15 February 2021

Macro Weekly

Week 7/2021

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Highlights, corona update

The world around us

The Norwegian economy

Market charts & comments

Last week 1: The corona story

- **The no of new Covid-19 cases** is falling sharply almost everywhere, even where mutated viruses are dominating totally, also where the vaccination levels (or immunity due to many earlier infections) are low. **UK and Spain** may finally have benefited from the many deaths, they have gained parts of herd immunity. Anyway the 'R's are well below 1 in almost all countries, and still very low in Ireland. Here, the no. of cases are down more than 85% the past month. The no. of hospitalisations and deaths are now coming rapidly down too, also where the mutants have been ravaging
- **The economic and social costs** that have incurred in order to fight the mutated virus have been substantial, but not disastrous, like last spring. GDP have fallen some places, but just a small fraction of the 10% – 20% setback in March/April last year. This week's PMIs will yield new info on the impact on the economy
- Most likely the **mutated viruses** will soon dominate in many countries, it will happen over just a few weeks - but not instantly! And luckily, the mutated viruses arrive just as the vaccines are coming. Our simulations indicate that if we achieve a reasonable vaccine rollout, at more than 2% per week, the gradual increase in immunity due to vaccination will be sufficient to keep the overall no. of new cases well in check, even as the mutants becomes totally dominant during the coming 8 – 10 weeks. Social distancing may soon start to decrease, as it always has when the virus is on retreat. In UK and Ireland, that will probably happen in a matter of few weeks. Others have still less room for manoeuvre, they need to balance vaccinations vs. the more aggressive mutants (the R can still not stay above 1 for long). But even here, life might gradually start to normalise during Q2, as the rate of immunity is rapidly lifted
- There were good news on the **vaccine** front last week. Pfizer will ramp up its production substantially, by 200 mill doses to both EU and US. Half of these extra doses will be delivered in Q2. Astra/Zeneca will very likely also deliver far more than agreed upon so far, also from Q2. In addition, Johnson & Johnson, Curevac and others most likely will be able to deliver substantial quantities from Q2. It is not unlikely that the Norwegian population above 18 will be fully vaccinated before the summer – and that during Q2, 4%-6% of the population per week will get their first jab. If so, there is plenty of room for increased social contact during Q2, there is no point waiting until all are vaccinated
- As all countries, for good reasons, have chosen to **vaccinate those who are mostly at risk** for becoming seriously ill or die from Covid-19, the pressure at the hospitals will be substantially reduced, even if the no of infections is not reduced. That should increase the societies tolerance vs the virus, making 'gradual open up calls' even more attractive for the authorities
- **The 'only' remaining risk is** that the vaccines will not be able **to tackle new mutants** that has and most likely will arrive**. Pfizer** last week reported that their RNA-based vaccine is capable to handle current mutations (and can probably easily be complemented with new RNAs should new variants turn up) **while Astra/Zeneca's** may not be effective vs. the South African mutant (which is found most places now)

Last week 2: The economy

- **China** reported strong January **credit growth**, calming fears of an excessive credit tightening. Still, credit growth has peaked most likely because authorities priorities have tilted from stimulating the economy following the corona setback in Q1 to not exposing the economy to an ever rising credit/income level. Money markets have stabilised too
- **US CPI** rose less than assumed in January, but the annual rate will very likely accelerate sharply the coming months, due to the base effect from the decline in prices lasts spring. **Small businesses** are very pessimistic vs. their larger counterparts (measured by the ISMs, PMIs, and all other surveys). Seems like they are missing Trump. Before he left office, he signed the USD 600/persons checks, and the **budget deficit** ballooned again in Jan, federal expenditures are up more than 50% y/y. And Biden wants to spend even more. *In an economy where lack of demand cannot be the main problem*…
- **UK GDP** rose more than expected in December and in Q4, but 2020 was an *annus horribilis*, as GDP collapsed by 9.9%, almost at the bottom of the league among rich countries (just Spain below, due to its dependence on tourism)
- **The Norwegian economy** ended last year at a stronger note than expected, leaving the **Mainland GDP** Q4 GDP down just 1.3% vs. Q4 '19, and 1.2% higher than Norges Bank assumed in December. Q4 GDP is 2.3% above the 2020 average (carry over into 2021, 'for free'). In Dec, GDP rose by 1%, far above our well above consensus estimate. Personal services are still struggling (down 20%-40%) but not more in December, and others are doing OK (and fisheries, electricity lifted GDP sharply, following a drag on the downside in Nov). Export(x tourism) and housing have recovered, and Mainland business investments rose through H2, and oil investments flattened in Q4. Last year ML GDP fell by 3.1%, the largest yearly drop since 1944, but the economic loss due to the corona crisis will probably be far less than during the Norwegian banking crisis 1988 – 92, because the downturn then lasted much longer than we assume the corona crisis will do. **We expect ML GDP** growth to surpass 4% in 2021 (even 4.5% is within reach), following the 3.1% drop last year. Services will recover sharply as soon as we can 'open up', and that should gradually happen through Q2 and into Q3, barring really bad luck on the virus front. Household have build up significant cash reserves, and are still saving far more than normal. **Core CPI** fell less than expected in January, down 0.3 pp to 2.7% y/y. Electricity prices soared and the **headline CPI** shot up to 2.5% from 1.4% in one go!

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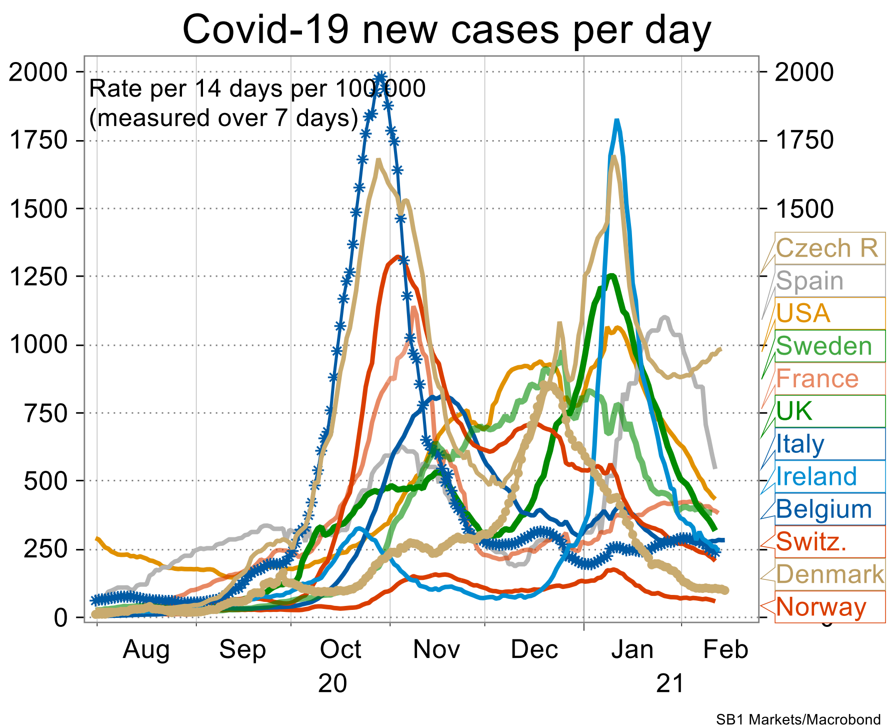
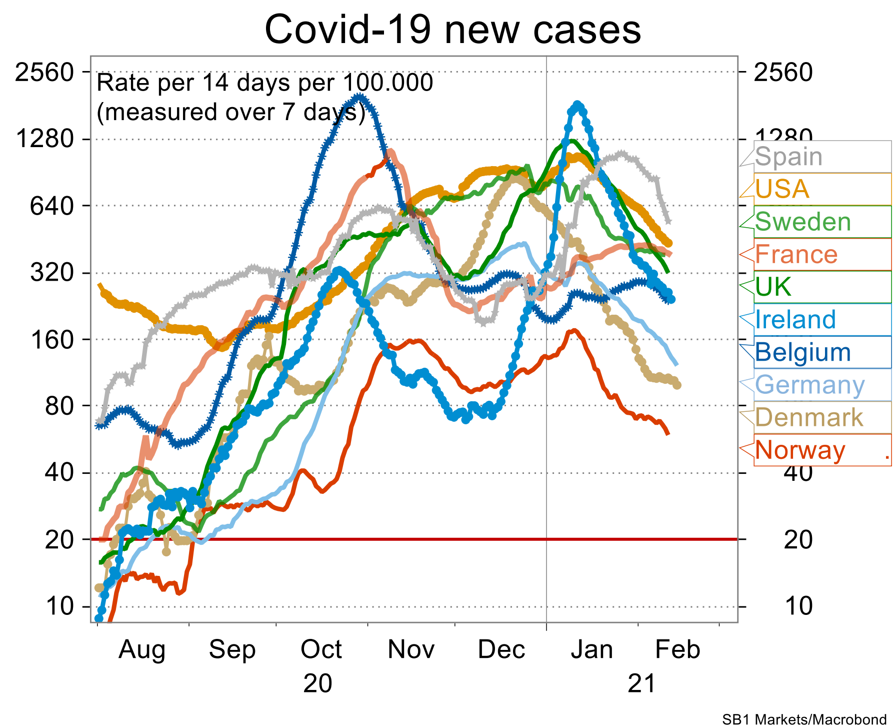
Still mostly good corona news, even where the mutants dominates

The 'R's are below 1 almost everywhere, even in the UK, Ireland, Spain and Portugal, with mutants





- The virus cycles are dramatic, and normally very short. Most countries are reporting fewer cases – and no country with a high prevalence is reporting more cases
- The no. of new cases is falling in Norway too, and faster again last week – and the no of newly infected is low. The mutated virus has arrived, local restrictions very imposed – and some already relaxex
- Even France and Belgium turned south last week

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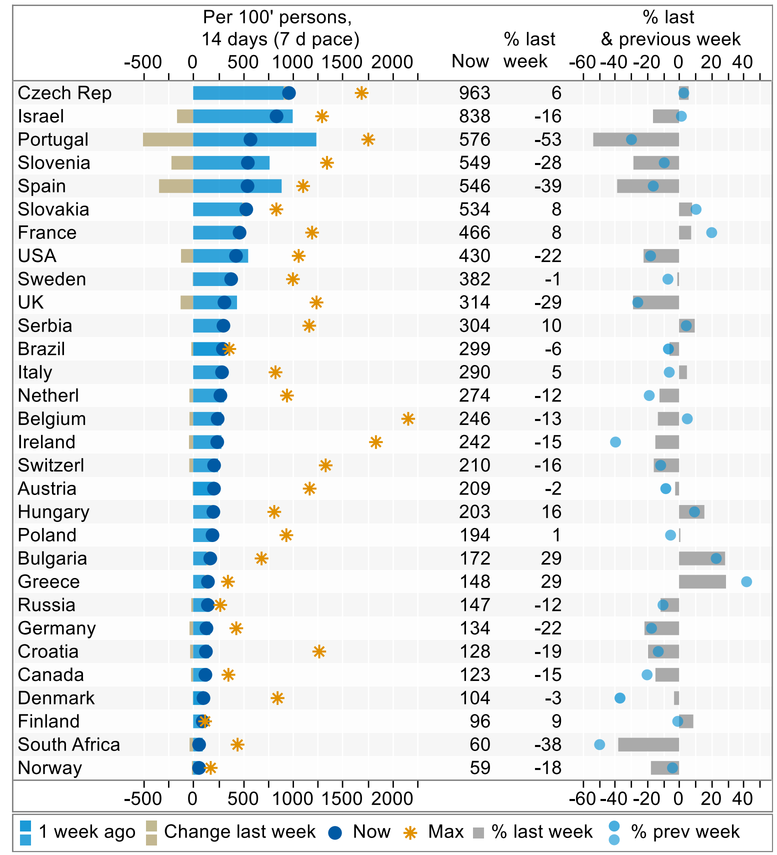
Positive corona news

Cases, hospitialisation & deaths down, even where mutated viruses dominate

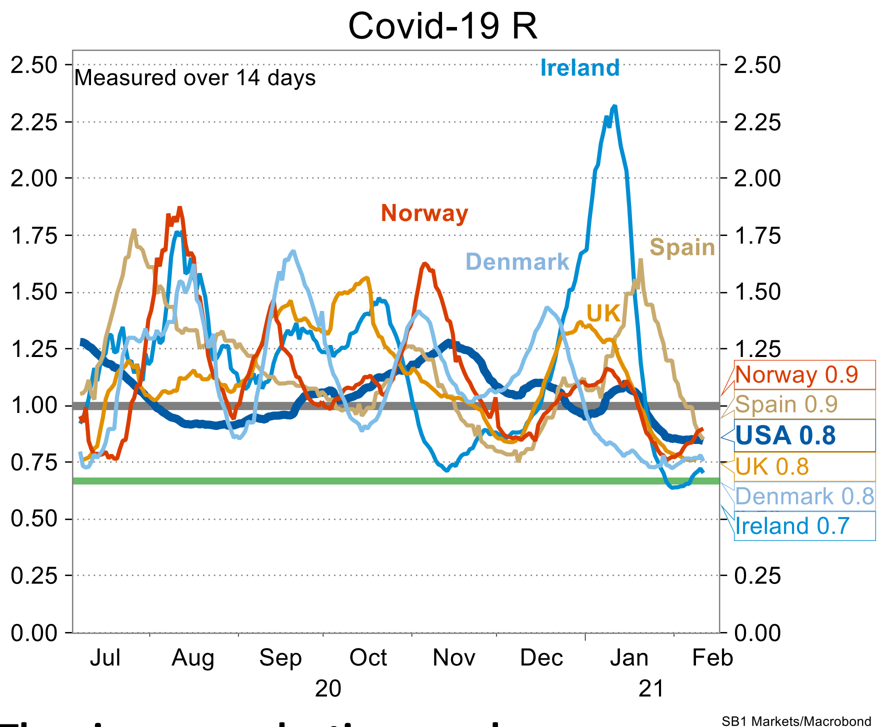
- **Almost all countries are reporting fewer new Covid-19 cases.**
  - » The no. of cases is still falling sharply in **UK**, where the mutated virus is dominant. The same goes for **Ireland**, and the no. of cases have fallen sharply in **Portugal & Spain** too, where mutated viruses probably were to blame for the rapid increase until 3 weeks ago. This demonstrated that even mutated viruses can be controlled, even before vaccines have arrived (they have probably contributed in the UK) – they have all pushed their 'R's down far down below 1, with mutants onboard
  - » **France, Belgium and the Czech Rep** are borderline cases, but just the Czechs have a high number of new cases (for the 3rd time in 5 months)
- The no. of **hospitalised patients** and **deaths** are down everywhere too
- **Mutated, and more infectious viruses** are taking market shares everywhere, and will be dominant most places before the spring, we assume
- However – as <u>the share of vaccinated persons increases week by week, most countries should have a reasonable chance to get the total no of new cases further down</u>, and at the same time even gradually reduce social distancing (lifting some restrictions) the coming moths. *See more on the next pages*
- Last week **Pfizer** stated that their vaccines were efficient vs. all mutated viruses so far reported. There is still doubt whether Astra/Zeneca's can protect against the South African variant
- Mostly positive **vaccine production** news last week. Several companies announced higher substantially production targets and countries that they were promised more vaccines – Norway incl.
- <u>We assume</u> production will be easily ramped up over the coming months and at least quarters, as bottlenecks are cleared. However, the world badly needs these vaccines now

COVID-19, New Cases



SB1 Markets/Macrobond

Covid-19: Back to the 'R'



The virus reproduction number:

$R_e = \beta_e\ C_e\ D_e\ X$

β the share of people you infect when you meet them

C no of contacts per day (measured vs. the β)

D days you are infectious

X share not immune (starts at 1, down to 0 when all have been infected or have been vaccinated).

Mutated corona viruses probably require a 75% immunity rate, if β & C are as 'before corona' (no masks, not mild distancing ect – very unlikely! <u>Will a 60% immunity rate be sufficient to really 'open up?'</u>

The no. of cases are falling rapidly most places

- The 'R' is well below 1 almost everywhere – though it does not normally last for too long, as behaviour adjusts
- The R is at 0.7 – 0.8 in UK & Ireland, even with the mutated viruses dominating. Soon, restrictions can be relaxed to bring the R closer to 1(when the level of contagion is low) even before taking the impact of vaccinations into account

However, what if mutated viruses spread to all countries?

- If the mutated viruses are 1.5 x as infectious as the original virus, for a given social distancing, R^{mut}= 1,5 x R^{org} then β^{mut} is 1.5 x larger than β^{ord}
- If the mutated virus took over the market, social distancing (C in the formula) had to be reduced by 33% in order to keep the R constant - which UK and Ireland were forced to do (and then further down to 0.7 – 0.8 to get the no. of cases down 80% – 90% over

Luckily

1) The mutant still have a small market share most places
2) The Rs are not at 1, they are already below
3) The vaccines are arriving. Even a 3% per week vaccinating rate reduces the R by 3% per week (if they work), and accelerating

The vaccines very likely able to reduce the R faster than the mutated virus will increase the R.
<u>The 'only' remaining risk: Vaccines are not effective!</u>

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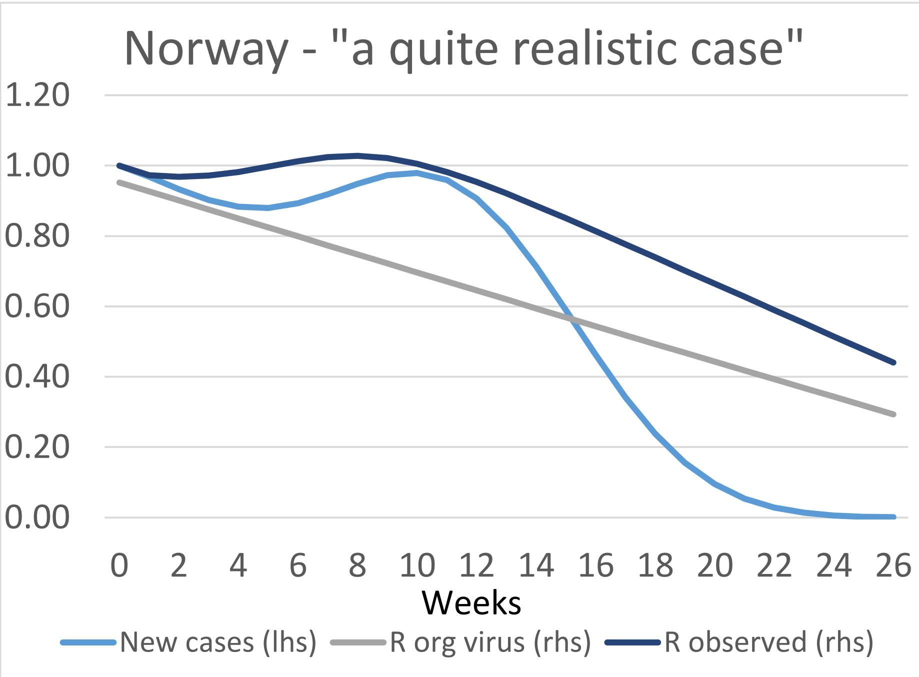
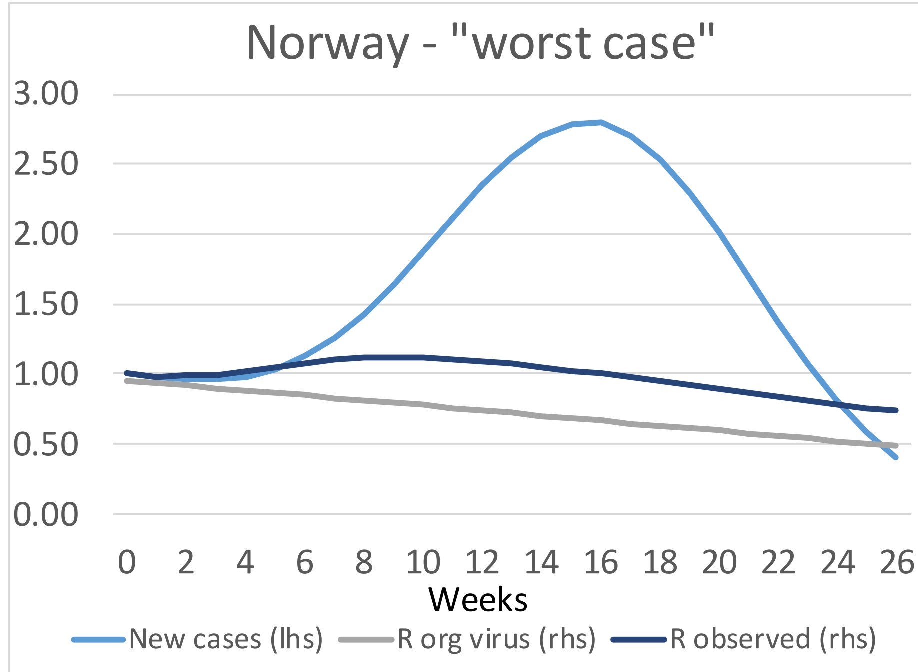
A 3%-4% weekly vaccination rate is much more than even mutants can stand

A 2% rate is a borderline case, if not the initial R is somewhat below 1 (which it is today)

If $R^{mut} = 1.5 \times R^{org,}$ the mutated virus yields an R below 1, after 3% 1st time vaccination per week in 10 weeks





Model assumptions:
R = 1 now (it is 0.9)
$R^{mut} = 1.5 \times R^{org}$
10% of the infections now are due to a mutated virus
3% vaccination rate per week, first dose
85% vaccine efficiency
5% are immune now, due to previous infection, vaccines in Jan/Feb
New cases are normalised to 1 now (the real number is 60 pr 14 days pr 100')

Model assumptions:
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***2%* vaccination rate per week,** first dose
85% vaccine efficiency
5% are immune now, due to previous infection, vaccines in Jan/Feb
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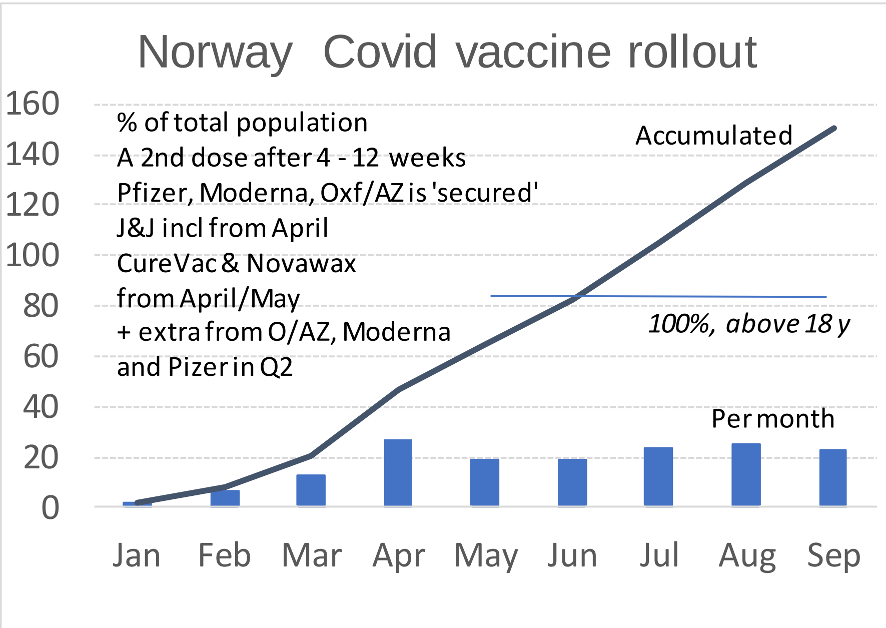
Pfizer and Astra/Zeneca: More doses are on the way. Will we get to 3% - 4%/w?

EU/Norway will receive more vaccines through Q2 – adult population vaccinated before the summer?



The first shot per week % of popul	
Jan	0
Feb	1
Mar	3
Apr	6
May	4
Jun	4
Jul	5
Aug	6
Sep	5

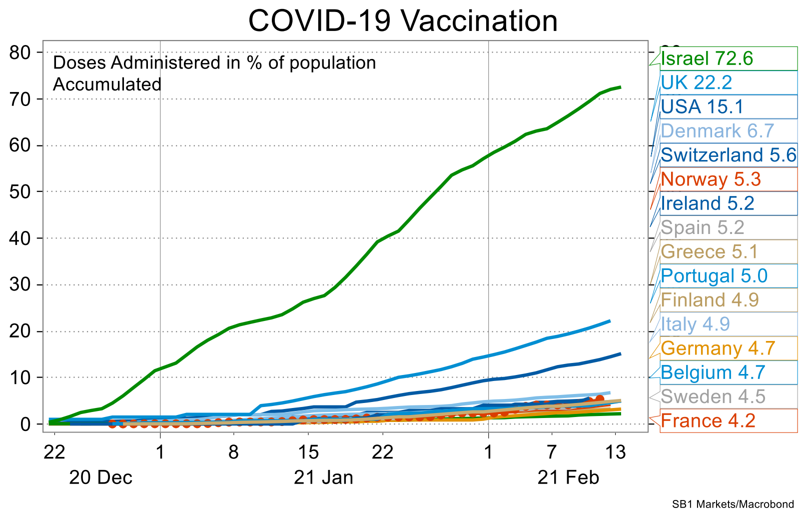
- Norway may reach a pace of vaccination at 3% of the population per week in March (adjusted for offset for the 2nd dose) – and substantially more during Q2

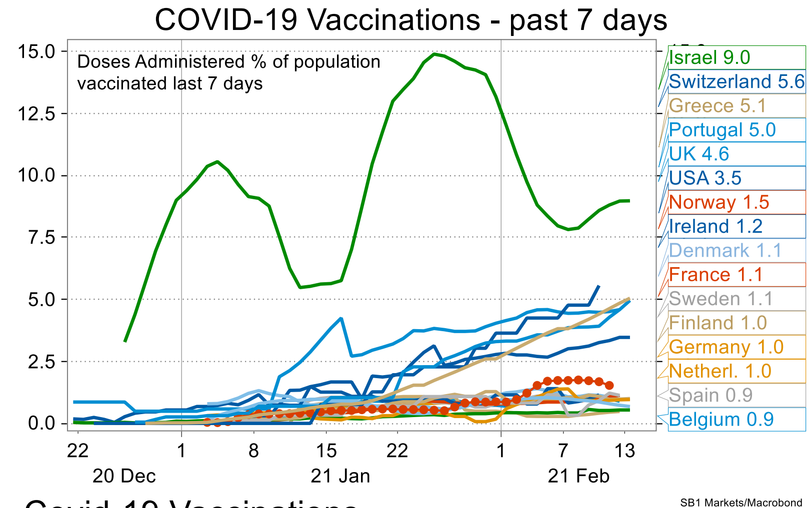
- There is still substantial uncertainty vs. the availability of vaccines, both concerning global production volumes and the share EU/Norway will receive
- Last week Pfizer announced a substantial increase in delivery of doses to the US and EU, some 200 mill to each – Norway will receive some 2 mill extra, of which almost the half during Q2.
- Astra/Zeneca will increase its deliveries to Europe by 50% (twice as much as we estimated one week ago)
- There are several vaccines underway but we have included Johnson & Johnson's, which probably will be authorised late Q1
- Some vaccines from CureVac & Novawax are included (EU has agreements with both of them)
- Moderna may be able to increase its production capacity substantially
- Norway may reach 100% coverage of the adult population by the end of Q2
- **However, immunity in the population will be lifted substantially before that**, reducing the 'R' proportionally by (1-immunity rate) for a given behaviour/social distancing. The impact is substantial, *check the next page*
- Old/sick or persons in the risk groups are vaccinated by early Q2 at the latest– no doubt **reducing the hospitalisation & death rates substantially** (like we now see in Israel) making a higher infection level acceptable

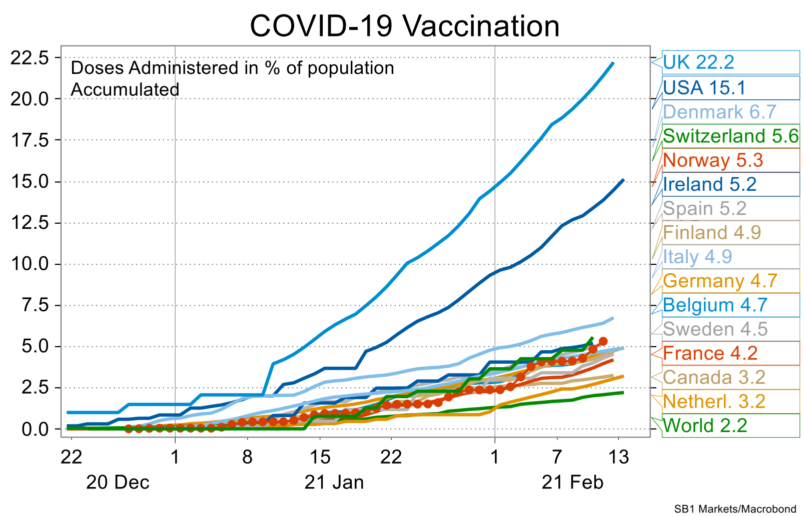
Data from FHI, VG, international media

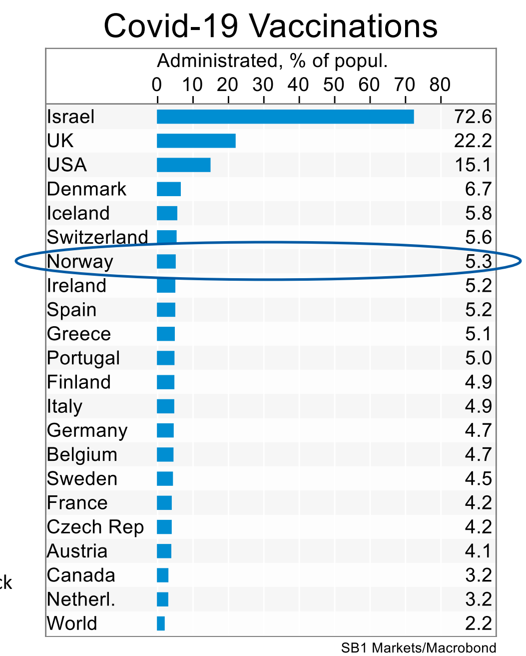
Vaccinations: UK, US in the lead (x Israel). Norway has moved upward on the list

The no. of doses equals just 1% – 1.5% of the population per week in most of Europe





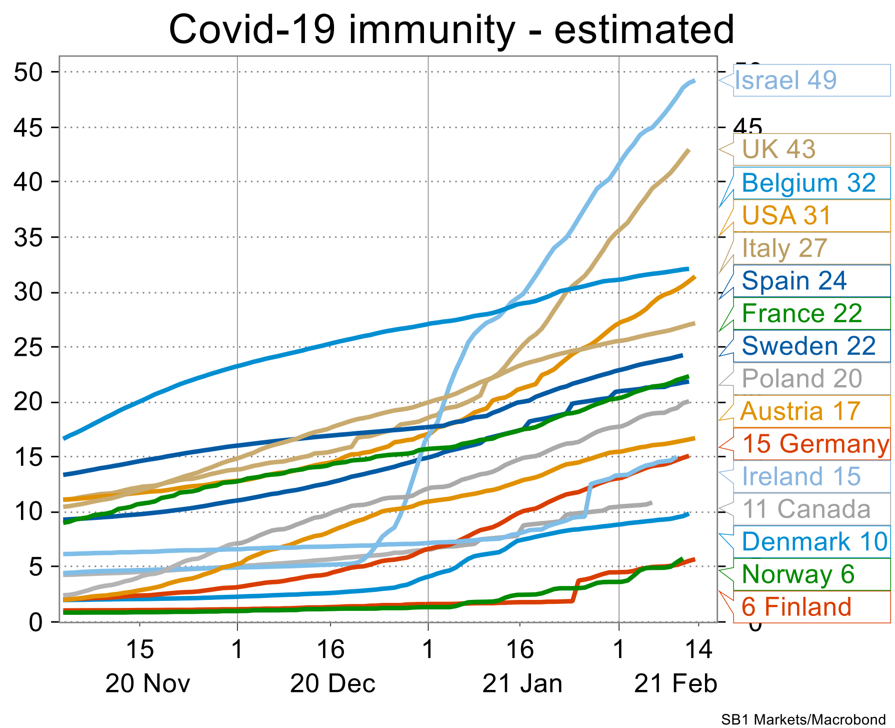


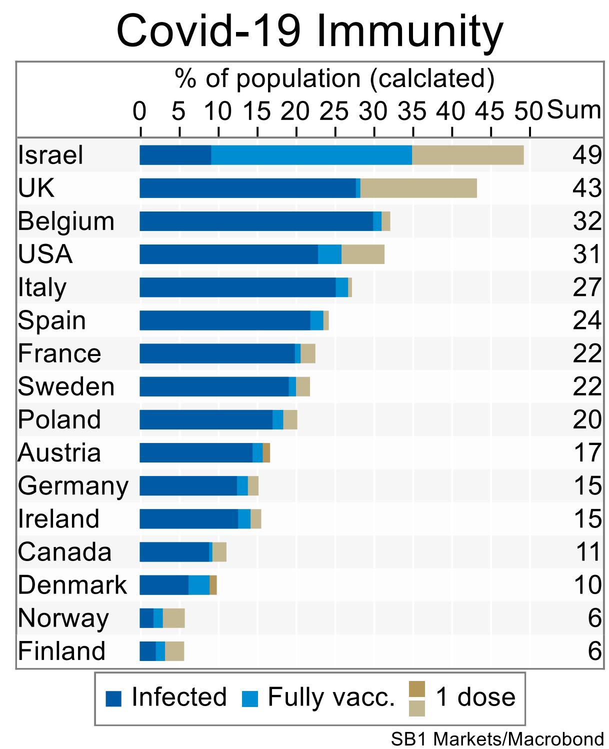


- The bottleneck in EU/Norway is the supply of doses. Oxford/AstraZeneca and Johnson & Johnson will eventually provide much larger quantities, as will Pfizer from Q2
- We doubt distribution will become an impossible challenge, as most countries are used to distribute large quantities of vaccines
  - Complicated priority systems create problems now, but hopefully not for too long

At this page, just **the no of doses are shown**, not how large part of the population that is vaccinated – check next page! Sources: Our World in Data/Macrobond.

How to reach herd immunity? Through infections or vaccinations?





- It may take at least 2 weeks before the vaccine works in the body, after receiving the first dose. If so, Israel should have reached some 35% immunity rate by now, and 45% in 2 weeks time, assuming the first dose create immunity
- UK, Belgium, USA and Italy may have reached an immunity rate through infections alone, Sweden 20%. UK has vaccinated a significant share of the population too

We calculate the infected rate by assuming a 0.5% infection fatality rate. We assume those who have been infected are vaccinated in line with others

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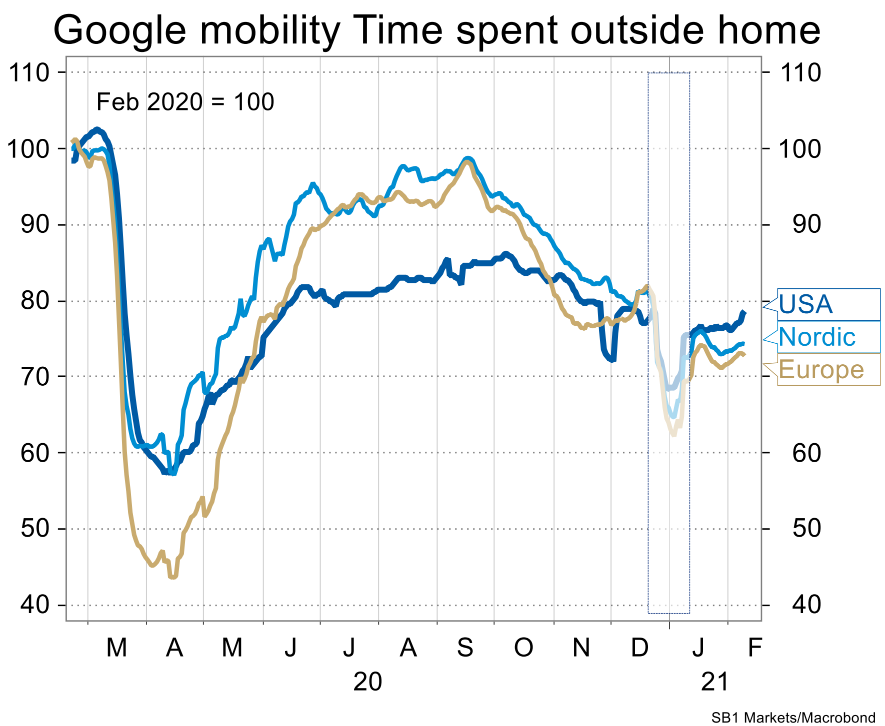
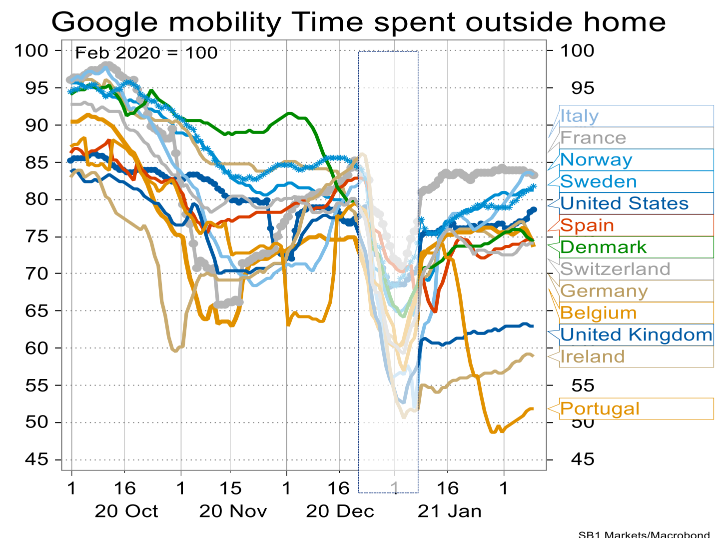
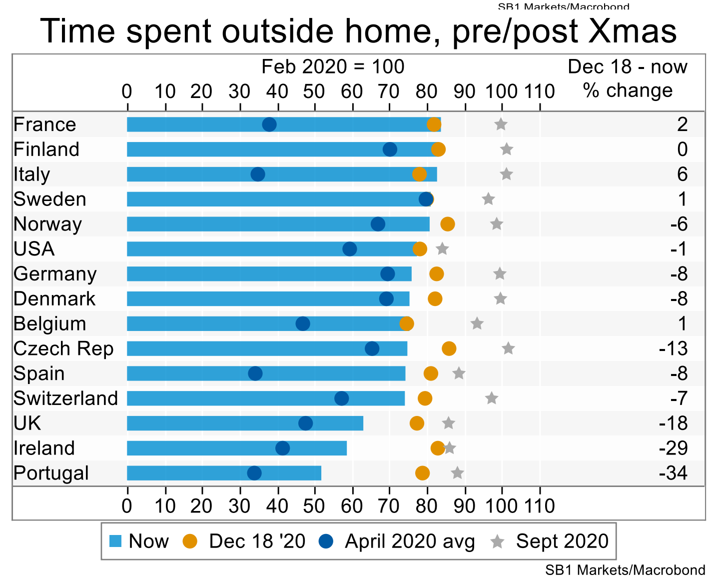
Mobility is trending upwards almost everywhere – as the 'R' has fallen below 1

Spain has turned down – and the no. of cases flattened



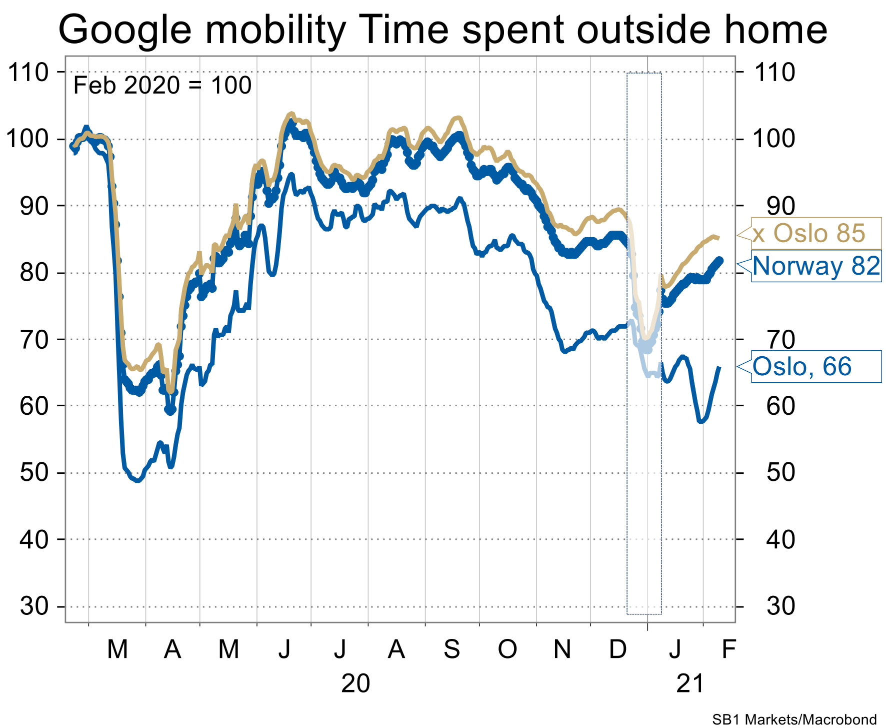




- Several countries are on par with the pre-Xmas level, France is even above (and the no. of cases is on the way up too)
- **In the UK**, time spent outside home is down 18% (not percentage points) – and mobility is down almost 40% vs. a 'normal' level (Feb 2020)
- **In Ireland**, -29% vs pre Xmas, and the level still now down more than 40% vs. 'normal'
- Germany, Denmark & Norway is down 6% – 8% vs the pre-Xmas level, and some economic costs will incur

Oslo back to 'normal' again?

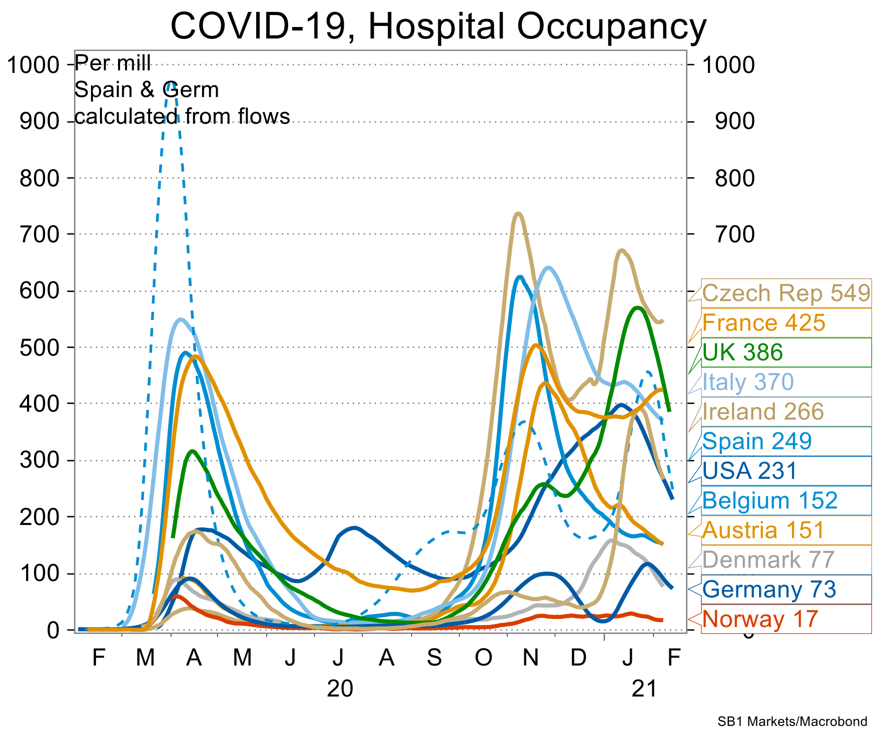
Well, far less time is spent outside home, not less than in January, before the recent 'lockdown'

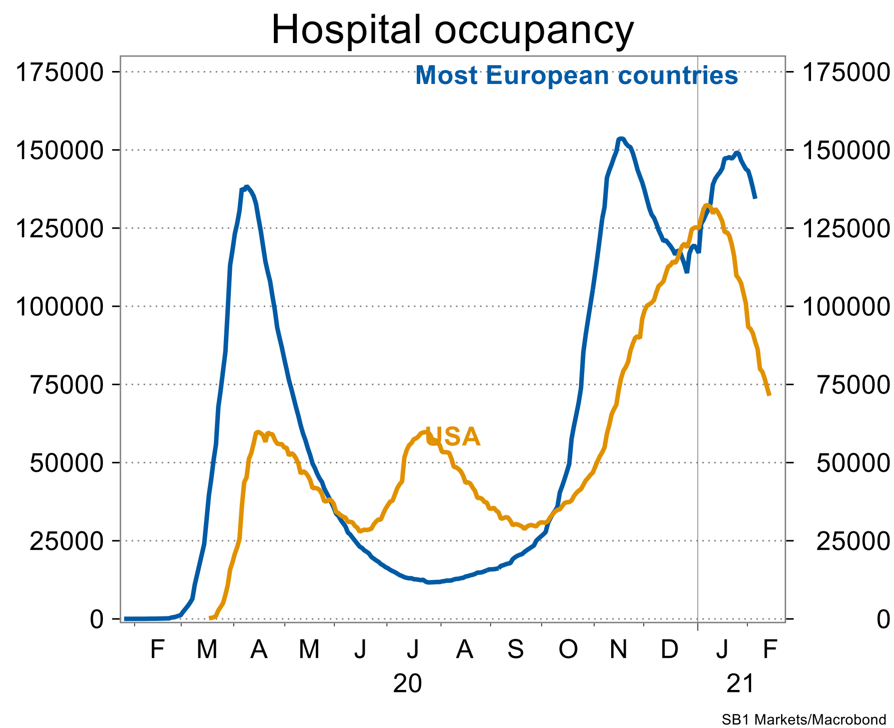


- Overall mobility is increasing again – but the no. of Covid cases is still on the way down

Hospitalisations on the way down almost everywhere

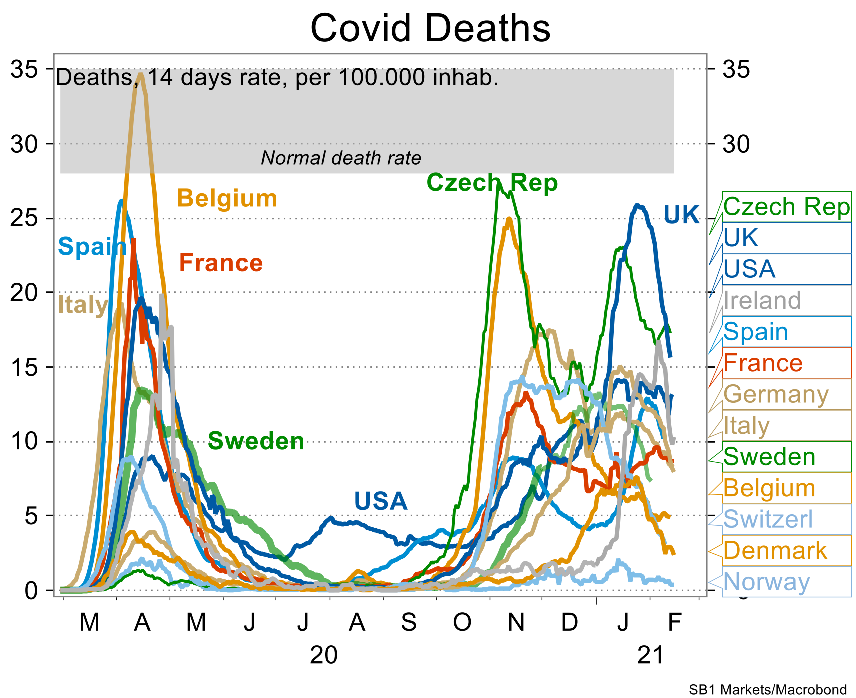
France is the exception

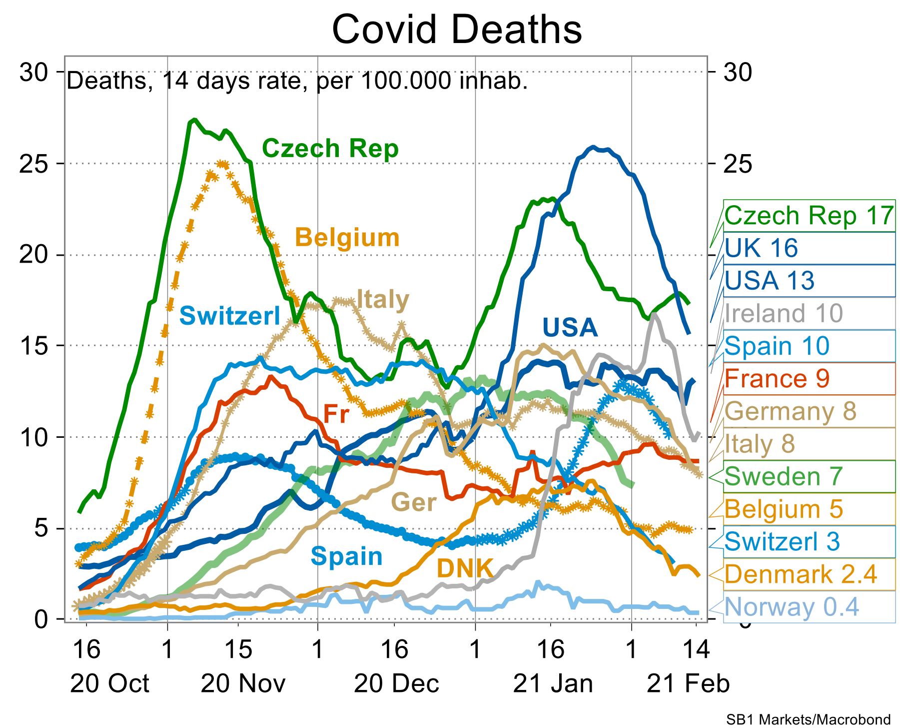




The deaths: Now UK and Ireland are reporting a steeper decline than all others

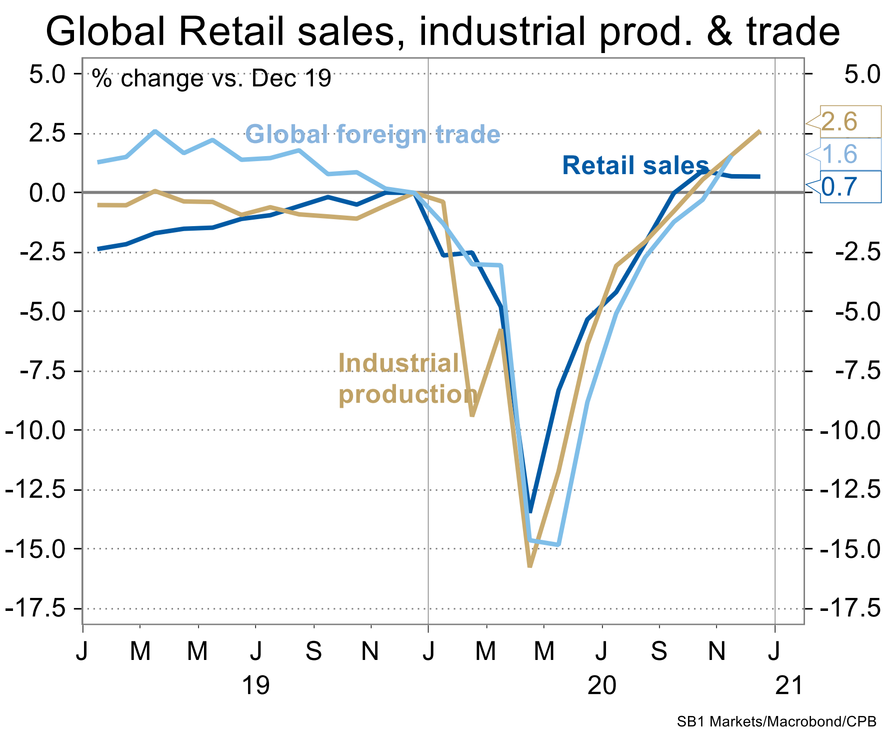
No 'important' country on the way up anymore!

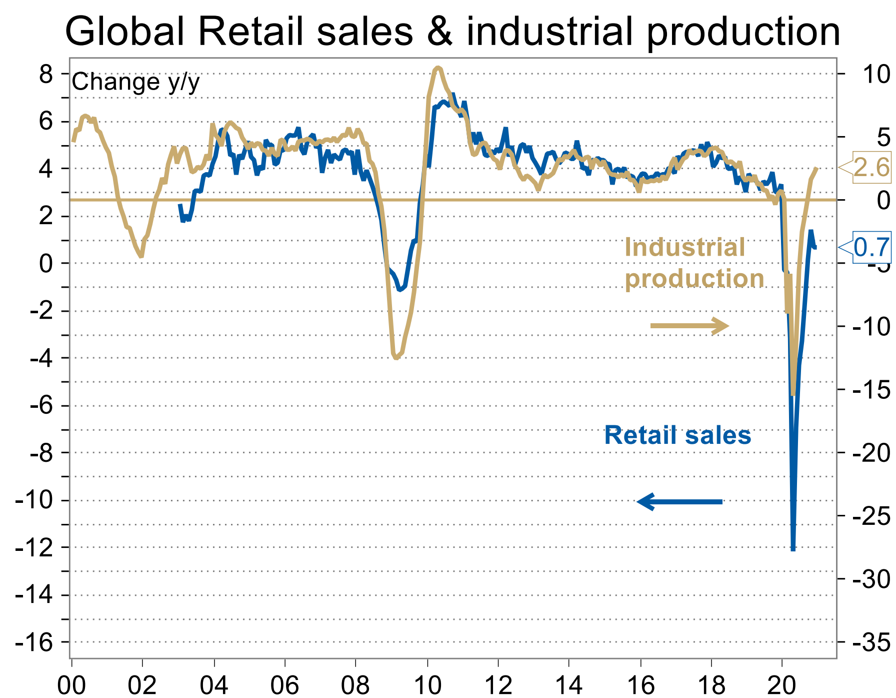




Retail sales has flattened, manufacturing production continues upwards

And global foreign trade rose almost 2% m/m in Nov, and trade volumes are above early 2020 level



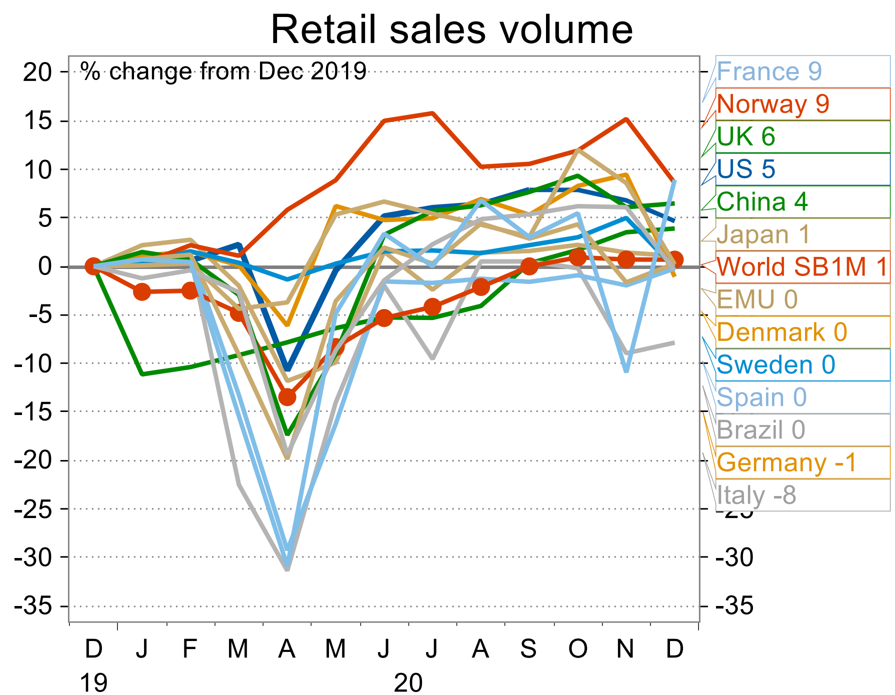


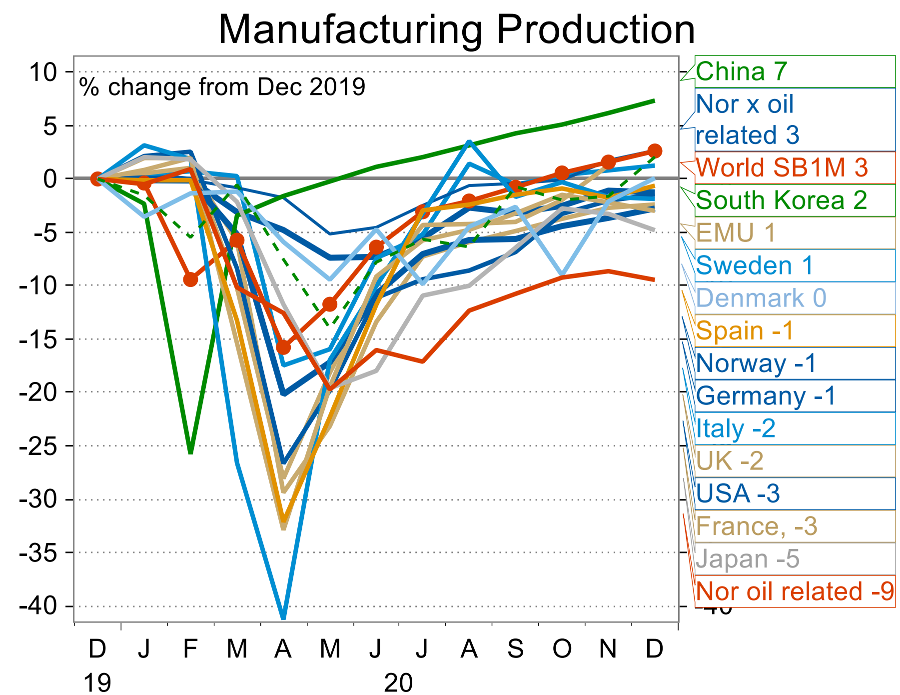
Memo: Keep in mind the different scales at the chart above

- **Retail sales** were flat in in Dec, following a small decline in Nov. Sales are 1% above the pre-corona level
- **Manufacturing production** probably climbed 1%, and is 2.6% above the pre-corona level, according to our estimates
- **Global foreign trade** rose 1.9% in November, and the level is 1.6% above the Dec-19 level – the gap is closed!!

Global retail sales flat in Nov/Dec due to US, Europe & Brazil, +1 % vs. Feb 20

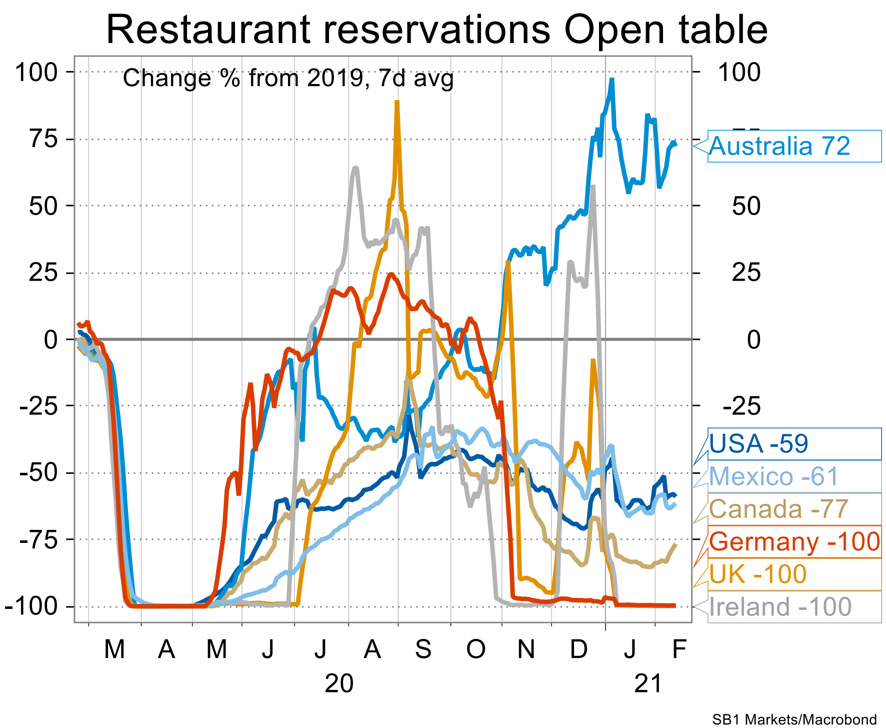
Manufacturing production still on the way up, 3% above Feb 20 level

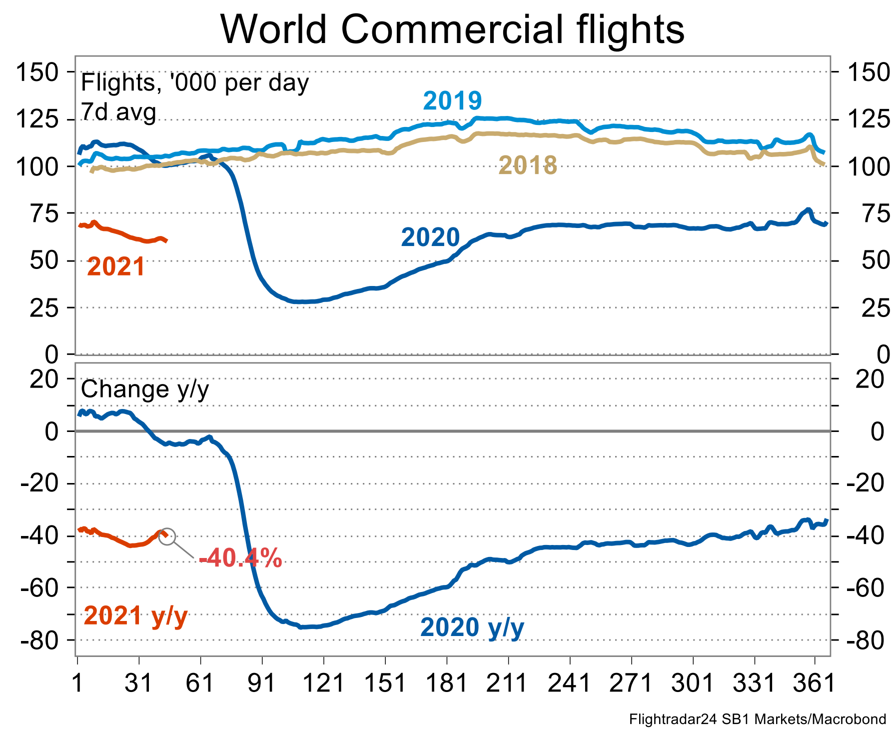




Restaurants open only in Australia. Full closure in Ireland, UK & Germany

US restaurants are slowly opening up!





