14 September 2020

Macro Research

Week 38/2020

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

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

Highlights, corona update

The world around us

The Norwegian economy

Market charts & comments

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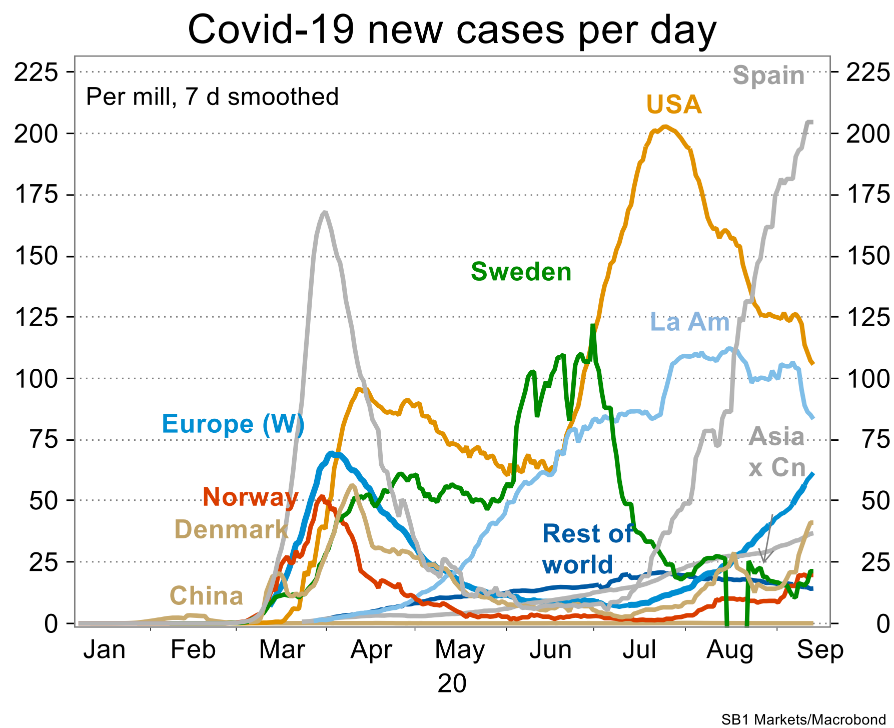
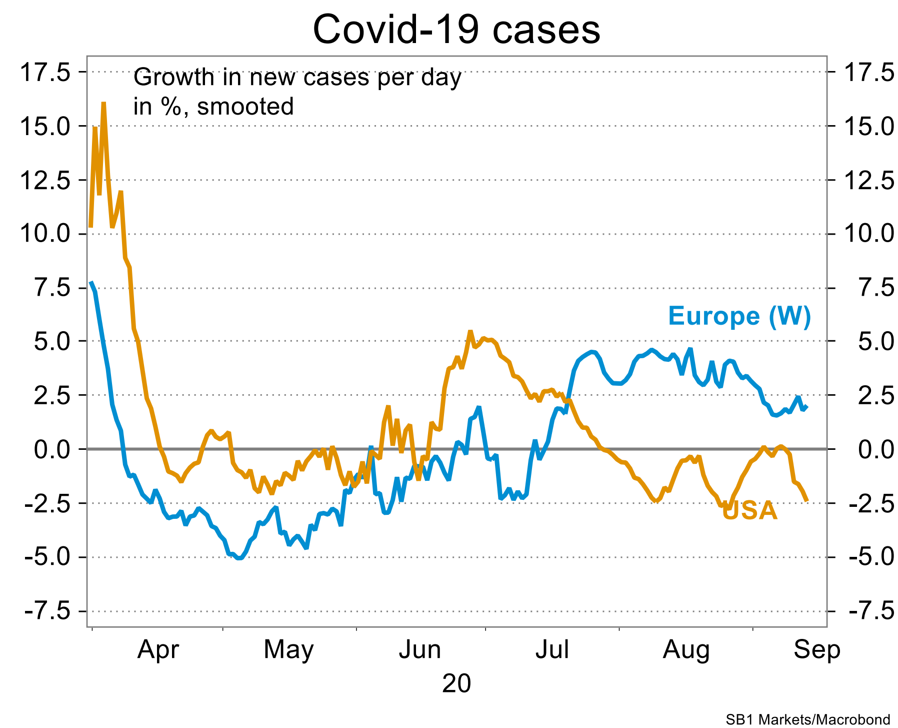
Last week:

- **Corona news:** The number of new daily cases in the US has turned down again, so have hospitalisations and deaths – and the economic costs of turning the curve appear to have been limited. Europe is still on the way up case wise but the virus is far less aggressive than before, the no of hospitalisations and deaths are even lower than in the US (vs. no of new cases). The virus is now far less aggressive than during the spring, at least vs. reported no of new cases. We expect more focus at the health consequences and less on the number of cases during the coming weeks and months A steep rise in the number of new cases in Denmark and Norway the past two weeks, but further in Norway last week. Sweden is reporting more cases as well, ahead of Norway, again. However, the levels seem to be manageable for contact tracing & local measures
- **Global auto sales** rose marginally in August and are back at the pre corona level. Chinese sales are above the 2019 avg, so are sales in Europe! US still 10% below, along with most other DM. EM x China recovering but remains some 17% below the 2019 level
- **China credit growth** has stabilised at 12%. **Core CPI inflation** is slowing, just at 0.5% y/y in August, total still at 2.5% due to higher food prices
- **US core CPI** surprised on the upside for the second month, up 0.4% m/m and the annual rate inched up to 1.7%. Inflation is still lower than before corona hit but demand is not doubt recovering**. New jobless claims** were steady last week, sliding down since early April but the inflow is still extremely high. The July **JOLTS labour market report** was rather upbeat, level and hires are rising rapidly, and unfilled vacancies are almost back to the Feb level, as are hiring plans! The lack of labour is confirmed by **the small business index which is reporting** difficulties attracting labour and higher hiring plans, while the outlook is back at an avg level. The August **Federal budget** was in red, but not that large – however the deficit is at 14% of GDP over the past year
- **The ECB** made no changes to its monetary policy and will continue its purchase programmes. The GDP f'cast was revised up somewhat, CPI f'cast unch. At the press conference, Lagarde emphasized that the risks to the outlook are tilted to the downside. **Manufacturing production** rose in July in all countries that have reported this far, however, the upswing is rather modest. We estimate a 3.9% increase in total EMU production. **Q2 GDP** details show that household demand was the main drag (as we already knew), followed by net trade and business investments
- **Norwegian Mainland GDP** up 1.1% m/m in July, we expected 2.5%. GDP is slowly recovering, still almost 5% below the pre corona level as services are lagging. **Core CPI prices** once again surprised on the upside, up 3.7% in July. Prices are accelerating in most sectors, boosted by imported prices. We expect a slowdown as the impacts from the NOK depreciation in the spring fades. **Manufacturing production** rose 1.8% (merely due to none oil related), but remains well below the February level. In its **Q3 Economic Outlook**, SSB revised up its 2020 GDP forecast to a 3.2% decline, from 3.9% (Norges Bank f'cast from June was -3.5%). A 3.6% increase is expected in 2021. House prices revised up from a 1% decline to 3.2% growth in 2020. SSB expects the interest rate to be raised already in mid-2021 (Norges Bank said 2022 in June, the market expects a hike in late 2021)

US cases down again, Europe still on the way up. Spain has not yet turned down

The US curve is tilting downward after a 3 weeks' break, while Europe still is on the way up





- **The US** curve has been moving down since late July. The number of new cases is now declining again, after flattening out the previous weeks. The no of hospitalised patients is falling sharply, and the no of deaths is now trending down too**. The economic cost of turning the curve has most likely been limited – the best corona news?**
- Growth in new cases in **Europe** has not yet slowed but the no of hospitalisations & deaths are still very low (and not visible at all in overall hospital or death stats)

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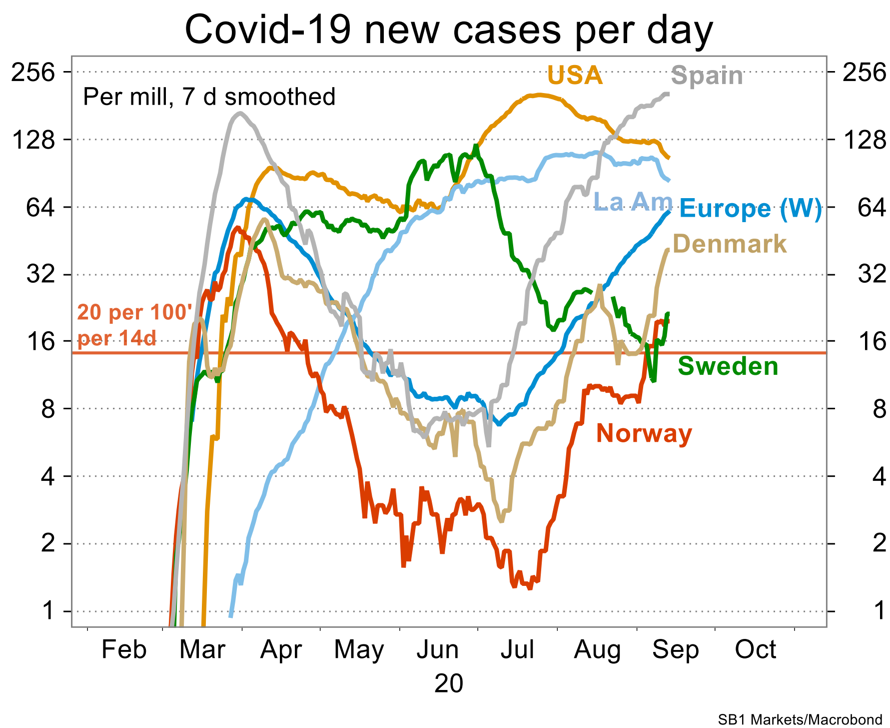
Norway and Denmark rising again, Sweden too

A sharp increase in new cases in Norway and Denmark, highest since April



- Sweden has been reporting a sharp decrease in new cases - but rose above the 'red line' again last week – more than 20 cases per 100.000 the past 14 days
- Both Norway and (even more) Denmark have been reporting a sharp increase in new cases the past two weeks – but not further in Norway the past days

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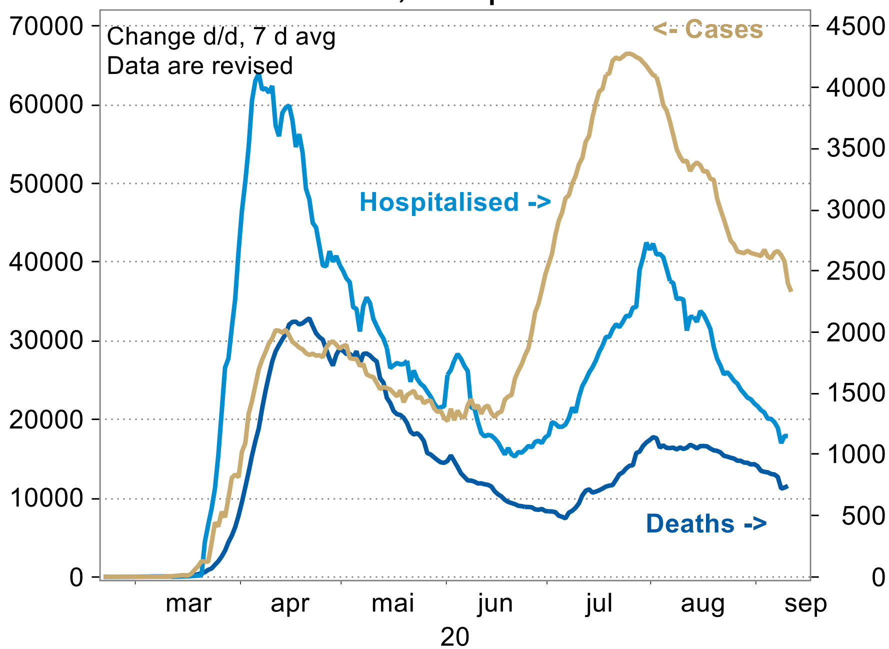
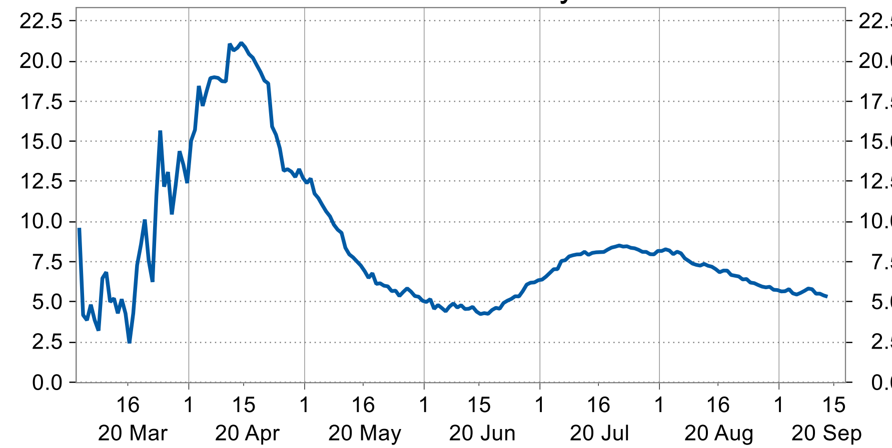
USA: The number of new cases is declining again, hospitalised & deaths too

.. And the number of patients in hospitals and no of deaths remains at a low level

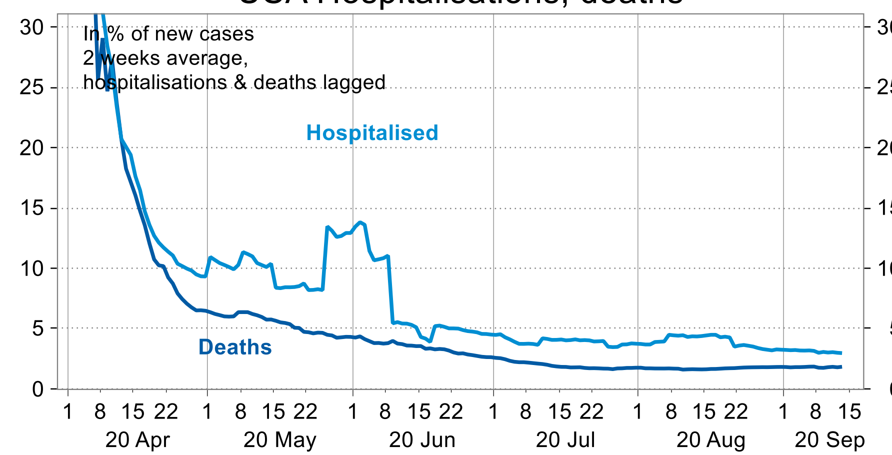
USA Covid-19 cases, hospitalisations & deaths



USA Covid-19 Positivity test rate



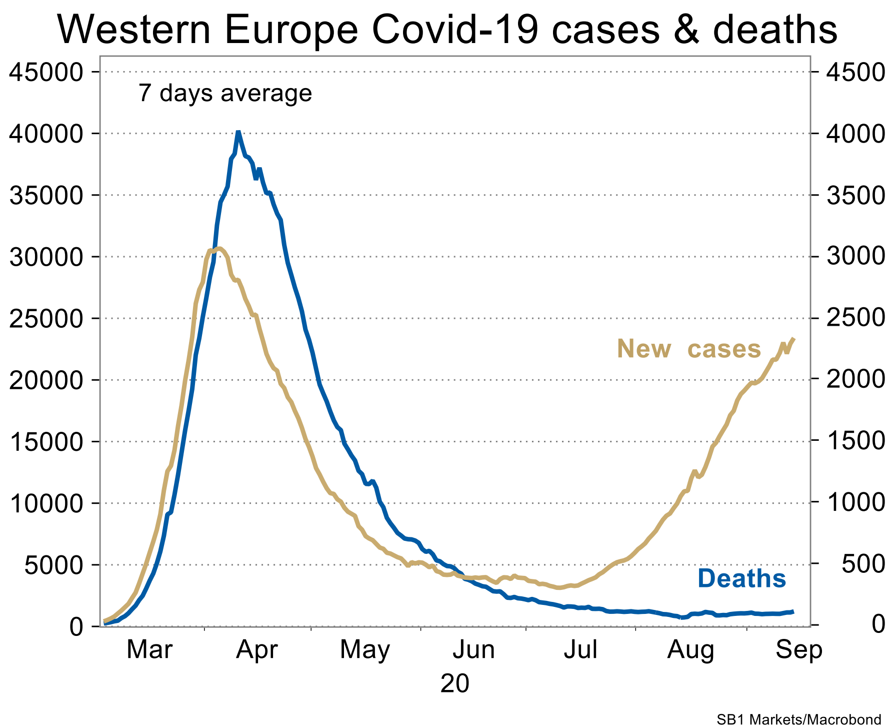
USA Hospitalisations, deaths

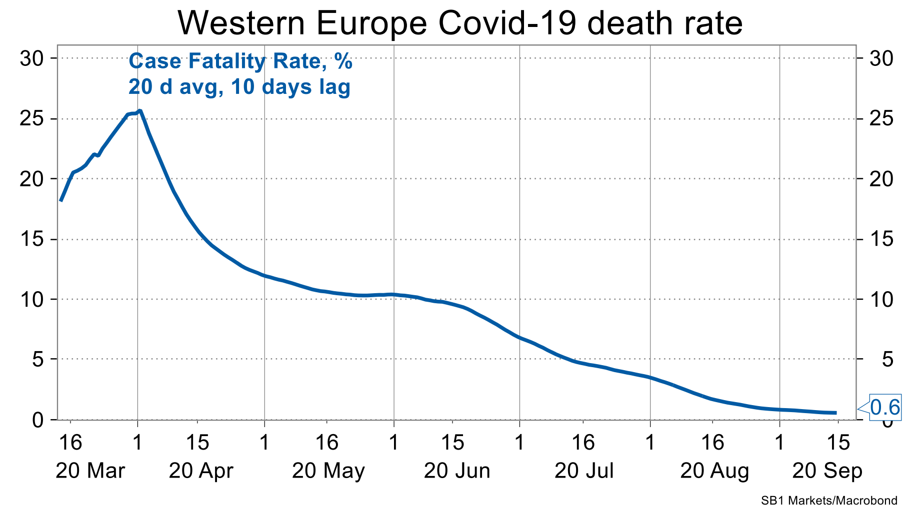


- The hospitalisation rate is far lower than during the early phases of the pandemic but has not fallen further the past two months
- The death rate (CFR) fell sharply until late July but has since flatted out - at a low level

Remarkably few deaths in Europe too

The CFR has fallen to close to 0.5% - from 10 – 20% during the spring



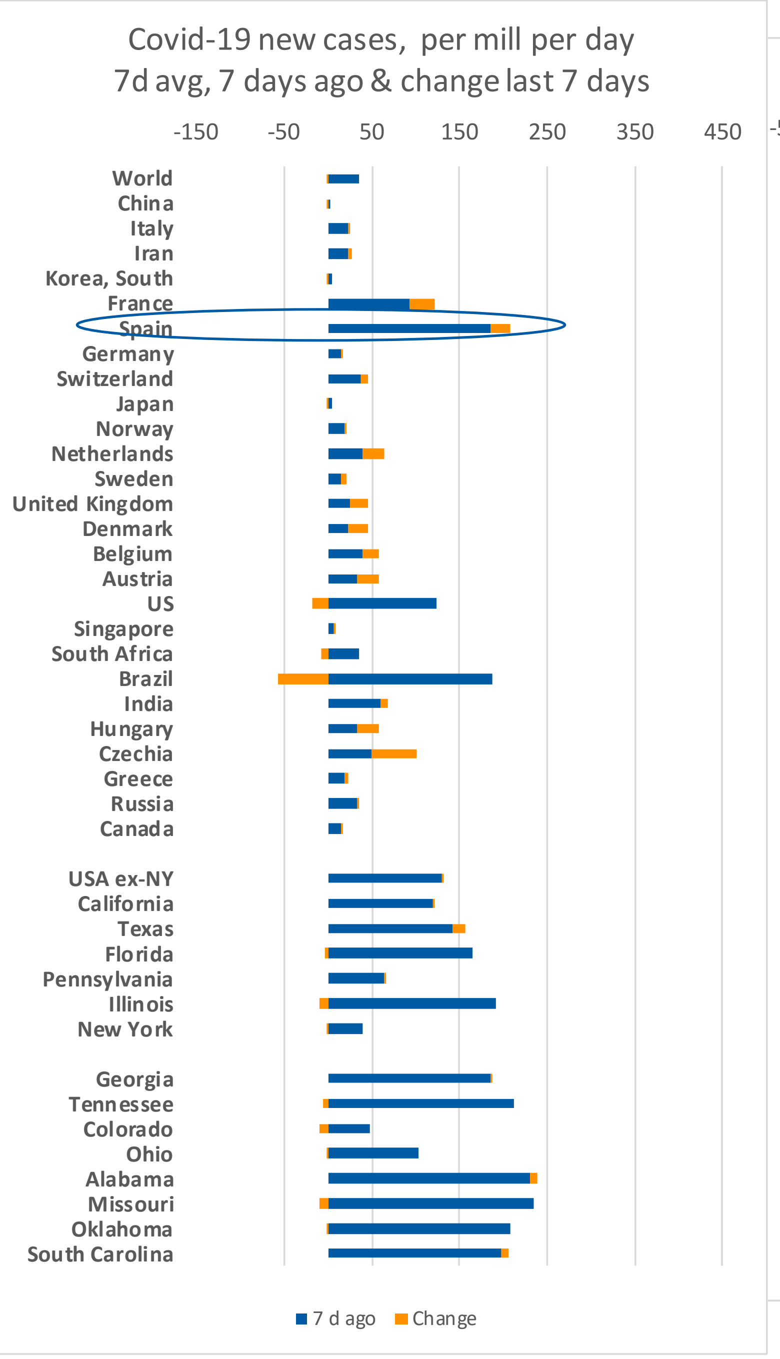


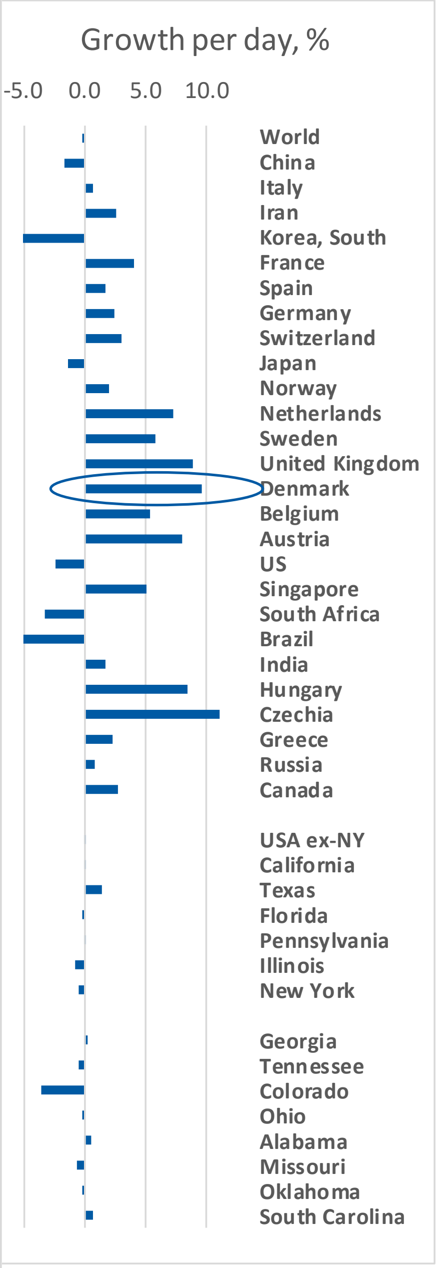
- The test regime is far more rigorous now than during the spring where the real no of infected was many times higher than the no of positive tests. The 'real' death rate was miles below 25% at the peak. However, it seems unlikely that the death rate back then was far less than 1% as the health system was overwhelmed with patients
  - » The present number o0f deaths is not visible in overall death stats in any European country
- In addition, the number of hospitalisations is a very small fraction compared with the levels during the spring and hospitals can return to their normal activities
- We assume that over the coming weeks, the number of really sick patients, and corona related deaths will become the main gauge of the corona crisis (as it was during the spring), and the focus at number of new case number will diminish

US & the rest: A comparison

It won't lay down…

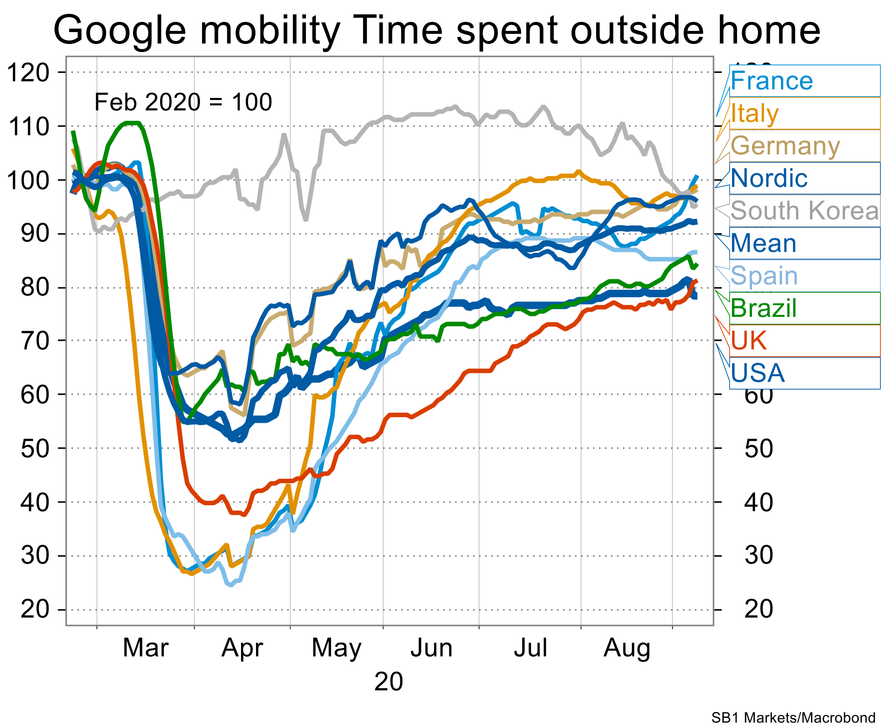
- More countries reporting an increase last week:
  - » In the US the number of new cases has turned down again
  - » In Europe, cases are still increasing but growth is slowing down. In Spain, which is hardest hit, growth may be slowing. Growth has slowed in Italy too, where the level is still low
  - » Norway is reporting a sharp increase in cases
  - » Denmark and Czechia reported the highest growth rates last week
- We do not trust all of these data
  - » There are changes in test policies & capacity
  - » Some countries do not report properly

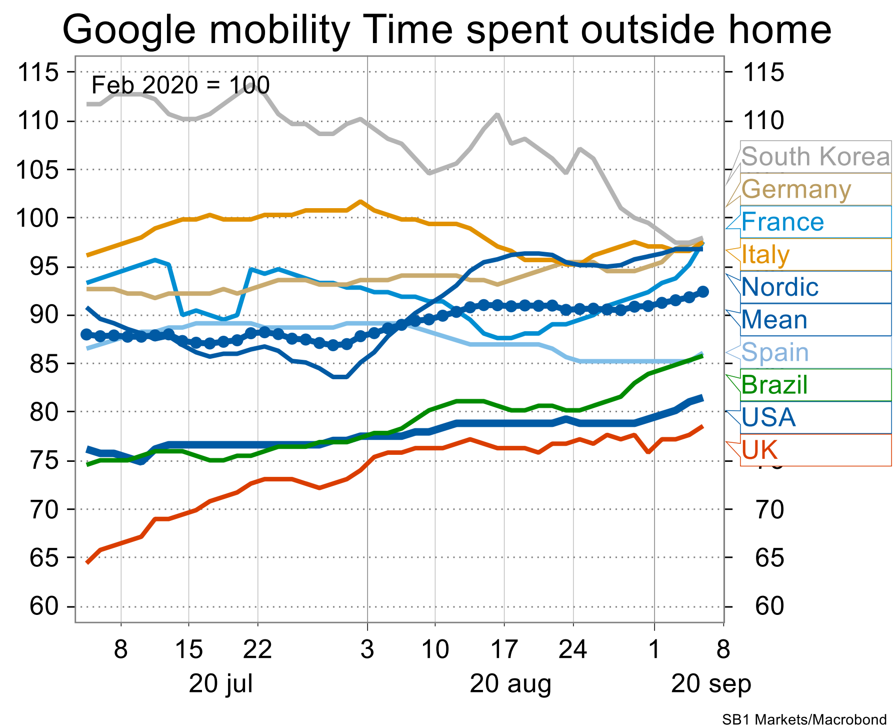




Time spent outside home on the way up

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

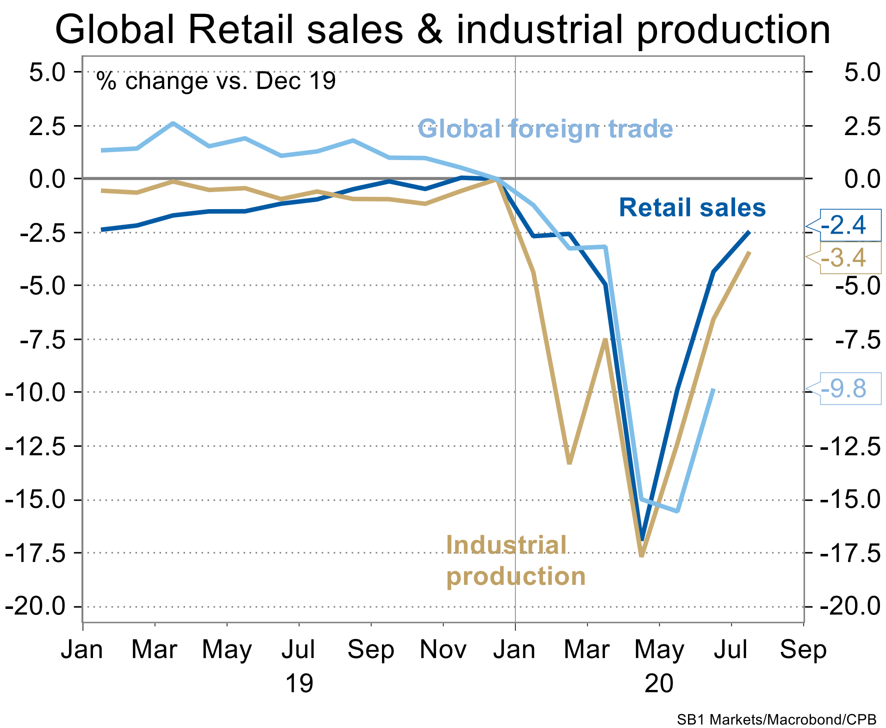


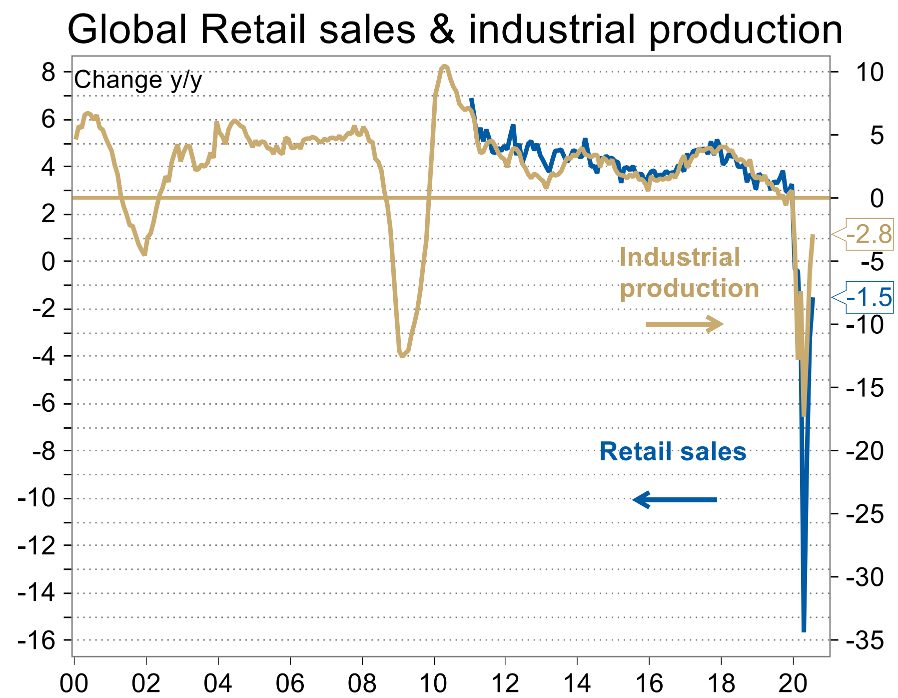


- The Nordics are quite similar, except for the 2 – 3 weeks from mid March when time spent outside home fell less in Sweden than in Denmark and Norway

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

July retail sales are just 2% below the Dec 19 level in July, manuf. 3% below





Memo: Keep in mind the different scales at the chart above

- Global retail sales grew 2% m/m in July, according to our preliminary est, after rising 6% in June. Sales are 2½ % below the pre corona (Dec) level (but on par with Jan/Feb). Sales in many DM countries are above the Dec level, China (and probably India is still well below (and many countries have not yet reported July data)
- Industrial production rose 3% m/m in July (our est), from 7% in June. Production is still 3½ % below the pre corona level
- Global foreign trade shot up 7% m/m in June but was still 10% below the pre corona level. No July data

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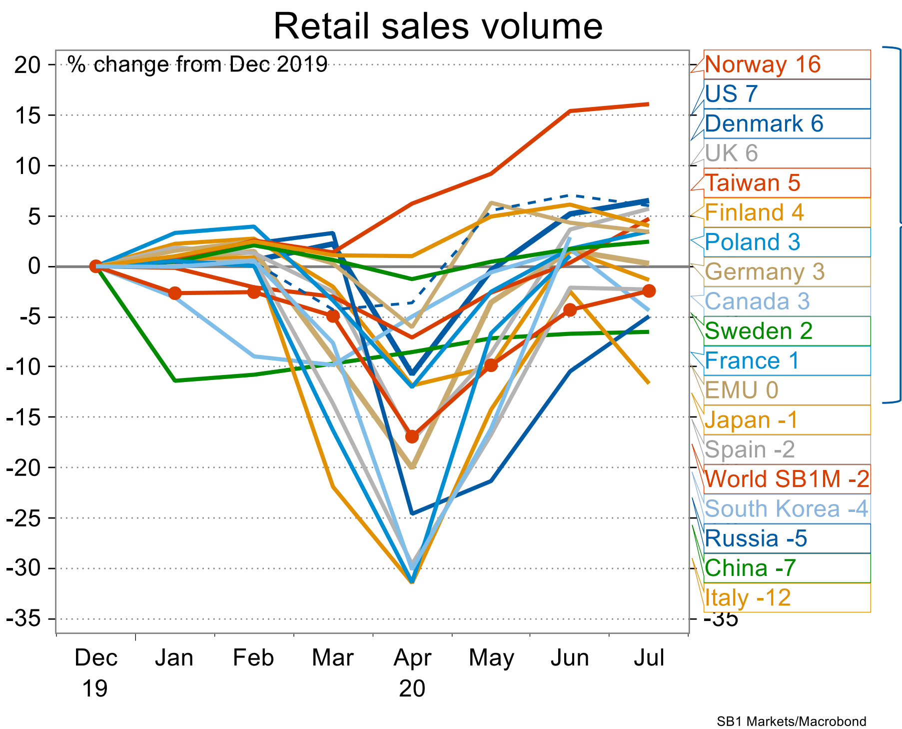
Retail sales are on the way back to pre corona levels

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



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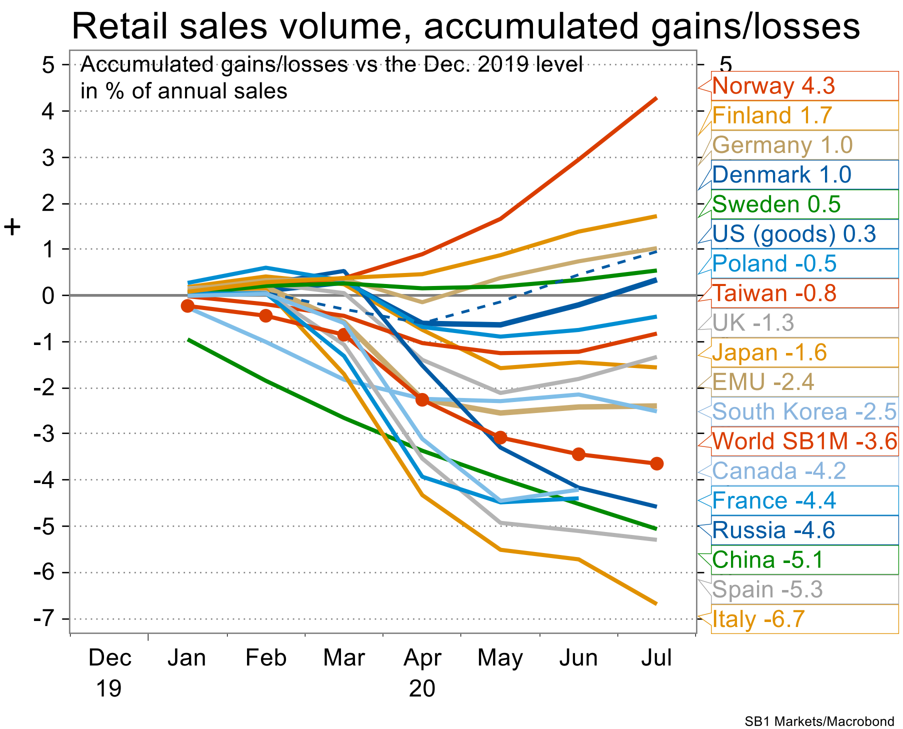

- We assume global retail sales rose 2% in July. If so, sales were just above 2% below the pre corona level. Most countries are now reporting higher sales than before corona hit
- The chart to the right presents the accumulated gains/losses vs. the level in Dec 19, measured in percent of annual sales. Sales in say US were 7% 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, due to the losses during the spring
- Consumption of services are not included in these retail sales data – and service consumption has fallen sharply, everywhere

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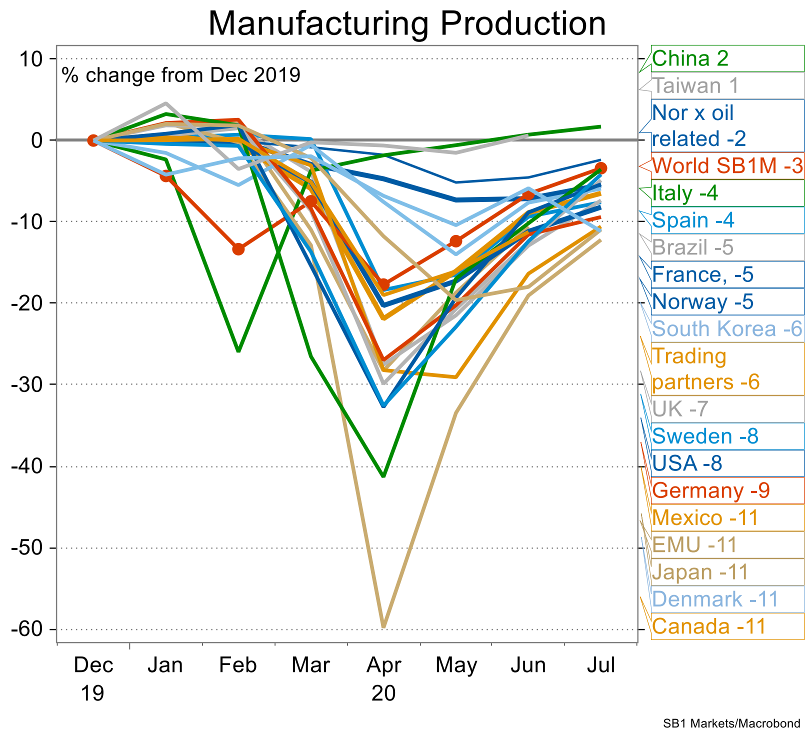
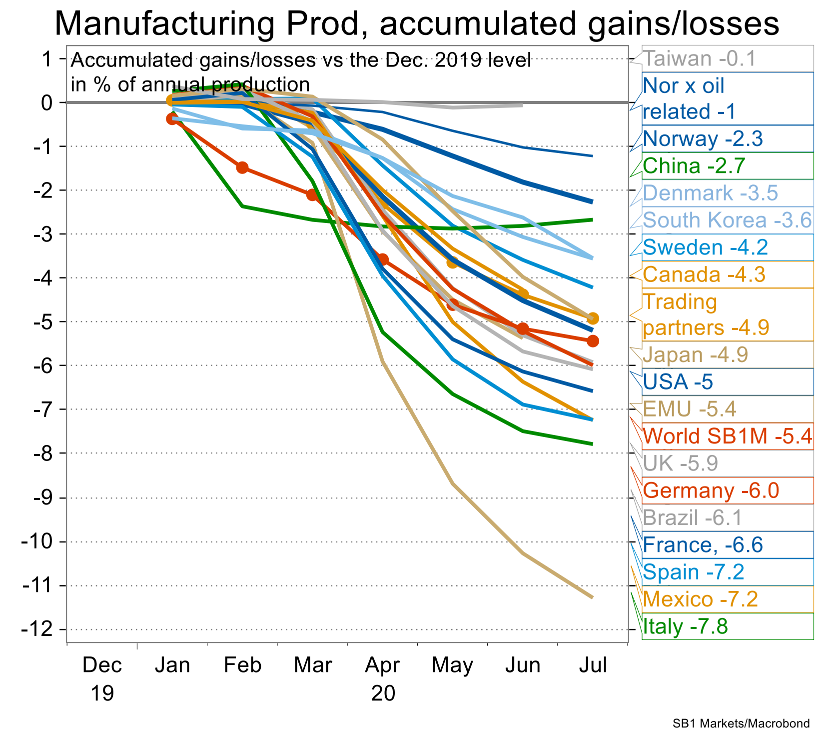
Manufacturing production on the way back, still some 5% of 2020 'is lost'

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

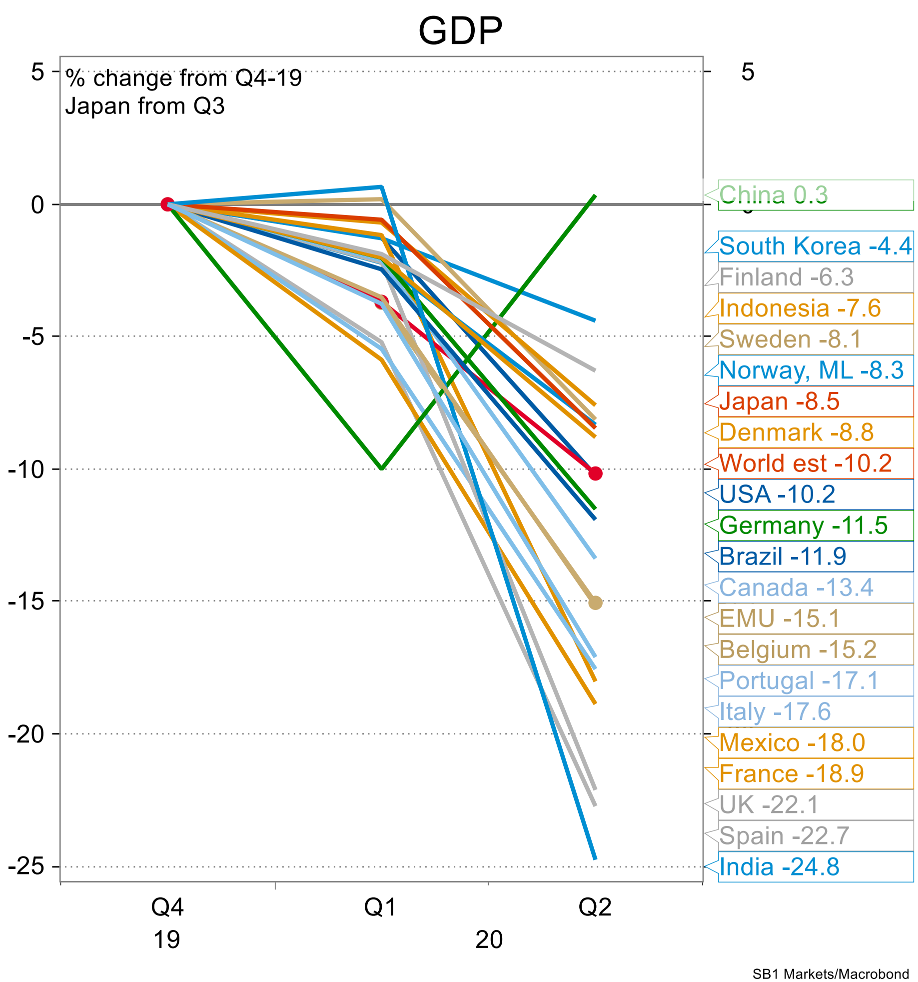




- We estimate approx. 3% m/m increase in manufacturing production in July. Production was still down 3.4% vs. the Dec level
  - » Compared to the Dec 19 level, China is in the lead (above the Dec level) followed by Norway and the US
- The chart to the right presents the accumulated gains/losses vs. the 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
- <u>Service sector production is not included</u> in these retail sales data – and service consumption has fallen sharply, everywhere

Global GDP down ‘just’ 6.7% in Q2 but down 10% v. Q4

Except China, all countries we follow have reported lower GDP



- 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 10% from the Q4 2019 level, and it was 10% below the pre corona trend path (see chart next page)
  - China up 11.5% q/q, and is up 0.3% from Q4
  - US down 9.1% q/q
  - EMU down 11.8% q/q
  - UK down 20.4%
  - Sweden down 8.3% in Q2, Denmark 7%
  - Norway Mainland down 6.3% in Q2, 8.3% from Q4
- 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)*

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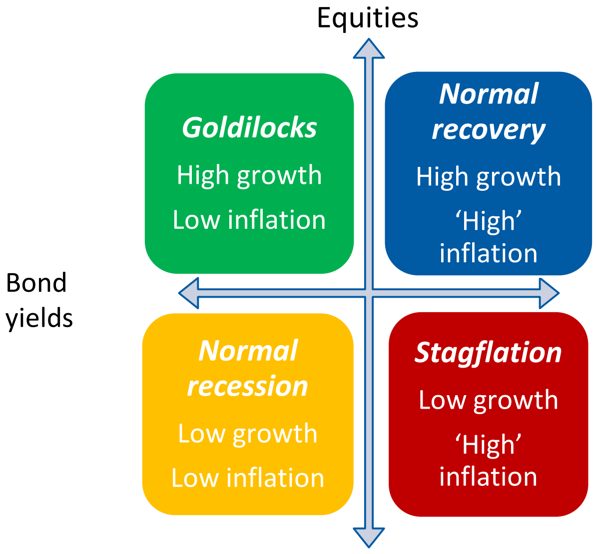
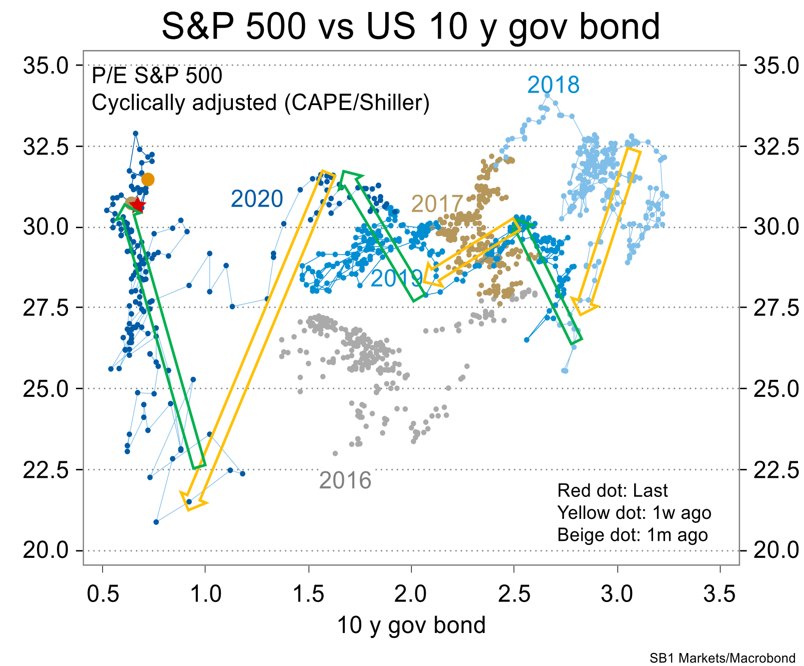
From the 'Goldilocks corner', where to go?

