30 August 2021

Macro Weekly

Week 35/2021

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Highlights, corona update

The world around us

The Norwegian economy

Market charts & comments

Last week

The virus

- Most countries are still reporting **growth in new virus cases**, thanks to the Delta variant. However, growth has slowed in almost all countries past 1 - 5 weeks, and in 13 out of 38 countries we track, the no. of new cases has fallen, and in some places sharply
- In Europe, **hospitalisation & death rates** (CFRs) have fallen sharply, and are at low levels. There are no widespread capacity problems at hospitals
- That has not been the case in the **US**, suggesting diverging testing policies as the positivity rate has shot up, and the no. of hospitalisation & deaths has increased far more than in Europe. In the US, the no. of hospitalised patients is just 30% below the Jan peak, and some (low vaccination rate states) are reporting a record high no. of patients, and capacity constraints. The good news: growth in cases in the US has fallen sharply, and fell to zero last week. Growth in hospitalisations is slowing too, signalling that the threat from the Delta variant may have peaked
- **In Norway,** the no. of new cases surged last week, +80% (only New Zealand reported an even higher growth rate). The no. of hospitalised patients almost doubled but the level is still low (11 per mill, vs 100 in the UK, almost 300 in the US) as just kids and young persons are unvaccinated, and few of them and of the older, fully vaccinated end up in hospitals, if infected. Still, with an R at 1.6, something will have to give the coming weeks, and some mild, local restrictions cannot be ruled out. A continued rapid vaccination among the youngsters might be sufficient
- In the West, **mobility** has not come down during the Delta outbreak, signalling that economic consequences are mild
- In the East, the lockdowns will probably not last for too long, and **India** is back at full speed. **China** have probably already beaten down the last (very limited) outbreak

The economy, part I

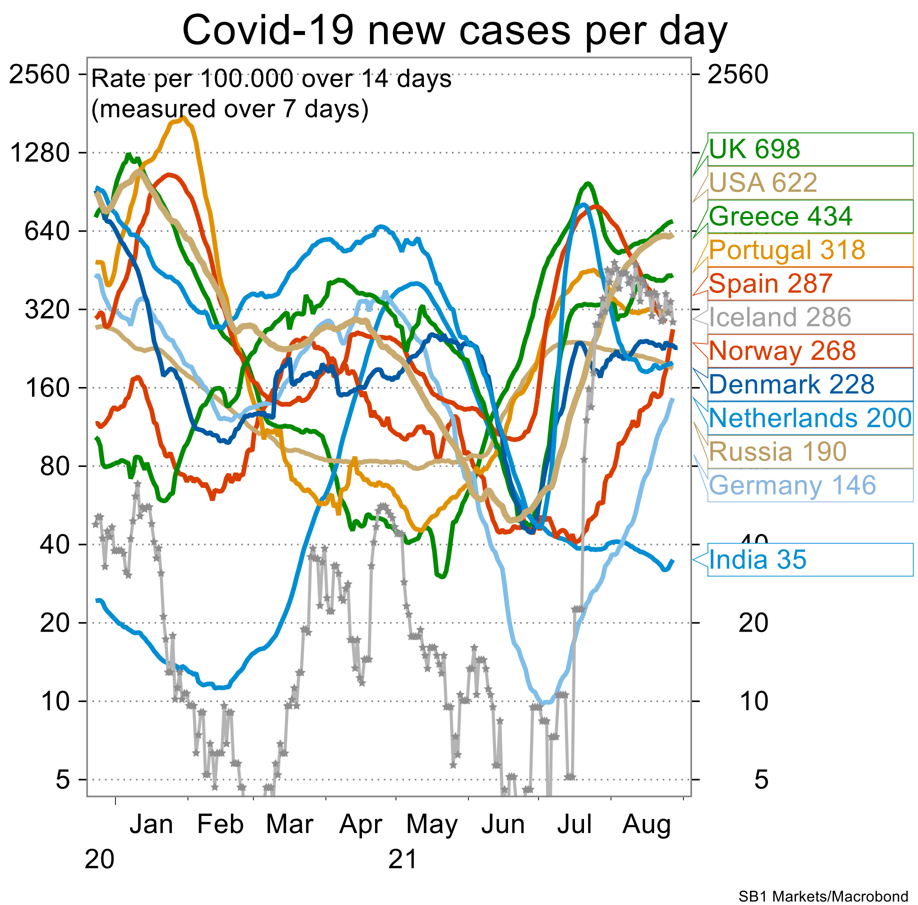
- **August PMIs**
  - **The preliminary PMIs** were weaker than expected, especially in the US, where service reported a further, and sharp decline in growth. In the EMU, service growth kept well up, while manufacturing slowed somewhat (but the sector is still reporting unusual strong growth). We estimate that the global PMI fell more than 2 p, down to 53, signalling growth a trend. However, Emerging markets may have fared better than DM in August, just like they did in July, dampening the decline in the global index. Data out this week
- **US**
  - If the labour market does not turn sour the coming few weeks (the most important check this week's payroll stats) the FOMC will very likely signal a gradual reduction in the USD 120 bn/m QE program from late 2021 at the September meeting, as employment has made substantial progress towards the maximum employment target. In his long awaited **Jackson Hole (digital) address on Friday, Gov. Powell** said that he at the late June meeting argued for a tapering start in late 2021. We didn't know, he did not indicate so at the press conference in late July. However, several FOMC members have signalled the same position recent days/weeks. They are arguing the supply side is the constraint in the US economy, not demand (and they are right). Still, while Powell also recognised that the price level had reached Fed's long term target, he signalled that inflation has not yet established itself at a sufficiently high level (!), and employment had not reached the maximum employment target. Thus, there is no hurry for hiking rates, even if a QE tapering is appropriate. Markets were well prepared for a tapering message (even if we thought he would wait until the Sept FOMC meeting), and were satisfied with his dovish stance on rates. The yield curve fell, all over, with a sharp decline in real rate, while inflation expectations rose somewhat. And the stock market celebrated by the 3rd ATH for the week

Last week: The economy, part II

- **USA (cont.)**
  - **Core PCE** prices rose by 0.3% in July, as expected but still more than 4% annualised. The annual rate rose 0.1 pp to 3.6%. Some re-openings impacts will surely subside (2nd hand prices have surged 40%) but prices increases are broadening somewhat, and businesses are still reporting unprecedented price hike plans. Wage inflation has accelerated too, the most serious threat vs. the inflation target over time (if sustained)
  - **Household consumption** has flattened since April, as services are recovering but spending on goods is on the way down to more normal levels. Household income is normalising too, as wage income is recovering, and transfers from the government are on the retreat (at least for the time being, new programs are on the table in the Congress). The savings rate is just 2 pp above a normal level but accumulated savings through the pandemic (the Wall of Money) equal 13% of disp. Income
  - **Both new and existing home sales** rose marginally in July, both better than expected – but both has fallen sharply so far in 2021, mostly due to lack of supply – and inventories are still low. However, the inventory of new homes are on the way up, at least for projects that are not started or are under contraction. Realtors reported a 1% m/m price appreciation but the annual growth fell sharply (to 17% from 23%) due to the 6% price surge one year ago
  - **Durable goods orders** are still on the way up, and better than expected in July. Surveys signal growth will continue
- **EMU**
  - **Consumer confidence** fell marginally in August but the level is still well above average – and at the same level as before the pandemic crisis
- **Sweden**
  - **Retail Sales** were down by 1.2% m/m in July, driven by a fall in household equipment and recreational goods. The level is still high and well above the pre-pandemic level and we expect sales to fall further as more spending is shifted towards services and travel abroad. **House prices** fell in July
  - **Consumer confidence** was virtually flat while the **KI business survey** fell just marginally in Aug, from super strong ATH in July
- **Norway**
  - **Retail sales** fell surprisingly by 3.1% in July, but just due to an unpresented decline in hardware/building materials, where sales fell 29%, in volume terms. Goods were in short supply, and demand was hampered by (an equally unprecedented) 26% price increase - sales fell 10% in nominal terms. (The price hike in one months seems unlikely but may be due to a low data collection frequency). As most of the sales of hardware/building materials are to homebuilders/professionals, the impact on households' consumption of goods was limited – in fact **total consumption of goods** (ex electricity) grew by 1.0%! As an indicator of total economic activity, the decline in retail sales still is 'for real' (if the price index is correct)
  - **Payrolls** rose 1.1% m/m in July, and the no. of employees living permanently in Norway was some 0.8% above the pre-pandemic level. The total, including foreigners on short term stay is still down - but just by 0.3%
  - **Consumer confidence** fell in August, according to the CCI, but just reversing the July hike – and the level is still strong (+1 st.dev above avg)

Growth in Covid cases are slowing – and are down in almost 1/3 of countries

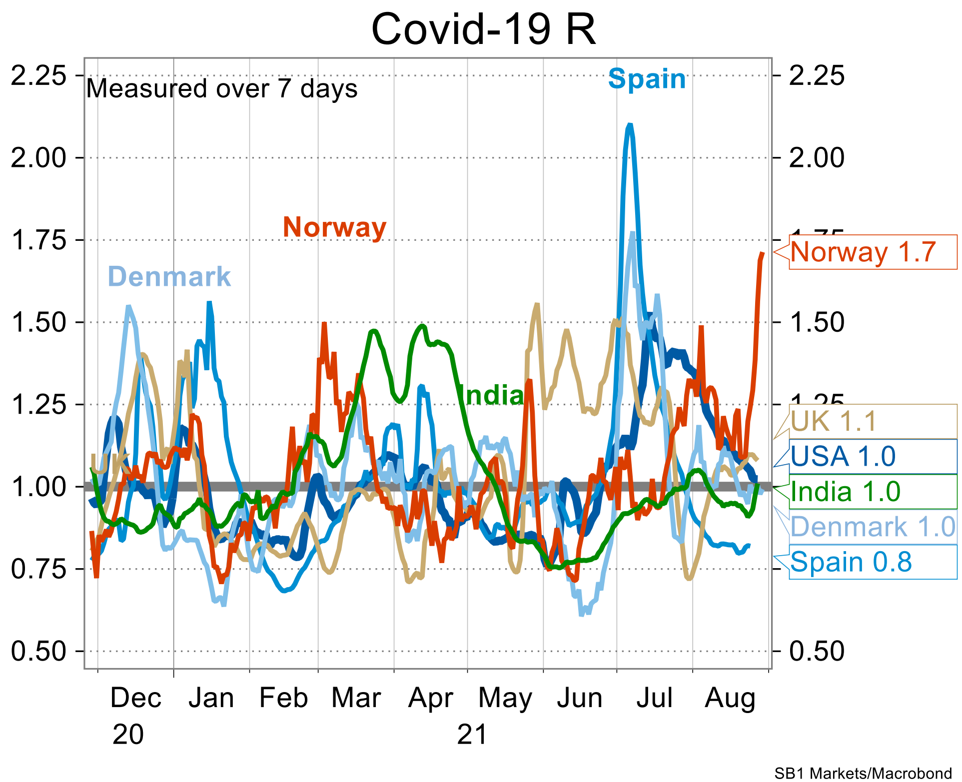
The main risk now: An even more contagious or vaccine resistant virus variant

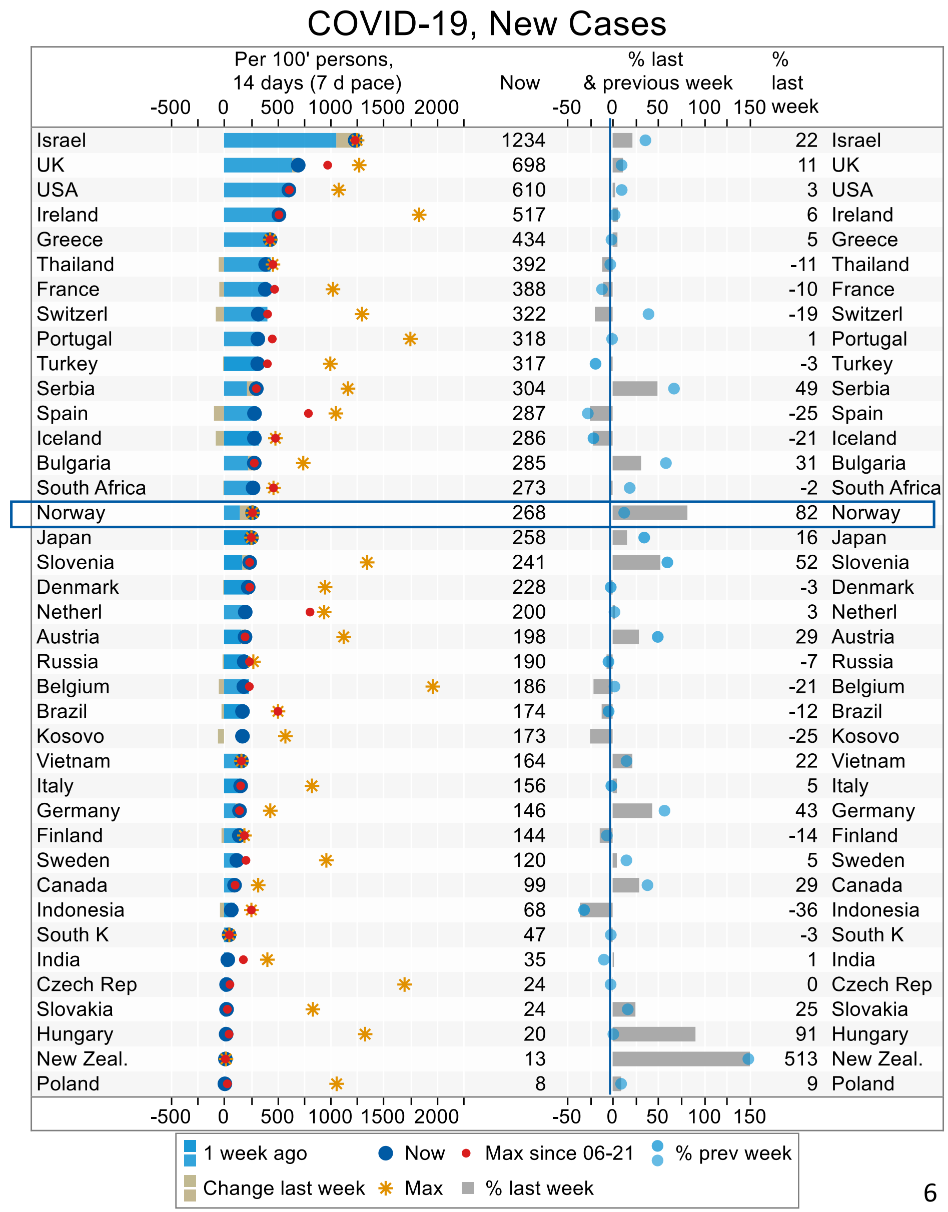


- In **Europe**, the Delta outbreak has led to more hospitalisations and deaths, but as hospitalisation/death rates have fallen sharply there is not any health crisis yet – and we doubt there will be
- The outlook is a bit more uncertain in the **US** where hospitalisation & death rates are much higher than in Europe (probably because the real no. of positive cases is underreported, the positivity rate has shot up too) – in tandem with a steep increase in new cases. The no. of hospitalised is just 30% below the Jan peak, and is record high in several states. However, growth new cases has slowed further and approached zero last week. Growth in hospitalisations is also slowing, signalling that the Delta outbreak is coming under control
- The situation is more challenge larger in many **Emerging Markets** but even there the no. of new cases has peaked in some countries, and growth has slowed. Few new cases are reported in **India** – and **China** close to none
- **In Norway,** the no. of new cases skyrocketed last week (80%, R = 1.6, just New Zealand reported higher growth last week) following opening of schools & universities from mid August. The no. of hospitalised patients has quadrupled – from a very low level – and still just 62 persons are hospitalised (11 per mill, vs 100 in the UK, and almost 300 in the US)
  - » We still deem it as rather unlikely that hospitals will be overwhelmed before 'everybody' is vaccinated – or some mild restrictions are re-introduced. However, a sharp increase in hospitalisations must be expected the coming days/weeks

New Zealand & Norway in the lead, growth wise

The level is still close to zero in NZ, not in Norway





- The red dots on the chart to the right indicate the peak in new cases since June (India's peak was in May). When these dots are in 'free air', cases are down vs the recent peak - which is the case in 13 of 38 countries (from 12). However, last week the no. of new cases grew in 23 countries (from 24) – so it is over over yet
- *Disclaimer: Testing policies/capacities may have changed (and they differ vastly between countries)*

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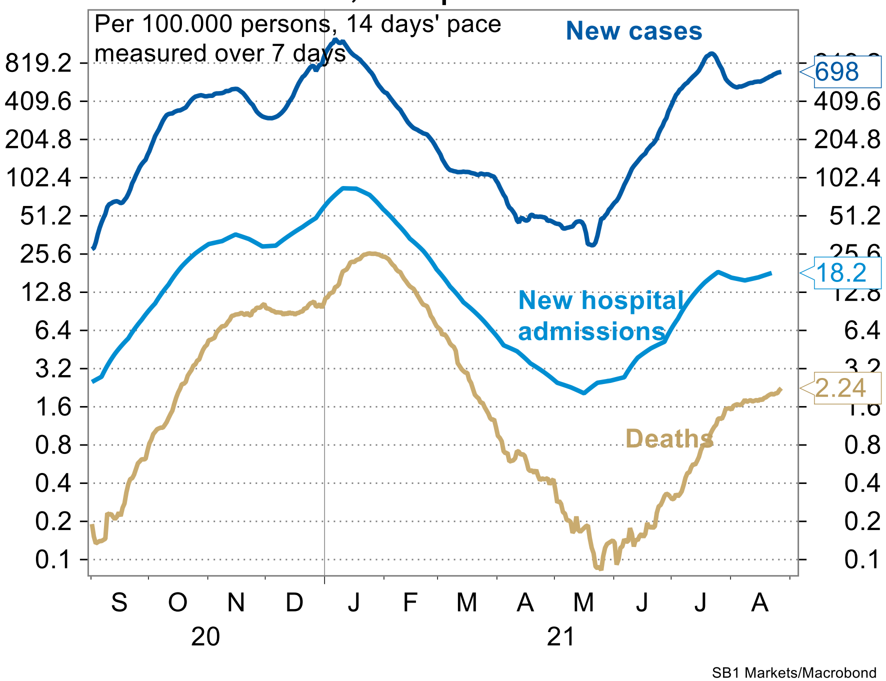
UK: Still a moderate level of hospital admissions & deaths

The no. of new cases is increasing again but slowly

UK Covid cases, hospitalisations & deaths



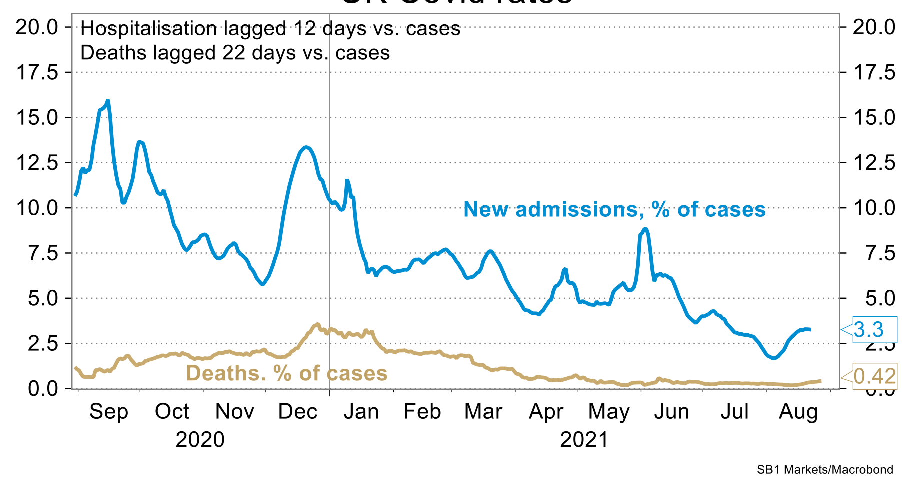
- The no. of **new cases per day** peaked before it reached the Jan top, then fell 50% during less than couple of weeks. Now, it is heading <u>slowly</u> up
- The no. of daily hospital admissions has increased 9 times from the bottom in May, but the level is just above 1/5 of the peak in Jan, and the no. admissions has flattened the past two weeks. The no. of deaths is up 20 times, still at just 8% of the Jan level

  » The **hospitalisation rate** has fallen sharply as both old persons and other risk groups are vaccinated, to 2% - 3% from 8%

  » The **case fatality rate** (of those tested positive) has fallen even more, to 0.4% from close to 3% in Jan/Feb

- **Implication:** The Delta variant has spread like a wildfire, but the number of infected will have to increase to very high levels before the UK will run into another serious <u>health</u> crisis
- <u>Other European countries are reporting low hospitalisation & death rates, while the US is not (probably because testing is far below European levels), check next page</u>

UK Covid rates



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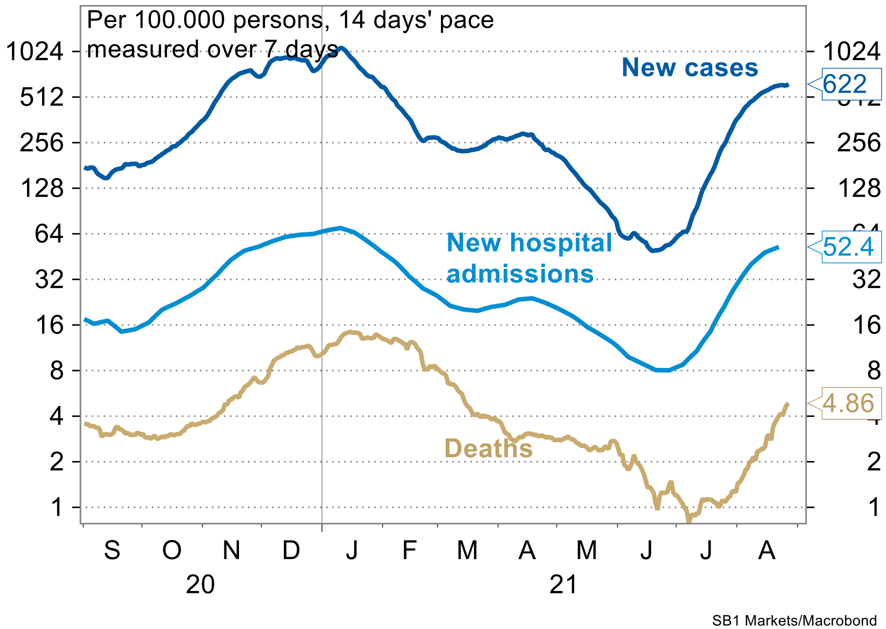
US is running into problems but stricter policies, more vaccinations will help?

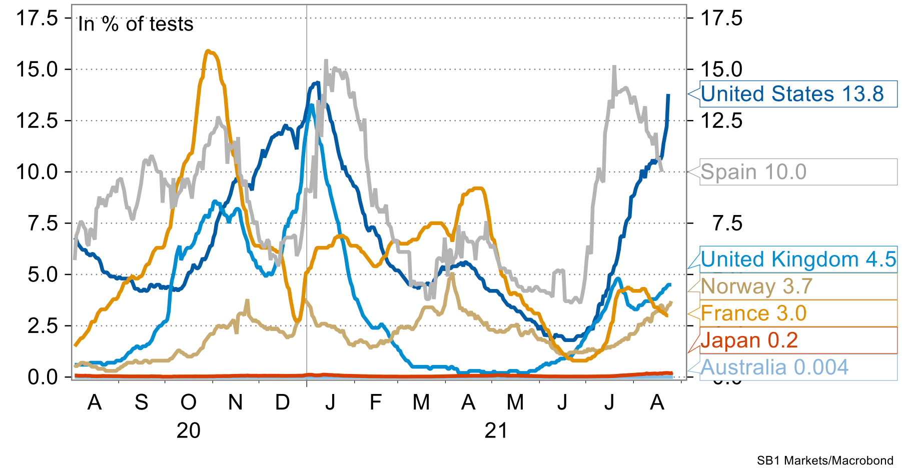
Far more hospitalisations/deaths, but growth in cases, hospitalisations is now slowing

United States Covid cases, hospitalisations & deaths

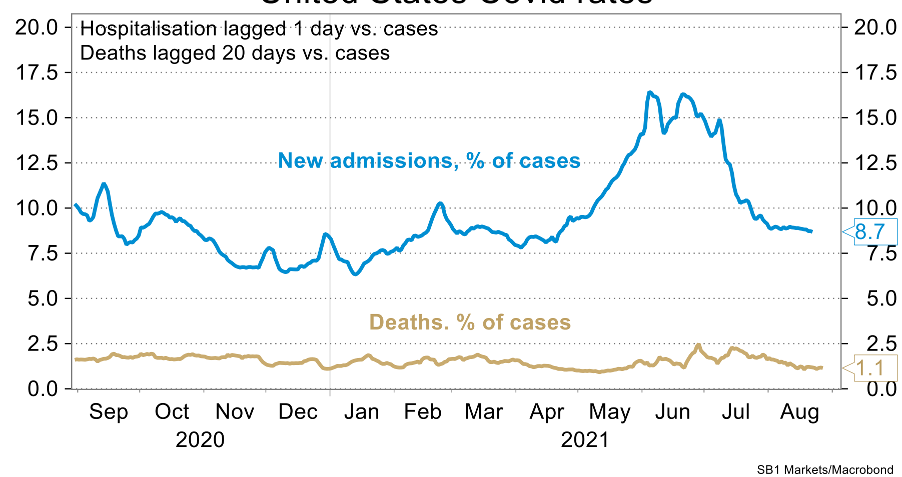


- The hospitalisation rate is 2 – 4 times higher than in Europe
- The death rate (Case Fatality Rate) is 2 – 8 times higher
  - » Thus, the no. of cases is very likely underreported vs. Europe
- However, growth in the (official, though) number of new cases has slowed substantially past 3 weeks – and growth in hospitalisations has slowed as well

Covid-19 Postive test rate



United States Covid rates



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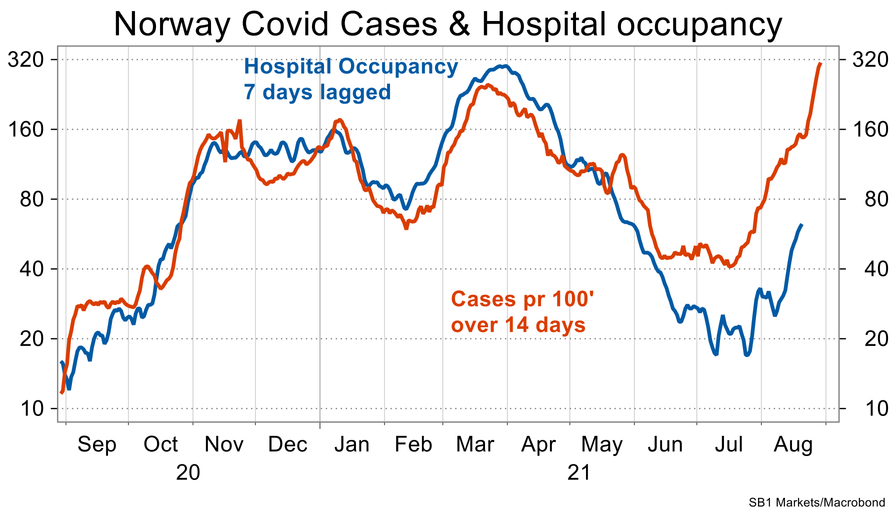
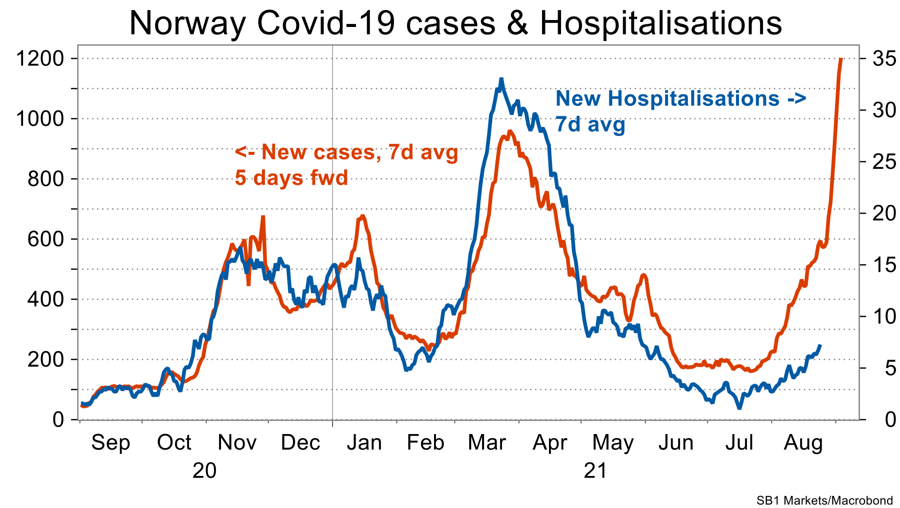
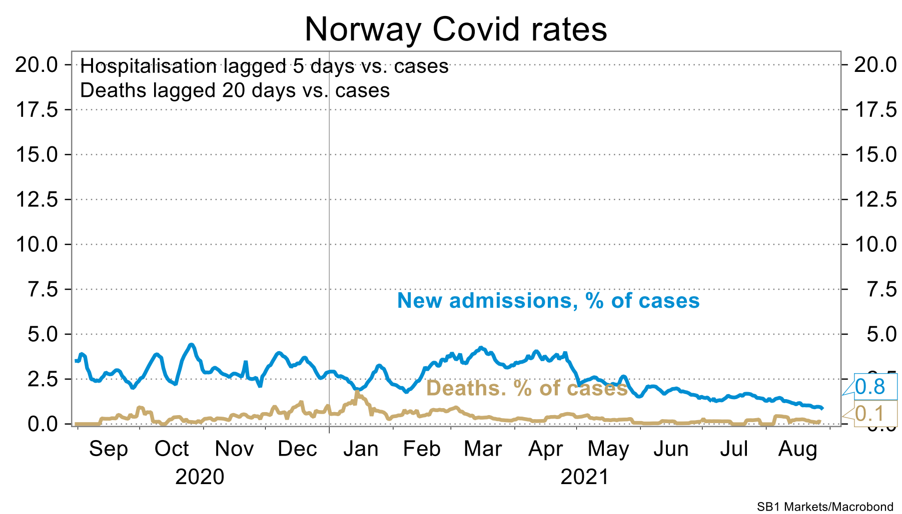
Norway: A sharp increase in no of new cases, more hospitalisations to come

However, as less than 1% of positive cases are hospitalised, still not serious health burden



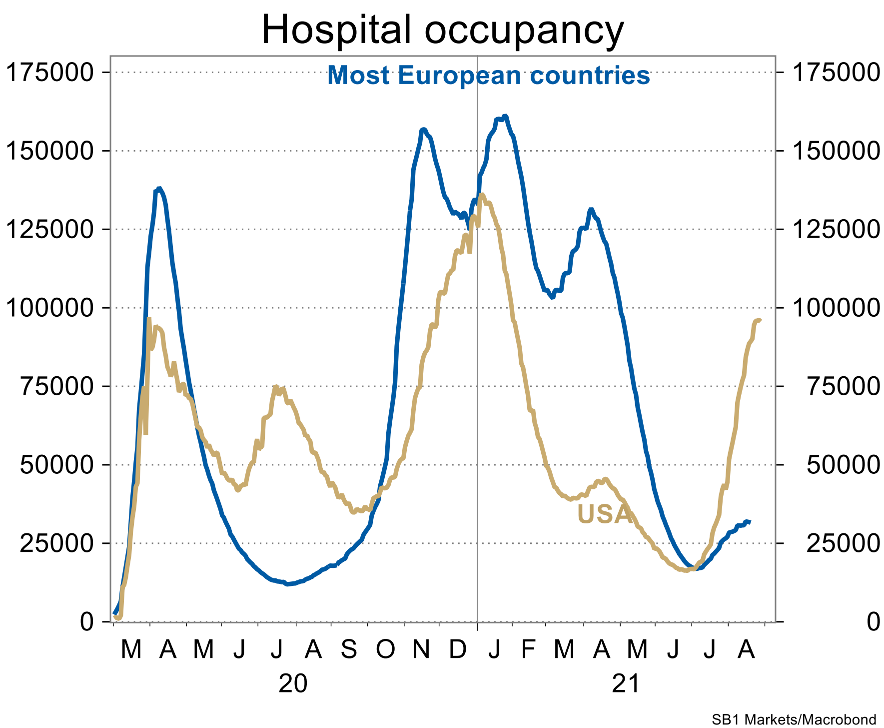


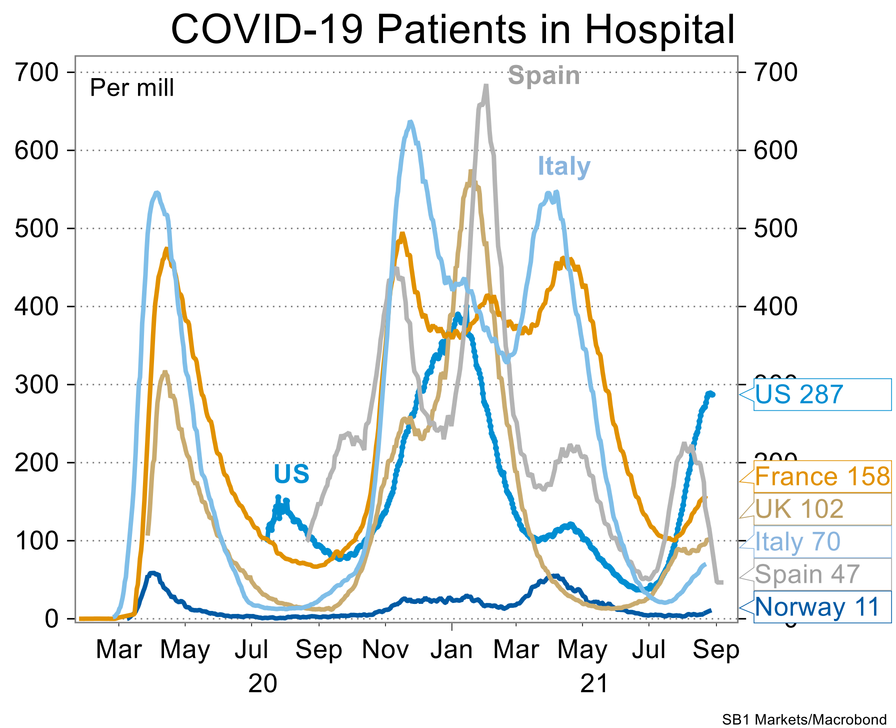
- Still, if growth the infection curve does not slow the coming weeks (from the present 80% rate), even a 1% hospitalisation rate will in the end create problems
- We think the likelihood for that to happen is limited
  - » Vaccinations will probably speed up again, now by including the 16 & 17 y/o cohorts, and probably soon down to 12 year olds.
  - » Some mild, local restrictions have been – and will be imposed



The no. of patients admitted due to Covid is increasing in several countries

But only the US is running into trouble, thus far





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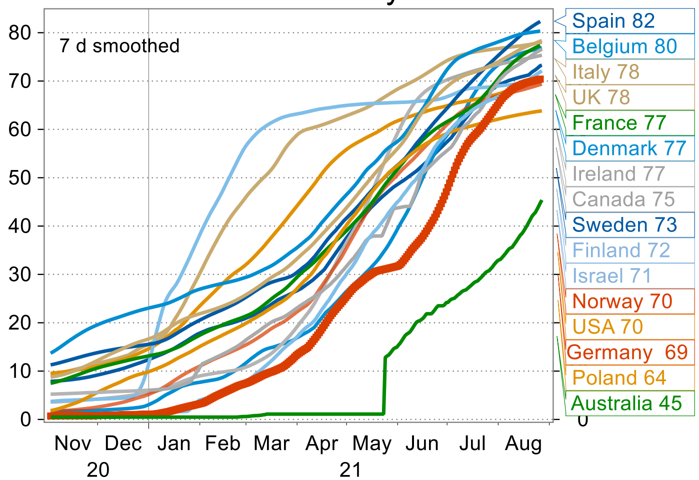
More jabs, at least in Europe

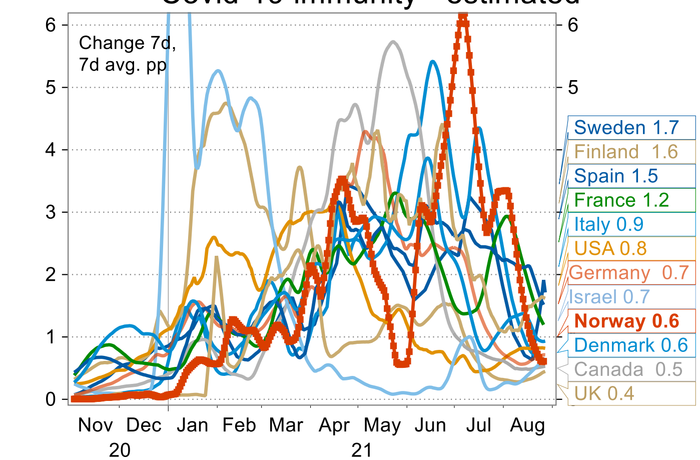
Even with high vaccination rates, the Delta variant is spreading rapidly. More vaccines needed

Covid-19 immunity - estimated



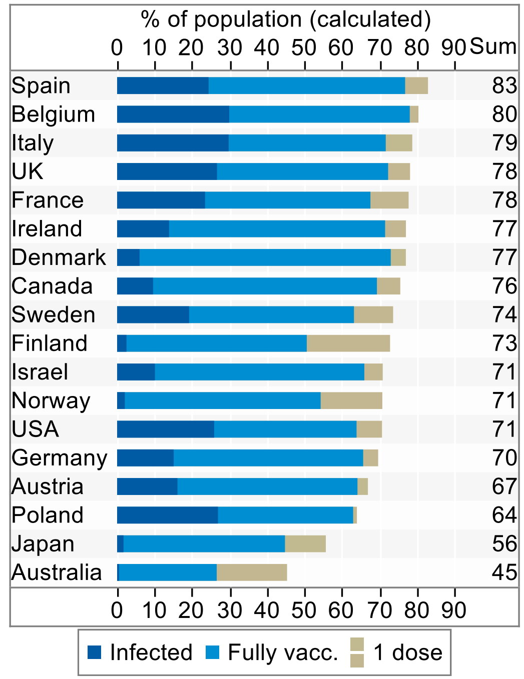
SB1 Markets/Macrobond

Covid-19 immunity - estimated



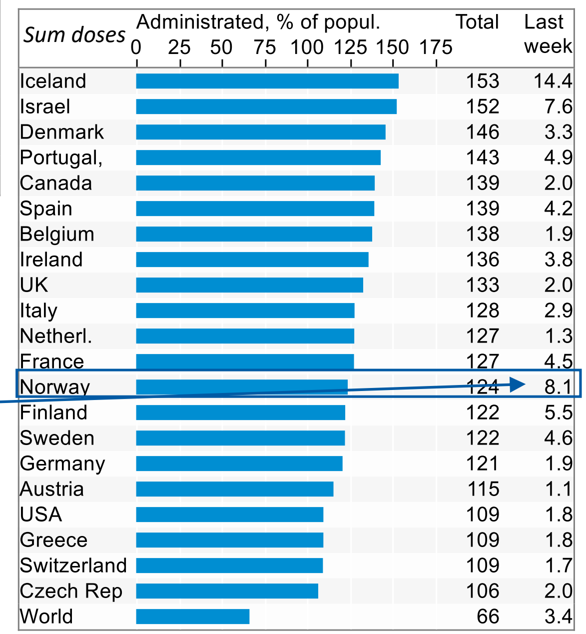
SB1 Markets/Macrobond

Covid-19 Immunity



SB1 Markets/Macrobond

Covid-19 Vaccinations



SB1 Markets/Macrobond

Mostly 2nd doses were administered in Norway last week

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 (a conservative assumption)

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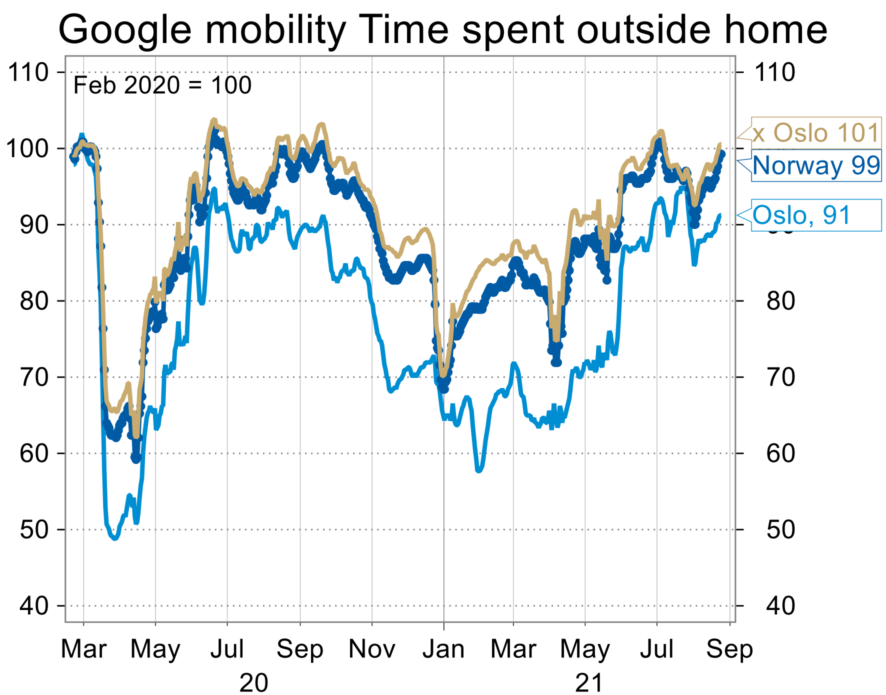
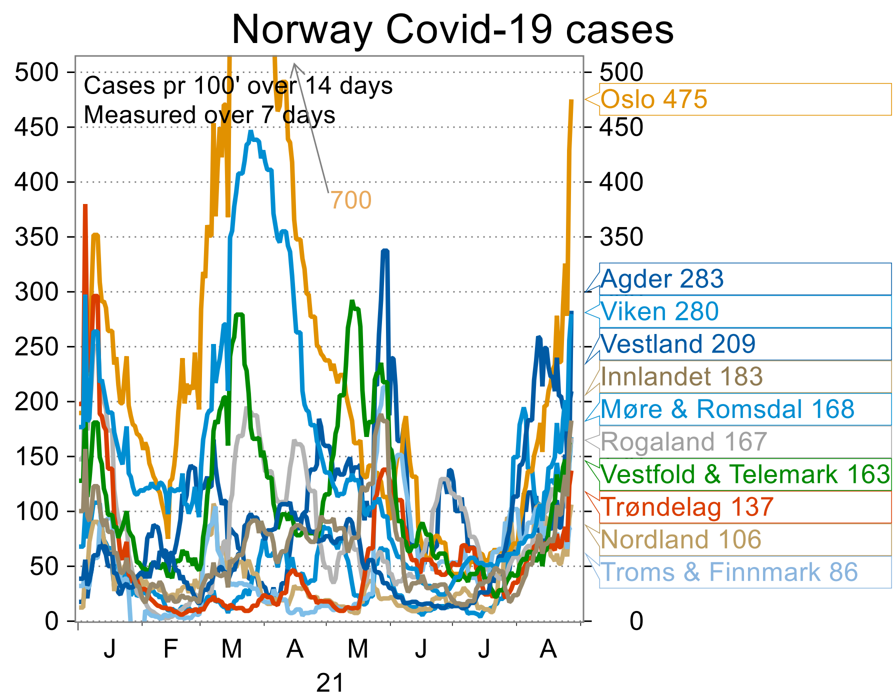
Norway: All counties are reporting more cases. Oslo, Agder & Viken in the lead

Mobility is on the way up again. Until further notice…





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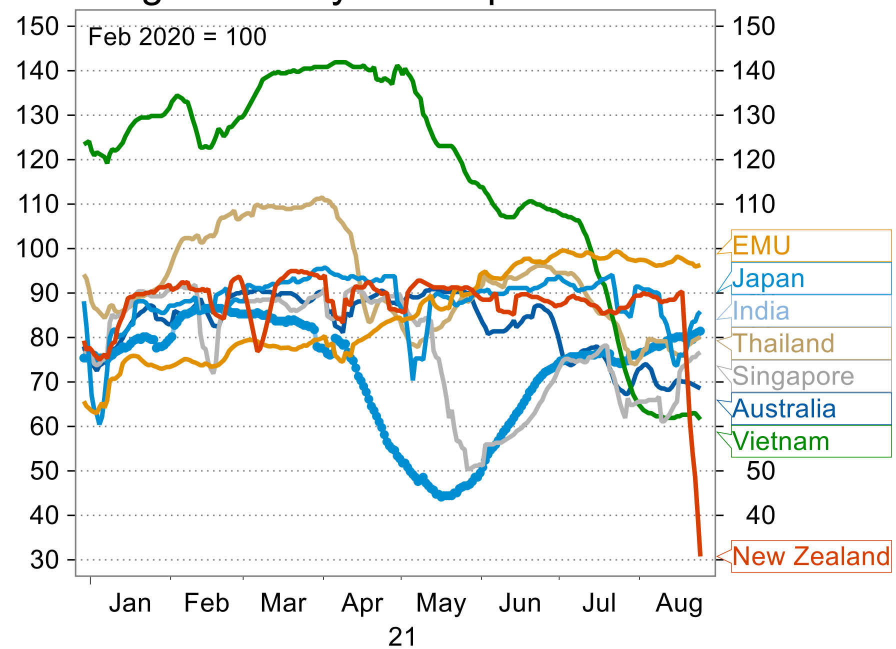
In the West, no signs of reduced mobility during the Delta attack

However, mobility sharply down in some Asian countries, and in Aus/NZ! India almost back to normal

Google mobility Time spent outside home

SB1 Markets/Macrobond

Google mobility Time spent outside home

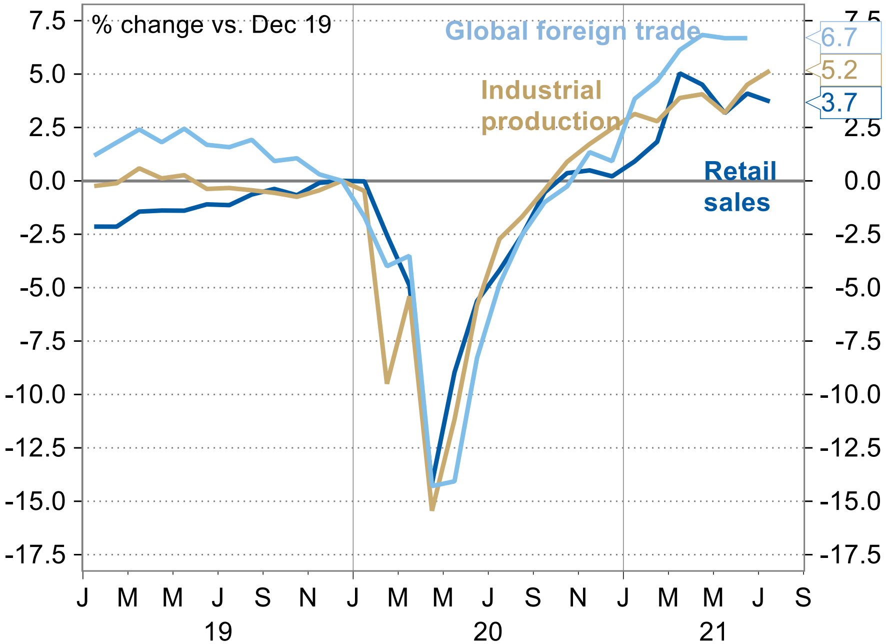


SB1 Markets/Macrobond

Activity in the goods sector is flattening

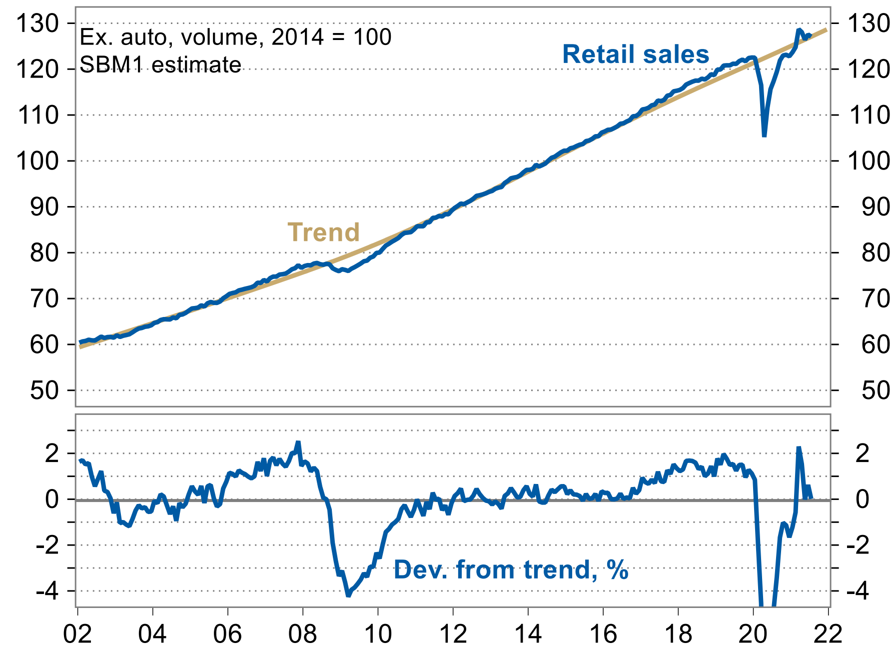
The setback in some Emerging Mkts due to Covid/Delta partially to blame. And DM demand peaks

Global Retail sales, industrial prod. & trade



SB1 Markets/Macrobond/CPB

Global retail sales volume

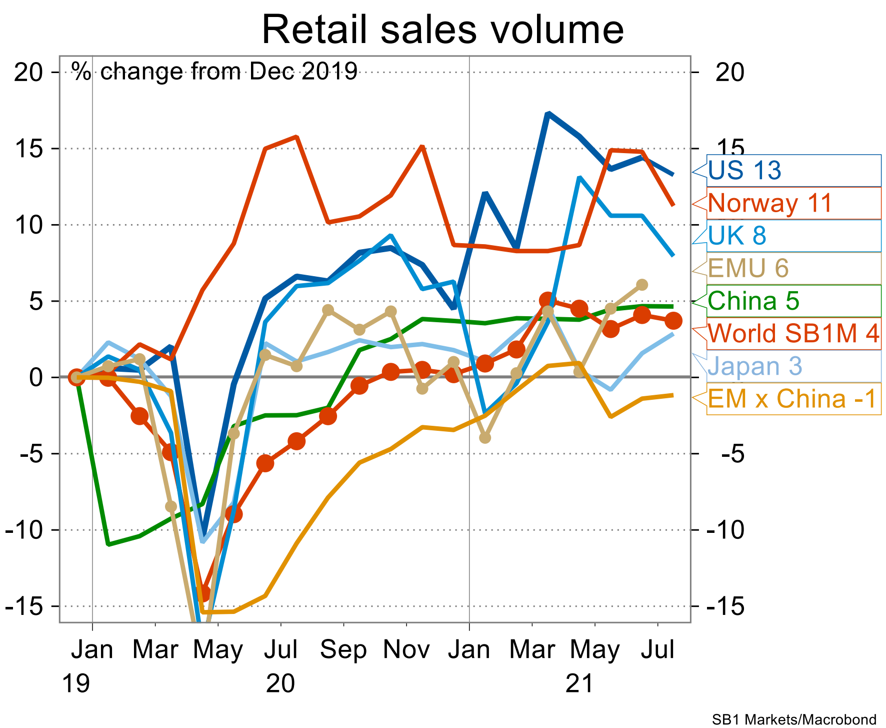


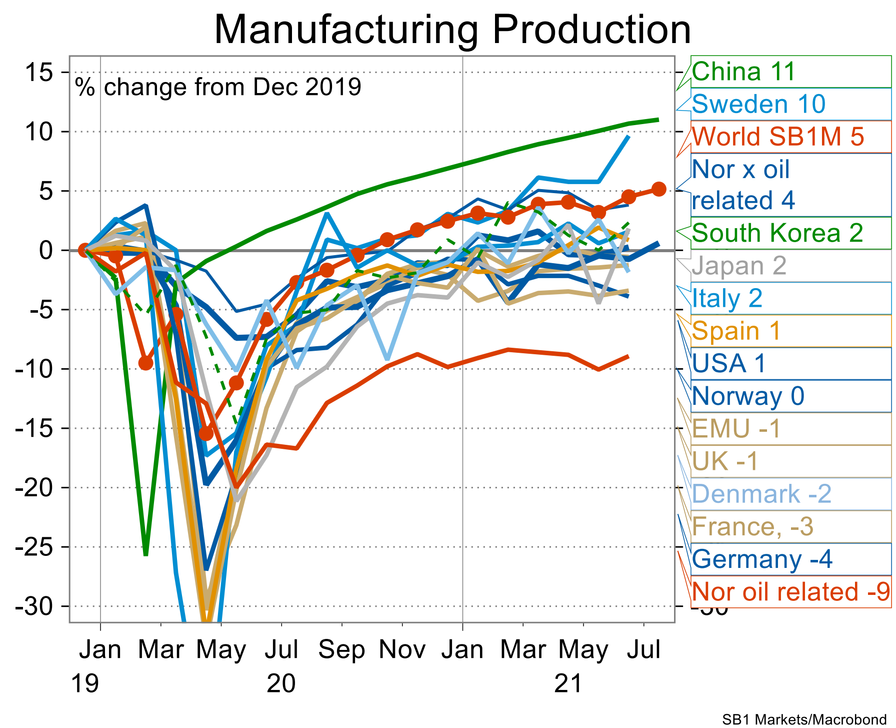
SB1 Markets/Macrobond

- **Retail sales** rose in June but may have fallen in July, according to our very preliminary forecast – and sales have flattened recent months, partly due to an assumed setback in India (data a lagging). The level is approx. 4% up vs the pre-pandemic level
- **Manufacturing production** rose in June, and probably in July too is still trending upwards. The level is some 4% above the pre-pandemic level. Trouble in India and in the auto industry globally have contributed on the downside recent months
- **Global foreign trade** flattened in May (was originally reported up), and was stable in June as well. The level is close to 7% above the pre-Covid level, according to CBP in Netherlands

DM market demand for consumer goods have peaked

The upside potential is large for Emerging Markets, but the Delta variant is hampering activity





- Manufacturing production is still drifting upwards
- Norwegian oil-related manufacturing production is down 9% vs the pre-pandemic level – non-oil sectors are up 4%, one of the better results in the rich part of the world (but behind Sweden, + 10%)

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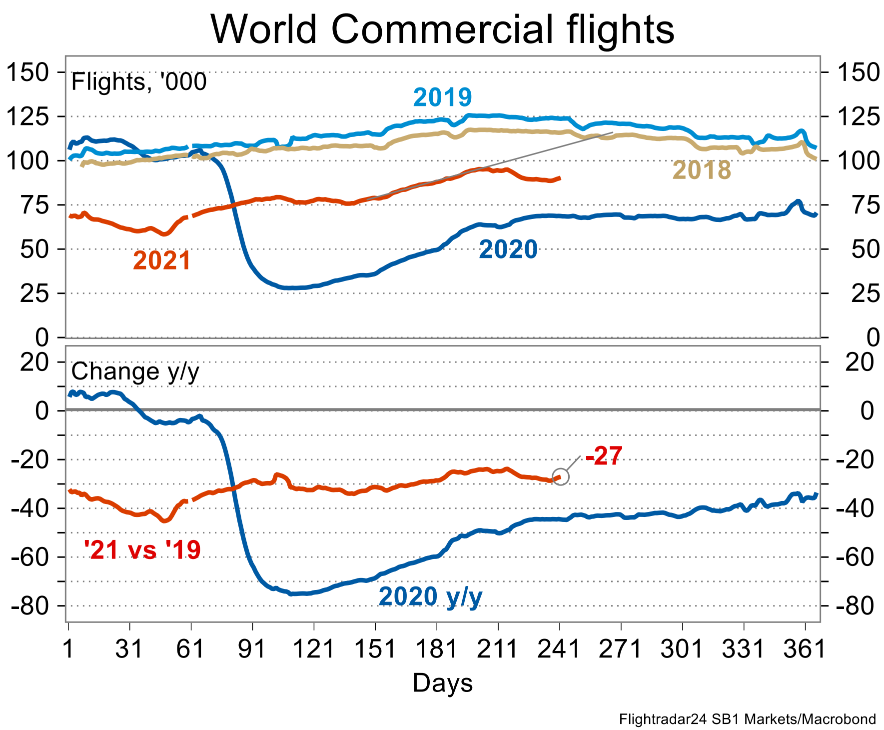
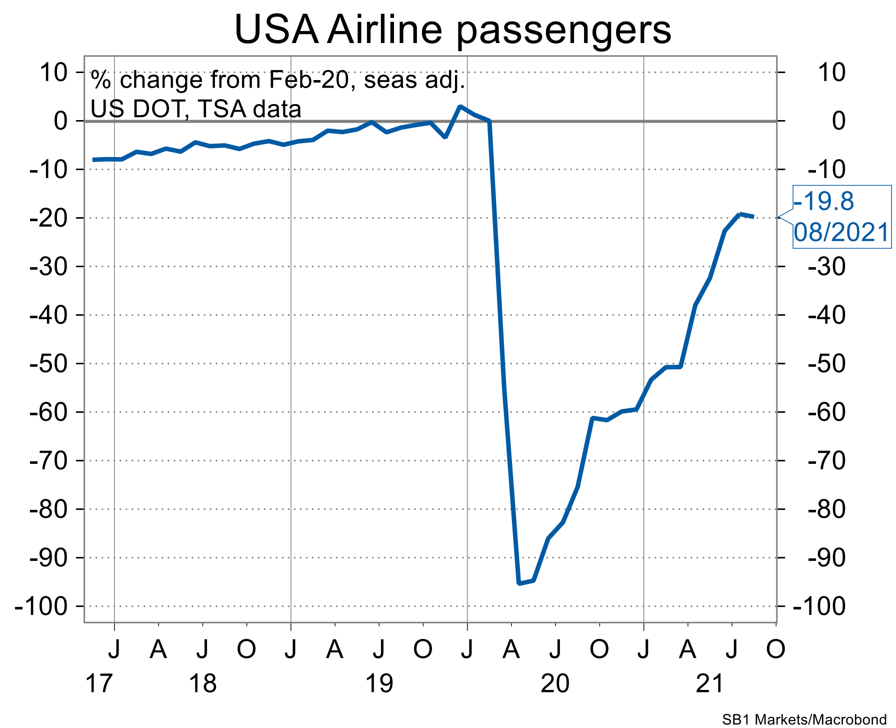
Global airline traffic may have bottomed, slightly up last week

In the US, traffic flatted in August, no doubt due to the Delta attack

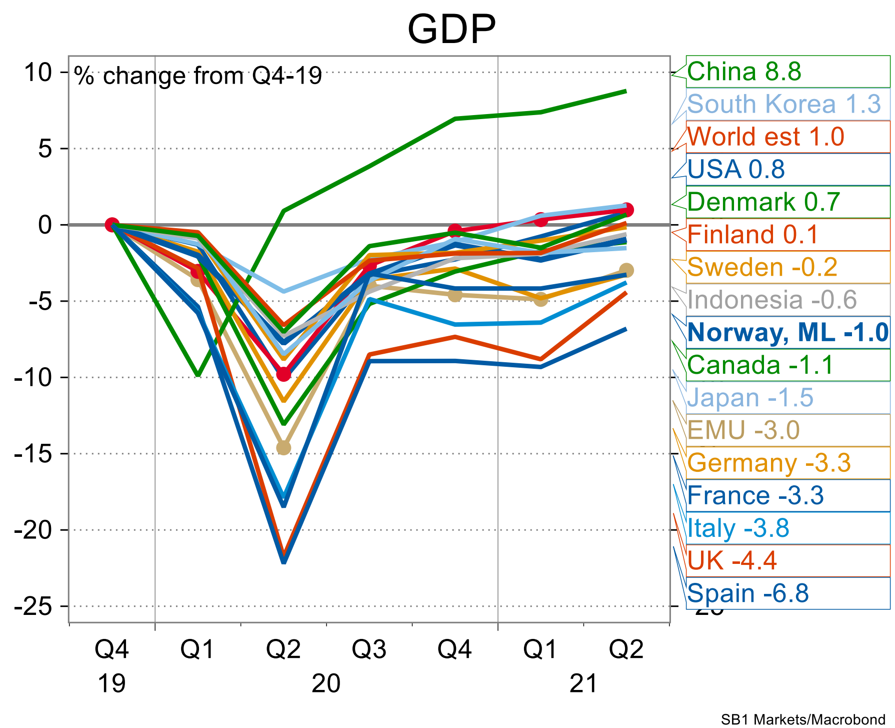


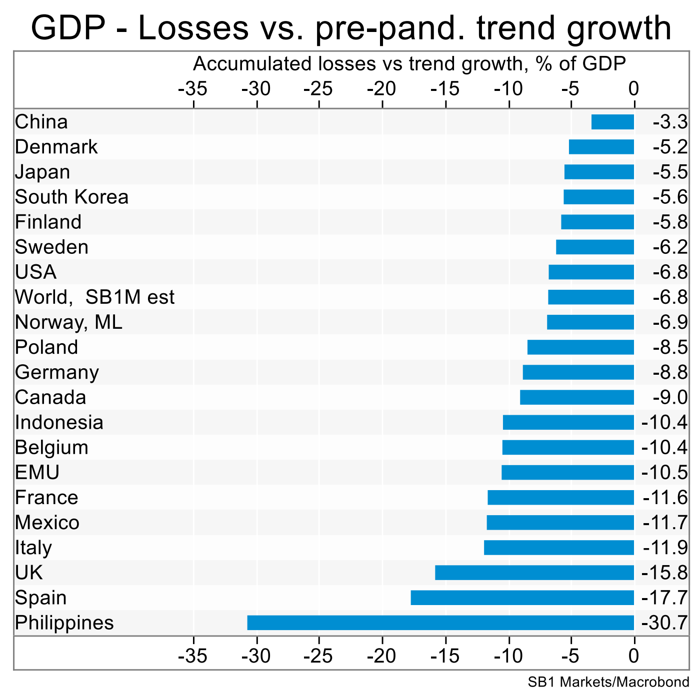


- Global traffic is down 27% vs. the 2019 level

Global GDP slowed in Q2

… as we assume slower growth in Emerging Markets (where few have reported so far)



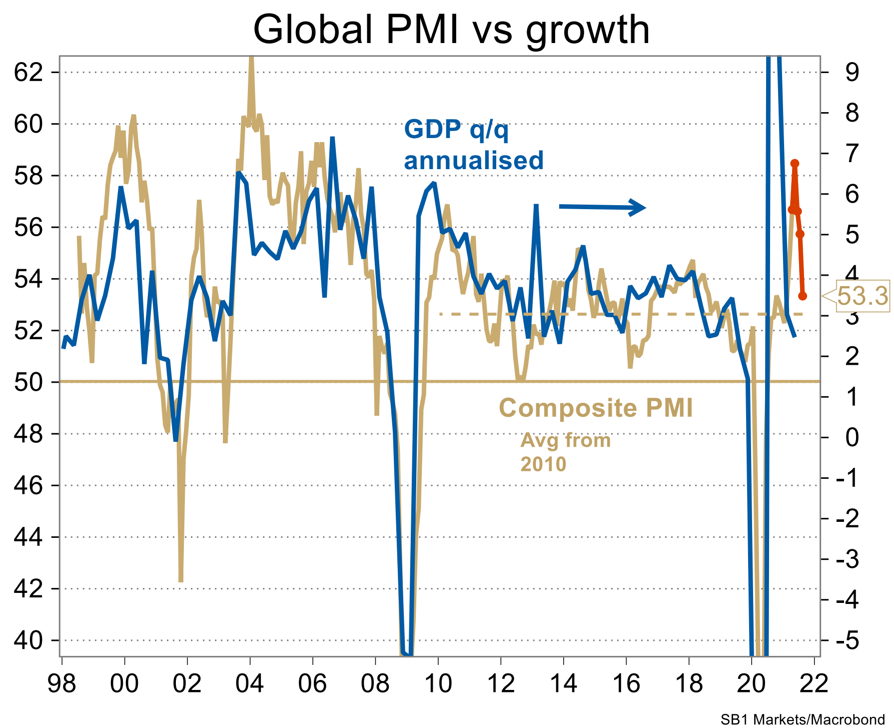


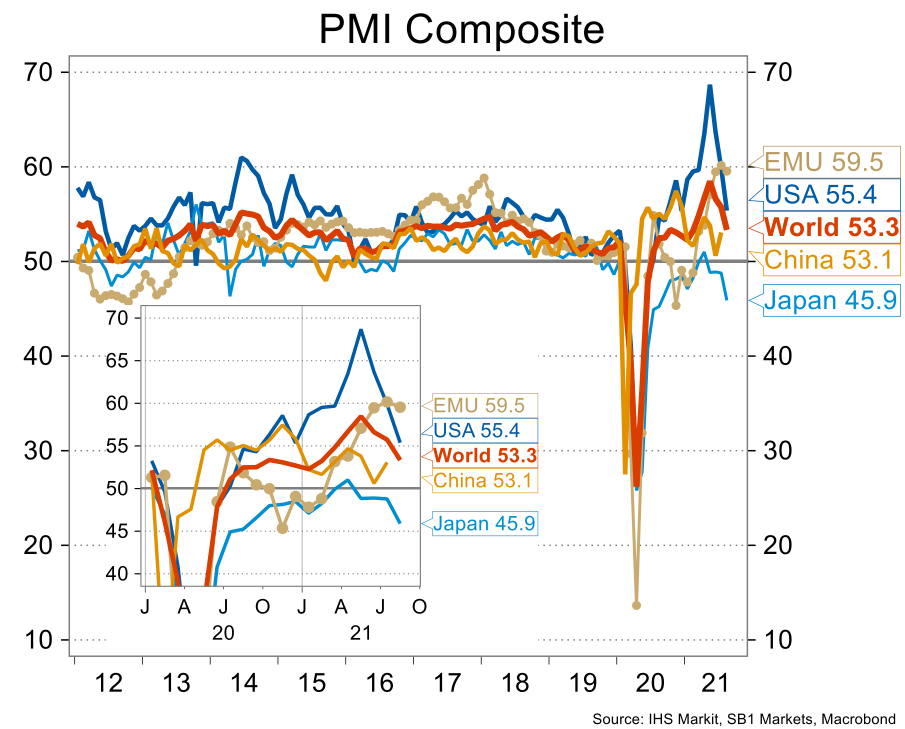
- We estimate a 2.4% **global growth pace in Q2** (0.6%), down from 0.8% in Q1
  - » The uncertainty is larger than normal due to the Covid outbreak in many Emerging Markets that has not reported so far (especially India)
- The global GDP is 1% above **the pre-pandemic level**, but still approx. 3% below the pre-pandemic trend growth path
- **Norway** is lagging our Nordic neighbours, both vs. the level in Q2, and accumulated losses during the pandemic (chart to the right)

- The **global accumulated loss vs the pre-pandemic growth trend** is some 7% of 1 year's GDP
  - » **China** is in the lead, with the smallest loss, 3.3%
  - » **US** is down 7% (which is among the smallest losses in a US recession since WWII)
  - » **EMU** is down 11%; Germany -9%, Spain -18%. **UK** is down 16%
  - » **Denmark** -5%, **Sweden & Finland** -6%, **Norway** -7% (as we where hit by the downturn in oil investments, check the chart two pages back)

PMI further down in August – to an average level

We estimate a 2 p decline to approx. 53, to an average level – based on weaker DM data



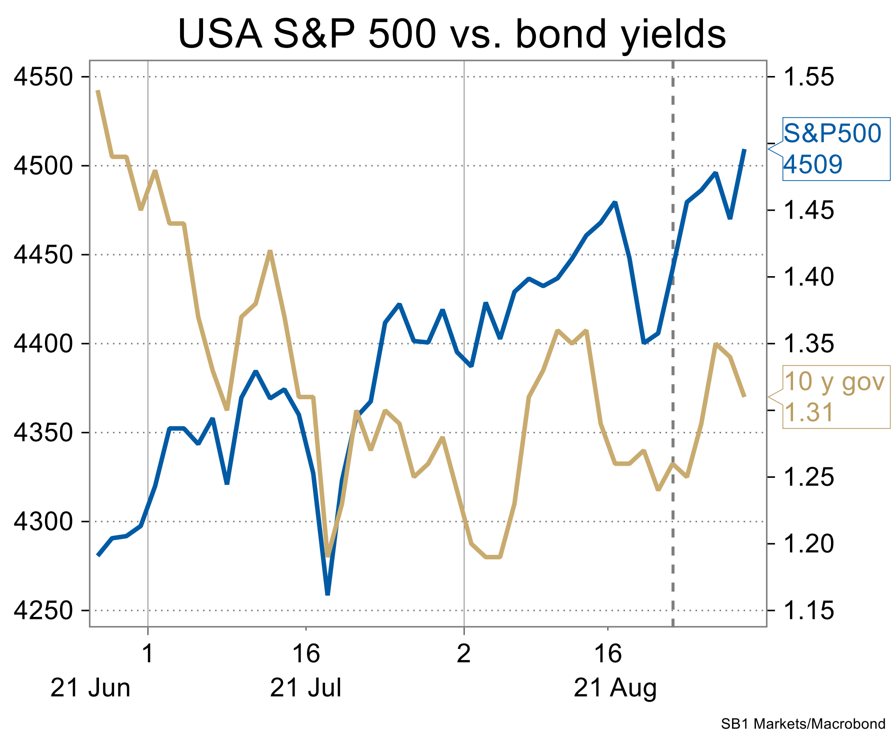


- **The global PMI** has peaked, so has very likely global growth. The August PMI signals 3% – 3.5% GDP growth
- **The US PMI** fell sharply, by 4.5 p to 55.4, far weaker than the expected -0.9 p, signalling 3% growth. The service sector PMI was the weak link in the chain
- **The EMU PMI** fell far less, by 0.7 p to 59.5, close to expectations – and the index signals 3% GDP growth. Services kept up well amid the Delta outbreak
- Both **Japan** and **UK** reported a decline in their PMIs in July, due to a sharp decline in services PMIs both places. Japan's PMI signals a GDP contraction
- **Delivery times rose even faster in the US, but slowed in Europe. Prices, input & output** prices are still increasing at a rapid pace but slower in August than in July
- In July, the **Developed Markets PMI** fell by 1.8%, while the **Emerging Markets PMI** rose by 1.2 p – but remained 5.5 p below the DM avg. It is possible the gap will be further closed in August – and that our estimate for the global PMI is on the weak side (like it turned out to be in July)

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

Fed will probably start tapering in Q4, but Powell argues rates will be kept at zero

Progress towards targets is sufficient for tapering but targets must be reached before a rate lift-off

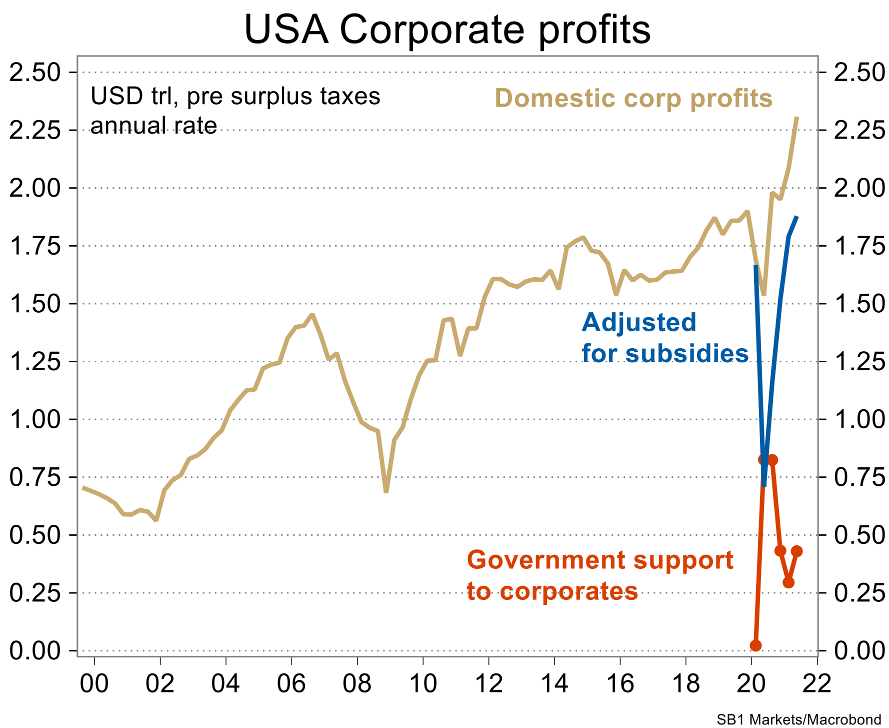


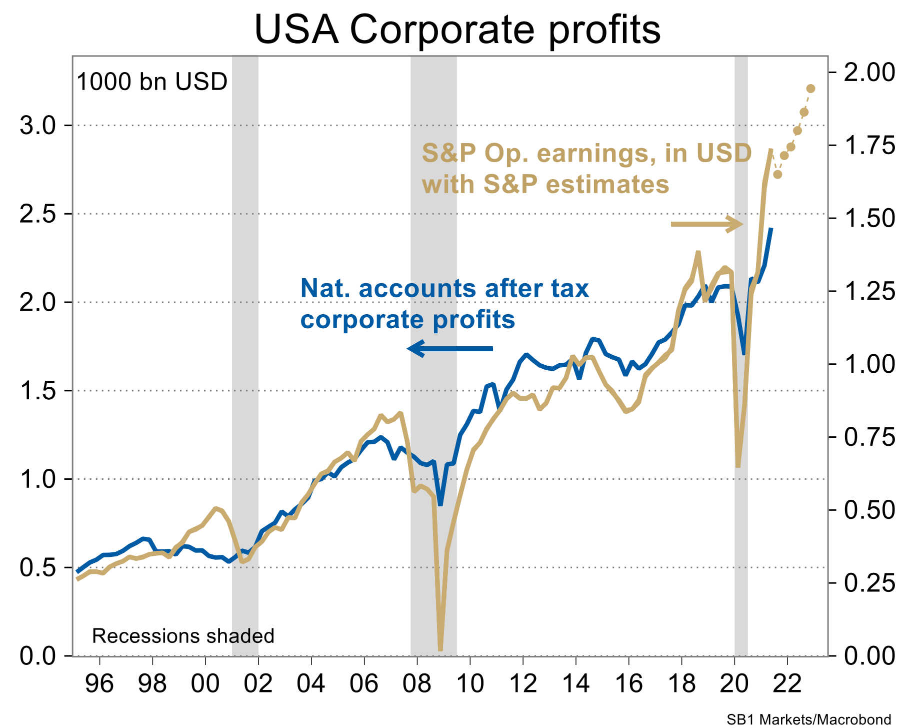
- **Markets** had discounted a late 2021 tapering start, and was not chocked by Powell's 'confession'
- Rather, markets responded favourably to his comments on when to hike rates, and that he still assumes today's high inflation will turn out to be transitory
- **Interest rates/bond yields fell** (real rates down, infl. expectations rose, a reasonable response), and another ATH was reached at the **stock market – cheap money forever**

- At the **Jackson Hole (digital) conference Powell** revealed that he – at the late July FOMC meeting – argued for starting tapering the QE program in late 2020 – if the labour market made further progress towards the target. The inflation criteria was met, and as the labour market had strengthened, substantial progress towards the maximum employment target has been achieved, and further progress was expected. Did we really hear him indicate that at the press conference following the meeting??
  - » Data since late July had confirmed his view, according to Powell, even if the Delta variant created increased uncertainty
  - » However, minutes from the meeting revealed that many FOMC members assumed that the Fed should start reducing the USD 120 bn/month QE program later in 2021, and several FOMC members have been very outspoken recently, in favour cutting back the QE program as there were no lack of demand in the US economy but rather lack of supply
- Once more, Powell stressed that <u>start of tapering did not imply the policy rate would be lifted anytime soon</u>. For tapering, progress towards targets were sufficient. For a rate take-off: Targets has to be reached
  - » The economy has <u>reached conditions consistent with maximum employment</u> (which is still not defined), <u>and</u>
  - » And Inflation has reached 2% on its track to <u>moderately exceed 2% for some time</u> (even if this argument was introduced when inflation had been too low, and the average inflation rate had to be brought up to 2%. Now it is, and more than that)
  - » He added: <u>We have much ground</u> to cover to reach maximum employment and <u>time to tell</u> whether we have reached 2% on a sustainable basis
- In his speech, he stressed than several factors could dampen inflation, as soon has the impact from the pandemic faded
  - » He did not see broad based inflation pressures
  - » Moderating inflation in higher-inflation items, like 2nd hand cars, which have flattened (and durable goods prices have been falling for 25 years)
  - » He saw little evidence that wage increases that might threaten excessive inflation
  - » Longer term inflation expectation were not elevated
  - » Global disinflationary forces had ruled for 25 years (technology, globalisation, perhaps even demography) and central banks' commitment vs low inflation had stabilised expectations

Corporate profits surged in Q2, both for ‘real’ and due to more government subs.