- Commercial airline traffic has bottomed? Still down 40% vs a normal level, measured in no of flights. And the decline in no of passengers is far worse

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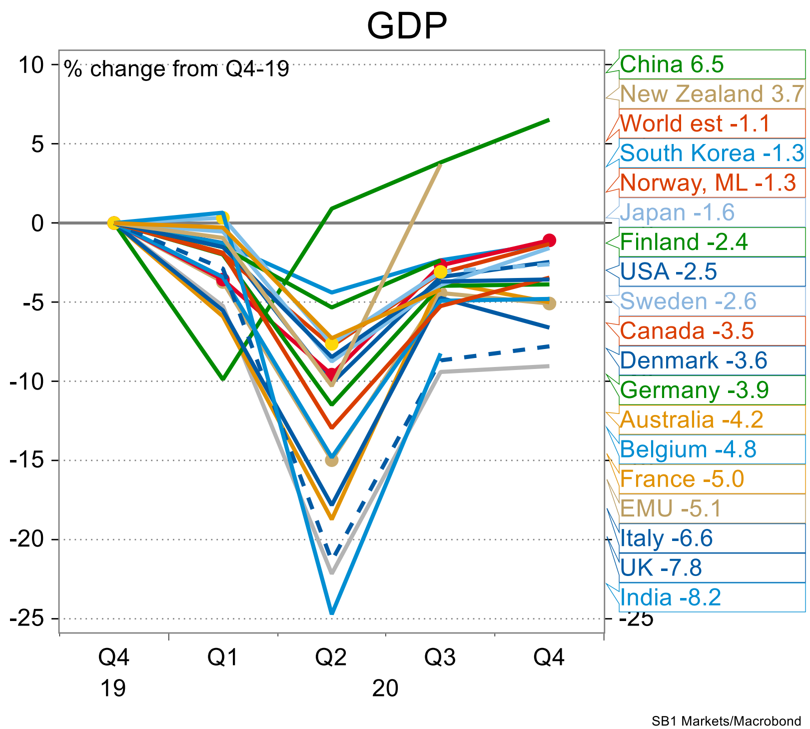
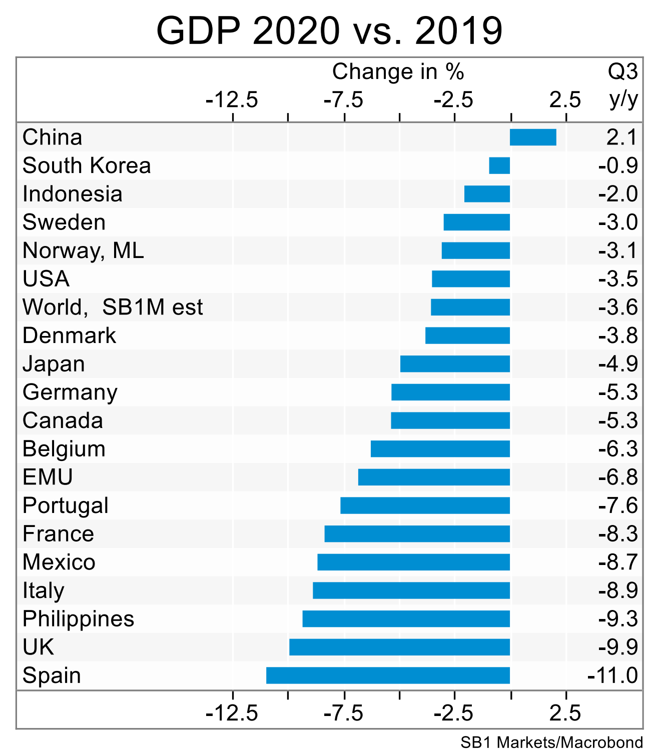
Growth slowed in Q4 but still grew above trend, at a 5%+ pace, 1.1% down y/y

GDP fell in EMU but most other countries/regions grew in Q4

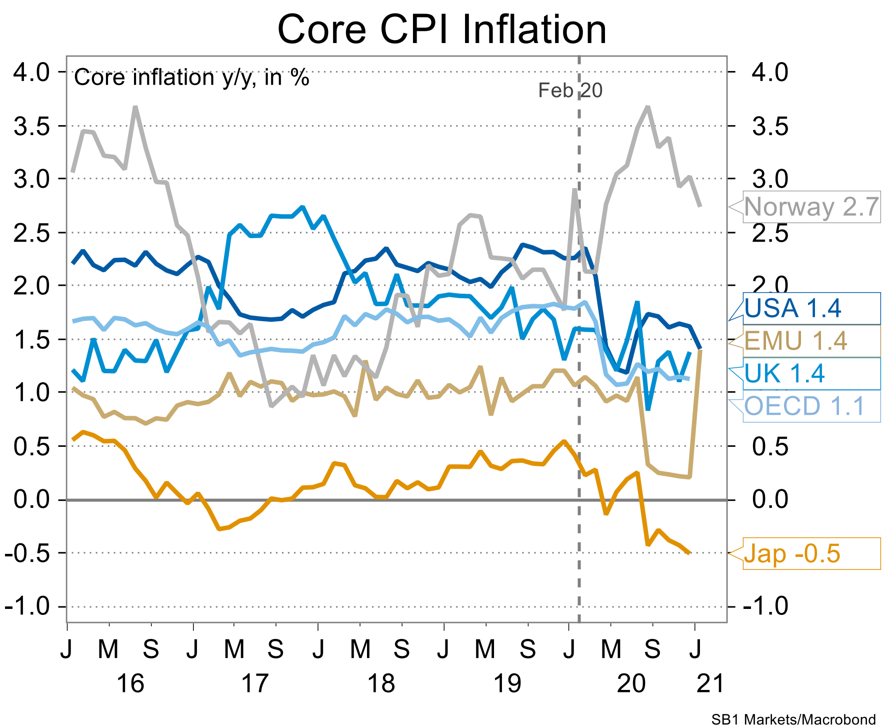


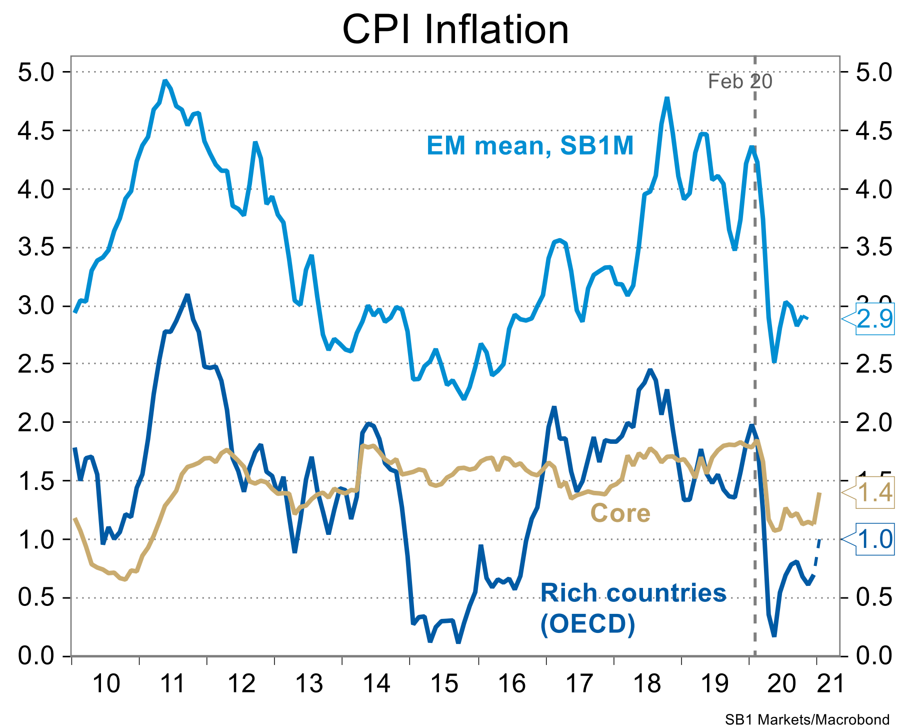


- We estimate that GDP grew by at least a 6% pace in Q4, if so leaving global GDP down 1.1% y/y. Last year GDP fell 3.6% (still an uncertain figure!)
- China & US have reported decent Q4 growth, alongside some Asian countries, UK & Norway! But most other countries reported growth too (but not France& Italy)
- China grew by 2.1%, all others down
- Sweden down 3%, Norway (Mainland) 3.1% (we expected -3.4%) and US -3.5%
- EMU contracted almost 7%, UK by 10% (and Spain by 11%). What a year…

Inflation still in the doldrums, but it is not declining further

Inflation in the EMU shot up in Jan, mostly due to the reversal of the German temp. 3 pp VAT cut

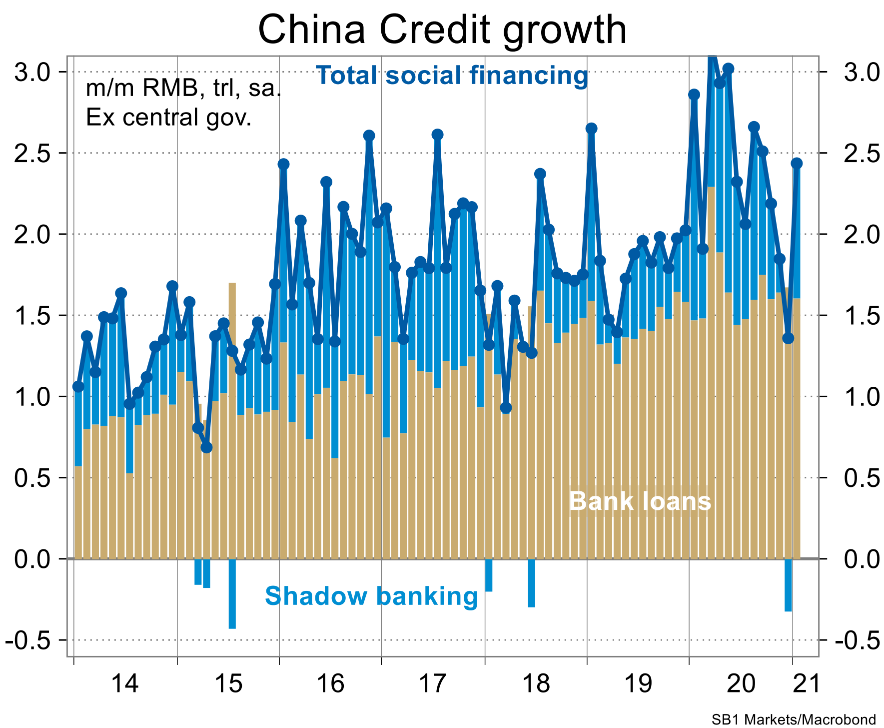


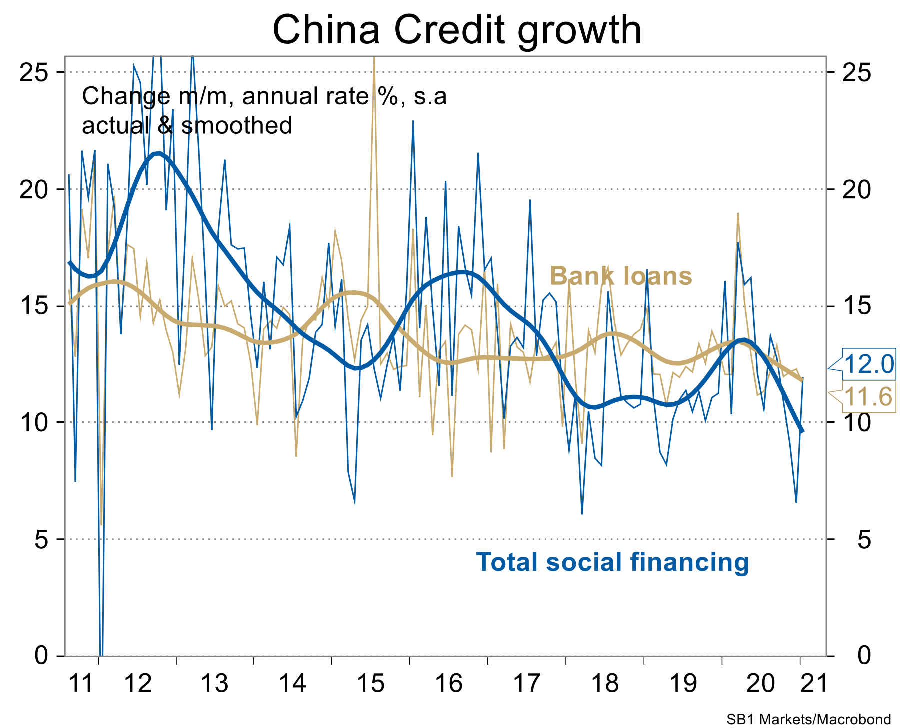


- The PMI reports as well as the increase in raw material prices towards a lift in at least the headline inflation rate the coming quarters

Credit growth accelerated in January

Trend may be down, but growth in shadow banking rebounded

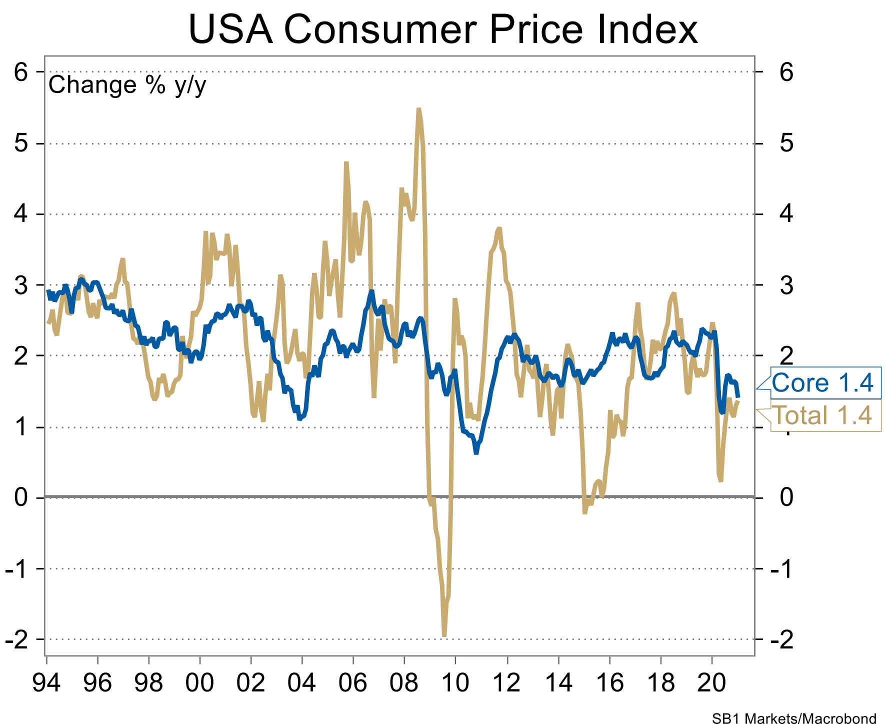


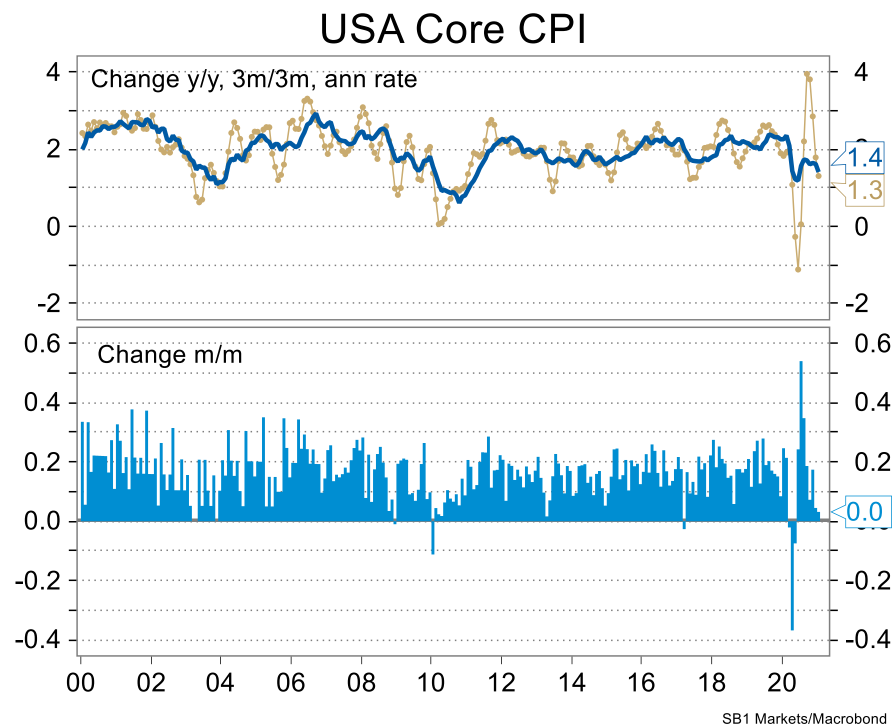


- In Jan credit grew at a 12% rate (m/m, annualised). Smoothed, the underlying rate may be some 10%, down from 13% during the spring (and >15% during some months). A 10% growth rate is most likely above trend growth in nominal GDP
  - Total credit rose by RMB 2.4 trl (not seasonally adjusted, *total social financing* ex central government bonds but including local governments, and ex. corporate equities). Our seasonal adj. is pretty good but always more uncertain in Jan/Feb due the Lunar New Year holiday. Actual credit grew by 4.9 trl, somewhat above exp. at 4.6 trl
  - Bank loans rose by 1.6 trl, and growth is slowly slowing. Actual lending rose by 3.6 trl, expected 3.5 trl. Shadow banking credit rose by 0.8 trl, more than 1/3rd of the total
- Total credit is still up 12.3% y/y, substantially above normal income growth – but this is just due to the rapid credit expansion in H1, when authorities opened up the gates to support the economy after the corona crisis
- Now, the authorities are trying to calm credit markets down. They no doubt acknowledge that the debt/GDP ratio already is dangerously high. **Still, they do not want to strangle the economy – which the strong January data signals!**

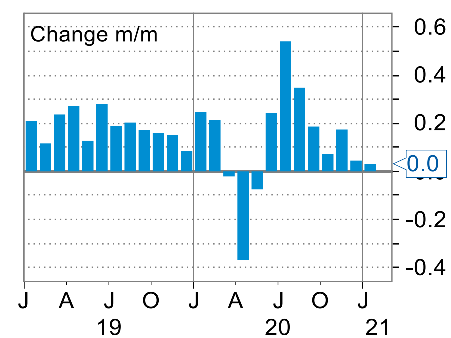
Inflation currently not a problem: Core CPI ticked in at 1.4%, below consensus

…while headline prices rose 0.1% to 1.4%



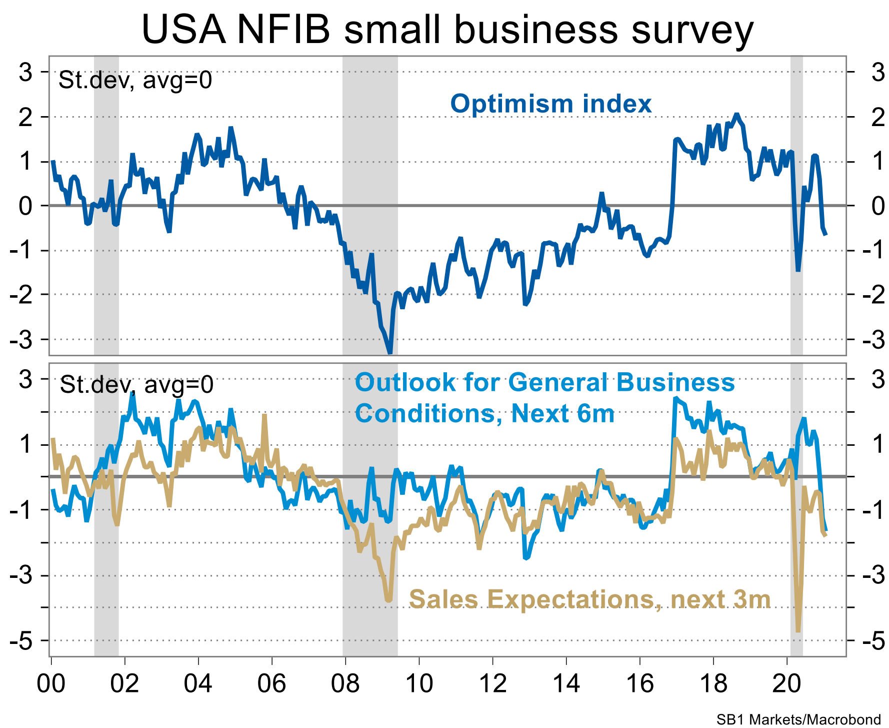


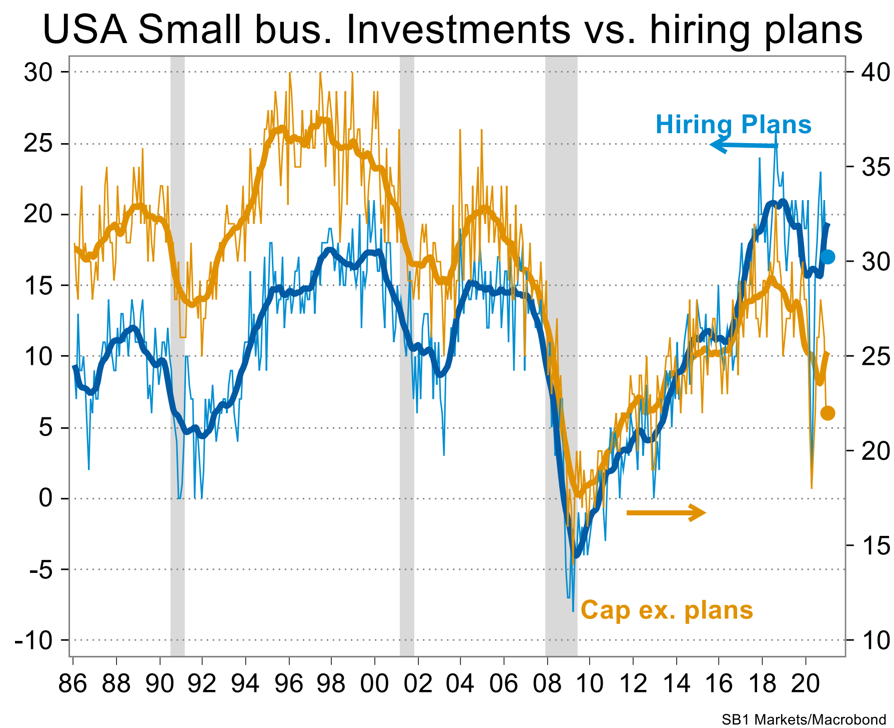
- The annual core rate came down to 1.4% (exp. unch at 1.6%), and is well below the 2.4% pre-corona level, and below Fed's 2% target (measured by the national account PCE price deflator, which over time has reported an inflation rate 0.2 – 0.3 pp below the CPI inflation rate)
- Headline CPI rose to 1.4% y/y; up from 1.3% in Dec, due to higher gasoline prices. In May, headline CPI was up 0.2% y/y
- Vehicles, lodging and airline ticket prices saw the biggest decline from previous month
- Going forward, base effects (prices fell sharply last spring) will bring the annual rate sharply up



Small businesses' optimism fell to 8-month low at 95 (-0.6 st.dev below avg)

In spite positive vaccine news, assessment of the outlook hasn't been more pessimistic in 8 years

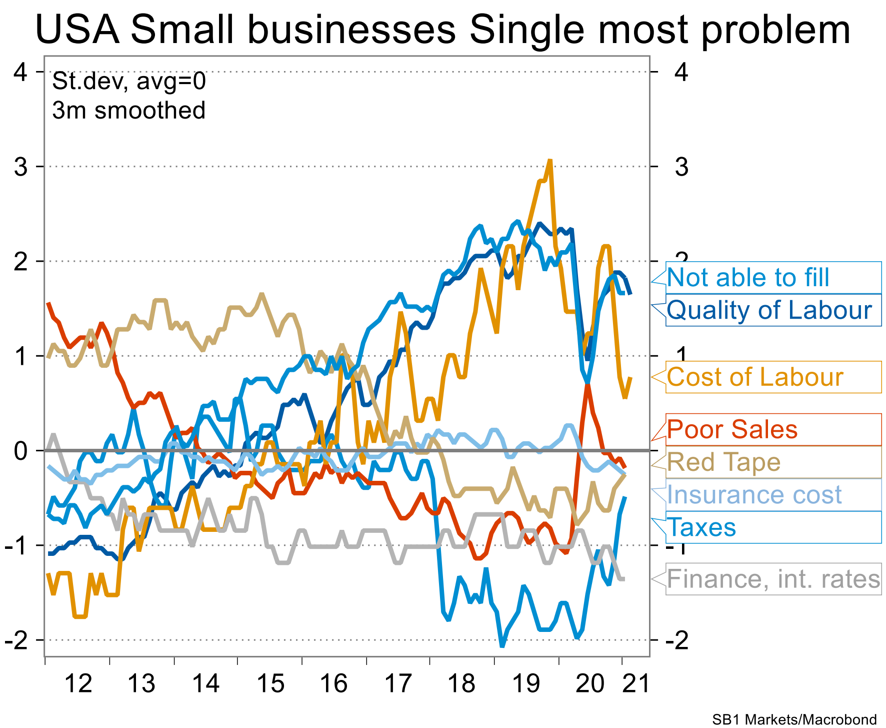


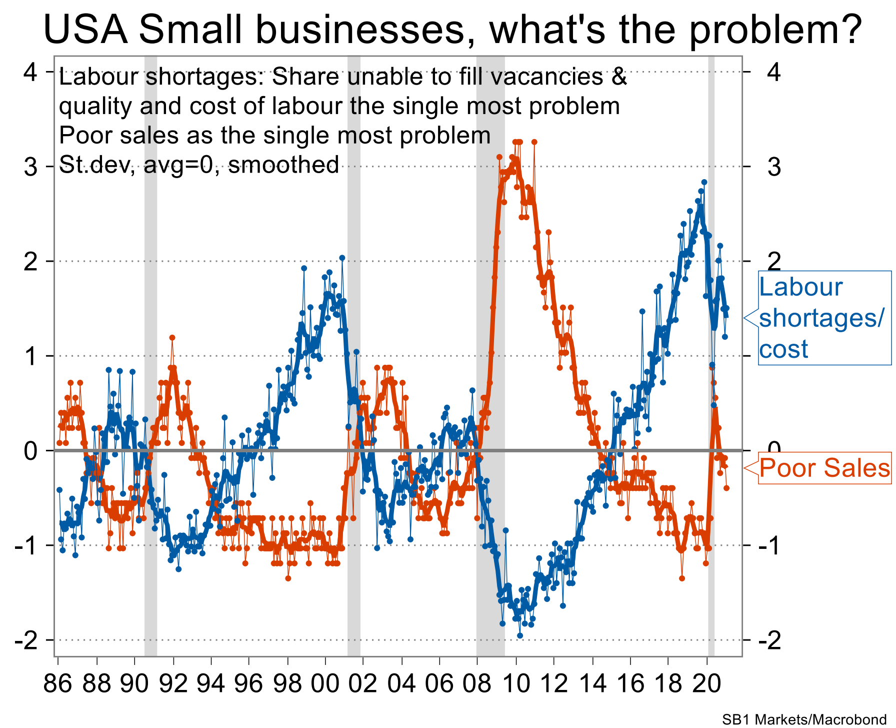


- The **NFIB optimism index** fell to 95.0 in January from 95.9 (expected up to 96.8). It's safe to assume that the latest coronavirus wave and weaker spending has influenced the opinion of small-business owners. In addition, Biden was probably not their favourite candidate for president. 4/10 components declined, just 2/10 improved
- **The expectation index**, the outlook for the next 6 months, fell for the 4th month – currently 1.65 st.dev below average
  - » Sectors: Services and professions are the most downbeat, while construction and manufacturing in the lead
- Businesses also cut back their **sales expectations** further in January, to the lowest level since 2011 (barring the March – May period last year)
- **Investment plans** remained unch from Dec, at well below an average level
- Business also did not change their **Hiring plans** from Dec, which remains at a far above average

Supply and quality of labour yet again reported as the major problems!

Interestingly, fewer than normal see poor sales as a problem. What a recession!



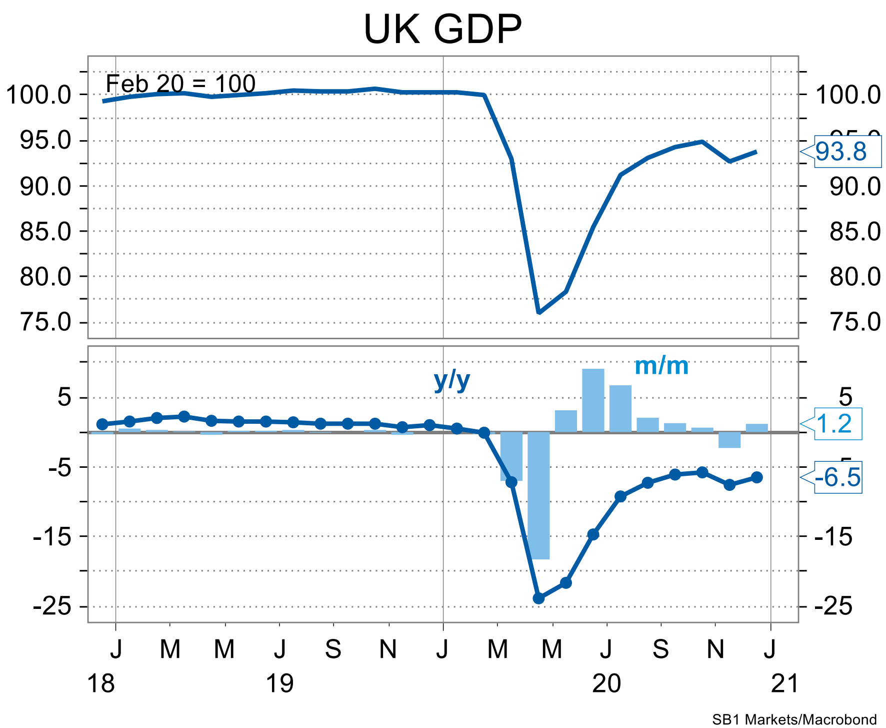


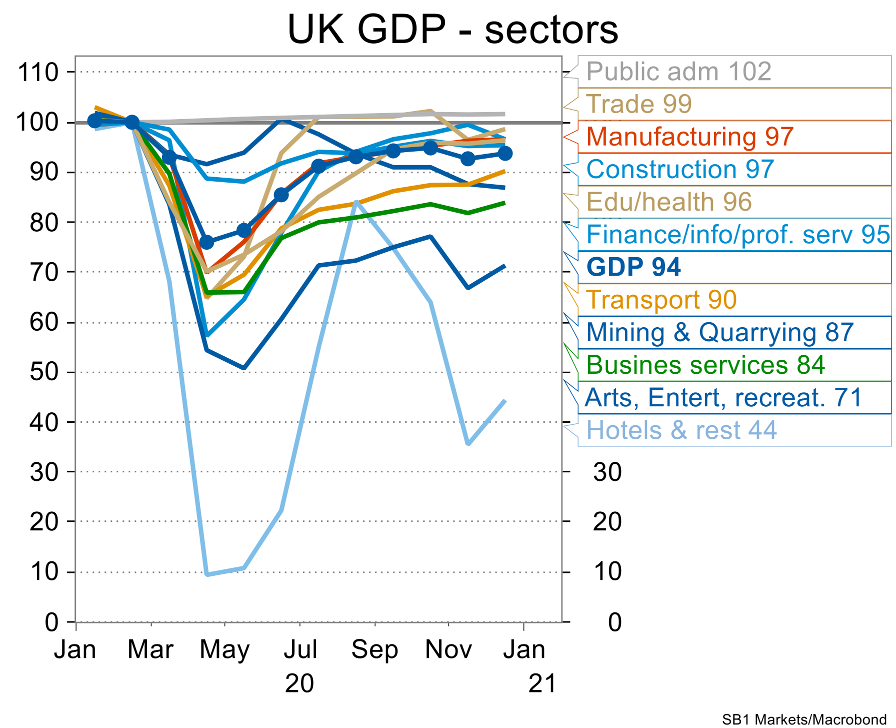
- More businesses have been stating **weak sales** as the major problem during the pandemic, but the level has been surprisingly low, and in January the level decreased and is <u>below average</u>!
- The share of businesses that have been noting problems with **tight labour markets** has fallen somewhat during the pandemic, but the share rose in Jan and <u>remains at a remarkably high level</u>
  - » Both the **ability to fill vacancies**, and **quality of labour** are still reported as huge problems (2 st.dev above avg). Concern about the **cost of labour** also increased and thus remains at a higher level than normal
  - » Unusually few companies are complaining about **finance/interest rates** and about **taxes** (although tax concerns increased post Biden win, so far without any taxes being increased, as far as we know)

SpareBank 1 MARKETS

UK economy shrinks 9.9% in 2020 – biggest decline since the 1700s

...But GDP grew by 1.2% in December, beating estimates by 0.2 pp. Q4 growth at 1% (exp. 0.5%)

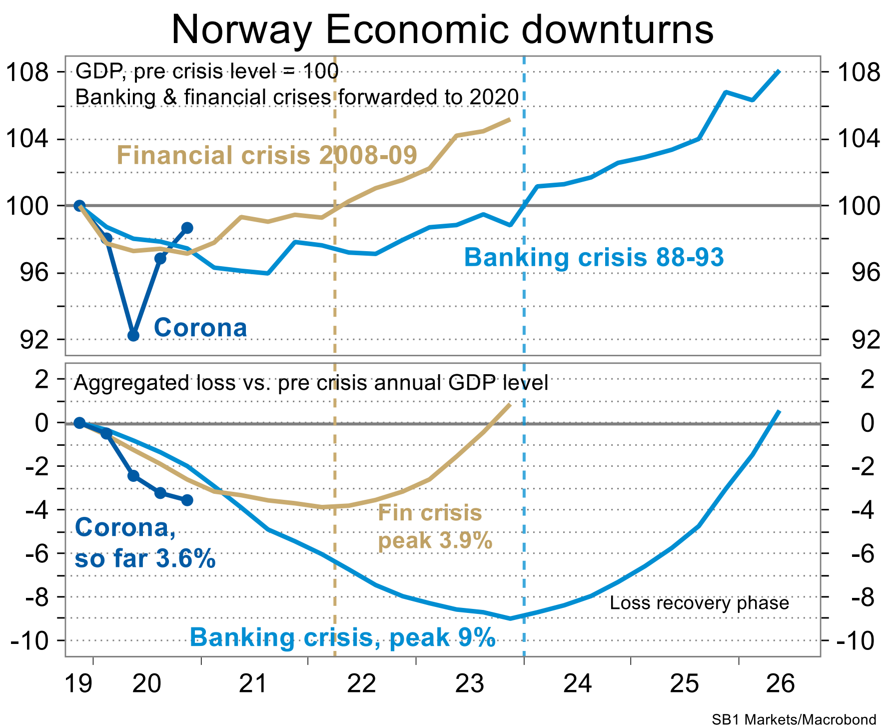




- The service sector was up 1.7% - the biggest contributors here were hotels and restaurants which were up 25%
- The construction sector fell by 2.9%, while manufacturing was up 0.2%
- Other sectors were mostly up, like trade (+2.2%), Transport (+3.1%), health (+2.4%), and arts/entertainment (+6.8%)
- GDP in December is down 6.2% below the Feb level. (Norway is down 1.1%)

A special year – that ended pretty well: Mainland GDP now 1 – 1½% down vs PC

GDP grew more than expected in both Dec & Q4, and declined less than expected in 2020, -3.1%



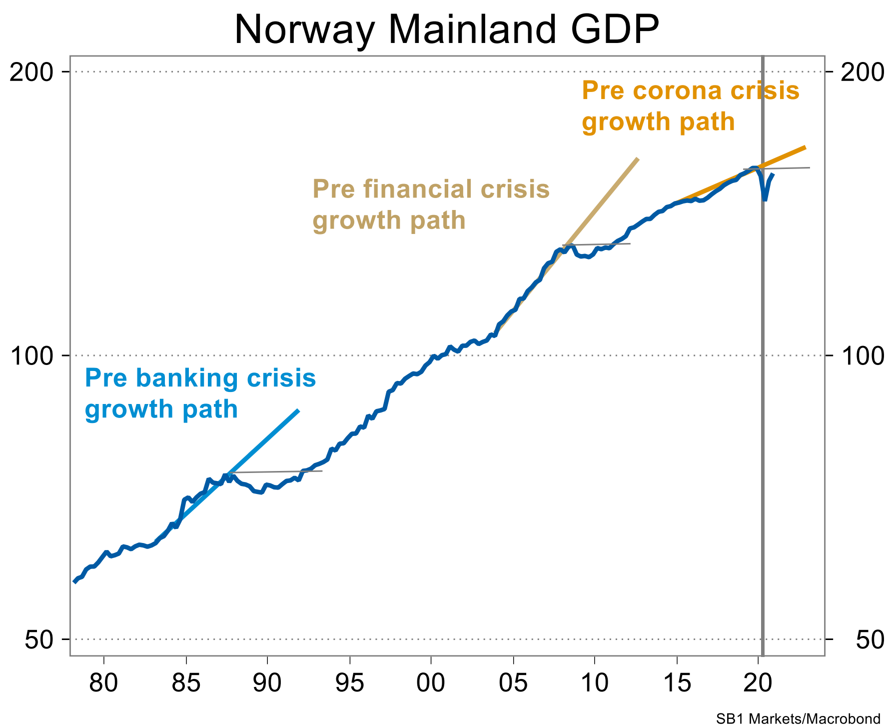
- **2020: Mainland GDP down 2.5%. Or 3.1%?**
  - Before working-days adjustment, Mainland GDP fell 2.5% (total GDP -0.8%, as oil production rose sharply), which is often referred to as the 'official' figure. 2020 yielded 3 more working days than 2019. We usually refer to WDA and seasonally adjusted data, in Norway and elsewhere. And the 'real' decline in GDP was 3.1%, the largest setback since 1944 (total GDP -1.3%)

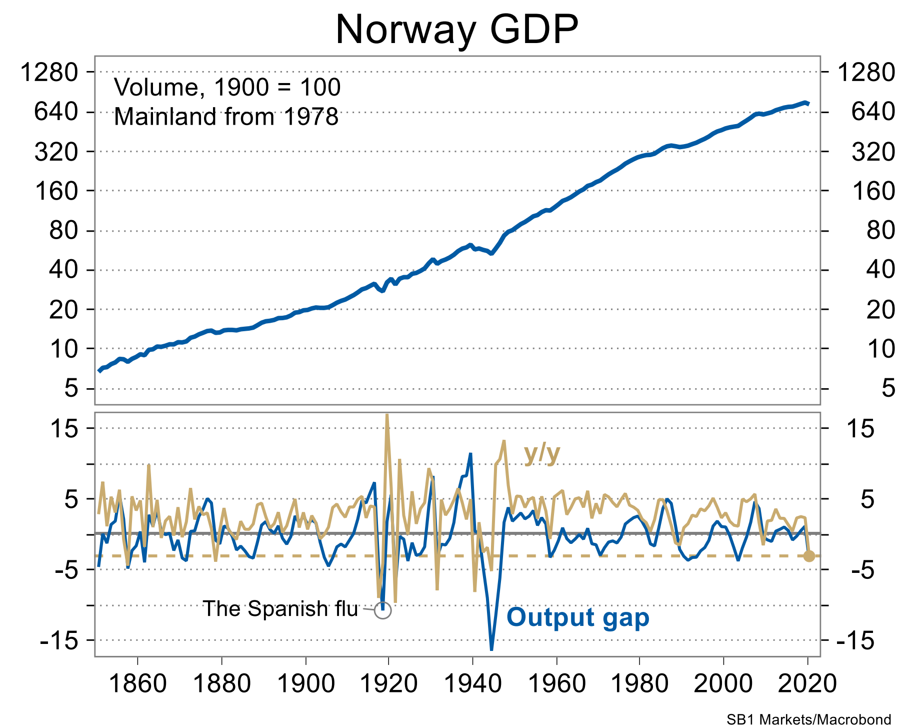
- **The 10% downturn last spring was extreme**, as has the recovery been so far . This is, of course, not a normal economic recession but a virus induced setback, defying all normal crisis cycle characteristics
- Following a strong recovery, starting in mid April, GDP is now just 1% – 1.5% below the pre-corona level, following a 1.0% growth in December (m/m) and 1.9% in Q4 (q/q)
- In 2020, Mainland GDP fell by 3.1%, the largest setback on record (2.5% not working days adjusted, we prefer the former)
- **The loss of economic output**, financially covered by the government (and future tax payers) so far, is substantial – and we do not yet know the final outcome
  - Calculated by the loss of activity vs. from the peak in Q4 19 until activity is back to the same level, we assume in late Q1 or in Q2 next year, the lost output will equal somewhat less than 4% of pre-corona annual GDP. That's close to the loss of output of the financial crisis, equalling 3.9% of GDP. During the housing bubble burst/banking crisis starting in 1988, the loss equalled no less than 9% of GDP
  - However vs. likely growth expectations before the financial crisis compared to the similar before the corona crisis, the corona crisis will most likely turn out to be far smaller (and miles smaller than during our banking crisis). *Check the chart at the next page*. In general, and for the world economy, that's why assets markets are so strong, surely also supported by record low interest rates

SpareBank 1 MARKETS

Expectations could not have been that bright, before corona hit, no boom then

Our expectations were muted – and growth had not been strong over the previous years

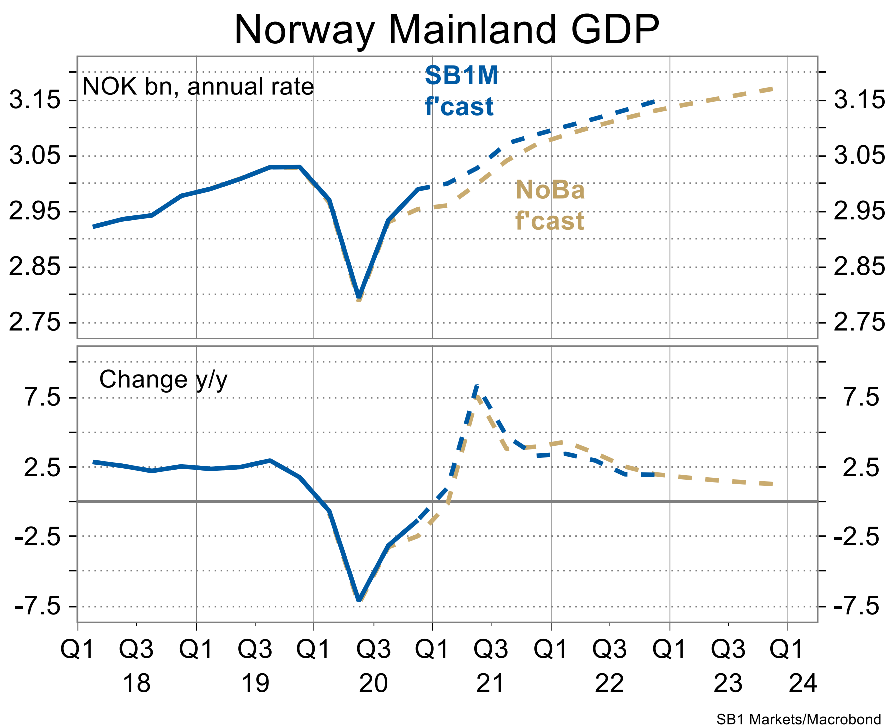




- The contrast to the banking & financial crises are obvious, the disappointment vs. especially long-term expectations is not that large this time
- For the record: A 3% drop in GDP is not normal. Last time was probably in 1944, and before that in 1940, 1931 and during post WWI shipping/banking boom that collapsed in 1921, and before that again a downturn as the Spanish Flu hit in 1918

The outlook: Towards 4 – 4½ % 2021 growth?

Q4 GDP is 2.3% above the 2020 avg, and 1.2% ahead of NoBa's Dec forecast



- We expect the **output gap** to be closed earlier than Norges Bank expects (Q2-22)
- Thus, we expect that Norges Bank will start hiking its **signal rate** in H2 – the vaccine rollout/virus containment will decide when

... and barring a bad virus/vaccine scenario, we expect economic activity to increase sharply through 2021, after a Q1 break

Households

- **Goods consumption** will slow down but remain higher than the pre-corona trend normal until we can spend more both on domestic services and abroad.
- **We are very confident that demand for services (x foreigners)** will recover briskly as soon as the virus is brought under reasonable control in Norway. Our base case is that this will happen through Q2 and into Q3. The large accumulated savings through last year, and still an extraordinary high savings rate make us even more certain
- **Foreigners' spending** in Norway (down equalling 1.4% of GDP) will not recover before the coronavirus is beaten down, abroad and in Norway. No quick fix. However, Norwegians spend 2.5 x more abroad, and this spending will not recover fully before foreigners are coming here. In the meantime, more 'Norwegian' spending in Norway
- **Housing investments** have bottomed, and the 2. hand market is tight, and new home sales are on the way up. Housing starts too. At least until interest rates are turning upwards

Businesses

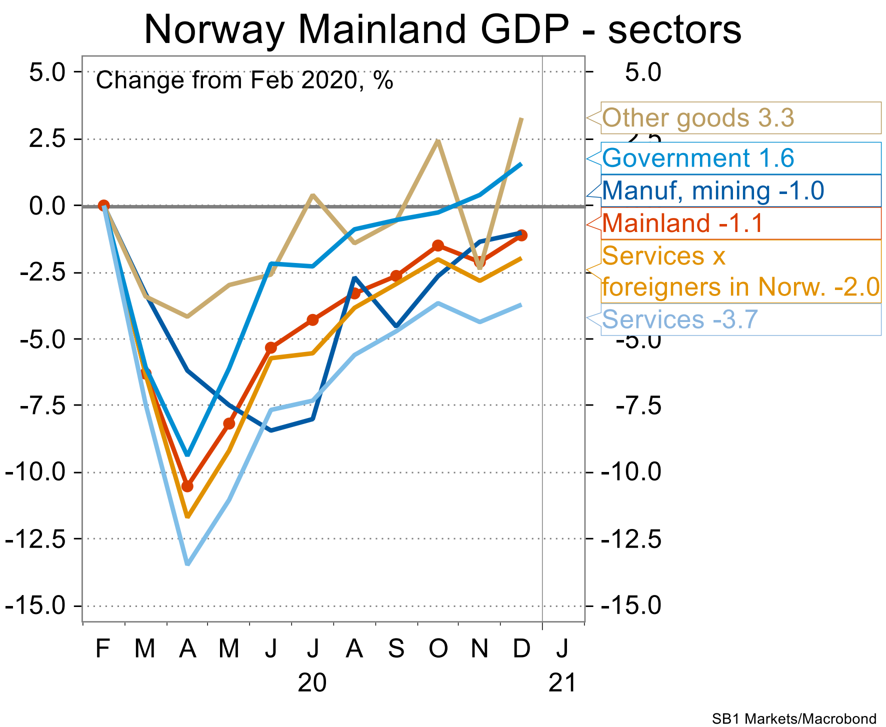
- **Mainland business investments** have stabilised – and surveys have strengthened. We are revising our forecast upwards.
- **Oil investments** fell sharply last year but favourable change in the tax regime as well as an oil price at USD 60, may stabilise investments in 2020

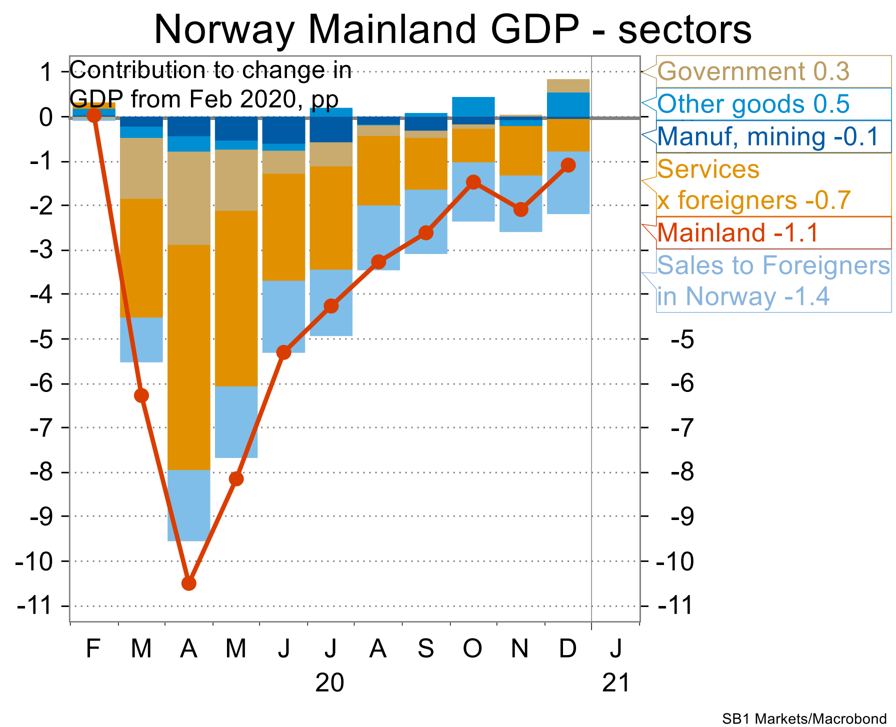
Exports

- **Mainland goods exports** have recovered will be kept up, as long as demand for goods abroad remains strong. And most likely, it will

Production: Private services recovered the November losses in December

Still down by 3.7% vs Feb '19 – of which more almost the half due to 'no' demand from foreigners

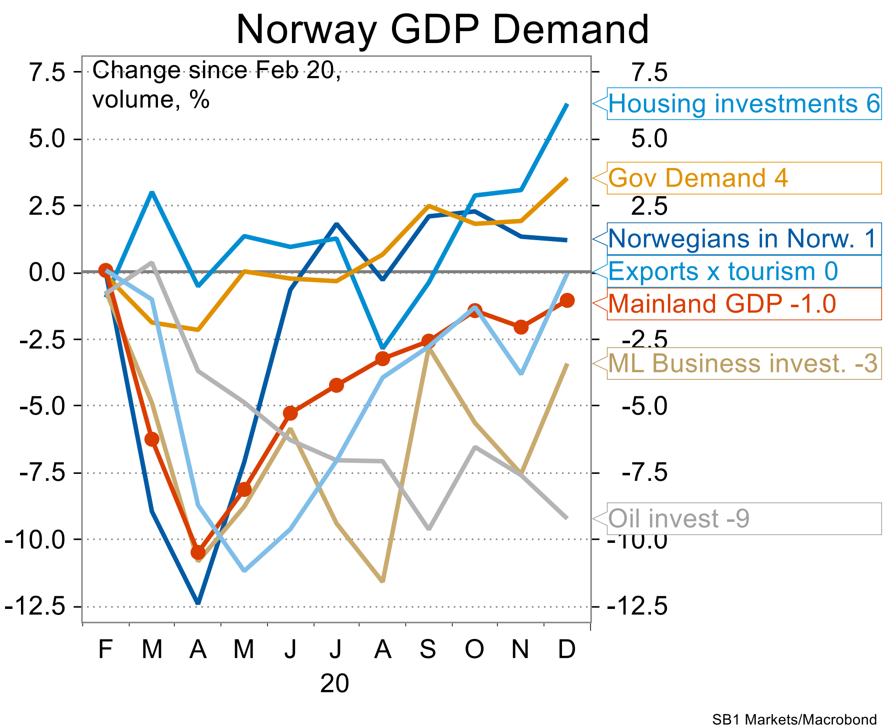


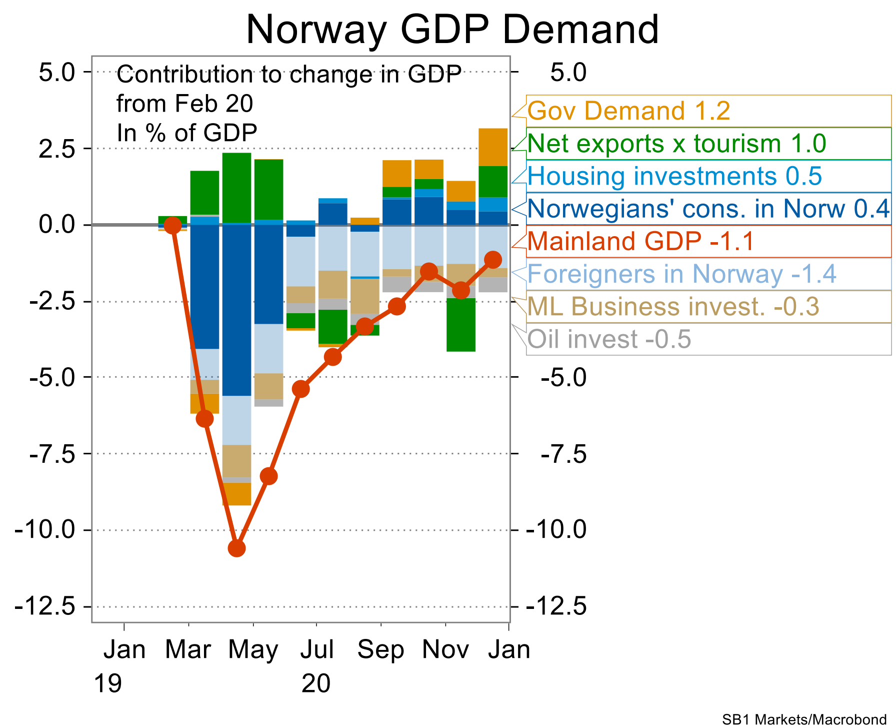


- In Nov-Dec **service sector production was unchanged** amid tighter corona restrictions – compared to the 13% drop last March/April. Still, the upside is limited before the virus it brought under control
- **Manufacturing production** is still recovering, and is now 1% below the Feb level. However the downturn is solely due to steep decline in oil related industries – as oil investments are down 9% vs Feb (and 14% vs Q4 '19). Ex oil related manufacturing industries, production is up
- **Other goods production** is volatile mostly due to (ocean) **fisheries and electricity production**, both down in Nov and sharply up in Dec, explaining large parts of the changes in total GDP! (*See more the two next pages*)

Demand: Exports, housing, mainland business inv., and gov't spending up in Dec

Household consumption fell marginally, oil investments somewhat more

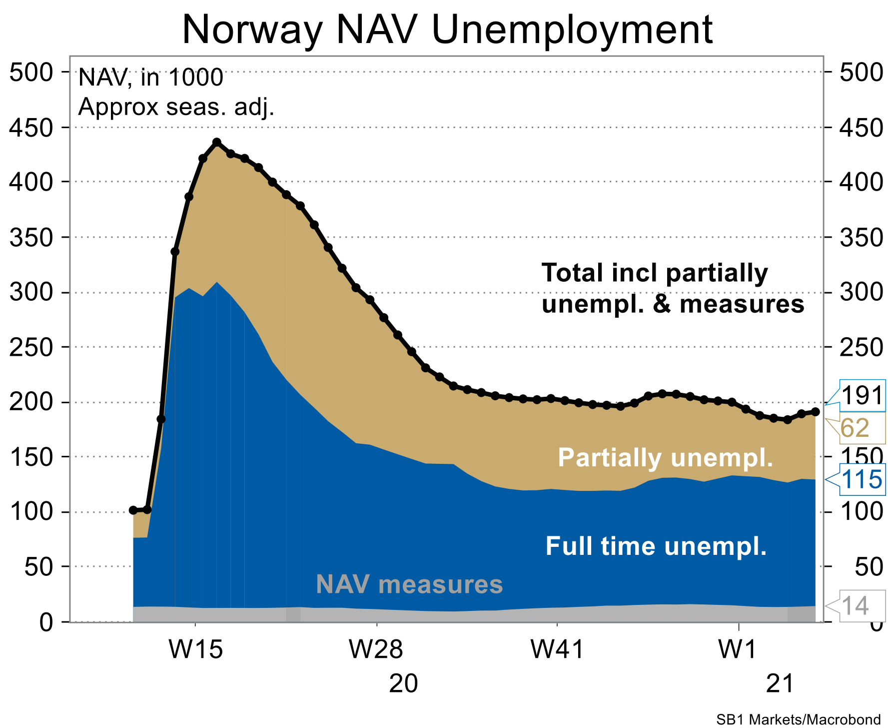


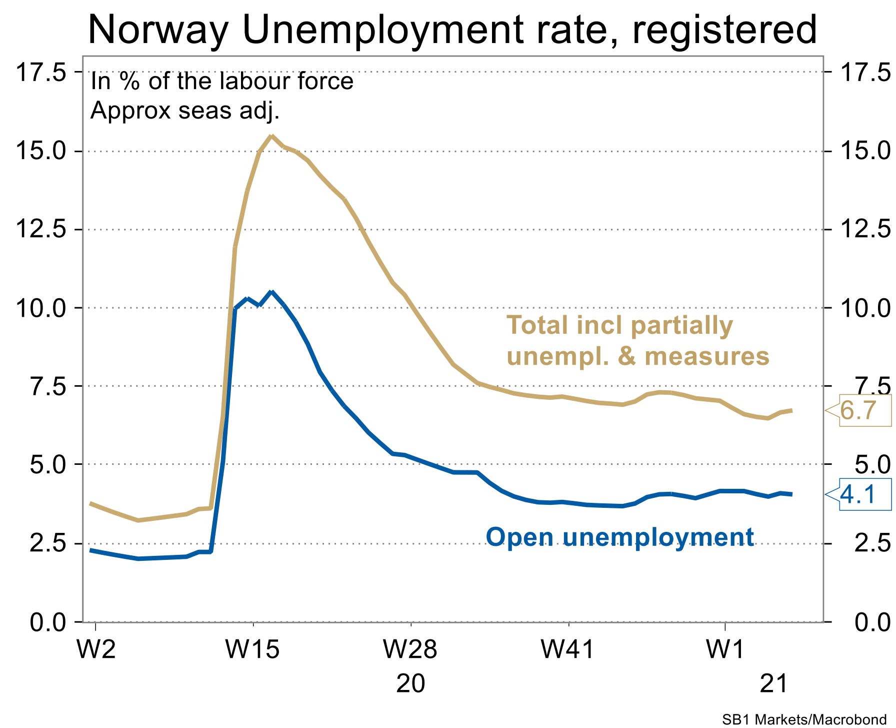


- **Norwegians' consumption in Norway** fell marginally due to lower consumption of goods – which remains strong. **Foreigners spent** a tad less in Dec, and their lack of demand deducts 1.4% from GDP (not adjusted for import content of goods they (used to) buy here)
- **Mainland business** investments reversed the loss in the two previous months, and are down just 3% vs. the Feb level – deducting 0.3% from GDP
- **Oil investments** are still on a slippery slope, down 9% (0.5% of GDP) vs Feb – and down 14% vs. Q4 2019
- **Government demand** is up 4% vs. Feb and has contributed to a 1.2% increase in GDP (alas, others are close to flat)
- **Mainland exports (x tourism)** rose and are back to the Feb level. Net exports are higher than in Feb, as **imports** are still below the Feb level
- **Monthly data are volatile, and consumption is trending up, as are exports x tourism. In sum, investments are trending up**

NAV weekly unemployment close to flat

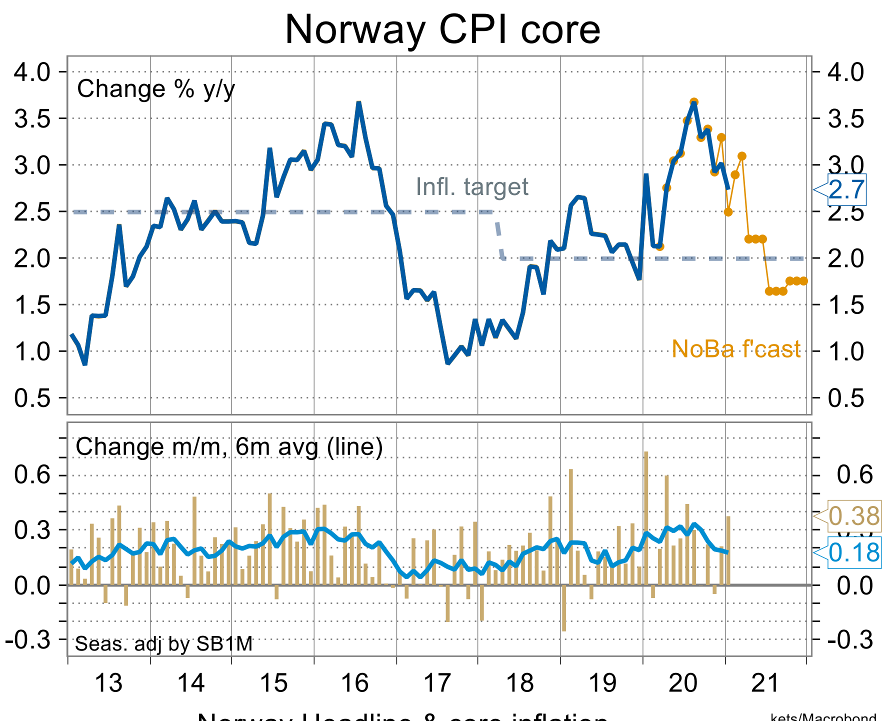
.. Adjusted for the normal seasonal pattern. Confirming no big hit due to the tightened restrictions

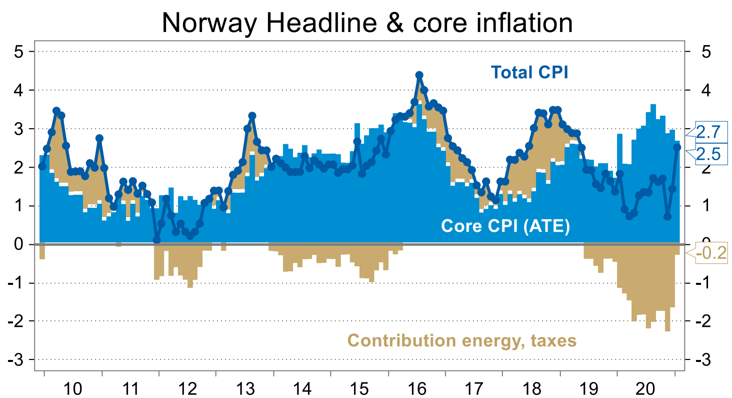




Inflation surprised on the upside in January

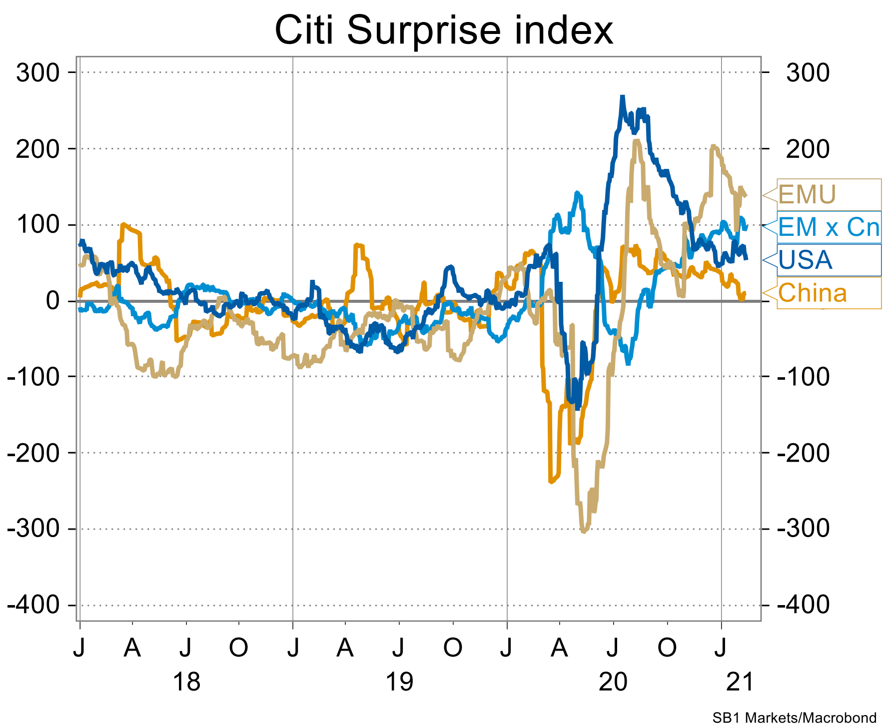
Core inflation fell but less than expected, and total inflation was far higher than we expected

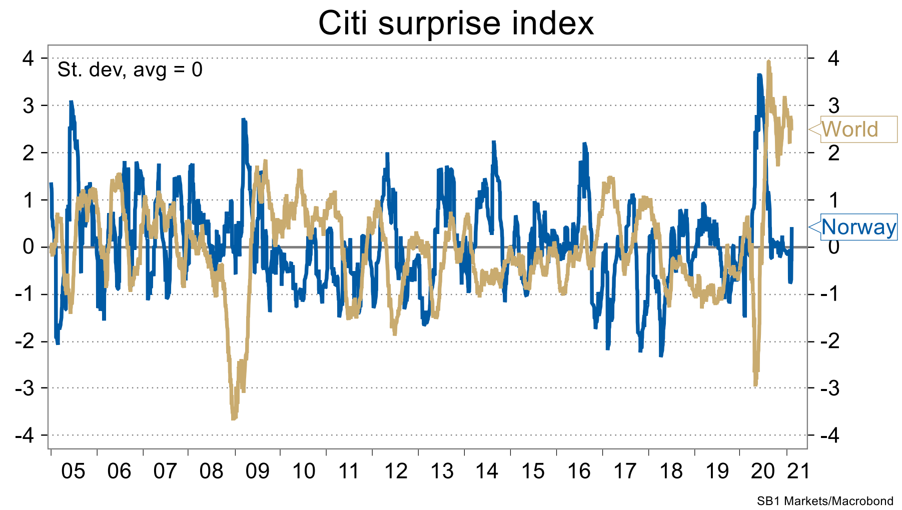


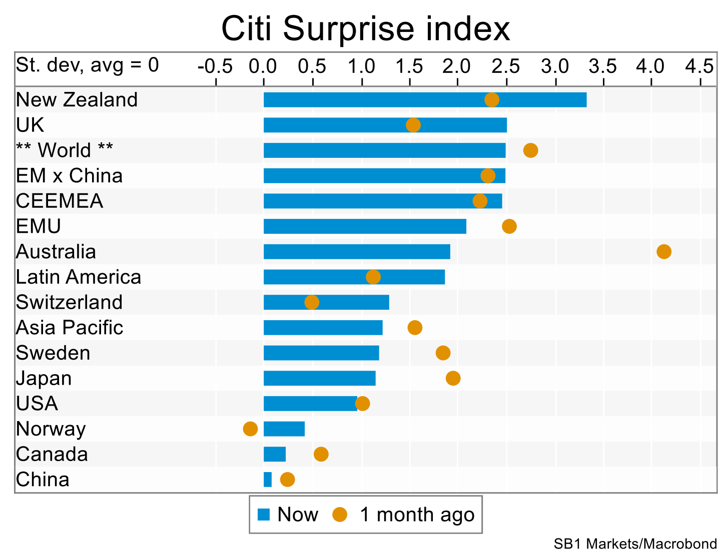


- CPI-ATE (ex. energy and taxes) inflation fell 0.3 pp to 2.7% in January; a print far above consensus (2.4%) and our forecast (2.3%). Norges Bank expected 2.5% (Dec MPR f'cast)
  - » Prices rose 0.4% m/m (s.a)
  - » Airfare ticket prices were higher than we expected, as were food and clothing prices
  - » Inflation is below 2% for housing, clothing, alcohol , and airline tickets – all others are still above
  - » Imported goods price inflation fell in Jan, and will recede further as NOK effect fades
- Total inflation accelerated 0.9 pp to 2.5%, far more than we expected as electricity prices rose more than we assumed. They are now up 19% y/y, up from down 21% last month
- **The price outlook**
  - » We expect inflation to slow the coming quarters as the NOK effect fades and wage inflation remains muted. Demand for goods will have to decline from a very high level, while the 'beaten down services' will not have pricing power anytime soon, even if demand should pick up steam during Q2/Q3
  - » Anyway, CPI inflation will not have any material impact on Norges Banks and monetary policy the coming months. It's all about the Covid-19 impact on the real economy. When the war on corona is won, we think the housing market will become more important for Norges Bank than actual inflation

Surprises are still on the upside, now even in Norway (and everywhere)







- **All major countries/regions** are reporting data above expectations, for the first time ever
- The **Euro Zone** is still far up on the list, even if the economy has slowed. Expectations have been adjusted
- The **US** is still well into positive territory – and is heading upwards
- **China** has moderated lately, has fallen down to an average level – at the bottom of the list
- **Other EMs** are well above their average level, and are on the way up
- **Besides China, Norway, US (!)** at the bottom

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

The Calendar

The calendar is packed this week: PMIs, EMU & US ind. prod. The oil investment survey in Norway

Time	Count.	Indicator	Period	Forecast	Prior
Monday Feb 15					
08:00	NO	Trade Balance	Jan		12.1b
11:00	EC	Industrial Production SA MoM	Dec	-0.6%	2.5%
Tuesday Feb 16					
08:00	NO	Housing starts			
11:00	GE	ZEW Survey Expectations	Feb		61.8
11:00	EC	Employment QoQ	4Q P		1.0%
11:00	EC	GDP SA QoQ, rev.	4Q	-0.7%	-0.7%
14:30	US	Empire Manufacturing	Feb	6.7	3.5
Wednesday Feb 17					
08:00	**NO**	**Oil sector investment plans '21**	**Q1**	**-3.0%**	**-9.0%**
08:00	NO	Manuf., power supply inv. Plans	Q1		
14:30	US	PPI Ex Food and Energy MoM	Jan	0.2%	0.1%
14:30	**US**	**Retail Sales Advance MoM**	**Jan**	**1.0%**	**-0.7%**
14:30	US	Retail Sales Control Group	Jan	1.0%	-1.9%
15:15	US	Industrial Production MoM	Jan	0.4%	1.6%
15:15	US	Manufacturing (SIC) Production	Jan	0.7%	0.9%
16:00	US	Business Inventories	Dec	0.5%	0.5%
16:00	US	NAHB Housing Market Index	Feb	83.0	83.0
20:00	US	FOMC Meeting Minutes	Jan 27		
Thursday Feb 18					
09:30	SW	CPIF Excl. Energy MoM	Jan	-0.90%	0.60%
14:30	**US**	**Building Permits**	**Jan**	**1668k**	**1709k**
14:30	US	Housing Starts	Jan	1659k	1669k
14:30	US	Initial Jobless Claims	Feb-13	765	793
14:30	US	Philadelphia Fed Business	Feb	20	26.5
16:00	EC	Consumer Confidence	Feb A	-15	-15.5
18:00	**NO**	**Governor Olsen, Annual Address**			
Friday Feb 19					
00:30	JN	Natl CPI YoY	Jan	-0.7%	-1.2%
06:00	SW	Houseprices, Valueguard			
08:00	UK	Retail Sales Ex Auto Fuel MoM	Jan	-2.1%	0.4%
09:15	FR	PMI Manufacturing	Feb P	51.5	51.6
09:15	FR	PMI Services	Feb P	47.0	47.3
09:30	GE	PMI Manufacturing	Feb P	56.5	57.1
09:30	GE	PMI Services	Feb P	46.5	46.7
10:00	**EC**	**PMI Manufacturing**	**Feb P**	**54.3**	**54.8**
10:00	**EC**	**PMI Services**	**Feb P**	**45.7**	**45.4**
10:00	**EC**	**PMI Composite**	**Feb P**	**48.0**	**47.8**
10:30	UK	PMI Manufacturing	Feb P	53.1	54.1
10:30	UK	PMI Services	Feb P	42.0	39.5
15:45	US	PMI Manufacturing	Feb P	58.6	59.2
15:45	**US**	**PMI Services**	**Feb P**	**58.0**	**58.3**
16:00	US	Existing Home Sales	Jan	6.62m	6.76m

- **Preliminary January PMIs**
  - » **European Services** have been struggling amid lockdowns and travel restrictions for the latter part of 2020 onwards. A marginal improvement in the PMI (to a slower pace of decline) as mobility has increased somewhat in most countries. **European Manufacturing PMIs** have come in at solid levels during the pandemic. **The US service sector** has fared much better than its European counterpart recent months, and the latest PMIs have signalled strong growth. No slowdown is expected in Feb either, as the spread of the virus has slowed sharply since early Feb. Services in the UK will probably still report weak PMIs but we doubt activity fell in Feb as no. of new Covid-19 cases has fallen sharply
- **USA**
  - » **Retail Sales** has fallen in the past two months. Uncertainty around the covid-relief checks and an increase in virus cases probably to blame. In January, covid cases fell sharply, and more important the USD 600 stimulus checks were dispersed and consumption rose instantly among low income families (so demand can be stimulated)
  - » **The Housing Market** has shown an incredible strength through the pandemic –fuelled by low interest rates and falling inventories. Interest rate expectations have come up lately, so perhaps sales will flatten/fall? Start/permits are expected marginally down too
  - » Manufacturing production is expected sharply up – and the first Feb surveys to signal further growth
- **EMU**
  - » **Manufacturing Production** probably fell more than expected due to a partial reversal of the 50% hike in Nov
- **UK**
  - » Possible downturn in **Retail Sales** as tighter restrictions were imposed in early January.
- **Norway**
  - » **What will the Oil Companies say?** We expect them to revise their 2021 **investment forecast** further up, following the leap in the Nov survey. The first 2022 f'cast is unreliable as just spending on projects that have sent their plans to the government (PUD) is included. The oil companies are strongly incentivised to apply before end of next year, and spending will incur before that but not counted in this survey. The investment survey for the **Manufacturing** sector, as well as **Power Supply** will be published. They have been weak lately, we expect somewhat of an improvement
  - » We do not expect **Norges Bank's governor Olsen** to signal any changes in the monetary policy outlook in his annual address – but he may sound some optimism on the behalf on the outlook Norwegian economy out of the corona crisis?

