24 August 2020

Macro Research

Week 35/2020

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Last week: Corona down in the US, up in Europe but slower. *Most rapidly up here*

- **Mixed corona news:** The number of new Covid-19 cases in the **US** fell faster again, the 'R' is now well below 1. The level is still high, and restrictions should not be lifted now – but perhaps before early November? The no of hospitalised patients is declining too, deaths should follow. In **Europe**, the no of new cases is still on the way up, with **Spain** in the lead – and new restrictions will be imposed. No of new cases in **Denmark, Sweden and Norway** are on the way down again, in D & N following rapid increases through July and early August. **South Korea** is fighting a substantial outbreak

- Recent tightening of restrictions or substantial changes in behaviour vs Covid-19 have so far **not hurt the overall economy in any major way** in the US, and probably not in Europe either. However, the activity is still below trend, growth may have slowed somewhat, and the real unemployment rate is sky high. The virus is still around – normal social activity (broadly defined) is not yet feasible anywhere. A new antibody based plasma treatment was approved by president Trump yesterday. No negative news on the large number of vaccines that are under development. Still, few believe vaccines will be widely available before early next year, at the very best. Thus, some sectors will still struggle, for months and quarters to come

- **The global composite PMI** rose approx 1 p to 51.8 in August, according to the preliminary prints. **US** surprised at the upside, **EMU and Japan** at the downside. In Japan, the PMIs signals a further decline in activity, even if most actual indicators are pointing up. Elsewhere the PMIs are still far weaker than the real activity data signals. In the US, two regional Fed manufacturing surveys fell more than expected but does not signal any contraction in August

- **US housing data were much stronger than expected in July/August.** The minutes from the FOMC late July meeting did not signal that bank is eager to immediately reformulate the monetary policy regime (bearish for bonds) but also that the committee, in the midst of the recent corona outbreak, was worried growth could surprise at the downside (bullish for bonds). No compromise on another **US fiscal stimulus package**, but most expect a wonder to suddenly to happen

- **The Swedish labour market** has weakened substantially and hours worked has fallen more than in Norway. Still, **house prices** have climbed to well above the pre corona level – except for Stockholm which is still below

- **Norges Bank** kept the policy rate unchanged at 0.0%, and signalled no intention of lifting the interest rate path in September, and was more dovish than we assumed. Market FRAs fell but are still up over the past weeks. **Oil companies** did not revise their investments plans by much in the Q3 investment survey, even if the oil price has doubled, and oil taxes are cut. Investments will decline substantially through both 2020 and 2021. **Manufacturing power supply** will cut too. Late Friday, the main trade union and the employers' association finally agreed upon a 1.7% **wage growth** in 2020, of which 1.2 pp due to a carry-over from wage increases through 2019. Minimum wages are lifted by some 5%. The deal will be the norm for the following negotiations.

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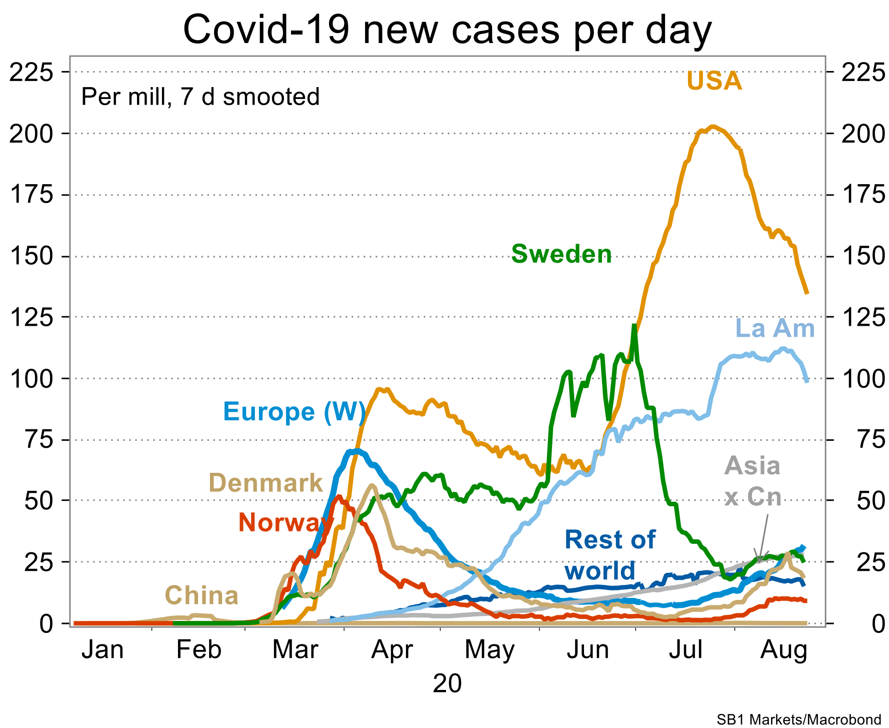
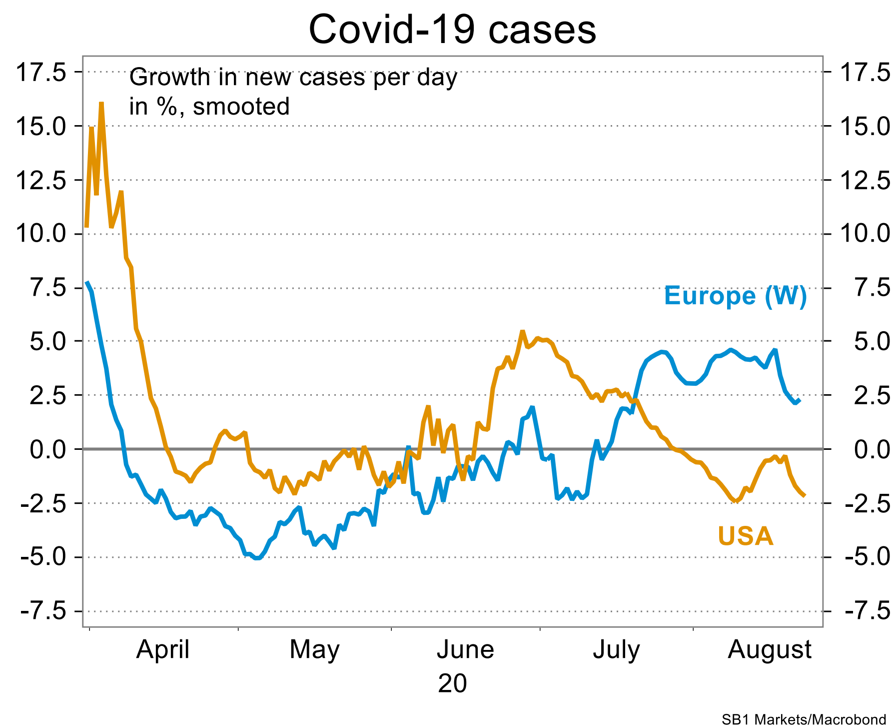
Europe still on the way up – US regained the speed downwards, still at a high lev.

Decline in new cases most other places, in Lat.Am and Asia (ex South Korea), and 'ROW'

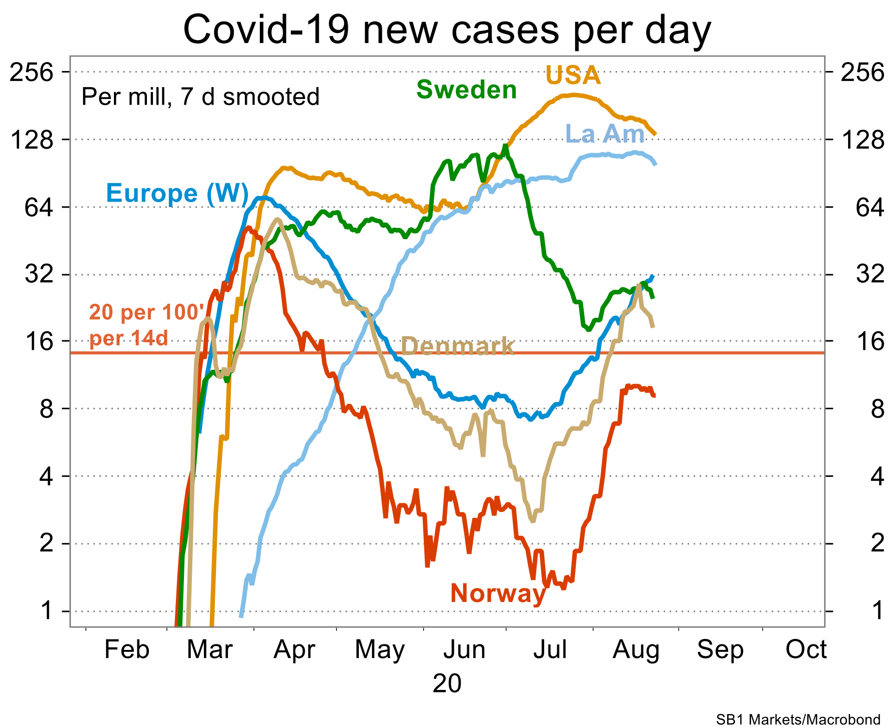




- **The US** curve is sharply on the way down, the 'R' is well below 1, even if some states are still struggling. The no of new cases is still very high, and it will take weeks to get it down to a level where restrictions should be eased again. Could it happen before early November? Most likely. The no of hospitalised patients is falling sharply, and soon will the no of deaths will decline too. The economic cost of turning the curve has been limited
- Growth in new cases in **Europe** is has slowed somewhat but the 'R' remains clearly above 1. More measures are still needed – and they will come. Since the level of contagion is 1/5th of the level in the US, Europe still has time to act (was 1/10th when US peaked)
- **Norway** took the lead in growth in new cases three weeks ago – but now the no is heading slowly down again. Some few measures are tightened – but the overall economic impact is very likely minimal. Sweden and Denmark is turning down too!

A log scale reveals some disturbing trends before they are ‘visible’

The trend was not Norway’s friend, at least not until last week. Denmark still rapidly on the way up



- Corona curves can be bent, if needed. This time around, the economic cost seems to be small vs. the spring experience
- Restrictions are tightened in several European countries, and more will probably come. The curve is still pointing upwards
- Denmark, Sweden and Norway are reporting fewer cases again
  - » Further measures to reduce the spread of the virus would probably not be needed
- More measures may be needed in Norway but the most recent data do not signal a further increase in the spread of the virus

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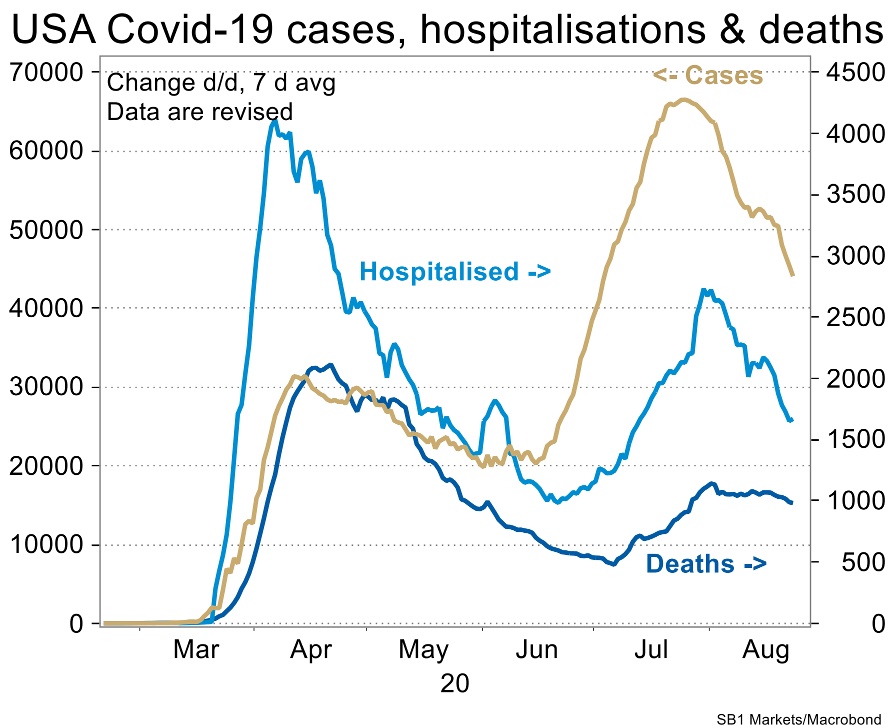
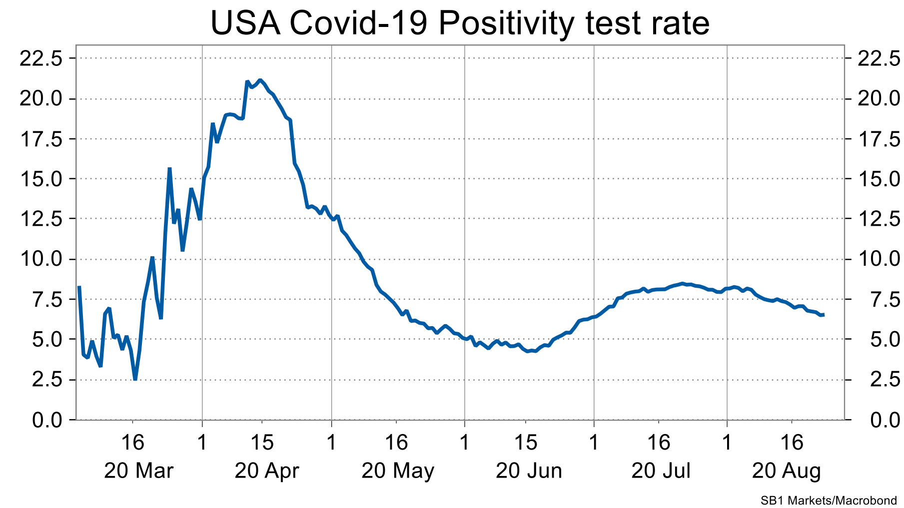
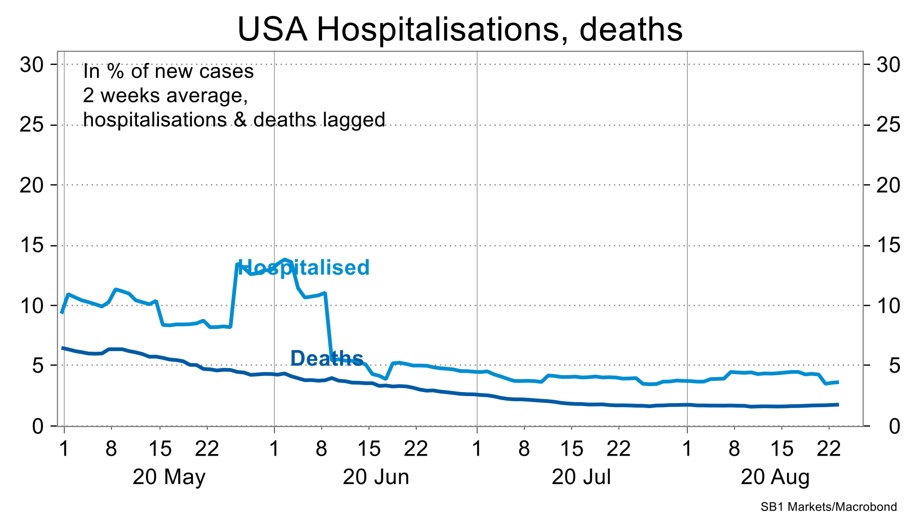
USA The no of new cases is falling sharply again

... And some more tests are taken



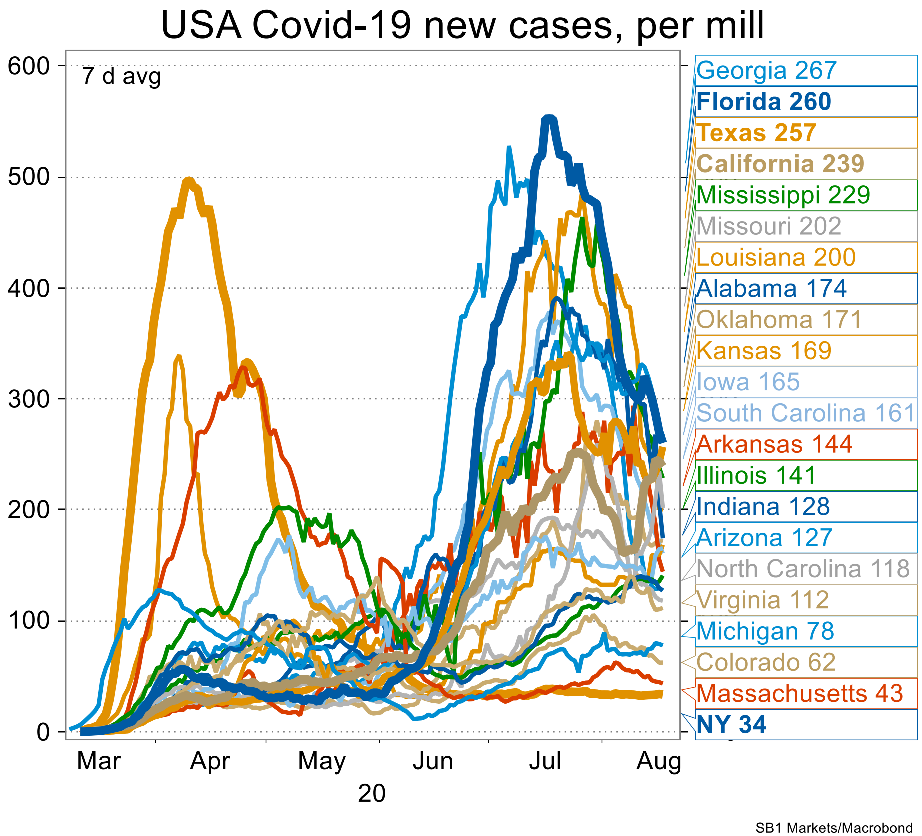


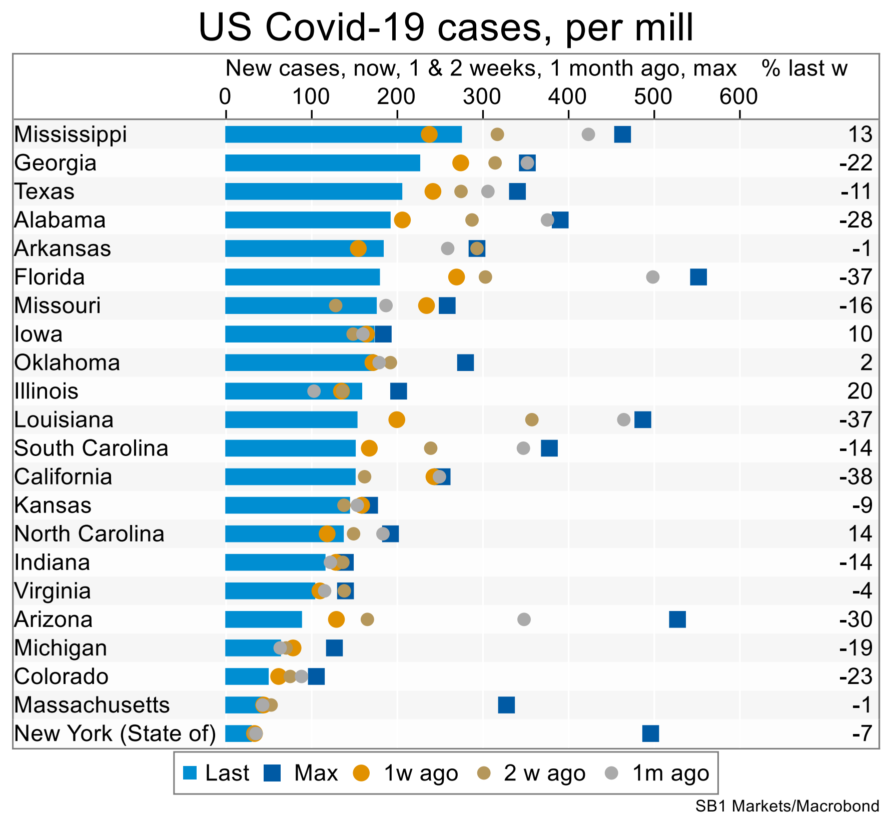


- The hospitialisation rate is far lower than during the early phases of the pandemic but has not fallen further the past two months
- The death rate (CFR) is still trending down or at least it din until late July.
  - The level is just a fraction of the level during the spring, due more cases counted (cfr the decline in the positivity rate), more young people infected and most likely better treatment methods

US: The virus has not disappeared but the overall trend is down

Will the virus mysteriously disappear before November 3rd ? May be, may be not

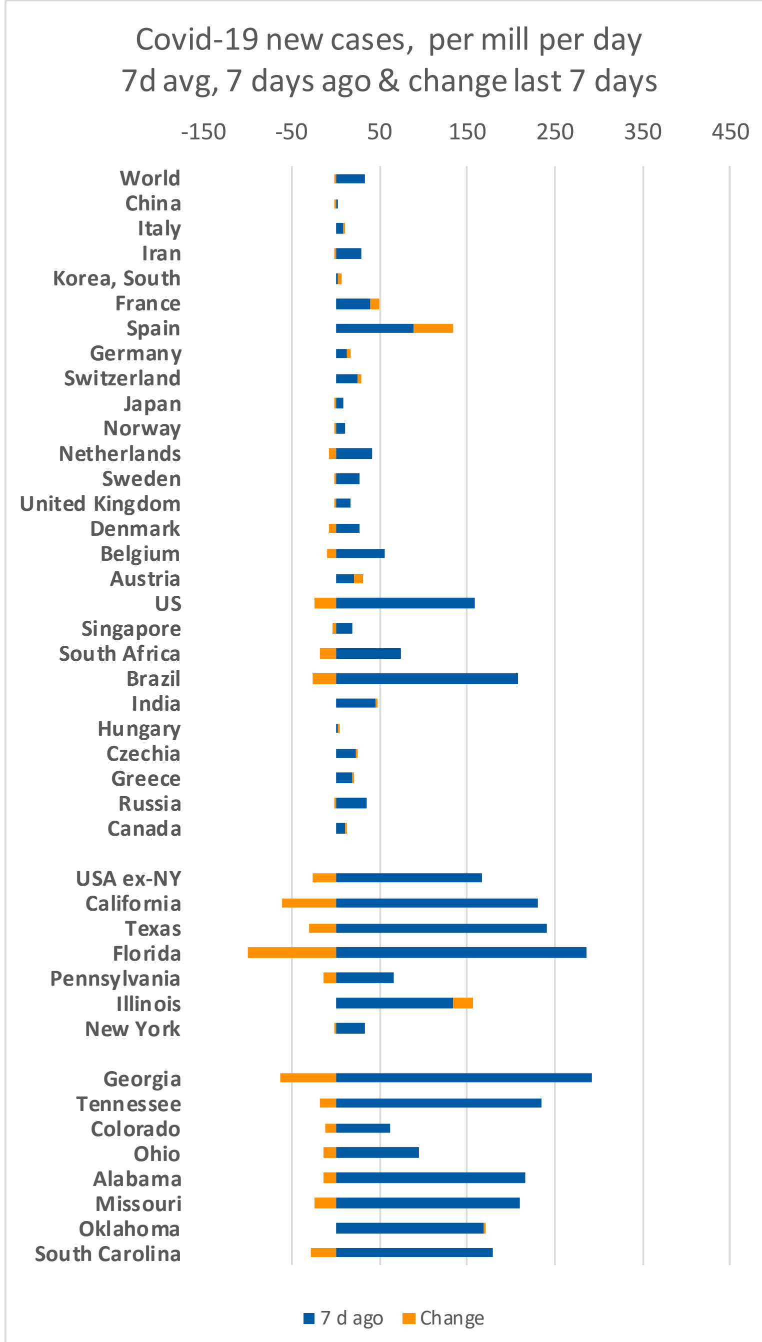


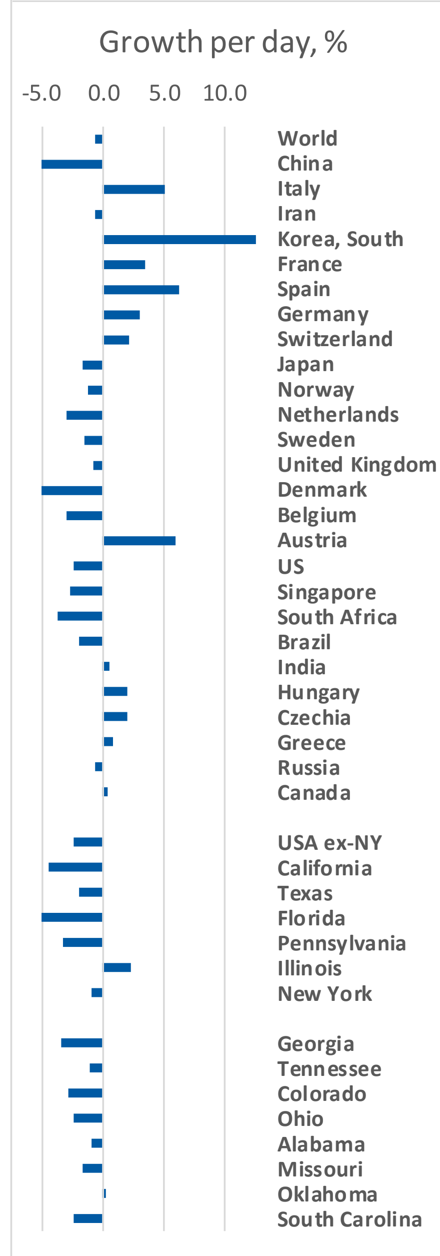


US & the rest: A comparison

More up than down (ex US)

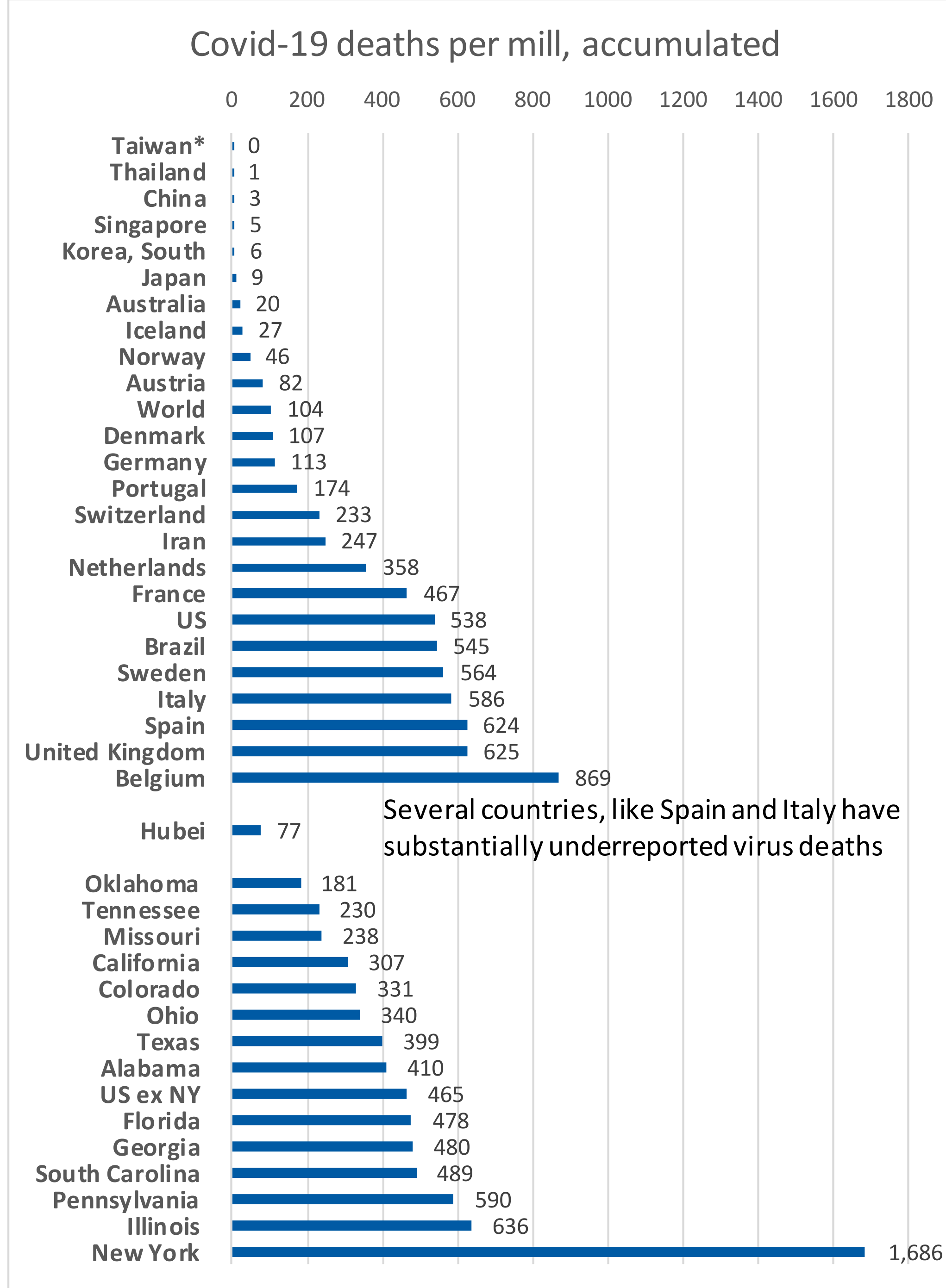
- Three weeks ago, most countries reported an increase in new daily cases but now R has fallen below 1 in several countries, of which US is most important – both economic/market wise, and because US had the highest incidence, and a rapid growth
- In Europe, most countries are still reporting more cases, but at a slower pace than the previous week in the majority of countries
  - » Spain still has the biggest challenge, and growth accelerated last week
  - » Norway reported the highest growth 3 weeks ago, 11%, R = 2!! Now on the way down, from a low level
- Sweden was an outlier in Europe but the number of cases & deaths has been falling sharply, now flattish
- <u>South Korea has reported a large outbreak but the overall level is very low</u>
- We do not trust all of these data
  - » There are changes in test policies & capacity
  - » Some countries do probably not report properly





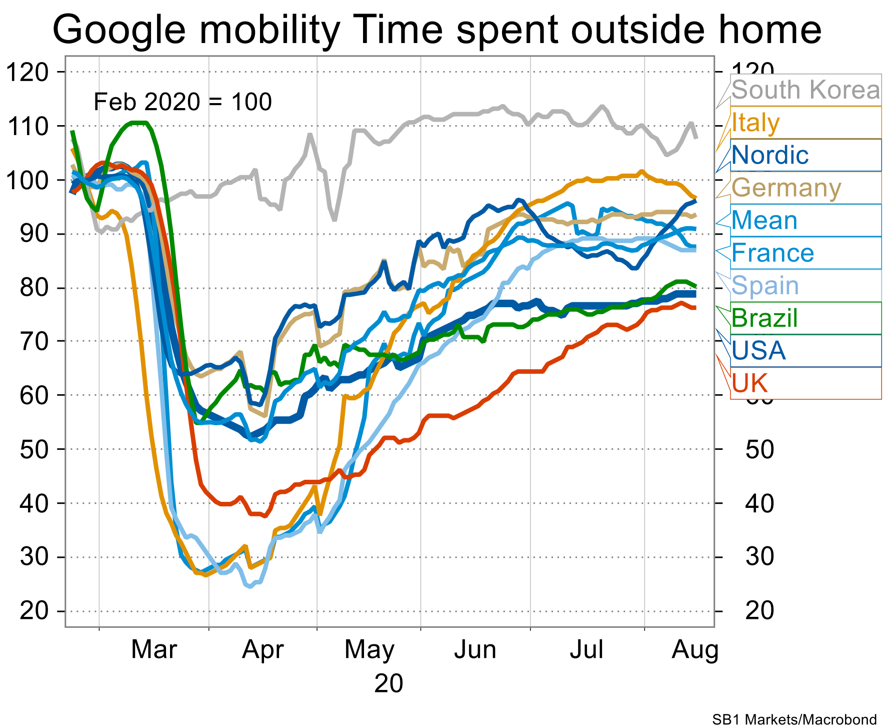
The final count

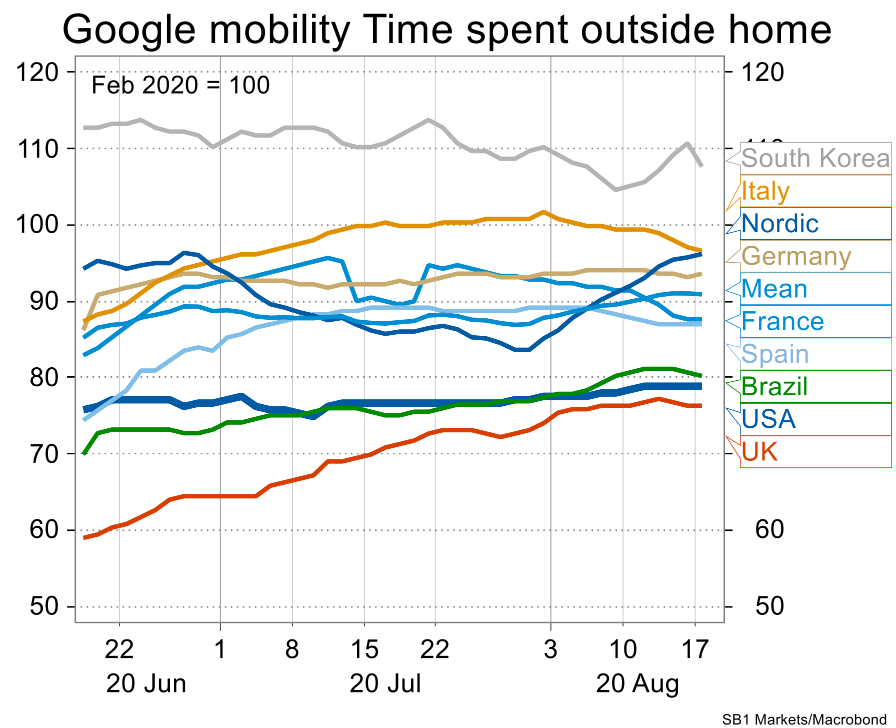
So far, that is



Time spent outside home on the way up, and now in the US again

Data are volatile and seasonality may be fooling us now, at least vs. a relevant economic analysis

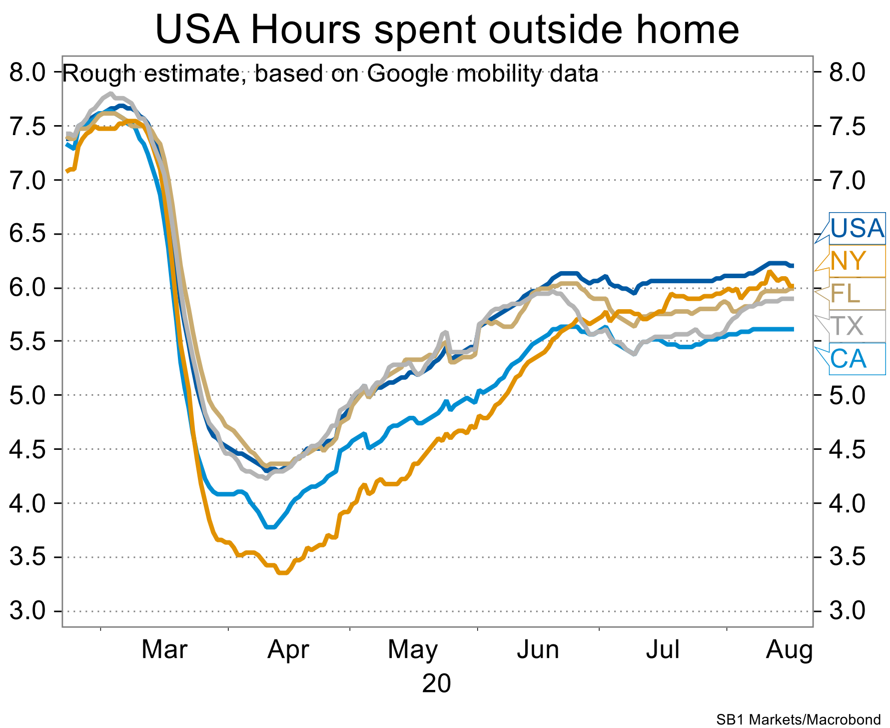


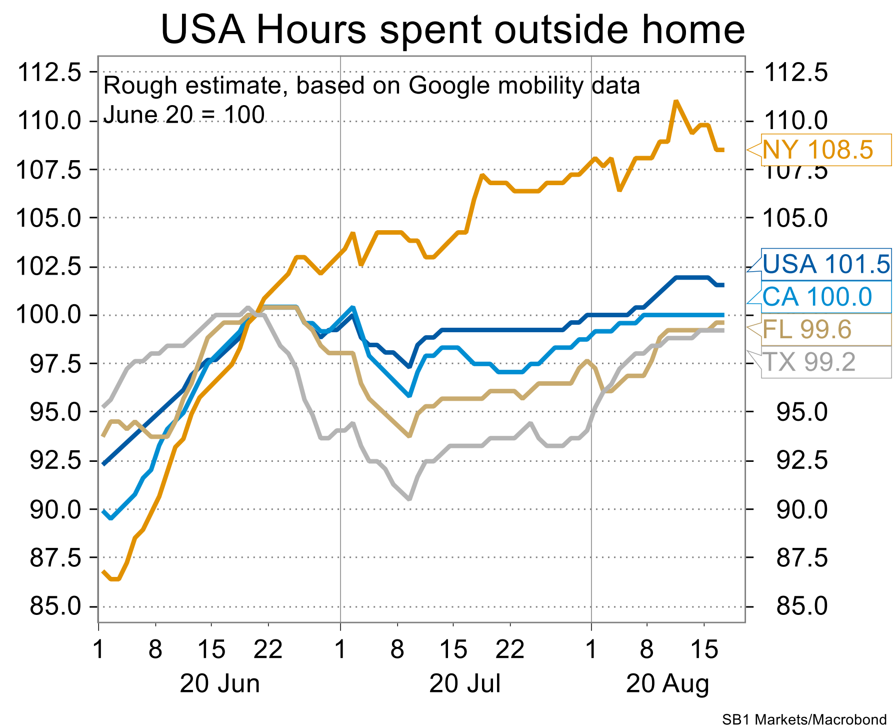


- The Nordics are quite similar, except for the 2 – 3 weeks from mid March where time spent outside home fell less in Sweden than in Denmark and Norway

Since June 20: Hours spent outside home +11% in NY, flat in CA/FL/TX

Whatever the authorities decide, the corona situation will influence the economy significantly





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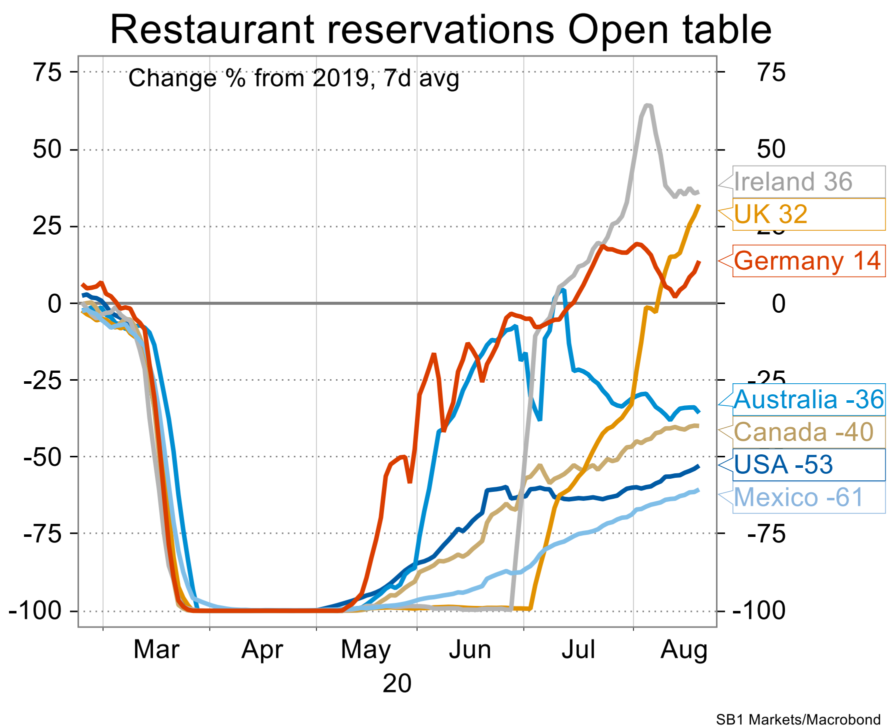
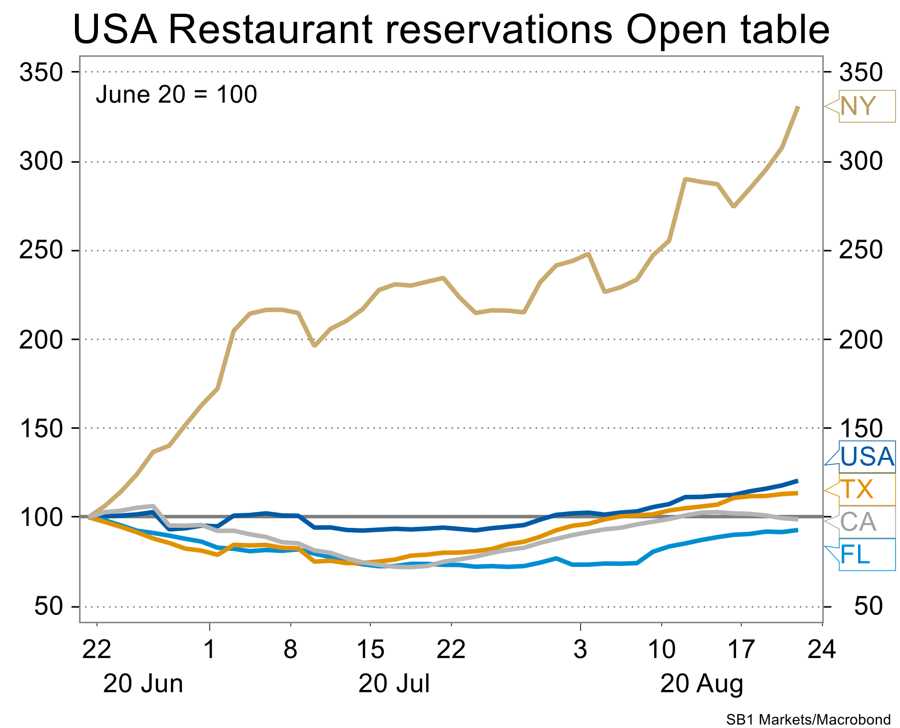
Restaurants are not open for normal business

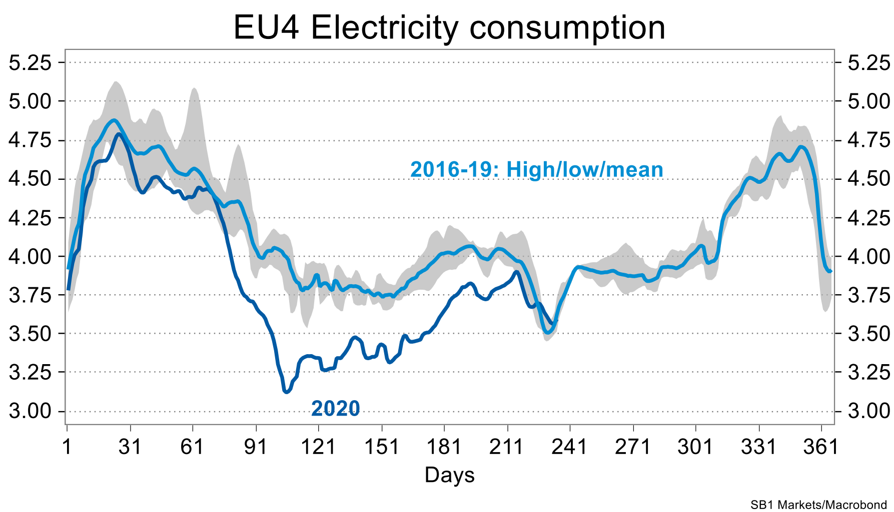
… if the corona virus is not brought under control. US i gradually on the way up again? Level still low

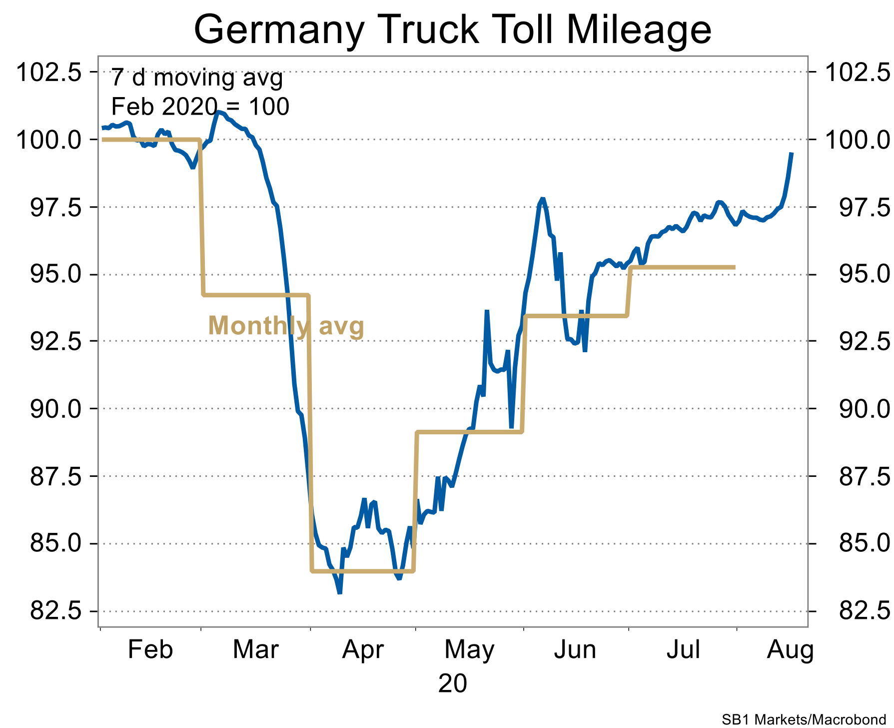


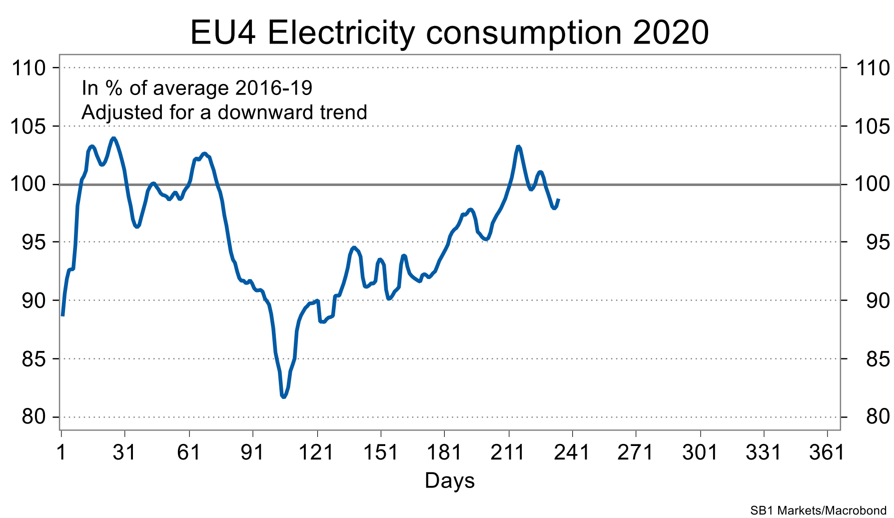


- There are huge differences between US states. NY has been moving sharply up since June 20, almost 200% up. At the other hand, California, Florida and Texas first fall – are not slowly recovering again – but they are just flat since June
- Australia is struggling again – and restaurants are not the place to be
- UK is back on stage, at least restaurant reservation through Open table