Domestic corporate profits up 11% q/q. Government subsidies still lift profits by 23%!

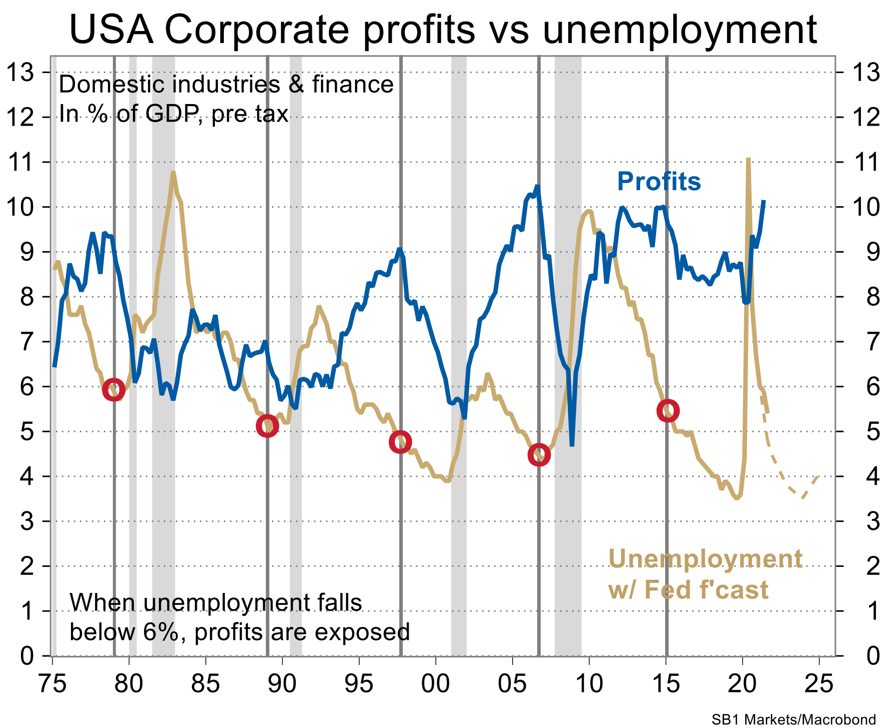


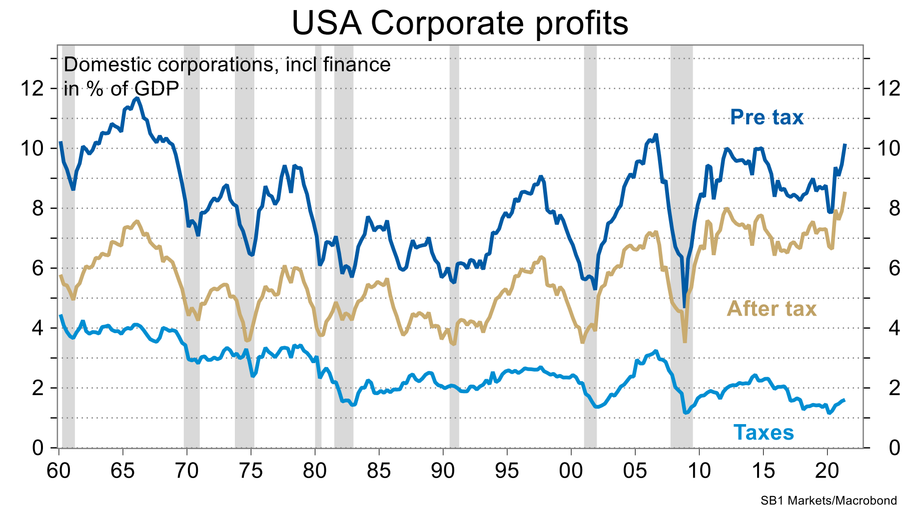


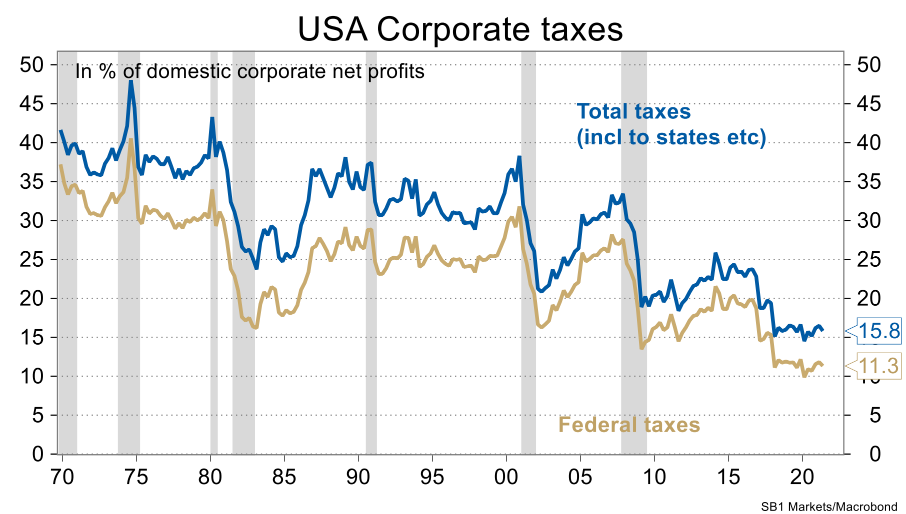
- **Government pandemic programs** have lifted **domestic corporate profits** at an unbelievable scale – and still support profits by 23% of normal profits. In Q2, the public support rose somewhat vs. the Q1 level, we expected a further reduction
  - » It is possible that some of the new programs that have been decided upon – and may be decided (the infrastructure program) have some elements of subsidies included, so that subsidies will remain at higher level than before
  - » Wages rose less than value added in Q2 (2% vs. approx. 2.3%), and thus far less than profits (+11%)
- We very much doubt profits will climb as fast at S&P’s forecast on the chart to the right
  - » We expect subsidies to decline, wage inflation will pick up, or top line growth (GDP) will slow

Profits were under pressure prior to corona – as usual when unemployment falls

… and for how long will unemployment remain high enough to 'protect' profits now?



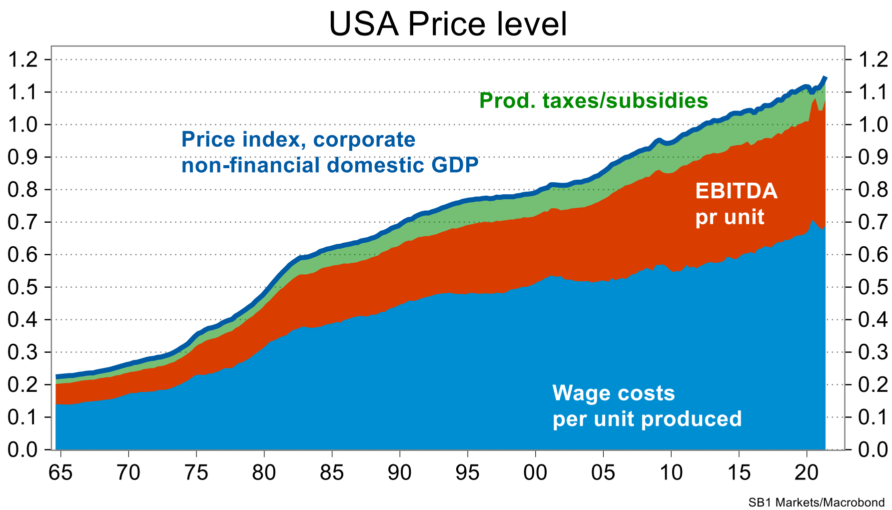


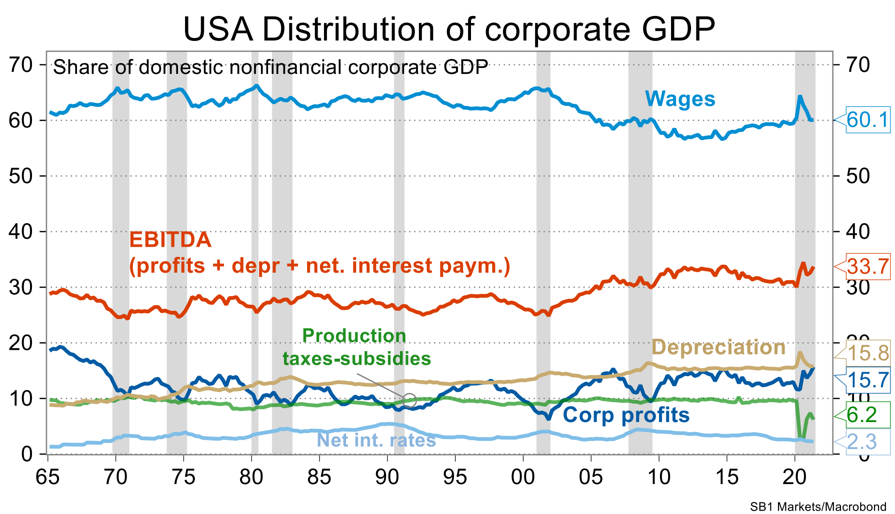


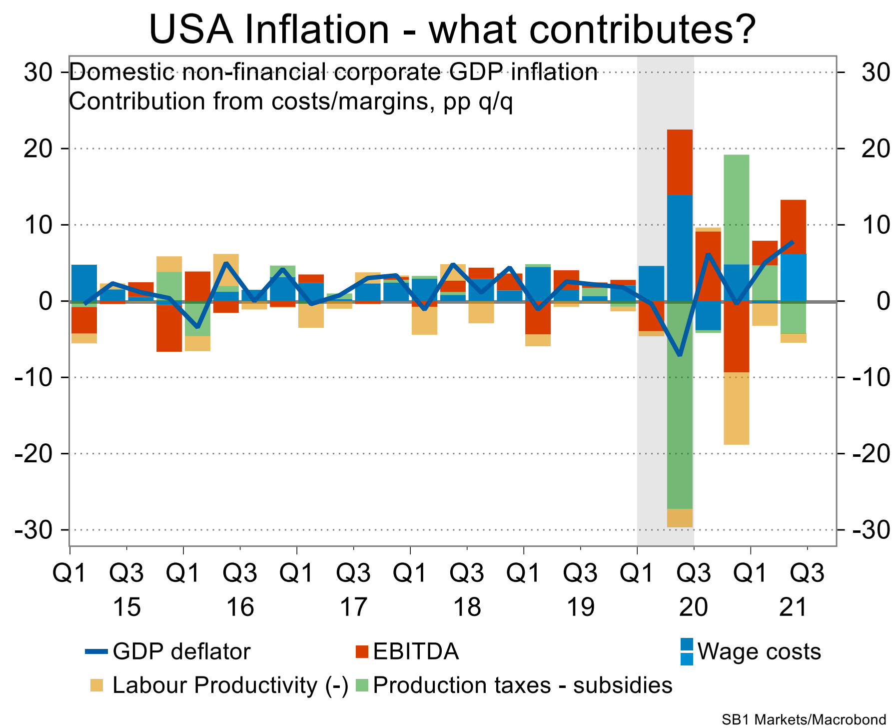
- When **unemployment falls below 6%,** corporate profits are exposed; at one stage the profit share will start to decline because wage earners will get the upper hand vs. employers. At least it has always happened in the past
  - » Before the corona crisis, the pre-tax profit share had fallen since the 2015 peak, because unemployment was 'too low' (however, profits have been revised up vs. previous estimates, the decline is less pronounced). After tax profits are record high vs GDP
- Taxes were cut substantially in 2018, equalling some 8% of corporate profits. Some of these cuts will probably be reversed in order to fund the infrastructure plan and the 'welfare' budget which now both are debated in the House

Why are prices on the way up?

In Q1, Q2: Higher margins, higher wages costs



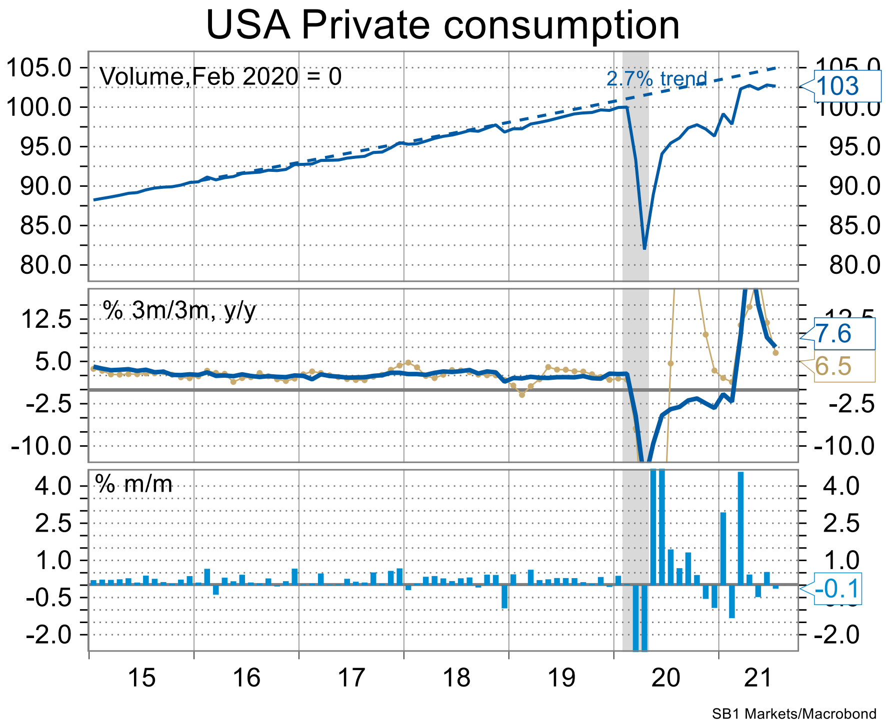


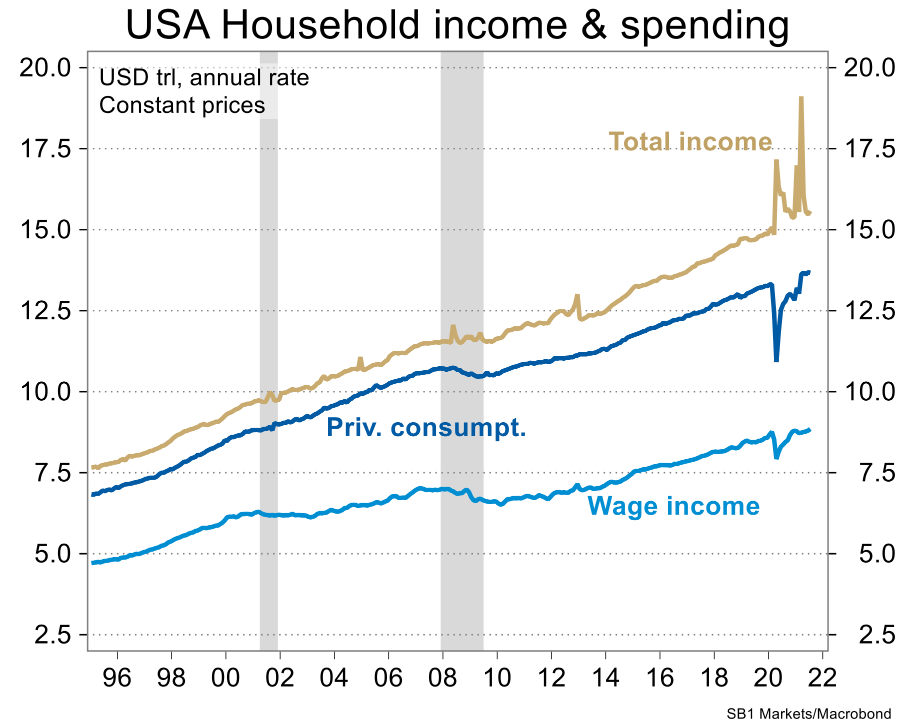


- Changes in subsidies recent quarters creates huge ups and downs in costs
- These subsidies will probably normalise the coming quarters – creating a pressure on prices and/or margins and wages
- Wage costs have been moving upwards

Household income up in July, real spending flat – and it has been flat since April

Signals substantial slowdown in GDP growth. The savings rate just 2 pp above the pre-pandemic level

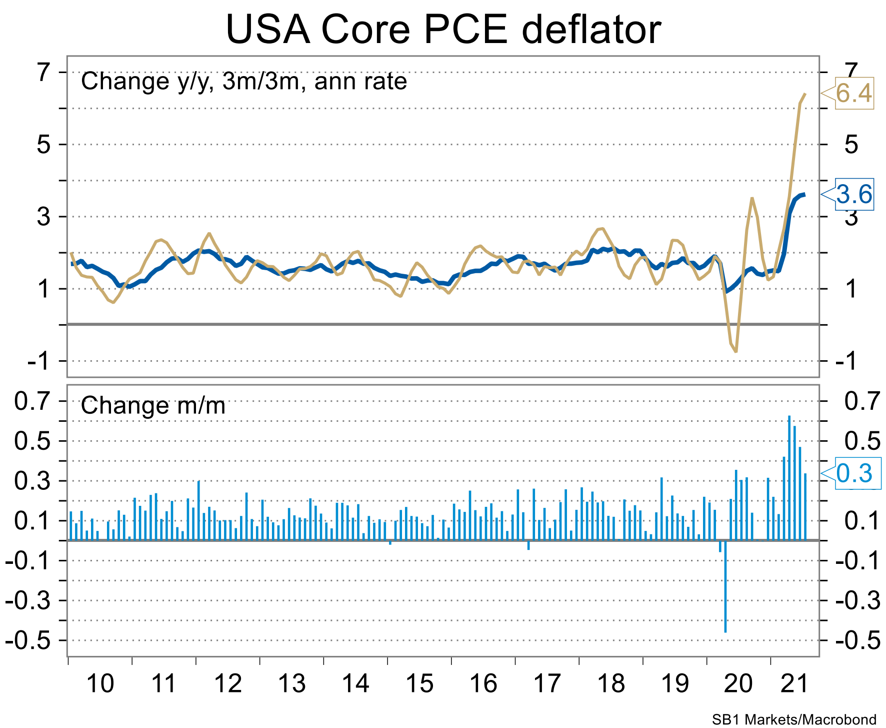


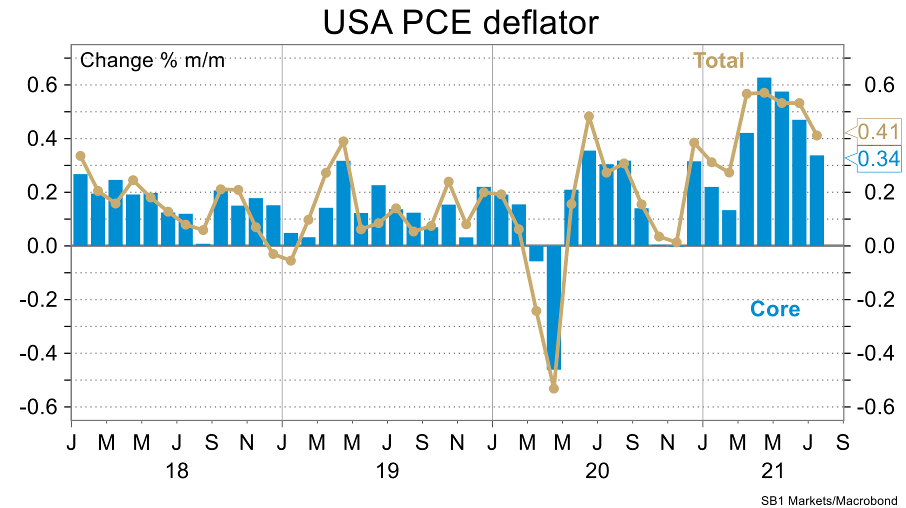


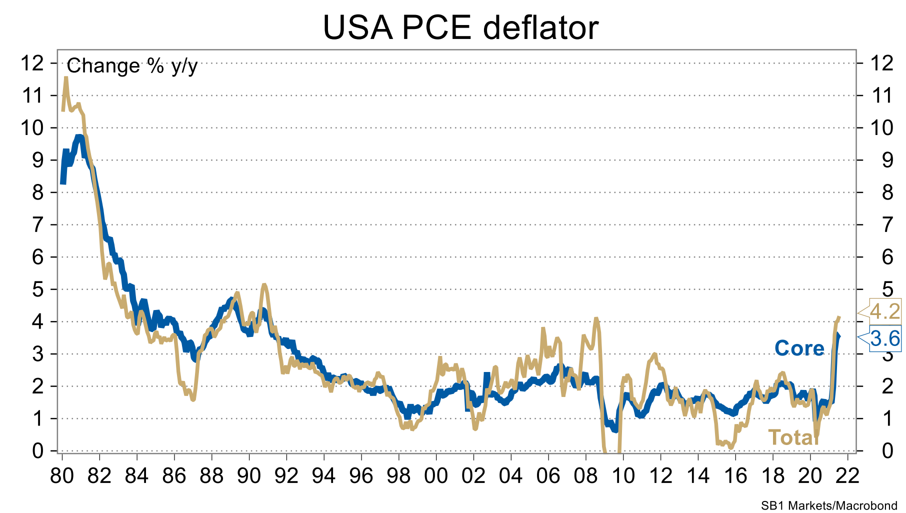
- **Private consumption fell** 0.1% in real terms in July, a tad less than expected (spending rose 0.3% in nominal terms, expected +0.4%). Consumption in real terms have flattened since April, as goods have yielded while services are recovering – but not that fast
- **Personal disposable real income** rose by 0.7% in July (household income rose by +1.1% nominally, expected 0.1%). Government transfers contributed to most of the increase, probably also vs. expectations. Market based revenues rose too, wage incomes are steadily on the way up
- **The savings rate** rose by 0.8 pp to 9.6%, following another downward revision (-0.6 pp this time). The savings rate is some 2 pp above the pre-pandemic level. In addition, since the pandemic started, households have saved an extra amount equalling 13% of one years GDP. There is still some money to be spent

Core PCE up 0.3% in July, 3.6% y/y – as expected

Price inflation is slowing (m/m) but is still too high, in July at a more than 4% annualised pace



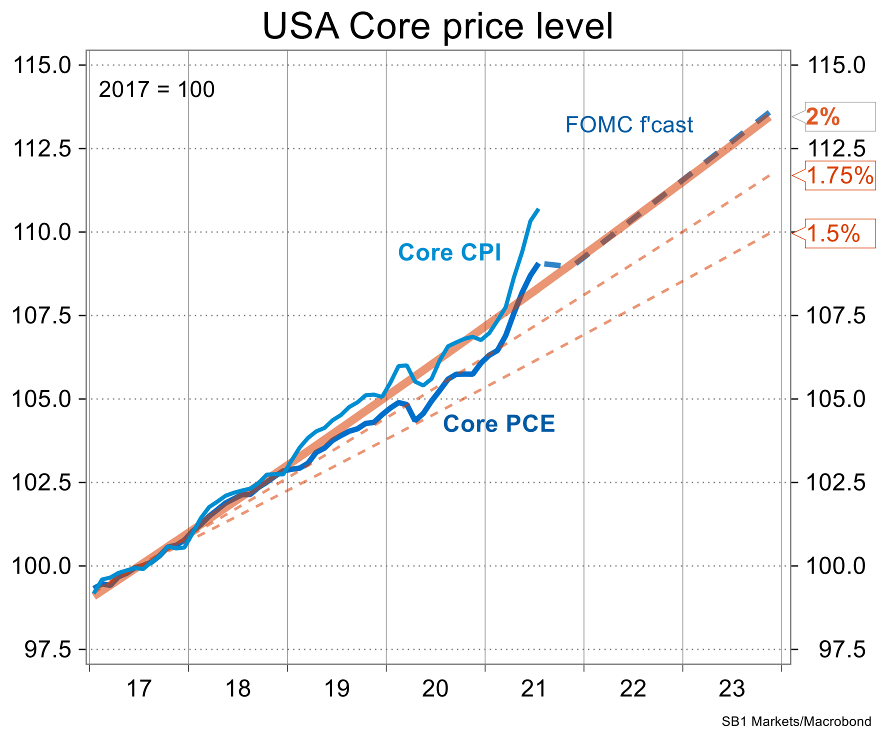


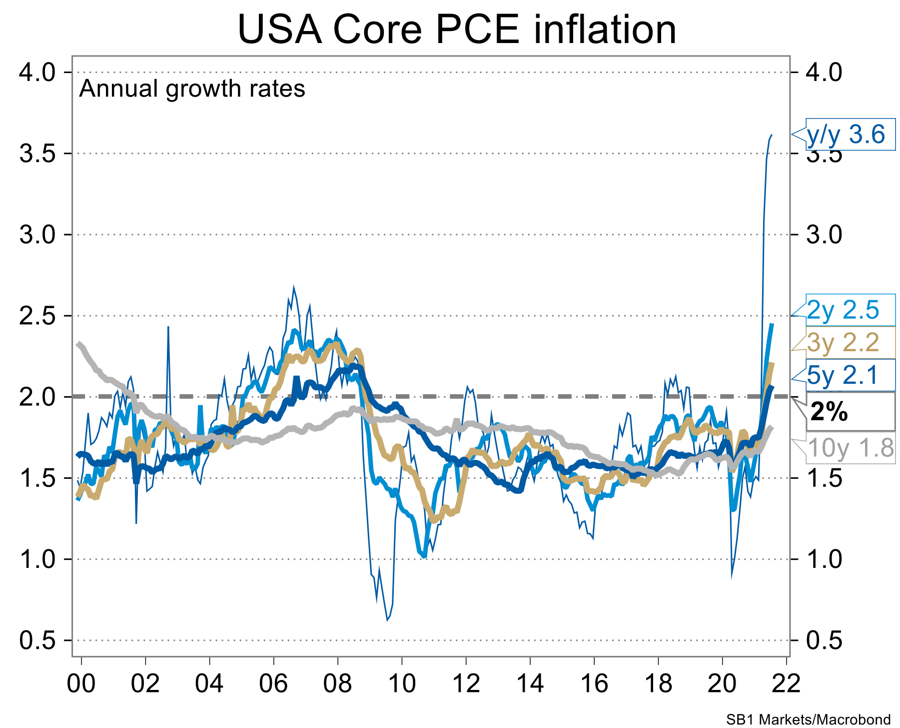


- **The core price consumption deflator** rose by 0.3% m/m in July, as expected. June was revised up 0.1 pp to 0.5%. The annual rate rose 0.1 pp to 3.6%, well above Fed's long term 2% inflation target
  - » Since June '19, the average core inflation rate has been 2.5%. Inflation has been higher than 2% measured up to 7 years back in time. So whatever plausible horizon Fed would like to apply, the average over time 2% inflation target is met (and more than that)
- **The total PCE deflator** rose by 0.5%, and the annual rate accelerated by 0.2 pp to 4.2%, both 0.1 pp higher than expected

The price level is on the right track, right? Finally, even Powell said so

However, he is still stressing that the recent hike is transitory – and he may still be correct



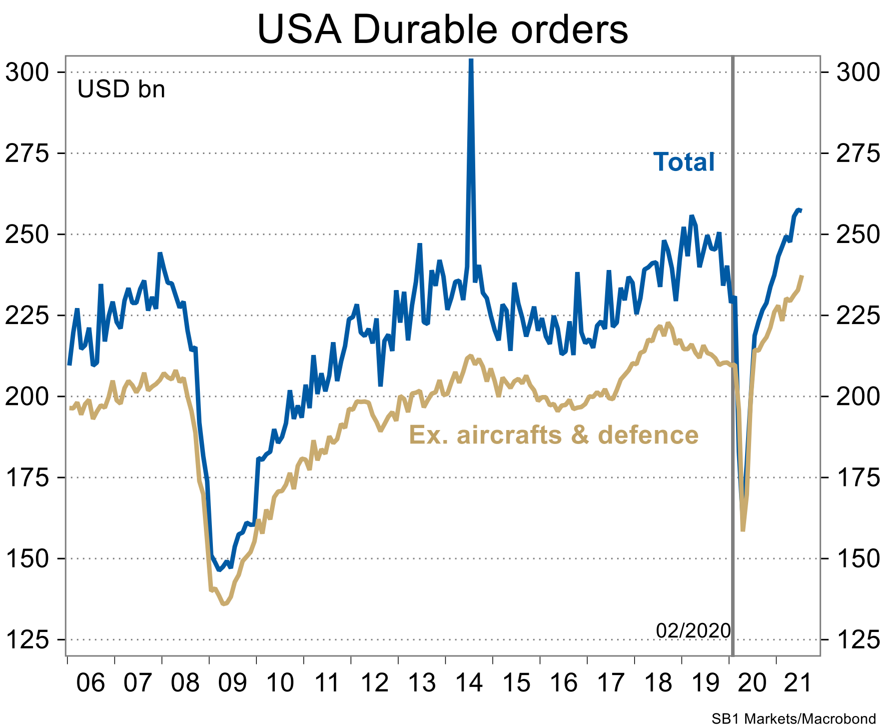


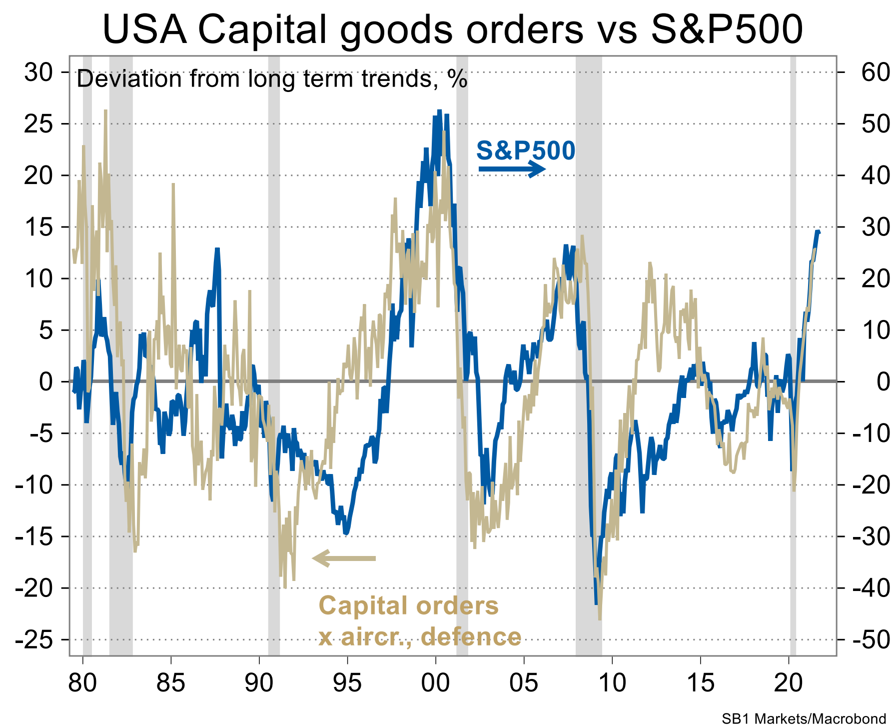
We stick to our main inflation analysis:

- **Raw material cycles** are not lasting that long and the impact on consumer prices are short lived
- **Higher profit margins** (unit profits) have never been the main reason for a sustained lift in inflation
- To sustain a lasting increase in inflation, **unit labour costs** have to grow faster. The ULC = wage inflation – productivity
- **A tight labour market** normally implies higher wage inflation. Now, almost all wage cost indicators signal higher wage growth, and more than the tilt towards higher paid employees can explain. This is the real challenge for the Fed

Core durable orders further up in July

Investment goods orders are trending up too, signalling further growth in business investments in Q3

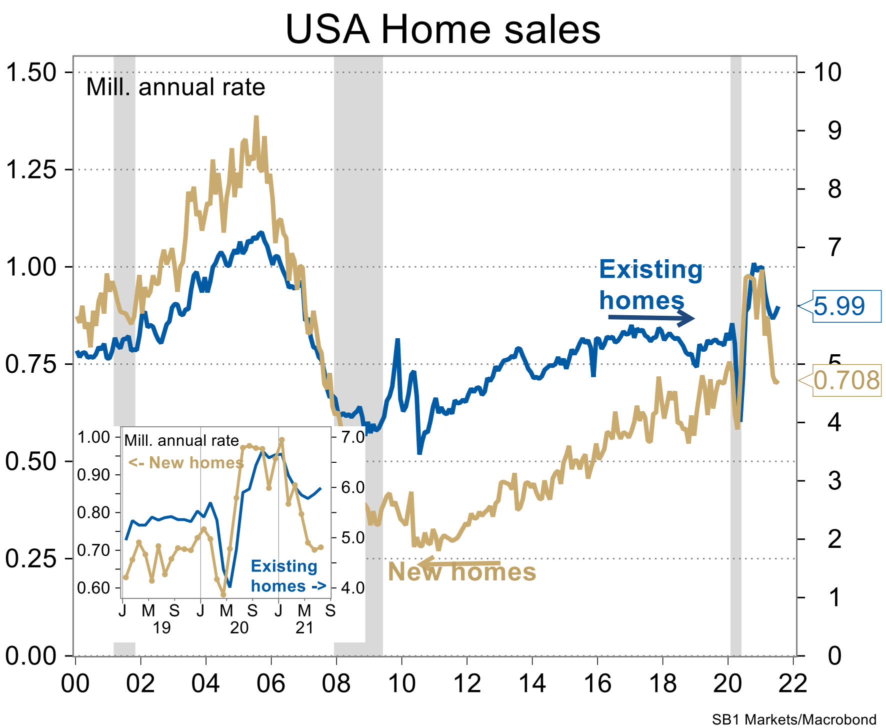


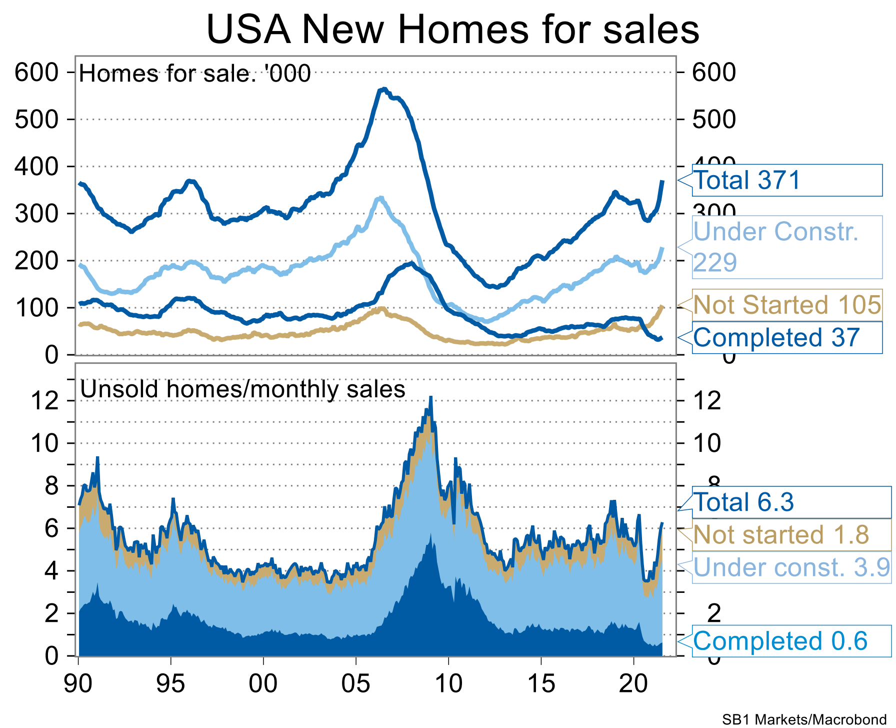


- **Total durable** orders fell by 0.1%, expected down 0.2%. Aircraft orders fell (but they have recovered for last year's slump). The trend is steeply up
- **Core orders** (ex aircrafts & defence) gained 2%, expected 0.5%. The trend is strong. Auto orders rose sharply in July
- **Core investment goods orders** fell 0.1% but the trend is still straight up, and order inflow in Q2 will be well above the Q1 level
- **Order inflow** is far above pre-pandemic levels, especially for investment good orders and surveys are still strongly hinting a further increase the coming months

New home sales slightly up in July, still down.

Too few completed homes to chose between? However, more new homes are underway

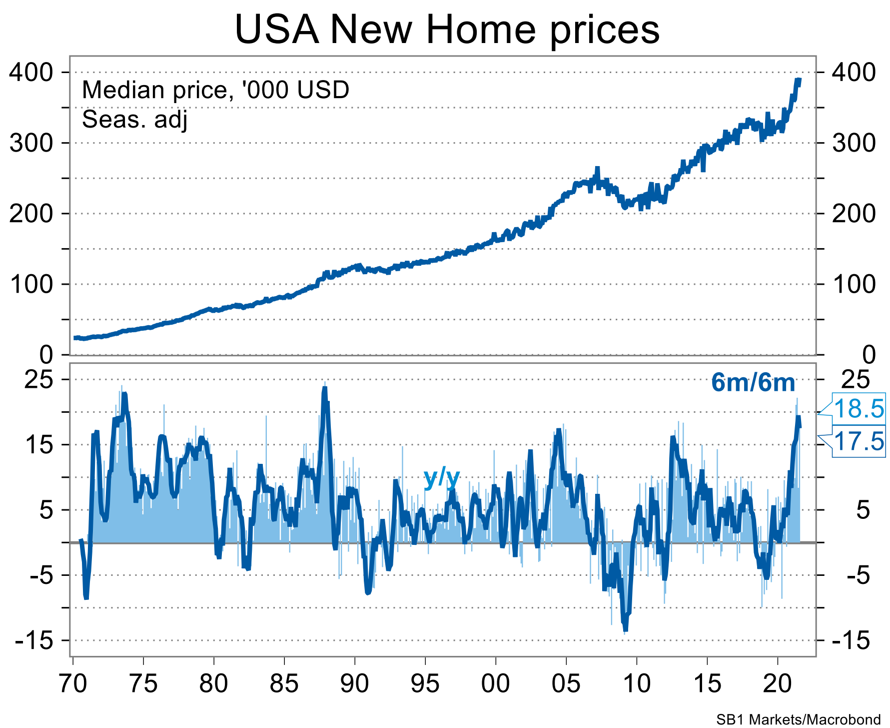


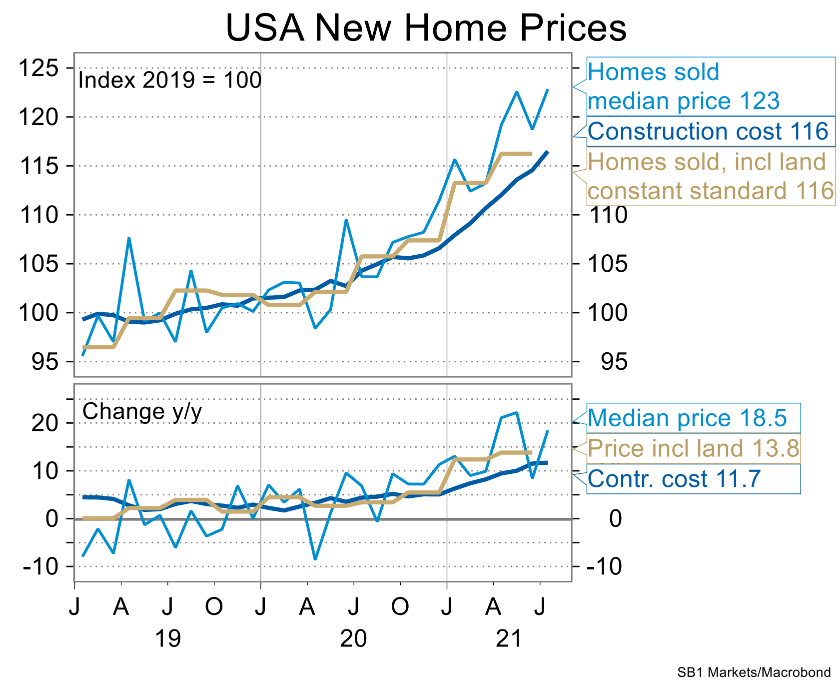


- **New home sales** rose to 708' (annualized rate) in July, up from down from 701' in June (revised up from 676', following several and larger downward revisions the previous months). Sales were expected at 700' in July. Sales are down 29% from January – and marginally below the pre-pandemic level. *On existing home sales: 2 pages fwd*
  - » The inventory of unsold homes has increased somewhat the past 8 months primarily because many projects that haven't started yet have been added, in fact more new projects than ever, a sign that the supply side is responding to the strong demand. The no. of completed homes for sale is record low, equalling 18 days' sale (if homes are sold 7 days per week)

Construction costs up, but new home prices even more

Construction costs are up 11% y/y, selling prices are up 14% – 16% (like existing home prices)

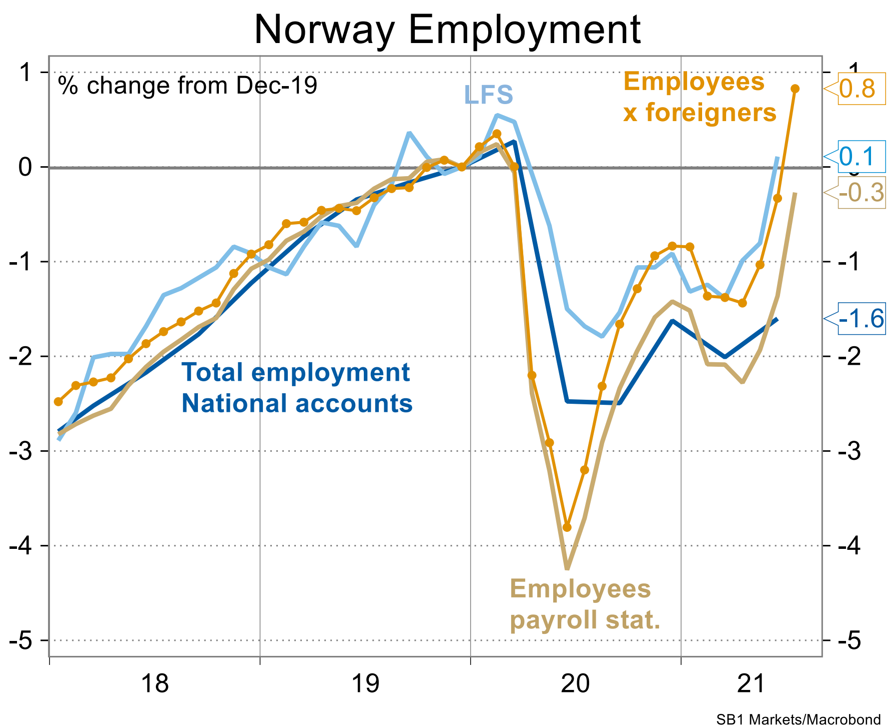




- Monthly **Median new home sales prices** are volatile, in July the annual rate was 18.5%, up from 6% in June (and 20% in May). The more relevant figure is the 6m/6m rate at 17.5% - the highest since 1987
  - » This price index is influenced by changes in the mix of homes sold – and over time by changes in standards & size
- The **construction price index** is adjusted for changes in standard & size, as is the **new homes sold price index**, which includes cost of land, and they are up by 12% and 14% resp. y/y (the latter Q2 data)
- As prices are still up more including land than the construction cost index (which of course is influenced by higher material costs), demand must be the main driver for the hike in prices (if not, land prices would have declined)

Employment surged by more than 1% in July (from June!)

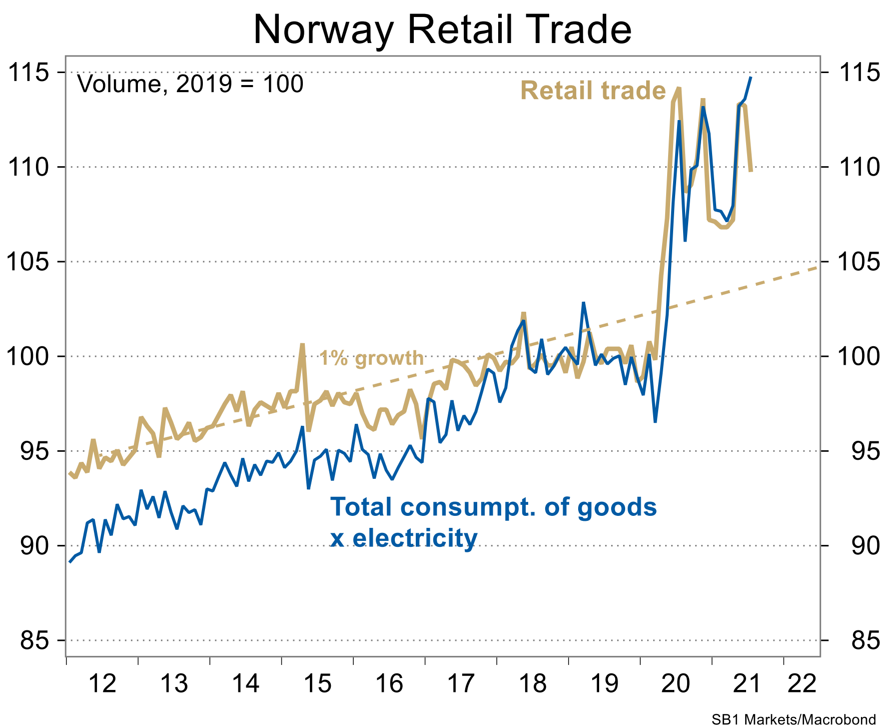
The no. of employees rose by 1.1% m/m in July, and is just 0.3% below Dec-20. Domestic empl. +0.8%

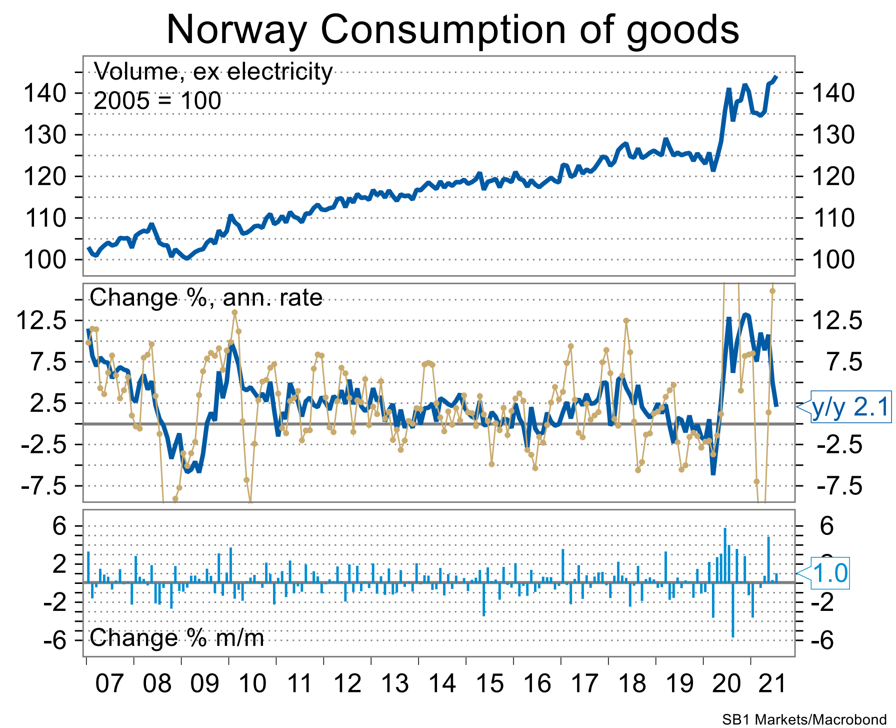


- The increase in employment in July suggest at brisk growth in Mainland GDP
  - » We do not have data for foreign workers on short-term stay for Q3, and 'domestic employment' (Norwegians and foreigners on permanent stay) in July is a estimate but probably not too far from the mark
  - » In June, employment grew by 0.8%
- **The LFS** (survey) employment data have also been strong recent months, the last data point is the April-June average
- **National Accounts** reported a modest rise in overall employment in Q2, and the level was still 1.6% below Q19. The NA data includes foreigners on short-term stay

Retail sales of building materials down 18% but consumption of goods further up

Total retail sales fell 3.1% (we expected -0.5%, consensus -0.4%), but consumption up 1%

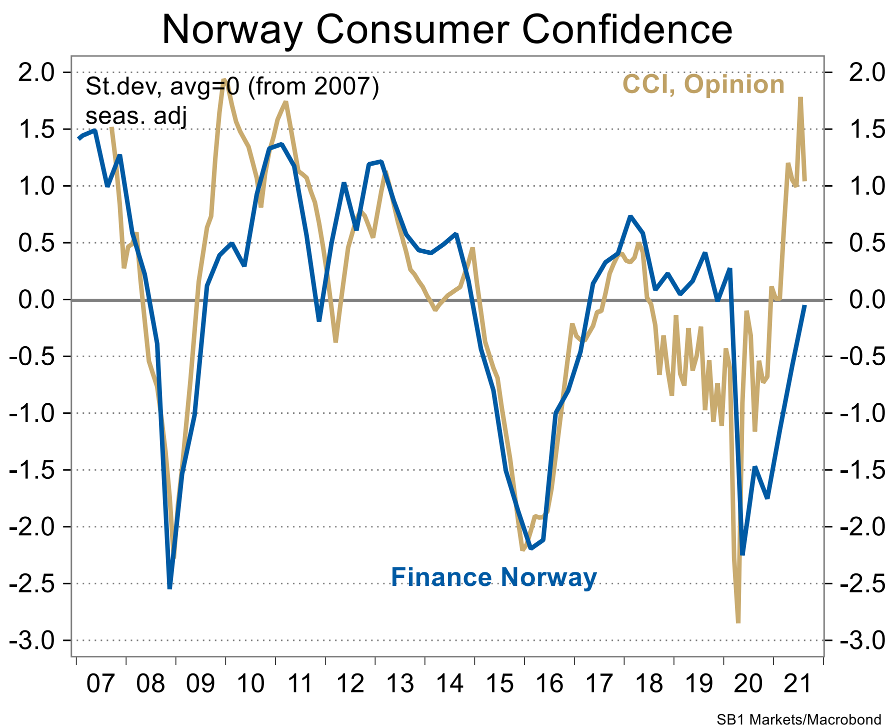




- **Retail sales** were down 3.1% m/m in July – far below expectations. Sales are still 10% above the pre-pandemic level
  - » The steep decline in retail sales were exclusively driven by a 29% drop in the sales volume of **building materials, and other hardware**. Prices rose 26%, and sales fell 10% in value terms. The decline is in the sales volume is probably both due to lack of supply and reduced demand due to the unprecedented price hike (which may be somewhat exaggerated – more on that next page)
- **Total consumption of goods** (x electricity) still rose by 1% in July! We have never seen such a discrepancy m/m (when adjusted for auto sales, which are not included in retail sales). Thus, household demand rose further in July, even if retail sales fell
  - » The reason is differences in weighting in the retail trade vs the private consumption index. Building material etc constitutes approx. 8% of retail sales. However, a large proportion of these sales are not sales to consumers but rather to professionals, like home builders, carpenters. In the goods consumption index just direct sales to consumers are included. The building material/hardware weight in total goods consumption may be below 1% (no exact data published, but the share in the CPI is low)
- **We still expect sales/consumption of goods** to slow further in the coming quarters, back the pre-corona trend path – when it becomes possible to spend more on services and abroad, both x-border shopping in Sweden and holiday travel in general

Consumer confidence reversed the July spike, and is still at a high level

Opinion's CCI fell by 0.7 st.dev, and almost reversed July hike. The level is still +1 st.dev

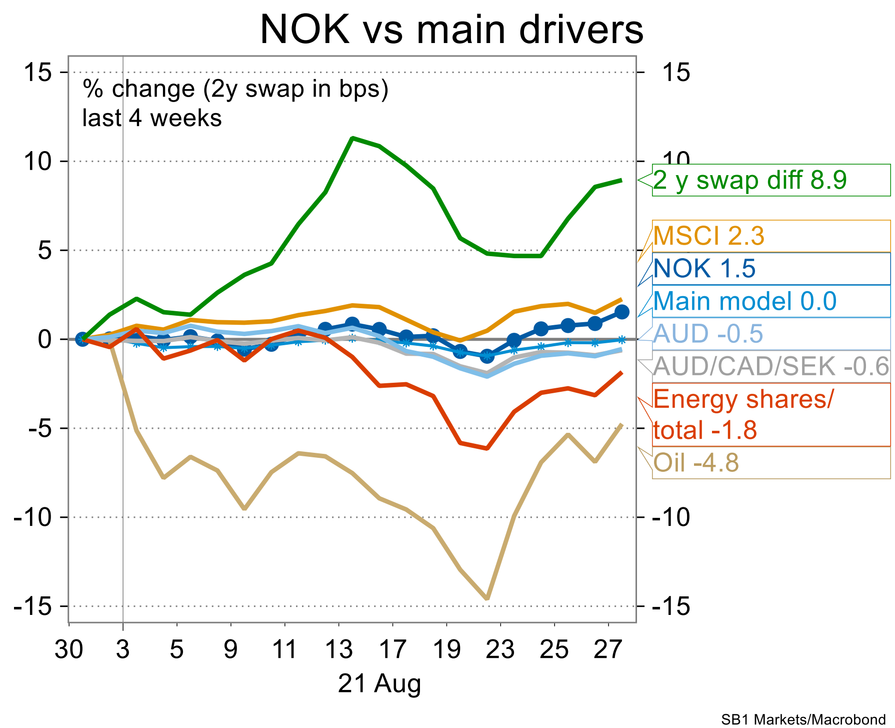


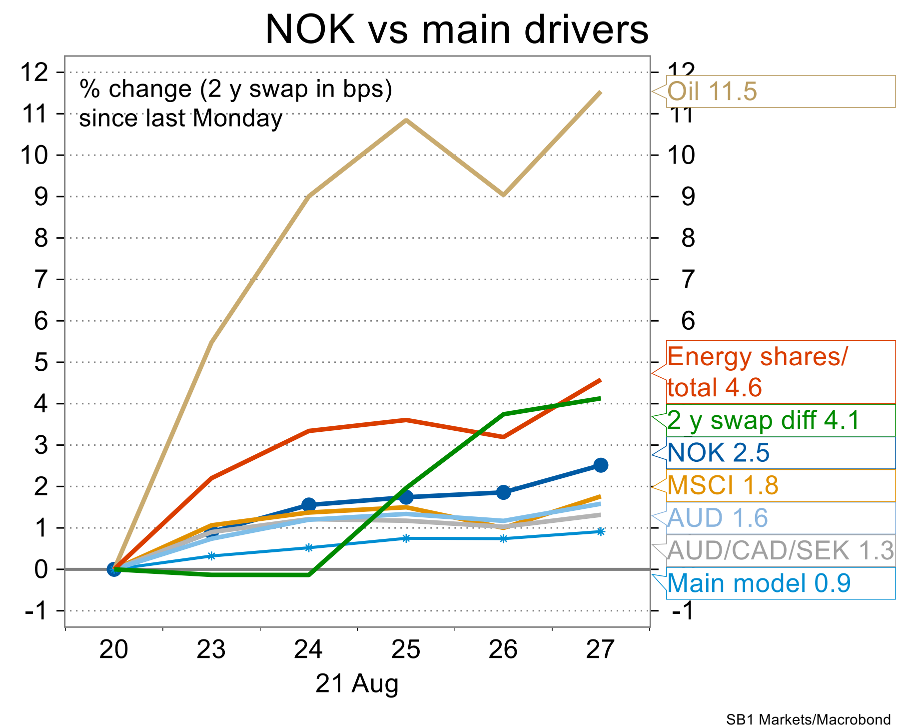
- The lift in July was substantial, 0.8 st.dev – as was the 0.7 st.dev decline in August. The level in August is still strong
- Finans Norge's confidence quarterly survey rose to an average level in Q3. This survey has been far weaker (some 1 st.dev) than the CCI survey the last year – and it still is. We have no good explanation for the discrepancy
  - » Given retail sales & the housing market Finans Norge's survey seems too weak

SpareBank 1 MARKETS

NOK up 2.5%, supported by oil, int. rates, fx peers & global stock markets

Our traditional model suggested an 0.9% appreciation





The status vs. the normal drivers:

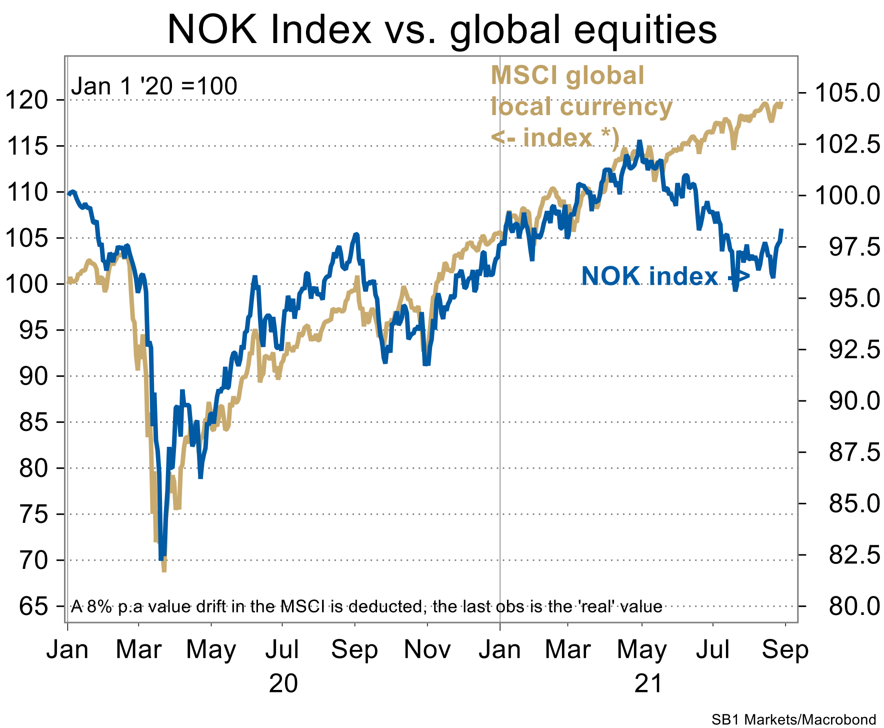
- ***The NOK is 6% <u>weaker</u> than suggested by our standard model (from – 8!)***
- The NOK is 6% '<u>weaker</u>' than the global stock market vs the correlation between the two since beg. of 2020 (from -7)
- The NOK is 9% <u>weaker</u> than our AUD/CAD/SEK-model, our 'super-cycle peers', predicts (from -10)
- NOK is far (10%) <u>stronger</u> than a model which includes global energy companies equity prices (vs the global stock market) (from 9)

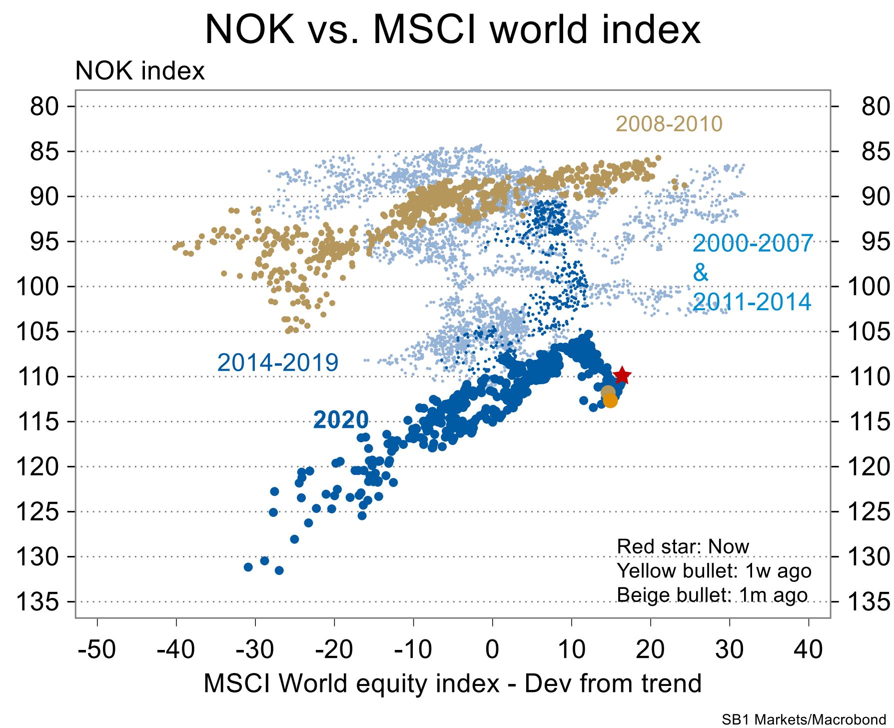
After been neutral vs NOK from May, we turned positive in early July, as the gap vs. our models had widened. *We have been wrong but less so now* ☺

At this and the following pages we have swapped Norges Bank's I44 index for JP Morgan's broad NOK index and rebased it to the current index value for the I44. The I44 has an earlier closing time than the 'official' closing time for fx crosses. There are no substantial difference between these two indices over time

The global stock market up, NOK even more

Still, NOK has lost some 6% vs. global stocks since May but 'gained' 1% last week

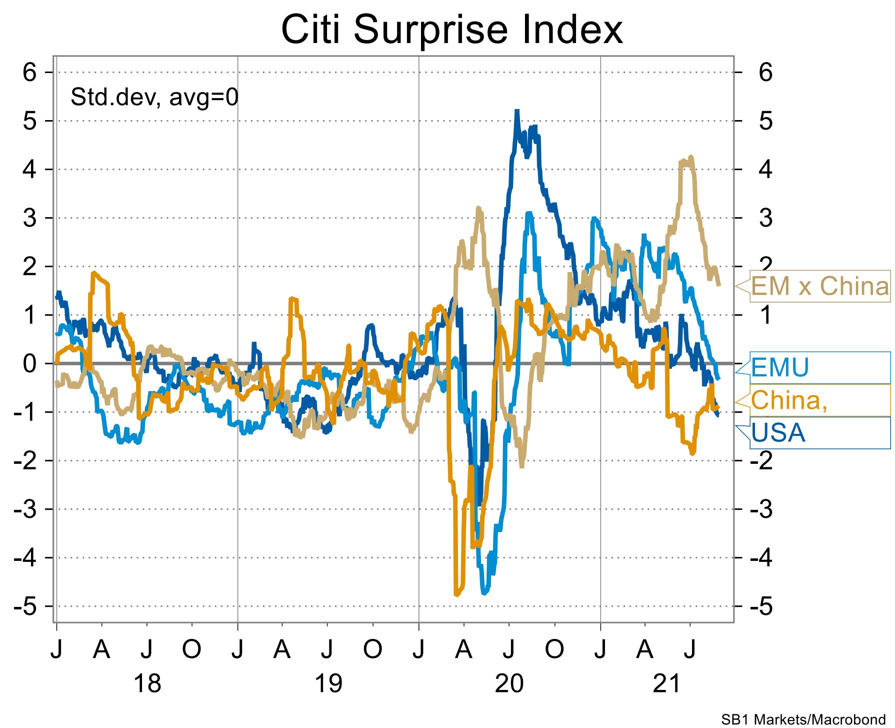


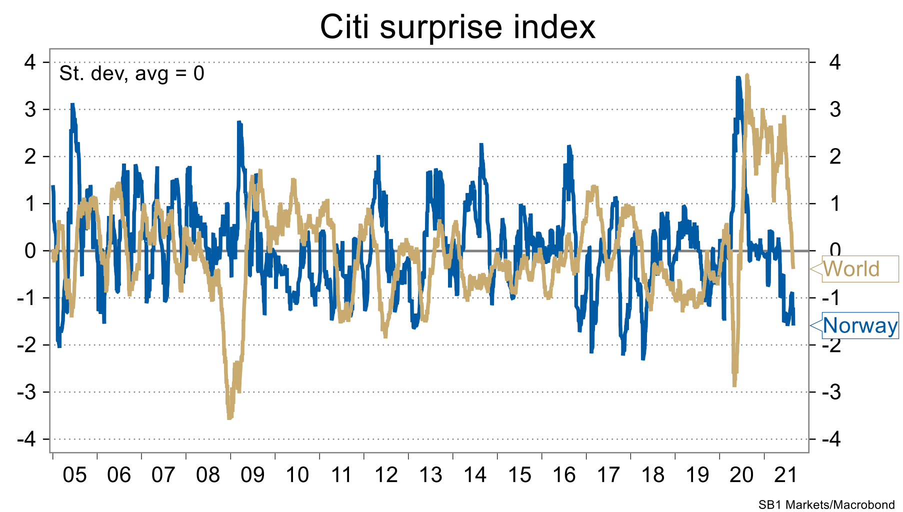


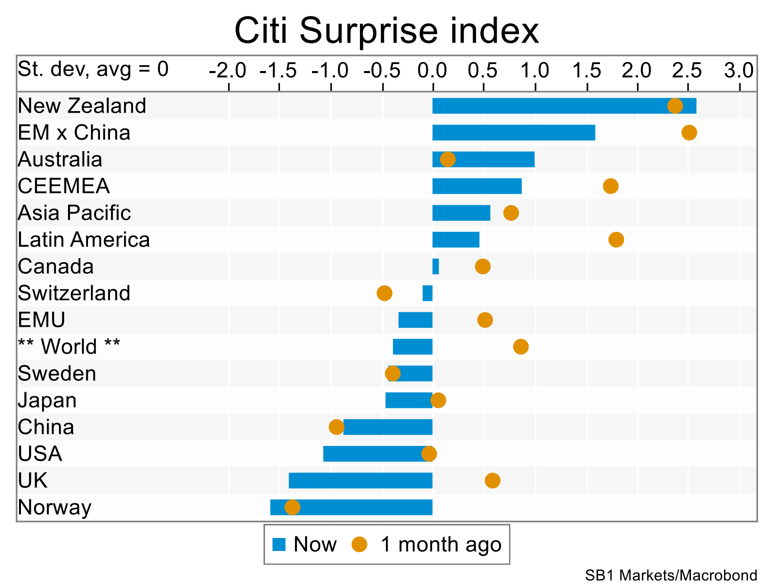
- Over time, there has not been a stable correlation between NOK and stock markets (the Oslo Stock Exchange, S&P 500 or the MSCI, the global equity index. (At the chart to the right, we have detrended the stock market as equities are drifting upwards, while NOK (hopefully) is stationary. However, the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

Now, global surprises are on the downside, if not by much

… according to Citi's surprise index. The US, China, UK, and Norway well below







- The **US** surprise has fallen further below average, and fell further last week
- The **EMU** has fell to below the neutral line last week
- **China** July date were weaker than expected
- **Emerging Markets x China** are still reporting better data than expected, but less than some weeks ago
- **Norway** has surprised sharply on the downside recent weeks, has have UK