Sources: Bloomberg. SB1M est. in brackets. Key data points are highlighted, **the most important in bold**

Highlights

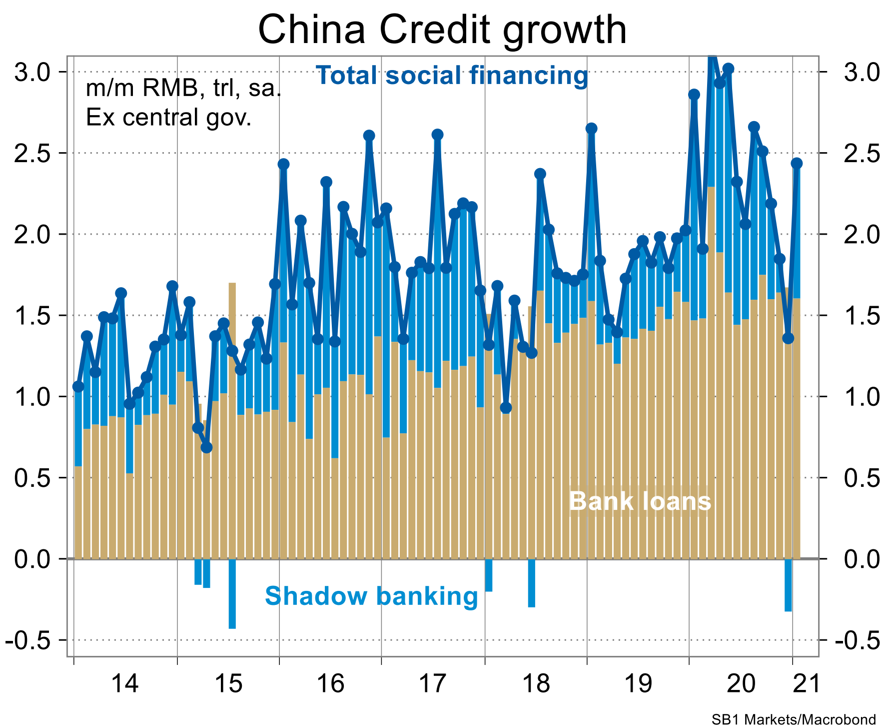
The world around us

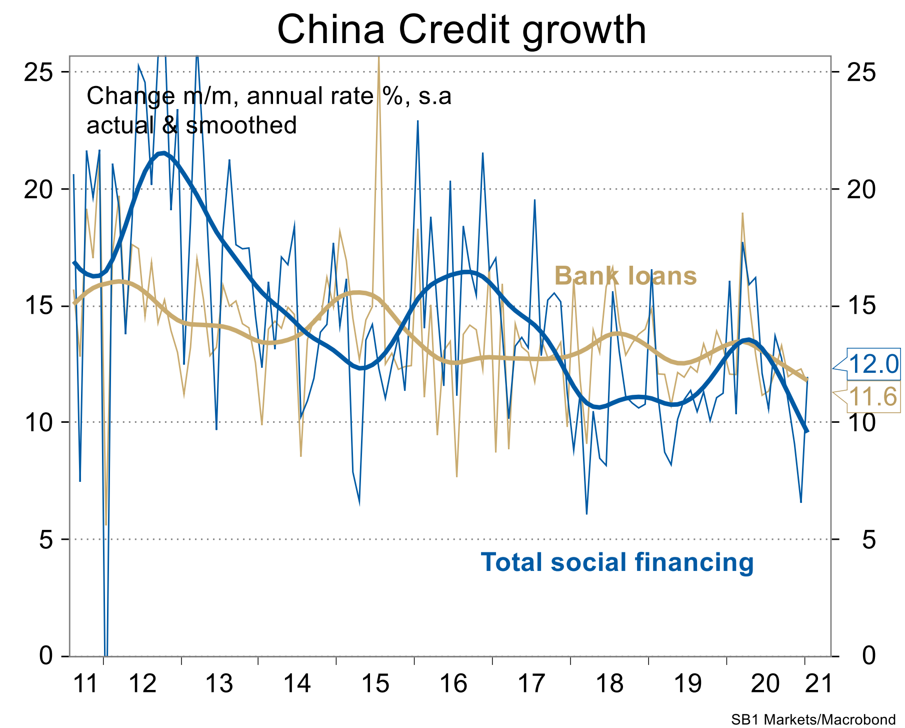
The Norwegian economy

Market charts & comments

Credit growth accelerated in January

Trend may be down, but growth in shadow banking rebounded





- In Jan credit grew at a 12% rate (m/m, annualised). Smoothed, the underlying rate may be some 10%, down from 13% during the spring (and >15% during some months). A 10% growth rate is most likely above trend growth in nominal GDP
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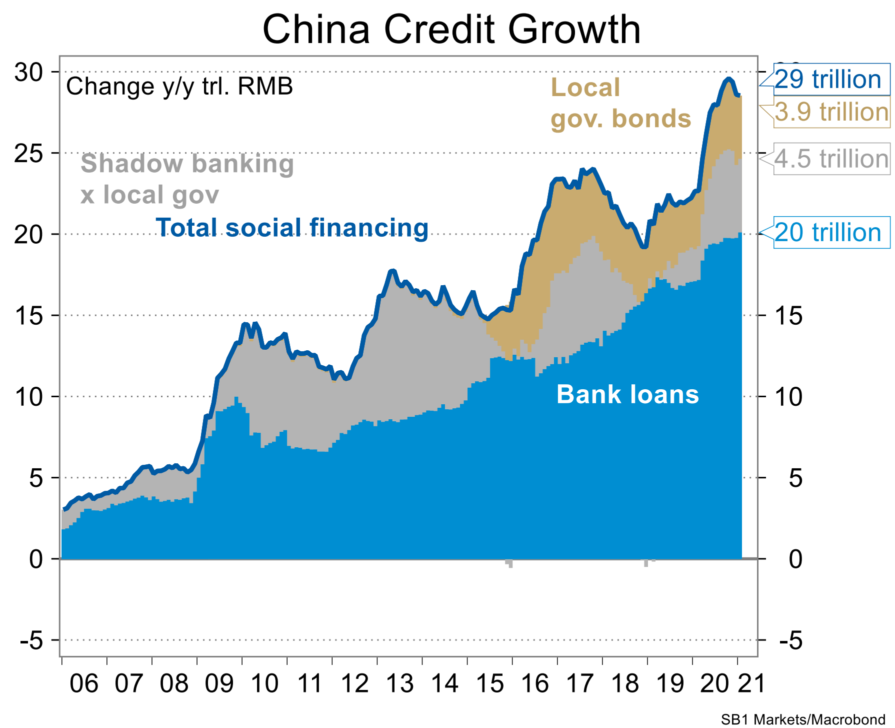
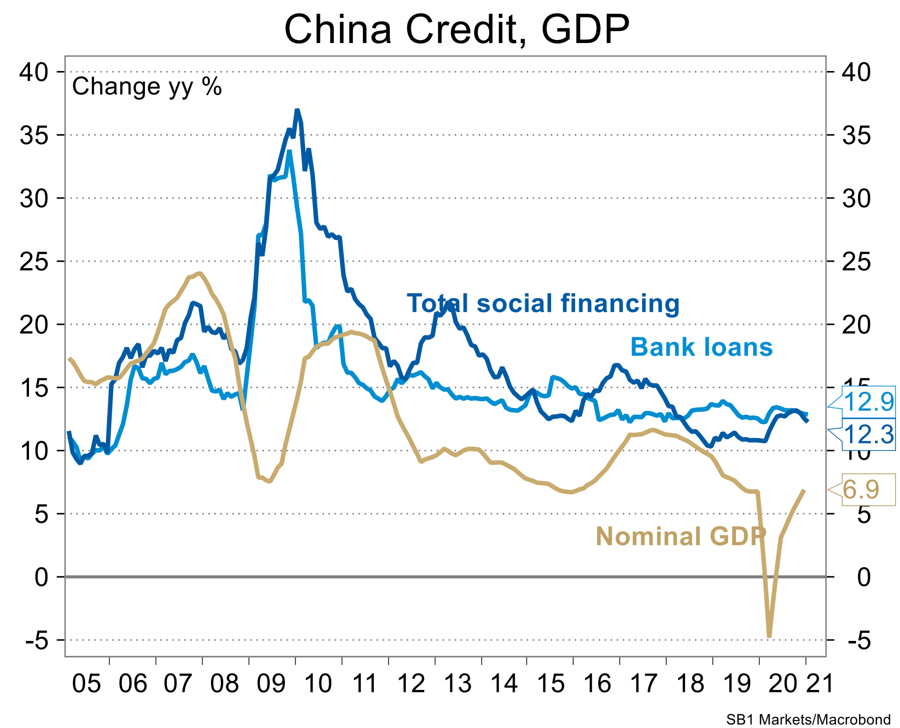
  - » Bank loans rose by 1.6 trl, and growth is slowly slowing. Actual lending rose by 3.6 trl, expected 3.5 trl. Shadow banking credit rose by 0.8 trl, more than 1/3rd of the total
- Total credit is still up 12.3% y/y, substantially above normal income growth – but this is just due to the rapid credit expansion in H1, when authorities opened up the gates to support the economy after the corona crisis
- Now, the authorities are trying to calm credit markets down. They no doubt acknowledge that the debt/GDP ratio already is dangerously high. **Still, they do not want to strangle the economy – which the strong January data signals!**

Credit growth curve shows signs of flattening

… but growth is still not low

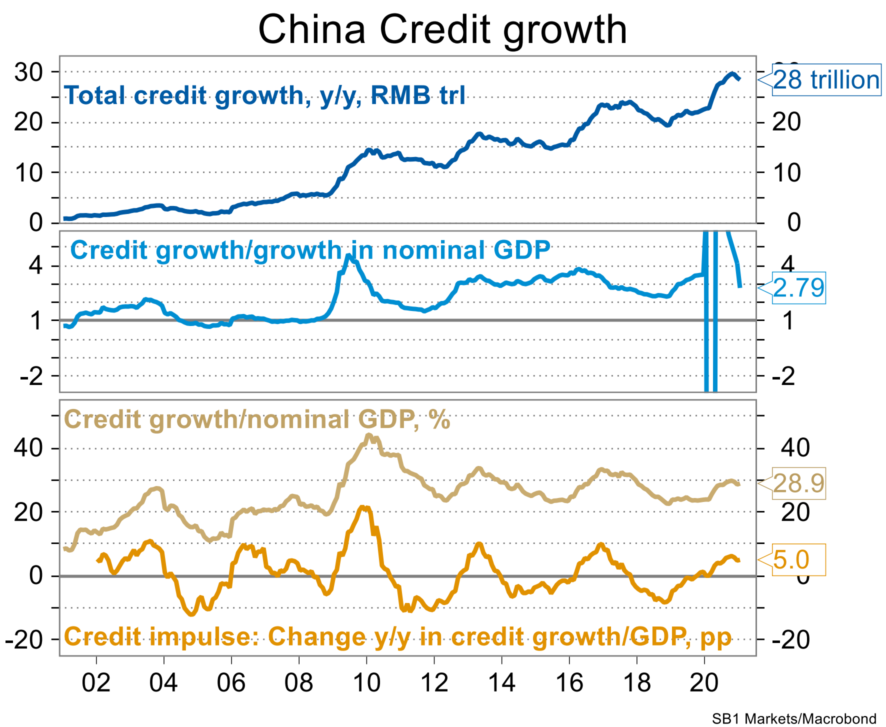


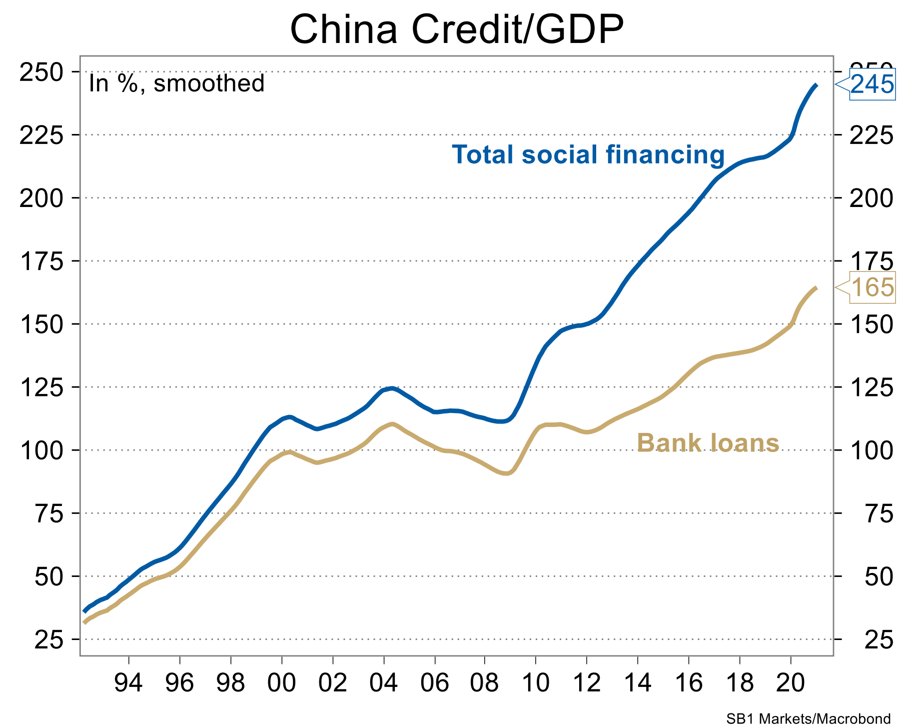


- Over the past year, total credit has expanded by CNY 29 trl, equalling 25% of GDP (even before the Q1 '20 collapse)
- Banks supplied CNY 20 trl of the y/y increase
- Local governments have not yet accelerated their borrowing by much, at least not in the bond market, still up 3.9 bn y/y
- Other credit – via the shadow credit market x local gov bonds is still up
- Total credit growth at 12%+ is well above trend nominal GDP

The credit impulse has peaked – but far from in tightening mode

A moderate pressure at the brake pedal is reasonable, given strong growth and a high dept/GDP ratio

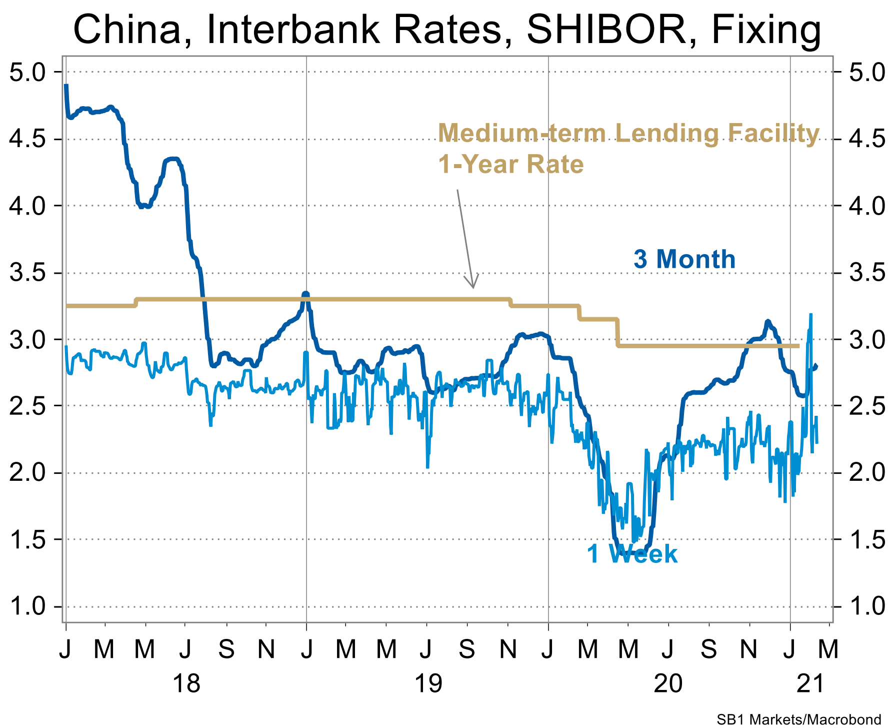




- A positive credit impulse implies that the credit growth/GDP ratio is increasing (the 2nd derivative of credit vs the GDP level)
  - » A negative credit impulse indicates credit tightening (or weaker demand) and has been associated with slowdowns in the Chinese economy
- The credit impulse has been in the positive territory since late 2019, but may be peaking – credit growth is slowing
  - » That's not surprising given signals from the authorities, and no need for keeping growth at the 11 – 12% GDP growth pace through H2, taking GDP up to above the pre corona GDP trend path! A mild credit slowdown is just what is needed!

Interest rates may be on the way up…

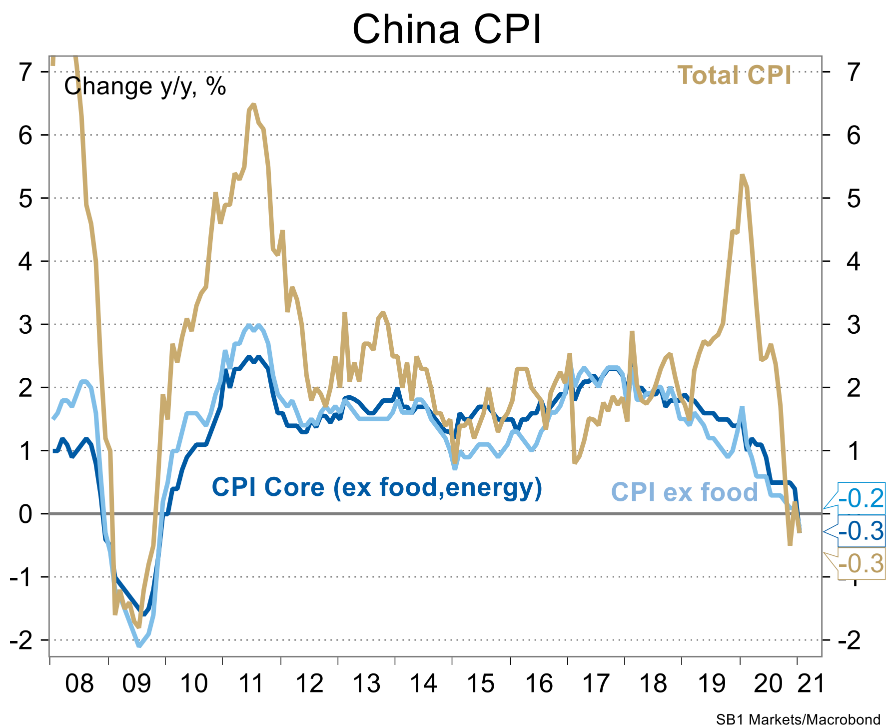
…but the spike in very short term rate was not a signal – and now rates have normalised

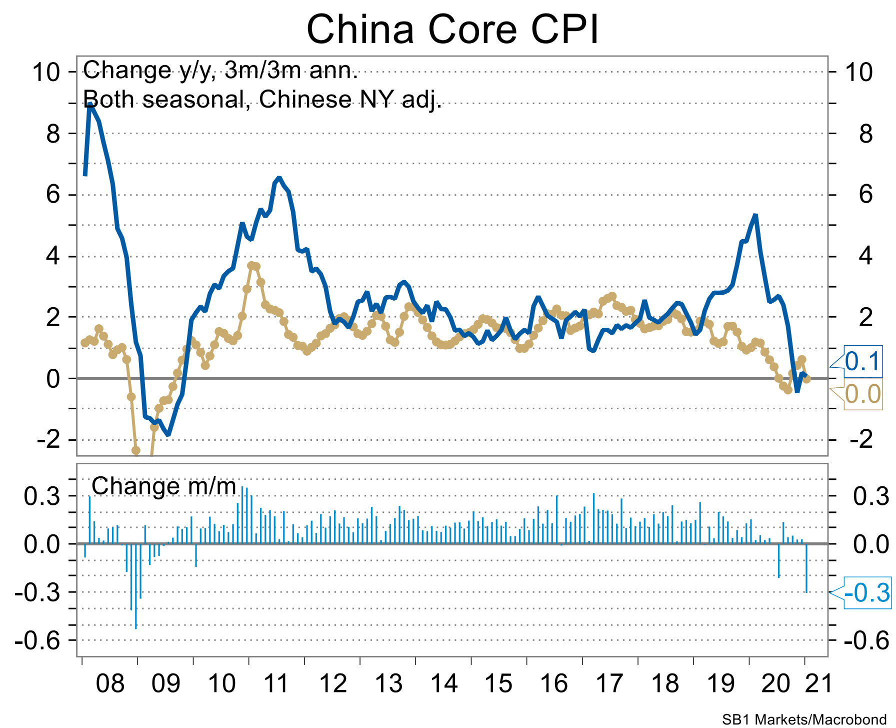


- Sure, interest rates have recovered sharply following the sharp reduction in early 2020, as a response to the corona crisis
- Authorities have tighten credit policy, and credit growth has calmed down
- Still, the 100 bp rise in 1w money market rates (and even more for O/N rates) was not a monetary policy signal – and rates have normalised thereafter

Deflation in China? Yes, and that's just fine!

The headline CPI y/y down 0.5 pp to -0.3%. The core fell 0.3% m/m, and is up just 0.1% y/y

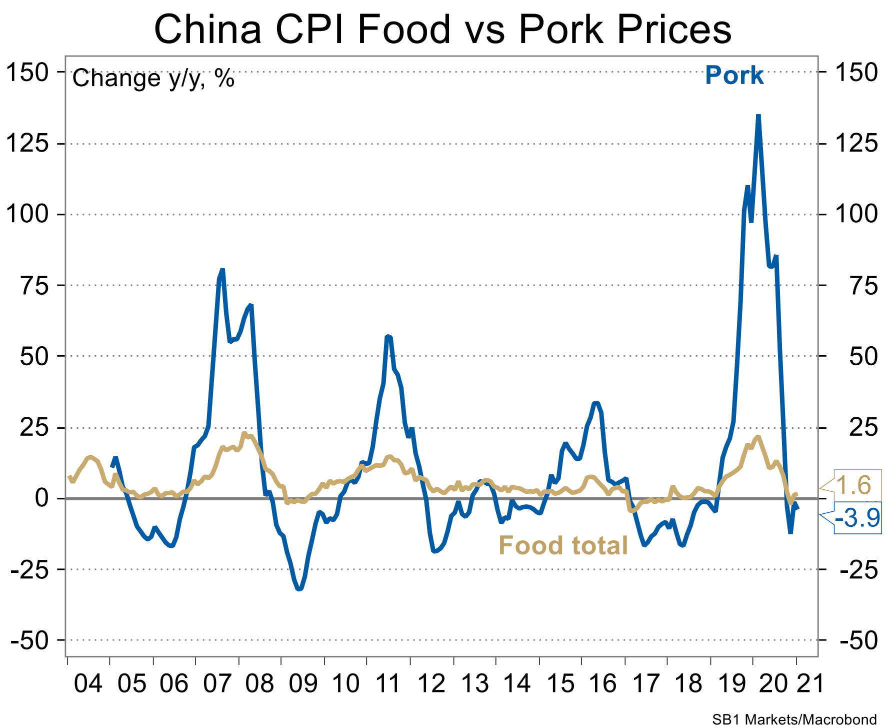


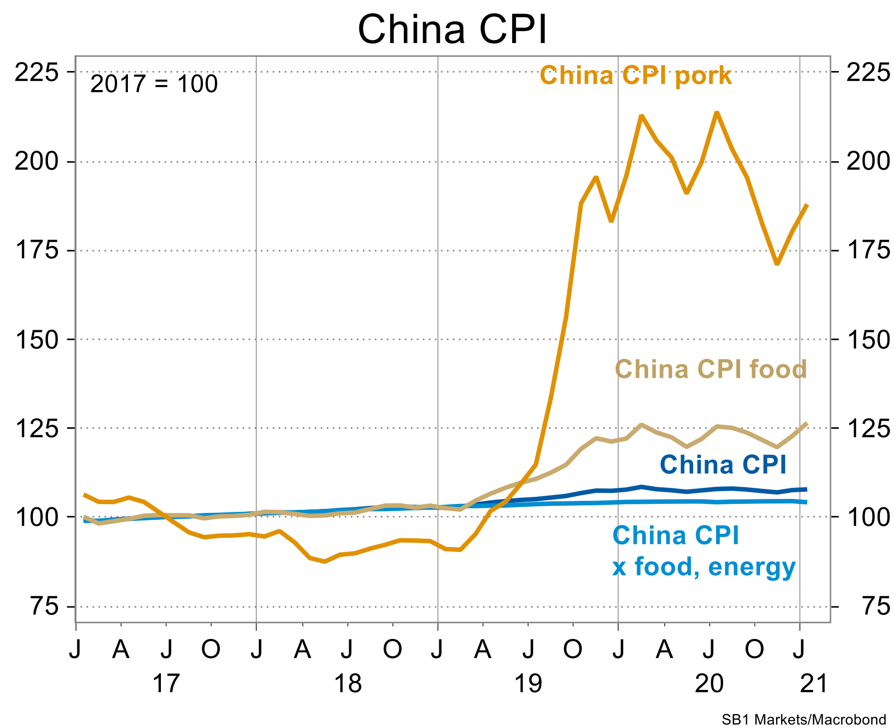


- **Total annual CPI** growth has fell from above 5% in early 2020 to -0.3% in Jan, expected -0.1%. The steep decline in headline CPI is due to a partial reversal of the ultra high pork prices last year. In January, they did contribute on the downside. The timing of the Chinese New Year contributed to 0.4 pp to the annual growth rate, the adjusted rate was +0.1% y/y
- **Food prices** rose by 3.0% m/m as pork prices rose 4%. Food prices are up 1.6% y/y. However, the latter is trending down following the 130% price increase due to the 'pig massacre' (swine flu), and prices are still up almost 100%, and will probably continue down substantially over time
- **The core, ex food & energy price index** fell by 0.3% m/m, and are just up 0.1% y/y (New year adj., -0.3% before adjustment)
- **Low inflation** support real income growth. **Monetary policy** will not respond at low inflation per se, the real economy is more important

Pork prices down 4%, still far above a normal level

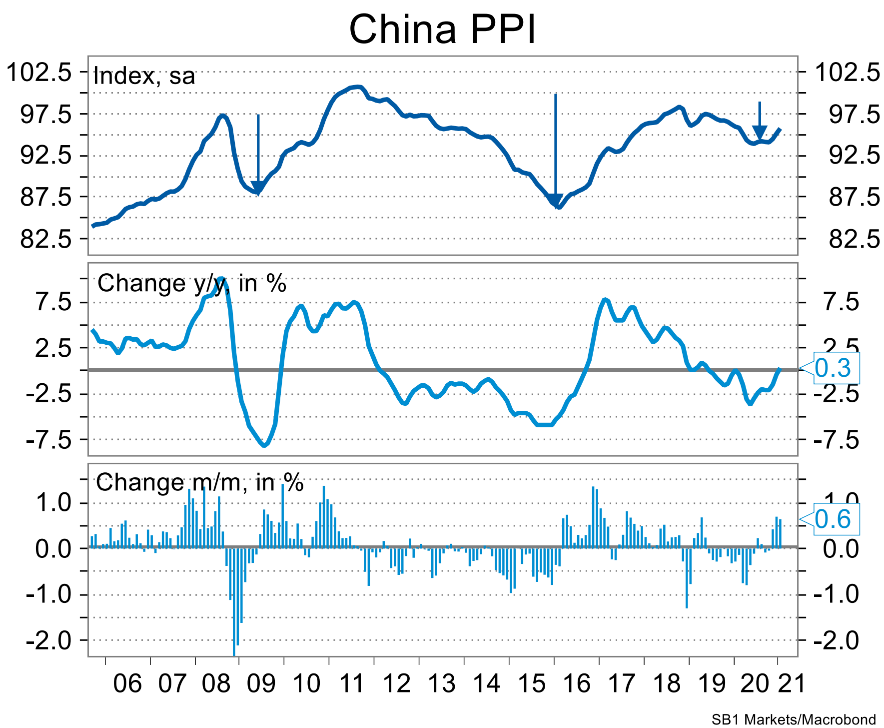
Pork prices will most like decline substantially, taking both overall food prices, and the total CPI down

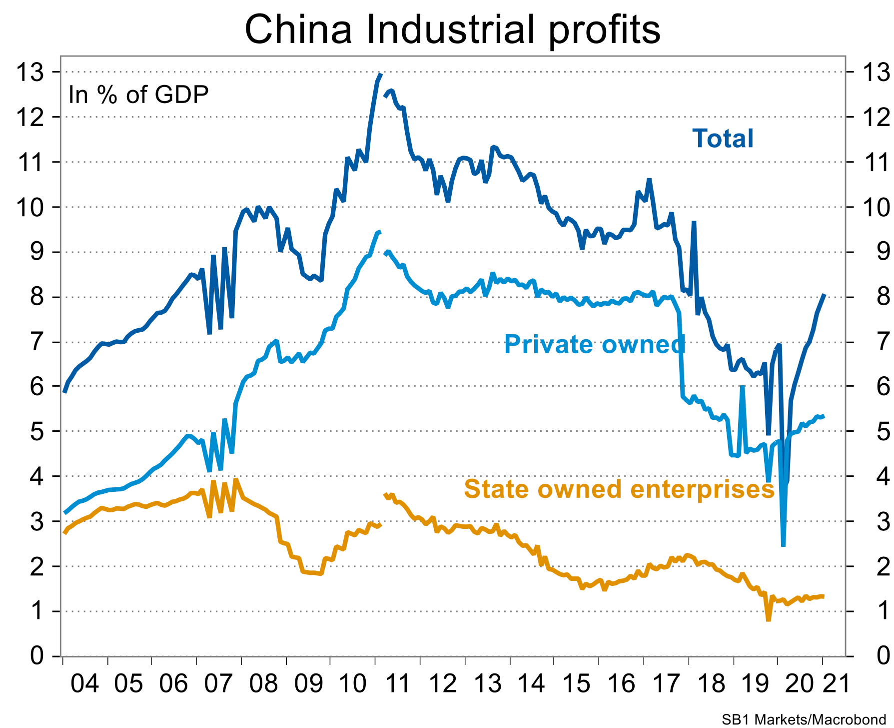




Producer prices have bottomed, profits on the way up again too

PPI up 0.6% m/m in Jan, up 0.3% y/y – was down almost 4% last May. Profits are recovering

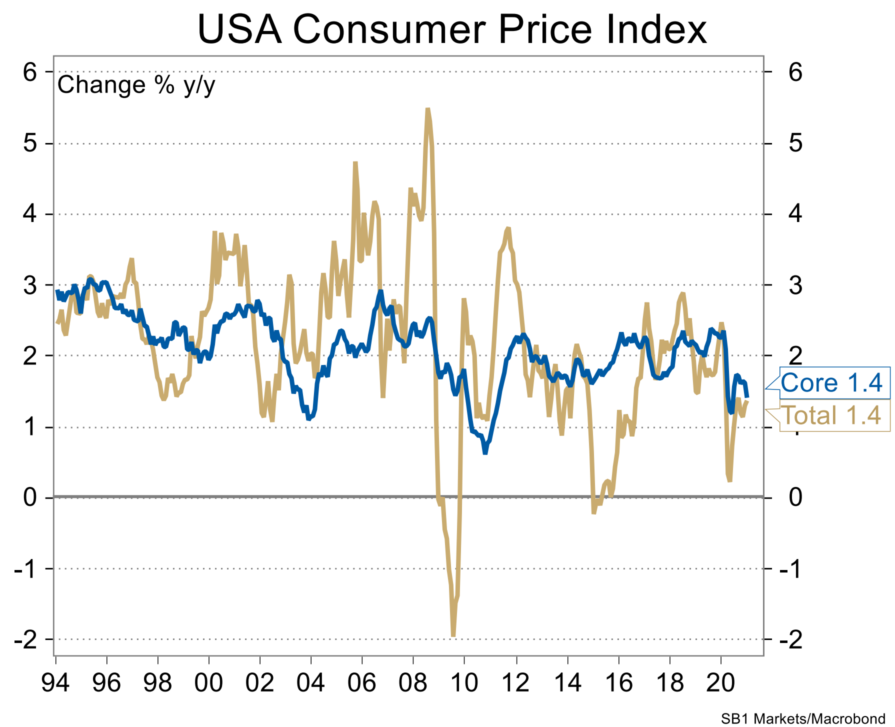


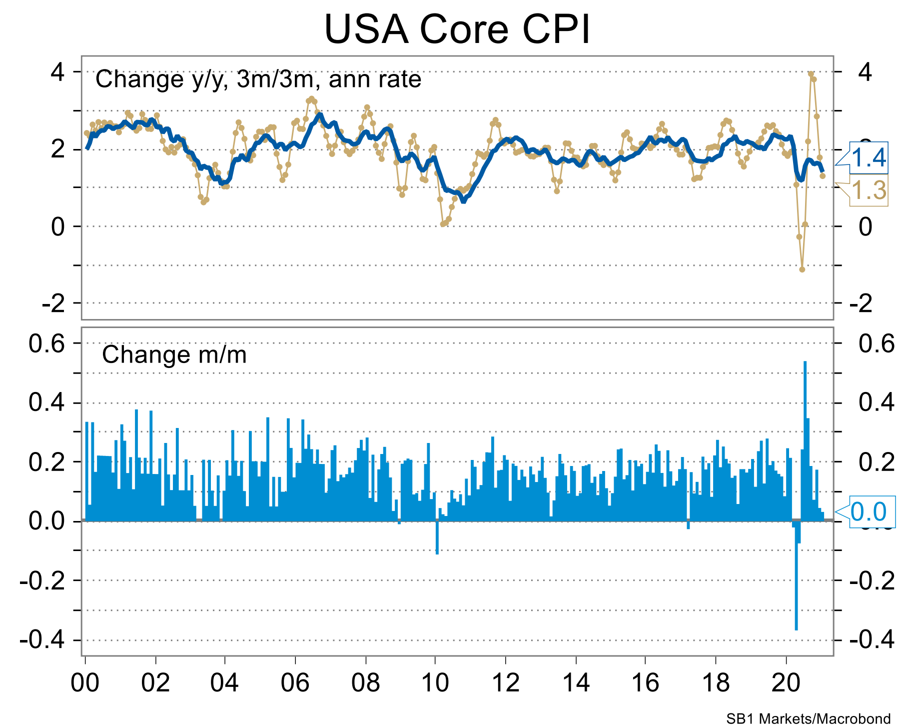


- The **PPI** peaked in late 2018 but prices just fell some 4%, some of it during the spring. During previous setbacks, PPI has fallen up to 13% (and never less than 8%). Prices are not much up y/y, but the change will be felt all over the world
- **Profits in privately owned industrial enterprises** 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 – and now it has climbed to 8%!
- **In state owned enterprises profits** have fallen from 2% in 2018 to just above 1% now – but the profit rate has slowly increased since last summer

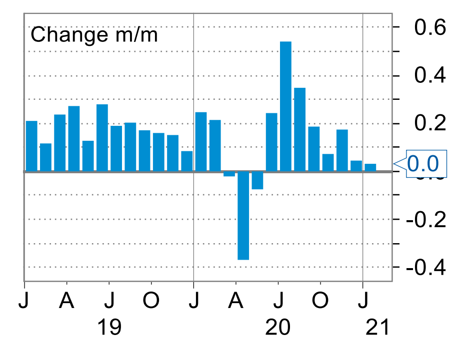
Inflation currently not a problem: Core CPI ticked in at 1.4%, below consensus

…while headline prices rose 0.1% to 1.4%



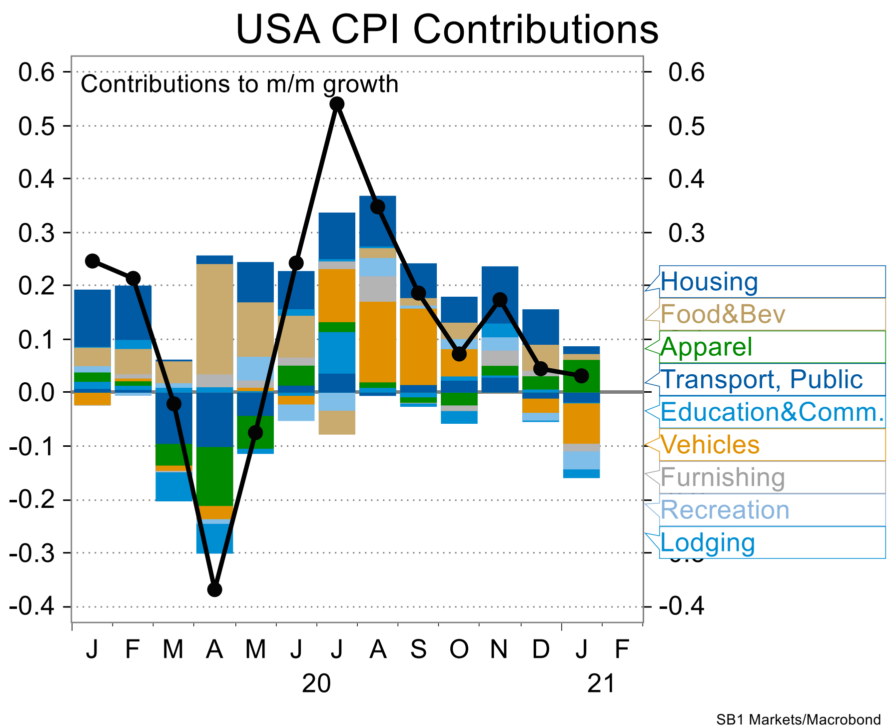


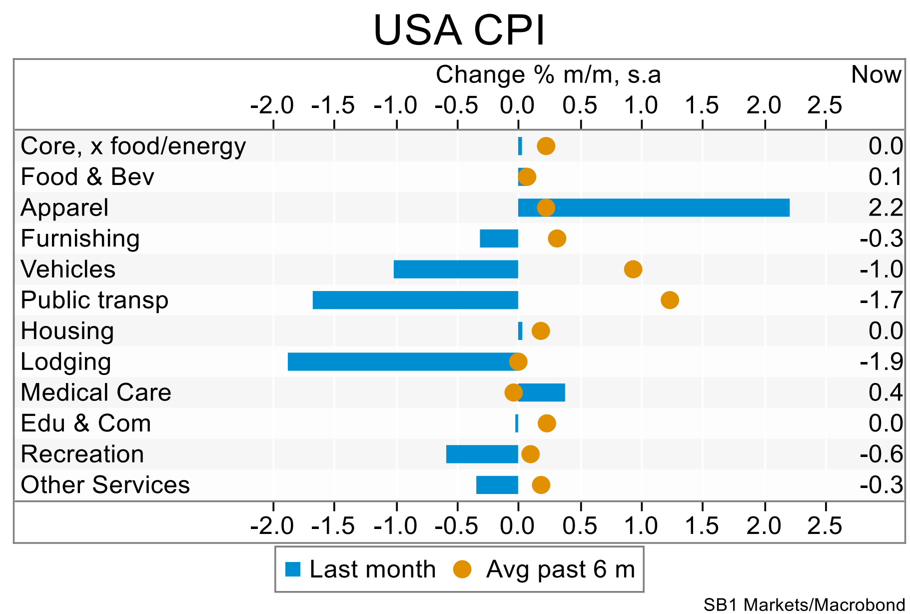
- The annual core rate came down to 1.4% (exp. unch at 1.6%), and is well below the 2.4% pre-corona level, and below Fed's 2% target (measured by the national account PCE price deflator, which over time has reported an inflation rate 0.2 – 0.3 pp below the CPI inflation rate)
- Headline CPI rose to 1.4% y/y; up from 1.3% in Dec, due to higher gasoline prices. In May, headline CPI was up 0.2% y/y
- Vehicles, lodging and airline ticket prices saw the biggest decline from previous month
- Going forward, base effects (prices fell sharply last spring) will bring the annual rate sharply up



Clothing prices up 2.2% in January, but car prices are falling!

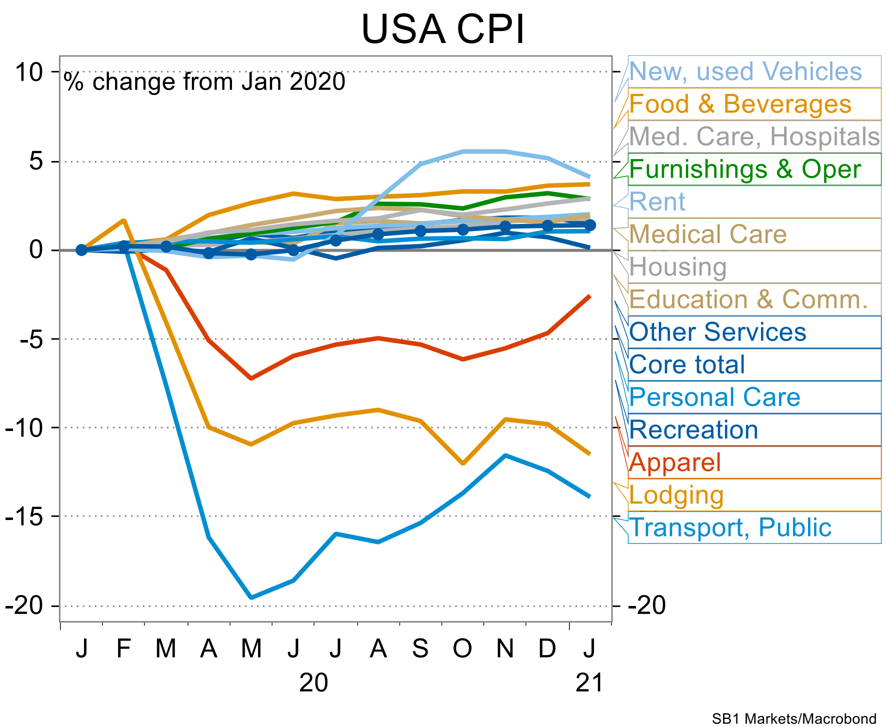
The prices of airfares, lodging, furnishing and recreation also on the downside in Jan

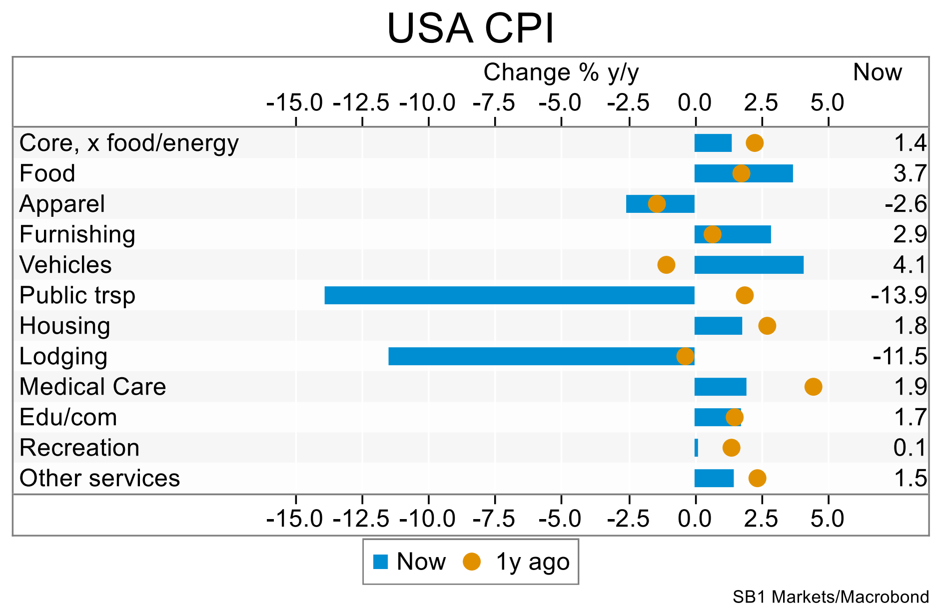




Clothing, hotels and transport (airline tickets) still very cheap

Public transport down -13.9% y/y, (airline tickets) and hotels -11.9%! At one stage…

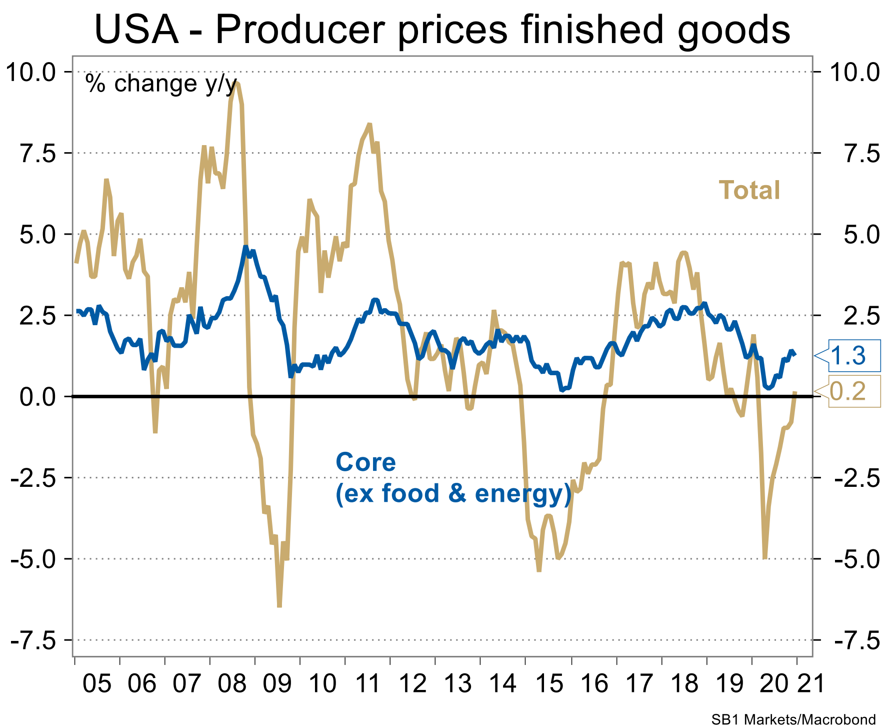


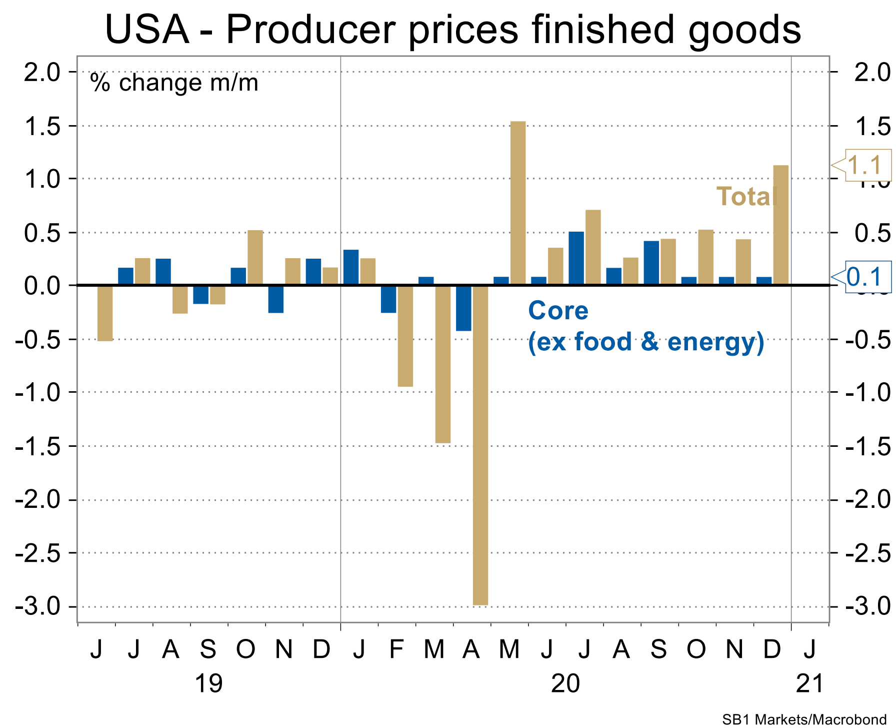


- Just some few components of the CPI contributed to the 'corona' setback: Public transport (airline tickets), lodging (hotels), apparel, and partly recreation (cinemas, parks etc). Most other components of the CPI have not slowed
  - » In 2 – 3 months these prises will be flat or up y/y. In 2 – 3 more months, these prices will most likely be up y/y, as the country re-opens. The impact on the CPI from the negative to zero will be ¼ pp on the headline CPI, and an additional ¼ pp in if these prices normalises to pre-pandemic levels
- Food (at home) prices are up 3.7% y/y, corona has no doubt boosted demand among households, due to less eating out (as in Norway). However, global food commodity prices are rising as well
- Medical care costs are up 1.9%

Core producer price inflation slowly moving upwards but not further in Dec

Core goods up 0.1% m/m, up 1.3% y/y. Total finished goods prices up 0.2% y/y – from -5% in April

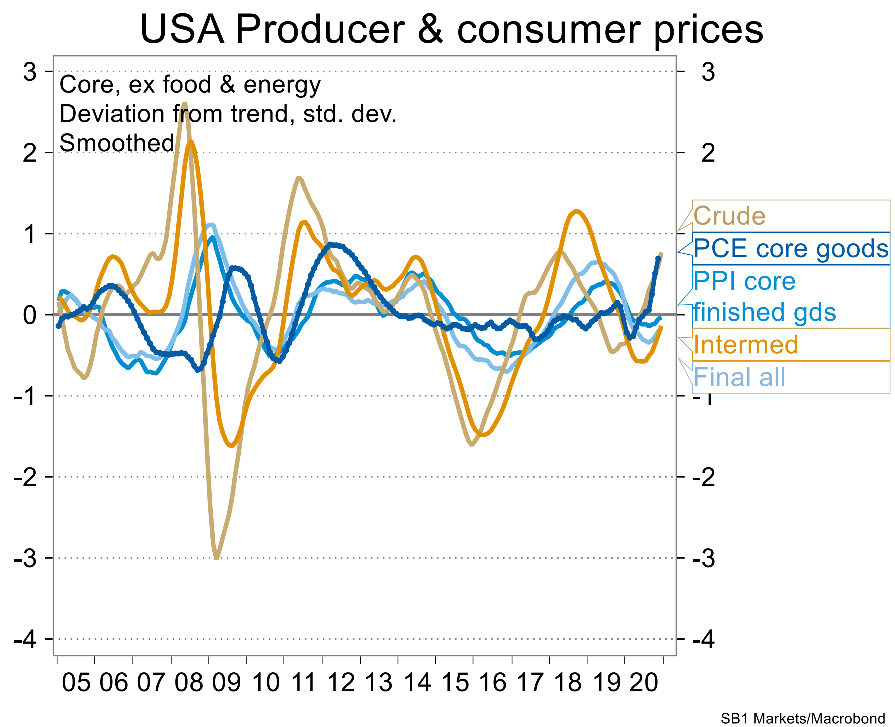


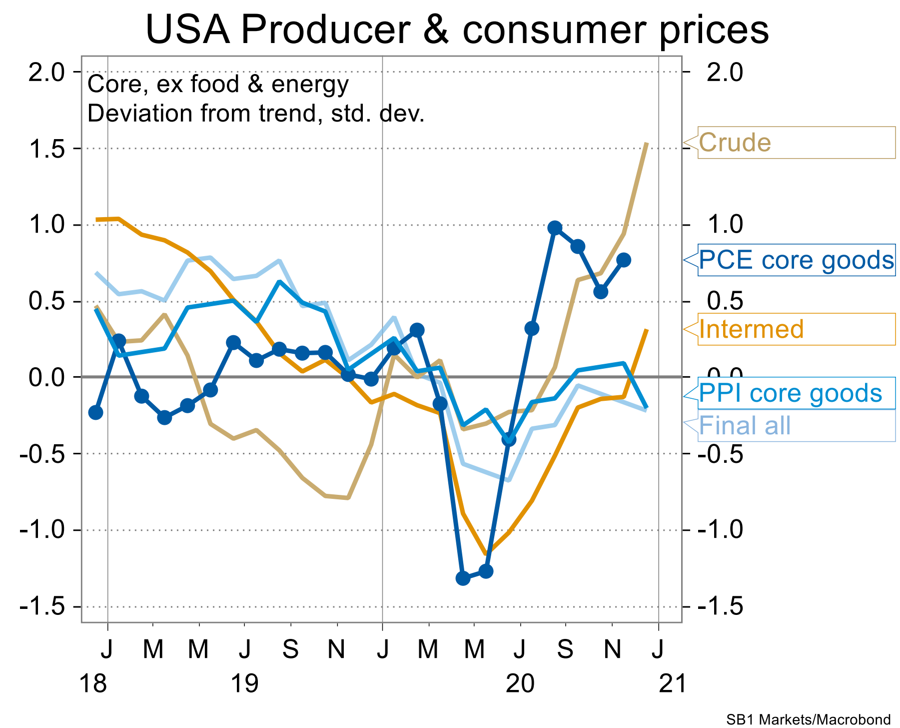


- Core finished goods x food & energy PPI rose by 0.1% m/m in Dec, as in Nov
- Core finished goods producer price inflation does not suggest high CPI inflation, but producers prices at earlier stages are now moving upwards
- Headline PPI rose 1.1% m/m, due to higher food & energy prices (and as expected). The annual rate climbed 1 pp to 0.2%

Something is brewing? Producer prices have turned up, and sharply for crude gds

Intermediate goods prices are on the way up too – confirming business surveys

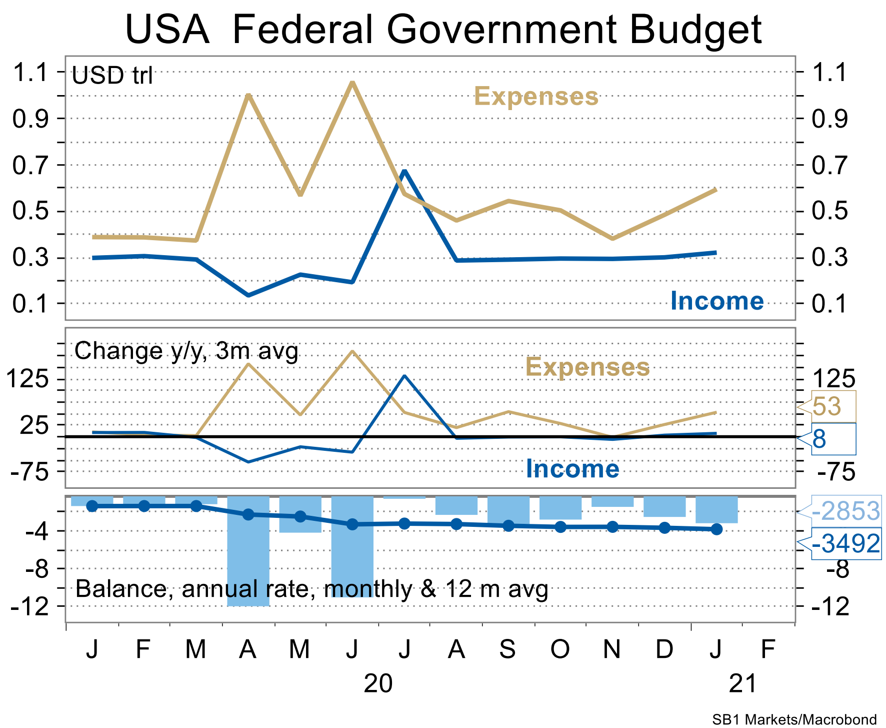


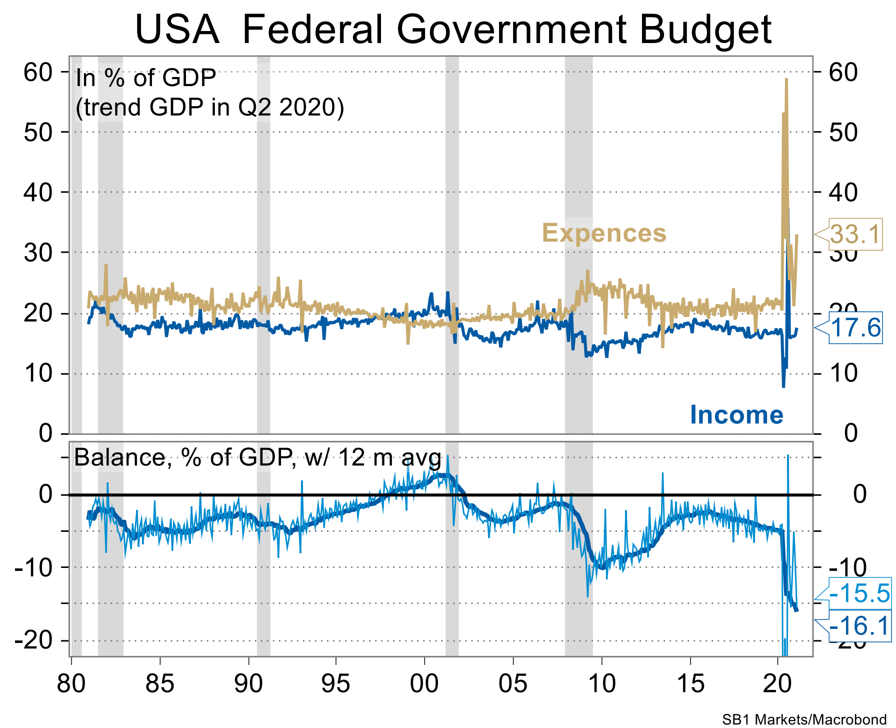


- Prices are on the way up, as are delivery times – and production is increasing rapidly. Hmm…
- However, consumer prices are rising faster than indicated by finished goods prices. Thus, short term, probably not that much more price pressure from producer prices. Looking forward however, the steep rise in crude prices and now followed by intermediate goods prices are signalling higher consumer price inflation (crude goods are leading consumer prices by 12 months, intermediate goods by 4 months)

The Jan budget deficit up to 15% from 5%, as the (small) checks were expedited

More to come the next months, as the BIG stimulus package is not yet decided

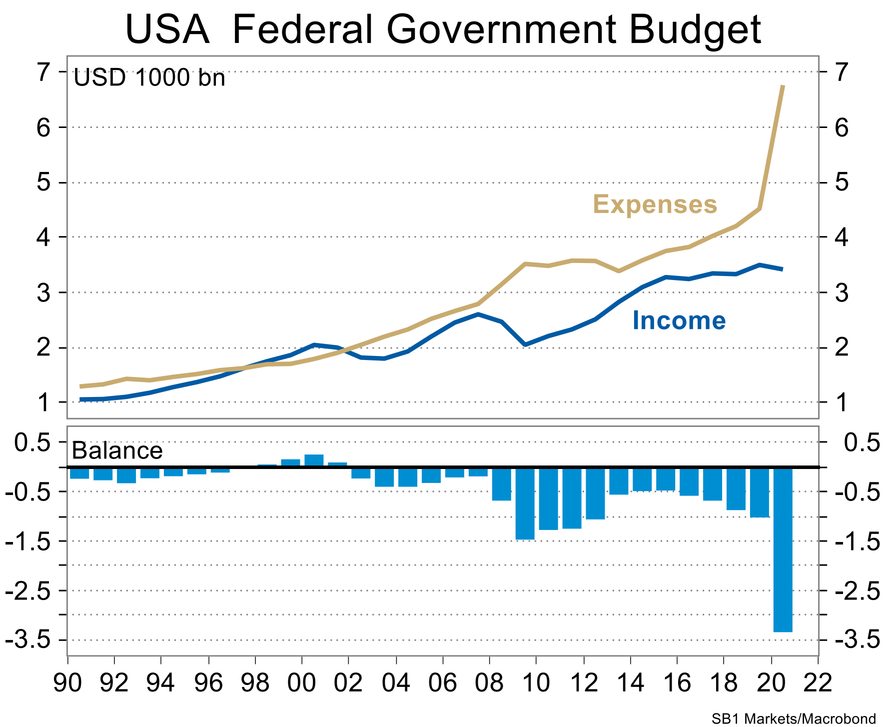




- **Federal expenses** rose by almost USD 300 bn in January (up 53% y/y ☺), as part of the 1st stimulus package at almost USD 900 (equalling 4% of GDP) was disbursed - the USD 600/person cash support (for persons with an annual income below USD 75'). Other payments will probably take longer time to execute
  - » Biden has proposed a 2nd stimulus package at USD 1.900 (9% of GDP). The bill is not decided in the Senate. Most likely, the amounts will be reduced – and some tax increases will come – <u>but the budget deficit will 'explode' – in an economy were lack of demand is not the problem</u>
- **Federal spending** equalled 33% of GDP in Jan, far higher than the 'normal' 21-22%. **Revenues** equals 18% GDP – and the <u>gap is of course huge – and expenditures are not</u>

Biden working to find support for his USD 1.9 trl (9% of GDP) package

… on the top of the USD 900 bn (4% of GDP) already decided

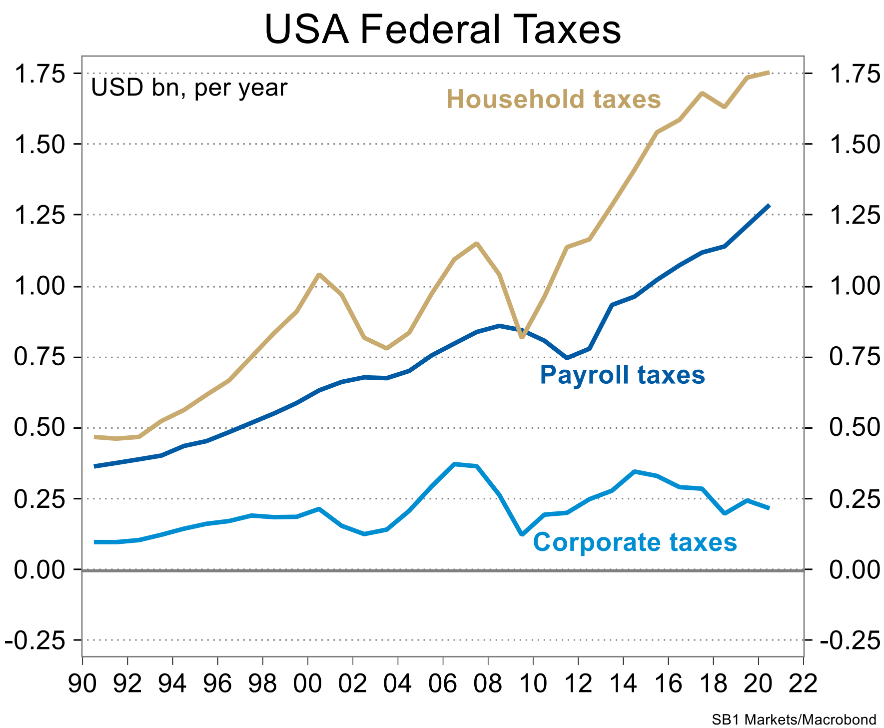


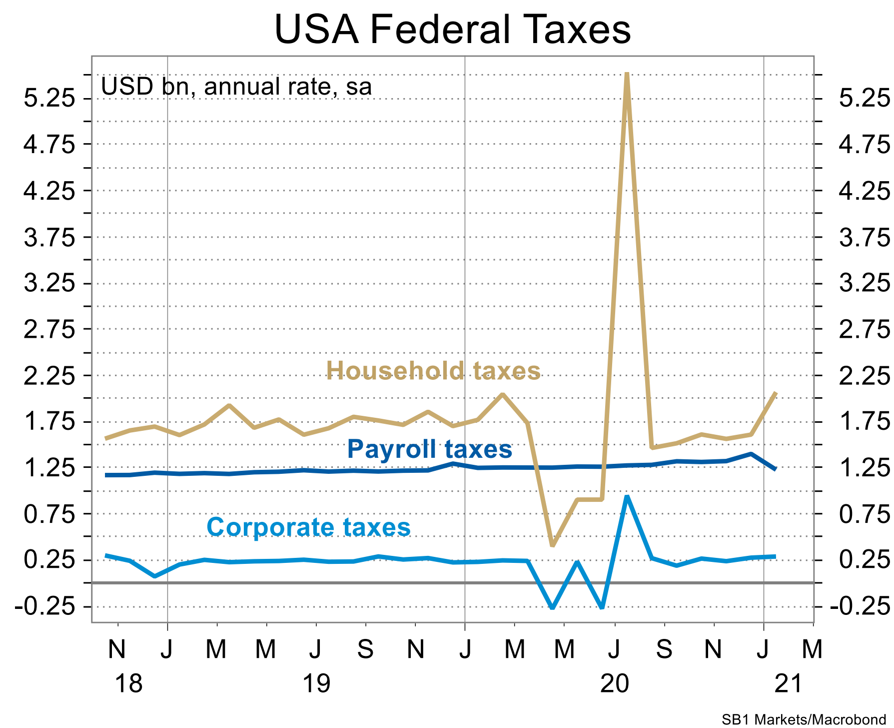
- Last year, federal expenditures rose by 2,300 bn, or 50% y/y, equalling 10% GDP
- Revenues fell marginally, due to lower corporate tax payments
- The deficit rose by USD 1,350 bn to 3,350 bn, or 16% of GDP, a new ATH
- We have not yet seen a recent estimate of the budget deficit in 2021, but it will huge, if not as large as the 2020 deficit? But it that's the outcome, it is because Bidens' proposal are not decided, and/or some revenue is found

- **What will be decided?**
  - » No compromise is so far not reached in the Senate, and it will not happen. The Biden admin will probably chose to invoke the budget reconciliation procedure
  - » However, the opposition to the generous package is increasing, even among liberal economist
  - » The amounts are plainly far too large vs. the available capacity in the US economy. Sure, activity is below par, but that' mostly due to the virus, and not due to lack of demand
  - » Support to the unemployed, paying for vaccines, helping states seems appropriate but not large scale cash income support to most Americans
- **Who will pay?**
  - » Biden's huge spending plan does not include any funding proposals. However a substantial reversal of Trumps 2018 corporate tax cuts, a clean up of favourable capital/partner taxes, and higher taxes 'on the rich' seem very likely – and can be decided by the Democratic Senate
  - » However, most of the increased spending will obviously be paid by issuing new public debt

Household taxes up 29% m/m due to timing of stimulus checks?

Both household and corporate taxes now back to a pre-corona level

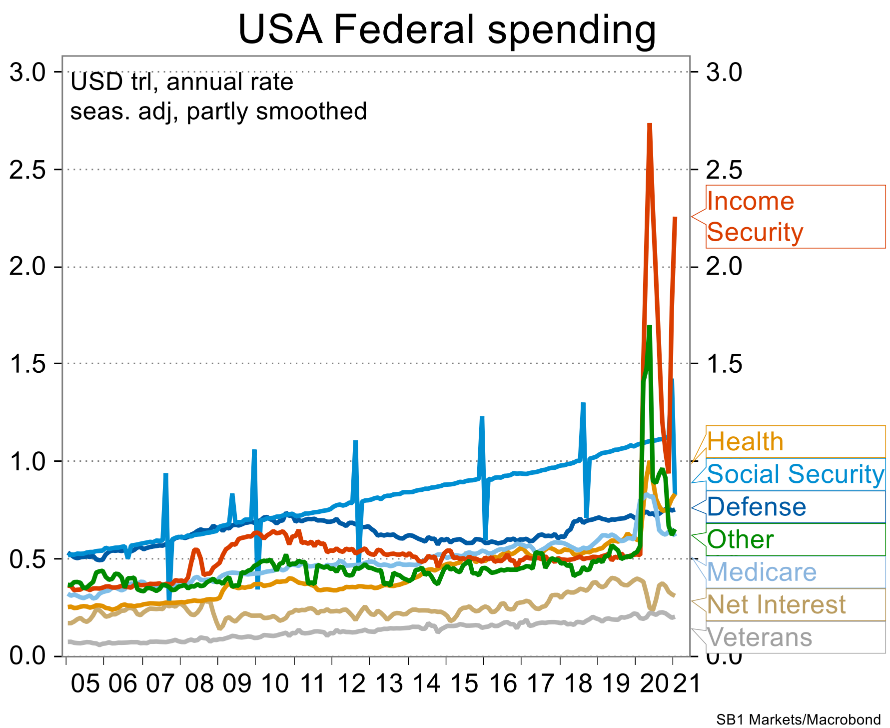


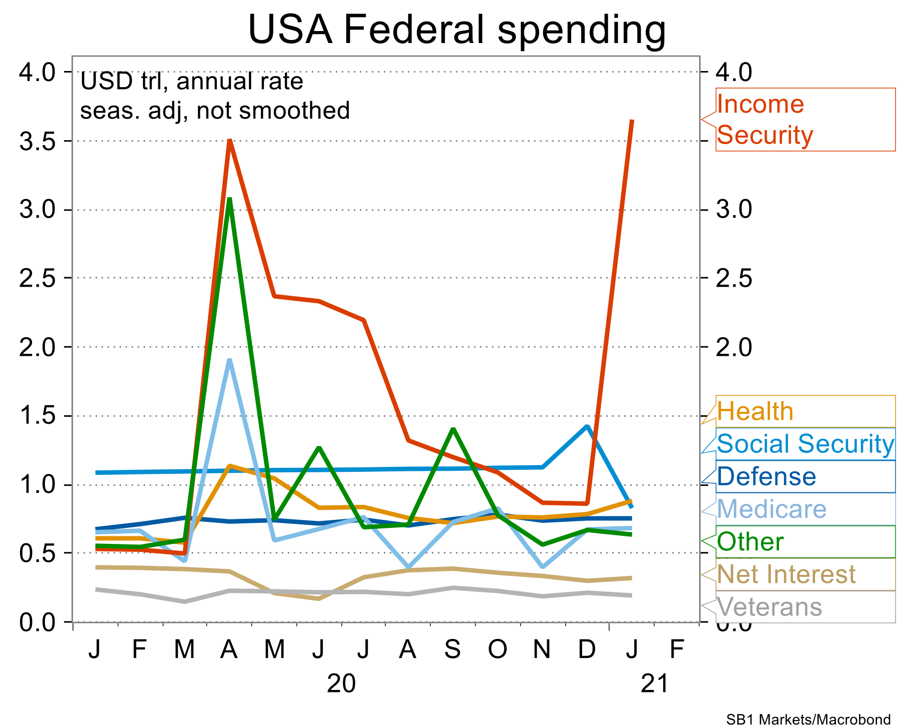


- Layoffs caused by COVID lowered payroll taxes down in Jan
- Households taxes were all over the place in 2020 due to timing of payments. Total tax payments ended slightly up but far less than income growth – and the average tax rate fell

USD 139 billion of stimulus checks sent out in January

… Another hike in transfers to households if Biden's **1.9 trl** package is approved!

