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Macro Weekly

Week 28/2021

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Highlights, corona update

The world around us

The Norwegian economy

Market charts & comments

Last week

The virus

- **The far more contagious Delta variant** is gaining market share, rapidly - and as more countries are reporting a steep increase in new cases, some restrictions are reimposed – and markets are taking notice. UK, Portugal, Russia, Spain, Netherlands, France, Greece, Denmark and Switzerland are among countries that are reporting a sharp increases in new cases
- However, in rich countries, where the old and exposed are vaccinated, the number of hospitalisations & deaths are just slowly increasing, and remain at very low levels. Thus, we are still far away from another heath crisis. We assume vaccinations will gain speed if the virus situation escalates, and slow the spread of the virus before a new, serious health crisis occurs
- **Norway** is now vaccinating more people per day than any other rich country ever has done, barring Israel in January. Still, the immunity level in Norway is the lowest among rich countries. The no. of new cases is increasing marginally but very few need hospital treatment (still less than 30 persons!)
- **Mobility** flattened/declined marginally last week. It may be due to the spread of the Delta variant

The economy, part I

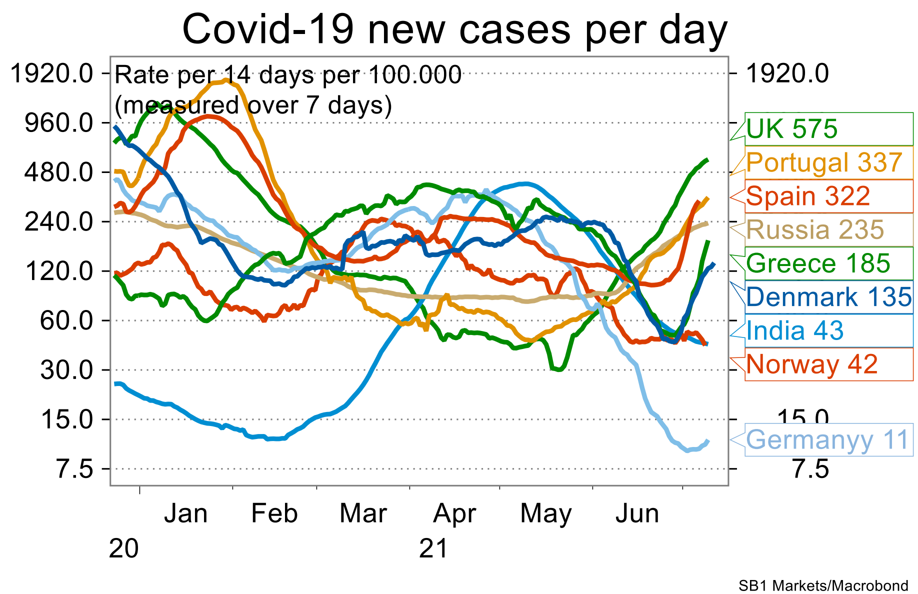
- **Global PMI**
  - » The global PMI fell by 1.8 p to 56.6 in June, with negative contributions from US, China and several other countries. In Europe, the PMIs rose further, as activity in the service sector recovered. US services reported slower growth (but still very high). While growth remains strong in the rich part of the world, EM countries are at the lower part of the chart. Global delivery times are still increasing fast, as are prices. But the growth in the global economy has probably peaked
- **Auto sales**
  - » **Global sales** fell some 4% in June, and is now 12% below the 2019 level. The decline in June was broad, led by the US and China (where sales the previous months were revised down). In the Euro Zone, sales remained at 20% of H2-20 level, we suppose mostly due to weak demand. In EM x China sales probably fell slightly, even if sales in India recovered somewhat (but was still 50% below April sales).
  - » No doubt, <u>lack of semi-conductors</u> explains the lion's share of decline in <u>global</u> sales. Auto producers world wide now report that this problem will not be solved anytime soon. If auto production is cut by 5%, global GDP will be reduced by some 0.1 pp, not a serious problem. However, other sectors are also reporting negative impact for data chips shortages

Last week: The economy, part II

- **China**
  - **Credit growth** accelerated somewhat in June, but the trend is still down, and the credit impulse is clearly negative
  - However, on Friday the **PBoC announced a cut in banks' reserve requirements** by 50 bps, following a surprising pre-warning on Wednesday. The impact on banks lending capacity is limited (3 weeks extra lending) but the policy signal may be more important. The authorities want to keep credit growth in check in order to reduce the risk for a future credit bust. On the other hand, they do not want to curb growth too much now either – a common trade off in China (and many other places…)
- **USA**
  - **The FOMC** is more divided than normal, but the majority still thinks the progress towards its target is not yet substantial, and that the expansionary policy should continue for a long while. Other members seem to be more eager to remove some of the QE earlier, and more members want to hike rates earlier. Bond yields have fallen sharply, probably due growth concerns but equities and commodities were not weak
  - **The no. of unfilled vacancies** remained at a record high level in May, confirming business surveys. However, the problem did not get worse in May/June, and the no. of voluntary quits fell slightly (but is still the 2nd highest on record, signalling a very tight labour market)
- **EMU**
  - **ECB has lifted its inflation target** to symmetric around 2% from 'below but close to 2%', signalling somewhat larger tolerance for inflation (at least vs. the old BuBa style). On the other hand, the ECB will include owner-occupied housing cost in the inflation target, bur probably in a way that will not influence inflation that much. However, as the housing market is now strengthening, and higher housing costs may have some impact on monetary policy. The 3rd change: ECB will focus more on implications of financial imbalances rather than inflation implications of a monetary developments, which has turned to be a complicated science. Again, a Bundesbank pillar is buried (perhaps just before the BuBa approach could be vindicated, at least in the US…)
  - **Retail sales** rose 4.6% in May, and sales are 5% above the Feb-20 level
- **Sweden**
  - **GDP** grew less than expected in May, and April was revised down. Still, GDP is now close to the pre-pandemic level
- **Norway**
  - **Mainland GDP** rose 1.8%, twice as much as expected, and April was revised slightly upwards, and GDP was just 0.7% below the Feb-20 level (NoBa assumed -1.8% in the June MPR). Services recovered sharply but still operates far below normal levels. We expect further lifts in GDP the coming months, which paves the way for a NoBa hike in September
  - **Core CPI** once more surprised on the downside, up 1.4% y/y as food & airline ticket prices were lower than we expected. Total CPI is just below 3%, due to the hike in electricity prices
  - **House prices** rose by just 0.2% in June, less than expected (NoBa 0.5%, we 0.6%). Prices rose slightly in Oslo, following 3 months decline. The market balance suggest higher prices, even (marginally) in Oslo. However, buyers are aware of the coming rate hikes this time?

The Delta variant is rapidly taking over the virus market

We have to add more countries to the spaghetti chart below every week…



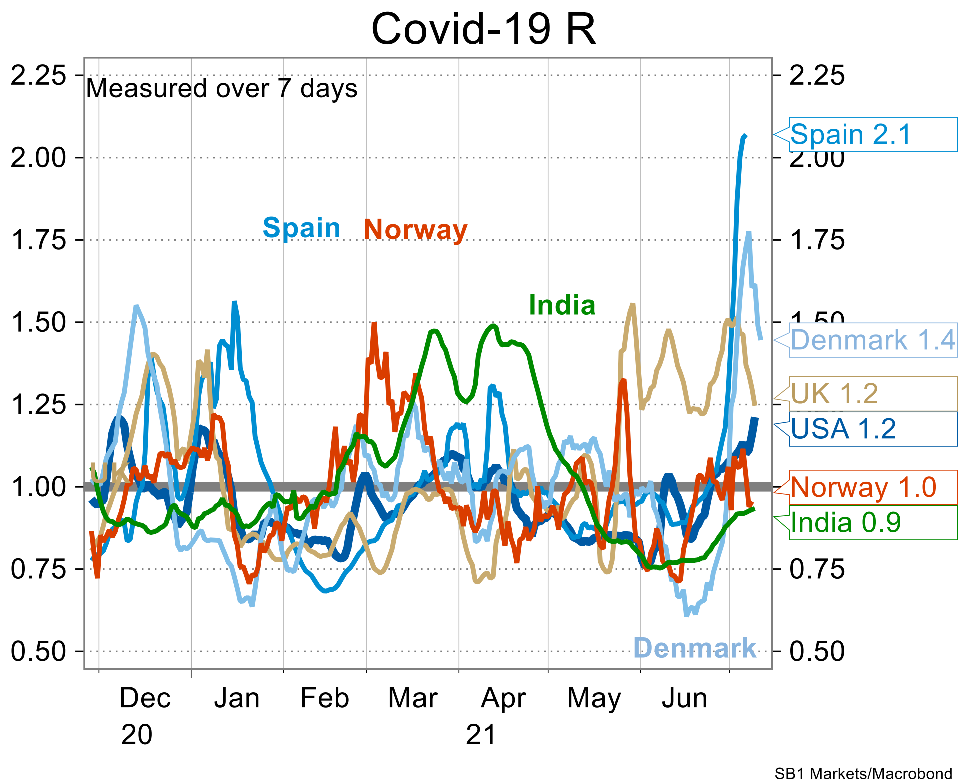
- The **Delta virus** will very likely capture the corona virus market in most countries
- UK, Portugal, Russia, Spain, Greece, France, Netherlands, Denmark are all hit
- On the other hand, while the no. of **hospitalisations,** and even more, **deaths** are on the way up in these countries, the level is low, and the hospitalisation rate is still falling – and the death rate remains very low
- Thus, there **will not be a health crisis anytime soon** but at the current growth rates there may be some clouds on the horizon. (See more next page)
- In **Norway**, the no. of new cases is increasing slowly but the no. of hospitalised remains very low
- In most **other rich countries**, the no. of new cases are stable or are still falling, even if restrictions are eased and mobility has increased sharply

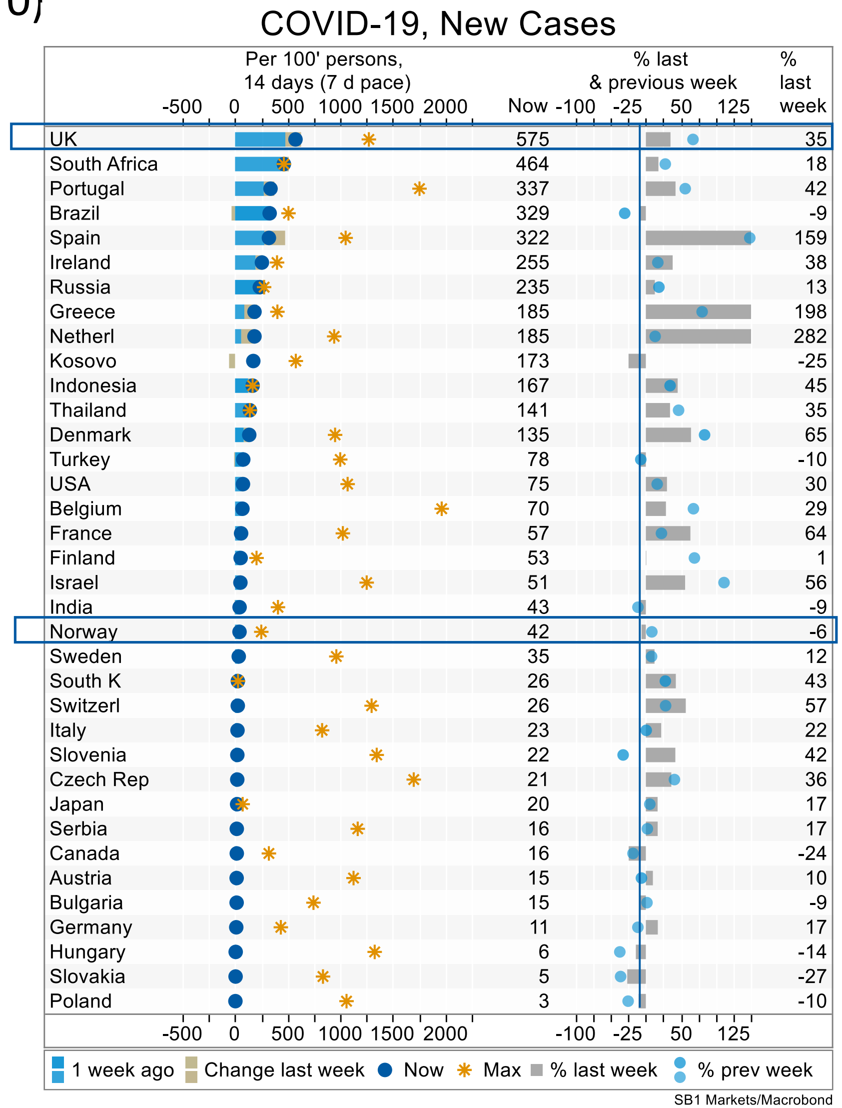
Source: Financial Times, June 20

A majority of countries are reporting more cases, the Delta to blame

UK at the top of the list, but just up 35% last week (from 70)

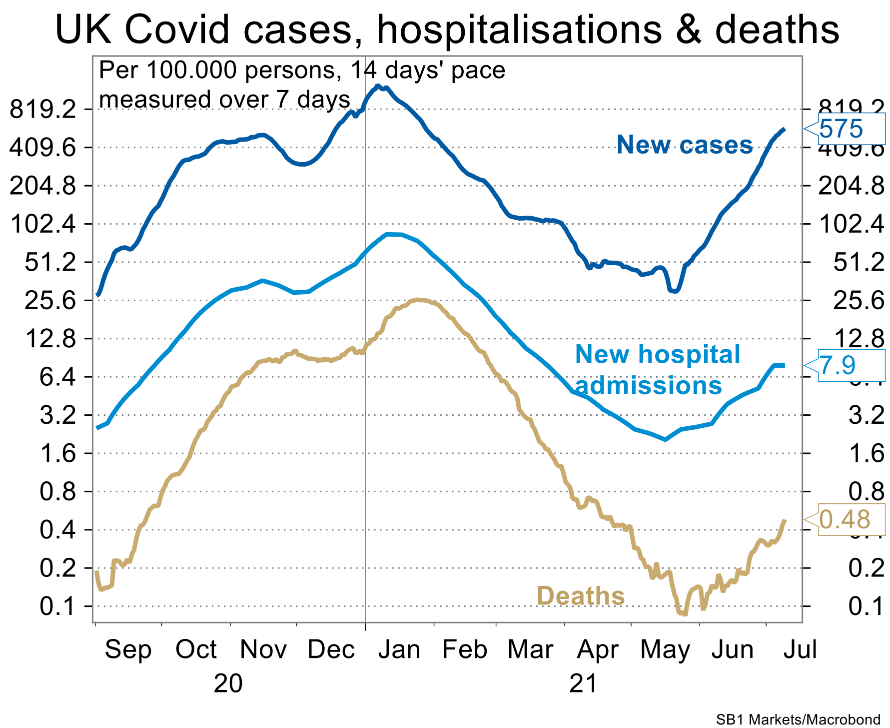
Spain, Greece and Netherlands are 'exploding'

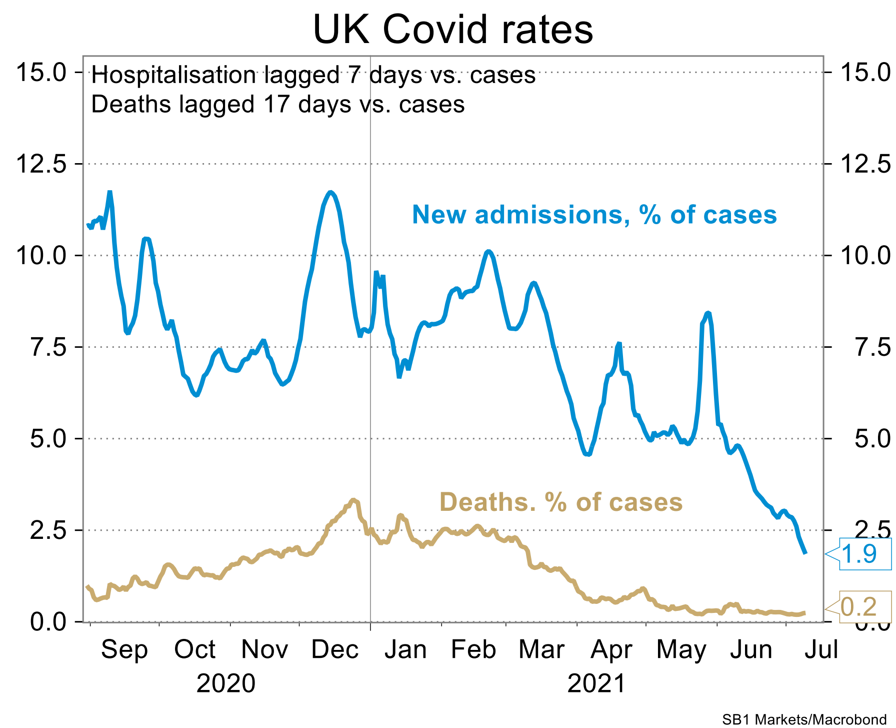




UK: Still a moderate increase in new hospital admissions, deaths

… And from very low levels, compared to before the vaccination process





- The no. of **new cases per day** is steadily growing, by 40% - 70% per week (R=1.3 – 1.5), and will reach the January peak by the end of the month – and by that time the immunity rate will have increased further (albeit not by much, UK immunity is increasing by just 1.5 pp per week now)
- However, the **hospitalization rate** has fallen sharply as both the old and other risk groups are vaccinated. The rate is approaching 2% from appox. 8% in January – and it is still declining. On the other hand, UK hospitals will be filled up once more if nothing changes the coming months. Hopefully, vaccination will speed up again, from the present 1.5% of population per week
- The **case fatality rate** (of those tested positive) has fallen even more, to 0.2% from close to 3%
- **Implication:** The Delta variant spreads like a wildfire but the number of infected will have to increase to very high levels before the UK will run into a health crisis

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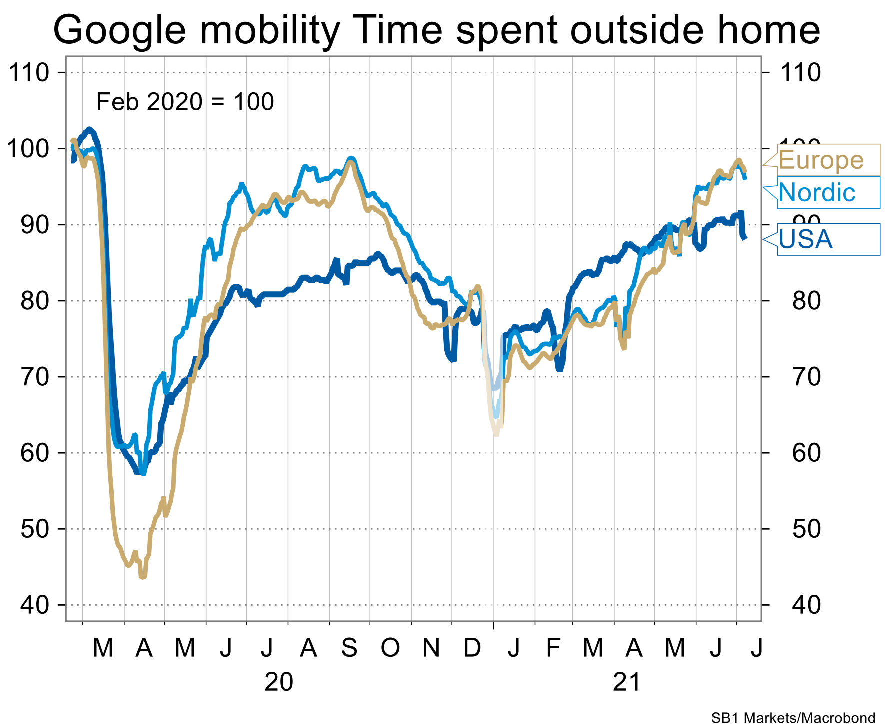
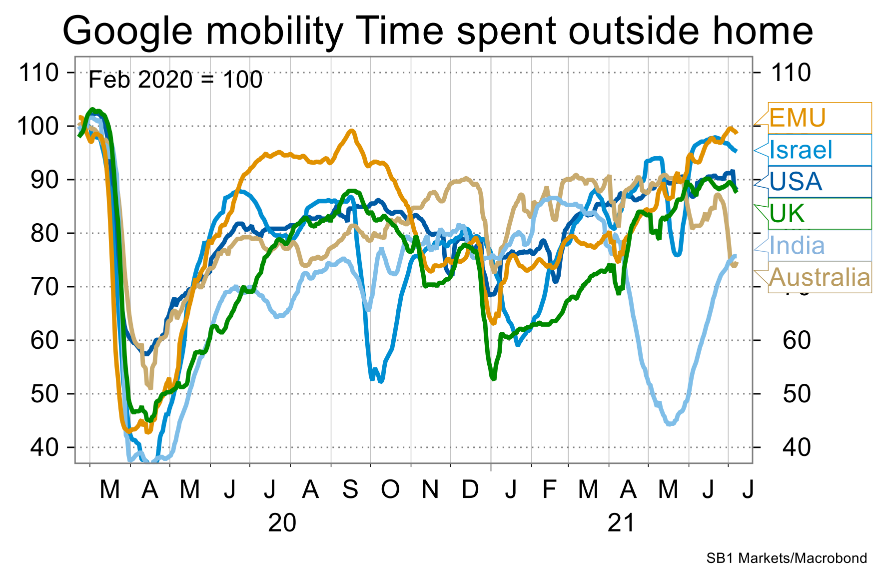
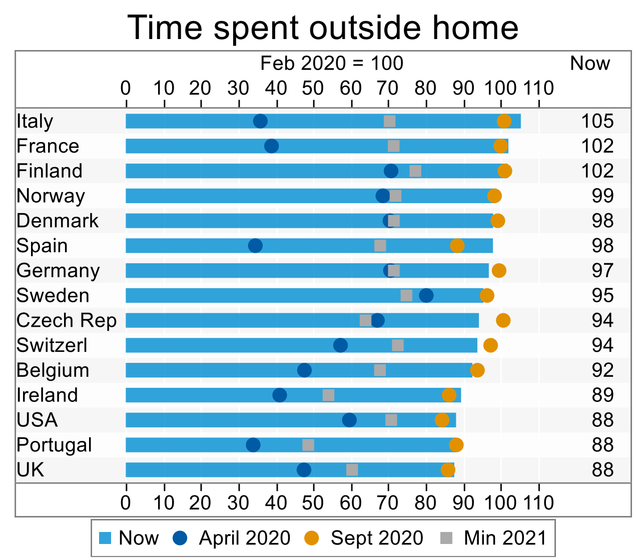
Are we seeing some impact of the Delta on mobility (outside India)?

Mobility sharply down in Australia, and UK is sliding?

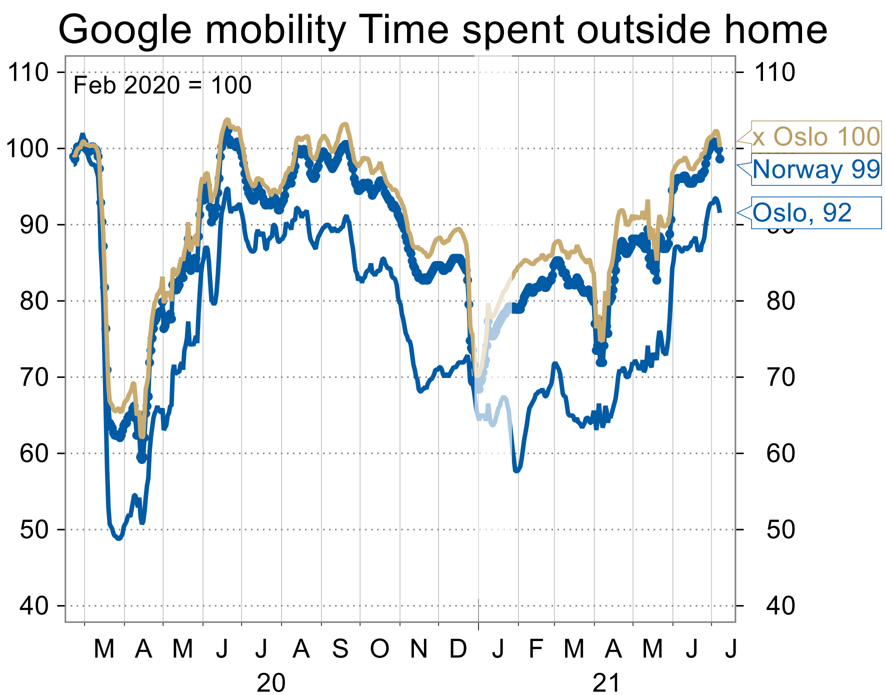




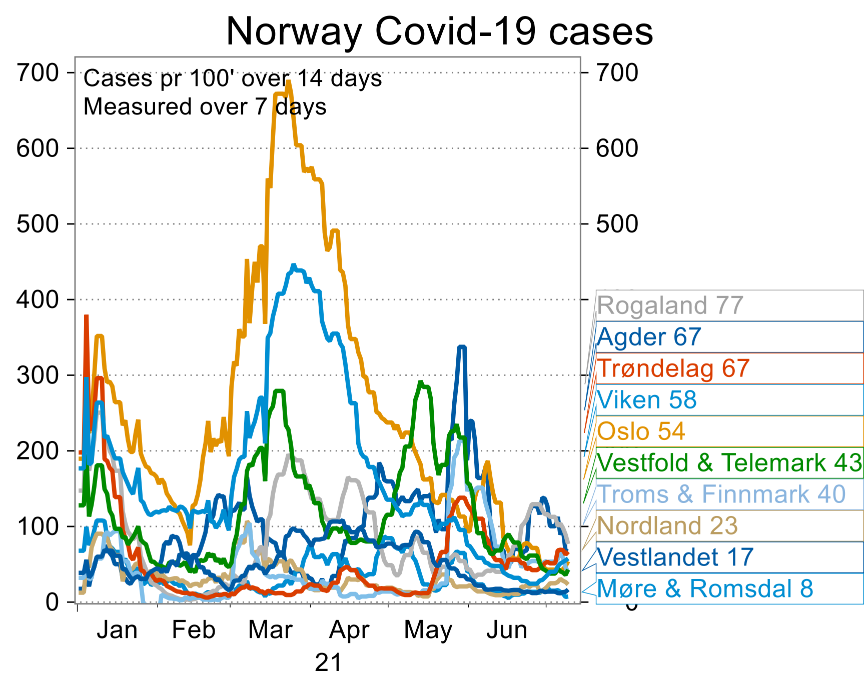


Mobility almost back to normal most places in Norway

Oslo still 13% down, according to Google. Some local outbreaks, …seems manageable



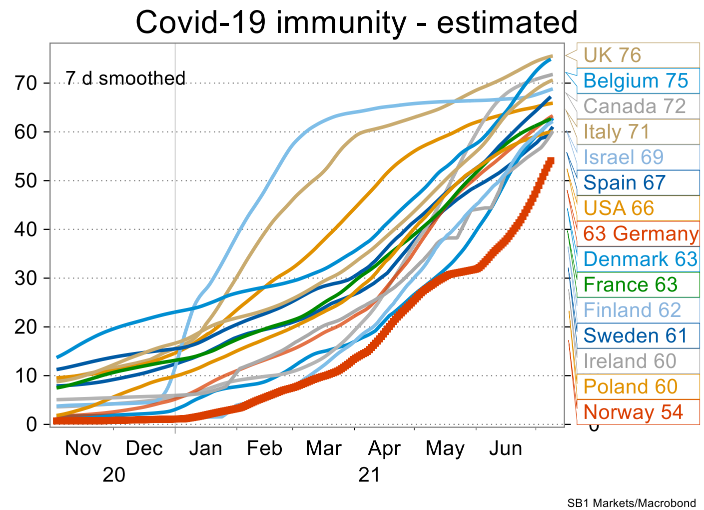
SB1 Markets/Macrobond

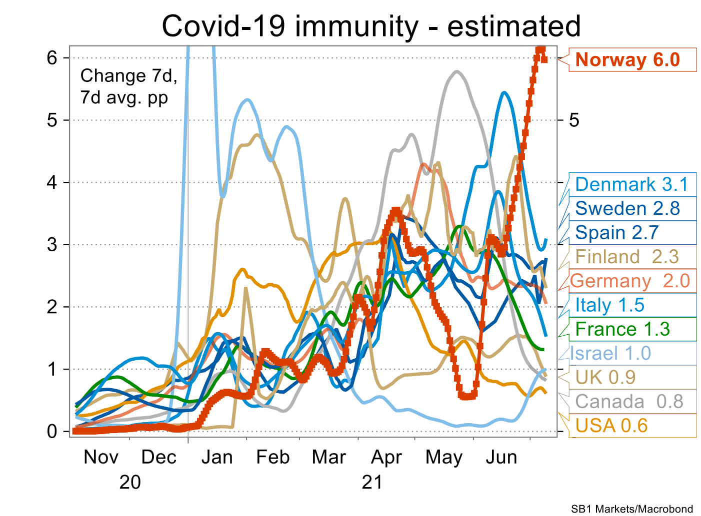


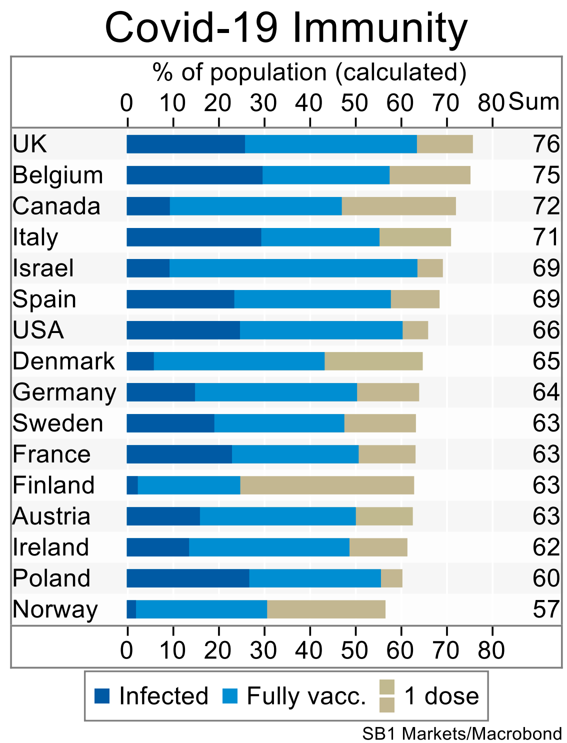
SB1 Markets/Macrobond

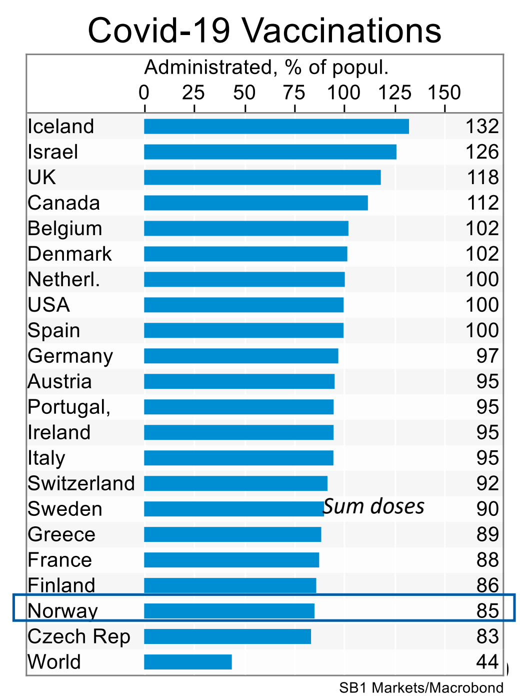
Vaccinations: Finally, Norway in the lead, at least with regards to the pace

However, Norway is a laggard vs the level, as we don't use AstraZeneca and J&J's vaccines



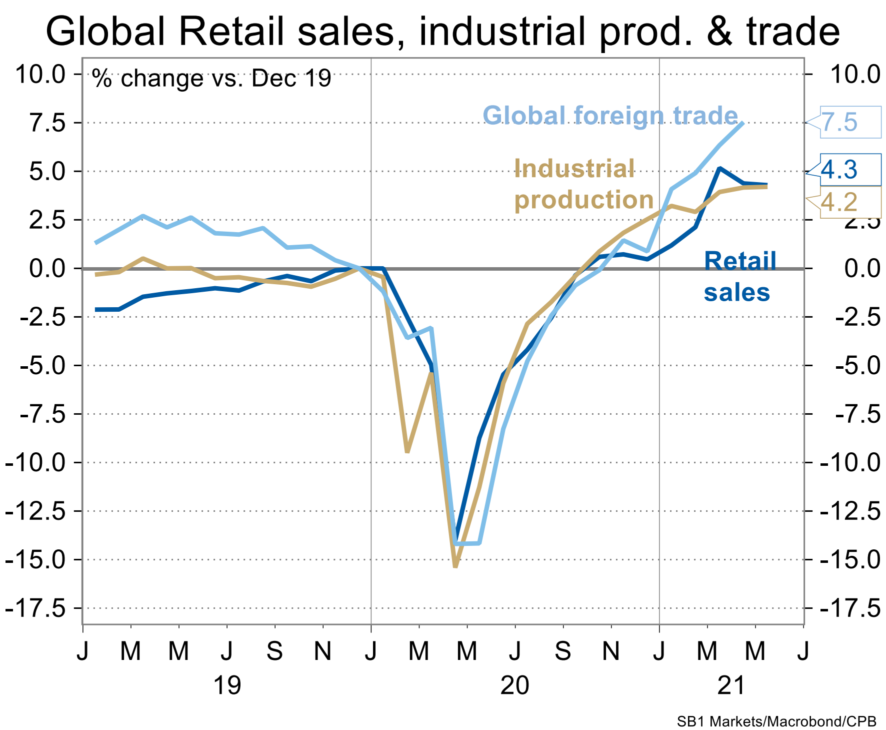


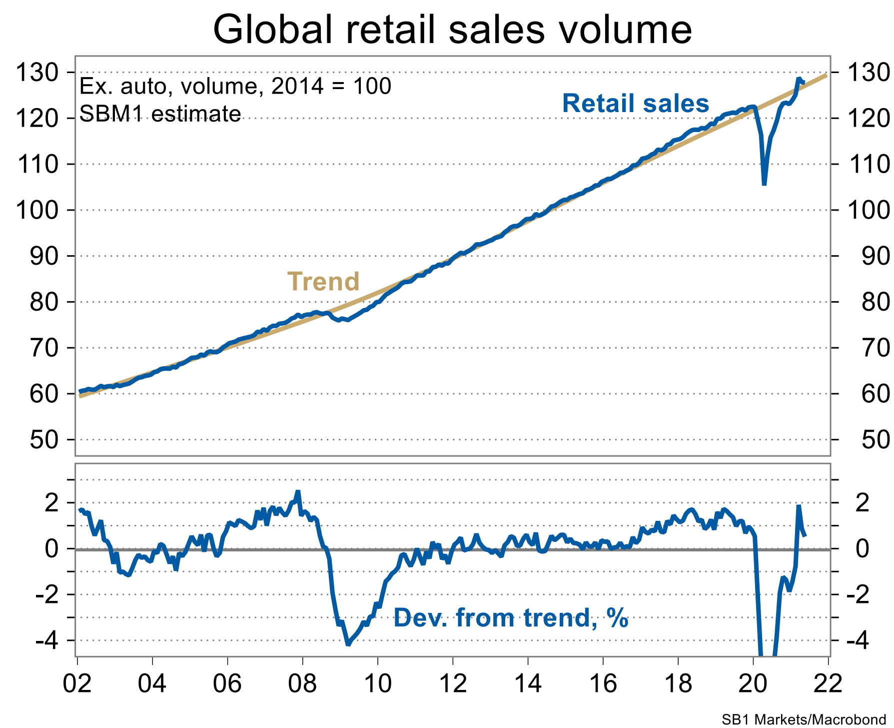




We calculate the infected rate by assuming a 0.66% infection fatality rate, and a 90% immunity from infection.
We assume those who have been infected are vaccinated in line with others. Denmark not fully updated

Global retail sales have flattened – and growth in manufacturing is slowing

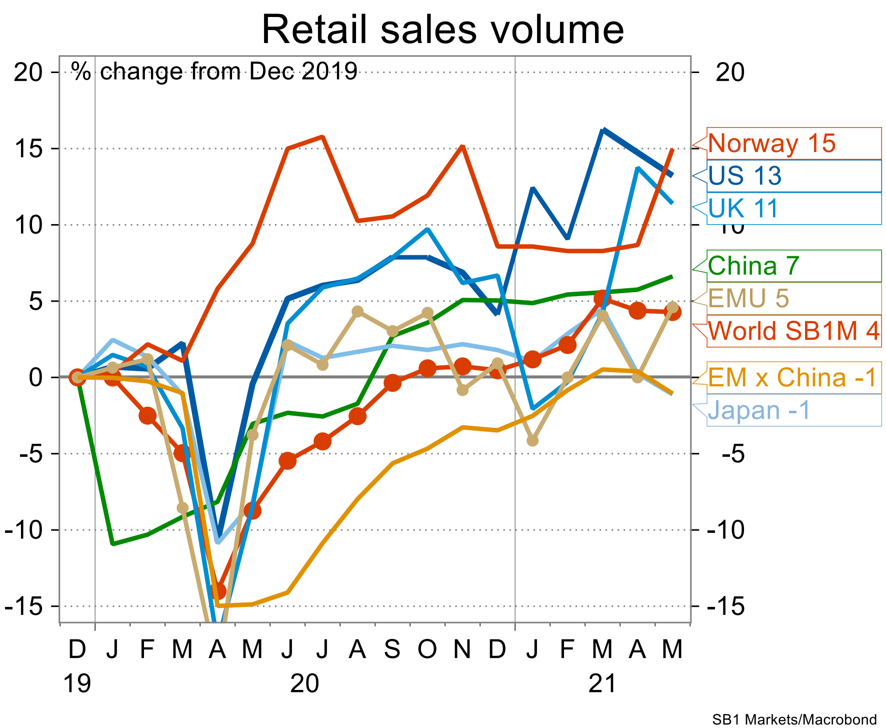


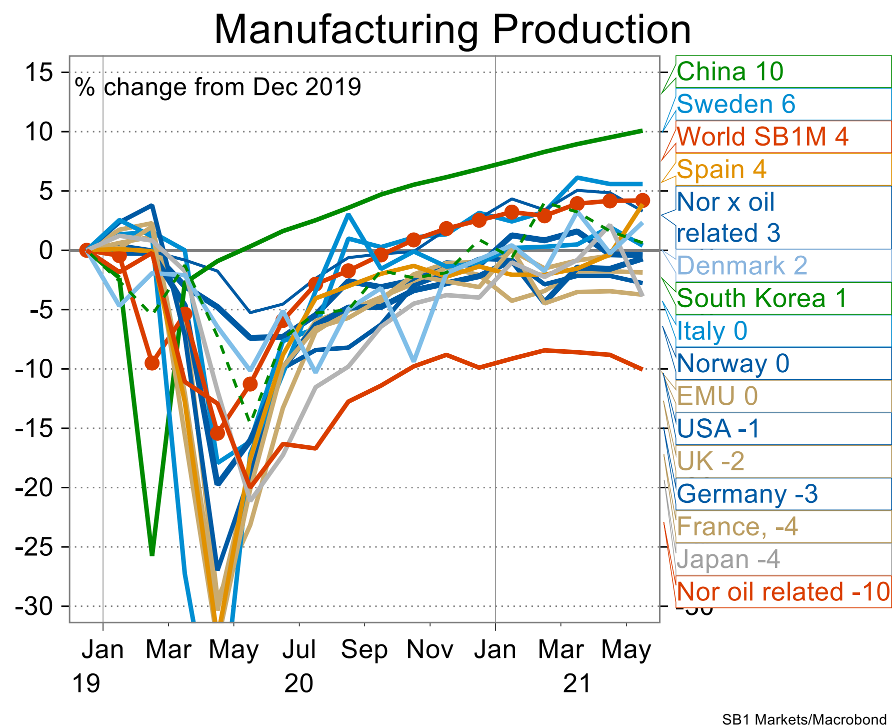


- **Retail sales** probably fell slightly in May, even if EMU sales rose close to 5%. Sales rose just marginally in China, fell in the US and we assume in India too. Sales are still 4% above the pre-pandemic level
- **Manufacturing production** climbed further in May, and is also 4% above the pre-pandemic level
- **Global foreign trade** rose further in April, to 7.5% above the pre-Covid level, according to CBP in Netherlands – and the trend is straight upwards

Volatile retail trade data, but the trend is up

... At least until we can spend more money on services. Manufacturing is still trending up, but slower





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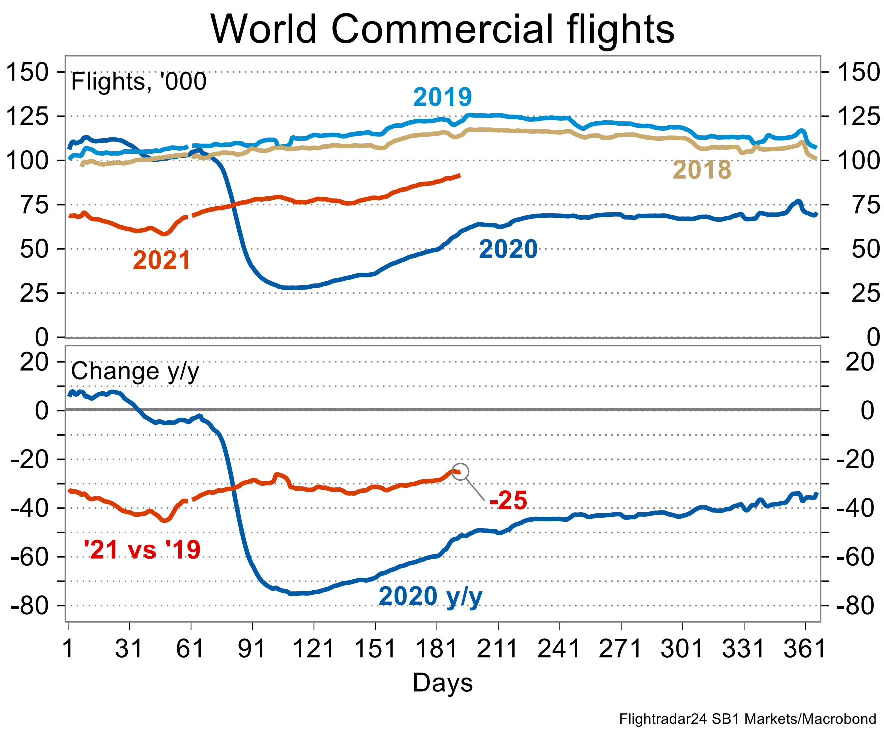
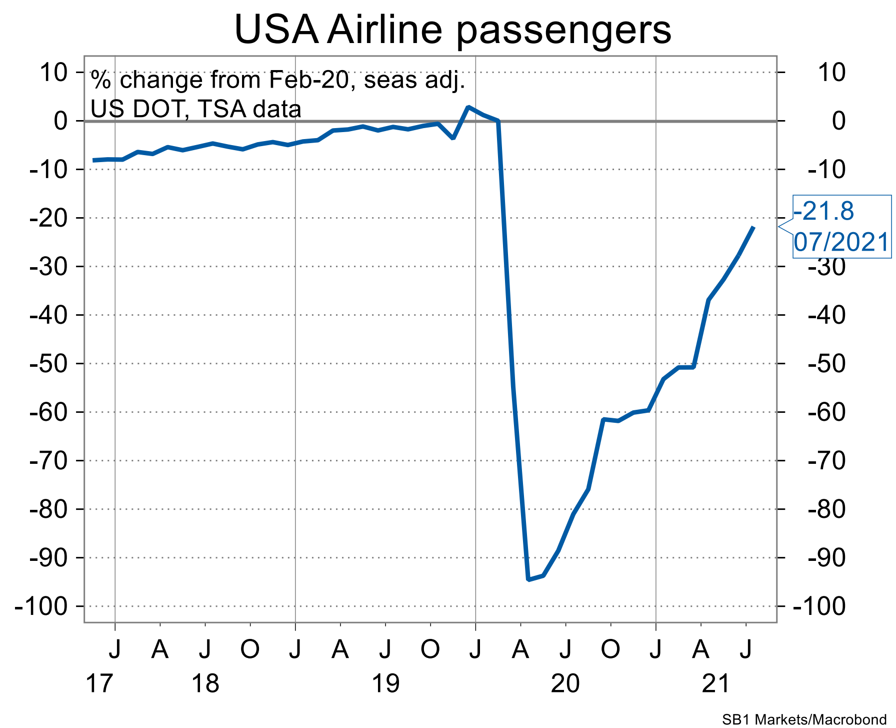
Global airline traffic on the way up again – still 25% below the 2019 level

US airline traffic straight up, but still 22% below par due to still little travel abroad

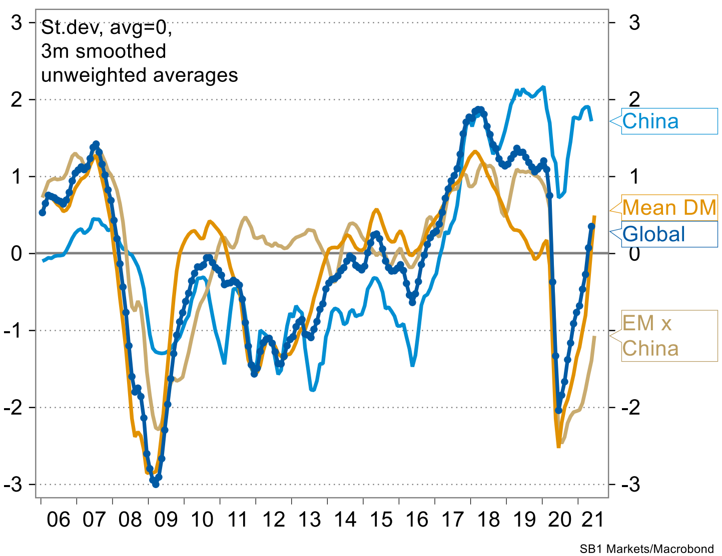




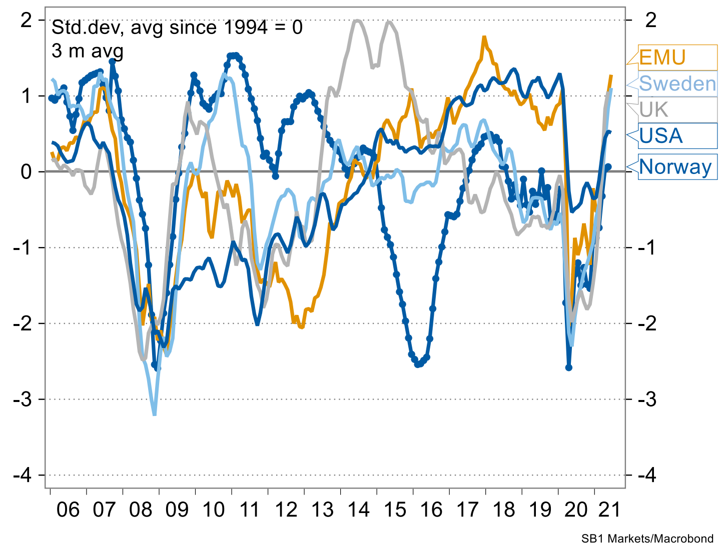
Consumer confidence is still recovering – remains below par in most EMs x Ch

In Europe confidence is well above avg., and above the pre-pandemic level

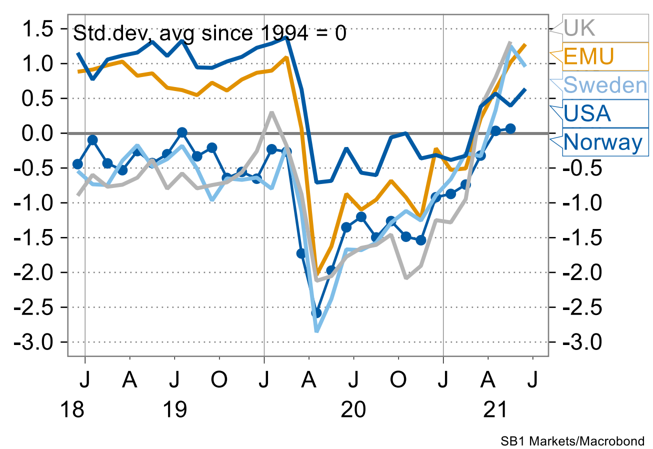
Global consumer confidence



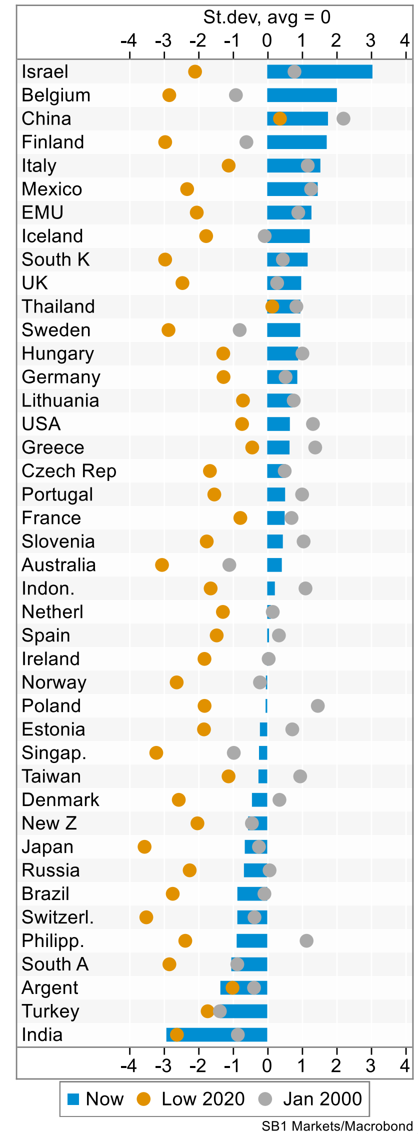
Consumer confidence



- US is reporting confidence above an average level, but (on average for the 2 main surveys) still below early '20 level
- In most EM x China, sentiment is below par
- India is at the bottom, for good reasons
- Israel is at the top, for goods reasons too (at least until June)
- **In sum: Households are ready to spend**



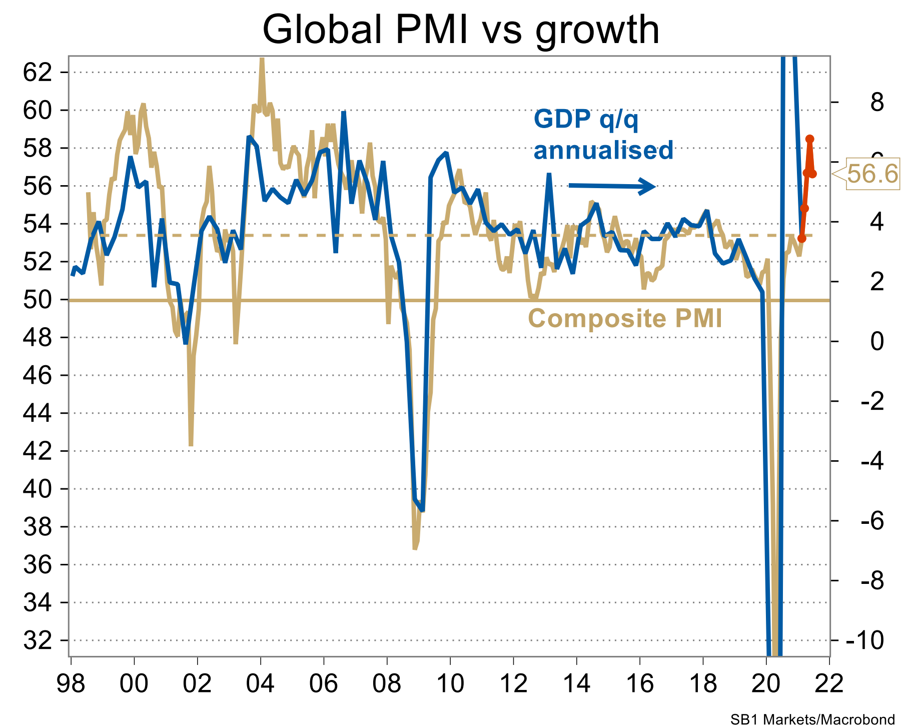
Consumer confidence

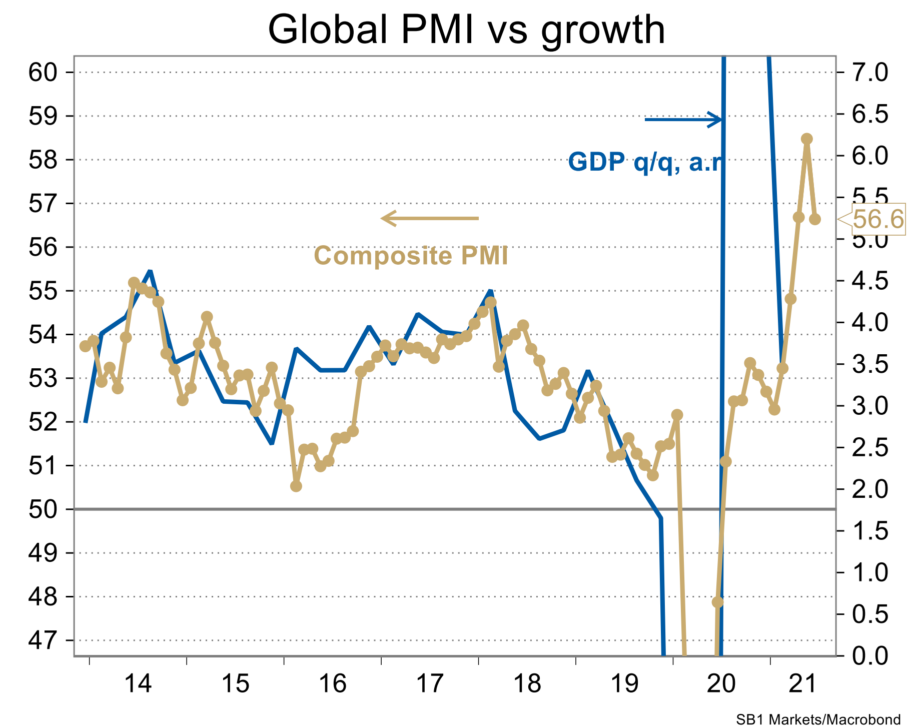


Last observation. Total EMU is leading 1 month on member countries
Norway is the average of Finans Norge & Opinion

Peak PMI: The global composite PMI down in June, still signalling 5% - 6% growth

As we assumed after the weak Chinese report, the global index lost 1.8 p to 56.6

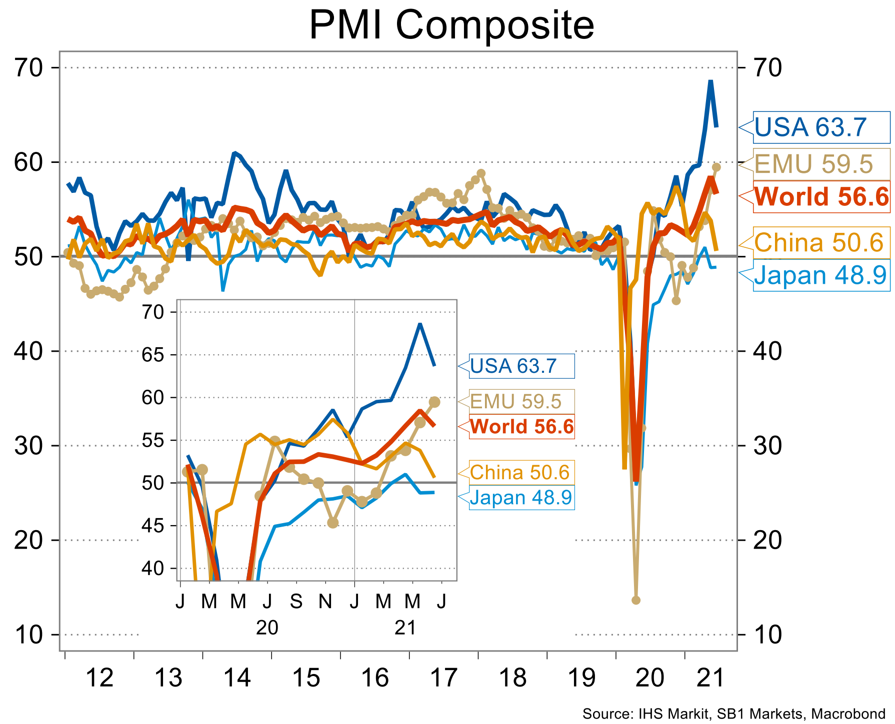


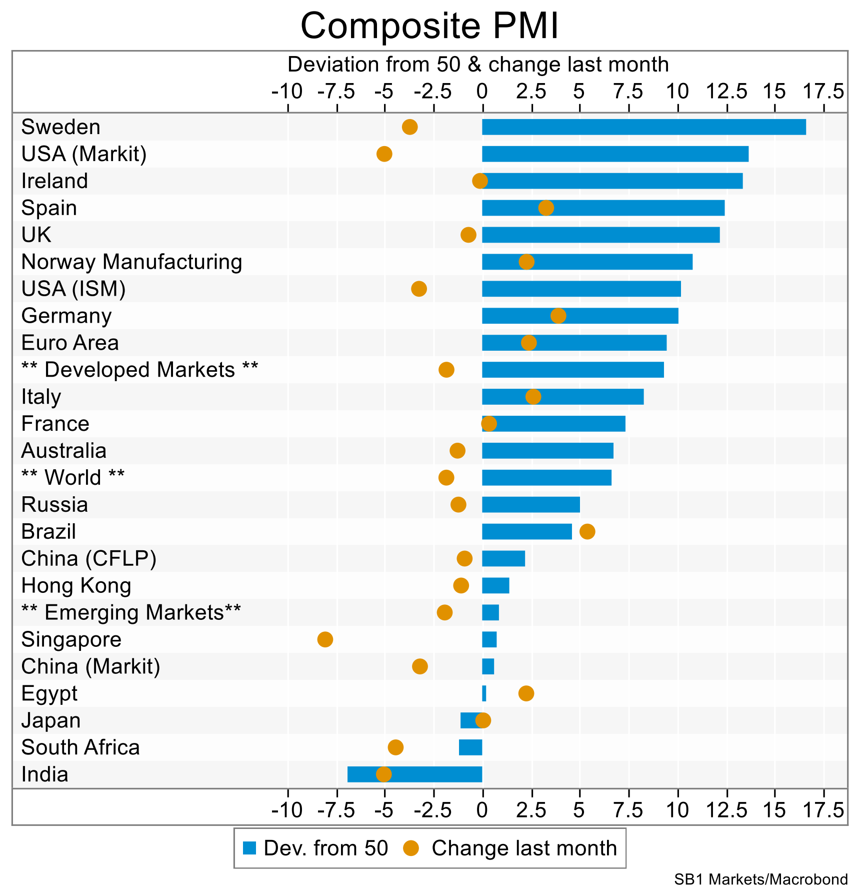


- The PMI signals growth at close to twice the trend growth
- Both services and manufacturing contributed on the downside in June

Rich countries in the lead, while some emerging markets struggle

The Swedish PMI is the best of all, ever. Just 3 countries below the 50-line





- 9 countries/regions up (from 17 in May), 16 down in June (from 8). 3 below the 50-line (from 4)
- Sweden, US, Spain, and the UK at the top.
- The Chinese PMIs were down across the board
- India at the bottom, following a further decline June – even if the virus outbreak has been beaten back and mobility has increased significantly

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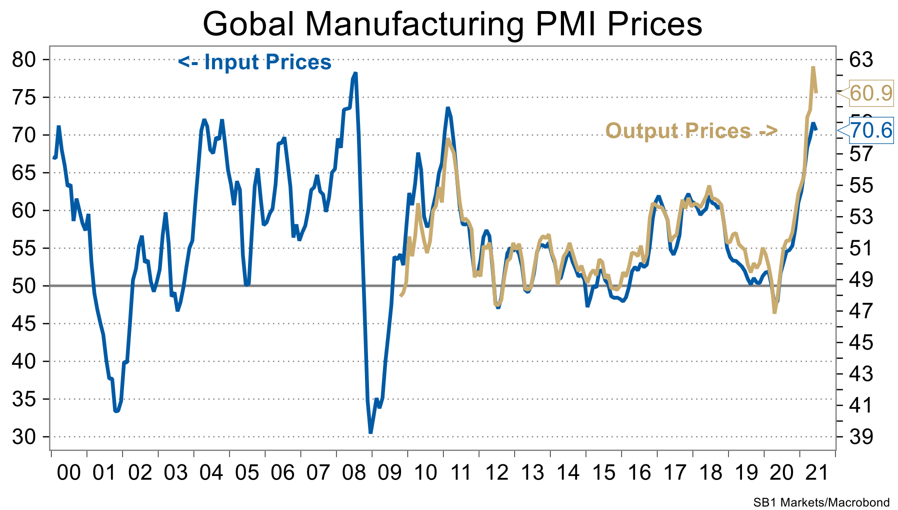
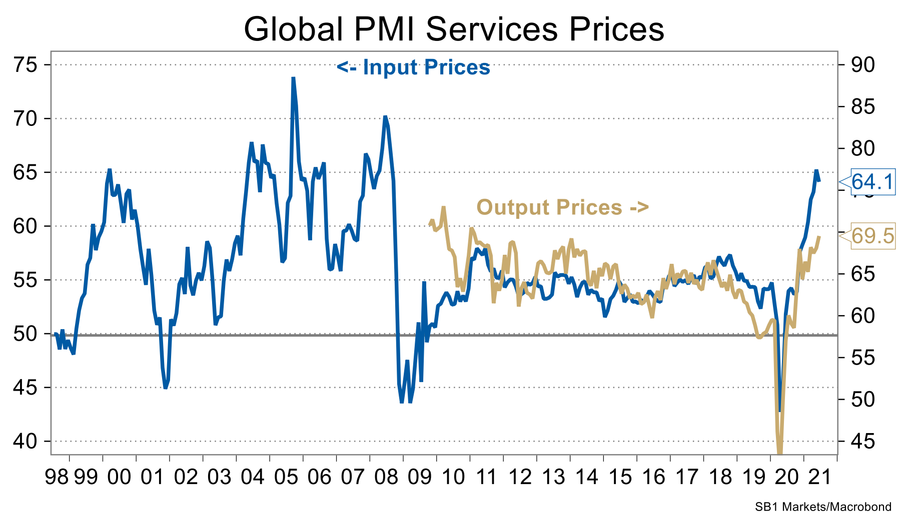
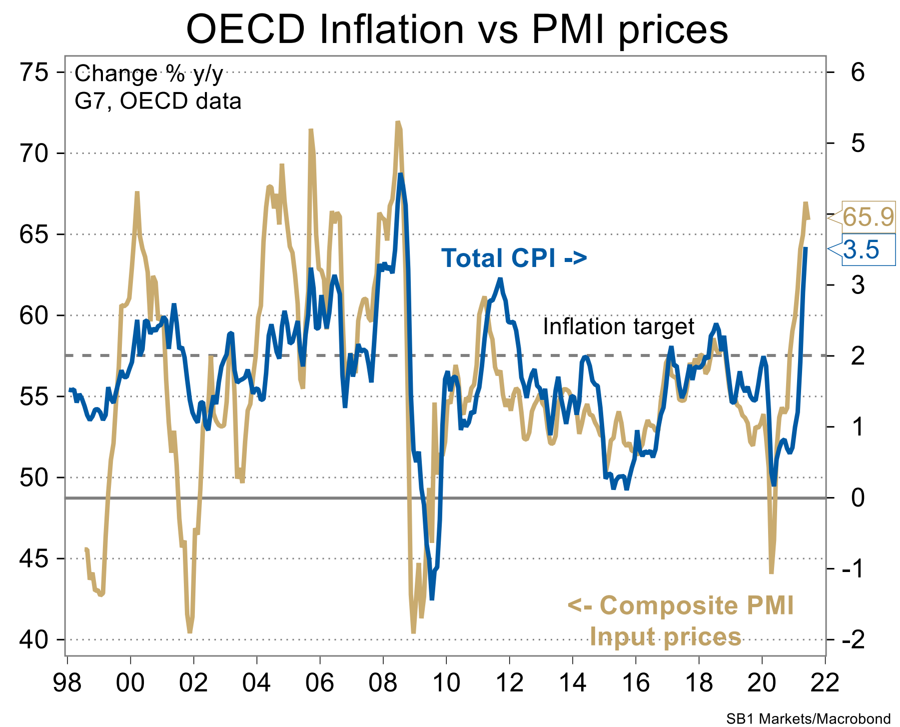
Businesses keep reporting rapid growth in input/output prices but a tad slower

Peak PMI price indices? Still, higher CPI inflation unavoidable, at least short term



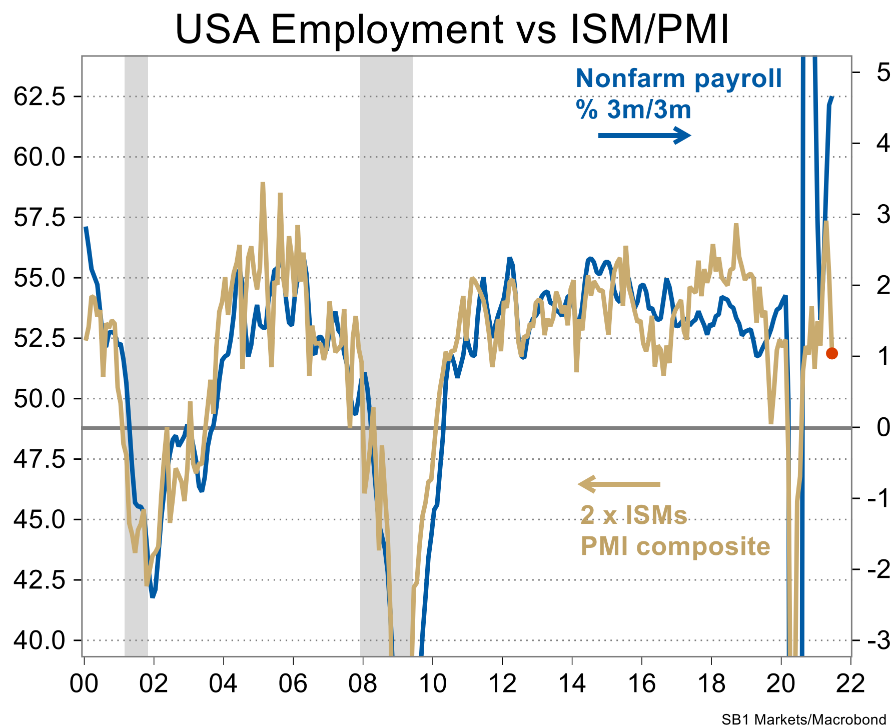




- **Both manufacturers and services** are reporting rapid increases in prices, both input & output prices
- The correlation to **actual CPI inflation** is not prefect, but the PMI price indices are signalling a lift in headline inflation, from 3.5% in rich countries in May
- The correlation to **core CPI** is far less impressive

PMI/ISM: The employment indices down, very likely due to lack of labour

Services are reporting a decline in employment – which is a 'catastrophe' today



- **Actual employment** growth surged in June – and far more than expected – and the past 3m/m employment is up at a 4.5% pace
- Now, **ISM services** are reporting a decline in employment, while **manufacturers** reported an increase in employment.
- The weighted average of PMI & ISM employment index is at an average level, signalling an average growth in employment which is far below what's needed, given the 4% – 5% shortfall in employment vs. the pre-pandemic level
- According to the **Markit PMI** survey, companies are reporting that they are struggling to find the right employees
- The respondents in the **ISM services** survey join in; several sector report lack of labour and one sector that wages are increasing in an unprecedented pace

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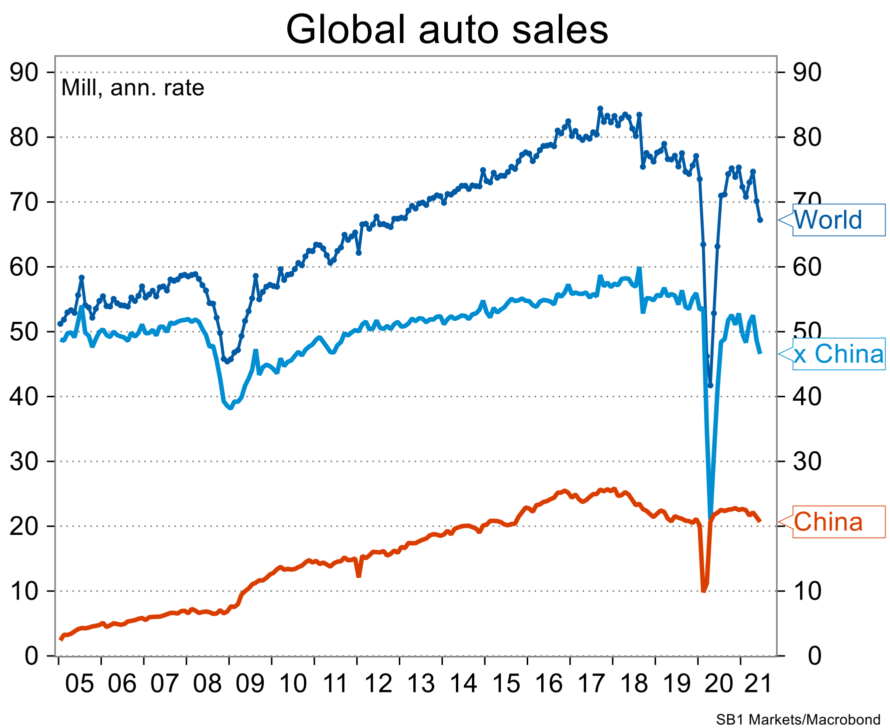
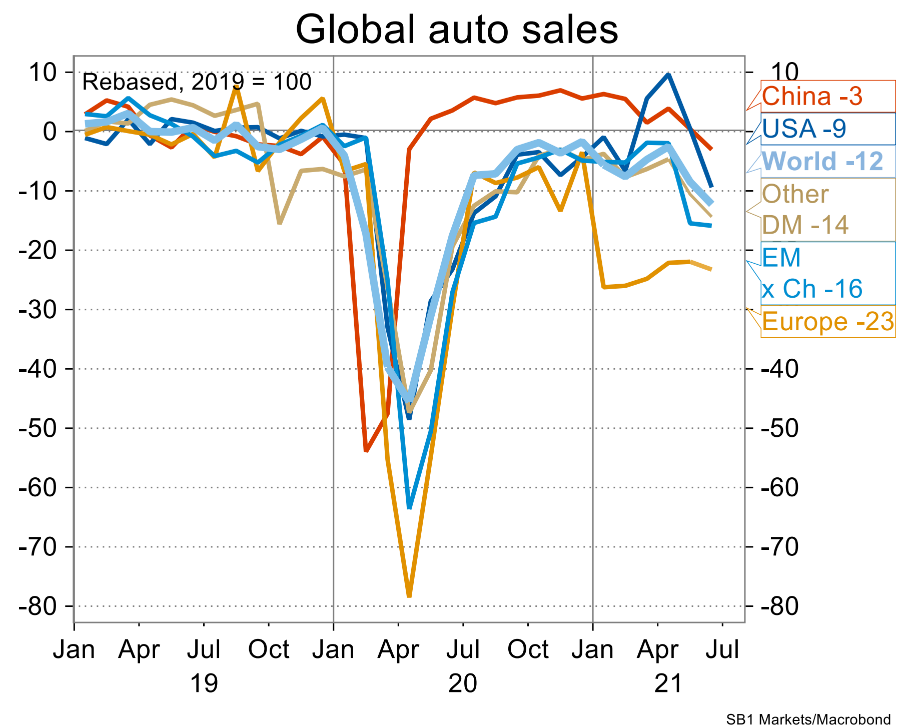
Auto sales down most places in June – global sales down 4%, -12% vs pre-Covid

Semiconductor shortages at least partly to blame for lower sales, but Covid also to blame directly

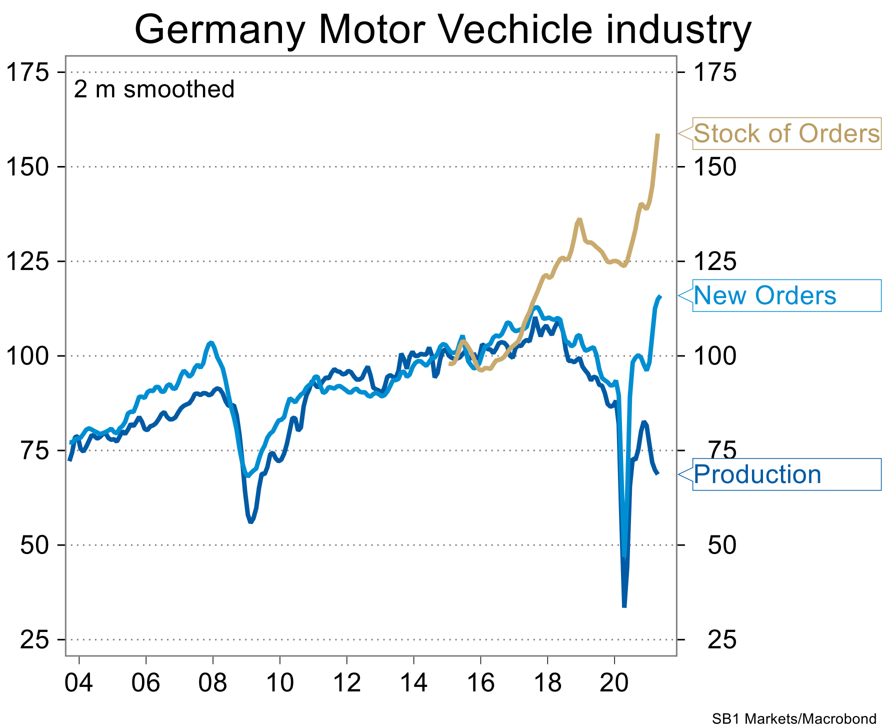


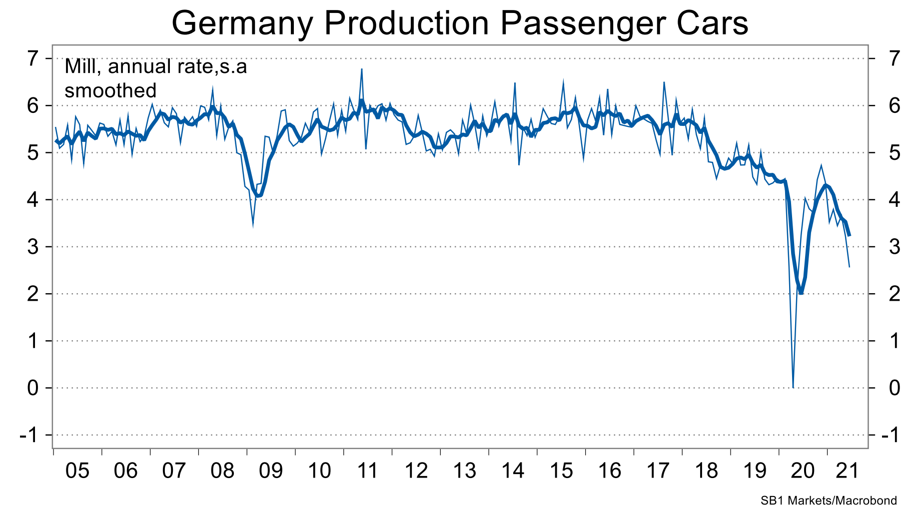


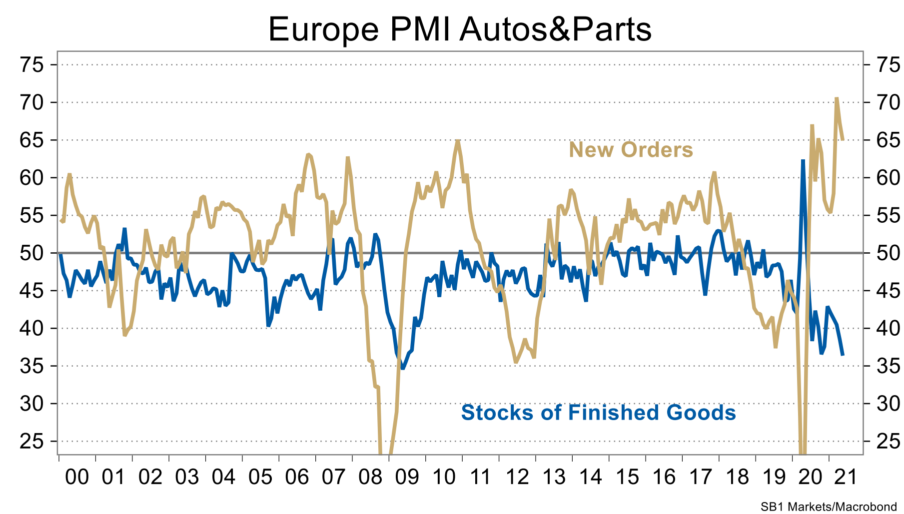
- Based on our preliminary estimate **global auto sales** fell by 4% in June. Sales are down 10% vs. the level in late '20 and 12% vs the pre-pandemic level. Both supply challenges (data chips) as well as weak demand due to the pandemic (in EMU, India) explains the downturn. We expect demand to pick up in both EMU and India the coming months. The lack of components may last for longer
- Sales fell all main regions, by the most in the **US**. Sales in the **Euro zone** fell marginally, and sales fell in UK as well
- Sales in **China** have been revised down by 3% - 5% and fell further in June, and are now below the pre-pandemic level, which was low
- Sales in **India** probably recovered somewhat in June but remains far below the April level, and sales fell in both **Russia** and **Brazil**

What's the problem? Seemingly, not demand…

Stock of orders are skyrocketing, production is nosediving. Seems to be a serious supply problem



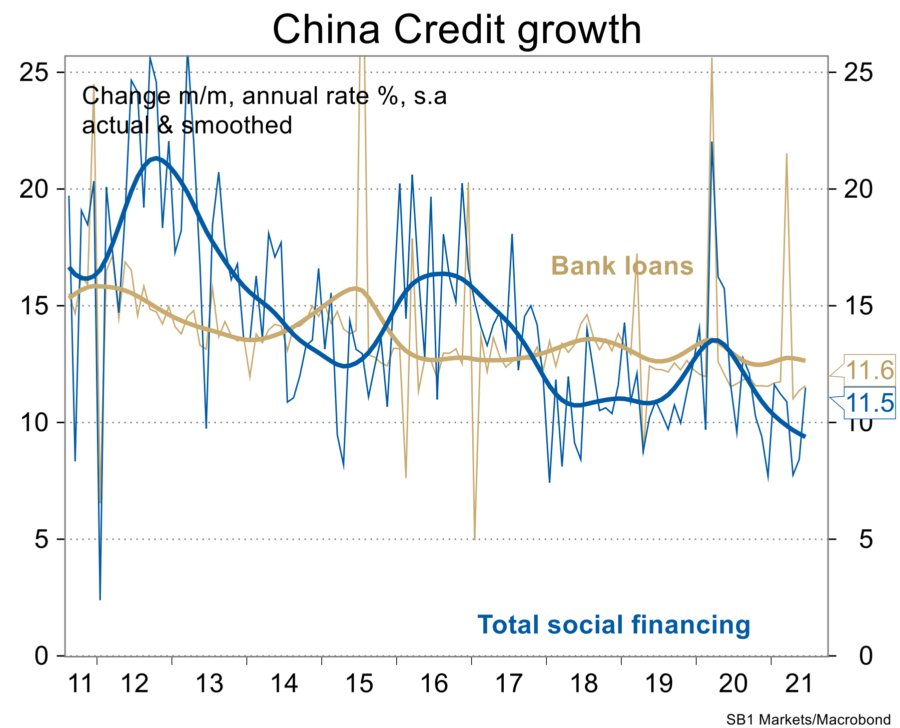




- The lockdown related 20% decline in auto sales in Europe the last months have not made a dent in orders or the order backlog, rather remarkable (both according to actual order data, and the European Auto PMI)
- Production of cars in June was down 45% (!!) from last November. The latter part of the decline in production is very likely due to lack of components, especially semiconductors

Credit growth accelerated in June, trend still probably down

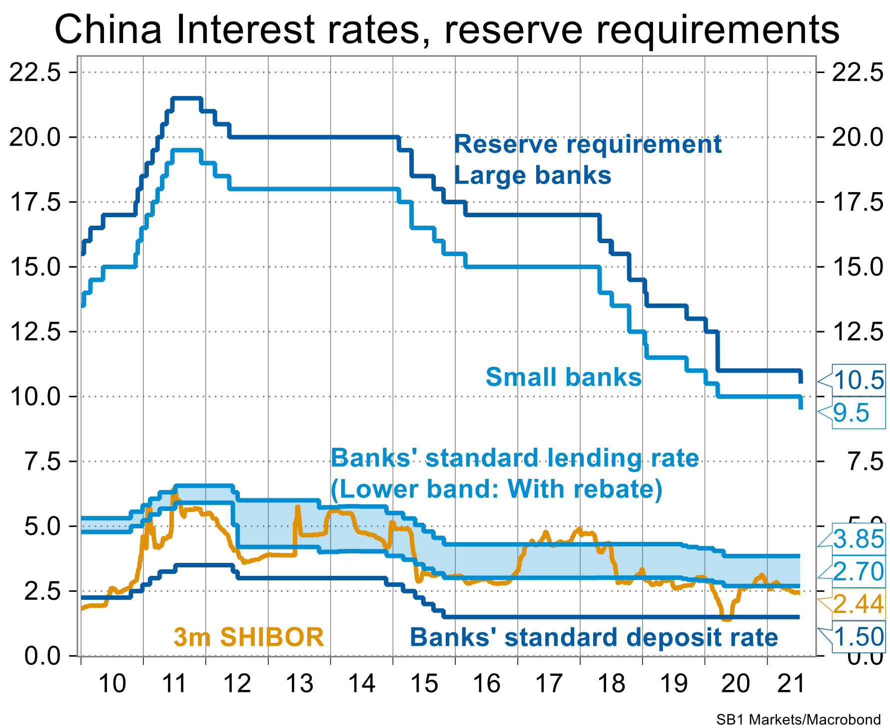
... but authorities are now changing tack, banks' reserve requirements cut!



