31 January 2022

Macro Weekly

Week 5/2022

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Highlights

The world around us

The Norwegian economy

Market charts & comments

Last week: Omicron is not harmful, Omicron measures are

.. At least in well vaccinated countries, and the pandemic is soon behind us?

- **Omicron has not been able to create any health challenges** in countries with a high vaccination rate
  - » It is rather the opposite, as Omicron burns rapidly through the population without creating too much sickness and need for hospital support, even more immunity is build up, hopefully vs. future variants, at least vs. serious illness
- **UK** (two weeks ago) and **Denmark** (last week) decided to lift all covid (or at least most) restrictions. **Norway** could have followed suit but we assume that most restrictions will be lifted this week
  - » The number of hospitalised persons have increased in both UK and Denmark but fewer need ICU treatment. In UK both the no. of cases and hospitalised persons have fallen. In Norway the no. of new hospitalisations has increased marginally but not the no. of patients that are still hospitalised is stable, and fewer patients need an ICU bed. The health cost – and even more the risk for a rapid rise in costs is negligible – and very likely not comparable to the cost of the remaining restrictions
- **US** may have turned the corner, the no. of new cases and hospitalised patients are now falling
- **China is still an unknown case.** The combination of a very contagious variant, with an R0 at 2.5 – 3 times Delta (and Delta managed 3 – 4 new infections per infected), few people that are immune due to previous infections, a vaccine that is not that effective, and a zero tolerance policy will require long lasting, extreme restrictions too succeed (if possible at all). Supply chain disruptions due to Chinese lockdowns may become a global challenge
- There are still many reports that many more patients **are admitted to hospitals with Covid, but due to other diagnoses**, and not due to Covid illness. Typically 50 – 60% of those counted as Covid patients are not admitted due to Covid which underscores the mildness of the Omicron variant

The economy, part I

- **January preliminary PMIs**
  - » Much weaker than expected, especially in US survey. Both services and manufacturing were weaker in the US, in the EMU services disappointed somewhat (even if German services surged, alongside manufacturing), and the first Chinese PMIs were much weaker than expected. Global growth is signalled at 2% from 4% in December, as the global PMI may have fallen by 3 p to just above 51. Omicron or something more lasting? Peak growth is behind us but we do not expect a sudden halt – and blame the virus for the abrupt setback in

Last week: The economy, part II

- **USA**
  - » **The FOMC - or at least Powell -** was more hawkish than expected. Rates surged during his press conference. Powell describes that the current situation is not comparable to 2015, when the last tightening campaign started; Inflation is much higher, the labour marked tighter and the economy much stronger, signalling willingness to hike rates rather rapidly. He stressed that the FOMC is ready to do what is needed. The timing of a moderate reduction of the bank's holdings of bonds had not been discussed in detail but a QT could start not a long time after the first hike in signal rate (by not reinvesting all proceeds from the current stock). The FOMC/Powell signalled that a March hike is a done deal – we assume barring a troublesome war, a stock market crash (down more than 20%?), or a terrible new virus mutant. Market is reasoning on a 50 bp hike, and the Fed funds future contracts signal that 5 or more hikes are more likely than 4 or less, following a sharp lift in the short end of the curve last week
  - » **The Employment Cost Index** rose 1.0% in Q4, 0.2 pp less than expected. However in the private sector costs rose 1.2% (4.7% annualised), and annual growth reached 4.4%, far higher than before the pandemic. All other wage indicators signal higher wage growth too
  - » **GDP** rose 6.9%, not because domestic demand or net trade was strong (1.9% and a -0.4 pp contribution resp.) but because inventories accelerated sharply, explaining 5 pp of the 6.9%. Inventories were growing faster than normal in Q4, but following the rundown in Q1, now problem, short term. **Consumption** fell in December, due to a 3% decline in consumption of goods. **Nominal GDP** grew 14.4%, and we assume that **profits** rose even faster, lifting the profit share further
  - » **Durable orders** are still going pretty strong overall but growth in orders for investment goods have slowed
  - » **New home sales** were better than expected in Dec. Existing home prices rose more than expected too (and are up 18% y/y, and almost 30% since before the pandemic!)
- **EMU**
  - » **GDP** fell at 2.8% pace (0.7% not annualised) in Germany in Q4, but activity rose in both France and Spain, and in Spain at brisk pace (8%)
- **Sweden**
  - » **GDP** rose further in December, and by 5.6% in Q4 – even if **retail sales** surprisingly fell by 4.4% in December
- **Norway**
  - » **The NAV ordinary full time** unemployment rose just by 0.1 pp to 2.4% in January, as we expected, 0.1 pp below consensus (based on non seasonal adj. estimates) and 0.6 pp below NoBa's f'cast (in the Dec MPR). Part time unemployment rose even less, and the no of new vacancies rose again. **Payrolls** rose by 0.4% in December, lifting the level to 2.3% above the Dec. 19 level, at least by mid Dec. **The LFS** (AKU) survey confirms a strong labour market: **Employment grew**, and **unemployment fell by** 0.1% to 3.5% (as we expected, consensus unch). The Omicron variant has not at all hurt the Norwegian labour market or economy by much – and the reopening must be just around the corner
  - » **Retail sales** fell 3.1% in December, far weaker than out -1% f'cast (consensus -0.3%). Some temporary factors we assume but the trend is down. The overall level is not that high anymore
  - » **Hotels** were hurt by Omicron & restrictions in December. The number of guest nights fell by 25% vs the normal level reached in Oct & Nov

The Calendar: PMIs, US labour market, ECB, BoE, EMU inflation, growth. Norw. house prices

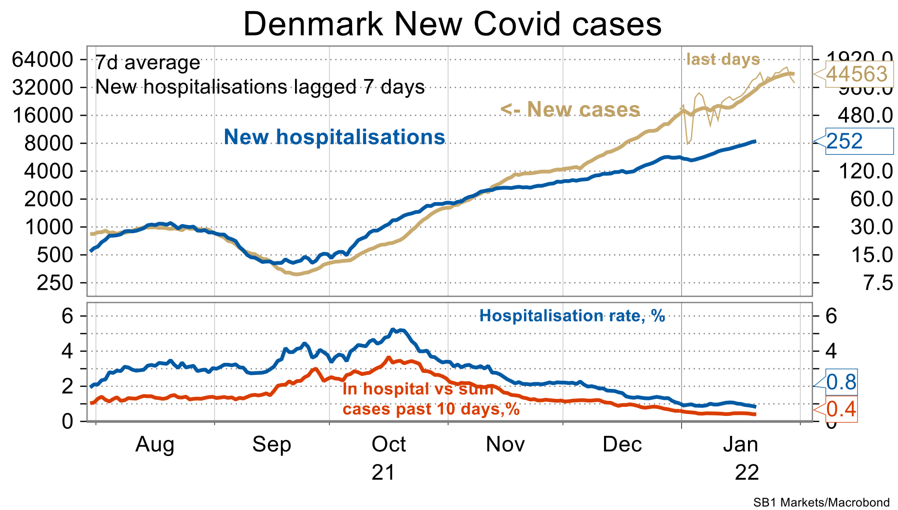
Time	Count.	Indicator	Period	Forecast	Prior
Monday Jan 31					
08:00	NO	Credit Indicator Growth YoY	Dec	(5.2)	5.1%
11:00	**EC**	**GDP SA QoQ**	**4Q A**	**0.4%**	**2.2%**
14:00	GE	CPI YoY	Jan P	4.4%	5.3%
Tuesday Feb 1					
08:00	GE	Retail Sales MoM	Dec	-1.4%	0.6%
08:30	SW	Manufacturing PMI	Jan		62.1
10:00	EC	Manufacturing PMI	Jan F	59	59
10:00	NO	Manufacturing PMI	Jan	(56)	58
11:00	EC	Unemployment Rate	Dec	7.1%	7.2%
15:45	US	Manufacturing PMI Markit	Jan F	55	55
16:00	**US**	**ISM Manufacturing**	**Jan**	**57.6**	**58.7**
16:00	**US**	**JOLTS Job Openings**	**Dec**	**10300k**	**10562k**
17:00	WO	Manufacturing PMI	Jan	(53.3)	54.3
	US	Auto Sales	Jan	12.65m	12.44m
Wednesday Feb 2					
11:00	EC	CPI Estimate YoY	Jan	4.4%	5.0%
11:00	**EC**	**CPI Core YoY**	**Jan P**	**1.80%**	**2.60%**
14:15	US	ADP Employment Change	Jan	220k	807k
Thursday Feb 3					
08:30	SW	Swedbank/Silf PMI Services	Jan		67.3
10:00	EC	Markit Eurozone Services PMI	Jan F	51.2	51.2
10:00	EC	Markit Eurozone Composite PMI	Jan F	52.4	52.4
11:00	EC	PPI YoY	Dec	26.1%	23.7%
11:00	**NO**	**House prices**	**Jan**	**(0.2%)**	**-0.2%**
13:00	**UK**	**Bank of England Bank Rate**	**Feb-03**	**0.5%**	**0.3%**
13:45	**EC**	**ECB Deposit Facility Rate**	**Feb-03**	**-0.5%**	**-0.5%**
14:30	US	Non-farm productivity	4Q P	3.0%	-5.2%
14:30	US	Unit Labor Costs	4Q P	1.5%	9.6%
15:45	US	Markit US Services PMI	Jan F	50.9	50.9
16:00	**US**	**ISM Services Index**	**Jan**	**59.5**	**62**
16:45	WO	Services PMI	Jan	(50.8)	54.6
17:00	**WO**	**Composite PMI**	**Jan**	**(51.2)**	**54.6**
Friday Feb 4					
08:00	GE	Factory Orders MoM	Dec	0.0%	3.7%
08:45	FR	Industrial Production MoM	Dec	0.5%	-0.4%
11:00	**EC**	**Retail Sales MoM**	**Dec**	**-0.8%**	**1.0%**
14:30	US	Change in Nonfarm Payrolls	Jan	175k	199k
14:30	**US**	**Unemployment Rate**	**Jan**	**3.9%**	**3.9%**
14:30	**US**	**Average Hourly Earnings MoM**	**Jan**	**0.5%**	**0.6%**
14:30	**US**	**Labor Force Participation Rate**	**Jan**	**61.9%**	**61.9%**
Monday Feb 7					
02:45	CH	Caixin China PMI Composite	Jan		53
02:45	CH	Caixin China PMI Services	Jan	50.3	53.1

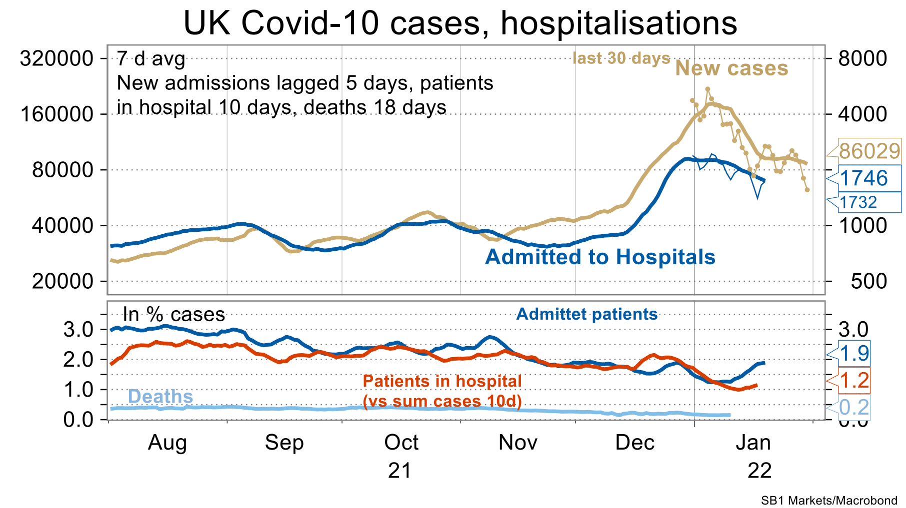
- **January PMIs**
  - » **The preliminary PMIs** signal a harsh downturn in January, by some 3 p to a below average level, signalling a 2% global growth rate, down from 4% in December. US contributed most at the downside, and **the ISMs** will be even more exciting than normal. The problem is that we will not know how much we can blame the (last?) virus wave, and how much is an underlying weakening of growth. We assume that growth will slow, at least in the rich part of the world – but not at a pace that the Dec to Jan PMIs signal. Delivery times are easing, as are prices
- **USA**
  - » **The labour market is tight**, which the Federal Reserve is now also acknowledging. The question is if there are some signs of easing or not. The payroll figure does not tell much, participation, unemployment and wage are far more important. The SMEs (NFIB) will also publish its assessment of the labour markets. In addition, the JOLTS report will reveal the number of unfilled vacancies
- EMU
  - » **The ECB** board will probably not signal new policy measures this week. A measured tapering is decided, and the policy rate will not be hiked anytime soon
  - » **The annual CPI inflation** rate will 'collapse' in January, due to the base effect - prices rose sharply in January 2021. A core rate below 2% will be good news ahead of the ECB board meeting
  - » **Q4 GDP** is expected up 0.4% (1.6 annualised) in Q4, we think that's a tad too optimistic
  - » **Unemployment** is steadily falling, and a further decline is expected in December
  - » December **retail sales** is expected down – like in so many other places
- **UK**
  - » **Bank of England** will very likely add 0.25 pp to the bank rate, and lift it to 0.5%. Inflation has surprised at the upside – and the BoE has been sending clear messages
- **Norway**
  - » We expect **house prices** to have appreciated marginally in Jan, reversing the decline in Dec. No doubt, higher interest rates are dampening demand. The flow (strong sales) & inventory data (record low) suggest a 0.75 – 1% pace of monthly price increases

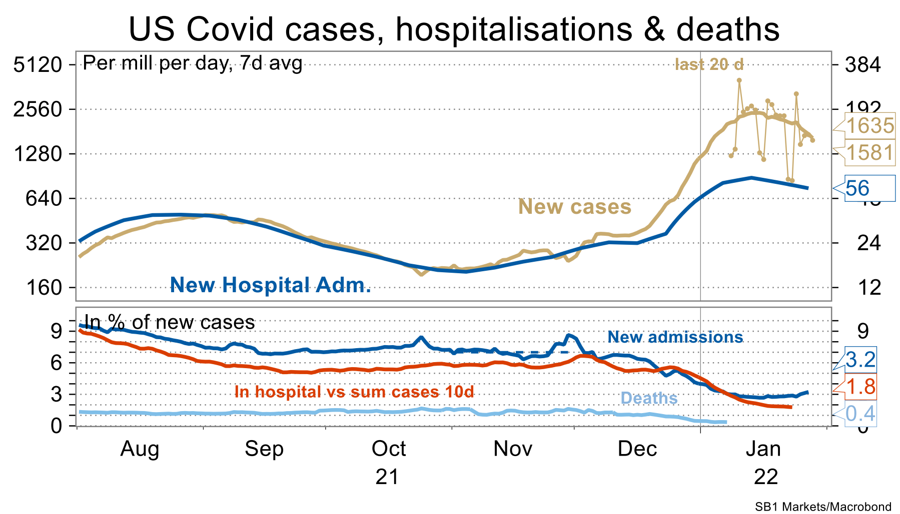
Sources: Bloomberg. SB1M est. in brackets. Key data are highlighted, **the most important in bold**

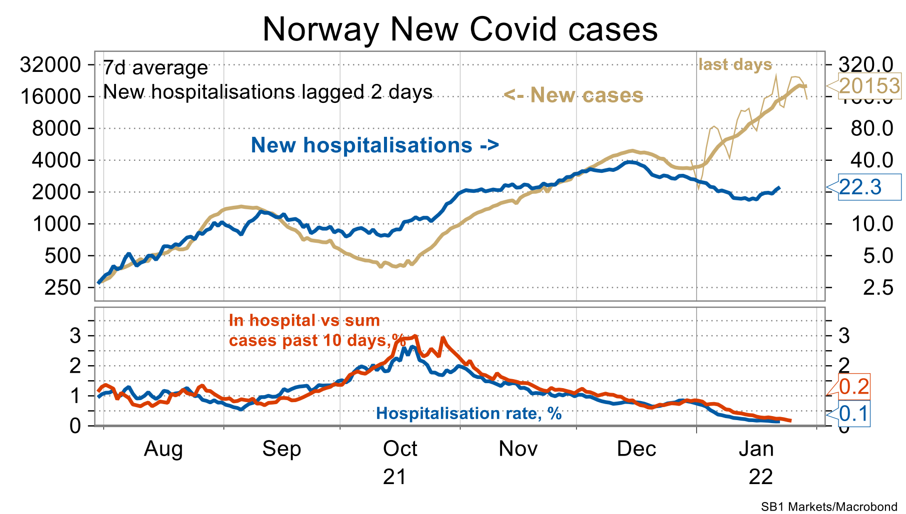
Denmark, Norway are reporting strong growth in new cases, a new variant around

However, so far no serious problems at hospitals (see next page). Cases are flattening i US, -50% in UK









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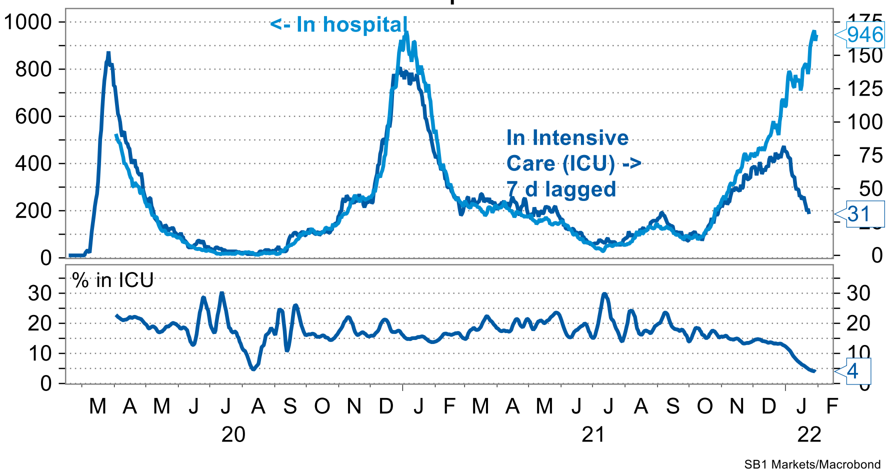
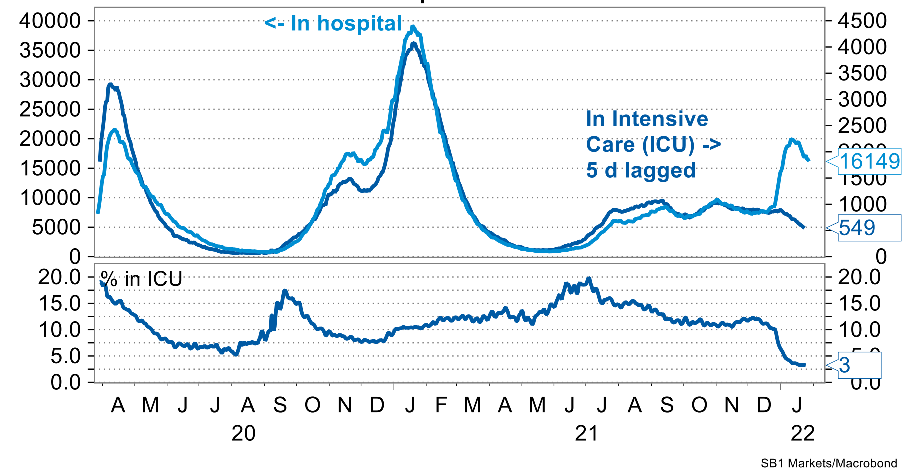
US hospitals are ~~not~~ over the hill, and there are fewer ICU patients everywhere

These are really encouraging data points. Norway should no doubt lift most of restrictions this week

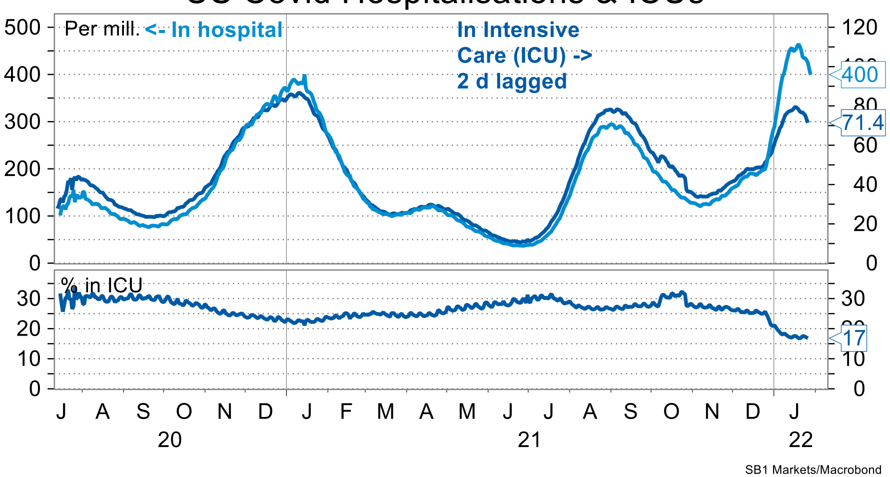
Denmark Covid Hospitalisations & ICUs



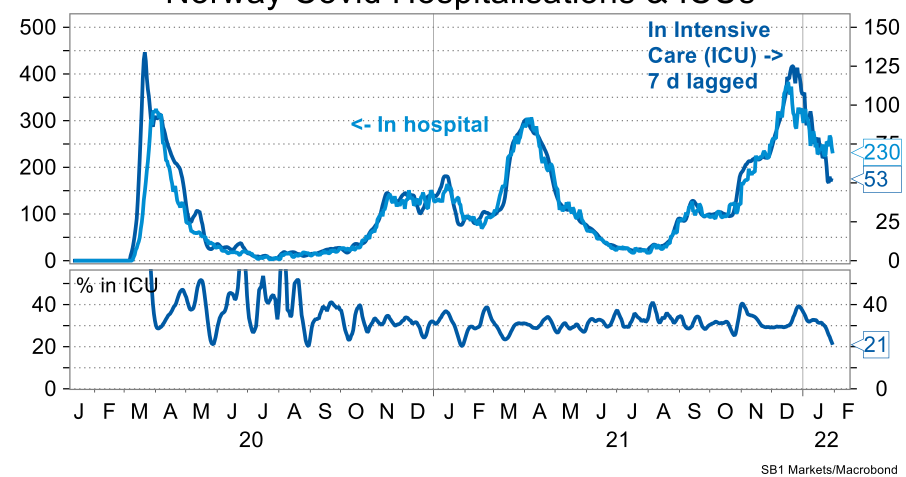
UK Covid Hospitalisations & ICUs



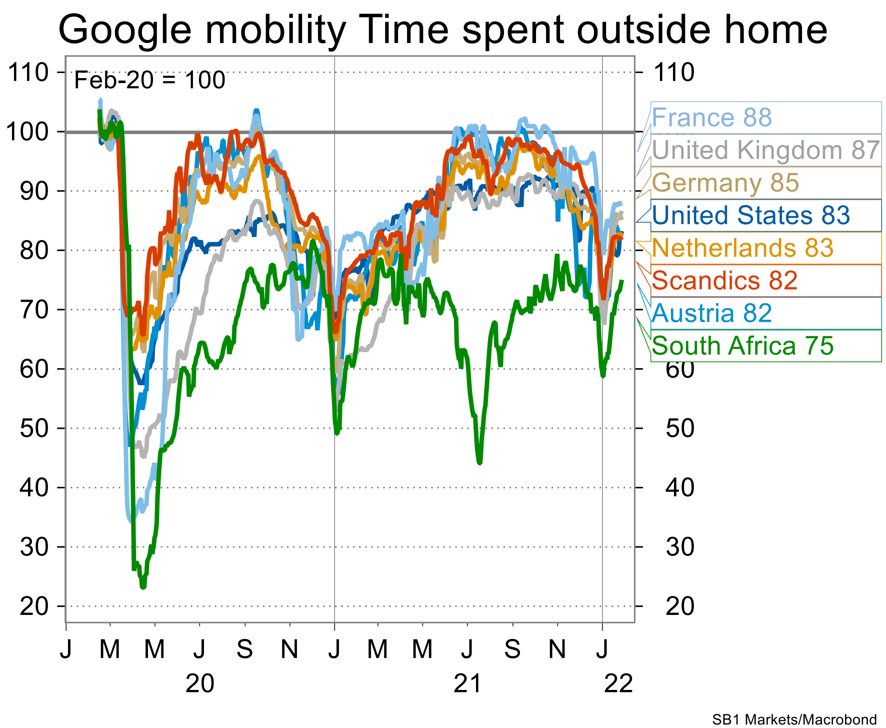
US Covid Hospitalisations & ICUs

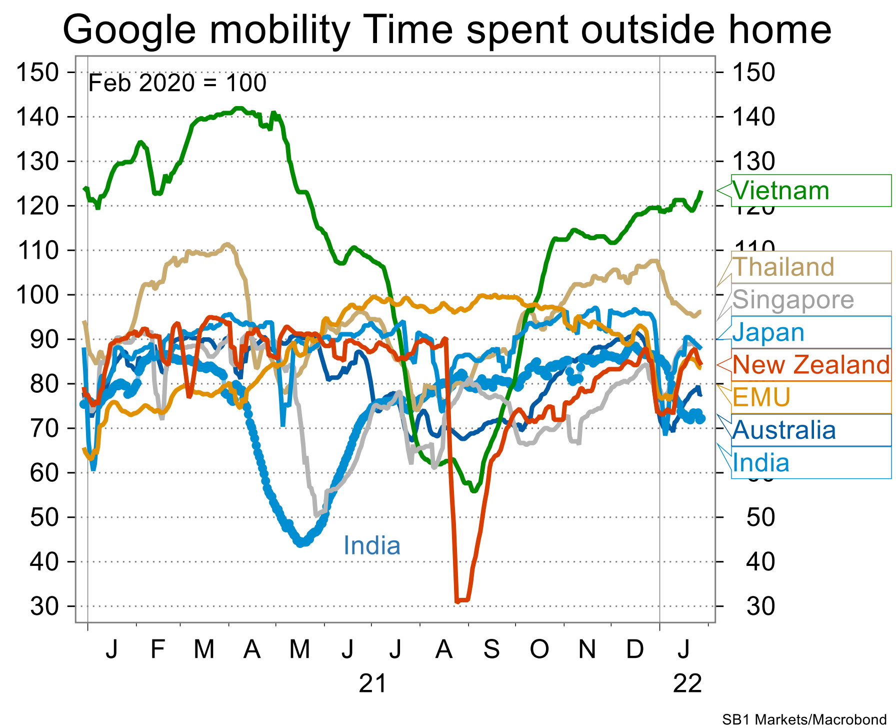


Norway Covid Hospitalisations & ICUs

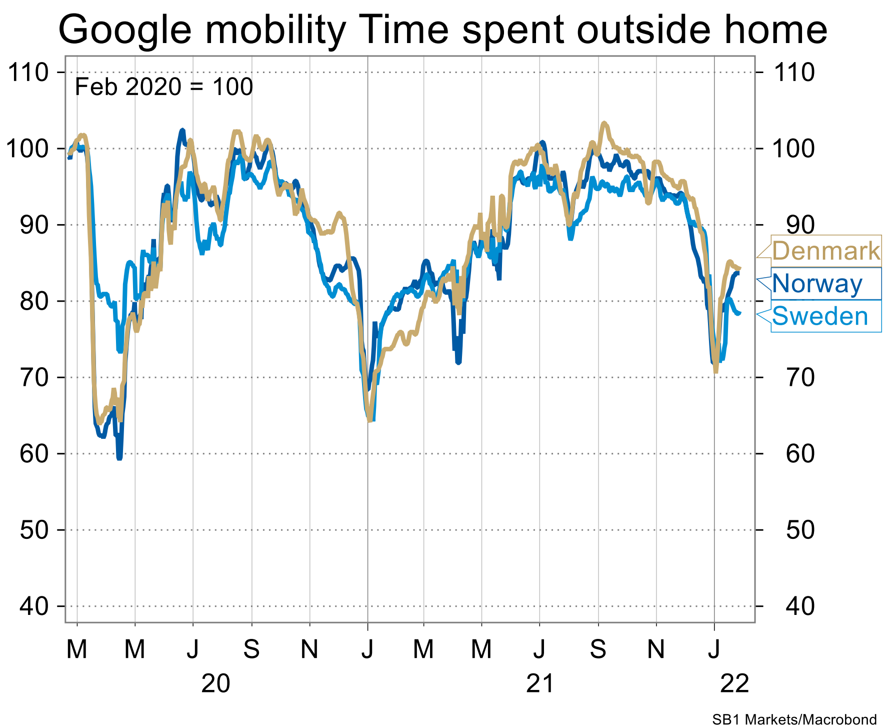


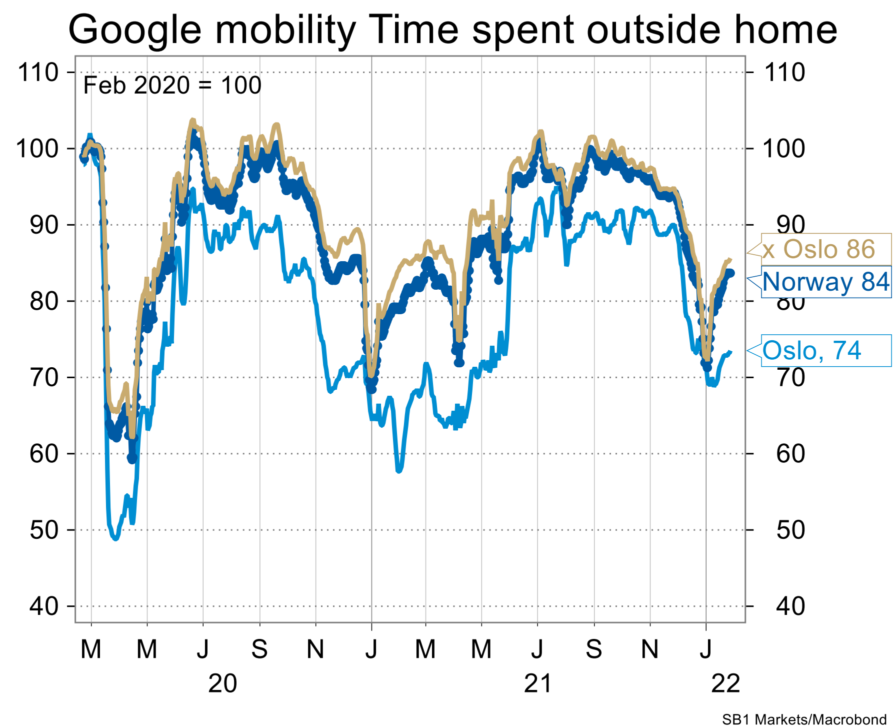
Mobility on the way up in the West, some challenges in the East?





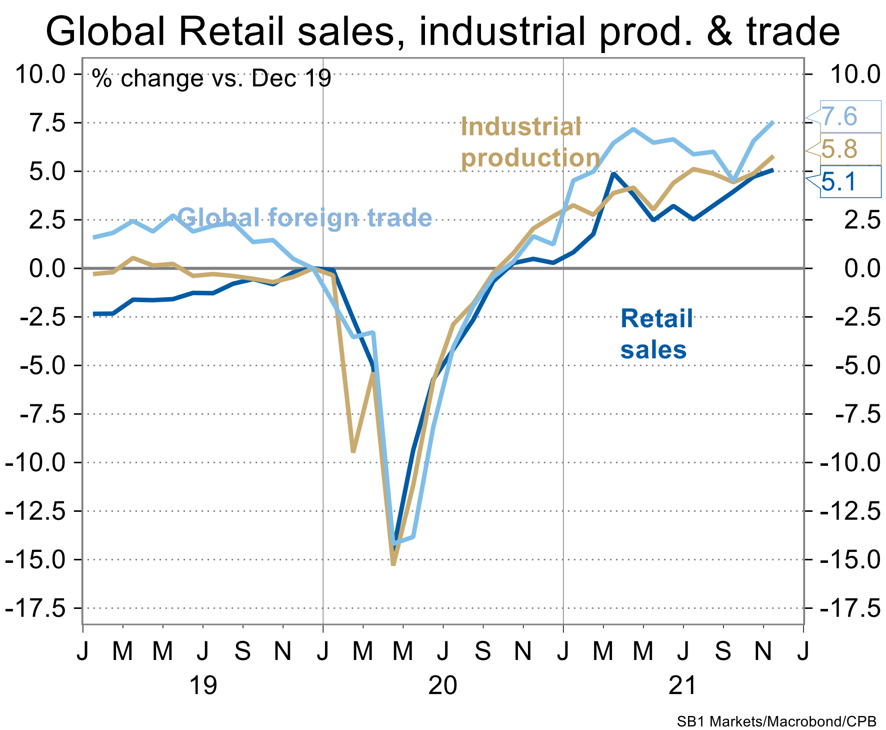
Less fear for Omicron in the Scandics as well – and some restrictions are eased

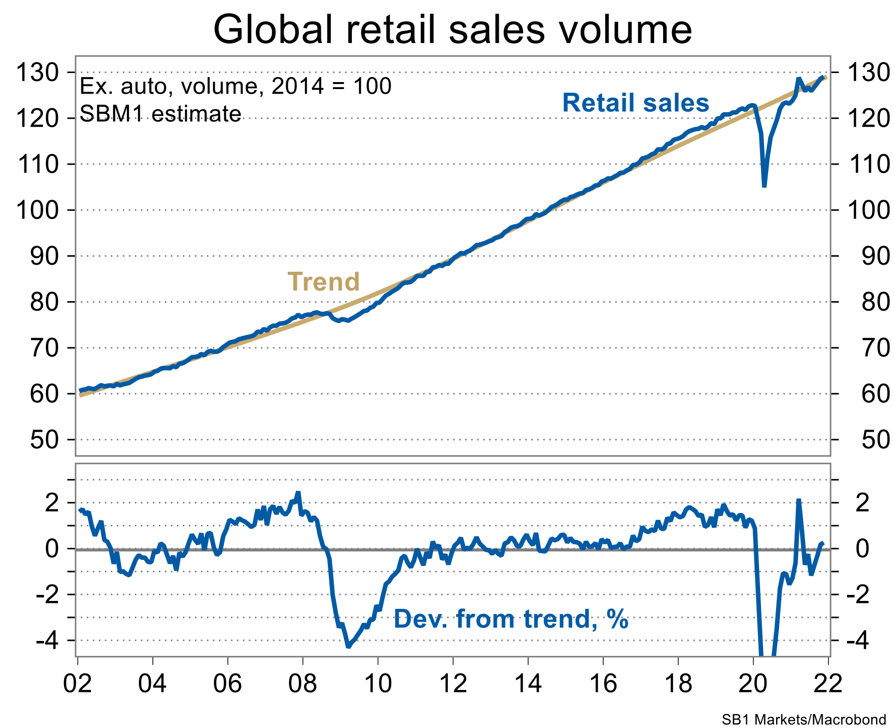




Global retail, industrial production & foreign trade have strengthened recently

Global trade is recovering again – at least well up in both October and November

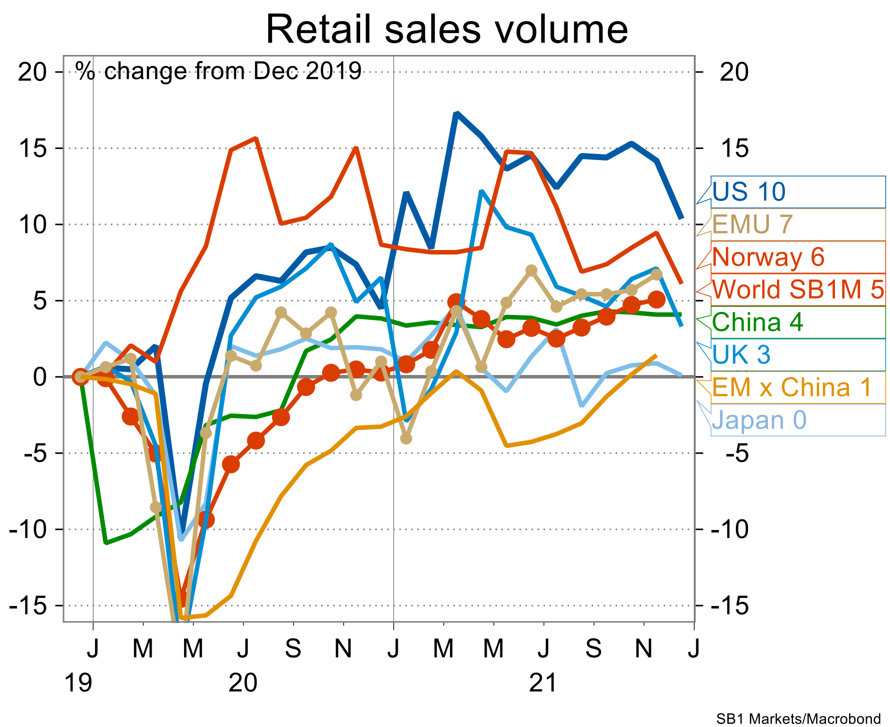


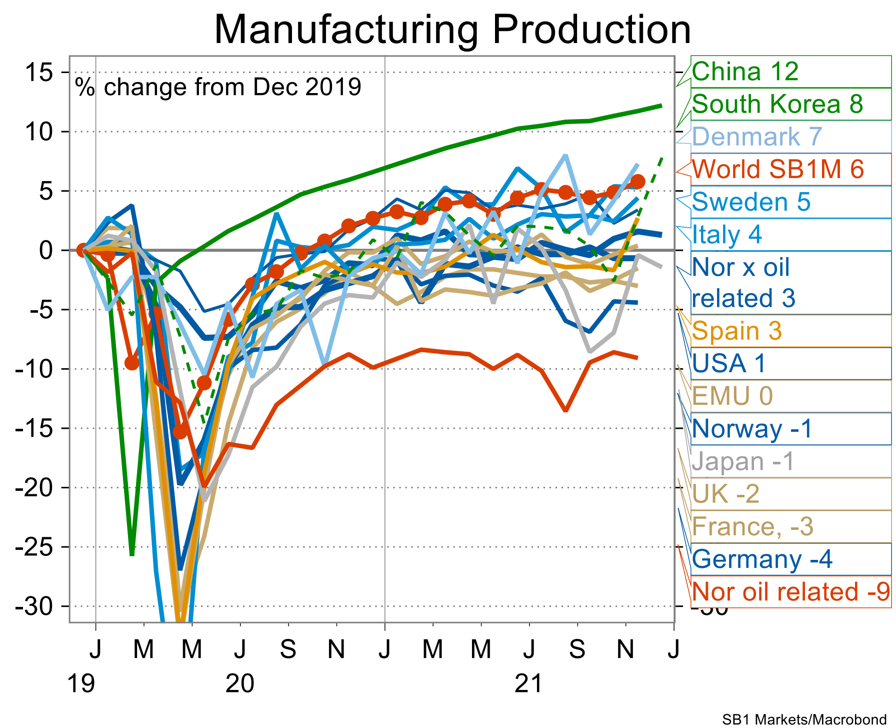


- **Global retail sales** rose at slower pace November, with slow/no growth. China & US on the downside, EMU surprised at the upside. Global sales (mostly excluding autos) are 5% above the pre-pandemic level. We have not yet finalised the first Dec estimate but sales very likely fell significantly, led by the US
- **Global manufacturing production** has recovered since the summer, and growth was strong in both October and November – the latter due to 6 – 7% growth in both South Korea and Japan. Production is up 6% from Dec-19
- **Global foreign trade** rose sharply in Oct/Nov, following the setback in September (and several weak months since last May). Trade is up 7.6% vs. Dec-19

DM demand for consumer goods have peaked, EMs are recovering from a low lev.

The upside potential is large for Emerging Markets x China, and the recovery has started





- **Retail sales** in Emerging Markets x China are recovering but is far below pre-pandemic trends
- **US retail demand is** fell sharply in December, however mostly due to another weak December for internet sales. A recovery in January? Still, the trend is flat, at the best – and the level too high. Some other rich countries have reported lower sales in December (like UK, Sweden and Norway)
- **Manufacturing production** has been hampered by a deep decline in auto production, but this sector is now recovering. The manufacturing PMIs are still strong, and delivery times very likely easing

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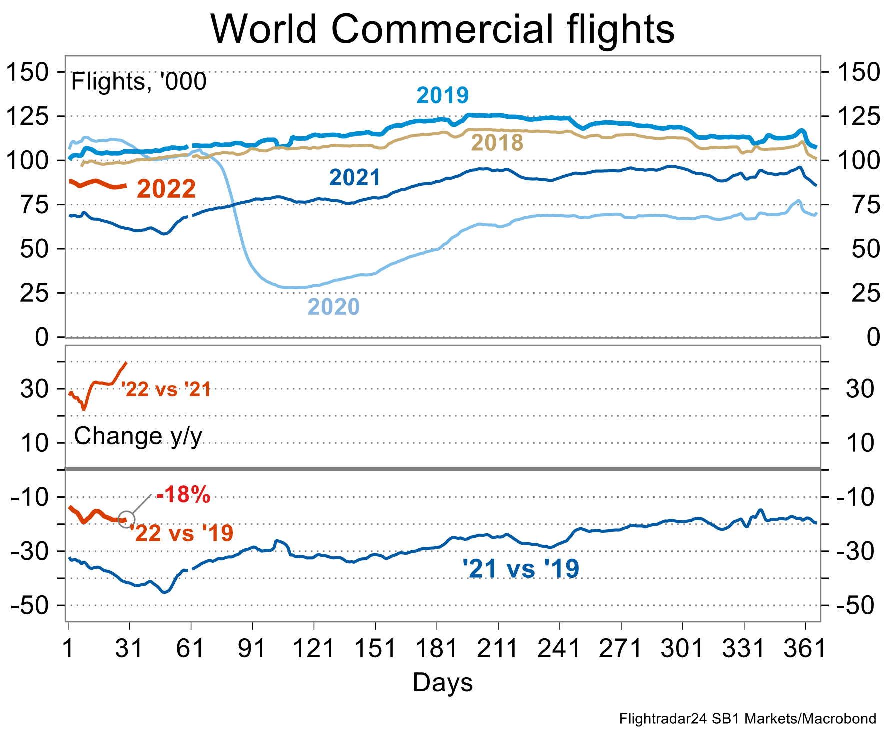
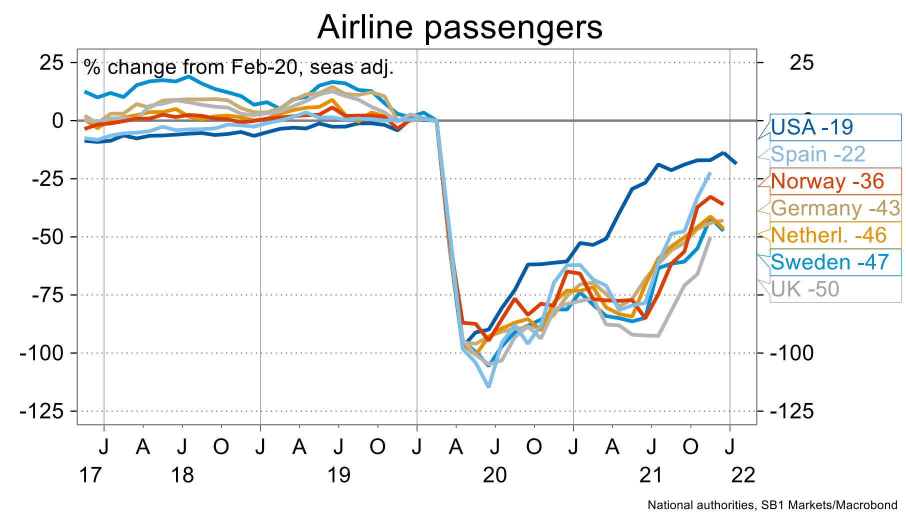
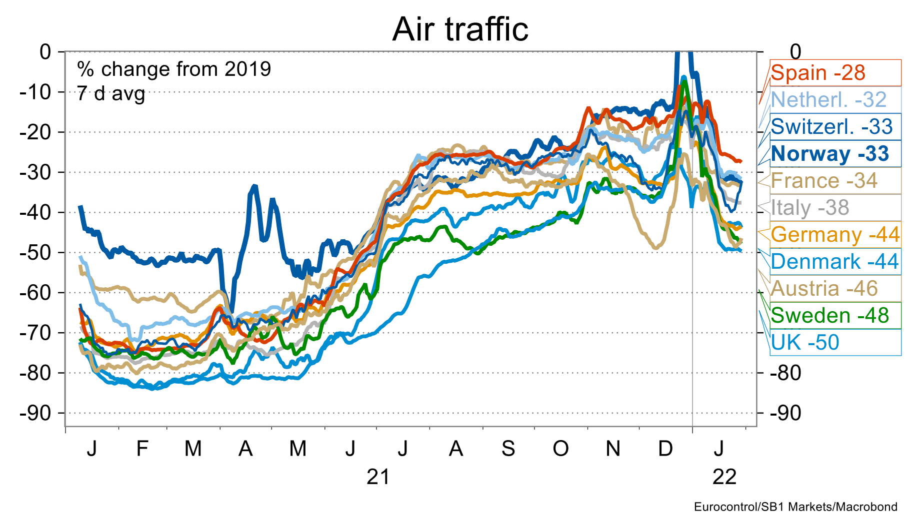
Global airline traffic still down 18% vs the 2019 level (but up 40% vs. 2021)

Omicron has not – at least not yet – killed global airline traffic. Some weakness in Europe though



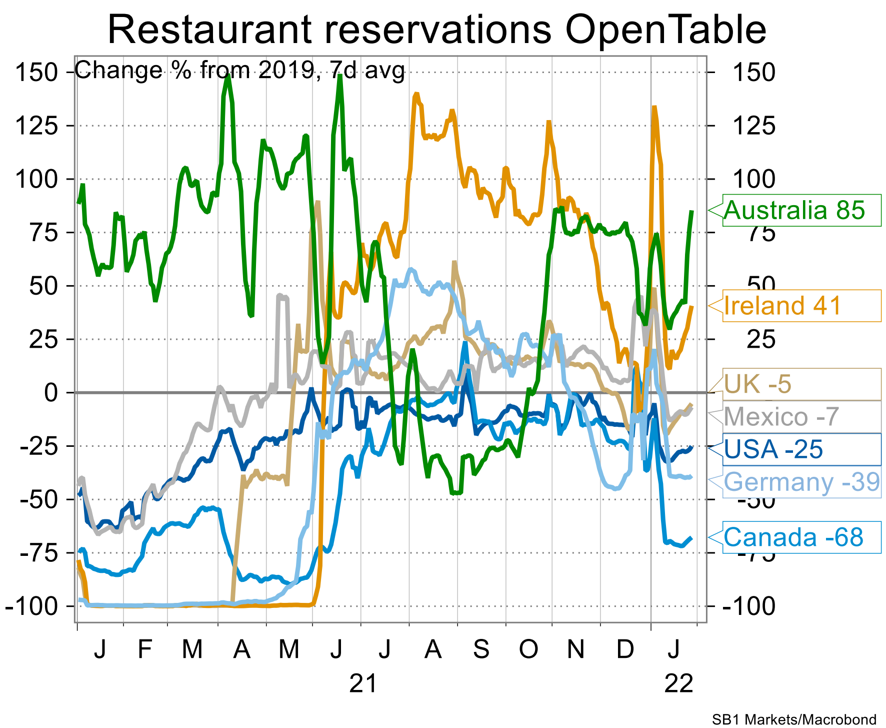


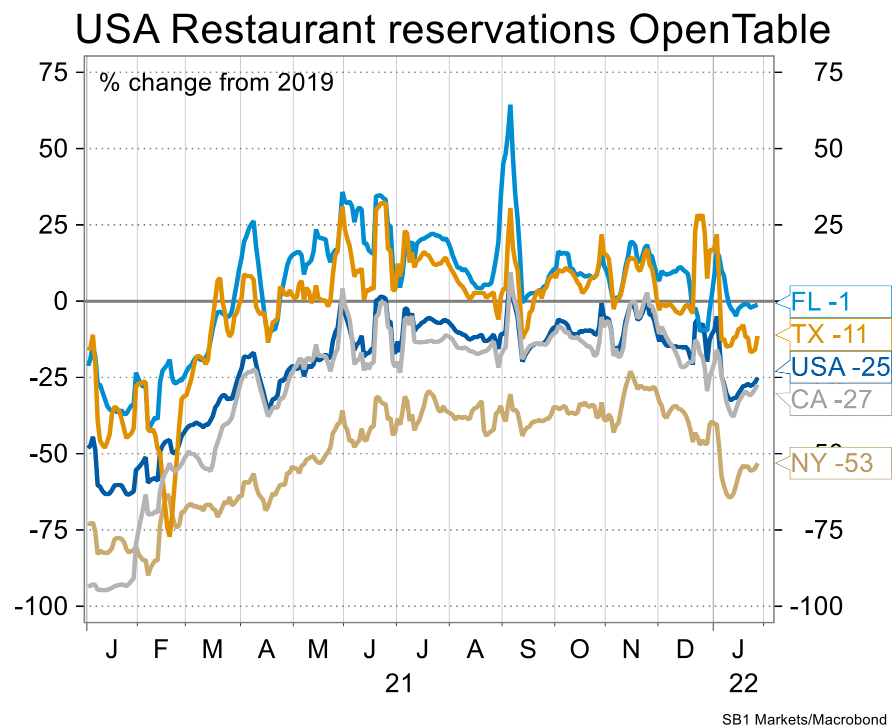


- Until November, strong growth in no. of passengers in Europe, and the gap vs the US was reduced
- The fight against the Delta reduced aircraft movements in Europe somewhat, and the Omicron may create more havoc for a while

More restaurant guests most places?

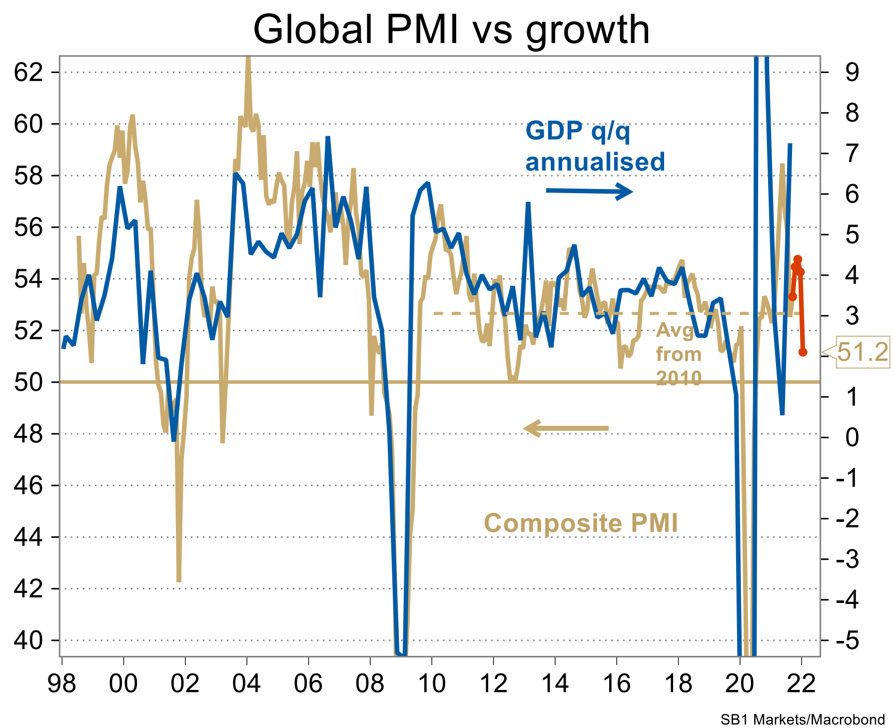
Data were volatile during the Christmans/New Year holidays but is the recent uptick for real?

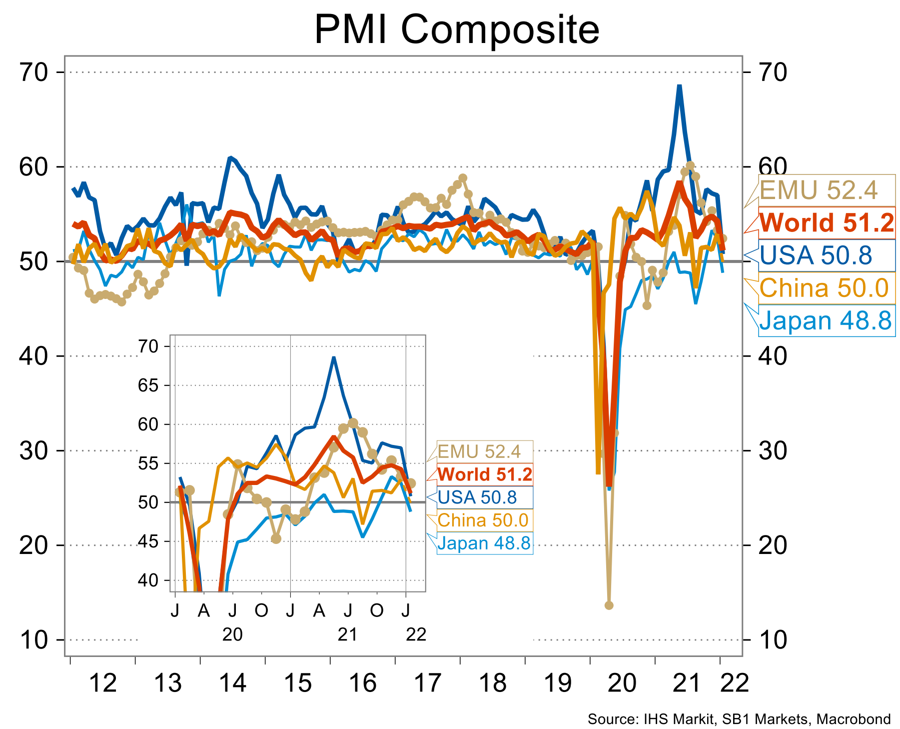




The preliminary PMIs sharply down in January, so far led by the US

We estimate a 3p+ decline m/m to 51.2, equalling 2 pp lower global GDP growth, down to 2%



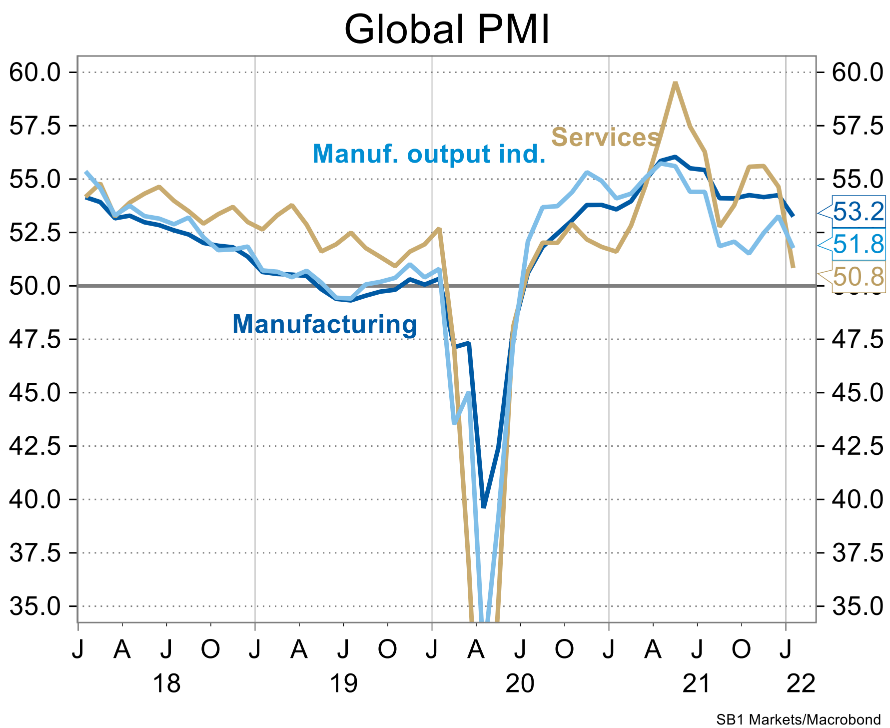


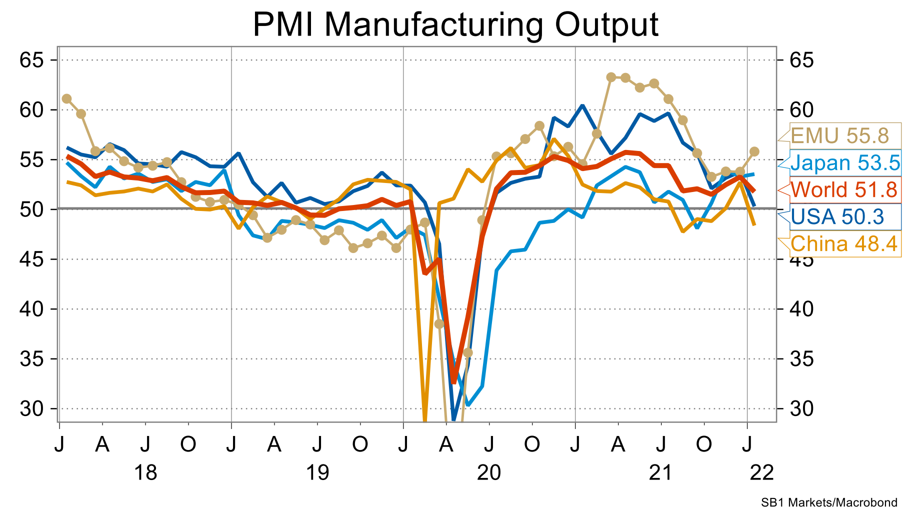
- **The flash composite PMI** January estimates declined, and more than expected everywhere (except for the UK). US surprised most at the downside, together with China, both in manufacturing and in services. Globally, the service sector index fell more than the manufacturing index (our est)
  - The EMU kept better up, as Germany surprised at the upside, big time, especially in services
- **The delivery times index** fell for the 3rd month in row – and **price inflation slowed, at least input prices**. The **order index** fell to an average level (manufacturing). We doubt a sudden corona related decline in demand explains the reduced pressure in the value chain but perhaps a gradual normalising of demand for goods in the rich part of the world an less hoarding after the Christmas season ease the supply chains bottleneck?
- Services are probably mostly hurt by the Omicron wave – and much more than expected. Can it be something more?

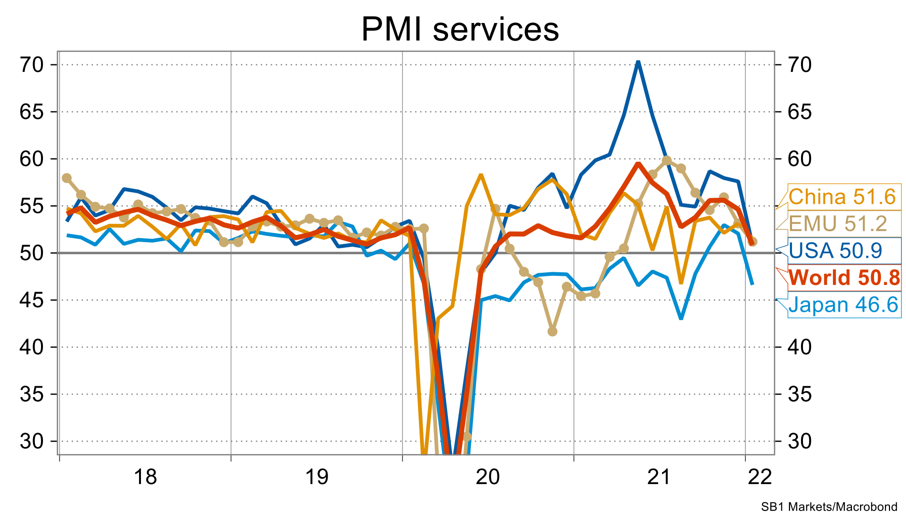
Our estimates are based on the preliminary PMIs from US, China, EMU, Japan UK, Australia. The estimates are uncertain, but usually by less than 0.5 p

A broad decline in growth in January. Is it just the (temporary) virus attack?

The service sector PMI probably down by almost 4 p, a very unusual setback. Manuf. output -1.5 p



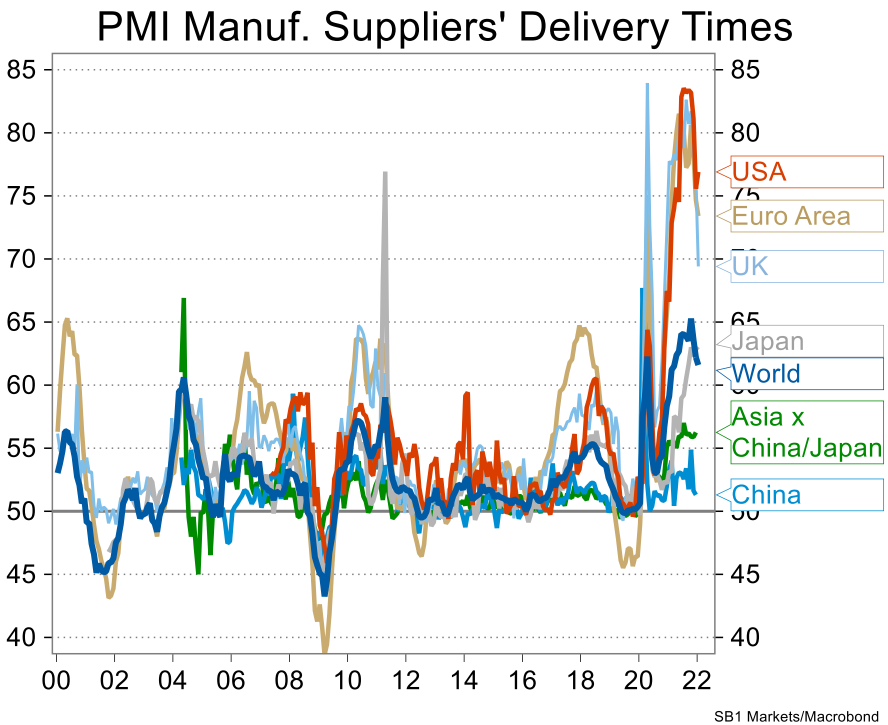


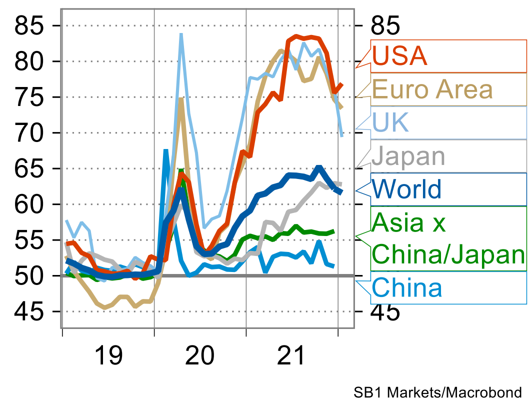


- Growth has very likely peaked, at least in the rich part of the world – but the setback in January is probably not the start of "the next recession"

Delivery times index further down in December

Are delivery times increasing less fast or are they slowing?



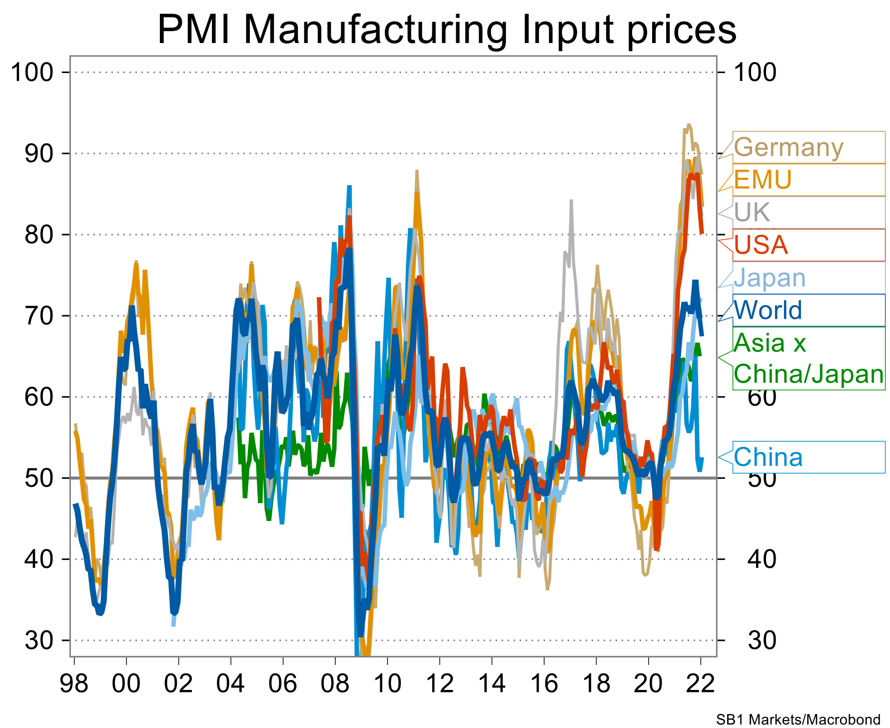


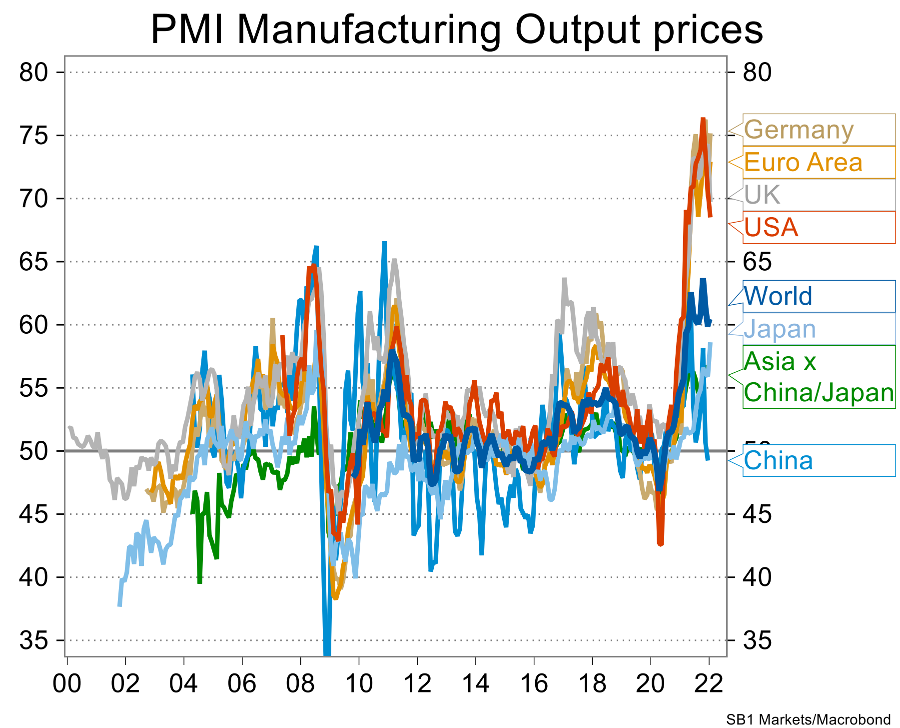
- Long delivery times have been a rich man's problem, while delivery times have not been that problematic in Emerging markets, China included

- **The global delivery times** PMI sub-index (changes in delivery times vs the previous month) inched down in both Nov, Dec and Jan, signalling some easing in congestion in the supply chains
- **The interpretation of this index is uncertain** – are companies really reporting changes in delivery times?
  - » This index as been above 50 most of the time (the past 20+ years), signalling longer delivery times. However, delivery times have not increased almost all the time – they have rather fallen! Companies may be reporting the level of delivery times. If so, delivery times are now contracting – while the index formally reports than delivery times are increasing at a marginally slower pace

Price indices have peaked – raw material prices have calmed down

However, companies are still reporting very rapid price growth in the rich part of the world

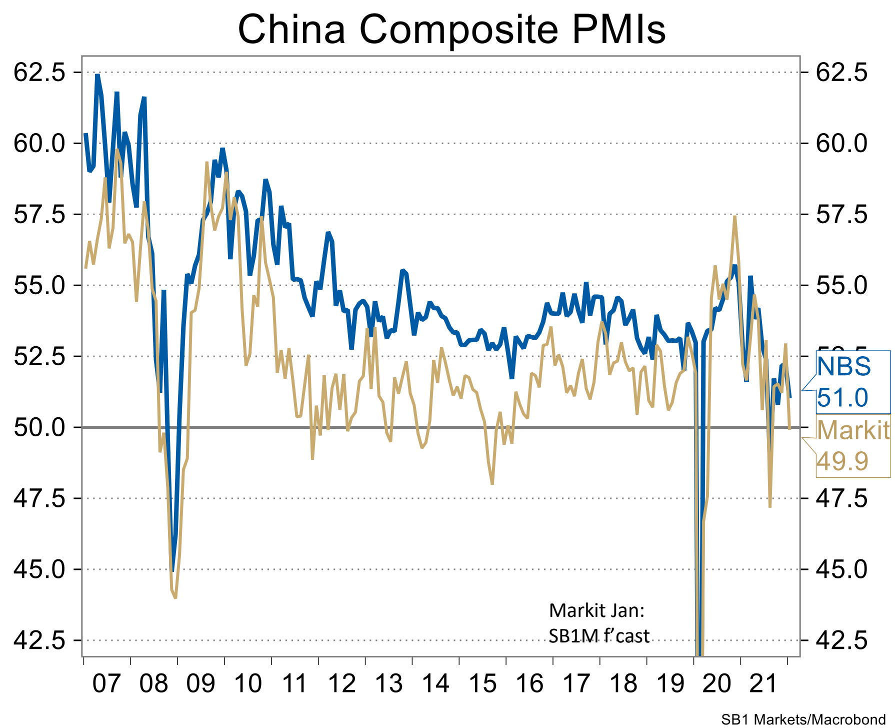


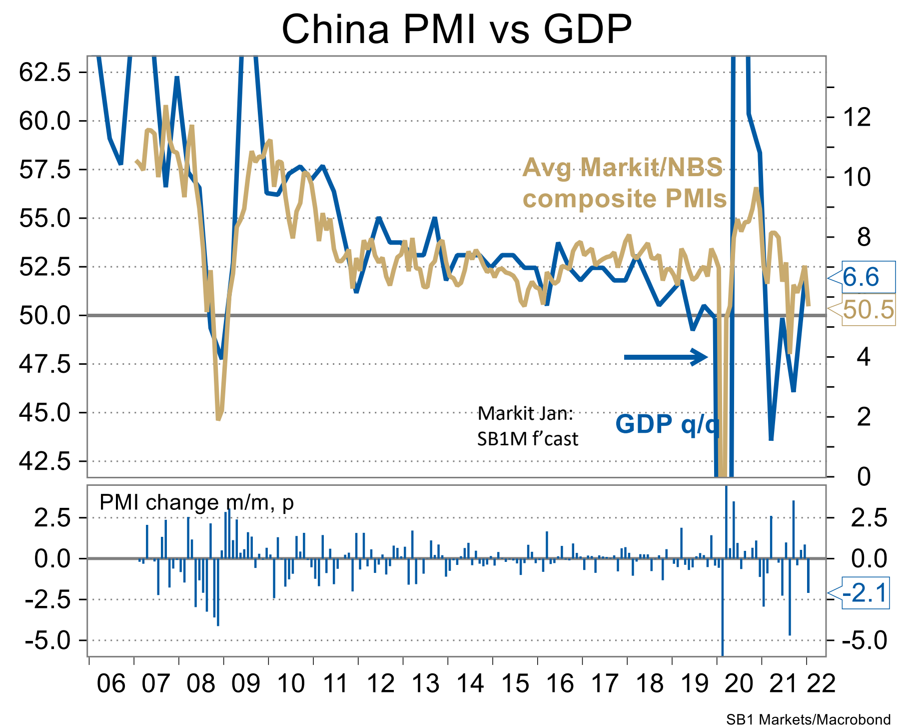


- Even so, some relief

A sharp drop in January PMIs

Services in the CFLP/NBS survey and Markit's manufacturing PMI significantly down

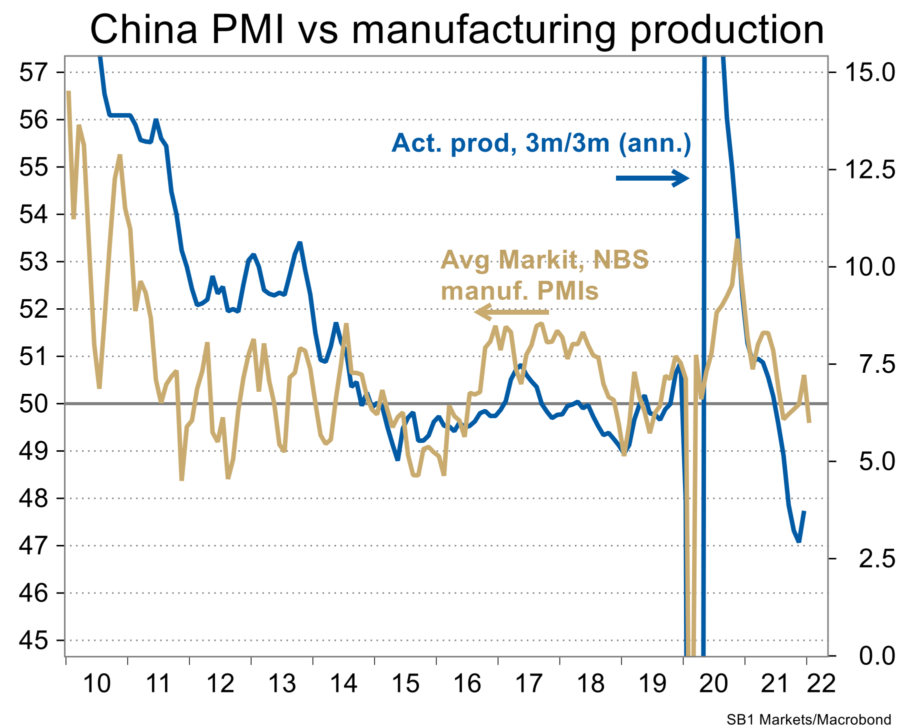




- The **NBS composite PMI** fell by 1.2 p in January, due to a 1.6 p decline in the service sector PMI (close to the expected 1.7 p drop) to 51.1 – very likely due to the impact of the fight against the Omicron variant. The manufacturing index was close to unch, and at tad better than expected
- **Markit's manufacturing total PMI** index fell 1.8 p to 49.1, and the output index fell by 4.3 p! The composite PMI probably fell by 3 p – as we assume even Markit's service sector PMI (not yet published) also contracted, like the service sector in the NBS index did
- **The average of the two PMI data sets** (given our Markit's service sector est) fell by 2 p, to 50.5, to well below and average level. <u>This level signals a growth rate clearly below trend into Q1</u>

Markit's manufact. PMI sharply down in Jan, the lowest since late '18 (x feb-20)

The average of the Markit's & NBS' surveys still not that weak

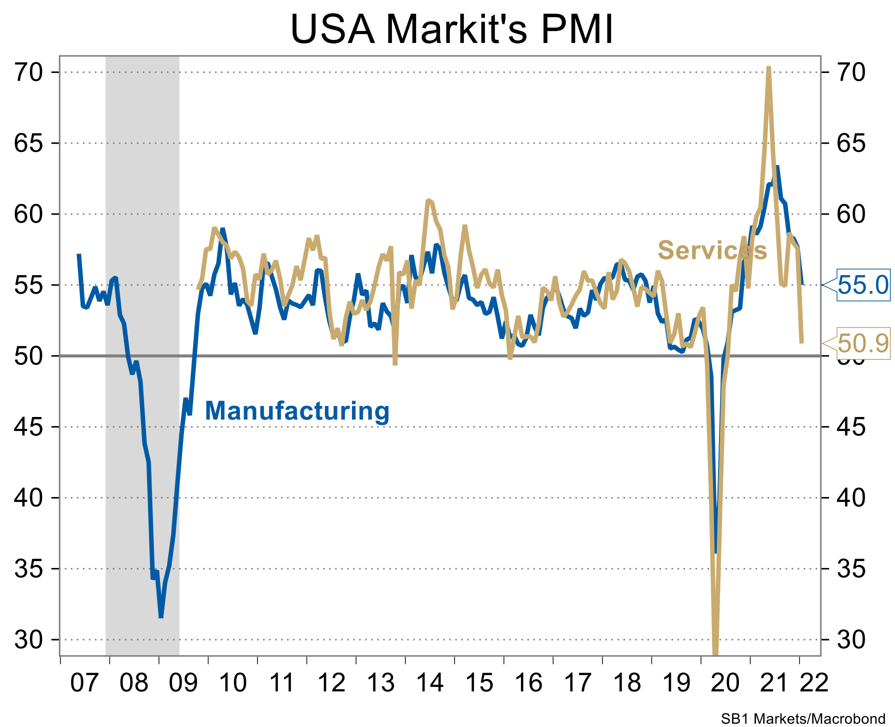


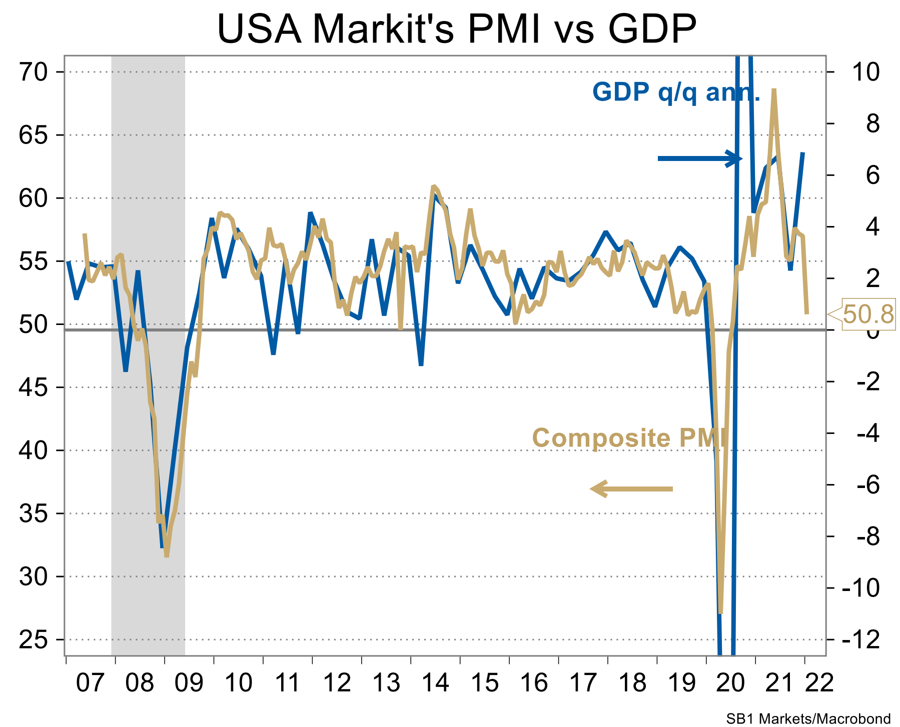
- The **NBS/CFLP PMI** declined 0.2 p to 50.1, while **Markit's PMI** fell 1.8 p to 49.1. The NBS survey is close to the average since 2012, while Markit's index is way below
- Growth in **actual industrial production** slowed in H1 last year (but gained some speed in Nov & Dec)

SpareBank 1 MARKETS

Oops, what happened in the US in January? Markit's PMIs straight down

The composite index fell by 6.2 p to 50.8, expected 2 down. Close to zero growth??

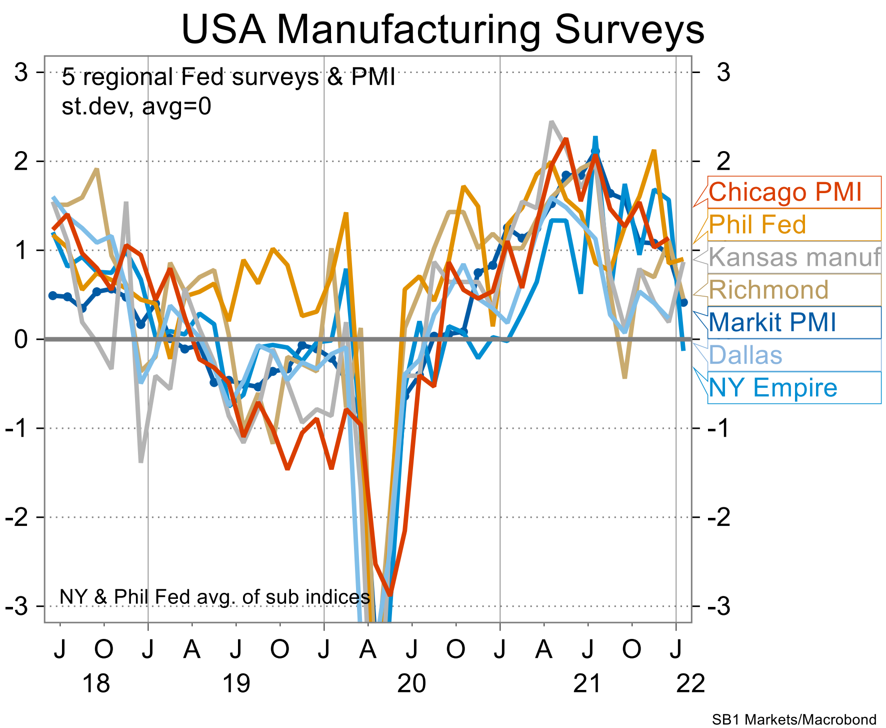


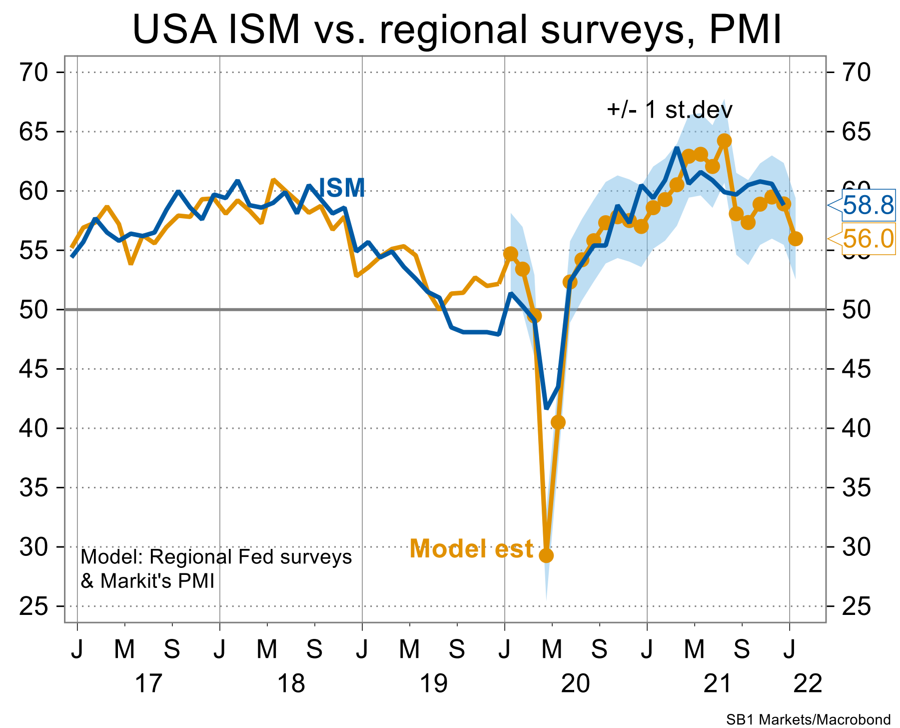


- **The composite PMI** reported the 3rd largest decline ever (data from 2007) – and just a minor decline was expected
- **The service sector PMI** fell by 6.7 p to 50.9, expected down 2.2 p to 55.4. The print is well below an average level
- **The manufacturing sector** also hit something, the PMI fell by 2.7 p to 55.0, expected -1p to 56.8. Order inflow slowed, and did output growth, almost down to the 50 line
- Companies report a moderate growth in **employment. Prices** are still soaring but at a slower pace
- The **delivery times index** fell sharply – but delivery times are still increasing rapidly (or they are at least still unusually stretched)
- **What happened??** The decline in the service sector PMI could may be explained by virus challenges, but not the (continued) decline in the manufacturing index. Other manuf. Indices were mixed in Jan, but in sum down, *check to pages fwd*

3 out of 5 manufacturing surveys down in December, so far

Substantial decline NY Fed survey, as well as in the Richmond and Markit’s PMI. ISM down 3 p to 56?