Fed's new strategy implies low rates even if inflation should climb to above the target

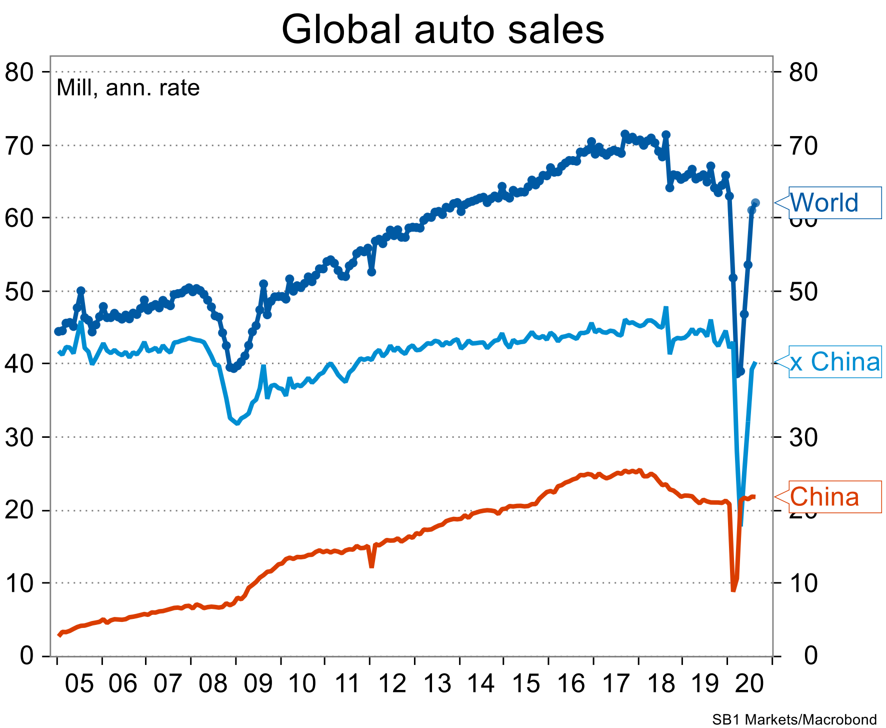


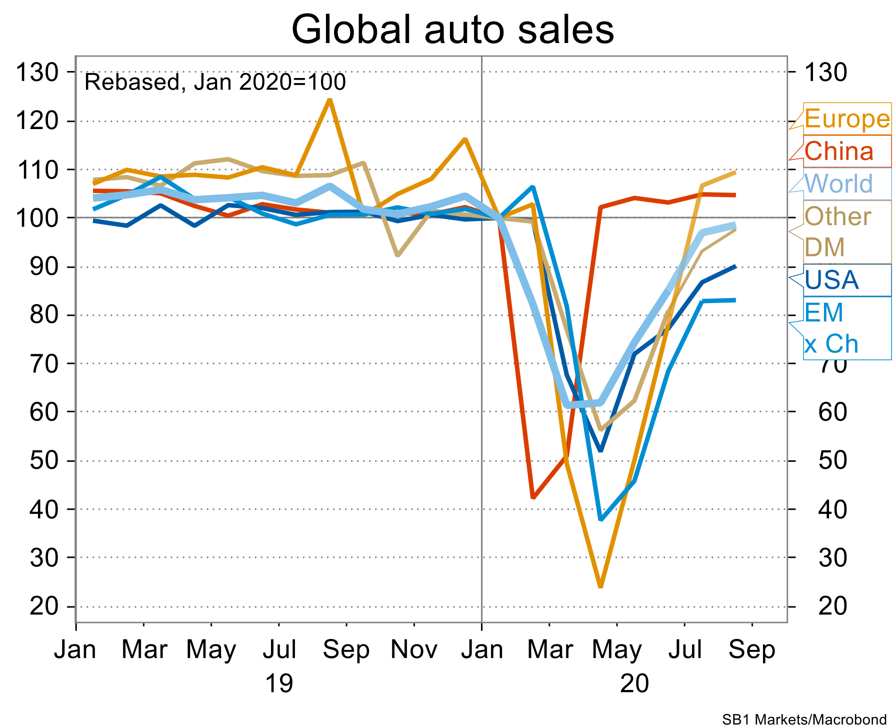


- Usually, we have associated drifts towards the 'green corner' - low inflation and solid growth at the same time - as <u>temporary</u> sweet spot for markets were growth above trend had not yet created imbalances in the economy – or at least not inflation.
- Now, the US Federal Reserve promises to keep monetary policy expansionary, until actual inflation has overshot the 2% target for a while, in order to bring average inflation over some years (not defined, but say some 5 years) back up to the 2% target. As a bonus (at this stage of the cycle), that would also make it possible for the Fed to push employment higher, profits margins lower, and thereby contributing to reduced inequality
- Will we stay up there, in the green? Perhaps, for a while – but probably not, long term
  - » The economy has rebounded rapidly from the corona through in mid April, and corporate earnings will follow suit. Any substantial disappointment on corona/vaccine or the growth cycle in general would be challenging for the equity market. Short term, the risk seems limited
  - » The Fed will not yield from its new strategy anytime soon. However, (higher than expected) actual wage or price inflation numbers may shake the market's confidence in the sustainability of Fed's strategy, pushing long term bond yields up, both interest rate expectations and real rates. Again, the risk is not serious, short term, even if inflation is heading <u>up</u> following the initial corona slowdown
- Why are we sceptical vs. the long term outcome? Before corona, the employment rate was high in the core age group, businesses reported (and are now again (!) reporting) unprecedented lack of labour, wage inflation was not low vs. inflation or productivity. Profits were under pressure, and investments on the way down. <u>Interest rates had not been too low, even if that is the popular view these days</u>

Global auto sales back at the (low) pre corona level, China above, EMU on par

Sales marginally up in August. China above last year's sales, ROW 7% below (from -60% in April)

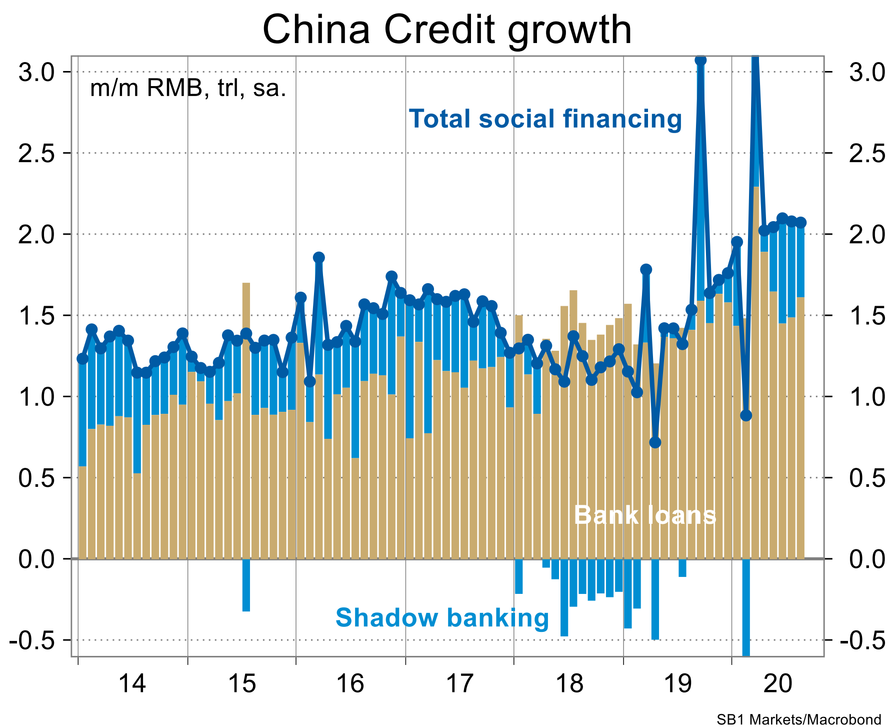


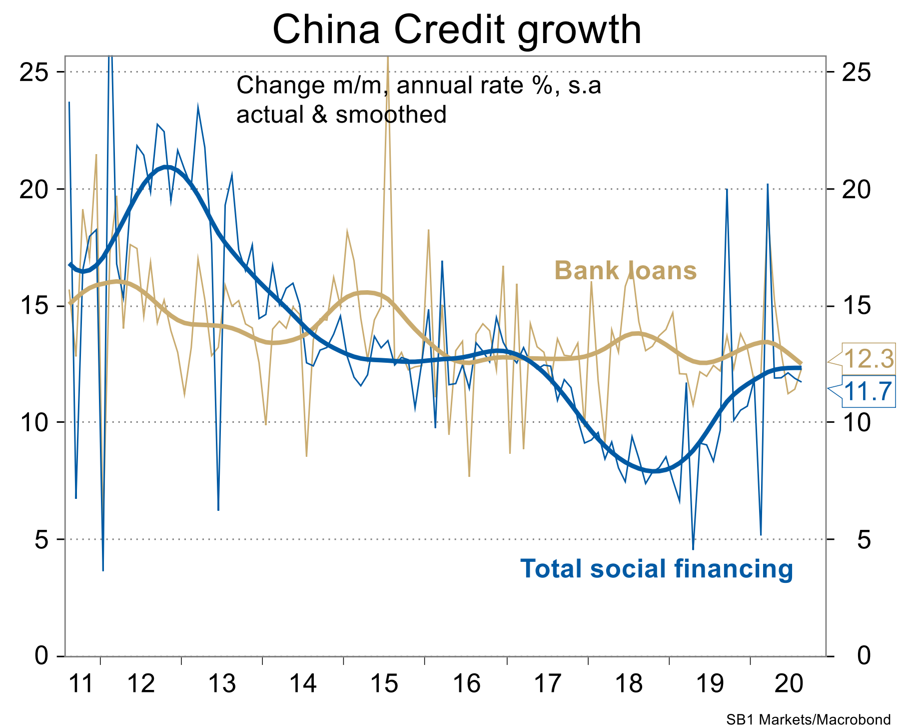


- This is the most undisputable 'V' we have on offer – data are reliable and updated. Just one caveat: Sales may now be boosted due to pent up demand – and may slow during the autumn, especially if the corona virus creates new, serious problems (which it is so far not doing)
- Chinese auto sales were flat in August, and are above both the pre corona and the avg 2019 level – which though both were rather depressed – by more than 20% vs. the pre 2018 trend. However, the corona downturn lasted just 2 months!
- Sales in Europe are back to a normal level, marginally below 2019 sales, which was the best year since 2007. US sales are still some 10% below the 2019 avg. Other DMs are just marginally (2%) below the corona level
- Sales in EM x China were probably close to flat August, after strong the previous months – broadly based. Still 17% below the 2019 avg

Credit growth has stabilised at some 12%, above trend growth in nominal GDP

Both banks and other sources (shadow banks) are contributing to total credit growth

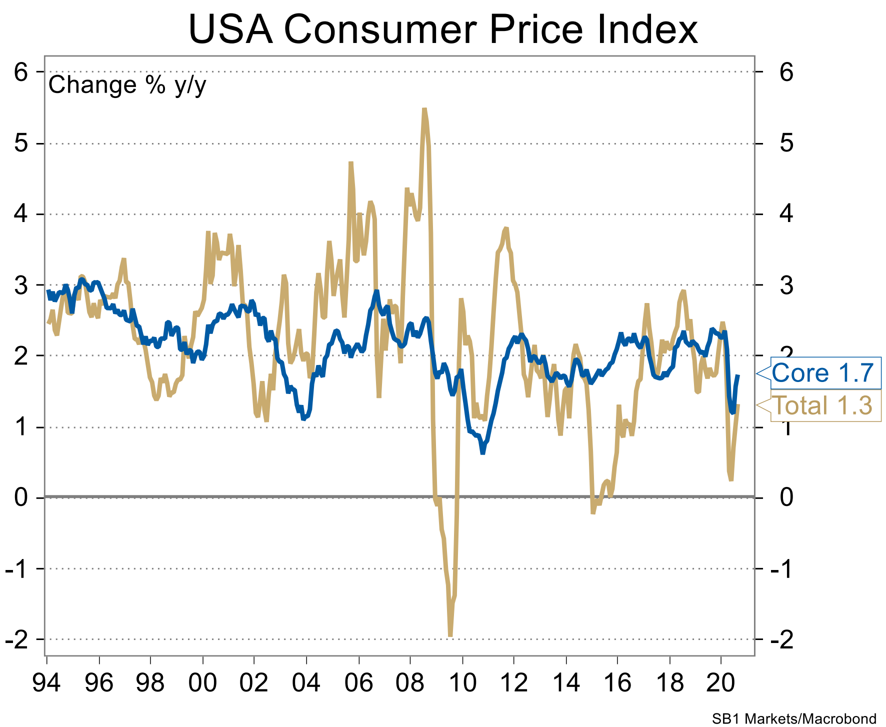


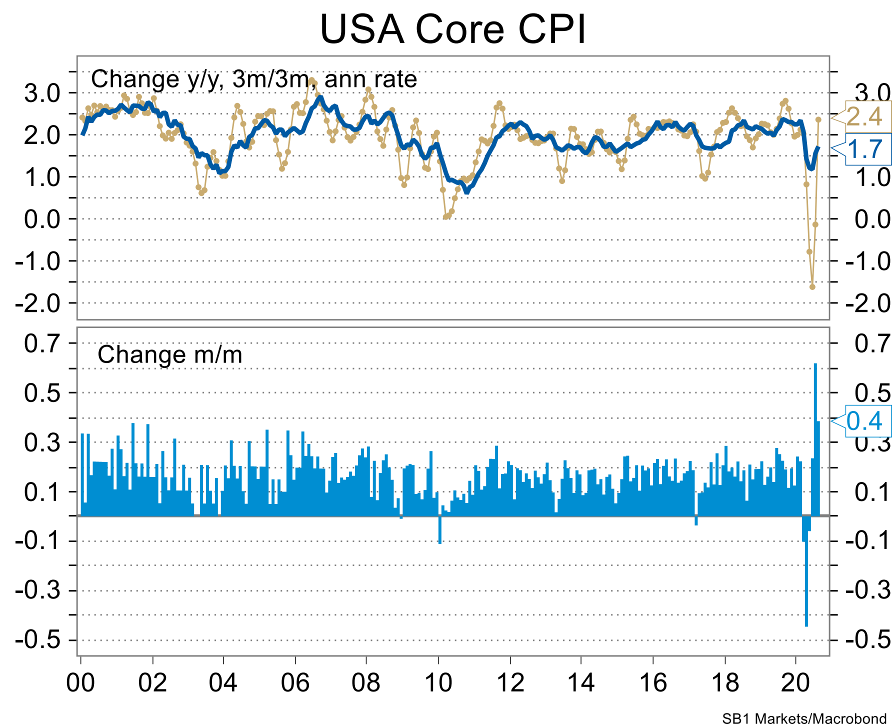


- Total credit growth has stabilised at approx 12%, if we smooth out volatile monthly figures
  - » Total credit rose 1.9 trl RMB (not seasonally adjusted), expected 2.6 trl. Banks supplied some 4/5th of the new credit (based on seasonally adj. data)
- The underlying total credit growth has been accelerating since early '19, but has flattened out recent months, at 12%
- Authorities have no doubt been trying to support growth through the credit channel during the corona setback, even if the risks are considerable

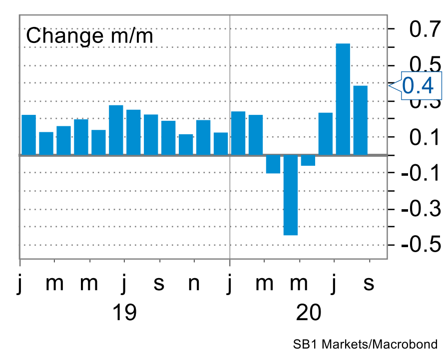
Core CPI up another 0.4% m/m in Aug, evidence of a demand comeback

Annual rate up 0.1 pp to 1.7%, expected unchanged. Vehicles, furniture and lodging boosted growth



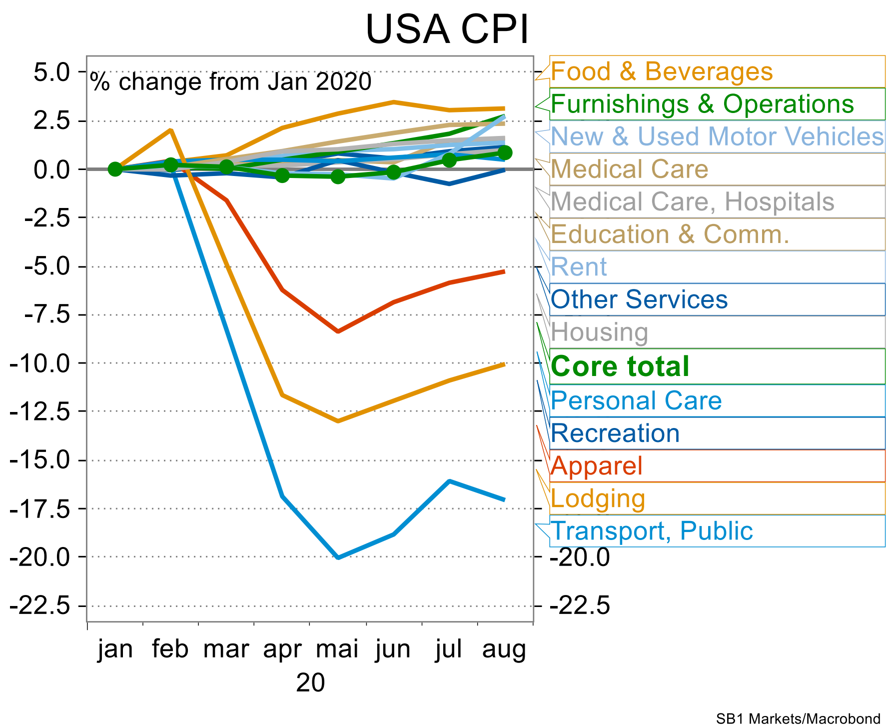


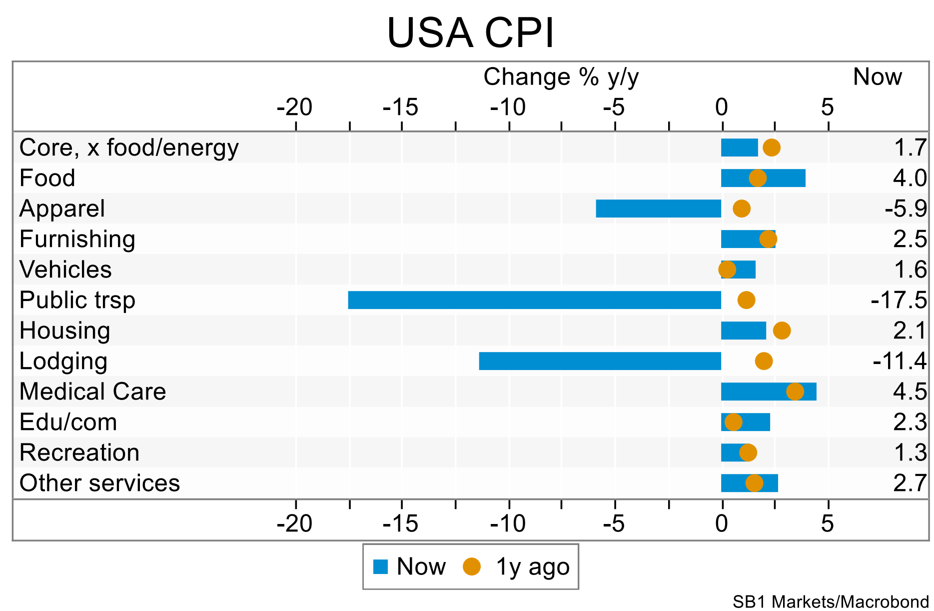
- Core CPI prices rose by 0.4% m/m in August, 0.2 pp higher than expected, following the surprising 0.6% jump in July. Annual inflation up 0.1 pp to 1.7%, still 0.7 pp below the pre corona level
- Core CPI inflation fell to 1.2% during the spring, from 2.4%. Thus, the first corona impact has been deflationary. However, the rapid increase the past two months signals that there will be no permanent deflationary impact
- Headline CPI is up 1.3% y/y, up from 1.0% in July. Energy prices are on way up



The most corona hit prices are on the way back. Food, furnishing accelerating

Public transport (airline tickets) and hotels are still far down – but are recovering

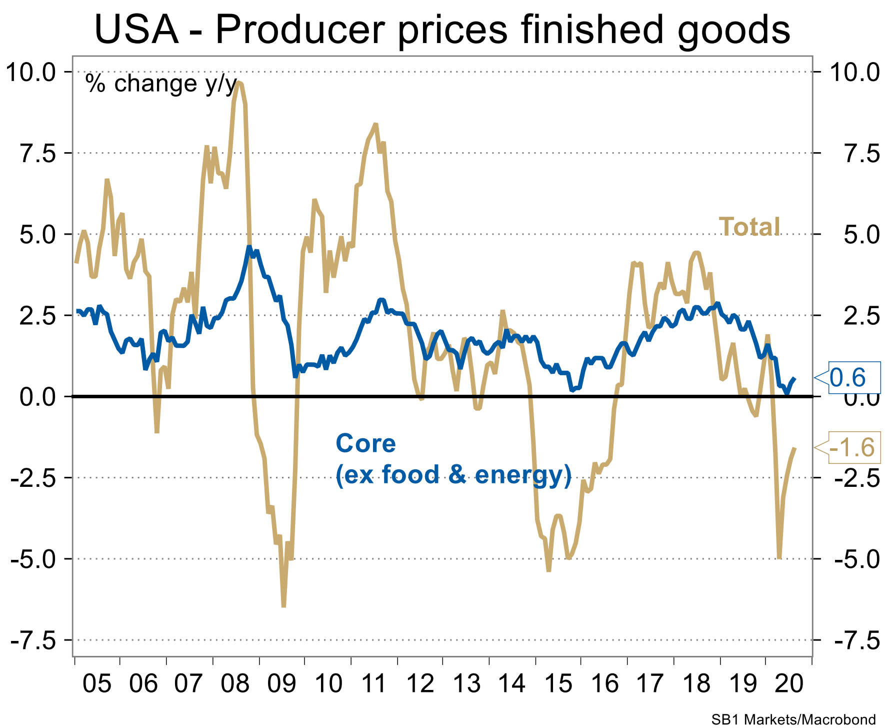


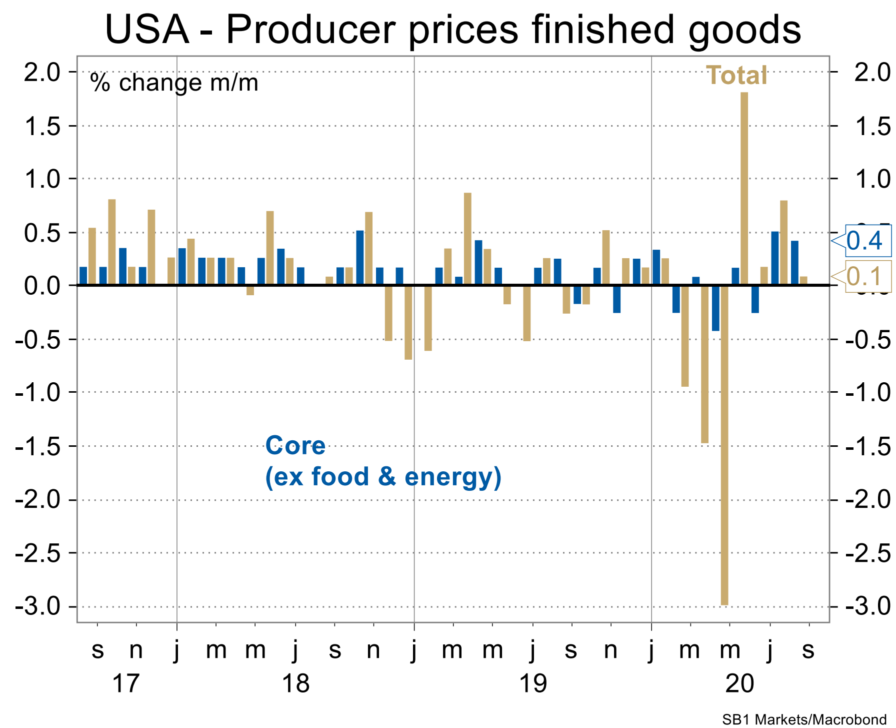


- Just some few components of the CPI contributed to the ‘corona’ setback: Public transport (airline tickets), lodging (hotels), apparel, and partly recreation (parks etc). Other components of the CPI have not slowed
- Food prices are up 4% y/y, corona has no doubt boosted demand among households, as in Norway
- Medical care up 4.5%

Core producer price inflation slowly moving upwards

Total finished goods prices down 1.6% y/y – from -5% in April

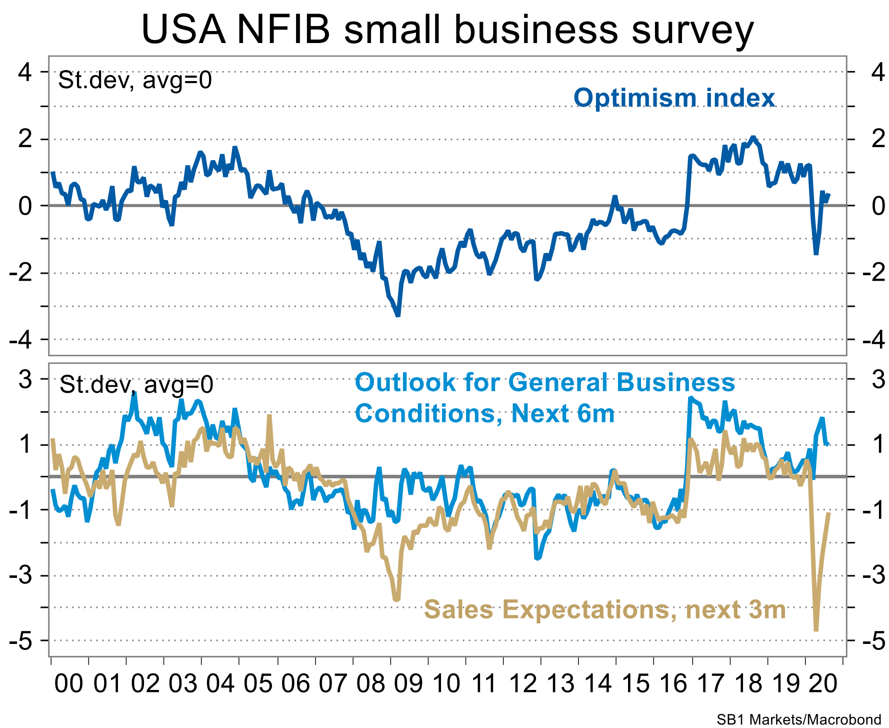


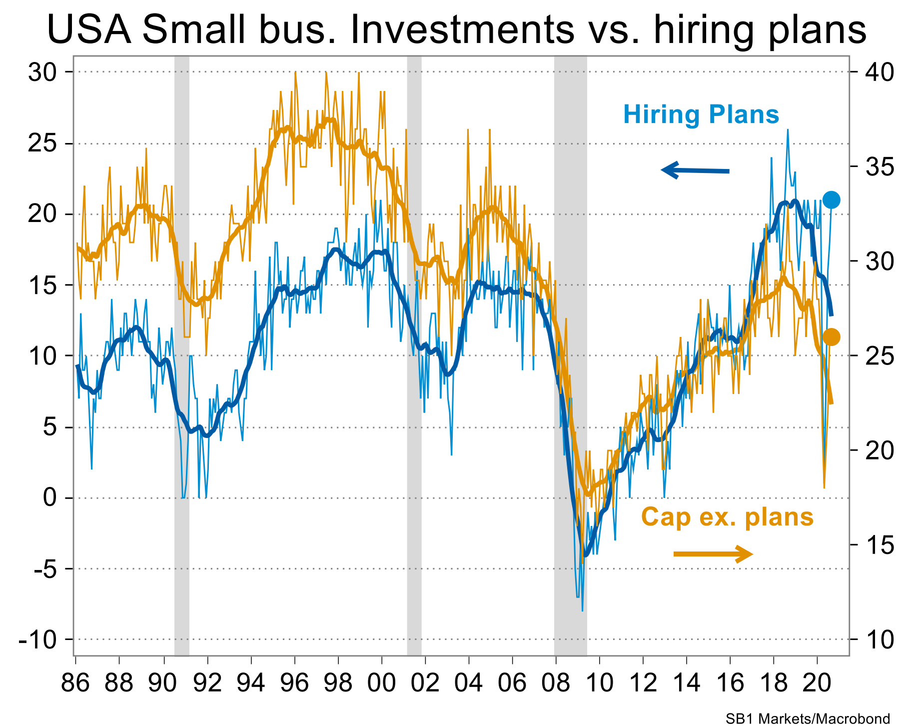


- Core finished goods x food & energy PPI rose by 0.4% m/m in Aug and the annual rate edged up to 0.6%, reflecting a slow comeback of demand . Core producer price inflation has slowed rapidly since early 2019
- Headline PPI rose 0.1% m/m and the annual rate rose to -1.6%. Total PPI inflation fell rapidly in March and April, along with the economic crisis and falling energy prices when the pandemic hit
- Core producer price inflation suggests that consumer inflation will remain muted for some time

Small businesses' optimism at OK level, sales expectations still below par

Businesses are reporting higher hiring plans – and more surprisingly – difficulties attracting labour

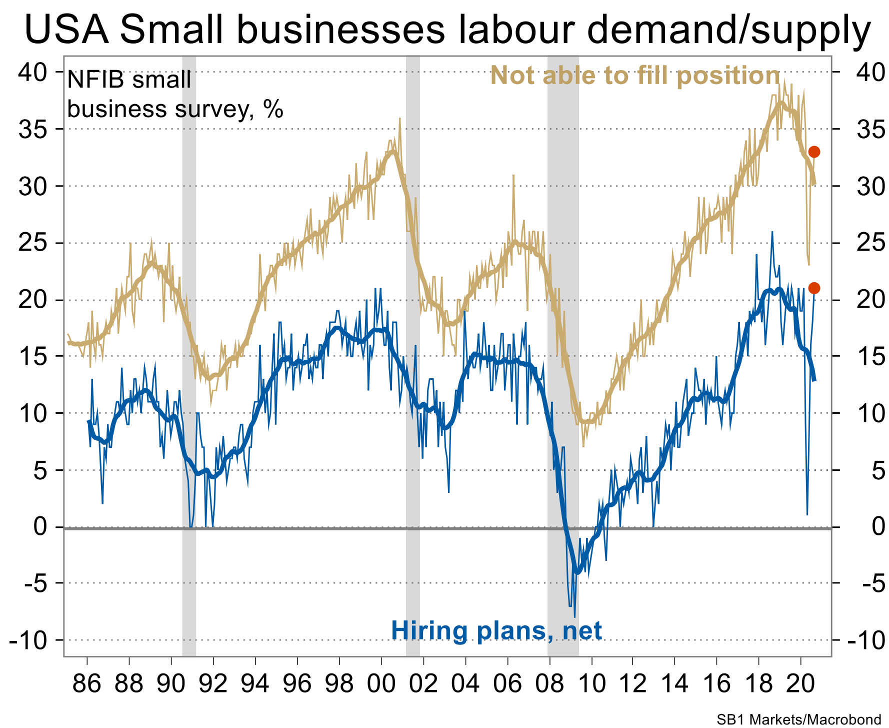


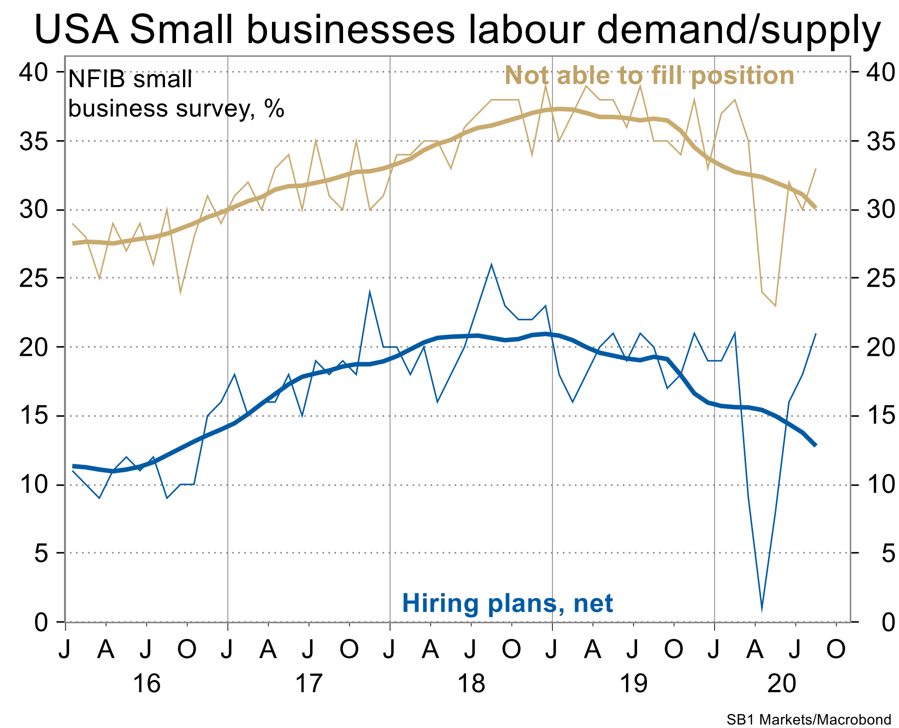


- The NFIB optimism index edged up in August, slightly more than expected. The level is just above average. The expectation index, the outlook for the next 6 months, inched down but have been surprisingly strong through the Covid crisis, as the total optimism index
  - » Sectors: Transportation and services are the most downbeat, construction and manufacturing in the lead
- Businesses slashed their sales expectations during the corona downturn. Expectations have recovered substantially but they are still not upbeat
- Investment plans have almost returned to a normal level, and companies are not signalling substantial cuts in investments (but no growth either)
- Hiring plans are back at the pre corona level – and their plans are rather aggressive. However, given that employment is still 8% below a pre corona level, it is not strange that hiring plans are pretty aggressive – and it do not signal a tight labour market. *However, check next page…*

Small businesses plan to hire again – and they are not able to fill vacant positions

It’s hard to calibrate the hiring plans, as so many companies have cut their workforce lately

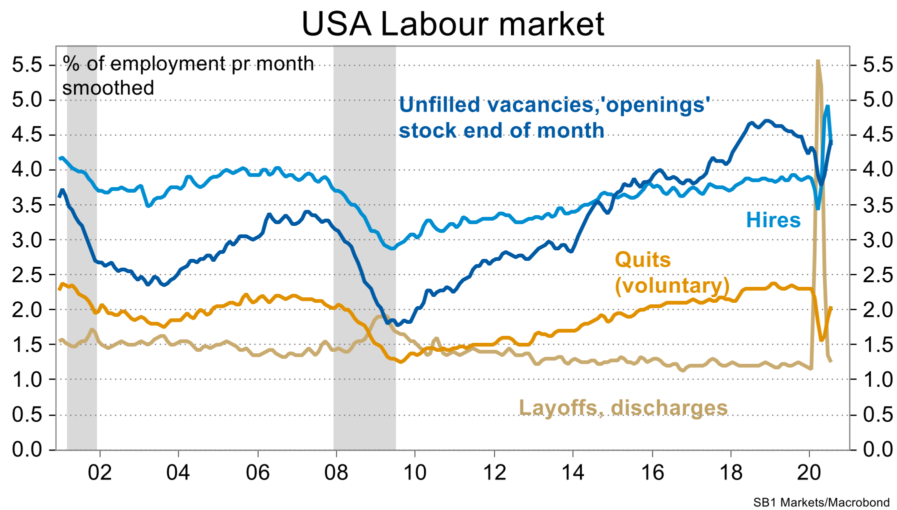




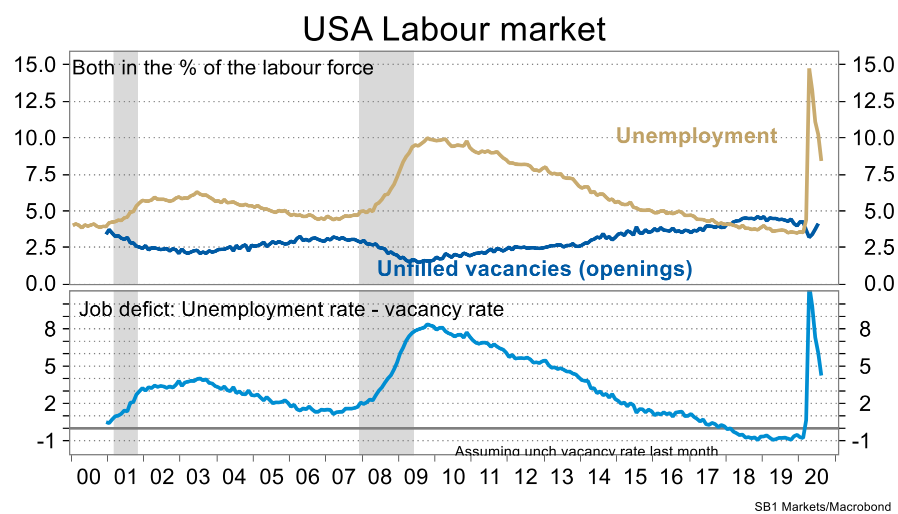
- However, it is remarkable that so many companies are reporting that it is unusually difficult to fill vacant positions when the unemployment rate is as high as now. Perhaps the unemployment benefits are too generous now? More on this conundrum here

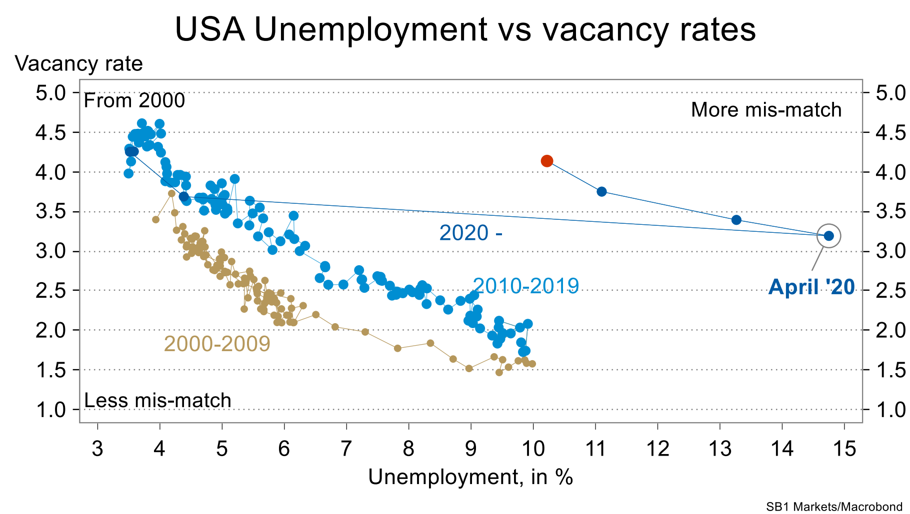
Layoffs down to a normal level. Hiring fell in July, still very high

The number of unfilled vacancies is now just slightly higher than before corona, rather strange?



- Why are companies still not able fill their vacancies, even if the unemployment rate is far above a normal level?
  - » More mis-match between the unfilled positions and the unemployed (geography, qualifications)?
  - » More unemployed prefer to remain unemployed due to the >100% compensation rate for a majority of the unemployed?
    - These JOLTS data covers July, where unemployed received the USD 600 extra federal support – which was cut or sharply reduced from August. Will more unfilled position be filled up?
- This JOLTS unfilled vacancies stats confirm the small business survey, companies are NOT able to fill their vacant positions!

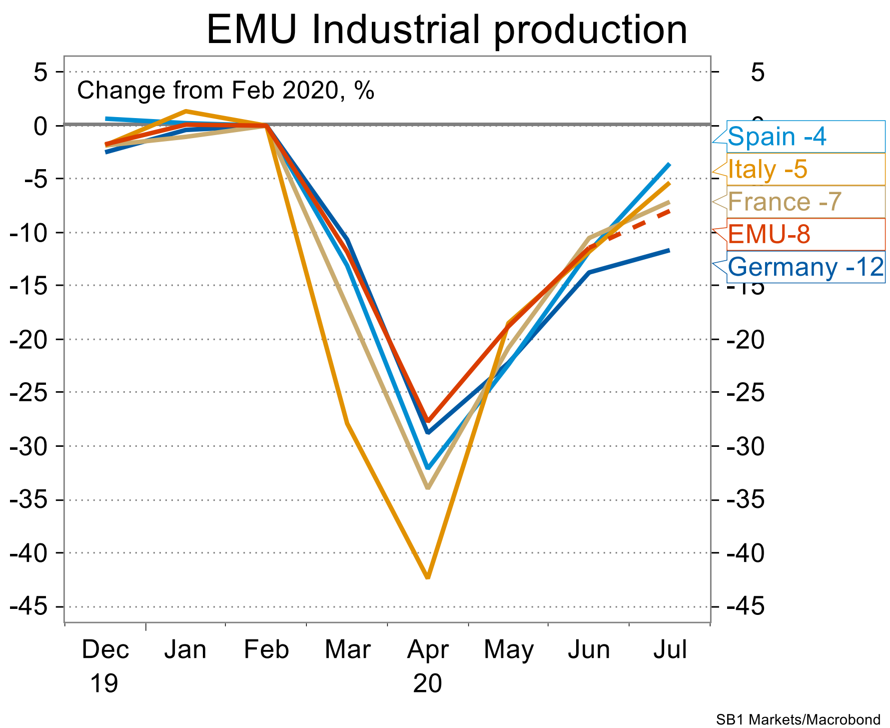


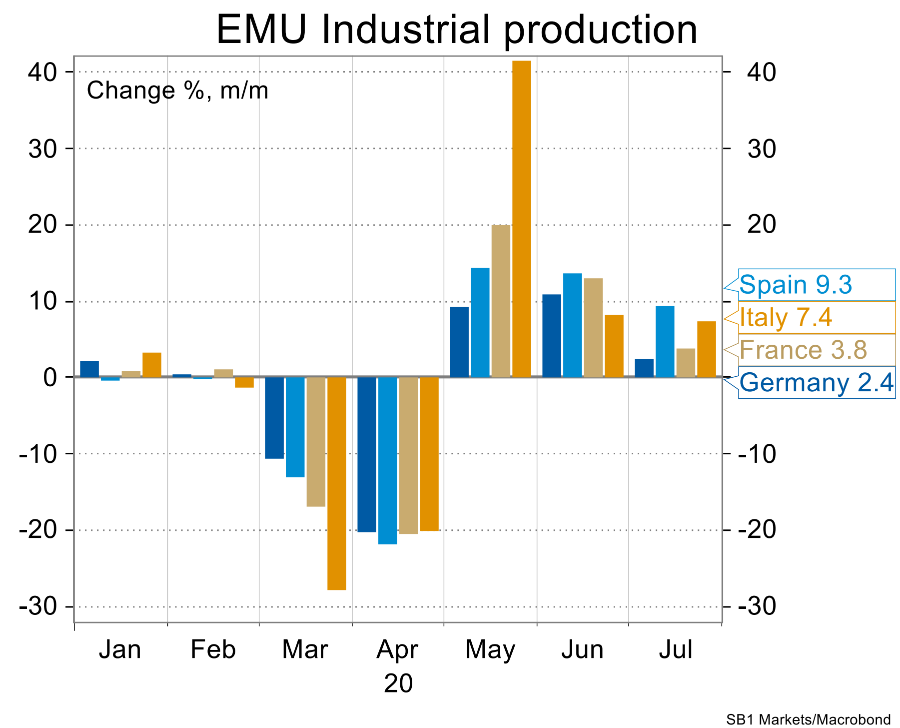


SpareBank 1 MARKETS

Manufacturing production rose less than expected in Germany, France, in July

We estimate a 3.9% lift in total EMU production in July, still an 8% gap vs the pre corona level

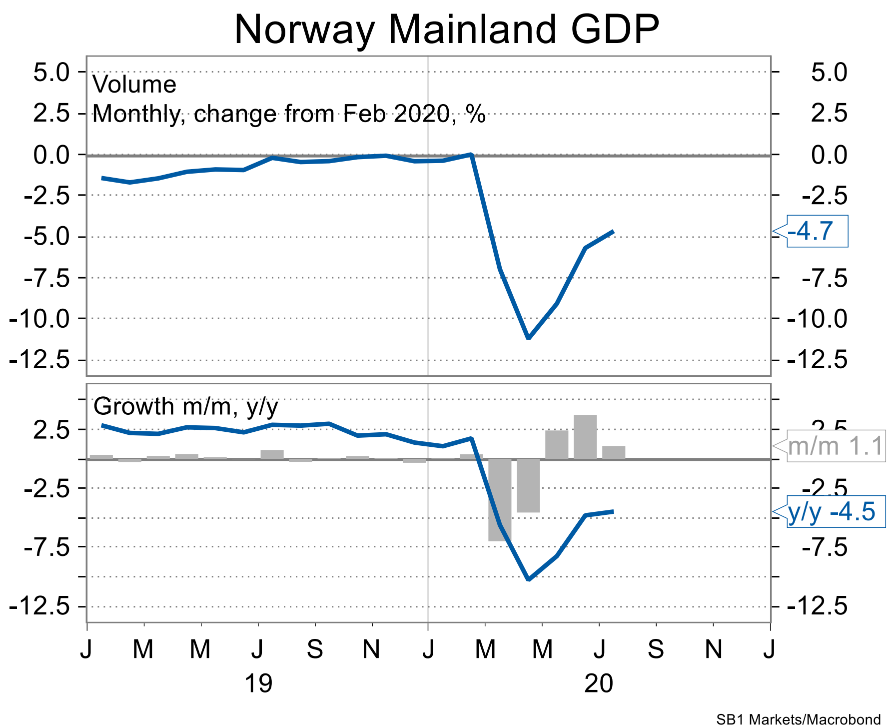




- Germany reported a 2.4% m/m rise in July, below the expected 4.6%. Production is slowly recovering but remains miles below the old levels. France up 3.8%, expected 4.9%. Production in Spain rose 9%, more than expected – and it is less than 4% below the February level

GDP up 'just' 1.1% m/m in July, less than expected, still 5% below par

Mainland GDP is recovering, still almost 5% below the February level – as services are still struggling

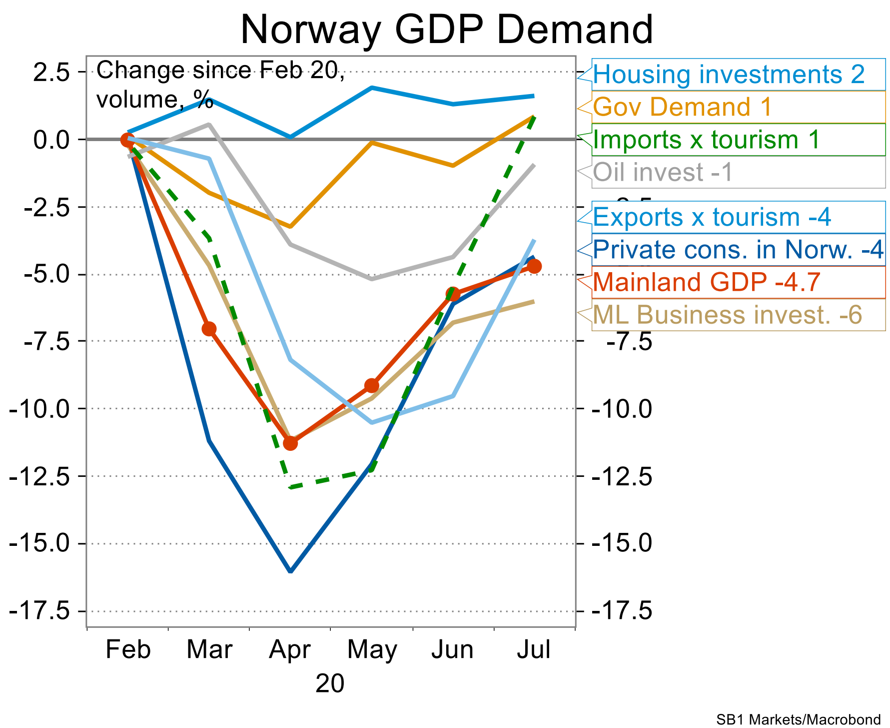


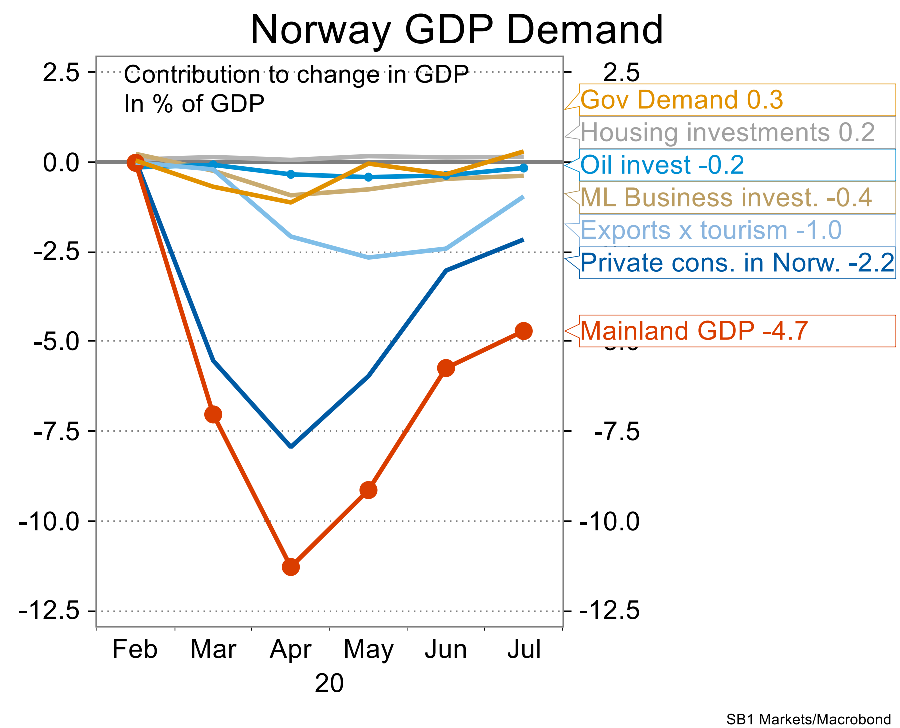
- Mainland GDP rose 1.1% m/m in July, we expected 2.5% (consensus at 2.0%)
- Mainland GDP is up 7.4% from the bottom in April, still 4.7% lower than the Feb level, and down 4.5% y/y.
  - » We expect GDP to continue to recover substantially the next months but remain below the pre corona trend
- If activity remains unchanged through Aug and Sept, Q3 GDP will be up 4.4%
  - » Some services will probably report lower activity in August, both hotels & air transport, following the July surge
- Travel, hotels, most cultural activities and partly restaurants will most likely not recover completely until the virus treat fades, either because it is becoming (even) less aggressive or a vaccine is widely available

- <u>On the demand side:</u>
  - » Most demand components rose in July from June
  - » Private consumption made the largest contribution to growth, for the 3rd month, but is still 8% below the February level (due to lower consumption abroad – while Norwegians' consumption in Norway is close to unch from Feb
  - » Government demand continued to pick up
  - » Business investments rose marginally, as did oil investments. Oil investments have fallen sharply since last year
  - » Exports and imports both increased in July

Most demand components up in July, still below the pre corona level

Private consumption has been the main drag, now the main contributor in the recovery

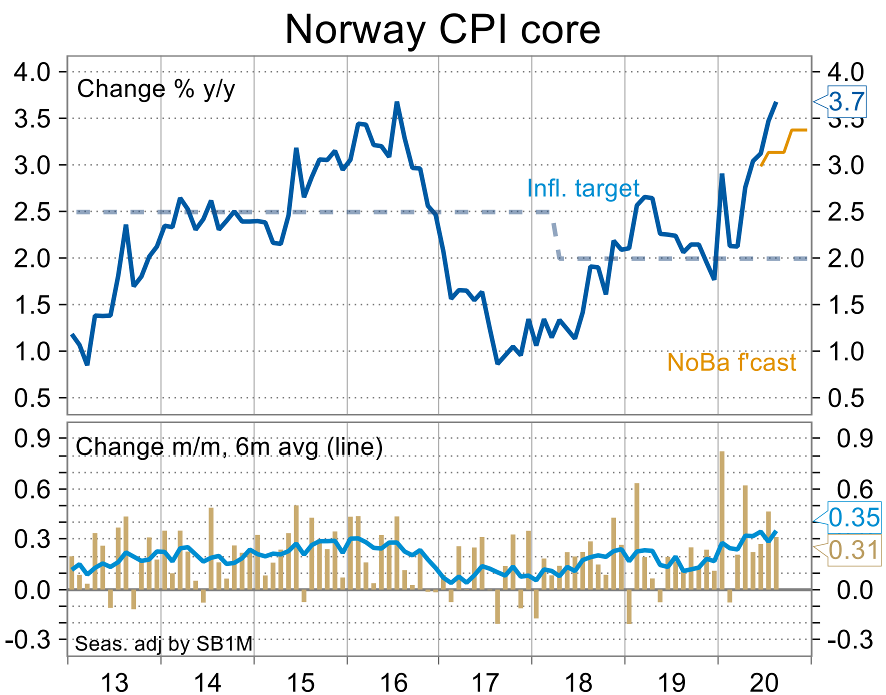




- Private consumption, exports have been the largest negative factors but oil investments as well as Mainland business investments have also contributed at the downside
- Since May, most demand components have recovered. Government demand is back at the pre corona level and oil investments just marginally below. Private consumption, trade and business investments are all still far weaker than in February

Core CPI accelerated to 3.7% in August! Most likely not a lasting problem

Inflation is running well above the target, highest in 4 years. Total inflation still moderate at 1.7%

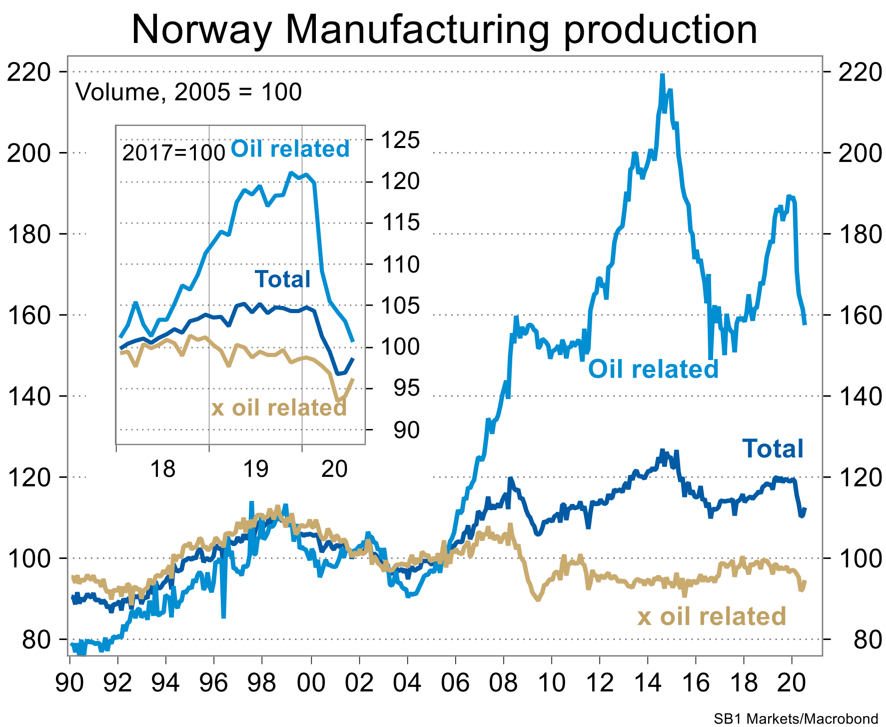


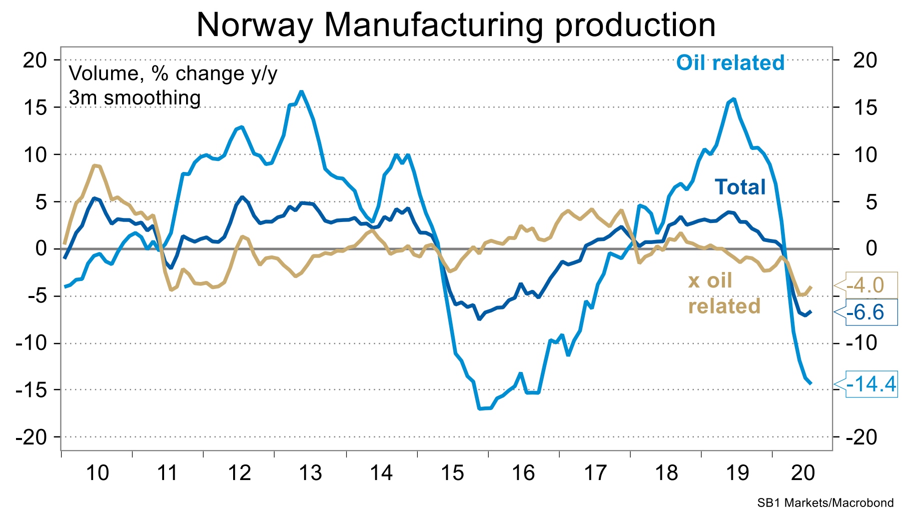
SB1 Markets/Macrobond

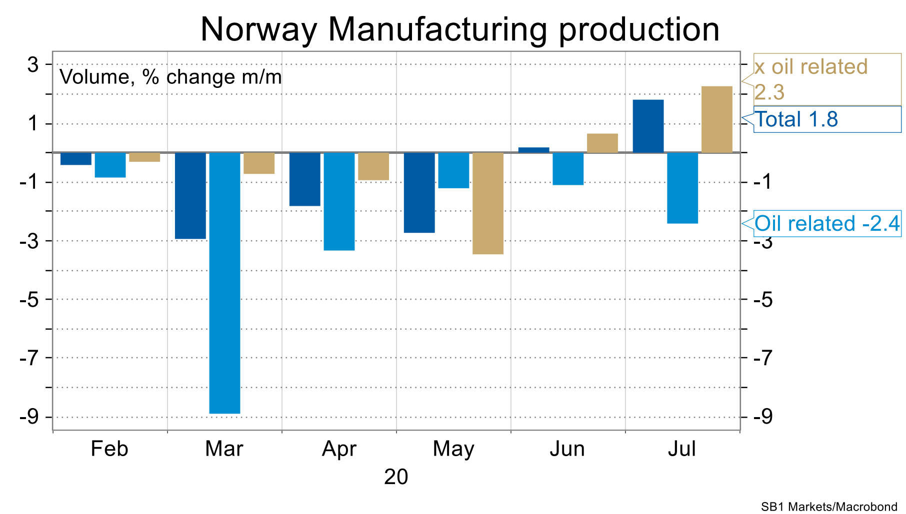
- CPI-ATE (ex. energy and taxes) inflation rose 0.2 pp to 3.7% y/y in August, we and consensus expected a downtick to 3.4%. Inflation is running well above Norges Bank's forecast, the bank expected a 3.1% average in Q3
  - » Prices rose 0.3% m/m (s.a), we expected 0.1%
  - » Inflation is above 2% for all major sectors, except housing and clothing/footwear
  - » Import prices have increased faster than our models indicate, now up 4.6% y/y, bringing core inflation up
- Total inflation accelerated to 1.7%, up 0.4 pp. Electricity & gasoline prices – explains 1.5 pp of the divergence to the core CPI
- **The price outlook**
  - » Impacts of the corona crisis are mixed
    - A weaker economy suggests low inflation. Wage inflation is no doubt on the way down. However, strong demand for goods, may lead to wider (profit) margins
    - The weak NOK has lifted inflation, however, this impact will soon fade as the NOK has stabilized
    - Energy prices have fallen
  - » Our take is that the overall impact will be a slowdown in inflation. But it may take some months before these changes are reflected in the CPI
  - » Anyway, CPI inflation will not have any material impact on Norges Banks and monetary policy the coming months. Wage growth will no doubt slow. At the Sept 24 meeting, Norges Bank will probably blame temporary factors and project a slowdown the coming quarters

Manufacturing up 1.8% in July, down 5% since Feb

Production rose more than expected in July, thanks to non-oil sectors. Oil related has fallen enough?







