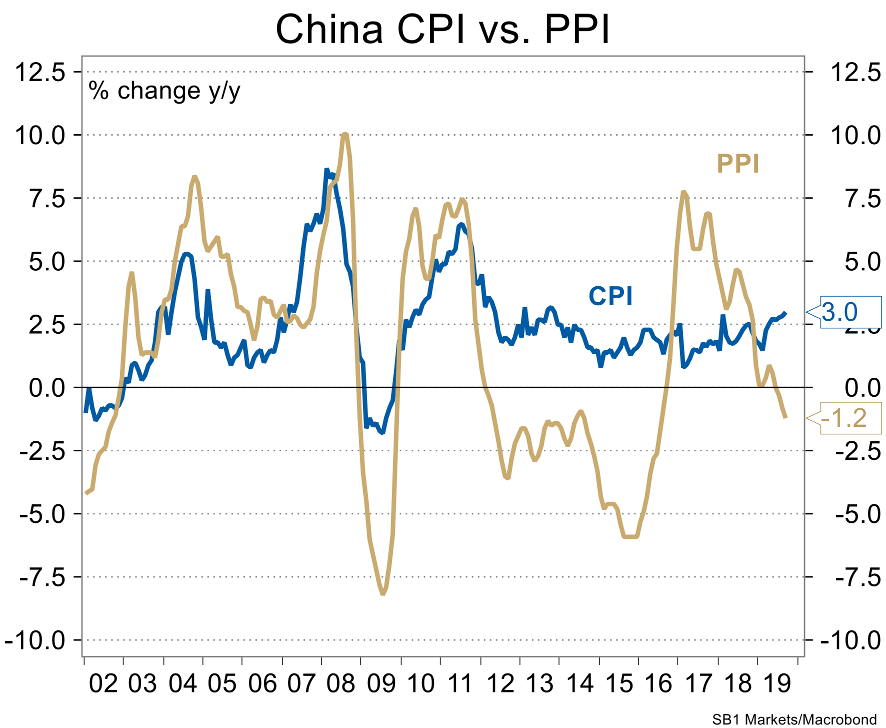


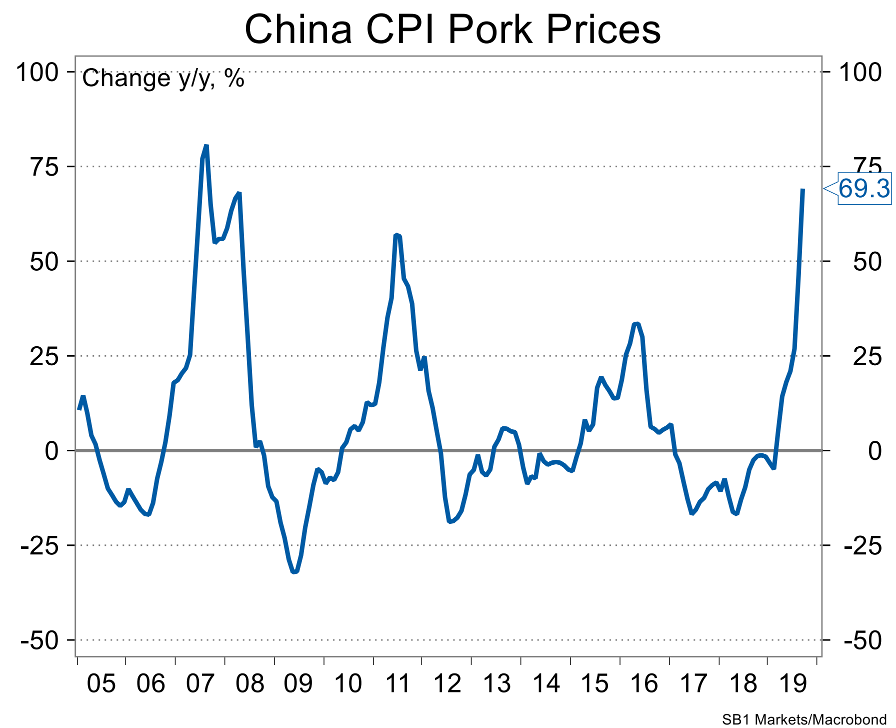
- Headline inflation rose to 3.9% in Sept, from 2.8% the prior month. Total inflation is fuelled by accelerating food prices
  - » Food prices jumped 2% m/m in Sept and the annual rate accelerated rose to 11.2%. Pork prices are up almost 70% y/y, flip to the next slide
- CPI ex food fell to 1.0% in Sept, sliding down the past year. The decline recent months is just due to lower energy prices, the core – CPI ex food and energy – is up 1.7% y/y, and the trend is flat. <u>Higher inflation will hamper real consumption growth. The slight decline in the PPI may signal a slowdown in the Chinese economy</u>, check next page

SpareBank 1 MARKETS

China producer prices are falling, not than unusual but not a signal of strength

PPI down 1.2% y/y in Sept, dragged down by oil, raw materials. Food prices up (0.3 pp contrib.)



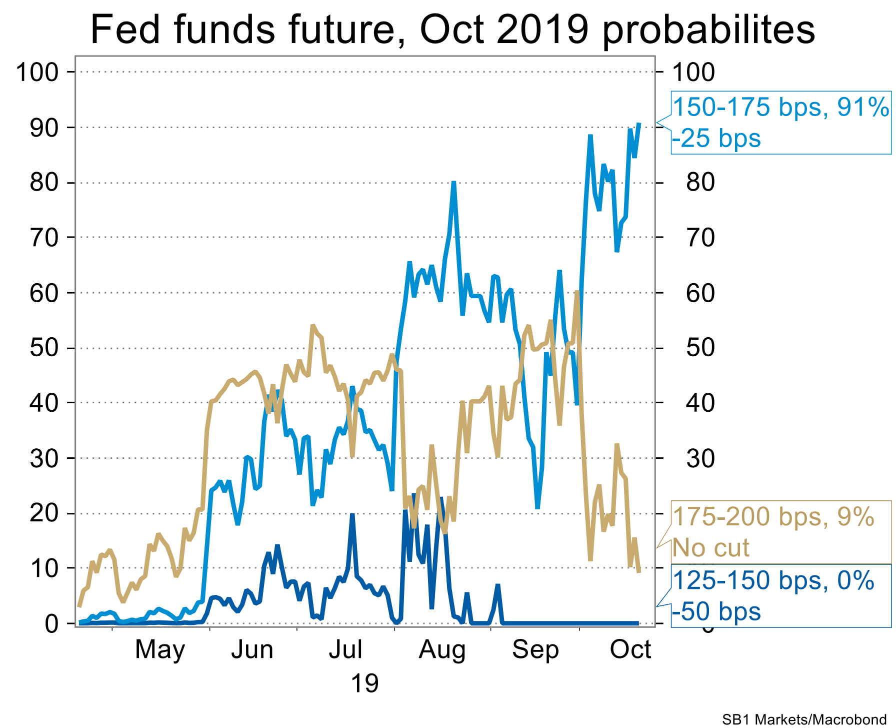


- The decline in PPI is so far not serious compared to previous periods with falling produced prices. From 2012 to 2016 prices fell by 3% per year in average, lowering the price level by more than 13%. Even that did not kill the Chinese economy
- Pork meat prices have soared by almost 70% due to the swine flue, driving total inflation up but the impact on the PPI is marginal

Fed's Beige Book reports slower growth but still very tight labour market

Fed's 'regional network' lowered the growth assessment to 'slight to modest', from 'modest'

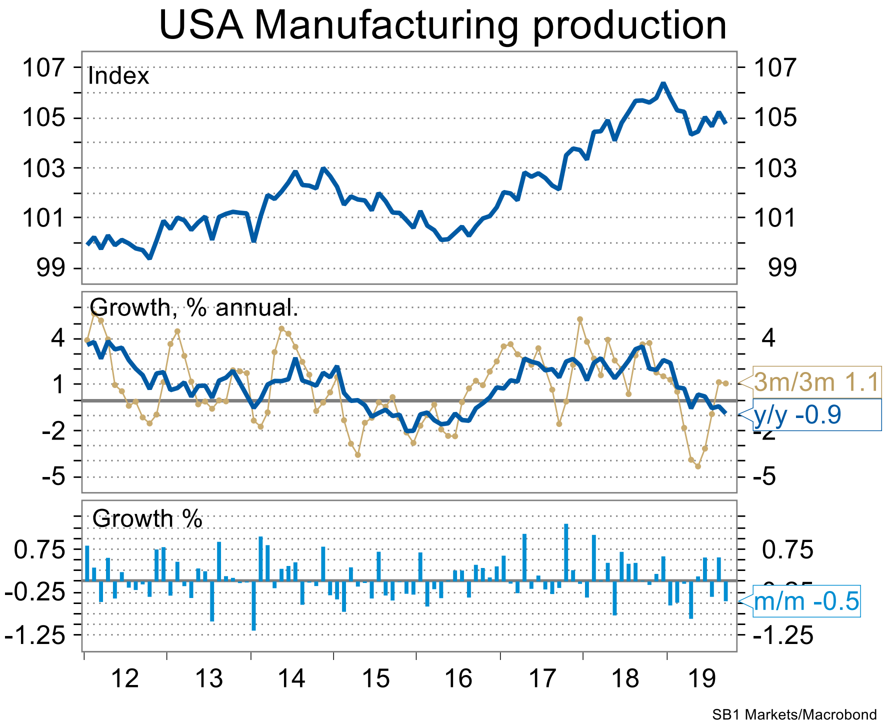
- Economic activity expanded at a '*slight to modest*' rate, according to the respondents to Beige book, downgraded from 'modest' in the September. Many businesses lowered their growth outlooks
- On the demand side
  - » Consumer spending was still solid; robust retail and auto sales
  - » No substantial changes in housing market conditions
- On the supply side
  - » Manufacturing is the major drag on growth, businesses report a further slowdown in manufacturing activity
- Labour market
  - » The assessment of employment growth was changed to 'slight' from 'modest', due to rising labour shortages
  - » Some businesses noted that they reduced working hours rather than staff levels as demand has slowed, due to concerns about future labour shortages (labour hoarding). Wages still rose 'just' moderately
- Prices
  - » Modest inflation and mixed reports on the impact of tariffs
- **In total, the Beige book reflects just a modest slowdown in the US economy, chiefly stemming from global trade uncertainties and labour market tightness. Not an argument for cutting interest rates once again!**

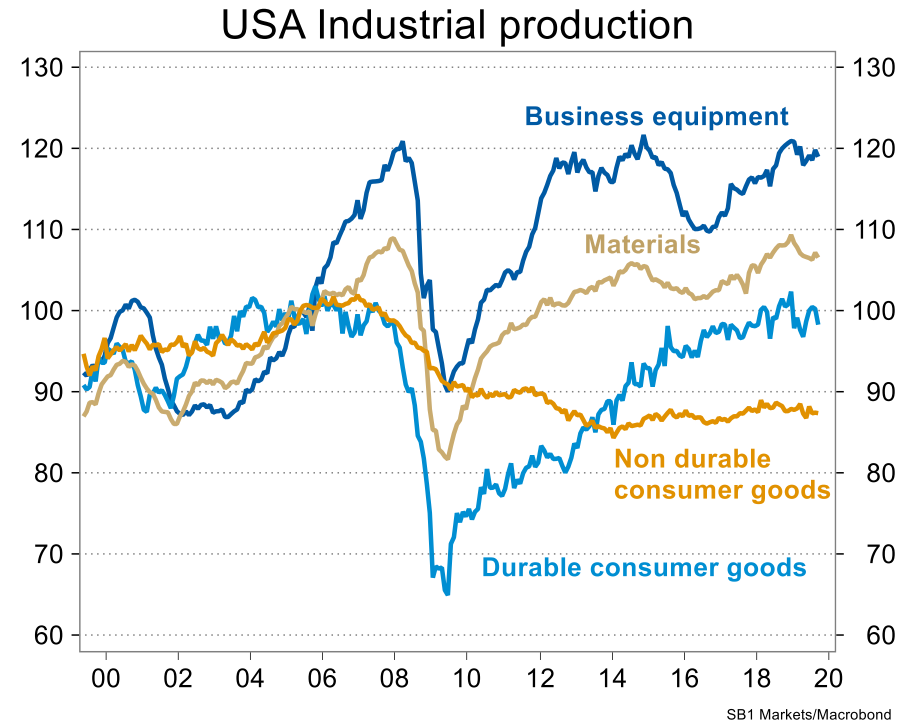


The market is pricing a 25 bps Fed cut on Oct 30 by an 91% probability (and 9% for no cut). We think the probability for a cut is lower, yet still above 50%, even if a cut is not needed and the FOMC was very divided at the Sep. meeting

Manufacturing production stabilized in Q3 but the outlook is gloomy

Production fell 0.5% m/m in September, up 1.1% in Q3. Surveys signals a weaker outlook

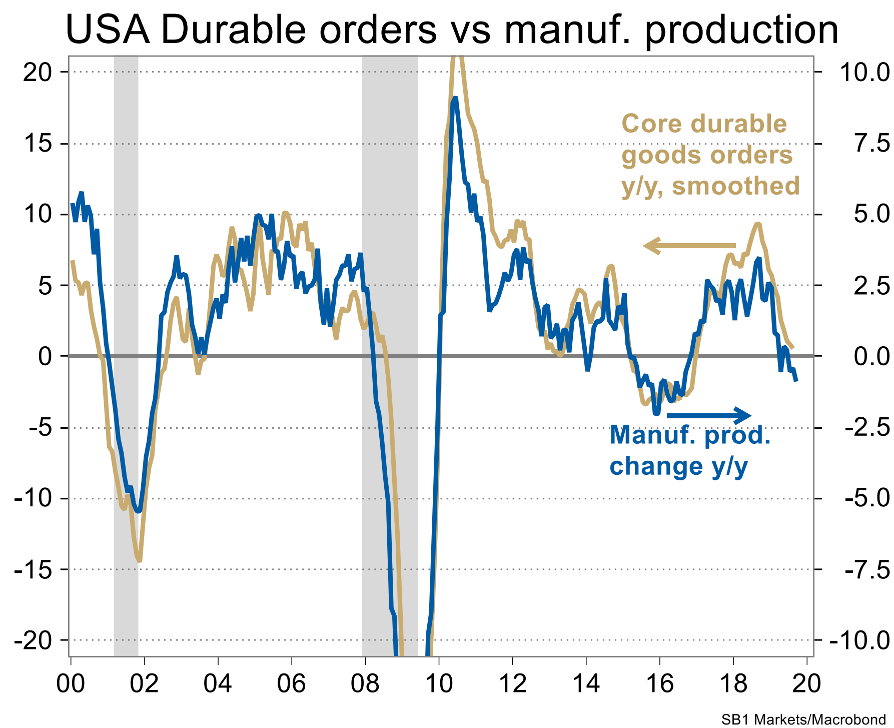


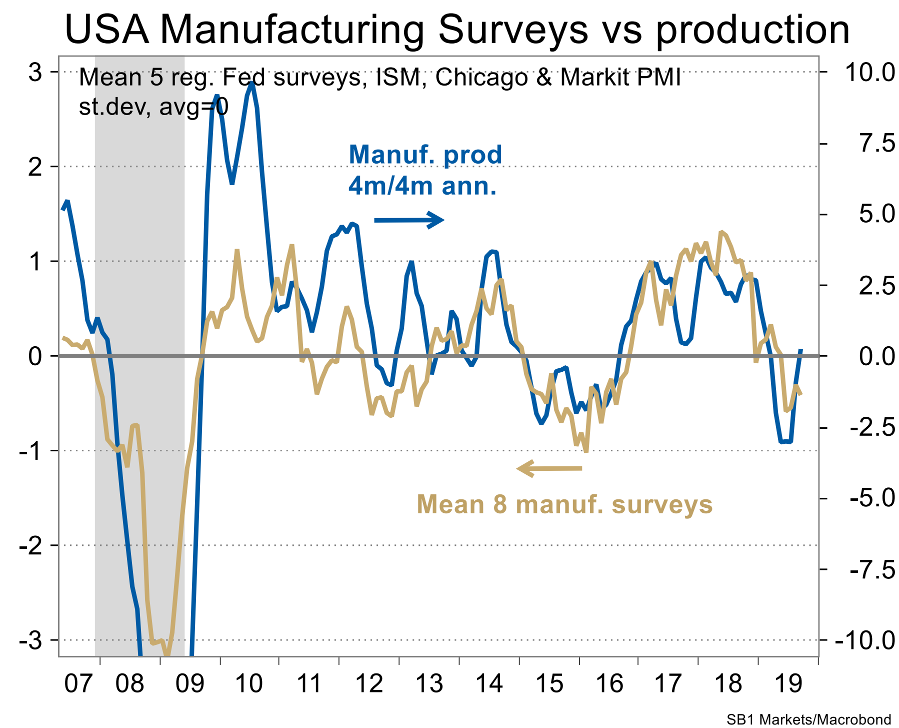


- Manufacturing production declined by 0.5% m/m in September, 0.2 pp below expectations. Still, production has increased marginally the past month and was up 1.1% annualized in Q3, vs the 3.2% drop in Q2. Production is still 1.5% below the Dec '18 local peak and the annual rate is down 0.9%
  - » Total industrial production including energy & mining fell 0.4% and underlying growth is marginally stronger than for manufacturing
  - » Production has slowed in most sectors, the steepest decline has been that of durable consumer goods the past year
- The first October surveys? Check two pages forward!

Unfortunately, orders & surveys do not signal any further recovery

An average of surveys signals a decline in production, orders point to just a stagnation

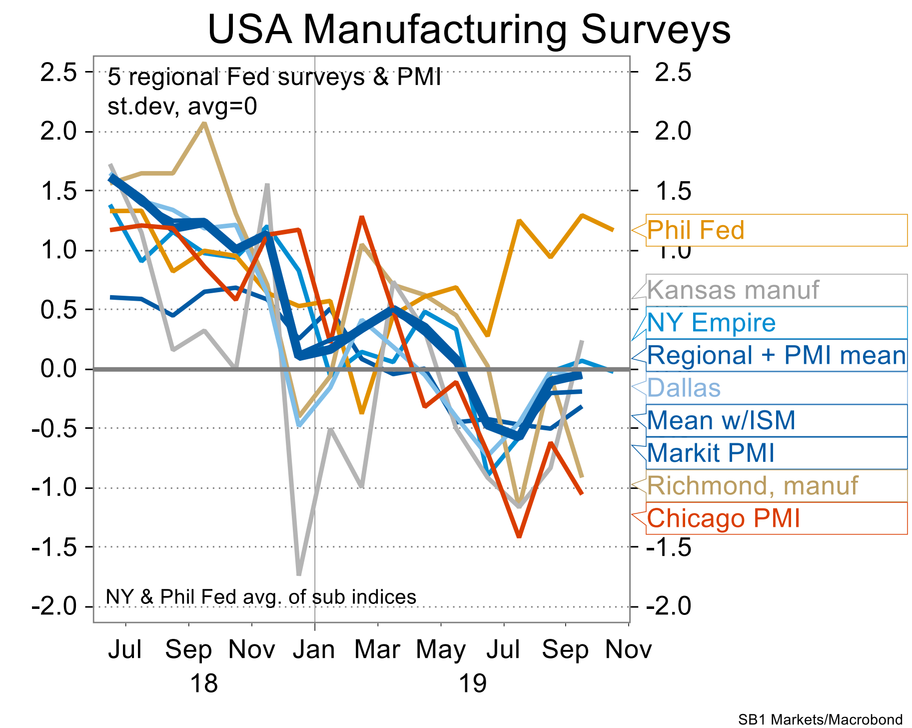


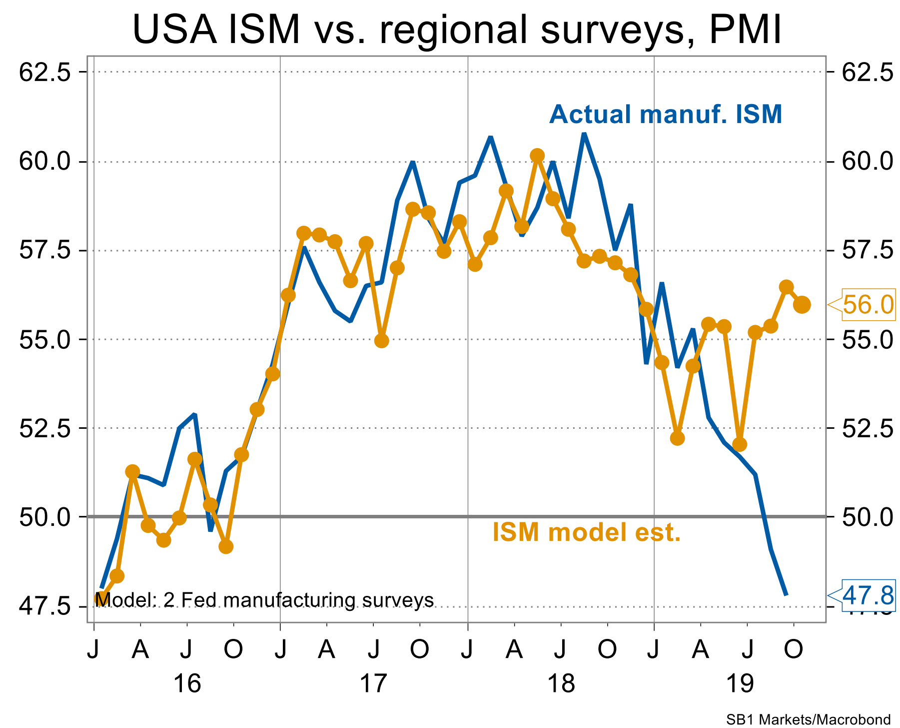


- <u>Flip to the next slide for more on the surveys</u>

NY Fed's manufacturing index a tad up in Oct, Phil Fed slipped

Phil Fed has been out of line vs other surveys recent months, the NY Fed survey closer to the ball

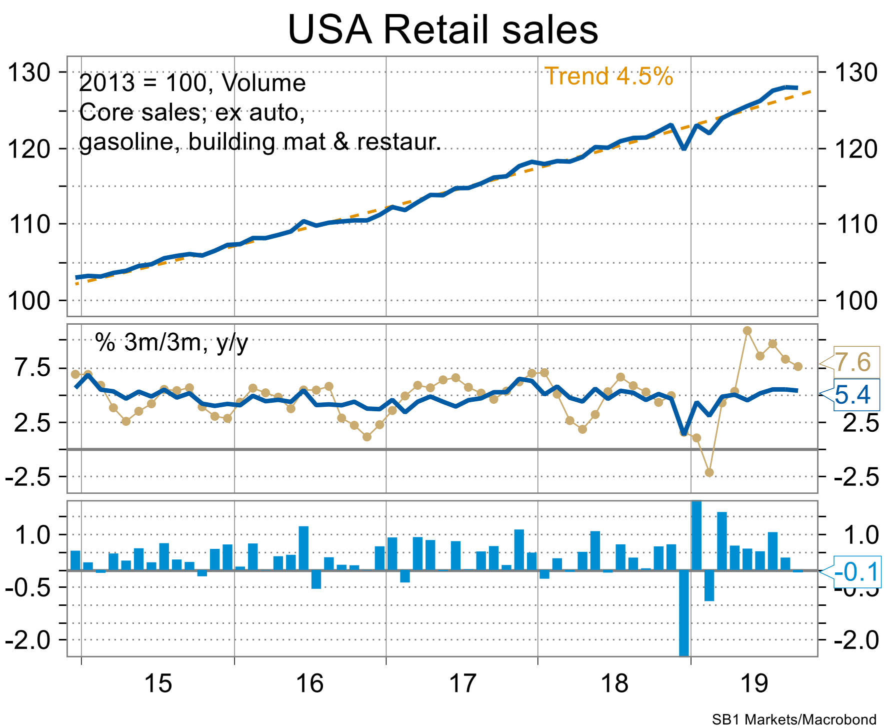


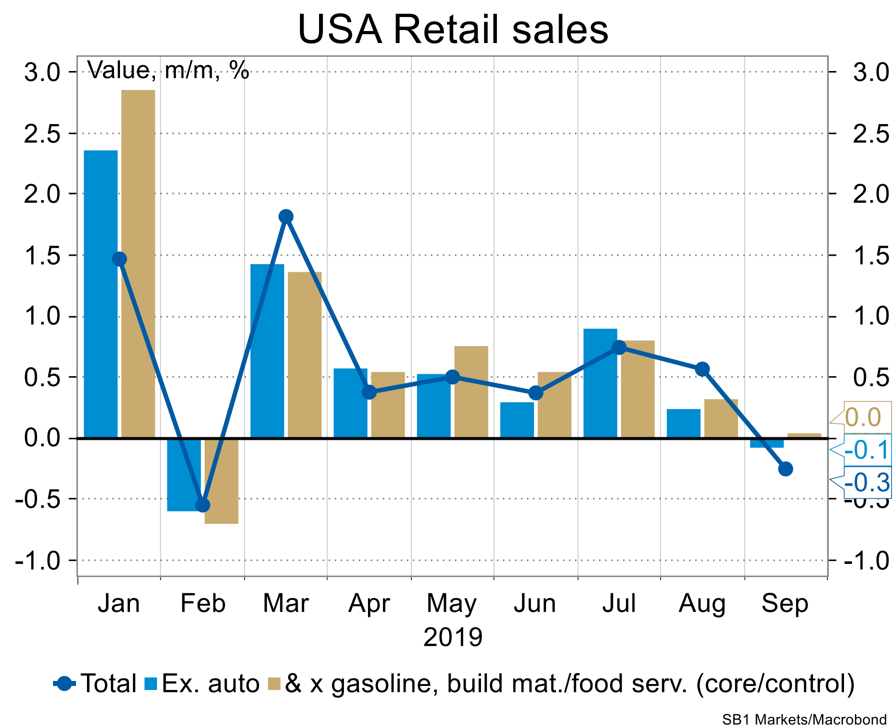


- The Philadelphia Fed index fell more than expected in Oct, to 5.6 (from 12). When calculated as the average between relevant sub indices, like the total ISM and PMI are calculated, the index also fell but the level is still well above average
- The NY Empire is more in line with others, the headline improved marginally in Oct, better than expected – while the average of the sub-indices fell marginally
- Taken face value, these indices signals a small decline in the manufacturing ISM. However, if we let the two surveys indicate the level, they signal a 'crazy level, at 56 (compared to actual ISM at 47.8 in Sept. However, these to regional surveys have been far too to strong compared to other surveys – and actual manufacturing production

Retail sales soared in Q3 but growth is slowly losing steam

Core sales volume fell -0.1% in Sept (our est), underlying growth is still solid

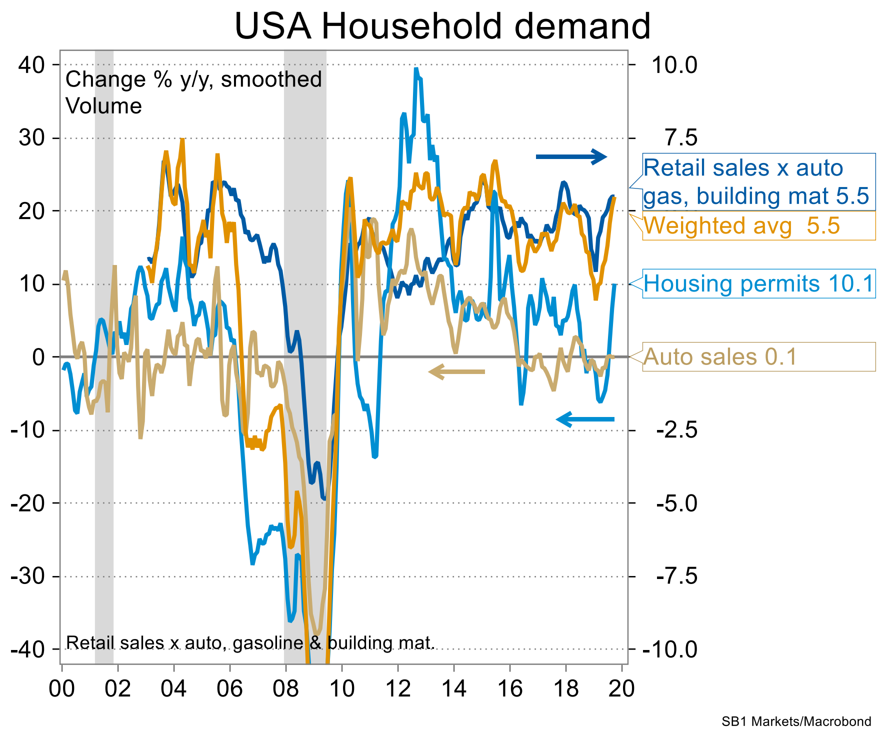


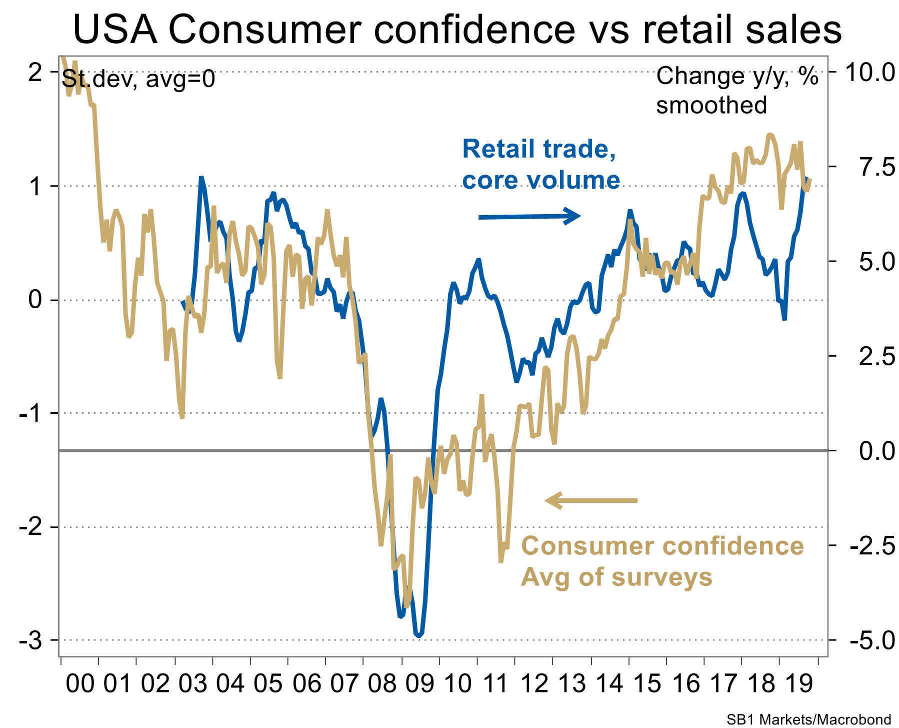


- Core retail sales (ex. auto, gas, building materials & restaurants; control group) were flat m/m in nominal terms in September, 0.3 pp weaker than expected. Total retail sales fell 0.3%, even as auto sales increased marginally
- We estimate a 0.1% m/m decline in core sales volume, following strong growth the prior months. Growth has eased somewhat, after accelerating in H1. Regardless, the 3m/3m speed at 7.6% is still rather impressive, and the annual rate is solid at 5.4%
  - » The slowdown the two past months may still be an early indication that the manufacturing led slowdown is now spreading to the consumer side
  - » Income growth has slowed somewhat, and consumer confidence is mixed – the risks are now skewed to the downside. However, we have no indication of an abrupt slowdown (even if declining savings have been funding half of the growth in consumption so far in 2019…)

Household demand is picking up, at least barring auto sales

Retail sales are soaring, housing has turned up, while auto sales have stagnated

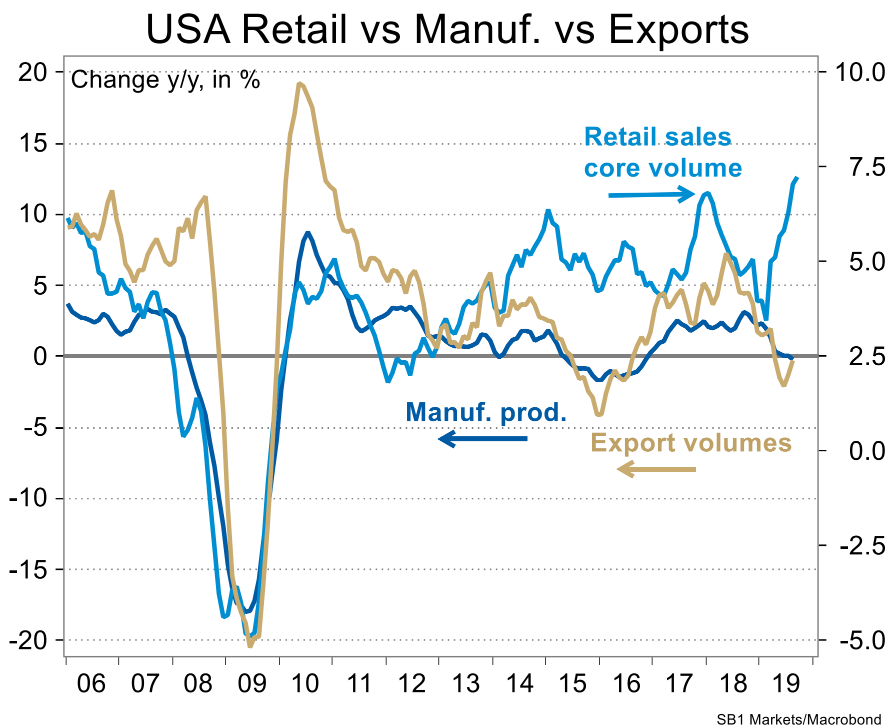


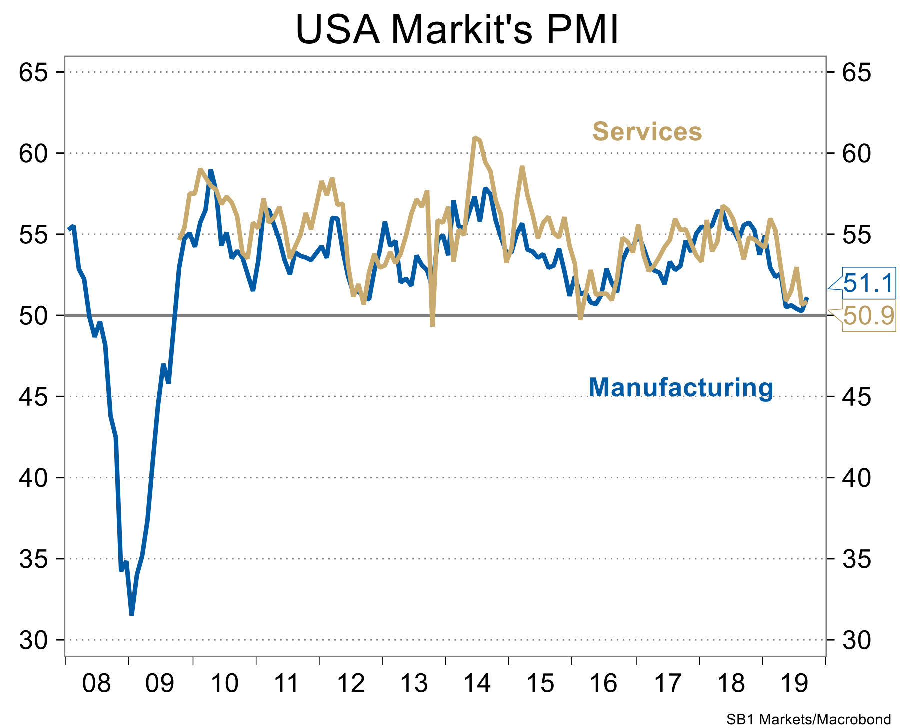


- Total household demand is not on the brink of sending the US into recession! The weakness in the US economy is stemming from businesses and global demand, not US consumers
- Consumer confidence (measured by the avg of University of Michigan's and Conference Board's indices) has moderated somewhat this autumn but remains at an elevated level

Consumer spending has been the pillar of economic growth this year

Consumer demand has been resilient to the manufacturing and slump and the global slowdown



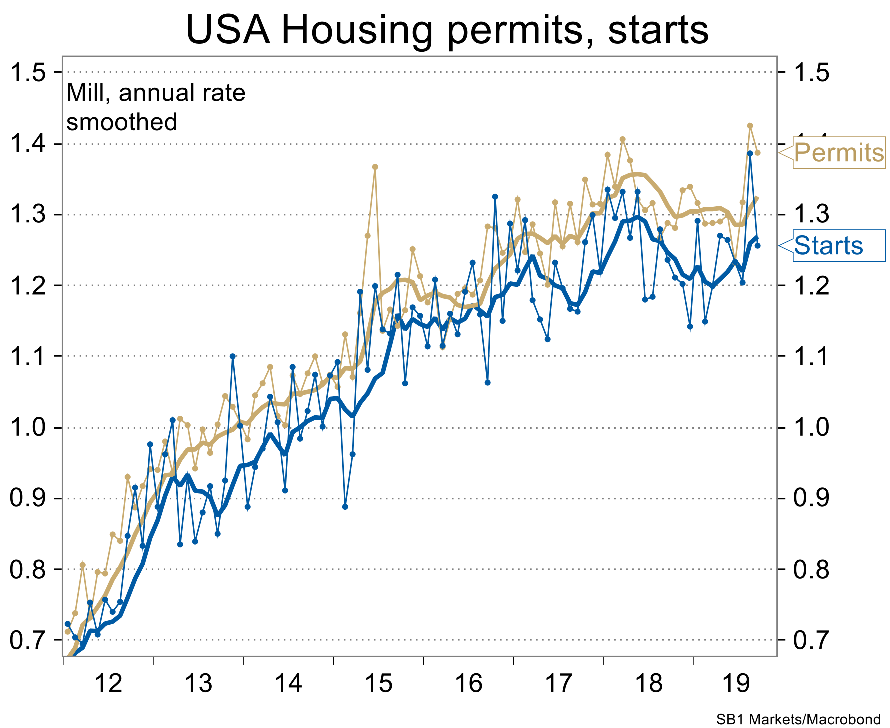


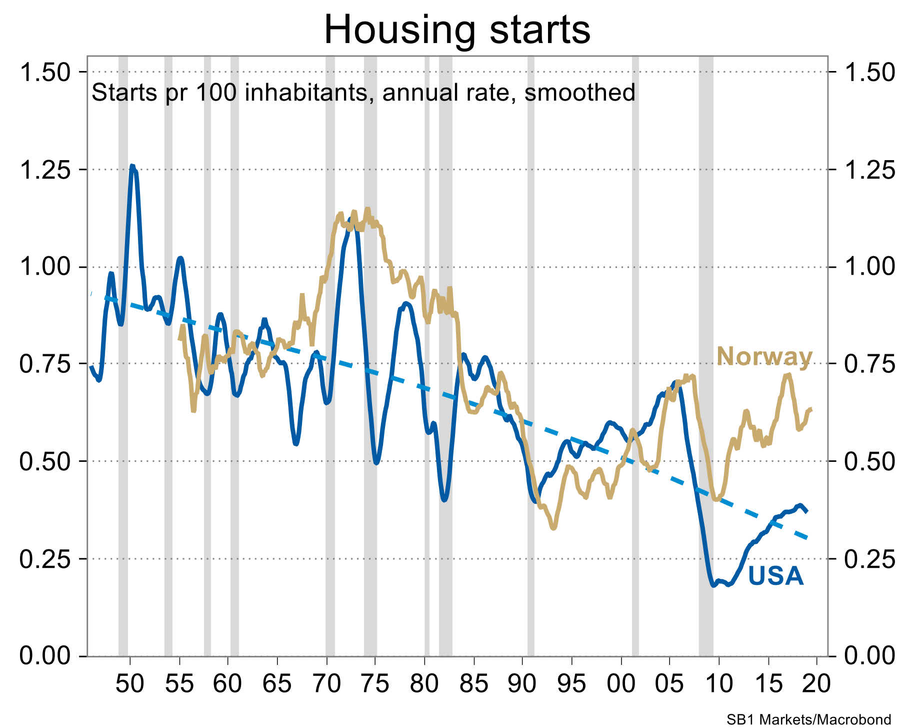
- The services PMI covers much more than retail (such as hotels, banks, education, health, professional services, real estate etc), however, the downturn in the PMI recent months may be a sign of weakness on the consumer side