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

Time	Count.	Indicator	Period	Forecast	Prior
Monday Aug 30					
11:00	EC	Economic Confidence	Aug	118	119
14:00	GE	CPI YoY	Aug P	3.9%	3.8%
Tuesday Aug 31					
01:50	JN	Industrial Production MoM	Jul P	-2.5%	6.5%
03:00	CH	Services PMI, NBS	Aug	52.0	53.3
03:00	CH	Manufacturing PMI. NBS	Aug	50.1	50.4
08:00	NO	Credit Indicator YoY	Jul	(5.4)	5.3%
08:00	NO	Hotel guest nights	Jul		
09:55	GE	Unemployment Rate	Aug	5.6%	5.7%
11:00	**EC**	**CPI Core YoY**	**Aug P**	**1.5%**	**0.7%**
15:00	US	S&P CoreLogic CS 20-City MoM	Jun	1.9%	1.8%
16:00	**US**	**Conf. Board Consumer**	**Aug**	**123.4**	**129.1**
Wednesday Sept 1					
03:45	**CH**	**Caixin Manufacturing PMI**	**Aug**	**50.1**	**50.3**
08:00	**NO**	**Unemployment Rate LFS/AKU**	**Jun**	**(4.6)**	**5.0%**
08:00	NO	Household savings rate	2Q		94.3b
08:00	NO	Current Account Balance	2Q		94.3b
09:00	GE	Retail Sales MoM	Jul	-1.0%	4.2%
10:00	NO	Manufacturing PMI	Aug	(60)	63.3
10:00	EC	Manufacturing PMI	Aug F	61.5	61.5
11:00	EC	Unemployment Rate	Jul	7.6%	7.7%
14:15	US	ADP Employment Change	Aug	650k	330k
15:45	US	Manufacturing PMI, Markit	Aug F	61.2	61.2
16:00	US	Construction Spending MoM	Jul	0.2%	0.1%
16:00	**US**	**ISM Manufacturing**	**Aug**	**58.5**	**59.5**
	US	Auto sales	Aug	14.80m	14.75m
Thursday Sept 2					
08:00	**NO**	**Vacancies, % of emloyment**	**Jun**		**2.5%**
11:00	EC	PPI YoY	Jul	11.0%	10.2%
14:30	US	Initial Jobless Claims	Aug-28	346k	353k
14:30	US	Unit Labor Costs	2Q F	1.0%	1.0%
14:30	US	Trade Balance	Jul	-$74.0b	-$75.7b
Friday Sept 3					
03:45	CH	Services PMI	Aug	51.3	54.9
10:00	**NO**	**Unemployment Rate, NAV**	**Aug**	**3.0(2.9)**	**3.1%**
10:00	EC	Services PMI	Aug F	59.7	59.7
10:00	EC	Composite PMI	Aug F	59.5	59.5
11:00	EC	Retail Sales MoM	Jul	0.10%	1.5%
14:30	**US**	**Nonfarm Payrolls**	**Aug**	**750k**	**943k**
14:30	**US**	**Unemployment Rate**	**Aug**	**5.2%**	**5.4%**
14:30	US	Particiaption Rate	Aug		61.7%
14:30	US	Average Hourly Earnings YoY	Aug	3.9%	4.0%
16:00	**US**	**ISM Services**	**Aug**	**62.0**	**64.1**

SpareBank 1 MARKETS

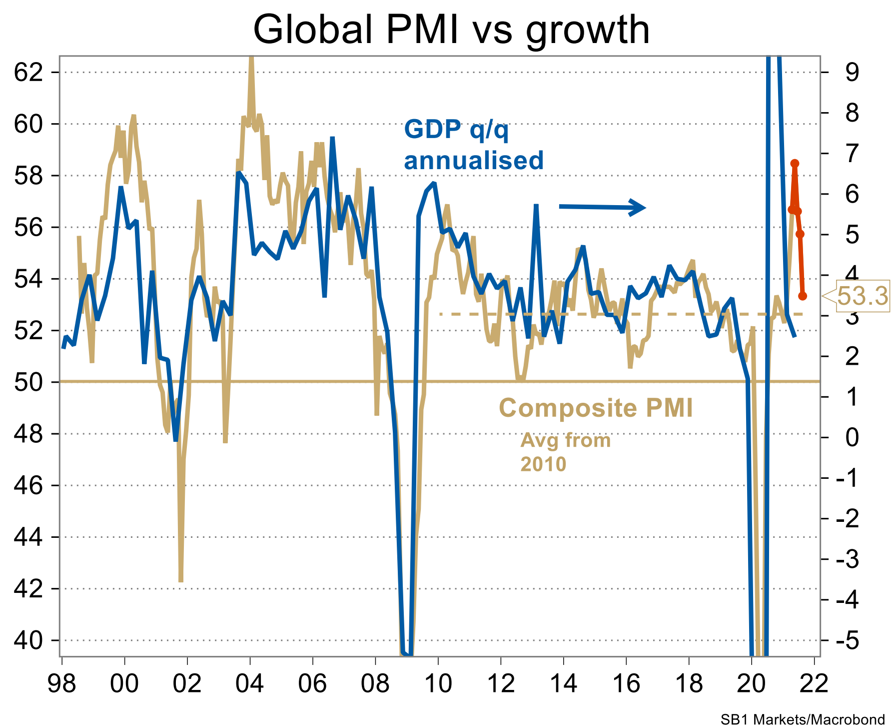
The Calendar: PMIs, ISMs, Auto sales, US & NOR Labour mkt, US consumer conf, EU retail

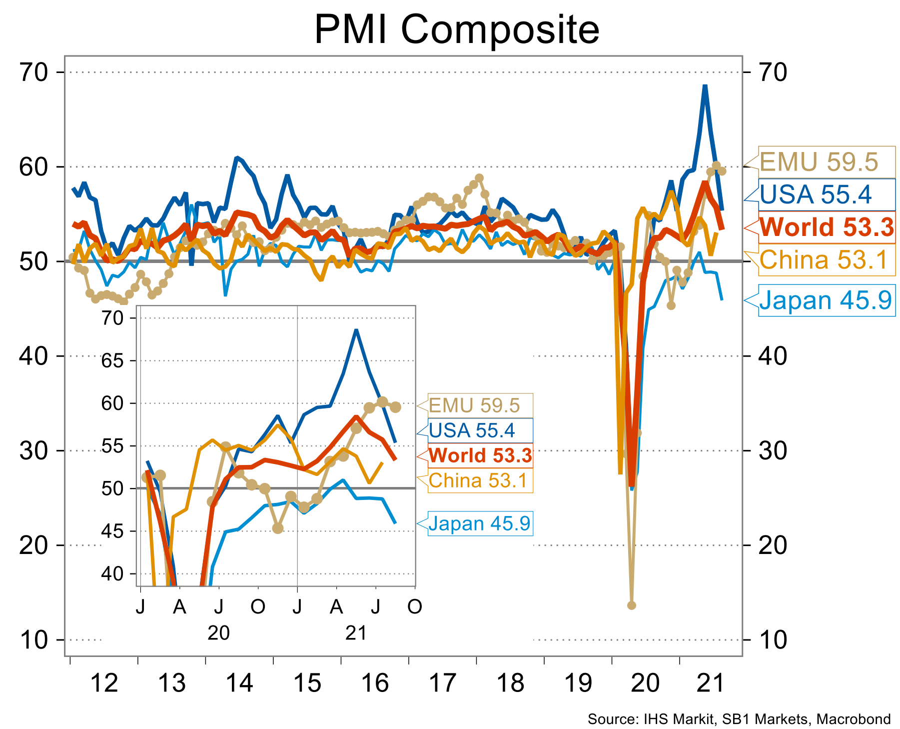
- **Final PMIs & ISMs**
  - » The preliminary PMIs pointed in the direction of a well above 2 p drop in the global PMI in August, due to steep decline in services in the US (+weaker UK, Japanese PMIs). EMU kept up pretty well. However, like in July, it is possible PMIs in Emerging Markets will keep up better (they rose, from much lower level though) than DM PMIs. If so, the decline in the global PMI will be milder than our model suggests. The Chinese PMIs have approached the 50 line, as growth is slowing. The US ISM service sector PMI should attend more focus than normal, given the weak services PMI
- **Auto sales**
  - » **Global auto sales** fell further in July, mostly due to supply constraints – that did most likely did not ease in August. Sales in Europe may be hampered by weak demand too. Chinese sales are sliding slowly down, while Indian sales recovered briskly in June & July, to the best level in years
- **USA**
  - » As the inflation target is met, 'a further progress towards the maximum employment target' is crucial for Fed's policy stance. Most likely, they will get sufficient confirmation from August **payrolls report** to signal a tapering of the QE program a the September FOMC meeting. Focus at the **supply** side as well (participation), **unemployment & wages** as well as these data have signalled limited spare capacity. **Survey data** (NFIB out this week) and unfilled vacancies stats will complement the assessment of the labour market
  - » The University of Michigan consumer sentiment survey 'collapsed' in August, from a low level – and we struggle to find good explanations. **Conference Boards confidence** survey was strong in July, and is expected almost unch. in August. There is a significant risk for a weaker print. And if not, we are inclined to believe in the CB survey, not the UM
- **EMU**
  - » **Annual inflation** will rise sharply in August, due to the 0.7% decline in core HICP in Aug last year as corona subsidies were introduced. The core is expected up to 1.5% from 0.7%, the headline to 2.7% from 2.2%. The German CPI is approaching 4%
- **Norway**
  - » **Both the LFS (AKU) and the NAV unemployment** reports are out this week. In July, the NAV unemployment was unch a 3.0% %, in line with NoBa's f'cast. We expect Aug unemployment to decline substantially to 2.7% (seas adj., 2.9% not adj), below NoBa's 2.9% s.a f'cast. LFS (AKU) unemployment rose in May (avg Apr-Jun), even if employment surged – because the participation rate rose even faster! In July, payrolls rose more than 1%, and we expect the LFS to confirm a rapid **employment** growth – and report a substantial decline in the unemployment rate. SSB will report end of Q2 **unfilled vacancies**

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

PMI further down in August – to an average level

We estimate a 2 p decline to approx. 53, to an average level – based on weaker DM data



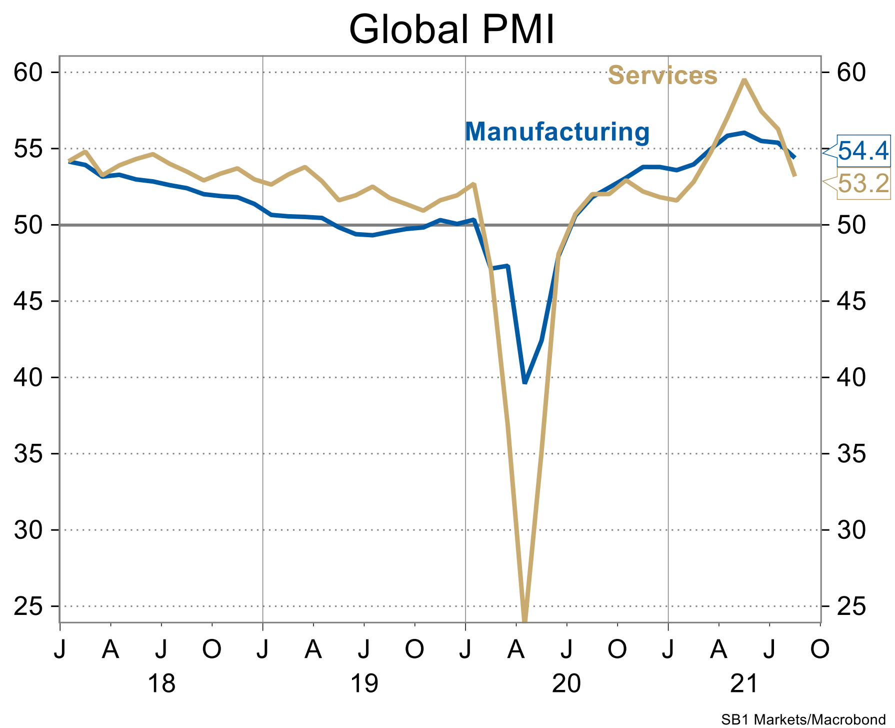


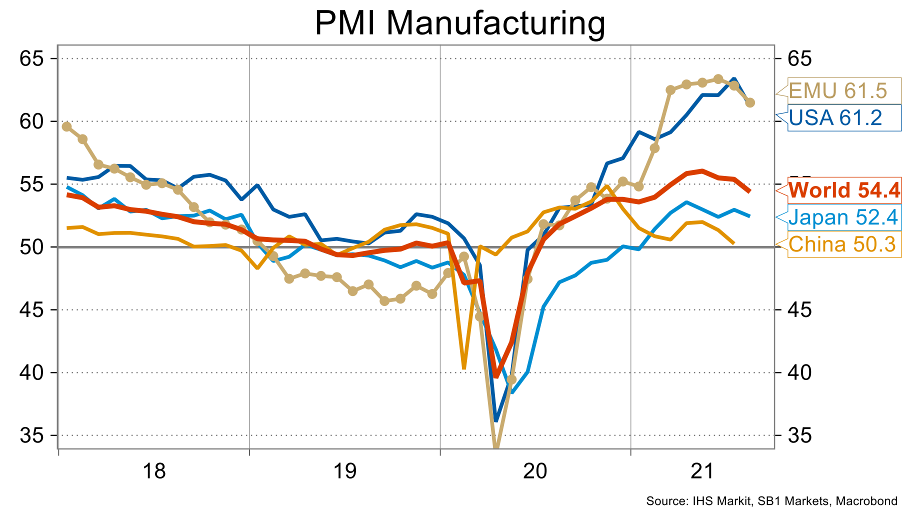
- **The global PMI** has peaked, so has very likely global growth. The August PMI signals 3% – 3.5% GDP growth
- **The US PMI** fell sharply, by 4.5 p to 55.4, far weaker than the expected -0.9 p, signalling 3% growth. The service sector PMI was the weak link in the chain
- **The EMU PMI** fell far less, by 0.7 p to 59.5, close to expectations – and the index signals 3% GDP growth. Services kept up well amid the Delta outbreak
- Both **Japan** and **UK** reported a decline in their PMIs in July, due to a sharp decline in services PMIs both places. Japan's PMI signals a GDP contraction
- **Delivery times rose even faster in the US, but slowed in Europe. Prices, input & output** prices are still increasing at a rapid pace but slower in August than in July
- In July, the **Developed Markets PMI** fell by 1.8%, while the **Emerging Markets PMI** rose by 1.2 p – but remained 5.5 p below the DM avg. It is possible the gap will be further closed in August – and that our estimate for the global PMI is on the weak side (like it turned out to be in July)

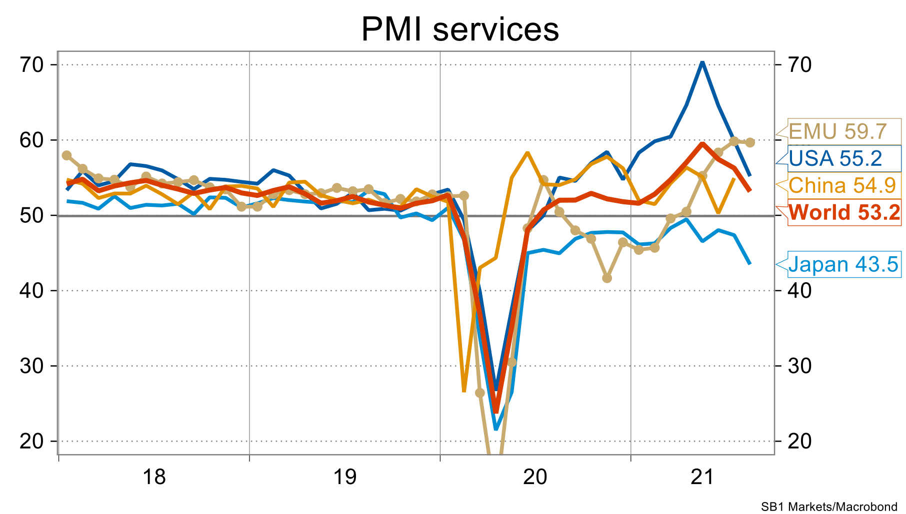
Our estimates are based on the preliminary PMIs from EMU, Japan UK, US. The estimates are uncertain, but usually by less than 0.5 p

Services weaker in August – but not in Europe

The manufacturing sector is still growing faster than trend



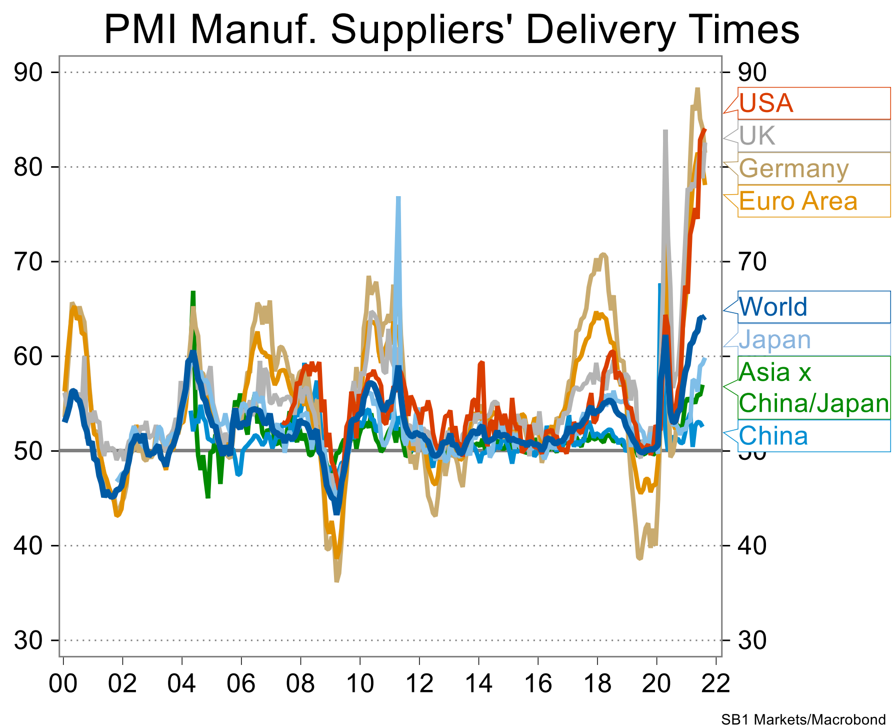


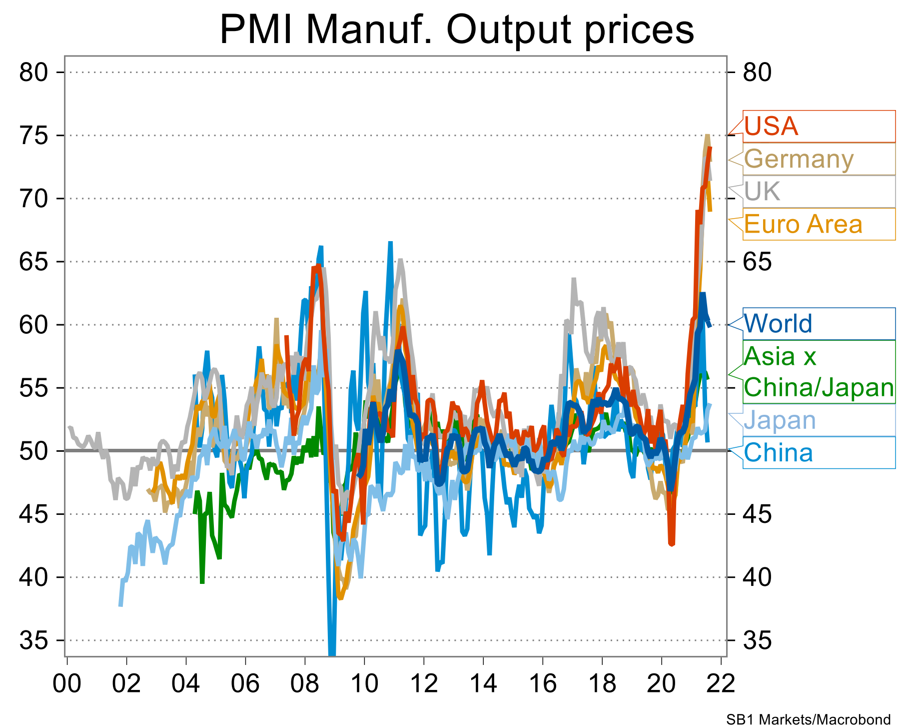


- We estimate a 1 p decline in the **manufacturing PMI** and a 3 setback in **services PMI**
- The slowdown in the manufacturing PMI was broad
- Services in the EMU kept up better than we feared, while US services continued rapidly downwards

Delivery times down in the Euro area, further up in the US

Prices are rising at a rapid pace but a tad slower in August than in July

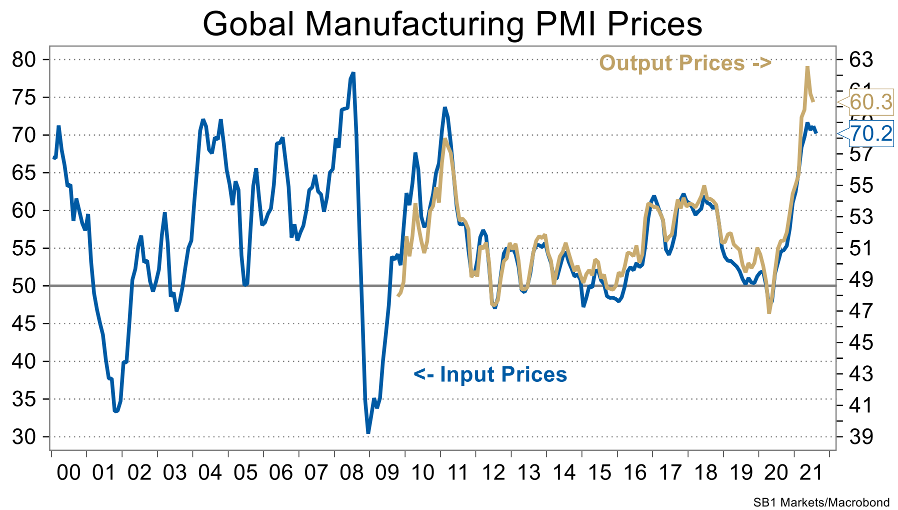


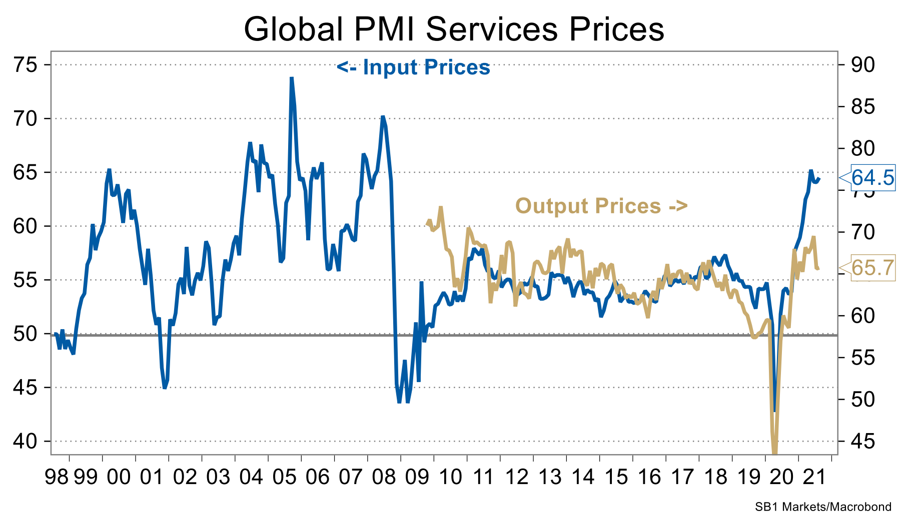


- **The global delivery times** PMI sub-index (changes in delivery times vs the previous month) have probably peaked – at a record high level. It does not imply delivery times are declining, at least not if companies give an honest answer when asked if delivery times are increasing or decreasing (but the delivery index is almost never been below 50)
- **The global manufacturing output price index** may have fallen marginally in August, following the decline in July. The level is still very high (just marginally down from ATH in June) – and companies are still reporting very rapid price increases

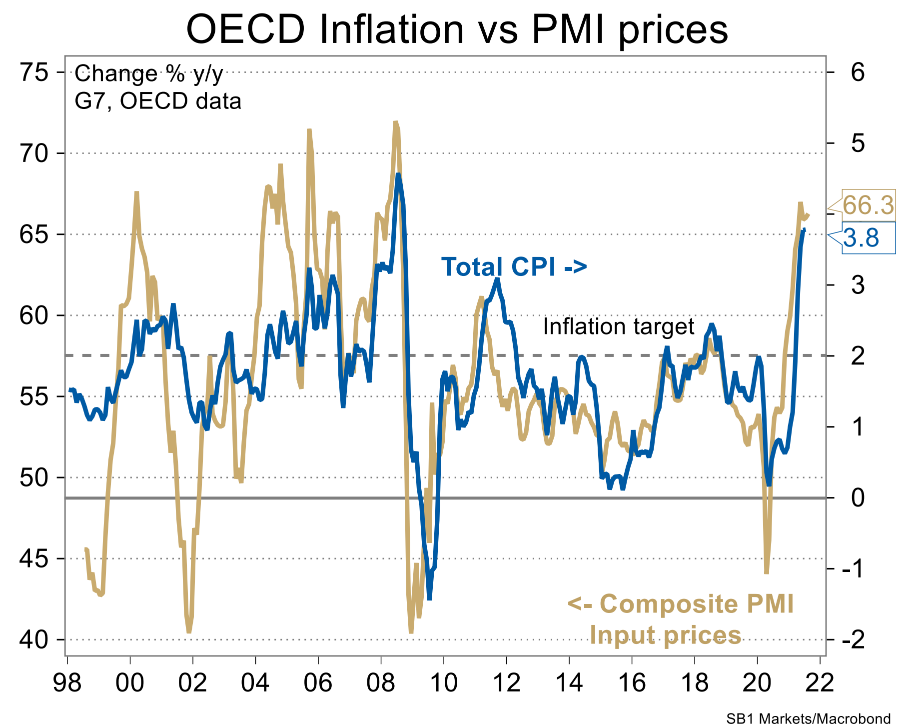
The global PMI price index has peaked – but remains at high level

Output prices are slowing somewhat





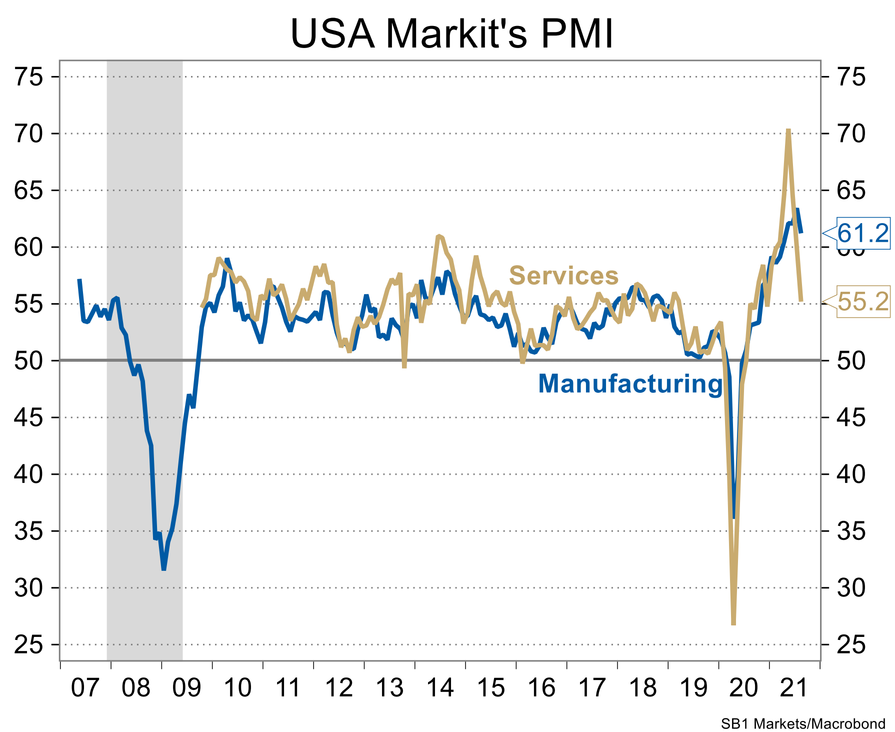
The last services PMI priced based on preliminary PMIs from EMU, Japan, UK, and the US

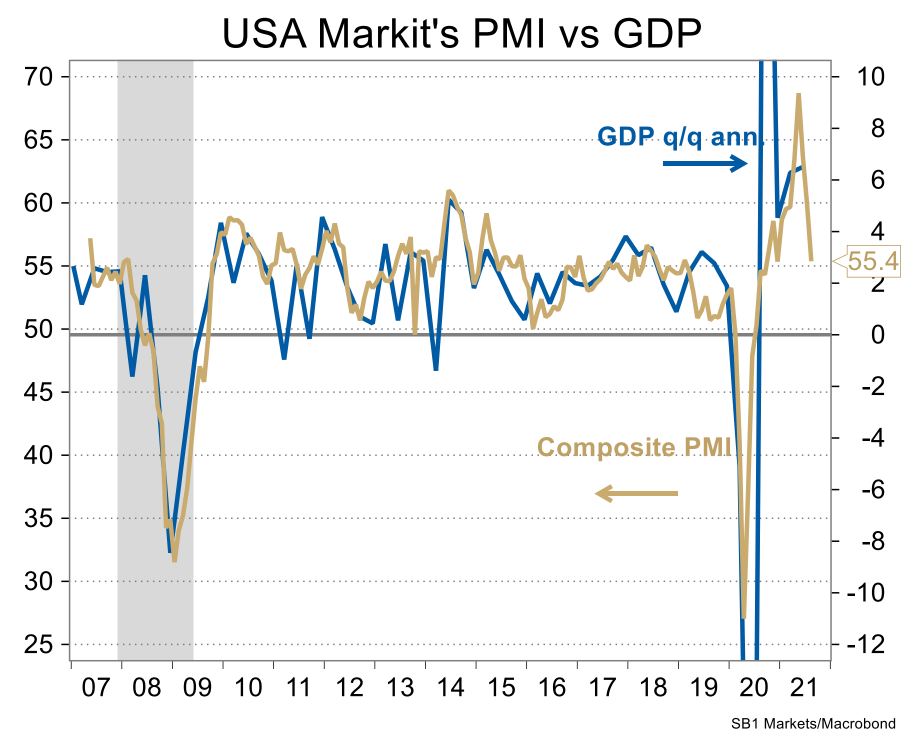


- Sure, companies world wide are reporting price increases far above normal level, and actual inflation prints will remain elevated for months (at least annual growth rates)

Services are slowing rapidly, the composite PMI signals 3% GDP growth

Delta outbreak likely explains part of the fall in the services PMI

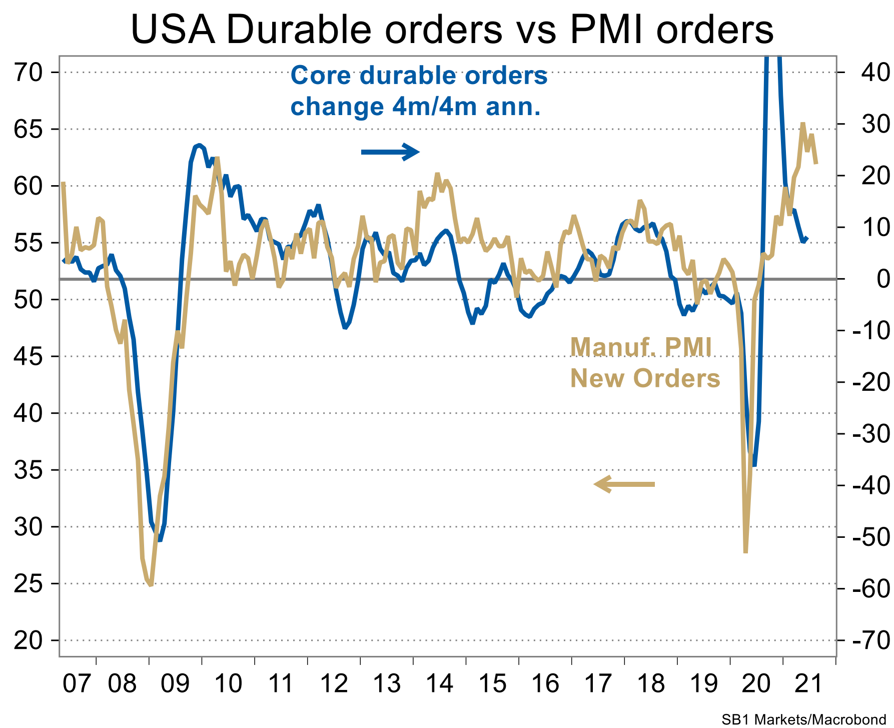


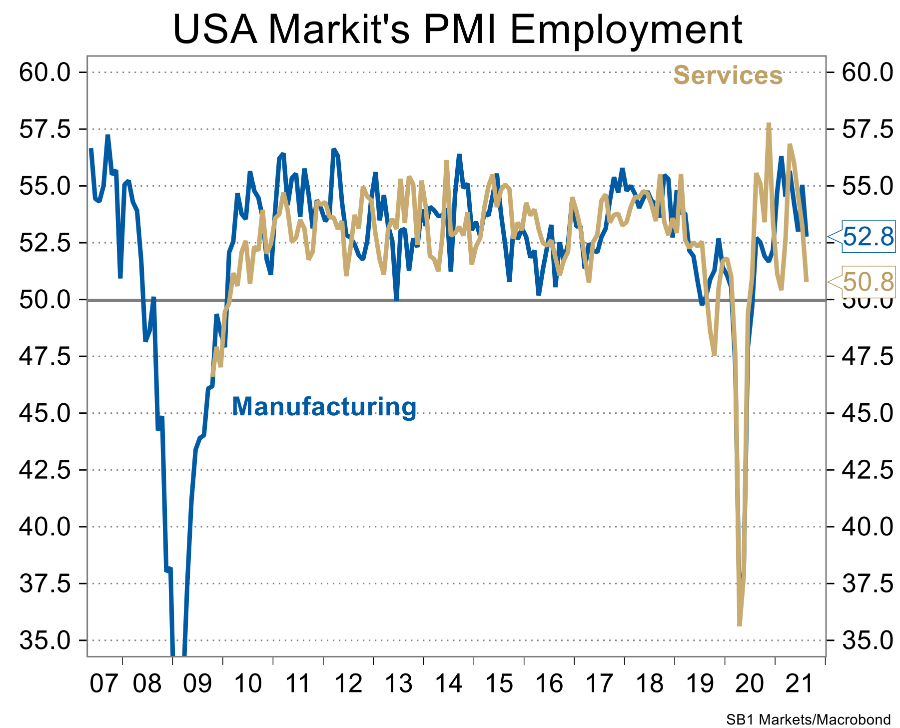


- The composite PMI fell 4.5 p to 55.5, far weaker than expected (-0.9p) – and now signals just 3% GDP growth, 2 pp less than signalled in July
- The services PMI fell by 4.7 p to 55.2. 3 months ago the index was above 70. The manufacturing index fell by 2.2 p to 61.2 – from ATH in July, and still a very high level
  - » Both were expected down just 0.9 p in August
- The Delta outbreak may explain the continued slowdown in services – but slower growth is reasonable when activity has recovered substantially. Lack of labour is also hampering growth
- Prices are still soaring – and just marginally slower faster than anytime since the composite index was introduced in 2009

Manufacturing orders still strong – but employment growth is slowing

Services are reporting just a marginal employment growth, we think mostly due to lack of labour

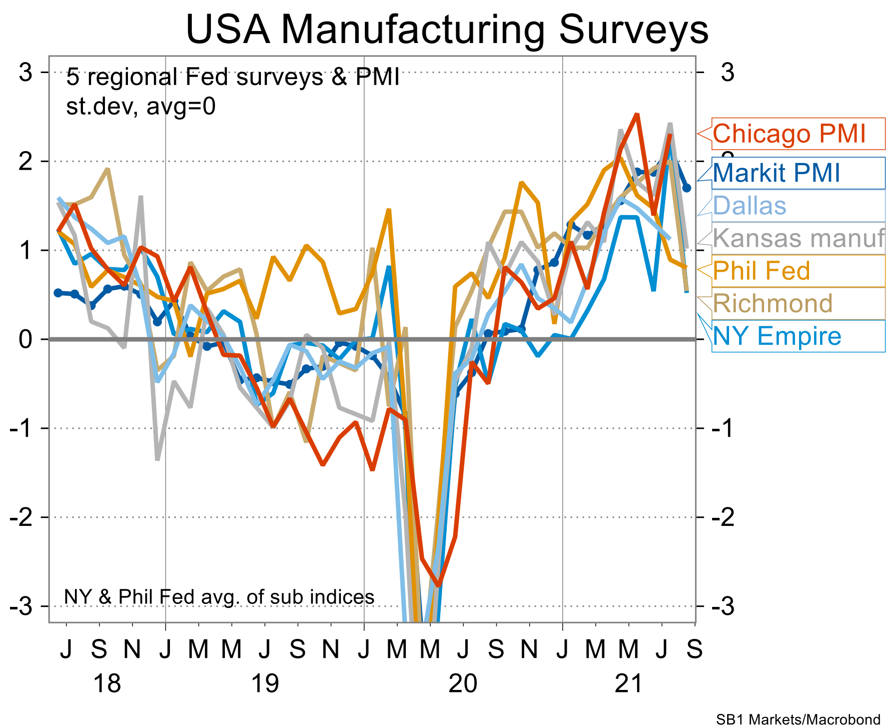


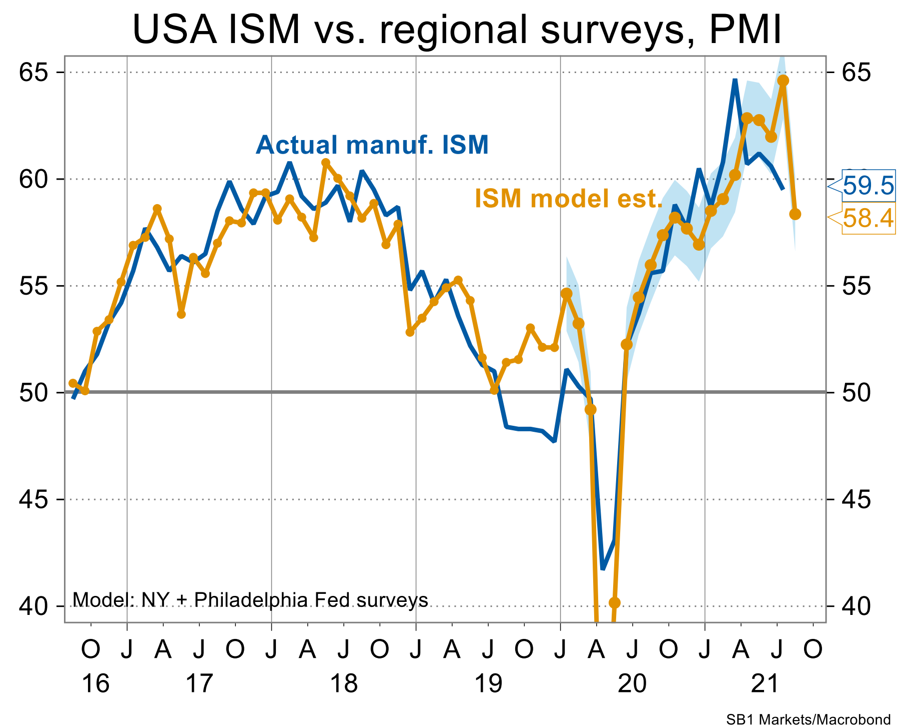


- The employment index, which measures actual change in employment from the previous month, may be 'moderate' both due to moderate demand and to supply constraints. Given comments from companies in this survey, other surveys, and the number of unfilled vacancies, supply constraints are no doubt the main culprit

Philadelphia Fed, NY Empire, Kansas, Richmond Fed surveys down, as is the PMI

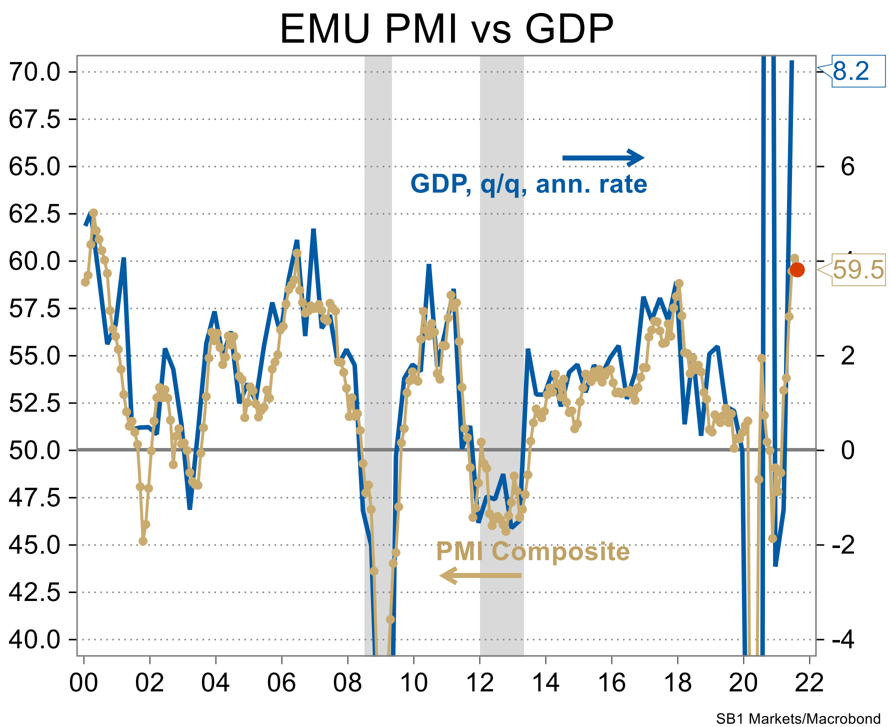
… and these surveys signal a substantial decline in the ISM in August

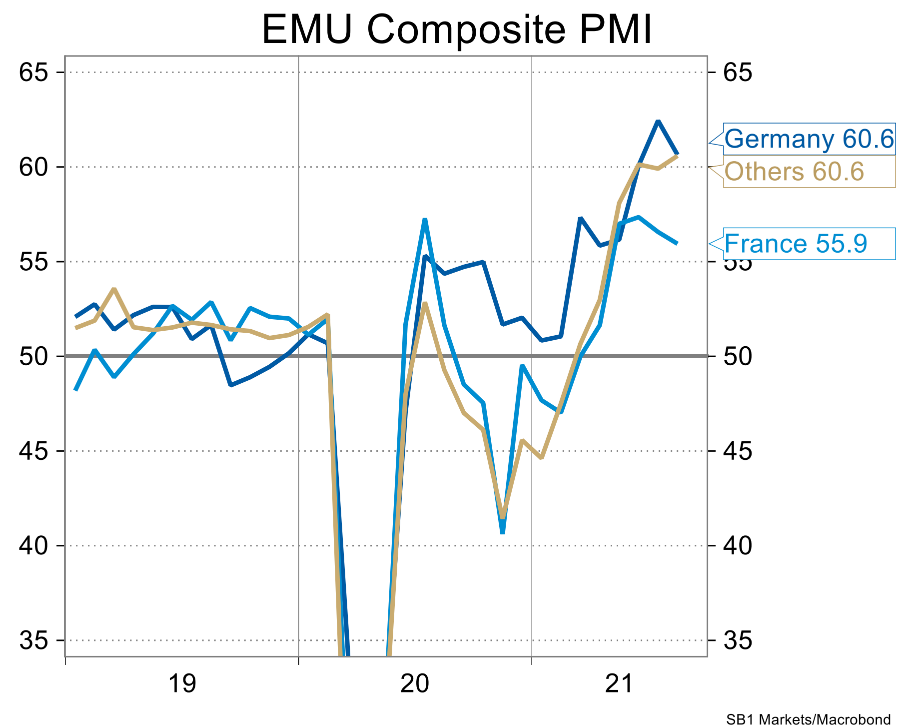




EMU PMI marginally lower due to supply chain constraints

PMI still at some of the highest levels since 2006

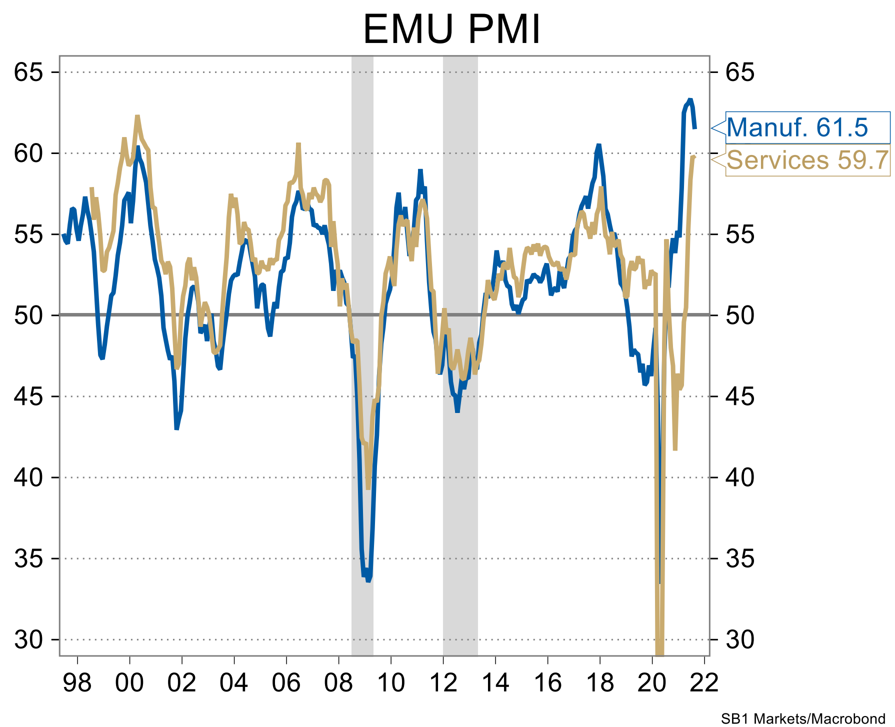


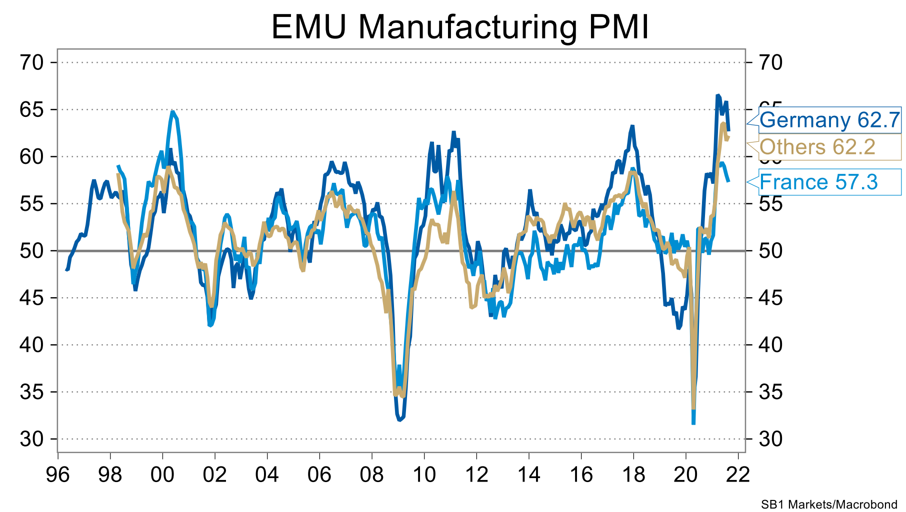


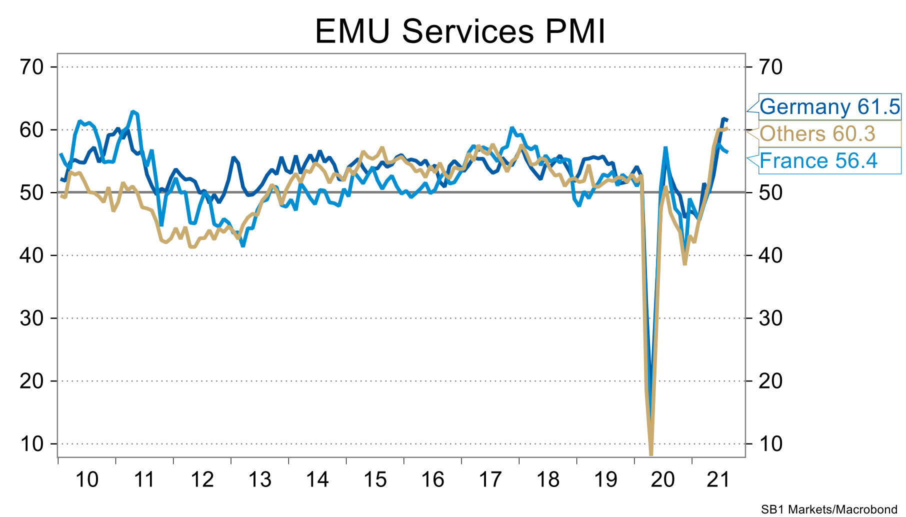
- **The composite PMI** fell 0.7 p to 59.5 (expected 59.6), which signals a 4% pace of growth in GDP (or 0.9 % per quarter)
  - » The composite index fell in Germany and France. The average of Spain & Italy (and very likely both countries) accelerated – and reported the highest composite PMI ever… yet again!
  - » The service sector fell marginally amid the surge of the Delta variant, while the manufacturing PMI fell somewhat more – but is still at a very high level at 61.5

August PMIs down, but the Delta variant has not derailed the recovery

Services are still reporting strong growth all over Europe. The manufacturing sector is even stronger



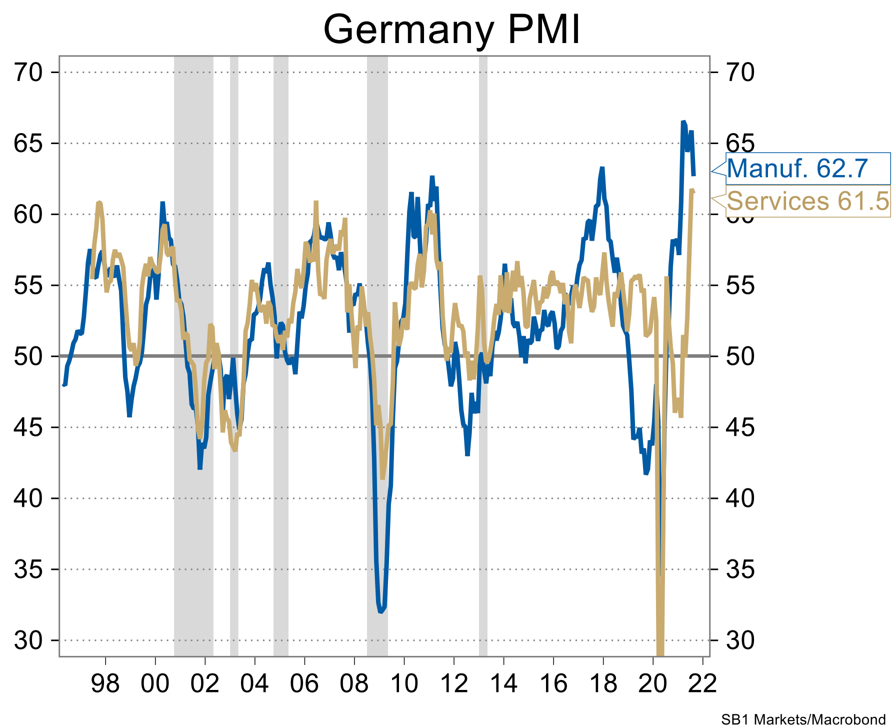


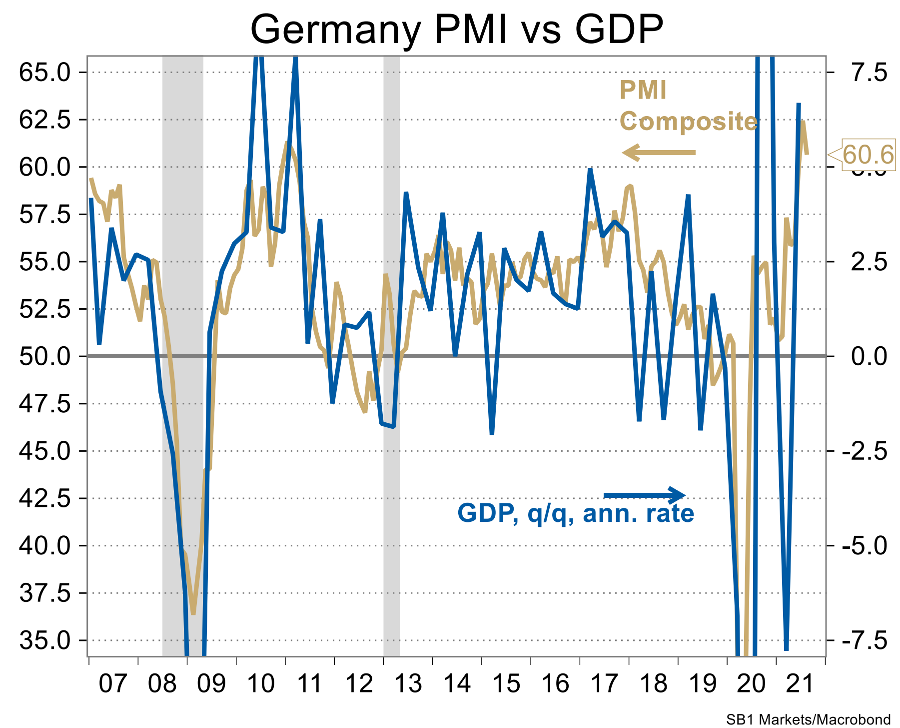


- **Services PMI** was down 0.1 p to 59.7, expected flat at 59.8. All countries are far above the 50 line
- The **manufacturing PMI** declined 1.3 p to 61.5

Germany: Manufacturing PMI surprised sharply on the downside

The composite PMI was down 1.8 p to 60.6, expected 62.2

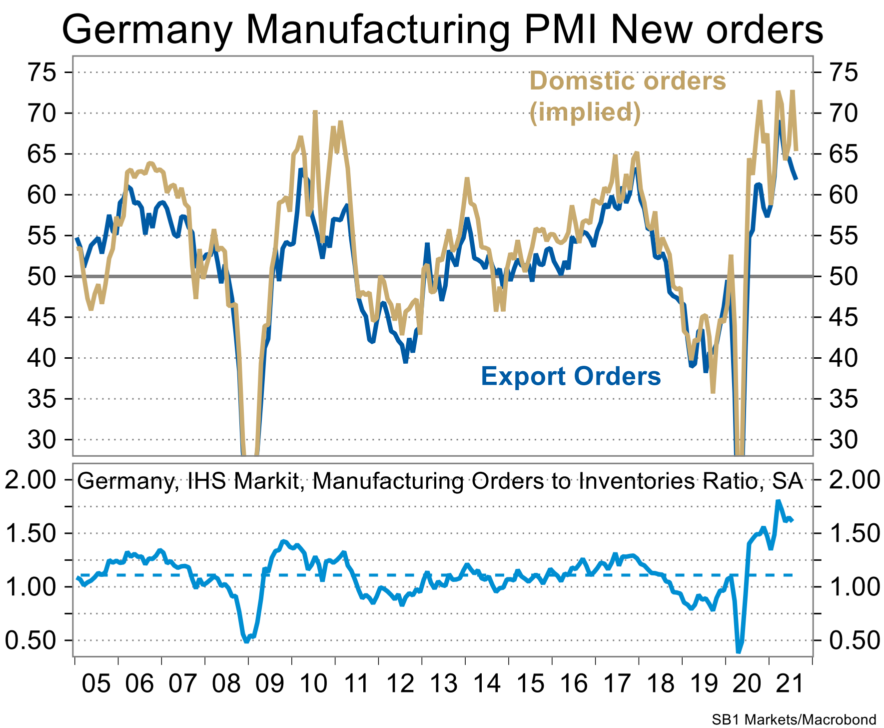


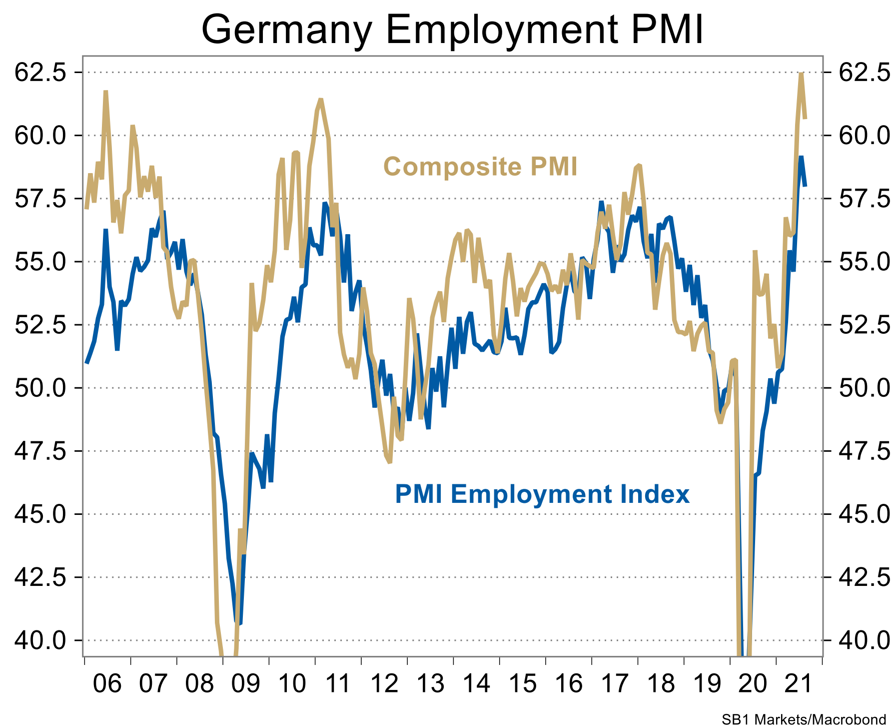


- **The prelim. manufacturing PMI** decreased by 3.2 p to 62.7, expected down 0.9 p to 65. Here too, supply constraints are restricting growth. BUT keep in mind, this is still a very strong print
- **The service sector PMI** was down 0.3 p to 61.5, but above expectations at 61
- **The composite PMI** still signals 5%+ GDP growth, far above the German trend, of course

Germany: Orders and Employment indices down, but no reason to panic…

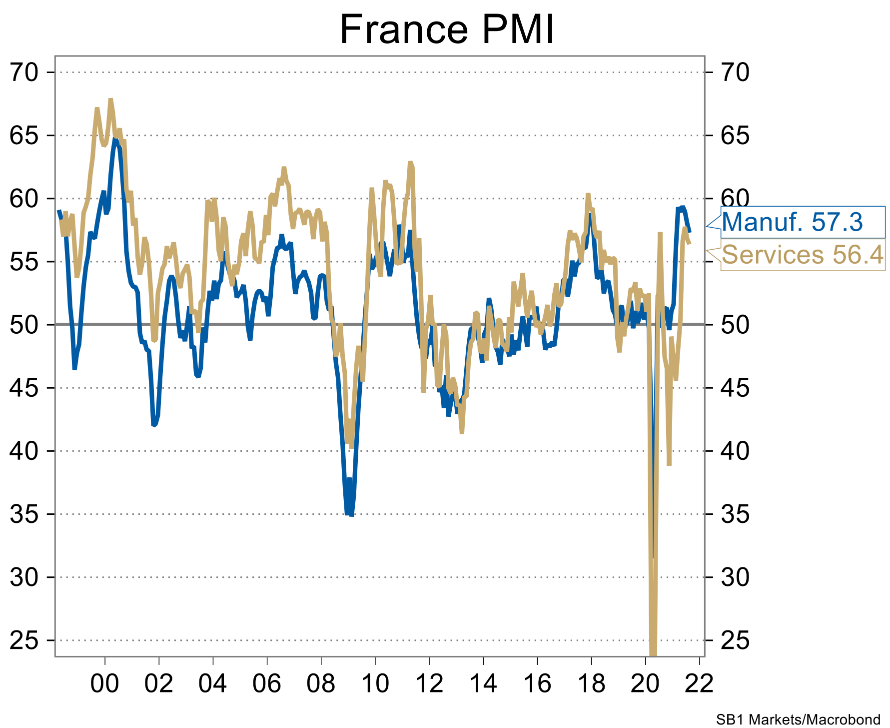
… levels are still some of the highest on record

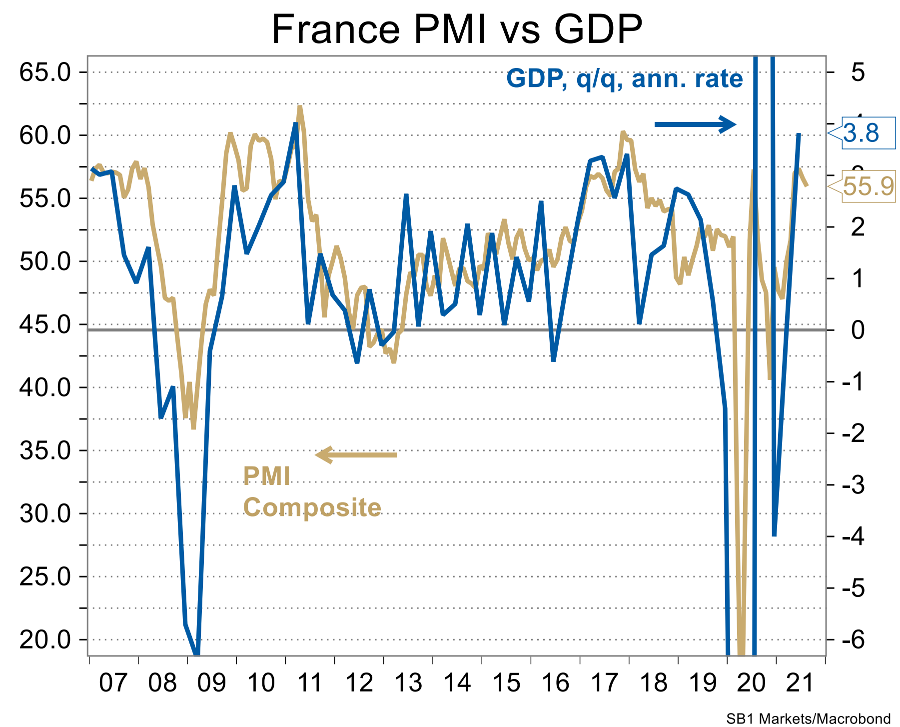




France: The PMIs slightly down in August – currently signalling 2.5% growth

… which is not that impressive. The composite index fell 0.9 p to 55.9, expected down to 56.5

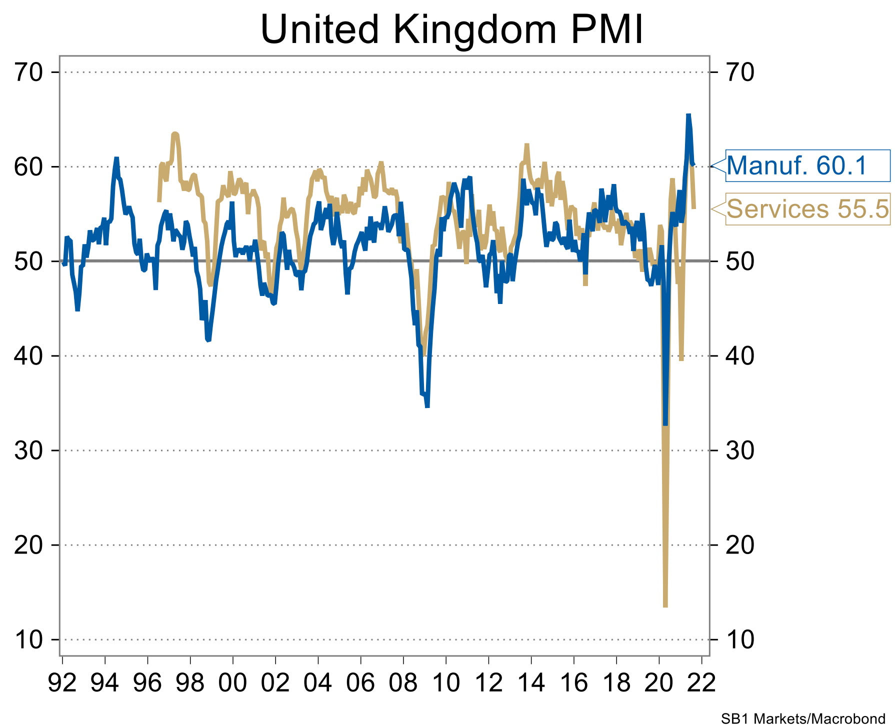


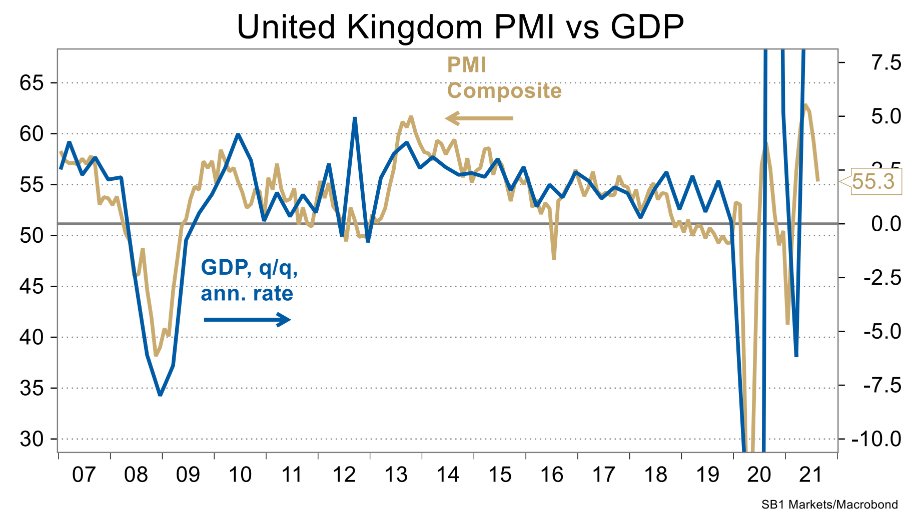


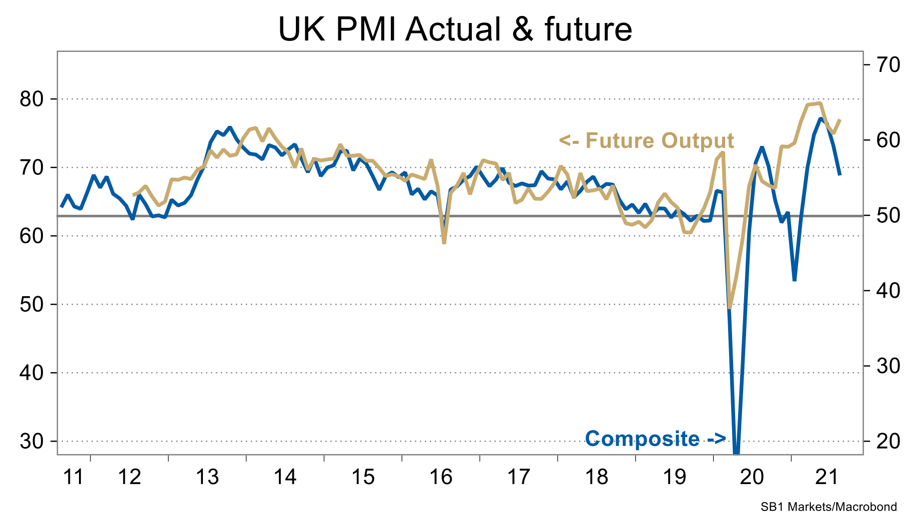
- The **services** PMI fell 0.4 p to 56.9, while the **manufacturing** PMI fell 0.7 p to 57.3

UK PMIs: Supply constraints and the Delta variant curbs momentum

Both the services and the manufacturing PMI were down in August – levels still signal expansion

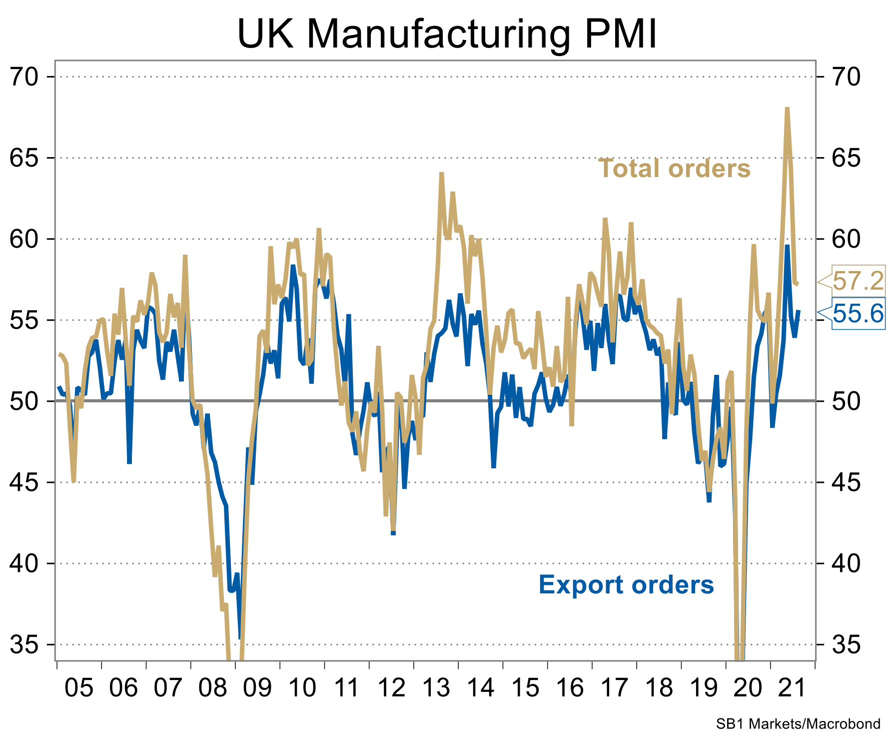


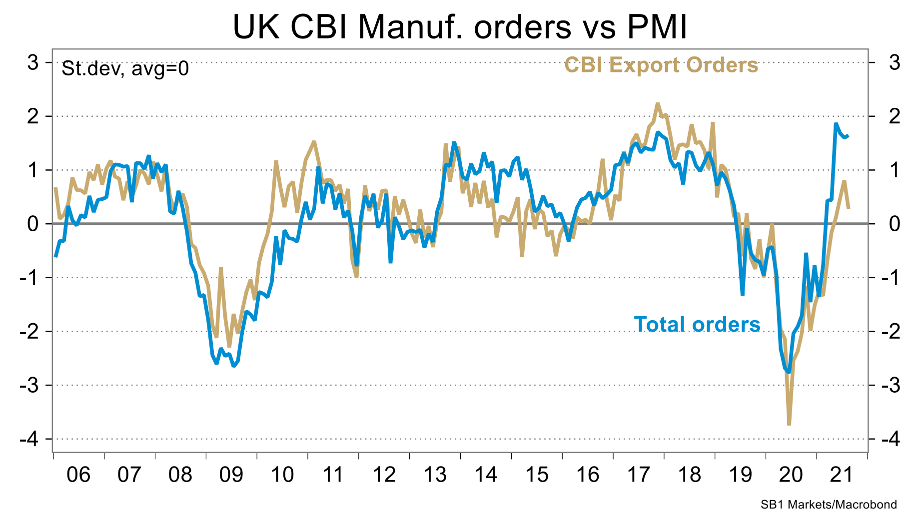


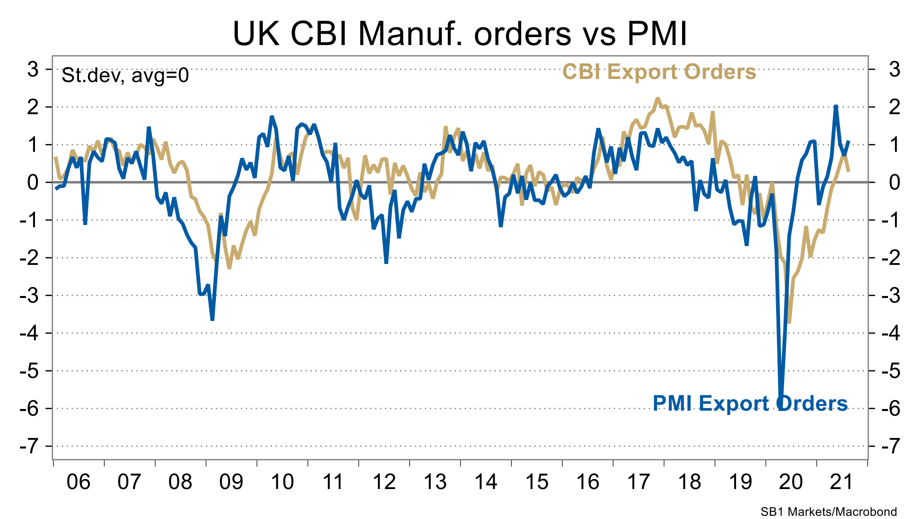


- **The composite PMI** fell 3.9 p to a 6-month low at 55.3. Firms cited supply issues (materials and labour) as reasons for dip, and most likely, the spread of the Delta variant has dampened growth somewhat – but growth is still well above trend
- **The total manuf. PMI** was down 0.3 p to 60.1
- **Services PMI** decreased by 4.1 p to 51.6
- **Employment growth** was the strongest in 25 years, according to Markit