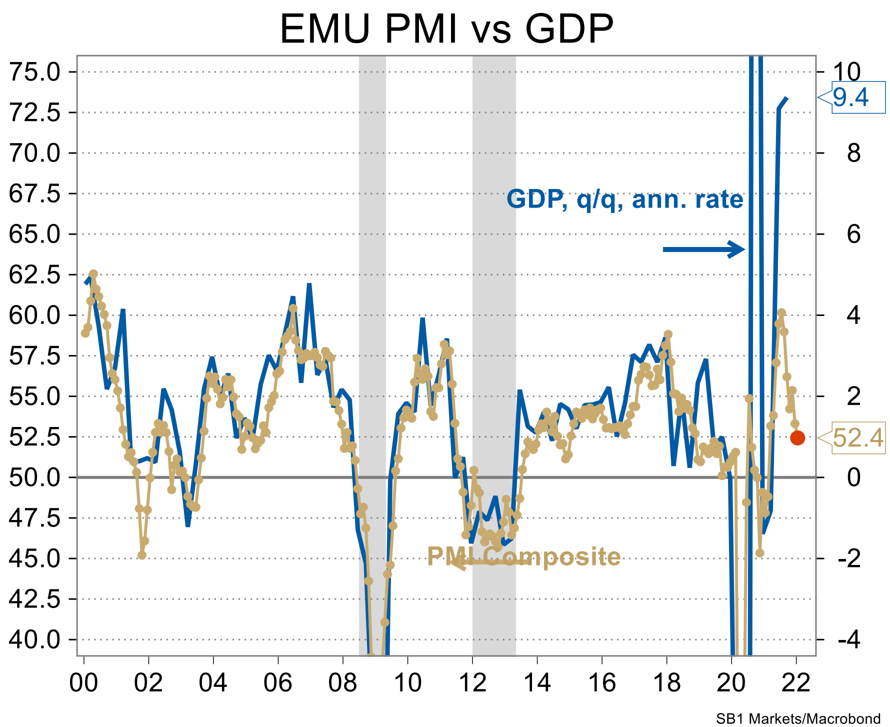


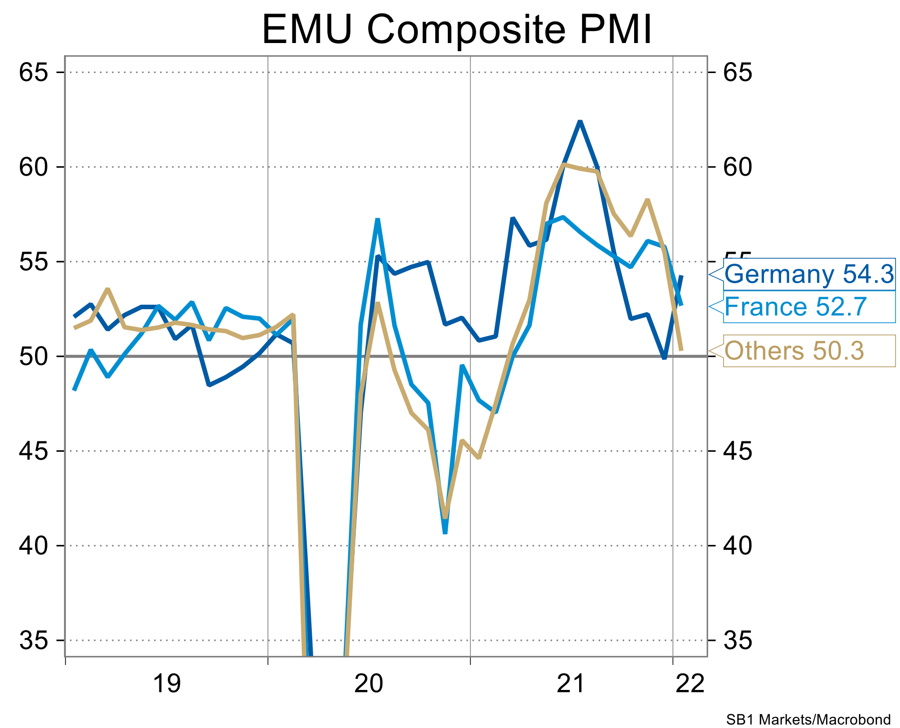


- Dallas Fed and Chicago PMI has not reported their manufacturing surveys yet

The composite PMI down 0.9 p to 52.4, signalling 1% GDP growth

Germany surprisingly recovered – and sharply. The others weaker than expected

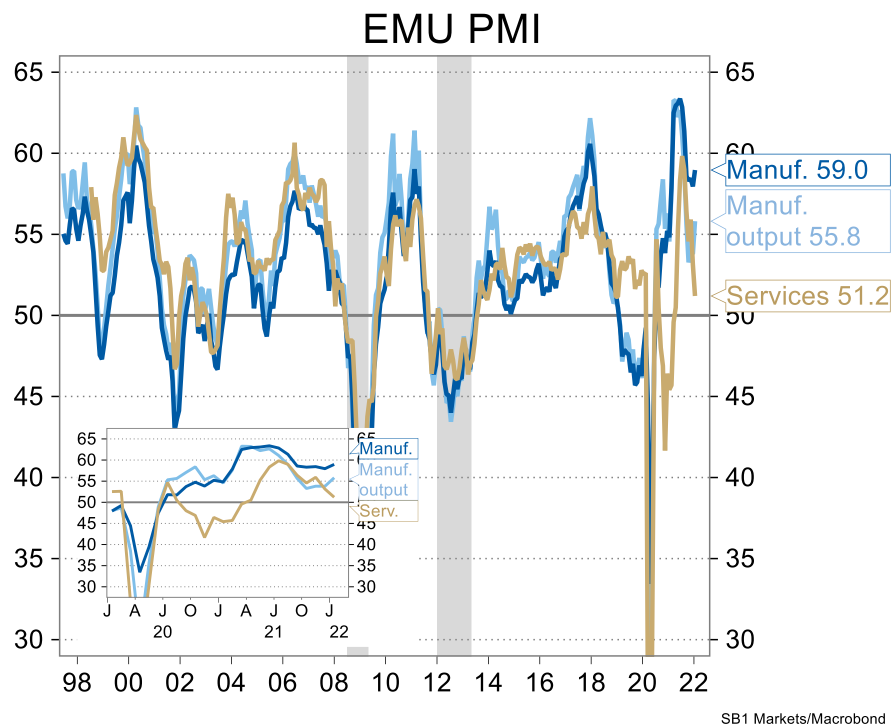




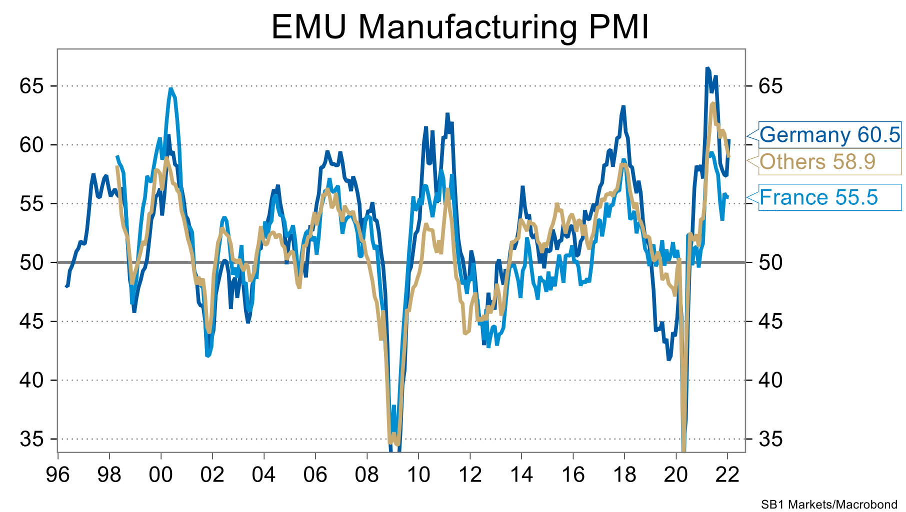
- More Covid measures (and individual changes in behaviour) probably contributed in both France as well as in (the implied average of) Italy and Spain
- The German PMI rose 4.4 p to 54.3 – while it was expected further down!
- The composite index fell in France and in the average of the rest of the union, the latter down to 50.3

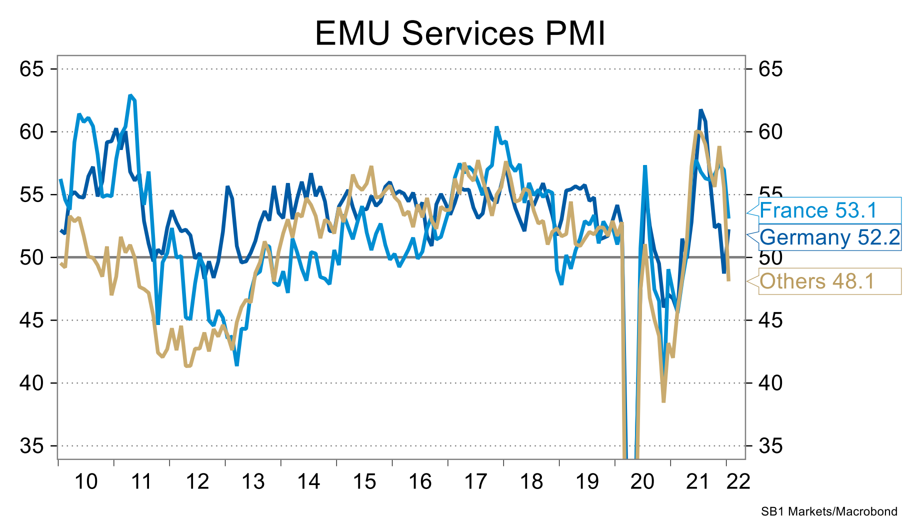
A surprising and strong German recovery but others as services took a hit there

The EMU region: Growth in manufacturing accelerated, but services very likely hit by the virus, again



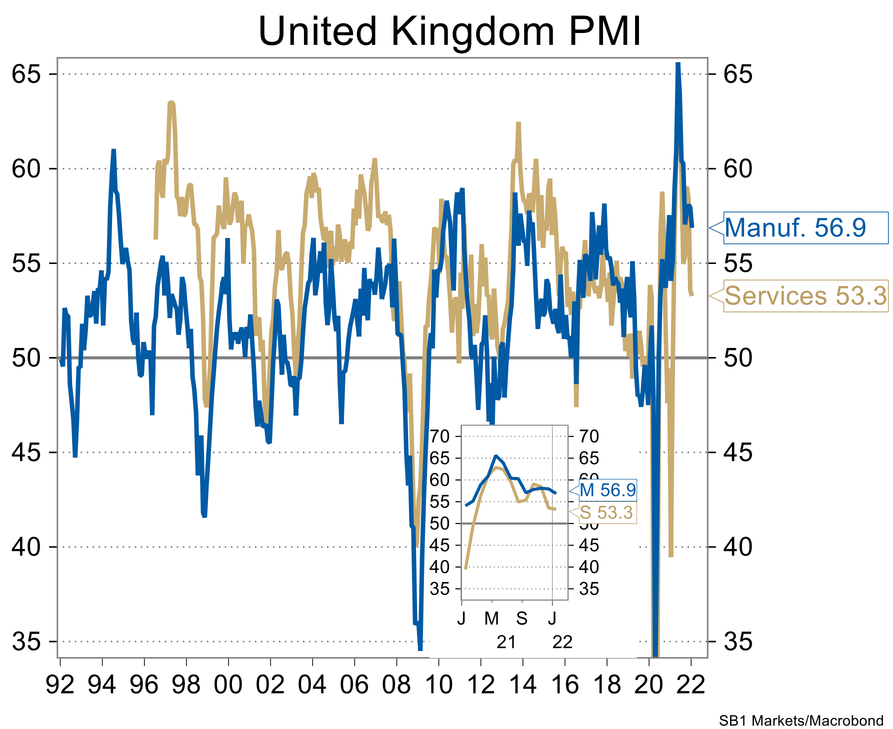
- The **service sector PMI** lost 1.9 p to 51.2, expected down to 52
- The **manufacturing PMI** added 1 p to 59.0, expected down to 57.5. The **output index** is not that strong, at 55.9 but the index climbed 2 p in January

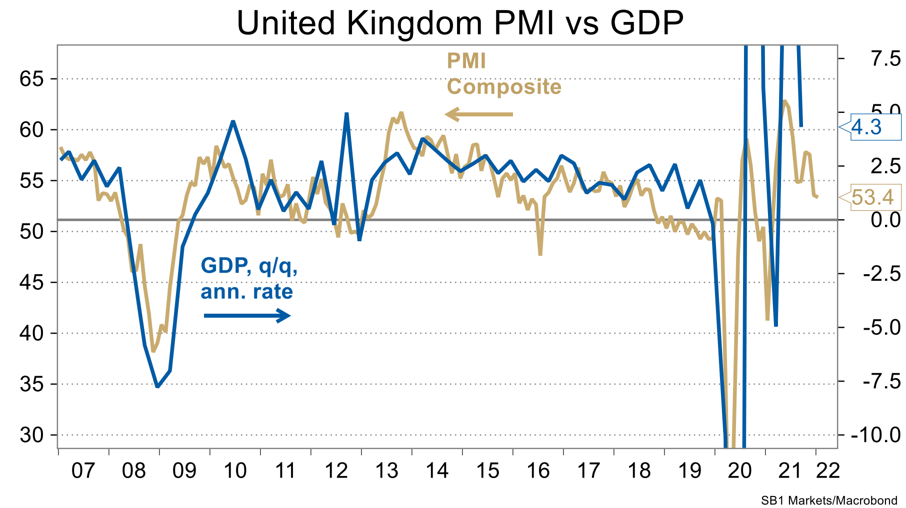


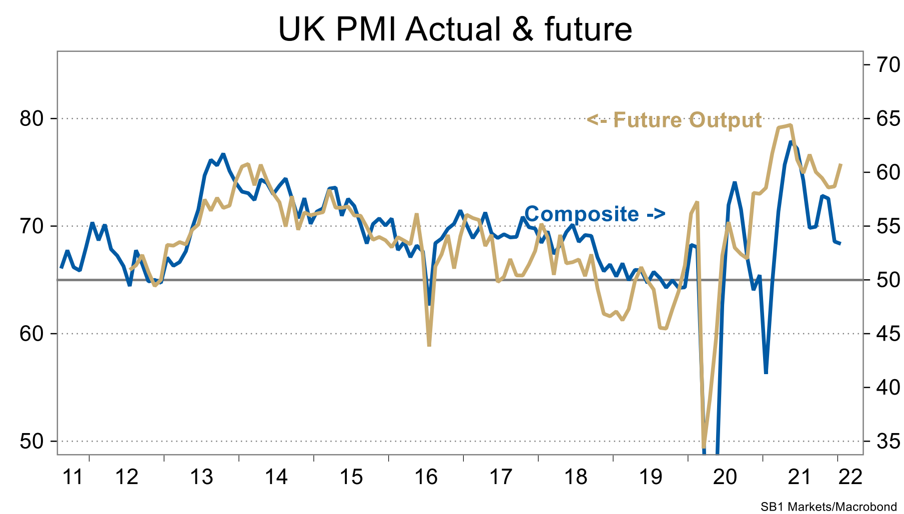


The PMIs stabilised in January, moderate growth signalled

Even services are reporting growth – before all Covid restrictions were lifted



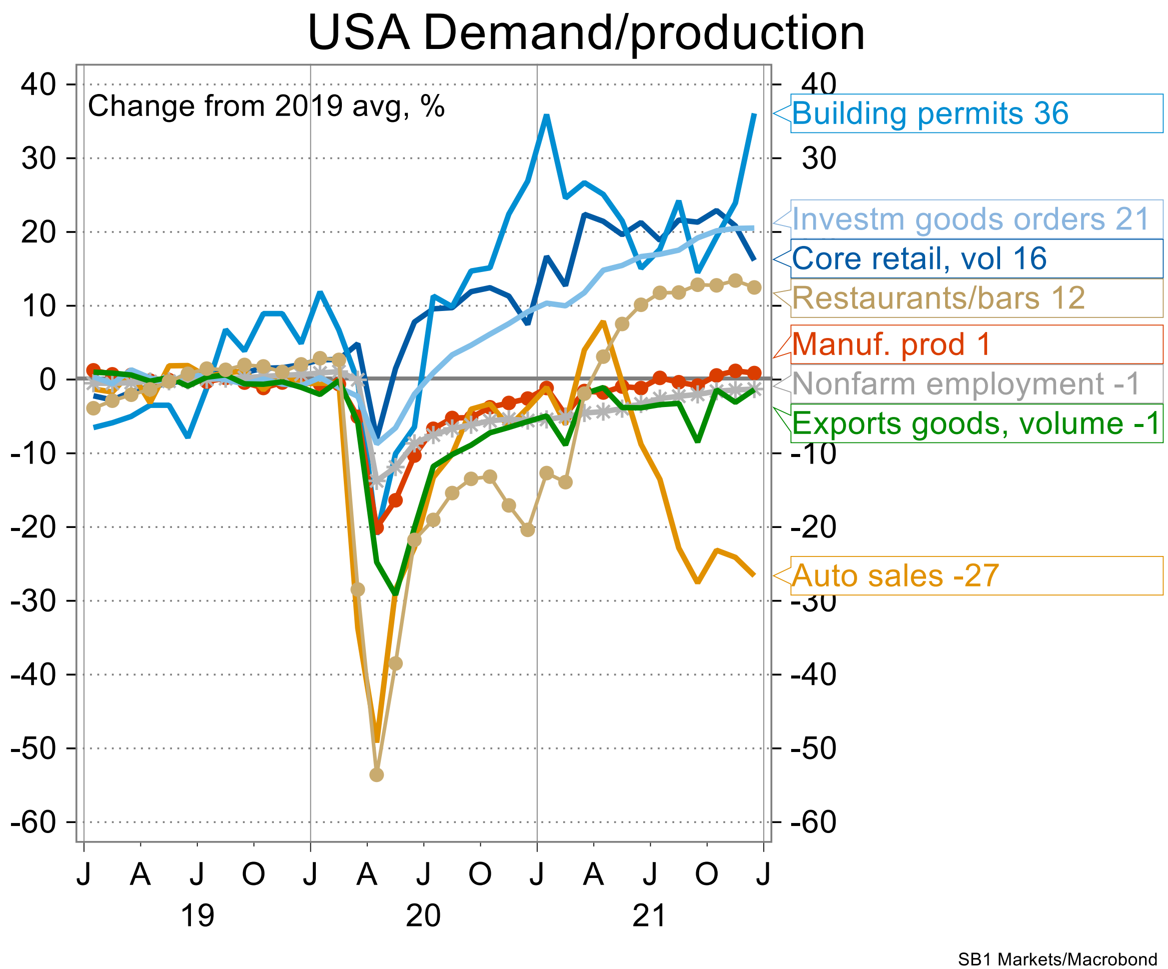




- **The composite PMI** declined by 0.2p to 53.4 in Jan, with just small changes in both manufacturing and services. In Dec, the index fell by 4 p and corona restrictions were imposed. In Jan, the index was expected up to 54
- **Services PMI** fell marginally to 53.3
- **The total manuf. PMI** was down 1 p to 56.9 , as expected (but the output component, included in the composite index, gained 0.6 p to 53.3)
- The delivery times index, as well as the price indices declined further – but they all remain at elevated levels (see next page)

Big picture: Growth is slowing as the economy as 'normalised'

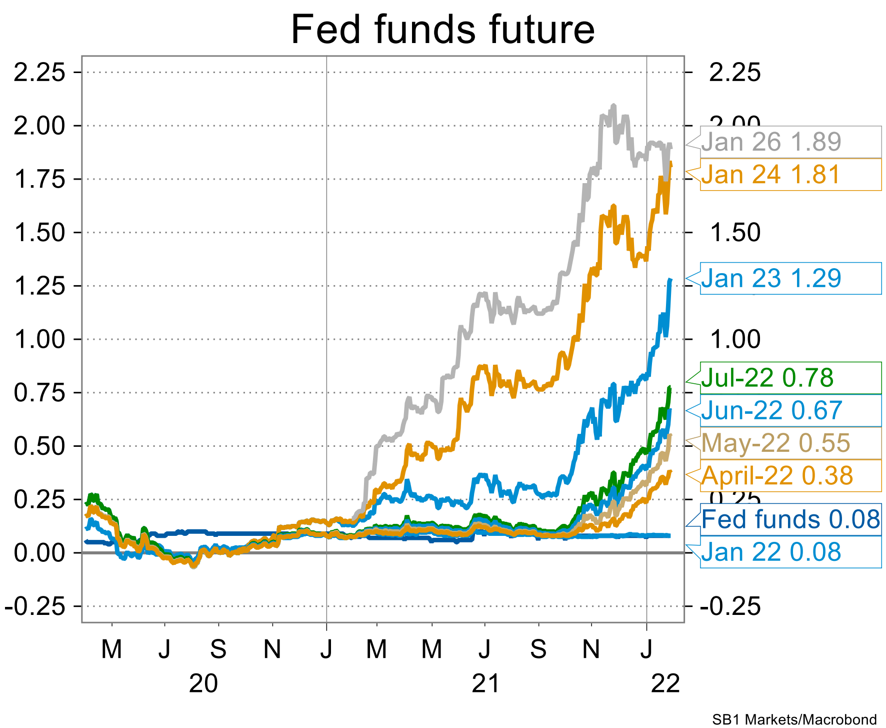
The upside now: Auto production & exports



- Retail sales have peaked, but is still at a high level (and Dec was likely artificially weak)
- Restaurants have recovered, at least nominally (prices are sharply up)
- Home building has flattened, mostly due to supply constraints, demand is still strong
- Manufacturing production is 'too weak' but supply constraints, exports have kept production in check
  - » Auto sales and production are way below normal levels

Fed: The huge policy shift confirmed. A rapid tightening can not be ruled out

We suspected that Powell as usual would be soft at the press conference but this time de was not



- **The press release from the FOMC meeting was 'neutral', and the market did not respond to the message which confirmed that a March hike was almost granted**
- **However, at the press conference Powell revealed a new side of himself, clearly stressing the uncertainty on the upside for inflation, as for the need for monetary tightening. Rate rose sharply all over the curve**
- Like in the minutes form the previous meeting, Powell commented that current situation is not comparable to 2015, when the last tightening campaign started; Inflation is much higher, the labour marked tighter and the economy much stronger. Thereby, he is signalling willingness to hike rates rather rapidly. He stressed that the FOMC is ready to do what is needed. He would not rule out that rates could be hiked more than 25 bps , or that rates could be adjusted at the 'mid' meetings
- The timing of a moderate **reduction of the bank's holdings of bonds** had not been discussed (at least not in detail) but a QT could start after the first hike in signal rate (by not reinvesting all proceeds from the current stock).
- For the record: The FOMC left the **target rate** unchanged at 0-0.25%, and confirmed the December decision that the **bond buying (QE)** program would be terminated by March
- **Market reactions:** Interest rates rose by up to 20 bps in the short end of the curve during Wednesday and Thursday (after a decline ahead of the meeting). The market now assumes that 5 or more hikes in 2022 is more likely than 4 or less! Stock wobbled, but ended the week marginally up

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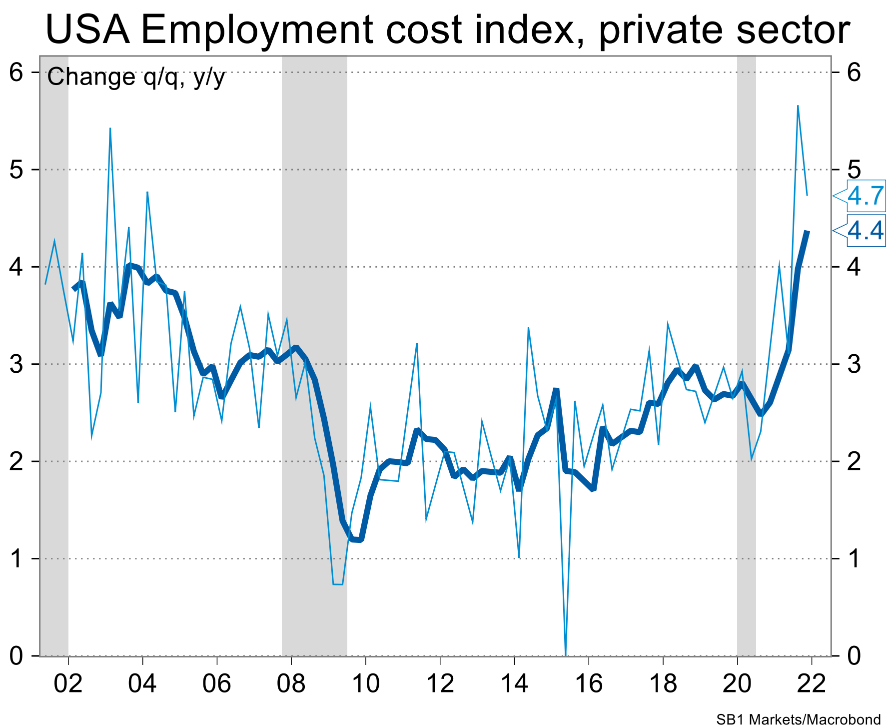
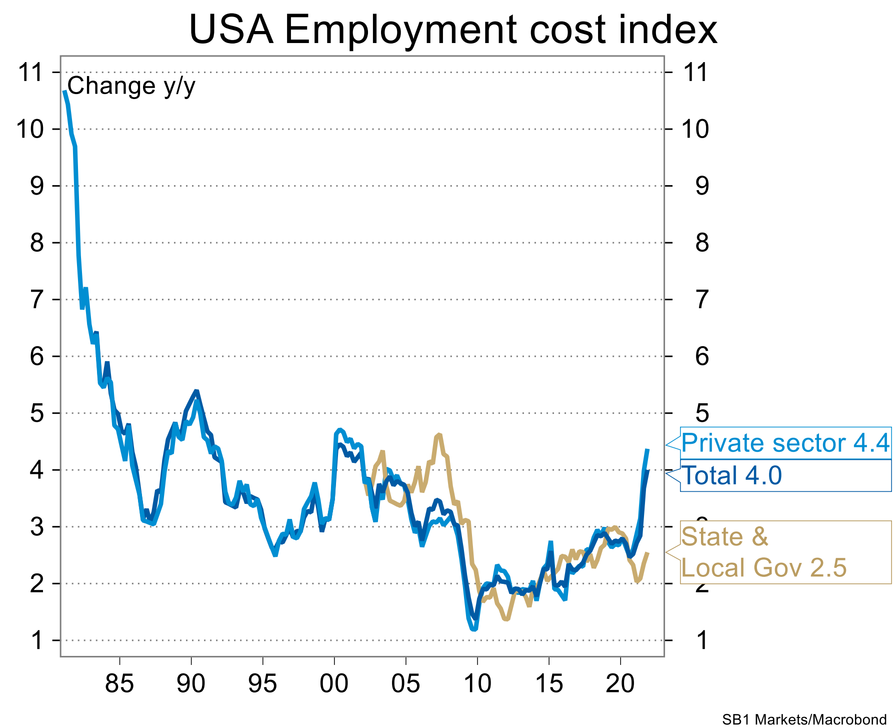
Employment cost are climbing fast in the private sector

Employment costs rose at 4.7% pace in the private sector in Q4, annual growth up to 4.4¤

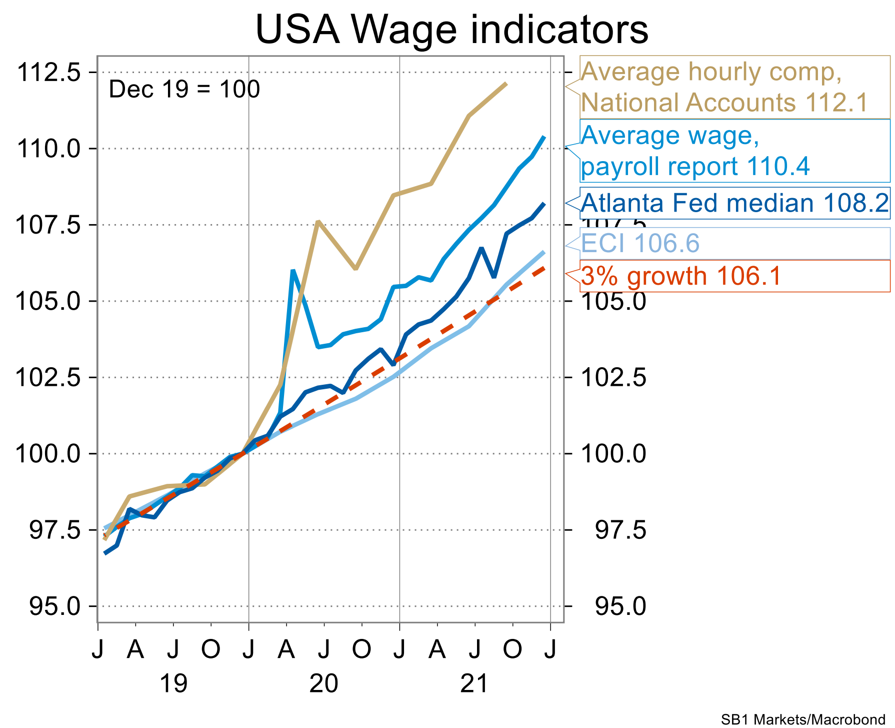


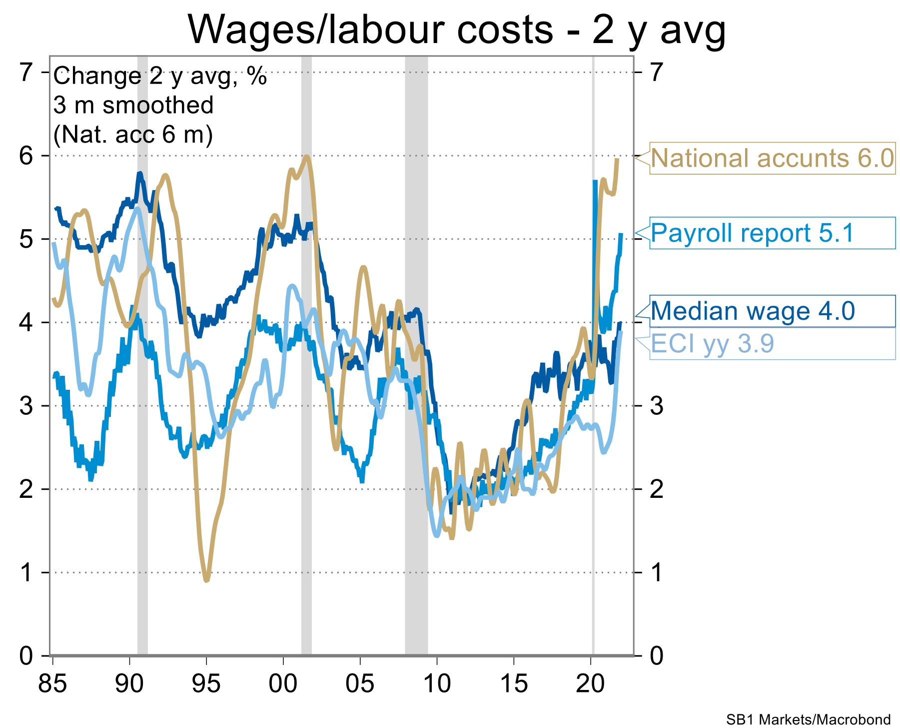


- The **Employment cost index for all civilian workers**, which measures wages and other wage costs for the same types of jobs (and is not influenced by changes in employment between sectors/type jobs), rose by 1.0% q/q in Q4, 0.2 pp less than expected, or at a 4% annualised pace. The annual rate accelerated to 4.0% from 3.7%, the highest since 2001
  - » In the private sector, the ECI rose by 1.2% q/q (4.7% annualised), and it is up 4.4% y/y
    - Wages & salaries in the private sector is up 5.0% y/y, highest since 1985. Benefits are up 'just' 3.0% (and the sum 4.4%)
  - » State and local gov employment costs are up just 2.5% y/y, the largest discrepancy to the private sector ever
  - » In general, low paid services reported the highest wage growth, both q/q & y/y
- **All other wage indicators have reported higher wage growth for a while**

Now all wage indicators are reporting higher wage inflation

… and substantially higher than during the previous 10 years that has yielded 2% inflation (or more)

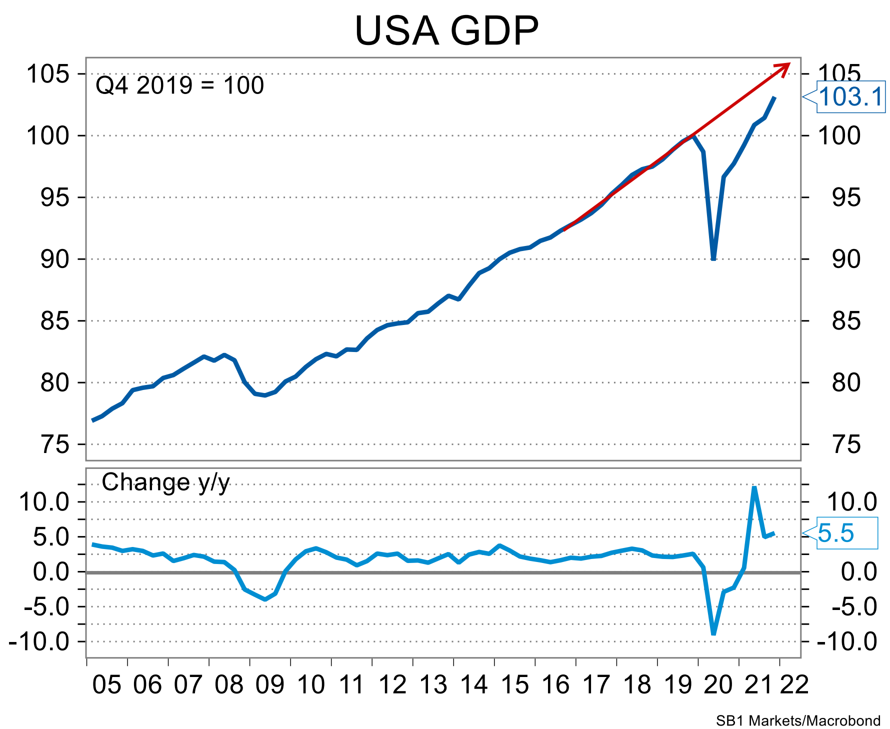


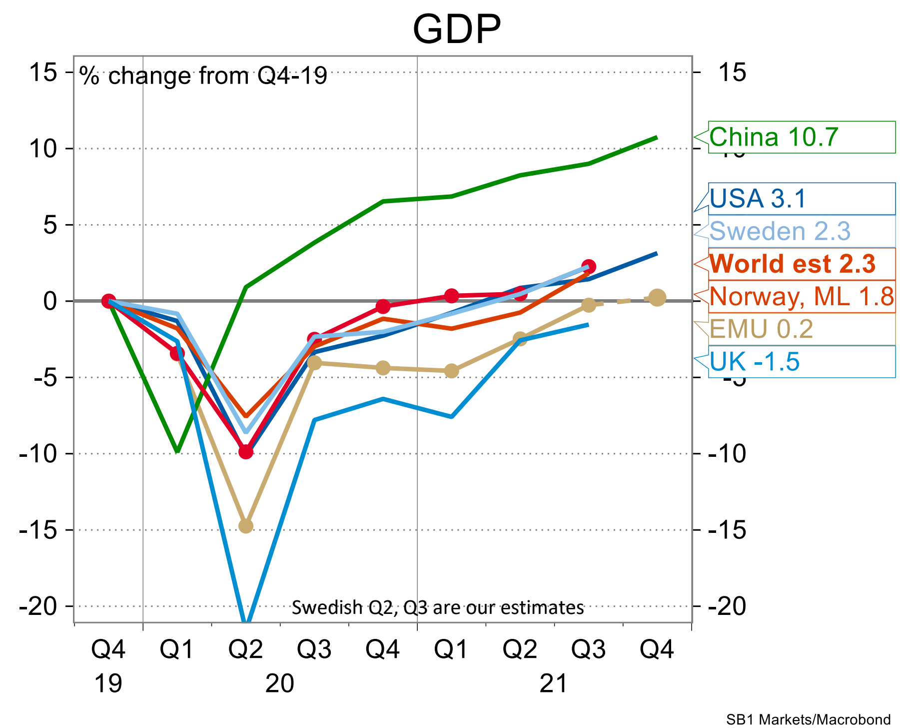


- **All wage indicators** are reporting faster wage growth, and all reporting wage growth well above the average recent years, also if we apply a 2-year average growth rate, to exclude the impact of changes in the first part of the pandemic (chart to the right)
- Growth in wage/earnings/compensation indicators are up 1.5 – 3.5 pp vs the their respective 10 y averagea. There is an obvious risk that wage inflation will accelerate further (check next page) – probably until the next recession hits as the labour market is extremely tight
- Over the past 10 years, inflation has been close to 2%, and well above 2% if calculated over a shorter period
- It will be a challenge to keep inflation at 2% if wage inflation remains at 4% or above. However, profit margins will probably decline substantially from the present very high level, and productivity growth has accelerated somewhat, leaving room for a slightly higher wage inflation than over the past 10 years without creating higher price inflation

GDP grew at a 6.9% pace in Q4, and is not that far below the pre-p trend path

Domestic demand was not that impressive as inventories 'explained' 5 pp of the 6.9%

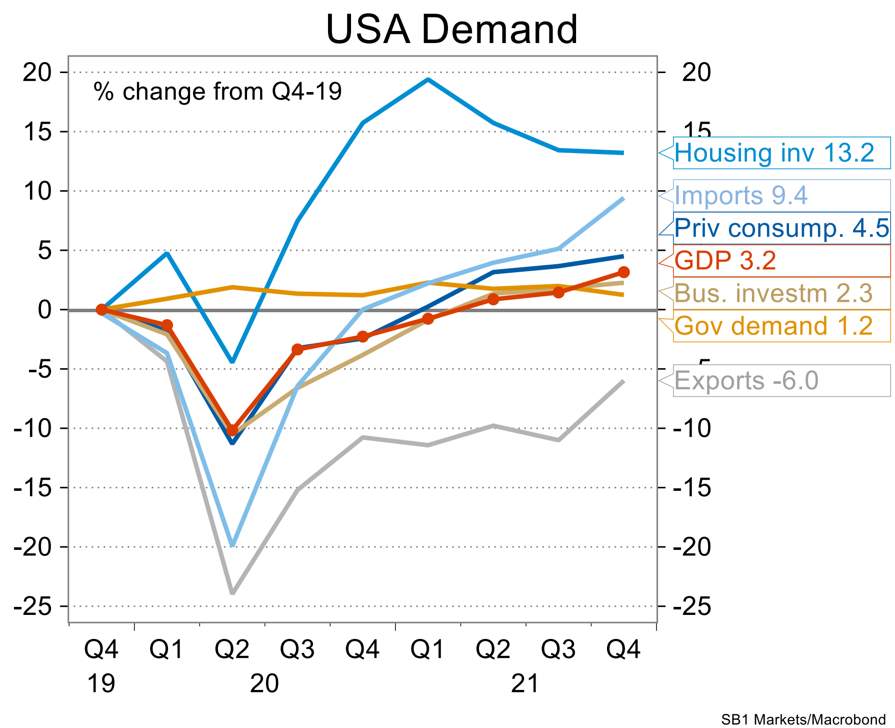


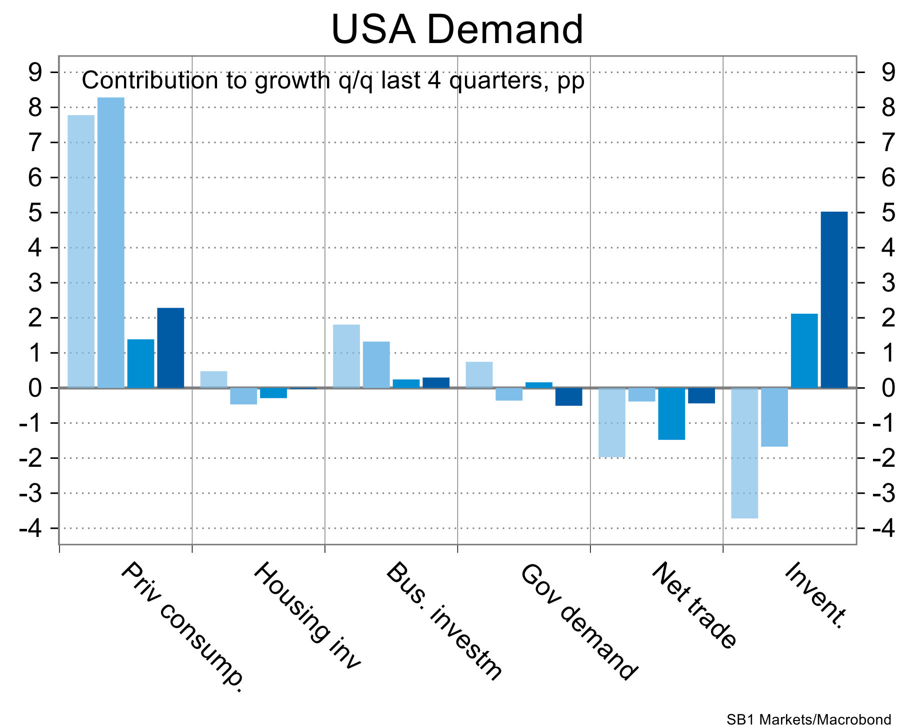


- **GDP** grew by 6.9% annualised in Q3 (1.7% not annualised),up from 2.3% in Q3, and well above expectations at 5.5%. The GDP level is 3.1% above the Q4-19 level – but still 1.7% below the pre-pandemic (2.4%) growth path, as services still operate below a normal level
  - » GDP grew by 5.5% y/y in Q4, and by 5.6% in 2021 vs. 2020, following the 3.4% decline in 2020
- **Private consumption** grew 3.3% in Q4, housing investments fell 0.8%, business investments added just 2%, t tad more than in Q3, and only driven by IP investments – construction investments fell sharply for the 2nd quarter in row, now by 11.4%. Government spending was cut by 2.9%
- **Domestic demand** rose no more than 1.9%. Exports rose 24%, from a low level – and imports rose 18%. However, imports as are far larger than exports, the contribution from net trade was negative, by -0.4 pp! So why did GDP grow by 6.9%? Because **inventories** rose big time, and added 5 pp to growth – that is, out of the 6.9%! Inventories contributed by 2.1% in Q3, following a huge inventory rundown in Q1 and Q2
- Big picture: The economy is still not fully back on track but growth is decent. The inventory cycle is still not worrisome

Inventories were the Q4 story but final demand is OK too

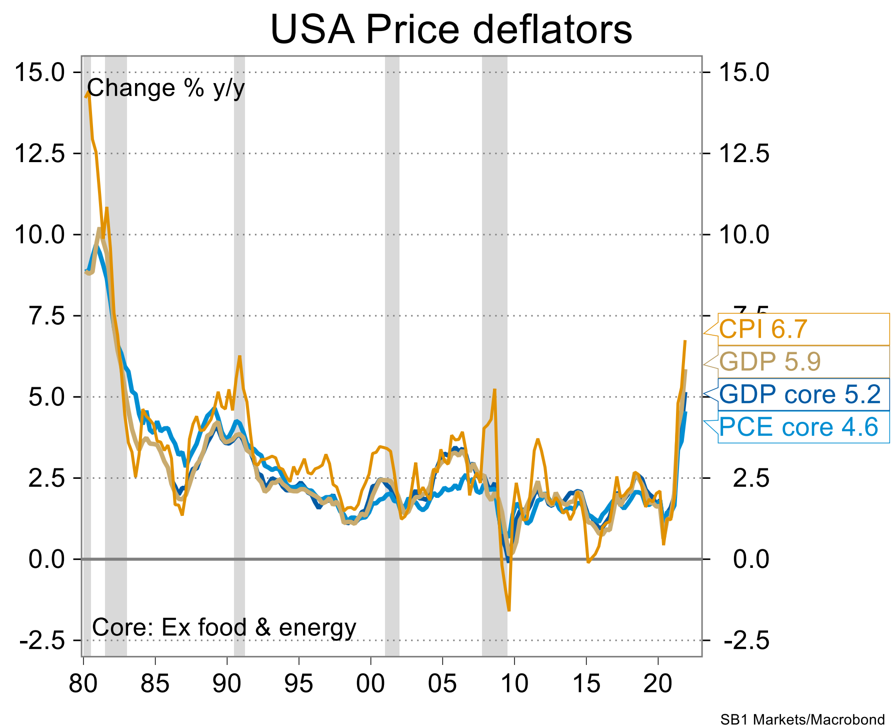
However, business investments are growing just slowly, and housing investment fell further

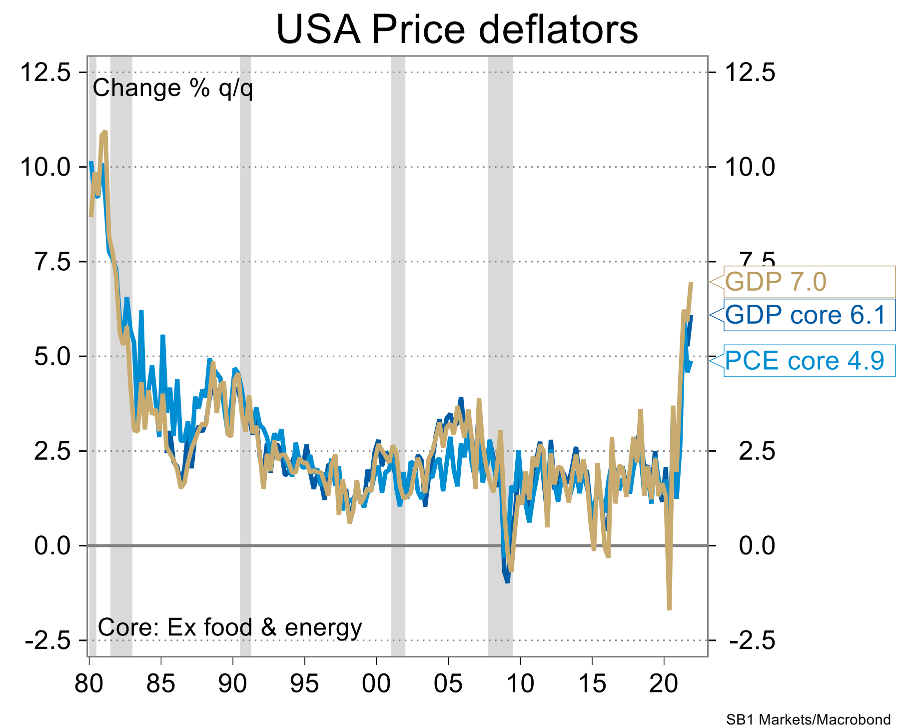




Price increases accelerated in Q4 – and we are at levels not seen in decades

All GDP/PCE deflators up 5 – 7% in Q3. Nominal GDP grew 14.4% in Q4!

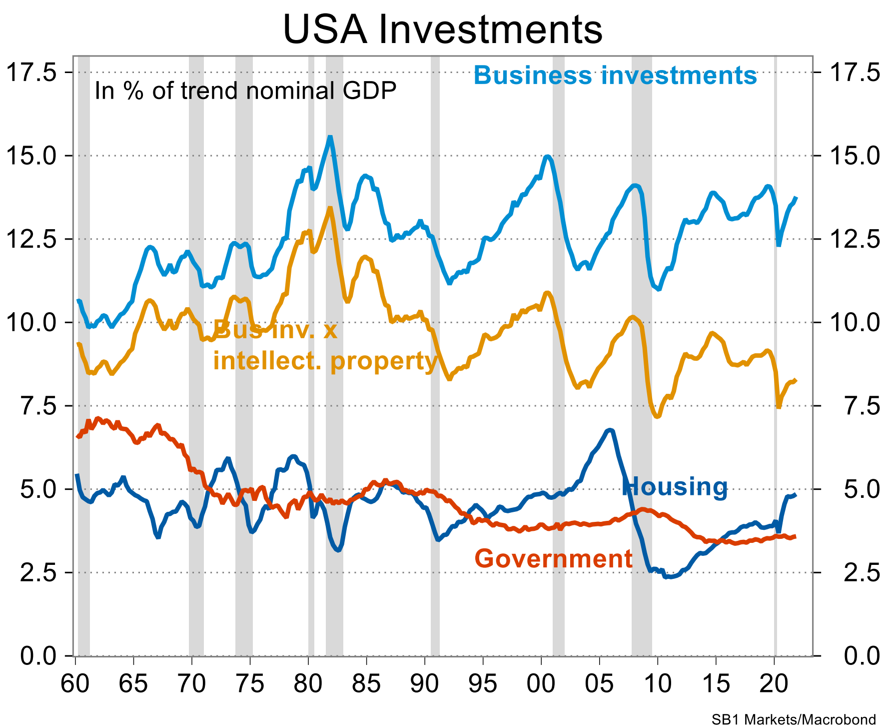


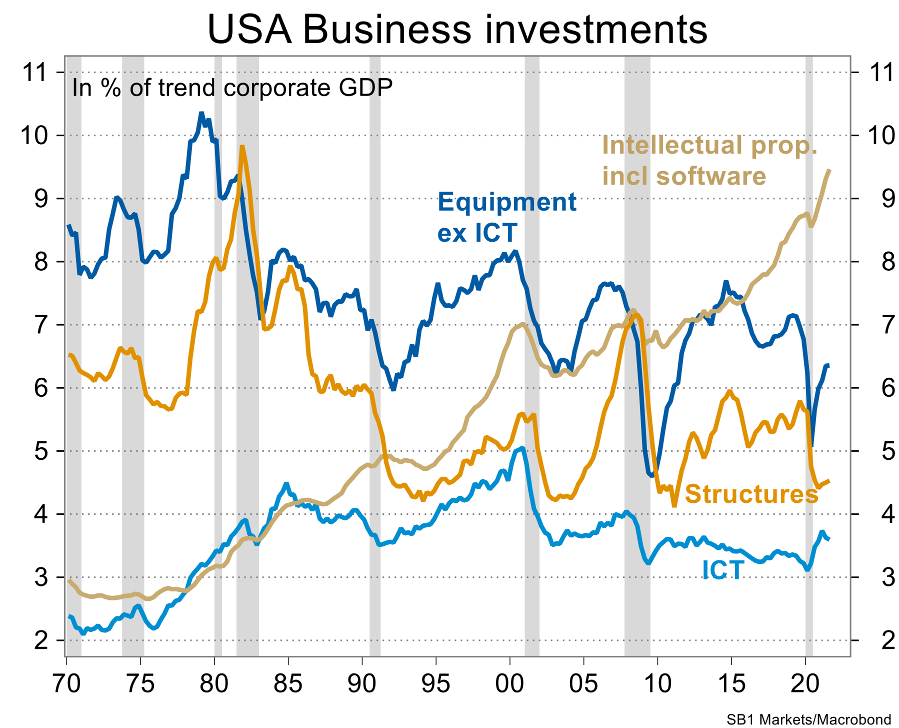


- Higher energy prices partly to blame but other prices also contributed in Q4, as during the previous quarters. The growth rates are the highest since 1982
- The core (x energy, food) PCE deflator (Fed's preferred measure) is up 4.6% y/y (and by 4.9% in Q4), the highest since 1991. The 40% lift in used auto cars explains a substantial part of the lift in the core PCE
- Nominal GDP grew at a 14.3% pace in Q4, the price deflator rose 7.0%. Over the past 2 years, nominal GDP is up 5.2% in average

Investments: Total business investments strong, housing investment high too

Business investments above trend just due to IP & software, ICT. Other equipment, structures still weak

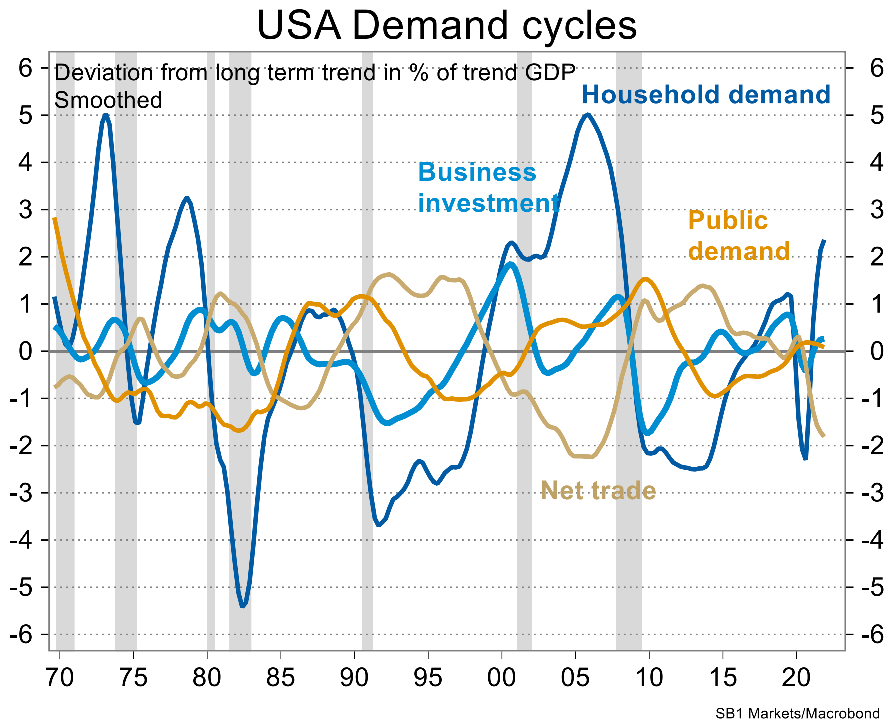


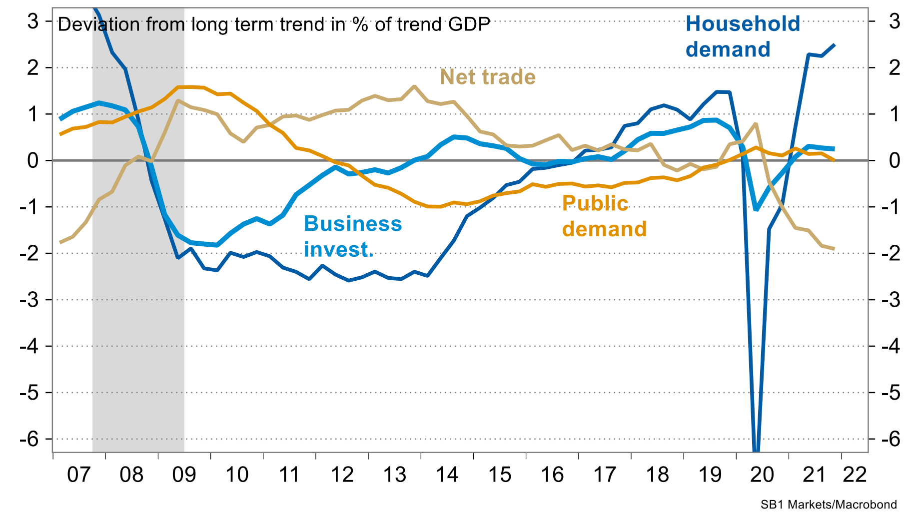


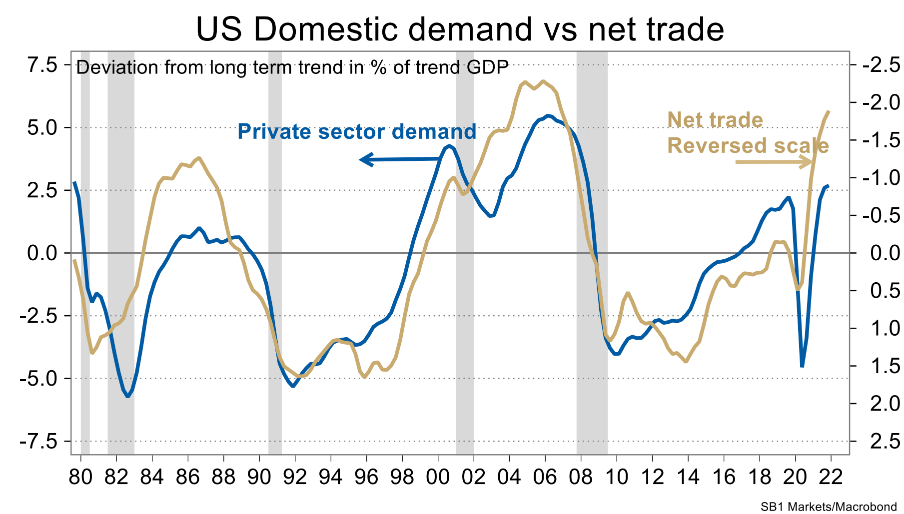
- **Business investments** are up 5.5% vs. the Q4-19 level (in volume terms), driven IP/software and ICT equipment. Investments in structures are still very low. Investments in equipment x ITC may be close to trend
  - » Thus the outlook for business investments is not clear: The boom in IP/software/ICT may well continue, even if the levels are high. There is still upside for other equipment and structures, at least vs the normal cycles in these sectors
- **Housing investments** fell in volume terms but prices rose sharply, and investments have just flattened vs. nominal GDP
- **Government investments** as share of GDP are close to flat vs GDP. The infrastructure package will lift the investment ratio by less than ½% of GDP, from the overall investment level at 3.5% now

A private consumption cycle. Or rather, a virus cycle…

A shallow & short business investment downturn. Net trade is on the weak side, but exports will recover?



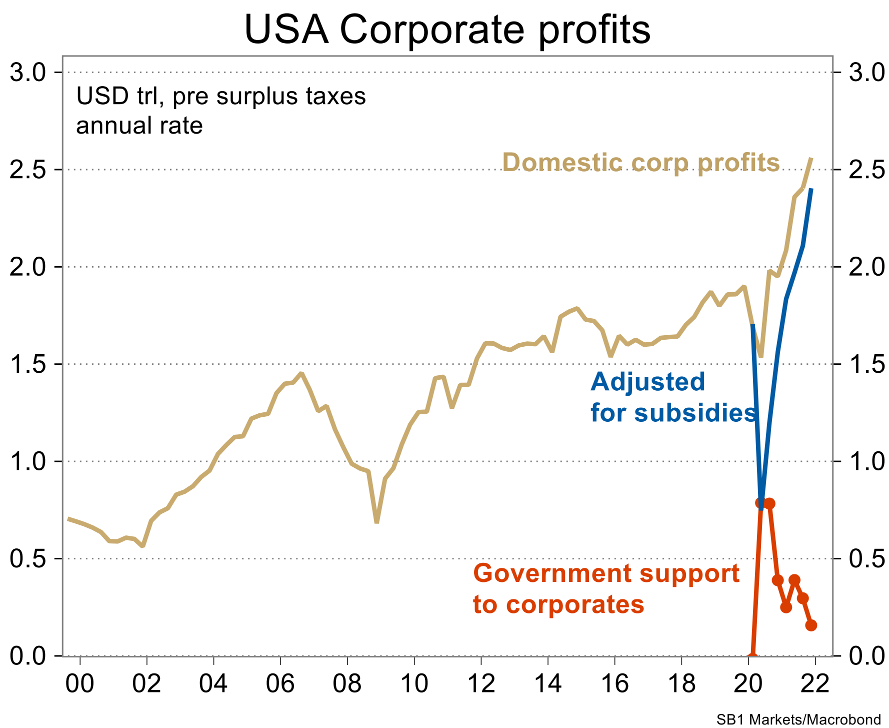


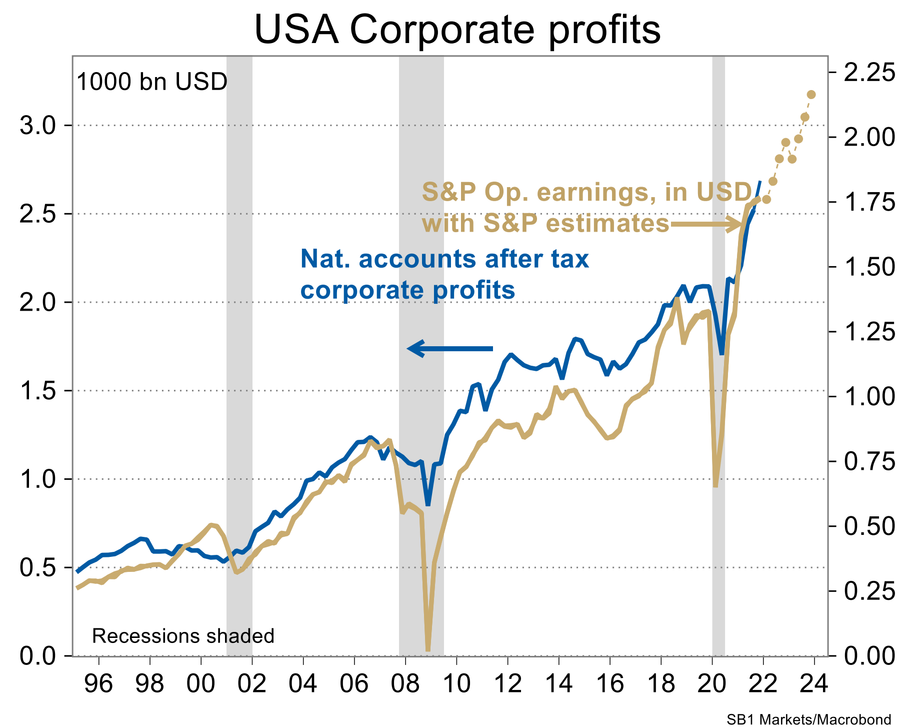


- *Check more on the household sector some few pages forward*

Corporates' profits rose further in Q4, as they lifted prices at a 8% pace

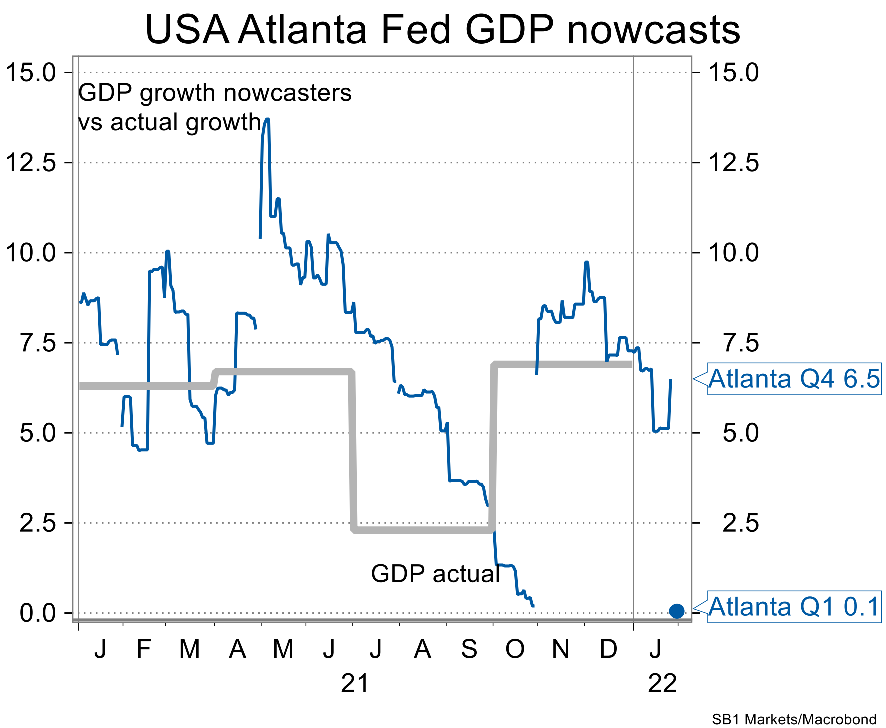
Subsidies were cut, but profits still rose even if the wage bill grew rapidly

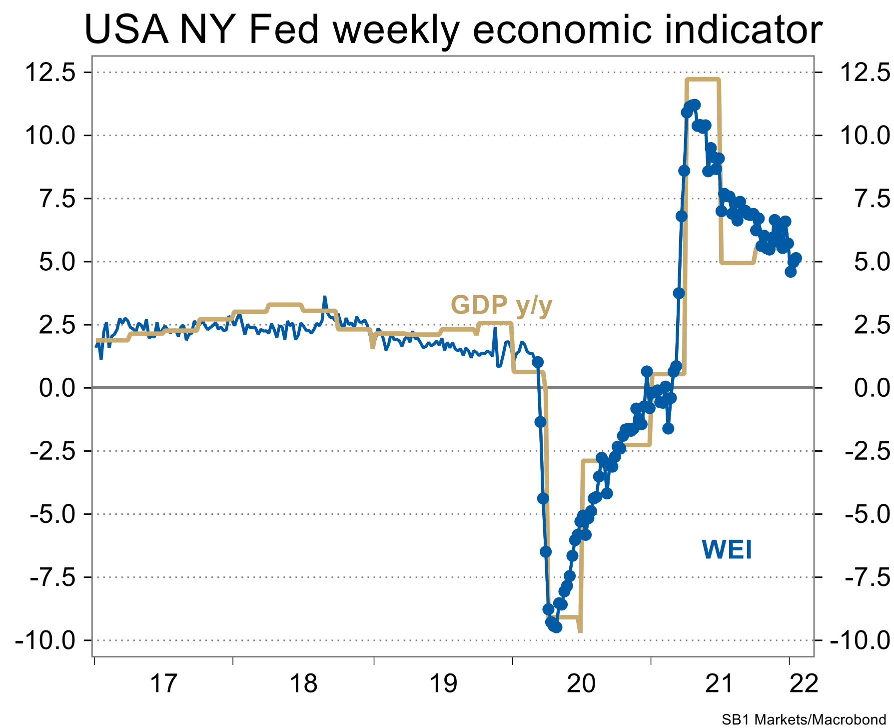




- **We assume domestic corporate profits** rose by approx. 6.5% in Q4, not annualised (28% annualised, and 31% y/y – even if the wage cost rose much faster than normal – and prices surged
  - » The wage bill rose by 10.5% (annualised) in Q4 (domestic corporate sector) but value added rose even faster, by a 17% pace, as companies were able to lift their prices at an 8% pace (domestic corp x finance), an incredible high number. And increasingly hard to swallow for the Federal Reserve…
  - » Government subsides (deviation from trend in indirect taxes – subsidies) were cut but still equals more than 1% of GDP
- The **S&P 500 companies** reported a further increase in profits in Q4 but at a rather slow pace, according to S&P estimates
- We think the profit outlook is muted. Wage inflation will not subside anytime soon given the super tight labour market – and a continued price inflation at the current pace cannot be tolerated by the Federal Reserve. Exciting times ahead

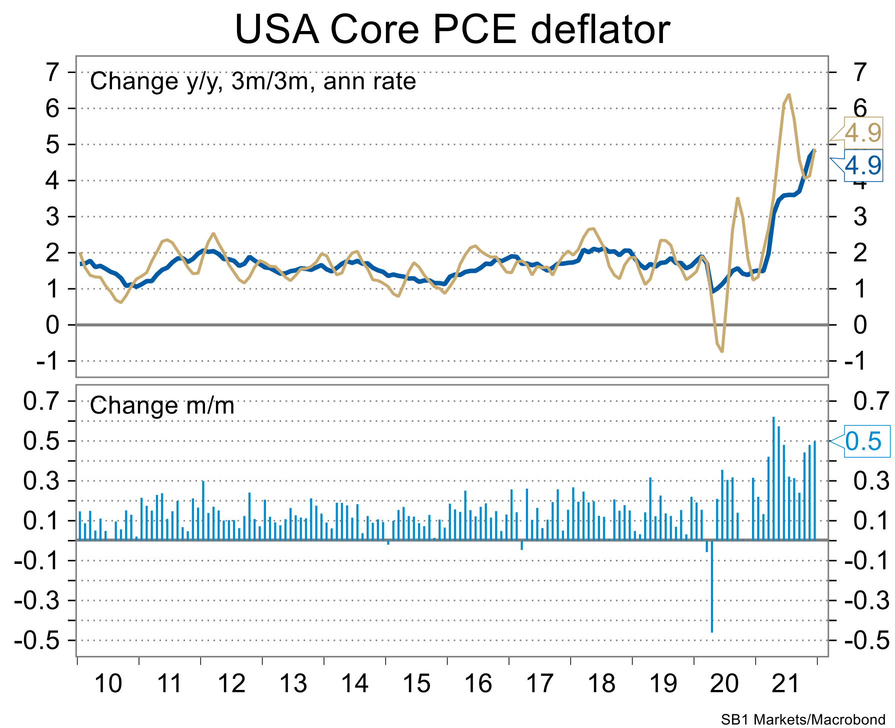
Atlanta Fed's nowcaster suggest close to zero growth in Q1, in the first estimate

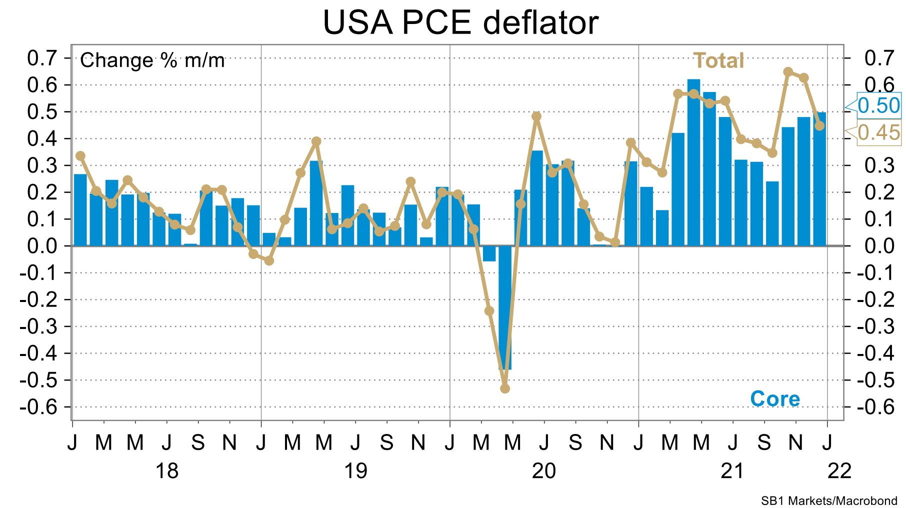


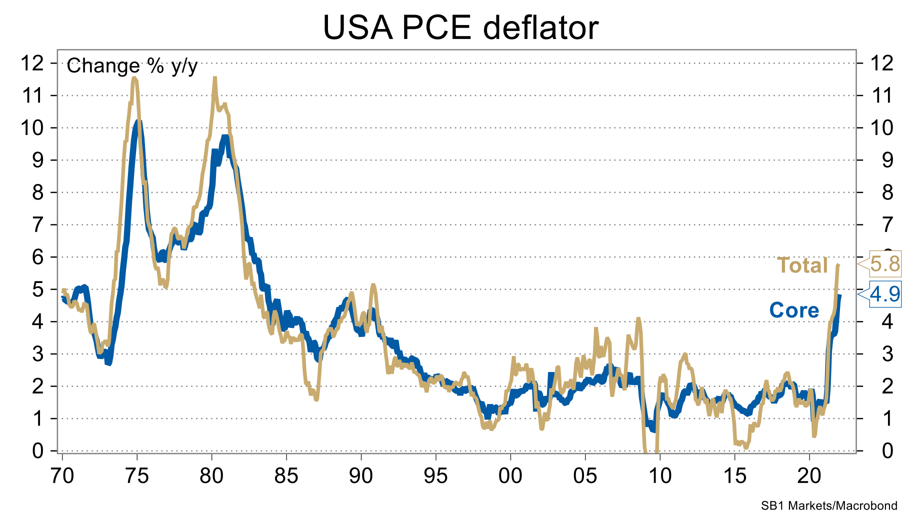


The PCE consumption deflator joined the CPI's large ~~Oct~~ ~~Nov~~ Dec hike

Inflation remains high, and its broadening. A substantial part of it is quite likely transitory but not all



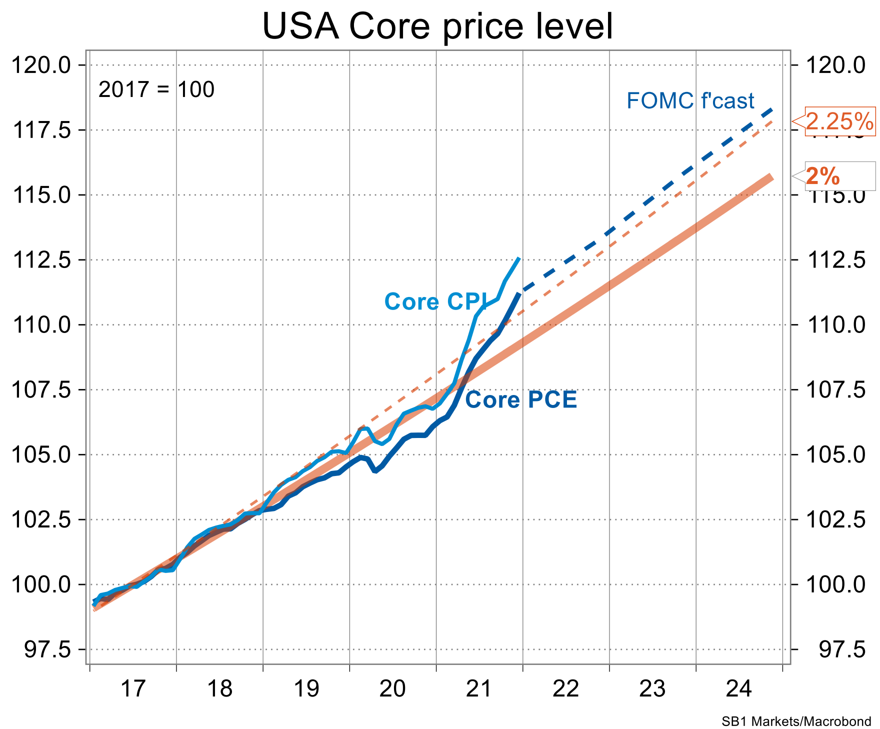


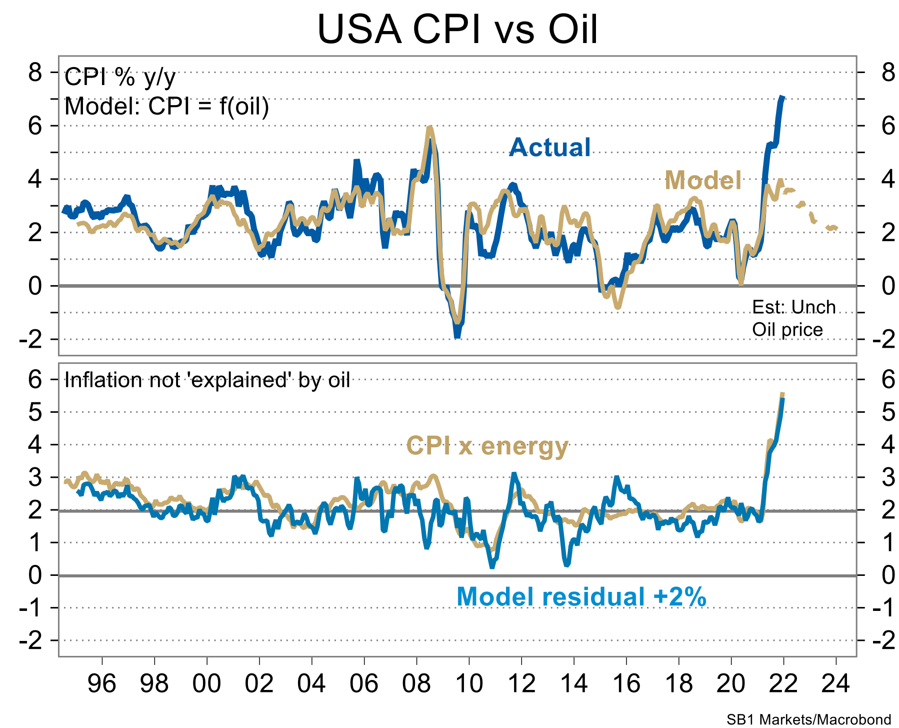


- **The total PCE deflator** rose by 0.4% in Dec, as expected, and the annual rate accelerated 0.1 pp to 5.8%, the highest since 1982
- **The core PCE** rose by 0.5% m/m, also as expected. Measured y/y, the core gained 0.2 pp to 4.9% - and has not been higher since 1983
  - » The 3m/3m rate is close to 5%
- **The price level** is far above Fed's 2% long term path target, and the FOMC members expect inflation to remain above 2%. Thus, they plan to leave the price level target even further behind, even if the maximum employment target also may already be met

The Fed expects the 2% price target to slip, even if the employment target is met

… or more than that





We stick to our main inflation analysis:

- **Raw material cycles** are not lasting that long, and the impacts on consumer prices are normally 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 inflation = wage inflation – productivity growth
- **A tight labour market** normally implies higher wage inflation. Now, the vacancy rate is the highest ever, and all wage cost indicators signal higher wage growth. This is the real challenge for the Fed. At the Dec FOMC meeting, Powell acknowledged that wage inflation in the end is the final criteria for judging if the maximum employment target is met. Thus, before soon, the Fed may be missing on both of its targets – at the same side

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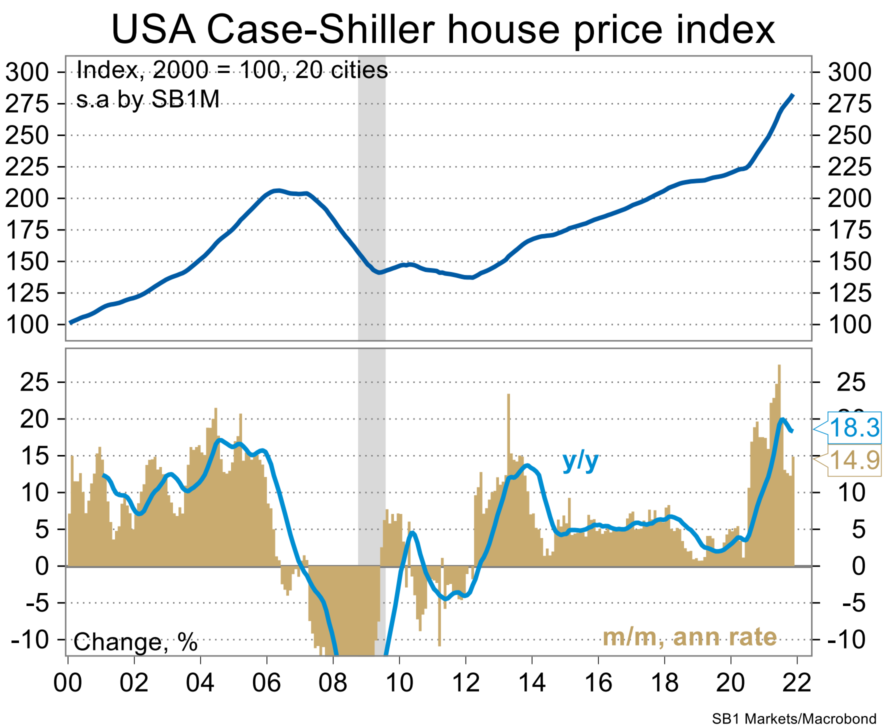
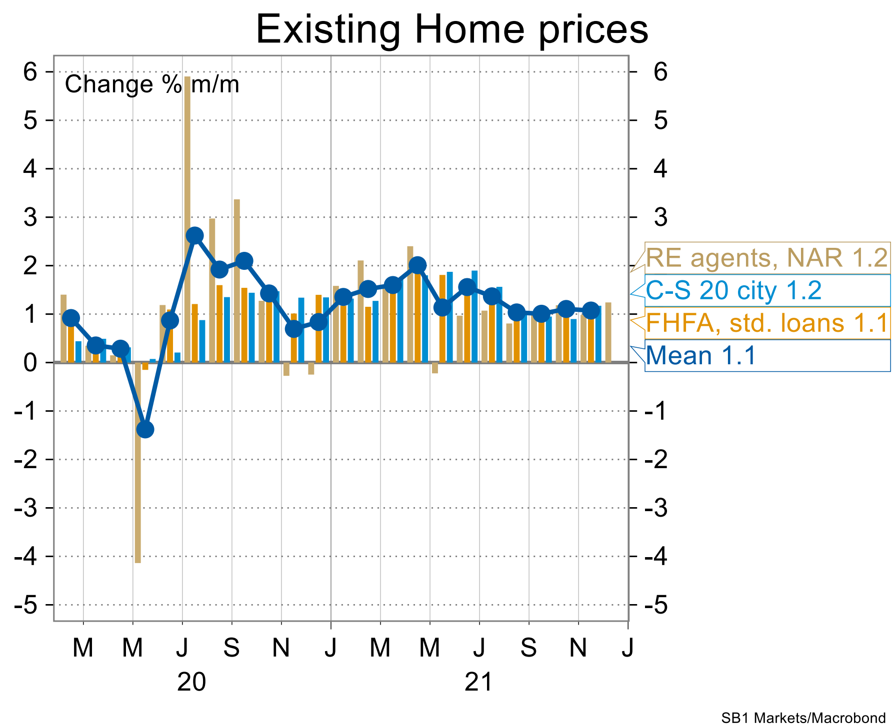
House prices inflation remains strong, 16 – 19% y/y. Prices are up 30% vs. pre-p

The Case/Shiller index gained 1.2% m/m (14% annualised), and the annual rate is 18.3%!

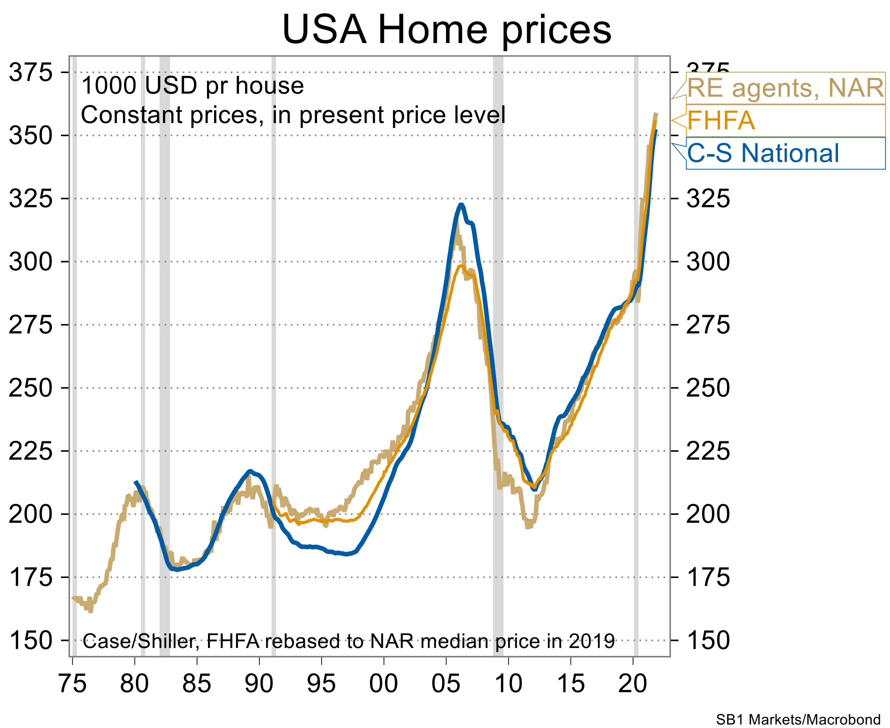


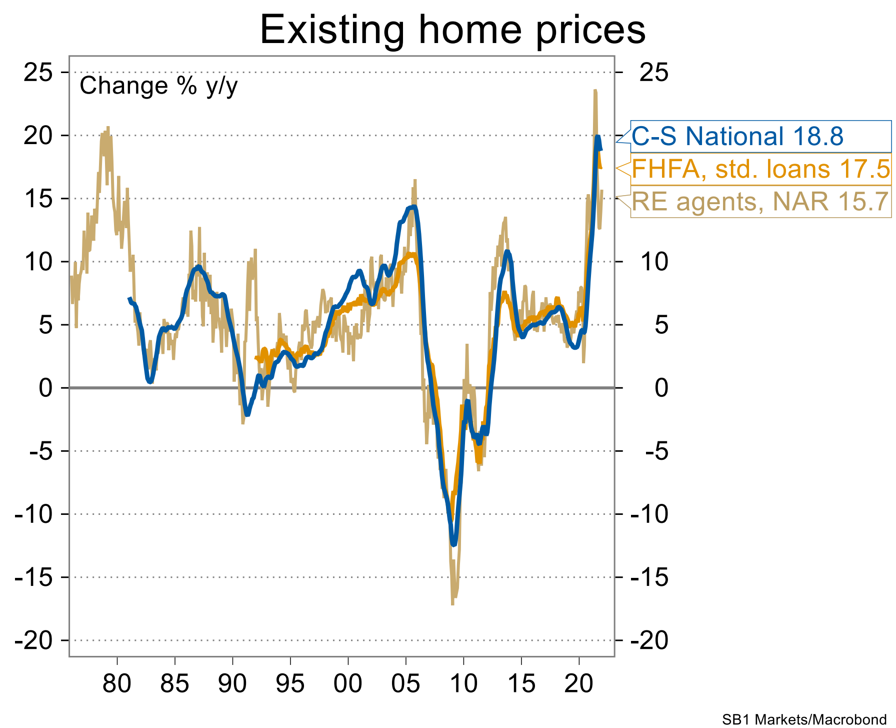


- **S&P's Case/Shiller's 20 cities** price index rose 1.2% m/m in November (Oct – Dec avg), equalling a 14.9% annualised pace, up from 0.9% in Oct. The annual growth rate was 18.3%, down 0.1 pp, expected 18.2%. In July prices were up 20.0%, the highest growth rate since just after WWII. The **national C-S index** is up 18.8% y/y. <u>Prices are up 28% since before the pandemic</u>
- **The FHFA** (Federal Housing Financing Agency) price index, which covers homes with loans guarantied by the government sponsored Fannie Mae or Freddie Mac ("Husbankene", has a countrywide coverage), rose 1.1% in Nov, and are up 17.5% y/y. The ATH annual rate before the pandemic surge was 11%, ahead of the housing crisis 15 years ago (chart next page)
- **Relators** reported a 1.2% price lift m/m in December, and the annual rate is 15.7%

Some special house data – both measured y/y & the real price level

Real prices are now 10 – 20% above the pre-financial crisis level



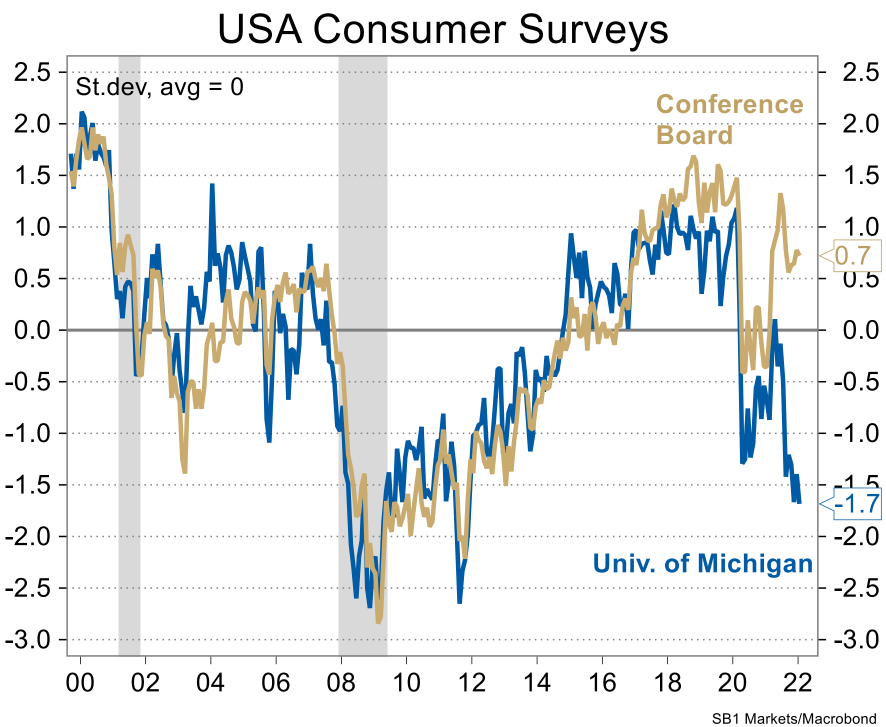


- Both the Case-Shiller National index, FHFA's index for homes with government sponsored mortgages (which includes most homes), and the realtors' price index reported the highest house price appreciation ever (or since 1948) during last year
- Real prices are far above the 2006 peak
- There are still some big differences vs the mid 2000 housing bubble
  - » Housing starts are at a lower level. The inventory of 2nd homes for sale is record low (vs high 15 – 16 years ago. However, the inventory of new homes for sale is climbing rapidly
  - » The debt/income ratio has fallen sharply since the peak before the financial crisis. However, credit growth has accelerated during the pandemic
  - » The savings rate/net financial investment has now fallen to below the pre-pandemic level– but the ratios are far above the level in 2005

SpareBank 1 MARKETS

Conference Board's confidence slightly down in Jan but miles above the UM surv.