SpareBank 1 MARKETS

Housing permits remained very strong, volatile starts back to a 'normal' level

Permits fell just marginally in Sept after Aug spike, both starts and permits trending moderately up

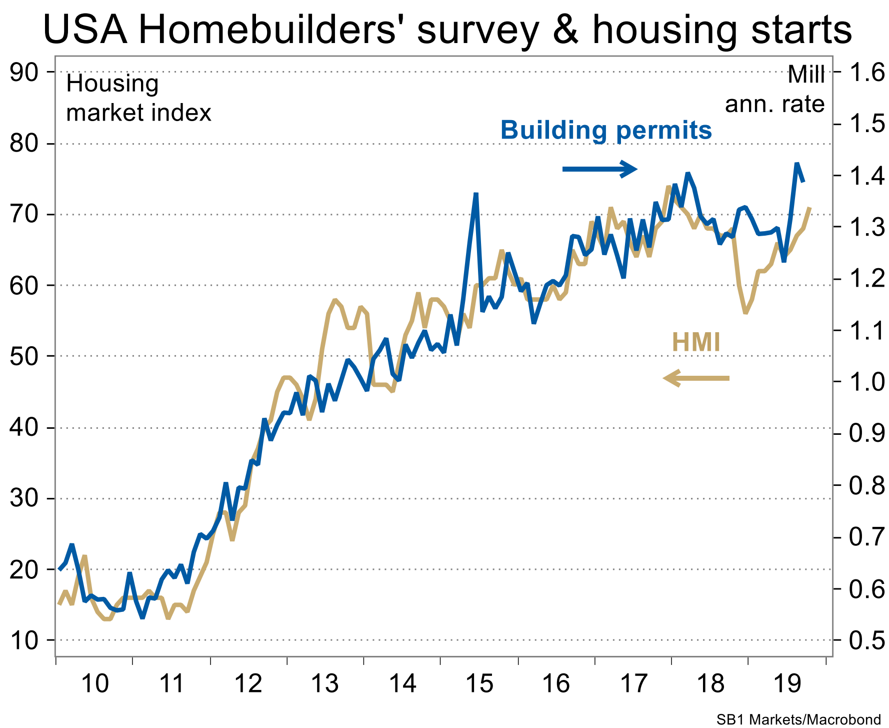


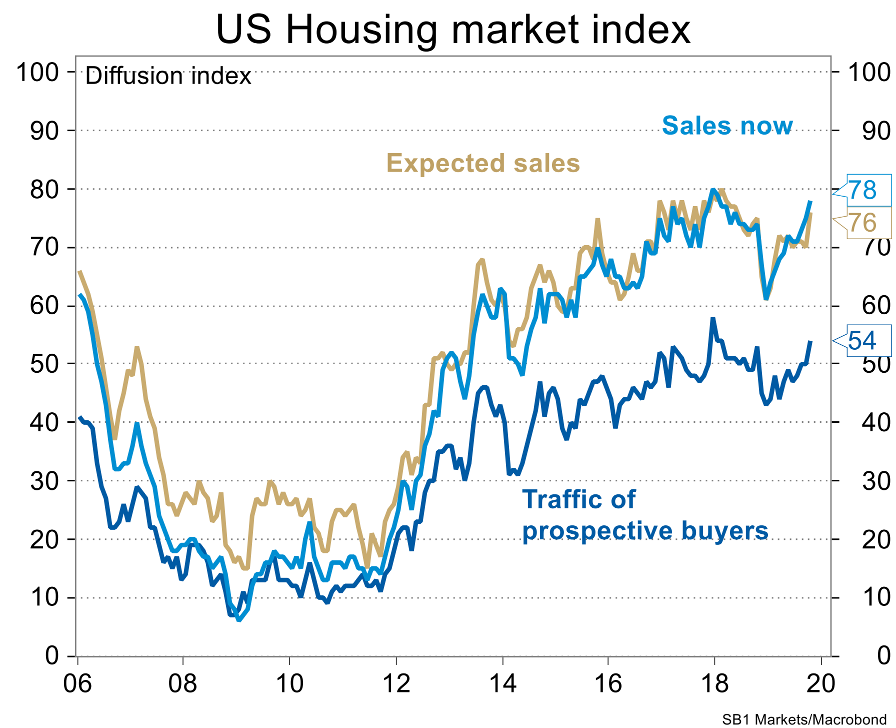


- Housing starts fell 9.4% m/m in Sept while permits fell 2.7%, thus, reversing just a small share of the surprising Aug jump. Permits were reported at an annual rate of 1.39 mill in Sept, vs expectations at 1.35 mill
- Housing permits are usually less volatile than actual starts, thus, a more useful gauge of the activity in the sector than actual starts. Permits have climbed steeply recent months and are back at the 2018 peak level, however, the smoothed rate is still 2.4% below the peak. Starts have increased more than permits the past months
- Housing starts/permits reflect a solid housing market, boosted by low mortgage rates. Upbeat Homebuilders' confirm a moderate upswing, so do home sales. The level of housing starts is still quite low, and the home construction downside is not large compared to the downturn in 2006-09

Homebuilders’ confidence is soaring

The HMI improved once again in Oct, however, the index does not signal higher building activity



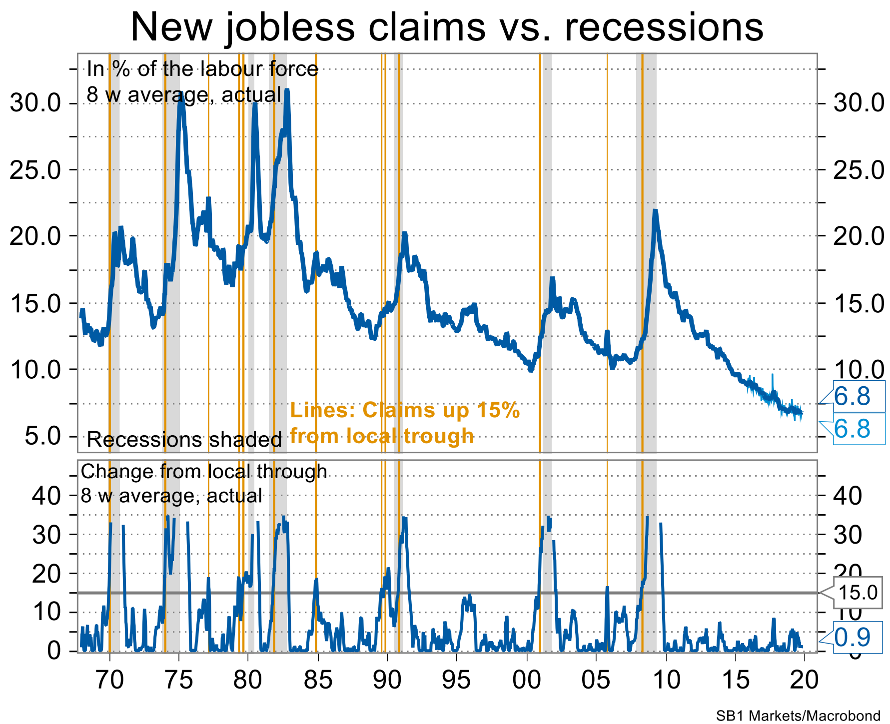


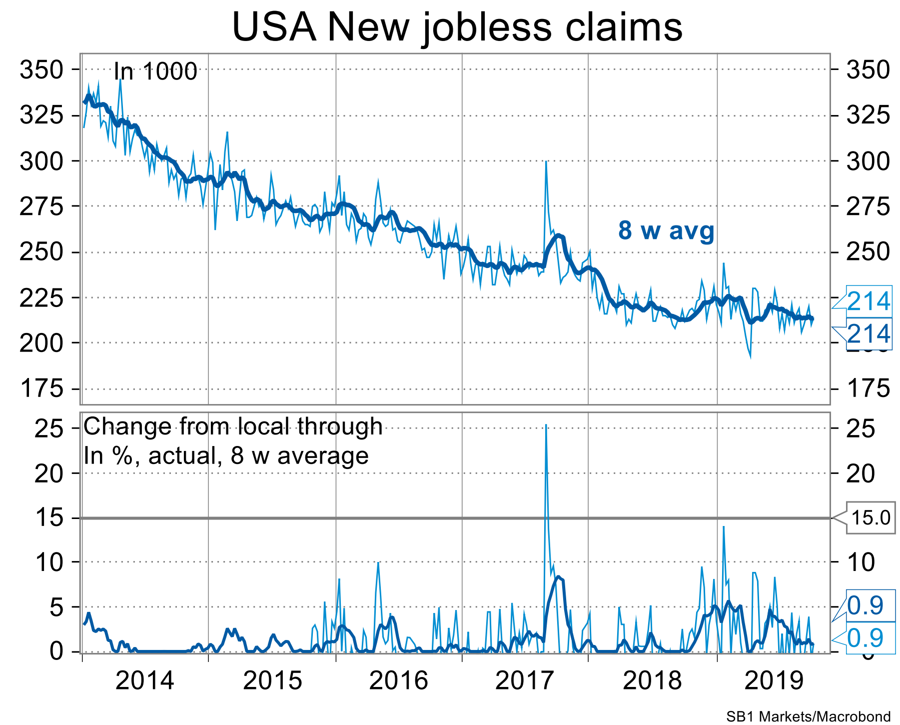
- The housing market index (HMI) rose to 71 p in October, a 3 p increase from Sept, expected unchanged. The homebuilders have been reporting improved market conditions since January and the HMI index is just 3 p below the 2018 peak
  - » According to the homebuilders, lower mortgage rates and strong demand are boosting activity
  - » The homebuilders have been complaining about lack of labour and lack of building lots recently
- Building permits rose steeply in Aug/Sept, the HMI does not signal a further lift

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

Jobless claims another remains very low, no signs of weakness yet

Jobless claims ticked up to 214’ last week, the 8 w average is equally low, at 214’

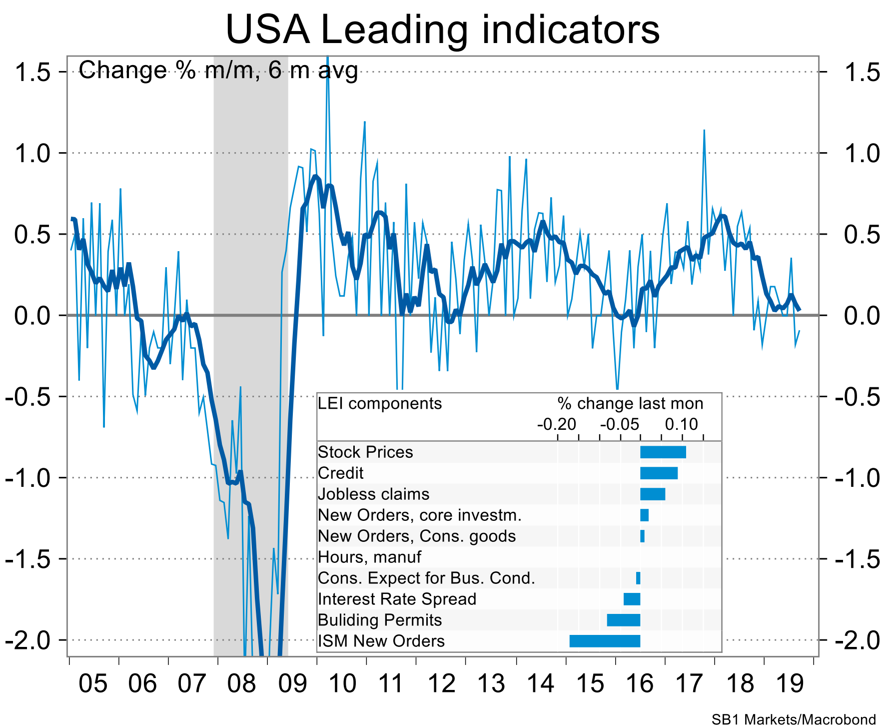


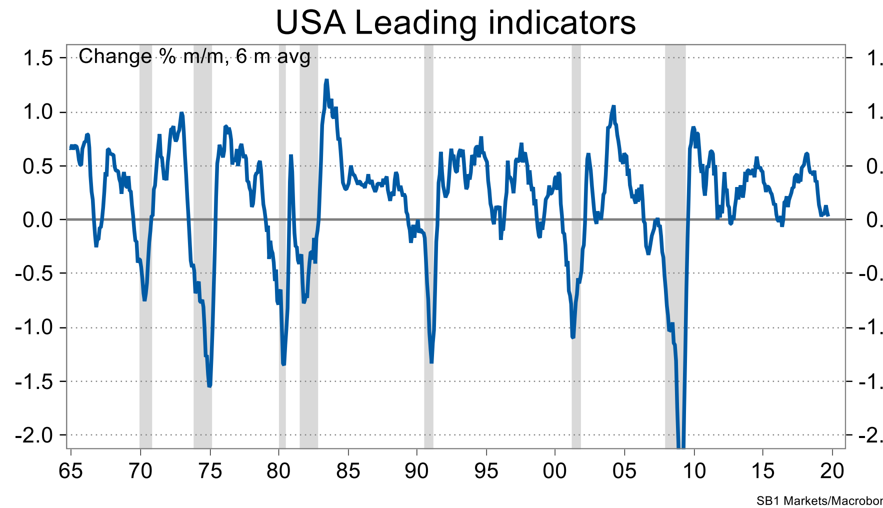


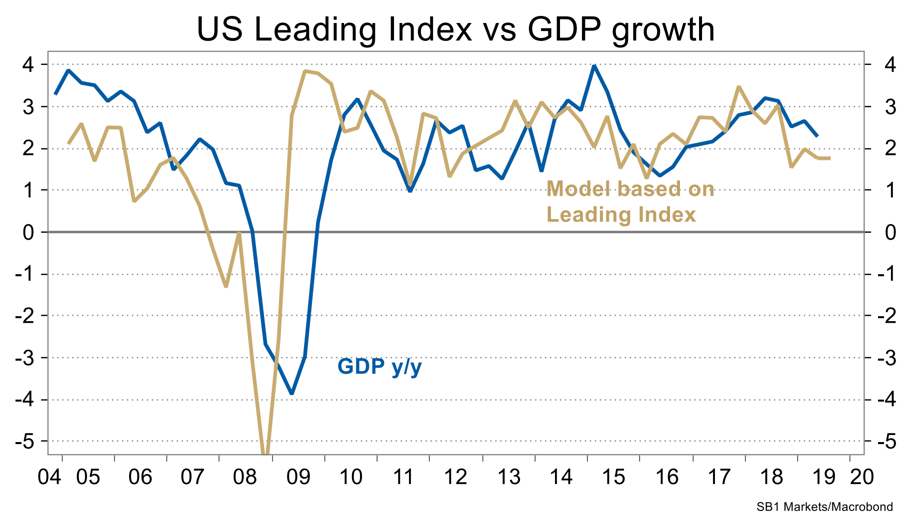
- A more than 15% increase in jobless claims (measured by the 8 week avg) is usually a good indication of a recession, and a yellow ‘recession’ warning line is to be drawn, check the chart to the left. So, no reason to worry now?

The Leading indicators softened in Aug/Sept

LEI has indicated a slowdown for a long time but not an abrupt one, just to some 1.8% GDP growth





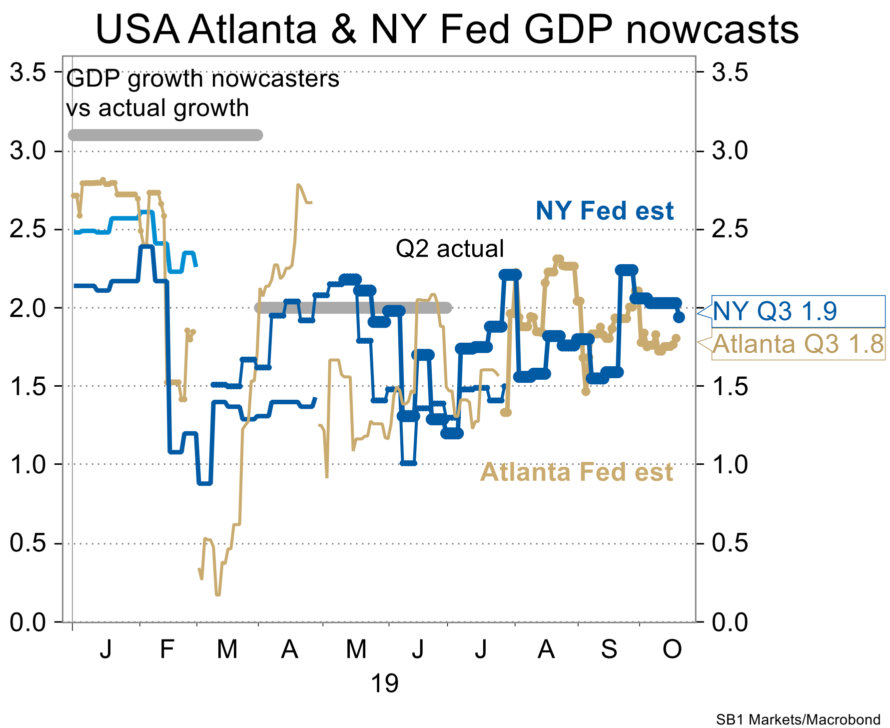


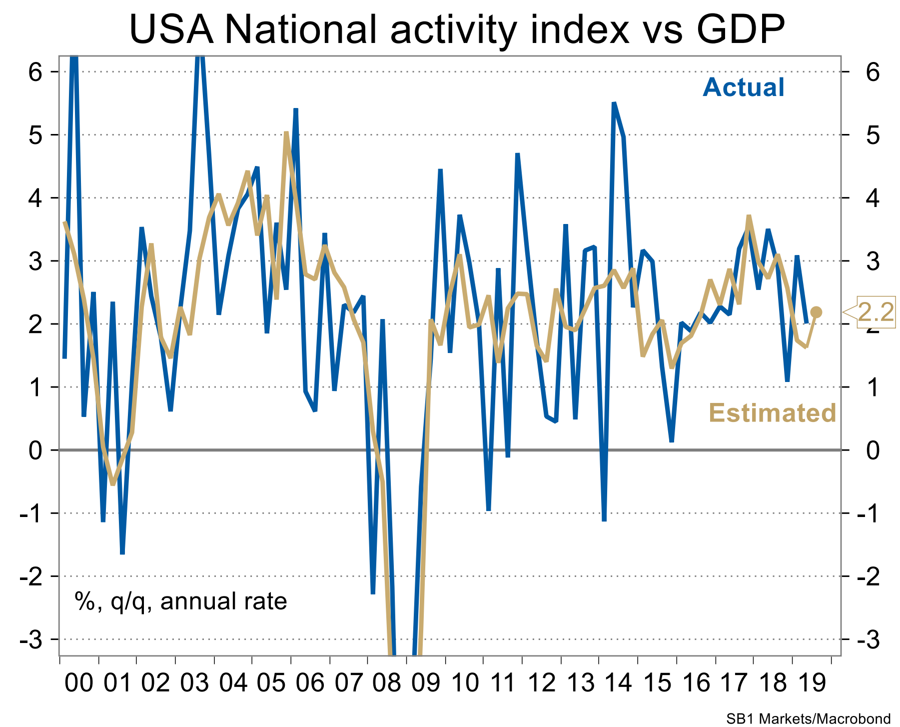
- Conference Board's Leading indicators fell 0.1% m/m in Sept, and Aug was revised down to -0.2% m/m, from 0. The 6 m average m/m growth is up just marginally
  - » The ISM and building permits (from a high level the past month) dragged the LEI down in Sept, stock market and credit the major positive contributions
- Face value, the LEI is signals just below a 2% growth rate

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

Nowcasters are signalling close to 2% growth in Q3 as well

The nowcasters are noting 1.8-2% GDP growth in Q3, the National Activity index at 2.2%





- The NY Feds weekly gauge marginally down to 1.9% last week, Atlanta up to 1.8%. The National index points to 2.2% GDP growth in Q3, from 1.6% last month (and 2.0% reported GDP growth in Q2)

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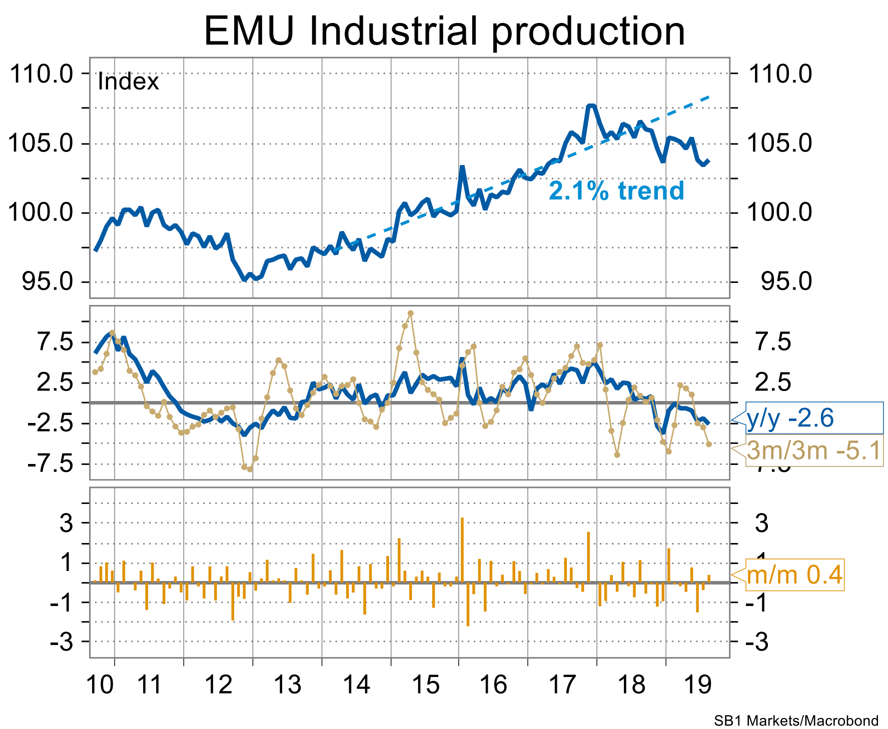
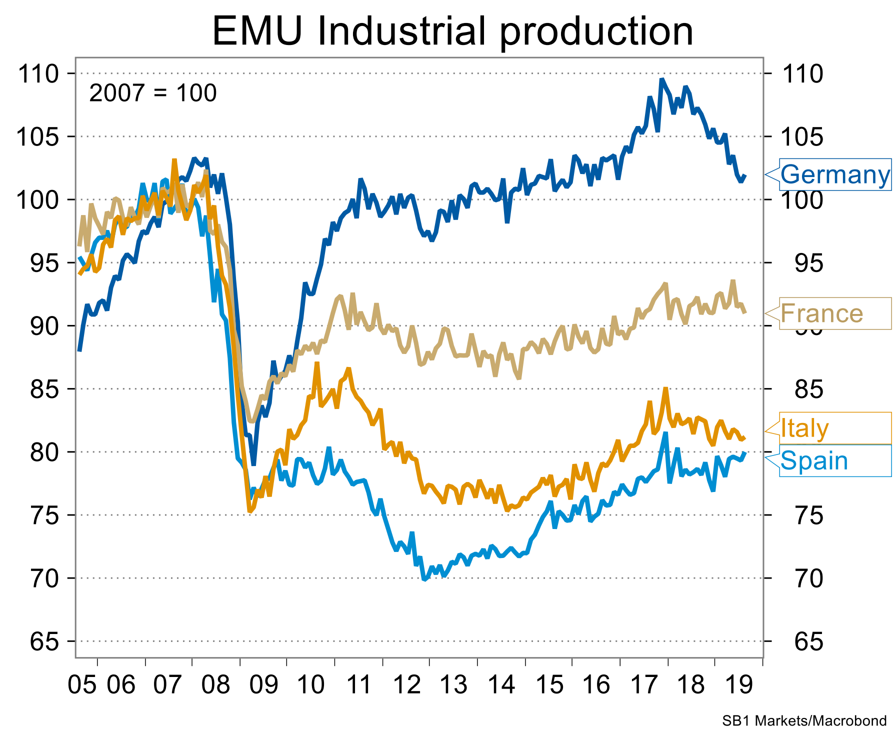
Industrial production slightly up in August, trend straight down

Production ticked up 0.4% m/m, most countries improved. Underlying growth still down 5.1%





- Industrial production (ex construction) in the Eurozone increased by 0.4% in August, we expected +0.2%. The slight recovery in August did not help much, production has fallen 5.1% 3m/3m annualized and the annual rate is -2.6%
  - » Germany inched up in August but the trend is steeply downwards, down 5% y/y (smoothed), and by 7% from the peak
  - » Other major countries are so far holding up better than Germany but not are shining. France has stagnated and production is down 0.7% y/y, Italy slides down slowly, by a 1.2% speed y/y, while Spain is still heading modestly up, +1.4% y/y
- <u>Manufacturing PMI has plummeted, and points to an accelerating decline in production. Orders do not signal any recovery</u>

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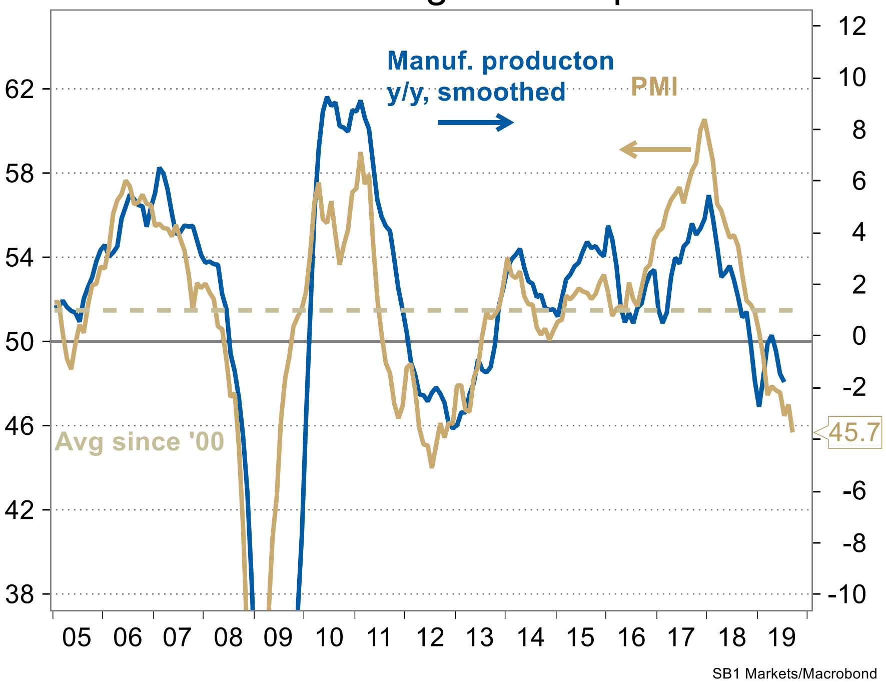
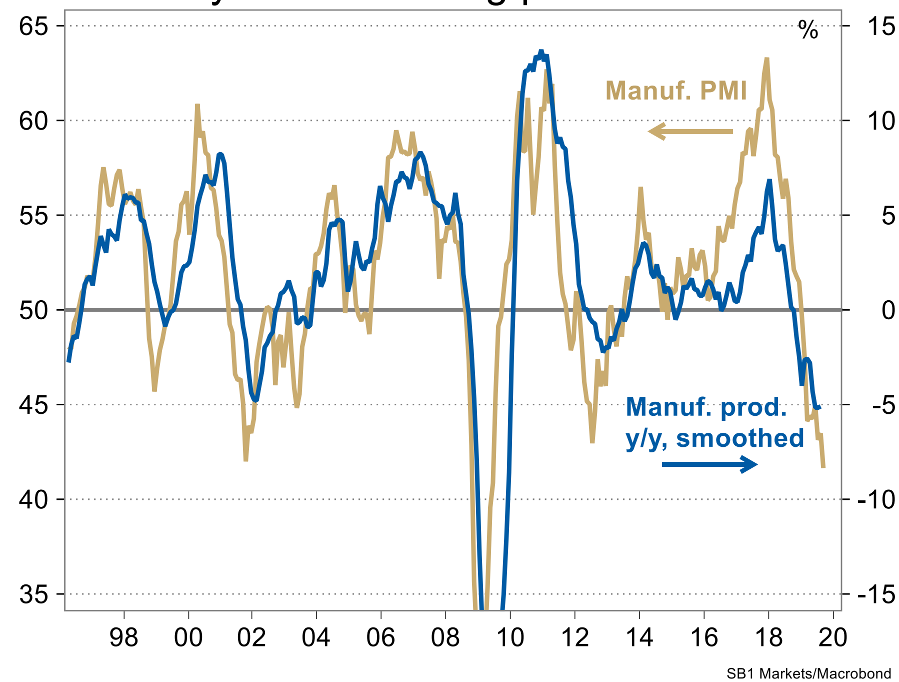
The PMI point to an even steeper contraction. Germany the weakest link

The outlook is not bright, according to manufacturers

EMU Manufacturing PMI vs. production



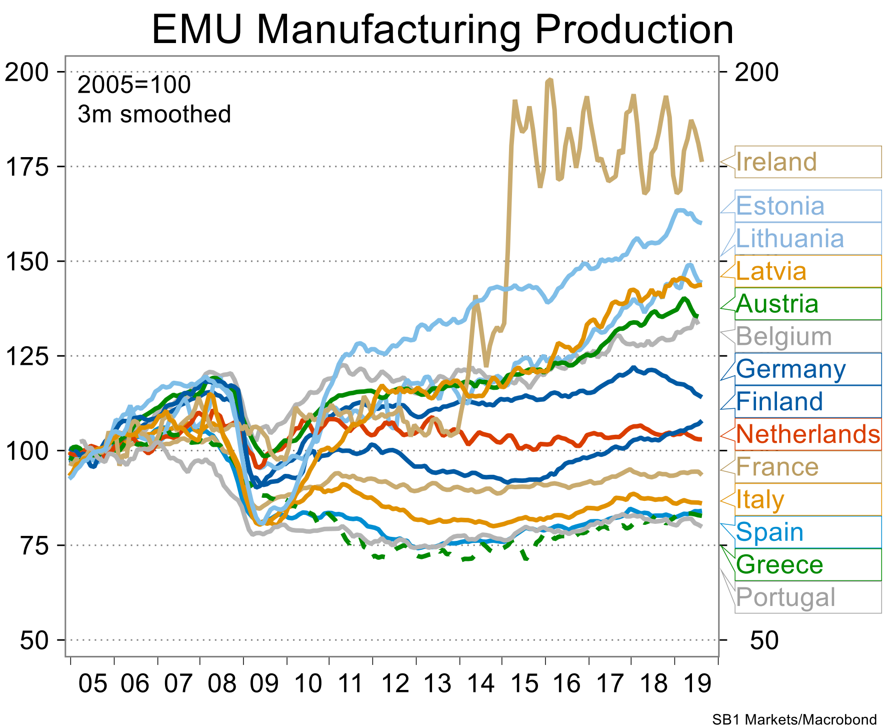
Germany Manufacturing production vs PMI

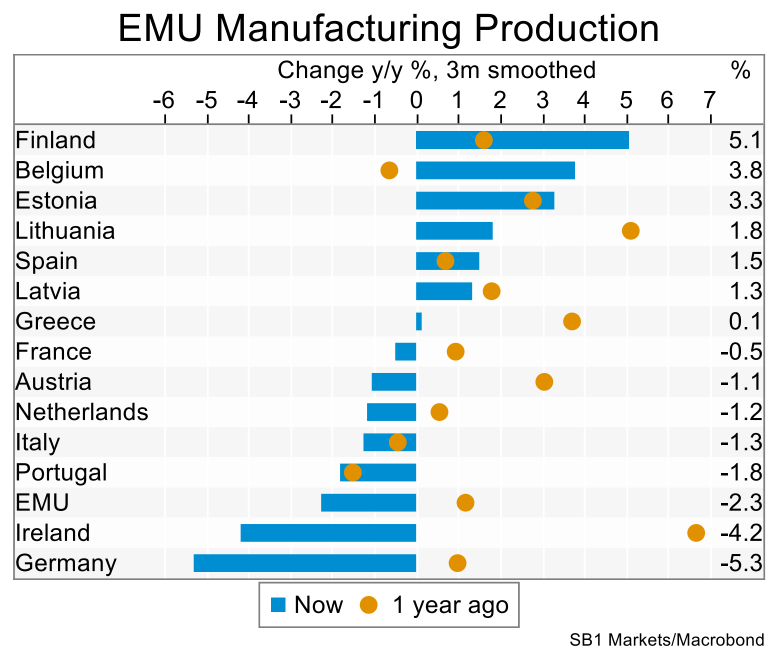


- The German manufacturing PMI signals the sharpest downturn since the financial crisis

Just Eastern Europe is thriving, Germany struggles the most

Production is falling in Germany, Ireland, Netherlands, Portugal, Italy, Austria and France





- Production is still up y/y in 6 of 14 countries, with Finland in the lead. Just 4 countries have been accelerating recent months, 10 countries are slowing or declining
- The slowdown has been rather broad among sectors, check the next slide

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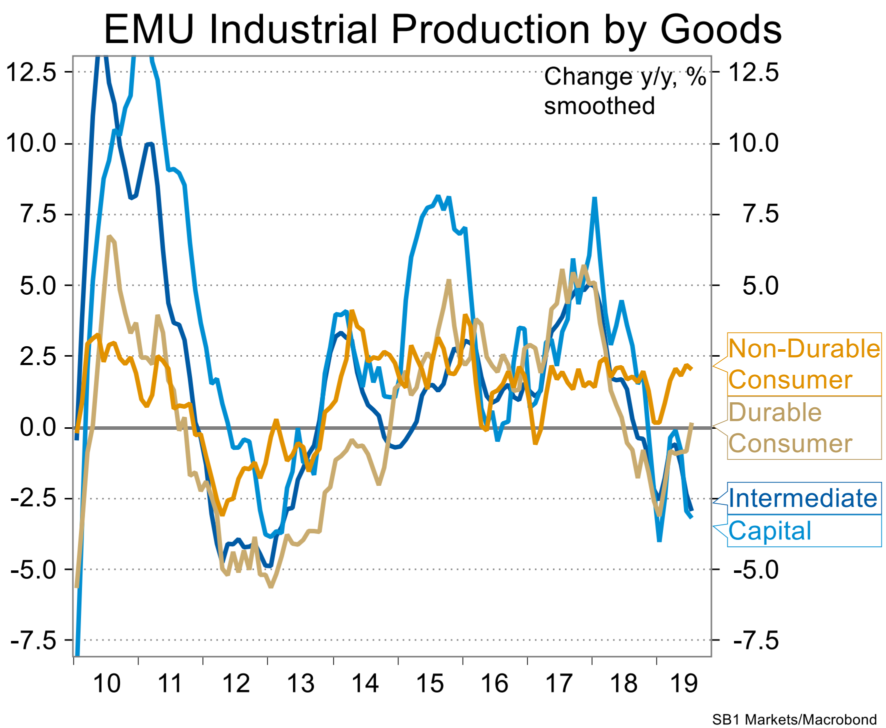
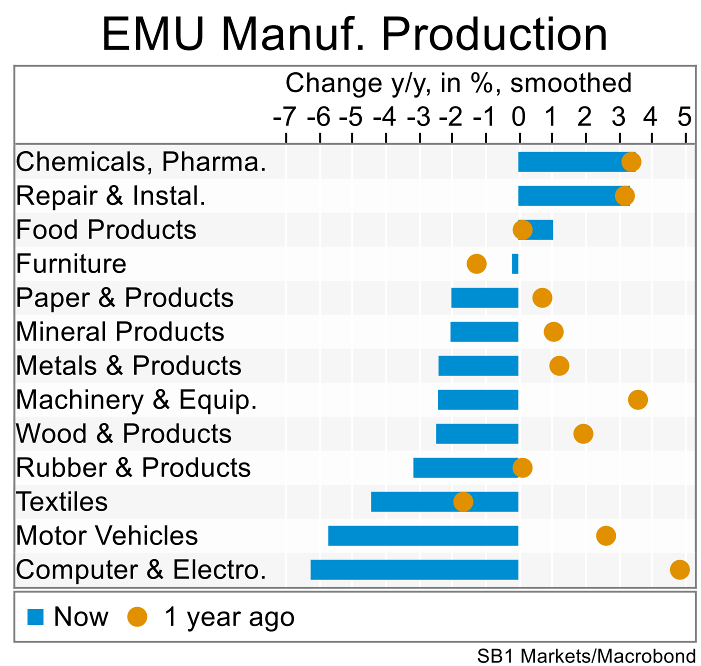
A broad downturn among sectors, yet consumer goods are holding up okay