- **Total credit** grew at an 11.5% rate in June (m/m, annualised), up from 8.2 % in May. Smoothed, the underlying rate may be 9% - 10%, down from 13% during last spring (and >15% during some months). A 9% - 10% growth rate is marginally above the trend growth in nominal GDP
  - » **Total credit** rose by RMB 3.5 trl, expected 2.7 trl (not seasonally adjusted, total social financing, including central & local government bond, and corporate equities). Seasonally adjusted the core total social credit (total ex central gov bonds & corporate equites) grew by 2.5 trl, up from 1.7 trl in May
  - » **Bank loans** rose by RMB 1.7 trl, seas adjusted. Bank loans are up 11.6% y/y
  - » **Shadow banking credit** was marginally up 0.8 trl in June, following much slower growth in May and April, and a decline in March. Underlying growth has still fallen sharply
- **The credit impulse has turned negative**, like it usually does every 4th year or so. The ramification may be felt in many markets
- **The slowdown has been by purpose**, as authorities have tightened, especially vs. credit supply outside banks. However, on Friday the PBoC cut banks' reserve requirements – the authorities may shift the foot to the accelerator again

The PBoC cut banks' reserve requirements, will stimulate bank lending!

Last Friday's 0.5 pp cut is the first since last spring, a too abrupt credit slowdown is not wanted

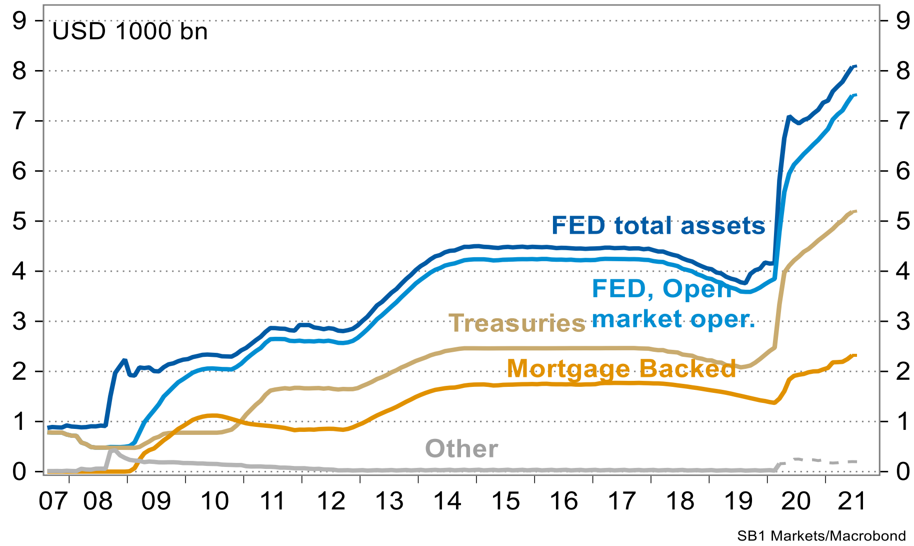


- The reserve requirement was cut by 0.5 pp to 10.5 for large banks and to 9.5% for smaller banks
- The cut will free up some RMB 1 trl in lending capacity in the banking system, equaling 3 weeks' growth in credit supply from banks, no more, no less
- Still, the measure signals that authorities do not want credit tightening to go too far, even if they at the same time are worried that credit grown too fast for too long, increasing the risk for financial instability. This change of tack is rather common in China – and many other countries

FOMC minutes: Sees progress towards target, but it’s not yet substantial

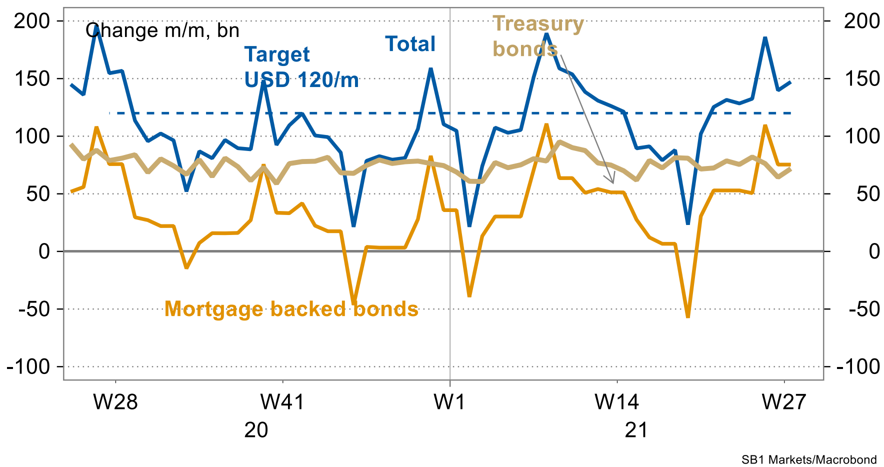
Tapering is coming closer but the essence lies in the development of the labour market

USA Federal Reserve balance

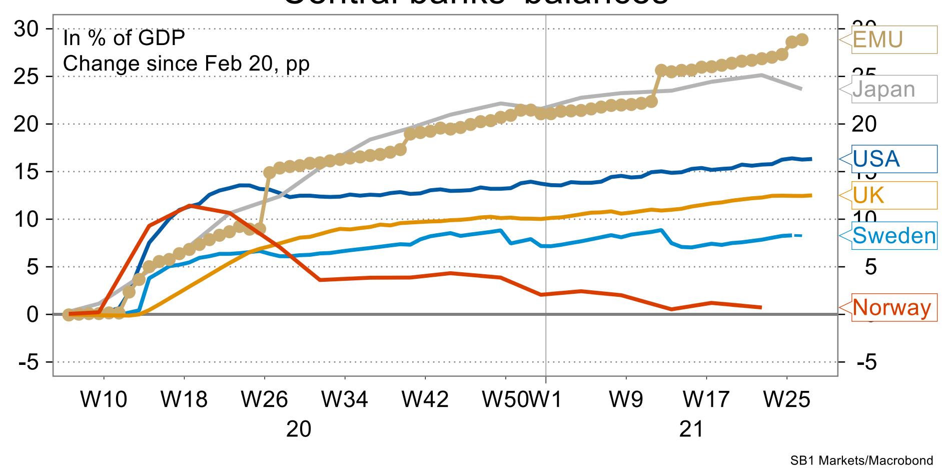


- The views among the FOMC members probably differed more than usual at the June meeting
- The minutes revealed that participants saw it as important to ‘be well positioned to reduce the pace of asset purchases in response to … faster-than-anticipated progress’.
- The minutes also stated that several participants saw benefits to reducing the pace of MBS (Mortgage backed) purchases as the housing market was booming
- At the press conference after the June meeting, Powell stressed that the bank would communicate an eventual tightening well on beforehand, and that the progress towards the bank’s target was not yet substantial

USA Fed Treasuries & MBS

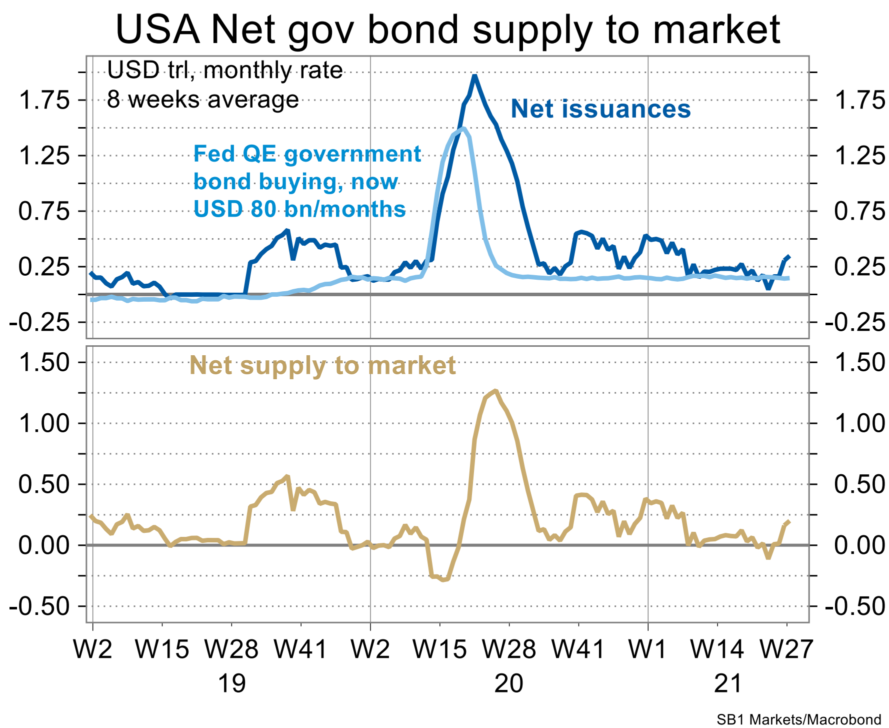


Central banks' balances



How much of the public debt is the Fed mopping up?

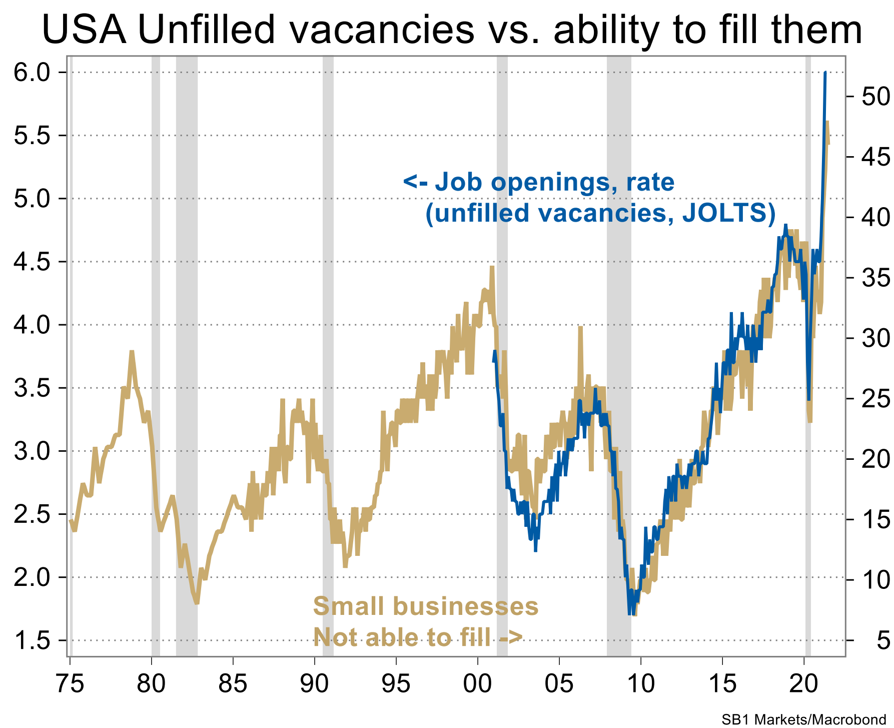
Quite a bit of it – and net extra supply has been close to zero for much of H1

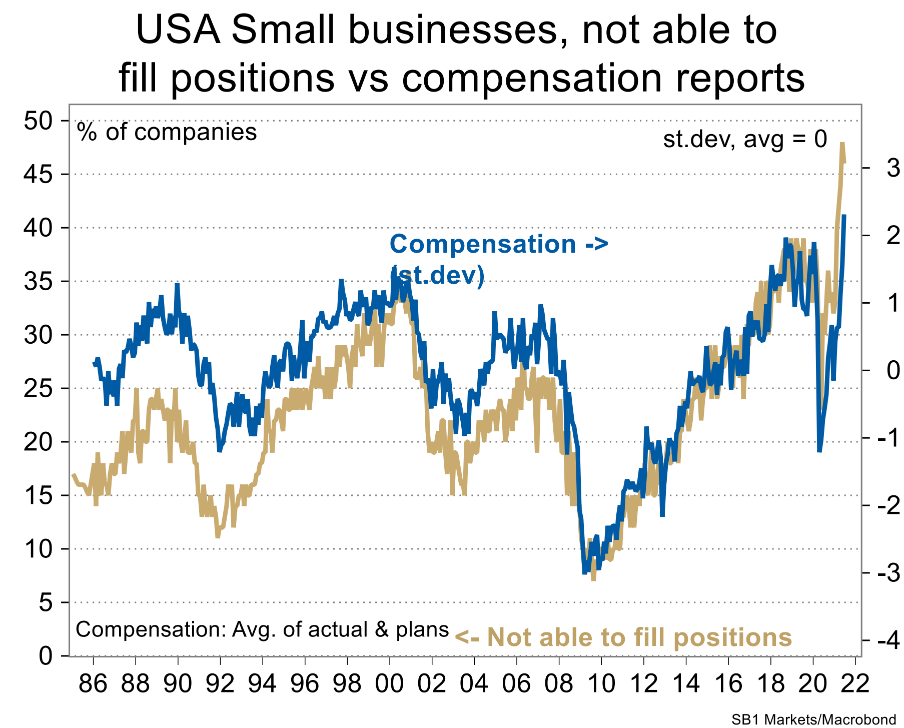


- In addition, the government have until now been transferring huge amounts of money to the private sector (=the budget deficit ☺), so far in 2021 at a pace of almost USD 0.3 trl per month, creating a similar extra savings surplus in the private sector (as the current account surplus is not that much larger)
- So, even if yields are low, there are money chasing these yields, which has been of rather limited supply

Official vacancy data confirm NFIB survey data (almost perfectly)

.. And we have never seen anything like this before. The correlation to wage inflation is <u>close</u>

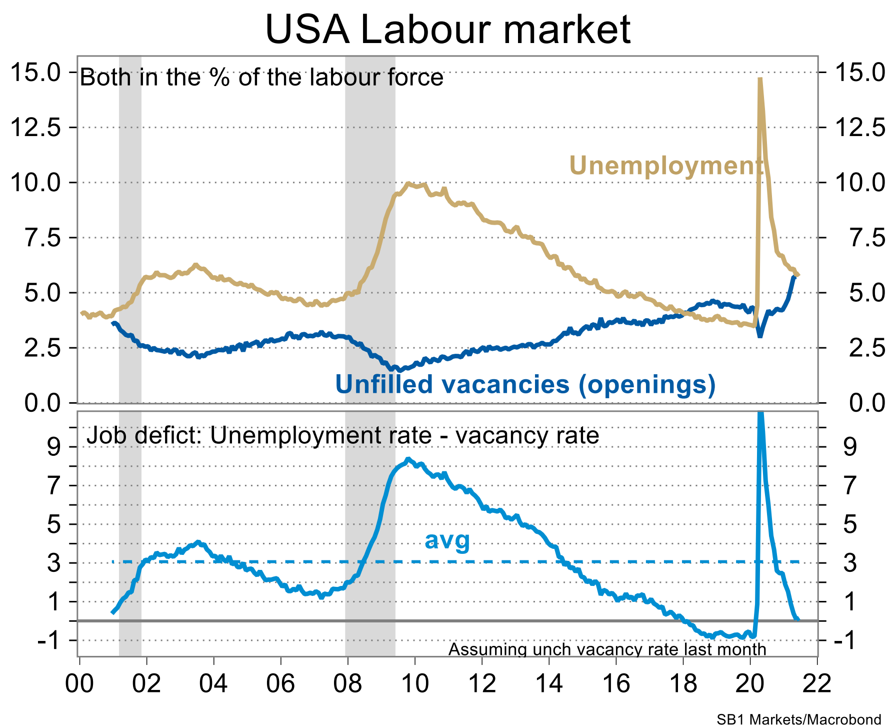


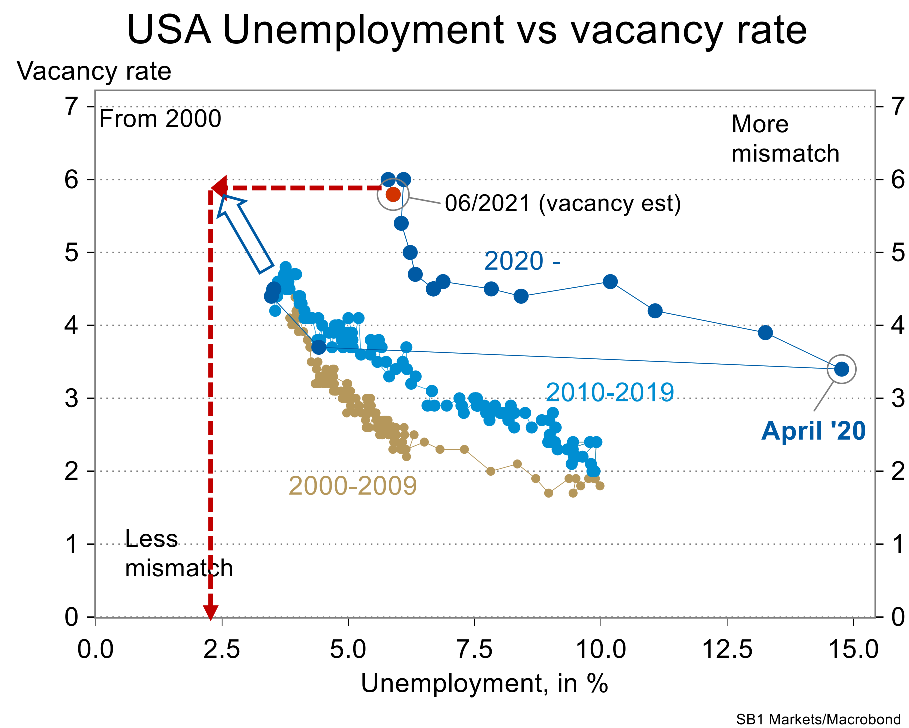


SpareBank 1 MARKETS

Such a high level of vacancies would normally signal a record low unempl. rate

… as if unemployment was below 3%. However it is still 5.9% - a huge shift in the 'Beverage' curve

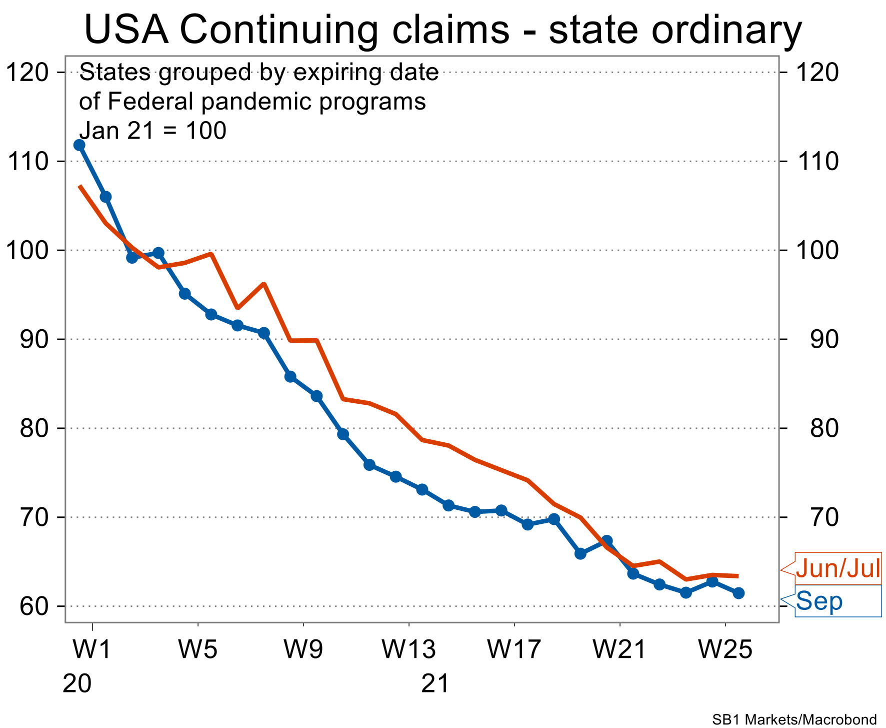




- **It is a permanent downward shift in labour supply** – a huge increase in mismatch in the labour market or that many workers now prefer to stay outside the labour market. If so, a 'disaster' – wage growth will accelerate sharply, inflation will be more than transitory & the Fed will have to respond. If the Fed does not respond, another disaster in the waiting, and a more abrupt and dramatic shift in policy will be needed at a later stage
- **Or it just at temporary sweet/sour spot:** 1% of the working age population can not work due to Covid-10 (school children, own health etc, they say) and another 3% – 4% are receiving extraordinary unemployment benefits, more than those that would normally have received such benefits. At least he latter group will have no income if they do not turn up in the labour market during the coming months, as these support programs will end now (in some states) or in September (everywhere)

Will the cancelling of pandemic federal benefit programs lift employment?

No clear message yet – but state data are volatile

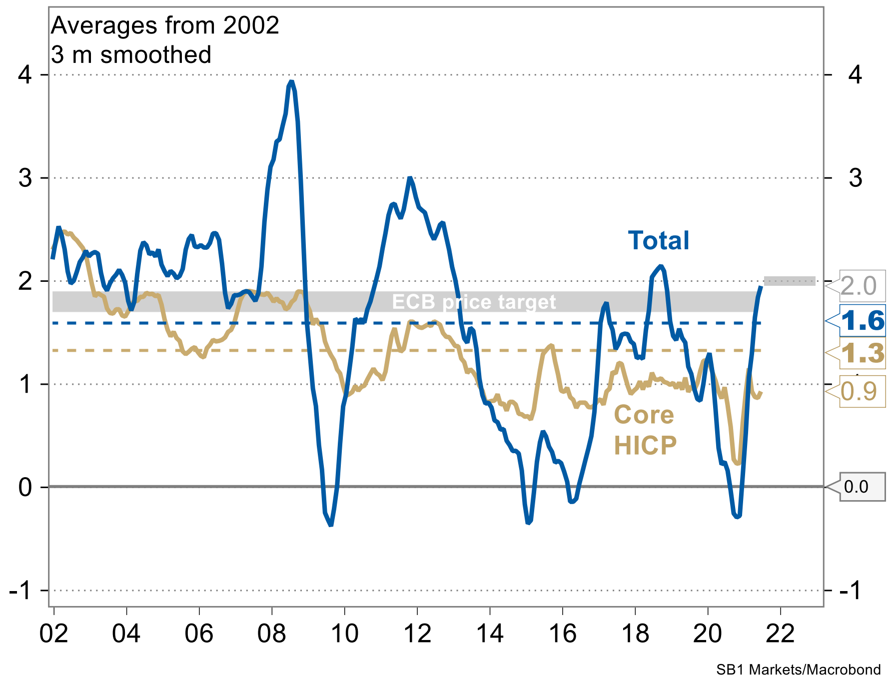


- 4 states dropped out of the federal unemployment benefit programs on June 12 (end of week 23), 8 states left June 19, and 10 states June 26 - which is the last week state unemployment benefit data are available
- We do not know what these former recipients do now – are they now trying to find a job?
- Some media reports suggest that employers in these states have been able to find more workers, but other reports have told other stories
- If we pool the 'early leavers' in one group, we have not yet seen a reduction in the no. of recipients of ordinary state benefits among these states
- Most likely, we will have to wait for state employment data, which are published 2 – 3 weeks after the national payrolls report
  - » We doubt we will find much information in the June state employment data (date are gathered mid-month), but July data (published in August) could reveal some information whether labour supply increases or not. We think the odds of finding some impact are pretty good, if not already in July employment data

ECB's new strategy: A 2% symmetric inflation target, clearly above the current

…but now includes house prices

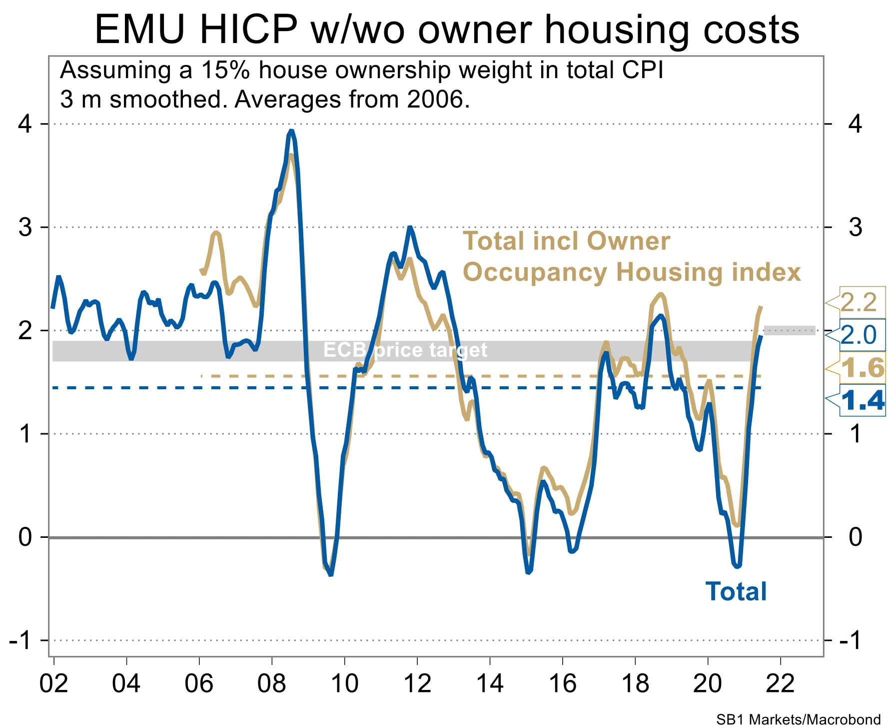
EMU HICP Total & Core



- **As has been widely communicated, the ECB lifted its inflation target** to <u>symmetric around 2%</u> from <u>'below but close to 2%'</u>, signalling somewhat larger tolerance for inflation (at least vs. the old Bundesbank line). A symmetric 2% has been the norm for most central banks.
  - » The Federal Reserve US has moved further to an average inflation target, but even the <u>ECB will tolerate transitory periods with inflation above 2% if needed to reduced the risk for entering a disinflationary trap</u>
- On the other hand (also well prewarned), the ECB will in one way or another **include owner-occupied housing costs** (OOH) in the targeted inflation measure. The ECB asks Eurostat to include a measure of the OOH in the HIPC (the EMU CPI). Until now, most of OOH has been excluded from the 'CPI' in EMU. It will probably take some time for Eurostat to implement this change (which is rather complicated). <u>However, the bank will start taking housing costs into account when assessing if the inflation target is met from now on</u> - see more next page
- The 3rd change: ECB will focus more on **implications of financial imbalances** rather than inflation implications of monetary developments as the latter has turned to be a complicated science. Again, a Bundesbank pillar is buried (perhaps just before the BuBa approach could be vindicated, at least in the US…)

ECBs preferred owner-occupied housing index does not change that much

… but inflation would have been 0.2 pp higher on average – and above the NEW target now

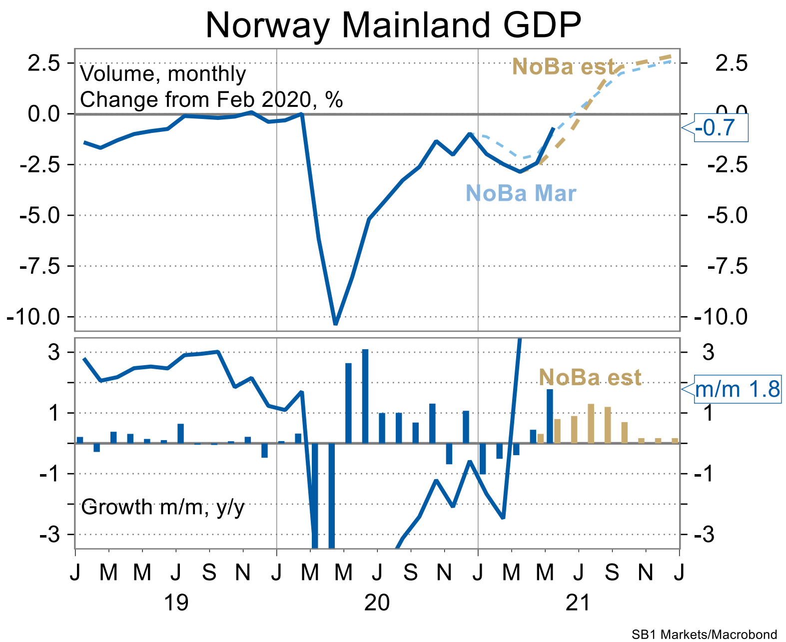


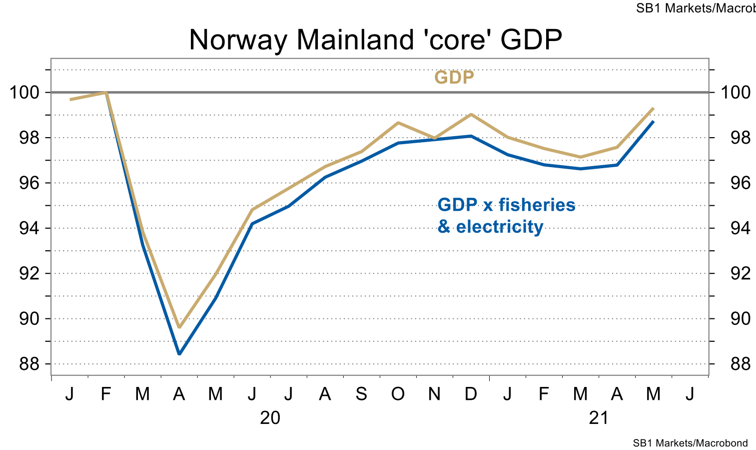
- On average, inclusion of the current Eurostat experimental quarterly total OOH, would have lifted average HICP by 0.2 pp per year the past 15 years – and now 'total' inflation to slightly above 2% vs the 'official' index at just below 2%. *See more next page*

- There are several alternatives for including owner-occupancy housing costs (OOH) in consumer price indices
  - » A **rental equivalent** is most common, as it is done in the US and Norway and several other countries, owners are assumed to pay (to themselves) the same rent as renters pay
  - » A **net acquisition approach** usually just include construction costs for new homes, and not the cost of land
  - » A **user cost approach**, where 2nd hand prices are the main element but where depreciation, real interest rates and expected capital gains are included are preferred by many economists. However, both a volatile real interest rate and an uncertain expected capital gains element complicates calculations (like if expected capital gains are high, the ownership cost is negative). A possibility is keeping capital gains out of the calculation, or assuming a stable relationship between (long term smoothed) real rates and expected real capital gains, implying the new and existing home prices
- The ECB has signalled that it prefers the net acquisition approach, implying that just new home construction costs (and not the cost of land) should be included in the index (alongside maintenance, renovation etc). The current Eurostat's experimental OOH index includes the cost of land (as far as we understand). However, some statements from ECB officials could be interpreted as if cost of land should be included, even 2nd hand house prices
- The Eurostat is assumed to spend some years figuring out how to include a OOH measure in the HICP (or construct an HICP-H index). In between time, the ECB will include some OOH-measures in the bank's assessment of price 'stability' - which may influence monetary policy, at least at the margin
- On average, we assume including OOH, measured by house prices, would have lifted average HICP by 0.2 – 0.3 pp per year the past 20 years – and now 'total' inflation is well above 2%. *See more next page*

Mainland GDP up 1.8% in May – and is just 0.7% below the Feb-20 level

… and 1.1% ahead of NoBa's 3 weeks' old forecast. Still much more to go in serviced

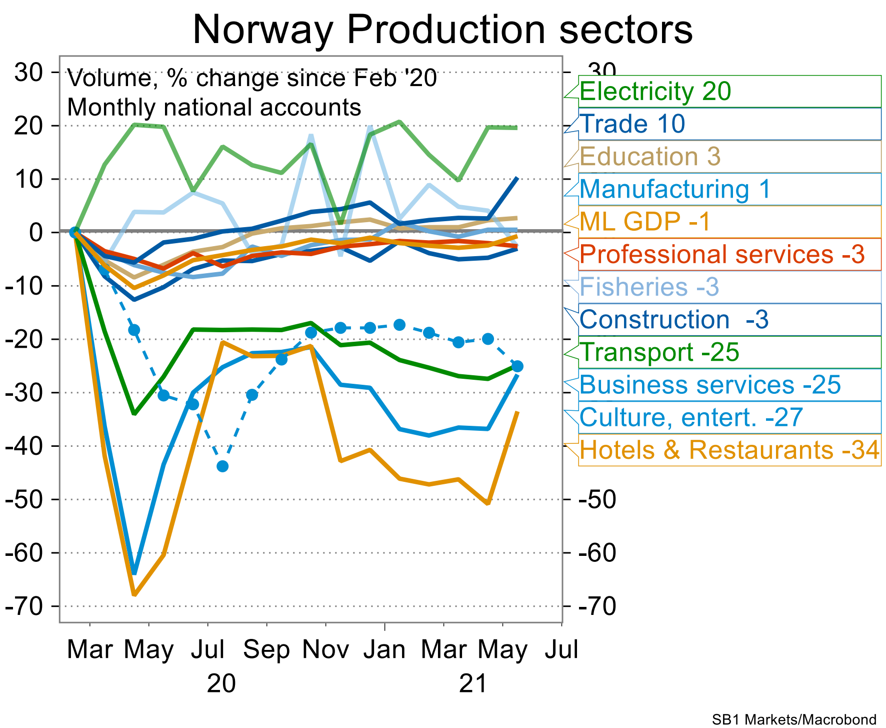


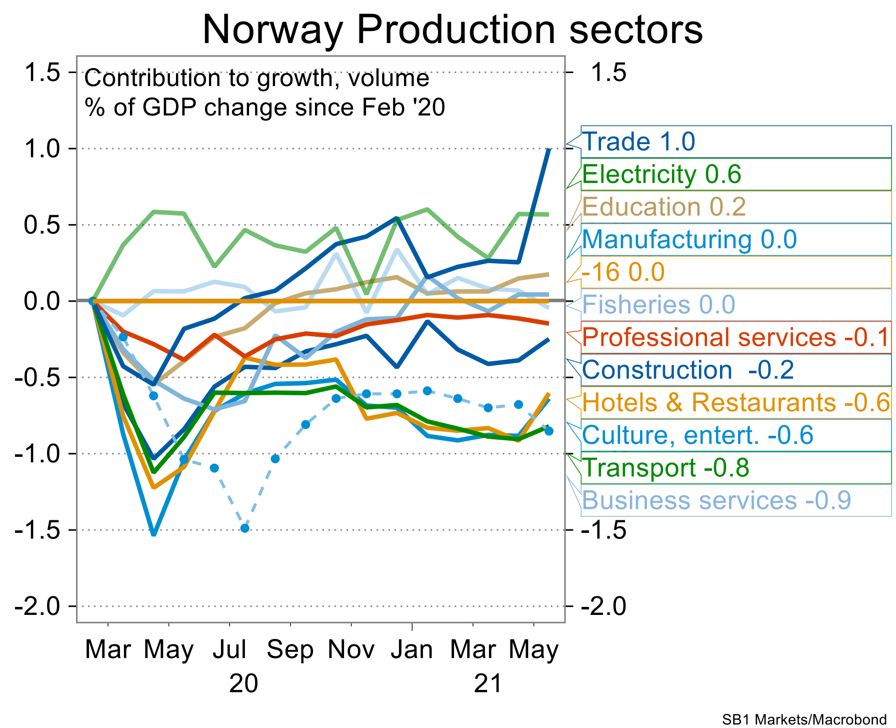


- **Mainland GDP grew by 1.8% m/m in May**, twice the consensus (and our) f'cast and 1 pp above NoBa f'cast. Growth in April at 0.4% was 0.1 pp higher than the first forecast. GDP is finally above the Dec-20 level, and just 0.7% below the Feb-20 level
  - » **Production:** Private services were up by 2.2% in May even business services reported a (strange) steep decline. Activity in hotels & restaurants rose by 35%. Trade up 10%, manufacturing flat
    - **Fisheries** down May, **and electricity** flat, 'core ML GDP' grew 2.0%
  - » **Demand:** Norwegians' spending at home shot up 4.6% in May, goods even more than services. Oil investments remained high in May, Mainland business investments fell further. Exports x travel rose 0.6%
- **Mainland GDP is down 0.7% vs the Feb-20 level**
  - » **GDP** was 1.1% above NoBa's f'cast
  - » **Production:** The 4 hard hit services are still far down, 25% – 34%. The total negative drag equals some 3% of Mainland GDP. Other sectors are up in sum flat, with trade, manufacturing & education in the lead. Construction is down 3%
  - » **Demand:** Norwegians' spending at home is unch. from Feb-20, goods +16%, services down 8%. Spending abroad has fallen by 97% (equalling 9% of disp. income), and the money is saved. Housing investments are up. Mainland business investments have fallen by 7%, while oil investments are up 5%! Exports ex petroleum (and tourism) are 3% below the Feb-20 level. Foreigners are not spending anything in Norway, a cut equalling 1.5% of Mainland GDP

Production details: Business services further down in May, must turn up soon?

Hotels/restaurants +35%, culture/entertainment +16%, still 30% below par. Transport still down 25%





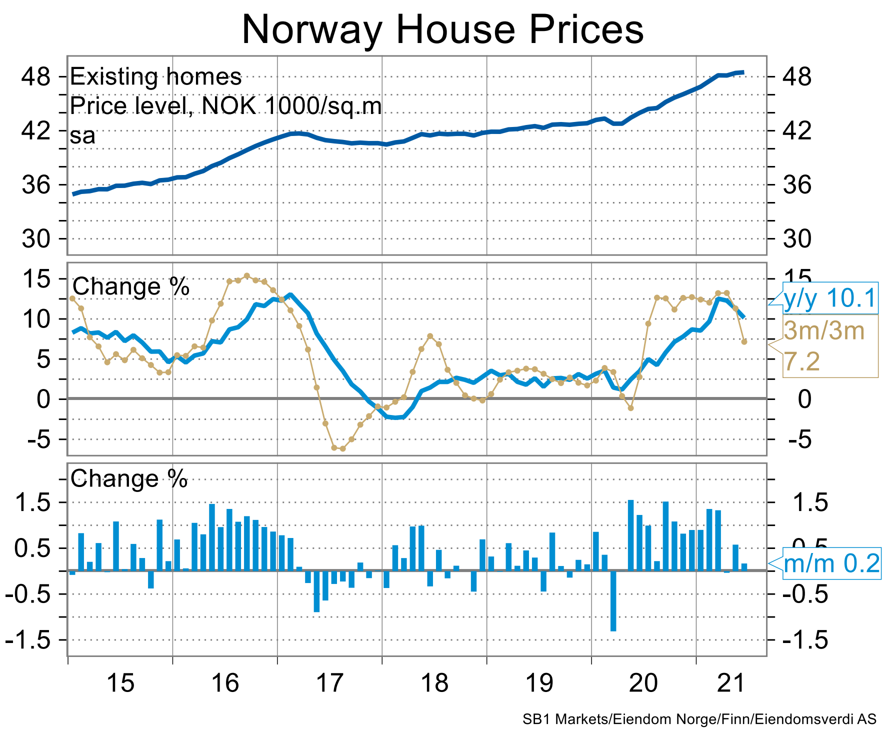
- **Business services** fell by more than 5% in May. We assume these activities will increase sharply the coming months
- **Hotels & restaurants, culture,** and **transport** all have miles to go before activity is normalised
- **Trade** reported a 7.5% lift in May, more than we assumed – but the level was strangely weak the previous months
- **Fisheries & aquaculture** contracted in May

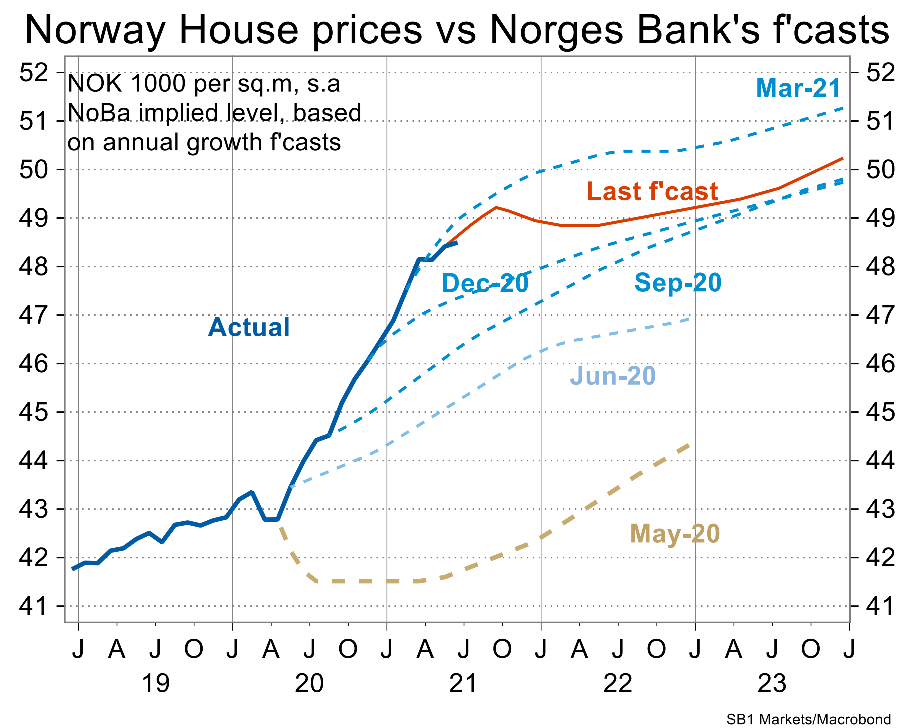
Business services: Temp services, travel agencies, call centres, congresses, cleaning, canteens, property services, leasing

SpareBank 1 MARKETS

House prices are slowing, just up 0.2% in June – NoBa expected 0.45%, we 0.6%

The impact of last year's lower rates are fading. And now something else will turn up…

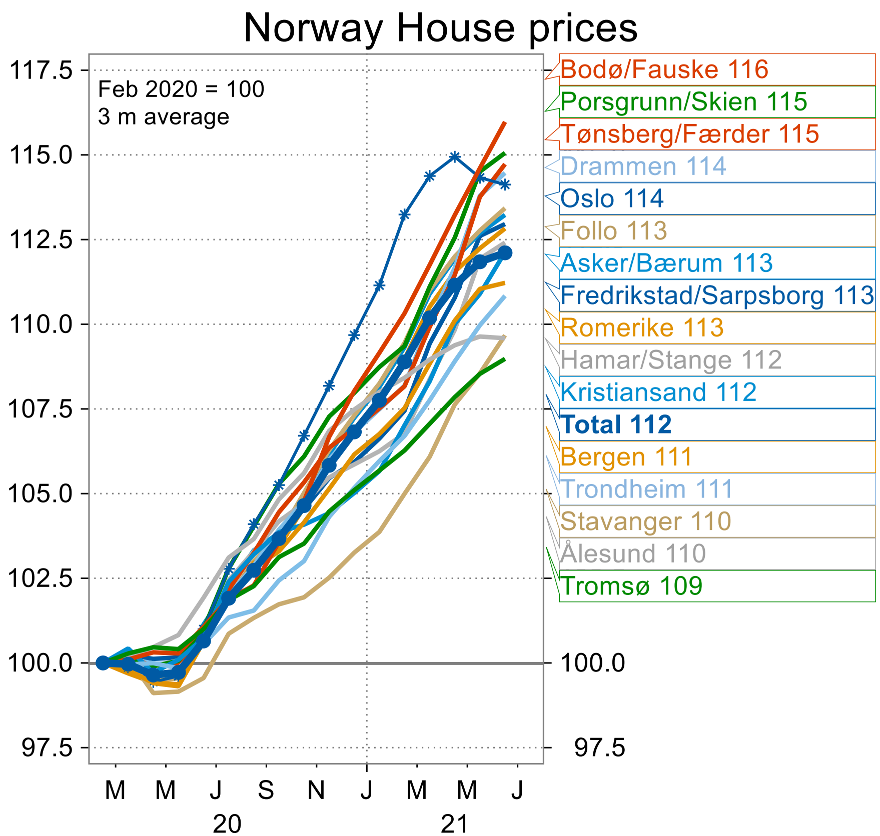




- **House prices** rose by 0.2% seas. adj in June, down from 0.6% in May. We expected 0.6%, NoBa 0.45% . Prices are up by 7% 3m/3m (annualised), down from above 10% . Prices are still up 10.1% y/y
- **Oslo** prices rose marginally in June, following 3 m months decline. Mixed in other towns, mostly a reversal of last months changes. Since before the pandemic, Bodø in the lead, followed by Porsgrunn/Skien, Tønsberg & Drammen. At the bottom: Berge, Tr.heim, Stavanger, Ålesund & Tromsø
- The **number of transactions** fell slightly in May but is high. The **inventory of unsold homes** fell further to a record low level
- Our Norway x Oslo **flow based price model** signals 1% m/m price growth, the Oslo model zero growth
- House prices are once again below NoBa's f'cast. The impact for last year's interest rate cut is fading, and soon rates will start to increase

Through the pandemic: Bodø, Porsgrunn/Skien, Tønsberg in the lead

Drammen is ahead of Oslo too – but too early to conclude that the capital will be deserted?



SB1 Markets/Eiendom Norge/Finn/Eiendomsverdi AS

Norway House prices

% change from Feb 2020

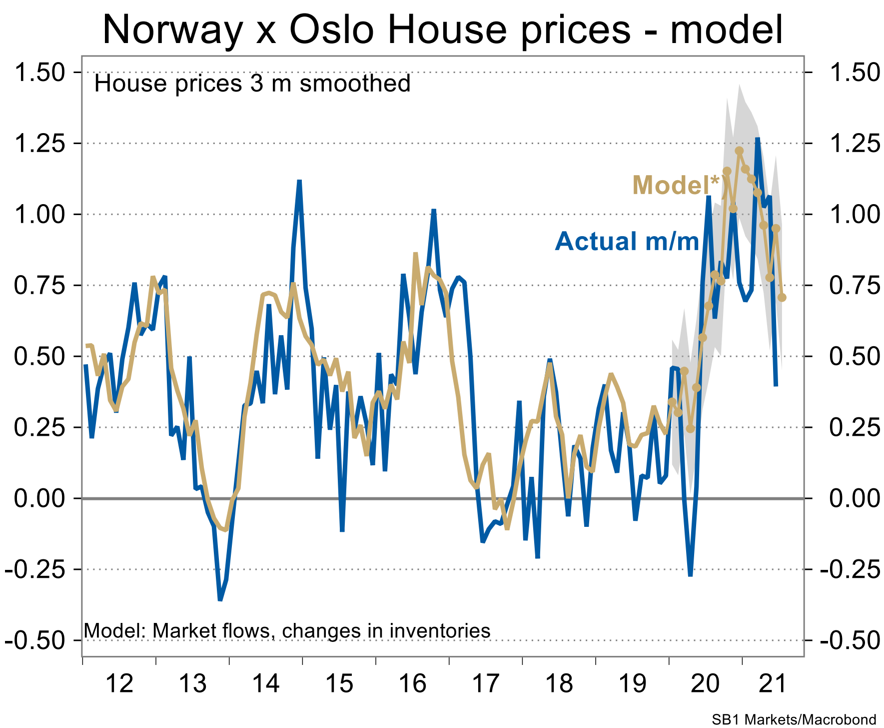
	% change
Bodø m/Fauske	16
Porsgrunn/Skien	15
Tønsberg m/Færder	15
Drammen	14
Oslo	14
Follo	13
Asker/Bærum	13
Fredrikstad/Sarpsborg	13
Romerike	13
Hamar m/Stange	12
Kristiansand	12
Total	12
Bergen	11
Trondheim	11
Stavanger m/omegn	10
Ålesund m/omegn	10
Tromsø	9

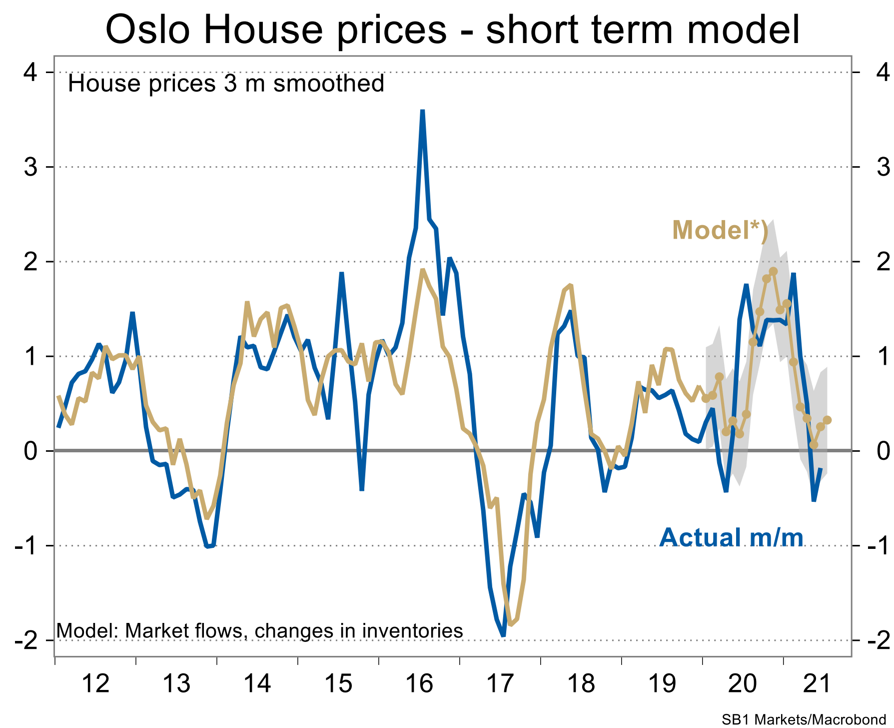
SB1 Markets/Macrobond

- Costal cities from Kristiansand to Tromsø (ex Bodø) at the bottom of the list

Short term market flows suggest continued price growth – outside Oslo

… and no further decline in Oslo

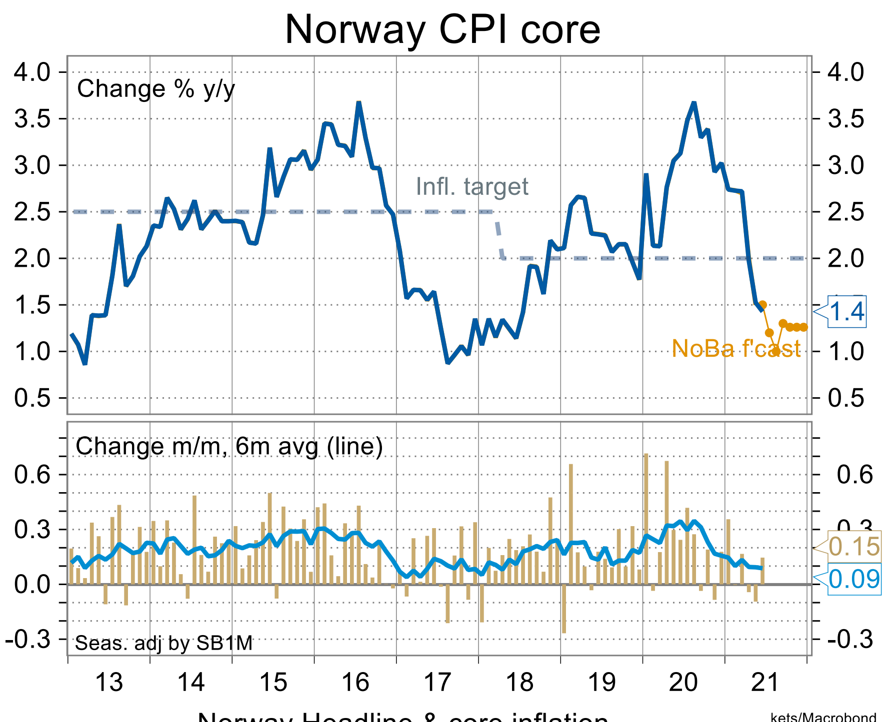


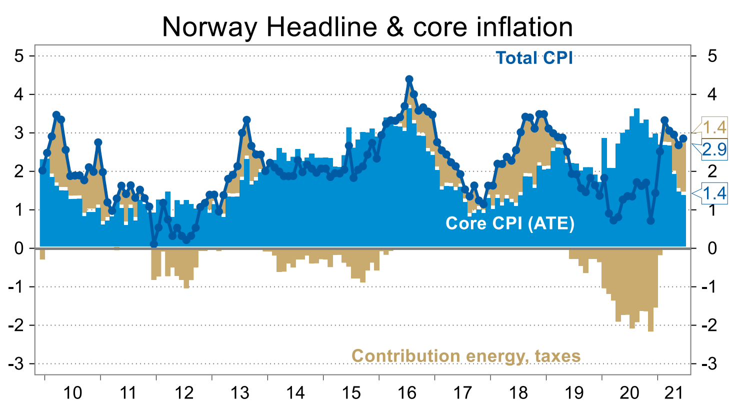


- Our **national x Oslo model** based on flows and the inventory signals a 0.75% growth in house prices per month (from above 1% some months ago)
- Our **Oslo model** signals marginal price growth (from zero 2 months ago)
- *These models are not long term price models, just short term price models based on flows of (existing) houses approved for sale actual sales & changes in inventories*

Inflation is not on the way up everywhere: CPI-ATE down 0.1 pp to 1.4% y/y!

… And now due do domestic goods & services, not cheaper imports

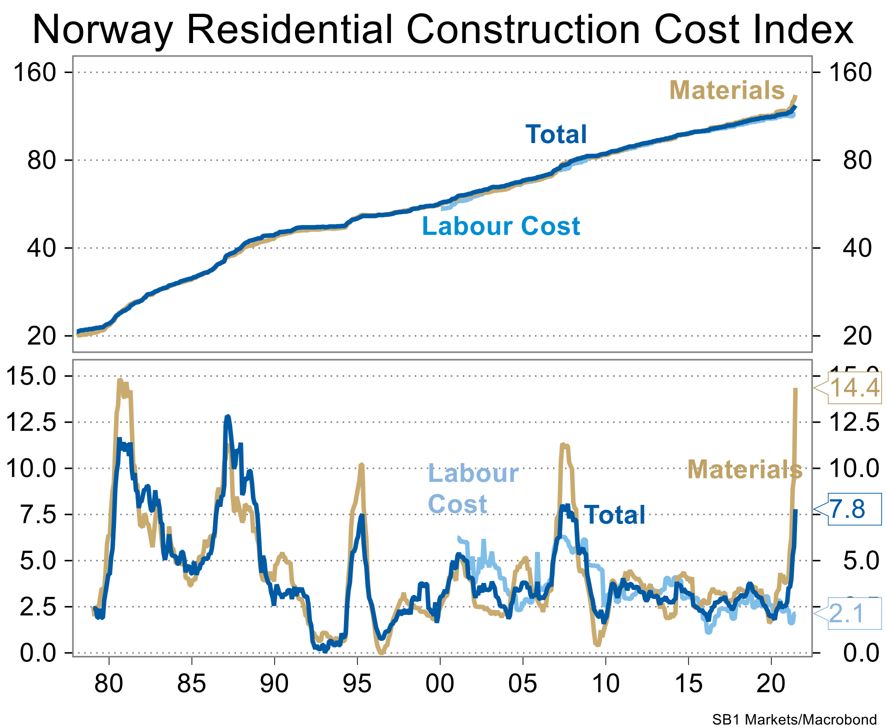


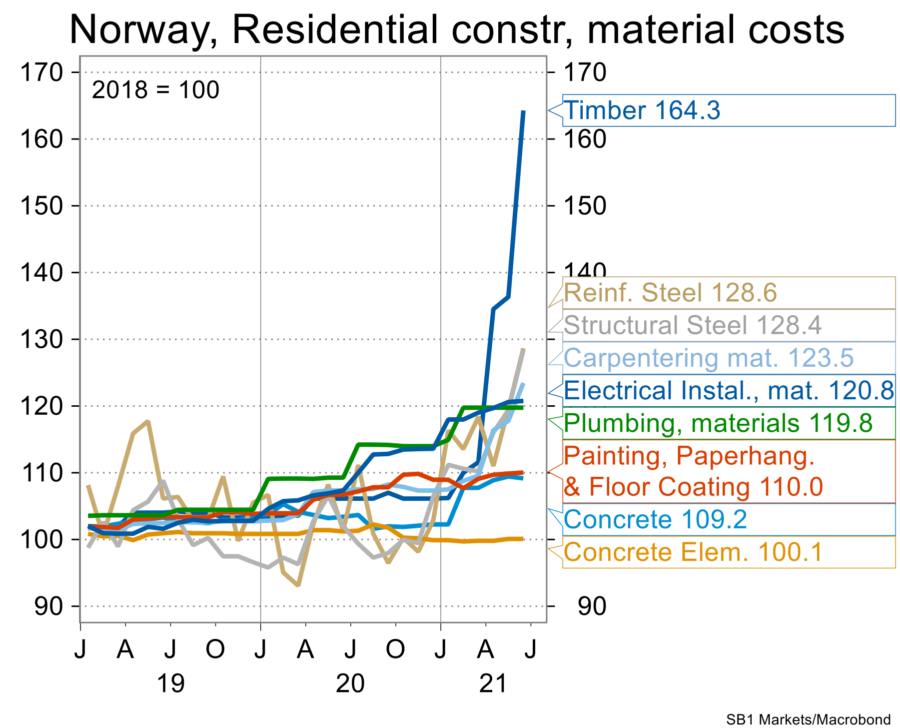


- **CPI-ATE** (ex. energy and taxes) inflation was down 0.1 pp to 1.4% in May; 0.1 pp below Norges Bank's & consensus f'cast, 0.2 pp below our estimate
  - » Prices were up 0.1% m/m (seas adj), up from -0.1% in April
  - » Inflation is below 2% for housing, clothing, food, alcohol, communication, transportation, and airline tickets – others are still above
  - » The main misses (vs our f'cast) on the downside were food and airline tickets, where furniture surprised at the upside
  - » Prices on imported goods rose in June, but annual inflation is trending down, following the strengthening of the NOK
  - » In addition, domestic inflation has slowed substantially to 1.4%
- **Total inflation** accelerated 0.2 pp to 2.9% as we expected
- **The outlook**
  - » **Inflation may slow** somewhat more the coming quarters. NOK has strengthened and wage inflation remains moderate (if not low). Demand for goods will have to decline from a very high level. Upside risk: Higher raw material prices/global price pressures but the spillover to the Norwegian CPI is not that significant
  - » Anyway, CPI inflation will not have any material impact on Norges Bank's monetary policy the coming months. It's all about the post Covid-19 recovery – and the housing market

‘Some’ cost pressure in the Norwegian construction sector too

But ‘just’ from some materials; lumber & steel, plumbing & electrical materials

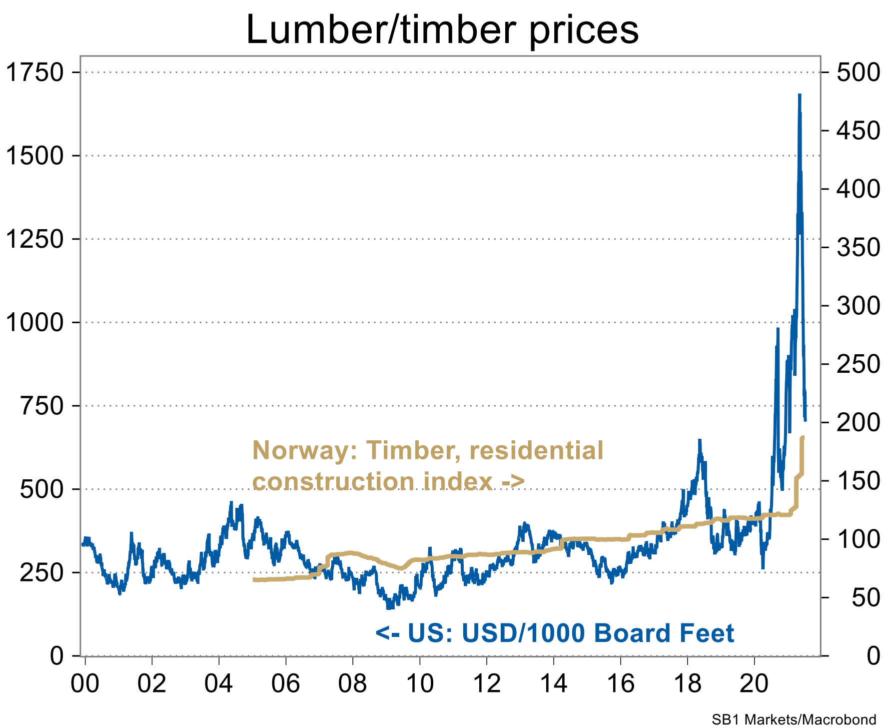




- Material prices are up ~~9.5~~ 14.4% in ~~May~~ June
  - » The 50%+ lift in lumber/timber prices over the past months is unprecedented
- Including labour costs, the total building cost index is up by 7.8%, the highest in almost 15 years

In the US, the lumber bubble has burst – if not totally (yet)

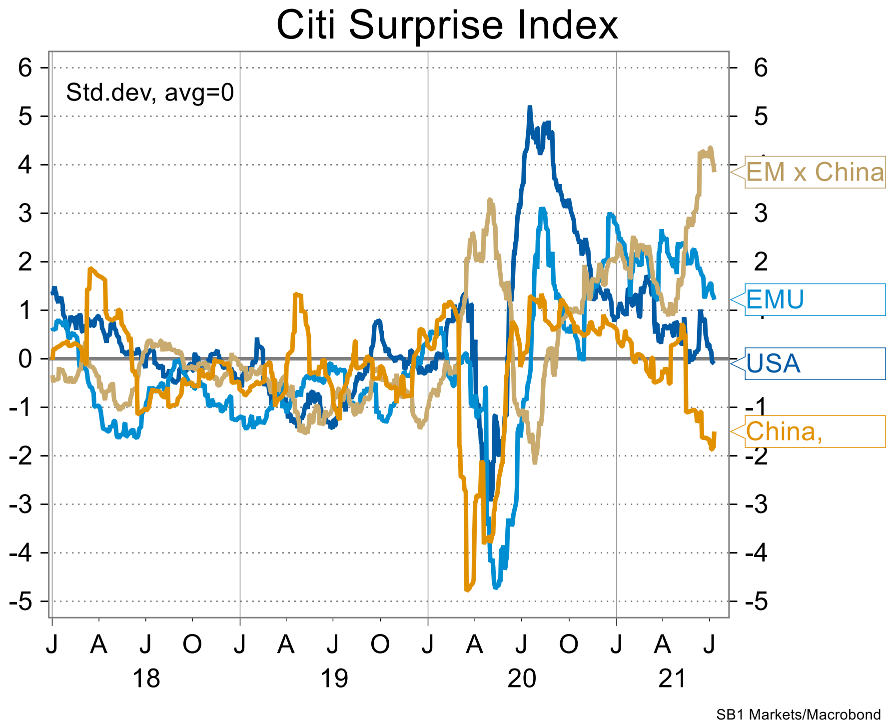
Raw material price cycles are normally not long lasting

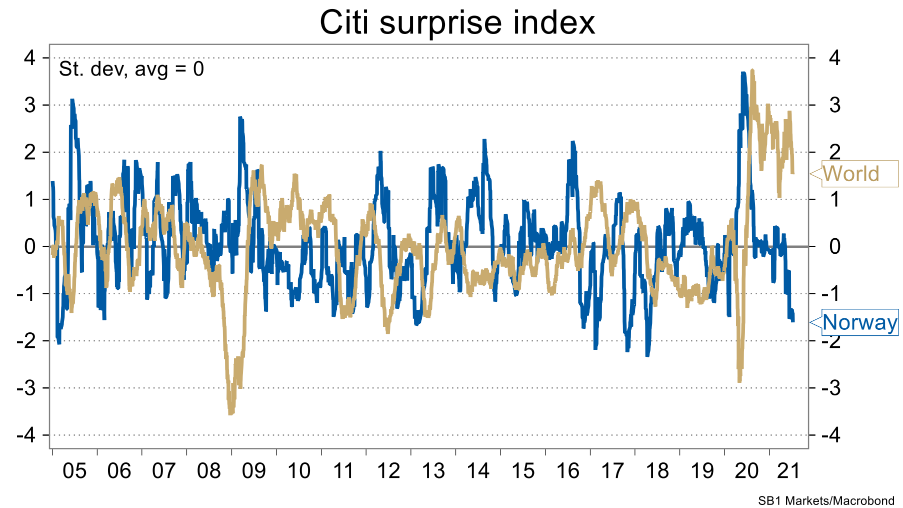


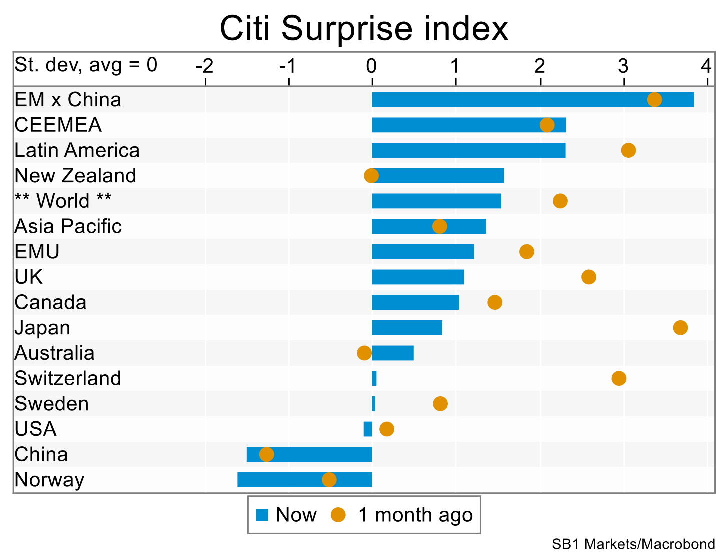
- .. And are not important for serious inflation cylces

Global surprises still on the upside but many countries are heading down

… according to Citi's surprise index. The US in negative territory last week







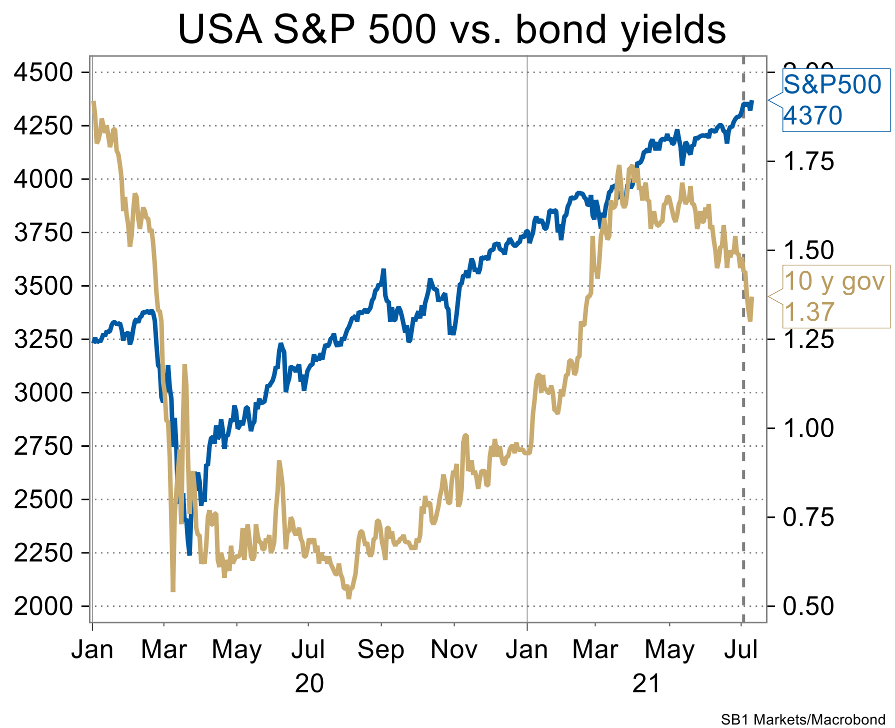
- **China** slides down, to well below neutral, alongside a credit tightening
- Japan has lost substantial height the past month
- **Emerging Markets x China** are reporting <u>much better</u> data than expected, and it is rather extreme (>4 st.dev above avg.)
- The **EMU** is still surprising on the upside, but less so
- The **US** surprise index fell marginally do below average last week
- **Norway** has surprised sharply on the downside recent weeks

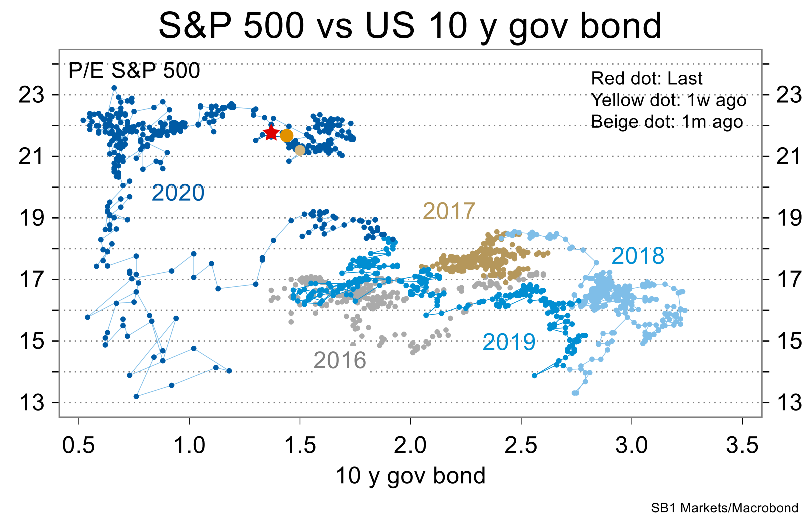
Surprise-indices measure the difference between economists' expectations and the actual outcome over a 3 month rolling window