Electricity & German heavy transport: No signs of any slowdown

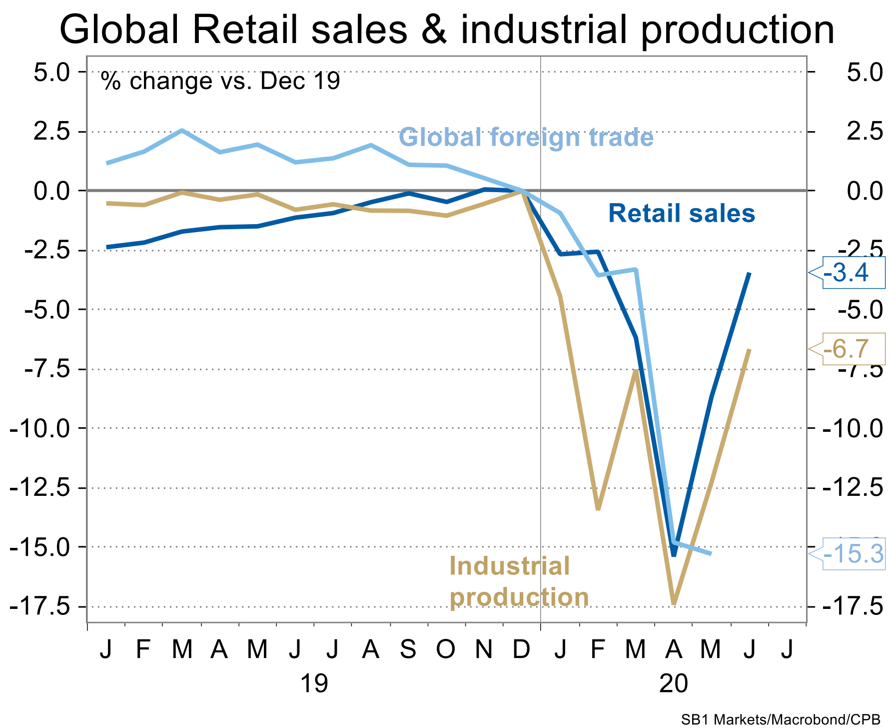


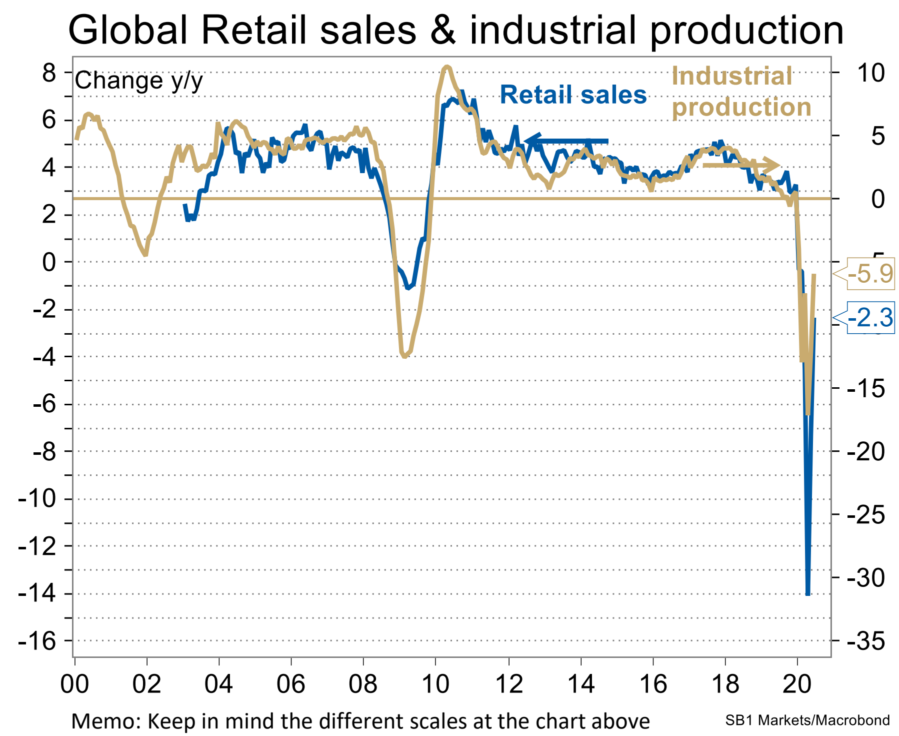




Industrial prod, retail sales further up in June, both still below pre corona trends

Retail sales are 3% below the Dec 19 level, >4% below trend. Manuf. 7% below Dec, >8% below trend

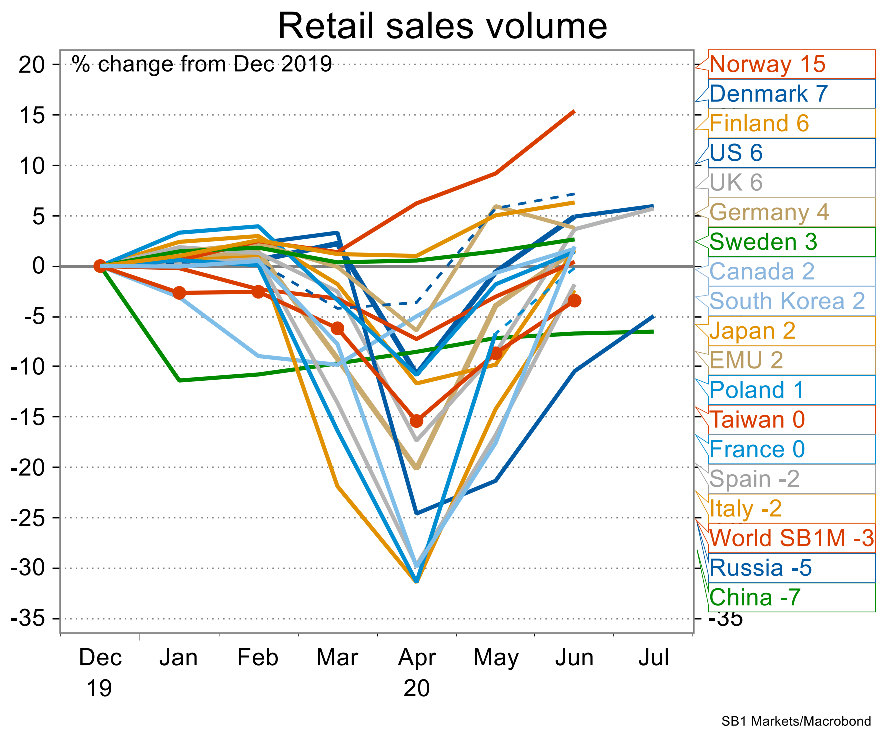


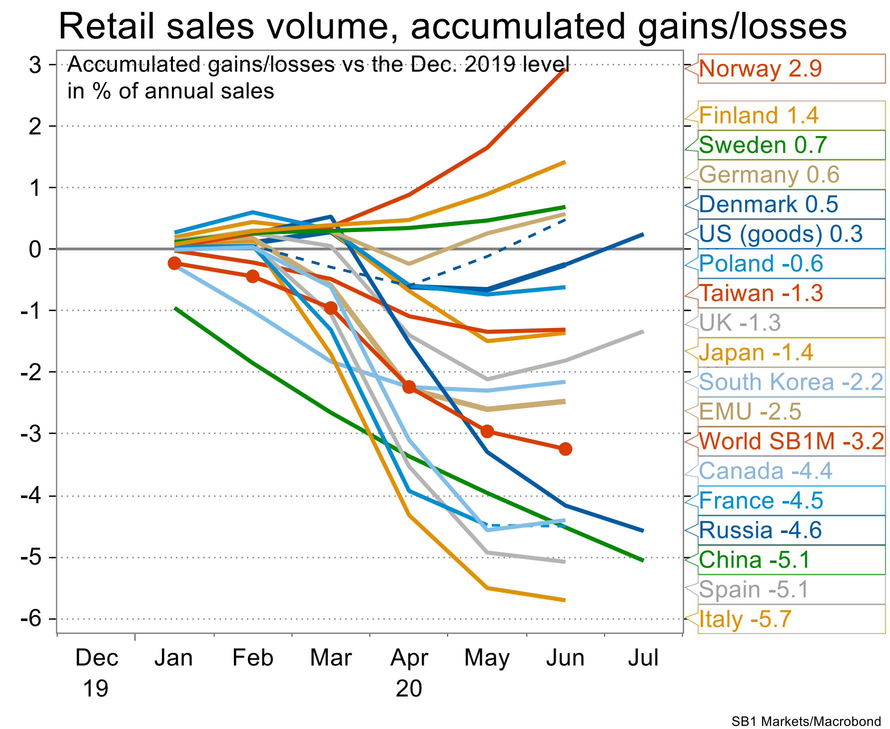


- Global retail sales grew 6.5% in June as in May. Sales were just 3.5% below the pre corona level. Sales in many DM countries are above the Dec level, China is still well below (Not all countries have reported June data)
- Industrial production rose 6.3% m/m in June, close to the May outcome. Production was still 7% below the pre corona level. We assume production rose some 2% in July, and not faster in August
- Global foreign trade fell marginally in May, and was 15% below the pre corona level. June will be far better

Retail sales are on the way back to pre corona levels

… sales are above the pre corona level in many countries, even accumulated through the 'crisis'





- We assume global retail sales rose more than 6% in June, as in May. If so, sales were still 3% below the pre corona level in June. In May, sales rose in all main countries. Norway is in the lead, far above any others, measured vs. the Dec 19 level
- The chart to the right presents the accumulated gains/losses vs. the level in Dec 19, measured in percent of annual sales. Sales in say US were 6% above the pre corona level in July but total sales during the first six months of 2020 were still just 0.3% above the pre corona level, measured in % of annual sales
  - » Level wise through H1, Norway is in the lead, by a wide margin, joined by, Finland, Sweden and Denmark – and Germany
- Consumption of services are not included in these retail sales data – and service consumption has fallen sharply, everywhere

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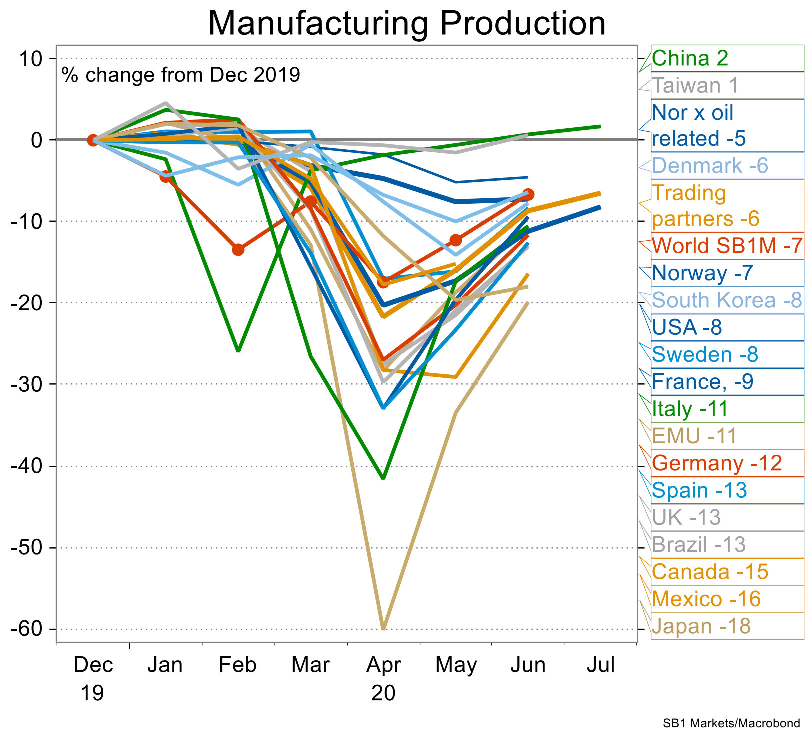
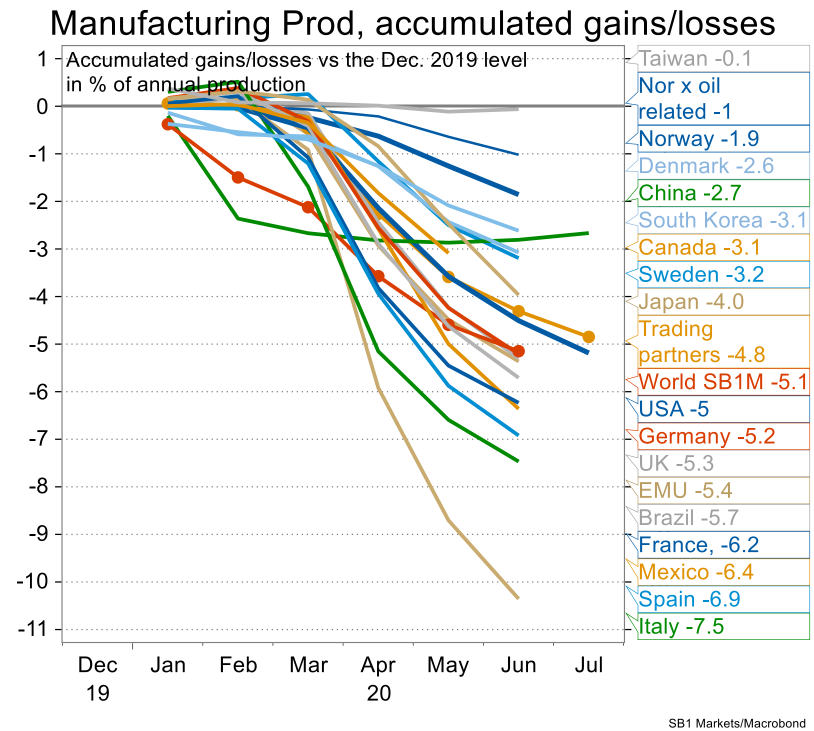
Manufacturing production on the way back, still some 5% of 2020 ‘is lost’

Production probably rose some 6 - 7% in June, and most likely further in July but far slower





- We estimate an almost 7% m/m increase in manufacturing production in June. Production was still down 7% vs. the Dec level
  - » Compared to the Dec 19 level, China is in the lead (above the Dec level) followed by Norway and the US
- The chart to the right presents the accumulated gains/losses vs. the level in Dec 19, measured in percent of annual production. Production in US was 8 below the pre corona level in July but total production during the first 7 months of 2020 was ‘just’ 5% below the pre corona level, <u>measured in % of annual production</u>. *This illustrates the loss of production during the corona crisis, <u>so far</u>*
  - » Taiwan has not reported any decline, while Norway has reported just a small loss (2%), followed by Denmark, China, South Korea (Canada has just reported May data so far, comparison irrelevant))
- <u>Service sector production is not included</u> in these retail sales data – and service consumption has fallen sharply, everywhere

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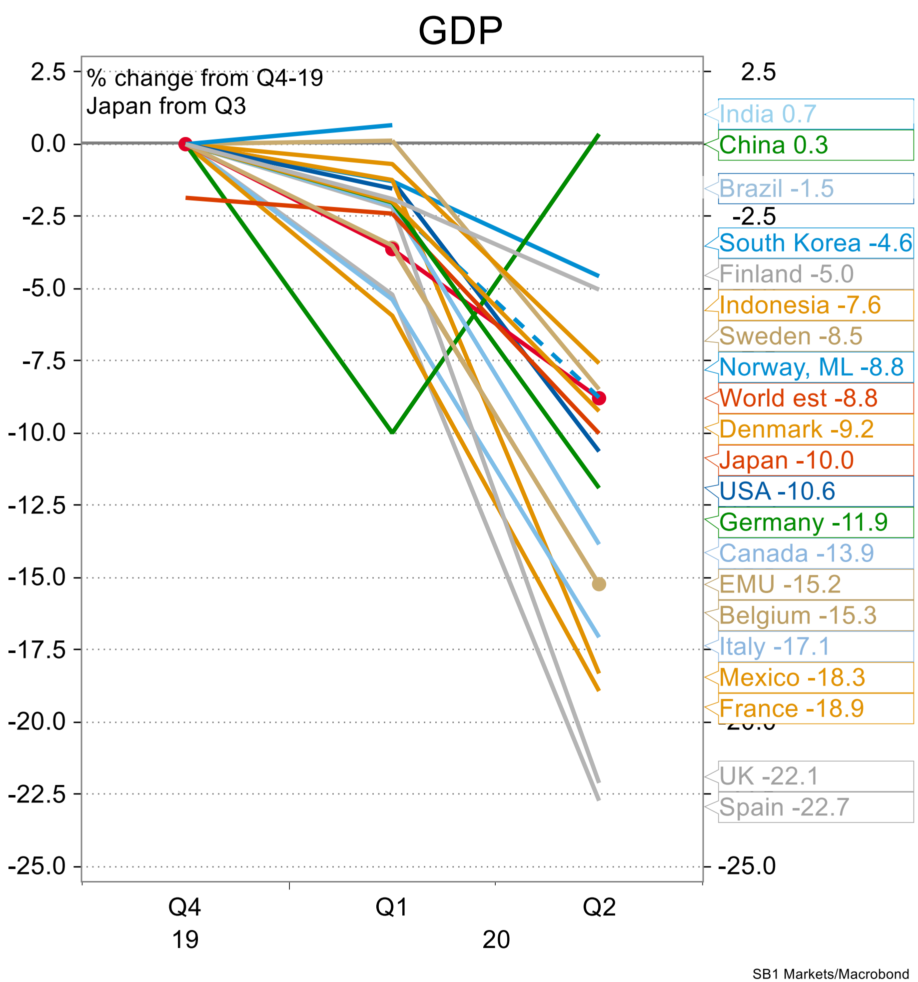
Global GDP down ‘just’ 5% in Q2 but some 12% ex China. Down 9% vs. Q4

Except China, all countries we follow have reported lower GDP. Still mange countries to report

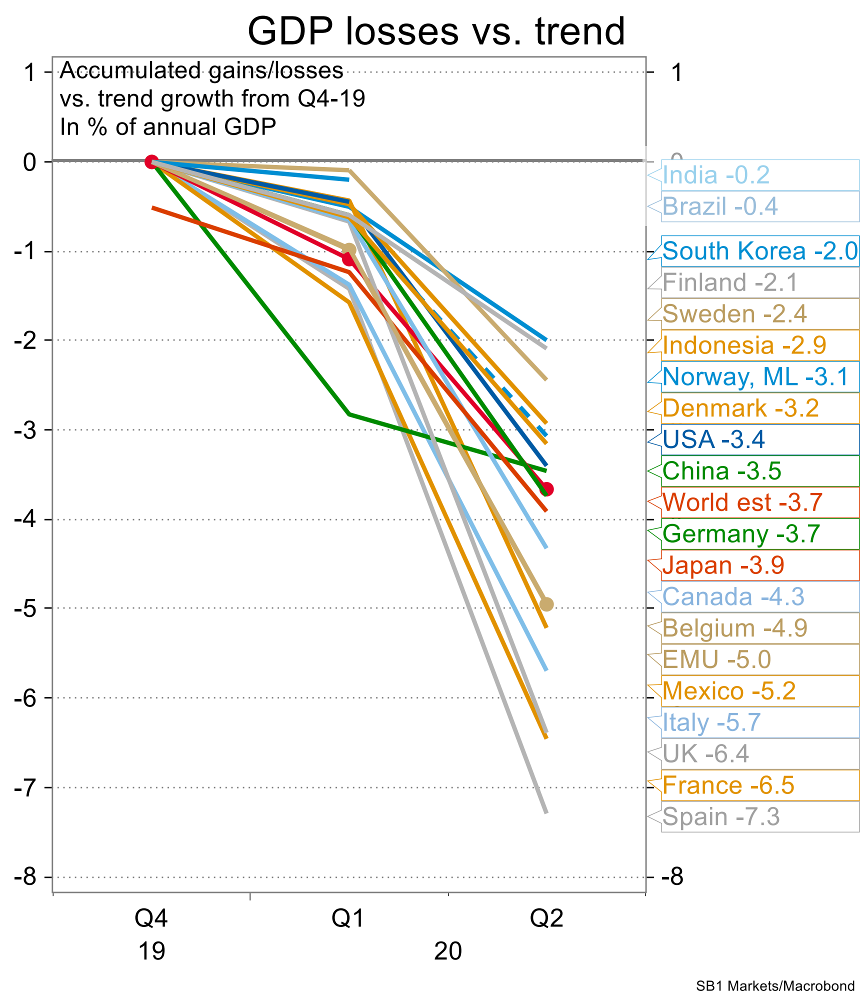


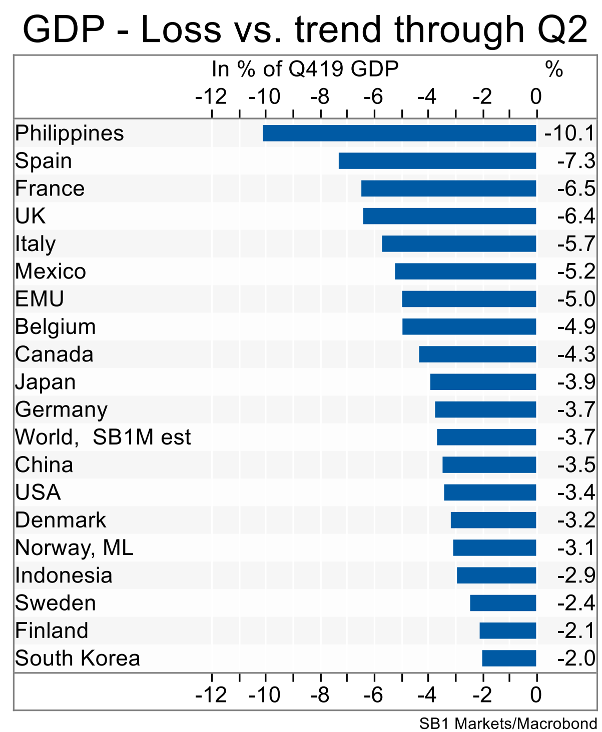
India and Brazil have not yet reported Q2 data! Norway, Japan + the world are our f’casts

- Global GDP declined by 3.7% in Q1, of which almost 2 pp due to China alone
- China has reported a 11.5% growth surge in Q2, bringing the GDP level up to slightly above the Q4 level
- In most (all?) other countries, GDP fell sharply in Q2 – and global GDP probably fell by approx the same amount as in Q1, or a tad faster.
- If so, global GDP has fallen by almost 9 % from the Q4 2019 level, and it was 10% below the pre corona trend path (see chart next page)
- Some countries
  - » China up 11.5% q/q, and is up 0.3% from Q4
  - » US down 9.5% q/q, 10.6% from Q4. Canada down 14% from Q4
  - » EMU down 12% q/q, 15.3% from Q4.
    - Germany down 11% from Q4, Spain -23%
  - » UK down 20.4%, as expected, -22.1% from Q4, just as bad as Spain, the two worst DM countries
  - » Japan down 7.8% in Q2, down 10% vs the Q3 19 level (Q4 was ‘artificially’ weak due to the VAT hike)
  - » South Korea just down 4.6% from Q4
  - » Sweden down 8.6% in Q2, sum 8.5%
  - » Denmark down 7.4% in Q2 following the 2% drop in Q1, sum down 9.2%
  - » Finland down just 3.2% in Q2, 5% through H1
- As production and demand recovered through Q2, we estimate that June was some 4 – 5% below the Q4-19 level
- *Our July global nowcast is for a further expansion in activity, and a 2 – 4% shortfall vs. the pre corona level and 5 – 6% negative output gap (check next page)*

The accumulated losses vs trend growth so far equals 3.7% of global GDP

… and it will grow larger in Q3 as the activity most places will remain far below the pre corona trend

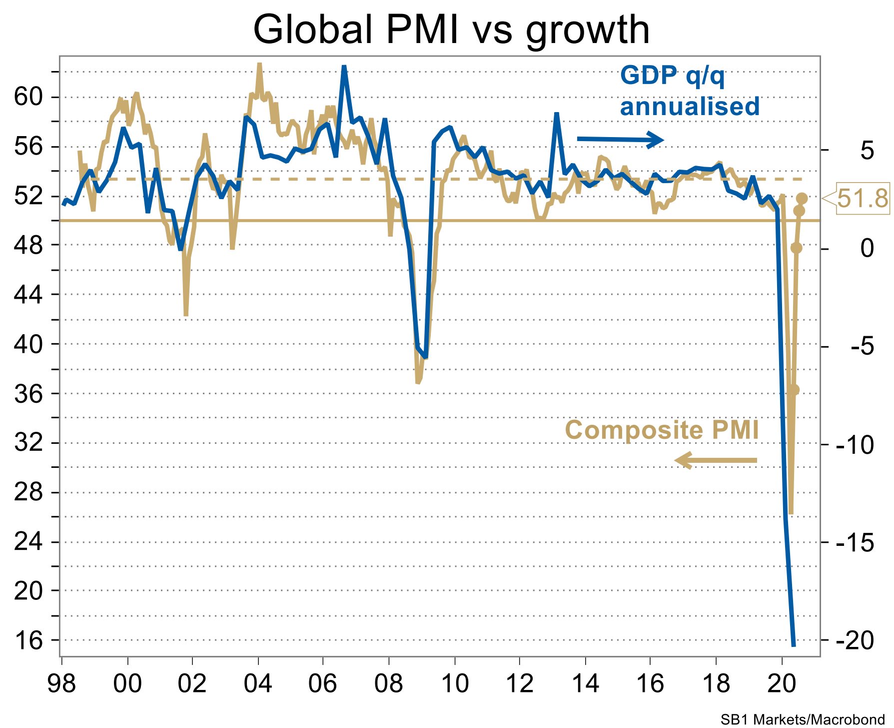


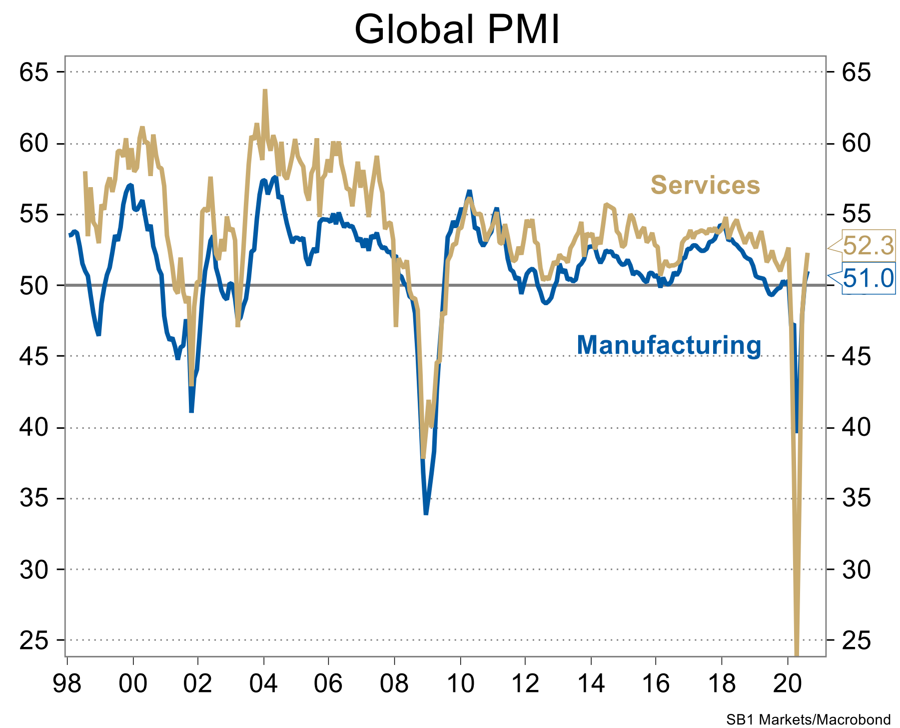


- So far, Sweden has lost less than most other, barring Finland and South Korea
- Spain has reported the largest loss in DM

PMIs further up in August but not in Europe

The global PMI probably rose by 1 p to 51.8 p. Still a low level in the 'sharpest recovery ever'



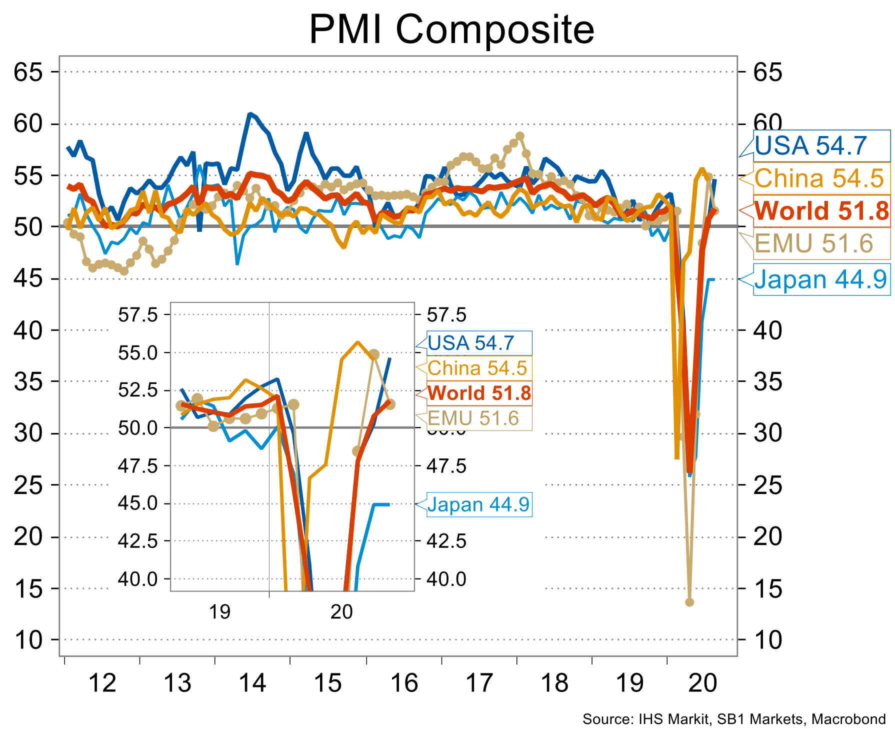


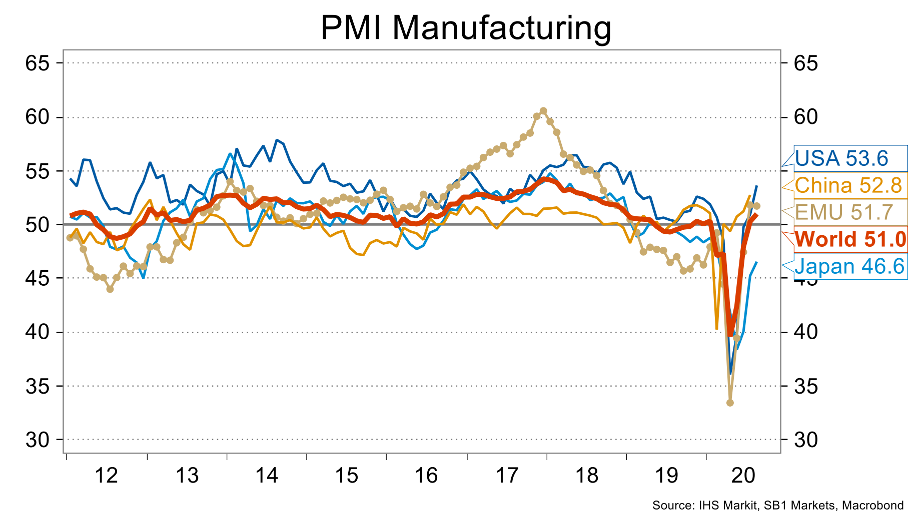
- The PMI respondents are still probably reporting somewhat between growth (which is strong), and the activity level (which is still below par) - and these indices cannot be used to estimate the growth rate – as we usually do
- Both manufacturing and services PMI rose further in August
- The EMU composite PMI surprisingly fell, while the US data set rose sharply – also unexpected – and US took the lead in the race. Japan is still struggling, the composite remained at 44.9, a low level

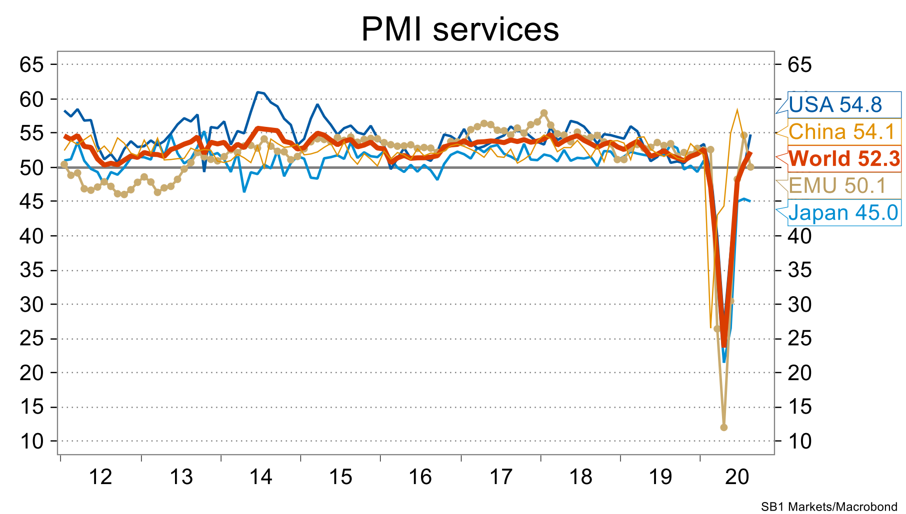
Our estimate is based on the preliminary composite PMIs from EMU, Japan UK, US. The estimate is uncertain

'V's everywhere, the recession was the shortest ever

The EMU PMIs fell sharply, by 3.2 p to 51.6. The US PMI rose by 3.3 p to 54.7!



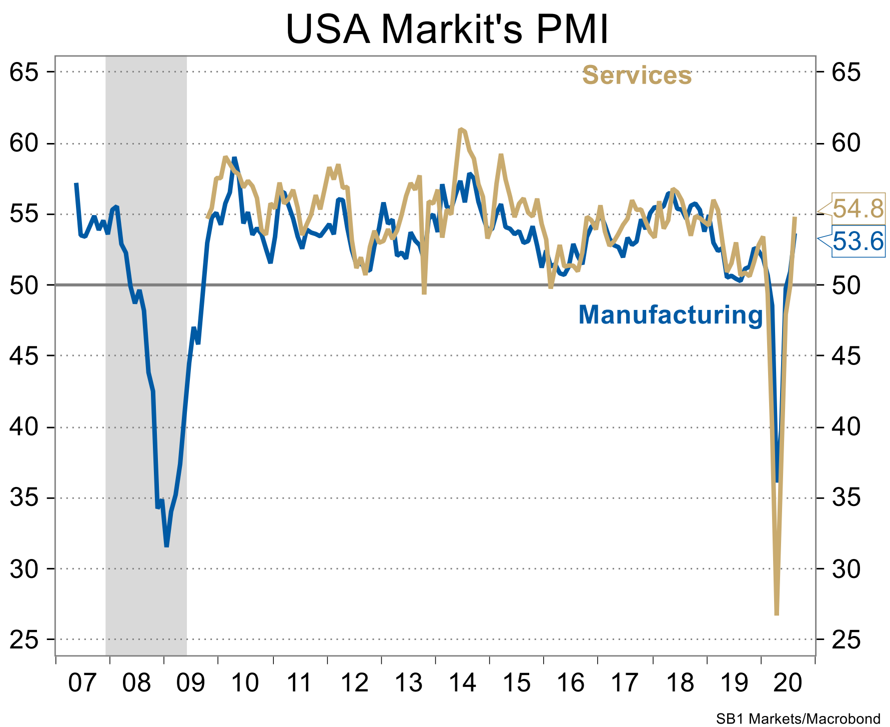


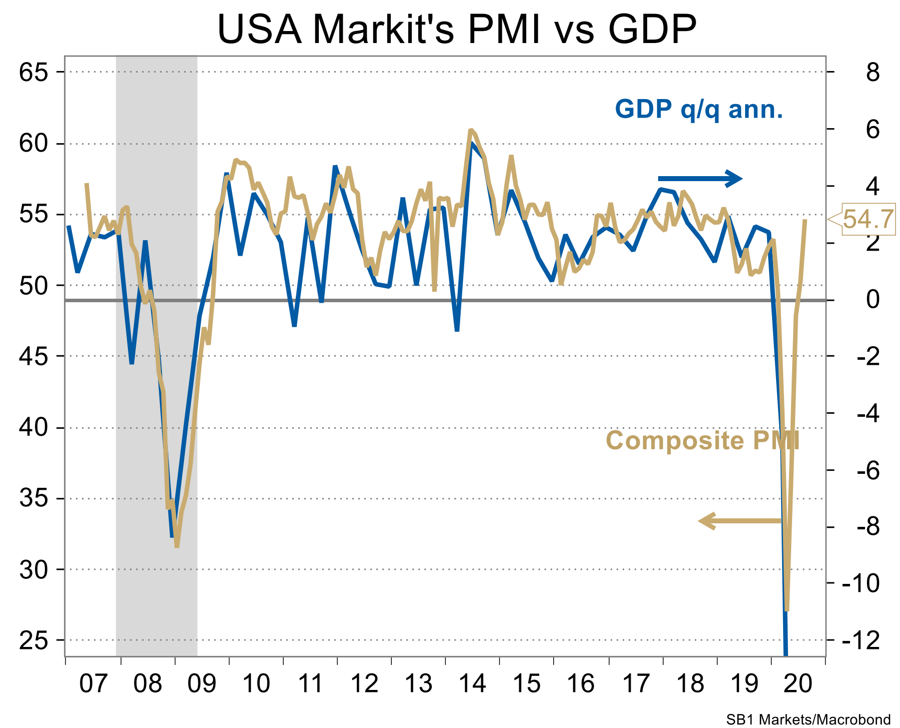


- In the EMU, services was the weak link
- In Japan, both the manufacturing and services are reporting continued decline in activity. However, actual manufacturing production rose in June (but the level was still 18% below the pre corona level)
- The US PMI rose sharply, both manufacturing of services

Markit's PMIs signalling faster growth – not corona setback

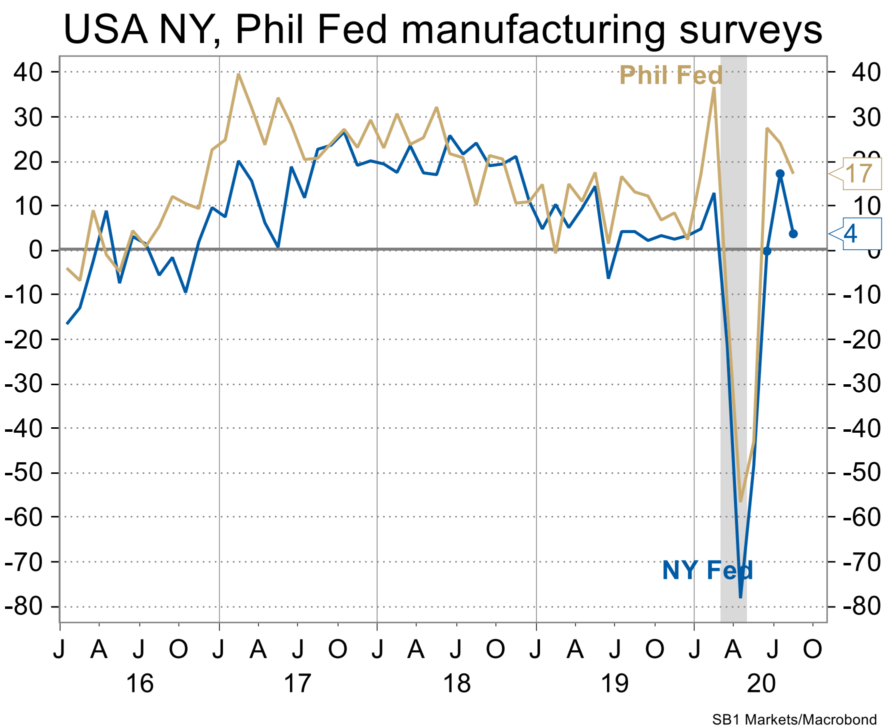
(But in July, the PMIs were on the weak side

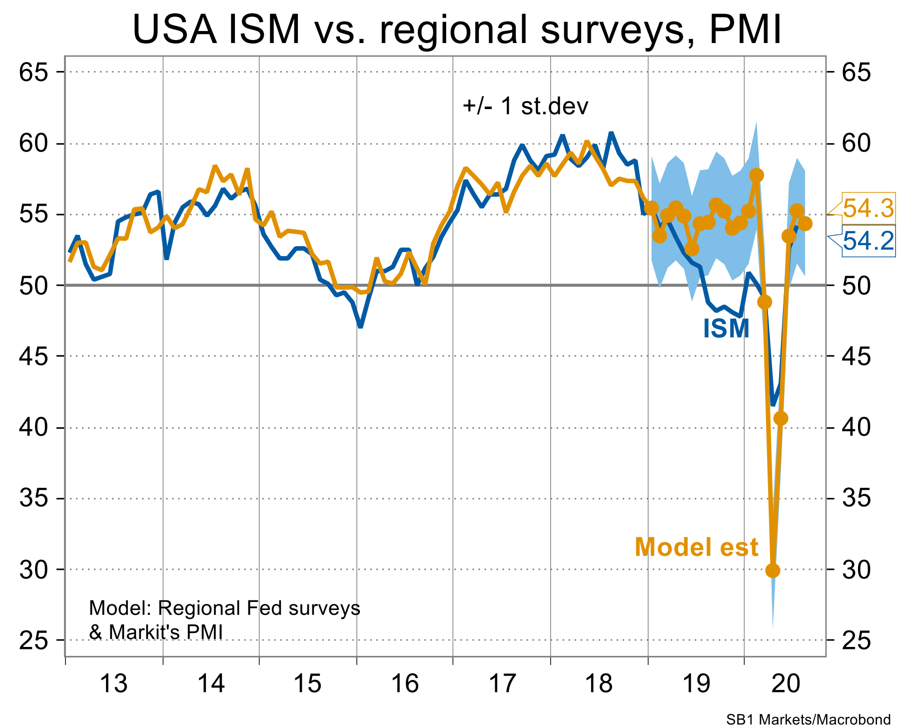




NY & Philadelphia Fed manufacturing indices down in Aug, and more than exp.

Levels are still OK (in average, due to Phil Fed). Suggest, together with Markit's PMI, ISM marg. down





- The surveys have underestimated growth during the first phase of the recovery
- We assumed that companies soon would become better to calibrate their answers to the actual growth rate now. The August surveys signal growth above trend in manufacturing production – but less than needed to close the production gap anytime soon – and less than our forecast for August.