Sector details mirror the gap between manufacturing & services, but few are thriving

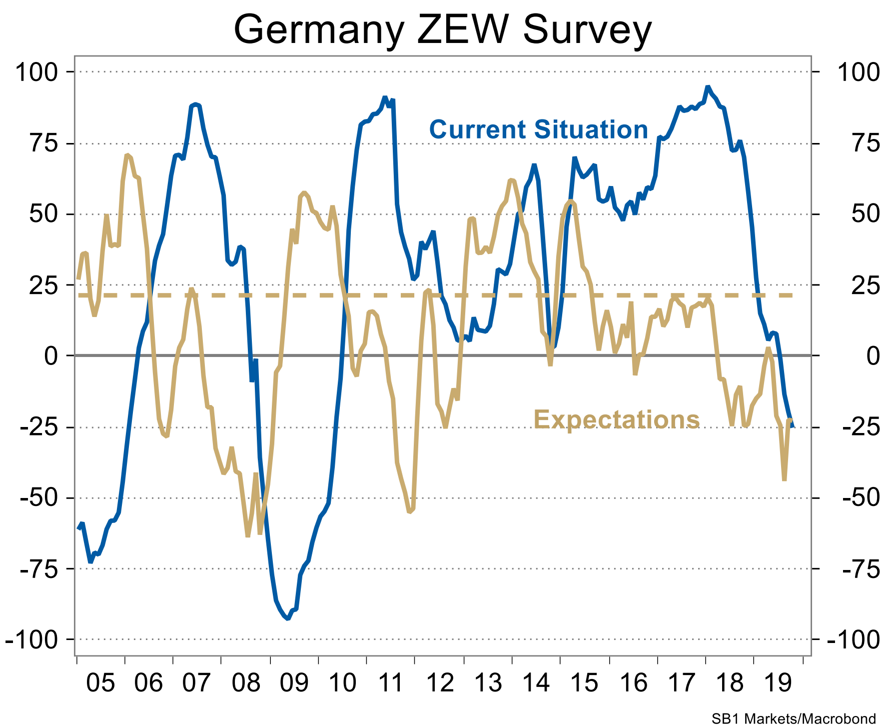


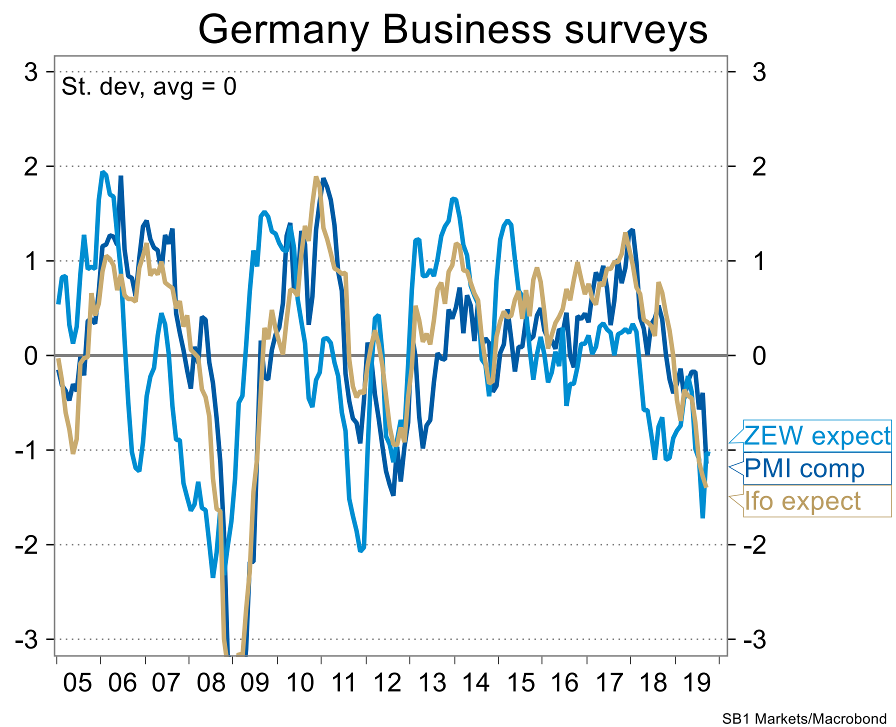


- In August, 9 of 12 manufacturing sectors were declining y/y (3m smoothed) and just 3 growing, a substantial deterioration from one year ago. Auto production is falling steeply but the downturn is no doubt broad

ZEW survey expectations steady in October, view of the current sit. weakens

Investors & economists view of the current situation fell to a 9 ½ year low

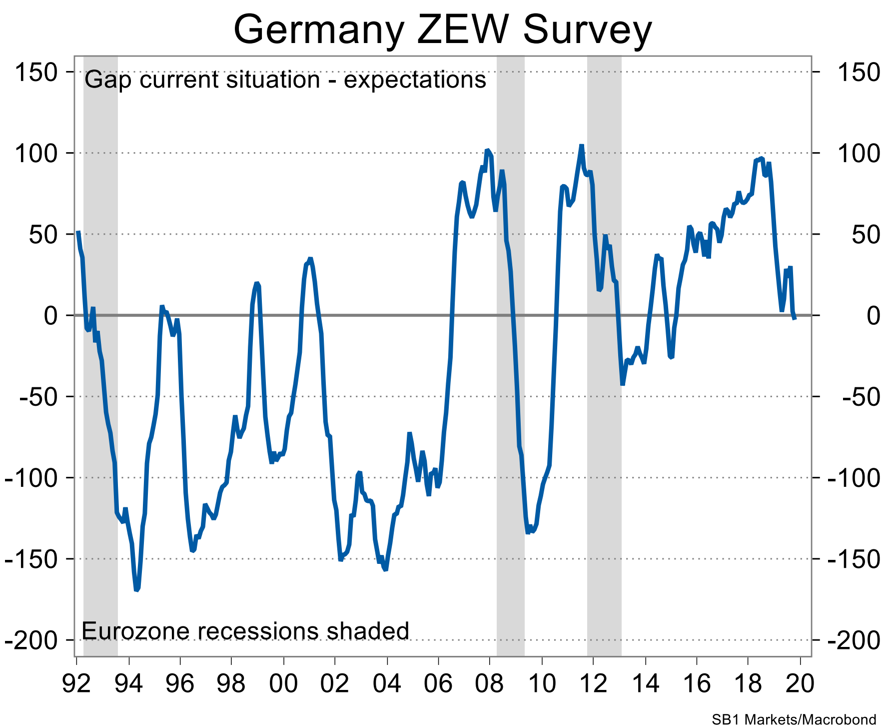




- An intensified trade dispute, Brexit turmoil and subpar domestic data flows, have been darkening the economic outlook. In October, the ZEW survey noted unchanged expectations, at a below average level. The assessment of the current situation came further down, down to a 9 ½ year low
  - » The ZEW survey do not signal any recovery in the German economy, neither do other surveys. The ZEW is a sentiment survey and not a business survey, as the PMI and Ifo. ZEW is usually leading the Ifo and PMI – however with a rather weak correlation. We prefer the business surveys
- All German surveys are pointing to a bleak outlook; the PMI (composite), Ifo and ZEW are more or less in sync

The gap between the ZEW current situation and expectations is not promising

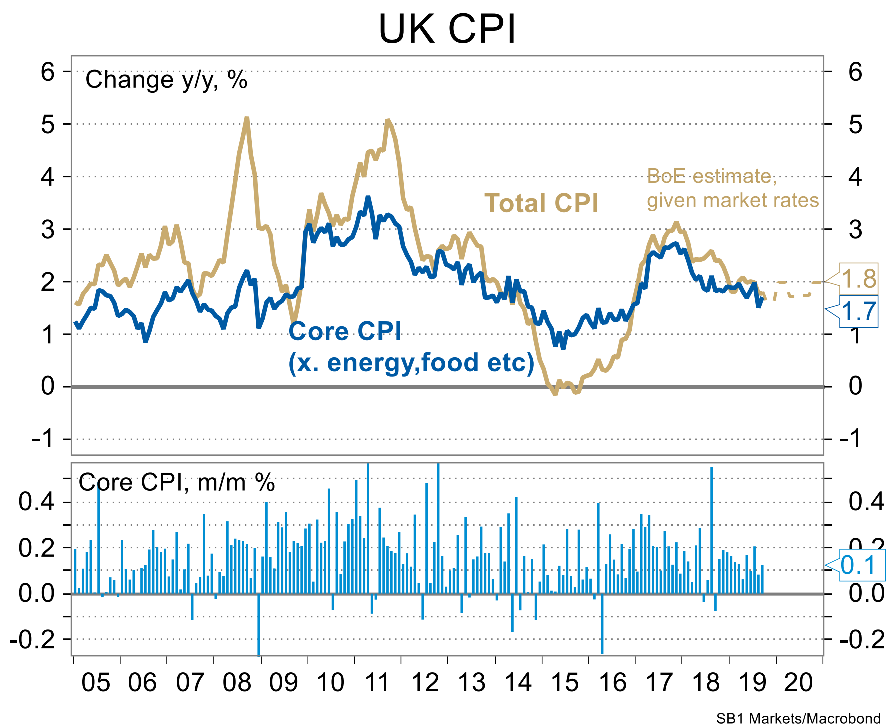
Surely, 3 observations are not sufficient, but still..

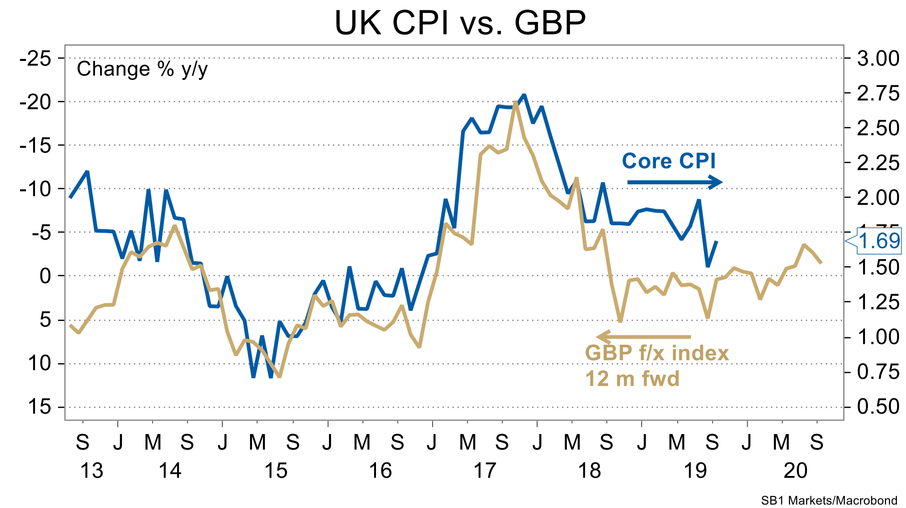


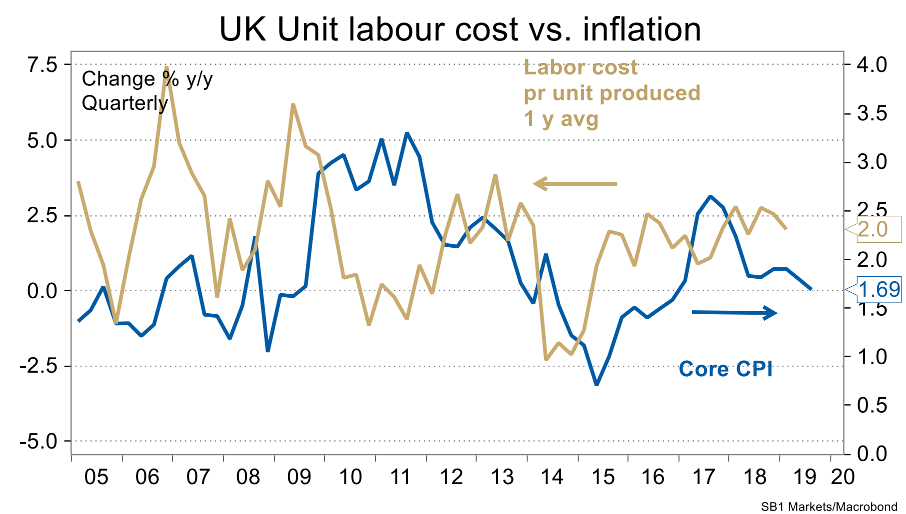
- Just before recessions hit (the 3 recessions since 1990 at least), the expectations component of the ZEW survey has fallen steeply, while the view of the current situations remains elevated. During the recession, the current situation assessment follows expectations down. Hence, based on data before/during the past 3 recessions, we should already be in a recession now
- We highly doubt the EMU is in a recession now, as parts of the economy are holding up well in spite the manufacturing dip; the consumer sector is still growing moderately, credit is increasing and overall unemployment is still declining

Core CPI inflation recovered but just to 1.7%, trend tilting downwards?

The (2016) GBP impact is probably taken out. Core inflation just below target, total inflation at 1.8%



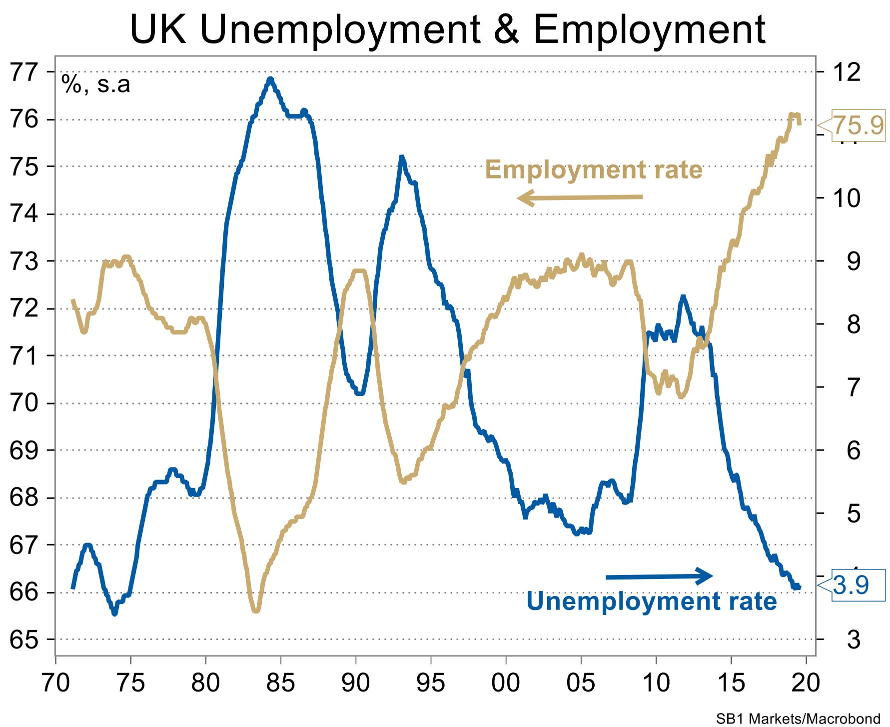


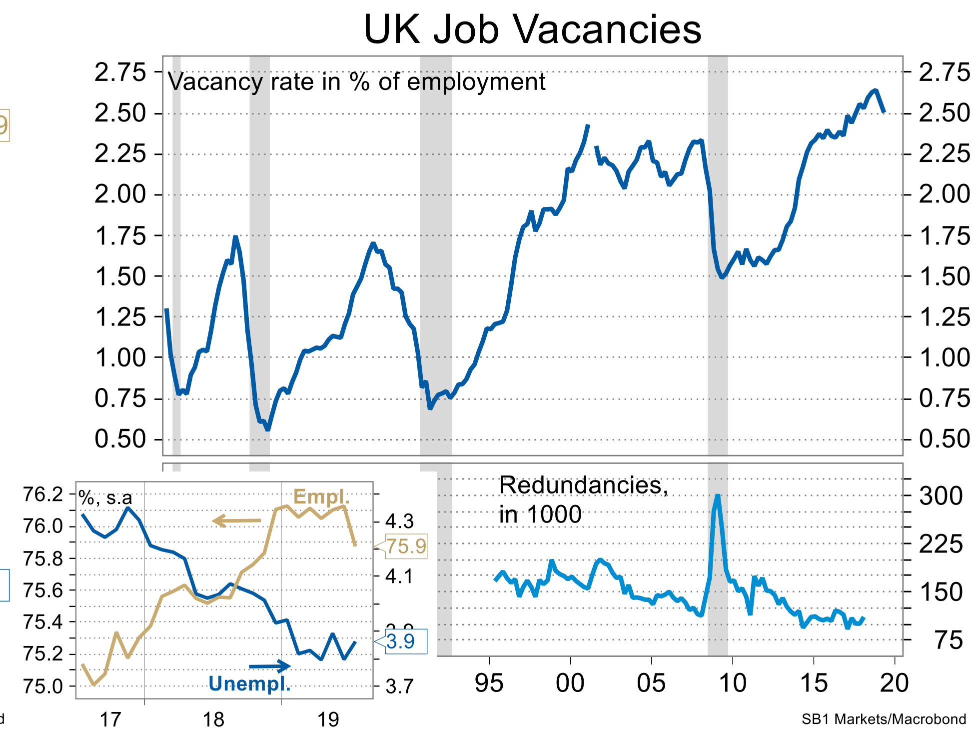


- Core CPI rose just 0.1% m/m in Sept, and just 0.2 p of the 0.5 pp Aug drop (base effects) was reversed. Core inflation may be heading slowly down, just below the BoE's price target. Total inflation was flat at 1.8% this month
- Inflation came down through 2018, as the upward pressure from the GBP depreciation in 2016 changed sign. Our simple f/x based model does not indicate much lower inflation. Moreover, dome-stic cost inflation is not low, and wage inflation has climbed to 4%

Unemployment rose, employm. fell; Brexit slowdown hitting the labour market?

Unemployment edged up 0.1 pp and employment dropped 0.2 pp. And wage growth flattens out

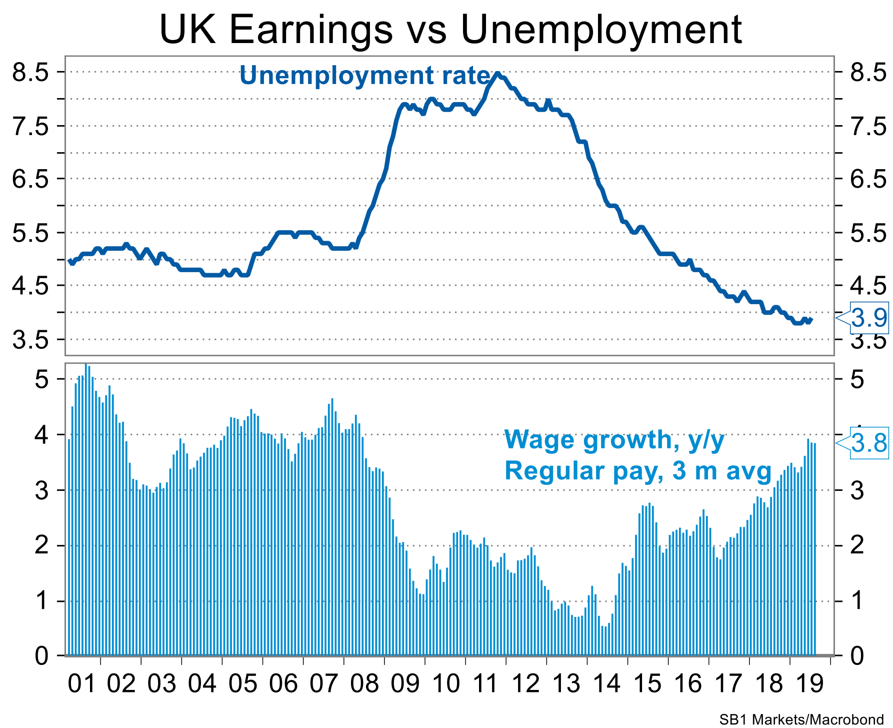


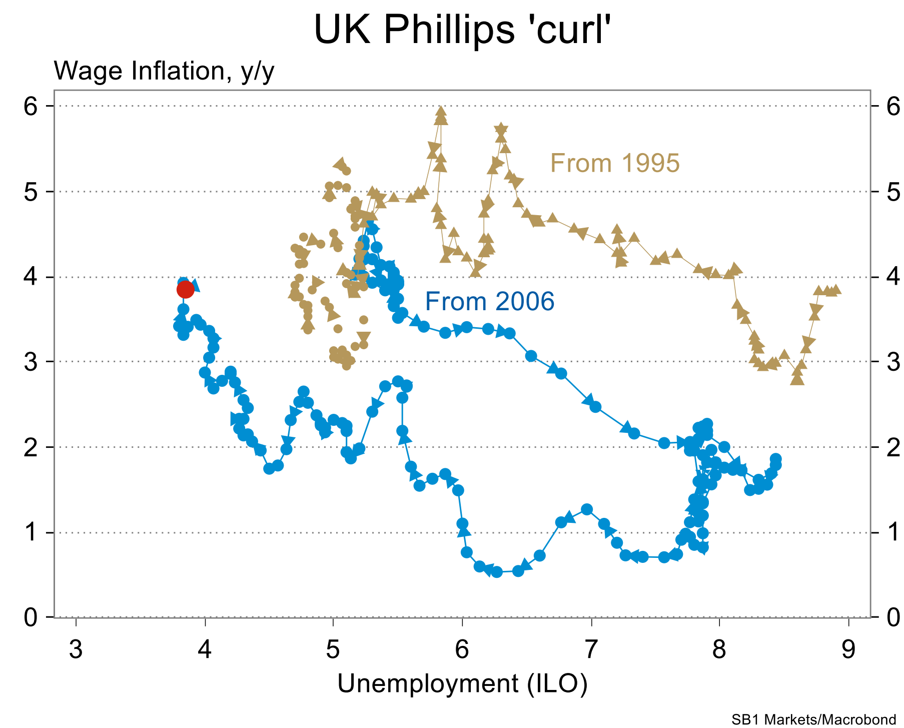


- Unemployment (LFS/ILO) ticked up to 3.9% in July (avg June-Aug), expected unchanged at 3.8%. Unemployment has flattened out since early 2019, at the lowest level since 1974
- The employment rate fell to 75.9%, a 0.2 pp decline. This is the largest monthly decline since 2009. May be a one off but the employment rate has anyway flattened out since January, due to supply constraints or lack of demand? The vacancy ratio is just slightly down from a record high level (Q2 data). Wage inflation is approaching 4% (check next page)
- In sum: these data may signal that the labour market is now at a turning point, probably triggered by Brexit troubles

Wage inflation was accelerating; unchanged at 11 y high the past 3 months

A tight labour market has been boosting wage inflation, at peak now?



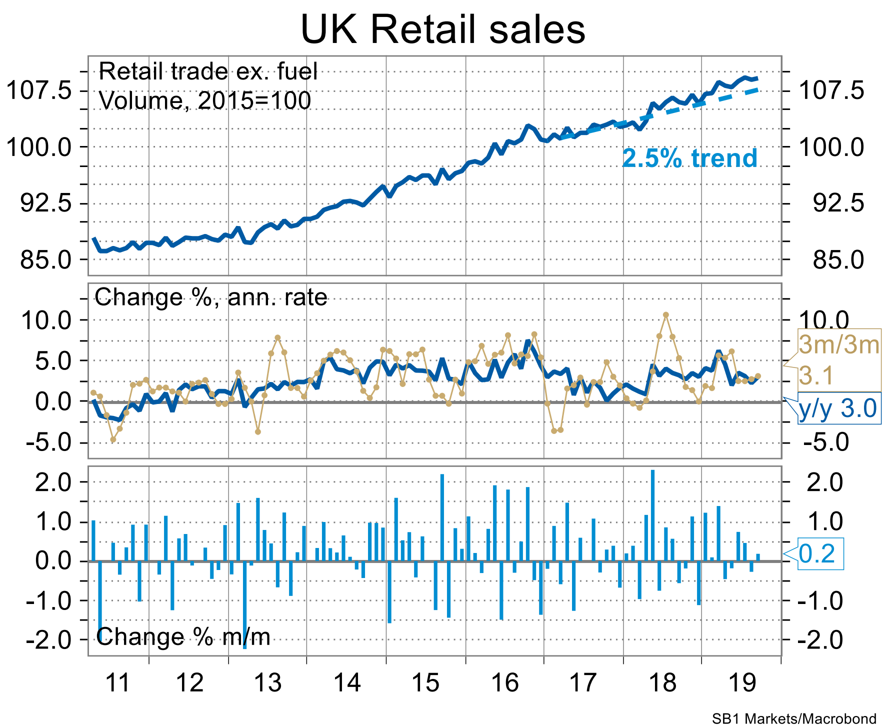


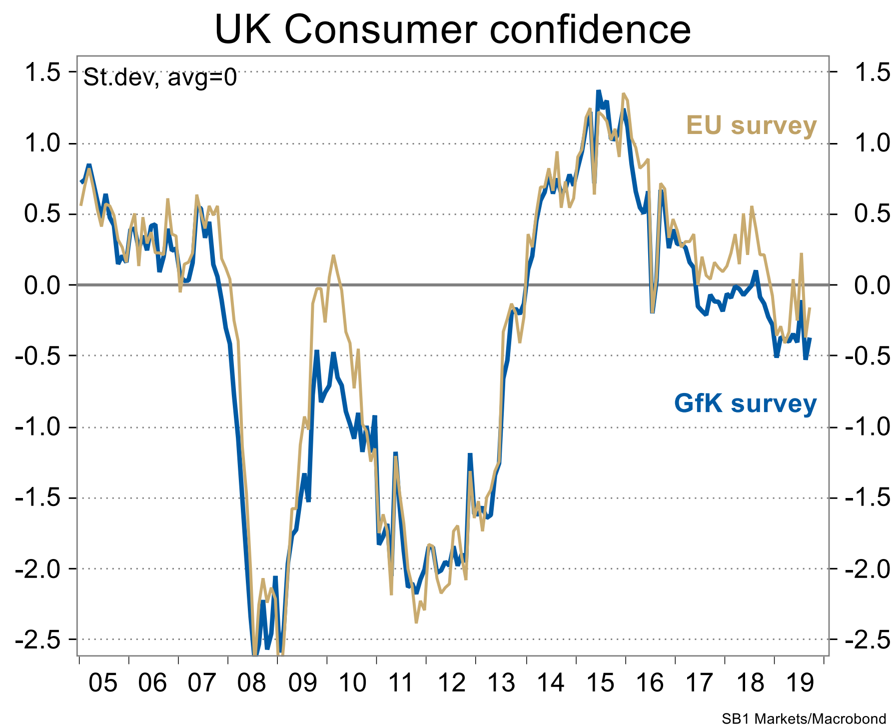
- Wage growth (regular pay) was flat at 3.8% y/y in August, or down 0.1 pp after adding a 3 m smoothing. Wage inflation was heading straight up but it has not accelerated further the past 3-4 months
- UK productivity growth is still well below 1%, and unit labour cost inflation was running at 2% in Q1. Cost pressure is not muted!

SpareBank 1 MARKETS

Retail sales still growing above trend

Sales rose 0.2% m/m in Sept & 3.1% in Q3. Confidence still below par

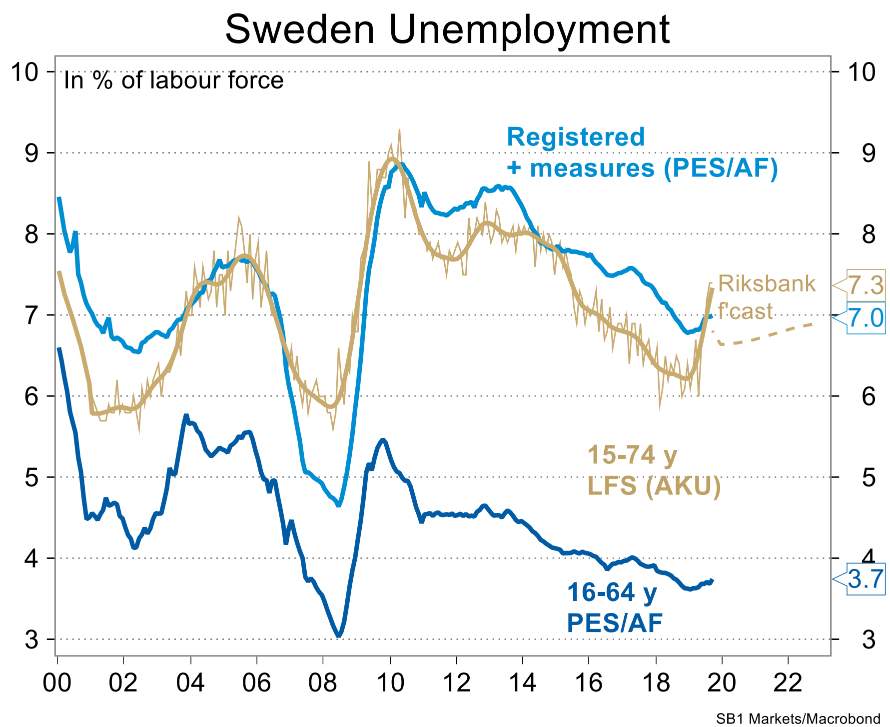


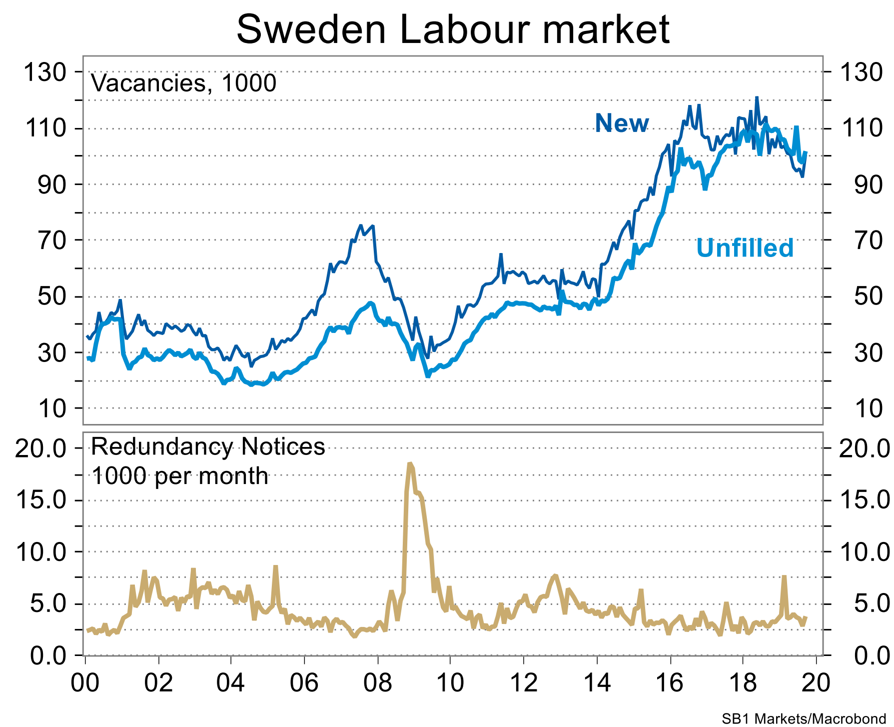


- Sales were a tad better than expected in September, up 0.2% m/m and Q3 came in solid at 3.1% annualized. Growth is running above the 2.5% trend path from 2017. <u>The best UK data point at hand?</u>
  - » High employment and rising real wages are helpful. However, over the recent years, consumption has also been fuelled by a sharp decline in household savings. Given the drop in savings, the risk is on the downside
- Consumer confidence has trended down since 2016, even if the labour market has been strong. Confidence improved slightly in September, probably helped by hope of a Brexit deal. The level is not far below average

Unemployment is soaring but the upturn has been overestimated

LFS unempl. remained elevated at 7.4% in Sept, however, SCB warns of data quality issues

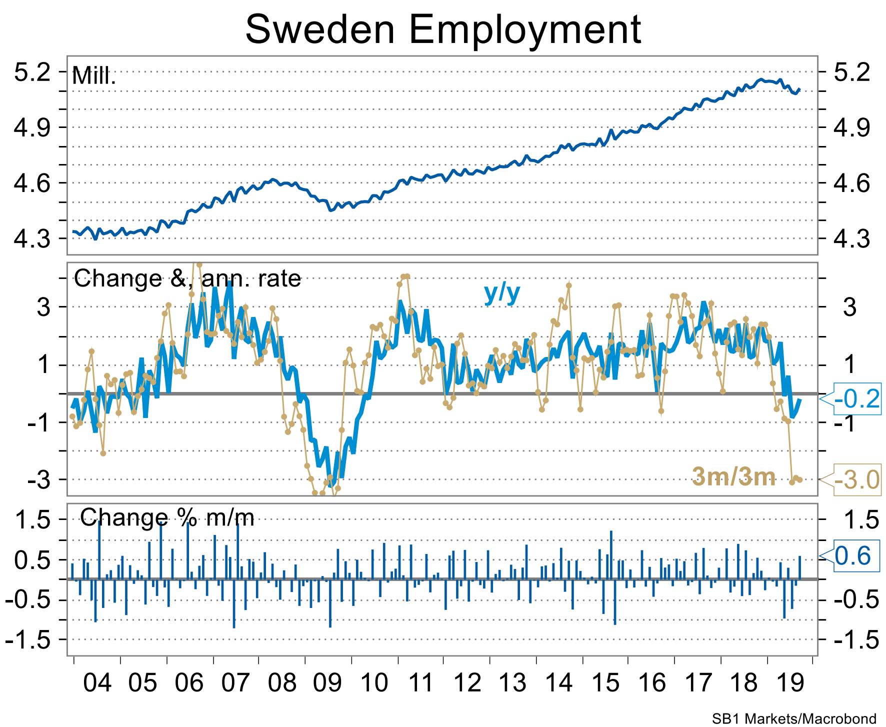


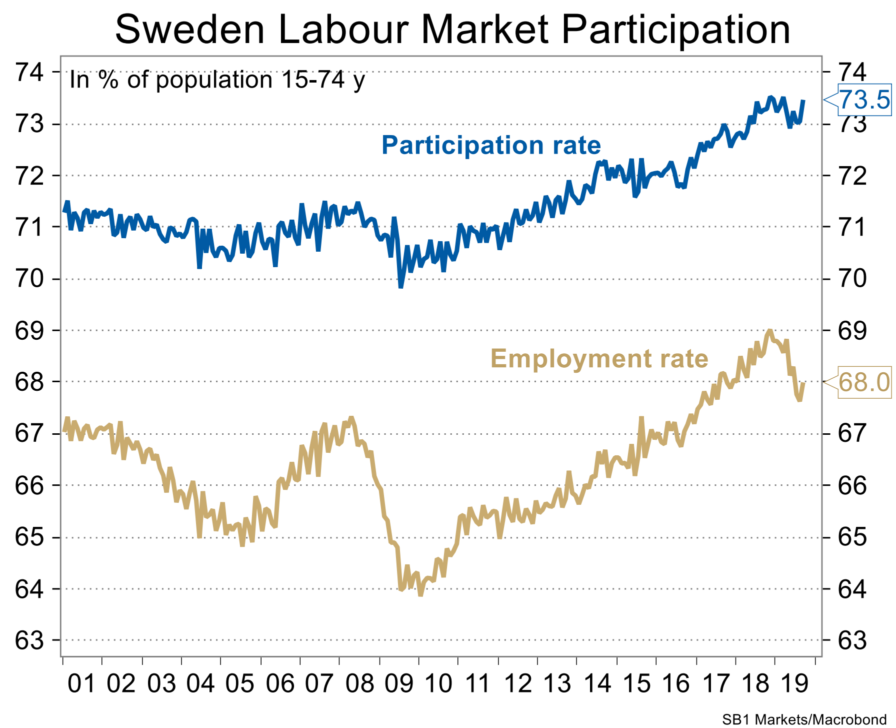


- LFS unempl. rate was unchanged at 7.4% in Sept (avg Aug-Oct), the highest level in 4 y and well above expectations. The smoothed rate, which we prefer, rose to 7.3%, up from 6.3% in early 2019. However, the Statistics Sweden reports data quality flaws, running back to 2018, resulting in an exaggeration of the increase in employment in the first half of '19 and then overestimated the decline in empl. and increase in unempl., but just the past 3 months. Thus, the labour market softening have started earlier than reported but the sudden weakness recent months has not been as rapid as reported. The SCB is working on revising data. Regardless, unemployment is no doubt increasing and it started in H1
  - » Employment is cooling, even if the recent drop is overestimated. Check our estimate on adjusted data to slides forward
- The PES/AF registered unemployment rate has turned up modestly recent months, confirming that the labour market is weakening somewhat

Employment is slowing but not as steeply as reported

Employment rates have fallen, and much more than participation recently, bringing unempl. up