Still rapid growth in orders, but not like in May. No specific export problems

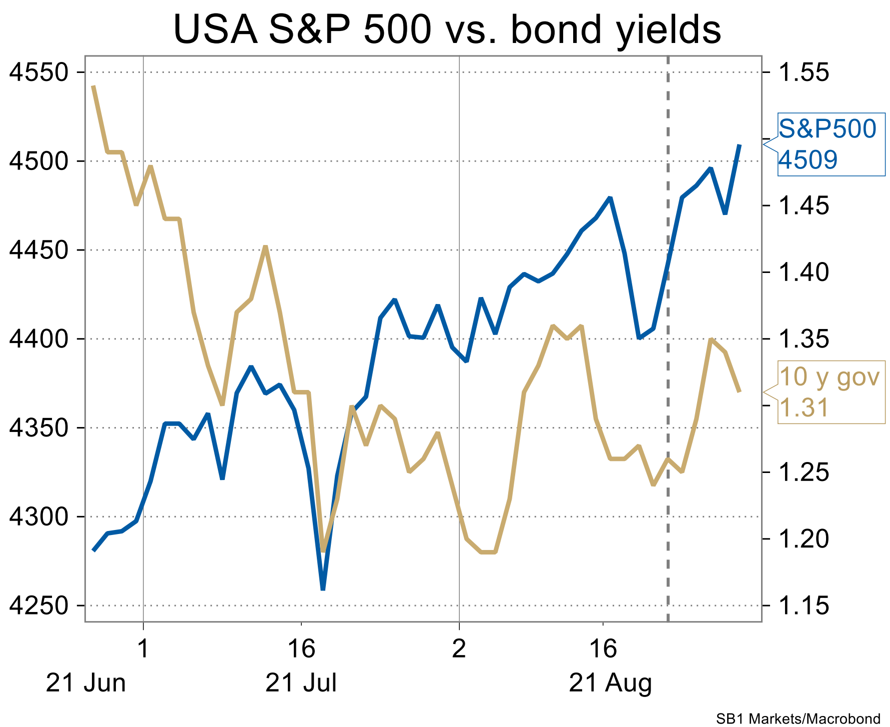






Fed will probably start tapering in Q4, but Powell argues rates will be kept at zero

Progress towards targets is sufficient for tapering but targets must be reached before a rate lift-off

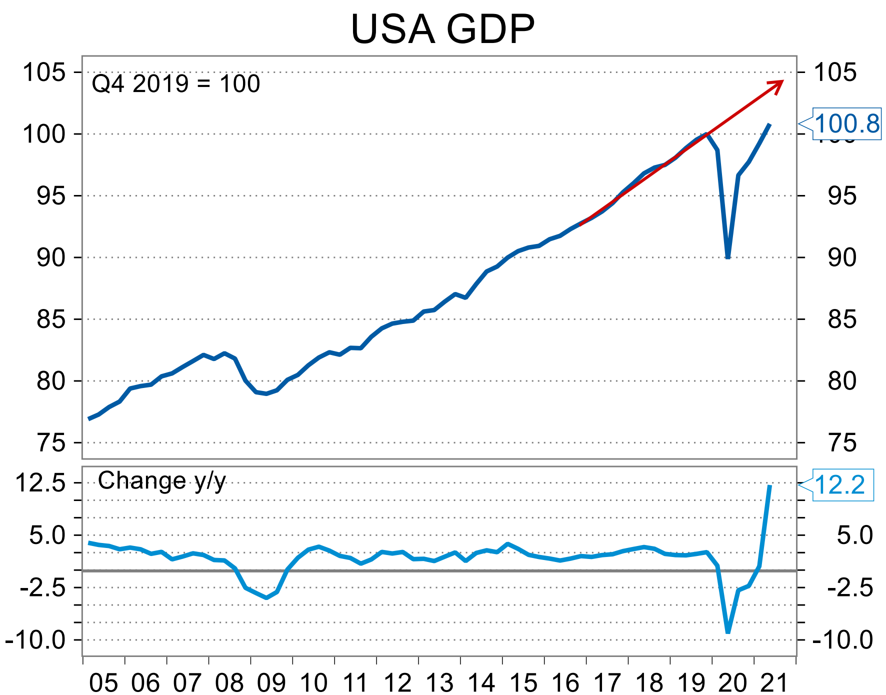


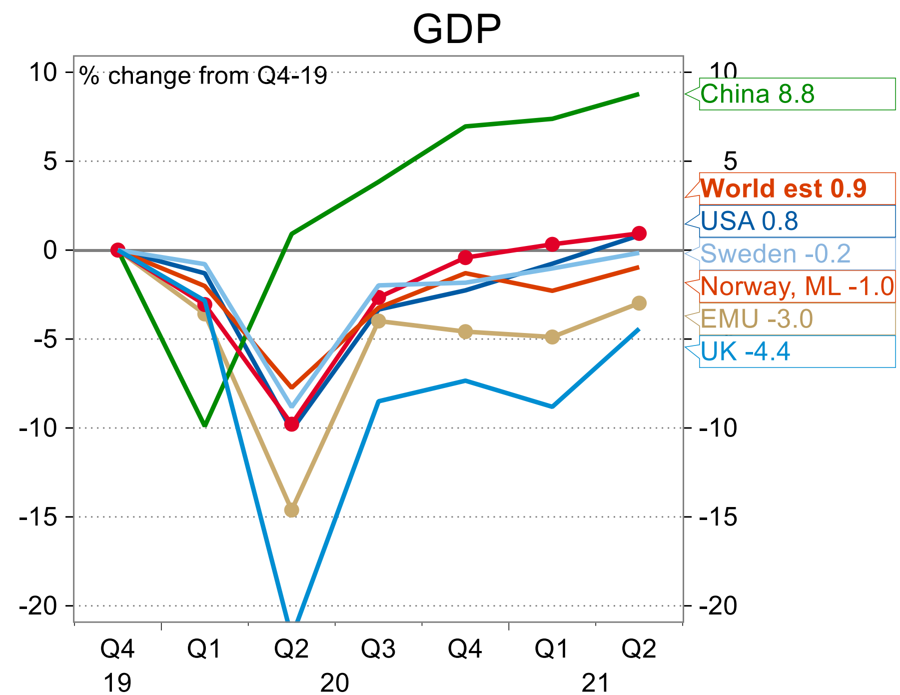
- **Markets** had discounted a late 2021 tapering start, and was not chocked by Powell's 'confession'
- Rather, markets responded favourably to his comments on when to hike rates, and that he still assumes today's high inflation will turn out to be transitory
- **Interest rates/bond yields fell** (real rates down, infl. expectations rose, a reasonable response), and another ATH was reached at the **stock market – cheap money forever**

- At the **Jackson Hole (digital) conference Powell** revealed that he – at the late July FOMC meeting – argued for starting tapering the QE program in late 2020 – if the labour market made further progress towards the target. The inflation criteria was met, and as the labour market had strengthened, substantial progress towards the maximum employment target has been achieved, and further progress was expected. Did we really hear him indicate that at the press conference following the meeting??
  - » Data since late July had confirmed his view, according to Powell, even if the Delta variant created increased uncertainty
  - » However, minutes from the meeting revealed that many FOMC members assumed that the Fed should start reducing the USD 120 bn/month QE program later in 2021, and several FOMC members have been very outspoken recently, in favour cutting back the QE program as there were no lack of demand in the US economy but rather lack of supply
- Once more, Powell stressed that start of tapering did not imply the policy rate would be lifted anytime soon. For tapering, progress towards targets were sufficient. For a rate take-off: Targets has to be reached
  - » The economy has reached conditions consistent with maximum employment (which is still not defined), and
  - » And Inflation has reached 2% on its track to moderately exceed 2% for some time (even if this argument was introduced when inflation had been too low, and the average inflation rate had to be brought up to 2%. Now it is, and more than that)
  - » He added: We have much ground to cover to reach maximum employment and time to tell whether we have reached 2% on a sustainable basis
- In his speech, he stressed than several factors could dampen inflation, as soon has the impact from the pandemic faded
  - » He did not see broad based inflation pressures
  - » Moderating inflation in higher-inflation items, like 2nd hand cars, which have flattened (and durable goods prices have been falling for 25 years)
  - » He saw little evidence that wage increases that might threaten excessive inflation
  - » Longer term inflation expectation were not elevated
  - » Global disinflationary forces had ruled for 25 years (technology, globalisation, perhaps even demography) and central banks' commitment vs low inflation had stabilised expectations

Q2 GDP revised up by 0.1 pp to 6.6%, expected 6.7%

Services are recovering but still well below par

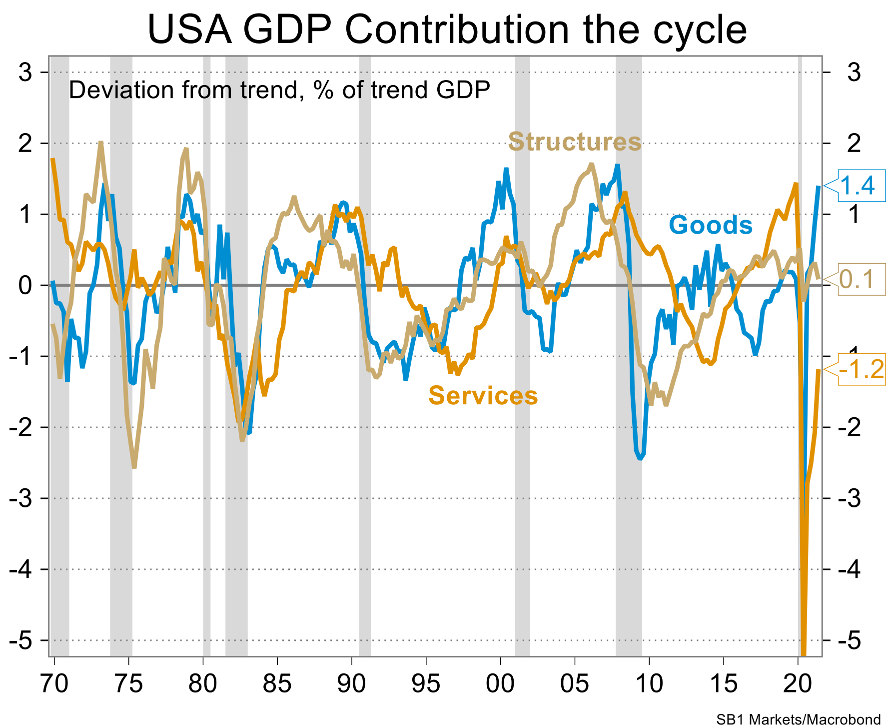


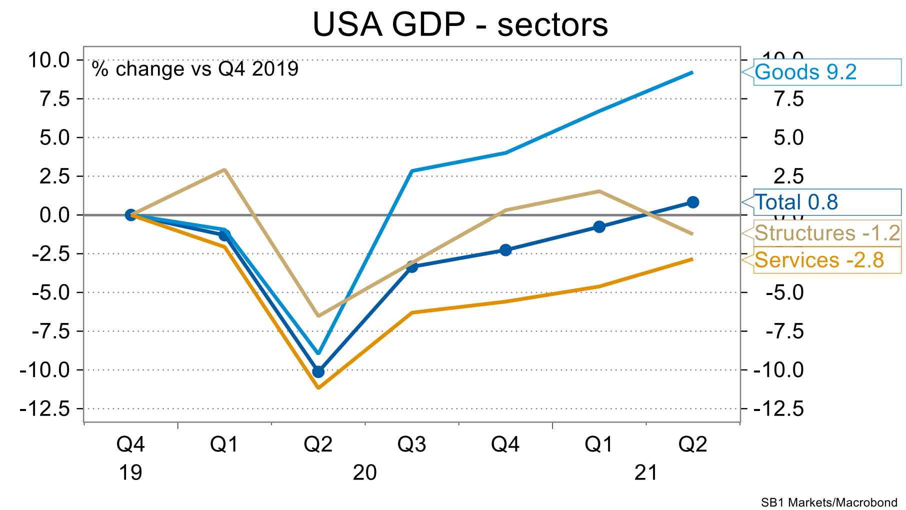


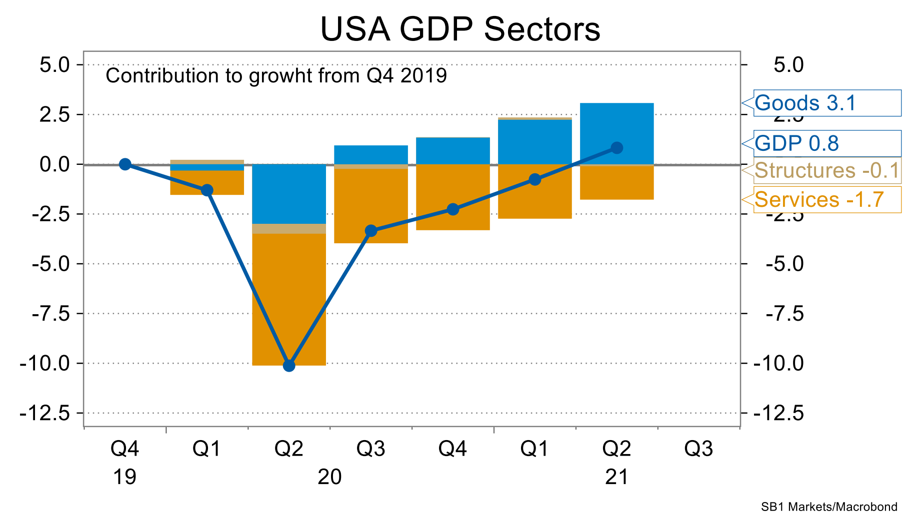
- **GDP** grew by 6.6% annualised in Q2 (1.6% not annualised), as in Q1 (6.4%) but below expectations at 6.7%. The GDP level is 0.8% above the Q4-19 level – but still some 2.7% below the pre-pandemic (2.4%) growth trend
  - » In order to reach FOMC's Q4 estimate, GDP must grow by a 7.2% pace in H2, which does not seem reasonable
- **No important revisions**, business investments a tad stronger, as were imports
- **US is now well ahead** of European countries. The extreme US fiscal policy measures taken in both 2020 and in Q1-21 explains most of the difference in performance vs the Eurozone

Services are recovering but are still a substantial drag on activity

A solid recovery in Q2, up 2% from Q1 – but goods are still going (extremely) strong



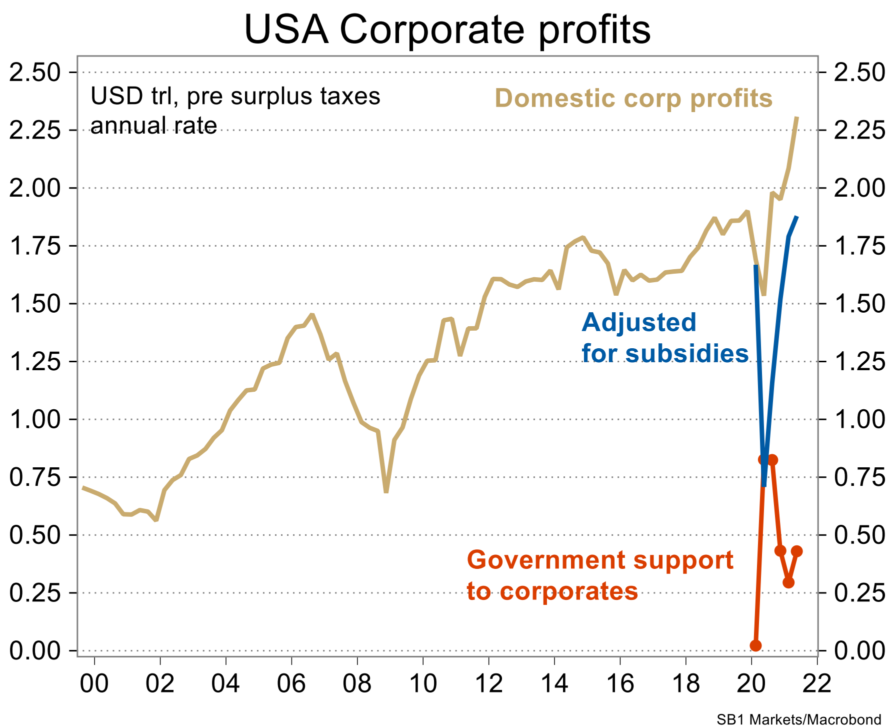


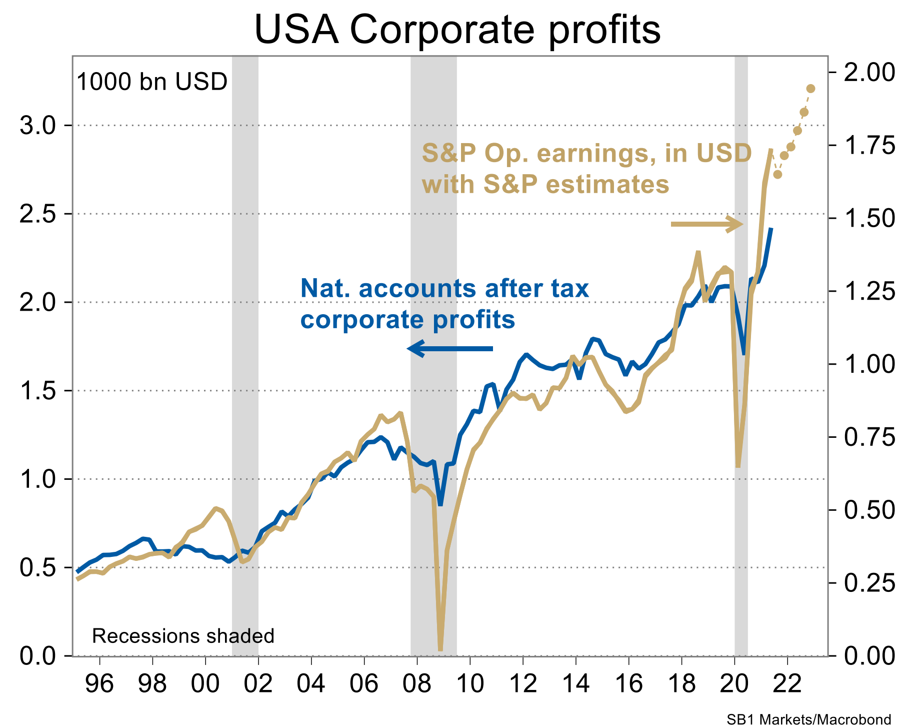


- Normally goods and structures are the main culprit during recessions, at these sectors are the most volatile elements in the economy. In addition, services are normally lagging. During the Covid-19 crisis, the service sector was the main swing factor – and it has far from recovered

Corporate profits surged in Q2, both for 'real' and due to more government subs.

Domestic corporate profits up 11% q/q. Government subsidies still lift profits by 23%!



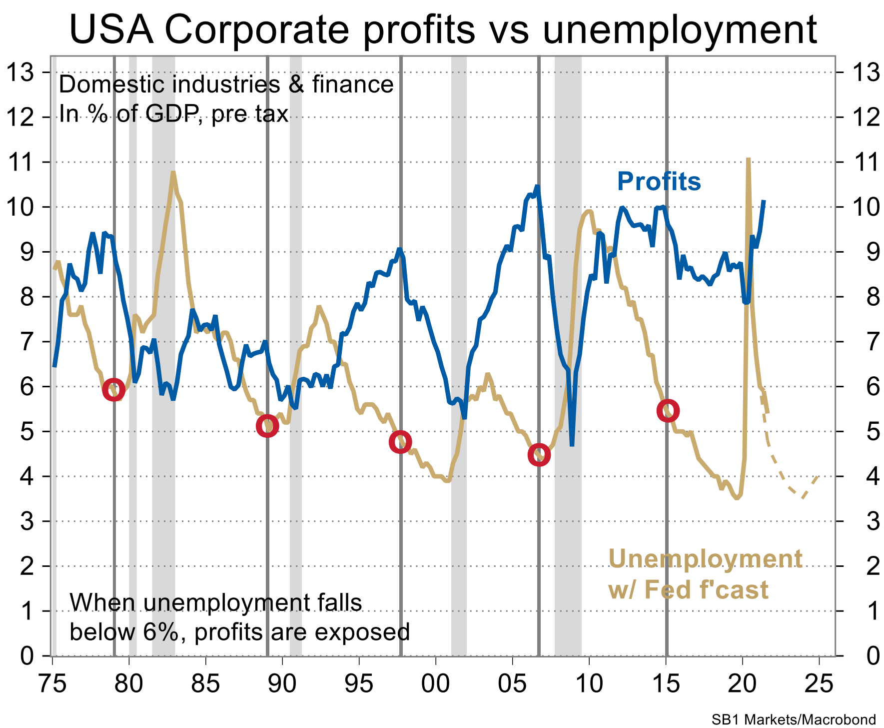


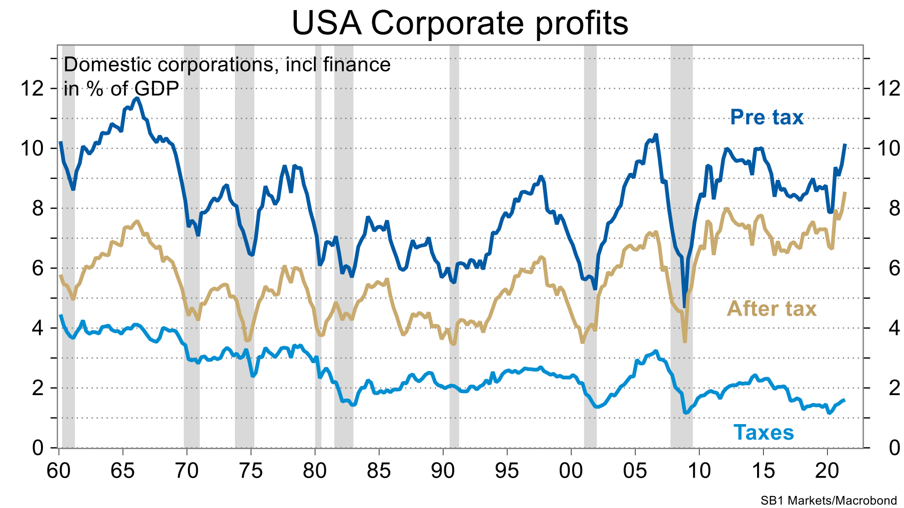
- **Government pandemic programs** have lifted **domestic corporate profits** at an unbelievable scale – and still support profits by 23% of normal profits. In Q2, the public support rose somewhat vs. the Q1 level, we expected a further reduction
  - » It is possible that some of the new programs that have been decided upon – and may be decided (the infrastructure program) have some elements of subsidies included, so that subsidies will remain at higher level than before
  - » Wages rose less than value added in Q2 (2% vs. approx. 2.3%), and thus far less than profits (+11%)
- We very much doubt profits will climb as fast at S&P's forecast on the chart to the right
  - » We expect subsidies to decline, wage inflation will pick up, or top line growth (GDP) will slow

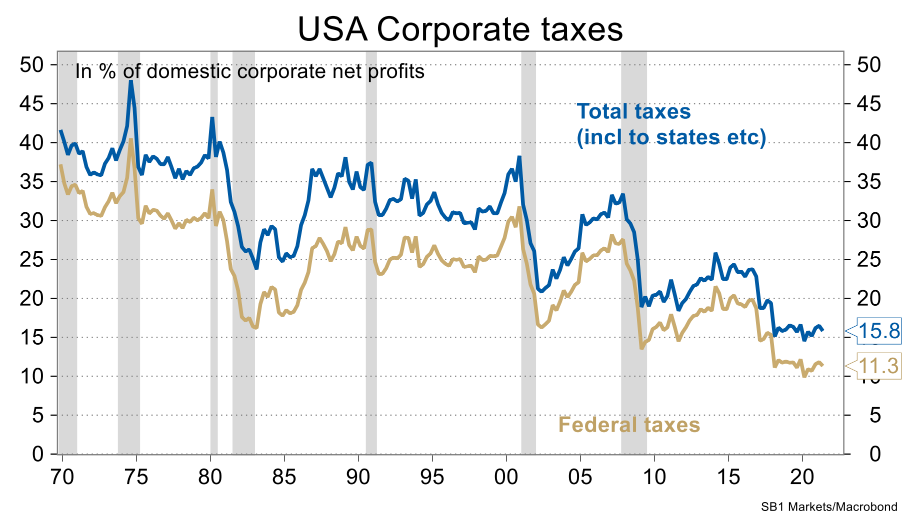
SpareBank 1 MARKETS

Profits were under pressure prior to corona – as usual when unemployment falls

… and for how long will unemployment remain high enough to ‘protect’ profits now?



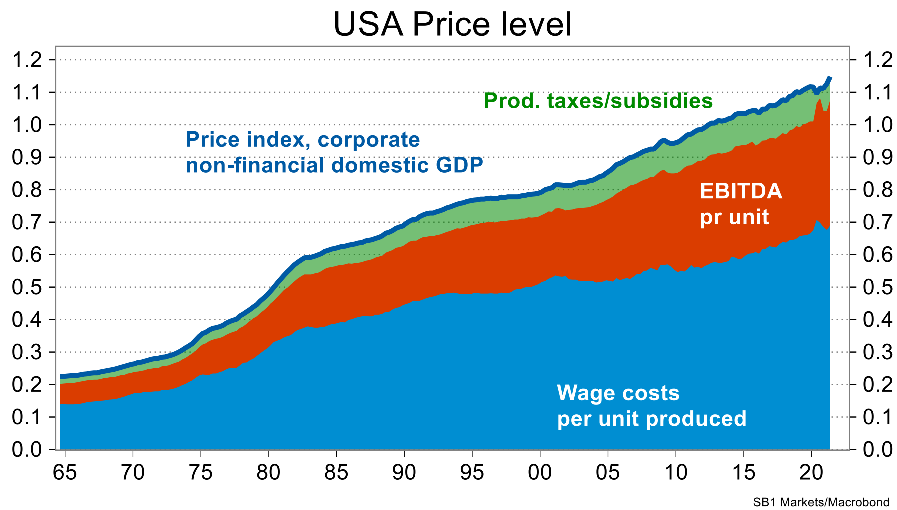


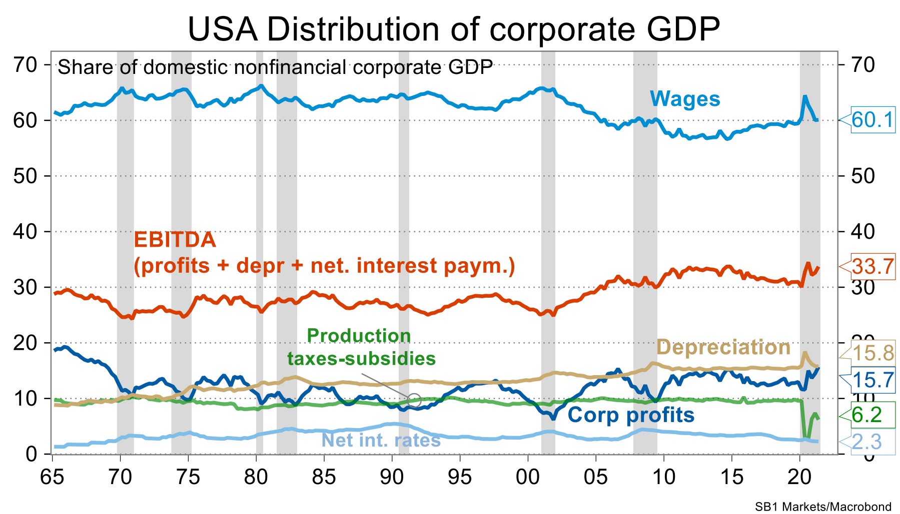


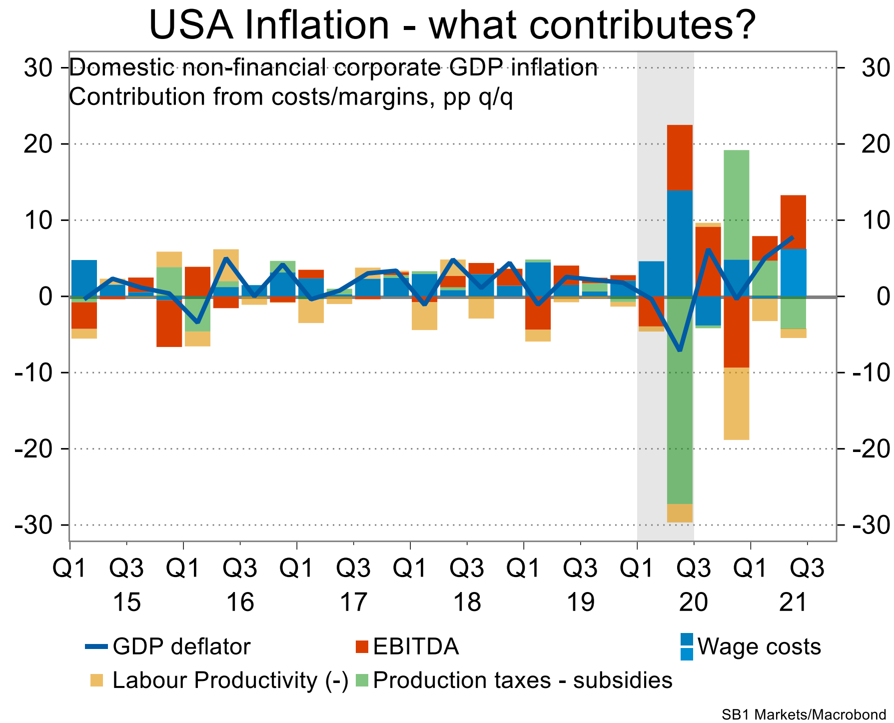
- When **unemployment falls below 6%,** corporate profits are exposed; at one stage the profit share will start to decline because wage earners will get the upper hand vs. employers. At least it has always happened in the past
  - » Before the corona crisis, the pre-tax profit share had fallen since the 2015 peak, because unemployment was ‘too low’ (however, profits have been revised up vs. previous estimates, the decline is less pronounced). After tax profits are record high vs GDP
- Taxes were cut substantially in 2018, equalling some 8% of corporate profits. Some of these cuts will probably be reversed in order to fund the infrastructure plan and the ‘welfare’ budget which now both are debated in the House

Why are prices on the way up?

In Q1, Q2: Higher margins, higher wages costs



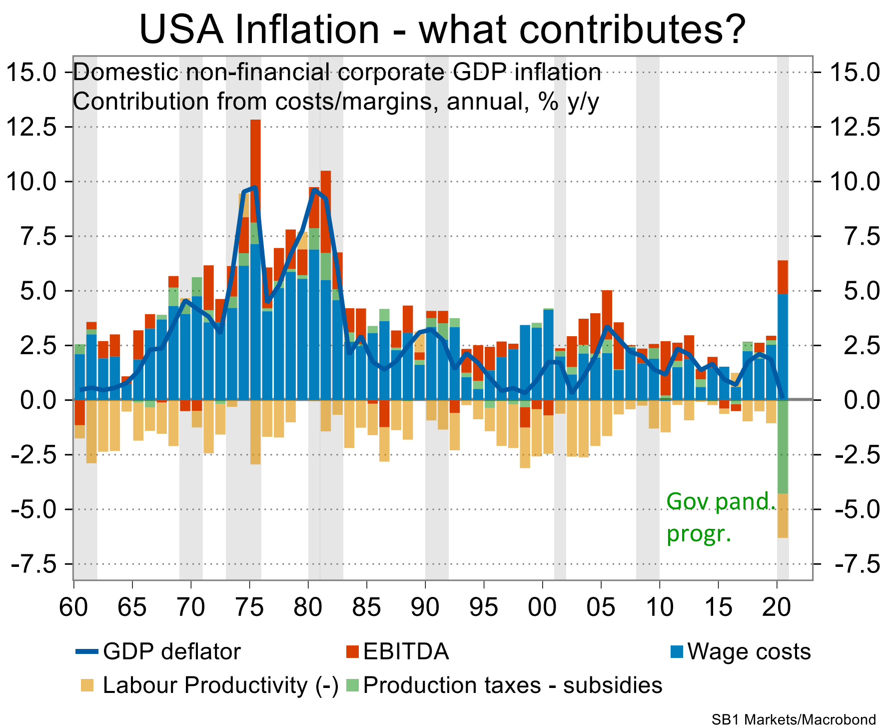




- Changes in subsidies recent quarters creates huge ups and downs in costs
- These subsidies will probably normalise the coming quarters – creating a pressure on prices and/or margins and wages
- Wage costs have been moving upwards

Higher inflation, how worried should we be?

Raw materials, higher margins are not the main challenge. Wages may become so

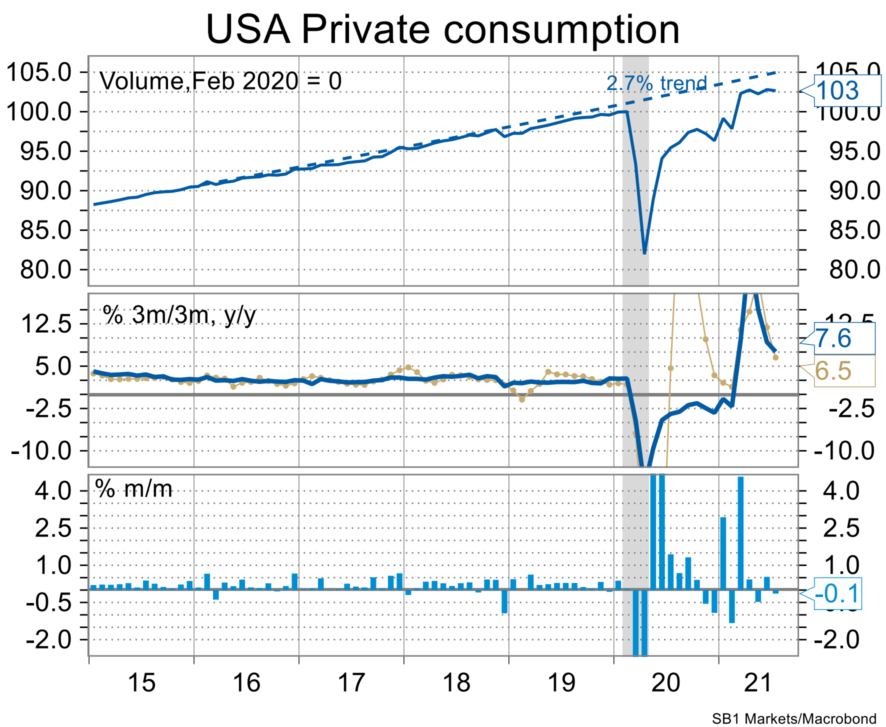


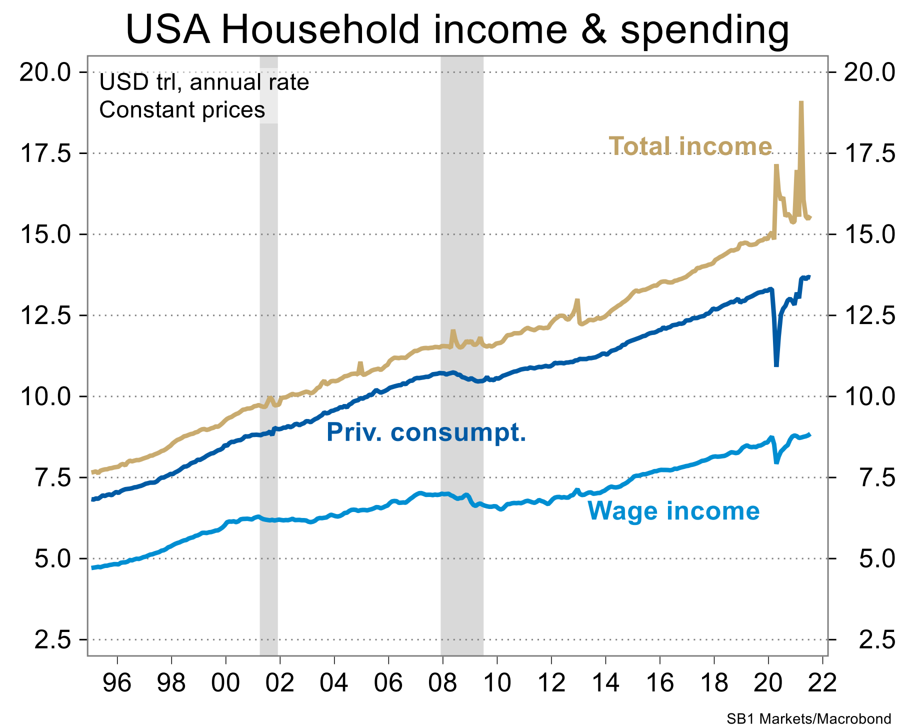
- **Higher EBITDA or profit margins**, due to higher selling prices to end users (consumption, investments), without any increase in wage costs – have normally not been important for explaining substantial and sustained lifts in inflation
  - » The reason is simply that historical or any likely variation in the EBITDA margin or in the profit rate normally have been too small to explain substantial and sustained changes in the inflation rate.
  - » If inflation should accelerate by 2 pp and stay there for 2 years, just due to a lift corporate sector margins, they would have to increase by almost 4 pp. From a normal profit level, like today, that's close to 'impossible', in macro
  - » If anything – and over time – corporate margins are negatively correlated with inflation
- **Sort term,** changes in corporate margins may explain changes in inflation without changes in other costs, normally when raw material prices increase rapidly – like what we observe now
- **Faster growth in unit labour costs** (wage growth – productivity growth), has normally been the main driver for substantial and sustained increases in inflation
- **Wage inflation** is so far kept reasonable in check in the US, but signals from the labour market are unanimous, the labour market has become extremely tight over the past few months
  - » **Demand for labour** is very strong, as witnessed by all surveys, official vacancy data and endless anecdotes
  - » **Supply of labour** is still lacklustre – and far below the pre-pandemic level. Most likely, supply will strengthen substantially the coming months as:
    1) The virus is brought fully under control, and there will be no reason for workers not apply for work (2.7 million (1.8% of the labour force stayed outside due Covid in April)
    2) The federal pandemic schemes for extra support to the unemployed runs through Sept (some 16 states has decided/are discussing to close theses programs immediately). Lower benefits will probably increase supply of workers
  - » However, even **before the pandemic**, the labour market was tight, wage costs were increasing and profit margins were under pressure
  - » Reports on **wage increases** are common too, both in surveys and from individual sectors & companies – as from Amazon, and McDonalds last week

More charts & comments on the following pages

Household income up in July, real spending flat – and it has been flat since April

Signals substantial slowdown in GDP growth. The savings rate just 2 pp above the pre-pandemic level

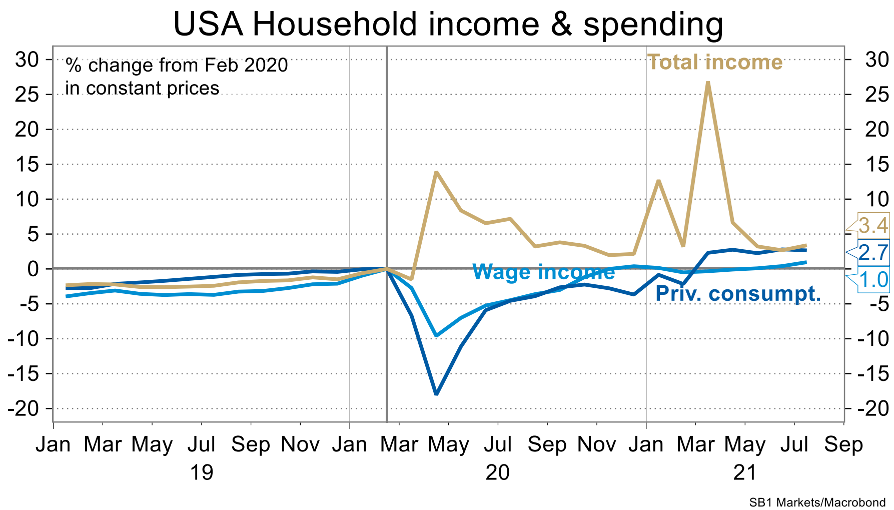


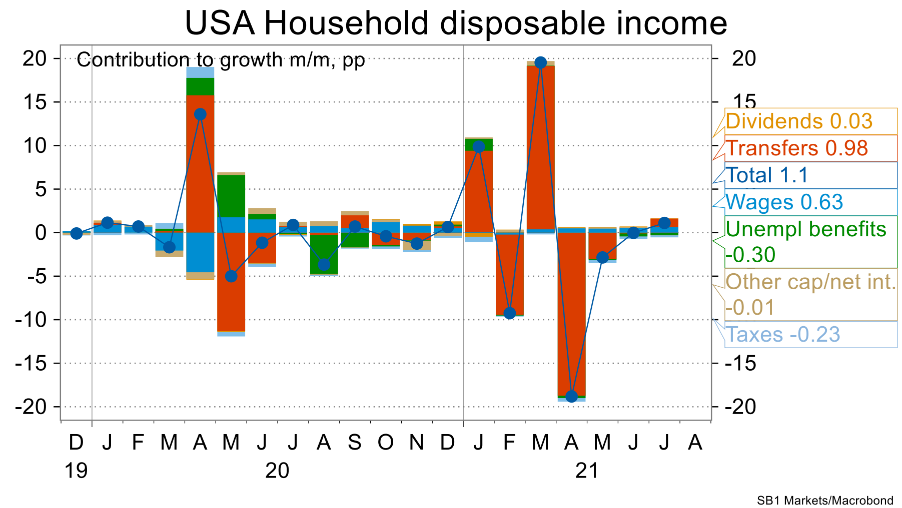


- **Private consumption fell** 0.1% in real terms in July, a tad less than expected (spending rose 0.3% in nominal terms, expected +0.4%). Consumption in real terms have flattened since April, as goods have yielded while services are recovering – but not that fast
- **Personal disposable real income** rose by 0.7% in July (household income rose by +1.1% nominally, expected 0.1%). Government transfers contributed to most of the increase, probably also vs. expectations. Market based revenues rose too, wage incomes are steadily on the way up
- **The savings rate** rose by 0.8 pp to 9.6%, following another downward revision (-0.6 pp this time). The savings rate is some 2 pp above the pre-pandemic level. In addition, since the pandemic started, households have saved an extra amount equalling 13% of one years GDP. There is still some money to be spent

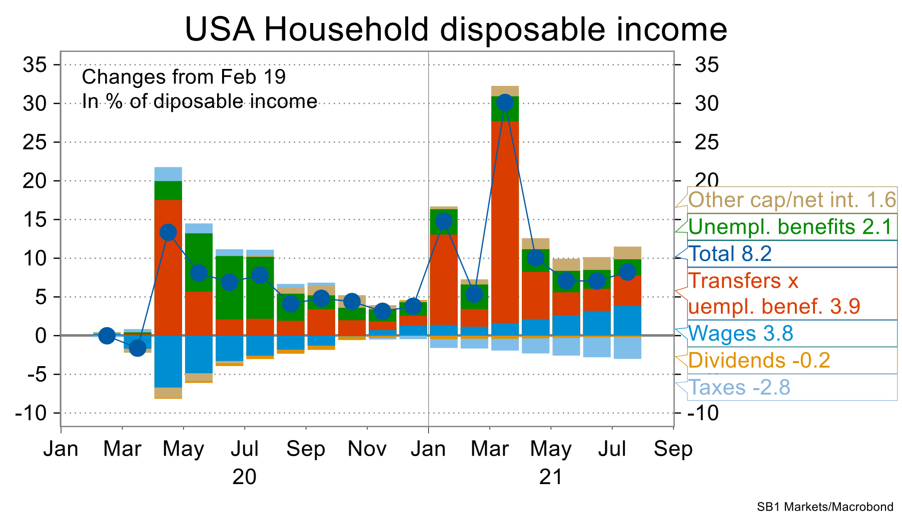
Income growth is normalising – but up more than expected in July

... due to an increase in transfers (ex unemployment benefits). Wage income is steady recovering



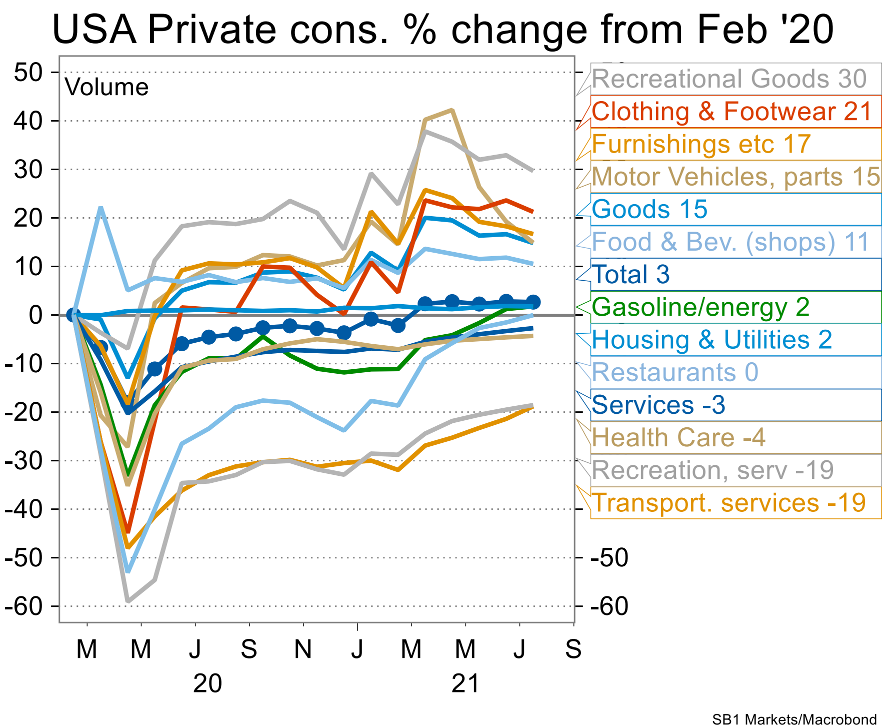


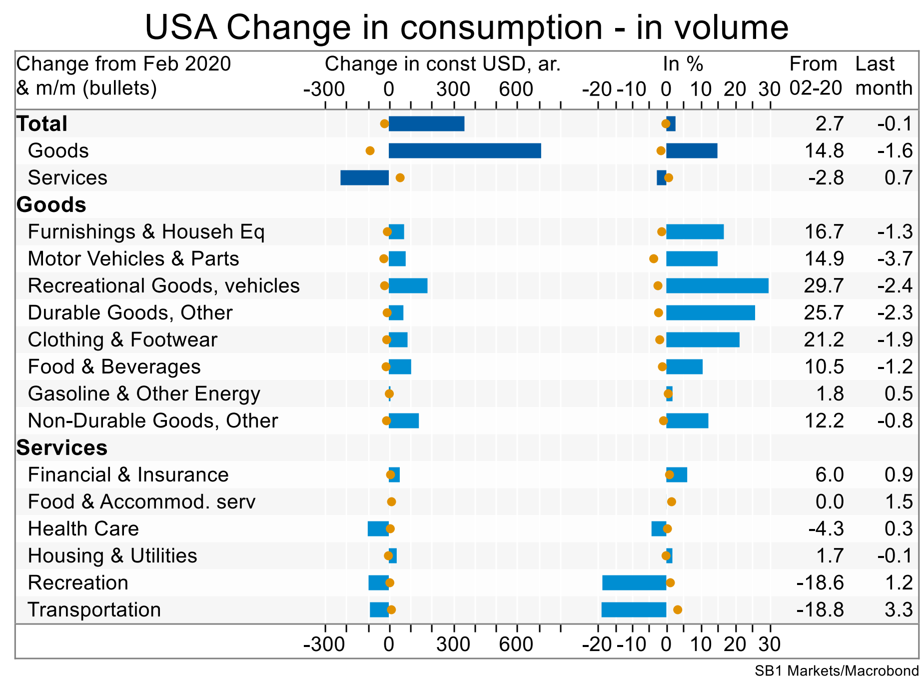
- **Last month:** Household disposable income rose by 1.1% in July, expected up just 0.1% (personal income, before tax), probably because a further cut in transfers were expected
  - » However, transfers from the government (ex. employment benefits) rose equalling 1% of income 0.5% of disposable income. Wage income contributed by 0.6%
- **From Feb-20:** Disp. real income is up by 3.4%, following a another downward revision. Nominally, disp. income is up 8.2%
  - » Nominal wage income is 3.8% above the Feb-20 level, even if hours worked still are far below, as the average wage is sharply up
  - » Unemployment benefits are up equalling 2.1 of disp. income. Total 'labour' income is up 5.9%, a normal income growth
  - » In addition, other transfers are up eq. 3.9% of disp. income, far higher than a normal growth rate
  - » Most of these extra incomes have been saved, as it has not been possible to spend them where consumers wanted



Consumption of goods is slowing, services up – but just slowly

Consumption of goods down 1.6% in June, services up 0.7%. Goods +15% vs Feb-20, services still -3%

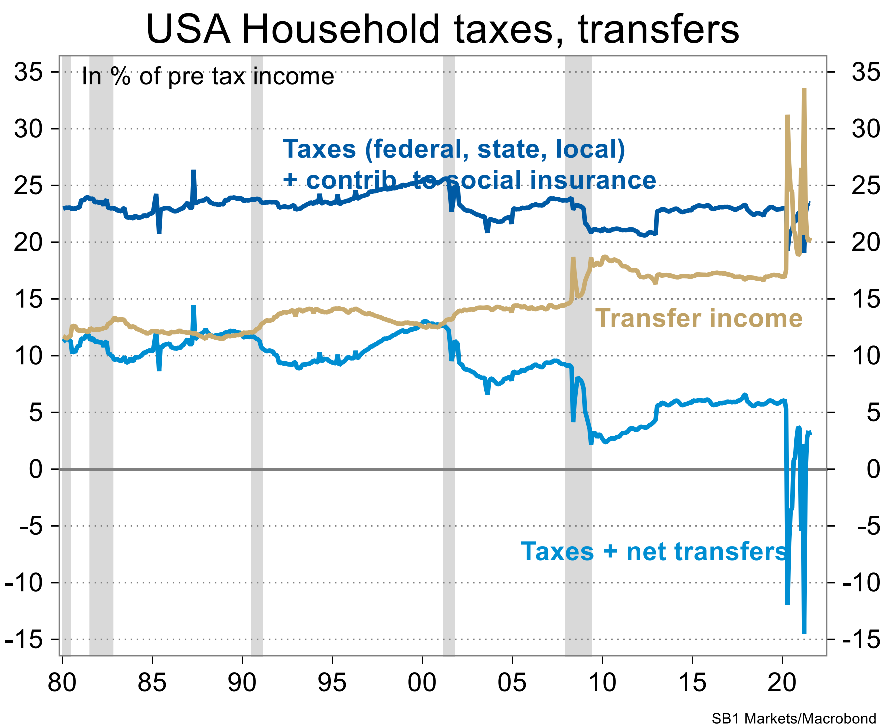


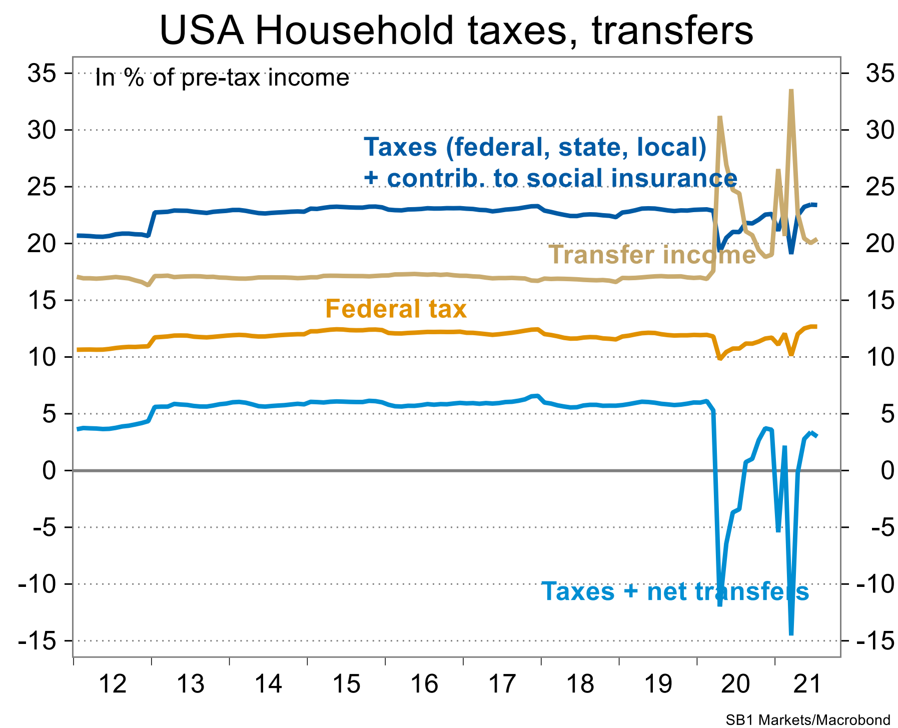


- The slowdown in **consumption of goods** is broad – and will very likely continue the coming months – as levels are way above any reasonable sustainable level – if spending on services should increase further
- **Consumption of services** rose 0.7% in July, all main sectors are up. Spending is now 3% below the Feb-20 level, in volume terms. Restaurants are back to the starting point, in volume terms (meals served'), while transportation and recreation are both down -19% (both revised down, again) - so there must be more to go the coming months/quarters
- Total consumption us up 2.7% vs. Feb-20, a below par growth rate over 16 months – and total spending has more or less flattened in real terms since April

Towards more normal times – but transfers are still higher than normal

The net balance between the government (state, federal) and households is unsustainable

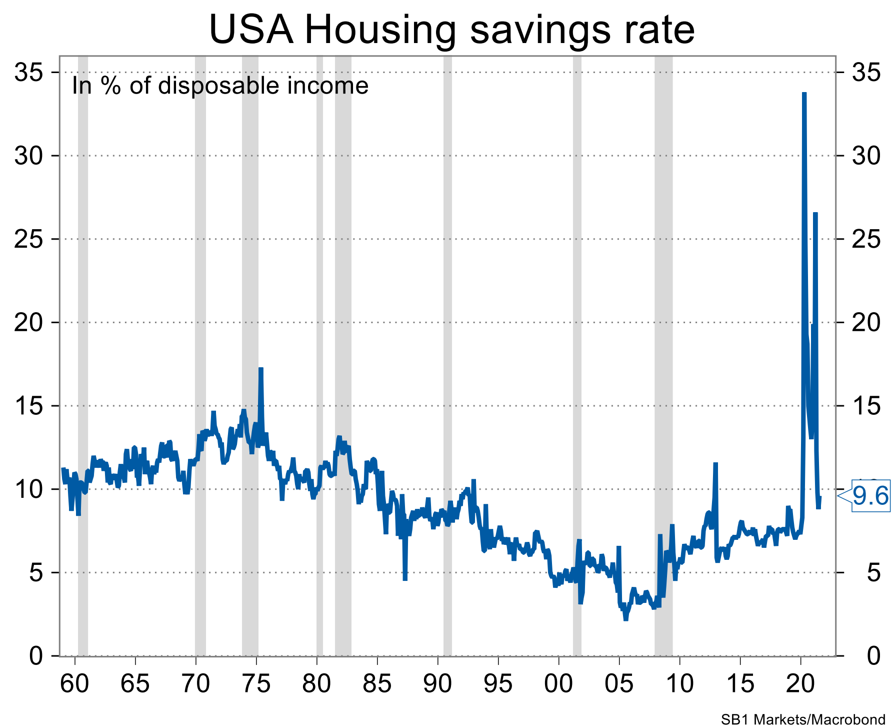


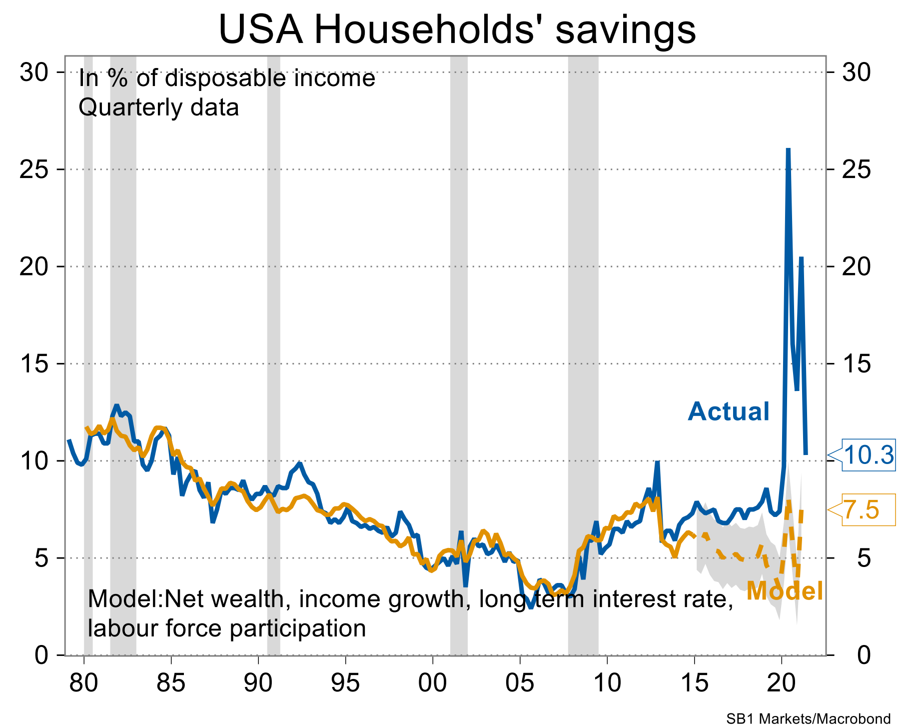


- The net balance is some 3% of disposable income below the pre-pandemic net transfer/tax rate
- In addition, the this 'normal' implied a substantial government deficit – <u>which was not sustainable either</u>
  - » Before year 2000, the net payment to the federal government equalled 10% - 12% of pre-tax income
    …. and somewhat below 10% until the Financial crisis. Since 2012, the net tax rate has been some 6% of GDP
  - » Now, the rate is at 3% of GDP – and the budget deficit is huge…

The savings rate revised down but rose marginally in July: + 0.8 pp to 9.6%

The Nat. account revision shaved another 0.6 pp of the savings rate (down to 8.8% in June)

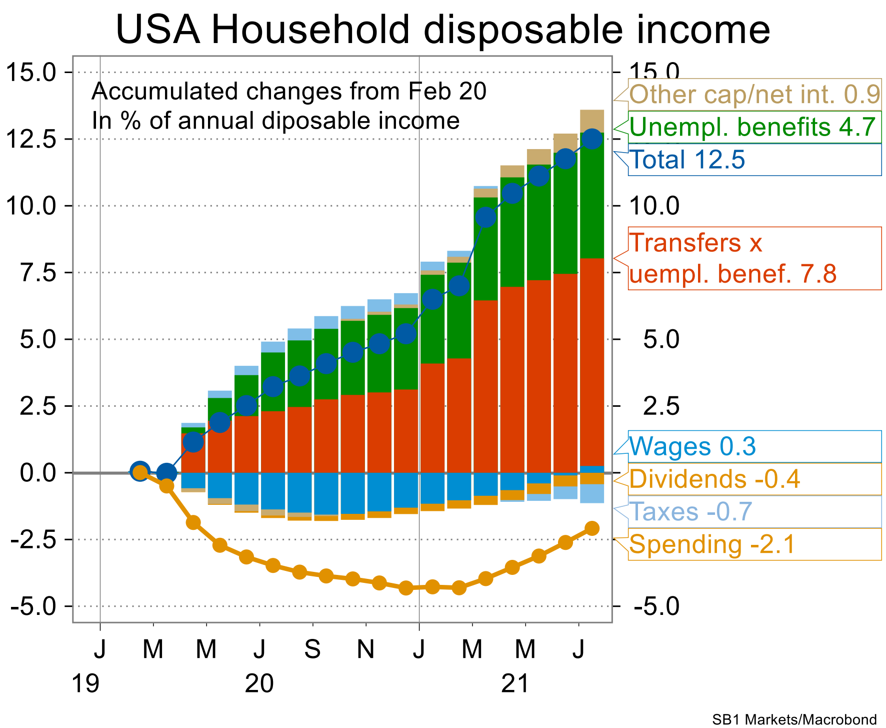


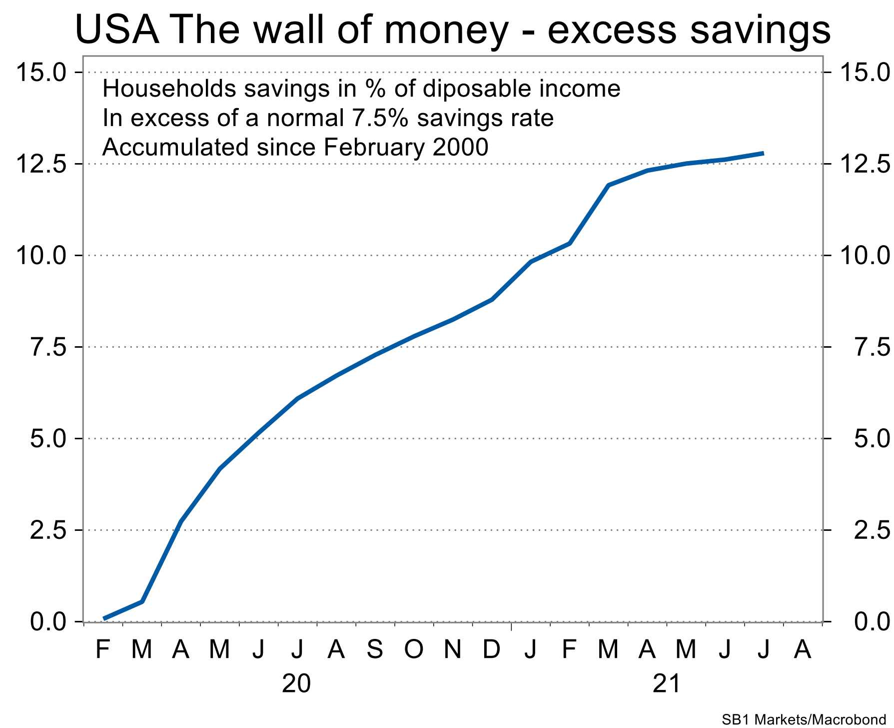


- The savings rate has approached pre-pandemic levels – but is still almost a couple of points above
- In addition, **accumulated households excess savings** during the covid crisis amount to some 13% of annual disposable income – the 'Wall of Money', check next page

The wall of money: How it is built – and the height

Transfers to households, both the cheques & the extra jobless benefits far larger than income losses

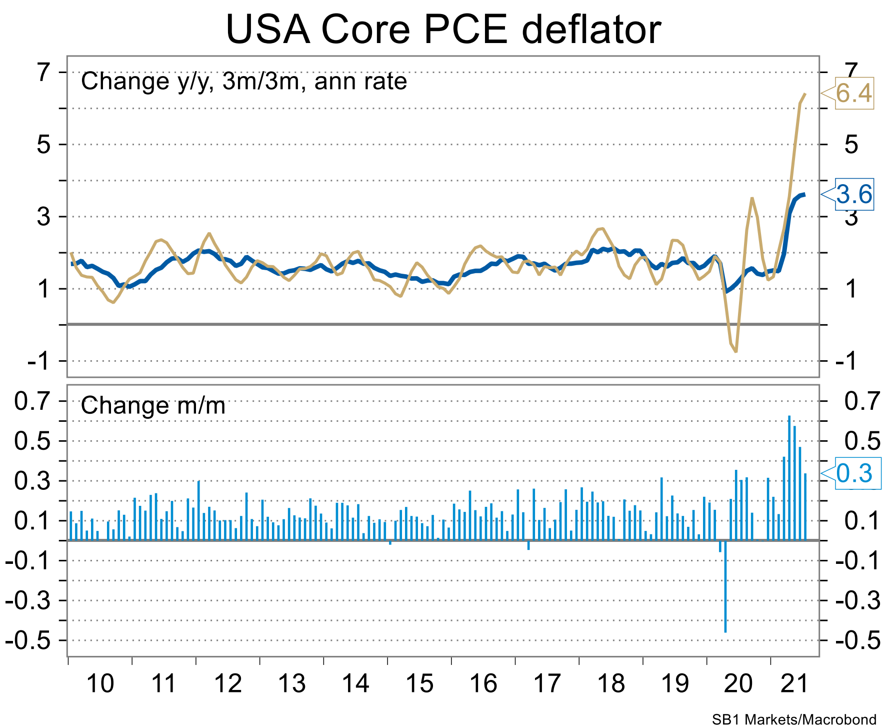


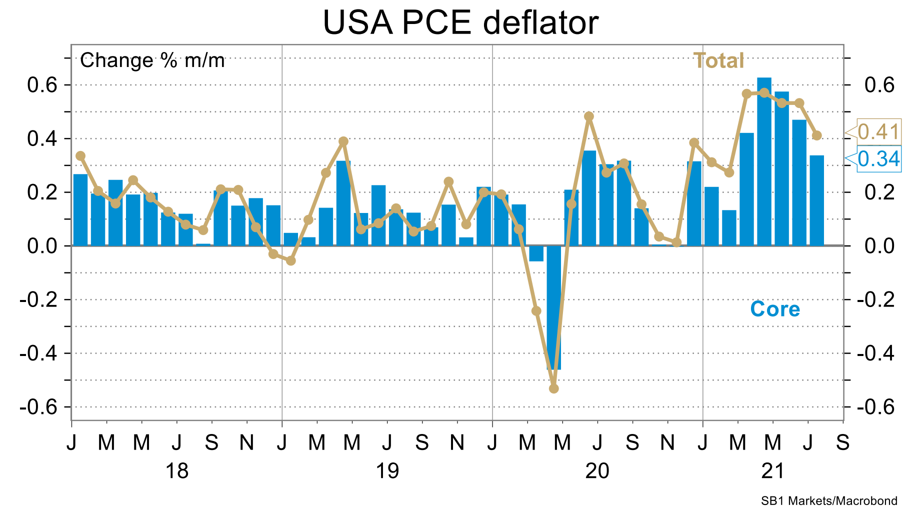


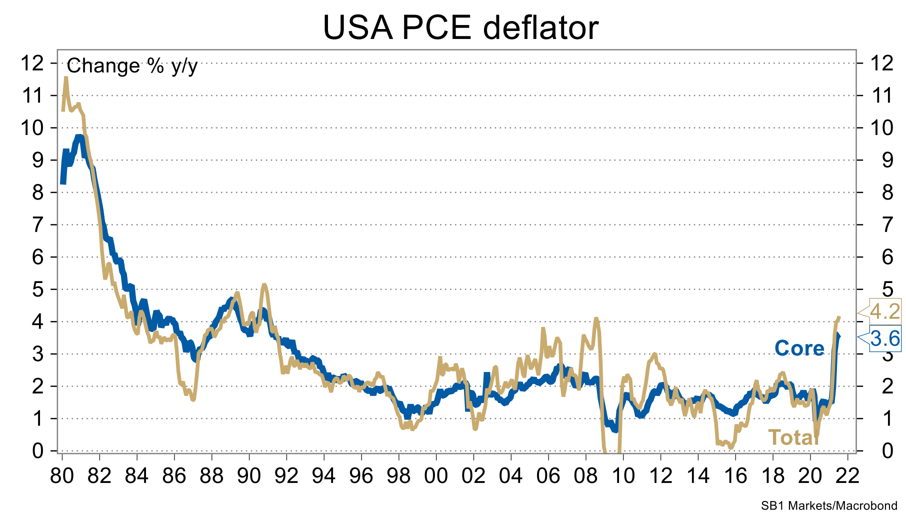
- … That is, income losses from 'the market', wages, dividends & other capital income. Income growth has been fabulous – and spending has been weak, on services & in total

Core PCE up 0.3% in July, 3.6% y/y – as expected

Price inflation is slowing (m/m) but is still too high, in July at a more than 4% annualised pace







- **The core price consumption deflator** rose by 0.3% m/m in July, as expected. June was revised up 0.1 pp to 0.5%. The annual rate rose 0.1 pp to 3.6%, well above Fed's long term 2% inflation target
  - » Since June '19, the average core inflation rate has been 2.5%. Inflation has been higher than 2% measured up to 7 years back in time. So whatever plausible horizon Fed would like to apply, the average over time 2% inflation target is met (and more than that)
- **The total PCE deflator** rose by 0.5%, and the annual rate accelerated by 0.2 pp to 4.2%, both 0.1 pp higher than expected