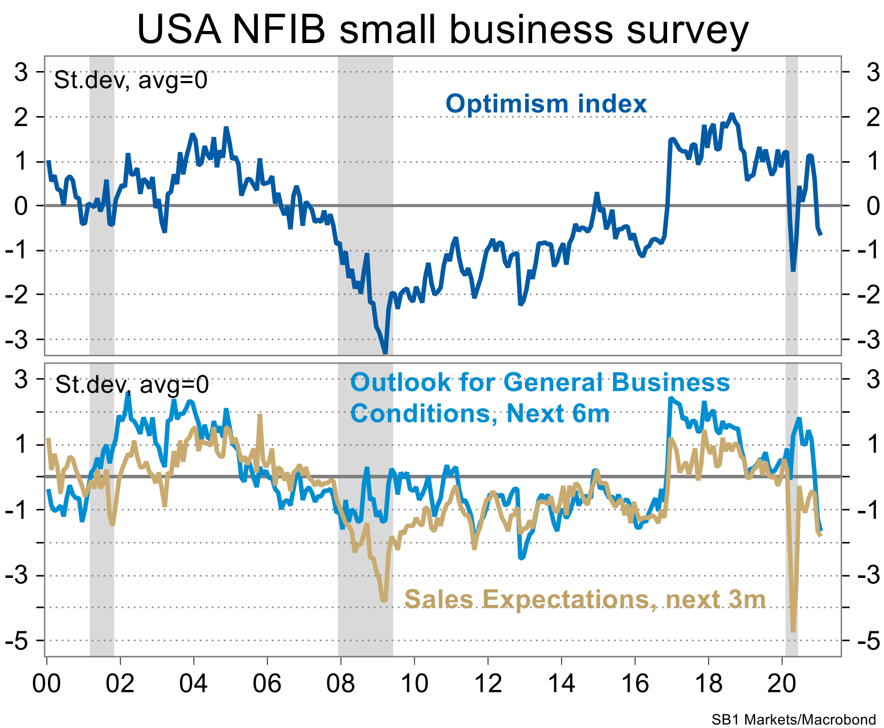


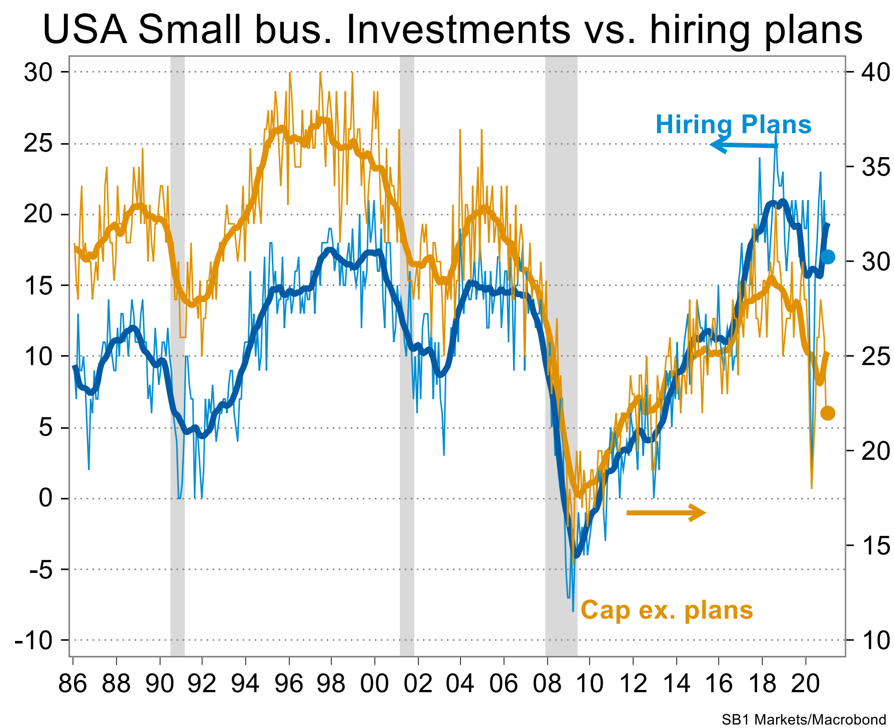


- The cost for a USD 2000/person cash support (for taxpayers + extras for dependents in the household) would, cost between USD 530-565 billion in total

Small businesses' optimism fell to 8-month low at 95 (-0.6 st.dev below avg)

In spite positive vaccine news, assessment of the outlook hasn't been more pessimistic in 8 years

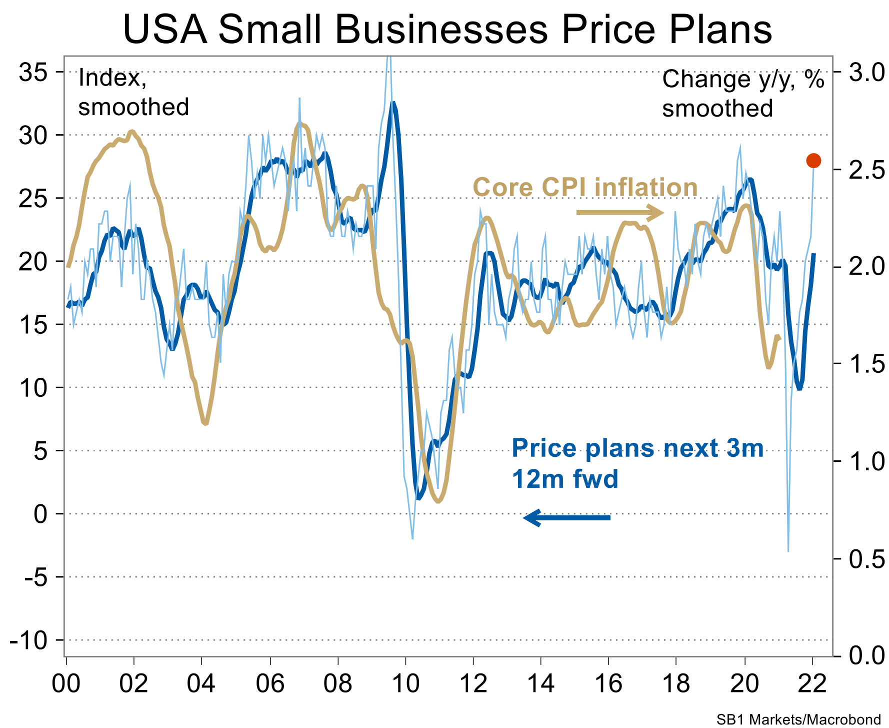


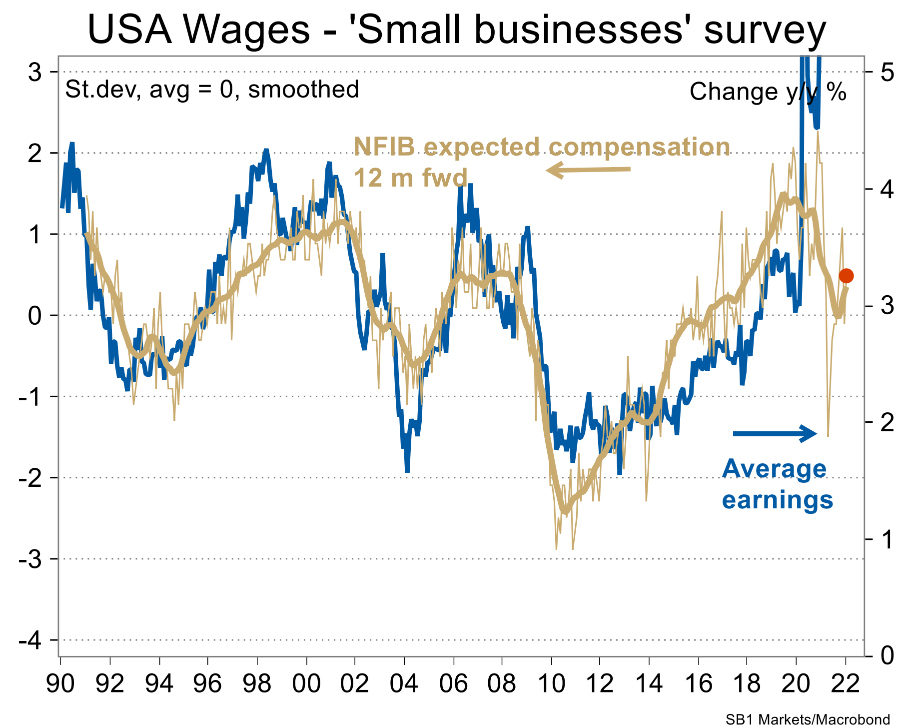


- The **NFIB optimism index** fell to 95.0 in January from 95.9 (expected up to 96.8). It's safe to assume that the latest coronavirus wave and weaker spending has influenced the opinion of small-business owners. In addition, Biden was probably not their favourite candidate for president. 4/10 components declined, just 2/10 improved
- **The expectation index**, the outlook for the next 6 months, fell for the 4th month – currently 1.65 st.dev below average
  - » Sectors: Services and professions are the most downbeat, while construction and manufacturing in the lead
- Businesses also cut back their **sales expectations** further in January, to the lowest level since 2011 (barring the March – May period last year)
- **Investment plans** remained unch from Dec, at well below an average level
- Business also did not change their **Hiring plans** from Dec, which remains at a far above average

Companies expect to lift prices sharply and to increase wages more than normal

Price expectations continued upwards (the 2nd highest in 12 ys)

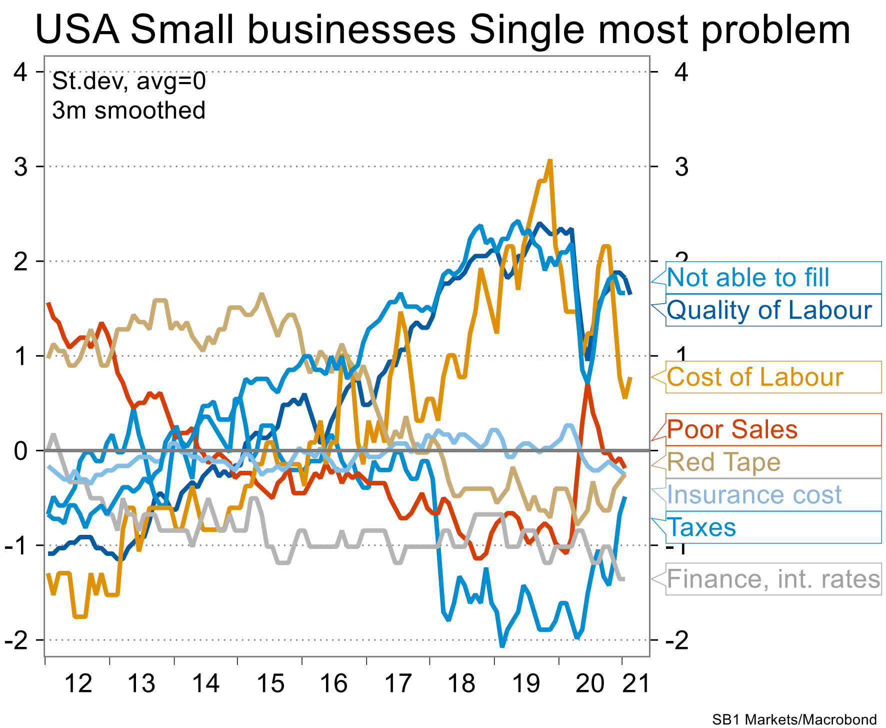


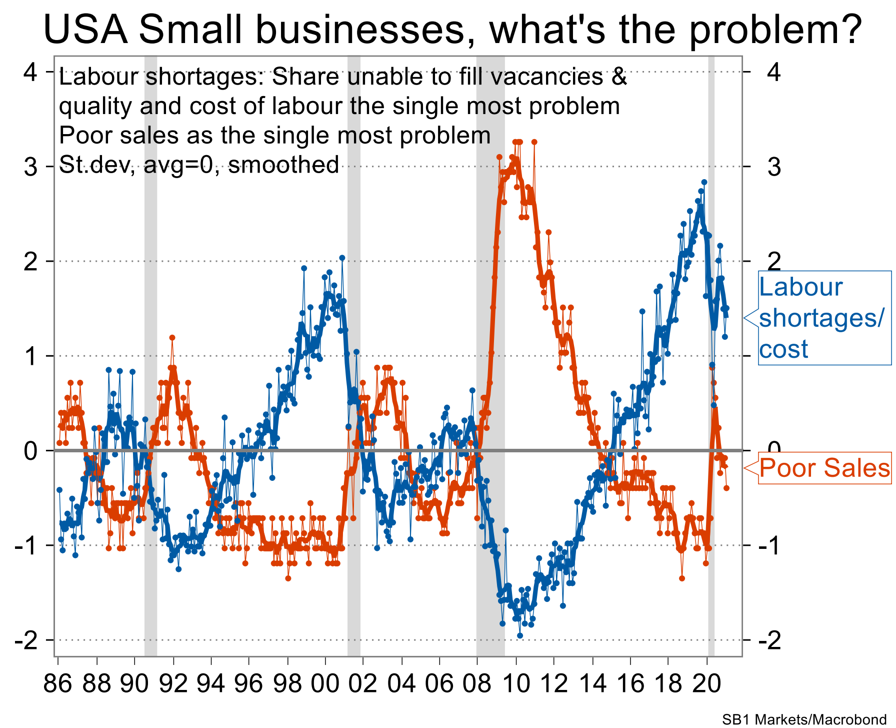


- Inflation expectations are well above the average level for the past 10 years, and higher than before corona
- The expected increases in wage compensation are at an average level in Jan (up from Dec), but has come substantially down during the corona crisis. Perhaps the most positive (or negative..?) news on wage, cost & price inflation in the US recent months?

Supply and quality of labour yet again reported as the major problems!

Interestingly, fewer than normal see poor sales as a problem. What a recession!

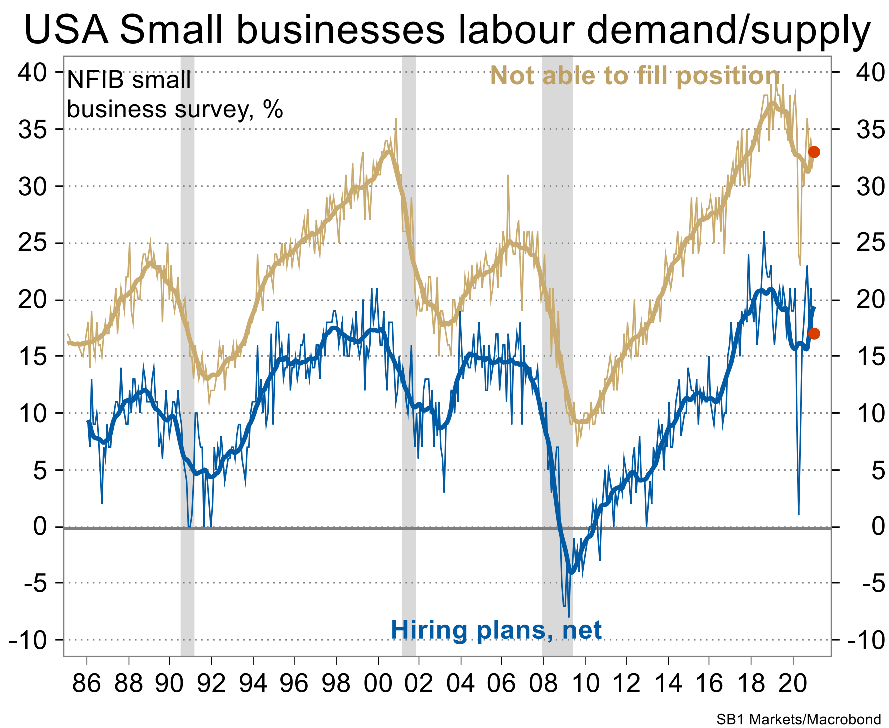


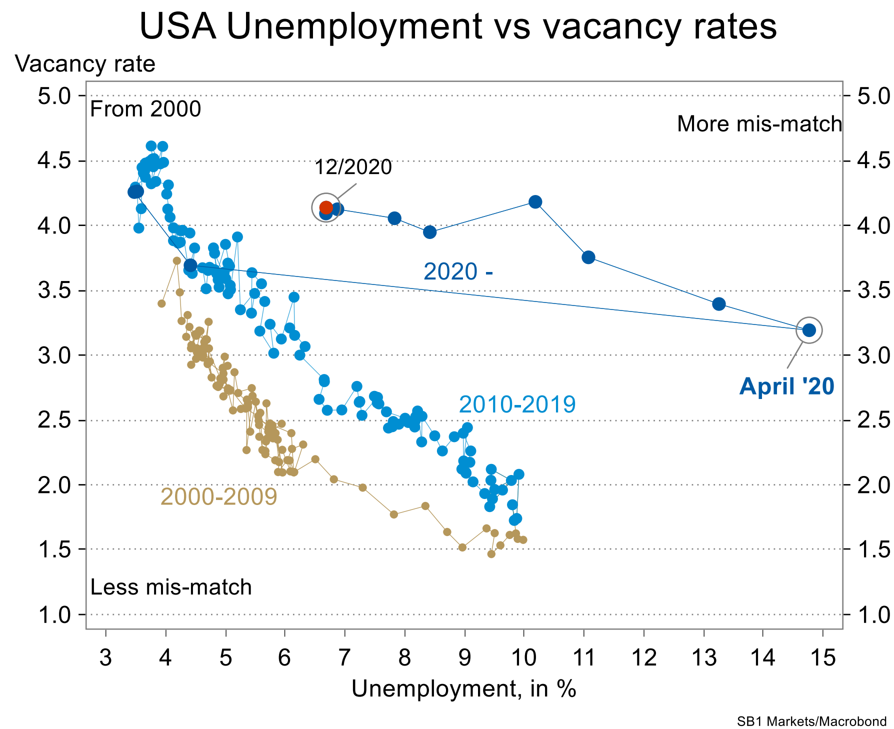


- More businesses have been stating **weak sales** as the major problem during the pandemic, but the level has been surprisingly low, and in January the level decreased and is below average!
- The share of businesses that have been noting problems with **tight labour markets** has fallen somewhat during the pandemic, but the share rose in Jan and remains at a remarkably high level
  - Both the **ability to fill vacancies**, and **quality of labour** are still reported as huge problems (2 st.dev above avg). Concern about the **cost of labour** also increased and thus remains at a higher level than normal
  - Unusually few companies are complaining about **finance/interest rates** and about **taxes** (although tax concerns increased post Biden win, so far without any taxes being increased, as far as we know)

Small businesses not able to fill vacant positions, despite a ‘higher’ unempl. rate

So much for the Beveridge curve…



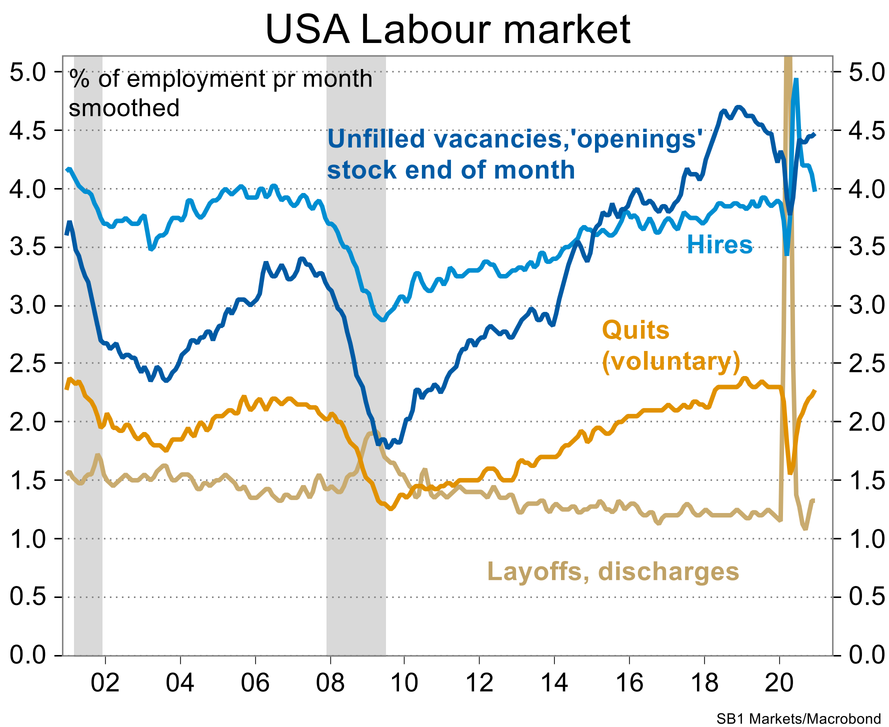


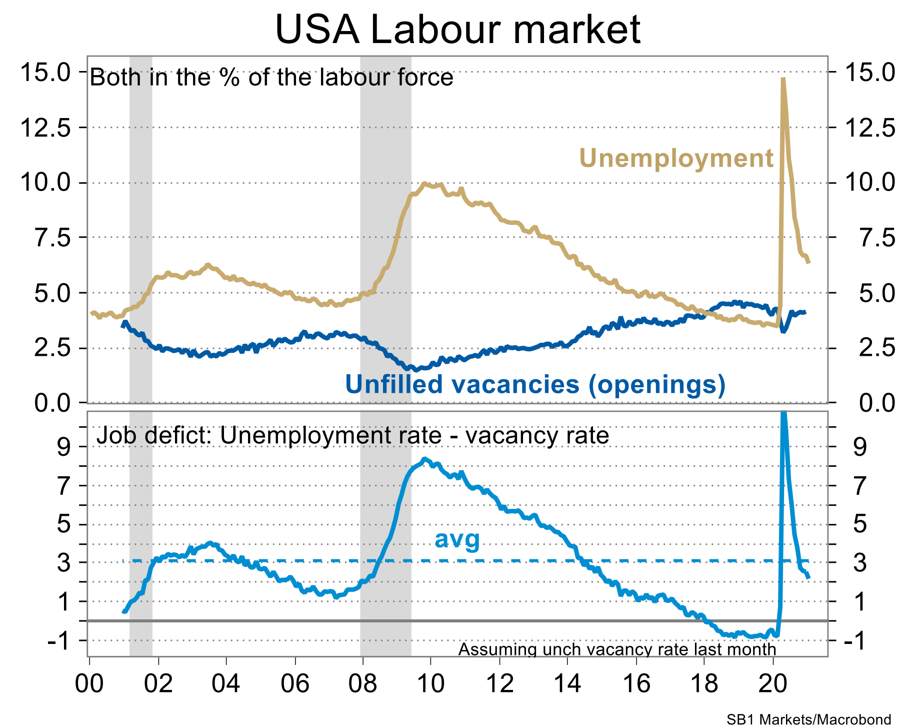
- The number of unfilled vacancies is also high, according to official statistics, *more next page*
- *Lack of transport, stay at home orders, closed schools - all due to the corona crisis - may explain that companies are not able to fill vacancies*

SpareBank 1 MARKETS

Tight labour market: Unfilled vacancies are up, and so are voluntary quits

According to the JOLTS report. Decline in hiring did not last for long, and the level is still very high

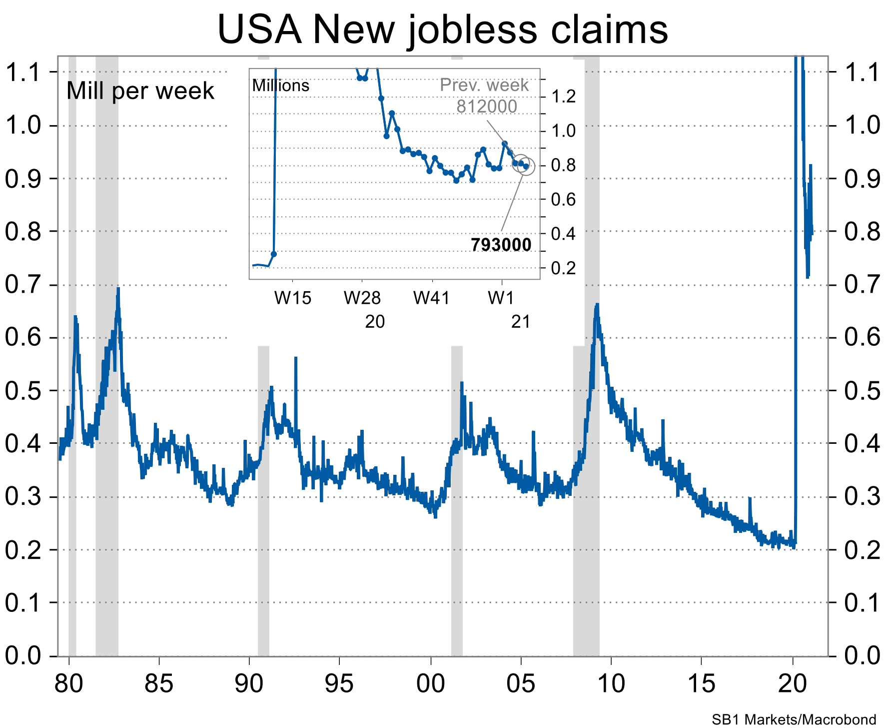


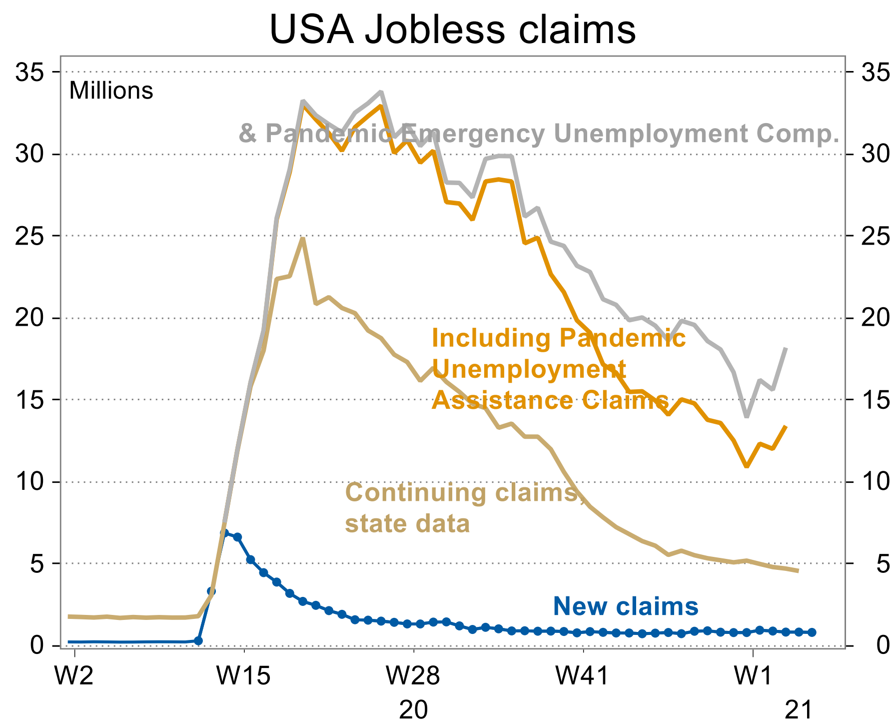


- The **difference between unemployment and unfilled vacancies** has fallen to below an average level, signalling a tighter labour market than normal (but not a really tight labour market)
- Some more layoffs in Dec but not many, at least not vs. the setback in the restaurant/bar sector

New jobless claims dipped to 793’, but still at a high level

Does not confirm a continued weakening of the labour market recent weeks

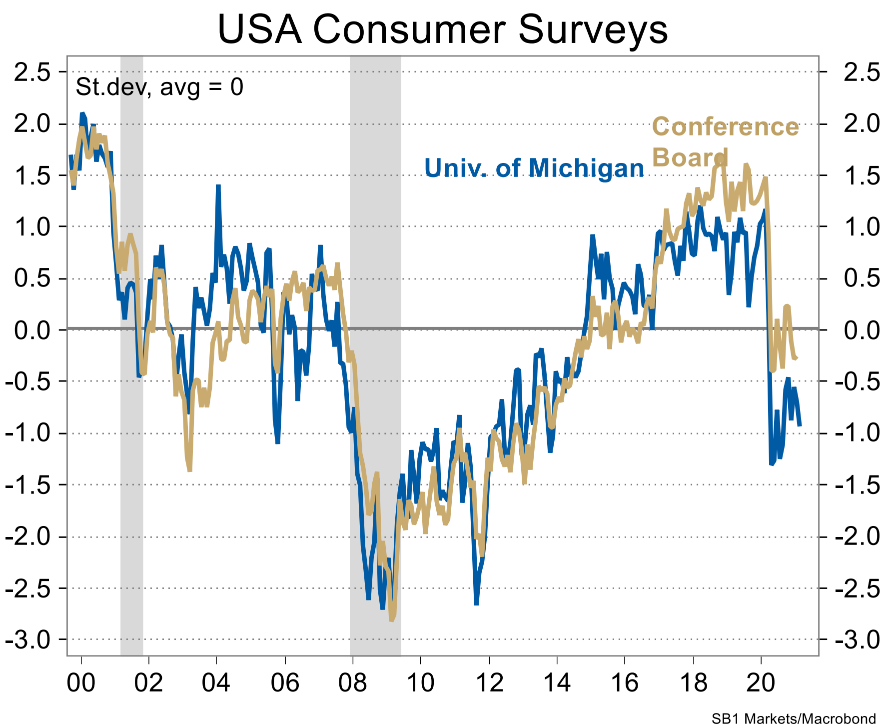


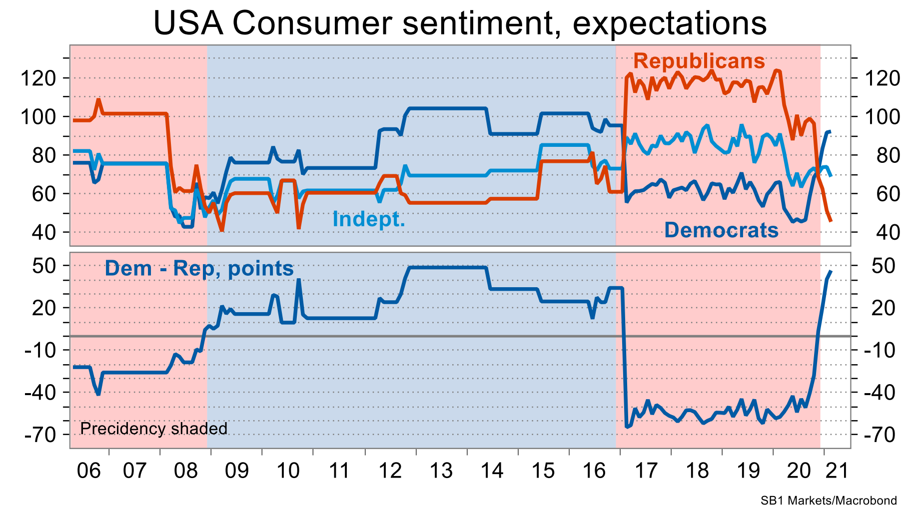


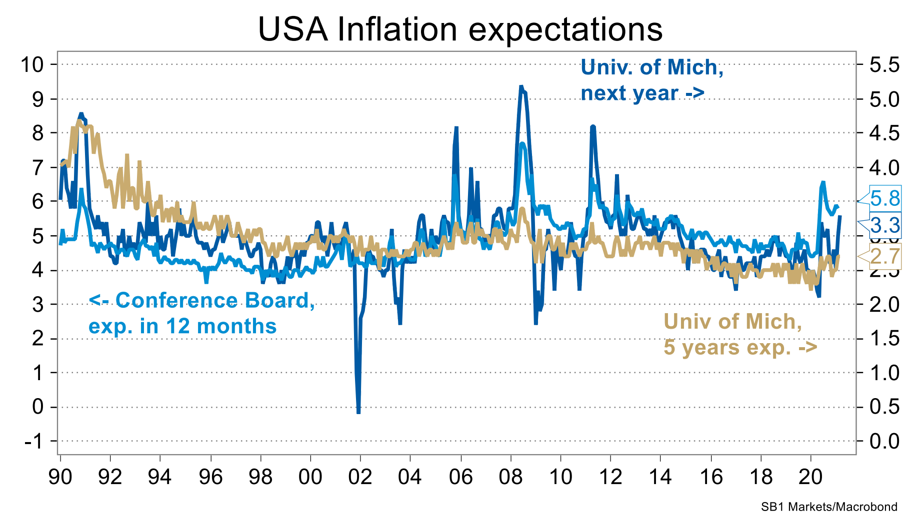
- New claims down 19’ to 793’ last week, from 812’ (revised up from 779’) in the previous week
- The no. is still higher than at the local through last autumn but the trend is downward
- Pandemic unemployment programs’ claims rose, as expected. On a brighter note: Continuing claims declined by 145’

Univ of Mich. consumer sentiment falls to lowest level since August

February print lower than most pessimistic estimate, according to Bloomberg





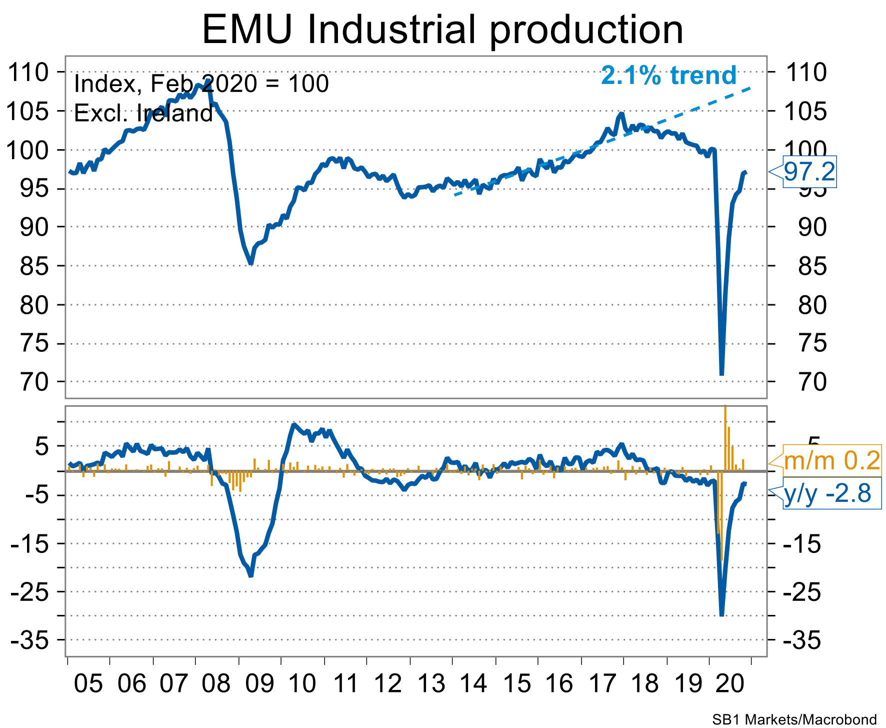


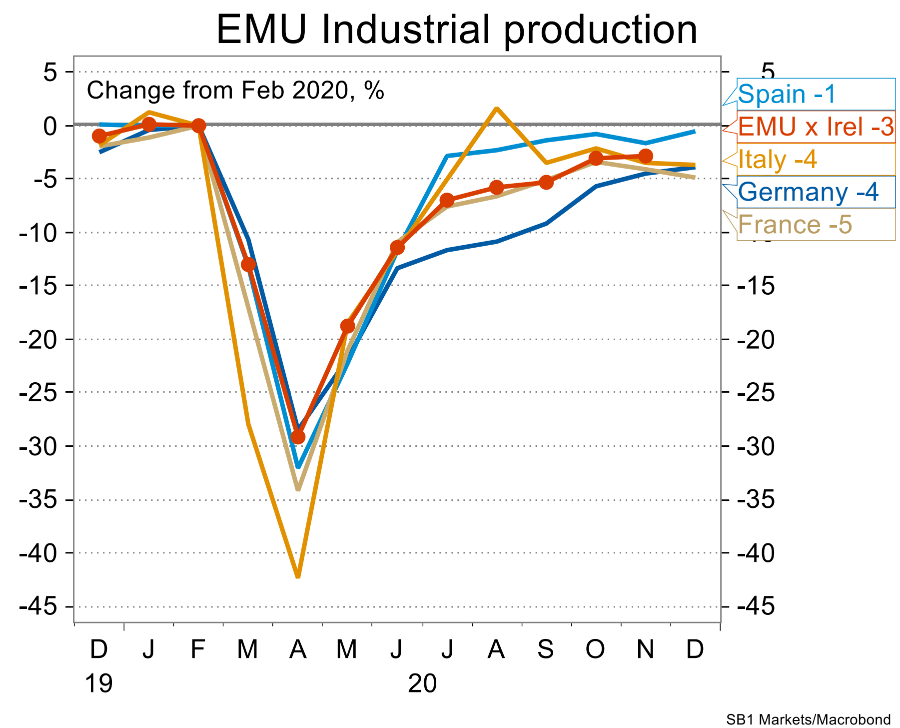
- The consumer sentiment survey fell 2.8 p to 76.2, while the market expected an increase to 80.9
- Both households' assessment of the **current situation** and **expectations** deteriorated
- **Republicans** have become much more pessimistic as of lately, while democrats' sentiment has improved – reflecting the election result
- **Inflation expectations** have not taken off, but they are on the way up. The expectation for next year increased 0.3 pp to 3.3%, while the 5-years expectation was unch. At 2.7%

SpareBank 1 MARKETS

Manufacturing production surely down in Dec (especially if Ireland is included)

In Nov, production rose 2.5% due to a 'technical 53% hike in Ireland, that partially reversed in Dec

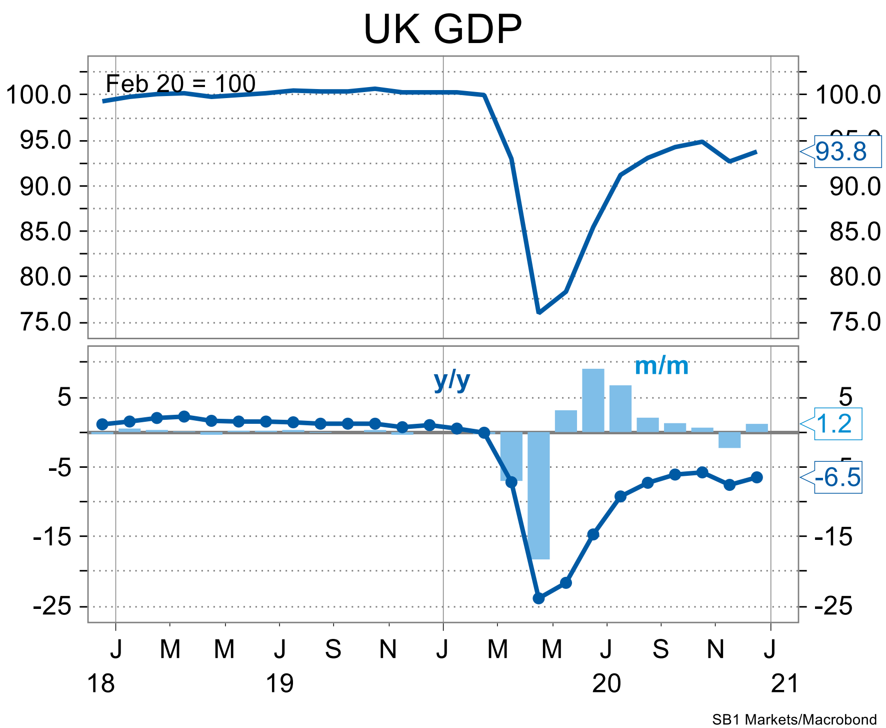


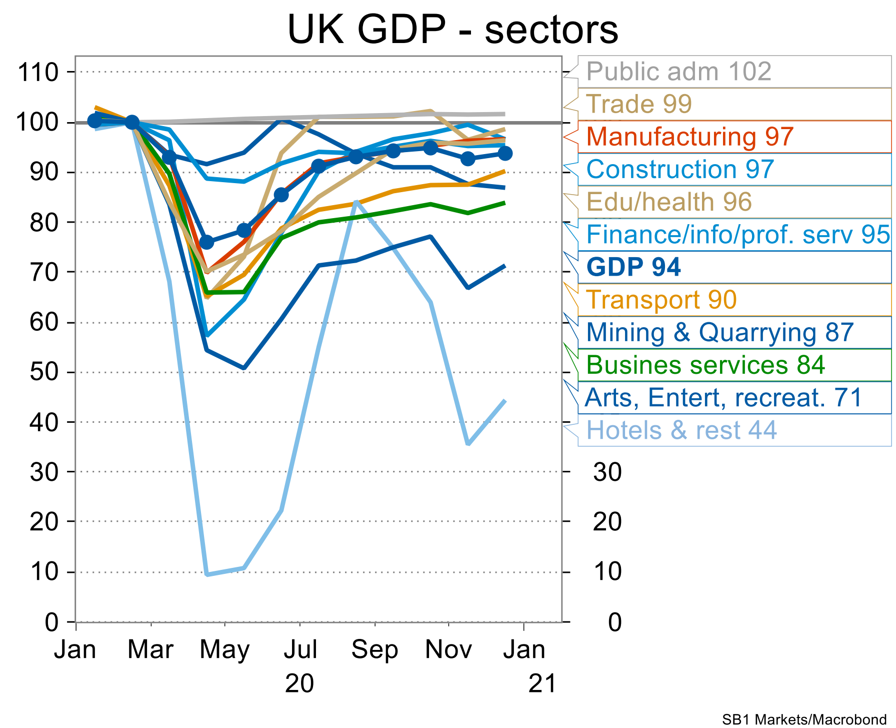


- The first Dec data: Production increased in Spain (1.1) & Germany (0.6%), while France (-0.2%) & Italy (-0.8%) have reported small setbacks. Production in Italy has been heading down from (a high level) in August
- EMU (x Ireland) manufacturing production rose 0.2% in Nov, and the outcome in Dec may be quite similar – still being more than 2½% down from Feb last year
- The 'silly' Irish production data drives the whole Euro Area data - production rose by 50% in Nov, and fell by 25% in Dec (tax motivated software transactions??). The Dec decline will subtract some 1¼% from EMU production - counterweighting a likely small increase in the rest of the union

UK economy shrinks 9.9% in 2020 – biggest decline since the 1700s

...But GDP grew by 1.2% in December, beating estimates by 0.2 pp. Q4 growth at 1% (exp. 0.5%)

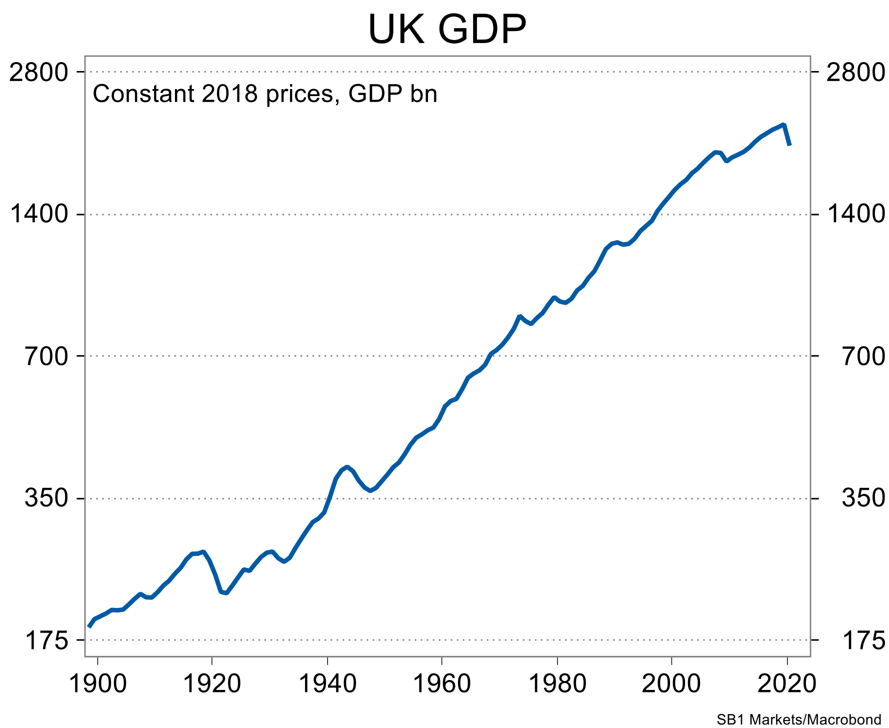


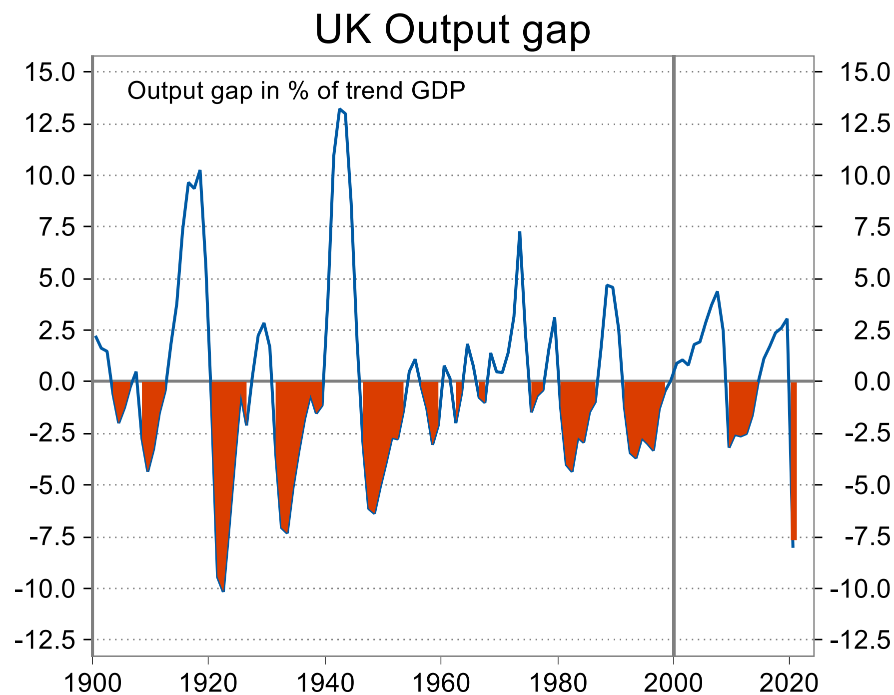


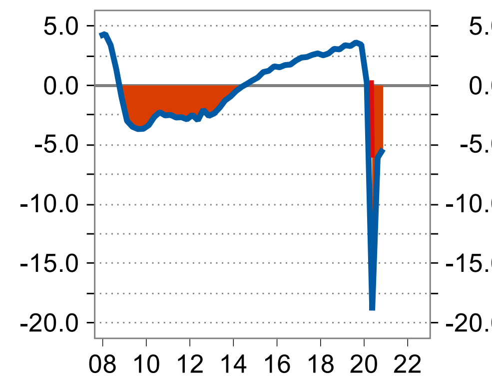
- The service sector was up 1.7% - the biggest contributors here were hotels and restaurants which were up 25%
- The construction sector fell by 2.9%, while manufacturing was up 0.2%
- Other sectors were mostly up, like trade (+2.2%), Transport (+3.1%), health (+2.4%), and arts/entertainment (+6.8%)
- GDP in December is down 6.2% below the Feb level. (Norway is down 1.1%)

An *annus horribilis* indeed – but incurred losses have been bigger before

However, while the downturn was deep, 2/3rd of the Q2 loss is recovered. How long to 'fill' the rest?





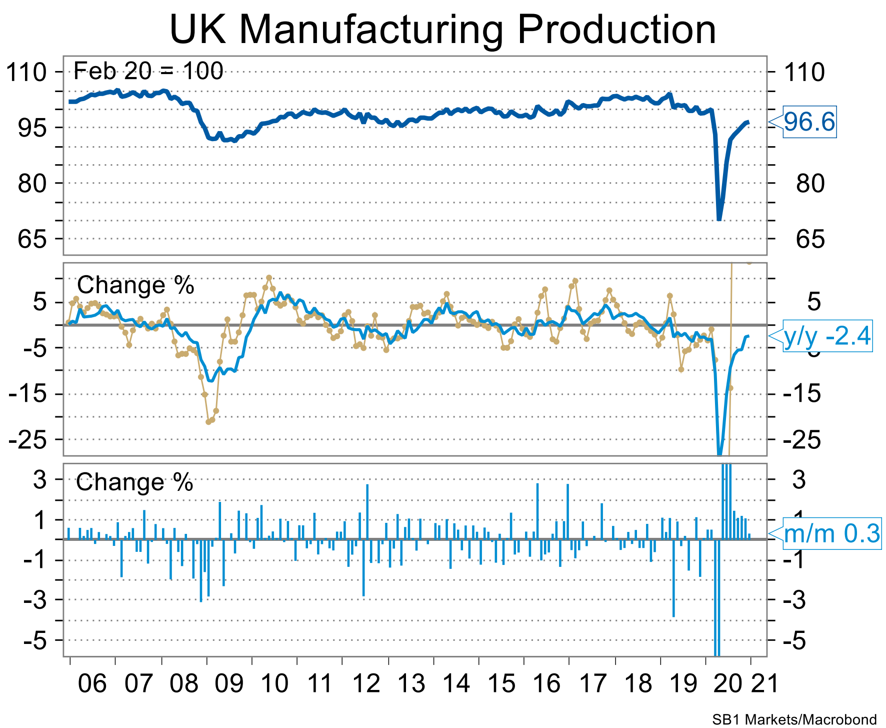


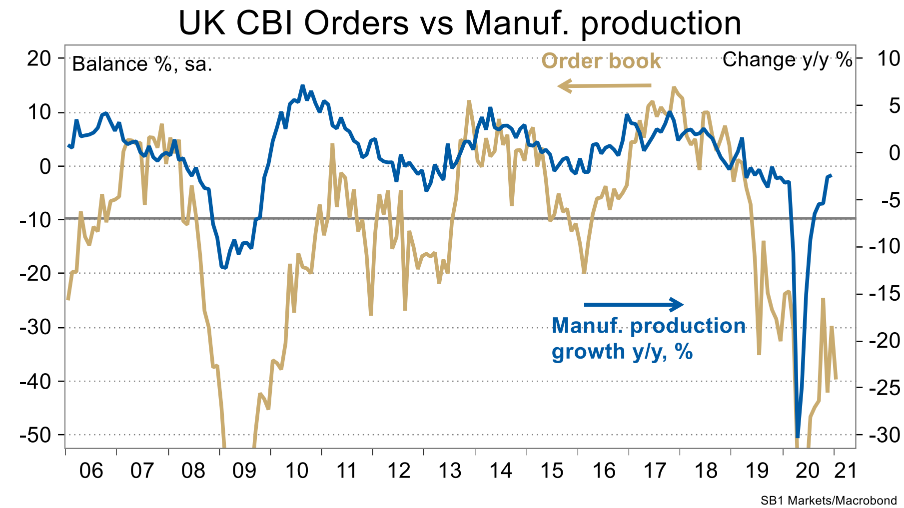
- The **economic loss during the downturns** are often described by the accumulated negative output gap, the red areas at the charts to the left
- The accumulated negative output gap during a 'typical' recession is some 10 – 15% of one year's GDP
- In 2020 the economy lost 7.5% (measured by the gap, the economy very likely was above trend in 2019
- How large will the remaining gap turn out to be? If the gap is closed at the end of 2021, we may add 3 pp, if it is closed in late 2022 we may add 5 pp. **In sum 10 – 15%**

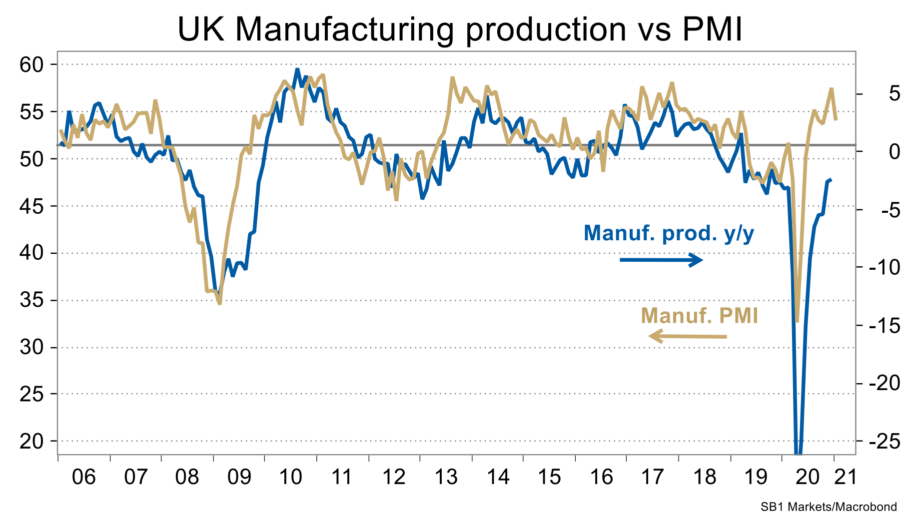
SpareBank 1 MARKETS

Manufacturing indicators mixed: The PMI still strong, the CBI order book not

Manufacturing production up 0.3% in December – missing expectations by 0.3 pp. Down 3.4% vs Feb

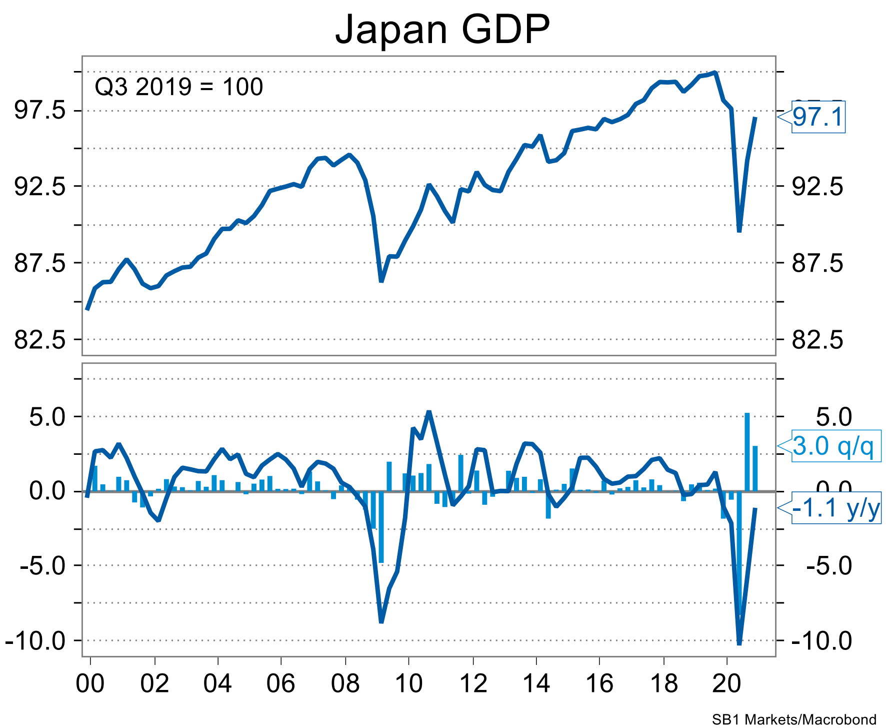


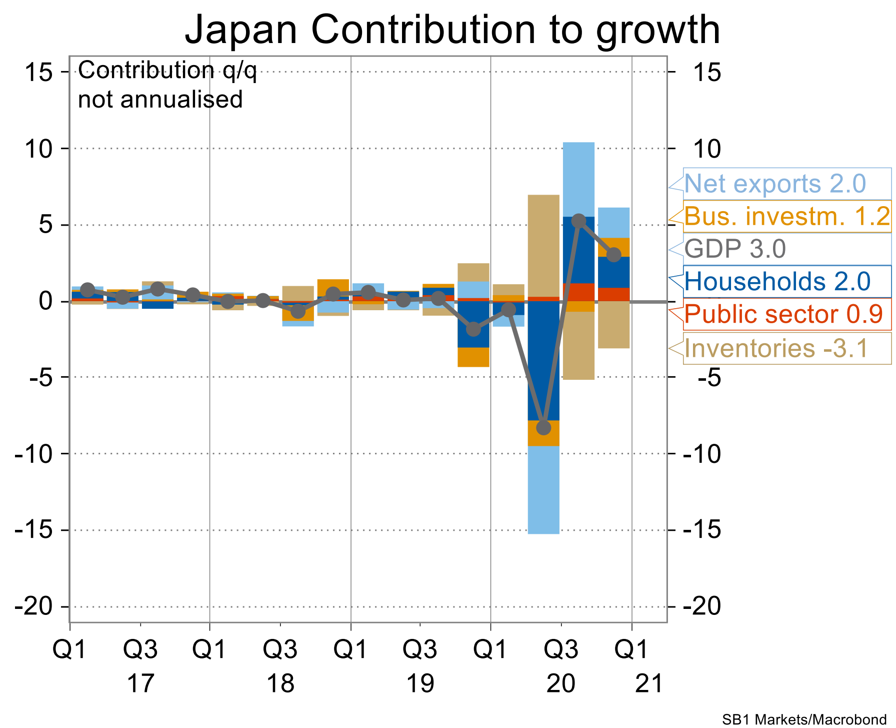




GDP +3% in Q4 (12.7% annualised), down just 1.1% vs Q4 19 (an easy comparison)

GDP was expected up 2.5%

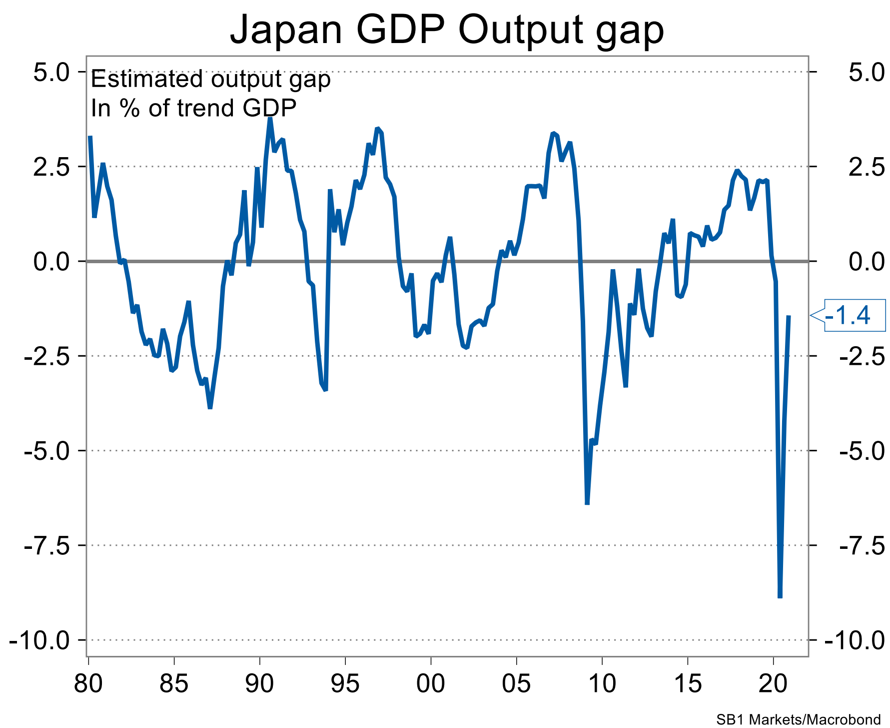


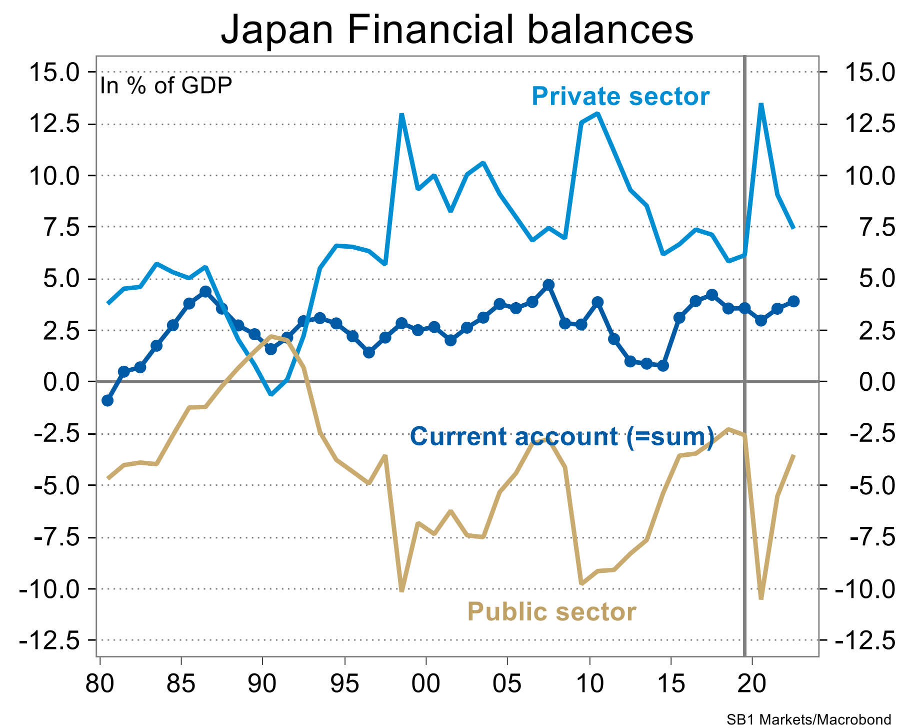


- Inventories were drawn down, while net exports, household demand and public demand rose. Business investments fell slightly
- GDP fell 4.8% year, of which some 2% was due to a weak starting point, GDP fell sharply in Q4 due, at least partly due to the VAT hike in Oct 2019. Thus, the 1.1% gap to the pre-pandemic level is correct, but not fully relevant when assessing the state of the Japanese economy

A deep downturn – but not that far up to the pre corona level

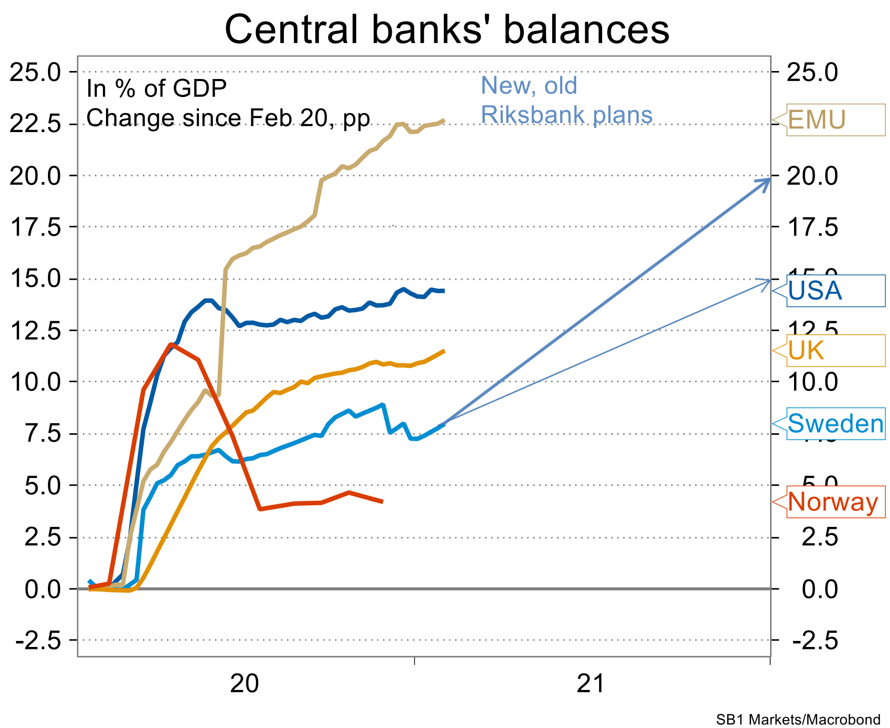
However, its more than a 2 pp longer way up the the pre VAT hike level





Riksbank keeps interest rate & QE program unchanged

An aggressive, dovish central bank – who don't want to be blamed if something goes wrong…



- The US Fed, ECB & BoE has been more aggressive than the Riksbank
- All the other banks plan to continue their QE programs – and will end up higher than the Rix now signals

- The Riksbank kept the **signal rate unchanged at zero**, as expected – and it's expected to stay there for a long as the Bank can see (till Q1 2024)
- The Bank keeps the **target QE level at SEK 700 bn,** as announced at the Nov meeting, until the end of 2021,– in order *'to give further support in an uncertain time, improve the conditions for a recovery, and to help inflation rise towards the target'*
- The Bank emphasises that it '*is making it clear that comprehensive monetary policy will be available **as long as it is needed**'*
- The Bank revised its growth projections as the 3rd/4th corona wave has shown to have less of a negative impact on **the Swedish economy**
  - GDP fell 2.8% last year, 1.2 pp less than the Riksbank's last forecast. The 2021 forecast is raised 0.4 pp to 3.0% - citing that the economy is now is more resilient to the effects of the virus
  - The unemployment rate will still increase from 8.3% in 2020 (revised down 0.1 pp) to 8.5% next year (-0.9 pp)
  - Inflation will remain well below the 2% target 'forever'
- **The Riksbank remains dovish, and takes out another insurance, as the new corona challenges may push the Swedish economy down again.**
- So far however, there are no signs of that to happen
  - An example: The Swedish PMIs is the strongest in the world, have been so for 3 months in row. We think the bank is too pessimistic

Highlights

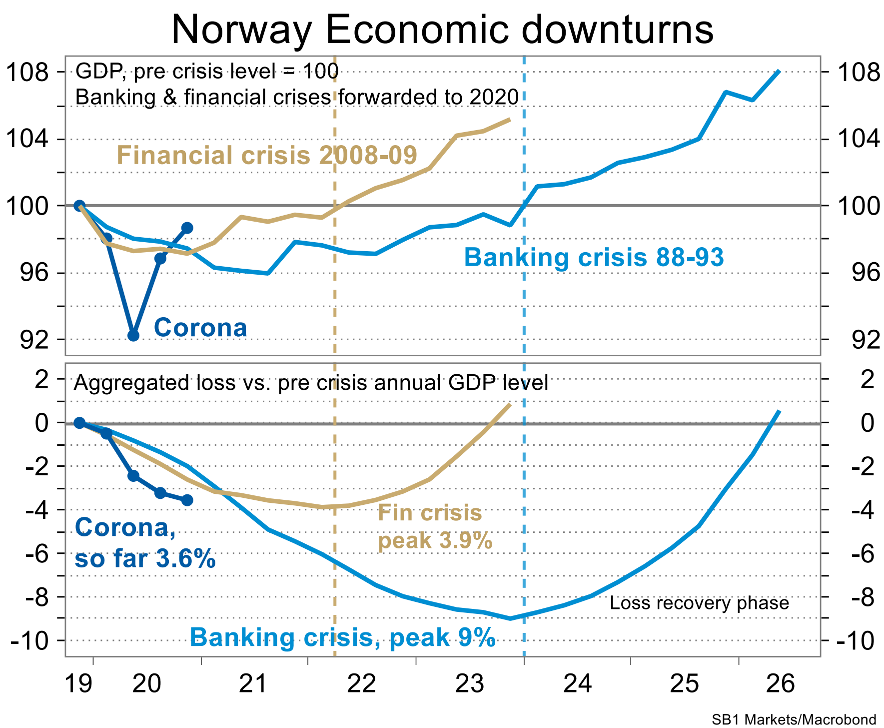
The world around us

The Norwegian economy

Market charts & comments

A special year – that ended pretty well: Mainland GDP now 1 – 1½% down vs PC

GDP grew more than expected in both Dec & Q4, and declined less than expected in 2020, -3.1%

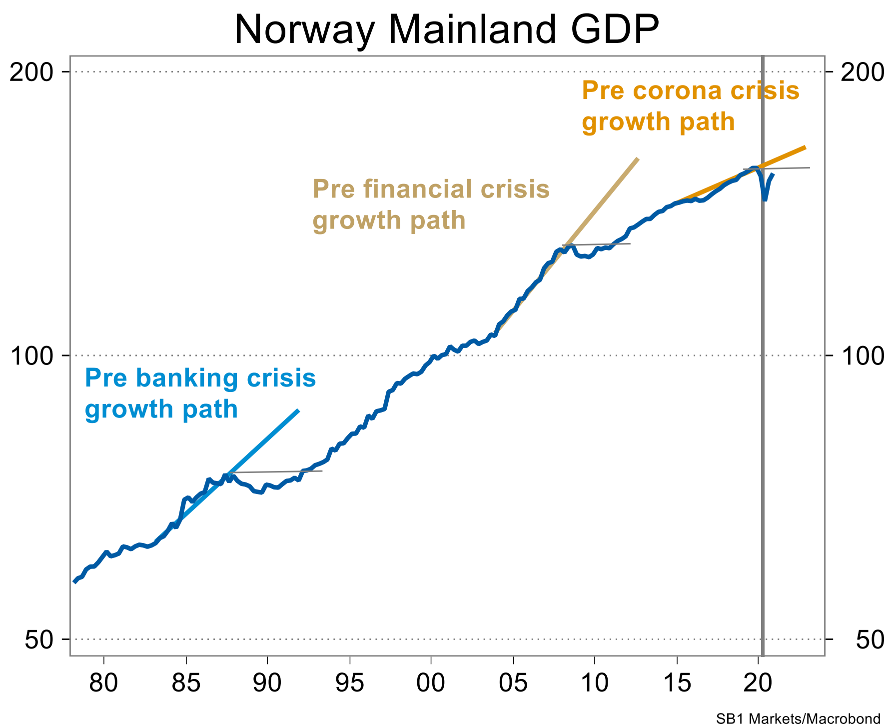


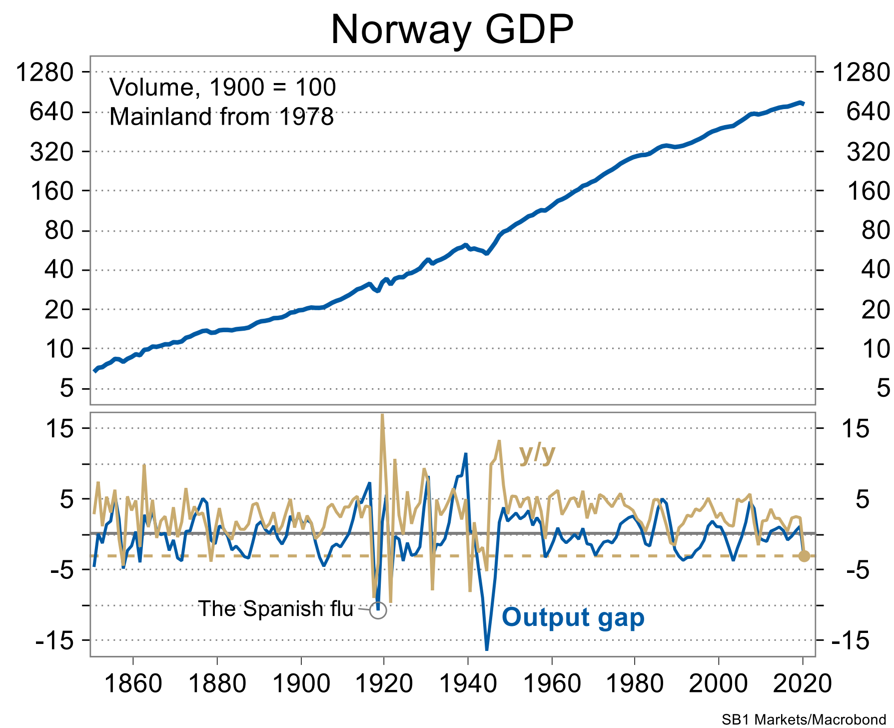
- **2020: Mainland GDP down 2.5%. Or 3.1%?**
  - » Before working-days adjustment, Mainland GDP fell 2.5% (total GDP -0.8%, as oil production rose sharply), which is often referred to as the 'official' figure. 2020 yielded 3 more working days than 2019. We usually refer to WDA and seasonally adjusted data, in Norway and elsewhere. And the 'real' decline in GDP was 3.1%, the largest setback since 1944 (total GDP -1.3%)

- **The 10% downturn last spring was extreme**, as has the recovery been so far . This is, of course, not a normal economic recession but a virus induced setback, defying all normal crisis cycle characteristics
- Following a strong recovery, starting in mid April, GDP is now just 1% – 1.5% below the pre-corona level, following a 1.0% growth in December (m/m) and 1.9% in Q4 (q/q)
- In 2020, Mainland GDP fell by 3.1%, the largest setback on record (2.5% not working days adjusted, we prefer the former)
- **The loss of economic output**, financially covered by the government (and future tax payers) so far, is substantial – and we do not yet know the final outcome
  - » Calculated by the loss of activity vs. from the peak in Q4 19 until activity is back to the same level, we assume in late Q1 or in Q2 next year, the lost output will equal somewhat less than 4% of pre-corona annual GDP. That's close to the loss of output of the financial crisis, equalling 3.9% of GDP. During the housing bubble burst/banking crisis starting in 1988, the loss equalled no less than 9% of GDP
  - » However vs. likely growth expectations before the financial crisis compared to the similar before the corona crisis, the corona crisis will most likely turn out to be far smaller (and miles smaller than during our banking crisis). *Check the chart at the next page*. In general, and for the world economy, that's why assets markets are so strong, surely also supported by record low interest rates

Expectations could not have been that bright, before corona hit, no boom then

Our expectations were muted – and growth had not been strong over the previous years

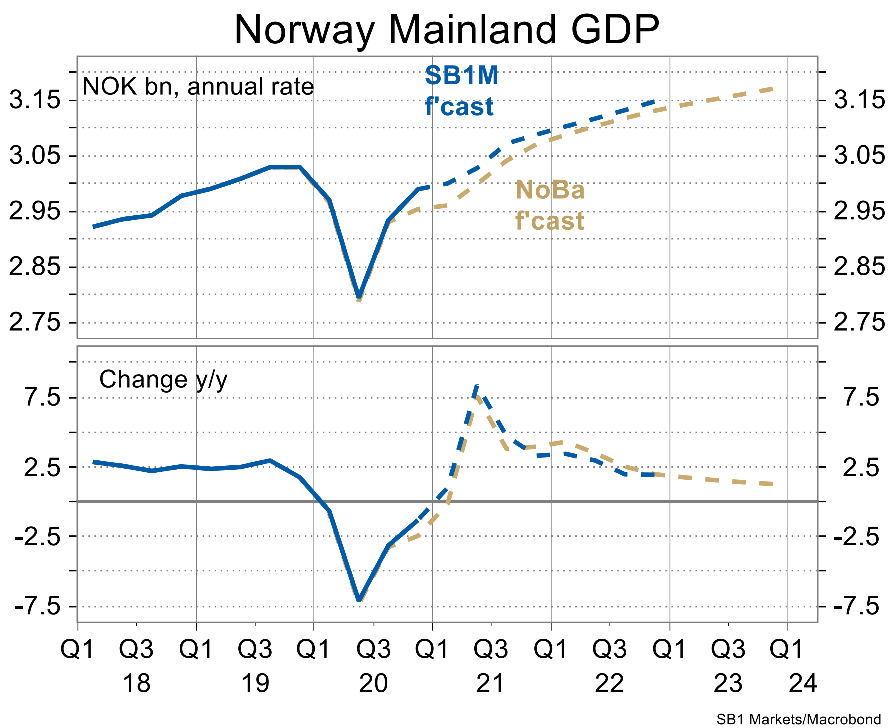




- The contrast to the banking & financial crises are obvious, the disappointment vs. especially long-term expectations is not that large this time
- For the record: A 3% drop in GDP is not normal. Last time was probably in 1944, and before that in 1940, 1931 and during post WWI shipping/banking boom that collapsed in 1921, and before that again a downturn as the Spanish Flu hit in 1918

The outlook: Towards 4 – 4½ % 2021 growth?