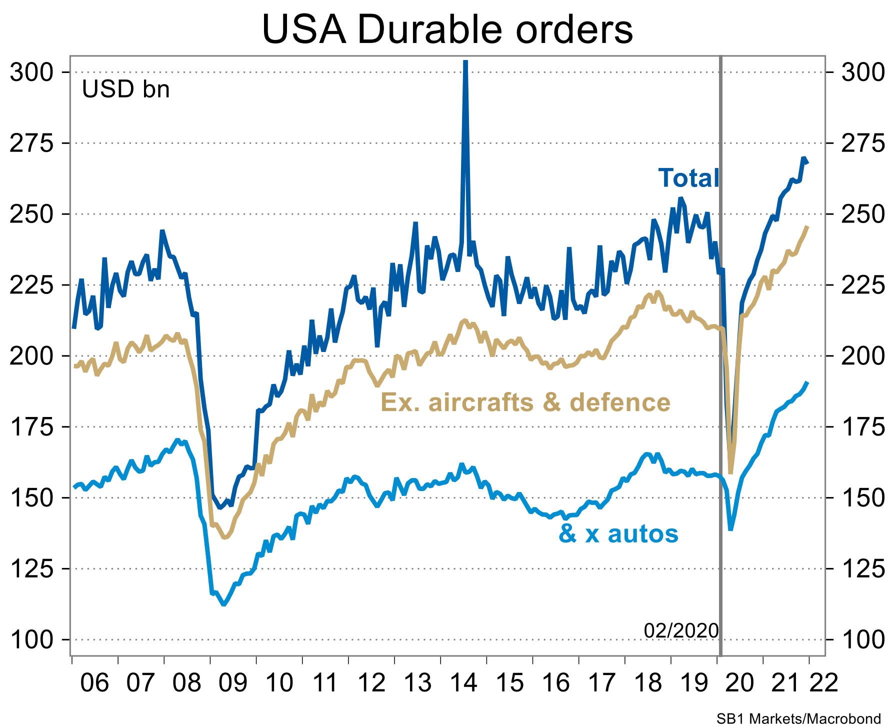
CB's index up 0.2 st.dev to +0.8, better than expected and miles above the Univ of Mich sentiment

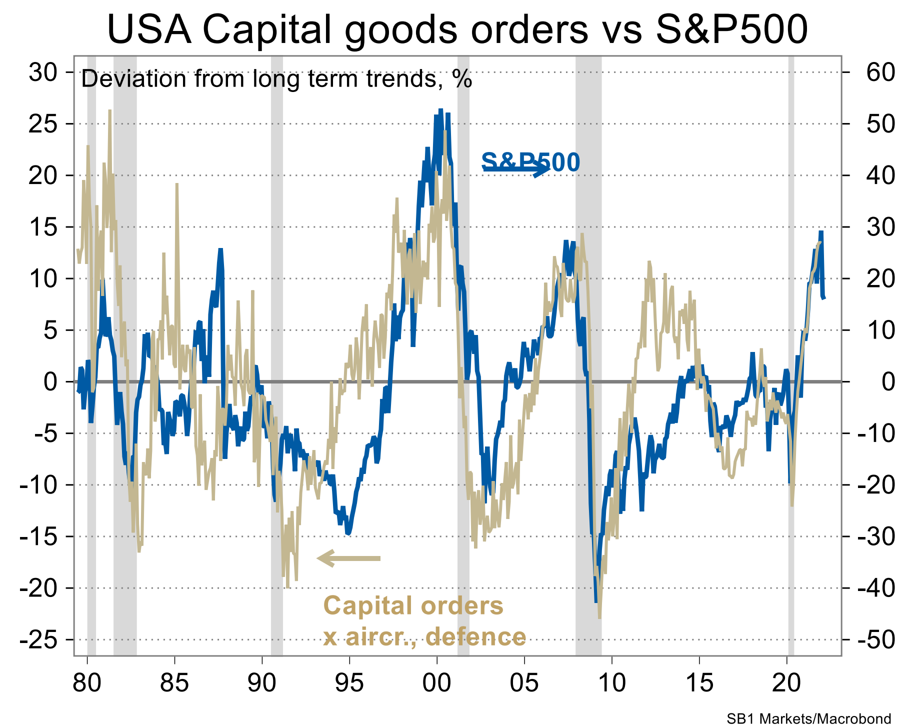


- The **Conference Board's consumer confidence** index lost 1.4 p to 113.8 in January, expected down to 111.7. The index is 0.7 st.dev above average (down 0.1). There were small changes in both the assessment of the current situation, and expectations
  - » Households still report a tight labour market, and they adjusted their spending plans upwards in January, home buying plans are now the most upbeat in years
- **University of Michigan's sentiment** survey is still way below a normal level, at -1.5 st.dev – even weaker than during the first wave of virus outbreak last spring (Jan was marginally revised down)
  - » If the UM survey is falling faster than CBs survey, often something unfortunate happens afterwards, check next page

Strong order inflow in December too

However, investment orders may be slowing somewhat





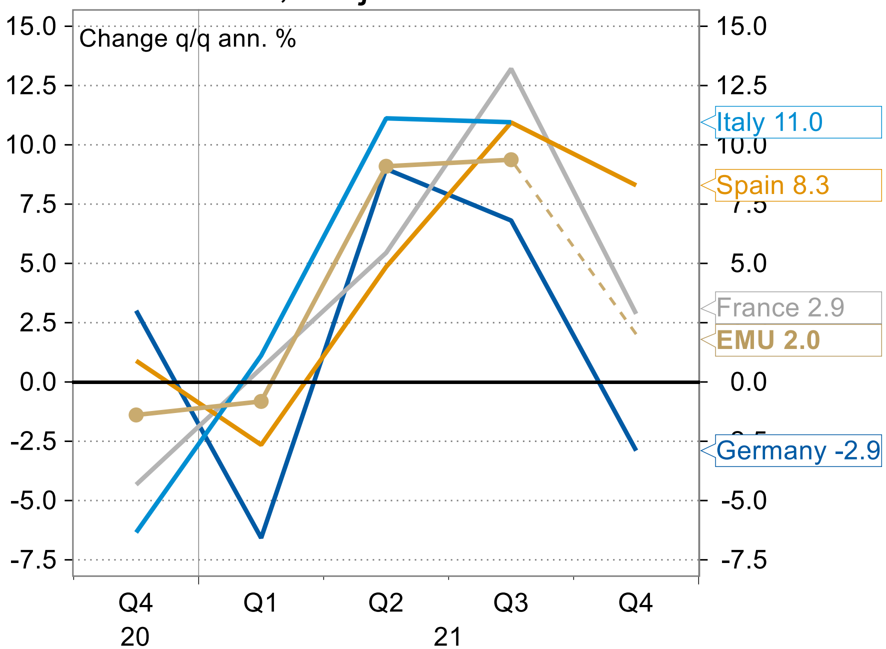
- **Total durable** orders fell by 0.9% in December, expected down 0.5%. Both the volatile aircraft & defence orders declined
  - » Ex these two components, the 'core' rose by 1.4%, well above expectations – and the trend is strong
  - » Auto orders rose too, but 'core x autos continued upwards
- **Core <u>investment</u> goods orders** were up 0.6%, and the trend is still straight up
- **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

SpareBank 1 MARKETS

GDP slowed in France and Spain, fell in Germany

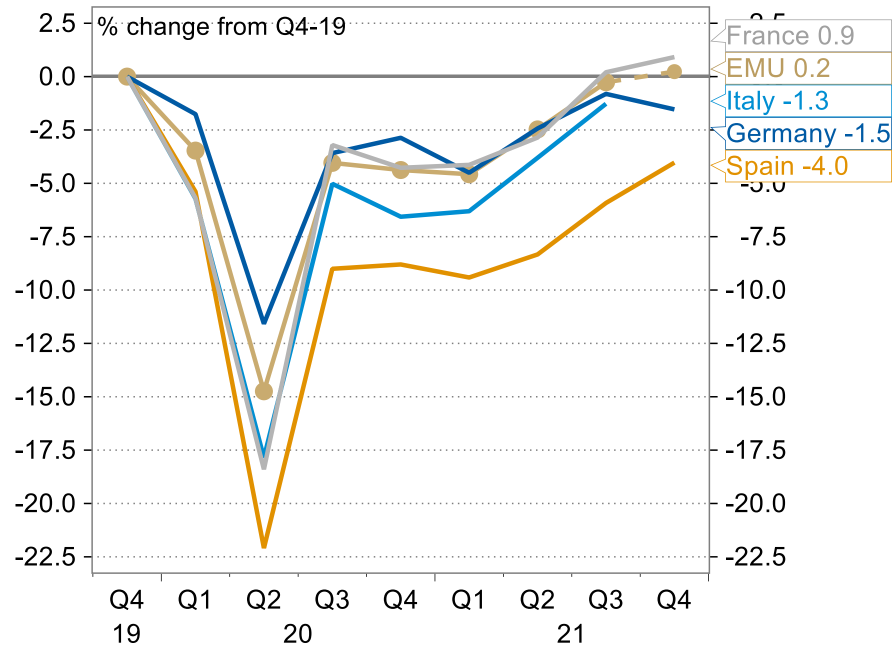
Italy has not yet reported. Spain remain far below the pre-pandemic level – Germany too

GDP, major EMU countries



SB1 Markets/Macrobond

GDP

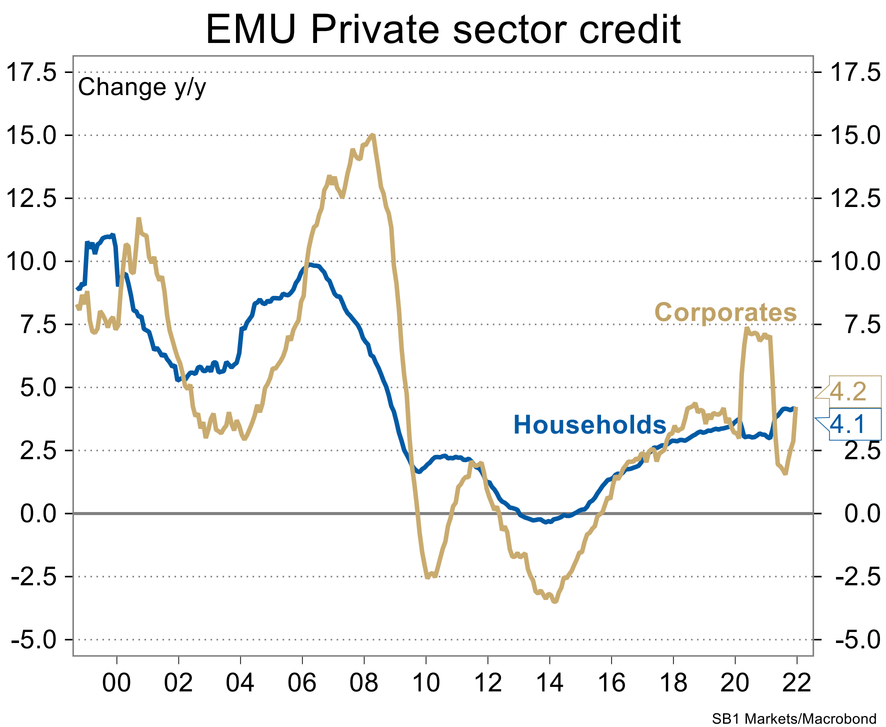


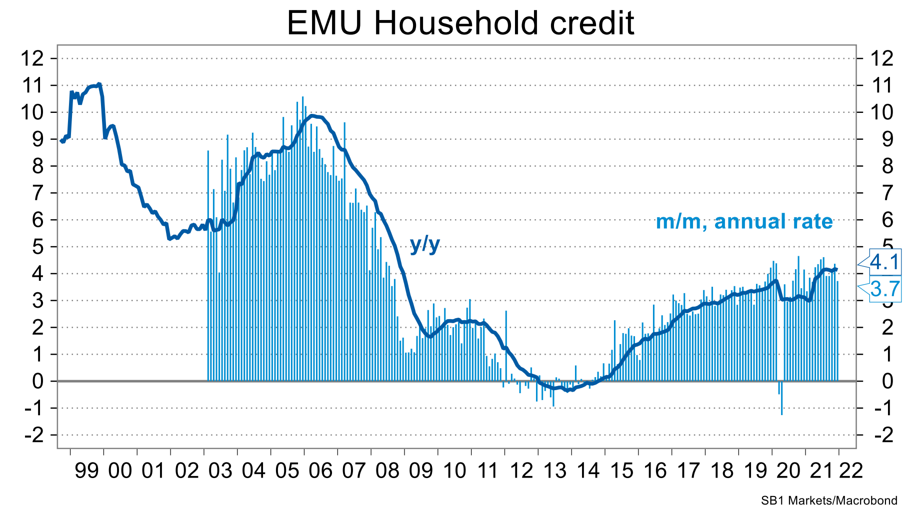
SB1 Markets/Macrobond

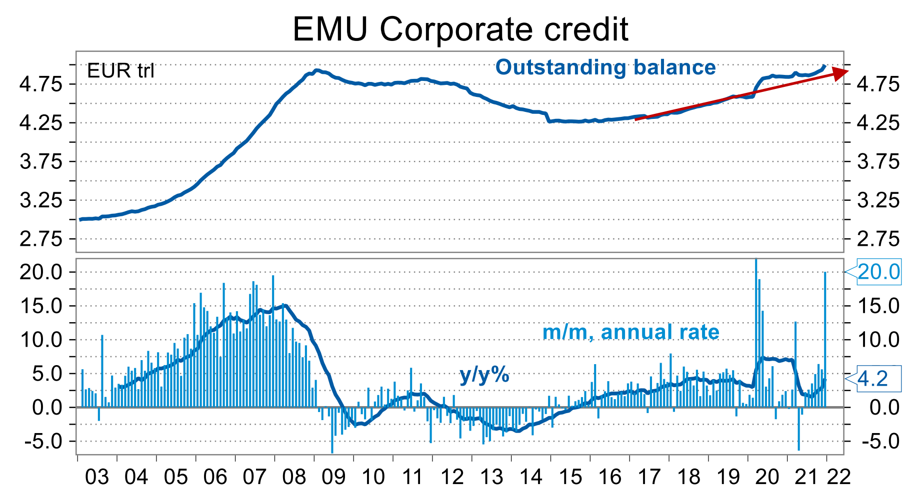
- GDP grew at a brisk pace in **Spain**, and not much down from Q3 (8.3% vs. 11%). GDP is still down 4% vs. Q4-19
- **France** slowed sharply to 2.9%, expected 2%. The level is down 0.9% vs. Q4-19
- **Germany** contracted by 2.9% (0.7% not annualised, in line with Bundesbank estimate two weeks ago). Level is down 1.5% vs Q4-19
- **Italy** (and the smaller) countries have not yet reported Q4 data
- We estimate a 2% growth pace (0.5%) for the whole **EMU region** . If so, GDP will finally cross the Q4-19, by 0.2 pp

Some life in corporate borrowing recent months, household debt up 4%+

Household debt is not accelerating – no credit boom to be seen



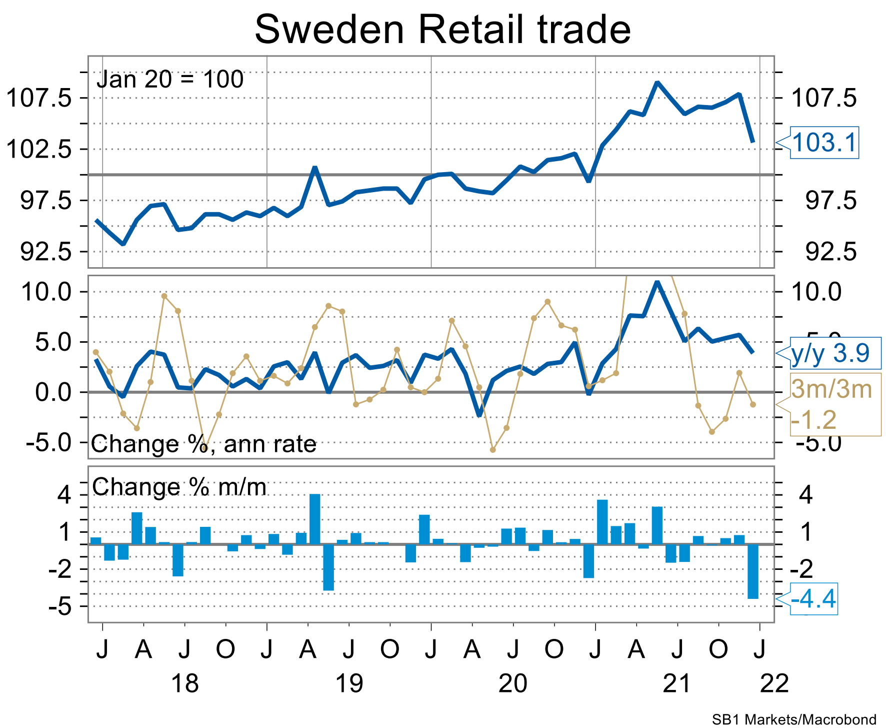


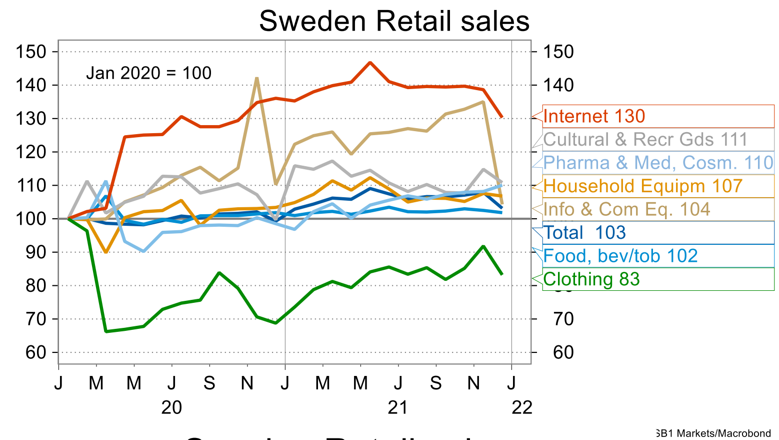


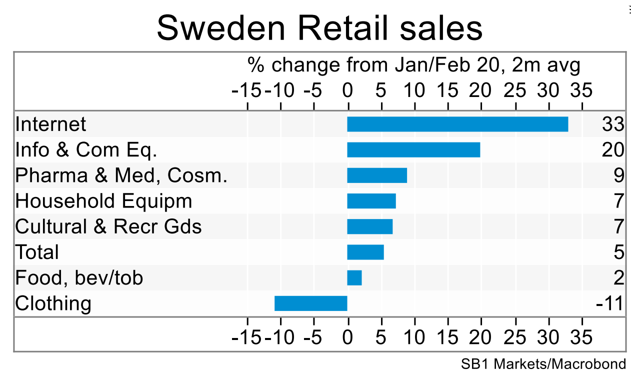
- The corporate debt level is still above the pre-pandemic trend growth path, and growth is now gaining some speed from month to month, with a substantial lift in Dec, very likely a one-off
  - The average growth over the past 2 years is 3.6%
  - The credit volume is not higher than in 2008 in nominal terms – and sharply down in real terms or in % of GDP

Retail sales down 4.4% in Dec, just out of the blue (like in Norway)

A broad decline in sales, info & communication equipment down by 23%, clothing 10%



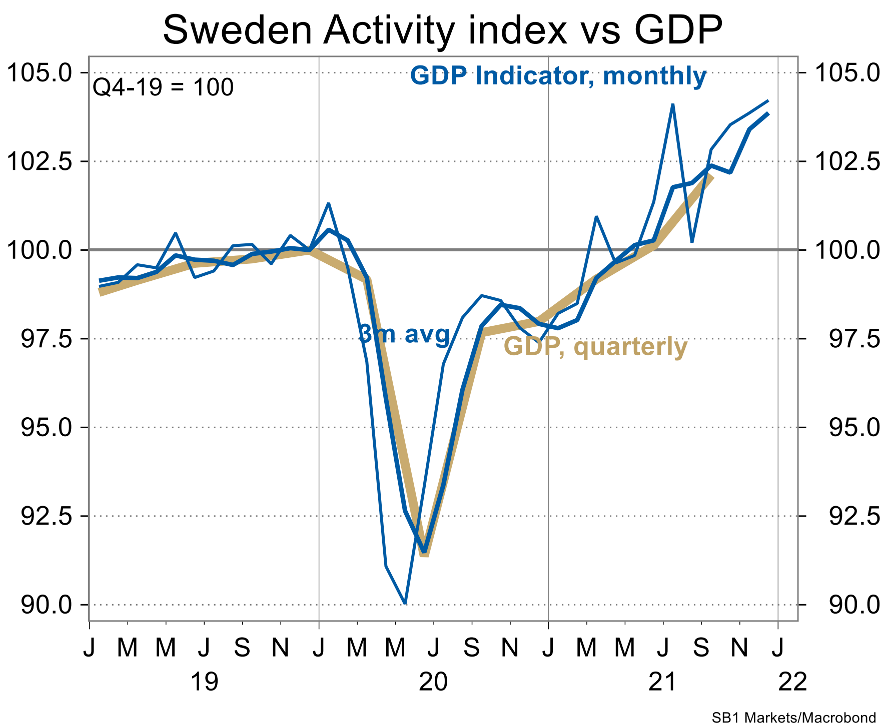


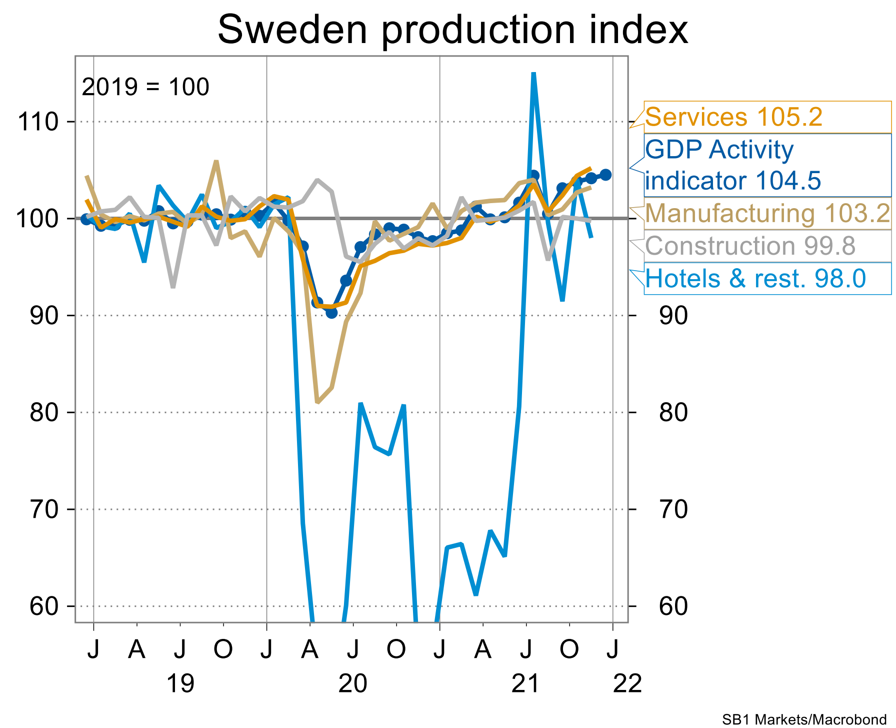


- Sales were not specifically strong in November – and the level in Dec was the lowest since last January.
- The sectoral differences are suspicious, a 23% drop in mobile phones etc does not seem likely
- Clothing is still weak, now down 17% vs. the Jan-20 level
- Retail sales in December is probably below a reasonable long term trend

GDP still on a strong recovery path in Dec, Q4 up 1.4% (5.6% ann.), +4.5% vs pre-p

Details not yet available but the strong recovery is still intact

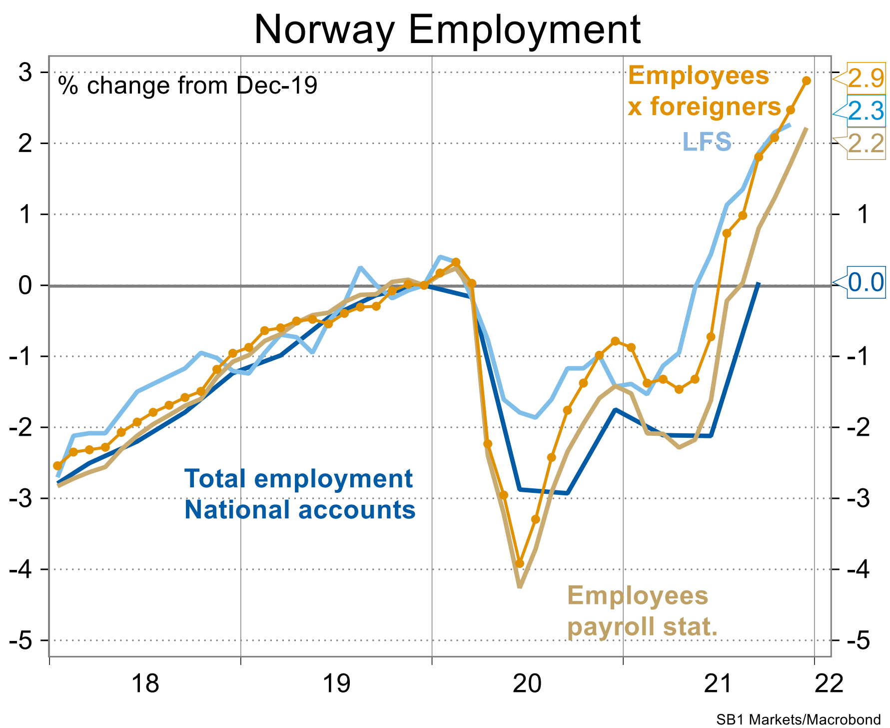




- **The outlook** remains excellent, according to Swedish companies. THE KI (NIER) survey is still close to ATH, and the PMI is the best in the world.
- In Nov, hotels and restaurants reported a decline in activity – but from above the p-p level to 2% below
- We still wonder if the Riksbank's extremely expansionary monetary policy stance is appropriate

Reg. employment up 0.4% m/m in 'lockdown' Dec, 2.2% above pre-p level

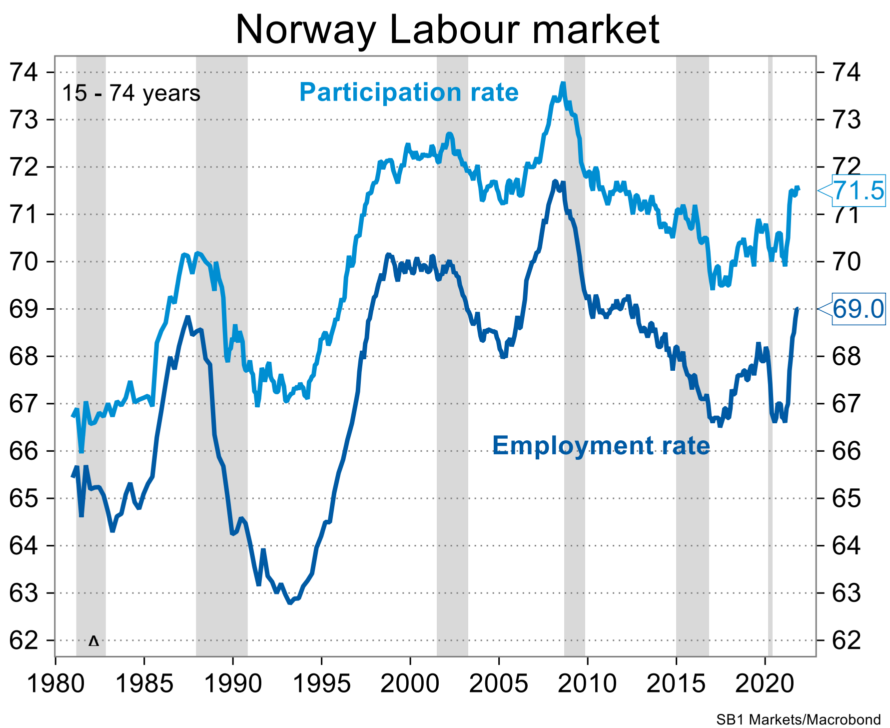
Employment up approx. 2.9% among persons living in Norway. The LFS confirms strong empl growth



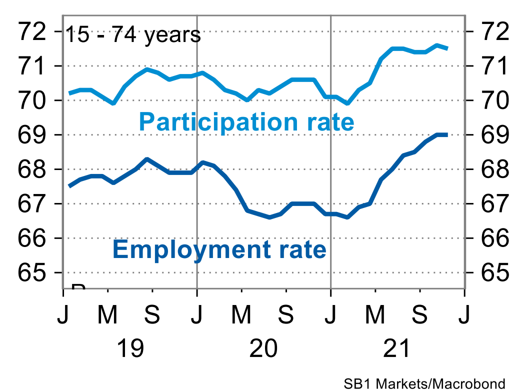
- The increase in the **register based no. of employees** in December suggests at continued growth in Mainland GDP above trend, at least until mid December
  - » The reference period is the week containing the 16th in months. Stricter corona restrictions were imposed by the mid of December and the impact came too late to be registered in the payrolls stats (a-ordningen)
  - » Payrolls grew by 0.4% m/m and is now 2.2% above the level in Dec-19 (Nov level was revised up by 0.2%)
  - » We estimate the no. of employees among permanent residents (Norwegian and foreign born) to be 2.9% above the pre-pandemic level (based on our Q4 estimate for foreign workers on short-term stay, not yet published)
  - » Growth is slowing but just slowly
  - » The increase in employment is broad based, check 2 pages fwd
- **The LFS** ('AKU' survey) employment data (both employees and self-employed, with permanent residency in Norway) reported a 3' (0.1%) growth in employment in Nov (avg Oct-Dec from avg Sept-Nov), and by 25' over the past 3 months, equalling 0.9% or a 3.5% annualised pace
  - » LFS employment is up 2.3% since before the pandemic, and both participation and employment rates are far above the pre-pandemic level – and the LFS unemployment rate has 'collapsed'
- **National Accounts** reported a 2.1% growth in total employment in Q3 – up to the same level as in Q4-19. These NA data includes foreigners on short-term stay

The employment rate is still trending up, participation may have flattened

Less competition from foreigners helped more permanent residents back to the labour market?

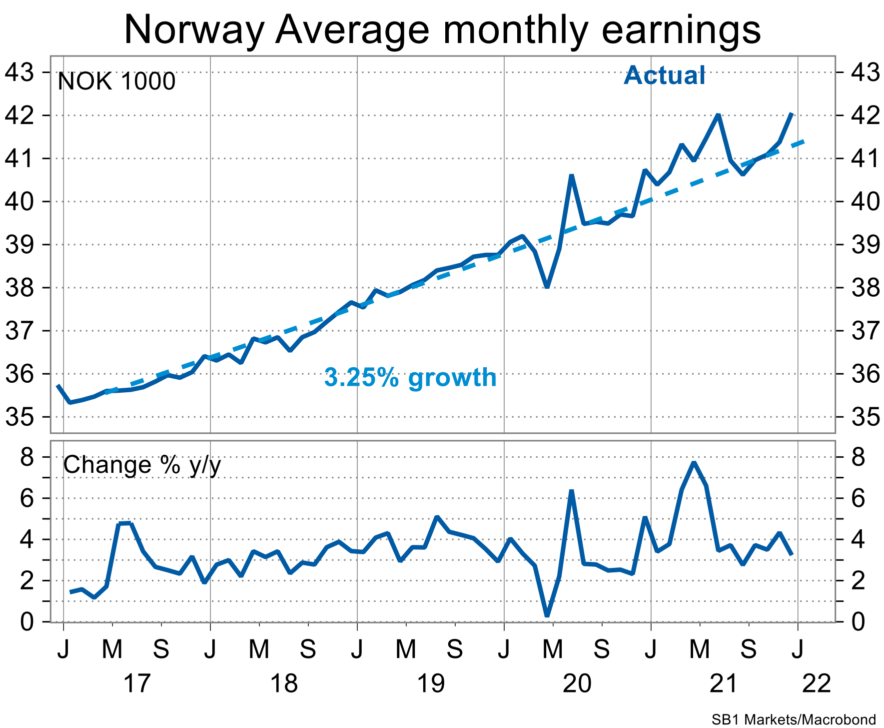


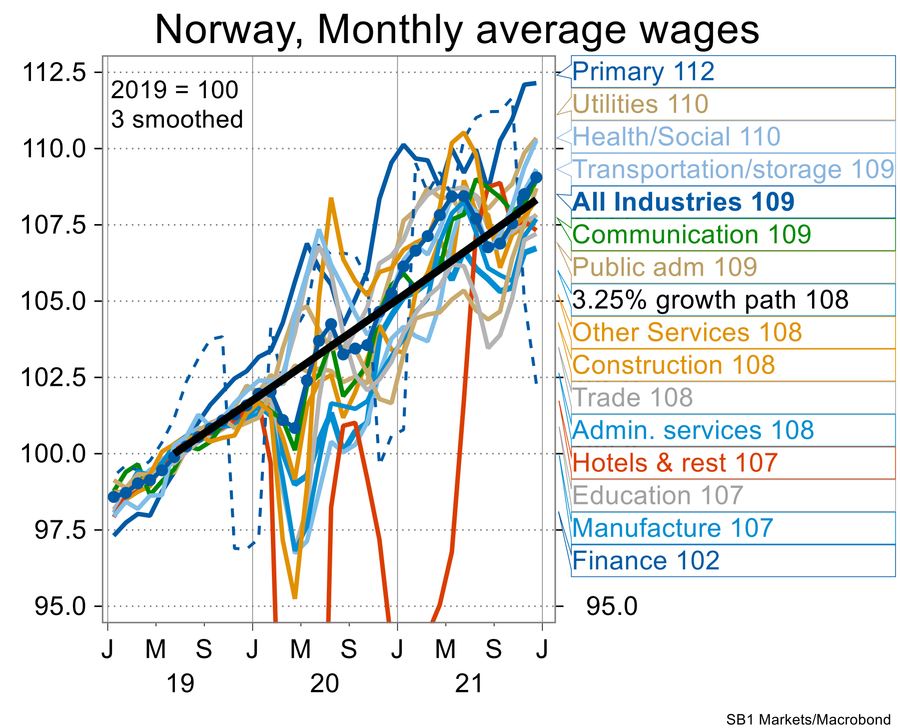
- **The employment rate** was flat in November, at 69%
  - » Ahead of the pandemic the rate was 68.1 – 68.2, and it is up from the 66.4 through in early 2021 (and from the same level in 2017, after the 'oil crisis'). The employment is measured in % of the working age 15 - 74 y population
  - » The employment rate is the highest since 2012
- **The participation rate** is also well above the pre-pandemic level but it has more or less flattened at 71.5% since last June. The participation rate is also at the highest level since 2012
- These monthly data are volatile but the flattening of the participation rate since the early summer even if demand for labour is still increasing <u>may indicate that the easy part of 're-engagement' is behind us</u>
- **Working age population** growth is 0.6% over the last year (Q4 est), in line with the moderate growth ahead of the pandemic



Higher wages in December, trend may now be above the 3.25% path

Substantial sectoral differences, in Dec (seas. adj.) wages in finance fell

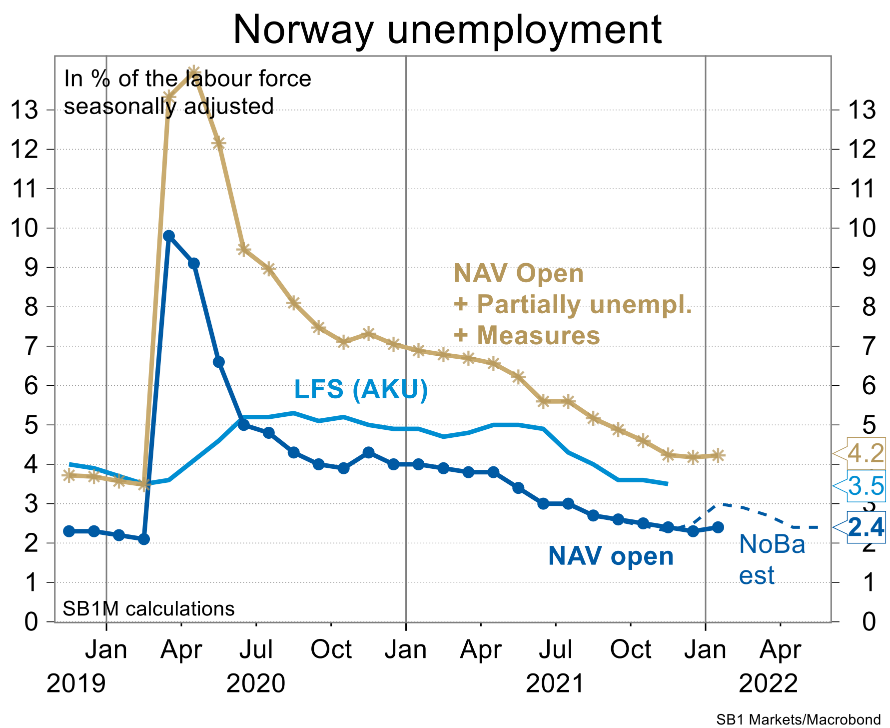


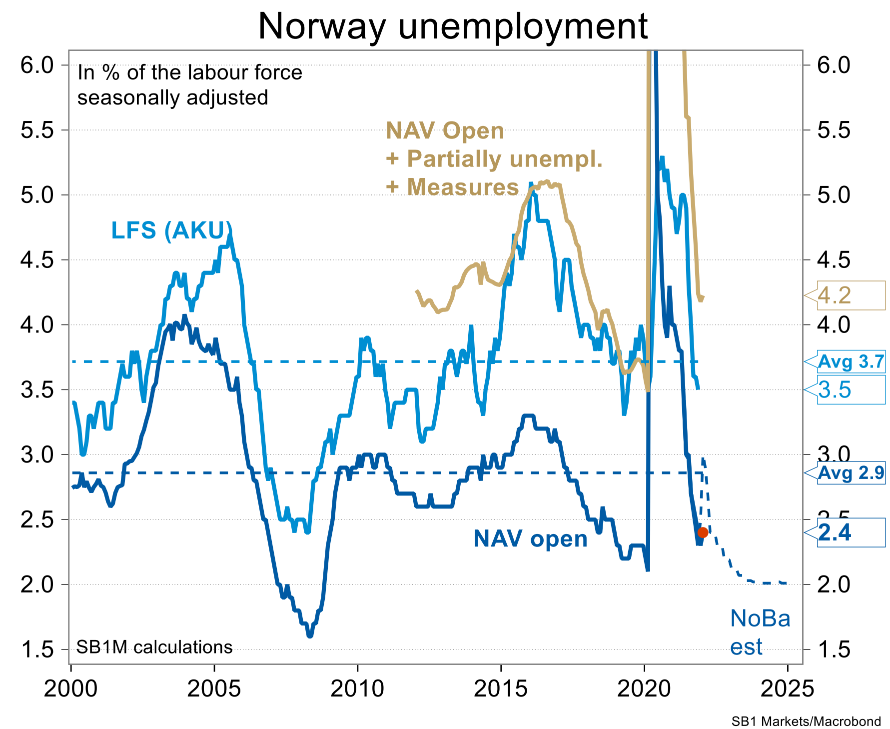


- Monthly average cash earnings are rather volatile, also depending on hours worked, bonuses
- Earnings have been above the 3.25% growth path from the start of the pandemic until June. The return of low paid service sector workers took the average down – before the average wage rate shot up in

Just a marginal increase in unemploym. in Jan, 0.1 pp to 2.4%! NoBa expected 3%

The LFS survey reported a 0.1 pp decline in Nov, to 3.5%. Both below consensus (but as we expected)

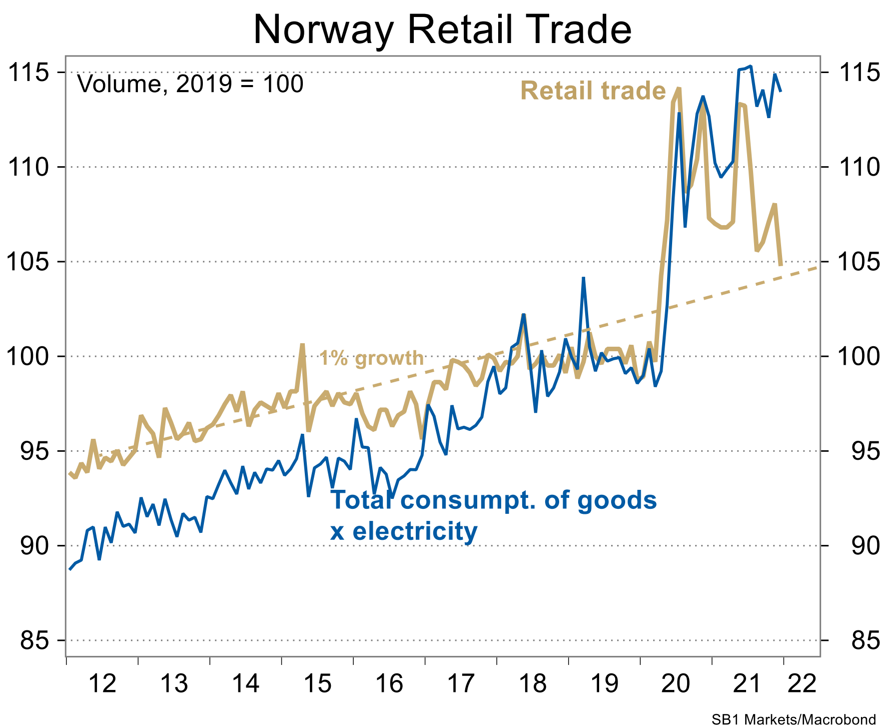


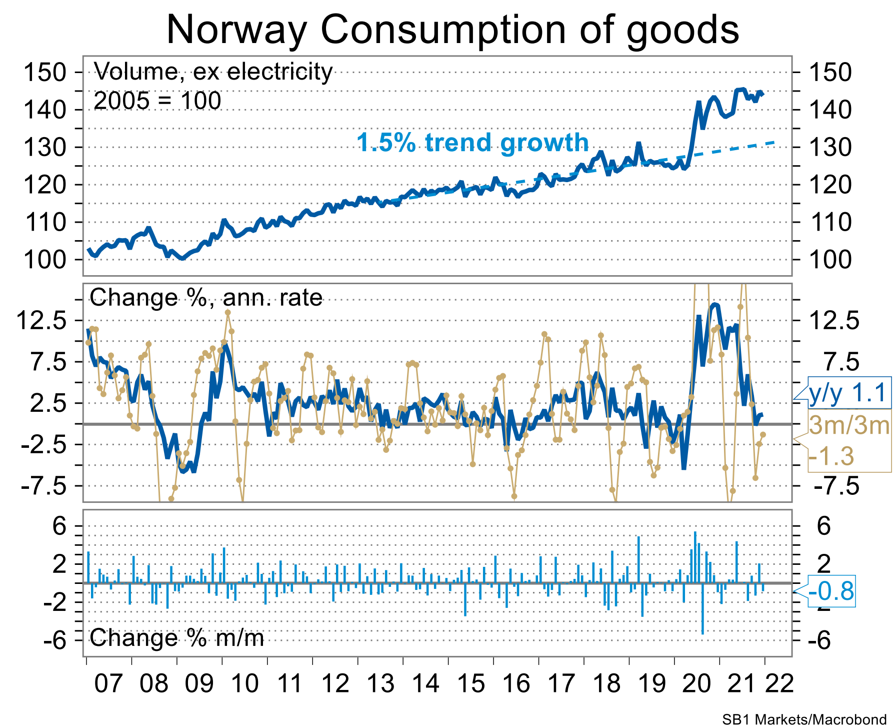


- **The 'full time' open NAV unemployment**, which includes furloughed workers, rose by 900 persons in Jan (seas. adj) to 67' we expected +3' to 68' (Dec was revised up by 1.3'). The rate added 0.1 pp to 2.4%, as we expected. In Dec. NoBa assumed an increase from 2.5% (outcome 2.3%) to 3.0%. Unadjusted, the rate as we expected rose to 2.6% from 2.2%, consensus was at 2.7% The 2.4% rate is well below the 2000 – 2019 avg at 2.9%, and just 0.3 pp above the pre-pandemic level. Barring the small Jan hiccup, unemployment is falling rapidly everywhere and for all sorts of labour .The no of furloughed workers increased, while ordinary full time unemployment fell further
- The number of **partially unemployed** (not included in the ordinary unemployment no.) rose by 1' to 40', and including measures, the **total unemployment** fell by rose 1' to 121', to 20' above the pre-pandemic level. The rate was unchanged at 4.2%, up from 3.5% in Feb-20
- The inflow of **new job seekers** fell further, and the **inflow of new vacancies** rose further from a high level the previous 6 months
- Last week: **The LFS (AKU) unemployment rate** nosedived by 0.4 pp to 3.6% in Sept, far more than expected, as the **employment rate** rose further

Retail sales sharply down in December, total consumption of goods still strong

Sales fell by 3.1%, we expected -1%. Sales are now back to a ‘normal’ level; Consumption is far above

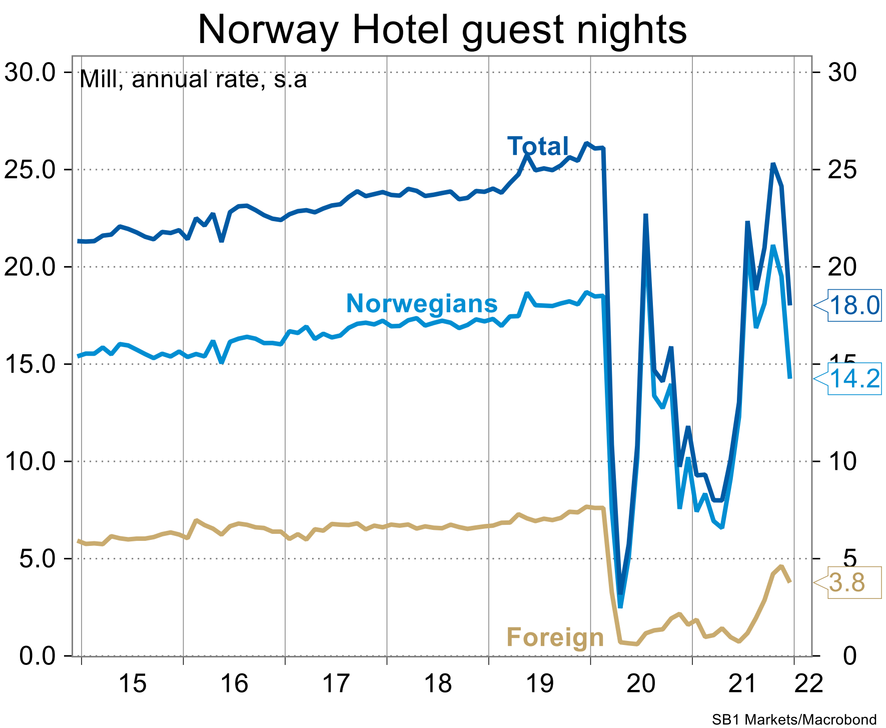


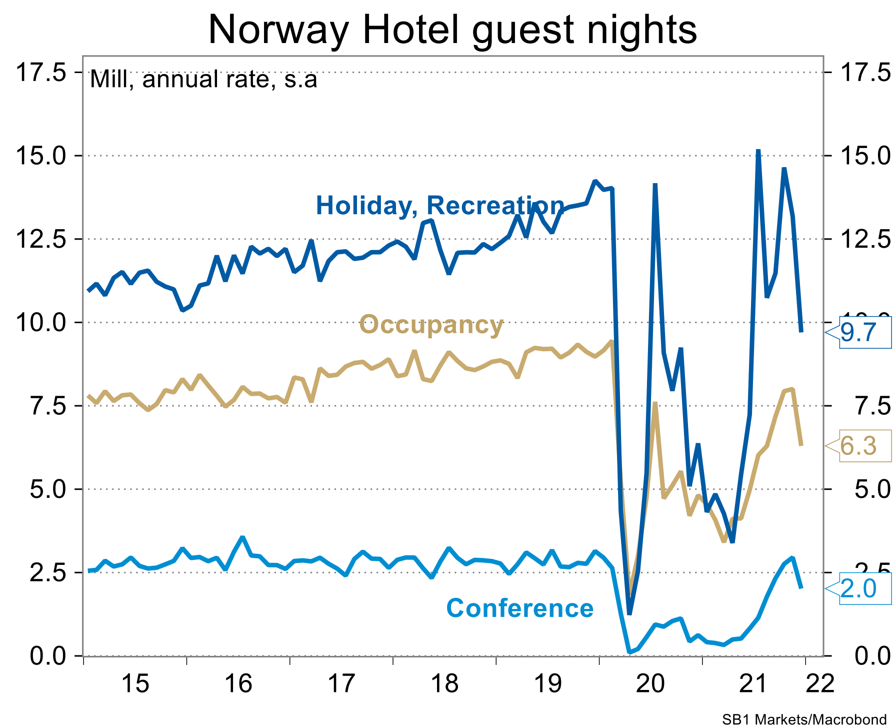


- **The consensus forecast** was -0.3%. Sales have been far more volatile than normal during the pandemic, and monthly data have been close to useless. Sales have been trending down through last year, from a very high level – and is now approaching the pre-pandemic trend, which was rather modest
- **In December**, sales of household equipment, electronics and clothing fell 6 - 9%, while sales of sport equipment rose 8%
- **Total household consumption of goods** (x electricity) subtracted just 0.8%, supported by very strong auto sales – which rose to the 2nd highest level ever in December
  - » The main reason for the difference between retail sales and consumption of goods during the pandemic has been strong auto sales and the decline in sales of building materials, which is included in retail sales but not by much in households’ consumption of goods

An Omicron hit in December, hotel guest nights down 25%

Guest nights were back at normal level in Oct/Nov but were hit by restrictions again in December

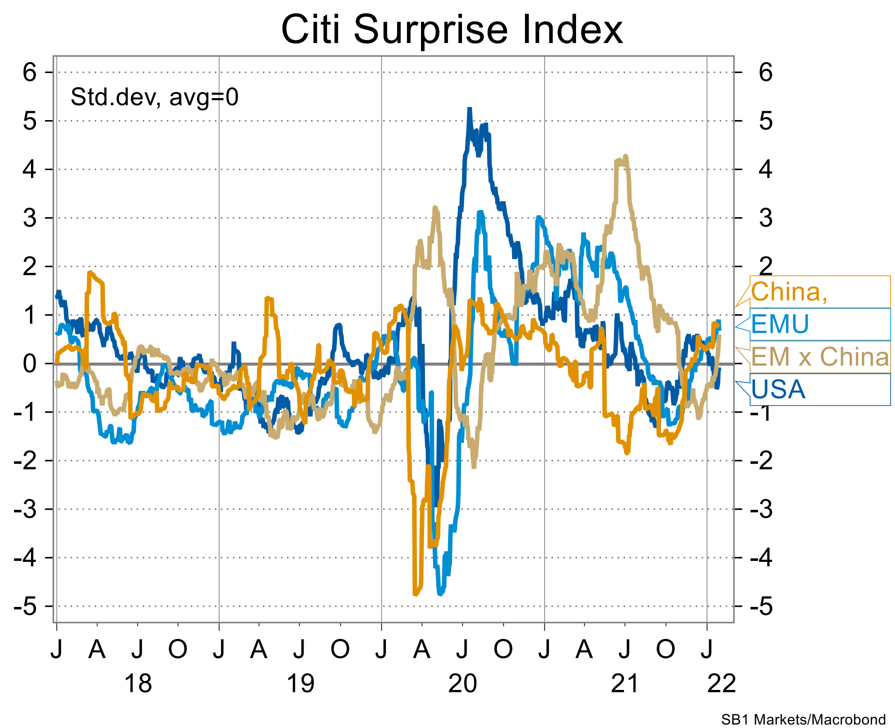


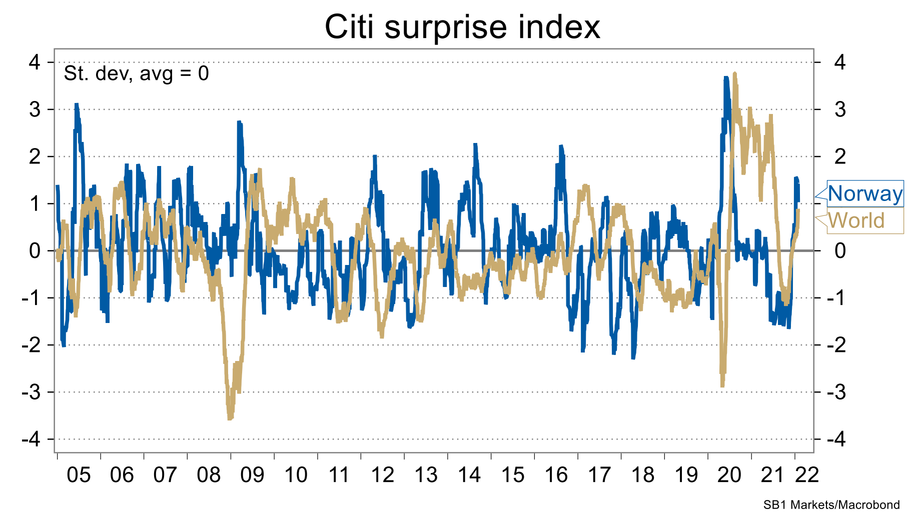


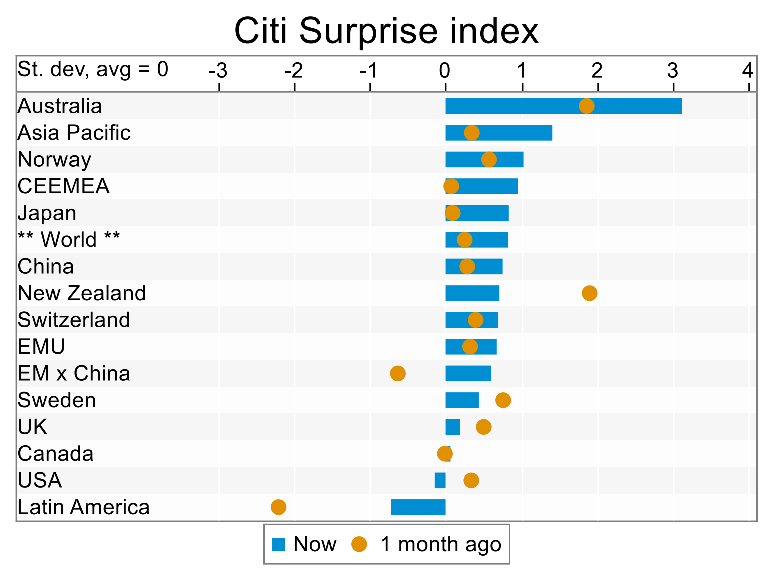
- **The no. of guest nights** recovered quickly last year, as we are pretty sure traffic will resume to a normal level as soon after virus restrictions are fully lifted
- **Business guest nights** (sum occupation & conferences) had almost recovered before the Omicron wave, while **Recreational traffic** was equal to the 2019 average. As foreigners in total are down 20%, we Norwegian recreational demand is far above the 2019 level

The global surprise index further up and slightly above par

Both EMU, China above and EM x Ch above average level again. Just US, Lat-Am below par







- **Norway** was surprising sharply on the downside through most of 2021, according to Citi. But in early December we crossed the zero line, and now we have suddenly moved up to the upper part of the list

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

Highlights

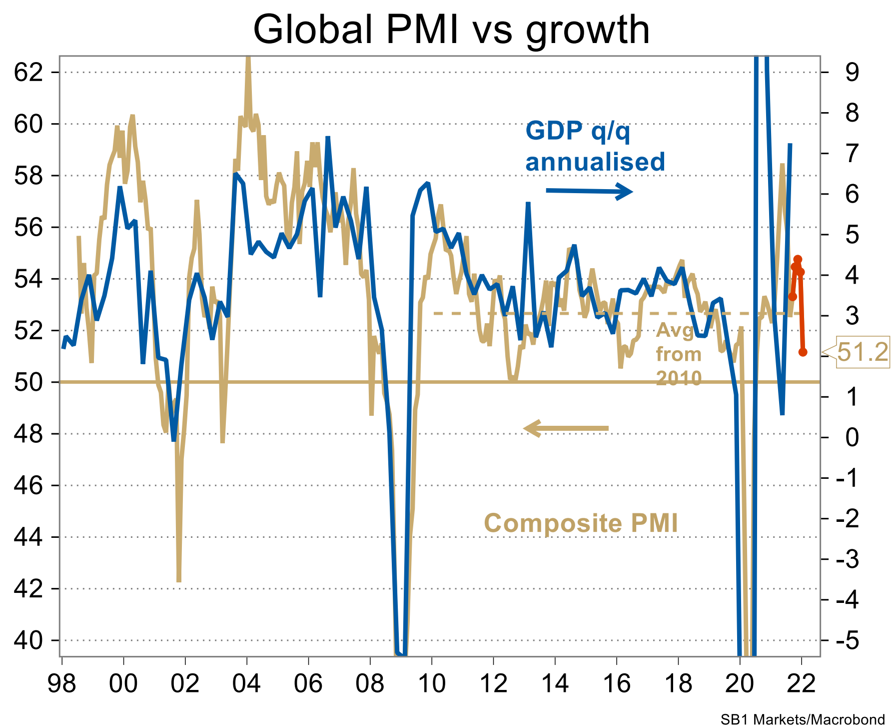
The world around us

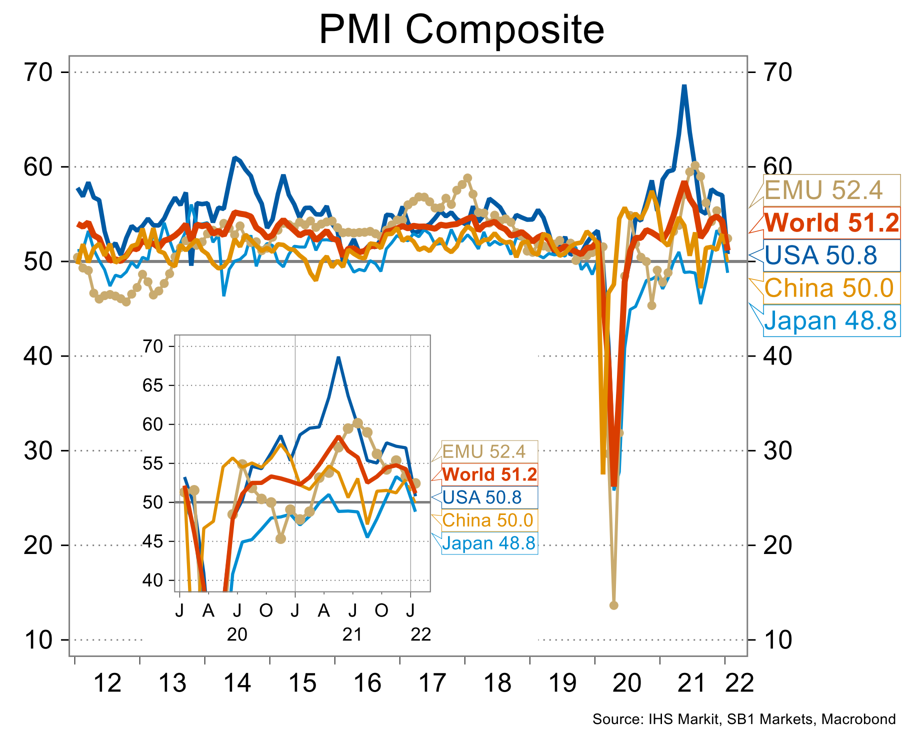
The Norwegian economy

Market charts & comments

The preliminary PMIs sharply down in January, so far led by the US

We estimate a 3p+ decline m/m to 51.2, equalling 2 pp lower global GDP growth, down to 2%



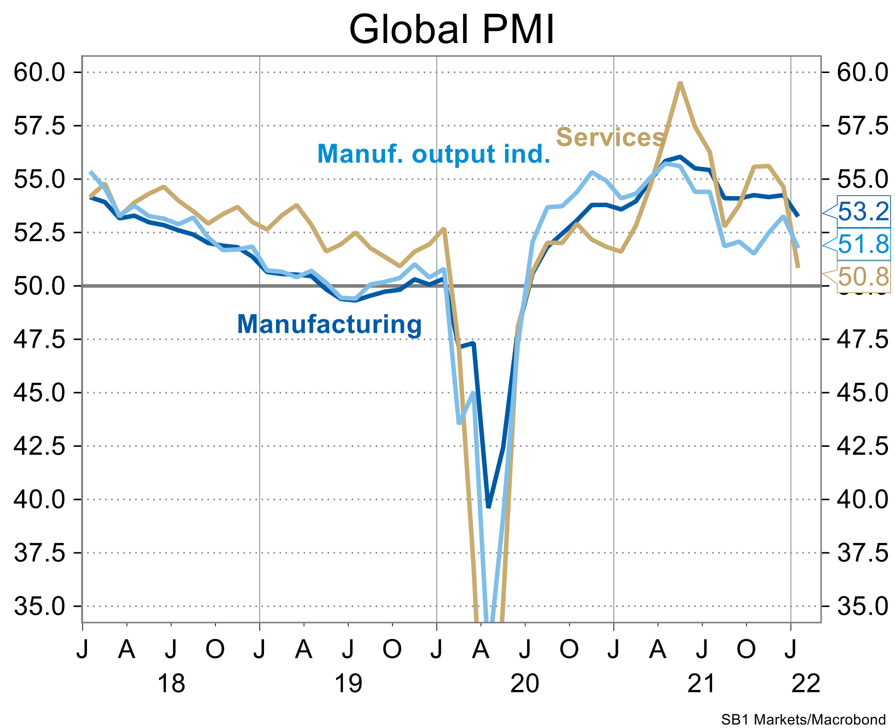


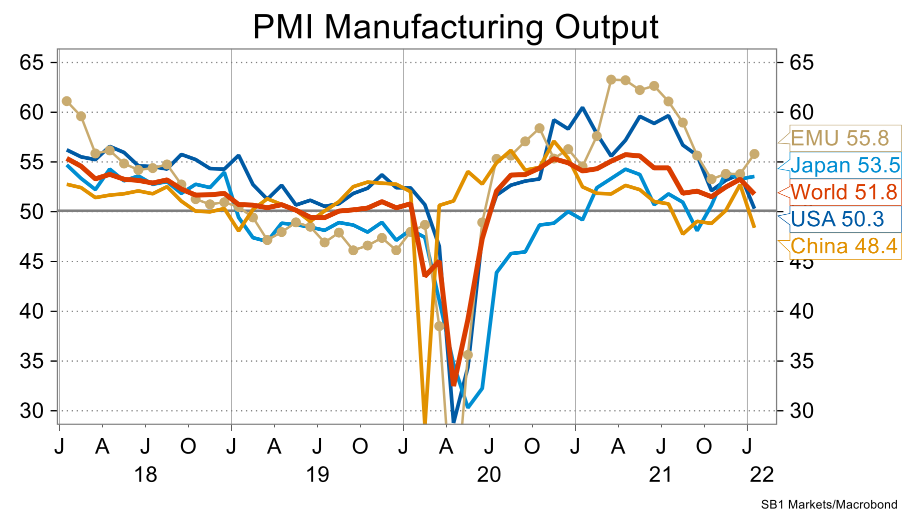
- **The flash composite PMI** January estimates declined, and more than expected everywhere (except for the UK). US surprised most at the downside, together with China, both in manufacturing and in services. Globally, the service sector index fell more than the manufacturing index (our est)
  - » The EMU kept better up, as Germany surprised at the upside, big time, especially in services
- **The delivery times index** fell for the 3rd month in row – and **price inflation slowed, at least input prices**. The **order index** fell to an average level (manufacturing). We doubt a sudden corona related decline in demand explains the reduced pressure in the value chain but perhaps a gradual normalising of demand for goods in the rich part of the world an less hoarding after the Christmas season ease the supply chains bottleneck?
- Services are probably mostly hurt by the Omicron wave – and much more than expected. Can it be something more?

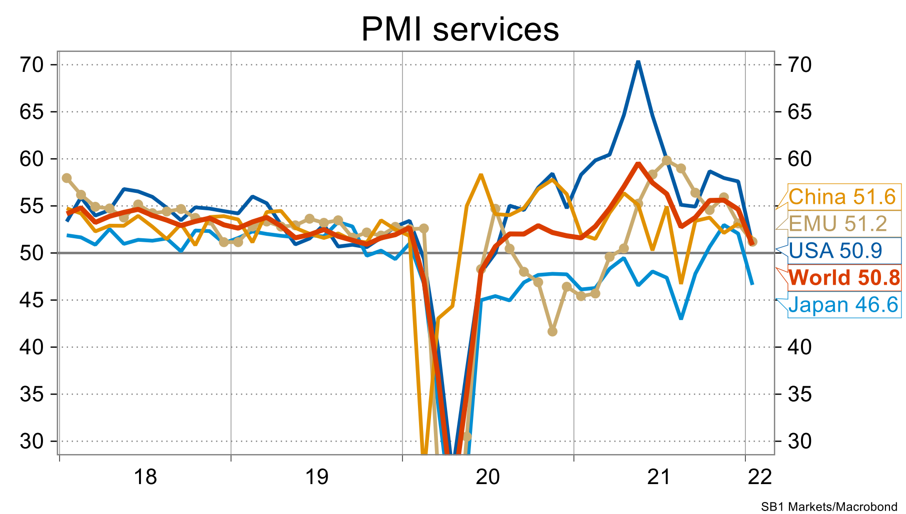
Our estimates are based on the preliminary PMIs from US, China, EMU, Japan UK, Australia. The estimates are uncertain, but usually by less than 0.5 p

A broad decline in growth in January. Is it just the (temporary) virus attack?

The service sector PMI probably down by almost 4 p, a very unusual setback. Manuf. output -1.5 p



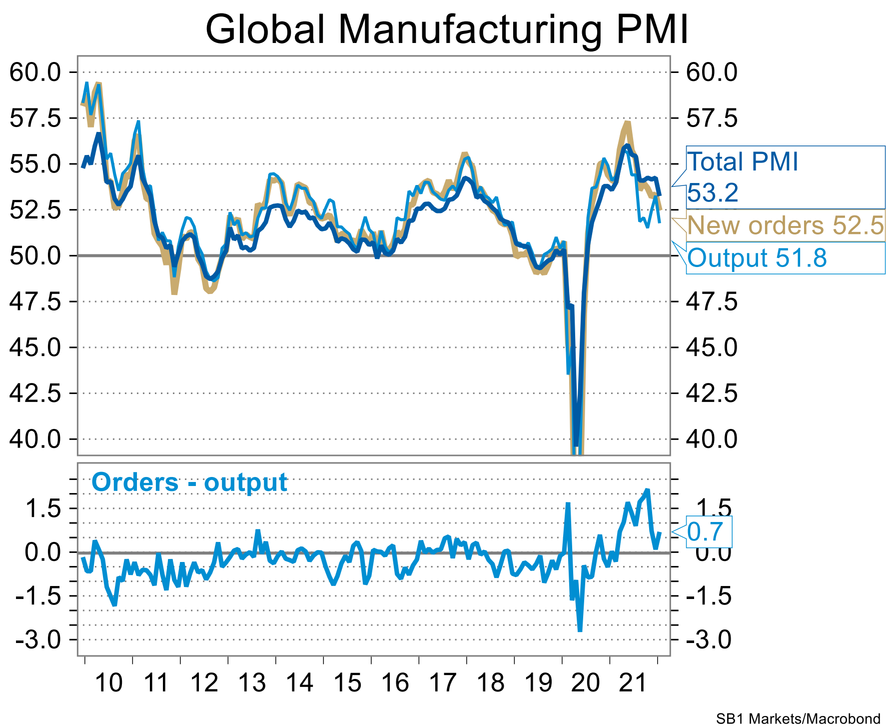


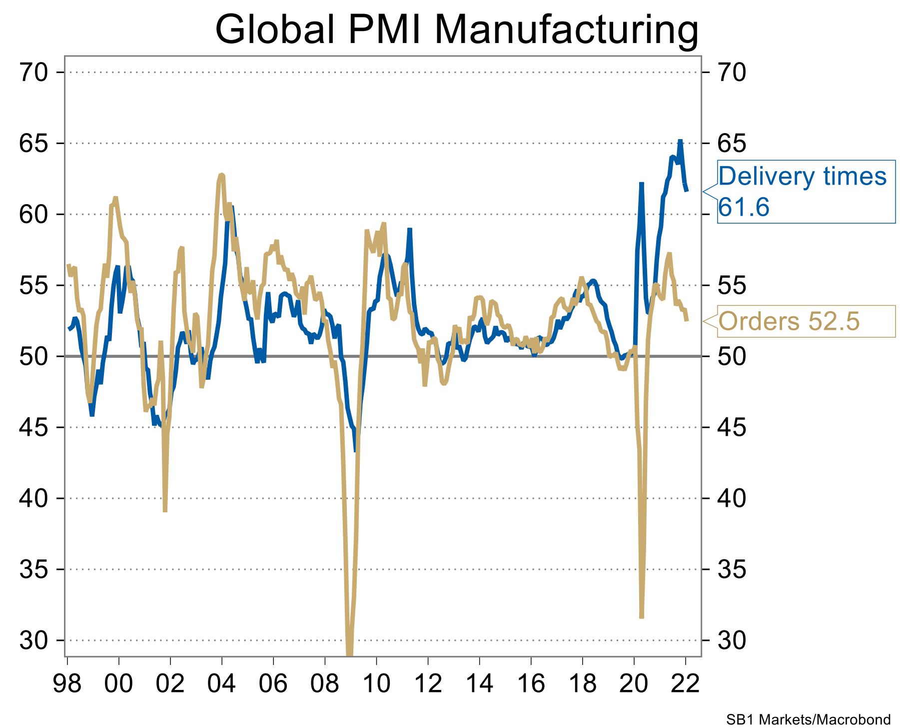


- Growth has very likely peaked, at least in the rich part of the world – but the setback in January is probably not the start of "the next recession"

Growth in manufacturing orders are slowing further, are back at an avg level

The delivery times index fell further in January but remains at a very high level

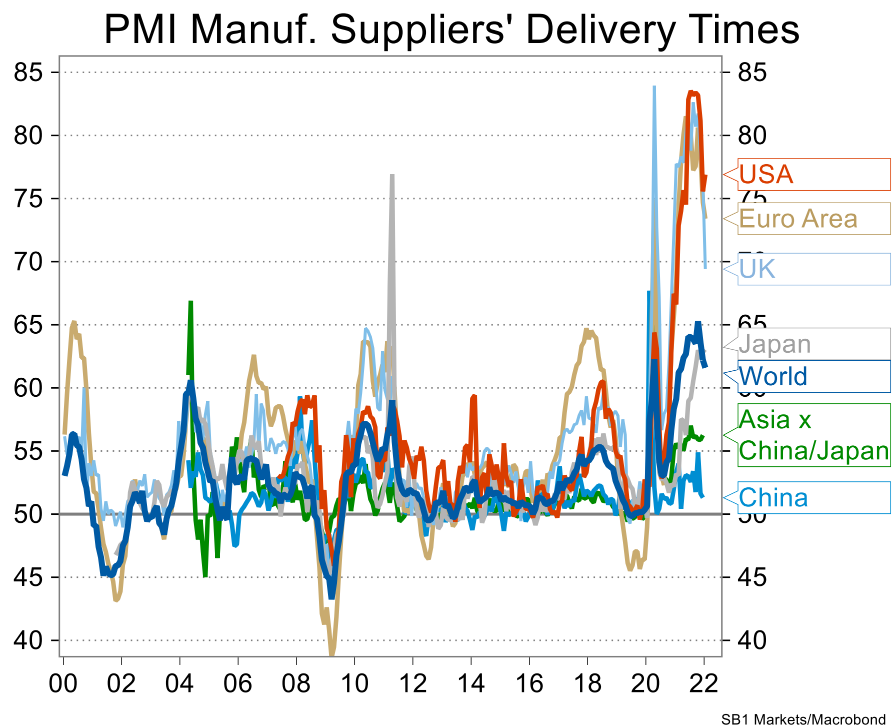


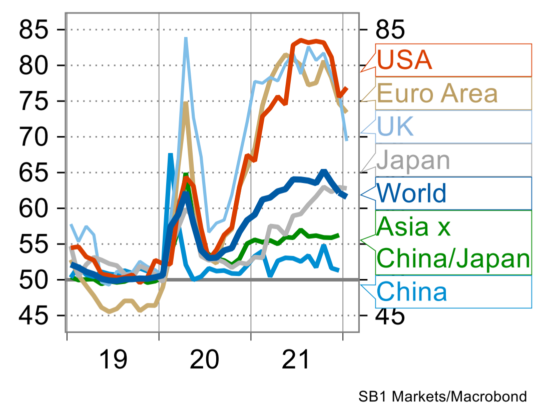


- **The current capacity in the manufacturing sector is more than reached**. The question is of course: <u>How much is capacity (transitory) impaired by the fight against Covid-19</u>? It is impossible to know before after the fact. Delivery times have increased more than growth in orders or production normally explain
- However, problems are most acute in Western countries where demand for goods have been much higher than normal. That may indicate the 'normal' capacity is not necessarily impaired but rather that the <u>exceptional strong demand for goods</u> – of course buoyed by exceptionally fiscal and monetary policy measures during the pandemic – is the main reason for the surge in delivery times and prices

Delivery times index further down in December

Are delivery times increasing less fast or are they slowing?



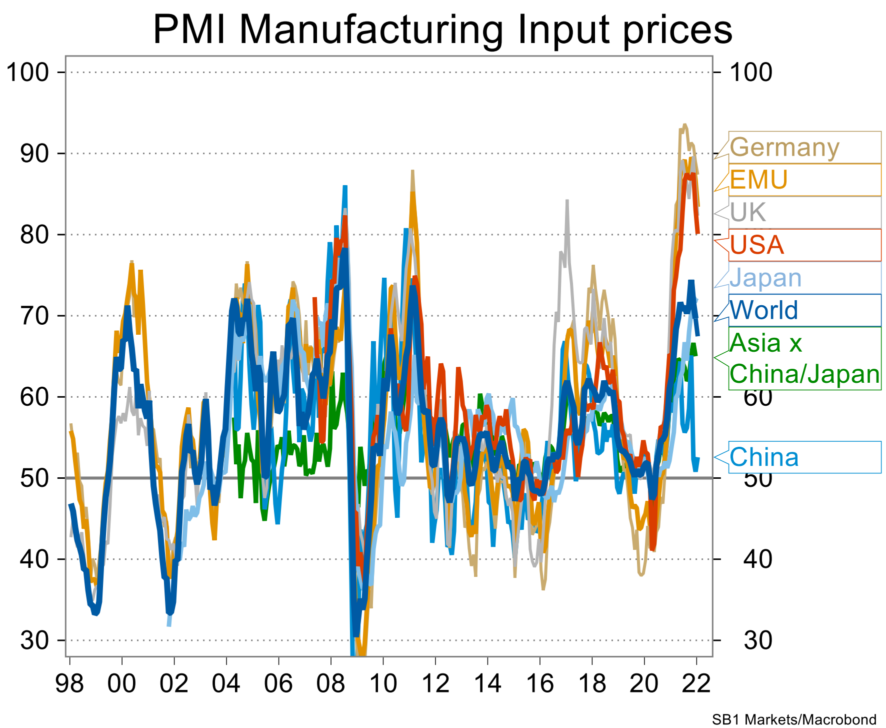


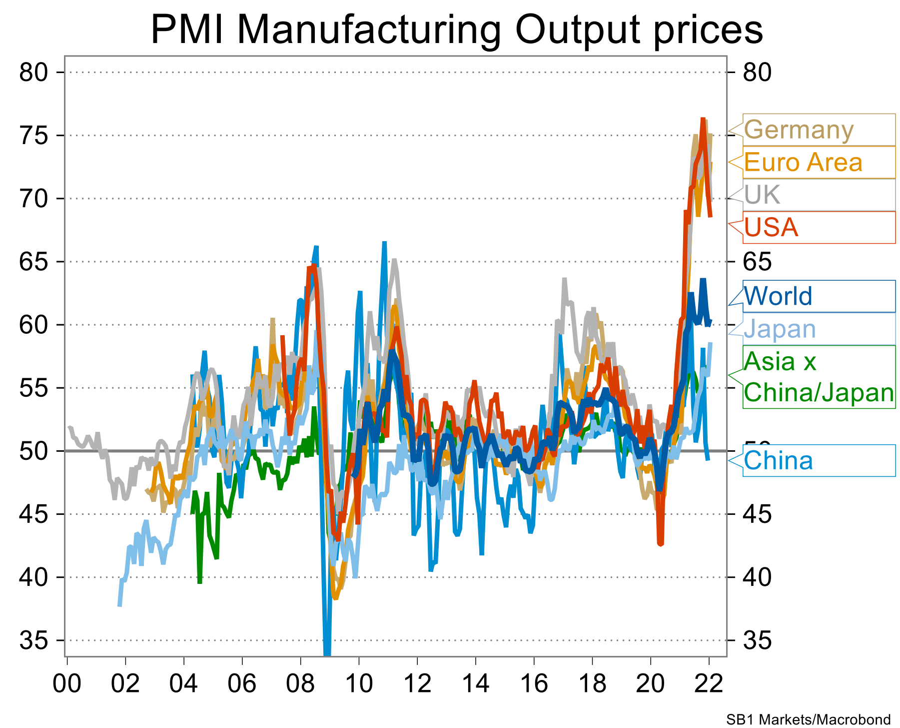
- Long delivery times have been a rich man's problem, while delivery times have not been that problematic in Emerging markets, China included

- **The global delivery times** PMI sub-index (changes in delivery times vs the previous month) inched down in both Nov, Dec and Jan, signalling some easing in congestion in the supply chains
- **The interpretation of this index is uncertain** – are companies really reporting changes in delivery times?
  - » This index as been above 50 most of the time (the past 20+ years), signalling longer delivery times. However, delivery times have not increased almost all the time – they have rather fallen! Companies may be reporting the level of delivery times. If so, delivery times are now contracting – while the index formally reports than delivery times are increasing at a marginally slower pace

Price indices have peaked – raw material prices have calmed down

However, companies are still reporting very rapid price growth in the rich part of the world

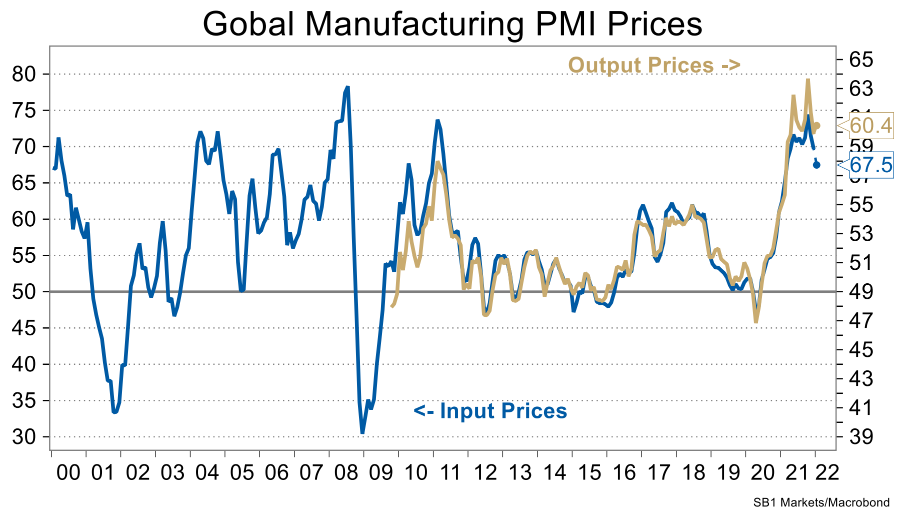


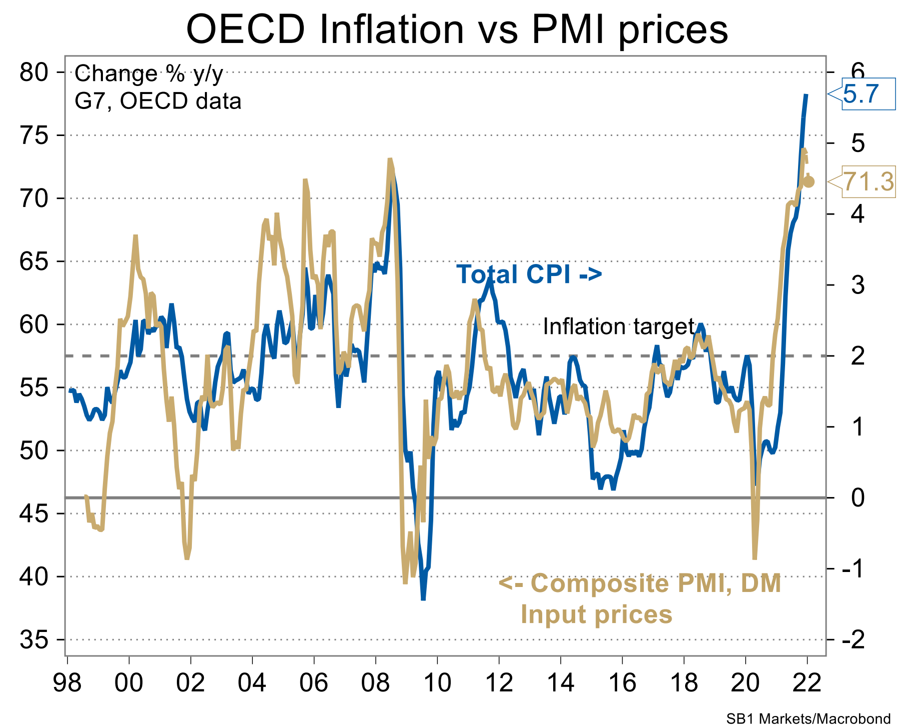


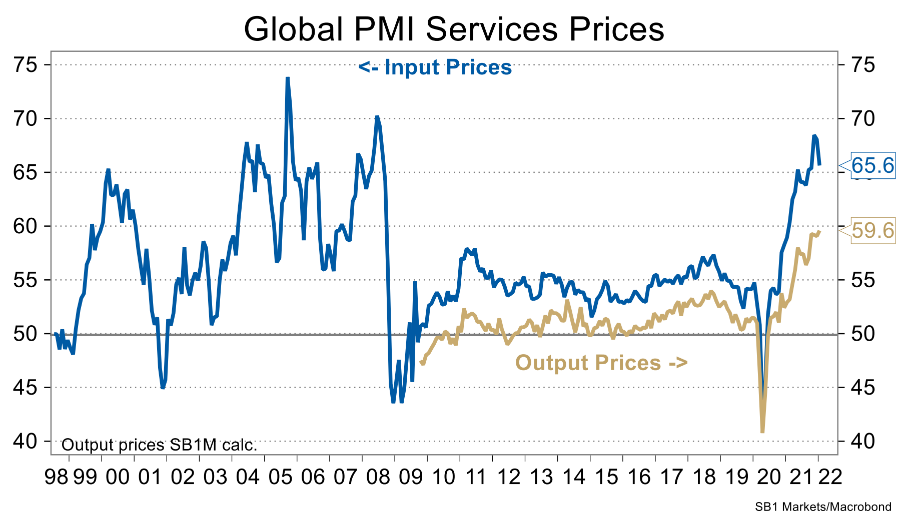
- Even so, some relief

Price indices have peaked, at least in manuf. – but they remain high

However, as soon as energy & other commodity prices stop rising, inflation will retreat rapidly





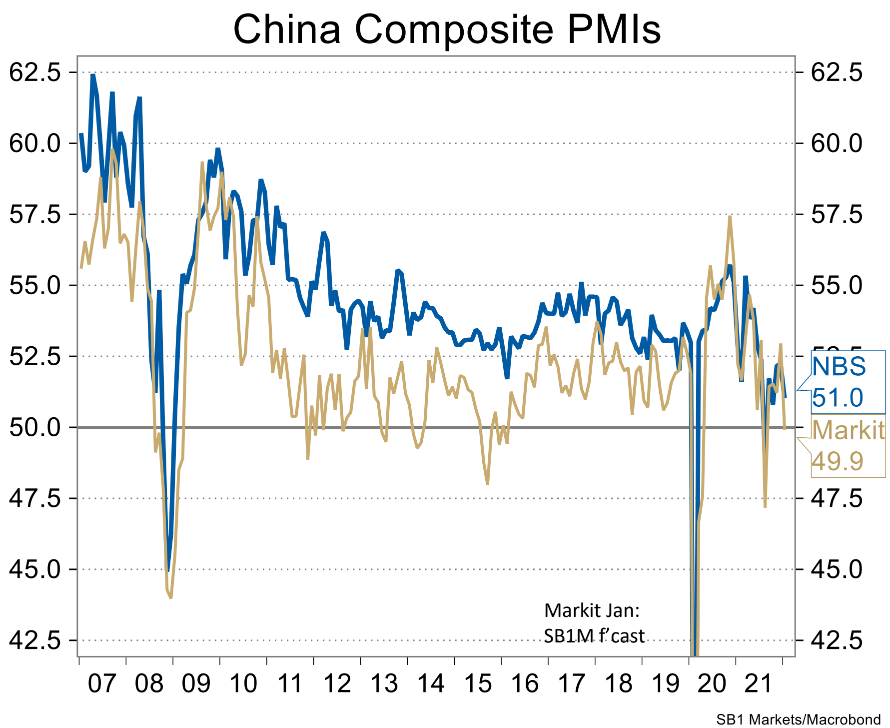


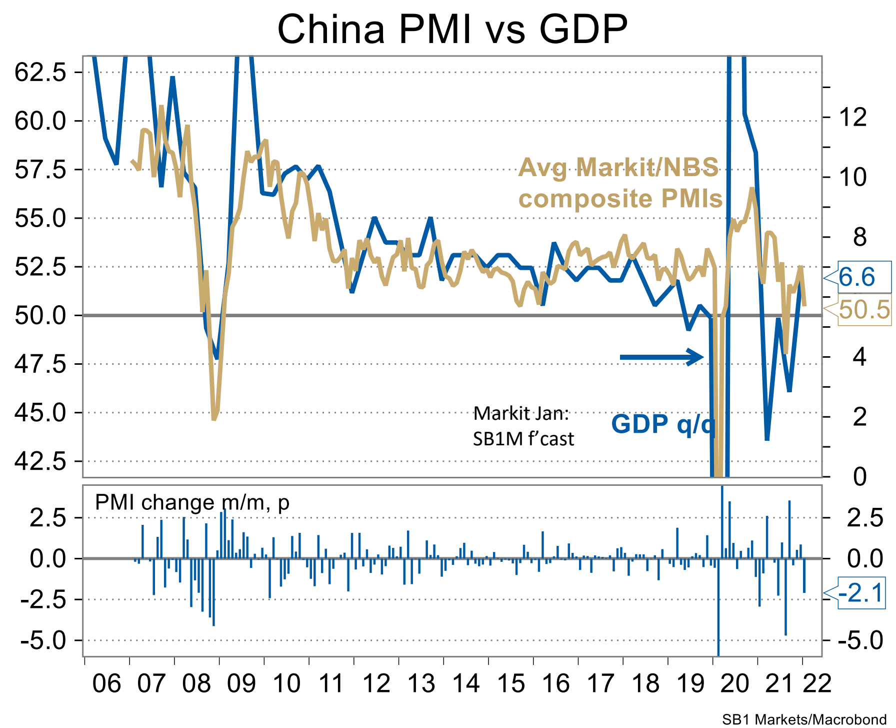
The last services PMI priced based on preliminary PMIs from EMU, Japan, UK, and the US

- In manufacturing, the price indices have clearly peaked
- Prices have not yet eased in the service sector, at least not output prices
- We are still much more concerned about wage inflation than the actual price inflation due to factors that most likely are transitory, like hikes in raw material prices, freight cost (which already may be yielding) or short lived margins expansion when demand is surprisingly strong

A sharp drop in January PMIs

Services in the CFLP/NBS survey and Markit's manufacturing PMI significantly down

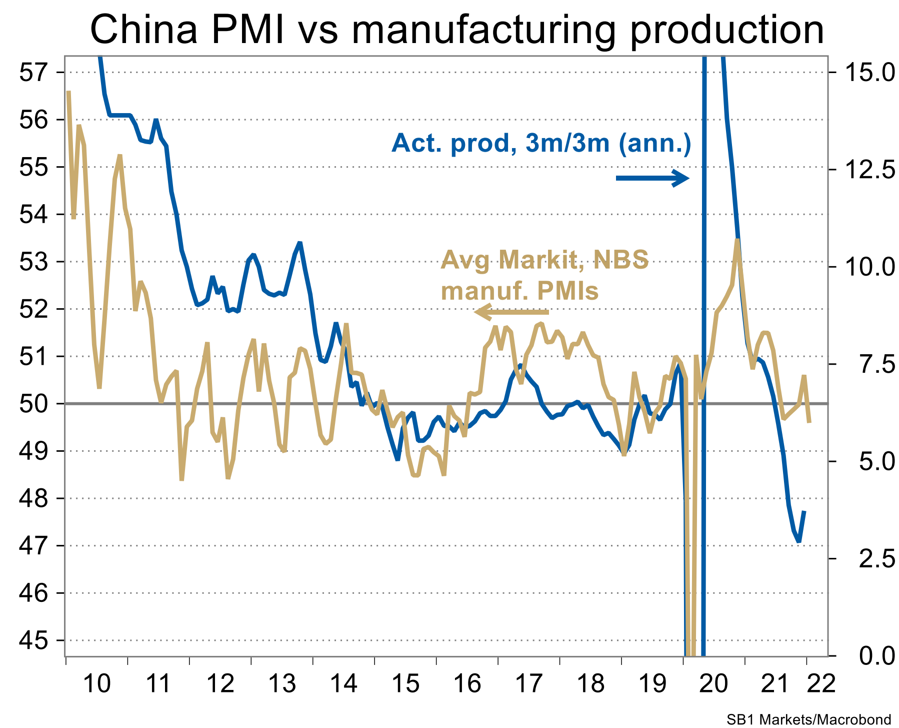




- The **NBS composite PMI** fell by 1.2 p in January, due to a 1.6 p decline in the service sector PMI (close to the expected 1.7 p drop) to 51.1 – very likely due to the impact of the fight against the Omicron variant. The manufacturing index was close to unch, and at tad better than expected
- **Markit's manufacturing total PMI** index fell 1.8 p to 49.1, and the output index fell by 4.3 p! The composite PMI probably fell by 3 p – as we assume even Markit's service sector PMI (not yet published) also contracted, like the service sector in the NBS index did
- **The average of the two PMI data sets** (given our Markit's service sector est) fell by 2 p, to 50.5, to well below and average level. <u>This level signals a growth rate clearly below trend into Q1</u>

Markit's manufact. PMI sharply down in Jan, the lowest since late '18 (x feb-20)

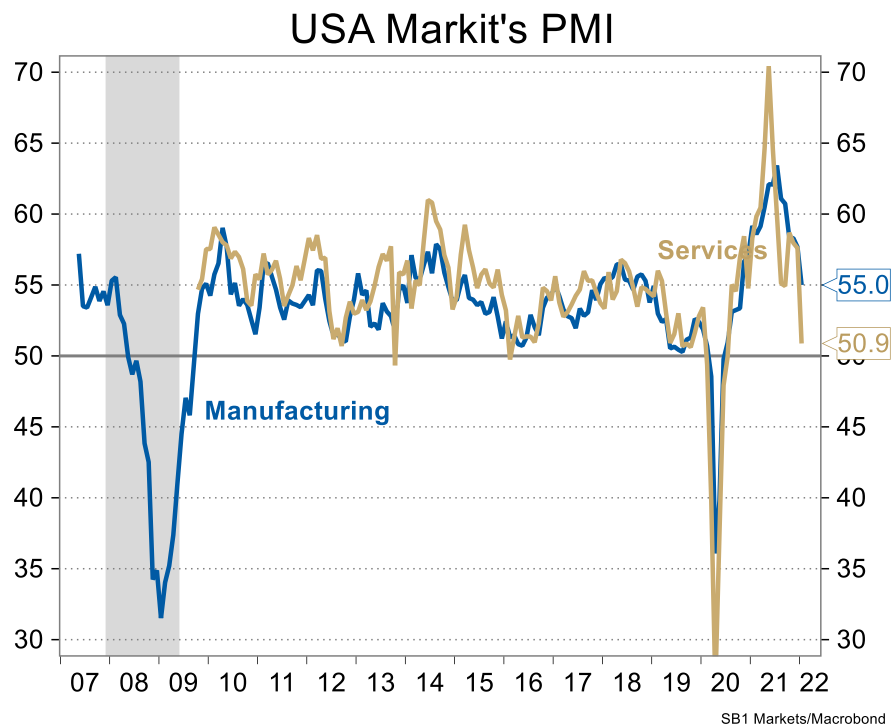
The average of the Markit's & NBS' surveys still not that weak

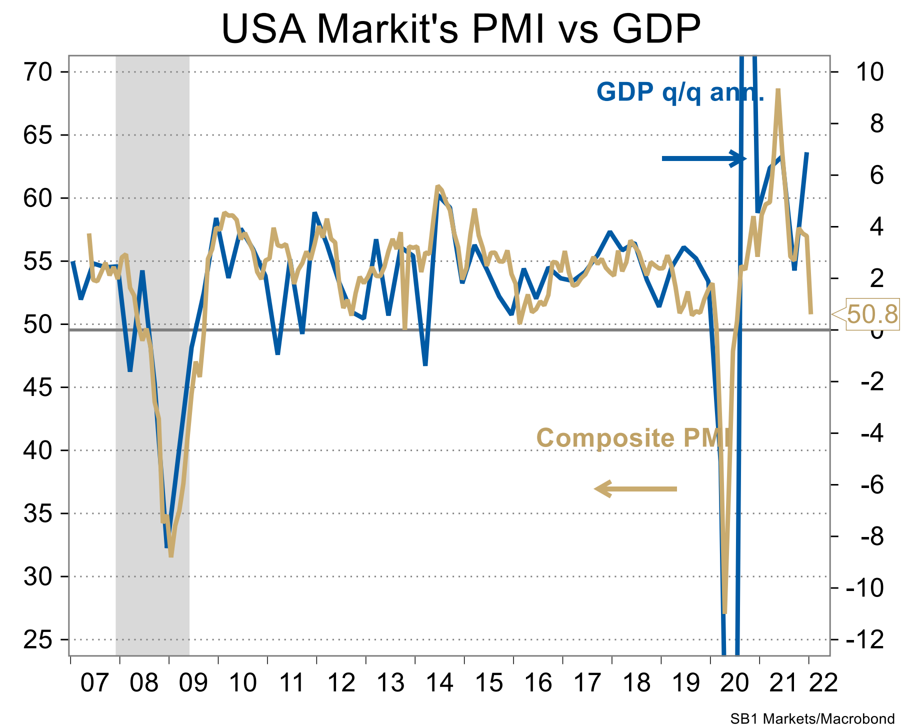


- The **NBS/CFLP PMI** declined 0.2 p to 50.1, while **Markit's PMI** fell 1.8 p to 49.1. The NBS survey is close to the average since 2012, while Markit's index is way below
- Growth in **actual industrial production** slowed in H1 last year (but gained some speed in Nov & Dec)

Oops, what happened in the US in January? Markit's PMIs straight down

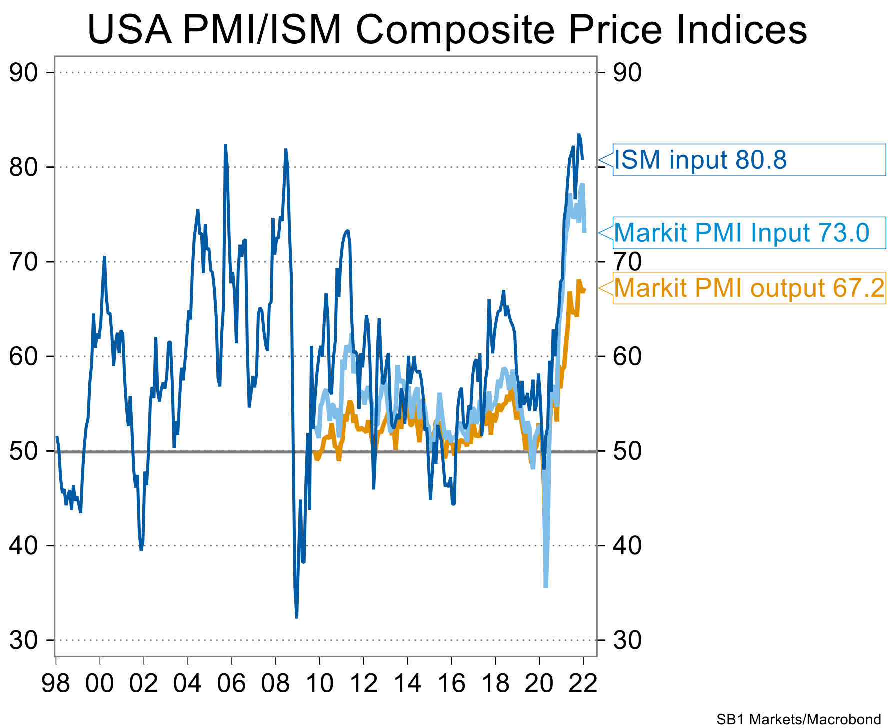
The composite index fell by 6.2 p to 50.8, expected 2 down. Close to zero growth??