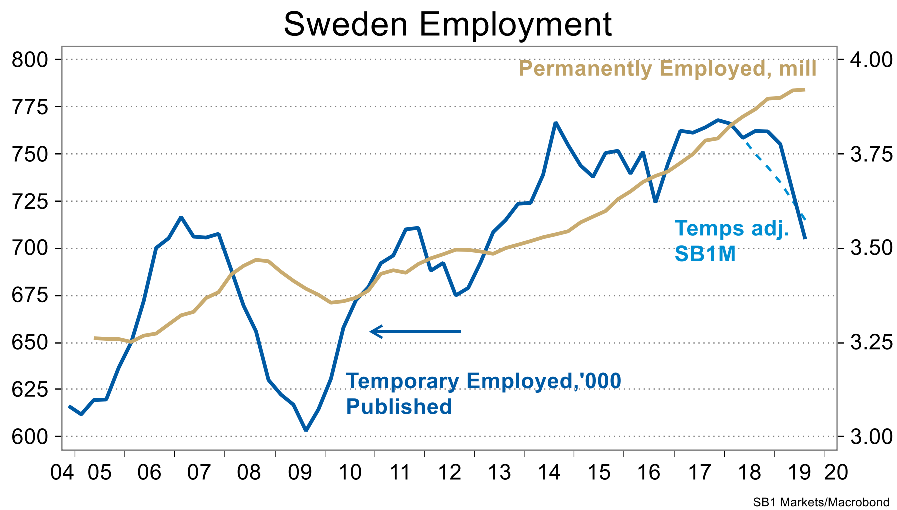


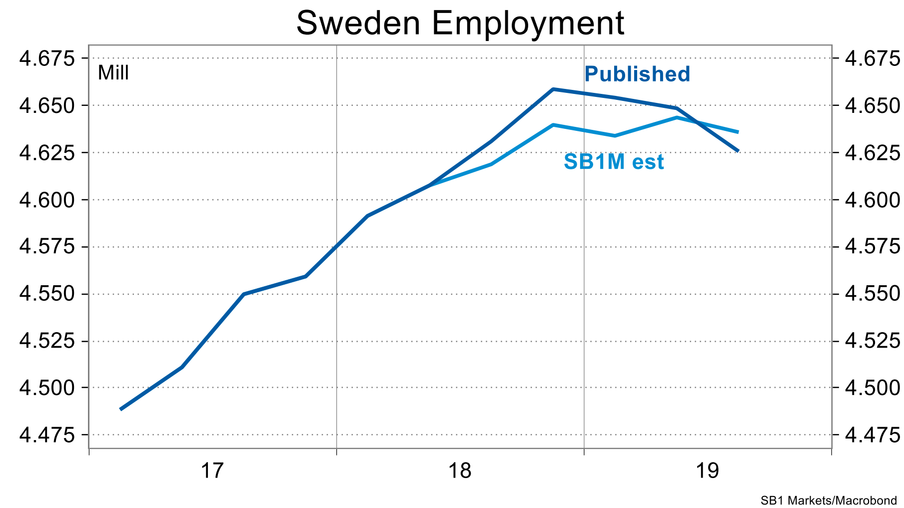


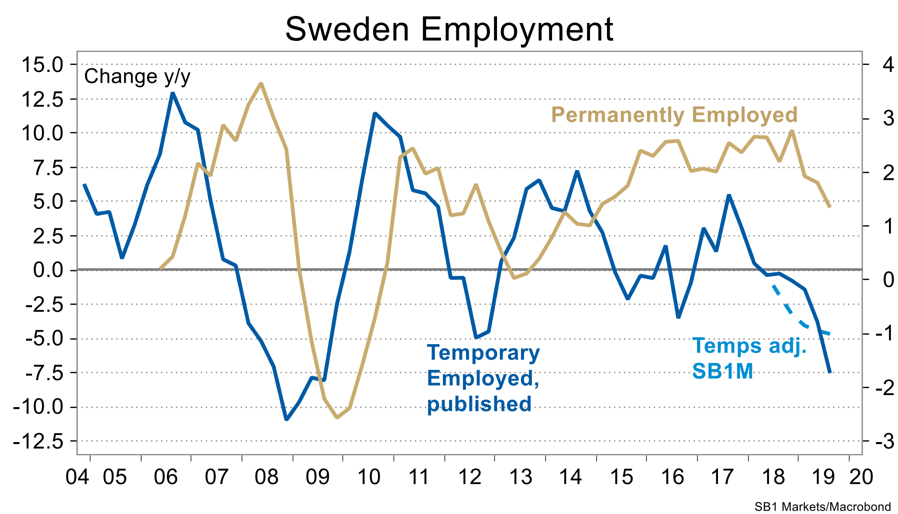
- Employment increased by 0.6% m/m in September but underlying growth is down 3% and the annual rate is -0.2%. According to Statistics Sweden, the decline in employment in July-September may be exaggerated due to the data flaws, which are mainly stemming from an overestimation of the number of temporary employed. Nonetheless, employment started retreating in early 2019 and had fallen by 0.7 pp by June (and SCB reports that this decline may have been underestimated)
  - » Check our estimate on the 'correct' employment figures at the next slide
- Labour market participation jumped 0.5 pp in Sept, while the employment rate rose by 0.4 pp

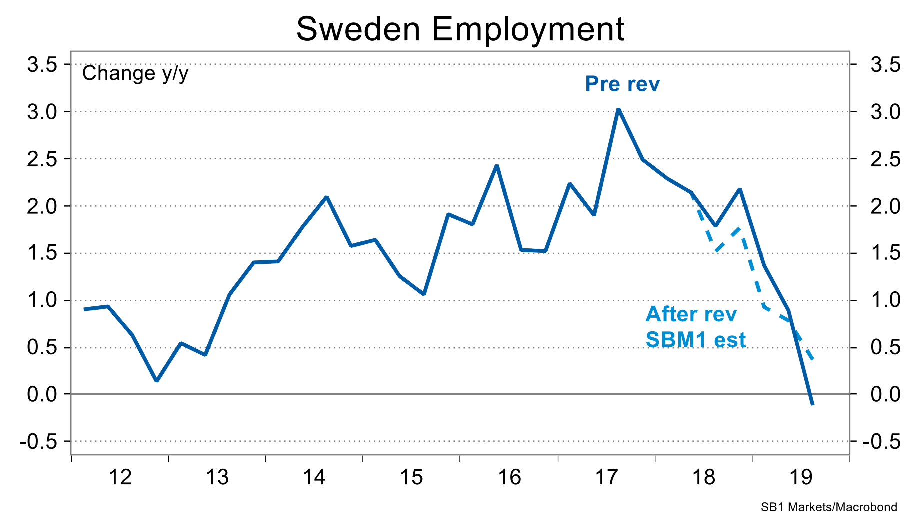
Employment growth has anyway slowed – and the temps are usually leading…

After our rough adjustment of temporary employment figures: A slower slowdown





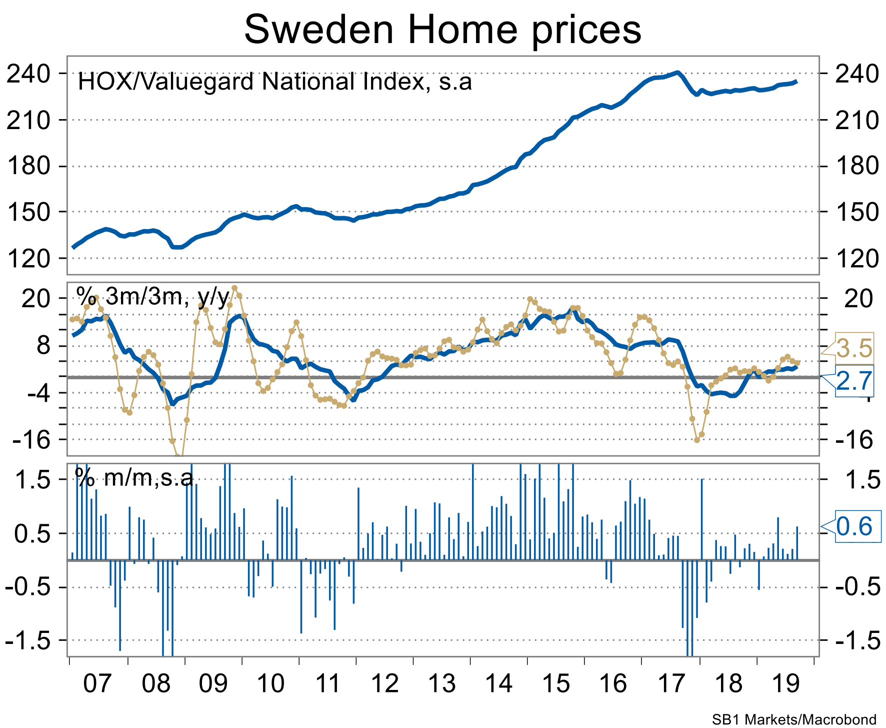


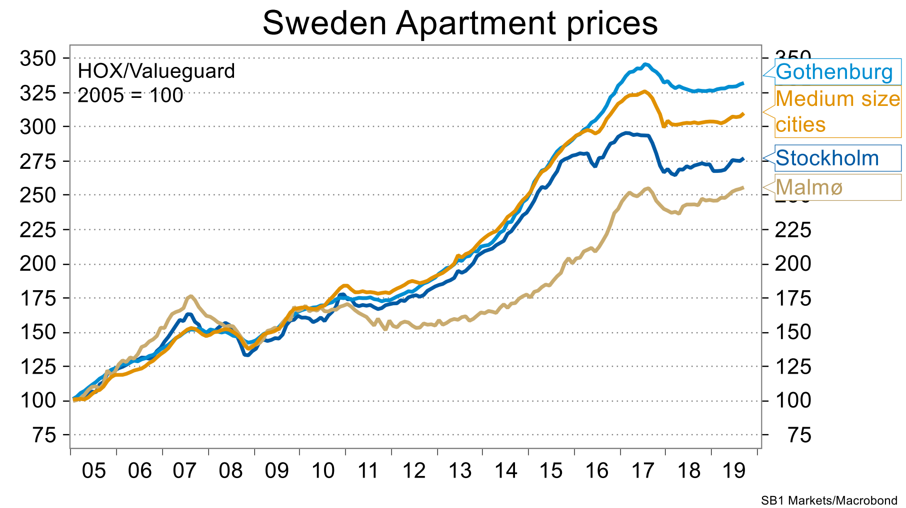


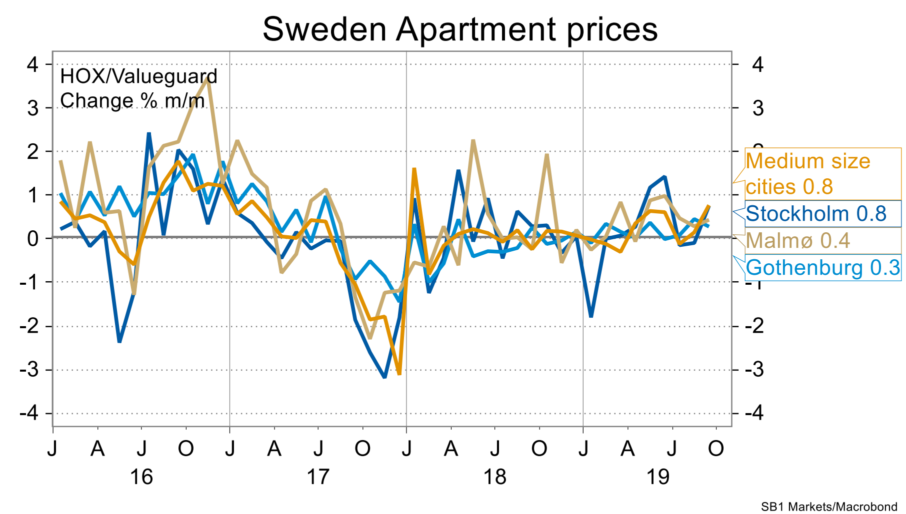
Temp employment is leading permanent employment by several quarters. Now, temp. employment is down 5% y/y (our est)
– indicating downside risk for total employment

House prices jumped in Sept, trending moderately upwards

Prices rose 0.6% m/m seasonally adjusted in Sept, underlying growth at 3.5%





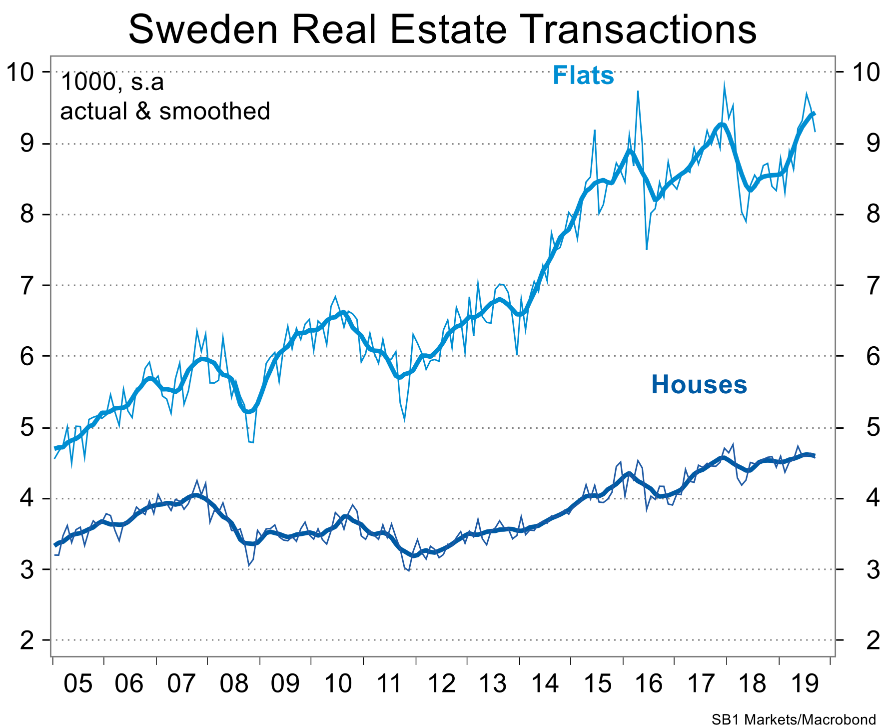


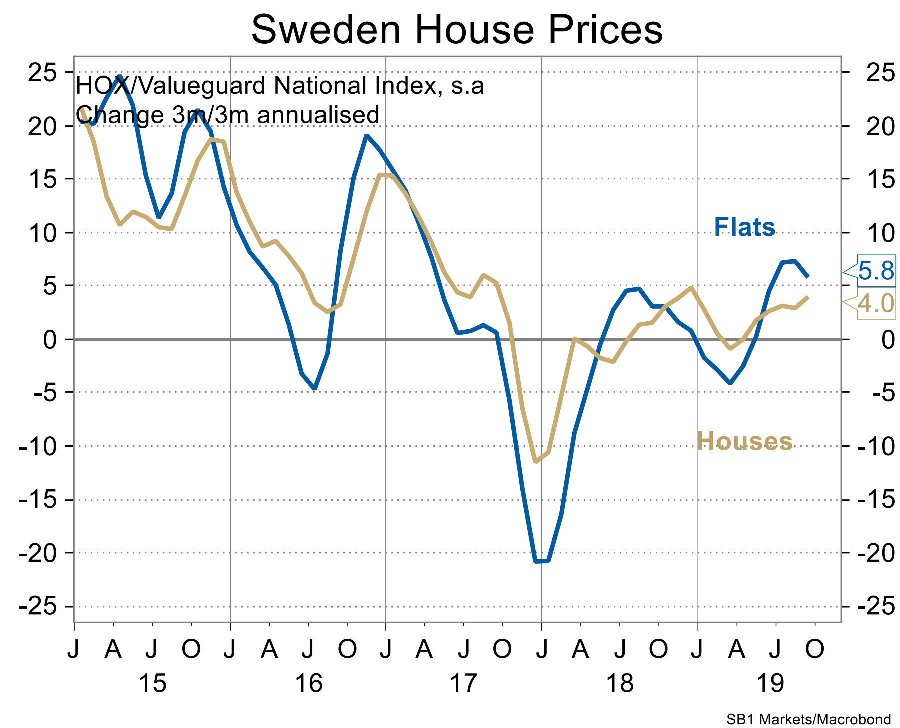
- Home prices rose 0.6% m/m seas. adj. in Sept (0.4% not adjusted). Prices are up 3.5% 3m/3m, and 2.7% y/y and are still 2% below the 2017 peak. Real prices are significantly lower than at that peak
  - » Apartment prices are trending up in all major cities, with the highest growth in Malmø and Stockholm recent months
- The number of transactions is heading up. Still, given recent signs of softness in the Swedish economy, a limited upside?

SpareBank 1 MARKETS

Apartment sales are accelerating, houses slowly upwards

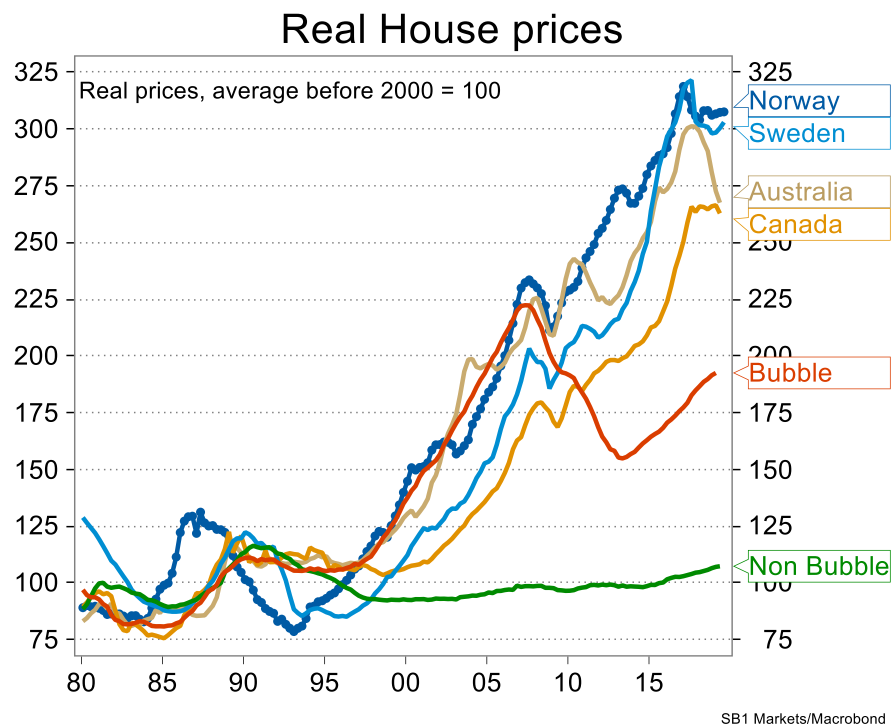
Demand must be strong, number of transactions above 2017 peak

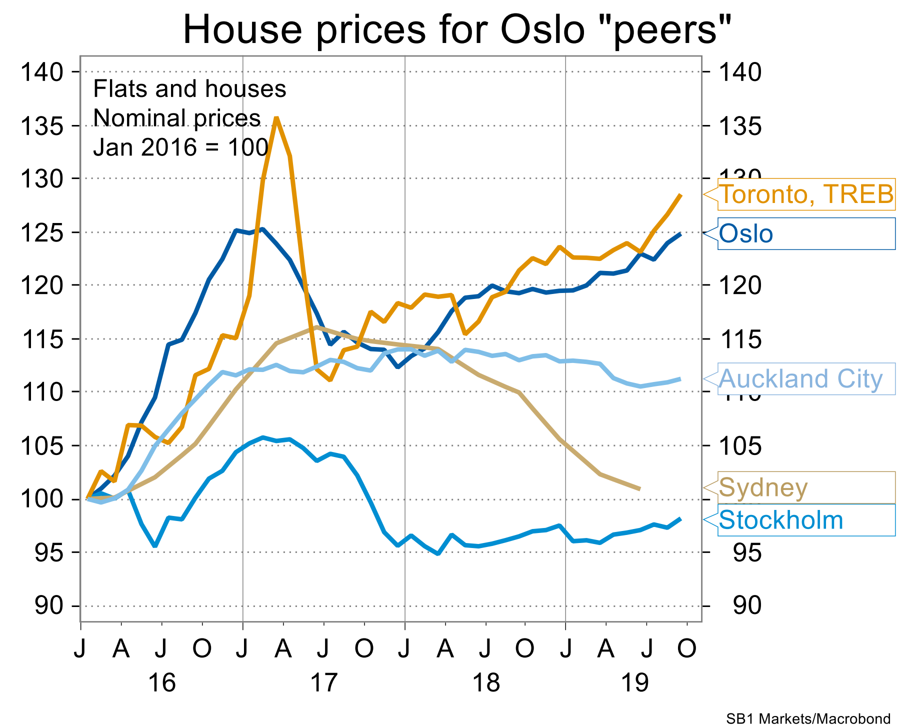




Real home prices have fallen/flattened out in all supercycle countries

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

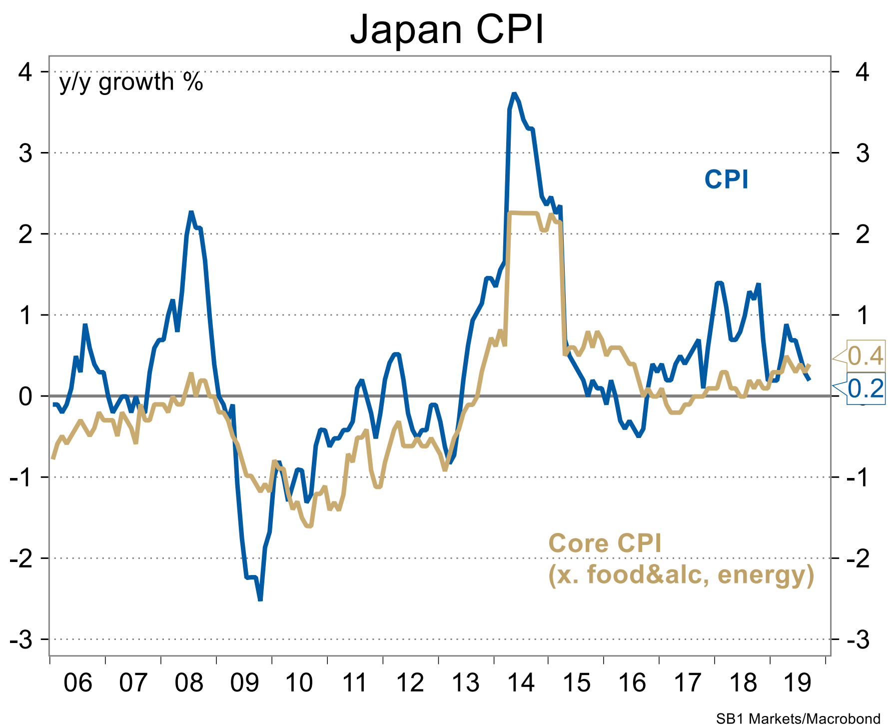


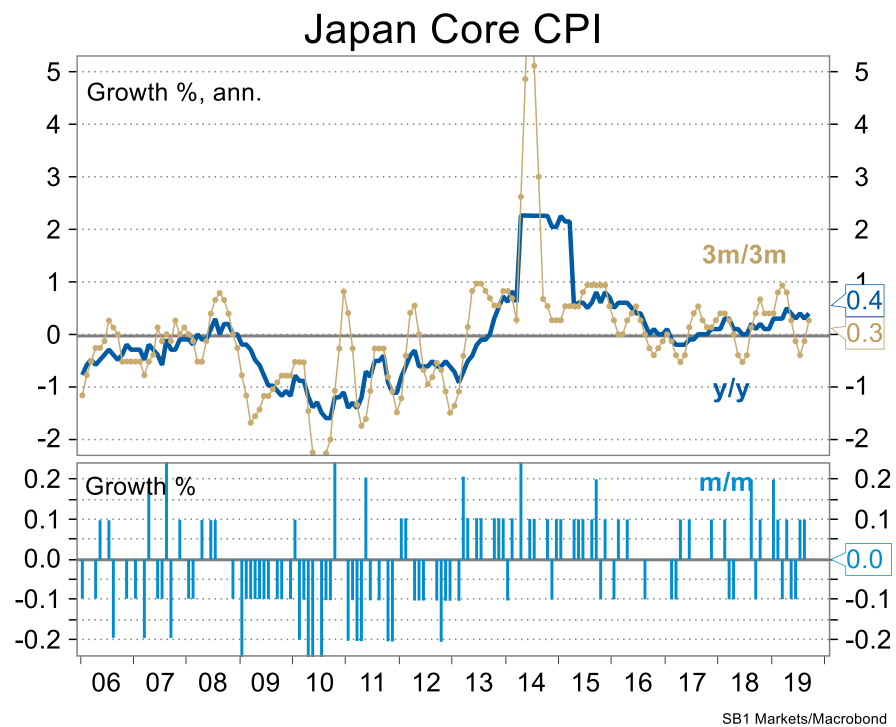


- Mixed among the supercycle guys recently: Oslo is slowly on the way up again, Stockholm slightly up in 2019, Toronto on thw way up again but not as fast as before. Auckland is trending down and Sydney has been falling steeply, down 12% from the peak in Q2 2017, in nominal terms. However, in Australia there are reports on a stabilisation recent months as interest rates have been cut, and lending standards eased!
- New housing market/debt regulations (foreigner buying restrictions, LTV/LTI/mandatory amortisation) – and in Canada higher interest rates – may have created 'some turbulence' – prices in these four countries have slowed/declined since 2017

Core CPI inflation is turning very slowly up

Core prices were up 0.4% y/y in Sept, from 0.3 pp in Aug. Total inflation fell to 0.2%





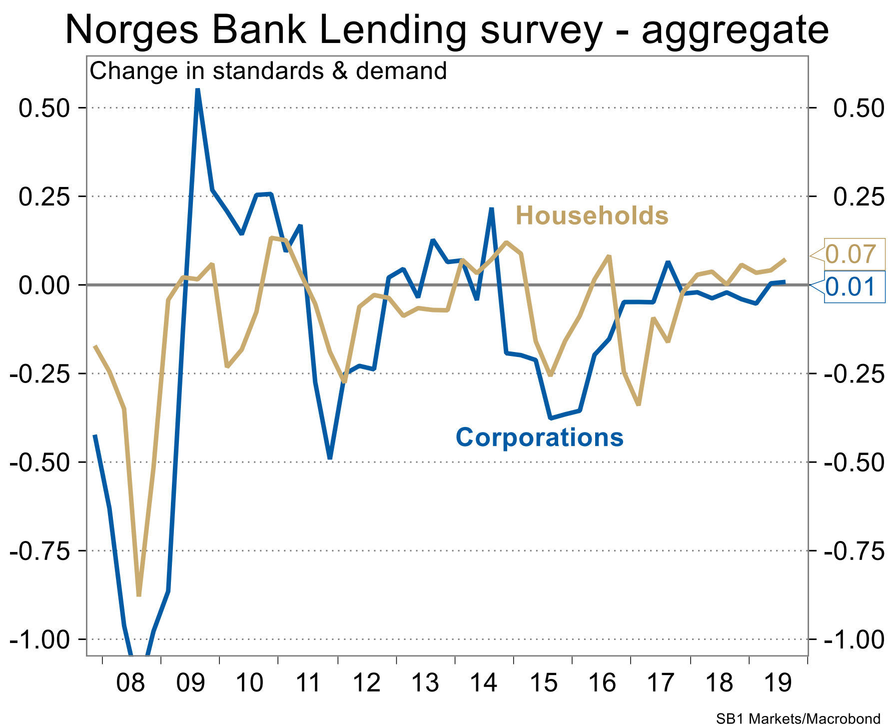
- Total inflation fell to 0.2% y/y. Core inflation is still muted but slowly turning up from the bottom
- Wage inflation has fallen steeply this year and does not indicate accelerating price growth

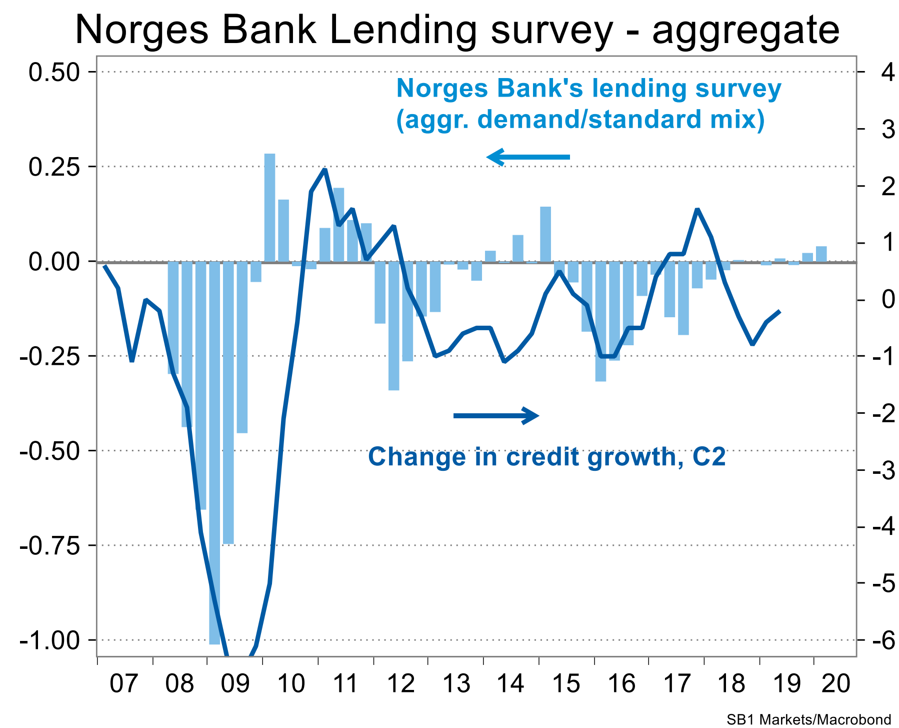
- Highlights
- The world around us
- **The Norwegian economy**
- Market charts & comments

SpareBank 1 MARKETS

Banks expect higher household loan demand in spite interest rate hikes

Banks report a surprising acceleration in mortgage demand in Q3 and expect even more in Q4



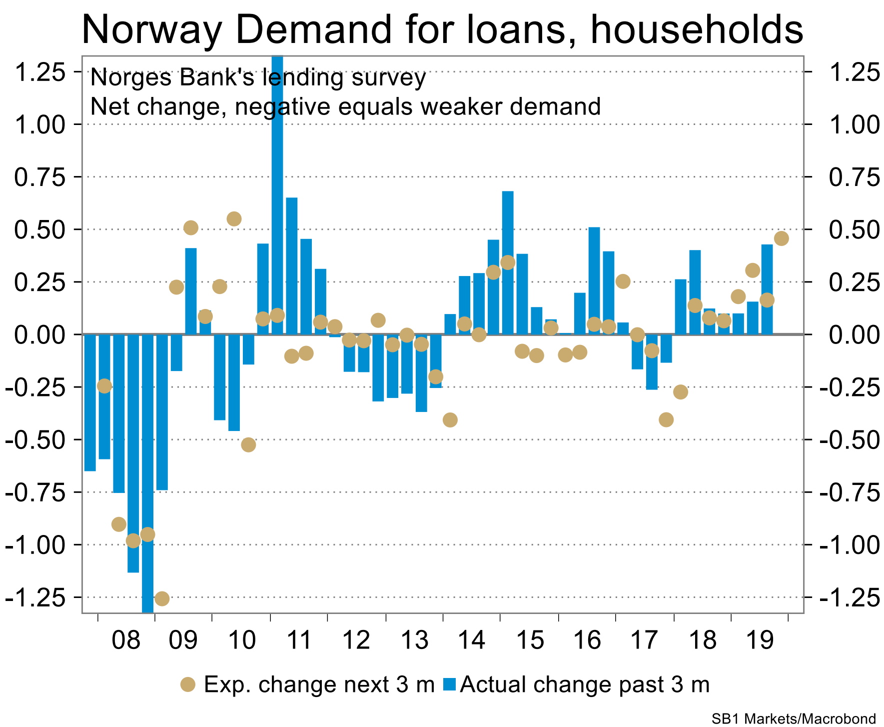


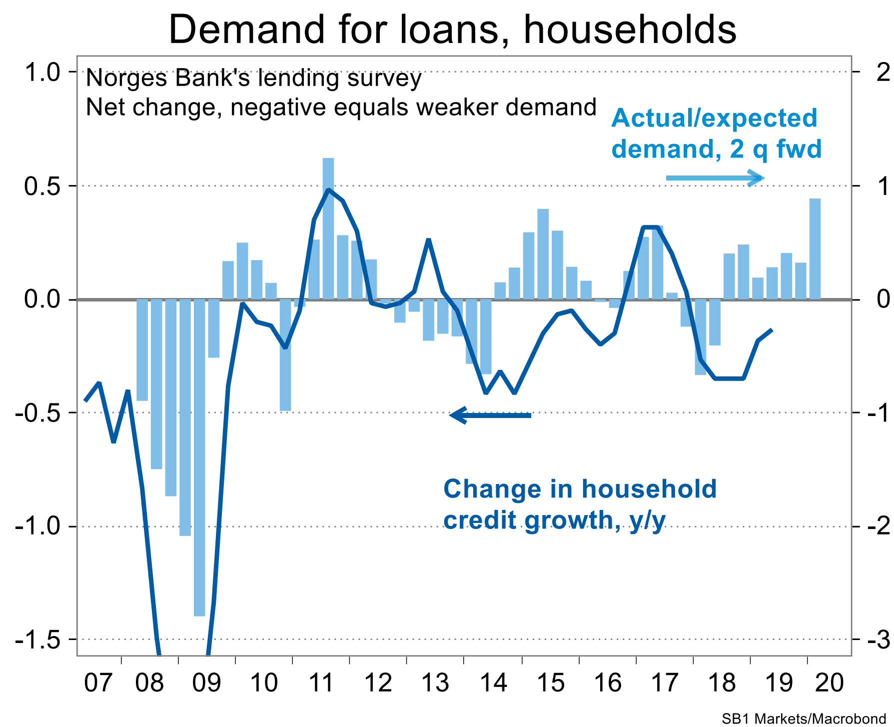
- Banks in Norges Bank's Q3 Lending Survey reports somewhat higher credit demand from households and unchanged demand from the corporate sectors. Our aggregate lending survey indicator (demand + standards reported in Q3 and Q4 expectations, both sectors) has inched up the past 2 quarters, reflecting slightly higher credit demand
  - » Banks report a lift in mortgage demand in Q3, in contradiction to the modest slowdown in actual household credit growth
  - » Credit demand from corporations was unchanged and banks project no changes the coming quarter

Data in this section are seasonally adjusted

If the banks' projections are correct, credit growth will turn up (we doubt so)

Banks report accelerating household loan demand, while actual credit is slowly softening

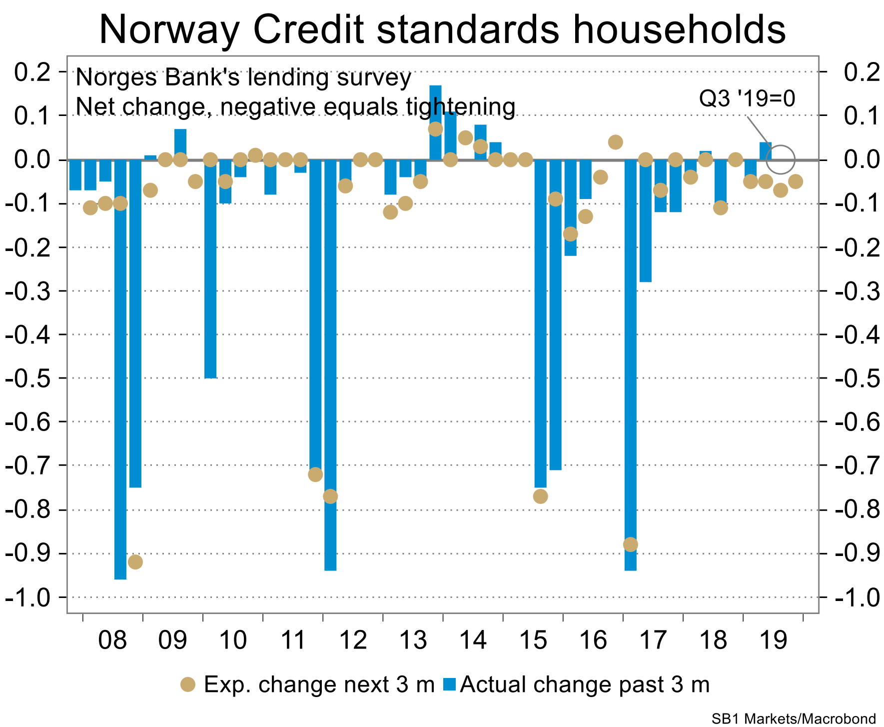




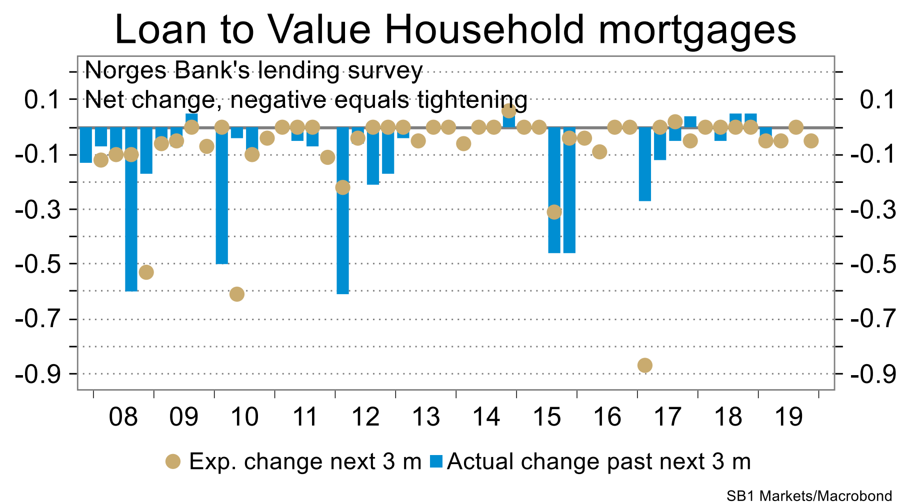
- Banks reported close to unchanged loan demand in Q2, slightly weaker than they expected in the previous report. Moreover, banks expect marginally higher demand in Q3, regardless of climbing interest rates
  - » A moderate upswing in the housing market, low unemployment and an overall solid economy are probably offsetting the negative effects on demand from higher interest rates. Effects from the Sept hike have not materialized in mortgage rates yet, though many banks have announced hikes
- Actual credit growth from households is sliding slowly down and m/m growth was softer than 'usual' in July/August (no Sept data yet). The lending survey pointing to an upturn in credit growth, however, the precision is not impressive. We highly doubt credit will accelerate now,

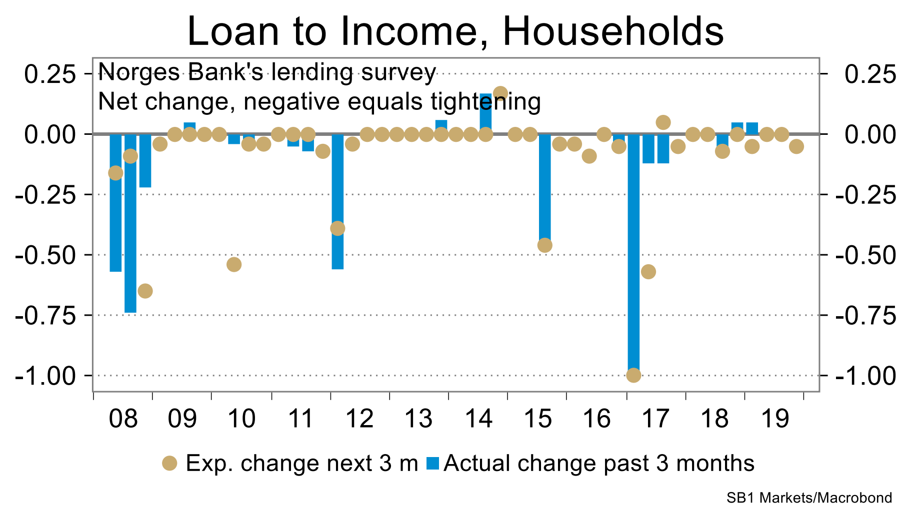
No substantial changes in credit standards vs households