- Oil related manufacturing production has fallen by more than 15% since early 2020. Oil investments have fallen less – and may be stabilising the coming months. Little downside risk from here? Or some upside potential?
- Production in other sectors is down just 2% since Feb (however, it was rather soft before corona hit, trending slowly down since late 2018)
- Surveys, including the weak August PMI, signal a decline in production but not increased activity in manufacturing among our trading partners

The Calendar

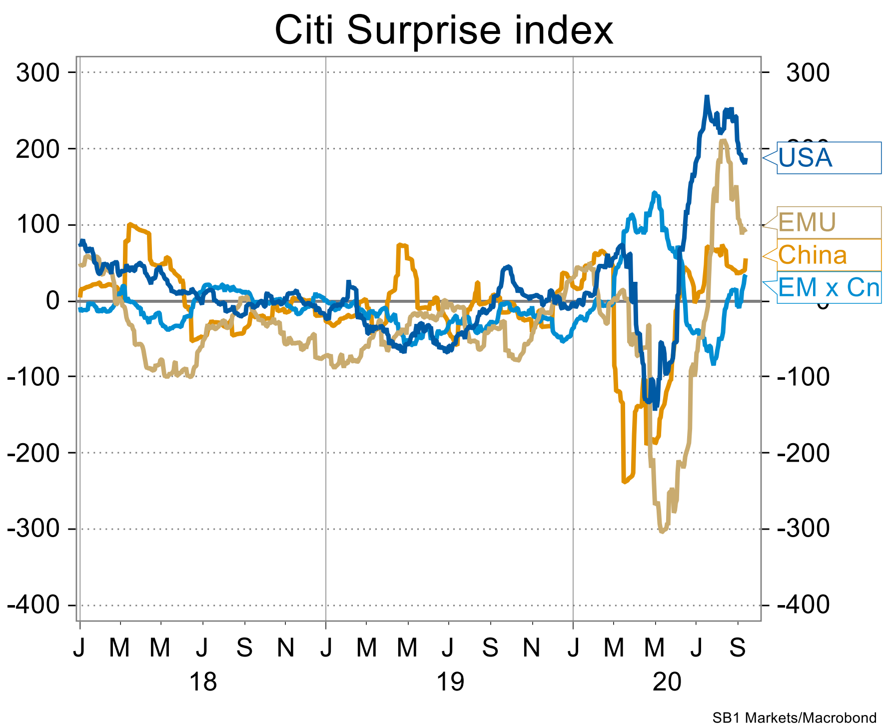
Time	Count.	Indicator	Period	Forecast	Prior
Monday Sept 14					
03:30	CH	New Home Prices MoM	Aug	--	0.5 %
06:00	SW	Unemployment Rate, Registered	Aug	--	5.7 %
11:00	EC	Industrial Production MoM	Jul	4%	9.1 %
Tuesday Sept 15					
04:00	CH	Industrial Production YoY	Aug	5.1 %	4.8 %
04:00	CH	Retail Sales YoY	Aug	0.0 %	-1.1 %
04:00	CH	Investments YTD YoY	Aug	-0.5 %	-1.6 %
08:00	NO	Trade Balance	Aug	--	-1.8b
08:00	UK	Average Weekly Earnings YoY	Jul	-1.3 %	-1.2 %
08:00	UK	ILO Unemployment Rate	Jul	4.1 %	3.9 %
09:30	SW	Unemployment Rate, LFS	Aug	9.2 %	9.2 %
10:00	NO	Norges Bank Region Network Survey	Aug	(0.5)	0.08
10:00	NO	Homebuilders' Survey	Aug		
11:00	EC	Labour Costs YoY	2Q	--	3.4 %
11:00	GE	ZEW Survey Expectations	Sep	68.8	71.5
14:30	US	NY Fed Empire Manufacturing	Sep	7	3.7
15:15	US	Manufacturing Production	Aug	2.3 %	3.4 %
Wednesday Sept 16					
08:00	UK	CPI Core YoY	Aug	0.7 %	1.8 %
14:30	US	Retail Sales Advance MoM	Aug	0.9 %	1.2 %
14:30	US	Retail Sales Core (Control Group)	Aug	0.3 %	1.4 %
16:00	US	NAHB Housing Market Index	Sep	78	78
20:00	US	FOMC Rate Decision	sep.16	0-0.25%	0-0.25%
Thursday Sept 17					
	JN	BOJ Policy Rate	sep.17	--	-0.1 %
11:00	EC	CPI Core YoY	Aug F	0.4 %	0.4 %
13:00	UK	Bank of England Bank Rate	sep.17	0.1 %	0.1 %
14:30	US	Building Permits	Aug	1520k	1495k
14:30	US	Housing Starts	Aug	1478k	1496k
14:30	US	Philadelphia Fed Business Outlook	Sep	15	17.2
14:30	US	Initial Jobless Claims	sep.12	825k	884k
Friday Sept 18					
01:30	JN	CPI Ex Fresh Food, Energy YoY	Aug	-0.1 %	0.4 %
06:00	SW	House Prices, Valueguard			
08:00	UK	Retail Sales Ex Auto Fuel MoM	Aug	0.5 %	2.0 %
14:30	US	Current Account Balance	2Q	-$158.0b	-$104.2b
16:00	US	Leading Index	Aug	1.2 %	1.4 %
16:00	US	UoM Consumer Sentiment	Sep P	75.00	74.1
Monday Sept 21					
03:30	CH	1-Year Loan Prime Rate	sep.21	3.85 %	3.85 %

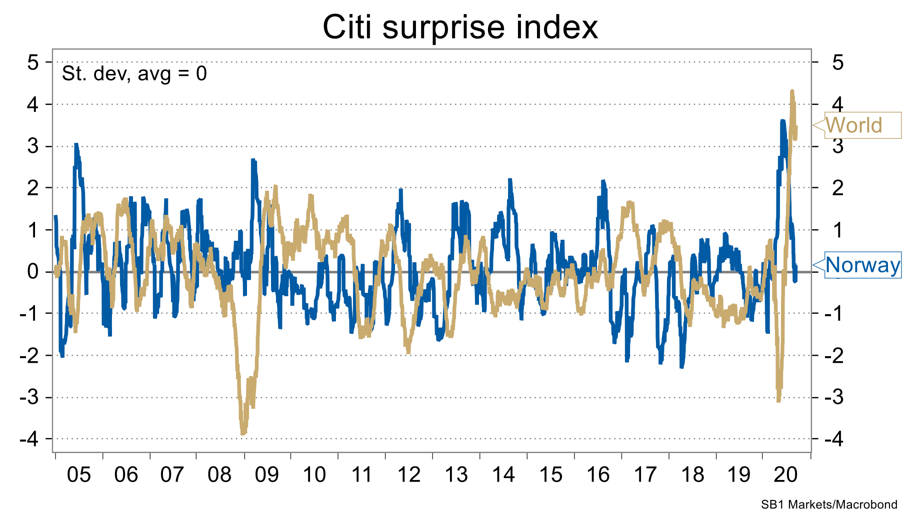
- **China**
  - **Retail sales** are on the recovery track, but still 8% below the pre corona trend. We expect another uptick in August. **Investments** have increased for 5 months, still 5% below the old trend. **Industrial production** is just marginally below par, following a brisk recovery. However, demand components will have to pick up in order to keep production growth up. Service prod. remain the laggard, still well below the old trend
- **US**
  - **The FOMC** is unlikely to announce changes in policy following the release of the updates to its monetary policy strategy in late August. At this week's meeting, the Fed is expected to offer more information on the new average inflation target, as well as an updated dot plot and projections
  - **Retail sales** have been soaring the past few months, with huge sectorial differences. Households have been heavily compensated for the downturn in wage income, boosting spending
  - **Manufacturing production** has been slowly recovering but activity is still very low. The first **September manufacturing surveys** will provide more information of the pace of recovery this month
  - **Housing starts & building permits** have moved in a V-shape, now back at the pre corona levels. Other housing market indicators are strong, too
  - **Jobless claims** came in below expectations last week, up 0.9 mill. However, the inflow is still higher than during all previous US recessions
- **EMU**
  - **Manufacturing production** is slowly turning up, we estimate a 3.4% m/m rise in July
- **Norway**
  - Unfortunately, the **Norges Bank Regional Network** has turned out to be rather imprecise when it comes to growth estimates during economic crises, just like most (all?) other business surveys. What starting point does companies refer to, and are they assessing growth over the period they are asked about. Still, the survey will provide insights on the sectorial outlook. We expect oil related industries to report a muted outlook, while other manufacturing industries should report a better growth outlook. Household services will not. We assume a 6 m forward growth indicator at 0.5, formally signalling just a 1% growth pace – but the uncertainty is too large for comfort

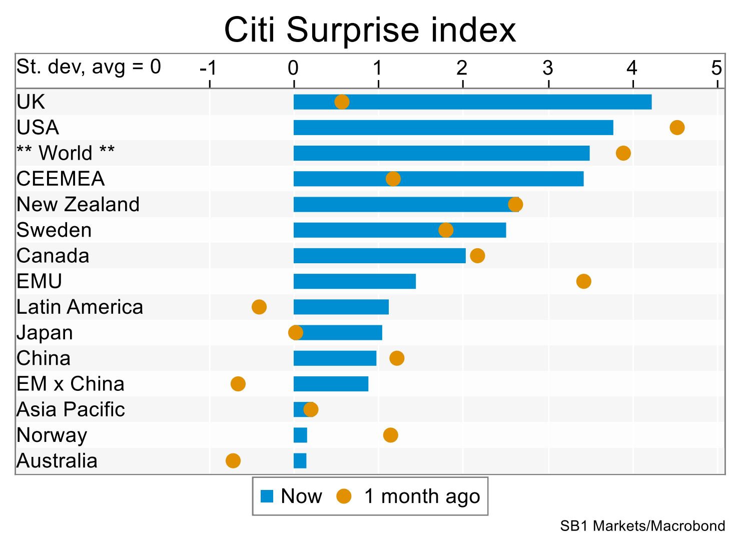
Source: Bloomberg. SB1M est. in brackets. Key data points are highlighted

Macro data are still surprising on the upside in DM, now almost everywhere!

Citi's US & EMU surprise indices have come down from their ATHs, still unusually strong





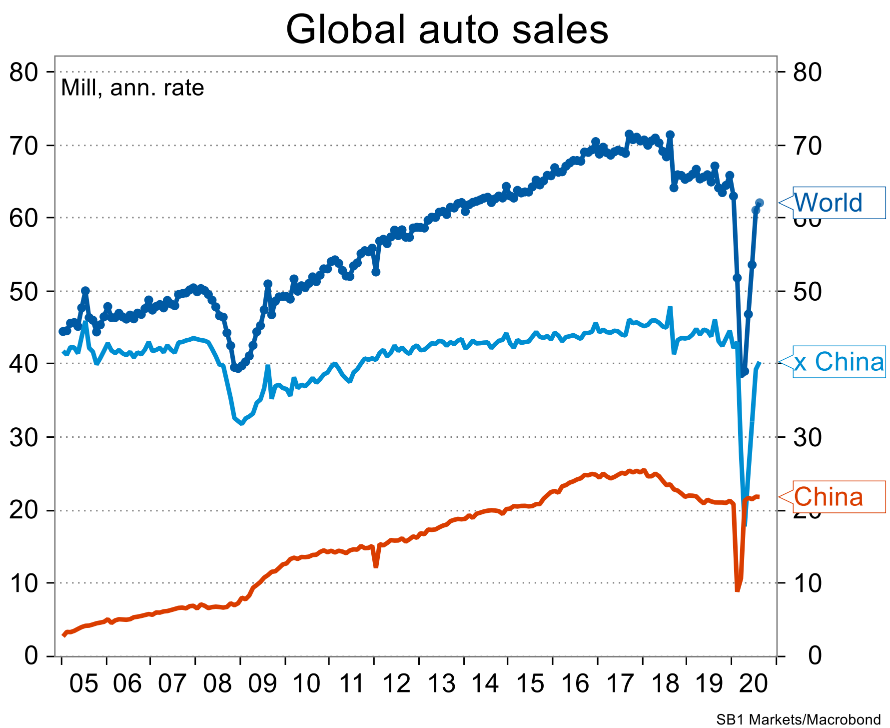


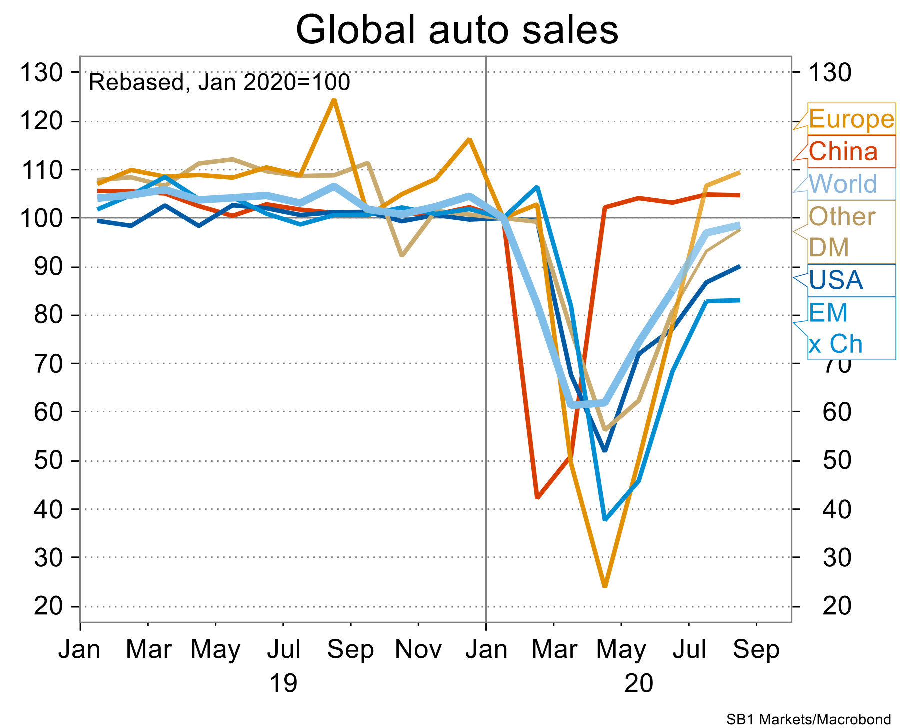
- Most major countries/regions are reporting data above expectations, just Asia Pacific is marginally below an average level (Norway and Australia close to avg)
- The US has been surprising more on the upside than ever before (data from 2003)
- EMU was close to record high some weeks ago, the index is still elevated
- China well into positive territory
- Other EMs rose to an above average level last week!

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

Global auto sales back at the (low) pre corona level, China above, EMU on par

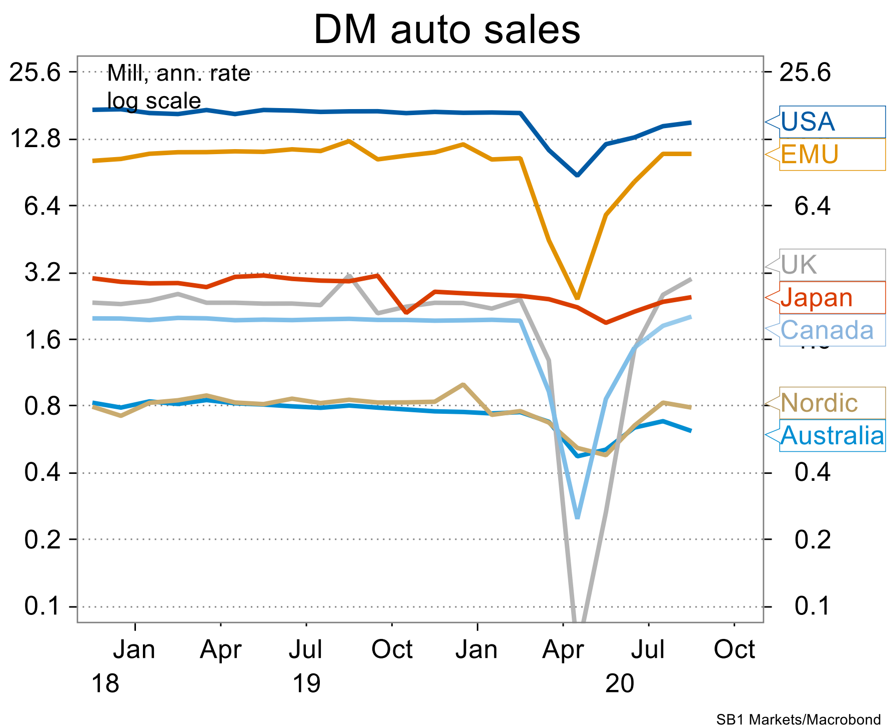
Sales marginally up in August. China above last year's sales, ROW 7% below (from -60% in April)

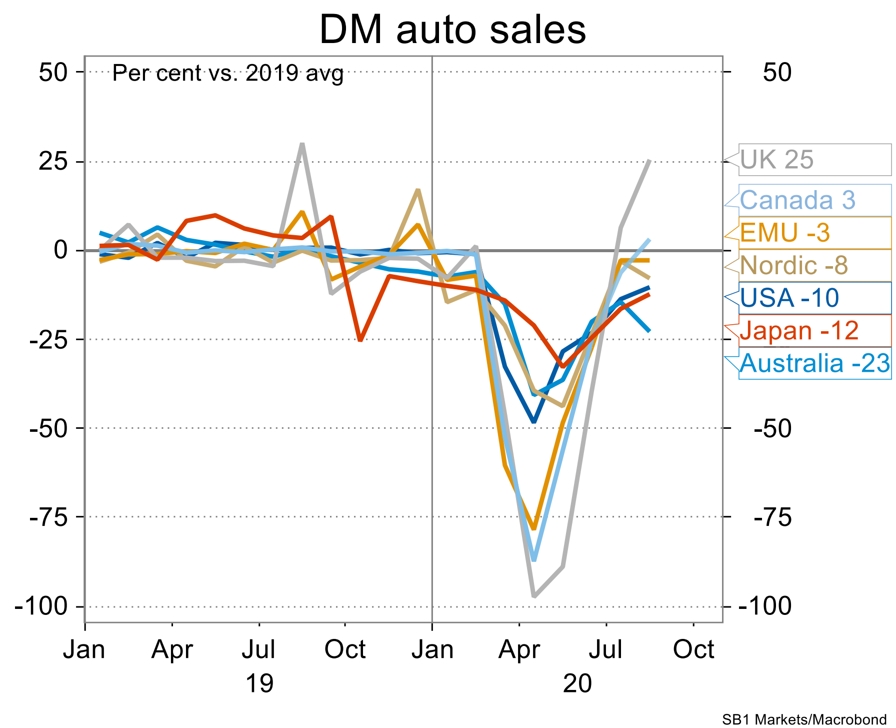




- This is the most undisputable 'V' we have on offer – data are reliable and updated. Just one caveat: Sales may now be boosted due to pent up demand – and may slow during the autumn, especially if the corona virus creates new, serious problems (which it is so far not doing)
- Chinese auto sales were flat in August, and are above both the pre corona and the avg 2019 level – which though both were rather depressed – by more than 20% vs. the pre 2018 trend. However, the corona downturn lasted just 2 months!
- Sales in Europe are back to a normal level, marginally below 2019 sales, which was the best year since 2007. US sales are still some 10% below the 2019 avg. Other DMs are just marginally (2%) below the corona level
- Sales in EM x China were probably close to flat August, after strong the previous months – broadly based. Still 17% below the 2019 avg

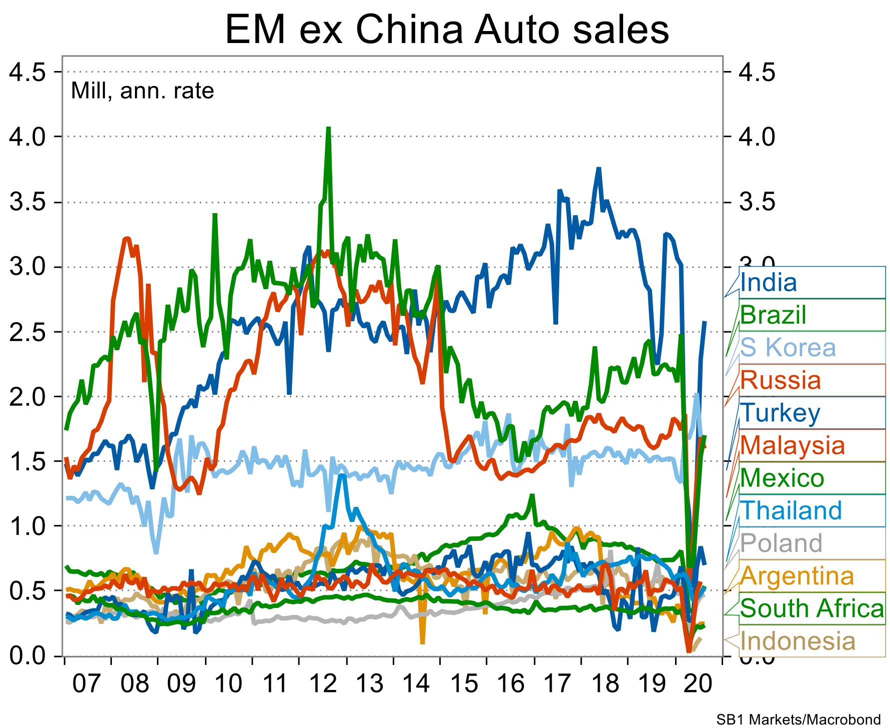
Sales up to normal levels in EMU, UK well above; other DMs still 10 – 20% down

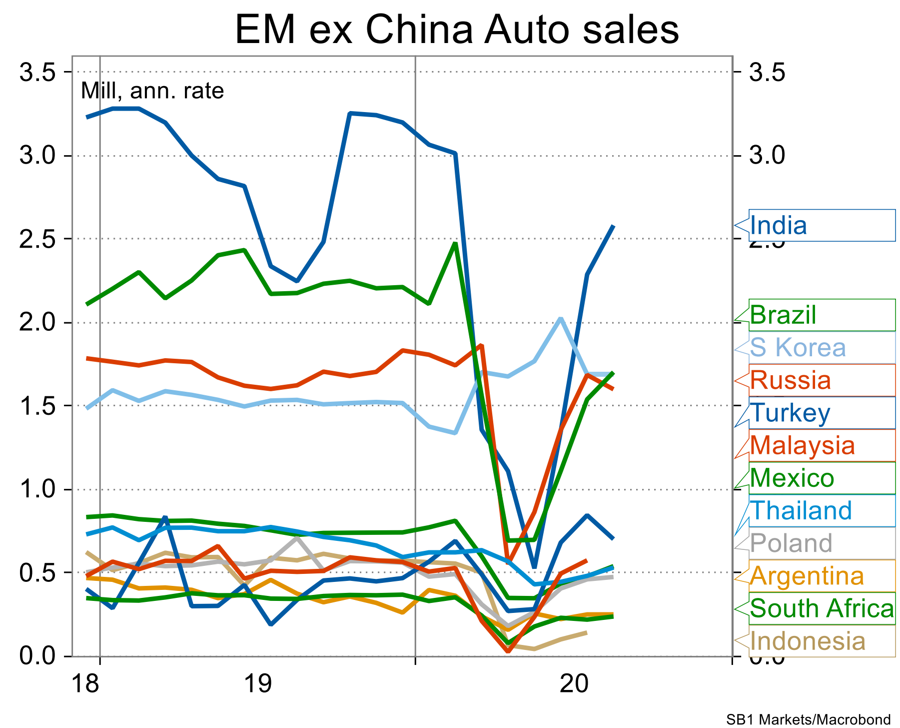




- Sales in both EMU were flat in August, close to a 'normal' level (vs 2019). UK rose sharply – to well above usual levels
- Sales in other DMs are still somewhat below par, Australia down 23%, Japan 12%

Indian & Russian sales almost back to a normal level, Brazil still below



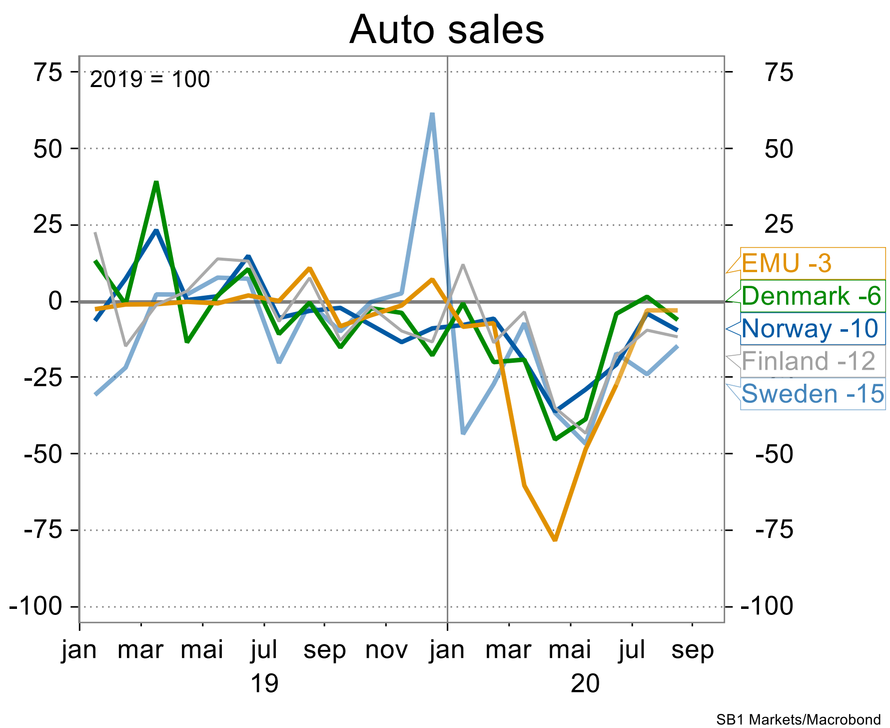


- All EMs are recovering, but most are still below the levels before corona hit. Turkey, South Korea (no August data), and Malaysia have recovered at the fastest speed - and are all above the January/Feb 2020 levels. Sales in Brazil are still down 25% vs the pre corona level. Indonesia at the bottom of the league

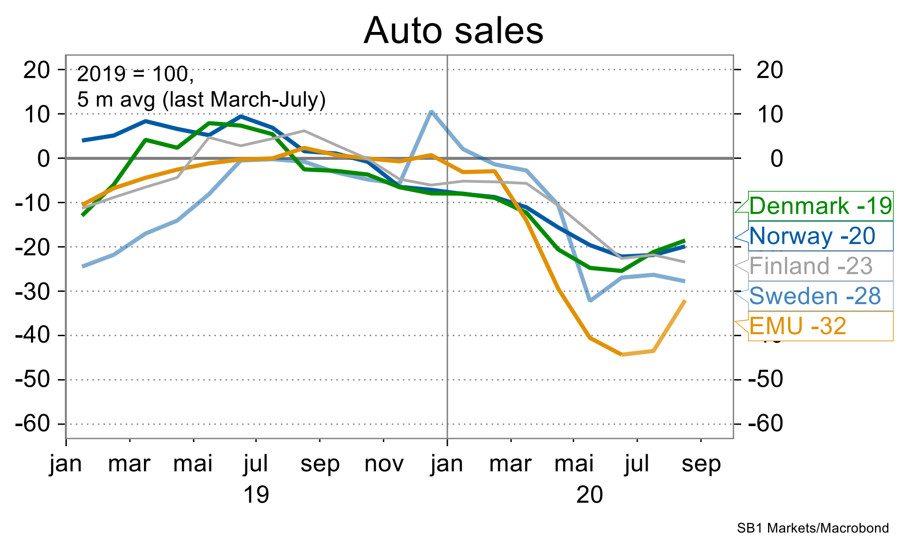
Not all countries have reported yet, and for some countries we have just plugged in figures from media reports that are not always correct

Mixed Nordic August sales: Norway, Denmark, Finland down, Sweden up

Sales in the Nordics are still below the 2019 avg level – and now outpaced by the Eurozone

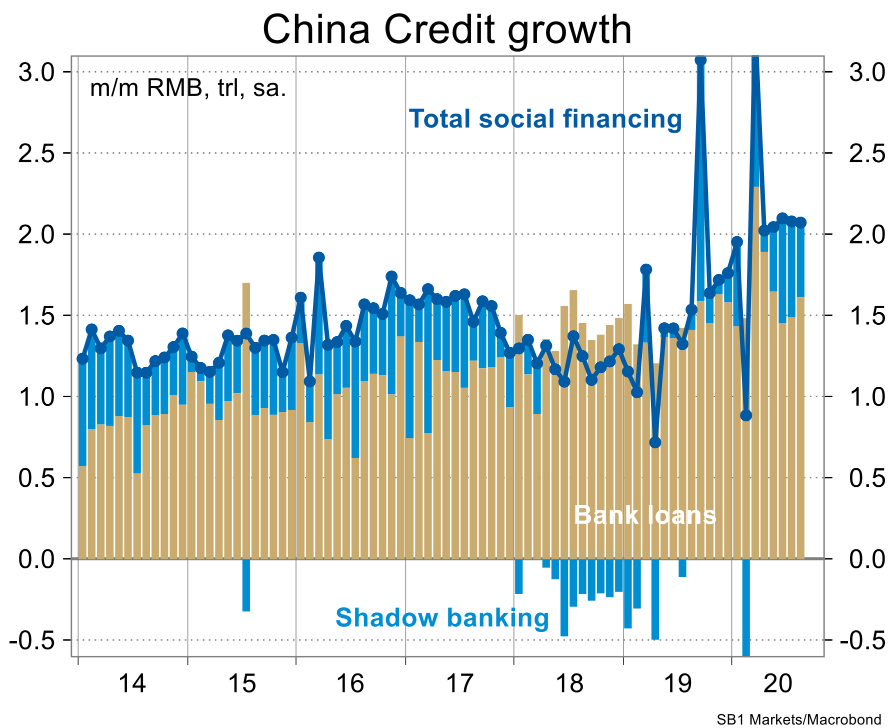


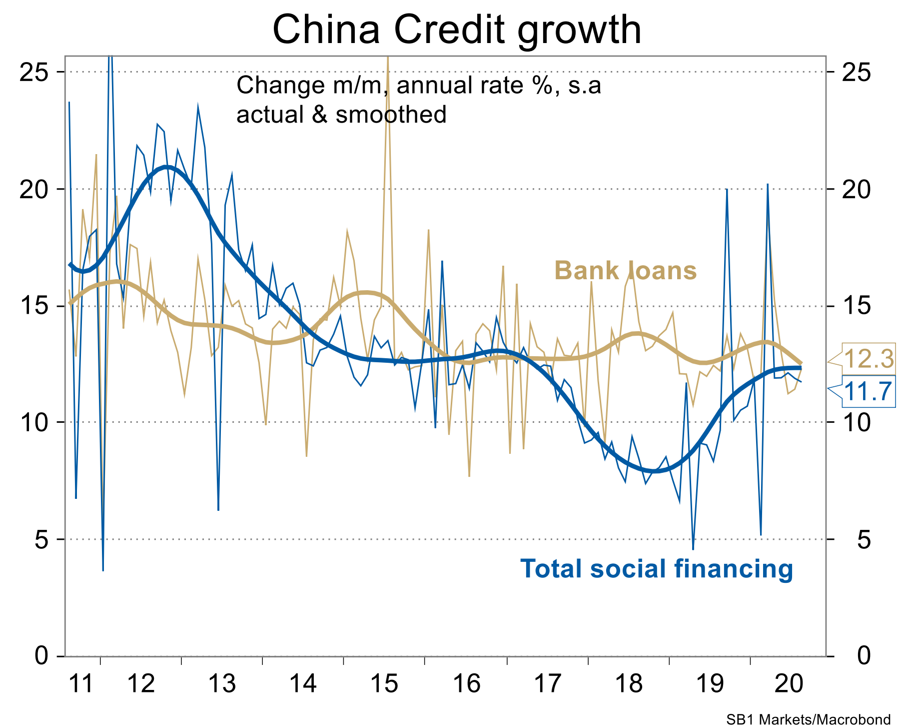
- No major differences between sales in the Nordic region during the 5 corona months (even if sales in Denmark were well ahead of the others in June), sales in the March – August period are down 19% - 28% vs. the 2019 average. Sweden at the bottom
  - » EMU sales recovered sharply in July and flat in August, the 5m avg rate at the chart below is weaker than the Nordics, as EMU sales fell much more in the spring



Credit growth has stabilised at some 12%, above trend growth in nominal GDP

Both banks and other sources (shadow banks) are contributing to total credit growth

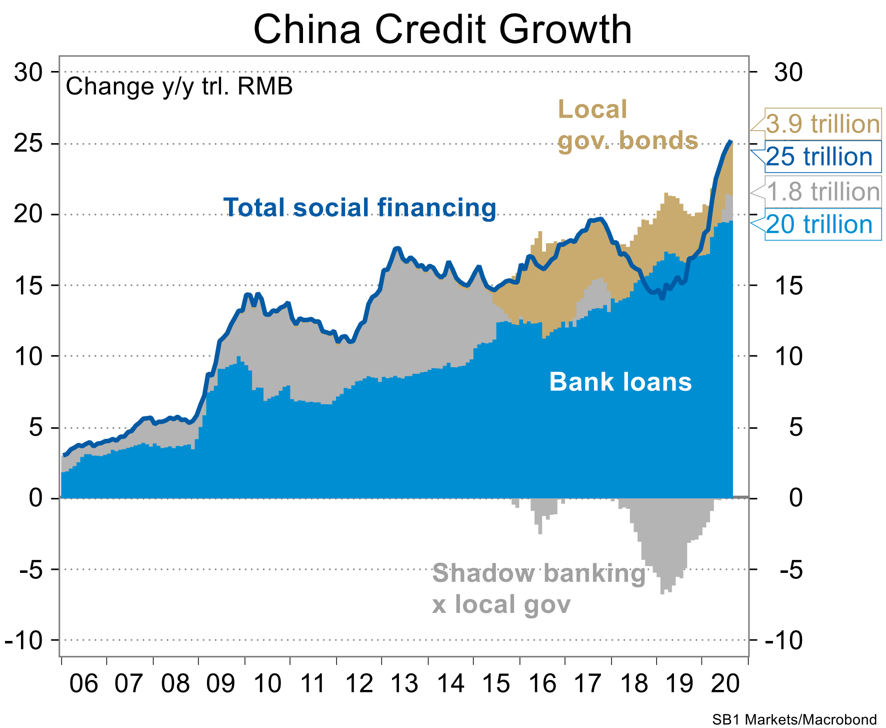


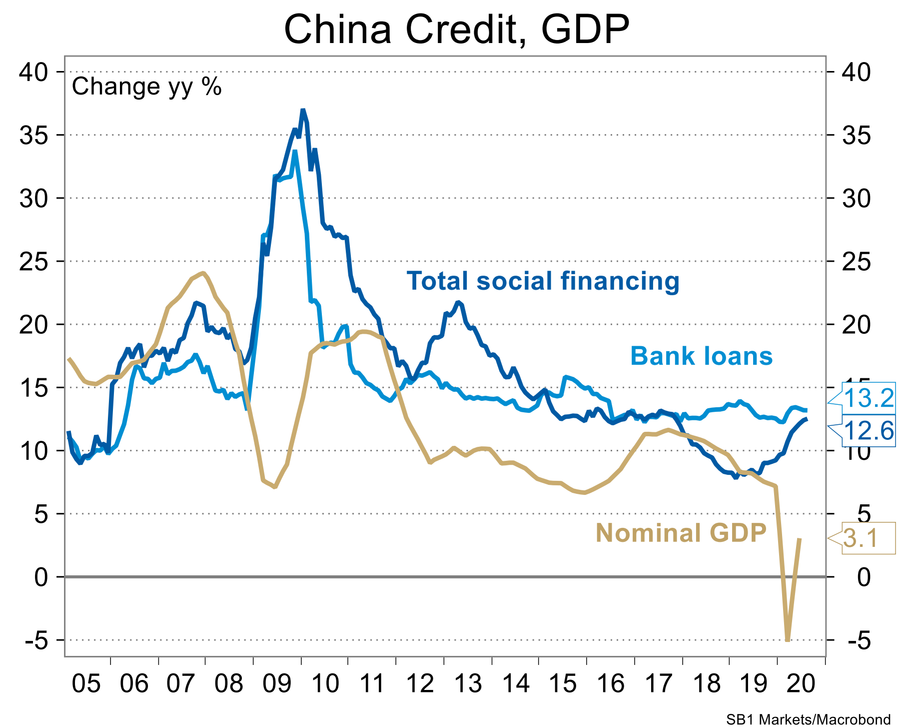


- Total credit growth has stabilised at approx 12%, if we smooth out volatile monthly figures
  - » Total credit rose 1.9 trl RMB (not seasonally adjusted), expected 2.6 trl. Banks supplied some 4/5th of the new credit (based on seasonally adj. data)
- The underlying total credit growth has been accelerating since early '19, but has flattened out recent months, at 12%
- Authorities have no doubt been trying to support growth through the credit channel during the corona setback, even if the risks are considerable

Credit growth has accelerated over the past year

More bank lending, shadow banking in plus too, from contraction

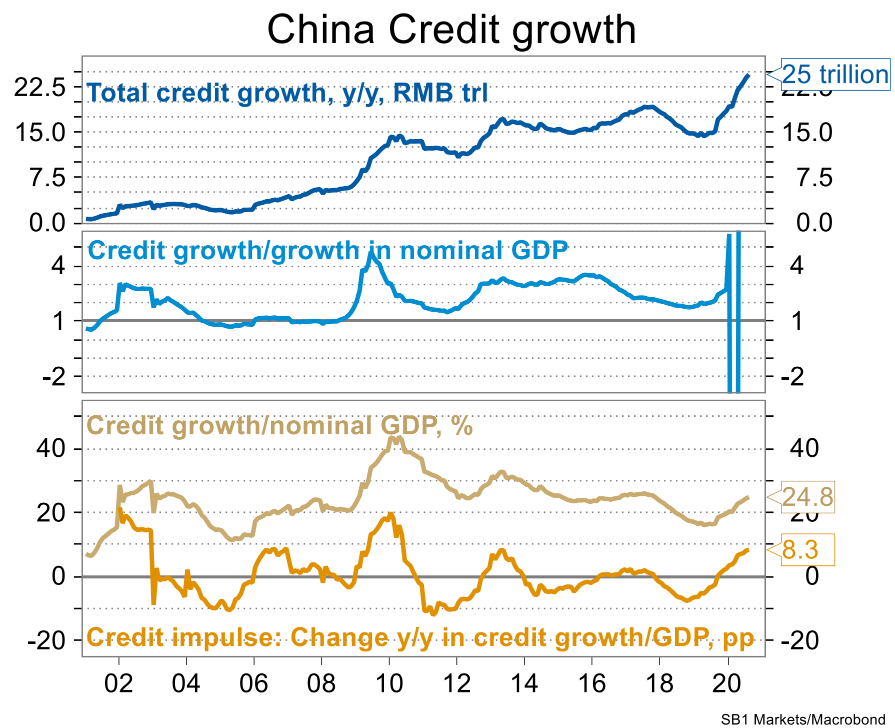


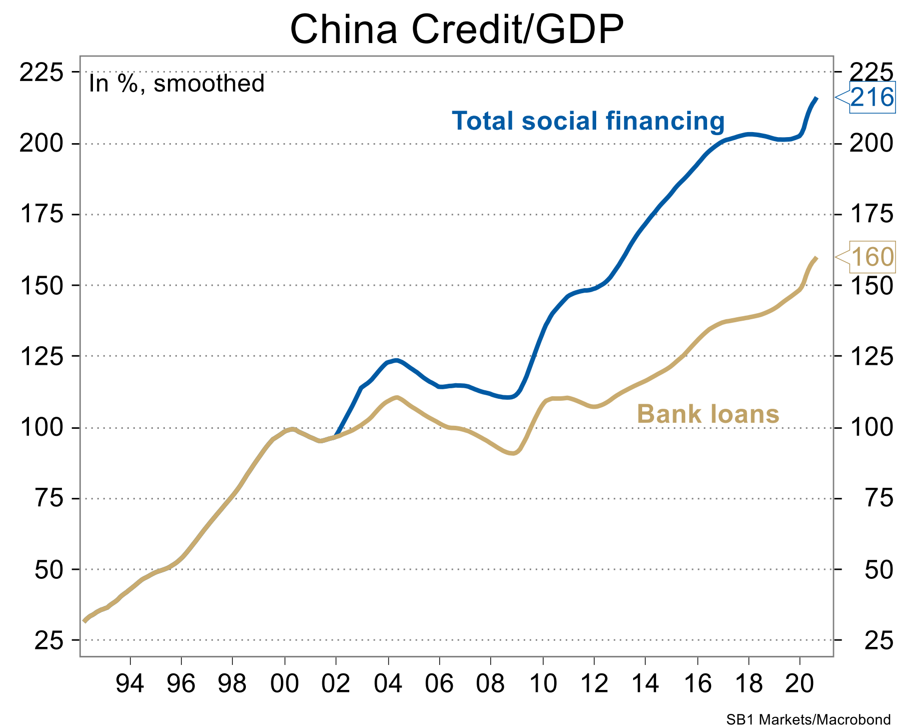


- Over the past year, total credit has grown by CNY 25 trl, this growth is equalling 25% of GDP (even before the Q1 collapse)
- Banks supplied CNY 20 trl of the y/y increase
- Local governments have not yet accelerated their borrowing by much, at least not in the bond market, still up 3.9 bn y/y
- Other credit – via the shadow credit market x local gov bonds is now marginally up y/y, by 2 bn
- Total credit growth at 12.6% is higher than growth in nominal GDP even before the corona shock – the debt ratio is increasing

The credit impulse has turned positive, and the credit/GDP ratio sharply up

Credit growth has been accelerating, whatever way we measure it

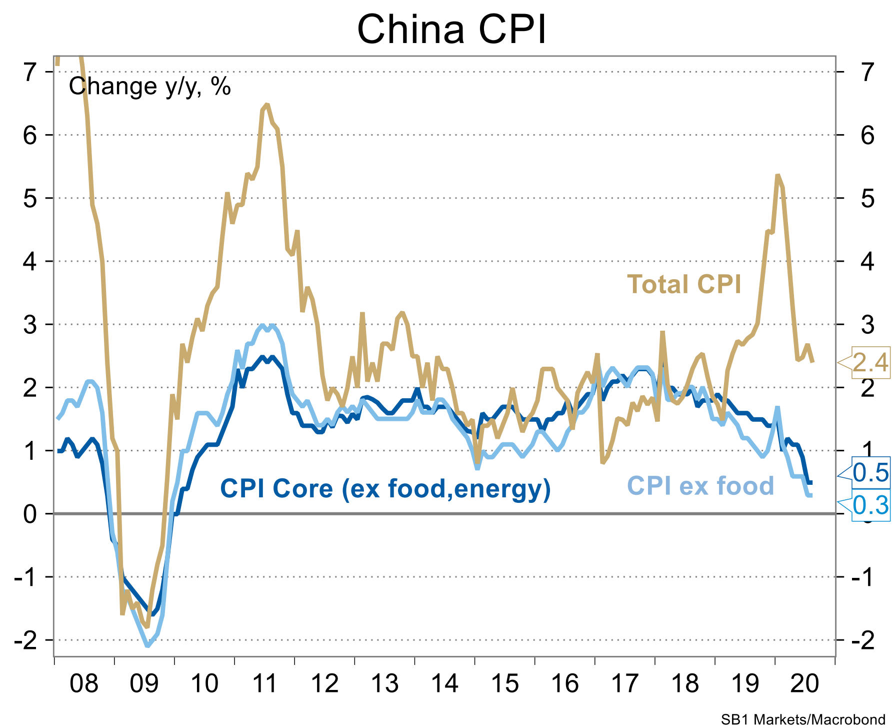


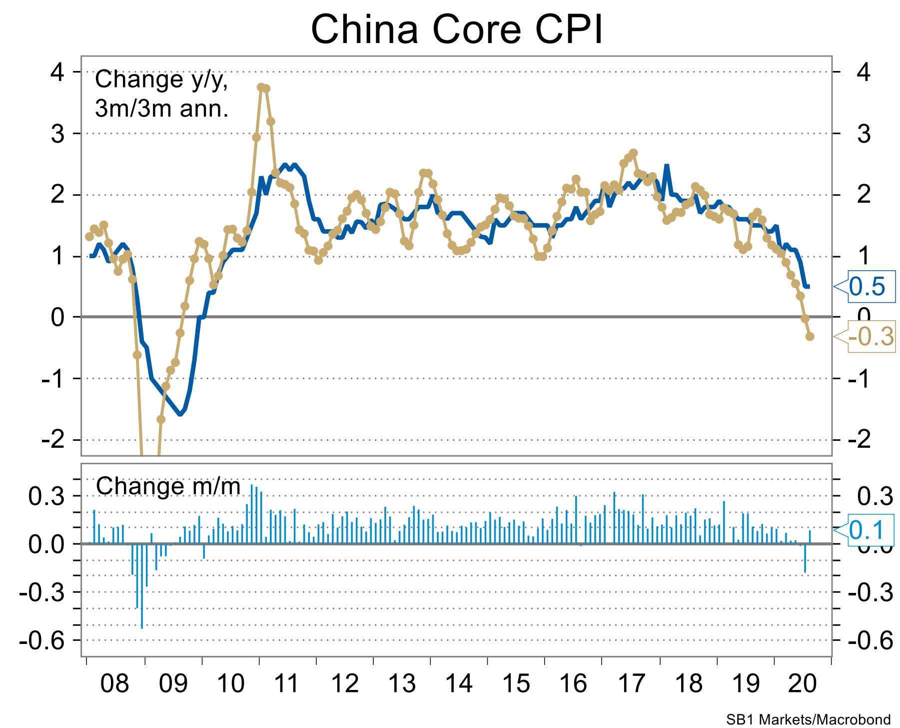


- A positive credit impulse implies that the credit growth/GDP ratio is increasing (the 2nd derivative of credit vs the GDP level)
  - » A negative credit impulse indicates credit tightening (or weaker demand) and has been associated with slowdowns in the Chinese economy
  - » Now, the credit impulse has risen well into positive territory
- We are uncertain how far the authorities are willing or able to bring growth back up, even as stimulus is needed now to support the economy. The credit/income level has flattened but the level is disturbingly high. In addition, for every RMB GDP grows, credit increases 2.8 by RMBs (given trend growth in GDP in Q1, which was not the case…), and each year's growth in credit equals 25% of GDP. That's not sustainable, long run, neither for lenders nor borrowers, as nominal GDP growth is well below 10%. The Government may succeed in increasing credit supply short term (if they dare to, vs long term risks) to stimulate the 'post' corona economy but there are risks attached

Core prices are stalling, up just 0.5% y/y, total inflation slowing to 2.4% in Aug

Core CPI up 0.1% m/m, flat at 0.5% y/y. Total down to 2.4%, food price inflation slowed (still at 11%)



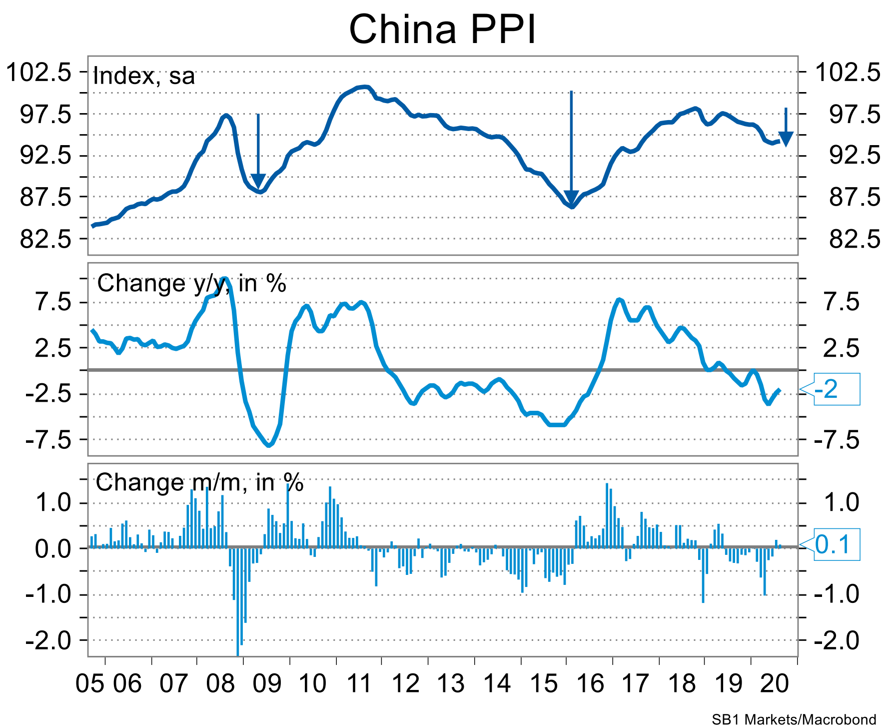


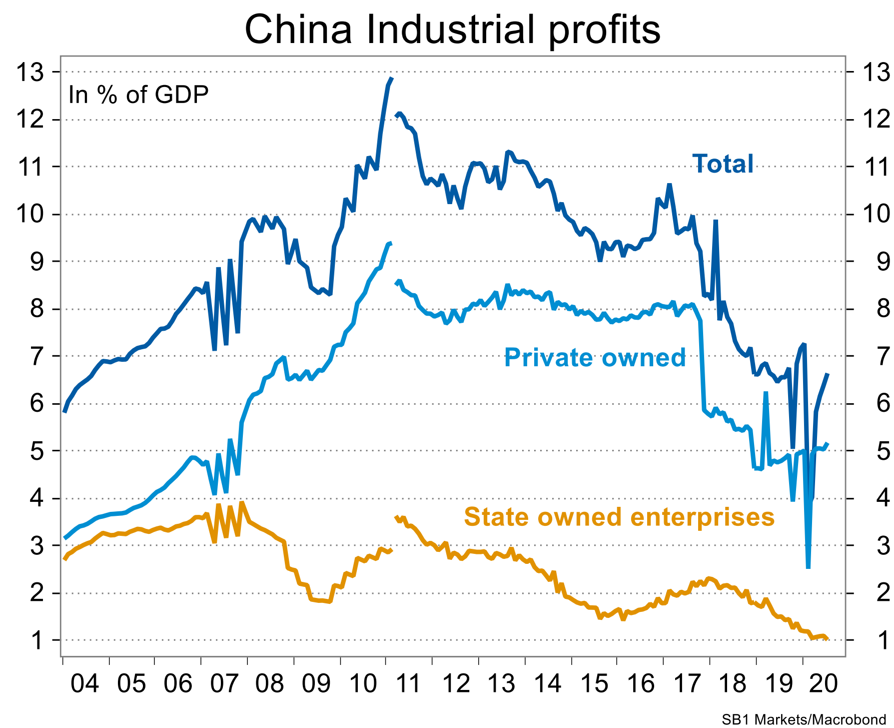
- The corona crisis has no doubt contributed to the decline core (ex energy, food) inflation since January. In August, core prices rose marginally and the annual rate was flat
- Food prices fell 0.5% m/m in August after a spike in July, and the annual rate came down to 11.2%. Food price inflation is still very high, but stabilized the past few months. The swine flu is to blame