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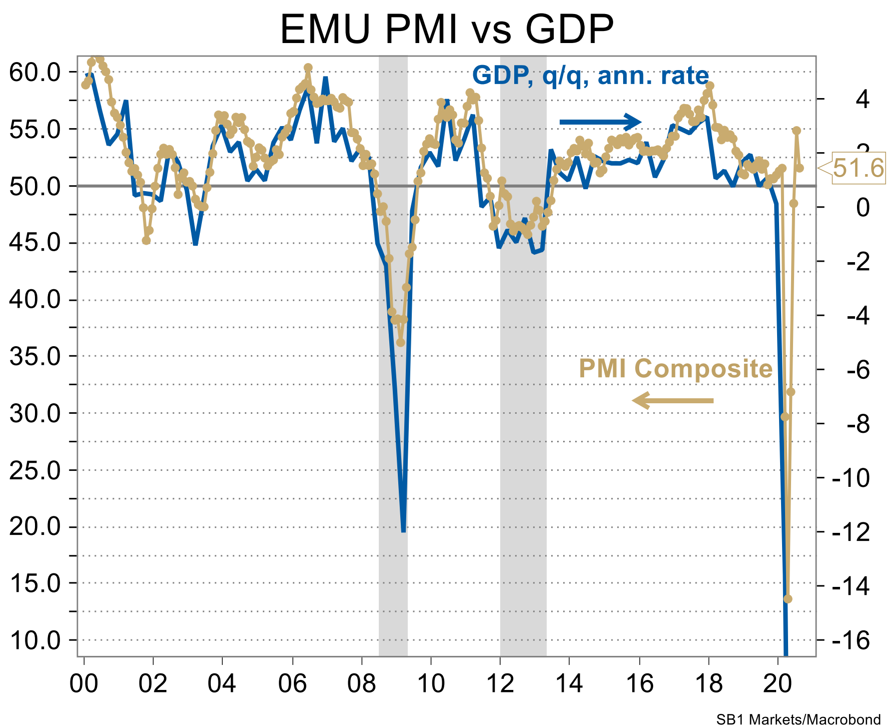
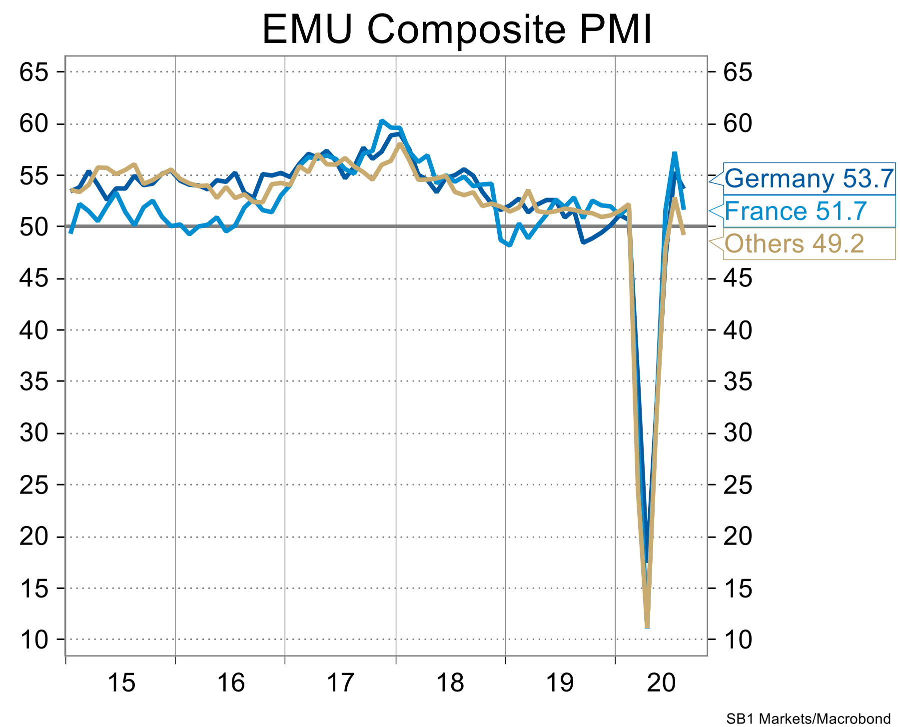
The composite PMI sharply down in August, still above 50

The slowdown was broad geographically. May be a response to the new corona challenges





- The composite PMI is signalling just 1% GDP growth (annualised), close to trend growth. That's way too low, given the low activity level following the 12% decline in GDP in Q2

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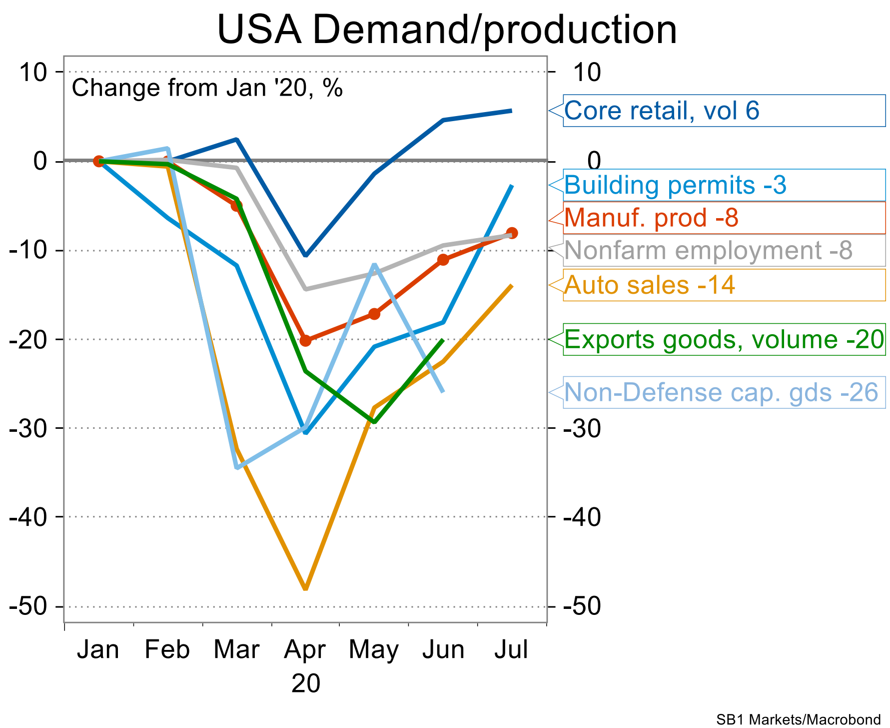
On the way back – but not synchronised yet

Core retail sales well above the pre corona level, building permits close too



Some different shapes and forms of 'V's

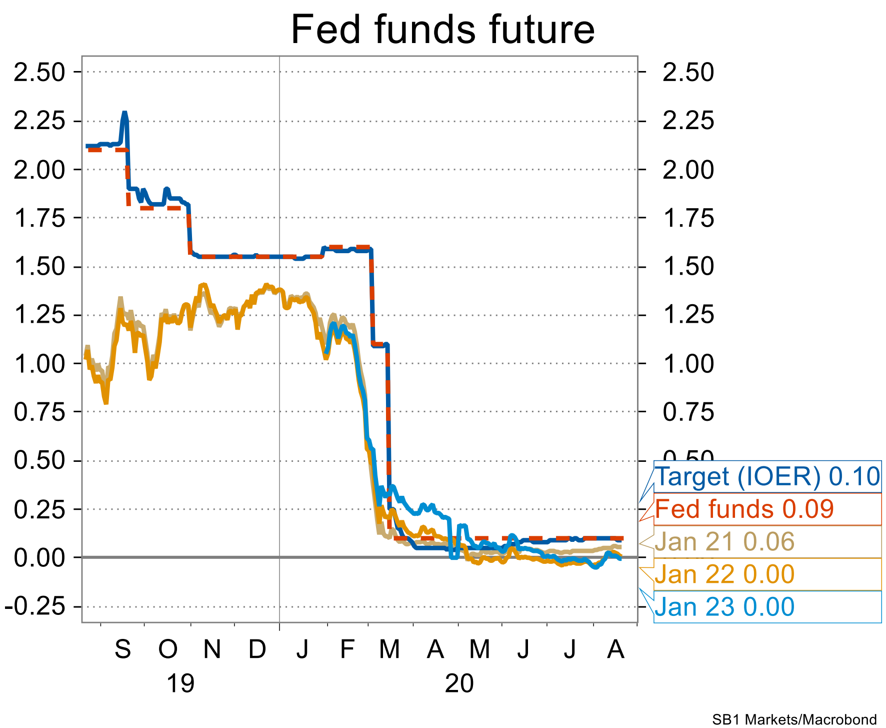
- Export volume still low, as are new investment goods orders (both June data), down 20 – 26%
- Auto sales down 14%
- Employment 8%, and manufacturing production -8%
- Households' goods demand strong, both housing & retail sales

Demand vs production

- Manufacturing production is weaker than household demand for goods. Weaker investment demand, exports and a sharp inventory drawdown explains the difference

FOMC minutes on the dovish side, but not Yield Curve Controal

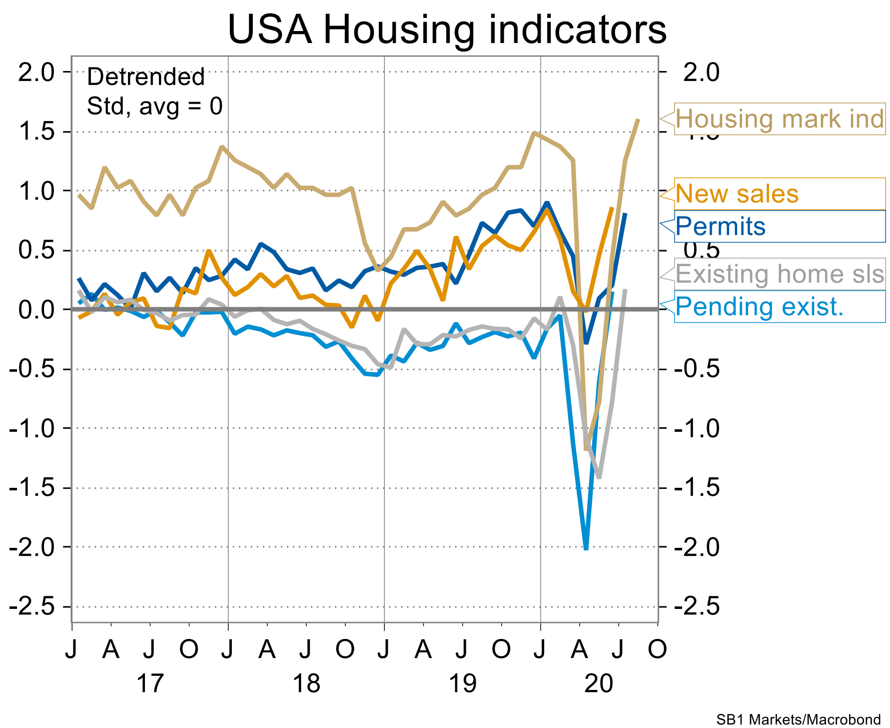
Dovish on the economy, no signals on the new monetary policy strategy – but it's on the table



- The FOMC is still worried growth will surprise on the downside, and begs for more fiscal policy support
- Markets have been focusing at the possibility of a change in the monetary policy strategi – which the bank is working at. At some point, '*a number of FOMC participants noted greater clarity of providing greater clarity regarding the likely path of the target range for the federal funds rate would be appropriate'*
  - » This sentence does not exclude the possibility of introducing a new strategy implying that interest rate will not be lifted before inflation has been above the 2% target for a while, perhaps to reach a 2% average inflation rate over time – or in order to maximise employment. However, it does not signal a shift, and certainly not the timing
  - » In addition: '*Many participants judged that yield caps and targets were not warranted in the current environment but should remain an option'*. No hurry, here either
- Yields fell, even if the comments on YCC were negative. The bank's assessment of the economy may have been more important

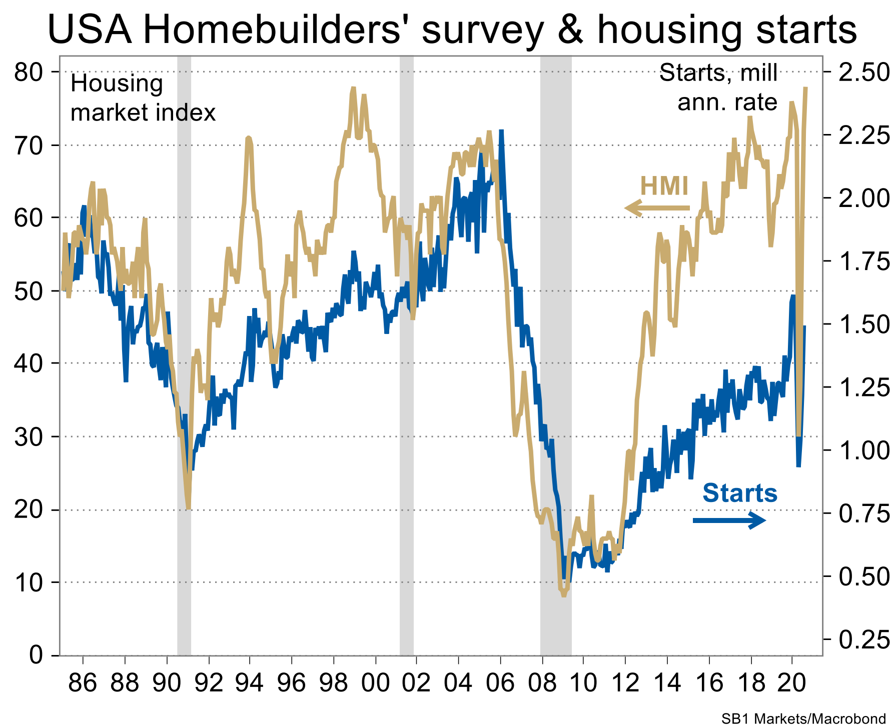
Check the housing market 'V's. It just took 4 – 5 months

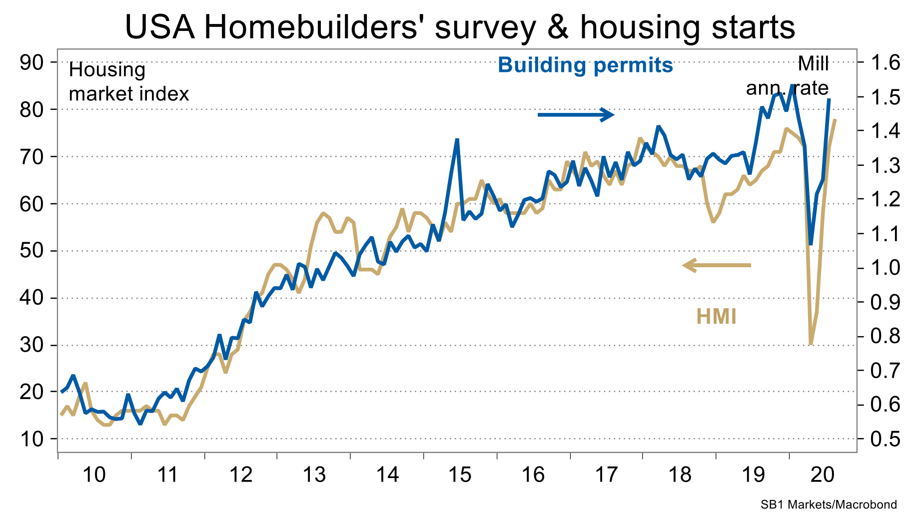
Starts, existing home sales & the housing market index all sharply up, well above expectations



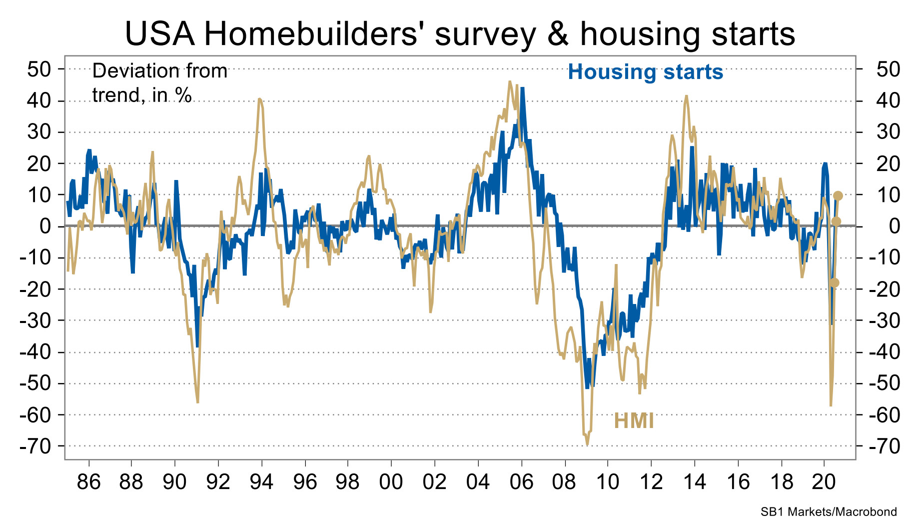
Homebuilders have never before reported stronger activity

The Homebuilders' Market Index surprisingly rose to ATH in august but it does signal more starts



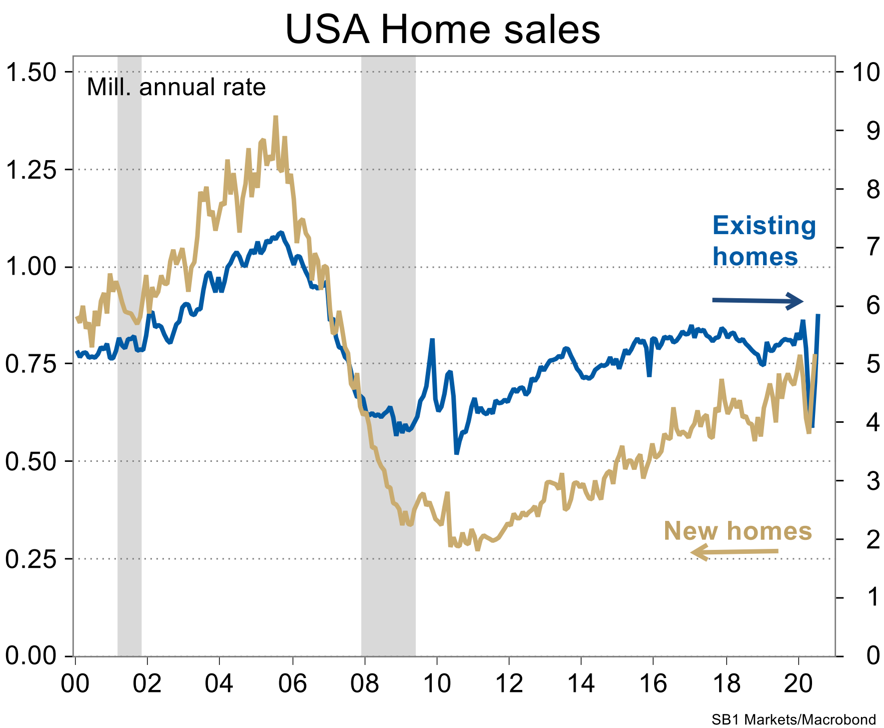


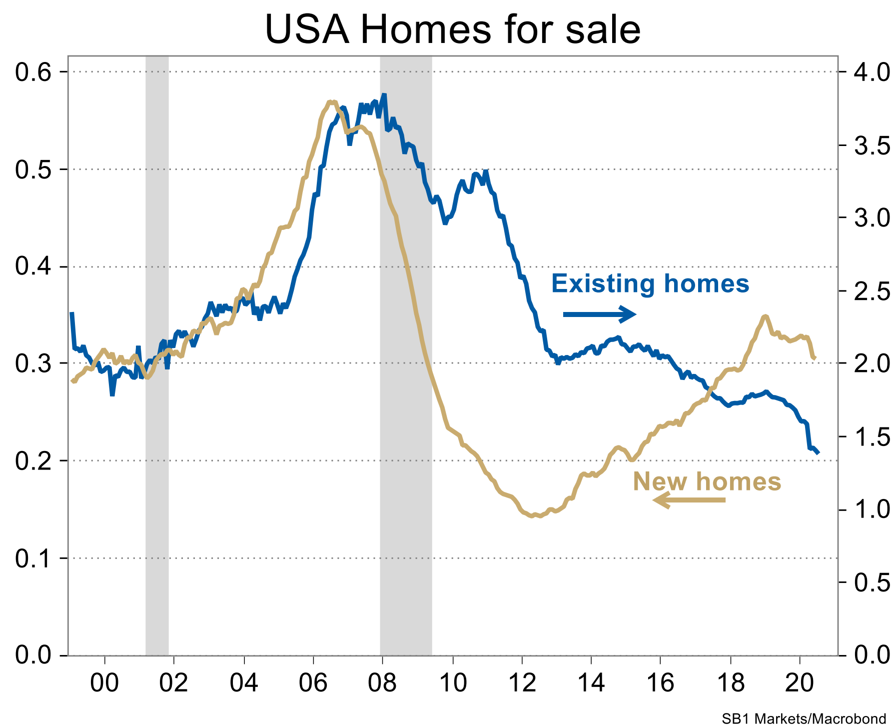
- The index has been at the same level once before, in '98
- The HMI is not an assessment of the 'level' of housing starts vs the long term average but rather deviation of starts from a more flexible trend, check the difference between the chart above and to the right
- The current index signals an unchanged housing starts level vs. starts in July



Existing home shot up in July, highest since 2007!

The number of homes for sale fell further – an the inventory is low





- Existing home sales jumped by 24% m/m in July, up to 5.86 mill – the highest level since 2007
- New home sales rise sharply in May and June
- Home prices rose sharply

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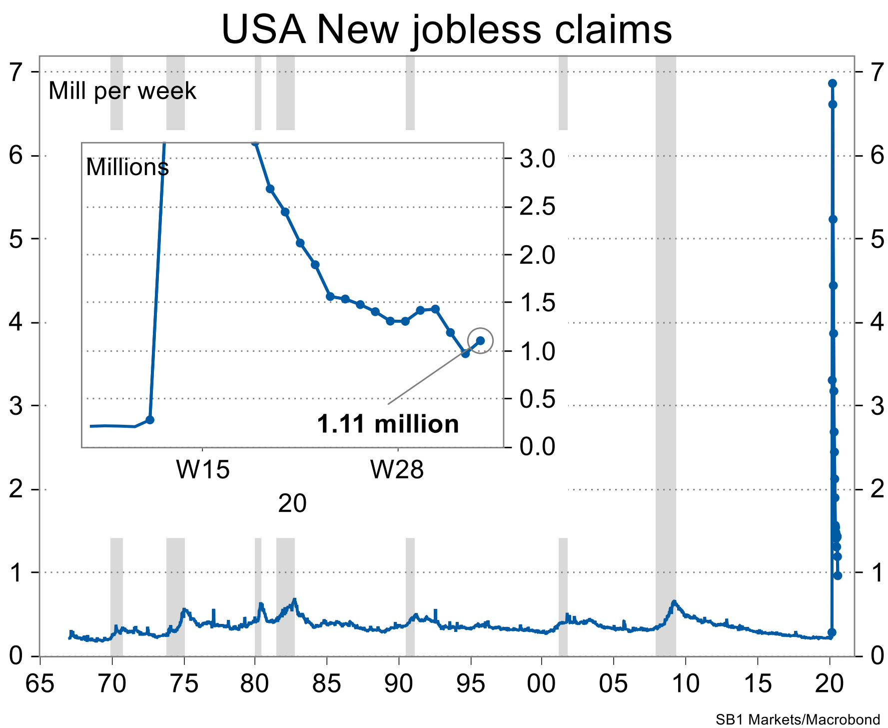
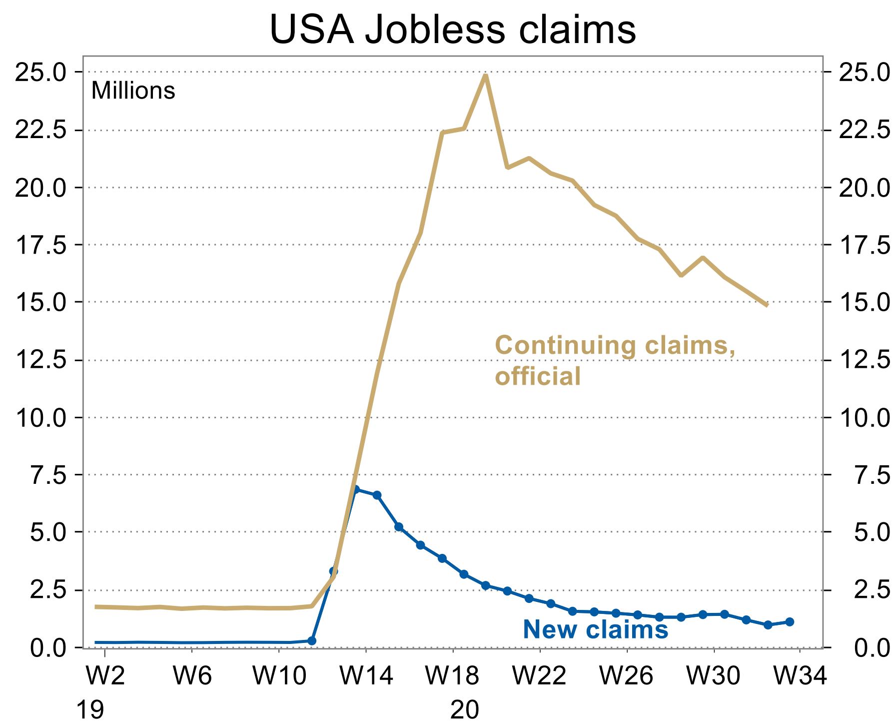
Oops, more new jobless claims again, and the inflow is pretty high

The trend is still down, following the previous two strong weeks. The level is still unusually high

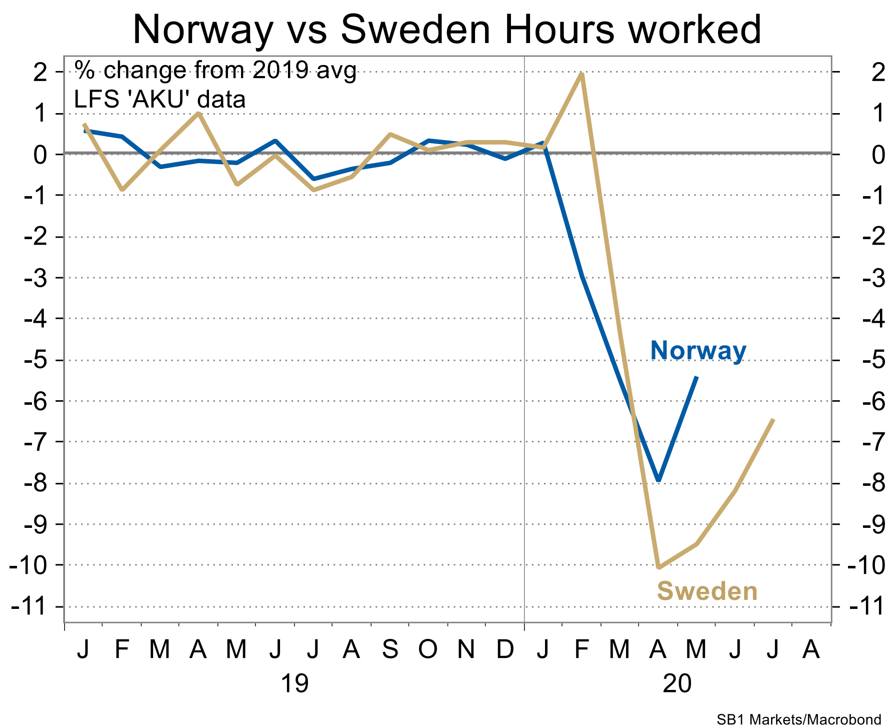


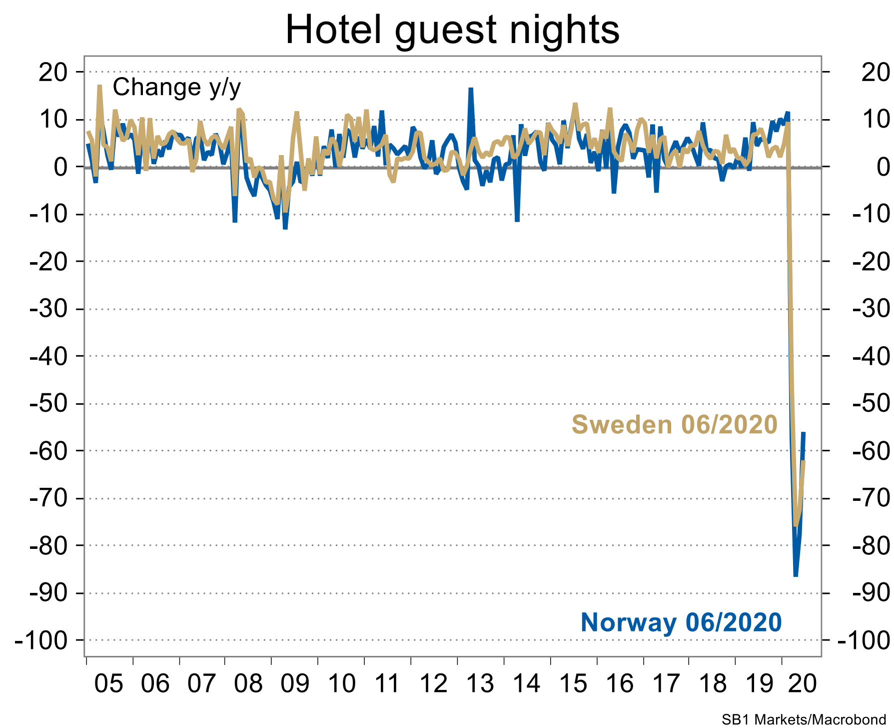


- The inflow is still far higher than during previous recessions now at 0.7%, and amid a rapid increase in employment. This gap illustrates the huge sectoral challenges, some have recovered, others are still struggling and have to reduce their payroll at a rapid pace
- Luckily, more are leaving the dole (for a job or are they leaving the labour market?): Continued claims has fallen to 15 mill from 25 mill.
- Most of the unemployed may now (at least for a while) lose their temporary USD 600/week extra federal unemployment benefit as the states have not been able to match the reduced USD 300/w federal assistance by 100 extra from the local state

Norway vs Sweden: Hours worked more down in Sweden than in Norway

At least according to Labour Force Surveys ('AKU'). National accounts out this week

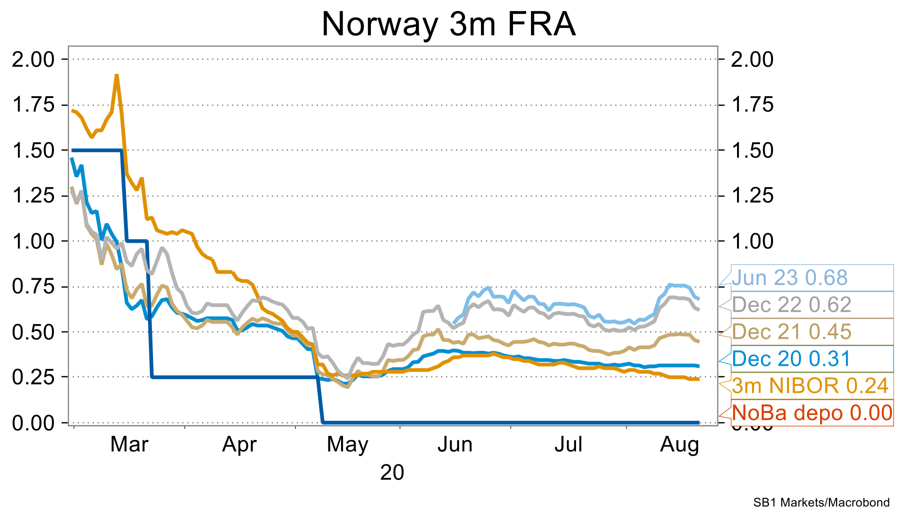


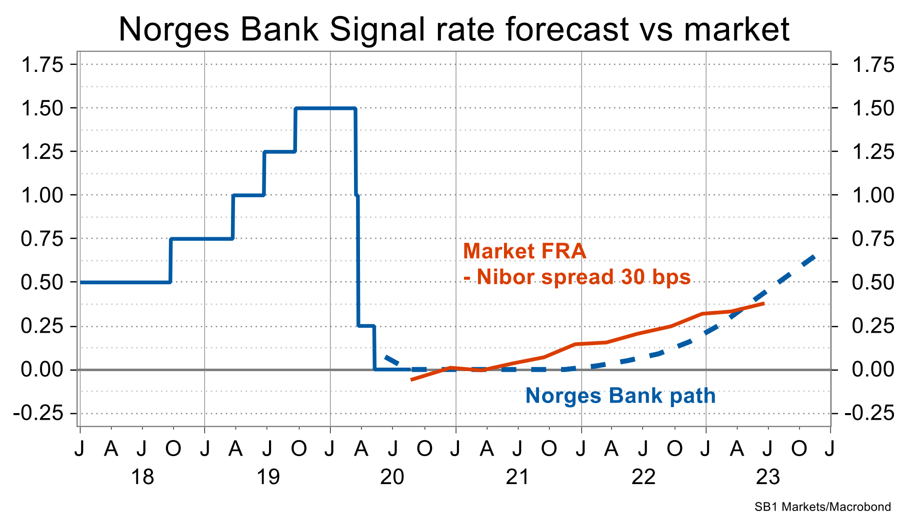


- BTW, not big difference between Norwegian or Swedish hotels – and retail sales have been much stronger in Norway than in Sweden – even without at Swedish 'lockdown' (which though was rather partial in Norway)

Norges Bank: On the dovish side

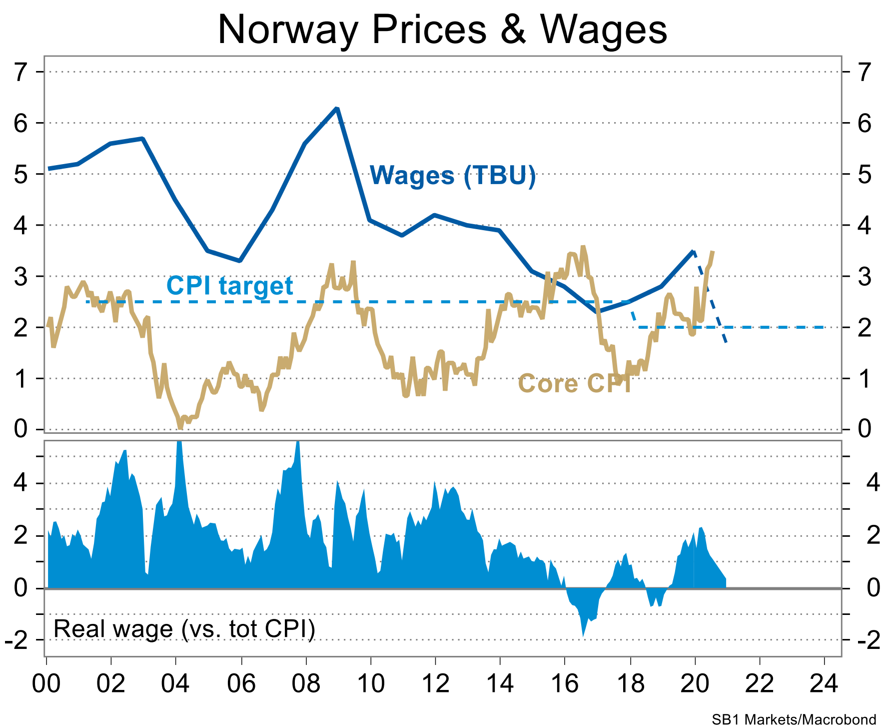
No hints of any upward revision of the interest rate path in the upcoming MPR





- Norges Bank left the signal rate unch. at 0.0%, as everybody expected
- The Bank was rather balanced – and dovish vs. our expectations – in its assessment of the economy and the outlook
  - » *'Both house prices and household credit have increased more than expected'*
  - » However, *'economic activity overall appears to have picked up broadly as projected'*
  - » And '*Labour market developments appear to have been somewhat weaker than expected'*
  - » The bank expects inflation to slow due to low wage growth and a stronger NOK
  - » The Bank focuses on the considerable uncertainty vs the economic outlook, also due to the newly increased spread of Covid-19 and reintroduced restrictions
- In sum, no hints of a further lift in the interest rate path in September. Still, we judge the risk to be on the upside, barring substantial corona problems abroad or back home
- FRA rates dropped some few bps on the announcement

No strike, of course. 1.7% wage inflation agreed upon



- At Friday, the first round of this year's (postponed) spring wage negotiations was finalised, after 22 hours extra mandatory mediation
- A 1.7% wage lift in 2020 was agreed upon, of which 1.2 pp is due to carry-over from wage increases during 2019
  - » The employer's offered these 1.2% (and nothing more), we expected an outcome closer to 2%
  - » Included in the sum, a substantial increase in minimum wages, we estimate some 5%!
  - » Other trade unions/employers associations are now entering the play. We expect the same 1.7% +/- some very few tenths (1 – 2) to become the norm for the deals to be concluded the coming weeks, including the public sector
- A 1.4% 2020 CPI inflation is expected, far below the present core rate (3.5%). Electricity prices have fallen sharply, and the 1.4% is not impossible to reach. If so, real wages will increase by 0.3% in 2020
- Norges Bank expected a 1.9% wage inflation in 2020. The estimate may not be changed in the upcoming monetary policy report if not for a change in the mix of the employed that will increase the average wage level – as more lower paid than higher paid employees have lost their jobs

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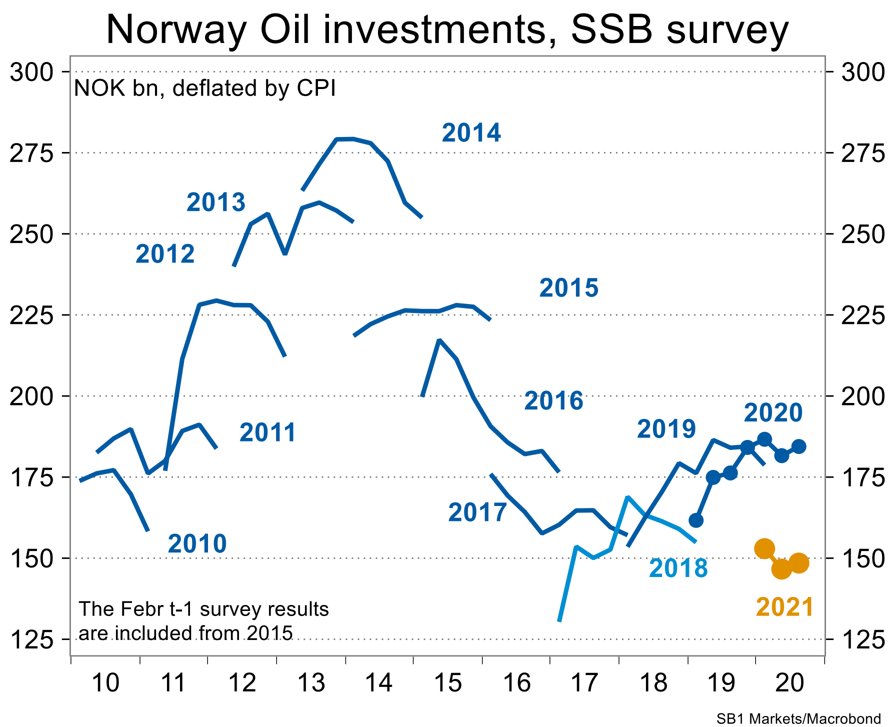
A doubling of the oil price, and a substantial tax cut did not alter that much

Just small revisions of investment estimates – a 12% decline is signalled <u>through</u> 2020 and ‘21



- In SSB’s Q3 oil & gas investment survey, companies adjusted their **2020 investment f’cast** up by NOK 4 bn to 184 bn, following the NOK 5 bn cut in the Q2 forecast. The recent estimate is 2% above the equivalent 2019 f’cast. We expect a 1% decrease in volume terms (up from our -6% May forecast) when books are closed). Norges
  - » <u>As investments grew fast through 2019, a 1% decline implies a sharp reduction through 2020, by some 10%</u>
- **The 2021 estimate was revised up by** NOK 3 bn to 149 bn. The estimate is 15% below the equivalent 2020 estimate one year ago, vs -16% in the Q2 survey. The upward revision was smaller than average to Q3 from Q2.
  - » We estimate a 13% decline in volume terms in 2021 (vs -17% in May). Norges Bank expected a 10% decline in the June MPR. Our estimate implies a decline in investments by some 15% through 2021
  - » We are uncertain how many project will be added even if the tax regime is changed. However, the recent doubling of the oil price could turn out to be more important
- **Oil companies have not changed their forecast materially from before corona**. As Johan Sverdrup was finished, a substantial decline in investments was signalled long time ago. We have now entered a new downward cycle in the oil industry

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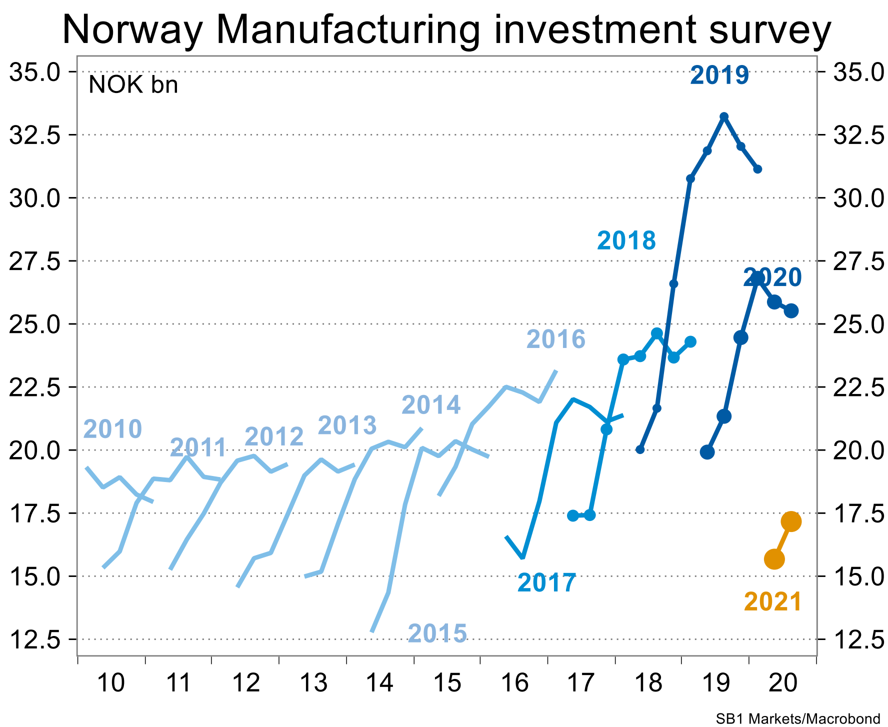
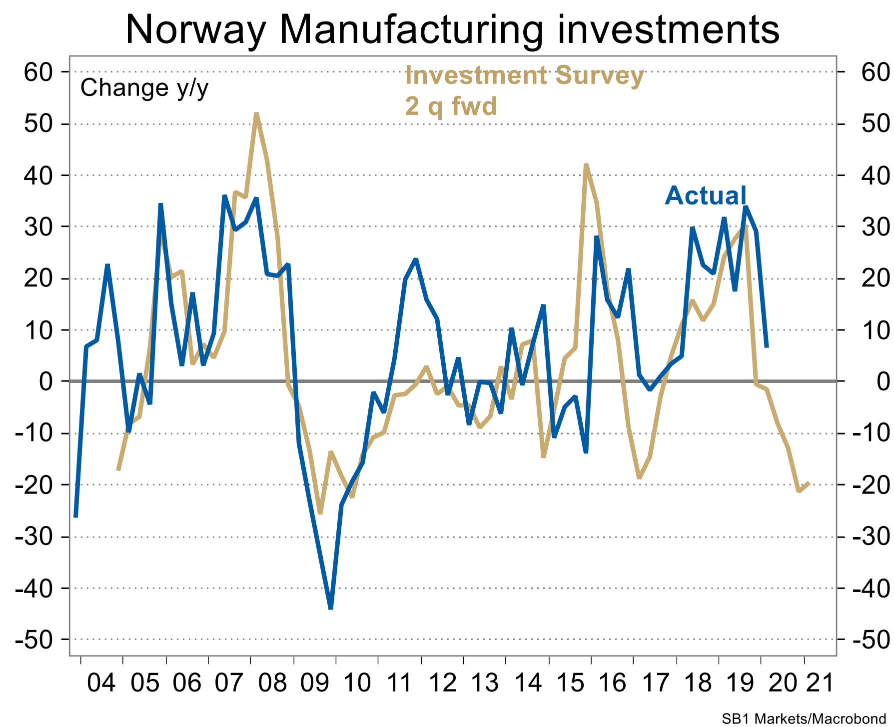
Manufacturing investments down 20% in 2020, another 15 - 20% in 2021

2019 investments were far above a normal level, 2021 will probably be below

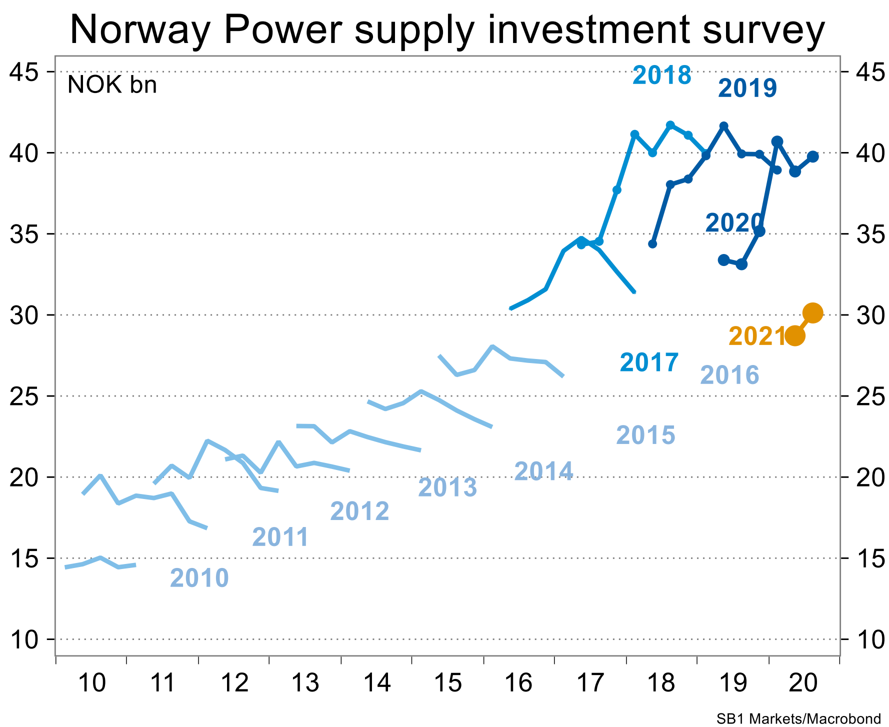


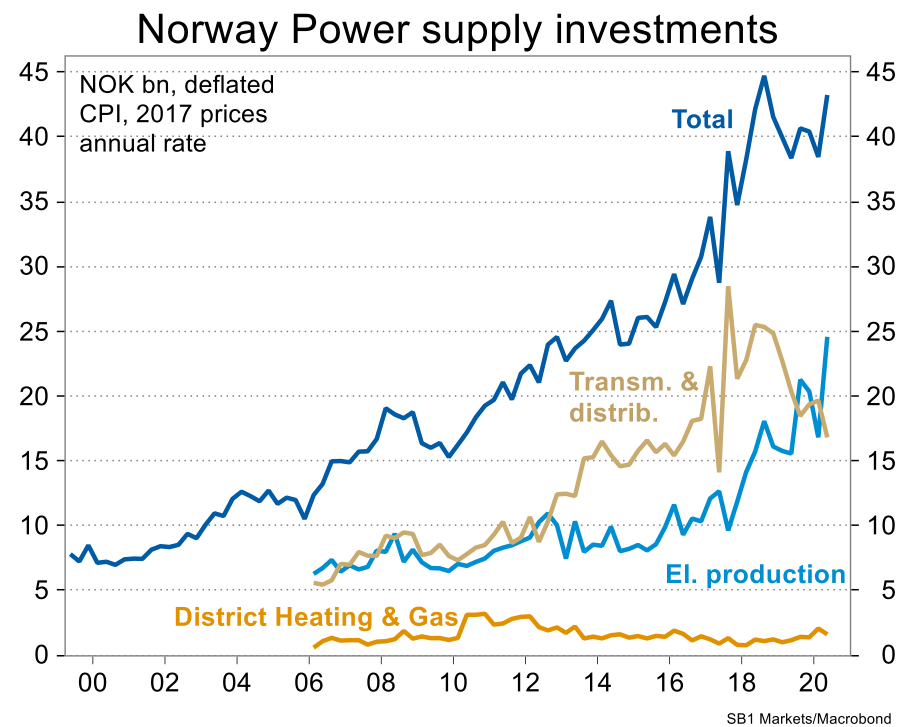


- Manufacturing companies adjusted their 2020 investment marginally down in Q3, and the estimate is now 20% below the equivalent 2019 estimate from Q3 last year. The 2020 downturn was signalled before corona
- The second 2021 estimate implies another 15 – 20 % decline, but the uncertainty is of course larger than for the 2020 estimate
  - » Investments in refined petro., chemicals and metals are the major drags in 2020, after soaring in 2019

Power supply: Investments are peaking now

The 2020 estimate was better than we assumed but the 2021 decline is confirmed – down 10%?

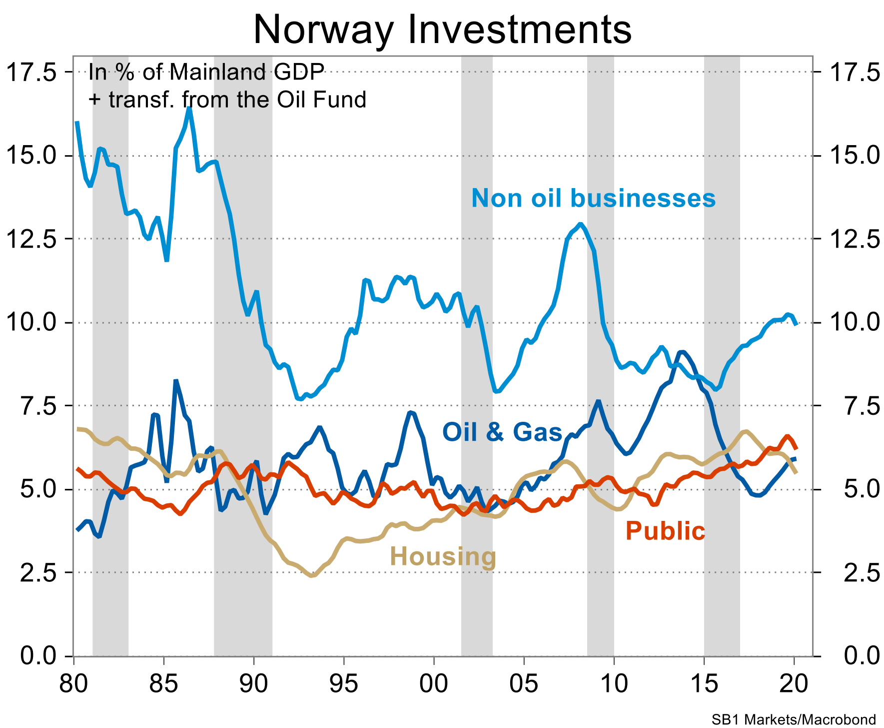




- Power supply (production & distribution) companies revised their 2020 investment f'cast map marginally in Q3, at a time of the year where investments normally are revised down. The 2020 estimate is now on par with the equivalent 2019 estimate, at NOK 40 bp, up from -7% in the May forecasts
- The second 2021 estimate is down 9% vs. the equivalent 2020 estimate, up from -14% in May. More projects may be added the coming quarters but a significant decline vs. 2020 is no very likely
- Investments have more than quadrupled in 25 years, more than 10% p.a in average. The investment level as % of Mainland GDP has been running at or just above 1%, the highest in decades. Investments in transmission and distribution has fallen the most

The investment cycles: A broad slowdown the coming quarters?

Business investments – on and offshore – peaked in Q4 – and will decline substantially



- **Oil investments** recovered until the peak in Q4 2019 – and is now heading down
- **Mainland businesses** have increased their investments sharply since '16. Investments peaked in Q4 19. the level is not low anymore. They are probably at peak, too, as manufacturing and power supply investments are set to decline, and the upside on service investments is probably limited
- **Government investments** are the highest in decades, vs GDP. Will come down long term, but limited downside short term
- **Housing investments** have been sliding down since 2017 but remains at a rather high level, at least vs a 40 year history

The Calendar

Time	Cour	Indicator	Period	Forecast	Prior
Monday August 24					
14:30	US	Chicago Fed Nat Activity Index	Jul	3.69	4.11
Tuesday August 25					
08:00	NO	GDP Mainland QoQ	2Q	-6.3%(-6.6)	-2.1%
08:00	NO	GDP QoQ	2Q	(5.4%)	-1.5%
08:00	NO	GDP Mainland (MoM)	Jun	3.9% (3.5)	2.4%
08:00	NO	GDP (MoM)	Jun	(2.6)	1.9%
10:00	GE	IFO Expectations	Aug	98.1	97
15:00	US	S&P CoreLogic CS 20-City MoM SA	Jun	0.10%	0.04%
16:00	US	Conf. Board Consumer Confidence	Aug	93	92.6
16:00	US	New Home Sales	Jul	776k	776k
Wednesday August 26					
08:00	NO	Unemployment Rate AKU	Jun	4.8% (4.9)	4.6%
14:30	US	Durable Goods Orders	Jul P	4.3%	7.6%
14:30	US	Cap Goods Orders Nondef Ex Air	Jul P	1.6%	3.4%
Thursday August 27					
06:30	JN	All Industry Activity Index MoM	Jun	6.3%	-3.5%
08:00	NO	Retail Sales MoM	Jul	0.6% (0)	5.7%
09:00	SW	Economic Tendency Survey	Aug		83.4
09:00	SW	Consumer Confidence	Aug		83.3
09:30	SW	Retail Sales MoM	Jul	1.0%	1.0%
14:30	US	GDP Annualized QoQ	2Q S	-32.5%	-32.9%
14:30	US	Initial Jobless Claims	Aug-22	1000k	1106k
16:00	US	Pending Home Sales MoM	Jul	2.0%	16.6%
Friday August 28					
	GE	Retail Sales MoM	Jul	1.3%	-1.6%
08:45	FR	Consumer Spending MoM	Jul	1.2%	9.0%
09:30	SW	GDP QoQ	2Q	-8.6%	0.1%
10:00	NO	Unemployment Rate, NAV	Aug	4.7%	4.9%
11:00	EC	Economic Confidence	Aug	85	82.3
14:30	US	Personal Income	Jul	-0.3%	-1.1%
14:30	US	Personal Spending	Jul	1.5%	5.6%
14:30	US	PCE Core Deflator YoY	Jul	1.2%	0.9%
14:30	US	Advance Goods Trade Balance	Jul	-$72.2b	-$70.6b
Monday August 31					
01:30	JN	Industrial Production MoM	Jul P		1.9%
01:30	JN	Retail Sales MoM	Jul		13.1%
03:00	CH	Manufacturing PMI	Aug	51.1	51.1

- **USA**
  - » **Revised Q2 GDP** data (with more details), July **personal income & spending** should confirm the Q2 setback, and that the gradual recovery is underway. **New durable orders** have been mixed, as airline orders as well as investment orders have been on the weak side. Housing data are all strong, **new home sales** out now. During the coming week-end, the world's monetary policy high flyers will gather in **Jackson Hole**. Some testing balloons have be been released here through the times, and monetary policy is more debated than ever (if not as much as fiscal policy)
- **EMU**
  - » More July **business surveys** (like the German Ifo, + EU surveys), and **July retail** sales will probably confirm the recovery but also that growth may have slowed in August, as the PMIs signalled last week
- **Sweden**
  - » **GDP** fell by 8.4% in Q2, according to a preliminary index. A revision + details out this week. Retail sales have been slower than in most other rich countries, July data are not expected much better
- **Norway**
  - » **Q2 GDP** is reported at 8:00 this morning. We expect a 6.6% Q2 decline. Both **LFS and NAV** are reporting **unemployment** data, we expect a higher LFS unemployment rate (more furloughed included) but a lower NAV headcount (the real unemployment is still falling). We expect flat **retail sales** vs. the very strong June number, but a 3 – 5% increase due to more holiday shopping in Norway would not be a shock either.