- **The composite PMI** reported the 3rd largest decline ever (data from 2007) – and just a minor decline was expected
- **The service sector PMI** fell by 6.7 p to 50.9, expected down 2.2 p to 55.4. The print is well below an average level
- **The manufacturing sector** also hit something, the PMI fell by 2.7 p to 55.0, expected -1p to 56.8. Order inflow slowed, and did output growth, almost down to the 50 line
- Companies report a moderate growth in **employment. Prices** are still soaring but at a slower pace
- The **delivery times index** fell sharply – but delivery times are still increasing rapidly (or they are at least still unusually stretched)
- **What happened??** The decline in the service sector PMI could may be explained by virus challenges, but not the (continued) decline in the manufacturing index. Other manuf. Indices were mixed in Jan, but in sum down, *check to pages fwd*

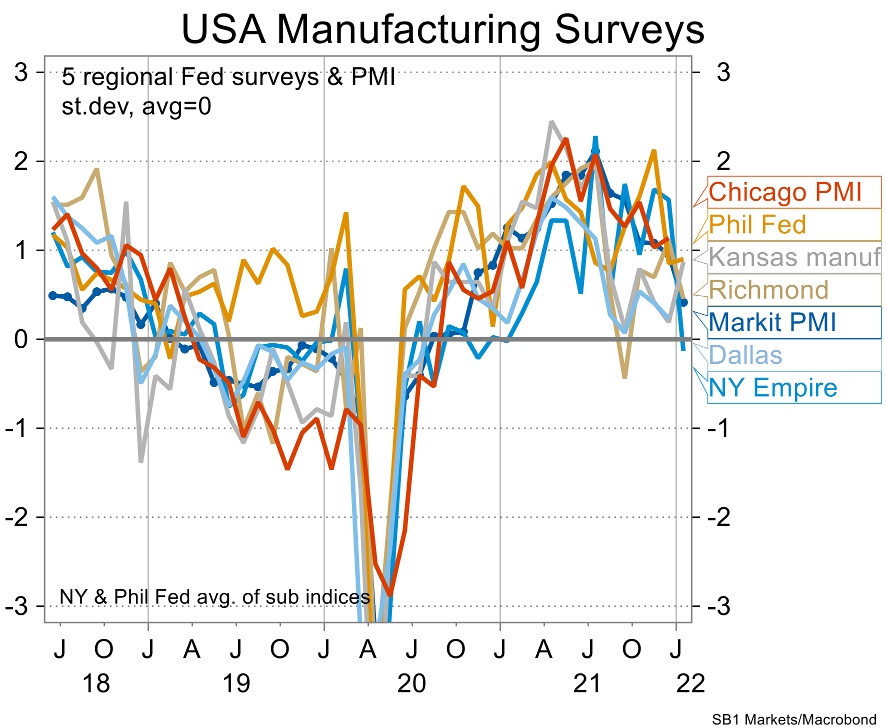
Peak price inflation? Very likely, some easing is seen in the prices indices

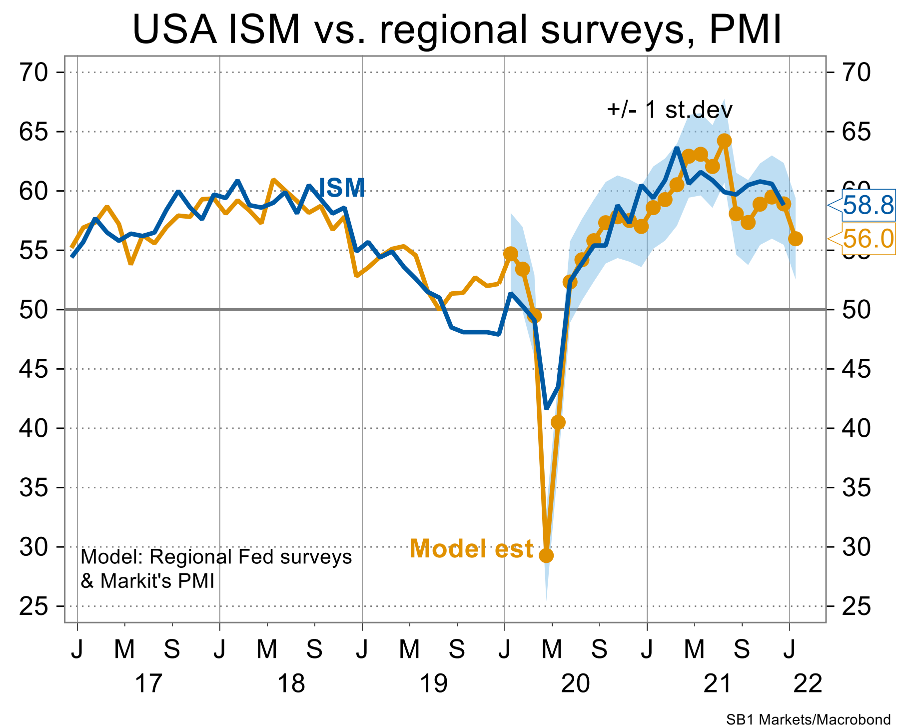


- ISM has not yet reported January data

3 out of 5 manufacturing surveys down in December, so far

Substantial decline NY Fed survey, as well as in the Richmond and Markit's PMI. ISM down 3 p to 56?





- Dallas Fed and Chicago PMI has not reported their manufacturing surveys yet

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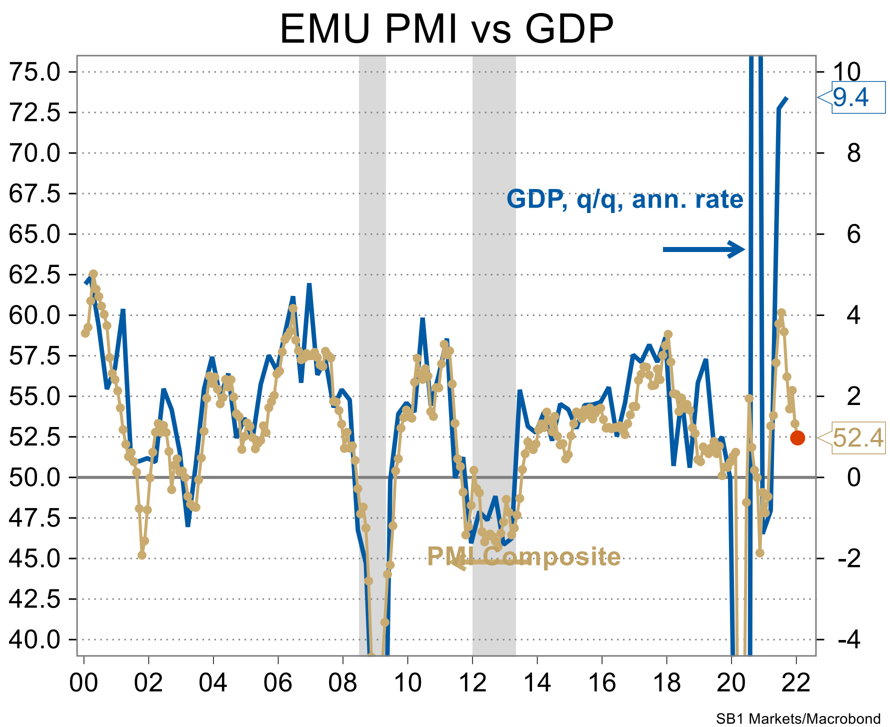
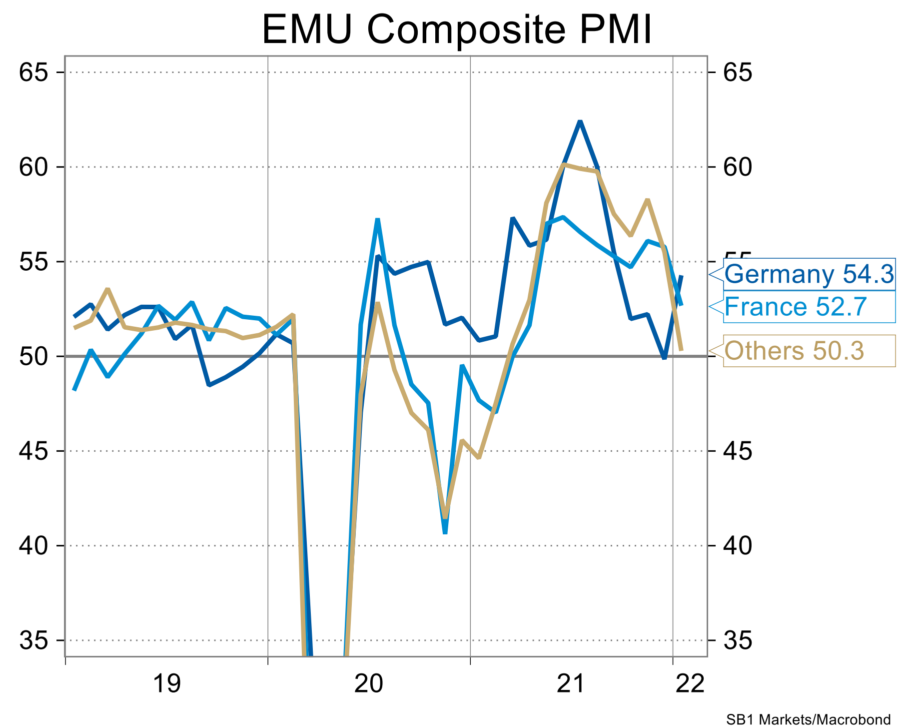
The composite PMI down 0.9 p to 52.4, signalling 1% GDP growth

Germany surprisingly recovered – and sharply. The others weaker than expected

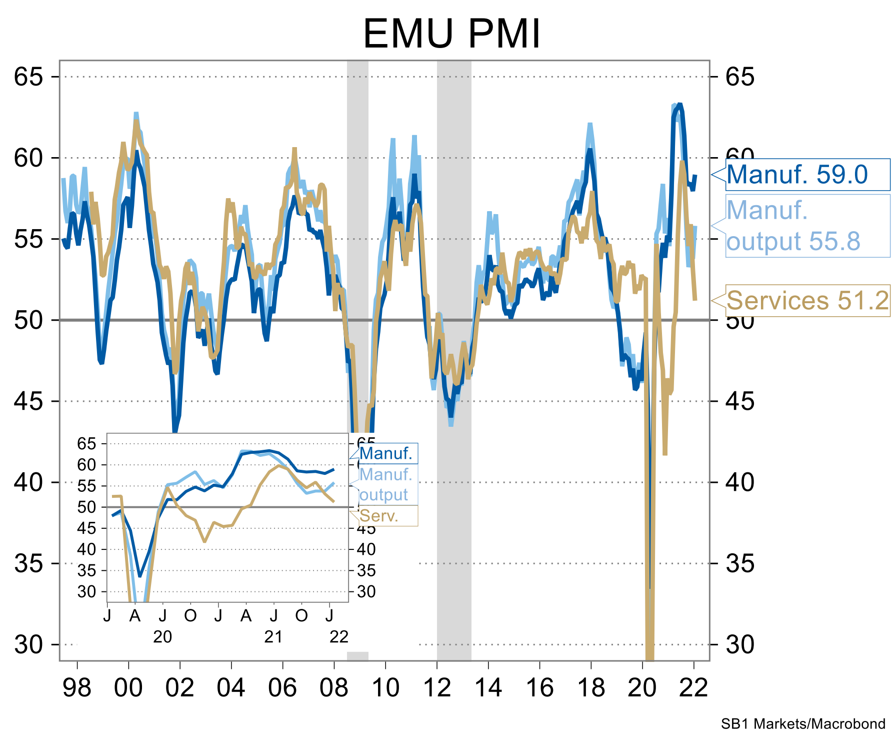




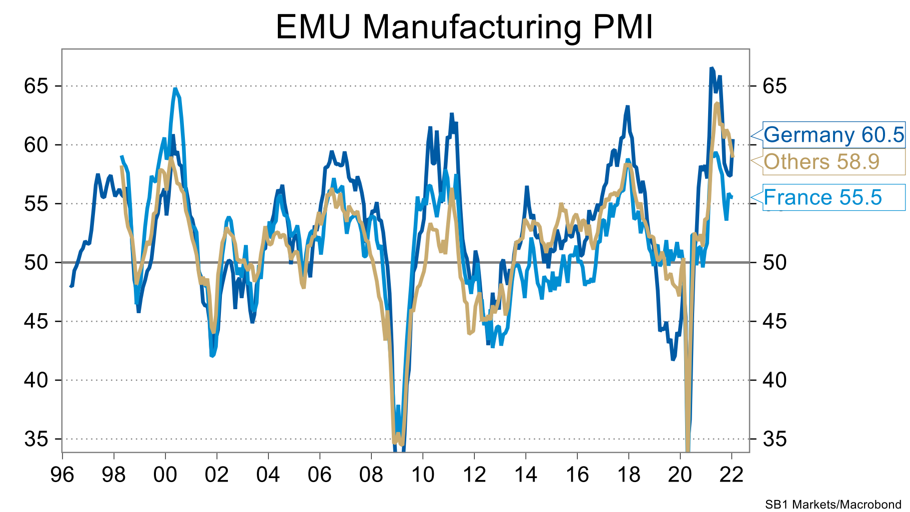
- More Covid measures (and individual changes in behaviour) probably contributed in both France as well as in (the implied average of) Italy and Spain
- The German PMI rose 4.4 p to 54.3 – while it was expected further down!
- The composite index fell in France and in the average of the rest of the union, the latter down to 50.3

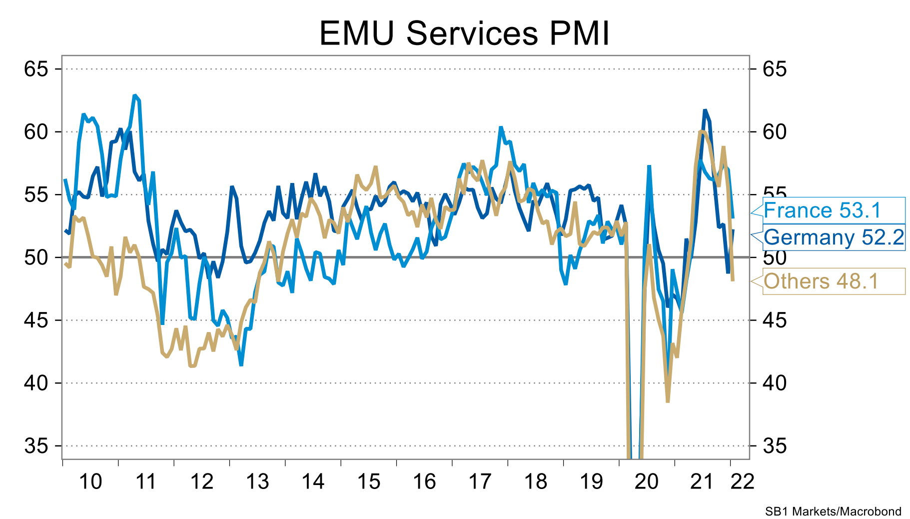
A surprising and strong German recovery but others as services took a hit there

The EMU region: Growth in manufacturing accelerated, but services very likely hit by the virus, again



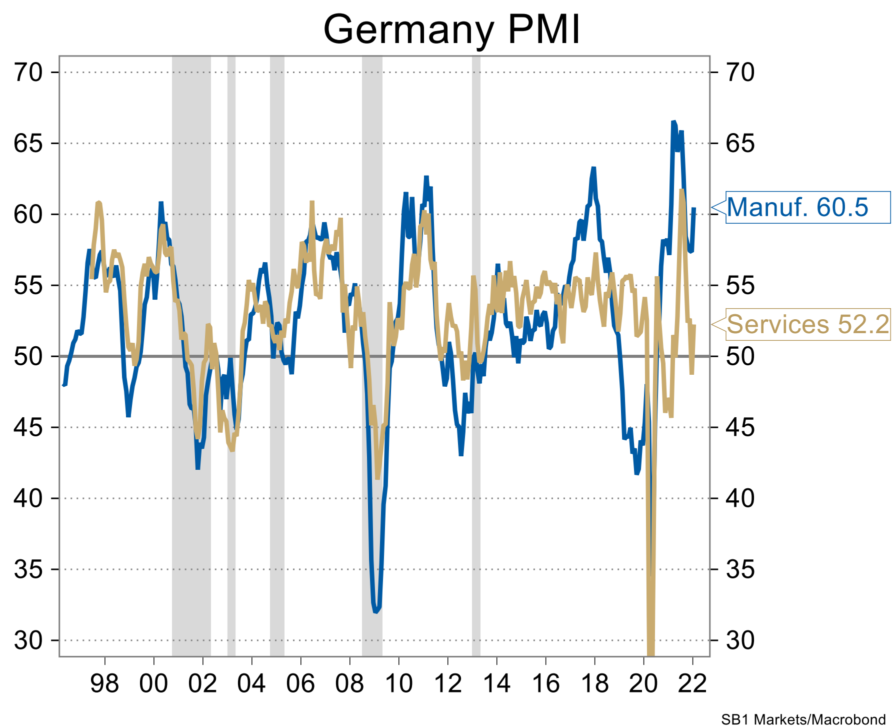
- The **service sector PMI** lost 1.9 p to 51.2, expected down to 52
- The **manufacturing PMI** added 1 p to 59.0, expected down to 57.5. The **output index** is not that strong, at 55.9 but the index climbed 2 p in January

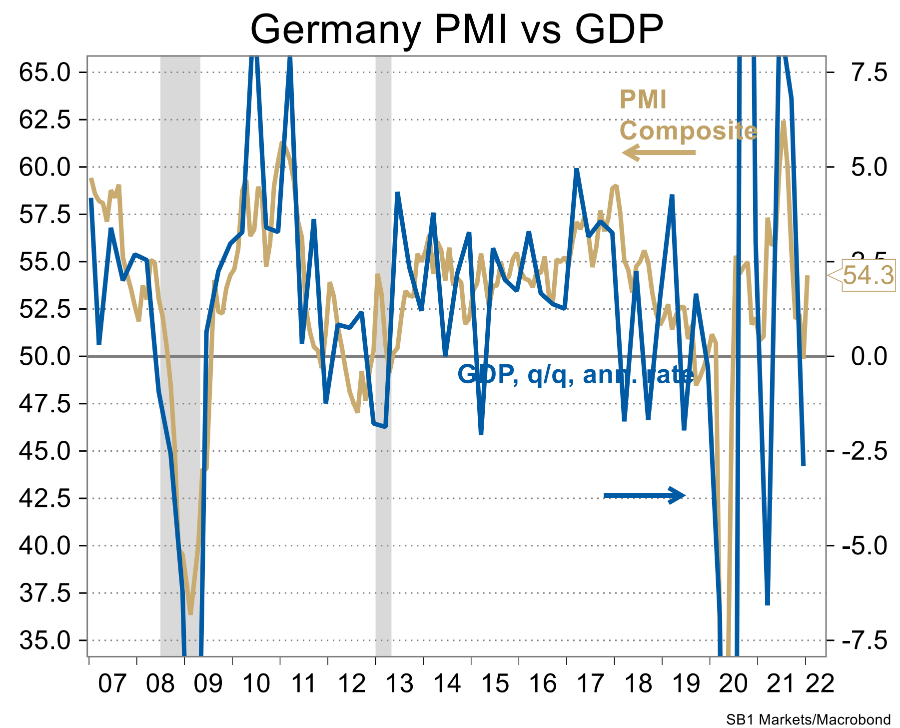




Germany: The composite PMI sharply UP – from a low level in December

Both manuf. and services PMIs turned upwards in Jan. The comp PMI + 4.4 p to 54.3 -> 2% growth

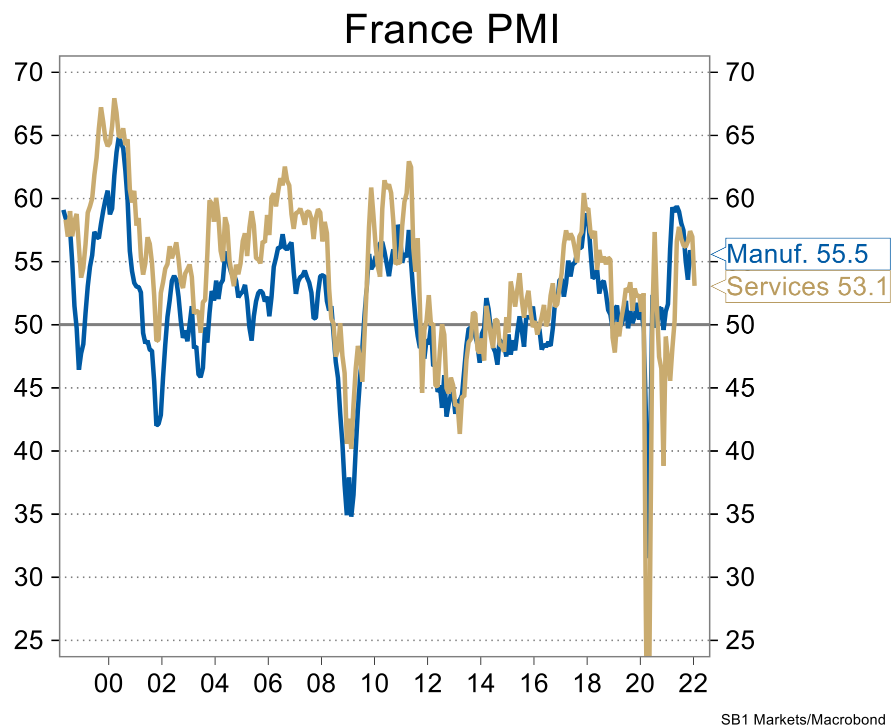


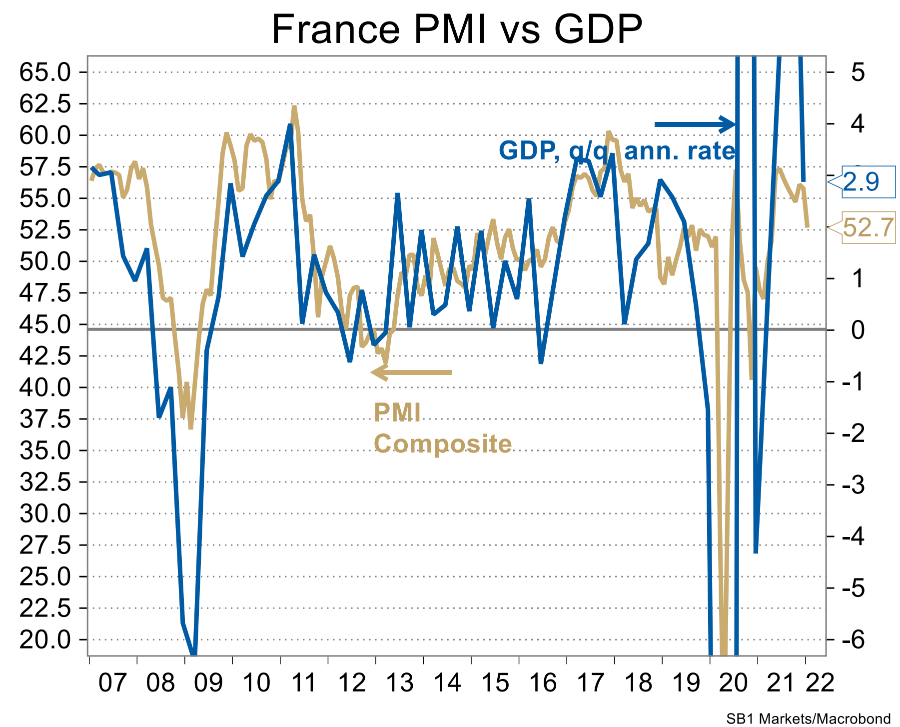


- **The composite PMI** surprised sharply at the upside, +4.4 to 54.3, expected down 0.5 p to 49.4!
- **The manufacturing PMI** added 3.1 p, to 60.5, a very high level. The output index rose even more
- **The service sector PMI** gained 3.5 p to 52.2, signalling some growth again. The virus has been on the retreat through January, and restriction eased. Still, this survey was expected further down in in January

France: Services sharply down, growth still signalled

Manufacturers are not complaining. The composite index down 3.1 to 52.7, -> 2% GDP grwt





- The **composite index** fell 3.1 p to 52.7, signalling 2% growth (from 2¾), still somewhat above trend. The index was expected 1.1 p down to 54.7
- The **services PMI** fell 3.9 p to 53.1, expected down to 55.3 – no doubt due to Omicron troubles
- The **manufacturing PMI** was down 0.1 p to 55.5, 0.2 pp better than expected. The level is far above average

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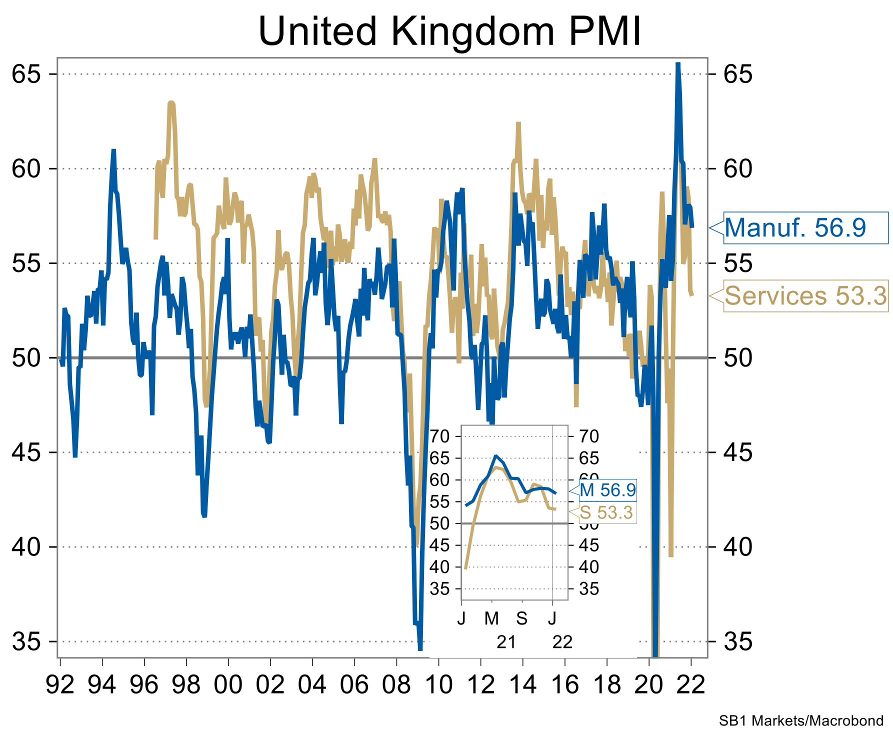
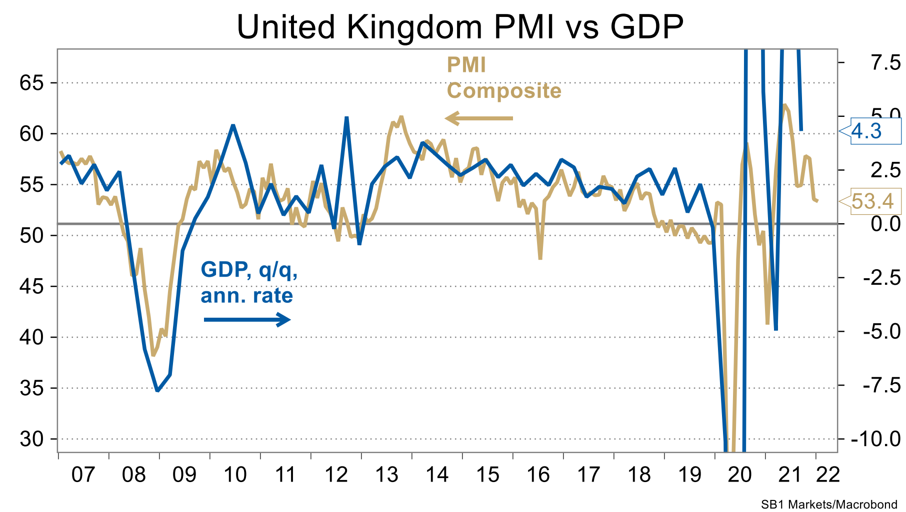
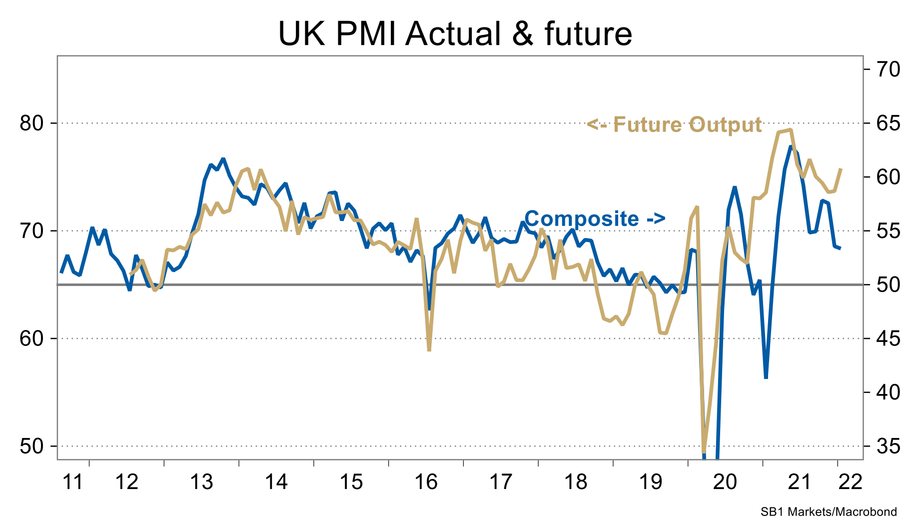
The PMIs stabilised in January, moderate growth signalled

Even services are reporting growth – before all Covid restrictions were lifted

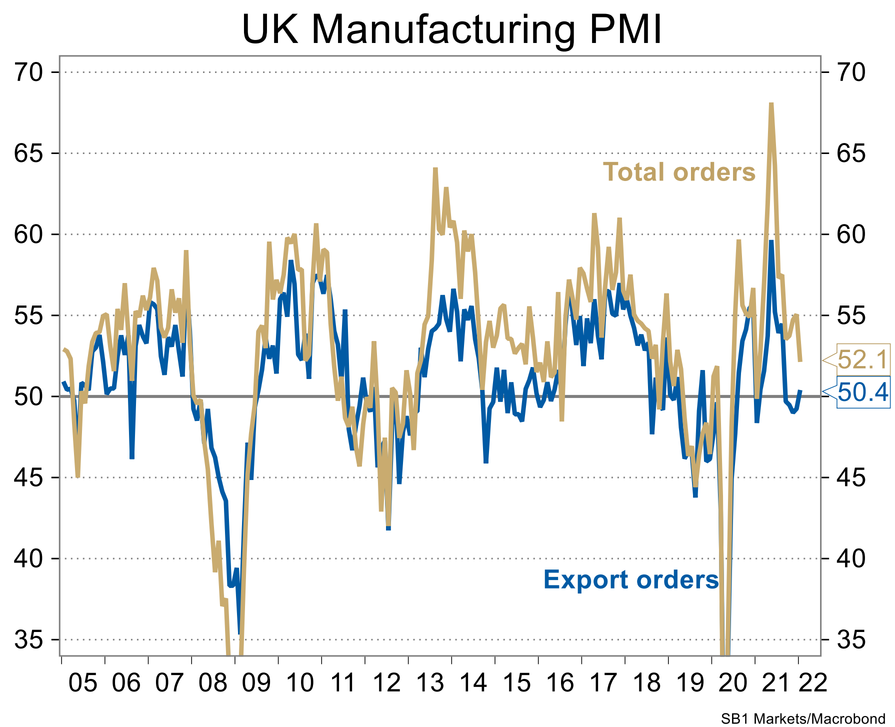


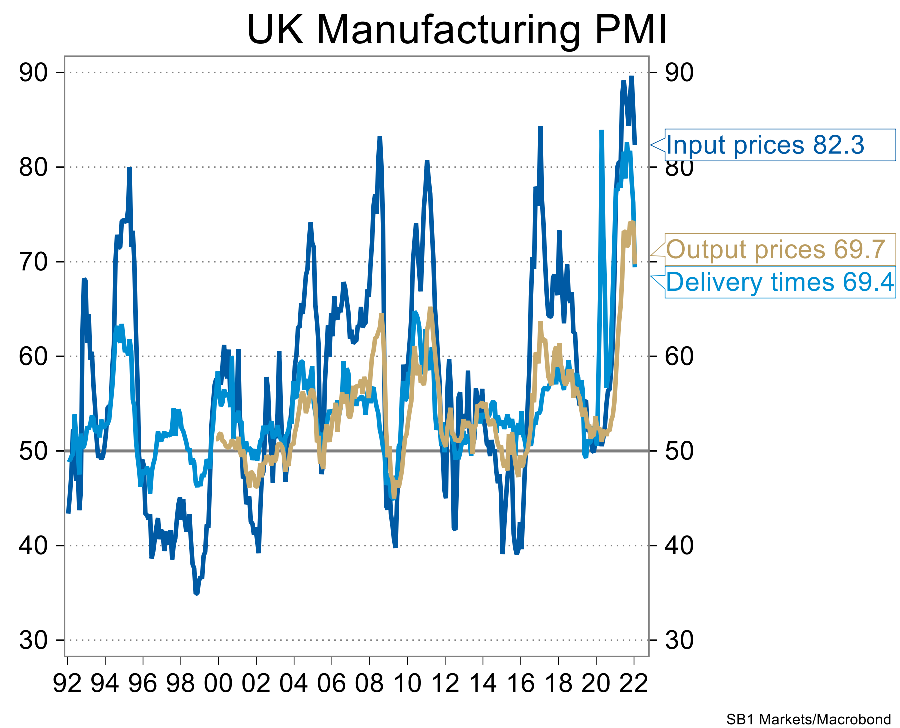




- **The composite PMI** declined by 0.2p to 53.4 in Jan, with just small changes in both manufacturing and services. In Dec, the index fell by 4 p and corona restrictions were imposed. In Jan, the index was expected up to 54
- **Services PMI** fell marginally to 53.3
- **The total manuf. PMI** was down 1 p to 56.9 , as expected (but the output component, included in the composite index, gained 0.6 p to 53.3)
- The delivery times index, as well as the price indices declined further – but they all remain at elevated levels (see next page)

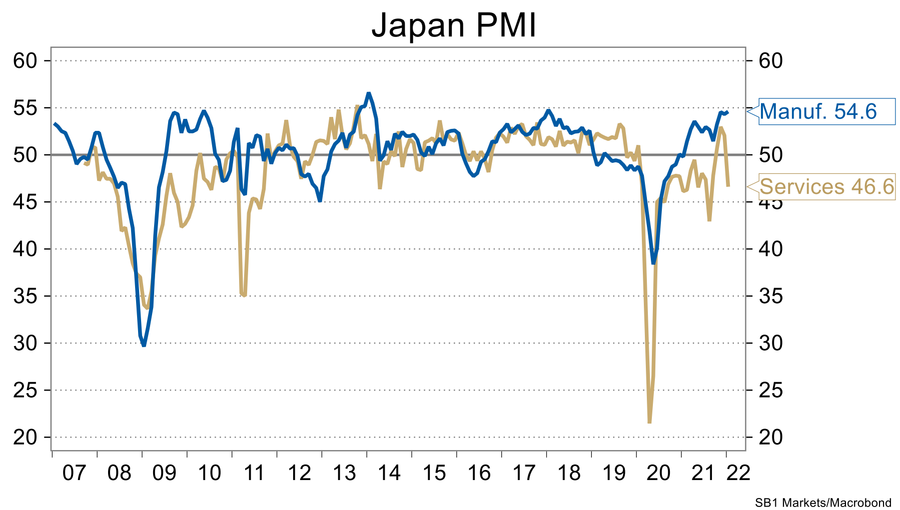
Order growth is slowing, as are delivery times & price increases

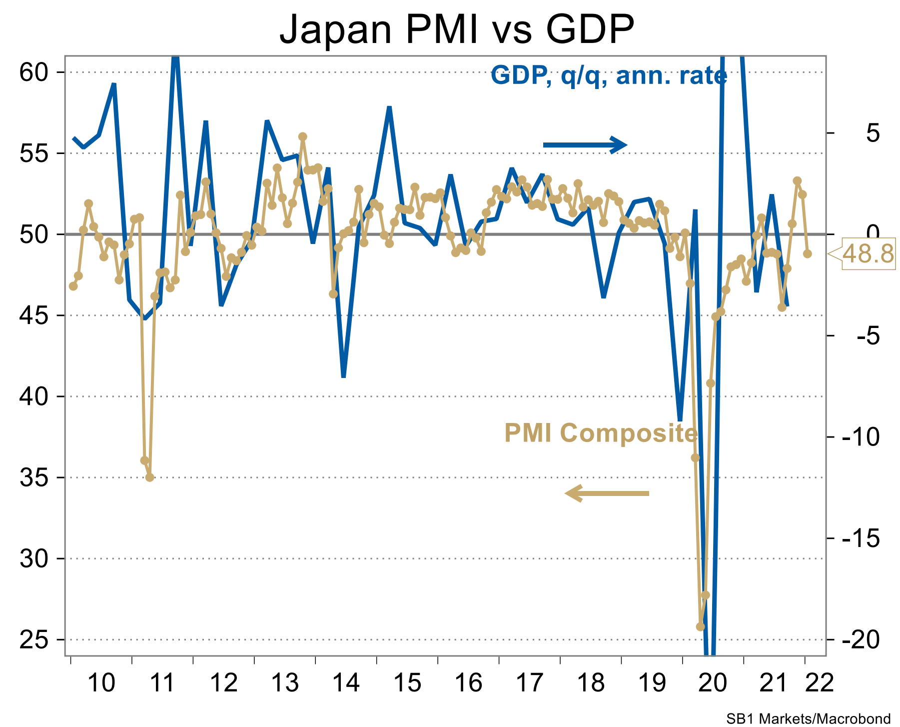


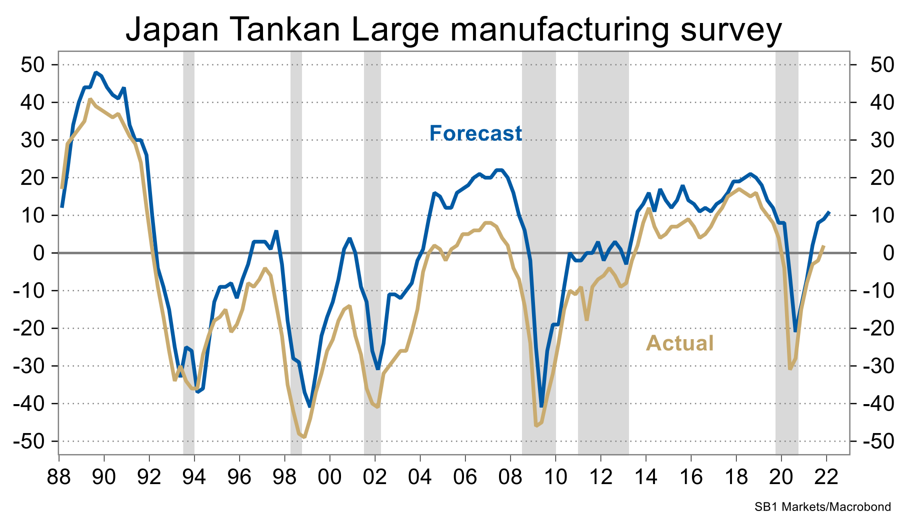


Services further down in Jan, blame the Omicron. Manuf. reports strong growth

The composite PMI fell by 3.6 p to 48.8, normally yielding a 1% GDP decline

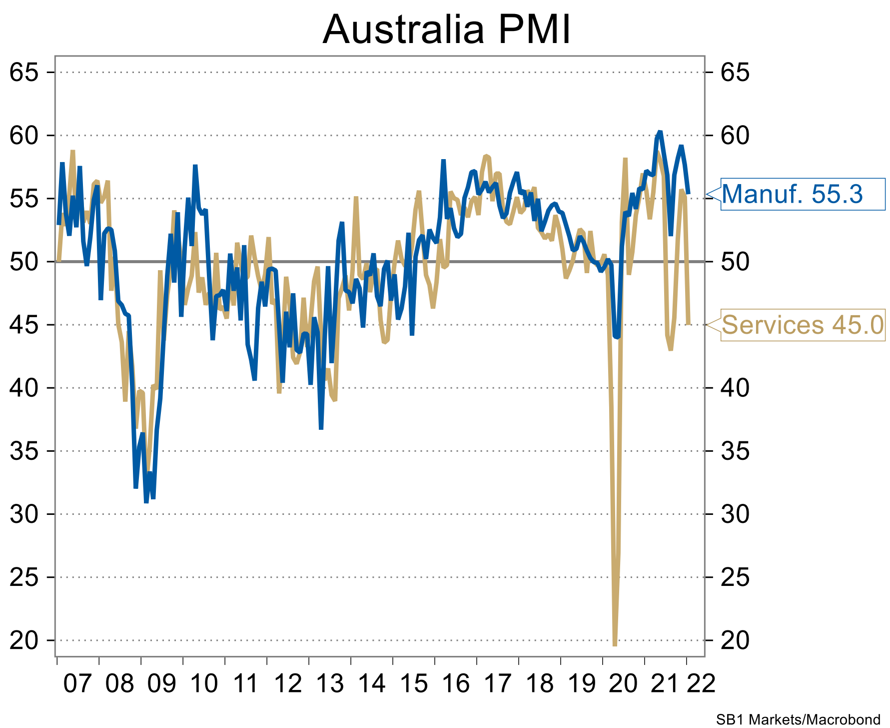


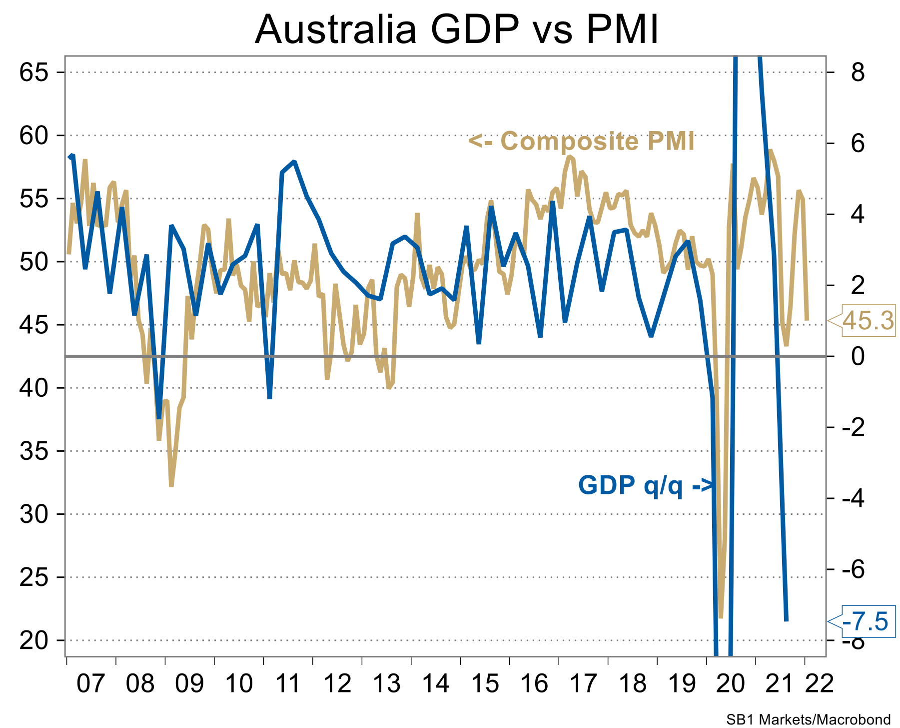




Australia reports an abrupt January slowdown, mostly in the service sector

Service down 10 p to -45.0, the composite down 9.5 p to 45.3, signaling close to zero growth

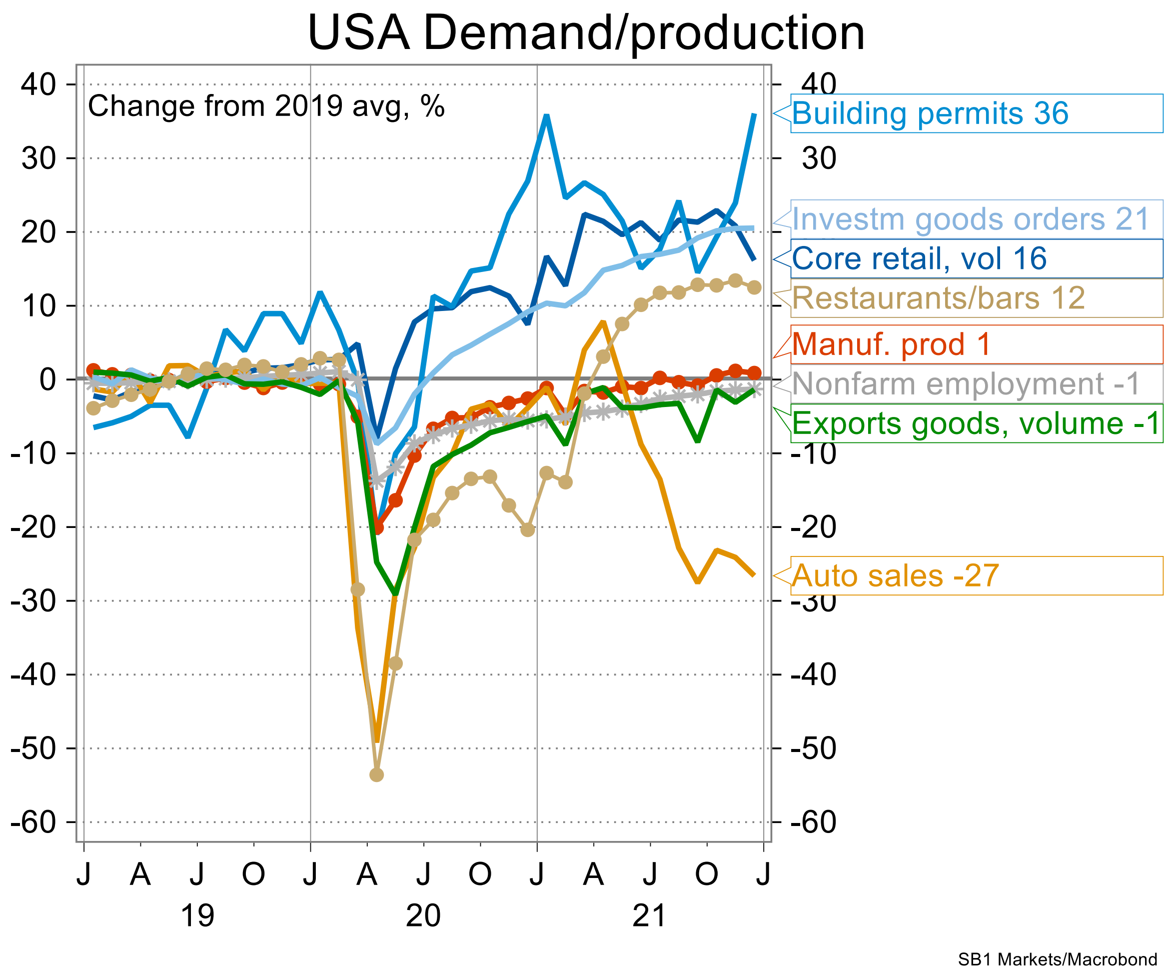




- The decline in **services** is no doubt due to the new restrictions imposed in order to contain the Omicron virus
- The **manufacturing PMI** fell too, but 'just' but 2.3 p,m and the level is still strong at 55.3
- **In Q3, GDP fell by** 1.9 (7.5% annualised) setback during the lockdown 3rd quarter

Big picture: Growth is slowing as the economy as 'normalised'

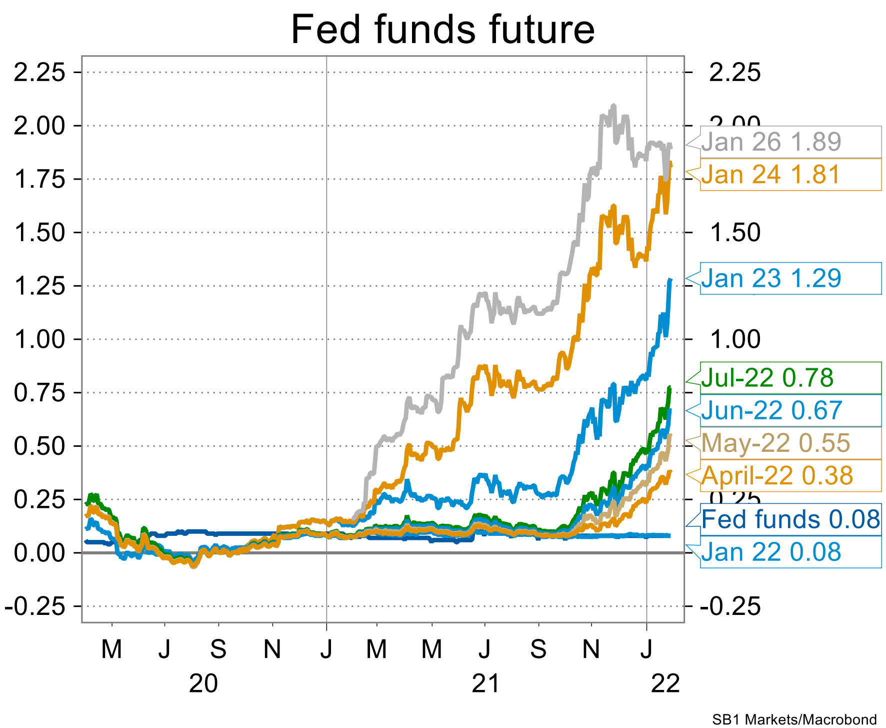
The upside now: Auto production & exports



- Retail sales have peaked, but is still at a high level (and Dec was likely artificially weak)
- Restaurants have recovered, at least nominally (prices are sharply up)
- Home building has flattened, mostly due to supply constraints, demand is still strong
- Manufacturing production is 'too weak' but supply constraints, exports have kept production in check
  - » Auto sales and production are way below normal levels

Fed: The huge policy shift confirmed. A rapid tightening can not be ruled out

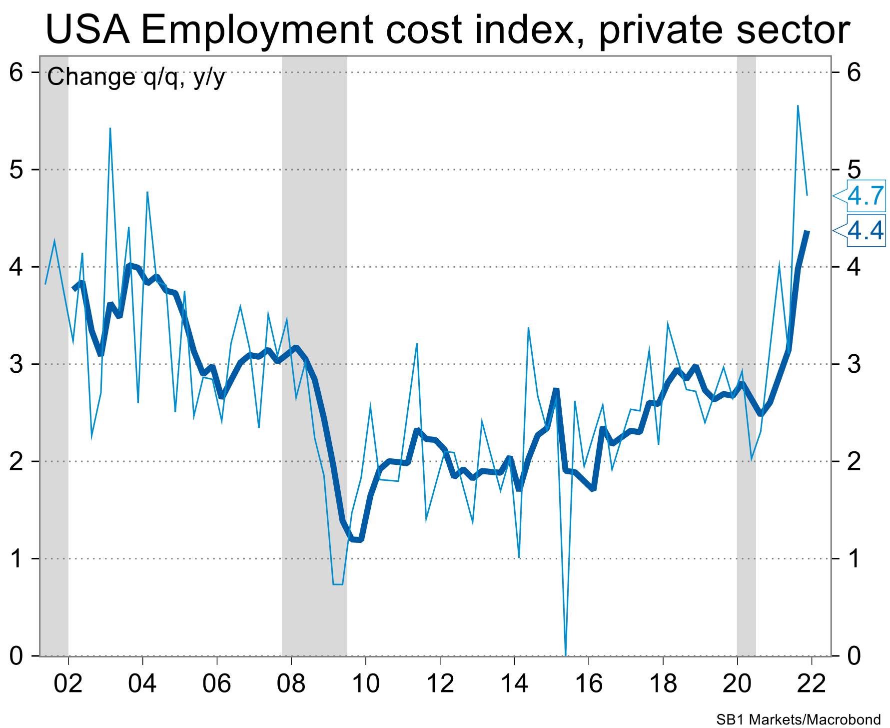
We suspected that Powell as usual would be soft at the press conference but this time de was not

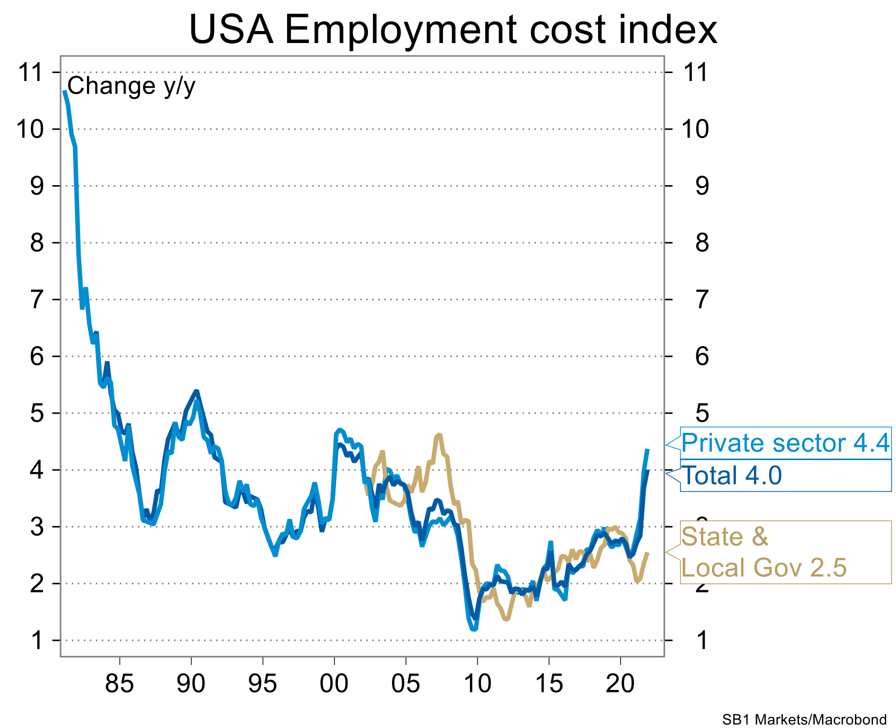


- **The press release from the FOMC meeting was 'neutral', and the market did not respond to the message which confirmed that a March hike was almost granted**
- **However, at the press conference Powell revealed a new side of himself, clearly stressing the uncertainty on the upside for inflation, as for the need for monetary tightening. Rate rose sharply all over the curve**
- Like in the minutes form the previous meeting, Powell commented that current situation is not comparable to 2015, when the last tightening campaign started; Inflation is much higher, the labour marked tighter and the economy much stronger. Thereby, he is signalling willingness to hike rates rather rapidly. He stressed that the FOMC is ready to do what is needed. He would not rule out that rates could be hiked more than 25 bps , or that rates could be adjusted at the 'mid' meetings
- The timing of a moderate **reduction of the bank's holdings of bonds** had not been discussed (at least not in detail) but a QT could start after the first hike in signal rate (by not reinvesting all proceeds from the current stock).
- For the record: The FOMC left the **target rate** unchanged at 0-0.25%, and confirmed the December decision that the **bond buying (QE)** program would be terminated by March
- **Market reactions:** Interest rates rose by up to 20 bps in the short end of the curve during Wednesday and Thursday (after a decline ahead of the meeting). The market now assumes that 5 or more hikes in 2022 is more likely than 4 or less! Stock wobbled, but ended the week marginally up

Employment cost are climbing fast in the private sector

Employment costs rose at 4.7% pace in the private sector in Q4, annual growth up to 4.4¤

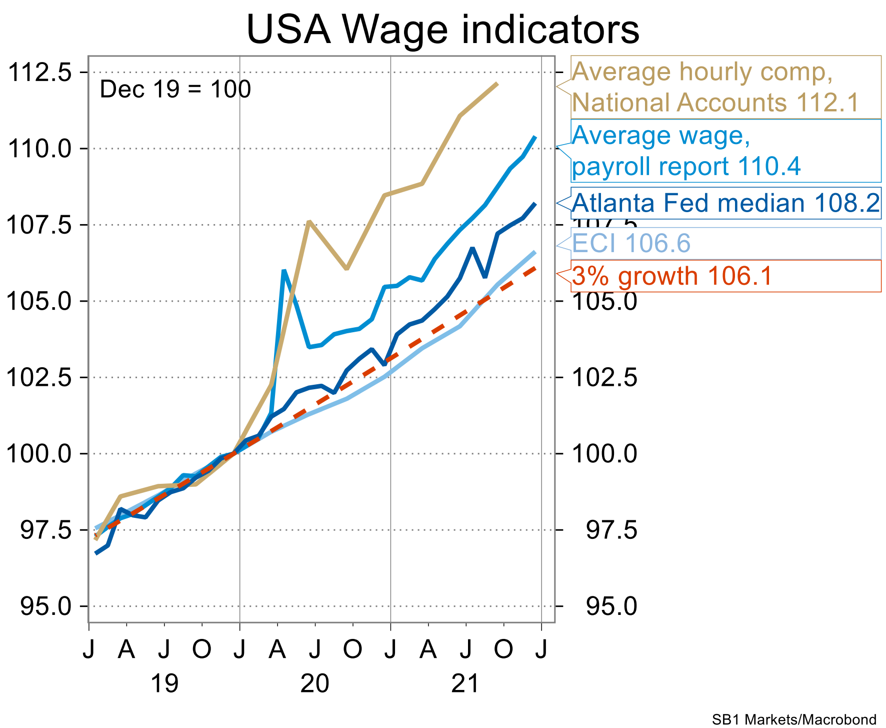


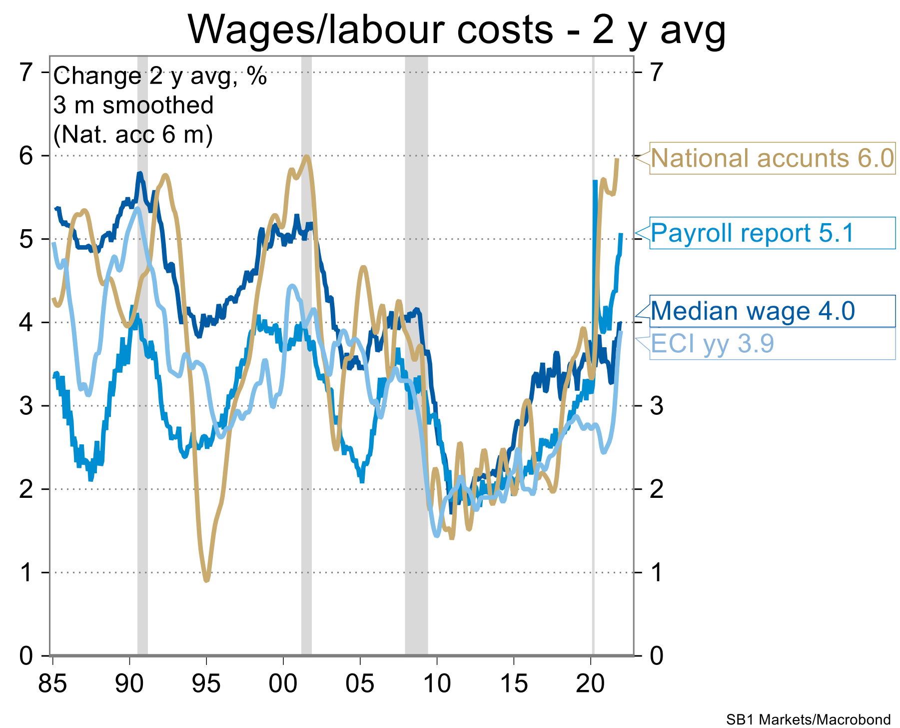


- The **Employment cost index for all civilian workers**, which measures wages and other wage costs for the same types of jobs (and is not influenced by changes in employment between sectors/type jobs), rose by 1.0% q/q in Q4, 0.2 pp less than expected, or at a 4% annualised pace. The annual rate accelerated to 4.0% from 3.7%, the highest since 2001
  - » In the private sector, the ECI rose by 1.2% q/q (4.7% annualised), and it is up 4.4% y/y
    - ▪ Wages & salaries in the private sector is up 5.0% y/y, highest since 1985. Benefits are up 'just' 3.0% (and the sum 4.4%)
  - » State and local gov employment costs are up just 2.5% y/y, the largest discrepancy to the private sector ever
  - » In general, low paid services reported the highest wage growth, both q/q & y/y
- **All other wage indicators have reported higher wage growth for a while**

Now all wage indicators are reporting higher wage inflation

… and substantially higher than during the previous 10 years that has yielded 2% inflation (or more)

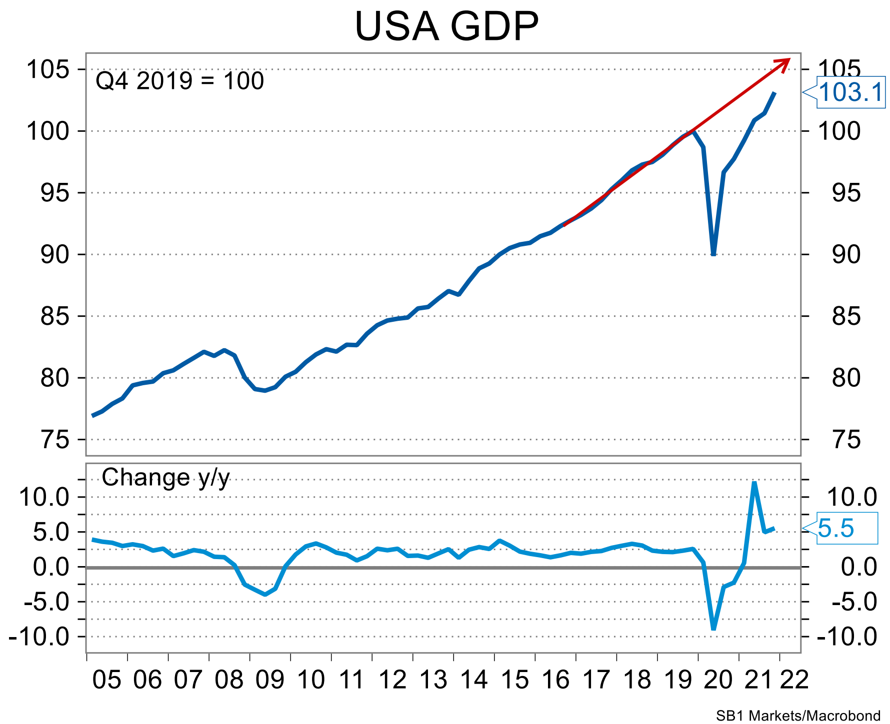


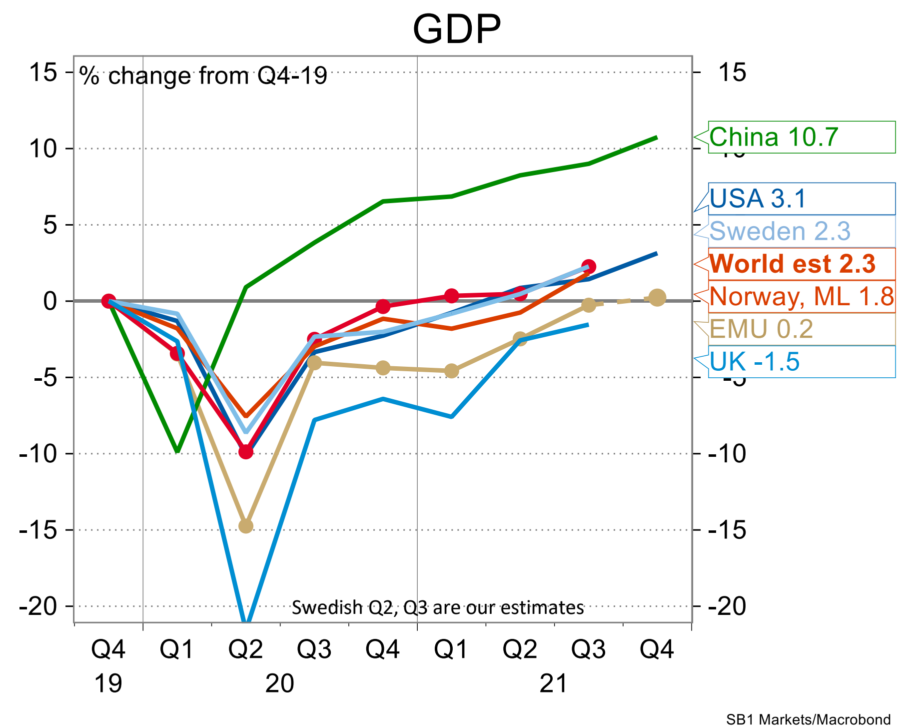


- **All wage indicators** are reporting faster wage growth, and all reporting wage growth well above the average recent years, also if we apply a 2-year average growth rate, to exclude the impact of changes in the first part of the pandemic (chart to the right)
- Growth in wage/earnings/compensation indicators are up 1.5 – 3.5 pp vs the their respective 10 y averagea. There is an obvious risk that wage inflation will accelerate further (check next page) – probably until the next recession hits as the labour market is extremely tight
- Over the past 10 years, inflation has been close to 2%, and well above 2% if calculated over a shorter period
- It will be a challenge to keep inflation at 2% if wage inflation remains at 4% or above. However, profit margins will probably decline substantially from the present very high level, and productivity growth has accelerated somewhat, leaving room for a slightly higher wage inflation than over the past 10 years without creating higher price inflation

GDP grew at a 6.9% pace in Q4, and is not that far below the pre-p trend path

Domestic demand was not that impressive as inventories 'explained' 5 pp of the 6.9%

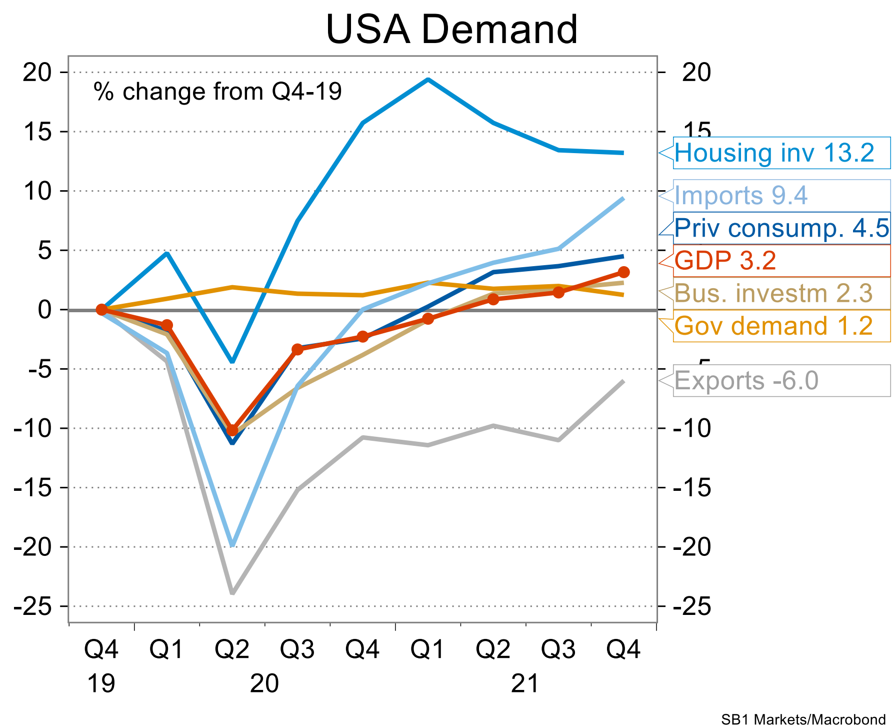


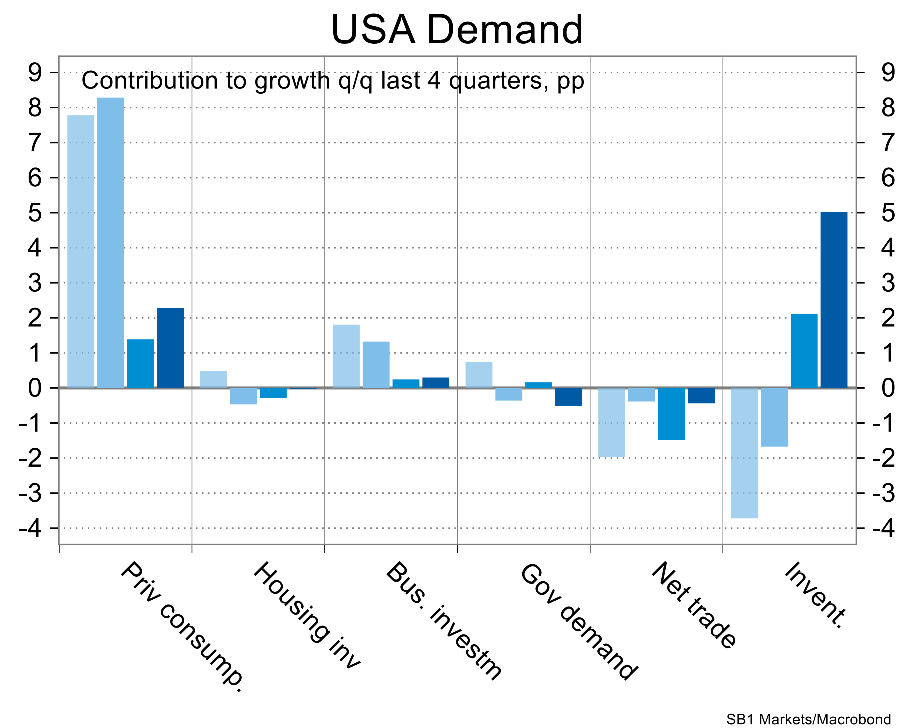


- **GDP** grew by 6.9% annualised in Q3 (1.7% not annualised),up from 2.3% in Q3, and well above expectations at 5.5%. The GDP level is 3.1% above the Q4-19 level – but still 1.7% below the pre-pandemic (2.4%) growth path, as services still operate below a normal level
  - » GDP grew by 5.5% y/y in Q4, and by 5.6% in 2021 vs. 2020, following the 3.4% decline in 2020
- **Private consumption** grew 3.3% in Q4, housing investments fell 0.8%, business investments added just 2%, t tad more than in Q3, and only driven by IP investments – construction investments fell sharply for the 2nd quarter in row, now by 11.4%. Government spending was cut by 2.9%
- **Domestic demand** rose no more than 1.9%. Exports rose 24%, from a low level – and imports rose 18%. However, imports as are far larger than exports, the contribution from net trade was negative, by -0.4 pp! So why did GDP grow by 6.9%? Because **inventories** rose big time, and added 5 pp to growth – that is, out of the 6.9%! Inventories contributed by 2.1% in Q3, following a huge inventory rundown in Q1 and Q2
- Big picture: The economy is still not fully back on track but growth is decent. The inventory cycle is still not worrisome

Inventories were the Q4 story but final demand is OK too

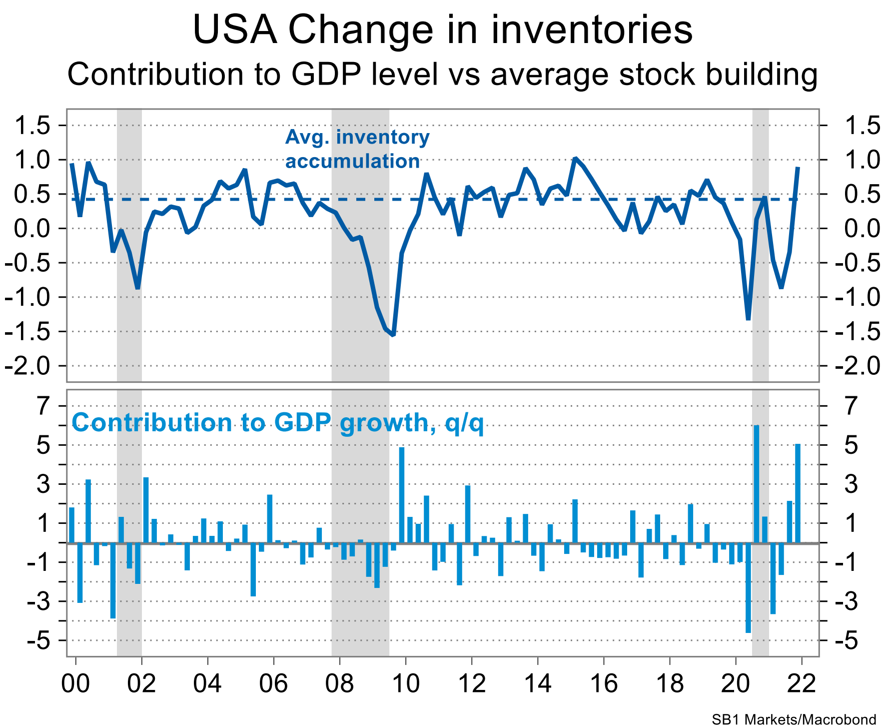
However, business investments are growing just slowly, and housing investment fell further





A large inventory contribution but growth in inventories still not that high

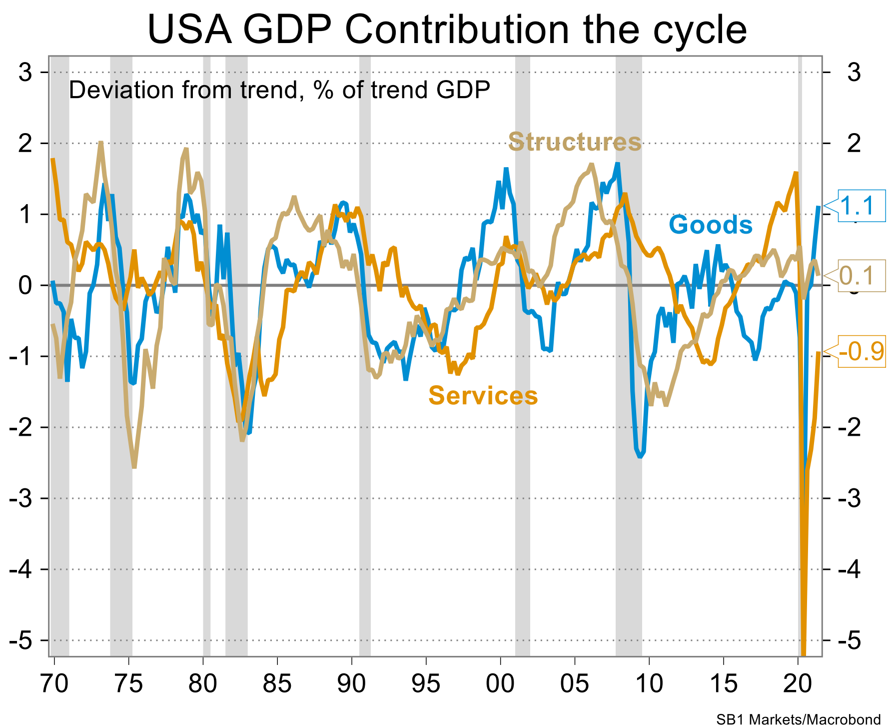
Especially following the run down of inventories during the pandemic

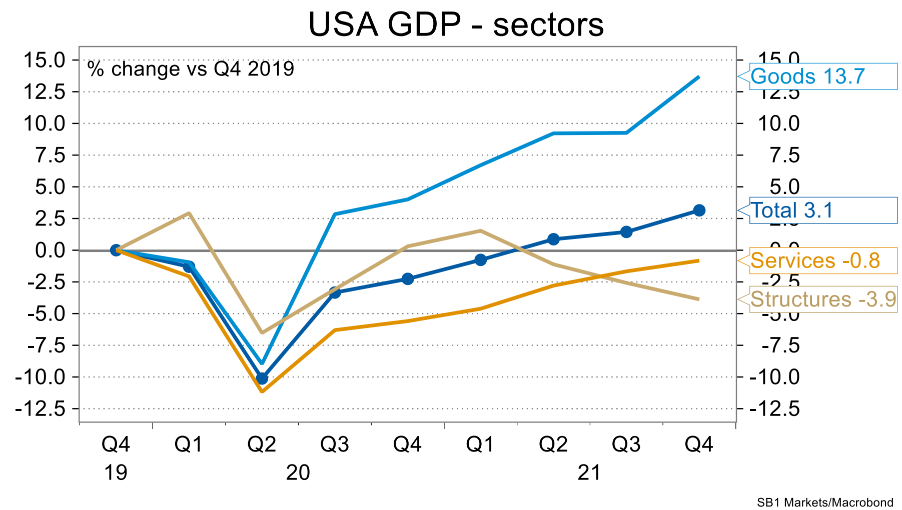


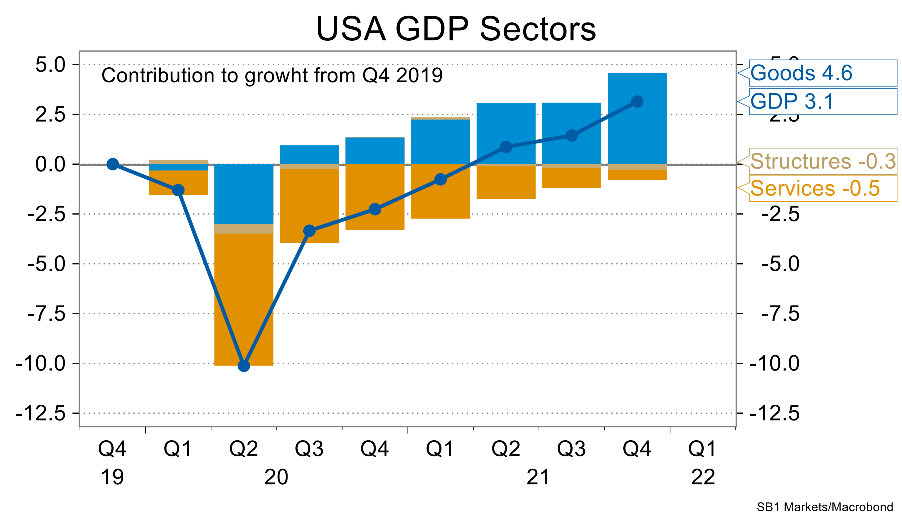
- However, inventories can not continue to grow at the same pace as during Q4 – then inventories will become too large over time

Services are recovering but are still a substantial drag on activity

A further recovery in Q4 but services are still down 0.8% vs. Q4 19. Goods are 14% above!



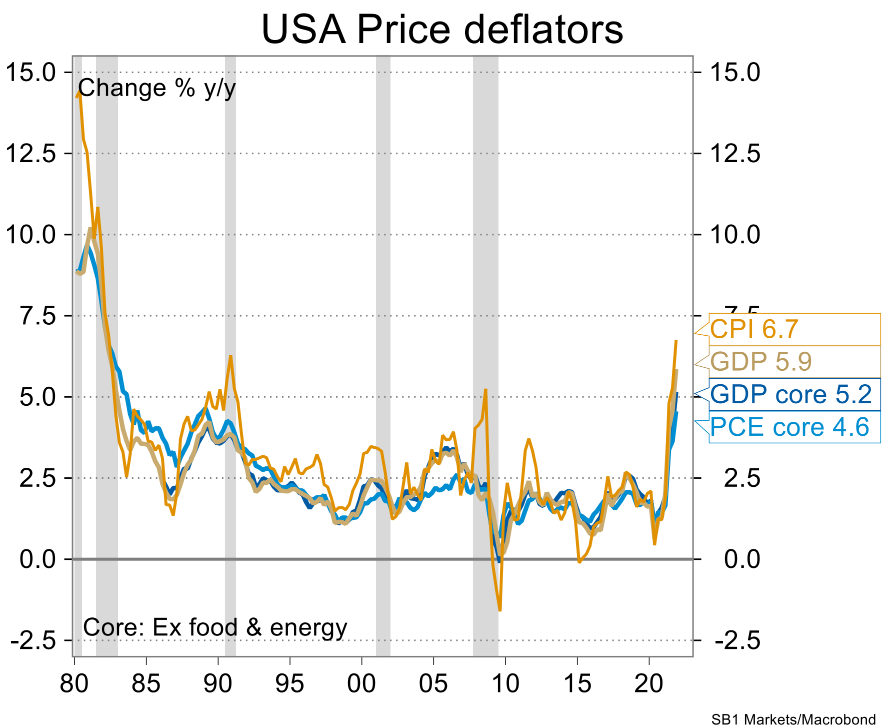


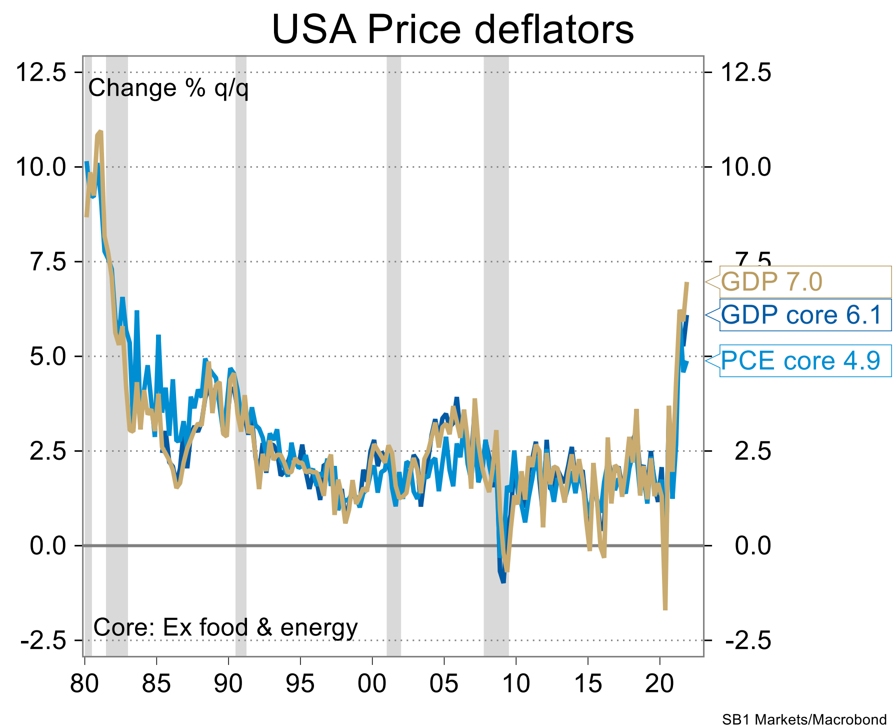


- Normally goods and structures are the main culprit during recessions, at these sectors are the most volatile elements in the economy. In addition, services are normally lagging. During the Covid-19 crisis, the service sector was the main swing factor – and it has far from recovered

Price increases accelerated in Q4 – and we are at levels not seen in decades

All GDP/PCE deflators up 5 – 7% in Q3. Nominal GDP grew 14.4% in Q4!

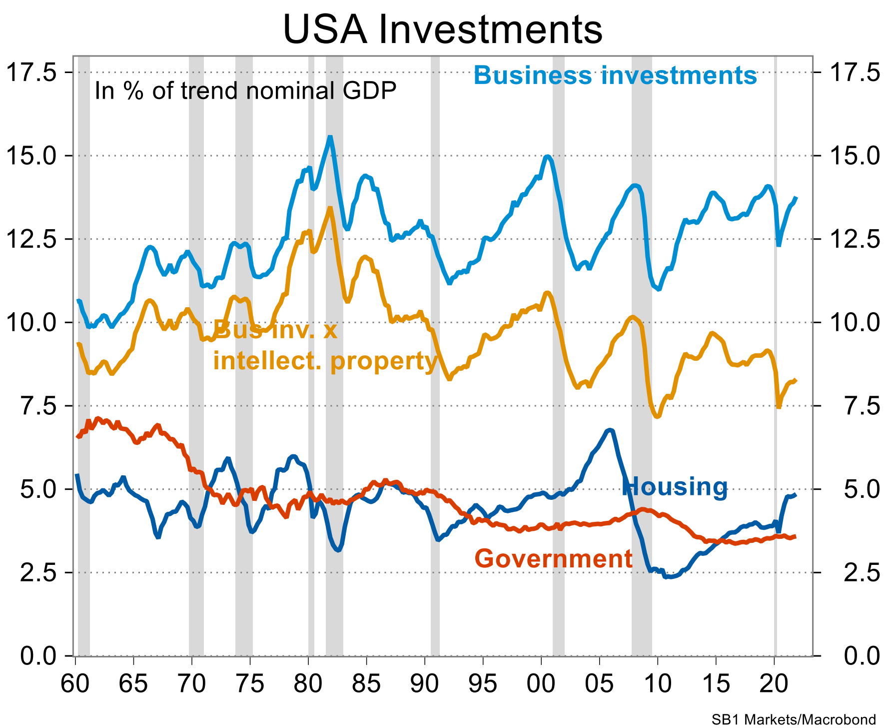


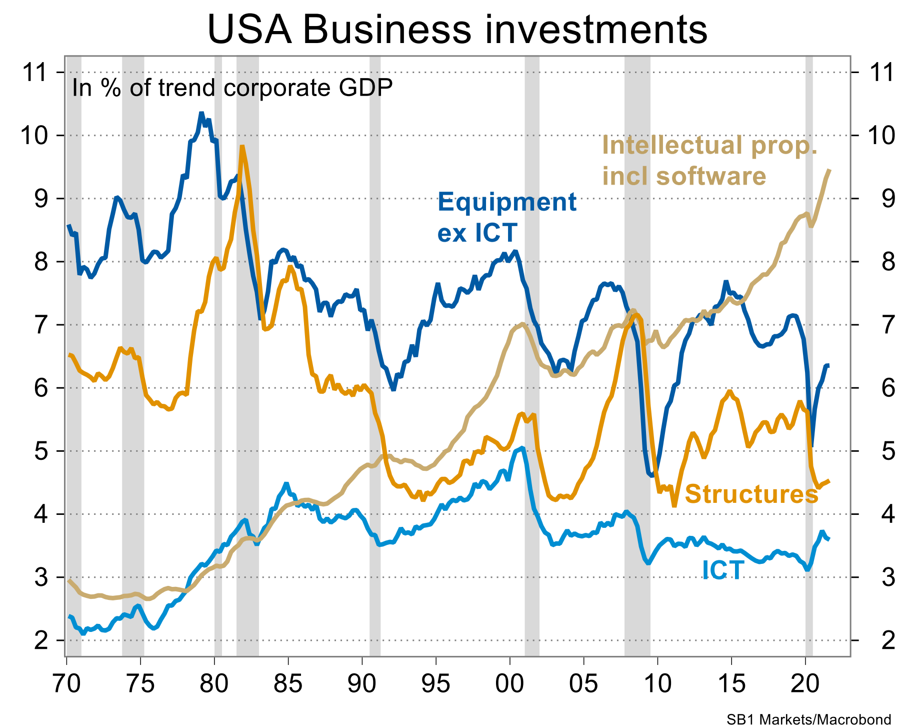


- Higher energy prices partly to blame but other prices also contributed in Q4, as during the previous quarters. The growth rates are the highest since 1982
- The core (x energy, food) PCE deflator (Fed's preferred measure) is up 4.6% y/y (and by 4.9% in Q4), the highest since 1991. The 40% lift in used auto cars explains a substantial part of the lift in the core PCE
- Nominal GDP grew at a 14.3% pace in Q4, the price deflator rose 7.0%. Over the past 2 years, nominal GDP is up 5.2% in average

Investments: Total business investments strong, housing investment high too

Business investments above trend just due to IP & software, ICT. Other equipment, structures still weak

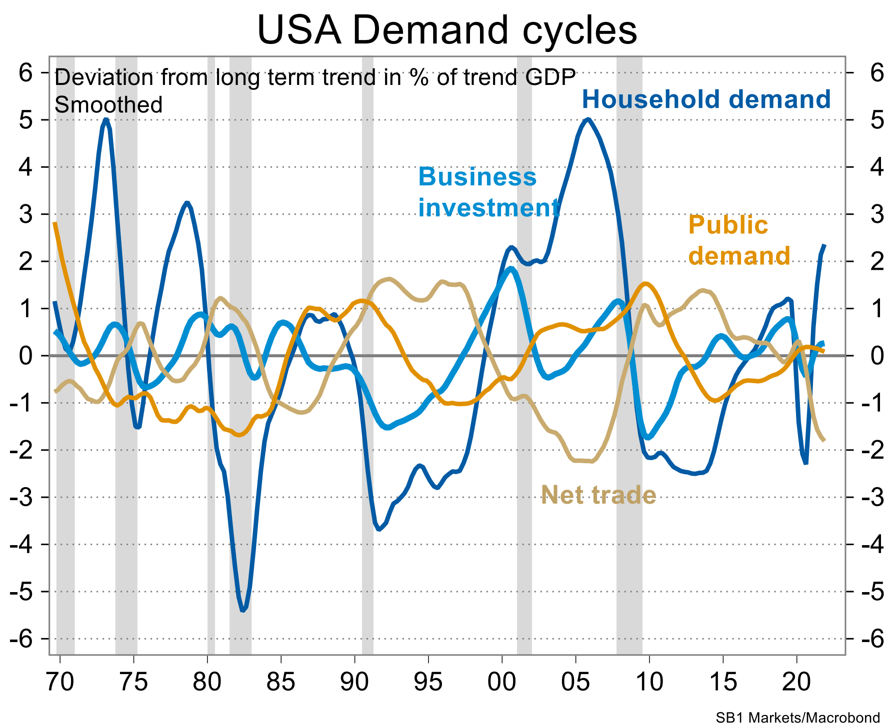


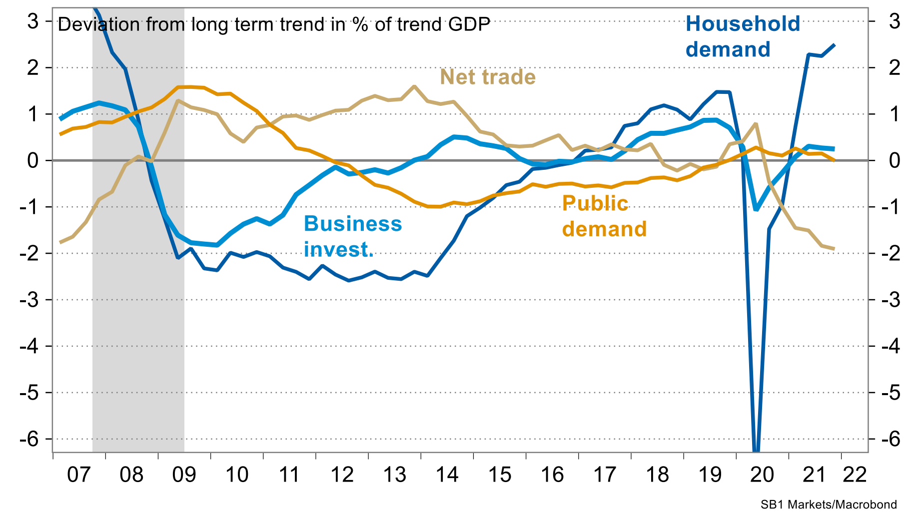


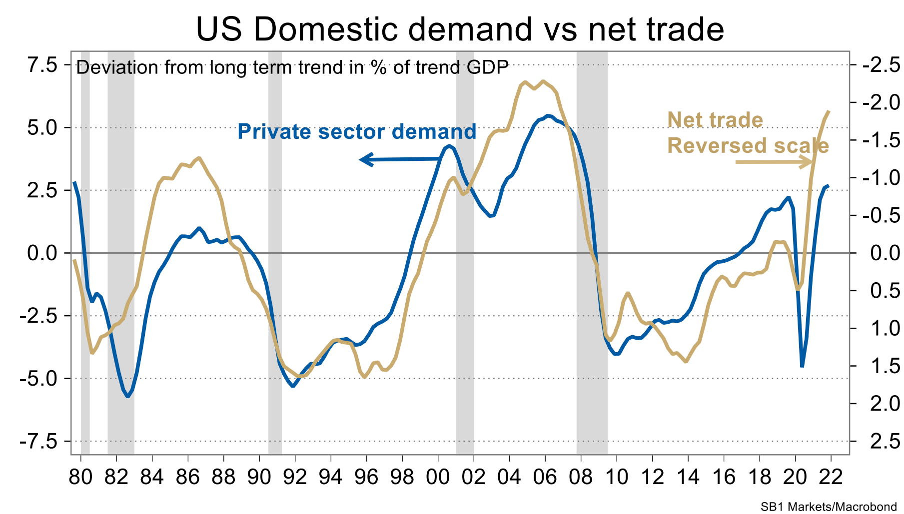
- **Business investments** are up 5.5% vs. the Q4-19 level (in volume terms), driven IP/software and ICT equipment. Investments in structures are still very low. Investments in equipment x ITC may be close to trend
  - » Thus the outlook for business investments is not clear: The boom in IP/software/ICT may well continue, even if the levels are high. There is still upside for other equipment and structures, at least vs the normal cycles in these sectors
- **Housing investments** fell in volume terms but prices rose sharply, and investments have just flattened vs. nominal GDP
- **Government investments** as share of GDP are close to flat vs GDP. The infrastructure package will lift the investment ratio by less than ½% of GDP, from the overall investment level at 3.5% now

A private consumption cycle. Or rather, a virus cycle…

A shallow & short business investment downturn. Net trade is on the weak side, but exports will recover?