SpareBank 1 MARKETS

Producer prices on the way down but not dramatically. Profits stabilised

PPI down 2% y/y in August, up from -3.7% in the spring – and they have stabilised m/m

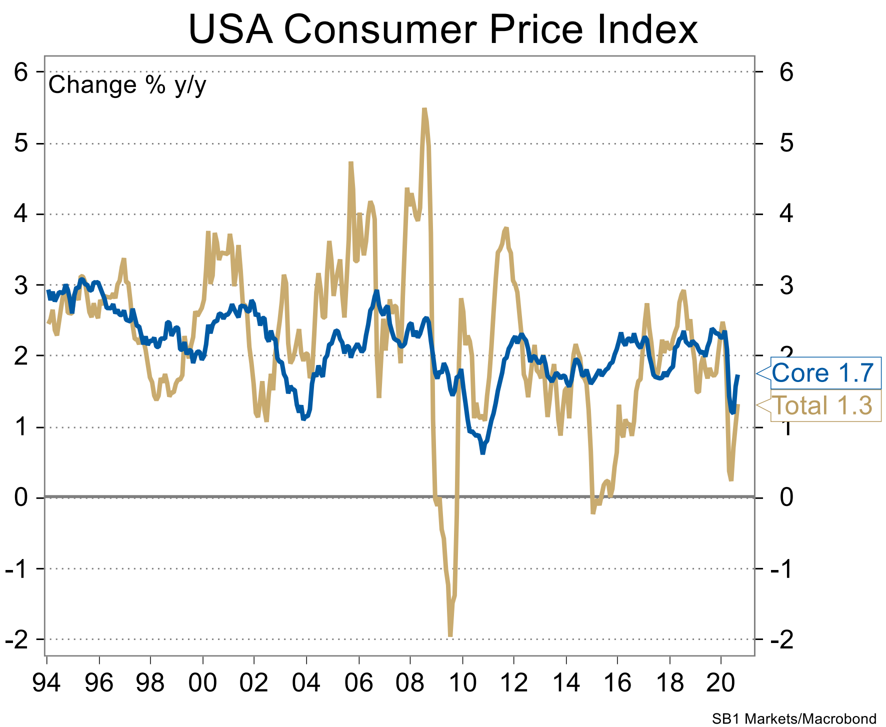


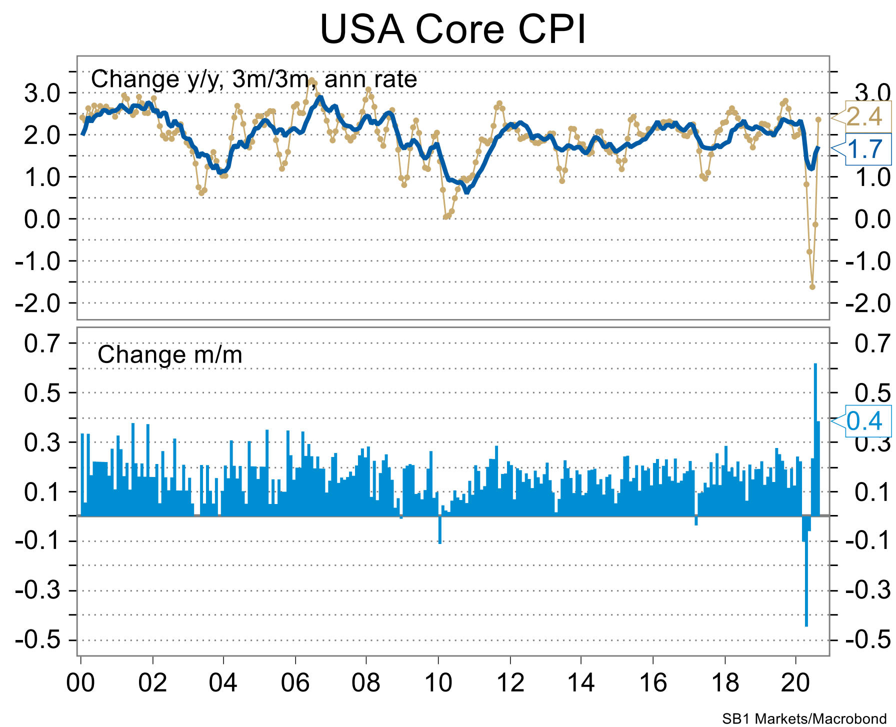


- The PPI peaked in late 2018 but prices have fallen just some 4% since then - and not much further the corona crisis. During previous setbacks, PPI has fallen up to 13% (and never less than 8%)
- Industrial profits in privately owned enterprises fell by 50% in February. Profits rose to a normal level in April/May – if we label the profit level in 2019 and early 2020 as normal - at 5% of GDP. Profits used to be far higher
- In state owned enterprises profits are falling and falling – and now equals just 1% of GDP, half the level 2 years ago
- The decline in industrial profits is not the best argument for expecting a further recovery in business investments

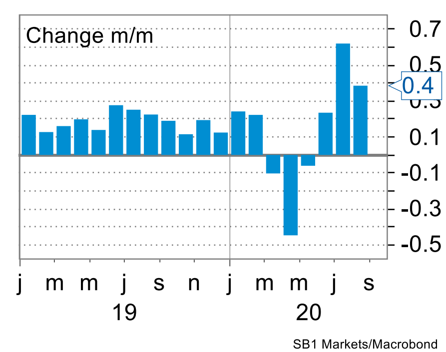
Core CPI up another 0.4% m/m in Aug, evidence of a demand comeback

Annual rate up 0.1 pp to 1.7%, expected unchanged. Vehicles, furniture and lodging boosted growth



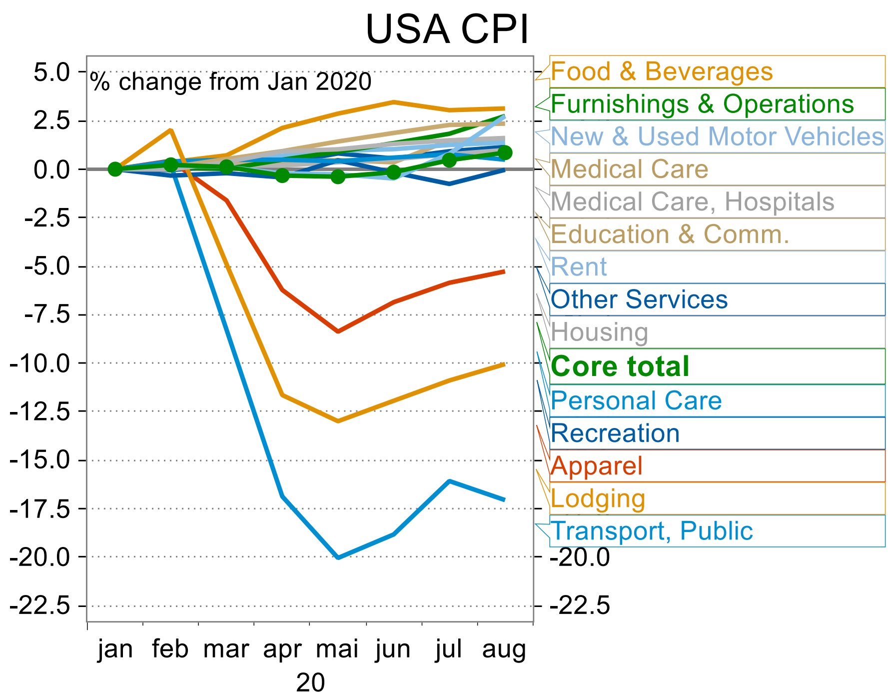


- Core CPI prices rose by 0.4% m/m in August, 0.2 pp higher than expected, following the surprising 0.6% jump in July. Annual inflation up 0.1 pp to 1.7%, still 0.7 pp below the pre corona level
- Core CPI inflation fell to 1.2% during the spring, from 2.4%. Thus, the first corona impact has been deflationary. However, the rapid increase the past two months signals that there will be no permanent deflationary impact
- Headline CPI is up 1.3% y/y, up from 1.0% in July. Energy prices are on way up

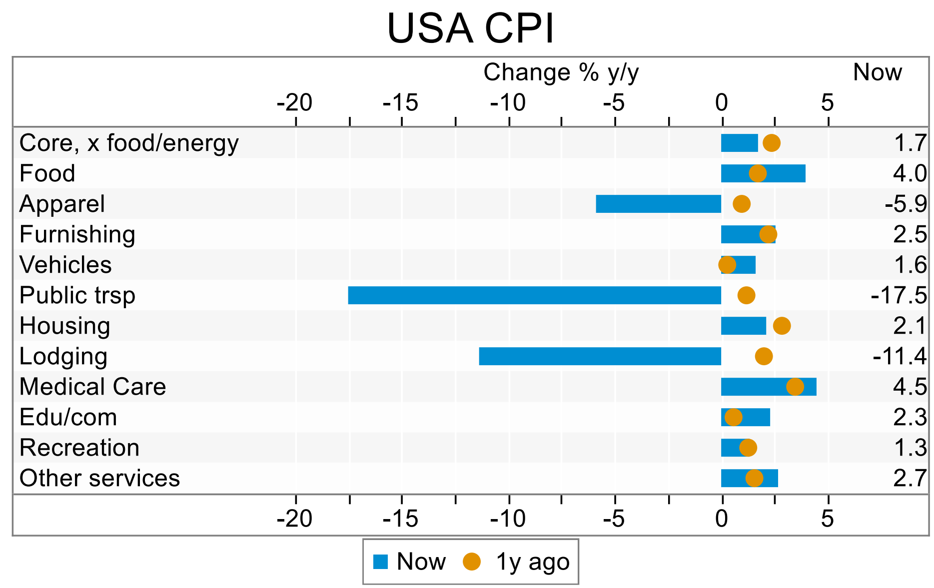


The most corona hit prices are on the way back. Food, furnishing accelerating

Public transport (airline tickets) and hotels are still far down – but are recovering



SB1 Markets/Macrobond

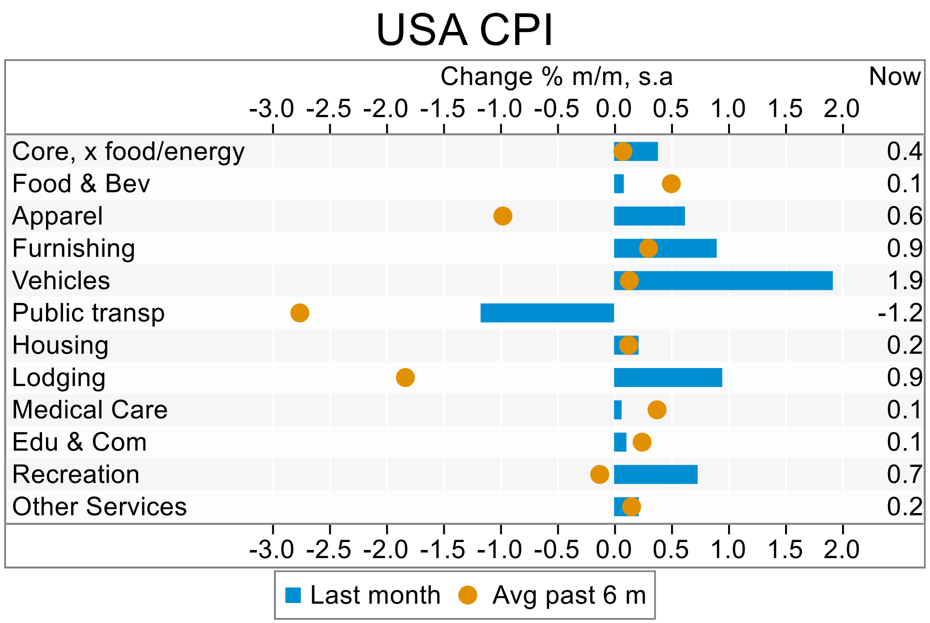


SB1 Markets/Macrobond

- Just some few components of the CPI contributed to the ‘corona’ setback: Public transport (airline tickets), lodging (hotels), apparel, and partly recreation (parks etc). Other components of the CPI have not slowed
- Food prices are up 4% y/y, corona has no doubt boosted demand among households, as in Norway
- Medical care up 4.5%

Prices on vehicles, furnishing, lodging (from a low level) rose the most in Aug

Vehicle prices lifted monthly core inflation by 0.14 pp in Aug



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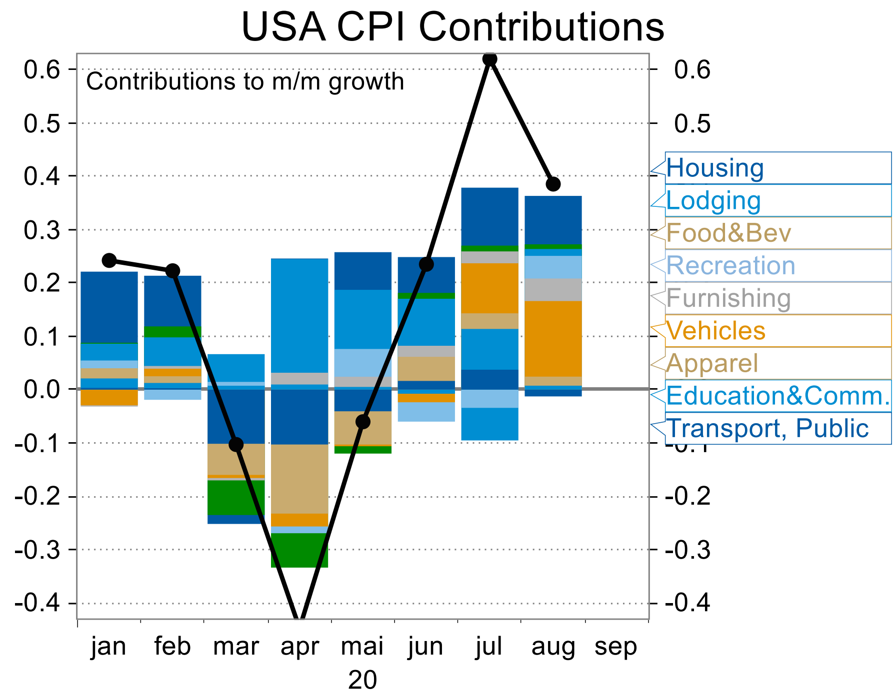
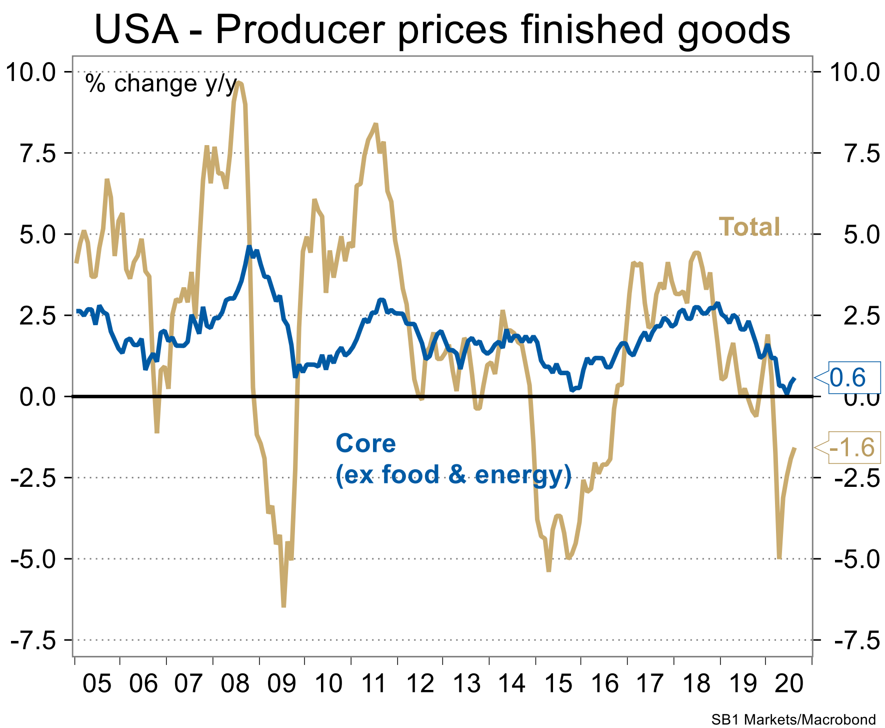
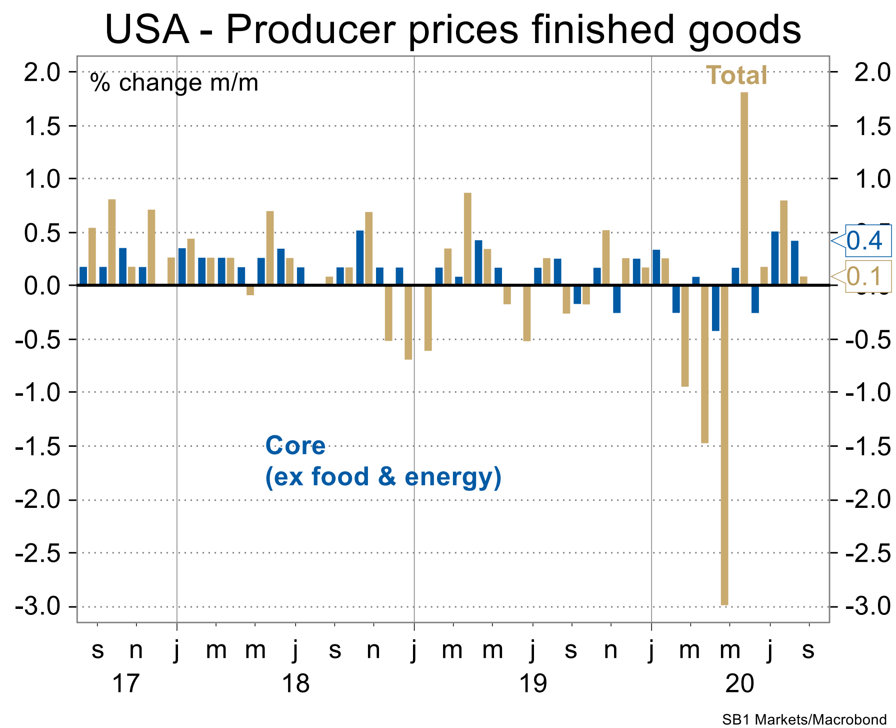


SB1 Markets/Macrobond

Core producer price inflation slowly moving upwards

Total finished goods prices down 1.6% y/y – from -5% in April

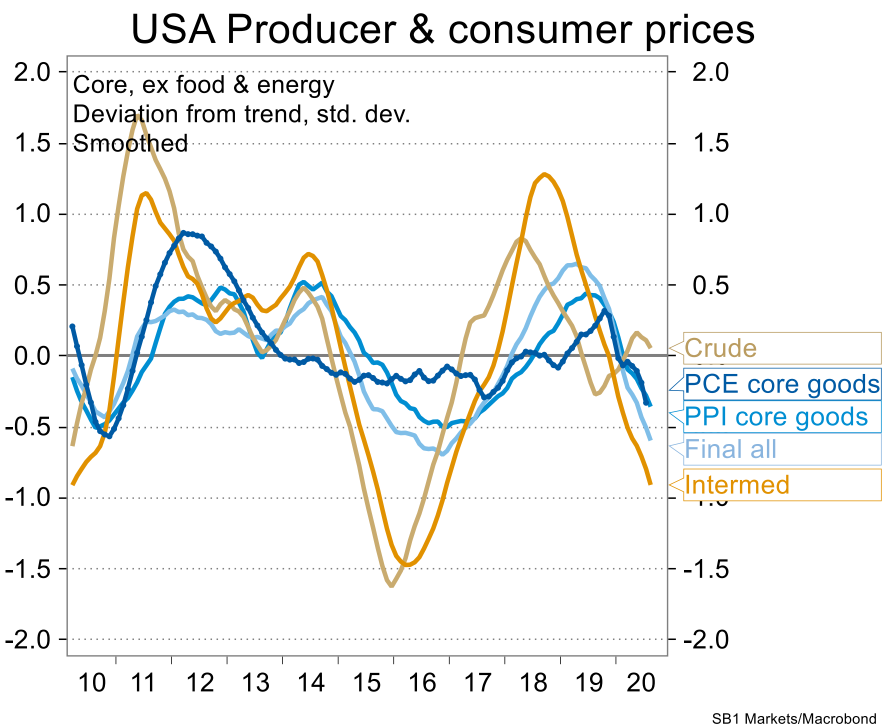


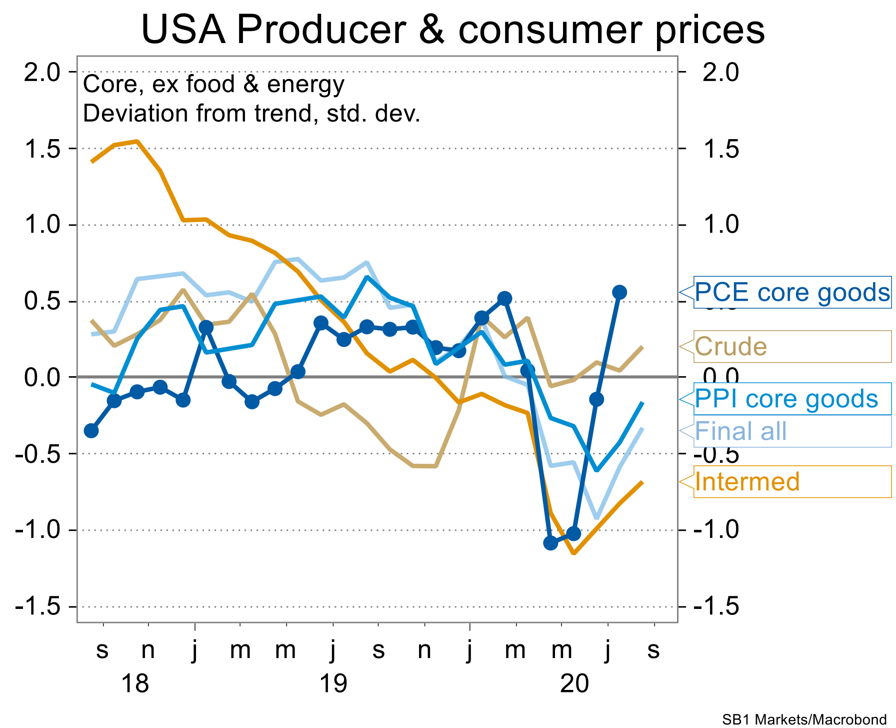


- Core finished goods x food & energy PPI rose by 0.4% m/m in Aug and the annual rate edged up to 0.6%, reflecting a slow comeback of demand . Core producer price inflation has slowed rapidly since early 2019
- Headline PPI rose 0.1% m/m and the annual rate rose to -1.6%. Total PPI inflation fell rapidly in March and April, along with the economic crisis and falling energy prices when the pandemic hit
- Core producer price inflation suggests that consumer inflation will remain muted for some time

Producer prices at early stages are turning up, but far from seriously

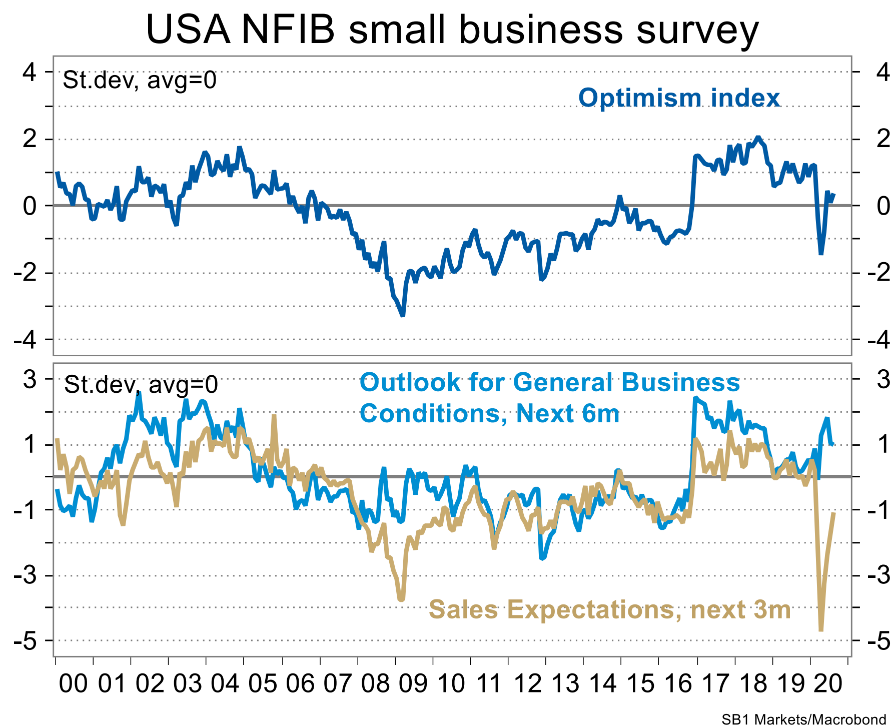
At least, the core PPI does not signal any deflationary pressure

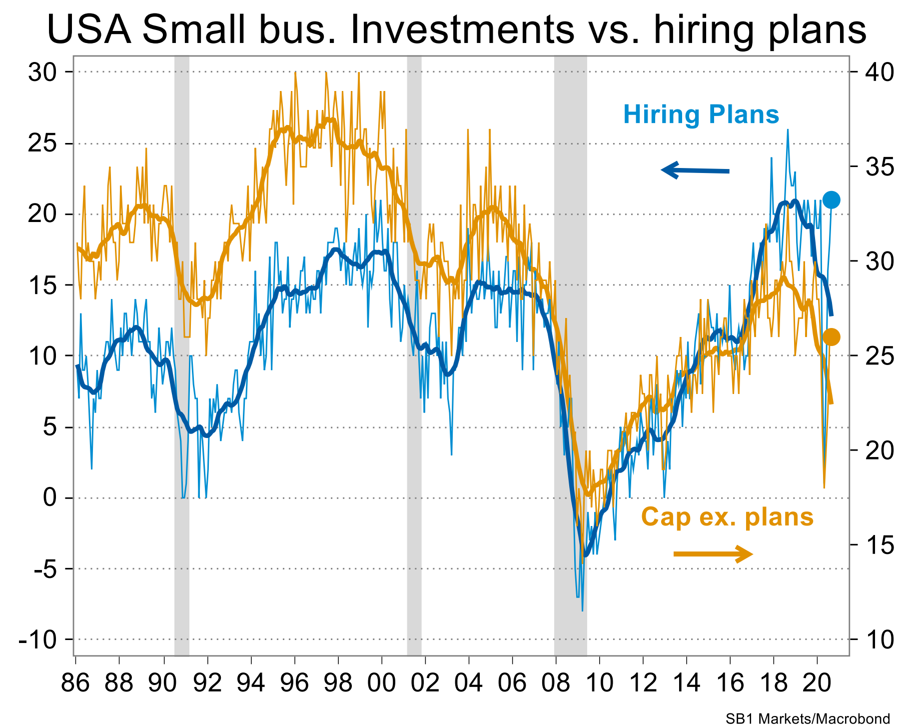




Small businesses' optimism at OK level, sales expectations still below par

Businesses are reporting higher hiring plans – and more surprisingly – difficulties attracting labour



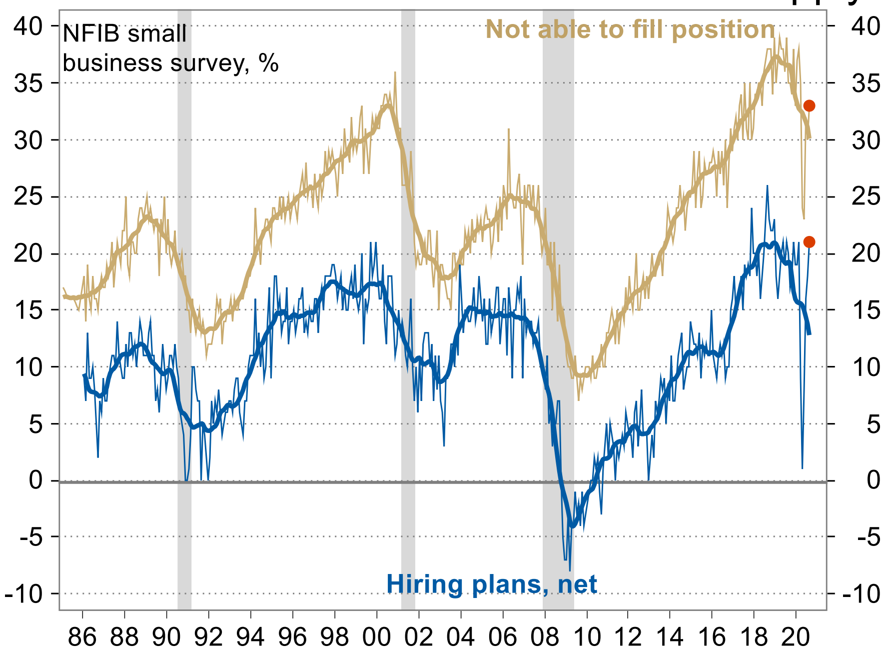


- The NFIB optimism index edged up in August, slightly more than expected. The level is just above average. The expectation index, the outlook for the next 6 months, inched down but have been surprisingly strong through the Covid crisis, as the total optimism index
  - » Sectors: Transportation and services are the most downbeat, construction and manufacturing in the lead
- Businesses slashed their sales expectations during the corona downturn. Expectations have recovered substantially but they are still not upbeat
- Investment plans have almost returned to a normal level, and companies are not signalling substantial cuts in investments (but no growth either)
- Hiring plans are back at the pre corona level – and their plans are rather aggressive. However, given that employment is still 8% below a pre corona level, it is not strange that hiring plans are pretty aggressive – and it do not signal a tight labour market. *However, check next page…*

Small businesses plan to hire again – and they are not able to fill vacant positions

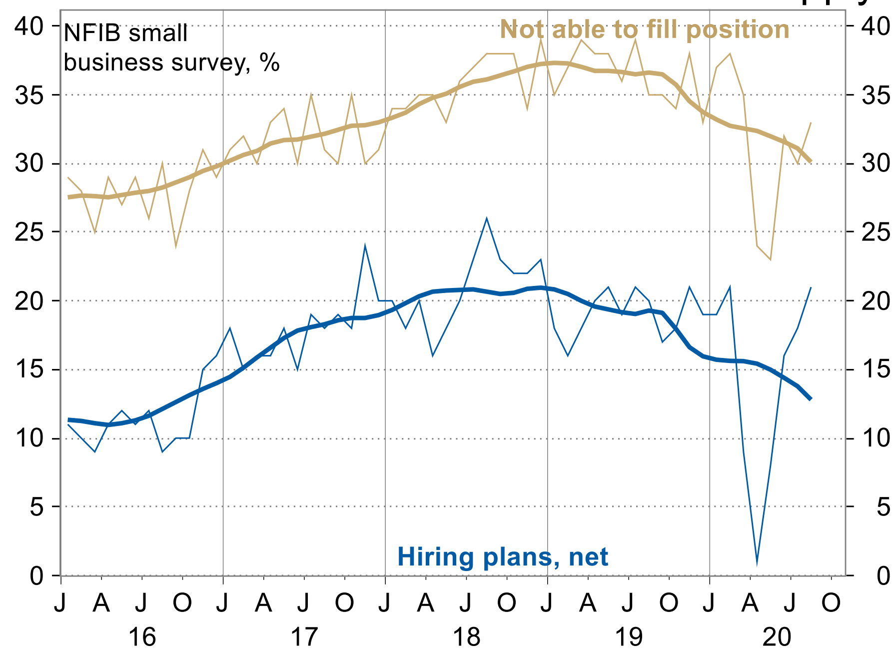
It's hard to calibrate the hiring plans, as so many companies have cut their workforce lately

USA Small businesses labour demand/supply



SB1 Markets/Macrobond

USA Small businesses labour demand/supply

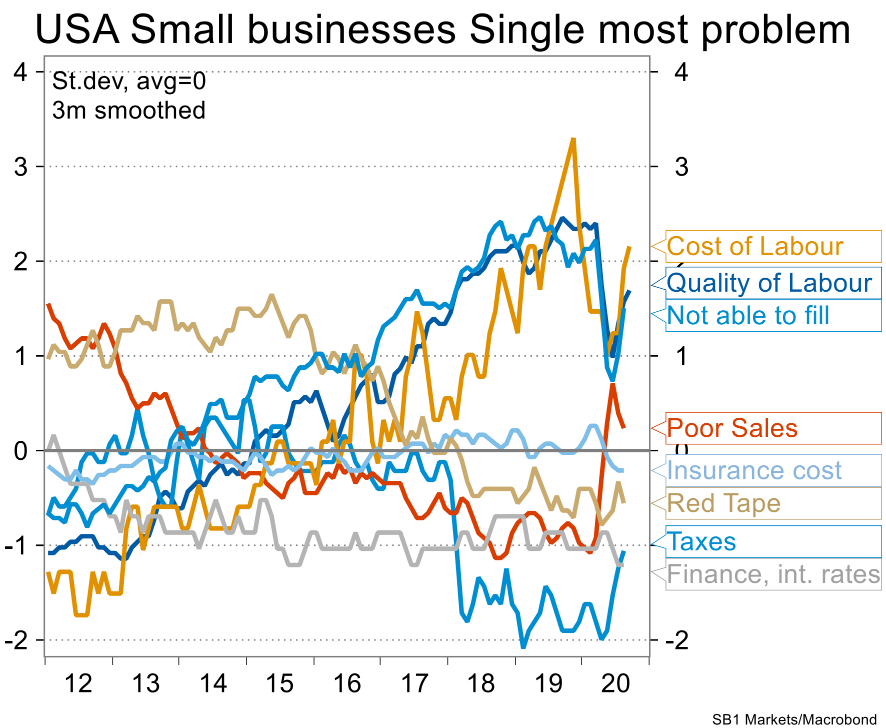


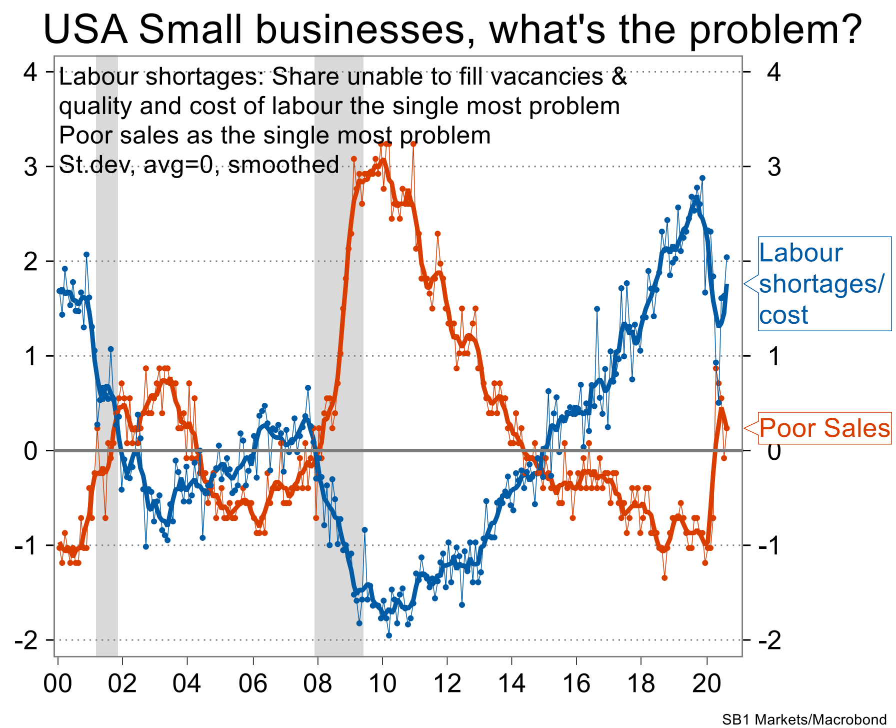
SB1 Markets/Macrobond

- However, it is remarkable that so many companies are reporting that it is unusually difficult to fill vacant positions when the unemployment rate is as high as now. Perhaps the unemployment benefits are too generous now? More on this conundrum here

Costs, supply and quality of labour still reported as the major problems

Slightly more than usual are citing poor sales as the major problem, but cost of labour #1!

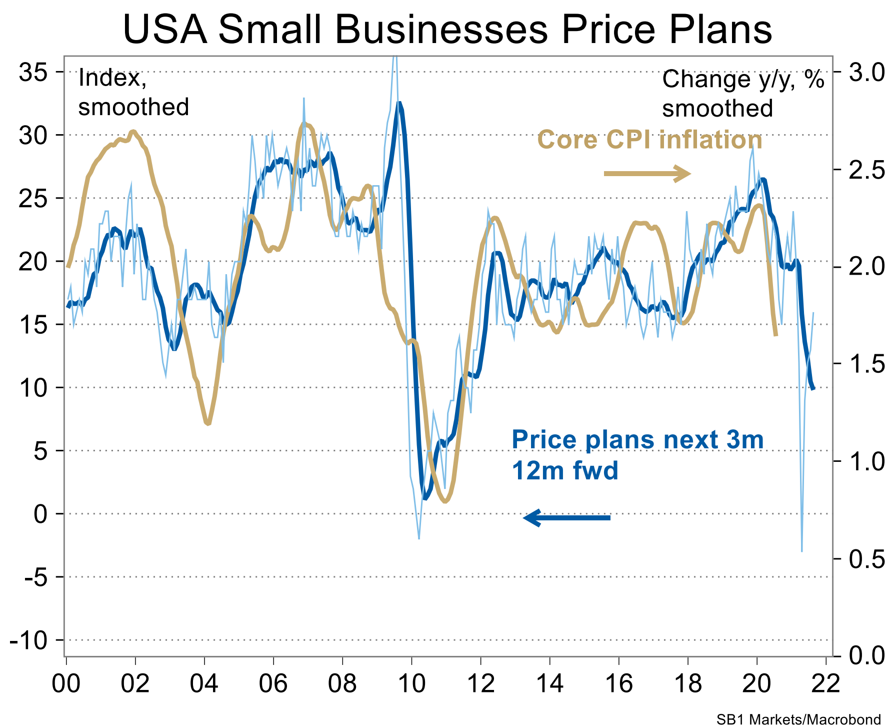


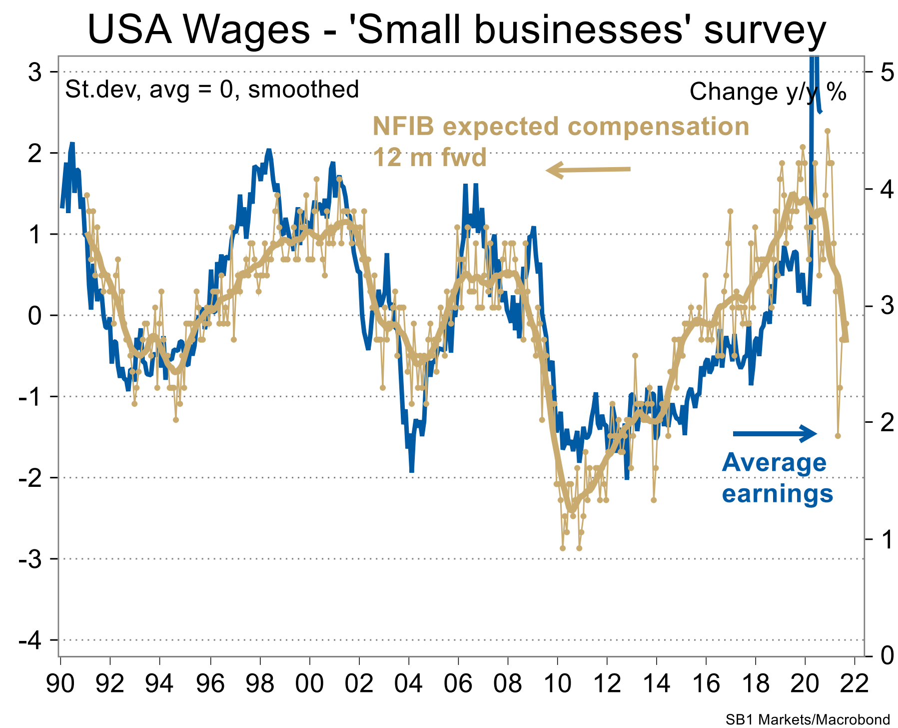


- Unusually few are complaining about finance/interest rates and about taxes
- More businesses have been stating weak sales as the major problem but the level has been surprisingly low
- The share of businesses that have been noting problems with tight labour markets have remained remarkably high during the economic downturn. Both the ability to fill vacancies, cost of labour and quality of labour are still reported as huge problems

Companies assume modest price & wage inflation

Not surprising, given the low capacity utilisation in several sectors in the economy

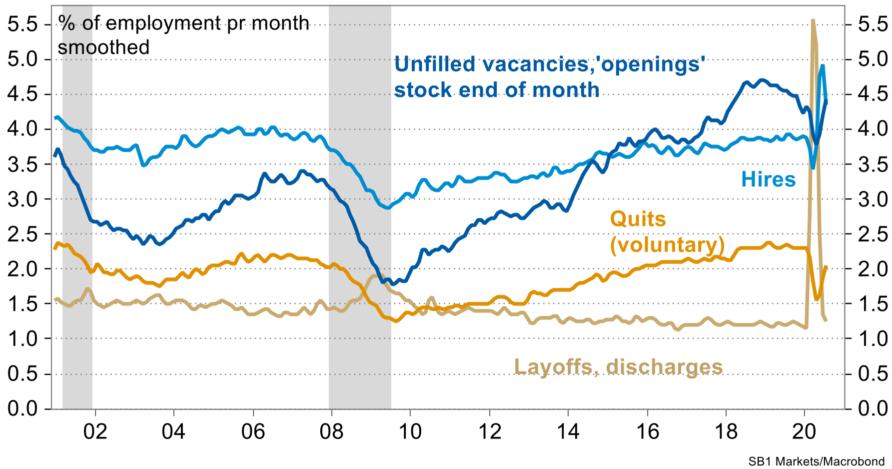




Layoffs down to a normal level. Hiring fell in July, still very high

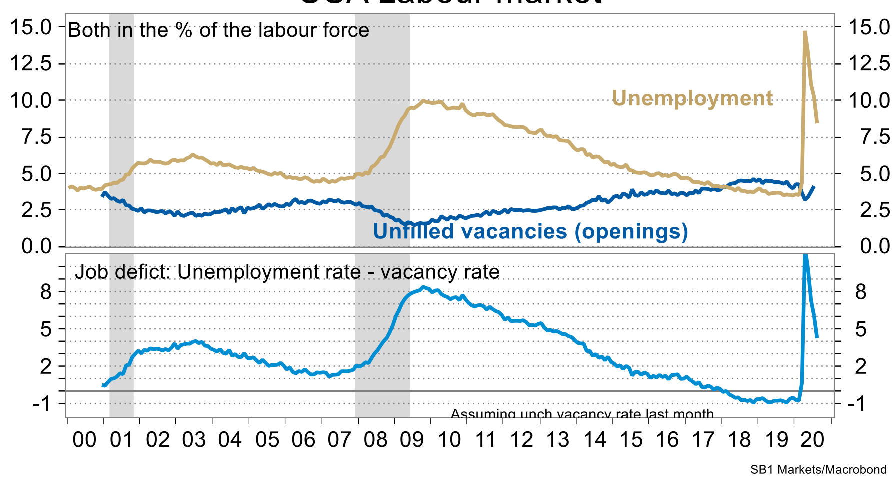
The number of unfilled vacancies is now just slightly higher than before corona, rather strange?

USA Labour market

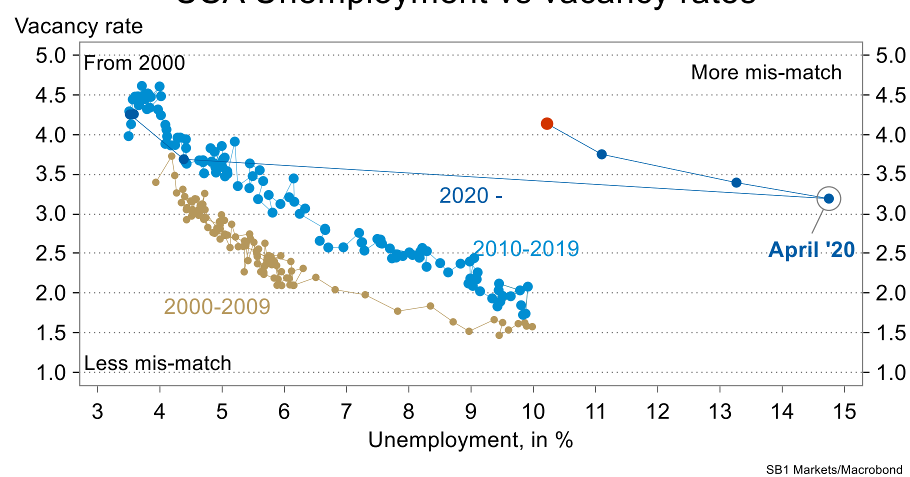


- Why are companies still not able fill their vacancies, even if the unemployment rate is far above a normal level?
  - » More mis-match between the unfilled positions and the unemployed (geography, qualifications)?
  - » More unemployed prefer to remain unemployed due to the >100% compensation rate for a majority of the unemployed?
    - These JOLTS data covers July, where unemployed received the USD 600 extra federal support – which was cut or sharply reduced from August. Will more unfilled position be filled up?
- This JOLTS unfilled vacancies stats confirm the small business survey, companies are NOT able to fill their vacant positions!