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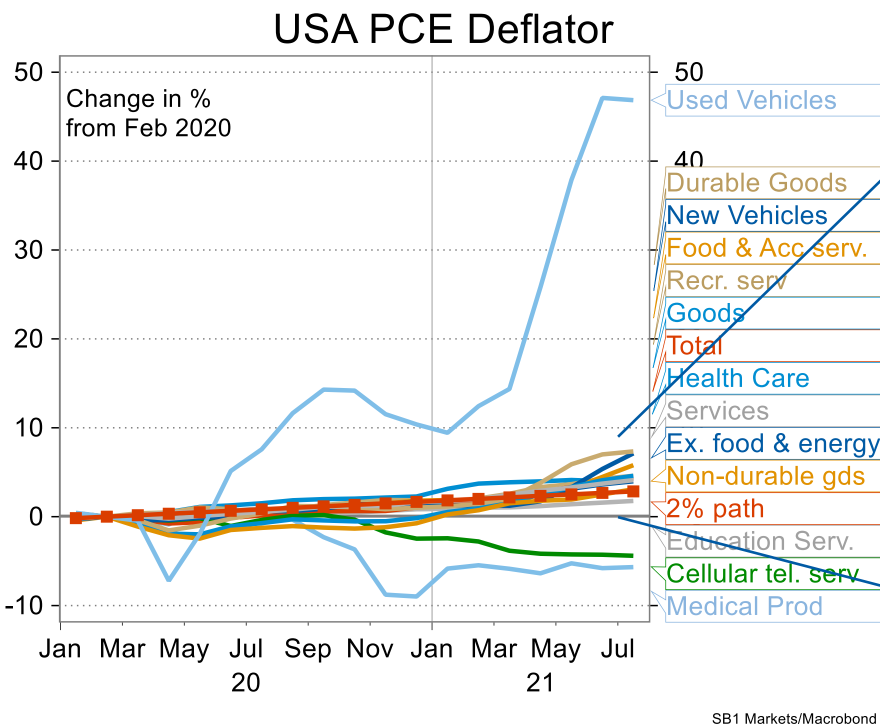
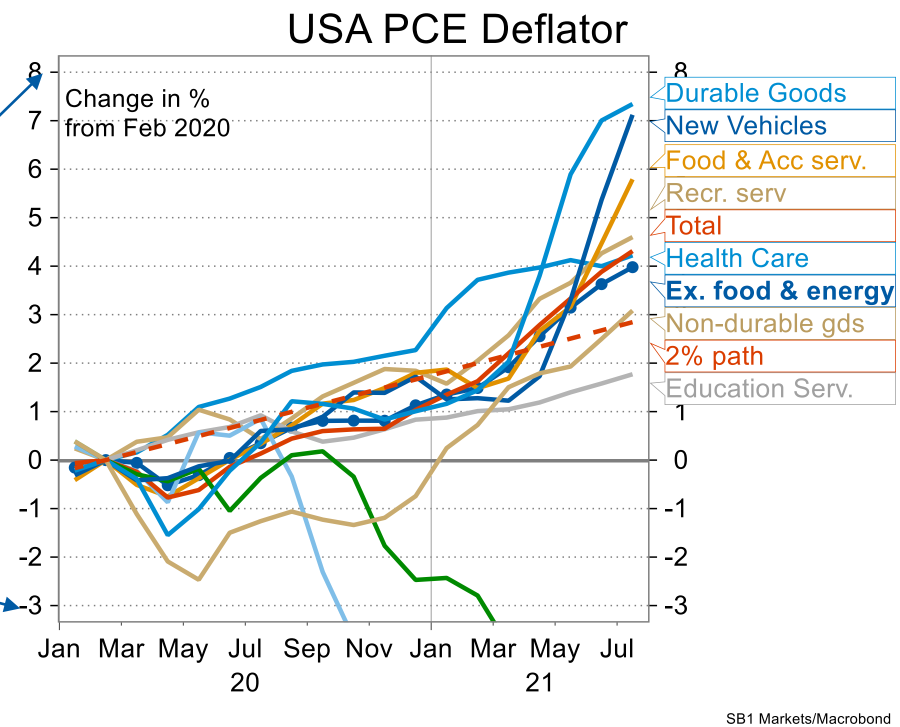
Used car prices slightly down in July – and will probably decline substantially

However, more prices are on the way up, and companies expect to increase their prices rapidly

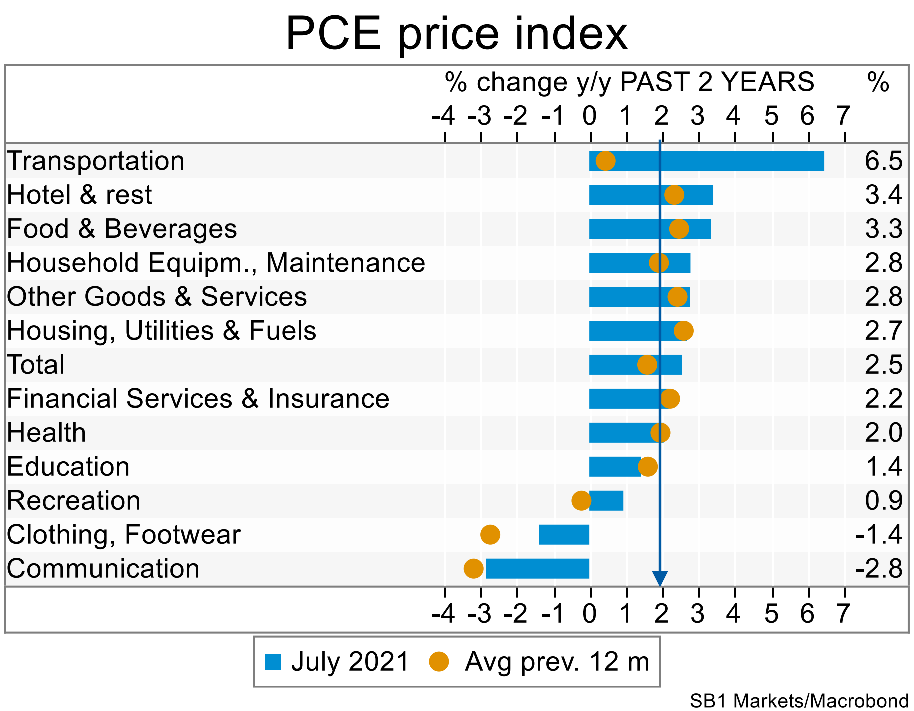


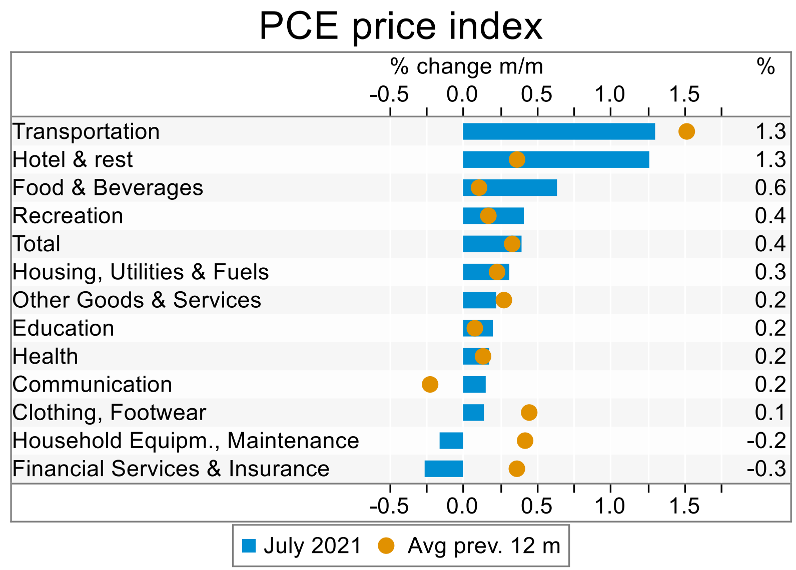


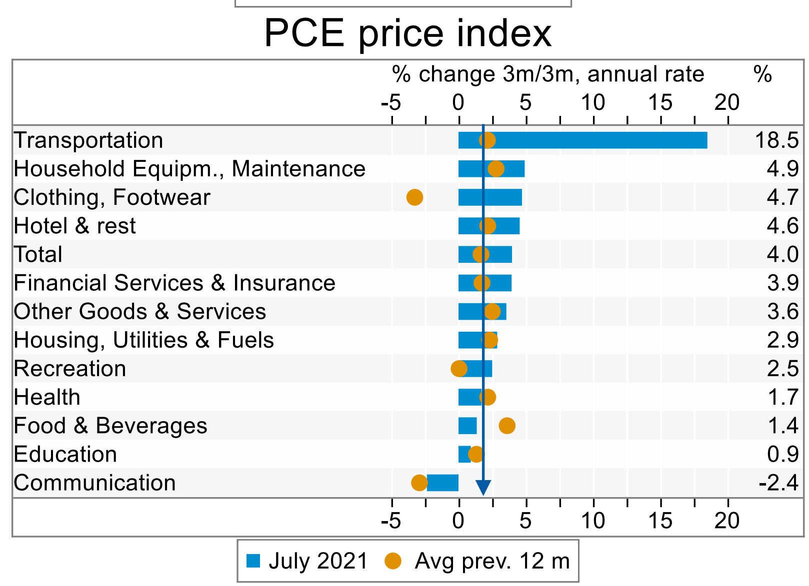
- **Used car prices** finally yielded, marginally. The downside is huge. Now, new car prices are increase sharply
- **Restaurants/hotels, recreational services** are lifting their prices sharply
- **Health care** costs have increased sharply since late last year but are now flattening

PCE by main sector: Transportation (autos & gasoline) explains a lot

However, most sectors report >2% pace of price increase the past 3m/3m (and past 2 years)







- Measured over the past 2 years, PCE inflation has been 2.4% on average. 4 sectors are below 2%, 7 sectors are above 2% (1 on par)

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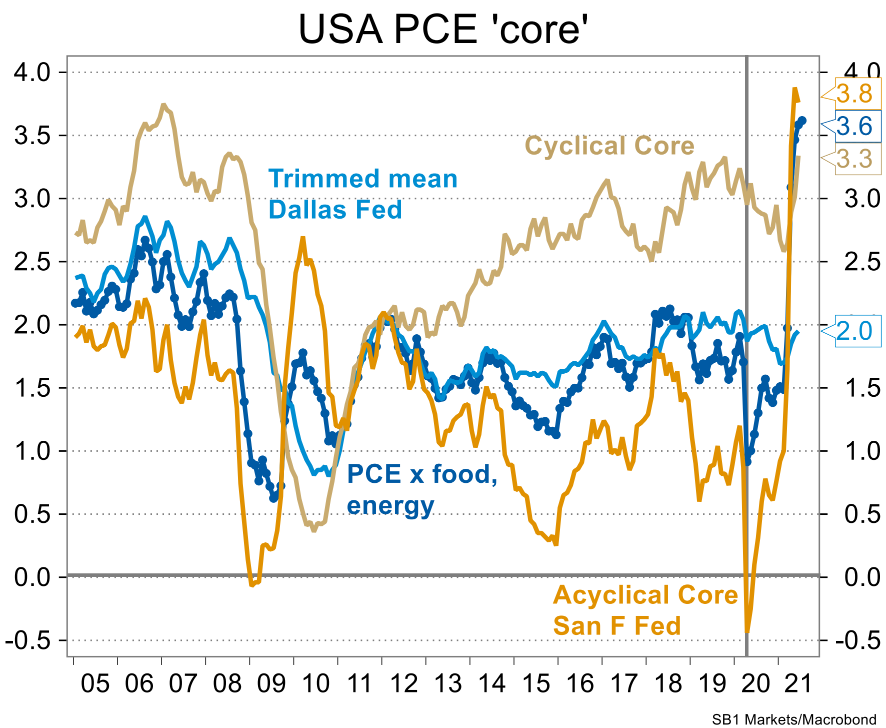
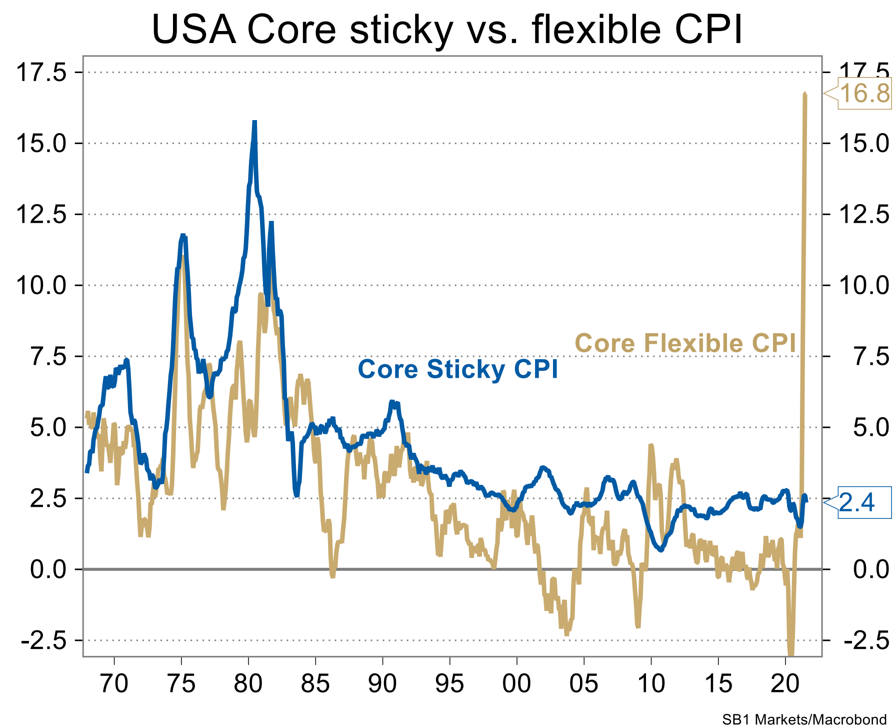
There are still some possible (and not unreasonable) excuses…

Inflation is broadening, but still just some few goods/services that have done the heavy lifting

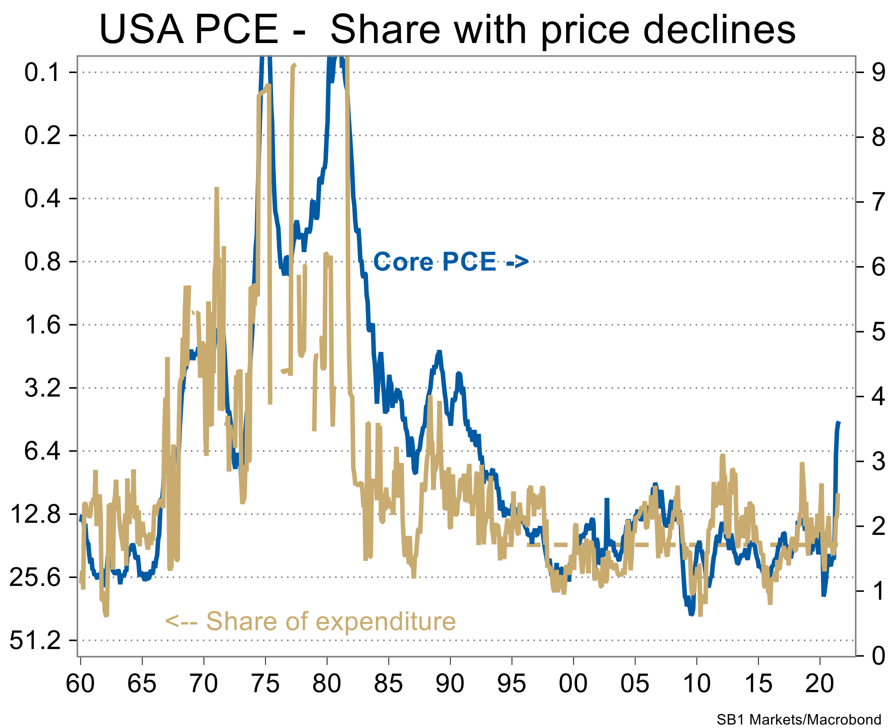


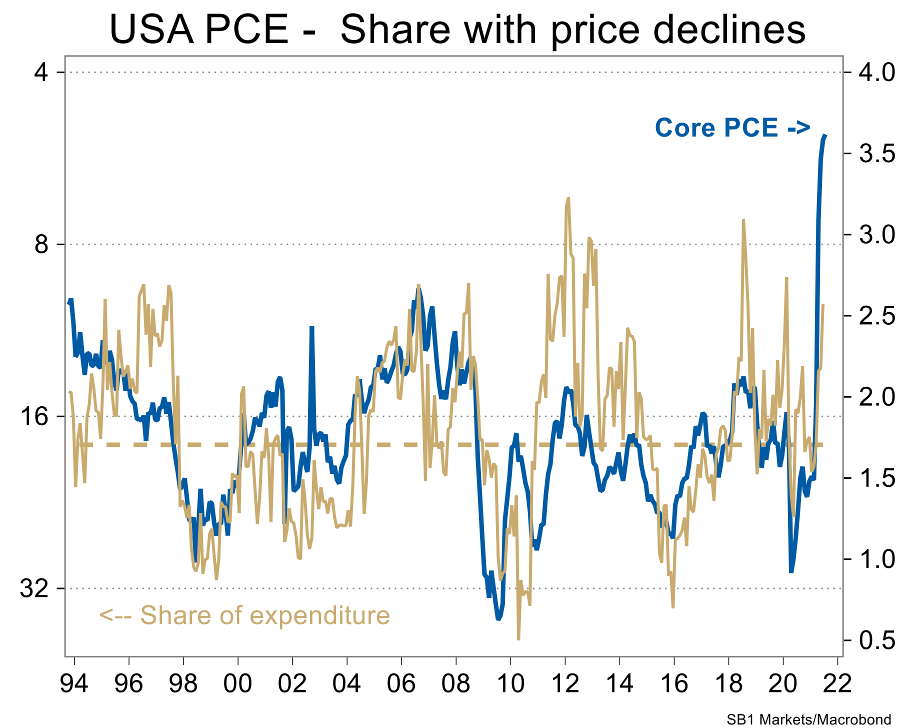


- The **trimmed PCE mean** is at 2.0% (June). The trimmed mean is probably the best gauge of 'underlying" PCE
- An index for typical **acyclical core PCE goods & services** are up 3.8%, up from -0.5% in April last year. The 2 y avg is at 1.6%
- The **cyclical core PCE** at 3.3% y/y is the highest since 2008 but not much higher than before the pandemic
- In the CPI, almost all of the lift in **core CPI** has been due to prices on good & services that normally are **flexible** – and they are more up than ever before. However, these prices are flexible both ways, and the cycles are normally rather short. The **sticky components** of the CPI is up 2.4%, marginally above the average recent years. For inflation really to take hold, these sticky prices have to accelerate (like they did from 1973). However, the flexible component has contributed substantially to keep inflation low the past 8 years

PCE: Fewer prices are falling but not that few

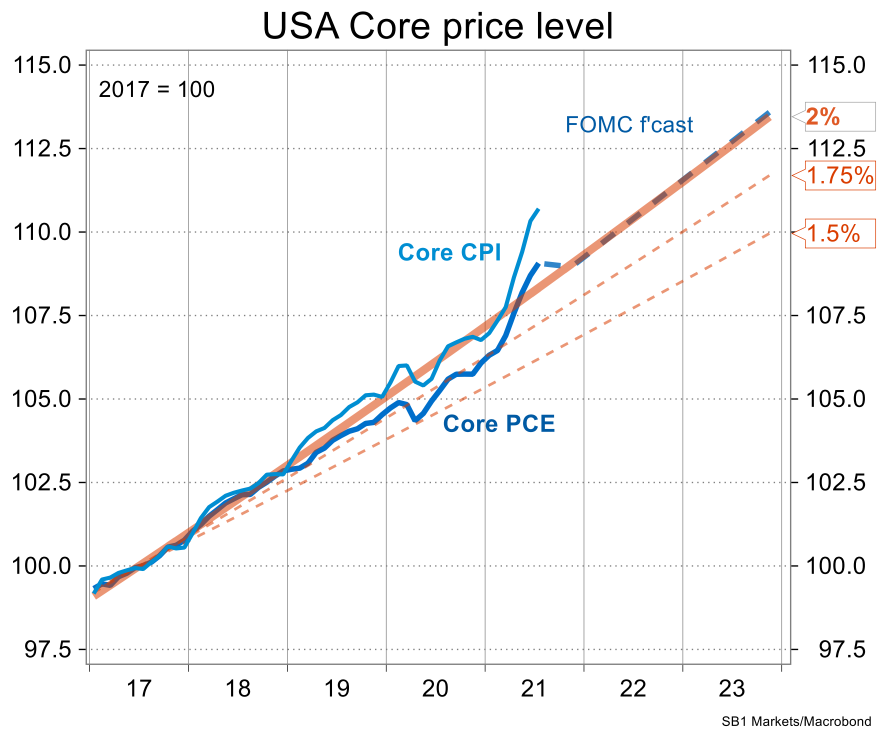
... though not an early bird to watch

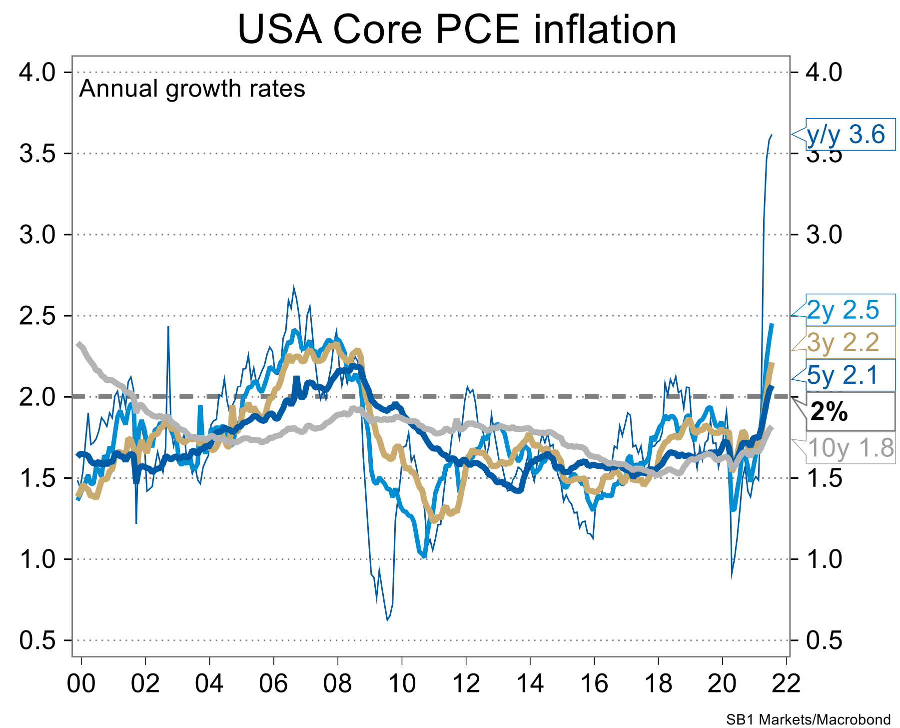




The price level is on the right track, right? Finally, even Powell said so

However, he is still stressing that the recent hike is transitory – and he may still be correct



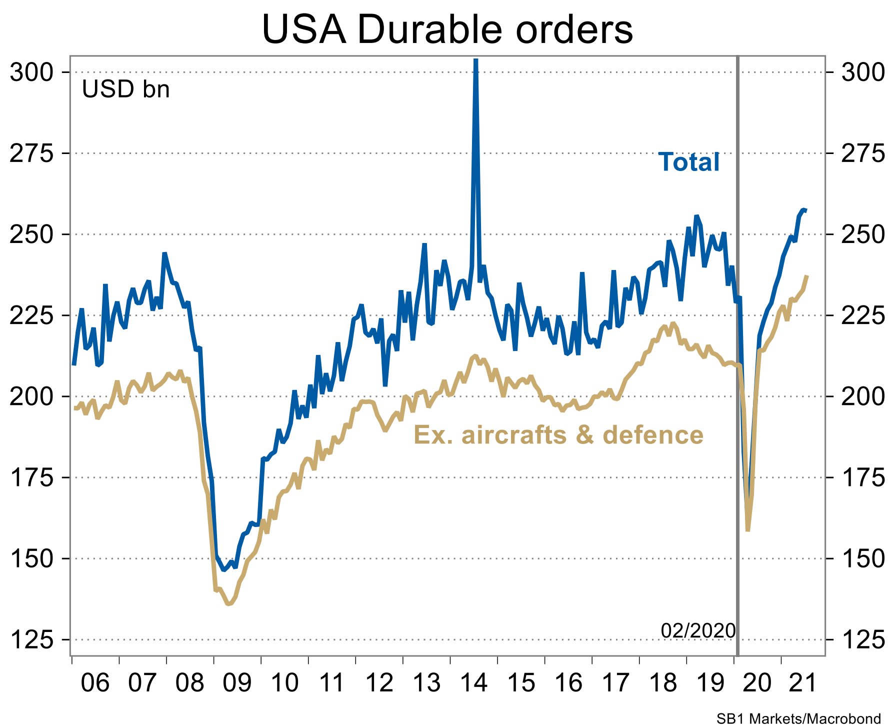


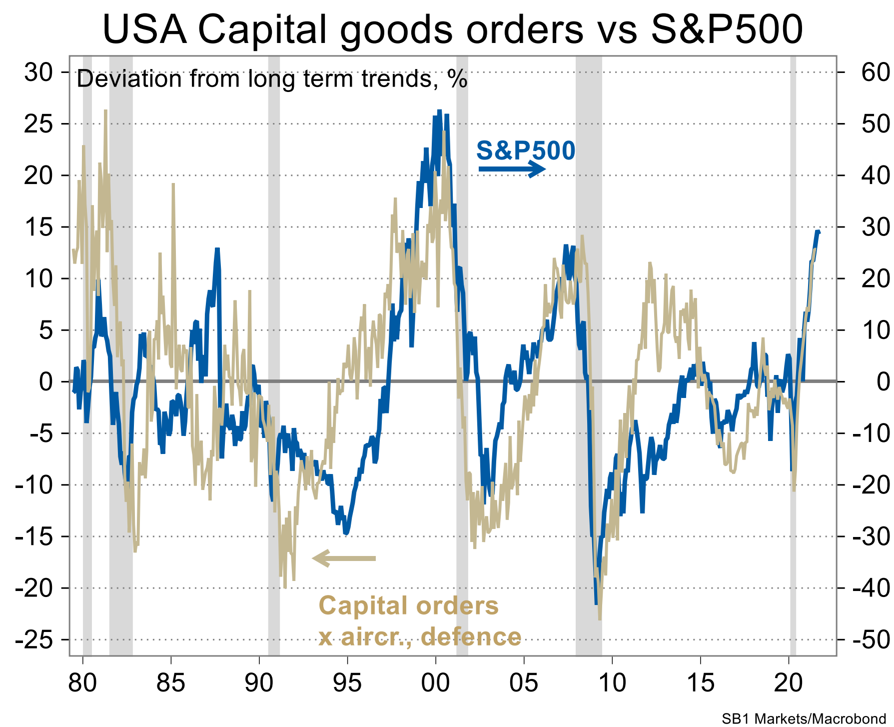
We stick to our main inflation analysis:

- **Raw material cycles** are not lasting that long and the impact on consumer prices are short lived
- **Higher profit margins** (unit profits) have never been the main reason for a sustained lift in inflation
- To sustain a lasting increase in inflation, **unit labour costs** have to grow faster. The ULC = wage inflation – productivity
- **A tight labour market** normally implies higher wage inflation. Now, almost all wage cost indicators signal higher wage growth, and more than the tilt towards higher paid employees can explain. This is the real challenge for the Fed

Core durable orders further up in July

Investment goods orders are trending up too, signalling further growth in business investments in Q3

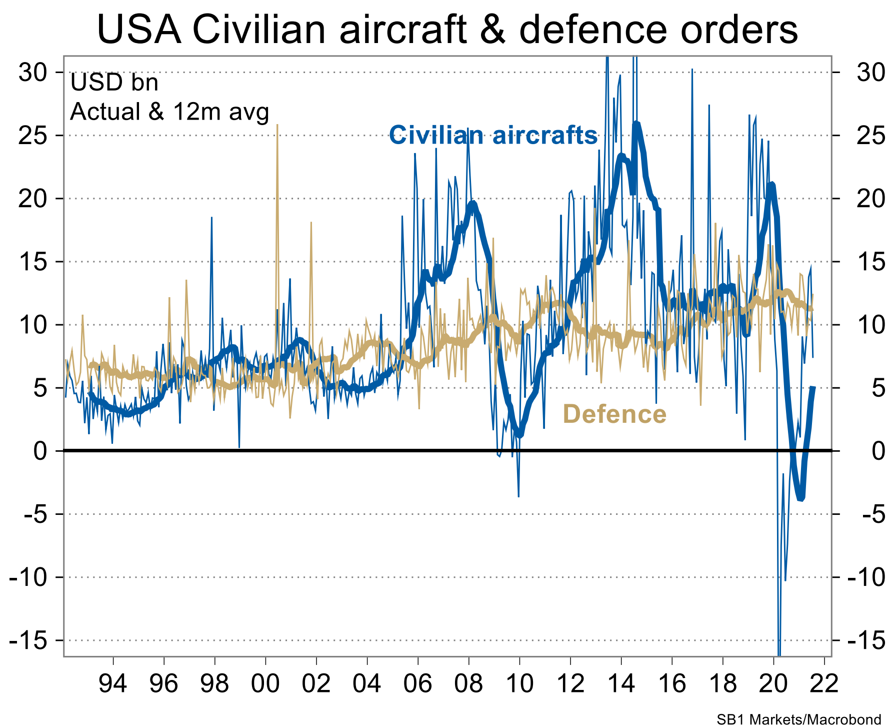


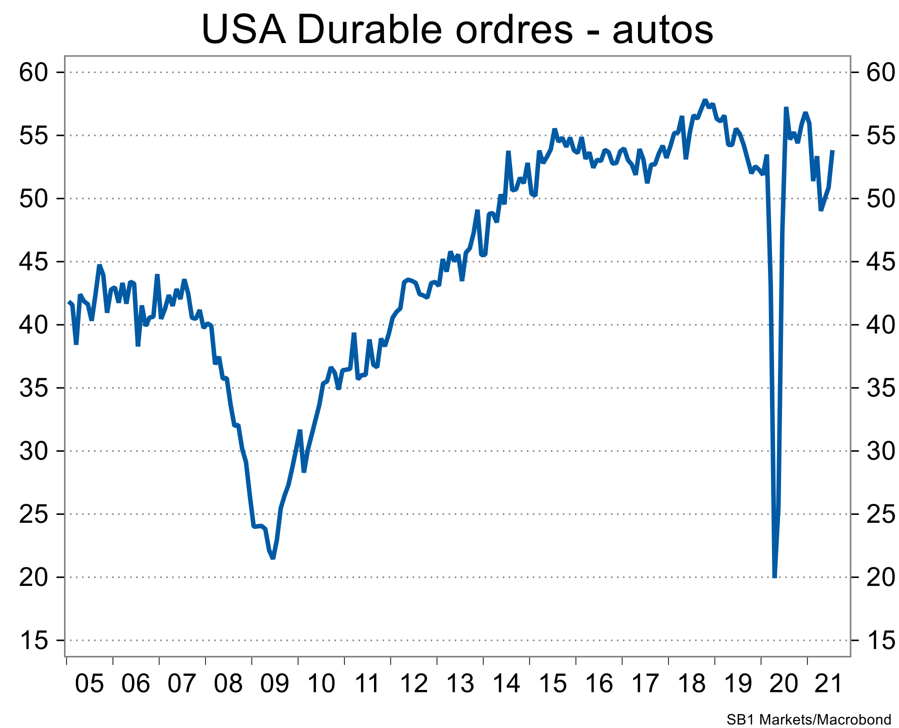


- **Total durable** orders fell by 0.1%, expected down 0.2%. Aircraft orders fell (but they have recovered for last year's slump). The trend is steeply up
- **Core orders** (ex aircrafts & defence) gained 2%, expected 0.5%. The trend is strong. Auto orders rose sharply in July
- **Core <u>investment</u> goods orders** fell 0.1% but the trend is still straight up, and order inflow in Q2 will be well above the Q1 level
- **Order inflow** is far above pre-pandemic levels, especially for investment good orders and surveys are still strongly hinting a further increase the coming months

Aircraft orders down in July but almost back to a normal level

... while auto orders rose sharply, and are almost back to a normal level too





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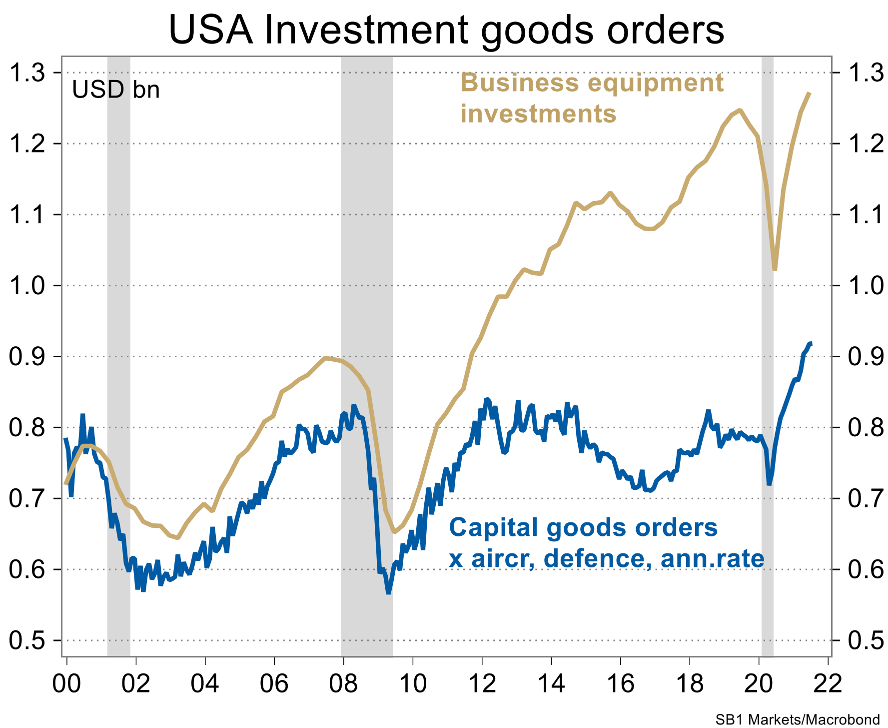
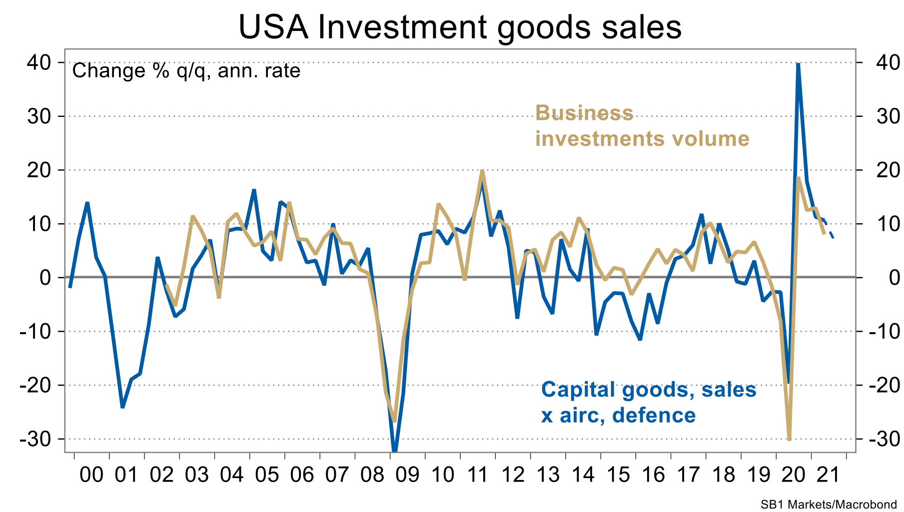
Core capital orders are still going strong

Signal decent growth in business investments into Q3

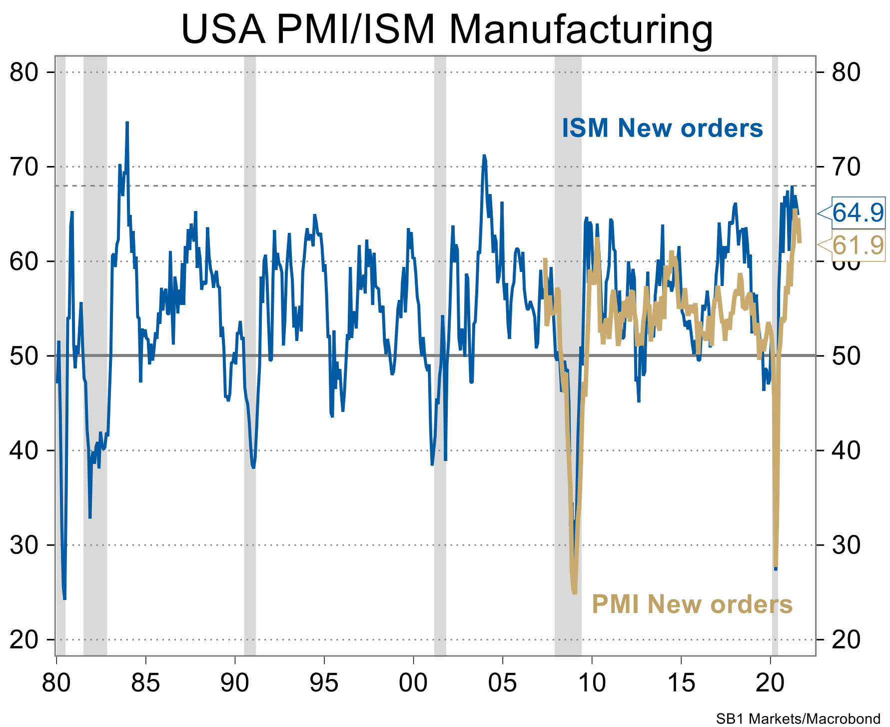


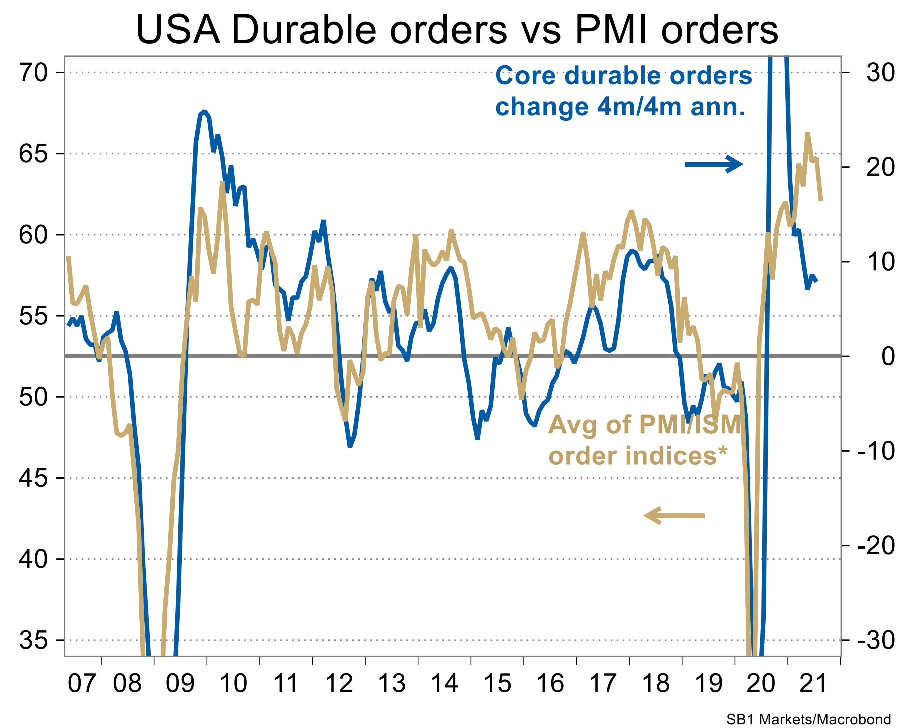


- **Core (x aircraft, defence) capital goods orders** were close to flat in July, expected up 0.5%, as expected but the history was marginally revised up. Shipments rose 1.0% in July. Both are growing at a brisk underlying pace signalling growth in business investments into Q3, albeit at a slower pace than during de previous quarters
- **The business investment** level is well <u>above</u> the pre-pandemic level – and not low vs. a reasonable long term trend

The ISM/PMIs are signalling a further and rapid growth in order inflow

These surveys are reporting a rapid increase in order backlogs as well

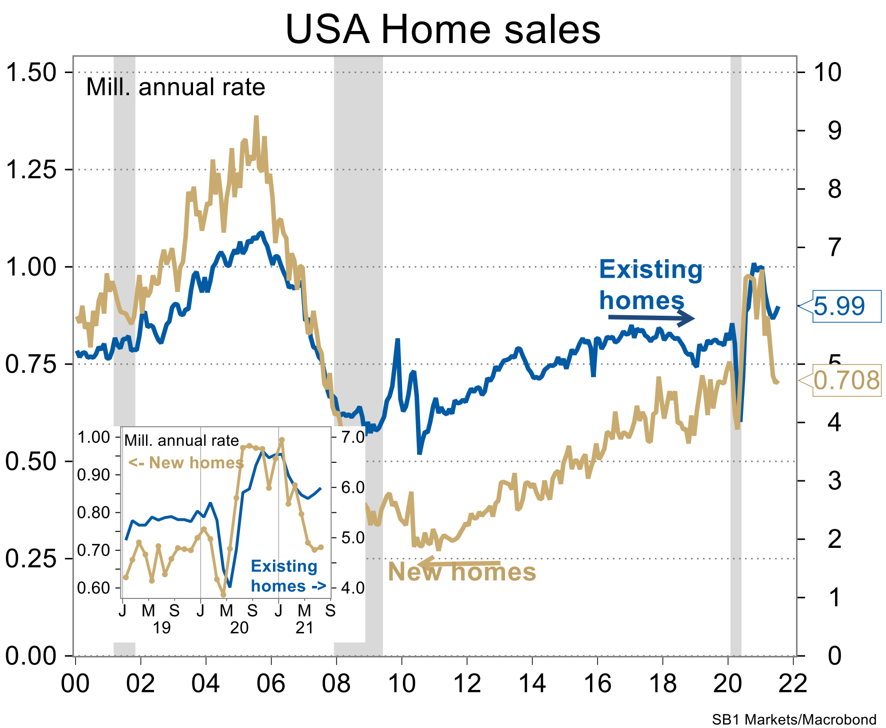


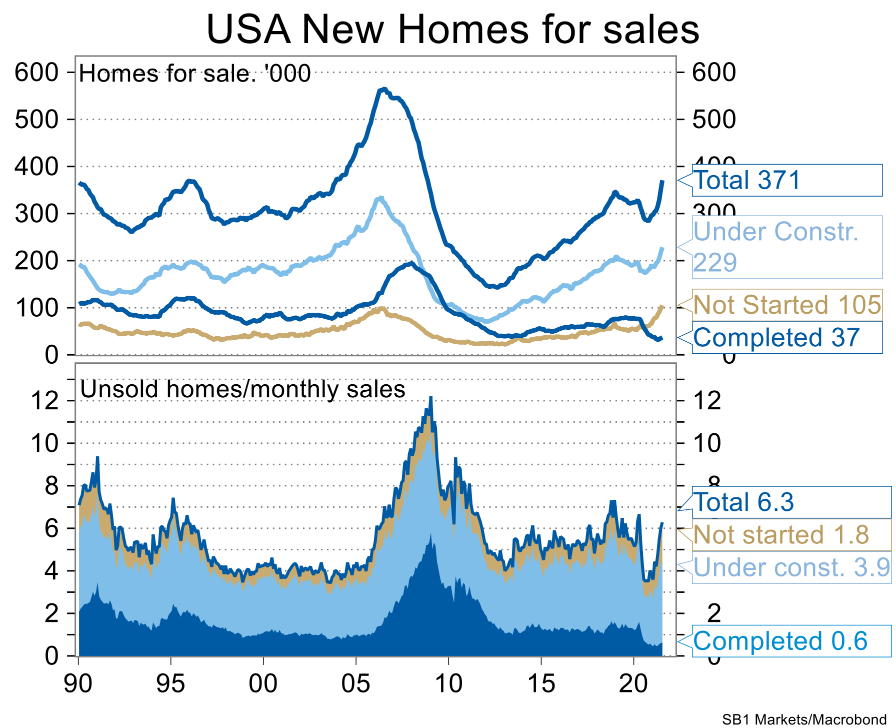


* The ISM order index is

New home sales slightly up in July, still down.

Too few completed homes to chose between? However, more new homes are underway

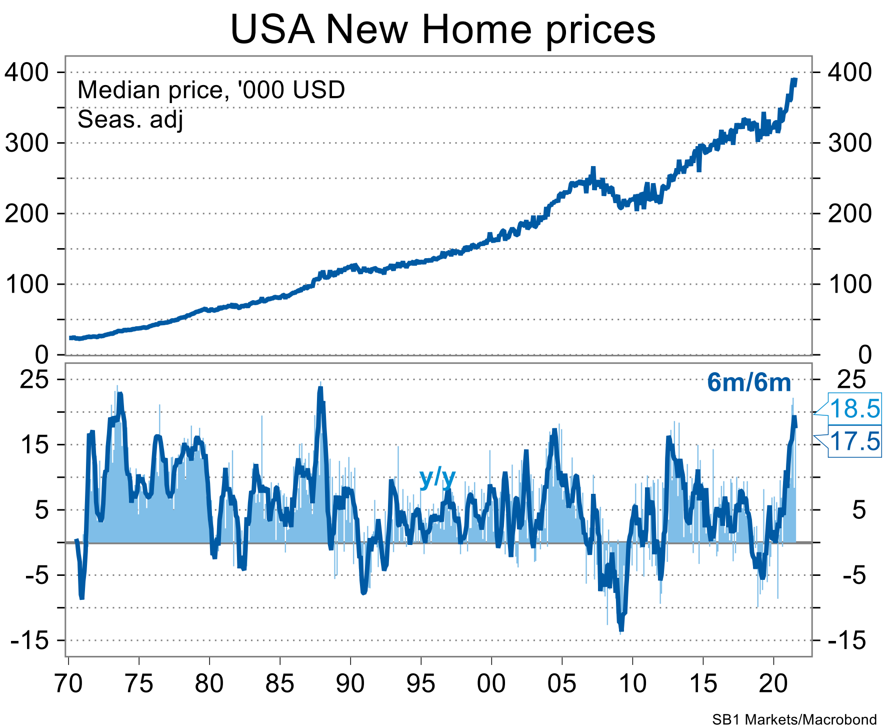


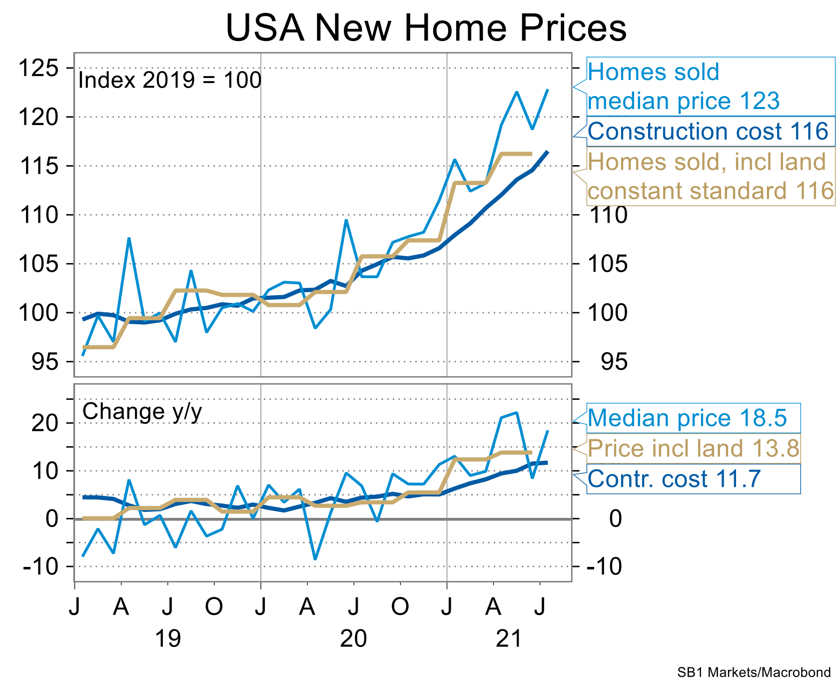


- **New home sales** rose to 708' (annualized rate) in July, up from down from 701' in June (revised up from 676', following several and larger downward revisions the previous months). Sales were expected at 700' in July. Sales are down 29% from January – and marginally below the pre-pandemic level. *On existing home sales: 2 pages fwd*
  - » The inventory of unsold homes has increased somewhat the past 8 months primarily because many projects that haven't started yet have been added, in fact more new projects than ever, a sign that the supply side is responding to the strong demand. The no. of completed homes for sale is record low, equalling 18 days' sale (if homes are sold 7 days per week)

Construction costs up, but new home prices even more

Construction costs are up 11% y/y, selling prices are up 14% – 16% (like existing home prices)

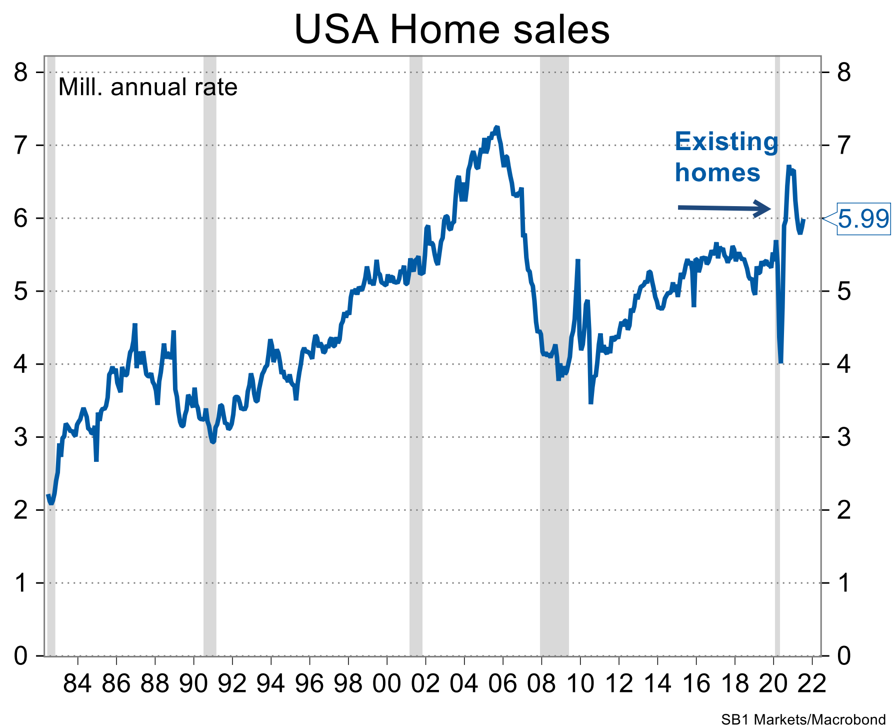


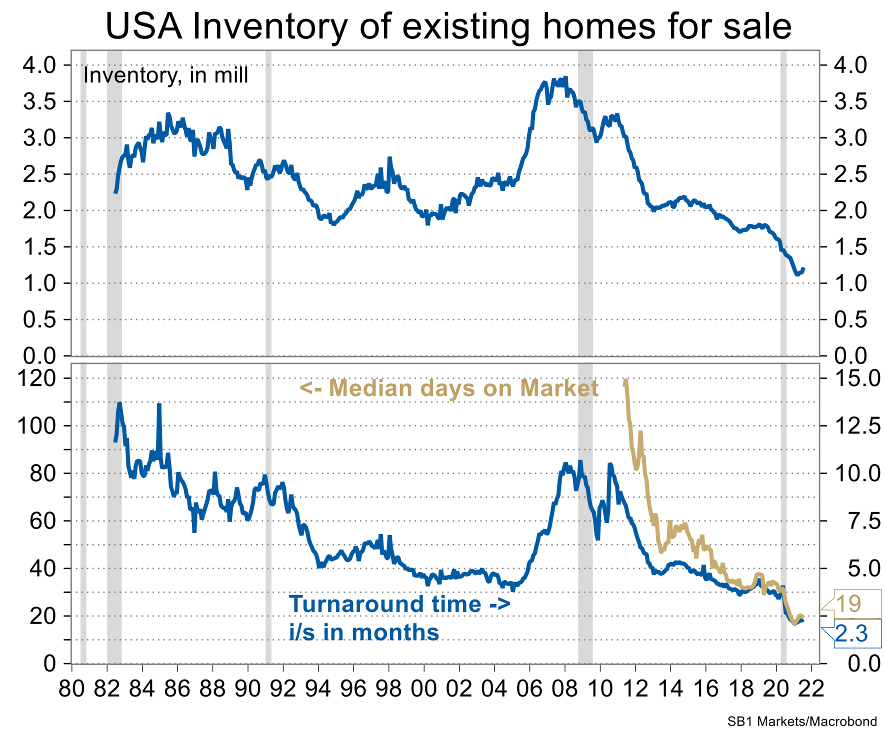


- Monthly **Median new home sales prices** are volatile, in July the annual rate was 18.5%, up from 6% in June (and 20% in May). The more relevant figure is the 6m/6m rate at 17.5% - the highest since 1987
  - » This price index is influenced by changes in the mix of homes sold – and over time by changes in standards & size
- The **construction price index** is adjusted for changes in standard & size, as is the **new homes sold price index**, which includes cost of land, and they are up by 12% and 14% resp. y/y (the latter Q2 data)
- As prices are still up more including land than the construction cost index (which of course is influenced by higher material costs), demand must be the main driver for the hike in prices (if not, land prices would have declined)

Existing home sales slightly up in July too – still well down from the local peak

The inventory is extremely low, but also marginally up past two months. Prices still on the way up

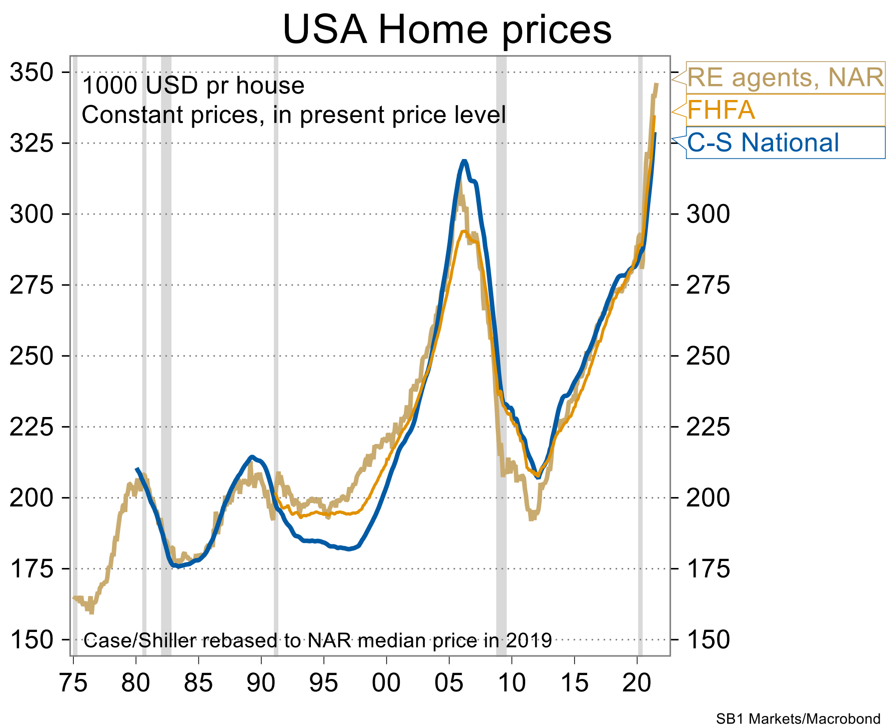


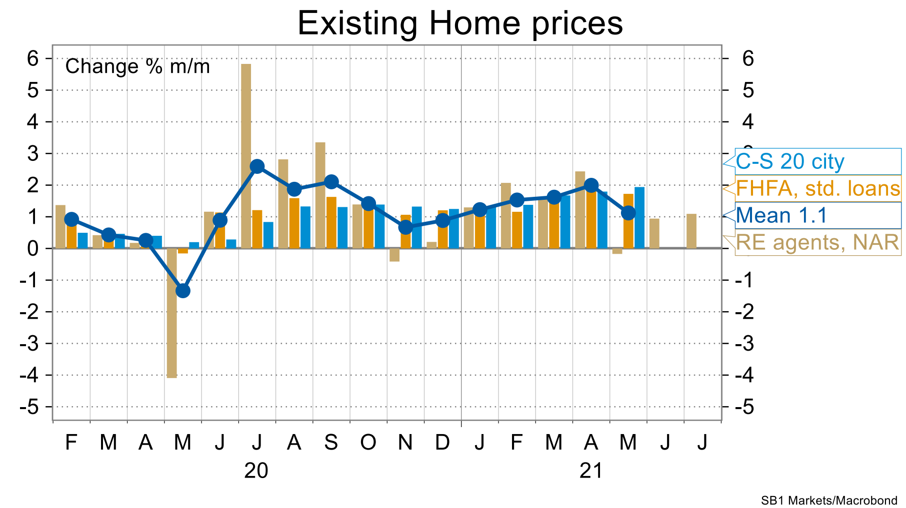


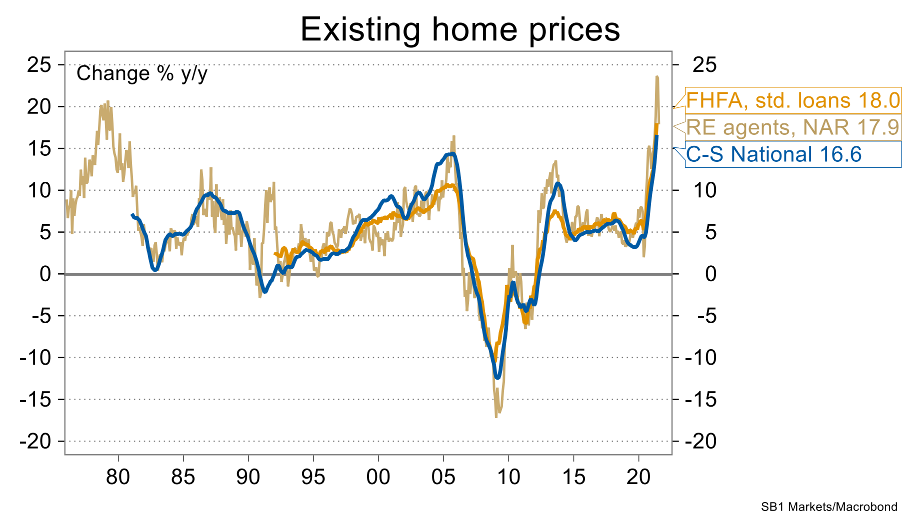
- Sales of **existing homes** rose to 5.99 mill (ann. rate) in July from 5.87 mill in June, expected down to 5.83 mill. Sales are down 11% from the local peak but still above 10% above the pre-pandemic level. Sales are no doubt kept down due to an unprecedented lack of supply. However, there are reports on buyers becoming more cautious following the steep rise in prices
- **The inventory of unsold homes** rose marginally in July too, but is still extremely low, and equals just 2.3 months of sales. During the 2005 boom, the i/s ratio was 4 months, in bad times is at 10 months. The median time at the market is just 19 days, down from 30 days before the pandemic
- **Prices** rose 1% m/m in July, like in June following the 0.1% setback in May. The annual rate still 'collapsed', to 17.0% from 23.4% in June – because prices fell 6% m/m last July *(charts next page)*

Existing home prices still on the way up

… even if the y/y rate fell sharply in July, due to the unprecedented 6% price hike in July-20



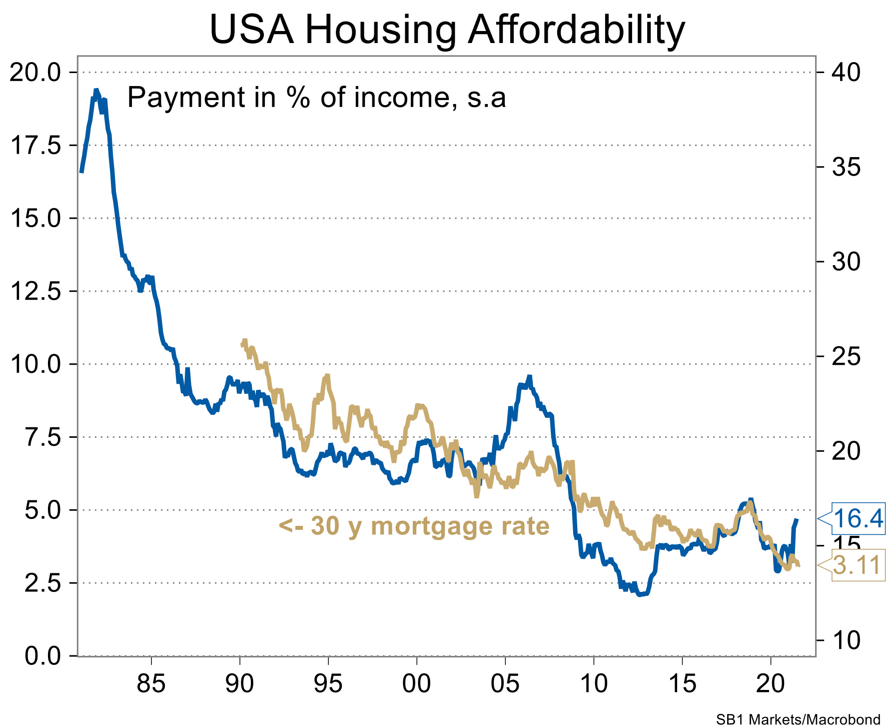


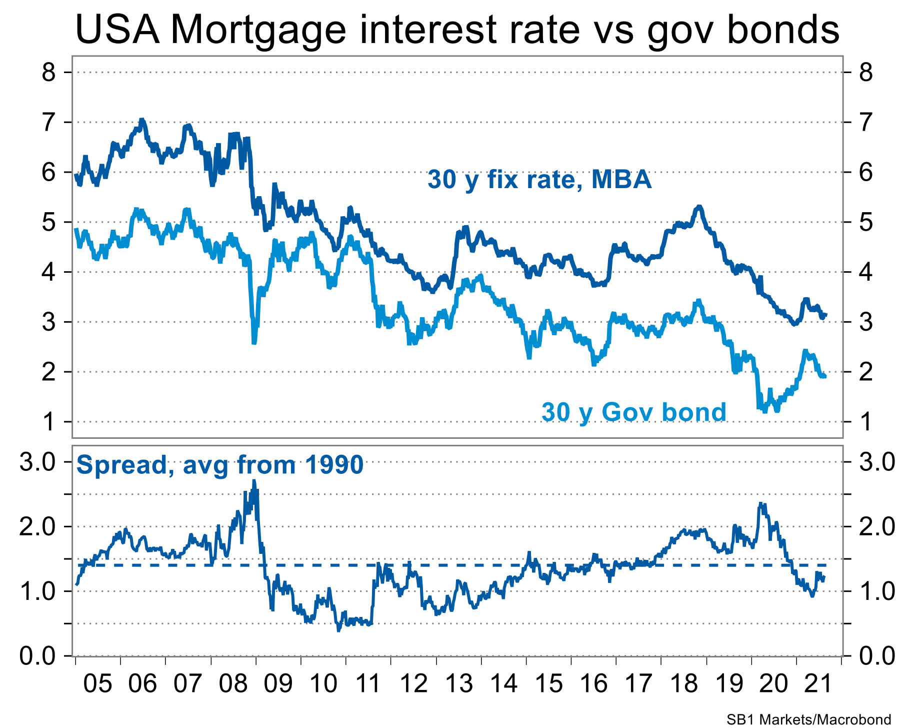


- **Prices** rose 1.1% m/m in July, according to the realtors - marginally faster than in June. Growth has slowed somewhat, the 3 last months prices are up at a 7% – 8% pace
  - » The annual rate fell to 17.0% from 23.4% in June
- **Other price indices** confirm the red hot housing market; prices are rising extremely fast, even after adjusting for the decline/slow growth last spring

Homes are still very affordable, because the mortgage rate is so low!