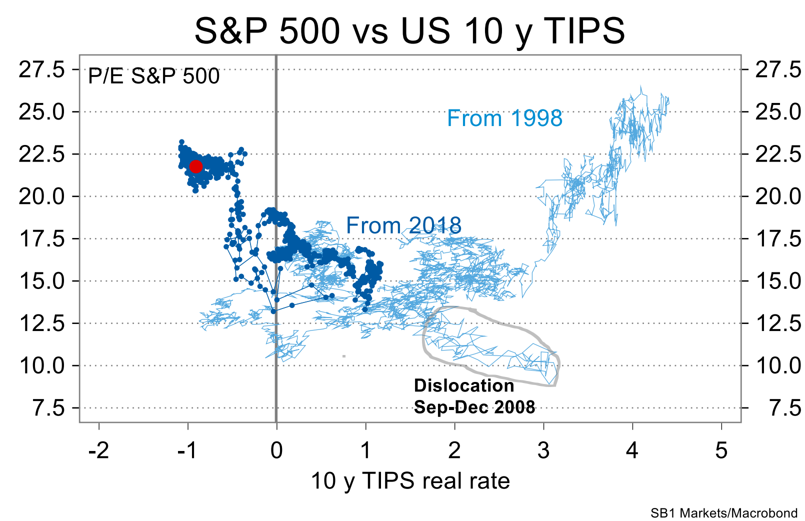
SpareBank 1 MARKETS

S&P 500 +0.4% to another ATH, the 10 y bond yield -7 bps, to 1.37%

… even if yields rose on Friday







The Calendar: China June/Q2 data, US CPI & retail sales, manufacturing

Time	Count.	Indicator	Period	Forecast	Prior
Monday July 12					
Tuesday July 13					
	CH	Trade Balance	Jun	$44.4b	$45.5b
	CH	**Exports YoY**	**Jun**	**22.0%**	**27.9%**
	CH	**Imports YoY**	**Jun**	**30.0%**	**51.1%**
12:00	US	NFIB Small Business Optimism	Jun		99.6
14:30	US	CPI MoM	Jun	0.5%	0.6%
14:30	**US**	**CPI Ex Food and Energy MoM**	**Jun**	**0.4%**	**0.7%**
14:30	US	CPI YoY	Jun	4.9%	5.0%
14:30	**US**	**CPI Ex Food and Energy YoY**	**Jun**	**4.0%**	**3.8%**
20:00	US	Monthly Budget Statement	Jun		-$132b
Wednesday July 14					
08:00	UK	CPI Core YoY	Jun	2.0%	2.0%
09:30	SW	CPIF Excl. Energy YoY	Jun	0.9%	1.2%
11:00	EC	Industrial Production SA MoM	May	-0.20%	0.8%
14:30	US	PPI Ex Food, Energy, Trade MoM	Jun	0.50%	0.7%
20:00	**US**	**Federal Reserve Beige Book**			
Thursday July 15					
03:30	CH	New Home Prices MoM	Jun		0.5%
04:00	**CH**	**GDP SA QoQ**	**2Q**	**1.3%**	**0.6%**
04:00	CH	GDP YoY	2Q	8.0%	18.3%
04:00	**CH**	**Retail Sales YoY**	**Jun**	**10.9%**	**12.4%**
04:00	CH	Fixed Asset Investments	Jun	12.5%	15.4%
04:00	**CH**	**Industrial Production YoY**	**Jun**	**8.0%**	**8.8%**
14:30	US	Empire Manufacturing	Jul	18.7	17.4
14:30	US	Philadelphia Fed Business	Jul	27.0	30.7
14:30	US	Import Price Index ex Petroleum	Jun		0.9%
14:30	US	Initial Jobless Claims	Jul-10	350k	373k
15:15	**US**	**Manufacturing (SIC) Production**	**Jun**	**0.6%**	**0.9%**
Friday July 16					
11:00	EC	Trade Balance SA	May	8.0b	9.4b
11:00	EC	CPI YoY	Jun F	1.9%	2.0%
11:00	EC	CPI Core YoY	Jun F	0.9%	0.9%
14:30	**US**	**Retail Sales Ex Auto MoM**	**Jun**	**0.4%**	**-0.7%**
14:30	**US**	**Retail Sales Control Group**	**Jun**	**0.5%**	**-0.7%**
16:00	US	Business Inventories	May	0.4%	-0.2%
16:00	US	U. of Mich. Sentiment	Jul P	86.5	85.5

- **China**
  - **GDP growth** is expected to remain low in Q2, at a 5.3% pace (expectations have varied, one survey reports 4%), still up from the lacklustre 2.5% pace in Q1, where travel restrictions during the Lunar New Year holidays dampened activity. Monthly data through May have signalled slower growth, and surveys are signalling some cooling of growth, at least partly due to a credit policy tightening (that now may be reversed). So far, **industrial production** has kept up well, but both **retail sales & investments** have slowed. **Exports** may have softened somewhat too
- **USA**
  - We 'know' we will see annual **CPI growth** rates not seen in decades at Tuesday, even if prices rose a at normal pace (core) or twice a normal pace (headline) m/m in June last year. However, whatever print, markets will probably retell the 'transitory' story, which can weather ugly figures for still a while. **Producer prices** will not look pretty either
  - **Retail sales** have fallen past two months but the level is sky high – and a further decline is very likely, at least over time, when spending on services will increase
  - **Manufacturing production** rose sharply in May but is still just back to the pre-pandemic level (even in consumption of goods is 13 % above). The first July **manufacturing surveys** will be reported on Thursday
- **EMU**
  - **Industrial production** probably fell slightly in May, dragged down by minor setbacks in both Germany, France and Italy – while Spain has reported higher growth
- **Sweden**
  - **Core CPI inflation** remains well below Riksbank's 2% target, at 1.2% y/y
- **Norway**
  - **No releases announced**

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

Highlights

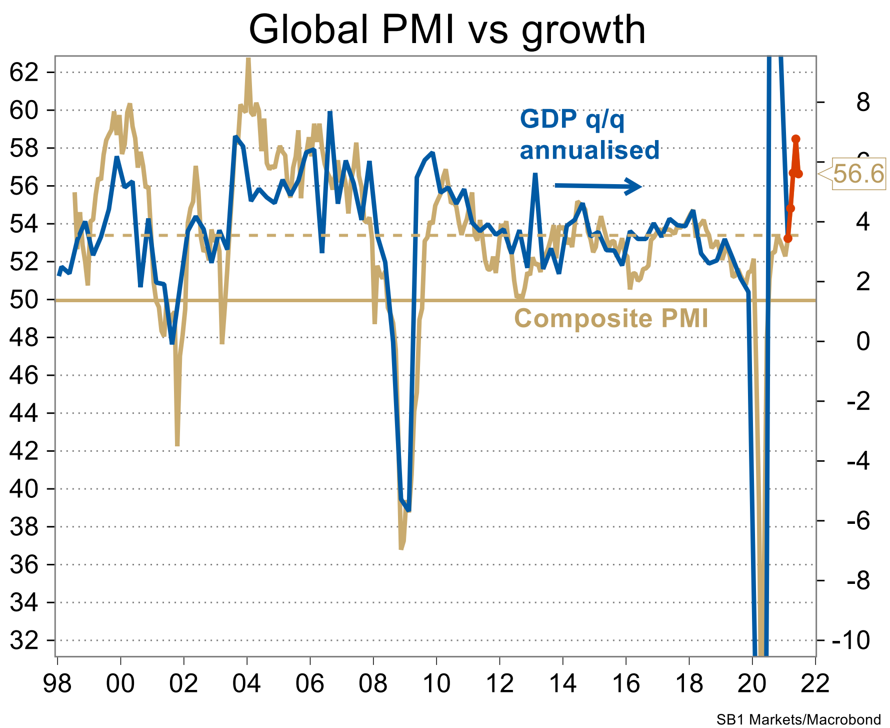
The world around us

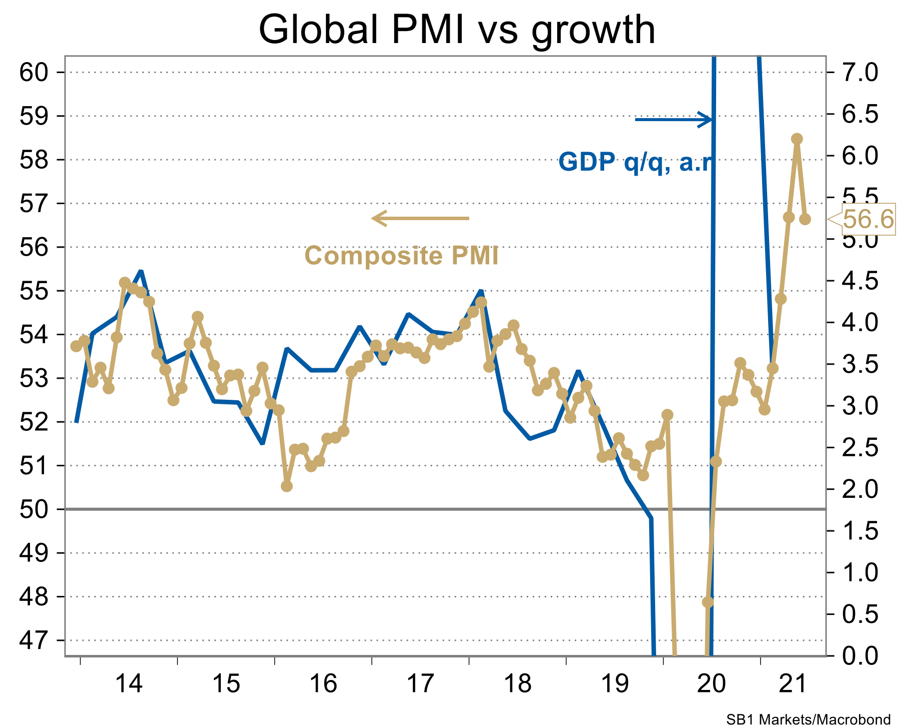
The Norwegian economy

Market charts & comments

Peak PMI: The global composite PMI down in June, still signalling 5% - 6% growth

As we assumed after the weak Chinese report, the global index lost 1.8 p to 56.6



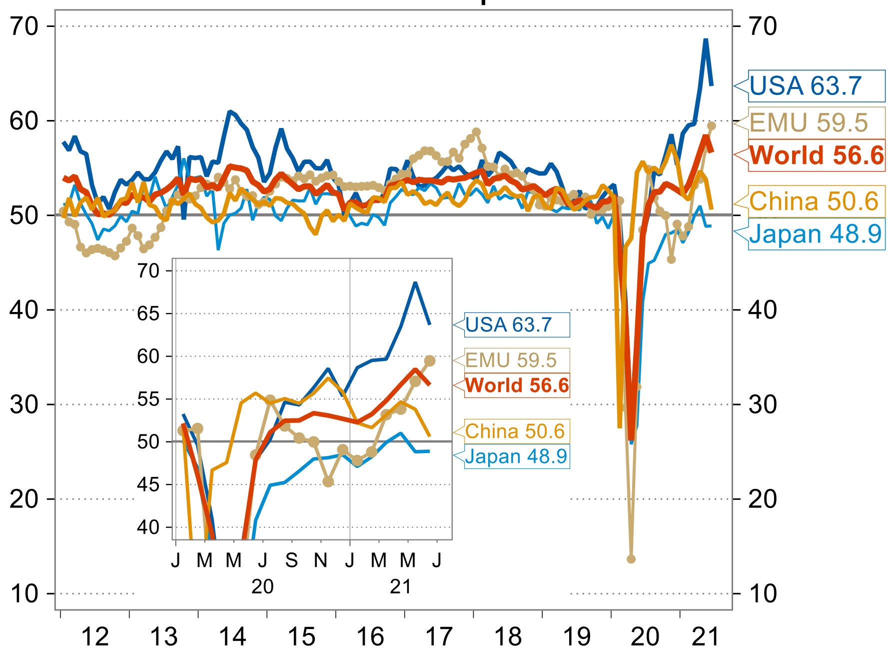


- The PMI signals growth at close to twice the trend growth
- Both services and manufacturing contributed on the downside in June

Rich countries in the lead, while some emerging markets struggle

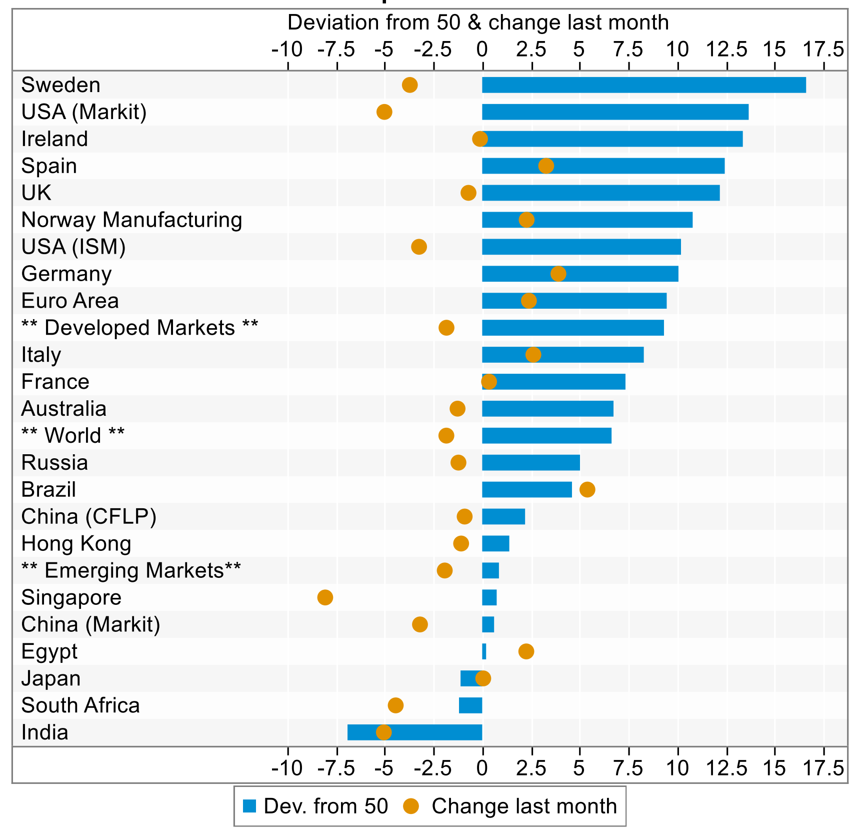
The Swedish PMI is the best of all, ever. Just 3 countries below the 50-line

PMI Composite



Source: IHS Markit, SB1 Markets, Macrobond

Composite PMI



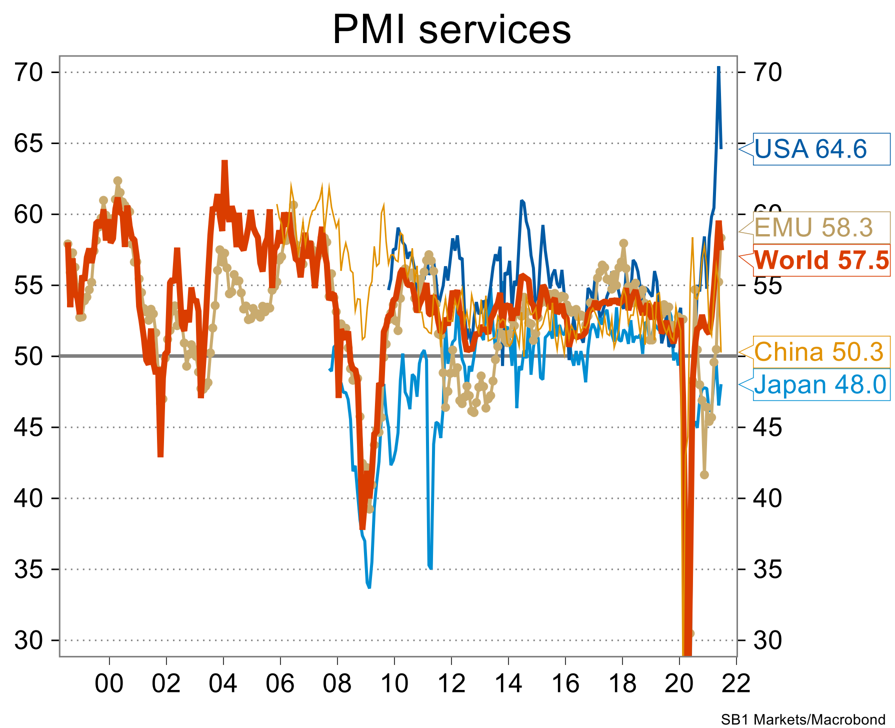
SB1 Markets/Macrobond

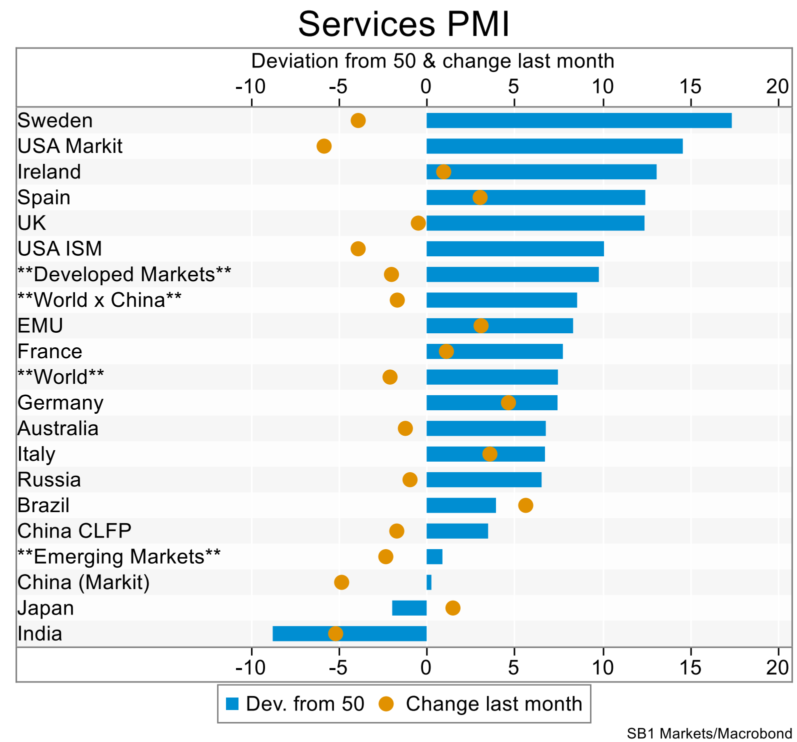
- 9 countries/regions up (from 17 in May), 16 down in June (from 8). 3 below the 50-line (from 4)
- Sweden, US, Spain, and the UK at the top.
- The Chinese PMIs were down across the board
- India at the bottom, following a further decline June – even if the virus outbreak has been beaten back and mobility has increased significantly

SpareBank 1 MARKETS

The service sector PMI -1.9 p to 57.5 in June – signals far above average growth

Sweden/US at the top. The service sector in India & Japan in contraction mode. Guess why?



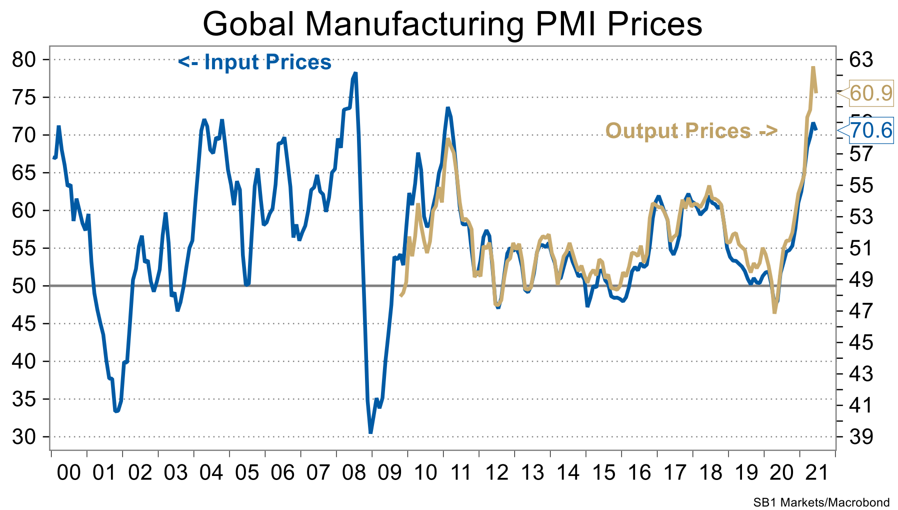


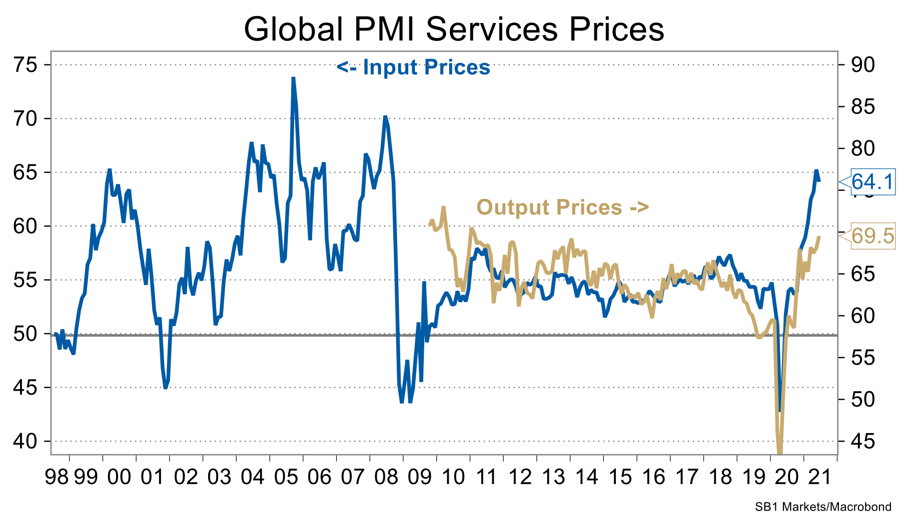
- The service sector PMI fell 0.1 p more than we assumed, but still signals a brisk ongoing recovery in services
- 8 countries/regions up (13 in May), 13 down (6); 2 below the 50-line (3) , 18 above
- Both the ISM and Markit's PMI fell in the US. Given the decline in Markit's PMI, the decline in the ISM was not surprising
- Services in France, Spain, and Italy surprised on the upside
- India and Japan are at the bottom, below the 50-line. All due to covid surges and restrictions, of course

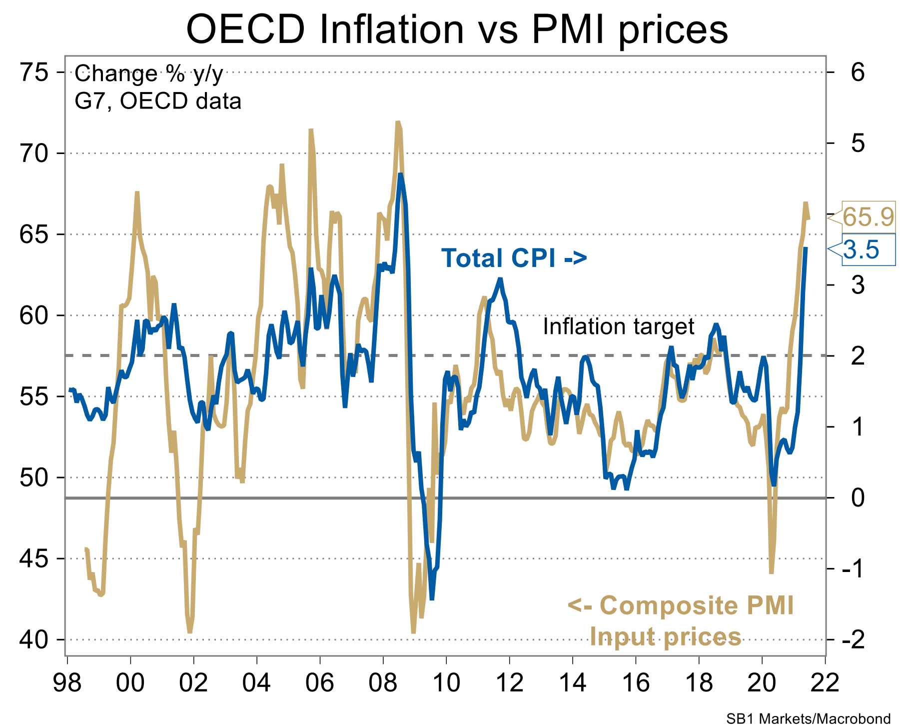
SpareBank 1 MARKETS

Businesses keep reporting rapid growth in input/output prices but a tad slower

Peak PMI price indices? Still, higher CPI inflation unavoidable, at least short term





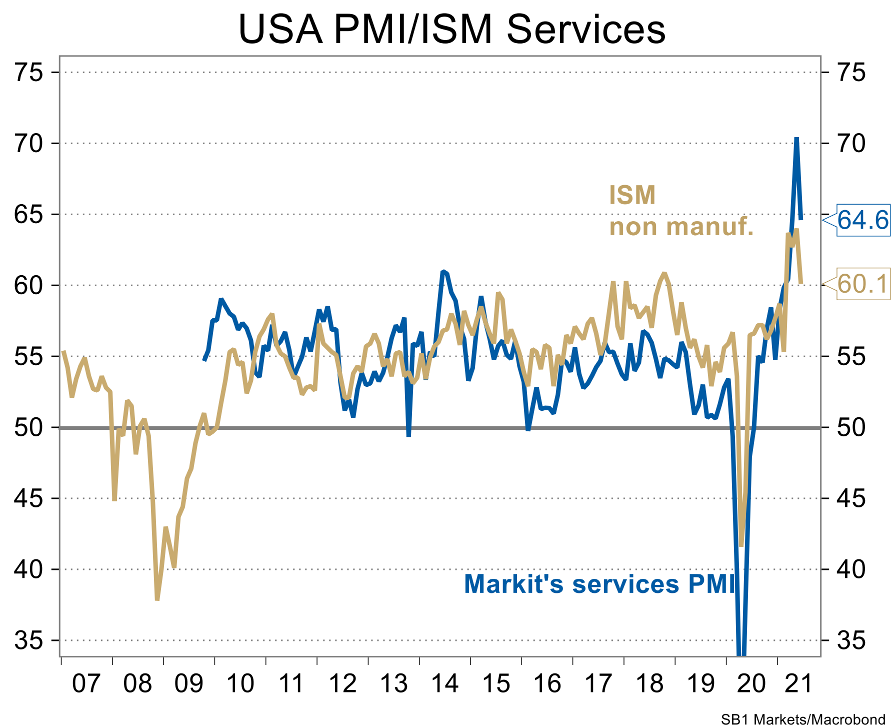


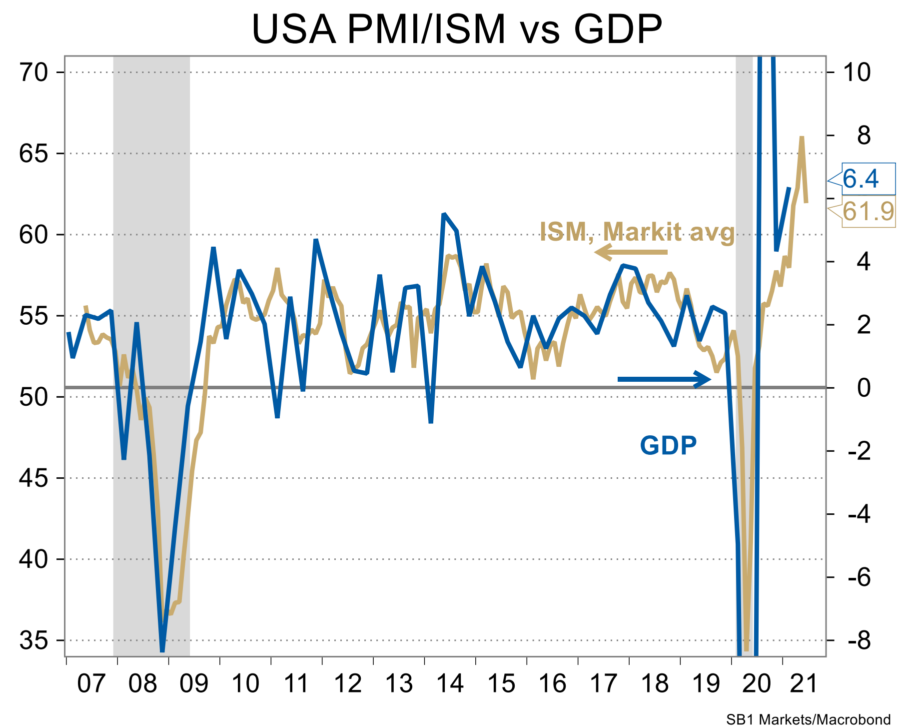
- **Both manufacturers and services** are reporting rapid increases in prices, both input & output prices
- The correlation to **actual CPI inflation** is not prefect, but the PMI price indices are signalling a lift in headline inflation, from 3.5% in rich countries in May
- The correlation to **core CPI** is far less impressive

SpareBank 1 MARKETS

Both the PMI, ISM services were down in June, but are still exceptionally strong

Markit's service sector down to 64.6 from ATH at 70.4. ISM also down to 60.1 from ATH at 64

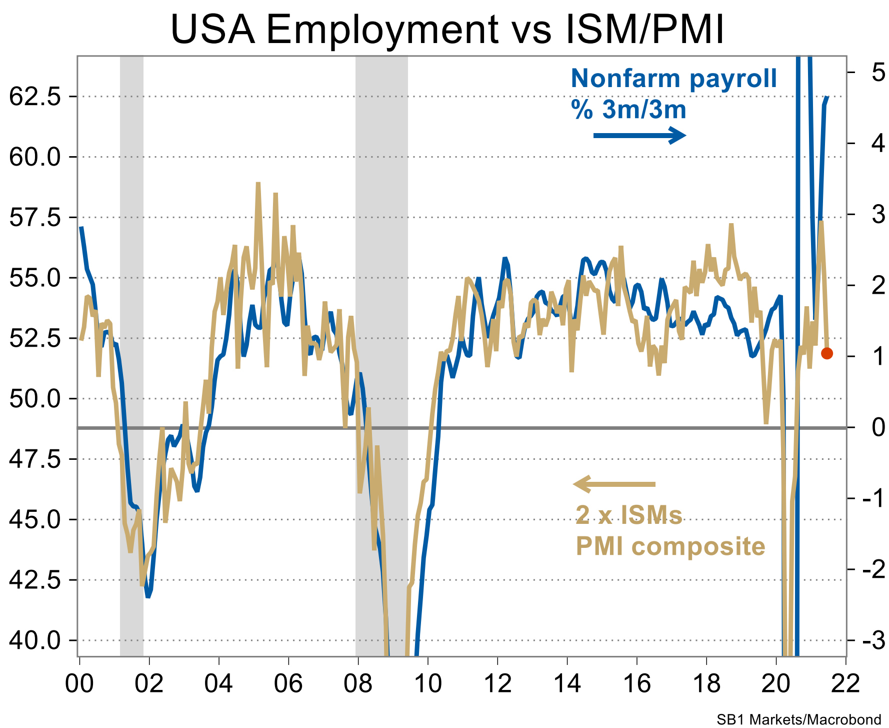




- **Markit's service sector** index was 0.4 p lower than the preliminary estimate, and down 5.8 p from May. The level is still the 5th highest print (of which 3 the previous 3 months)
- **Services ISM fell** 3.9 p to 60.1, expected down to 63.5. Given the decline in PMI services, no big surprise. 16 sectors report growth, 2 lower activity (real estate, agriculture). Some sectors are reporting serious labour shortages, and transport/warehousing report unprecedented wage increases. <u>Services are reporting a decline in employment!</u>
- Together with their manufacturing indices, the **PMI/ISMs** signal some 6% GDP growth in Q2. Does not seem unreasonable at all
- **Prices indices** are soaring, for input prices as well as output prices (in Markit's PMI)

PMI/ISM: The employment indices down, very likely due to lack of labour

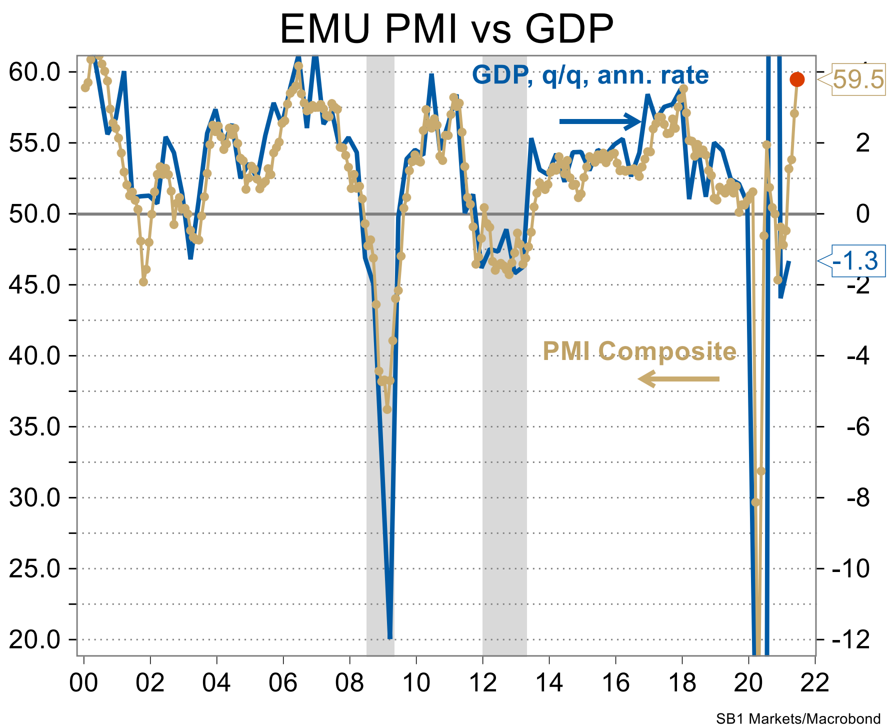
Services are reporting a decline in employment – <u>which is a 'catastrophe' today</u>

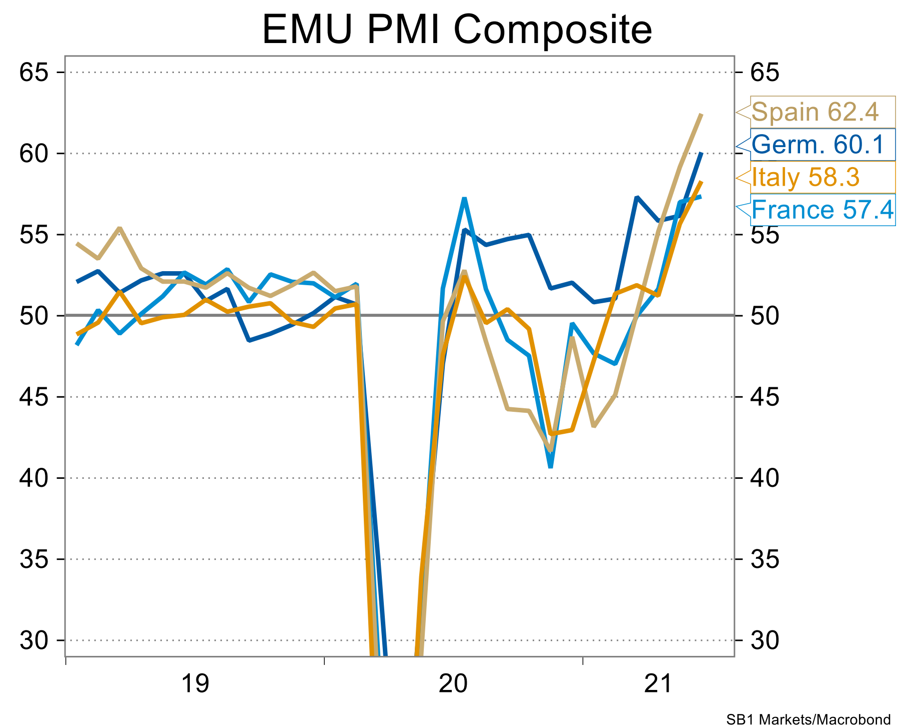


- **Actual employment** growth surged in June – and far more than expected – and the past 3m/m employment is up at a 4.5% pace
- Now, **ISM services** are reporting a decline in employment, while **manufacturers** reported an increase in employment.
- The weighted average of PMI & ISM employment index is at an average level, signalling an average growth in employment <u>which is far below what's needed, given the 4% – 5% shortfall in employment vs. the pre-pandemic level</u>
- According to the **Markit PMI** survey, companies are reporting that they are struggling to find the <u>right</u> employees
- The respondents in the **ISM services** survey join in; several sector report lack of labour and one sector that wages are increasing in an unprecedented pace

The June PMI sharply up, and even a tad more than the prelim. estimate signalled

Services strong as restrictions are eased, and the manufacturing is reporting the highest growth ever

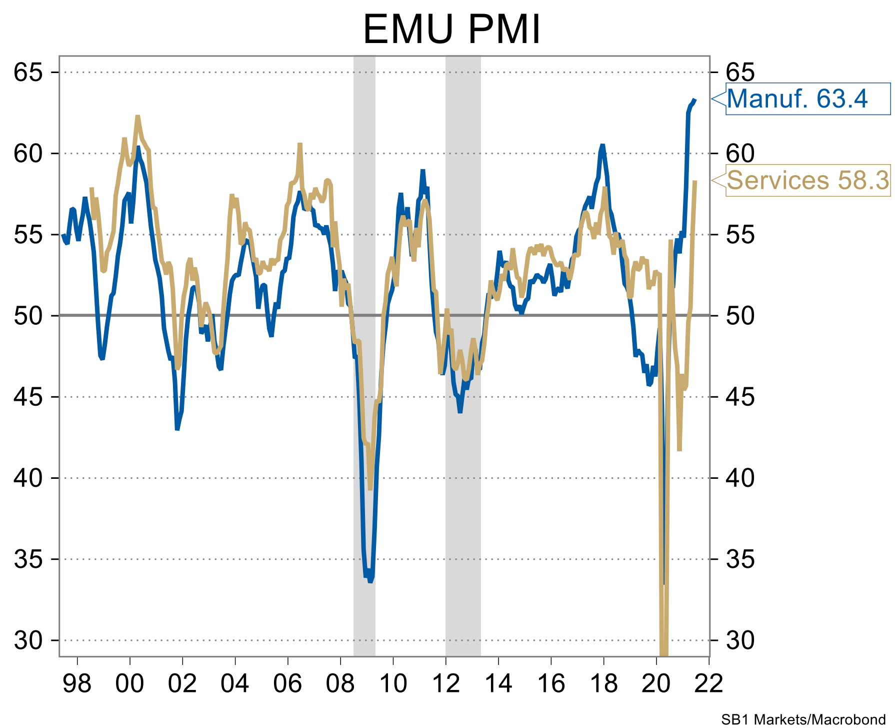


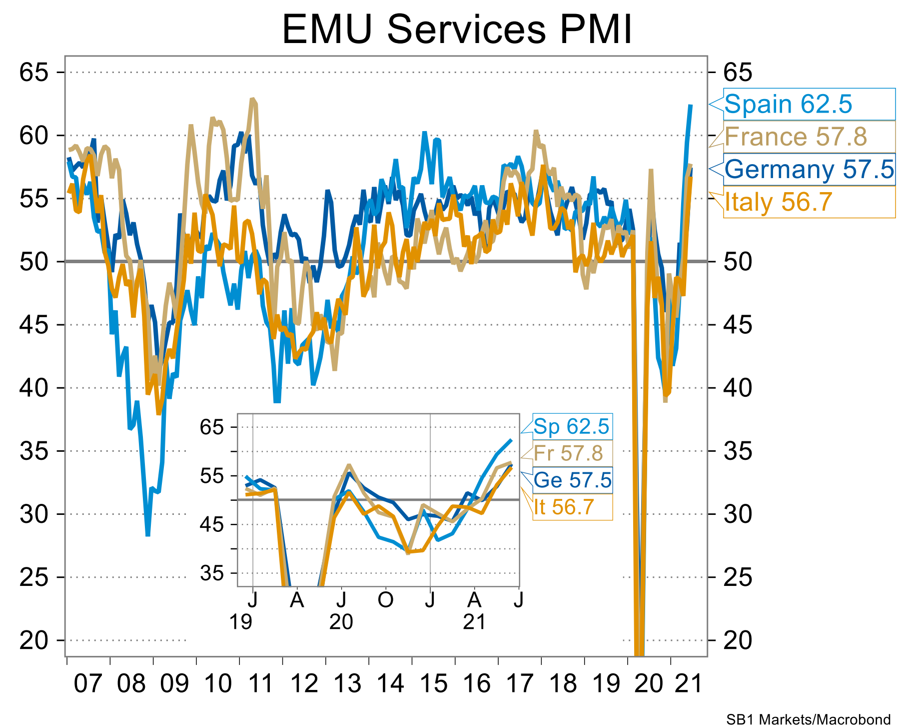


- The final **composite PMI** rose to 59.5 from 57.1 (0.3 p higher than flash estimate)
- The composite PMI is at or above 55 in all of the big four economies
  - » The PMI was higher than the initial estimate, and now signals close to 4% growth in GDP
  - » GDP fell by 0.6% in Q1 (2.4% annualised), more than signalled by the PMIs. Q2 and Q3 will be far better ☺

Services report strong growth as more restrictions are eased

Manufacturing sector still solid – but very likely close to peak (and Germany may have peaked)

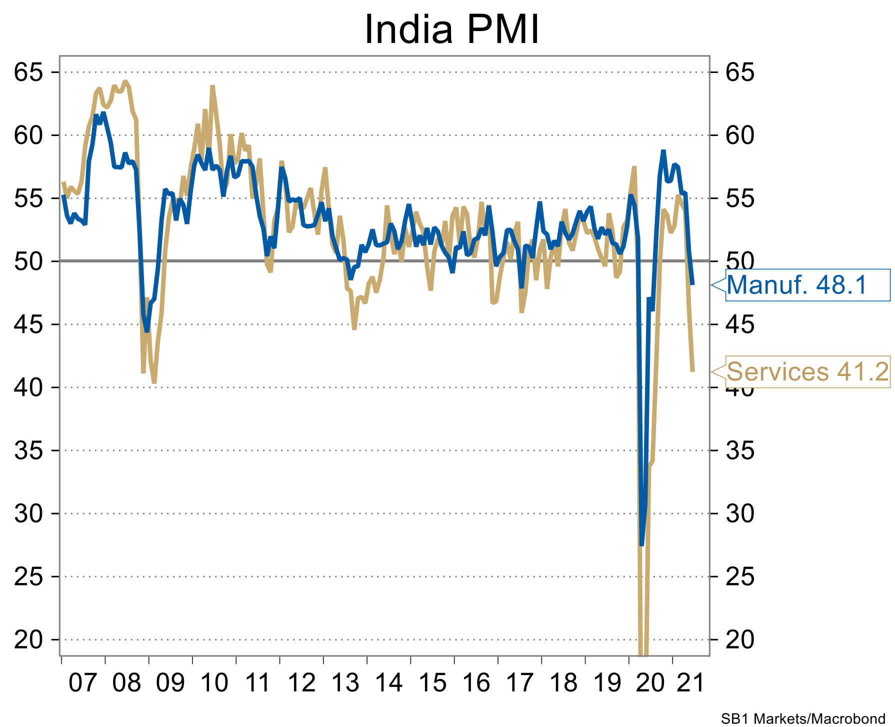


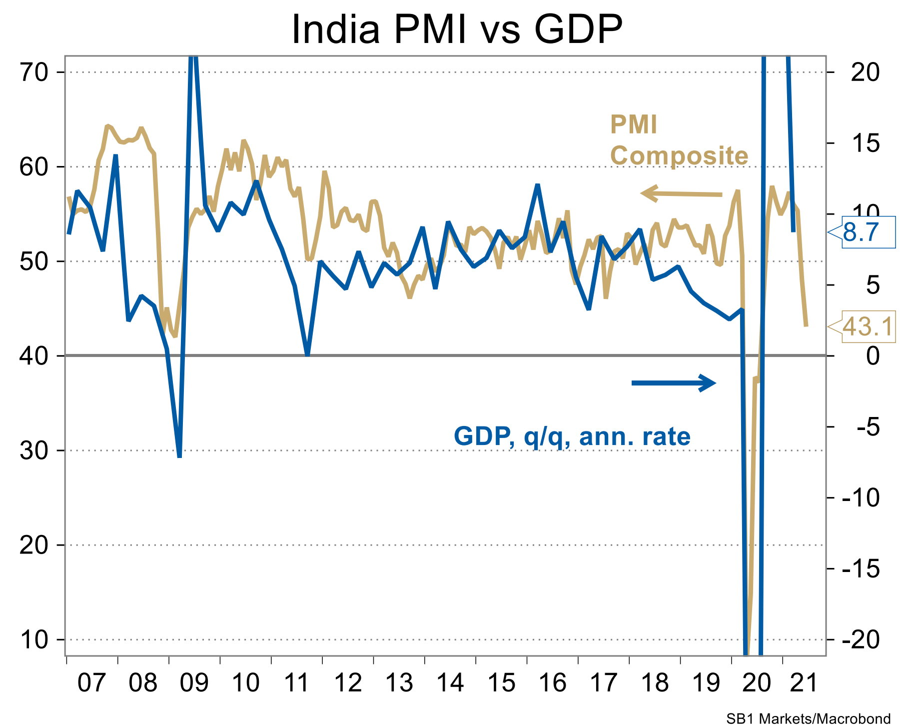


- The **services PMIs** came in <u>above</u> the preliminary estimate/expectations in three of the big four economies in the EMU in June. The PMIs rose by 4.7 p in Germany, and 3.6 p in Italy, 3.1 p in Spain, and 1.2 p in France from the previous month. EMU service index at 55.2 in May, up 4.7 p
- **The Eurozone manufacturing PMI** was up 0.3 p to 63.4 to a new ATH in June. The manufacturing PMIs rose in two out of four major EMU countries, but the level is still rock solid everywhere: up 1.8 p in Germany, down 0.4 p in France, down 0.1 p (from ATH) in Italy, and up 1.0 p in Spain.

It took some time, but the Covid crisis did have some economic consequences

Composite fell 5 p in June down to 43.1. Still, a contraction in GDP is not given

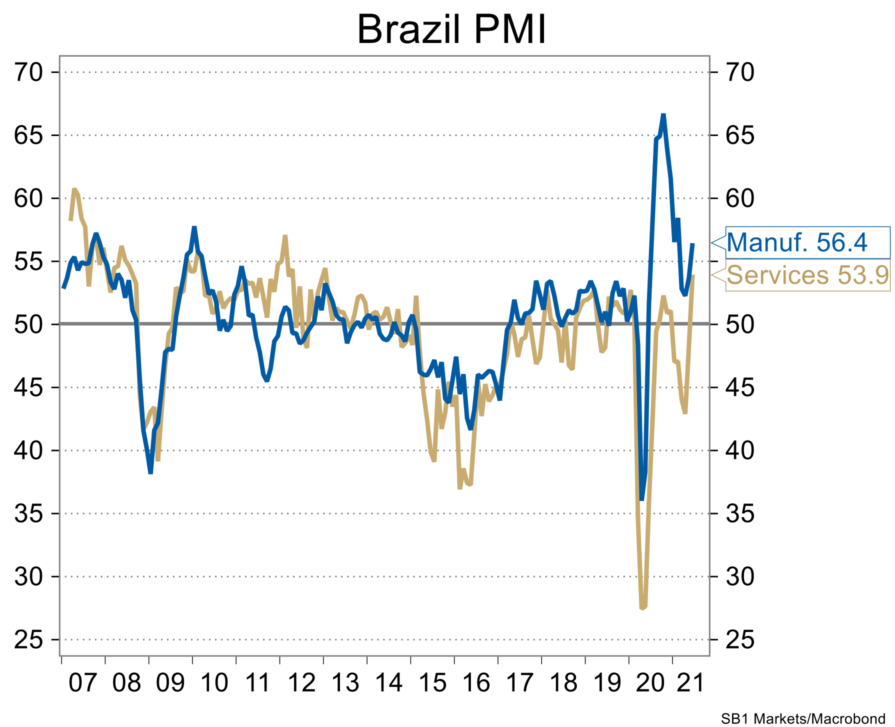


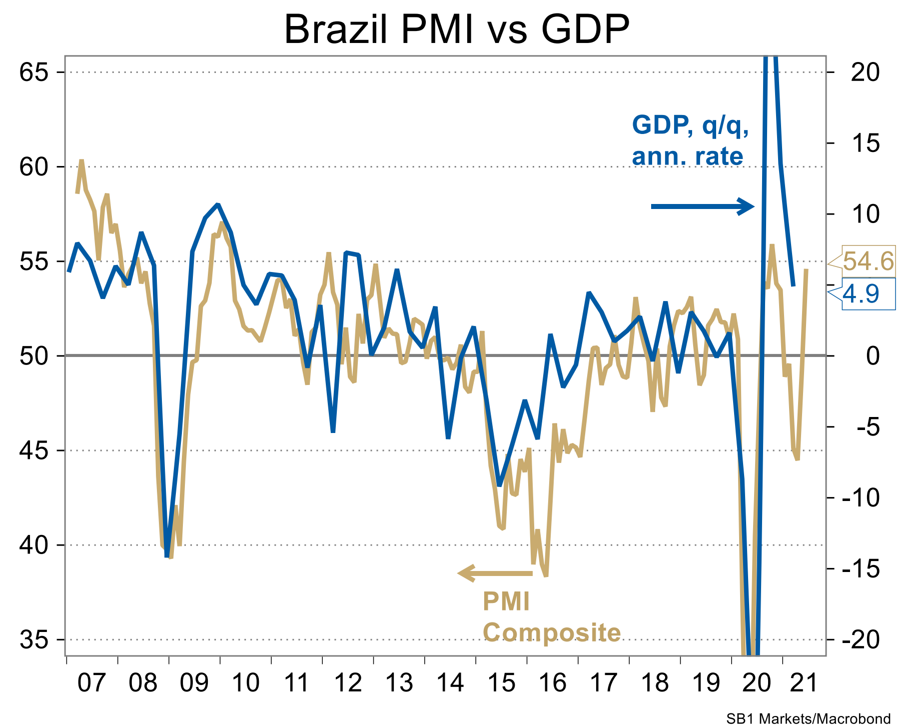


- **The manufacturing PMI** fell by 2.7 p 48.1, down below an average level and into contraction territory
  - » Manufacturing cost inflation running very high, according to Markit
- **The services PMI** was down 5.2 p to 41.2 in June, both due to restrictions and lower international demand for Indian services
- The correlation between **PMI and GDP** is not that impressive but the 43.1 composite PMI does not necessarily imply a decline in GDP
- GDP rose by 8.7% (annualised) in Q1 (down from 43% in Q4), and is 2.7% up vs. Q4-19, beaten only by China. Still, GDP was almost 4.5% below the pre-pandemic trend path – and the gap very likely widened in Q2

Brazilian service sector is expanding for the first time since December

Eased restrictions and cont'd vaccination sends PMI up 5.6 p to 59.9 in June

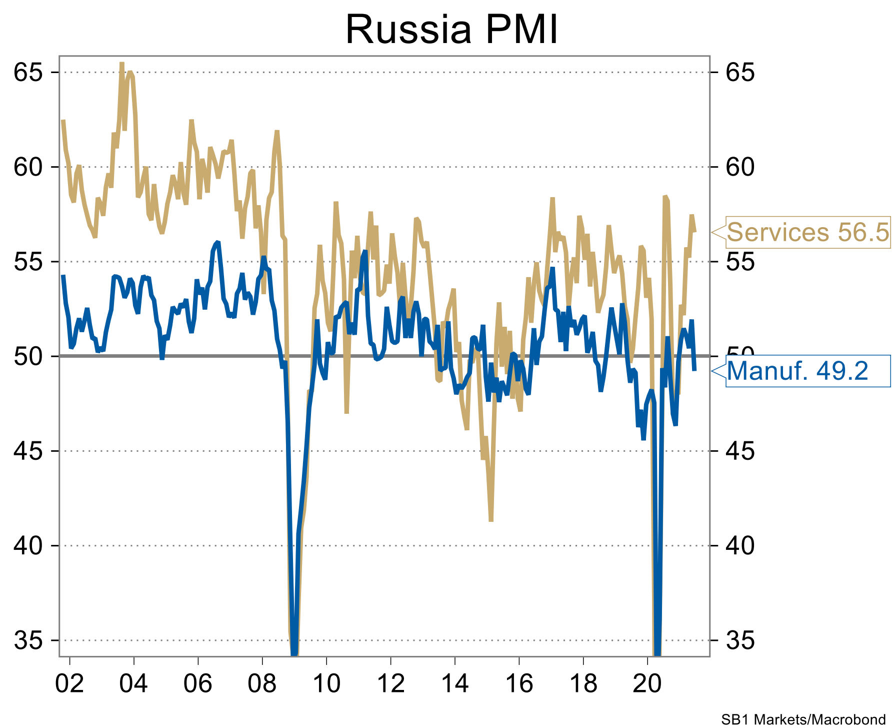


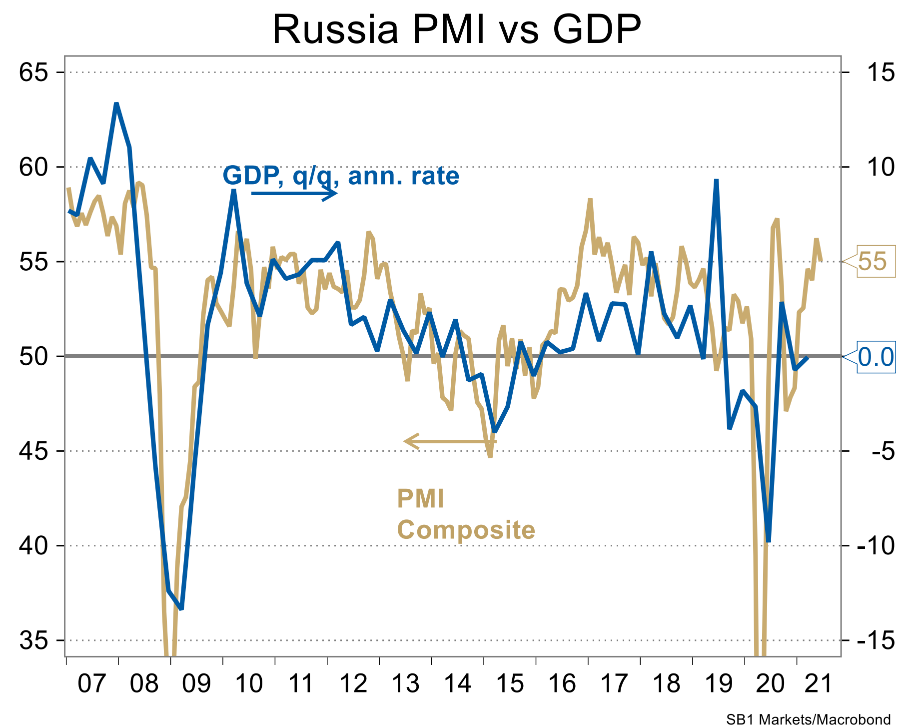


- **Manufacturing PMI** increased by 2.7 p to 56.4. Orders are rising, production is rising, costs are rising, and so are selling prices. Employment in the manufacturing sector increased at the fastest pace in 7 months
- **The service sector PMI** was up 5.6 p to 53.9; as restrictions were eased, the service sector rebounded – here as everywhere else
- **The PMIs** signal some 6% pace growth in GDP by the end of Q2 – but the average PMI in Q2 equals zero growth
- **GDP** grew more than expected in Q1, by 4.9% (the PMI signalled zero!) and the GDP level is back to the Q4-2019 level, among the best on our list (just China, India, South Korea are above). GDP is down just 1.3% vs the very weak pre-pandemic growth path

Russia's manufacturing sector in contraction mode, service PMI still very strong

The PMI signals ~5% growth in Q2, – if so, Russian GDP on par with pre-Covid level

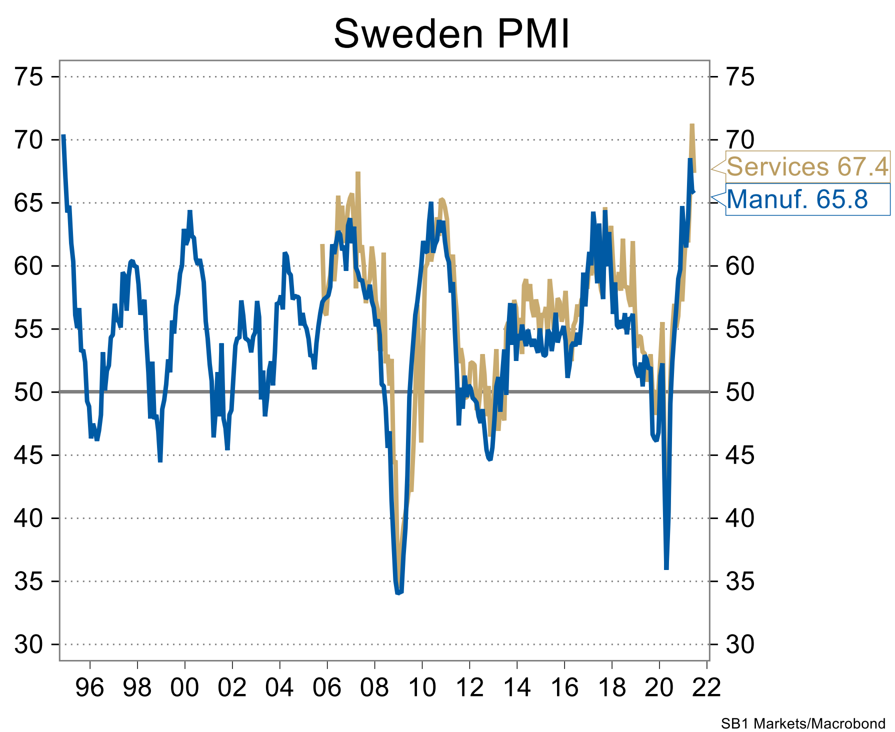


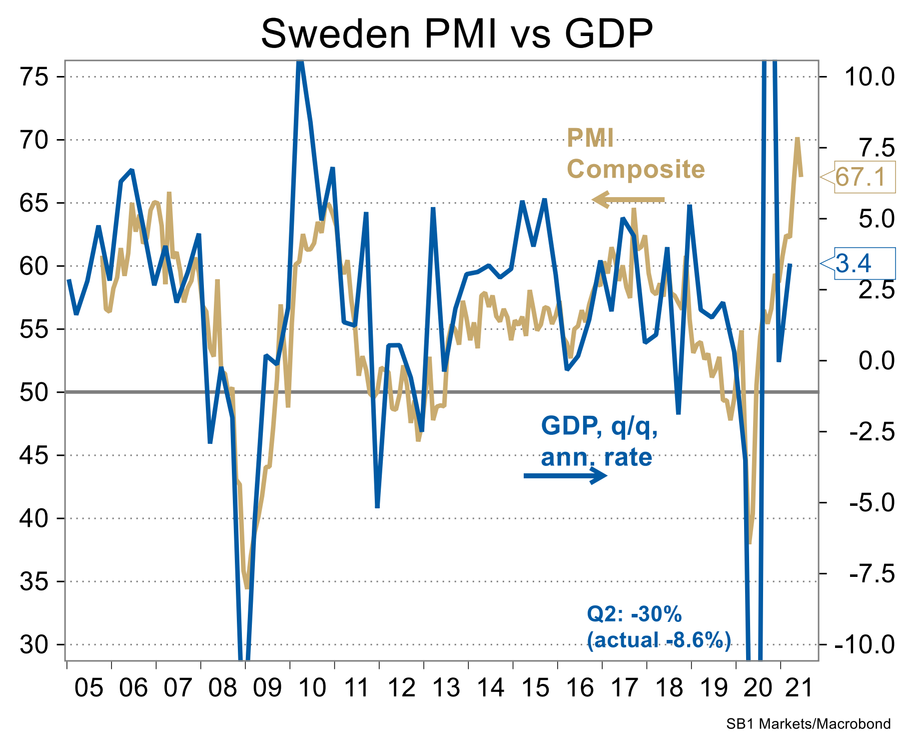


- **Manufacturing PMI** fell to 49.2 in June from 51.9 a month ago
- **The service sector PMI** down 1.0 p to 56.5 in June – but remains above an average level
- **The composite PMI at** 55 (down 1.2 p) signals GDP 5% growth
- **GDP** is still 1.6% below the pre-Covid level, but on the bright side, Markit is reporting that export orders rose at the fastest pace in over 2 years and that employment hasn't increased faster since 2011

The composite PMI down 3.5 p, but still incredibly strong at 67.1

The services index was down 3.9 p to 67.4 in June (down from ATH at 71.3 in May)

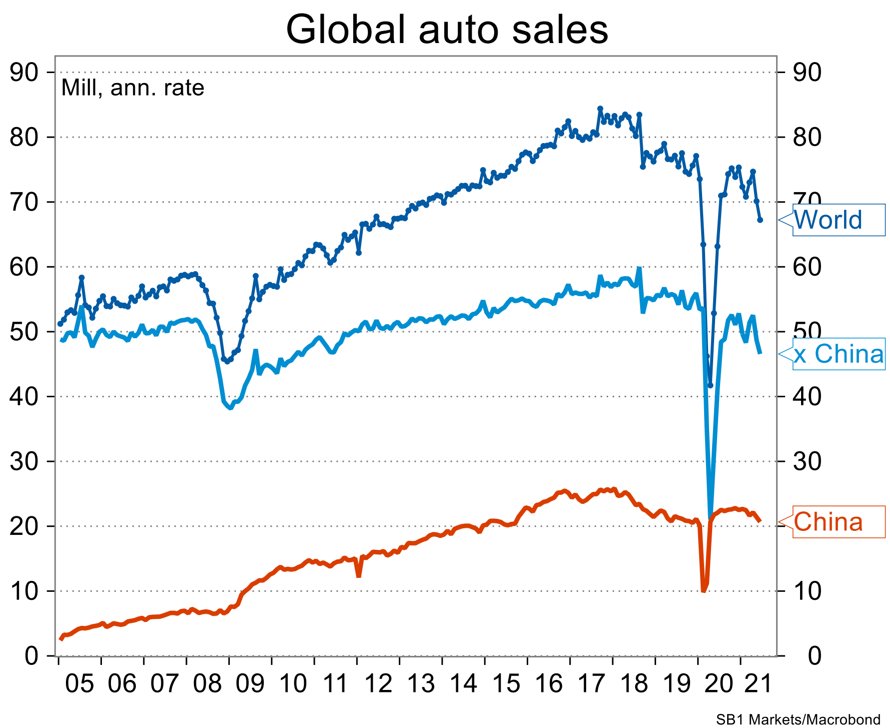


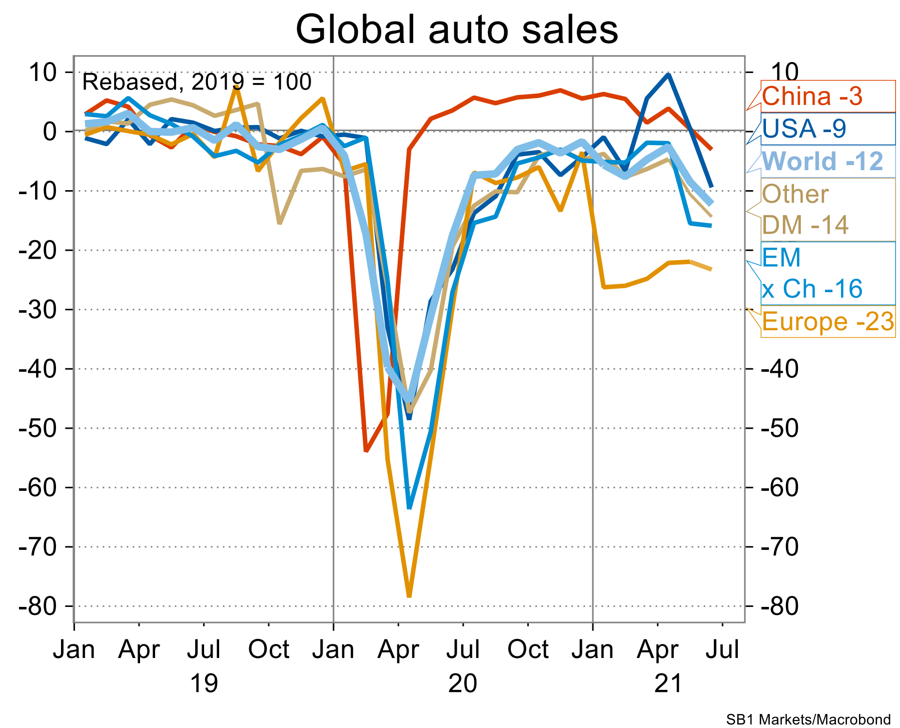


- The **PMI** has gone from record to record for several months, but came down somewhat in June. However, the numbers are still very strong, signalling some 6% - 7% GDP growth. The service sector is still expanding fast (here as elsewhere), even though the **services PMI** was down 3.9 p in June. The **manufacturing PMI** was down 0.2 p to 65.8, but who cares at this level anyway…
- **GDP** grew at a 3.4% pace in Q1, somewhat less than preliminary data implied
- **The Riksbank** is still buying bonds, and says it expects to keep the signal rate at zero until 2024. We are not so sure…

Auto sales down most places in June – global sales down 4%, -12% vs pre-Covid

Semiconductor shortages at least partly to blame for lower sales, but Covid also to blame directly

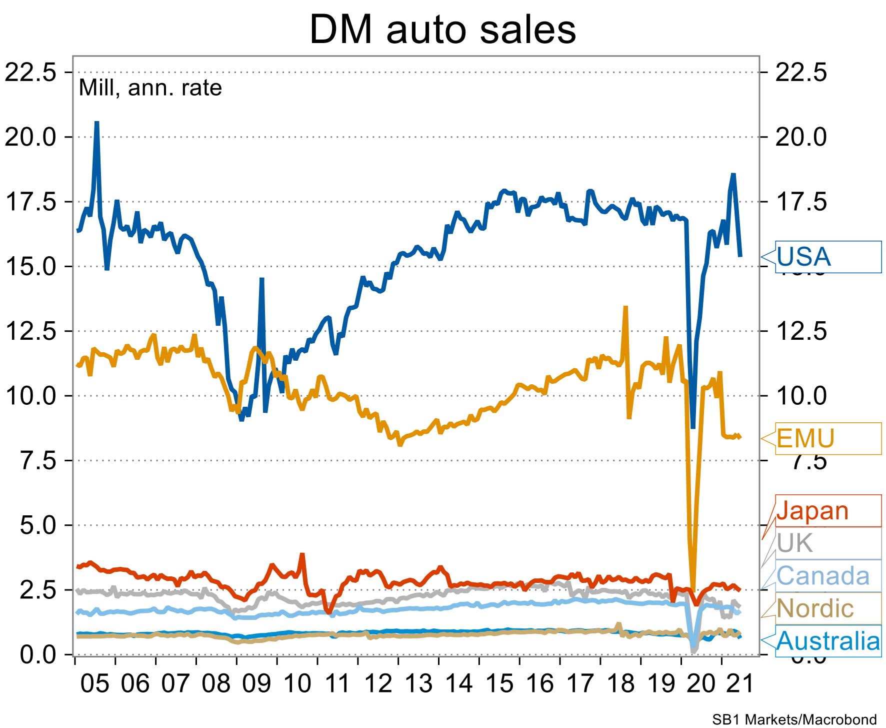


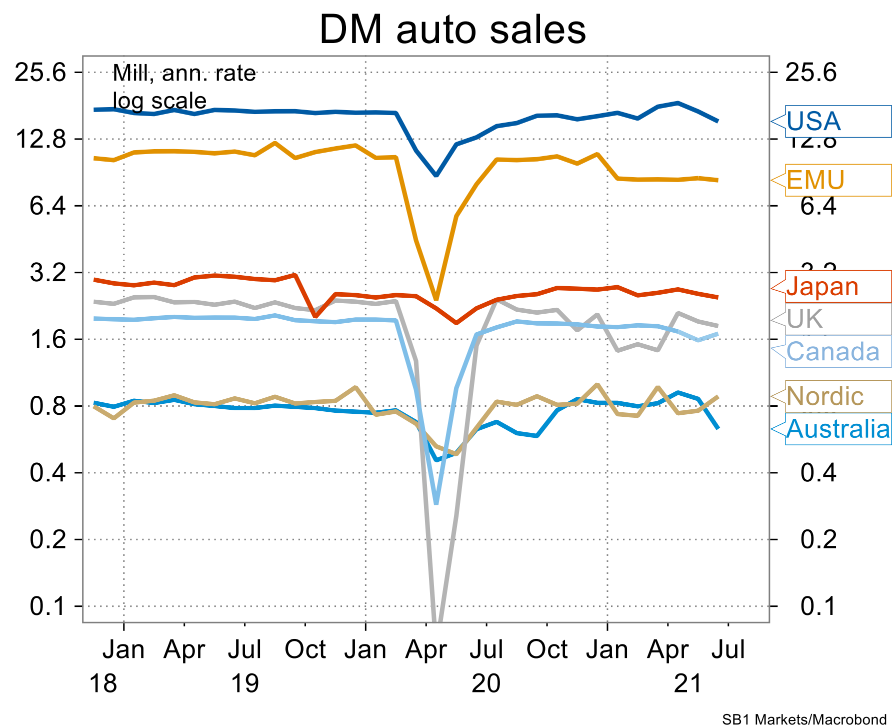


- Based on our <u>preliminary</u> estimate **global auto sales** fell by 4% in June. Sales are down 10% vs. the level in late ’20 and 12% vs the pre-pandemic level. Both supply challenges (data chips) as well as weak demand due to the pandemic (in EMU, India) explains the downturn. We expect demand to pick up in both EMU and India the coming months. The lack of components may last for longer
- Sales fell all main regions, by the most in the **US**. Sales in the **Euro zone** fell marginally, and sales fell in UK as well
- Sales in **China** have been revised down by 3% - 5% and fell further in June, and are now below the pre-pandemic level, which was low
- Sales in **India** probably recovered somewhat in June but remains far below the April level, and sales fell in both **Russia** and **Brazil**

DM sales: EMU is still down 20% vs. last Dec/pre-pandemic sales

Sales in UK are almost back to the Dec/pre-pandemic level, but fell in both May & June

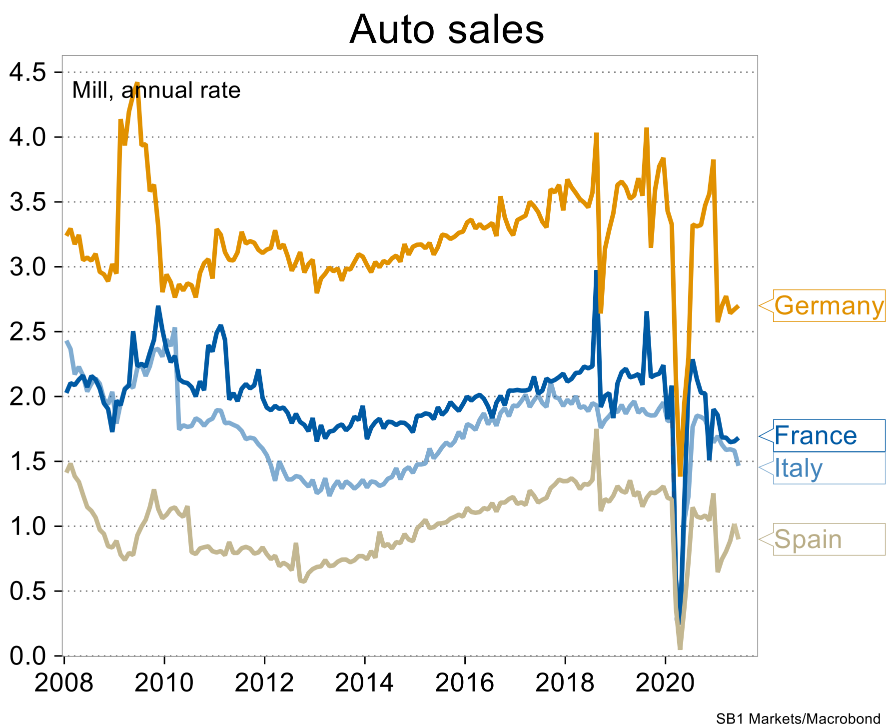


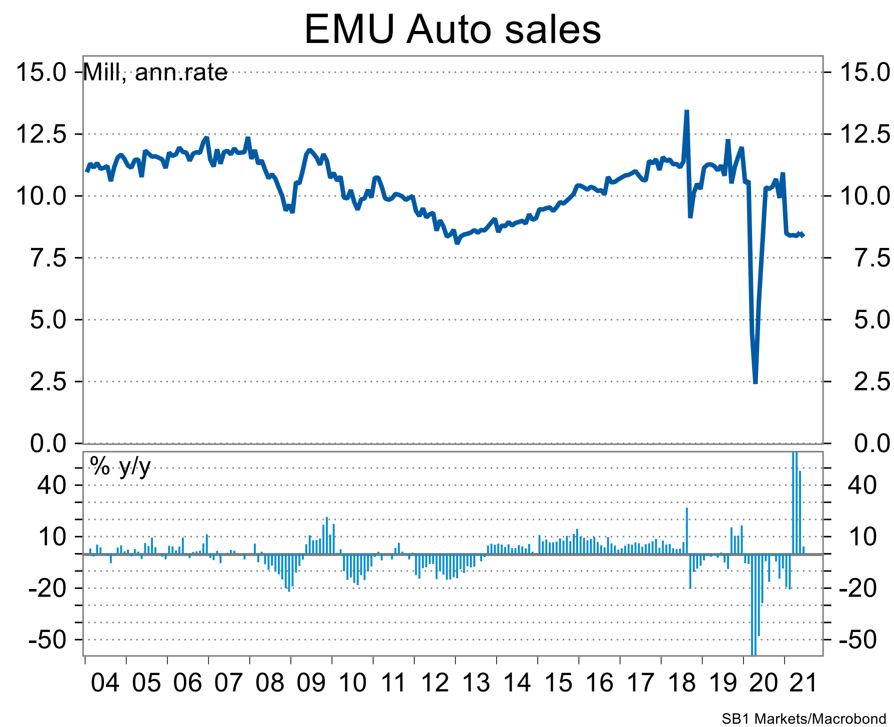


- The decline in the EMU very likely mostly due to weak demand during the 2nd/3rd wave, at least initially. Slow sales in June may also be due to lack of supply as auto production has fallen

EMU: Auto sales slightly down in June – level remains 20% below H2-20 level

Sales rose marginally in Germany and France but fell more in Spain & France. Demand still weak?