USA Labour market

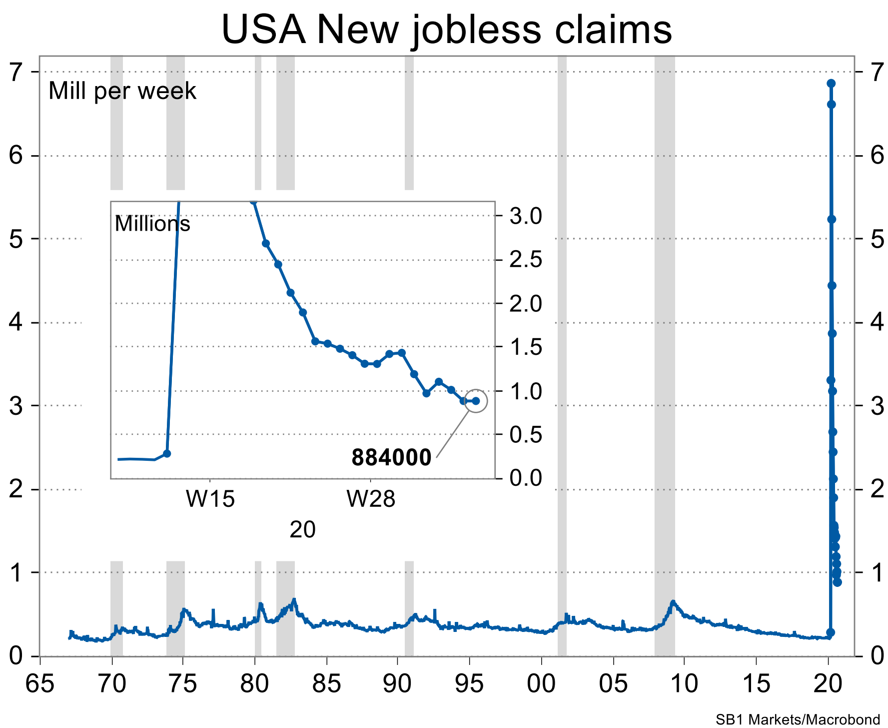


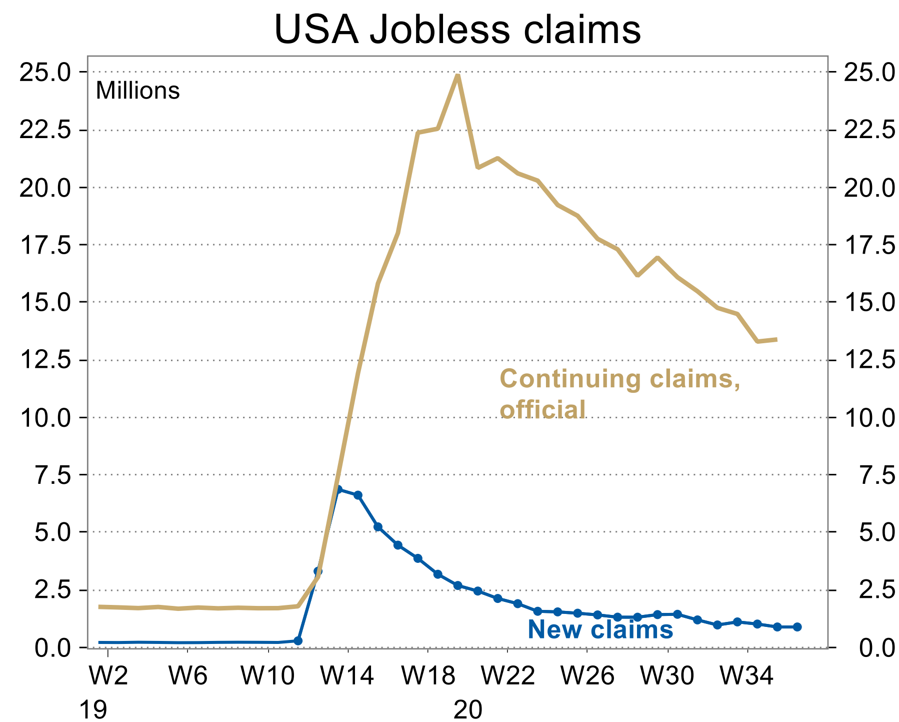
USA Unemployment vs vacancy rates



New jobless claims steady at a high level

The inflow of new claims is sliding down but 0.88 mill per week is still very high

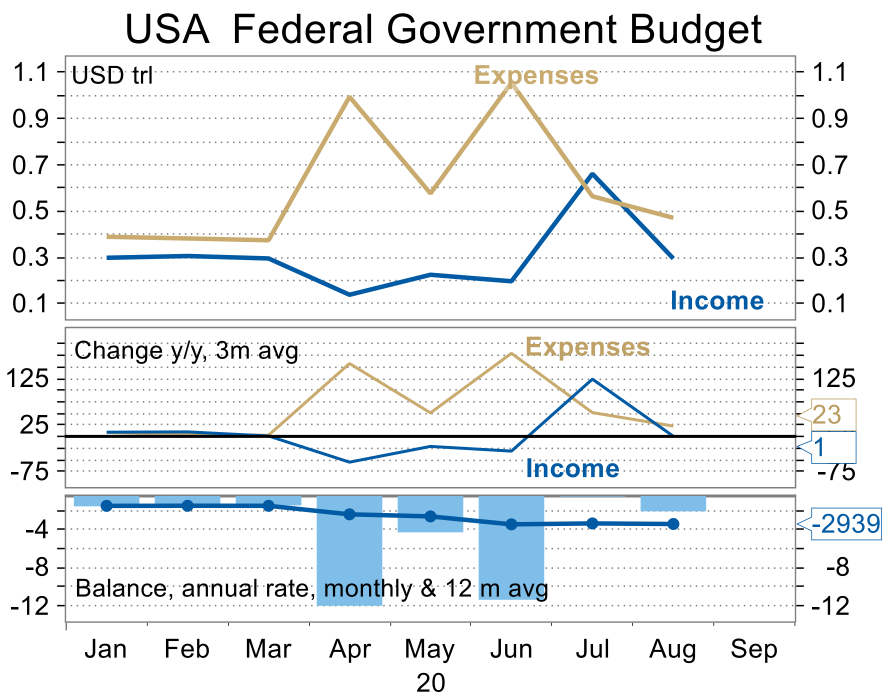


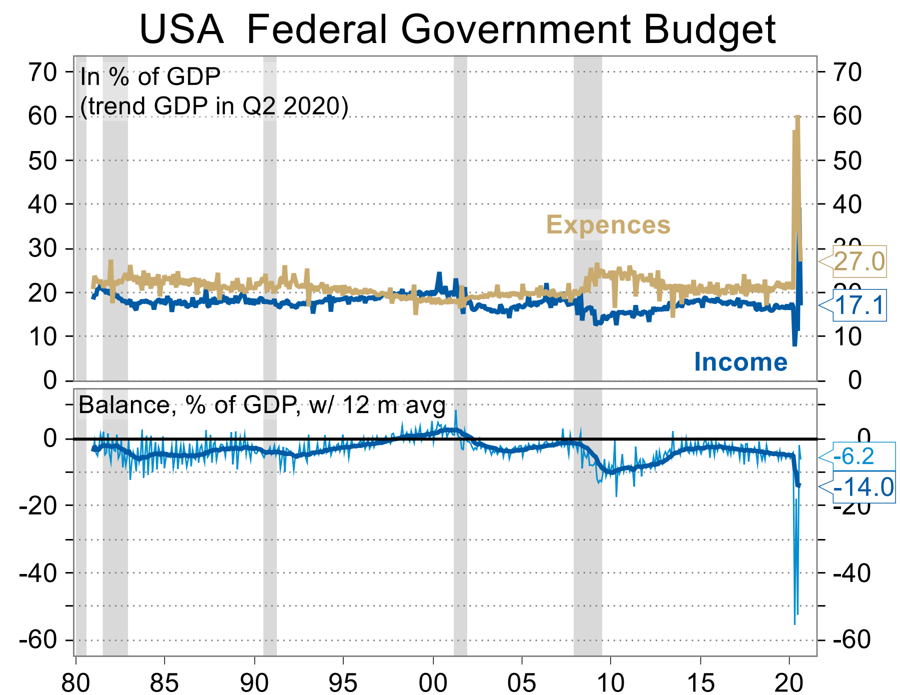


- The inflow is abating, however, it equals 0.6 % of the labour force entering the labour market offices as newly unemployed each week! The number much higher than during any earlier USA recession
- Luckily, more are leaving the dole (for a job or are they leaving the labour market?): Continued claims has fallen to 13 mill. from 25 mill. – still 8% of the labour force is on the dole

The budget almost balanced in July/Aug, but -14% of GDP past 12 m

Huge changes in monthly flows, so far the 12 m total deficit is USD 3.000 bn, 14% of GDP

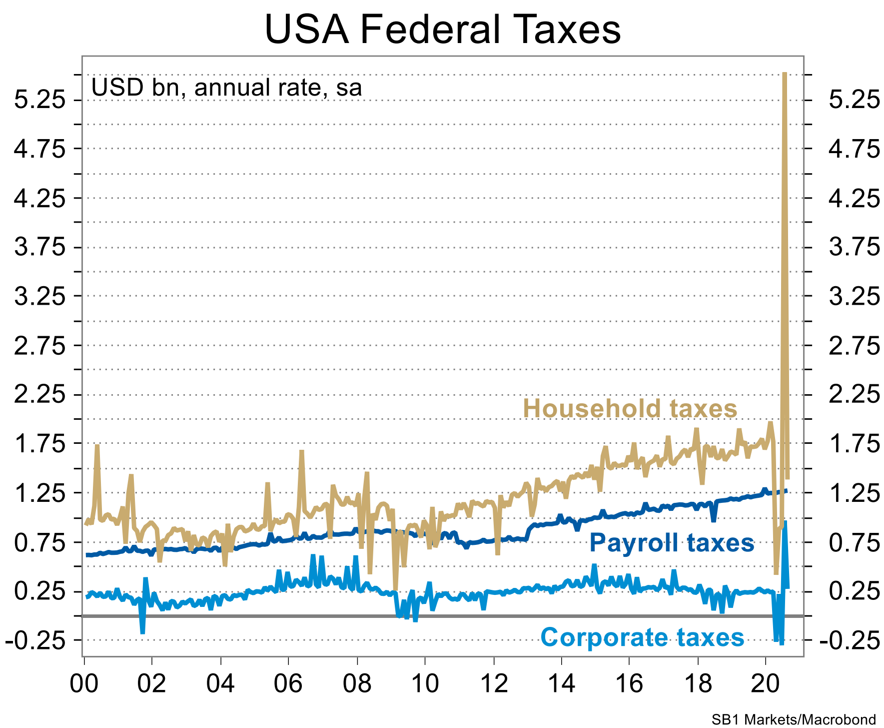


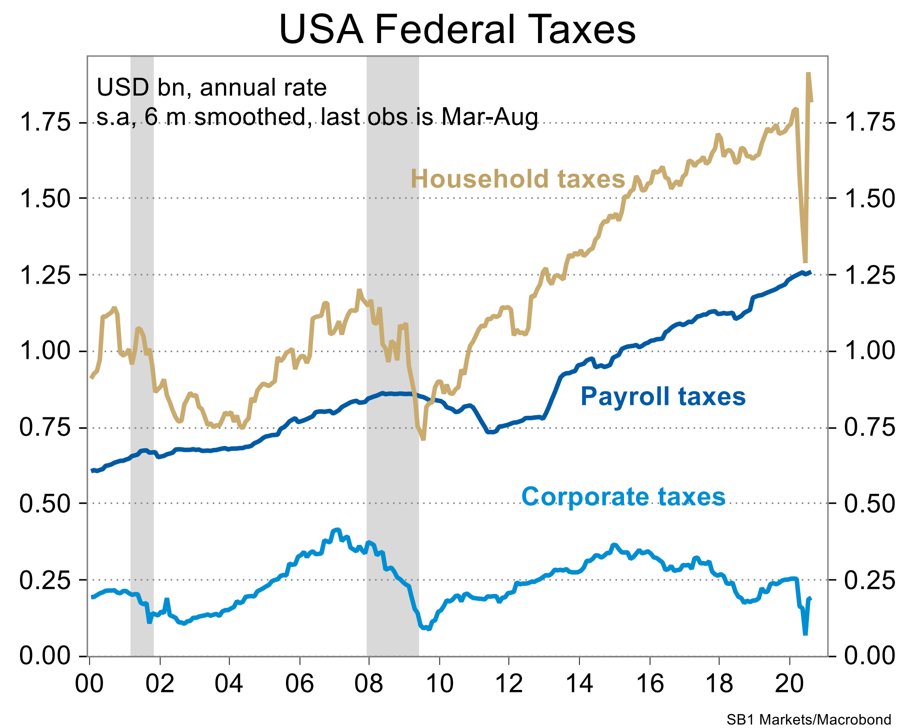


- It is not possible to know the underlying budget position (the underlying run rate now), as both expenditures and revenues are influenced by corona measures. We assume activity below par will dampen federal revenues, while outlays will not be lower than normal (and most likely higher, even if a compromise on a new stimulus package is not yet reached in Congress)

Huge ups and downs in tax payments, both from households & corporates

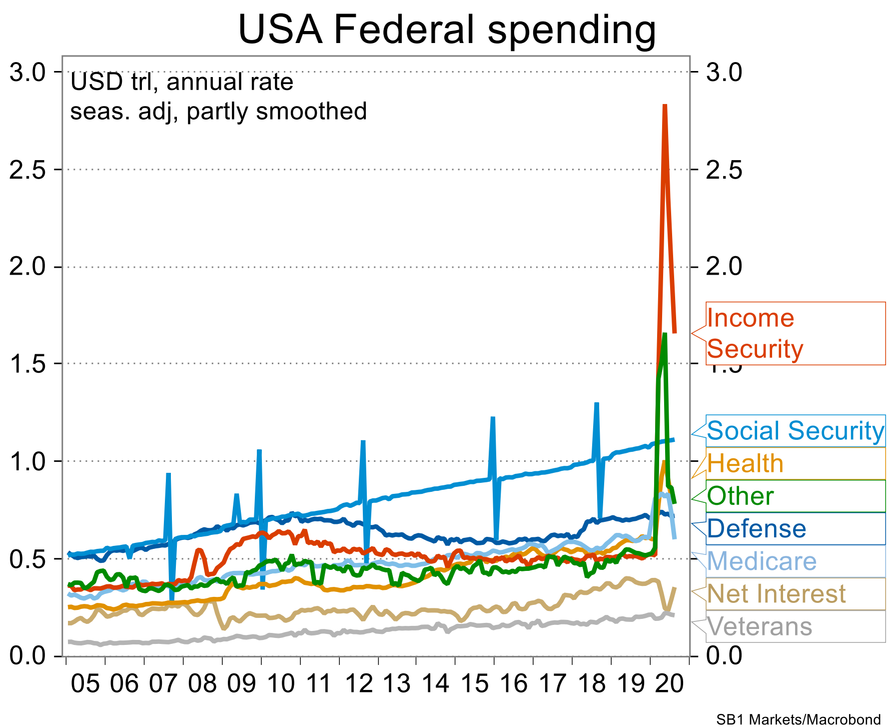
Over the corona period, corporate taxed are cut (by some 30%), household taxes are up

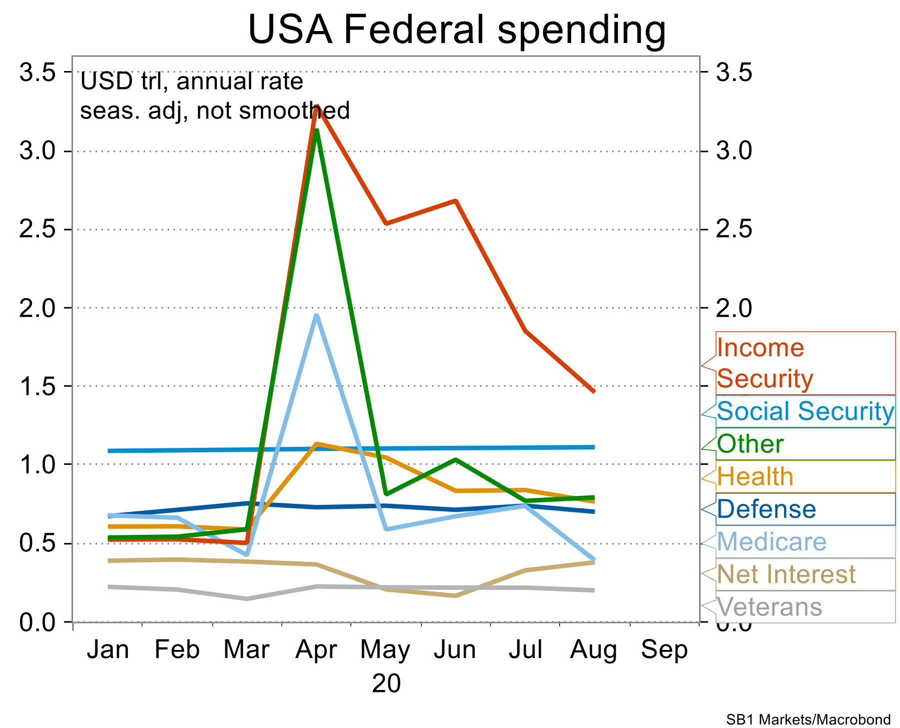




Unemployment benefits and other transfers are scaled back

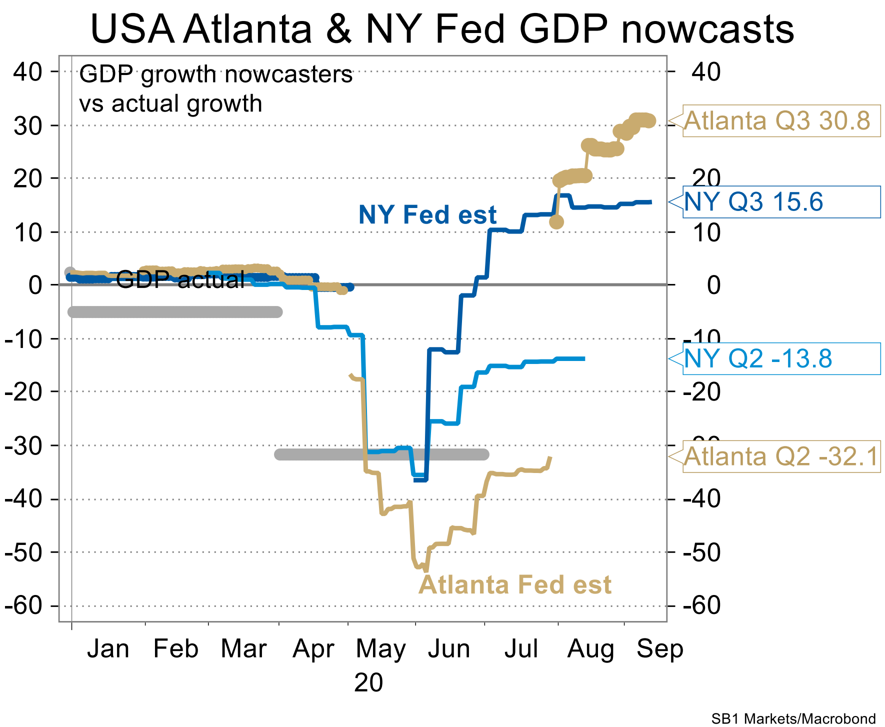
… and the Congress has not agreed on a 'skinny' budget deal

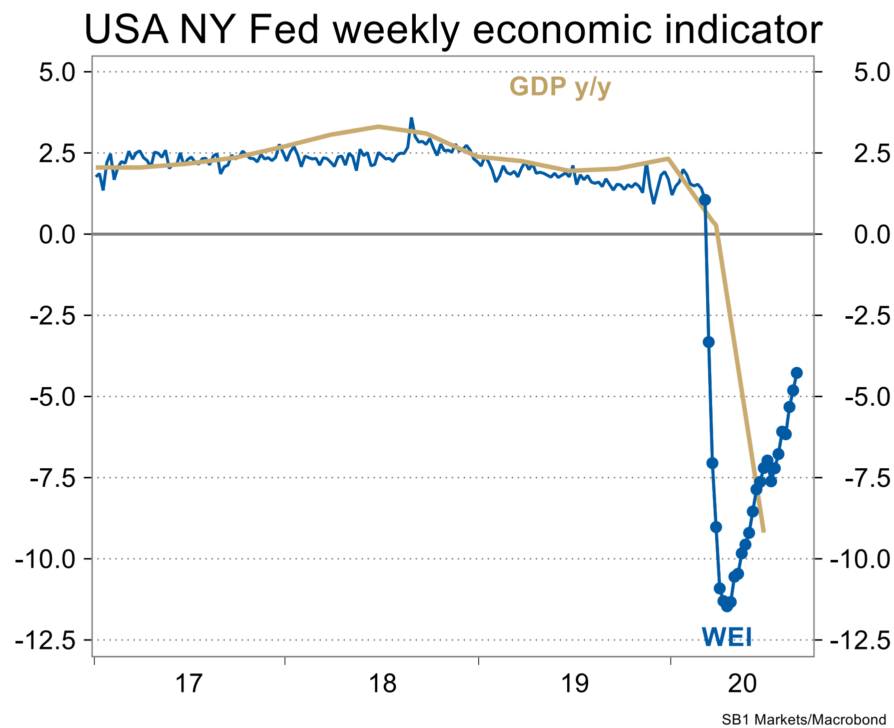




Nowcasters are looking upwards in Q3, of course. But still far less than the Q2 loss

15 – 20% growth (4 – 7% not annualized) signaled, vs. the 31% (9.1 n.a) Q1 setback



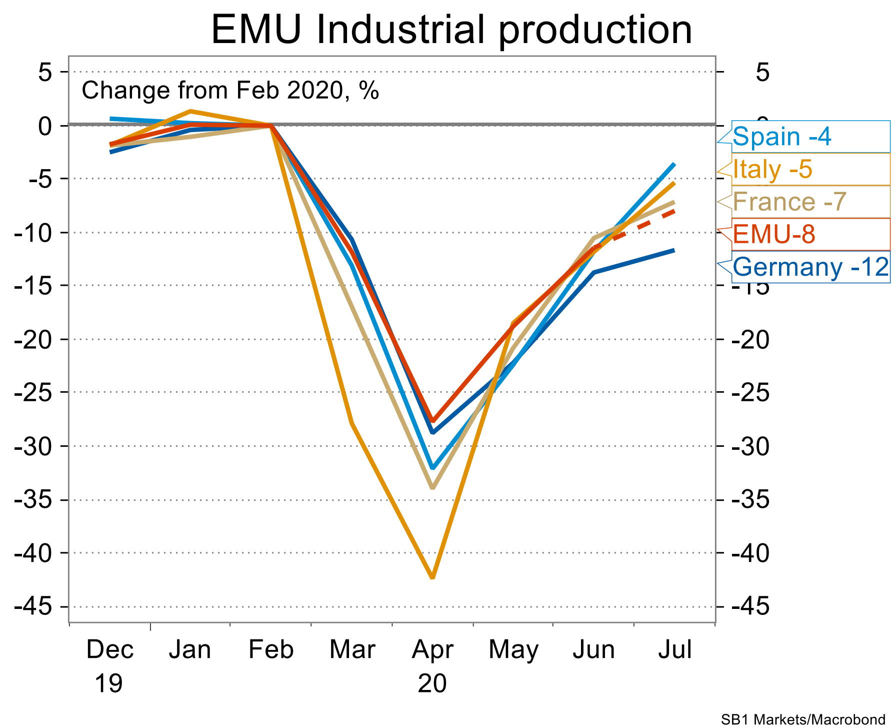


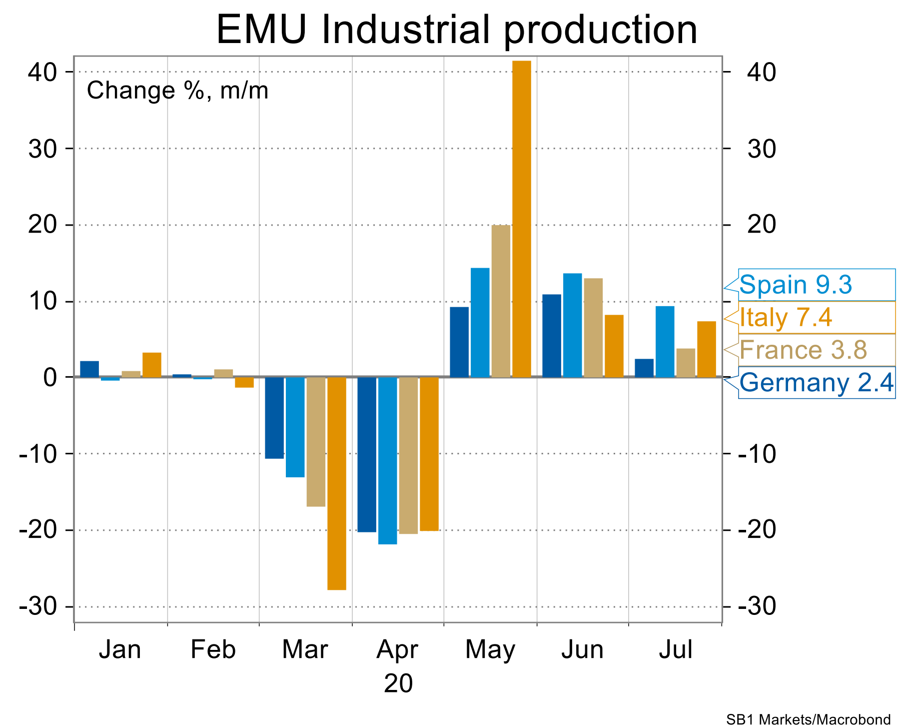
- The nowcasters' Q3 forecasts are still very uncertain - and they don't even get it right after the quarter is done. So for what they are worth, the Atlanta and NY Fed nowcasters reports 15 – 30% growth in Q3 (annualised rate)
- NY Fed's weekly model signal some 5.5% decline y/y in Q3, equalling a 20% (4.5% not annualised) growth pace q/q in Q3. We still assume growth will turn out to be better than that

SpareBank 1 MARKETS

Manufacturing production rose less than expected in Germany, France, in July

We estimate a 3.9% lift in total EMU production in July, still an 8% gap vs the pre corona level



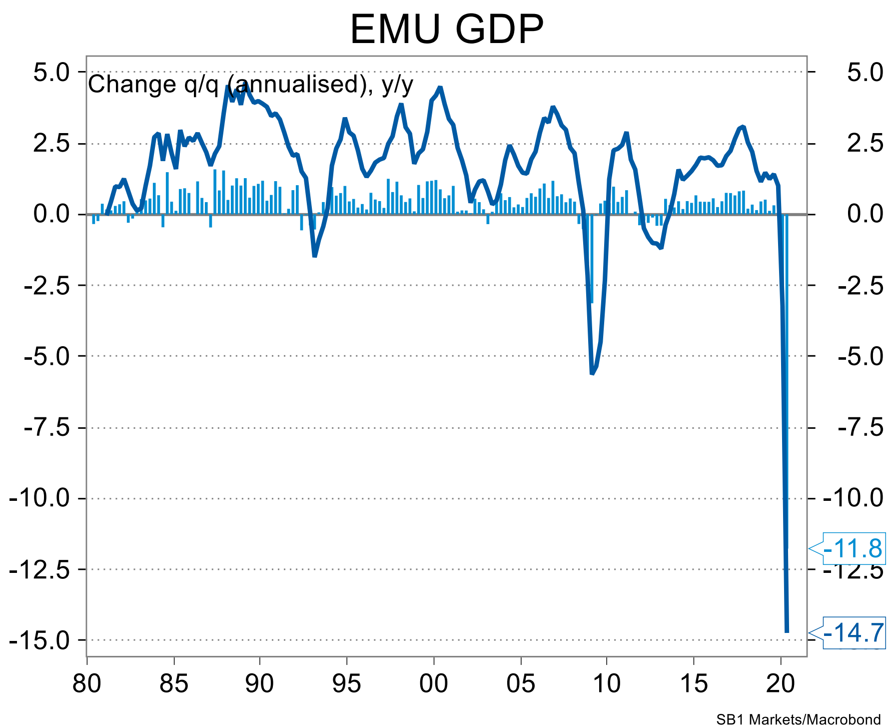


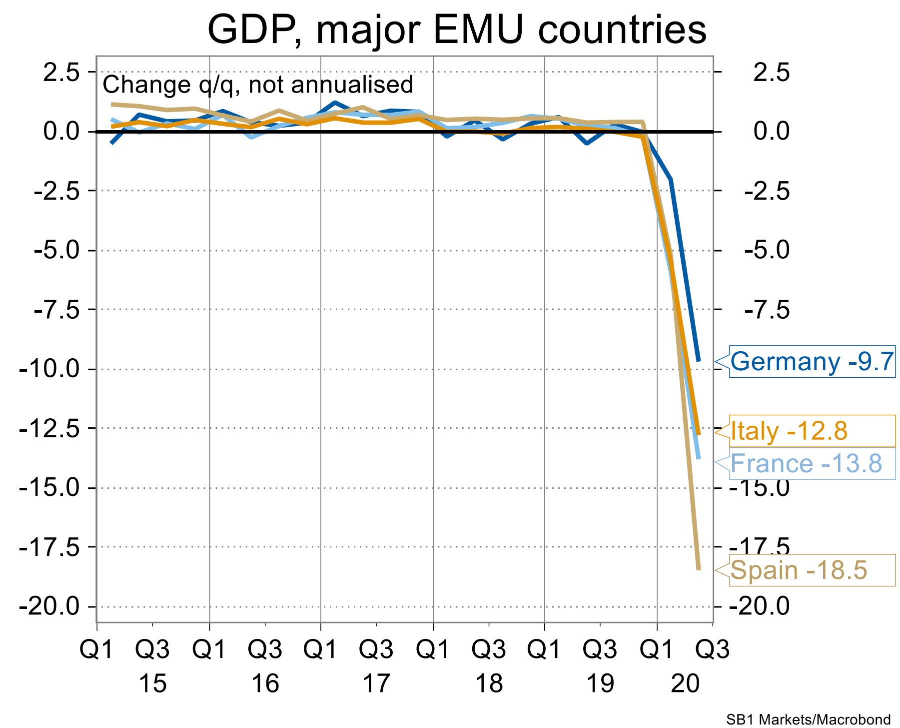
- Germany reported a 2.4% m/m rise in July, below the expected 4.6%. Production is slowly recovering but remains miles below the old levels. France up 3.8%, expected 4.9%. Production in Spain rose 9%, more than expected – and it is less than 4% below the February level

SpareBank 1 MARKETS

GDP fell 11.8% in Q2, marginally less than first reported (still -39% annualised)

All major demand components dropped - private consumption the main drag



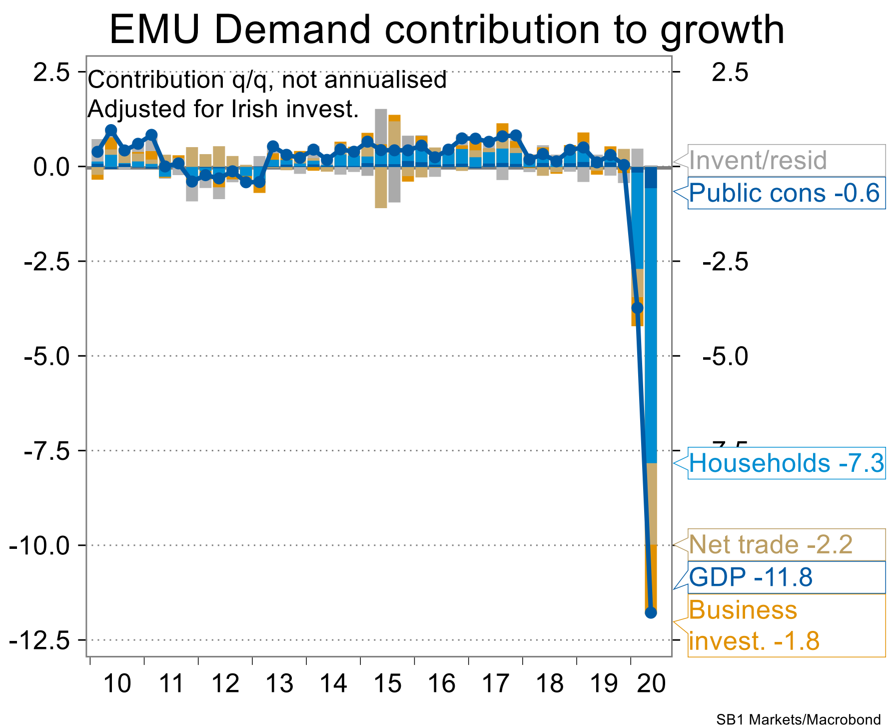


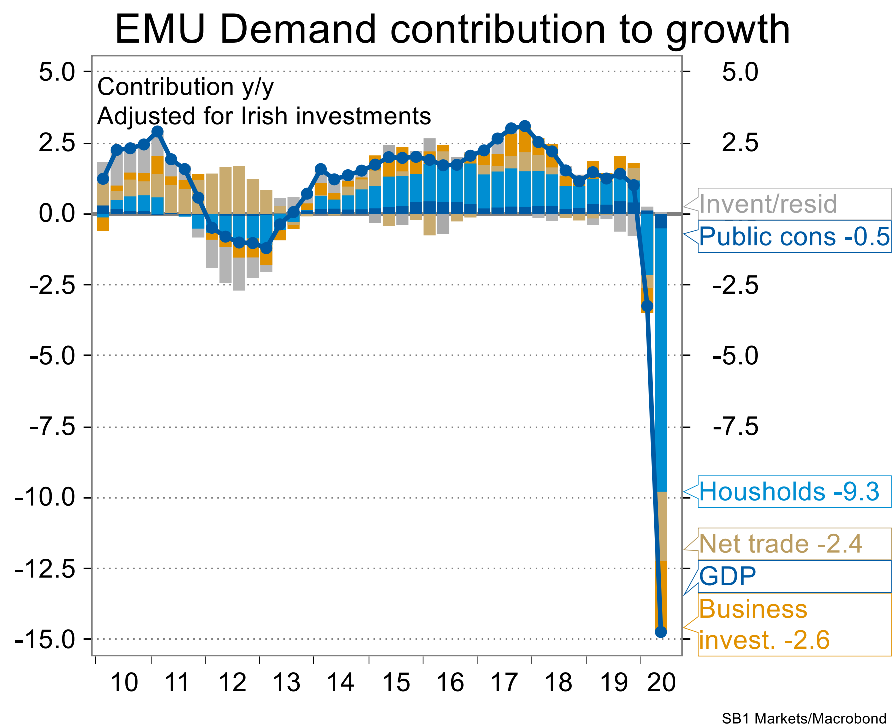
- GDP in the Eurozone was reported down 11.8% (not annualized) in Q2 in the 2nd report, 0.3 pp less than previously reported. Spain took the hardest hit, as expected, Germany the least
- Check the next slides for details, private consumption is the main culprit, as everywhere else
- Q3 will be the best quarter, ever ☺

SpareBank 1 MARKETS

All demand components down, private consumption collapsed, here too

Household demand (consumption & housing invest) down 7.3% q/q, similar to other countries



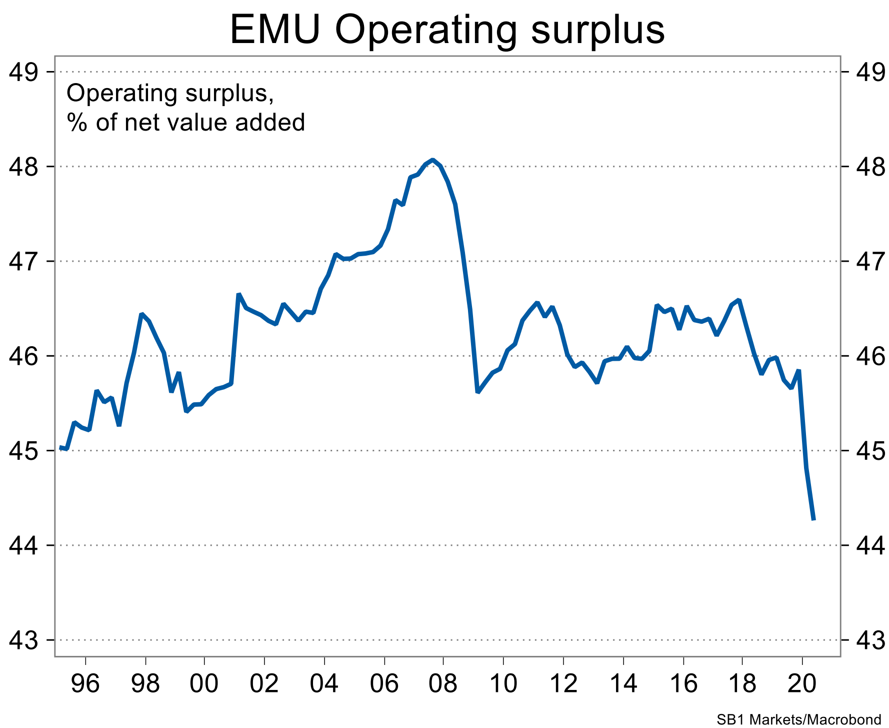


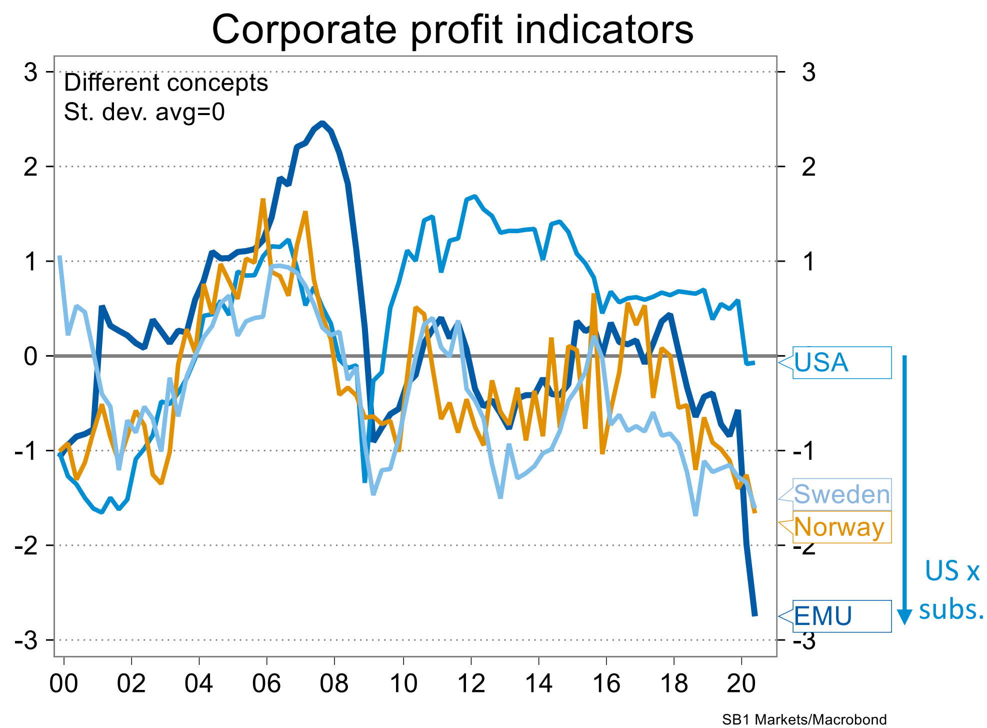
- Private consumption & housing investments fell at a pace we have never seen before (statistics back to 98'). And will increase like never before in Q3
- Business investments declined by 1.8% q/q
- Both exports and imports fell rapidly, net trade down 2.2%. Inventories made a marginally positive growth contribution

On the charts above, and on the next page we have adjusted total EMU investments and net trade data for anomalies in Irish national accounts. Huge, and highly volatile imports of immaterial goods, at times just as large as GDP itself (equalling 1% of EMU GDP!), and parallel lifts in investments in such goods creates trouble for European (!) National Accounts. These transactions are not 'real' activity, just due to accounting adjustments within some huge global software companies. Hence, we adjust EMU data by applying modified data, supplied by the Irish Statistical Office

Corporate profits sharply down in Q1 & Q2, less public support than in the US

There may be subsidies included in EMU profits as well, but nothing like in the US

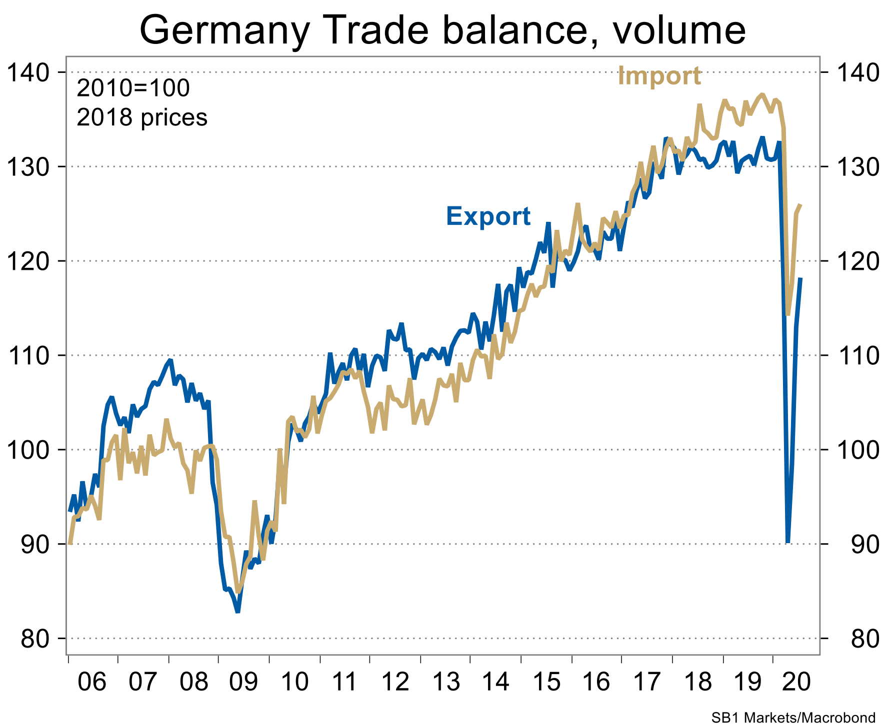


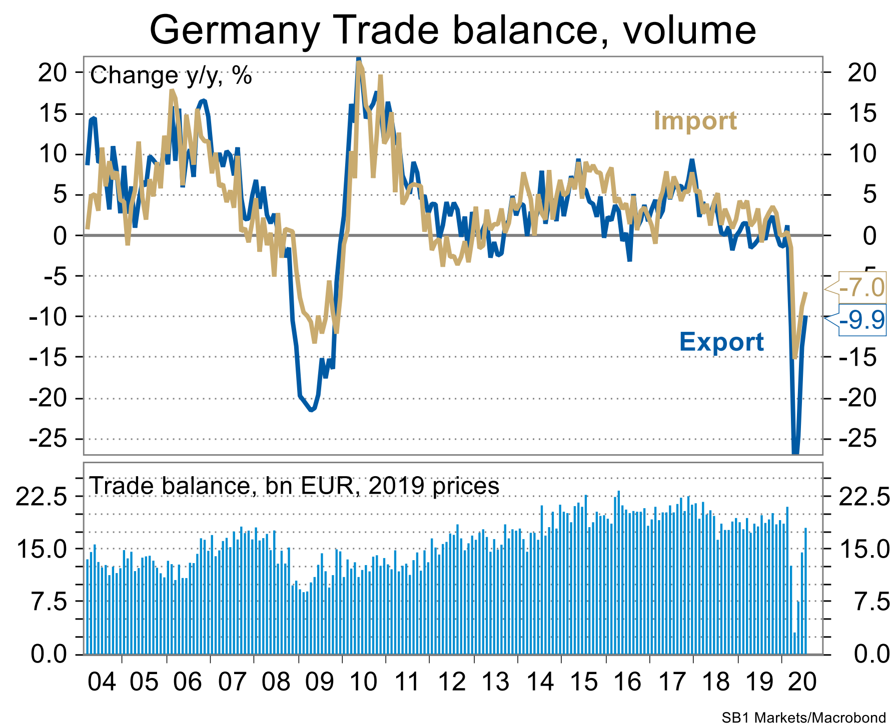


- In the US, public support lifted profits equalling 5% of GDP in Q2
- Profits are far less down in Norway (Mainland), and in Sweden

Foreign trade recovering but still miles below normal levels

Imports 8% below the February level, exports 11%

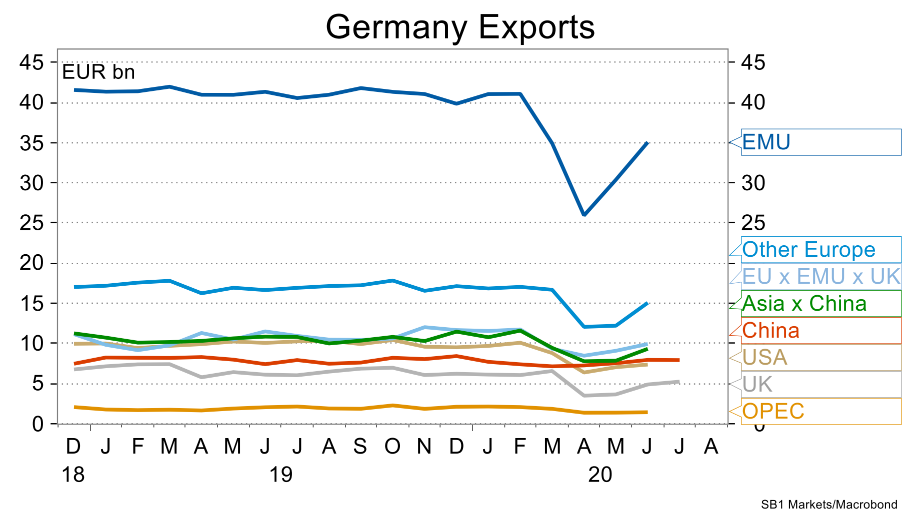


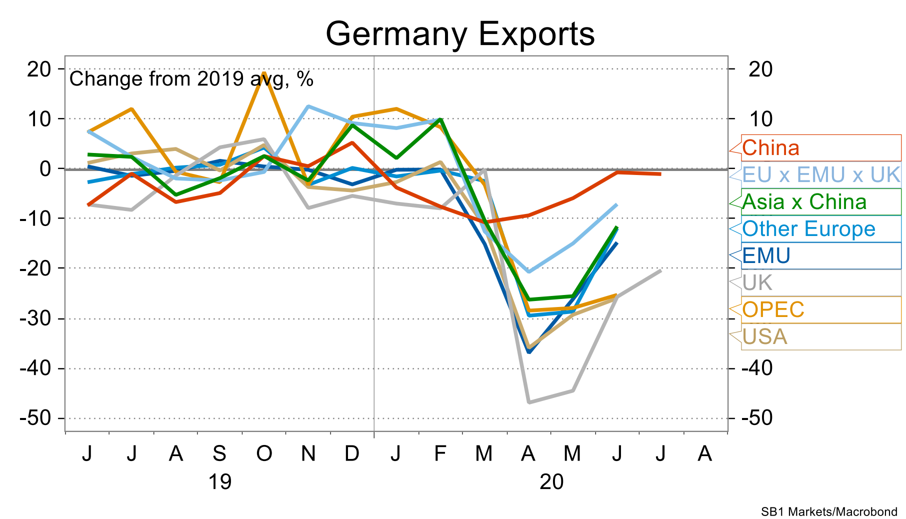


- Export volumes rose 4.7% m/m in July and have recovered approx 2/3rd of the March/April loss
- Import volumes increased by 0.8% m/m in July, have recovered just some 50%
- The German trade surplus shrank rapidly during the corona crisis in the spring, to the lowest levels in 20 years. In August, the surplus was almost back at a ‘normal’ level

German foreign trade was hit somewhat harder than the world in total

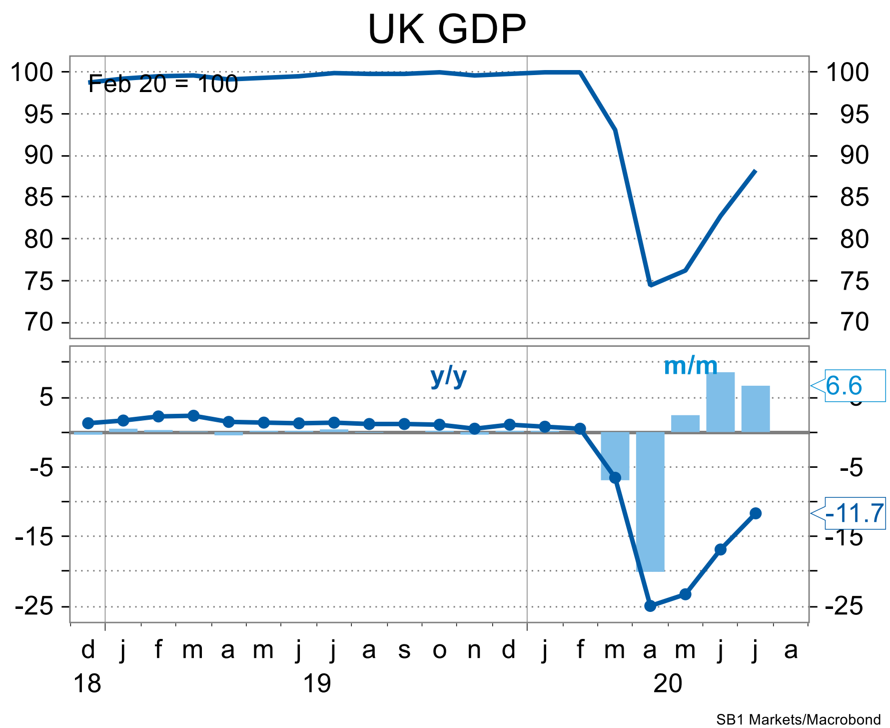
Exports fell in all directions – but are now recovering in all markets

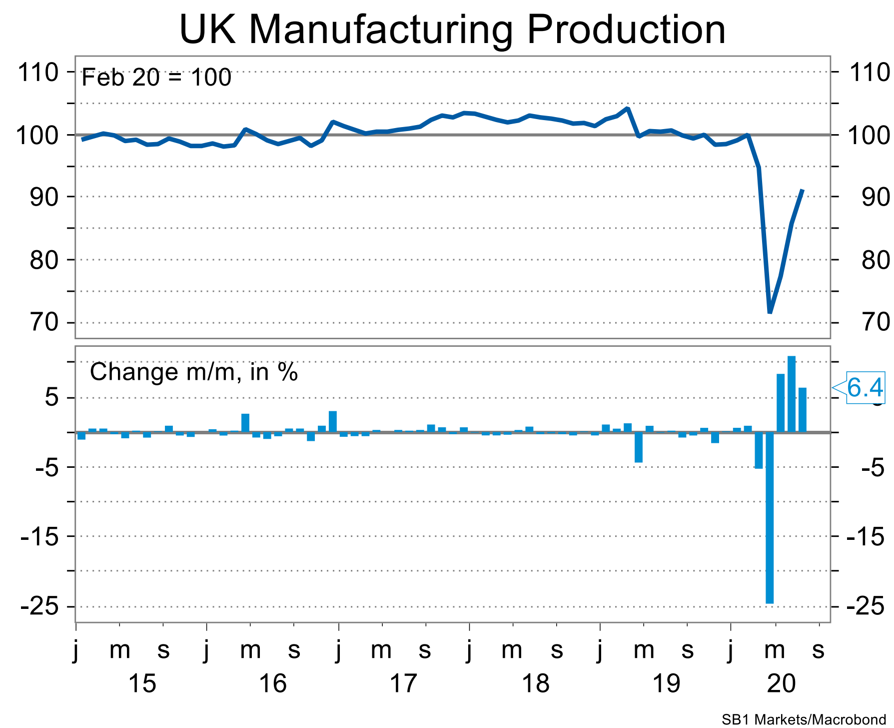




Activity is slowly resuming , GDP up 6.6% in July, manufacturing production 6.4%

GDP slowly recovering since May, still down 12% vs Feb. Manufacturing -9% vs February

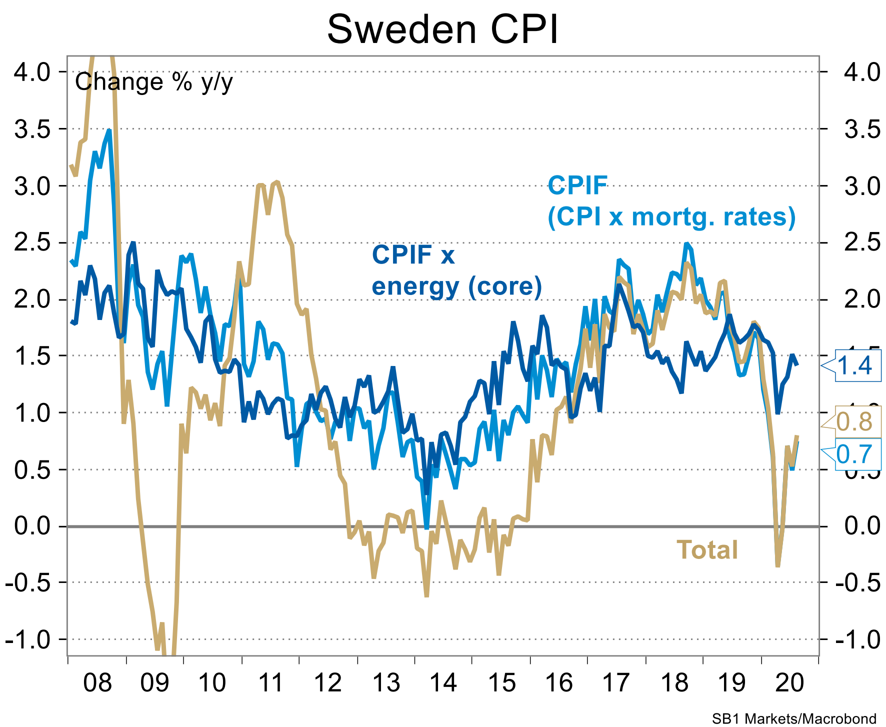


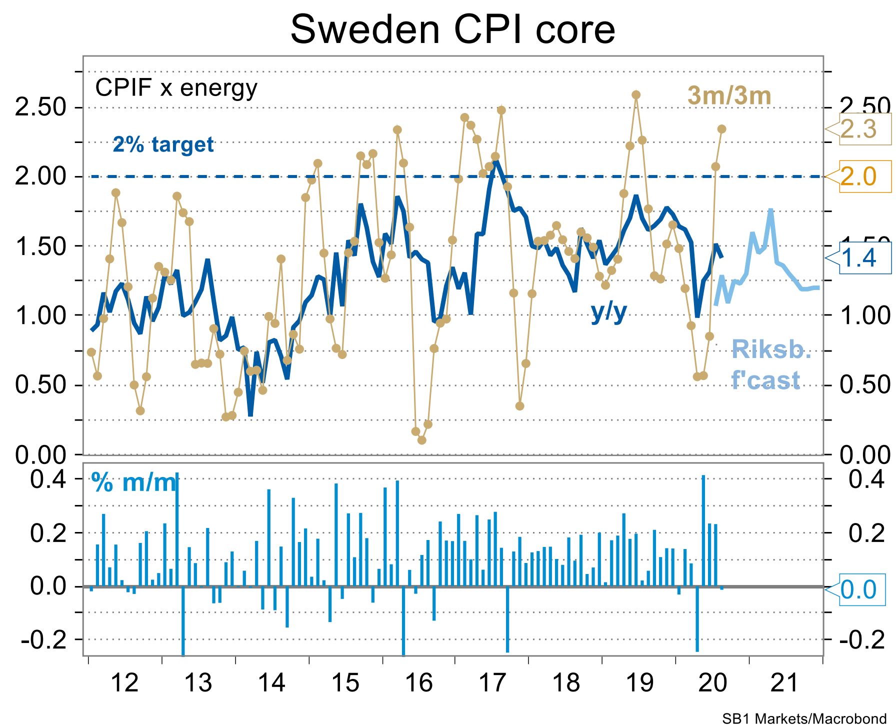


- UK should, like most other countries, report the highest growth ever in Q3, following the 20% (not annualized!) drop in Q2

Core inflation at 1.4%, headline inflation still low, now up to 0.8%

Core CPIF inflation inched down to 1.4% in August. Inflation below the 2% target for 3 years

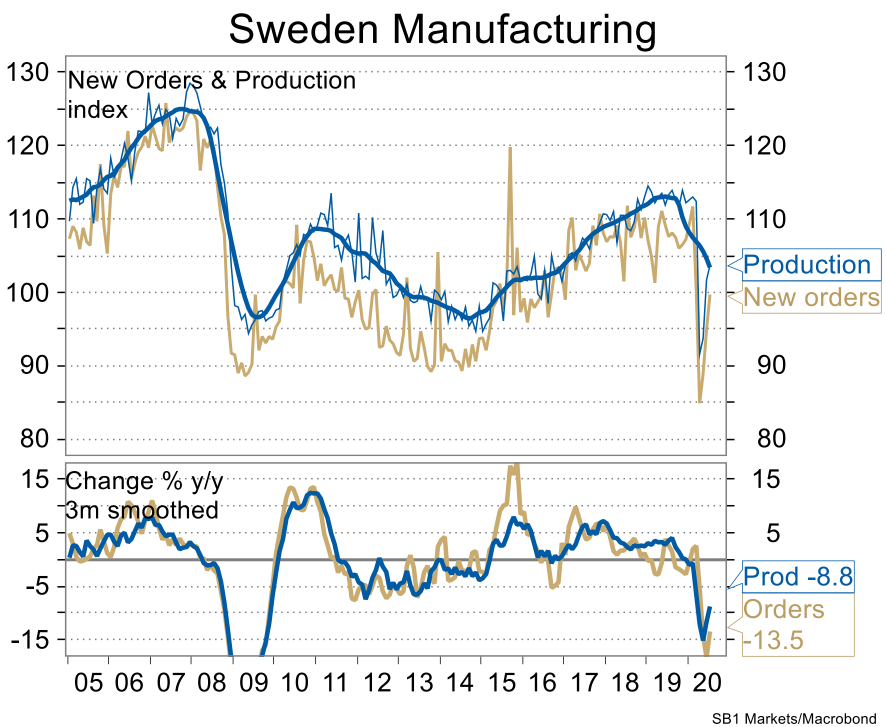


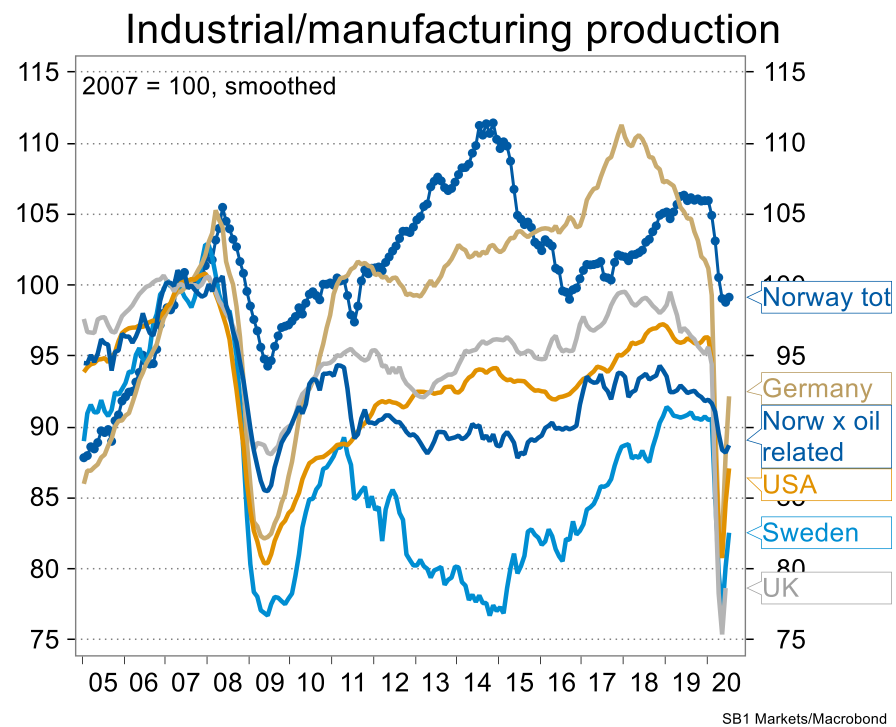


- The ‘real’ core (CPIF ex energy) was unchanged in August. Annual inflation came down marginally, to 1.4%. Core inflation has climbed the past 4 months, after a drop in March. Price growth is 0.1 pp below the Riksbank’s f’cast
  - » CPIF (ex mortgage rates) is up 0.7% y/y and growth has turned up since April. Total inflation at 0.8%
- Inflation has been below the Riksbank’s 2% price target since 2017. However, Riksbank is wary about going below 0 again and core inflation is anyway not that low. Interest rates are likely to be kept at 0 for a long time. Markets are pricing a low probability of an interest rate cut – and no hike in sight