However, mortgage rates have more or less flattened – and home prices are sharply up

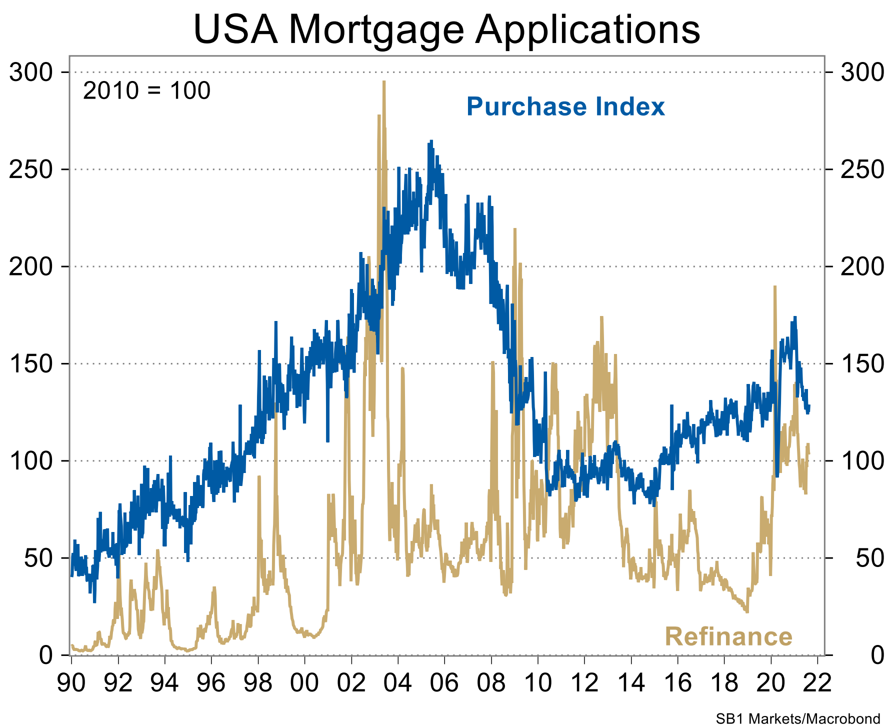


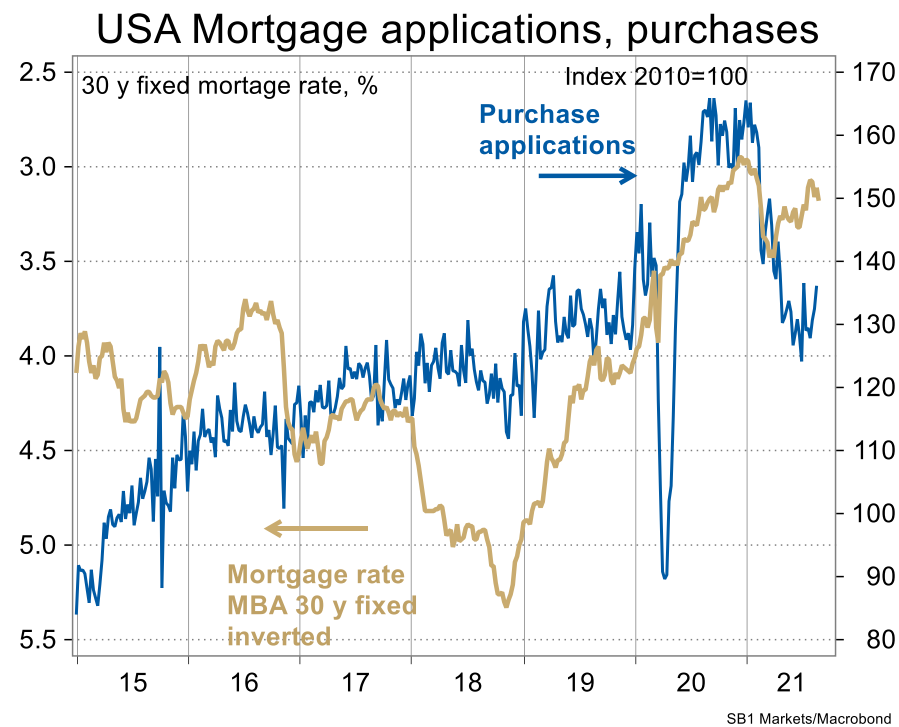


- The lift in prices is felt, no doubt

- **The 30 y fixed mortgate rate** has fallen some 40 bps since March, even if the spread to the 30 y gov bond has increased somewhat
- **Household mortgage** debt is up USD 500 bn y/y. Fed is buying USD 40 bn per month, 480 bn per year. The Fed is funding the housing party, all of it! Cheers ☺

Mortgage rates are down but demand for loans has not yet responded

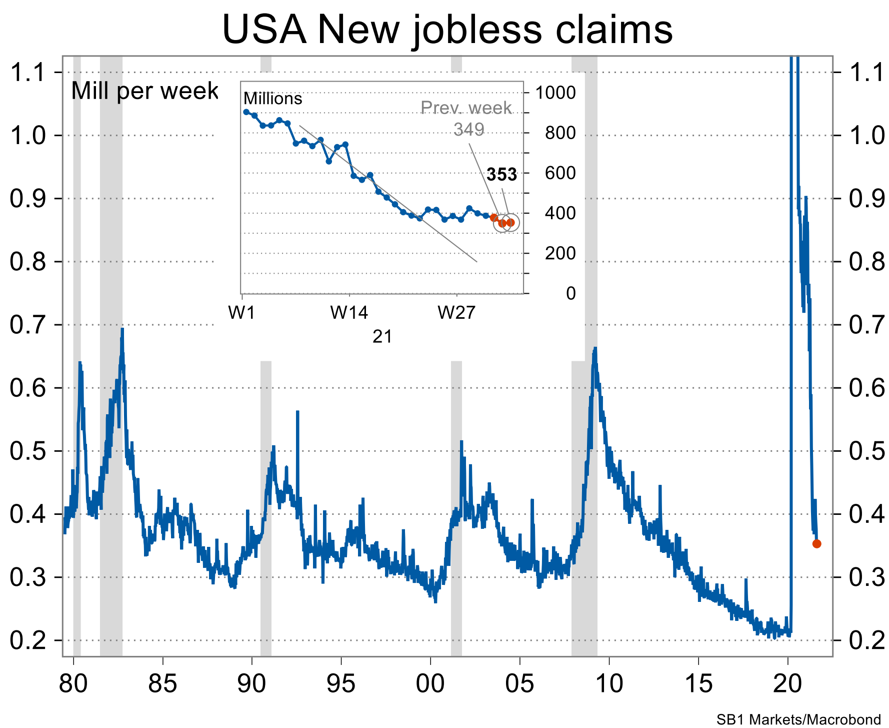


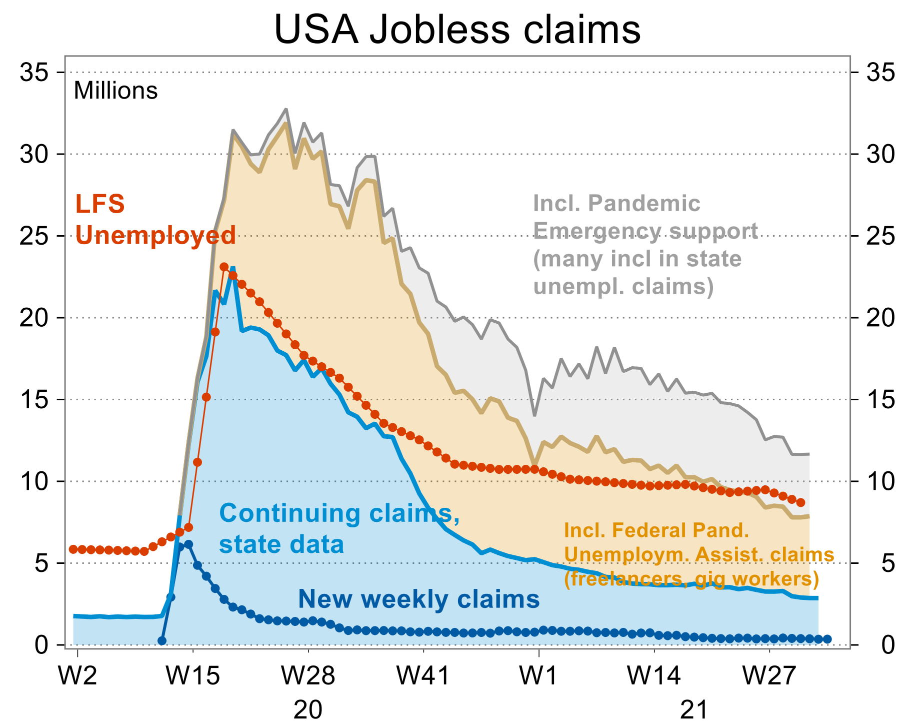


- Demand for new mortgages (for buying, not refinancing) is not closely correlated to mortgage rates but the increase in demand last year was influenced by the steep decline in mortgage rates
- Demand for new mortgages rose marginally last week but has not responded to the 40 bps decline in the 30 y mortgage rate since March – the no. of applications has fallen

New jobless claims marginally up from the week before

The decline seems to have flattened. Puzzling considering the record-high vacancies…

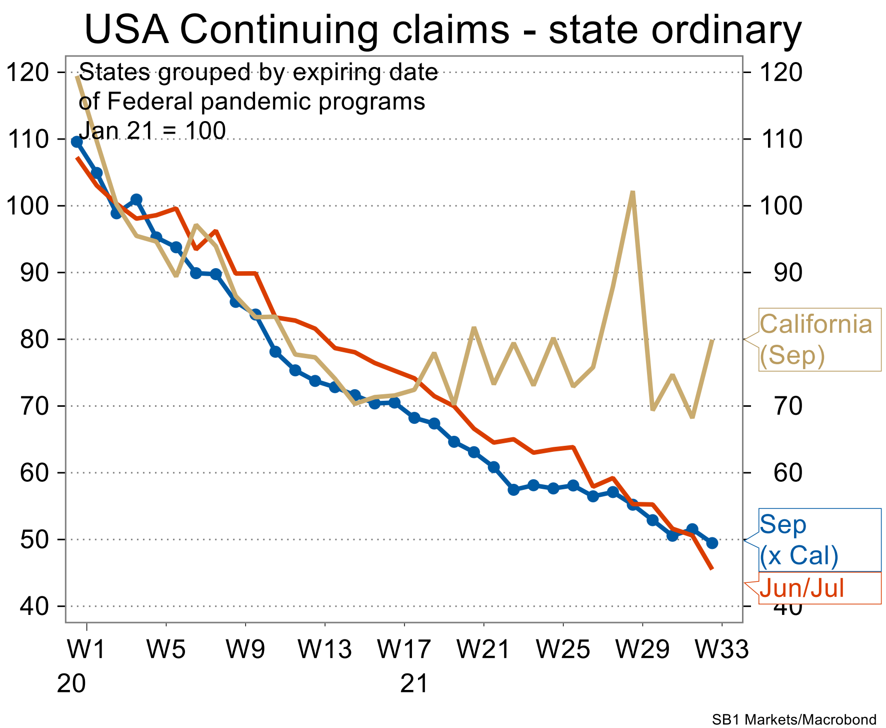


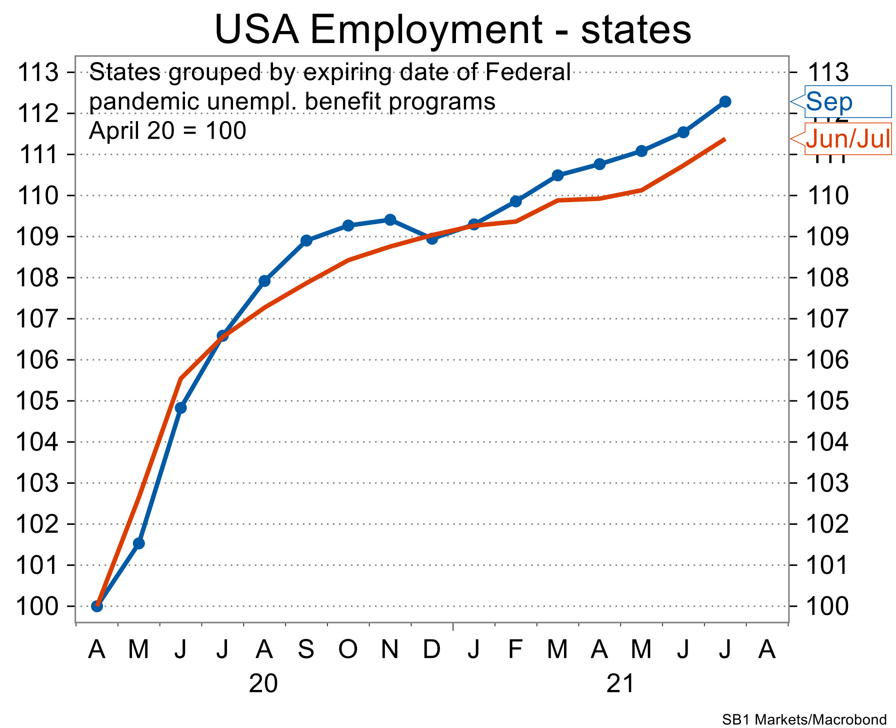


- **New jobless claims rose** by 4' to 353' in week 33 – below expectations at 350'. The inflow is still high given all other indicators of demand for labour – and far above the rapidly declining trend which ruled until 2 months ago
- **Ordinary continuing claims** fell the previous week (week 32), by 3' to 2.86 mill. Over the past 3 months, the no. of recipients have fallen by ¾ mill. **Both the new and ordinary claims numbers for the previous weeks were revised up**
- The number of recipients of benefits from the **two temporary federal pandemic programs** increased in week 31, by 53' to mill to 8.8 mill. By September 6, all the 8.8 mill workers will lose their federal support. What will they then do? More than 3 mill recipients have left these programs the the past 3 months. Many of these workers have probably returned to work as employment is up by 2.5 mill the past 3 months. However, employment has so far not grown faster in the early leaver states than in the stayer states (*check next page*)

Ordinary claims are falling everywhere, except for in California

Still not big difference in no. of receivers of ordinary state unemployment benefits between states

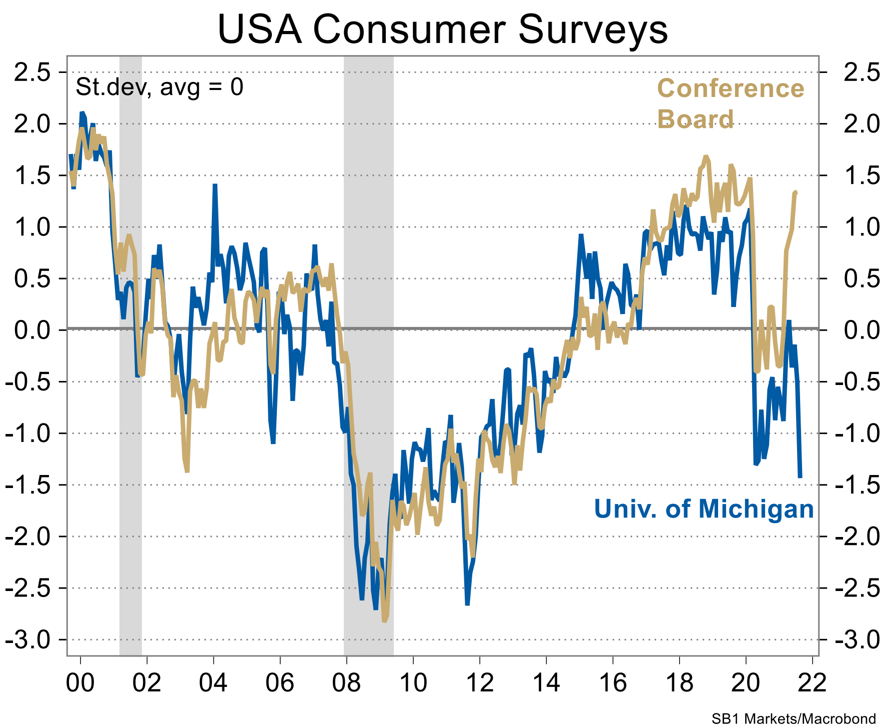




- 4 states dropped out of the federal unemployment benefit programs on June 12 (end of week 23), 8 states left June 19, and 10 states June 26, and 3 more states July 3 and 10 (week 27). The no. of recipients has fallen by 3 mill persons past 3 months
- If we pool the 'early leavers' states in one group, there has been a reduction in number of recipients of ordinary state benefits the past weeks which may imply that those who lost their federal support also leave the 'ordinary' dole. However, barring the volatile Californian data, the decline has been almost the same in states that have not opted to leave before the programs expire next month
- In July, there were no difference in **employment** between early leaver states, and the others
- So the jury is still out: How many of the 8.6 millions on federal support will find a job when these benefits expires Sept 6

Univ. of Mich consumer sentiment confirmed down in the basement in August

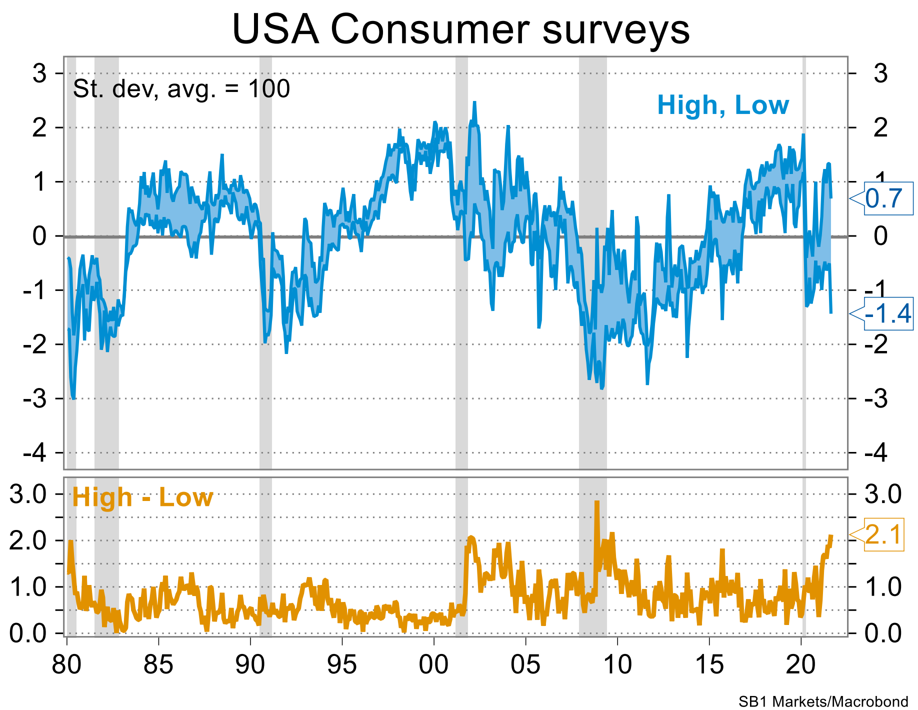
The 1 st.dev decline in August was not revised. Upcoming confidence surveys will be exiting!

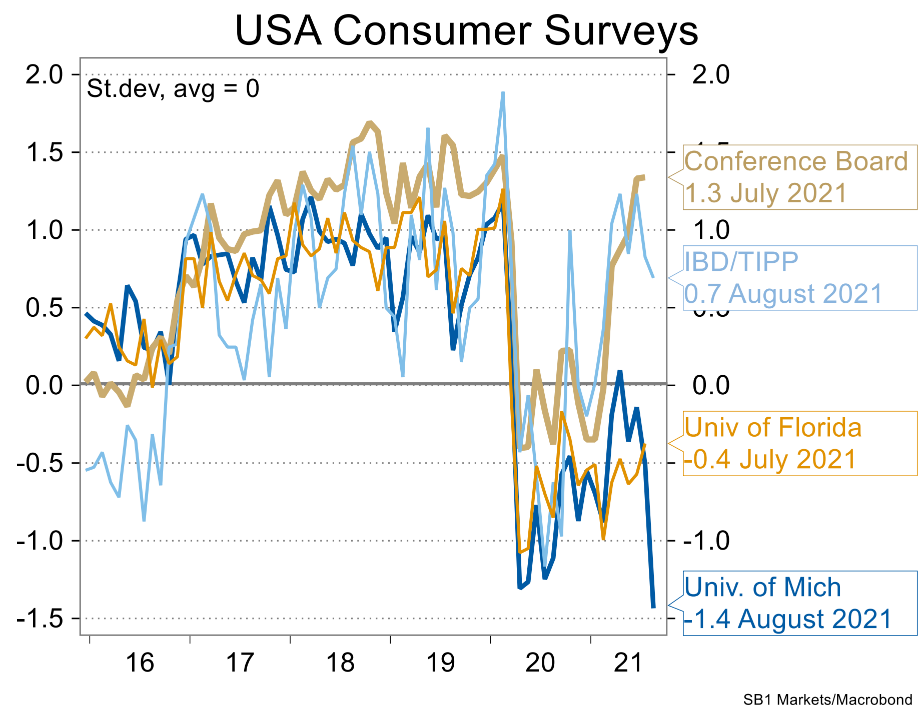


- **The UM sentiment index,** out of the blue, fell by 11 p to 70.2 in August, originally expected unchanged! (The lowest est. on Bloom was 78). The level is the lowest since 2011. The final result was 70.3. The Afghanistan crises had not escaladed when the preliminary data were gathered, and the full month was marginally better than the first estimate
- Our assessment 2 weeks ago:
  - The decline equalled almost 1 st.dev, or ¼ of a 'normal cycle', one of the bigger monthly setbacks (the 7th largest ever). The level is 1.4 st.dev below par
  - **Expectations** fell more than households assessment of the **current situation** but the latter still weaker than the former
- Why this sudden– and totally unexpected – drop in household sentiment?
  - The **virus situation** has deteriorated in most states recent weeks, but nothing like the during previous 3 waves
  - The **stock market** is OK, to put it mildly
  - The **labour market** is recovering rapidly, and jobs are extremely plentiful (also according to households themselves)
  - The **housing market** is still going strong, **mortgage rates** have fallen, and **credit** is available
  - **Gasoline prices** are up but just marginally since April, and they are far from high in real terms
  - **Inflation expectations** are well above a normal levels, but they did not (in sum) rise further in August, and cannot explain the sentiment shock
  - **Republicans** lost confidence much more than Democrats, and the partisan divide is close to ATH, but there have been no political drama in early August?
  - **Other surveys** have not recorded any sudden death – but just one other survey has published August data (IBD/TIPP). The gap between surveys is in reality the largest ever

Conference Board's survey out this week, is expected close to unchanged

If so, the spread to UM's survey would be the highest ever

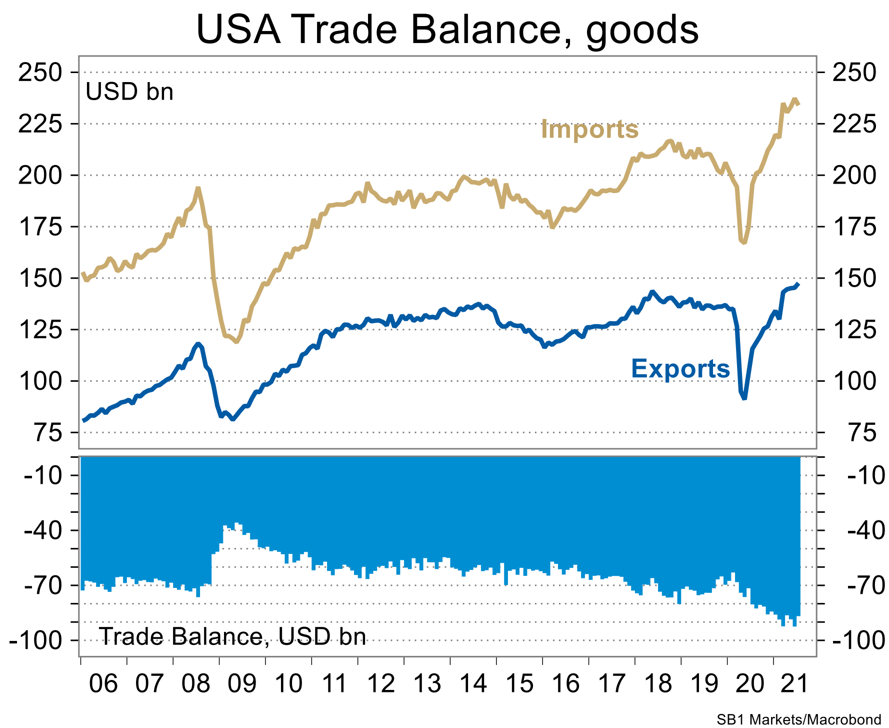


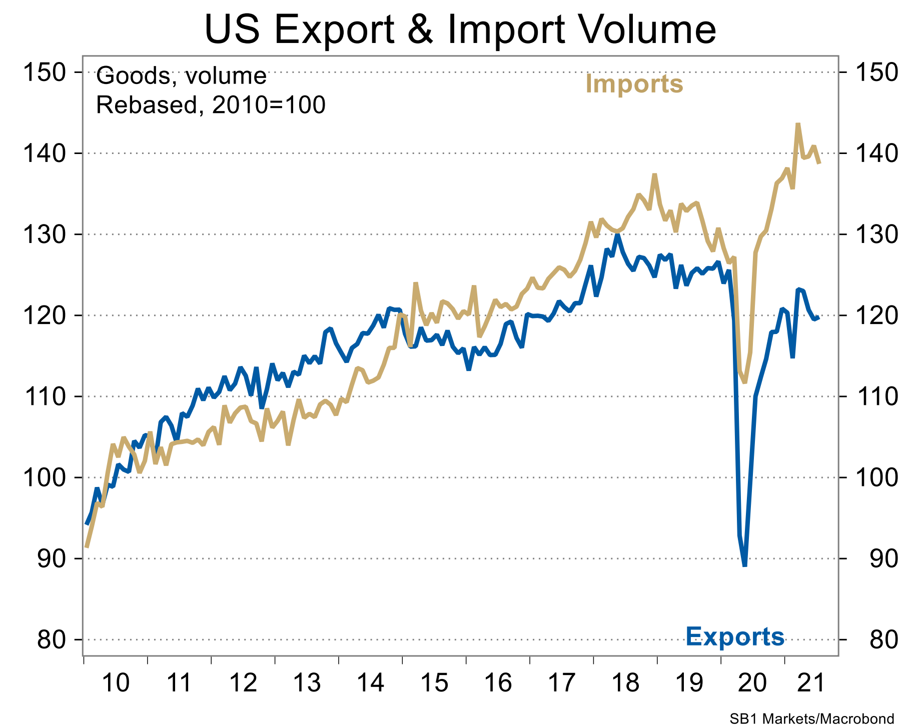


- Sure, the Univ. of Mich. August print could turn out to be a wild shot too – but the UM is far less volatile than the IBD/TIPP survey. University of Florida's survey has been at the weak side since the start of the pandemic, just like Michigan's survey (but no August data yet)
- Conference Board will publish its August survey next week

Imports down, exports up in July

The trade deficit in goods fell by USD 6 bn to 86 bn – expected unchanged

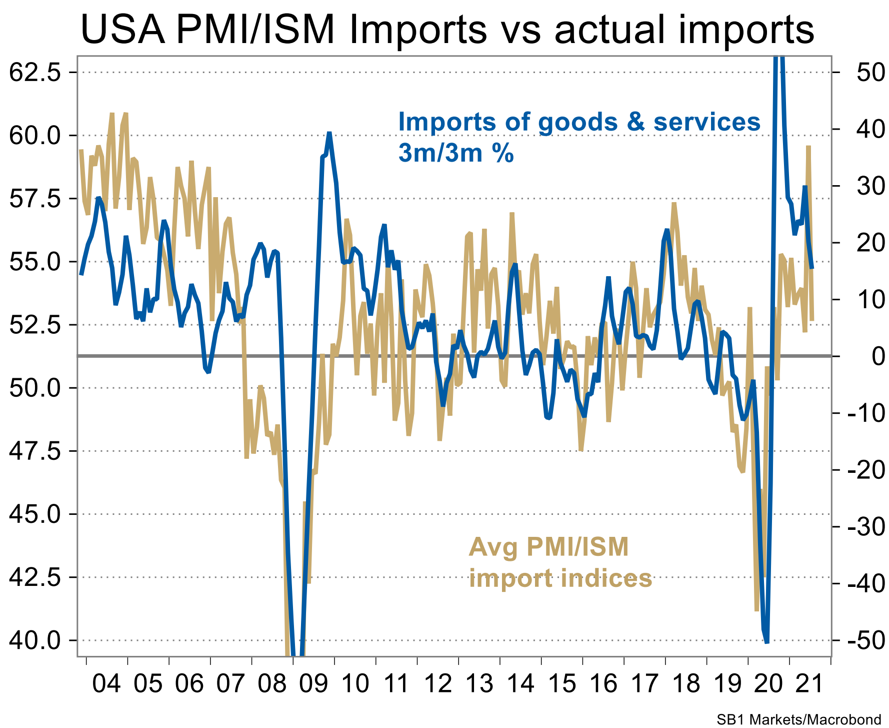




- The monthly changes in July were small
- **Imports** of goods are far above the pre-pandemic level, both in value (-15%) and volume terms (-7%)
  - » Imports have surged due to the rapid rise in demand for goods in the USA, both consumption & investments
- **Exports** are up in value terms (-8.9%), but still down in volume terms (-4%)
- **Global trade** volumes are some 7% higher than early last year – but has flattened the past 2 months

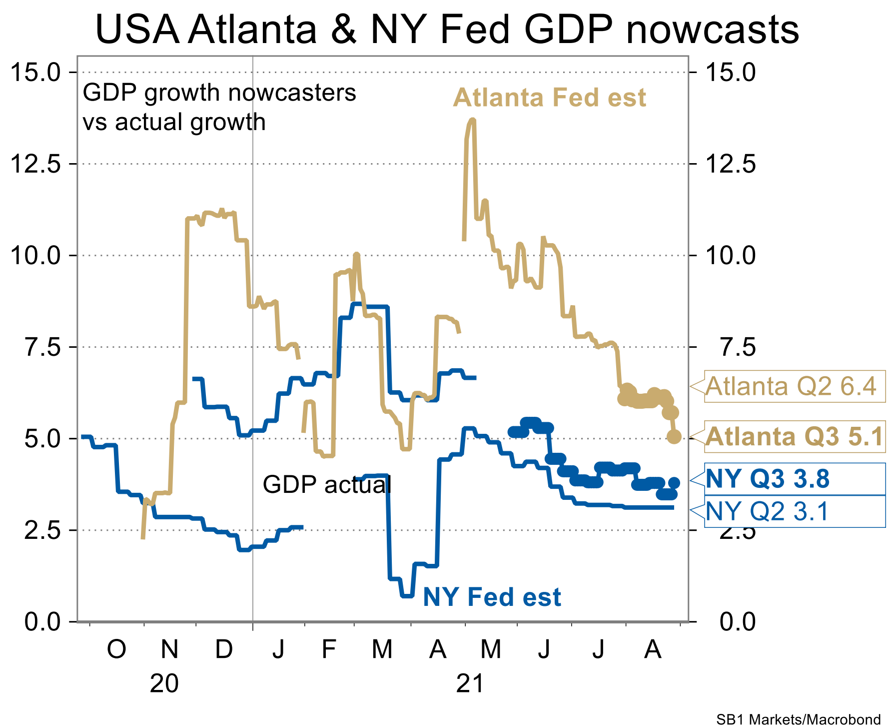
PMI/ISM signal slower growth in imports

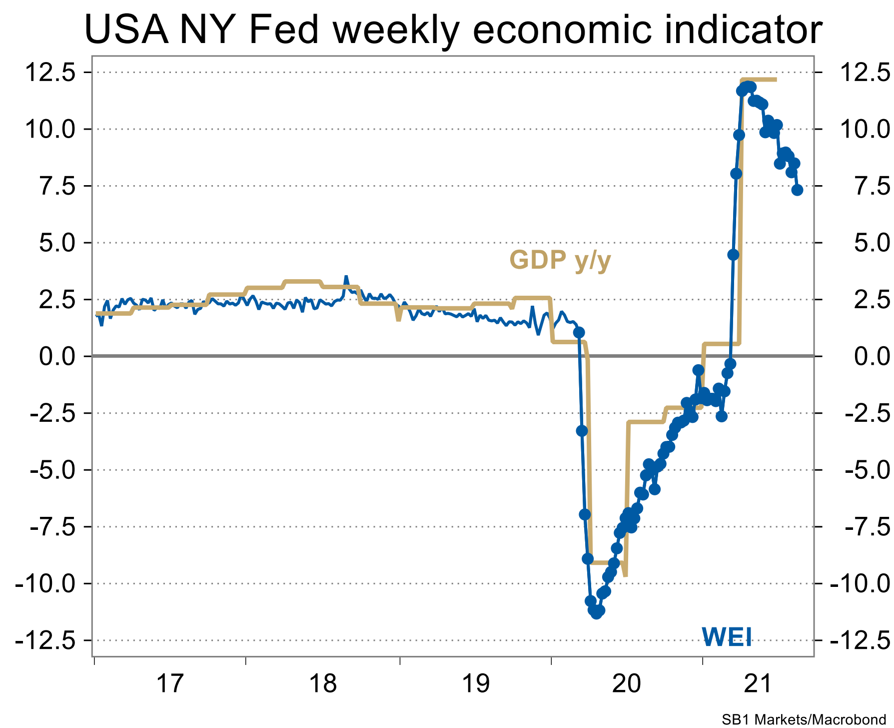
… following the surge. Consumption of goods will have to slow – taking some imports down



- However, actual import have so far kept up quite well

The nowcasters still signal 4% to 6% GDP growth in Q3





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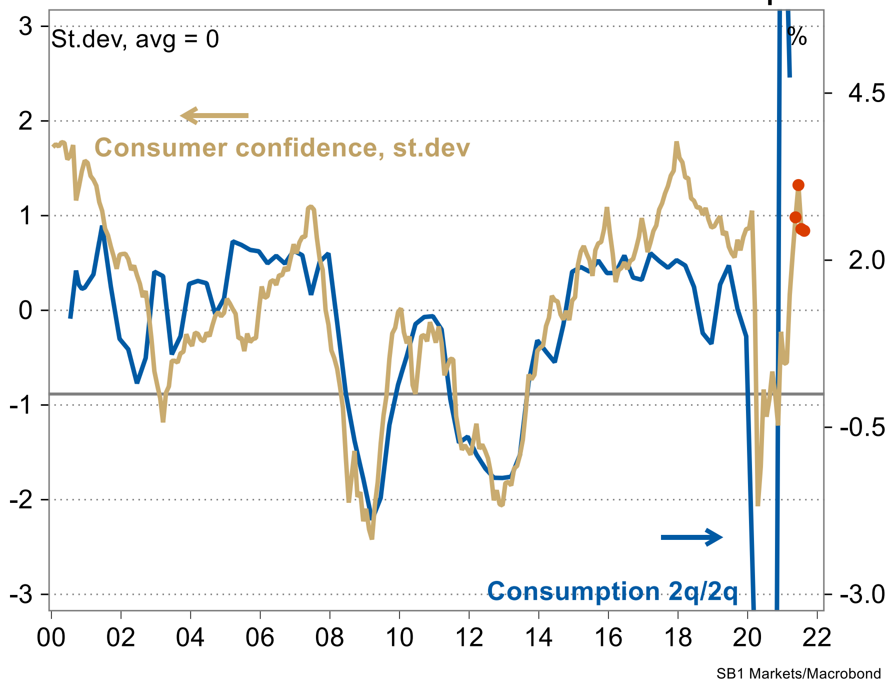
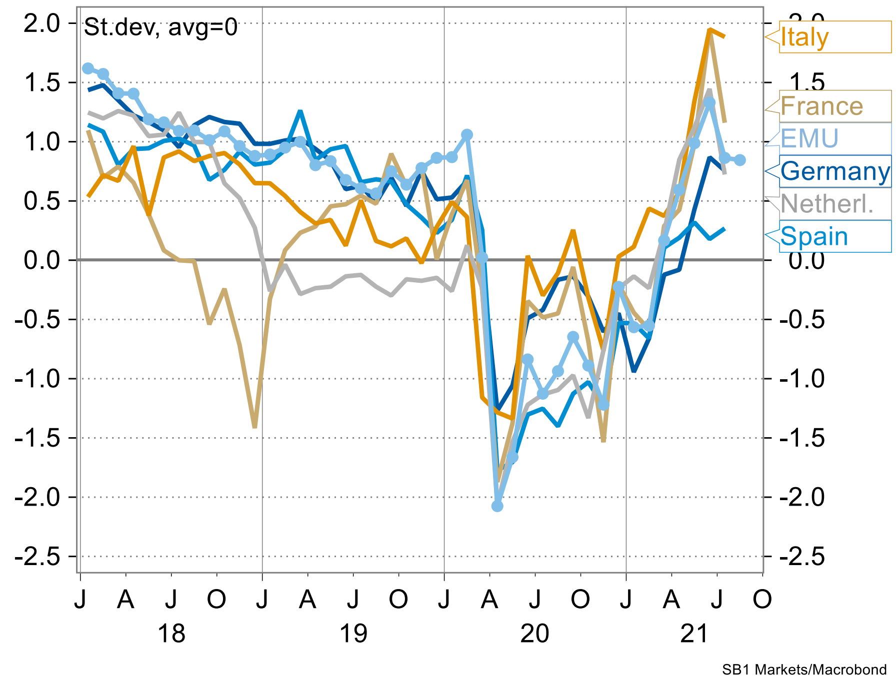
The Delta variant has not killed consumer confidence, level still on par with pre-p

Consumer confidence fell by 0.2 st.dev in August, and the level still 0.8 st.dev above average

EMU Consumer confidence vs consumption

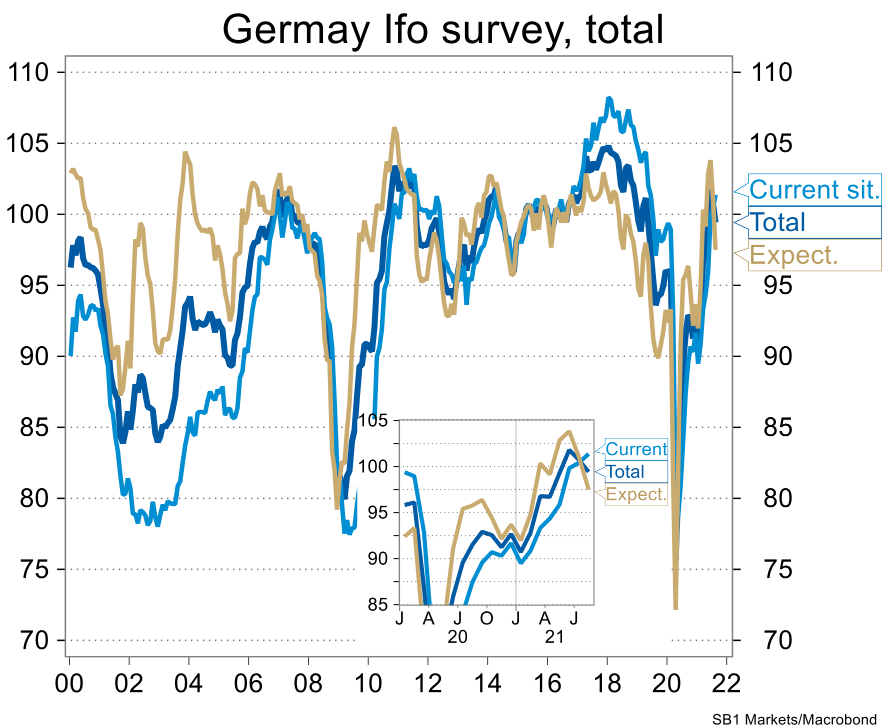


EMU Consumer Confidence



- **The consumer confidence index** decreased to -5.3 in August from -4.4 in July, expected down to -5.0
- Even after the decline, the level is high and does not signal a cut in household demand
- No August country data or details yet
  - » All of the large EMU economies reported confidence above par in July. Italy has been above average since December, and is in the lead

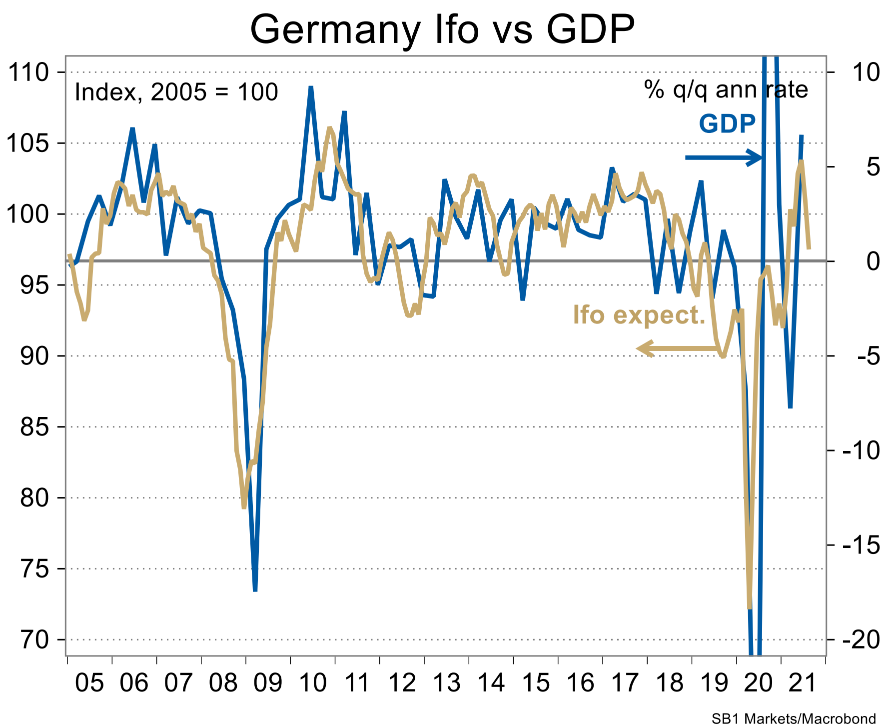
Ifo expectations down in August too. Assessment of current situation further up

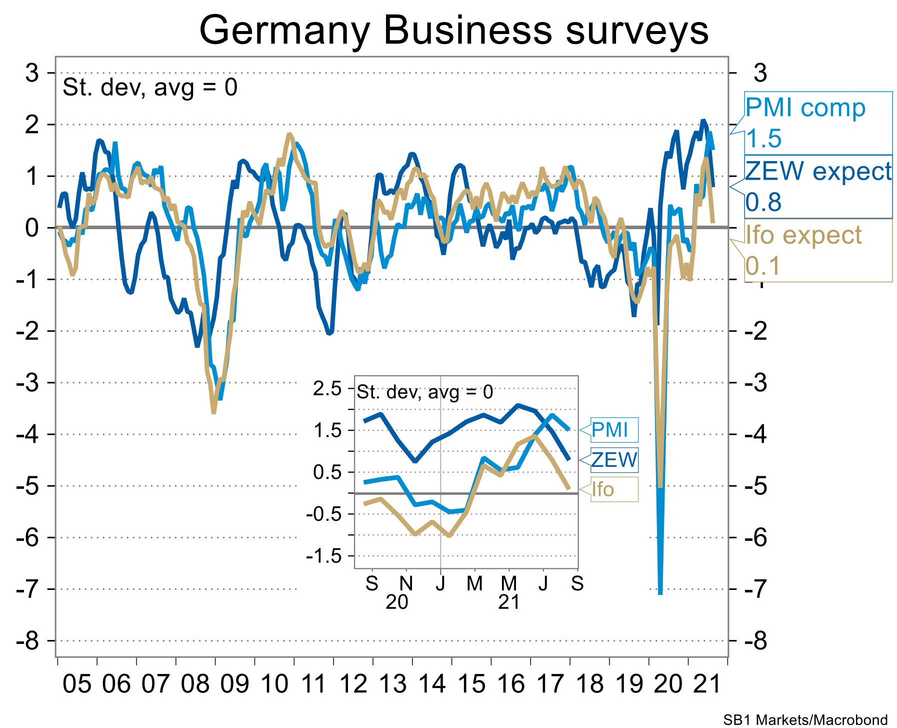


- In August, the **expectations index** fell by 3.5 p to 97.5, equalling 0.2 st.dev from 0.7 st.dev above average
- The assessment of the **current situation** rose to 101.4, up from 100.4 in July – or to 0.9 st.dev above average
- **Manufacturing** business climate (average of current situation & expectation) declined in August, but is still close to the highest level since May '18. The **retail** and **service sector** indices also declined, while **construction** was up. All sectors are reporting activity well above average, signalling growth above average
- **All other German surveys** have come down somewhat recent months – but all are at/above average. They signal some 2%-5% GDP growth rate

By and large, surveys signal growth above trend

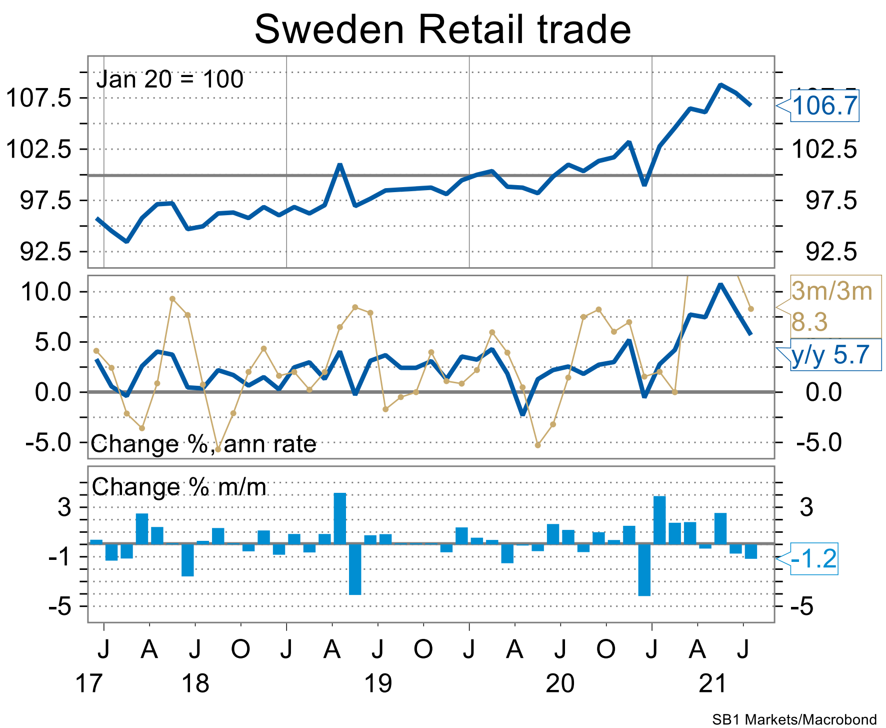
Surveys signal some 2% - 5% GDP growth rate

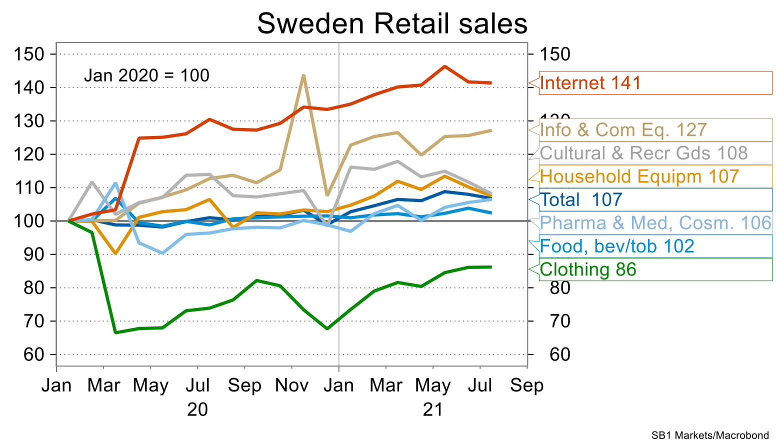


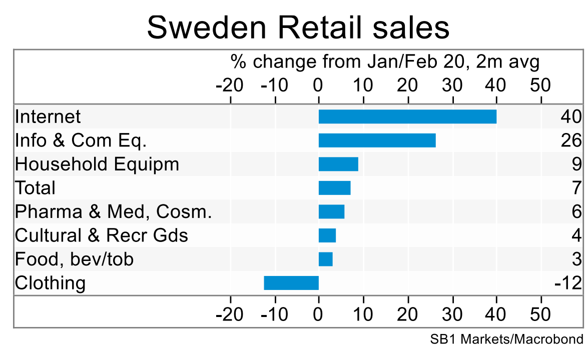


Retail sales down by 1.2% in July – up 6.7% vs pre-pandemic level

Household equipment and recreational goods contributed the most on the downside



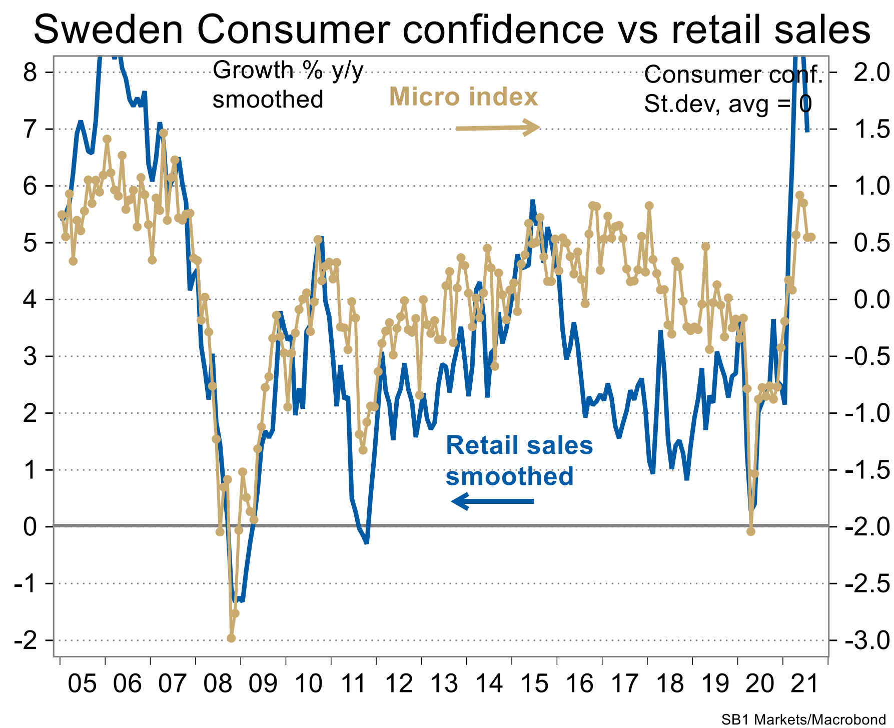


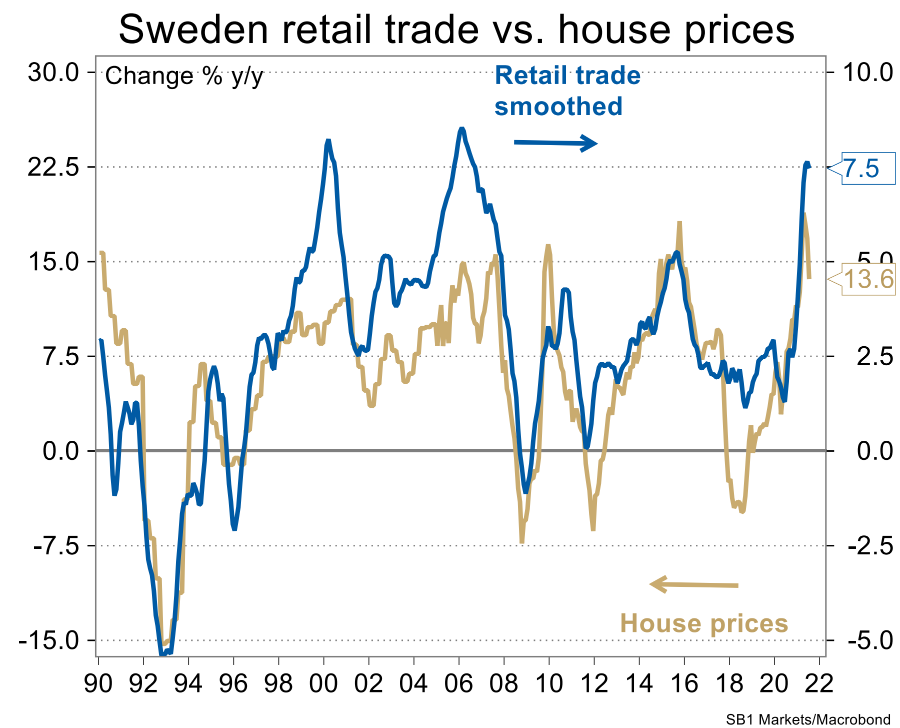


- Sales were expected up 0.5%, following the 0.7% drop in June, revised from -0.3%
  - » Huge sectoral differences. Internet sales up 40% (here like in many other countries), info/communication +26%. Food sales are close to flat, which is strange, given far less activity at restaurants (and Norwegians do not normally buy that much in Sweden, do we??). Also, clothing sales are still down 14% vs Jan-20
- As for Norway and several other countries: Retail sales are very likely above a the long term trend – and will decline as spending on services (and abroad) normalises

Consumer confidence flat/stronger in August

…but retail sales and house prices have taken a breather

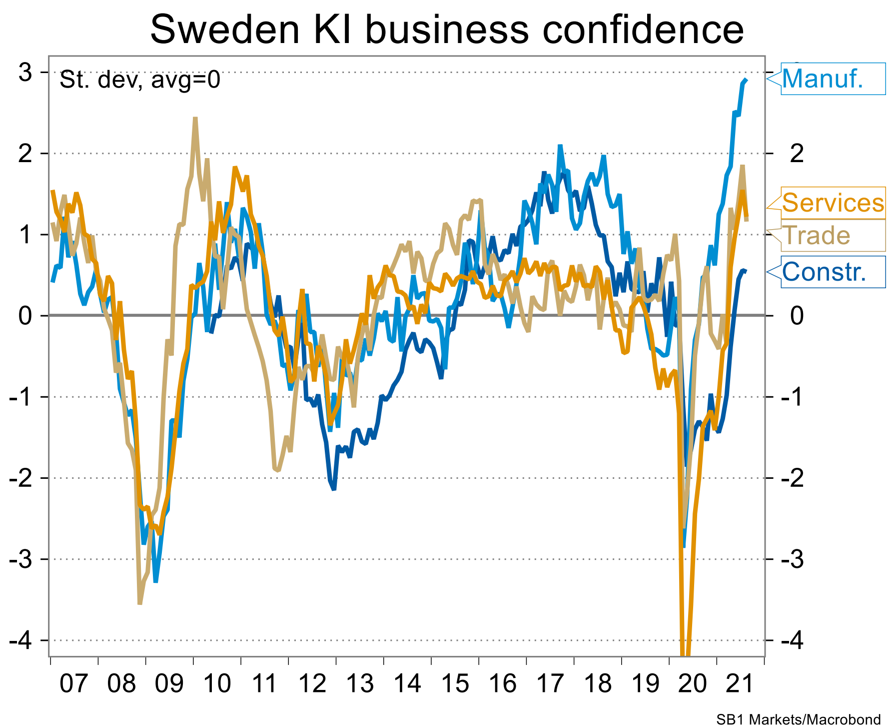


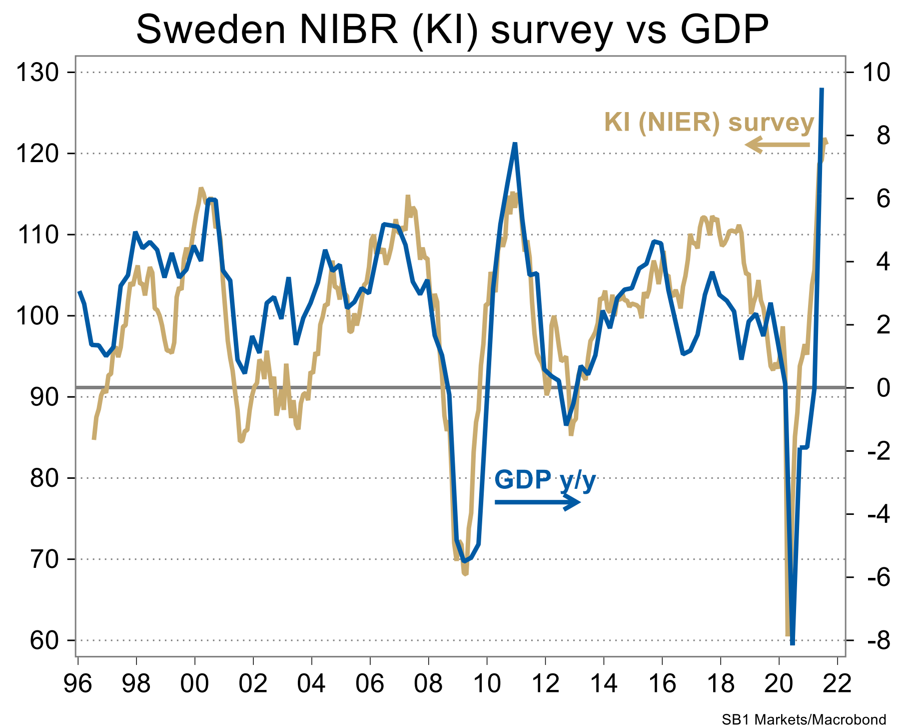


- The **total consumer confidence** index rose to 108.6 in August from 106.2 in July. The 'macro' index fell from a high level, while the 'micro' index rose ever so slightly
- **Confidence** is well above the pre-pandemic level, alongside retail sales - and a booming housing market (house prices up more than in over 30 years), conversely house prices were down in July, and so were retail sales. The fall in retail sales, however, need not be a sign of weakness as the level is still high and people are now able to spend more money on domestic services, as well as travel abroad
- Over the past 4 years, the correlation between stated confidence and actual spending has waned. Even so, during 2020, the relationship may have strengthened. So no reason the expect Swedes to stop spending now

KI business survey marginally down in August, from ATH in July

... and all sectors reporting growth well above trend. Manufacturers in the lead, and further up

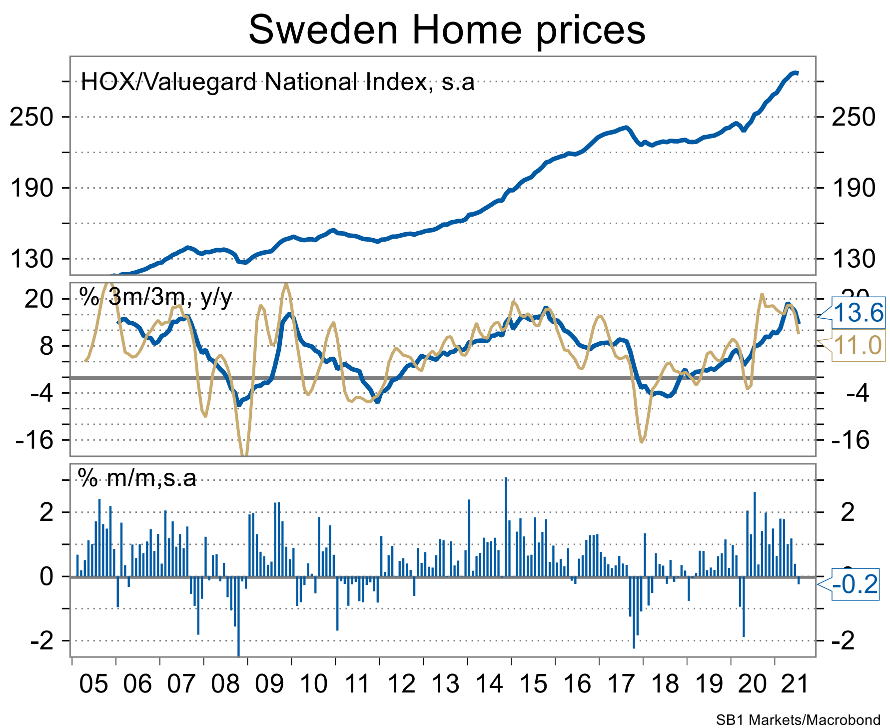


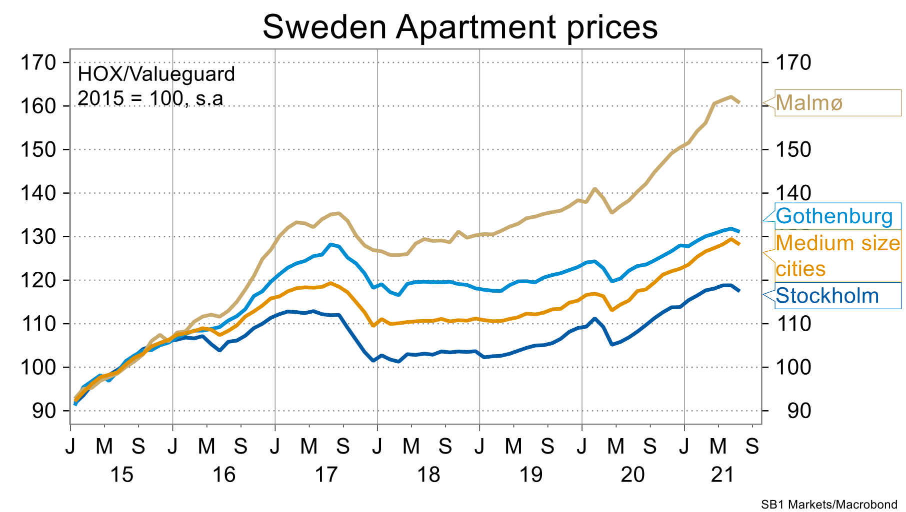


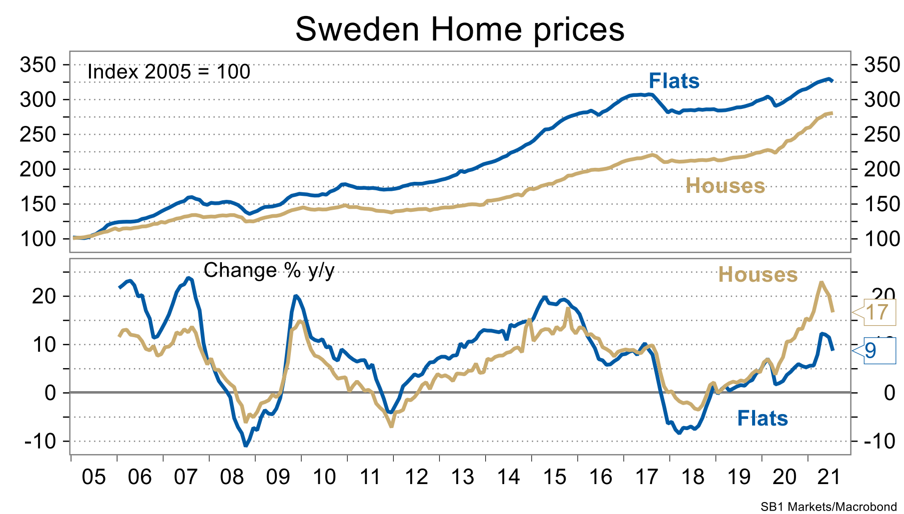
- **The composite index** fell to 121.1 in August from the ATH at 121.9 in July. The survey still signals an 8% GDP growth rate
- **3 out 4 main sub-sectors** contributed to the fall: While confidence among **manufacturers** increased, the services and trade sectors were less confident
- Most likely, growth is now close to peaking as the gap to the pre-pandemic growth path most likely will be closed during H2
- Still the **Riksbank** is still concerned about the impact of the corona crisis, and buys large quantities of government bonds, and thinks it will keep the policy rate at zero forever. At least until well into 2024. If growth calms down rapidly, that may be OK. If not..

Swedish house prices down 0.2% in July, the first decline since April-20

At one stage, house price inflation had to slow down



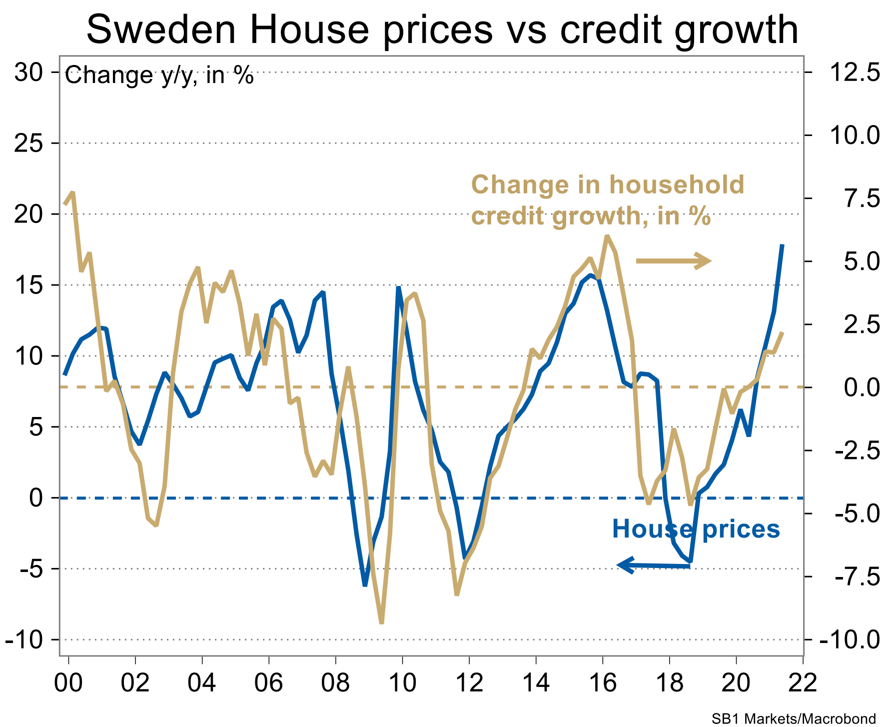


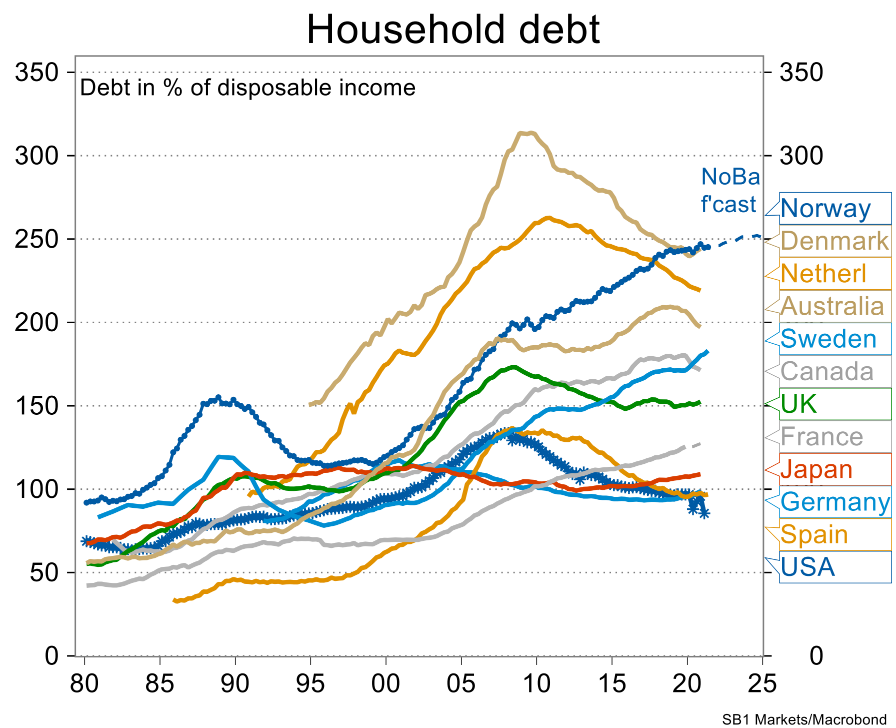


- The annual price inflation fell to 13.6% in July from 16.9% in June. Prices are up 17% from Feb-20, or 12% annualised, a substantial lift
- Apartment prices fell in all major cities in July
- The Riksbank has so far not signalled any change in its monetary policy

Credit growth is accelerating rapidly

… and more than in any other rich country, without cuts in (record low) mortgage rates





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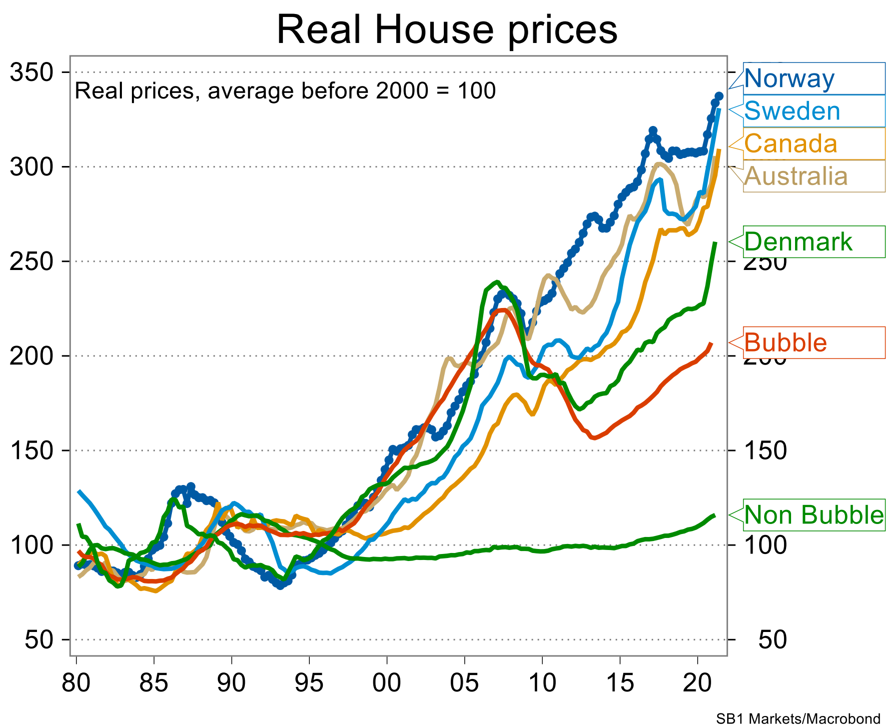
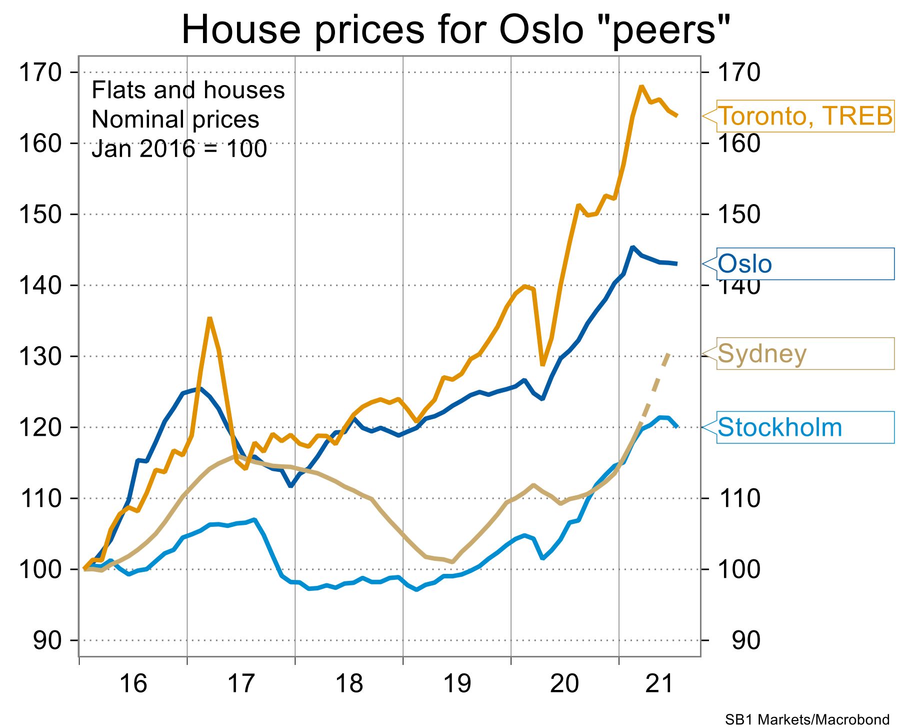
Zero-interest rates are just wonderful! At least for a while

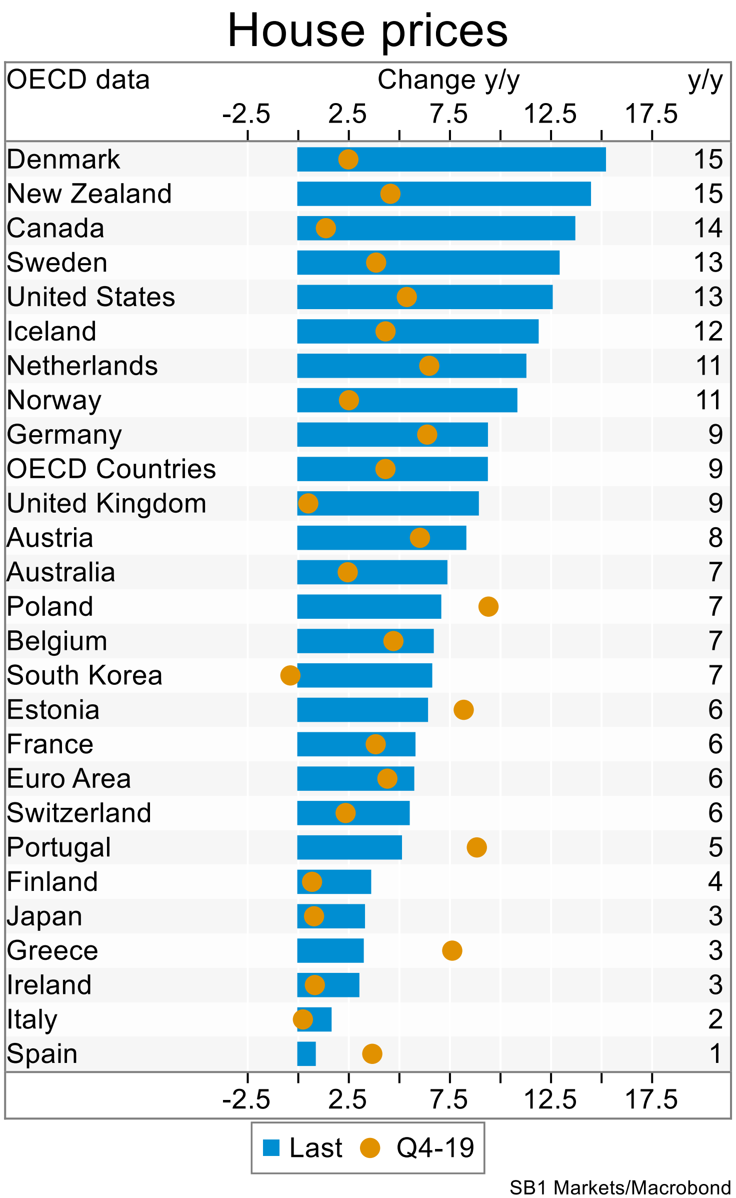
However, now prices are sagging in both Canada and Oslo, alongside Stockholm.





- Real house prices are at high levels in both Australia, Canada, Norway, and Sweden
- Home prices in the capitals in these countries are mixed recent months, as Oslo and Toronto and now Stockholm have taken a break – but Sydney is probably still on the way up

House prices up everywhere, and have accelerated in 21 of 26 countries

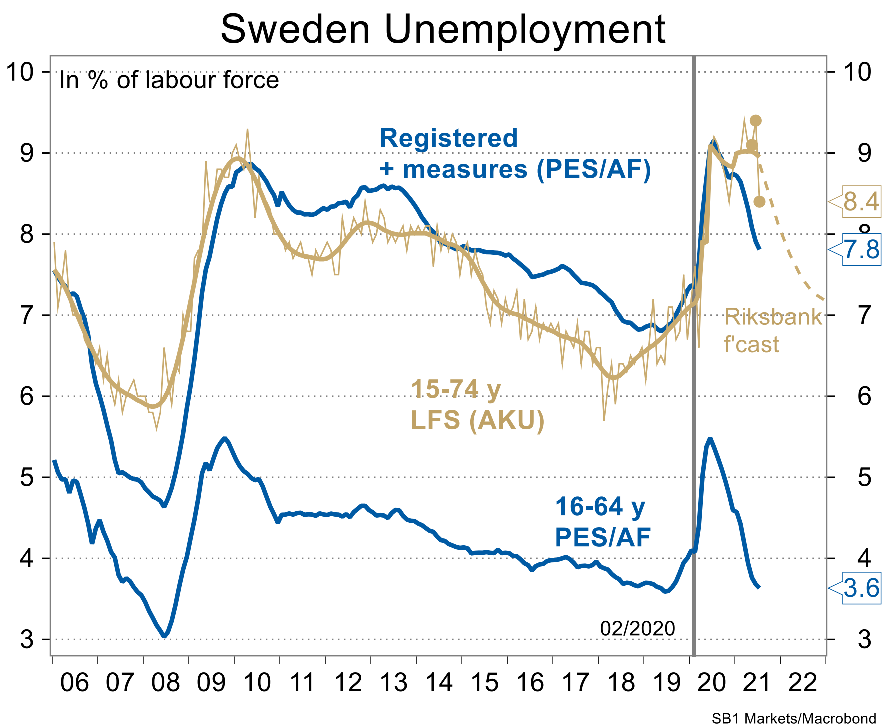


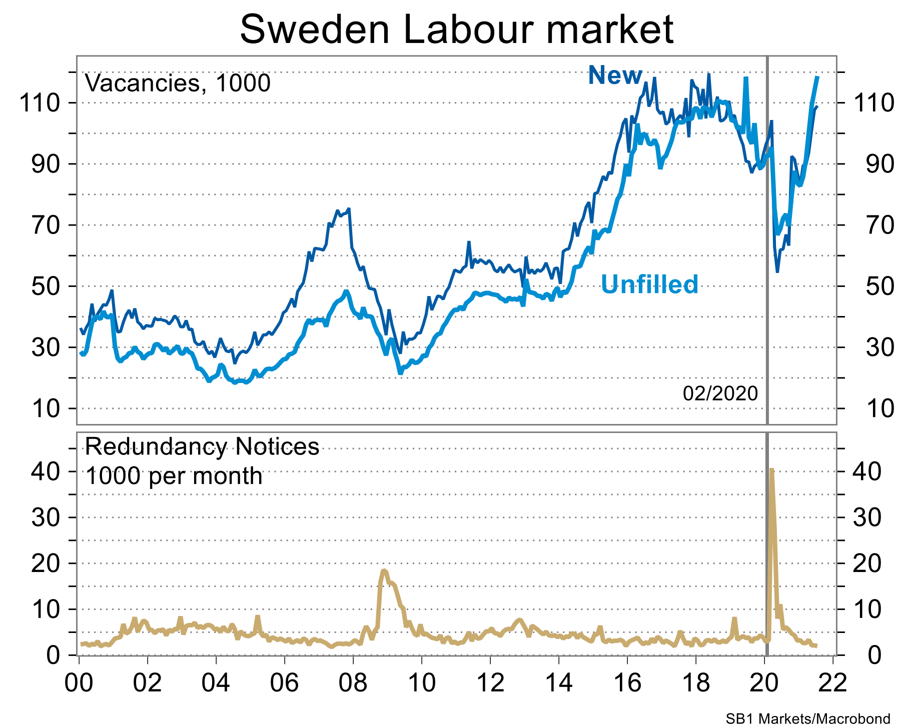
- The average price appreciation in the OEDC area was 9% in Q1, up from a 4% before the pandemic
- Denmark, New Zealand, Sweden and Norway have reported the steepest acceleration vs. pre-corona growth rates
- Price inflation has slowed the most in Greece, for good reasons – the tourist country has been through a harsh downturn. The house market in Spain has been hurting, for the same reason

OECD quarterly data, the last quarter Q1 or Q2-21

'Useless' LFS unemployment stats: unemployment down 1 pp to 8.4% in July

However, indicators in sum signal a rapid recovery of the Swedish labour market

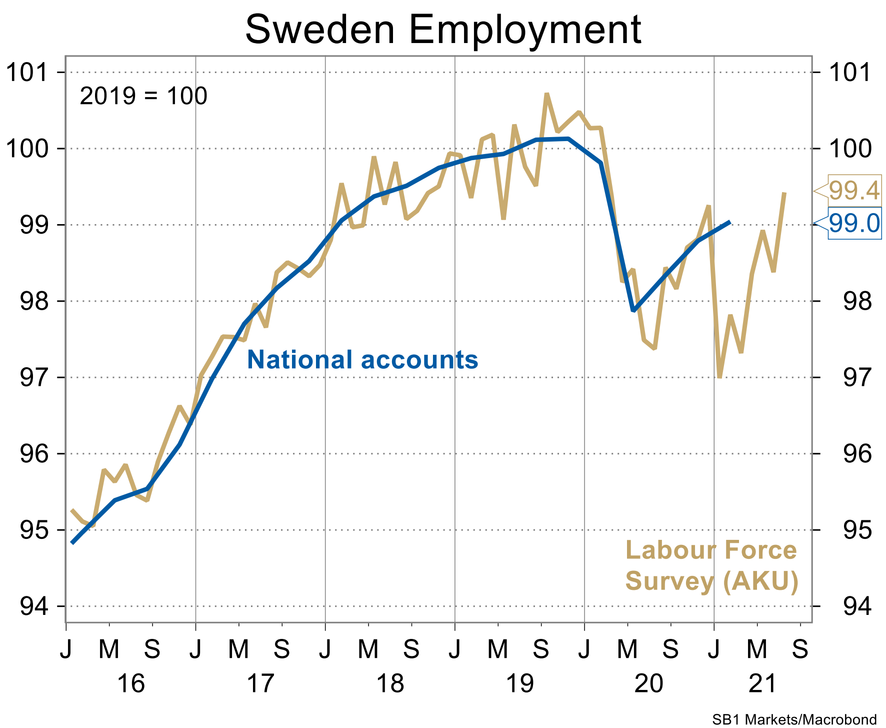


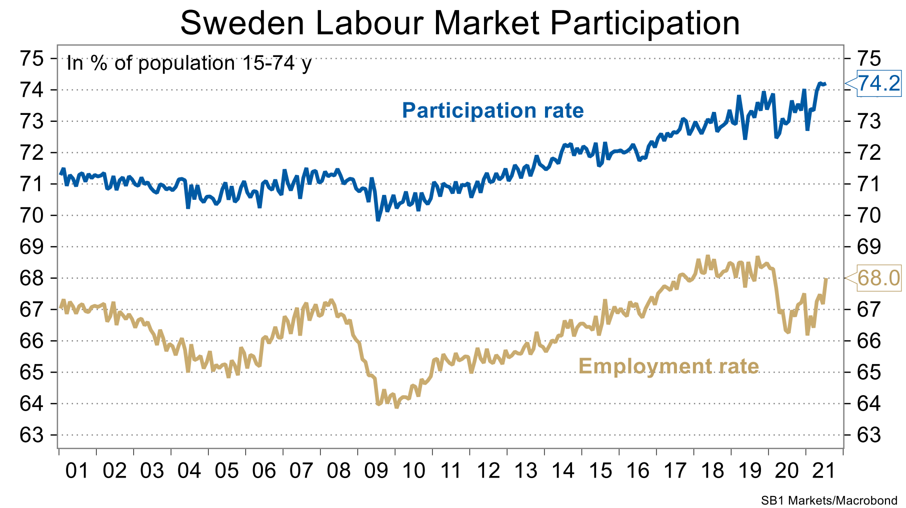


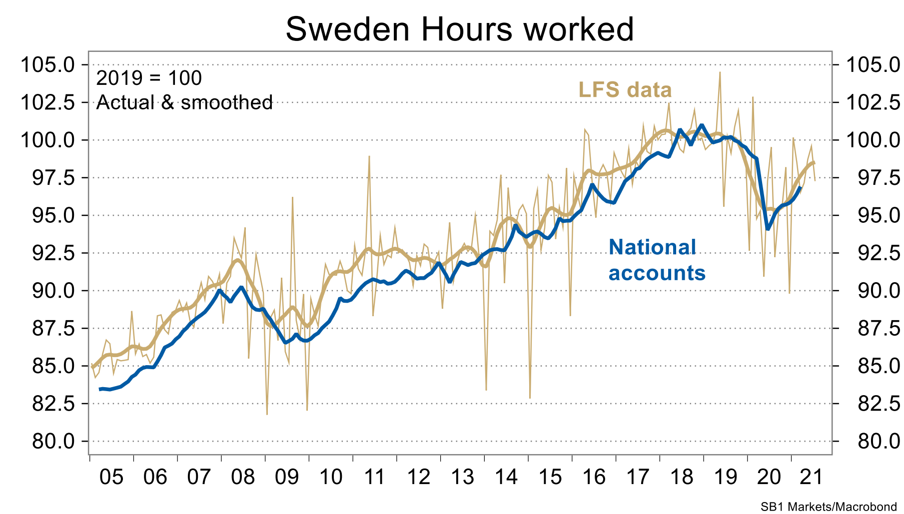
- LFS (AKU) unemployment rate was 'too high' in June, and may be 'too low' in July. The quality of the 'new' LFS is not good – and data have always been volatile during the summer months. Most likely, the LFS unemployment rate is now on the way down – and employment is on the way up, *check next page*
- **Registered 'open' unemployment** (PES/AF) has fallen rapidly since last June, and currently stands at 3.6%, 0.1 pp lower than in June and below the pre-pandemic level at 4.1% (and down from 5.5% at the top)
  - **Incl. labour market measures**, PES/AF unemployment is declining rapidly too - but somewhat less than open unemployment. The rate fell by 0.1 pp to 7.8% in July, but the level is still 1 pp above the early 2020 level
- The number of **new and unfilled vacancies** rose further, and **layoffs** were down in July. The inflow of new vacancies are equal to the very high pre-pandemic level, while the no. if unfilled vacancies is higher!