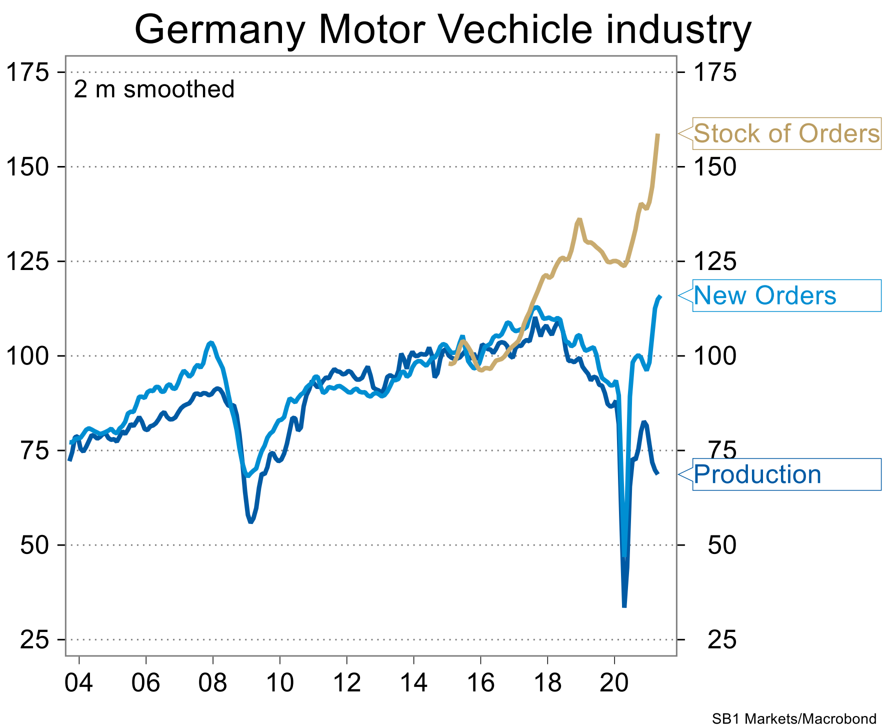


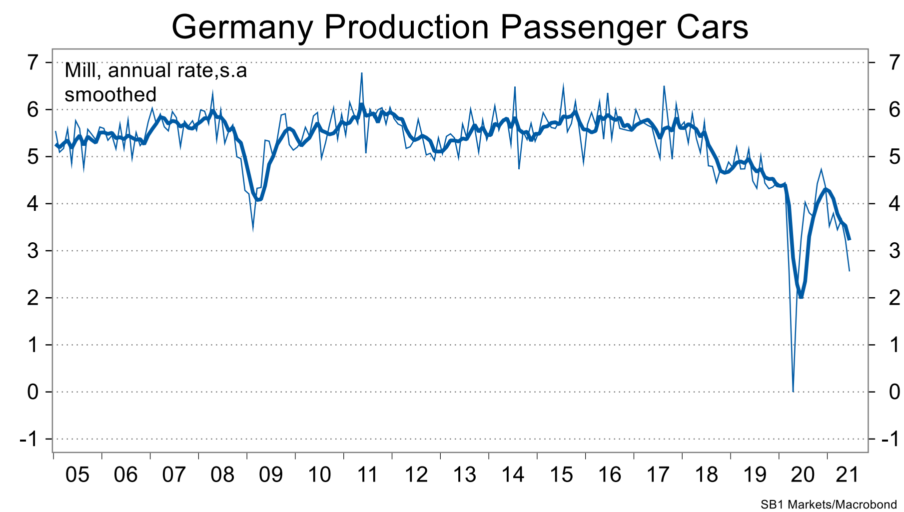


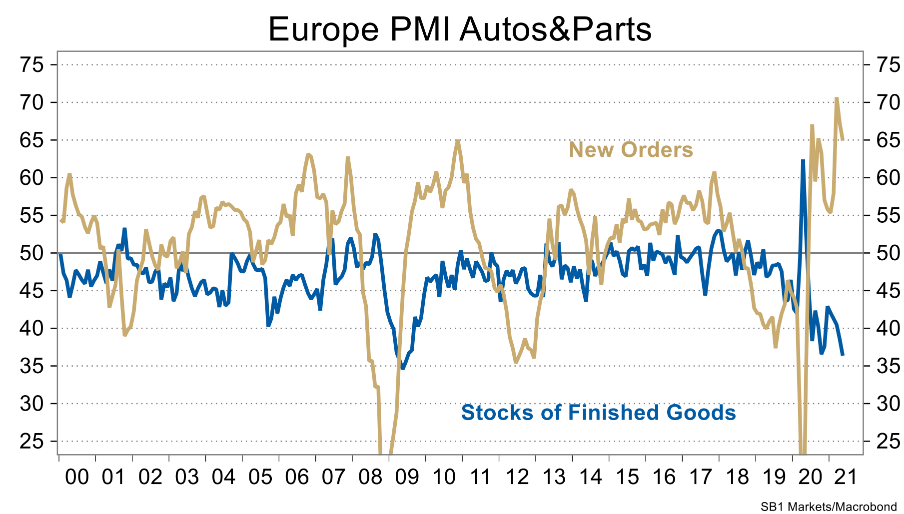
- There are serious production challenges in the European auto industry due to lack of data components. However demand has very likely been the main reason for decline in sales in H1 – and lockdowns have made it challenging to buy cars
- Still, we expected sales to climb significantly in June, as restrictions were eased in all countries

What's the problem? Seemingly, not demand…

Stock of orders are skyrocketing, production is nosediving. Seems to be a serious supply problem



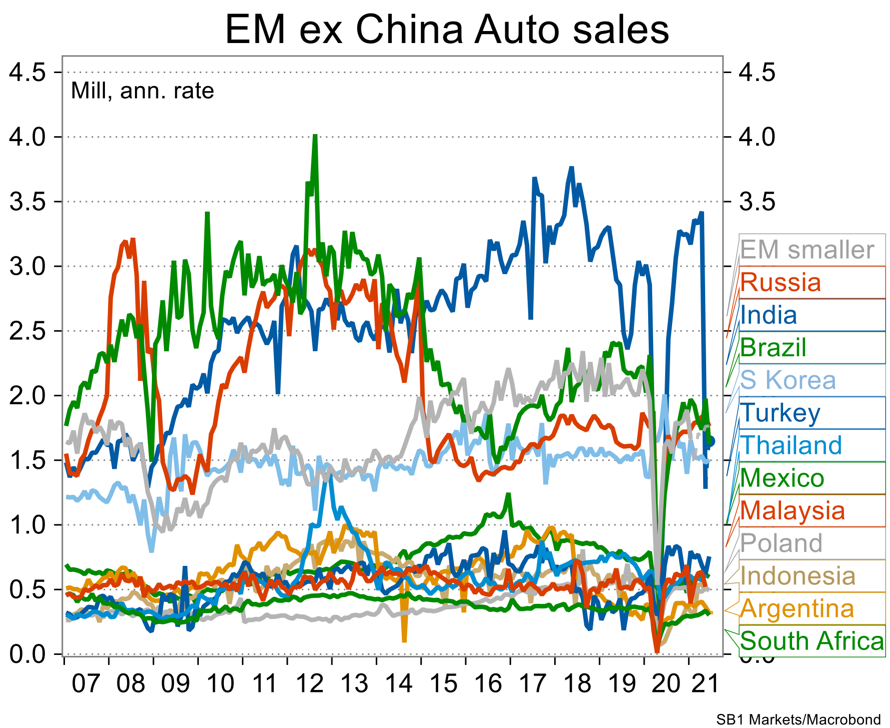


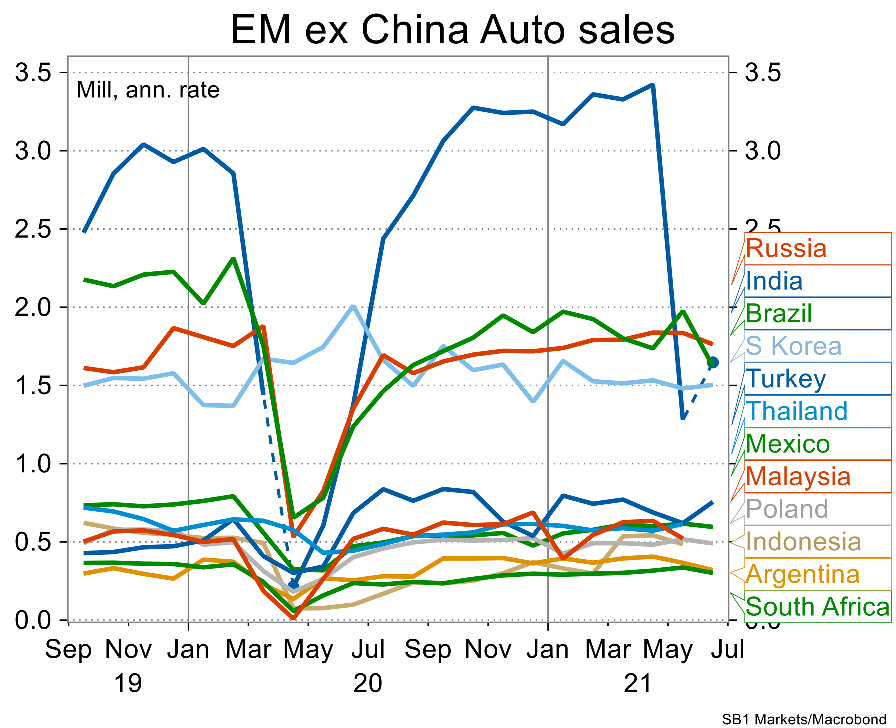


- The lockdown related 20% decline in auto sales in Europe the last months have not made a dent in orders or the order backlog, rather remarkable (both according to actual order data, and the European Auto PMI)
- Production of cars in June was down 45% (!!) from last November. The latter part of the decline in production is very likely due to lack of components, especially semiconductors

EM: Indian auto sales probably up in June, still down 50% vs. April!

Sales down in Brazil and Russia – and others more down than up too

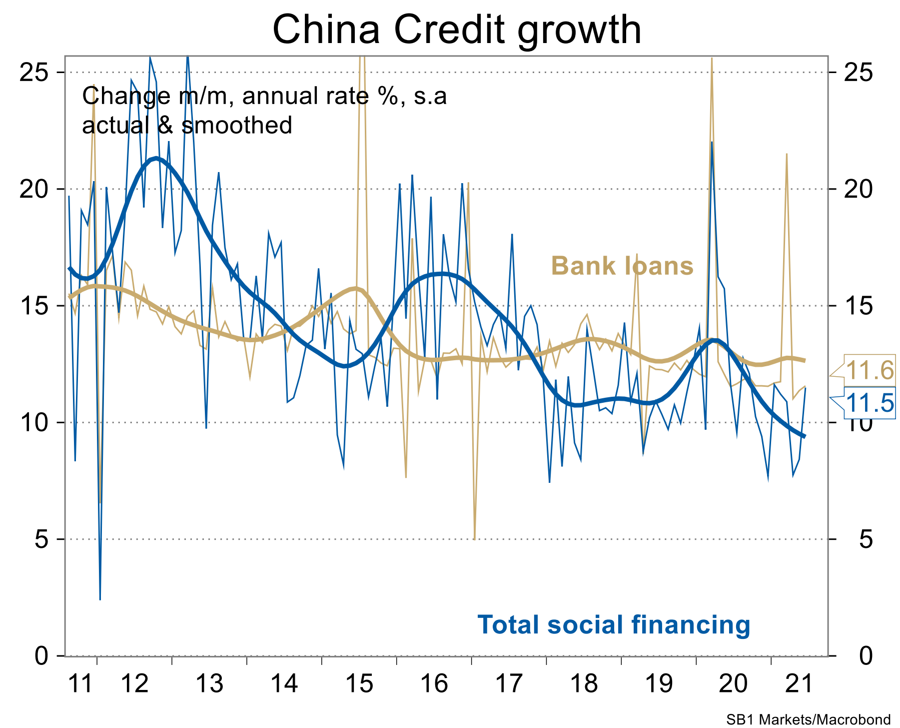




Not all countries have reported yet, and for some countries we have just plugged in figures from media reports that are not always correct

Credit growth accelerated in June, trend still probably down

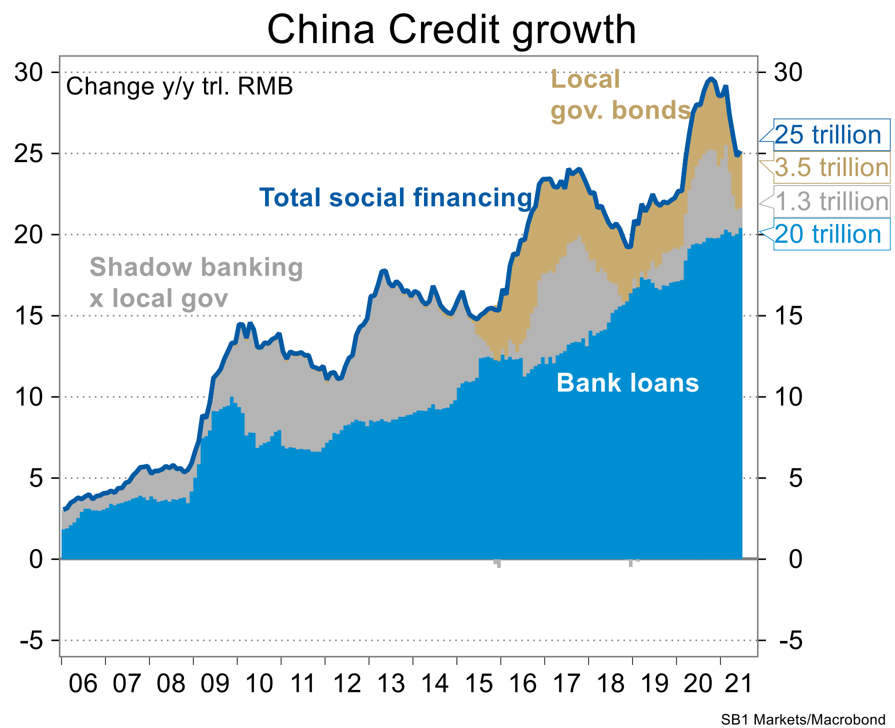
… but authorities are now changing tack, banks' reserve requirements cut!

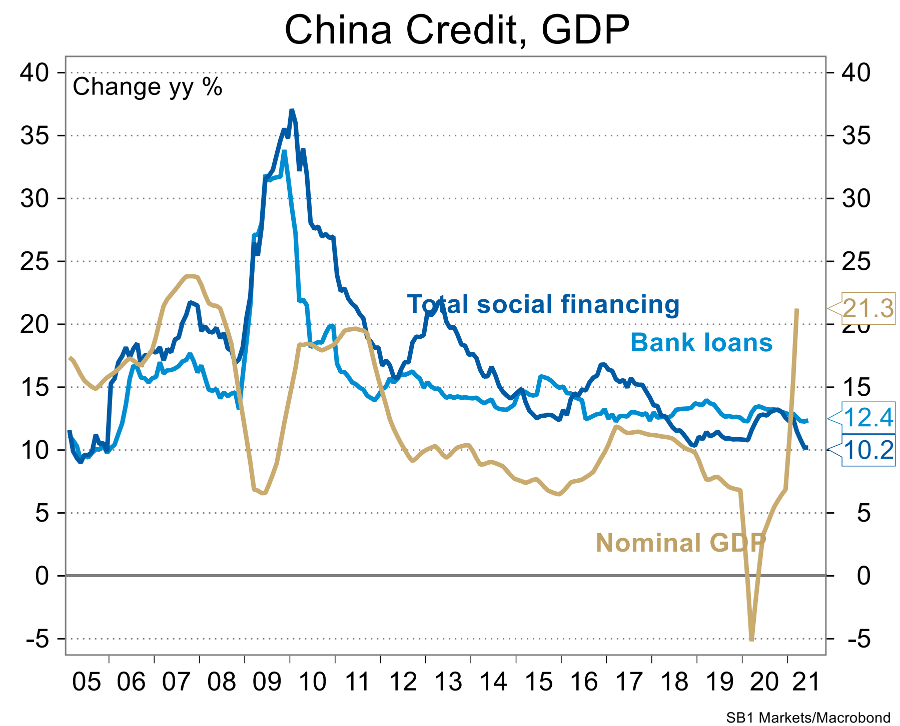


- **Total credit** grew at an 11.5% rate in June (m/m, annualised), up from 8.2 % in May. Smoothed, the underlying rate may be 9% - 10%, down from 13% during last spring (and >15% during some months). A 9% - 10% growth rate is marginally above the trend growth in nominal GDP
  - **Total credit** rose by RMB 3.5 trl, expected 2.7 trl (not seasonally adjusted, total social financing, including central & local government bond, and corporate equities). Seasonally adjusted the core total social credit (total ex central gov bonds & corporate equites) grew by 2.5 trl, up from 1.7 trl in May
  - **Bank loans** rose by RMB 1.7 trl, seas adjusted. Bank loans are up 11.6% y/y
  - **Shadow banking credit** was marginally up 0.8 trl in June, following much slower growth in May and April, and a decline in March. Underlying growth has still fallen sharply
- **The credit impulse has turned negative**, like it usually does every 4th year or so. The ramification may be felt in many markets
- **The slowdown has been by purpose**, as authorities have tightened, especially vs. credit supply outside banks. However, on Friday the PBoC cut banks' reserve requirements – the authorities may shift the foot to the accelerator again

Credit growth has turned south, very likely due to policy tightening

As it usually does, every 4th year. The turnaround now is not faster than before

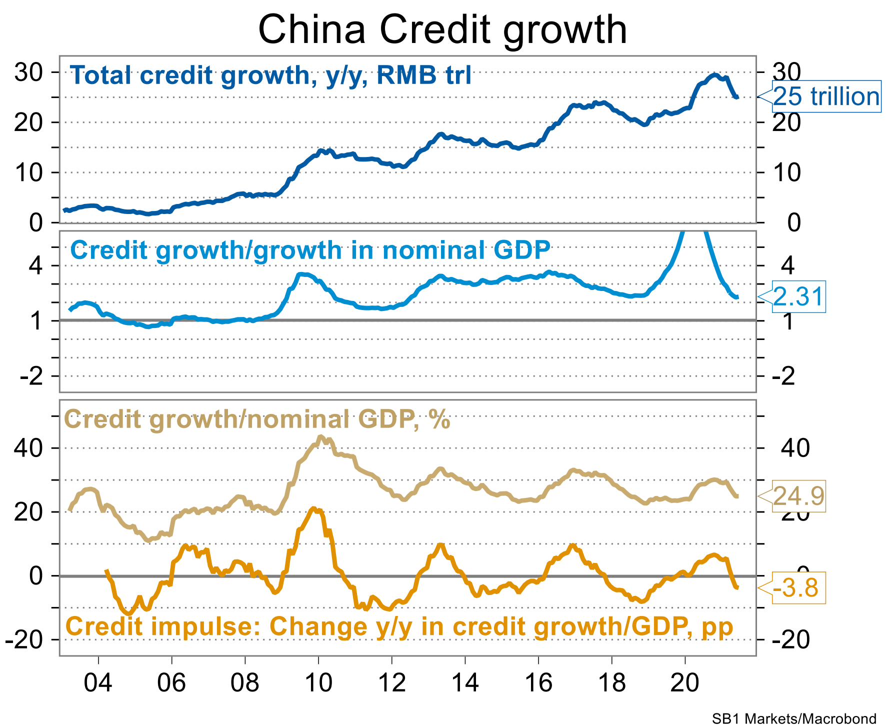


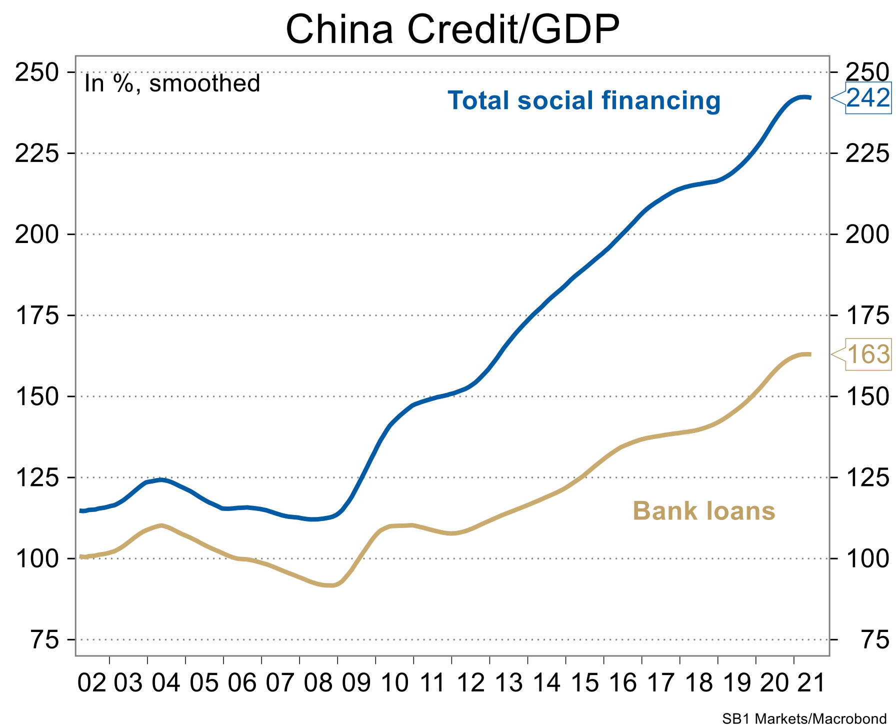


- Over the past year, **total credit** has expanded by CNY 25 trl, equalling 25% of annual GDP, down from CNY 30 trl at the peak
- **Banks** supplied CNY 20 trl of the y/y increase
- **Local governments** have not yet accelerated their borrowing by much, at least not in the bond market, still up 3.5 bn y/y
- Other credit – via the **shadow credit market** x local gov bonds gained speed last spring but has slowed substantially in recent months just up 1.3 trl (from +5 trl!)
- **Total credit** growth unch at 10.2% y/y, the slowest pace since 2005, but still well above nominal GDP growth before the pandemic. Underlying growth in credit recent months is even lower

The credit impulse has turned negative but no drama yet

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



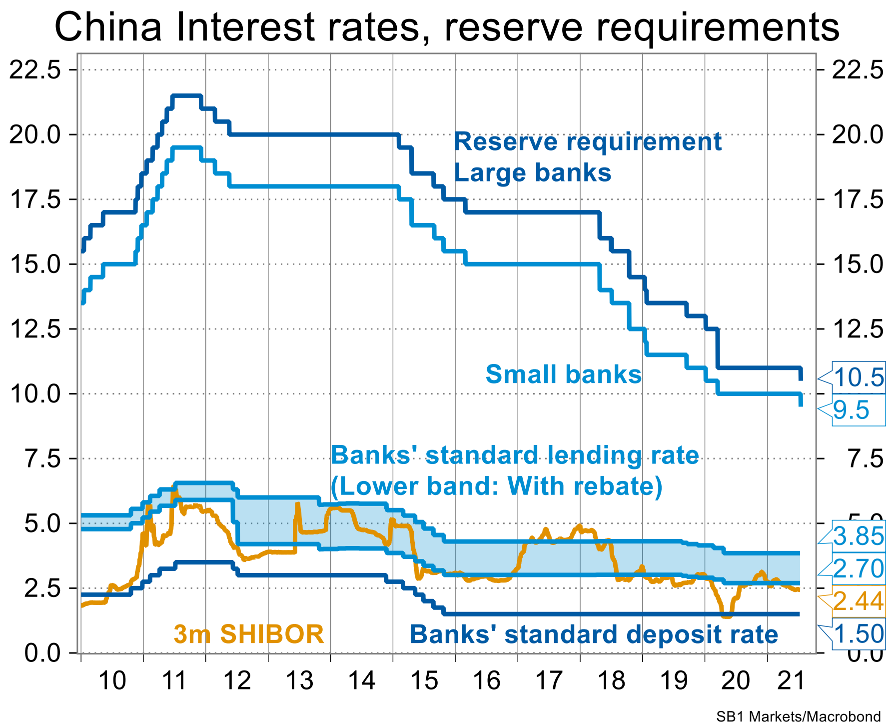


- A positive **credit impulse** implies that the credit growth/GDP ratio is increasing (the 2nd derivative of credit vs the GDP level)
  - » A negative credit impulse indicates credit tightening (or weaker demand) and has been associated with slowdowns in the Chinese economy, which have had impacts at other markets
- The **credit impulse** bottomed in late 2018, turned positive one year later, peaked last autumn and has now – and has now fallen into negative territory – growth in credit is slowing
- Are authorities worried that they have tightened too much? *Check next page*

GDP is smoothed at the calculations on the charts above

The PBoC cut banks' reserve requirements, will stimulate bank lending!

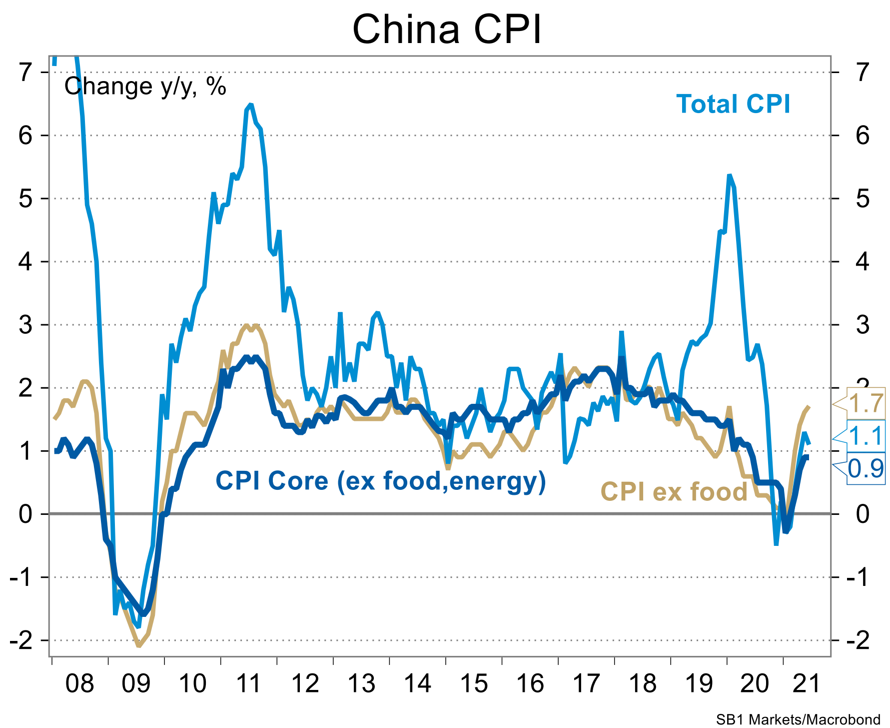
Last Friday's 0.5 pp cut is the first since last spring, a too abrupt credit slowdown is not wanted

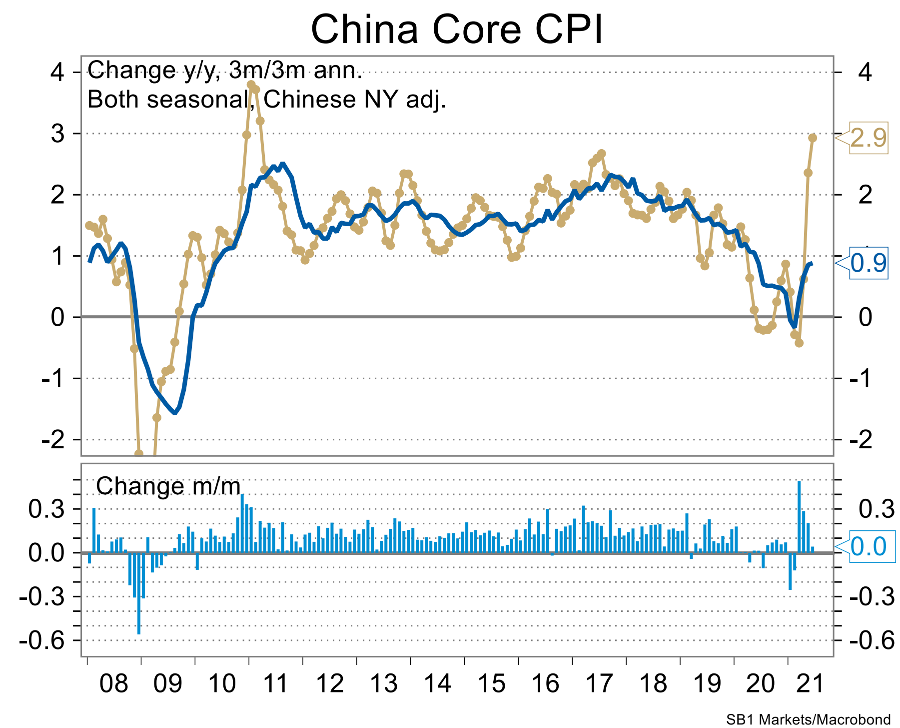


- The reserve requirement was cut by 0.5 pp to 10.5 for large banks and to 9.5% for smaller banks
- The cut will free up some RMB 1 trl in lending capacity in the banking system, equaling 3 weeks' growth in credit supply from banks, no more, no less
- Still, the measure signals that authorities do not want credit tightening to go too far, even if they at the same time are worried that credit grown too fast for too long, increasing the risk for financial instability. This change of tack is rather common in China – and many other countries

Chinese inflation below consensus, as food prices fell. CPI up 1.1% y/y

Core CPI flat m/m, and up to 0.9% y/y

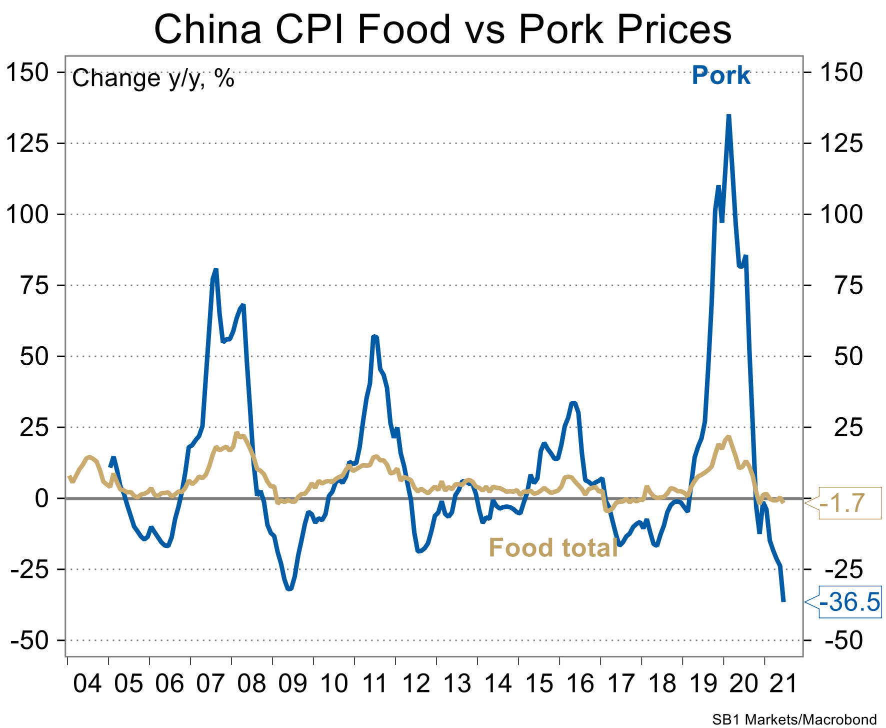


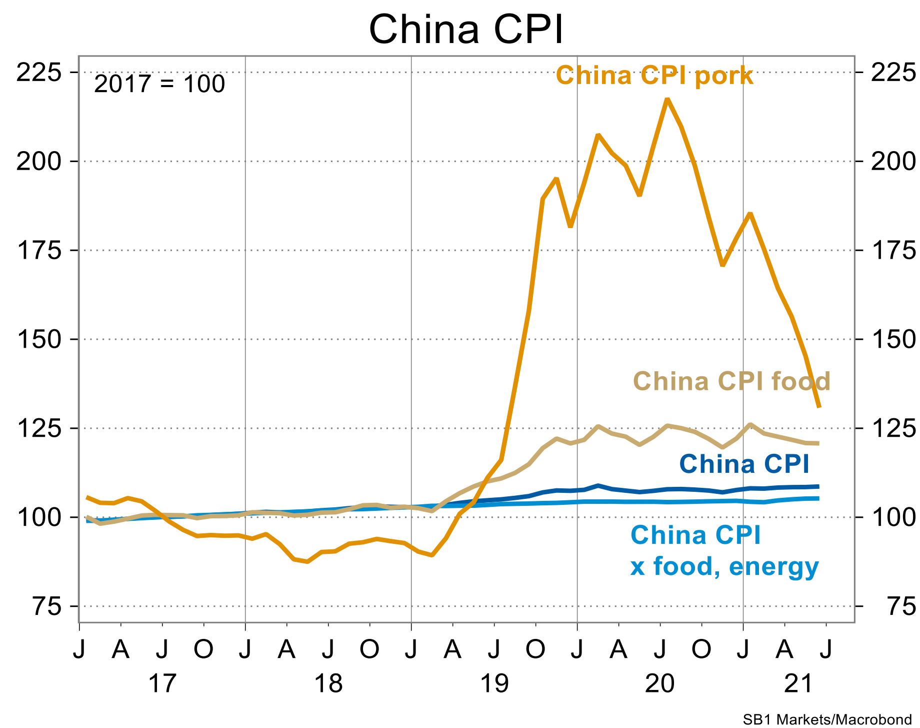


- **Total annual CPI** growth fell from above 5% in early 2020 to -0.2% in Feb. In June, CPI was at 1.1% y/y, down 0.2 pp from the previous month, expected unch.
- **Food prices** fell by 0.1% m/m as pork prices fell 10%. Food prices are down 1.7% y/y. Pork prices are falling rapidly following the doubling of prices due to the 'pig massacre' (swine flu), and prices are still up 30% vs. the level before the flu, and will probably continue to decline some more over time
- **The core, ex food & energy price index was flat** m/m, and is up 0.9% y/y. The monthly price increases were high in both March & April – and the 3m/3m rate has surged to 3%, the highest growth pace in more than 10 years
- **Inflation is up but is still low,** and supports real income growth. **Monetary policy** will not respond at low inflation per se, the real economy is more important

Pork prices down 10% m/m in June, pulling down food price inflation

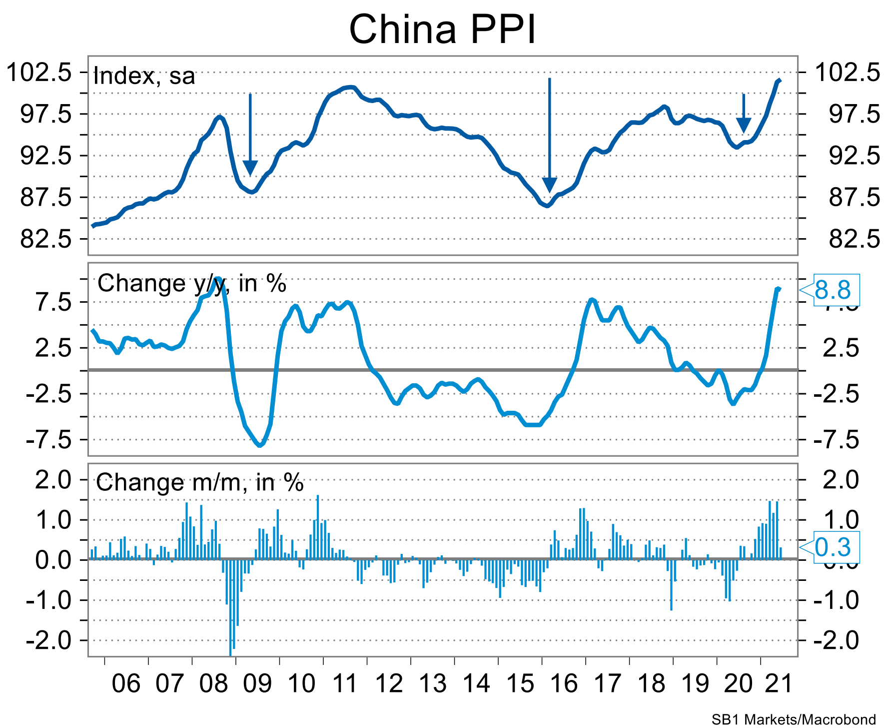
Pork prices are down 40%, but are still 30% higher than before the swine flu – probably more to go

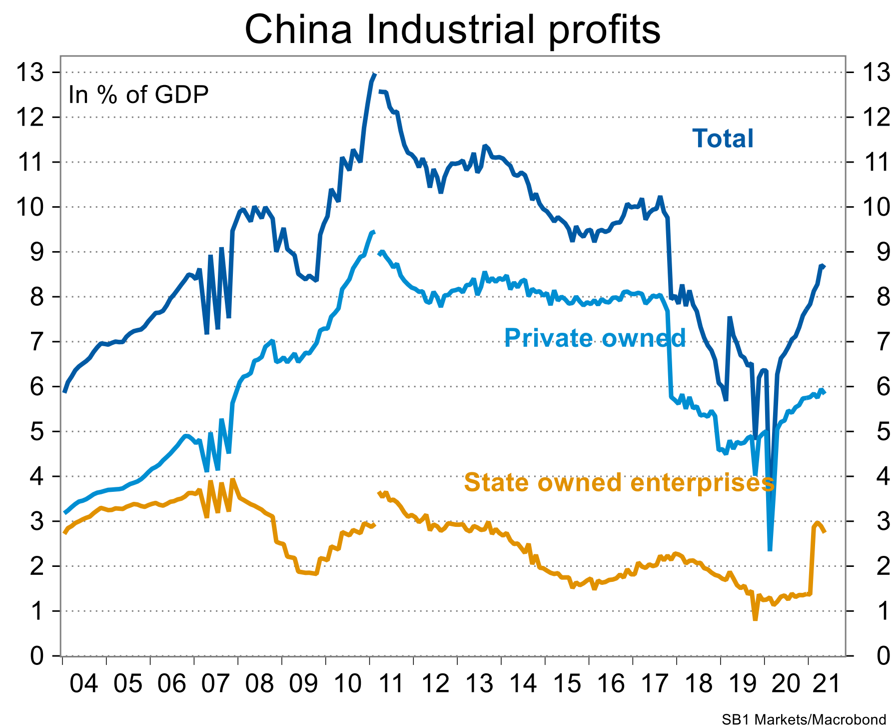




Factory gate prices are stabilising as authorities try to curb commodity prices

PPI up ‘just’ 0.3% m/m in June, up 8.8% y/y, spot on the consensus estimate

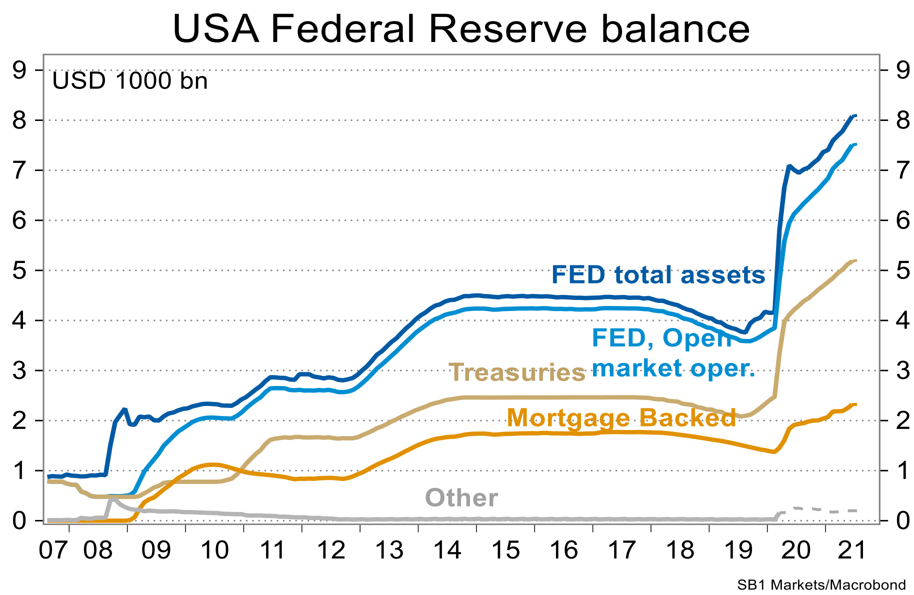




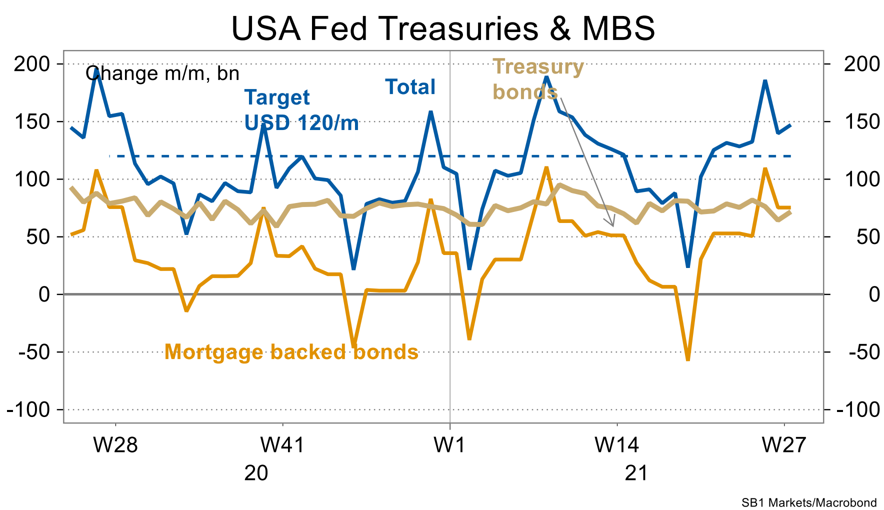
- **The rise in PPI** in the last few months can largely be contributed to an increase in commodities prices
  - » The correlation to Chinese CPI is not that strong. It is more important for other countries, check next page
- **Profits in privately owned industrial enterprises** fell by 50% in February ‘20. Profits rose to a normal level in April/May ‘20 – if we label the profit level in 2019 and early 2020 as normal – at 5% of GDP – and now it has climbed to 6%
- **Profits in state owned enterprises profits** have now come back around 3% - a level not seen since 2013 (however, there is something strange in these data…)

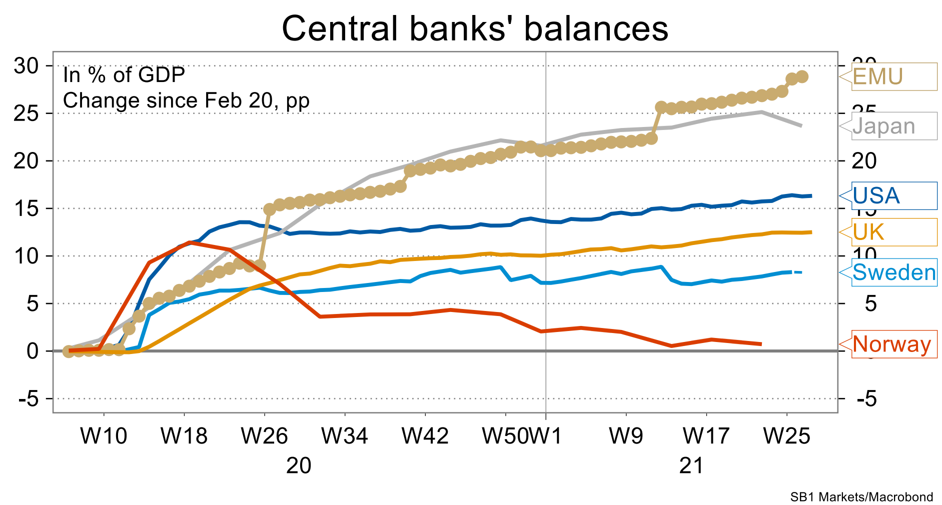
FOMC minutes: Sees progress towards target, but it's not yet substantial

Tapering is coming closer but the essence lies in the development of the labour market



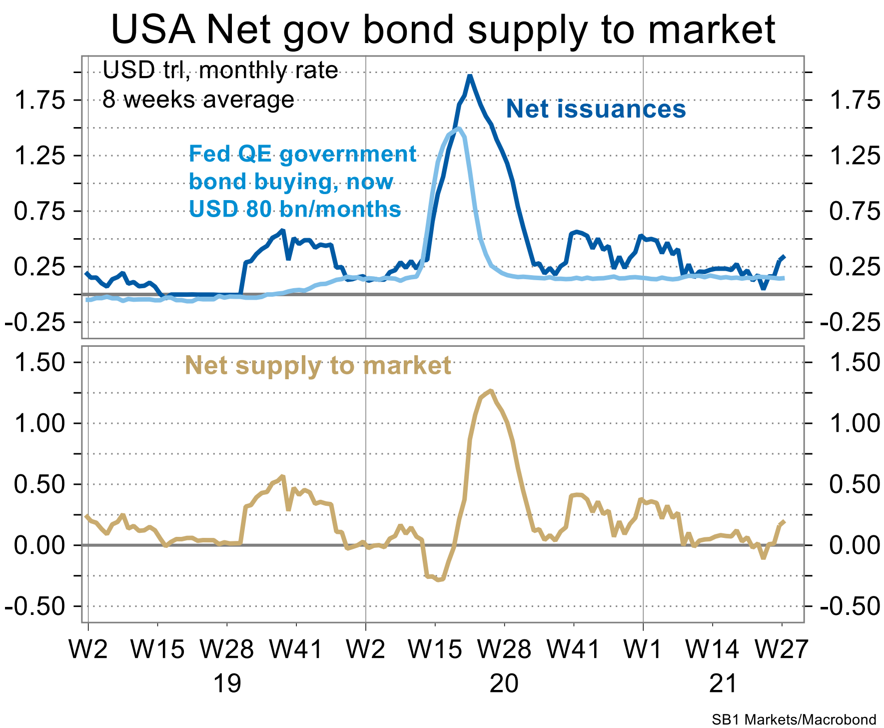
- The views among the FOMC members probably differed more than usual at the June meeting
- The minutes revealed that participants saw it as important to 'be well positioned to reduce the pace of asset purchases in response to … faster-than-anticipated progress'.
- The minutes also stated that several participants saw benefits to reducing the pace of MBS (Mortgage backed) purchases as the housing market was booming
- At the press conference after the June meeting, Powell stressed that the bank would communicate an eventual tightening well on beforehand, and that the progress towards the bank's target was not yet substantial





How much of the public debt is the Fed mopping up?

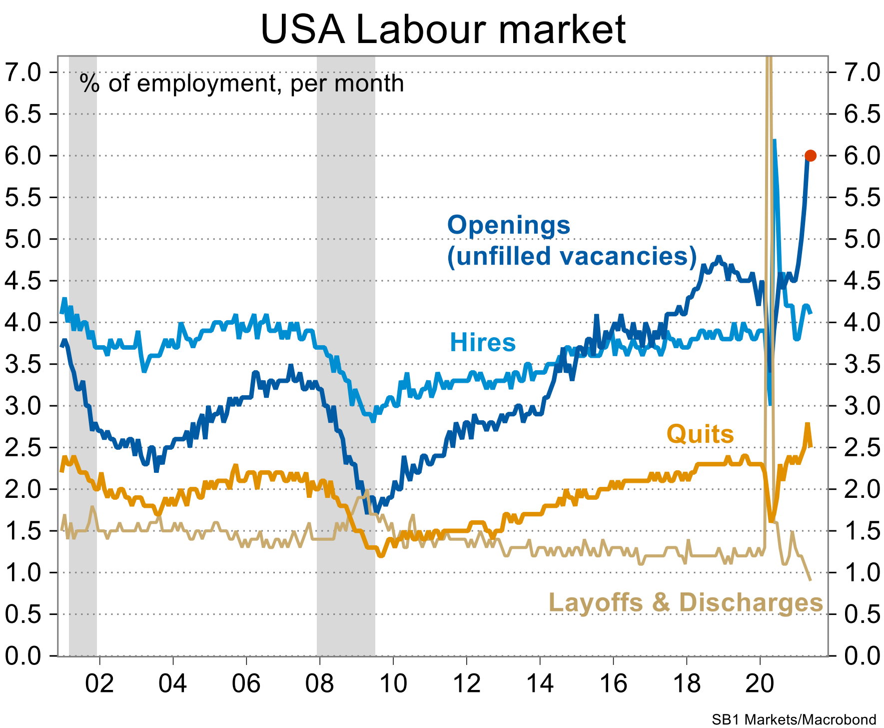
Quite a bit of it – and net extra supply has been close to zero for much of H1



- In addition, the government have until now been transferring huge amounts of money to the private sector (=the budget deficit ☺), so far in 2021 at a pace of almost USD 0.3 trl per month, creating a similar extra savings surplus in the private sector (as the current account surplus is not that much larger)
- So, even if yields are low, there are money chasing these yields, which has been of rather limited supply

The vacancy rates still the highest ever. Hiring down in May. And 'no' layoffs!

The vacancy rate unchanged at 6.0%, even if businesses are hiring at a fast pace - workers are quitting

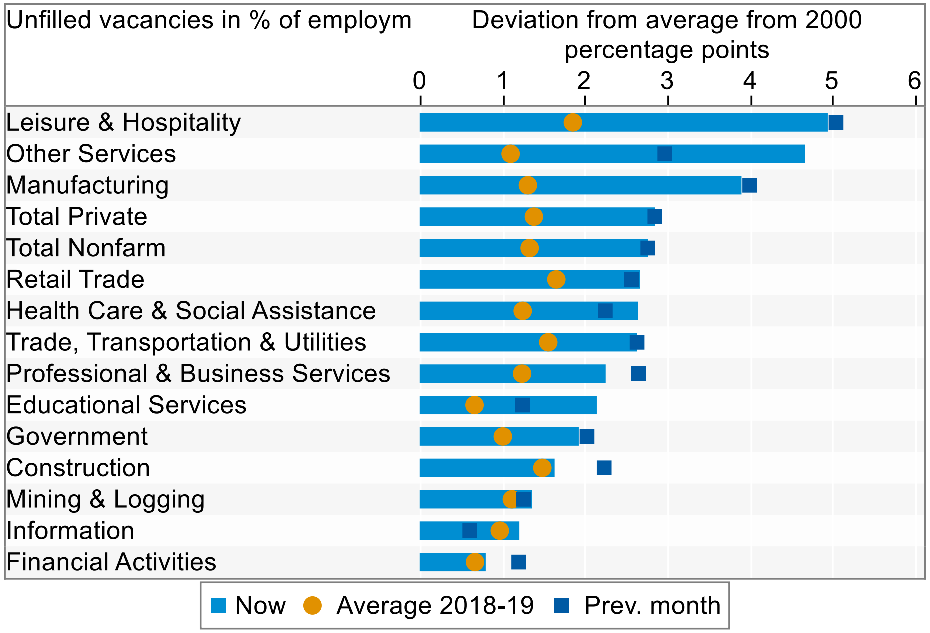


- The no. of **unfilled vacancies** was virtually unchanged from April (+16'), and is at record high, both in the actual number (9.2 mill) and in % of employment (6.0%). The highest rate before corona was 4.8%, in 2018 (and 3.5% before the financial crisis)
- **Hiring decreased** by 0.1 pp (-85') in May. However, businesses are hiring at a very rapid pace, at more than 4% per month, only beaten by the first part of the recovery last year
- The rate of **voluntary quits** decreased to 2.5% in May, from 2.8% in April. The level is still the 2nd highest ever, and a sign of a tight labour market as workers are leaving their jobs voluntarily to get at better job, which is harder in bad times. As with unfilled vacancies, quits are closely correlated to wage inflation – for obvious reasons
- **Layoffs** fell to the lowest level ever in May. Thus, it is strange that the inflow of new jobless claims remain above normal levels, check 6 pages forward
- **In sum:** The report confirms an extreme tight labour market

All sectors are reporting more vacancies than before the pandemic

The problem is largest in sectors that have been closed down, in leisure & hospitality

USA Unfilled vacancies (JOLTS job openings)

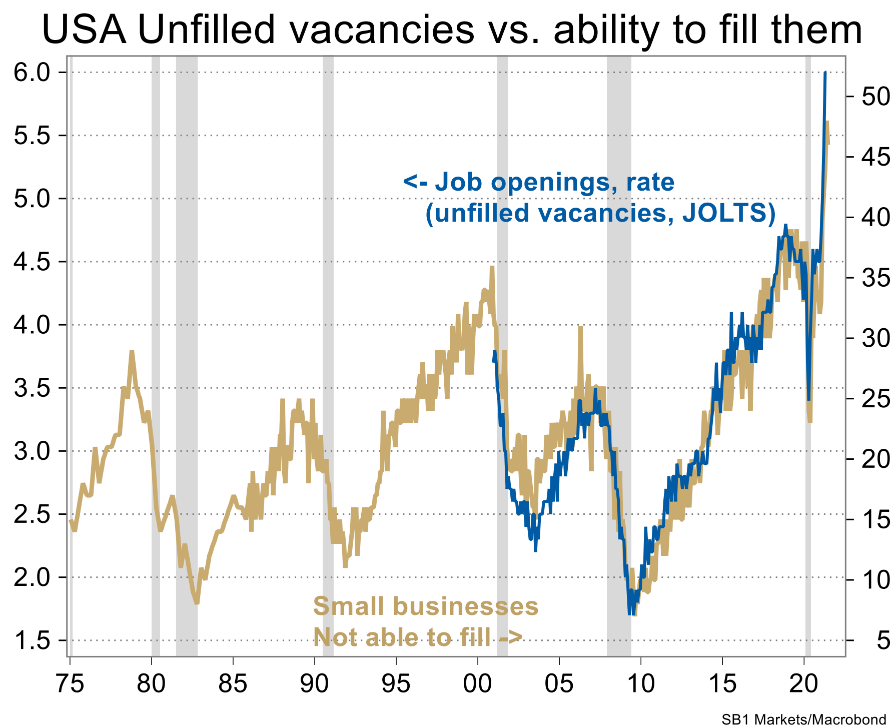


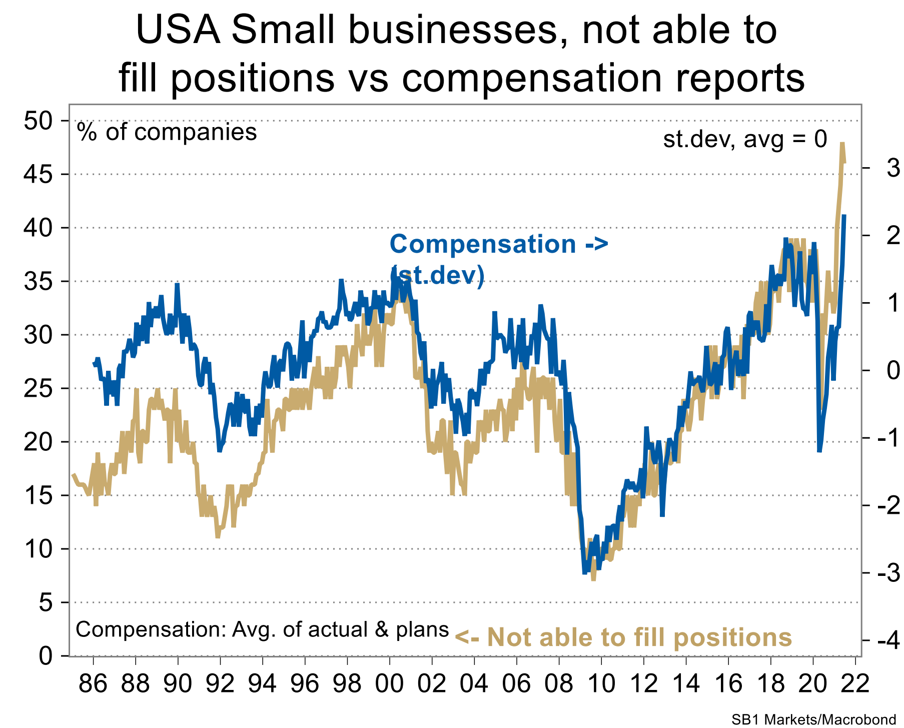
SB1 Markets/Macrobond

- … but also in manufacturing and retail trade
- Have previous active workers
  - » Left the labour market temporary, due to corona?
  - » Left these low paid sectors for better jobs elsewhere?
  - » Or are they staying outside the labour market because unemployment benefits are too generous due to the temporary USD 300/week extra federal support?
  - » .. Or have too many just left the labour market??
- Surveys indicate that a large proportion of workers that have been laid off are not planning to return to the same sector. Will they be absorbed in other parts of the economy?
- In addition, many workers state whey want teleworking permanently
- Both locally and regionally the pandemic may have created new mismatches in the labour market

Official vacancy data confirm NFIB survey data (almost perfectly)

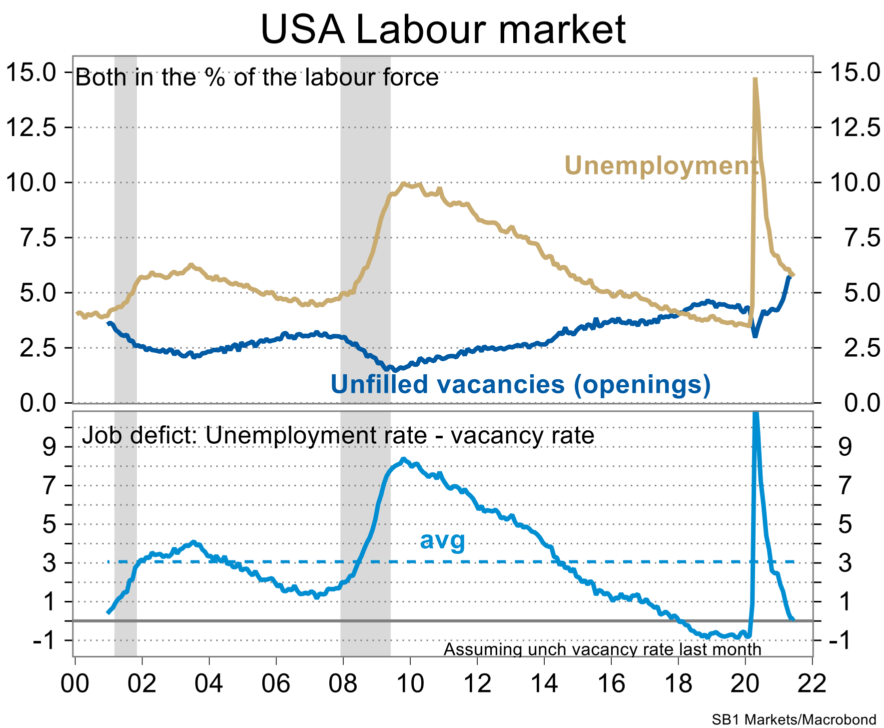
.. And we have never seen anything like this before. The correlation to wage inflation is <u>close</u>

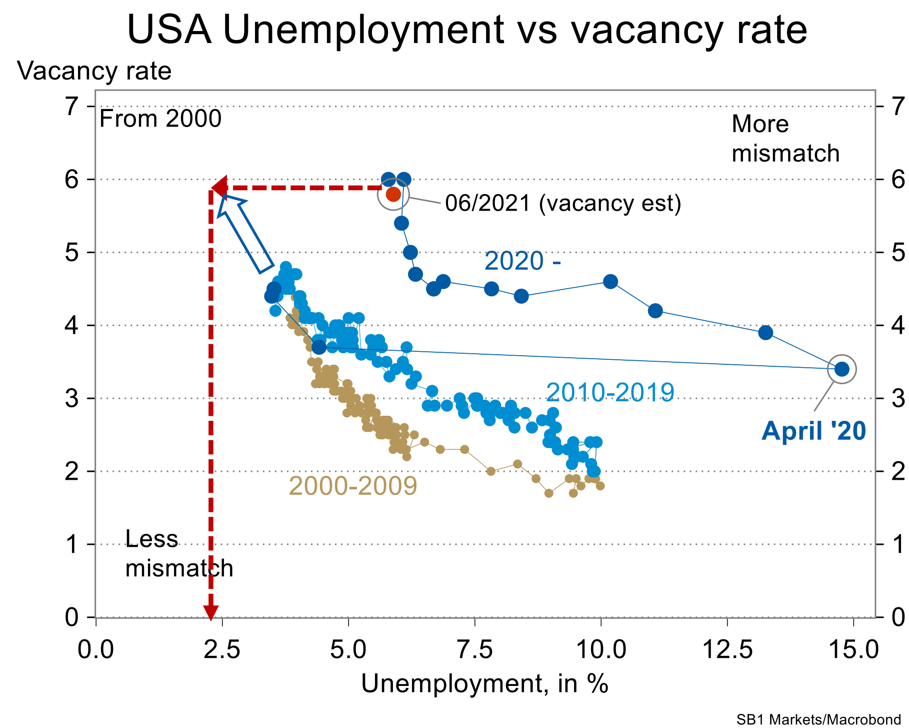




Such a high level of vacancies would normally signal a record low unempl. rate

… as if unemployment was below 3%. However it is still 5.9% - a huge shift in the 'Beverage' curve

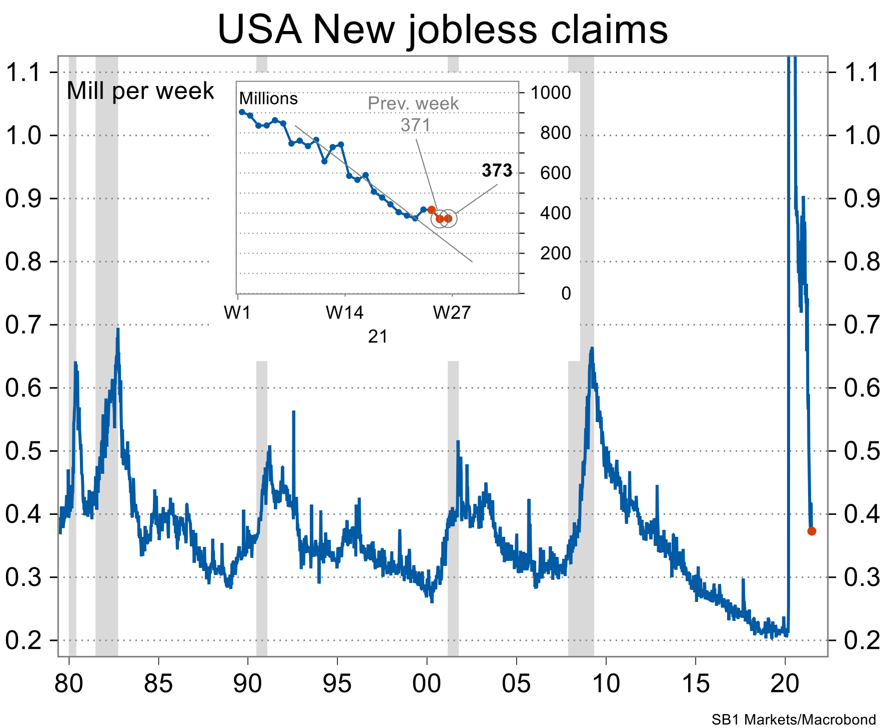


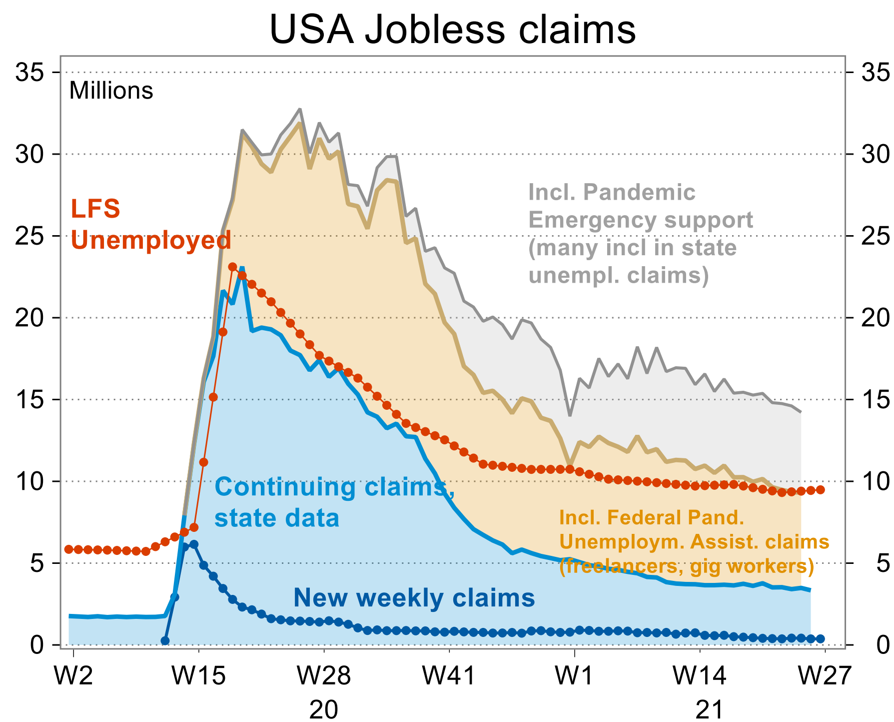


- **It is a permanent downward shift in labour supply** – a huge increase in mismatch in the labour market or that many workers now prefer to stay outside the labour market. If so, a 'disaster' – wage growth will accelerate sharply, inflation will be more than transitory & the Fed will have to respond. If the Fed does not respond, another disaster in the waiting, and a more abrupt and dramatic shift in policy will be needed at a later stage
- **Or it just at temporary sweet/sour spot:** 1% of the working age population can not work due to Covid-10 (school children, own health etc, they say) and another 3% – 4% are receiving extraordinary unemployment benefits, more than those that would normally have received such benefits. At least he latter group will have no income if they do not turn up in the labour market during the coming months, as these support programs will end now (in some states) or in September (everywhere)

New jobless claims are stagnating – claims marginally up last week

New claims rose by 2’ to 373’ (previous week’s no. was also revised up by 7’), expected 350’

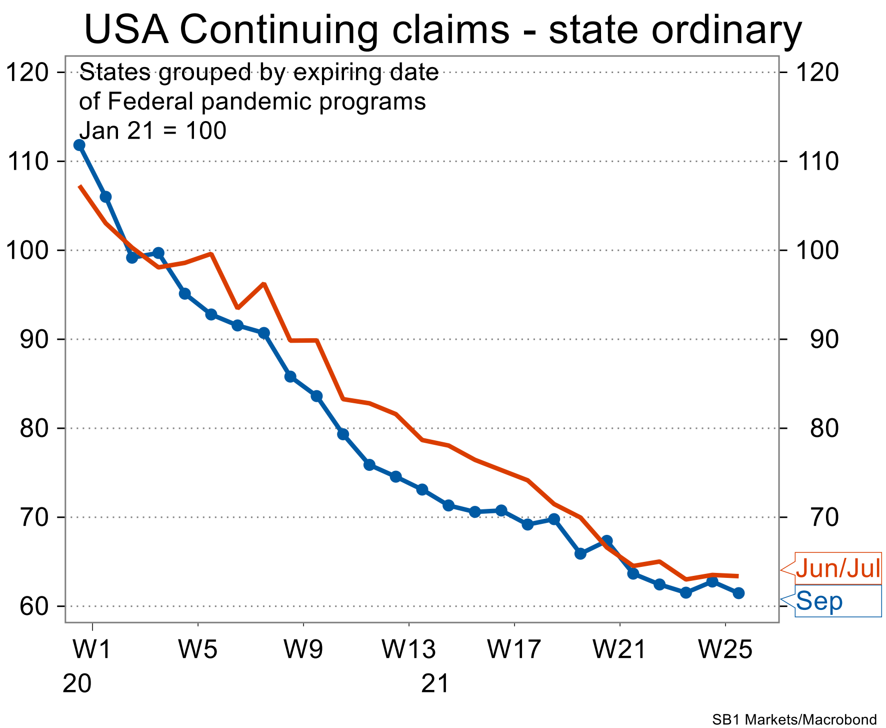




- **New claims** rose to 373’ from 371’ (revised up from 364’) the previous week, expected down to 350’. Over the four previous weeks, claims have been much higher than we and the market had expected, despite the rapid improvement in the economy – 5 weeks ago, just 375’ asked for a new benefit, and had the trend been intact, the weekly inflow should have been below 260’ by now. We know that businesses are saying that it is hard to find the right people, but with so many people out of work, the stickiness of the labour market is greater than we had anticipated
- **Ordinary continuing claims** increased by 54’ to 3.26 mill, while the no. of receivers of the Pandemic Emergency Support Program (52 weeks instead of 26, and USD 300 extra/week) decreased by 354’ to 4.9 mill, and the no. of receivers of the Pandemic Assistance Program (gig & freelancers) fell by 111’ to 5.8 mill. The coming weeks these programs will be sharply reduced as at least 24 states have opted out (see more next page)

Will the cancelling of pandemic federal benefit programs lift employment?

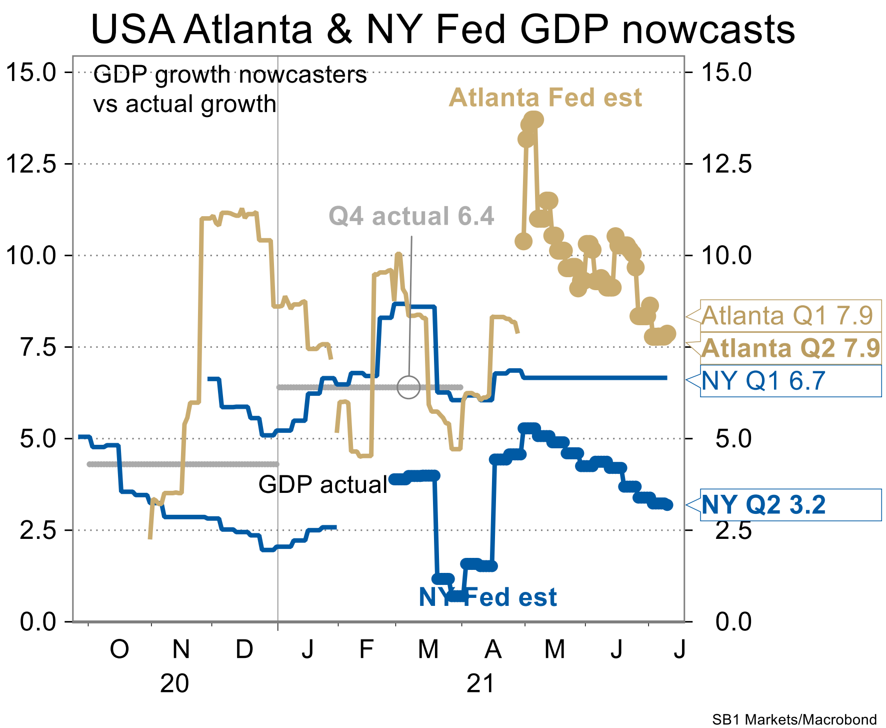
No clear message yet – but state data are volatile

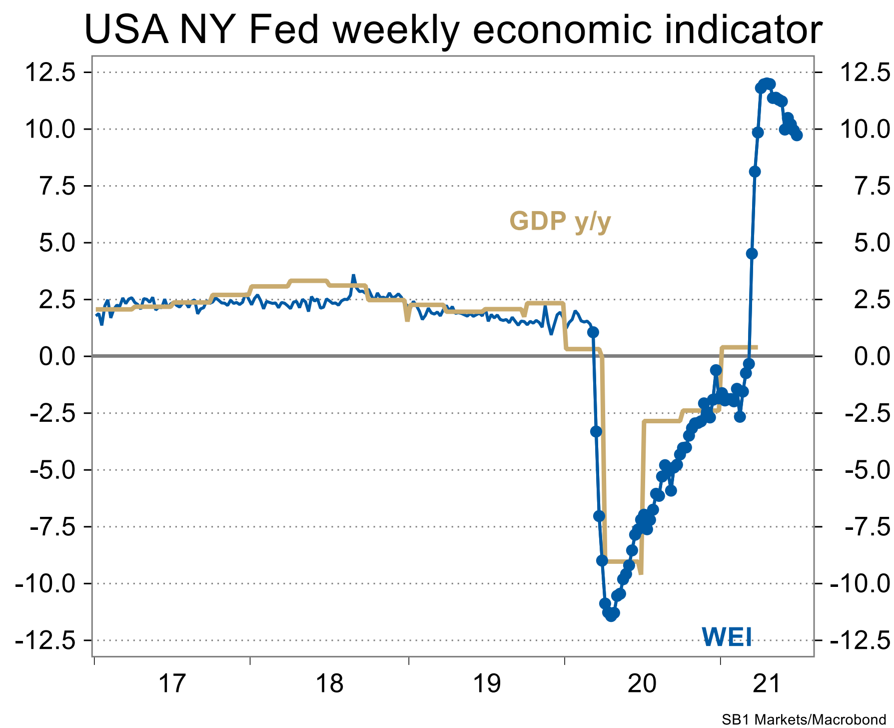


- 4 states dropped out of the federal unemployment benefit programs on June 12 (end of week 23), 8 states left June 19, and 10 states June 26 - which is the last week state unemployment benefit data are available
- We do not know what these former recipients do now – are they now trying to find a job?
- Some media reports suggest that employers in these states have been able to find more workers, but other reports have told other stories
- If we pool the 'early leavers' in one group, we have not yet seen a reduction in the no. of recipients of ordinary state benefits among these states
- Most likely, we will have to wait for state employment data, which are published 2 – 3 weeks after the national payrolls report
  - » We doubt we will find much information in the June state employment data (date are gathered mid-month), but July data (published in August) could reveal some information whether labour supply increases or not. We think the odds of finding some impact are pretty good, if not already in July employment data

The nowcasters signal 3% to 8% GDP growth in Q2

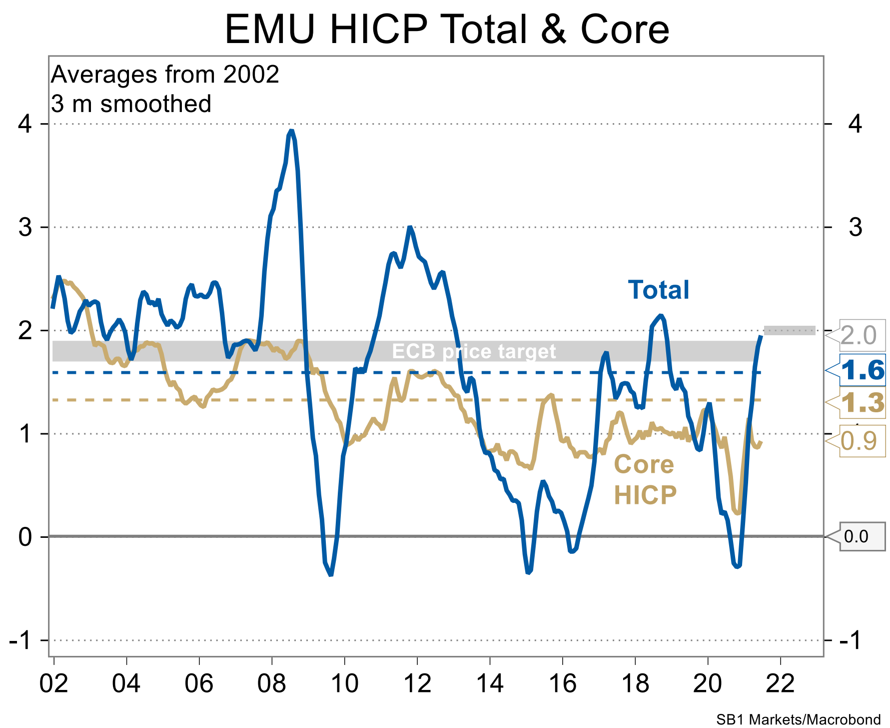
… as growth nowcasts have been gradually slashed past two months





ECB's new strategy: A 2% symmetric inflation target, clearly above the current

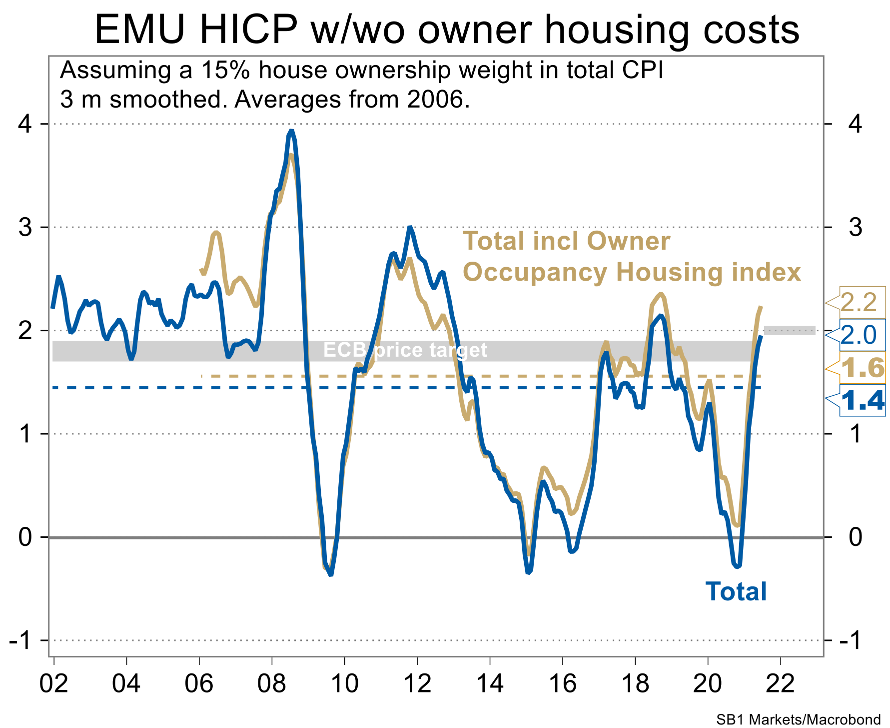
…but now includes house prices



- **As has been widely communicated, the ECB lifted its inflation target** to symmetric around 2% from 'below but close to 2%', signalling somewhat larger tolerance for inflation (at least vs. the old Bundesbank line). A symmetric 2% has been the norm for most central banks.
  - » The Federal Reserve US has moved further to an average inflation target, but even the ECB will tolerate transitory periods with inflation above 2% if needed to reduced the risk for entering a disinflationary trap
- On the other hand (also well prewarned), the ECB will in one way or another **include owner-occupied housing costs** (OOH) in the targeted inflation measure. The ECB asks Eurostat to include a measure of the OOH in the HIPC (the EMU CPI). Until now, most of OOH has been excluded from the 'CPI' in EMU. It will probably take some time for Eurostat to implement this change (which is rather complicated). However, the bank will start taking housing costs into account when assessing if the inflation target is met from now on - see more next page
- The 3rd change: ECB will focus more on **implications of financial imbalances** rather than inflation implications of monetary developments as the latter has turned to be a complicated science. Again, a Bundesbank pillar is buried (perhaps just before the BuBa approach could be vindicated, at least in the US…)

ECBs preferred owner-occupied housing index does not change that much

… but inflation would have been 0.2 pp higher on average – and above the NEW target now

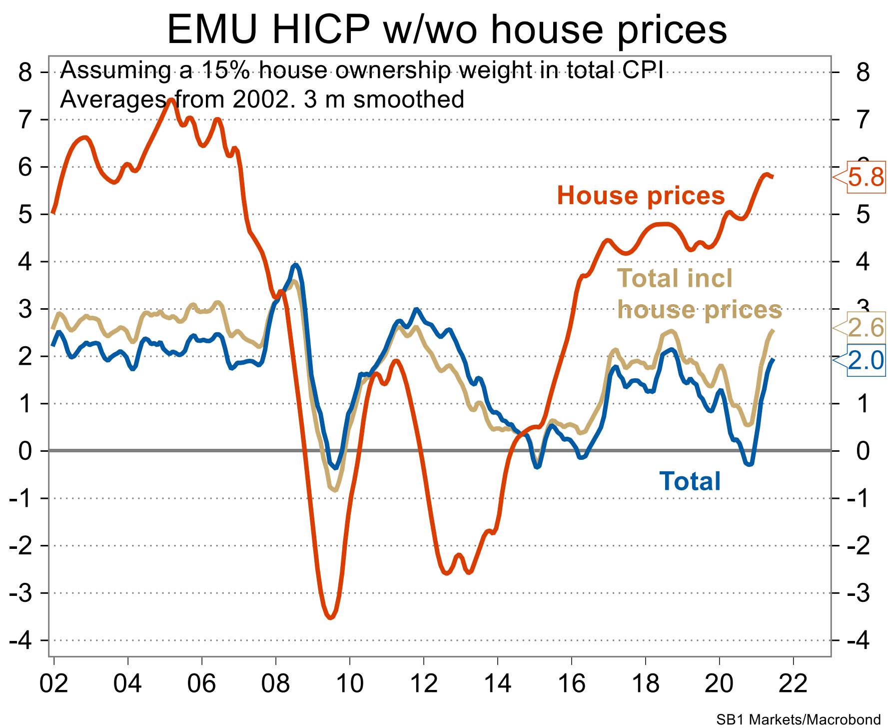


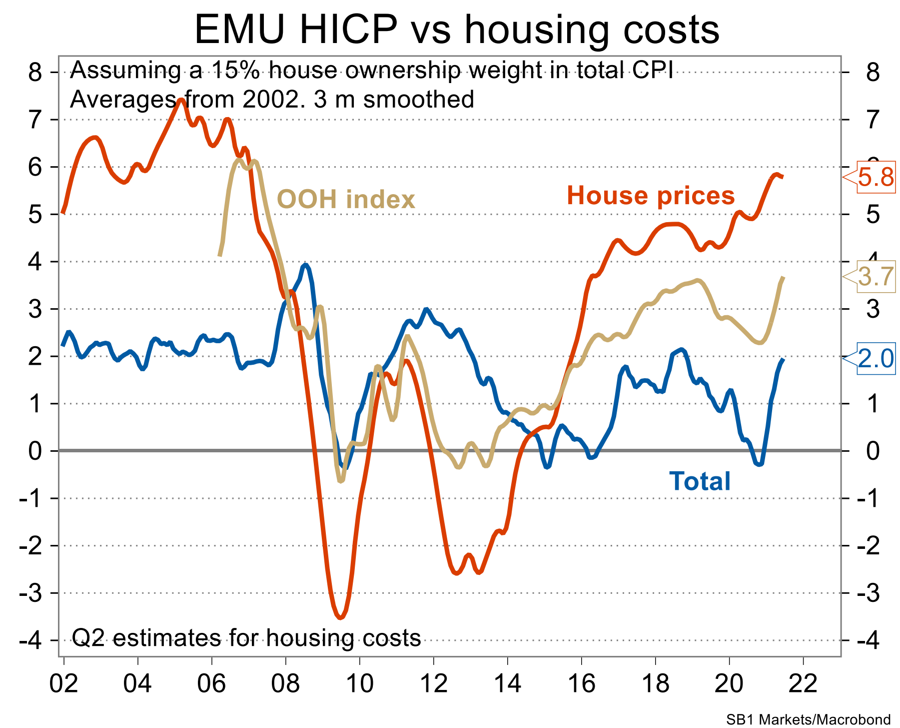
- On average, inclusion of the current Eurostat experimental quarterly total OOH, would have lifted average HICP by 0.2 pp per year the past 15 years – and now 'total' inflation to slightly above 2% vs the 'official' index at just below 2%. *See more next page*

- There are several alternatives for including owner-occupancy housing costs (OOH) in consumer price indices
  - » A **rental equivalent** is most common, as it is done in the US and Norway and several other countries, owners are assumed to pay (to themselves) the same rent as renters pay
  - » A **net acquisition approach** usually just include construction costs for new homes, and not the cost of land
  - » A **user cost approach**, where 2nd hand prices are the main element but where depreciation, real interest rates and expected capital gains are included are preferred by many economists. However, both a volatile real interest rate and an uncertain expected capital gains element complicates calculations (like if expected capital gains are high, the ownership cost is negative). A possibility is keeping capital gains out of the calculation, or assuming a stable relationship between (long term smoothed) real rates and expected real capital gains, implying the new and existing home prices
- The ECB has signalled that it prefers the net acquisition approach, implying that just new home construction costs (and not the cost of land) should be included in the index (alongside maintenance, renovation etc). The current Eurostat's experimental OOH index includes the cost of land (as far as we understand). However, some statements from ECB officials could be interpreted as if cost of land should be included, even 2nd hand house prices
- The Eurostat is assumed to spend some years figuring out how to include a OOH measure in the HICP (or construct an HICP-H index). In between time, the ECB will include some OOH-measures in the bank's assessment of price 'stability' - which may influence monetary policy, at least at the margin
- On average, we assume including OOH, measured by house prices, would have lifted average HICP by 0.2 – 0.3 pp per year the past 20 years – and now 'total' inflation is well above 2%. *See more next page*

Will a 'narrow' OOH index solve the 'problem'?