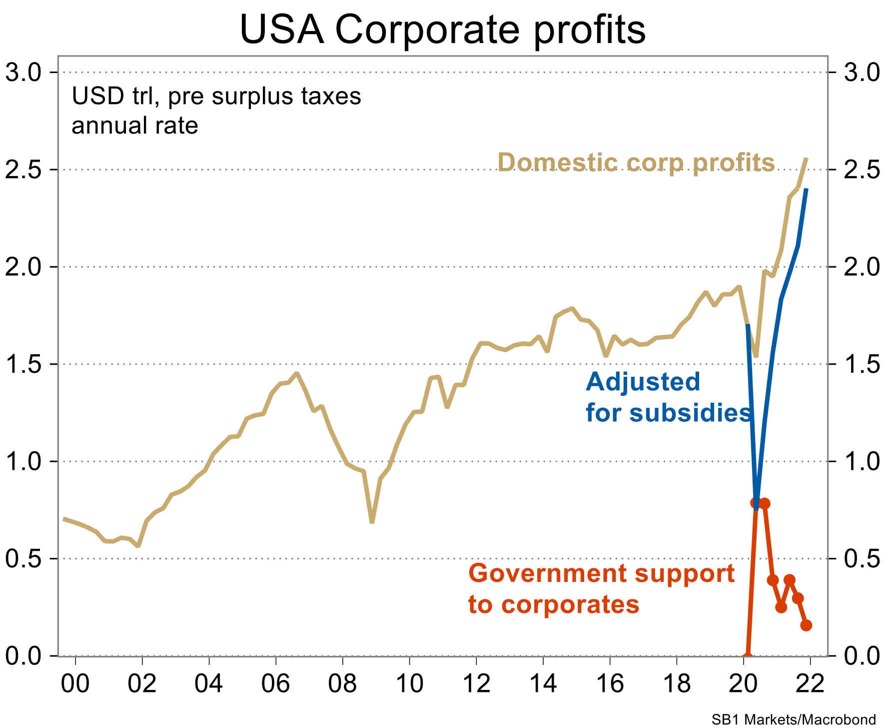


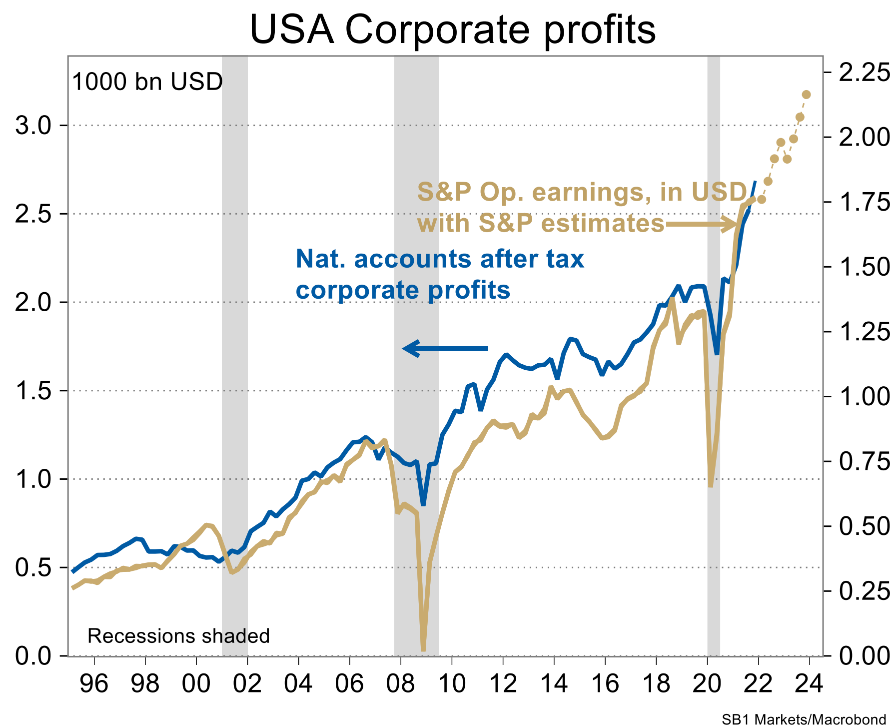


- *Check more on the household sector some few pages forward*

Corporates' profits rose further in Q4, as they lifted prices at a 8% pace

Subsidies were cut, but profits still rose even if the wage bill grew rapidly



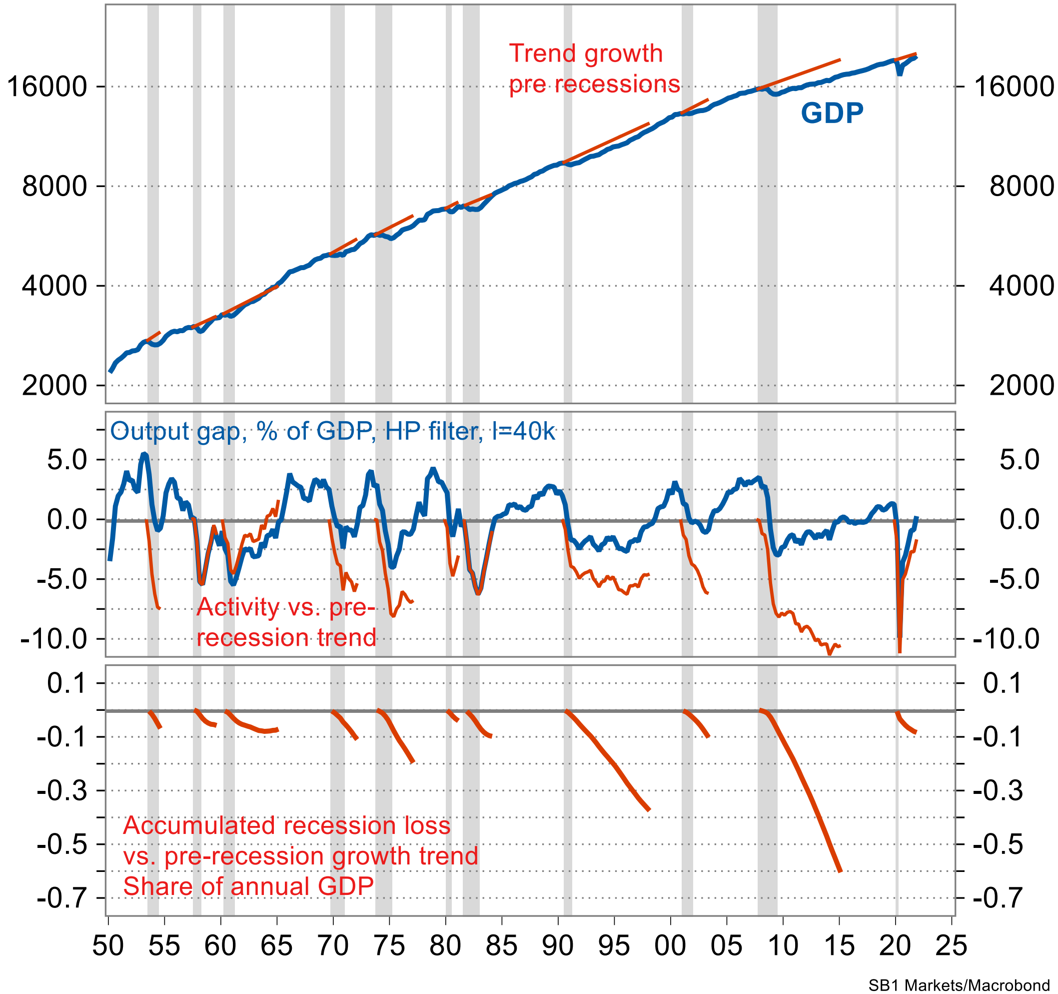


- **We assume domestic corporate profits** rose by approx. 6.5% in Q4, not annualised (28% annualised, and 31% y/y – even if the wage cost rose much faster than normal – and prices surged
  - » The wage bill rose by 10.5% (annualised) in Q4 (domestic corporate sector) but value added rose even faster, by a 17% pace, as companies were able to lift their prices at an 8% pace (domestic corp x finance), an incredible high number. And increasingly hard to swallow for the Federal Reserve…
  - » Government subsides (deviation from trend in indirect taxes – subsidies) were cut but still equals more than 1% of GDP
- The **S&P 500 companies** reported a further increase in profits in Q4 but at a rather slow pace, according to S&P estimates
- We think the profit outlook is muted. Wage inflation will not subside anytime soon given the super tight labour market – and a continued price inflation at the current pace cannot be tolerated by the Federal Reserve. Exciting times ahead

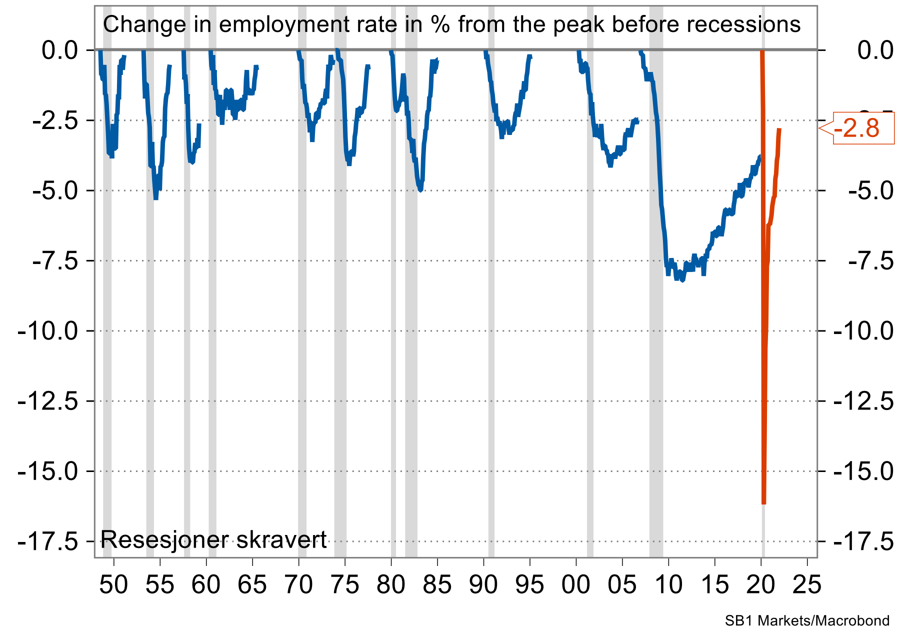
The big picture: The pandemic downturn was deep but very short

The accumulated economic loss will very likely turn out to be among the smallest in history

US GDP vs recessions



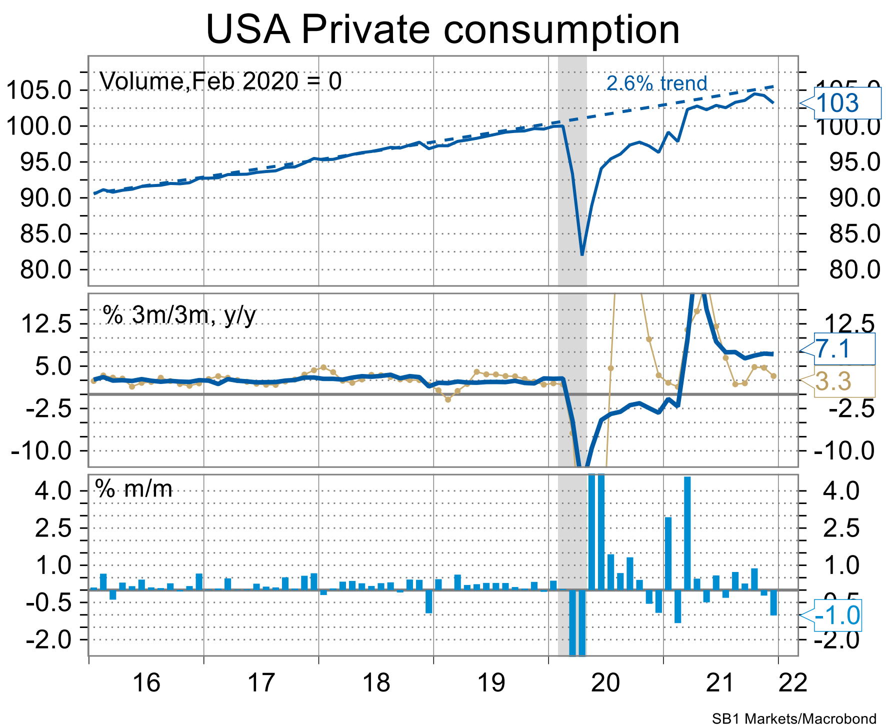
USA Employment during recessions, and afterwards

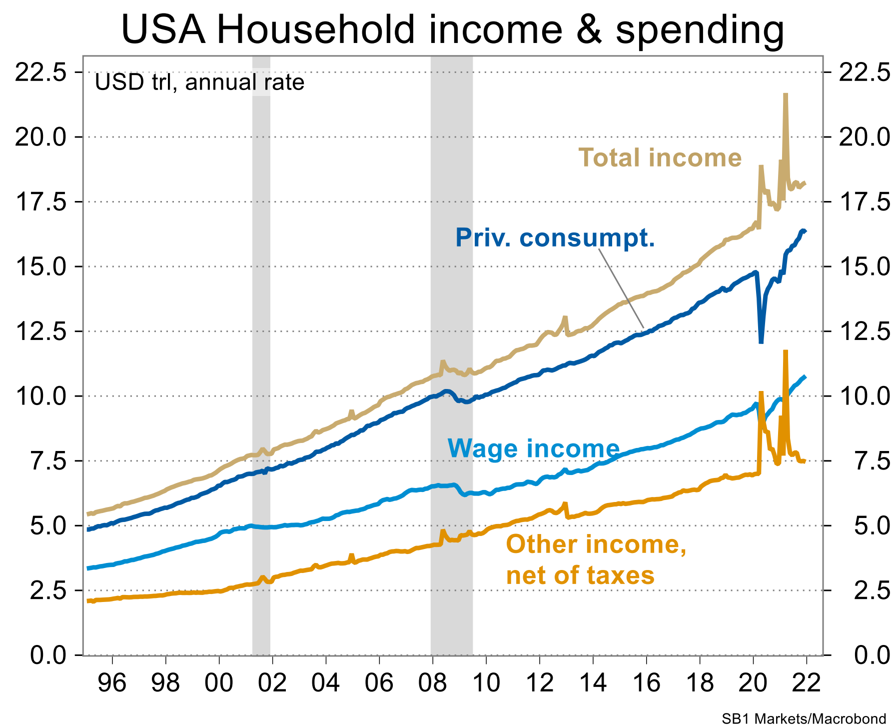


- **The accumulated GDP loss** at the bottom chart to the left is calculated by accumulating the gap to a reasonable growth forecast ahead of the recession based on actual growth trends in the 3 – 5 years before the downturn (adaptive expectations; red lines at the top panel to the left). These gaps are accumulated until the traditional output gap is closed (which is an arbitrary ending point of course, and unknown real-time)
- Most metrics will conclude that the Financial crisis (2008 – 09) created the hardest economic downturn since WWII by far, as growth the following years was far lower than most expected before the crisis
- The accumulated employment loss was large as well – and rather limited this time (even if the employment rate is not back to a normal level yet

Real consumption down 1% in December, goods down 3% - broad based

Real incomes fell by 0.2% - and the savings rate added 0.7 p to 7.9%, in line with the pre-p level

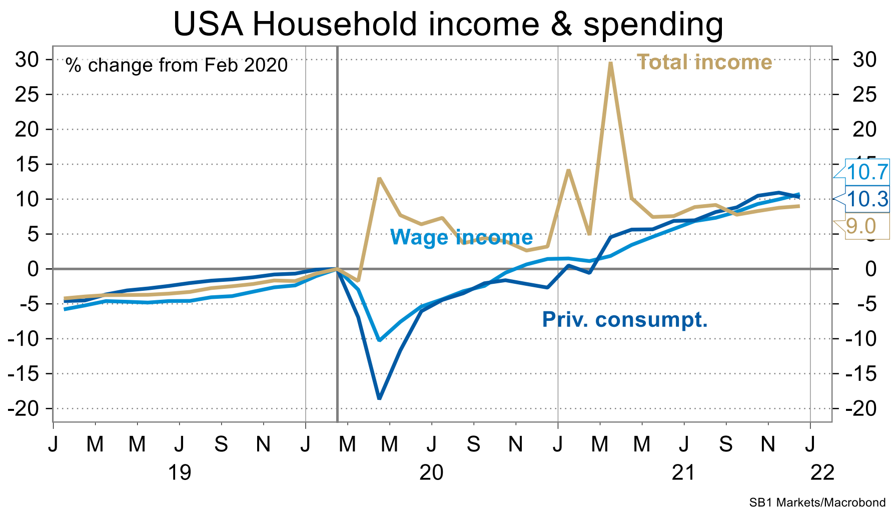


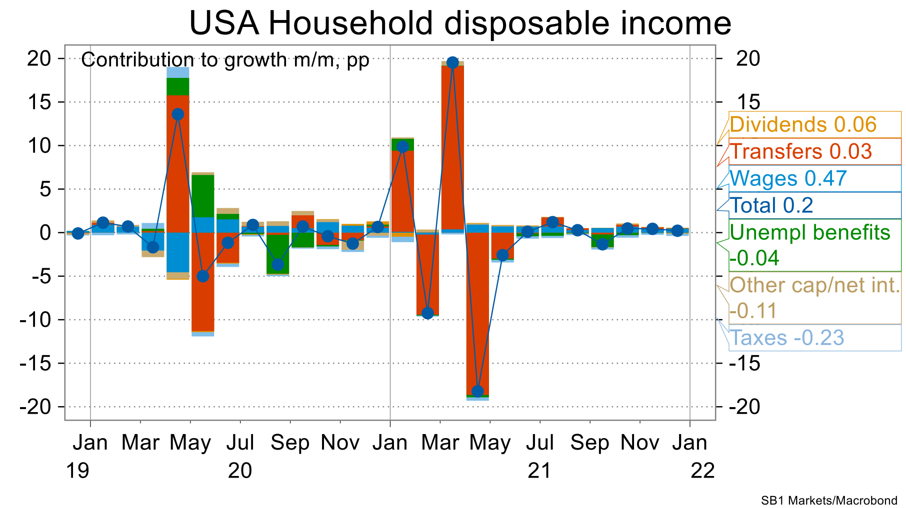


- **Private consumption fell 1% in** Dec, as expected. In nominal terms, spending fell by 0.6% - and prices fell 0.4%. In Q4, consumption grew at at 3.3% pace. Consumption of goods fell 3%, as signalled by the surprisingly weak retail sales report – but the level is still 5% above the pre-pandemic growth path! Services have been somewhat slowed by the Delta/Omicron outbreak, but consumption is heading steadily upwards. Total consumption is up 3% vs. the Feb-20 level, but still 2% below the 2.6% pre-pandemic growth path
- **Real personal disposable income fell by 0.2%** in Dec. Income before taxes rose by 0.5%, as expected. Wage revenues contributed the most at the upside. Underlying wage income growth is still strong – and nominal wage incomes are still well above the pre-pandemic trend path
- **The savings rate** rose by 0.7 pp to 7.9% (from a 0.3 pp upward revised level in Nov). Savings are at the same level as before the pandemic. However, households have saved an extra amount equalling 13% of one year's disposable income during the pandemic – in average, that is. Some of this 'Wall of Money' may well be spent the coming quarters, taking the savings rate further down
- **Both consumption and income growth is normalising.** Spending on goods is still too high, and too low on services. In total, the level is not far from 'fair'

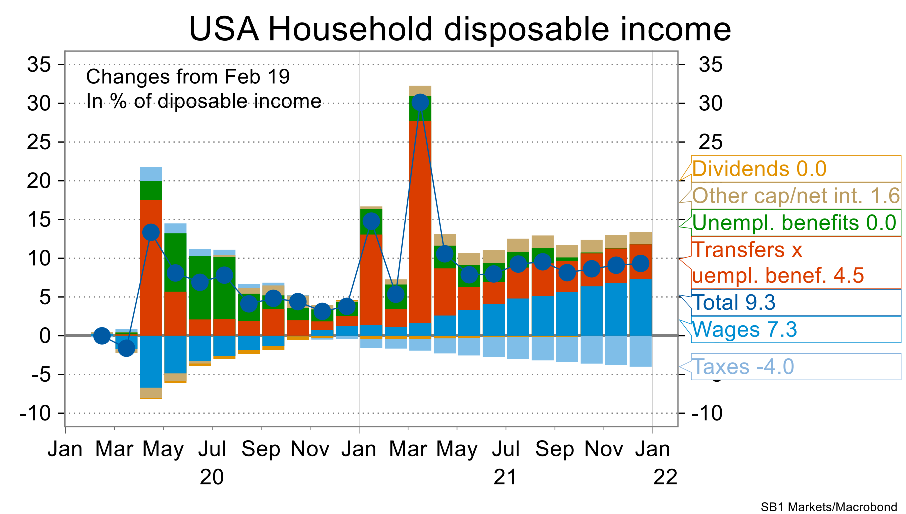
Income growth is not impressive anymore, and was just at 0.2% in December

Wage revenues are climbing rapidly. Transfers ex. unemployment benefits are back on trend



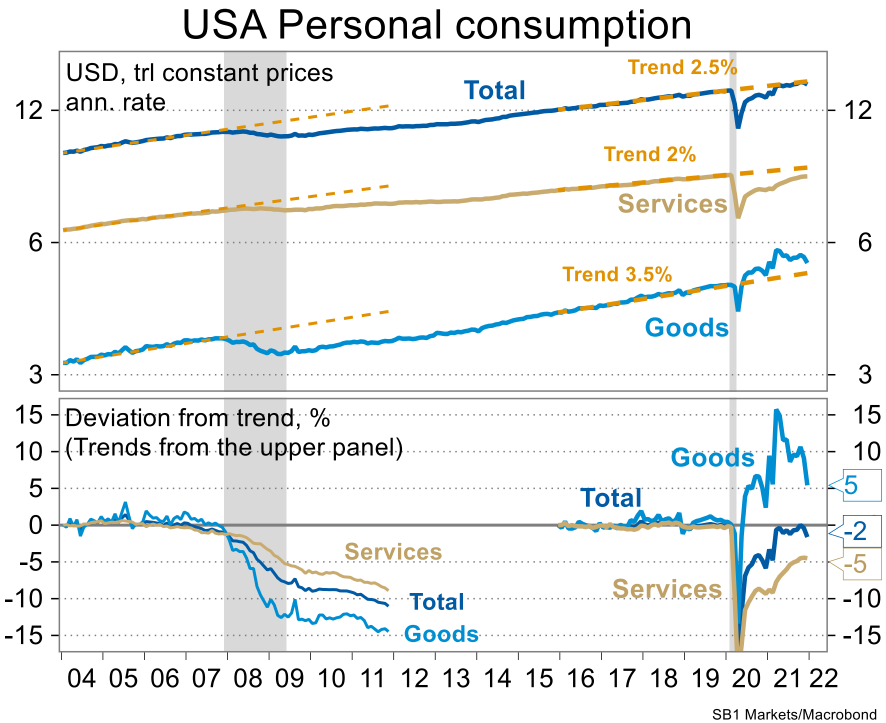


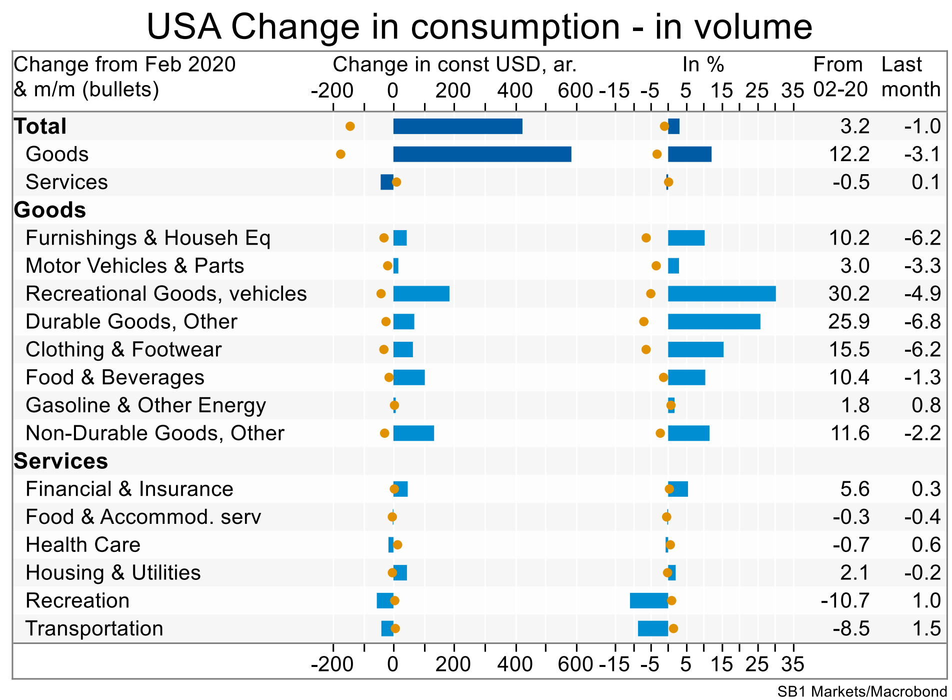
- **Total income has** flattened since the spring as ordinary public transfers and unemployment benefits have normalised
- **Total wage income** is growing rapidly and are above the pre-pandemic growth path at 4.25%, even if employment & hours worked remain well below the pre-pandemic level. The reason is of course the sharp increase in wage inflation



A sharp, and broad decline in consumption of goods in Dec, still too high?

Services are gradually recovering but are 5% below the pre-pandemic trend path





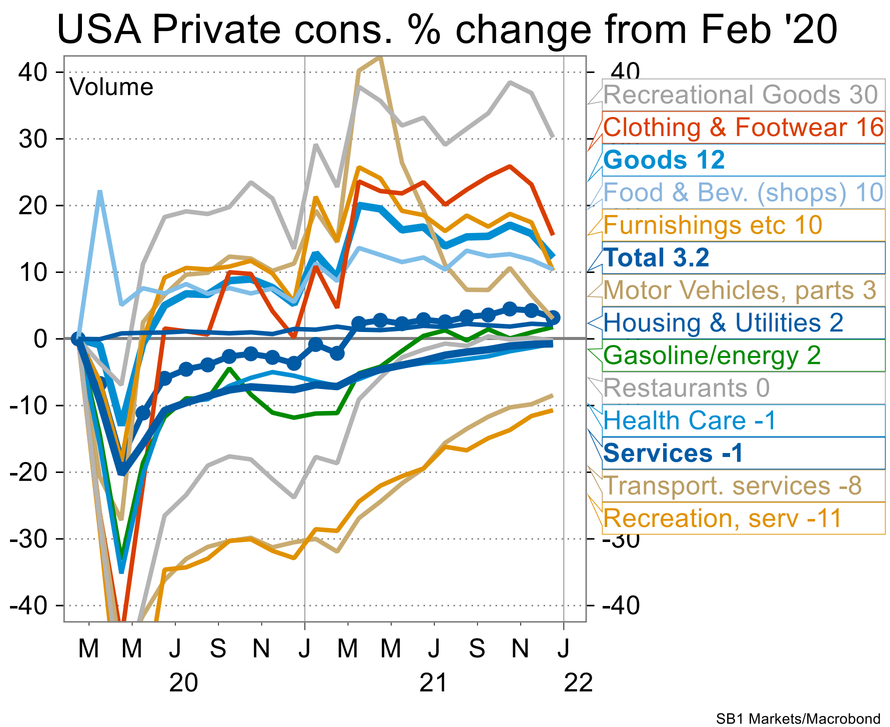
Change from Feb 2020 & m/m (bullets)	From 02-20	Last month
Total	3.2	-1.0
Goods	12.2	-3.1
Services	-0.5	0.1
Goods		
Furnishings & Househ Eq	10.2	-6.2
Motor Vehicles & Parts	3.0	-3.3
Recreational Goods, vehicles	30.2	-4.9
Durable Goods, Other	25.9	-6.8
Clothing & Footwear	15.5	-6.2
Food & Beverages	10.4	-1.3
Gasoline & Other Energy	1.8	0.8
Non-Durable Goods, Other	11.6	-2.2
Services		
Financial & Insurance	5.6	0.3
Food & Accommod. serv	-0.3	-0.4
Health Care	-0.7	0.6
Housing & Utilities	2.1	-0.2
Recreation	-10.7	1.0
Transportation	-8.5	1.5

- Services are recovering, but even so down 0.5% vs. the Feb-20 level, and down 6% vs the pre-pandemic trend path
- Demand for durable goods (ex autos) are way above sustainable levels, we assume
- Spot the differences between the Financial Crisis downturn and the pandemic ‘downturn’

There are some larger aggregating differentials than usual in the PCE accounts, and the sums do not add up to the total

Consumption of goods down 3% m/m, still up 12% vs the pre-pandemic level

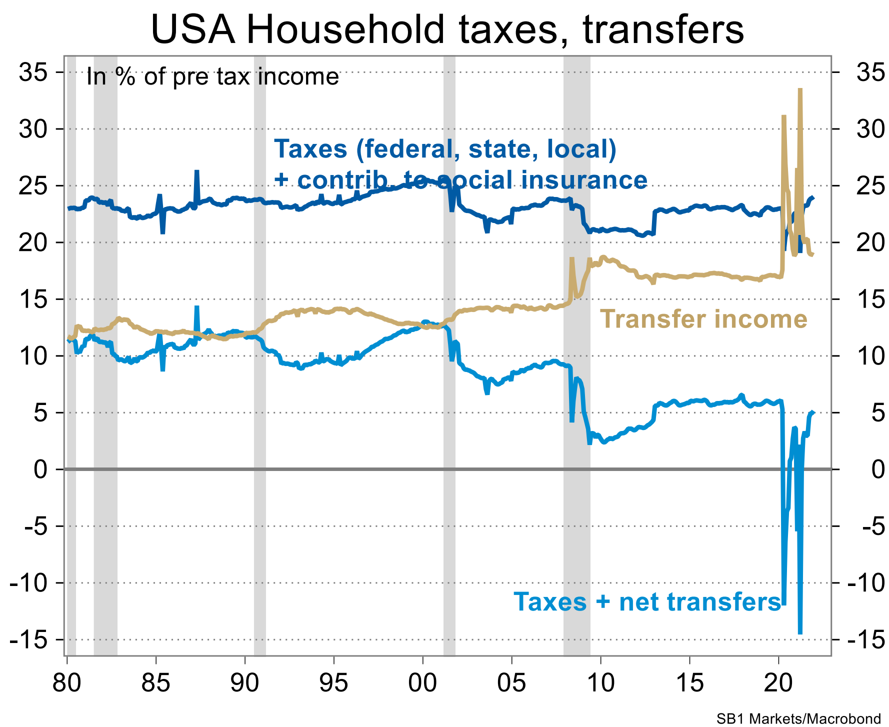
Services are recovering but none (x housing) are above the p-p level. Recr. services are still down 13%

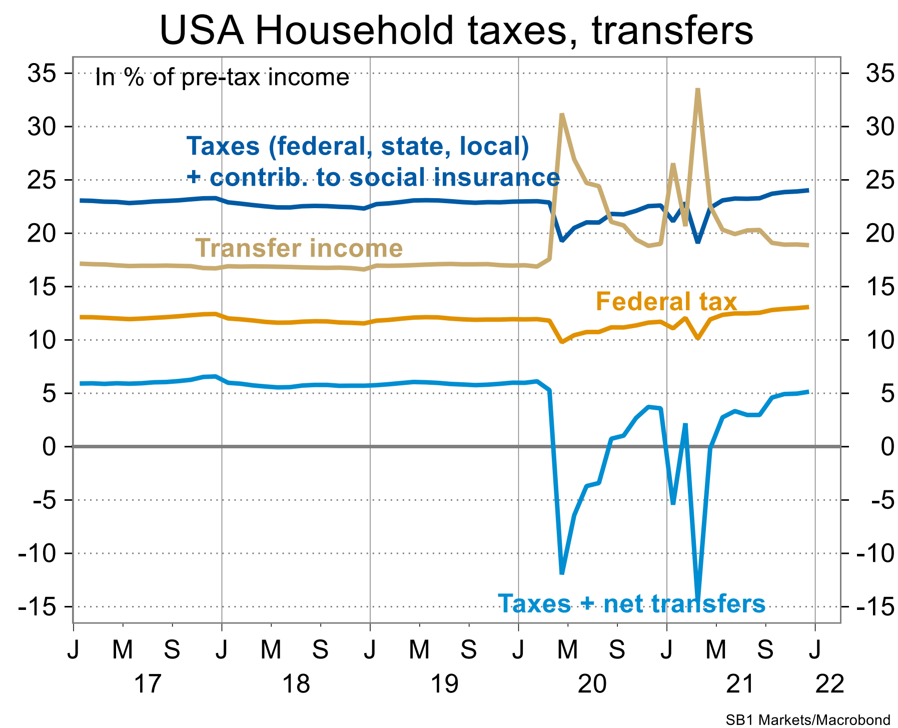


- **Consumption of goods** fell sharply in December, and we cannot put the blame on an extra strong November. The trend is down, as one should expect given the still very high level
- **Consumption of services** grew 0.5% in Nov. Spending is 0.5% below the Feb-20 level, in volume terms. Restaurants are back to the starting point, in volume terms ('meals served'), while transportation (-8%) and recreation (-11%) are far below – <u>so there must be more to go the coming months/quarters, at least when (not if) the fight against Omicron is won</u>
- **Total consumption** is up 3.2% vs. Feb-20. Since March, growth in spending has been muted, but recent months growth has gained some speed, supporting GDP growth in Q4

Towards more normal times – transfers still above par

Net taxes at 5% of pre-tax income is just 1% below the pre-p level – which though was far too low

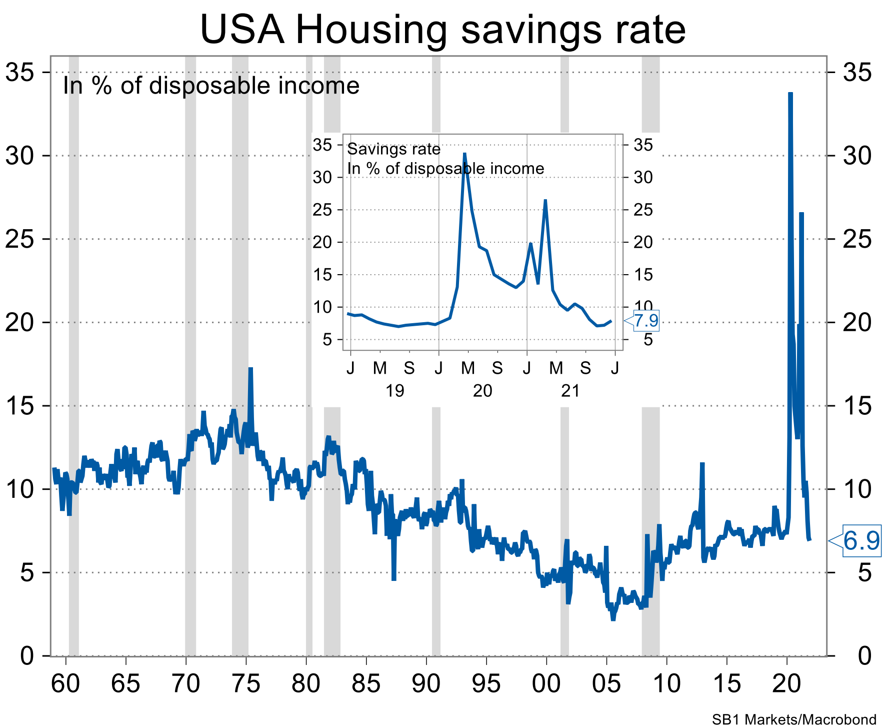


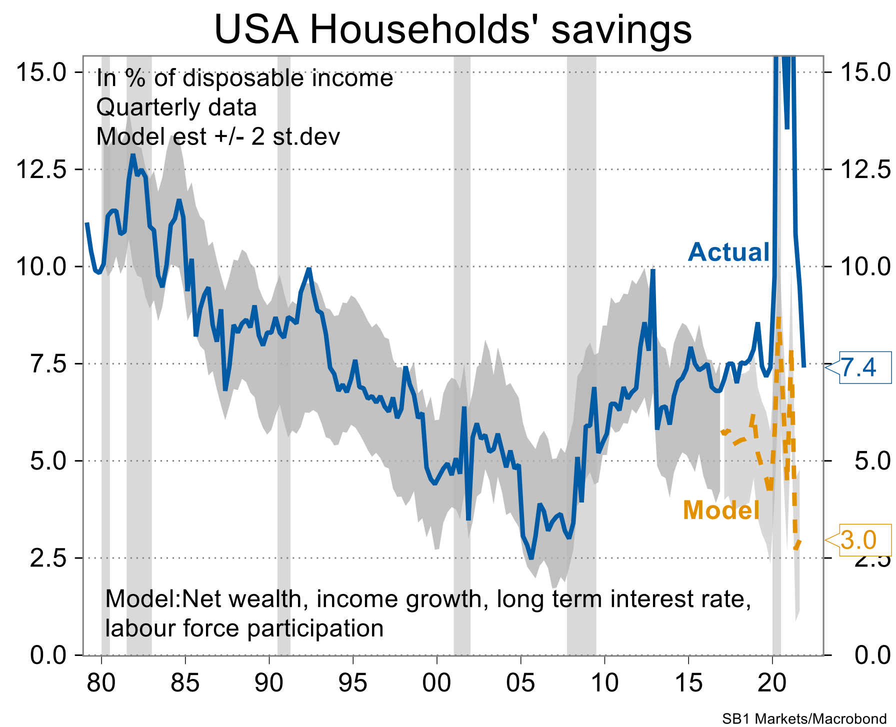


- The 'normal' net tax rate (taxes-transfers) implied a substantial government deficit – which was not sustainable
  - » Before year 2000, the net payment to the federal government equalled 10% - 12% of pre-tax income …. and somewhat below 10% until the Financial crisis. Since 2012, the net tax rate has been some 6% of GDP, and now at 5%
  - » Taxes are back to the pre-pandemic – or even a tad above – while transfers are

The savings rate up 0.7p to 7.9%, in line with the pre-pandemic level

Will the savings rate stabilise at today's level? If so, income growth will decide consumption growth

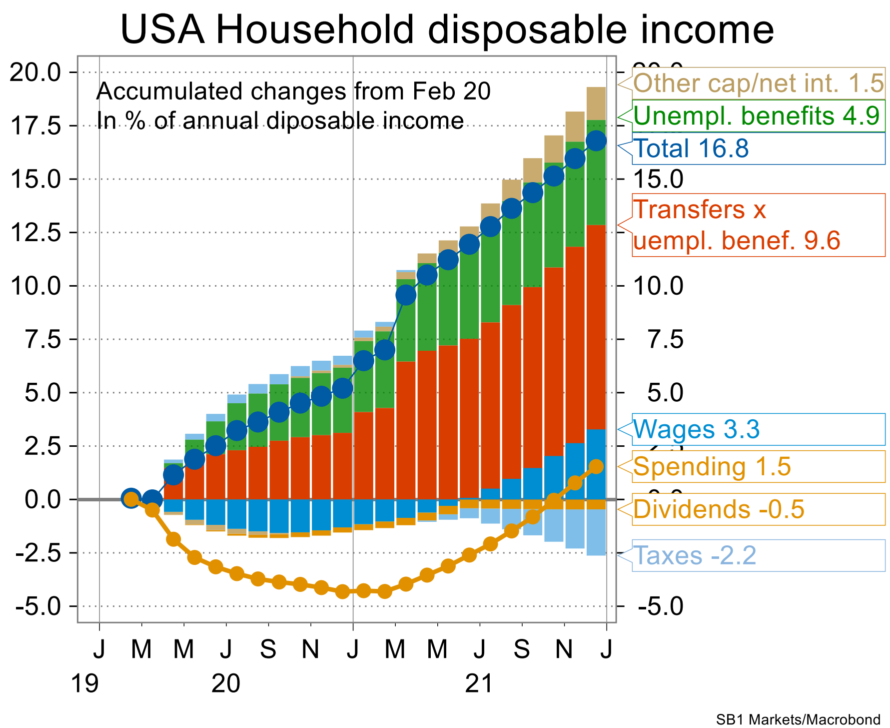


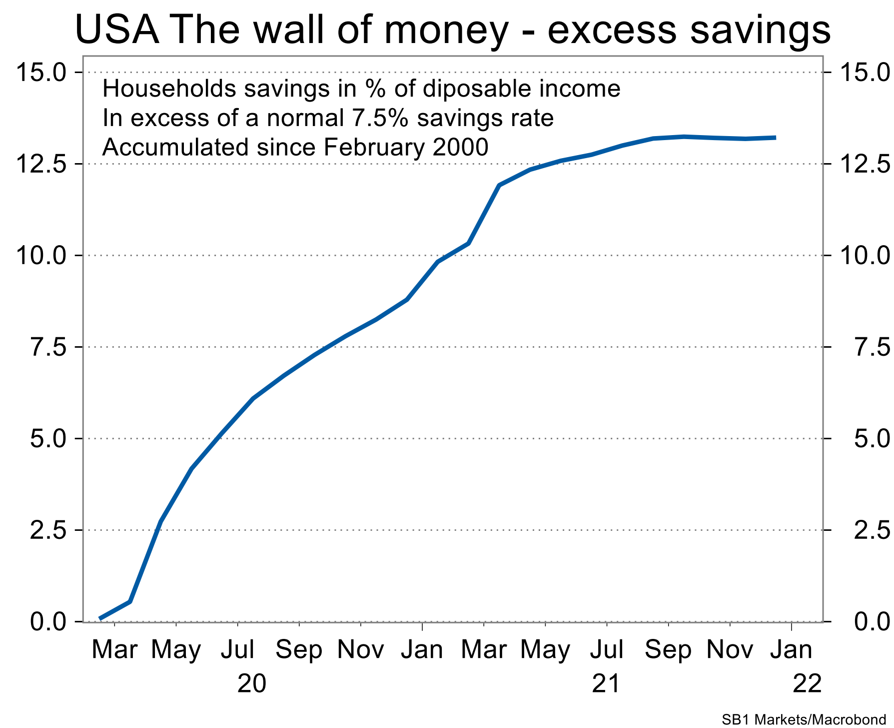


- Our old savings model, yields a 3% savings rate in Q3. During the 2016 – 19 period our old model has underestimated the savings rate systematically by some 2 pp
- The gap is now much larger – and it has been so during the pandemic, of understandable reasons – spending was not possible
- A downside potential for the savings rate (and upside for spending): **the 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 is still intact

The sum of ‘excess savings’ through the pandemic is at some 13% of annual disposable income

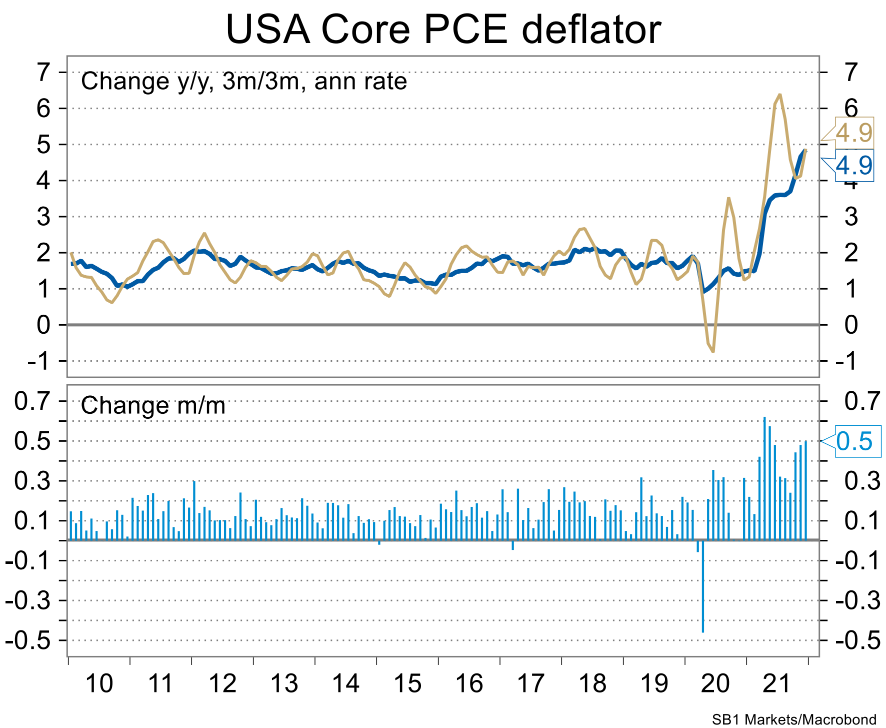


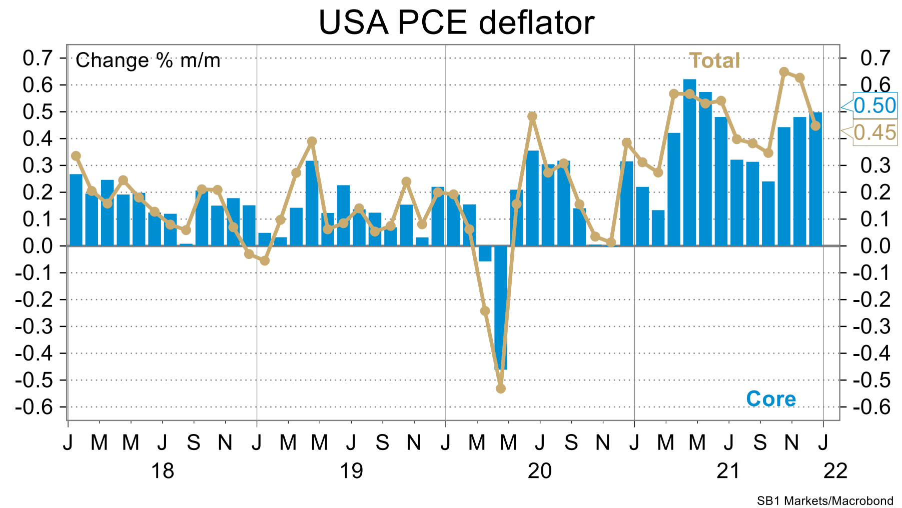


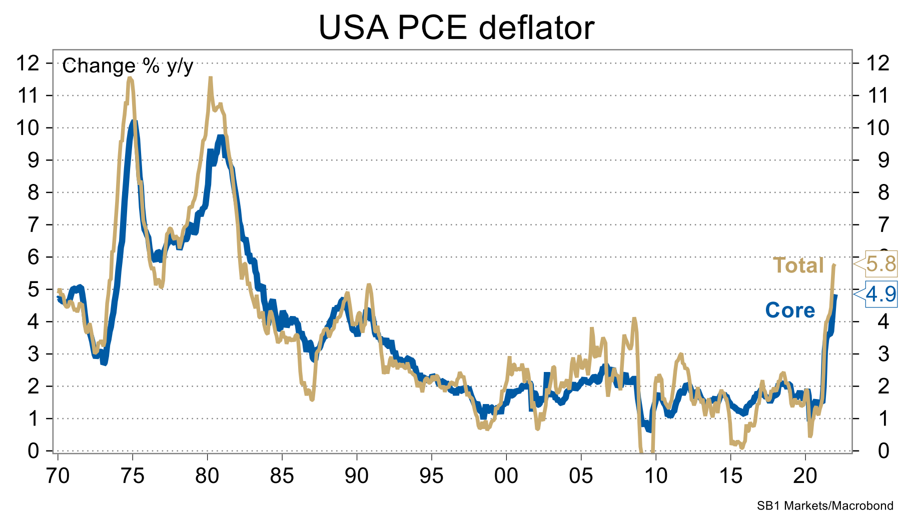
- Transfers from the government and low spending (on services) explained the lift in savings - but now spending is coming back, and the savings rate is now lower than before the pandemic

The PCE consumption deflator joined the CPI's large ~~Oct~~ ~~Nov~~ Dec hike

Inflation remains high, and its broadening. A substantial part of it is quite likely transitory but not all



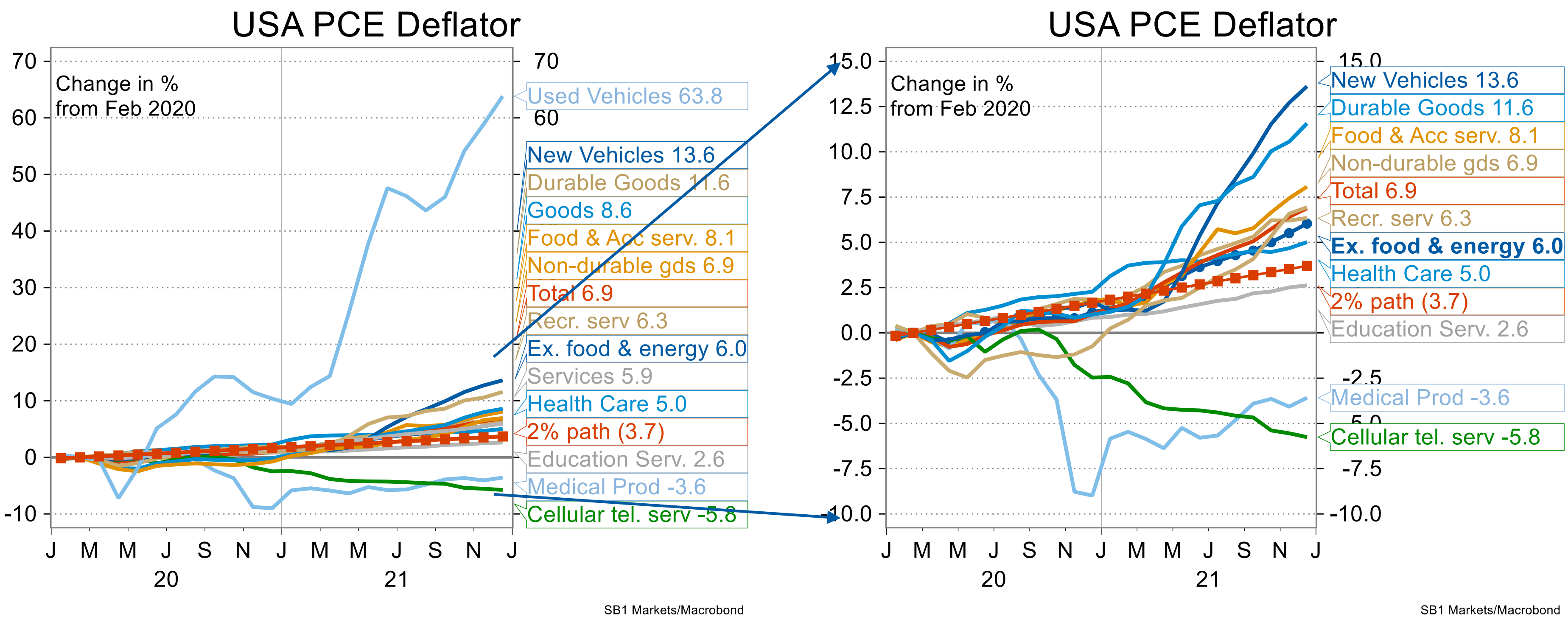




- **The total PCE deflator** rose by 0.4% in Dec, as expected, and the annual rate accelerated 0.1 pp to 5.8%, the highest since 1982
- **The core PCE** rose by 0.5% m/m, also as expected. Measured y/y, the core gained 0.2 pp to 4.9% - and has not been higher since 1983
  - » The 3m/3m rate is close to 5%
- **The price level** is far above Fed's 2% long term path target, and the FOMC members expect inflation to remain above 2%. Thus, they plan to leave the price level target even further behind, even if the maximum employment target also may already be met

Most prices are up more than at a 2% pace since before the pandemic

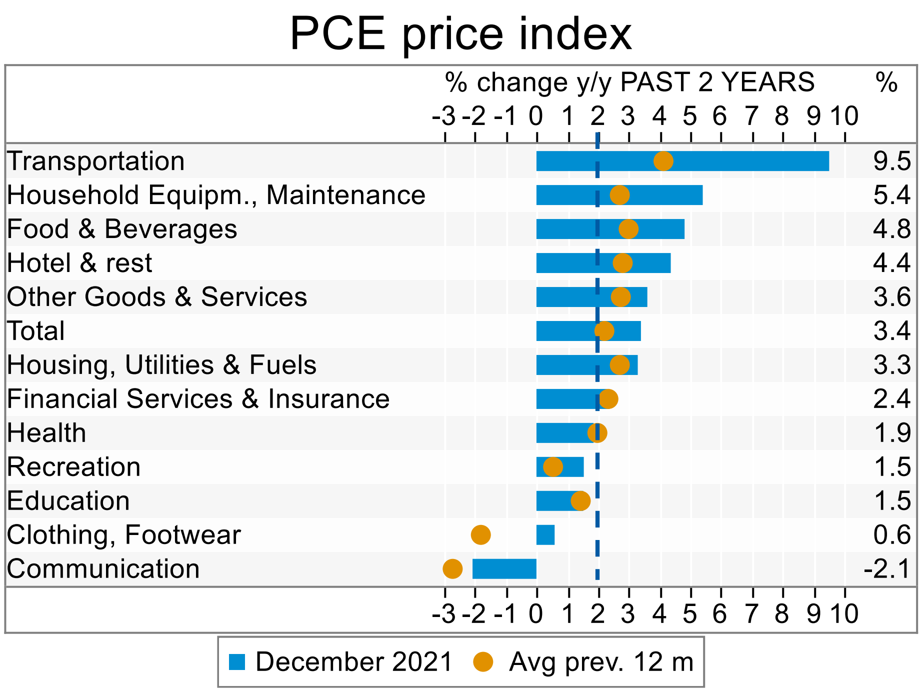
We are still waiting for used car prices to come back to earth – they are up more than 60%!!!



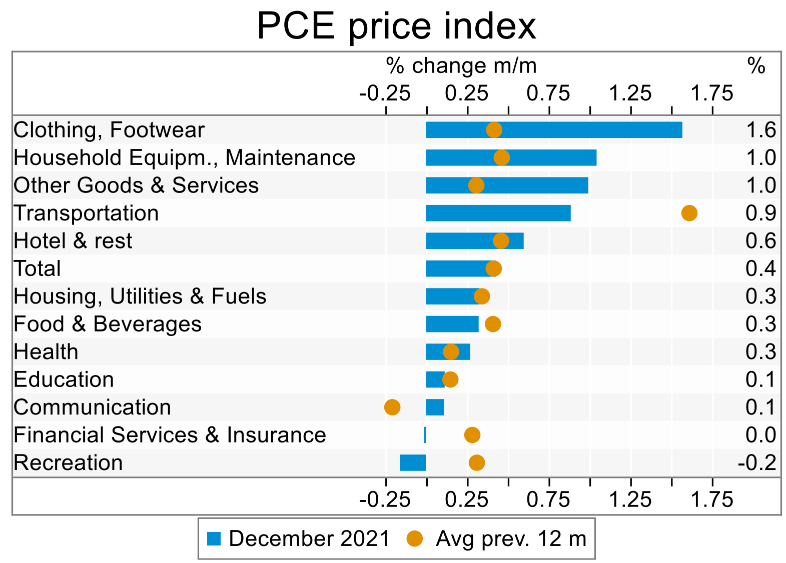
- **New car** prices are up ‘just’ 13.6% since Feb-20
- **Hotel & restaurant prices** are up 8.1% since Feb-20

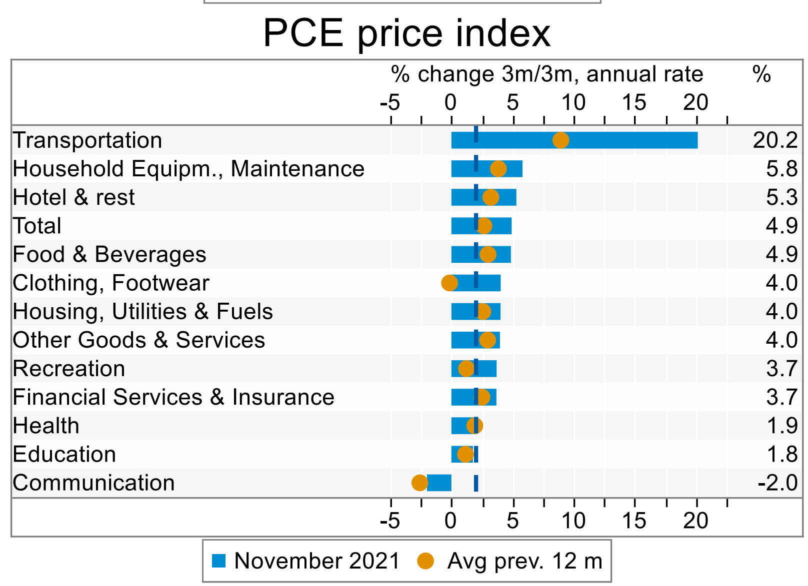
PCE by main sectors: Most sectors report >2% growth past 2 years

… and most sectors are up more than 2% measured 3m/3m, the total is up 4.9%



SB1 Markets/Macrobond

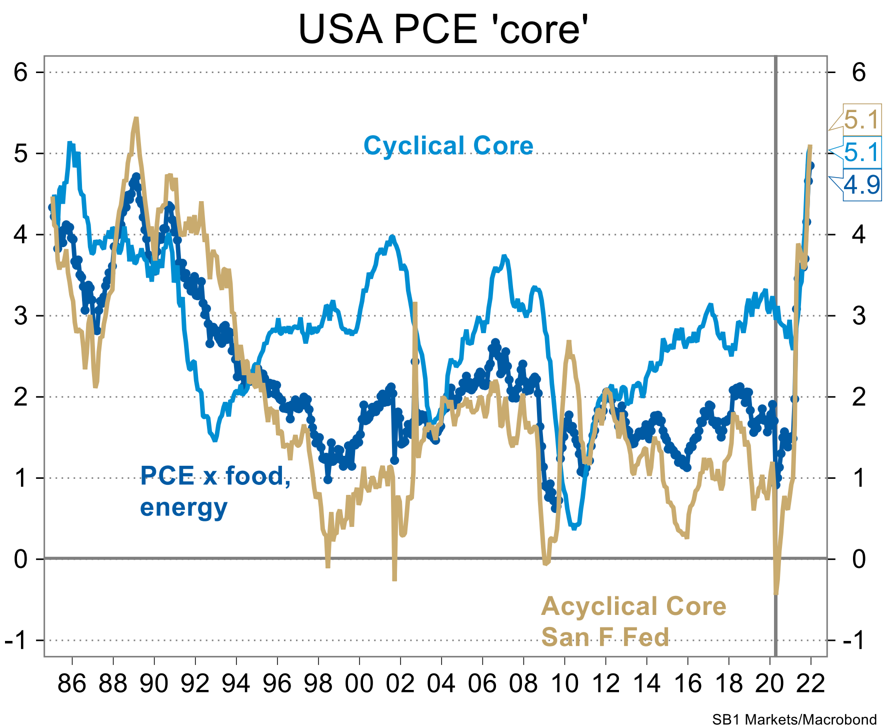


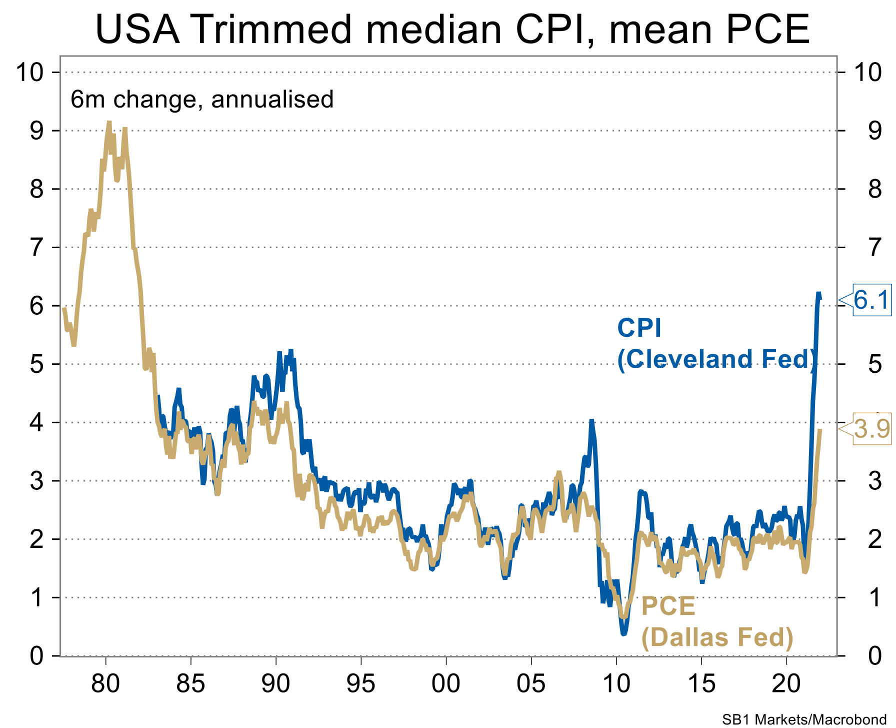


- Just health (!), education, communication, recreation and education prices are up less than 2% on average over the past 2 years
- The momentum is still strong, almost sectors report accelerating price growth (the 3m/3m is above the annual rate)

Inflation has broadened, more prices are climbing faster

All 'underlying' measures are now above the 3% line, not seen in decades

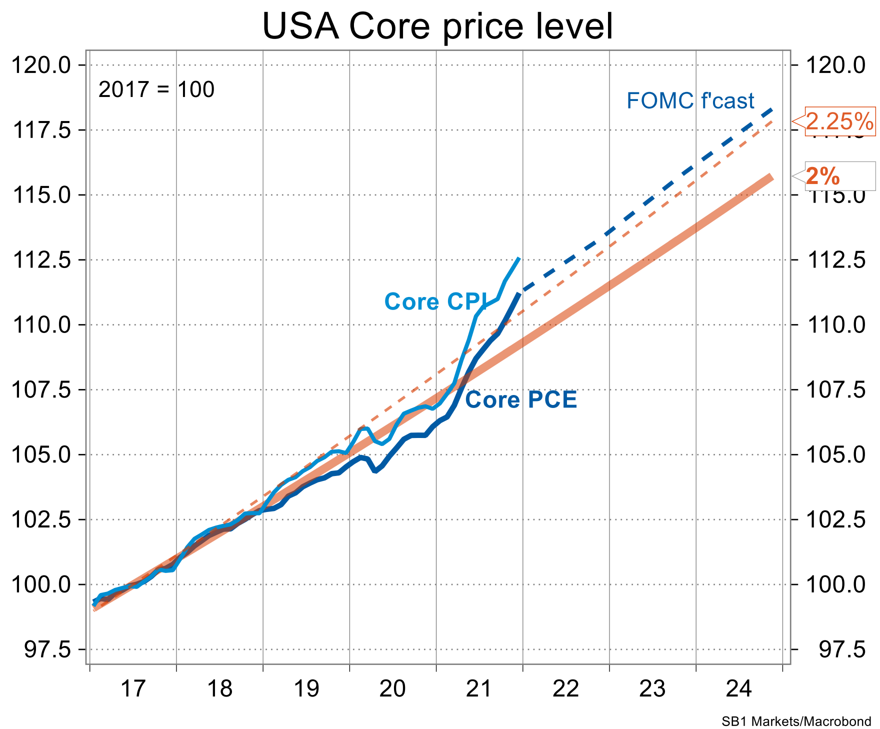


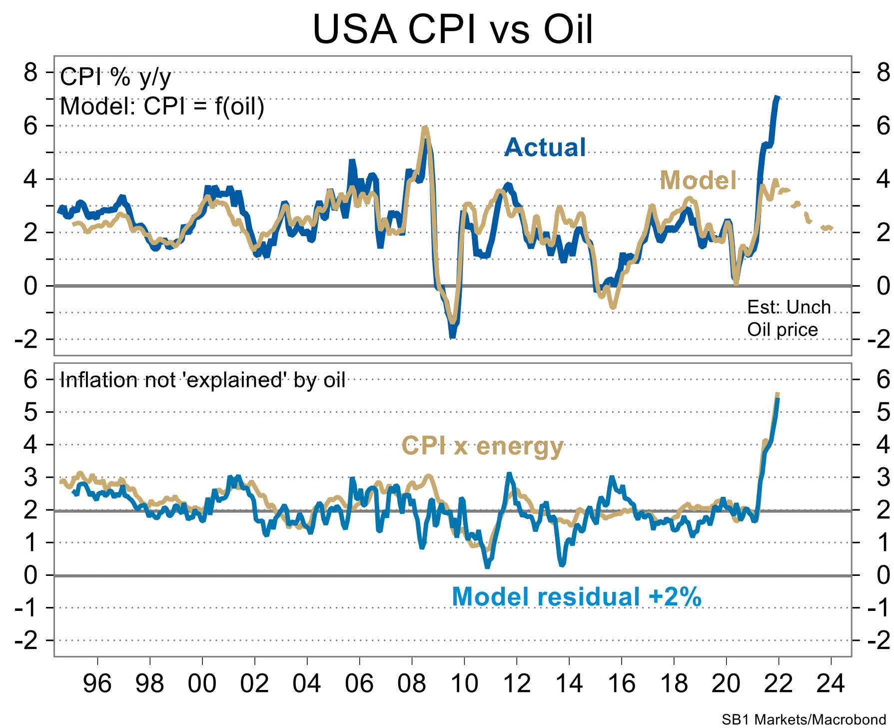


- The **trimmed PCE mean** (Dallas Fed) is up at a 3.9% pace over the past 6 months, up from 2% ahead of the pandemic (and 3.5% in Nov). This indicator of underlying inflation has not been growing faster since 1991
- The trimmed median CPI (Cleveland Fed) is up 6.1% over the 6 months, the highest on record, data back to 1983
- Both core cyclical and acyclical PCE prices are up close to 5% y/y
- Other measures of underlying inflation are also at the highest levels in 30 years
- At that time – 30 years ago – the Fed funds was not at zero

The Fed expects the 2% price target to slip, even if the employment target is met

… or more than that



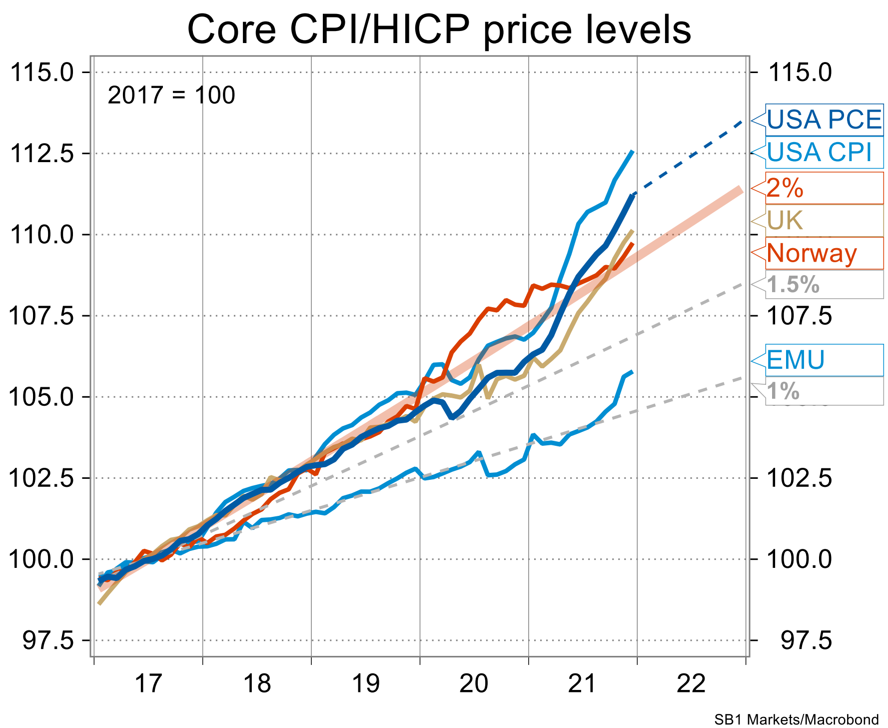


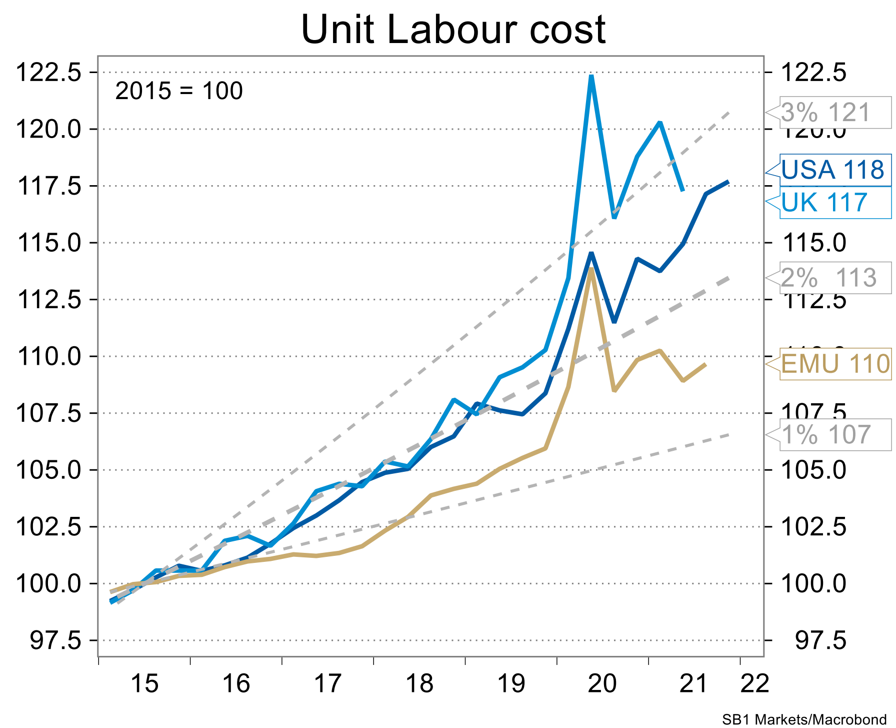
We stick to our main inflation analysis:

- **Raw material cycles** are not lasting that long, and the impacts on consumer prices are normally 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 inflation = wage inflation – productivity growth
- **A tight labour market** normally implies higher wage inflation. Now, the vacancy rate is the highest ever, and all wage cost indicators signal higher wage growth. This is the real challenge for the Fed. At the Dec FOMC meeting, Powell acknowledged that wage inflation in the end is the final criteria for judging if the maximum employment target is met. Thus, before soon, the Fed may be missing on both of its targets – at the same side

So far, inflation is mainly a US problem (excluding the common energy factor)

UK is also reporting high core inflation rates but prices slowed last year

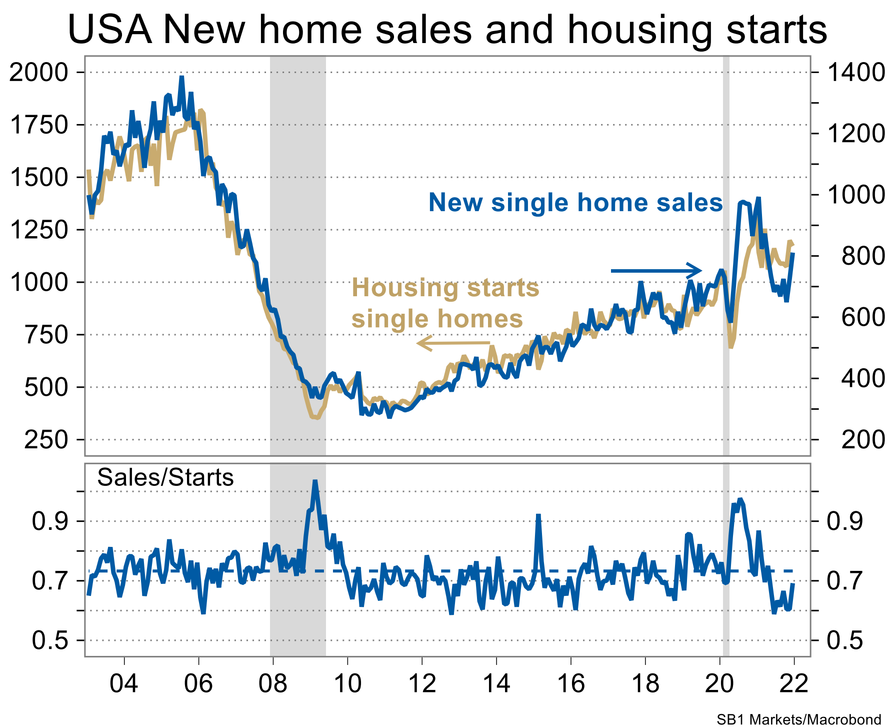


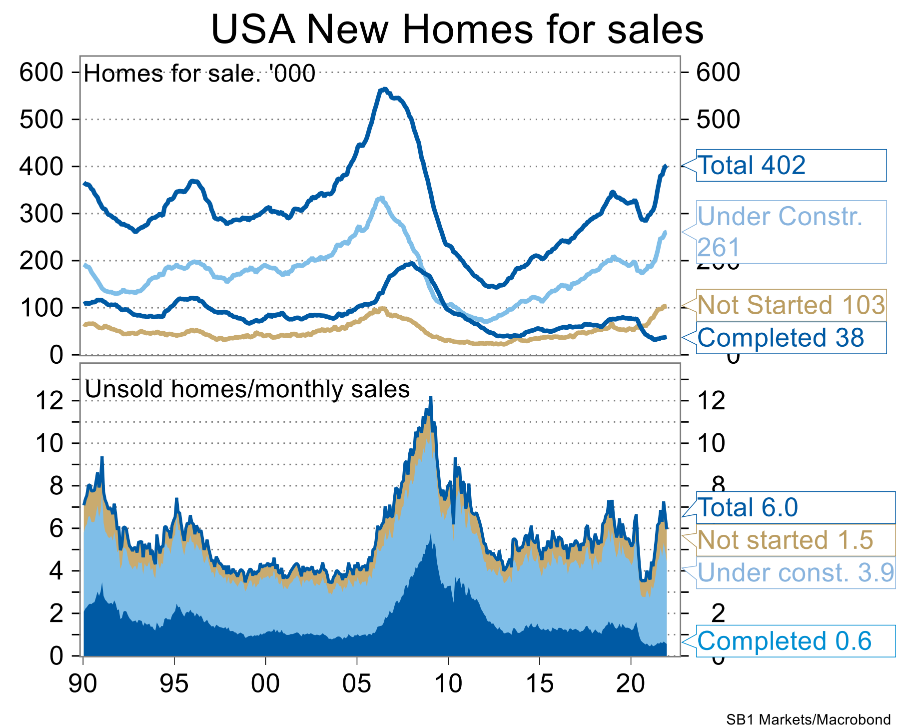


- UK is still close to a longer term 2% trajectory, while the US is well above
- The EMU price level is still hoovering around a 1% path but prices rose sharply in November
- The core Norwegian CPI is among the best behaved, now close to the 2% path, after being far above in 2020, when the NOK fell sharply

New home sales strengthened in December, above expectations

However, the inventory is growing rapidly, as the supply side has responded

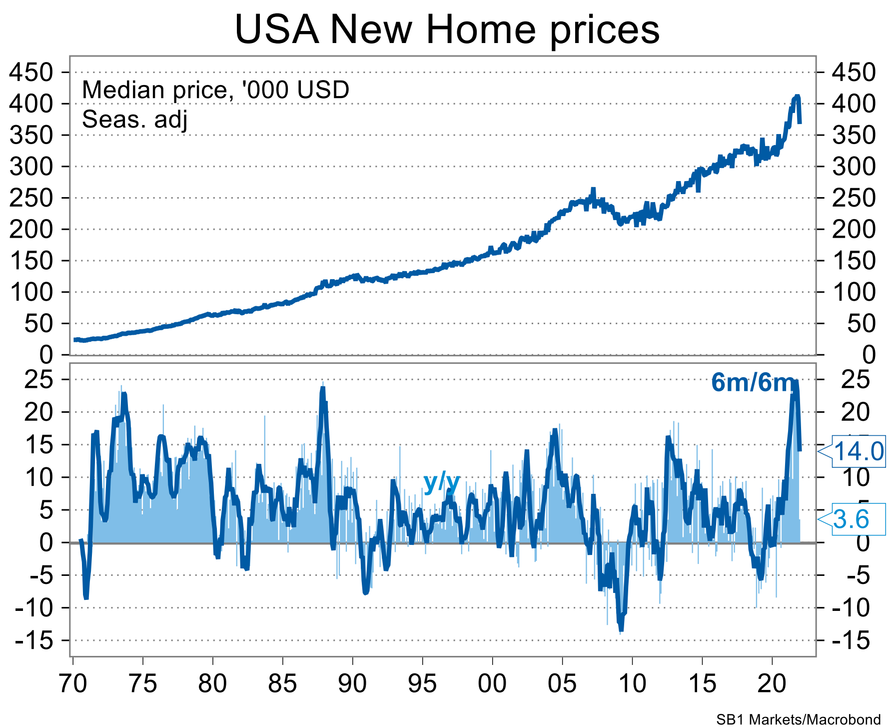


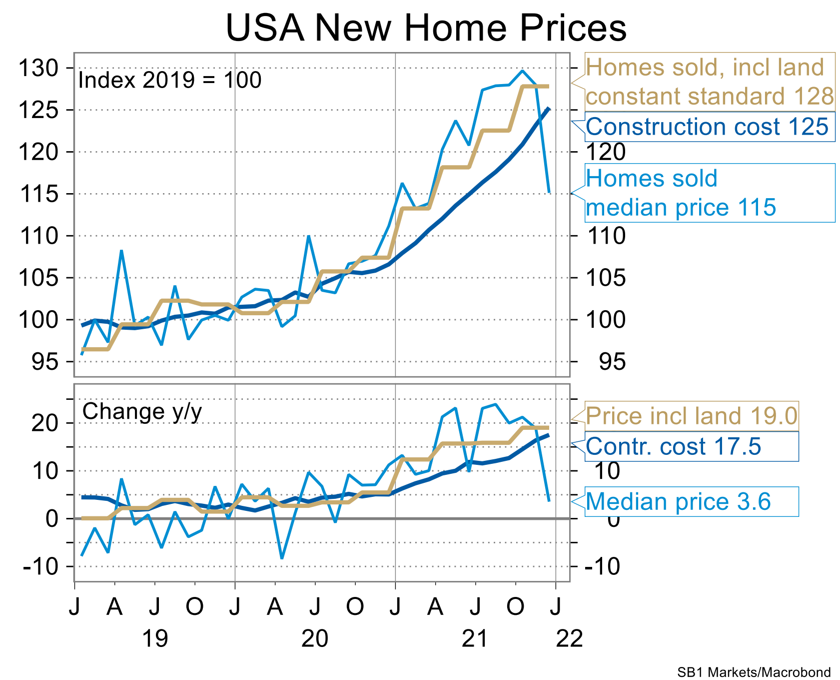


- **New single home sales rose to 811'** (annualised rate) in December – from a slightly downward revised 725' in Nov, and above the expected 757'. These monthly figures are often revised substantially and the last observation is close to useless – but now anyway better than expected
- **The big picture:** Following a 30% decline from January to June, sales were stable through H2 last year, at approx. the same level as before the pandemic – until the Dec hike. Sales have been somewhat lower than normal vs. new single home starts (in avg. sales are 70%+ below starts, as may homes are built by the homeowner)
- **The inventory of unsold homes** has increased by 43% since Oct 2020, and the level is the highest since Sept 2008. The inventory equals 6 months of sales, a bit higher than 'normal' – and up from the record low level at 3.5 months in Sept 2020
  - The increase in the inventory is not due to large increase in completed house for sale (the most 'effective' supply), and the inventory just equals 19 days of sale (half of a normal level). However, the no. of projects not yet started (but for sale) has doubled, to the highest number ever, and the no. of new homes for sales but which are still under construction has climbed rapidly, to the highest level since 2007. So, there are lot of homes in the pipeline, and clearly a confirmation that the supply side is responding to the steep increase in demand. At one stage, combined with higher mortgage rates, that could change the housing market outlook

New home prices fell in Dec but the trend is still up

Construction costs are up 17% y/y, selling prices 19%. Land prices are up even more, demand is strong

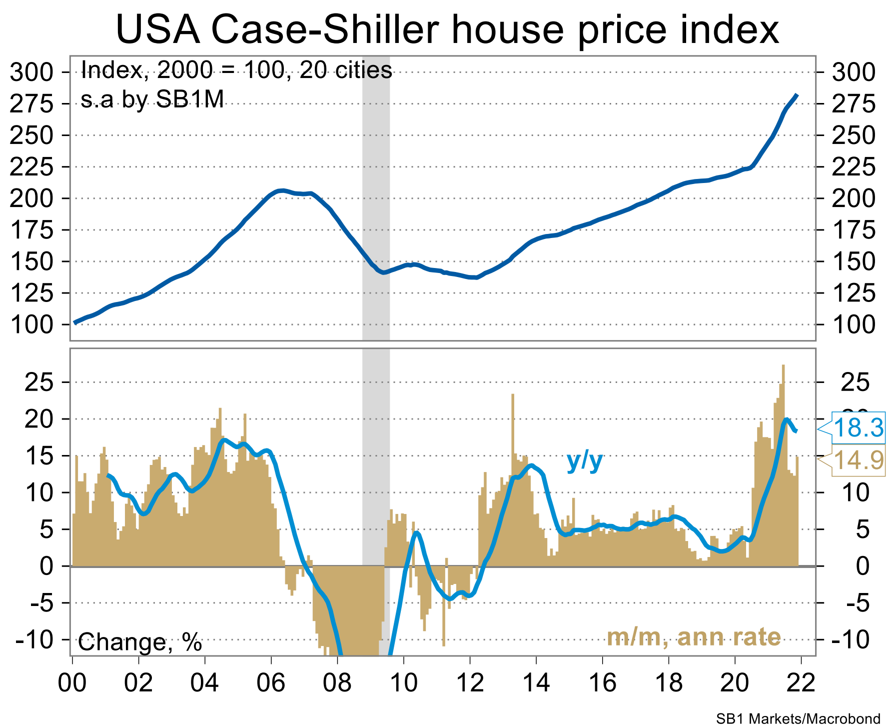


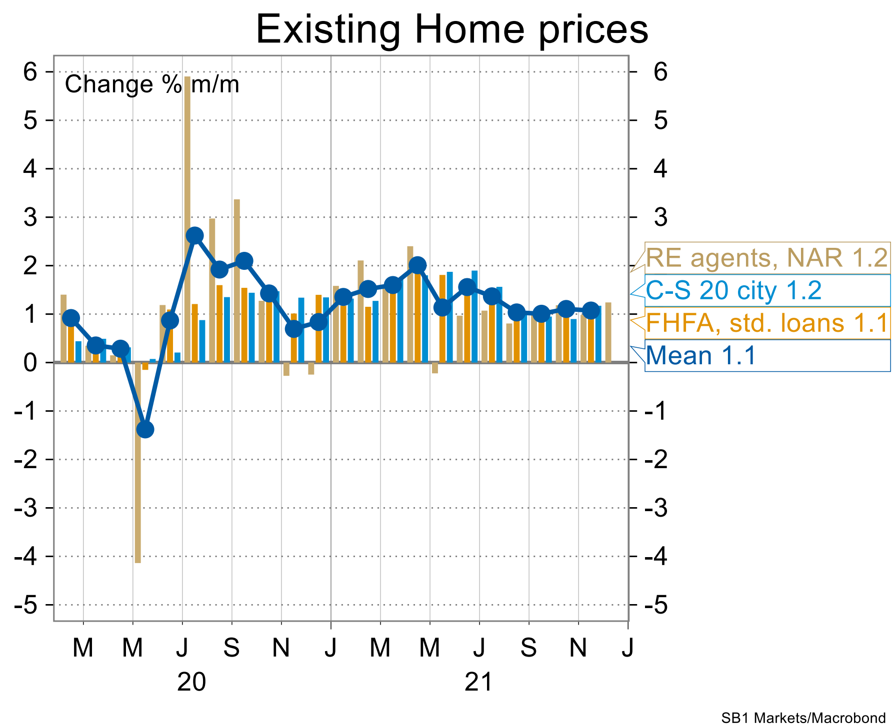


- Monthly **median new home sales prices** are volatile, and in Dec prices fell by 10% m/m (!), which no doubt is not 'for real' but just due to changes in the mix of the homes sold this month. The underlying price appreciation is still strong
- The **construction price index** is adjusted for changes in standard & size, as is the **new homes sold price index**, which also includes cost of land, and they are up by 17,5% and 19% resp., measured y/y in Dec/Q4
  - As prices including land are still up more than the construction cost index (which of course is influenced by higher material costs), which implies an even faster increase in land prices. Thus, demand must be the main driver for the hike in prices, not the construction cost (if demand was weak due to high prices, prices including land would have climbed less than construction costs)

House prices inflation remains strong, 16 – 19% y/y. Prices are up 30% vs. pre-p

The Case/Shiller index gained 1.2% m/m (14% annualised), and the annual rate is 18.3%!