Employment probably less than 1% below the pre-pandemic level

… and hours worked less than 2% below, both trending rapidly upwards







- Employment is very likely down less than 1% from before the pandemic in Q2, vs the 1% shortfall reported by the national accounts in Q1
- Hours worked has recovered substantially vs last spring, and are still on the way up - and are now 1 - 2% below the pre-pandemic level (but further below the long term trend)
- In July, a steep increase in the employment rate explained the large decline in the unemployment rate. The participation rate is close to all time high!

Highlights

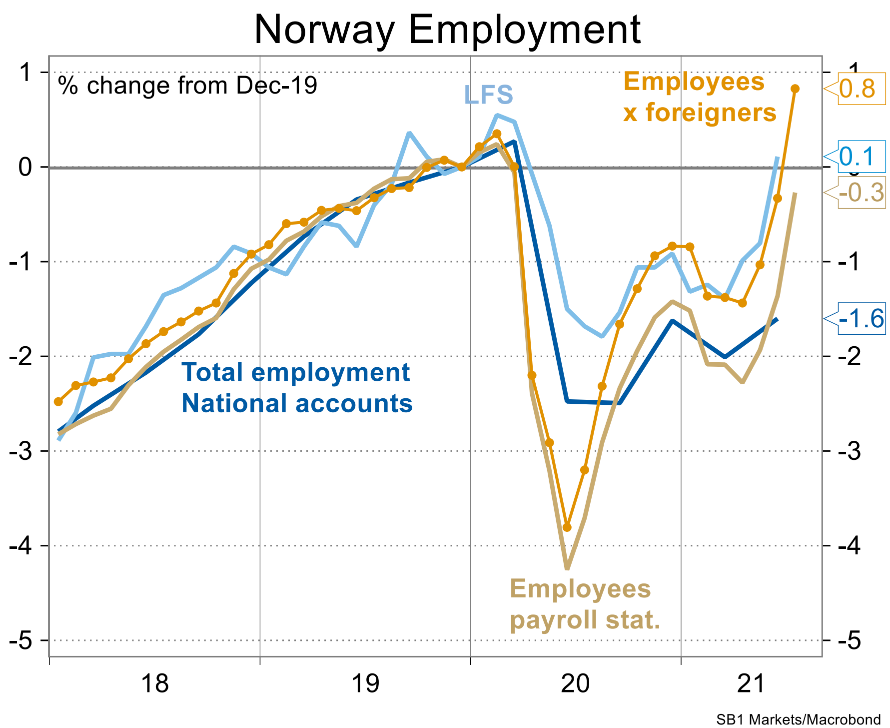
The world around us

The Norwegian economy

Market charts & comments

Employment surged by more than 1% in July (from June!)

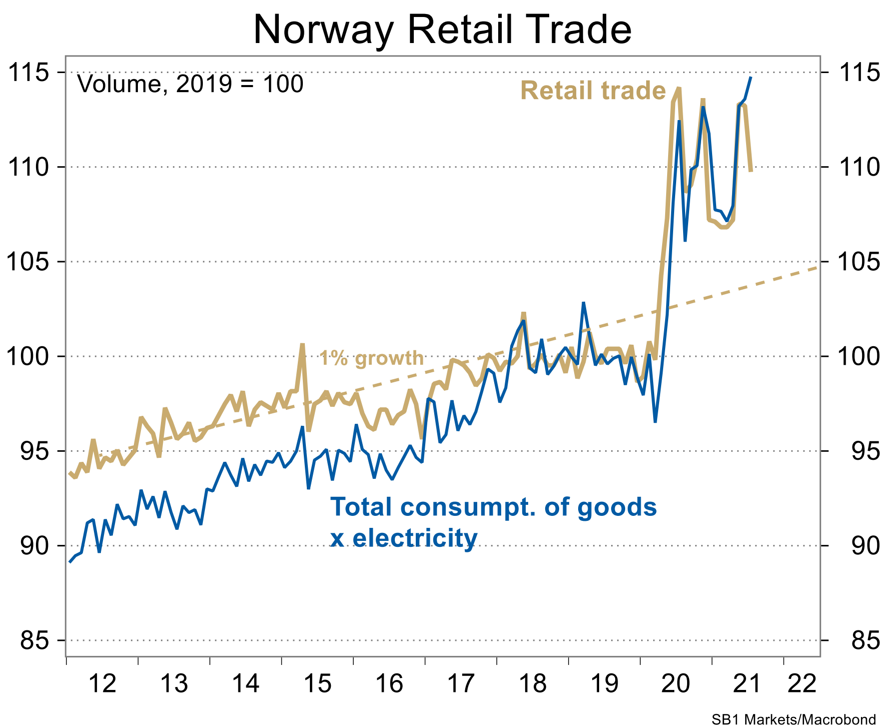
The no. of employees rose by 1.1% m/m in July, and is just 0.3% below Dec-20. Domestic empl. +0.8%

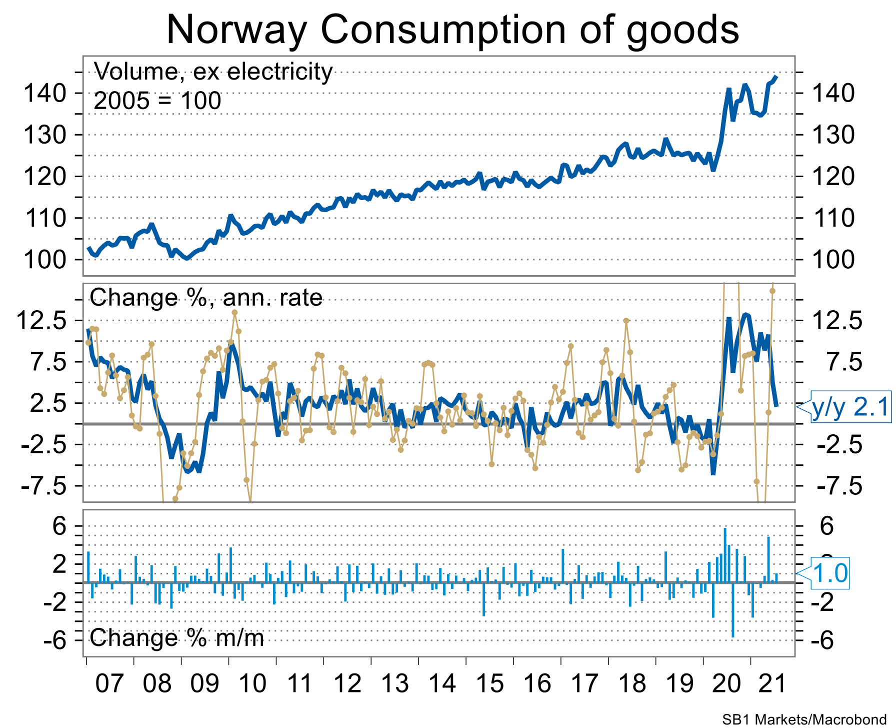


- The increase in employment in July suggest at brisk growth in Mainland GDP
  - » We do not have data for foreign workers on short-term stay for Q3, and 'domestic employment' (Norwegians and foreigners on permanent stay) in July is a estimate but probably not too far from the mark
  - » In June, employment grew by 0.8%
- **The LFS** (survey) employment data have also been strong recent months, the last data point is the April-June average
- **National Accounts** reported a modest rise in overall employment in Q2, and the level was still 1.6% below Q19. The NA data includes foreigners on short-term stay

Retail sales of building materials down 18% but consumption of goods further up

Total retail sales fell 3.1% (we expected -0.5%, consensus -0.4%), but consumption up 1%

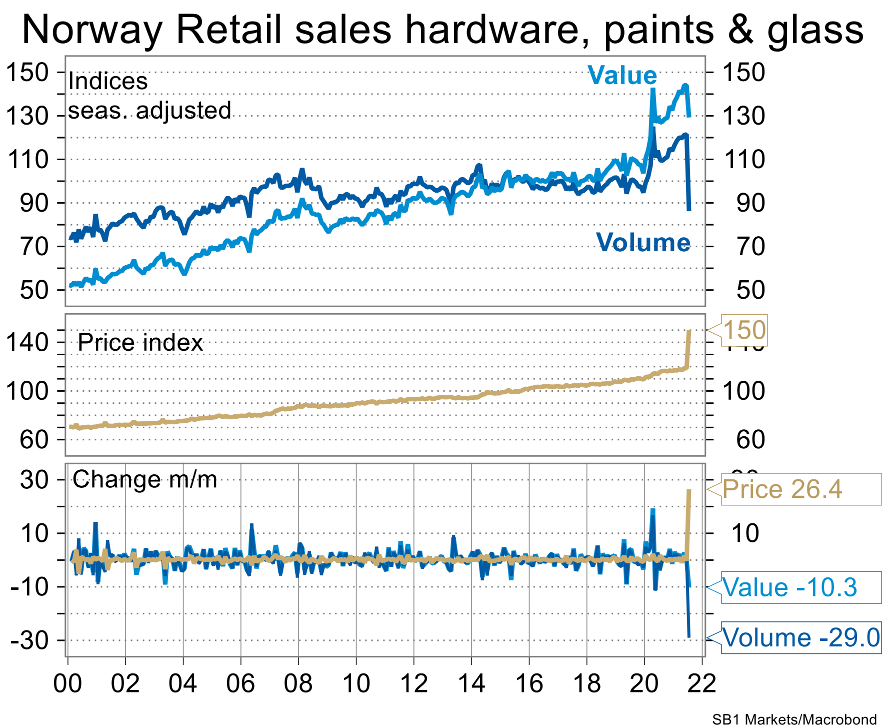


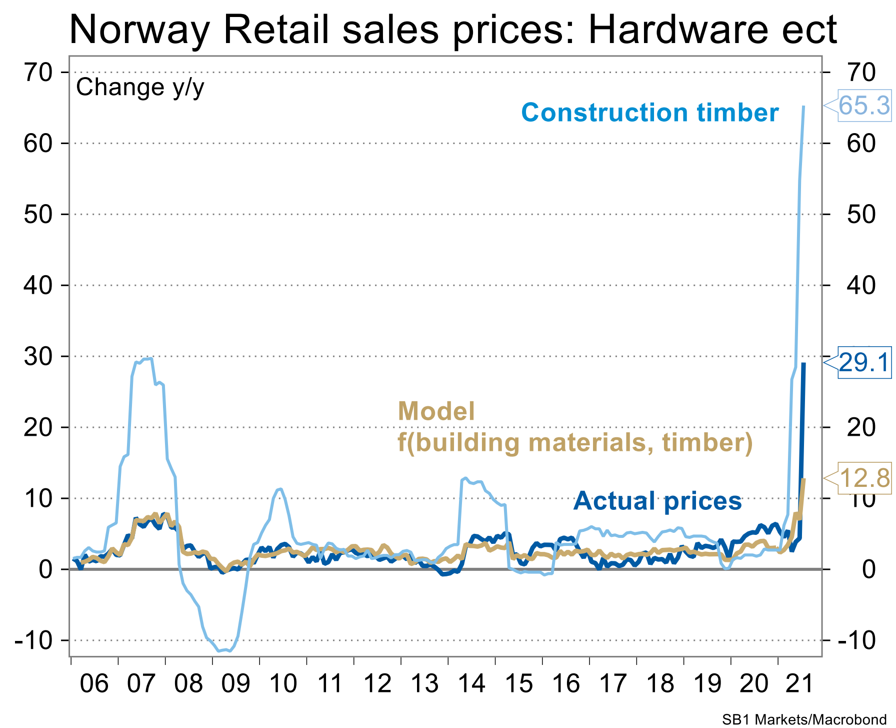


- **Retail sales** were down 3.1% m/m in July – far below expectations. Sales are still 10% above the pre-pandemic level
  - The steep decline in retail sales were exclusively driven by a 29% drop in the sales volume of **building materials, and other hardware**. Prices rose 26%, and sales fell 10% in value terms. The decline is in the sales volume is probably both due to lack of supply and reduced demand due to the unprecedented price hike (which may be somewhat exaggerated – more on that next page)
- **Total consumption of goods** (x electricity) still rose by 1% in July! We have never seen such a discrepancy m/m (when adjusted for auto sales, which are not included in retail sales). Thus, household demand rose further in July, even if retail sales fell
  - The reason is differences in weighting in the retail trade vs the private consumption index. Building material etc constitutes approx. 8% of retail sales. However, a large proportion of these sales are not sales to consumers but rather to professionals, like home builders, carpenters. In the goods consumption index just direct sales to consumers are included. The building material/hardware weight in total goods consumption may be below 1% (no exact data published, but the share in the CPI is low)
- **We still expect sales/consumption of goods** to slow further in the coming quarters, back the pre-corona trend path – when it becomes possible to spend more on services and abroad, both x-border shopping in Sweden and holiday travel in general

An unprecedented decline in sales of hardware/building materials

Volumes down 29% - and the value down 10%. Lack of supply + weaker demand as prices rose 26%

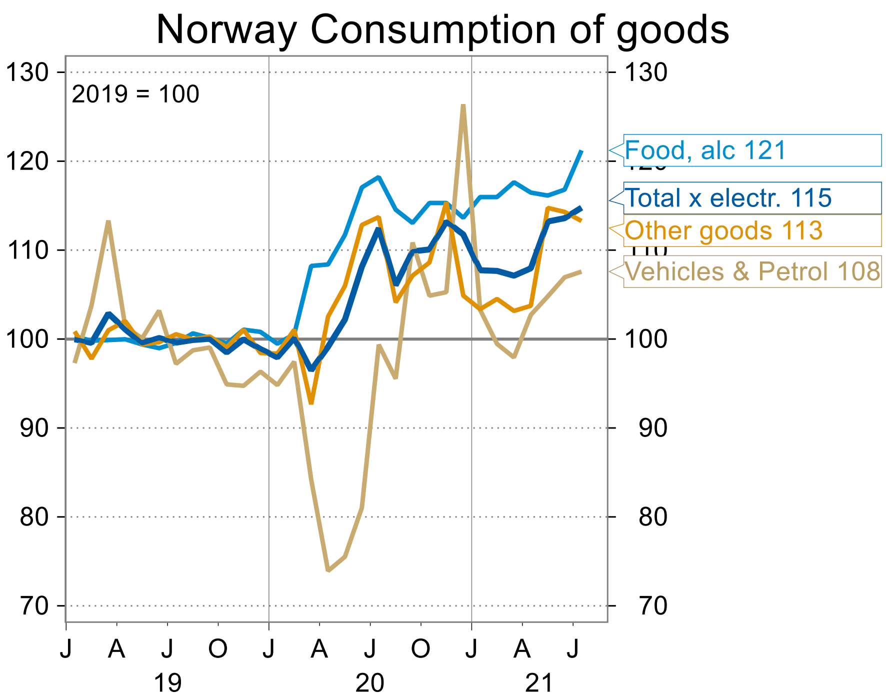




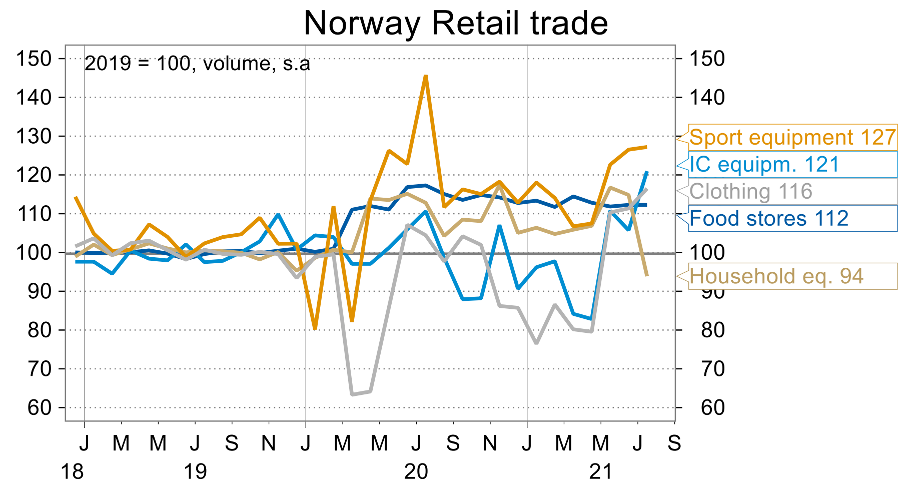
- There have been media reports on lack of supply of timer and other building material. The price hike has also trimmed demand
- The estimated price hike at 26% m/m, without any pre-warning the previous months, seems too high, vs reported price increases for building materials, timber included (but SSB insists the data are double-checked). Prices are up 29% y/y, our model suggests 13%
  - » In the CPI, prices for goods for maintenance of dwelling shot up 35% in July, and is up 44% y/y – which 'explains' the lift in the retail price index, but were are not able to replicate these index either, by utilising the normal suspects (building material costs, timer)
- We suspect that hardware prices at least should have been more gradually adjusted but some of the input prices are not collected each month. It that's the case, sales volumes have fallen more gradually that the 29% drop m/m in July
- US timber prices have collapsed past two months – which should contribute to a normalisation of timber prices in Europe/Scandinavia too. Other material prices are up, but not that dramatically as timber prices

Household equipment down 18.2% in July, due to the 29% drop in hardware etc.

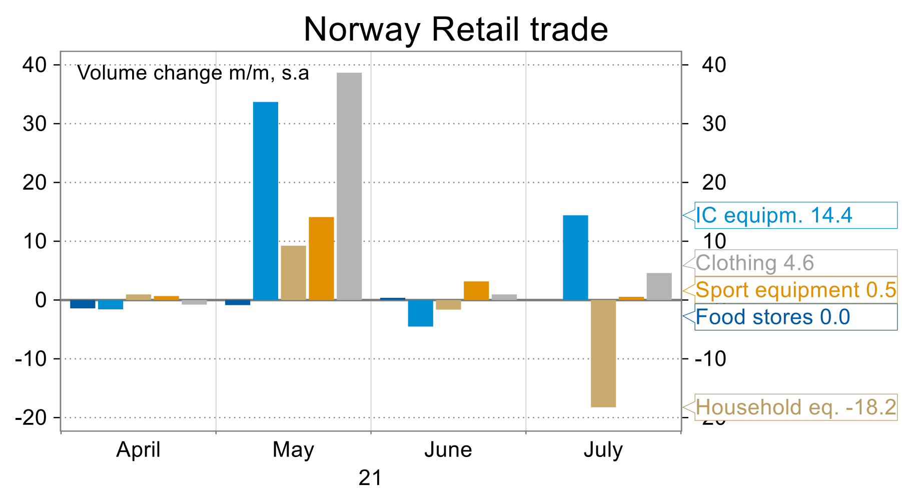
Other sales OK in July, sport slightly up, info/comm up 14%



SB1 Markets/Macrobond



SB1 Markets/Macrobond

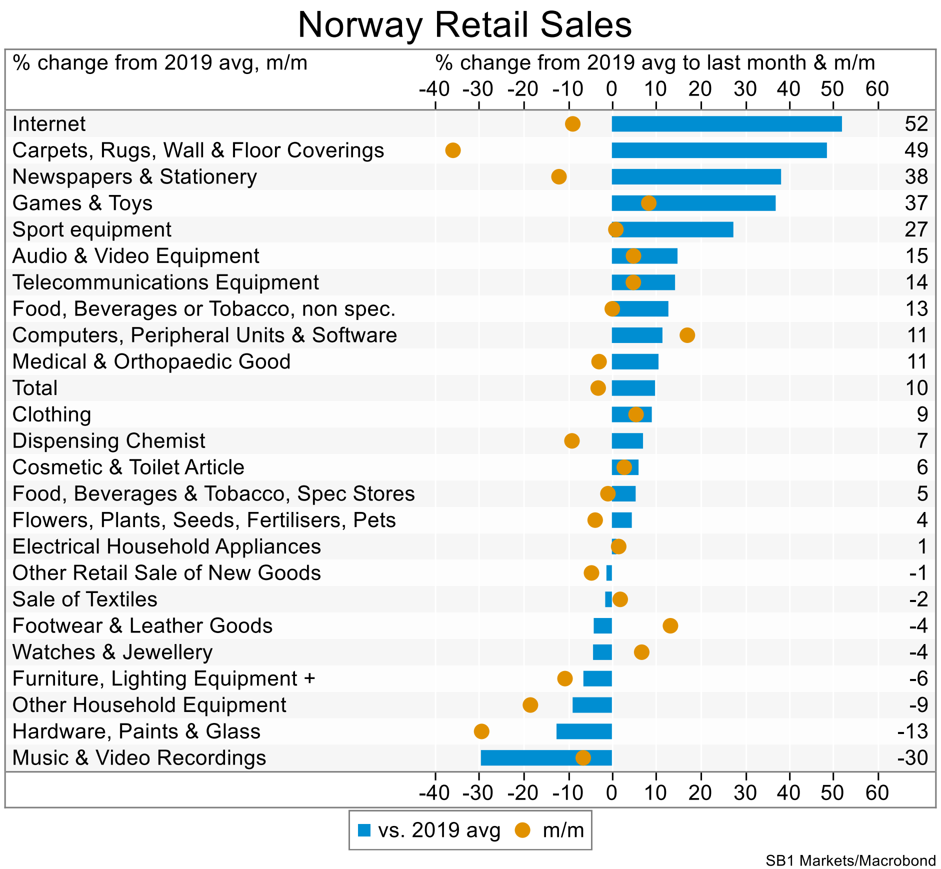


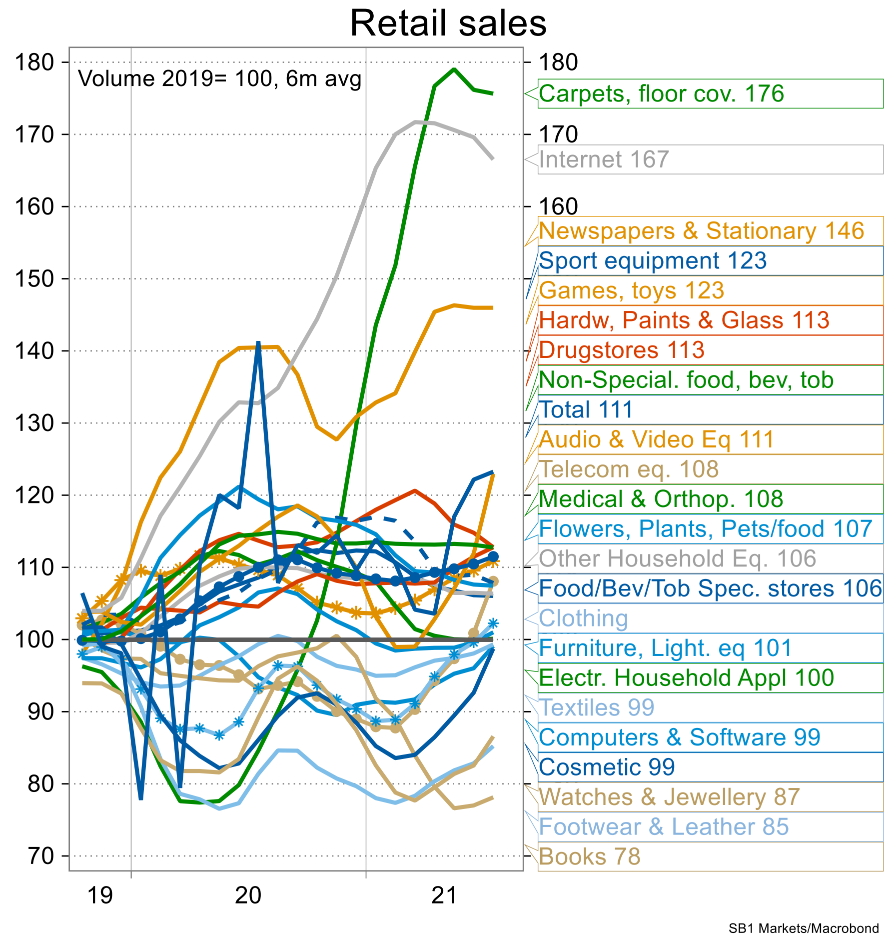
SB1 Markets/Macrobond

- In the consumption of goods index, sales of 'other goods' are down just 0.9%, while a weighted average of retail sales of goods assume are included in these other goods fell by almost 6% due to the 18% decline in household equipment (which is explained by the 29% setback in hardware/building materials). This discrepancy explains the record large difference between the retail sales index and the consumption of goods index in July

Huge sectoral differences – home refurnishing at the top

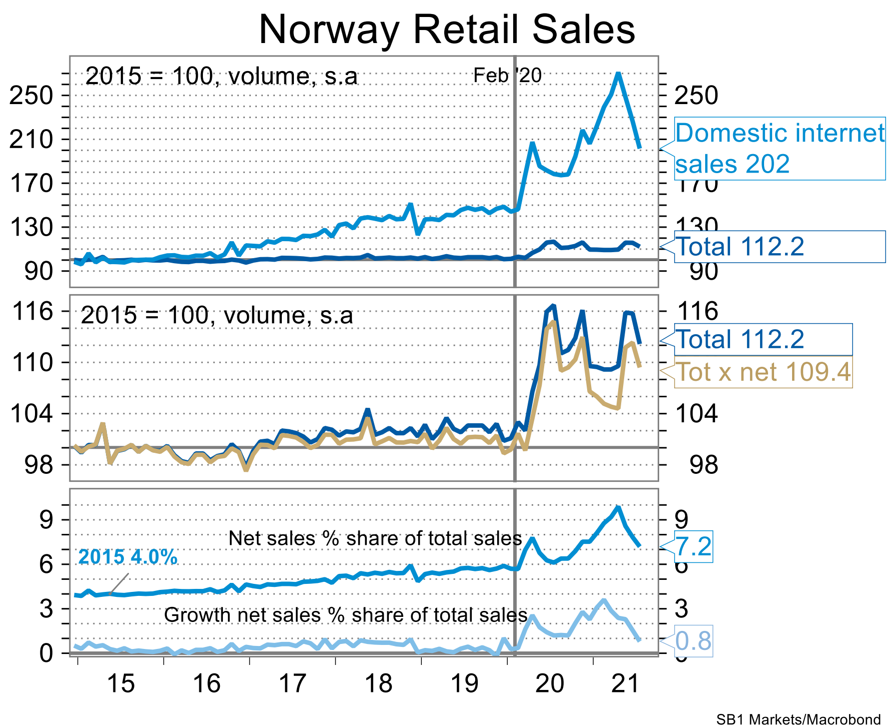
…and several sectors are trending down, mostly from 'too high' levels during the pandemic

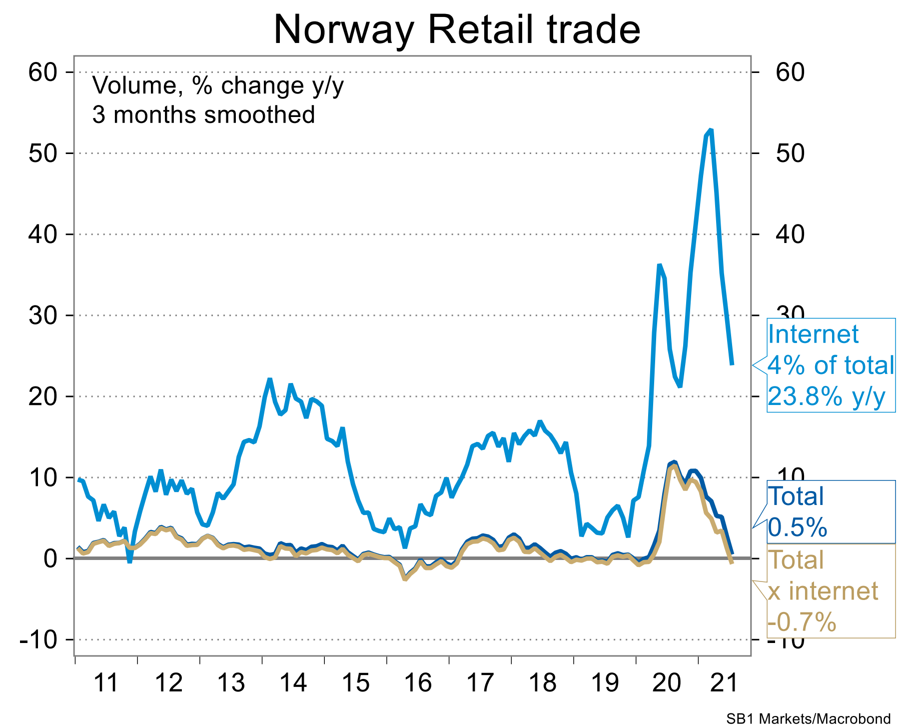




Internet sales (domestic) have fallen 25% past 3 months, as shops reopened

The market share has fallen to 7% from 10% - still above the 6% pre-pandemic level

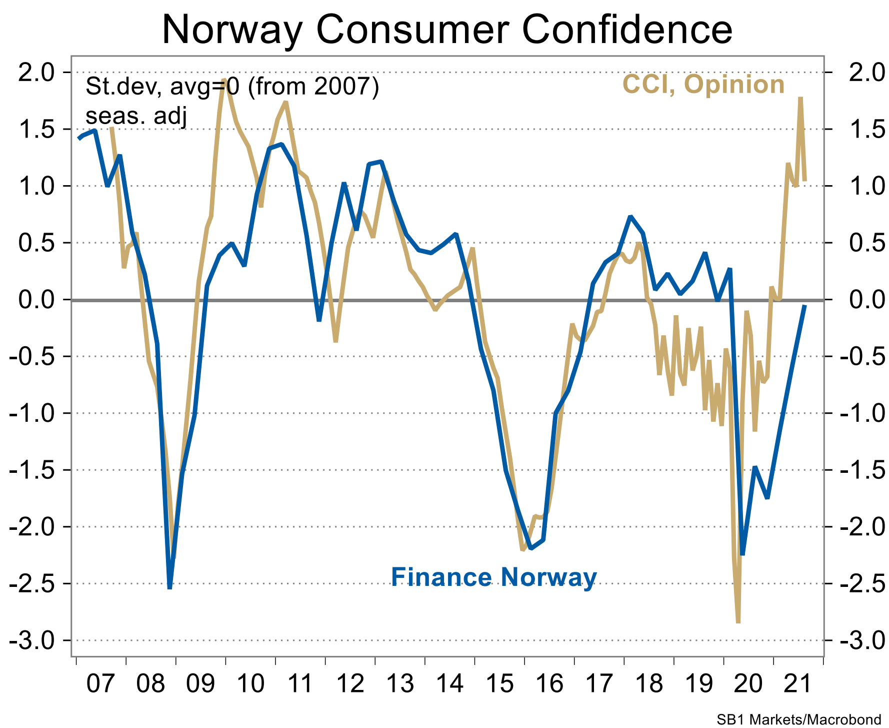




- Since 2015, domestic internet sales (not included direct import from abroad) have increased its market share to 7% from 4%, via 10% at the top in April. Internet sales fell by 11% m/m
- ICT equipment, cosmetics/drugs, clothing, food, and sports equipment are the 5 largest product categories sold from net outlets

Consumer confidence reversed the July spike, and is still at a high level

Opinion's CCI fell by 0.7 st.dev, and almost reversed July hike. The level is still +1 st.dev

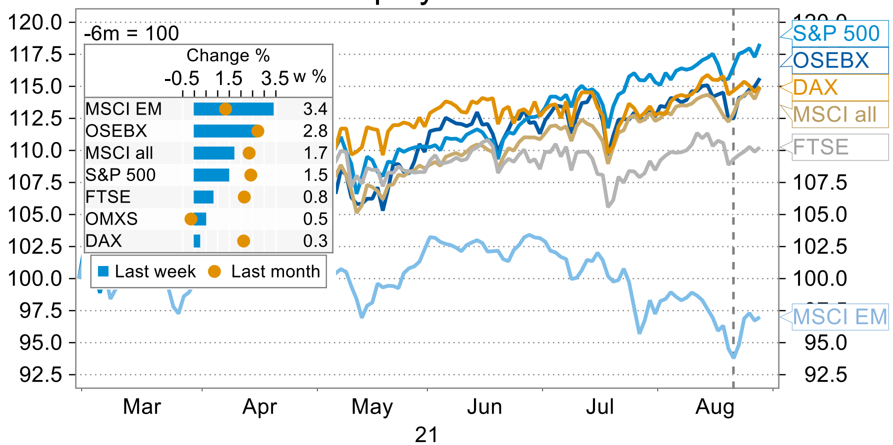


- The lift in July was substantial, 0.8 st.dev – as was the 0.7 st.dev decline in August. The level in August is still strong
- Finans Norge's confidence quarterly survey rose to an average level in Q3. This survey has been far weaker (some 1 st.dev) than the CCI survey the last year – and it still is. We have no good explanation for the discrepancy
  - » Given retail sales & the housing market Finans Norge's survey seems too weak

Equities, bond yields, commodities (and the NOK) up

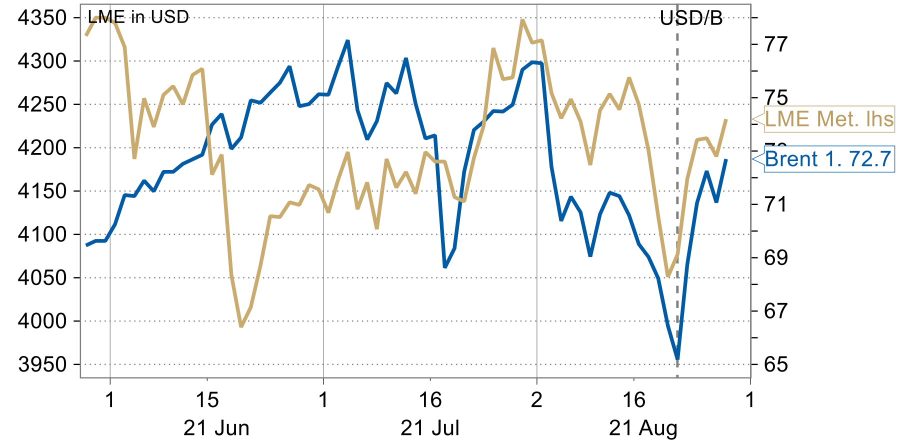
A tapering start in Q4 2021 is now fully discounted? And the Delta variant will not knock out the world etc.

Equity Indices



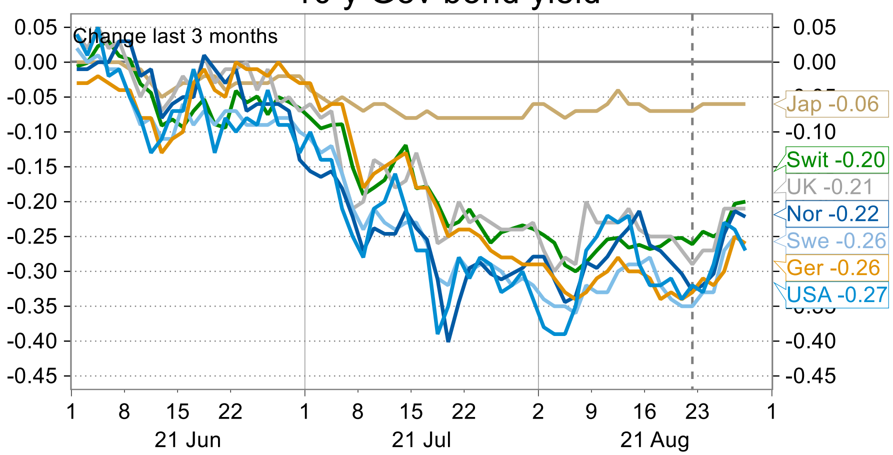
SB1 Markets/Macrobond

Oil vs. metals



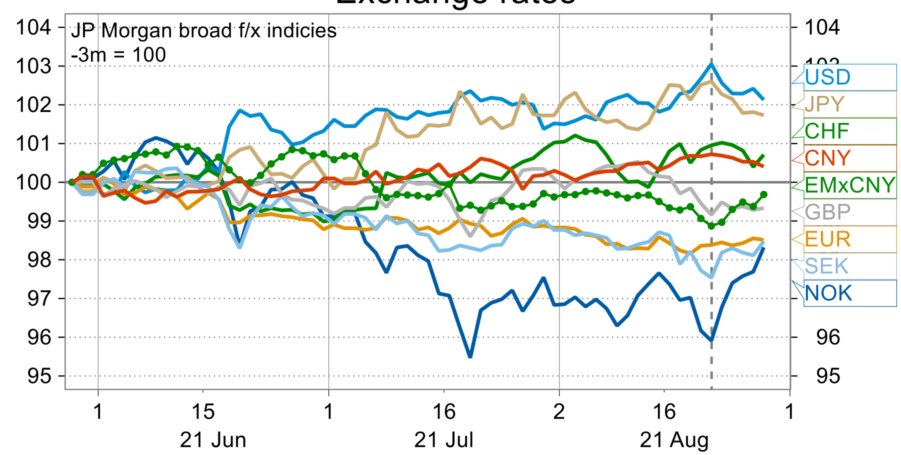
SB1 Markets/Macrobond

10 y Gov bond yield



SB1 Markets/Macrobond

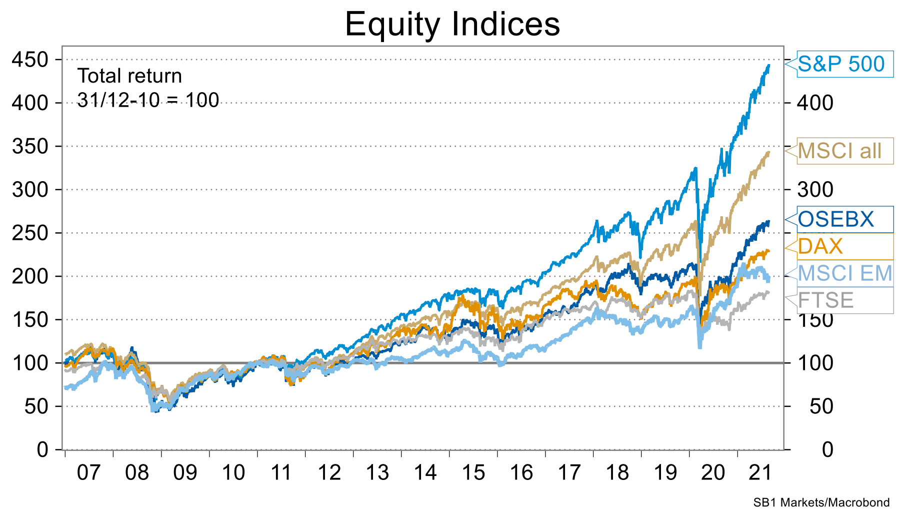
Exchange rates

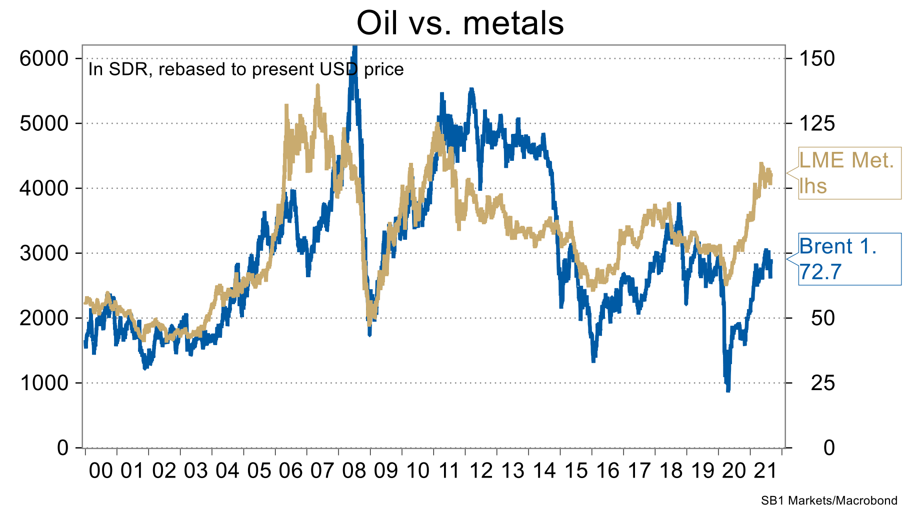


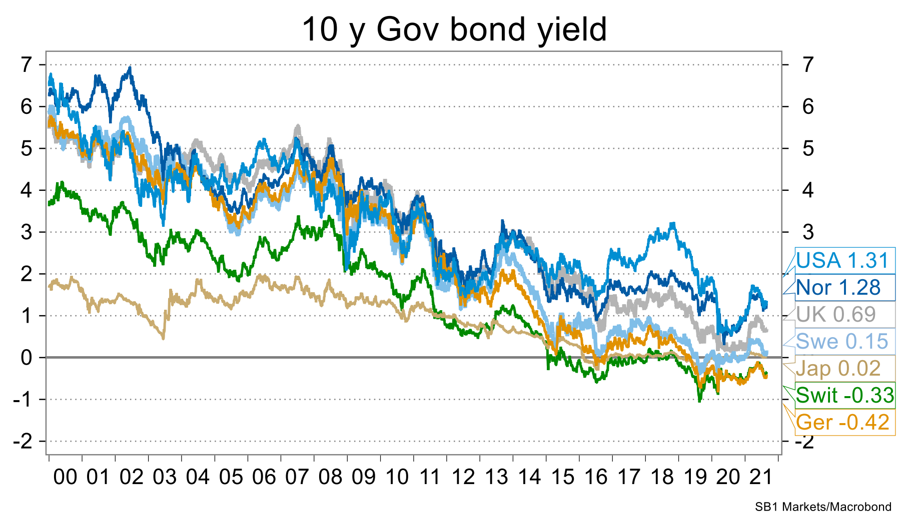
SB1 Markets/Macrobond

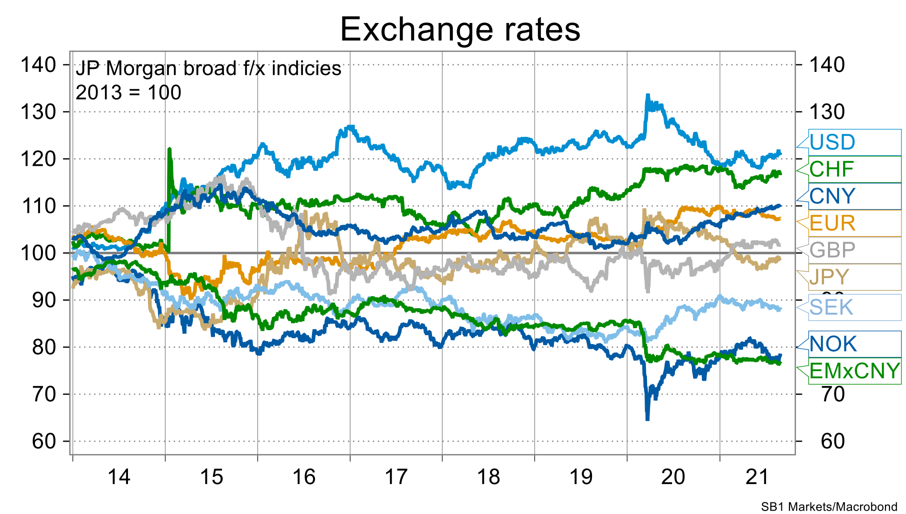
The big picture: Strong stock & commodity markets

Still, yields are heading down everywhere. The CNY is steady climbing, other EM f/x & NOK weak



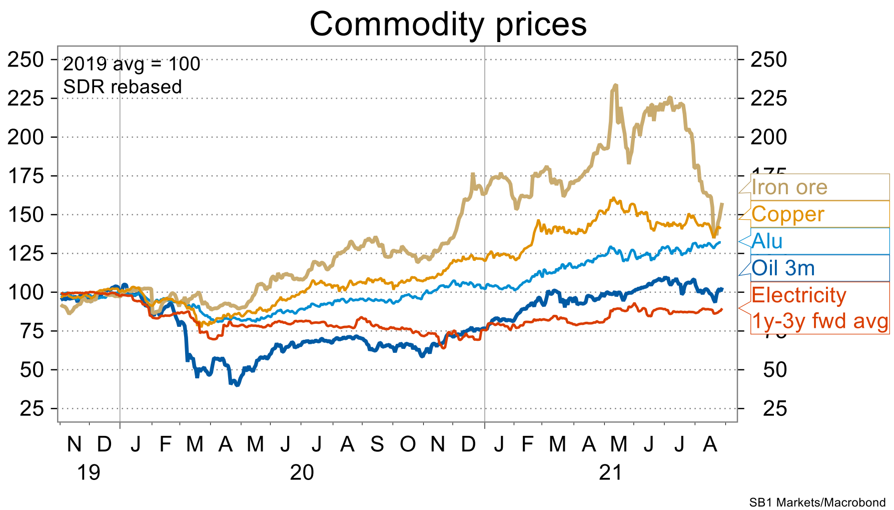


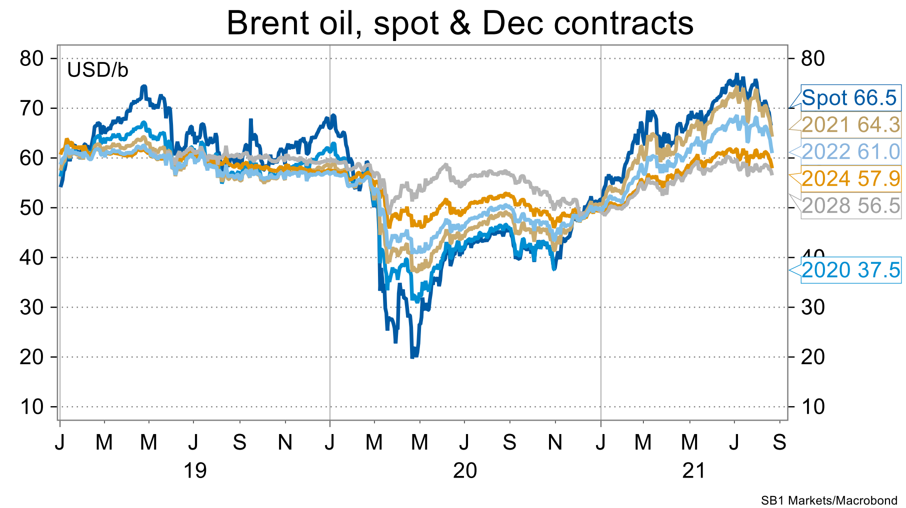


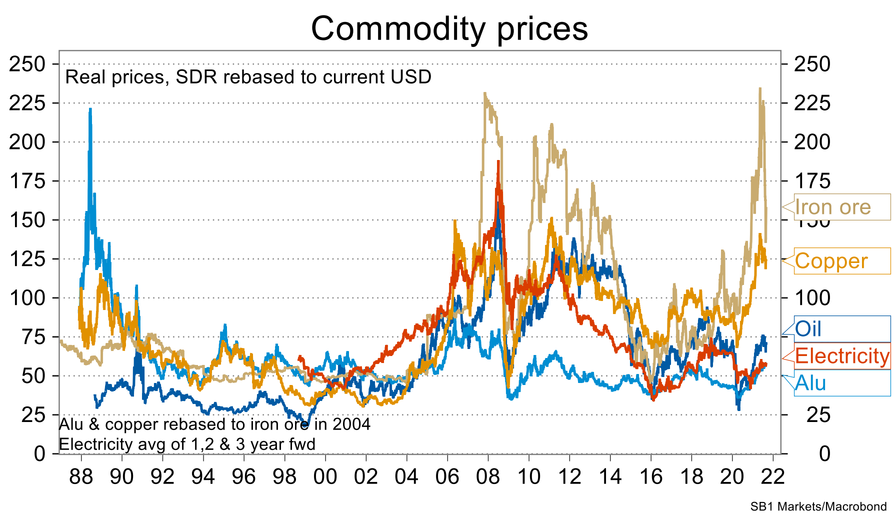


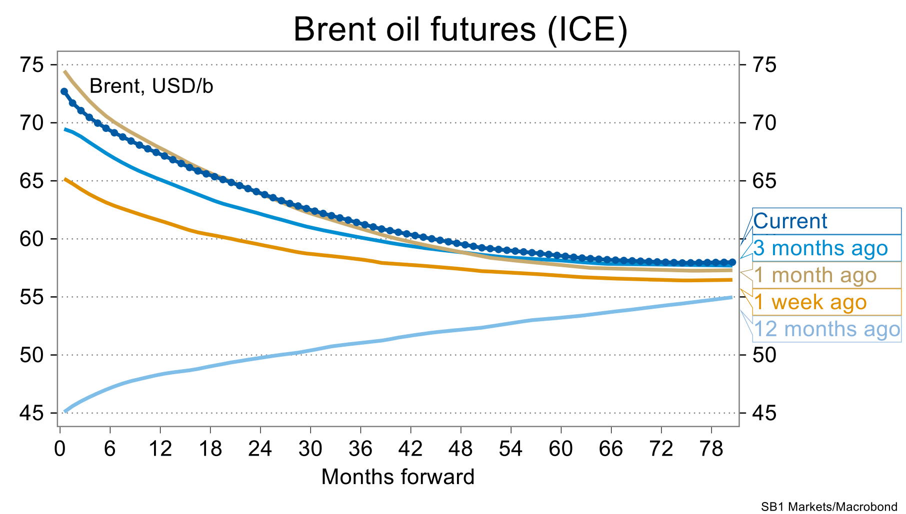
All commodity prices up, even iron ore

… perhaps because China seems to have beaten down the virus again. Good for demand for oil too





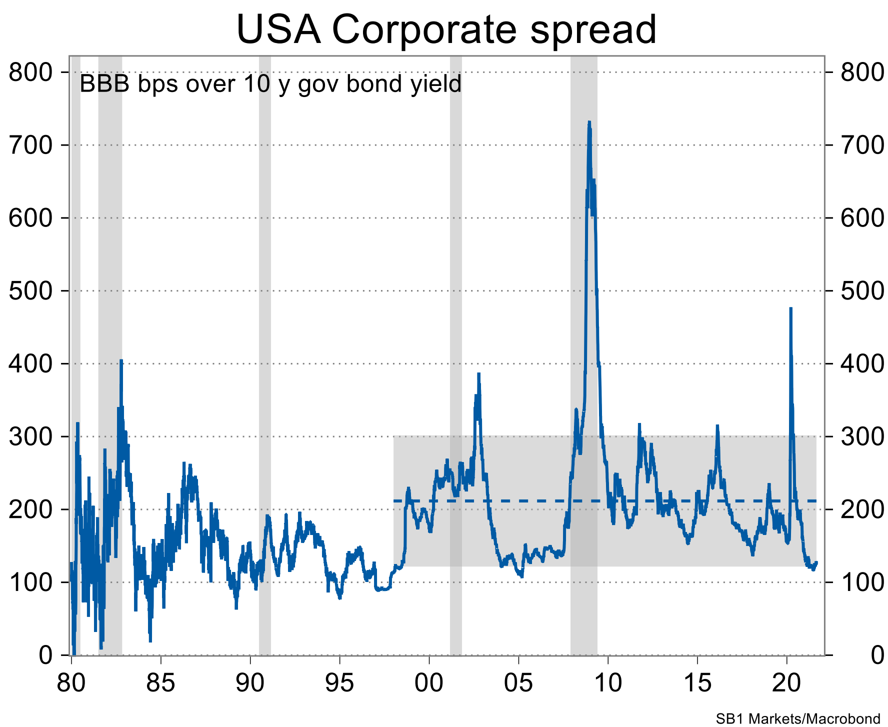


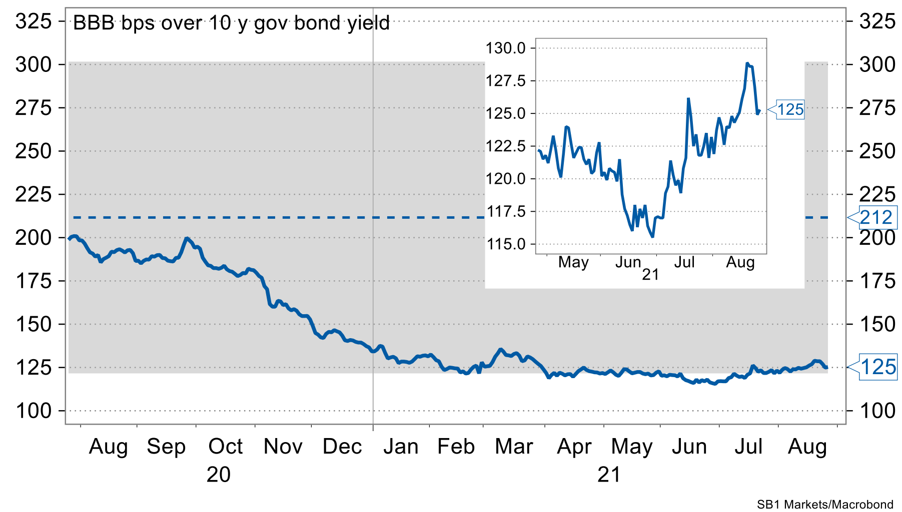


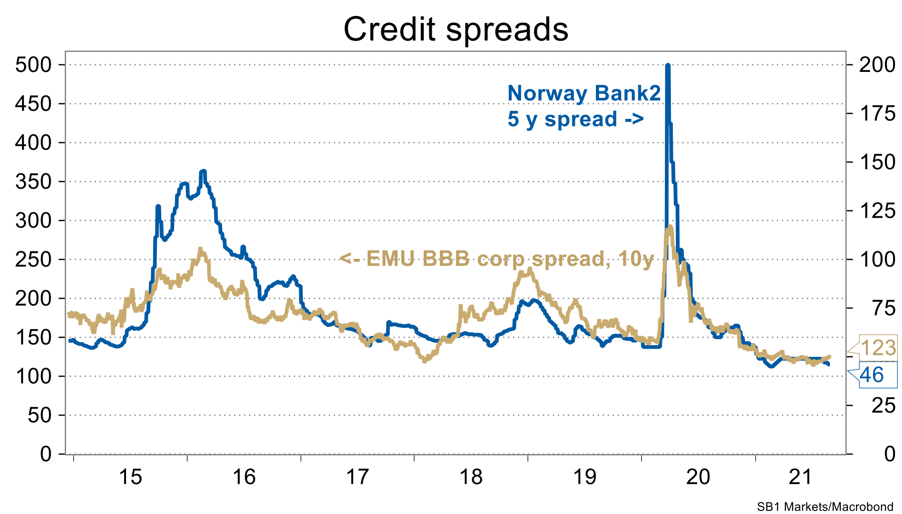
SpareBank 1 MARKETS

A marginal lift in foreign credit spreads partially reversed last week

… in Norway, bank spreads are heading down

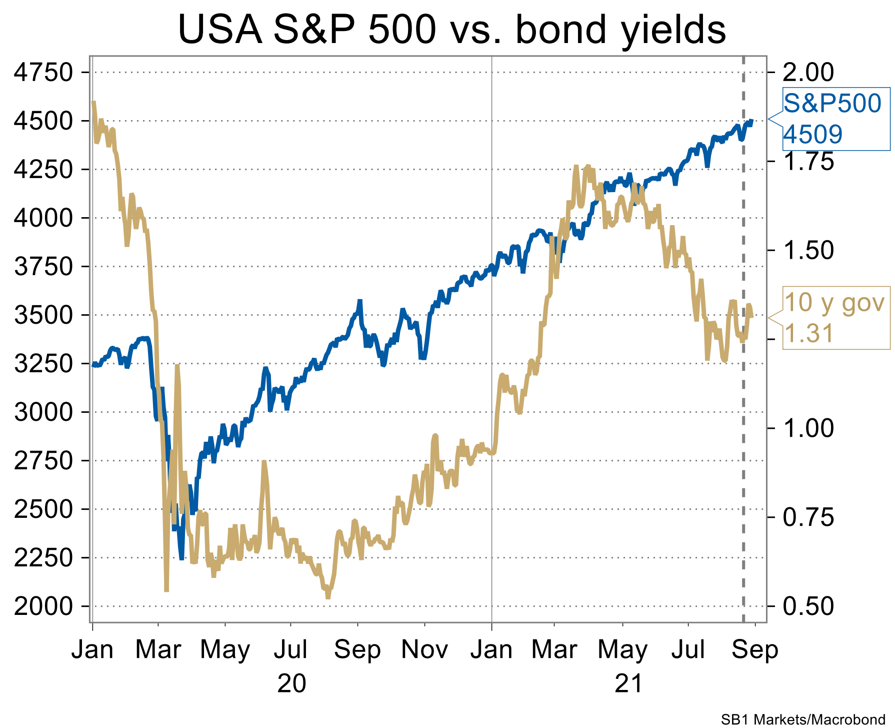


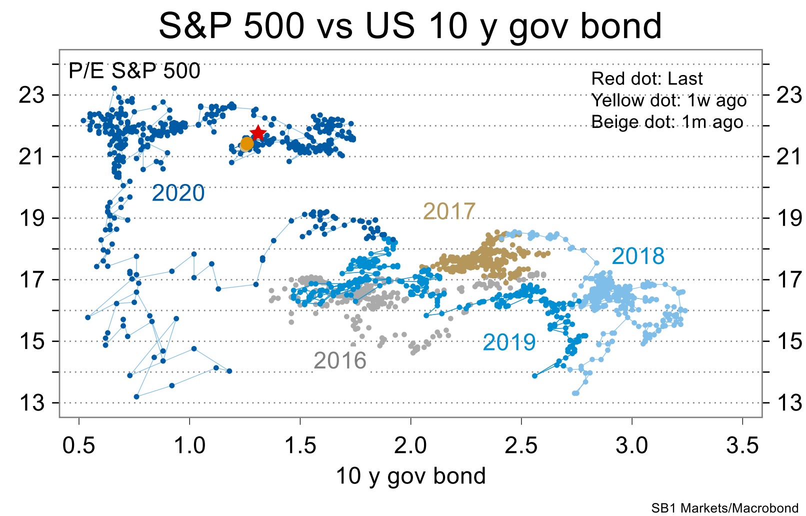


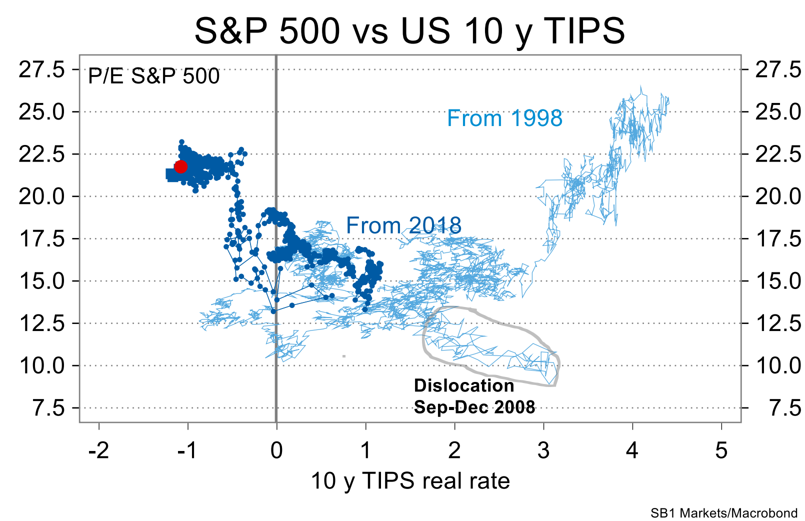


Another S&P 500 ATHs on Tuesday, Wednesday & Friday. Bonds slightly up

However, yields fell following Powell's Jackson Hole speech. Tapering yes, of course. But no hikes



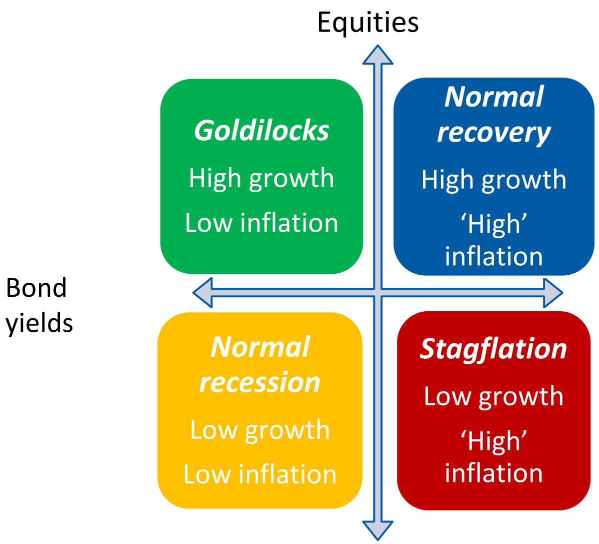


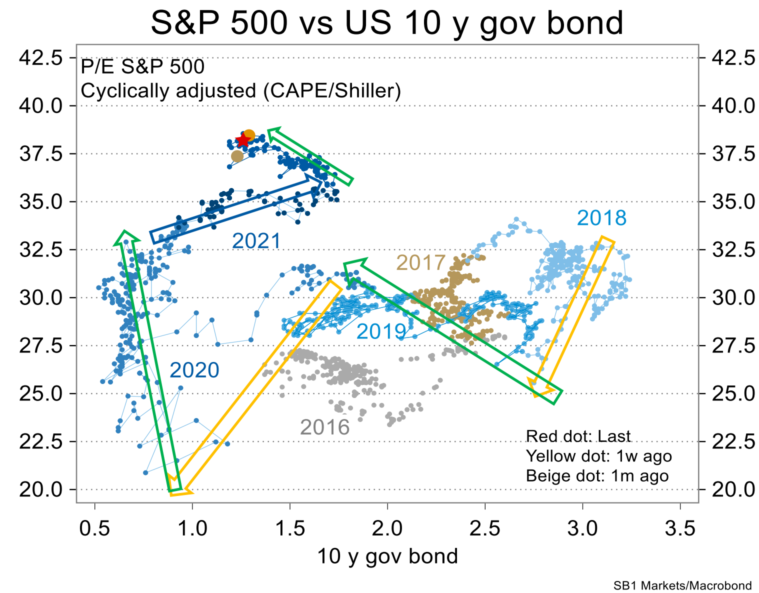


SpareBank 1 MARKETS

Still well into the 'Goldilocks corner'

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





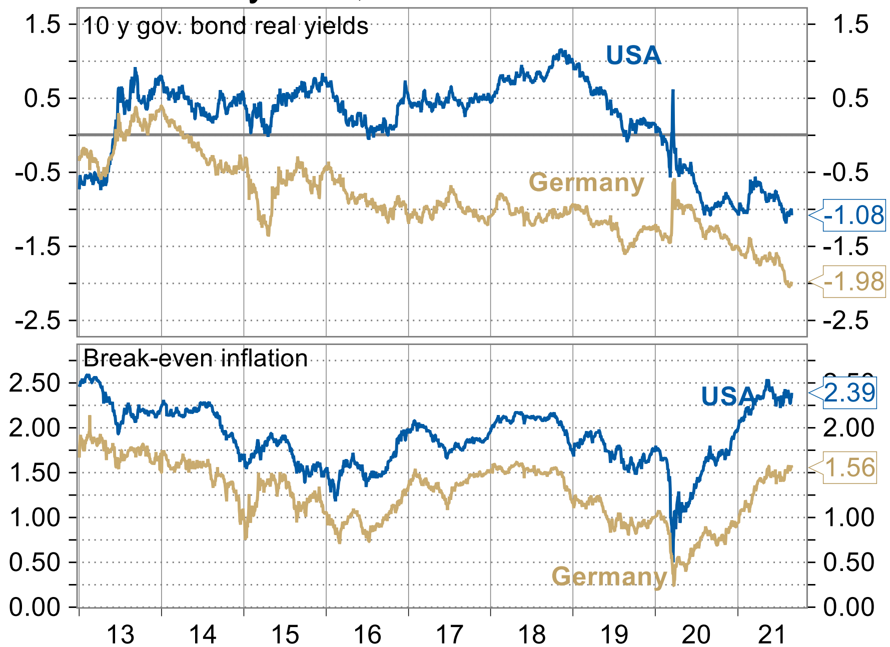
- Usually, we have associated drifts towards the 'green corner' - low inflation and solid growth at the same time - as a <u>temporary</u> sweet spot for markets
  - » Interest rates have climbed 100 bp+, and stock valuations have kept up or climbed (like the Shiller PE). Still, we deem the current yield 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
    - <u>If companies are able to increase their selling prices</u>, 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)
    - <u>If companies are not able to increase their selling prices</u>, 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

SpareBank 1 MARKETS

Here we go again: US real rates down, inflation expectations more up

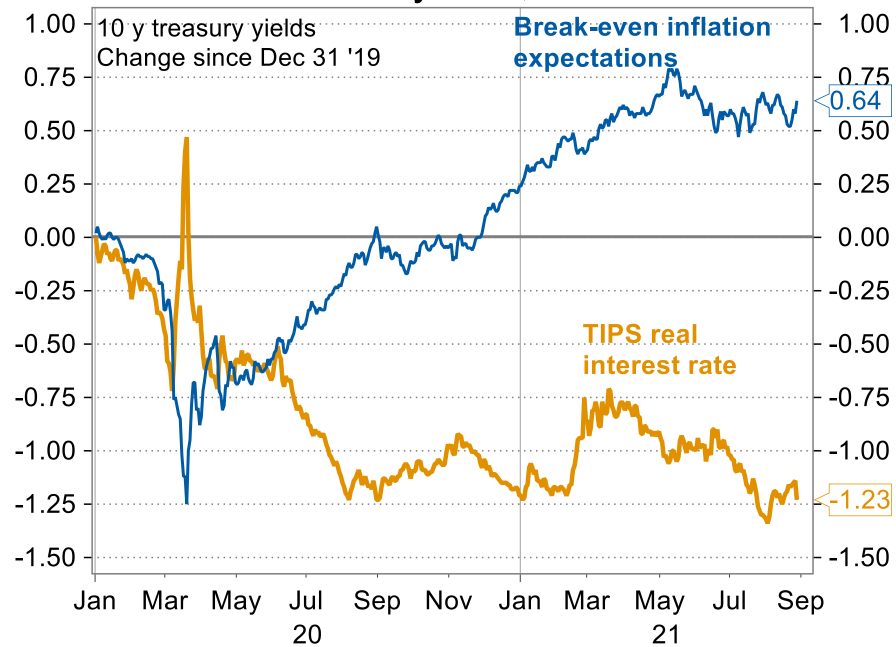
US 10 y nominal yield up 5 bps, real rate -7 bps, break even inflation +12 bps