Manufacturing production and orders slowly recovering

Production fell even more in Sweden than Norway, still down 8% from Feb (vs 5% in Norway)

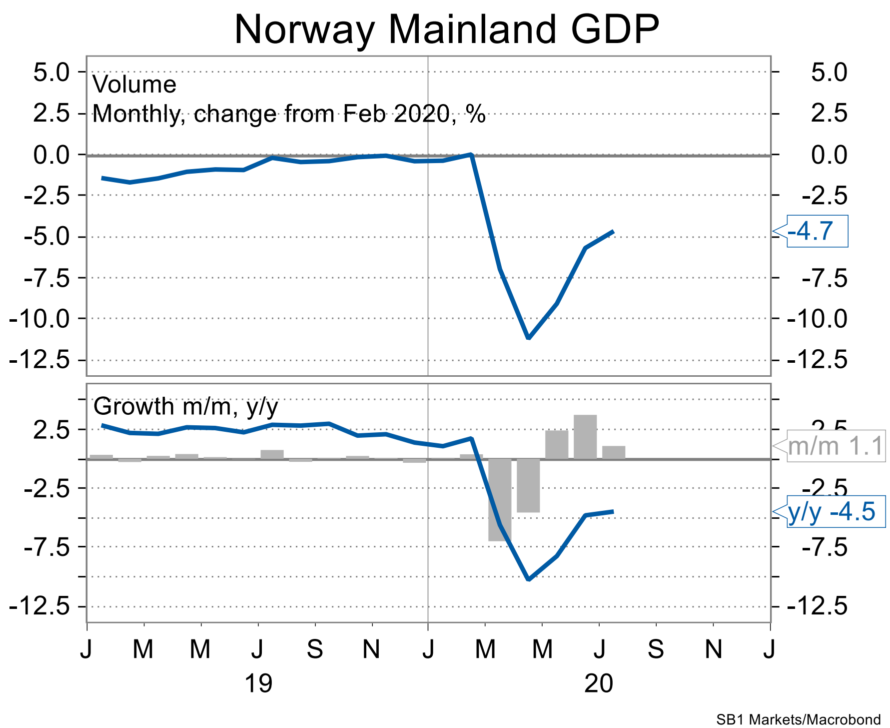




- Both production and orders have increased m/m since May

GDP up ‘just’ 1.1% m/m in July, less than expected, still 5% below par

Mainland GDP is recovering, still almost 5% below the February level – as services are still struggling

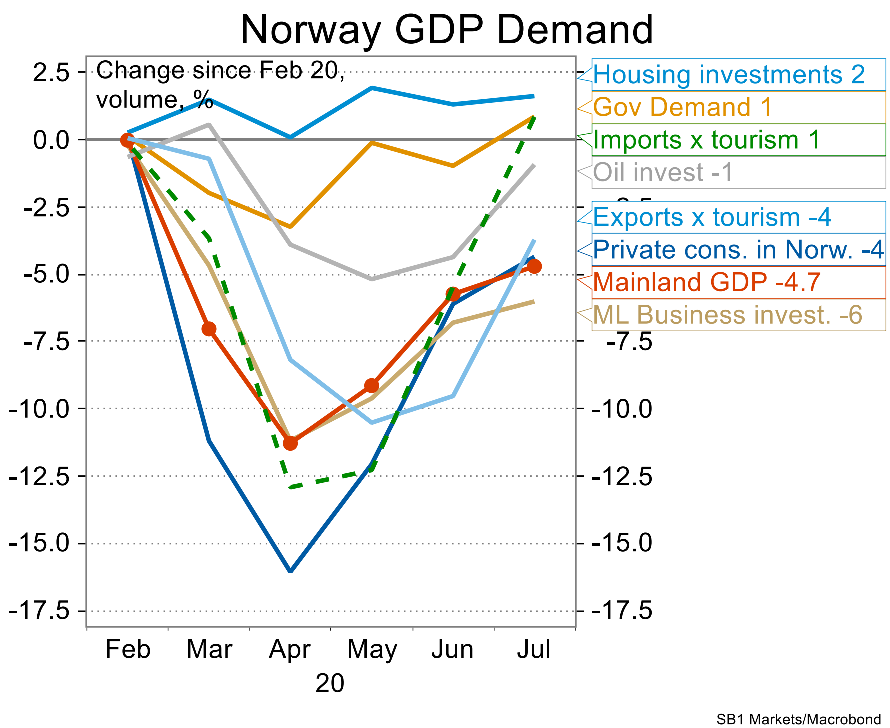


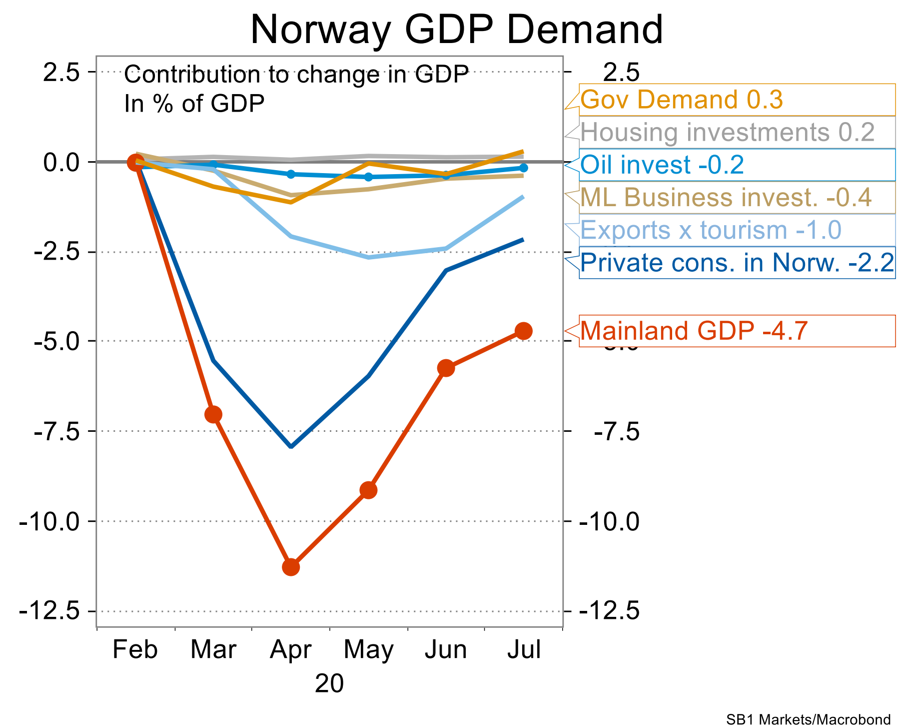
- Mainland GDP rose 1.1% m/m in July, we expected 2.5% (consensus at 2.0%)
- Mainland GDP is up 7.4% from the bottom in April, still 4.7% lower than the Feb level, and down 4.5% y/y.
  - » We expect GDP to continue to recover substantially the next months but remain below the pre corona trend
- If activity remains unchanged through Aug and Sept, Q3 GDP will be up 4.4%
  - » Some services will probably report lower activity in August, both hotels & air transport, following the July surge
- Travel, hotels, most cultural activities and partly restaurants will most likely not recover completely until the virus treat fades, either because it is becoming (even) less aggressive or a vaccine is widely available

- <u>On the demand side:</u>
  - » Most demand components rose in July from June
  - » Private consumption made the largest contribution to growth, for the 3rd month, but is still 8% below the February level (due to lower consumption abroad – while Norwegians’ consumption in Norway is close to unch from Feb
  - » Government demand continued to pick up
  - » Business investments rose marginally, as did oil investments. Oil investments have fallen sharply since last year
  - » Exports and imports both increased in July

Most demand components up in July, still below the pre corona level

Private consumption has been the main drag, now the main contributor in the recovery

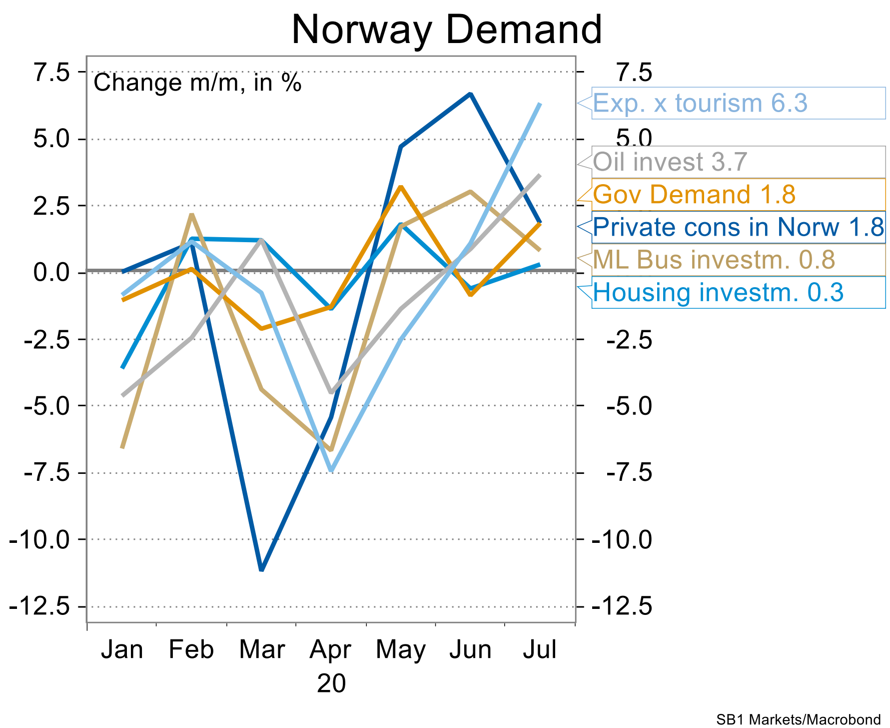


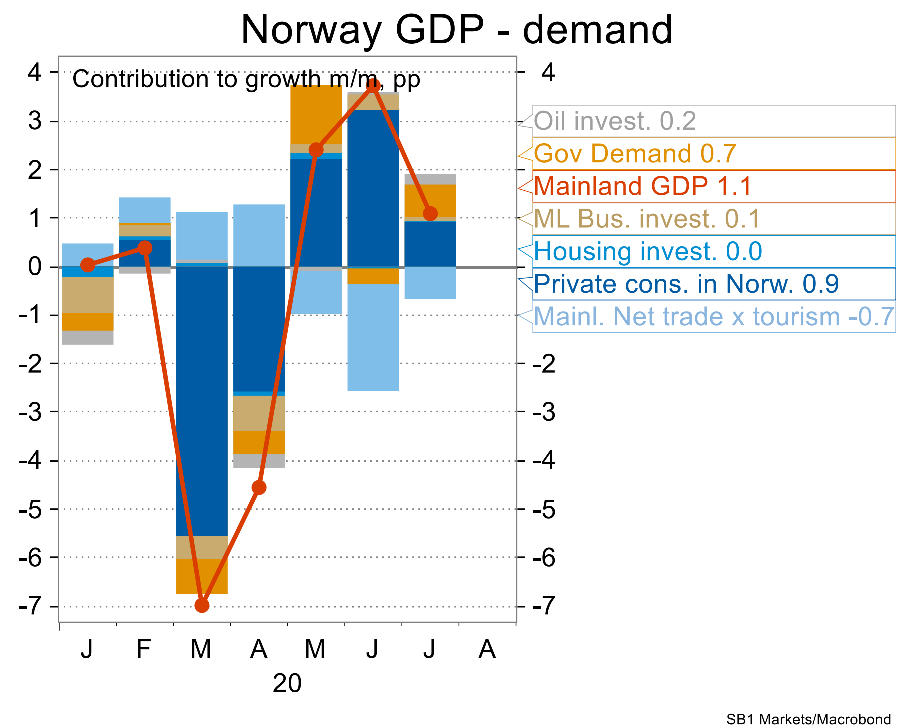


- Private consumption, exports have been the largest negative factors but oil investments as well as Mainland business investments have also contributed at the downside
- Since May, most demand components have recovered. Government demand is back at the pre corona level and oil investments just marginally below. Private consumption, trade and business investments are all still far weaker than in February

Private consumption is now the main growth engine (from a deep low)

In July, oil investments and private consumption increased at the fastest speed

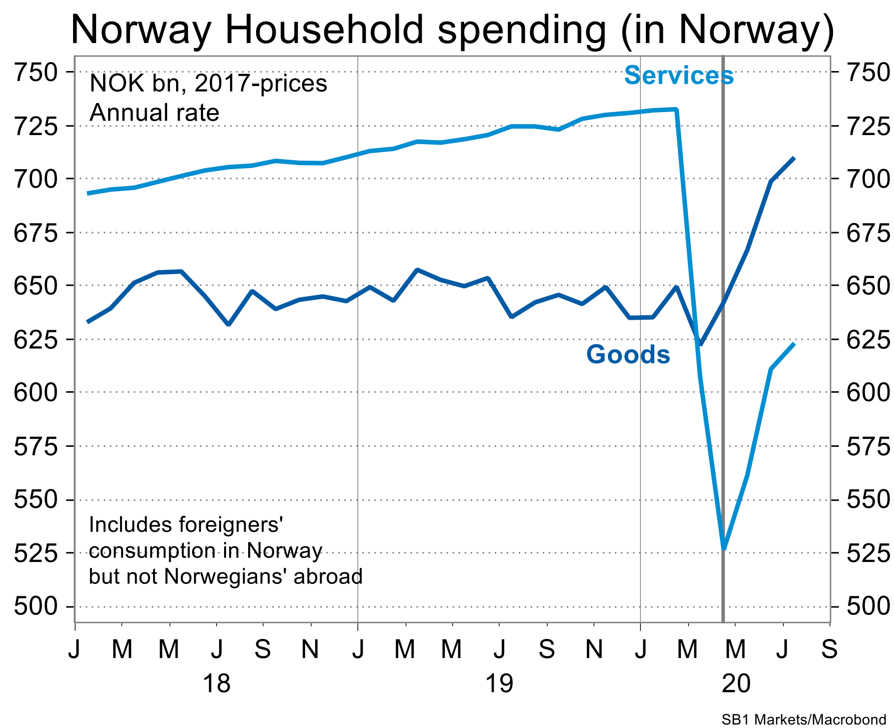


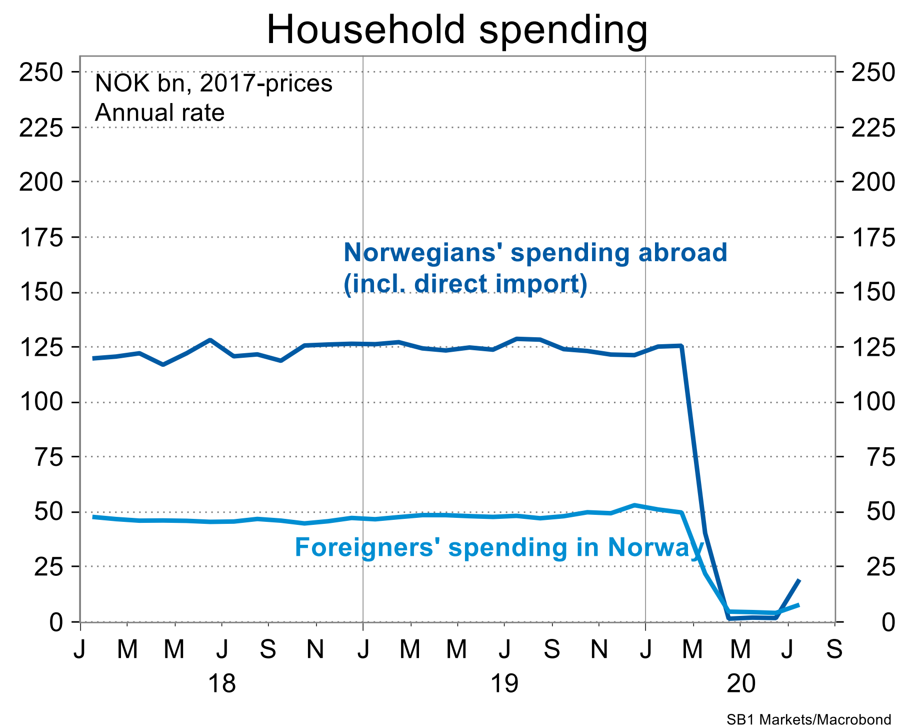


SpareBank 1 MARKETS

Consumption of goods up 9% from February, services down 15%

Norwegians' spending abroad 'collapsed', improved in July. Foreigners' are still not spending here

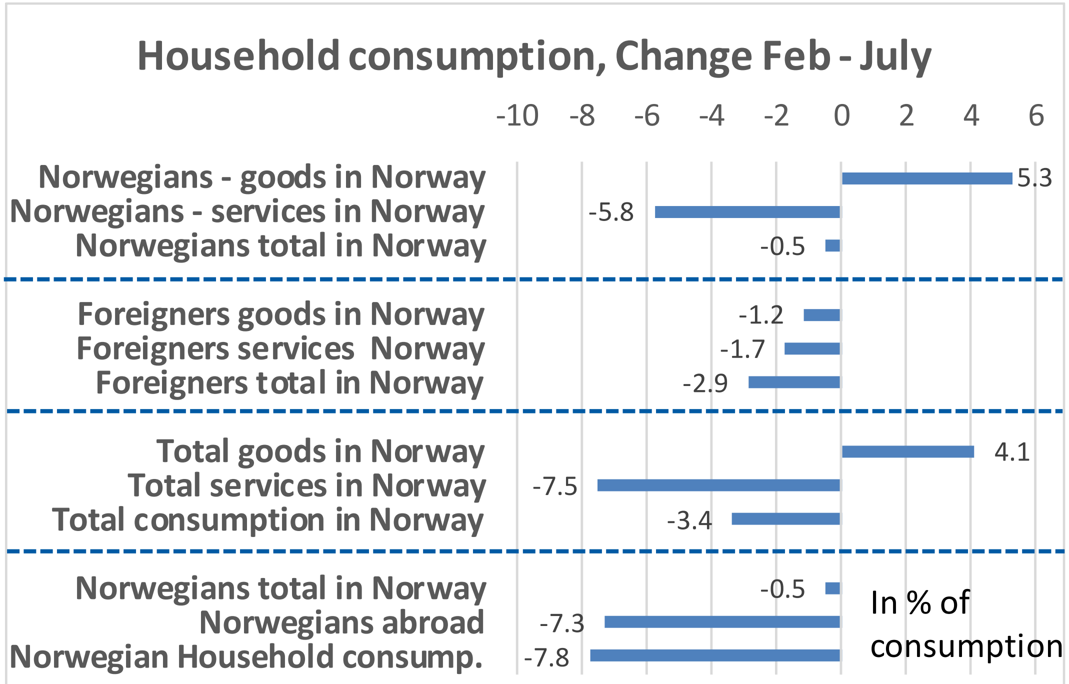




- Norwegian households have reduced their consumption abroad (=lower imports) much more than foreigners have reduced their consumption in Norway (lower exports). Check the next two pages for details

Norwegians are consuming like normal, in Norway

Goods consumption has been soaring, services cut sharply. And no foreigners are consuming here!

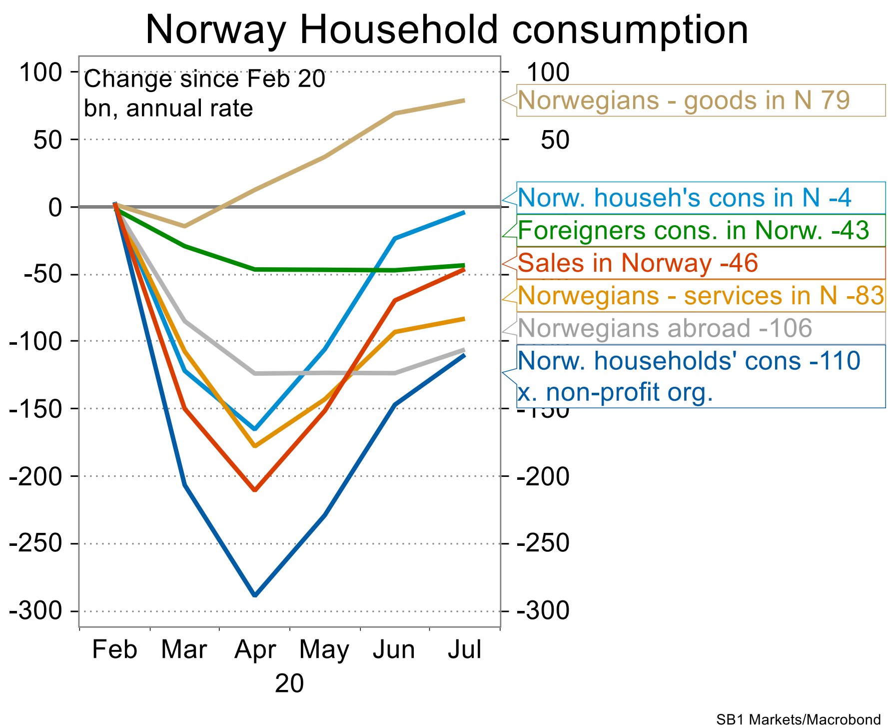


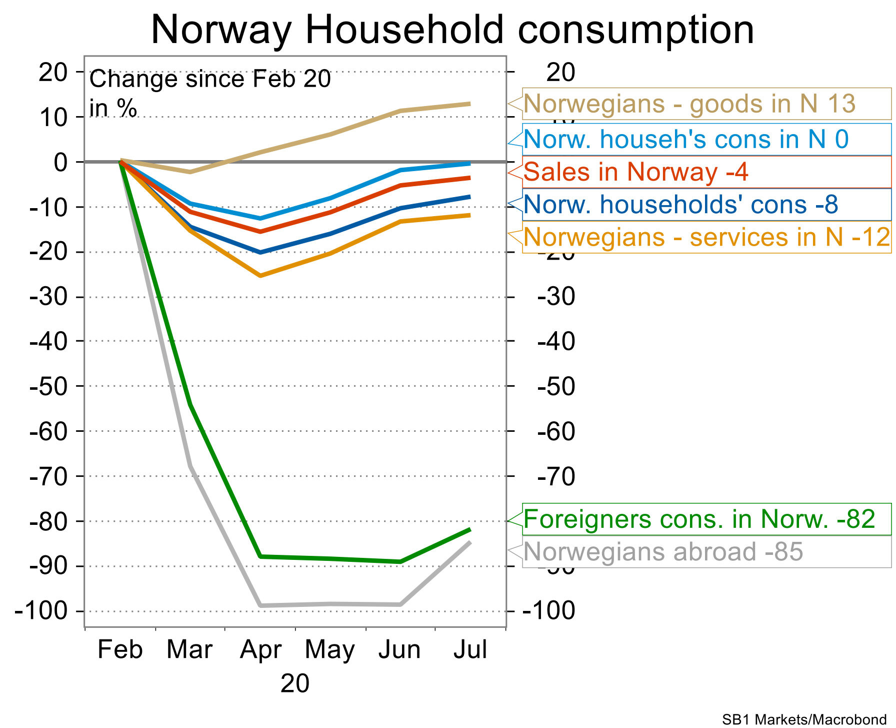
- Norwegian households have reduced their consumption of services in Norway more than they have lifted their consumption of goods – in sum down 0.5% of total household consumption
- Foreigners have cut their spending in Norway equalling 2.9% of *total private consumption*
- Sales of consumption goods are up 4.1%, and services are down 6.9%. The total is down 3.4% - *all in % of total consumption*
- Norwegians have reduced their spending abroad equalling 7.3% of their total consumption – and total Norwegian household consumption is down by 7.8%
  - » Other countries 'have taken 94% of the beating' of the cut in Norwegian's spending (before calculating for import content in consumption
  - » Norwegians have reduced their consumption abroad almost 2.5 x more than foreigners have cut their spending in Norway (because Norwegians are spending 2.5 more abroad than foreigners in Norway)

SpareBank 1 MARKETS

Consumption: Another twist of the numbers

Domestic consumption flat, but sales of consumer goods & services down due to the foreigners

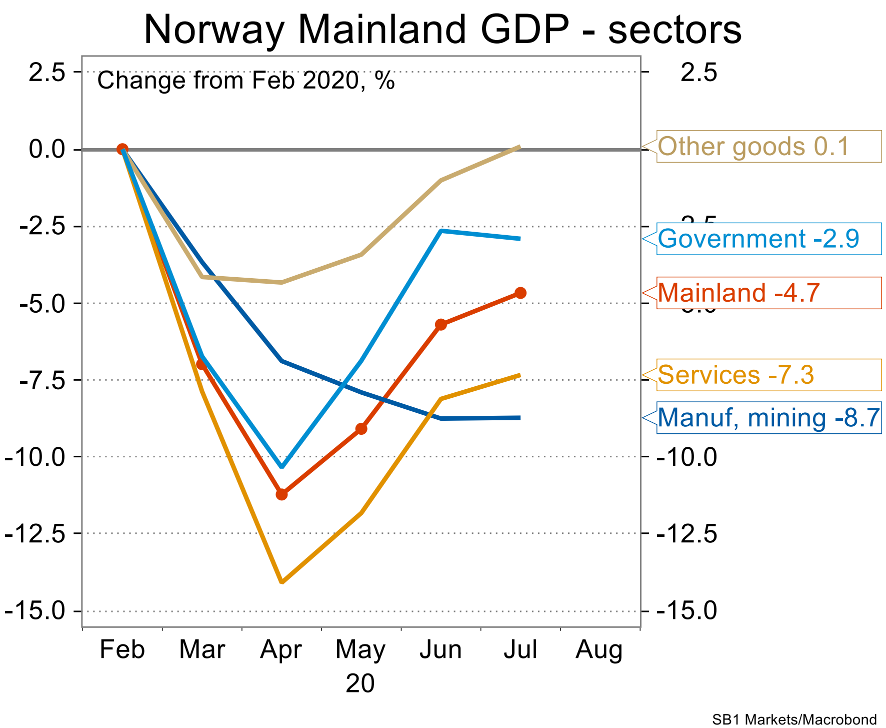


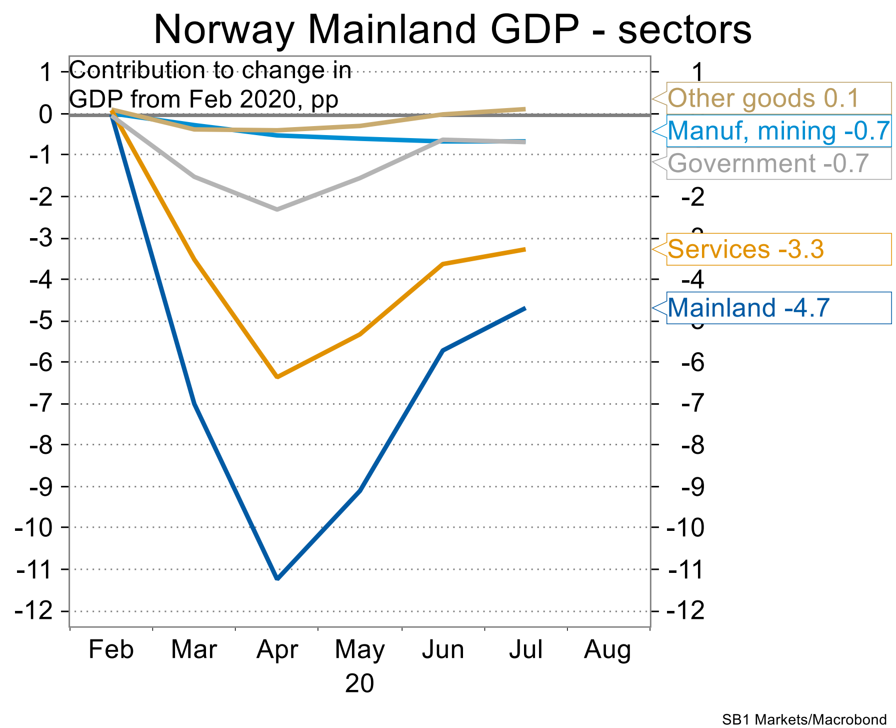


- Norwegian households have reduced their consumption by 8% or 124 bn (annual rate) – of which 106 bn abroad (-106%) and just 4 bn in Norway! Their consumption of goods is up 13% (79 bn), while their spending on services in Norway is down 83 bn or 12%!
- Sales of goods and services in Norway to Norwegians and foreigners are down by 4% or 46 bn – of which 43 bn is due to lower demand from foreigners in Norway (down 43%) and just 3 bn due to lower domestic demand from Norwegians
- Norwegian households' consumption of services is increasing but remains well below the pre corona level. In July, some few foreigners started buying in Norway again – and Norwegians will buy somewhat abroad

The production side: Manufacturing even weaker than services vs February

Services production is down 7.3% from the pre corona level, manufacturing & mining -8.7%

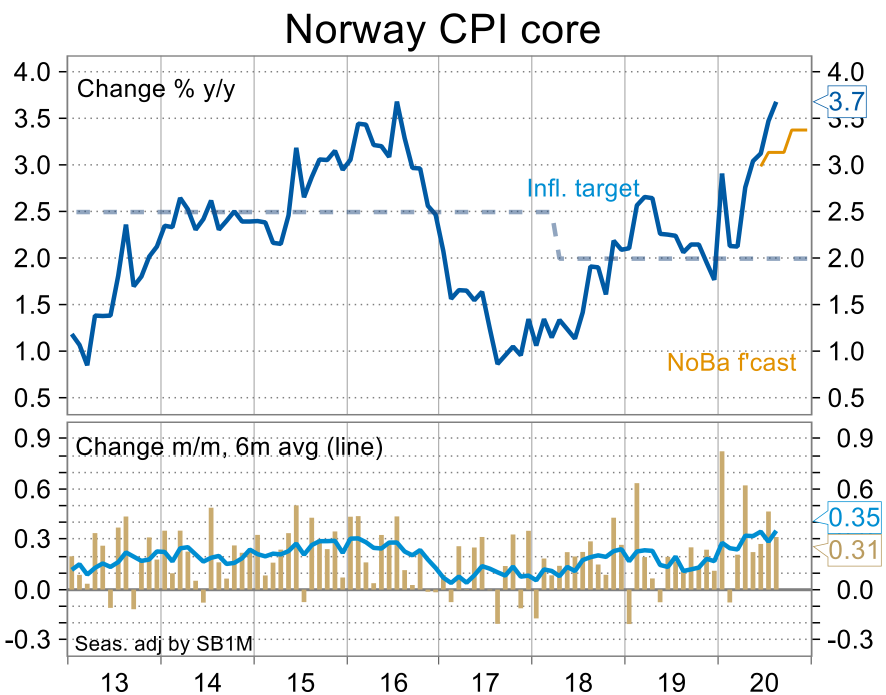




- We think the downside risk for the manufacturing sector is limited as oil related production has fallen substantially vs. the decline in oil investments (check more here). A minor recovery in H2 is more likely, given the recovery in the global manufacturing sector
- The upside potential for the service sector is probably limited as long as the corona virus stays around

Core CPI accelerated to 3.7% in August! Most likely not a lasting problem

Inflation is running well above the target, highest in 4 years. Total inflation still moderate at 1.7%



- CPI-ATE (ex. energy and taxes) inflation rose 0.2 pp to 3.7% y/y in August, we and consensus expected a downtick to 3.4%. Inflation is running well above Norges Bank's forecast, the bank expected a 3.1% average in Q3
  - » Prices rose 0.3% m/m (s.a), we expected 0.1%
  - » Inflation is above 2% for all major sectors, except housing and clothing/footwear
  - » Import prices have increased faster than our models indicate, now up 4.6% y/y, bringing core inflation up
- Total inflation accelerated to 1.7%, up 0.4 pp. Electricity & gasoline prices – explains 1.5 pp of the divergence to the core CPI
- **The price outlook**
  - » Impacts of the corona crisis are mixed
    - A weaker economy suggests low inflation. Wage inflation is no doubt on the way down. However, strong demand for goods, may lead to wider (profit) margins
    - The weak NOK has lifted inflation, however, this impact will soon fade as the NOK has stabilized
    - Energy prices have fallen
  - » Our take is that the overall impact will be a slowdown in inflation. But it may take some months before these changes are reflected in the CPI
  - » Anyway, CPI inflation will not have any material impact on Norges Banks and monetary policy the coming months. Wage growth will no doubt slow. At the Sept 24 meeting, Norges Bank will probably blame temporary factors and project a slowdown the coming quarters

Most sectors surprised on the upside in August, just clothing down

Prices are accelerating in many sectors. Food, furnishing and recreation increased the most in Aug

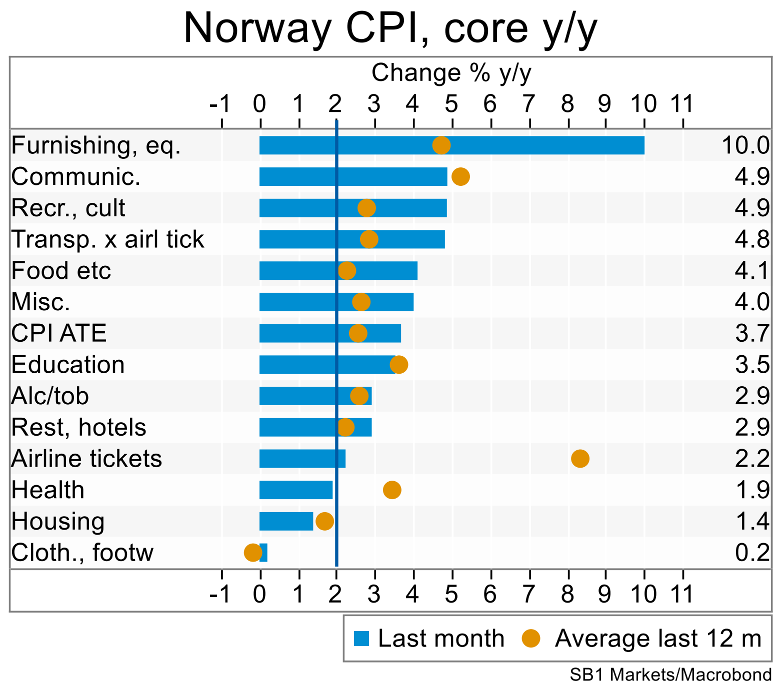
		Change m/m, seas. adj			Change y/y			Contribution, pp		
Aug-20	Weight	Out-	SB1M	Dev.	Last	Out-	SB1M			Dev. vs
CPI ATE	%	come	f'cast	pp	month	come	f'cast	m/m	y/y	f'cast
Food, non alc bev	12.5	1.1	0.2	0.9	2.5	4.1	2.8	0.13	0.51	0.11
Alcohol, tobacco	3.9	0.3	0.2	0.1	2.7	2.9	2.8	0.01	0.12	0.00
Clothing, footwear	4.9	-2.3	0.0	-2.3	2.1	0.2	2.2	-0.11	0.01	-0.11
Housing x. energy	20.1	0.4	0.1	0.3	1.3	1.4	1.1	0.08	0.28	0.06
Furnishing	6.6	1.0	0.0	1.0	7.5	10.0	7.9	0.07	0.66	0.07
Health	3.2	0.4	0.2	0.2	3.5	1.9	1.5	0.01	0.06	0.01
Transp. ex. gas, airl. tick	12.0	0.0	0.3	-0.3	5.0	4.8	5.1	0.00	0.58	-0.03
Airline tickets	1.2	0.6	0.0	0.6	4.1	2.2	1.1	0.01	0.03	0.01
Communication	2.2	0.4	0.2	0.2	5.1	4.9	4.3	0.01	0.11	0.00
Recreation, culture	11.9	0.6	-0.3	0.8	4.3	4.9	4.0	0.07	0.58	0.10
Education	0.5	-	-	-	3.5	3.5	3.5		0.02	0.00
Restaurants, hotels	6.2	0.2	-0.3	0.5	2.8	2.9	2.4	0.01	0.18	0.03
Other	8.8	-0.1	0.1	-0.2	4.2	4.0	4.2	-0.01	0.35	-0.02
CPI-ATE	94	**0.3**	**0.1**	0.3	**3.5**	**3.7**	**3.4**			
Imported	33	0.4	-0.0	0.5	3.8	4.6	4.0	0.14	1.51	0.15
Domestic	61	0.3	0.1	0.2	3.5	3.7	3.4	0.19	2.23	0.15
Energy, housing	4	2.1	4.0	-1.9	-35.1	-33.4	-32.3	0.08	-1.29	-0.07
Energy, transport	4	-2.5	0.5	-3.0	-4.5	-5.0	-2.0	-0.09	-0.18	-0.11
CPI Total	101	**0.3**	**0.1**	0.2	**1.3**	**1.7**	**1.3**	0.27	1.74	0.19
Change m/m based on seasonally adjusted data										
Sum of parts does not necessarily add up to totals										
Norges Bank m/m s.a. estimate is implied, calc by SB1M										

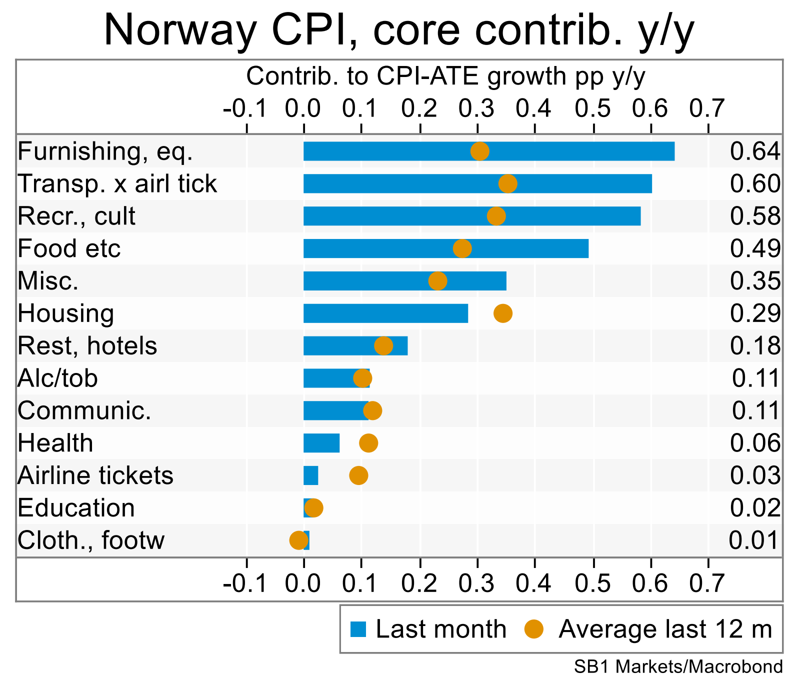
- Food price inflation up to 4.1% y/y, higher than we expected. Demand is no doubt strong
- Clothing prices fell sharply in August and are up just 0.2% y/y, far below our f'cast
- Furniture prices are up 10% y/y! Demand is up, but the NOK impact will soon fade?
- Car prices are up 3%, rising sharply. NOK impact
- Recreation and culture rose more than expected in Aug, up 4.9% y/y. Demand/NOK impact
- **CPI-ATE up 3.7% y/y, highest in 4 years**
- Imported prices rose by another 0.4% m/m, the annual rate accelerated to 4.6%. Will probably slow as the NOK impact fades
- Electricity prices are down 33% y/y
- Total inflation up 0.4 pp to 1.7%

Monthly changes are seasonally adjusted by SB1 Markets. The weighted sum of the components does not necessarily sum exactly up to the total. Norges Bank m/m s.a. estimate is implied, calculated by us. Sources: SSB, Norges Bank, SB1 Markets calculations

Furnishing, recreation, transport ex fuel/airline have lifted annual core inflation

Furnishing prices up 10%! Just clothing & footwear, housing (rent) below the 2% inflation target

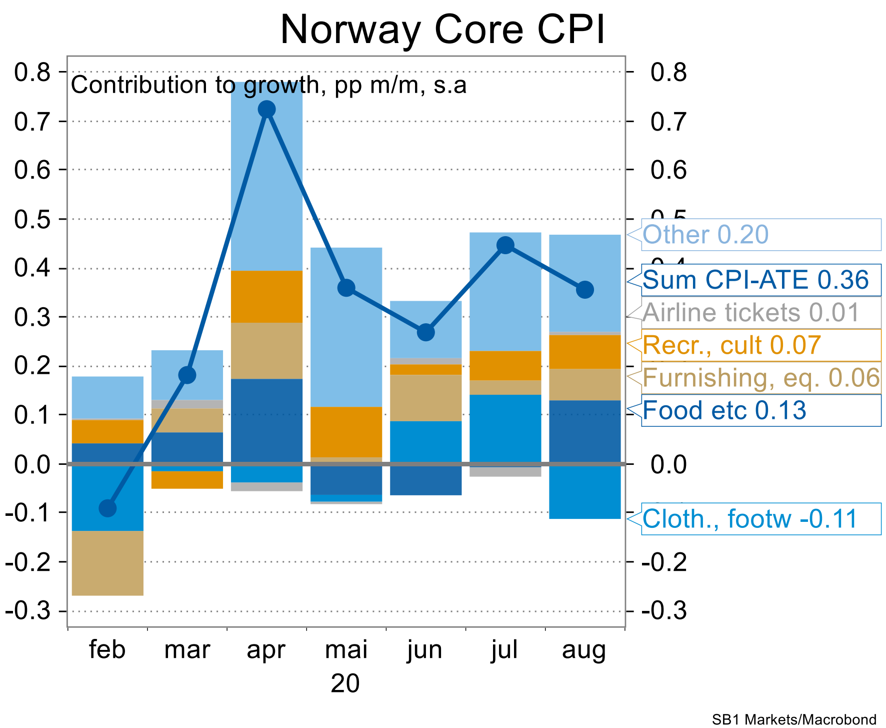


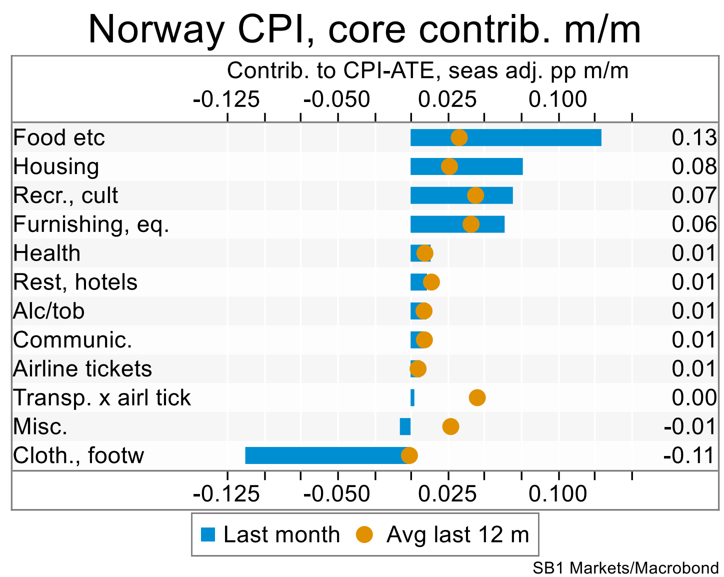


- Transport: Auto prices have increased rapidly the past few months, up 3% y/y (from -0.6% in May)
- Price growth has been accelerating in 9 sectors, slowing in 4

Just clothing & footwear a drag in August, all other sectors up

Food, housing (rent), recreation&culture and furniture contributed the most

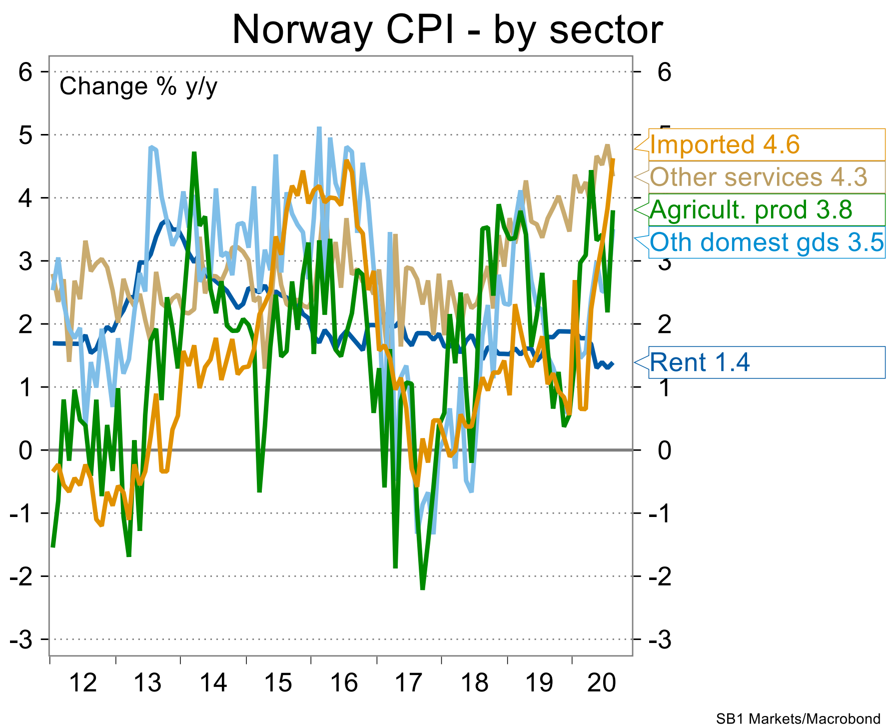


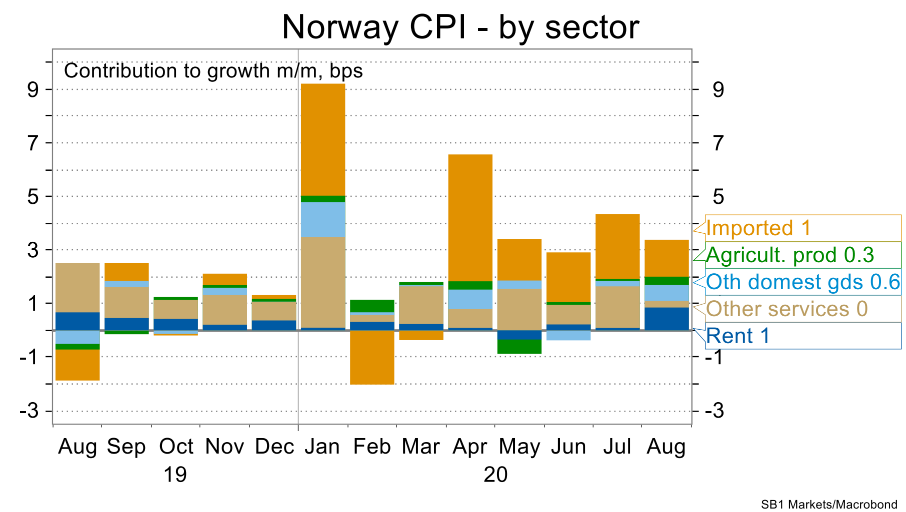


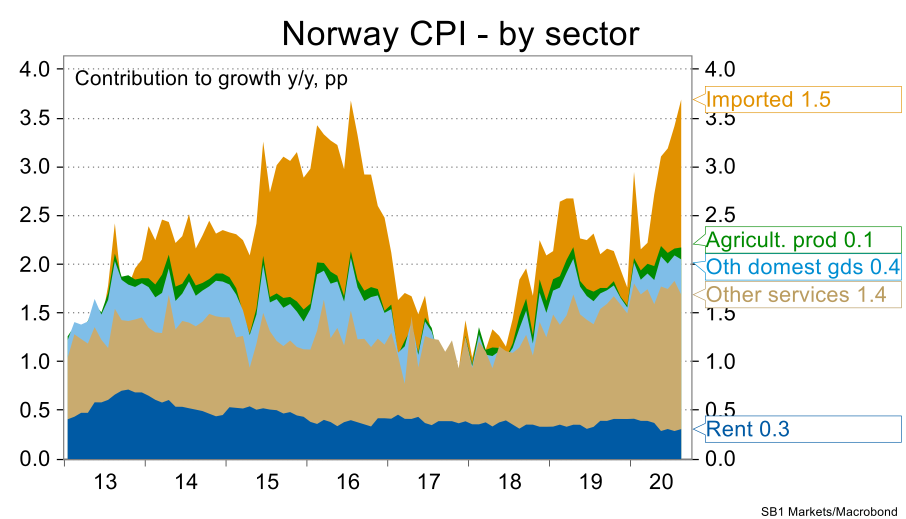
- The decline in clothing prices in August followed a large increase in July

Imported goods inflation is accelerating, to 4.6%, highest since 2016

Prices on imported goods are rising 1.1 pp faster than domestic goods, services up 4.3% y/y



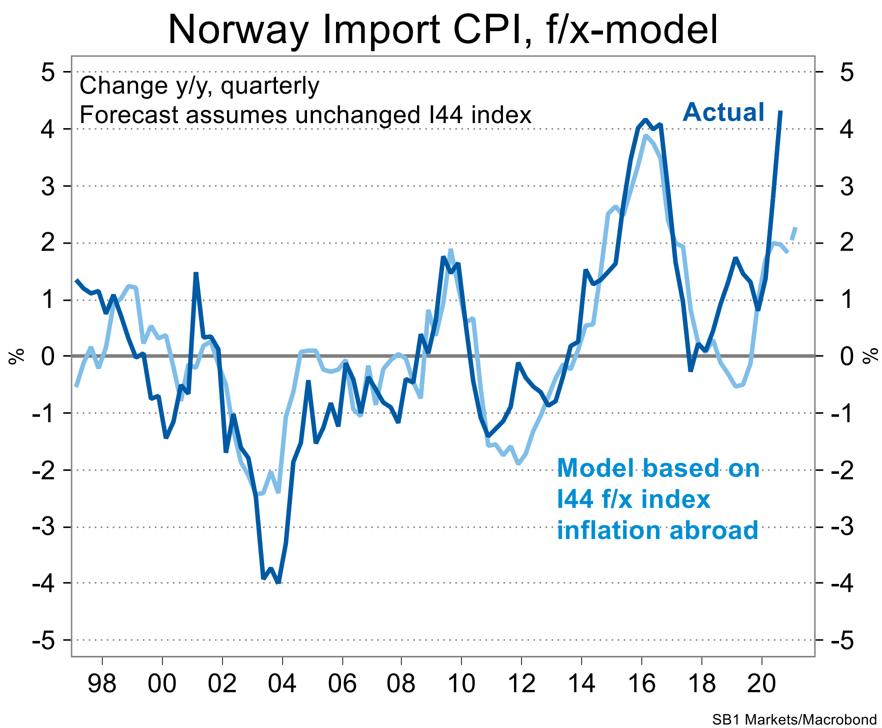


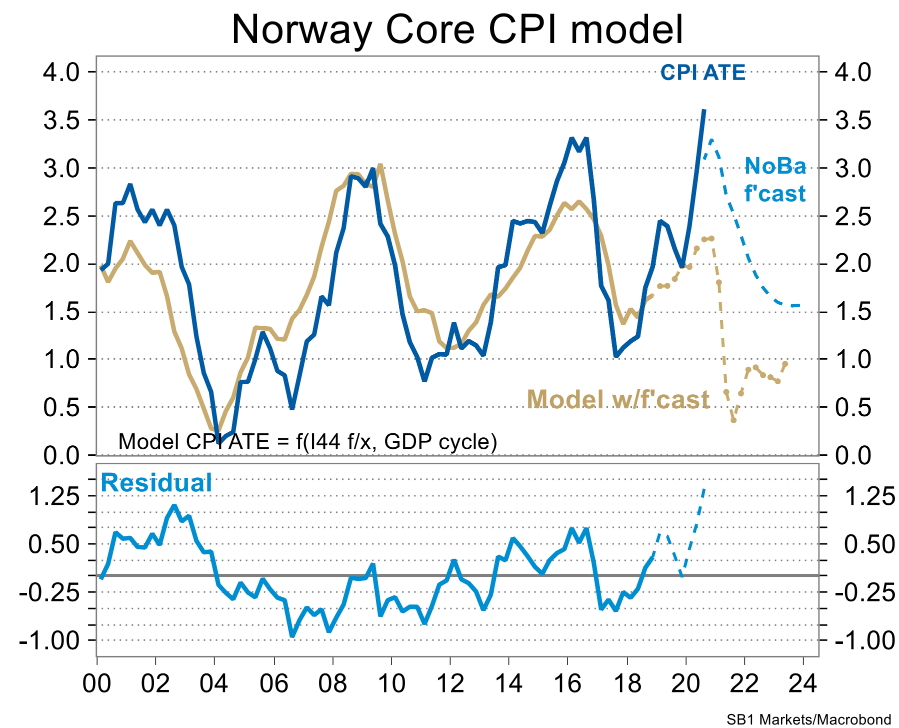


SpareBank 1 MARKETS

Imported prices: Too much up now? Should come down, soon

Our core CPI model is not calibrated for the present decline in GDP, but the sign is no doubt correct