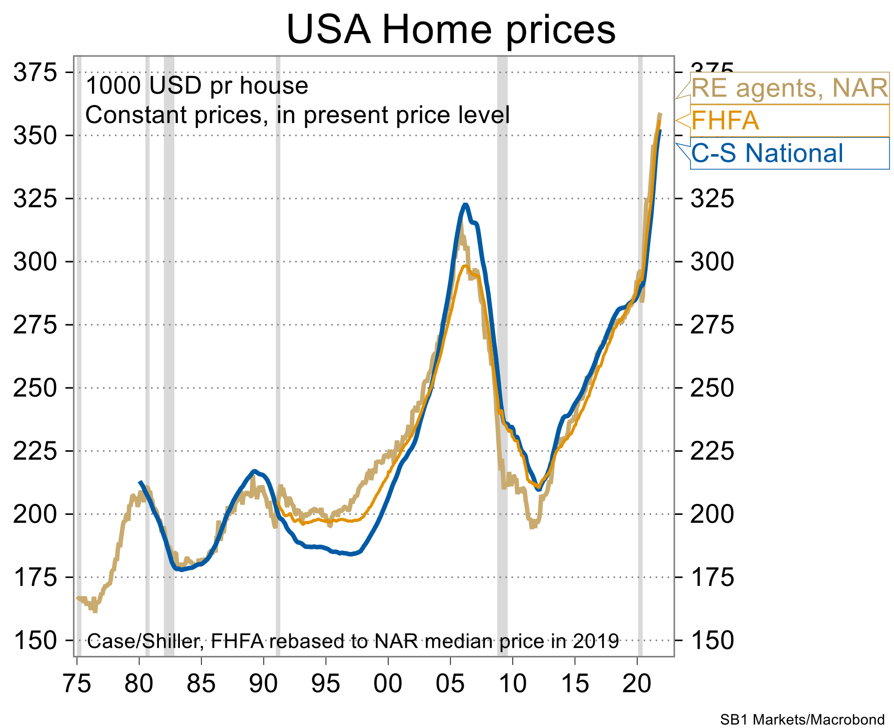


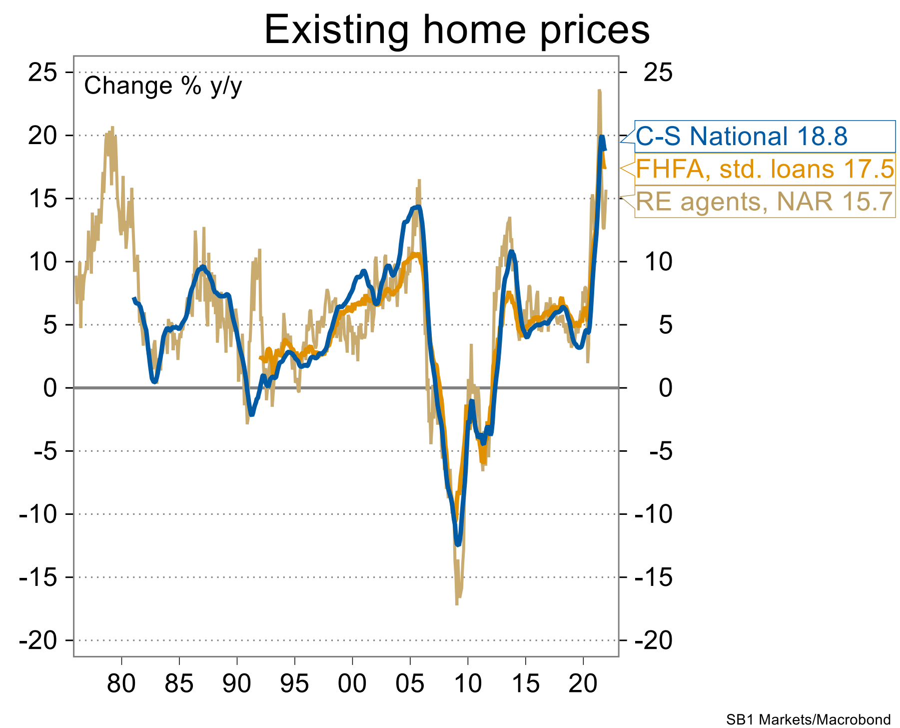


- **S&P's Case/Shiller's 20 cities** price index rose 1.2% m/m in November (Oct – Dec avg), equalling a 14.9% annualised pace, up from 0.9% in Oct. The annual growth rate was 18.3%, down 0.1 pp, expected 18.2%. In July prices were up 20.0%, the highest growth rate since just after WWII. The **national C-S index** is up 18.8% y/y. <u>Prices are up 28% since before the pandemic</u>
- **The FHFA** (Federal Housing Financing Agency) price index, which covers homes with loans guarantied by the government sponsored Fannie Mae or Freddie Mac ("Husbankene", has a countrywide coverage), rose 1.1% in Nov, and are up 17.5% y/y. The ATH annual rate before the pandemic surge was 11%, ahead of the housing crisis 15 years ago (chart next page)
- **Relators** reported a 1.2% price lift m/m in December, and the annual rate is 15.7%

Some special house data – both measured y/y & the real price level

Real prices are now 10 – 20% above the pre-financial crisis level

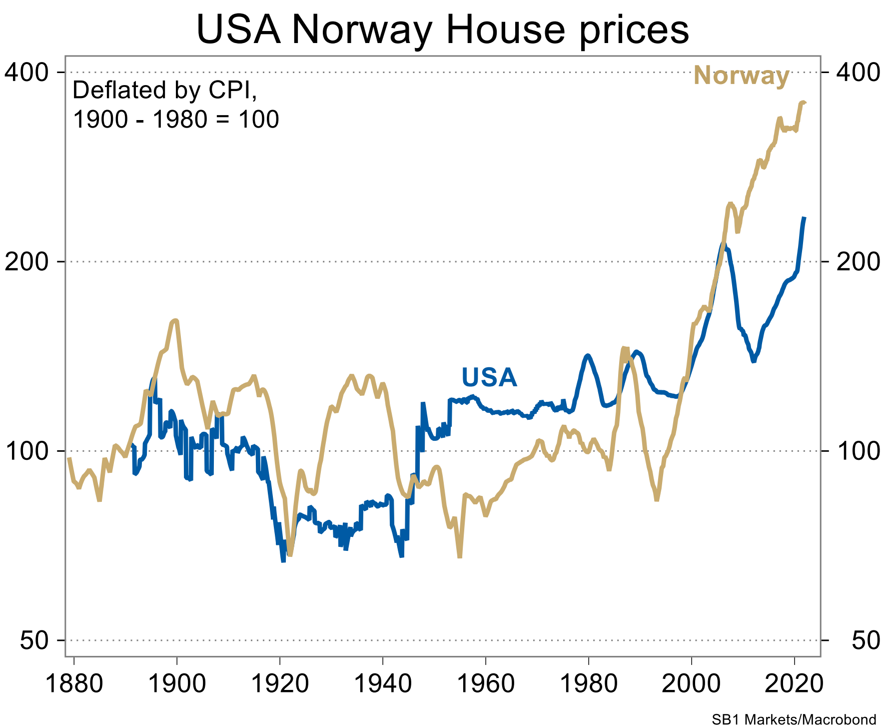


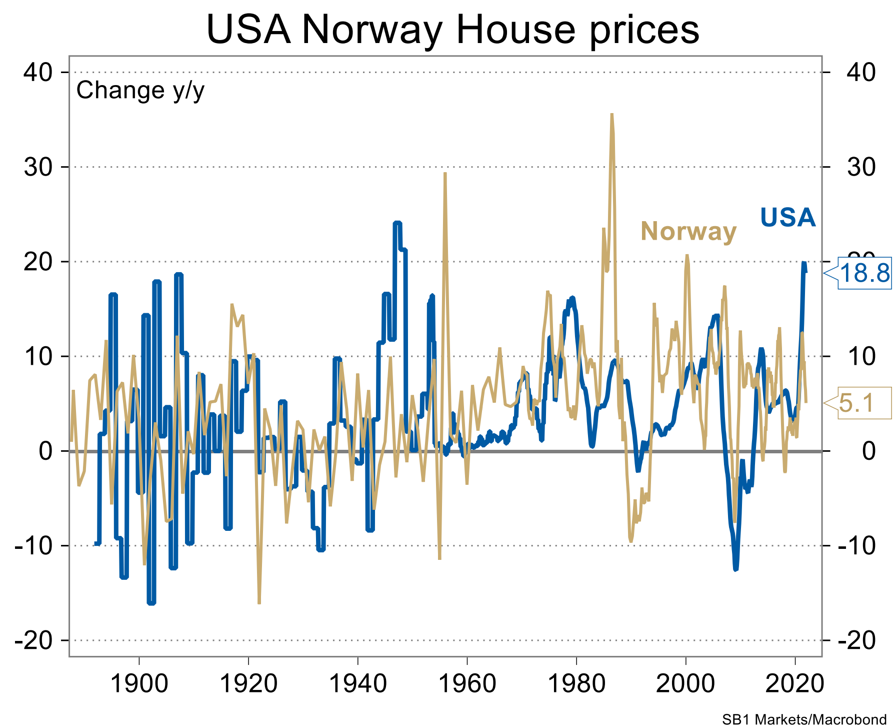


- Both the Case-Shiller National index, FHFA's index for homes with government sponsored mortgages (which includes most homes), and the realtors' price index reported the highest house price appreciation ever (or since 1948) during last year
- Real prices are far above the 2006 peak
- There are still some big differences vs the mid 2000 housing bubble
  - Housing starts are at a lower level. The inventory of 2nd homes for sale is record low (vs high 15 – 16 years ago. However, the inventory of new homes for sale is climbing rapidly
  - The debt/income ratio has fallen sharply since the peak before the financial crisis. However, credit growth has accelerated during the pandemic
  - The savings rate/net financial investment has now fallen to below the pre-pandemic level– but the ratios are far above the level in 2005

For the record

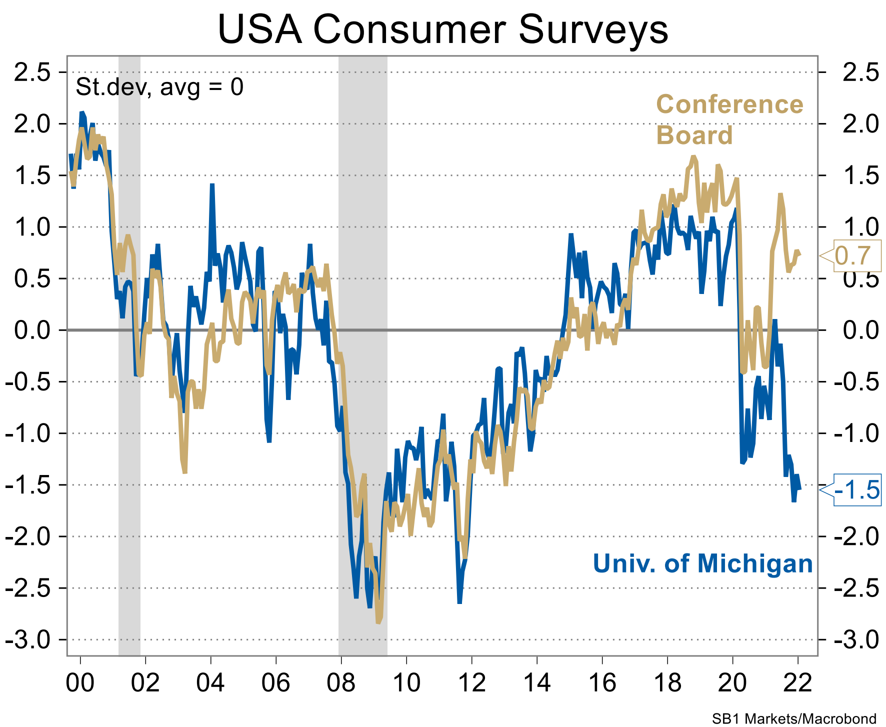
Some entertaining house price charts





Conference Board's confidence slightly down in Jan but miles above the UM surv.

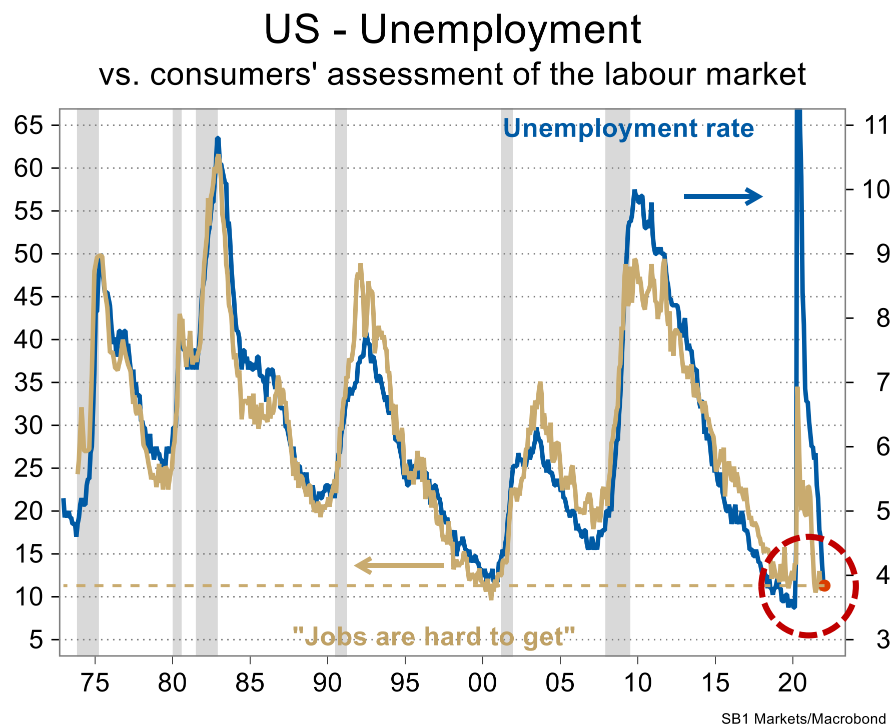
CB's index up 0.2 st.dev to +0.8, better than expected and miles above the Univ of Mich sentiment

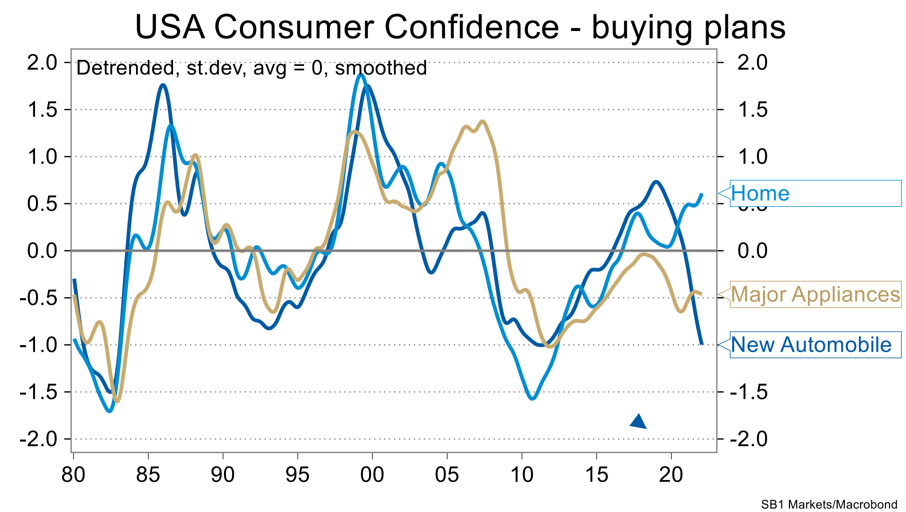


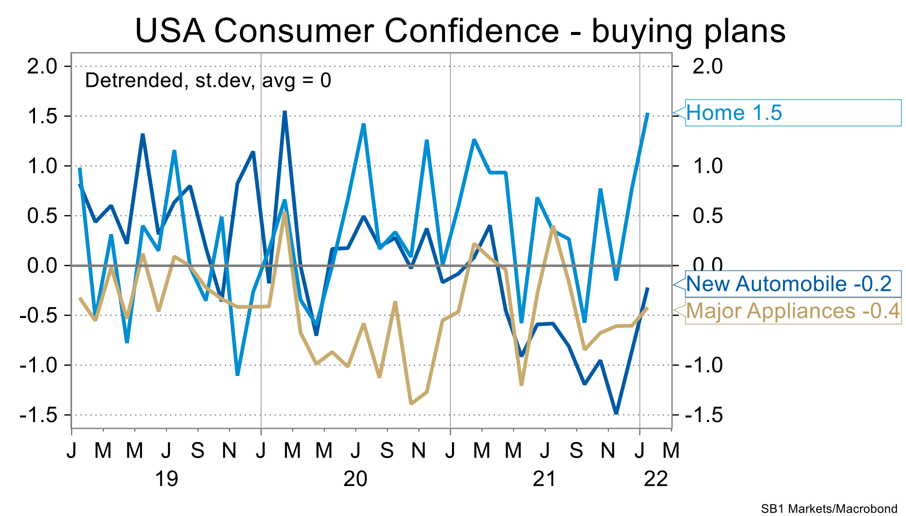
- The **Conference Board's consumer confidence** index lost 1.4 p to 113.8 in January, expected down to 111.7. The index is 0.7 st.dev above average (down 0.1). There were small changes in both the assessment of the current situation, and expectations
  - » Households still report a tight labour market, and they adjusted their spending plans upwards in January, home buying plans are now the most upbeat in years
- **University of Michigan's sentiment** survey is still way below a normal level, at -1.5 st.dev – even weaker than during the first wave of virus outbreak last spring
  - » If the UM survey is falling faster than CBs survey, often something unfortunate happens afterwards, check next page

Jobs are very easy to get, buying plans revised up, even for buying a car

Home buying plans best in years, even if mortgage rates are on the way up. The economy is OK?



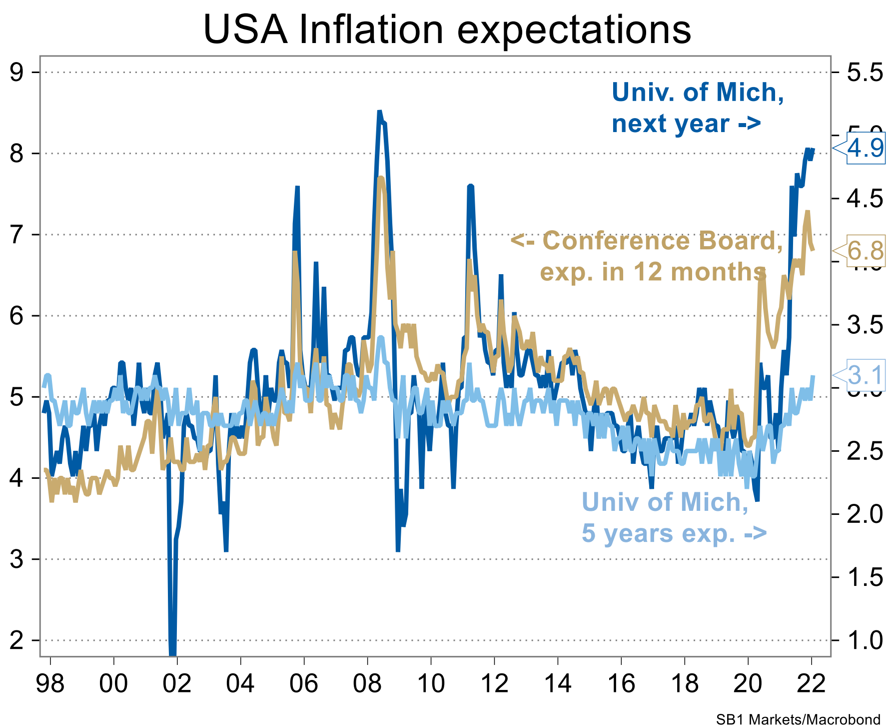




- Household spending plans are volatile, and in sum not aggressive – but in Dec and Jan home buying plans climbed sharply, to the best level in years - even if mortgage rates were on the way up!
  - » Plans for buying a new cars are still lower than normal, for good reasons – but recovered in Dec and Jan

Inflation expectations are well above normal levels, especially the short term

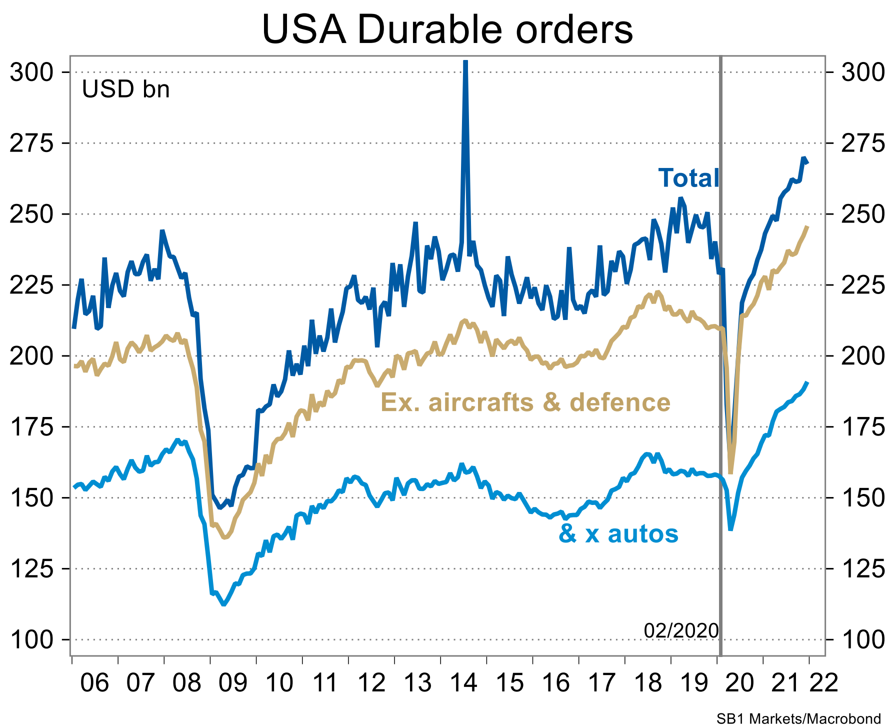
Long term expectations are up but are not that high – and short term expectations fell in Dec & Jan

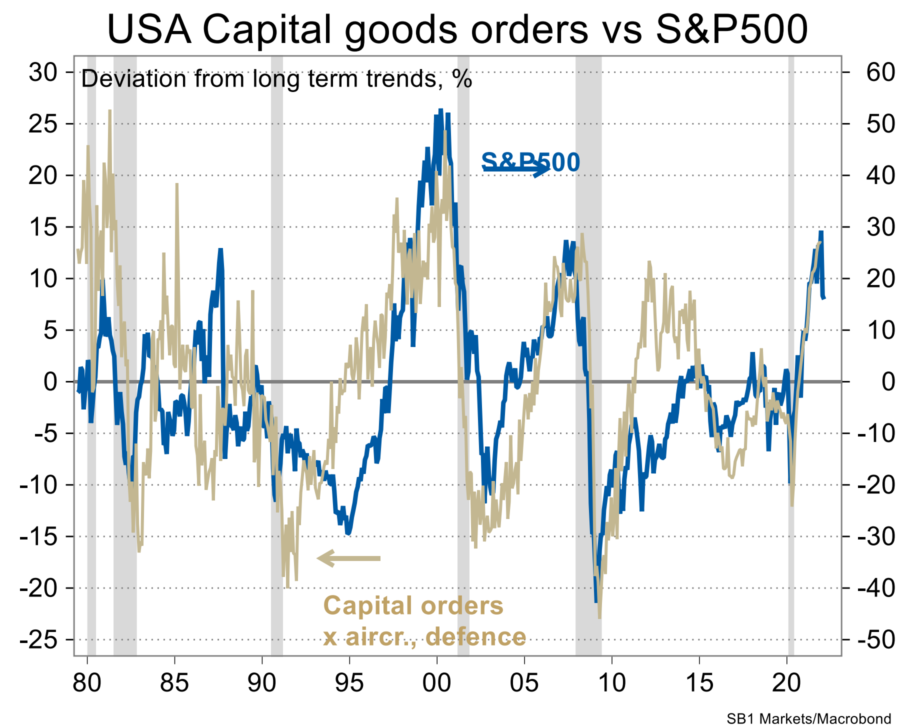


- … at least according to Conference Board

Strong order inflow in December too

However, investment orders may be slowing somewhat

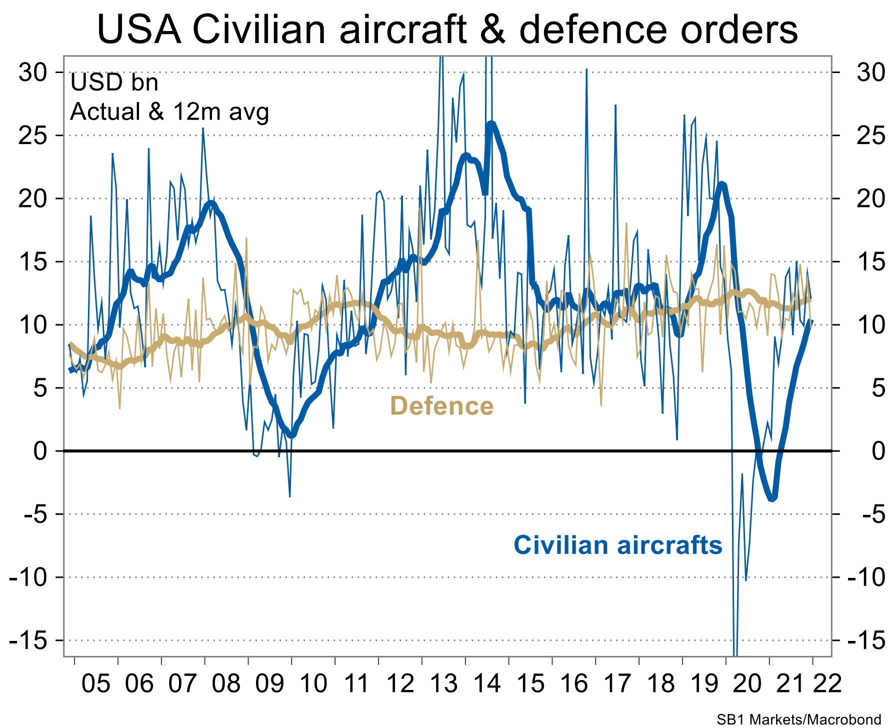


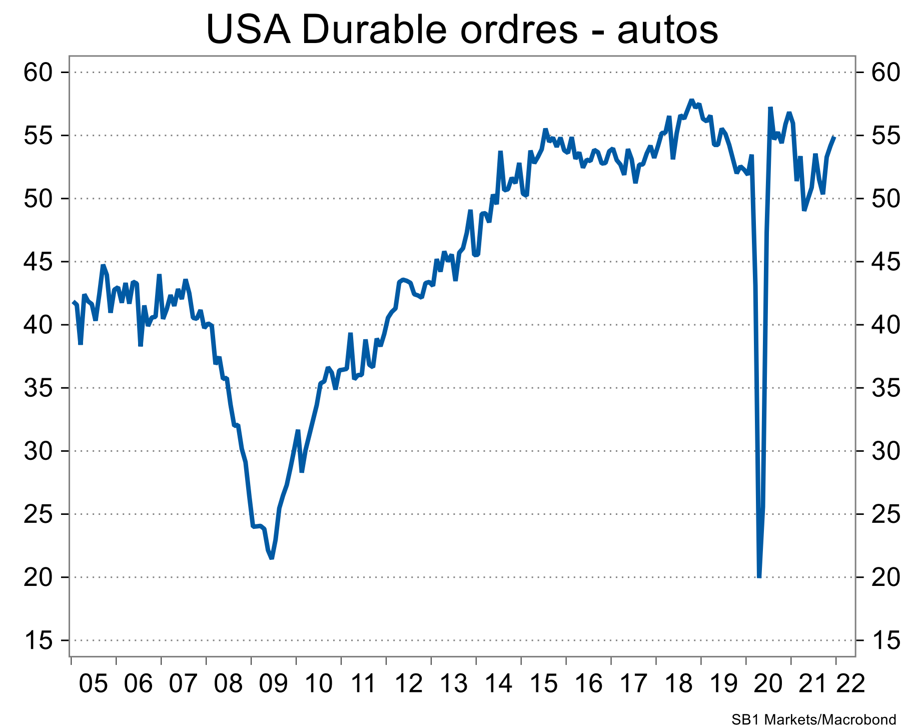


- **Total durable** orders fell by 0.9% in December, expected down 0.5%. Both the volatile aircraft & defence orders declined
  - » Ex these two components, the ‘core’ rose by 1.4%, well above expectations – and the trend is strong
  - » Auto orders rose too, but ‘core x autos continued upwards
- **Core <u>investment</u> goods orders** were up 0.6%, and the trend is still straight up
- **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 & defence orders down in October

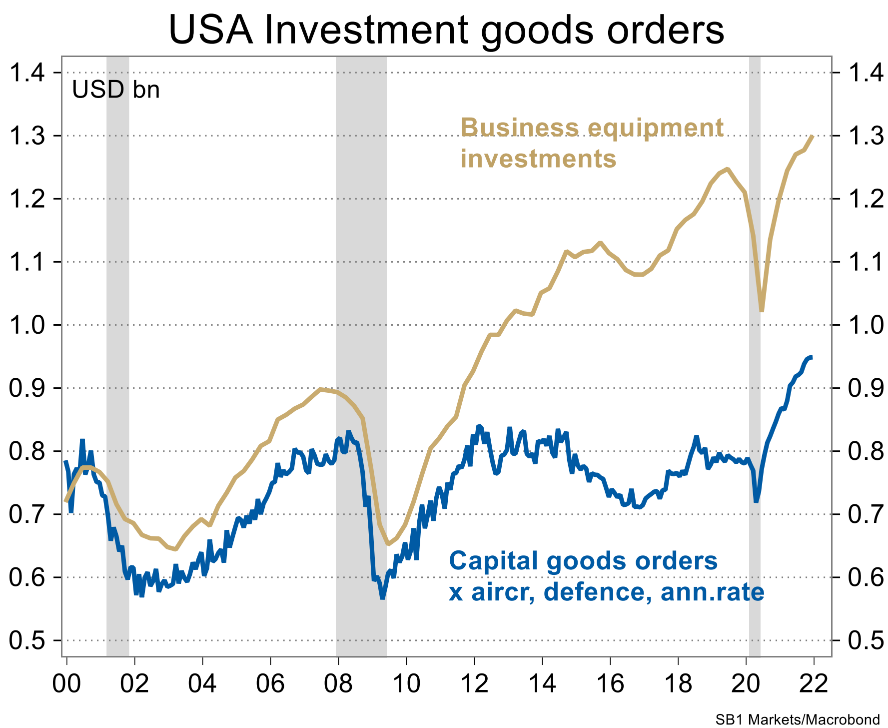
... while auto orders rose – and they are not at low level!

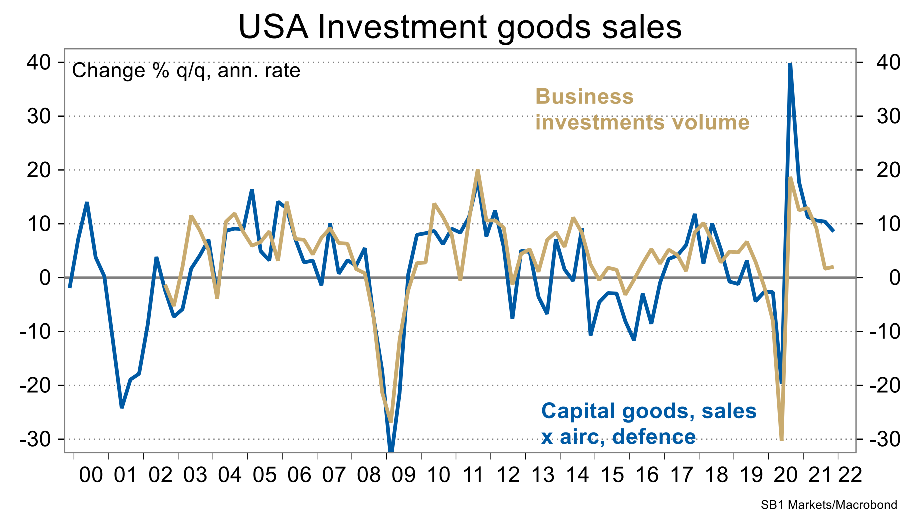


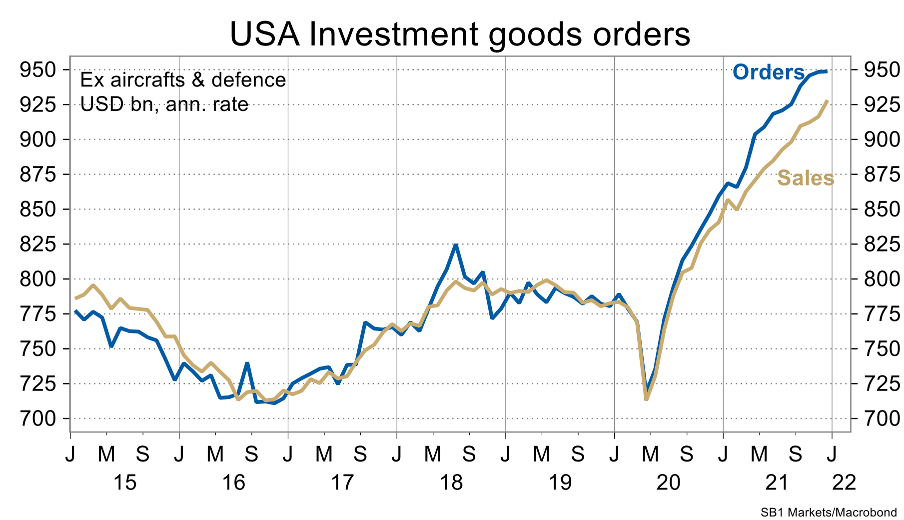


Core capital orders are still going strong

Signal decent growth in business investments into Q4 following a weak Q3



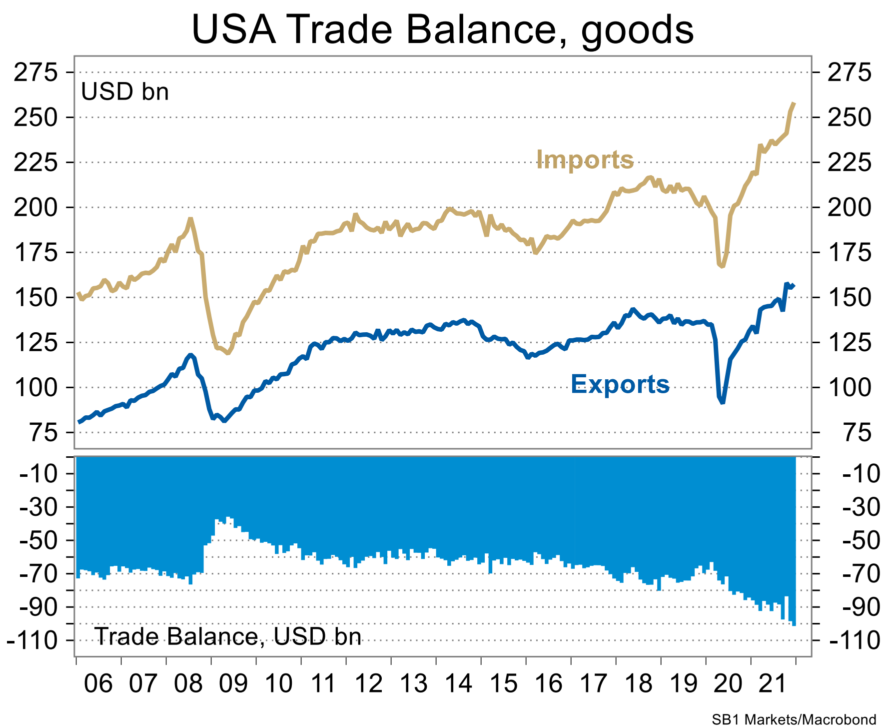


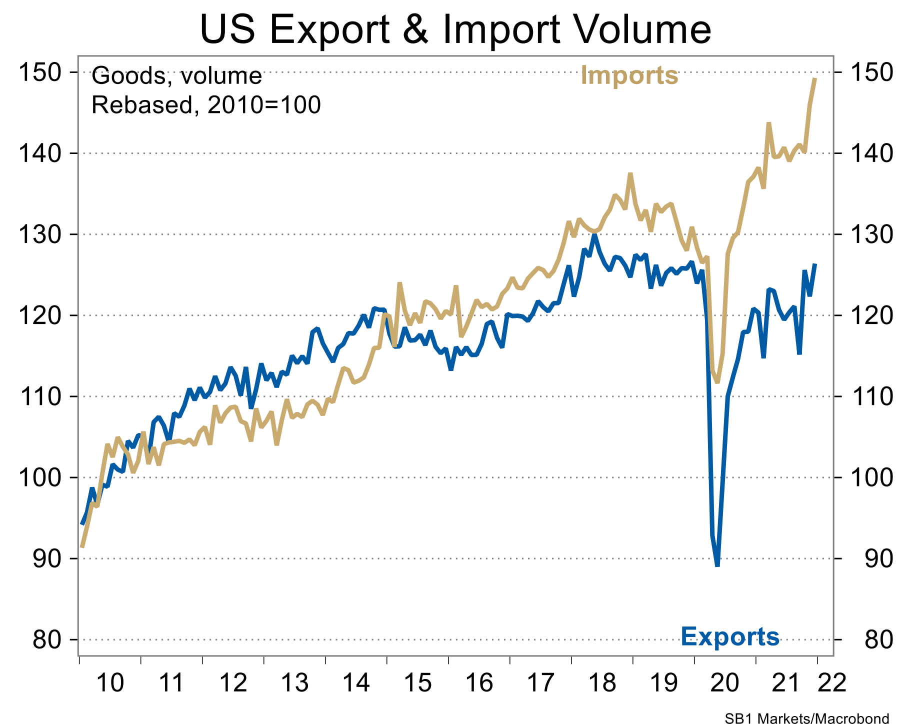


- **Core (x aircraft, defence) capital goods orders** were flat in Dec, and growth has slowed recent months. Still, the 3m/3m rate is at 9%. Shipments were up 1.3%. A decent growth in business investments is signalled (following a rather slow growth in Q3 and Q4)
- **The business investment** level is well above the pre-pandemic level – and not at low vs. a reasonable long term trend (see more data, comments here)

Another ATH trade deficit in goods, imports are climbing rapidly

Imports rose in both nominal and real terms in Dec, exports fell following the Oct surge

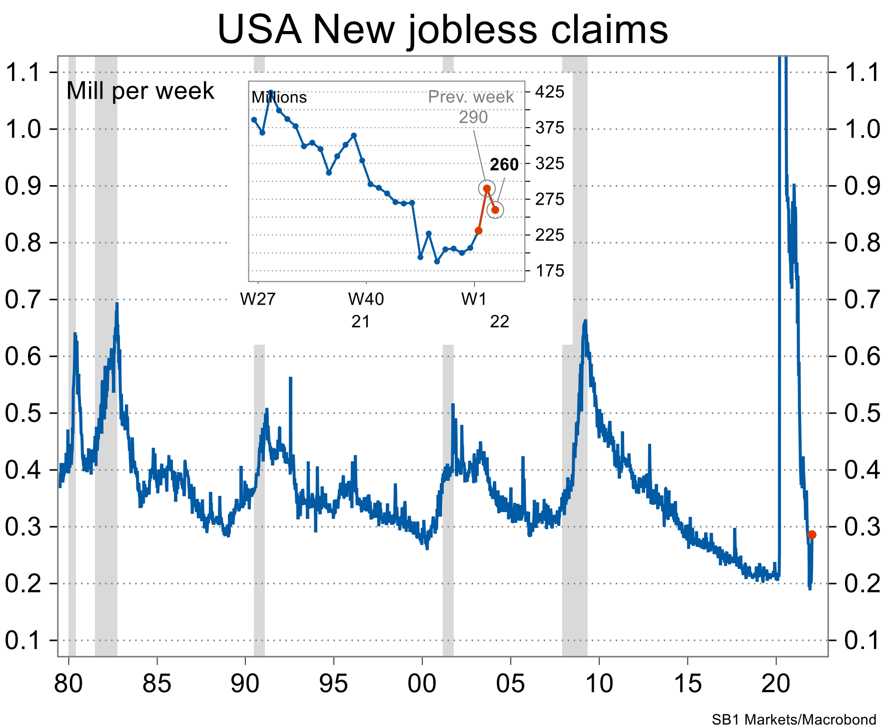


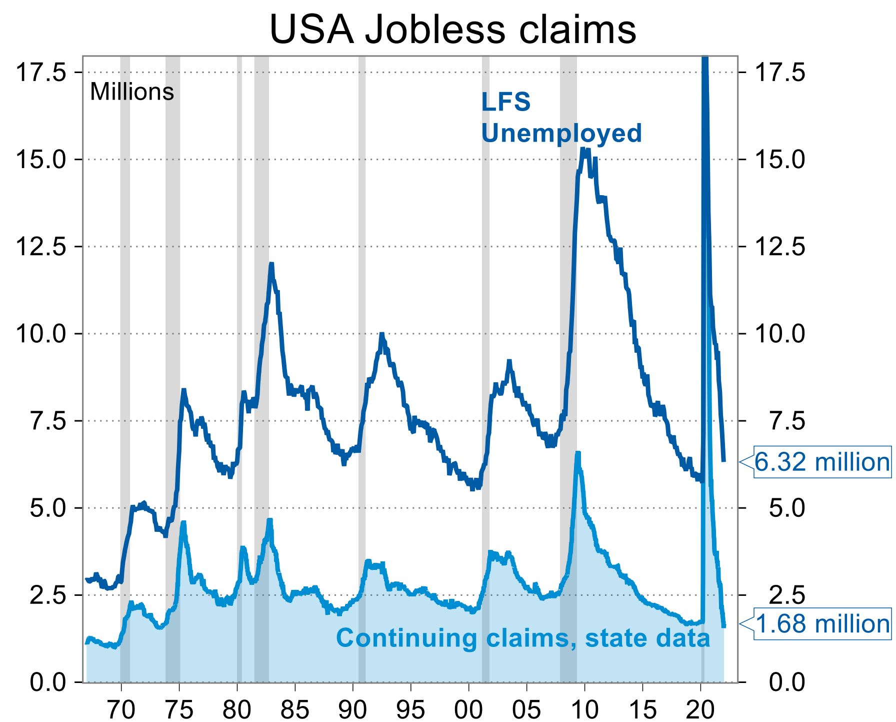


- **Imports** of goods rose by 2% m/m in value terms in Dec, and is almost 30% above the Feb 2020 level
  - » In volume terms imports also rose 2%, and are up 15% above the pre-pandemic level! Demand for goods has been strong during the pandemic, driving imports – even if auto imports have been low. We expect US households' demand for goods to slow the coming quarters, from the present very high level – dampening demand for imports too
- **Exports** of goods added 1% in Dec and are up 15% vs the pre-pandemic level
  - » Export volumes are still below the pre-pandemic level
- **The trade deficit** in goods shot up to USD 101 bn (first time above the 100 line), from 98 bn

Jobless claims down last week, still higher than late last year

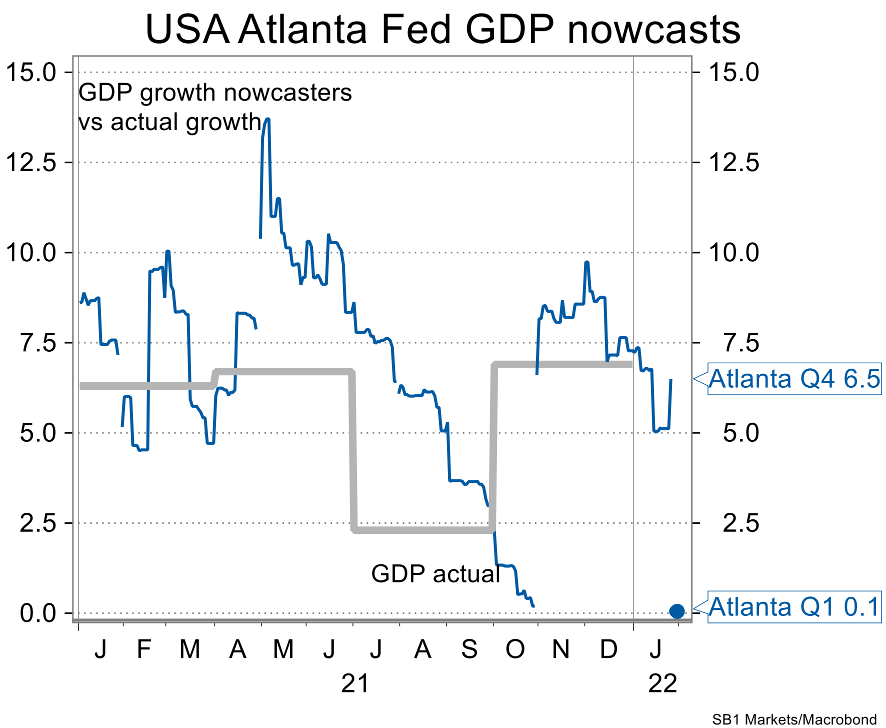
Some more are staying in dole too. Even so, the level for both is low

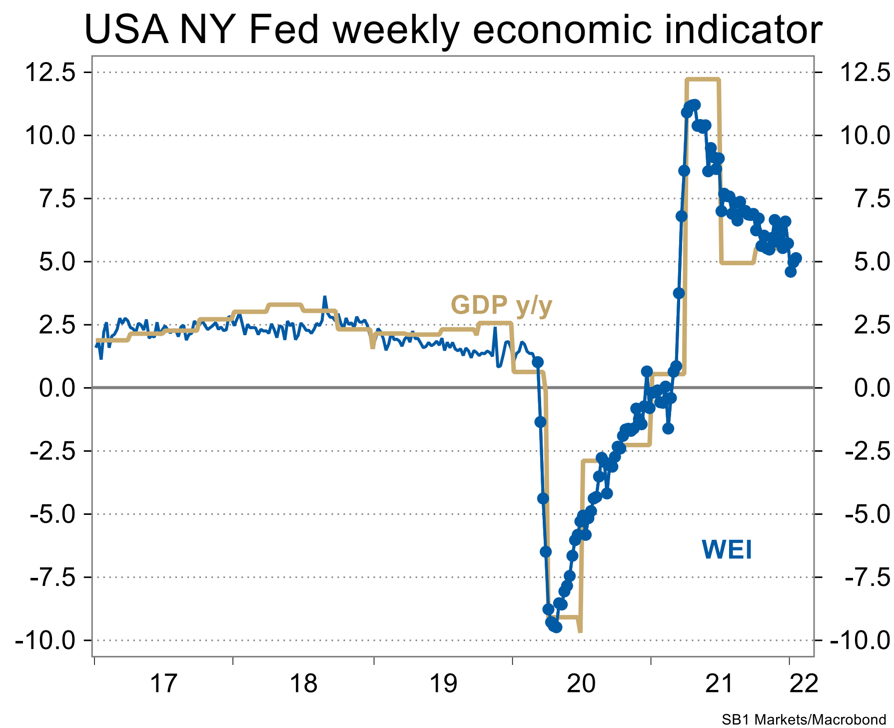




- **New jobless claims** declined to 260’ in week 3 from 290’ the previous week. The level is still low but above the 200’ level late last year
- **Ordinary continuing claims** rose by 51’ in week 2, to 1.68 mill. The level is still close to the lowest since 1973!
- The increase in **new & continued claims** may of course signal some ‘real’ trouble at the labour market but most likely some temporary disturbances, like the impact of the omicron variant

Atlanta Fed's nowcaster suggest close to zero growth in Q1, in the first estimate

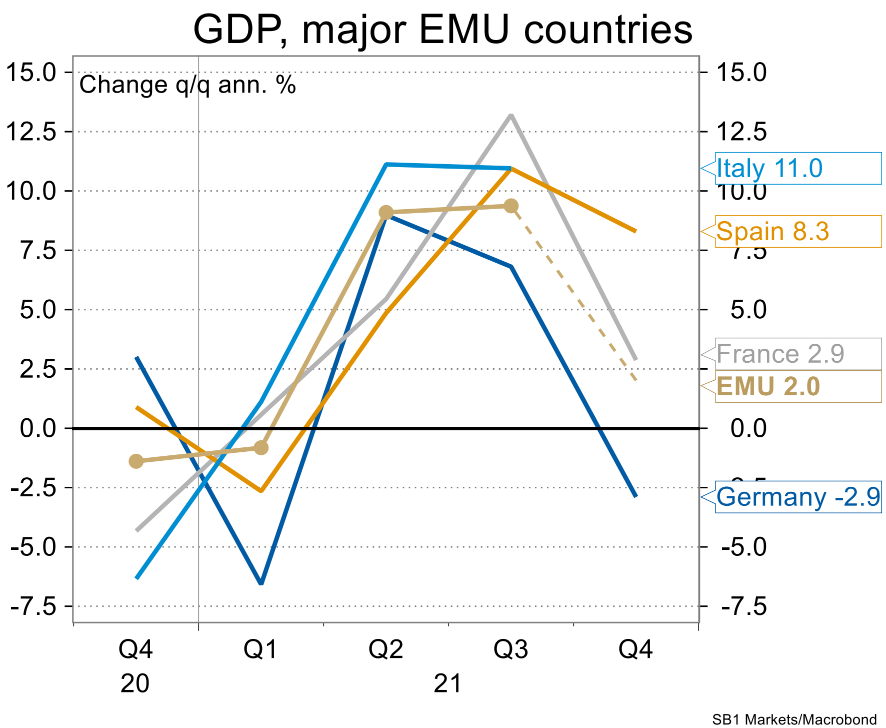


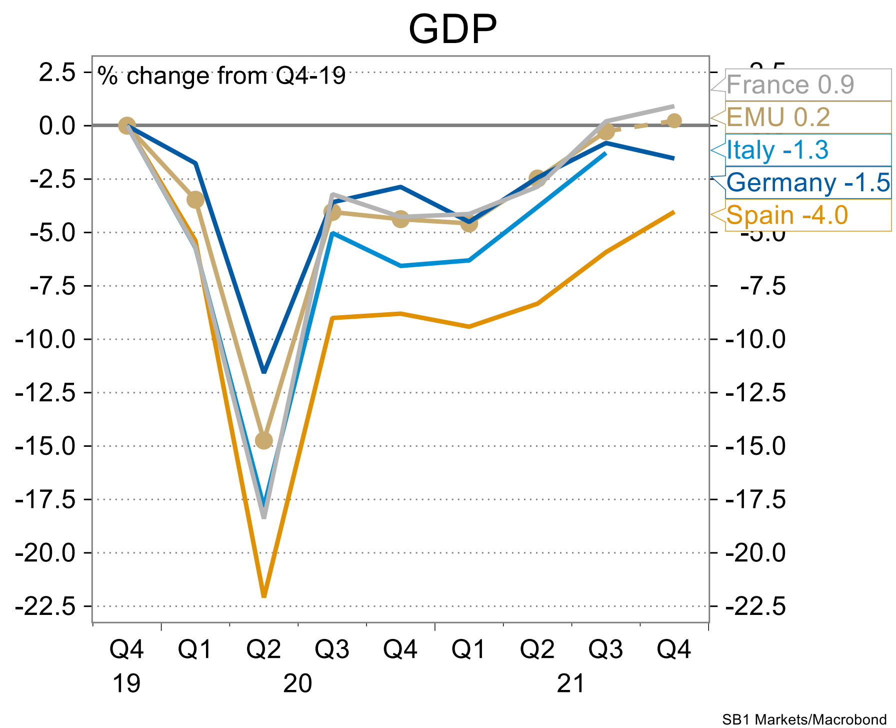


SpareBank 1 MARKETS

GDP slowed in France and Spain, fell in Germany

Italy has not yet reported. Spain remain far below the pre-pandemic level – Germany too

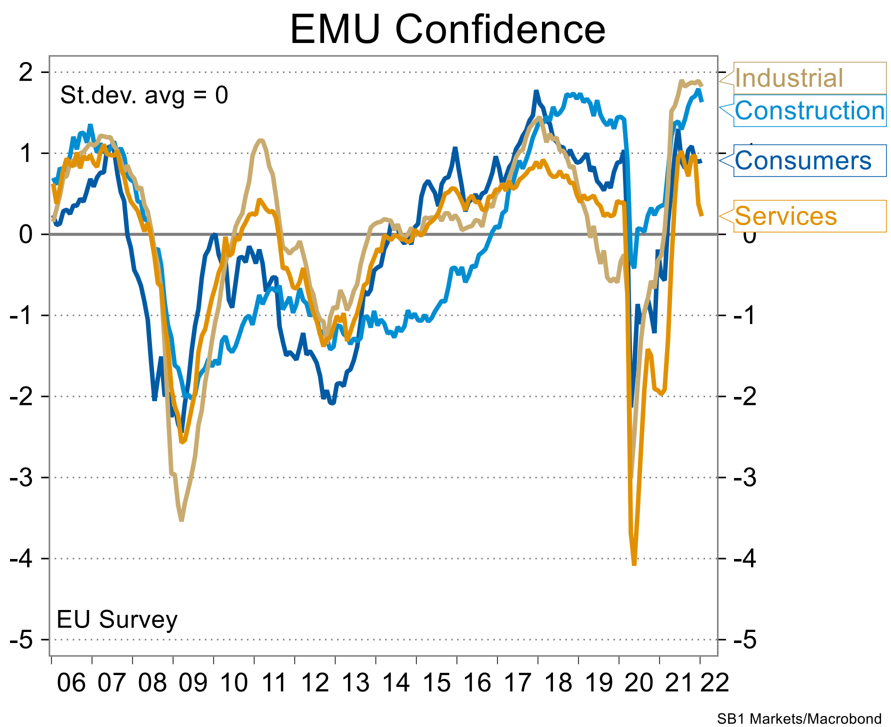


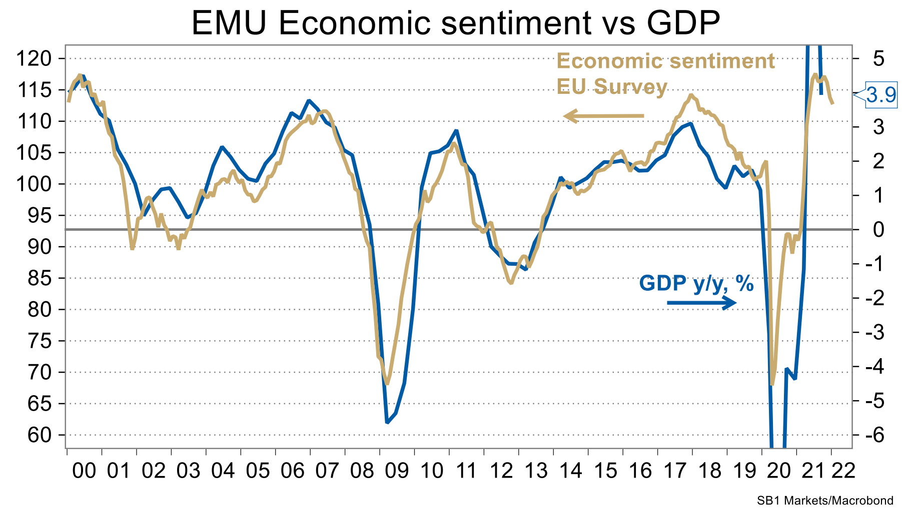


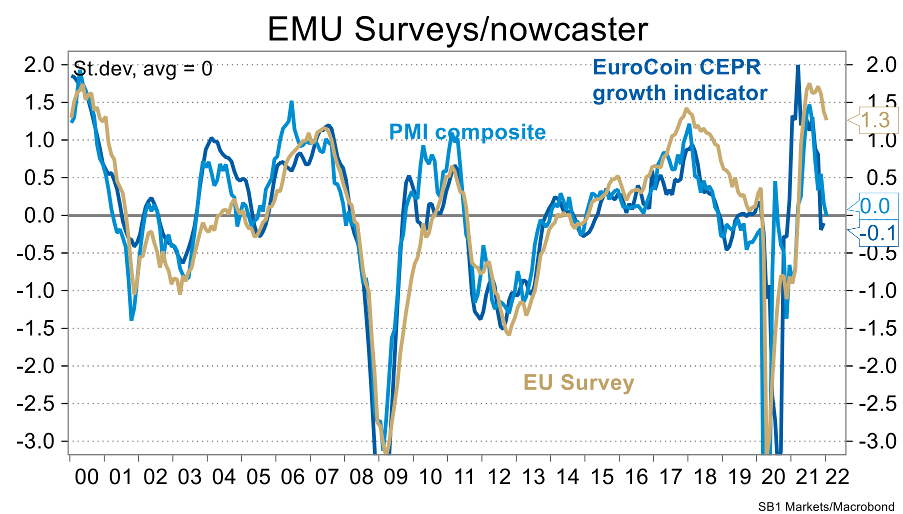
- GDP grew at a brisk pace in **Spain**, and not much down from Q3 (8.3% vs. 11%). GDP is still down 4% vs. Q4-19
- **France** slowed sharply to 2.9%, expected 2%. The level is down 0.9% vs. Q4-19
- **Germany** contracted by 2.9% (0.7% not annualised, in line with Bundesbank estimate two weeks ago). Level is down 1.5% vs Q4-19
- **Italy** (and the smaller) countries have not yet reported Q4 data
- We estimate a 2% growth pace (0.5%) for the whole **EMU region** . If so, GDP will finally cross the Q4-19, by 0.2 pp

Services are reporting a further slowdown in Jan but growth remains above avg

EMU economic sentiment fell 0.1 st.dev, but remains 1.3 above avg, signalling 3.5% growth





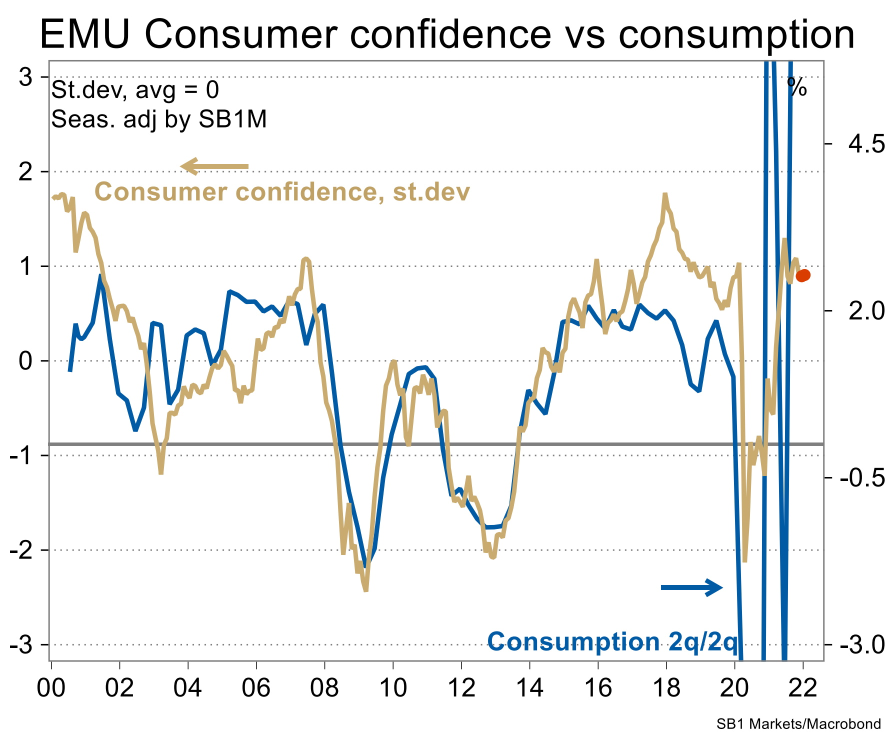


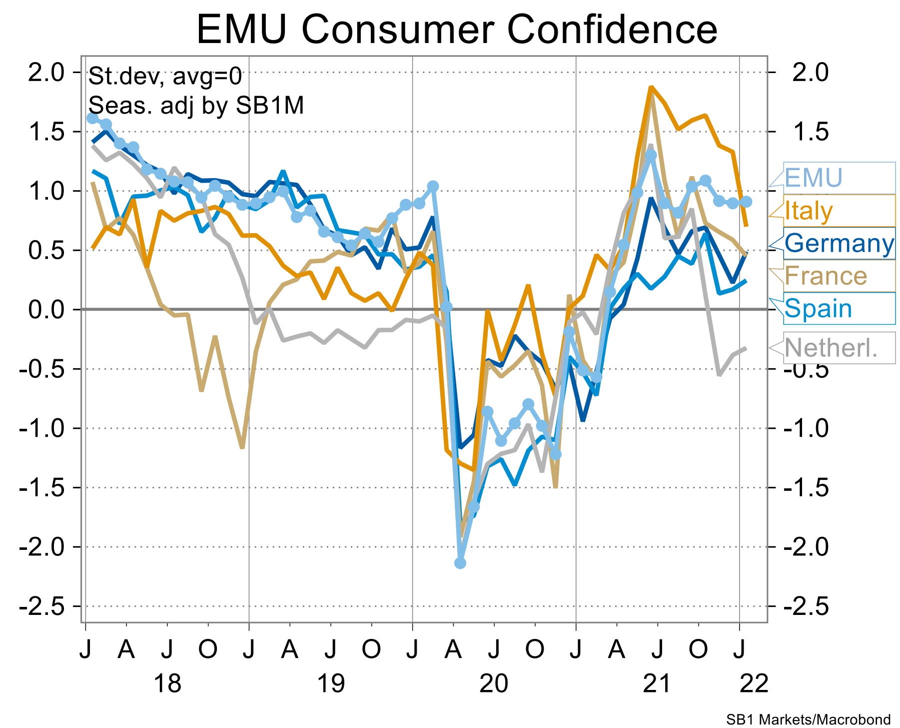
- **EU's confidence survey for the Euro area** declined 1.1 p to 112.7 in Jan, from a 1.5 p downward revised level in Dec, expected 114.5. The level equals 1.3 st.dev above average, signalling a GDP growth well above average, at 3 - 4 %
  - » **All sectors** are signalling above average growth, even if the
  - » **Service sector** index fell further
  - » **Industry and construction** confidence both fell marginally from ATH
- The **EuroCOIN GDP nowcaster** signals far slower growth than EUs survey, as do the PMI reports – in average trend growth (1 – 1.5%)

SpareBank 1 MARKETS

The fight against the virus has not brought consumer confidence down

The level is 0.9 st.dev above average – and stronger than before the pandemic

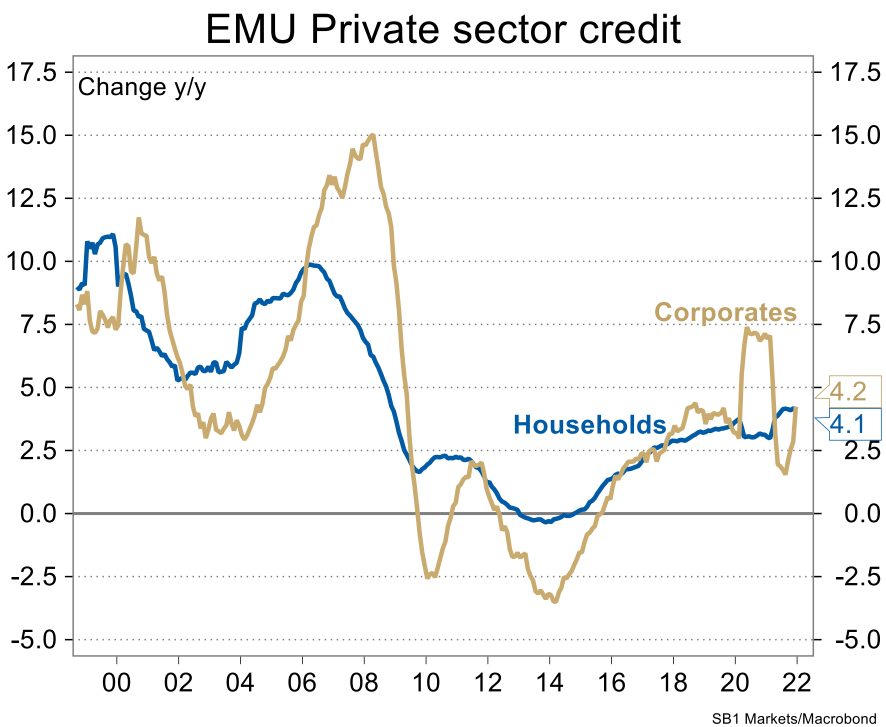


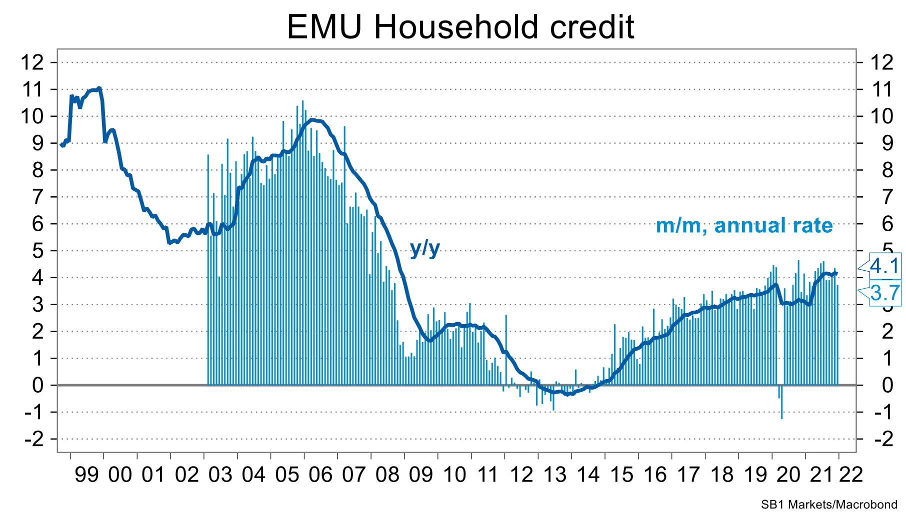


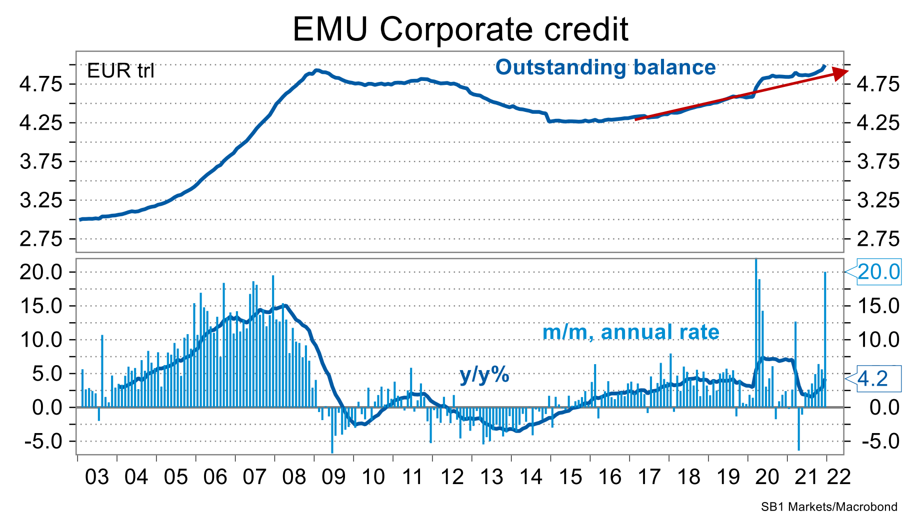
SpareBank 1 MARKETS

Some life in corporate borrowing recent months, household debt up 4%+

Household debt is not accelerating – no credit boom to be seen



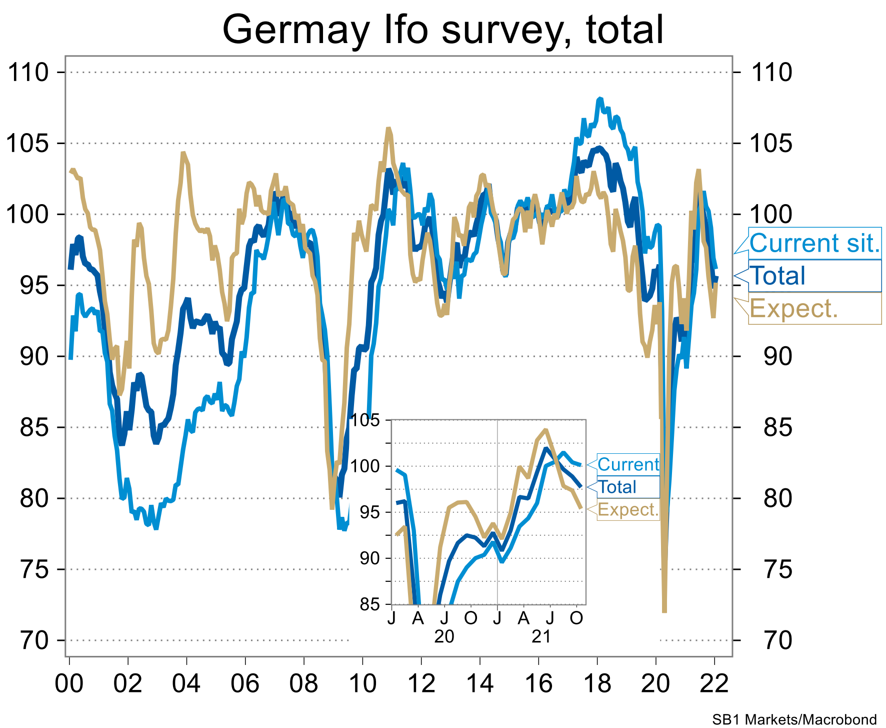




- The corporate debt level is still above the pre-pandemic trend growth path, and growth is now gaining some speed from month to month, with a substantial lift in Dec, very likely a one-off
  - » The average growth over the past 2 years is 3.6%
  - » The credit volume is not higher than in 2008 in nominal terms – and sharply down in real terms or in % of GDP

Ifo expectations bottomed in December, a small uptick in January

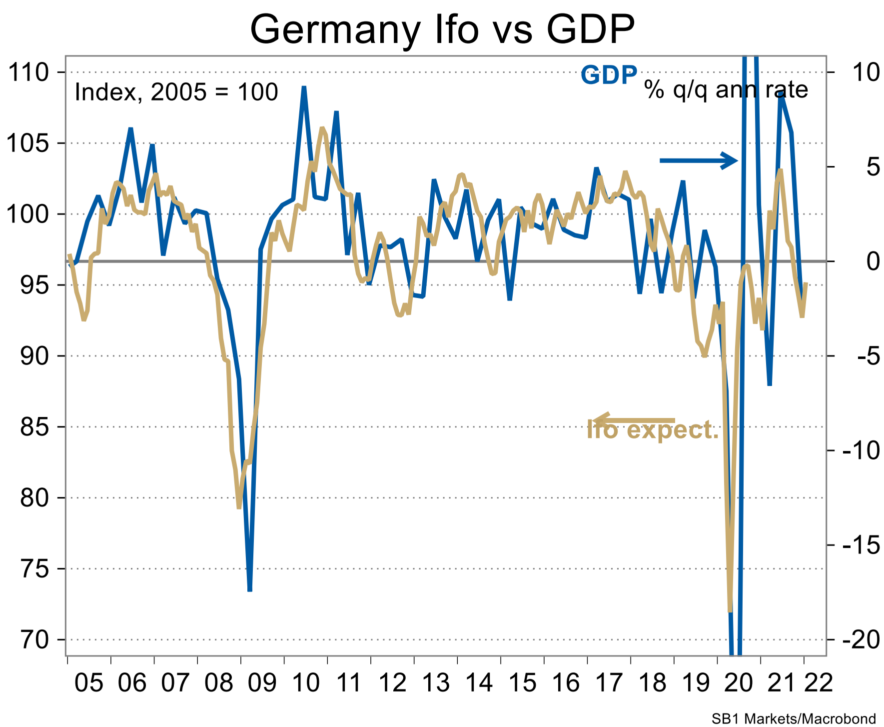
All sectors lifted their outlook in January, just services report growth below par

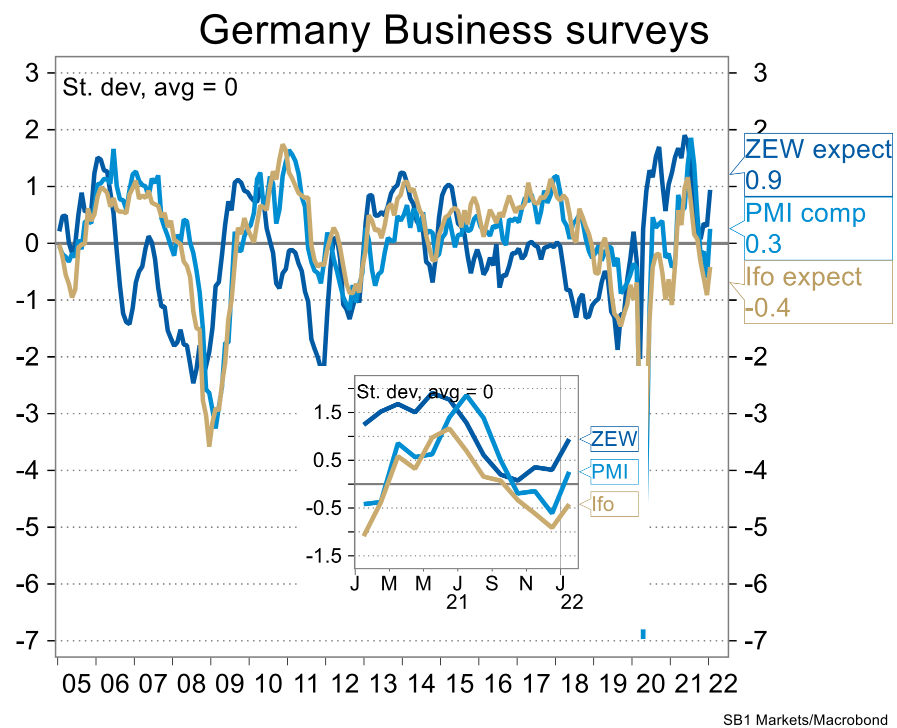


- **The expectation index** rose to 95.2 in Jan from 92.6 in Nov, expected up to 93.0
- The **assessment of the current situation** fell further, by 0.8 p to 96.1, as expected

By and large, surveys signal growth slightly close to trend

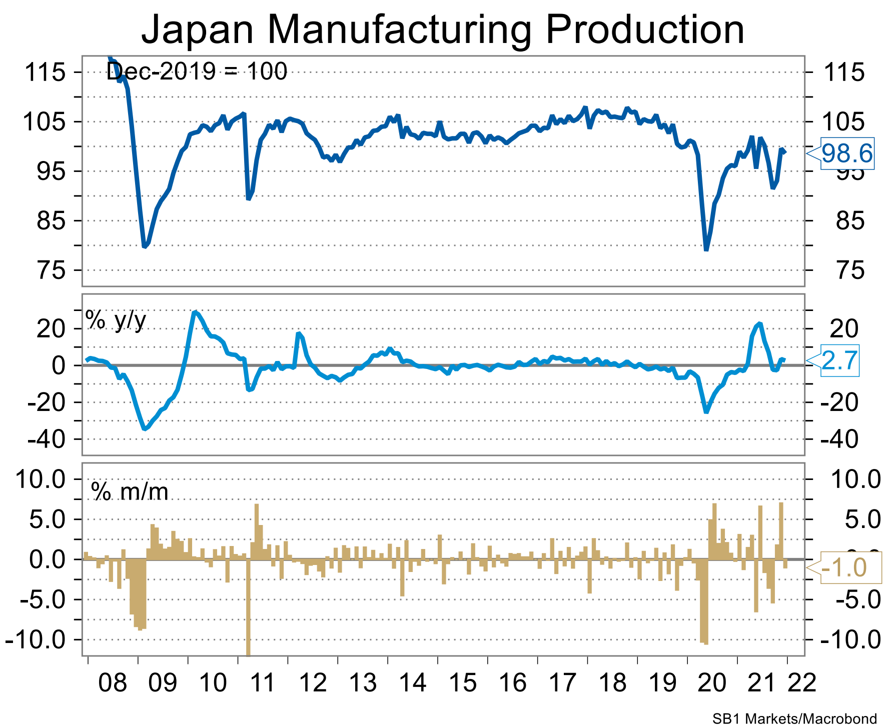
.. But they all turned up in January

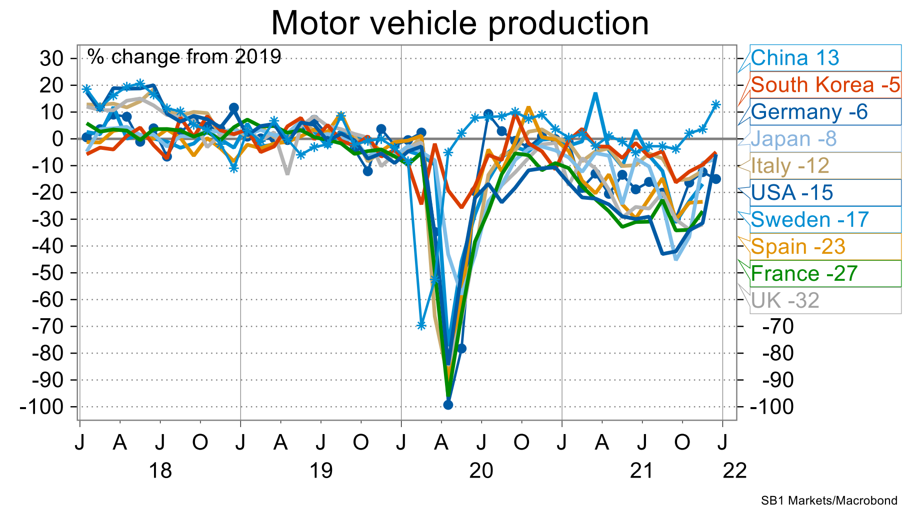


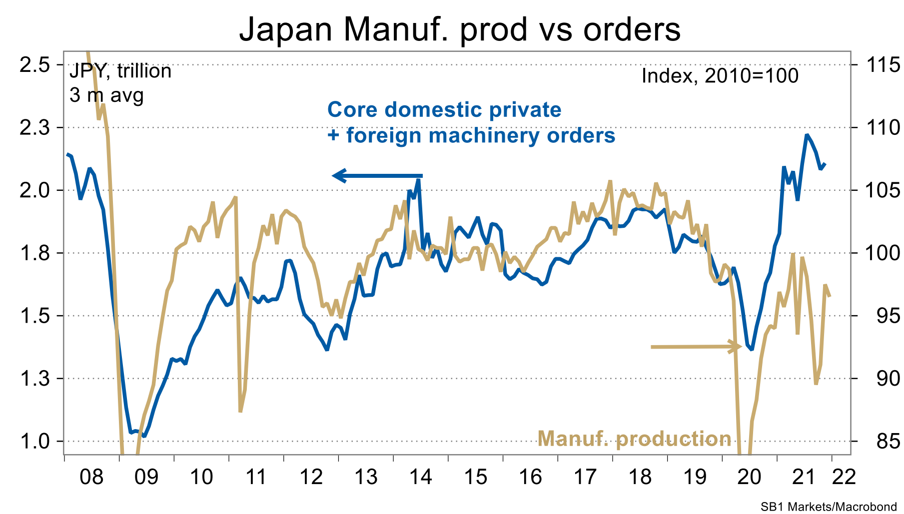


Manufacturing production down 1.0 m/m in Dec. expected -0.6%

Production is 1.4% below a low level in Dec-19



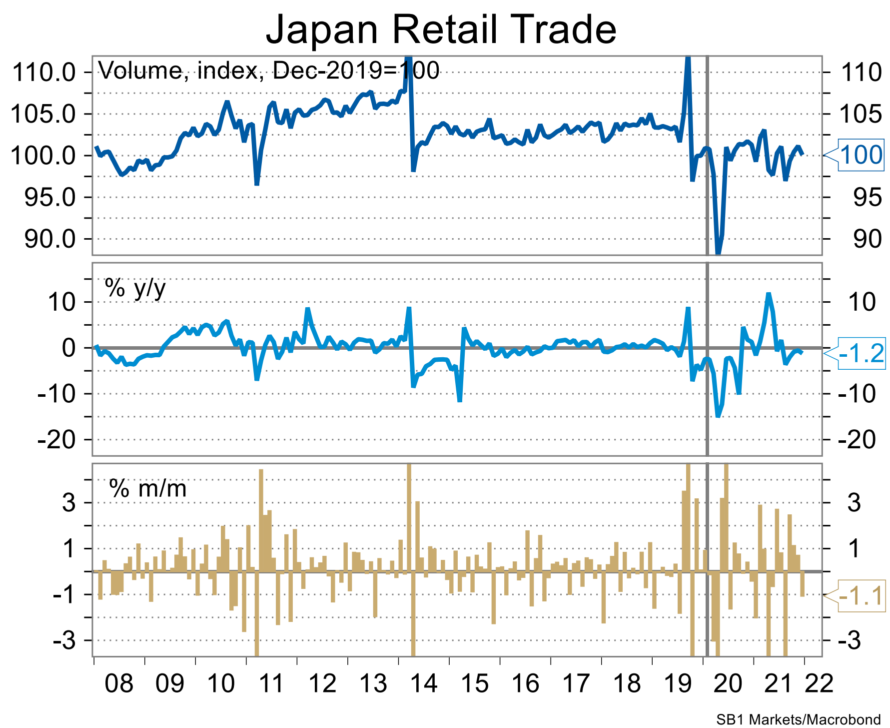


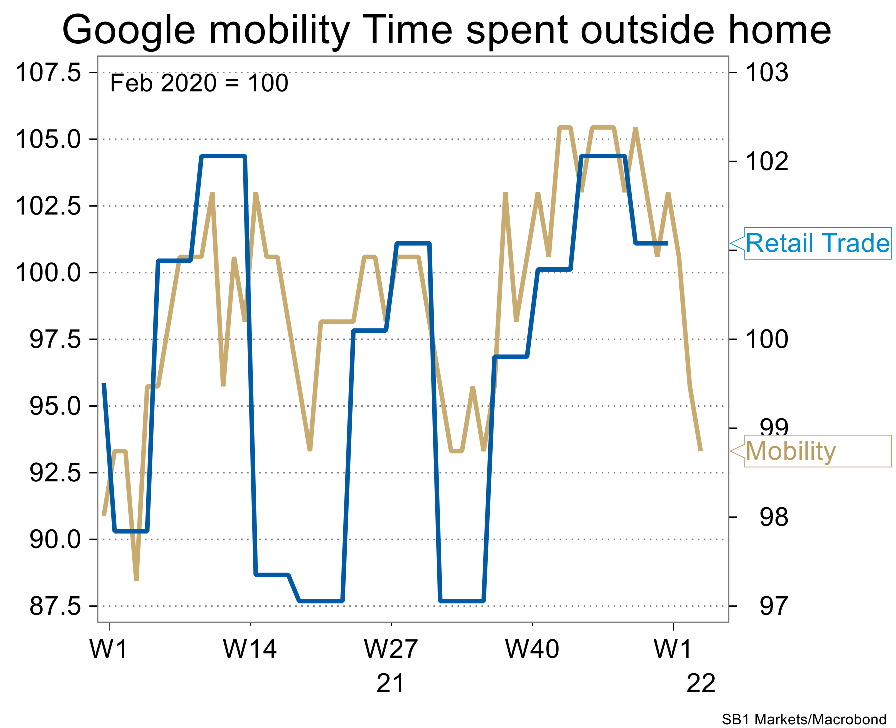


- **Motor vehicle production** was almost half the normal level in September, rose significantly in October, and then surged 44% to just 9% below the 2019 level in November – and it was -8% in Dec
  - » However, auto producers are still reporting serious lack of components og production below par the coming months
- **Overall order inflow** has strengthened substantially through 2021, and signals a much higher production level than the present

Retail sales further down 1.1% in Dec – and more to come in January?

Sales are om par with the pre-pandemic level – which was rather weak

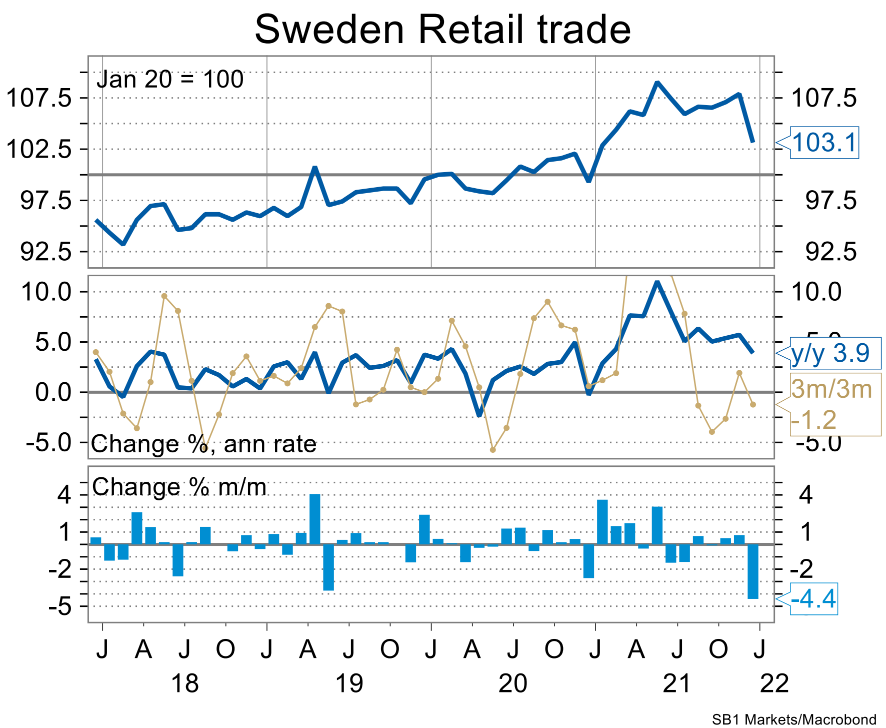


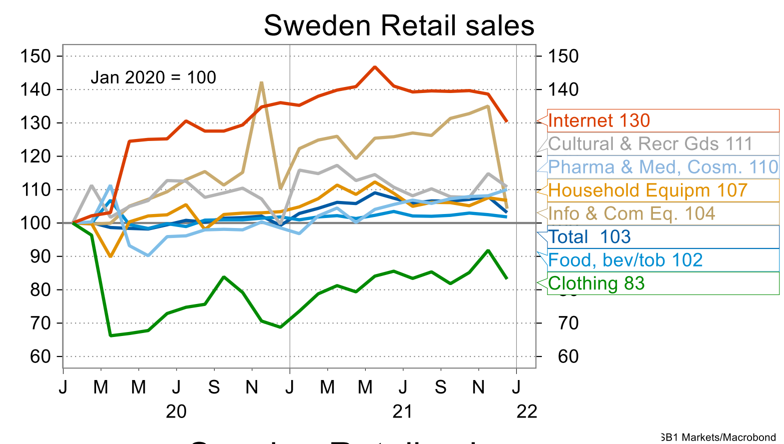


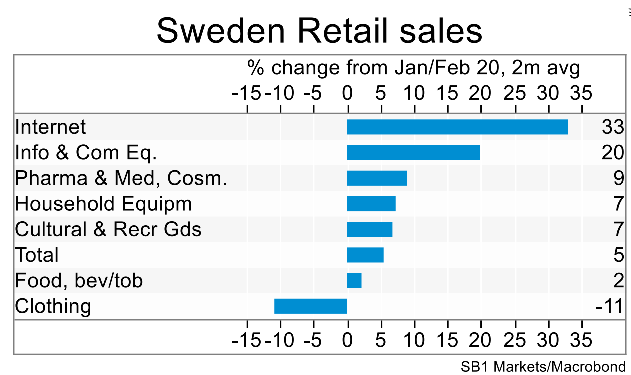
- **Retail sales** in Nov was revised down some 0.4% - and growth in Dec was 1.4% lower than expected
- **Mobility** has fallen sharply in Jan, during the Omicron wave – and retail sales have tended to follow mobility

Retail sales down 4.4% in Dec, just out of the blue (like in Norway)

A broad decline in sales, info & communication equipment down by 23%, clothing 10%



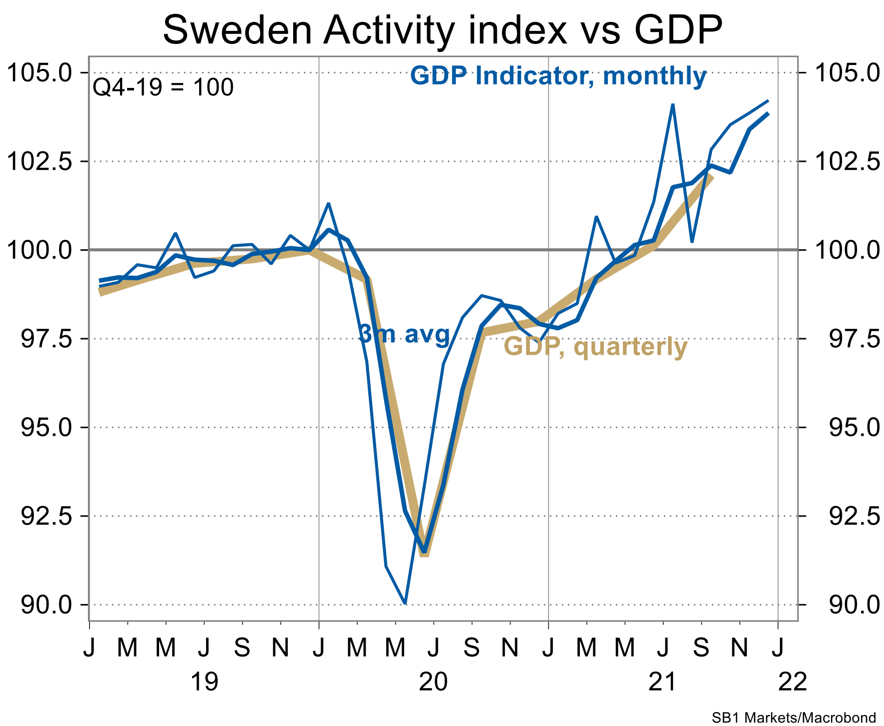


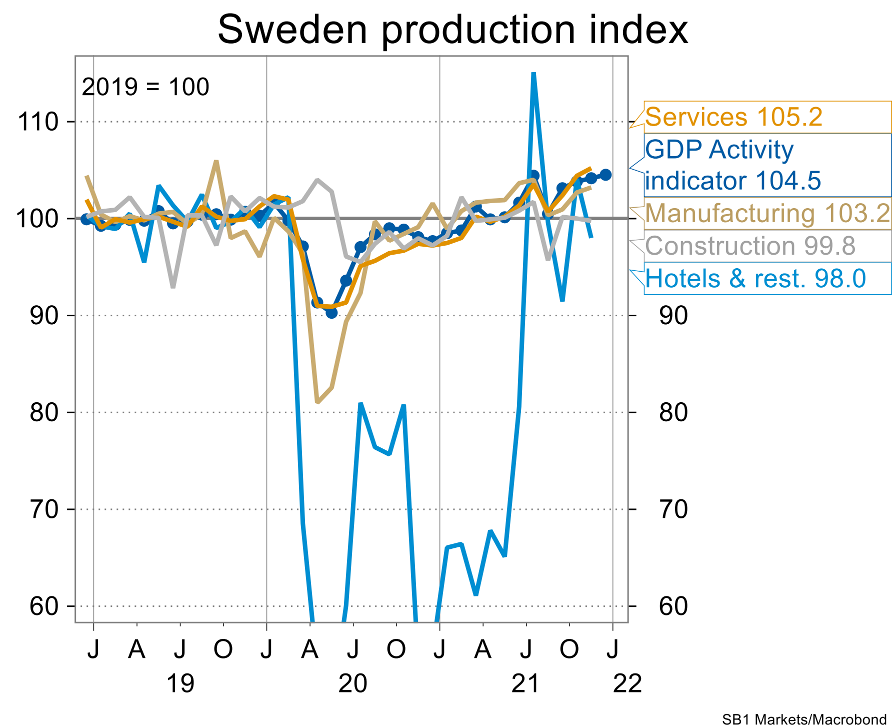


- Sales were not specifically strong in November – and the level in Dec was the lowest since last January.
- The sectoral differences are suspicious, a 23% drop in mobile phones etc does not seem likely
- Clothing is still weak, now down 17% vs. the Jan-20 level
- Retail sales in December is probably below a reasonable long term trend

GDP still on a strong recovery path in Dec, Q4 up 1.4% (5.6% ann.), +4.5% vs pre-p

Details not yet available but the strong recovery is still intact

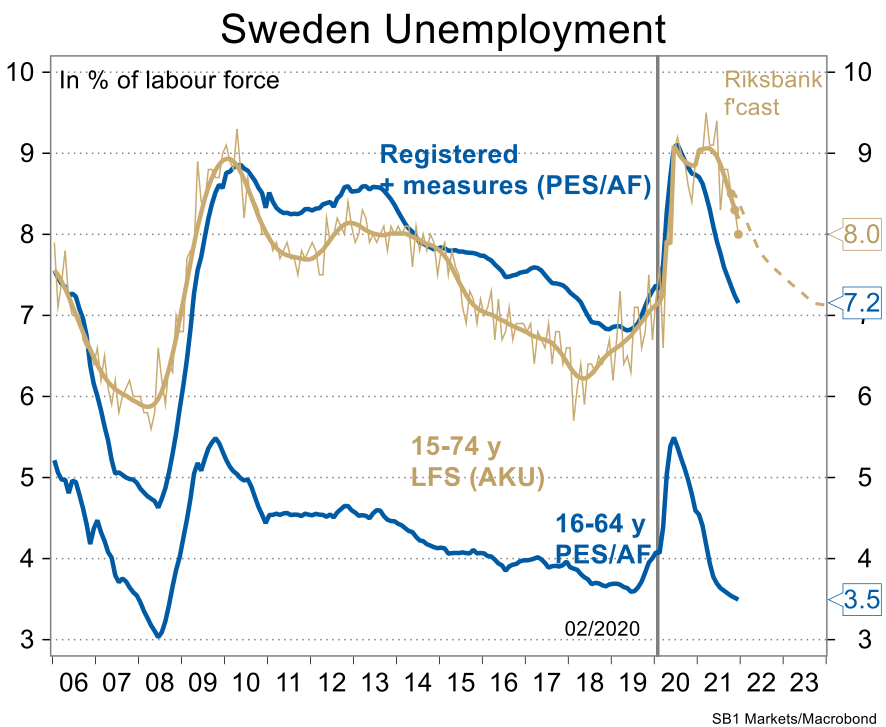


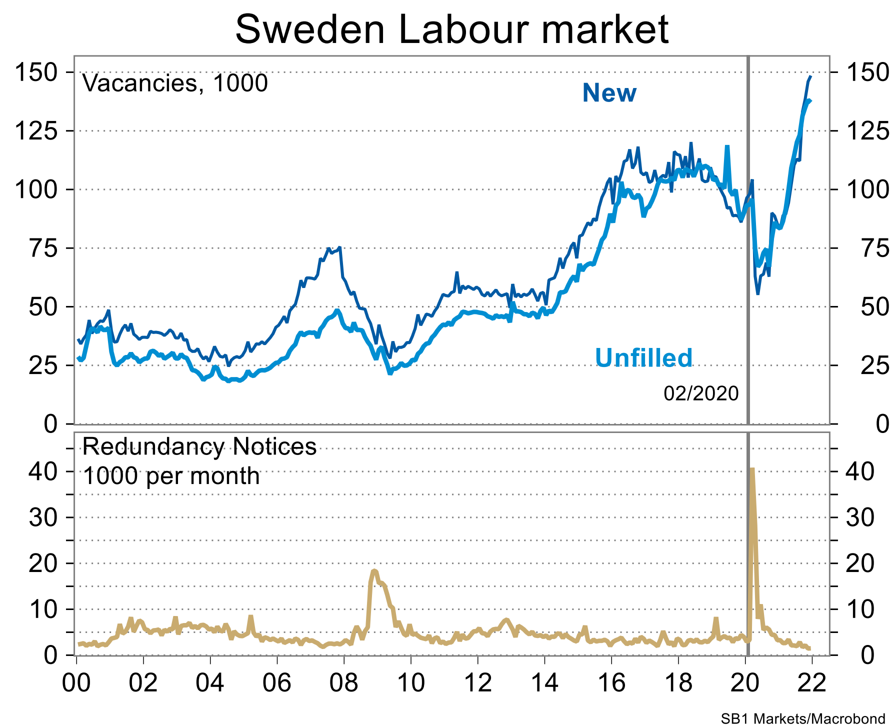


- **The outlook** remains excellent, according to Swedish companies. THE KI (NIER) survey is still close to ATH, and the PMI is the best in the world.
- In Nov, hotels and restaurants reported a decline in activity – but from above the p-p level to 2% below
- We still wonder if the Riksbank's extremely expansionary monetary policy stance is appropriate

Unemployment is heading down, as vacancies are soaring

The LFS unemployment fell by 0.3 pp to 8.0%, still 0.9 pp above the pre-pandemic level

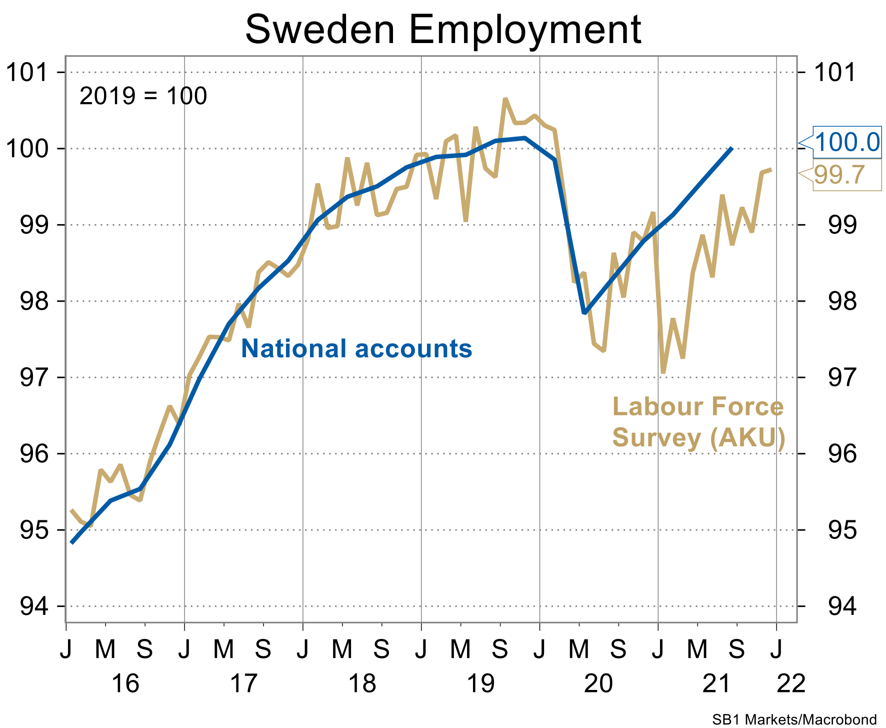


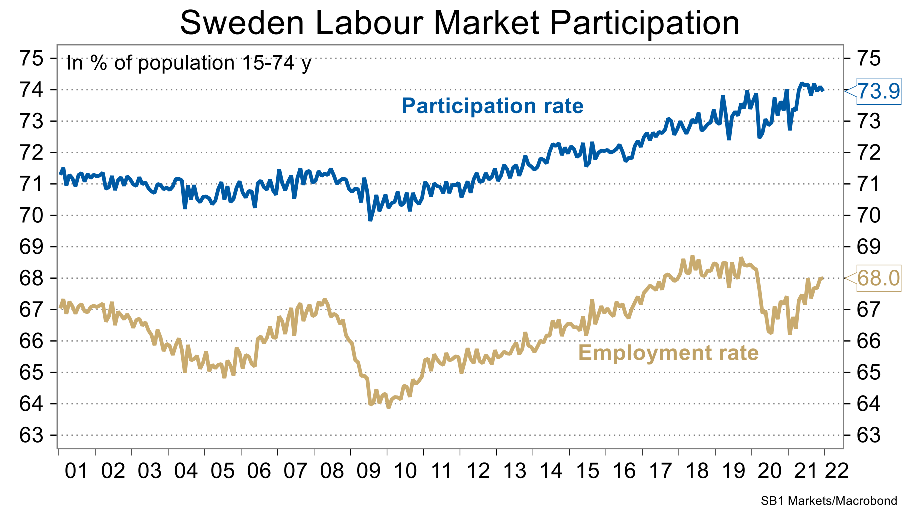


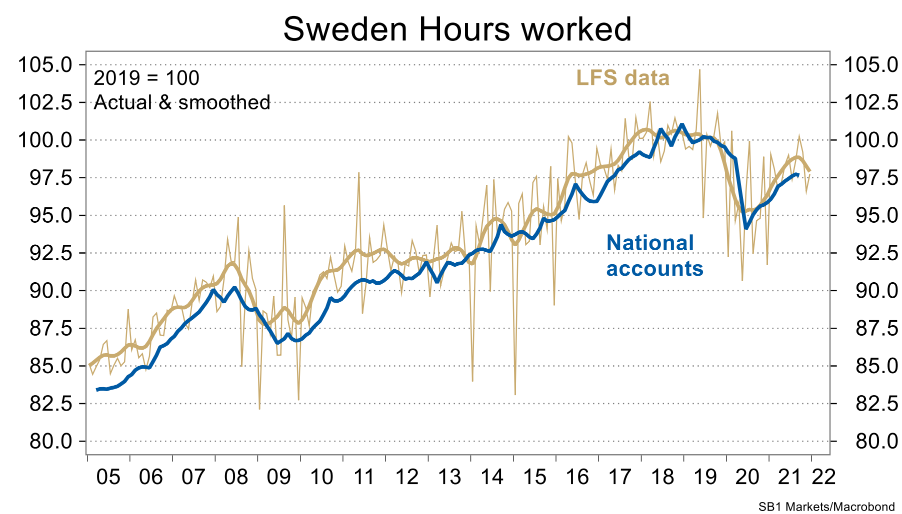
- The **LFS (AKU) unemployment fell 0.3 pp to 8.0%** in Dev, expected down to 8.2%. Unemployment is down 1%+ from the peak early 2021 but it remains 1.3 pp higher than in early 2020. (However, this survey is heavily revised, and we are not sure the Swedes have made data comparable)
- **Registered 'open' unemployment** (PES/AF) has fallen rapidly since last June 2020 but at a slower pace the recent months, and remained at 3.5% in December. Registered unemployment is below the 4.1% pre-pandemic level
- **Incl. labour market measures**, PES/AF unemployment is falling too. The rate fell by 0.2 pp to 7.2%, to below the pre-pandemic level
- The number of **new vacancies** and **unfilled vacancies** rose further in Dec, up to another ATHs! **Layoffs** were further down in Dec.