The current owner-occupancy housing index is correlated to exisisting home prices, but less volatile

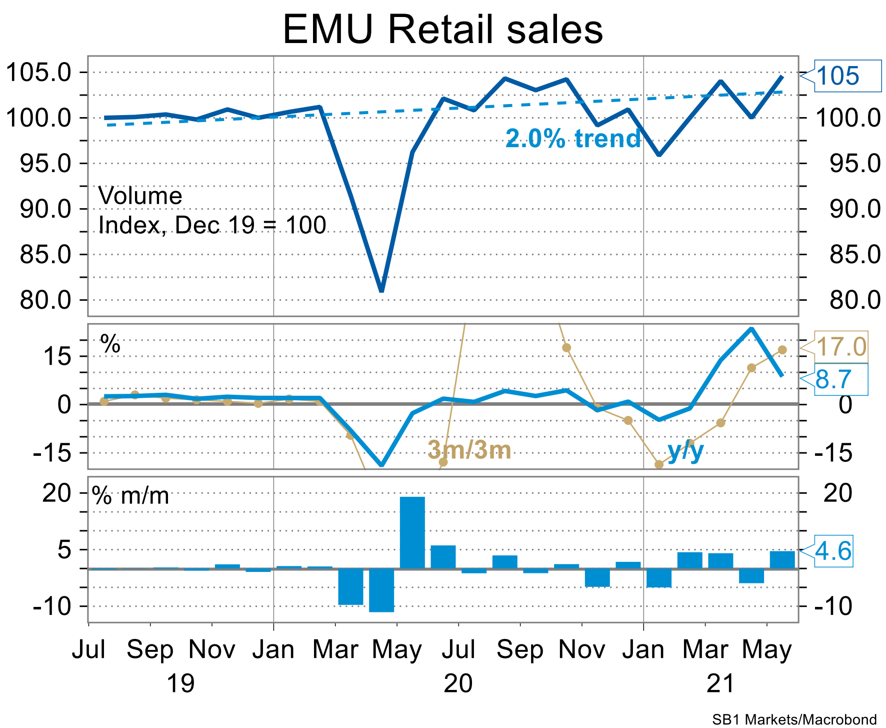


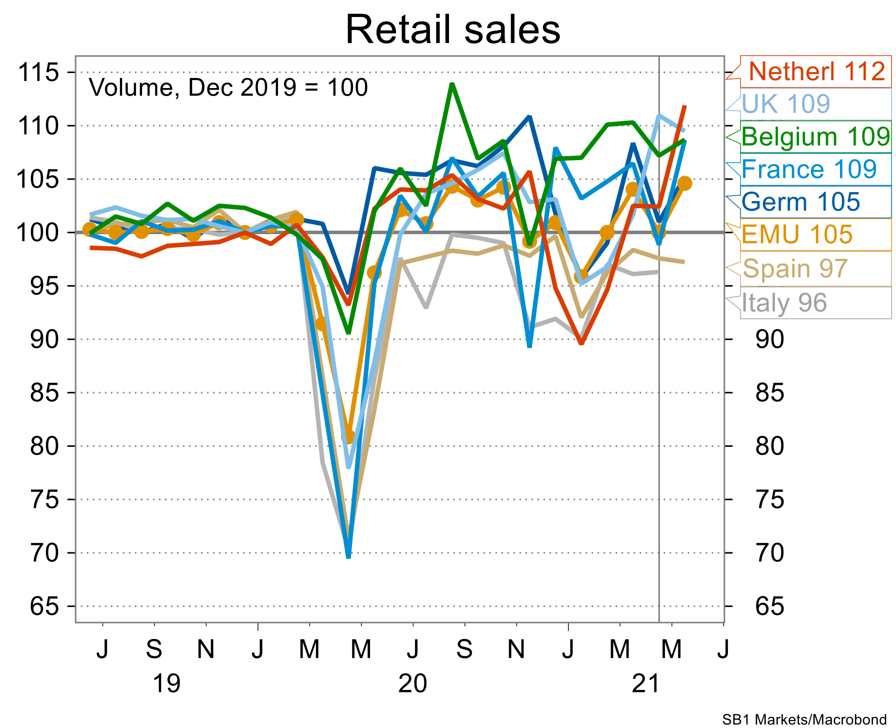


- It is not written in stone whether a monetary policy aiming to stabilise 'pure consumer prices' or an index including house prices is best suited to 'stabilise' the purchasing power of money or the economy – and neither politicians, central bankers nor economists agree
  - » Our stance has over the past 25 years been tilted towards Leaning Against the Wind-strategy, where asset prices have to be taken into account when conducting monetary policy, both on the way up and on the way down, if these asset prices influence economic activity, and long term economic & financial stability
  - » People feel – and act – as though inflation is high – and real interest rates low, when house prices increase – and vice a versa
- Thus, a more narrow OOH, excluding land cost, may not meet the criticism against the current EMU HICP consumer price measure, which exclude much of the housing cost
- A broader representation of housing in the 'CPI' would have lifted 'real' inflation further in the EMU. In other countries the impact would have been even larger, both at the downside, and even more at the upside. (BTW, the large discrepancy in house price developments between EMU countries will pose a challenge to the ECB, if price developments continue to differ)

Eurozone retail sales sharply up in May – and probably more to go

Retail sales up 4.6% m/m in May. Sales now 5% above pre-Covid level

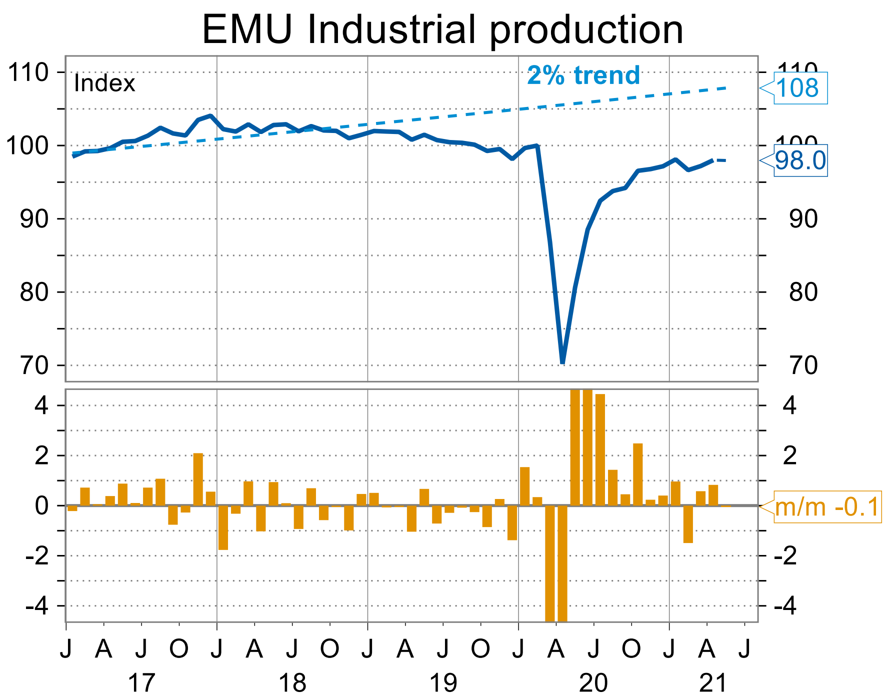


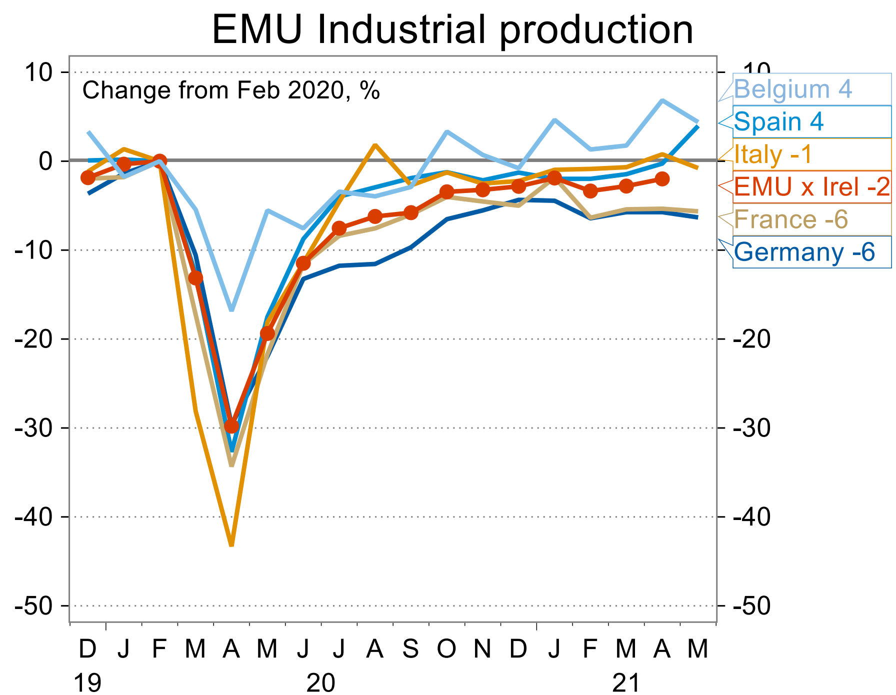


- Sales rose sharply in most EMU countries in May – except for Spain (which did not receive the normal inflow of tourists that always lifts sales in the summer season (not seasonally adjusted). Italy has not yet reported. Sales in the UK were also down, but still at a high level

June another lost month: Industrial production close to flat in June

Production is still 2% below the pre-pandemic level

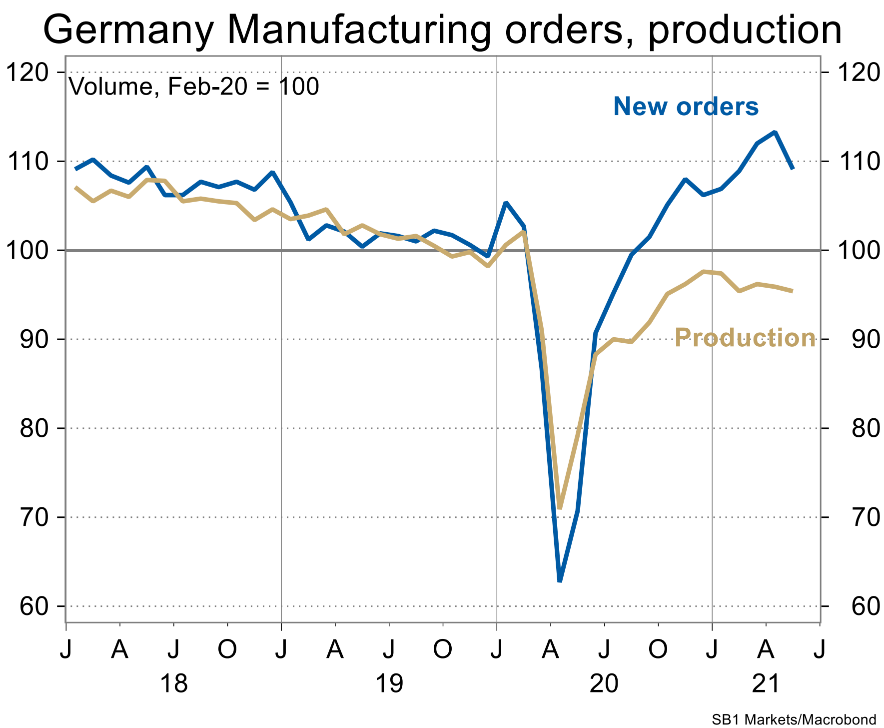




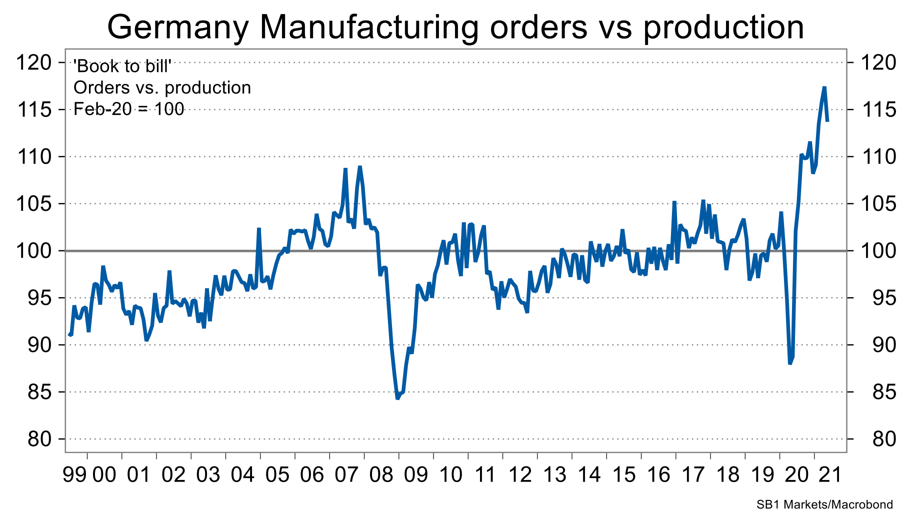
- **Industrial production** was probably close to unch. in June, well below our expectations, as both Germany, France & Italy (and Belgium) reported small declines, while Spain reported a sharp lift
- Auto production very likely contributed substantially on the downside in May
- **Order inflow** indicates higher production the coming months
- **Surveys** are also signalling strong growth the coming months (if put goods are delivered, we suppose)

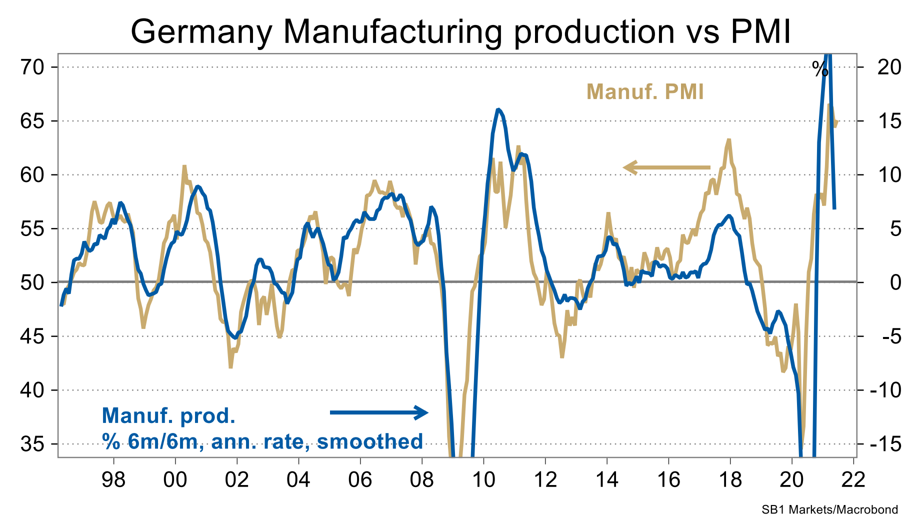
German production to turn up soon?

Orders, surveys suggest so



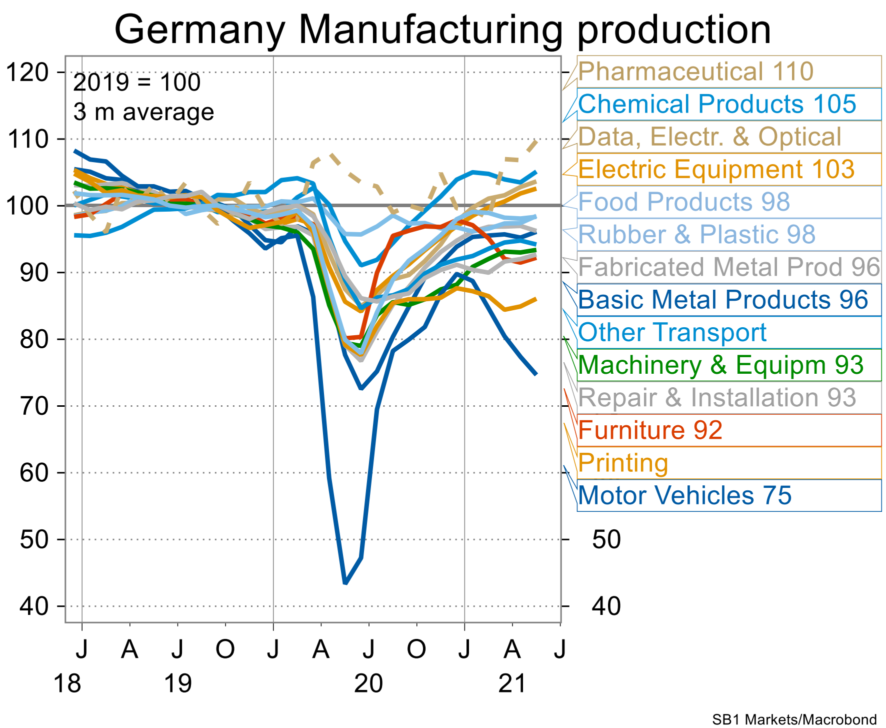
- **German manufacturing orders** fell 3.7% in May, expected up 1.1% but April was revised 1.4% upwards - and the level is 9% above the pre-pandemic level
- **German manufacturing production decreased** by 0.5% in May, expected up 0.5% (but April was revised up by 0.7%). The level is still 4% below the Feb-20 level
  - » This discrepancy is unusual, to put it mildly
  - » Surveys confirm strong growth in order inflow – and hopefully in activity (even in longer delivery times are a major challenge, here too)





Mixed among manufacturers but most are below the pre-pandemic line

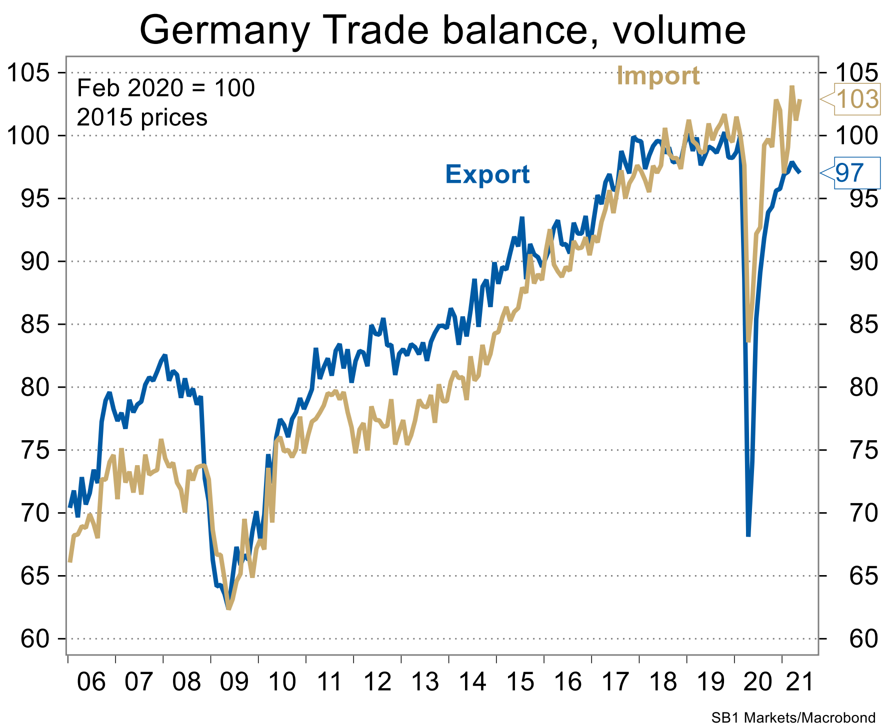
Vehicle production is struggling but not due to lack of demand

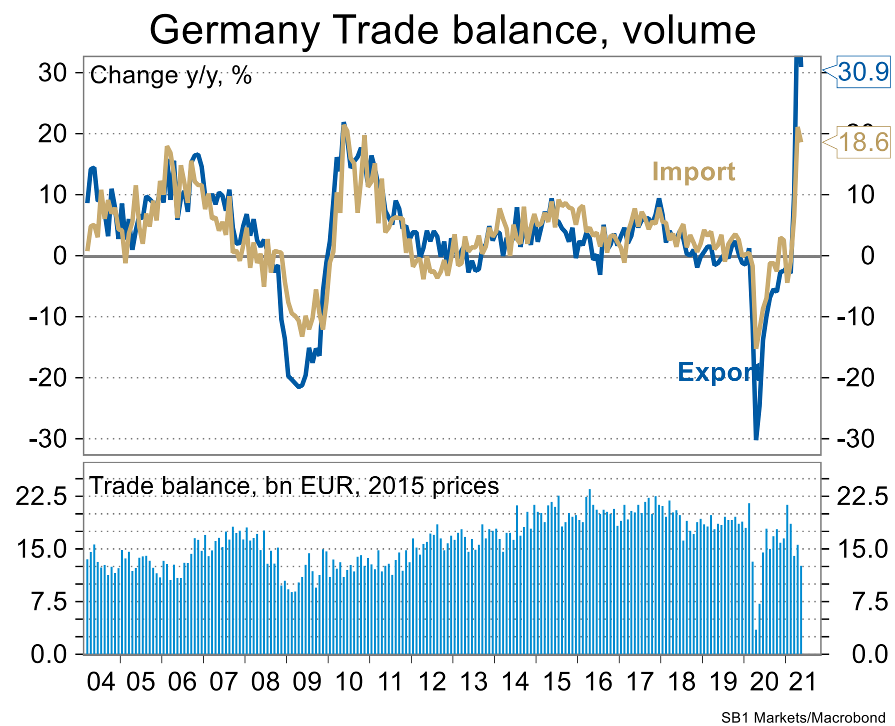


- However, several other sectors are still operating at rather low levels, and just some few are back at reasonable normal levels

Exports increased by 0.3% in May – still 3% below the pre-Covid level

Imports were up 3.4% - and back to a pre-pandemic (2018 – 19) trend growth path

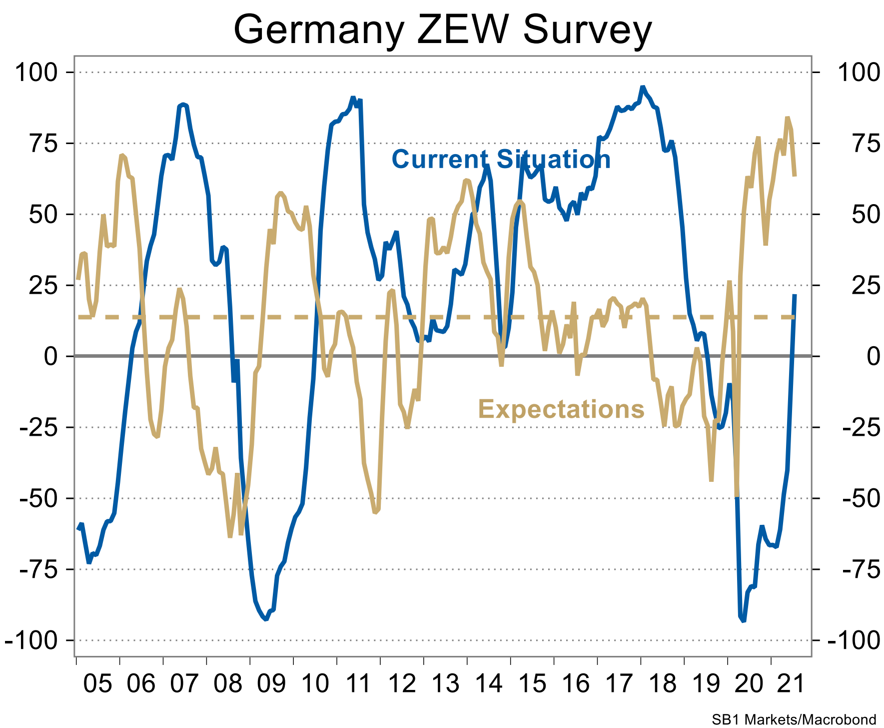


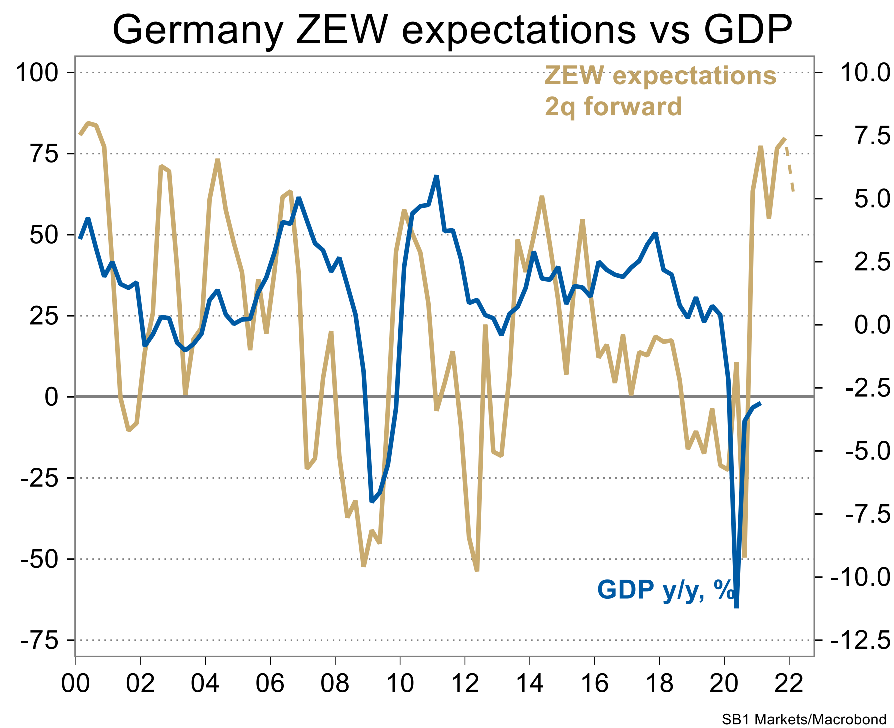


- Export volumes rose 0.3% m/m in May, imports up 3.4%
- The German trade surplus shrank rapidly during the corona crisis in the spring, to the lowest levels in 20 years. Since August, the surplus has been almost back to normal. The surplus is May was EUR 12.6 bn, whereas the average before the pandemic was approx. EUR 19 bn/ month (seas. adj.)

ZEW analyst/investor sentiment fell down in July, still extremely high

– signals very strong GDP growth

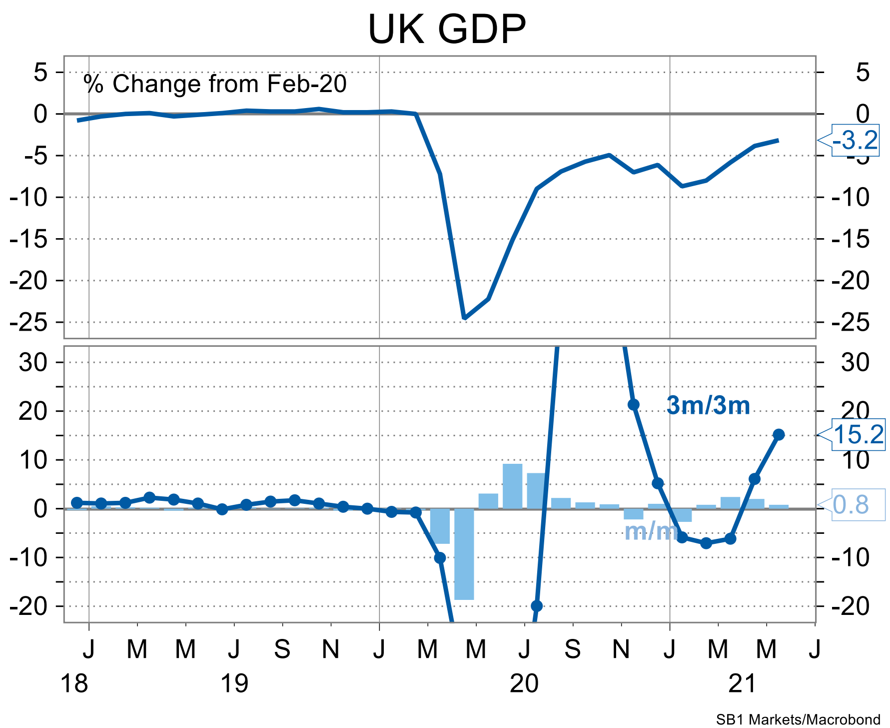


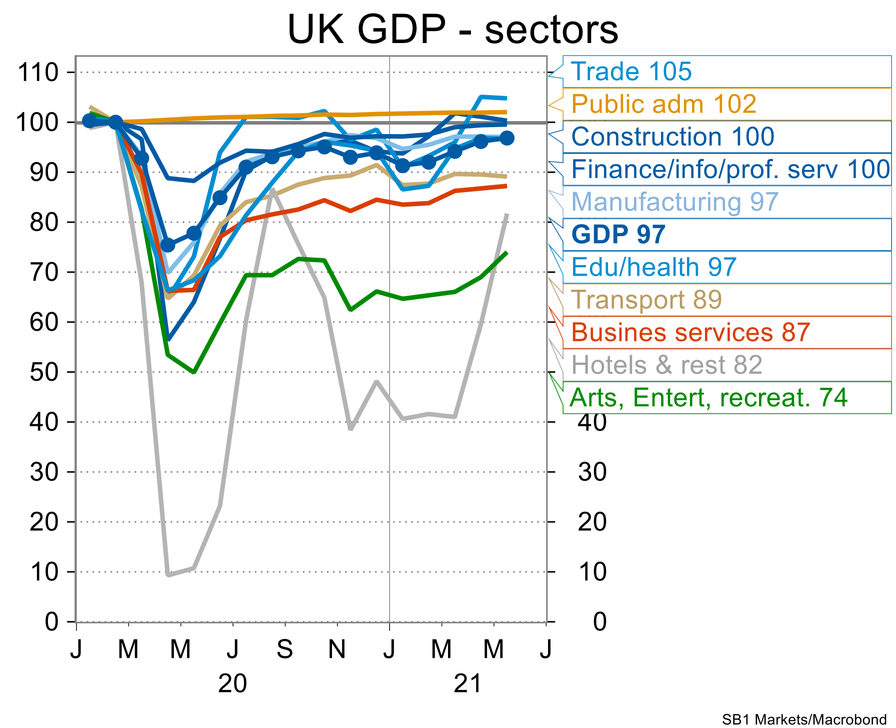


- The ZEW expectation index fell 16.5 p to 63.3 in July, expected down to 75.2. The index is 1.1 st.dev above average, and still close to the best prints the past 20 years – check the chart above!
  - Thus, investors and analysts are just pretty sure that the economy recover sharply the coming months. Which is reasonable
- Assessment of current situation sharply improved in July (up 30.4 p), as more restrictions have been lifted and vaccinations are increasing. The level is now above average. During the next months the gap between the two components should narrowed substantially, mostly from the downside

UK GDP grew by just 0.8% m/m in May, April revised down

Still, the recovery is still on track





- **The recovery in GDP** is still on track – but at a slower pace than expected. May was 1.3% lower than expected, and GDP was still 3.2% below the pre-pandemic level
- **Services** rose just 0.9% m/m, even if **hotels & restaurants** were up 37%, and **culture/entertainment** rose 7%. These two sectors are still down 20 – 25%, and will very likely contribute on the upside the coming months – if the Delta variant does not create too much problems
- **Manufacturing, construction, and professional services** declined further in May

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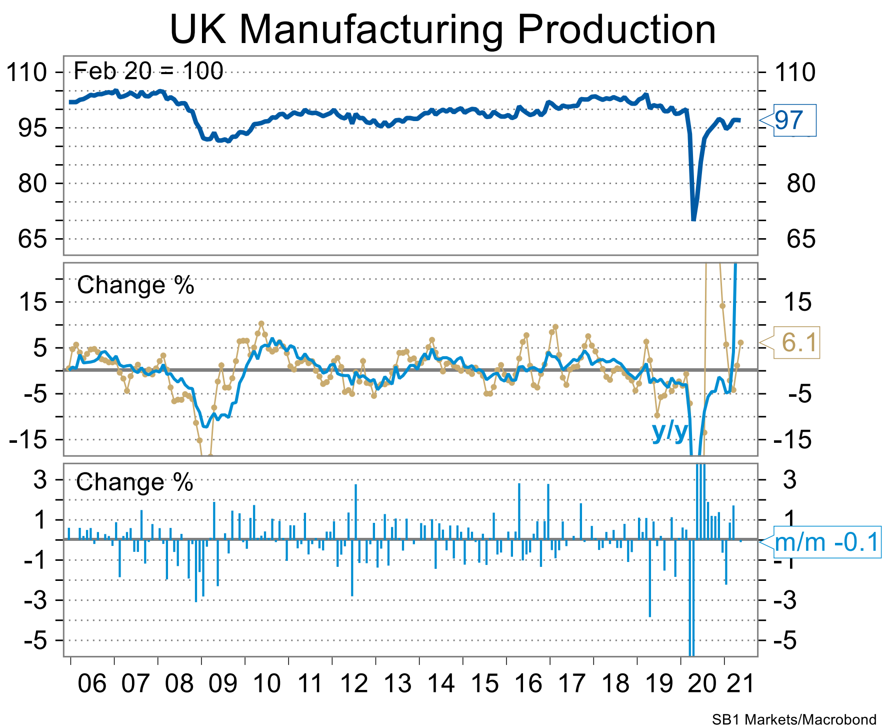
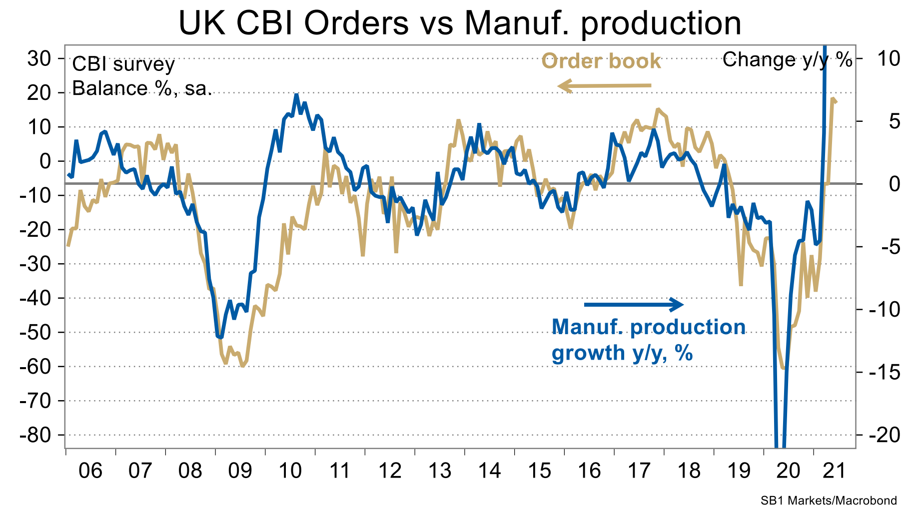
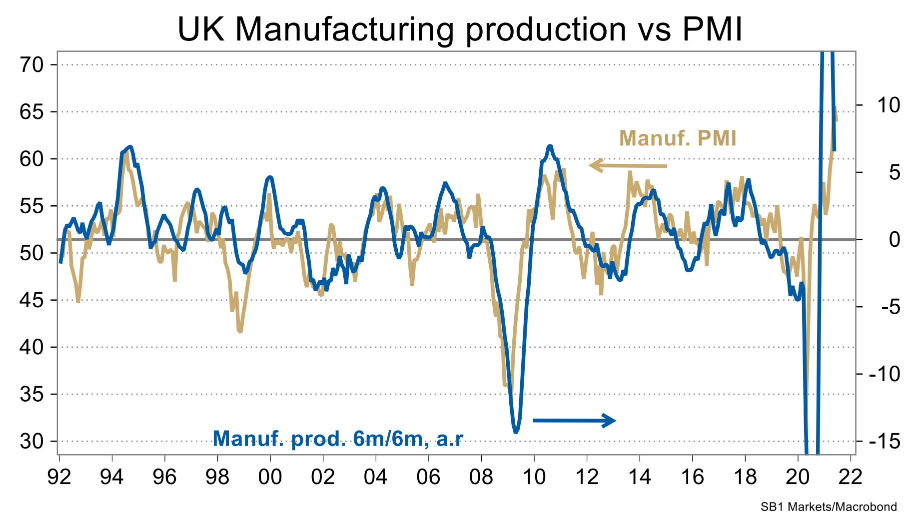
Auto production put a brake on manufacturing in May, contributed by -3,2 pp

… while total production just fell by 0.1% (expected +0.9%). Other sectors sharply in plus



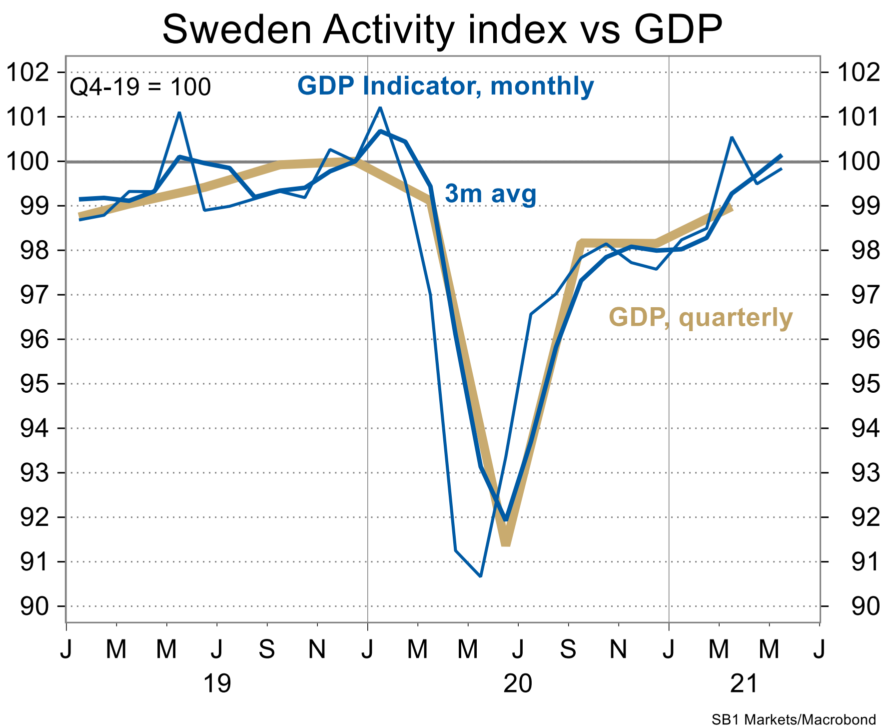


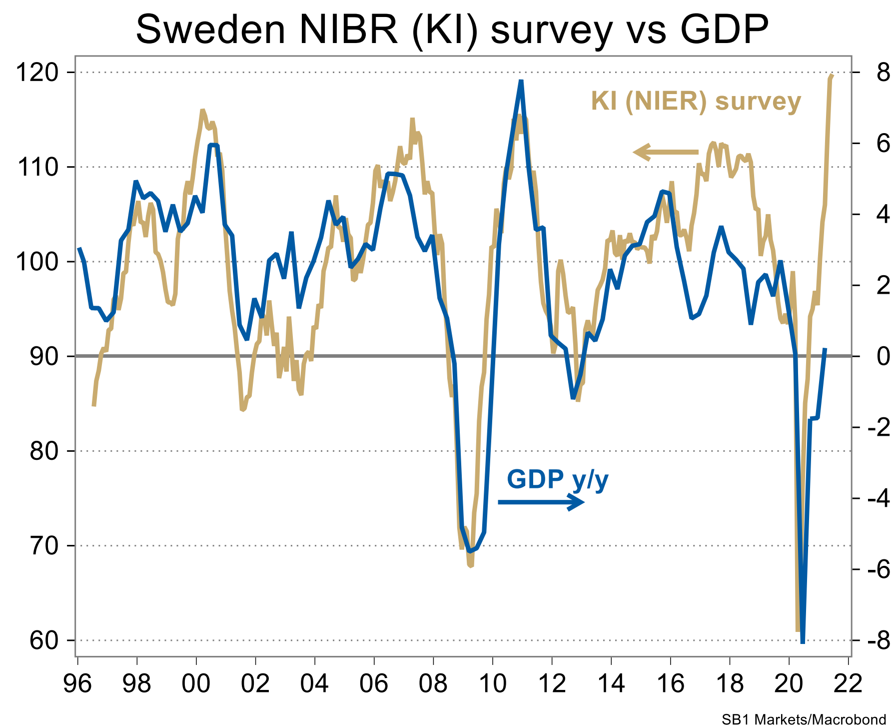


- Ex. transport, production rose sharply, with pharma in the lead
- Manufacturing production is still 2.5% below the pre-pandemic level
- On a the bright side: PMIs and other surveys are at the best levels ever – and signalling terrific growth the coming months. If businesses have enough materials, labour of course…

GDP up 0.4% in May, the level back at the pre-pandemic level

GDP probably rose less than expected but the decline in April was revised down to -1.0%, from -1.4%

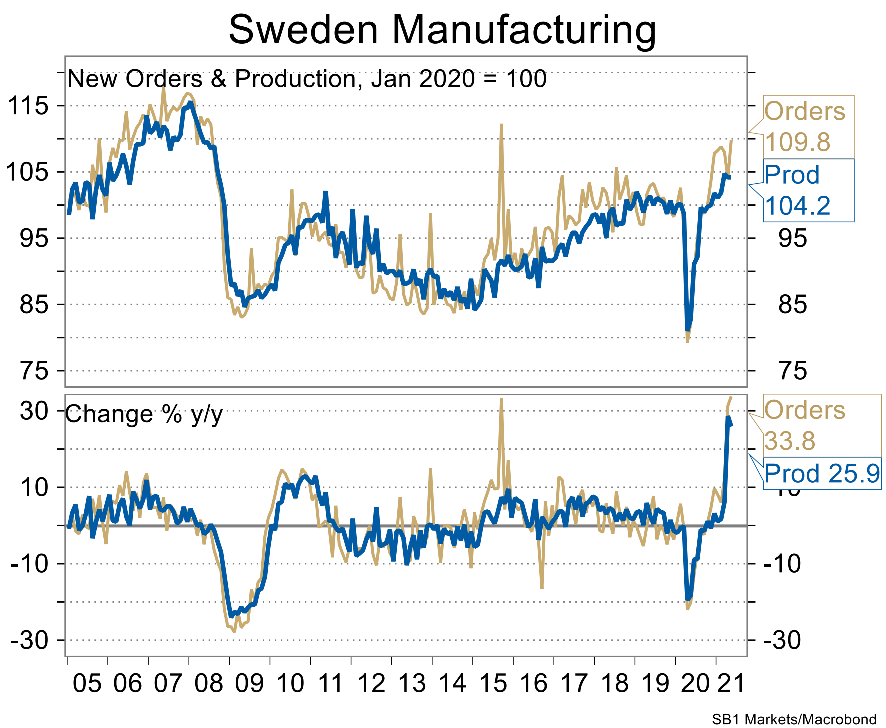


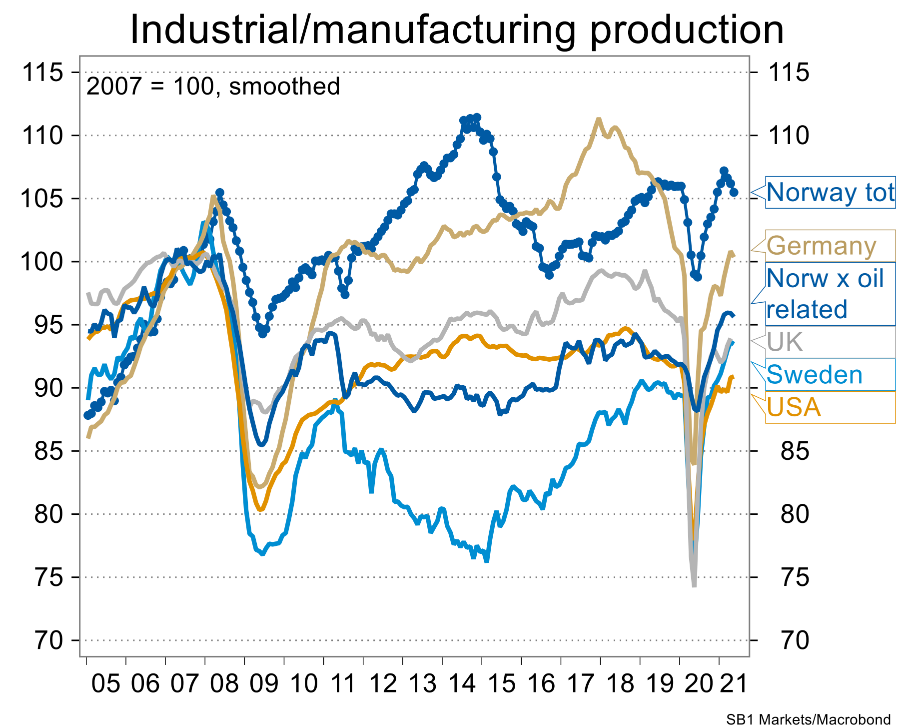


- **Q1 GDP** grew by 0.8% according to the last publication (the first estimate was 1.1%) but monthly data signal a slightly higher growth rate
- In Q2, GDP is on track for 1% gain, bringing activity back up to the same level as before the pandemic. Still, GDP will be some 2.5% below the pre-pandemic growth path
- **The outlook** for the coming months is still good, if we should believe the reports from the business sector, measured by KI or the PMI

Industrial production flat in May, 4% above the pre-pandemic level

After an upward revision of the past months. New orders up 6% m/m, level up 10% vs early 2020





- Production will very likely continue on the upward trend the coming months
- Long term, manufacturing production in Sweden has not been that impressive

Highlights

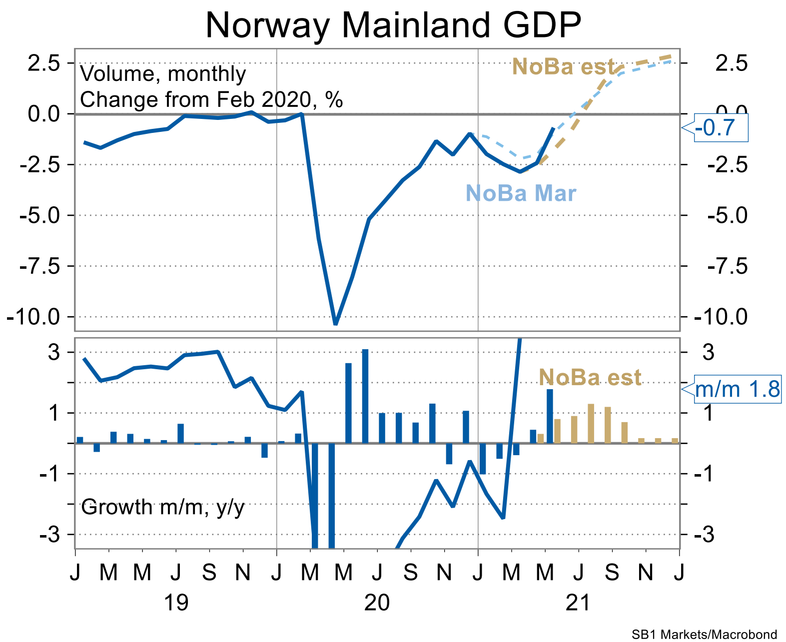
The world around us

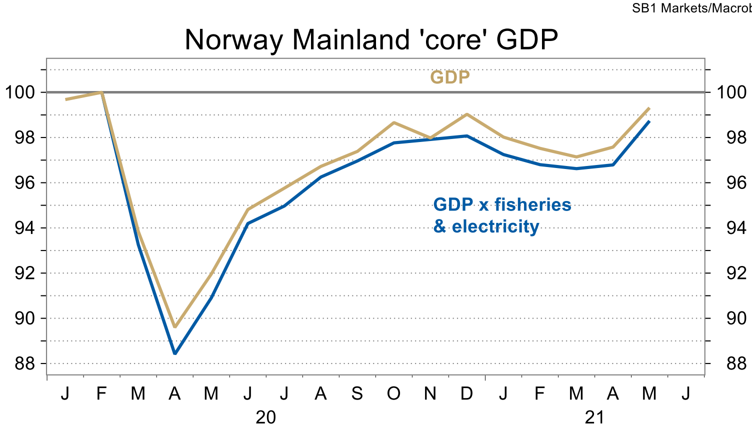
The Norwegian economy

Market charts & comments

Mainland GDP up 1.8% in May – and is just 0.7% below the Feb-20 level

... and 1.1% ahead of NoBa's 3 weeks' old forecast. Still much more to go in serviced

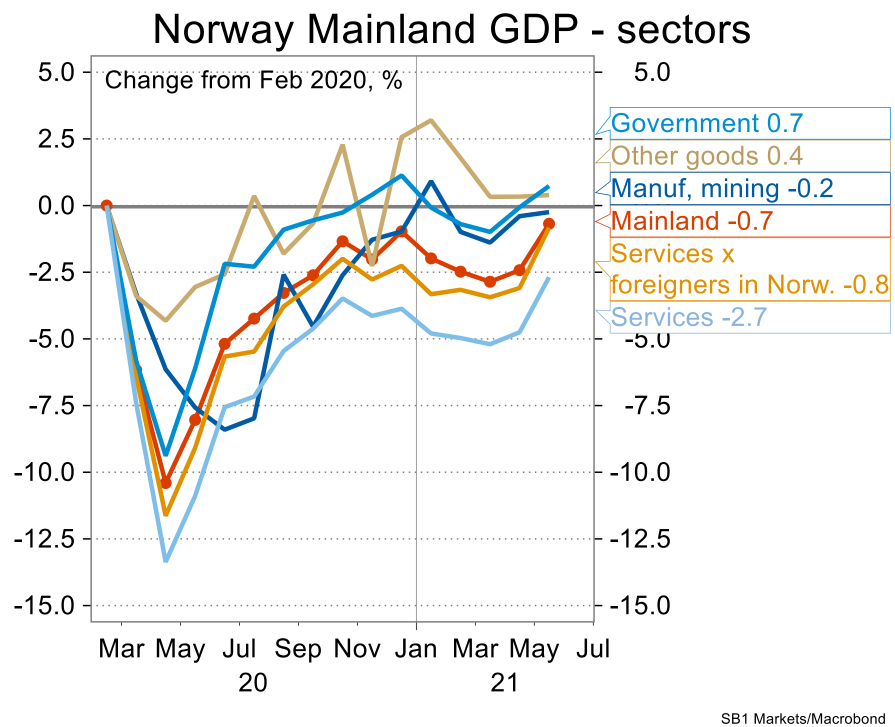


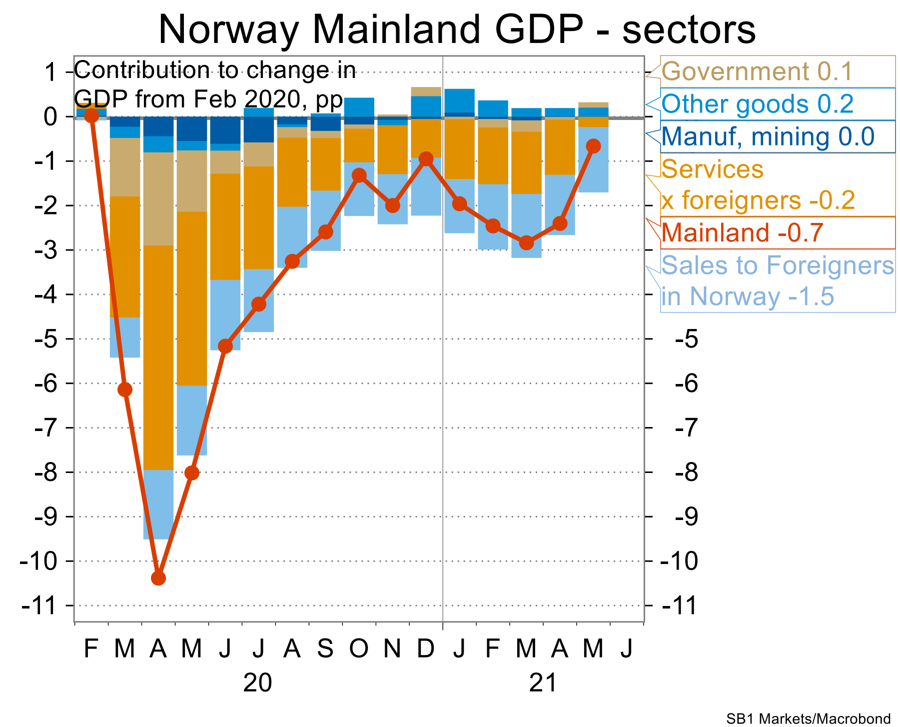


- **Mainland GDP grew by 1.8% m/m in May**, twice the consensus (and our) f'cast and 1 pp above NoBa f'cast. Growth in April at 0.4% was 0.1 pp higher than the first forecast. GDP is finally above the Dec-20 level, and just 0.7% below the Feb-20 level
  - » **Production:** Private services were up by 2.2% in May even business services reported a (strange) steep decline. Activity in hotels & restaurants rose by 35%. Trade up 10%, manufacturing flat
    - **Fisheries** down May, **and electricity** flat, 'core ML GDP' grew 2.0%
  - » **Demand:** Norwegians' spending at home shot up 4.6% in May, goods even more than services. Oil investments remained high in May, Mainland business investments fell further. Exports x travel rose 0.6%
- **Mainland GDP is down 0.7% vs the Feb-20 level**
  - » **GDP** was 1.1% above NoBa's f'cast
  - » **Production:** The 4 hard hit services are still far down, 25% – 34%. The total negative drag equals some 3% of Mainland GDP. Other sectors are up in sum flat, with trade, manufacturing & education in the lead. Construction is down 3%
  - » **Demand:** Norwegians' spending at home is unch. from Feb-20, goods +16%, services down 8%. Spending abroad has fallen by 97% (equalling 9% of disp. income), and the money is saved. Housing investments are up. Mainland business investments have fallen by 7%, while oil investments are up 5%! Exports ex petroleum (and tourism) are 3% below the Feb-20 level. Foreigners are not spending anything in Norway, a cut equalling 1.5% of Mainland GDP

Production: An improvement in all main sectors in May

The recovery is well underway – but services have much more to go





- **Service sector production was up 2.2%** in May, as corona restrictions were eased
- **Manufacturing production (incl. mining)** rose marginally
- **Other goods production** is volatile mostly due to (ocean) **fisheries and electricity production.** Production rose marginally in May

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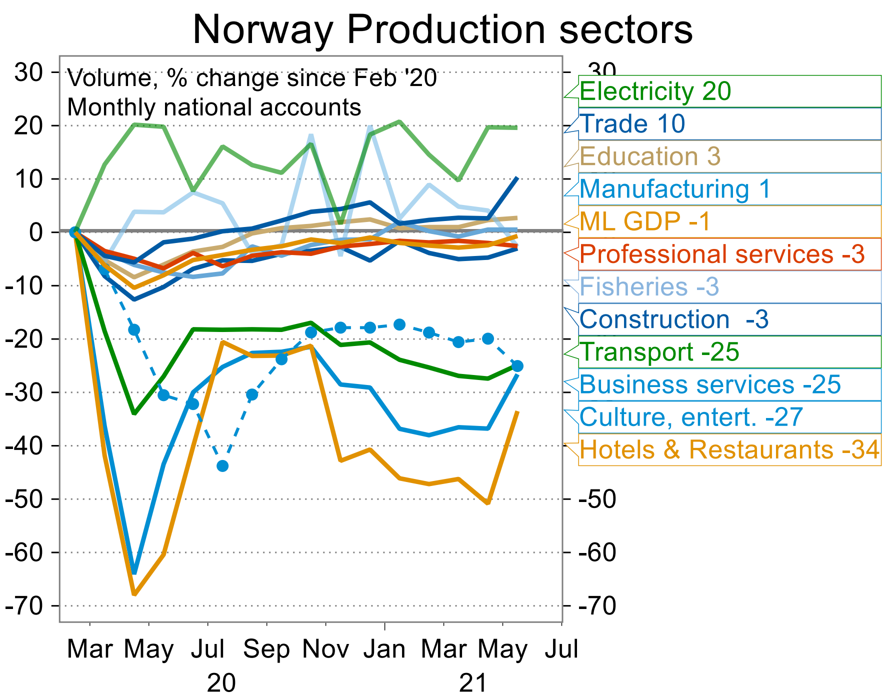
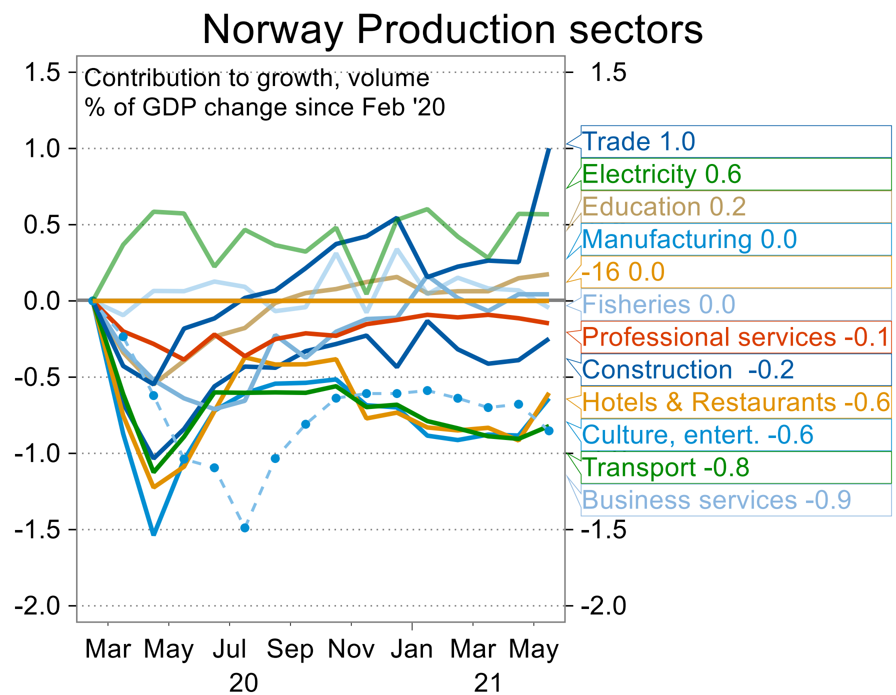
Production details: Business services further down in May, must turn up soon?

Hotels/restaurants +35%, culture/entertainment +16%, still 30% below par. Transport still down 25%



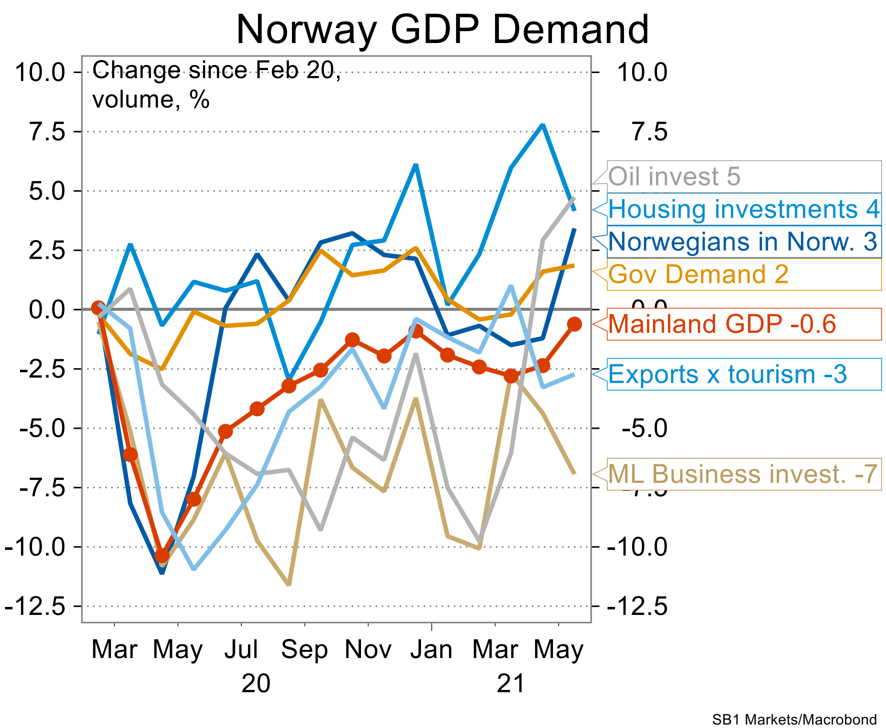


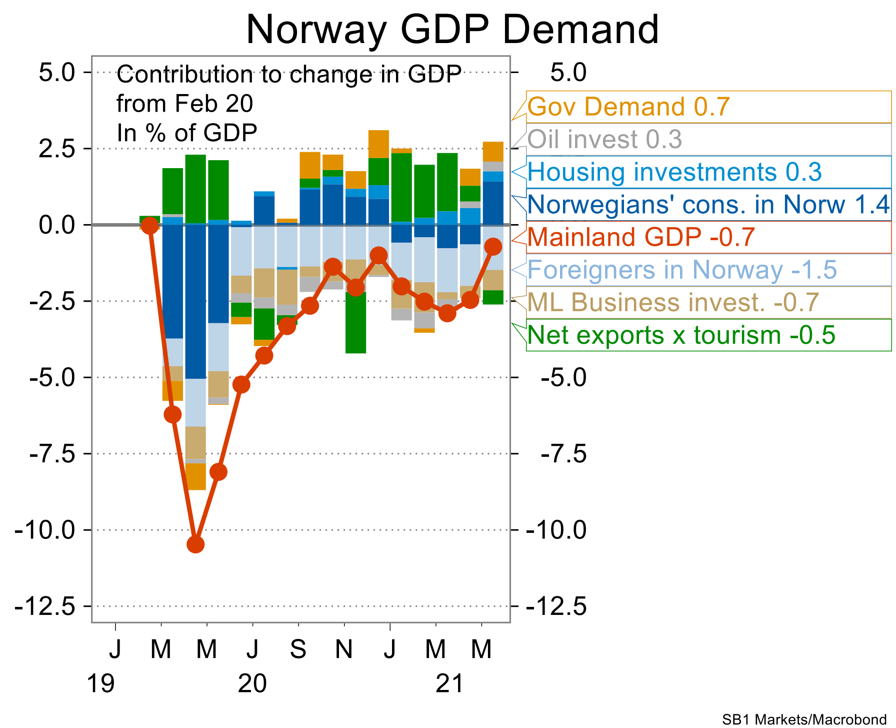
- **Business services** fell by more than 5% in May. We assume these activities will increase sharply the coming months
- **Hotels & restaurants, culture,** and **transport** all have miles to go before activity is normalised
- **Trade** reported a 7.5% lift in May, more than we assumed – but the level was strangely weak the previous months
- **Fisheries & aquaculture** contracted in May

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

Demand: Households demand came strongly back

Norwegians' consumption rose 4.3% in May, both goods & services up

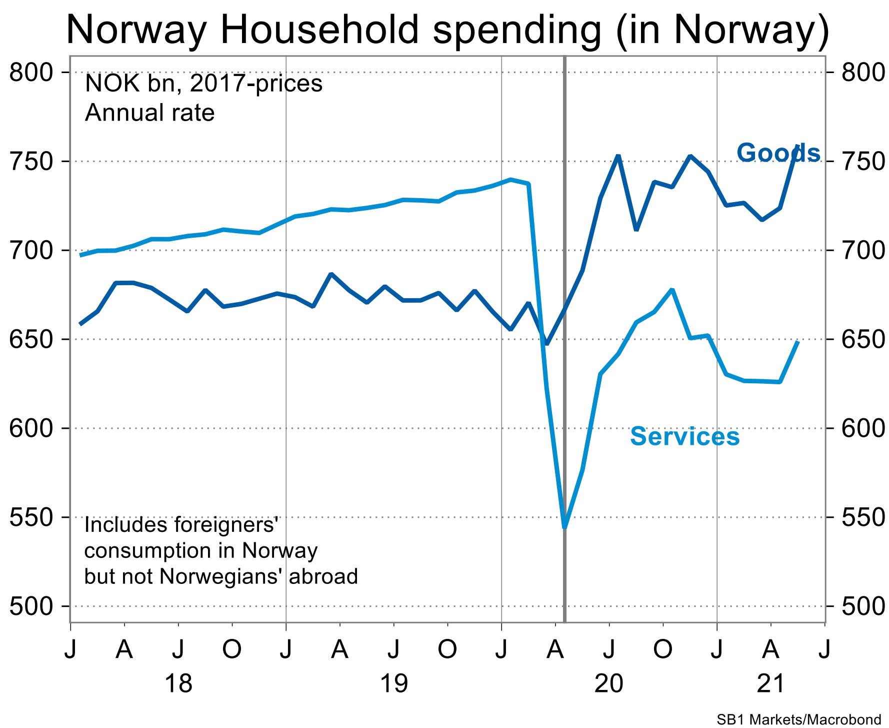


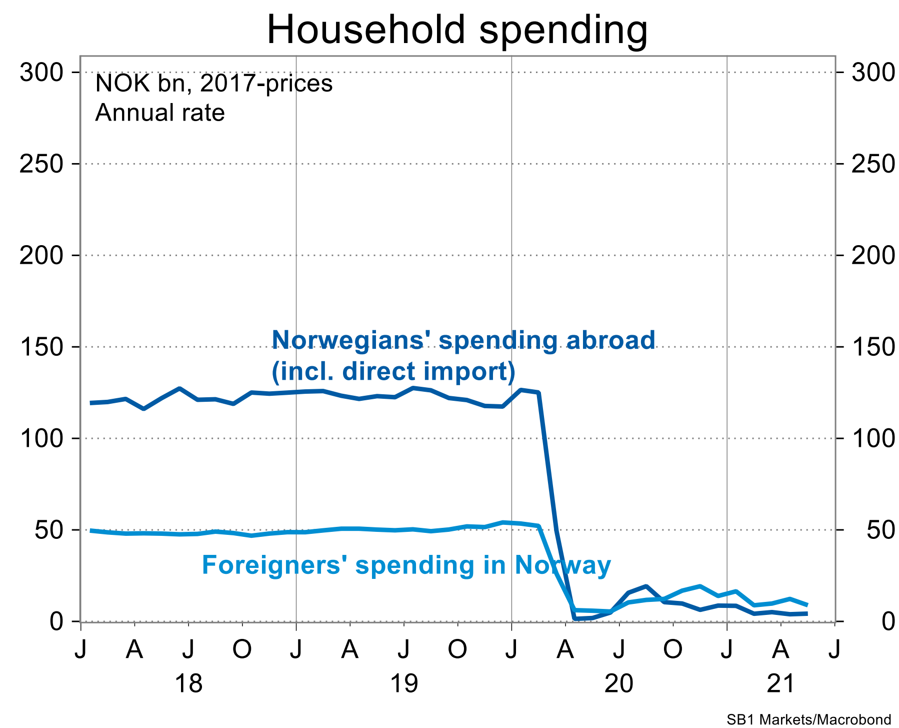


- **Norwegians' consumption in Norway** shot up by 4.3%, and the level is 3% above the Feb-20 level
  F**oreigners** are still not spending anything, and deducts 1.5% from GDP (not adjusted for import content of goods they (used to) buy here)
- **Mainland business** investments rose 3.3% in May, and are 7% down vs. Feb-20
- **Oil investments** increased 1.8% in May, and are now up 5% since Feb-20, adding 0.3% to GDP
- **Government demand** rose 0.3% in May, up 2% vs. Feb-20
- **Domestic demand x inventories** rose by 2.9%. Inventories rose faster than in April, a 0.9 pp contribution to GDP in May (from -2.6 pp in April)
- **Mainland exports** (x tourism) rose 0.2% in May, but are 3% below the **Feb-20 level**. Net exports x tourism are slightly below Feb last year, as **imports** rose sharply in May

Consumption of both goods & services up in May

Huge upside for services as the economy opens up. And a substantial downside for goods…





- At least when we start travelling abroad again

Norwegians are consuming like normal – in total – in Norway. Not abroad

Huge increases in domestic spending in May

Norway Consumption spending

Sales of consumer goods/ services & consumption	Change from Feb 20, NOK bn, annual rate, const. bn	% Change %
Sales in Norway	**0**	**0.0**
Goods	89	13.2
Services	-88	-12.0
Norwegians in Norway	**44**	**3.2**
Goods	106	16.3
Services	-62	-8.8
Foreigners in Norw.	**-43**	**-83.0**
Norwegians' consumption	**-77**	**-5.2**
In Norway	44	3.2
Abroad	-121	-96.6

SB1 Markets/Macrobond

Norway Consumption spending

Sales of consumer goods/ services & consumption	Change m/m NOK bn, annual rate, const. p bn	% Change m/m %
Sales in Norway	**59**	**4.3**
Goods	36	4.9
Services	23	3.7
Norwegians in Norway	**62**	**4.6**
Goods	37	5.2
Services	25	4.0
Foreigners in Norw.	**-3**	**-28.0**
Norwegians' consumption	**62**	**4.7**
In Norway	62	4.6
Abroad	0	8.6