Credit standards have been more or less unchanged since the mortgage regulations came in 2017



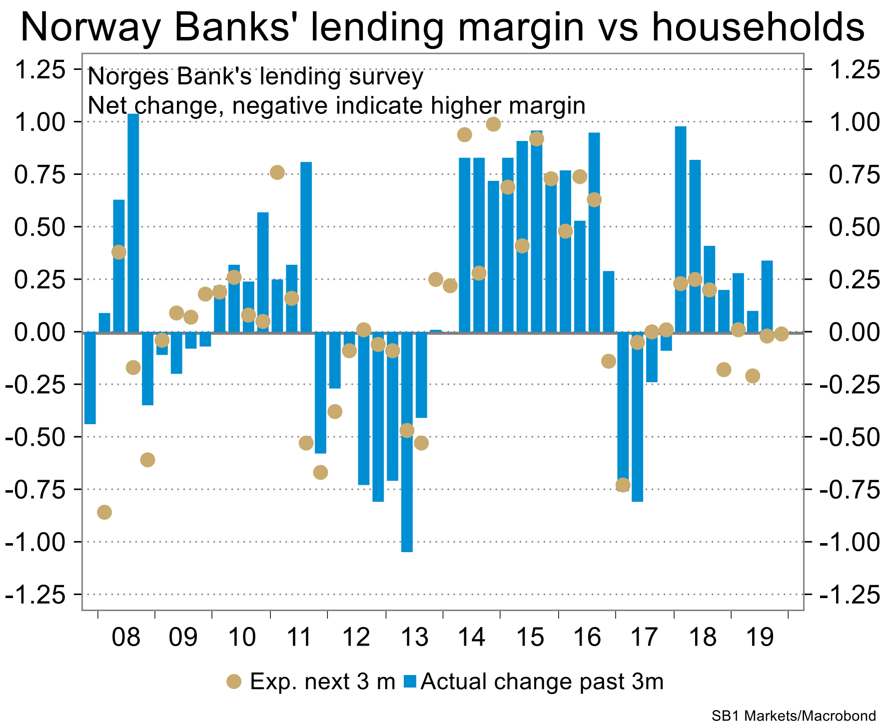
- Few changes in credit standards since the banks implemented the new mortgage regulations in Q1 2017
- Banks eased standards marginally in Q2, unchanged in Q3. They expect marginally tighter credit standards the coming quarter
  - » The new debt register may be the reason for the expected (marginal) tightening
  - » The Finance Ministry will soon decide on whether to implement the suggested tightening of mortgage requirements

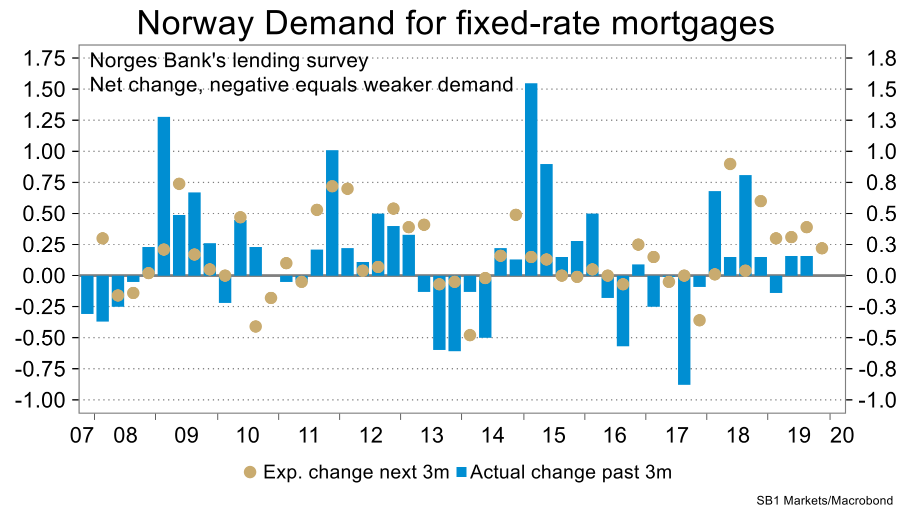


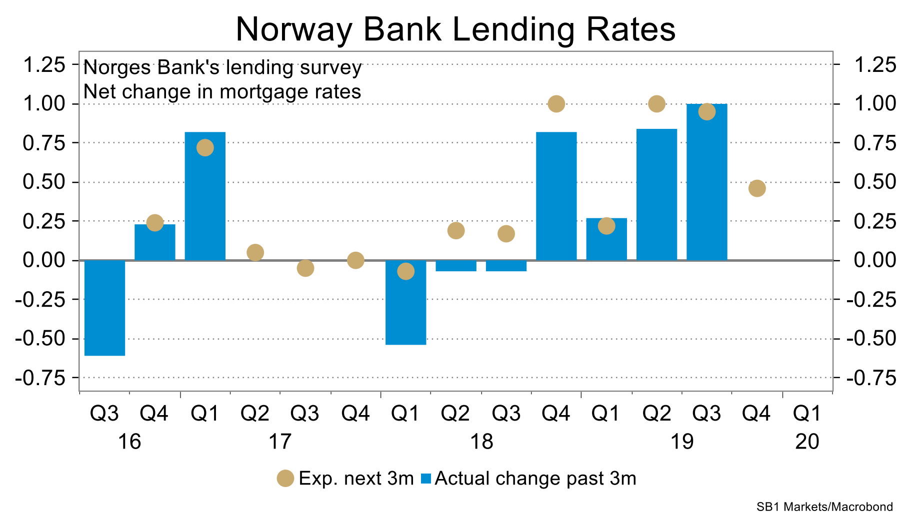


Rising funding costs and higher competition are pushing margins down

Most banks nudged up mortgage rates in Q3, fewer are planning to do so in Q4



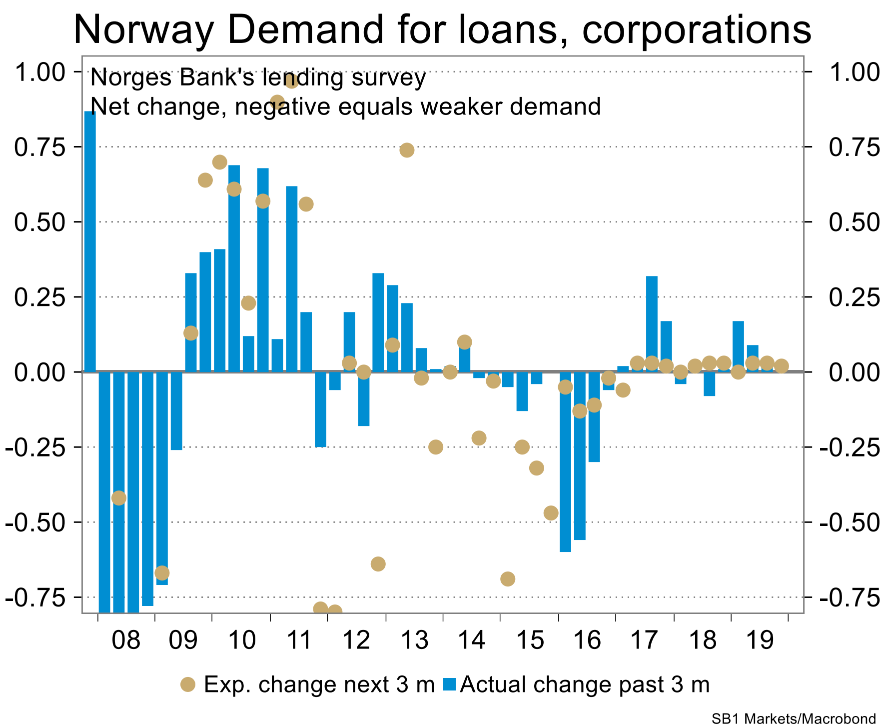


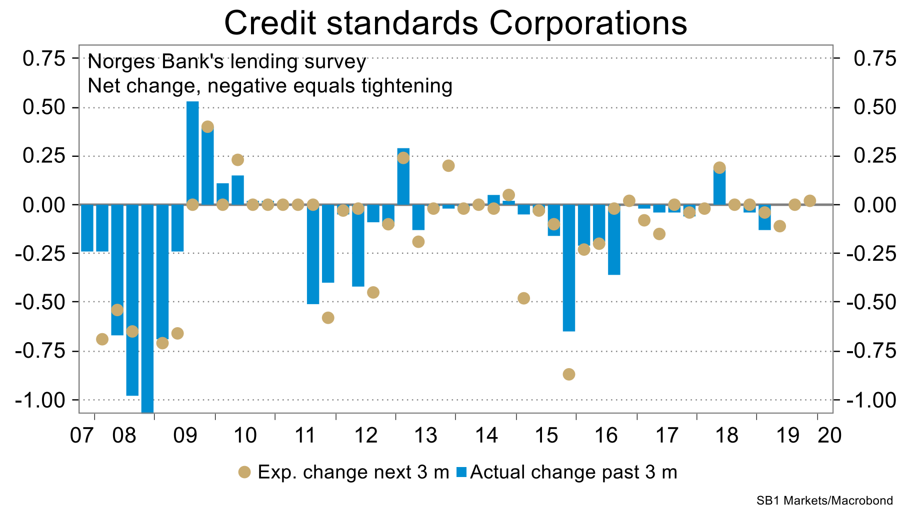


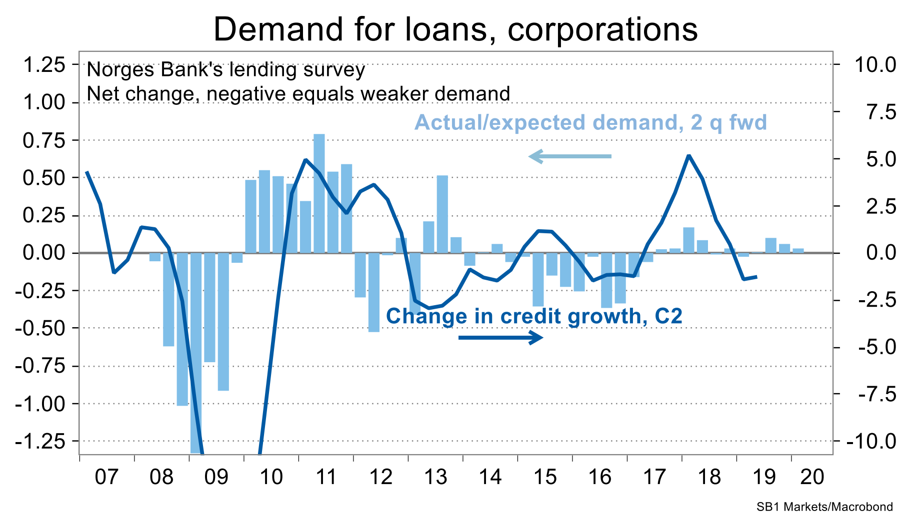
- Many banks raised mortgage rates in Q3, following Norges Bank's June hike
  - » Several banks have increased mortgage rates following the Sept hike, however, these are noted as Q4 plans. Some 2/3 of the NoBa hikes since Sept '18 have materialized in mortg. rates
- Demand for fixed-rates increased in Q3, but less than expected. The banks are expecting a modest rise in Q4

Stable corporate loan demand & standards

Demand was unchanged in Q3 and is expected so in Q4. No changes in credit standards



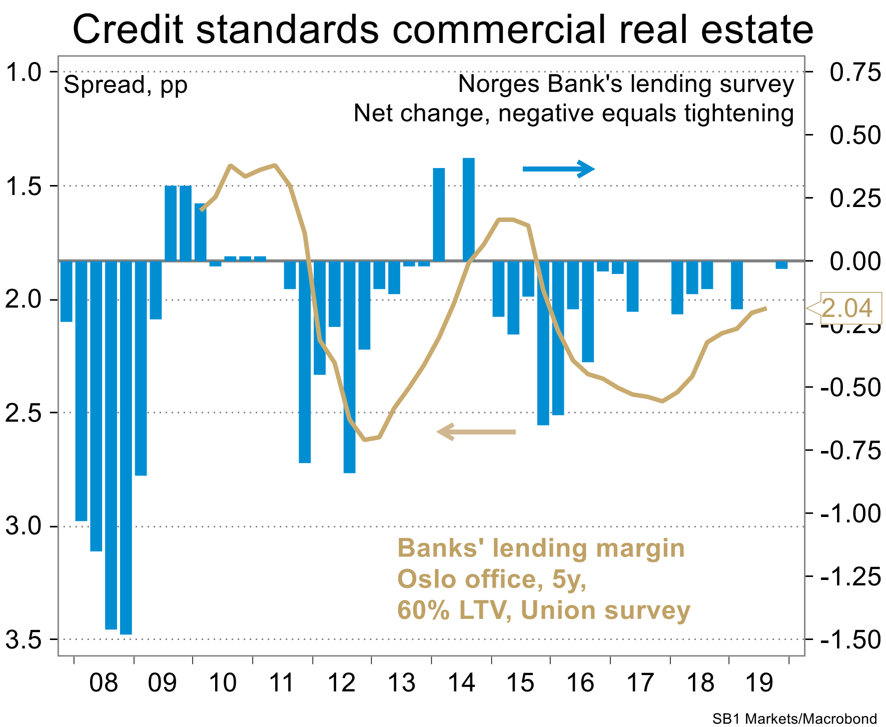


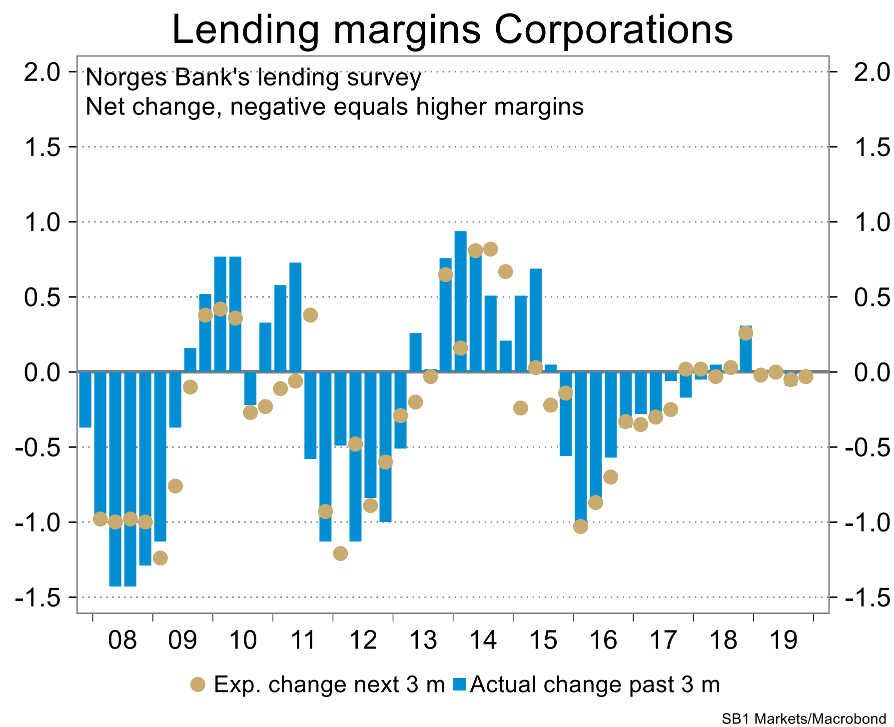


- Actual lending to the corporate sector (domestic C2) has slowed somewhat following an upswing in late 2018, the annual rate is steady at 5.7%. The Q3 lending survey signals stable corporate credit demand going forward
- Credit standards were eased marginally in late 2018/early 2019 and have been held unchanged since

No changes in lending standards vs commercial real estate

Banks note unchanged lending margins vs corporations

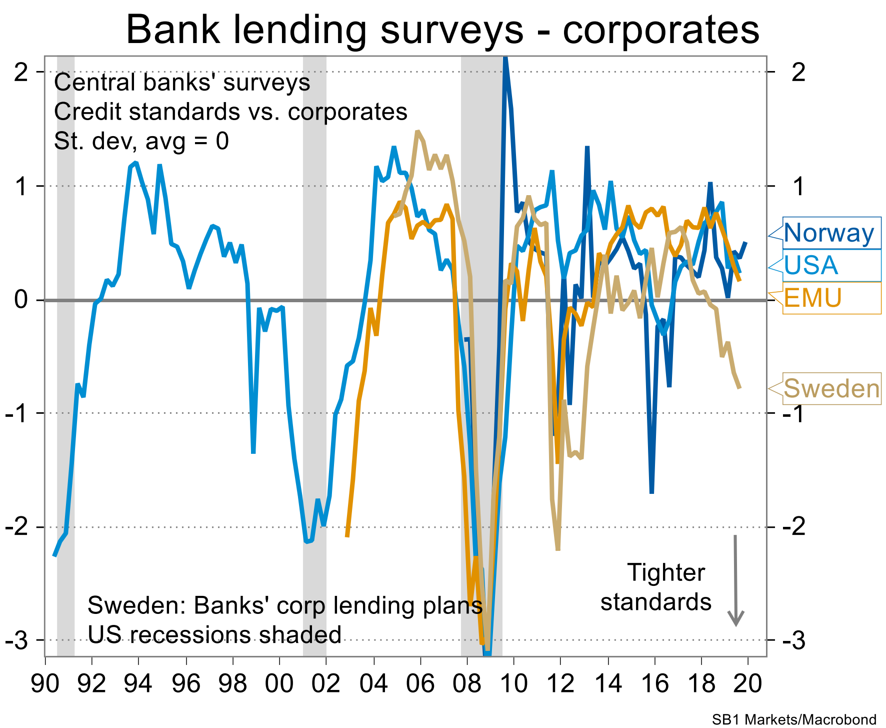


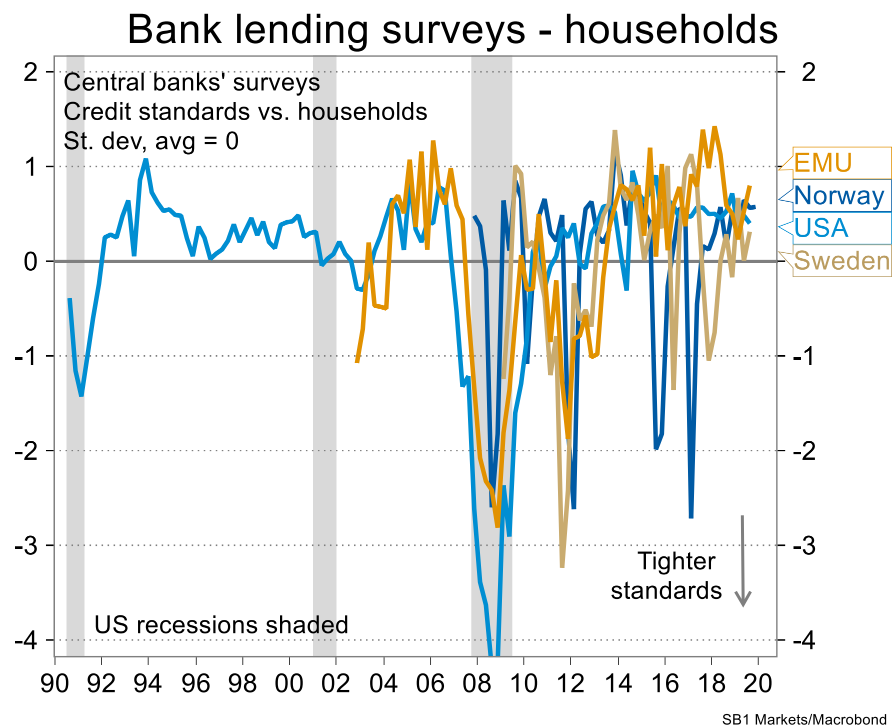


- Lending standards to commercial real estate were unchanged in Q3 and no changes are planned in Q4
- Lending margins to corporations are unchanged too

Global view: Credit easing most places vs both corporates & households

But banks are becoming a tad less upbeat vs. the corporate sector, and Swedish banks to cut lending?

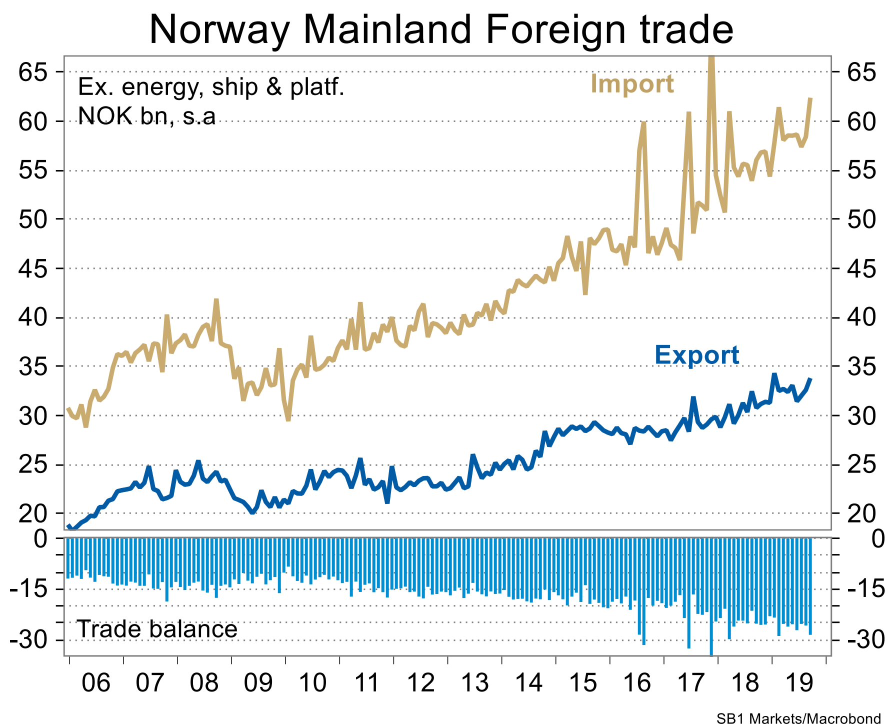


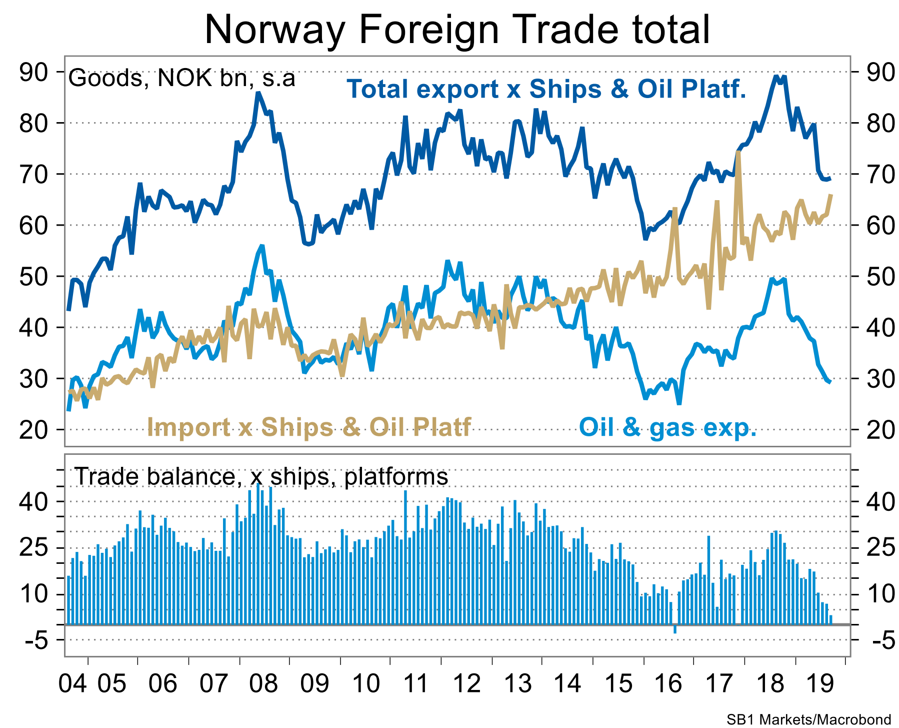


- Credit standards implemented on corporates have eased most places, although standards on both US and Eurozone corporations are less loose than they were in 2018. Norwegian banks have been loosening standards vs corporations the past year. Swedish banks are planning to pull back lending (not standards)
- Banks are reporting easing credit standards vs households in both the US and the Eurozone, and marginally in Sweden. Standards in Norway have eased too, after the implementations of new mortgage regulations in 2017

Imports soared in Sept, net trade most likely a drag on Q3 growth

Mainland trade deficit widened in Sept, both exports and imports are trending up

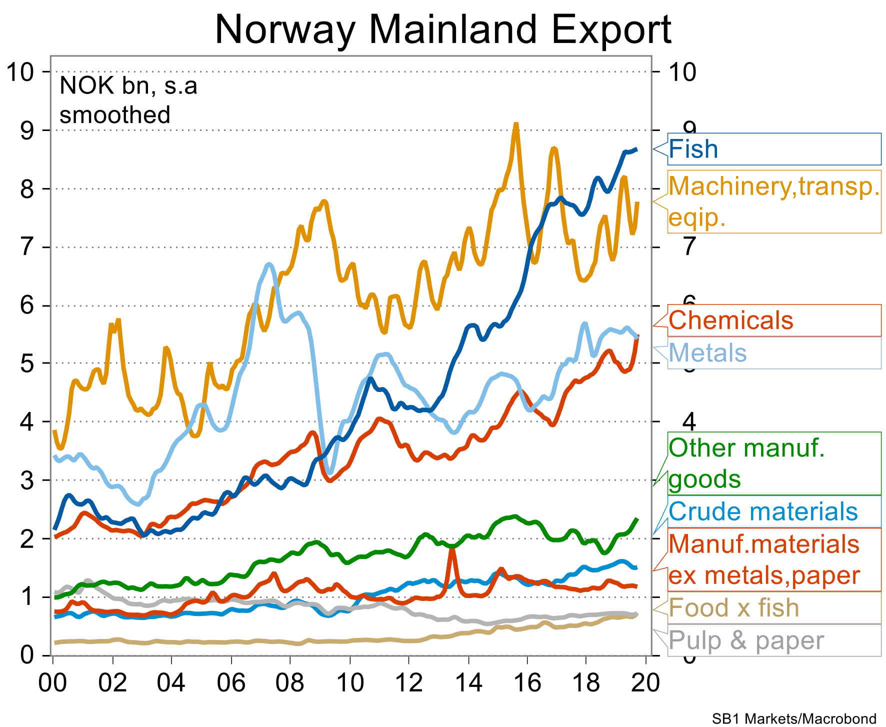


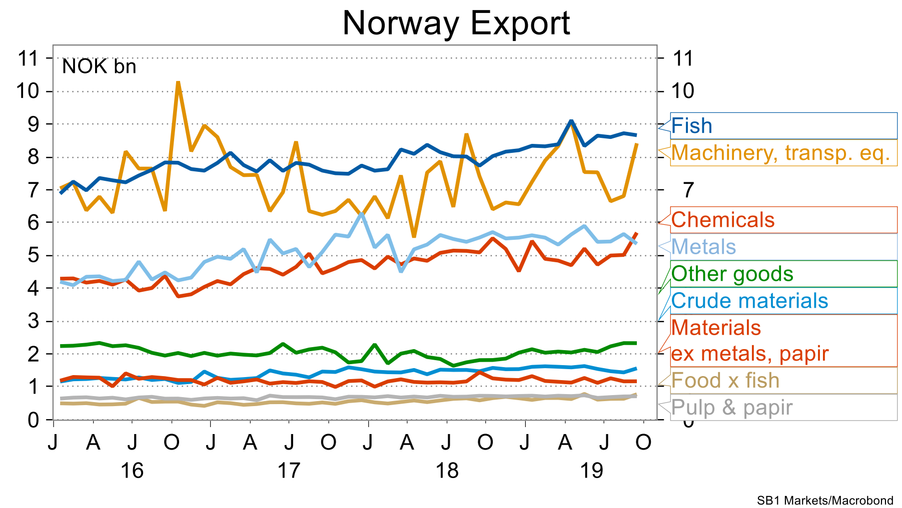


- The Mainland (non energy) trade deficit widened to NOK 28.6 bn in Sept. The deficit has been more or less stable this year, but the longer term trend is a widening deficit. Measured in goods & services, as reported in the monthly national accounts (no Sept data), net trade has turned negative and will most likely be a drag on Q3 GDP growth
  - Imports surged in Sept, primarily due to machinery & equipment (probably oil related) and is up 7% y/y, smoothed
  - Mainland exports have improved the past 3 months, helped by the weak NOK? Exports are trending up and the y/y rate is 6.2% (smoothed)
- The overall trade surplus (incl oil & gas, ex ships & platforms) shrank to NOK 3.2 bn in Sept, from 6.9 bn in August, the lowest in 2 years. Oil/gas exports have fallen sharply due to reduced gas prices. Recent years, the total trade surplus has equalled some 6% of total GDP

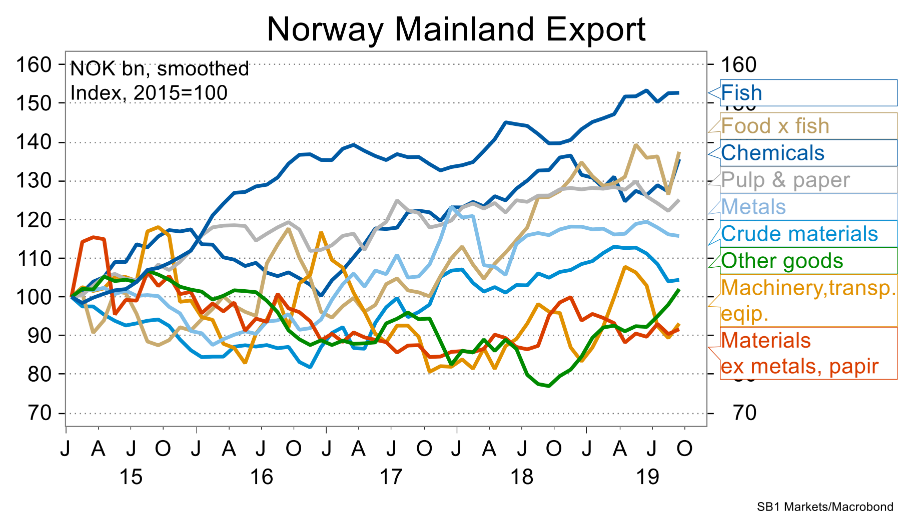
A broad export upswing; fish is the big winner

Exports of fish, machinery, chemicals and other manufacturing goods have gained pace recently



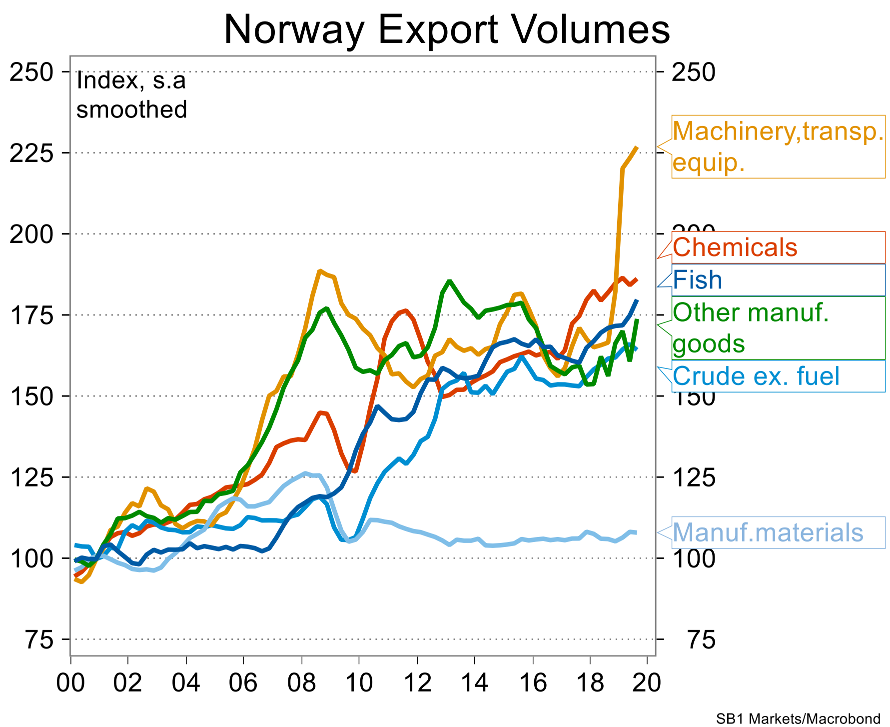


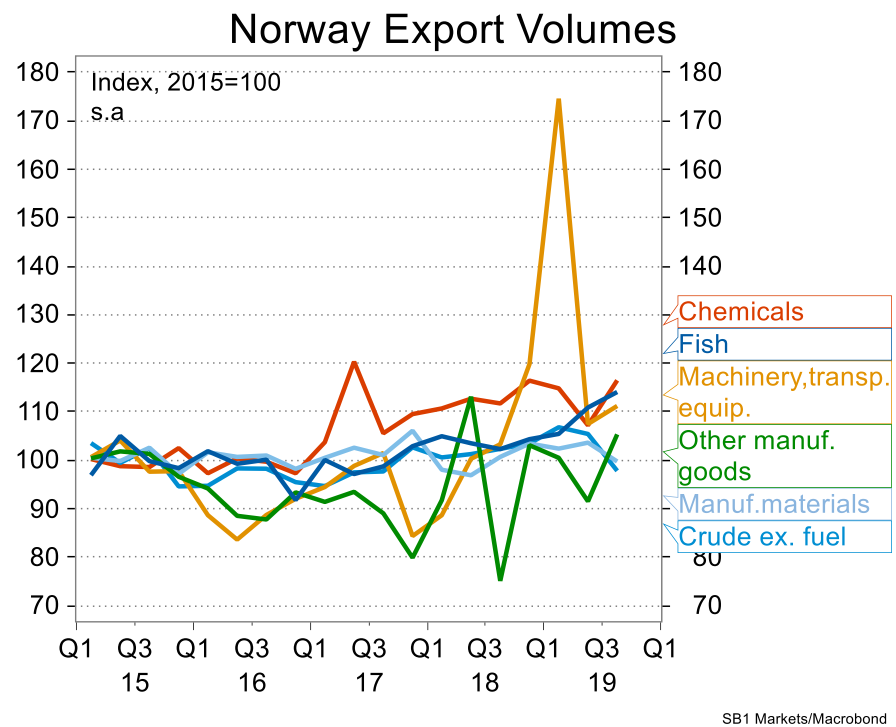
- Fish exports have been soaring both in value and volume recent years
- Exports of machinery and transport equipment (of which much is related to oil activities abroad are volatile. Exports accelerated in Sept and are trending up, although well below the 2015 and 2016 peaks



Most export categories are heading up, ex manufacturing materials

In volume terms, exports of machinery & equipment, chemicals and fish have been soaring

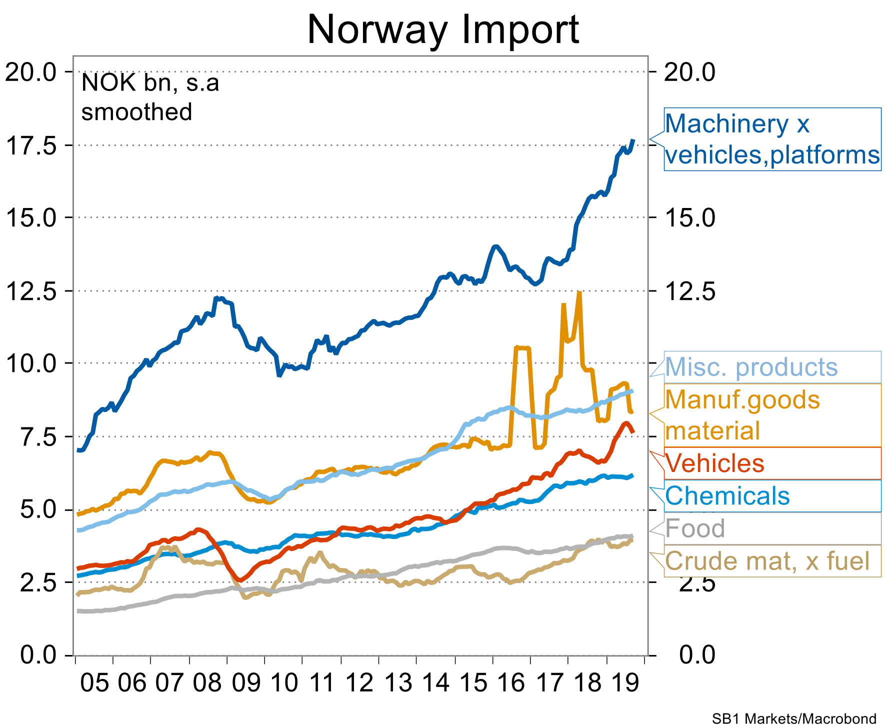


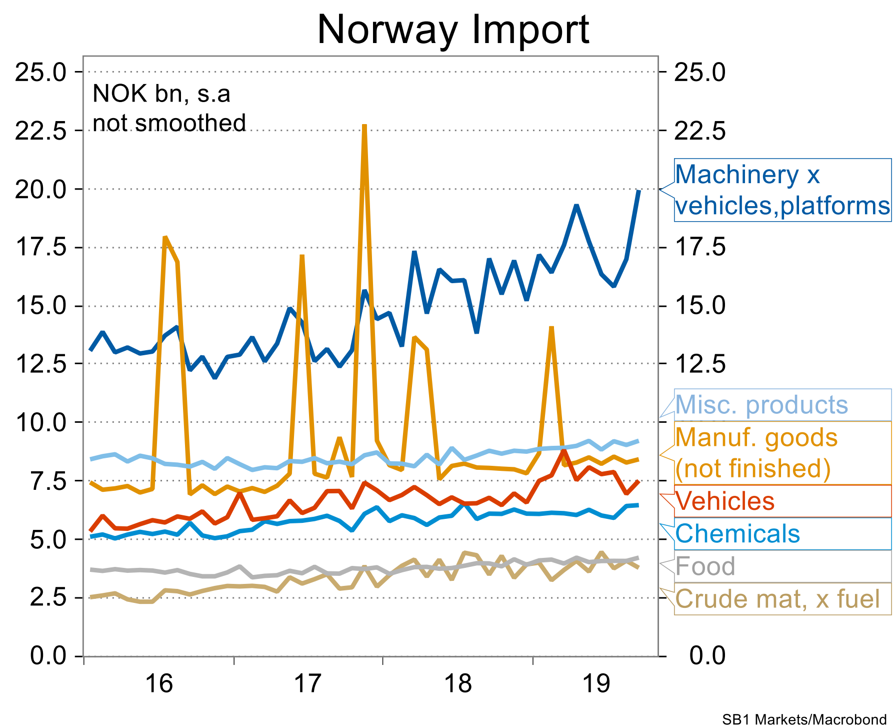


- Export volumes of chemicals, fish, manufacturing goods and crude materials ex. fuels are trending up. Machinery & transport equipment (primarily oil-related) exports are accelerating but these data are volatile
- Manufacturing materials have been flat since 2015