Employment is back to the 2019 level but the employment rate is still below

The employment rate is down 0.4% (0.3 pp) vs. late 2019. The participation rate is up!





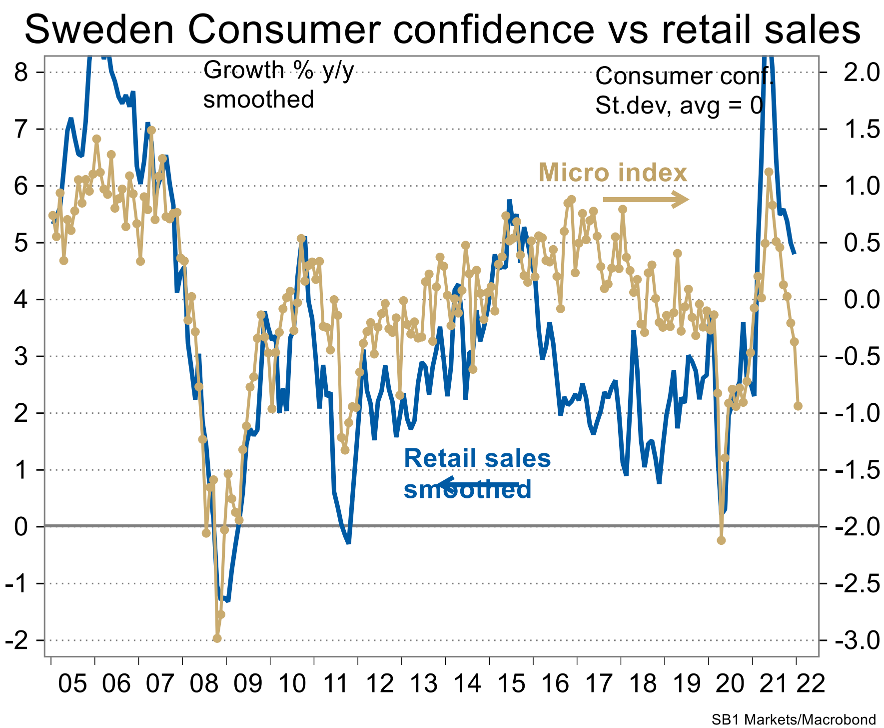


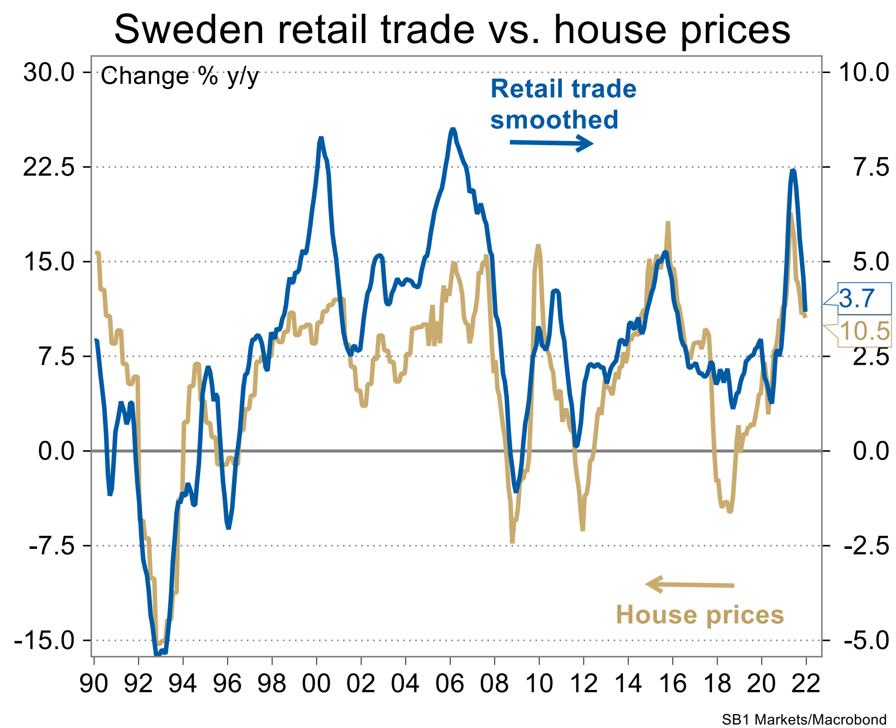
- The **participation rate** has fallen marginally the previous months but is close to the highest level ever. The increase in the participation rate explains most of the increase in unemployment since before the pandemic
- **Hours worked** has recovered substantially vs last spring but is still down 2.5% vs the pre-pandemic level

SpareBank 1 MARKETS

Consumer confidence further down in January, to well below par

Virus fatigue? Electricity prices? Quite likely. The economy is OK, but growth may be peaking

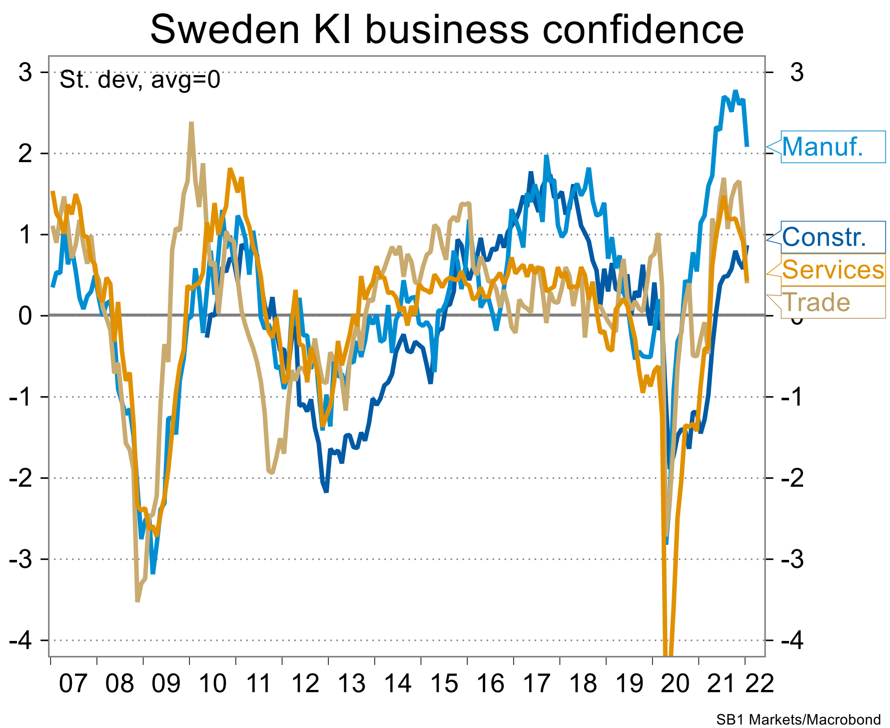


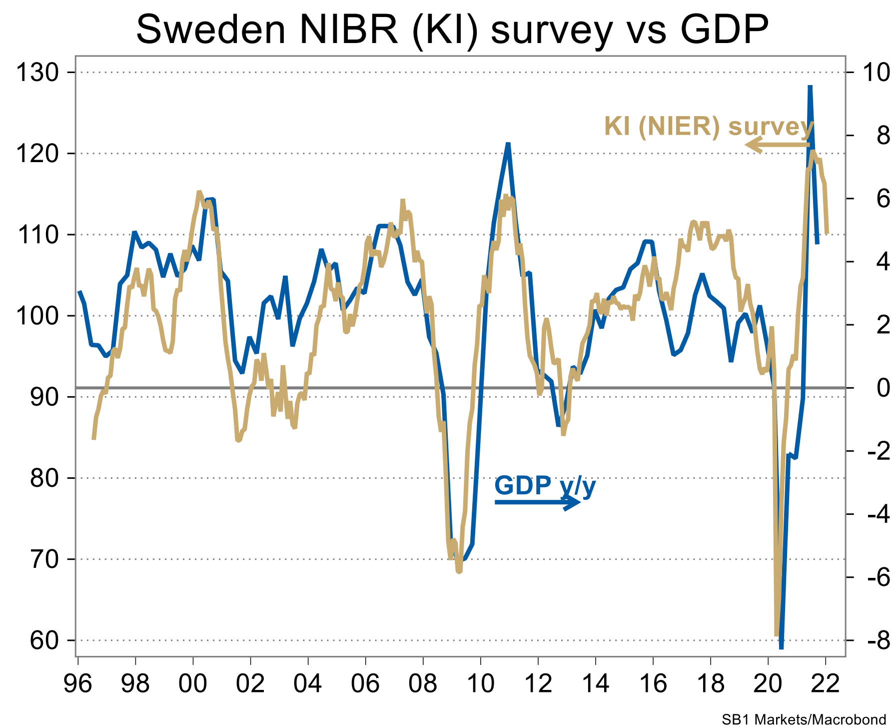


- **Confidence** is slightly below the pre-pandemic level – after being well above during most of last year
- Since 2015, the correlation between stated confidence and actual spending has waned. Even so, during 2020, the relationship may have strengthened. <u>The confidence level does not suggest a setback in household demand</u>

KI business survey down in January, 'just' 5% growth signalled

Both construction, manufacturing and services report slower growth – just trade higher growth

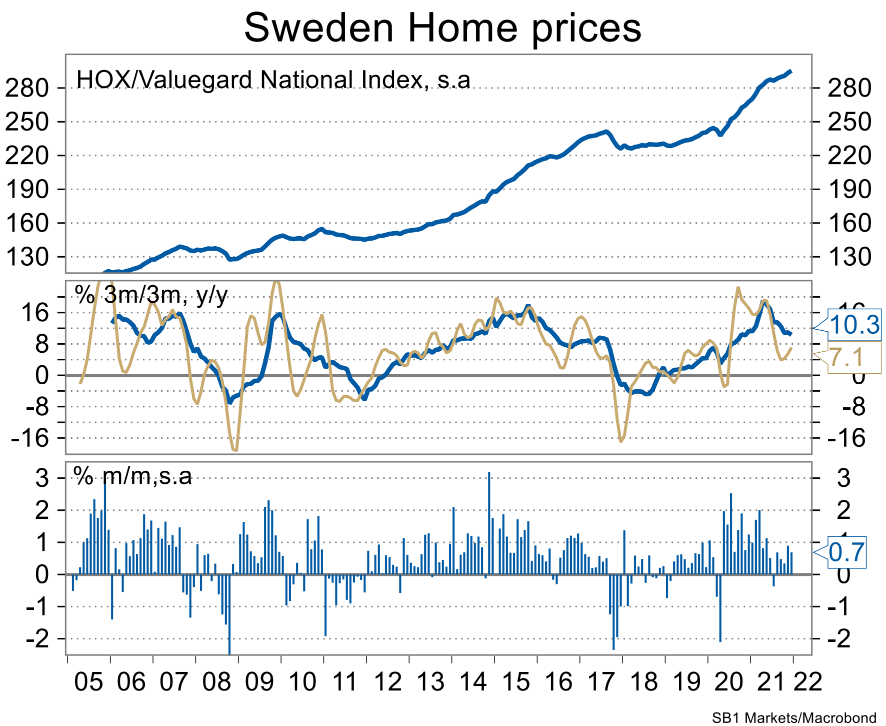


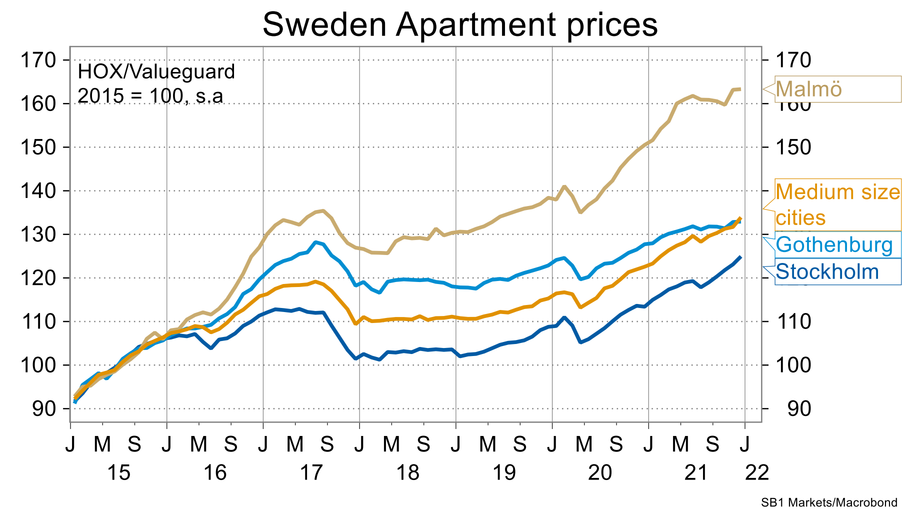


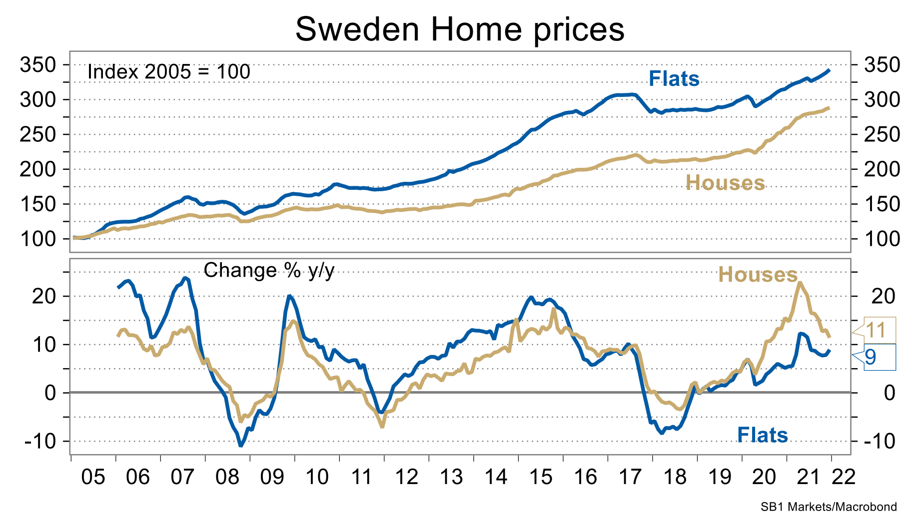
- **The composite index** still signals a 5% GDP growth rate, well below the 7 – 8% growth signalled the previous months but still a high growth rate, of course
- **All 4 main sub-sectors** are reporting growth far above average. Trade slowed the most but is still second to manufacturing, where the confidence index rose slightly
- The **Riksbank** is still concerned about the impact of the corona crisis, and thinks it will keep the policy rate at zero until late 2024. If growth subsides rapidly, that may be OK. If not..

Swedish house prices up 0.7% in Dec, underlying growth has slowed

The annual price growth has fallen to 10%, from the peak at 19%



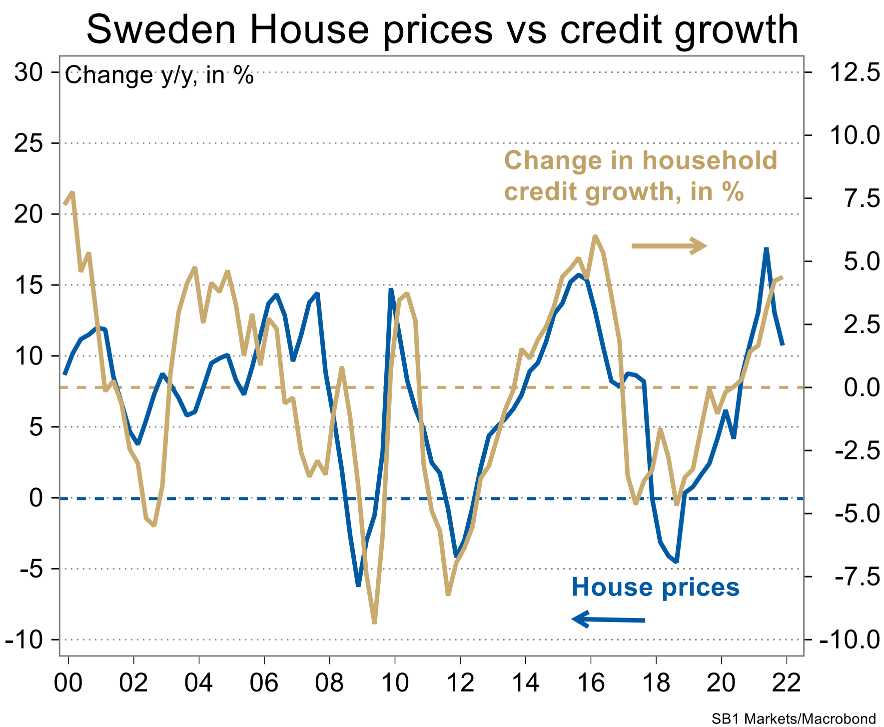


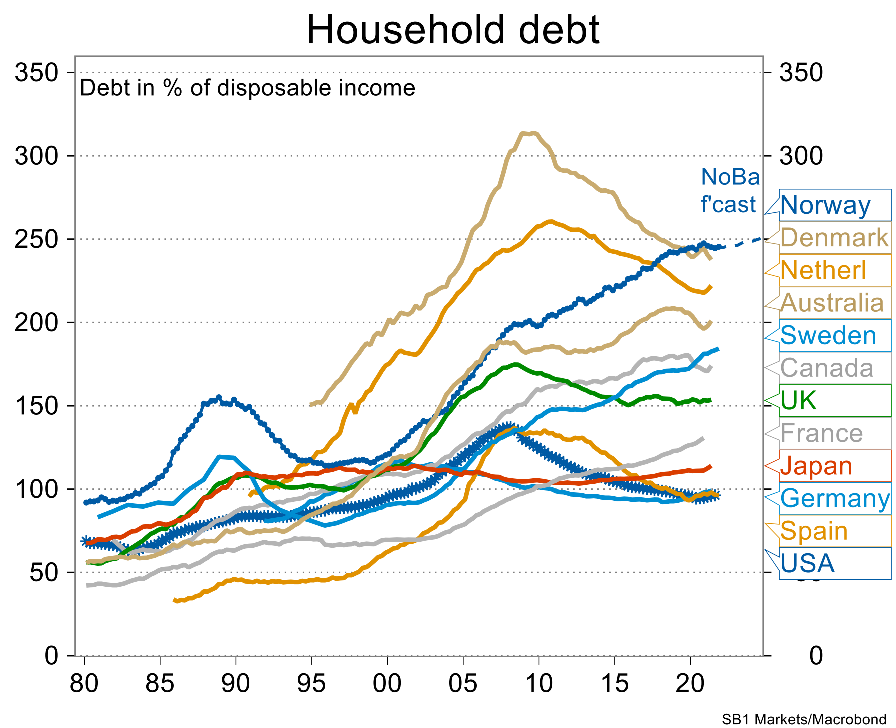


- The annual price inflation slowed almost 1 pp to 10.3% in Dec. Last April, the rate was 19% vs the local trough in Apr-20
  - » The underlying price growth (3m/3m) has fallen to 7%
- Malmö reported flat prices in Dec, the other towns further price increases
- House prices have slowed more than flat prices, reversing some of the opposite movement last year but houses are still up 11% y/y, flats 9%

Credit growth is accelerating rapidly – and will for still a while

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





Highlights

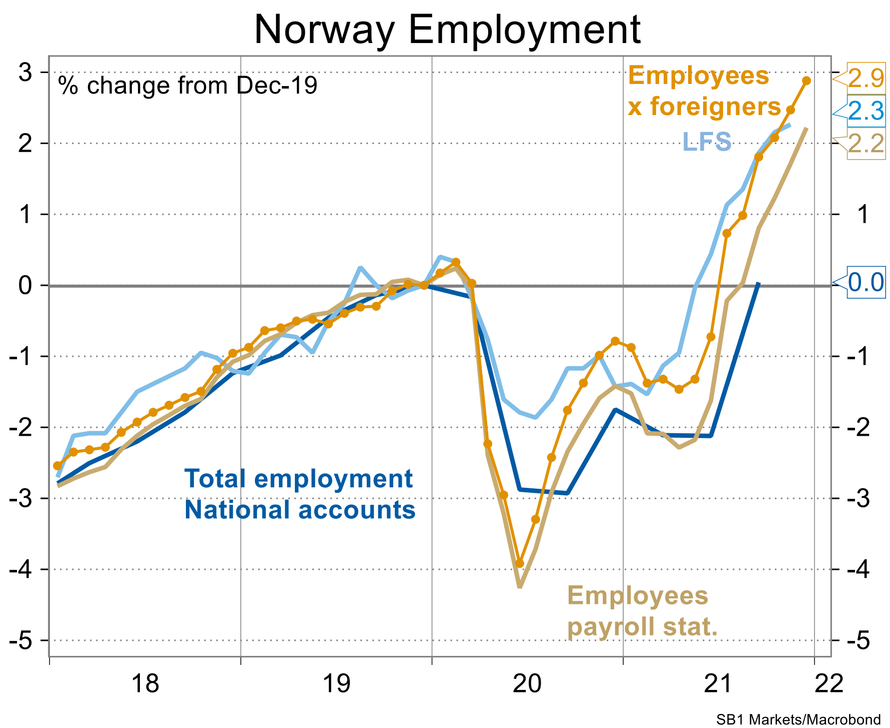
The world around us

The Norwegian economy

Market charts & comments

Reg. employment up 0.4% m/m in 'lockdown' Dec, 2.2% above pre-p level

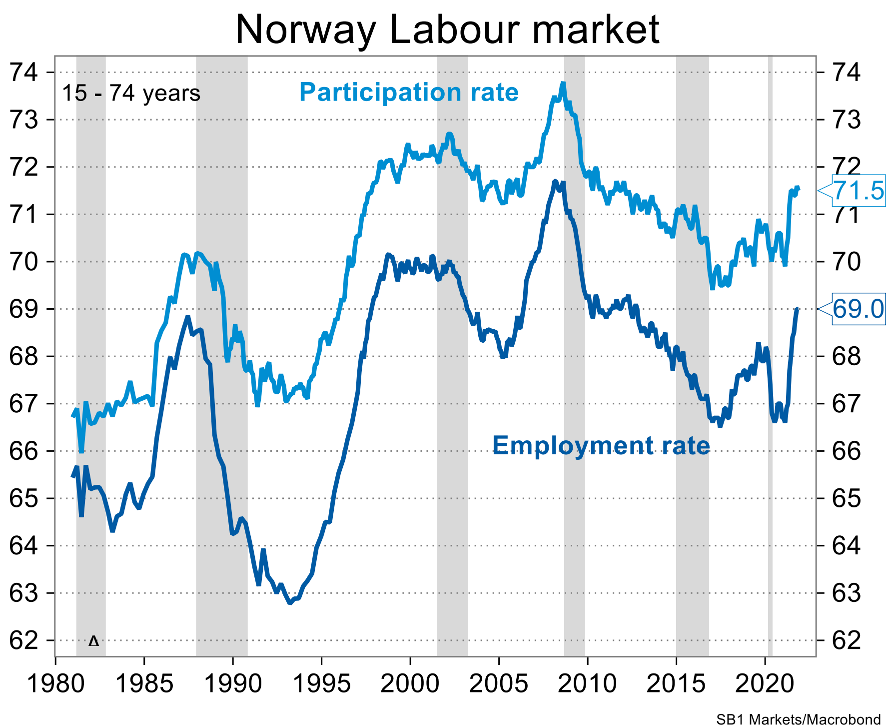
Employment up approx. 2.9% among persons living in Norway. The LFS confirms strong empl growth



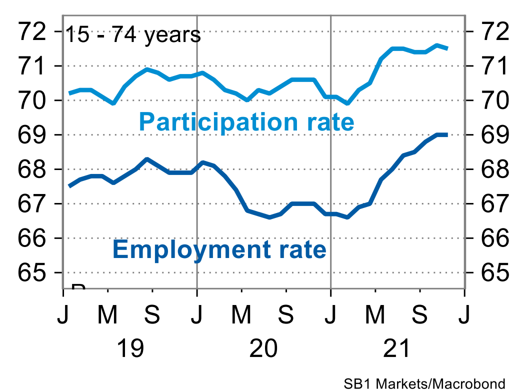
- The increase in the **register based no. of employees** in December suggests at continued growth in Mainland GDP above trend, at least until mid December
  - » The reference period is the week containing the 16th in months. Stricter corona restrictions were imposed by the mid of December and the impact came too late to be registered in the payrolls stats (a-ordningen)
  - » Payrolls grew by 0.4% m/m and is now 2.2% above the level in Dec-19 (Nov level was revised up by 0.2%)
  - » We estimate the no. of employees among permanent residents (Norwegian and foreign born) to be 2.9% above the pre-pandemic level (based on our Q4 estimate for foreign workers on short-term stay, not yet published)
  - » Growth is slowing but just slowly
  - » The increase in employment is broad based, check 2 pages fwd
- **The LFS** ('AKU' survey) employment data (both employees and self-employed, with permanent residency in Norway) reported a 3' (0.1%) growth in employment in Nov (avg Oct-Dec from avg Sept-Nov), and by 25' over the past 3 months, equalling 0.9% or a 3.5% annualised pace
  - » LFS employment is up 2.3% since before the pandemic, and both participation and employment rates are far above the pre-pandemic level – and the LFS unemployment rate has 'collapsed'
- **National Accounts** reported a 2.1% growth in total employment in Q3 – up to the same level as in Q4-19. These NA data includes foreigners on short-term stay

The employment rate is still trending up, participation may have flattened

Less competition from foreigners helped more permanent residents back to the labour market?

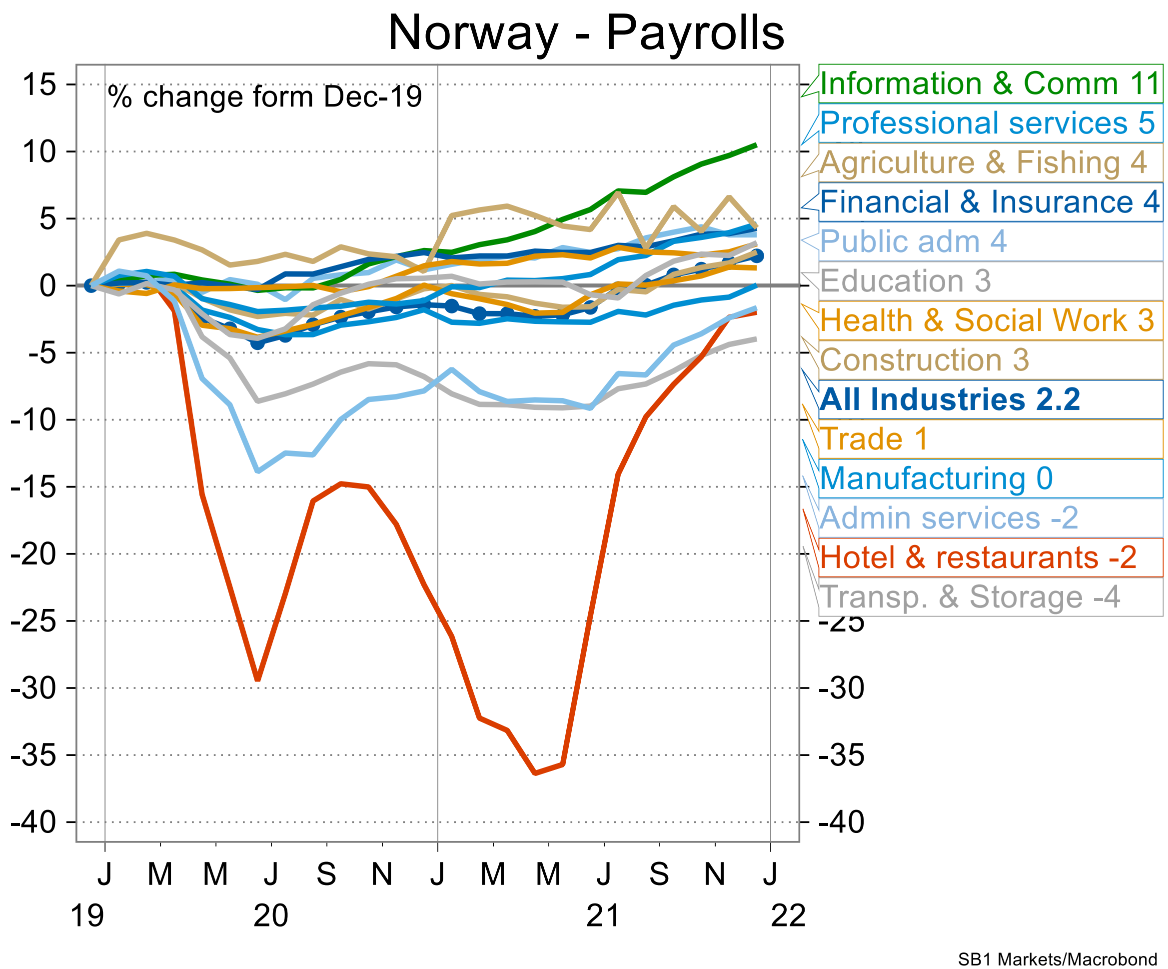


- **The employment rate** was flat in November, at 69%
  - » Ahead of the pandemic the rate was 68.1 – 68.2, and it is up from the 66.4 through in early 2021 (and from the same level in 2017, after the 'oil crisis'). The employment is measured in % of the working age 15 - 74 y population
  - » The employment rate is the highest since 2012
- **The participation rate** is also well above the pre-pandemic level but it has more or less flattened at 71.5% since last June. The participation rate is also at the highest level since 2012
- These monthly data are volatile but the flattening of the participation rate since the early summer even if demand for labour is still increasing <u>may indicate that the easy part of 're-engagement' is behind us</u>
- **Working age population** growth is 0.6% over the last year (Q4 est), in line with the moderate growth ahead of the pandemic

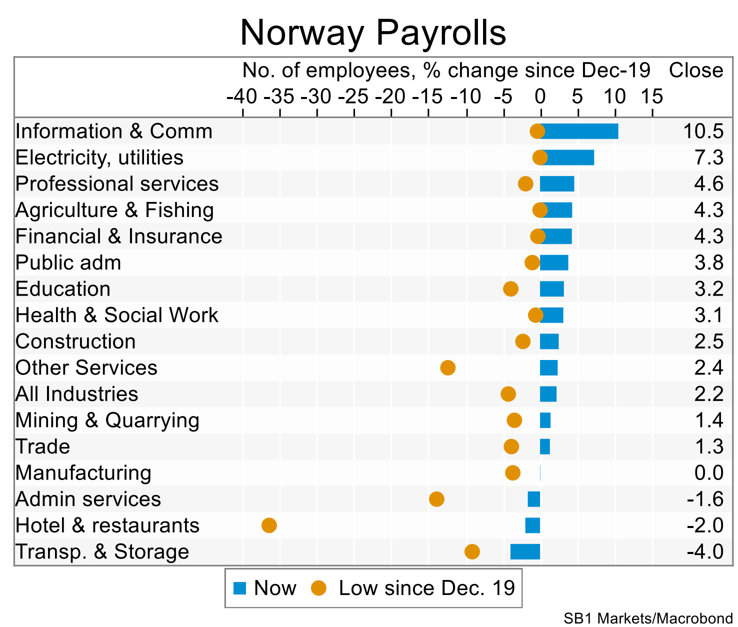


No decline in no. of employees in hotels & restaurants in MID December

The past two weeks were probably less upbeat for the sector

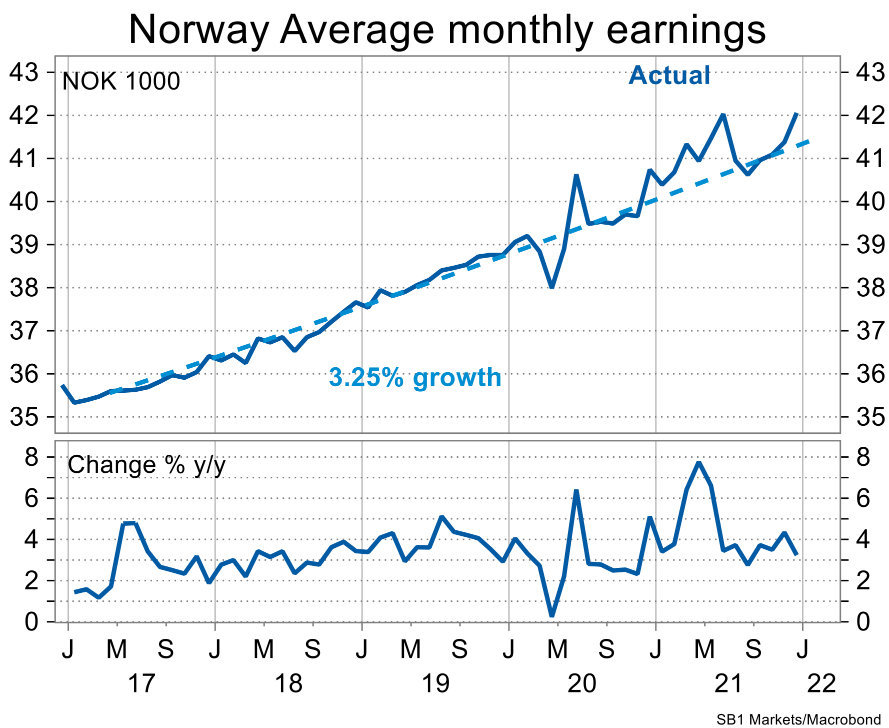


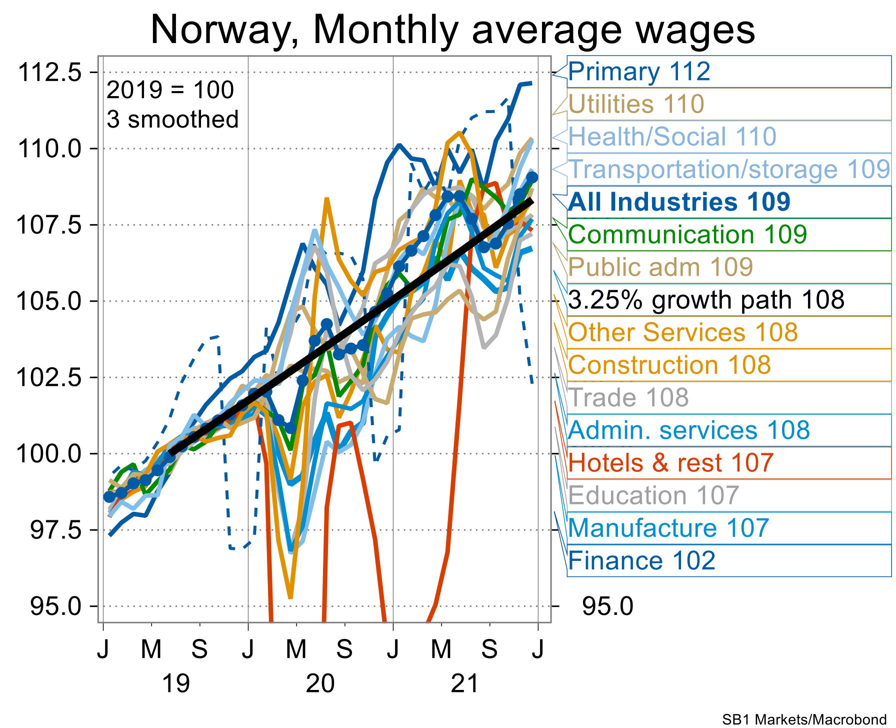
- Strong growth in most sectors



Higher wages in December, trend may now be above the 3.25% path

Substantial sectoral differences, in Dec (seas. adj.) wages in finance fell

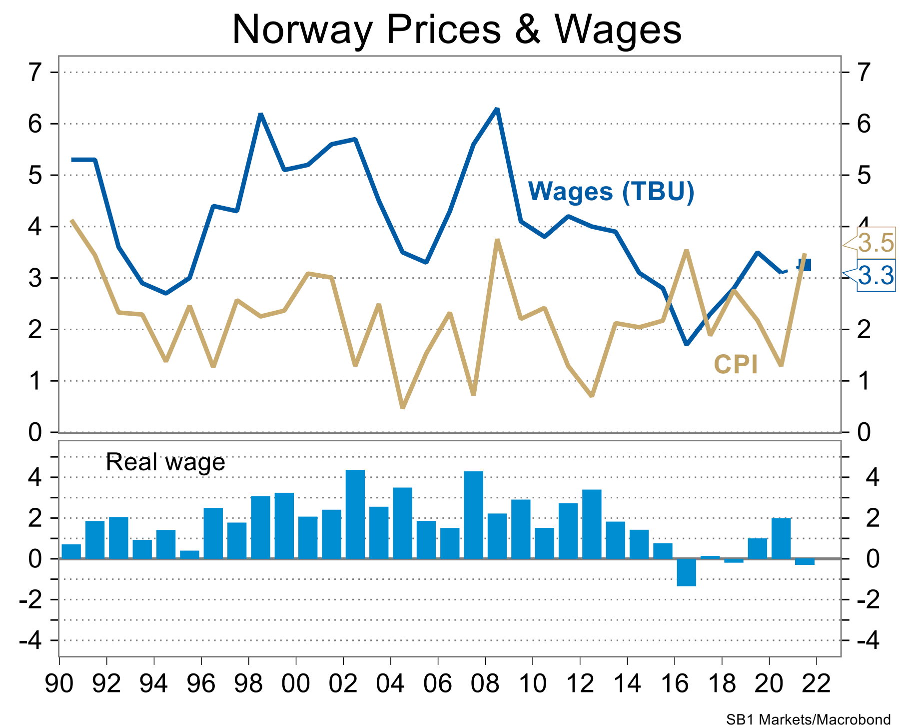




- Monthly average cash earnings are rather volatile, also depending on hours worked, bonuses
- Earnings have been above the 3.25% growth path from the start of the pandemic until June. The return of low paid service sector workers took the average down – before the average wage rate shot up in

The average wage up 4.4% last year, following the 3.1% lift in 2020

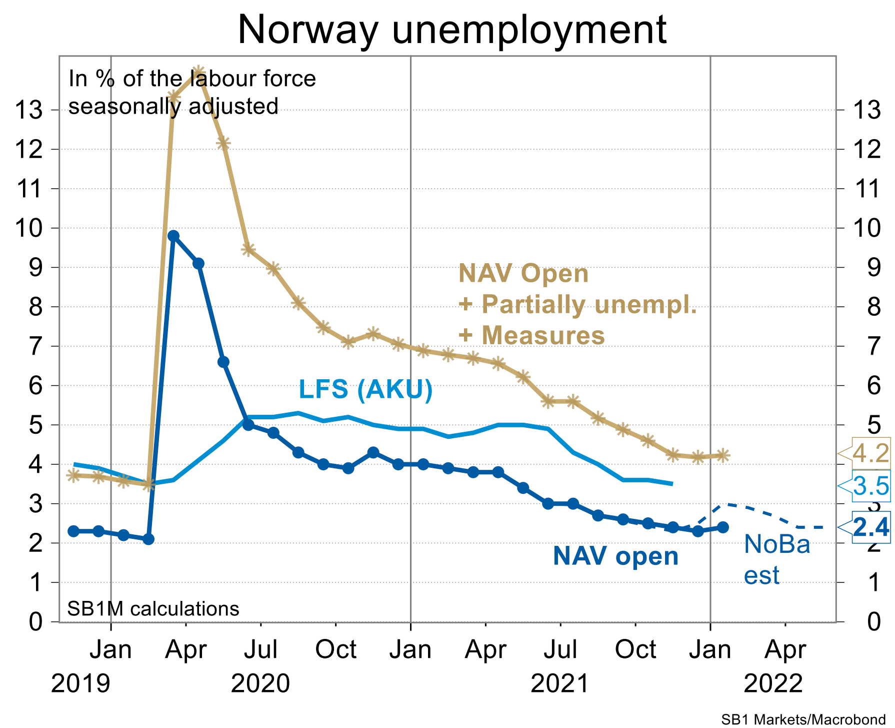
Likely large changes in the composition of employment make these data difficult to decipher

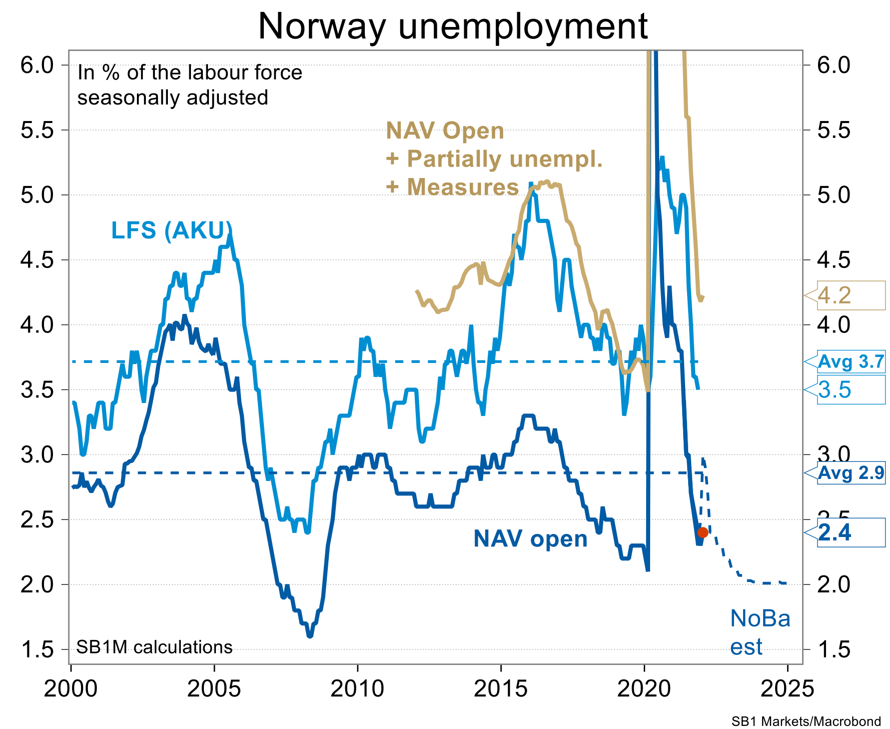


- We still assume the 'official' average wage growth was somewhat above 3% last year, a tad higher the 3.1% rate in 2020

Just a marginal increase in unemploym. in Jan, 0.1 pp to 2.4%! NoBa expected 3%

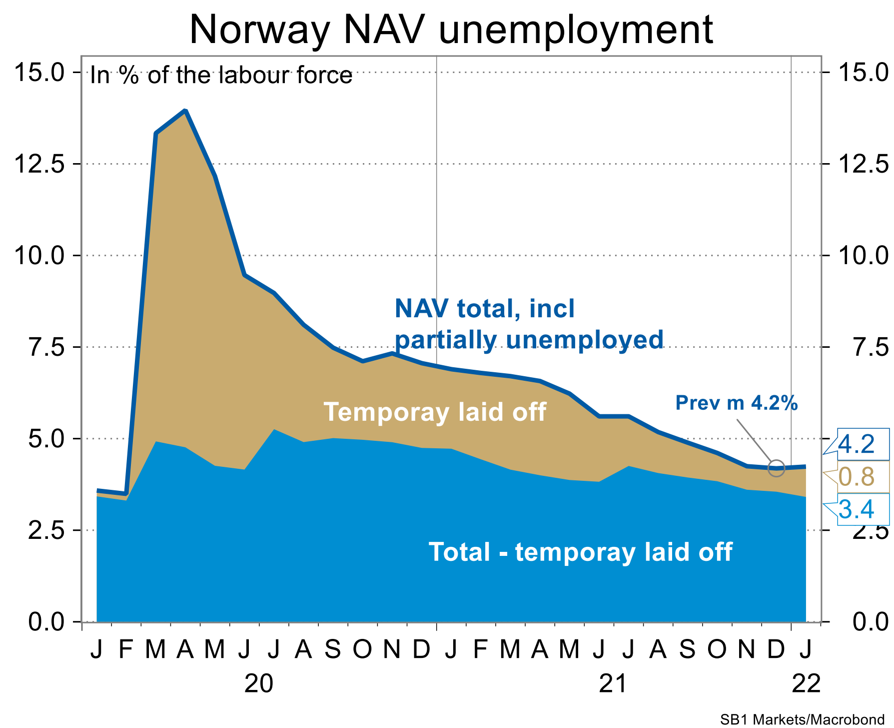
The LFS survey reported a 0.1 pp decline in Nov, to 3.5%. Both below consensus (but as we expected)

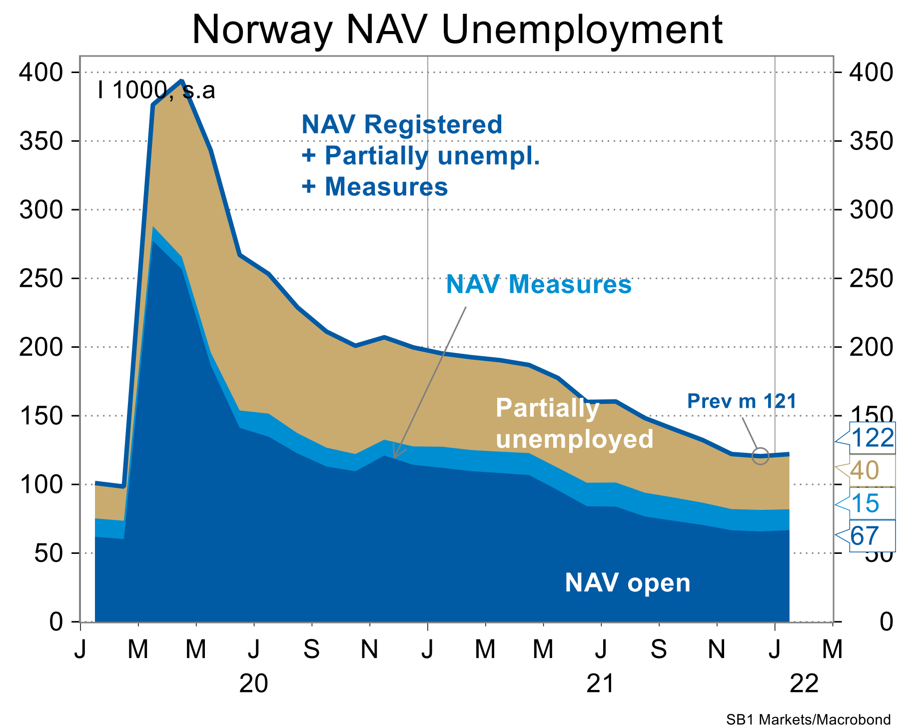




- **The 'full time' open NAV unemployment**, which includes furloughed workers, rose by 900 persons in Jan (seas. adj) to 67' we expected +3' to 68' (Dec was revised up by 1.3'). The rate added 0.1 pp to 2.4%, as we expected. In Dec. NoBa assumed an increase from 2.5% (outcome 2.3%) to 3.0%. Unadjusted, the rate as we expected rose to 2.6% from 2.2%, consensus was at 2.7% The 2.4% rate is well below the 2000 – 2019 avg at 2.9%, and just 0.3 pp above the pre-pandemic level. Barring the small Jan hiccup, unemployment is falling rapidly everywhere and for all sorts of labour .The no of furloughed workers increased, while ordinary full time unemployment fell further
- The number of **partially unemployed** (not included in the ordinary unemployment no.) rose by 1' to 40', and including measures, the **total unemployment** fell by rose 1' to 121', to 20' above the pre-pandemic level. The rate was unchanged at 4.2%, up from 3.5% in Feb-20
- The inflow of **new job seekers** fell further, and the **inflow of new vacancies** rose further from a high level the previous 6 months
- Last week: **The LFS (AKU) unemployment rate** nosedived by 0.4 pp to 3.6% in Sept, far more than expected, as the **employment rate** rose further

The labour market has weathered the Omicron wave well

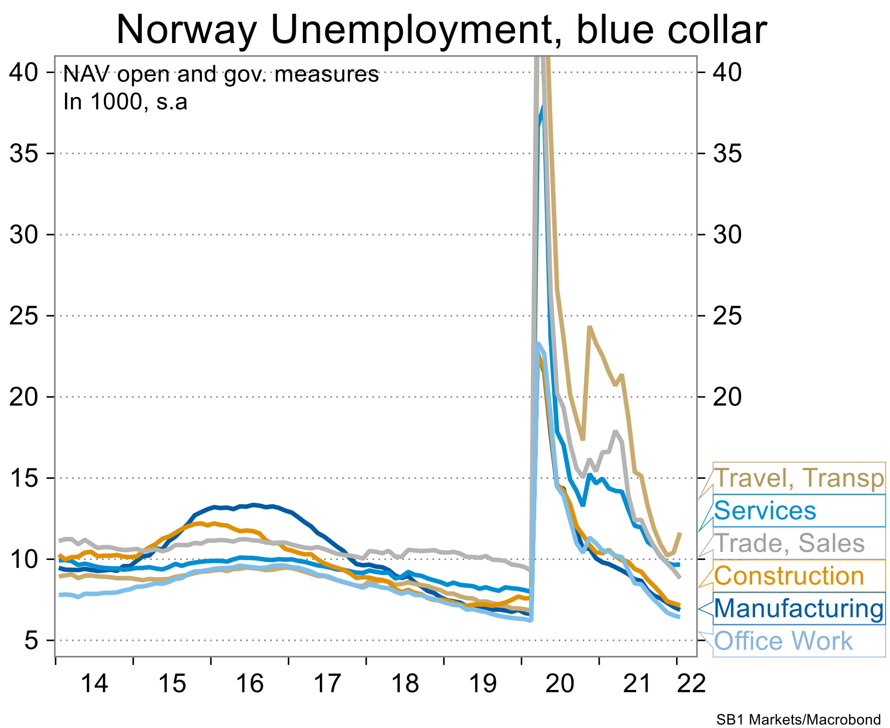


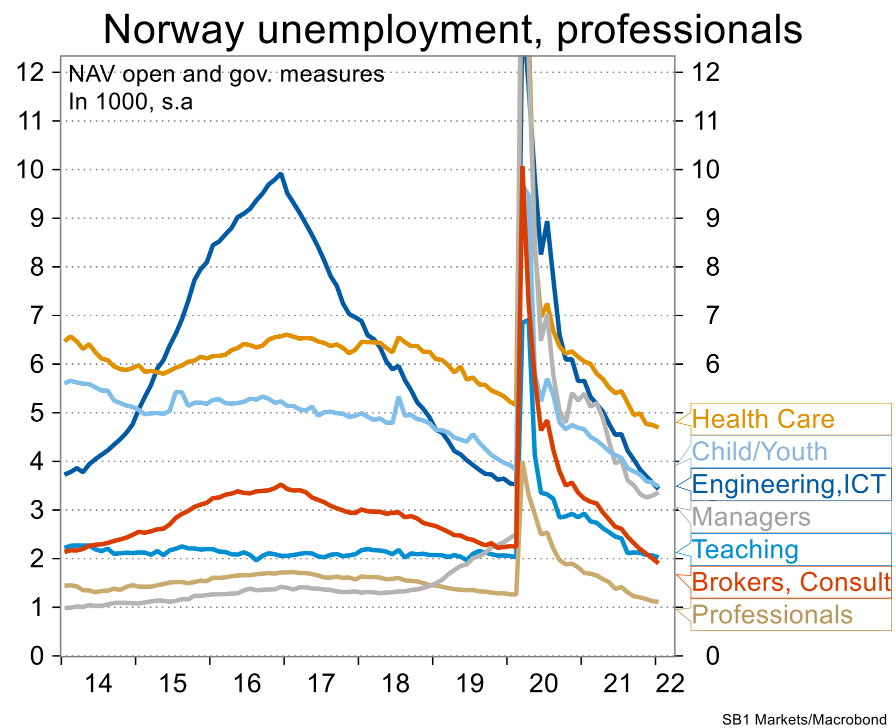


SpareBank 1 MARKETS

Some few more unemployed in travel/transport – all others sectors flat/down

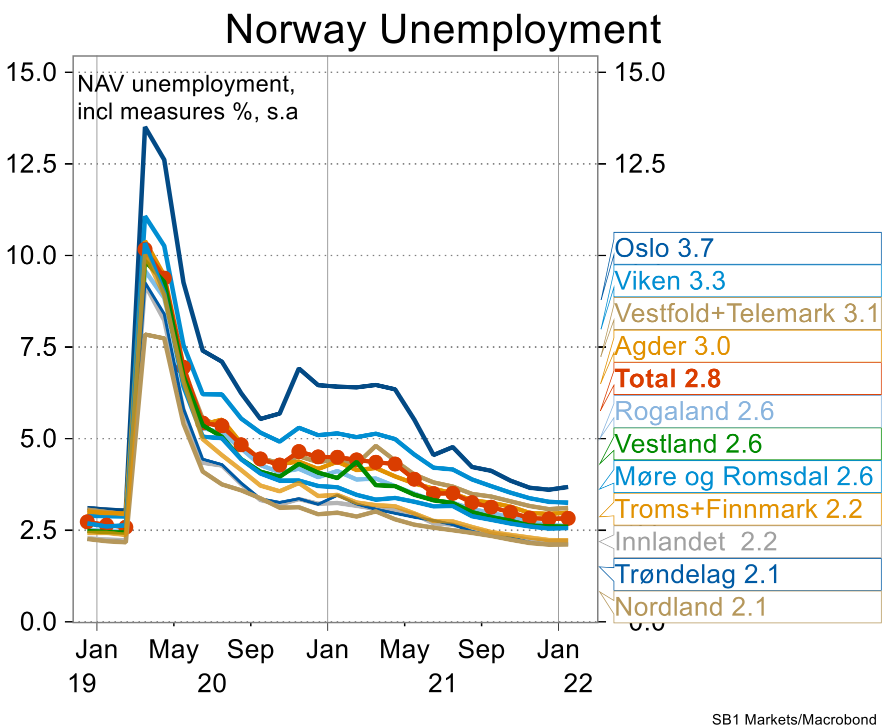
Employment has fallen in rapidly in all sectors until now

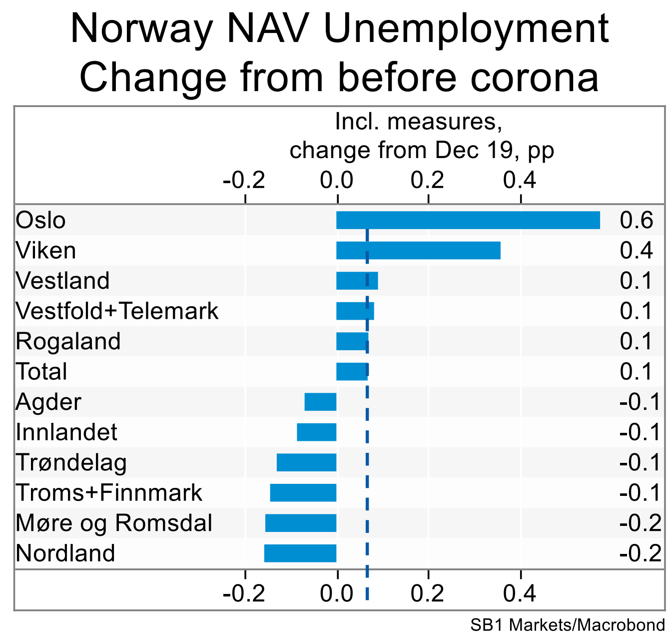




Unemployment flat or just marginally up in the regions

No Omicron crisis to be seen nowhere

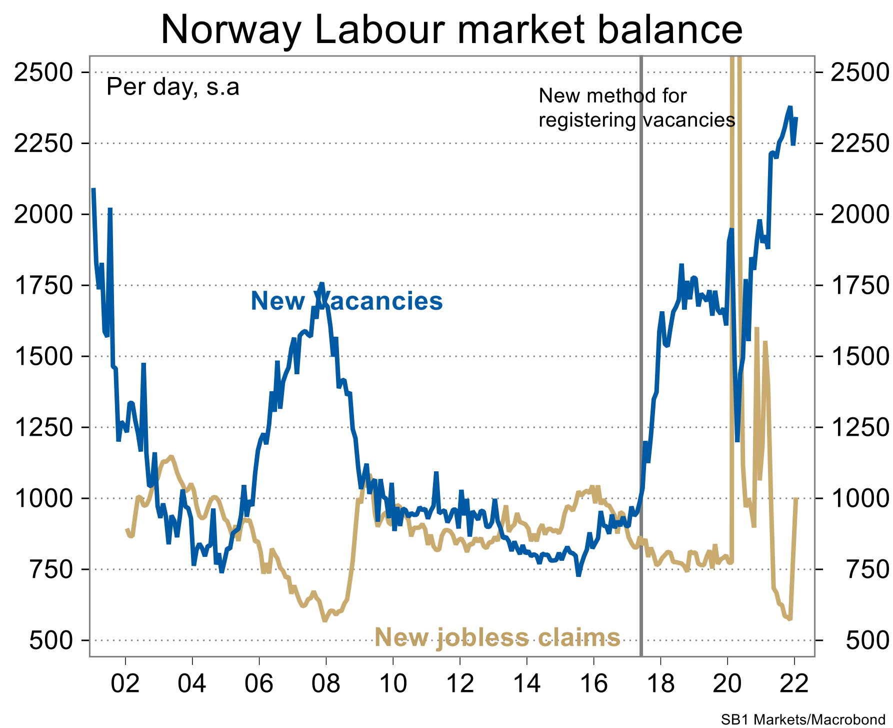


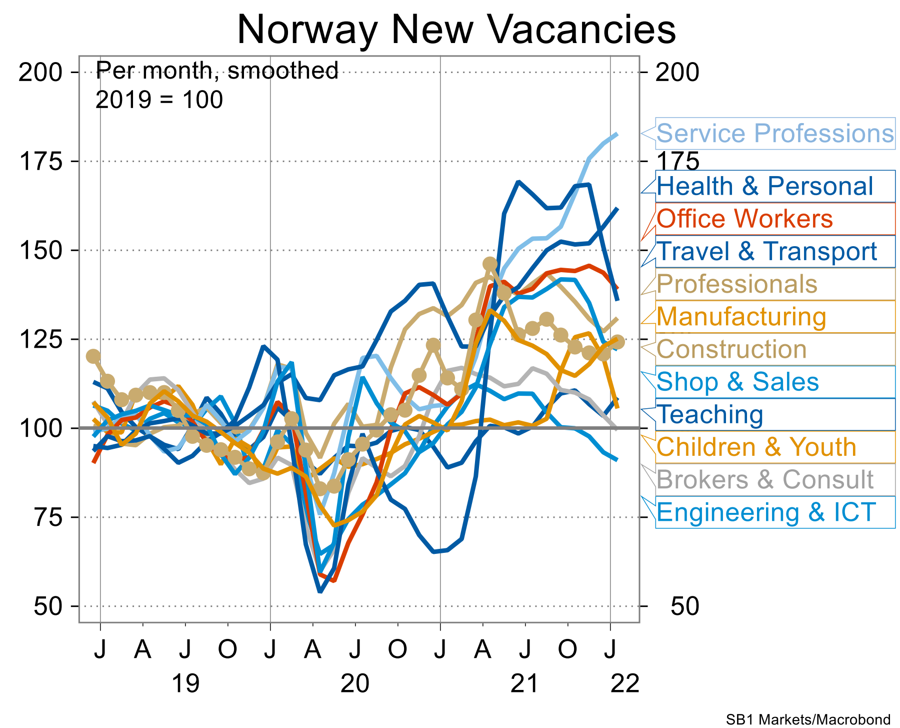


- Just **Viken and Oslo** is still reporting an unemployment rate at > 0.1 pp higher than before the pand.
  - » **Oslo** has by far been the hardest hit county, both due to tighter restrictions and a large service sector – followed by Viken
- Ordinary unemployment (full time, temporary laid offs and measures included) falling everywhere – and it is approaching the pre-pandemic levels in most counties.

A new uptick in the no. of vacancies in January!

However, a lift in new jobless claims, probably temporary

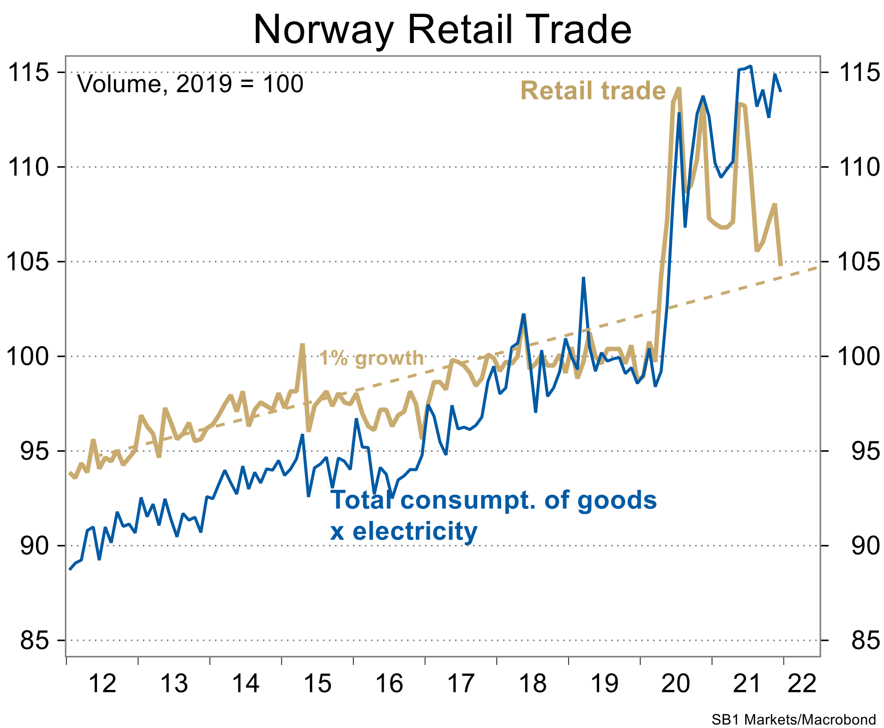


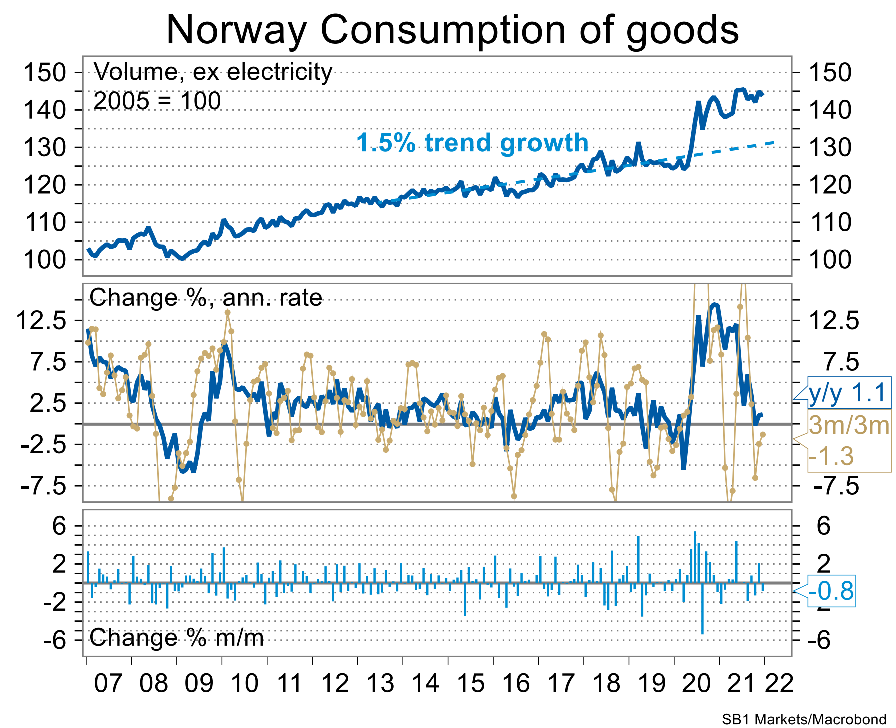


We have made a preliminary adjustment of the 2020 vacancy data due to a NAV reporting error which have led to under reporting of new positions through the year. NAV reports that the no. of new vacancies is at the same level in January 2021 as one year ago

Retail sales sharply down in December, total consumption of goods still strong

Sales fell by 3.1%, we expected -1%. Sales are now back to a 'normal' level; Consumption is far above

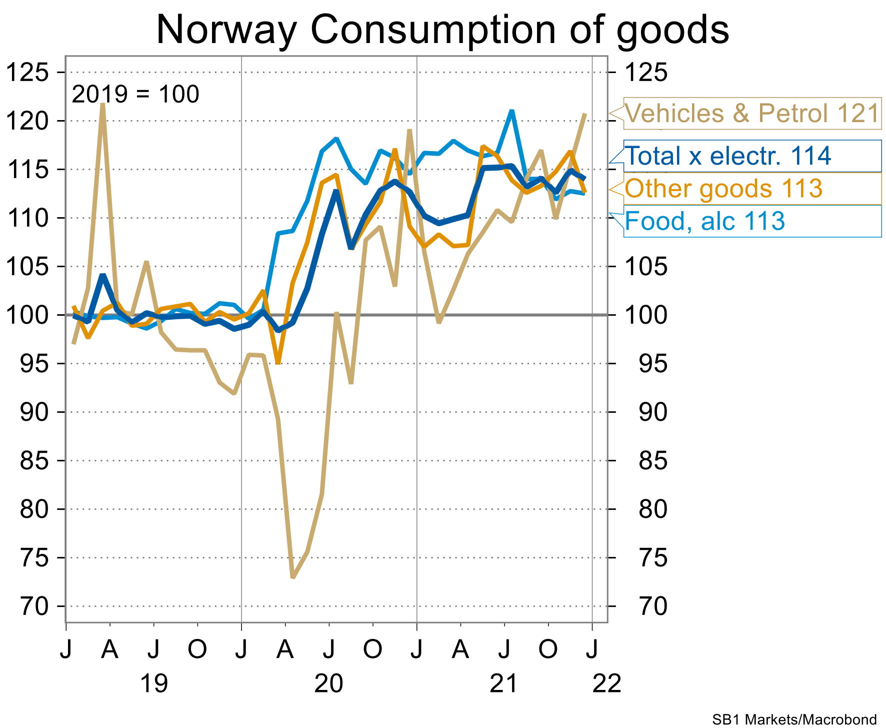


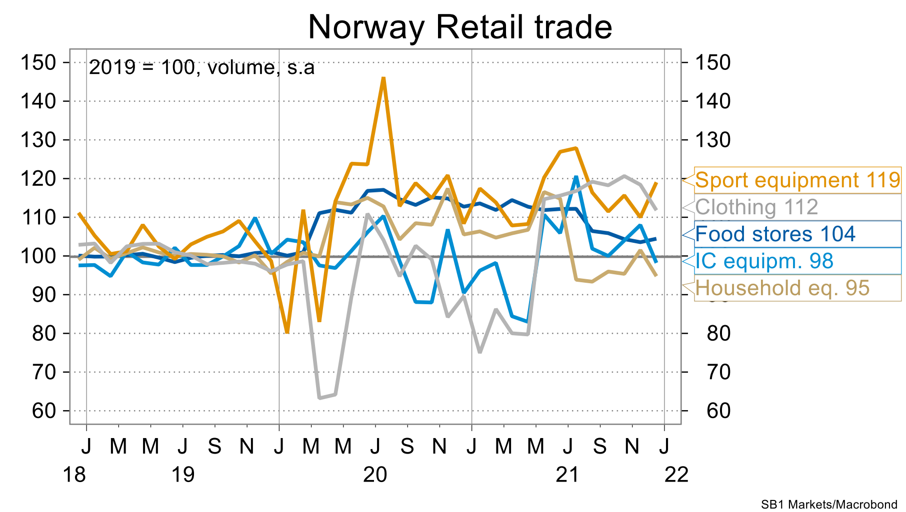


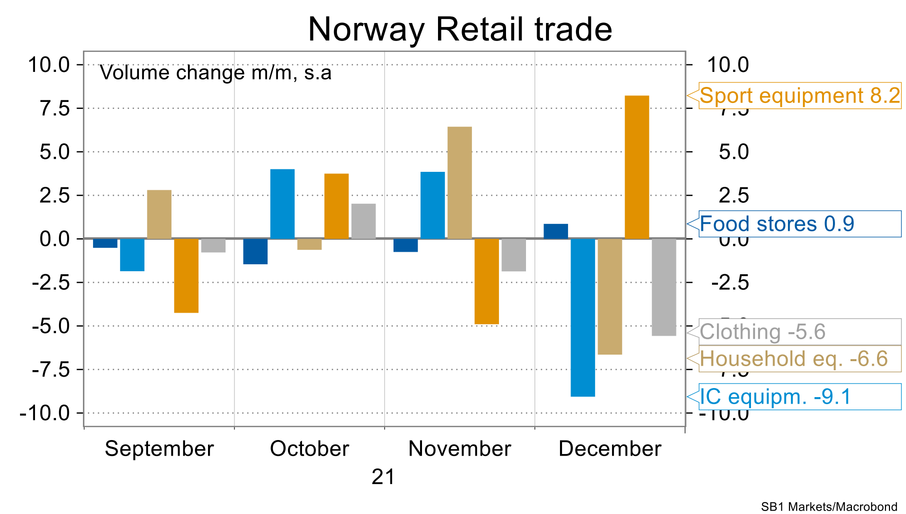
- **The consensus forecast** was -0.3%. Sales have been far more volatile than normal during the pandemic, and monthly data have been close to useless. Sales have been trending down through last year, from a very high level – and is now approaching the pre-pandemic trend, which was rather modest
- **In December**, sales of household equipment, electronics and clothing fell 6 - 9%, while sales of sport equipment rose 8%
- **Total household consumption of goods** (x electricity) subtracted just 0.8%, supported by very strong auto sales – which rose to the 2nd highest level ever in December
  - » The main reason for the difference between retail sales and consumption of goods during the pandemic has been strong auto sales and the decline in sales of building materials, which is included in retail sales but not by much in households' consumption of goods

Once more, substantial differences between sectors

Sport the big gainer in December; clothing, electronics and household equipment the big losers





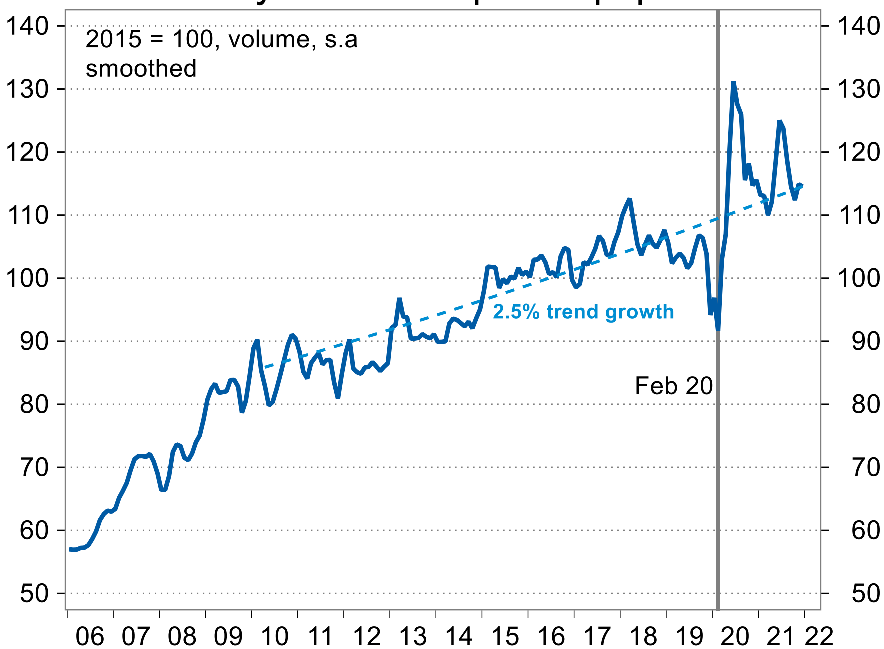


- Food store/grocery store sales fell marginally, even if x-boarder trade in Sweden probably fell. Still, the level is high, up 13% vs. the 2019 level
- Consumption of other goods (than food, electricity, vehicles & petrol) are up 13% vs. the pre-pandemic level – which is far above any reasonable long term trend

Where is the long term trend?

Sport equipment sales are up 19% vs the 2019 level but still in line with a 10 y reasonable trend?