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

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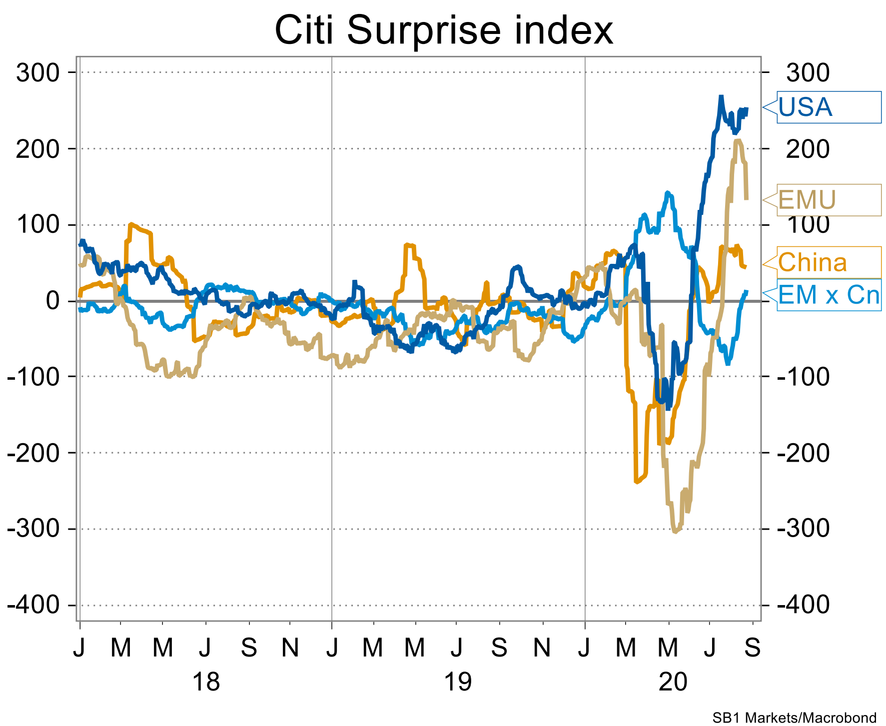
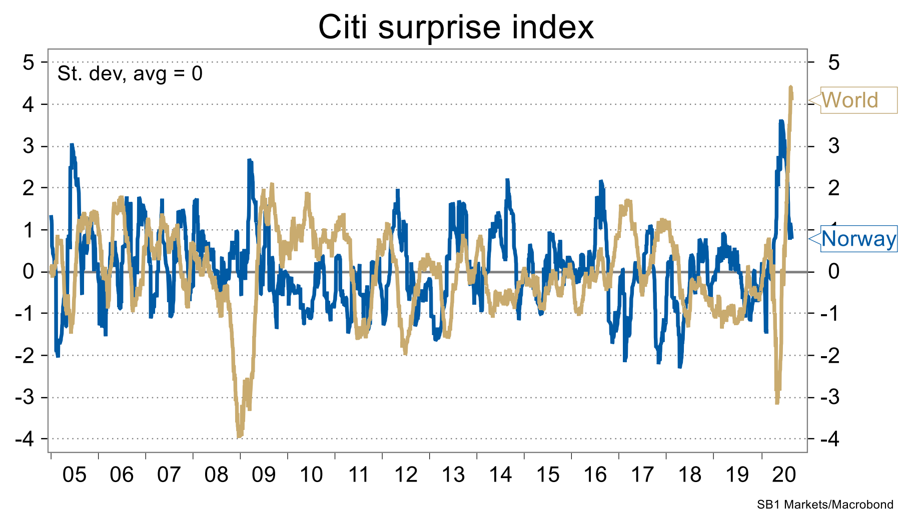
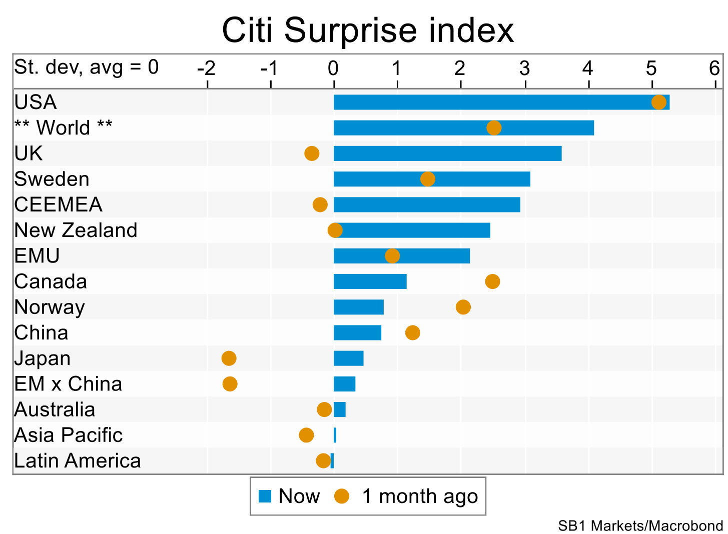
Macro data are surprising on the upside in DM, big time

Both US and the EMU – as well as China is surprising on the upside. The global surprise record high





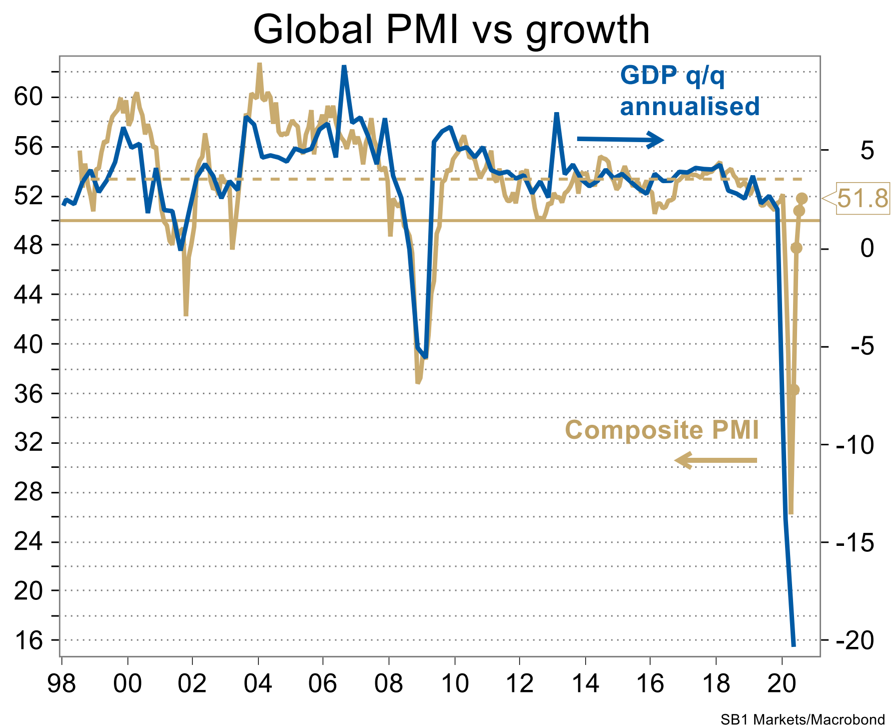


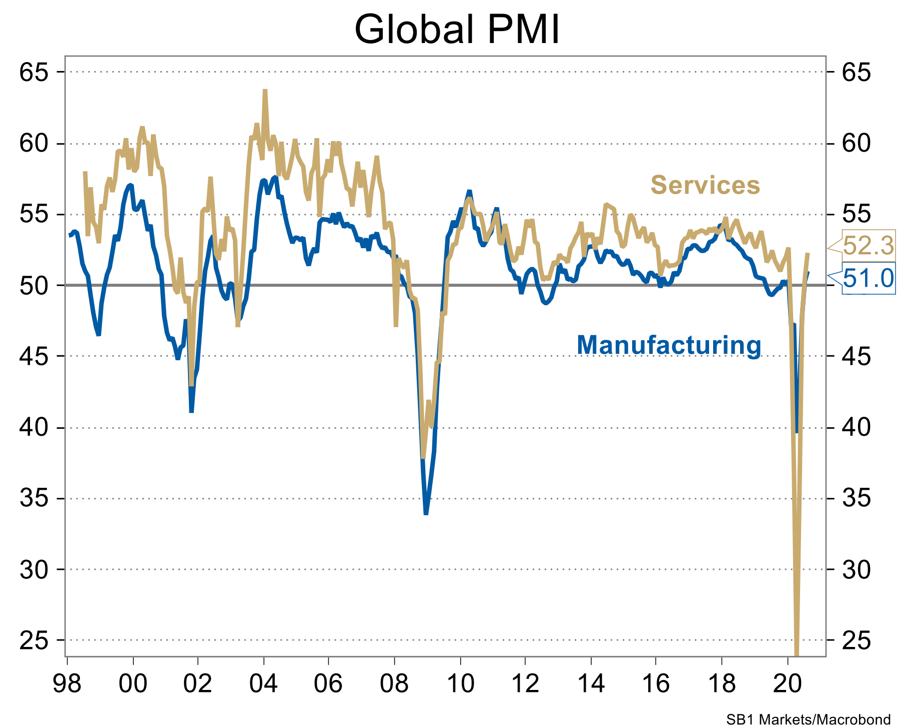
- Both the US is still surprising more on the upside than ever before (data from 2003). The weak PMIs contributed to a decline in the surprise index last week
- China in well into positive territory too
- Other EMs have been reporting weaker data than expected, now back to normal
- Norway has been surprising on the upside too – big time – but less so past three weeks

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

PMIs further up in August but not in Europe

The global PMI probably rose by 1 p to 51.8 p. Still a low level in the ‘sharpest recovery ever’



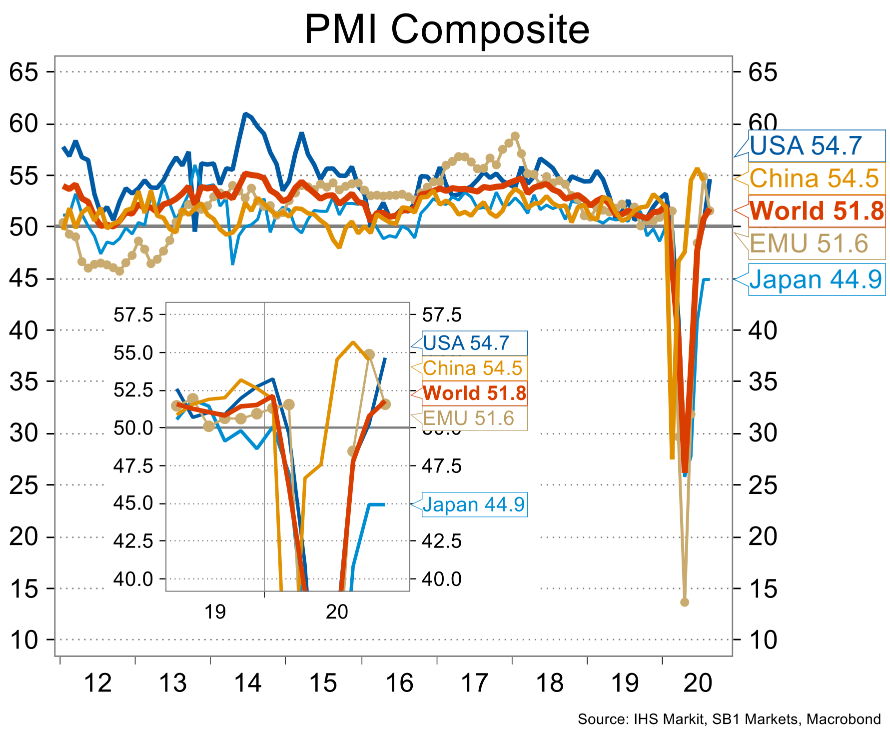


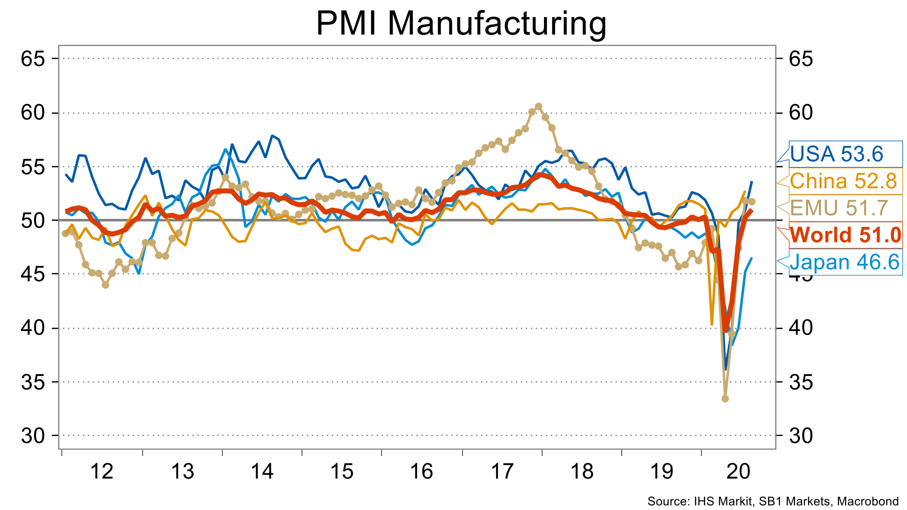
- The PMI respondents are still probably reporting somewhat between growth (which is strong), and the activity level (which is still below par) - and these indices cannot be used to estimate the growth rate – as we usually do
- Both manufacturing and services PMI rose further in August
- The EMU composite PMI surprisingly fell, while the US data set rose sharply – also unexpected – and US took the lead in the race. Japan is still struggling, the composite remained at 44.9, a low level

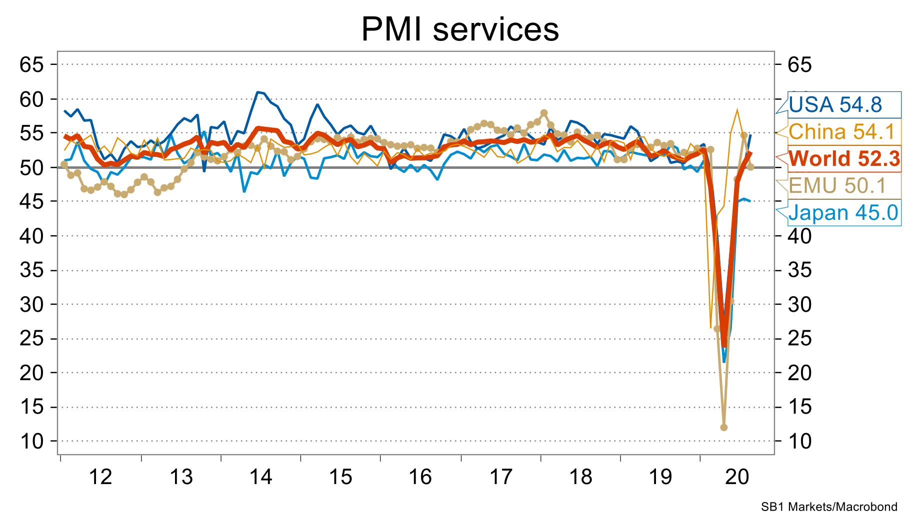
Our estimate is based on the preliminary composite PMIs from EMU, Japan UK, US. The estimate is uncertain

'V's everywhere, the recession was the shortest ever

The EMU PMIs fell sharply, by 3.2 p to 51.6. The US PMI rose by 3.3 p to 54.7!







- In the EMU, services was the weak link
- In Japan, both the manufacturing and services are reporting continued decline in activity. However, actual manufacturing production rose in June (but the level was still 18% below the pre corona level)
- The US PMI rose sharply, both manufacturing of services

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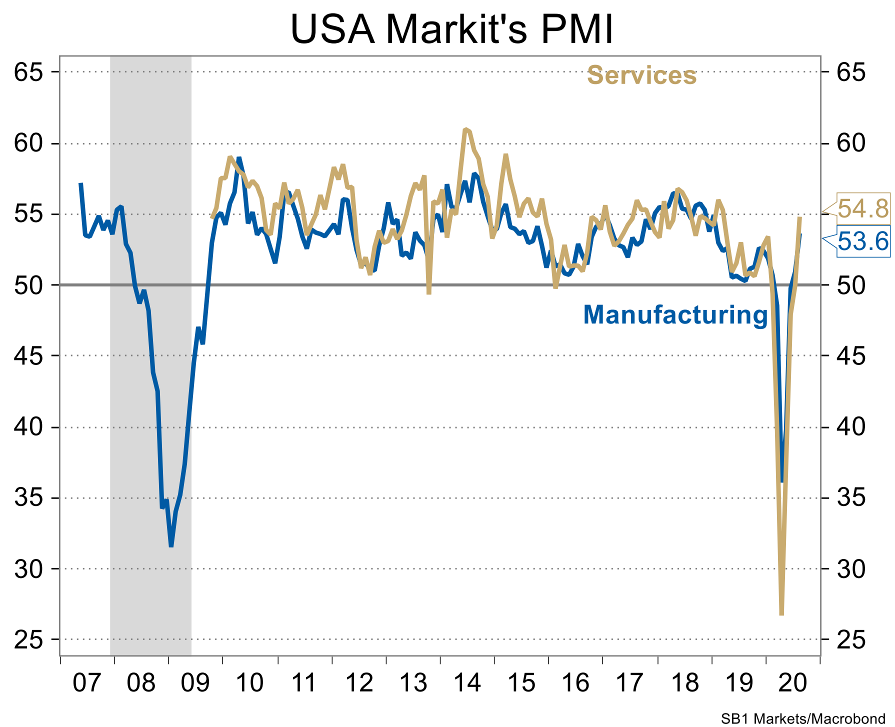
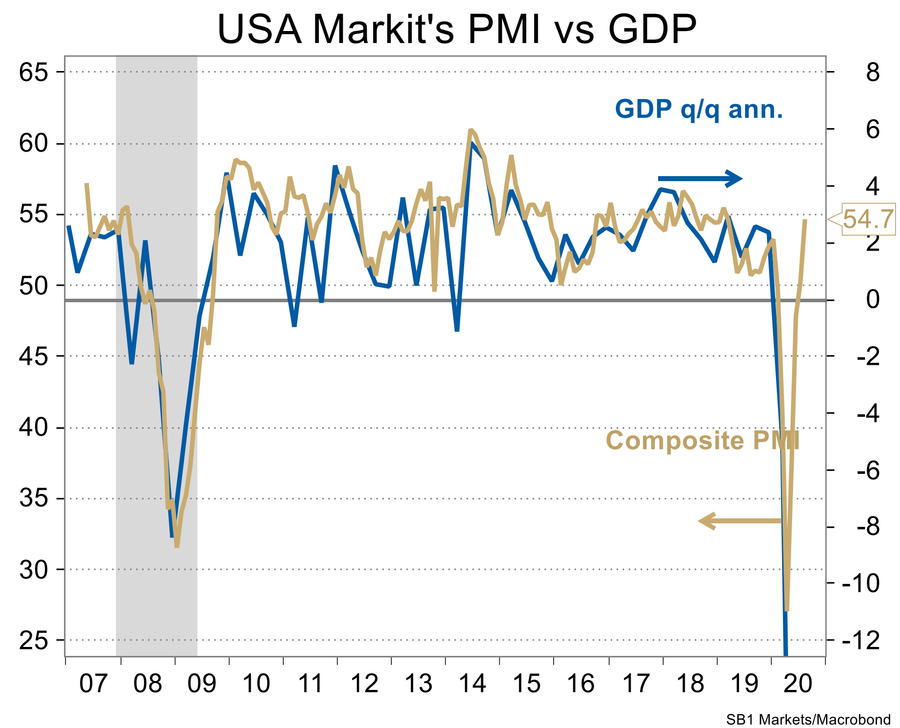
Markit's PMIs signalling faster growth – not corona setback

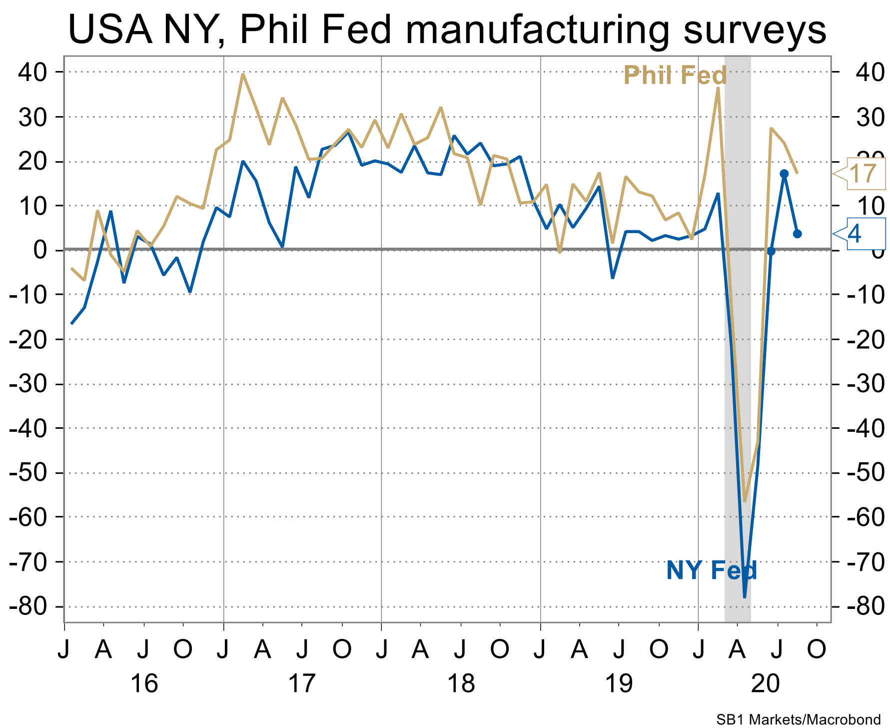
(But in July, the PMIs were on the weak side

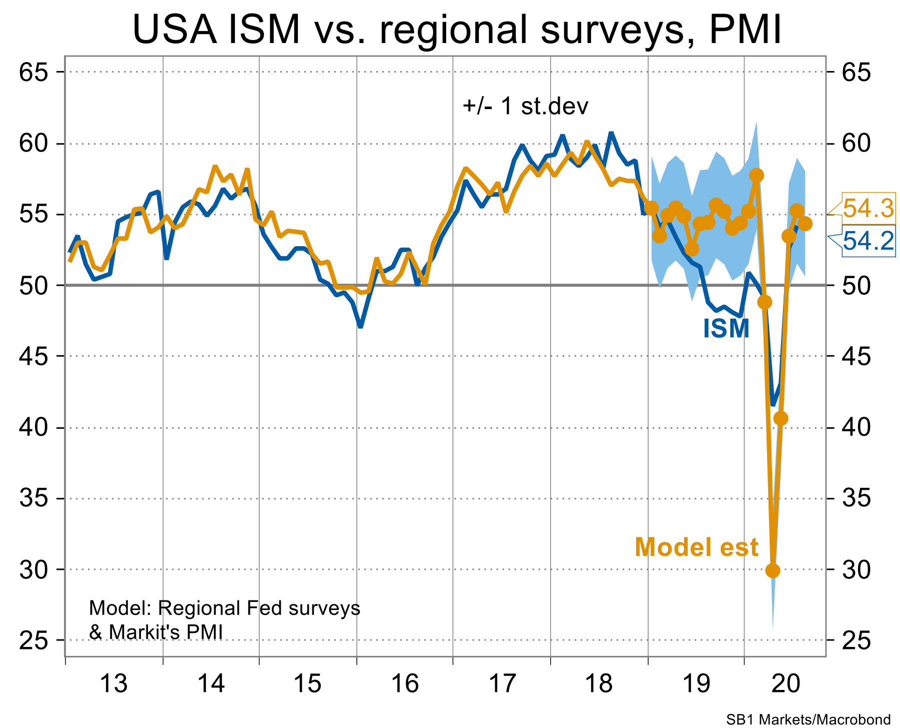




NY & Philadelphia Fed manufacturing indices down in Aug, and more than exp.

Levels are still OK (in average, due to Phil Fed). Suggest, together with Markit's PMI, ISM marg. down

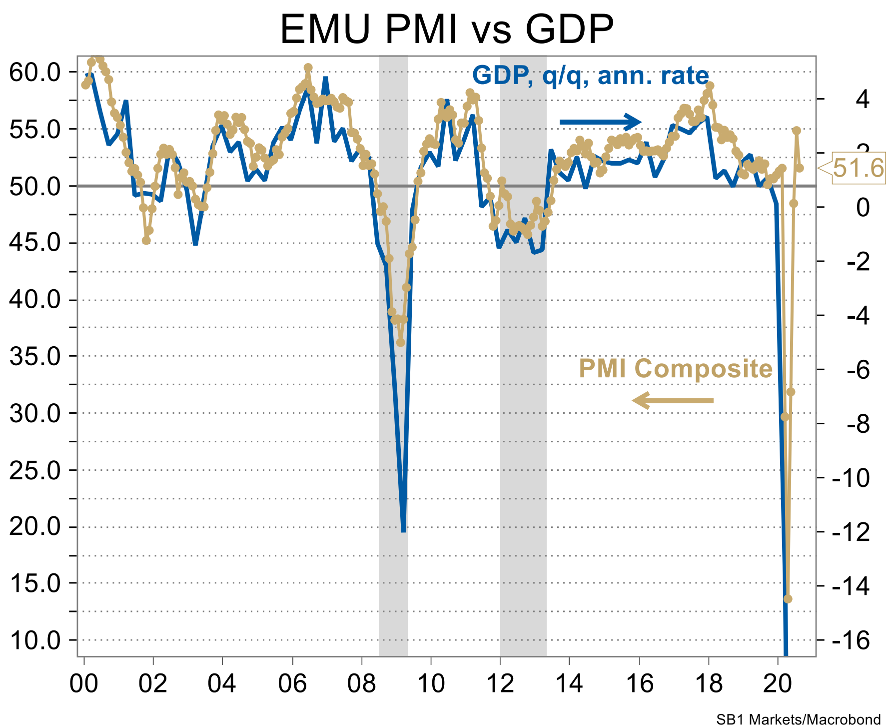


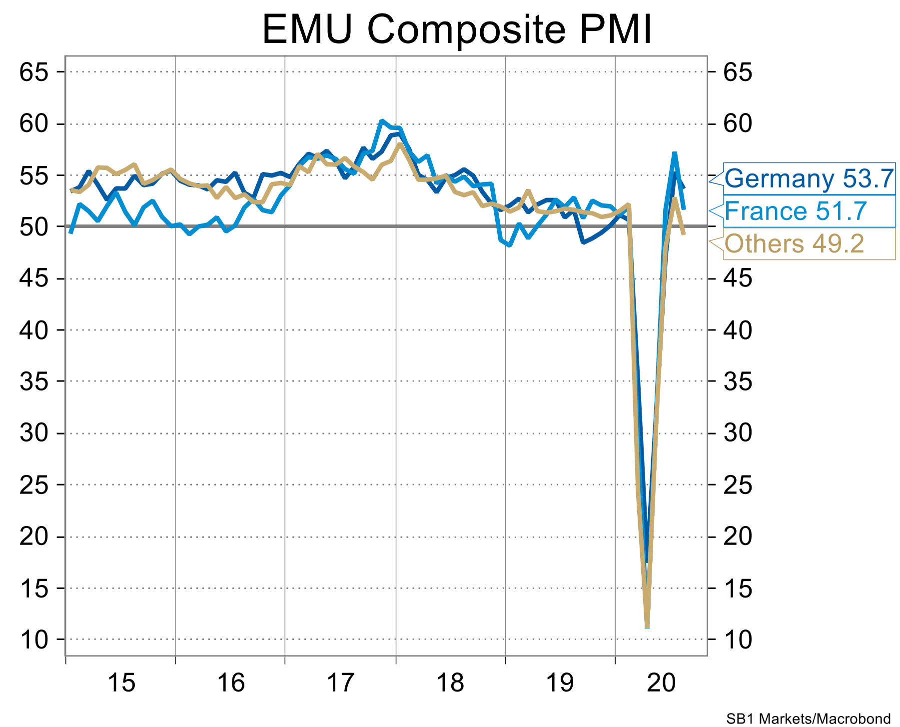


- The surveys have underestimated growth during the first phase of the recovery
- We assumed that companies soon would become better to calibrate their answers to the actual growth rate now. The August surveys signal growth above trend in manufacturing production – but less than needed to close the production gap anytime soon – and less than our forecast for August.

The composite PMI sharply down in August, still above 50

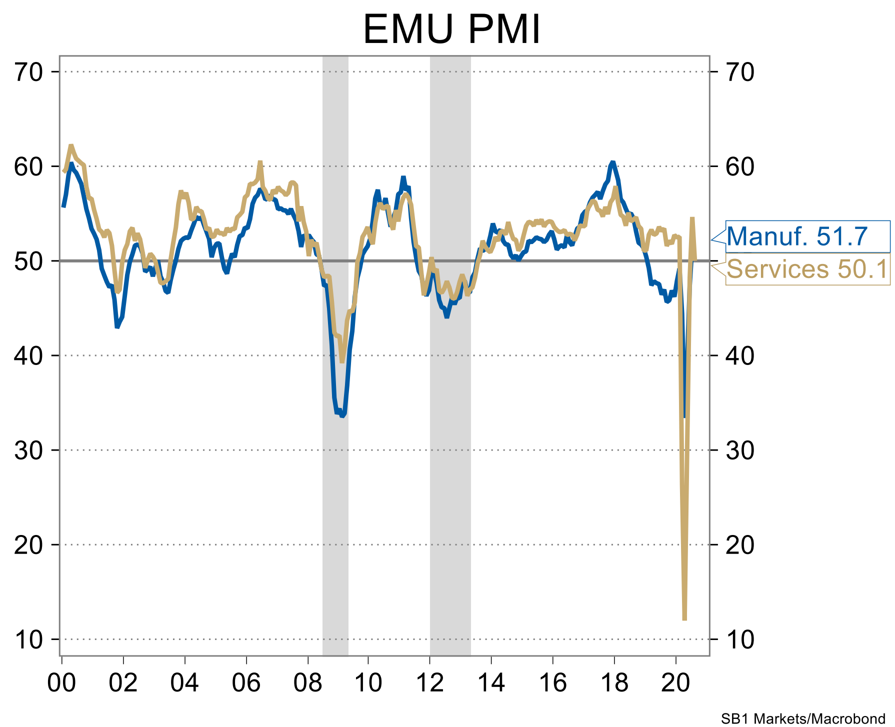
The slowdown was broad geographically. May be a response to the new corona challenges

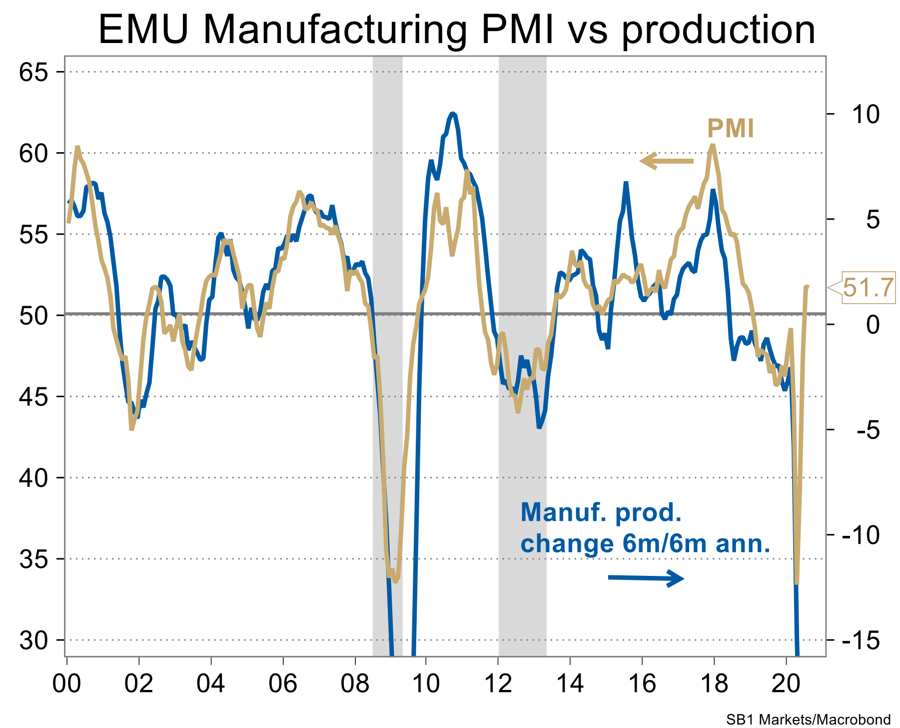




- The composite PMI is signalling just 1% GDP growth (annualised), close to trend growth. That's way too low, given the low activity level following the 12% decline in GDP in Q2

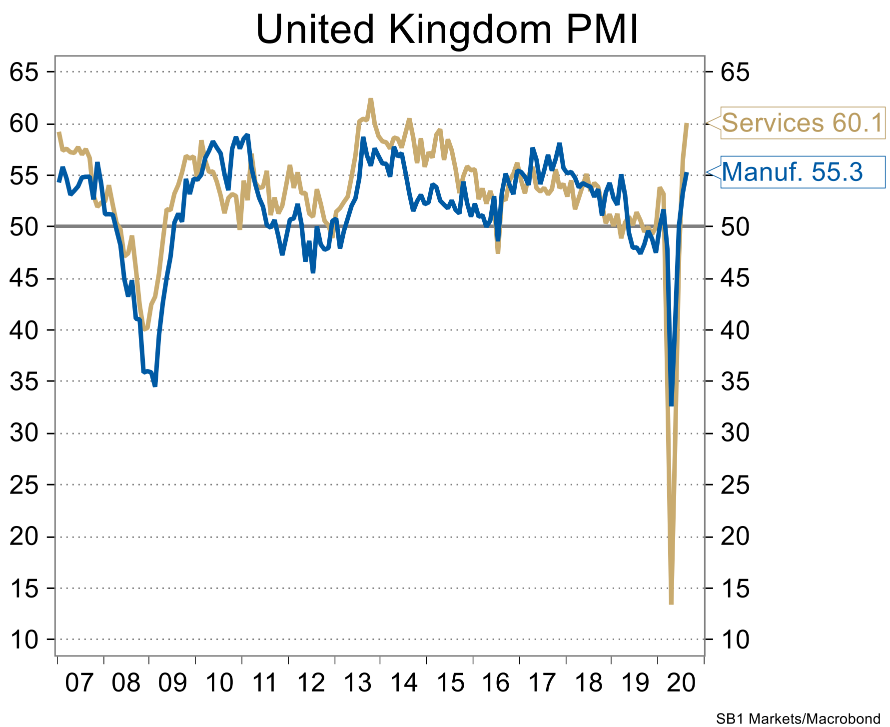
Services slowed down – signals slow growth. New corona restrictions to blame?

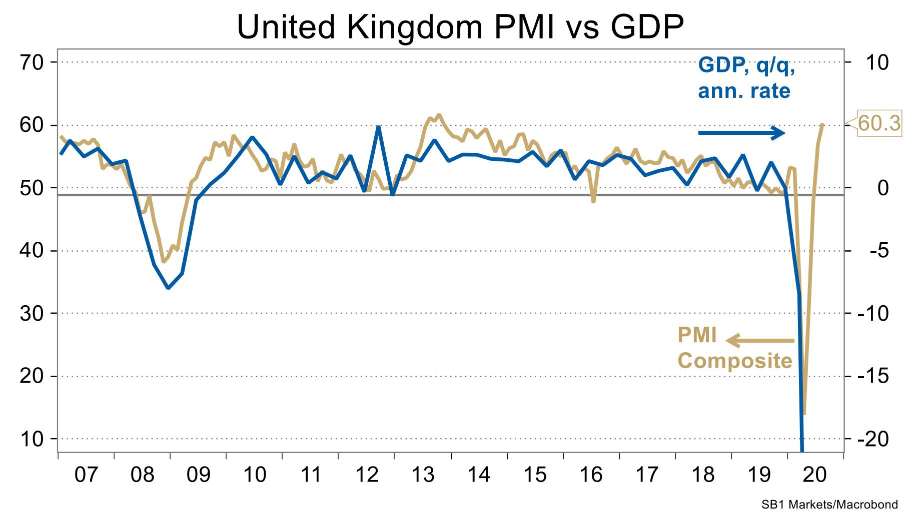


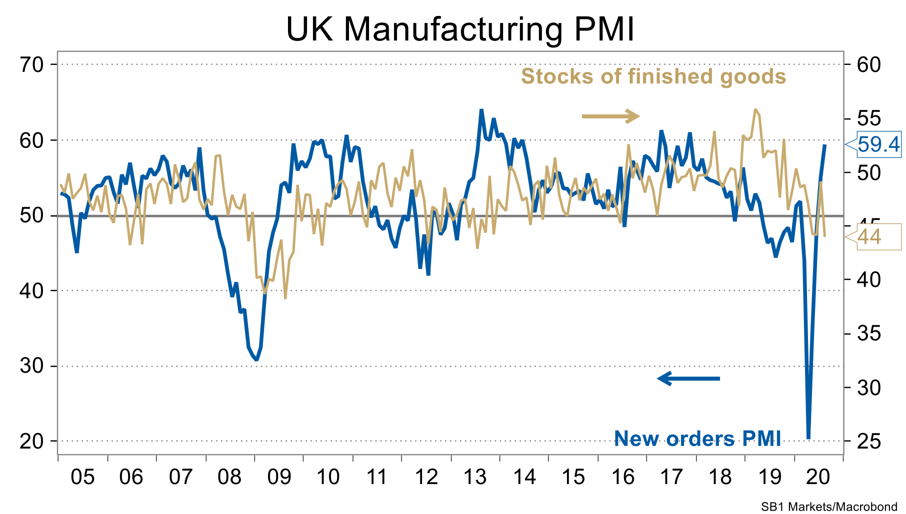


The composite PMI at 60. Signals much needed growth

Both services and manufacturing are both reporting decent growth

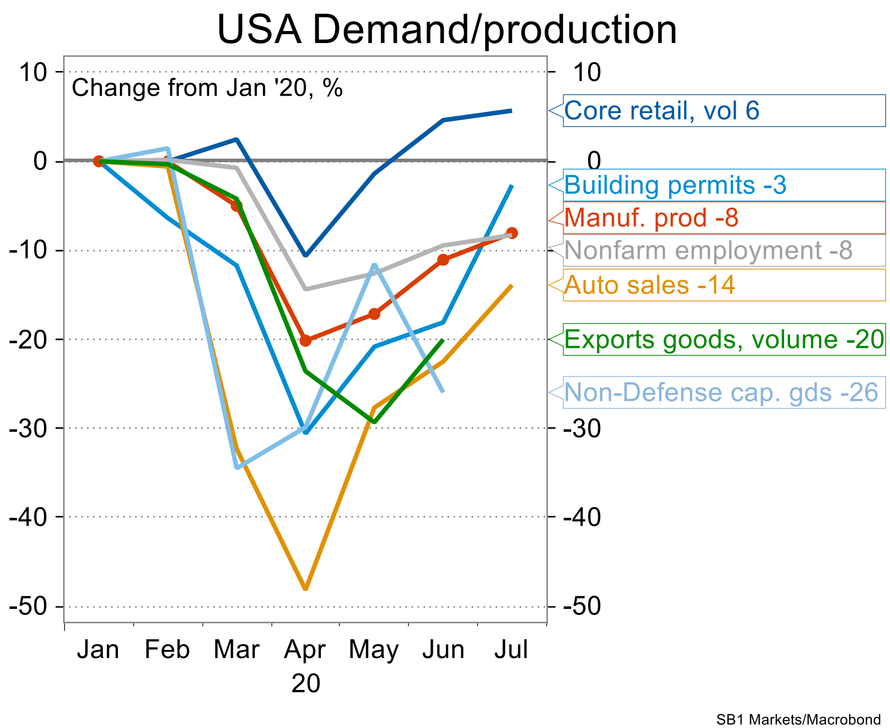






On the way back – but not synchronised yet

Core retail sales well above the pre corona level, building permits close too



Some different shapes and forms of 'V's

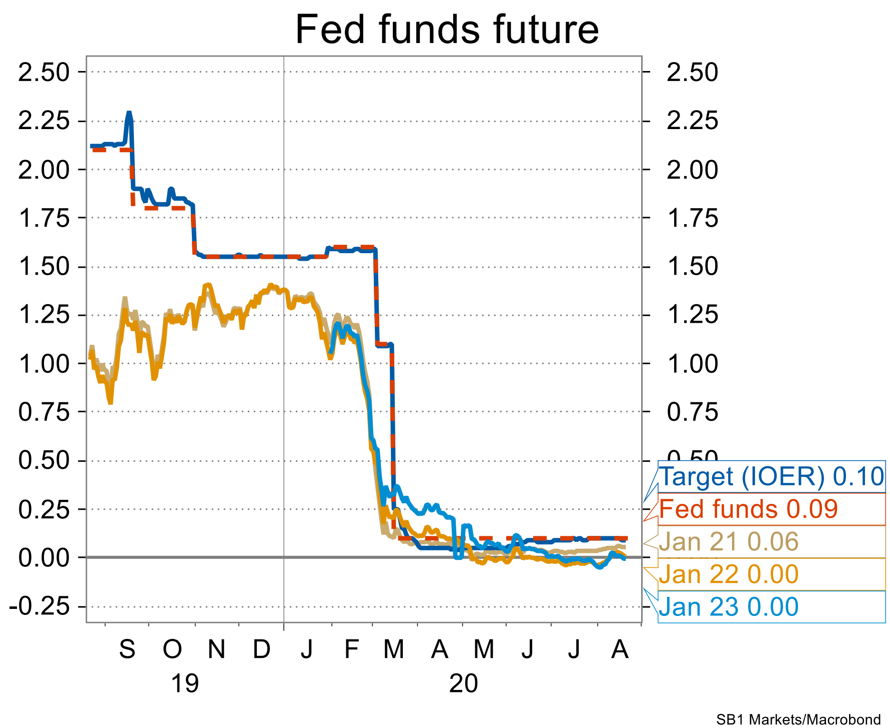
- Export volume still low, as are new investment goods orders (both June data), down 20 – 26%
- Auto sales down 14%
- Employment 8%, and manufacturing production -8%
- Households' goods demand strong, both housing & retail sales

Demand vs production

- Manufacturing production is weaker than household demand for goods. Weaker investment demand, exports and a sharp inventory drawdown explains the difference

FOMC minutes on the dovish side, but not Yield Curve Controal

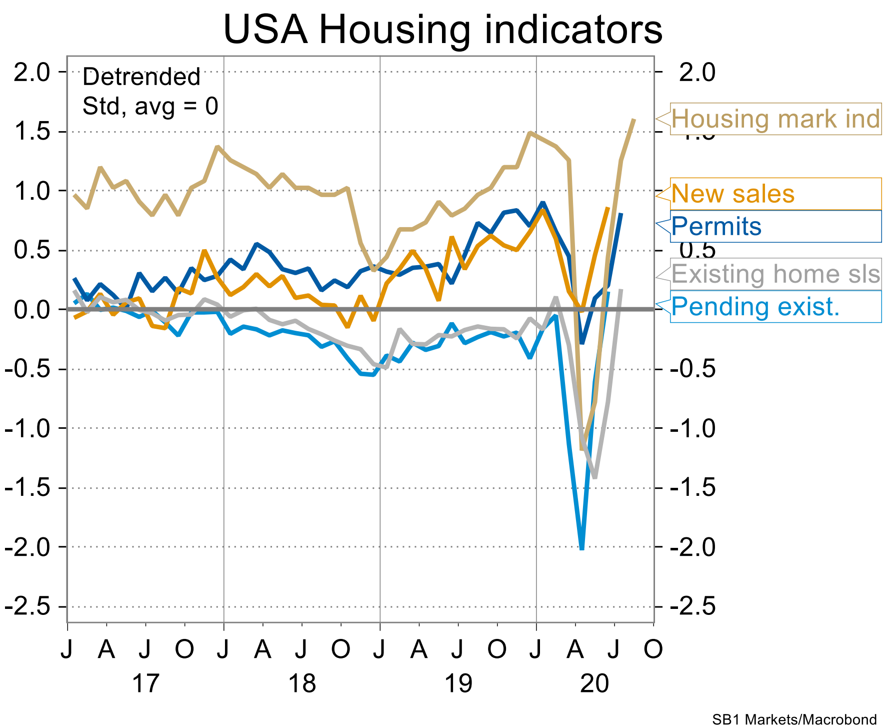
Dovish on the economy, no signals on the new monetary policy strategy – but it's on the table



- The FOMC is still worried growth will surprise on the downside, and begs for more fiscal policy support
- Markets have been focusing at the possibility of a change in the monetary policy strategi – which the bank is working at. At some point, '*a number of FOMC participants noted greater clarity of providing greater clarity regarding the likely path of the target range for the federal funds rate would be appropriate'*
  - » This sentence does not exclude the possibility of introducing a new strategy implying that interest rate will not be lifted before inflation has been above the 2% target for a while, perhaps to reach a 2% average inflation rate over time – or in order to maximise employment. However, it does not signal a shift, and certainly not the timing
  - » In addition: '*Many participants judged that yield caps and targets were not warranted in the current environment but should remain an option'*. No hurry, here either
- Yields fell, even if the comments on YCC were negative. The bank's assessment of the economy may have been more important

Check the housing market 'V's. It just took 4 – 5 months

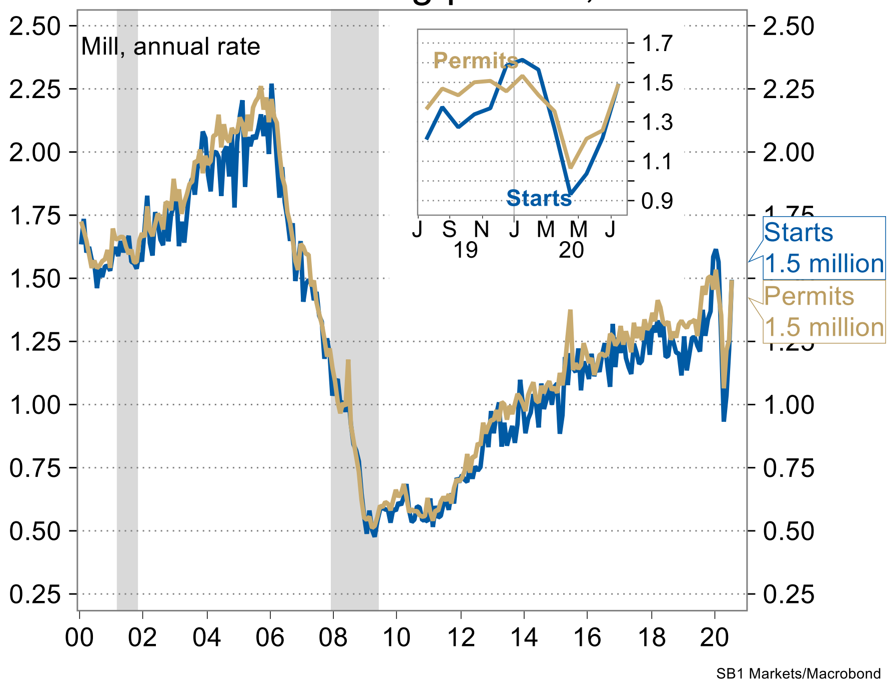
Starts, existing home sales & the housing market index all sharply up, well above expectations