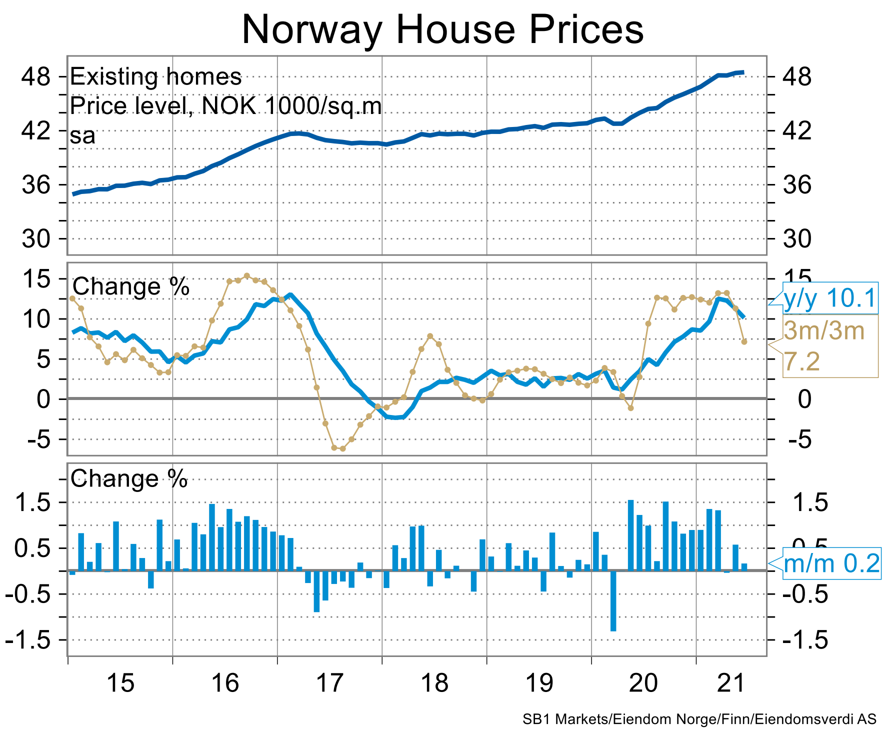
SB1 Markets/Macrobond

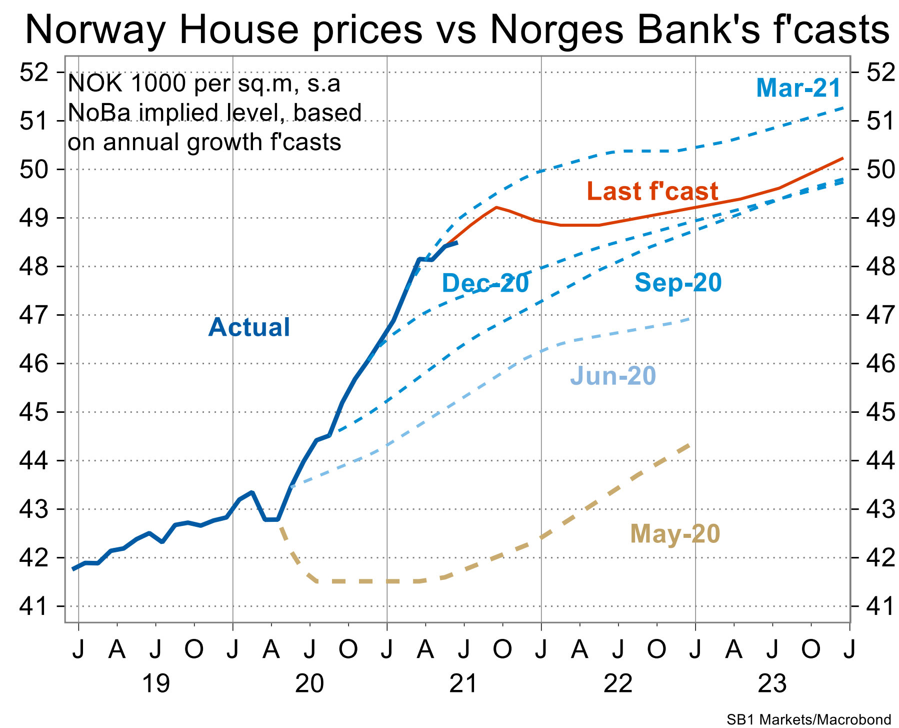
- **Sales of consumer goods** in Norway are up 13.2% vs. Feb-20, while services are down 12%, the sum is flat
  - » Lack of foreigners' demand in Norway – which has fallen by 83% - has deducted 3.2% from domestic spending
- **Norwegian households** have increased their consumption of goods in Norway by 13% but reduced consumption on services by 12% in sum +3.2%
- **Total (Norwegian) household consumption** has fallen by 4.7% vs. Feb-20. Of this is 8 pp due to the 97% (!) decline in Norwegians' spending abroad

- **We expect consumption to normalise** rapidly the coming quarters. Demand for goods is very likely above long term trend and will slow when spending on services picks up, and when we can start spending abroad again, probably in full scale during Q3. We expect the savings rate to decline substantially

House prices are slowing, just up 0.2% in June – NoBa expected 0.45%, we 0.6%

The impact of last year's lower rates are fading. And now something else will turn up…

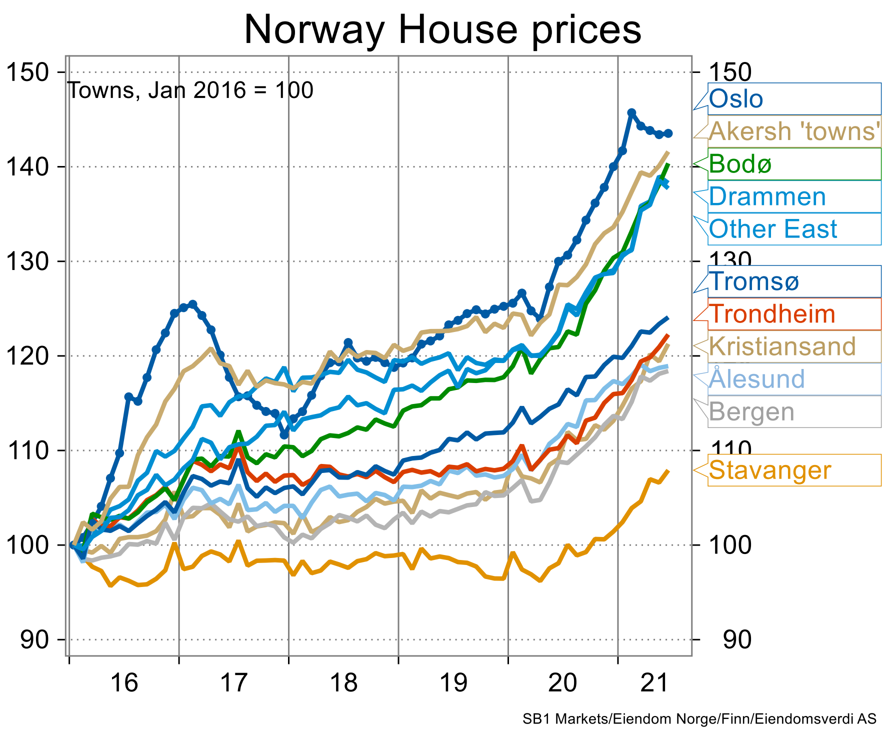


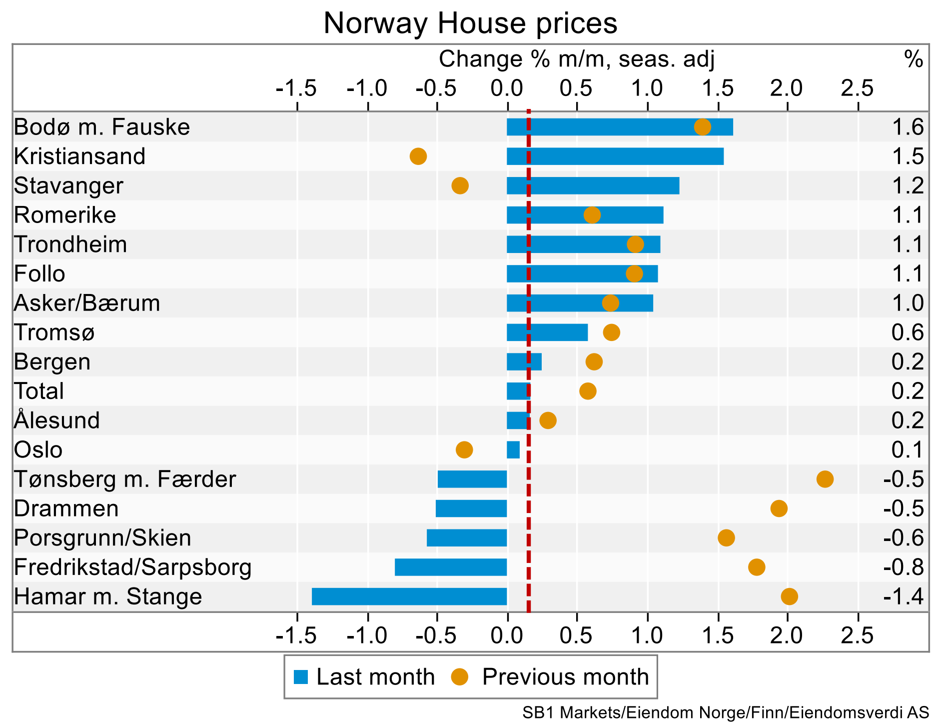


- **House prices** rose by 0.2% seas. adj in June, down from 0.6% in May. We expected 0.6%, NoBa 0.45% . Prices are up by 7% 3m/3m (annualised), down from above 10% . Prices are still up 10.1% y/y
- **Oslo** prices rose marginally in June, following 3 m months decline. Mixed in other towns, mostly a reversal of last months changes. Since before the pandemic, Bodø in the lead, followed by Porsgrunn/Skien, Tønsberg & Drammen. At the bottom: Berge, Tr.heim, Stavanger, Ålesund & Tromsø
- The **number of transactions** fell slightly in May but is high. The **inventory of unsold homes** fell further to a record low level
- Our Norway x Oslo **flow based price model** signals 1% m/m price growth, the Oslo model zero growth
- House prices are once again below NoBa's f'cast. The impact for last year's interest rate cut is fading, and soon rates will start to increase

Oslo prices rose in June, 'outer east' prices fell. Bodø, Kr.sand & Stvg at the top

Oslo prices still 1.5% down vs. Feb, all other towns (x Ålesund) are up vs Feb

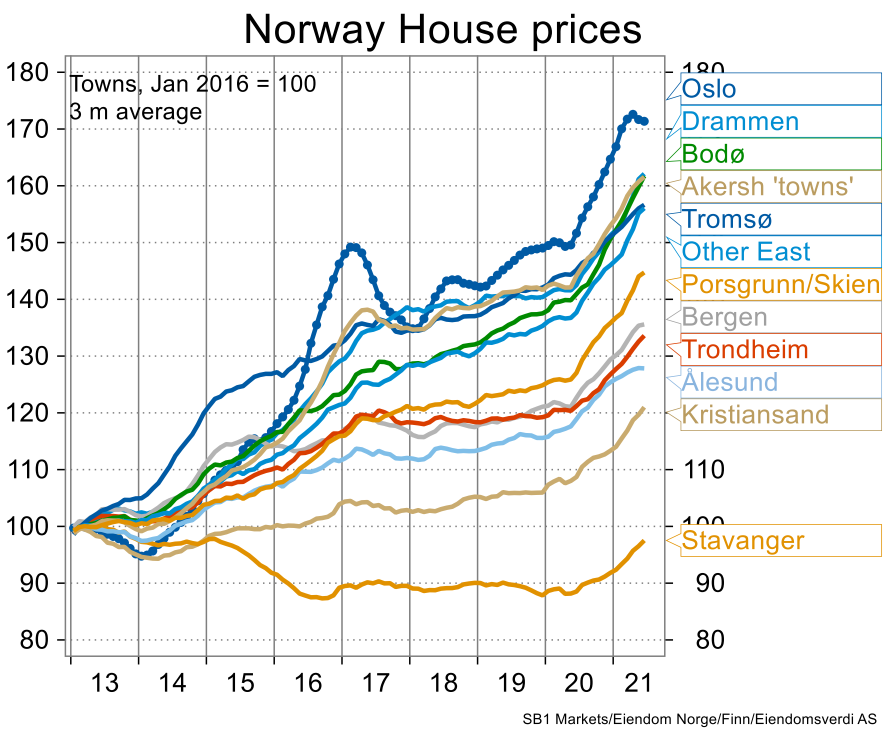


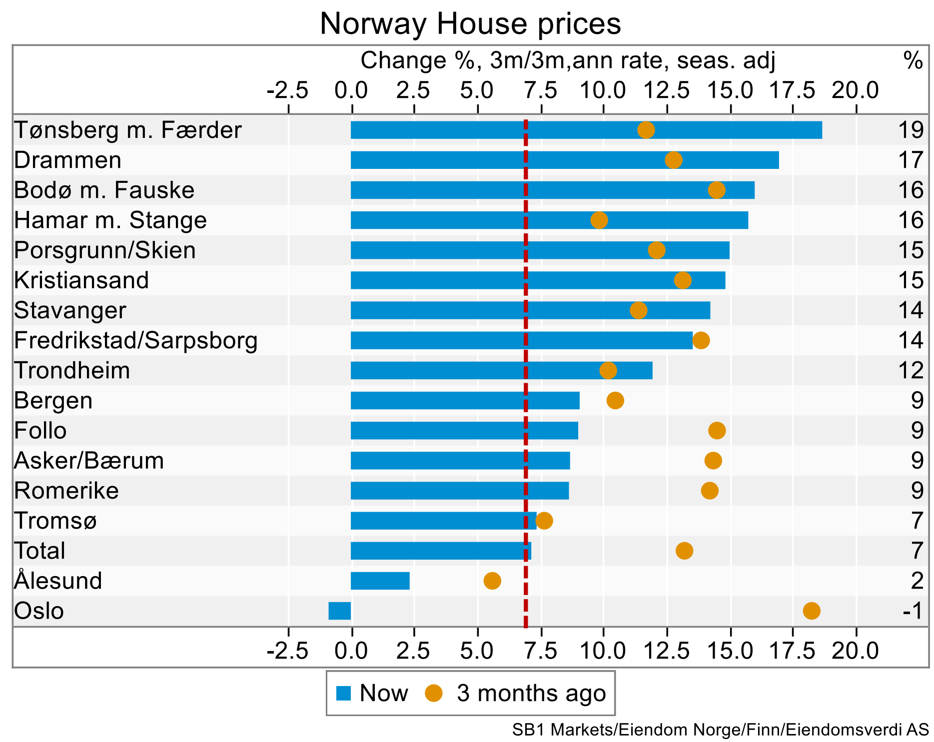


- In June: 11 cities up; 5 down

Smoothed 3m/3m Oslo down, all others up. Tønsberg & Drammen in the lead

3 months ago, the momentum was strongest in Oslo, up 18% 3m/3m

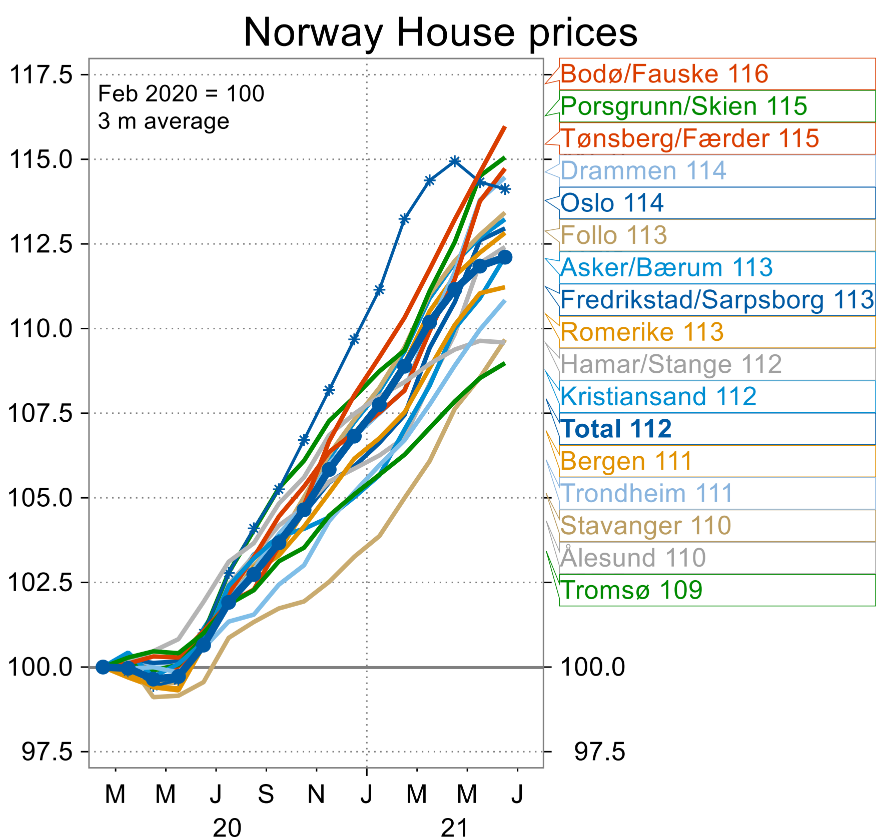




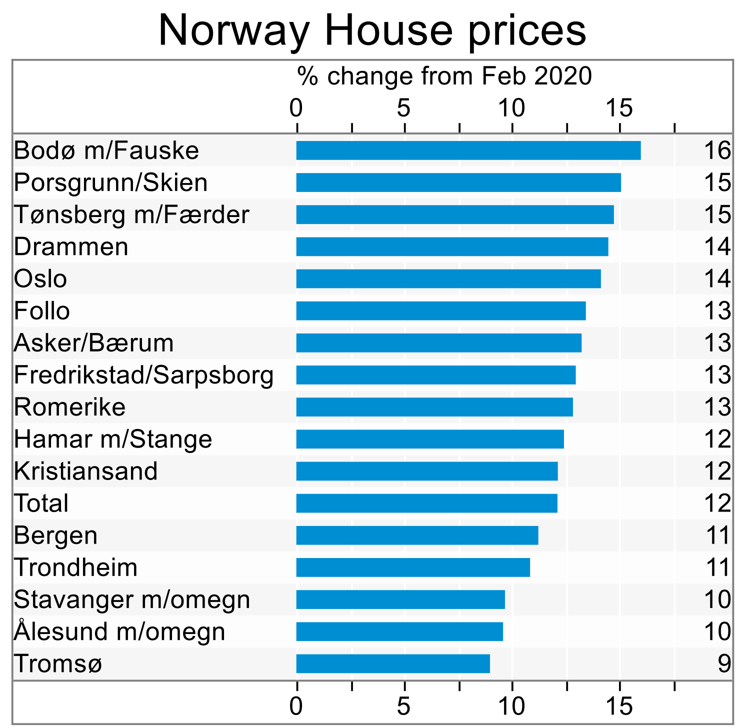
- <u>From 2013</u>:
  - » Oslo in the lead, together with Drammen, Bodø. Asker/Bærum/Follo ('towns' close to Oslo), followed by Tromsø
  - » Stavanger has been the weakest town, but is now heading upwards again – faster than the national average
  - » Kristiansand, Ålesund, Trondheim & Bergen at the lower part of the list too

Through the pandemic: Bodø, Porsgrunn/Skien, Tønsberg in the lead

Drammen is ahead of Oslo too – but too early to conclude that the capital will be deserted?



SB1 Markets/Eiendom Norge/Finn/Eiendomsverdi AS

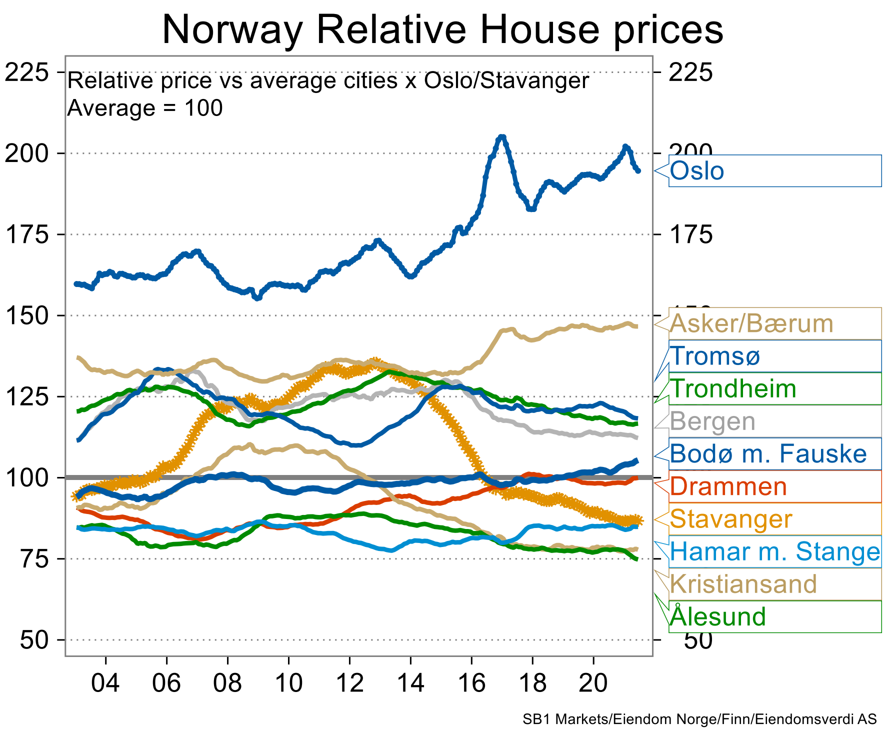


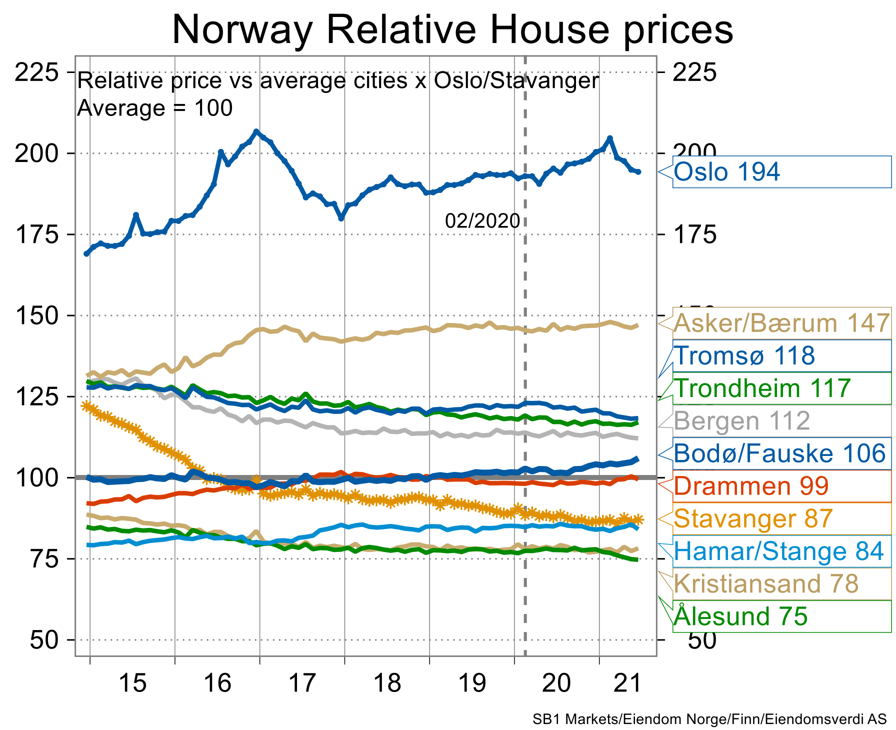
SB1 Markets/Macrobond

- Costal cities from Kristiansand to Tromsø (ex Bodø) at the bottom of the list

Oslo relative prices back to the pre-pandemic level

The costal cities Stavanger – Tromsø (x Bodø) are trending down. Hamar (w/Stange) soon above Stvg?

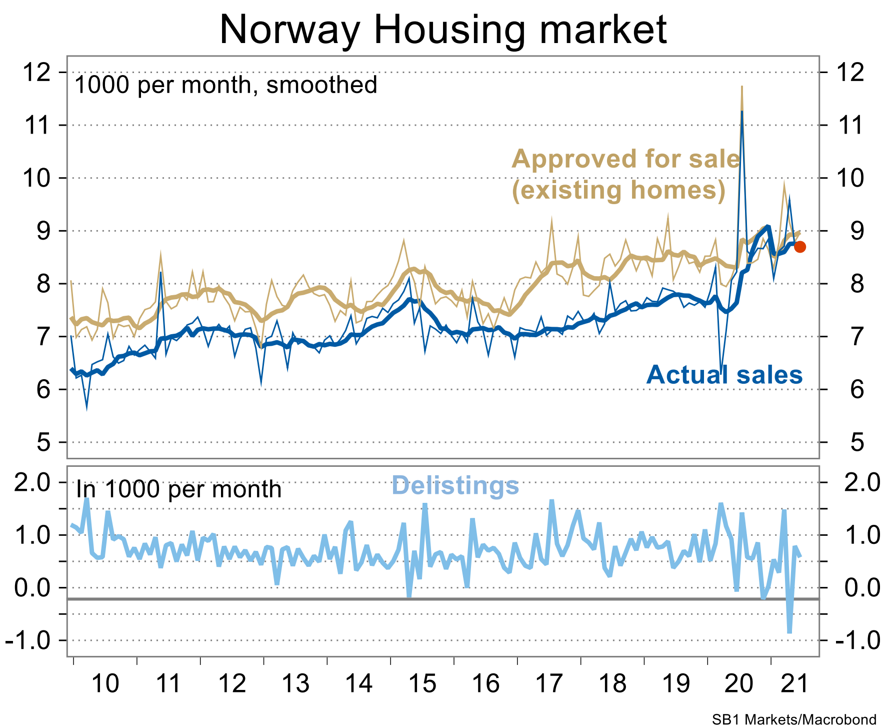


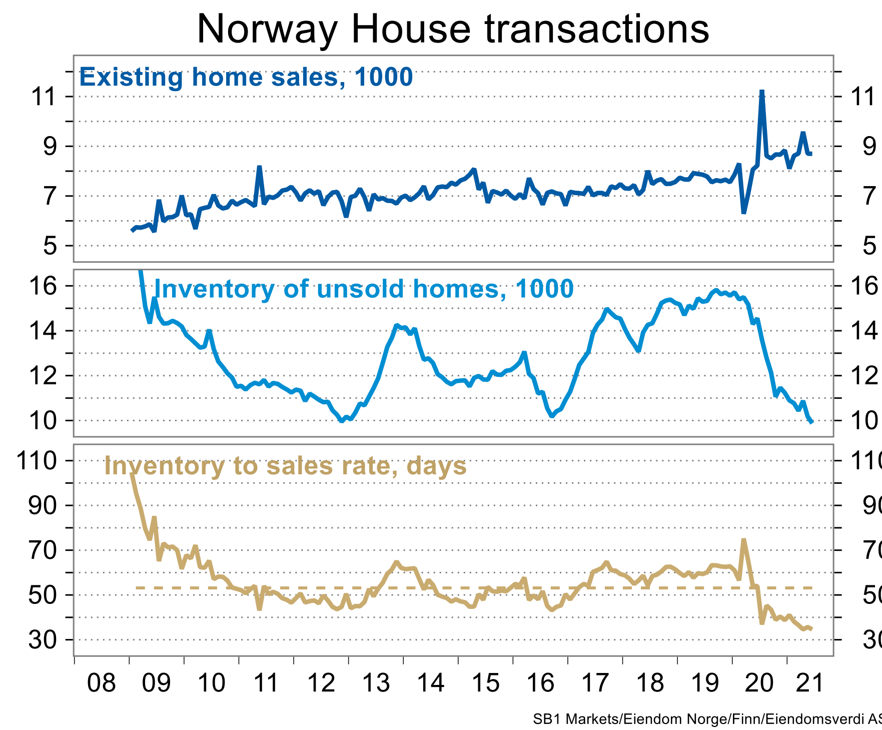


- Housing starts in Stavanger are still not lower than normal. It is still profitable to build, even at 'Hamar/Stange' prices!

The no. of transactions remains high, but so is the no. of homes approved for sale

The inventory fell further, and to ATL, in absolute terms & vs. sales

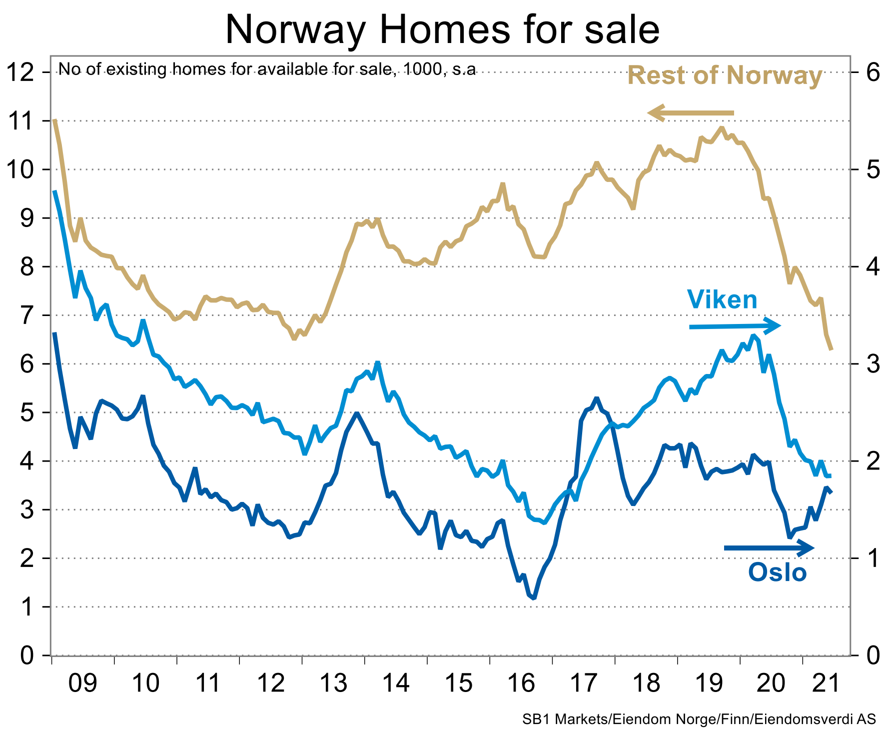


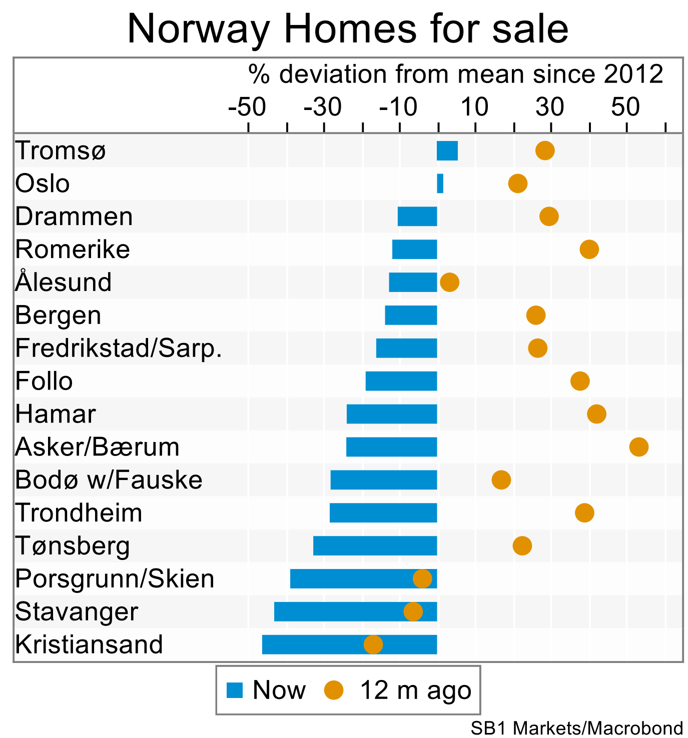


- **The number of transactions** remains well above the pre-corona level- and was close to flat vs May
- The **supply of new existing homes for sale (approvals)** rose in June, and the trend up
- **The number of delistings** was at normal level in June
- The **inventory of unsold homes** fell further in June, and is almost 40% down vs. the pre-pandemic level, and at the lowest level on record
- The **inventory/sales ratio** has contracted sharply too, and is at ATL, by far. The **turnover time** was 35 days in June vs an avg. of 53 days.
- The **actual time on market** for those homes sold was down 2 days to 37 days, well down from more than 60 days last spring (the avg. is at 43 days)

The inventory in Oslo on the way up – while it is still falling rapidly elsewhere

In addition, the inventory is lower than normal everywhere – except in Oslo & Tromsø

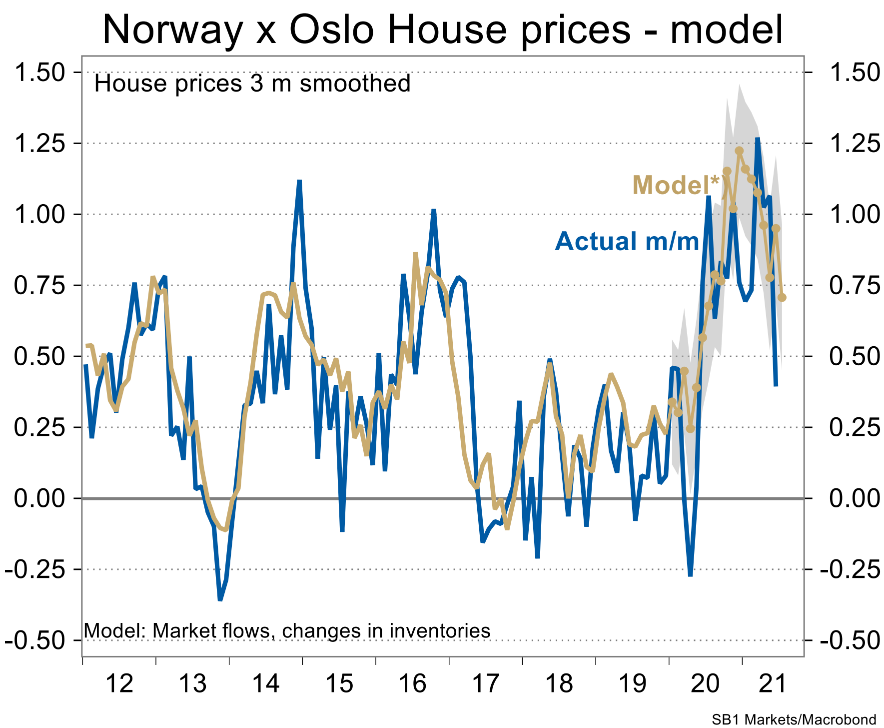


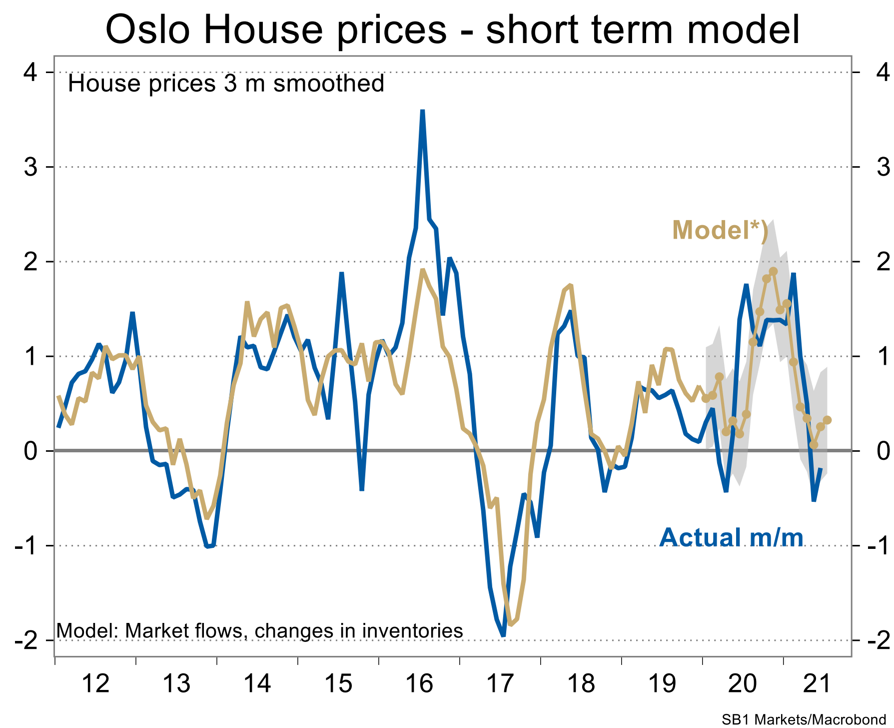


- The inventory is still down y/y in Oslo but has increases significantly since last October

Short term market flows suggest continued price growth – outside Oslo

… and no further decline in Oslo

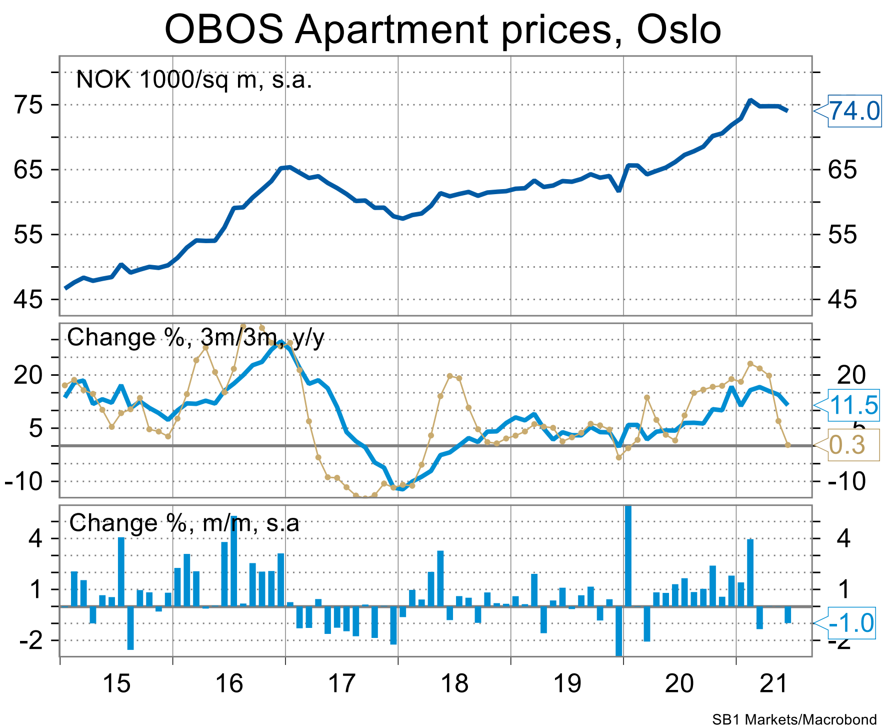


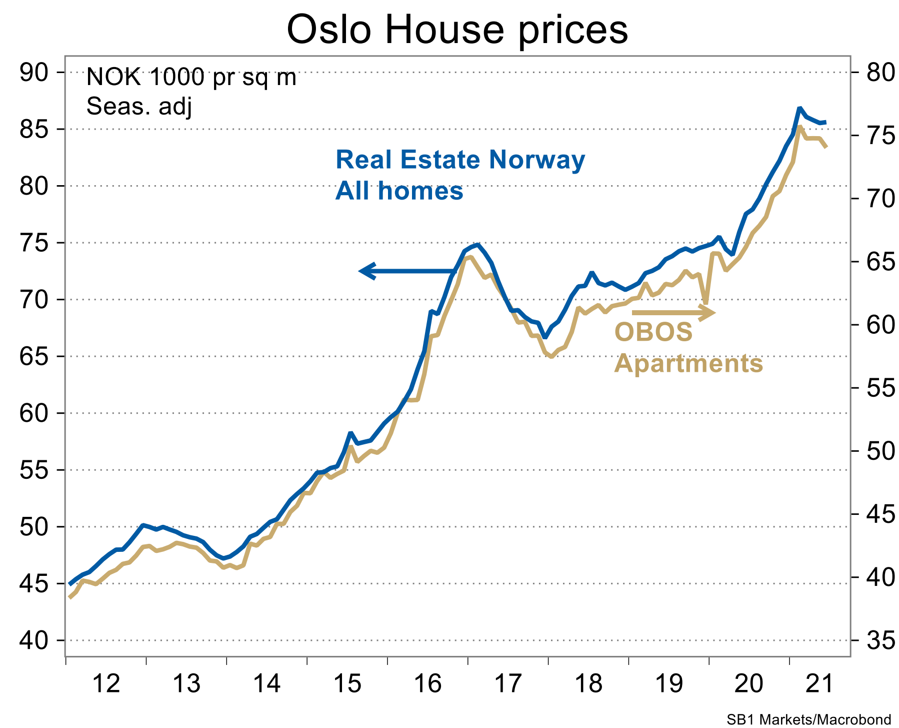


- Our **national x Oslo model** based on flows and the inventory signals a 0.75% growth in house prices per month (from above 1% some months ago)
- Our **Oslo model** signals marginal price growth (from zero 2 months ago)
- *These models are not long term price models, just short term price models based on flows of (existing) houses approved for sale actual sales & changes in inventories*

OBOS apartment prices down 1% in June (seas adj.), still up 11.5 y/y

Prices are down 2.4% since the February ATH, all homes are down 1.5%, says Eiendom Norge



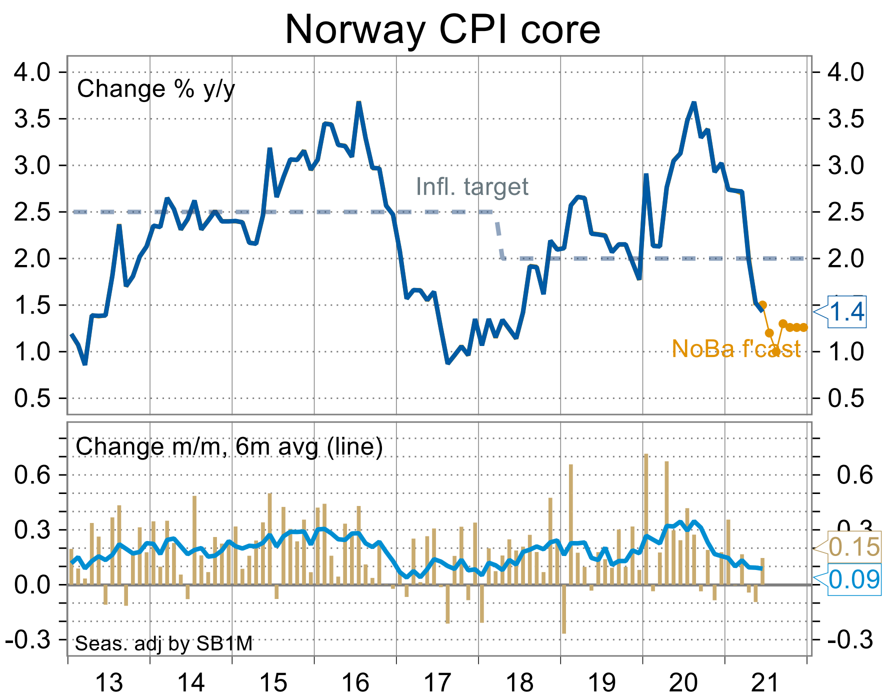


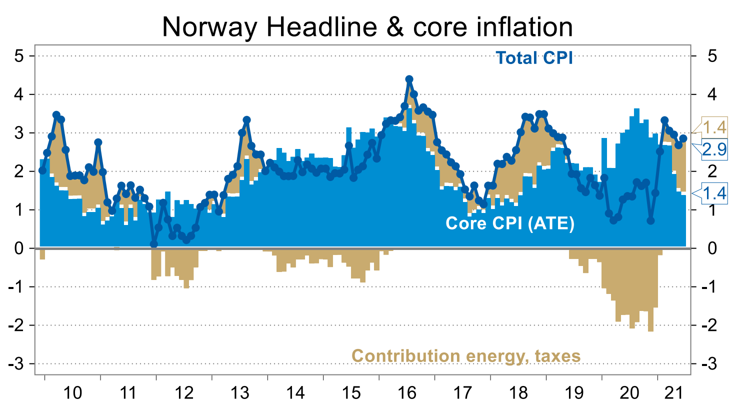
- The parallel change in both co-op & total house prices in Oslo signal a real turning point in the market

Co-op apartment prices follow the overall Oslo market quite closely, the average price level is somewhat lower than total Oslo market

Inflation is not on the way up everywhere: CPI-ATE down 0.1 pp to 1.4% y/y!

… And now due do domestic goods & services, not cheaper imports





- **CPI-ATE** (ex. energy and taxes) inflation was down 0.1 pp to 1.4% in May; 0.1 pp below Norges Bank's & consensus f'cast, 0.2 pp below our estimate
  - » Prices were up 0.1% m/m (seas adj), up from -0.1% in April
  - » Inflation is below 2% for housing, clothing, food, alcohol, communication, transportation, and airline tickets – others are still above
  - » The main misses (vs our f'cast) on the downside were food and airline tickets, where furniture surprised at the upside
  - » Prices on imported goods rose in June, but annual inflation is trending down, following the strengthening of the NOK
  - » In addition, domestic inflation has slowed substantially to 1.4%
- **Total inflation** accelerated 0.2 pp to 2.9% as we expected
- **The outlook**
  - » **Inflation may slow** somewhat more the coming quarters. NOK has strengthened and wage inflation remains moderate (if not low). Demand for goods will have to decline from a very high level. <u>Upside risk: Higher raw material prices/global price pressures but the spillover to the Norwegian CPI is not that significant</u>
  - » <u>Anyway, CPI inflation will not have any material impact on Norges Bank's monetary policy</u> the coming months. It's all about the post Covid-19 recovery – and the housing market

Lower food and transportation prices than expected

		Change m/m, seas. adj			Change y/y			Contribution, pp		
Jun-21	Weight	Out-	SB1M	Dev.	Last	Out-	SB1M			Dev. vs
CPI ATE	%	come	f'cast	pp	month	come	f'cast	m/m	y/y	f'cast
Food, non alc bev	13.0	-0.2	0.2	-0.4	0.0	0.1	0.9	-0.02	0.01	-0.05
Alcohol, tobacco	4.3	0.2	0.1	0.1	0.6	0.9	0.8	0.01	0.04	0.00
Clothing, footwear	4.9	0.1	0.2	-0.1	-1.7	-2.9	-3.0	0.00	-0.15	-0.01
Housing x. energy	20.5	0.1	0.2	-0.0	1.3	1.3	1.3	0.03	0.26	-0.00
Furnishing	6.8	2.8	0.5	2.3	2.8	3.6	2.2	0.19	0.25	0.15
Health	3.2	0.0	0.3	-0.2	3.7	3.3	3.6	0.00	0.11	-0.01
Transp. ex. gas, airl. tick	12.0	-0.2	0.3	-0.4	1.8	1.4	1.7	-0.02	0.17	-0.05
Airline tickets	1.0	-2.7	0.2	-2.9	-16.3	-20.1	-16.3	-0.03	-0.20	-0.03
Communication	2.5	0.4	0.2	0.2	1.6	2.5	1.9	0.01	0.06	0.01
Recreation, culture	11.2	0.5	0.3	0.2	3.4	3.8	3.5	0.06	0.43	0.02
Education	0.5	-	-	-	2.1	2.1	2.1		0.01	0.00
Restaurants, hotels	5.9	0.3	0.3	0.0	3.0	3.5	3.4	0.02	0.20	0.00
Other	8.7	0.0	0.2	-0.2	2.5	2.3	2.6	0.00	0.19	-0.02
CPI-ATE	94	**0.1**	**2.9**	-2.76	**1.5**	**1.4**	**1.6**			-2.61
Norges Bank est.			**2.9**		**1.5**		***1.5***			
Imported	34	0.7	0.2	0.5	0.8	1.0	0.4	0.24	0.34	0.16
Domestic	60	-0.2	0.2	-0.4	1.5	1.4	1.6	-0.11	0.86	-0.25
Energy, housing	4	3.5	-1.0	4.5	55.1	68.9	62.2	0.12	2.47	0.16
Energy, transport	2	0.9	1.5	-0.6	12.0	10.0	10.7	0.02	0.20	-0.01
CPI Total	100	**0.2**	**0.2**	-0.0	**2.7**	**2.9**	**2.9**	0.17	2.85	-0.04

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** prices fell by 0.2%, and well below our f'cast. Up 0.1% y/y
- **Clothing** prices were up after falling for the past two months, by 0.2% m/m, but are down 2.9% y/y
- **Furniture/hardware/equipm.** surprised sharply on the upside, up 2.8% m/m!
- **Transport ex. gas/airline** – fell 0.2%, we exp +0.3%.
- **Airline ticket** prices were down 2.7% m/m. Still down 20% y/y, to the extent they are measurable
- **Recreation** was down 0.5% m/m, we expected +0.3%
- **Restaurant/hotel** prices are up 3.5 y/y%

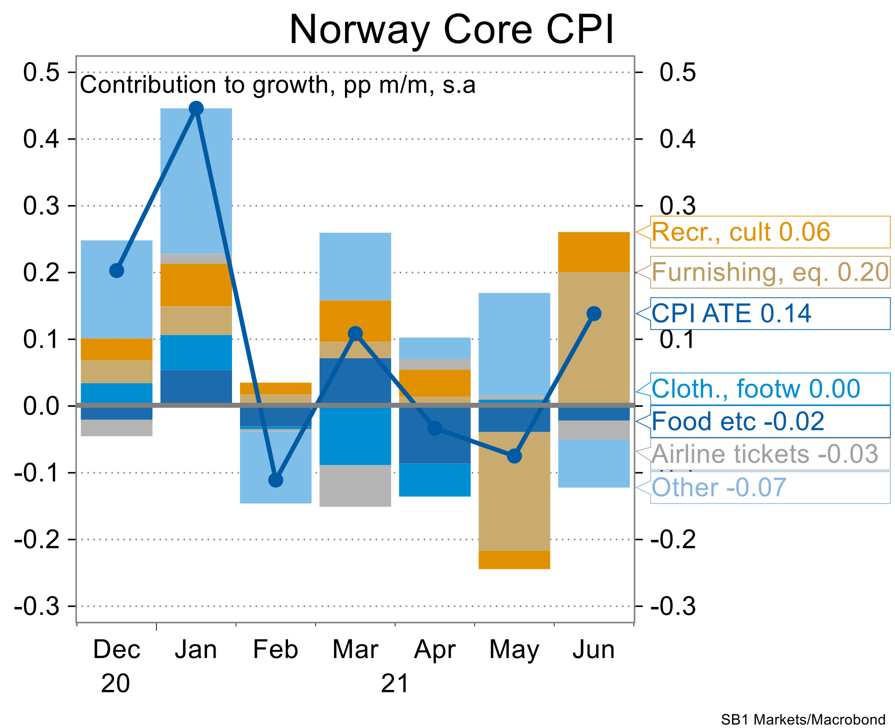
- **CPI-ATE up 1.4% y/y, 0.1 pp below our expectations, consensus had 1.6% & NoBa f'casted 1.5%**

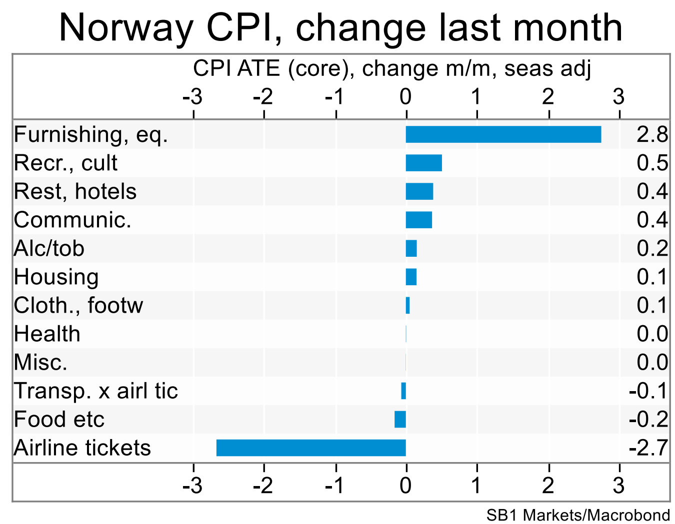
- Prices on **imported goods** was up by 0.7% m/m
- Prices on **domestically produced** goods & services fell by 0.2% m/m. The annual rate at 1.4% is low, according to Norwegian standards
- **Electricity** prices rose more than expected and is up 69% y/y
- **… and the headline inflation came in at 2.9%, spot on our estimate**

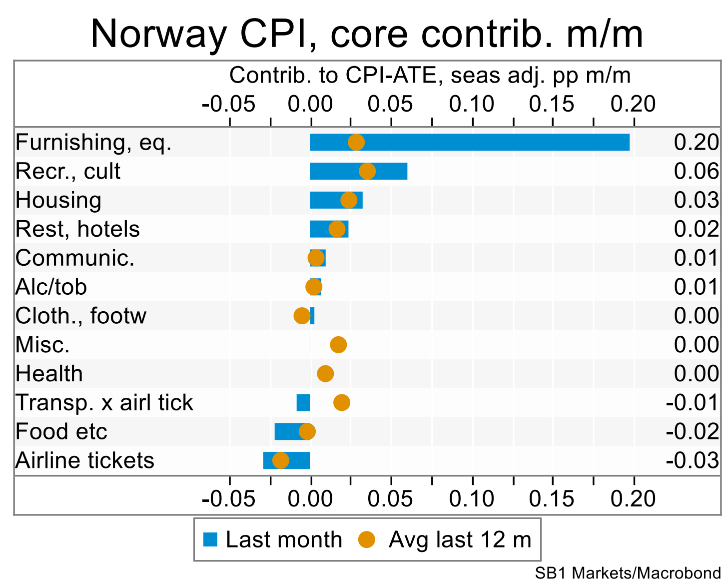
Monthly changes are seasonally adjusted by SB1 Markets. The weighted sum of the components does not necessarily sum exactly up to the total, and deviations m/m and y/y do not necessarily add up. Norges Bank m/m s.a. estimate is implied, calculated by us. Sources: SSB, Norges Bank, SB1 Markets calculations

Furnishing and food prices biggest downside contributors in May

Other goods & services up in May

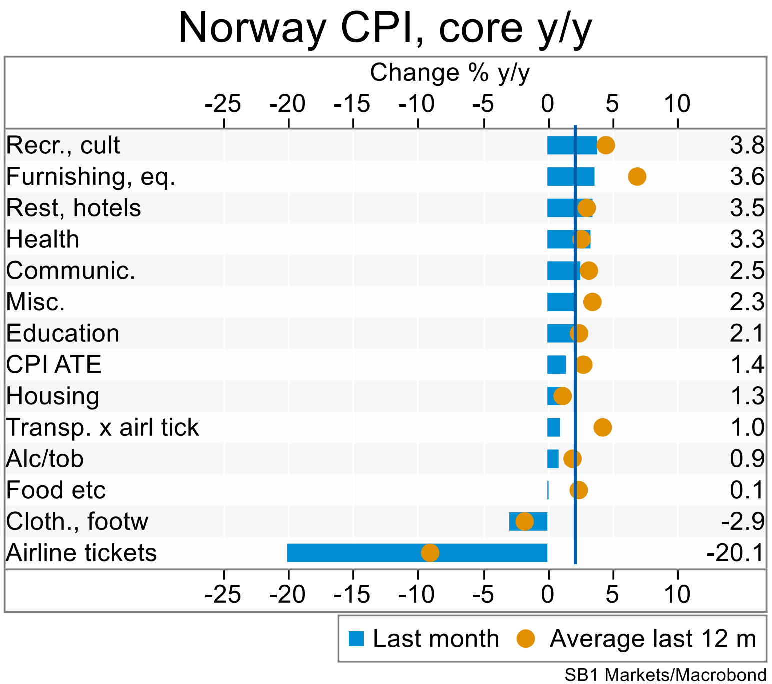


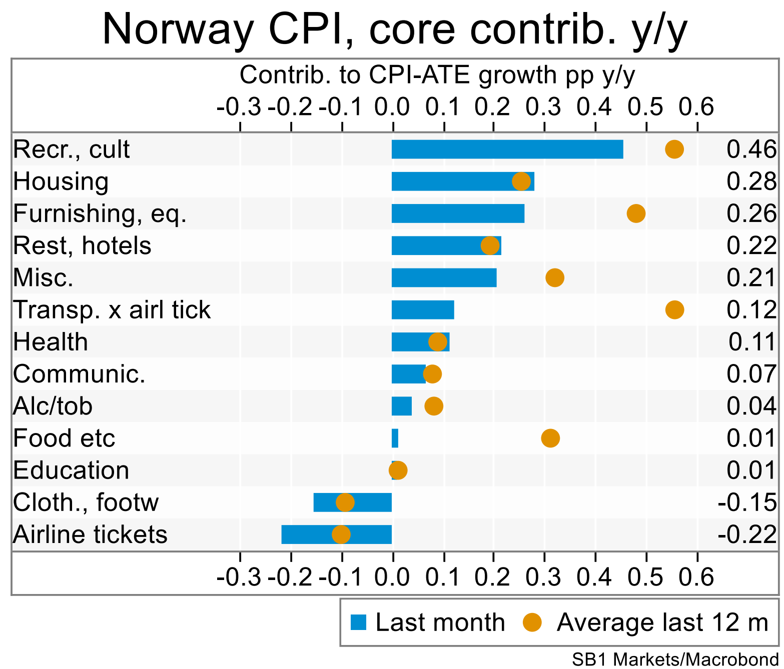




6 sectors report inflation above 2%, 1 is close to 2%, 6 clearly below

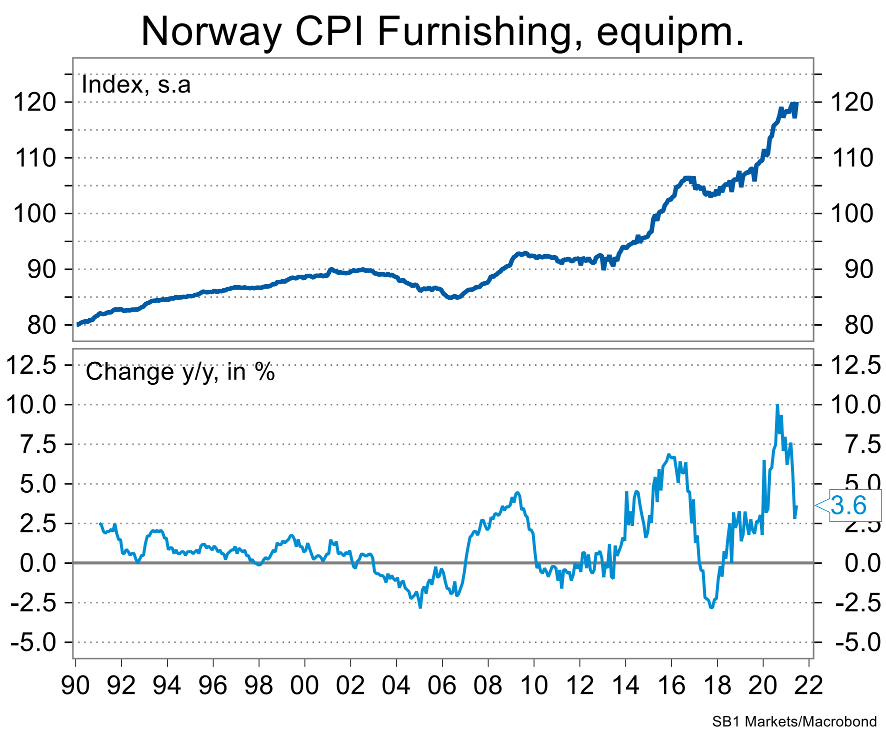
Food inflation down to 0; Clothing, rents, alcohol, communication & airfares << the 2% infl. target

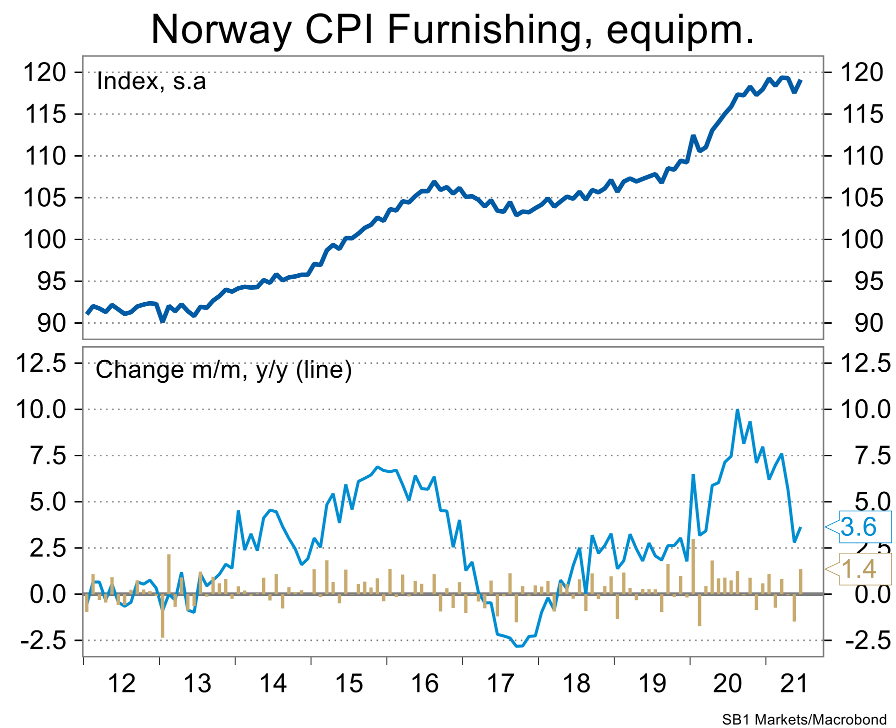




Furnishing prices up in June but annual inflation has come significantly down

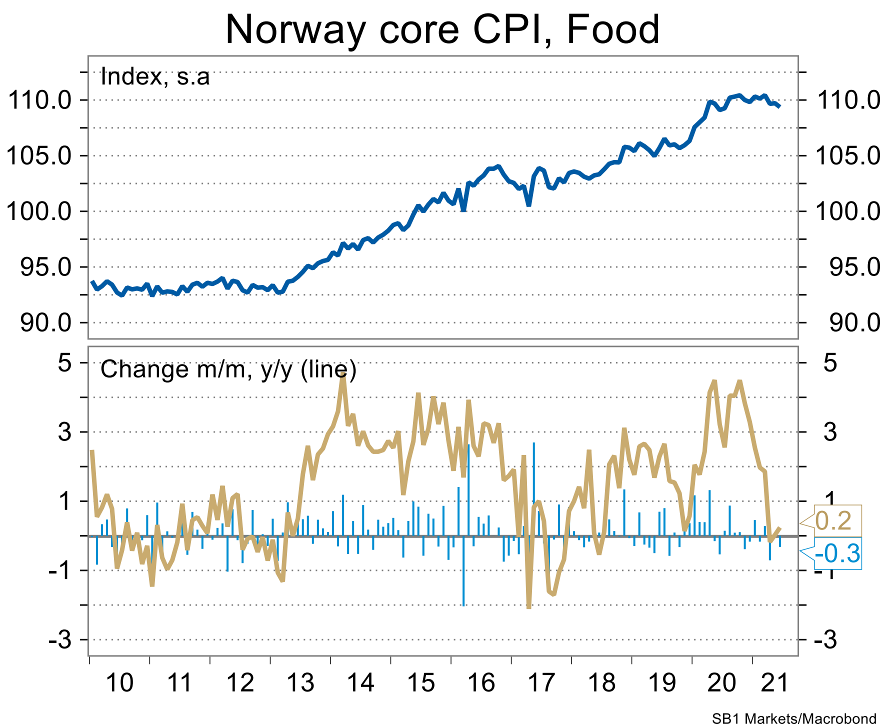
At the peak, 10% y/y, now 3.6%

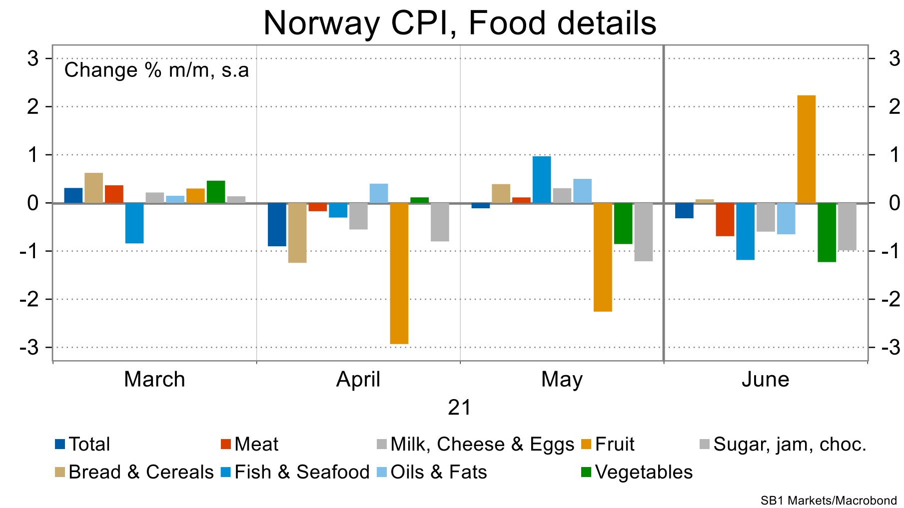


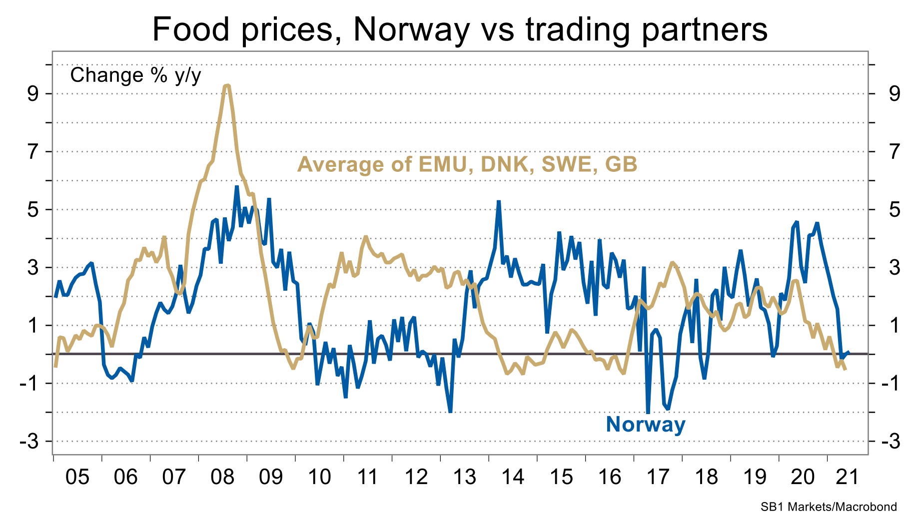


Food prices fell for the 3rd month

Prices fell 0.3% m/m and the annual rate rose is at 0.2%



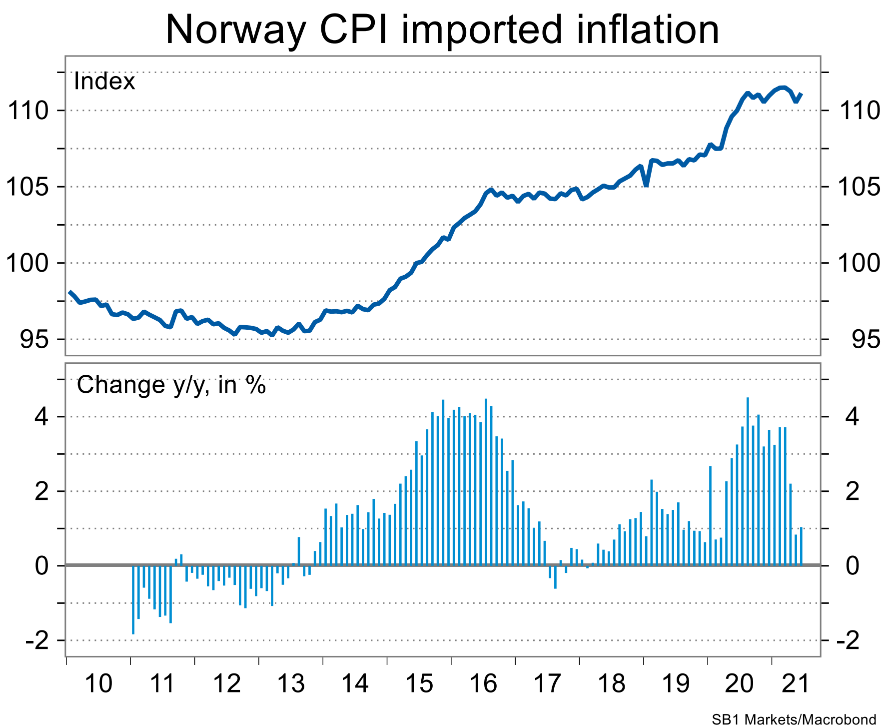


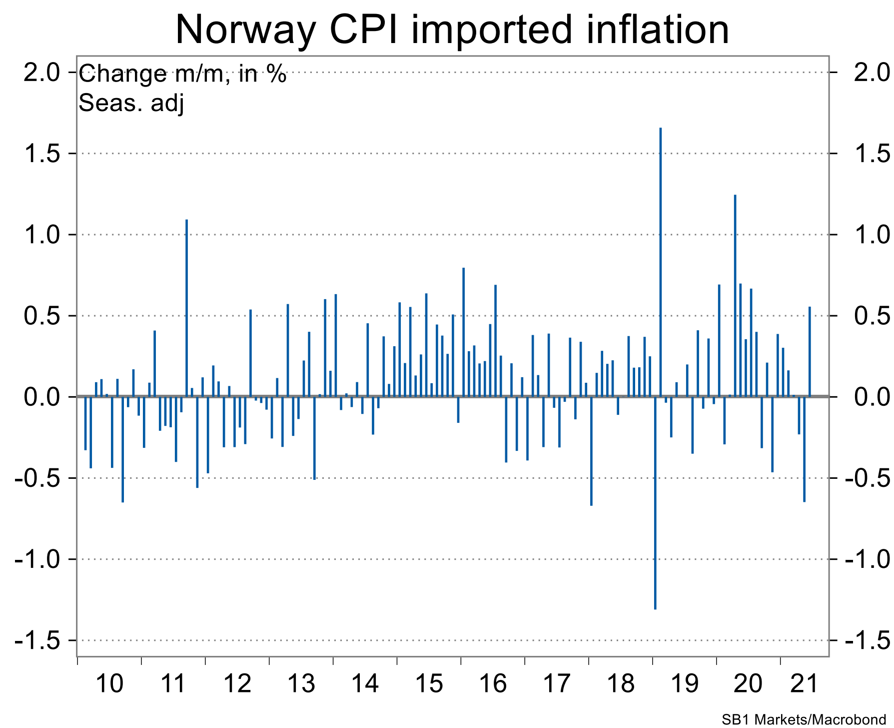


- Prices have fallen for the past three months, but the decrease in June was more widespread. The price of fruit was the only area of significant price increase in May
  - » Vegetables and seafood were down the most, while bread & cereal prices were practically unch.
- Food prices are now slowing at the same pace as in our neighbouring countries, despite lifts in some agricultural commodities

Imported goods prices have flattened

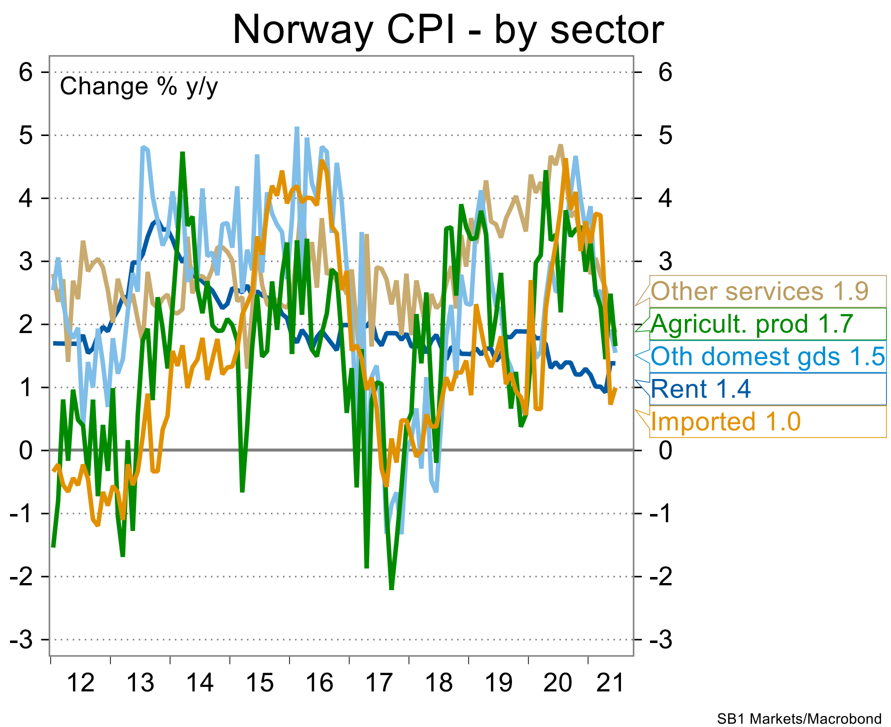
Annual imported inflation was 1.1% m/m in May – and will remain low

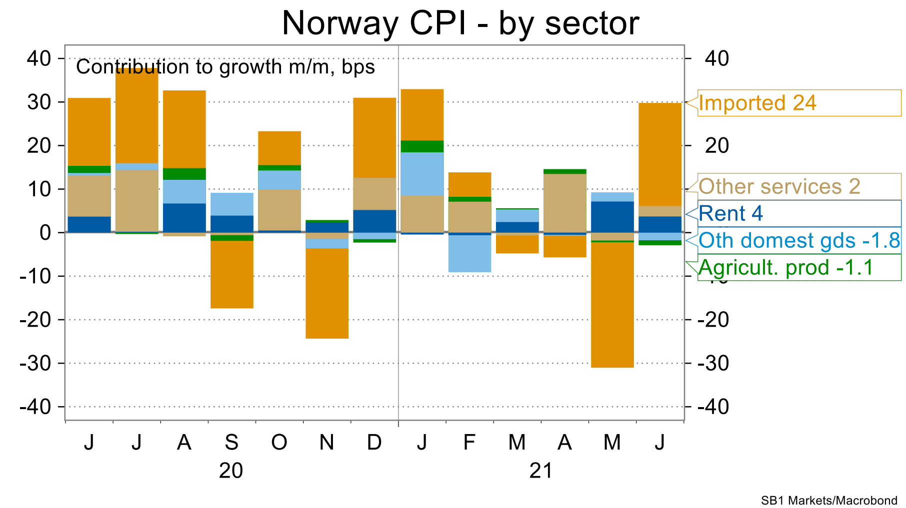


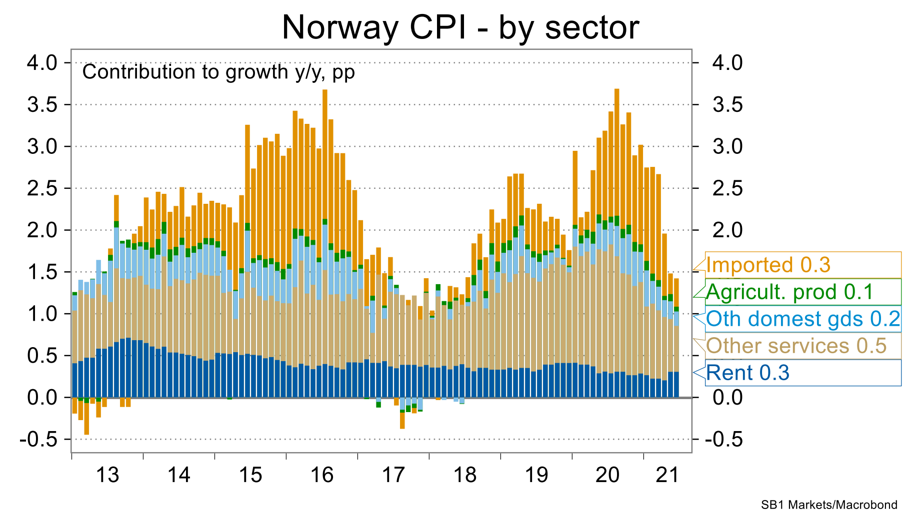


- The contribution to overall inflation in June was 0.2 pp

A broad decline in inflation – it is not just imported goods



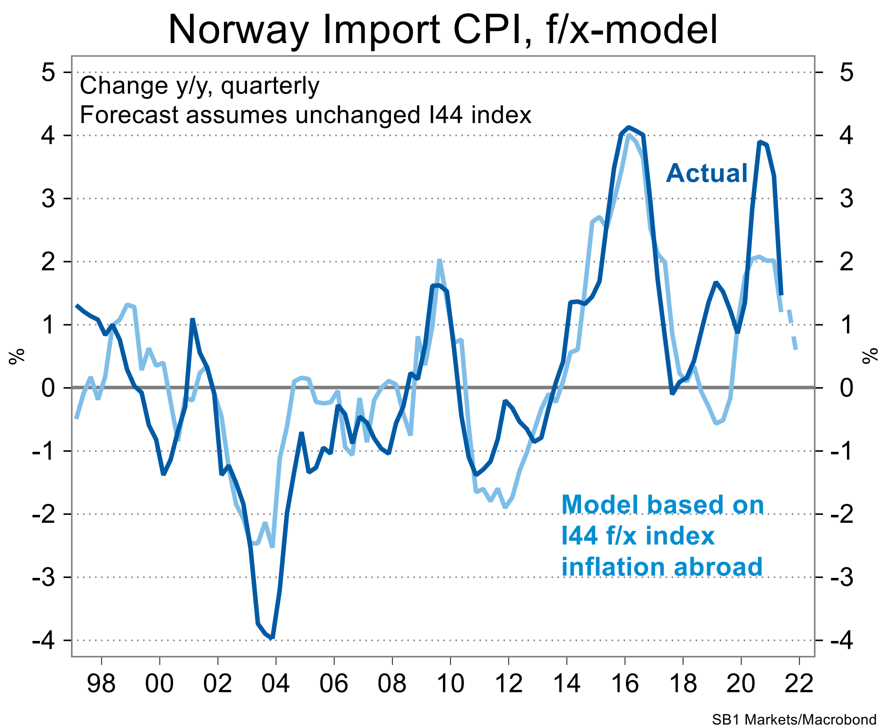


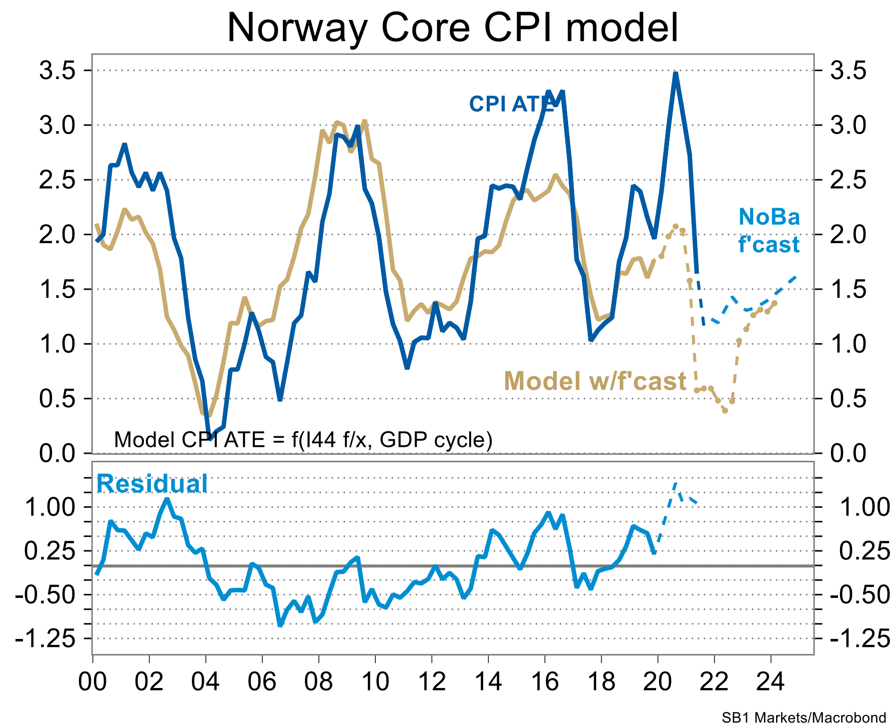


- **Domestic services inflation** has slowed sharply during the corona crisis, and not just only the cheaper airline tickets
  - » We expect some reversal the coming months
- **Rent inflation** has slowed but has picked up marginally past two months