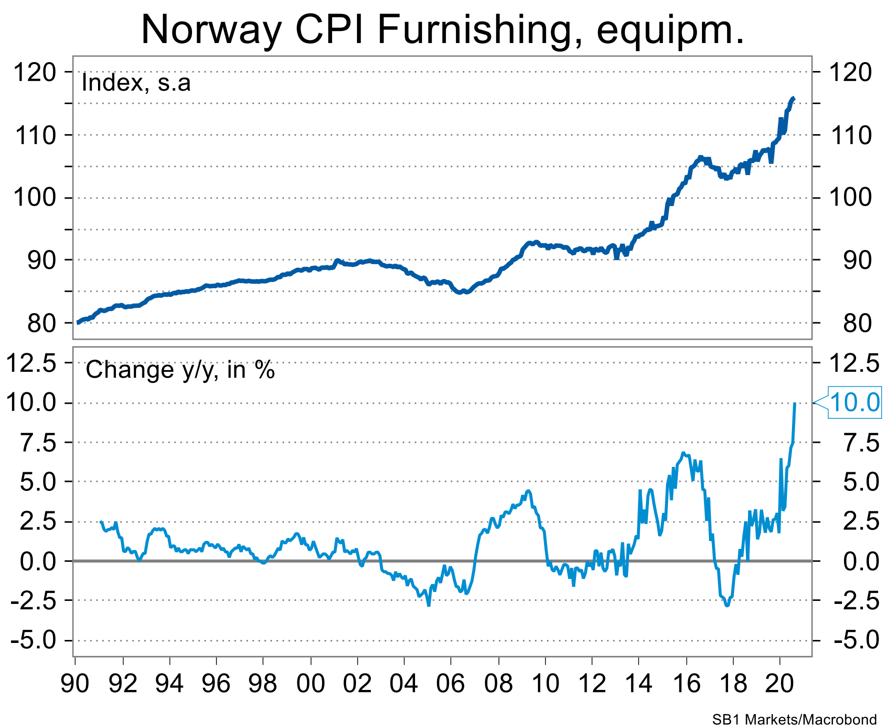


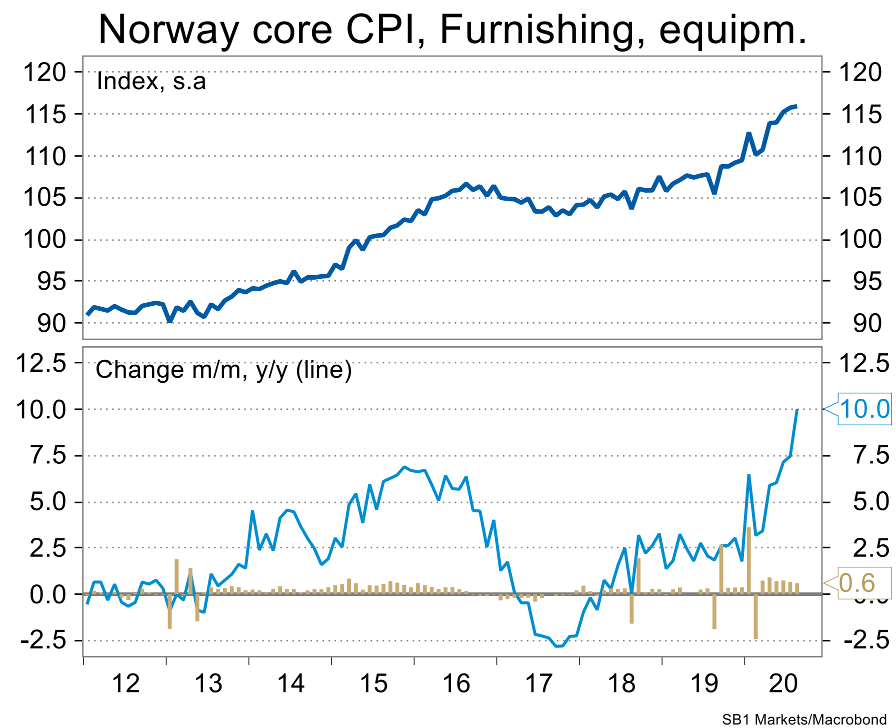


- The NOK steep depreciation in the winter/early spring is no doubt driving imported inflation up. It usually takes a few months before these impacts are reflected in the CPI. Closed borders due to Covid-19 may have contributed to the lift in import prices too, as have the strong growth in demand for some goods (like sport equipment/furniture).
- We expect inflation to slow down within the next few months as the NOK has stabilised

Steepest rise in prices on furnishing & houshold equipment on record

Explanation: A combination of a weak NOK (which has now stabilized) and strong demand

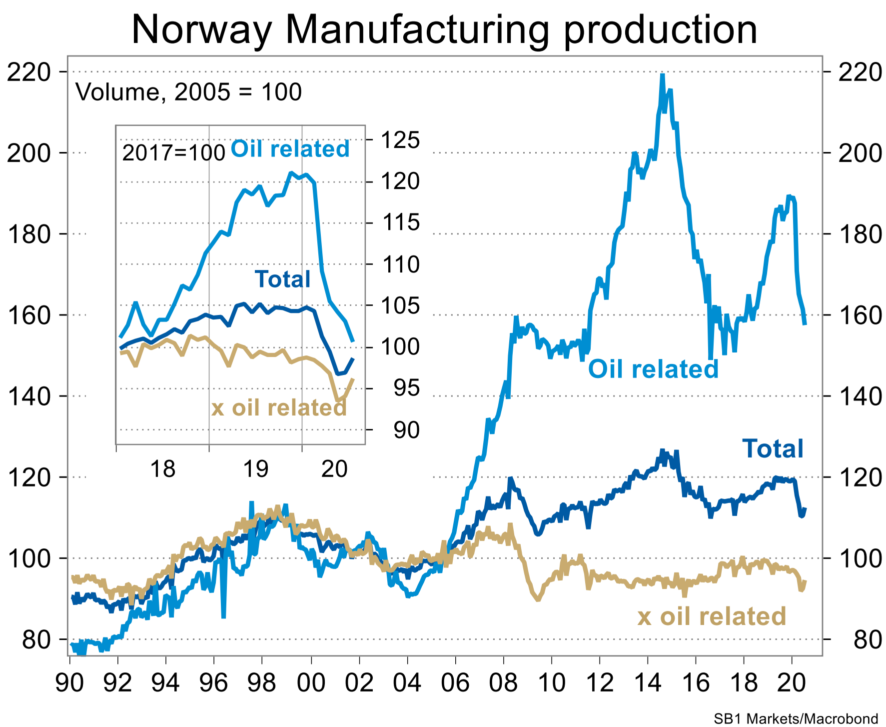


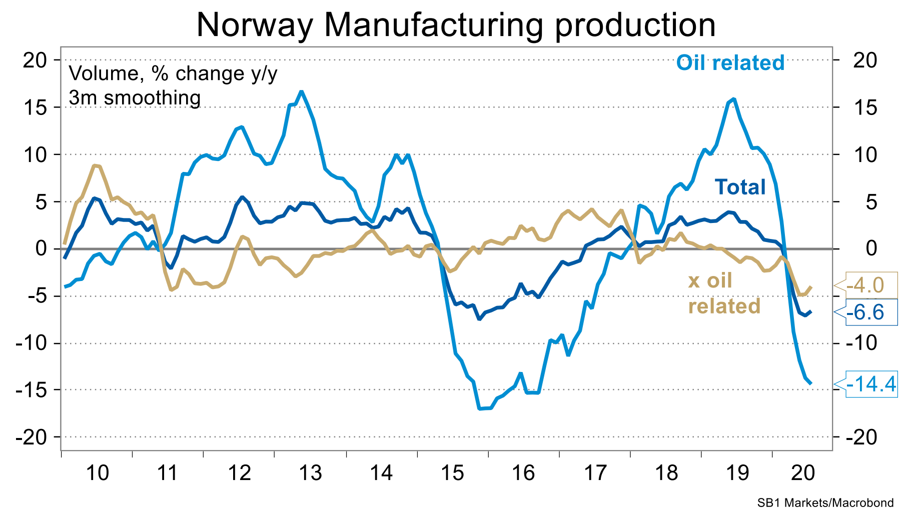


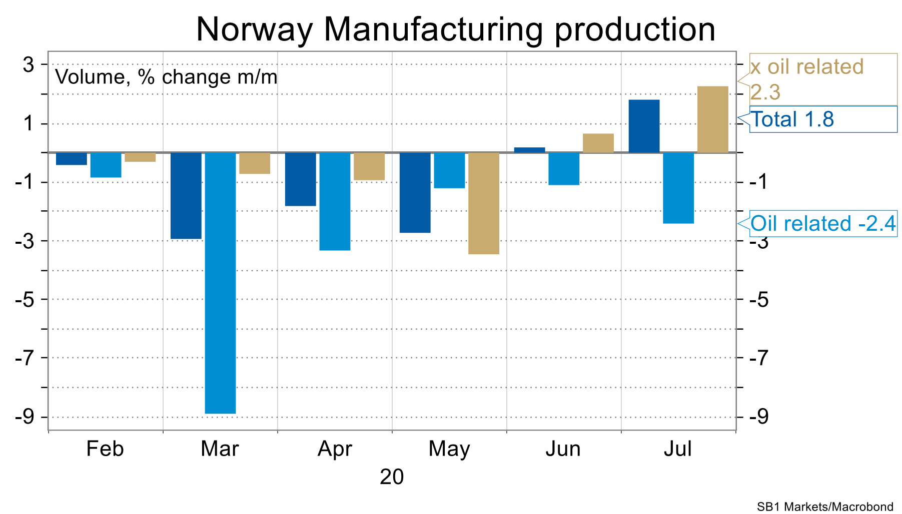
SpareBank 1 MARKETS

Manufacturing up 1.8% in July, down 5% since Feb

Production rose more than expected in July, thanks to non-oil sectors. Oil related has fallen enough?



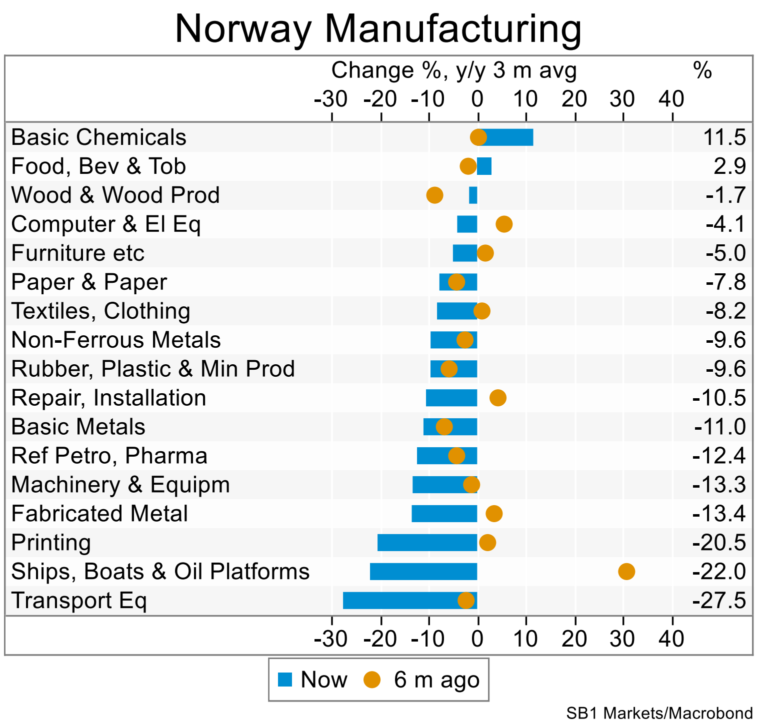


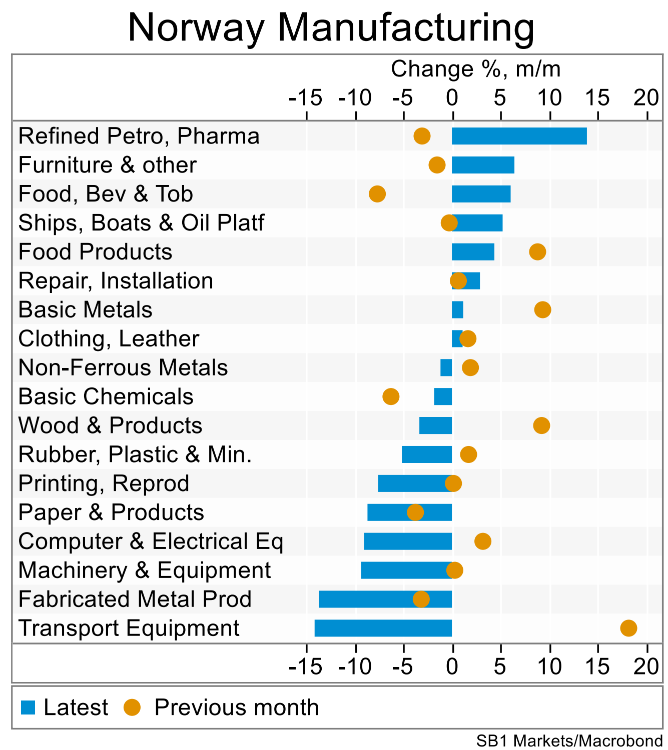


- Oil related manufacturing production has fallen by more than 15% since early 2020. Oil investments have fallen less – and may be stabilising the coming months. Little downside risk from here? Or some upside potential?
- Production in other sectors is down just 2% since Feb (however, it was rather soft before corona hit, trending slowly down since late 2018)
- Surveys, including the weak August PMI, signal a decline in production but not increased activity in manufacturing among our trading partners

An unusually broad downturn, just food, basic chemicals and food OK

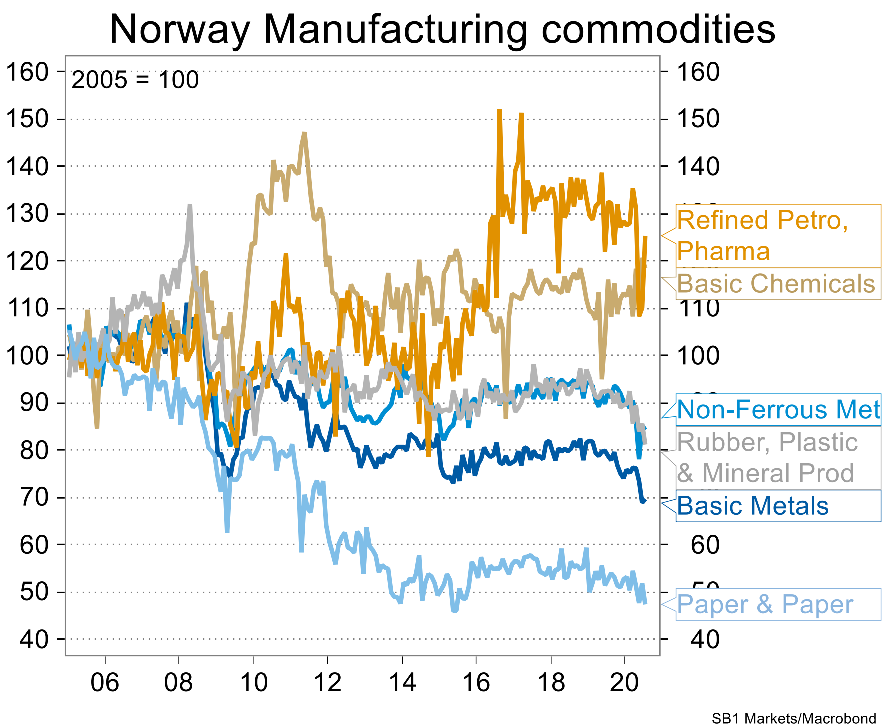
All other sectors are down y/y – but some have been increasing production recent months

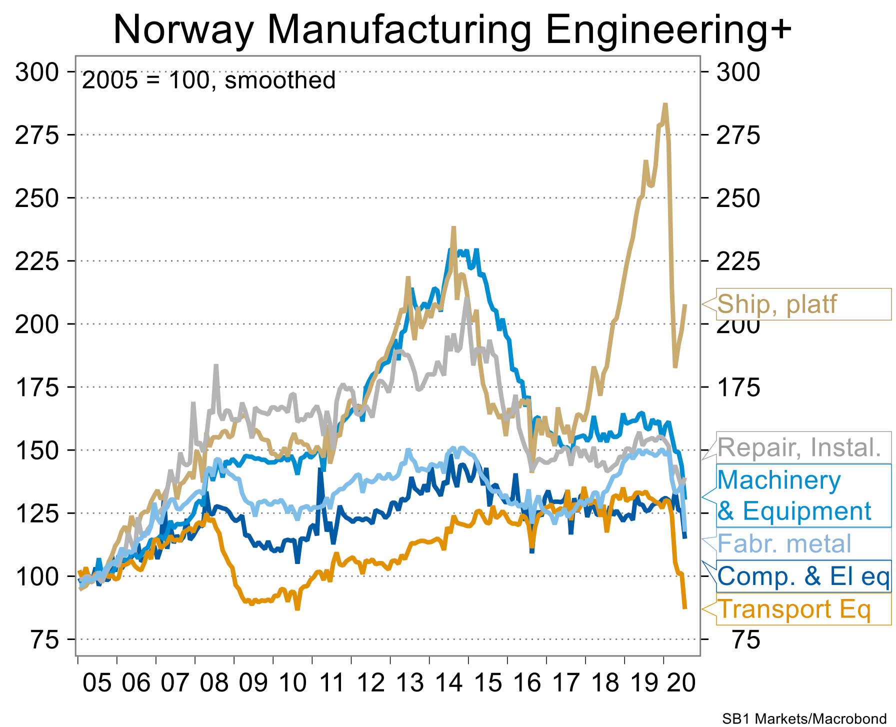




Production in engineering sectors steeply down

Most other sectors hit too. Production of ships/platforms up in May-July, down 28% from Jan

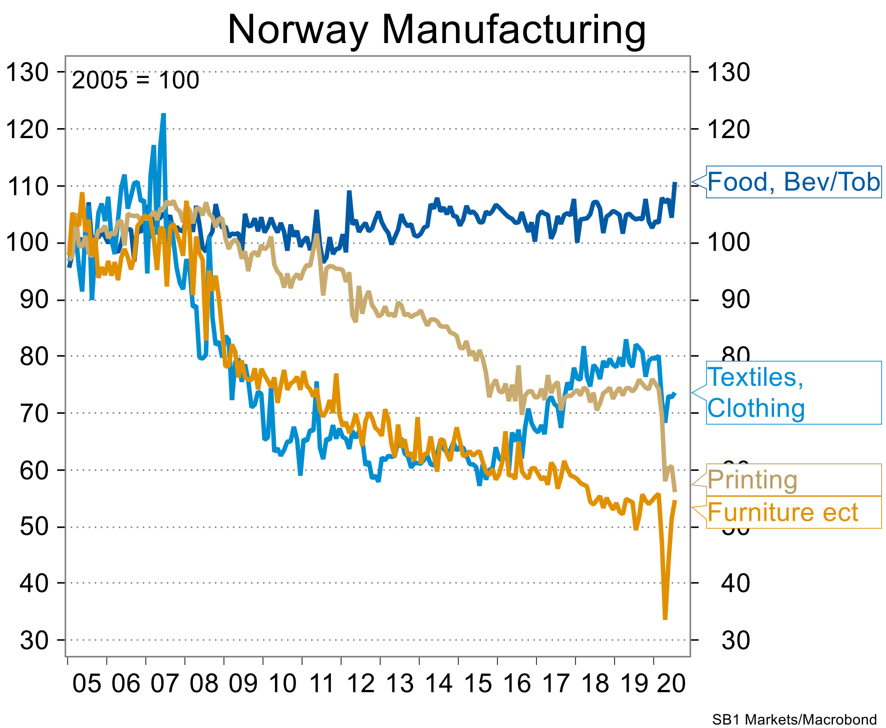




- Ships/platforms: Still above the 2016/17 ‘oil crisis’ downturn following an extreme downturn – which CANNOT be explained by the corona crisis as production is based on long term orders/contracts. The decline is rather due to ‘holes’ in order books as the Johan Sverdrup field is completed (and it was signaled by both oil companies and manufacturers before the corona crisis)
- Engineering sectors: Most partly oil-related sectors have lost some steam, particularly machinery & equipment production and transport equipment
- Commodities: None are impressive, refined petroleum and pharmaceuticals recovered some of the loss in July

We still need food (and more than usual, as we buy/eat less abroad)

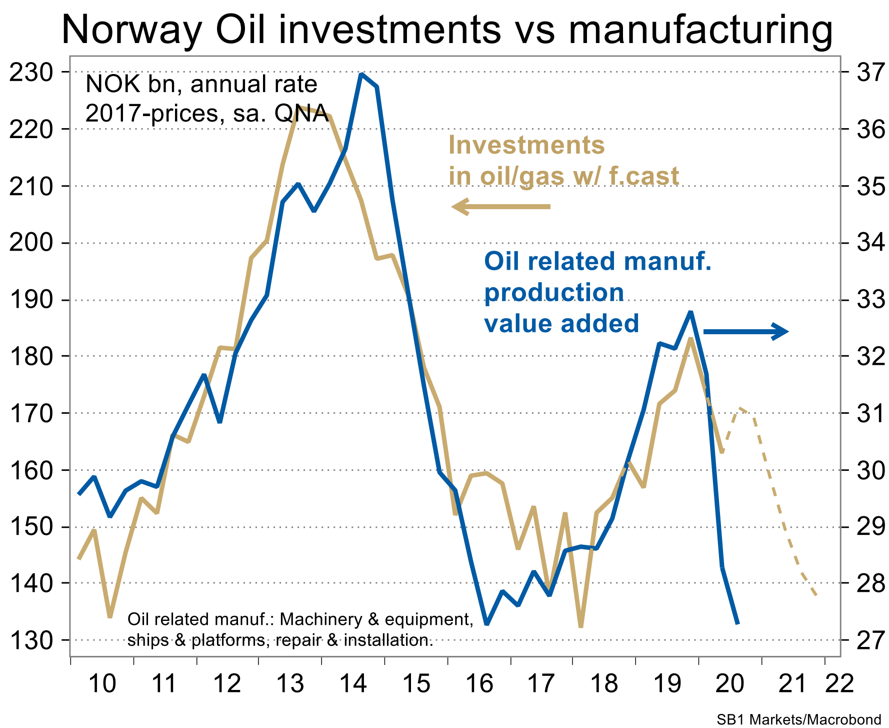
Other domestically oriented sectors down during the corona crisis…



- … but all bottomed in April, and production of furniture is now back at a 'normal' level

Oil related production has soon fallen enough?

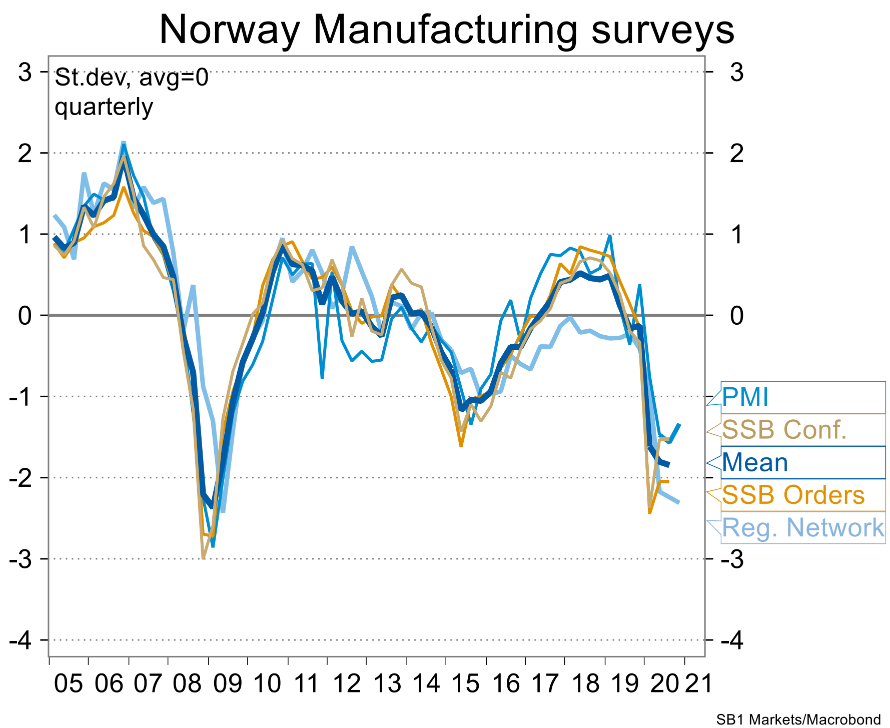
Oil investments are heading down but oil related production has fallen quite a lot already

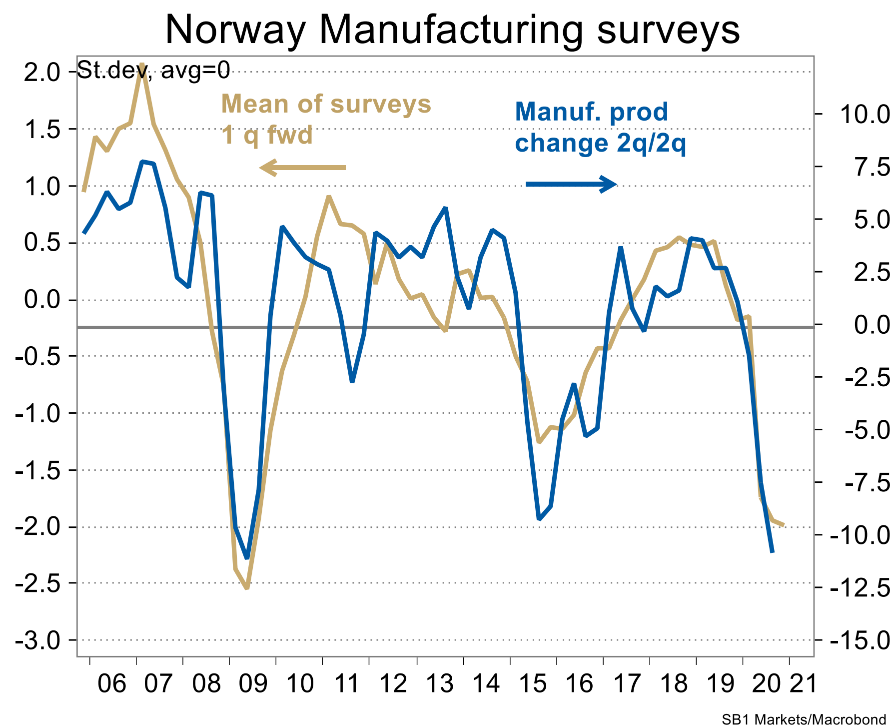


- Both oil sector investments and oil related manufacturing production peaked in Q4 last year, as we forecasted long time ago (before corona hit)
- Oil companies have for a long period signalled a substantial decline in investments on the Norwegian shelf through 2020 and 2021 – and they did not løin the Q3 investment survey
- The substantial cut in oil taxes decided by the Parliament in June may increase oil companies' investment appetite but probably not already in 2021
- Oil related manufacturing production has fallen sharply since early 2020, and the downside is probably limited from the present level, given the decline in oil investments so far

Manufacturing surveys are not signalling a recovery

All manuf. surveys fell rapidly and none have yet suggested a comeback





- Some of these surveys are already ‘outdated’. The Regional Network was published in May, SSB’s survey in Q2, the Q3 report will be released this week. However, the PMI which was published in August signals a continued decline in production (we trust PMI data less than usual these days, as these surveys are usually late to announce a recovery after a steep downturn)

Highlights

The world around us

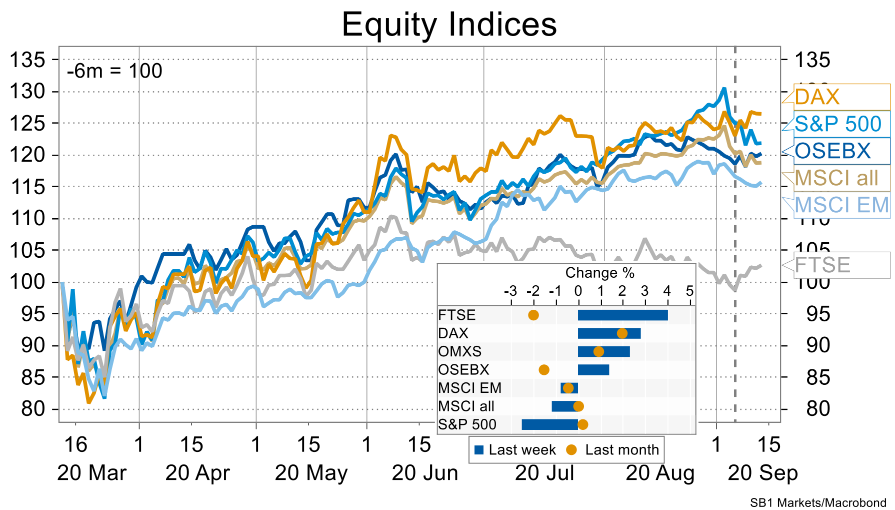
The Norwegian economy

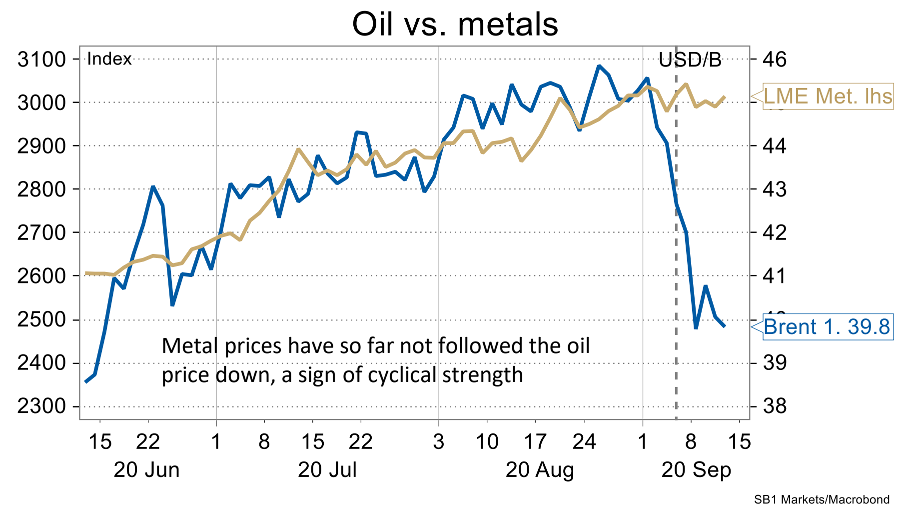
Market charts & comments

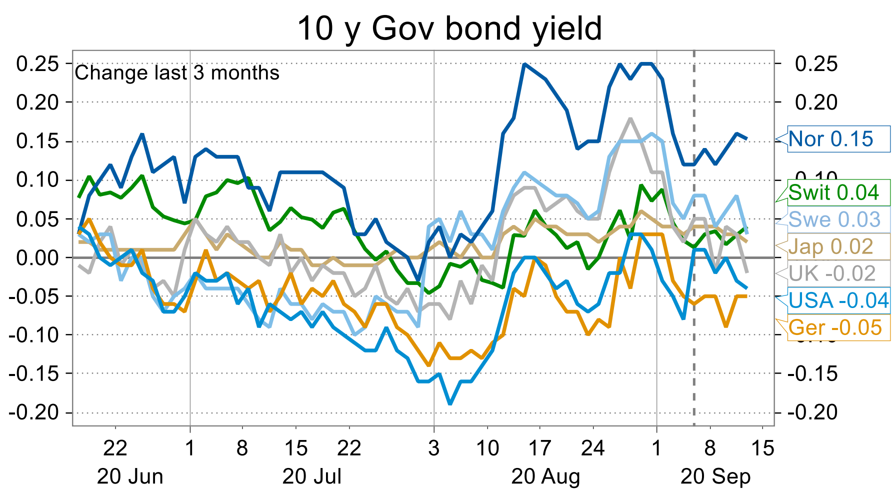
SpareBank 1 MARKETS

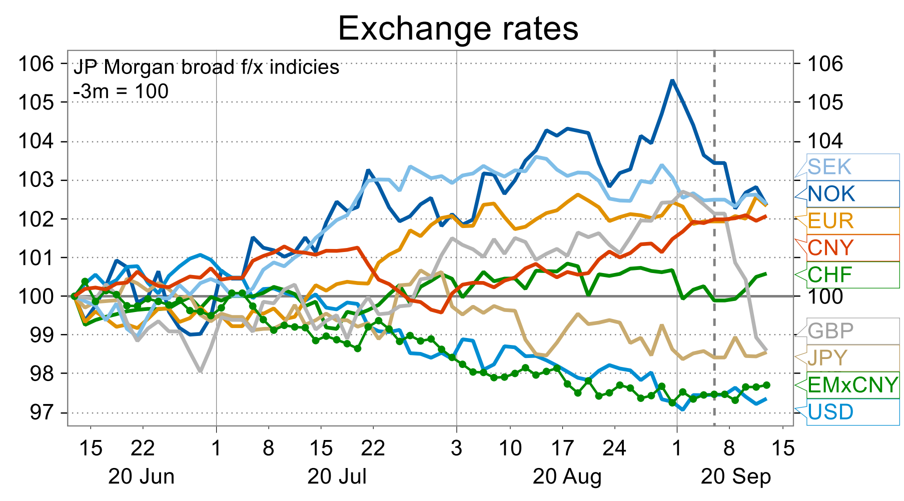
US down but most other stock markets up; bonds mixed too. Oil sharply down

S&P down 6.7% from early Sept peak. Oil down to below USD 40/b. GBP sharply down, Brexit trouble, again





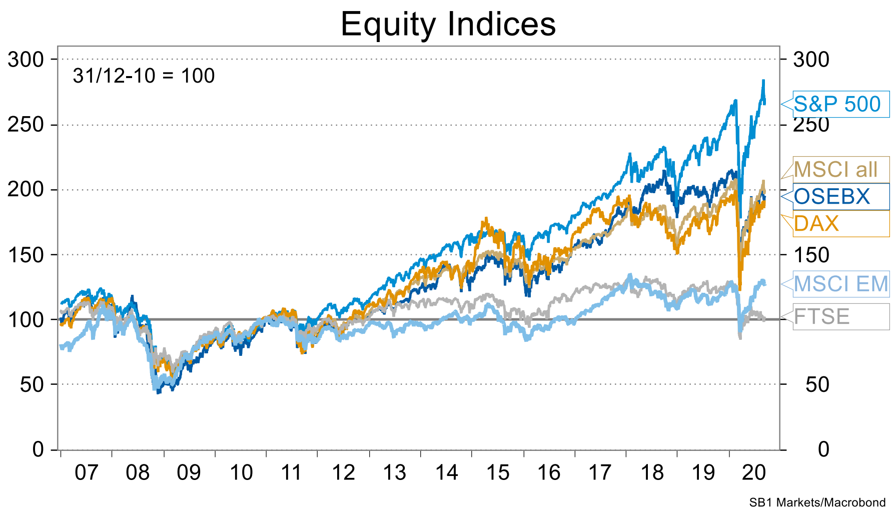


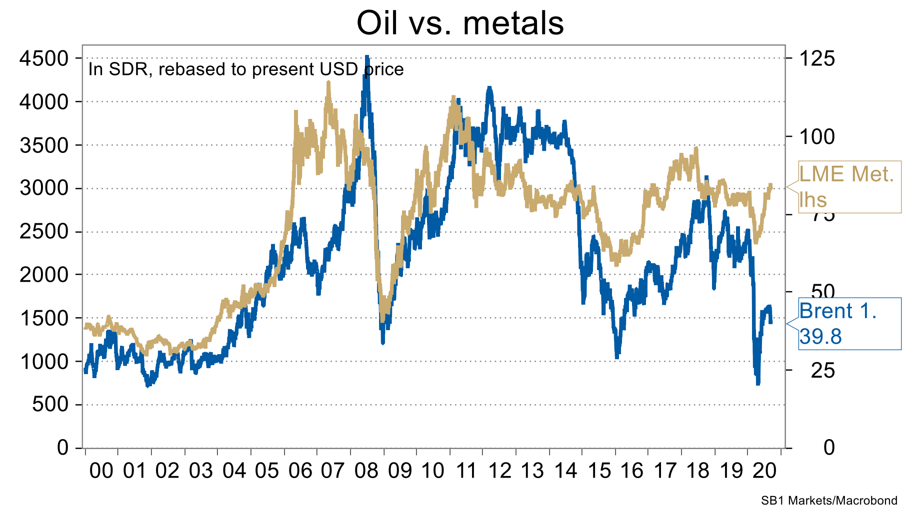


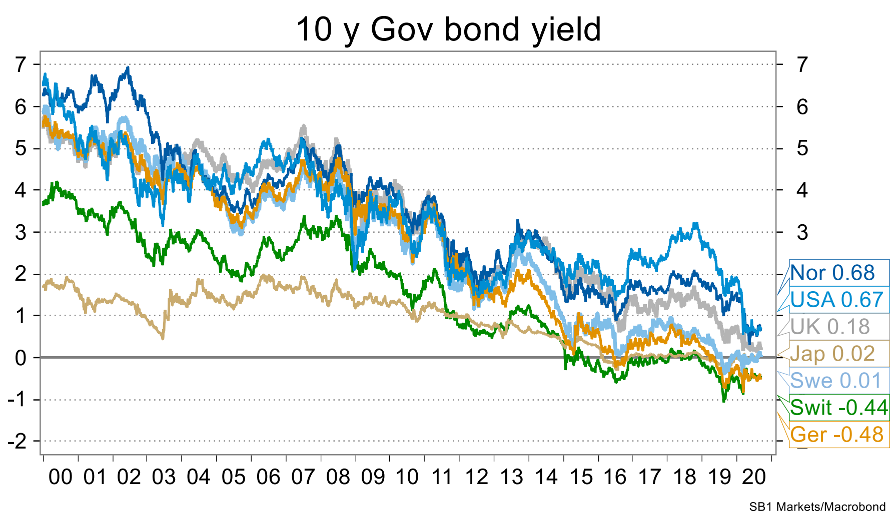
The USD is still sliding down but is not yet weak. NOK further down but the big loser last week was

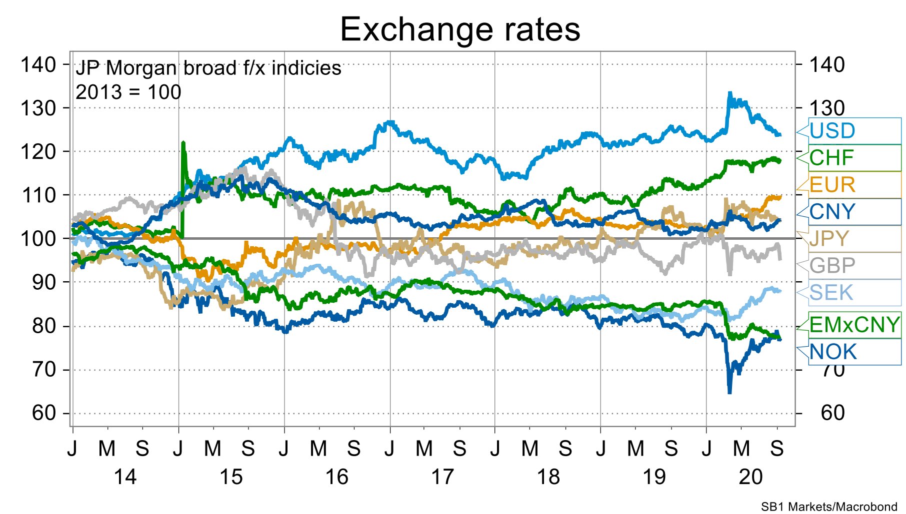
In the long run: Stock markets are looking like a ‘V’ (except the FTSE!!)

Bond yields are still close to record low everywhere. The USD is on the way down, NOK on the way up





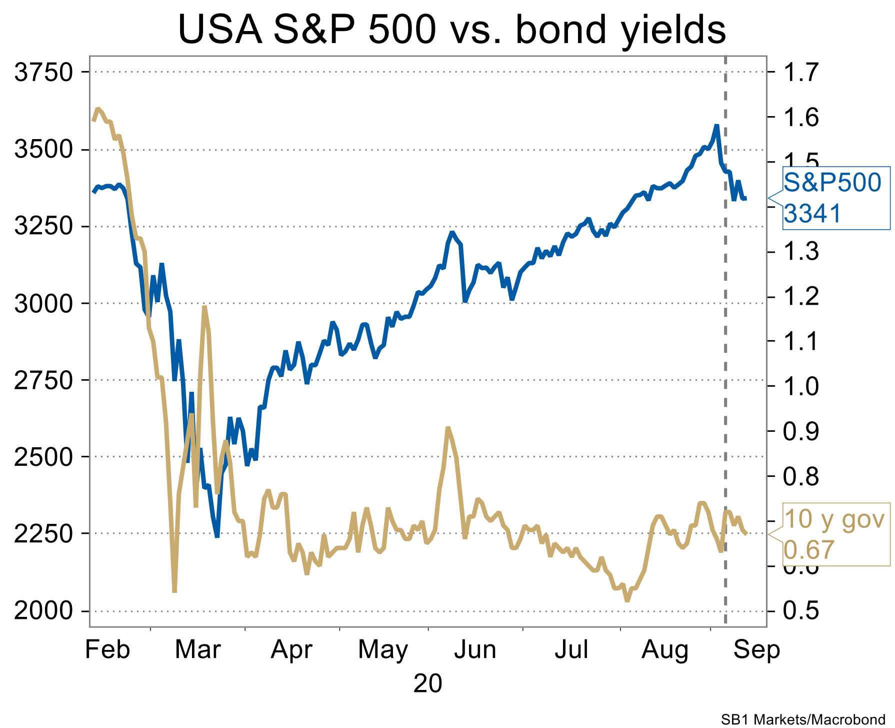


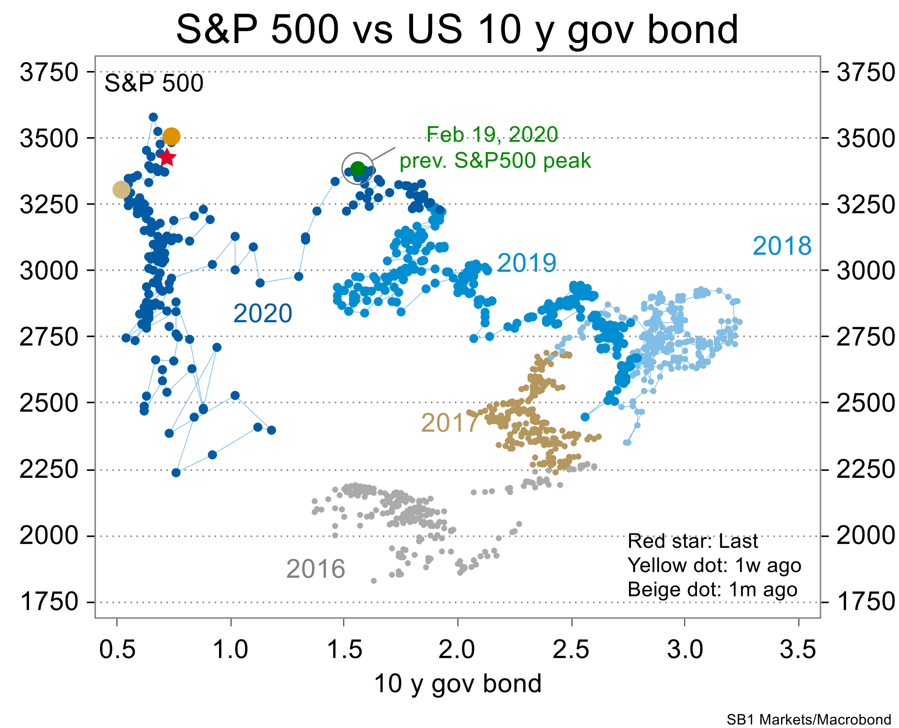


The USD is down but still not weaker than in Feb – and over the previous years (measured by broad f/x indices)

So far, a modest setback at the stock market, and yields are not yielding

S&P down 2.6% on the week, -6,7% from ATH. Bond yields marginally up

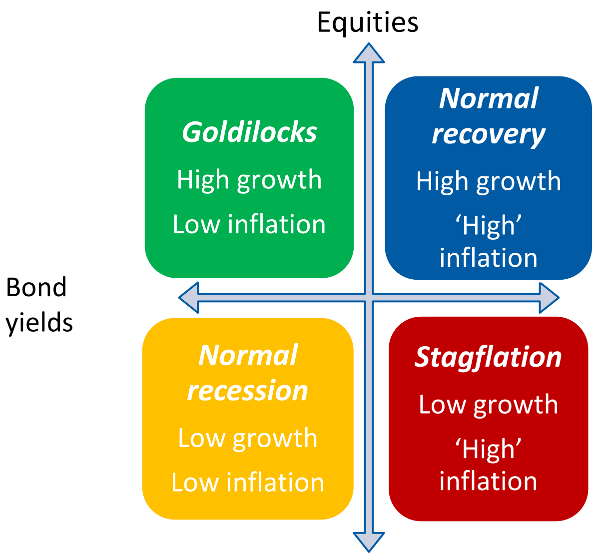


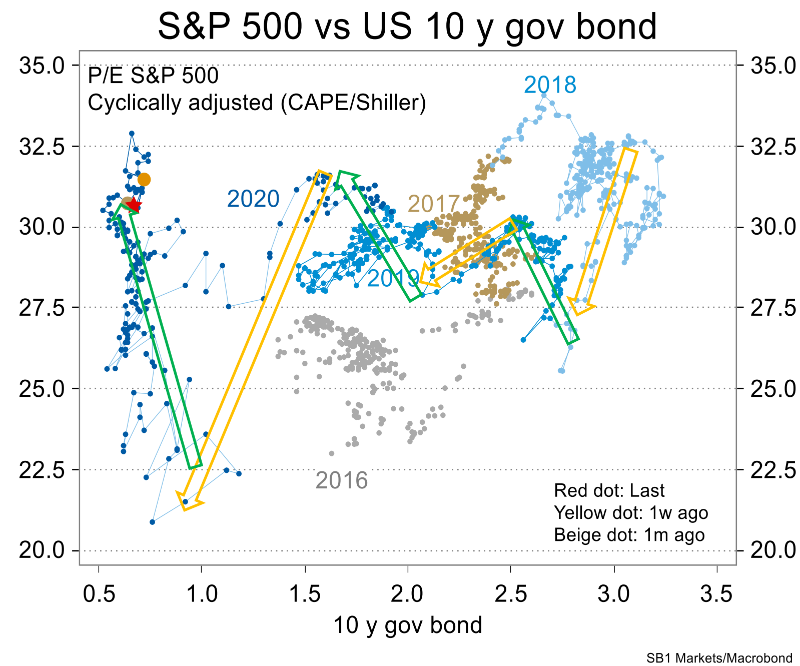


- The 10 y bond yield fell 5 bp last week, less than the ascend the previous week

From the 'Goldilocks corner', where to go?