Q4 GDP is 2.3% above the 2020 avg, and 1.2% ahead of NoBa's Dec forecast



- We expect the **output gap** to be closed earlier than Norges Bank expects (Q2-22)
- Thus, we expect that Norges Bank will start hiking its **signal rate** in H2 – the vaccine rollout/virus containment will decide when

... and barring a bad virus/vaccine scenario, we expect economic activity to increase sharply through 2021, after a Q1 break

Households

- **Goods consumption** will slow down but remain higher than the pre-corona trend normal until we can spend more both on domestic services and abroad.
- **We are very confident that demand for services (x foreigners)** will recover briskly as soon as the virus is brought under reasonable control in Norway. Our base case is that this will happen through Q2 and into Q3. The large accumulated savings through last year, and still an extraordinary high savings rate make us even more certain
- **Foreigners' spending** in Norway (down equalling 1.4% of GDP) will not recover before the coronavirus is beaten down, abroad and in Norway. No quick fix. However, Norwegians spend 2.5 x more abroad, and this spending will not recover fully before foreigners are coming here. In the meantime, more 'Norwegian' spending in Norway
- **Housing investments** have bottomed, and the 2. hand market is tight, and new home sales are on the way up. Housing starts too. At least until interest rates are turning upwards

Businesses

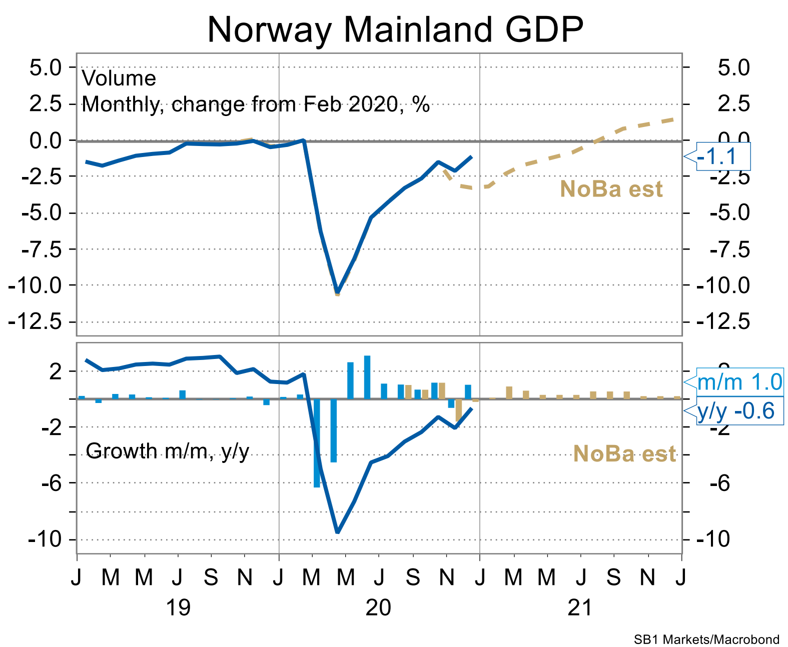
- **Mainland business investments** have stabilised – and surveys have strengthened. We are revising our forecast upwards.
- **Oil investments** fell sharply last year but favourable change in the tax regime as well as an oil price at USD 60, may stabilise investments in 2020

Exports

- **Mainland goods exports** have recovered will be kept up, as long as demand for goods abroad remains strong. And most likely, it will

GDP up 1% in Dec, supported by fisheries & electr. prod by 0.9%

However, December was a decent month – and much better than expected

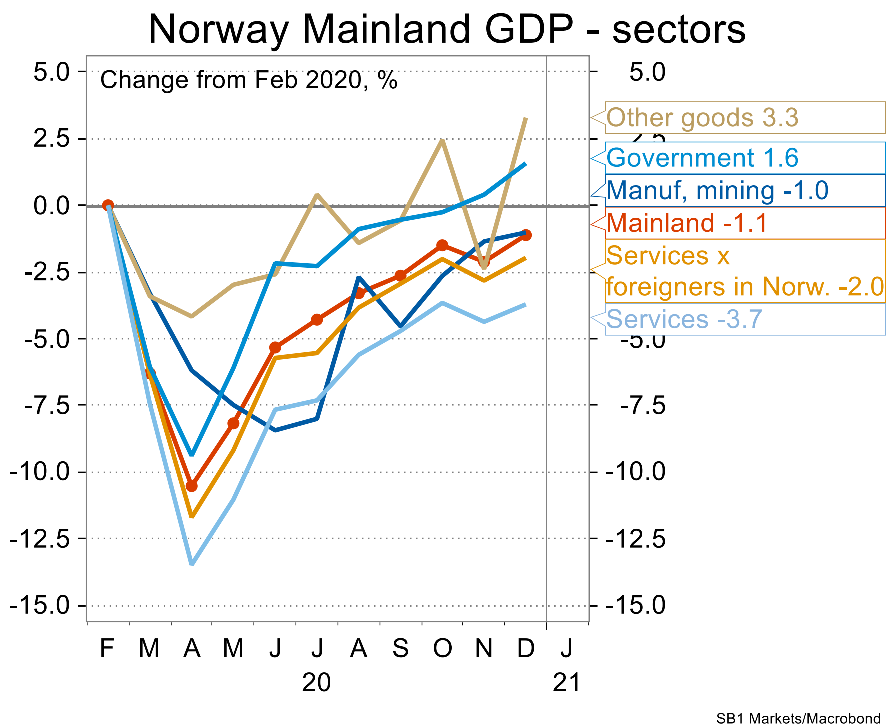


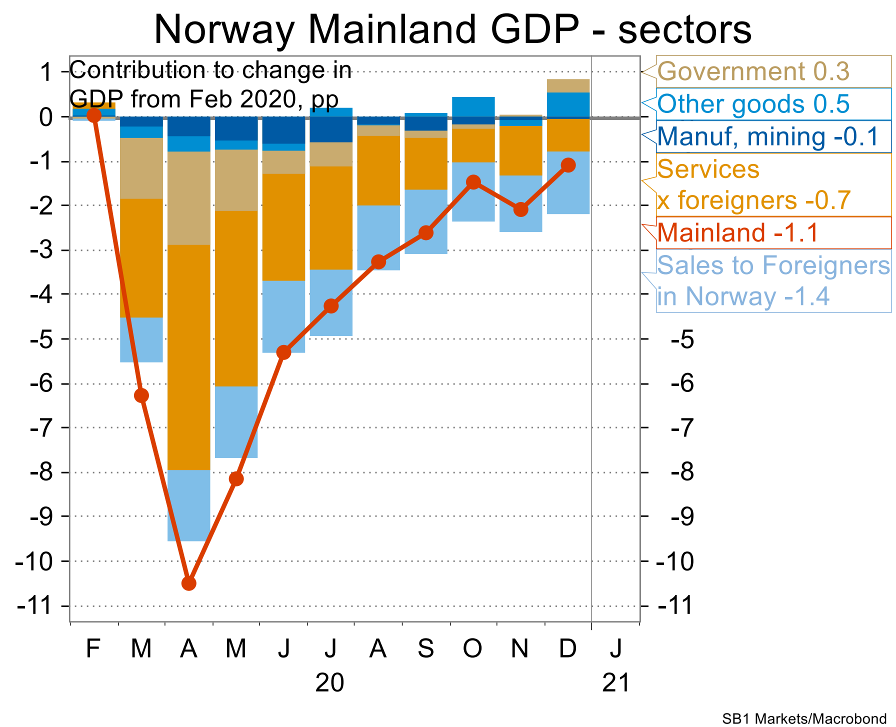
- **Dec Mainland GDP was better than expected, up 1% m/m,** we exp. 0.2% (consensus – 0.2%). The setback in Nov was smaller than prev. reported, -0.6% (from -0.9%)
  - » December GDP was 2.1% above Norges Bank's forecast published mid Dec. So, the targets are moving, even the closer ones
  - » Fisheries & electricity lifted activity equalling 0.9 pp of ML GDP (we expected ' just' 0.4 pp) – following a negative drag in Nov
  - » Other sectors were stronger than we assumed +0.1% vs -0.2%. Services stabilised. GDP ex fisheries & electricity GDP is down 1.7% vs Feb
  - » Exports, housing & government demand contributed upwards on the demand side, as did Mainland business investments, while oil investments fell
- **Mainland GDP is down 1.1% vs the Feb level**
  - » **Demand:** Norwegians are spending more in Norway than in early 2020, as consumption of goods have increased more than services have declined. Spending abroad has fallen by 95% (equalling 8% of disp. income), and the money is saved. Housing investments are up. Mainland business investments have fallen by 3%, while oil is down 9%. Exports ex petroleum (and tourism) are back to the Feb level. Foreigners are not spending anything in Norway, a cut equalling 1.4% of GDP
  - » **Production:** Trade (retail+) and education is up vs. Feb '19, manufacturing and professional services are close to the Feb level. Hotels & restaurants are down 40%, transport, culture/ entertainment and business services are down 18 – 29%.

SpareBank 1 MARKETS

Production: Private services recovered the November losses in December

Still down by 3.7% vs Feb '19 – of which more almost the half due to 'no' demand from foreigners

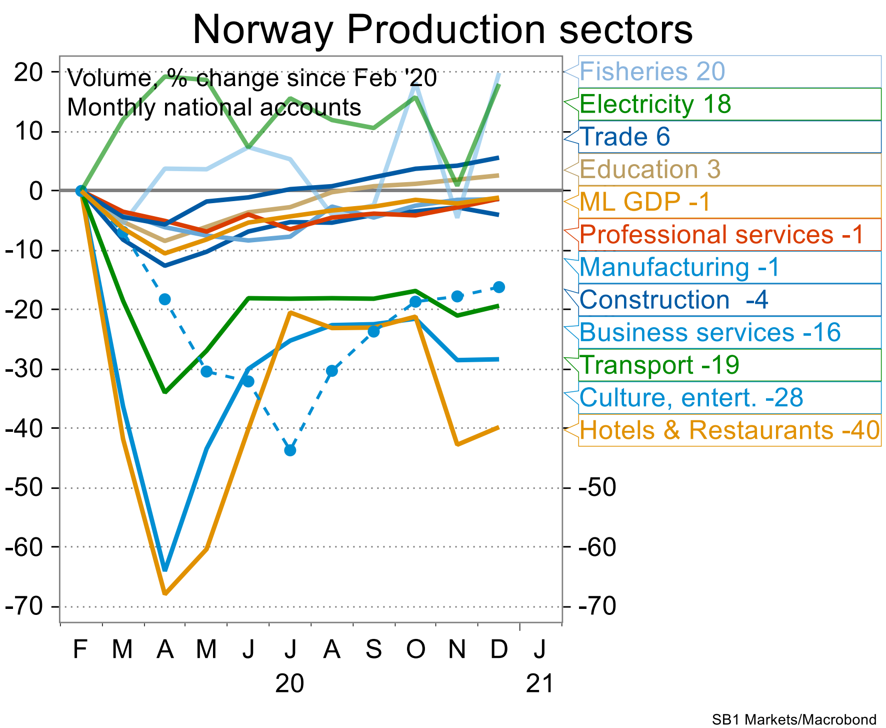


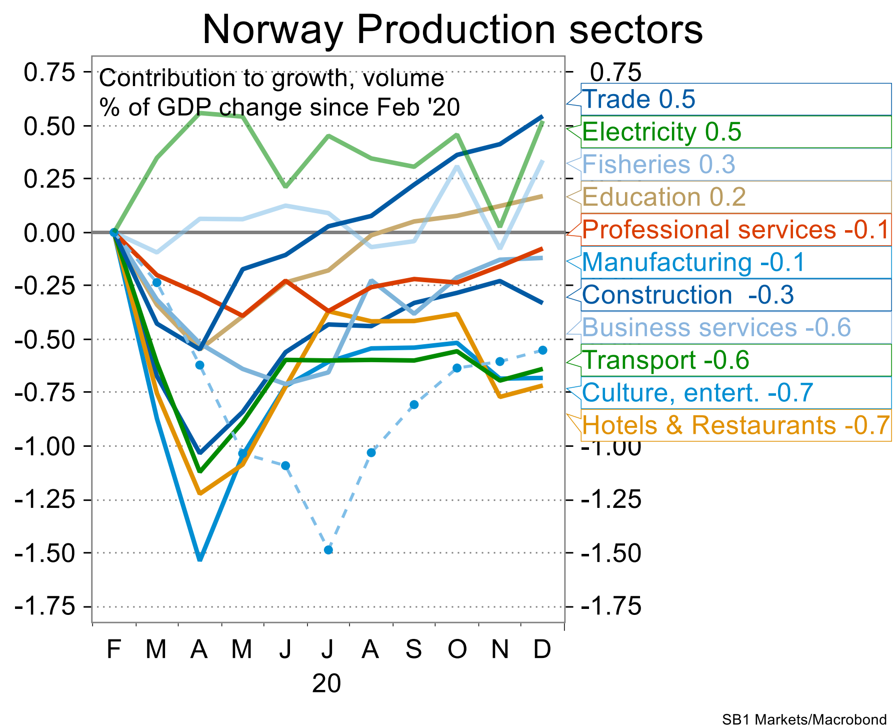


- In Nov-Dec **service sector production was unchanged** amid tighter corona restrictions – compared to the 13% drop last March/April. Still, the upside is limited before the virus it brought under control
- **Manufacturing production** is still recovering, and is now 1% below the Feb level. However the downturn is solely due to steep decline in oil related industries – as oil investments are down 9% vs Feb (and 14% vs Q4 '19). Ex oil related manufacturing industries, production is up
- **Other goods production** is volatile mostly due to (ocean) **fisheries and electricity production**, both down in Nov and sharply up in Dec, explaining large parts of the changes in total GDP! (*See more the two next pages*)

Production details: Hotels & restaurants up in Dec, down 40% vs. Feb

Peoples' business down 20-40%, in sum a 2.6% negative drag on GDP

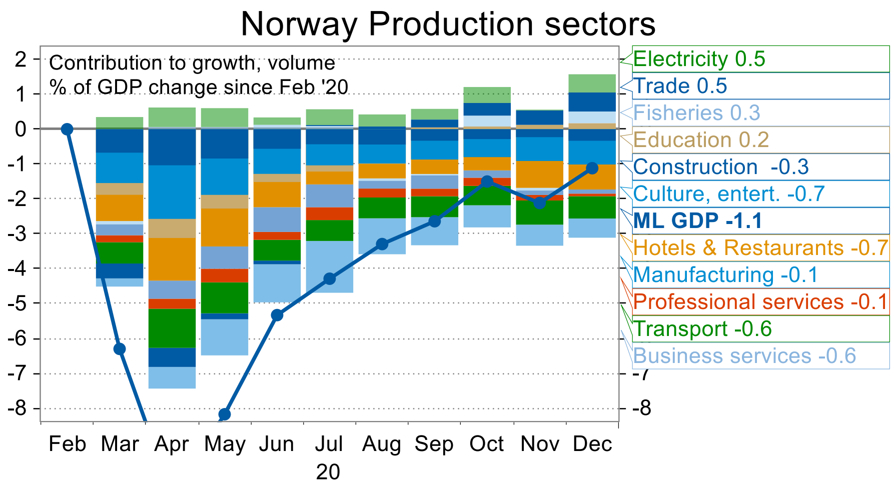


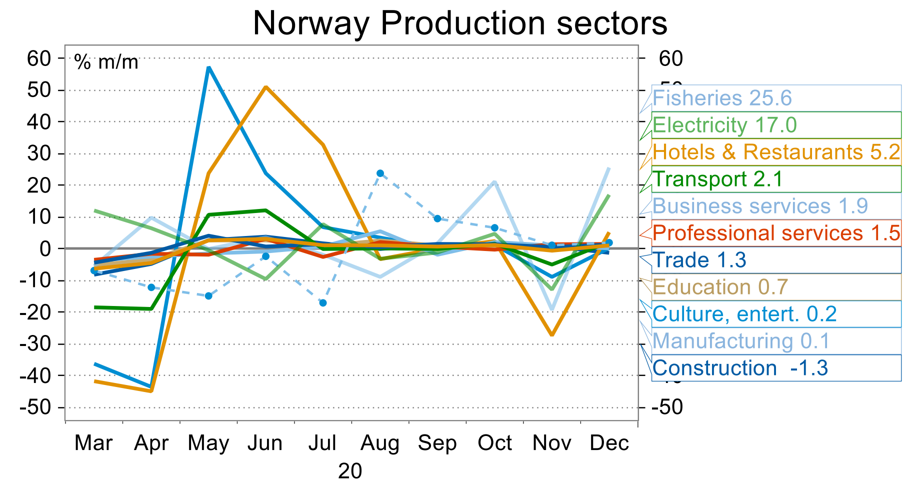


- No further decline in **hotels & restaurants, culture or transport** in Dec. Most likely, Jan/Feb may be somewhat weaker
- Activity in **fisheries & aquaculture** and **electricity production** rose sharply in Dec, following the Nov setback, contribution 0.9 pp to GDP growth in Dec, and the level is very likely above normal, at least for fisheries
- Thus, according to our calculations, the 'underlying" GDP rose by just 0.1%, following a -0.1% decline in Nov
- Several sectors reported growth: **Health, manufacturing, trade, professional & business services, while construction fell**

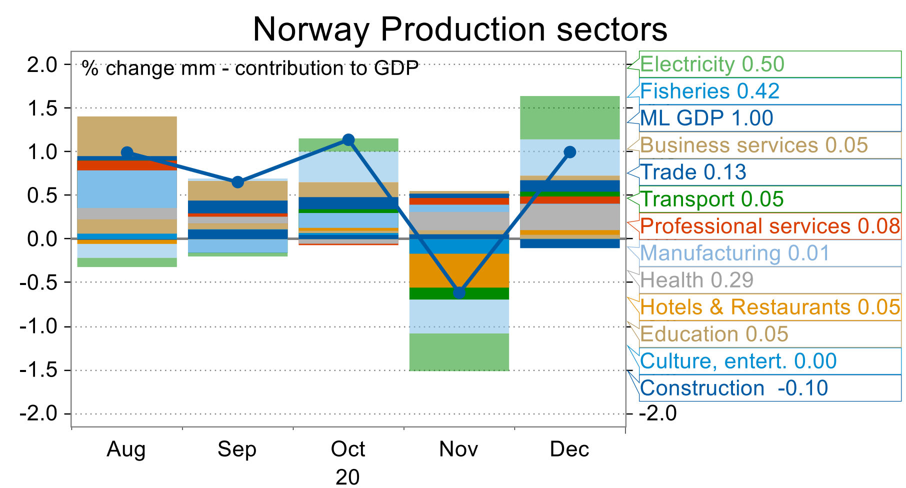
Business services: Temp services, travel agencies, call centres, congresses, cleaning, canteens, property services, leasing

Production details: Squeezing the data





- **In December**
  - » Fish & aquaculture up 25%, following the 20% setback in Nov. The level in Nov is very likely above normal
- **Since February**
  - » Hotels & Rest, culture & entert., and transport services have all contributed by 0.6 – 0.7 pp, in sum equaling 2.4% of Mainland GDP (while GDP fell by 1.1%)
  - » However, electricity production will not contribute the same way going forward, and the 'real' activity is lower than the reported 1.1% vs. the pre-pandemic level

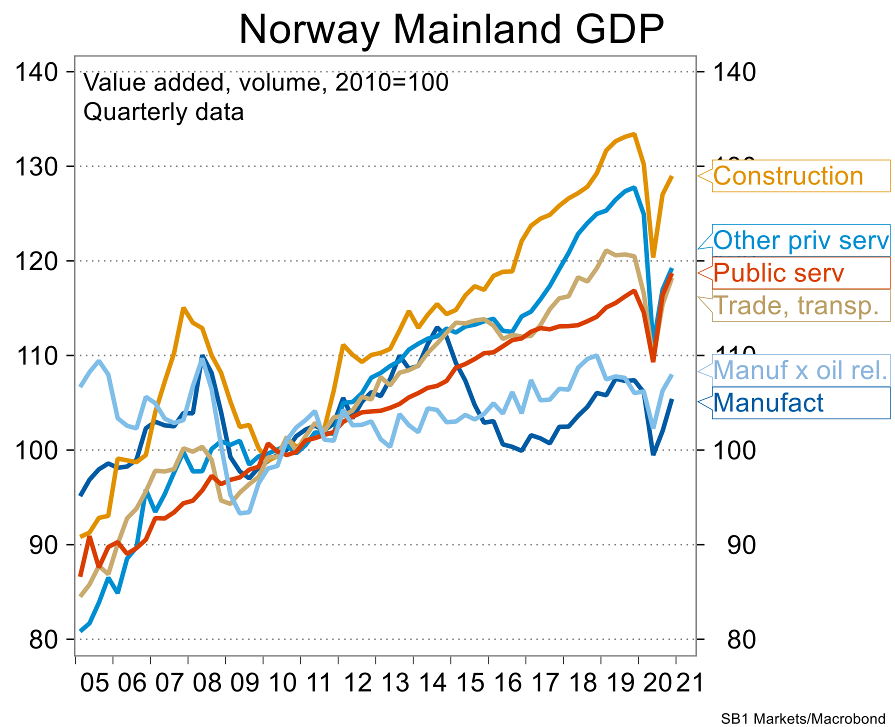


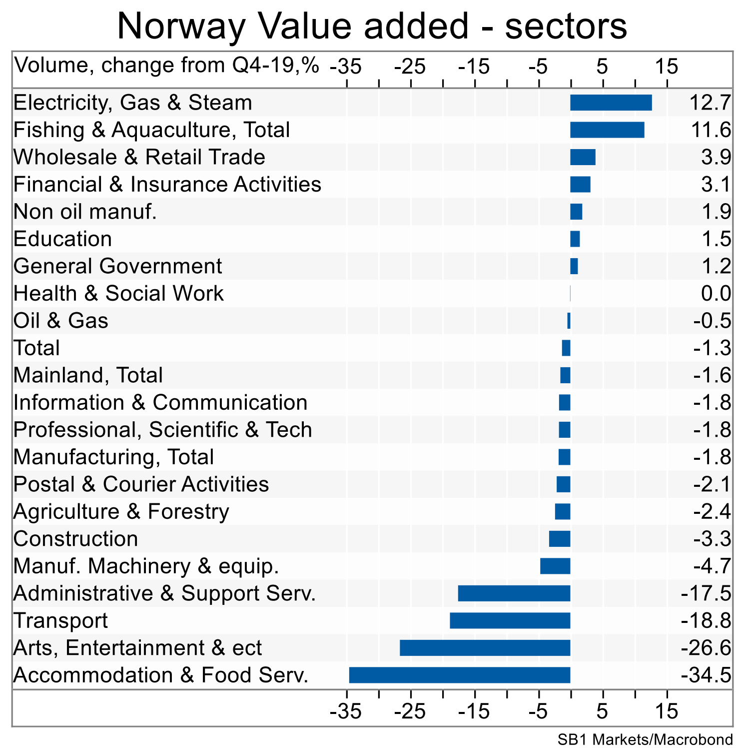
Not all sectors are included in this monthly detailed data

SpareBank 1 MARKETS

Production: A longer view…

Transport, arts, entertainment, hotels & restaurants at the bottom – down 18 – 24% in Q3





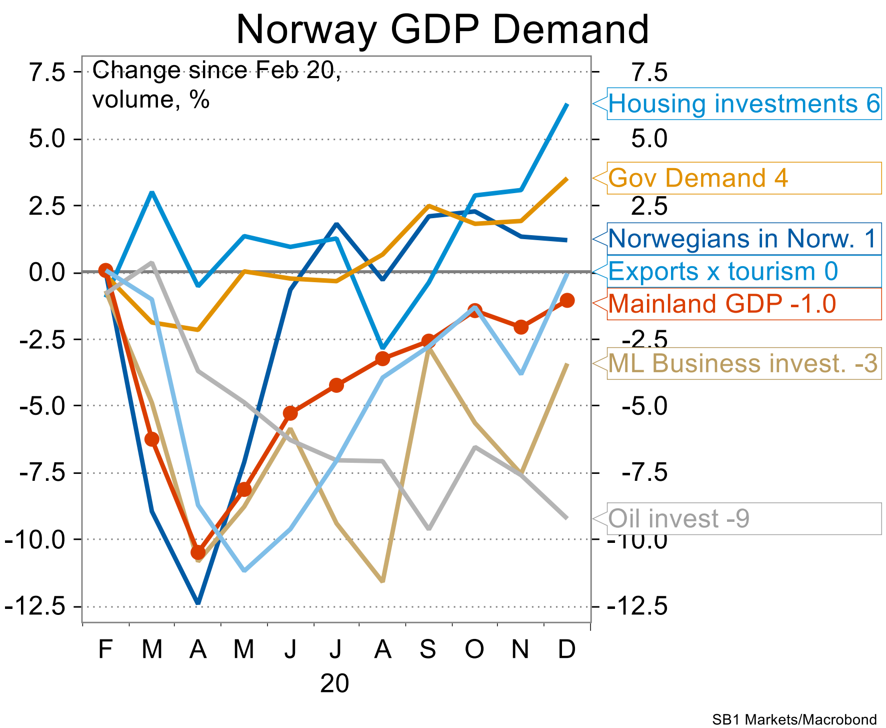
The Q4 data (vs. the monthly data at the previous pages)

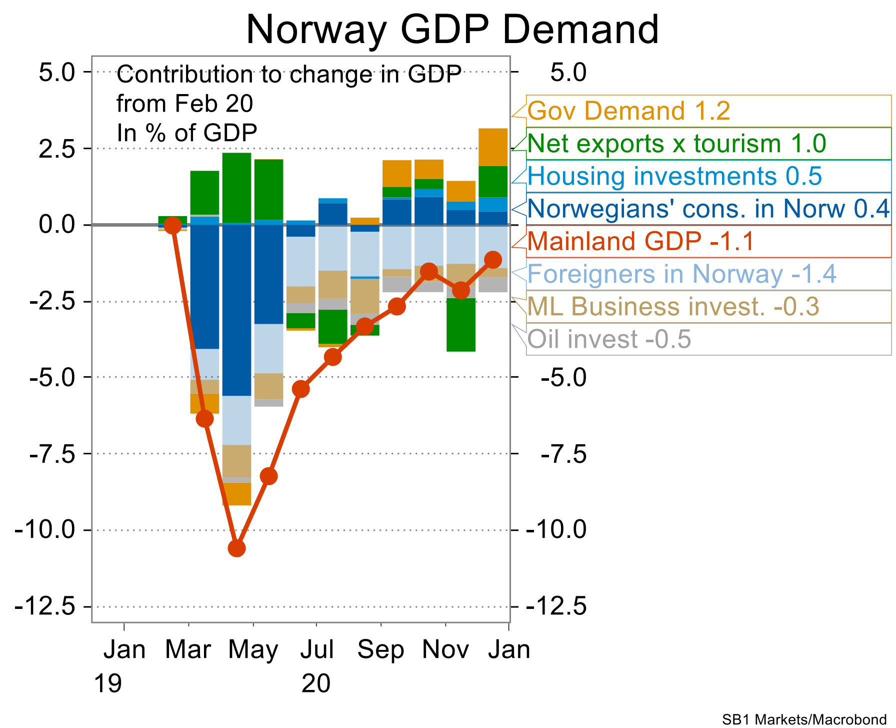
- Hotels & restaurants down 35%. Culture & Entertainment -27%
- Administrative & support services (like staffing & travel agencies, cleaning, canteens, leasing etc) are down 17%
- Transport -19%, both due to a steep decline in personal transport (airlines, train etc)
- Manufacturing is down 2%, due to the decline in production in oil related industries, others are up 2% vs Q4 19.
- Construction is weaker than we have assumed, 3% down vs. Q4-19

SpareBank 1 MARKETS

Demand: Exports, housing, mainland business inv., and gov't spending up in Dec

Household consumption fell marginally, oil investments somewhat more

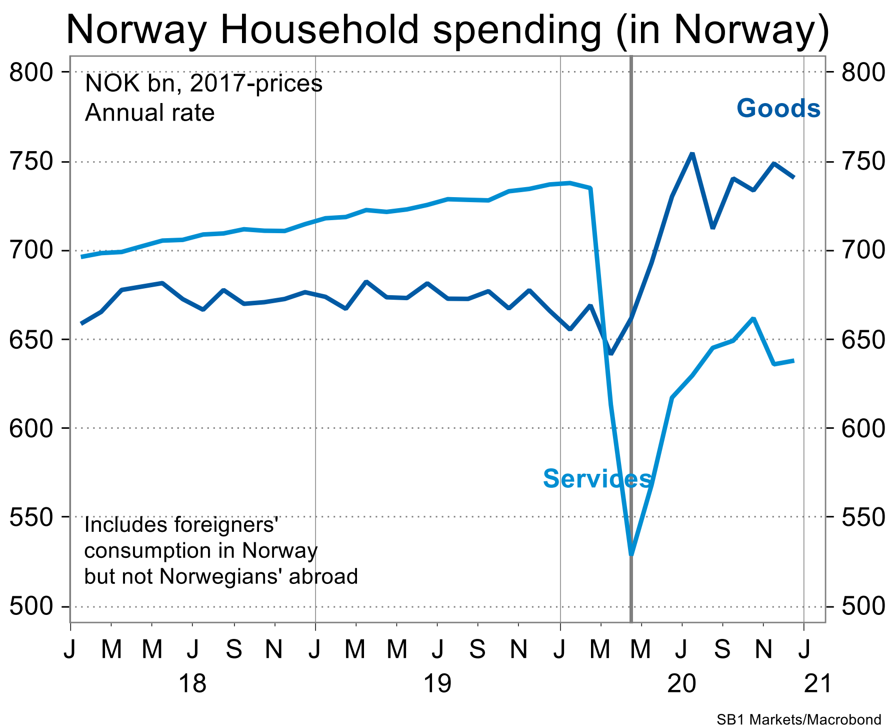




- **Norwegians' consumption in Norway** fell marginally due to lower consumption of goods – which remains strong. **Foreigners spent** a tad less in Dec, and their lack of demand deducts 1.4% from GDP (not adjusted for import content of goods they (used to) buy here)
- **Mainland business** investments reversed the loss in the two previous months, and are down just 3% vs. the Feb level – deducting 0.3% from GDP
- **Oil investments** are still on a slippery slope, down 9% (0.5% of GDP) vs Feb – and down 14% vs. Q4 2019
- **Government demand** is up 4% vs. Feb and has contributed to a 1.2% increase in GDP (alas, others are close to flat)
- **Mainland exports (x tourism)** rose and are back to the Feb level. Net exports are higher than in Feb, as **imports** are still below the Feb level
- **Monthly data are volatile, and consumption is trending up, as are exports x tourism. In sum, investments are trending up**

Service consumption has flattened since last summer, the virus is still around

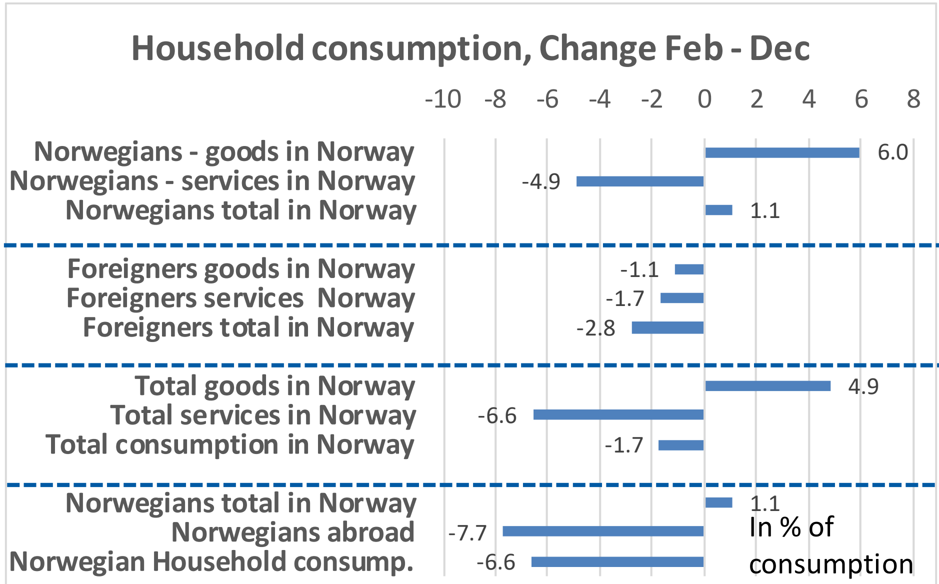
Spending on services a tad up in December, following the Nov decline. Level down 13% vs Feb!

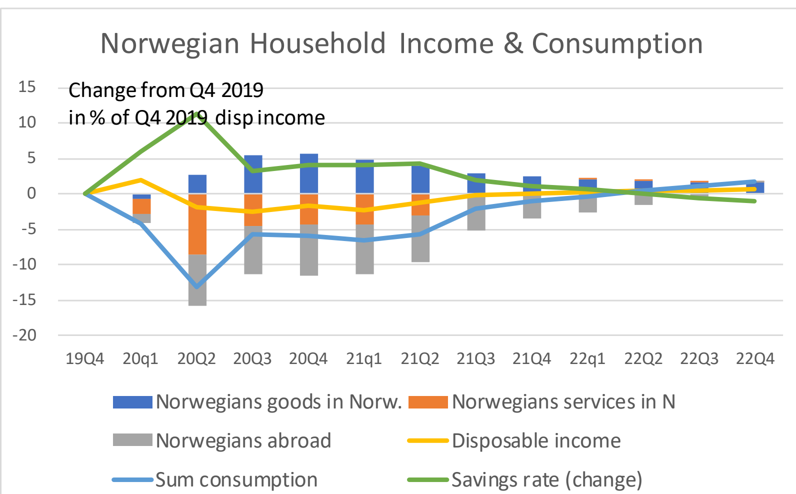


- Consumption of goods is up more than 12% vs February '19 but the decline in services is larger, and total consumption spending in Norway is down close to 2%. Norwegians are spending more at home in early 2020, but foreigners are have cut their Norwegian spending even more (equalling 2.8% of consumption in Norway), taking the total down
- Household consumption, which includes Norwegians' spending at home, and their spending abroad (but not foreigner's consumption in Norway), was flat in Dec, and is still down 6.6% vs. Feb
- We do not yet have all **Q4 income data**, but wage revenues are up, and we expect total disposable income to rise too. If so, the savings rate will increase vs. the comfortable 12% Q3 level. Savings have been running high through 2020, and will support a recovery in spending on services as soon as it safe and allowed to do so!

Norwegians are consuming like normal – in total – in Norway

Goods consumption has soared, services cut. And no foreigners are spending money here!

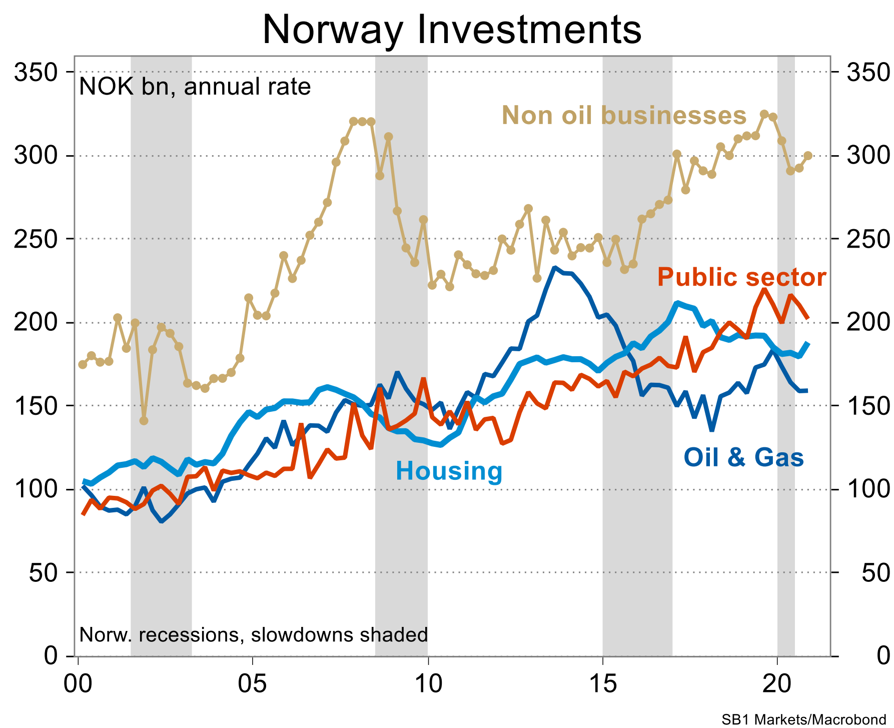


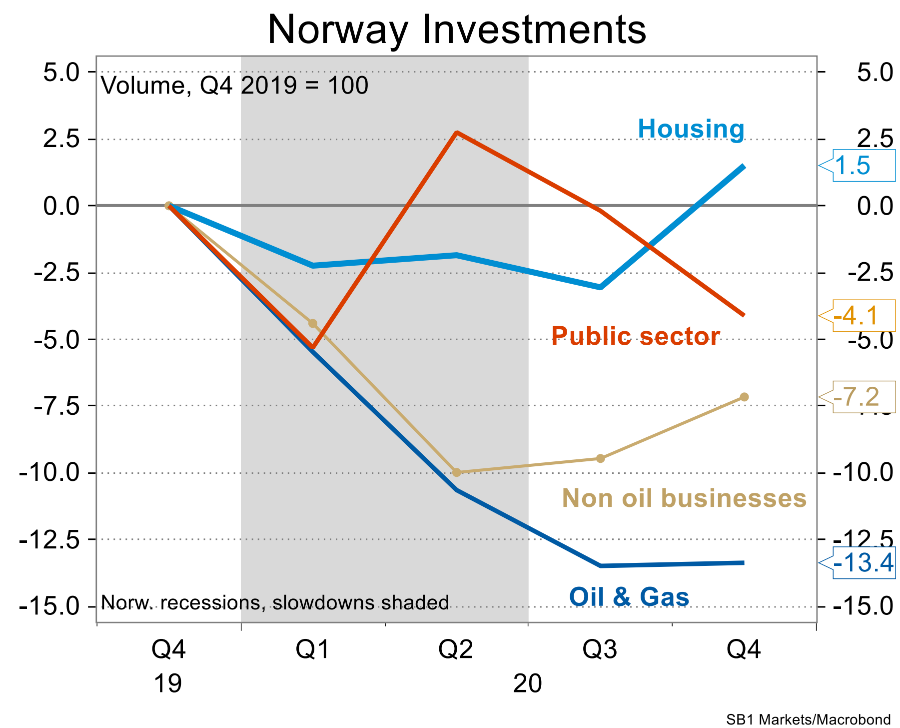


- Norwegian households have increased their consumption of goods in Norway more than they have cut their consumption of services – in sum up 1.1% of total household consumption
- Foreigners have cut their spending in Norway equalling 2.8% of *total private consumption*
- Sales of consumption goods are up 4.9%, and services are down 6.6%. The total is down 1.5% - *all in % of total consumption (+12% & -13.5% actual ch.)*
- Norwegians have reduced their spending abroad equalling 7.7% of their total consumption – and total Norwegian household consumption is down by 6.6%
  - » Other countries have taken the beating from the cut in Norwegian's spending (before calculating for import content in consumption)
  - » Norwegians have reduced their consumption abroad by 2.5x more than foreigners have cut their spending in Norway (because Norwegians are spending 2.5 more abroad than foreigners in Norway ☺)
- The **savings rate** fell to 13% in Q3 from 21% in Q2, and probably rose marginally in Q4 – and is way above a normal 5%-9% rate, as consumption is sharply down, incomes not
  - » We expect consumption to normalise the coming quarters, funded by a decline in the savings rate, down to a 'normal' level. Growth in real incomes will be moderate

Investments: Mainland businesses, housing is recovering, oil flattening

Still, all three down in 2020 vs. 2019 (6%, 4%, 5% resp.)

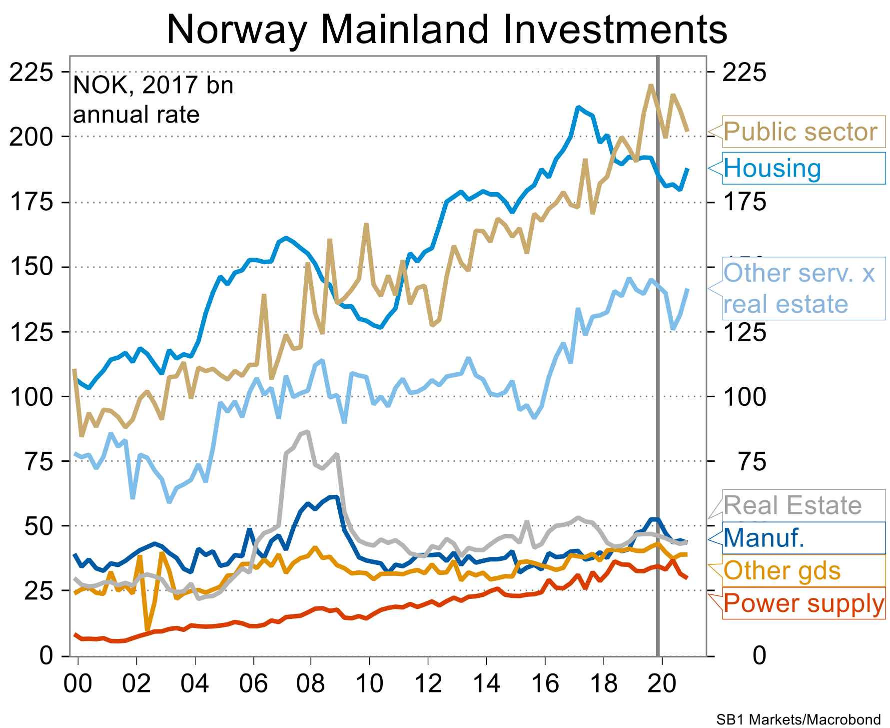


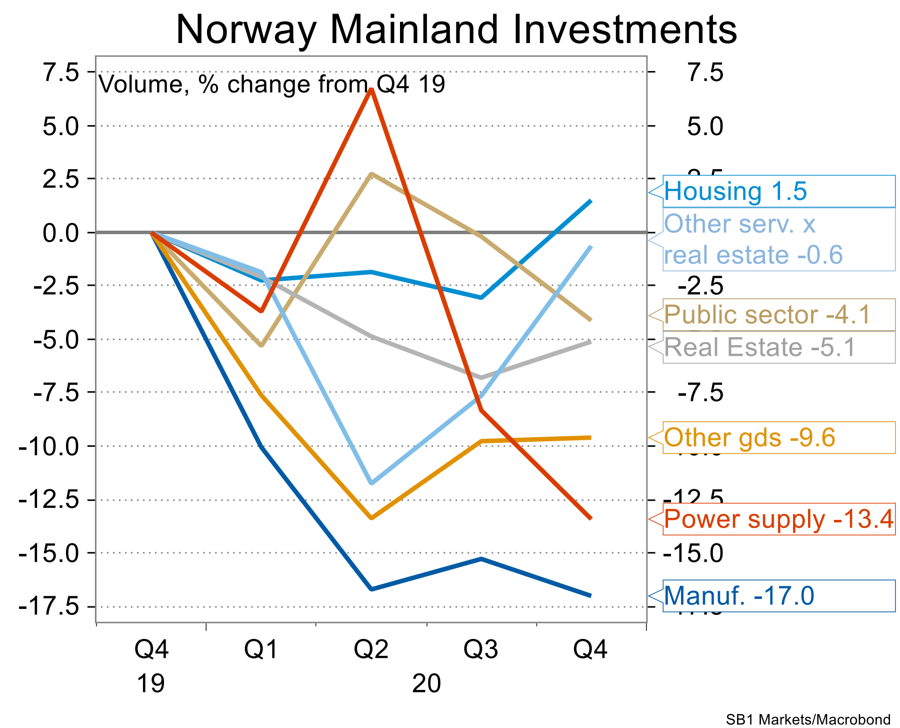


- Both Mainland business, housing, and oil sector investments were headed down, before the corona virus hit, either measured by actual investments (Mainland businesses, housing) and as signaled by investment plans/surveys (oil)
- Oil investments fell by 13% through the year, Mainland businesses by 7% - while housing investments ended up by 1.5%
- *On the outlook, check next pages*

Mainland business investments up in Q3 & Q4: The trough was not that deep?

Mixed between sectors, but in sum business investments are headed upwards

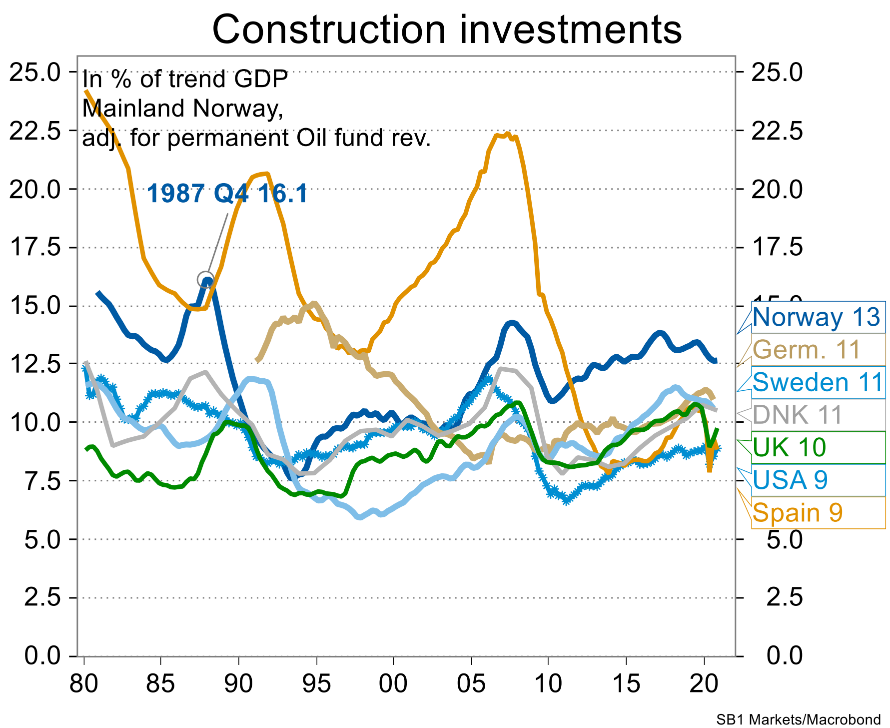


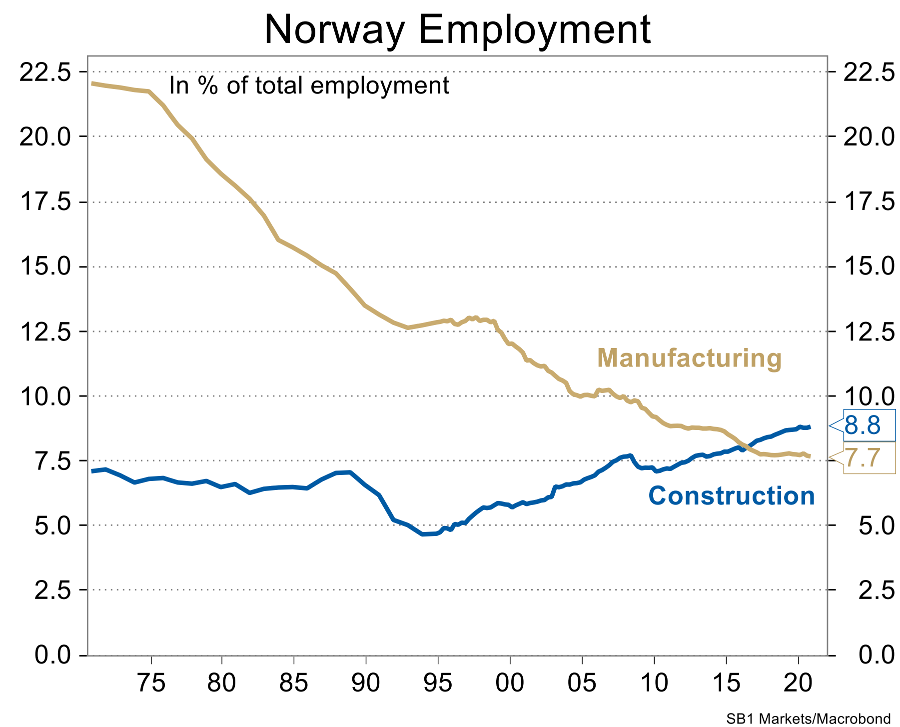


- **Public sector** investments are volatile (F35 fighter imported) but the underlying trend still upwards
- **Housing** investments have been falling since 2017, but recovered sharply in Q4, now up y/y
- Investments in **private services** soared in 2016-2017, then flattened and fell sharply in H1 last year. Almost all of the corona setback was reversed in H2
- **Manufacturing** has fallen 17%, from a high level, through the years, as signalled by investment surveys before the pandemic
- **Real estate** investments are sliding down slowly – The level is not that high, and the downside is probably not that large
- **Power supply** investments fell last year – as signalled by SSB's investment survey

Construction investments have flattened, still at a high level?

Construction activity is probably higher than needed, long term

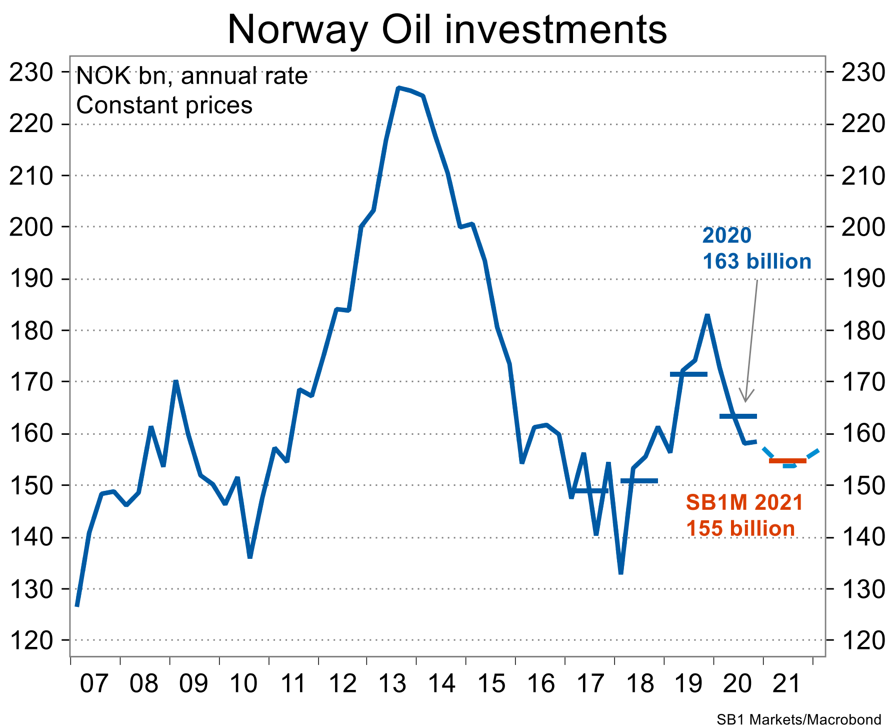


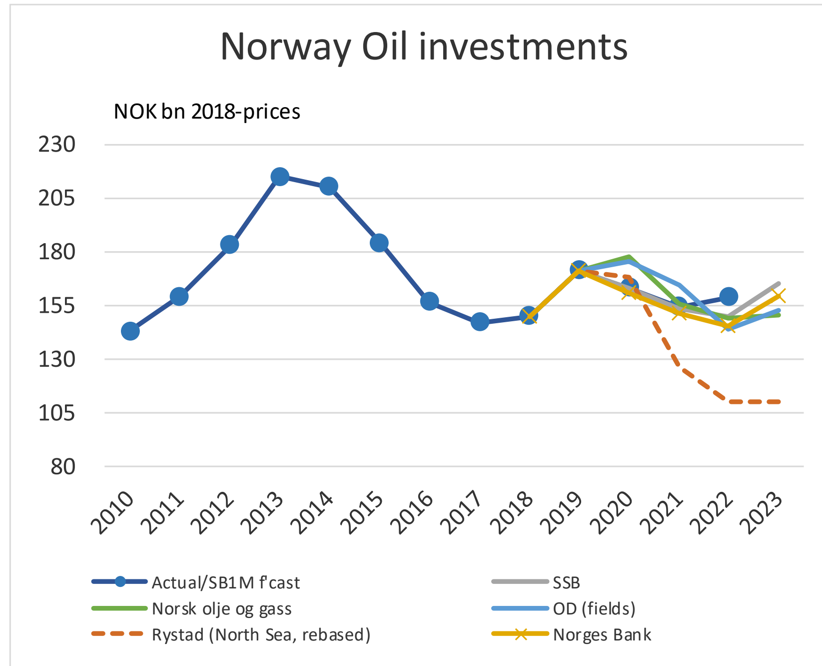


- Construction investments/GDP has flattened but remain at a high level – vs the past 30 y average and vs. other countries
- Construction employment now equals 8.8% of total employment, much higher than anytime before
  - » Construction is larger than manufacturing industries, employment wise, probably for the first time in a civilised country (except Spain and Ireland before the financial crisis)

Oil investments: Flattened in Q4, still down 13% y/y (and 5% y/y in 2020)

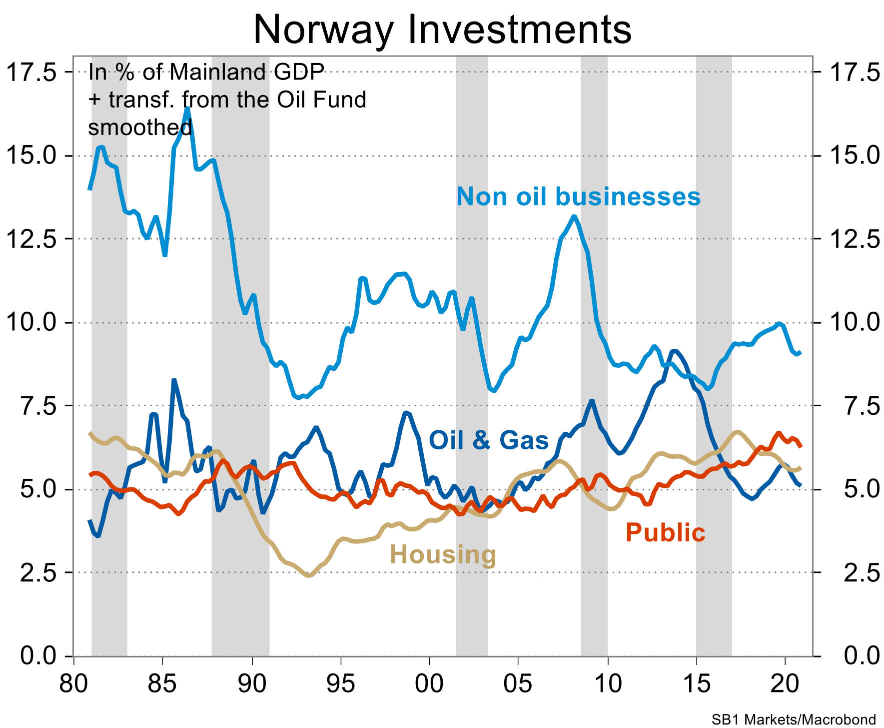
We expect a further decline in ‘21, but less than we assumed: Taxes are cut, oil price at USD 60/b





- We are eagerly awaiting SSB’s Q1 oil investment survey – we have been nudging our forecasts upwards. However, it will take time before the impact of the tax cut & higher oil prices will be visible in total oil investments. (Field exploration/ development investments are probably on the way up already
- The downturn in oil investment in this cycle has been very limited vs the 2013 – 2017 setback

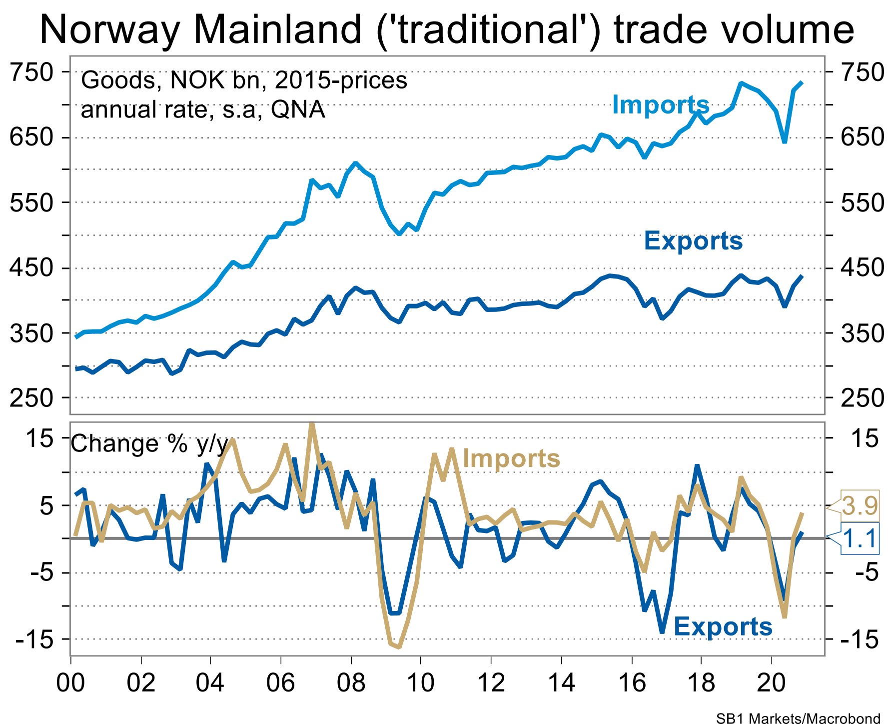
The investment cycles: The outlook is brighter?