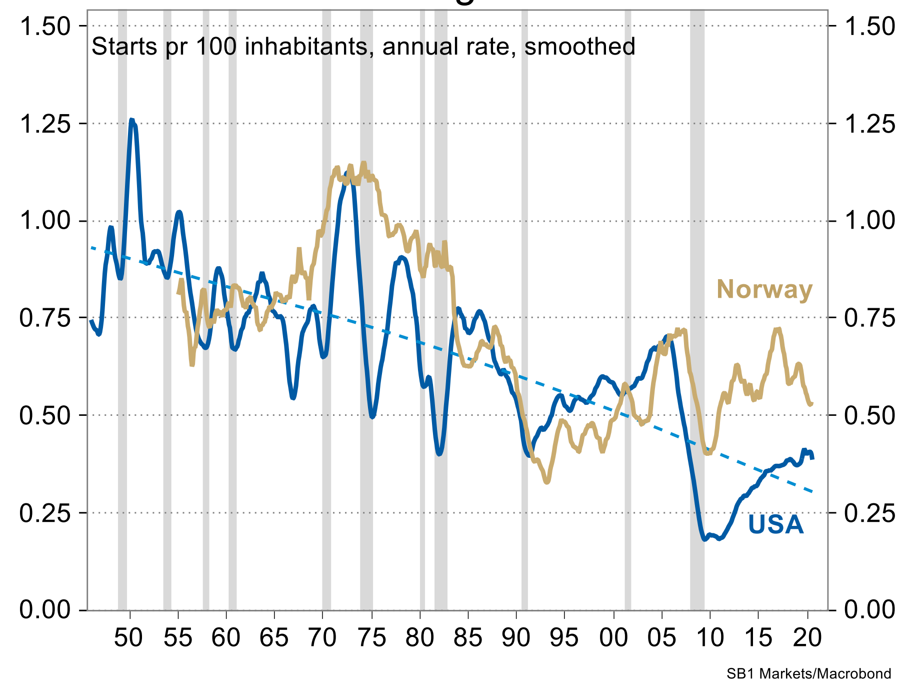
Housing: The ‘V’ is closed! It took just 5 months

Both housing starts and permits rose more than expected in July, and both are back to pre cor. level

USA Housing permits, starts



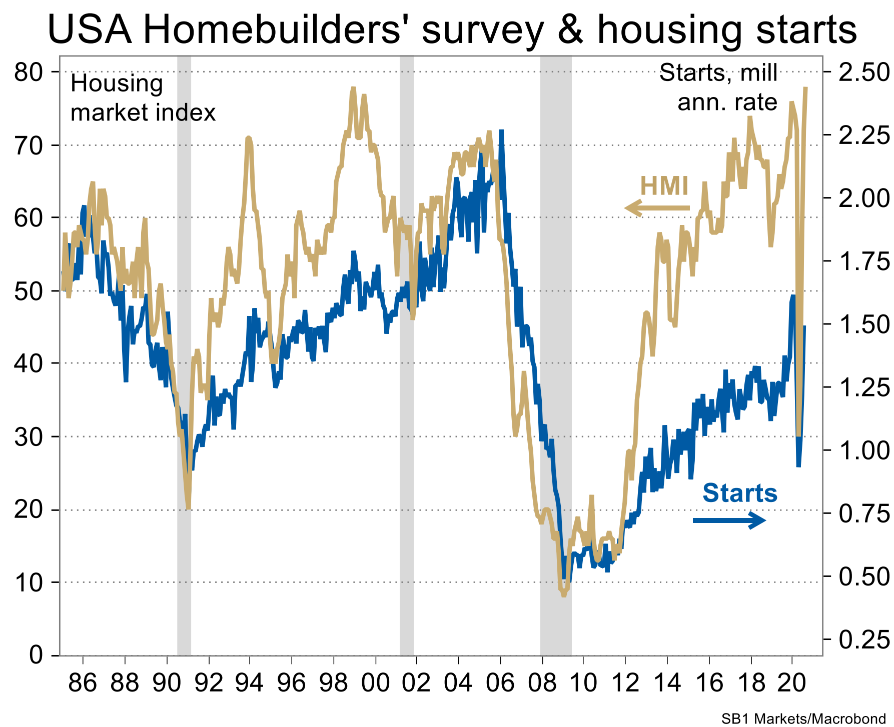
Housing starts

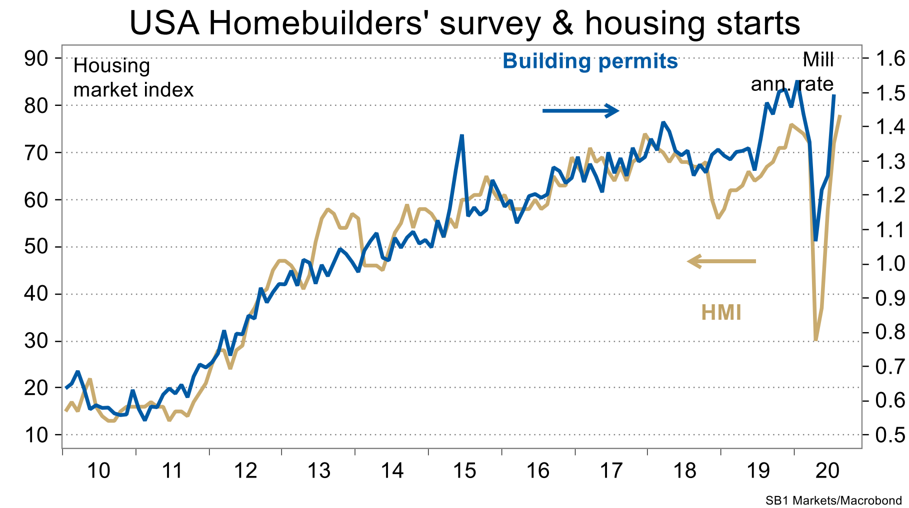


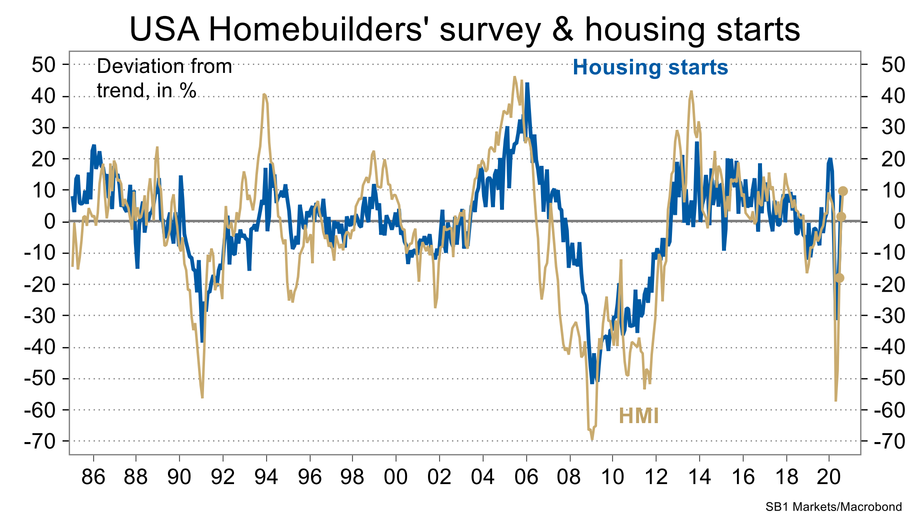
- Both housing starts and building permits rose approx 20% m/m in July to 1.5 mill, expected just up to 1.2 – 1.25 mill – a real surprise!
- Both starts and permits are back to the pre corona level, take of give. The ‘V’ was quite narrow, it took just 5 months to come back to the pre corona level

Homebuilders have never before reported stronger activity

The Homebuilders' Market Index surprisingly rose to ATH in august but it does signal more starts



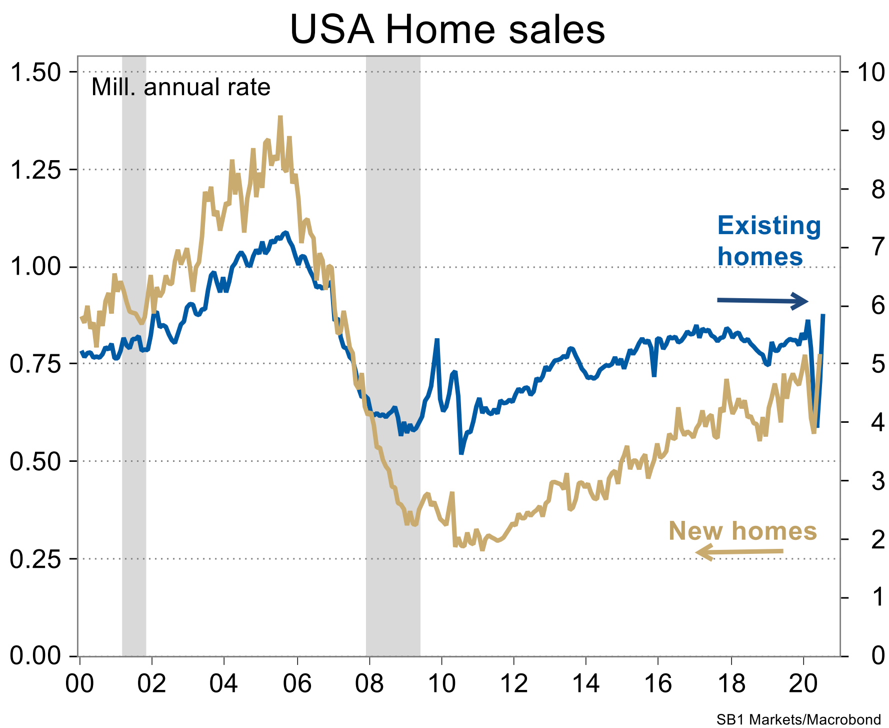


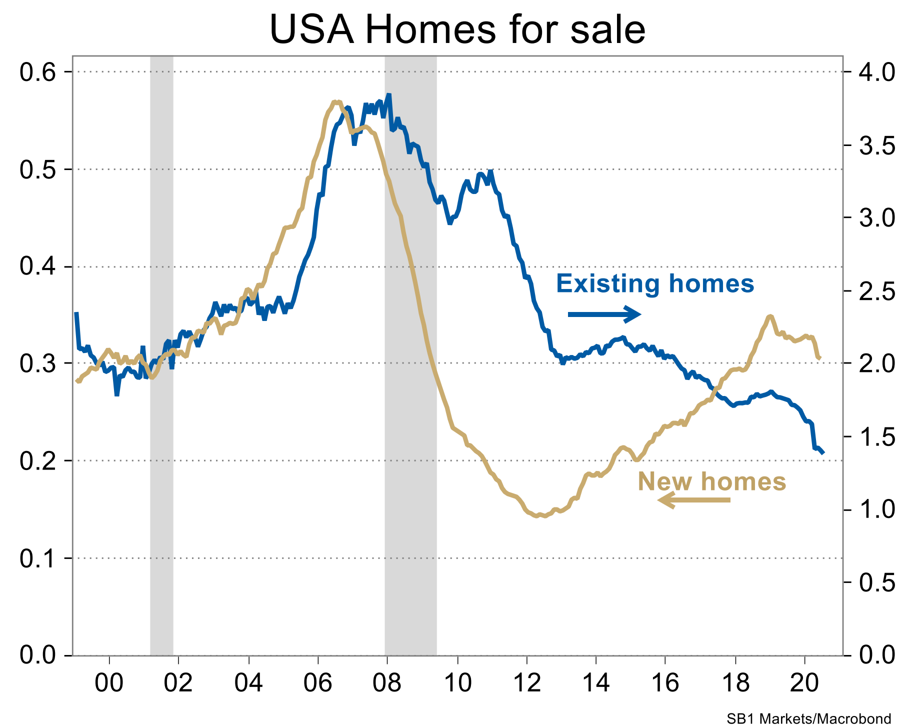


- The index has been at the same level once before, in '98
- The HMI is not an assessment of the 'level' of housing starts vs the long term average but rather deviation of starts from a more flexible trend, check the difference between the chart above and to the right
- The current index signals an unchanged housing starts level vs. starts in July

Existing home shot up in July, highest since 2007!

The number of homes for sale fell further – an the inventory is low

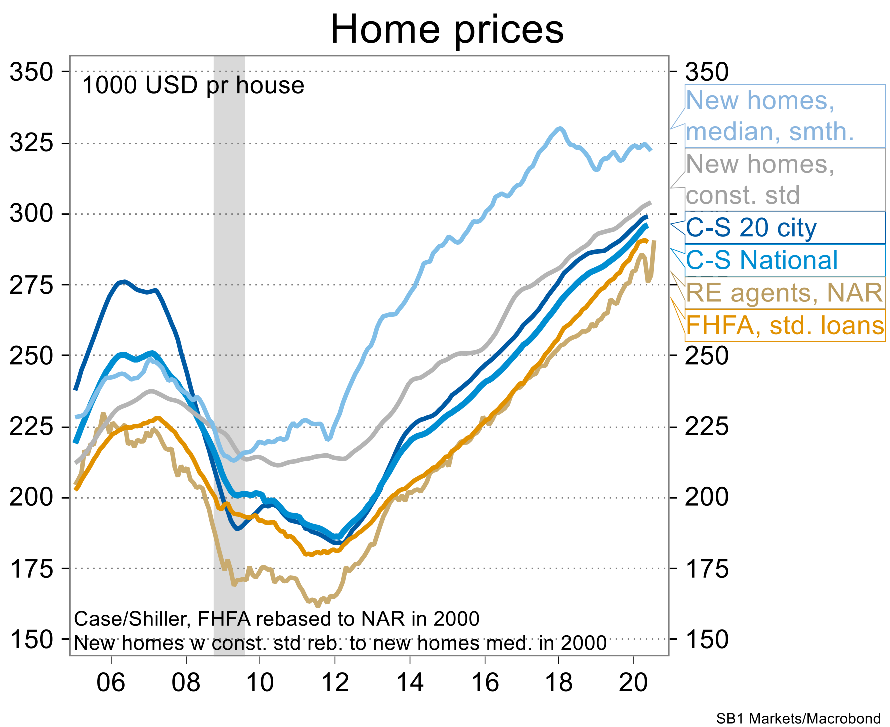


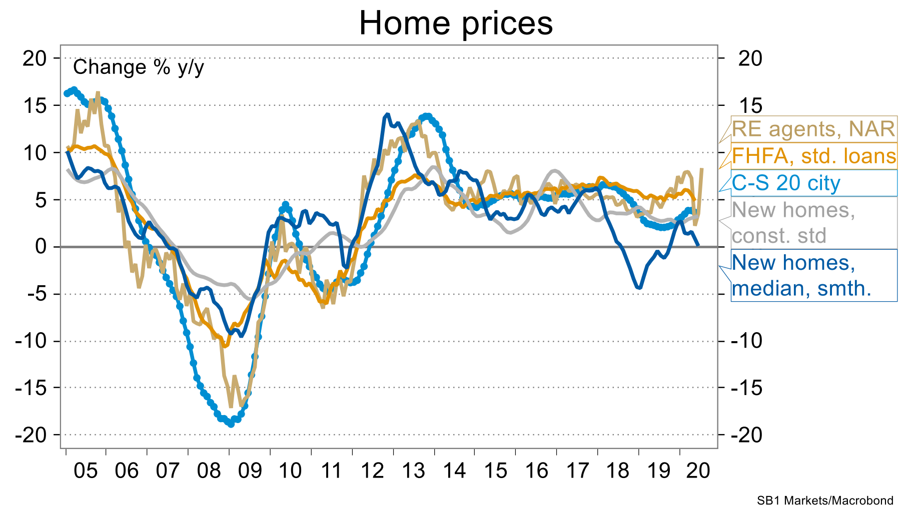


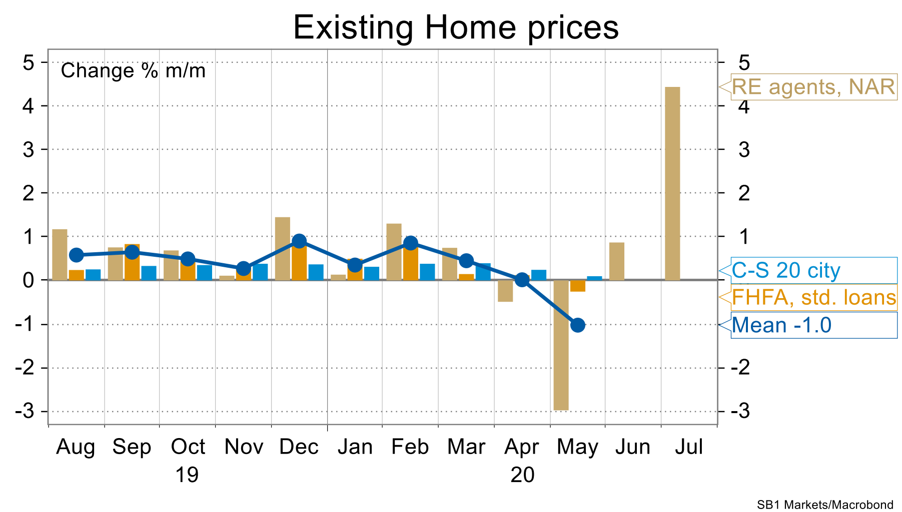
- Existing home sales jumped by 24% m/m in July, up to 5.86 mill – the highest level since 2007
- New home sales rise sharply in May and June
- Home prices rose sharply

House prices up again, according the realtors

Prices rise 4% m/m in July, more than ever before – and prices are up 8% y/y highest since 2013



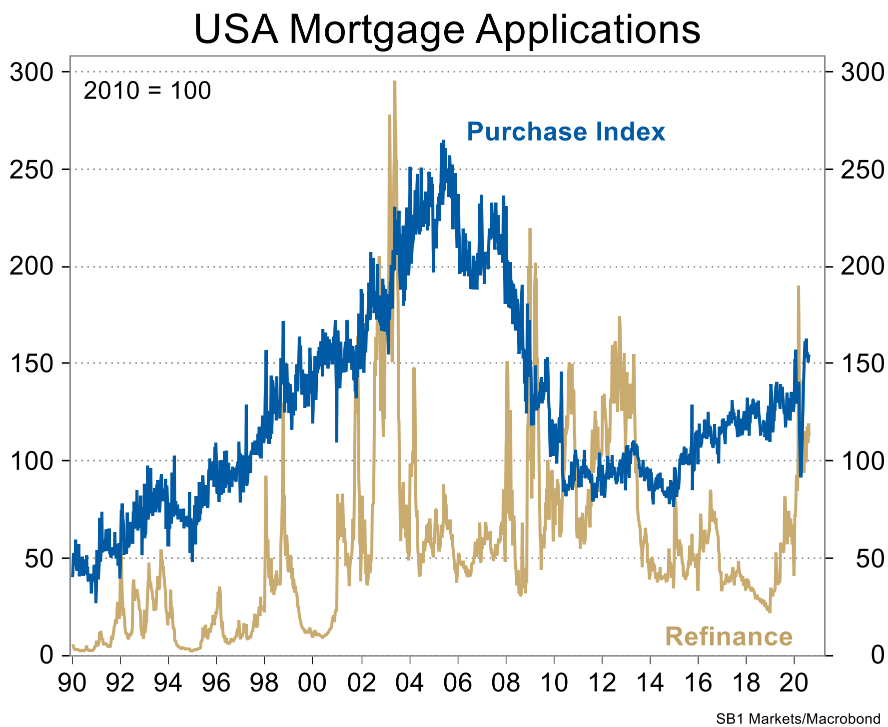


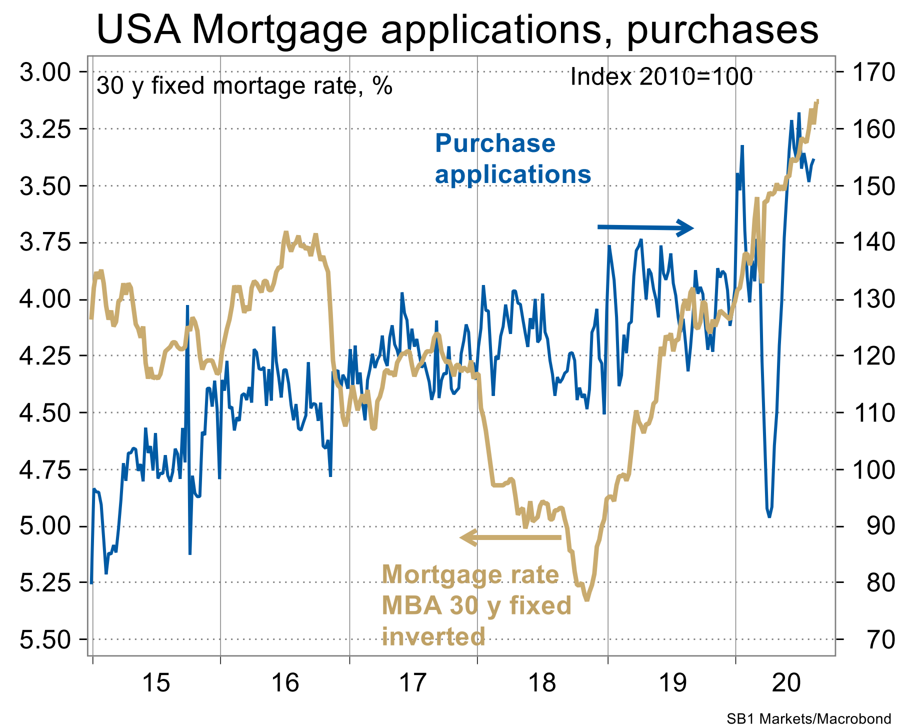


- NAR prices are more volatile – and prices fell by 3% in May – but the price recovery is impressive too
  - » We assume some of the price changes are due to changes in the mix of home sales. This price level is measured by the median of actual sales in each month, not adjusted for factors like location, size or quality

Mortgage applications are still at a high level

Applications fell sharply during the first phase of the corona crisis, then a sharp ‘V’ recovery

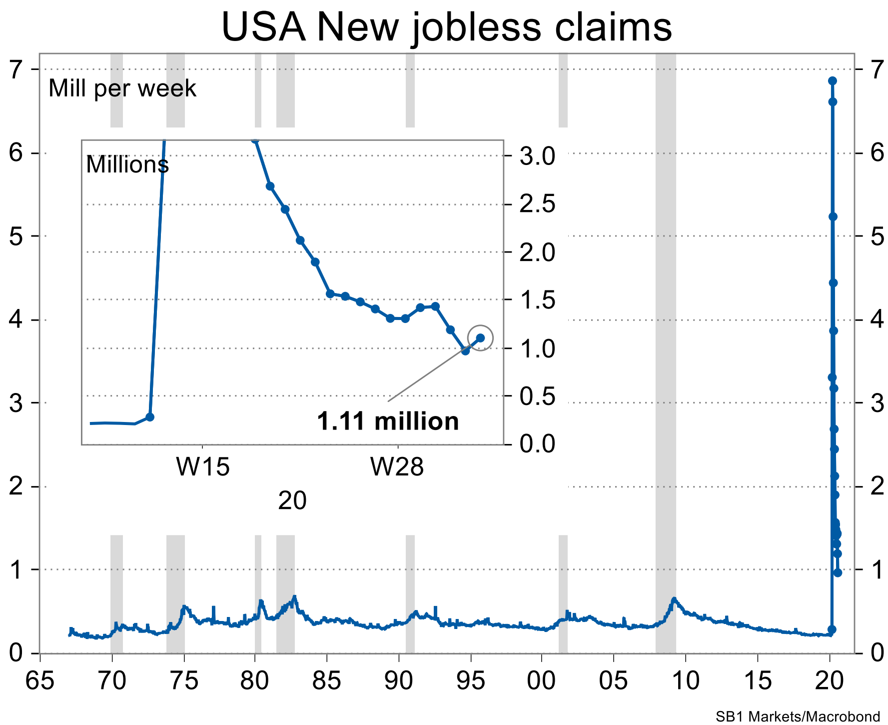


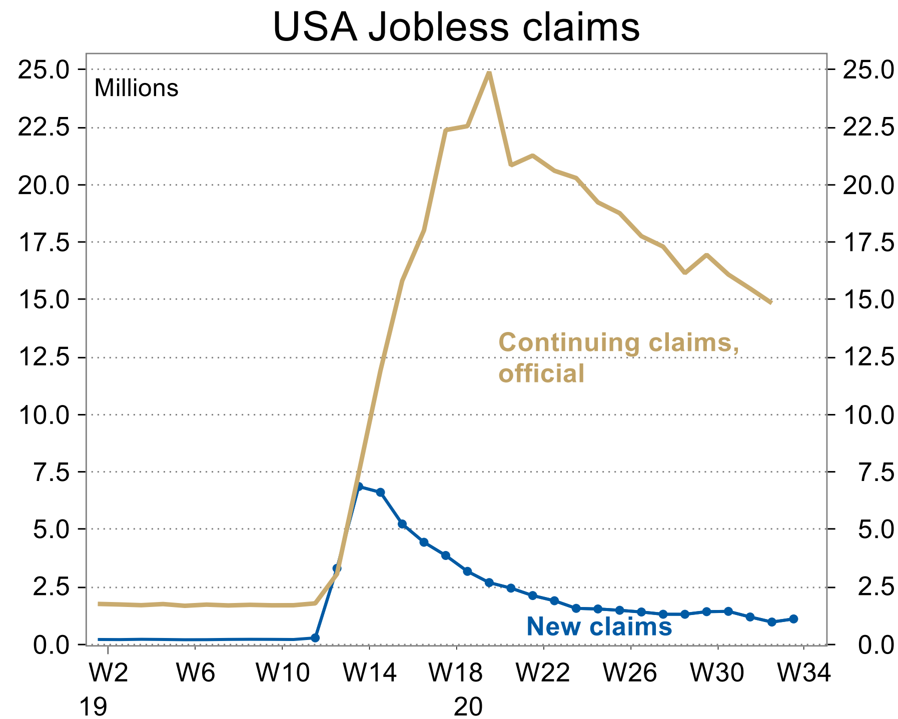


- No doubt, low mortgage rates stimulates demand
- Disclaimer: Demand for new mortgages has not been a reliable leading indicator for the housing market. Still, the spike in demand for new mortgages cannot be a sign of weakness

Oops, more new jobless claims again, and the inflow is pretty high

The trend is still down, following the previous two strong weeks. The level is still unusually high

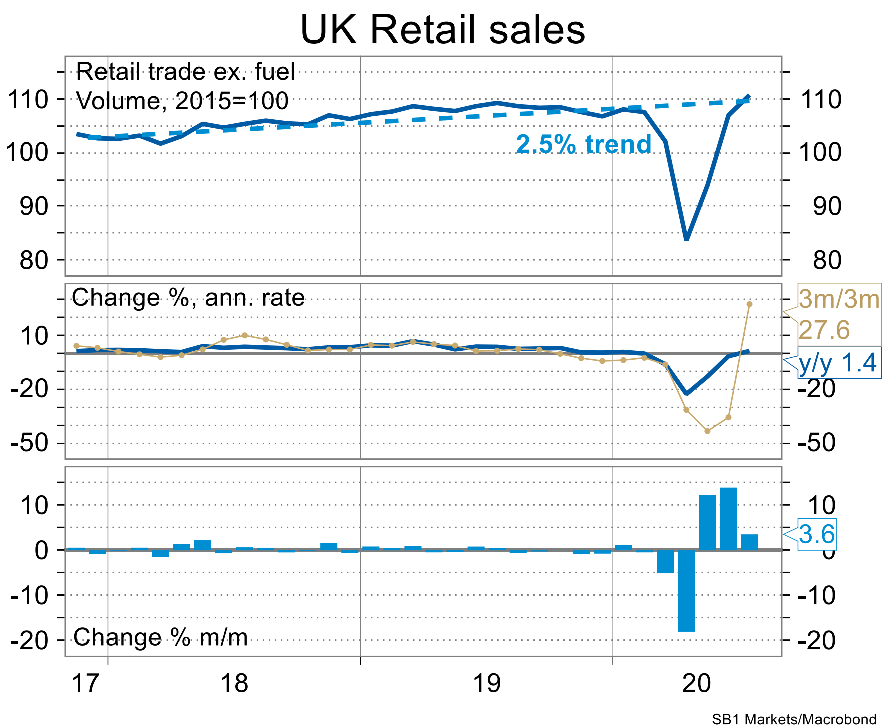




- The inflow is still far higher than during previous recessions now at 0.7%, and amid a rapid increase in employment. This gap illustrates the huge sectoral challenges, some have recovered, others are still struggling and have to reduce their payroll at a rapid pace
- Luckily, more are leaving the dole (for a job or are they leaving the labour market?): Continued claims has fallen to 15 mill from 25 mill.
- Most of the unemployed may now (at least for a while) lose their temporary USD 600/week extra federal unemployment benefit as the states have not been able to match the reduced USD 300/w federal assistance by 100 extra from the local state

Retail sales back on track, here too

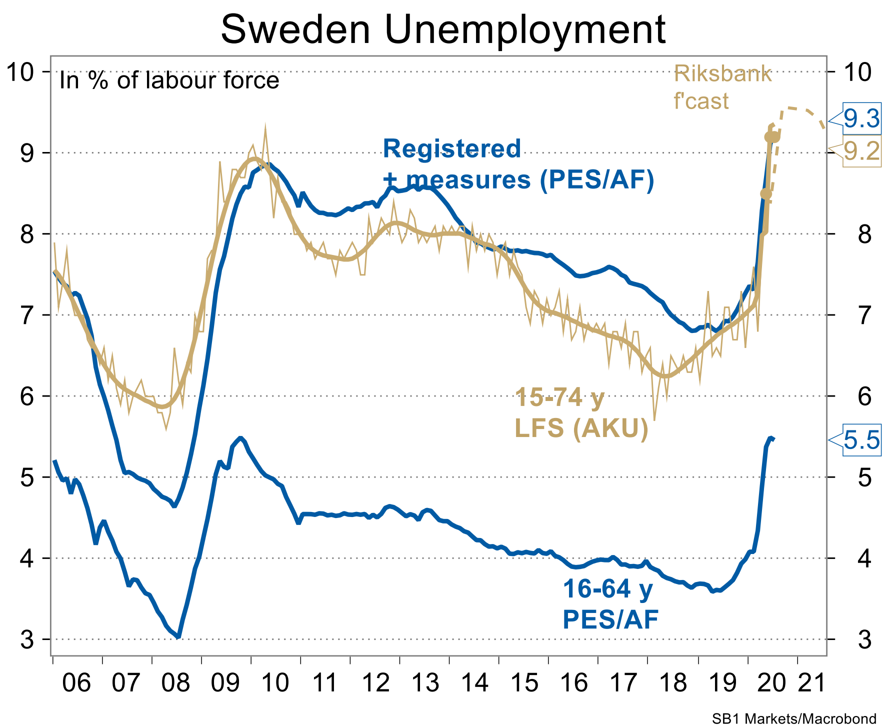
Sales rose 3.6% in July, expected up 2,0%. Sales are 3% above the Feb level – following a 22% drop

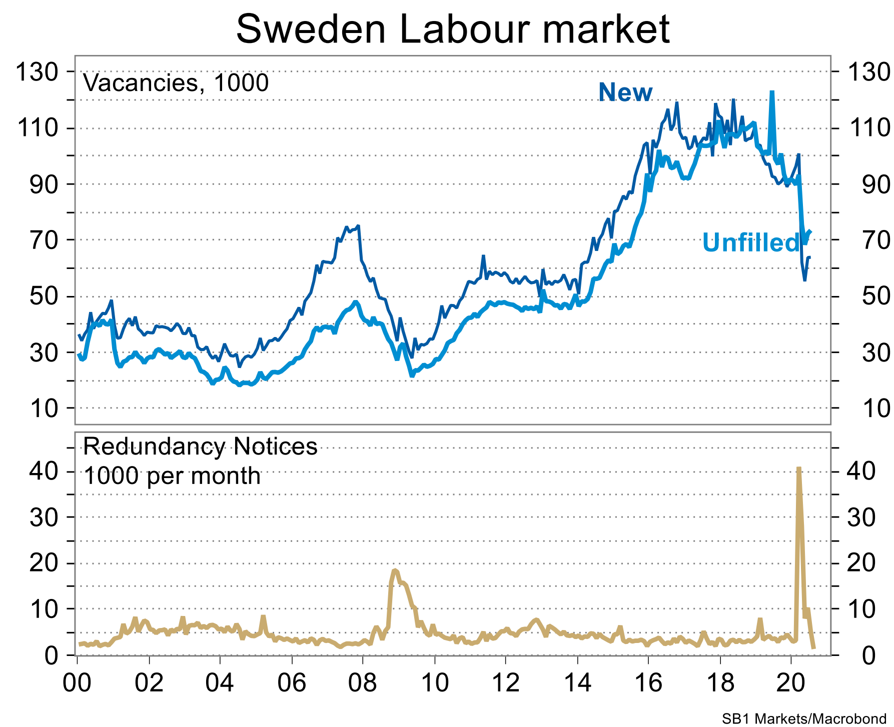


- Another sharp 'V'
- Services are not included in retail sales – and service consumption is still far below the pre corona level

Unemployment is increasing, employment is falling

The LFS rate was flat at 9.2% in July, up 2 pp from pre corona. The official, open rate stable at 5.5%

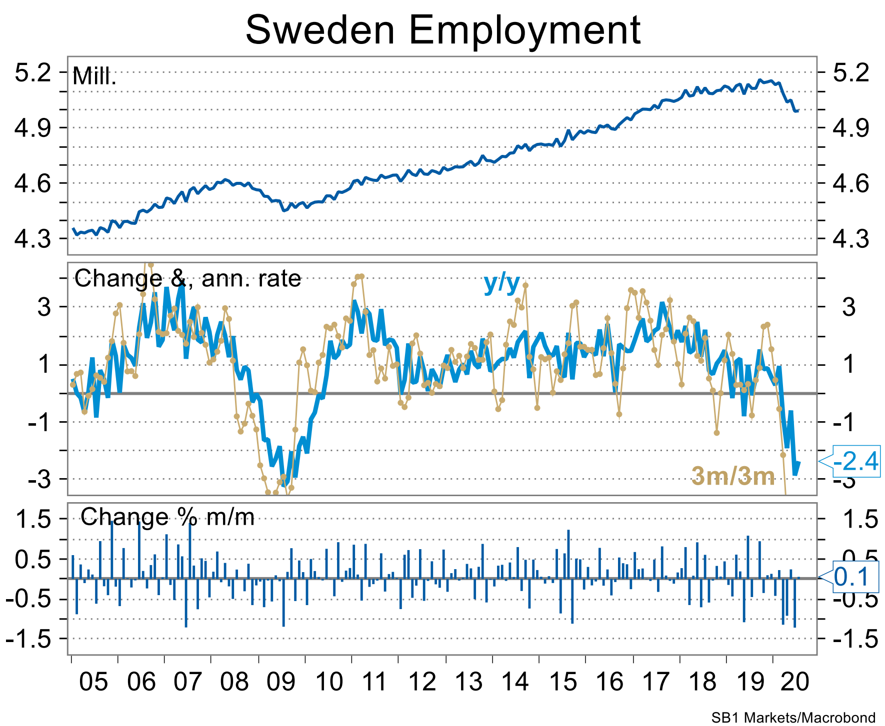


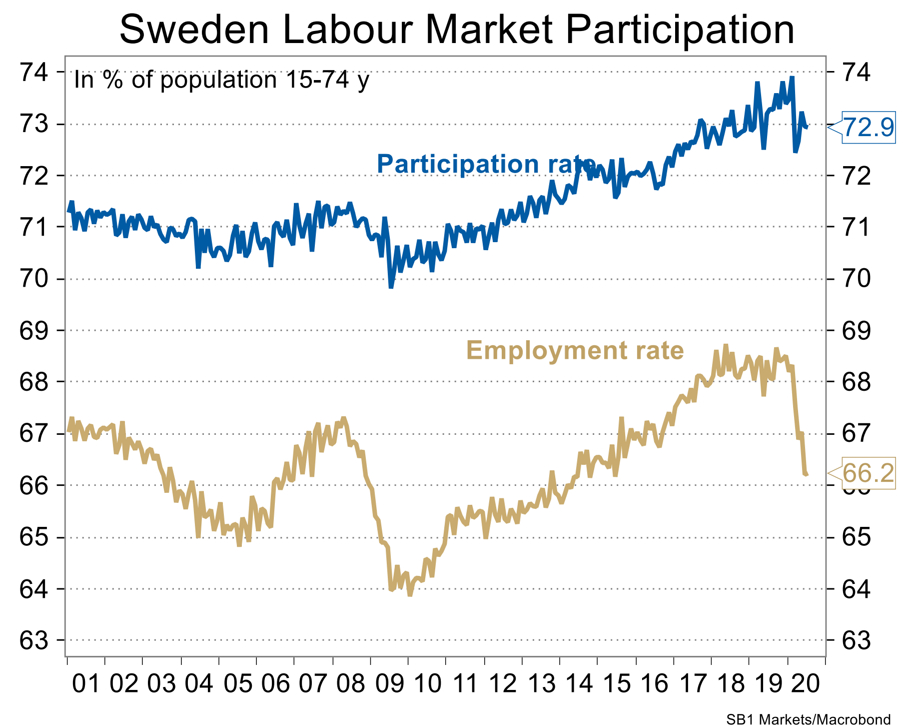


- Sweden has less furlough schemes, and less measures to subsidise employers to keep workers at job, and the unemployment rate is not comparable to other countries (like between most countries these days)
- Sweden has reported a 2 pp increase in unemployment, and a 2.5% drop in employment
- However, hours worked was down 10% at the worst, and are still down 6.5% vs pre corona (in July). In Norway, hours worked fell 'just' 8%, and was down just over 5% in the April-June avg.

Employment sharply down but far less than hours worked

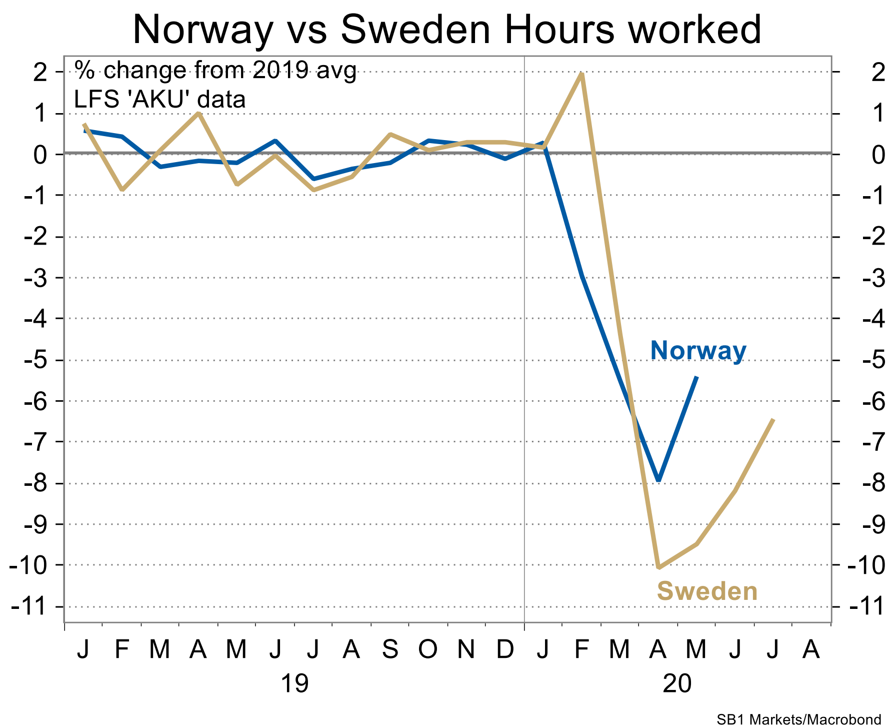
The participation rate has fallen somewhat but less than normal vs. the decline in the empl. rate

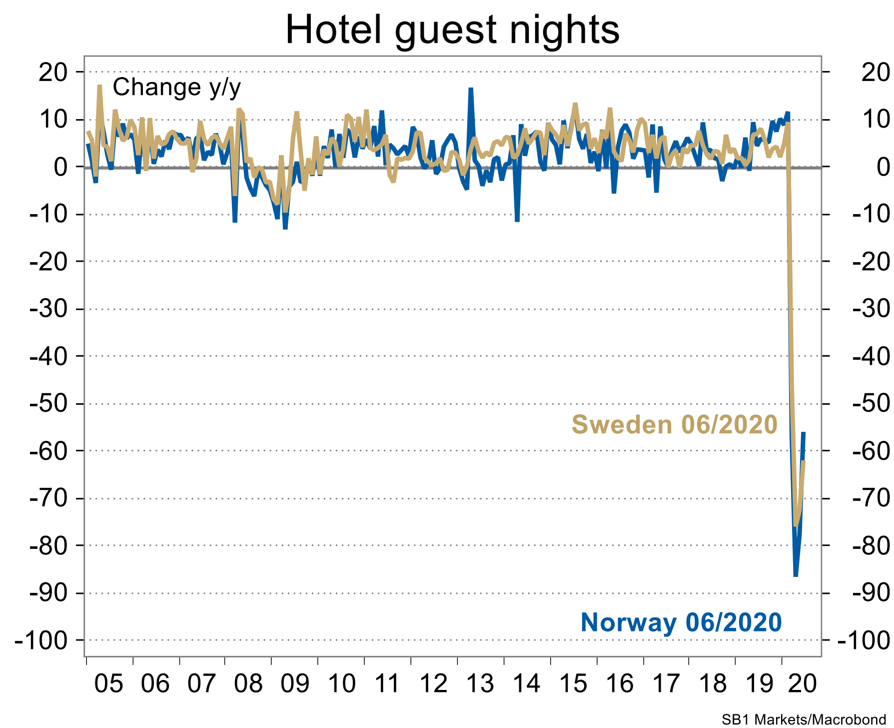




Norway vs Sweden: Hours worked more down in Sweden than in Norway

At least according to Labour Force Surveys ('AKU'). National accounts out this week

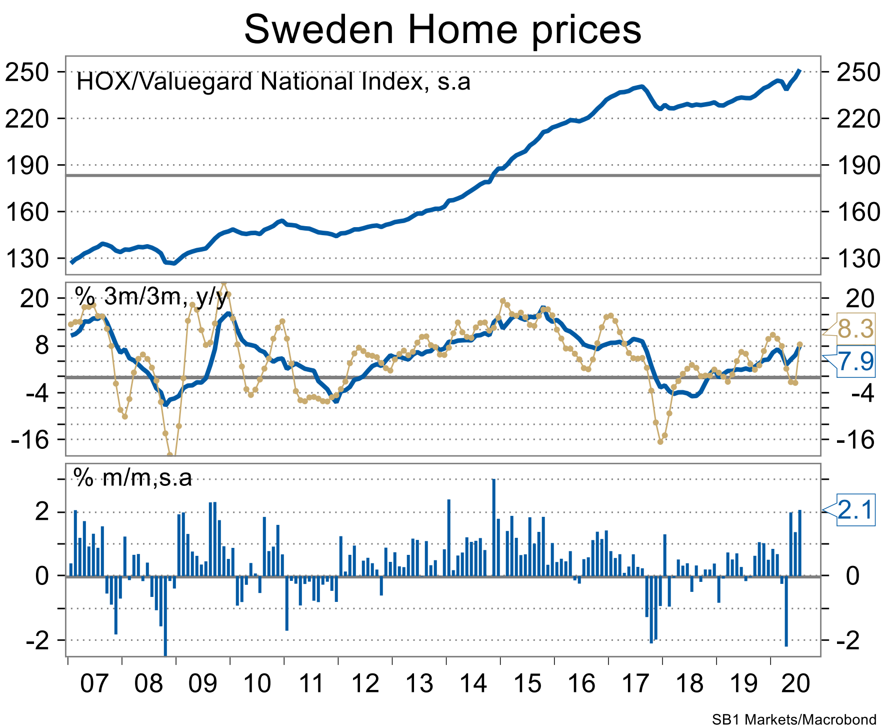




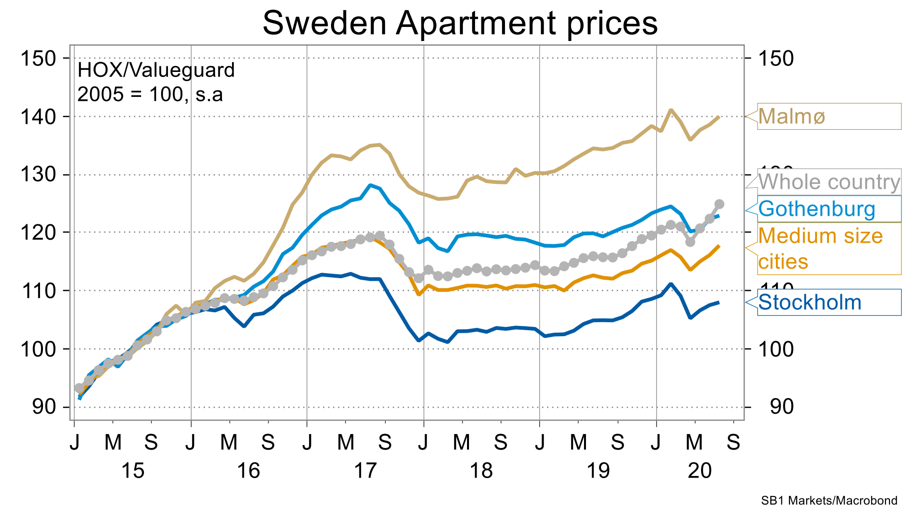
- BTW, not big difference between Norwegian or Swedish hotels – and retail sales have been much stronger in Norway than in Sweden – even without at Swedish 'lockdown' (which though was rather partial in Norway)

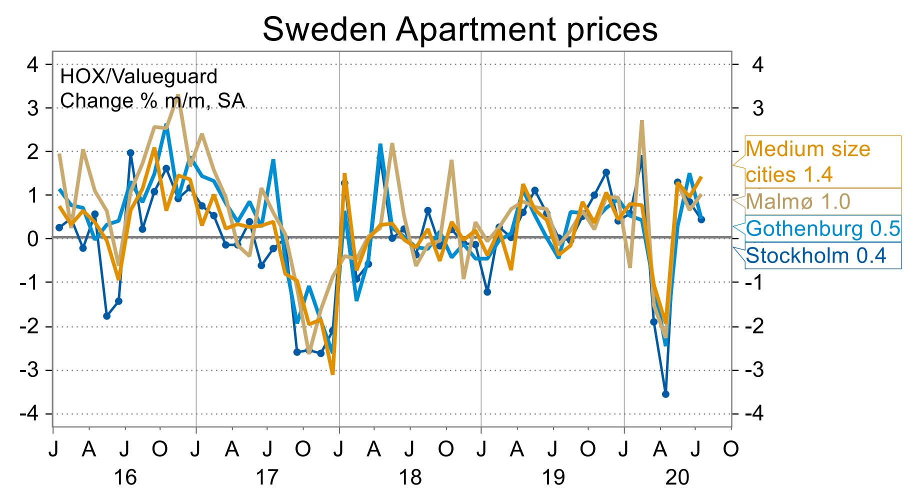
House prices sharply up in July too, now well above pre corona level

National prices rose 2.1% in July, following 1.4% in June. Stockholm is lagging



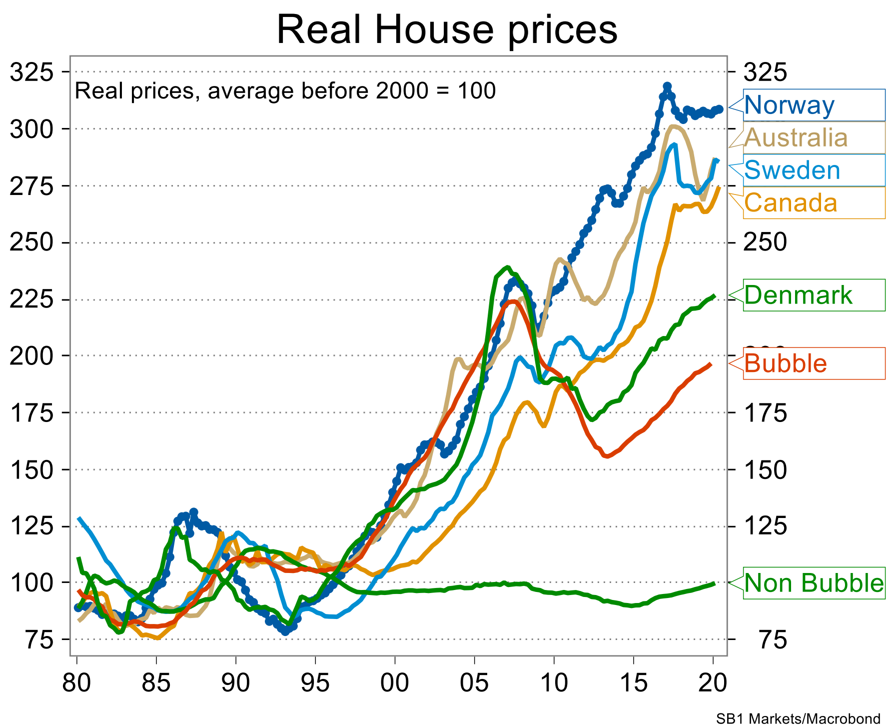
- Prices rose in all towns in July but 'just' 0.4% in Stockholm. Stockholm apartment prices are still well below the Feb level – and below the 2017 peak level