Fed's new strategy implies low rates even if inflation should climb to above the target





- Usually, we have associated drifts towards the 'green corner' - low inflation and solid growth at the same time - as temporary sweet spot for markets were growth above trend had not yet created imbalances in the economy – or at least not inflation.
- Now, the US Federal Reserve promises to keep monetary policy expansionary, until actual inflation has overshot the 2% target for a while, in order to bring average inflation over some years (not defined, but say some 5 years) back up to the 2% target. As a bonus (at this stage of the cycle), that would also make it possible for the Fed to push employment higher, profits margins lower, and thereby contributing to reduced inequality
- Will we stay up there, in the green? Perhaps, for a while – but probably not, long term
  - » The economy has rebounded rapidly from the corona through in mid April, and corporate earnings will follow suit. Any substantial disappointment on corona/vaccine or the growth cycle in general would be challenging for the equity market. Short term, the risk seems limited
  - » The Fed will not yield from its new strategy anytime soon. However, (higher than expected) actual wage or price inflation numbers may shake the market's confidence in the sustainability of Fed's strategy, pushing long term bond yields up, both interest rate expectations and real rates. Again, the risk is not serious, short term, even if inflation is heading up following the initial corona slowdown
- Why are we sceptical vs. the long term outcome? Before corona, the employment rate was high in the core age group, businesses reported (and are now again (!) reporting) unprecedented lack of labour, wage inflation was not low vs. inflation or productivity. Profits were under pressure, and investments on the way down. Interest rates had not been too low, even if that is the popular view these days

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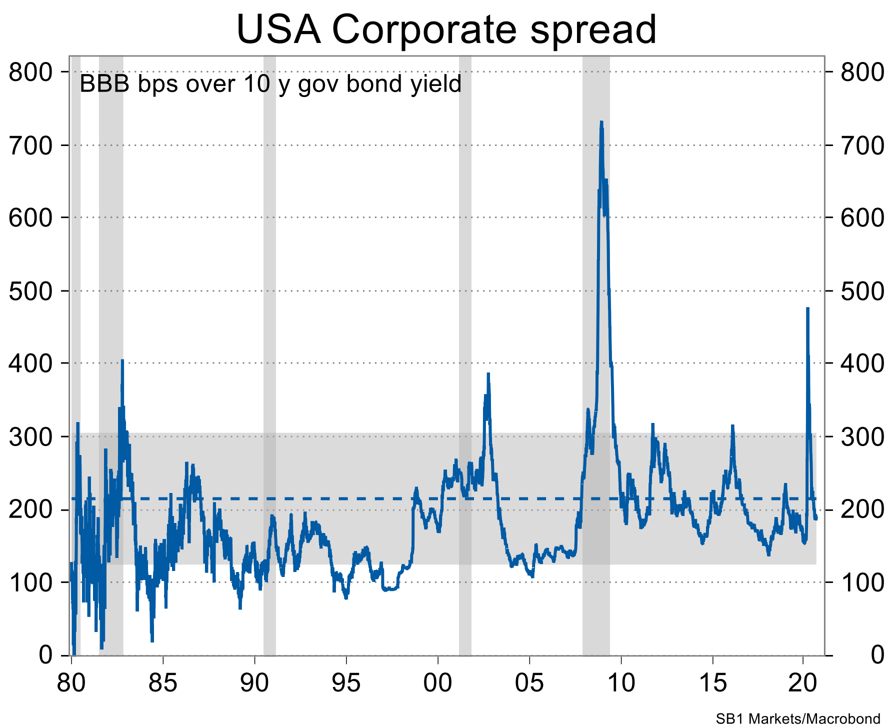
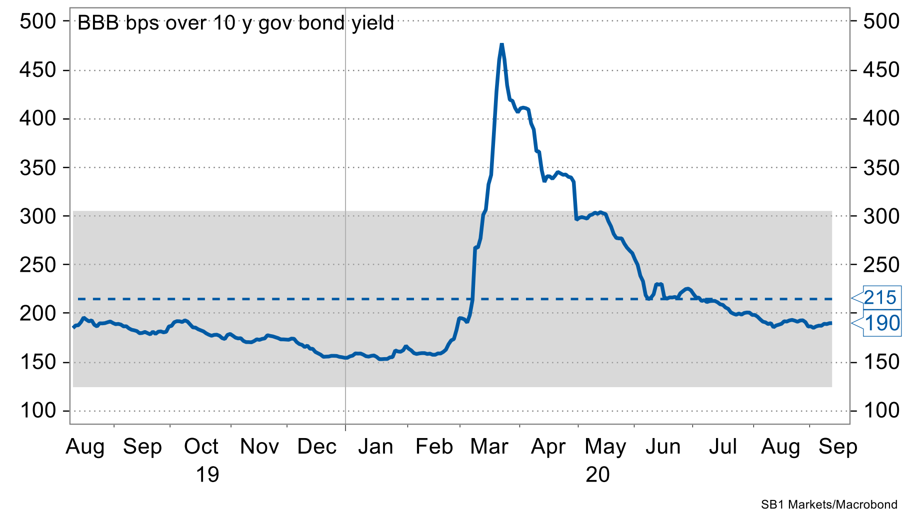
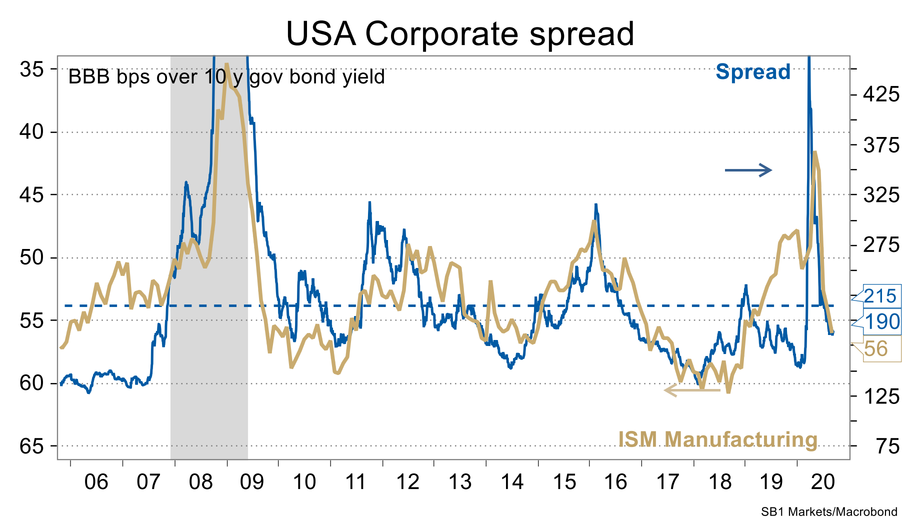
Credit spreads steady at a rather low level

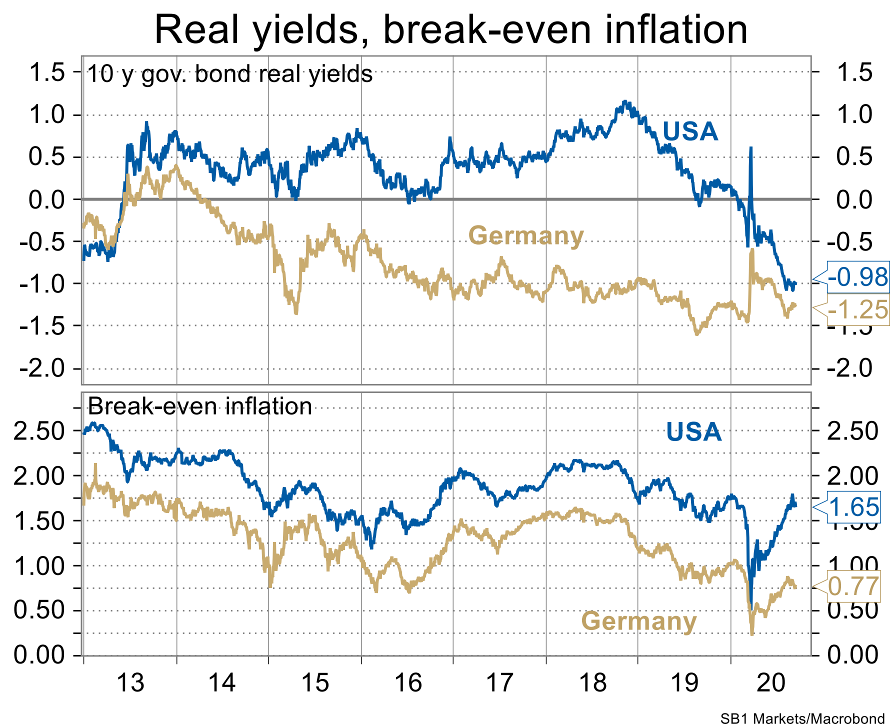


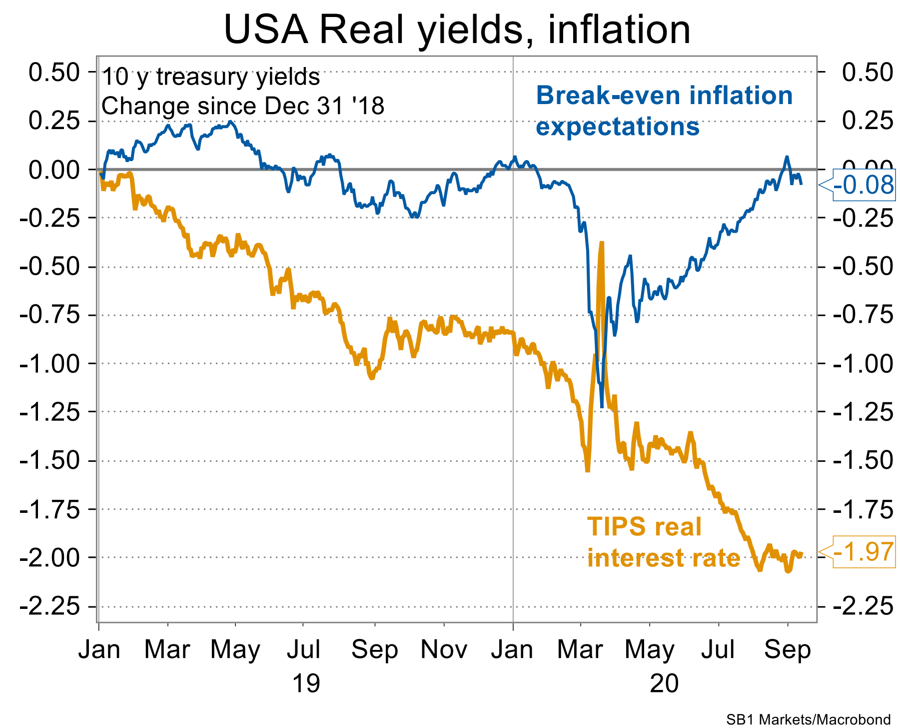




USA 10 y inflation expectations slightly down last week, has been trending up

Inflation expec. have been climbing since April and are not that low anymore, at 1.65%

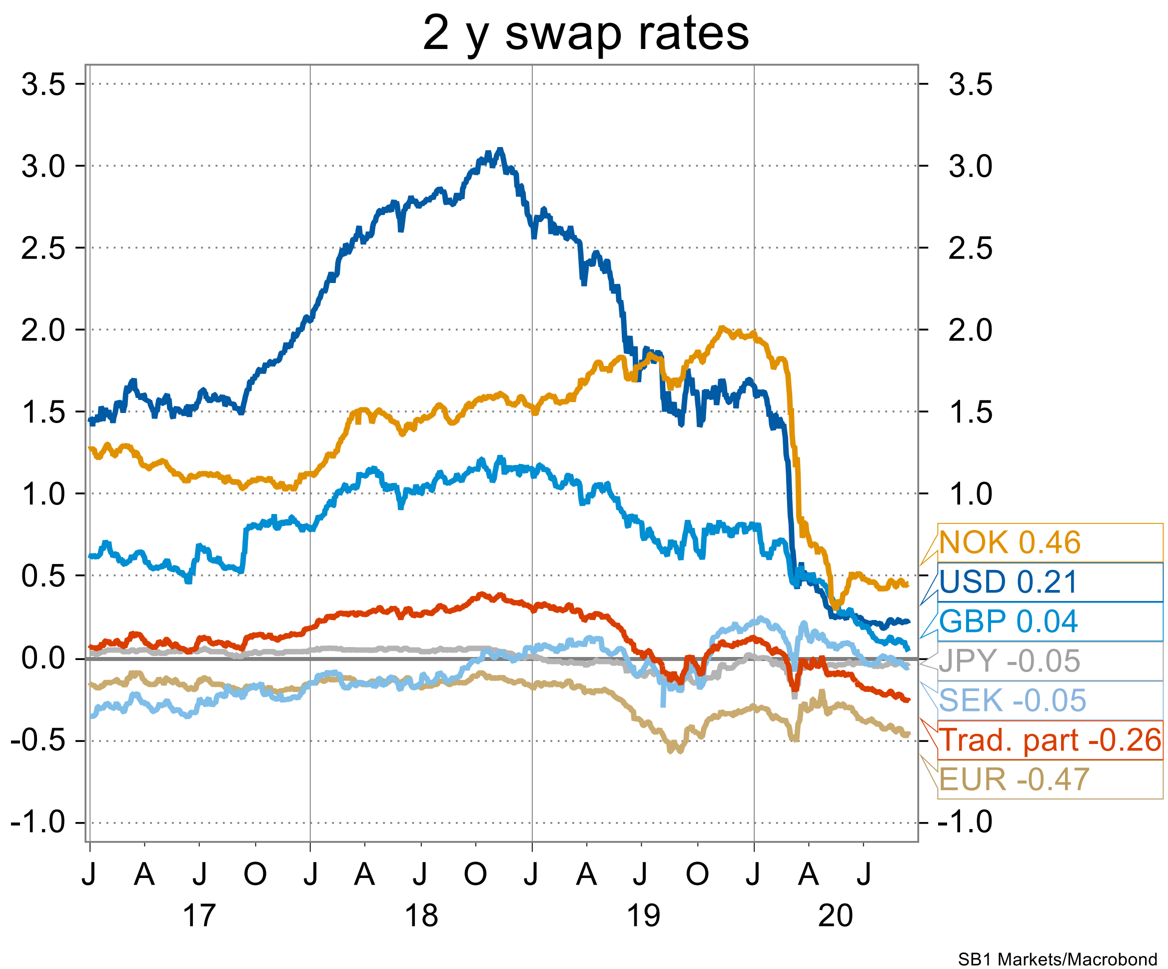


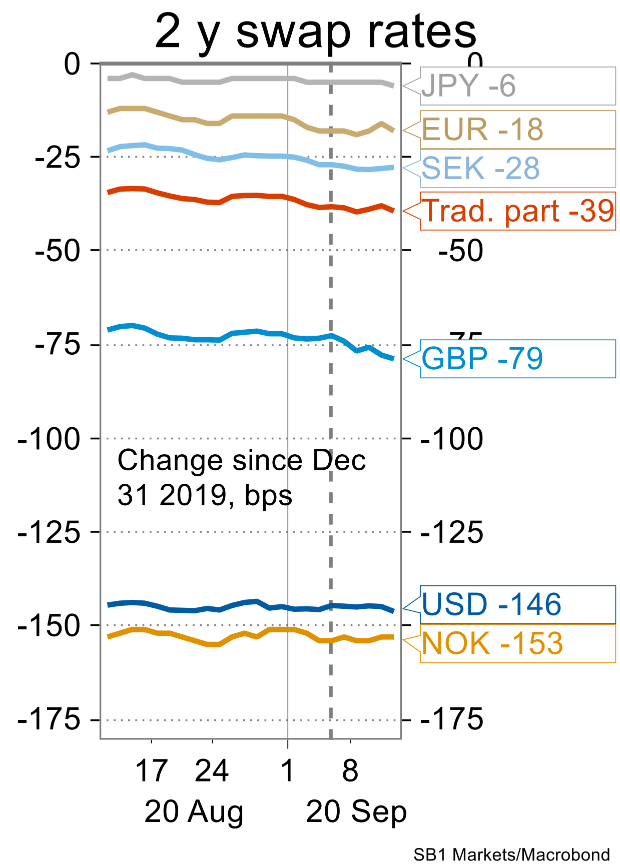


- The implied break even inflation rate has increased since April. Following Powell's announcement of the new Fed price level target strategy two weeks ago, inflation expectations were pushed further up, however, this lift has later been reversed. Last week, break even inflation inched down 5 bps, to 1.65% (in 10 years)
- The US real interest rate has more or less stabilized since early August, at a very low level, of course – flat last week
- The German real rate is at -1.25%, marginally up recent weeks. Inflation expectations slightly down, to 0.77%

2 y swap rates are still sliding down in EUR – NOK, USD rates steady

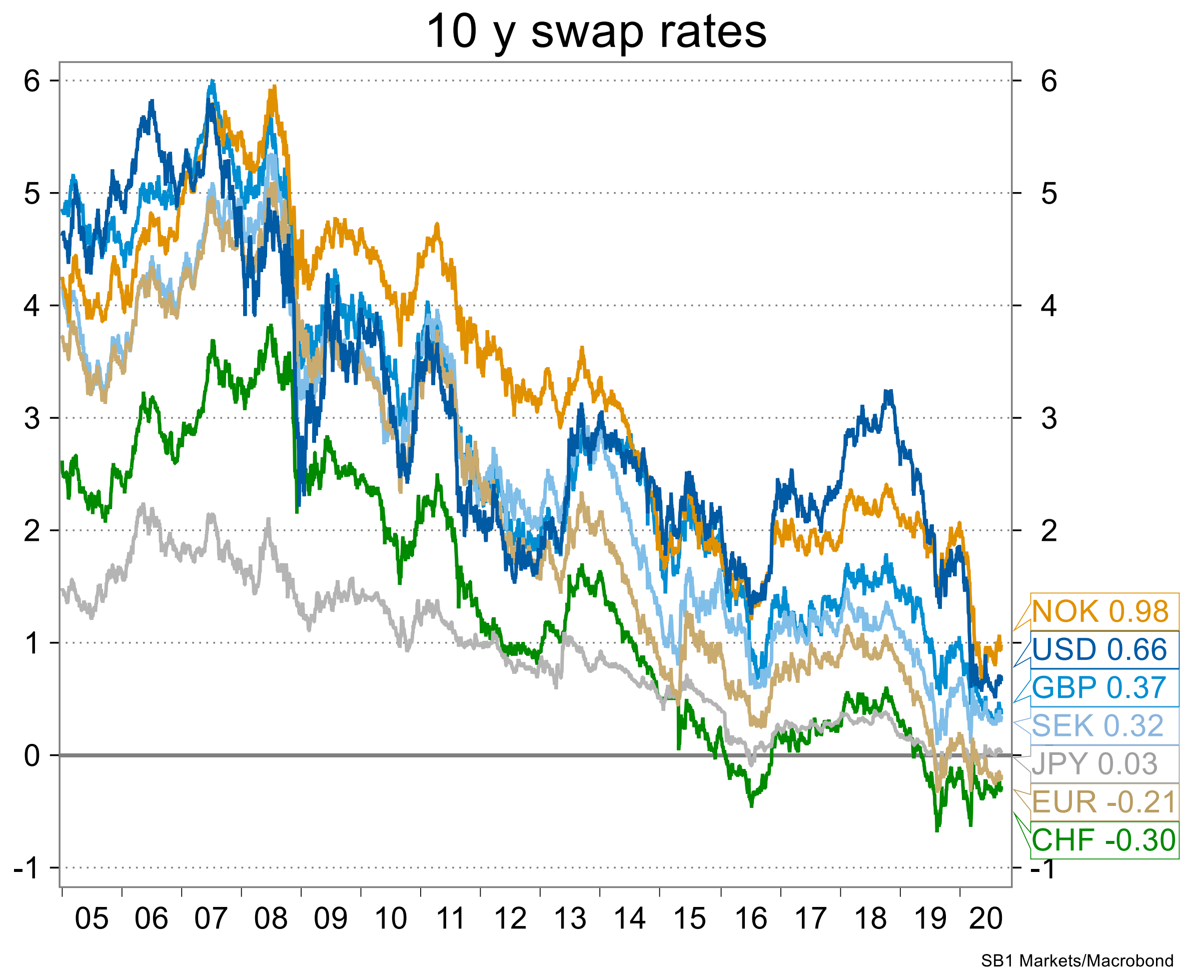
Last week, short rates inched up most places

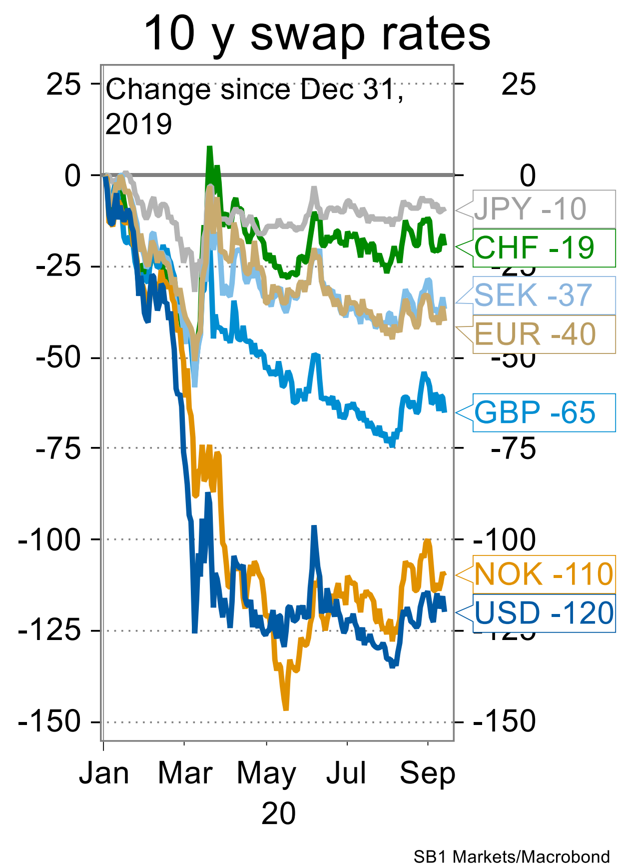




Long term swaps up from the August trough

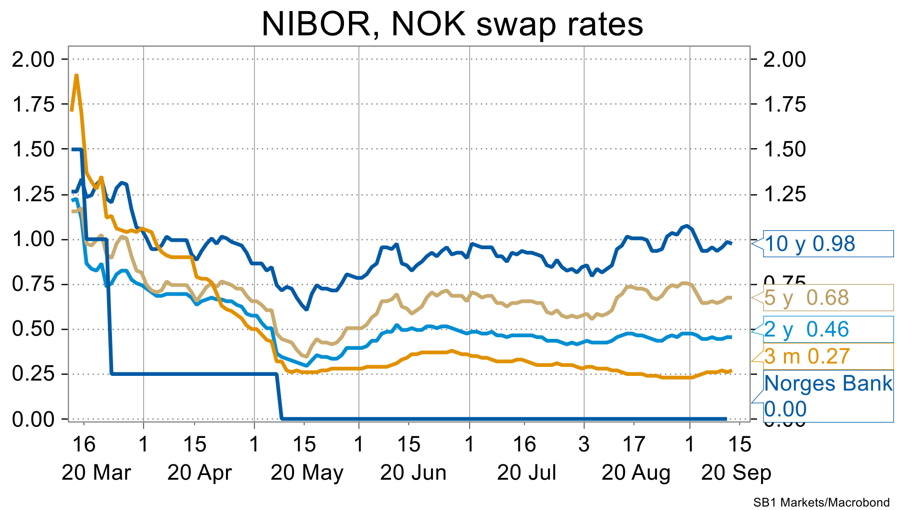
10 y swap rates are slowly moving upwards – but not further

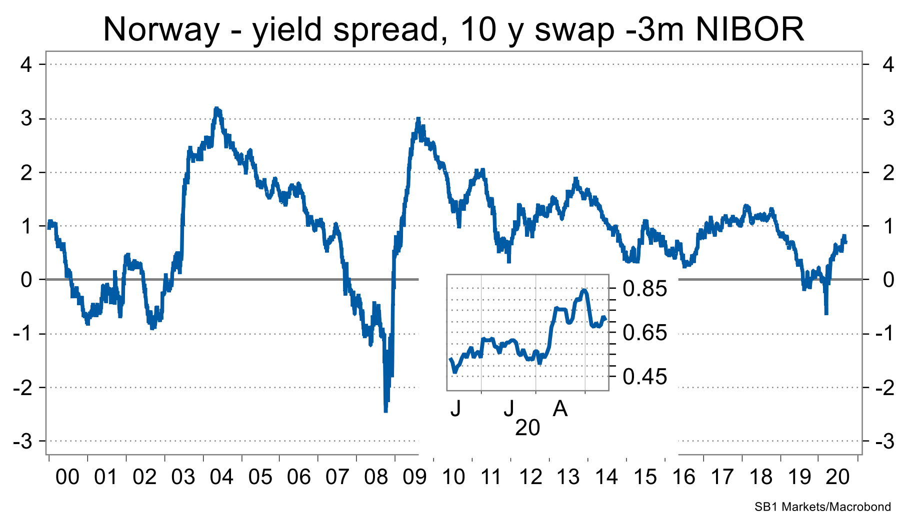


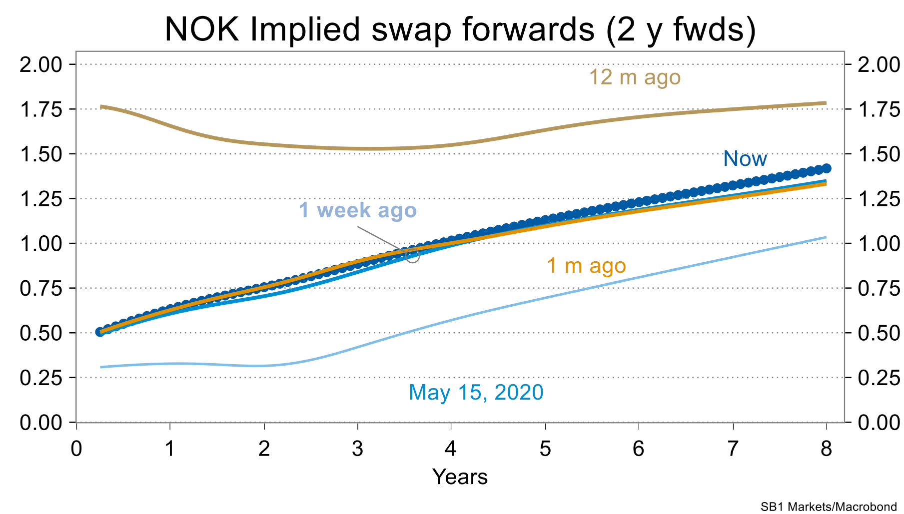


The long end of the NOK curve moving slowly upwards, 3m NIBOR flat at 0.27%

The yield spread has been rising since March, with a moderate retreat two weeks ago







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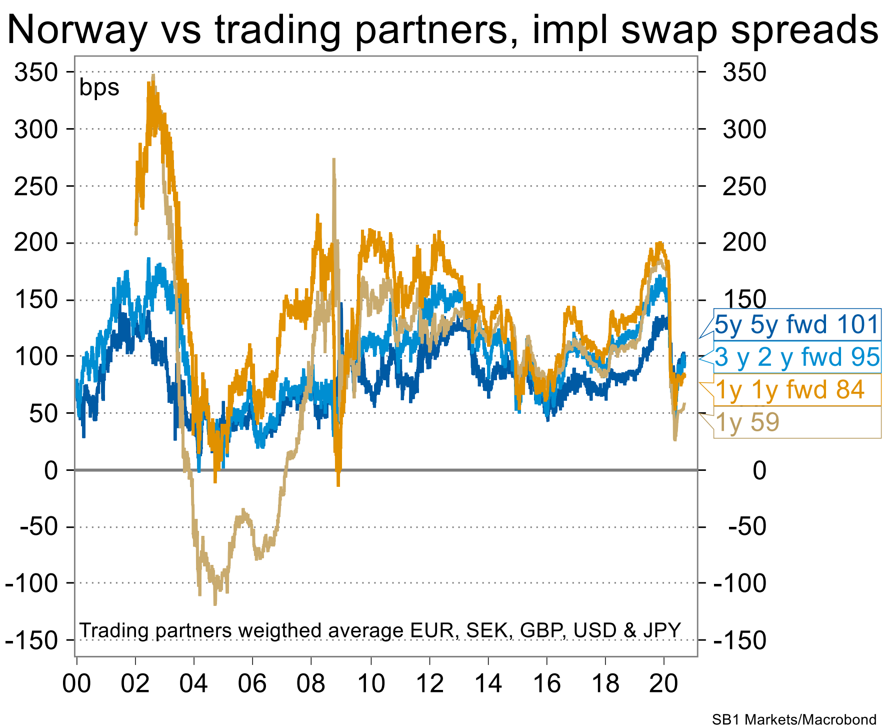
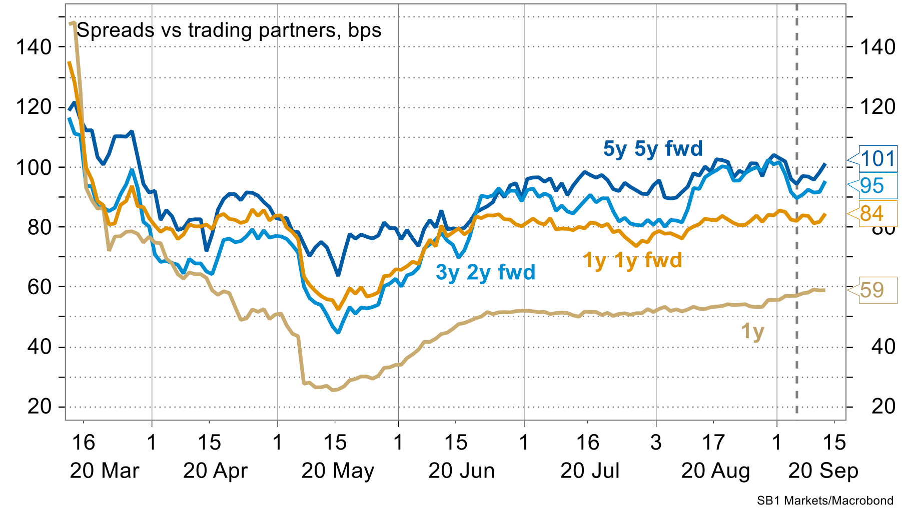
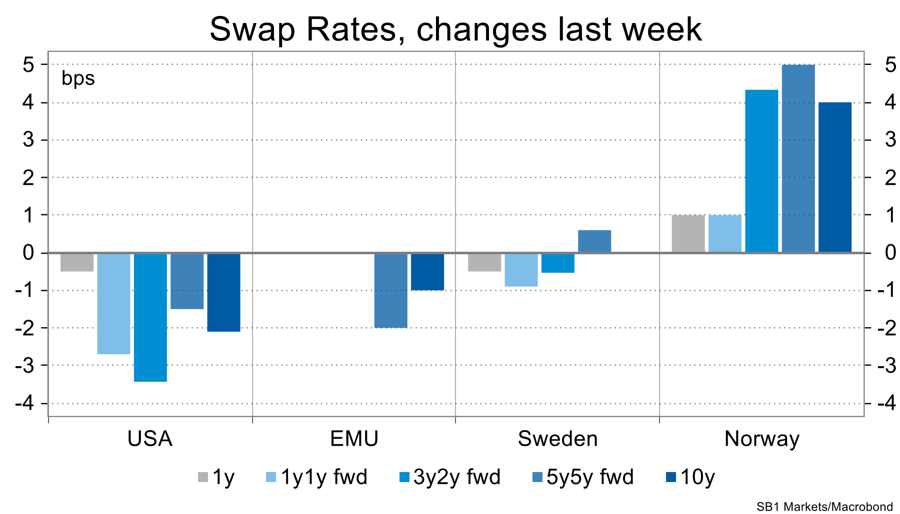
Swap spread vs trading partners slightly up last week – are trending flat/up

Spreads have flattened out in the long end since July, short end moving slowly upwards



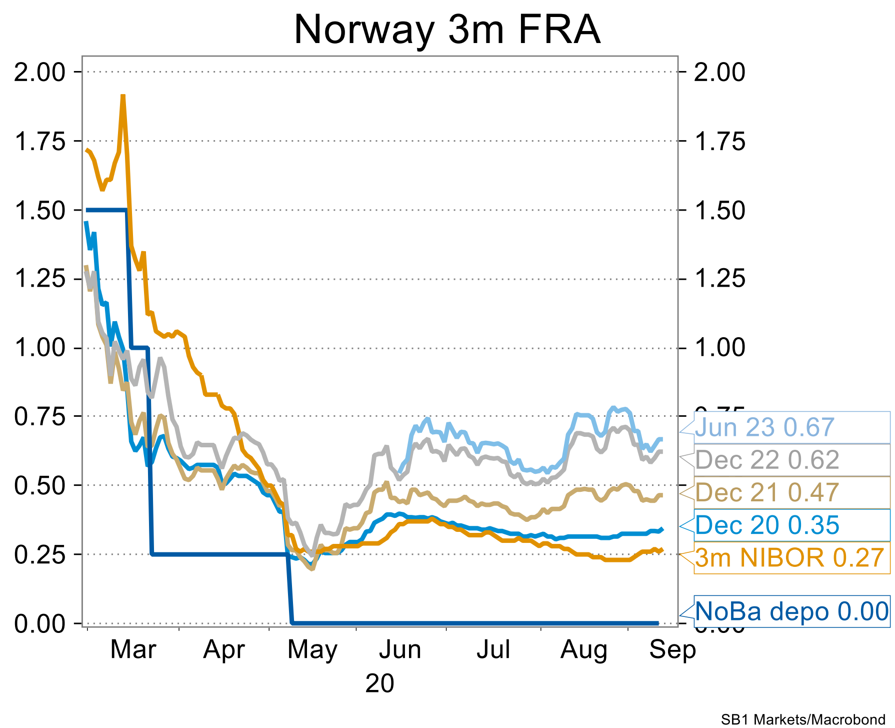




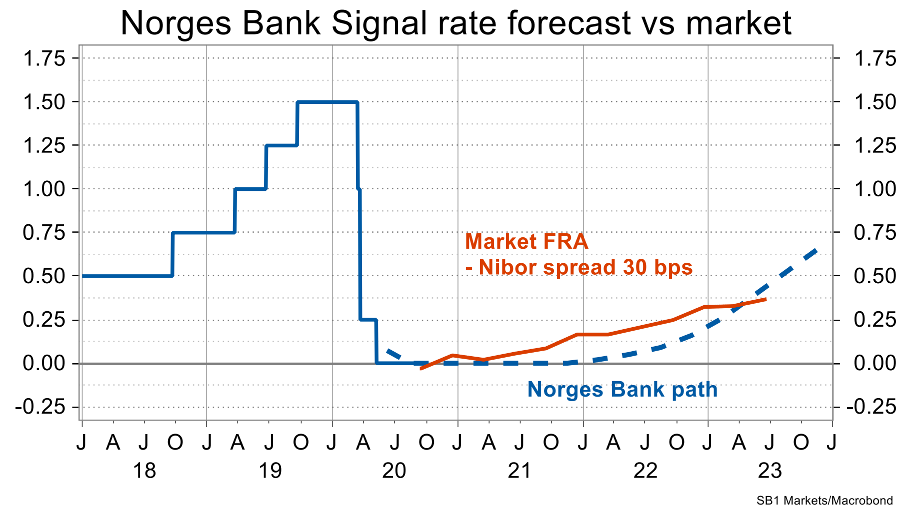
- Spreads vs trading partners have been trending wider since the May local trough but not further recent weeks (in average)
- We are still neutral vs. the spread

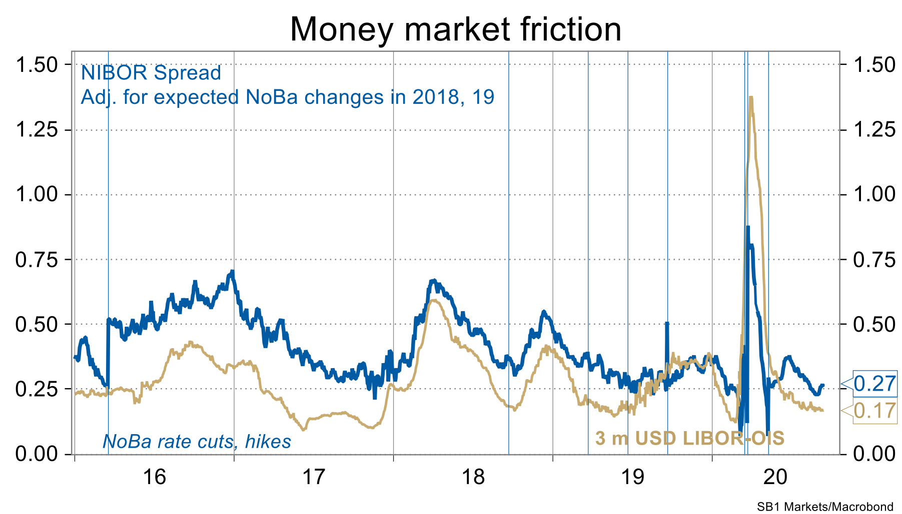
3m NIBOR stable 0.27%, FRAs slightly up again

Market pricing still signals a possible hike (by more than a 50% probability) in Q4 2021

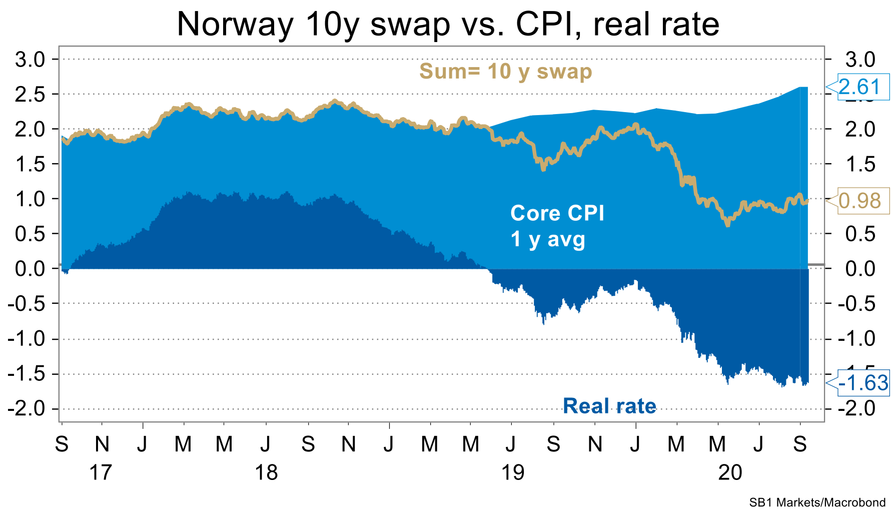


- We think it is completely unlikely that markets are pricing in any probability for an interest rate cut (or hike) the coming 3 months
- The first hike is probably priced in by Q4 2021 (with >50% prob). In June, NoBa said Q4 2022

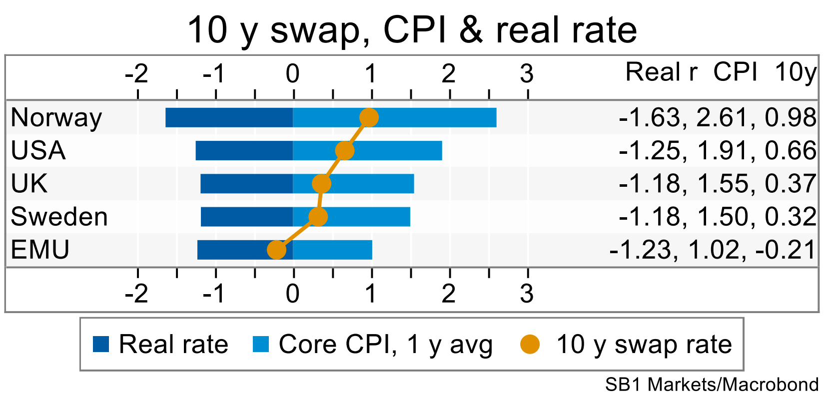




Negative (actual) real interest rates everywhere – NOK at the bottom



- NOK 10 y swap nominal rates are down more than 1 pp since January
- Real rates have fallen to -1.62%, based on actual core annual inflation (smoothed 12 m)
  - » All other measures of actual/expect inflation will yield results in the same ballpark, from -1% or lower)



NOK real rates among the lowest, inflation exp. at top

- Inflation among Norway and our main trading partners varies between 1 to 2.6% (here measured by actual annual core inflation, smoothed over 12 months). EMU at the bottom, Norway at the top
- Real rates are quite similar among our trading partners, in the range -1.1% (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*

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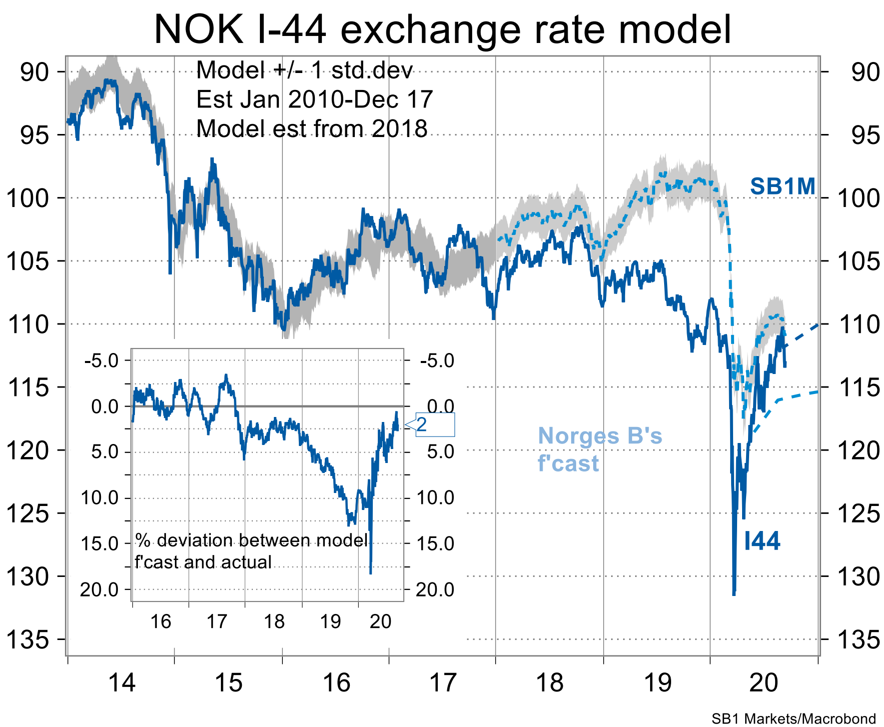
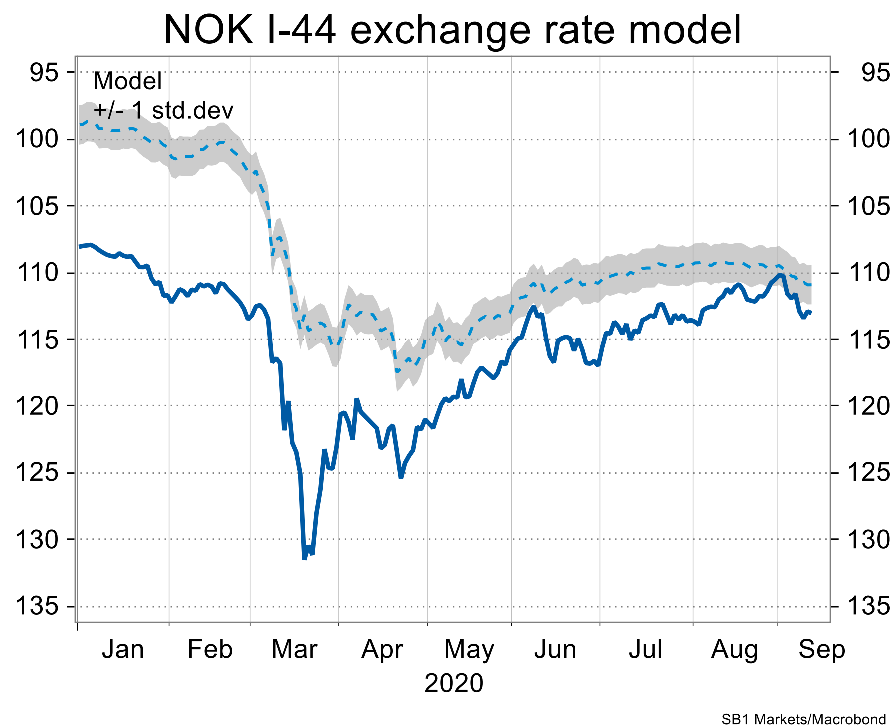
NOK down 0.6% last week, slightly less than oil and other fundamentals

The NOK has almost closed the gap to our traditional model, just 2% below

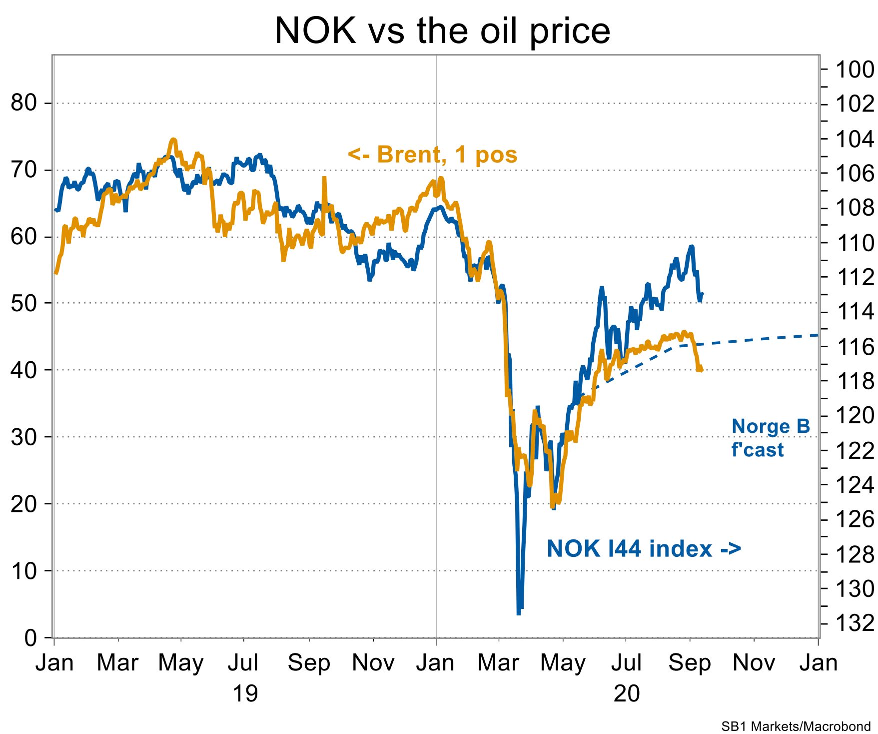


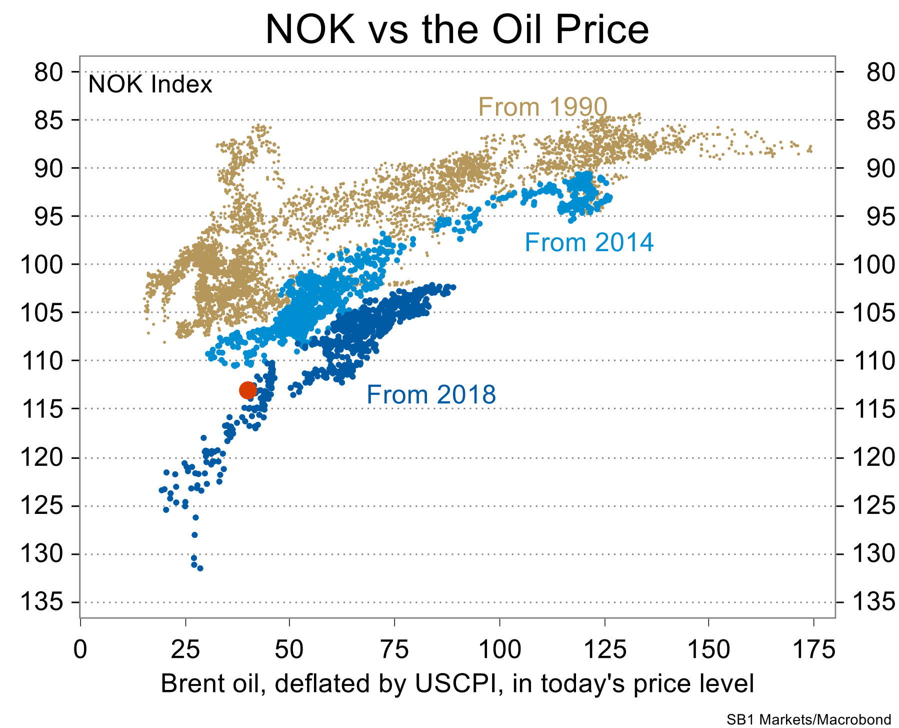


- We still have a NOK buy recommendation but it is not as strong as before!
- The NOK is ‘too strong’ vs a model based on oil company stock prices but weaker than the other supercycle currencies (AUD, CAD, SEK)

Now, the NOK has followed the oil price down

However, the NOK is still on the strong side vs. the oil price given the relationship since 2019

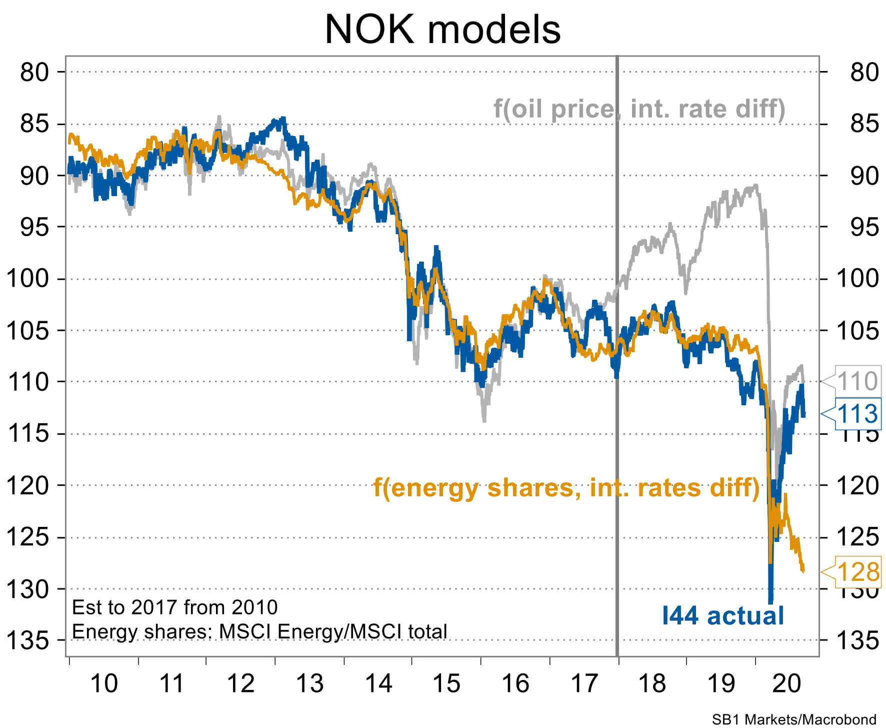


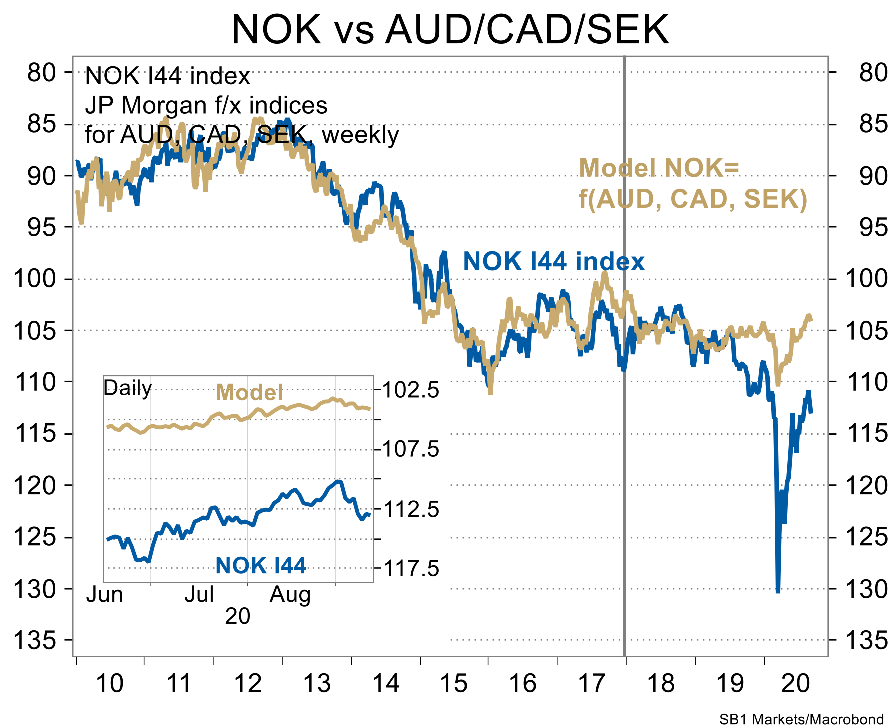


- On the other hand – the NOK is still somewhat weaker vs the oil price than the normal correlation until 2018

NOK has left the oil companies far behind but is still weak vs its peers

The NOK 12% ‘too strong’ vs energy shares, 9% ‘too weak’ vs a model based on AUD, CAD & SEK

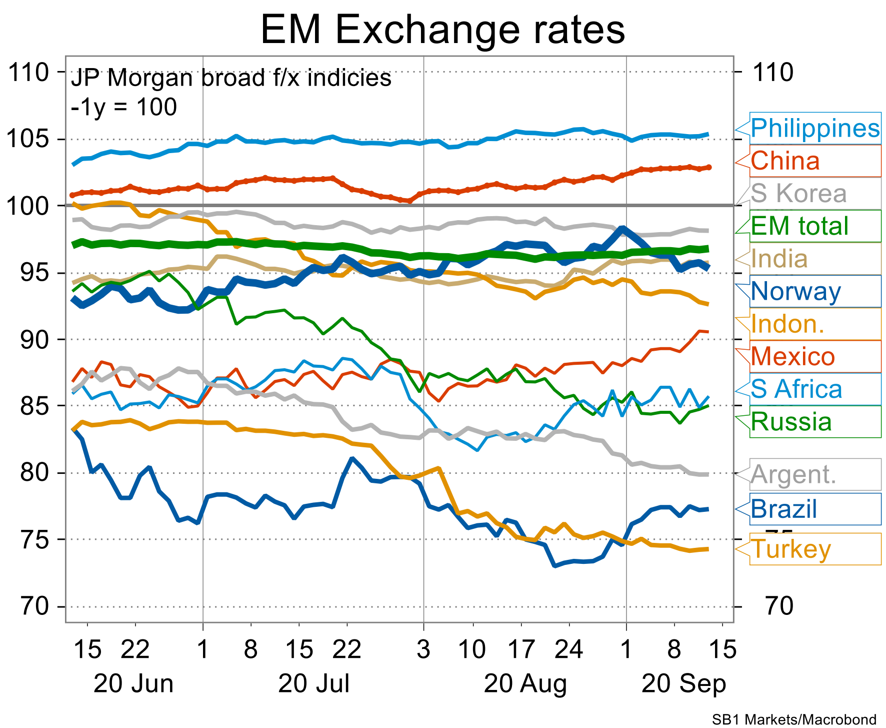


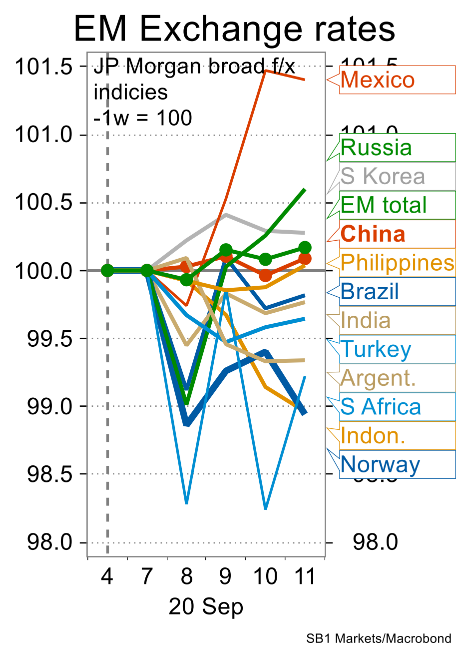


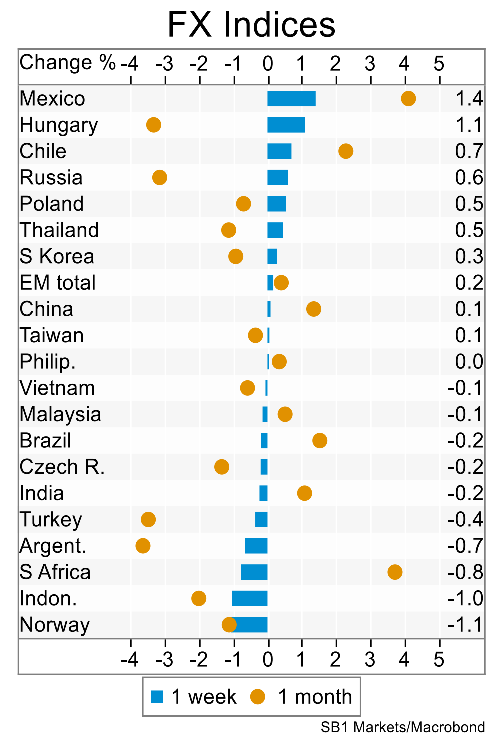
- On the alternative NOK models
  - Our NOK model based on pricing of oil companies (oil shares/total market) has ‘explained’ the NOK much better than our traditional model since 2017, as have our ‘super-cycle’ peers currency model [NOK=f(AUD, CAD, SEK), with just a marginal contribution from SEK]. The EM x CNY currency aggregate is also quite closely correlated to the NOK
  - Now, the NOK is 12% ‘too strong’ vs our oil equity price model (the gap has been shrinking for the past two weeks). 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. We think the AUD/CAD/SEK model is more relevant than the oil stock price model

EM currencies slightly up last week & month, Mexico the winner

The CNY has been strengthening since late July too







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