Imports of machinery equipment spiked in Sept, trend straight up

Imports of most goods are heading up. Vehicles lifted by imports of electric cars the past months





- Imports of manufacturing materials have had some huge spikes, due to some massive transactions; of oil platforms, wind mills and combat airplanes. Regardless, the trend is up. Machinery ex vehicles and platforms, much oil related, are rising steeply too, and jumped in Sept
- Chemicals, food and crude materials are all slowly expanding
- Vehicle imports soared in H1 and have slowed somewhat since. The uptick is partly due to rising imports of electric cars, particularly the new Tesla in March, and electric busses. Imports of vehicles equal some 12% of total goods imports (in value)

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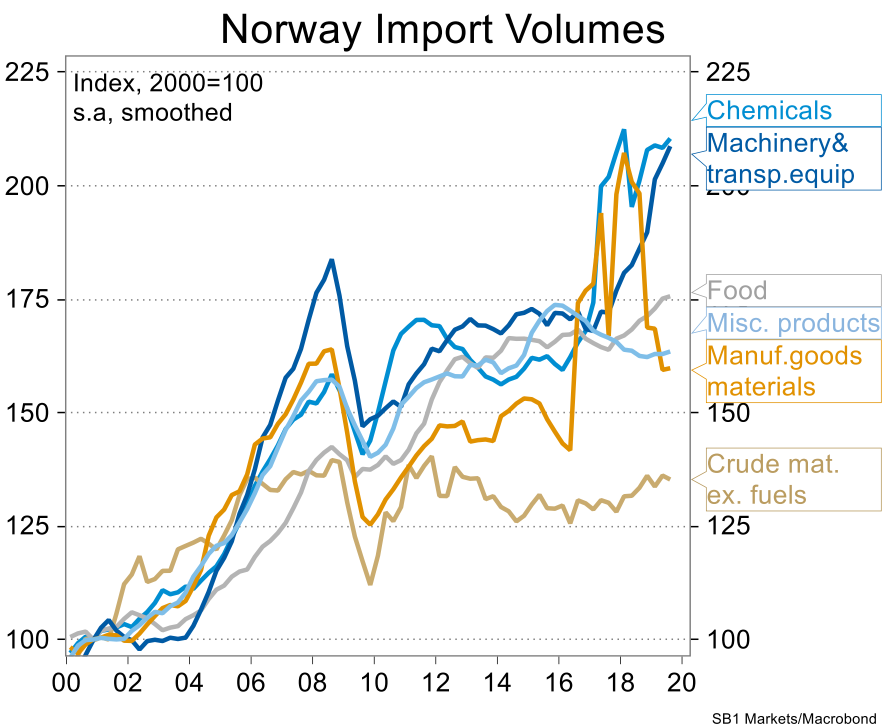
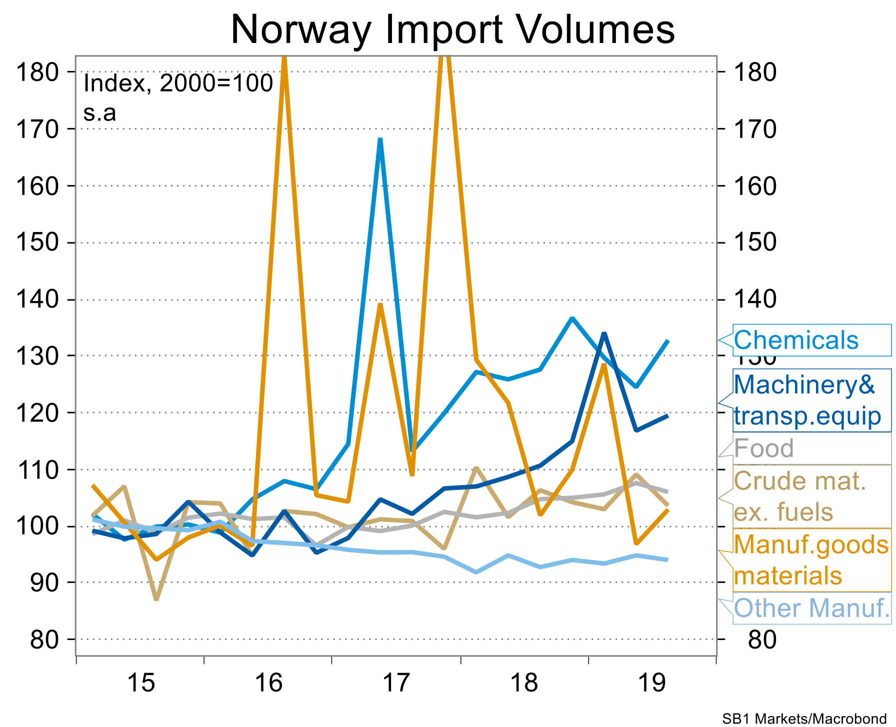
Import volumes of machinery, chemicals rising strongly

Manufacturing materials & products have been retreating, following a huge lift in 2018





- Some huge transactions within manufacturing goods & materials the past 2 years, primarily delivery of a gas platform and new combat airplanes
- Imports of machinery & transport equipment (much oil related) are soaring, so are chemicals. Food imports are heading up, crude materials slowly expanding

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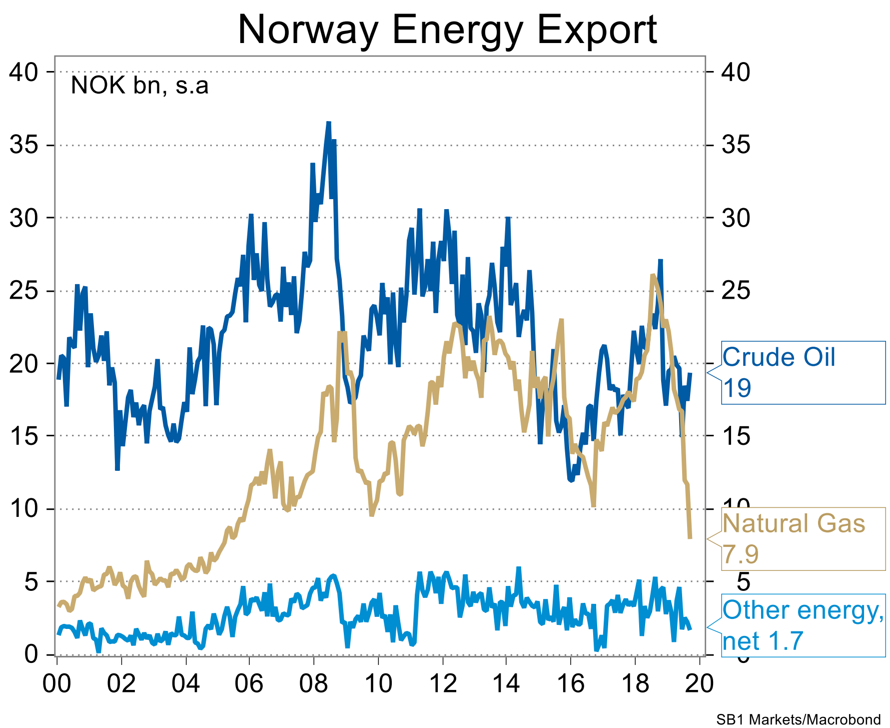
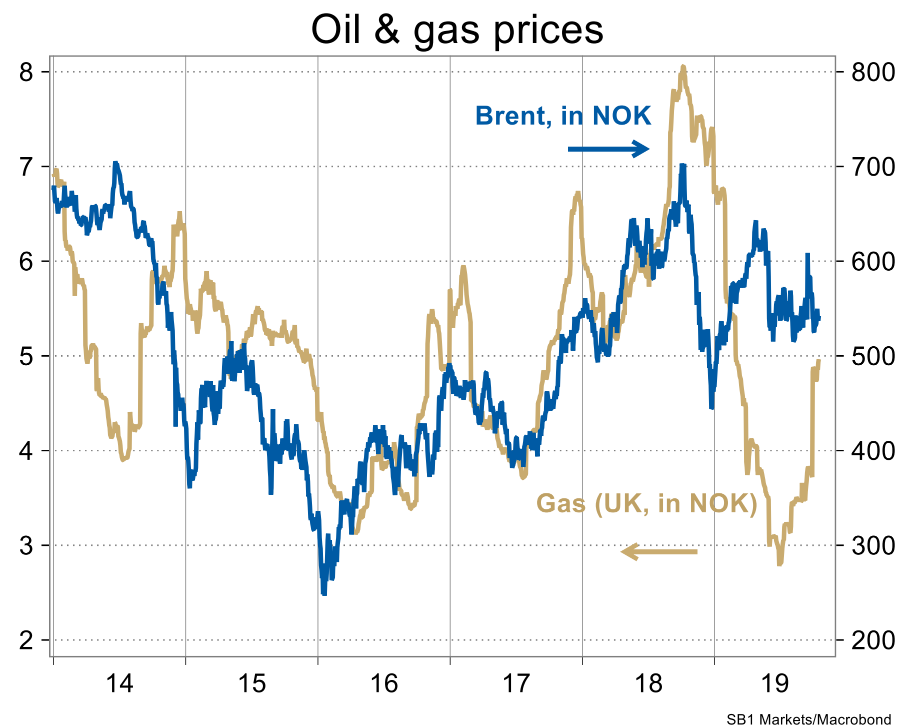
Value of oil exports have been recovering; gas export drops rapidly

Gas exports are slipping, in spite a price rebound. Oil exports have stabilized with the oil price





- **Crude oil** exports (in NOK bn) rose to NOK 19 bn in Sept, up from 15 bn at the trough in June (but down from 28 bn at peak in Oct ’18). Export values have more or less stabilized with the oil price since early 2019. Still, exports are down 21% y/y, smoothed

- **Gas** export values tumbled to NOK 7.9 bn in Sept, the lowest since 2005 and the annual rate is -60%. European gas prices (UK balance price) have recovered so far in H2, while volumes have been slipping. According to SSB, the downturn in gas exports in September is partly due to maintenance work

Highlights

The world around us

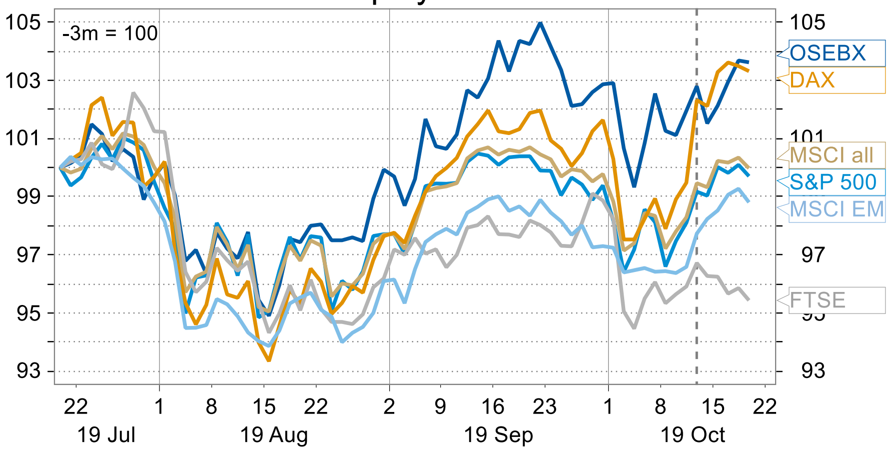
The Norwegian economy

Market charts & comments

Risk markets continue to recover, helped by hopes of Brexit breakthrough

Stock markets recovered swiftly, bond yields followed, muted in the US. The GBP another 1% up

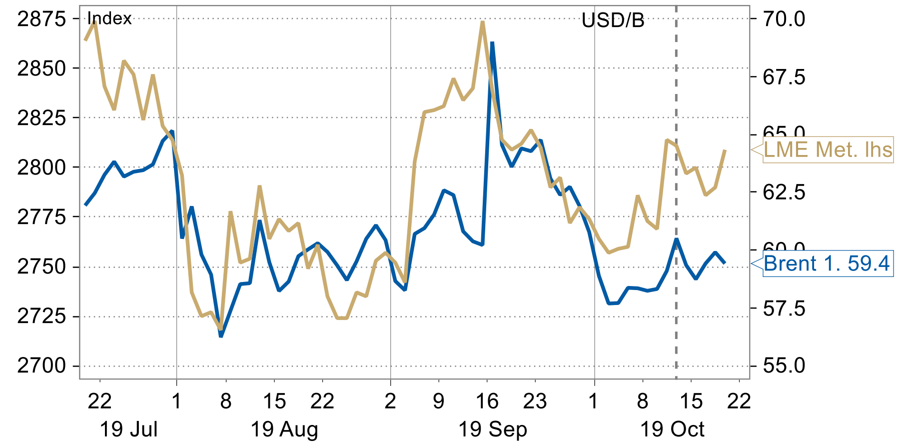
Equity Indices



Stock markets climbed through the week, trade deal hopes and upbeat US third quarter results from some large companies

SB1 Markets/Macrobond

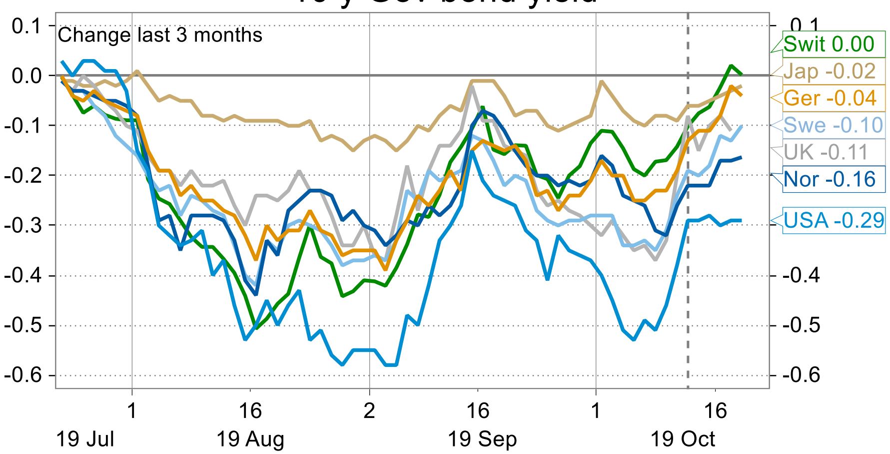
Oil vs. metals



Brent oil price fell to 59.4 last week, metal prices marg. down

SB1 Markets/Macrobond

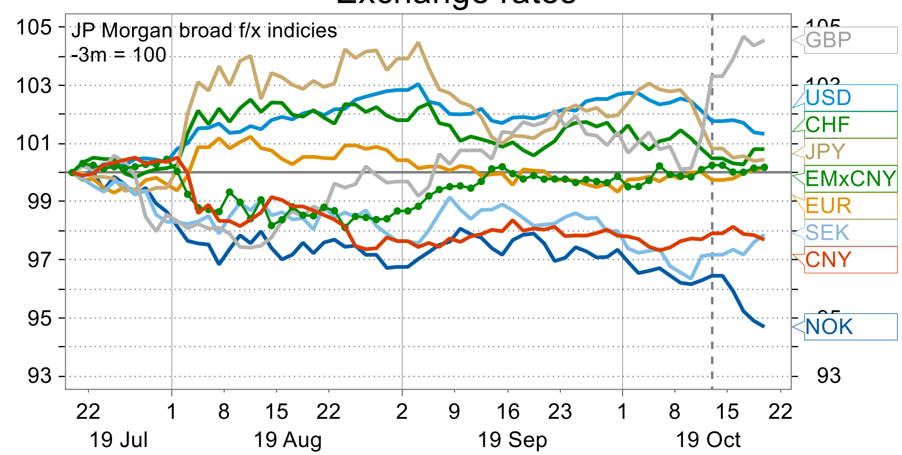
10 y Gov bond yield



Bond yields rose everywhere x the US, which was flat through the week. Some weak US macro data probably weighted

SB1 Markets/Macrobond

Exchange rates

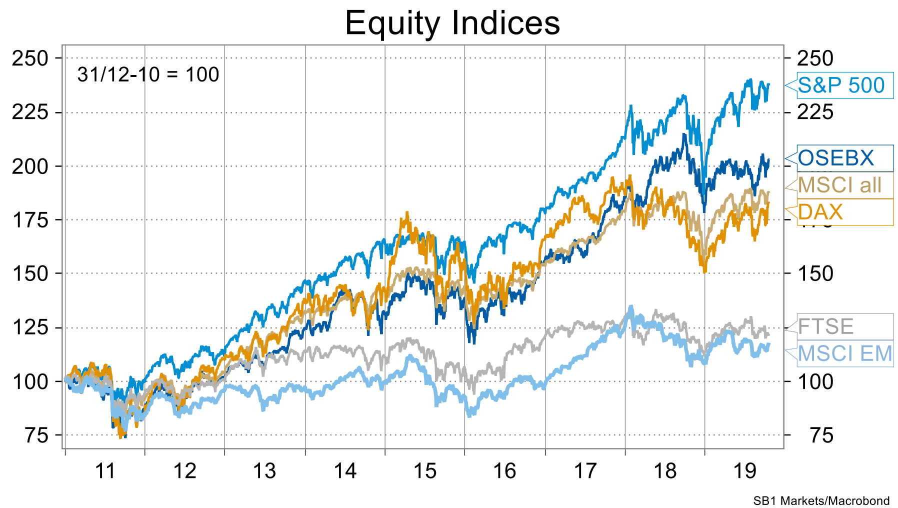


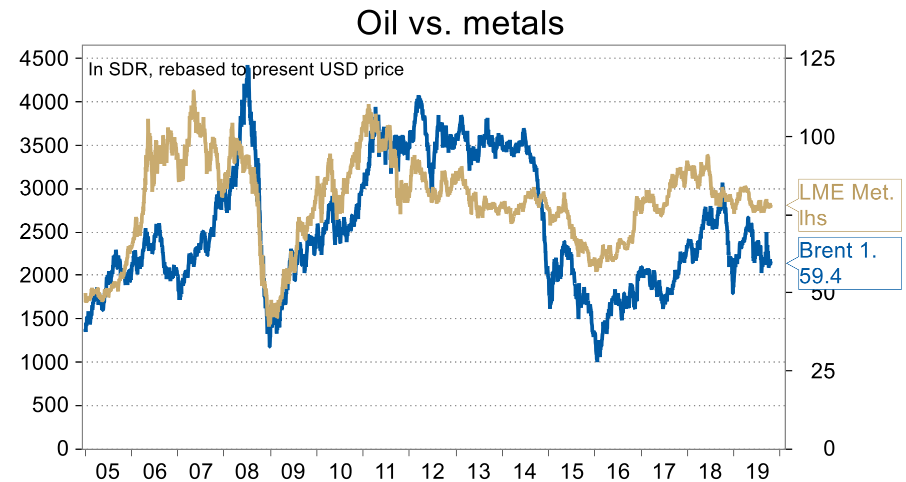
GBP climbed another 1%+ last week after a 3% jump the prior week, on encouraging Brexit news. GBP steady after the Brexit vote was delayed. USD weakened, CNY steady. And the NOK depreciates once again

SB1 Markets/Macrobond

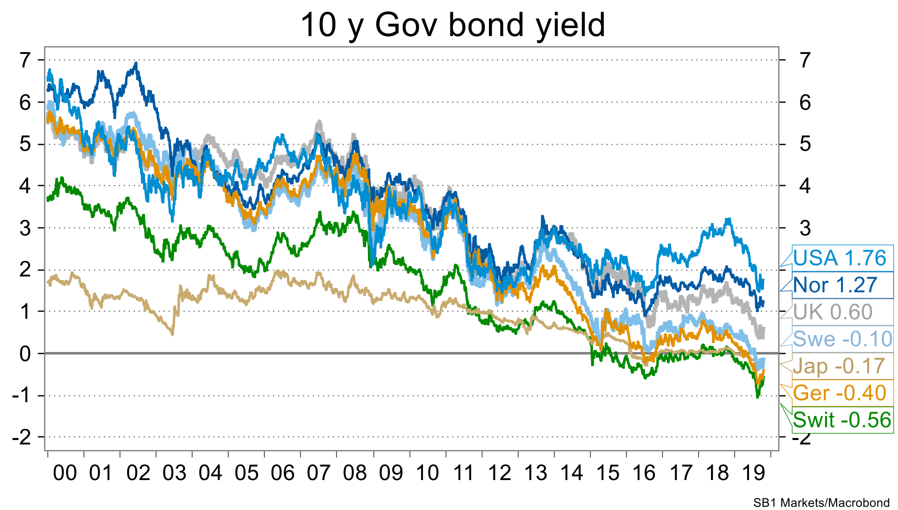
In the long run: Bond yields close to ATLs, US stock markets not far below ATHs

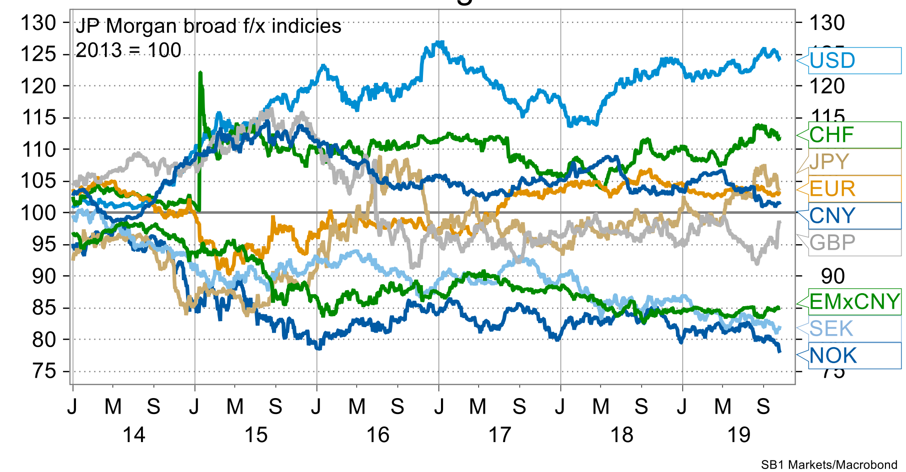
Oil, metals are trending slowly down. The trade war rules. And then some economic data





Metal prices may be trending down but slowly and the decline from the local peak is not large





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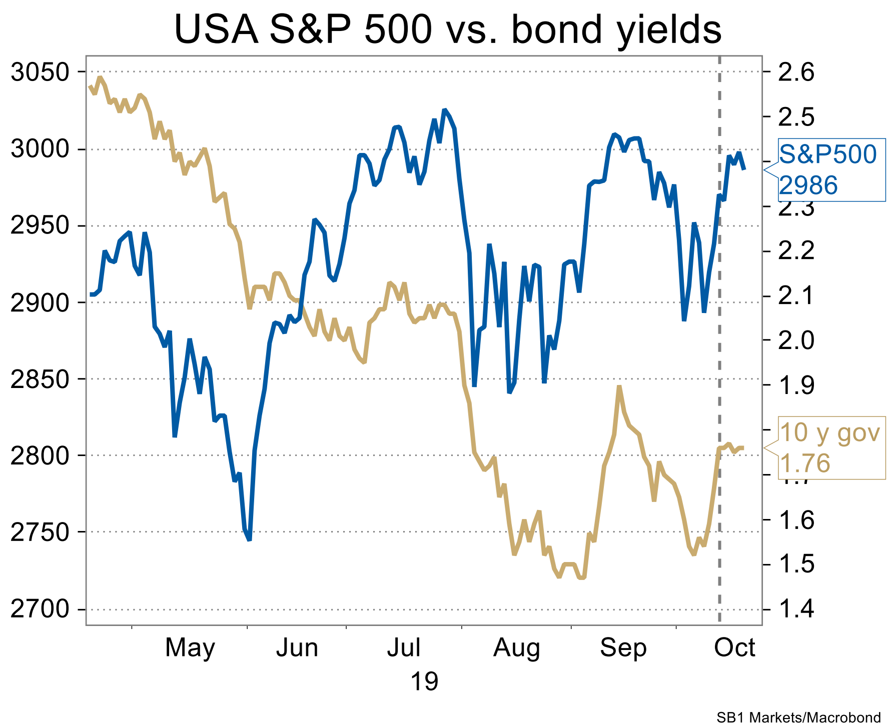
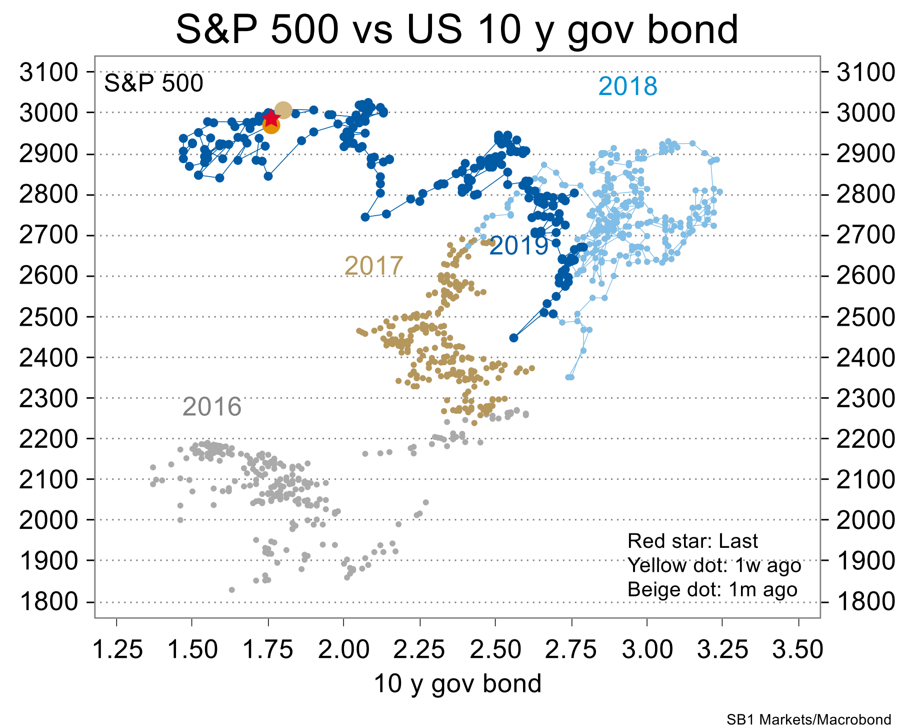
US: Stocks rebounded (somewhat), bond yields flat

S&P rose 0.5% last week, while the 10 y gov yield held steady at 1.76%



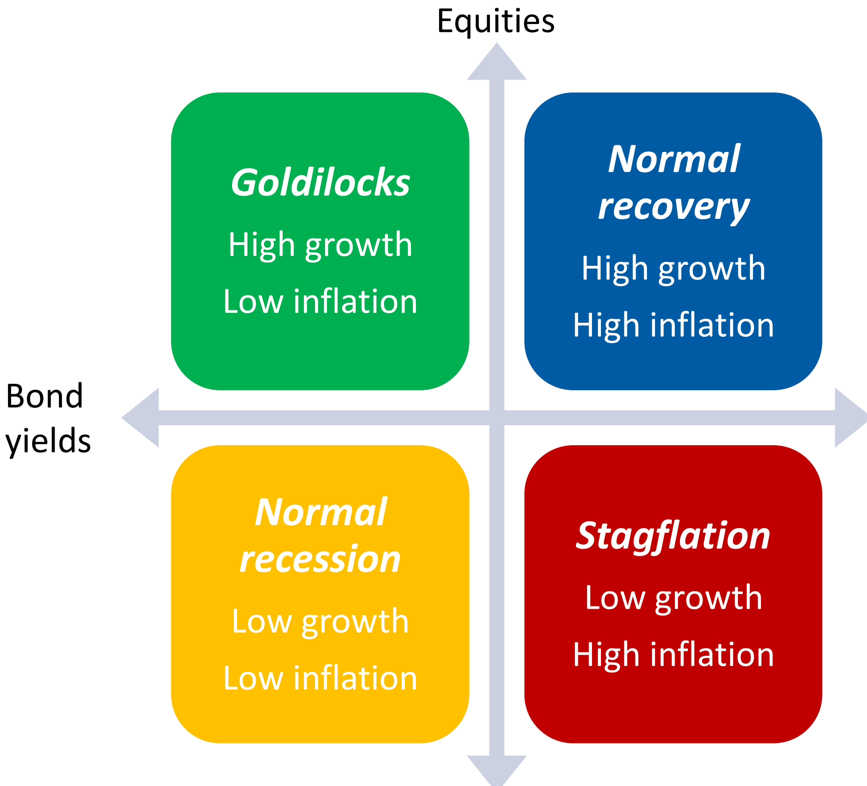


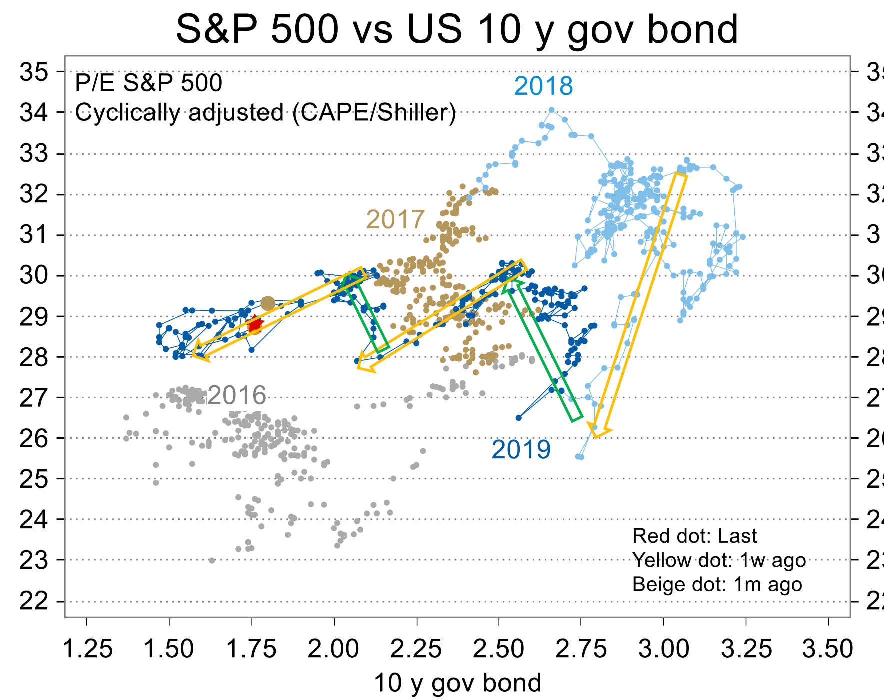
- The stock market response to last weekend's US China partial 'trade deal' was muted, as investors (rightfully, we think) had second thoughts on the impact of the deal (which BTW was not at done deal at all, according to the Chinese, it turned out at Monday). S&P rose later in the week on strong earnings results from some big US companies and rising hopes of a Brexit deal
- The 10 y bond yield did not follow stock markets up, some soft US macro data (particularly retail sales) may have contributed

SpareBank 1 MARKETS

US markets move away from the recession corner

Stocks/bonds are almost back to where they came from one month ago



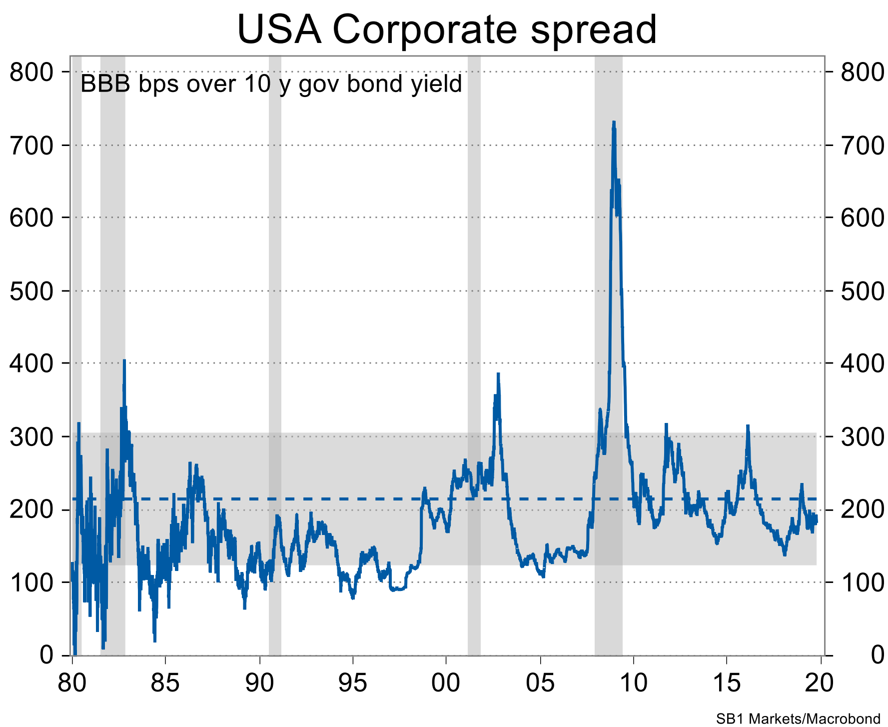


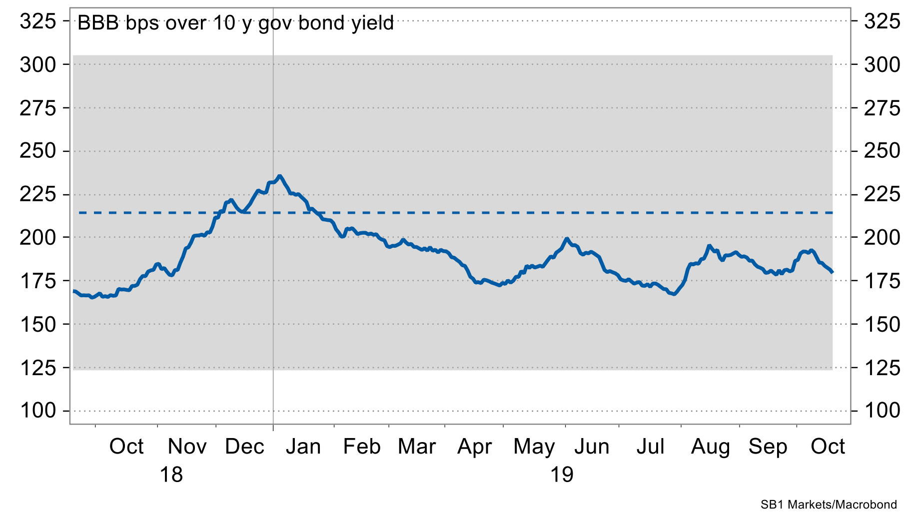
SB1 Markets/Macrobond

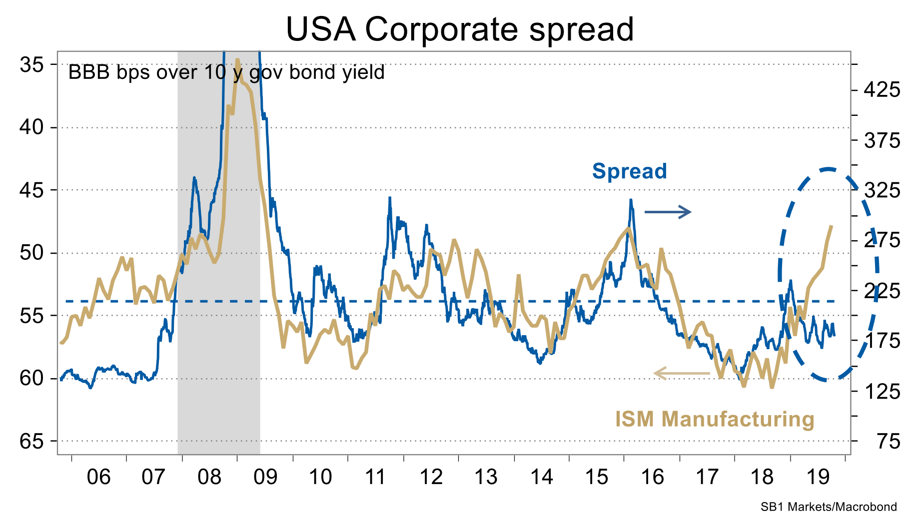
- Recent months, markets have been zig-zagging along with developments/news on the trade war. In August, markets moved towards the recession corner following the bad trade policy news. In early September, both markets were recovering, on hopes of a trade war de-escalation and some upbeat US macro data. The previous two weeks, trade news were positive, and market recovered, again – out of the recession corner. Last week more mixed again
- We do not think a long term Goldilocks scenario is likely. Should yield 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

Credit spreads down last week, are below an average level, far too low?