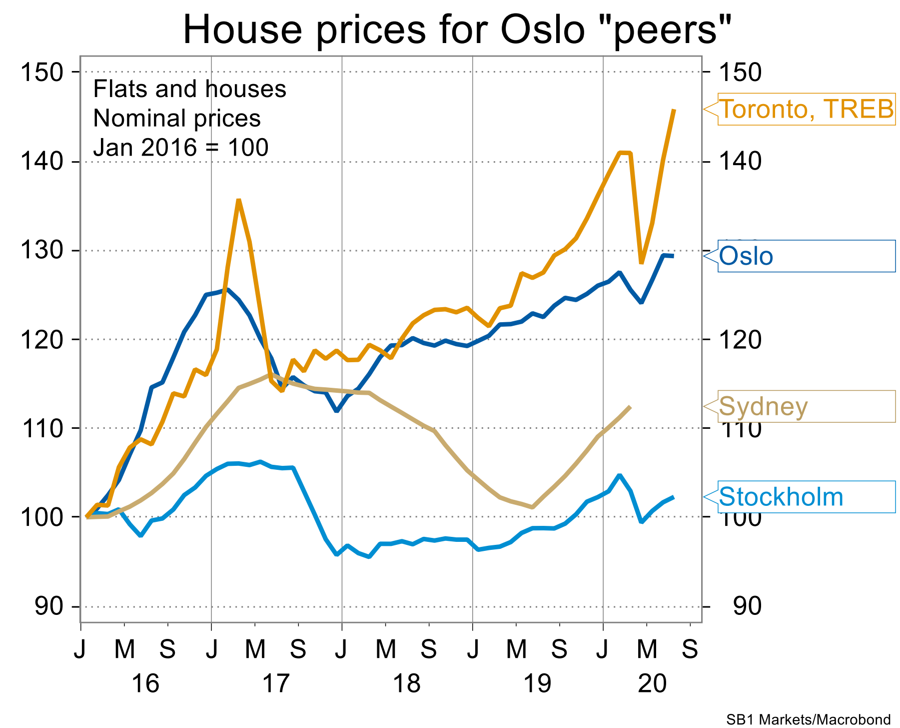




Of all the recent 'V's, the Stockholm 'V' is the least impressive

Prices have recovered early corona losses in Toronto and Oslo





Highlights

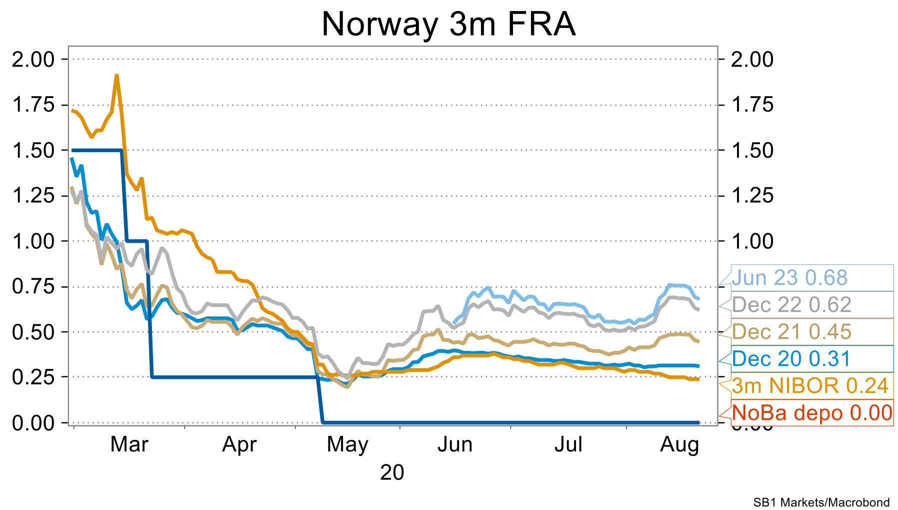
The world around us

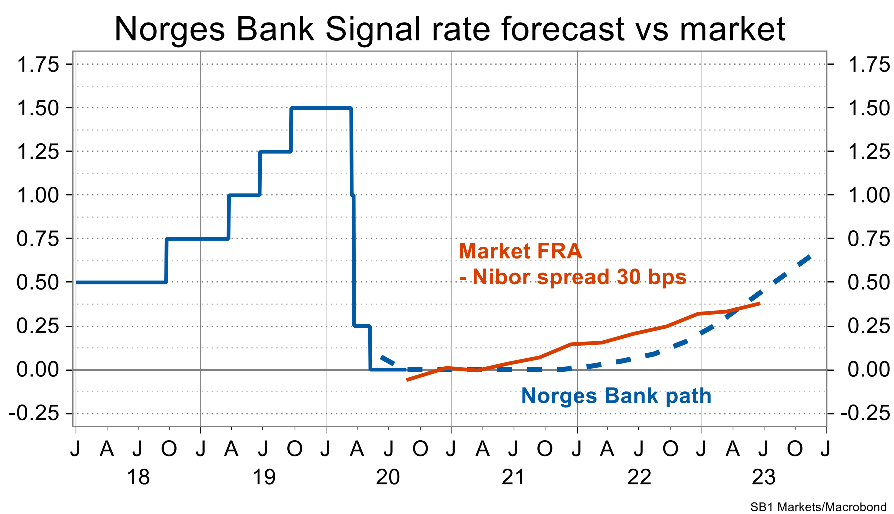
The Norwegian economy

Market charts & comments

Norges Bank: On the dovish side

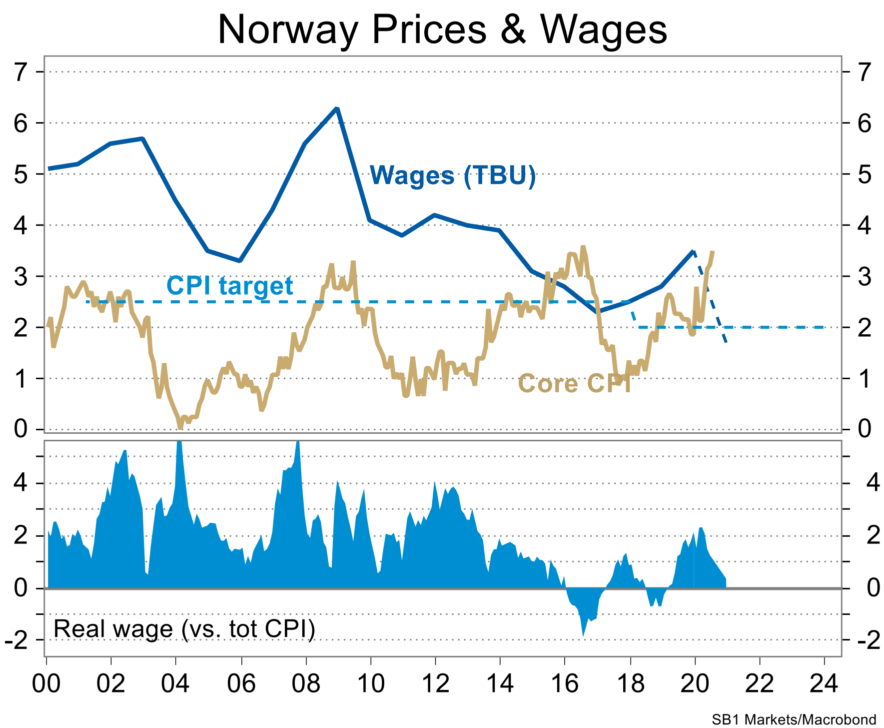
No hints of any upward revision of the interest rate path in the upcoming MPR





- Norges Bank left the signal rate unch. at 0.0%, as everybody expected
- The Bank was rather balanced – and dovish vs. our expectations – in its assessment of the economy and the outlook
  - » *'Both house prices and household credit have increased more than expected'*
  - » However, *'economic activity overall appears to have picked up broadly as projected'*
  - » And '*Labour market developments appear to have been somewhat weaker than expected'*
  - » The bank expects inflation to slow due to low wage growth and a stronger NOK
  - » The Bank focuses on the considerable uncertainty vs the economic outlook, also due to the newly increased spread of Covid-19 and reintroduced restrictions
- In sum, no hints of a further lift in the interest rate path in September. Still, we judge the risk to be on the upside, barring substantial corona problems abroad or back home
- FRA rates dropped some few bps on the announcement

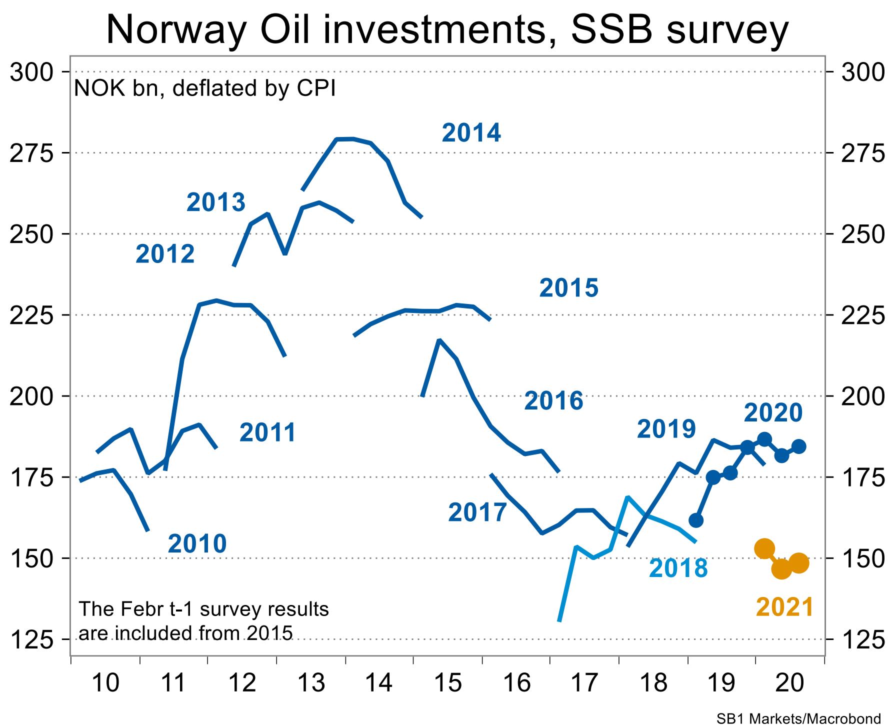
No strike, of course. 1.7% wage inflation agreed upon



- At Friday, the first round of this year's (postponed) spring wage negotiations was finalised, after 22 hours extra mandatory mediation
- A 1.7% wage lift in 2020 was agreed upon, of which 1.2 pp is due to carry-over from wage increases during 2019
  - » The employer's offered these 1.2% (and nothing more), we expected an outcome closer to 2%
  - » Included in the sum, a substantial increase in minimum wages, we estimate some 5%!
  - » Other trade unions/employers associations are now entering the play. We expect the same 1.7% +/- some very few tenths (1 – 2) to become the norm for the deals to be concluded the coming weeks, including the public sector
- A 1.4% 2020 CPI inflation is expected, far below the present core rate (3.5%). Electricity prices have fallen sharply, and the 1.4% is not impossible to reach. If so, real wages will increase by 0.3% in 2020
- Norges Bank expected a 1.9% wage inflation in 2020. The estimate may not be changed in the upcoming monetary policy report if not for a change in the mix of the employed that will increase the average wage level – as more lower paid than higher paid employees have lost their jobs

A doubling of the oil price, and a substantial tax cut did not alter that much

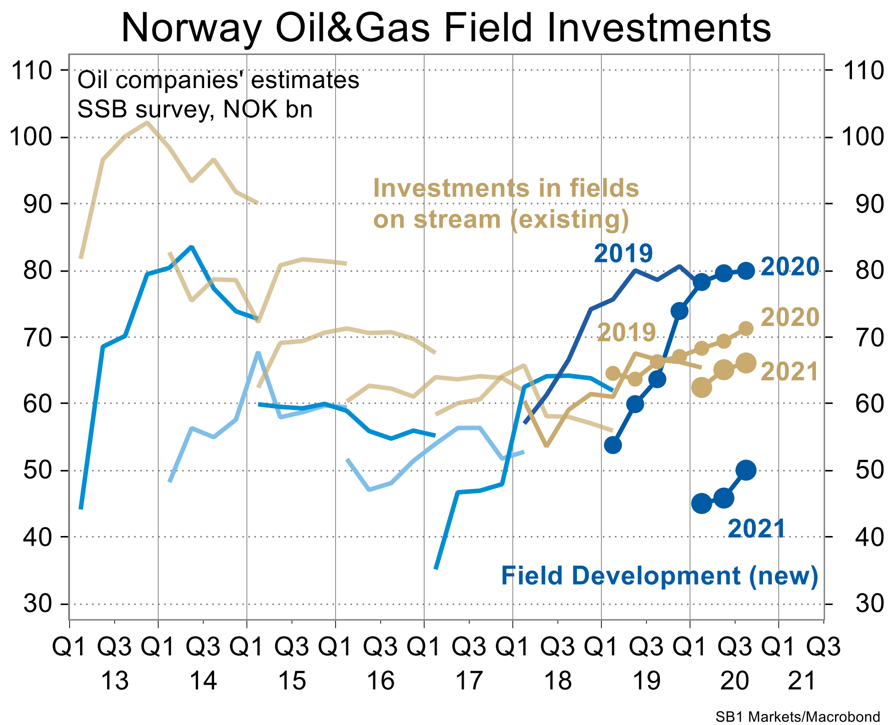
Just small revisions of investment estimates – a 12% decline is signalled through 2020 and ‘21

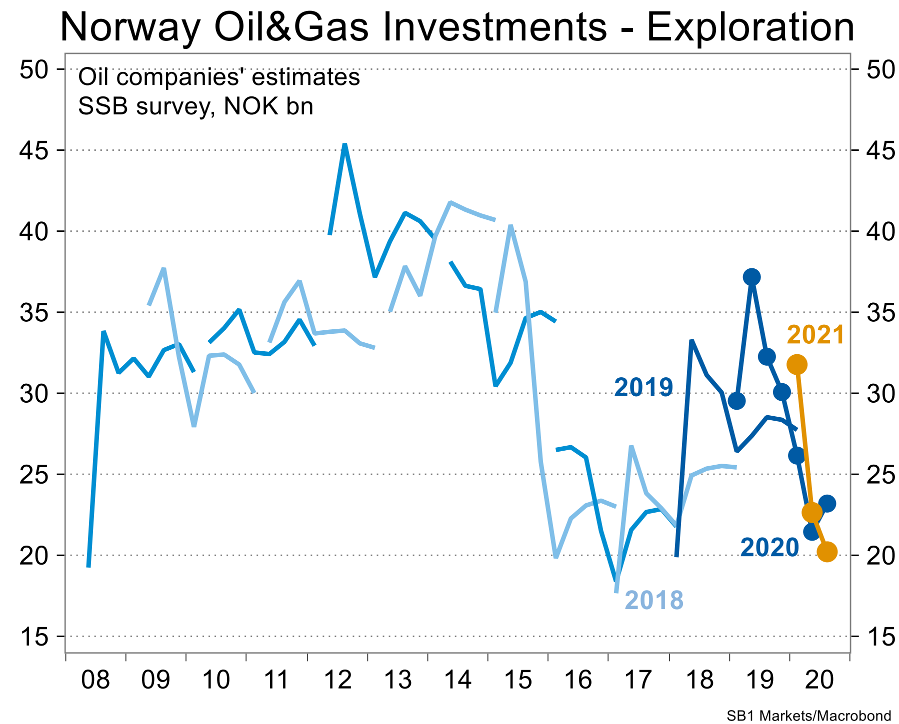


- In SSB’s Q3 oil & gas investment survey, companies adjusted their **2020 investment f’cast** up by NOK 4 bn to 184 bn, following the NOK 5 bn cut in the Q2 forecast. The recent estimate is 2% above the equivalent 2019 f’cast. We expect a 1% decrease in volume terms (up from our -6% May forecast) when books are closed). Norges
  - » As investments grew fast through 2019, a 1% decline implies a sharp reduction through 2020, by some 10%
- **The 2021 estimate was revised up by** NOK 3 bn to 149 bn. The estimate is 15% below the equivalent 2020 estimate one year ago, vs -16% in the Q2 survey. The upward revision was smaller than average to Q3 from Q2.
  - » We estimate a 13% decline in volume terms in 2021 (vs -17% in May). Norges Bank expected a 10% decline in the June MPR. Our estimate implies a decline in investments by some 15% through 2021
  - » We are uncertain how many project will be added even if the tax regime is changed. However, the recent doubling of the oil price could turn out to be more important
- **Oil companies have not changed their forecast materially from before corona**. As Johan Sverdrup was finished, a substantial decline in investments was signalled long time ago. We have now entered a new downward cycle in the oil industry

Field investment estimates are nudged up, but will decline in sharply in '21

In addition, exploration investments are slashed, more than lower rig rates may explain



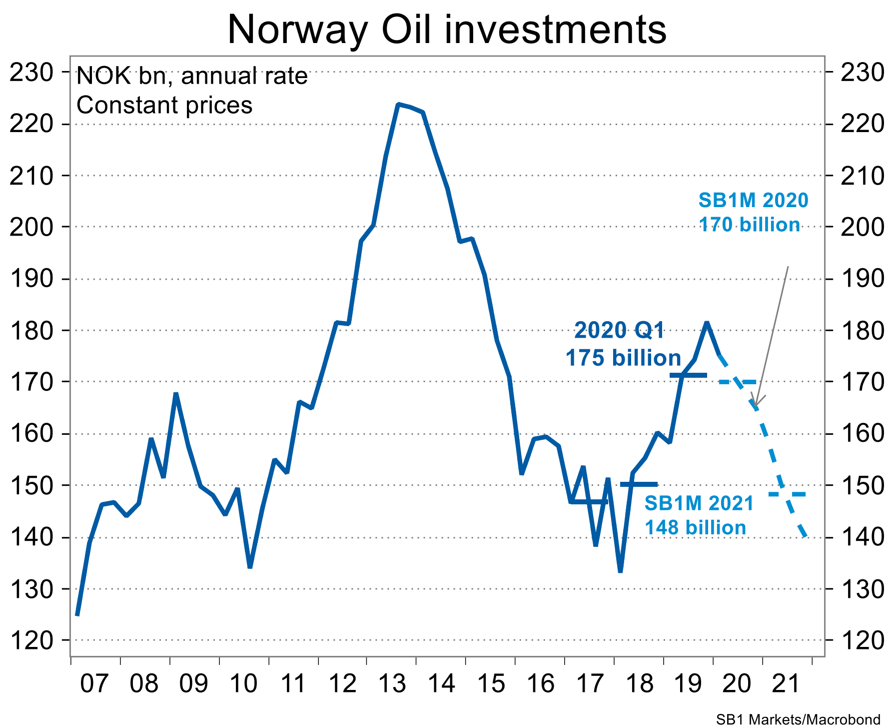


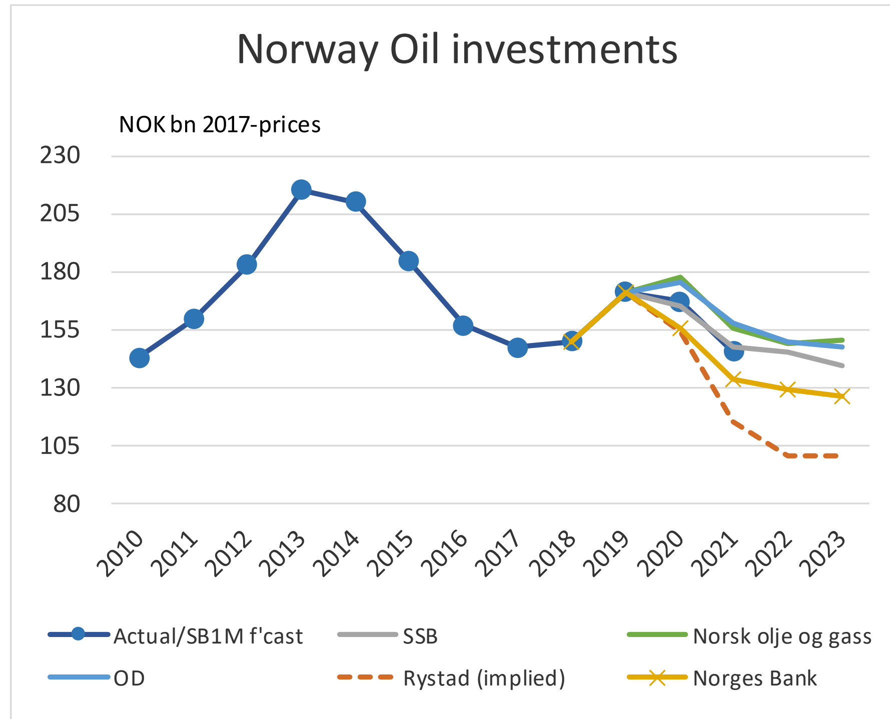
- One new PDO (plan for development and operation) is included in the Q3 survey. Next year, another rather large project will be included but investments in 2021 are quite limited. Other projects may be added too
- F'casts for 2020 investments in **existing fields** are 7% above the equivalent 2019 f'cast, while the 2021 f'cast suggest at least 5% decline vs 2020. 2020 **investments in field developments (new fields)** are close to flat vs the 2019 f'cast. The 2021 f'cast is almost 40% below the 2020 f'cast as Johan Sverdrup investments are completed
- 2020 **exploration investments** have been cut dramatically in the previous surveys but rose marginally in Q3 – still down 15%, and a further decline is signalled in 2021. Not a signal of strength vs. investments in field development the coming years

SpareBank 1 MARKETS

A crucial growth engine has changed sign

Our annual forecasts imply a 12% decline <u>through</u> both 2020 and ’21. Still not at bad as during ’14-’17

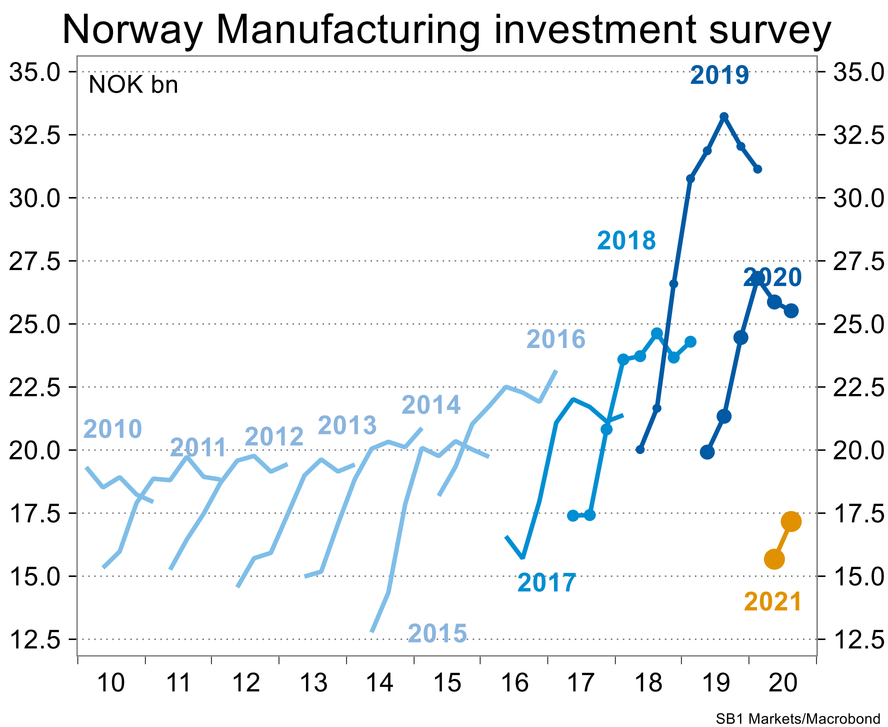


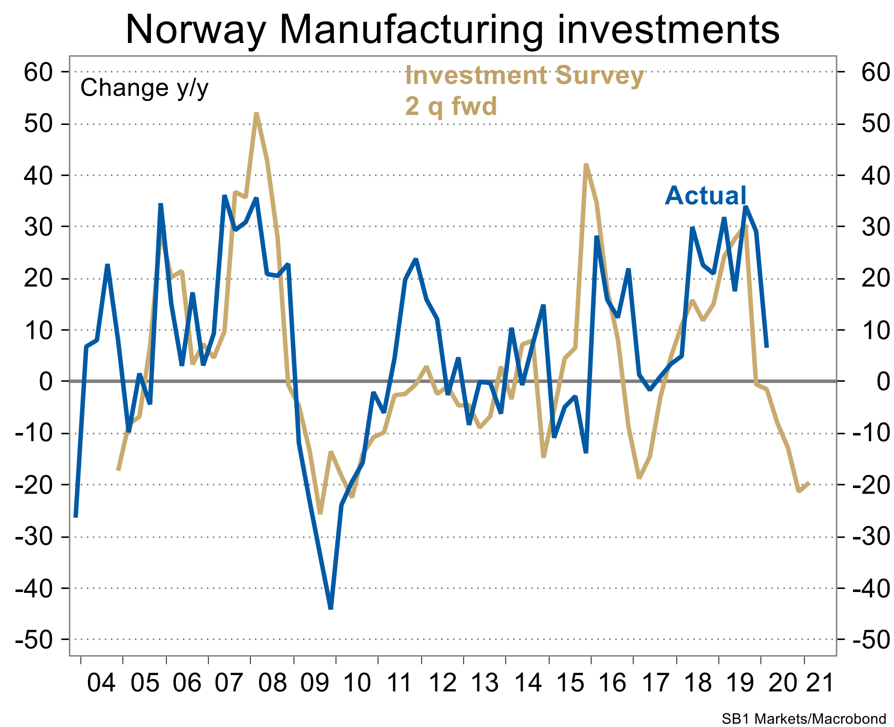


- 3 months ago, we expected a 16% decline through both years, now revised to -16%
- We expect a substantial decline in oil and gas investments during the next quarters. Our estimate is marginally below NoBa’s June estimate but well above Rystad’s (implied) forecast (based on North Sea, USD forecast)

Manufacturing investments down 20% in 2020, another 15 - 20% in 2021

2019 investments were far above a normal level, 2021 will probably be below



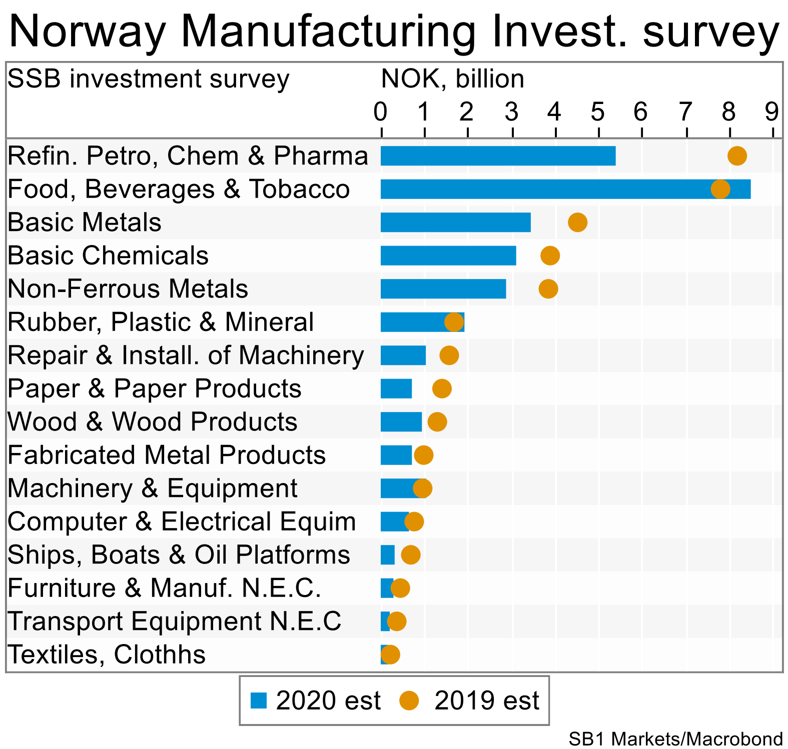


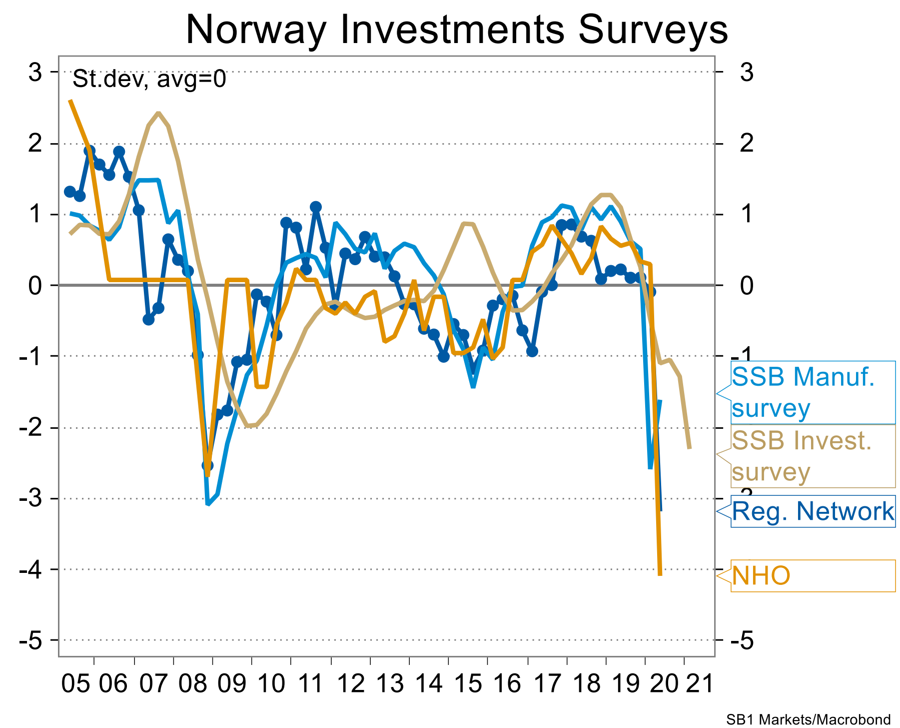
- Manufacturing companies adjusted their 2020 investment marginally down in Q3, and the estimate is now 20% below the equivalent 2019 estimate from Q3 last year. The 2020 downturn was signalled before corona
- The second 2021 estimate implies another 15 – 20 % decline, but the uncertainty is of course larger than for the 2020 estimate
  - » Investments in refined petro., chemicals and metals are the major drags in 2020, after soaring in 2019

SpareBank 1 MARKETS

The boost from refined petro, metals & chemicals will reverse

2020 f'casts have been nudged down vs the '19 f'casts in most sectors. Other surveys confirm



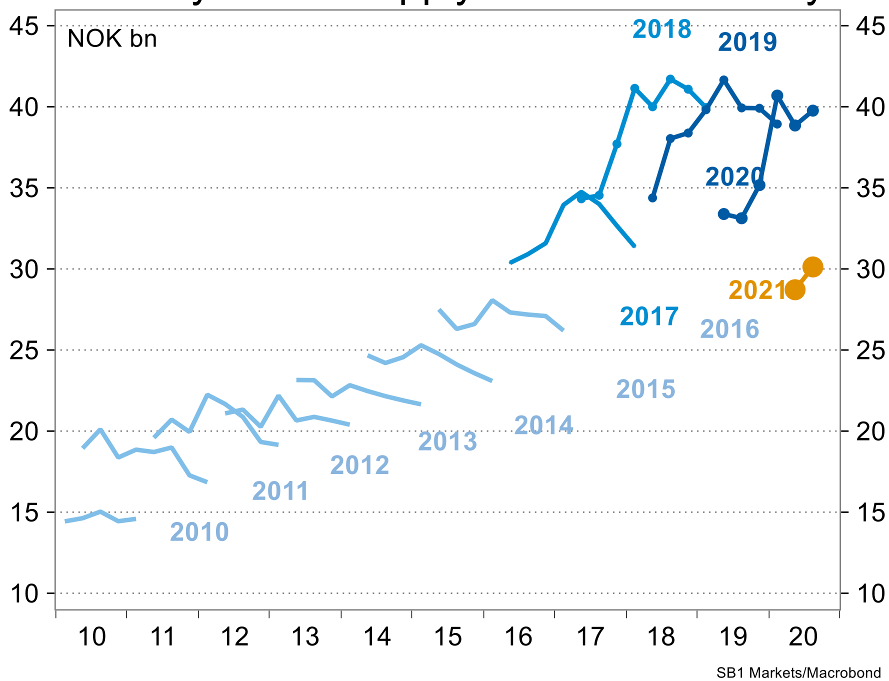


- In late 2018 and early 2019, the SSB manuf. investment survey was much more upbeat than other surveys (and it was right, as usual). Now, however, the level is far weaker. Other surveys confirm deep investment cuts

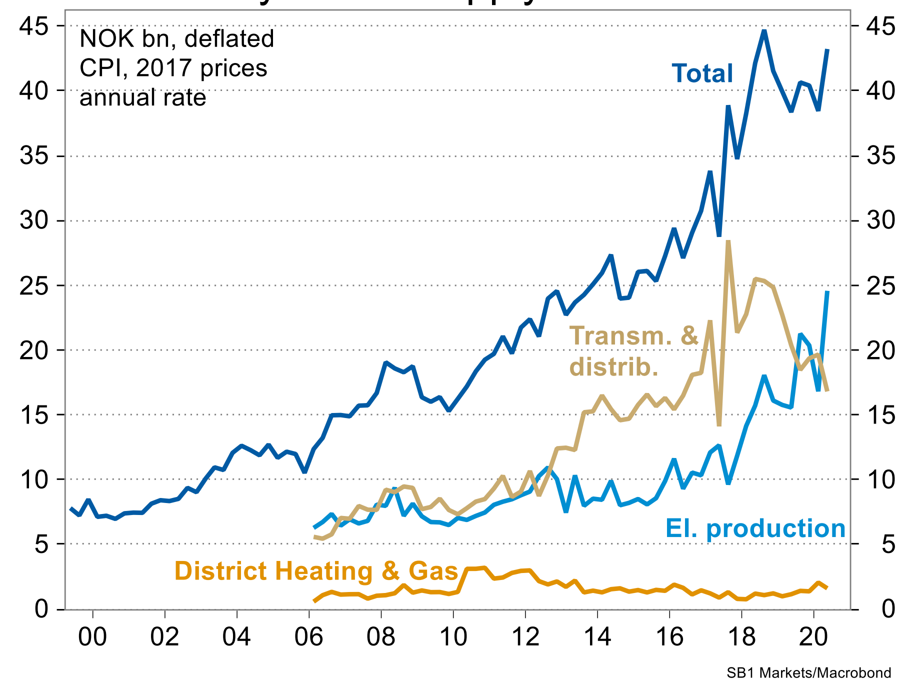
Power supply: Investments are peaking now

The 2020 estimate was better than we assumed but the 2021 decline is confirmed – down 10%?

Norway Power supply investment survey



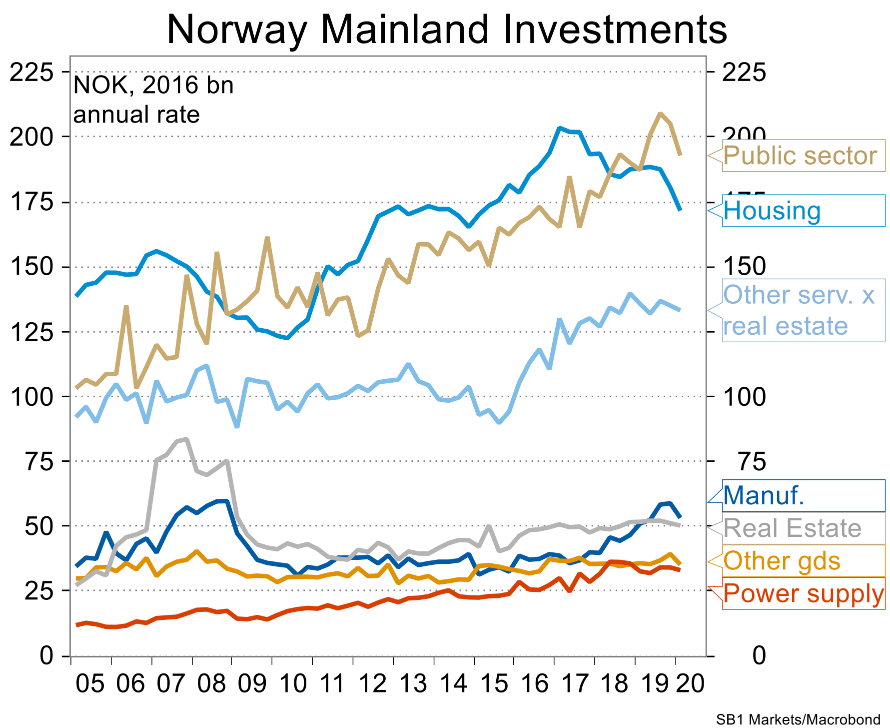
Norway Power supply investments

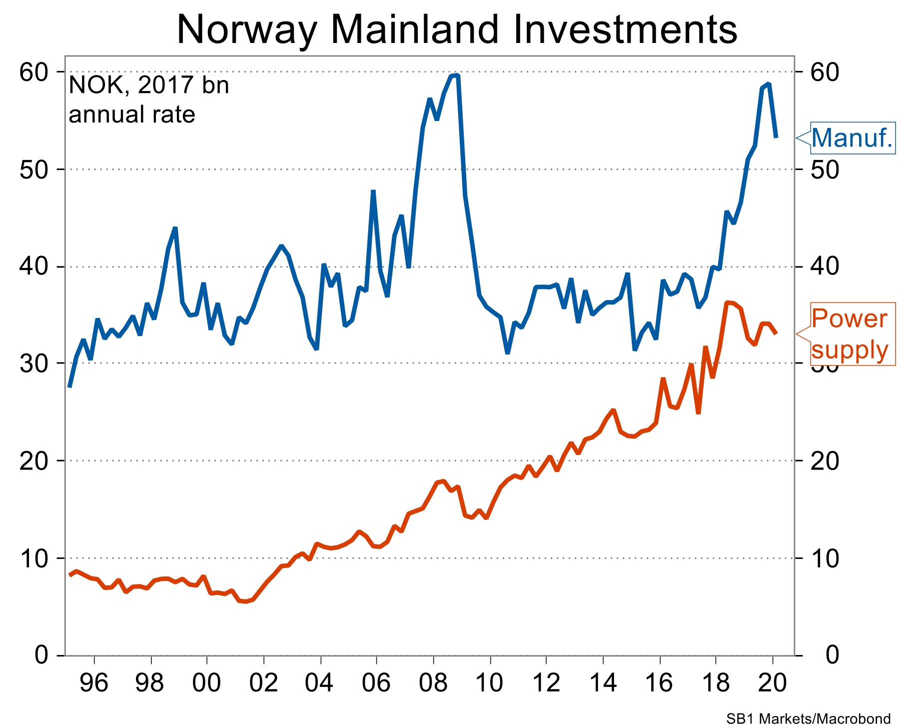


- Power supply (production & distribution) companies revised their 2020 investment f'cast map marginally in Q3, at a time of the year where investments normally are revised down. The 2020 estimate is now on par with the equivalent 2019 estimate, at NOK 40 bp, up from -7% in the May forecasts
- The second 2021 estimate is down 9% vs. the equivalent 2020 estimate, up from -14% in May. More projects may be added the coming quarters but a significant decline vs. 2020 is no very likely
- Investments have more than quadrupled in 25 years, more than 10% p.a in average. The investment level as % of Mainland GDP has been running at or just above 1%, the highest in decades. Investments in transmission and distribution has fallen the most

Power supply investments have peaked, manuf. investments peaking now

The each equal 1 - 2% of Mainland GDP and 5 – 8 of total Mainland investments (private/public)

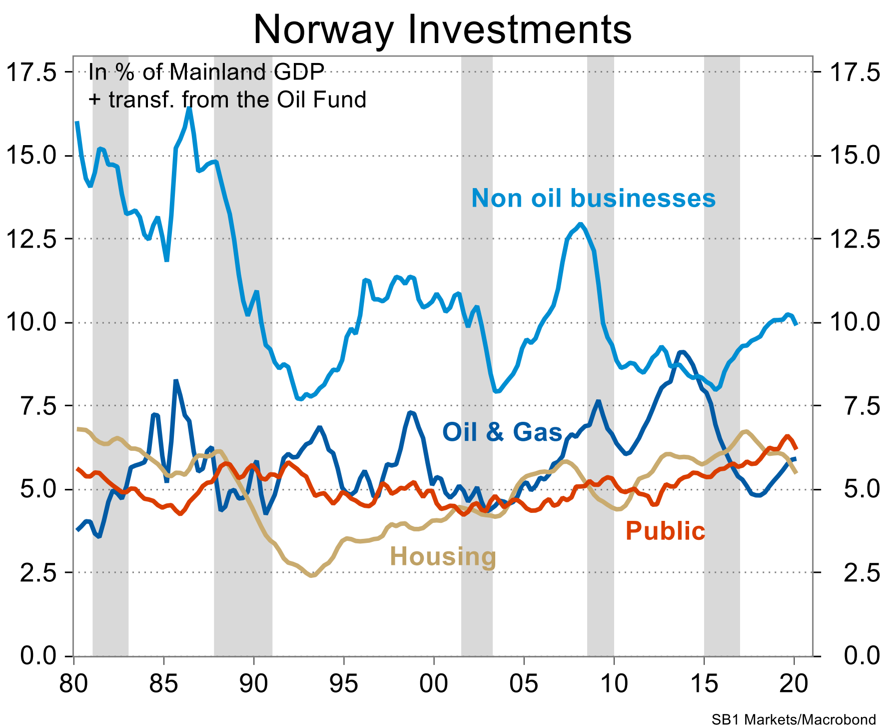




- In volume terms, investments in the manufacturing have accelerated sharply the past two years, but companies are signalling a sharp decline in 2020. Investments in power supply flattened in 2019 and is heading down, at least in 2020
  - Real estate investments and investments in other private services are the main components in Mainland business investments – and they are still at rather high levels
- The outlook for Mainland investments is not upbeat, given the expected drop in investments in manufacturing and the modest decline power supply - and probably a limited upside on real estate investments, as housing starts are slowing. The public sector cannot continue to climb for a long time either? Check the next slide for more

The investment cycles: A broad slowdown the coming quarters?

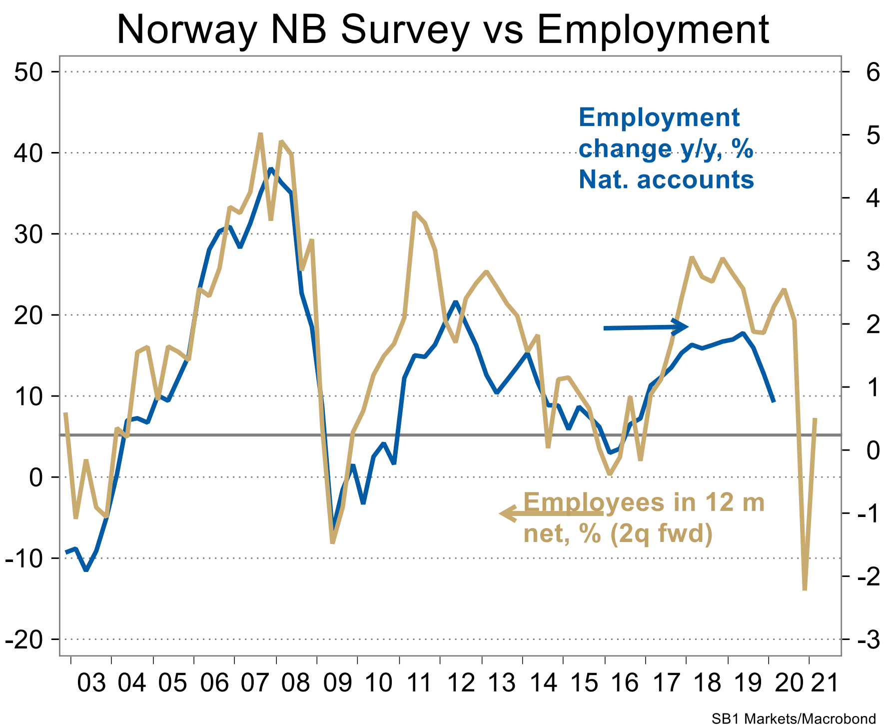
Business investments – on and offshore – peaked in Q4 – and will decline substantially

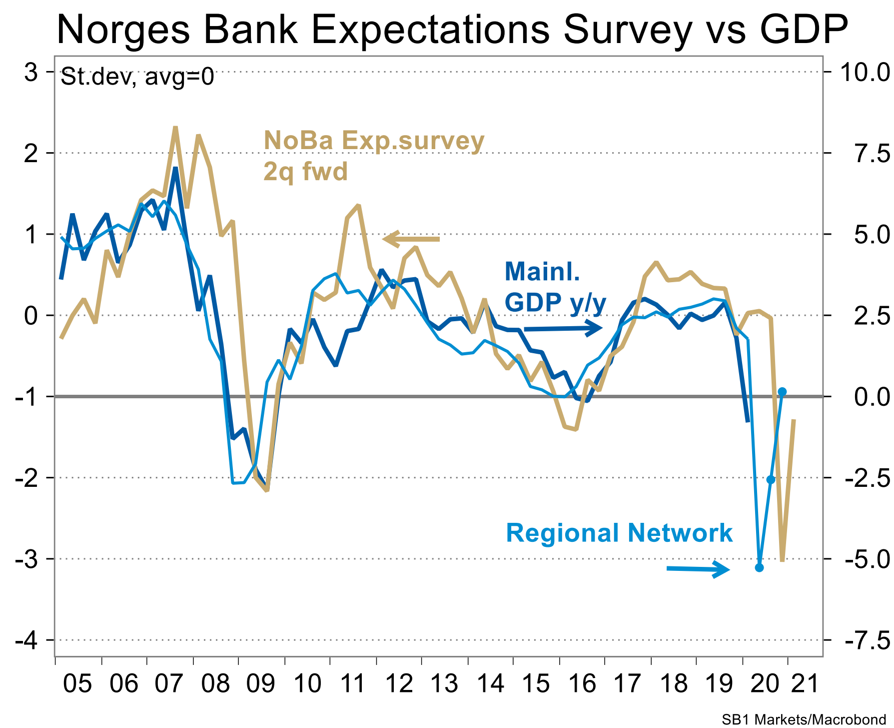


- **Oil investments** recovered until the peak in Q4 2019 – and is now heading down
- **Mainland businesses** have increased their investments sharply since ’16. Investments peaked in Q4 19. the level is not low anymore. They are probably at peak, too, as manufacturing and power supply investments are set to decline, and the upside on service investments is probably limited
- **Government investments** are the highest in decades, vs GDP. Will come down long term, but limited downside short term
- **Housing investments** have been sliding down since 2017 but remains at a rather high level, at least vs a 40 year history

NoBa Expectation survey: A 'V' confirmed. But how firm is the second leg??