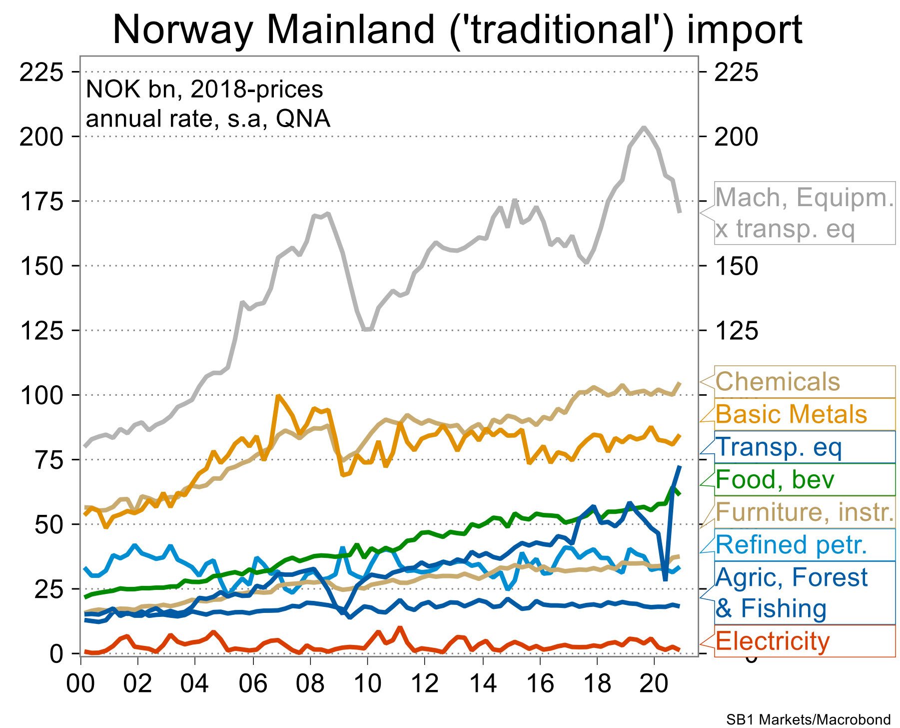


- **Housing investments** have been sliding down since 2017 but remains at a rather high level – and now they are turning up again amid the strong 2nd market – and more new home sales
- **Mainland businesses** peaked before the pandemic, and fell in Q2. However, they are now turning up again. Investment surveys have bottomed – and we expect more to come
- **Oil investments** are now down 13% from the local peak one year ago. Last year's generous tax reform, making it very profitable to start up new projects the coming two years (at least deliver an application, a 'PUD') before 31 Dec 2022), and the oil price recovery will stabilise investments quicker than we assumed last spring
- **Government investments** are the highest in decades, vs GDP. Will come down long term, but limited downside short term

Both exports & imports above pre-corona levels

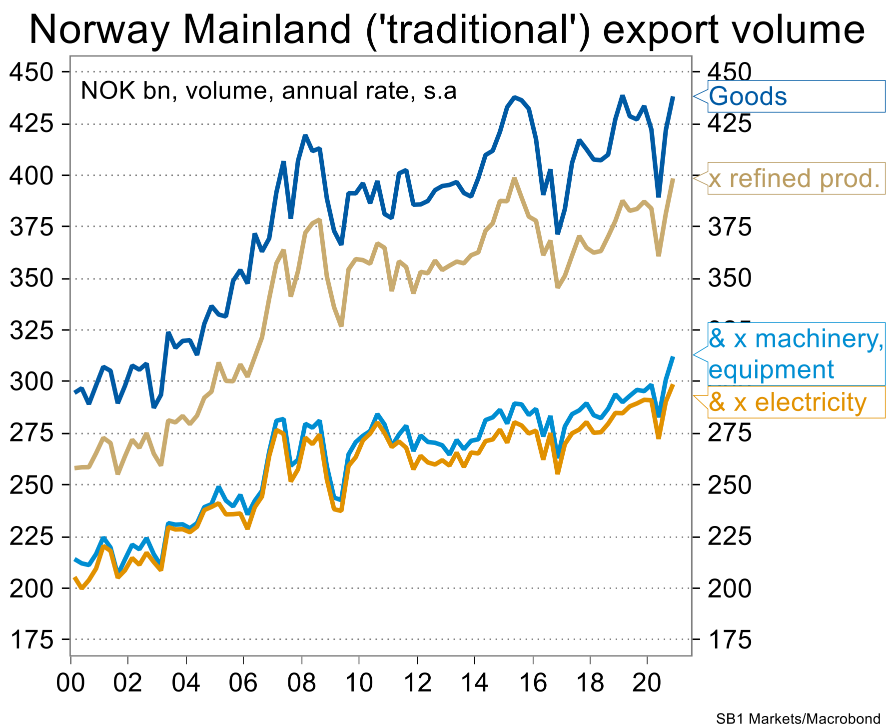
Imports of transport equipment soared in H2. Machinery on the weak side

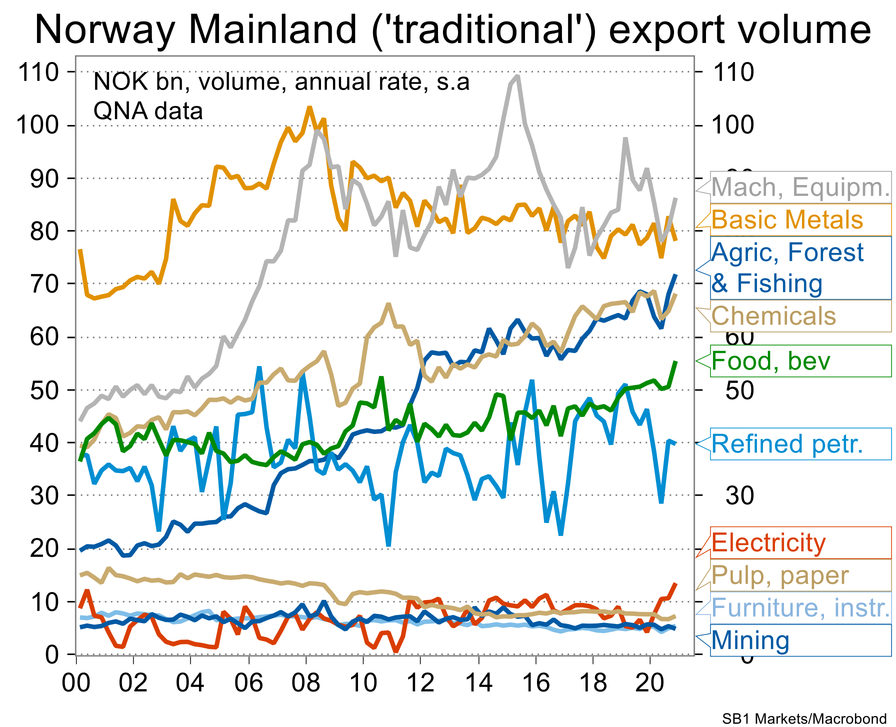




Mainland goods exports ex (oil related) machinery quite impressive

Machinery is still far below previous peaks, many others are on the strong side

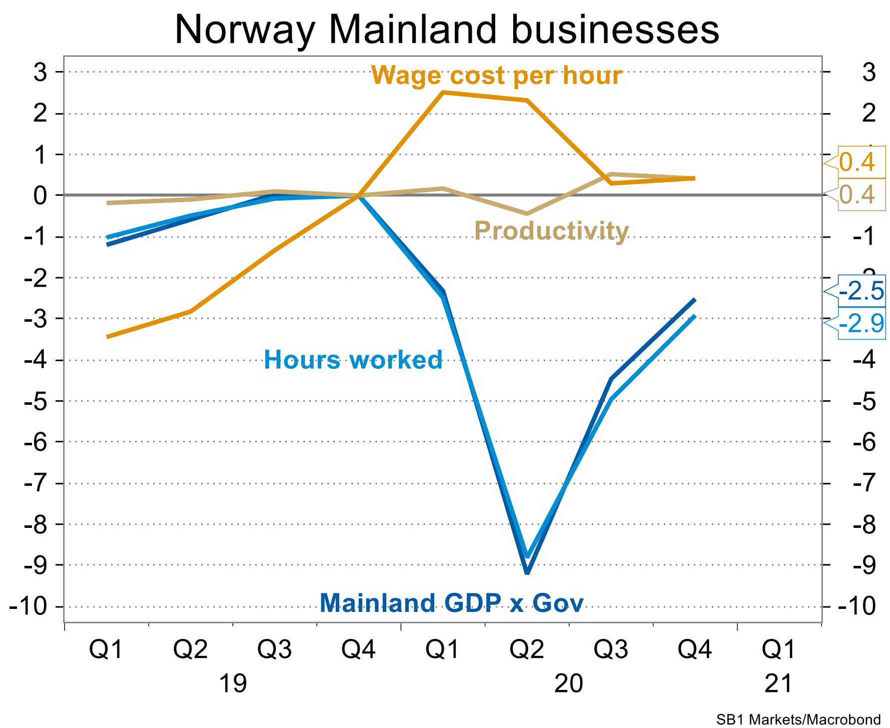


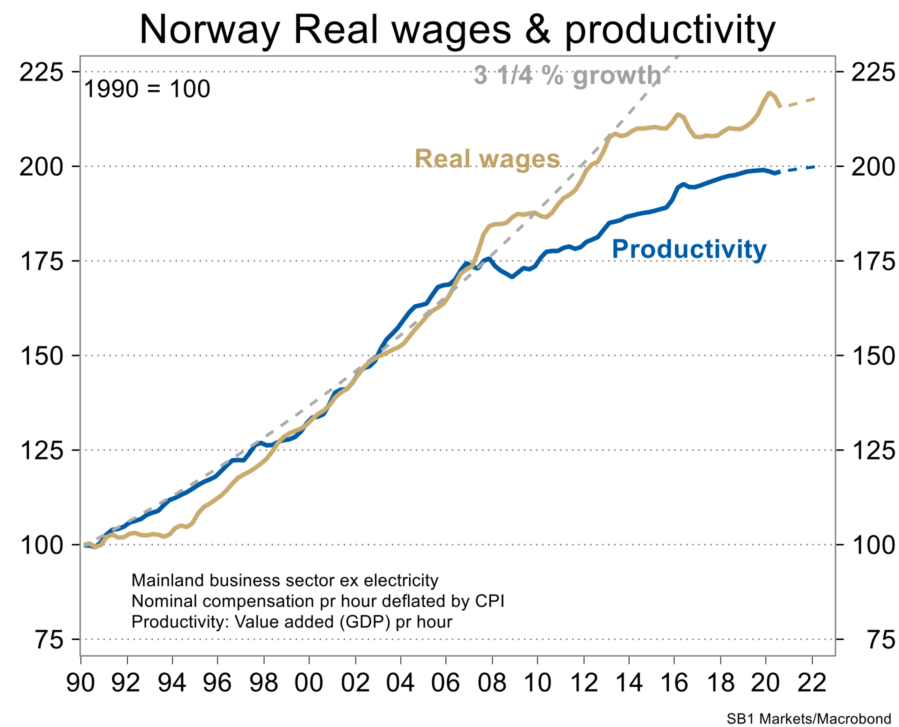


- Much of exports of machinery is oil related - and these markets are not strong these days

Hours track GDP – productivity just up 0.4% through last year, not unlikely

Still, we take these data with a grain of salt – both production, ours worked and average wages

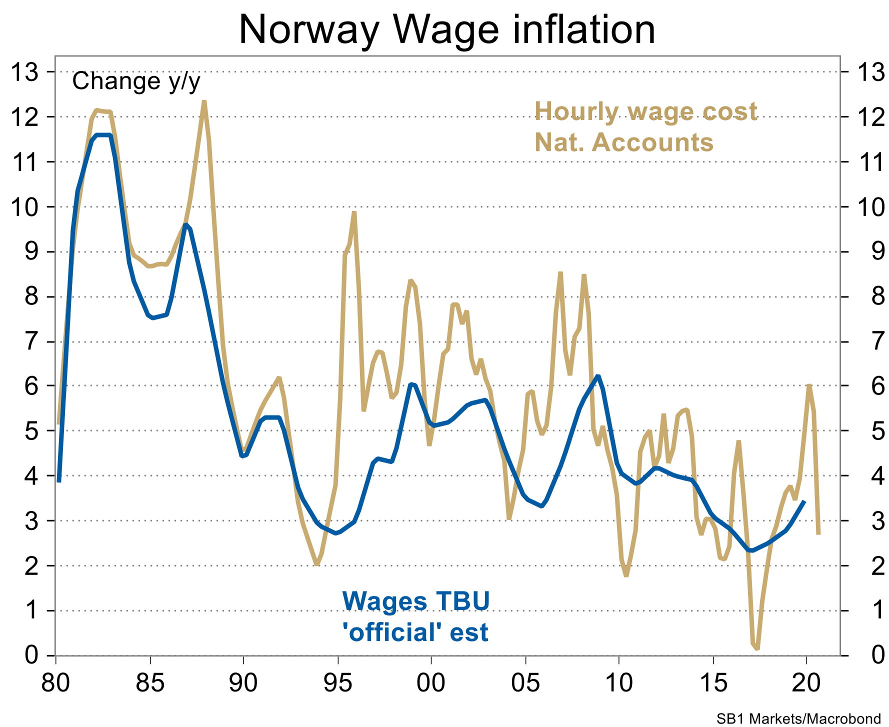


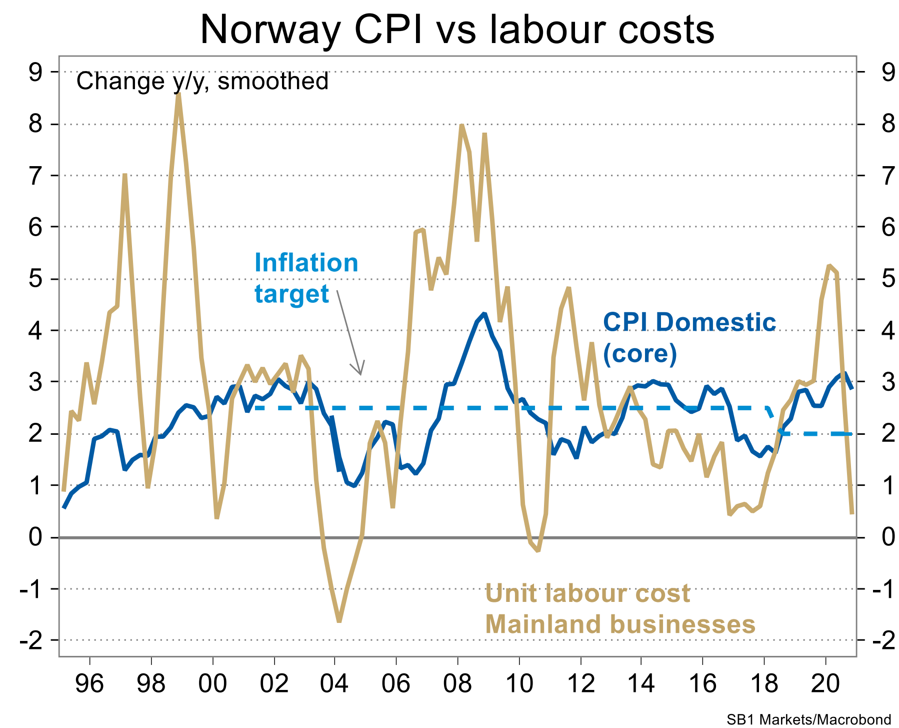


- Changes in **hours worked** in the private sector have been quite equal to changes in production in the business sector
- Thus, **productivity** has been flat since Q1 2019
- The **average hourly wage** rose sharply in Q1, but fell in both Q2 and Q3, while rising slowly in Q4, according to the National accounts. These data are influenced by government measures, like how the furlough program is booked
- We do not expect **real wages** to show strength the coming quarters. Wage inflation has slowed, and will probably not pick up sharply this year. Headline inflation will – at least for a while – get a boost from electricity prices – and those prices will most likely not turn negative y/y and core inflation will not collapse. The underlying weakening of corporate profitability may also contribute to keep inflation up – as may the post-corona recovery in domestic demand

Labour cost inflation is slowing – but unit costs are still up quite a lot

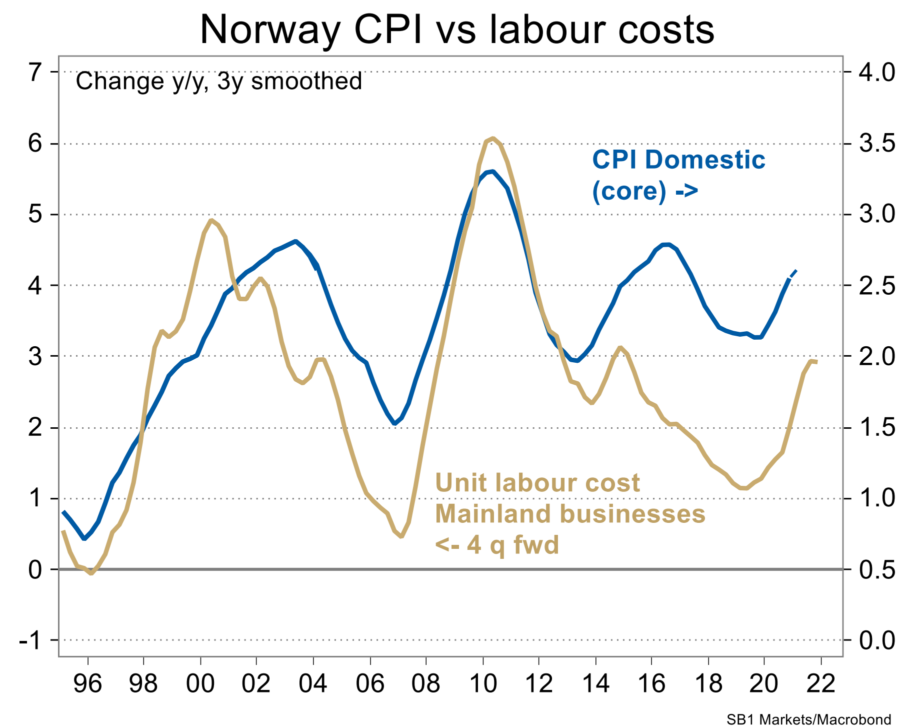
The corona downturn makes most data uncertain, including these wage & productivity data





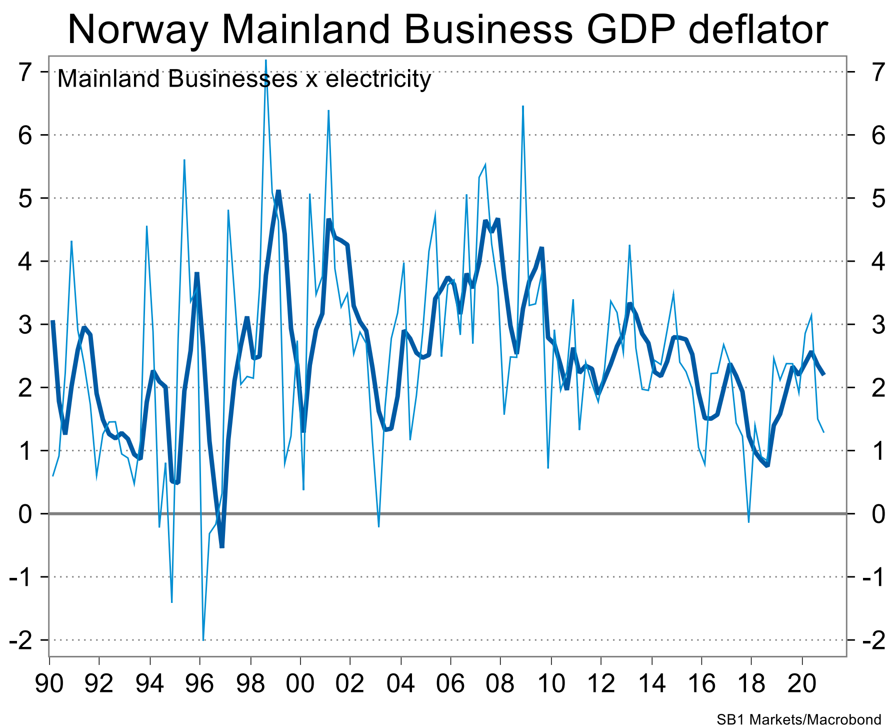
- Quarterly hours worked & payments are always volatile – and there are extra challenges now
- We are confident that underlying wage inflation is slowing – as witnessed by the outcome 2020 wage negotiations

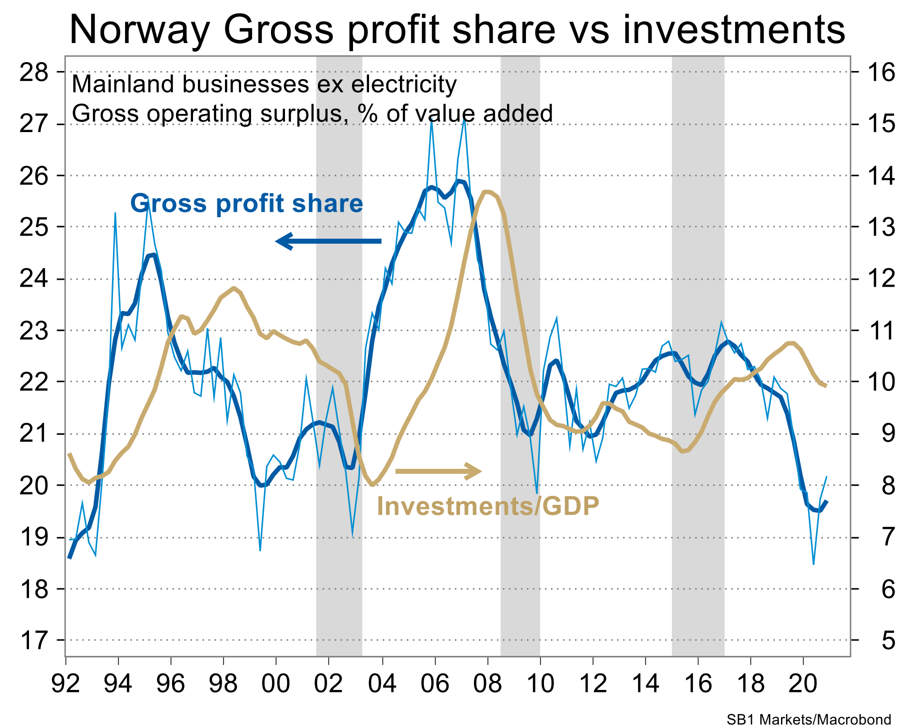
Over time, costs are important for inflation



The profit share was under pressure, before corona – and fell further

Profits recovered in Q3 and Q4, partly supported by gov't subsidies

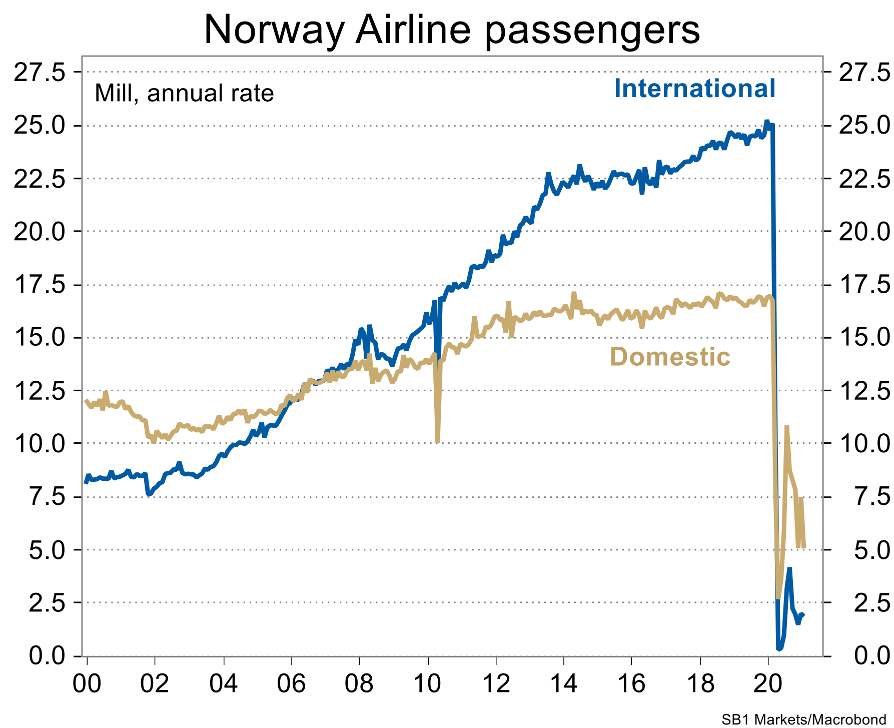


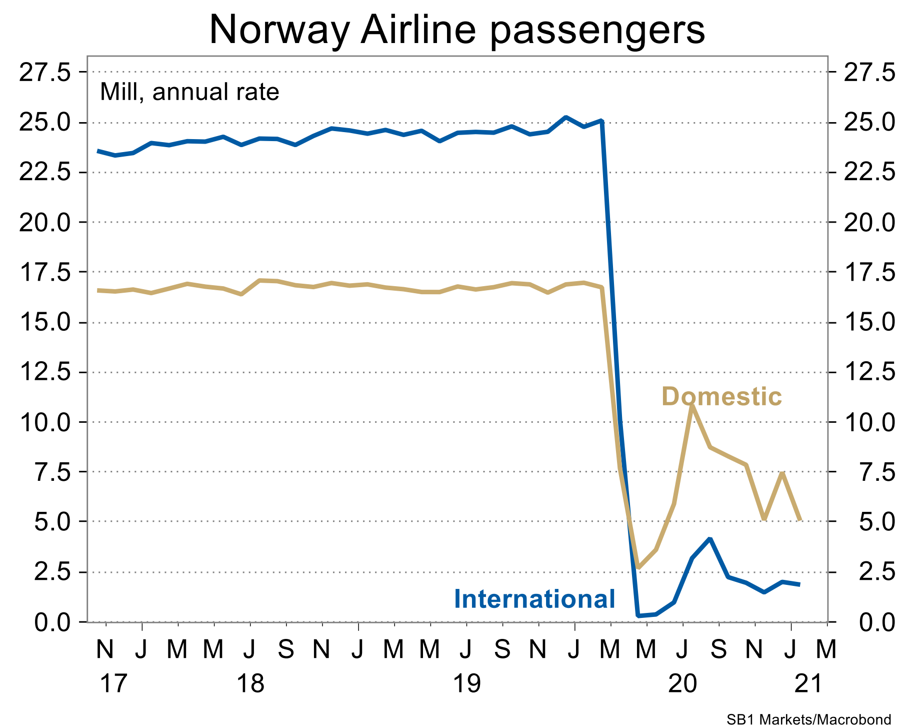


- Increased transfers to the business sector lifted gross operating profits by NOK 20 bn last year, equalling 5% of gross profits or 1% of value added. (In the US, the comparable figures are at least five times larger)
- The Mainland business GDP price deflator (ex the volatile electricity sector) slowed through last year but smoothed it is still above 2%

Air traffic down again in Jan – domestic -71% y/y, international -92%

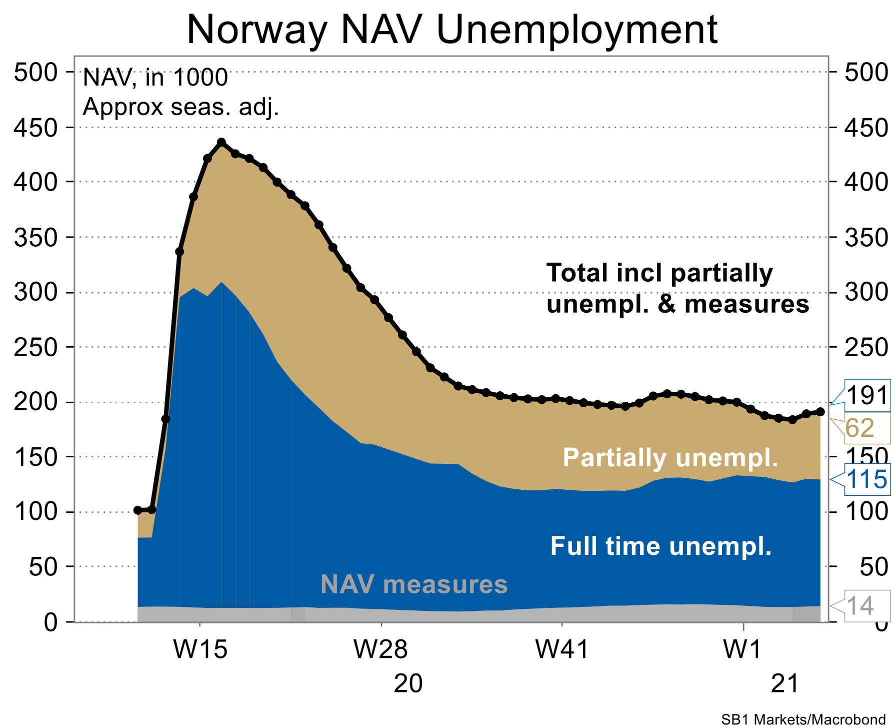
Traffic fell m/m too, but the negative m/m GDP drag is very limited, as the level is so low

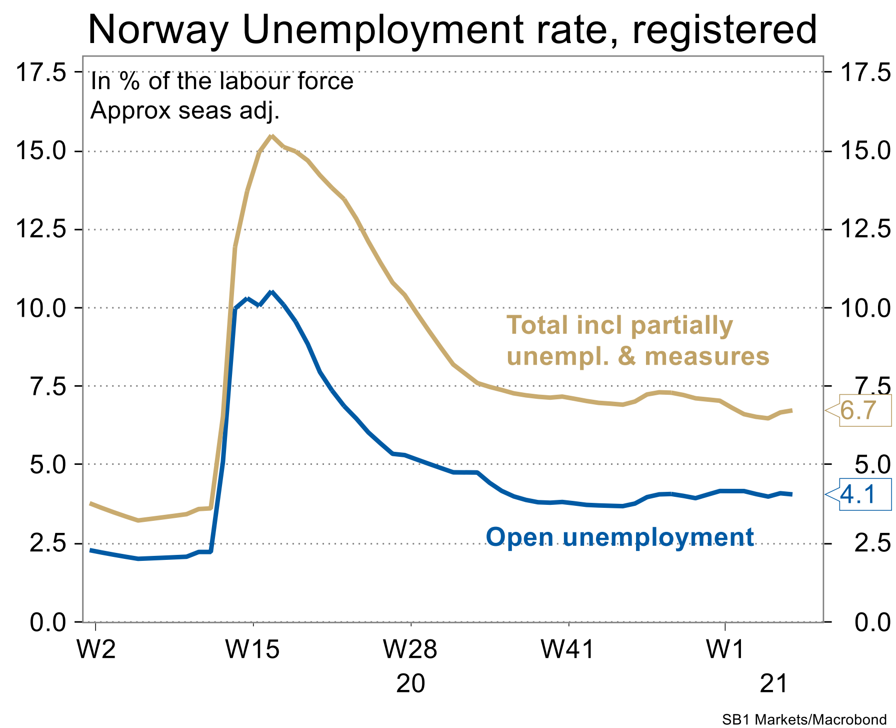




NAV weekly unemployment close to flat

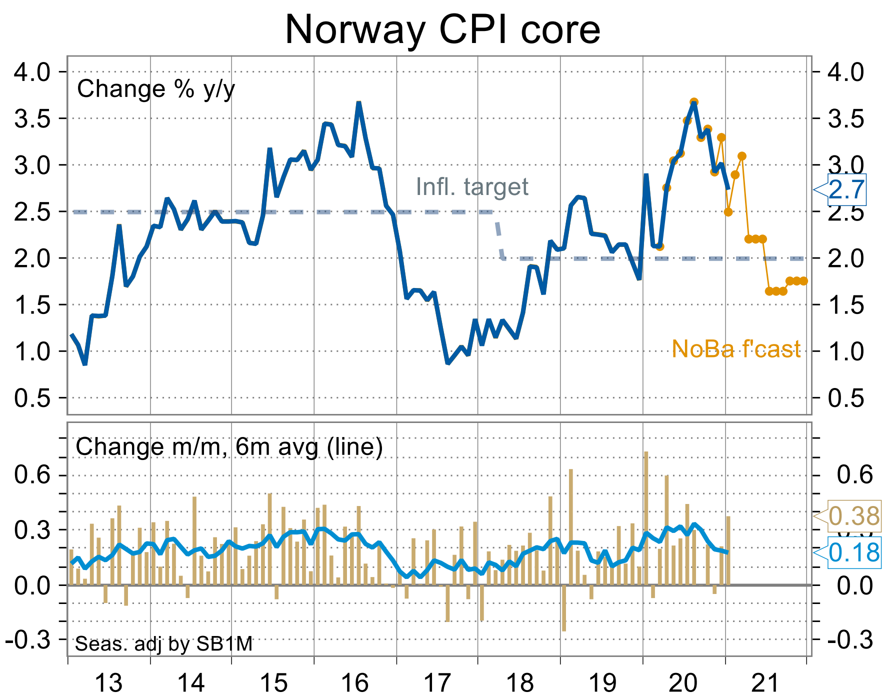
.. Adjusted for the normal seasonal pattern. Confirming no big hit due to the tightened restrictions

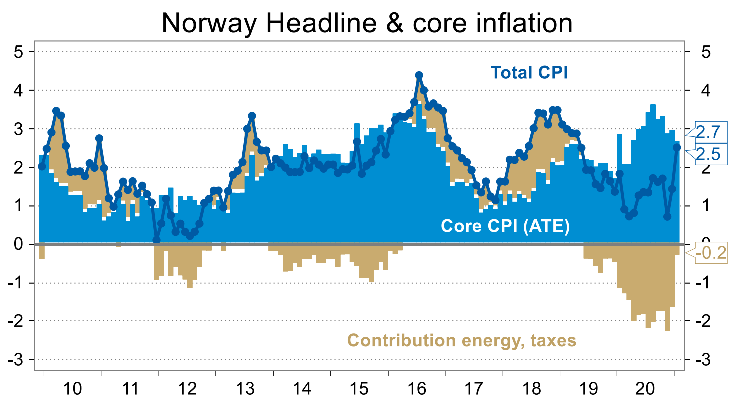




Inflation surprised on the upside in January

Core inflation fell but less than expected, and total inflation was far higher than we expected





- CPI-ATE (ex. energy and taxes) inflation fell 0.3 pp to 2.7% in January; a print far above consensus (2.4%) and our forecast (2.3%). Norges Bank expected 2.5% (Dec MPR f'cast)
  - » Prices rose 0.4% m/m (s.a)
  - » Airfare ticket prices were higher than we expected, as were food and clothing prices
  - » Inflation is below 2% for housing, clothing, alcohol , and airline tickets – all others are still above
  - » Imported goods price inflation fell in Jan, and will recede further as NOK effect fades
- Total inflation accelerated 0.9 pp to 2.5%, far more than we expected as electricity prices rose more than we assumed. They are now up 19% y/y, up from down 21% last month
- **The price outlook**
  - » We expect inflation to slow the coming quarters as the NOK effect fades and wage inflation remains muted. Demand for goods will have to decline from a very high level, while the 'beaten down services' will not have pricing power anytime soon, even if demand should pick up steam during Q2/Q3
  - » Anyway, CPI inflation will not have any material impact on Norges Banks and monetary policy the coming months. It's all about the Covid-19 impact on the real economy. When the war on corona is won, we think the housing market will become more important for Norges Bank than actual inflation

Far stronger increase in energy prices than expected – Total CPI at 2.5% in Jan

Prices of airfare, food, and clothing surprised on the upside

Jan-21 CPI ATE	Weight %	Change m/m, seas. adj Out-come	Change m/m, seas. adj SB1M f'cast	Change m/m, seas. adj Dev. pp	Change y/y Last month	Change y/y Out-come	Change y/y SB1M f'cast	Contribution, pp m/m	Contribution, pp y/y	Contribution, pp Dev. vs f'cast
Food, non alc bev	13.0	0.4	0.2	0.2	3.2	2.6	2.2	0.06	0.34	0.03
Alcohol, tobacco	4.3	-0.2	0.2	-0.4	2.5	1.9	2.4	-0.01	0.08	-0.02
Clothing, footwear	4.9	1.6	0.0	1.6	-2.8	-0.6	-2.5	0.08	-0.03	0.08
Housing x. energy	20.5	-0.0	0.2	-0.2	1.2	1.0	1.2	-0.01	0.21	-0.04
Furnishing	6.8	0.2	0.3	-0.1	8.0	6.2	5.3	0.01	0.42	-0.01
Health	3.2	0.5	0.2	0.3	1.7	2.0	1.6	0.01	0.06	0.01
Transp. ex. gas, airl. tick	12.0	0.1	0.3	-0.2	5.2	4.7	5.2	0.01	0.56	-0.03
Airline tickets	1.0	1.8	-5.0	6.8	-11.7	-13.4	-19.8	0.02	-0.14	0.07
Communication	2.5	0.2	0.3	-0.1	2.7	2.6	2.7	0.00	0.06	-0.00
Recreation, culture	11.2	0.5	0.2	0.3	4.8	4.5	4.3	0.06	0.50	0.03
Education	0.5	-	-	-	2.1	2.1	2.1		0.01	0.00
Restaurants, hotels	5.9	0.4	0.2	0.3	3.1	3.5	3.2	0.03	0.21	0.02
Other	8.7	0.2	0.3	-0.1	4.1	2.9	3.1	0.01	0.25	-0.01
CPI-ATE	94	**0.4**	**0.1**	0.2	**3.0**	**2.7**	**2.3**			
Norges Bank est.			**0.3**				***2.5***			
Imported	34	0.4	0.1	0.2	3.7	3.3	3.1	0.12	1.12	0.08
Domestic	60	0.4	0.1	0.3	2.7	2.4	2.1	0.24	1.48	0.16
Energy, housing	4	31.3	18.0	13.3	-21.1	18.9	4.4	1.12	0.68	0.48
Energy, transport	3	6.6	2.0	4.6	-7.6	-3.9	-8.0	0.21	-0.12	0.14
CPI Total	101	**1.3**	**0.8**	0.5	**1.4**	**2.5**	**1.9**	1.34	2.54	0.52

Change m/m based on seasonally adjusted data (calc by SB1M)
Sum of parts does not necessarily add up to totals
Norges Bank m/m s.a. estimate is implied, calc by SB1M

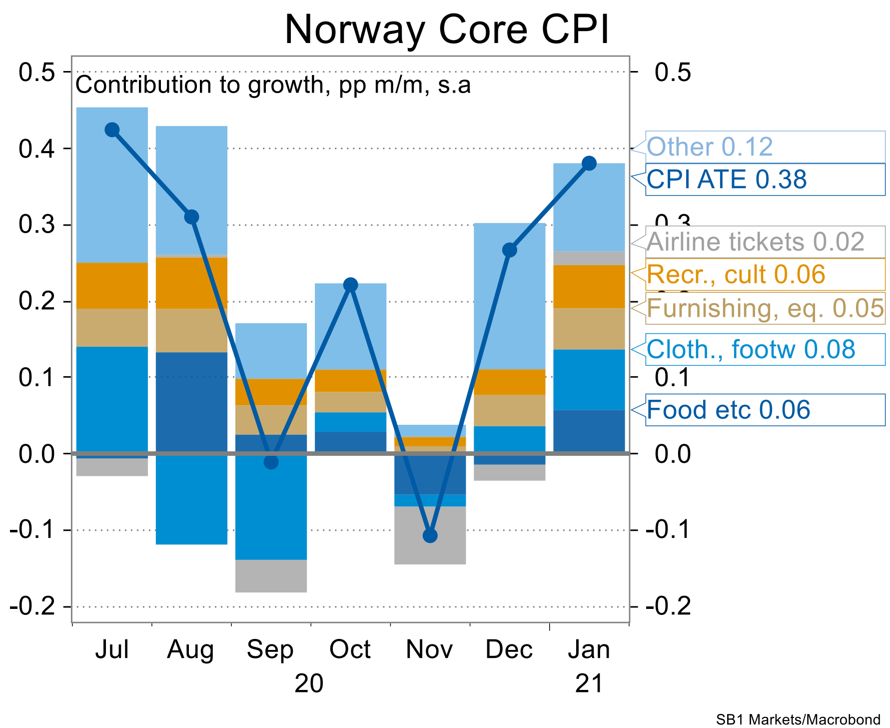
- Food price inflation is down to 2.6%, but above our f'cast
- Clothing prices are down 0.6% y/y, up 2.2 pp since Dec, following a 1.6 lift m/m
- Furniture/hardware/equipment prices are up 6.2% y/y!
- Transport ex. gas/airline – mostly cars – rose 4.7% y/y
- Airline ticket prices were up 1.8% m/m, far stronger than expected.
- Prices of games, toys and books increased significantly in January
- Restaurant price inflation was higher than expected. Hotel prices are still falling, but less than in the previous months. Bottoming out?

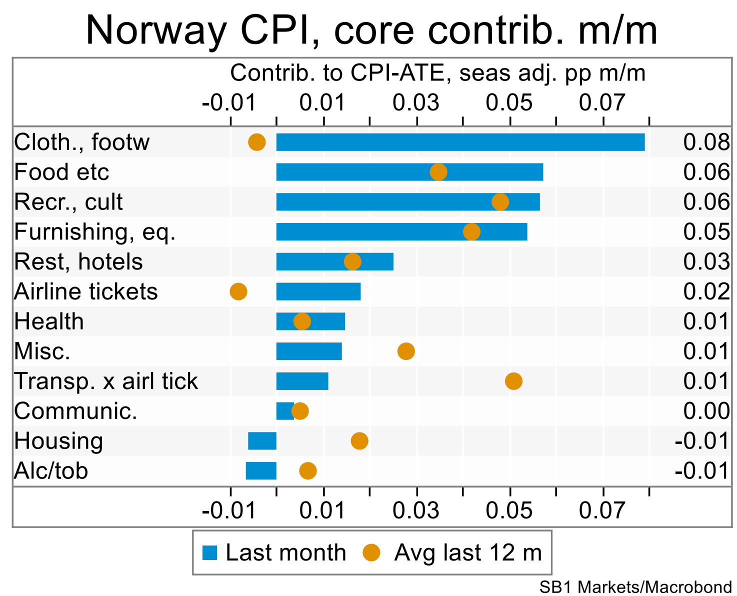
- **CPI-ATE up 2.7% y/y, 0.4 pp above our expectations!**
- Prices on imported goods rose by 0.4% m/m and the annual rate fell by 0.4 pp to 3.3%. Will probably slow as the NOK impact fades
- Domestically produced goods & services rose by 0.4% too. The annual rate is down by 0.3 pp to 2.7%, still a high number!
- Electricity prices rose by 31% in Jan, far more than we expected
- **… and so the headline inflation came in at 2.5%, higher than our estimate at 1.9%**

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

Clothing, food, toys, games and books big contributors

Prices of airline tickets rose for the first time since August





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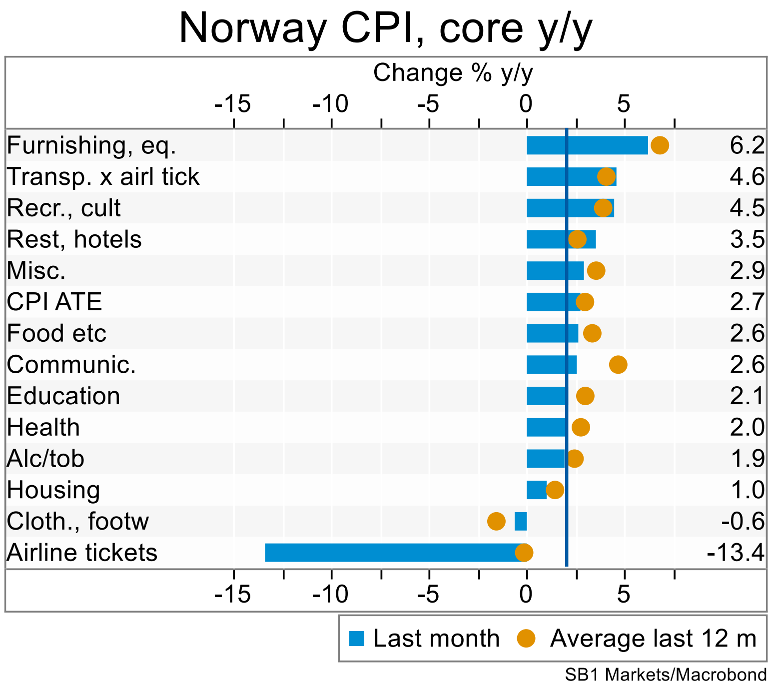
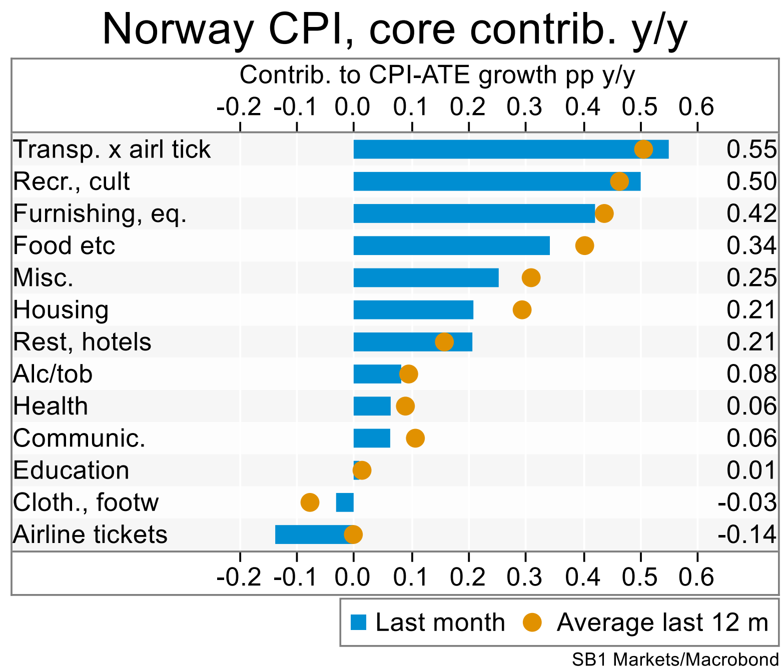
Most sectors report inflation above 2%

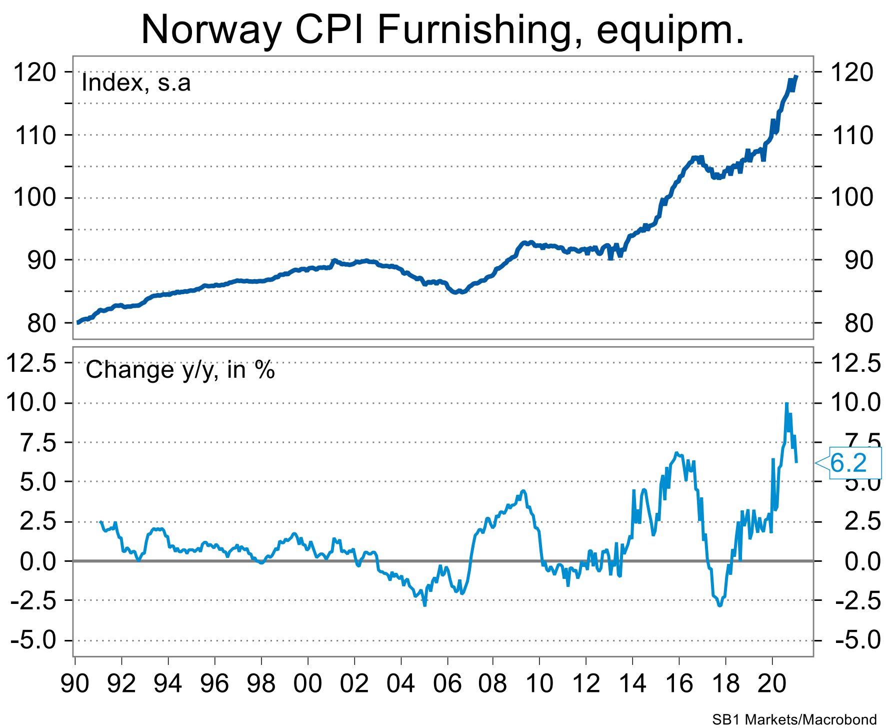
Just clothing & footwear, housing (rent), alcohol, and airline tickets < the 2% infl. target

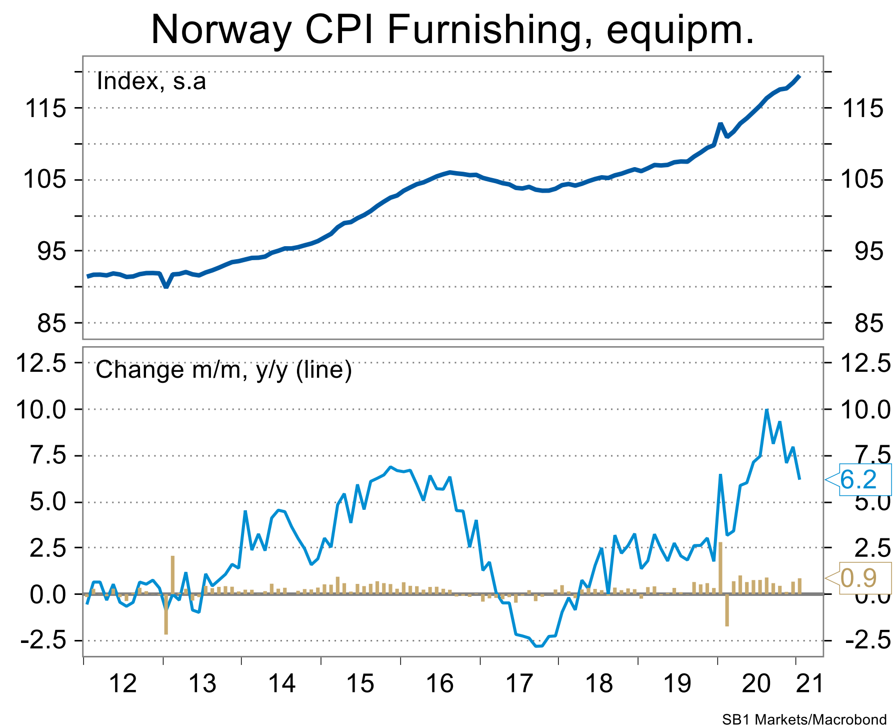




After dipping in Nov, furnishing prices up 0.2% m/m in January

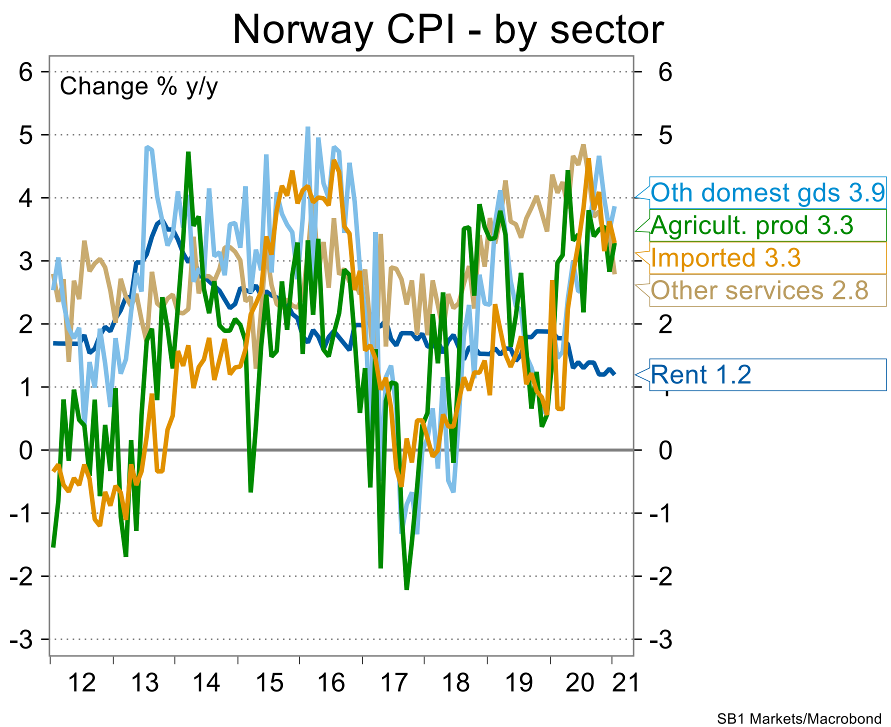
Prices are still up 6% y/y. We expect furnishing price inflation to taper further

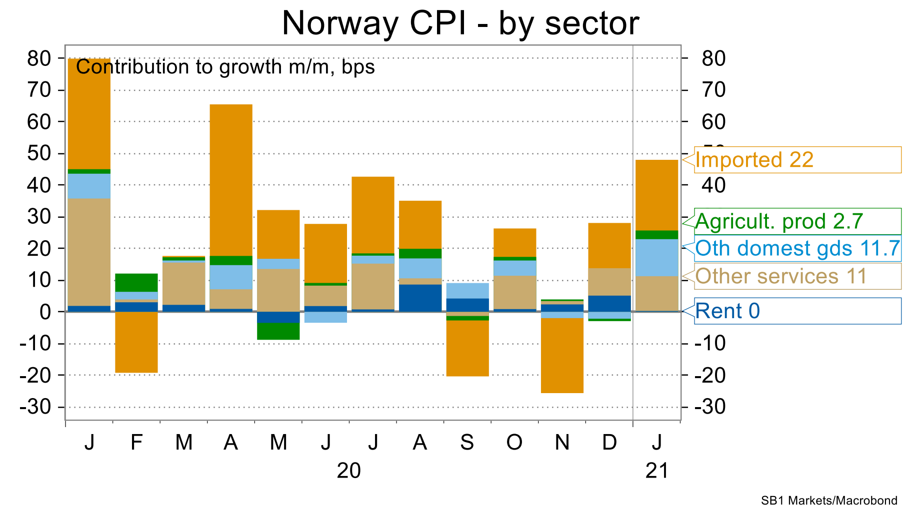


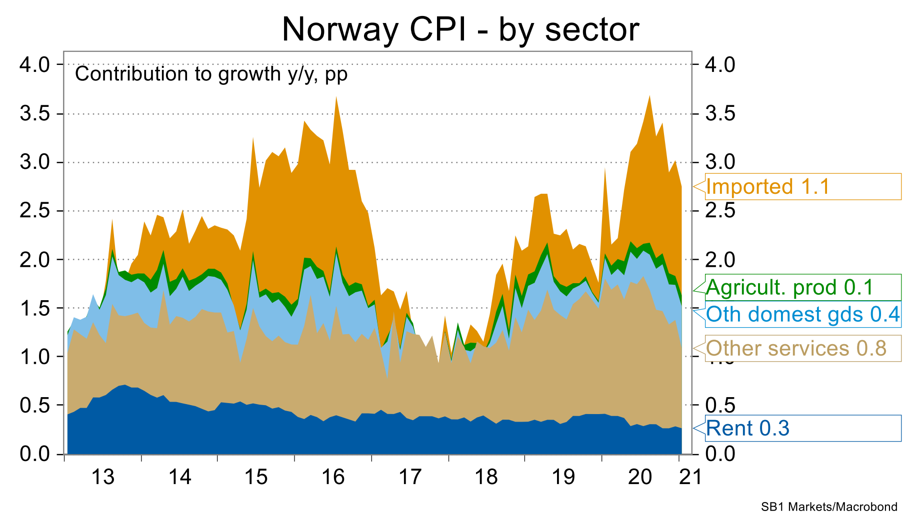


Imported goods prices up 0.4% m/m – and are up 3.3% y/y

Should shrink with a stabilisation/strengthening of NOK. Domestic inflation is also up



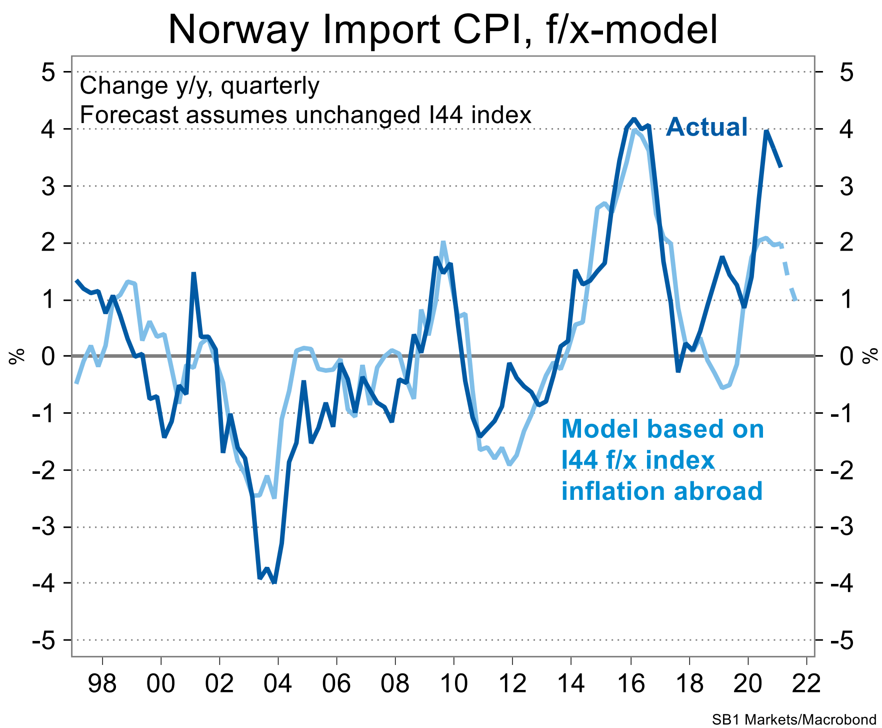


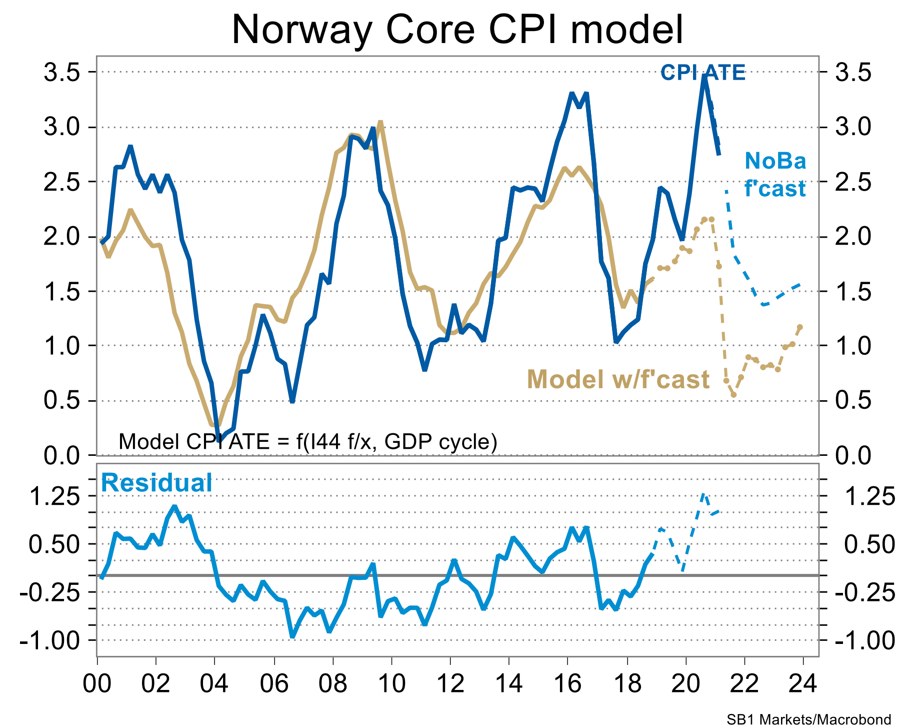


- Imported goods are up 3.3% y/y - however, down from 4.7% some few months ago

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

Our total core CPI model is not calibrated for a huge decline in GDP, but the sign is probably correct

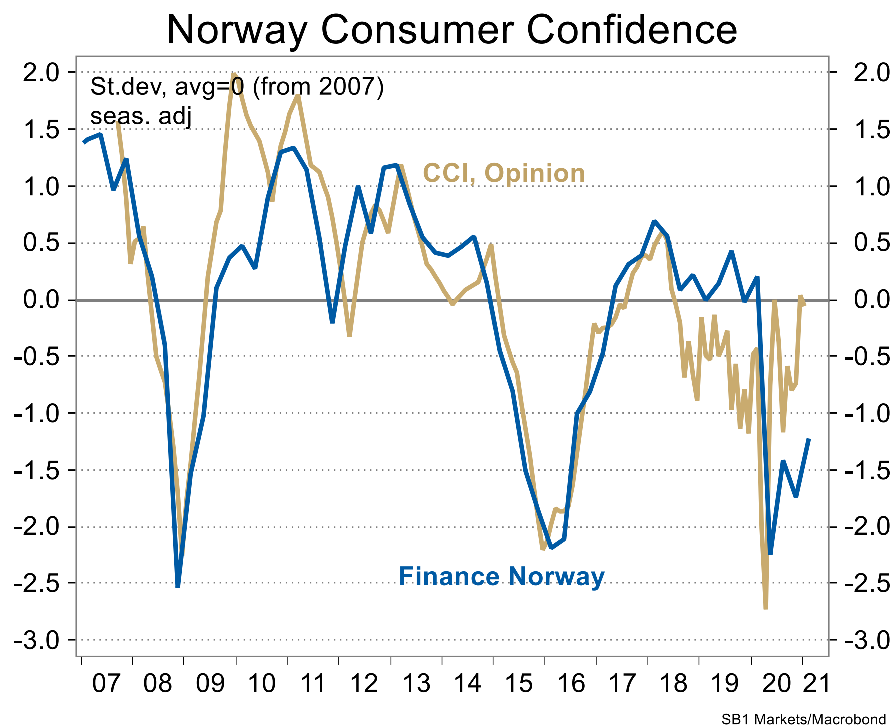


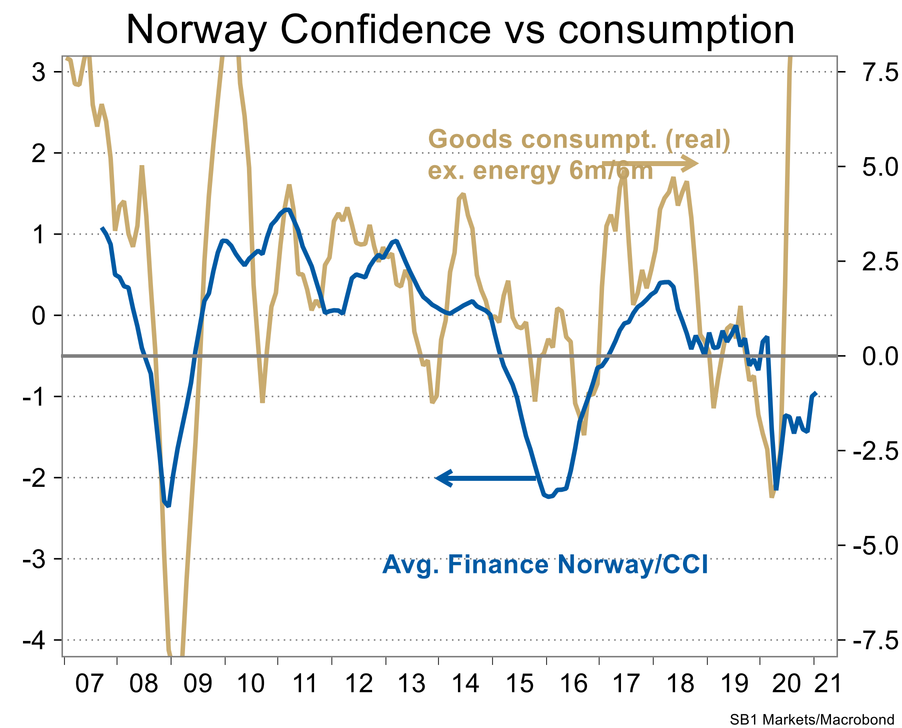


- The NOK steep depreciation in early 2020 has no doubt been driving **imported inflation** up. It usually takes a few months before these impacts are reflected in the CPI. Closed borders/supply chain challenges due to Covid-19 may have contributed to the lift in import prices too, and more importantly: <u>the strong growth in demand for some goods</u> (like sport equipment/furniture)
  - » Still, given moderate inflation abroad and a stabilisation of the NOK exchange rate, we expect imported inflation to slow the coming months – and quarters
- Domestic inflation will be kept in check due to low wage inflation – and total inflation will come down, as signalled by our **total core CPI** model (to the right)

Consumer confidence improved but still pessimistic

Finans Norges' Q1 survey surprised (us) on the downside





- Finance Norway's quarterly consumer confidence index rose from -1.8 st.dev below par to -1.2 in Q1. We expected up to -0.9. A bit surprising, given that the opinion CCI rose sharply, and is not at an average level. The unemployment rate has risen following the latest corona wave, but only marginally. Virus mutations and increased restrictions for large parts of the population may have impacted the survey
- More people are now saying that they want to spend on travel, and they considering large items purchases.

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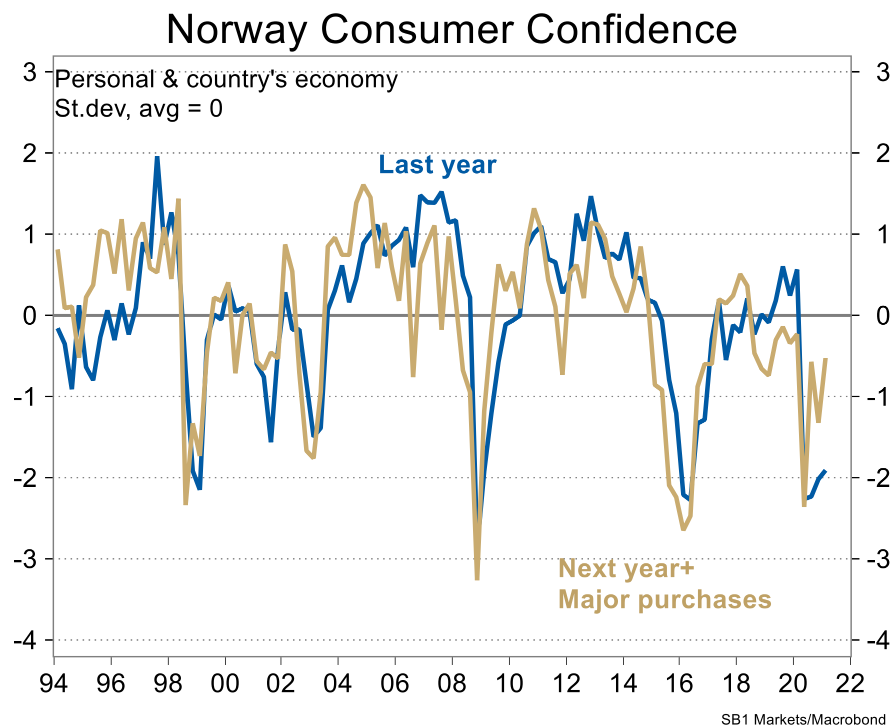
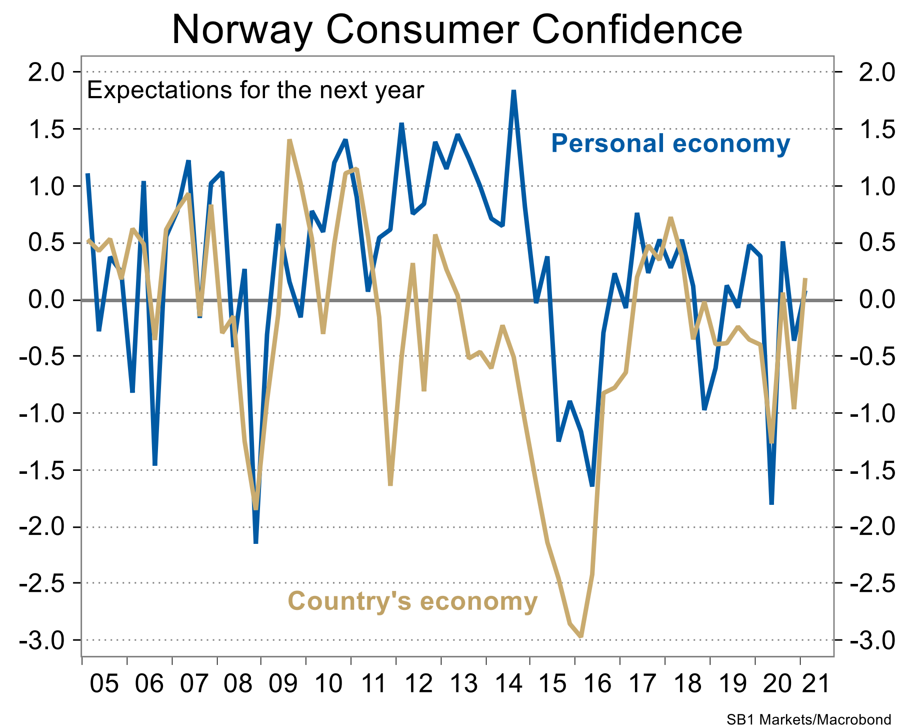
Outlook is brighter, but households assessments of the past year still weak

The anticipation of vaccination seems to put a positive spin on sentiment





- The **forward looking components** in the index (equally weighted by us) rose in Q1, but the level is below average
- Household expect their **personal economy** to be somewhat stronger than normal the coming year – as is their assessment of the outlook for the country. More households think the timing for buying big ticket items is favourable
- There are no recognisable **regional, age or income** differences, as usual

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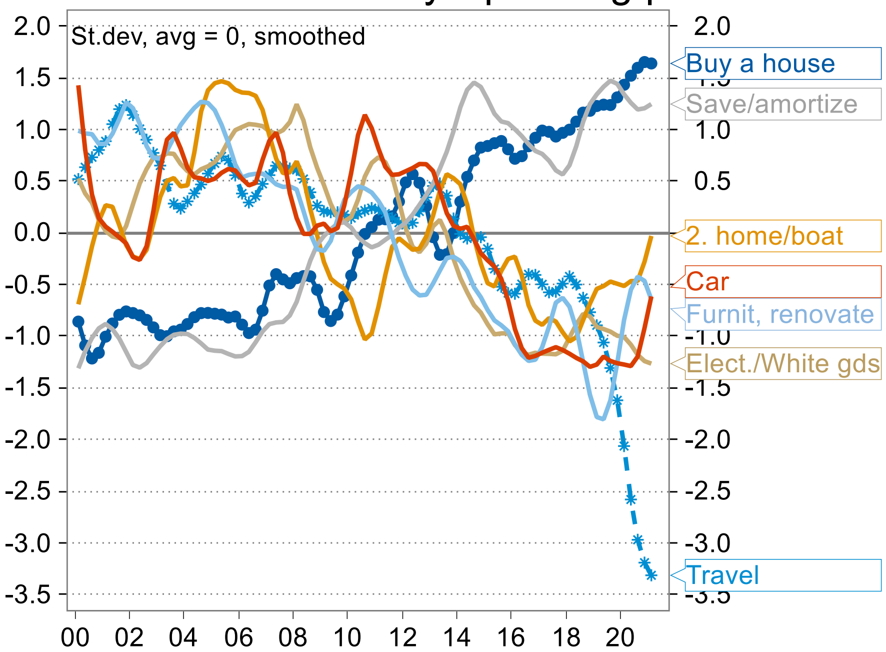
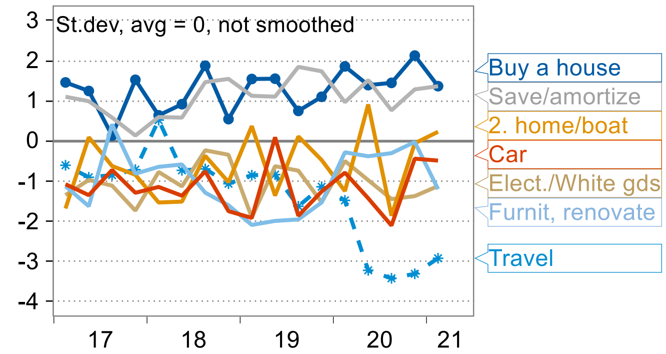
People are done renovating

…and the vaccine is welcome as (a tad more) people want to spend money on travel

Finance Norway Spending plans



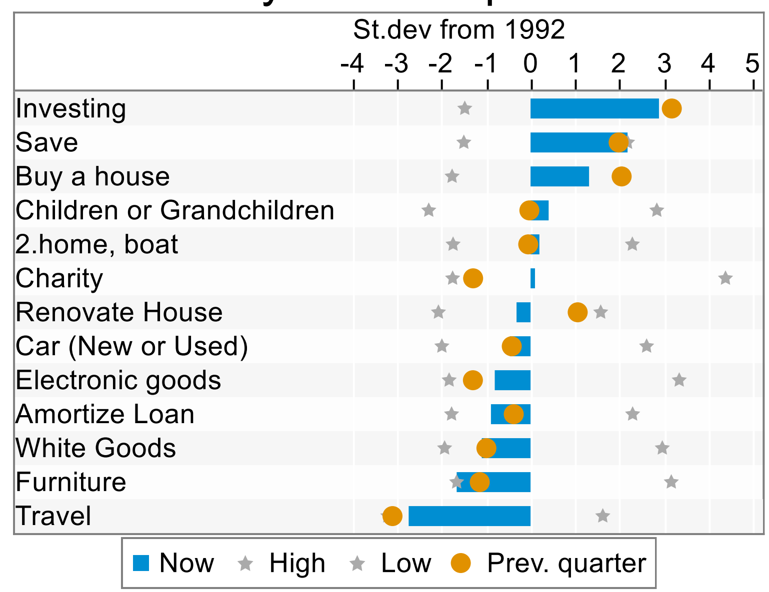
SB1 Markets/Macrobond



SB1 Markets/Macrobond

- Less need for down payment on mortgage while the demand for big items seems to be ticking up. And there is a limit to how much Norwegians can renovate their houses.

Norway How to spend it?