Imported goods prices: Finally on the way down

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

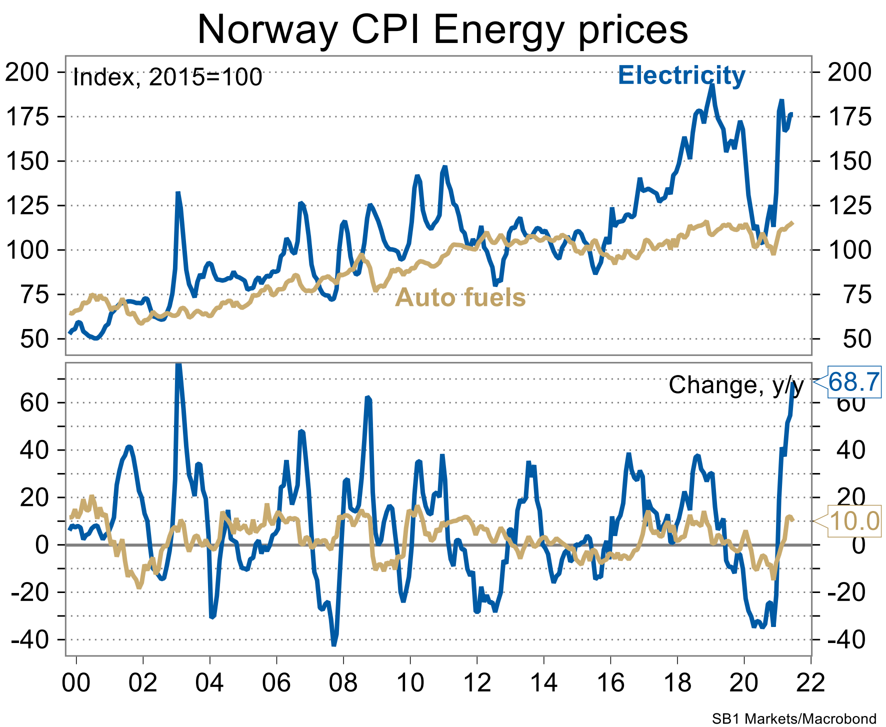


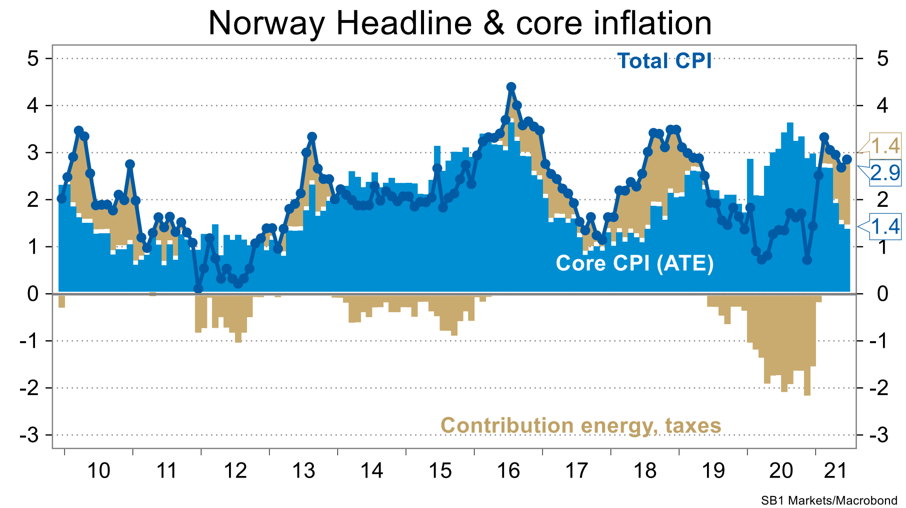


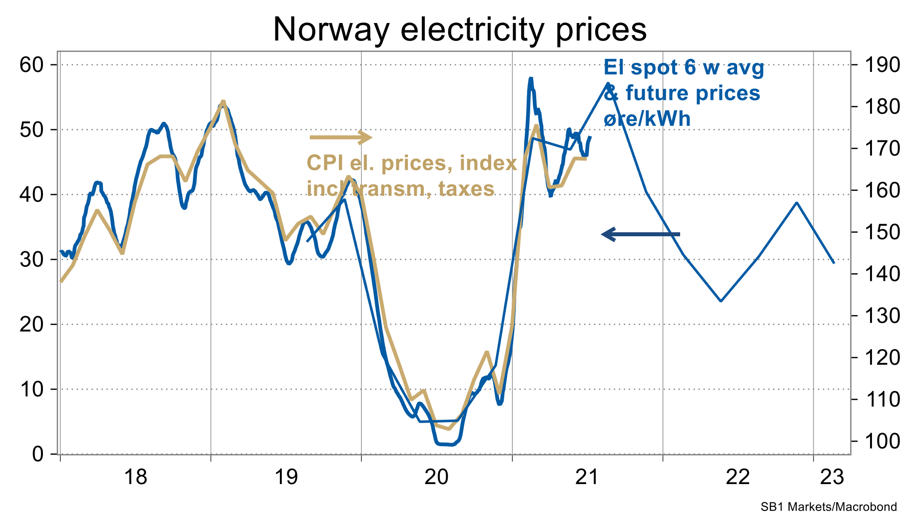
- **The NOK steep depreciation** in early 2020 no doubt drove **imported inflation** up last year. Closed borders/supply chain challenges due to Covid-19 may have contributed to the lift in import prices too, and more importantly: the strong growth in demand for some goods (like sport equipment/furniture) made it possible to increase prices. Now the NOK has recovered, and import price inflation is falling sharply
  - » Even if goods price inflation abroad is on the way up, we assume imported inflation to slow further due to the stabilisation of the NOK
- **Domestic inflation** will be kept in check due to moderate wage inflation – and overall core inflation will come down, as signalled by our **total core CPI** model (to the right)

Electricity prices sharply up y/y but has flattened recent months

Electricity prices are adding 1.4 pp to total inflation



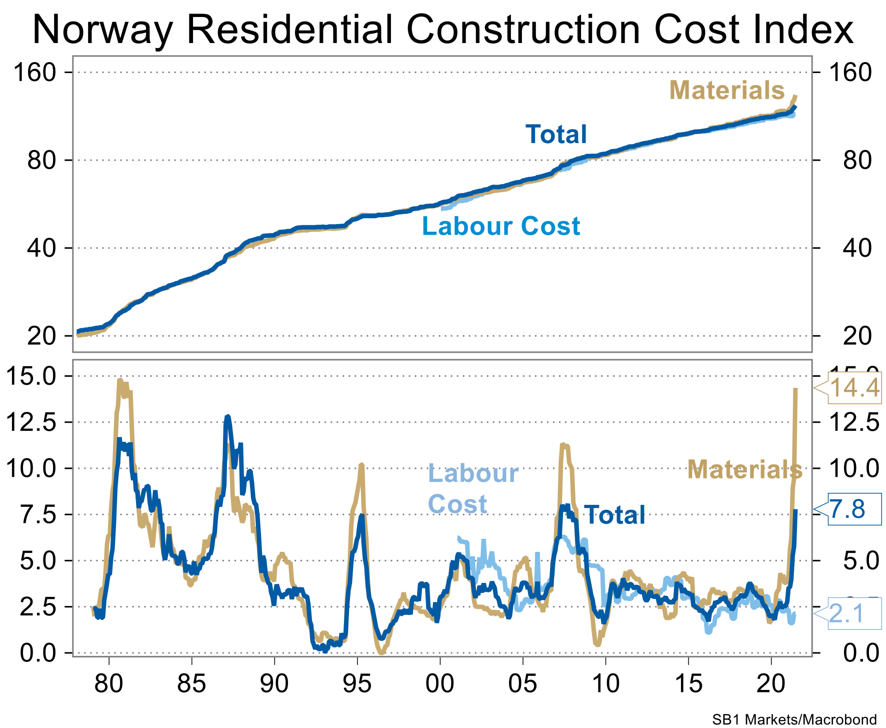


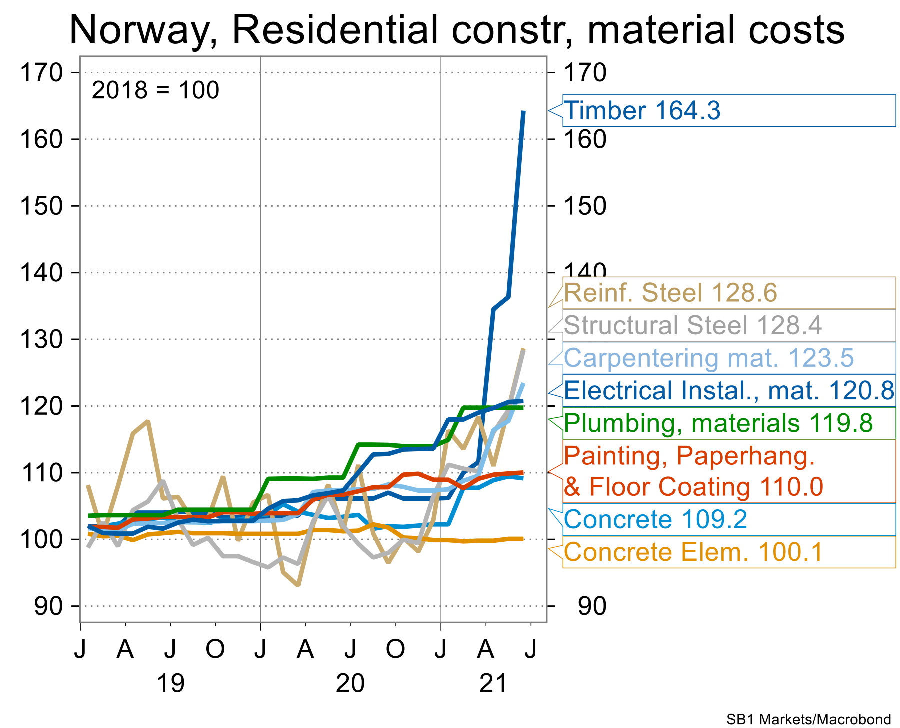


- Electricity prices are volatile, and explains much of the volatility in headline Norwegian CPI
- Last year electricity prices collapsed alongside oil prices. Now both have recovered – which pushes CPI up by 1.4 pp (with a small contribution from gasoline prices)
- Electricity futures signal higher spot prices the coming months – and a substantial decline next year

‘Some’ cost pressure in the Norwegian construction sector too

But ‘just’ from some materials; lumber & steel, plumbing & electrical materials

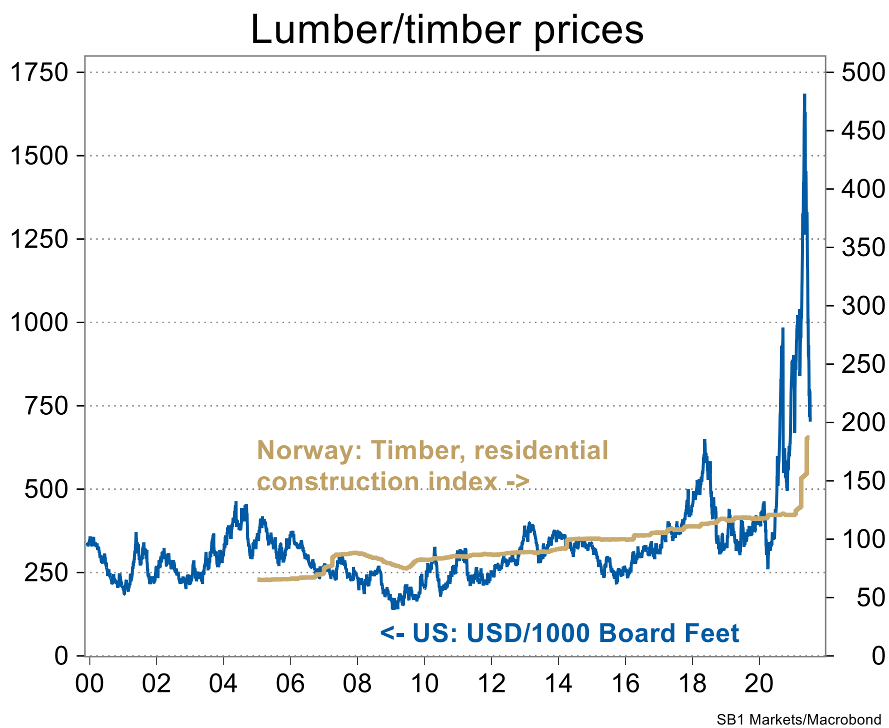




- Material prices are up ~~9.5~~ 14.4% in ~~May~~ June
  - » The 50%+ lift in lumber/timber prices over the past months is unprecedented
- Including labour costs, the total building cost index is up by 7.8%, the highest in almost 15 years

In the US, the lumber bubble has burst – if not totally (yet)

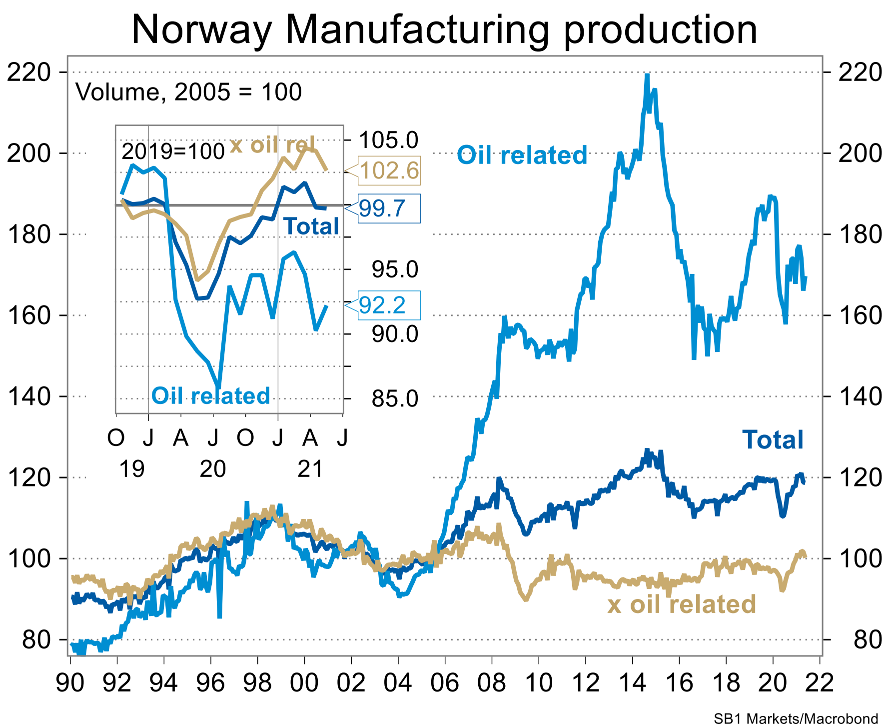
Raw material price cycles are normally not long lasting

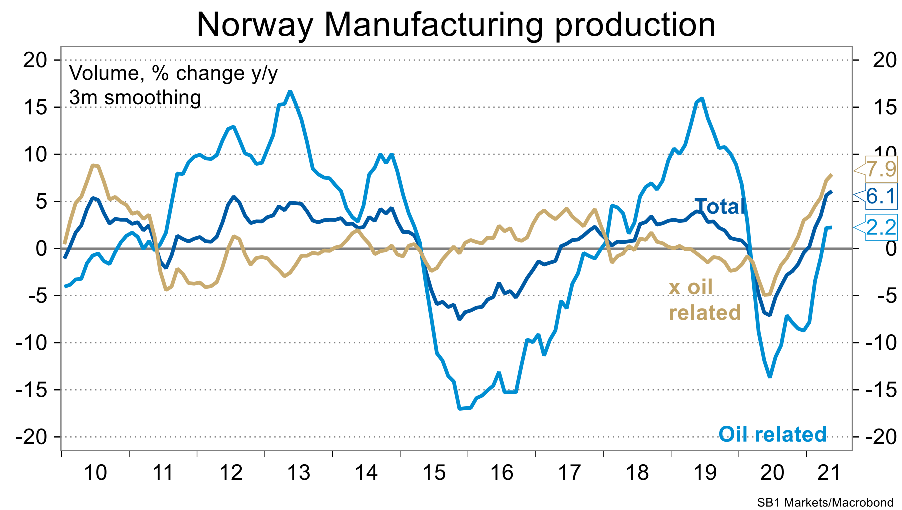


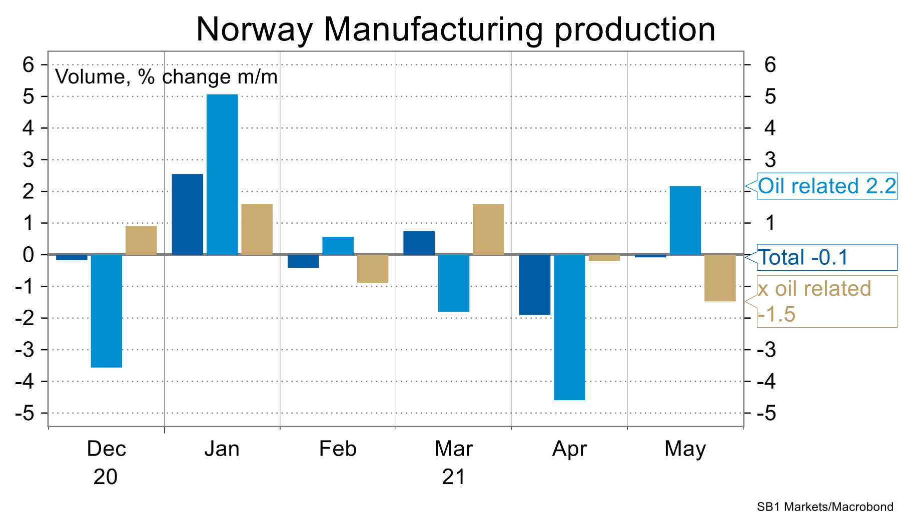
- .. And are not important for serious inflation cylces

Manufacturing production further down in May – we expected a steep rise

Production down 0.1% due to a decline in x-oil related sectors, oil related up 1.5%



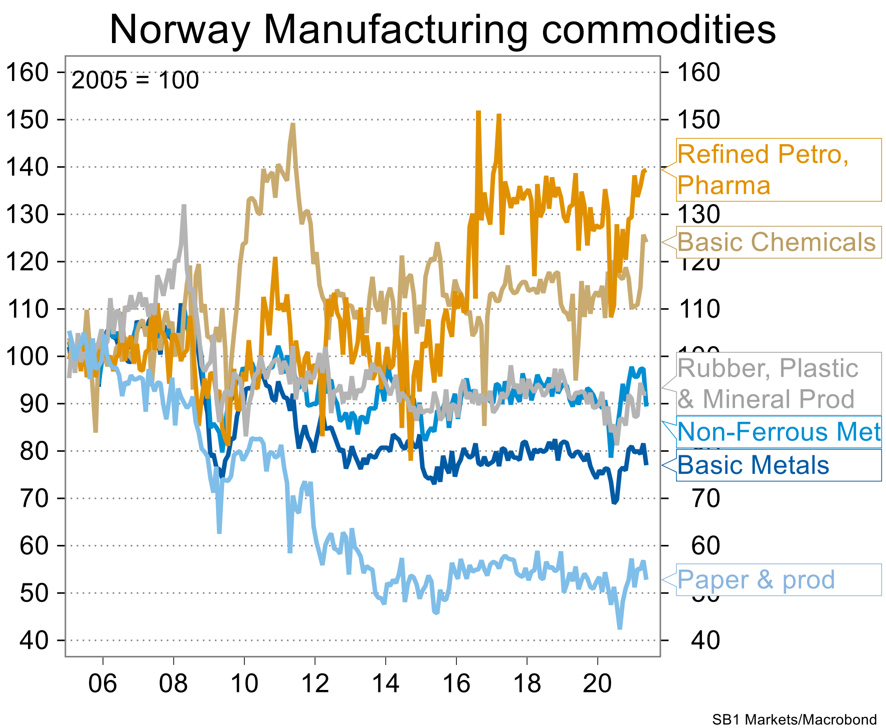


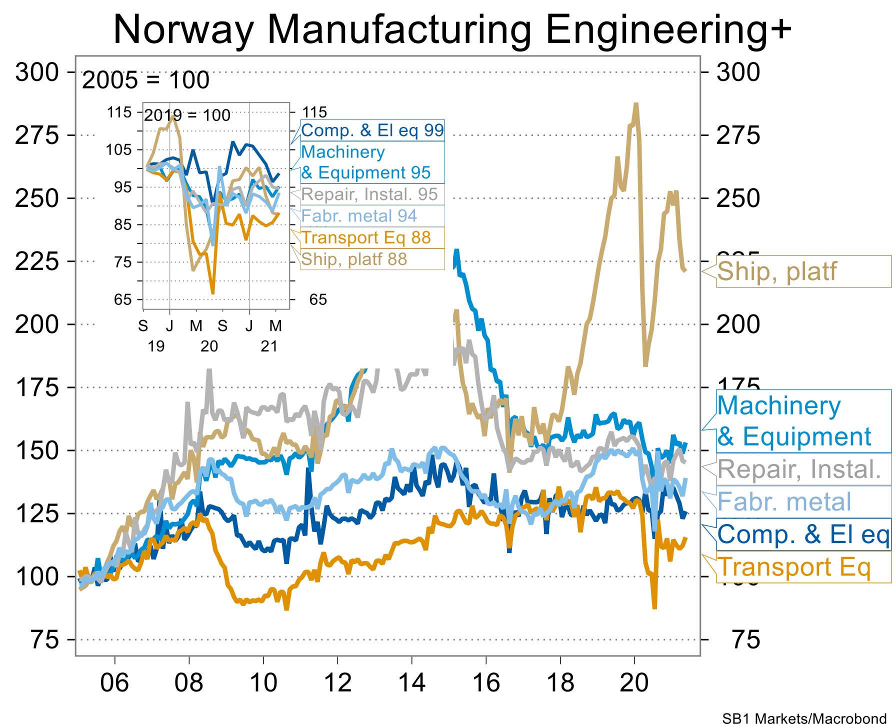


- Production fell by 1.9% in April and we expected a recovery in May – which did not materialise
  - » Oil related manufacturing production rose by 2.2% other sectors were down 1.5%, mostly due to metals, food
- However, as manufacturing surveys are signalling strong growth in activity, we expect decent production numbers the coming months
- Production x oil related sectors are well above the pre-pandemic level, a the peak level the past 12 years

Metals weaker in May, chemicals better.

Engineering (and oil related) industries are still operating below normal levels

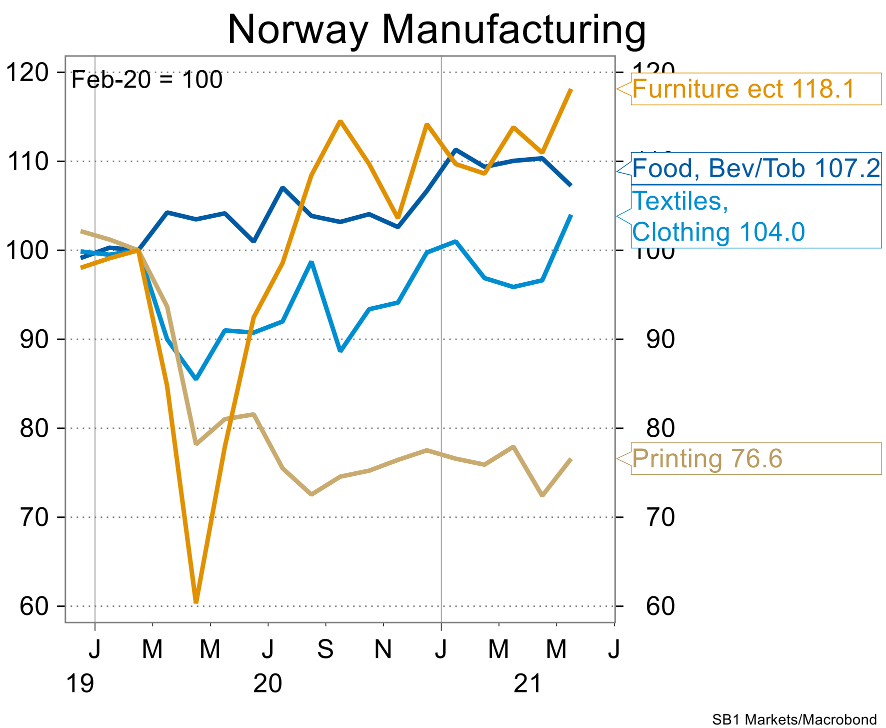




- **Production of ships & platforms** was incredibly strong in 2018/19, then fell 30% in H1 last year but has now recovered sharply since last summer but has sagged the past two months
  - » Corona measures (lack of foreign labor, contacts with foreign vendors/customers), supply chain challenges probably explained parts of the recent drop
- **Commodities** have are on the way up – but were mixed in April/May

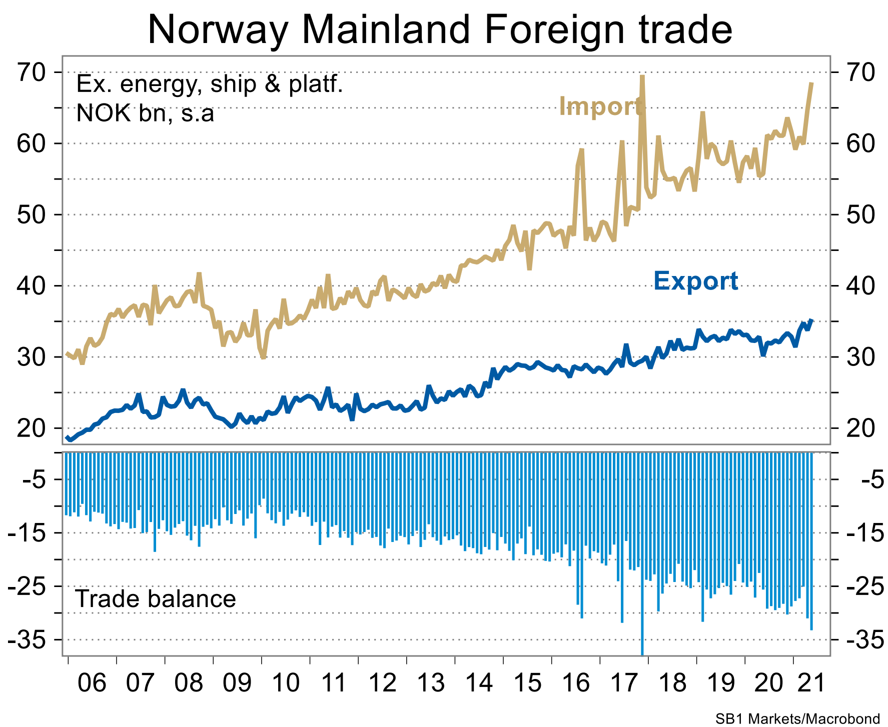
Furniture production up 18% vs pre corona!

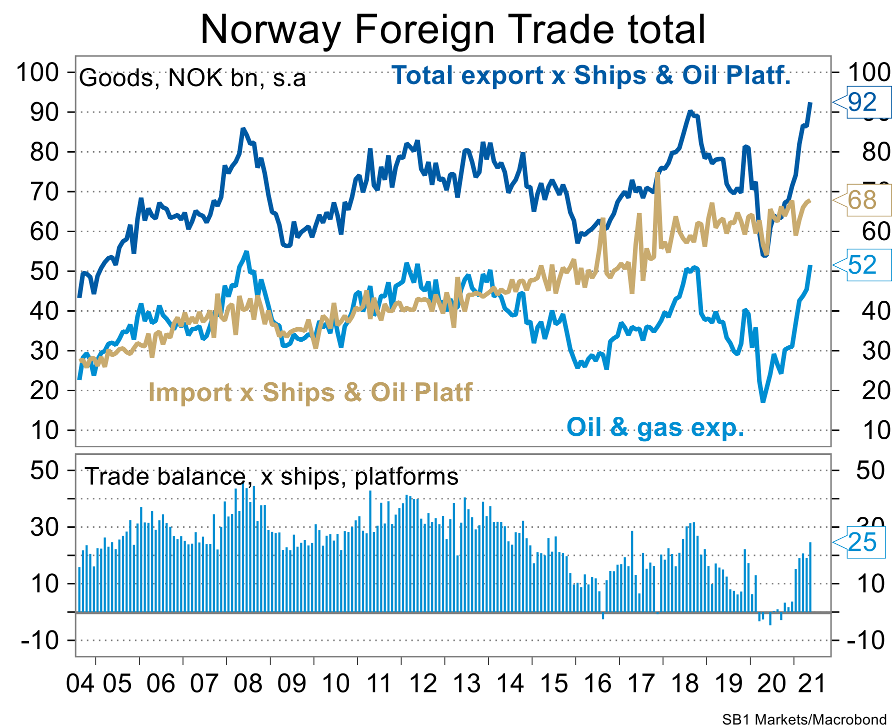
Food production is supported by closed borders



Mainland trade deficit higher in May as imports increased by 9.5%

Total balance surplus up in May, equaling 11% of GDP

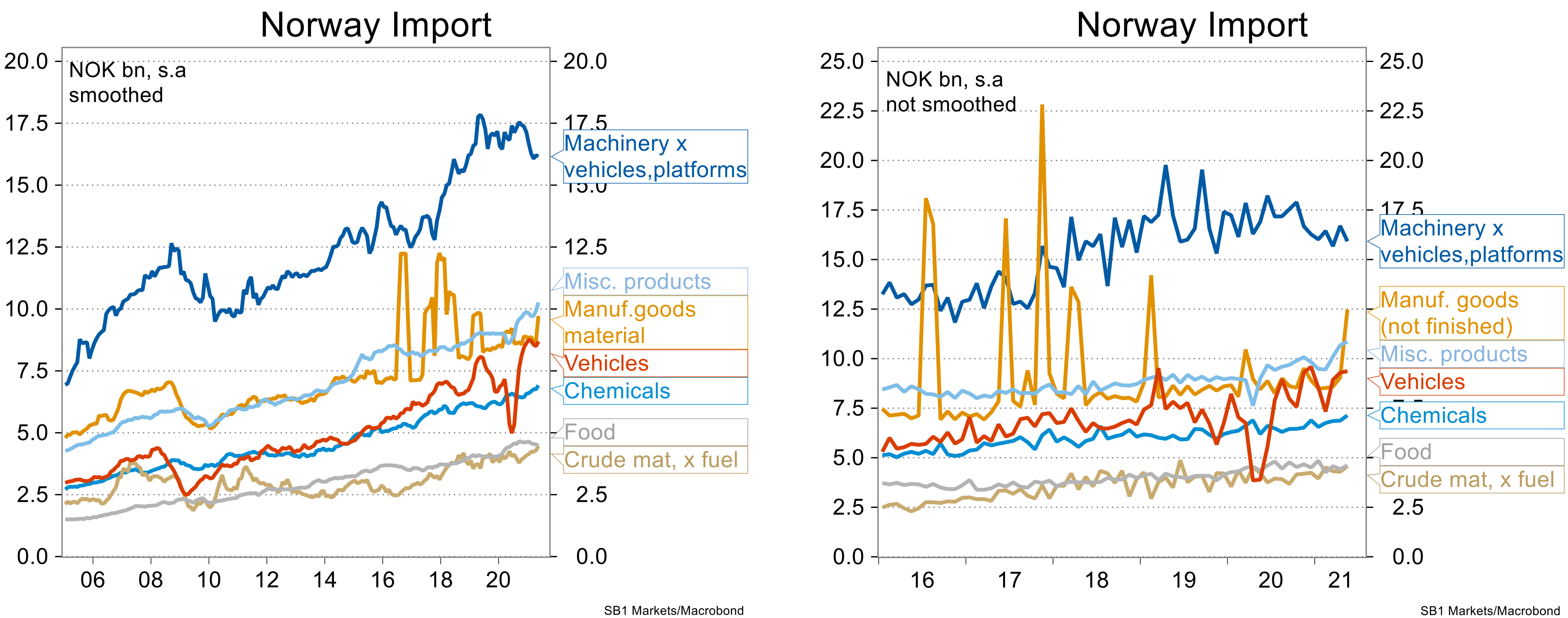




- **The <u>Mainland (non energy) trade deficit</u>** <u>in goods</u> rose quite a bit again in May, after the jump in April.
- **Non-energy exports were** again at ATH in May. The main contributors on the upside for exports were crude materials, metals, chemicals, and other manufactured goods
- **Import** rose sharply of which a substantial part (almost 50%) of the 9.5% increase in imports are due to a likely one-off, 'manufactured goods, not finished', probably a ship or a platform. The underlying trend for import
- **Export of oil and gas**, helped by higher prices, is well above pre corona levels, totalling 52 bn in May (+7 bn m/m), bringing the total trade surplus to 25 bn, or some 11% of GDP. We are not broke, yet

Machinery imports down in May, all others up – signalling OK domestic demand

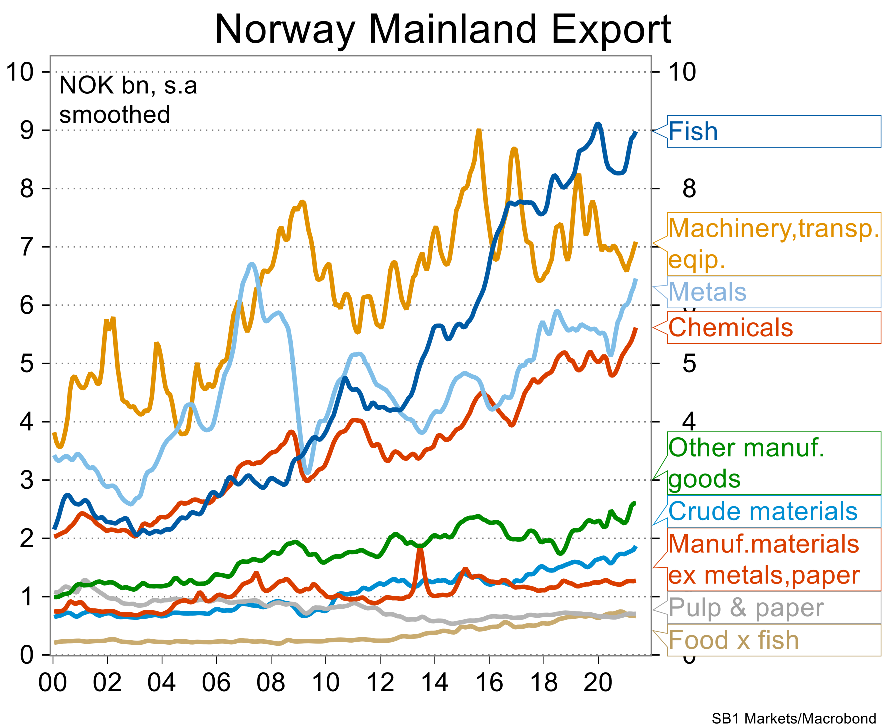
Manufactured goods up 38% m/m, probably platform or a ship not yet finished

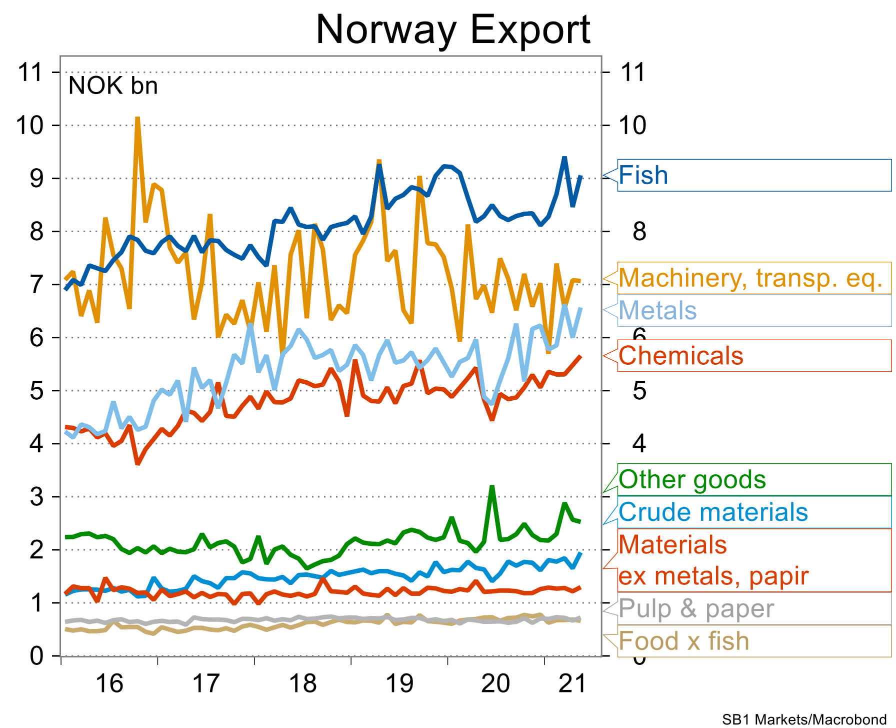


- Imports of chemicals, crude materials, and food have all increased y/y. Machinery imports are down 7% from May last year. Manufactured materials exports had been virtually unchanged for some time, before increasing 38% last month
- Vehicle imports slowed rapidly in H2 2019 and early 2020, along with auto sales. Since April '20, imports have shot up to the highest level ever, but was only marginally up in May

Most exports higher in May

Just machinery exports are struggling

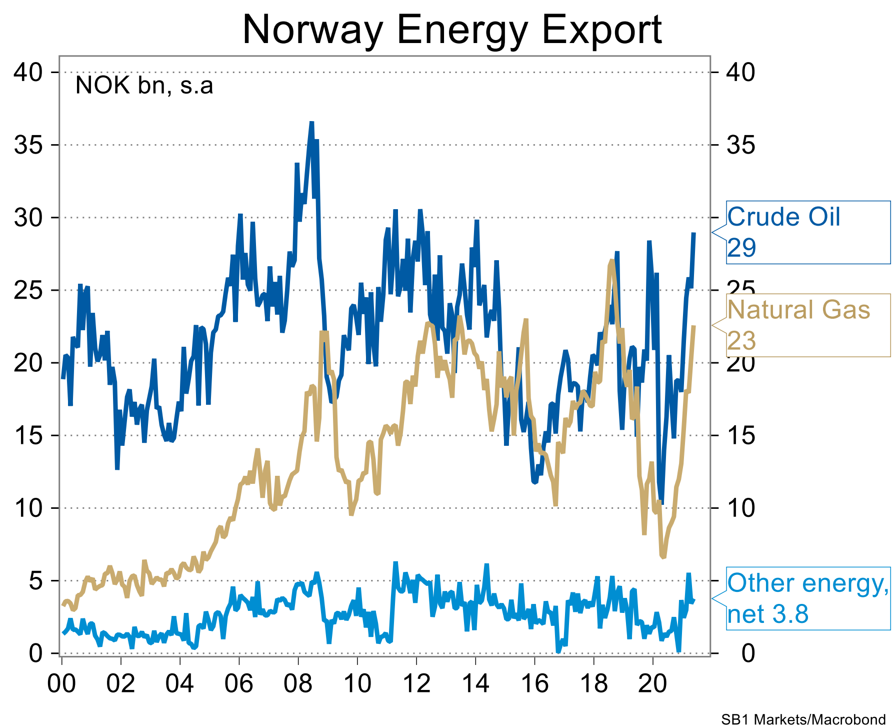


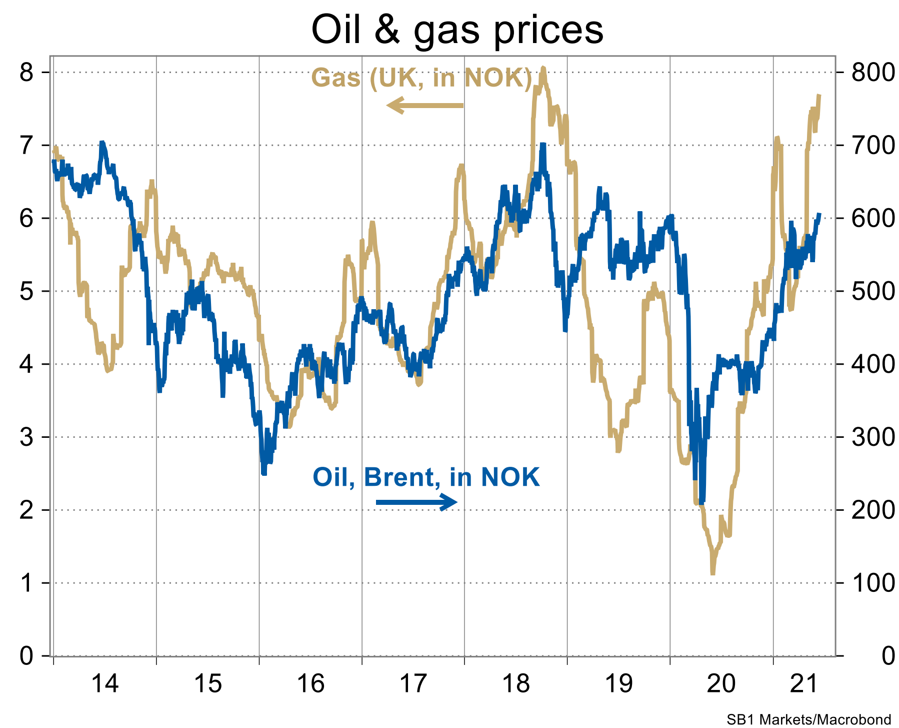


- Exports of machinery and transport equipment (of which much is related to oil activities abroad) is trending down, very likely due to lower oil sector investments abroad
- The main contributors to the m/m increase in mainland exports were crude materials, metals, chemicals, other manufactured goods, and fish

It’s stating the obvious: Oil & gas exports increased as prices increased

Gas prices are soaring (Thank you, Putin). Oil prices are back to a rather high level too





- **Crude oil** exports (in NOK bn) fell rapidly in March and April 2020 as the oil price dropped and global demand subsided. Exports have turned up since then, with the oil price, and exports have recovered. In May (21), crude exports were the highest since 2013!
- **Gas** export values fell sharply during H1-20 but has recovered to above pre-corona level as gas prices recovered substantially – to the best level since 2018. Export volumes are up over 10% y/y

Highlights

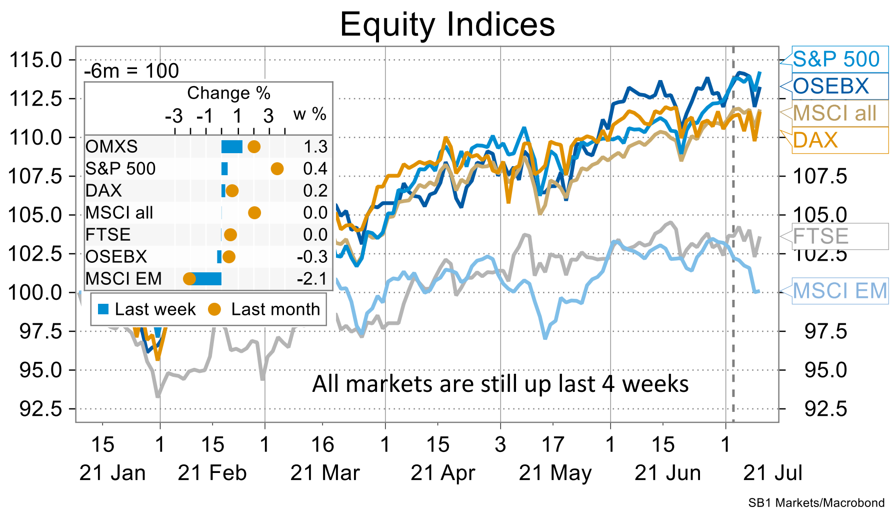
The world around us

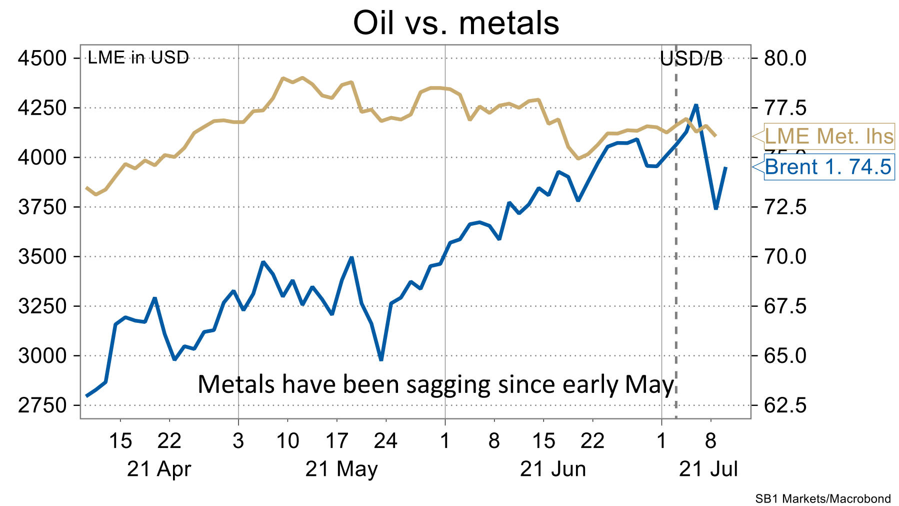
The Norwegian economy

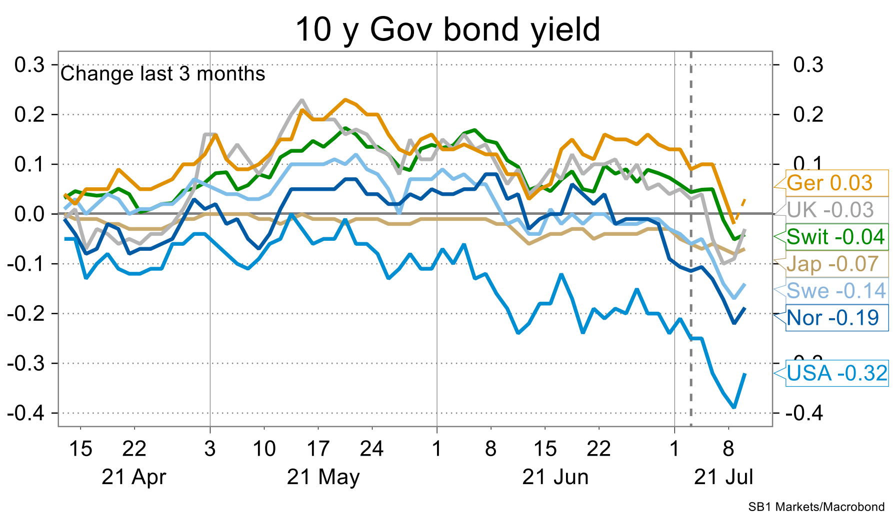
Market charts & comments

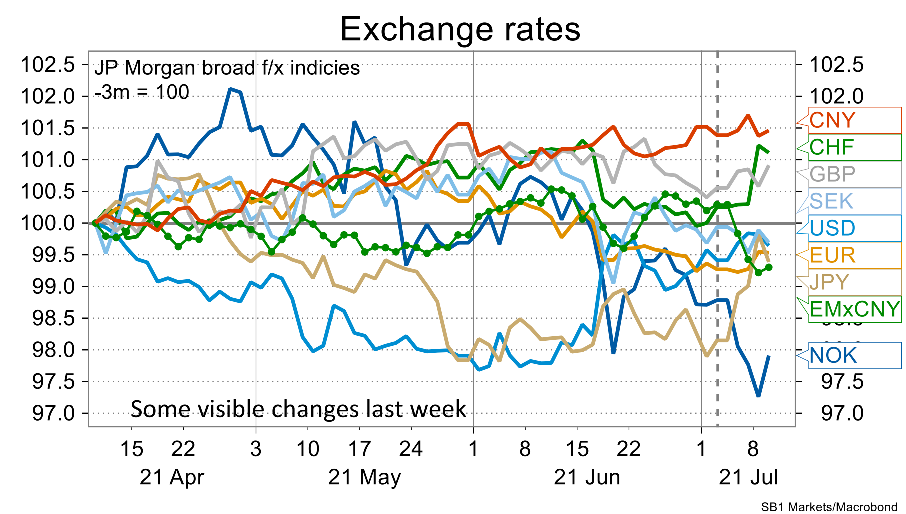
Most stock markets up, yields still down – and 'more' than commodities

EM (and super cyclicals) f/x down on growth angst





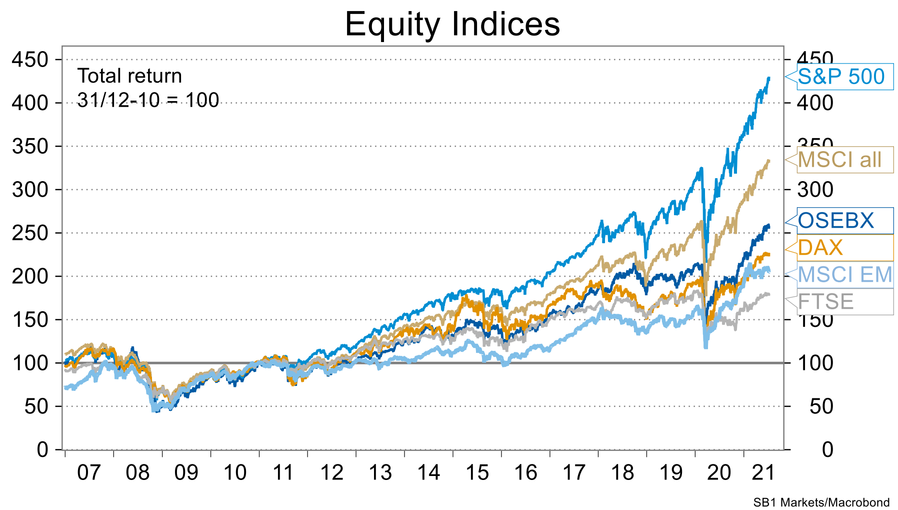


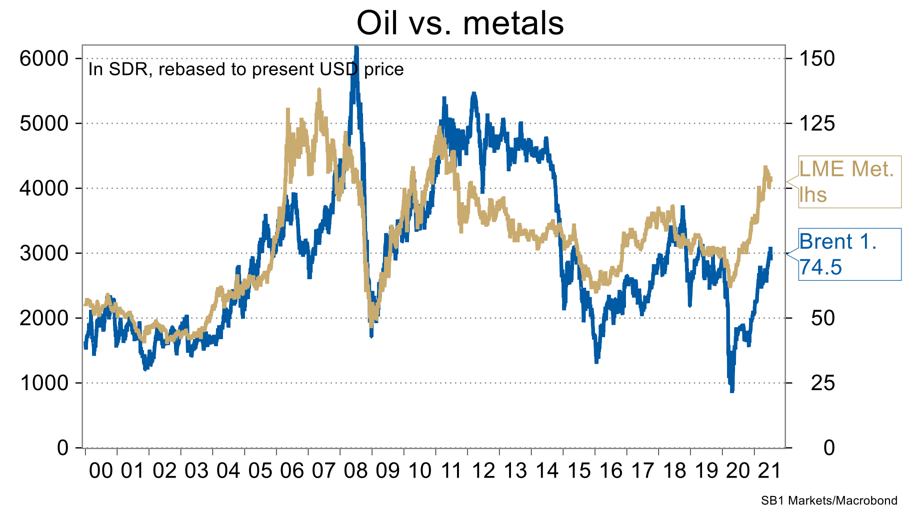


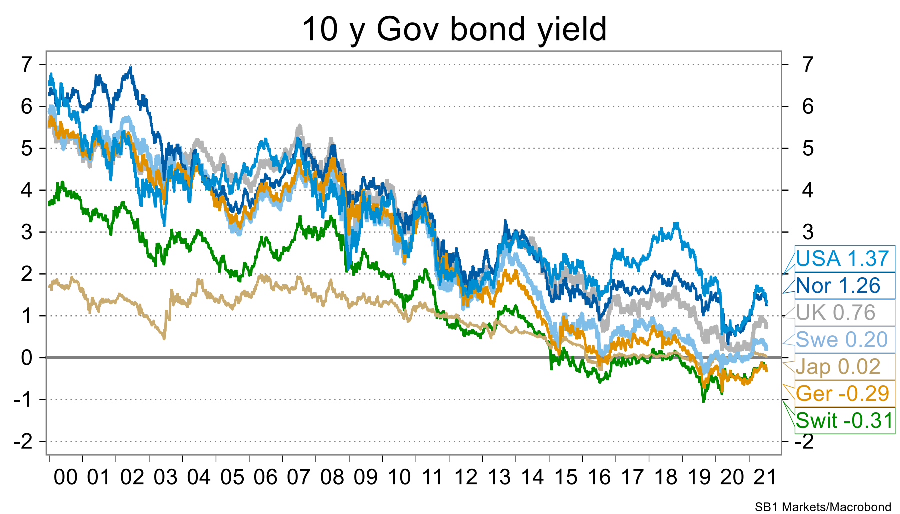
SpareBank 1 MARKETS

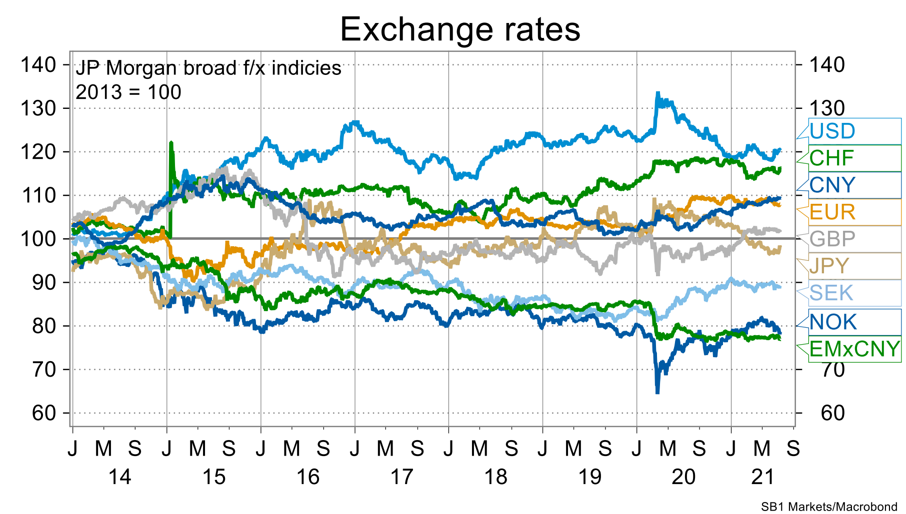
The big picture: Strong stock & commodity markets. USD trend is still down

The MSCI World at ATH this Friday too, as were several local markets. And bond yields trend down!

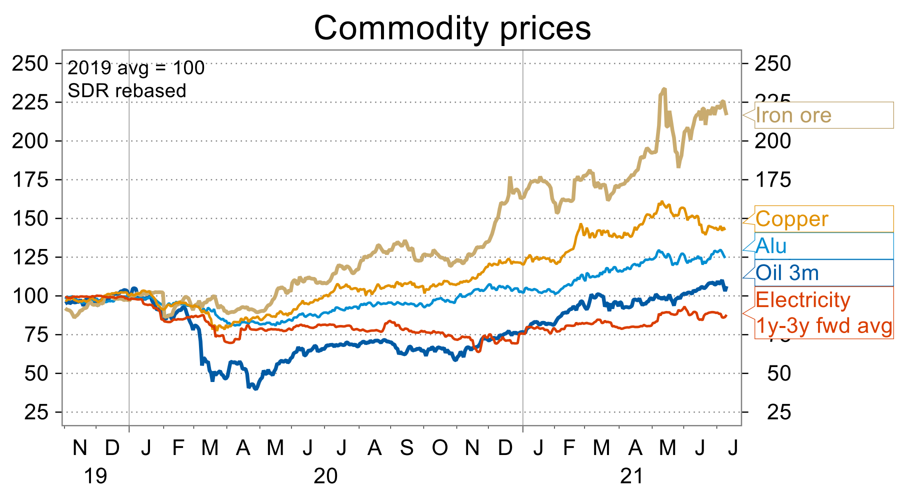


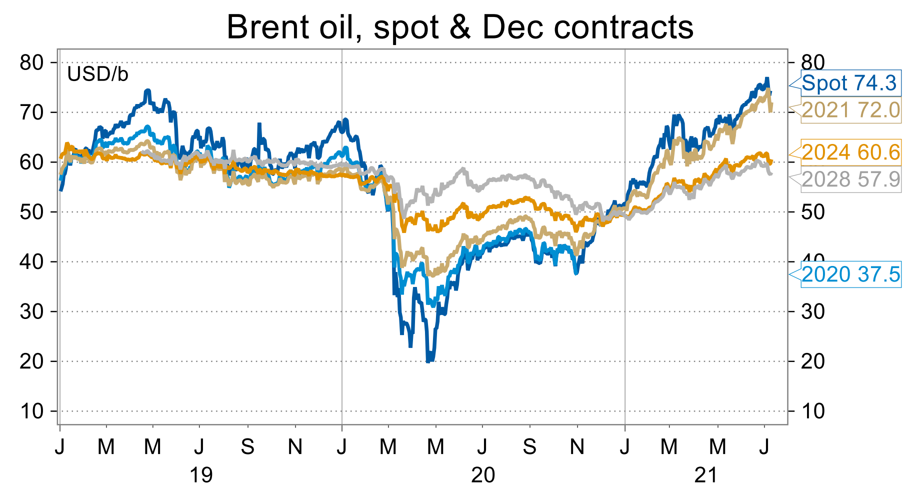


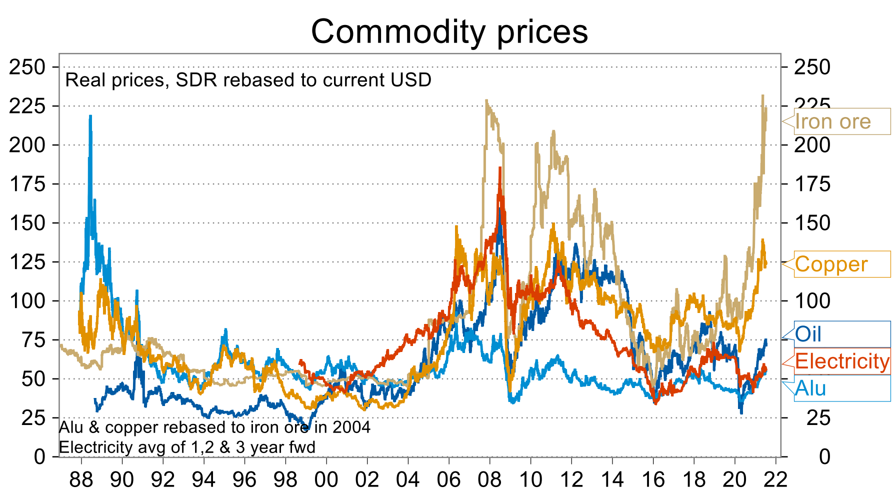


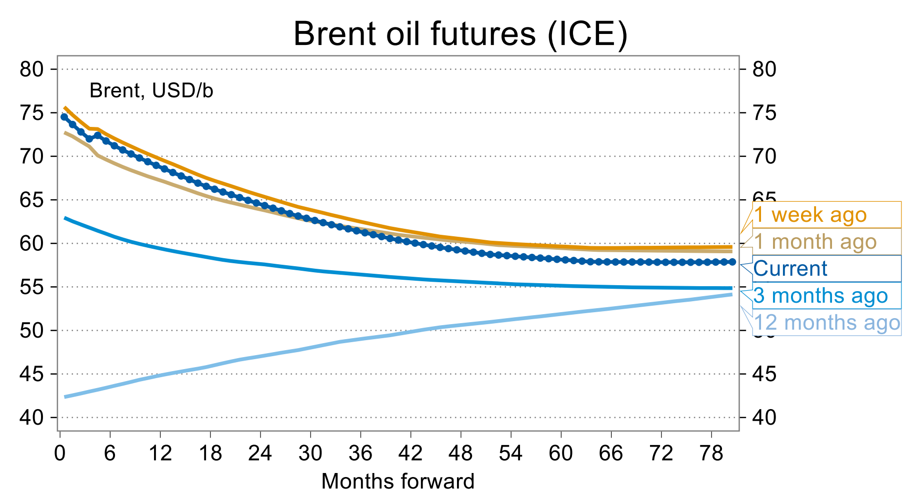


A small commodity setback

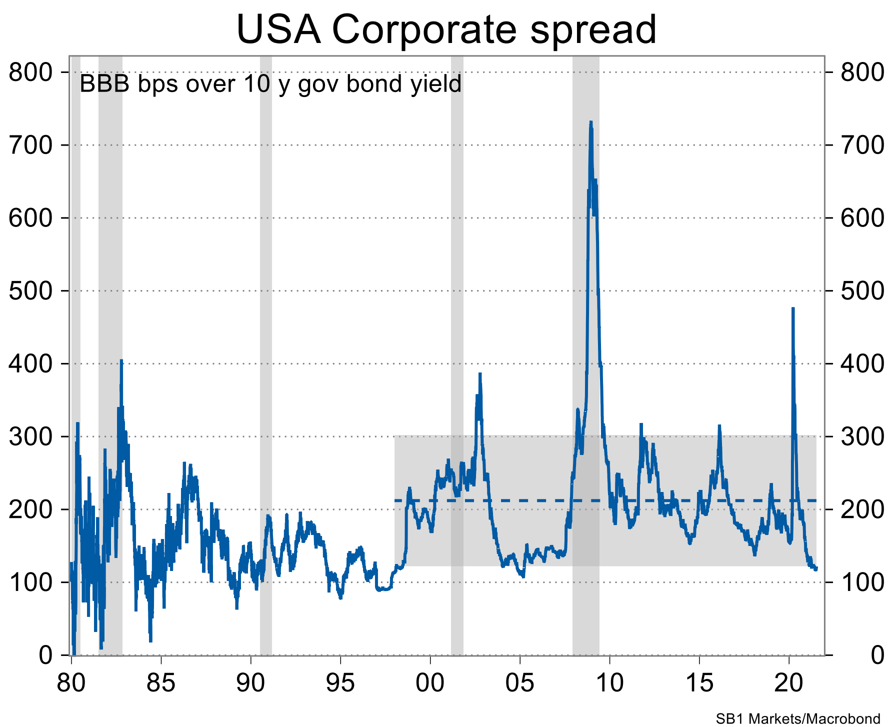


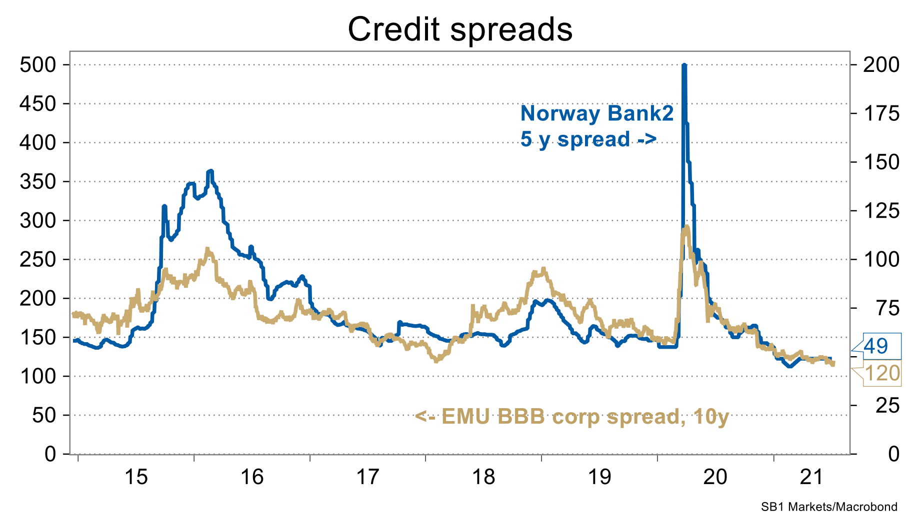






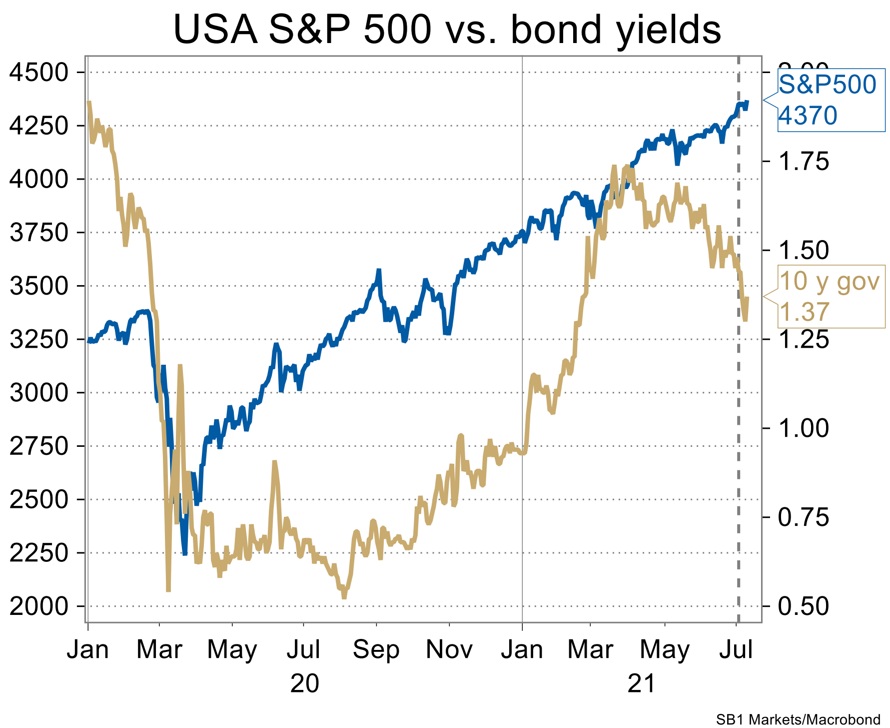
US credit spread slightly up last week – still at very low levels of course

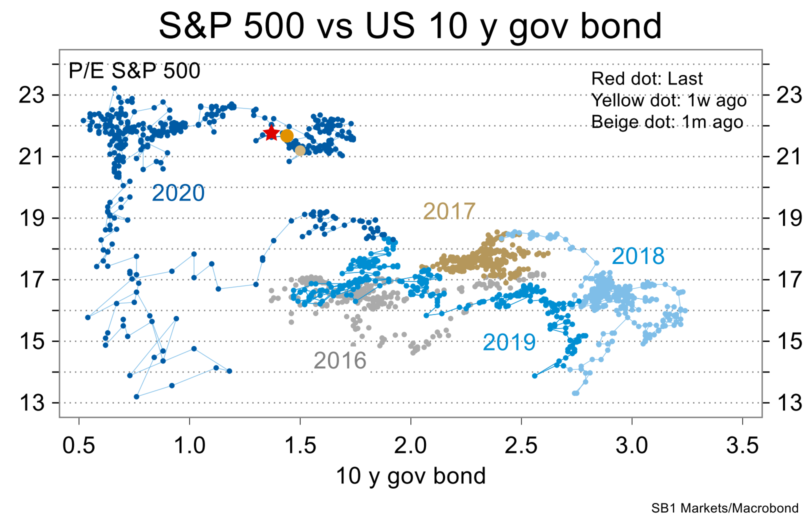


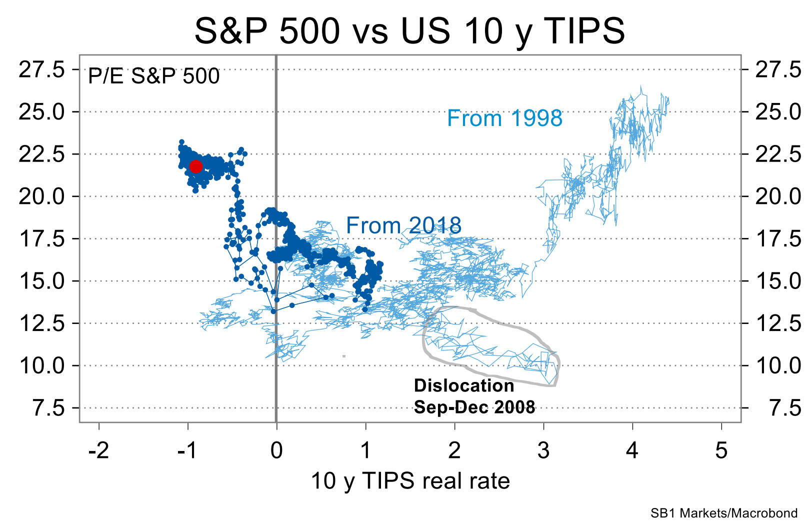


S&P 500 +0.4% to another ATH, the 10 y bond yield -7 bps, to 1.37%

… even if yields rose on Friday

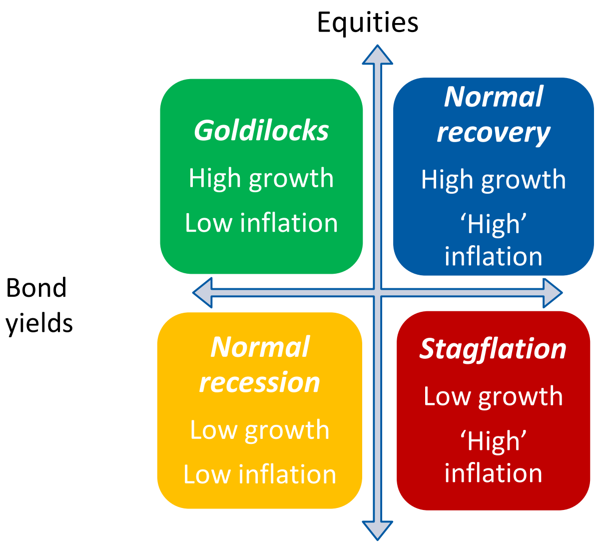


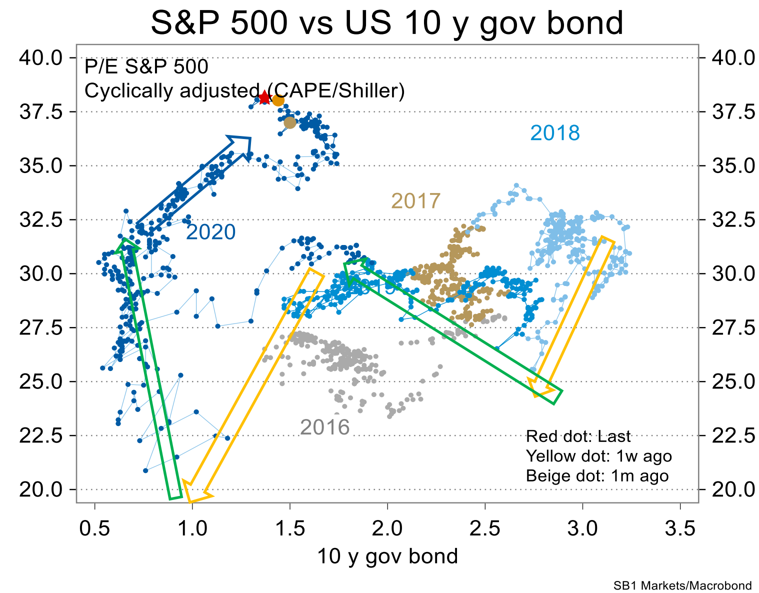




Further into the 'Goldilocks corner'

But will markets remain there? Actual wage/price inflation dynamics will in the end decide. And not the Fed…



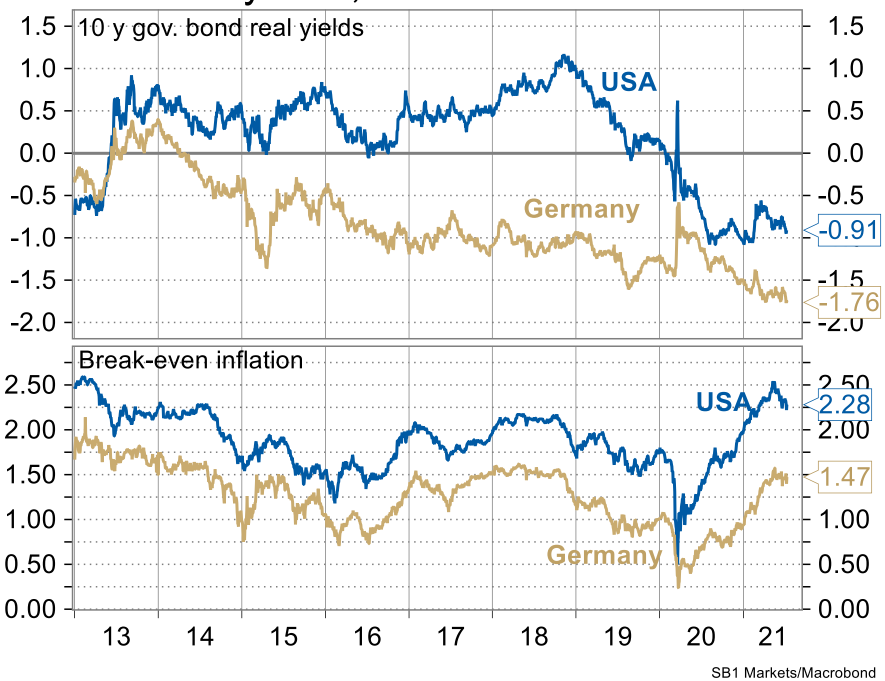


- Usually, we have associated drifts towards the 'green corner' - low inflation and solid growth at the same time - as a temporary sweet spot for markets
  - » Interest rates have climbed 100 bp+, and stock valuations have kept up or climbed (like the Shiller PE). Still, we deem the current yield level to qualify for the "Goldilocks" corner (especially the real bond yield, check the chart on the previous page). Where to go from here?
- The inflation/growth mix will decide:
  - » If 'nothing' happens, we can stay in this Green quadrant. Raw material prices normalise, wage inflation is kept in check because the US labour supply finally returns to normal. Inflation turned out to be transitory, profits are OK, yields remain low
  - » If the labour supply in the US does not yield, wage inflation will very likely accelerate
    - If companies are able to increase their selling prices, profits will be kept up, but higher inflation well very likely push the Fed to tighten monetary policy, which is challenging for high multiples. Move to the blue quadrant. However, after a while profits will anyway come under pressure. The stock market will be rewarded with lower profits & lower multiples (it will resemble the Red corner, before moving to the Yellow)
    - If companies are not able to increase their selling prices, inflation will be kept in check but profits will decline rapidly. A 2% lift in wages, cuts profits by well above 10%. That's the Yellow corner