Spreads are <u>far too low</u> if the ISM and (most) other surveys are correct; that is, <u>*if growth is slowing*</u>

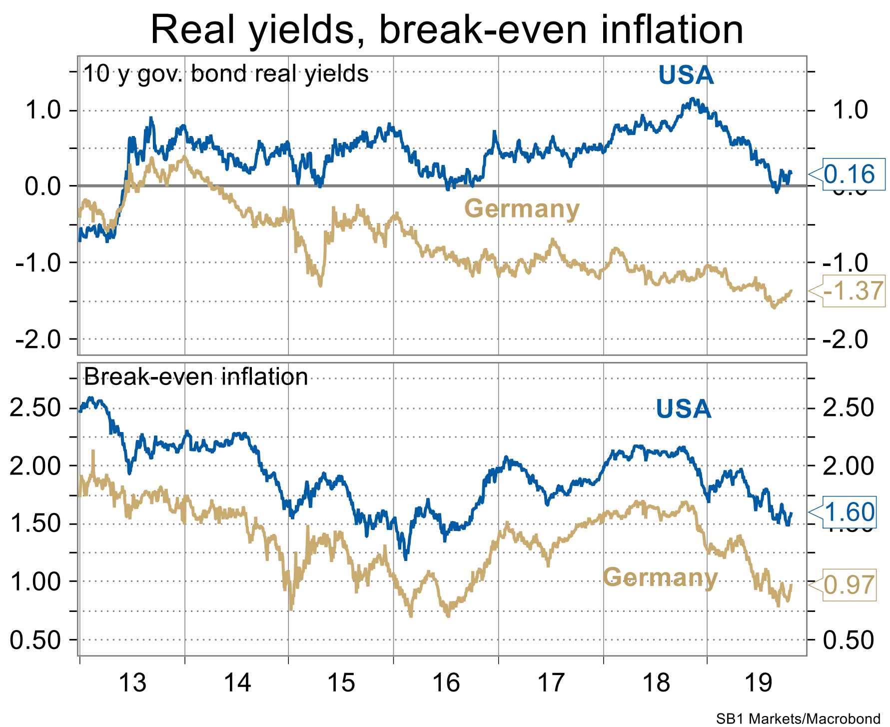


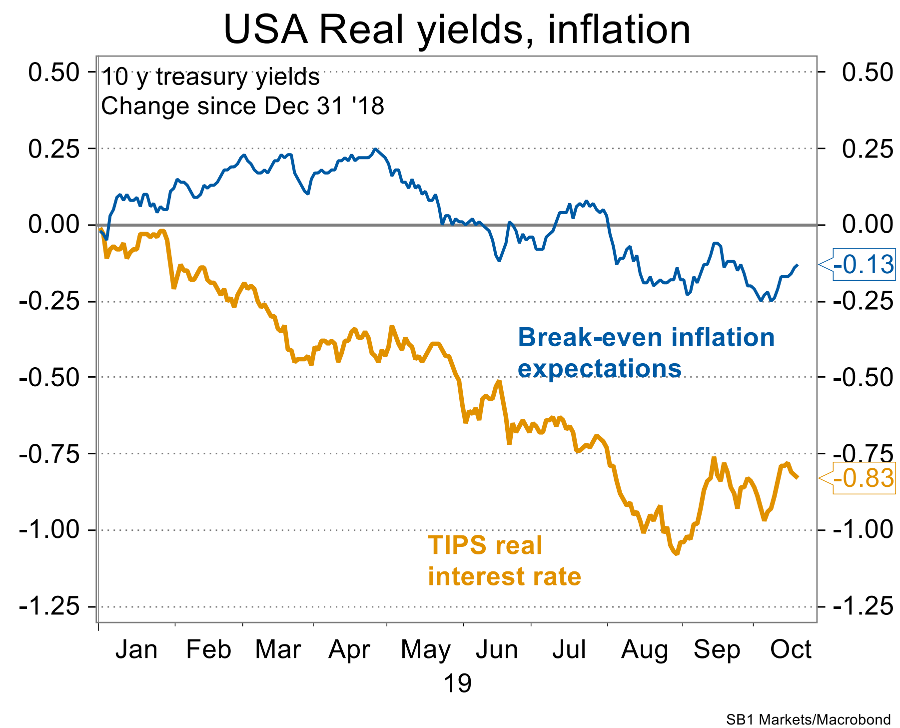




US real rates have recovered softly, inflation expectations follow up

US real rates fell marginally last week, inflation up. German real rates and inflation exp. improved

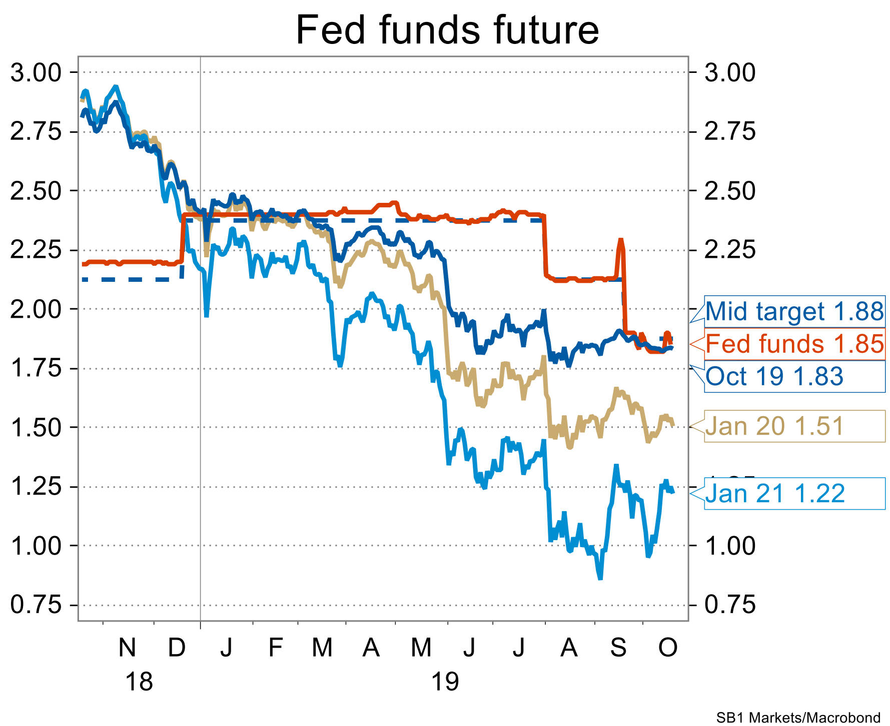


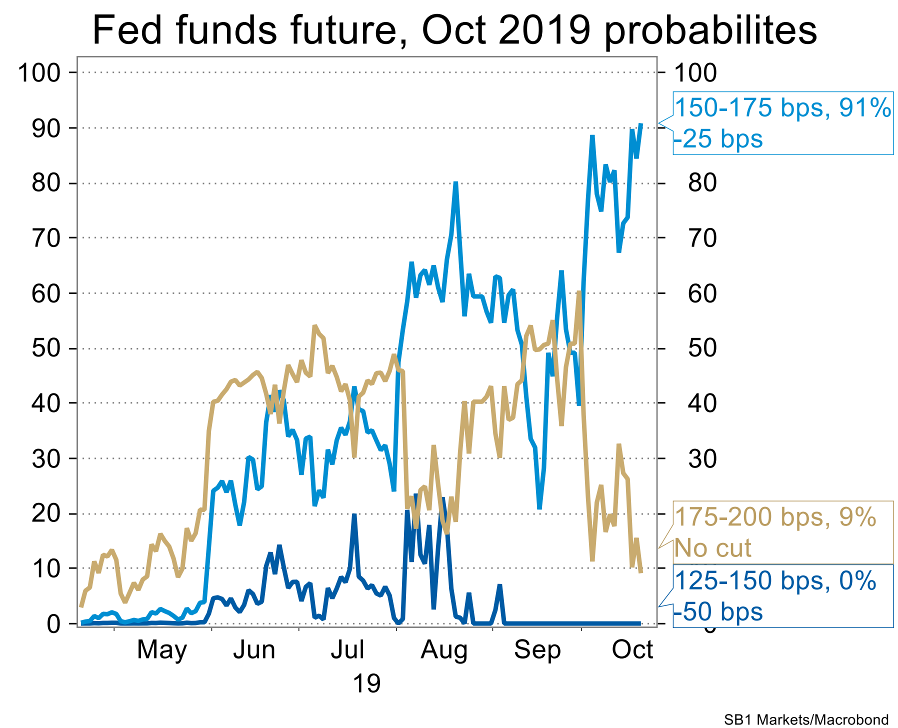


- Both real rates and break even inflation have been heading steeply down this year, in US and Germany. Since early Sept, real rates have recovered much better than inflation expectations, probably primarily due to hopes of a trade war solution
  - » Last week, US real rates inched down while inflation expectations improved. In Germany, both inflation expectations and real rates ticked up
- German real rates bottomed out at 1.6% in late August, and have edged up to -1.37%, which is still ridiculously low. Inflation expectations at 0.97% does not seem that far off, although far below the ECB's price target at close to 2%
- US inflation expectations rose to 1.60% last week, the real rate bounced to 0.16%

Fed fund futures steady last week, above 90% probability of an October cut

Unless US macro data deteriorates substantially the next week, we doubt the Fed will cut now

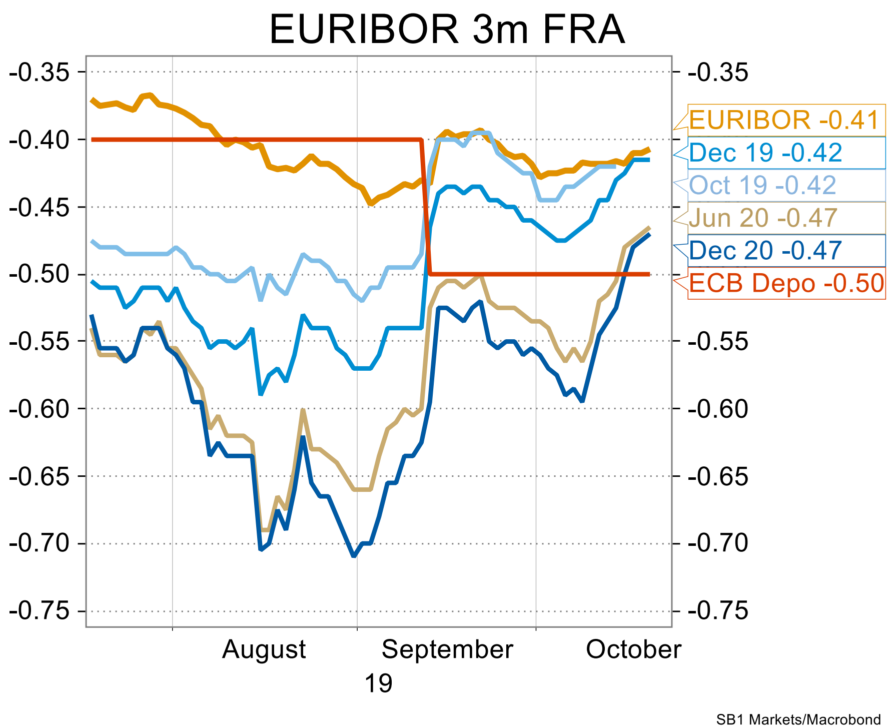


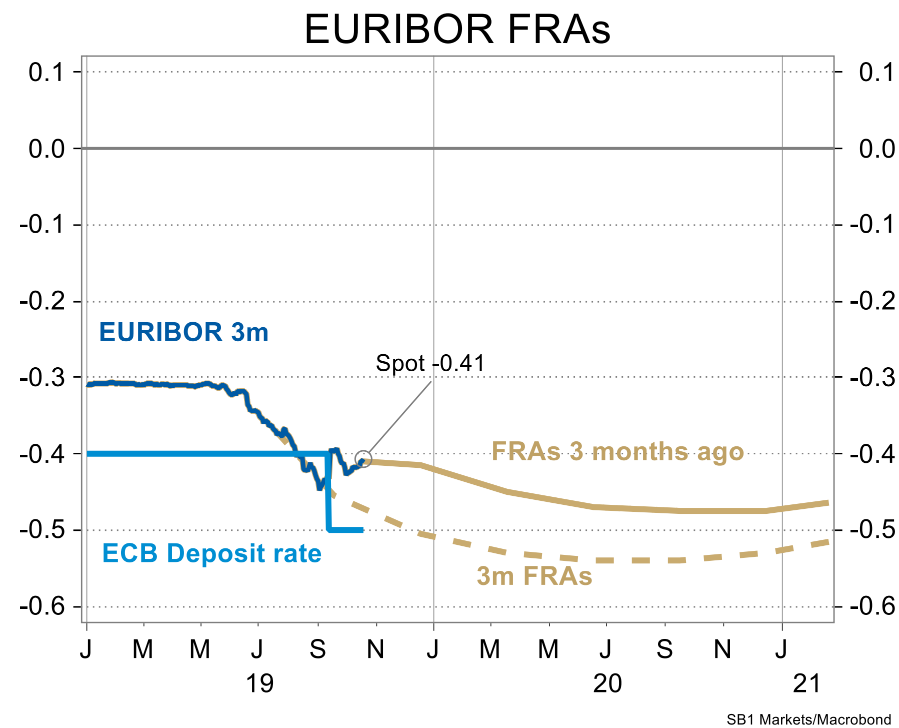


- The probability of a 25 bps Fed cut at the Oct 30 meeting is elevated at approx. 85%, a tad up last week. The Jan '20 contract implies just below 50% probability of another cut in Dec. 3 more cuts (of 25 bps) are expected by the end of '20
- US growth is slowing but it is still above or at trend. PCE inflation is not far below the target. Yes, some 'soft' data are deteriorating but 'hard' data are not yet that weak. And the USD is stronger than normal but not by that much. The economy does not justify another interest rate cut in October, in our view (and a few of the FOMC members'). Still a cut is probably more likely than not (but the probability is well below 90%)

EUR FRAs are climbing, expectations of another 2019 cut are subdued

FRAs are recovering all over the curve, fuelled by good news on Brexit and the US/China trade war





- Weak macro data sent EUR FRAs down in late Sept/early Oct. Since then, the FRA rates have turned up all over the curve. Positive news from the US/China trade talks turned the mood, even as the partial trade deal was narrow. Hopes of a quick Brexit solution helped too – and a highly divided ECB
  - » Moreover, minutes from the ECB Sept meeting revealed opposition from 'several members' about the resumption of QE, making further monetary easing in the short term less likely. Christine Lagarde will inherit a split ECB when she takes over on Nov 1.

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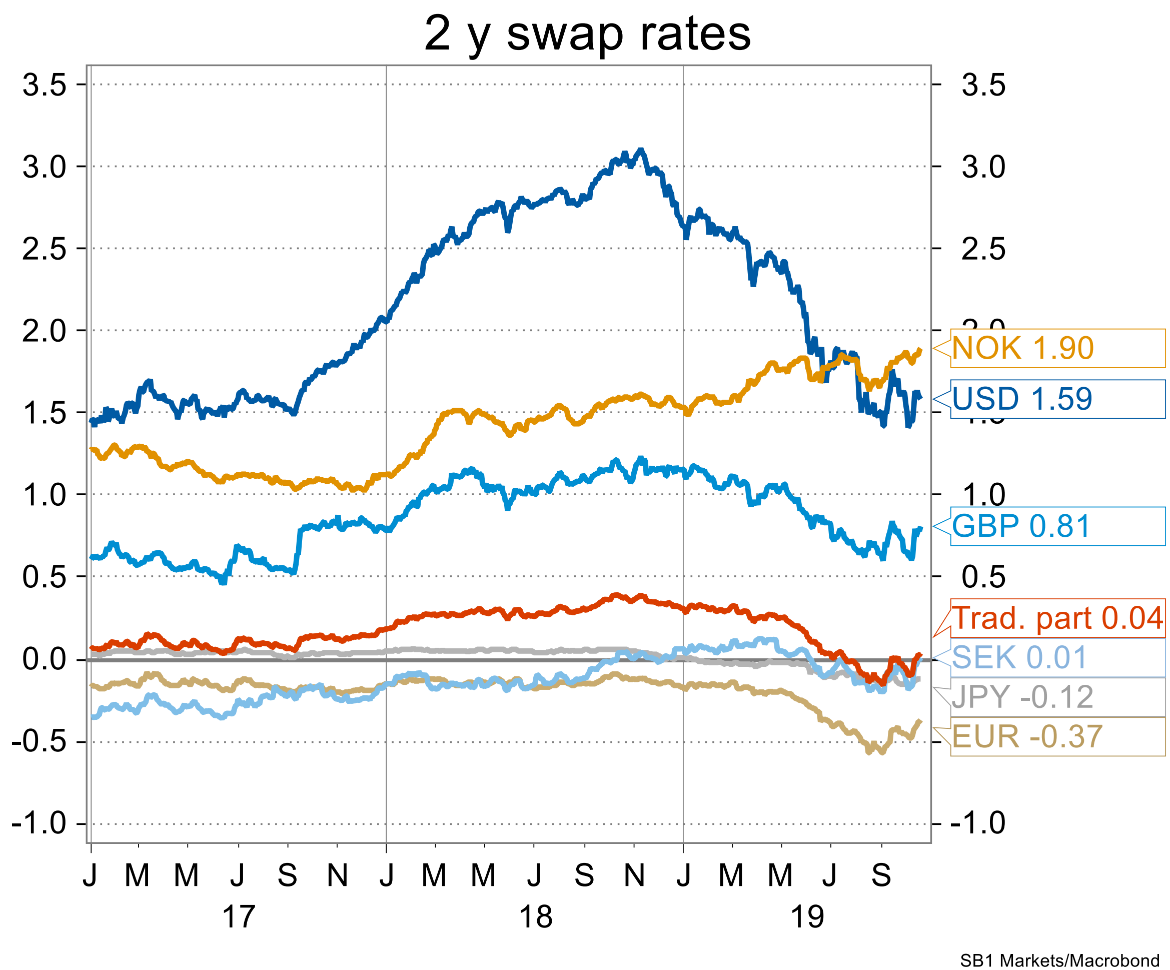
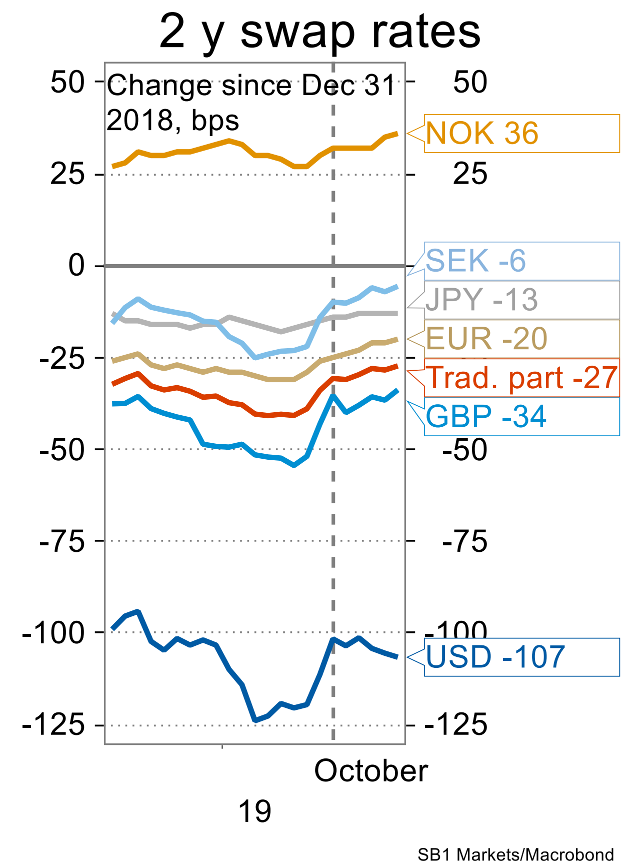
Short term rates up most places, USD took a pause last week

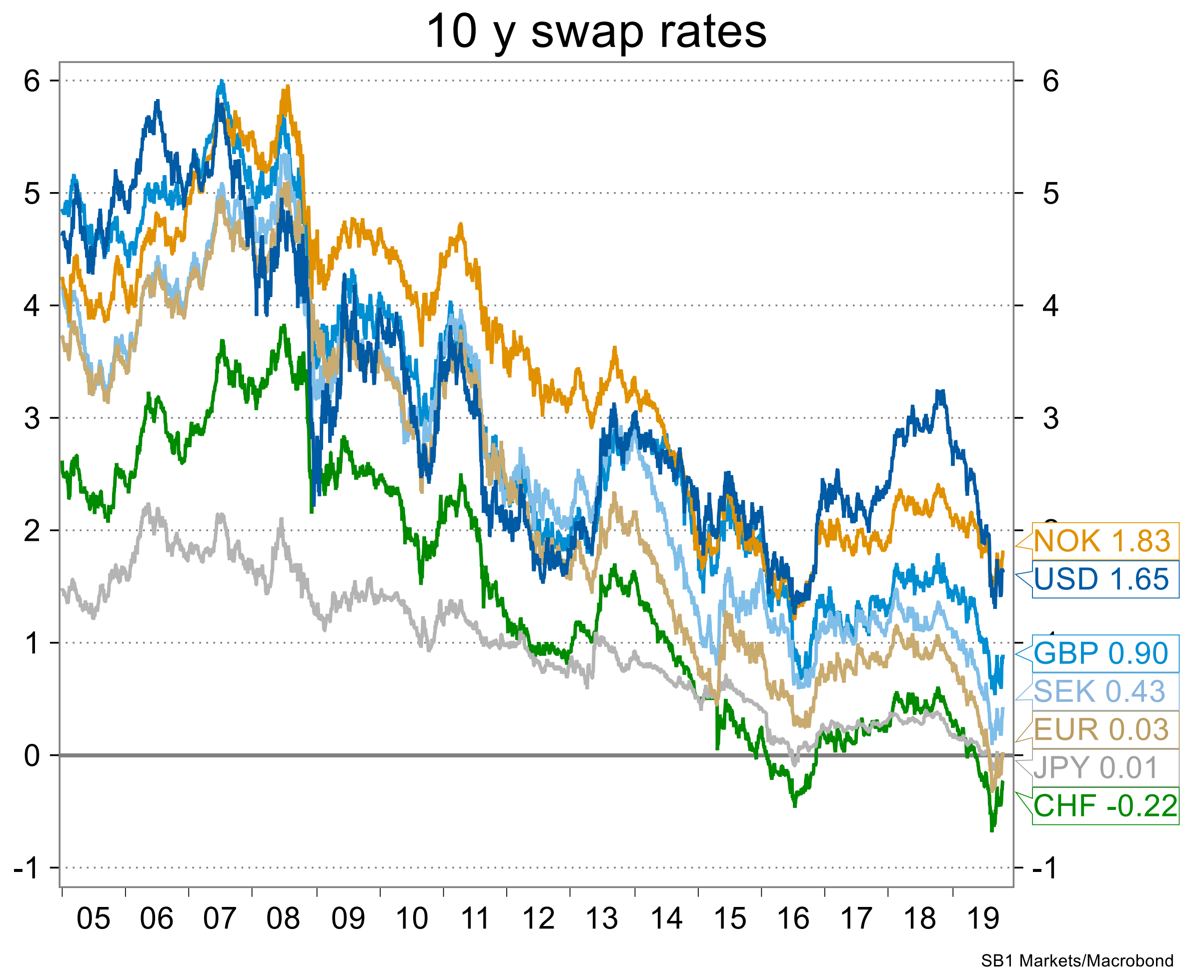
Short term rates are recovering everywhere, EUR rates steeply up on Brexit deal hopes

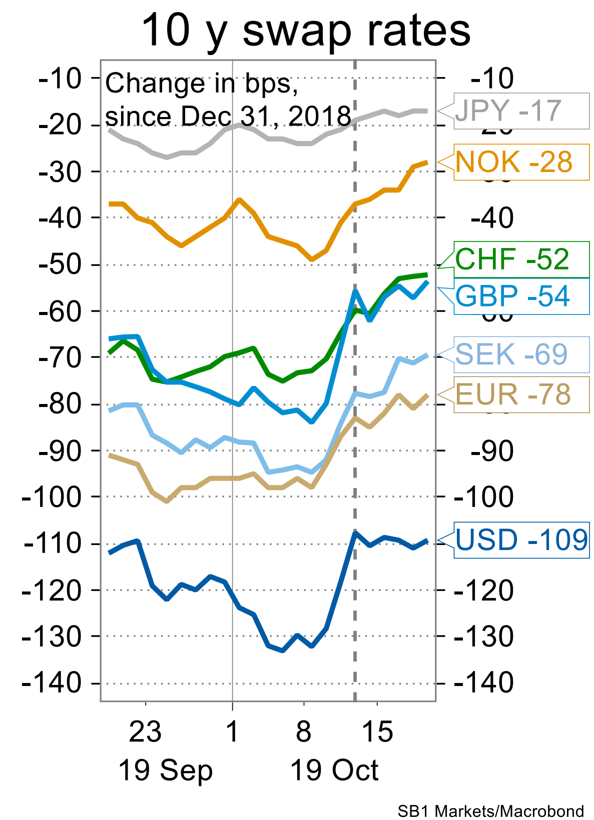




Long term swap rates up from the bottom

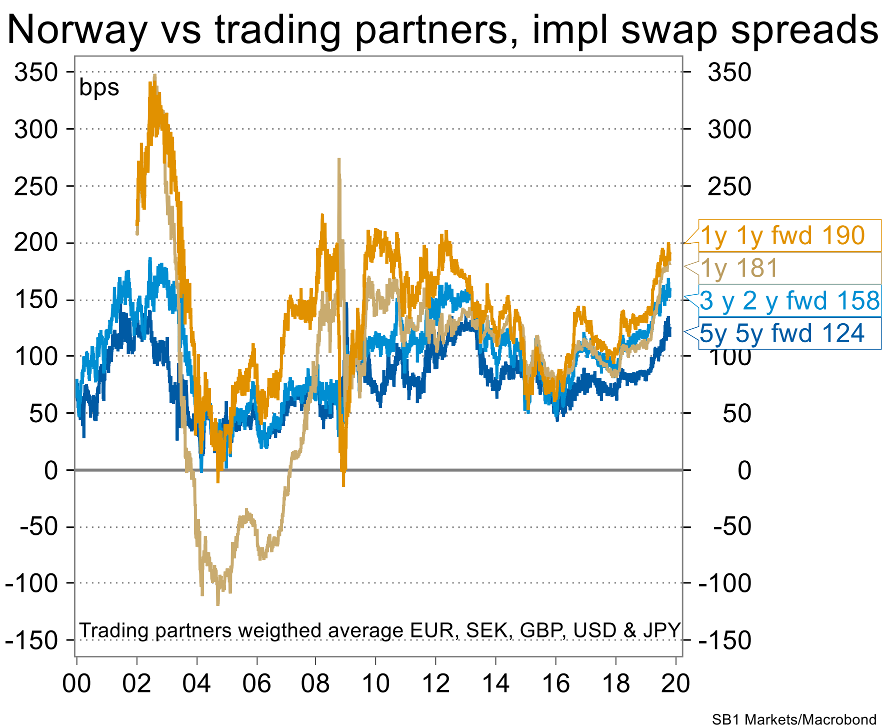
All swap rates have turned up, US 10 y swap rate is up 22 bps from Oct 4th

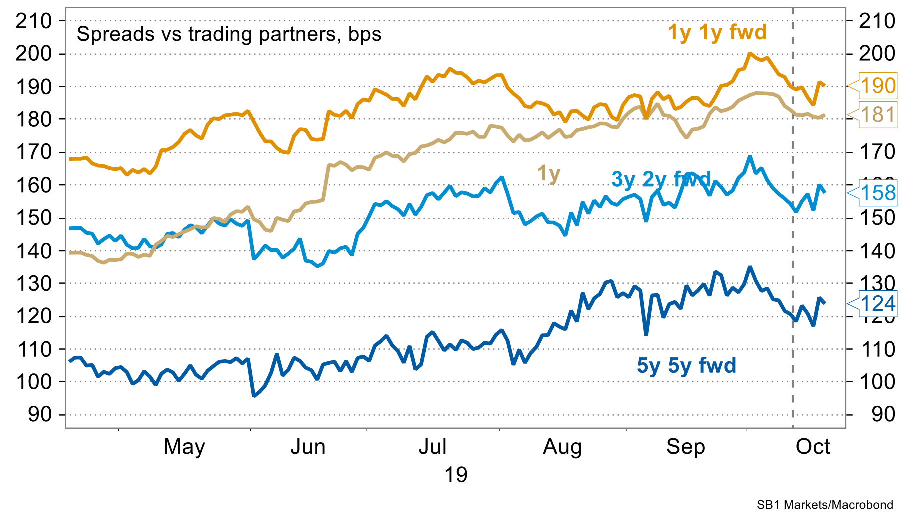


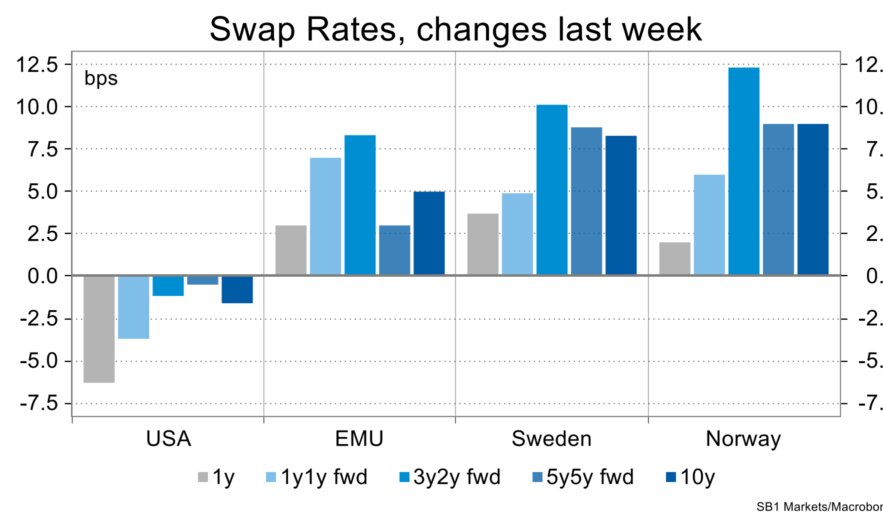


NOK swap spreads vs trading partners are narrowing, at least until last week

Spreads have narrowed the past weeks, as trading partners' interest rate rose more than NOK rates







- Swap spreads between NOK rates and our trading partners have been widening rapidly this year, all over the curve. This months, spreads have 'finally' caved in
- While 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. <u>It must be 'too' high, still?</u>

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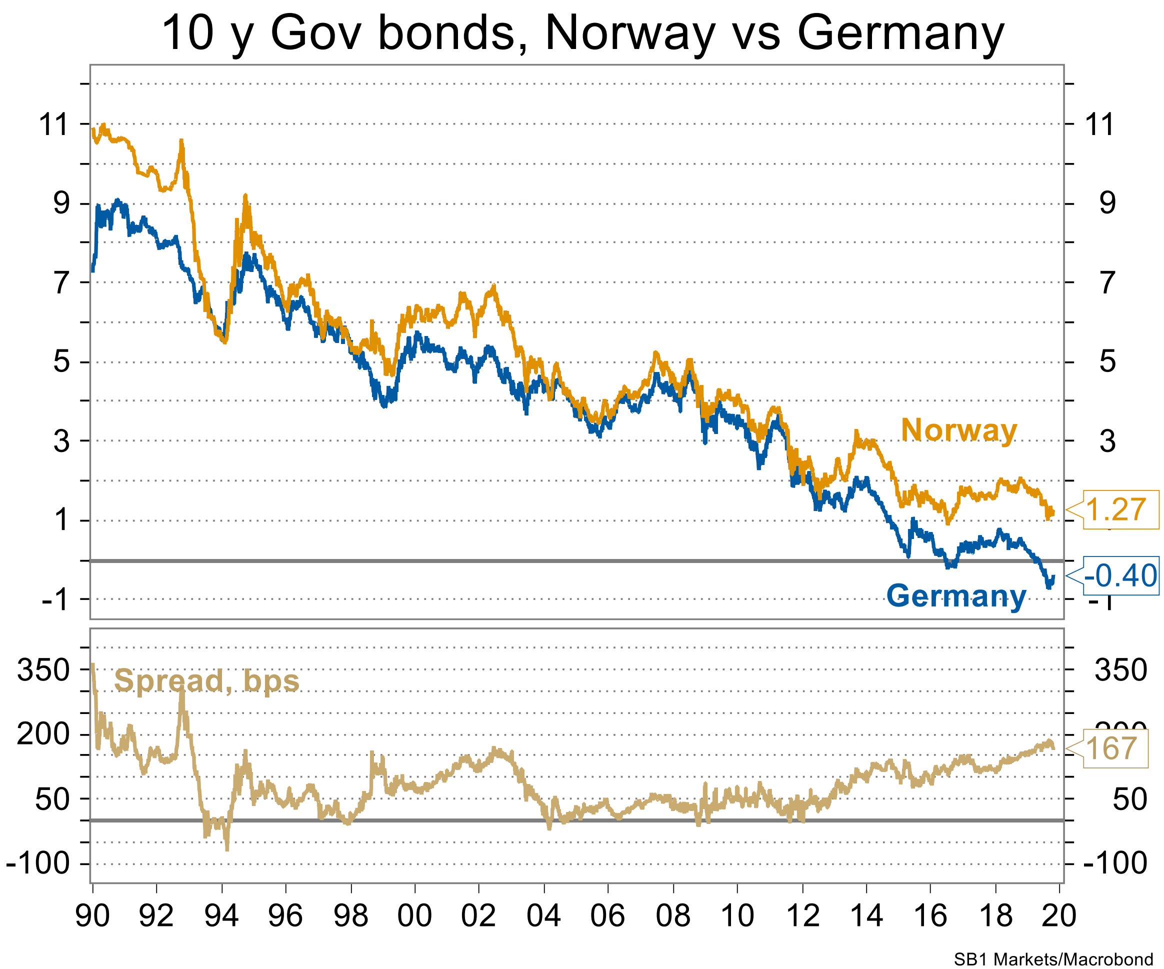
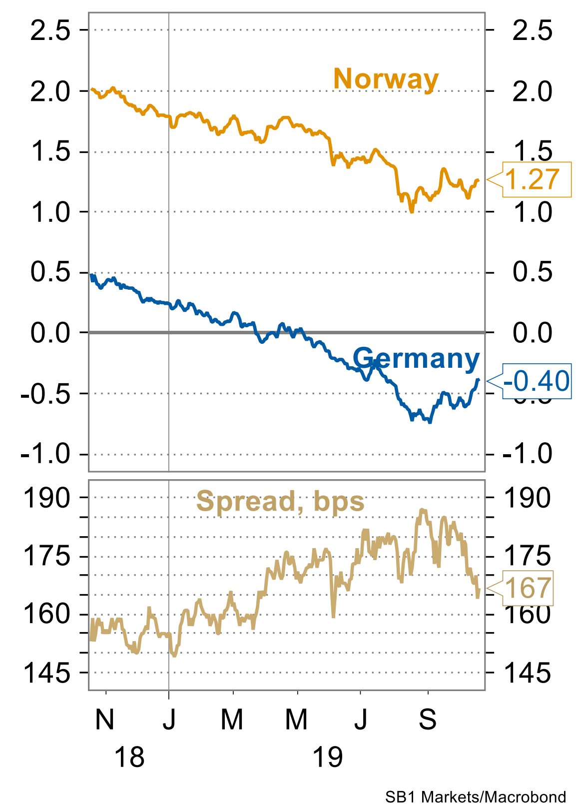
The Norway/German 10 y gov spread narrows

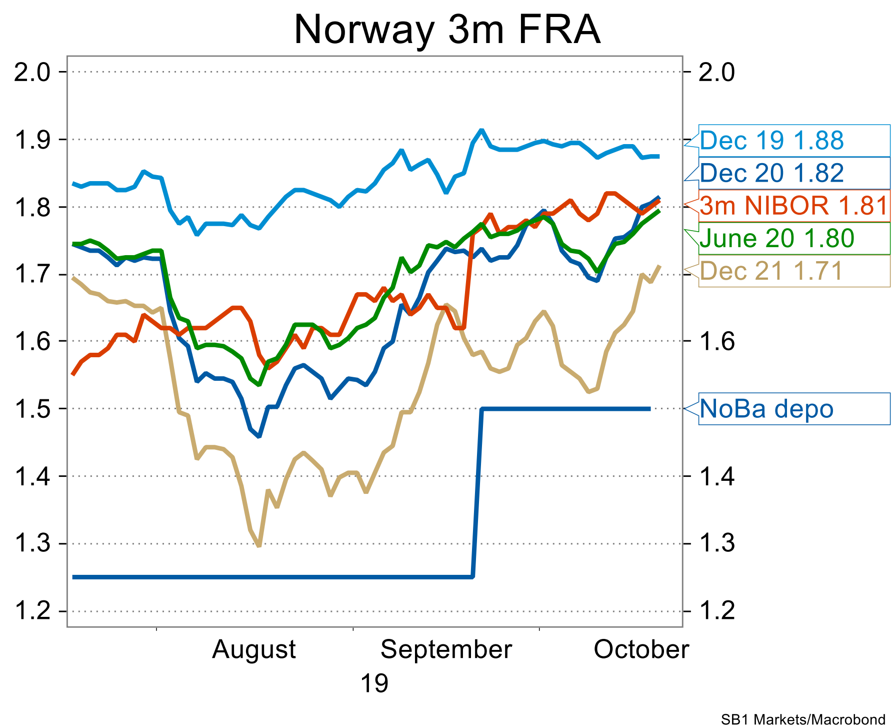
The spread at 1.67% is still unusually elevated, but it was 20 bps higher in late Sept!

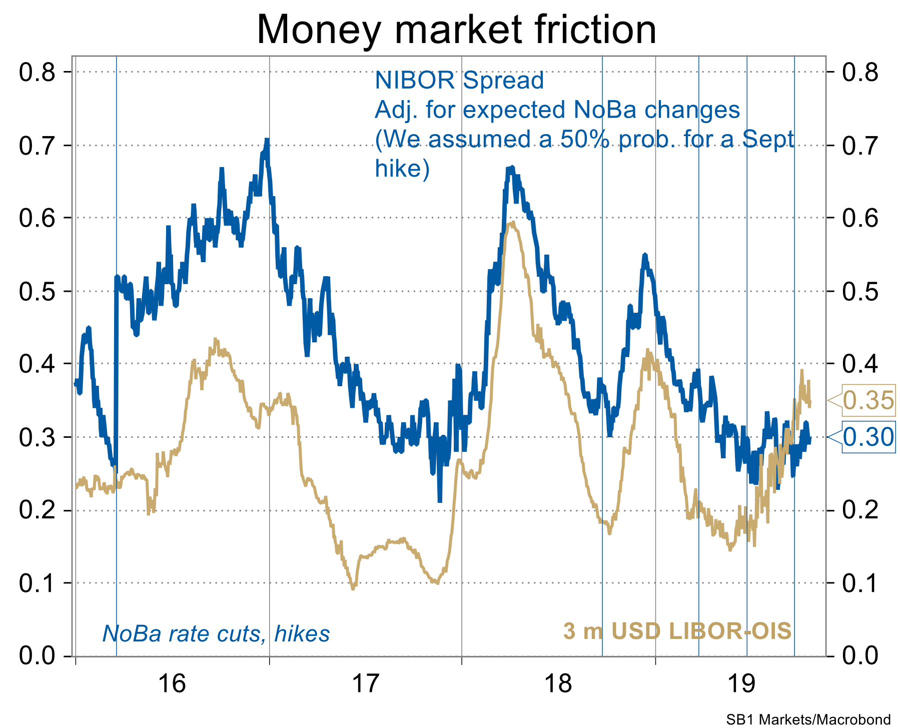




The 3 m NIBOR trends flat, at 1.81% now, more to go (up)?