SB1 Markets/Macrobond

Highlights

The world around us

The Norwegian economy

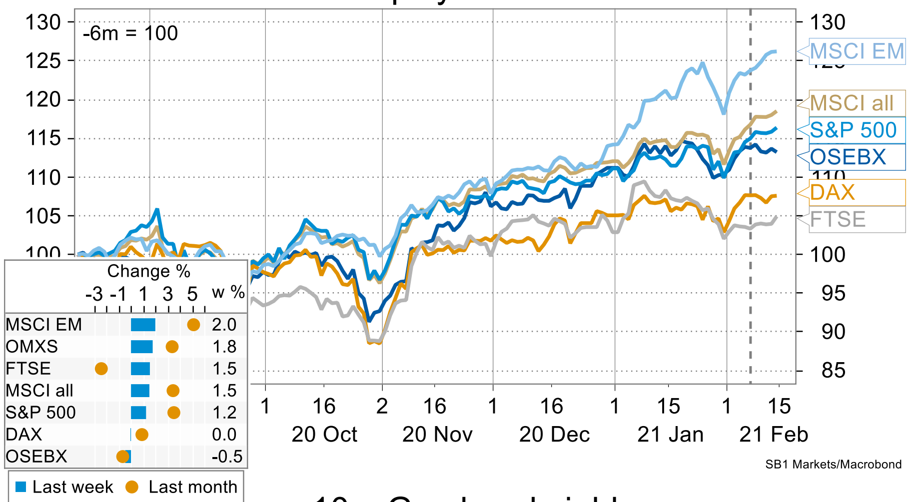
Market charts & comments

SpareBank 1 MARKETS

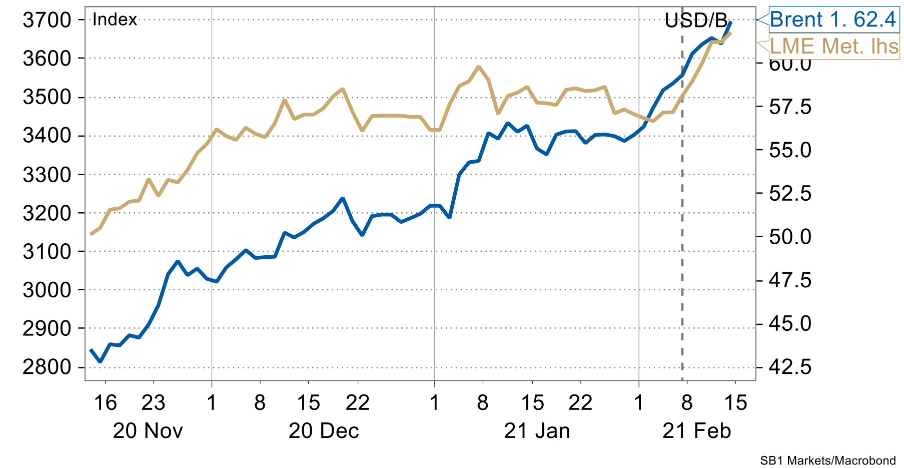
Stimulus bonanza? Equities up on the week – at record volumes in the U.S.

Oil at above USD 60/b! Yields still flattish; NOK stronger; USD weaker again

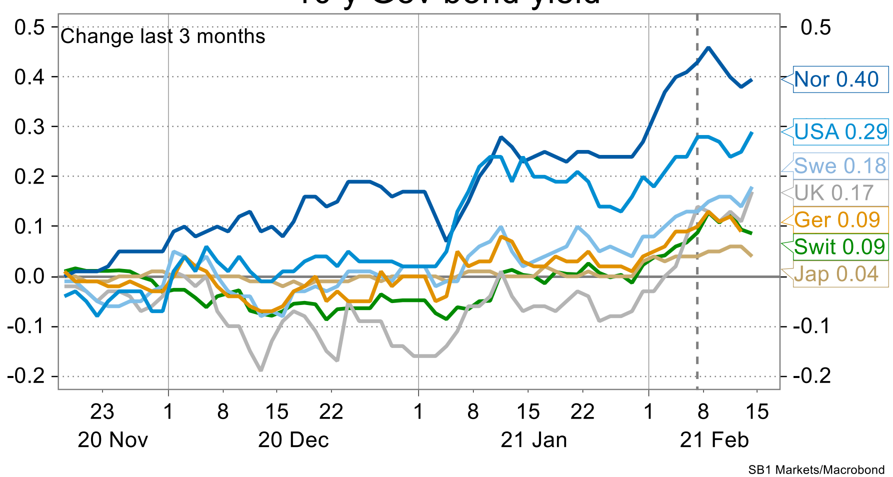
Equity Indices



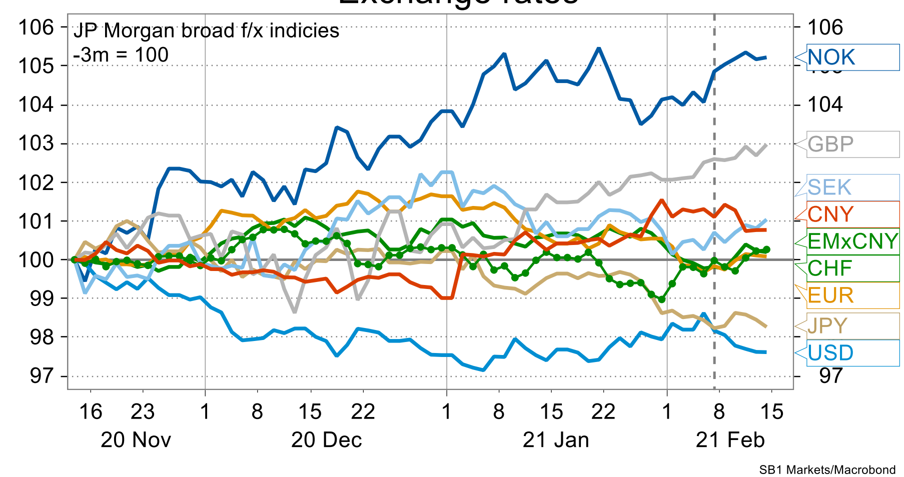
Oil vs. metals



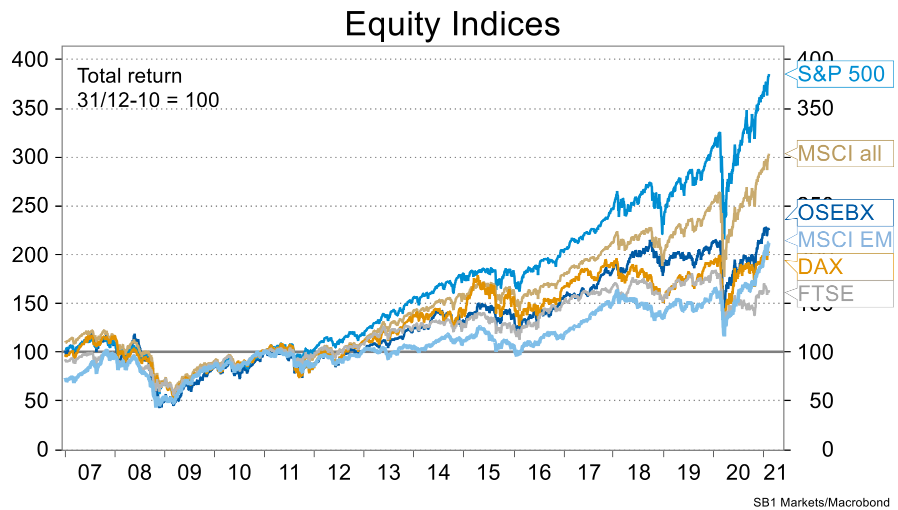
10 y Gov bond yield

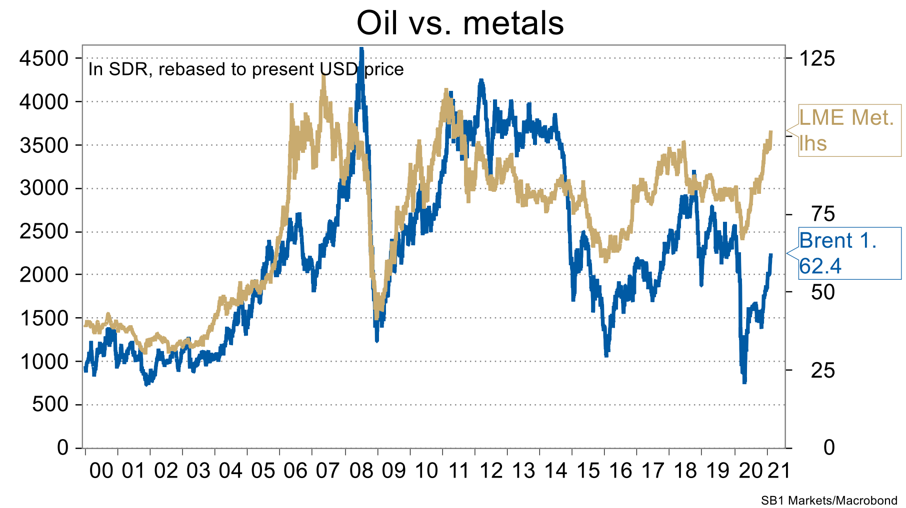


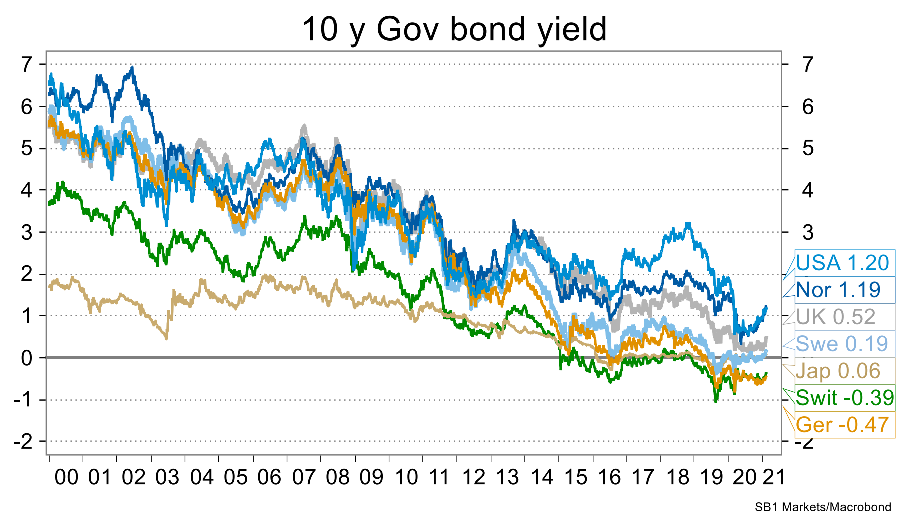
Exchange rates

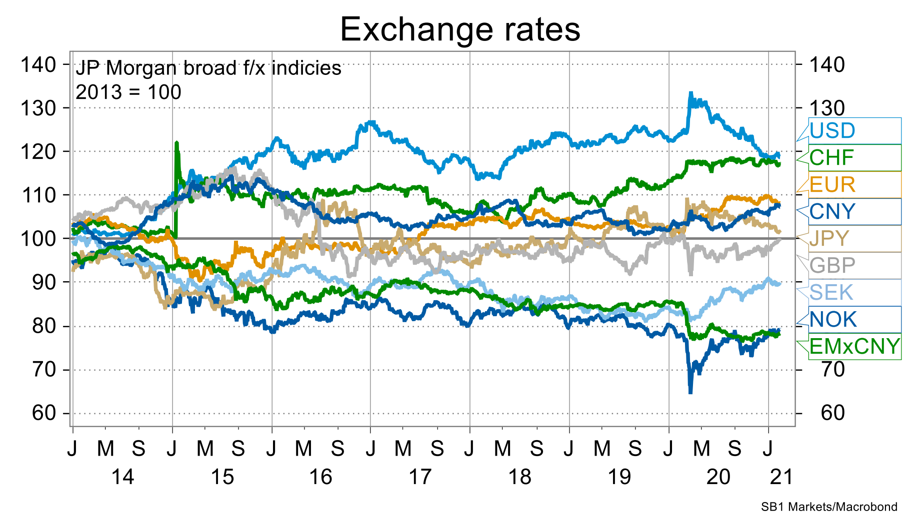


What happens when economies actually open fully?

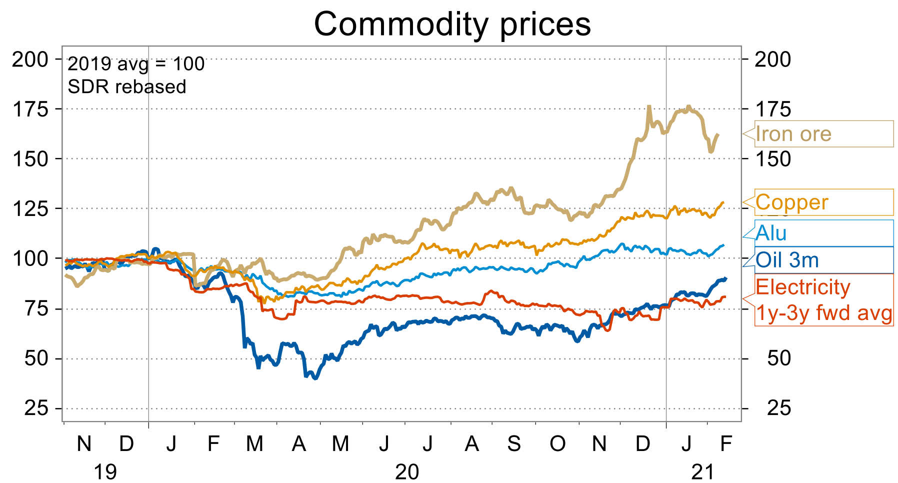


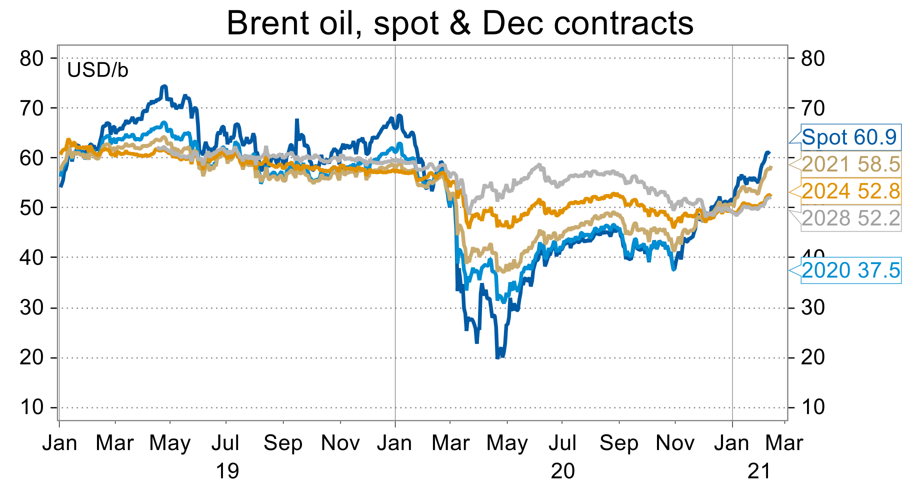


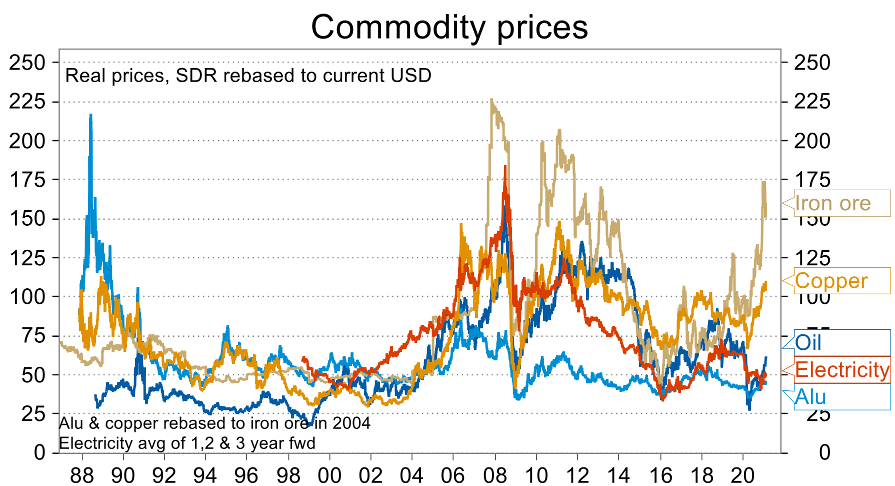


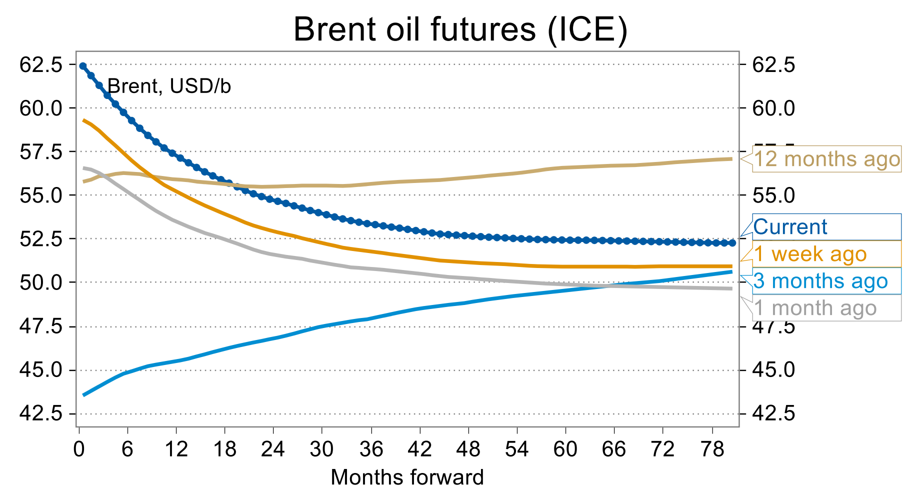


Commodities up. Oil up across the curve as inventories are declining

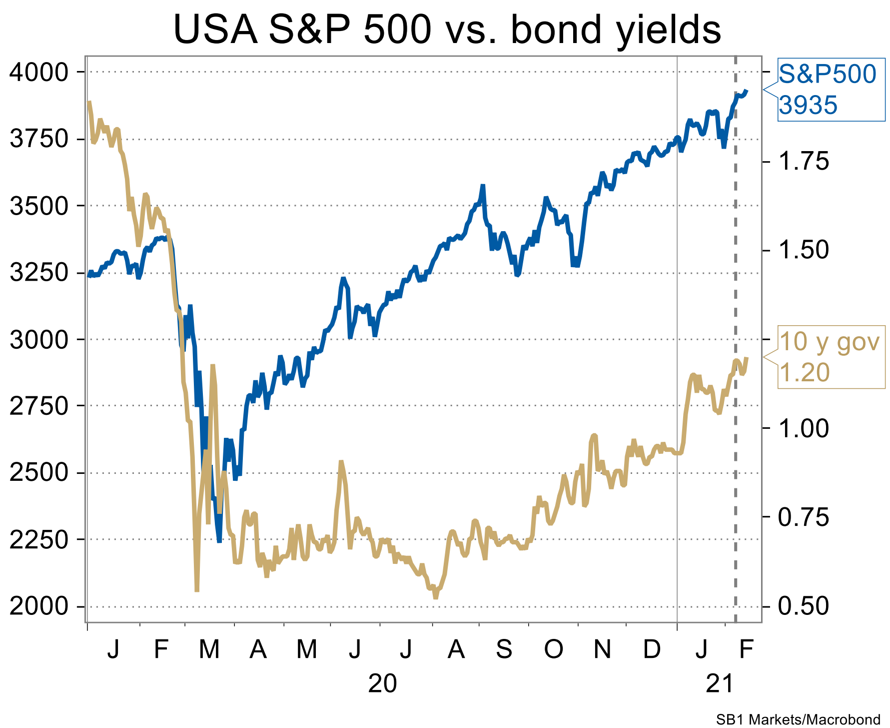


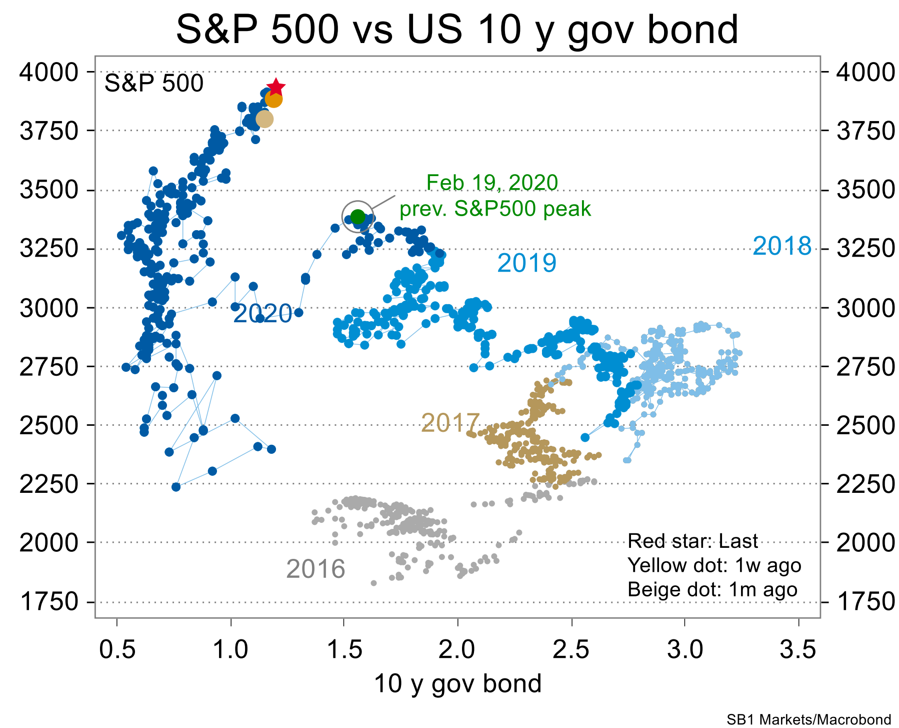






The S&P up 1.2% last week, to another ATH, 10 y Gov up 1 bps to 1.20

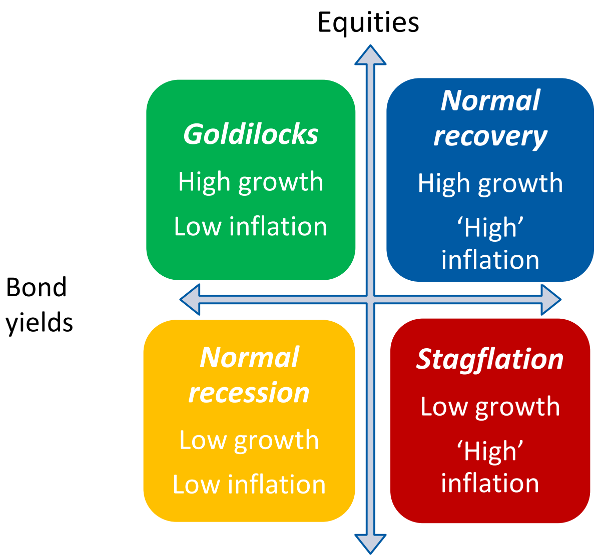


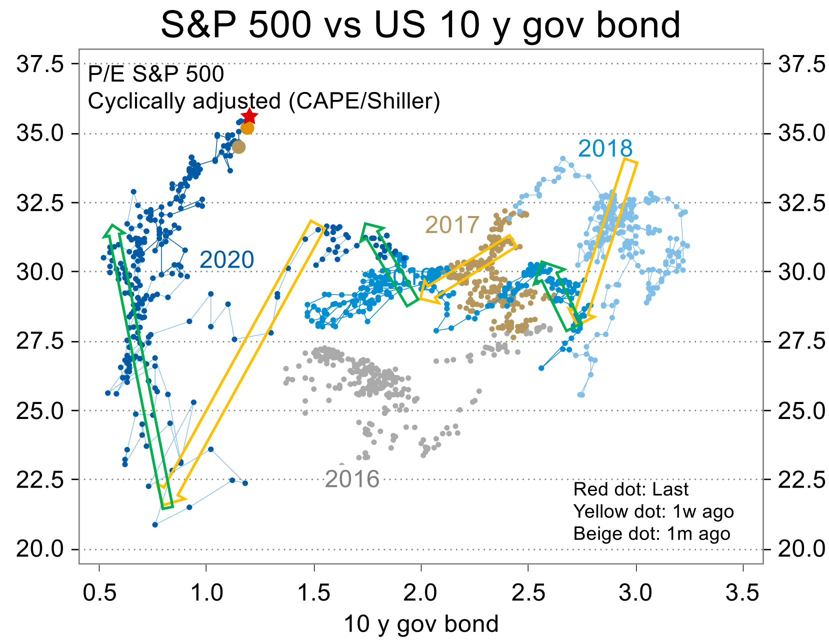


* Since the through in yields in early August, almost 70 bps ago (10 y gov), the stock market has climbed 20%

A long term view: From the 'Goldilocks corner', where to go?

Over the past month/week: <u>Towards</u> the normal recovery 'blue' corner, but we are still in the 'green' Goldil.'s





SB1 Markets/Macrobond

- Usually, we have associated drifts towards the 'green corner' - low inflation and solid growth at the same time - as a <u>temporary</u> sweet spot for markets
- The US Federal Reserve promises to keep monetary policy expansionary, until actual inflation reaches the 2% target and is expected to exceed 2% for some time. As a bonus (at a late stage of a cycle), that would also make it possible for the Fed to push employment higher and profits margins lower (which the market will not discount before it is too late?)
- Will we stay up here, in the green? <u>Perhaps, for while – but probably not, long term</u>
  - » The economy has rebounded rapidly from the corona trough. Any substantial disappointment on corona/vaccine or the growth cycle in general would be challenging for the equity market. Still, the corona hit is most likely behind us, and vaccines have arrived
  - » The Fed will not yield from its new strategy anytime soon. However, (higher than expected) actual wage or price inflation numbers or just a rapid decline in the unemployment rate may shake the market's confidence in the sustainability of Fed's strategy, pushing long term bond yields up. Again, the risk is not serious, short term
- 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 growth was not low vs. CPI 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>

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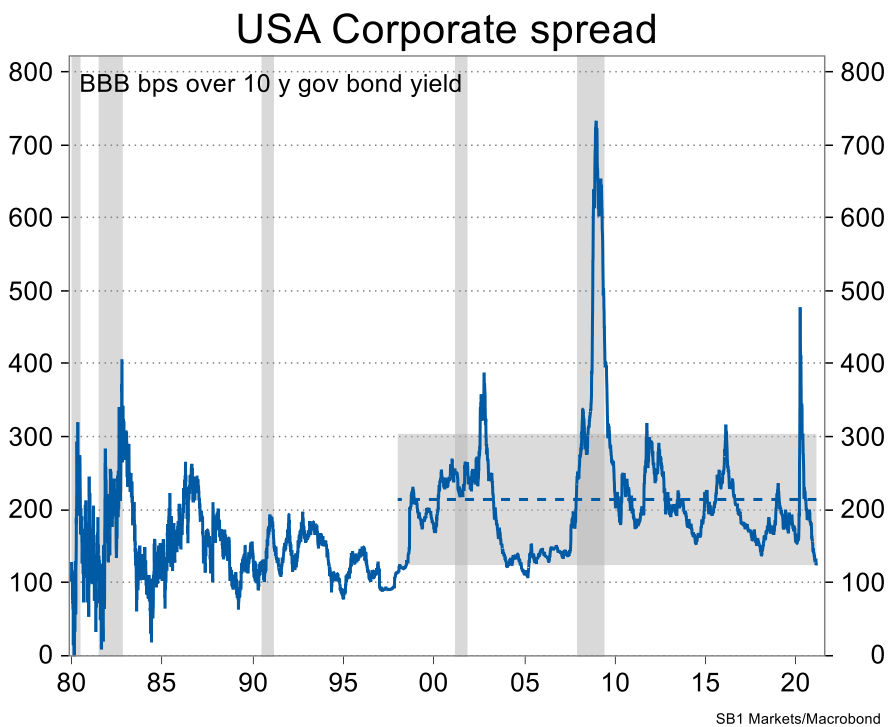
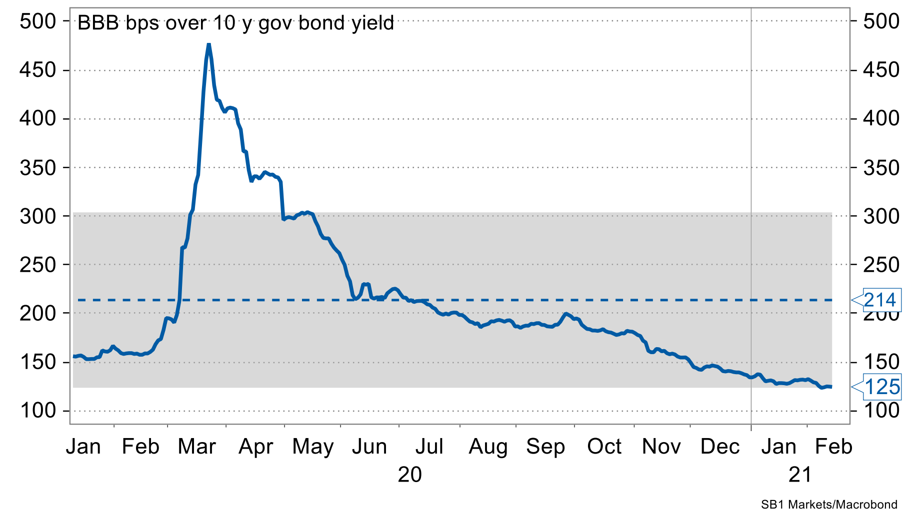
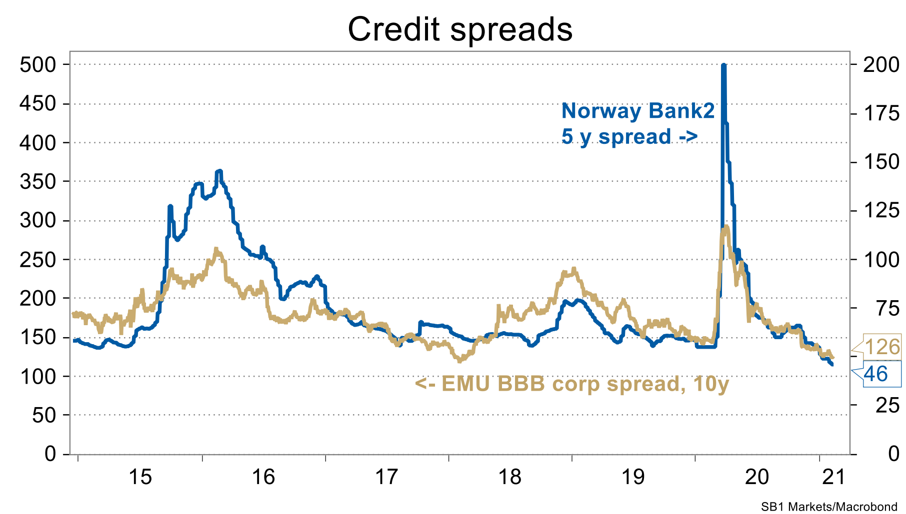
The market is throwing caution to the wind: Credit spreads down – again!

Credit spreads haven't been lower since 2005!

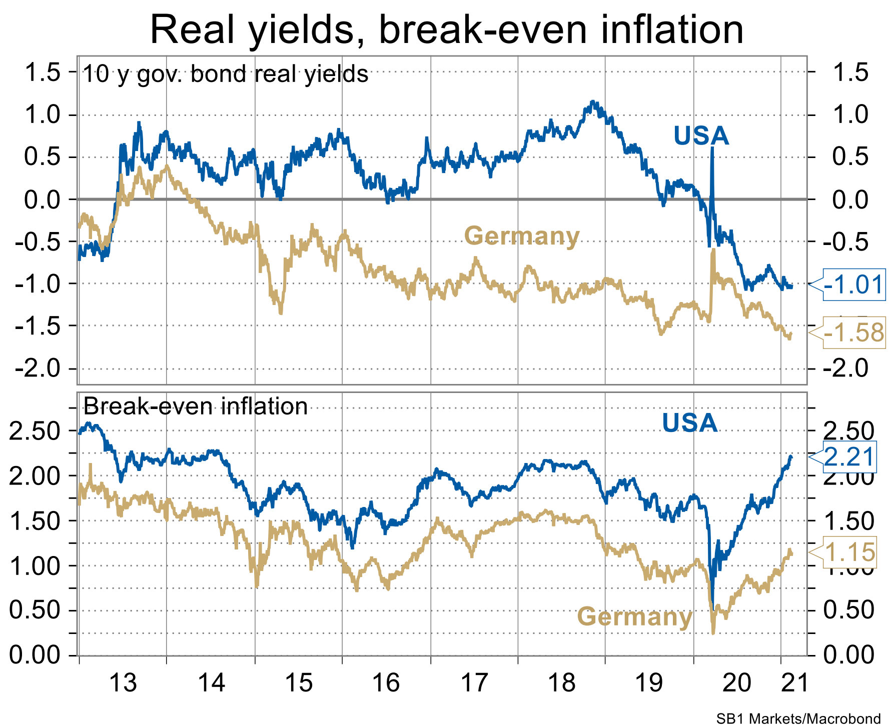


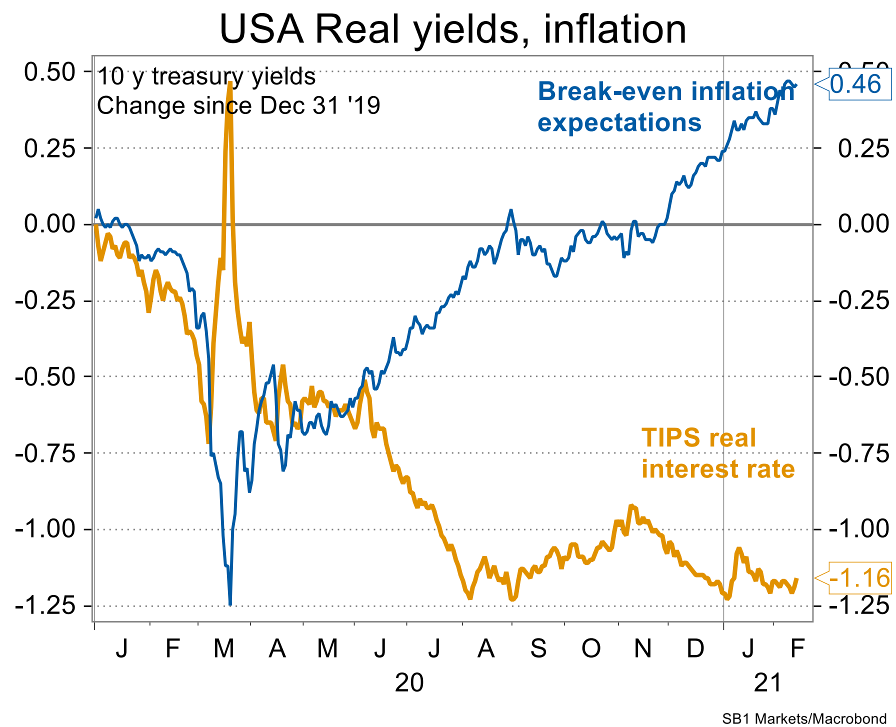




Inflation expectations held steady

Inflations expectations are trending upwards – and are at the highest level in 7 years in the US

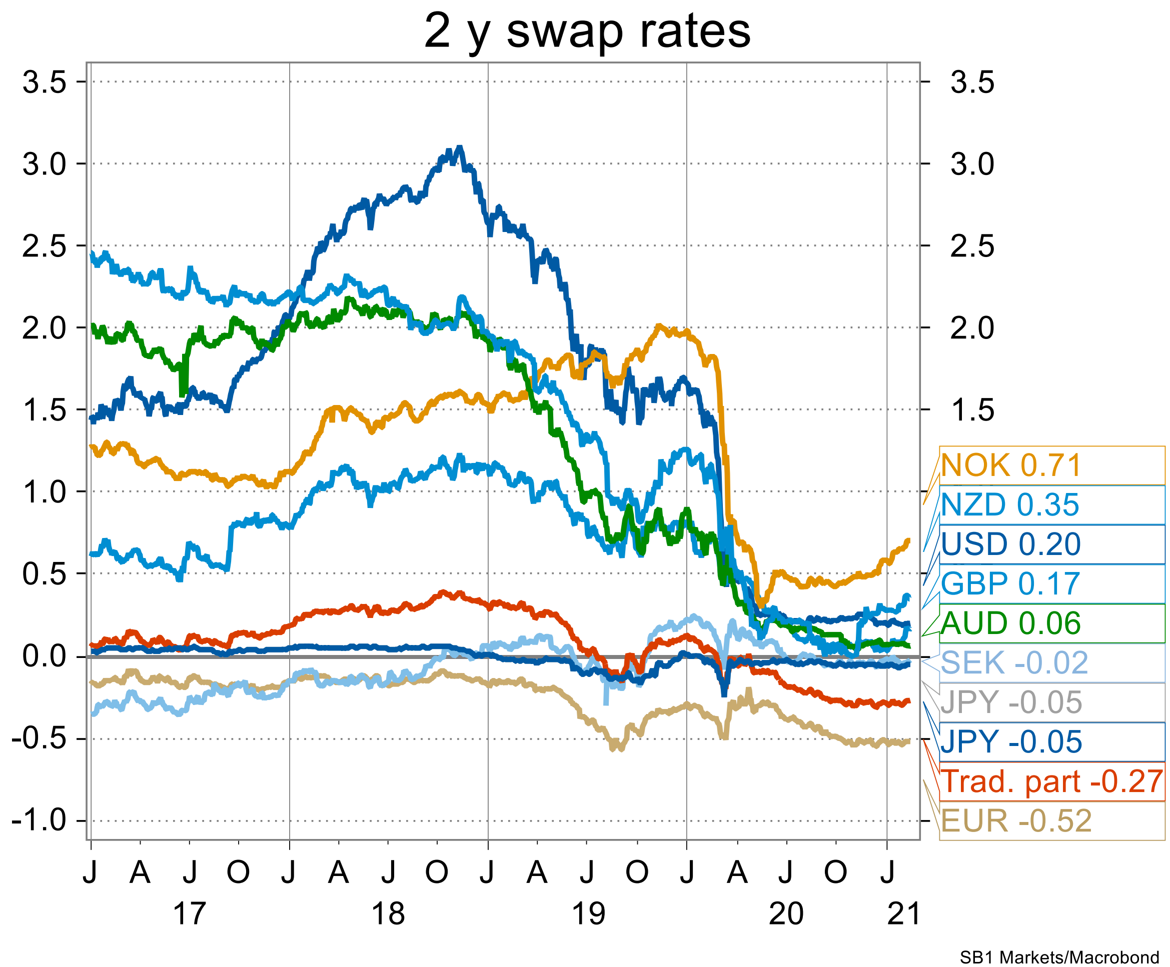


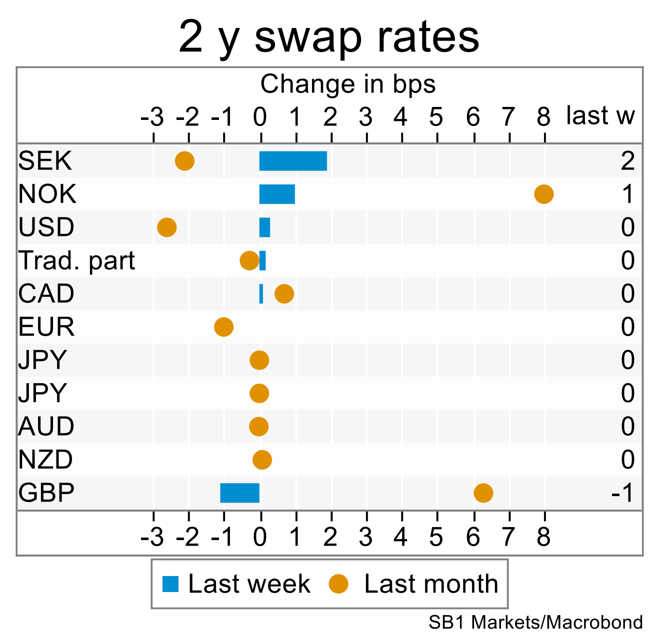


- **US 10 y +<u>1 bps to 1.20%</u>**
  - » Inflation expectations unch. At 2.21% (up 45 bps from late Nov) – <u>**and at the highest level since 2014. *The anchor is not lost, but it is dragging?***</u>
  - » The TIPS real rate +1 bp to -1.01%. The level remains almost 1 pp below the pre-corona level (and 200 bps lower than in late 2018)
- **Germany 10y<u> down 2 bps to -0.47%</u>**
  - » Inflation expectations flat at 1.15%
  - » Real rate +3 bps -1.58%, still close to an extremely low ATL

Short-term swap rates slightly up in NOK and SEK

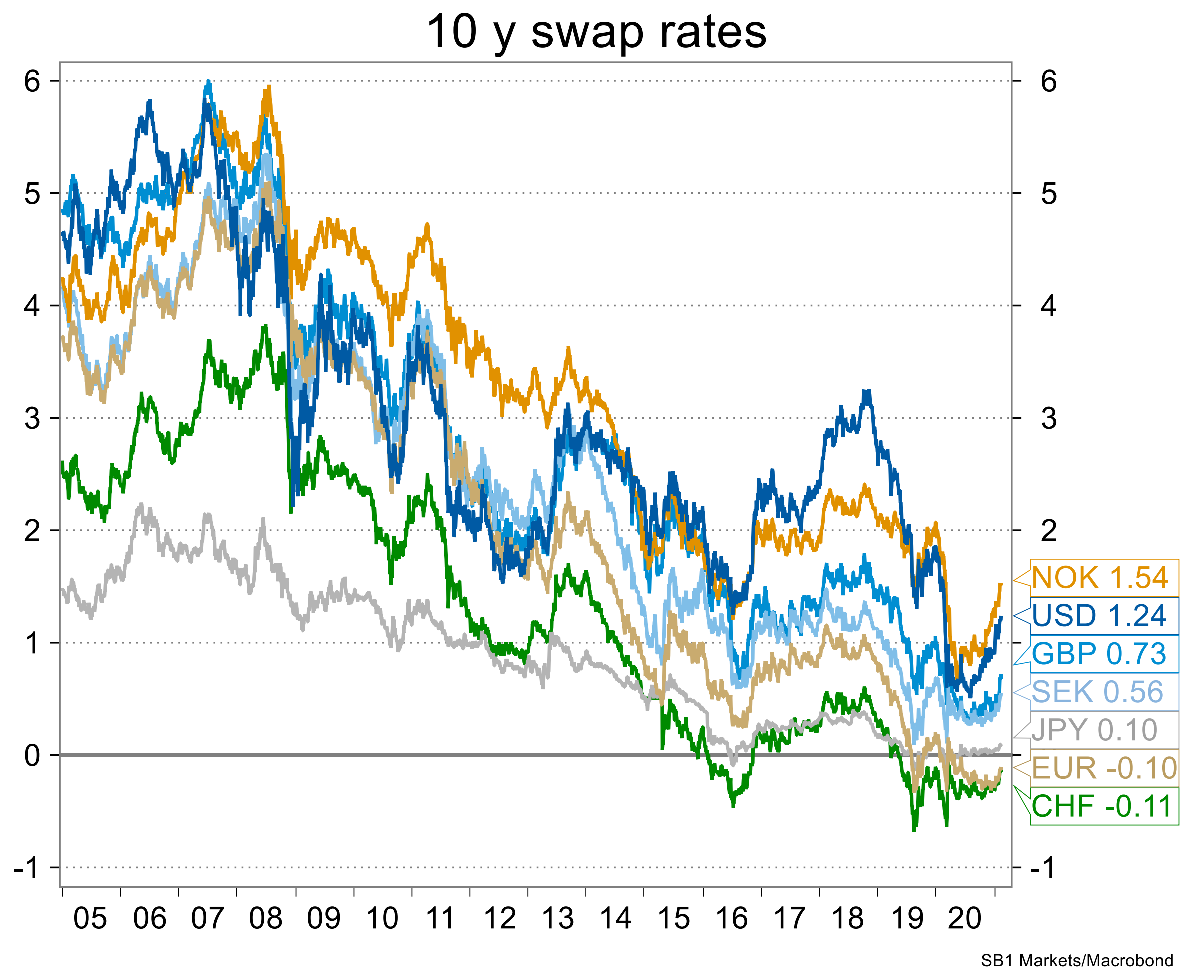
The trend is flat for most currencies

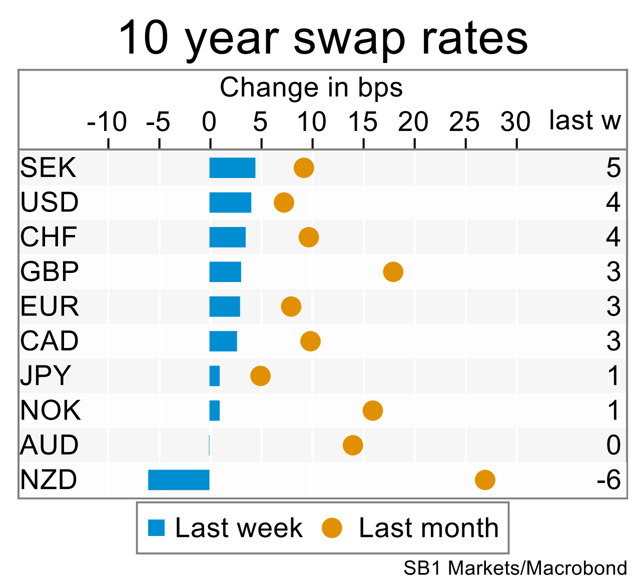




10y rates are up over the past week and month

Volatile rates in New Zealand is the exception





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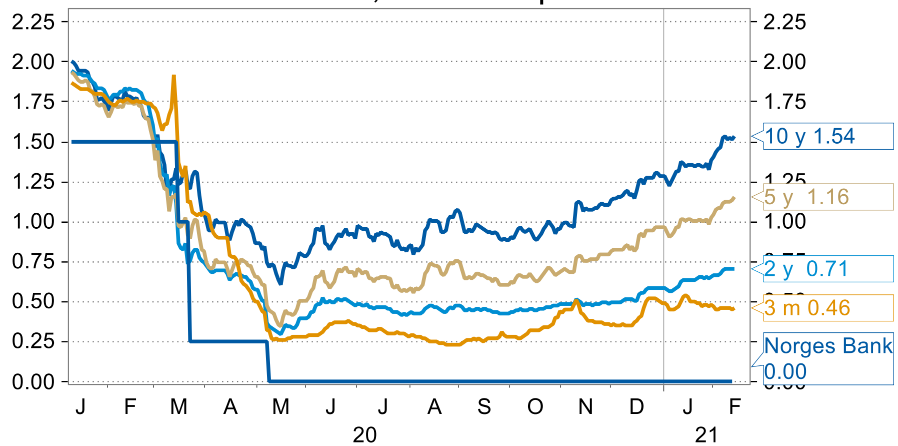
NOK rates keep nudging higher

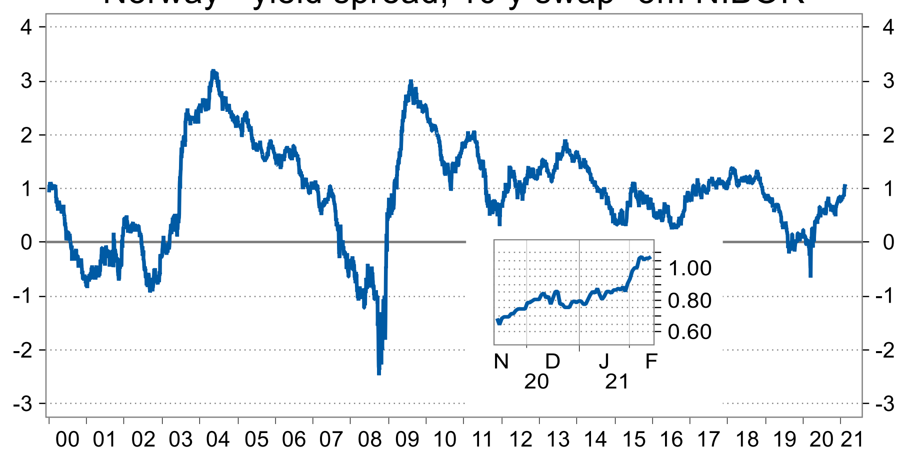
NOK 10 y swap +1 bp to 1.54, up 91 bps vs bottom

NIBOR, NOK swap rates

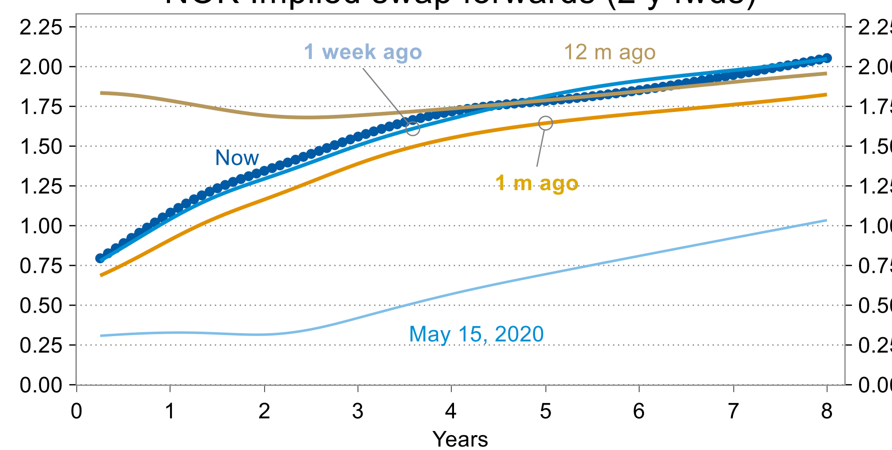


- 10 y swap rate is still some 25 – 50 bps below the level in early 2020, before the corona angst hit. Still, implied rates from 4 – 5 years onwards are on par, at the implied rate 10y fwd is back to 2%!
- The first half of the curve is still well below but it is inching upwards
- The 10 y swap rate almost flattened, while the 5 y rate rose further – and the 5y 5y fwd fell

Norway - yield spread, 10 y swap -3m NIBOR

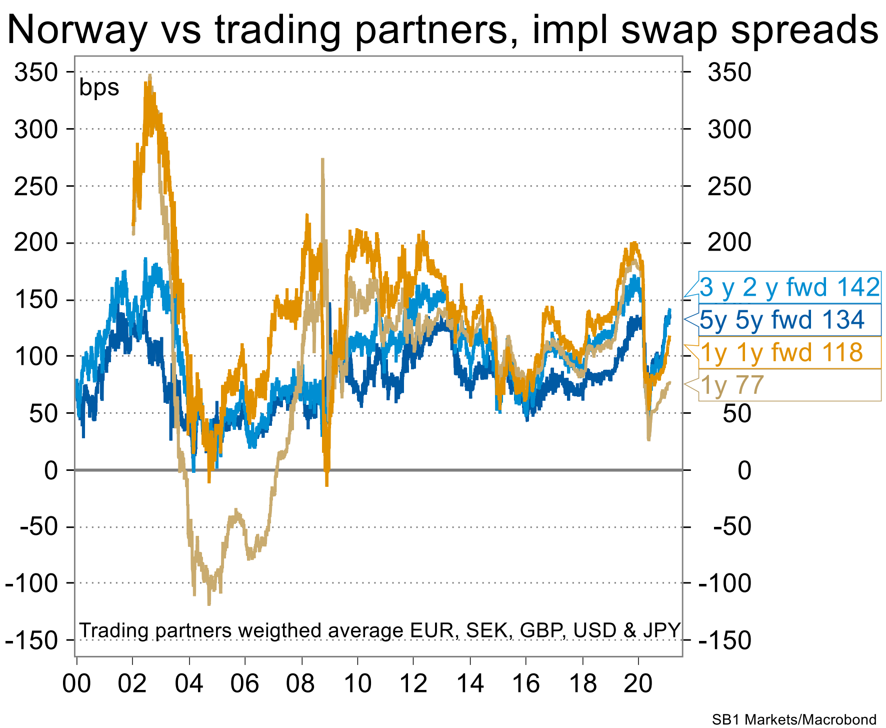


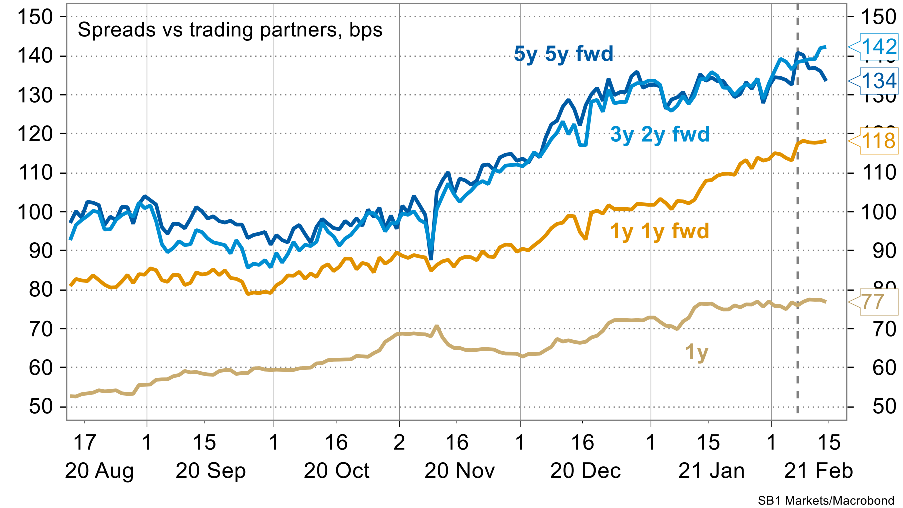
NOK Implied swap forwards (2 y fwds)

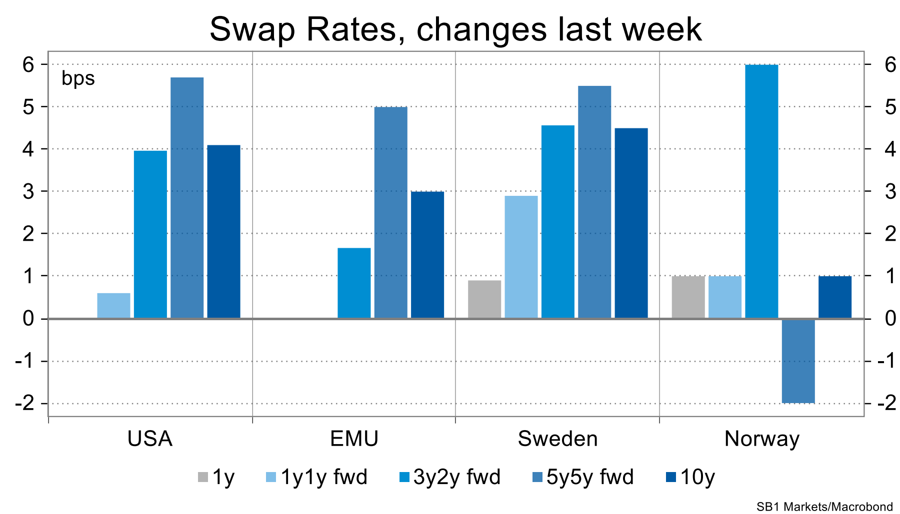


Rates abroad rose more than rates in Norway this week

As we said, the potential for a spread widening in the long end of the curve is likely limited

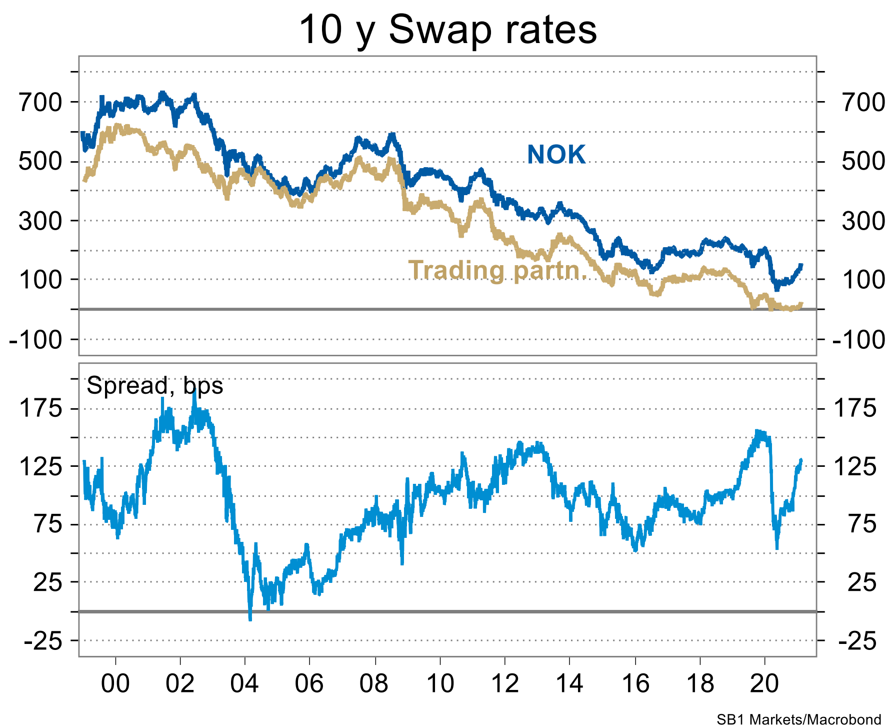


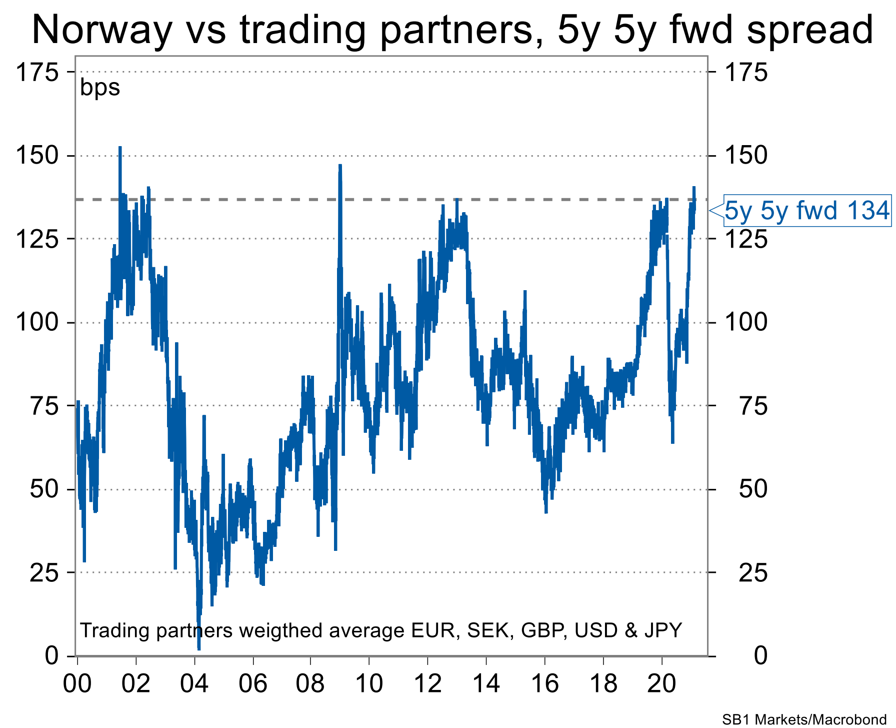




- Longer end of swap curves abroad up by 4-5 bps last week. NOK curve flattened
- It's tempting to weight against a further increase in implied spread between NOK rates and trading partners' at the second half of the curve (check the chart at the next page too)
- In the short end of the curve, spreads are still below previous peak levels *–and may well widen further*

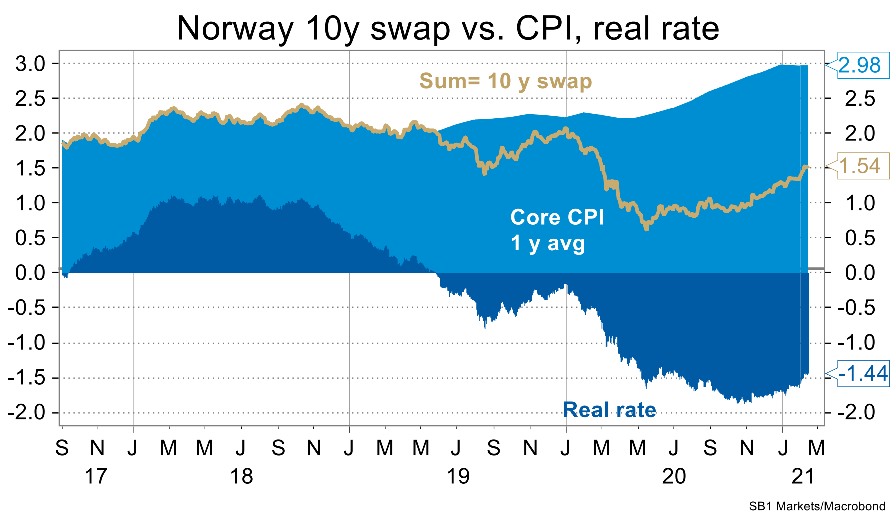
The 5y 5y fwd down 7 bps from a very high level – seems reasonable





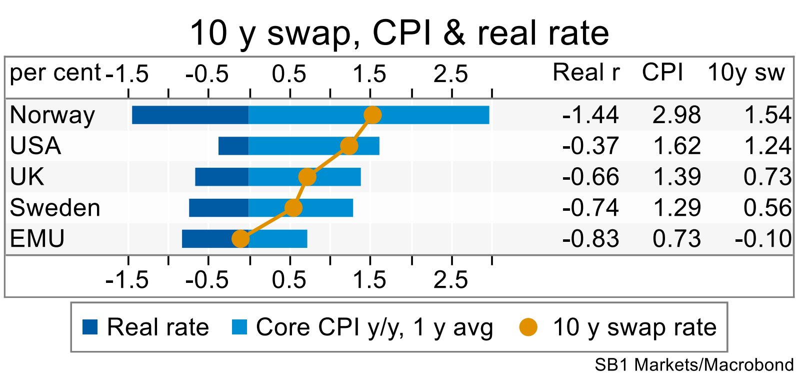
- How much inflation will Norway have, over time?
- How much faster growth will Norway deliver, over time?
- Thus, how much higher interest rates will Norway need, over time?

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



NOK 10 y swaps are drifting upwards

- The **10y NOK swap rate** has climbed by 94 bps since the bottom in May, to 1.54%!
- **The real rate**, after deducting average inflation over the 2 past years still equals -1.44%
  - » This week, we expect the CPI-ATE core inflation rate to fall substantially but the 12 m smoothed rate will decline by just 0.05%. Long term, we do not expect a 3% rate of inflation, but inflation has for years been somewhat higher in Norway than abroad



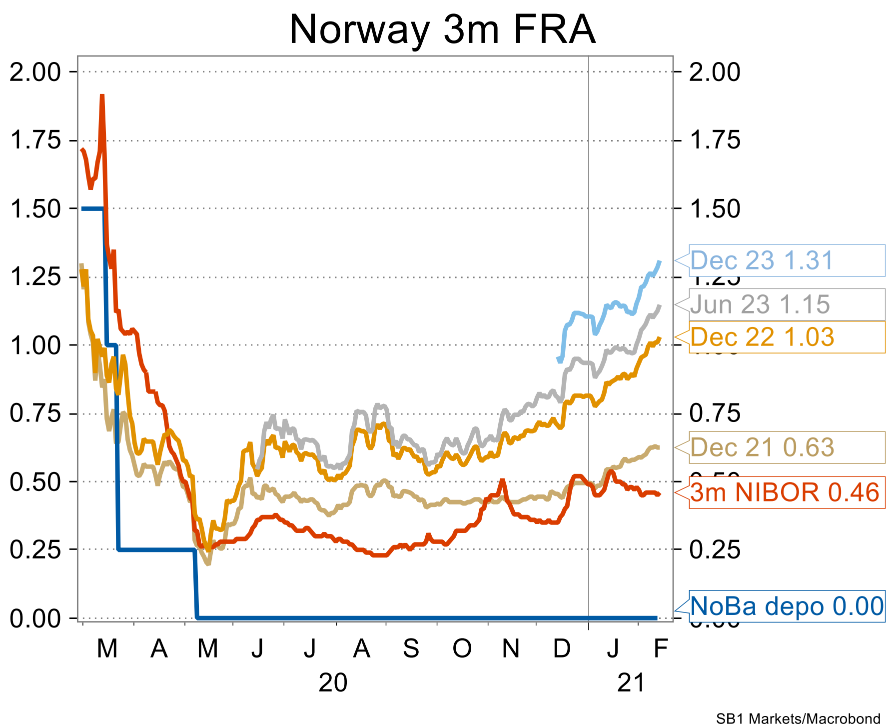
NOK real rates among the lowest, as inflation is at the top

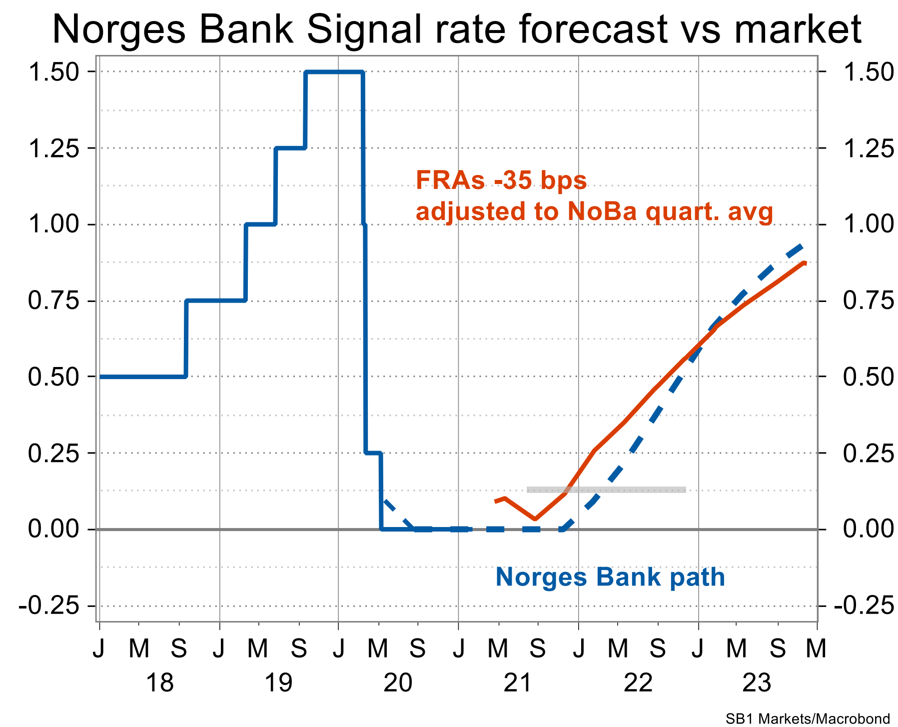
- **Inflation** among Norway and our main trading partners varies between 0.73% to 2.98% (here measured by actual annual core inflation, smoothed over 12 months). EMU at the bottom, Norway at the top, by far
  - » Other measures of inflation trends, looking backward or including forward expectations yields the same ranking
- **Real rates** are quite similar among our trading partners, at -0.37% to -0.83% measured vs. the 10 y swap rate and core inflation over the past two years
- **Thus, the Norwegian real rate at -1.4% is an outlier at the downside, even if the nominal rate is the highest**

SpareBank 1 MARKETS

3m NIBOR has stabilised but the FRA curve is steadily shifting upwards

Most likely, just really bad virus/vaccine news will dampen rate expectations

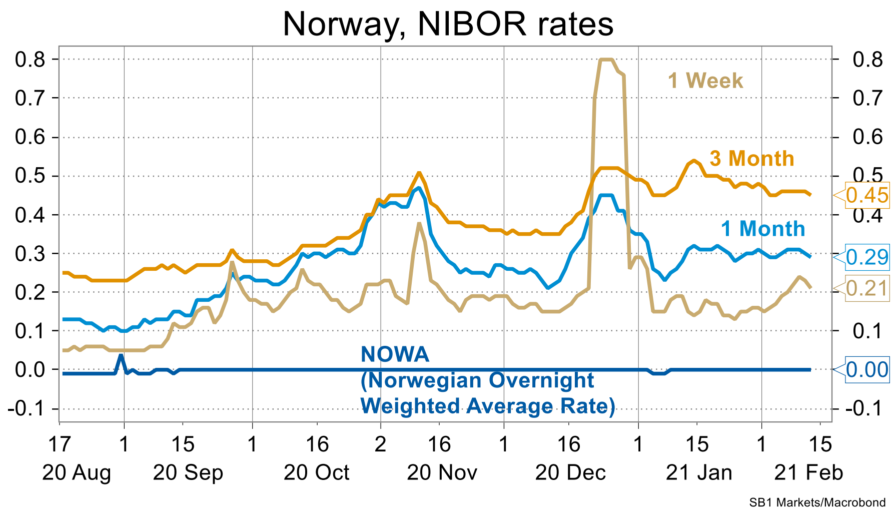


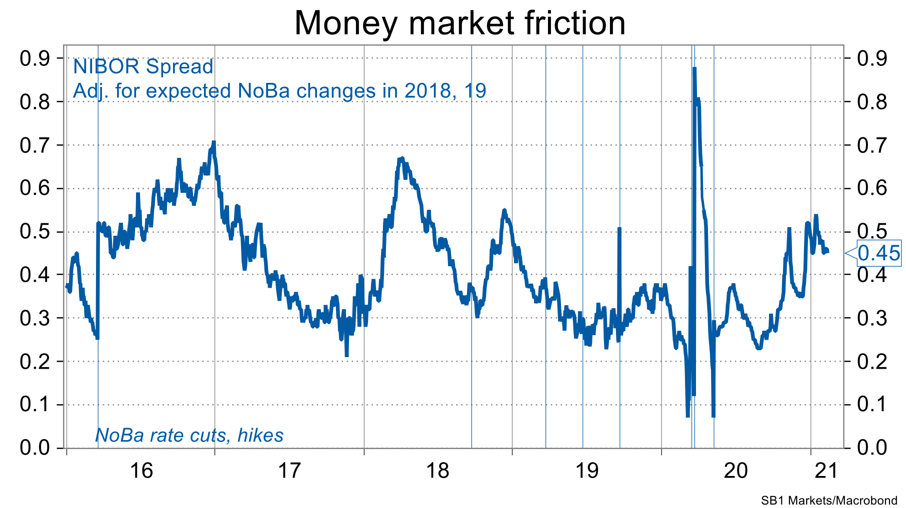


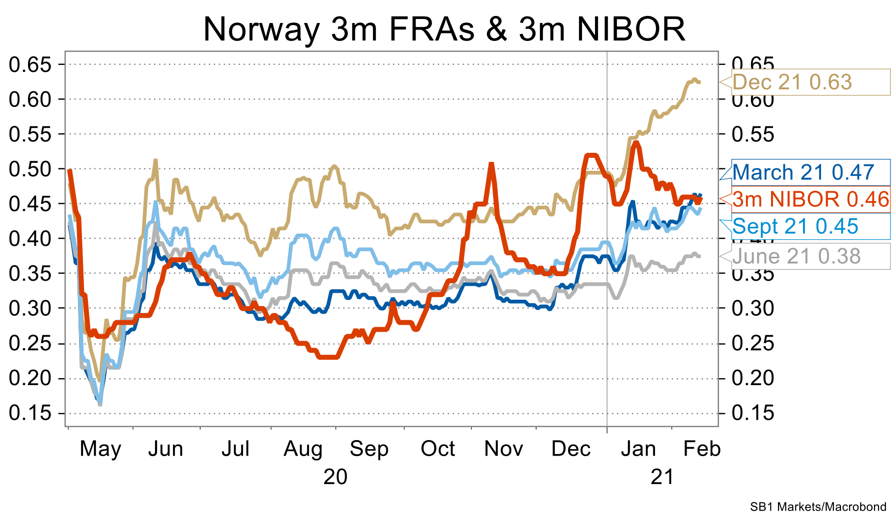
- The curve is above NoBa's path until early 2022 – if the expected NIBOR spread is at 35 bps (we are slowly accepting a higher spread, until now we have said 30 bps – and 40 may be an even better estimate)

NIBOR rates sliding slowly down, but the 3 m rate at 0.45% is still on the high side

The March 3 m FRA at 0.46%, and June at 0.38% signal that market do not expect 30-35 bps anymore



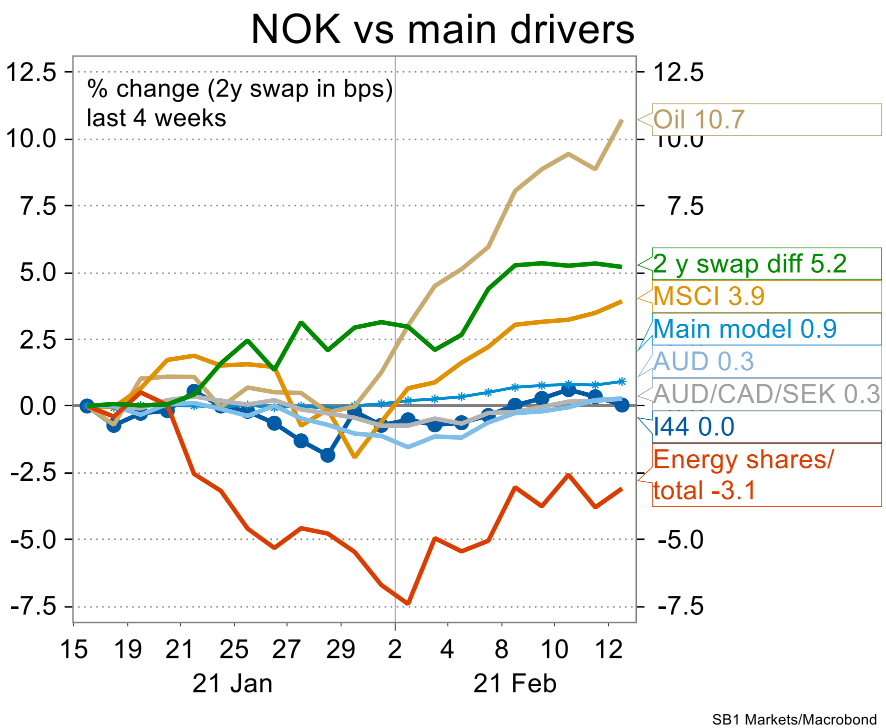


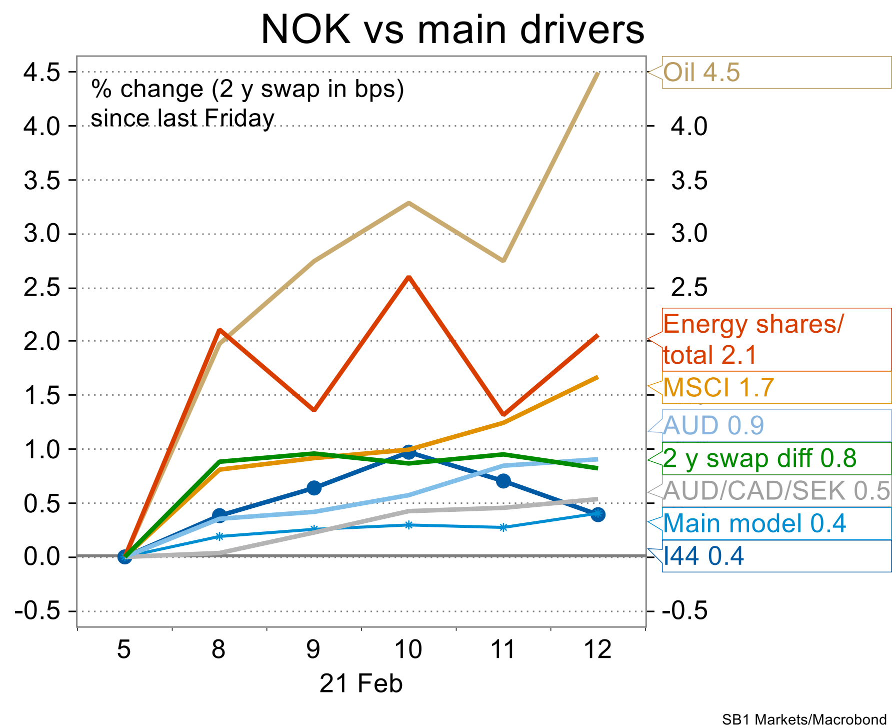


- **The 3m NIBOR** was flat last week but the spread vs. the NoBa deposit rate remains larger than 'normal'
- Now, the **FRA rates implies** that market participants expect that the spread will remain higher than the 'normal' 30 – 35 bps
  - » However, the spread has been far from stable, though mostly driven by LIBOR-OIS spread in dollar market. The present gap between the spreads are larger than normal
- **Of the NOK 47 bn 3 month f-loan** that was due Feb 10th, Norges Bank offered **20 bn** in new f-loans due March 1st

Brent and equities had a strong week, but NOK I-44 only gained 0.4%...