Following the steep Q2 decline, companies are not reporting impressive growth expectations

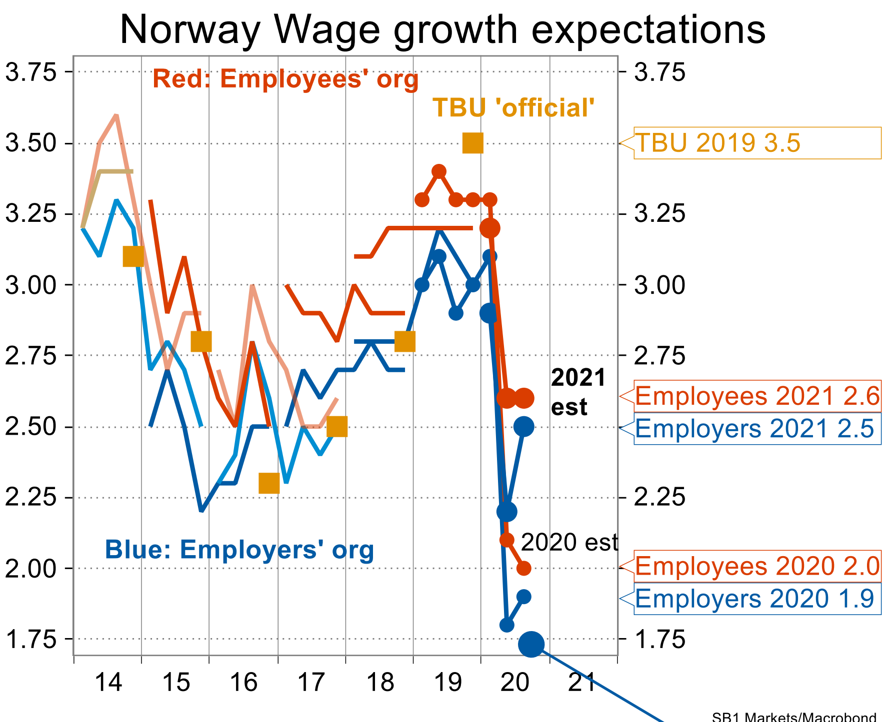




- Companies are just reporting stabilisation in employment and profits – but formally that's from a very low level in Q2.
  - » We think companies are not able to calibrate their answers because the starting point is so low. They are not reporting expected changes, which they are asked to but rather (at least an element) of an assessment of the expected level. The PMI surveys are experiences the same mismeasurements these days
- We expect something much better than zero growth the coming 12 months. Zero would really be a disaster!

Wage expectations converged to 2% in 2020, and to 2.5% in 2021

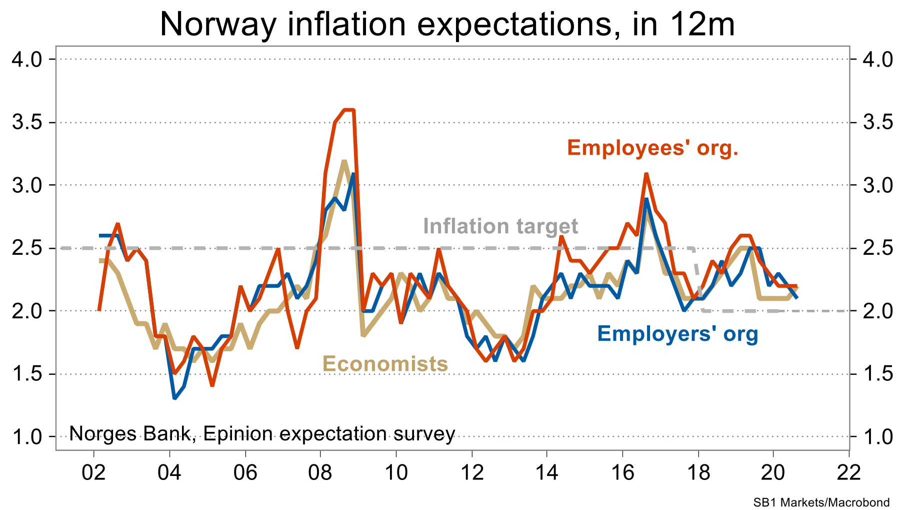
Economists in employers' organisations moved their expectations up, especially for 2021

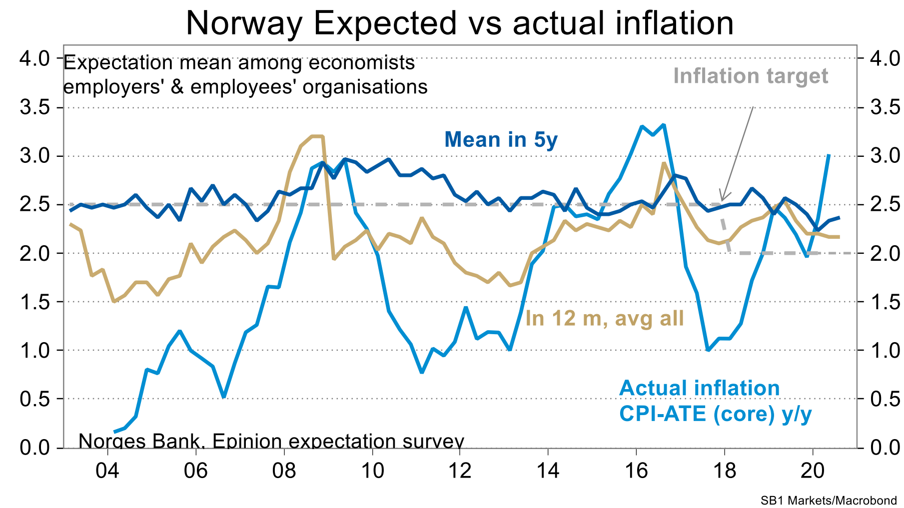


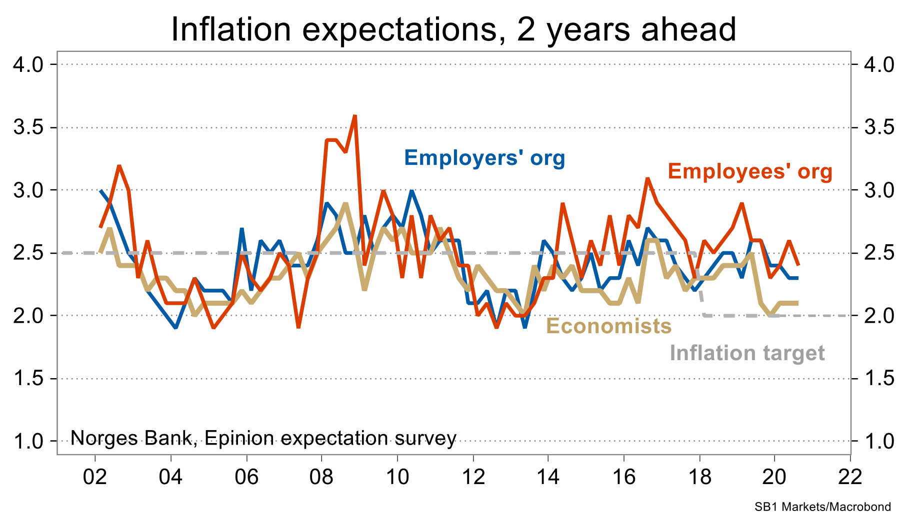
- **2019:** Wages increased by 3.5%, according to the TBU report (revised up from 3.4%)
  - » The outcome is well above both economists in both employers' and employees' organisations expected by the end of 2019 (3.2% and 3% resp.)
- **2020:** A huge 'cut' in Q2, by more than 1 pp, small changes in Q3 – a compromise at 2%?
  - » Economists in employers' organisations lifted their forecast by 0.1 p to 1.9%. In trade unions, 0.1 pp down to 2%. If if was up to the economists, they should be able to strike a deal?
  - » In general, employees' org expects higher wage growth than their peers at the employer side, as one should expect
- **2021:** Employers' economists yield, they lifted their forecast by 0.3 pp to 2.5%. In unions, no change – at 2.6%
- In the June MPR, Norges Bank expected 1.9% wage inflation in 2020, and 2.0% in 2021 – and the 2021 will very likely be revised up in the Sept. MPR
- At Friday, a 1.7% wage lift in 2020 was agreed upon, of which 1.2 pp is due to carry-over wage increases during 2019

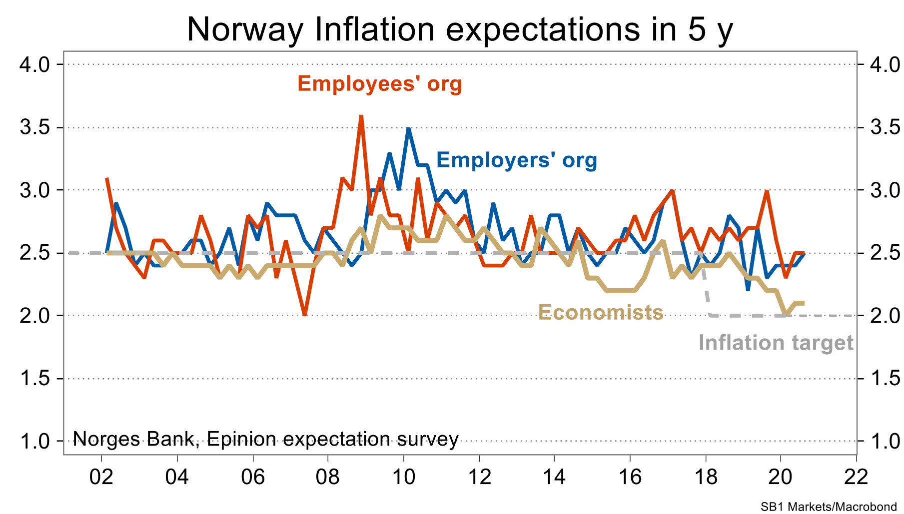
Inflation expectations unmoved by the corona crisis

Expectations stable at 2 - 2.5% (the lowering of target to 2% from 2.5% impressed just the economists)









Highlights

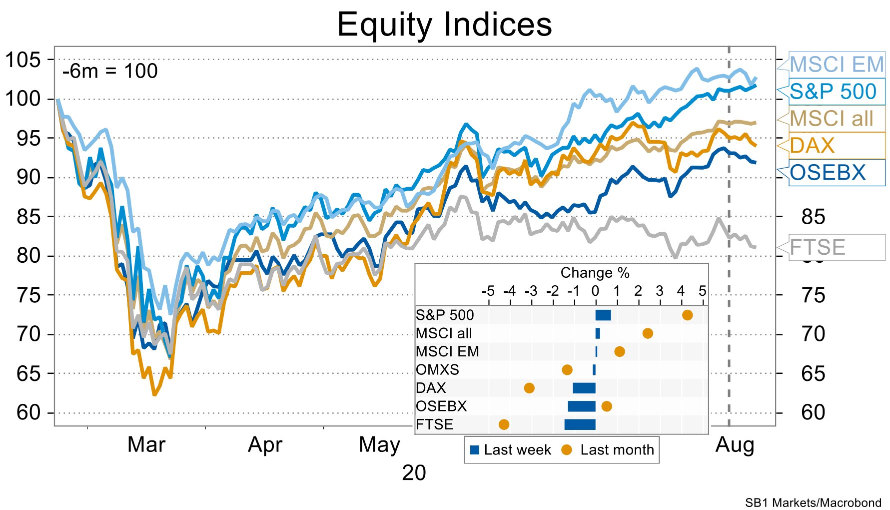
The world around us

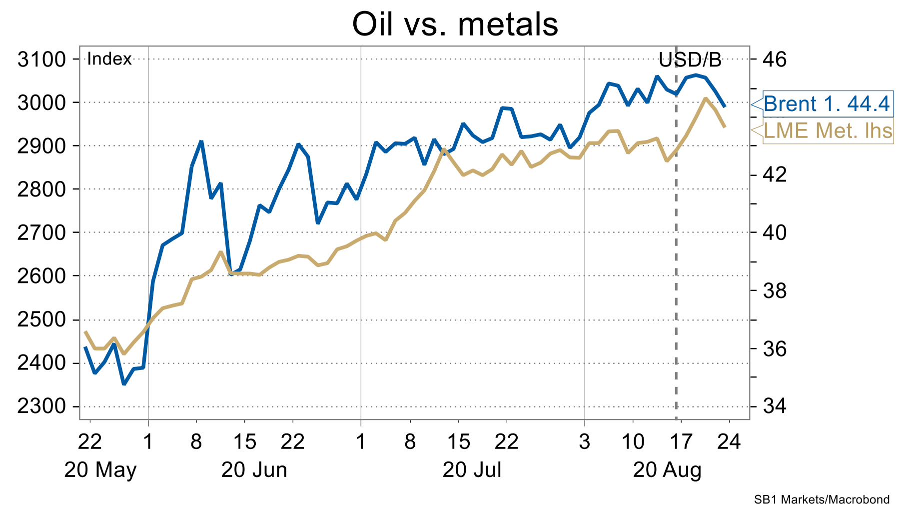
The Norwegian economy

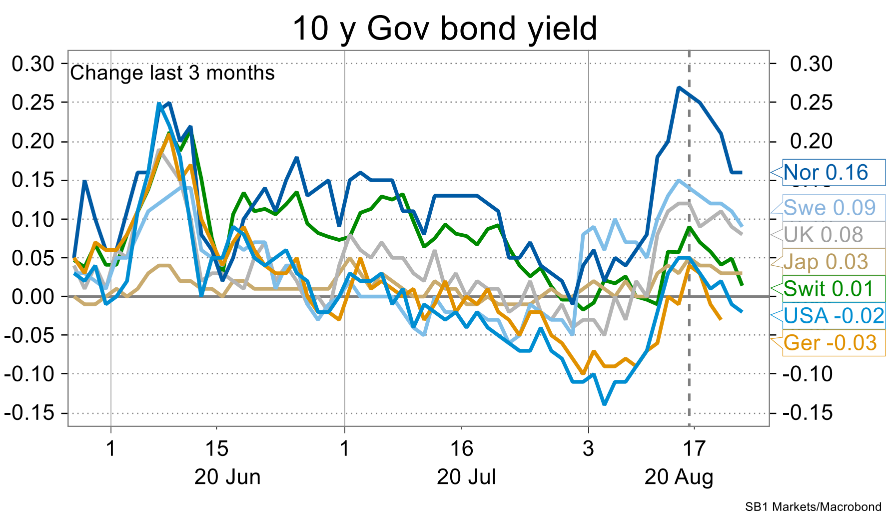
Market charts & comments

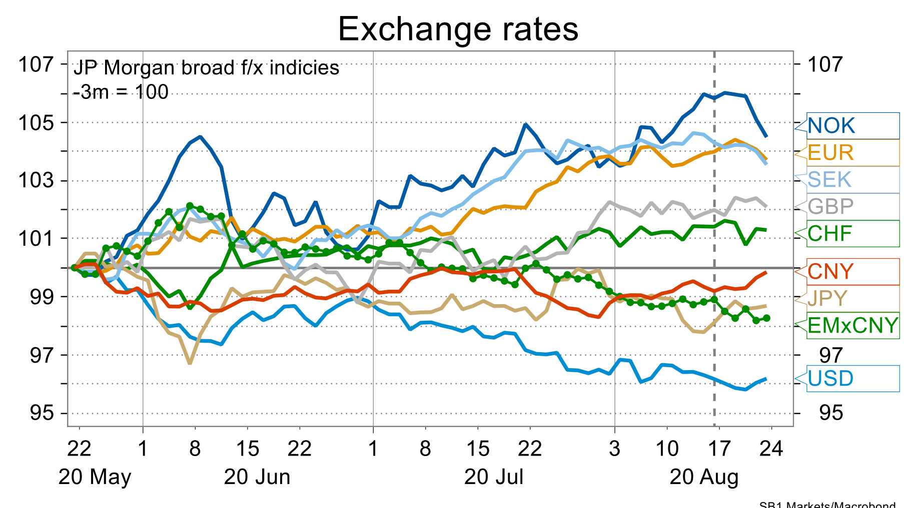
S&P500 up to ATH; oil & NOK down, bond yields down too

Some of the hike in bond yields reversed last week but all up from the bottom







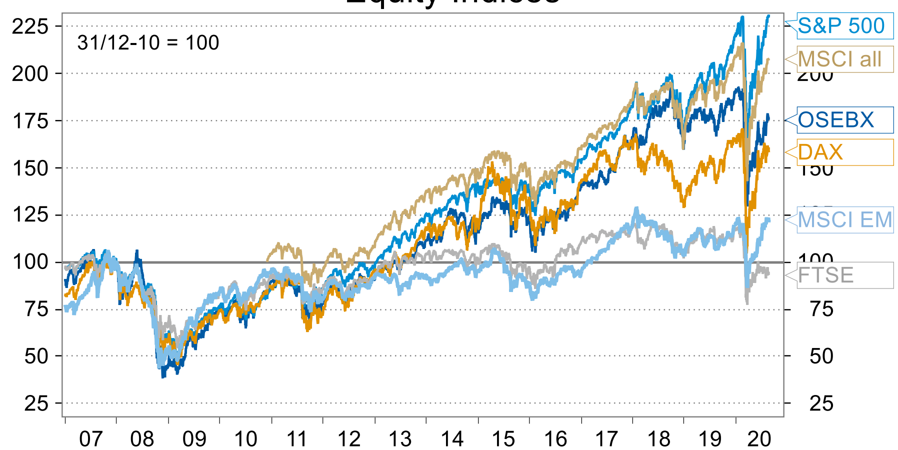


The USD has been the laggard since mid May, and was just flat last week Still just as strong a before the corona crisis. NOK lost last week, and more than the oil price usually explains. Something else going on??

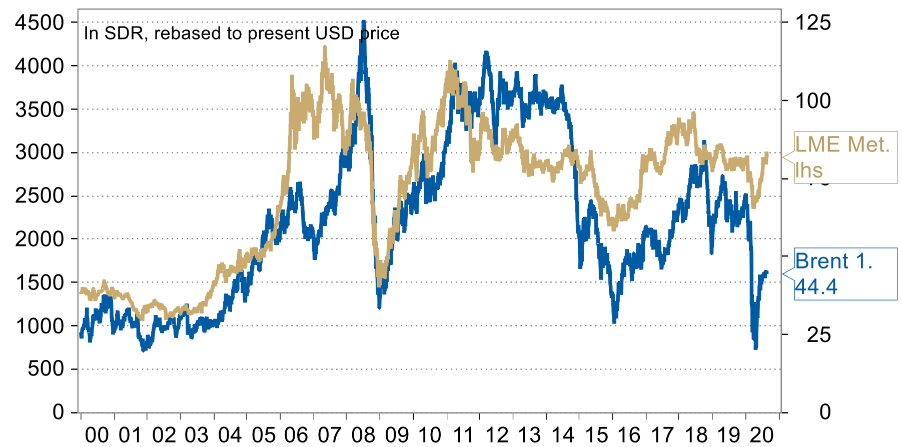
In the long run: Stock markets are looking like a 'V'

… because investors are looking for a 'V'-shaped corona recovery? Oil, metals up too. Bond yields not

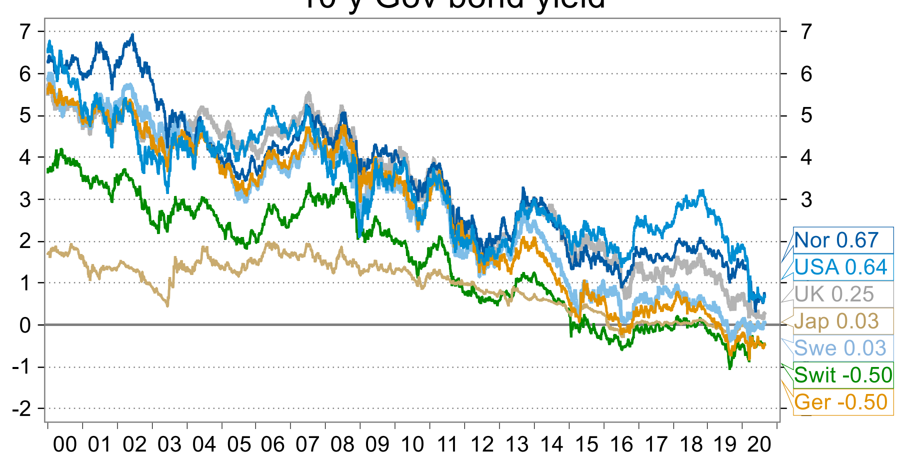
Equity Indices



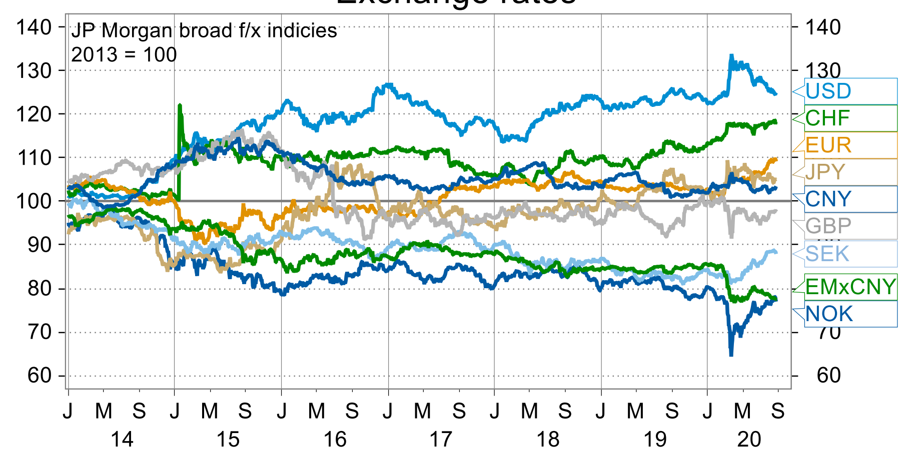
Oil vs. metals



10 y Gov bond yield



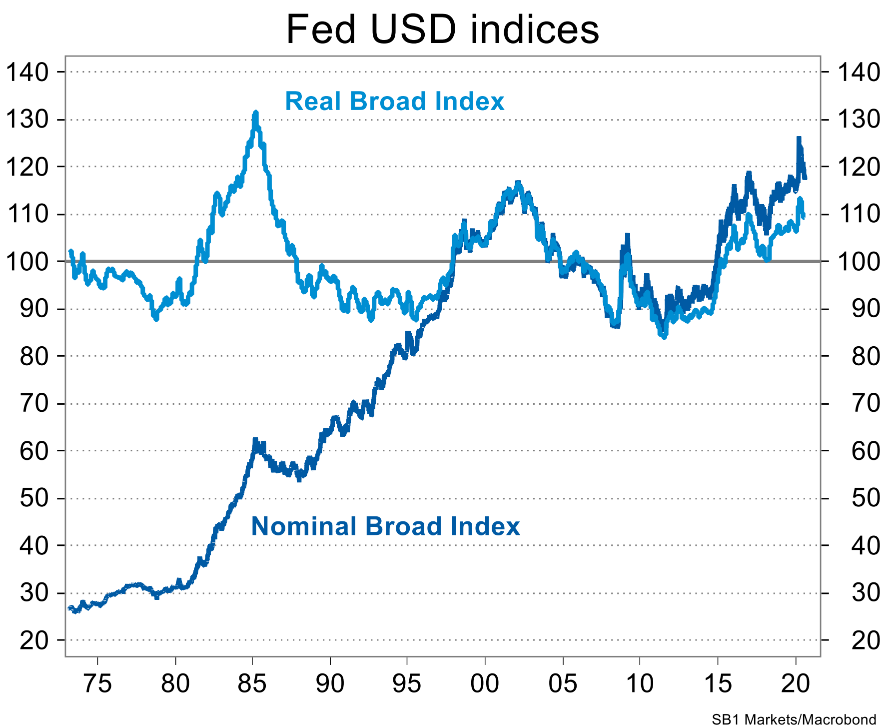
Exchange rates

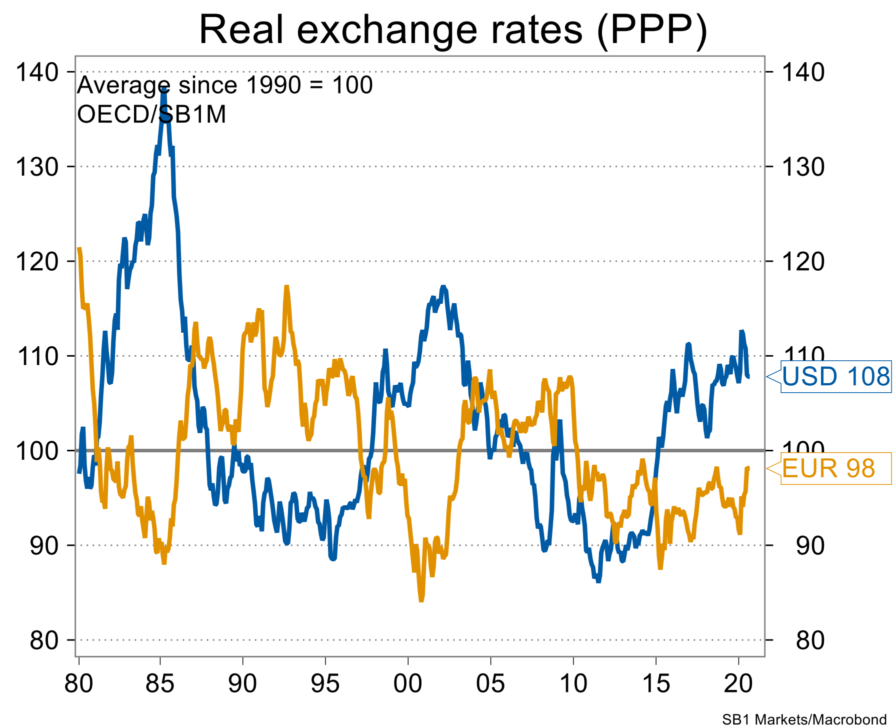


The USD is down but still stronger than in February – and over the previous years (measured by broad f/x indices)

Sure, the USD is down – and it may depreciate much more. But so far, *no drama*!

The USD is down some few per cent – but is still far above average levels in PPP terms





- Corona, slowing growth, social unrest, political turbulence, budget deficits (that will become even larger) & money printing, trade deficits, the US China conflict. You name it, there are always reasons for the USD to decline
- Still, measured by broad indices, the USD remains <u>stronger</u> than in February, before the corona crisis unfolded

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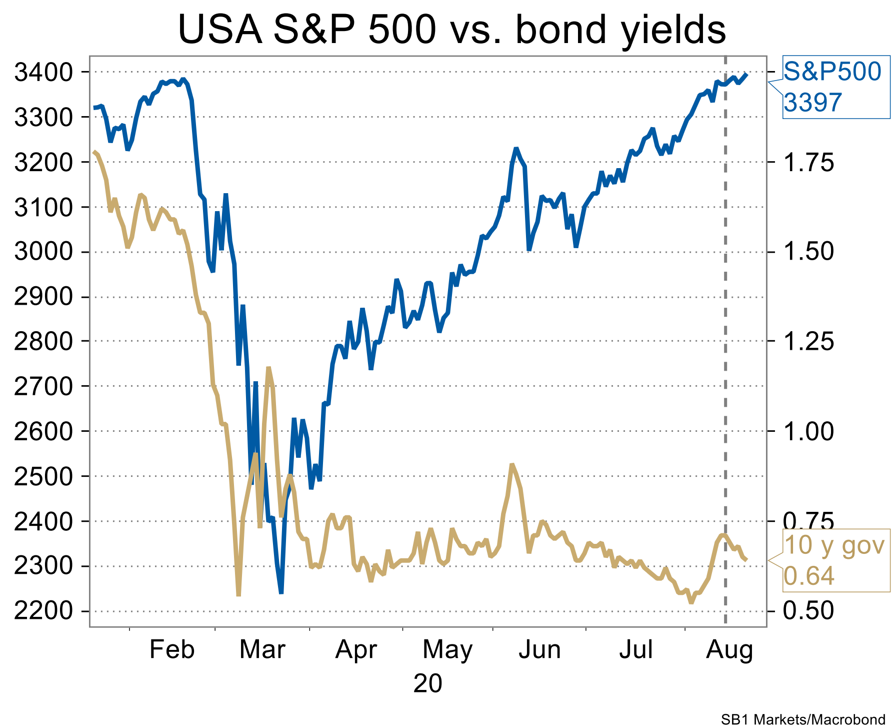
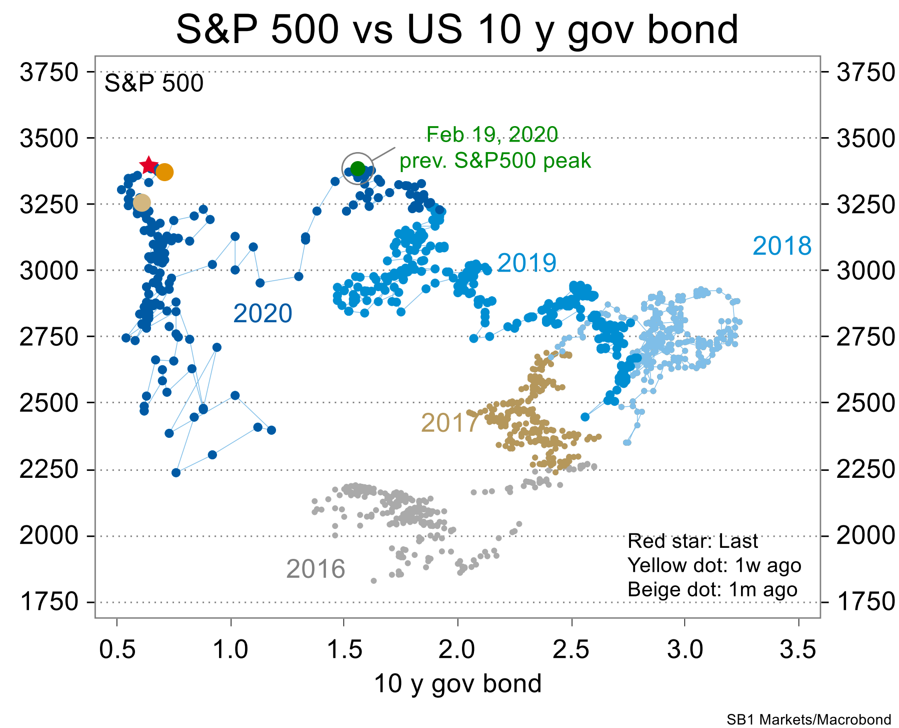
S&P 500 up to a new ATH, bond yields are down 90 bps since last time, in Feb

The run since the March trough has been remarkable, equities are up 50%





- Mixed economic data were good enough even if the Fed signalled caution on the economic outlook in the minutes from the last FOMC meeting
- Bond yields fell last week, down 7 bps to 0.64%

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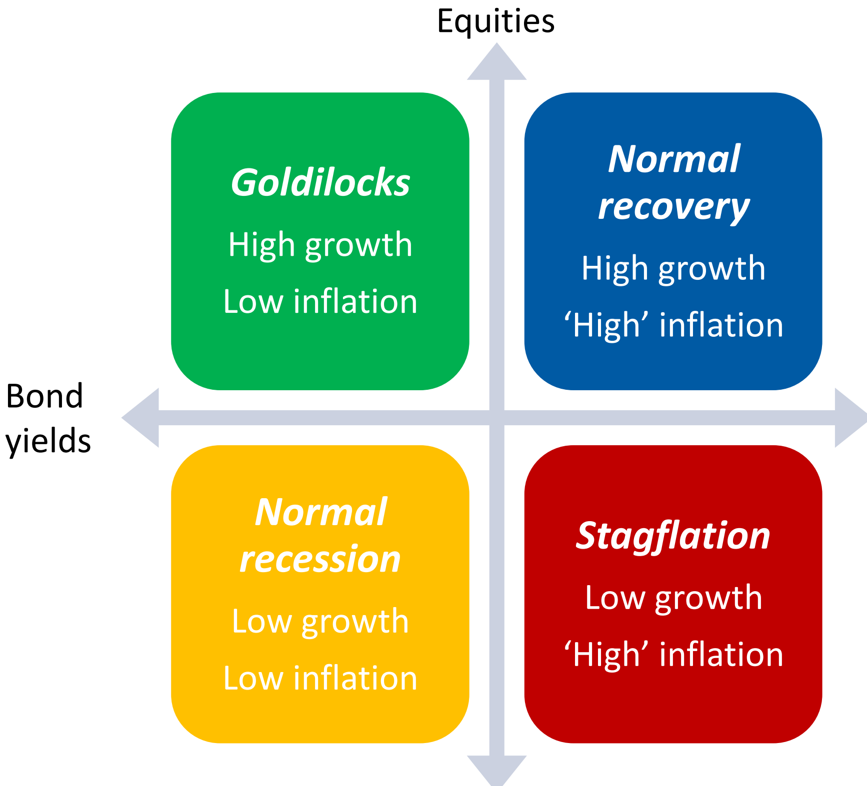
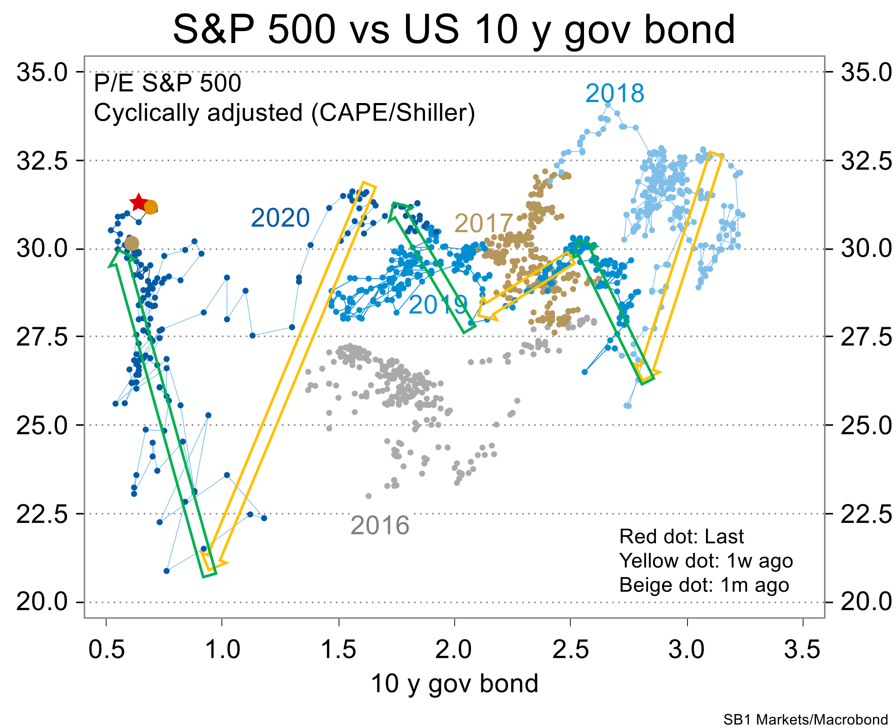
Until two weeks ago: Towards the Goldilocks corner

Finally, bond yields rose visibly amid OK growth data – and an inflation uptick. Stock still further up

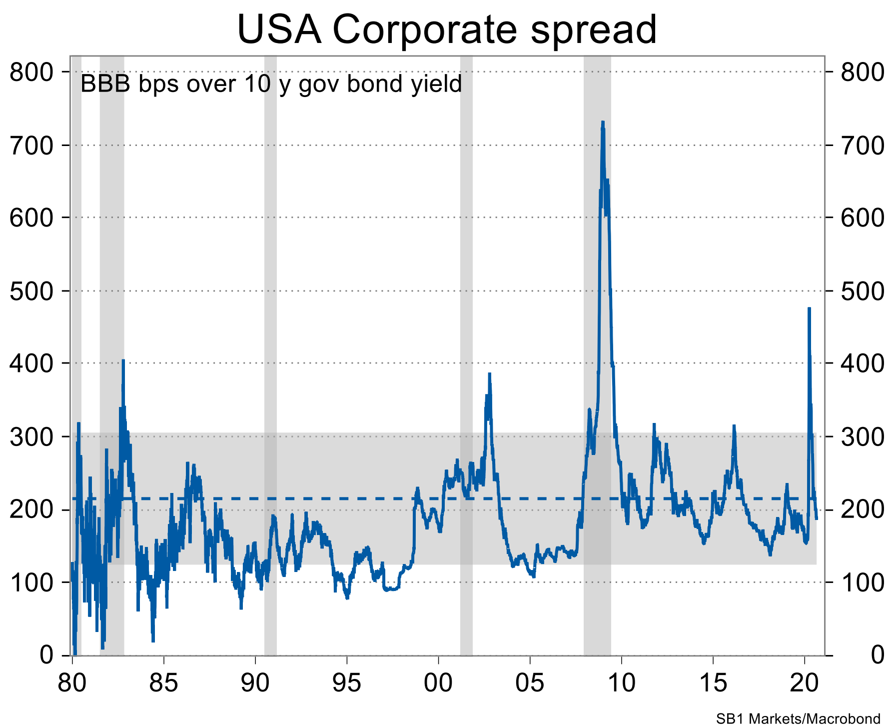


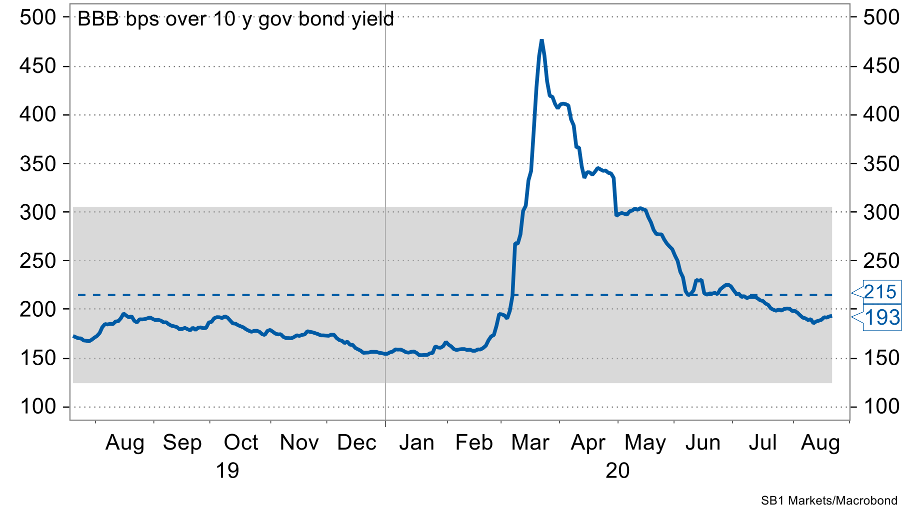


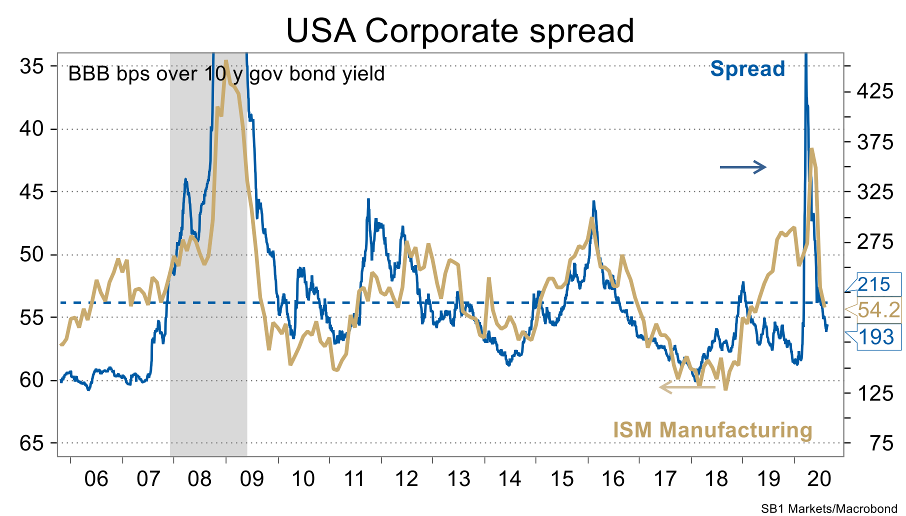
- Has the '**Goldilocks'** travel (towards the green corner) come to an end? May a continued economic recovery, and a normalisation of actual and expected inflation (which both has taken place over the past weeks/months) dampen expectations of an 'eternal' extreme monetary policy (negative real bond yields, even measured forward based, for more than 10 years? Bond yields would increase but not no much that it led to a crash in the stock market a move towards the '**Normal recovery**' (blue) corner. Such a shift has been one of our two most likely scenarios – the other was in the opposite direction, towards the '**Normal recession'** (yellow) corner, falling yields & risk markets.
- We are still not worried for the falling into the '**Stagflation trap**', at least not permanently. Inflation (and interest rates) will <u>not</u> climb if the economy weakens again from here - inflation will decline, and rates will remain low. However, given the 80 bps decline in 10y US treasuries since February, and the equity market flat, a short term correction with higher yields and lower stock prices is not that unlikely

Corporate spreads stabilised after falling below an average level

Bond issuances are at record high levels



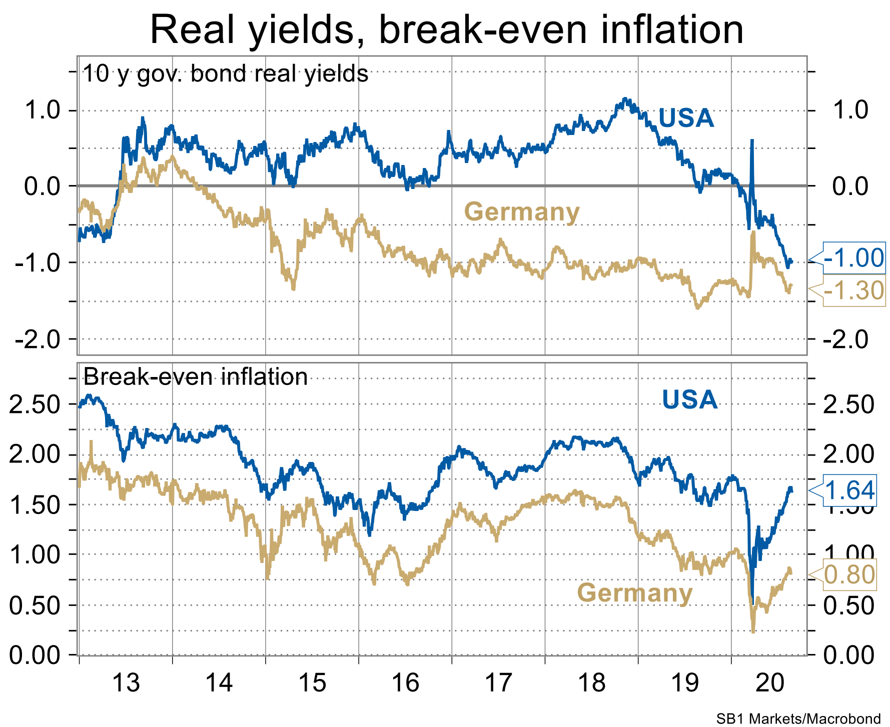


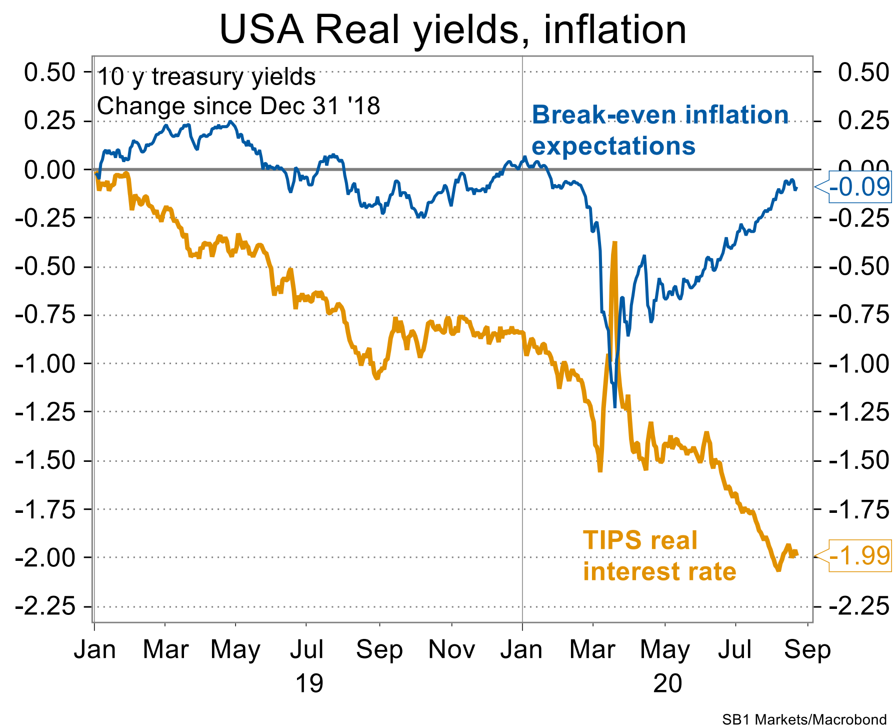


- However, is the credit risk at an average level now??