Dec 20 contract at 1.88% still implies a higher spread (and zero hike probability, we assume)

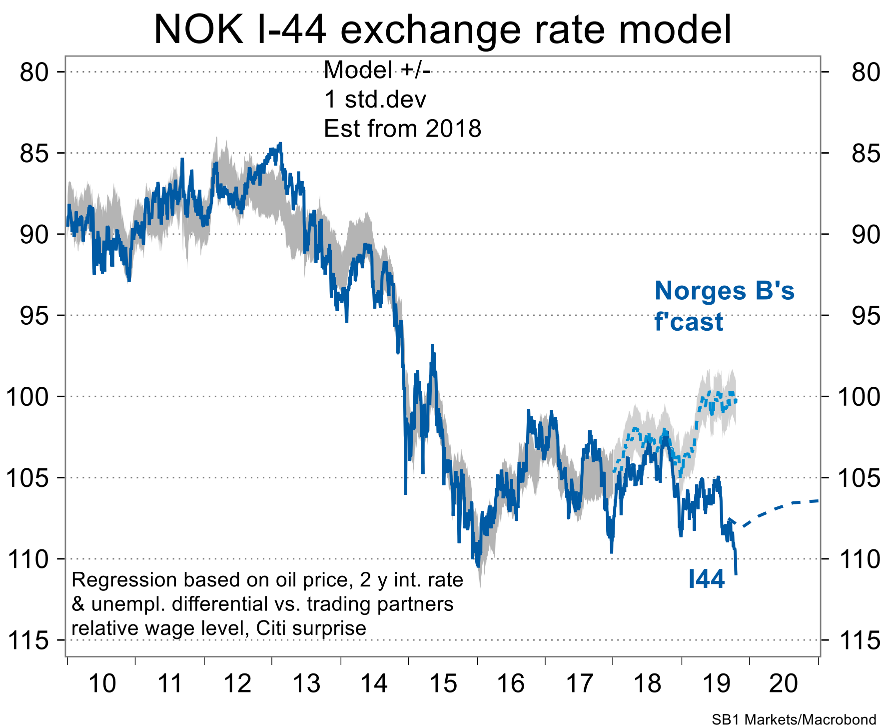


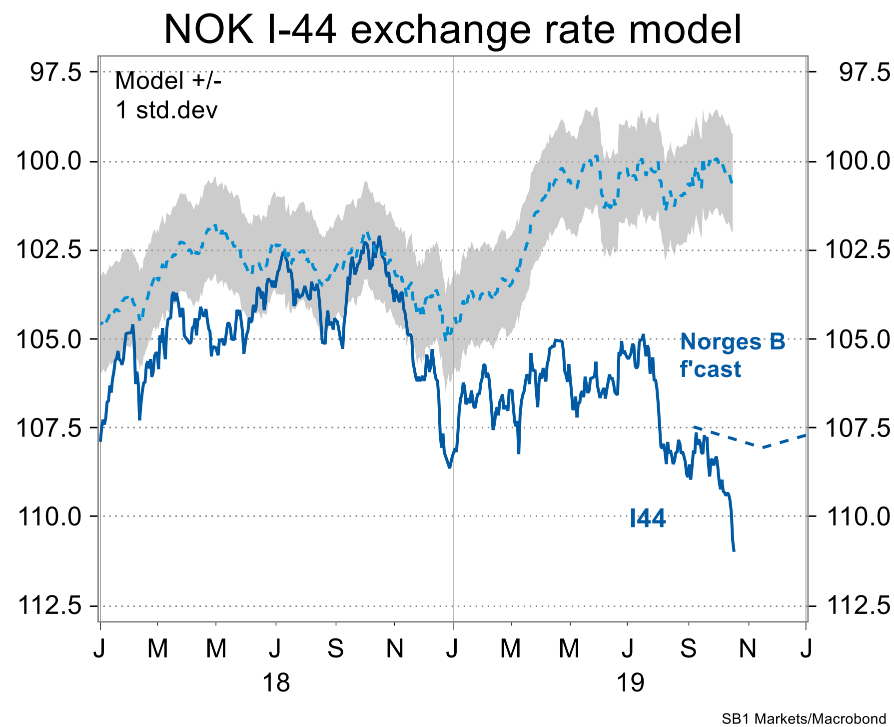


- The NIBOR – NoBa deposit spread narrowed 1 bps to 31 bps last week. Our take is that the spread is too narrow. The Dec 3 m FRA trades at 1.88% (implying a 38 bps spread), and in the US the LIBOR-OIS spread 35. Historically, the NIBOR spread has been wider than the LIBOR-OIS spread. Norges Bank assumed a 40 bps NIBOR spread in the MPR.
  - » The Dec spread may be influenced by expectations of a year end liquidity squeeze – which has happened before. The FRA-curve peaks in Dec '19, and there are smaller local peaks in the next Dec FRAs as well. Still, we expect the 3m NIBOR to drift further upwards the coming weeks
- Longer dated FRAs are climbing. The FRA curve is inverted after Dec '19, the market is pricing more than a 50% probability of at cut in Q2 2021 but not a 100% probability before 2023 (and hardly then)

Our old behavioural model: Seems like it doesn't work anymore

What can explain the NOK weakness? First some fundamental pros&cons, then an alternative model





.. And then a story on 'the Supercyclicals' – at the end of their journey?

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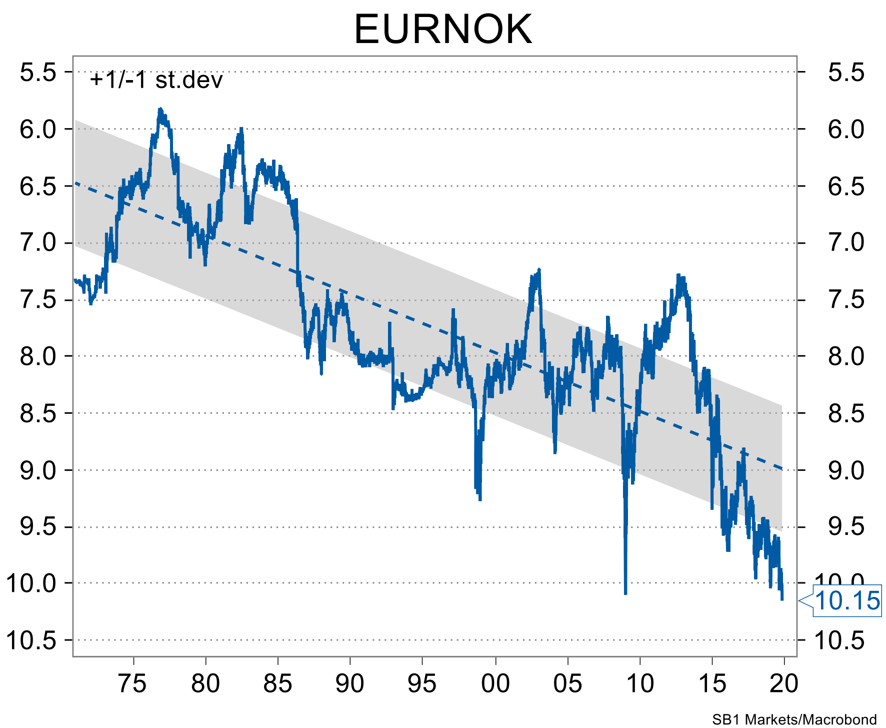
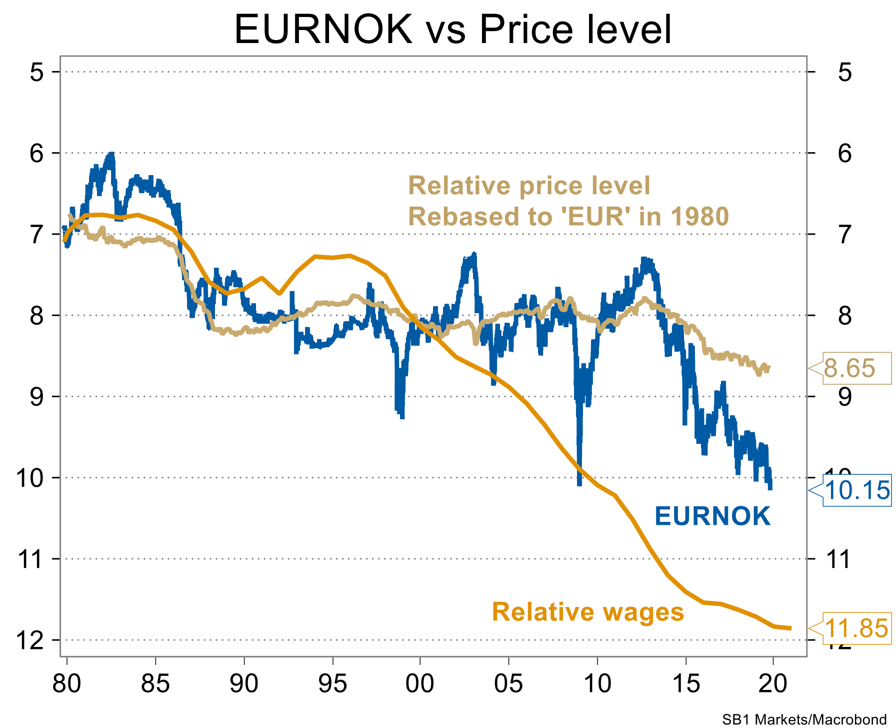
NOK on a slippery slope (as it has been for 40 years). Any good explanations?

PPP-wise, the NOK is 15% weaker than normal vs the <u>EUR</u>, but 15% too strong vs. relative wages

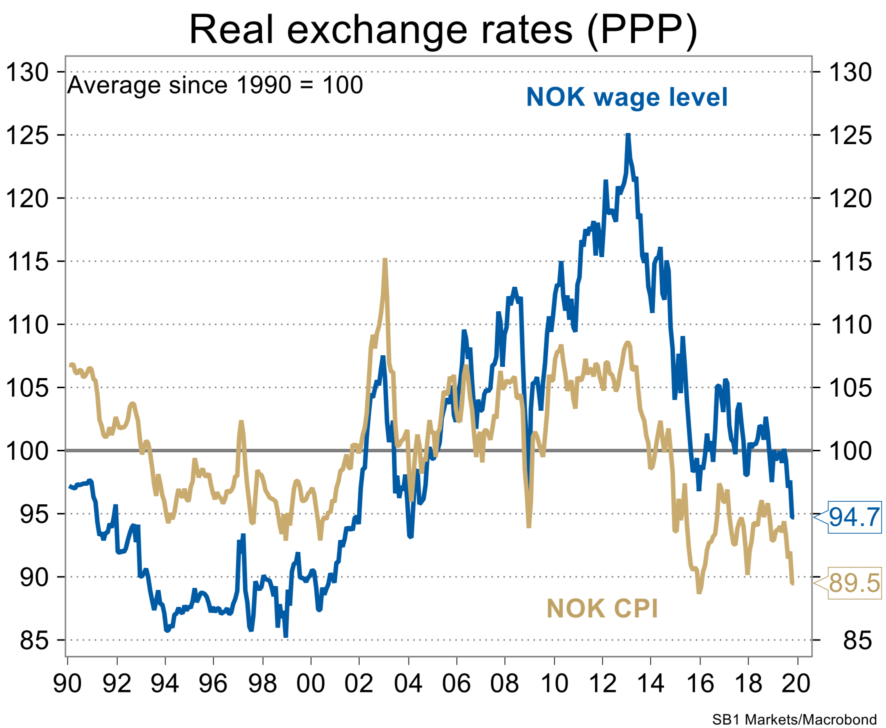


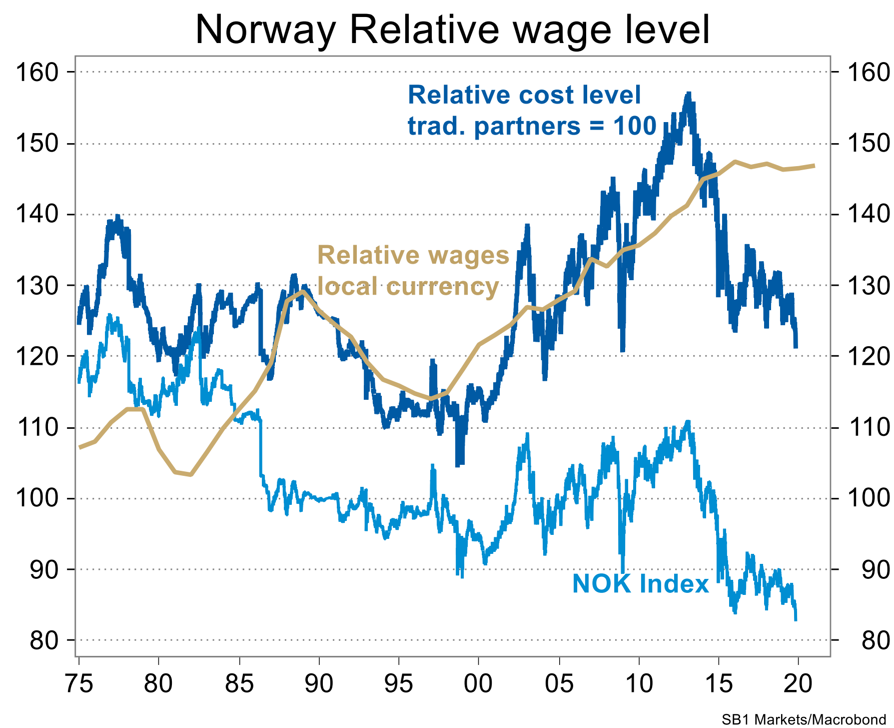


- If the relative price level should have remained unchanged vs the euro zone (a stable PPP), the NOK should have been at 8.65 (starting the calculation in 1980 or in 2000 or in 2010). <u>The NOK is too weak now</u>
- If the relative wage level should have remained unchanged vs. the euro zone, the NOK should have fallen to 11.85, if the relative cost level was 'correct' in 1980 or in 2000. <u>The NOK is too strong now</u>
- However, vs all trading partners, the cost level is quite low, *check next page*

.. vs all trading partners, the relative cost level is <u>not</u> high anymore

It's 5% lower than the average since 1990, and in line with the average from 1980 - 2000





- Compared to the pre-2000 period, Norway has established a 3 x GDP Oil fund. The expected capital income from the fund can now cover (finance) ¼ of Norway's imports. Thus, Mainland exports do not have to pay for all of our imports, as before. The cost level has to be adjusted upwards, to reduce profitability and employment in the exposed industries (exports/import competing) in order to free up labour that has to be transferred to the sheltered sector (so that we can enjoy the benefits of the fund's return)
- The cost level was most likely too high at the peak of the supercycle in raw materials (early 201) but now the cost level has fallen to a more reasonable level. If is fair or not cannot be proven. Long term a fair cost level will yield balance at the current account (ex. 'temporary' oil revenues) and full employment. Our assessment is that we are not far from that now

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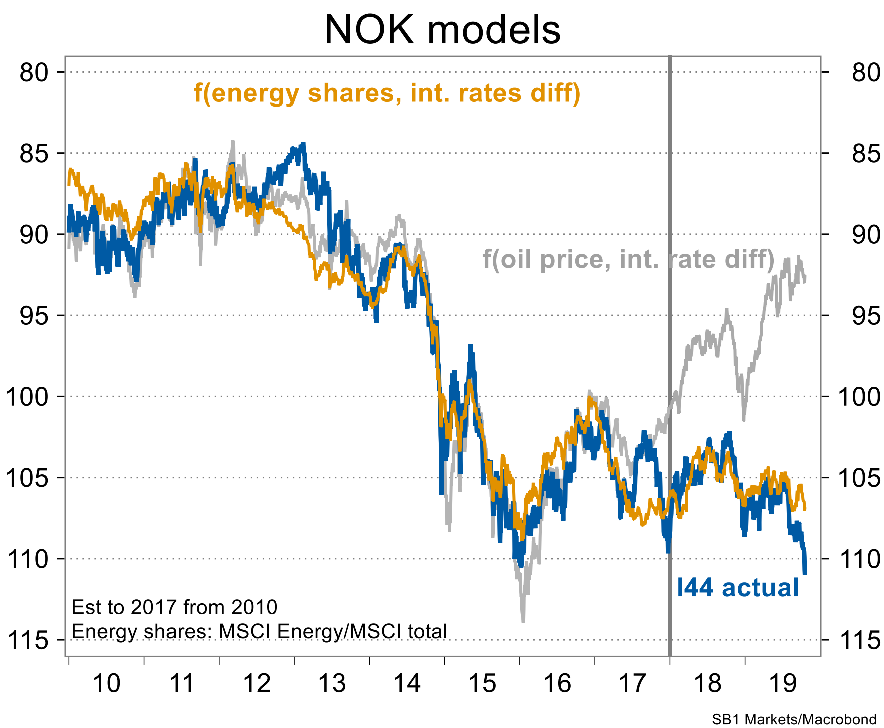
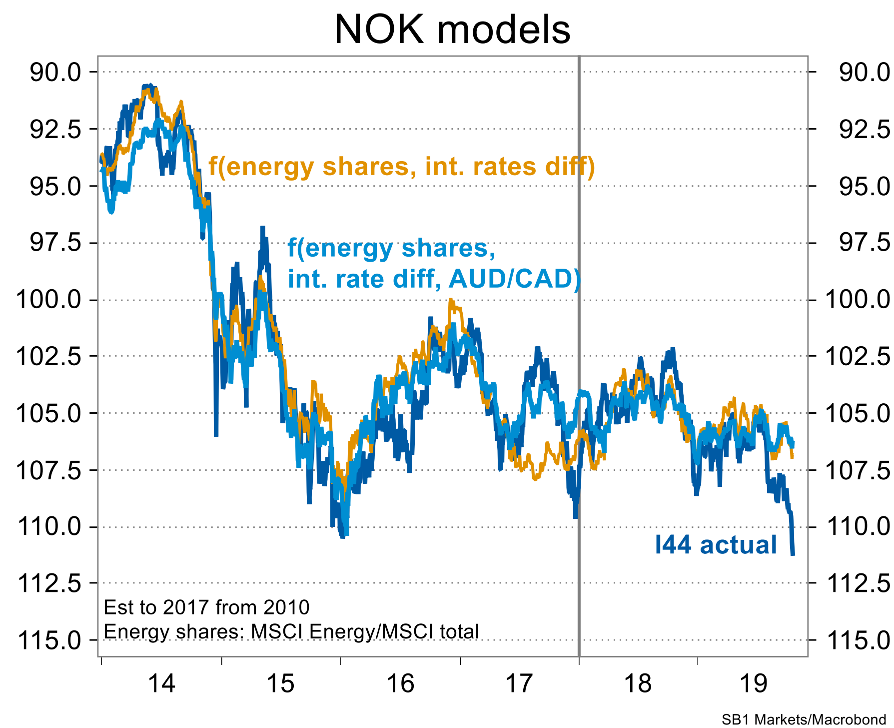
NOK hit by the green wave, like the oil industry?

Our old short term behavioural f/x model has not worked well past two years. Why? The green shift?



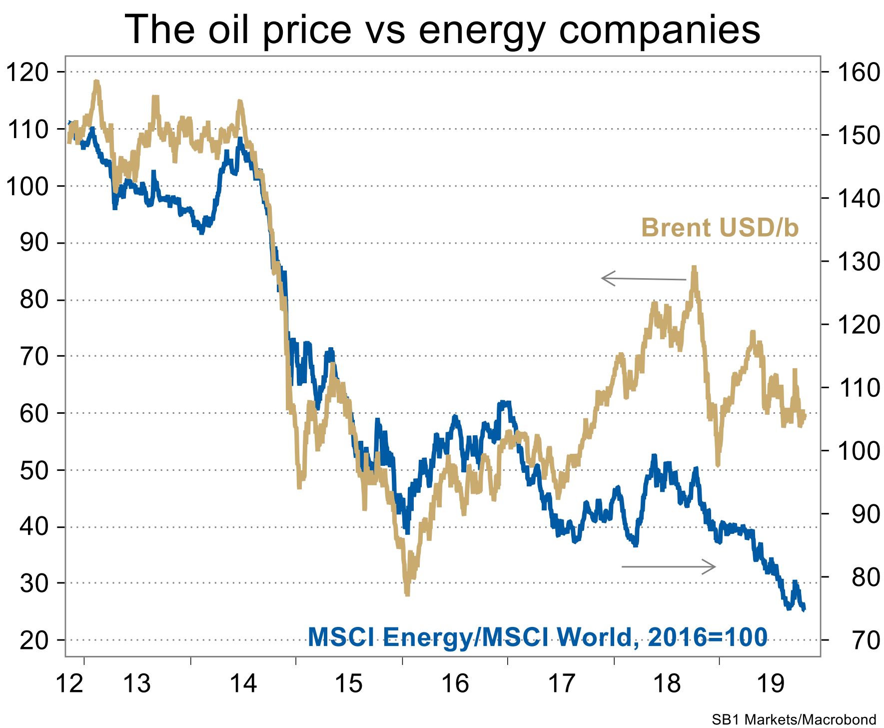


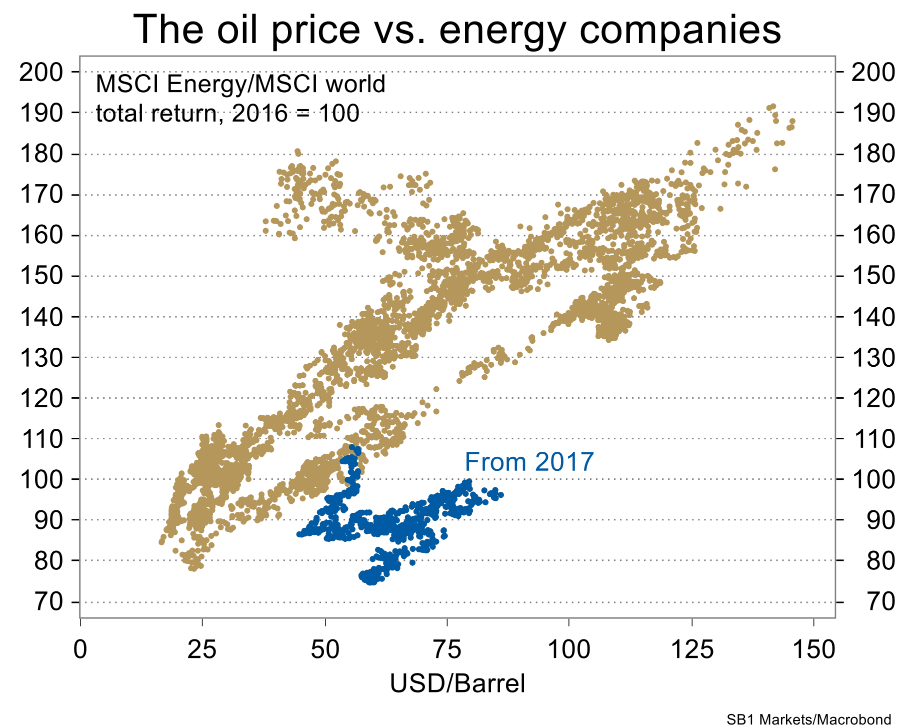
- The first step: We have swapped the oil price with the market's pricing of oil assets, measured by the relative return for energy shares vs the total market in the NOK f/x model. Until 2017 it did not matter which 'oil' variable we applied, they explained the NOK equally well. When forecasting the NOK, by using the model parameters estimated 2010 – 2017 (including the 2y interest swap rate spread vs. trading partners), the deviation is startling. The energy share model explains the actual NOK way better than the oil price model. The residual is 4%, compared to the 15% gap vs. a simple oil price model (or 10% in our augmented oil price model). The market judges the Norwegian economy as it judges oil companies, and has lost the long term confidence in both. And not because of greenwashing, but out of real concerns for the future for oil/gas producers. We think the market puts too much weight on the oil sector's importance on the oil sector, but that's another debate. *Check next page for energy companies vs. the oil price*

- If we include AUD and CAD in the model, the forecast model works even better. Both Australia and Canada are energy net exporters (Aust. coal, Canada oil/gas). Their energy exports equals some 5% of their GDPs vs 12-15% for Norway. Even a NOK model with just AUD and CAD (and SEK, but just to please our neighbours) as explanatory variables, works far better over the past 2 years than the oil price/int. rate differential model
  - » However, both the model with the relative return of energy shares and the one including AUD and CAD fail to explain the NOK weakness since late July. NOK is 4% too weak

ESG: Oil companies have fallen out of favour – and are cheap vs. the oil price

The relative pricing of oil companies have been quite closely correlated to the oil price

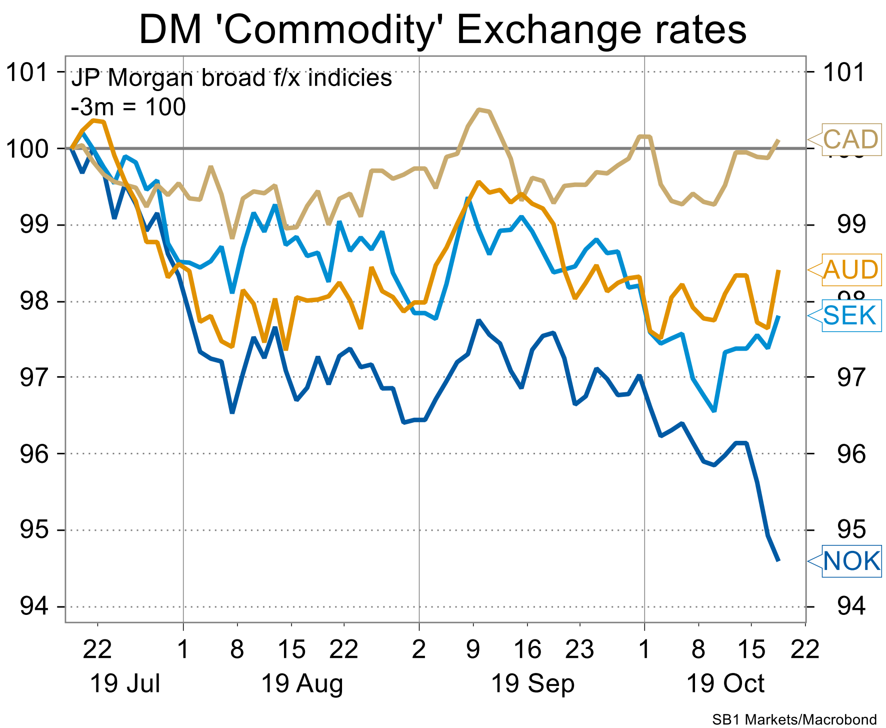


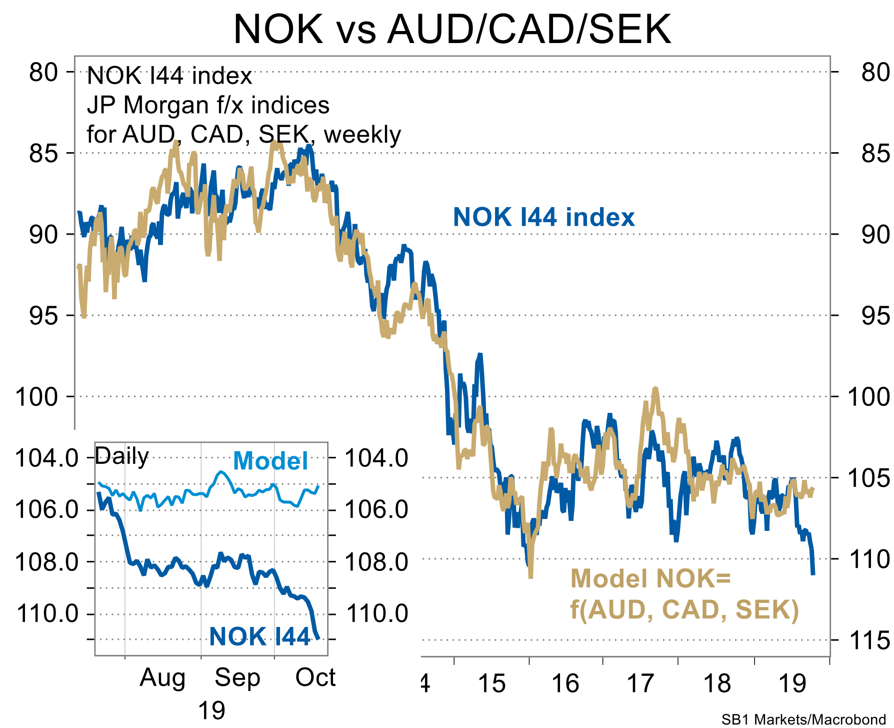


- They still are, but just after a shift down in the pricing of oil companies vs. the oil price during 2017 and '18, down approx 30% vs rest of the stock market

All supercyclicals are weak, but the NOK weaker than the others since July

CAD is stronger than the others, AUD & SEK have fallen less than the NOK since July

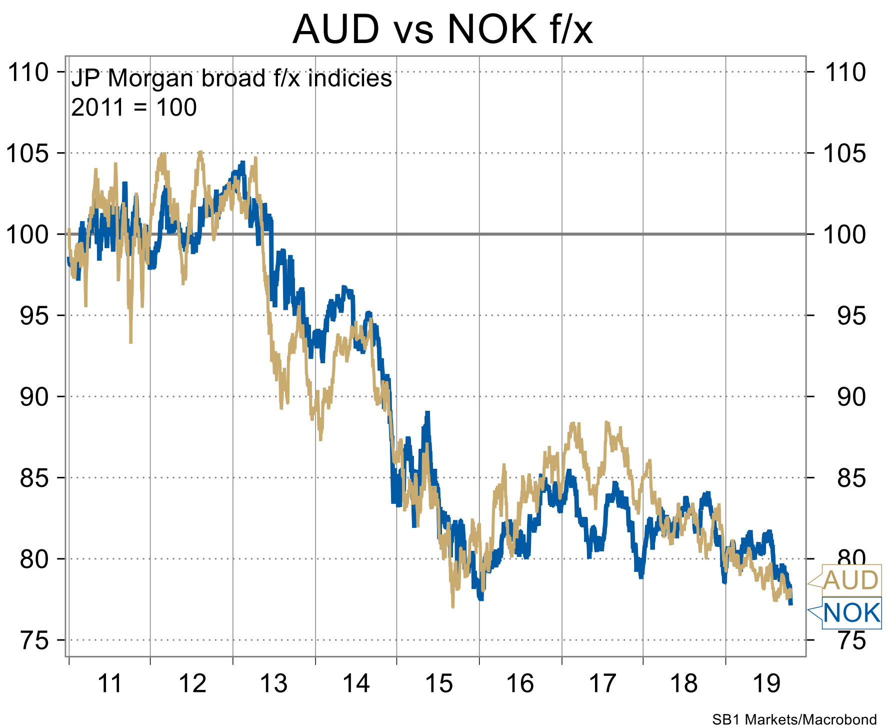


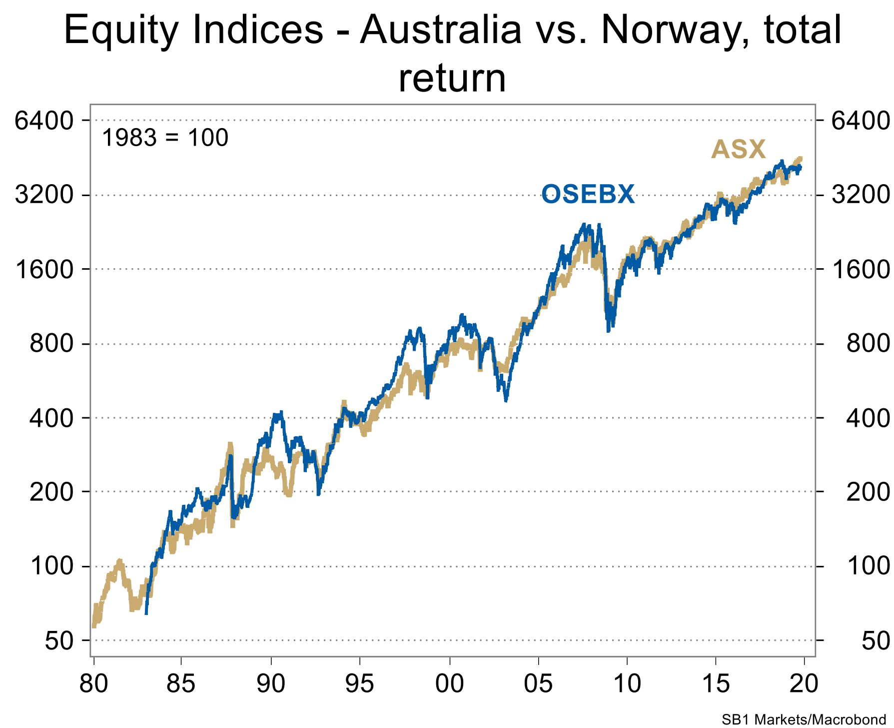


- The supercycle currencies are all sensitive to oil/energy prices (check the previous slide) and global growth outlook. The past two weeks, both CAD, AUD and SEK have recovered, probably fueled by hopes of Brexit solution, and a (slight) de-escalation of the US/China trade war. Unlike our peers, the NOK has tumbled during the last weeks
- Together, the other supercyclicals cannot 'explain' the NOK setback recent weeks. The NOK has lost 6% vs. the supercycle f/x model estimate since mid July. The discrepancy is not unusual but not something that happens that often either
  - Our model is tilted towards the link between NOK and CAD, more than towards AUD and much more than towards SEK (even if AUD works pretty good). Since July, the CAD has been rather stable, while AUD & SEK have depreciated but both less than the NOK

.. Or make it even simpler: Just check NOK vs the Aussie!

The same goes for the Oslo Stock Exchange vs Sydney, of course

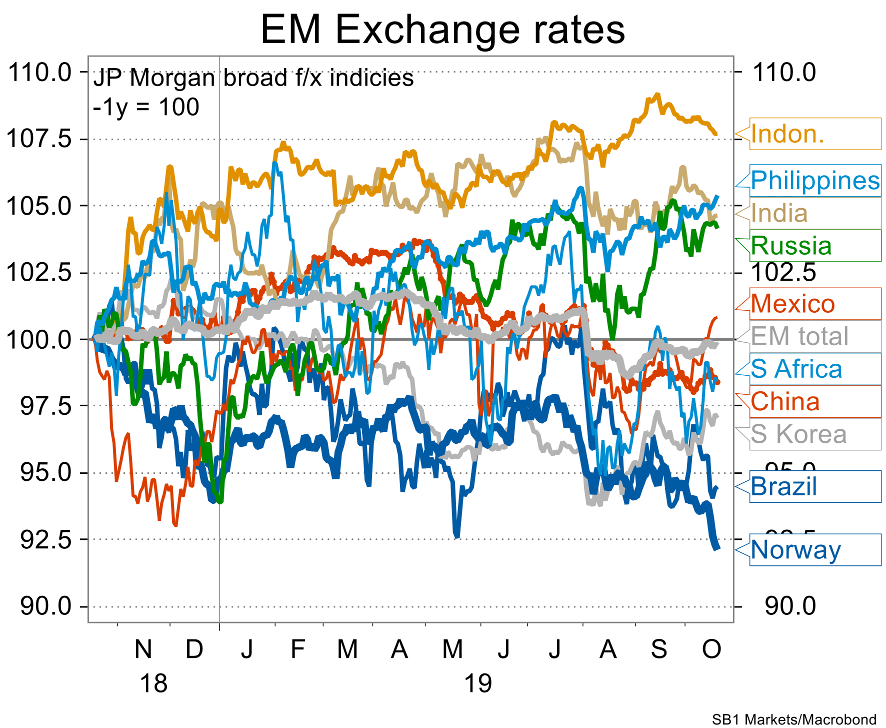


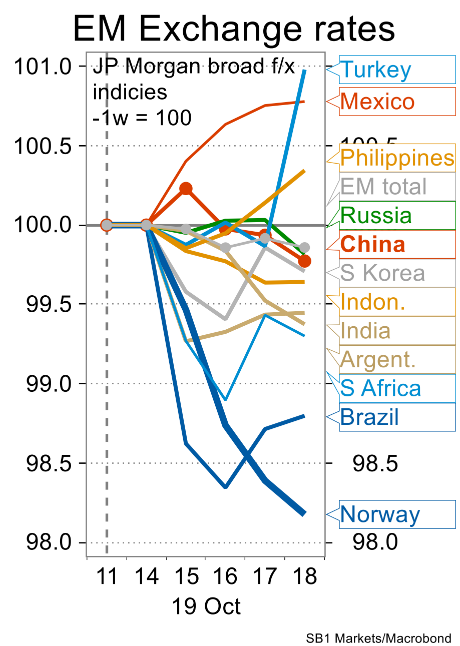


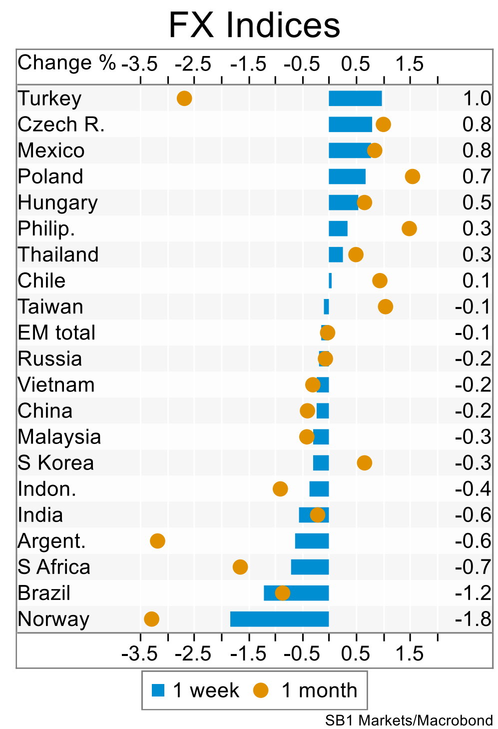
- Australia has cut rates, Norway has hiked. Does not matter at all, it seems like, vs their currencies

EM f/x in sum down last week, including the CNY

Most EM currencies have been stable the past month, x Turkey, Argentina (and the non-EM(?) NOK)







- Most EM currencies have stabilized/recovered in Sept/Oct. Trade war de-escalation probably the best explanation
- BTW, if we take out the Argentinian peso, the NOK has fallen substantially more than any of the (other) 18 main EM currencies we are following the past year!

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