…however the NOK is still following our supercycle buddies closely



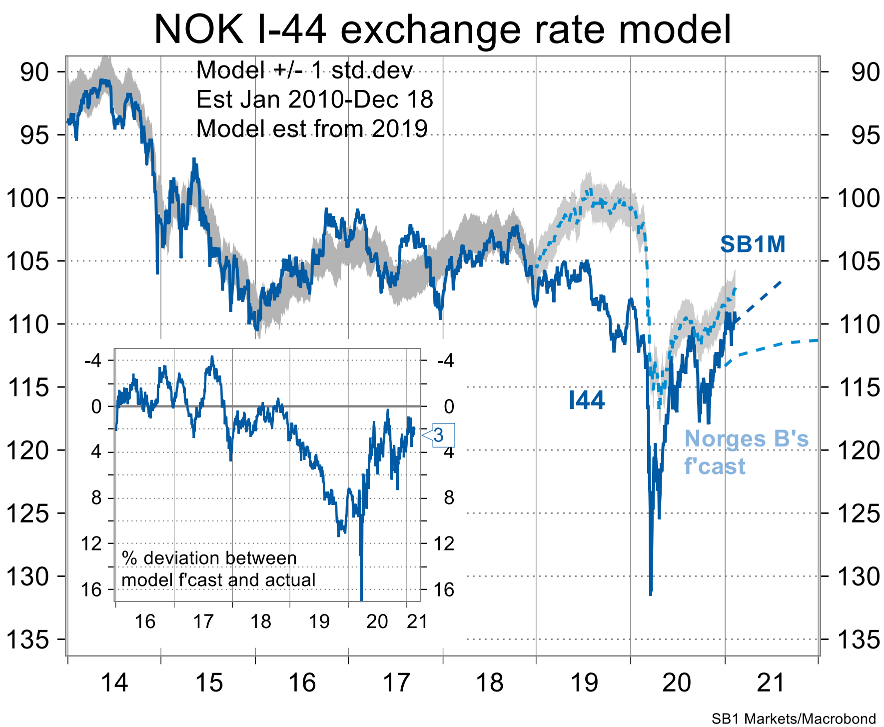


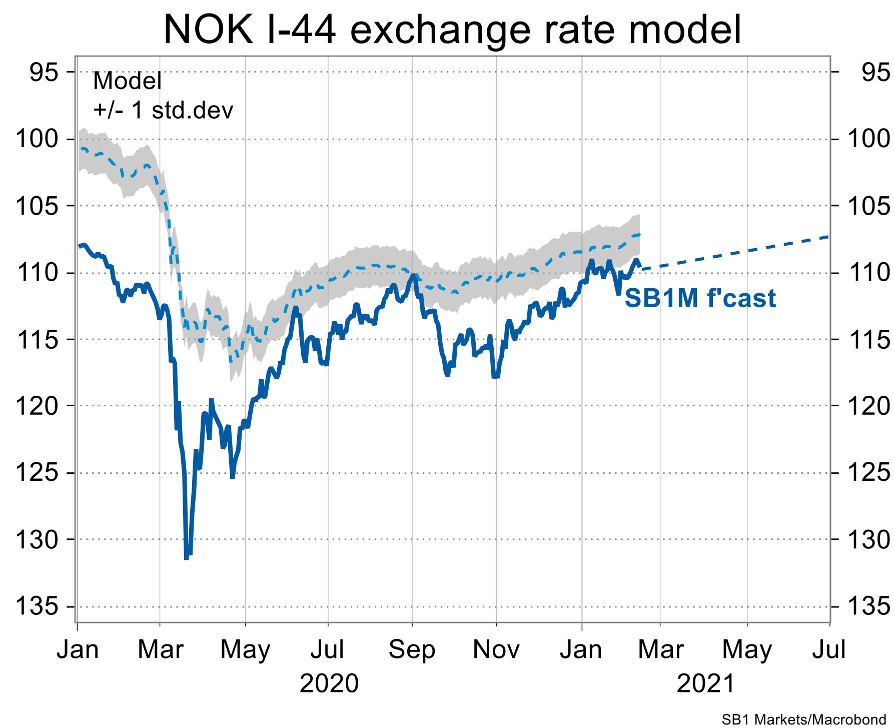
In sum, the NOK is still a buy:

- The NOK is 3% weaker than suggested by our standard model
- The NOK is 7% 'weaker' than the global stock market vs the correlation between the two in 2020
- The NOK is 6% weaker than an average of AUD/CAD/SEK, our 'supercycle peers'
- On the other hand, the NOK is far (12%) stronger than a model which includes global energy companies equity prices (vs the global stock market)

NOK I44 up 0.4%, just as our model (by accident) suggested

The NOK is 3% below our model forecast

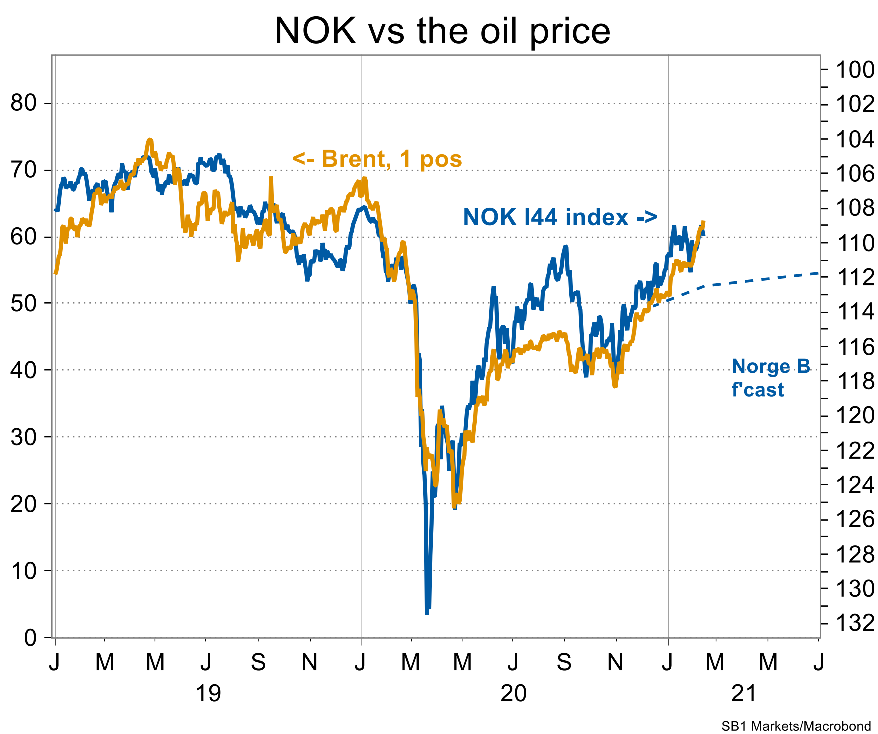


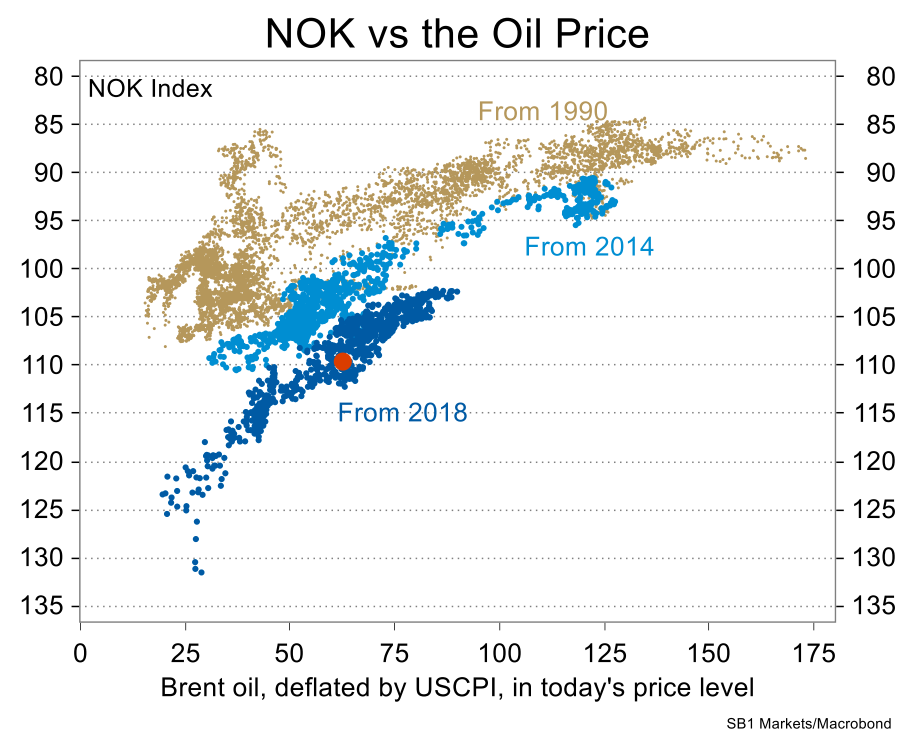


SpareBank 1 MARKETS

NOK only slightly stronger over the past weeks, even if the oil price is up

The oil price is approaching USD 60/b, to above the pre-pandemic level. Thank you, Saudi & Russia

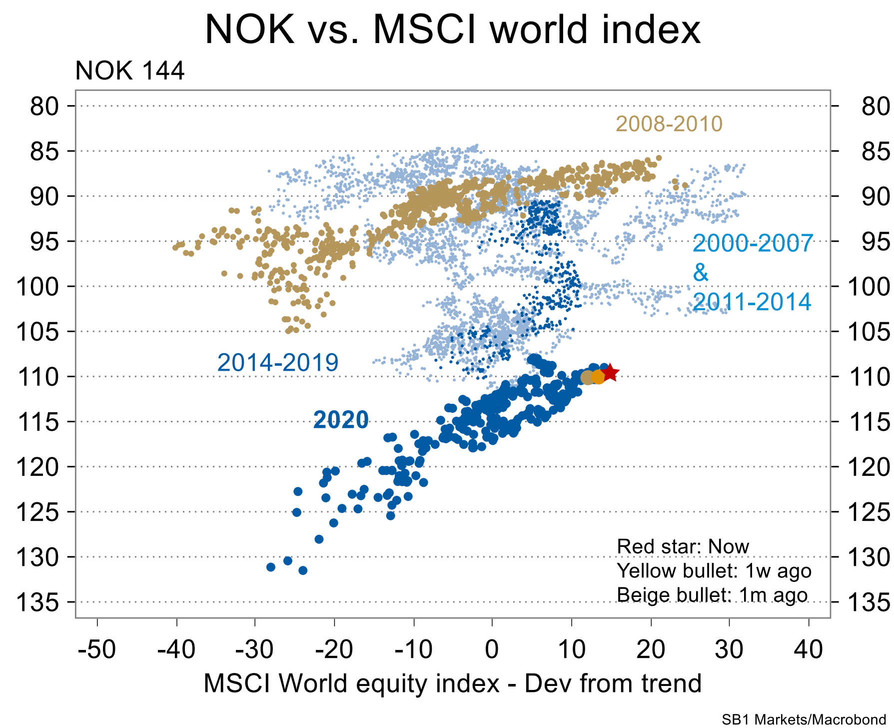




- Opec+ has announced that the cartel + will keep production down in order to trim inventories back to a normal level

Equities were up – and more than NOK

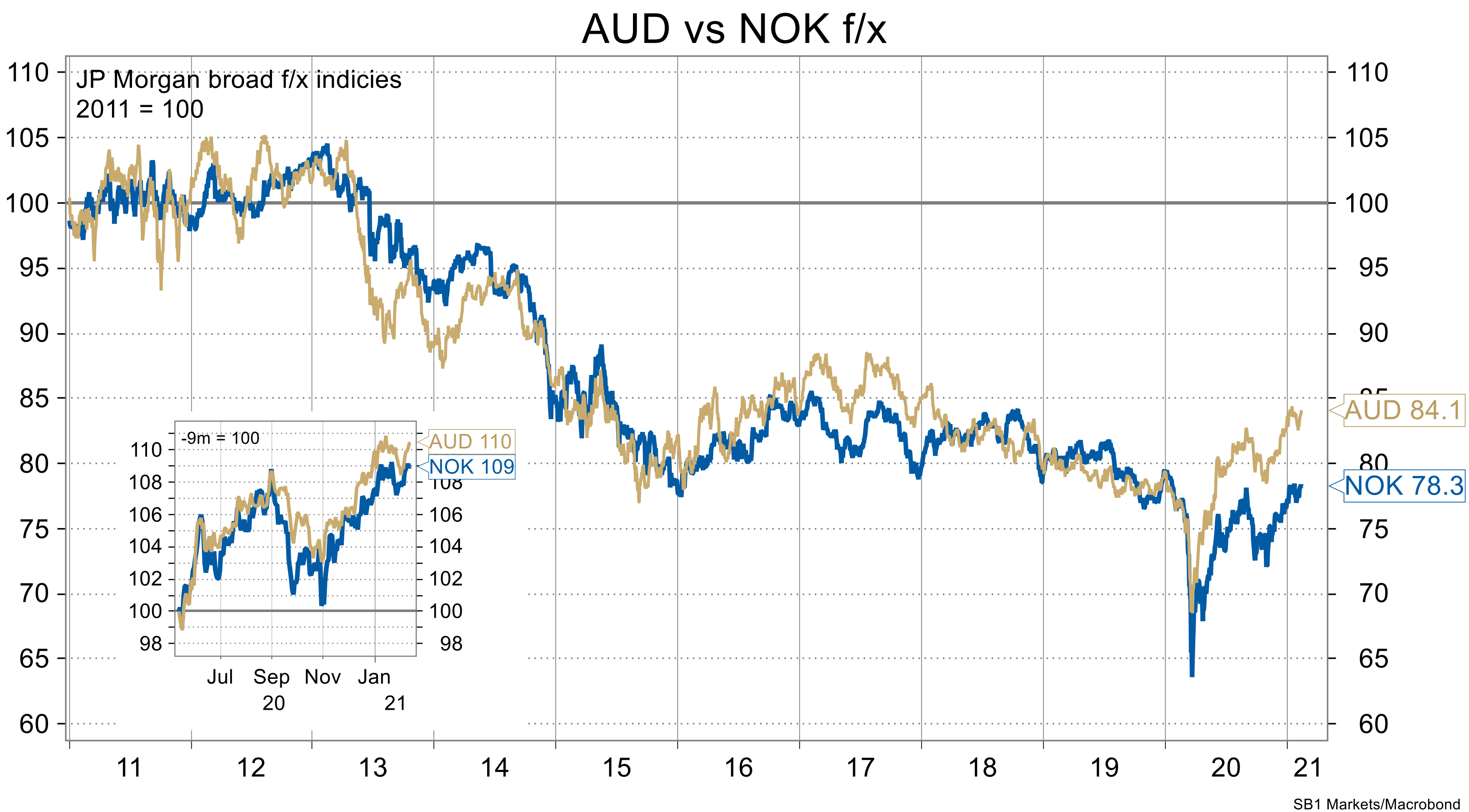
Except for Sept. NOK and global equities have walked in tandem last year. In Sept, NOK 'lost' 5%



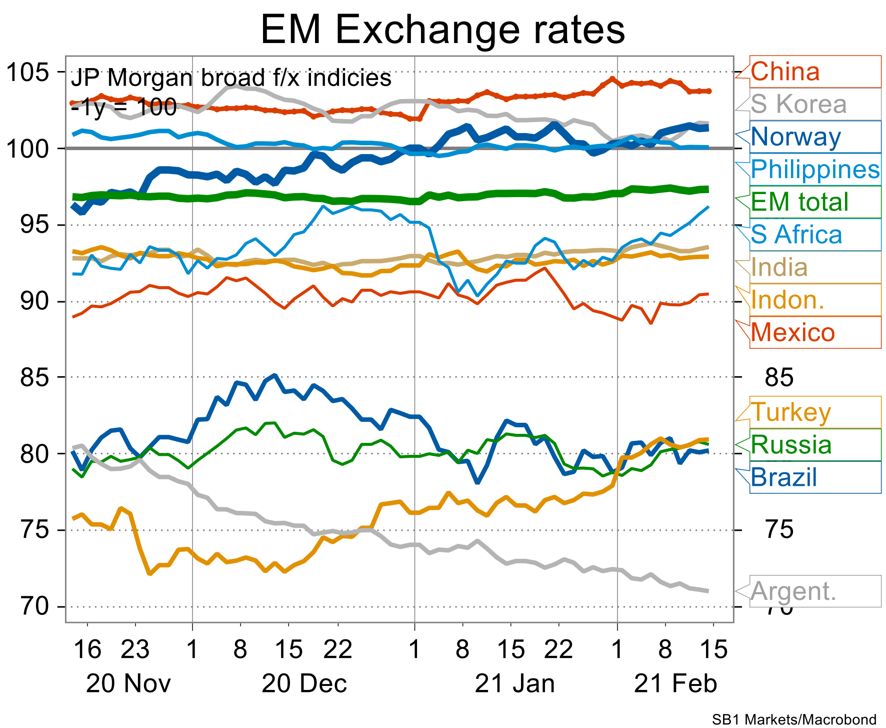
- Over time, there has not been a stable correlation between NOK and stock markets (the Oslo Stock Exchange, S&P 500 or the MSCI, the global equity index. (At the chart to the right, we have detrended the stock market as equities are drifting upwards, while NOK (hopefully) is stationary. However, the two has been pretty closely correlated from time to time
  - Now, the NOK is more than 4% weaker than 'normal' vs the stock market as the NOK lost ground in mid Sept, based on the link between the NOK and MSCI since Jan 2020). However, at one stage we will have to recalibrate the scales, as equities are trending upwards 6 – 8% per year
- We have long argued that global equity prices should be more important for the NOK than the oil price, as our global equity assets in the Oil fund are larger than the value of the remaining oil & gas reserves. Has the market 'finally' (and rather sudden) come to the same conclusion? We doubt. It's probably a "risk on, risk off" world, where many risky asses move in tandem, more than usually

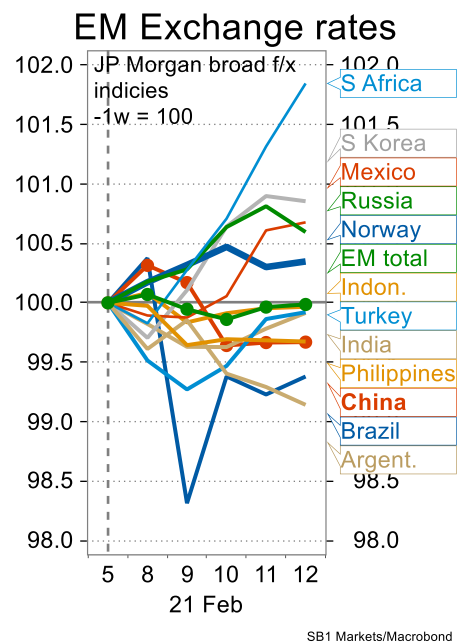
Like two peas in pod

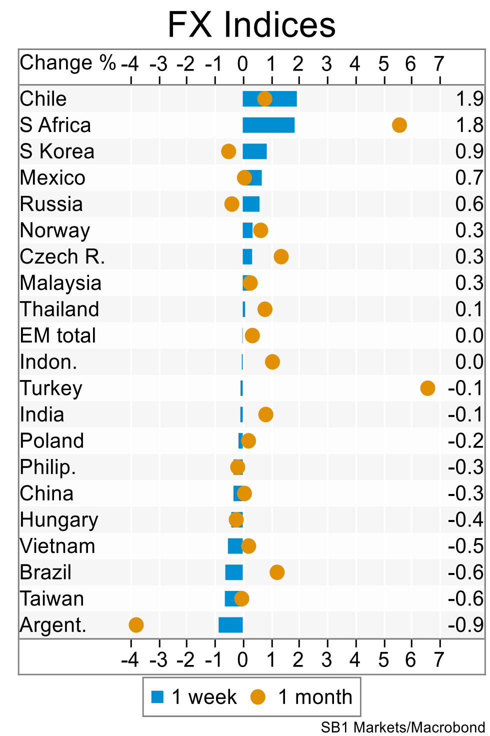
… if we accept NOK's 6% step backwards last March as a permanent shift. We doubt it was



Mixed week for EM currencies. CNY slightly down this week too







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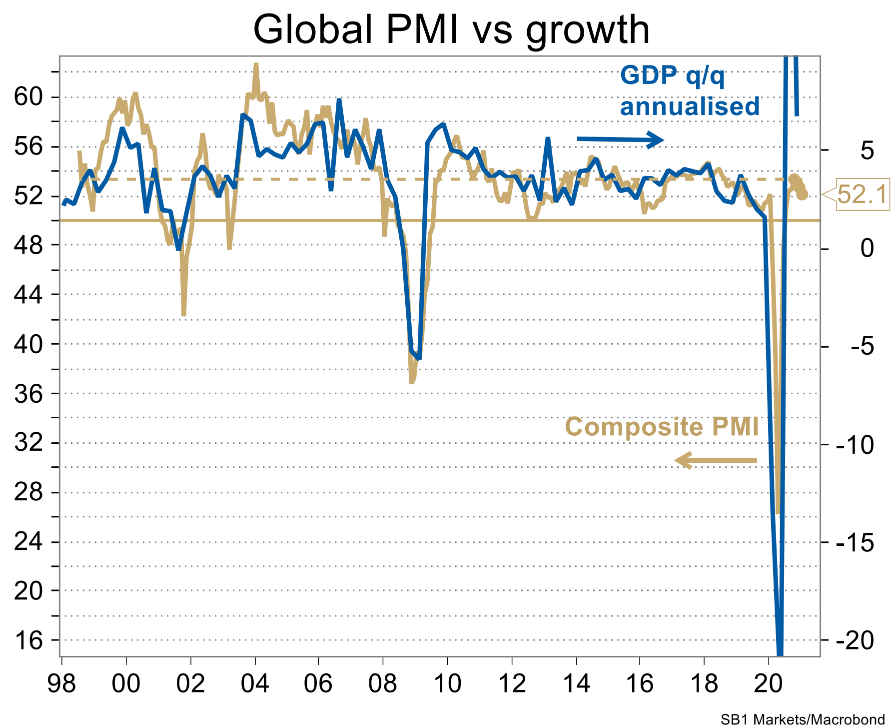
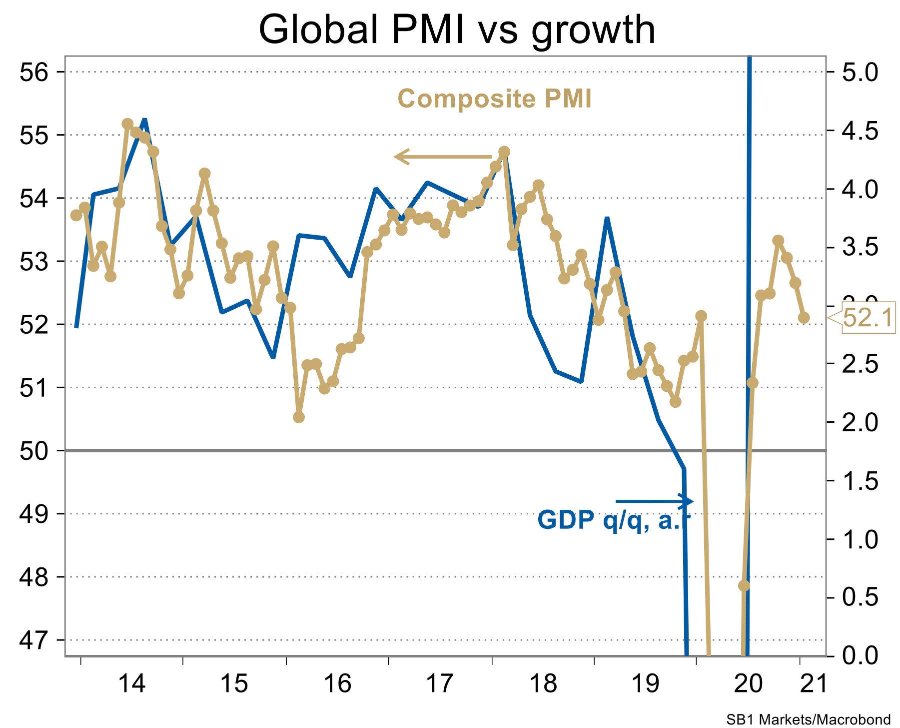
The global composite PMI probably down 0.6 p to 52.1 in Jan

China & the EMU contributes at the downside, and more than the US at the upside



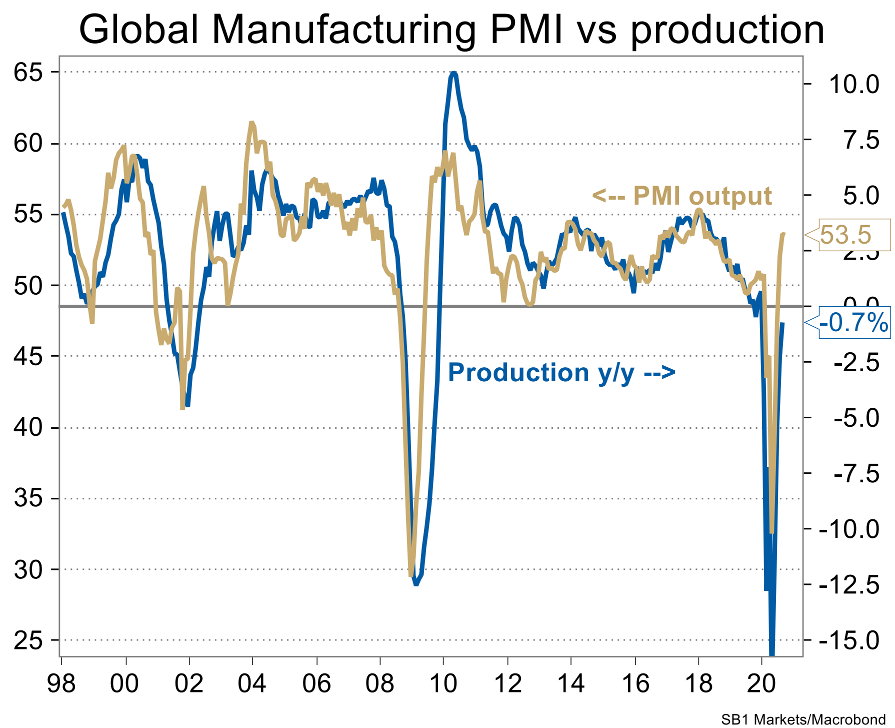


- The preliminary PMIs were mixed, a surge in the US was not sufficient to compensate for a decline in both China, EMU, Japan and UK (a sharp drop here). (The China service sector PMI is not yet reported, our estimate is included)
- Our **global PMI composite** estimate is down 0.6 p to 52.1 . The level signals some 3% growth in the global economy, vs the actual growth rate at 5 -6% in Q4 (our very preliminary estimate)
- The **global manufacturing PMI** total index was probably just marginally down but the output index fell sharply, while the **service sector** index may have fallen by 0.1 p

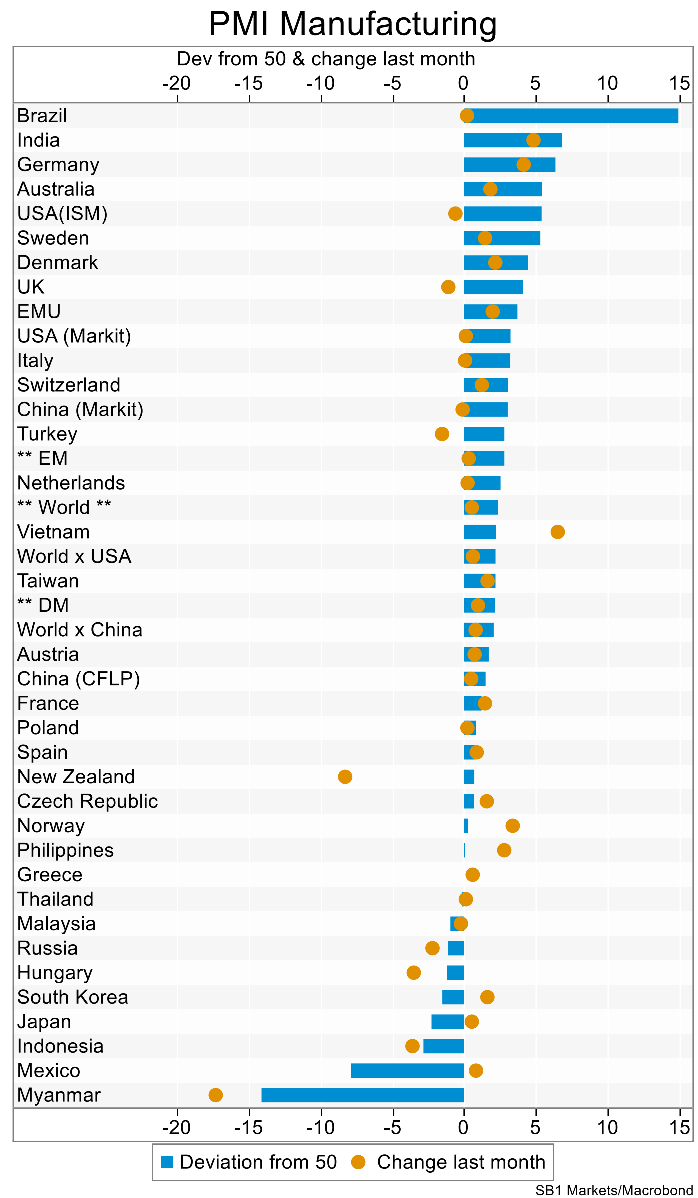
Our estimates are based on the preliminary PMIs from EMU, Japan UK, US. The estimates are uncertain, but usually by less than 0.5 p

Manufacturing PMI climbs, most countries above 50

The PMI rose 1.5 p in Sept but the level is still not impressive



- The global manufacturing PMI rose 1.5 p to 52.3 in Sept, close to our estimate based on preliminary PMIs
  - » 69% of the countries/regions reported higher PMIs in September than August
  - » A majority of the countries (72%) are reporting PMIs above the 50 line
- Rich countries (DM) recovered somewhat more than Emerging Markets (EM), from a lower level. Brazil and India in the lead, Mexico at the bottom



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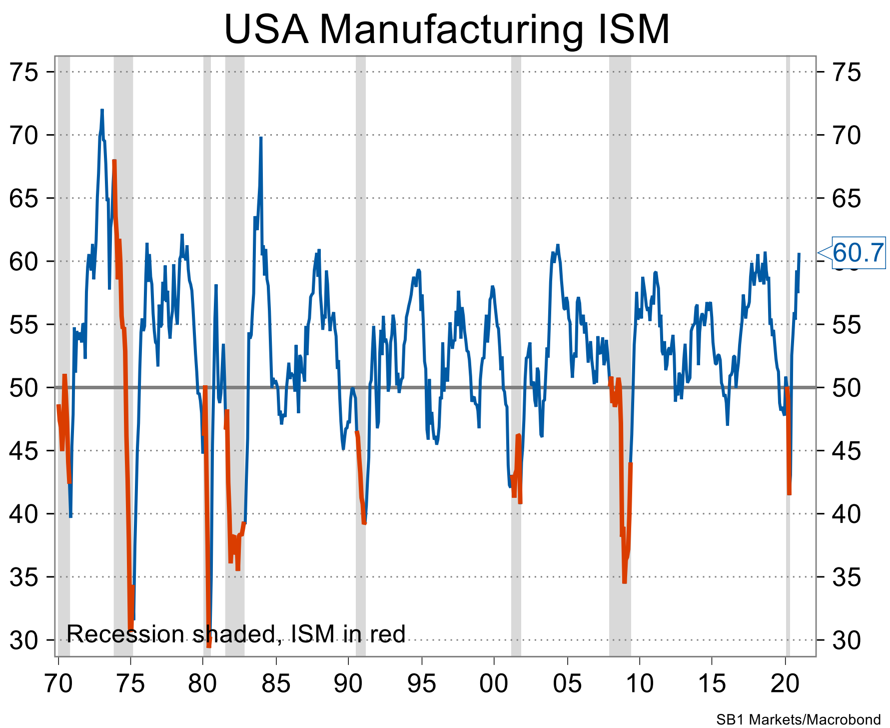
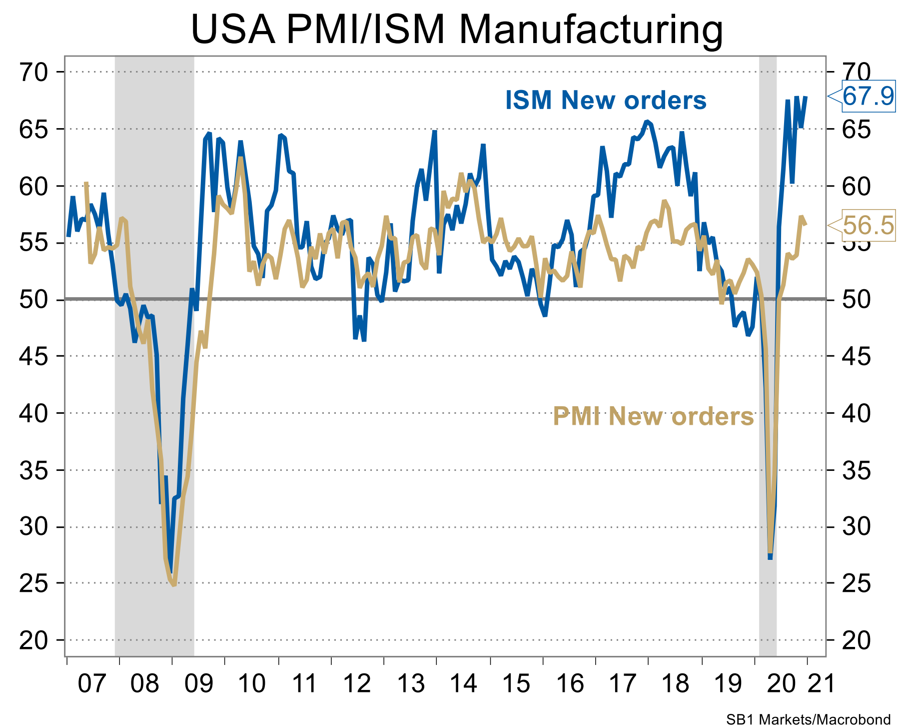
Manufacturing ISM surged in Dec, has been marg. higher just 3 times past 40 y

The ISM surprised sharply at the upside, +3.2 p to 60.7, expected down to 56.6. Orders strong too

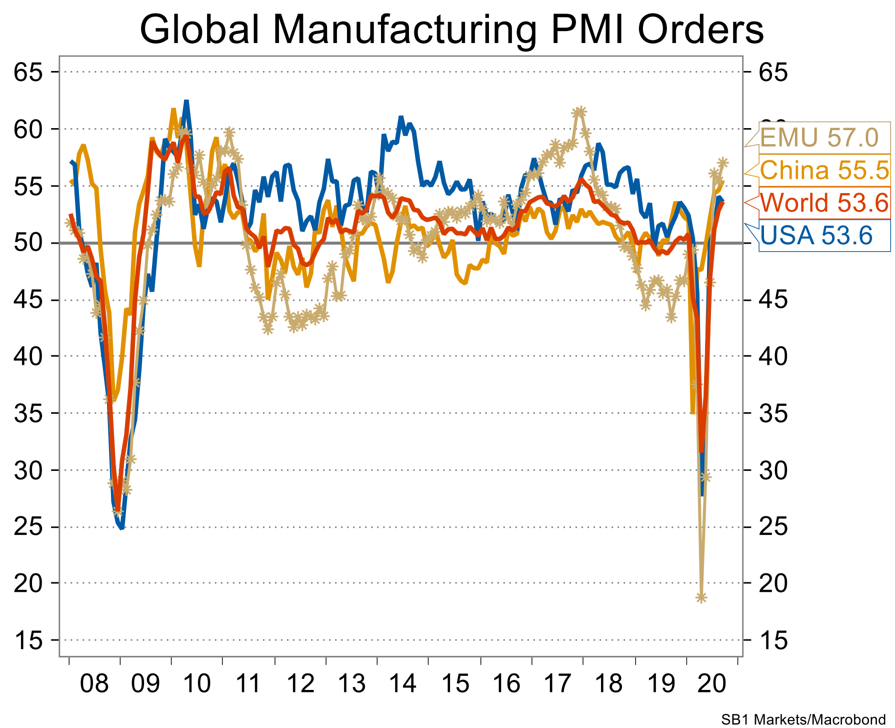


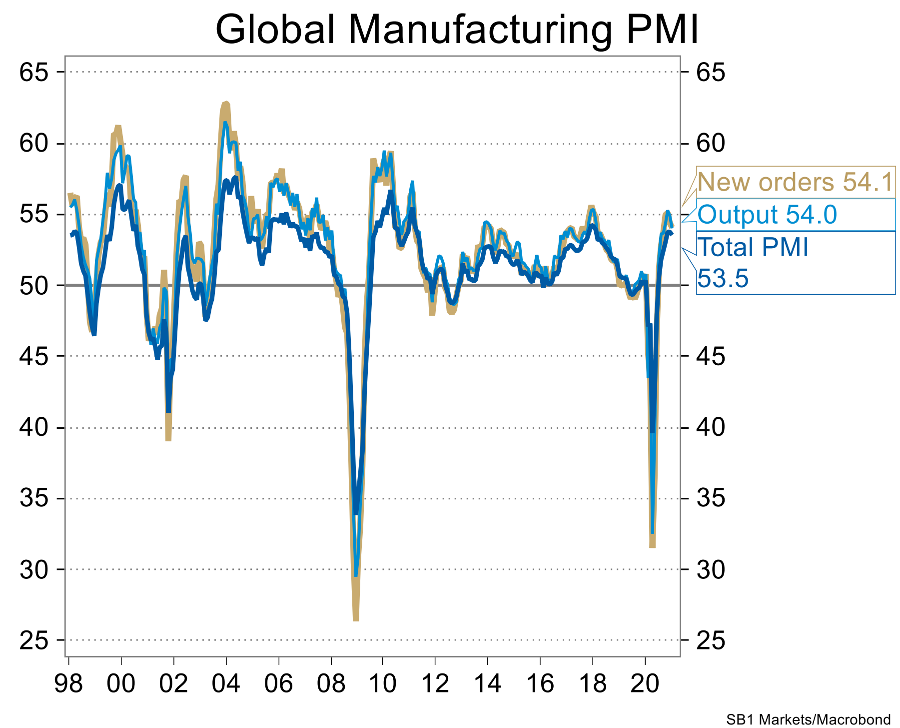


- No signs of a slowdown, of course

Manufacturing PMI signals growth in major countries/regions

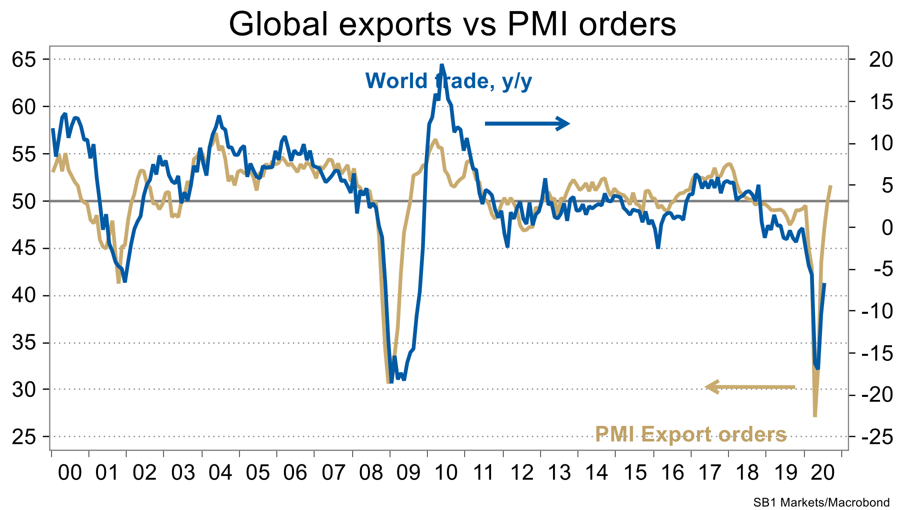
Orders are increasing at the fastest speed in Europe, from the steepest decline

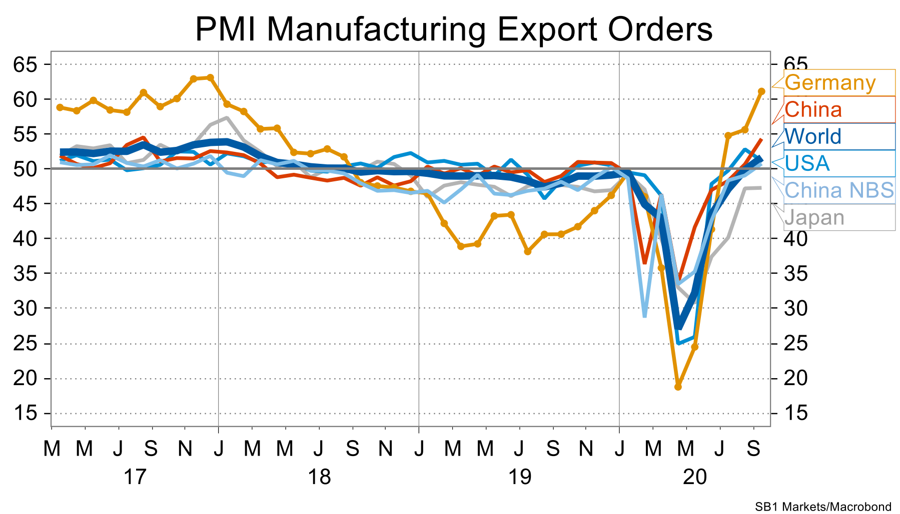




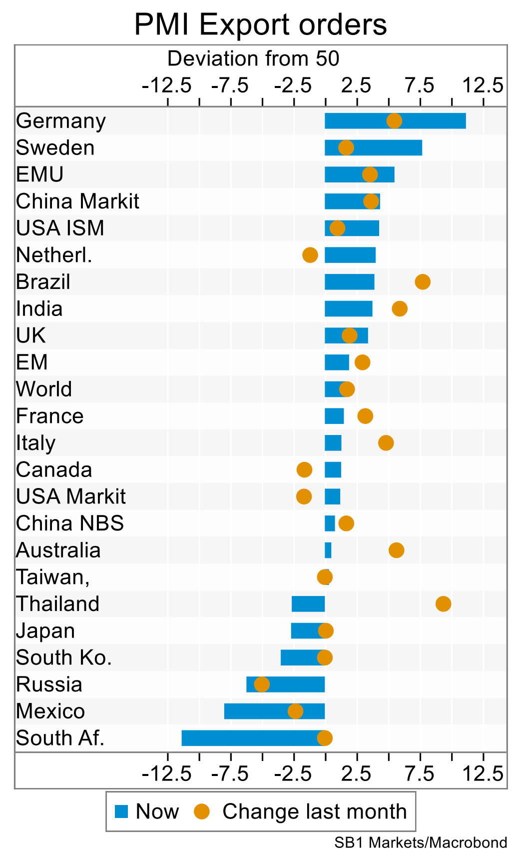
Export order PMIs further up but does not signal a fast recovery, Germany at top

Some Asian & EM countries still below the 50 line





- Most countries are now reporting an increase in export orders (index >50)
  - » Germany has moved to the top of the list, from the bottom in April/May!



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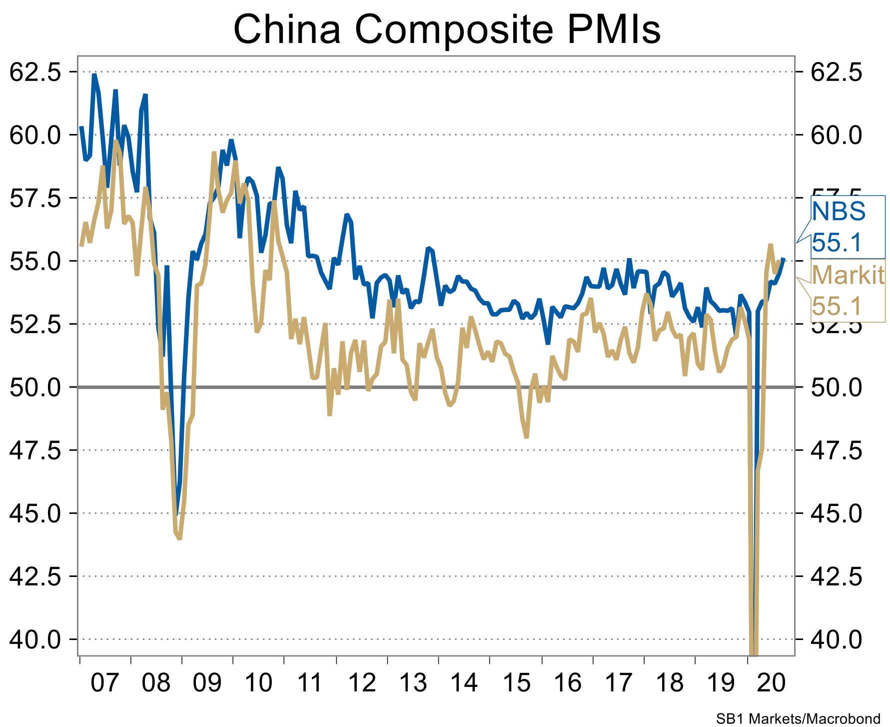
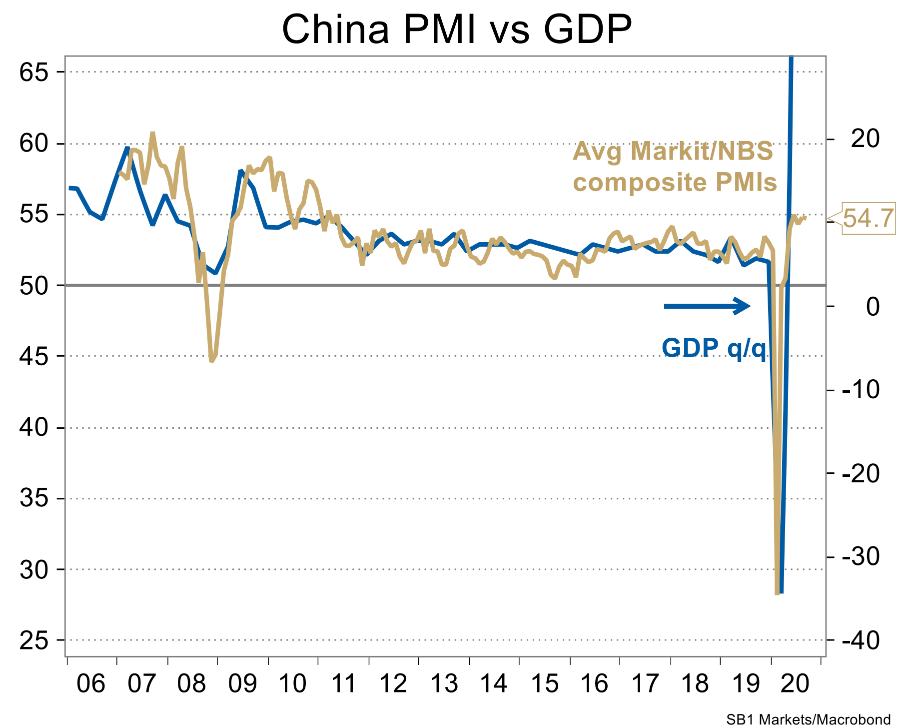
September PMIs in sum steady, signalling growth well above trend

The NBS composite PMI rose by 0.6 p to 55.1, we estimate a 0.8 p decline in Markit's PMI

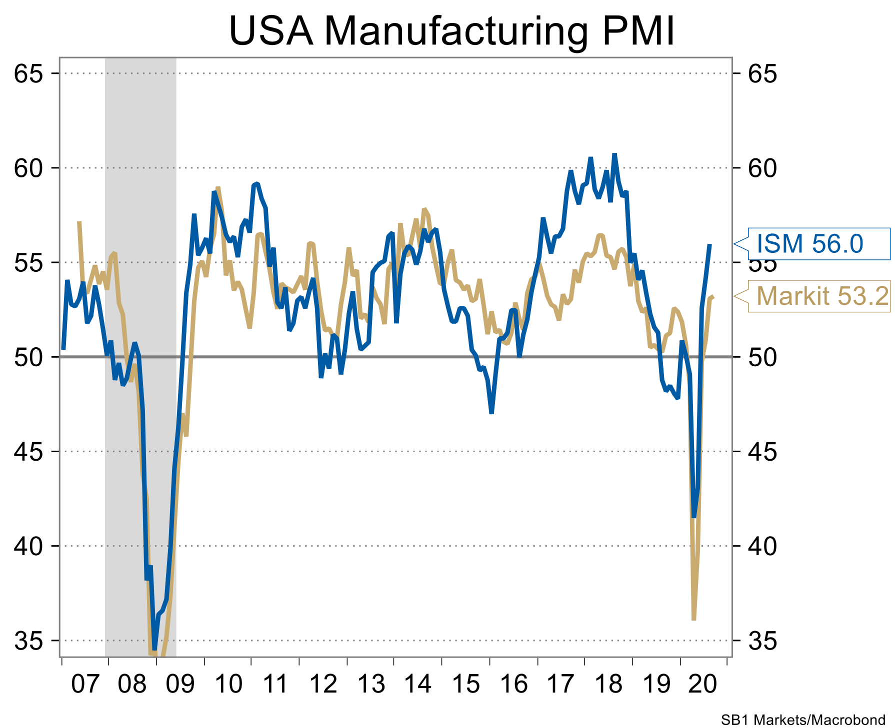


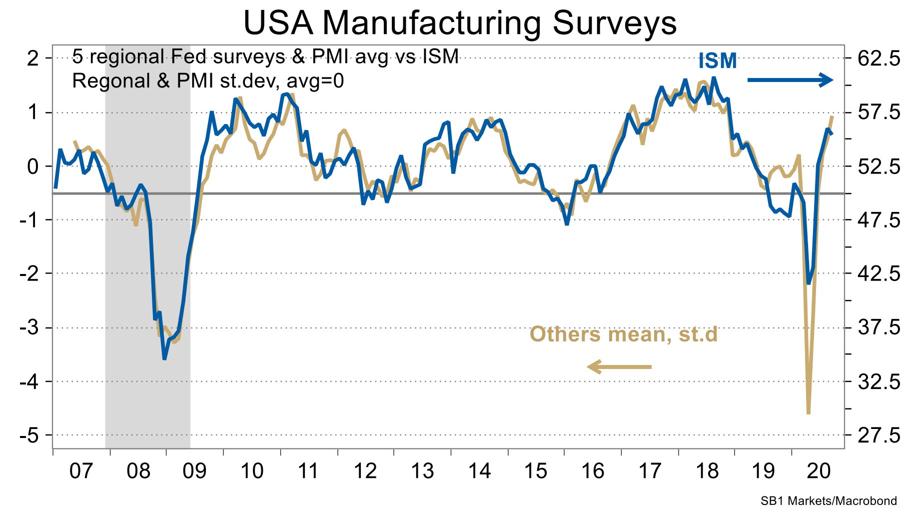


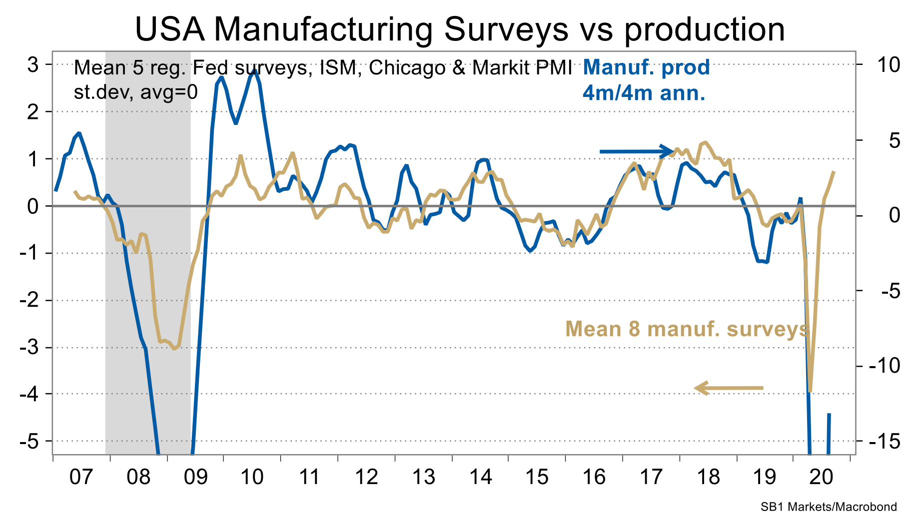
- The NBS' 'official' composite PMI edged up to 55.1 in Sept, up 0.6 p. The manufacturing index rose by 0.5 p to 51.5, services up 0.7 p to 55.9. The higher level of the services index is needed to bring activity in the service sector back to pre corona levels (it is still well below the pre corona trend, while manufacturing is fully recovered)
- Markit's manufacturing PMI inched down to 53.0, composite down 0.8 p if we assume a 0.7 p rise in services (not yet reported)
- In sum, these two PMI data sets confirm a continued recovery in the Chinese economy (a 8 – 9% growth pace), and growth above trend in Q3 too – which is needed to close the 2 – 3% negative output gap in Q2

Other manufacturing surveys somewhat more upbeat than the ISM in Sept

In average, the surveys are not that impressive, we expect growth well above an average pace



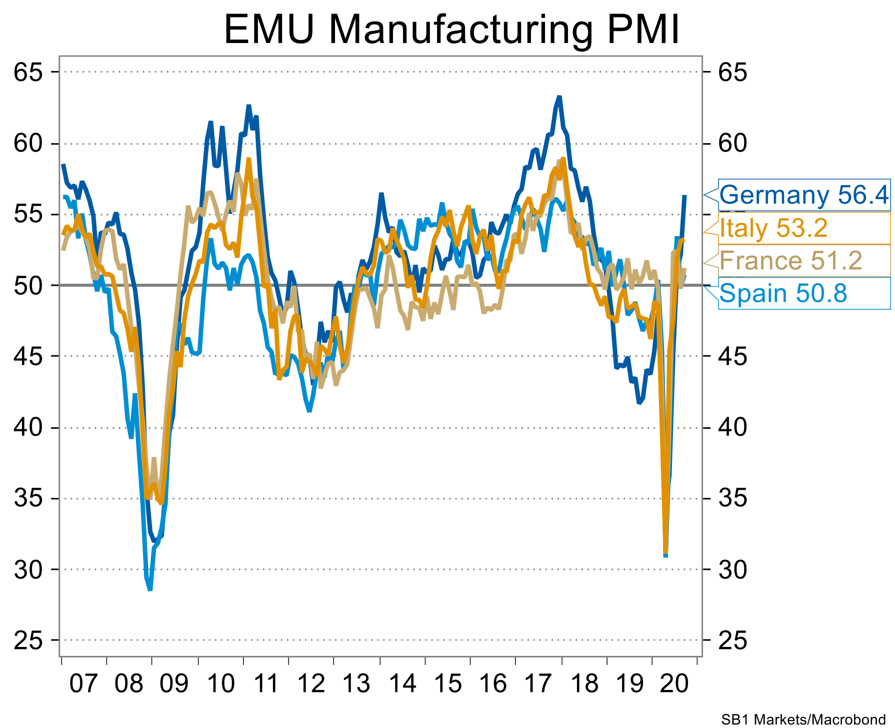


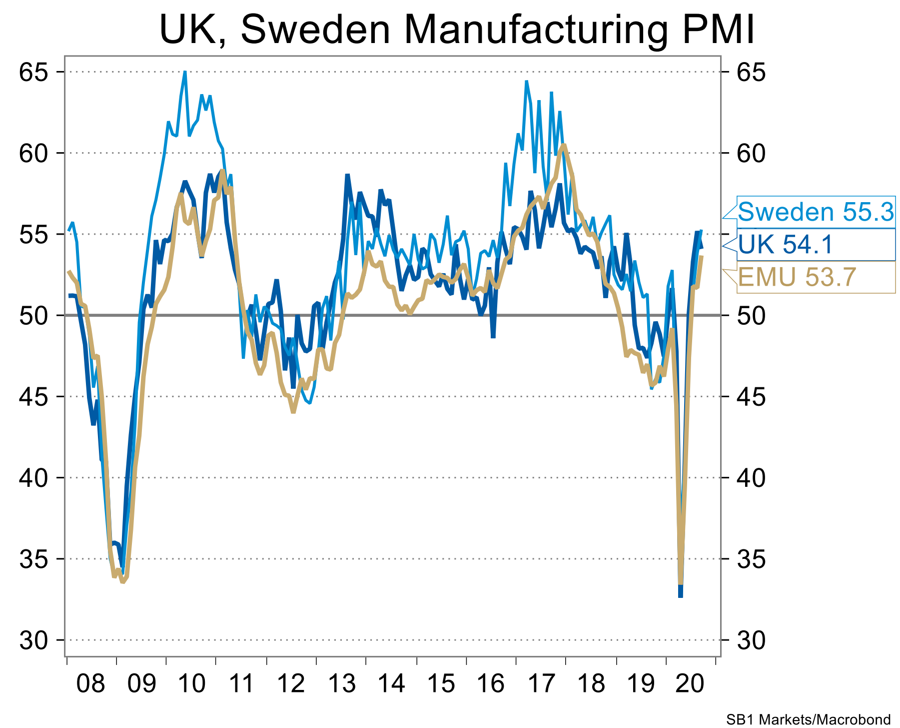


- Markit's final manufacturing PMI at 53.2, 0.3 p weaker than first reported (and up 0.1 p from Aug)
- Actual manufacturing production is on the recovery track but is still some 7% below the pre corona level
- We expect a continued growth the coming months. Core durable goods orders are above the pre corona level and goods consumption is strong

Eurozone manufacturing recovery gains speed, as in UK and Sweden

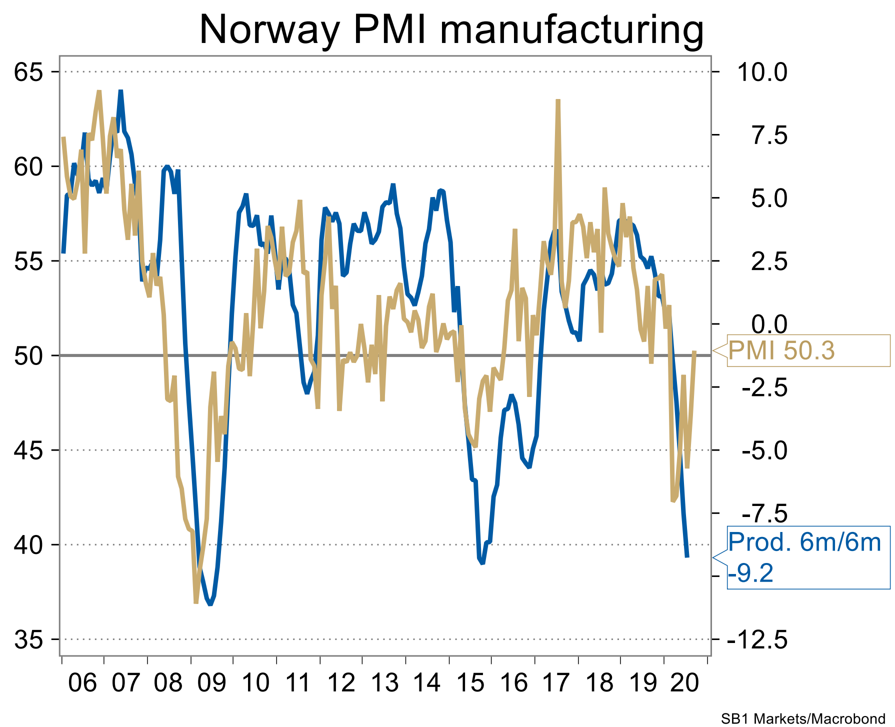
The PMI was unchanged at 53.7 in the final report (+2 from Aug). All main four countries above 50

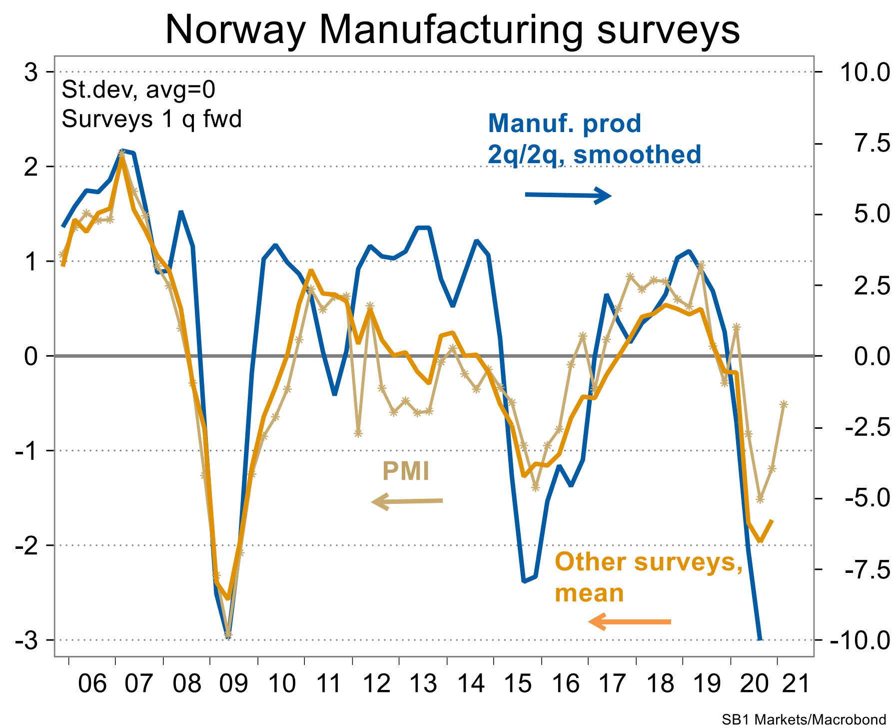




Manufacturing PMI finally (just) above 50 in September

The manufacturing recovery has so far been subdued, PMI signals a stabilisation, at best





- The manufacturing PMI rose to 50.3 in September, a 4.2 p increase, we expected up to 48. Activity in the Norwegian manufacturing industries fell in the spring but did not experience a deep setback. So far, we have not seen any upturn either, and the PMI signals just a stabilisation
  - » The details were not bright, even as all sub indices rose. New orders failed to increase and employment continued to decline
- Other surveys are still signalling a substantial decline in manufacturing production

Norwegian manufacturers fared better during the spring but lags now

… at least growth wise (Norway is still ahead, level wise)