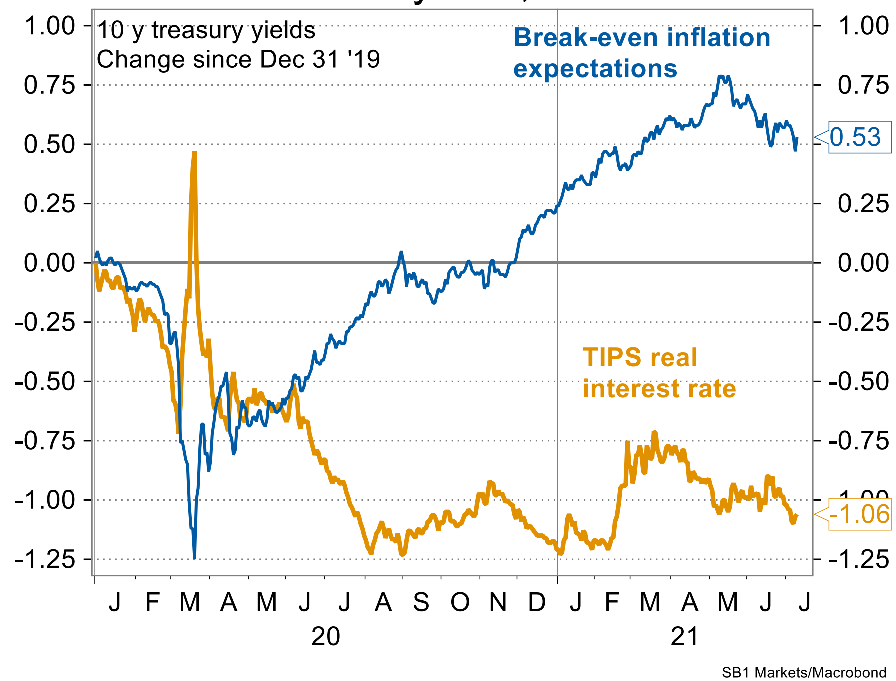
Both real rates and inflation expectations are heading down in the US

In Germany, just the real rate took the beating as the ECB lifted the inflation target to 2%

Real yields, break-even inflation



USA Real yields, inflation



US & Germany 10 y Gov bond yield

	Yield	Change 1w	Change 1m	Min since April-20
USA nominal treasury	1.37	-0.07	-0.13	0.52
.. break-even inflation	2.28	-0.05	-0.04	1.06
.. TIPS real rate	-0.91	-0.02	-0.09	-1.08
Germany nominal bund	-0.29	-0.06	-0.05	-0.65
.. break-even inflation	1.47	0.02	-0.01	0.40
.. real rate	-1.76	-0.08	-0.04	-1.77

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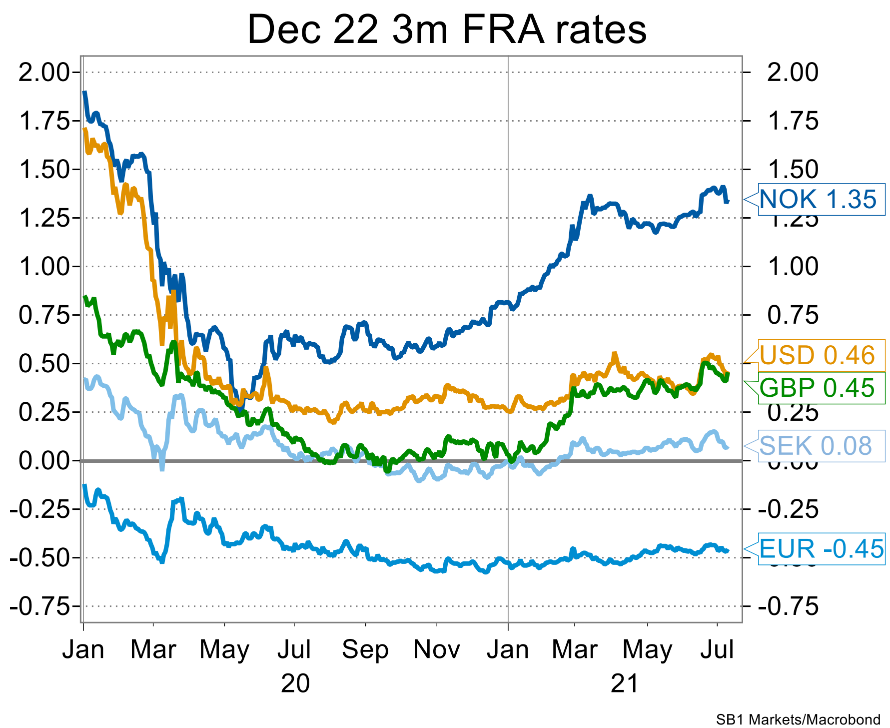
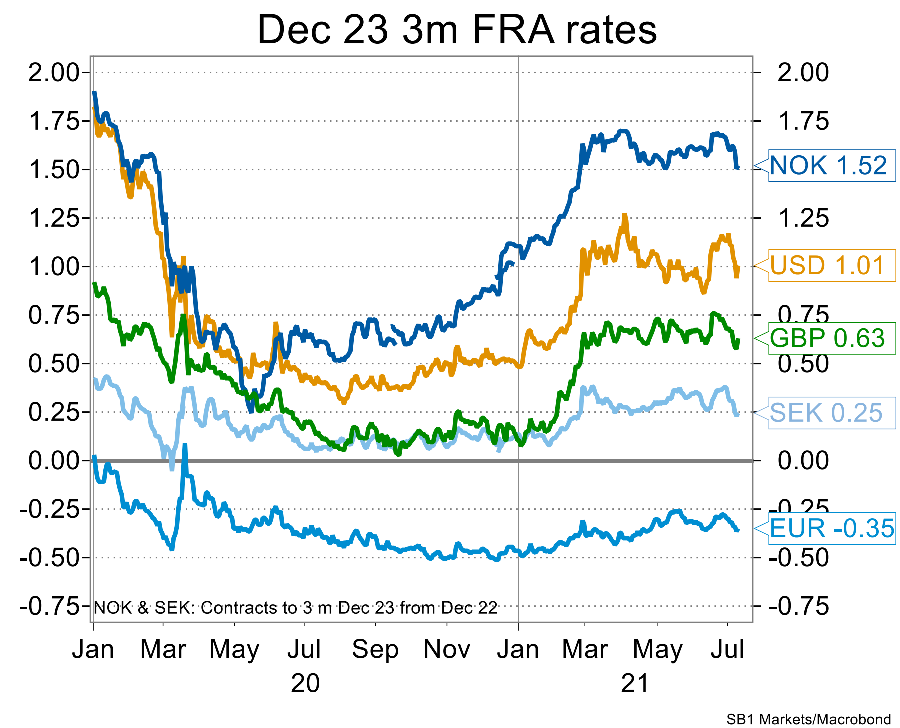
- The German real rate is close to the lowest level ever, at minus 1.76%, per year, the next 10 years. Think about that…

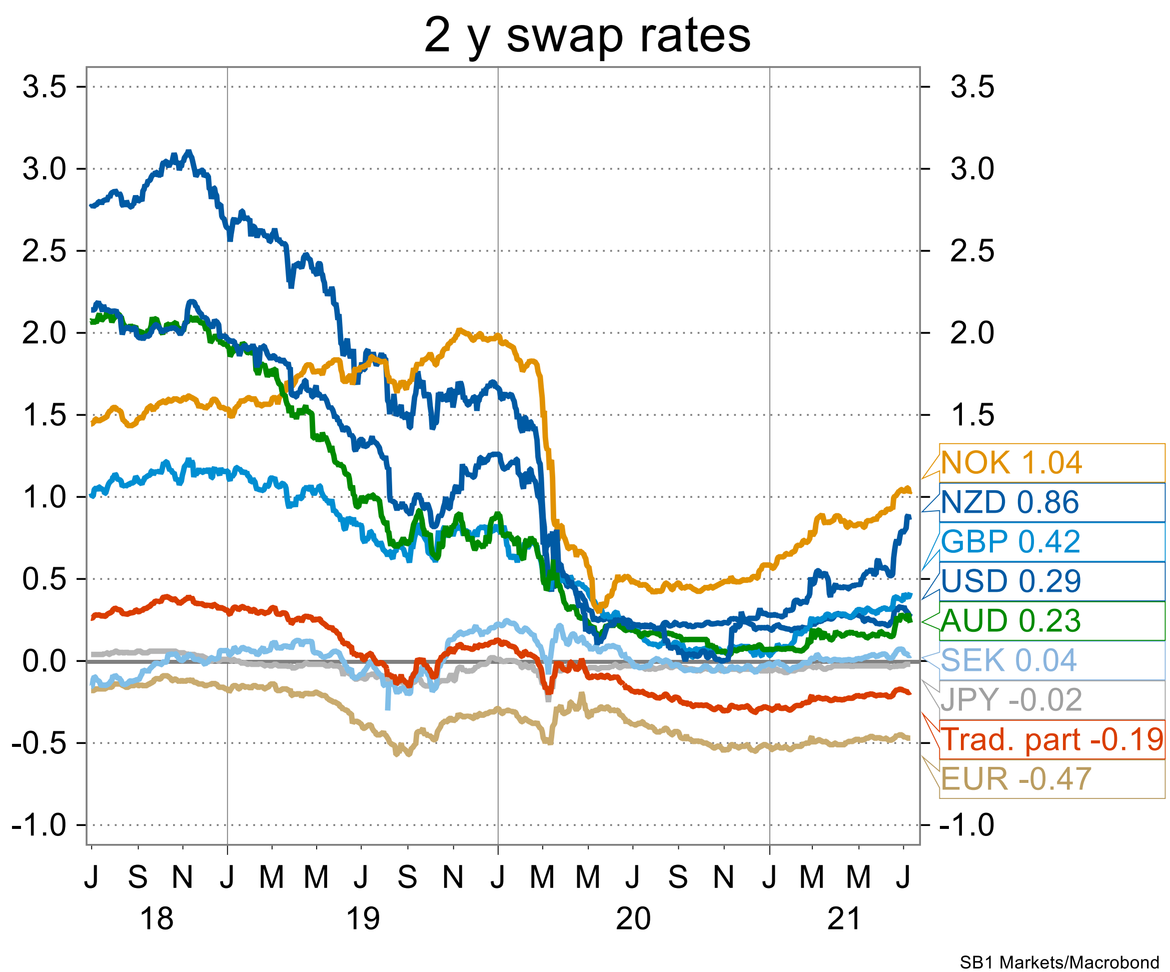
FRAs: rates down across the board

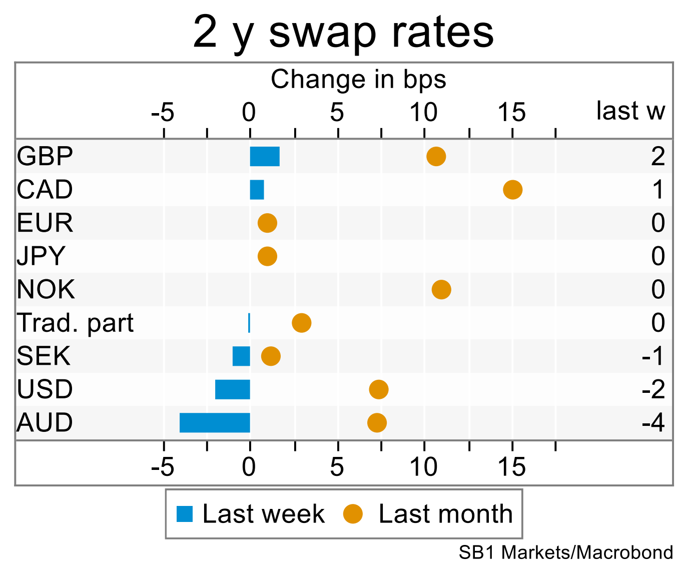
Still, the market discounts a first Fed hike in 2022





Mixed in the short end of the curve





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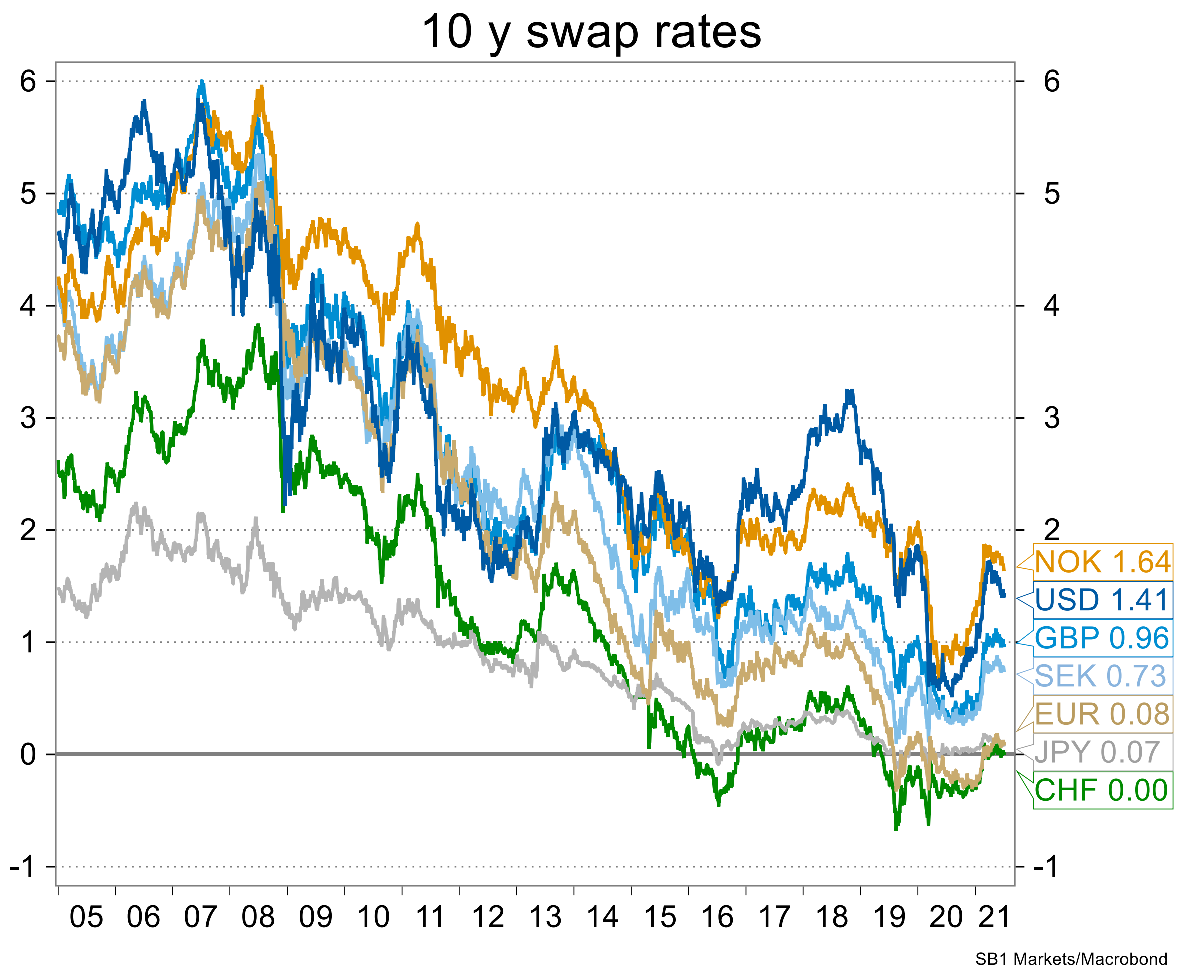
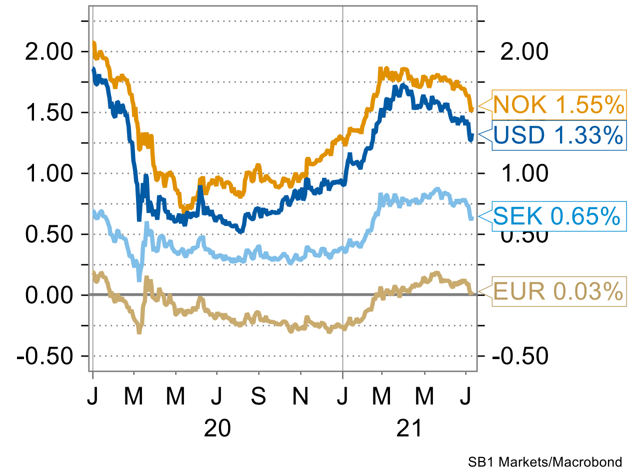
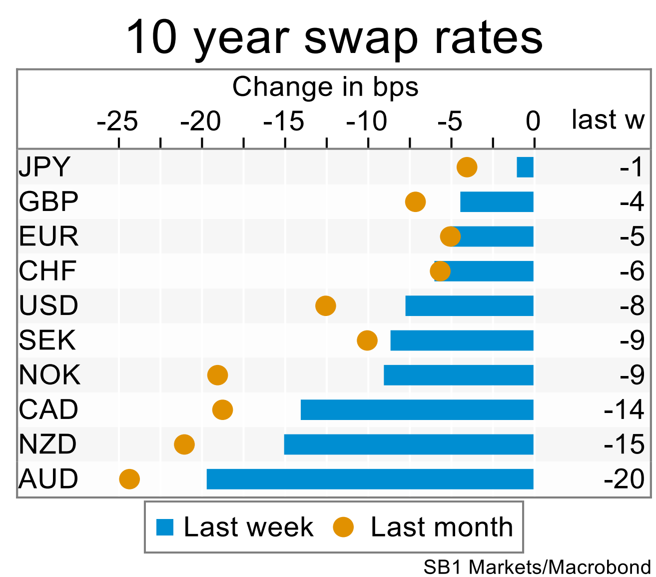
The long end of the curve down, everywhere

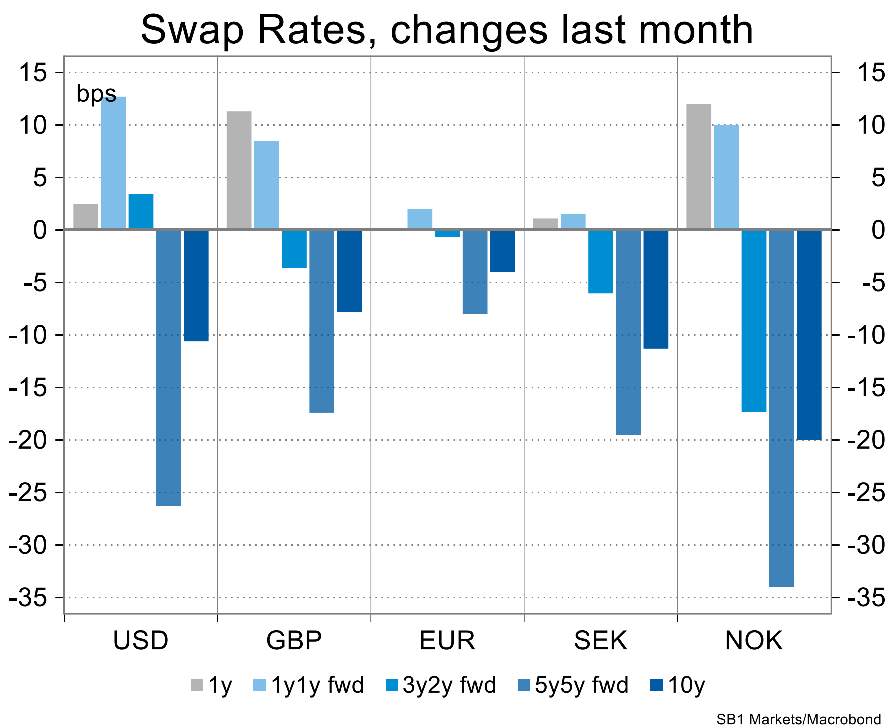
And by most in the ‘super cyclical’ countries (AU, CA, NO, SW)

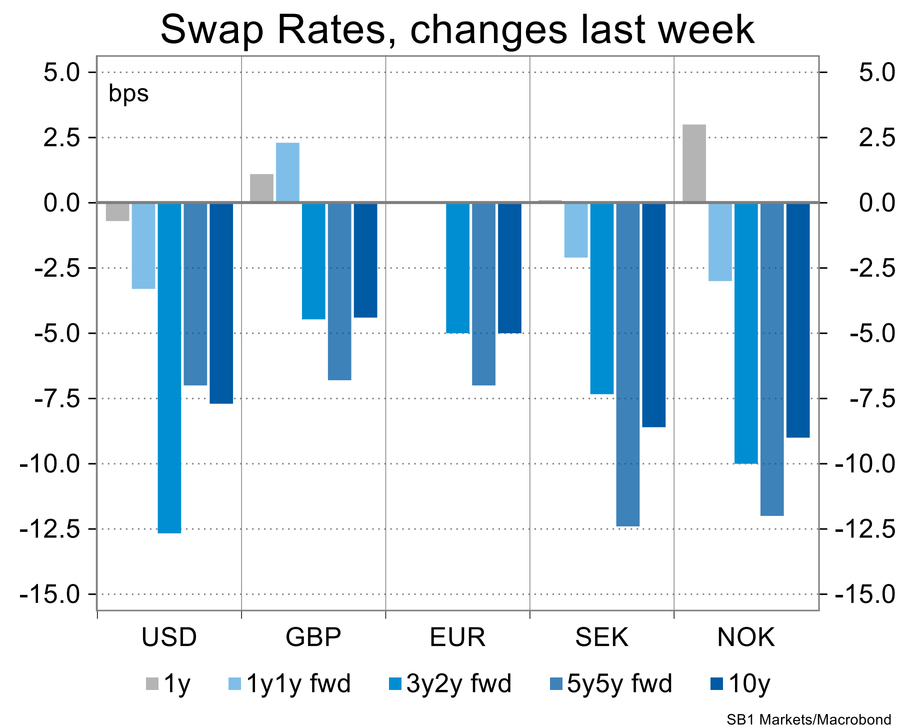




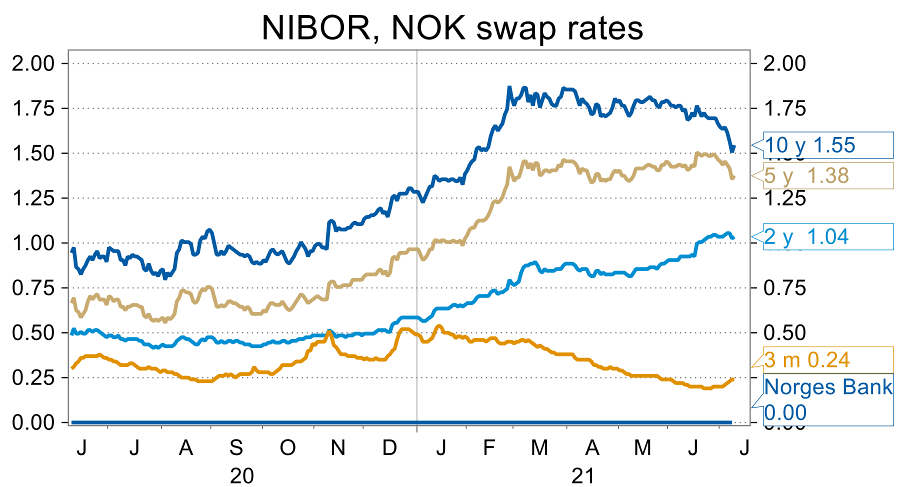


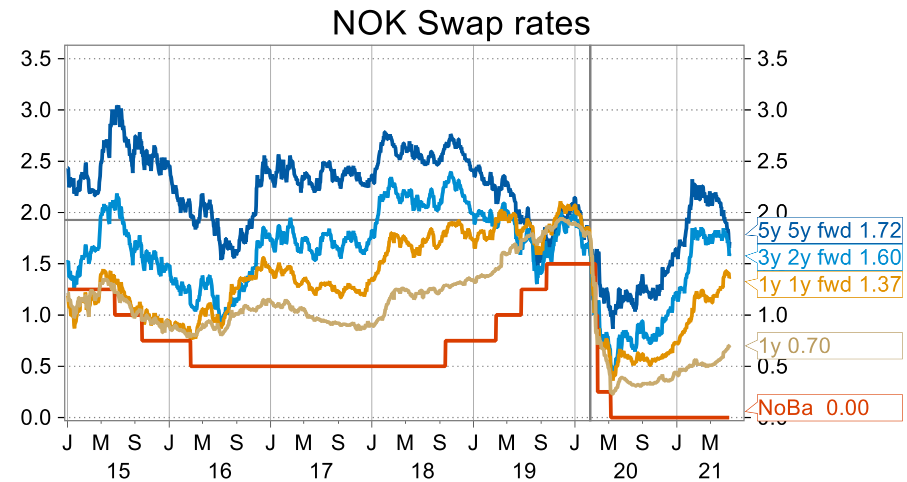
(Almost) all rates down everywhere

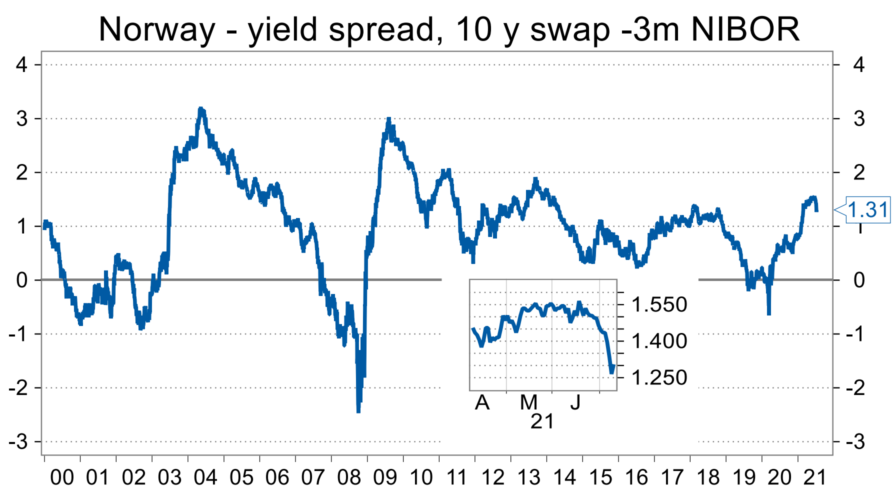


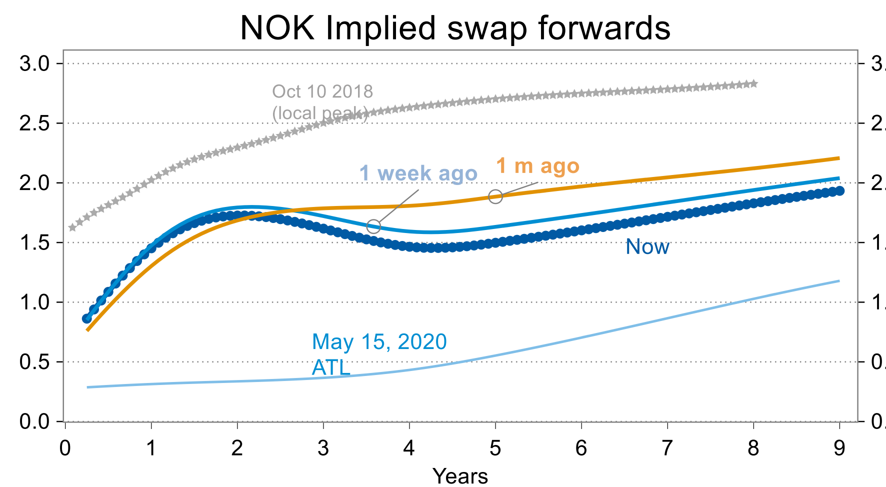


Implied swap rates down from 2 y onwards (as over the previous week)









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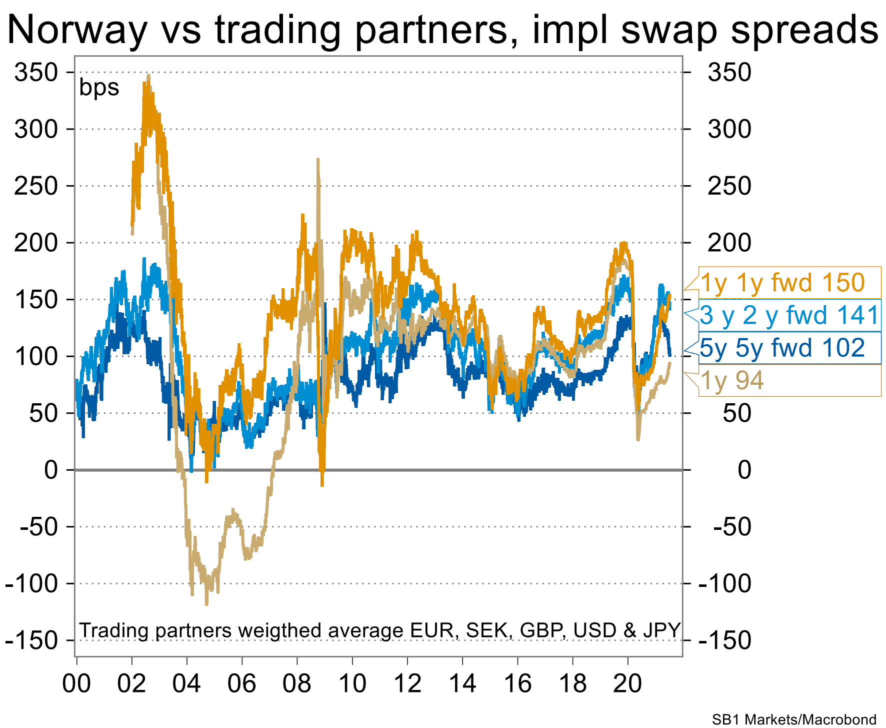
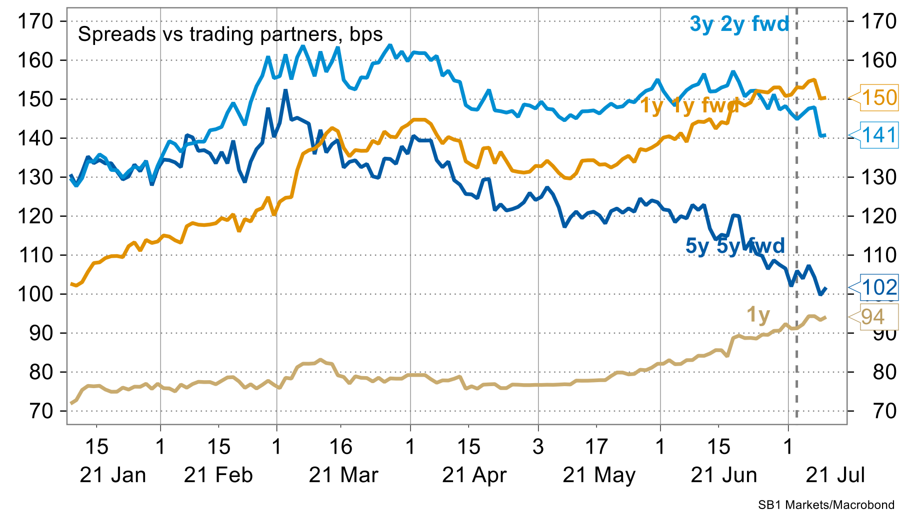
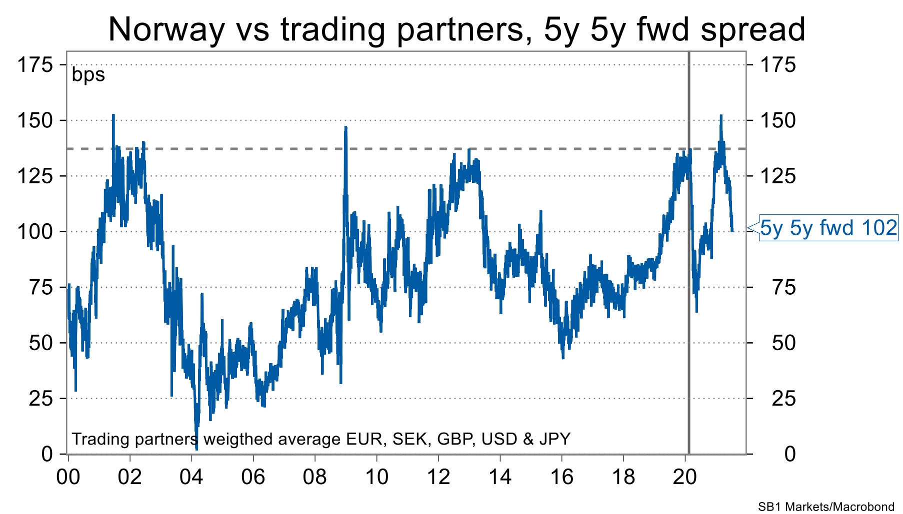
Forward spreads are twisting, up in the short end, sharply down in the long end







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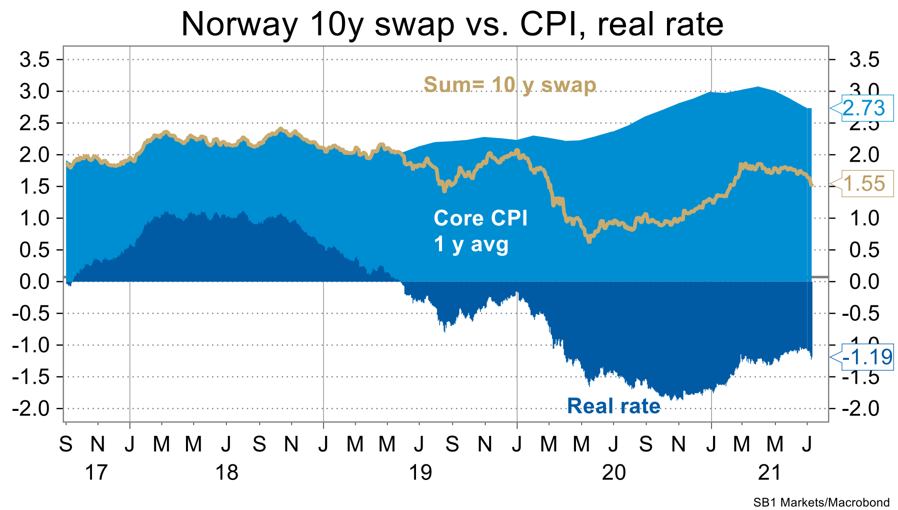
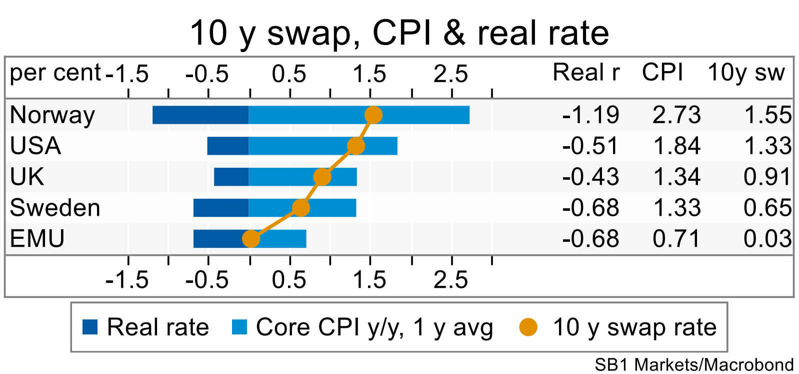
Negative (actual) real interest rates most places – NOK at the bottom



NOK 10 y swaps have flattened

- The **10y NOK swap** rate fell by 8 bps to 1.55% - and the trend has been down since March
- **The real rate**, after deducting 2.7%, an average core CPI inflation over the 2 past years equals -1.2%
  - » However, if we use a longer CPI inflation average, the real rate is higher, as the average rate of inflation has been lower than the current 2 y avg at 2.7%
  - » On the other hand, barring economists' in academia & finance, nobody else believe in the 2% inflation target. Other economists say 2.5% as to leaders in labour market organisations, business leaders 3.5% and households 3.7% (in 2 to 3 years' time)
  - » In seems unreasonable to assume an expected inflation below 2.5% - and in may in fact be that it is even higher than 3% among decision makers in the private sector

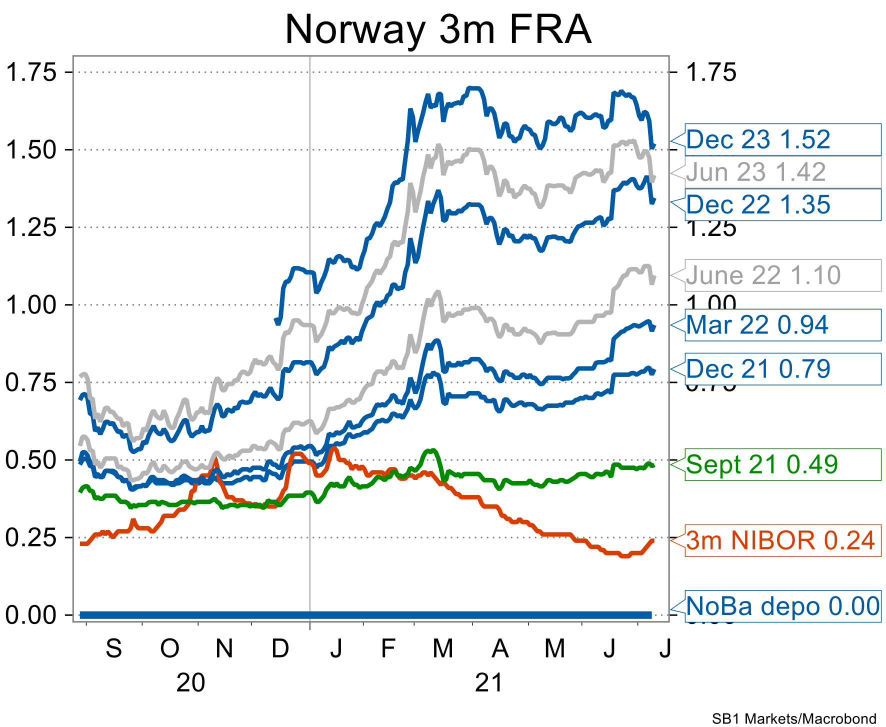


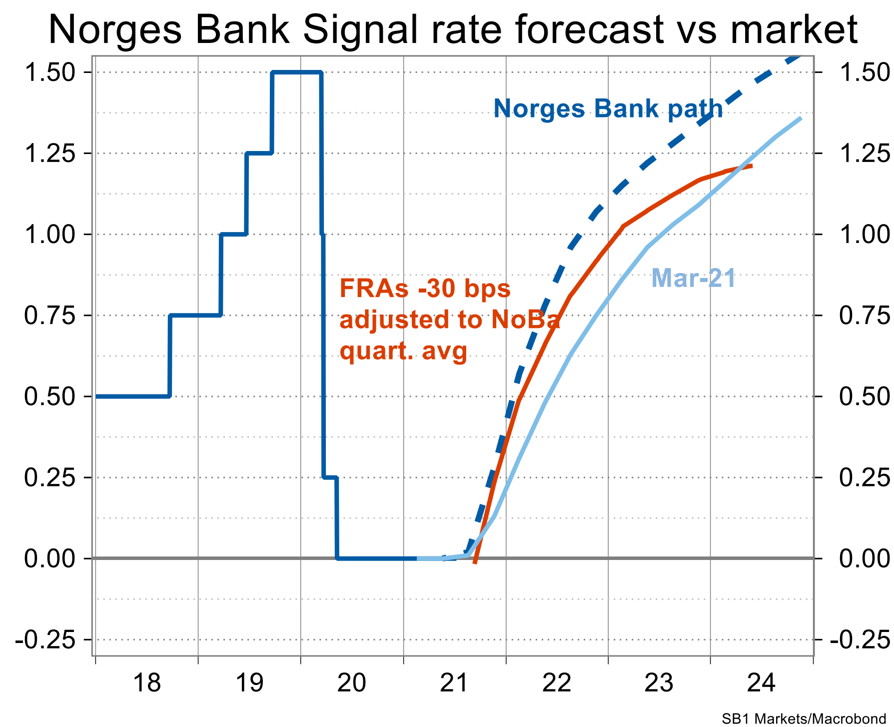
NOK real rates among the lowest, as inflation is at the top

- **Inflation** among main trading partners varies between 0.7% to 1.8% (here again measured by actual annual core inflation, smoothed over 12 months). EMU at the bottom, US at the top, the latter will climb rapidly the coming months
  - » Other measures of inflation trends, looking backward or including forward expectations yields the same ranking
- **Real rates** among our trading partners, and ranging between -0.4% and -0.7% measured vs. the 10 y swap rate and core inflation over the past two years
- **Thus, the Norwegian real rate at -1.2% is still an outlier on the downside, even if the nominal rate is the highest**

Longer dated FRAs sharply down last week too – like rates abroad

... but the 3 m NIBOR continues it's long march upwards, up to 0.24%

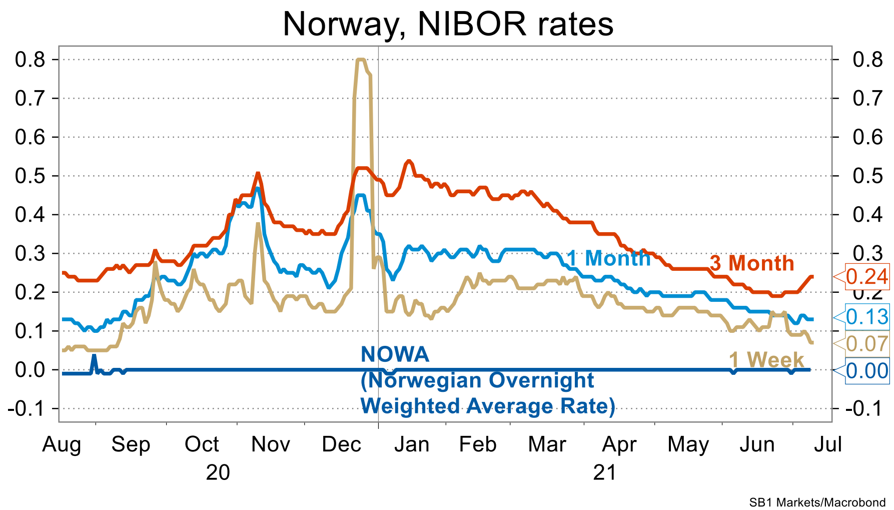


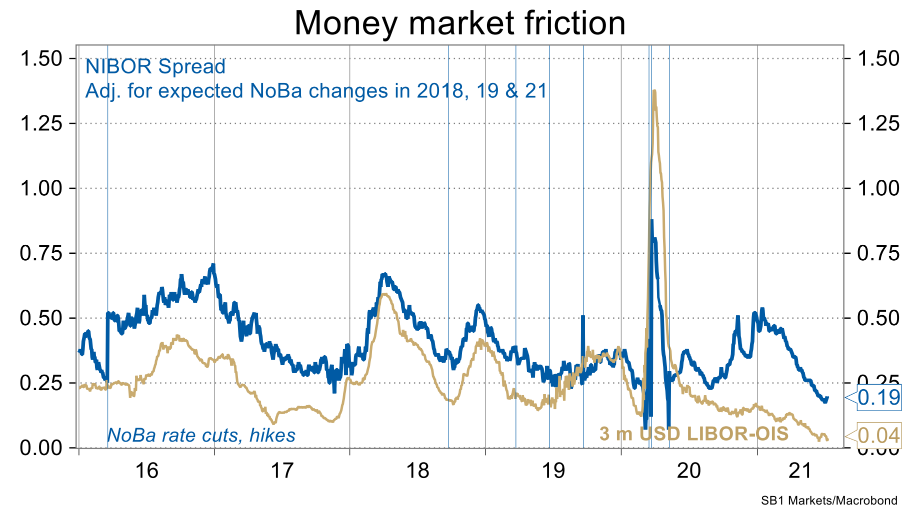


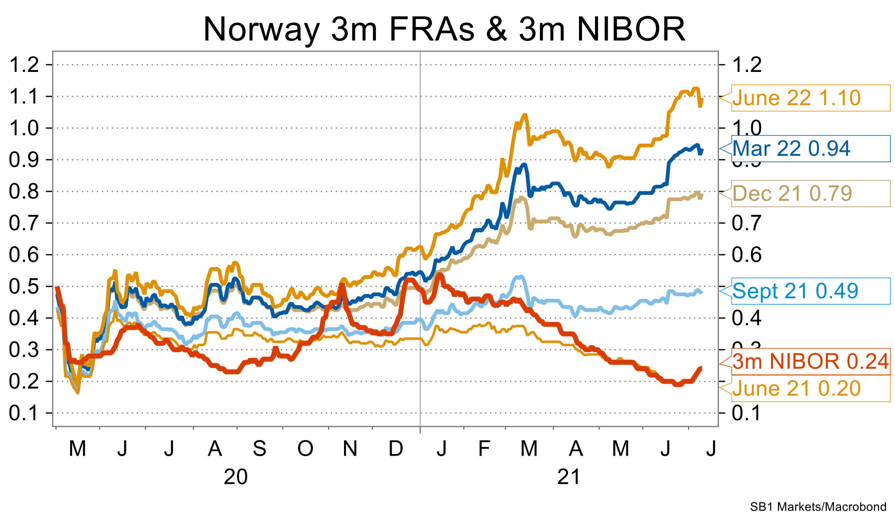
- The Dec 23 FRA rate is now lower than before Norges Bank lifted the interest rate path more than expected in June. The June 23 FRA is even
- The shorter FRAs are still above the pre-June meeting level but the market has lost some most of the confidence in the 4^{th} hike, next June

3 m NIBOR 4 bp up to 0.24%, the 'real' NIBOR slightly up

As the 3 m NIBOR runs into the first NoBa hike, it will drift up by 2 – 3 bps per week



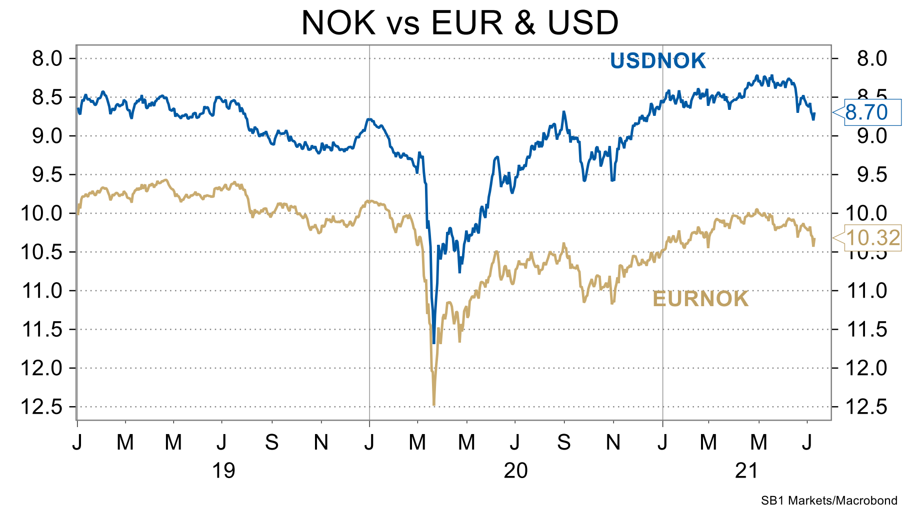


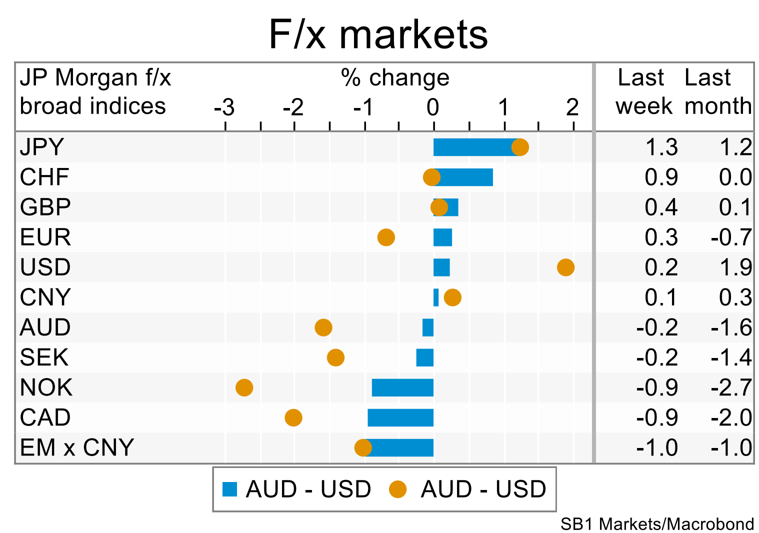


- The LIBOR OIS spread is still low – but has stabilised as the Fed offers 0.05% on excess bank liquidity (via reversed repos)
- The Sept-21 3 m contract at 0.49% bps is 25 bps above the current 3 m NIBOR. If the Sept contract remains unch., <u>the 3 m NIBOR will climb by 2.6 bps pr week until 15 September</u> and thereafter by 2 bps per week until NoBa stops hiking the signal rate by 25 bps per quarter (if the record low NIBOR spread remains unchanged).
- Last week the 'real' spread rose 2 bps to 19 bps. We expect the spread to drift upwards the coming months

EM f/x, raw material currencies down last week

Some growth angst priced into these markets, at least until last Friday

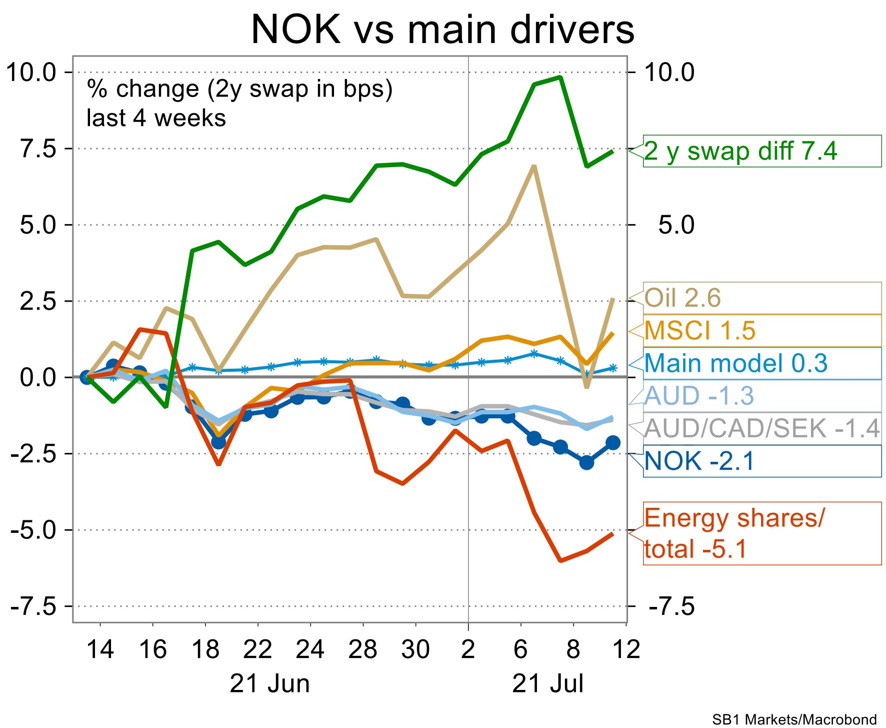


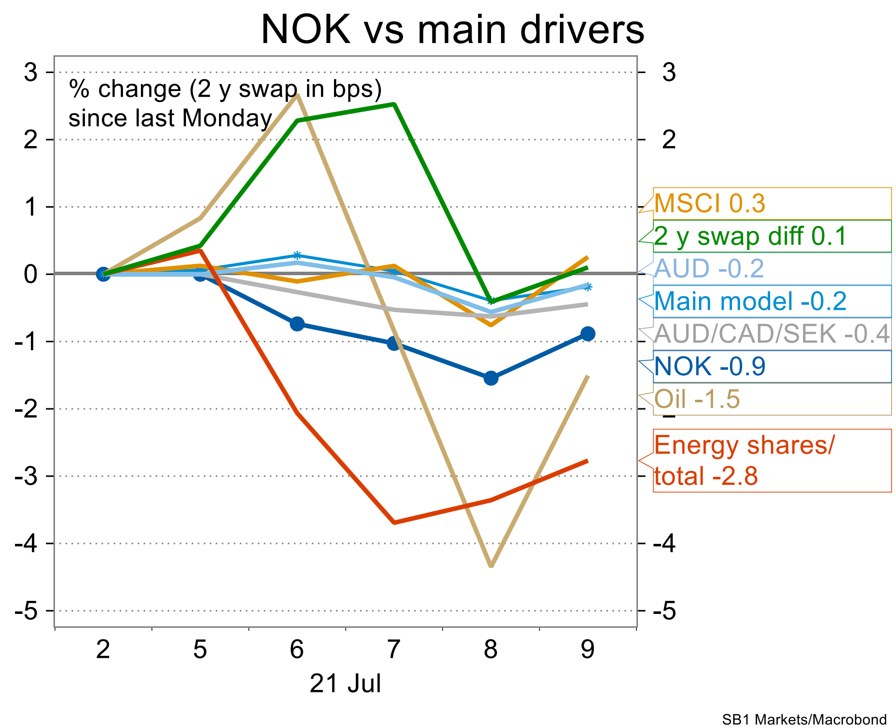


JP Morgan f/x broad indices	Last week	Last month
JPY	1.3	1.2
CHF	0.9	0.0
GBP	0.4	0.1
EUR	0.3	-0.7
USD	0.2	1.9
CNY	0.1	0.3
AUD	-0.2	-1.6
SEK	-0.2	-1.4
NOK	-0.9	-2.7
CAD	-0.9	-2.0
EM x CNY	-1.0	-1.0

The NOK down 0.9%, our model said -0.2%. Most drives down too

However, the global stock market rose marginally





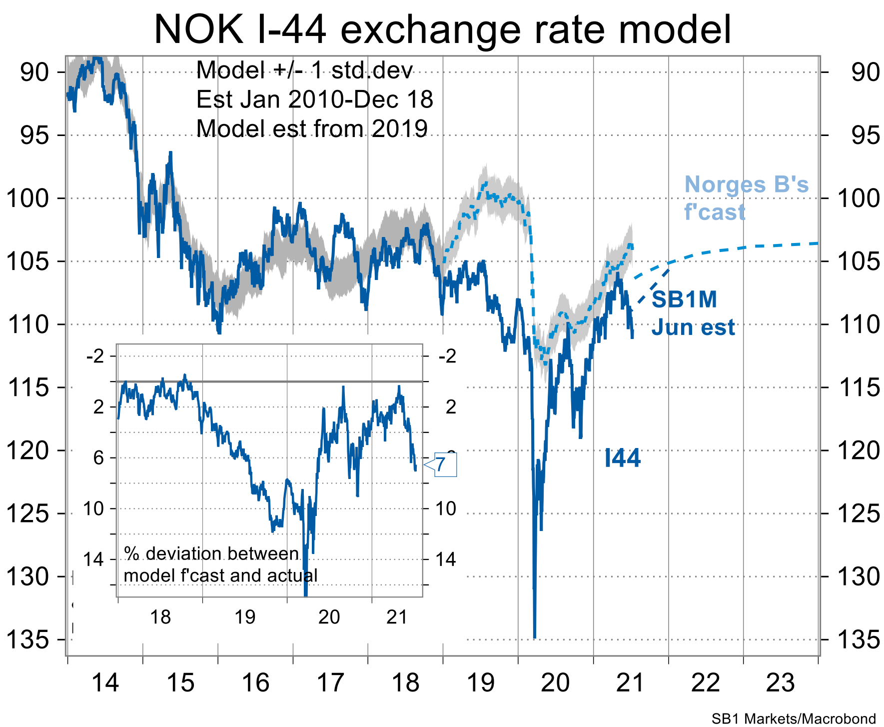
The status vs. the normal drivers:

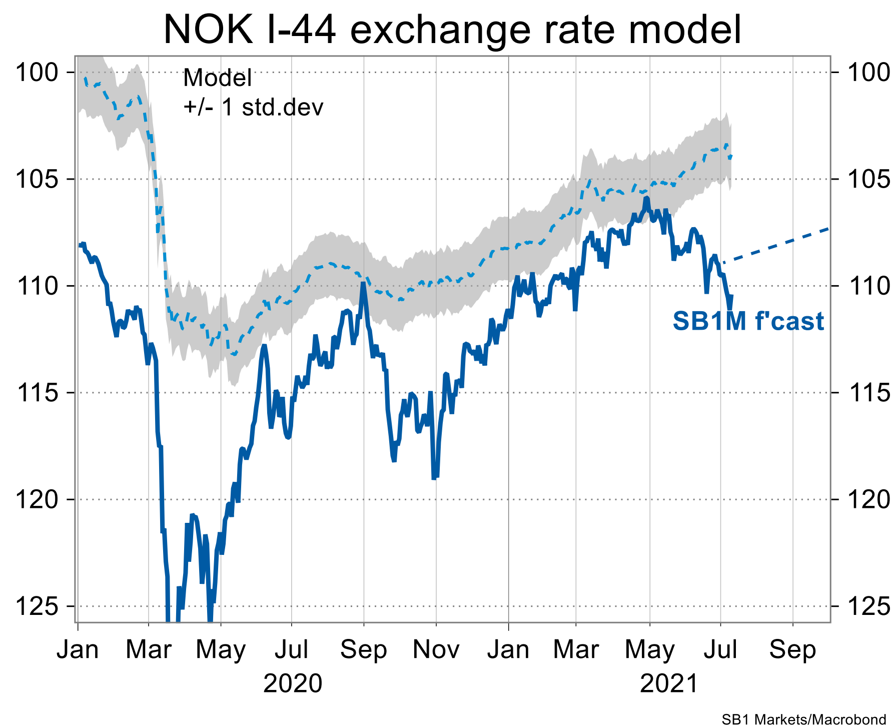
- ***The NOK is 7% weaker than suggested by our standard model (from -6%)***
- The NOK is 6% 'weaker' than the global stock market vs the correlation between the two since beg. of 2020 (unch)
- The NOK is 9% weaker than our AUD/CAD/SEK-model, our 'super-cycle peers', predicts (unch)
- NOK is far (9%) stronger than a model which includes global energy companies equity prices (vs the global stock market) (unch)

From early of May we have been neutral vs. NOK (from buy). The recent decline may have created a short term trading opportunity

At this and the following pages we have swapped Norges Bank's I44 index for JP Morgan's broad NOK index for the last 25 observations. The I44 has an earlier closing time than the 'official' closing time for fx crosses, which is the same as for JP Morgan's indices. Thus, JP Morgan's index correlates closer to the 'official' main NOK fx crosses. There are no substantial difference between these two indices over time. JPM ind. is used for other f/x too

NOK now 7% below our model estimate





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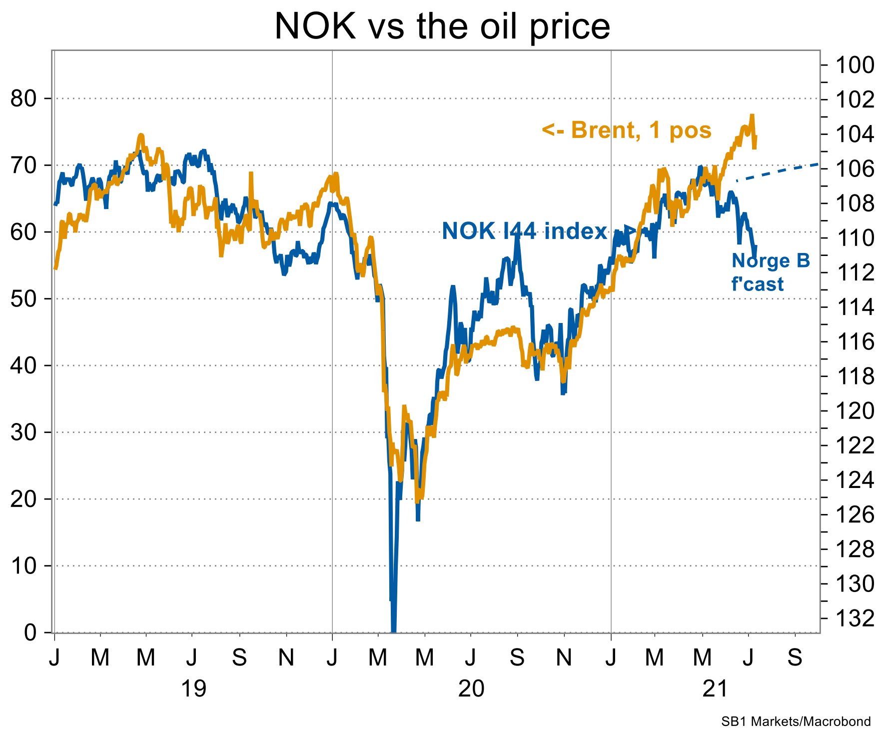
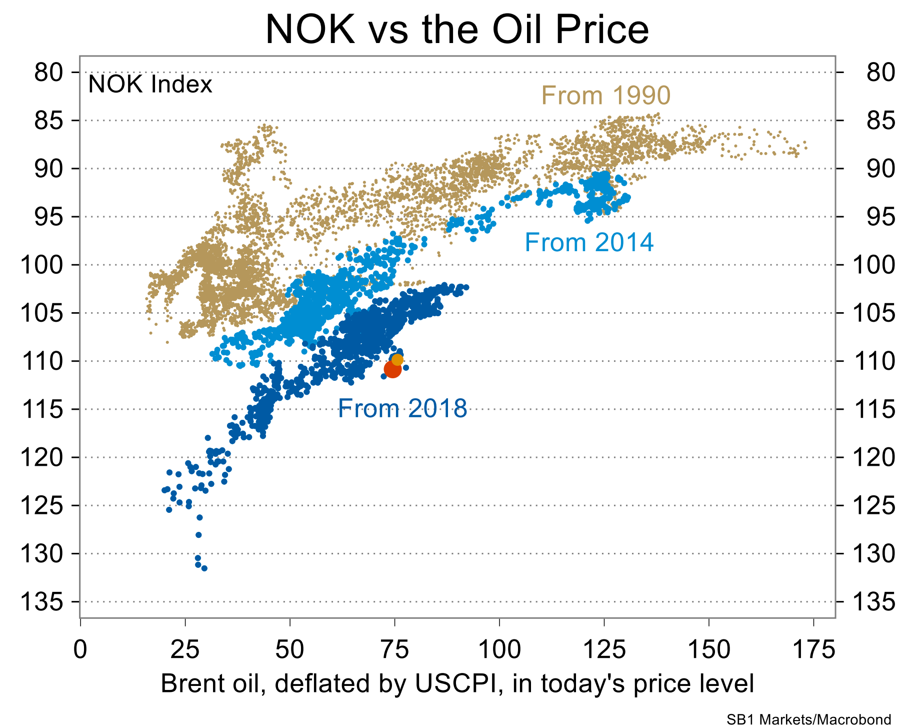
Oil down, NOK down – but NOK is 'weak' vs the oil price

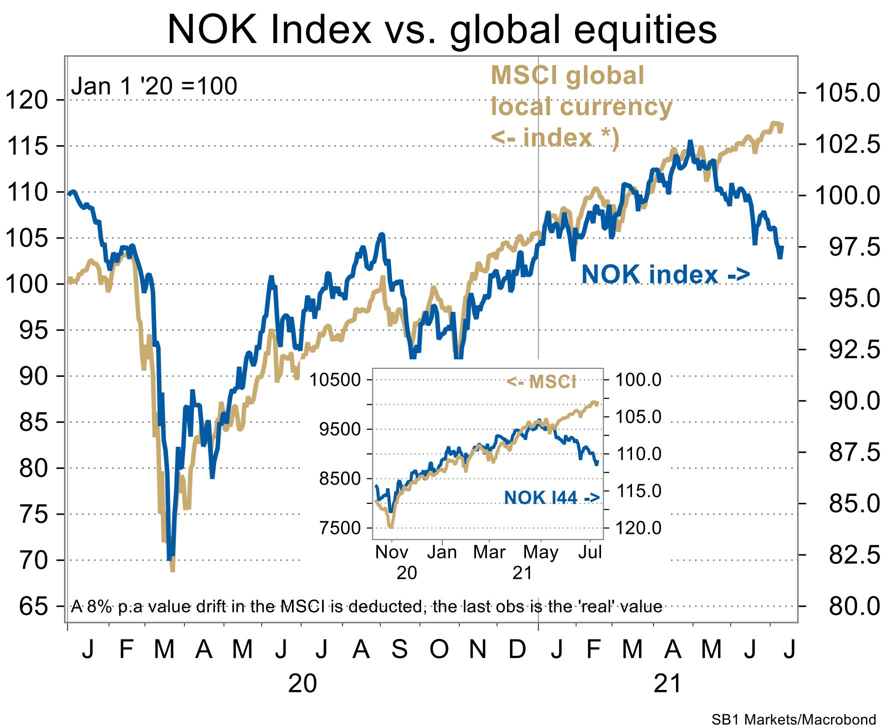


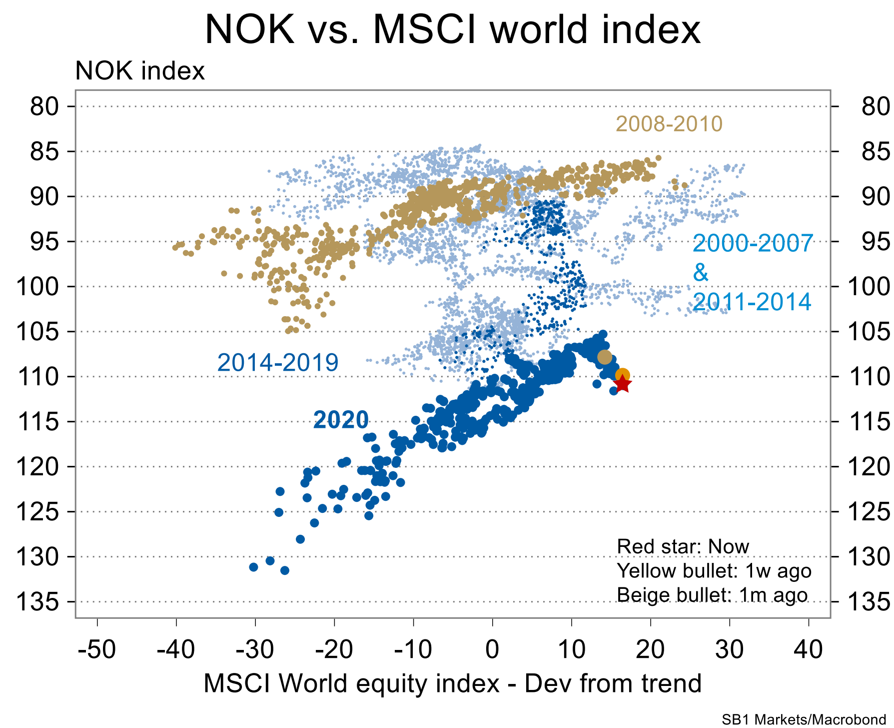


- NOK is still correlating quite closely to the oil price but at a lower level than before 2018 – and now the NOK is weak even vs the past 3 years' relationship
- A USD 10 drop in the oil price weakens the NOK by some 2.5%, as a partial effect.
  Within a broader model, the impact is somewhat smaller

Global stock markets still strong. NOK not. NOK moves into uncharted territory

NOK has lost some 6% vs. global stocks over the past months/weeks

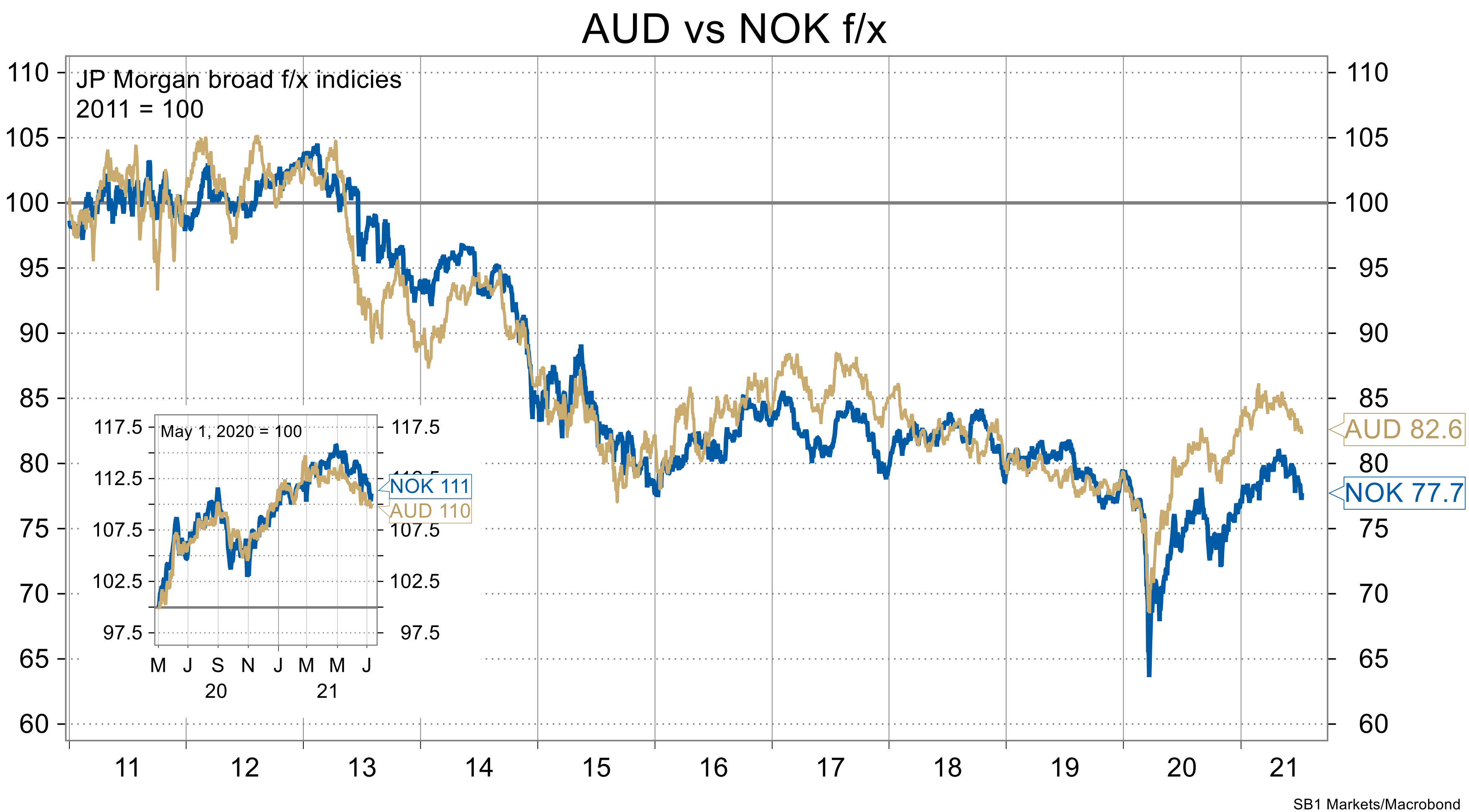




- Over time, there has not been a stable correlation between NOK and stock markets (the Oslo Stock Exchange, S&P 500 or the MSCI, the global equity index. (At the chart to the right, we have detrended the stock market as equities are drifting upwards, while NOK (hopefully) is stationary. However, the two has been pretty closely correlated from time to time
  - Now, the NOK is somewhat 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).
- 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

NOK & AUD still in tandem – but AUD was down 0.2% last week, the NOKIE -0.9%

…but the NOK is still 6% weaker than AUD since last spring



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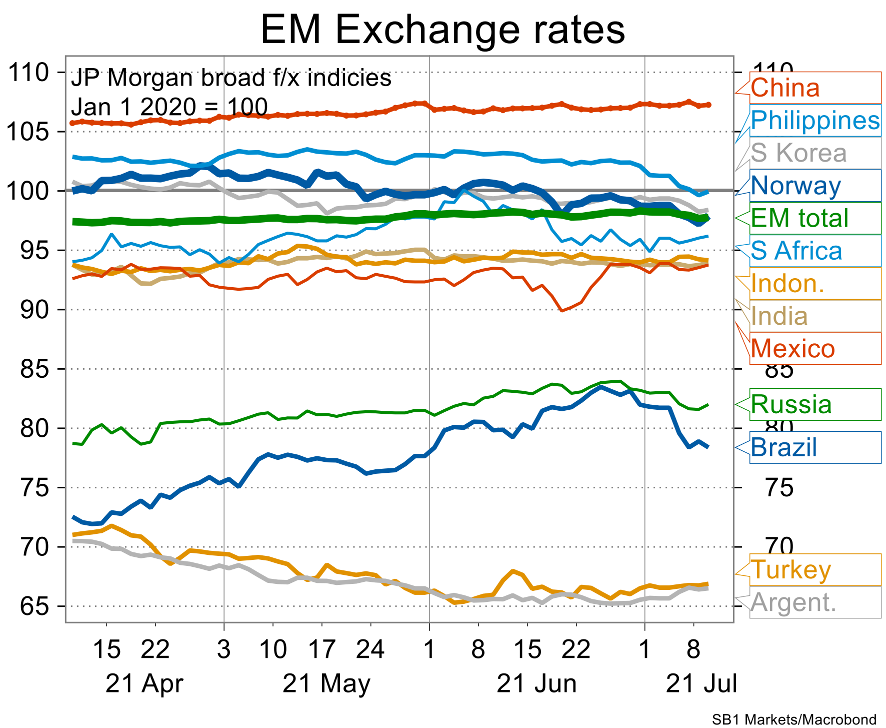
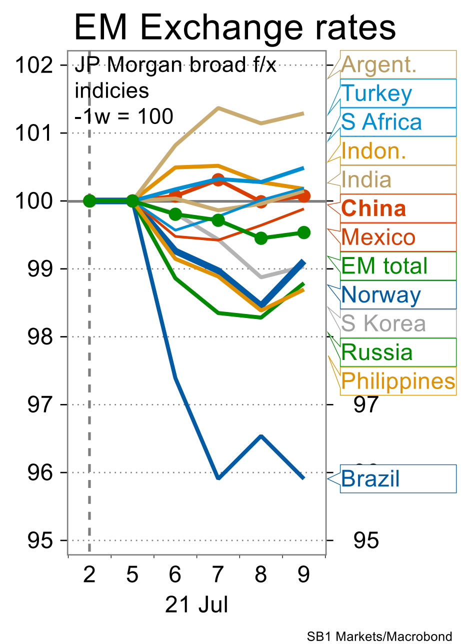
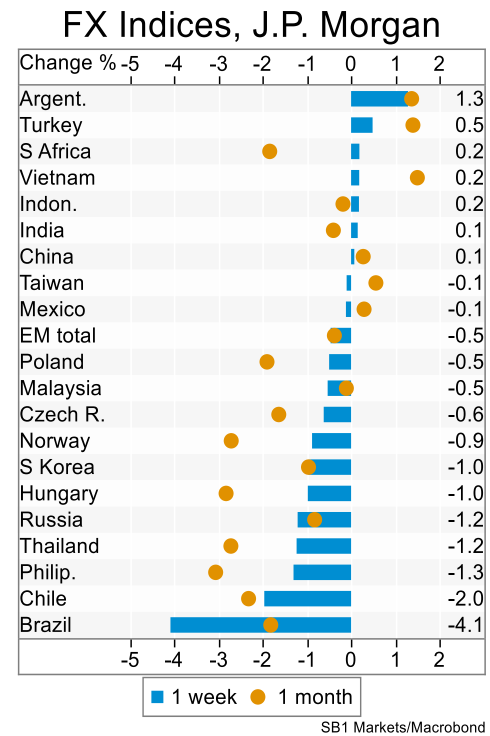
EM f/x down, the Brazilian real down 4%. The rouble down too

Some growth angst?







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