Inflation expectations down last week – but has been trending up

The 10 y TIPS real rate marginally down but has stabilised past two weeks, at a record low level, -1%



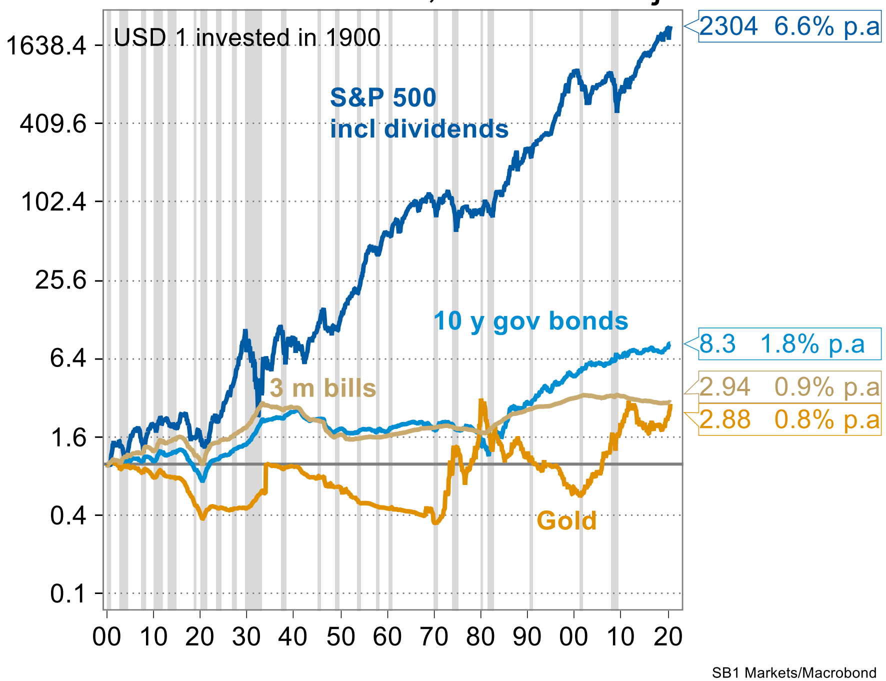


- The implied break even inflation rate have steady been increasing by some 20 bps per month since May – and by 25 bps the past 4 weeks. Now, the implied break even inflation is at 1.64% - and if it continues upward at the same pace for two more months, market's inflation expectations will reach 2% - Fed's inflation target
  - » That's probably one reason for the increase in real rates last week – will the Fed have to conduct an extreme expansionary monetary policy forever, if inflation is not dead?
- In Germany, inflation expectation are on the up too, a tad slower than in the US – and the level is just 0.80%. The real rate at -1.30% - close to record low

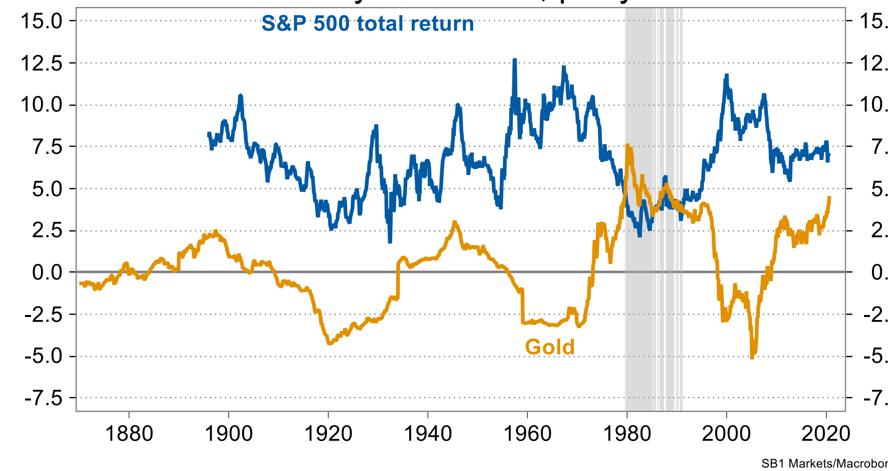
For the gold bugs: A long and a short story

Gold has through the history been a really bad (zero yield) investment. However, from time to time…

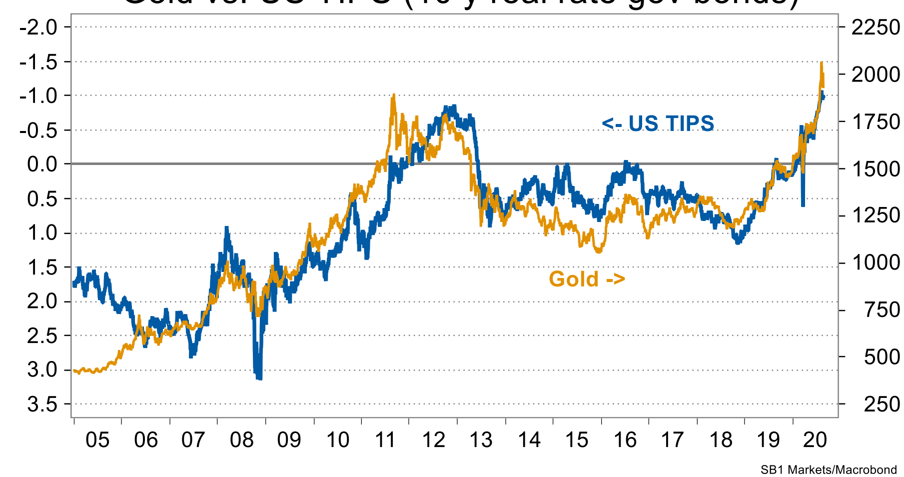
USA Total return, inflation adjusted



USA 25y real return, per year

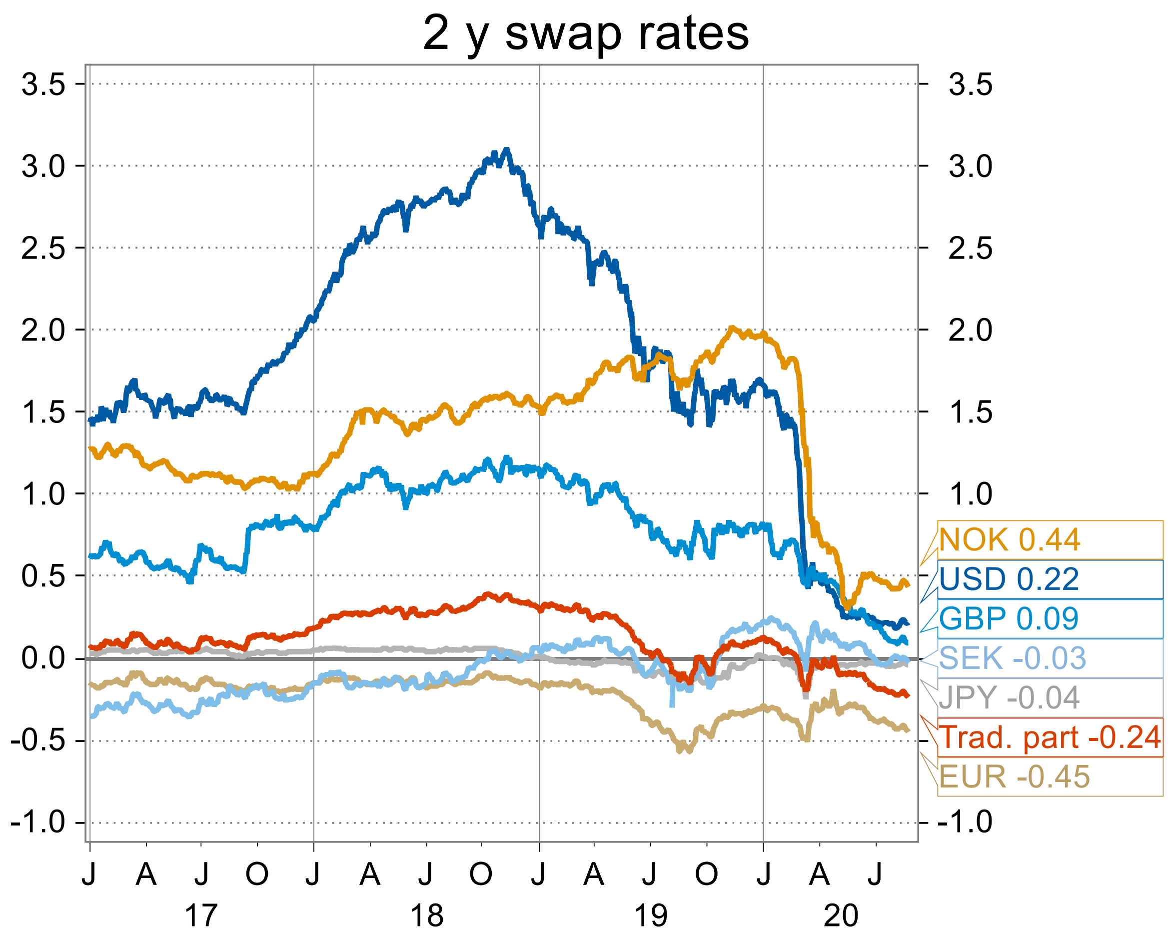


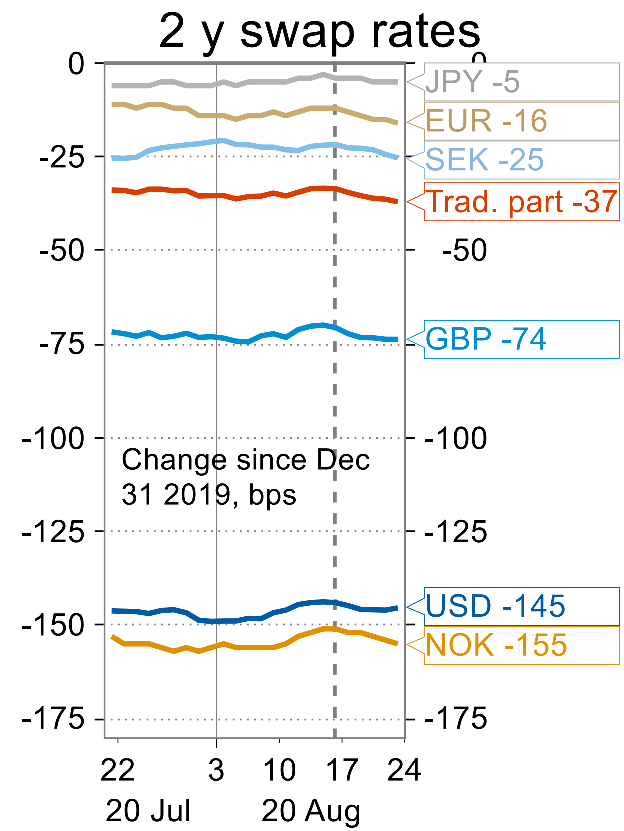
Gold vs. US TIPS (10 y real rate gov bonds)



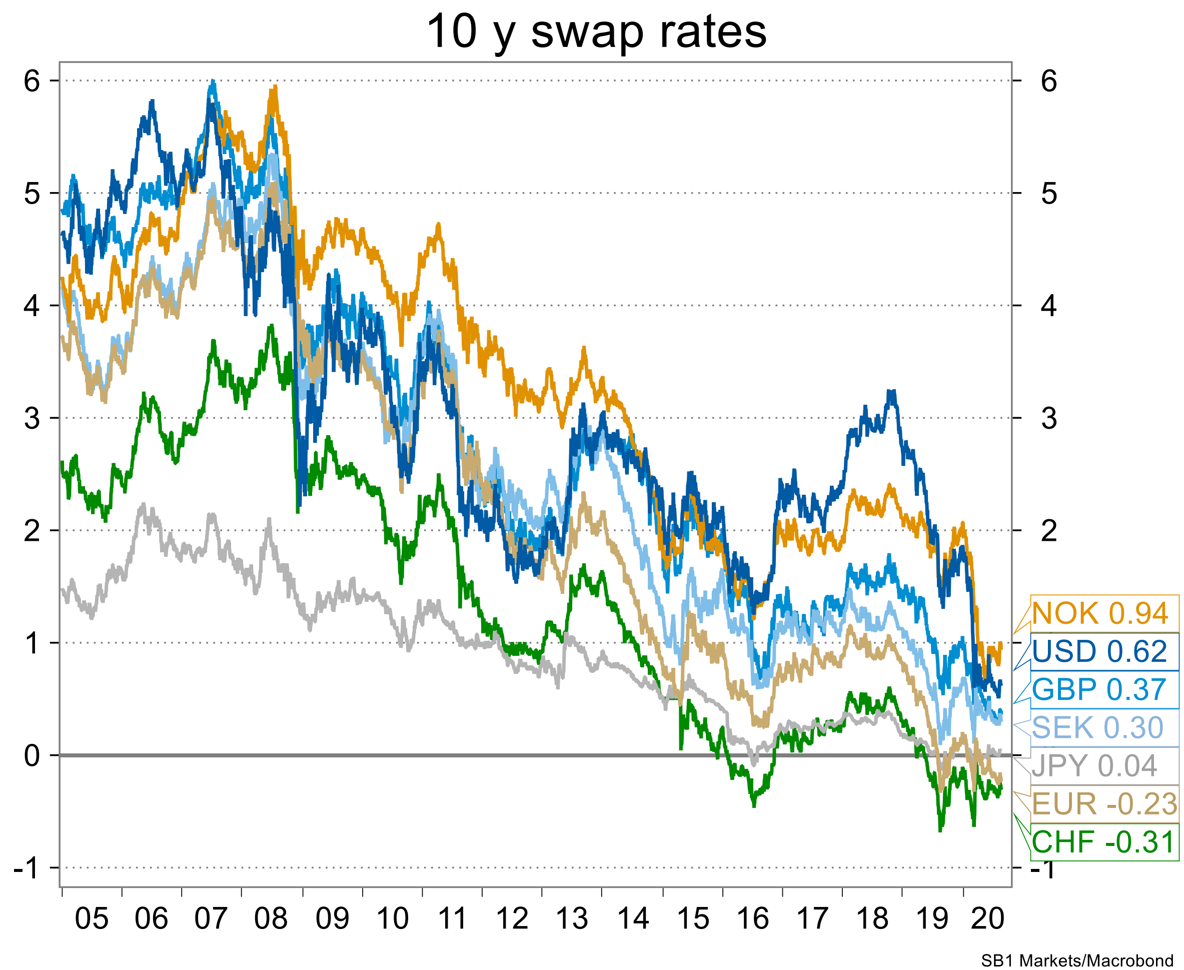
- Like during the past 2½ years when real rates have been tumbling to record low levels
- The past week, real rates rose sharply – and gold fell some few percent
- The long term outlook? We do not know – but long term (and we mean quite long term), gold has normally been a really bad investment, at least compared to equities
  - » The real gold price is still lower than 40 years ago, in 1980. Equities are up 22 times (and 2200 x since 1900. Gold is up 2.9 x)

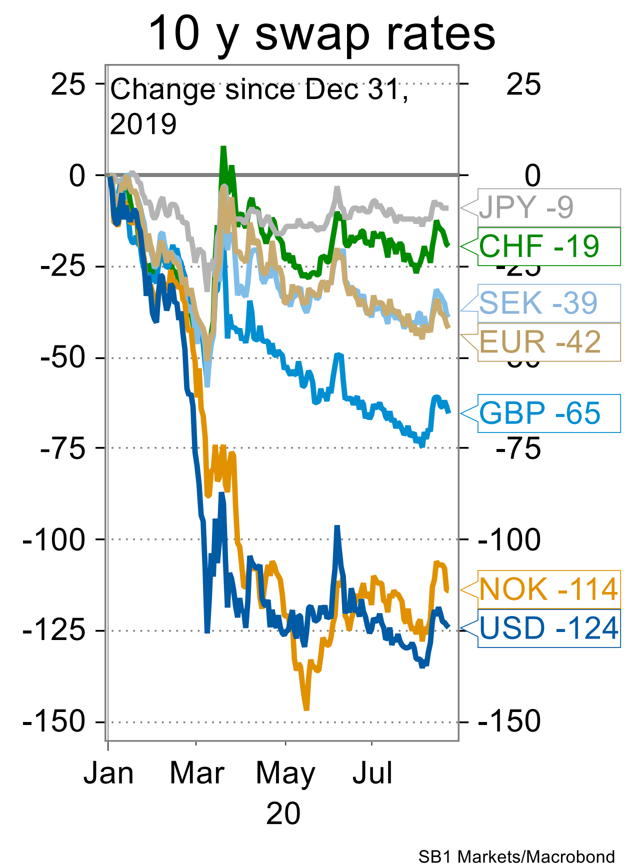
Short term swap rates marginally down, is still trending down





Long term swap rates down, but less the lift the previous week





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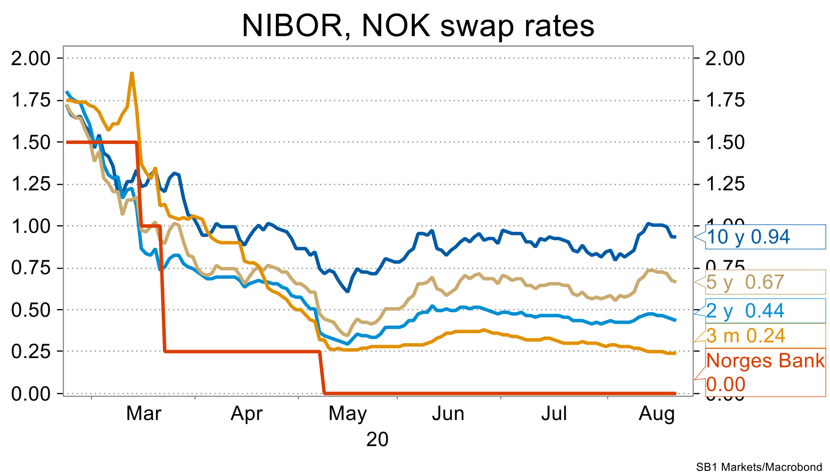
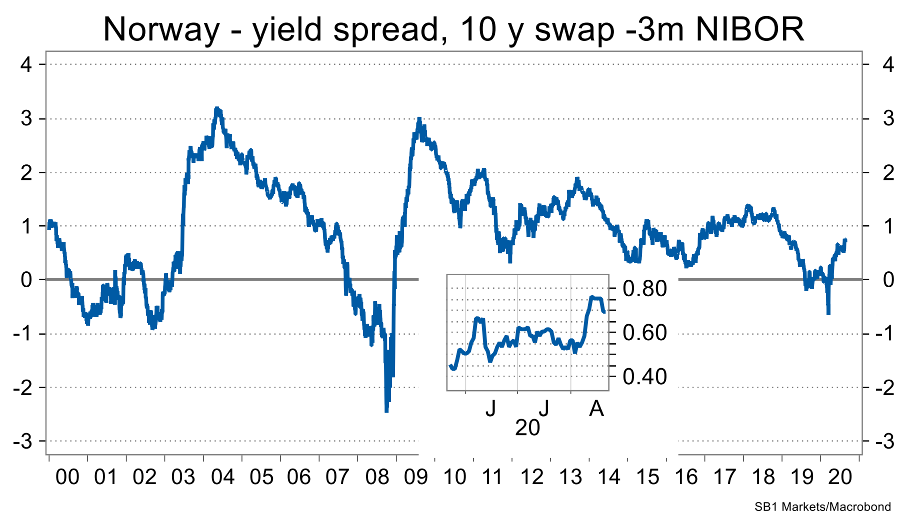
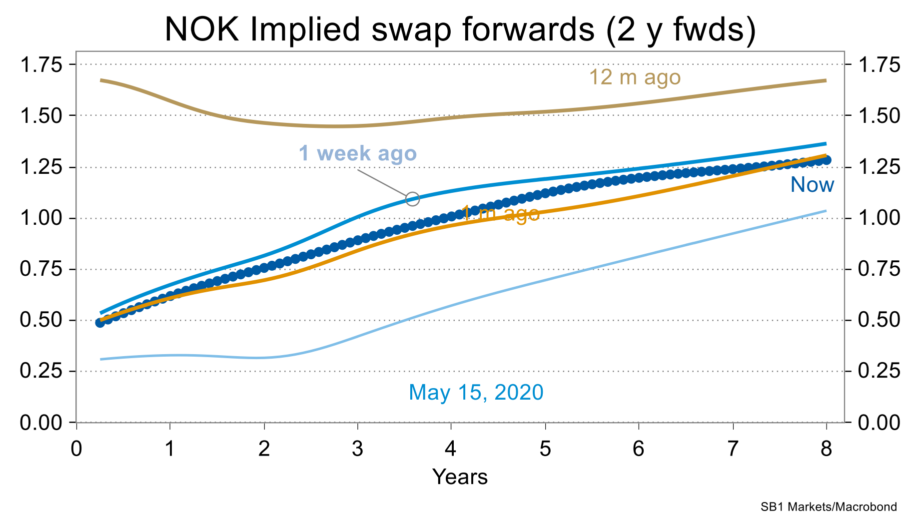
NOK down from the highest level since April

The mid segment reversed half of the lift the previous week

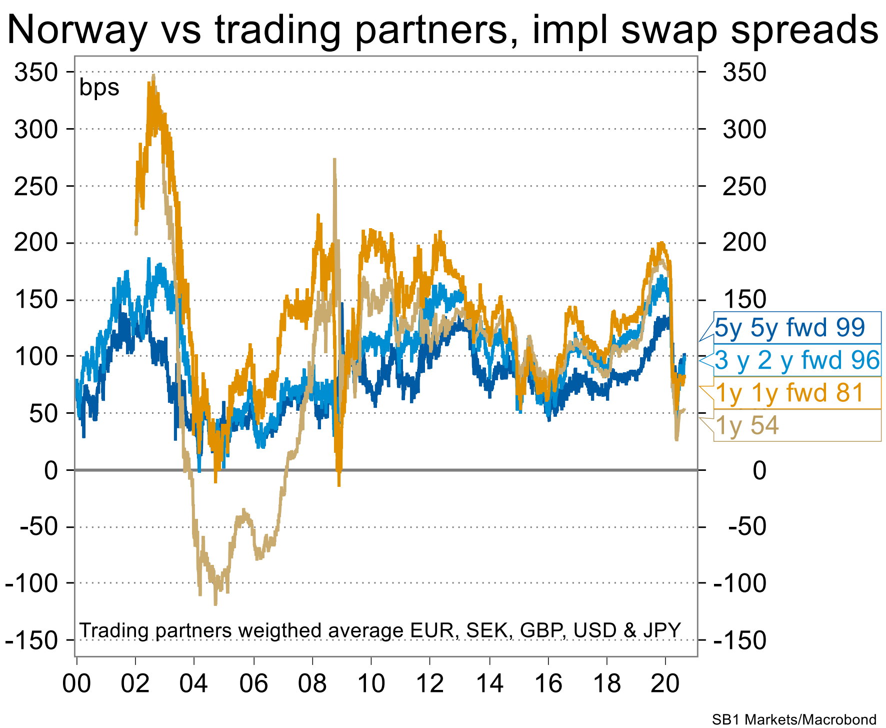


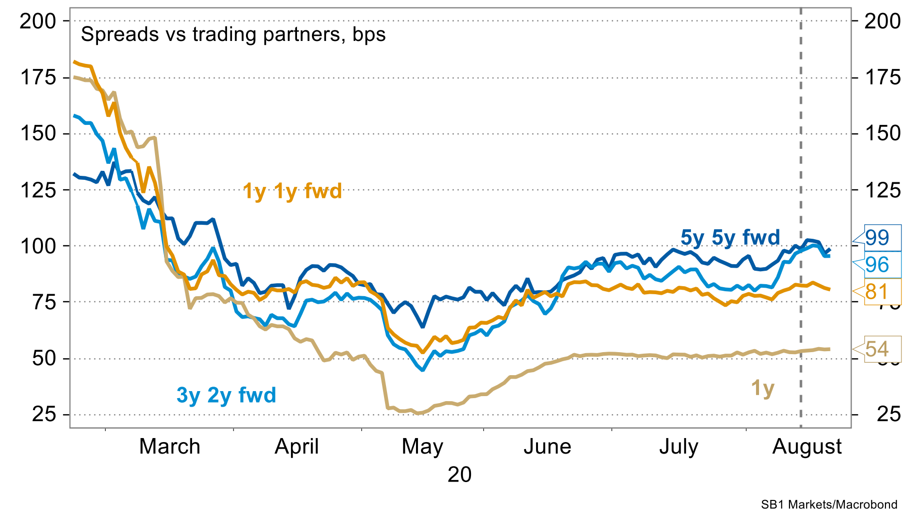


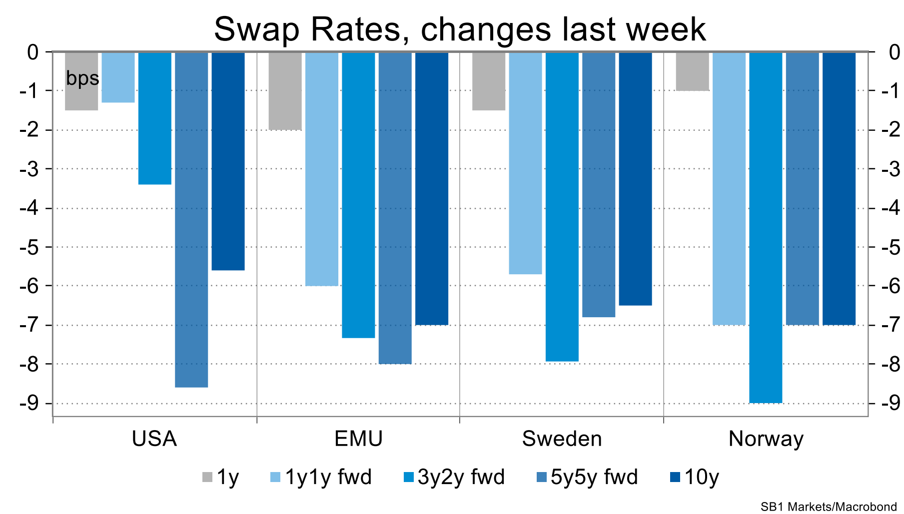


A parallel 5 – 7 bps shift down

The very short end of the curve unchanged,the rest down. No change in NOK-trading part. differential







- Spreads vs trading partners stabilised last week, following a small uptick
  - » Spreads bottomed in mid May, and have mostly widened since
- We are still neutral vs. the spread

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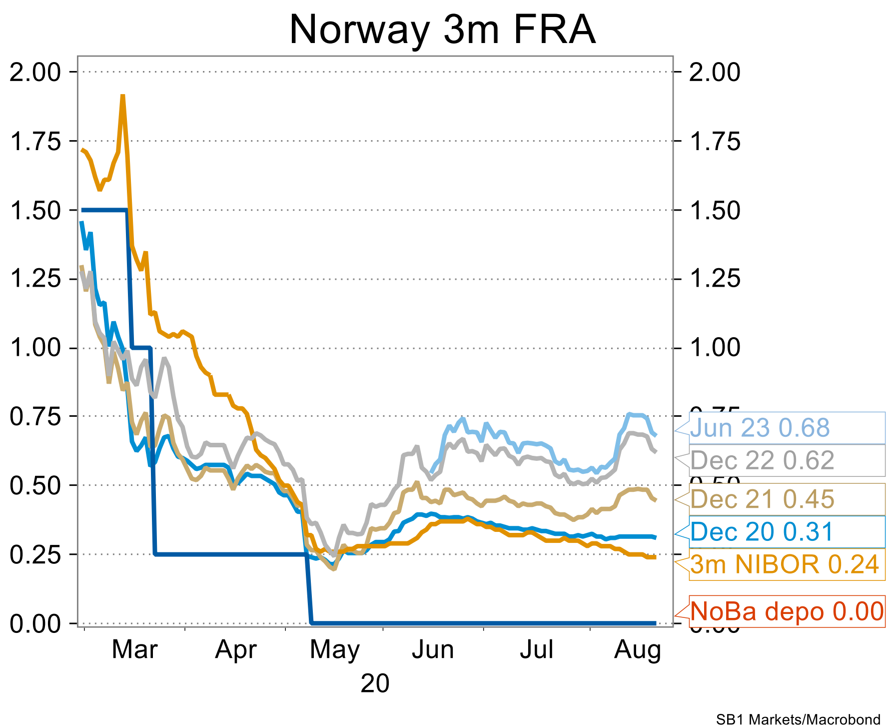
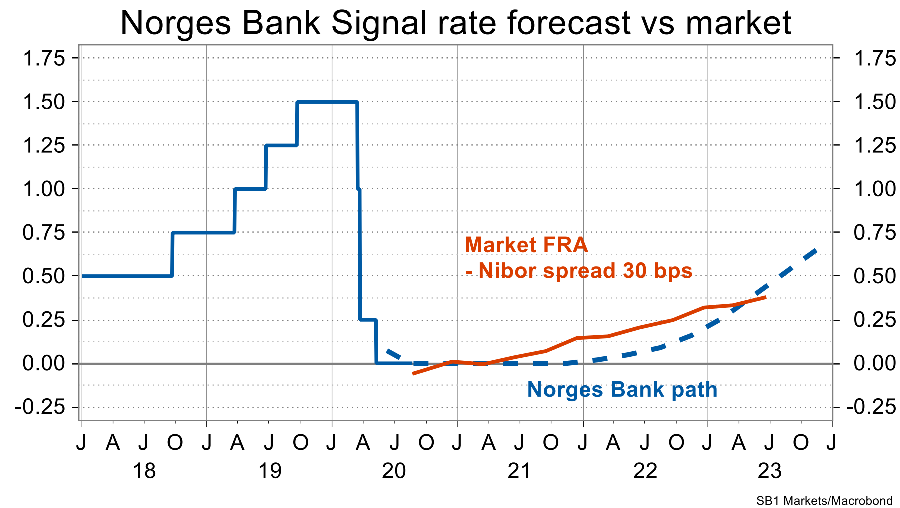
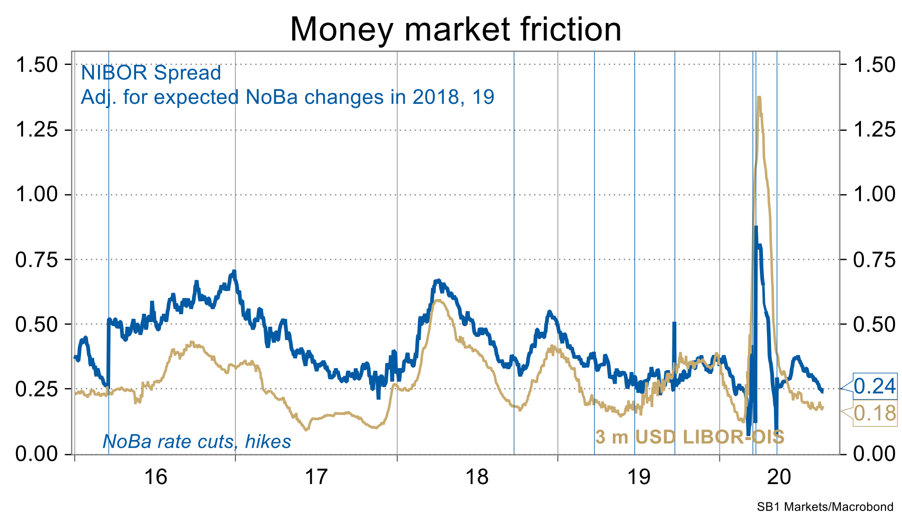
Oobs – 3m NIBOR down to 0.24%! FRAs down too, after a dovish NoBa

Following a 10 – 20 bps lift in FRAs the two previous weeks, rates fell 5- 8 bps. Still a hike in Q4 21??



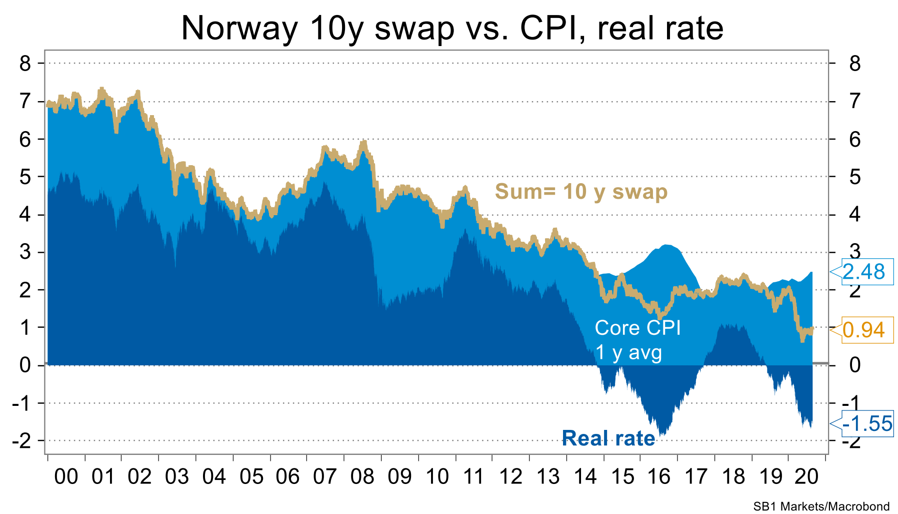




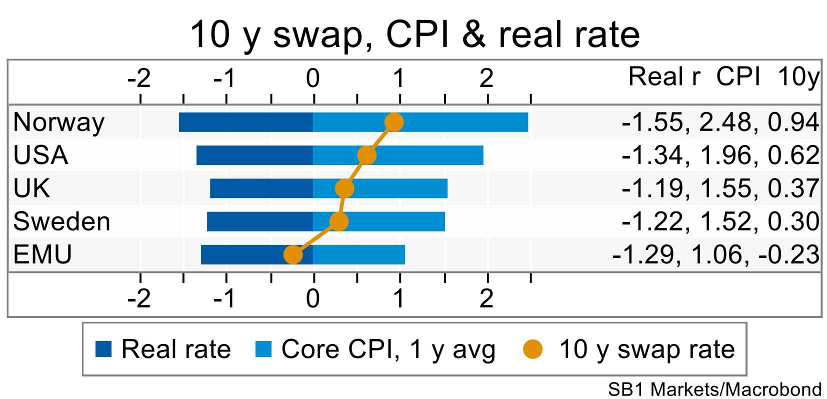
The NIBOR spread has fallen even further, and to 24 bps, as we think it is unlikely that markets are pricing in any probability for an interest hike the coming 3 months. We have cut out estimate for the NIBOR spread to 30 bps, from 35

Even if FRA's fell too, the first hike is priced in (more than 50% probability) for Q4 21, and fully by Q3 22. NoBa signalled Q4 22 in the June MPR, and did not signal any change last week

Negative (actual) real interest rates everywhere – NOK & USD at the bottom



- NOK 10 y swap nominal rates are down more than 1 pp since January
- Real rates have fallen to -1.5%, based on actual core annual inflation (smoothed 12 m
  - » All other other measures of actual/expect inflation will yield results in the same ballpark, from -1% or lower)



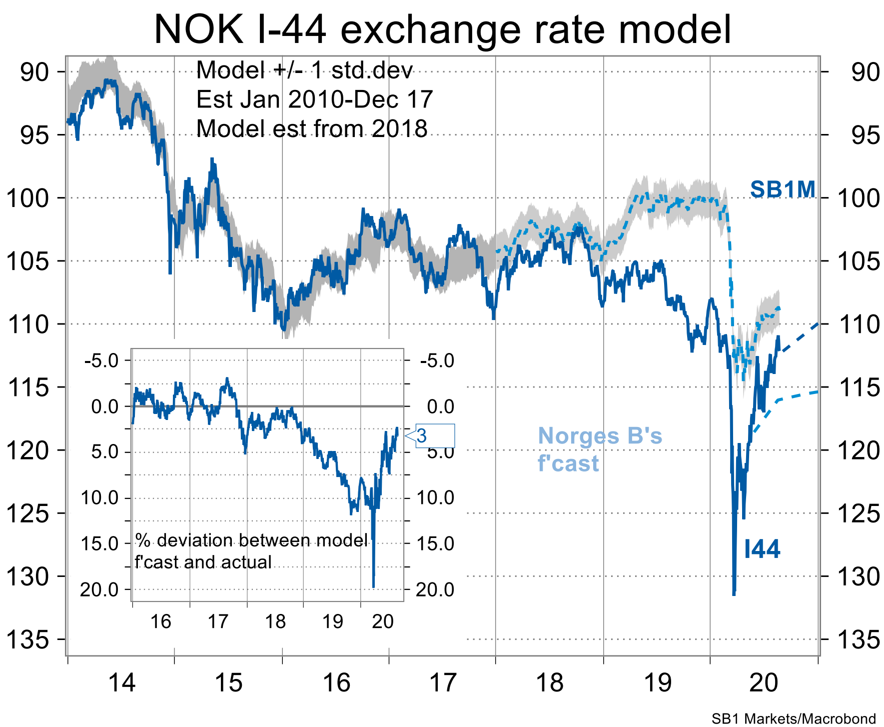
NOK real rates among the lowest

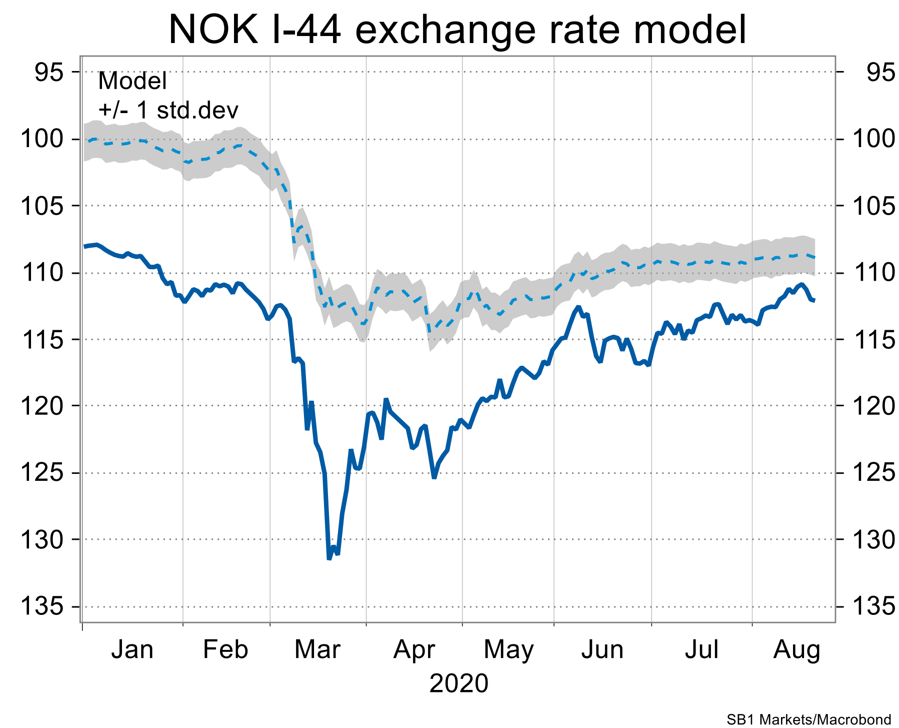
- Inflation among Norway and our main trading partners varies between 1.1 to 2.5% (here measured by actual annual core inflation, smoothed over 12 months). EMU at the bottom, US and Norway at the top, by a wide margin
- Real rates are quite similar among our trading partners, in the range -1.2% (UK, Sweden) to -1.6 (Norway), vs the 10 y swap rates

- *Thus: Inflation differentials explain most of the differentials in long term swap rates*

The down 0.5% last week, the model signalled -0.1%

Is the 0.4% gap due to the confusing debate on the appointment of the new Oil Fund CEO? We doubt





- Anyway, the NOK movement last week was miniscule
- Should the conflict between Norges Bank, the Parliament and the Ministry of Finance escalate substantially, markets could of course respond - but the Norwegian institutions will prevail, no doubt

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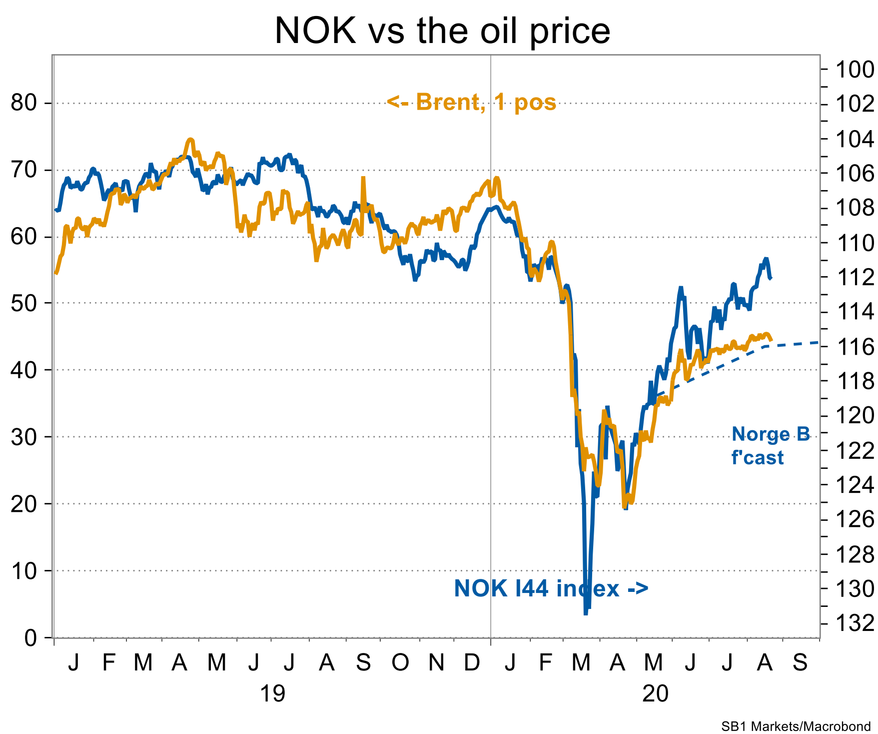
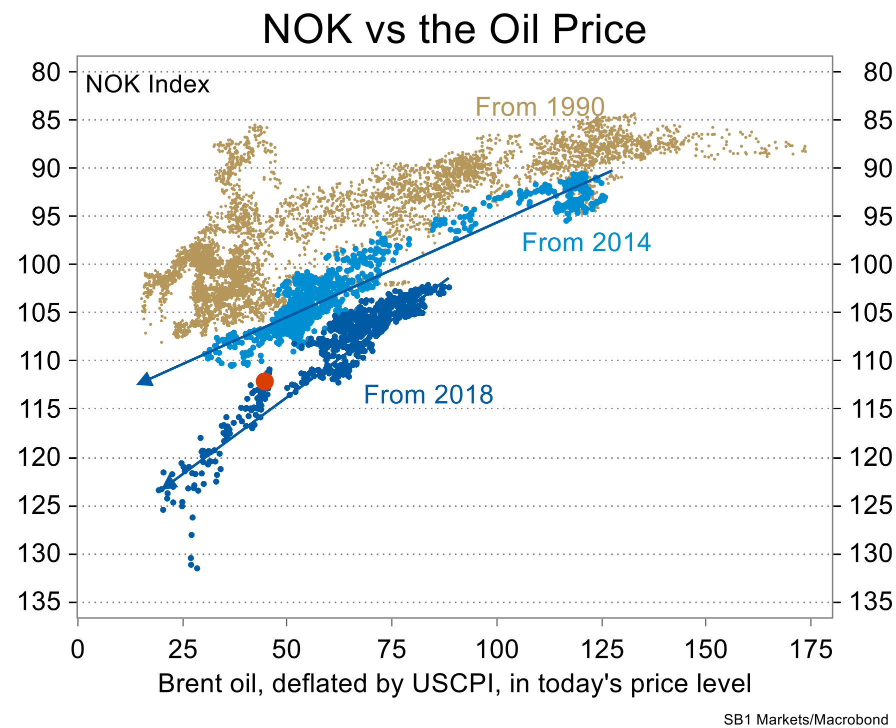
Over last weeks, the NOK has strengthened vs. the oil price (but not last week)

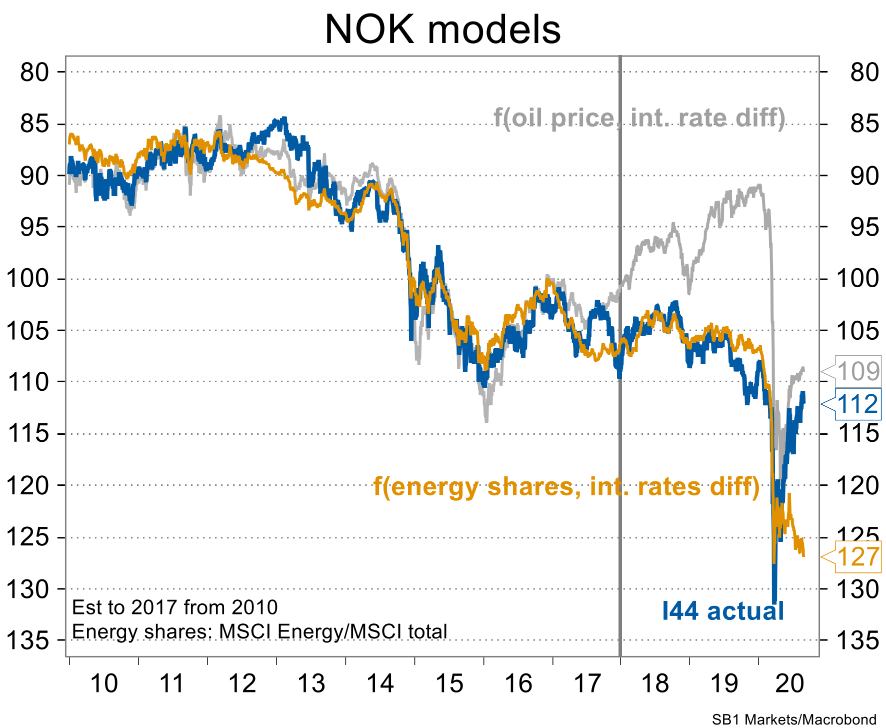


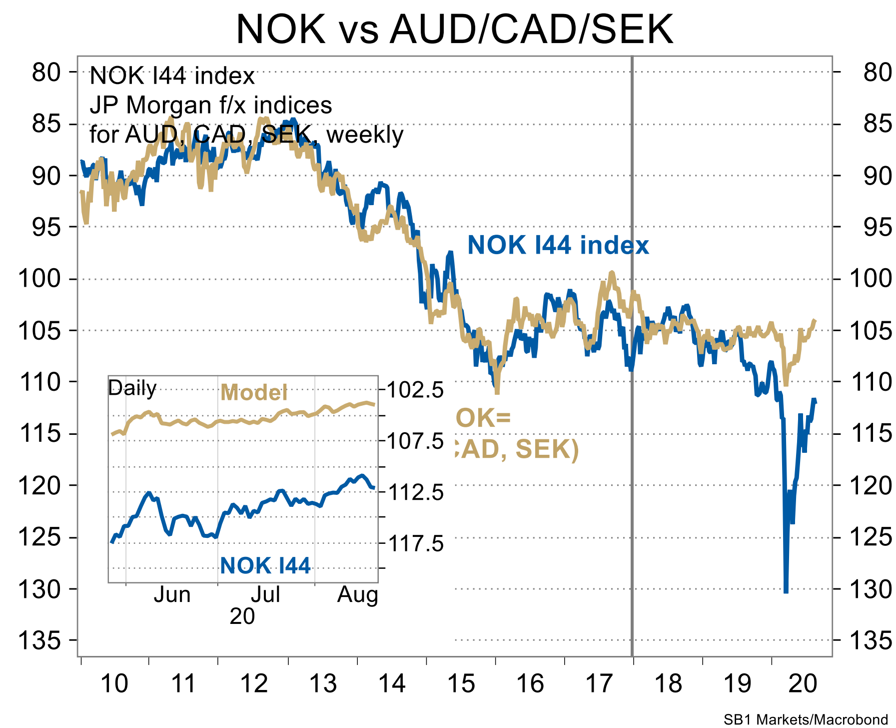


- The NOK has been much weaker vs the oil price than normal the past few years but it is still correlated to the *changes* in the oil price like it used to be. Now the NOK is on the strong side vs the oil price vs the relationship since 2018

NOK has left the oil companies. A small setback vs. AUD/CAD/SEK last week

Is the conflict about the new leader of the Oil Fund to blame for the depreciation?

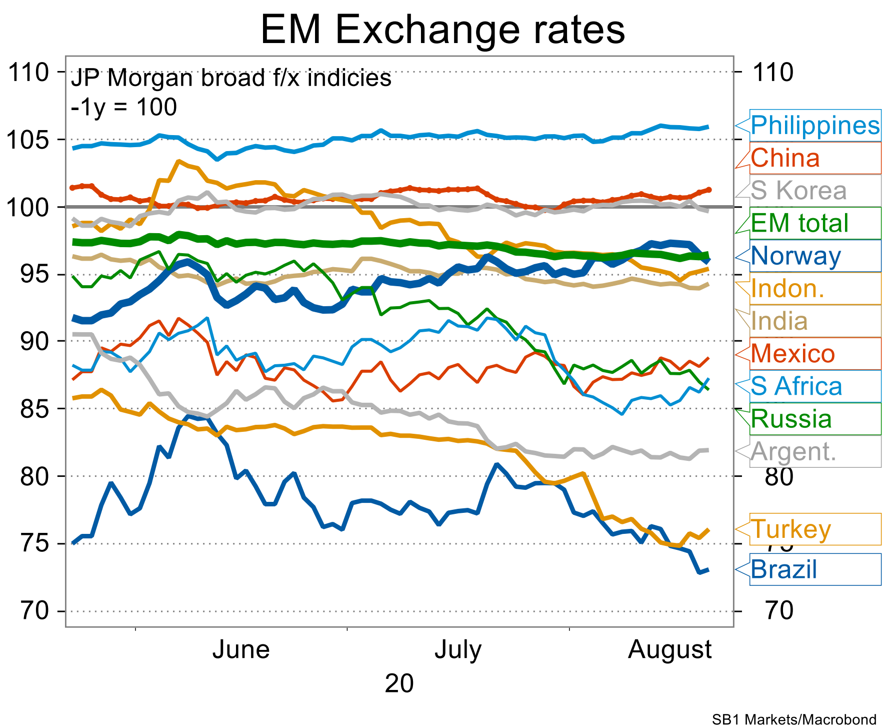


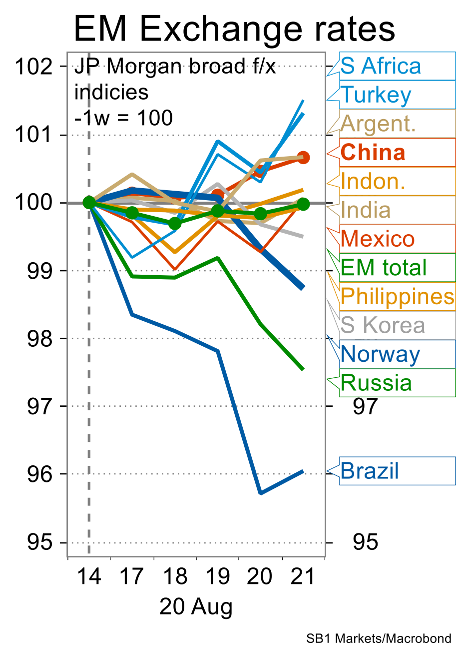


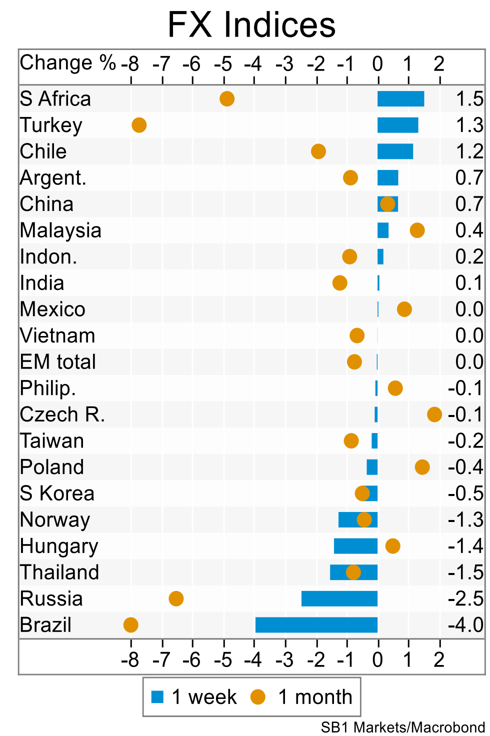
- Well, we have seen much larger NOK movements than over the past few days… The NOK lost 1% vs out supercycle friends
- On the alternative NOK models
  - Our NOK model based on pricing of oil companies has 'explained' the NOK much better than our traditional model since 2017, as have our 'supercycle' currency model [NOK=f(AUD, CAD, SEK), with just a marginal contribution from SEK]. The EM x CNY currency aggregate is also quite closely correlated to the NOK
  - The NOK is now 13% 'too strong' vs the oil price model. Has market realised that Norway is not an oil company, or at least much more than an oil company? On the other hand, the actual NOK is 8% below our AUD/CAD/SEK model forecast

EM currencies flat in average but volatile – Russian and Brazil tumble

The CNY appreciated – and has been stabile lately







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Service sector PMIs signal growth above normal

... which is needed in order to close the output gap