Real yields, break-even inflation



SB1 Markets/Macrobond

USA Real yields, inflation



SB1 Markets/Macrobond

US & Germany 10 y Gov bond yield

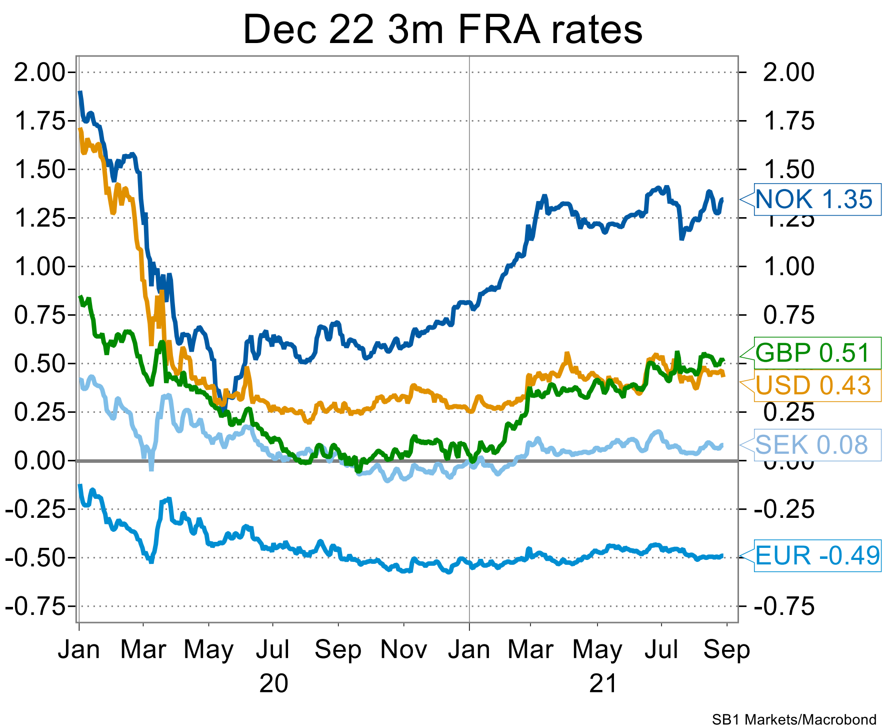
	Yield	Change 1w	Change 1m	Min since April-20
USA nominal treasury	1.31	0.05	0.06	0.52
.. break-even inflation	2.39	0.12	0.01	1.06
.. TIPS real rate	-1.08	-0.07	0.05	-1.19
Germany nominal bund	-0.42	0.07	0.02	-0.65
.. break-even inflation	1.56	0.02	0.11	0.40
.. real rate	-1.98	0.05	-0.09	-2.05

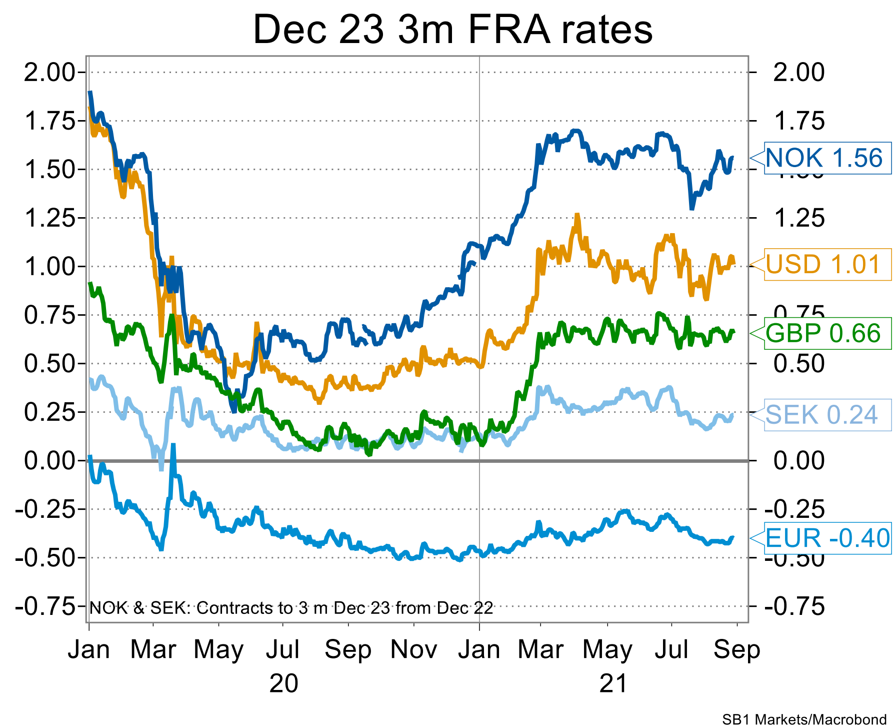
SB1 Markets/Macrobond

- US real rates ‘collapsed’ at Friday (down 9 bps) – and more than inflation expectations rose – after Powell’s speech at the Jackson Hole (digital) conference. Tapering will probably start in late 2021, but that was discounted beforehand, but Powell succeeded in calming nerves that Fed will turn aggressive vs inflation – he had lot of arguments for inflation to return to a normal level again, signalling that a tough tightening is not in the cards

FRAs: Mostly up, by the most in Norway

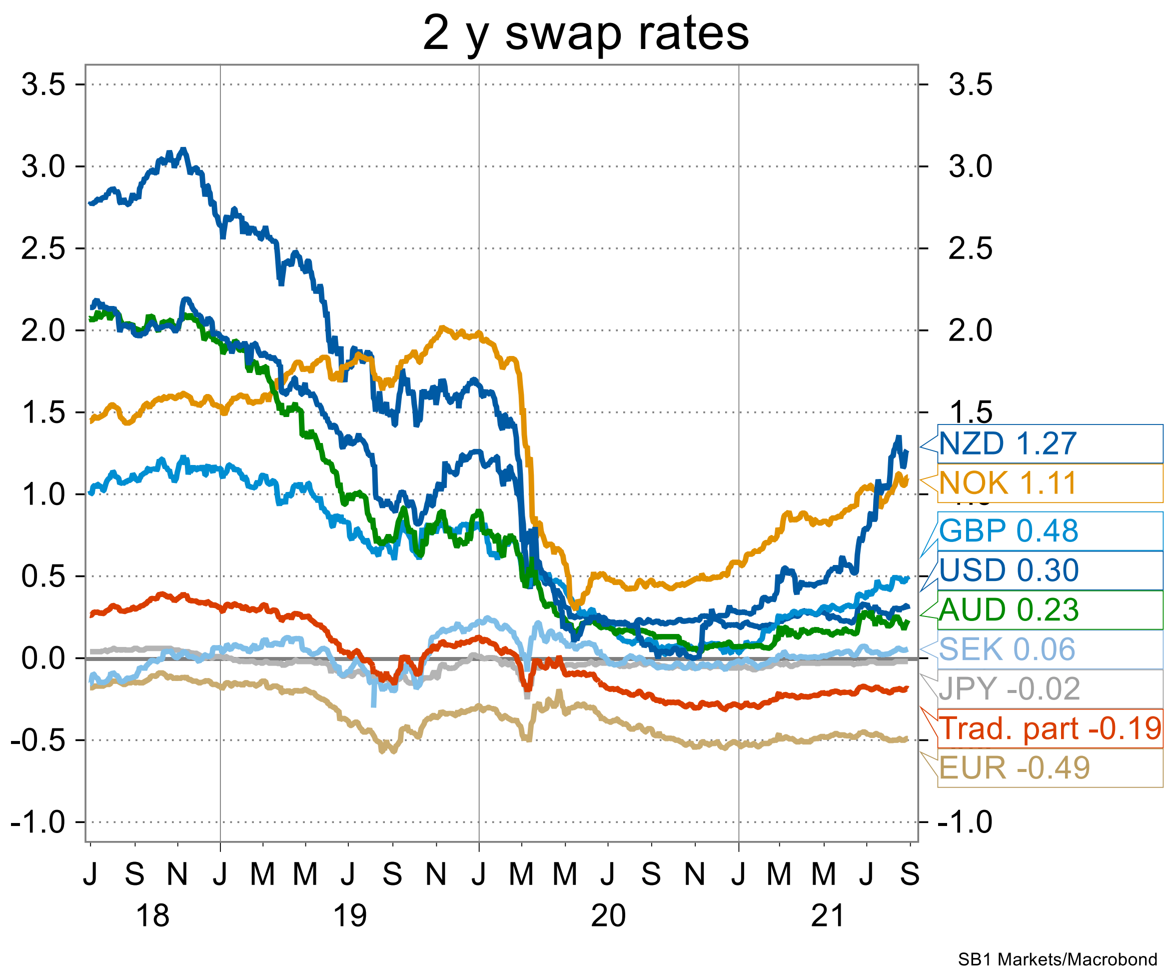
Short term interest rate expectations in the US fell on Friday, as Powell calmed markets

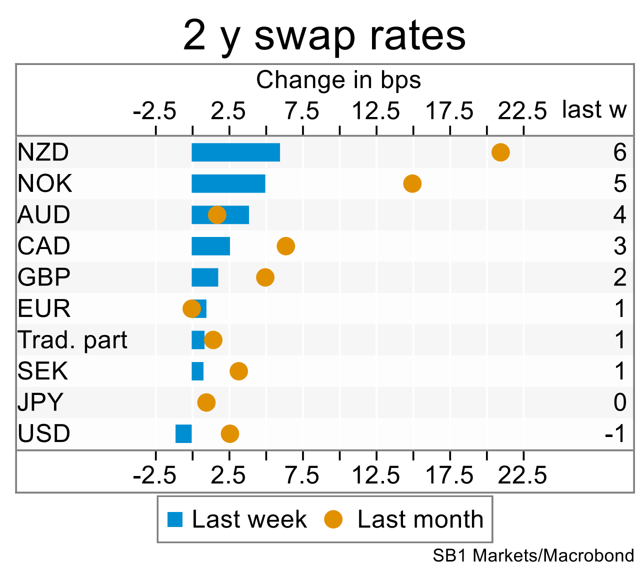




- The market expects both **BoE** and the **Federal Reserve** to hike next year

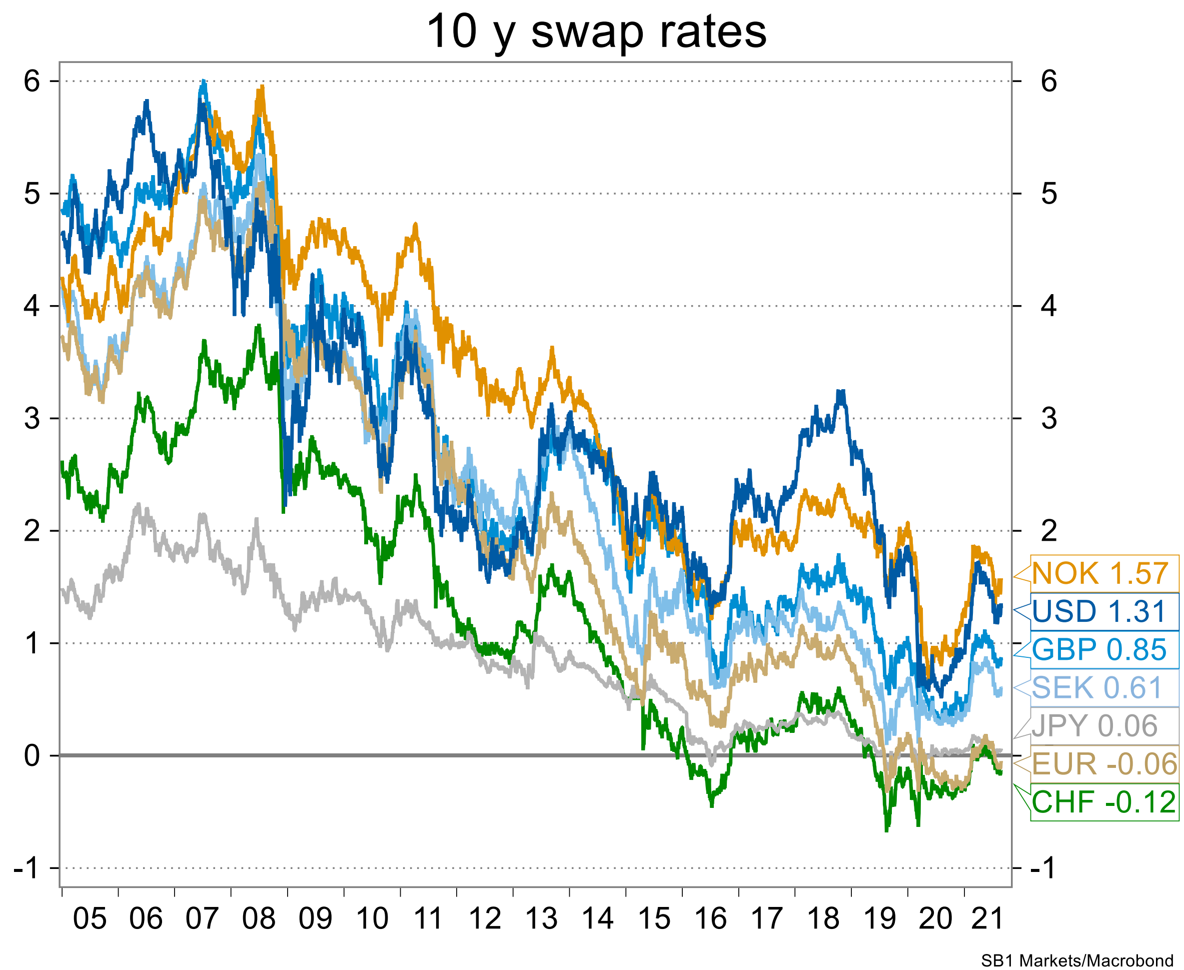
US rates down, others up last week

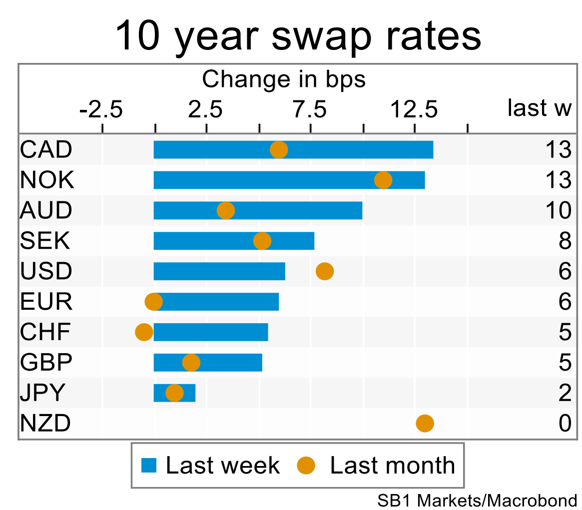




Up everywhere last week, with the super-cyclicals in the lead

Both rates and f/x up in both in AUD, CAD, NOK and SEK (following last week's decline)

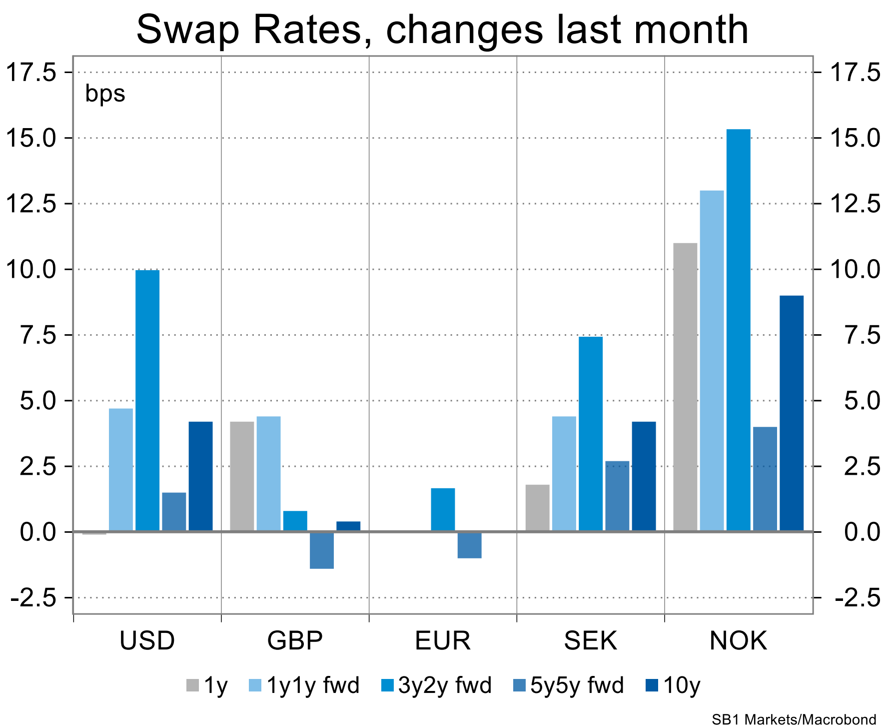


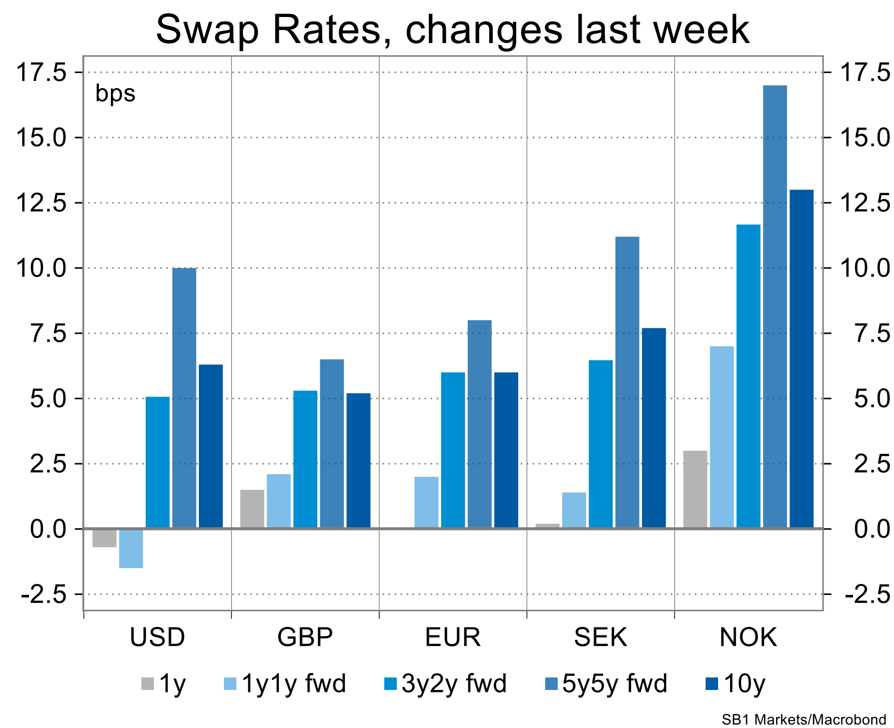


SpareBank 1 MARKETS

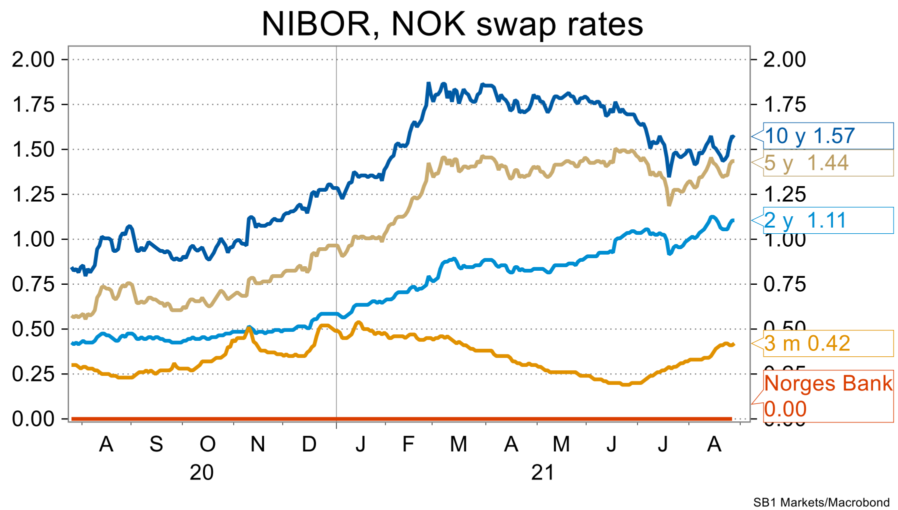
The short end in the US down last week, all other rates up

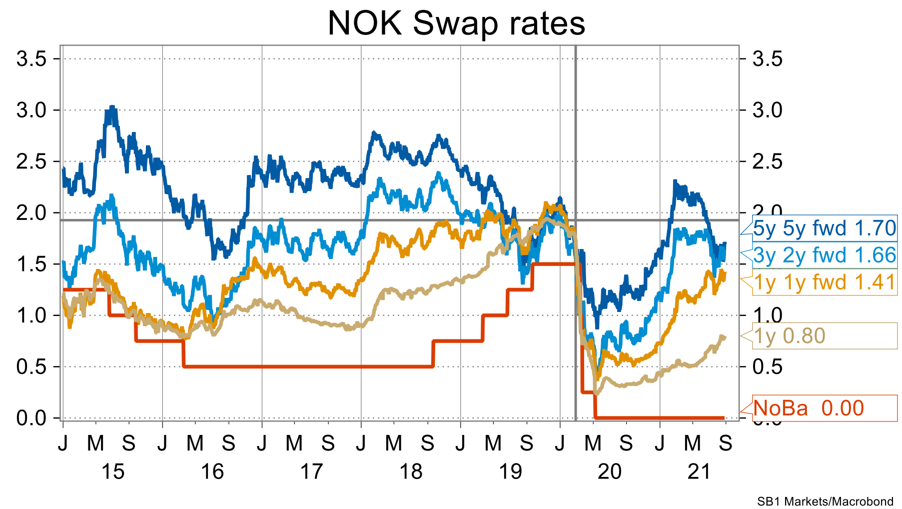
… and NOK rates in the lead, all over the curve

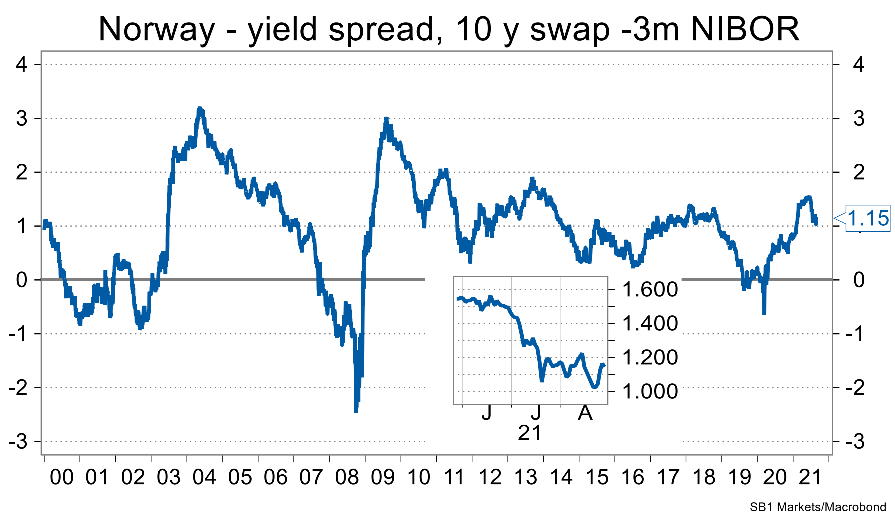


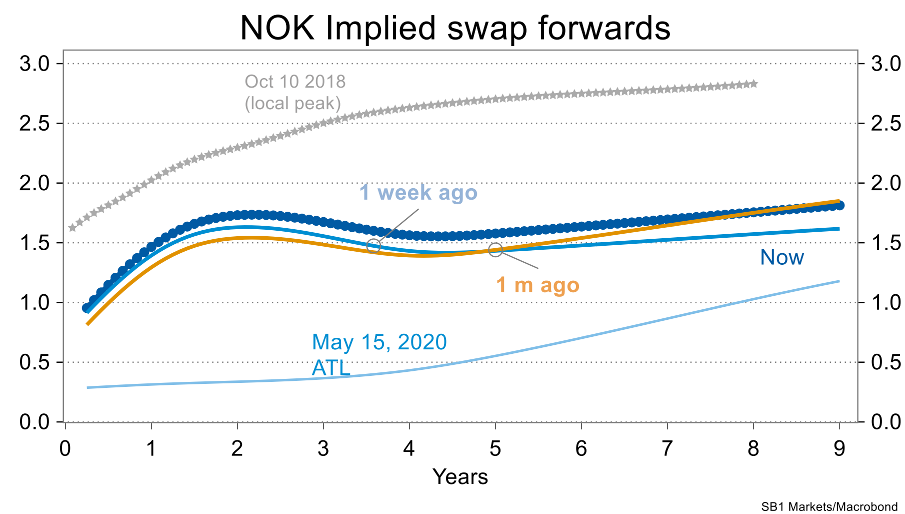


Rates up all over the curve, most in the long end of the curve





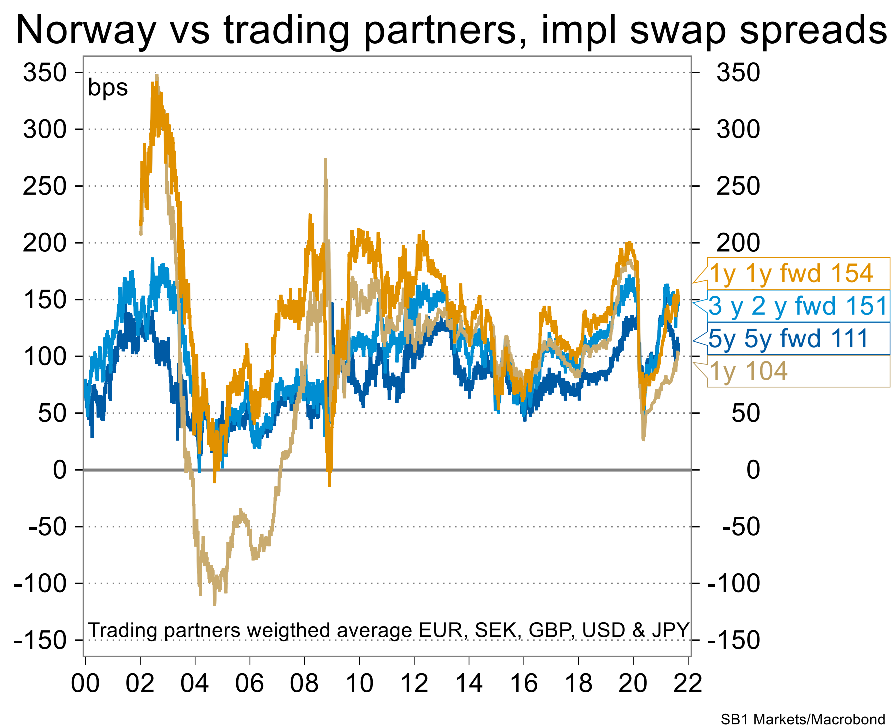


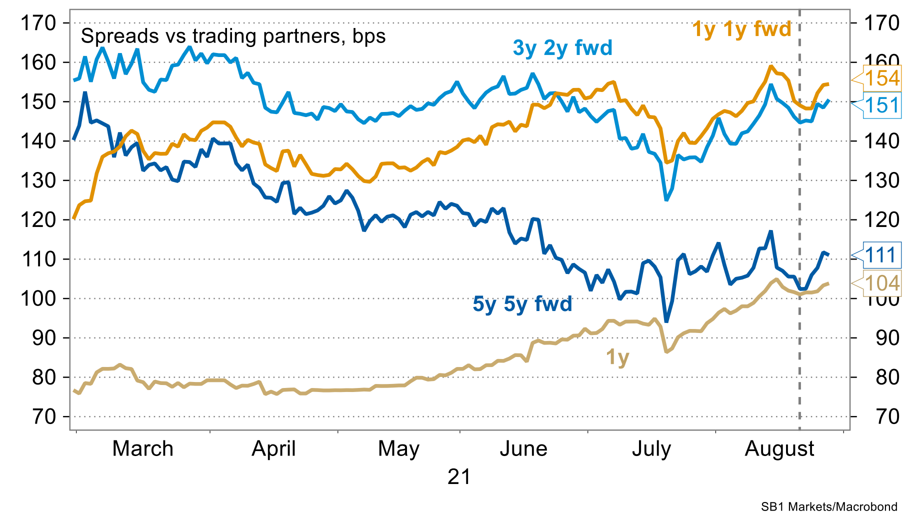


SpareBank 1 MARKETS

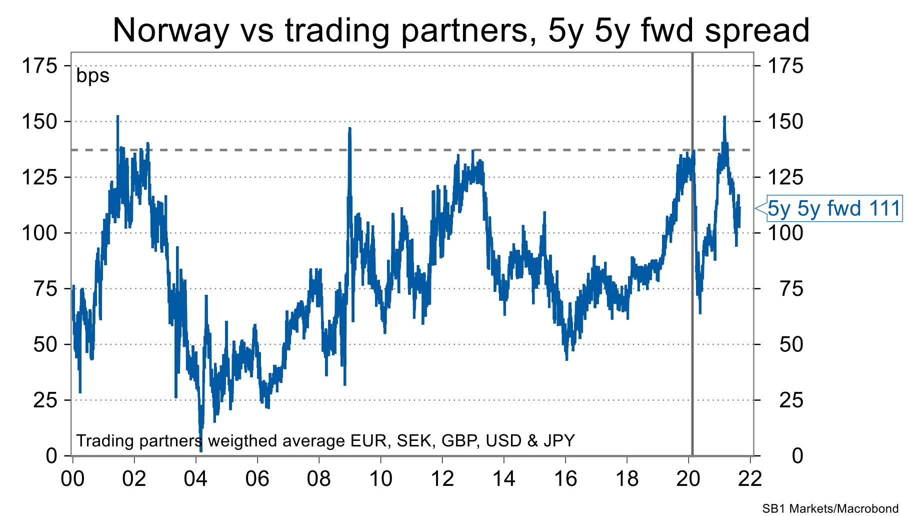
Forward spreads vs trading partners up 4 - 12 bps, most at the mid segment

Without any strong Norwegian macro data (barring the most important report, on payrolls)





- The 5 y 5y fwd spread fell by 15 bps last week!



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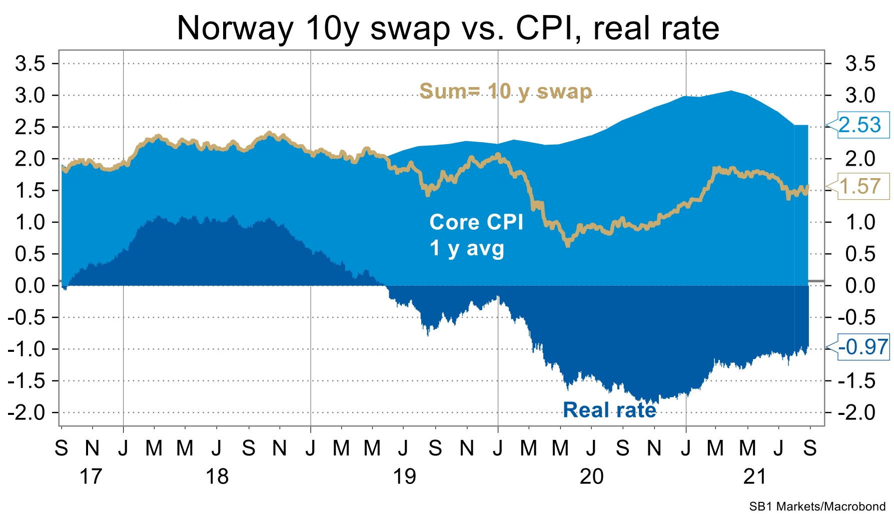
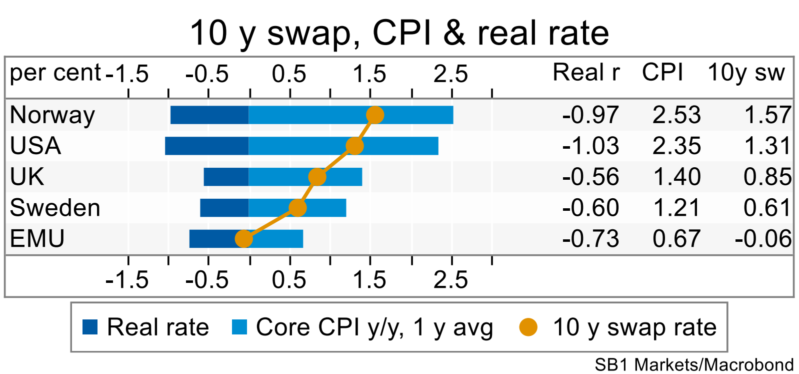
Negative (actual) real interest rates most places – NOK at the bottom



NOK 10 y swaps have flattened

- The **10y NOK swap** rate up 13 bp to 1.57%
- **The actual real rate**, after deducting a 2.5% average core CPI inflation over the 2 past years equals -1%
  - » 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 2.5%
  - » On the other hand, barring economists' in academia & finance, 'nobody else' believe in the 2% inflation target. Other economists say 2.5% as do 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



per cent	Real r	CPI	10y sw
Norway	-0.97	2.53	1.57
USA	-1.03	2.35	1.31
UK	-0.56	1.40	0.85
Sweden	-0.60	1.21	0.61
EMU	-0.73	0.67	-0.06

The NOK real rate not the lowest anymore

- **Inflation** among main trading partners varies between 0.7% to 2.4% (measured by actual annual core inflation, smoothed over 12 months). EMU at the bottom, US at the top, the latter is now climbing rapidly
  - » Other measures of inflation trends, looking backward or including forward expectations yields the same ranking
- **Real rates** among our trading partners, and ranging between -0.6% and -1% measured vs. the 10 y swap rate and core inflation over the past two years
- **Thus, the Norwegian real rate at -1% is among the lowest**

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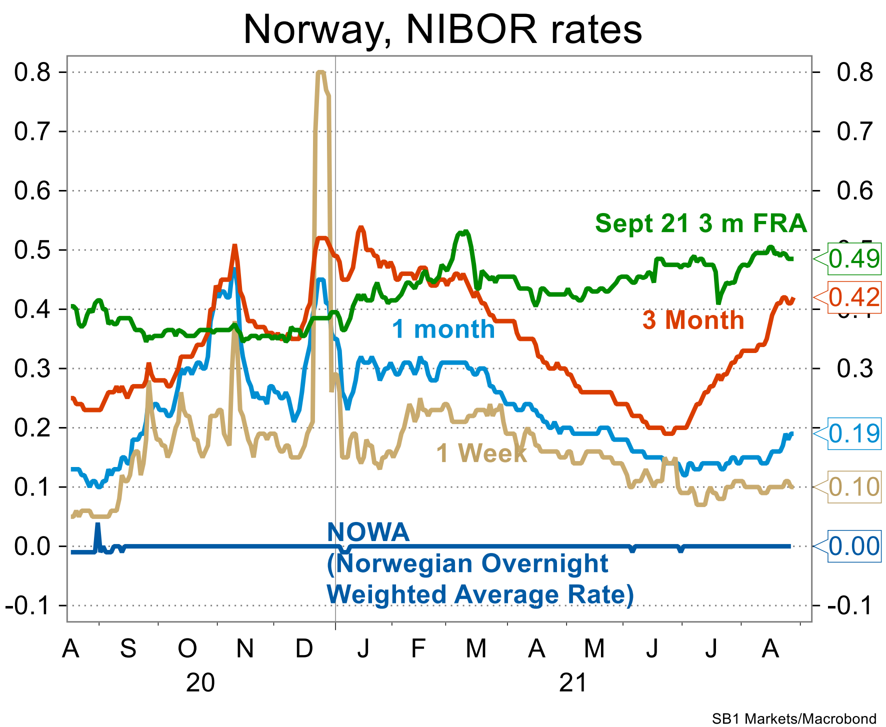
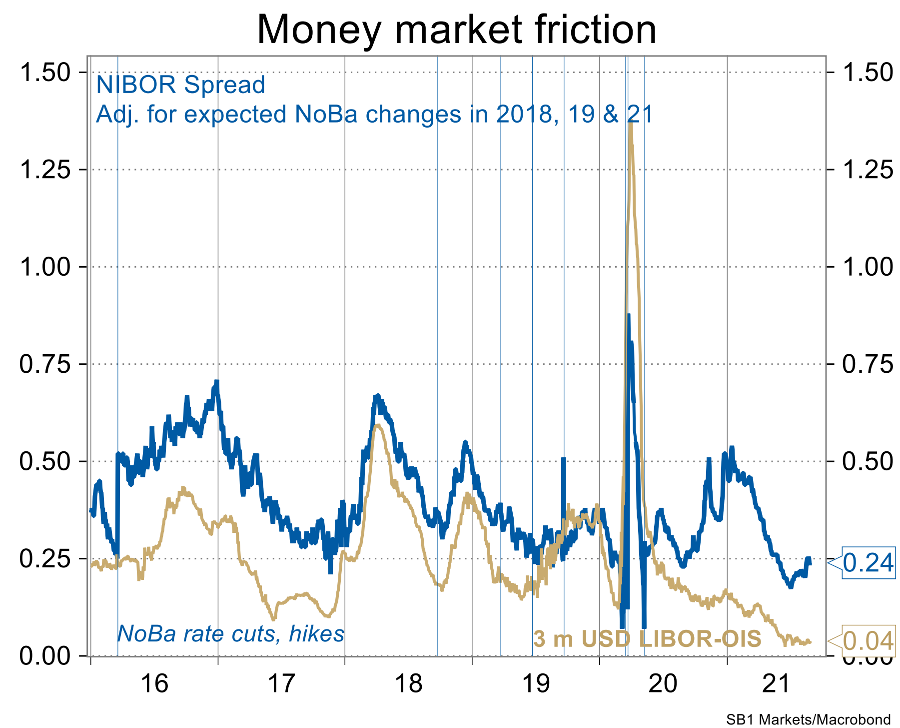
3 m NIBOR 1 bp up to 0.42%, the 'real' NIBOR spread probably down to 24 bps





- The **USD LIBOR OIS spread** is still low, even if the Fed has tried to mop up excess liquidity in the money market by heavy use of reversed repos
- The **Sept-21 3 m FRA contract** at 0.49% bps (unch. last week) is 7 bps above the current 3 m NIBOR, implying further lift the coming weeks. Thereafter the 3 m NIBOR will climb by 2 bps per week until NoBa stops hiking the signal rate by 25 bps per quarter (if the low NIBOR spread remains unchanged)
- Last week **the 'real' NIBOR spread** probably fell 1 bp to 24 bps, as we assume the market is fully discounting a NoBa hike in September. We expect the spread to drift upwards the coming months

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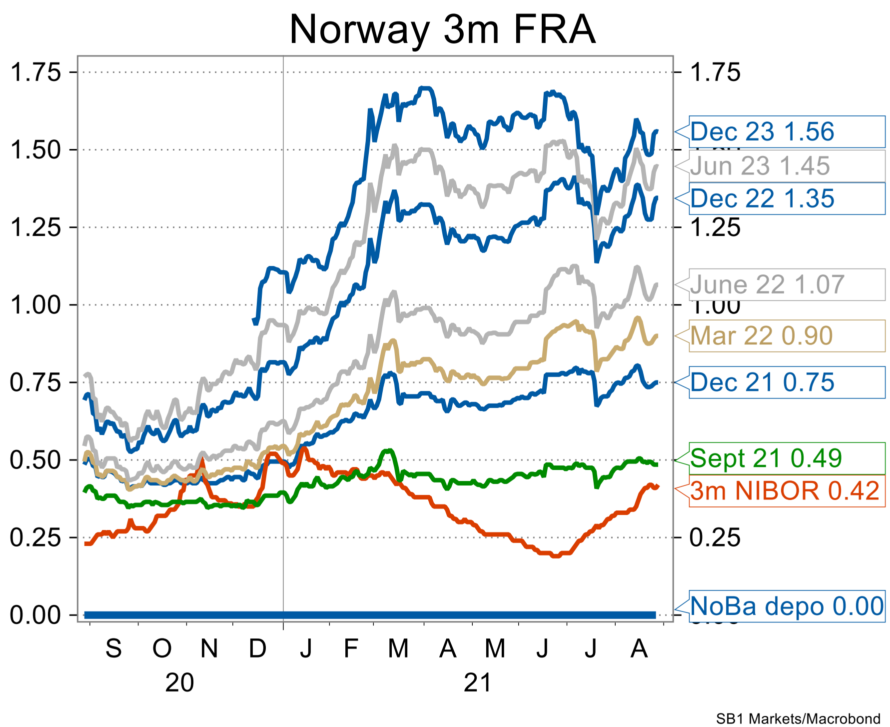
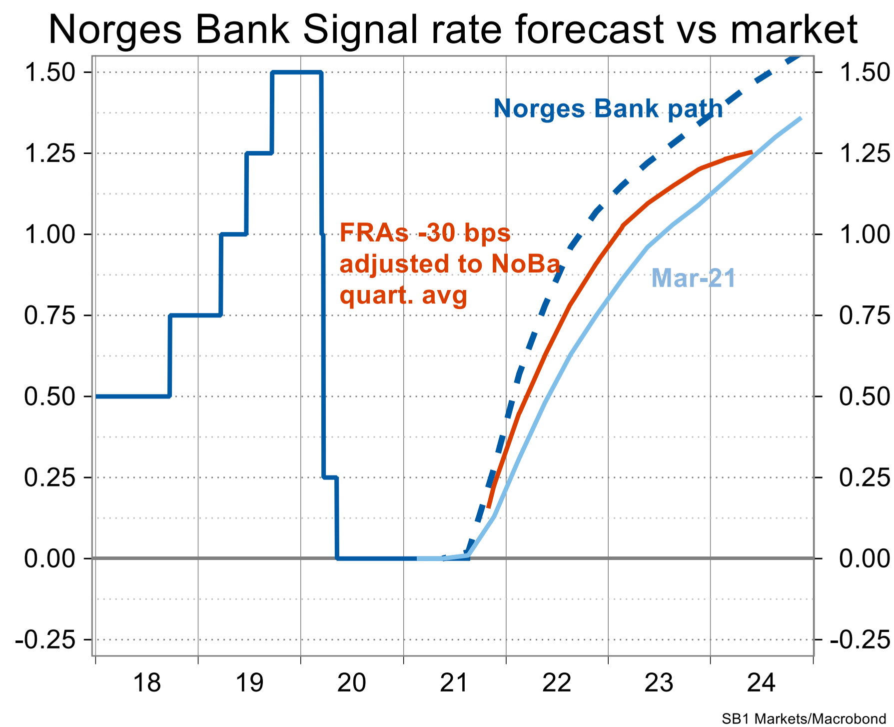
3m FRA rates up by 7 bps, from March '22 onwards, still below NoBa's curve

Still, a 2nd hike in December is deemed quite likely

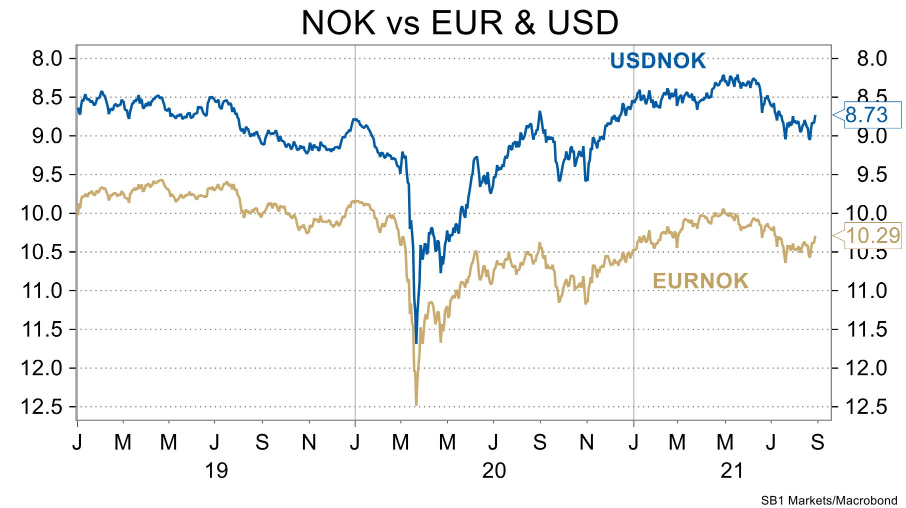


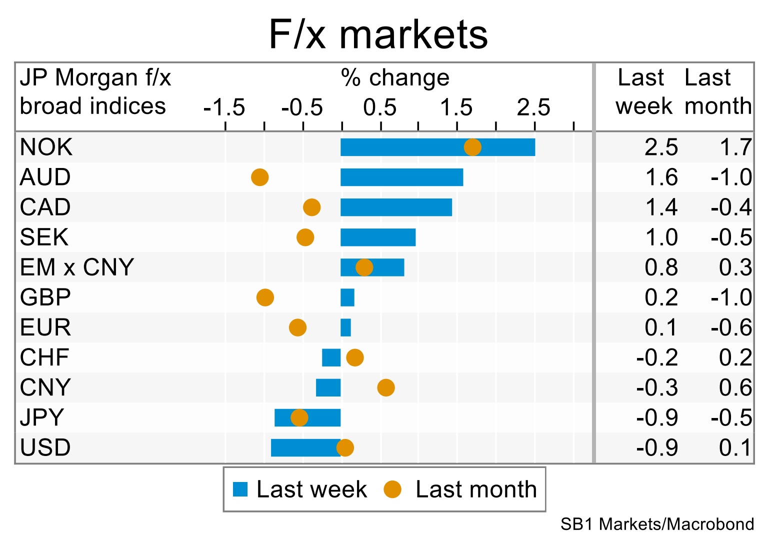


- The market is still betting on a **NoBa hike in September** – and more than fully if the NIBOR spread remains at 0.25 bps. If a 30 bps spread is assumed, the implied probability falls to 88%
- The Dec-21 FRA at 0.75%, after deducting a Q4 liquidity premium at 7 bp, implies a 76% probability for a **2nd hike in December** if the NIBOR spread stays at 24 bps. It the spread widens to 30 bps, the probably for a 2nd hike falls to 50%
- The Mar-22 FRA at 0.90% implies a more than 50% for a 3rd NoBa hike in March, given a 2nd hike in December, it the spread remains at 24 bps

After being the loser, NOK turned out to be the winner last week, up 2.5%

The other supercyclicals up too. The USD down





JP Morgan f/x broad indices	Last week	Last month
NOK	2.5	1.7
AUD	1.6	-1.0
CAD	1.4	-0.4
SEK	1.0	-0.5
EM x CNY	0.8	0.3
GBP	0.2	-1.0
EUR	0.1	-0.6
CHF	-0.2	0.2
CNY	-0.3	0.6
JPY	-0.9	-0.5
USD	-0.9	0.1

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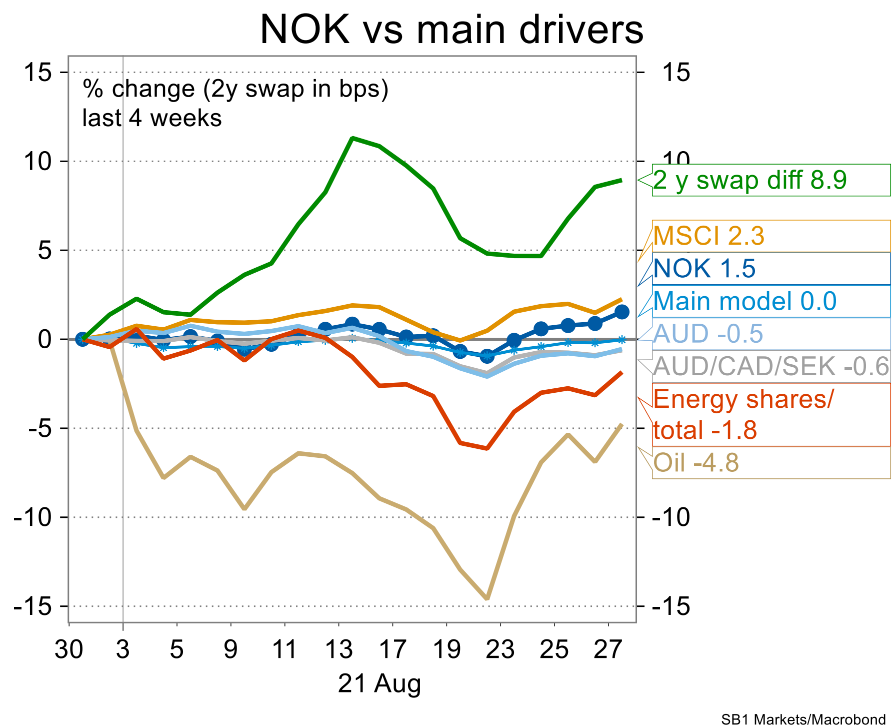
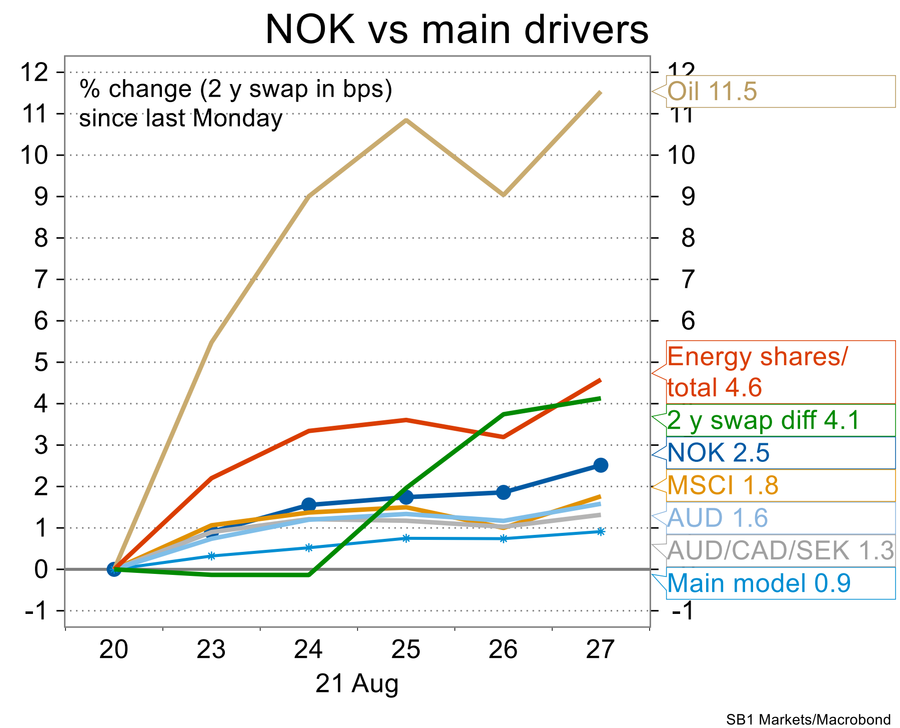
NOK up 2.5%, supported by oil, int. rates, fx peers & global stock markets

Our traditional model suggested an 0.9% appreciation





The status vs. the normal drivers:

- ***The NOK is 6% weaker than suggested by our standard model (from – 8!)***
- The NOK is 6% 'weaker' than the global stock market vs the correlation between the two since beg. of 2020 (from -7)
- The NOK is 9% weaker than our AUD/CAD/SEK-model, our 'super-cycle peers', predicts (from -10)
- NOK is far (10%) stronger than a model which includes global energy companies equity prices (vs the global stock market) (from 9)

After been neutral vs NOK from May, we turned positive in early July, as the gap vs. our models had widened. *We have been wrong but less so now* ☺

At this and the following pages we have swapped Norges Bank's I44 index for JP Morgan's broad NOK index and rebased it to the current index value for the I44. The I44 has an earlier closing time than the 'official' closing time for fx crosses. There are no substantial difference between these two indices over time

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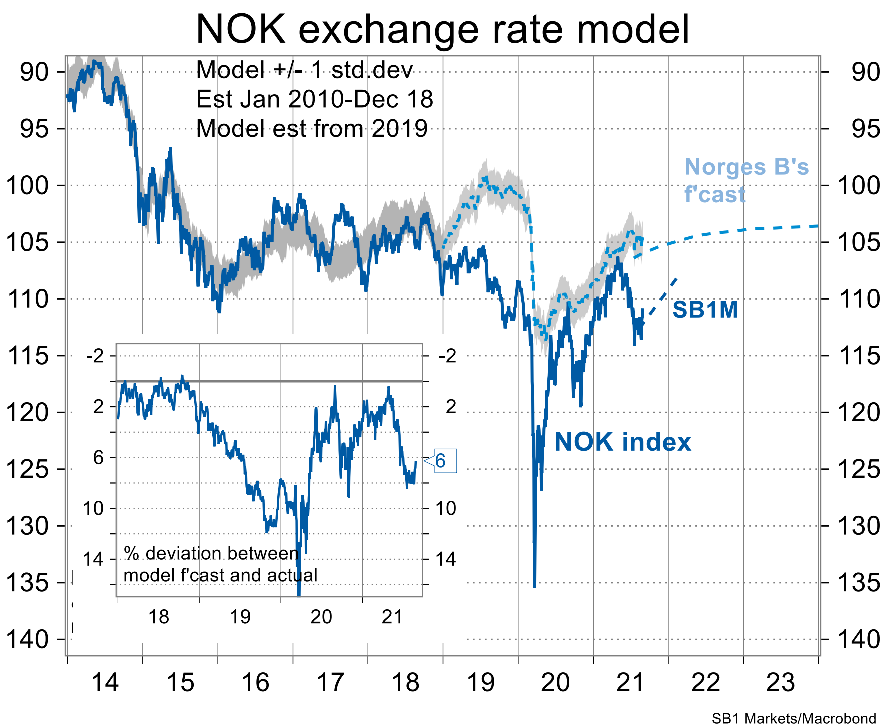
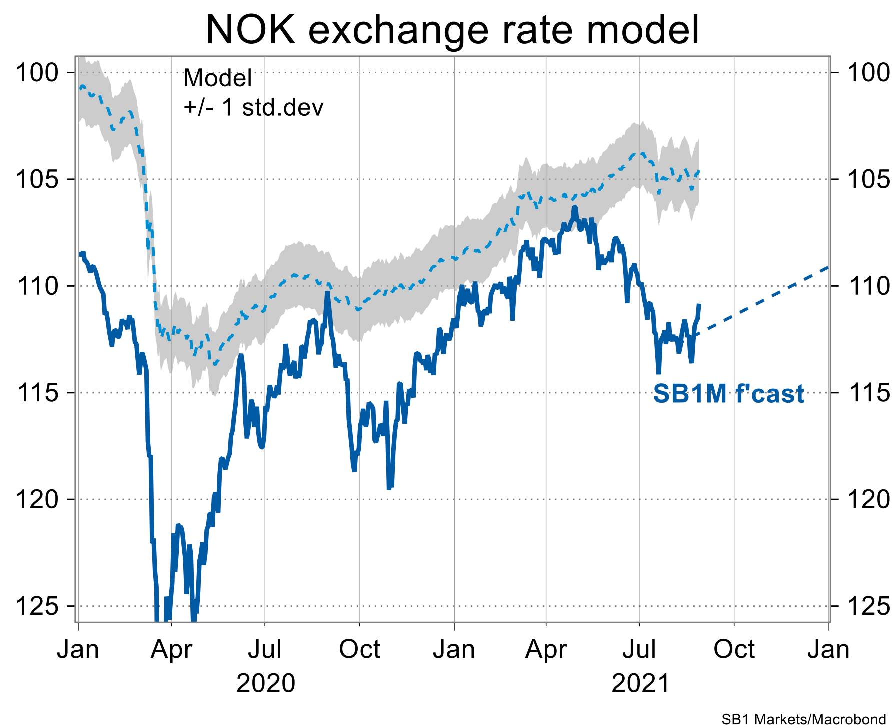
NOK 'just' 6% below our model estimate, from -8%

The gap narrowed last week





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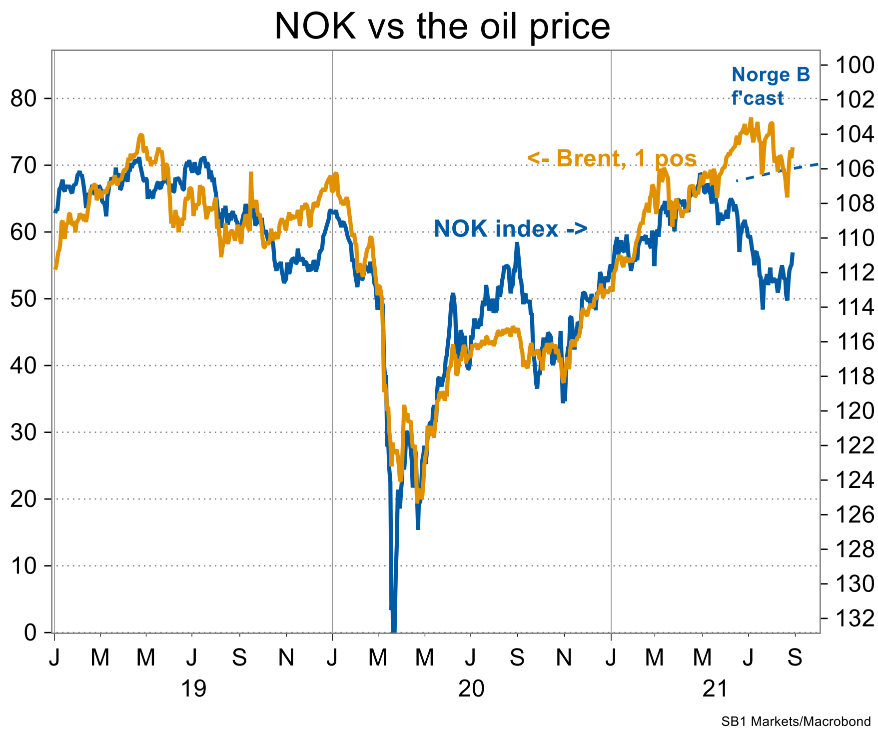
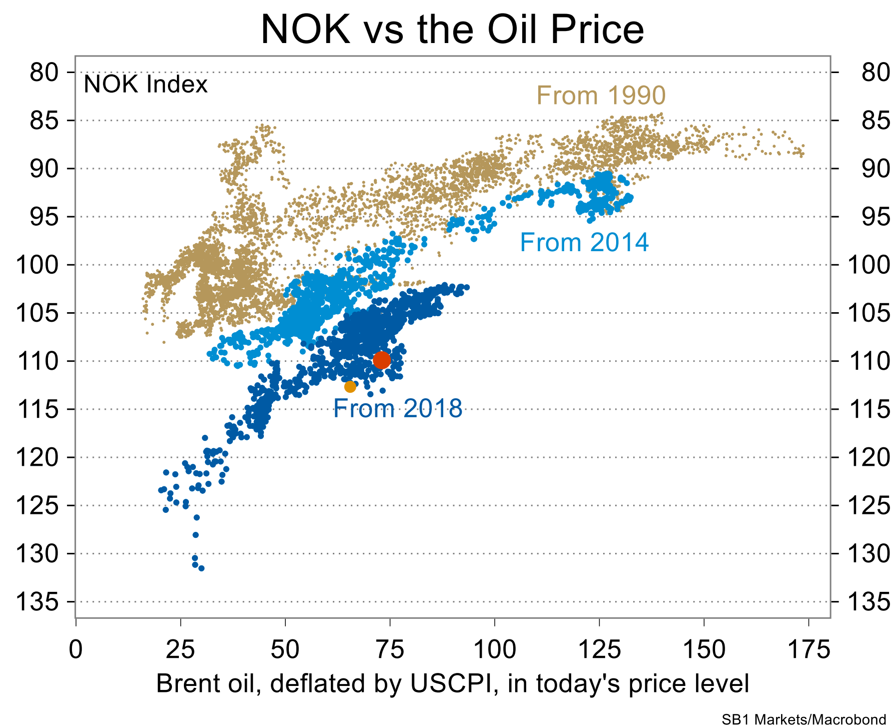
Oil & NOK sharply ~~down~~ up

The NOK is still on the weak side vs the oil price

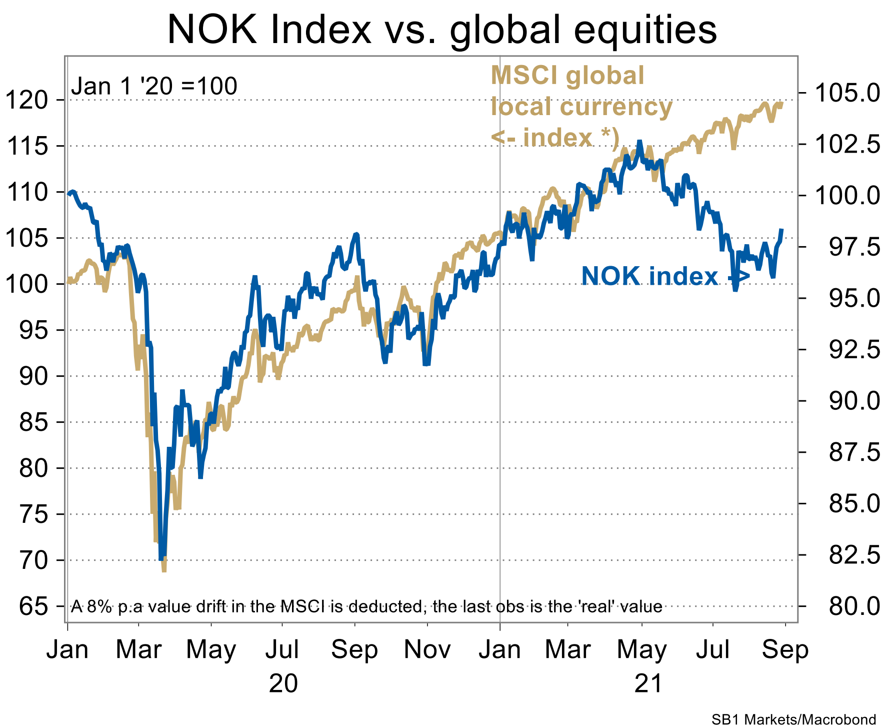


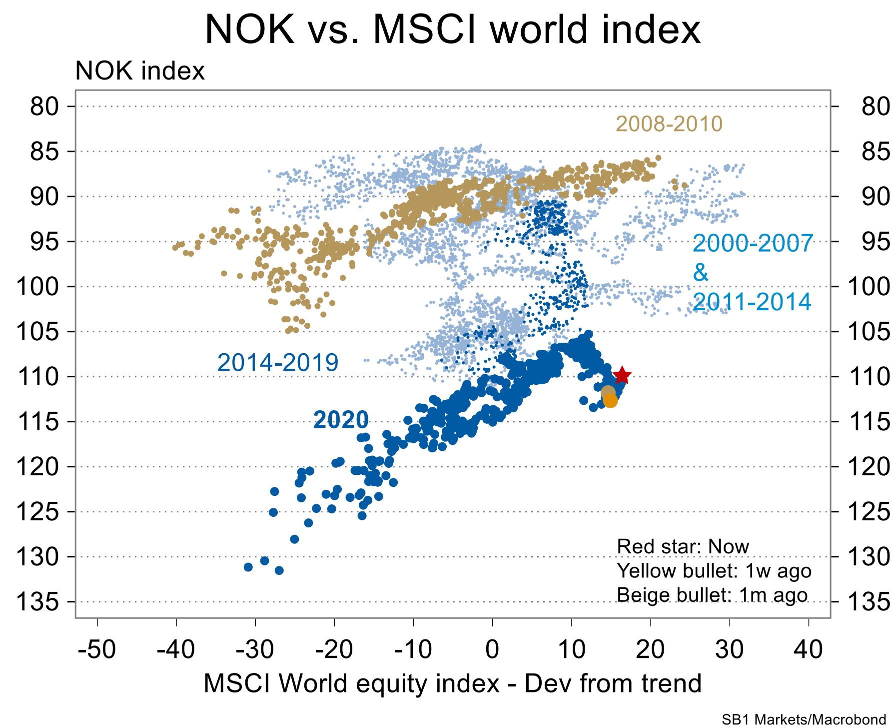


- NOK is still correlating quite closely to the oil price but at a lower level than before 2018 – and now the NOK is weak even vs the past 3 years' relationship
- A USD 10 drop in the oil price weakens the NOK by some 2.5%, as a partial effect.
  Within a broader model, the impact is somewhat smaller

The global stock market up, NOK even more

Still, NOK has lost some 6% vs. global stocks since May but 'gained' 1% last week





- 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

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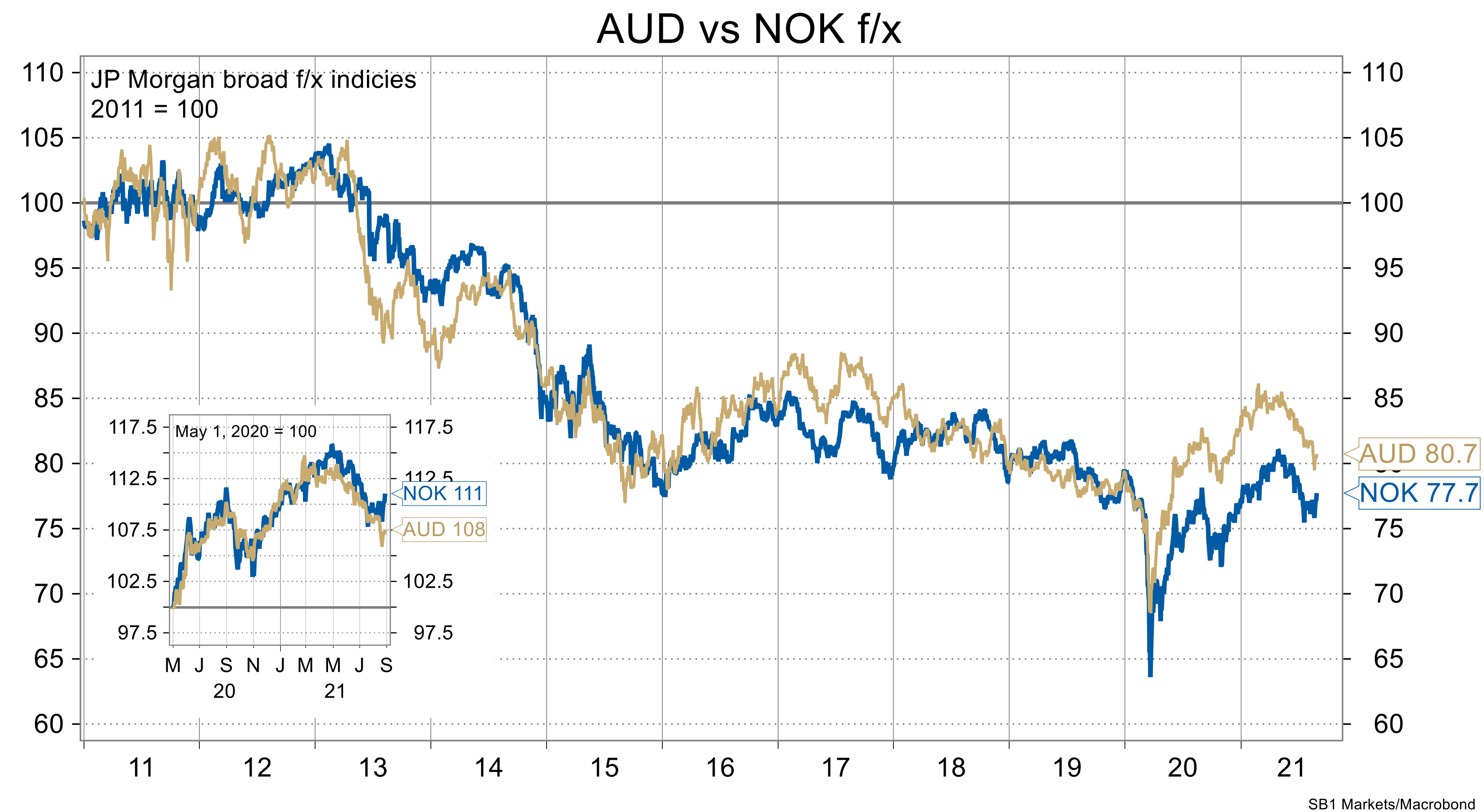
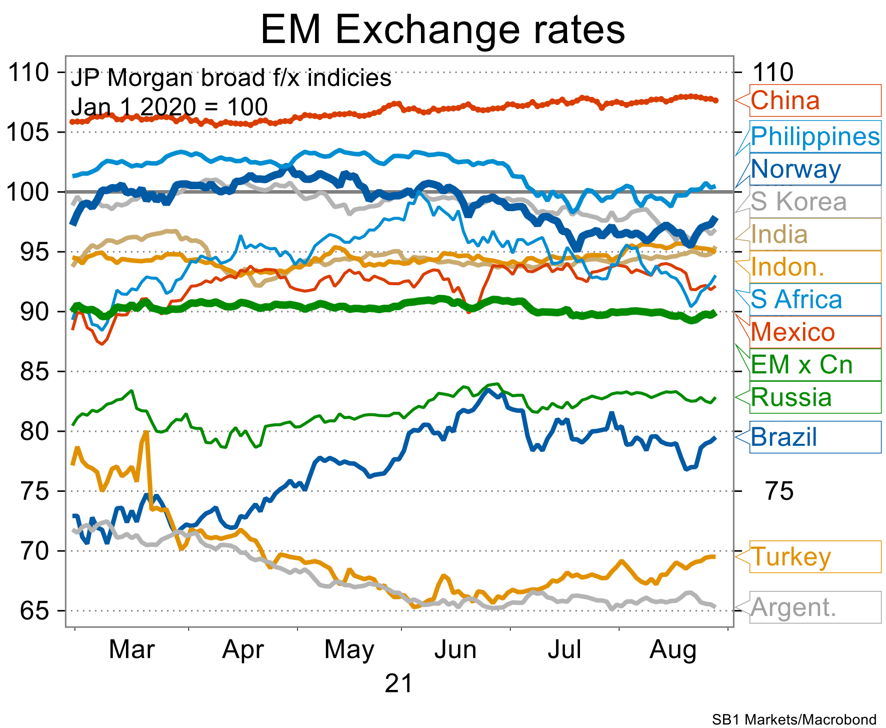
NOK & AUD still dancing extremely tight

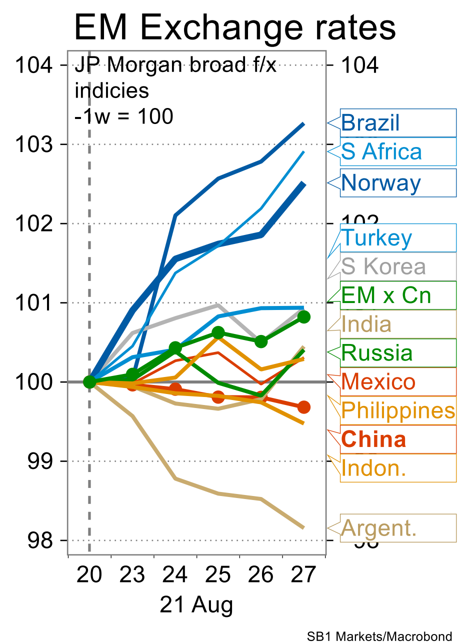
But the AUD has been a tad weaker past 2 weeks, partly due to weak iron ore prices

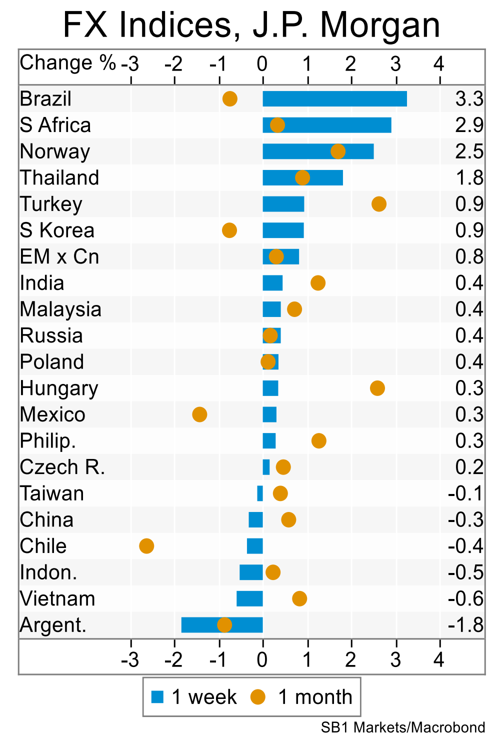


EM x China f/x sharply up last week, no taper tantrum

… and Powell is not signalling willingness to hike rates anytime soon







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