Norway Sales of sport equipment

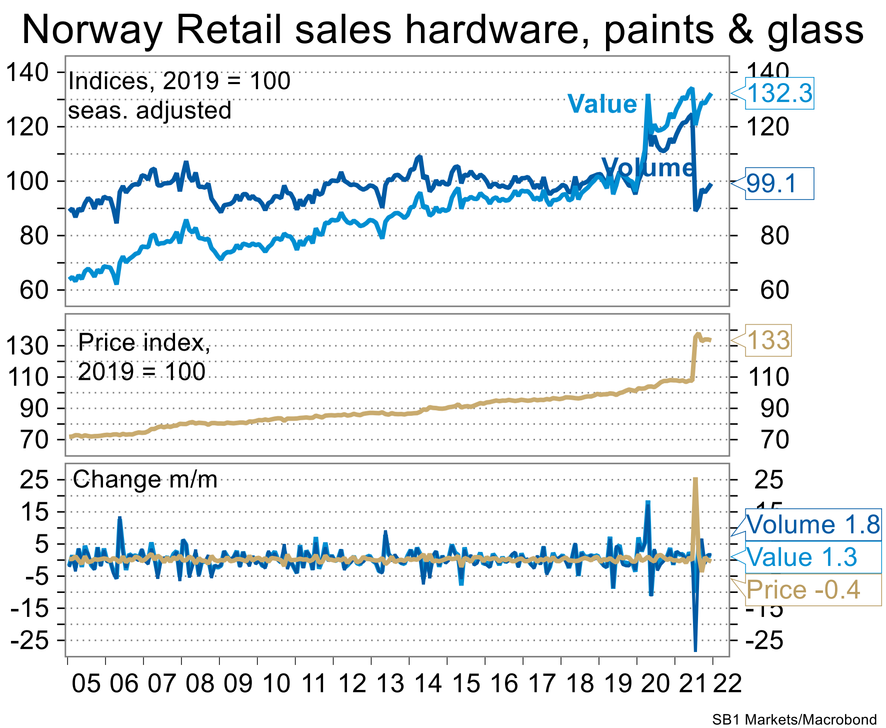


SB1 Markets/Macrobond

- Sales are smoothed at the chart to the left

Sales of building materials has recovered, is back at normal level again

Sales have climbed some 10% since July following the drop last summer, when prices exploded

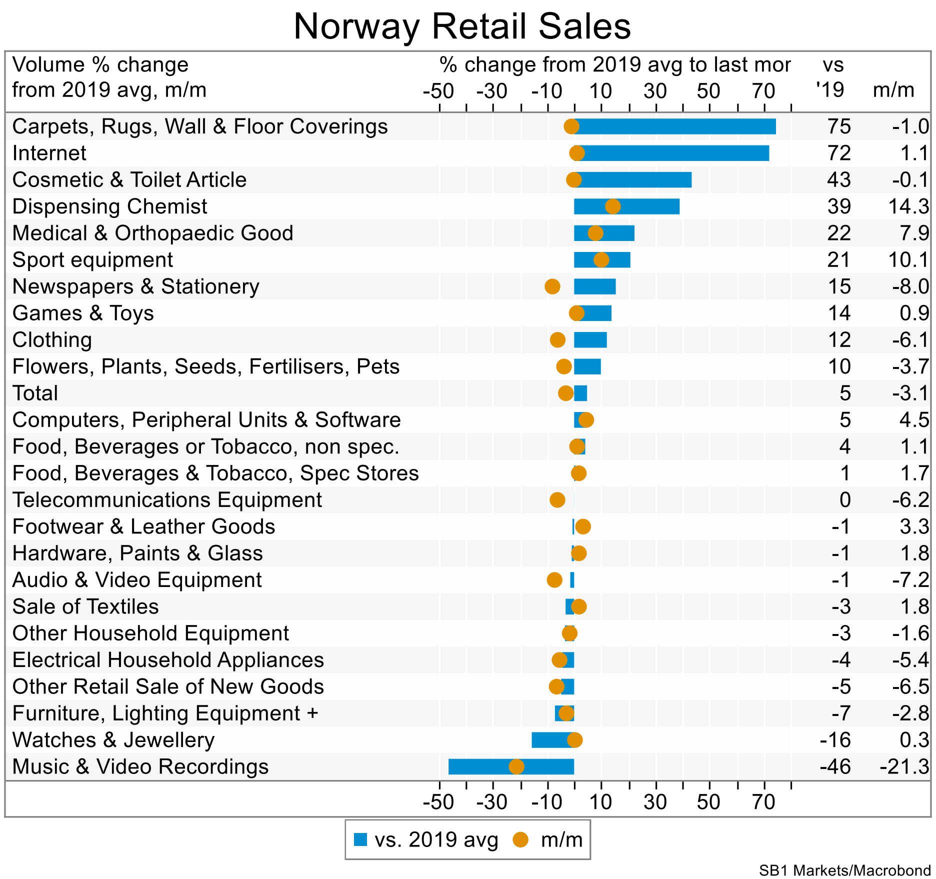


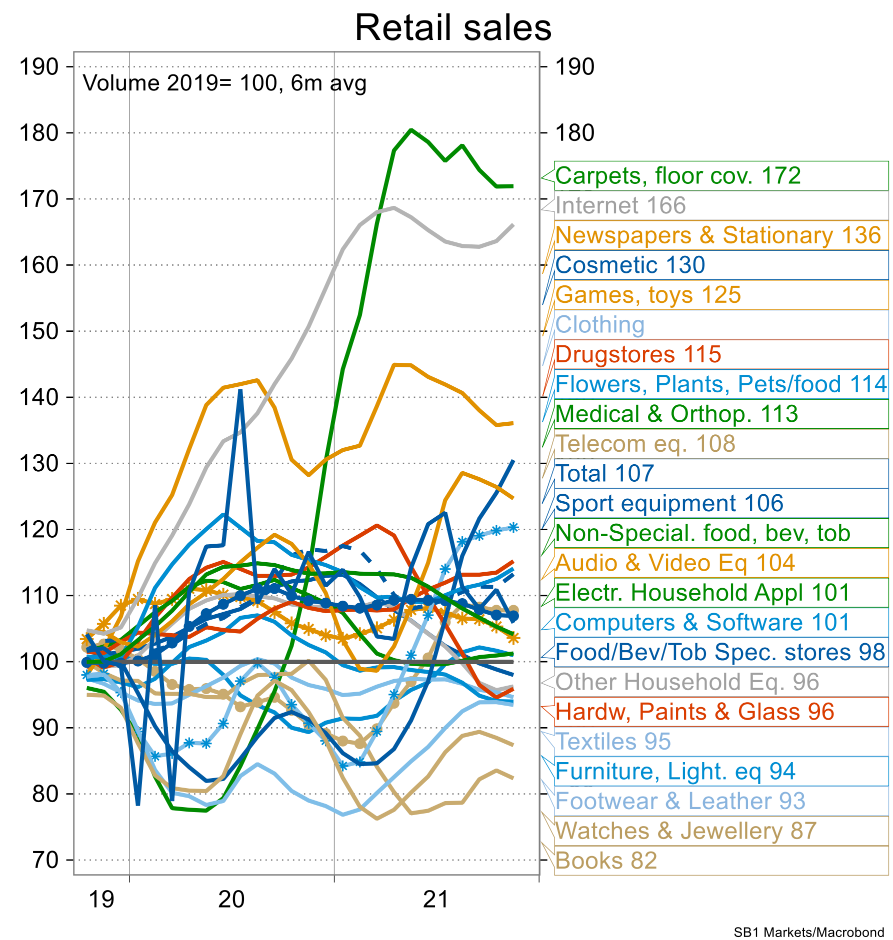
- A decline in new home sales and construction starts – may explain some of the decline in sales of hardware, paints & glass
  - » Until the decline last summer, the level almost was 20% above the pre-pandemic levels – obviously not sustainable
- Following the almost 30% drop in volumes in July, sales have recovered some of the losses recent months. In December, the volume was just 1% below the 2019 level – which was in line with a flattish trend

- **Hardware etc. prices** soared 26% m/m last July – and sales volumes collapsed, from a rather high level. Construction lumber was mostly to blame. Now, prices have stabilised, at 33% above the pre pandemic level
- **Households** buy just of small fraction of total retail sales of building materials, homebuilders and professionals are the main clients, and households' consumption is not much influenced by the ups and downs of retail sales of building materials

Since before the pandemic: Still huge sectoral differences

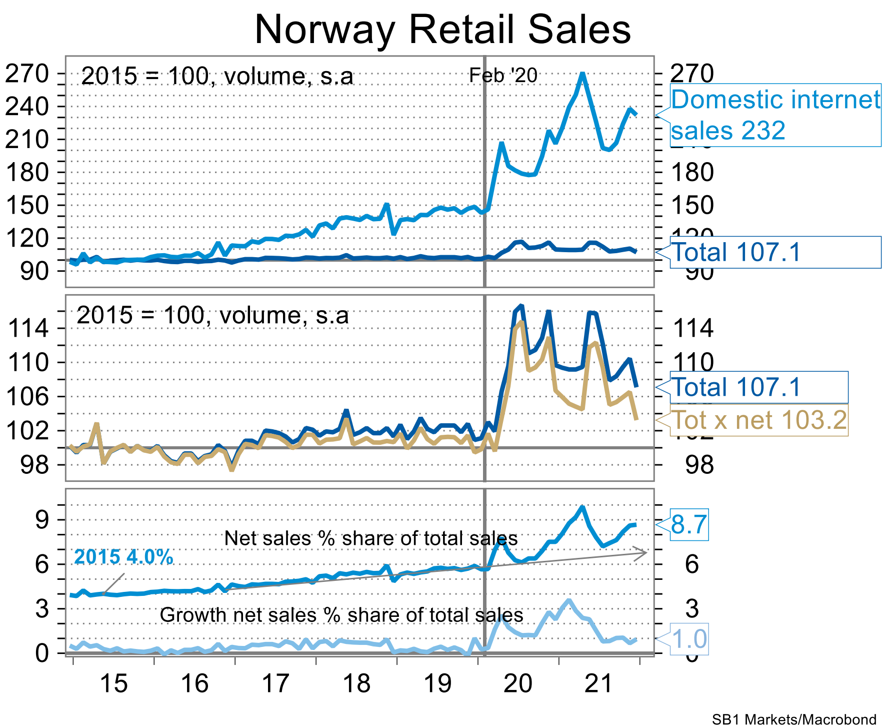
– net sales & home refurnishing at the top. The losers were mainly losers before the pandemic too

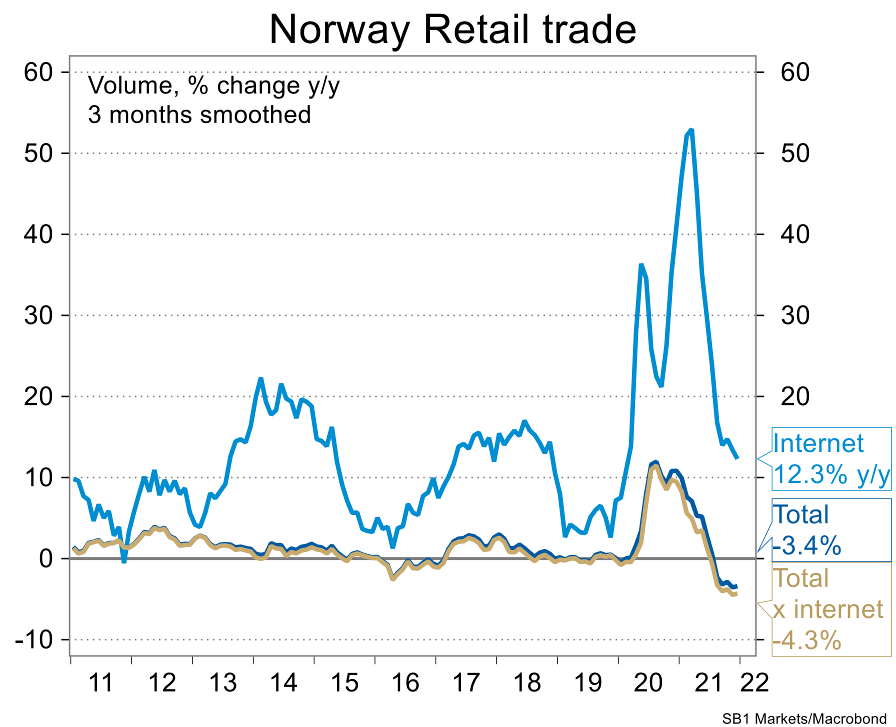




Internet sales (domestic) slightly down in December, up during H2

Sales are up 12% y/y, and the market share has recovered somewhat – still below the pandemic peak

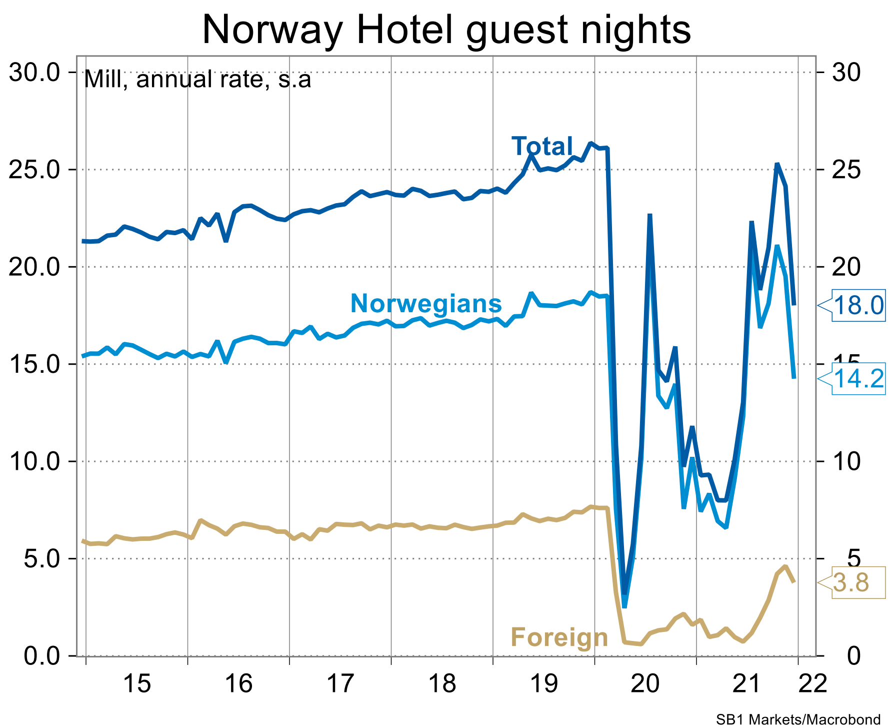


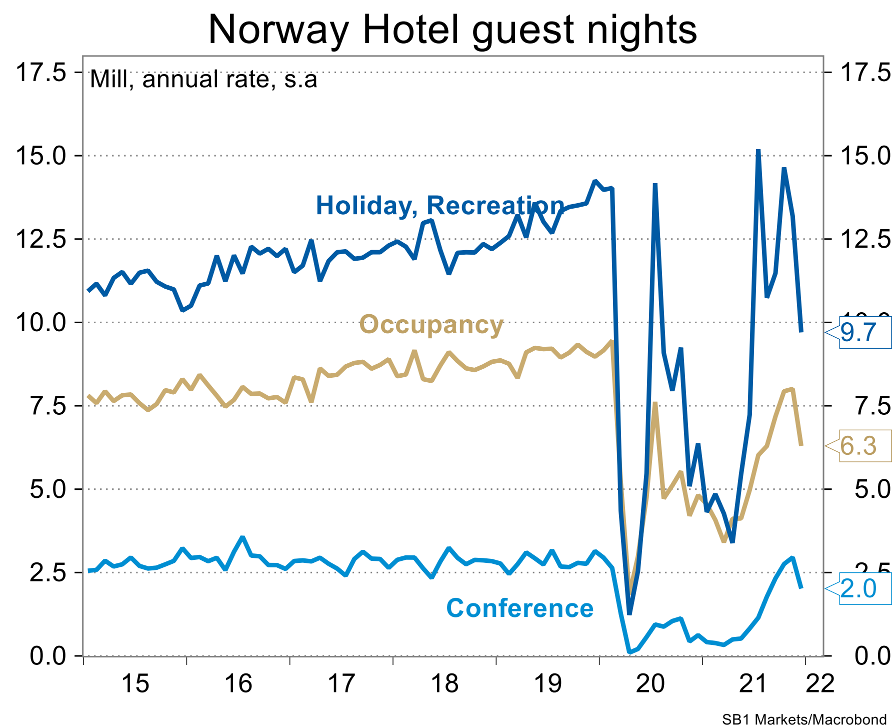


- Since 2015, **domestic internet sales** (not included direct import from abroad) have increased its market share to 8.6% from 4%, via 6% just before the pandemic, to 10% at the top in April. By now, the pre-pandemic trend would have yielded market share not far below 7%. Thus the pandemic gain has not been that impressive
- ICT equipment, cosmetics/drugs, clothing, food, and sports equipment are the 5 largest product categories sold from net outlets

An Omicron hit in December, hotel guest nights down 25%

Guest nights were back at normal level in Oct/Nov but were hit by restrictions again in December





- **The no. of guest nights** recovered quickly last year, as we are pretty sure traffic will resume to a normal level as soon after virus restrictions are fully lifted
- **Business guest nights** (sum occupation & conferences) had almost recovered before the Omicron wave, while **Recreational traffic** was equal to the 2019 average. As foreigners in total are down 20%, we <u>Norwegian recreational demand is far above the 2019 level</u>

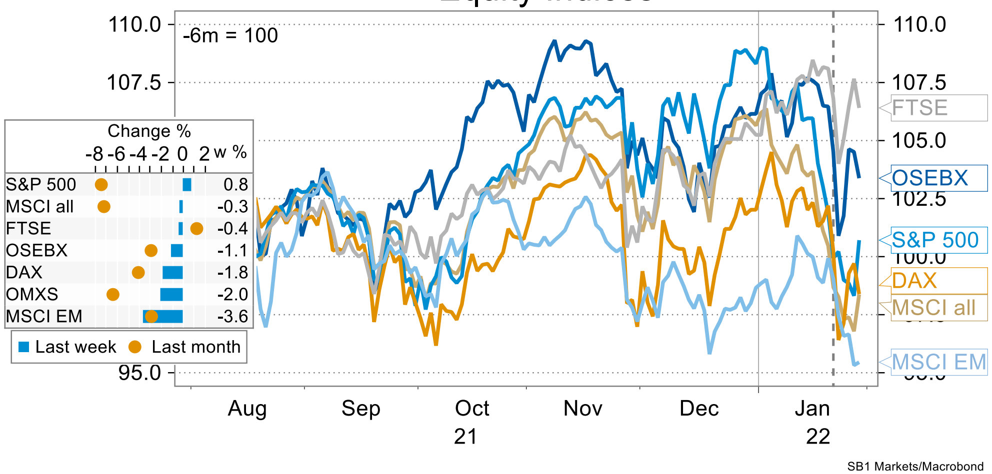
SpareBank 1 MARKETS

SpareBank 1 MARKETS

Very volatile markets, the S&P ended the week marginally up, others down

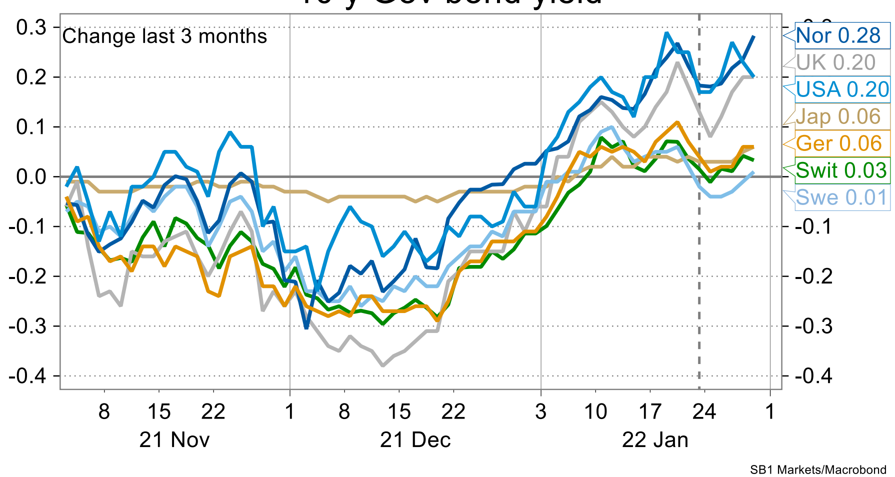
Bond yields up on a hawkish FOMC/Powell. Oil up to USD/b, but metals down – and the NOK flat

Equity Indices

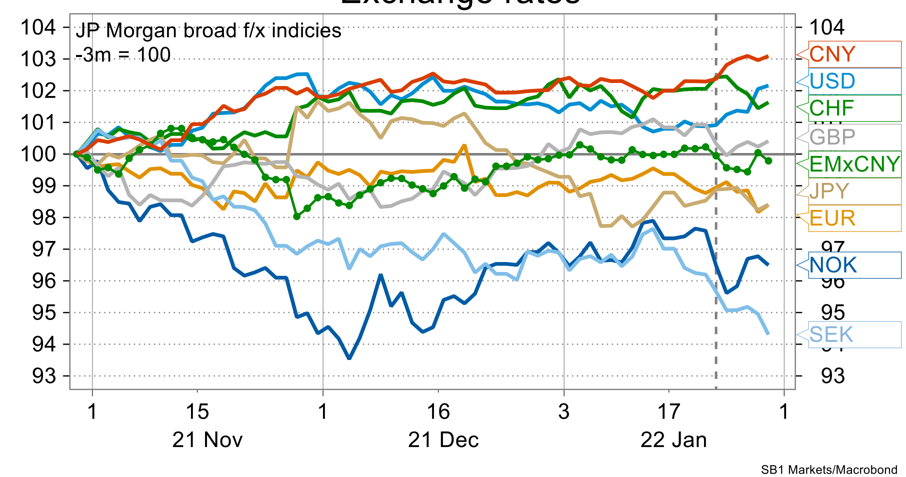


Oil vs. metals

10 y Gov bond yield



Exchange rates



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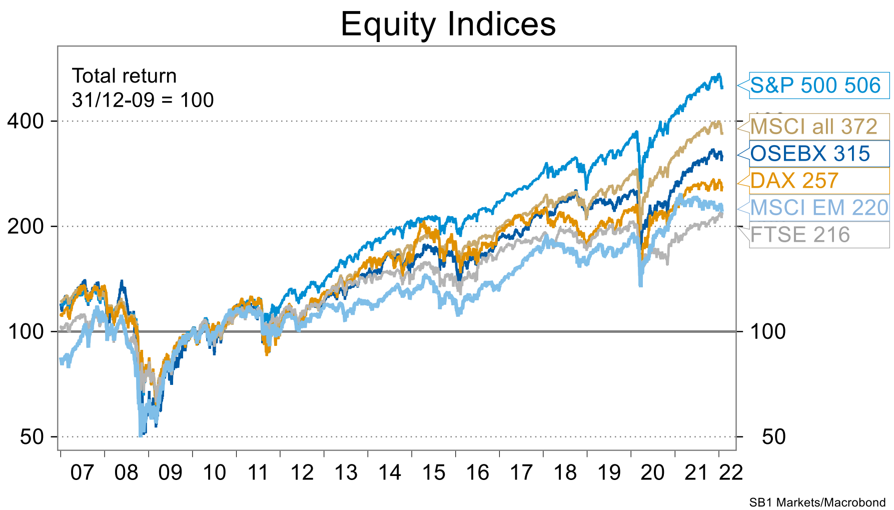
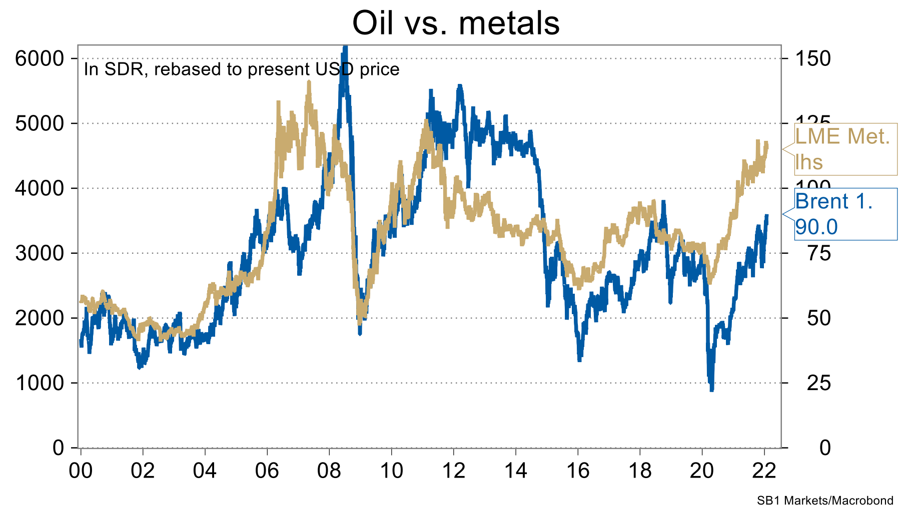
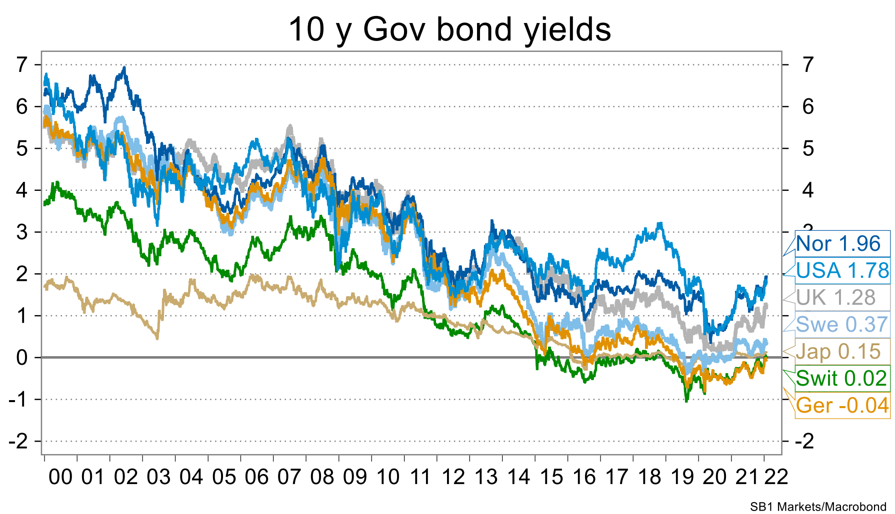
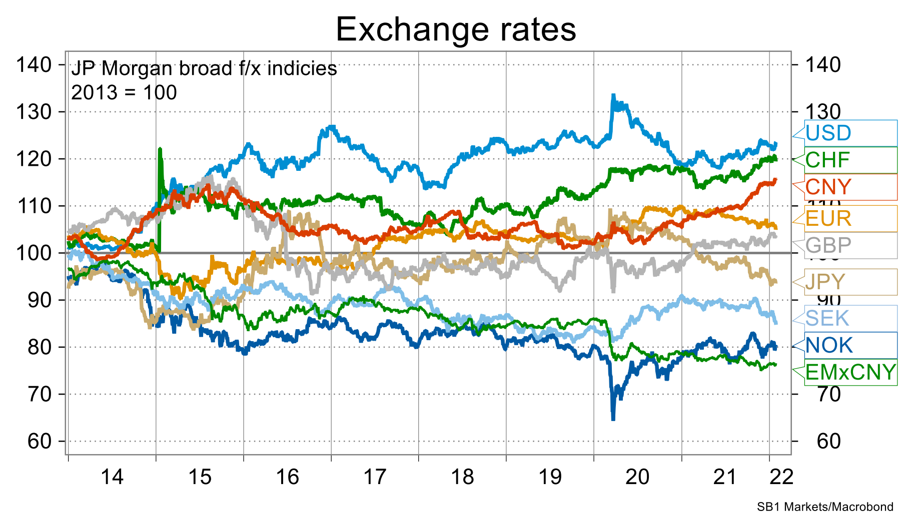
The big picture: Who is flying the highest?





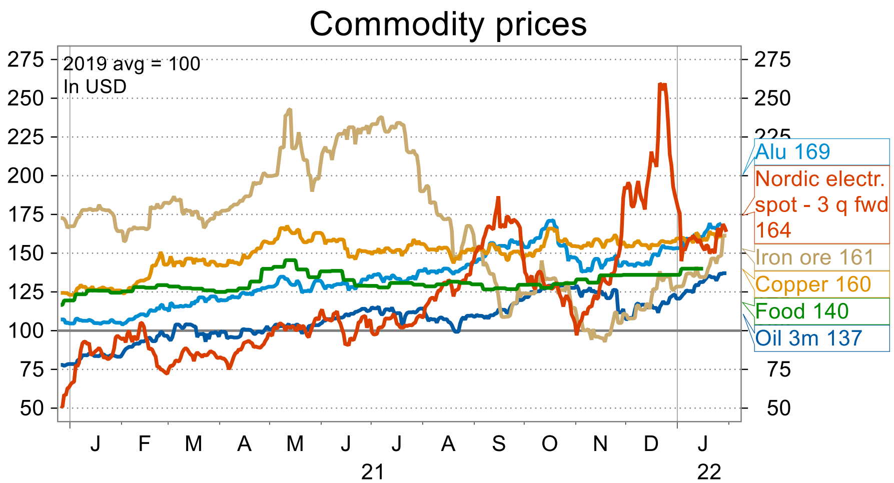


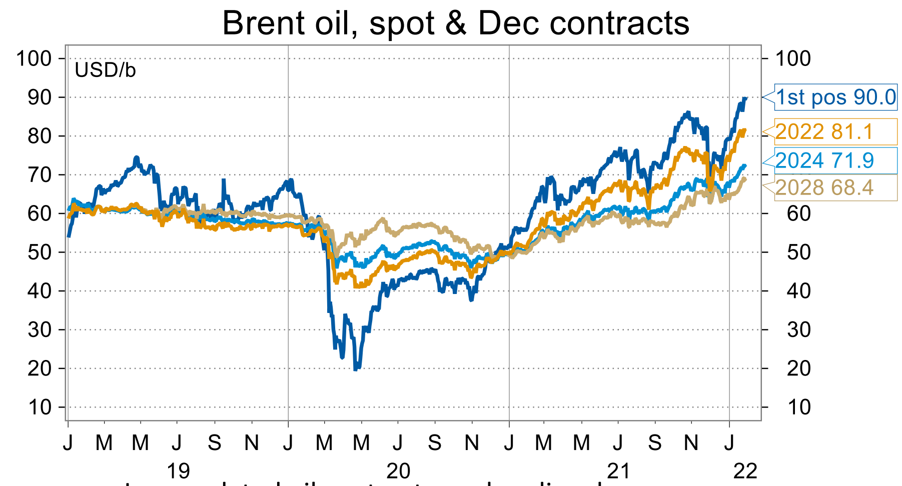


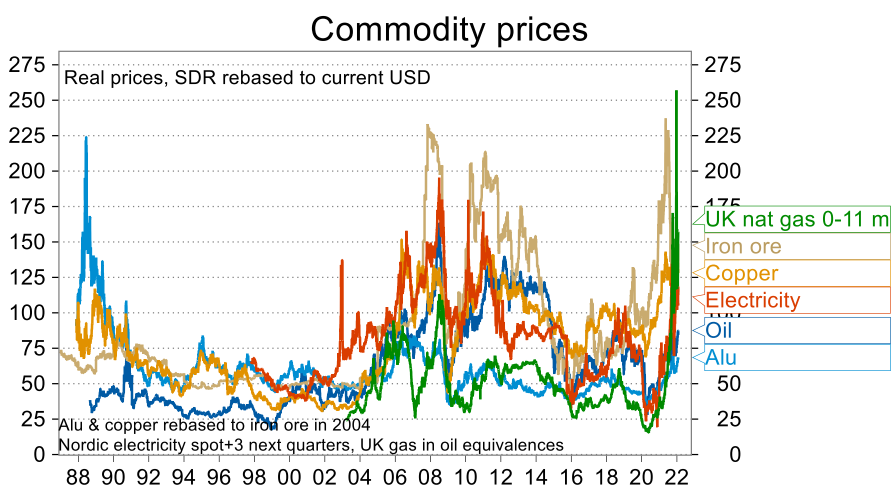
SpareBank 1 MARKETS

Commodities up last week, including the short end of the oil curve

Brent up to USD 90/b – partly supported by the Ukrainian situation. Iron ore prices further up!

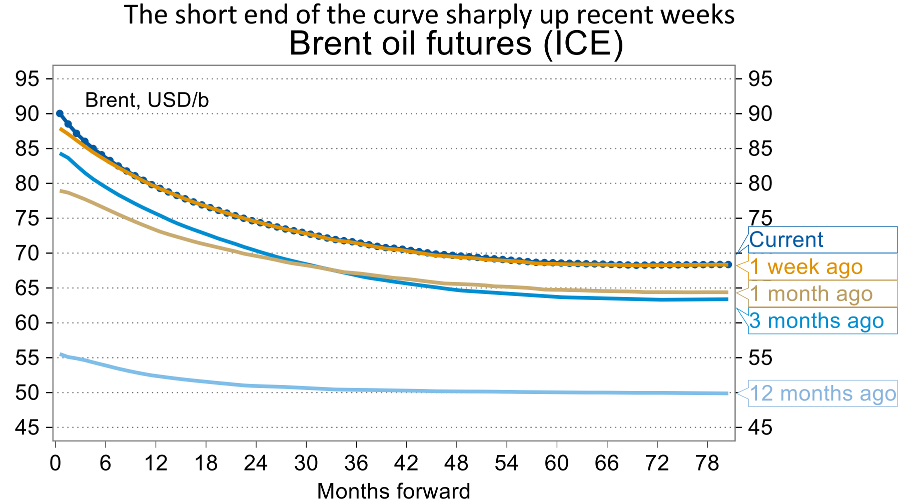






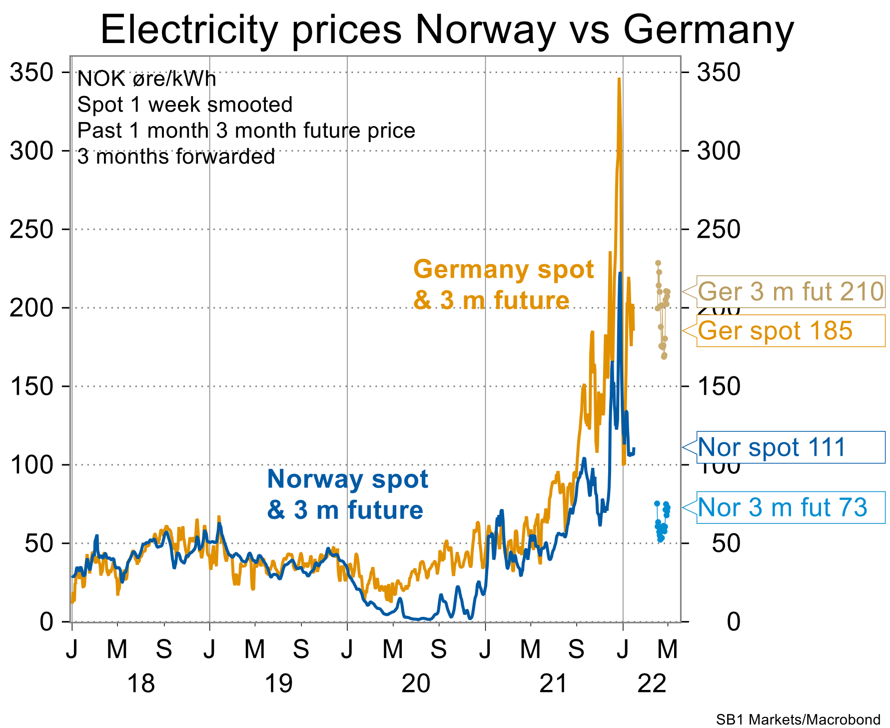
Longer dated oil contracts are heading down

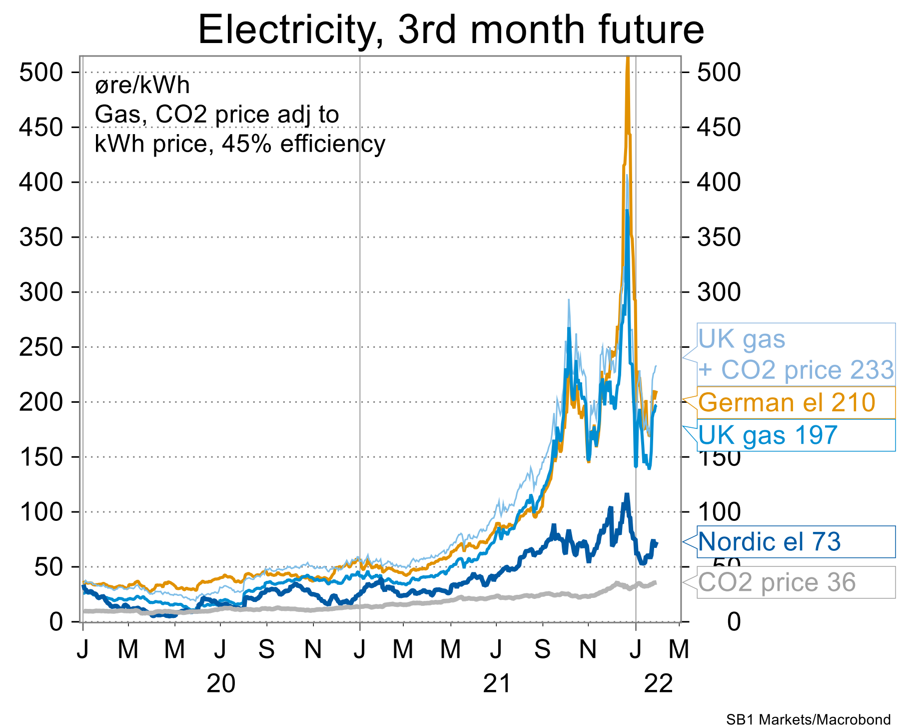
The short end of the curve sharply up recent weeks



European energy markets are still volatile, and further price rose last week

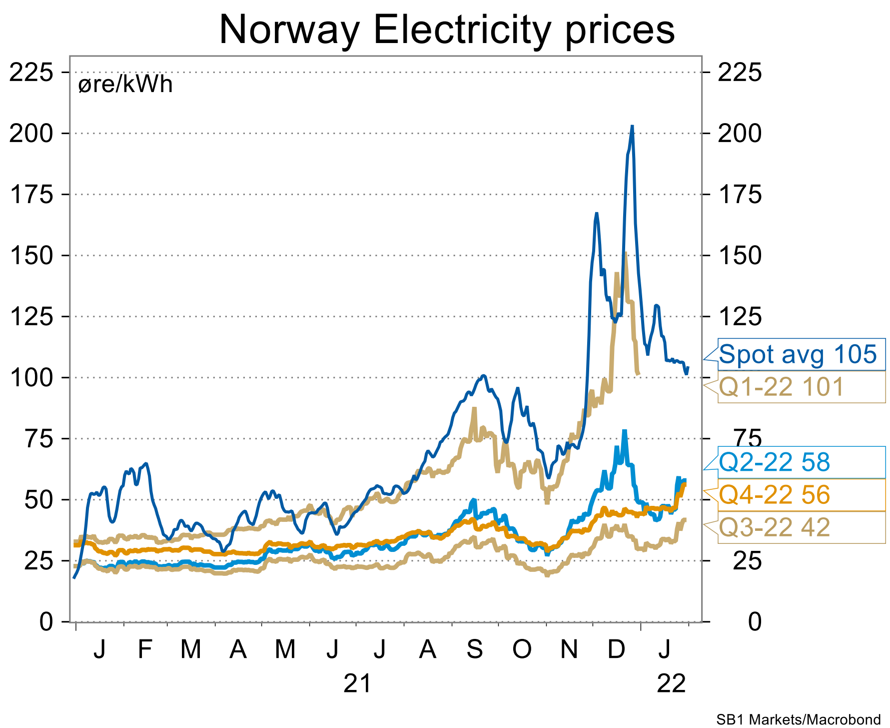
… but still well down from the peaks

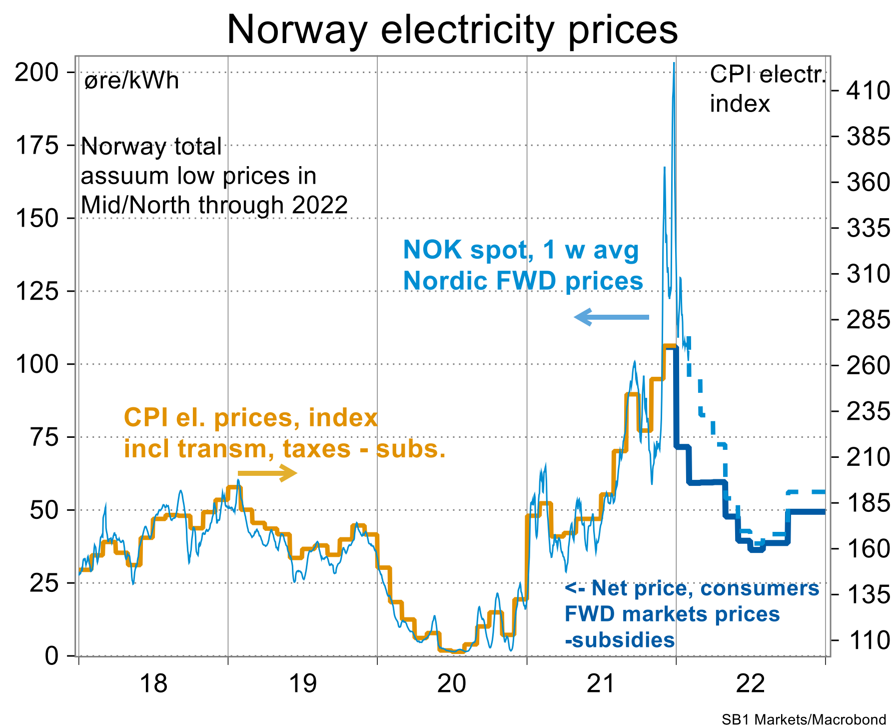




- Future European prices have fallen sharply recently but remains far above normal levels – and far above Nordic prices (which are too low??)

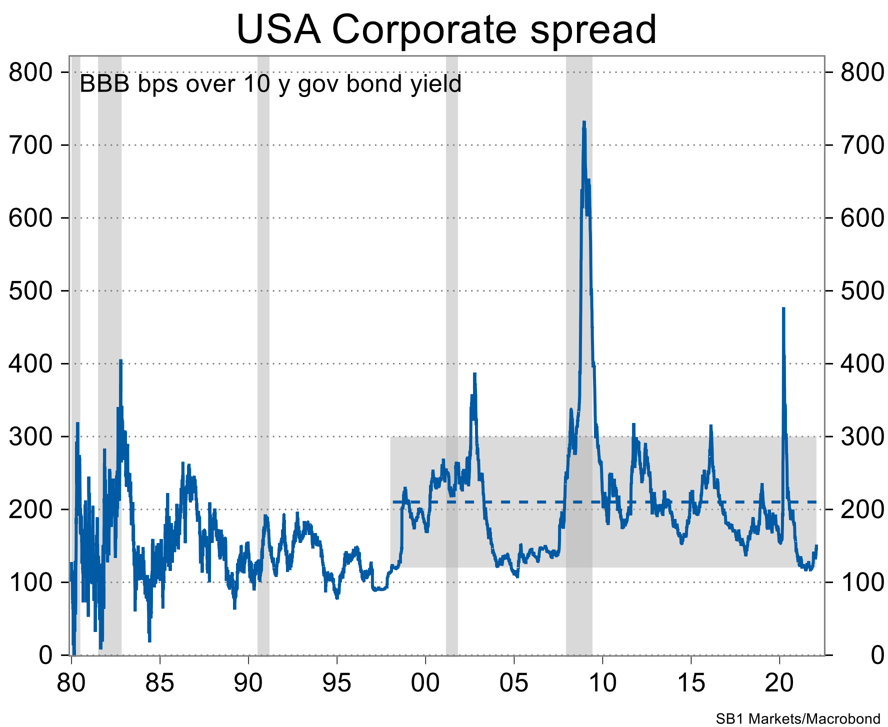
Norwegian electricity prices are sliding down but future prices are inching upw.

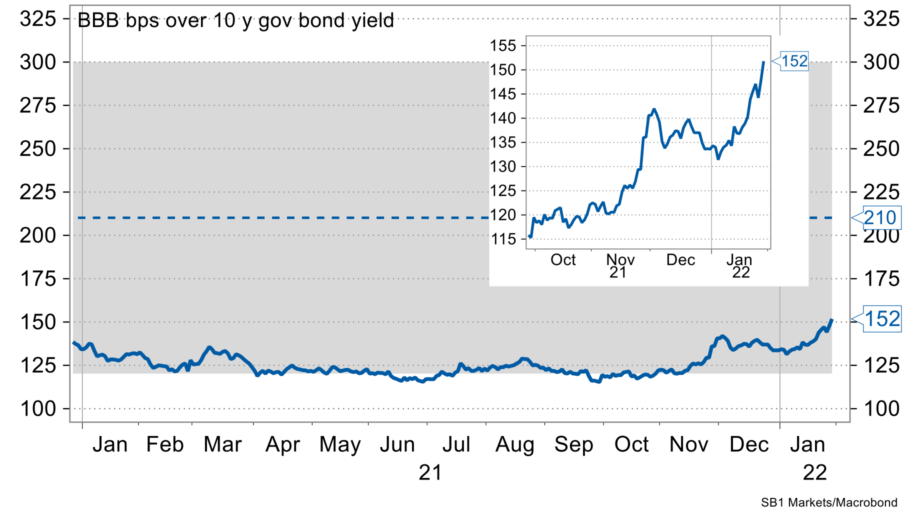


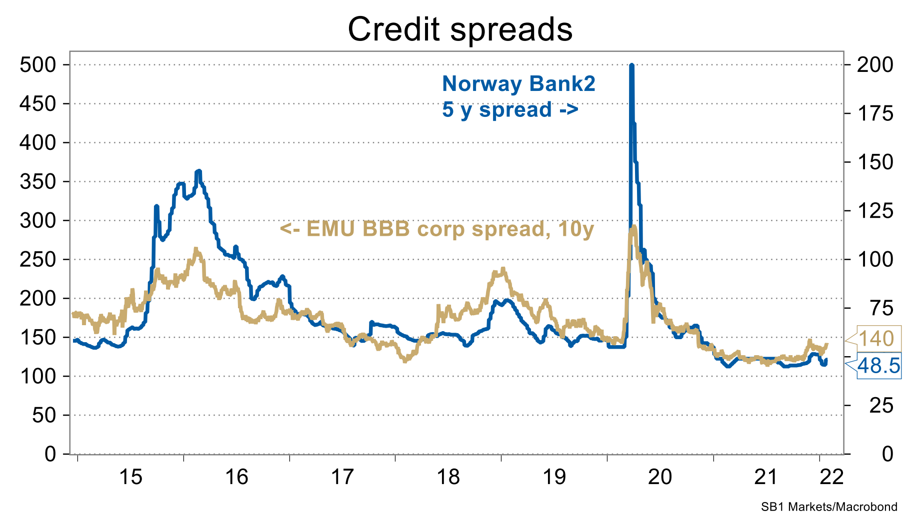


Credit spreads abroad visibly up last week too – risk off!

Norwegian spreads widened last week. The next leg is further upwards?







The NOK Bank 2, 5y spread widened 2 bps to 48.5

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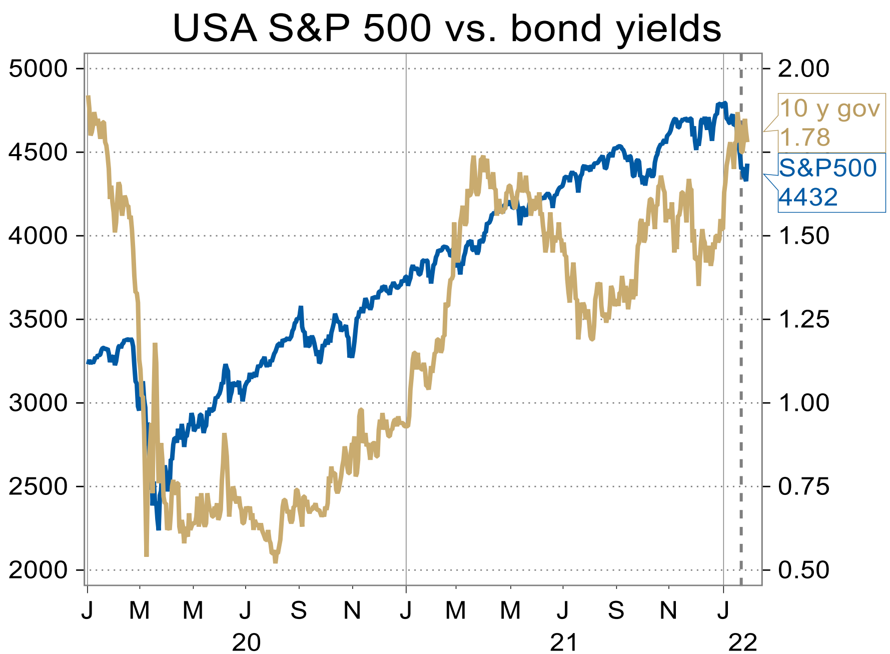
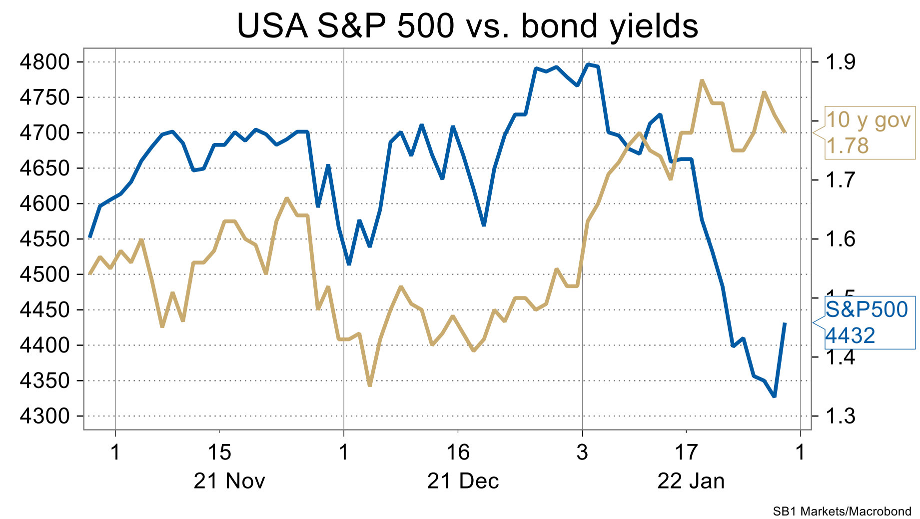
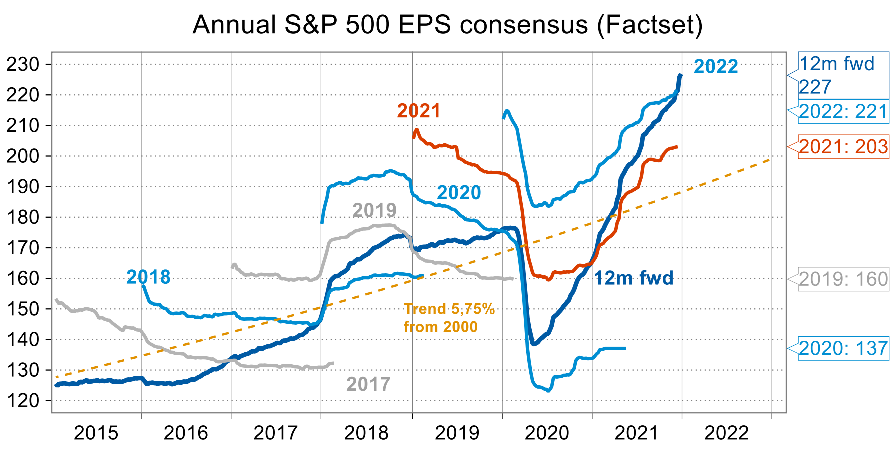
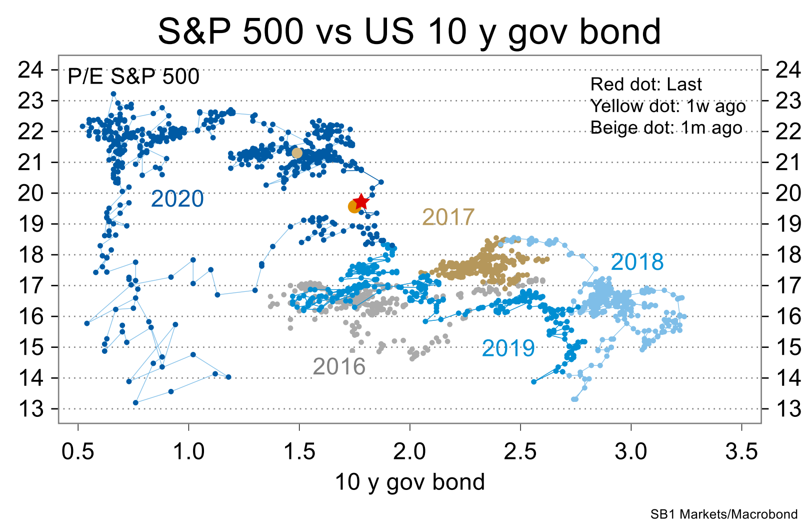
S&P 500 closed up 0.8% but after had been way down several times.

10 y bond yields up 3 bps to 1.78% - but almost tested 1.90 again on a hawkish Powell at Wednesday





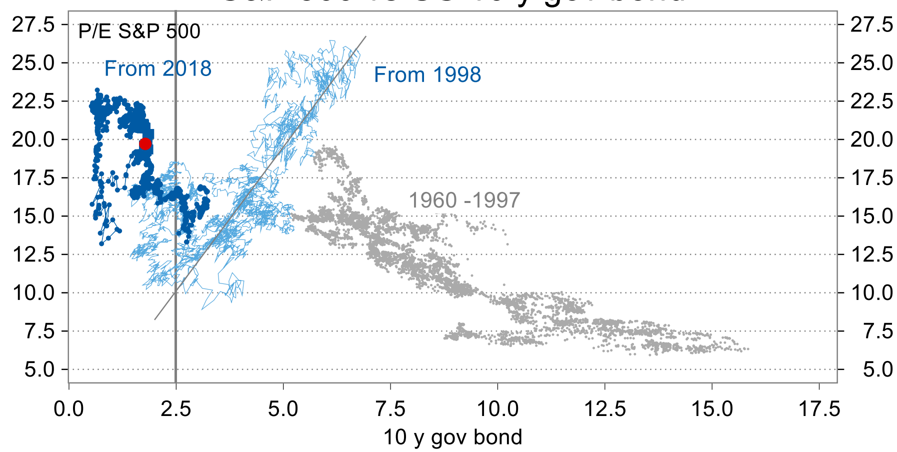




Bonds vs. equities: What's next?

Are we leaving the Goldilocks corner for the real (and much tougher) world?

S&P 500 vs US 10 y gov bond



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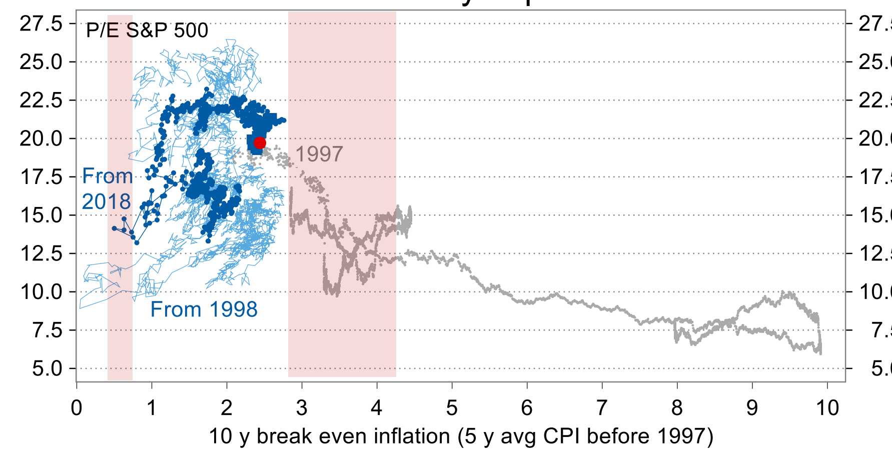
S&P 500 vs US 10 y expected inflation



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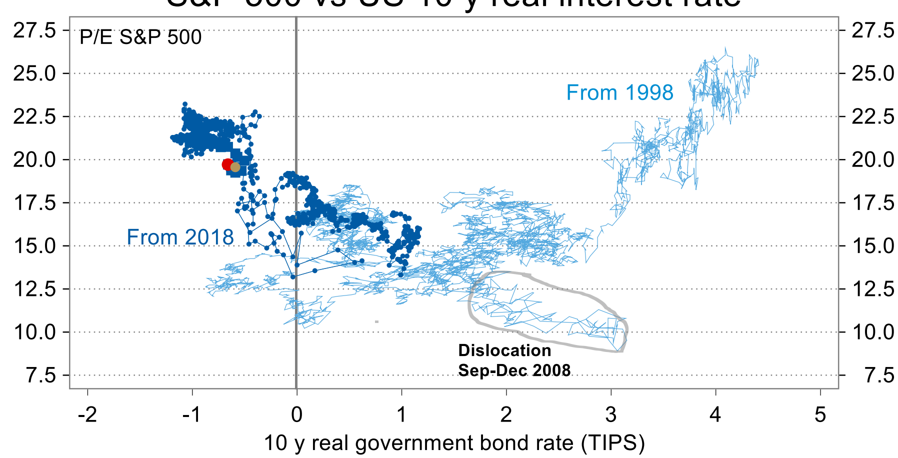
S&P 500 vs US 10 y real interest rate



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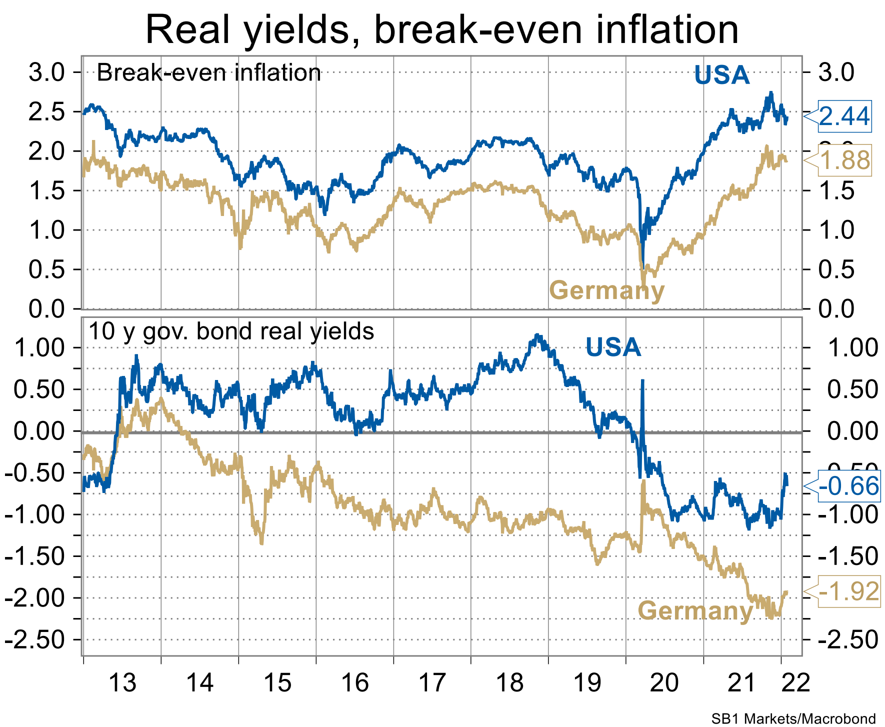
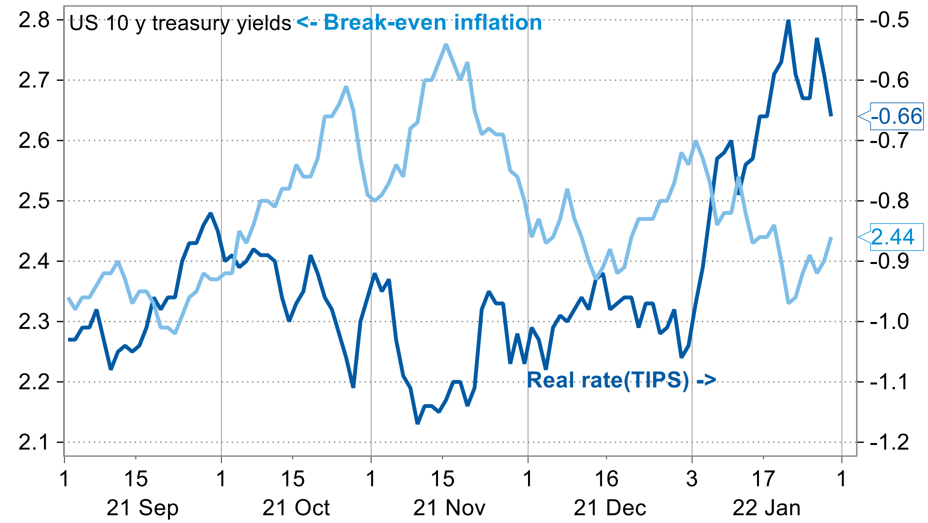
- **Expected inflation**
  - » ***If its not too low or too high: No problem***
    - 'Real' expected earnings are unaffected, higher inflation implies stronger growth in earnings, and vice versa
  - » ***If its too low or too high: A problem***
    - Something is rotten: Deflation or far too high inflation. The economy is not stable. Risk are increasing, earnings are exposed
- **Expected long term real interest rates**
  - » ***Low real rates normally not good news, high rates were OK***
    - Real rates were low when the economy was weak, the outlook uncertain
    - High real rates when the economy was booming, with high P/Es
  - » **Since 2018:** real rates have been low (and falling sharply) even if the economic outlook has been OK
    - Central banks wanted to lift growth, inflation was anyway not a problem – we entered the 'Goldilocks' corner'
    - The RISK now: Very low real rates may not stabilise the economy, and inflation has become too high
    - . WHERE IS THE WAY OUT?? Higher real rates, lower growth expectations and lower multiplies?

US real rates -7 bps last week, inflation expectations +10 bps (due to the oil price?)

The trends have been in the opposite directions since mid November





US & Germany 10 y Gov bond yield

	Yield	Change 1w	Change 1m	Min since April-20
USA nominal treasury	1.78	0.03	0.29	0.52
.. break-even inflation	2.44	0.10	-0.06	1.06
.. TIPS real rate	-0.66	-0.07	0.35	-1.19
Germany nominal bund	-0.04	0.02	0.19	-0.65
.. break-even inflation	1.88	0.01	-0.03	0.40
.. real rate	-1.92	0.01	0.22	-2.26

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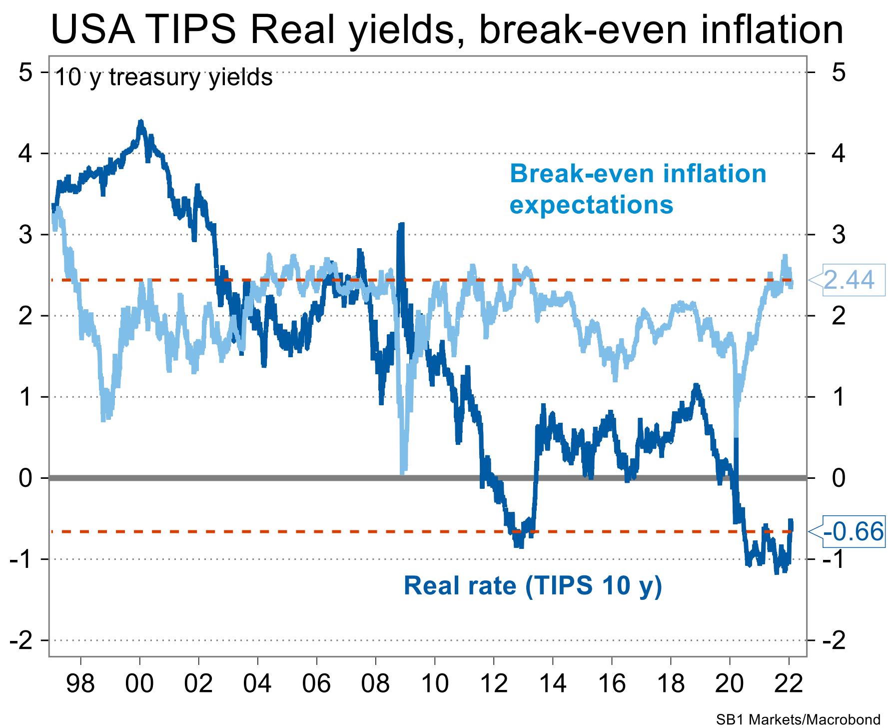
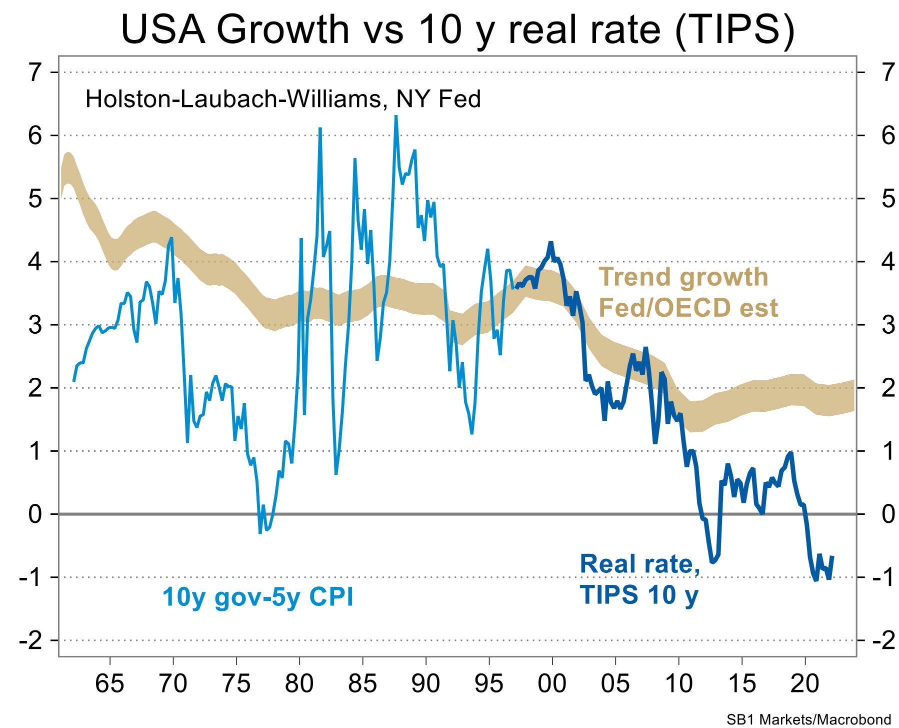
- **The 10 y TIPS real rate** has climbed 55 bps from the ATL last year
- 10 y inflation expectations have fallen by 30 bps past 3 months

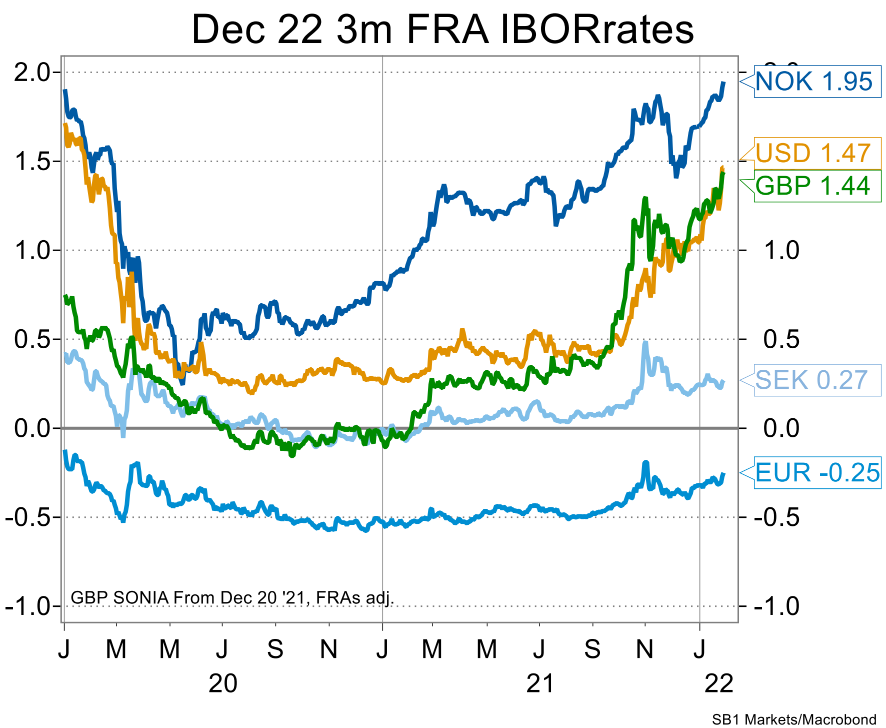
What if the gap between growth expectations and the real rate narrows further?

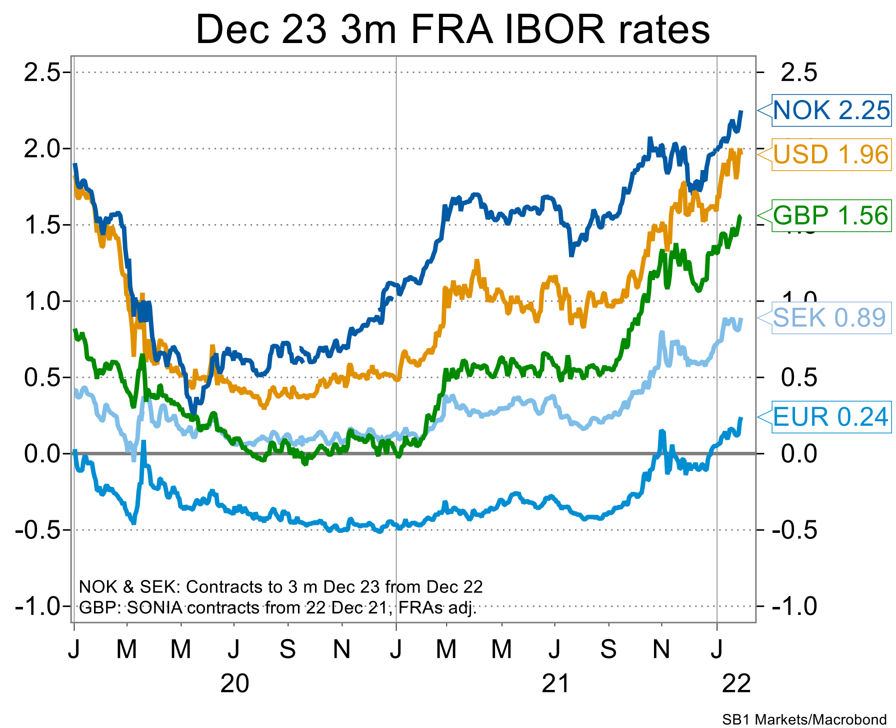




- Something is happening: The 10 y real TIPS rate is on the way up, now by 60 bps from the ATH last year

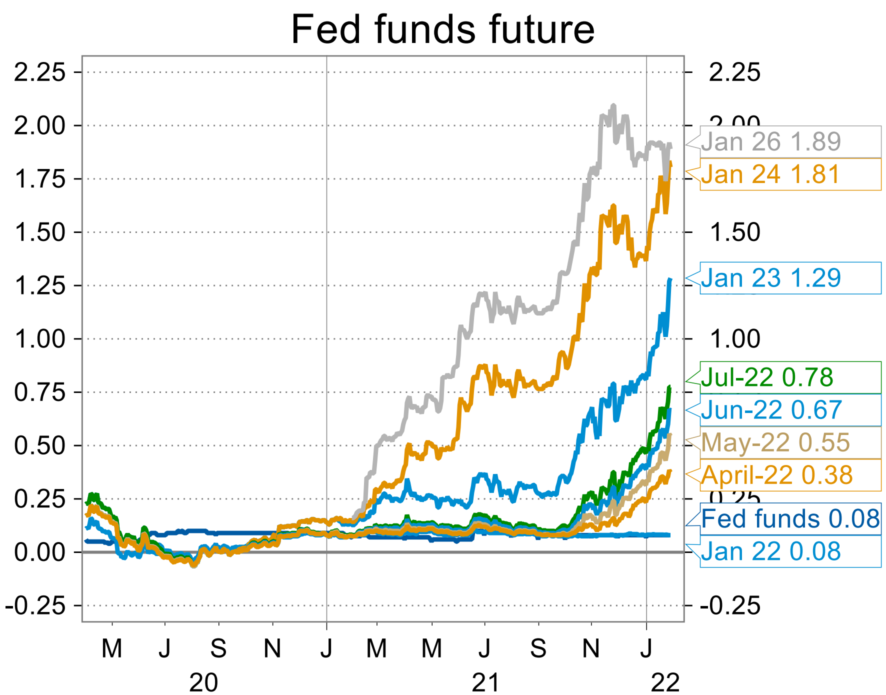
FRAs: The FOMC & Powell pushed US rates sharply up last week





63% probability for 5 or more hikes in 2022

If 25 bps hikes are assumed, but 50 bps are on the table. The short end of the curve has exploded



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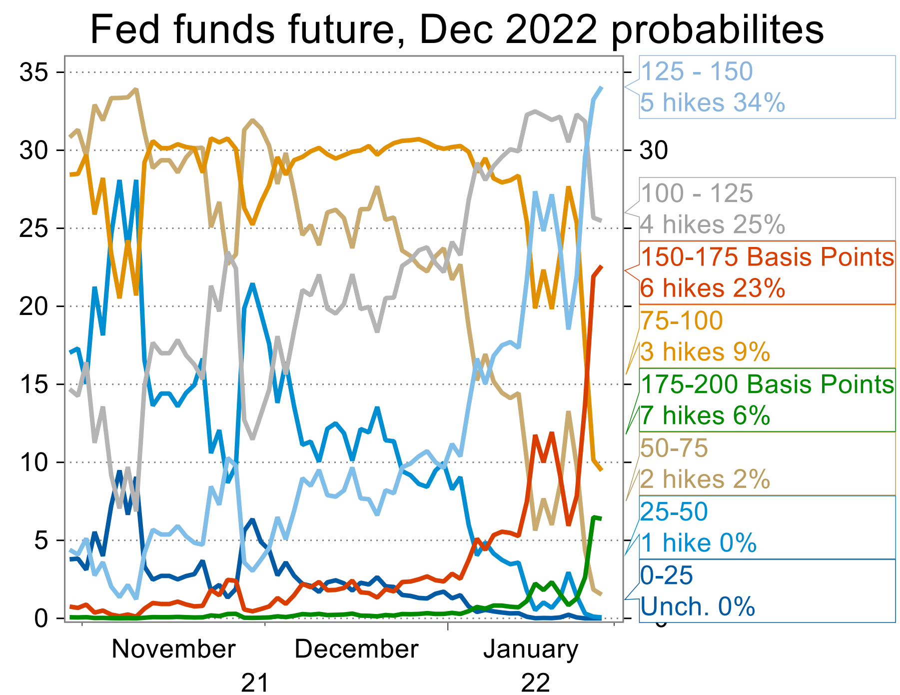

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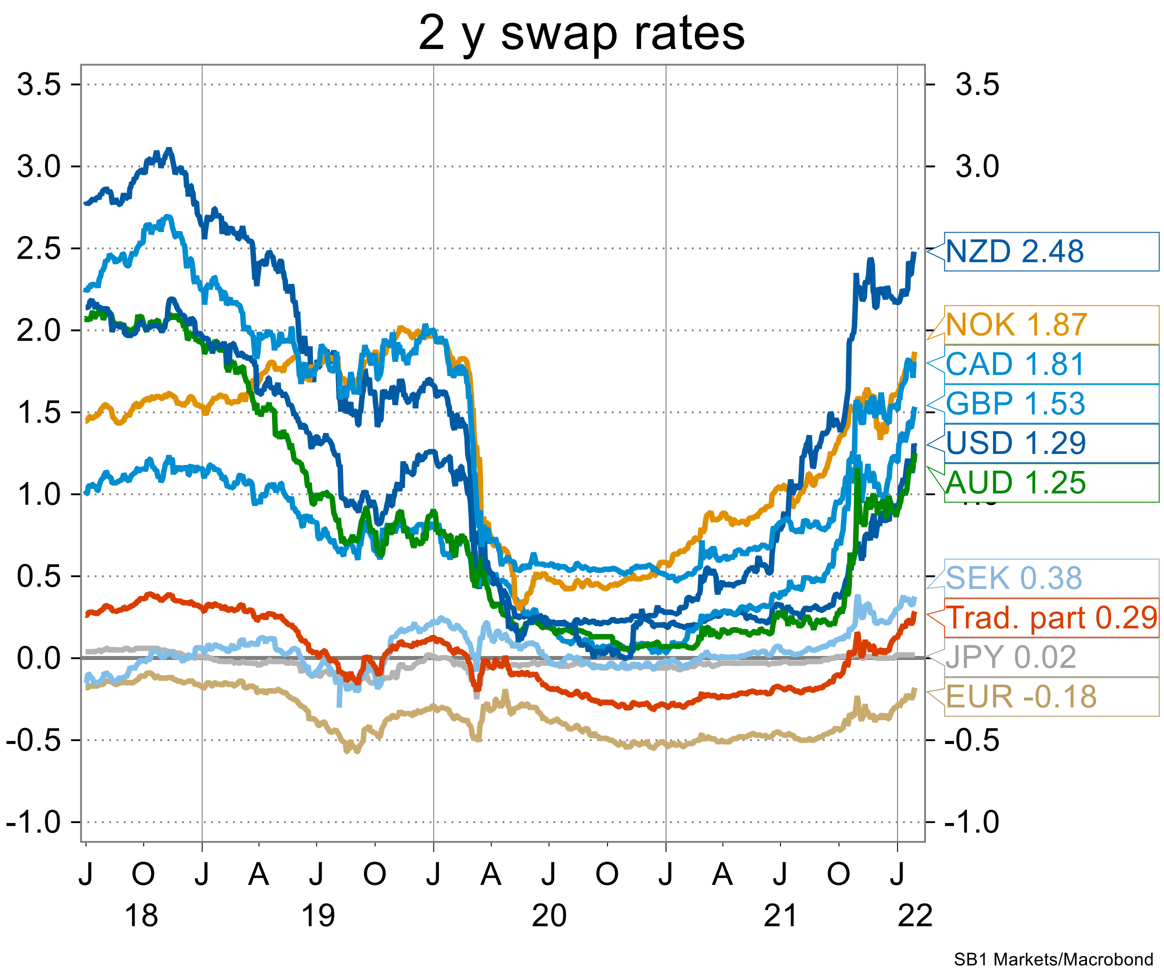
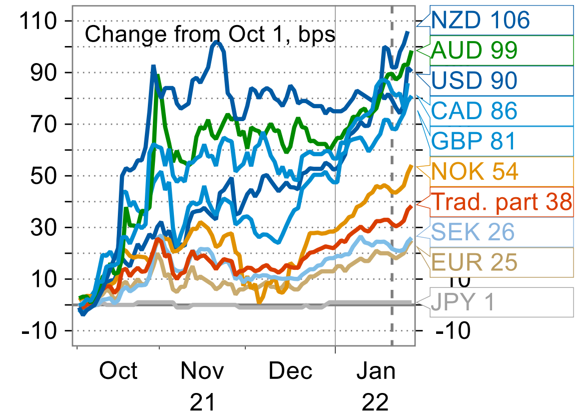
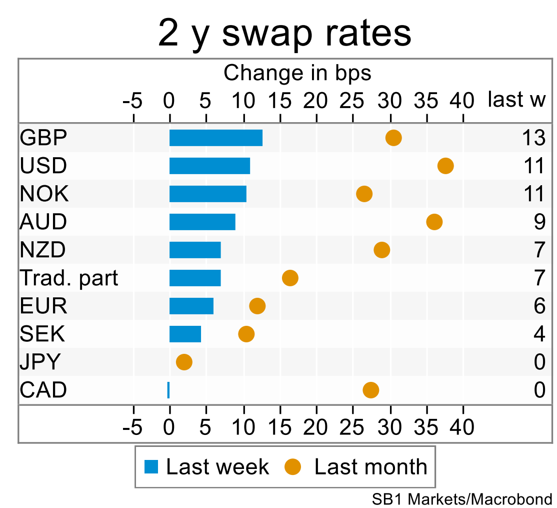
Short term rates further up, but more than 10 bps in USD, NOK







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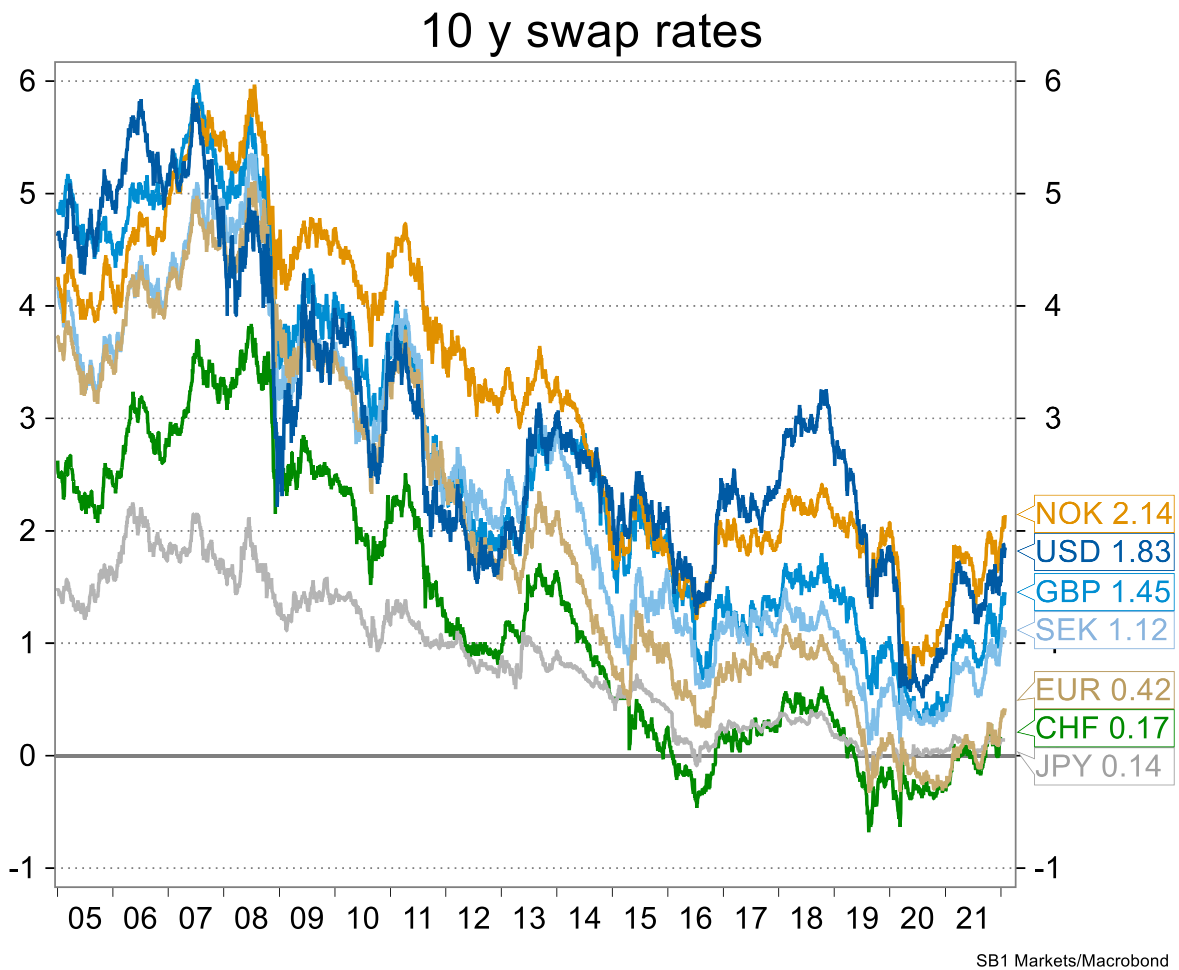
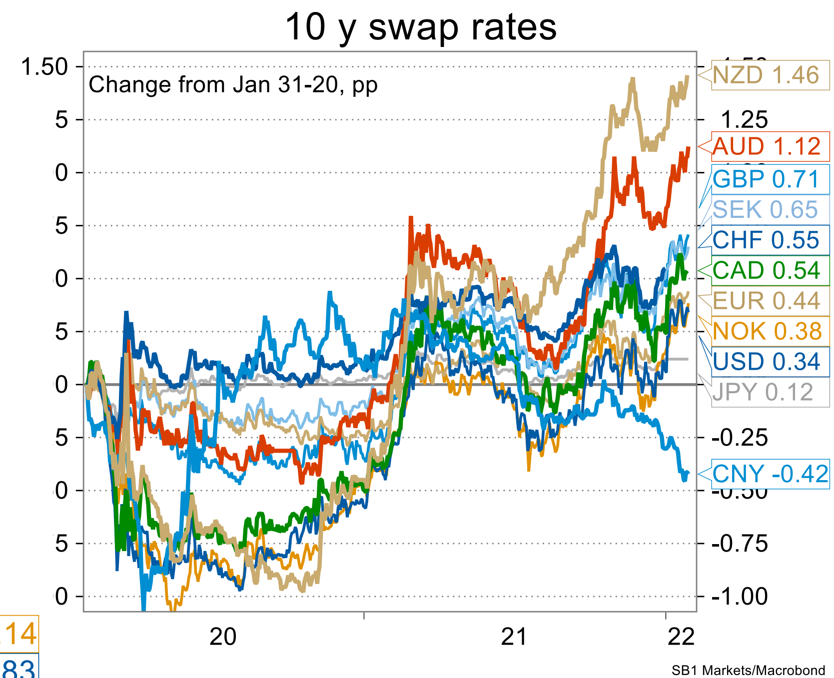
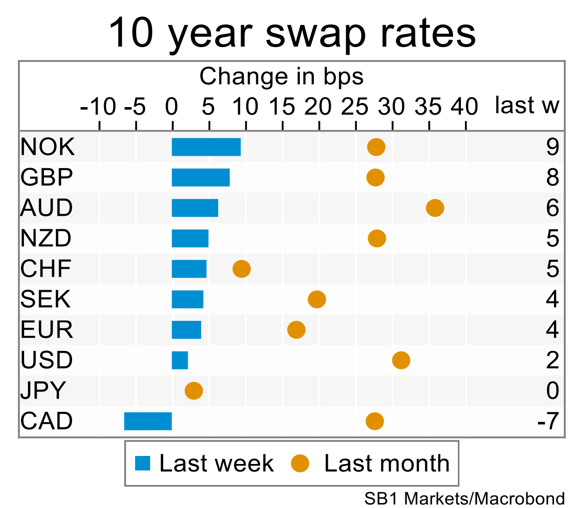
Mostly up again last week – and the trend is set?

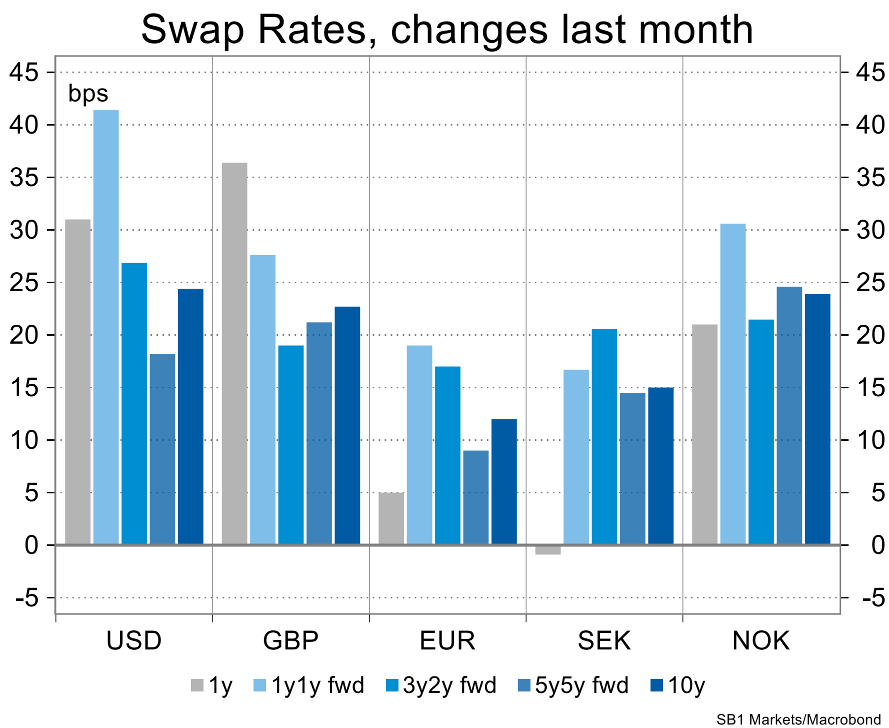


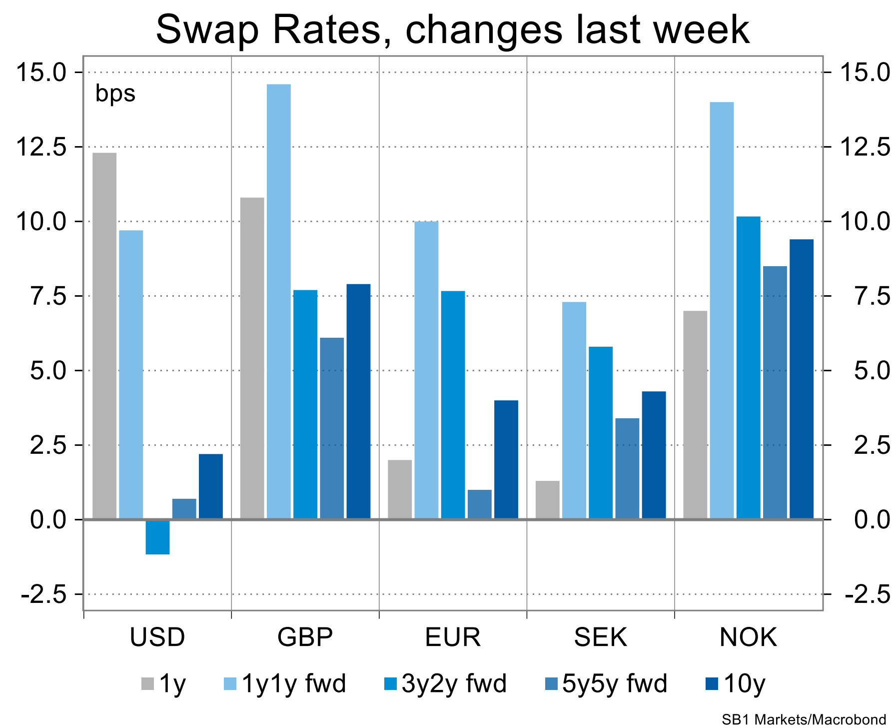




Another lift – except for a ‘strange’ decline at the mid segment at the USD curve

Norway in the lead last week

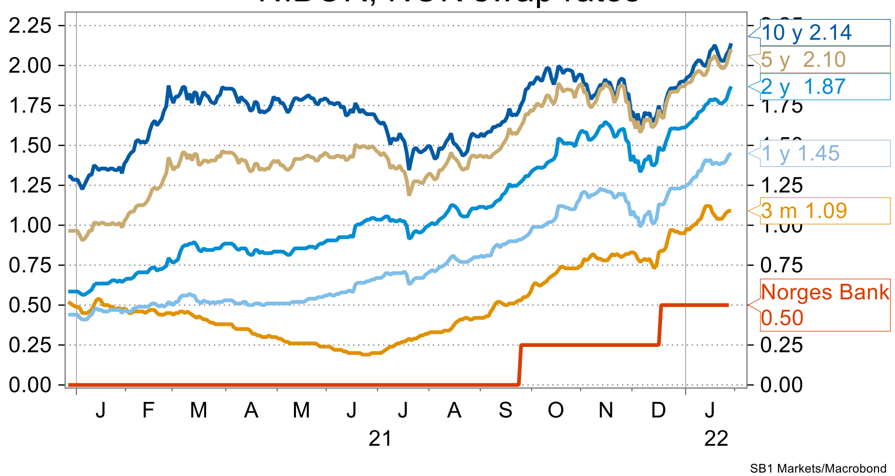




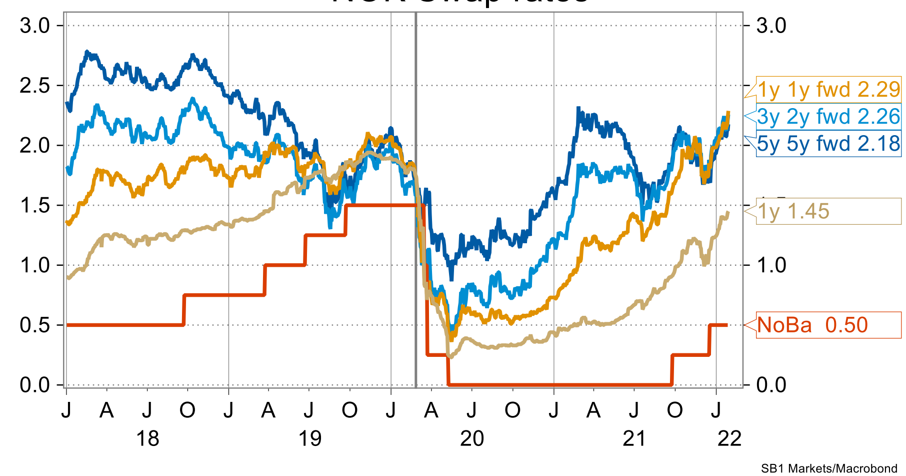
Up all along the curve last week, the 10 y up to 2.14%

The implied forward curve peaks at 1.5 – 2 year

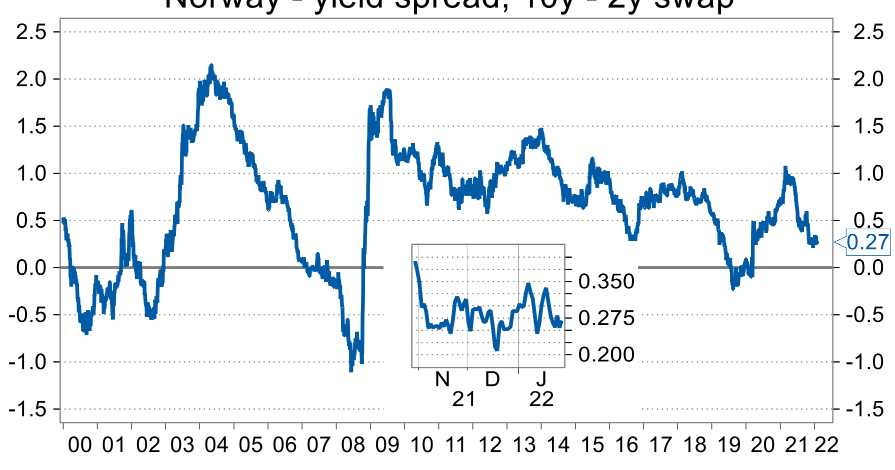
NIBOR, NOK swap rates



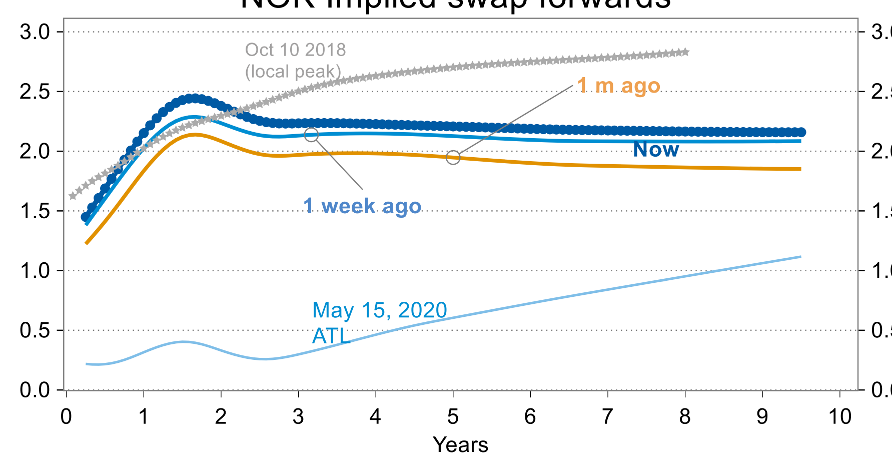
NOK Swap rates



Norway - yield spread, 10y - 2y swap

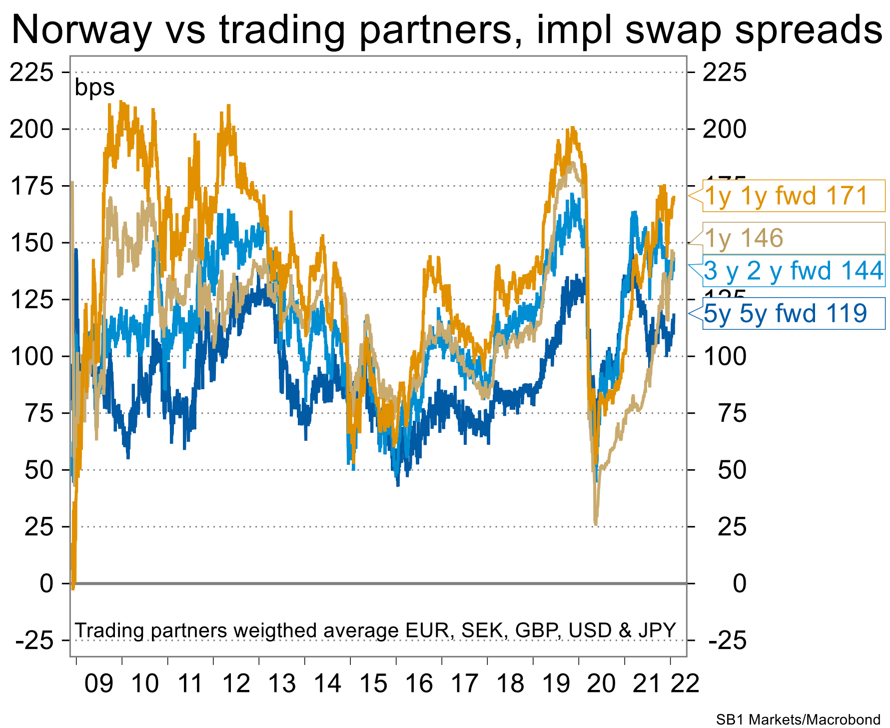


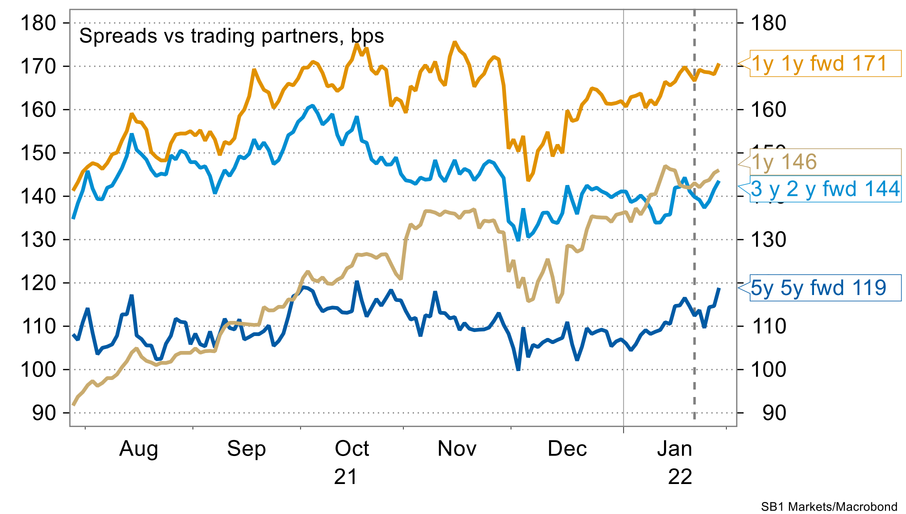
NOK Implied swap forwards

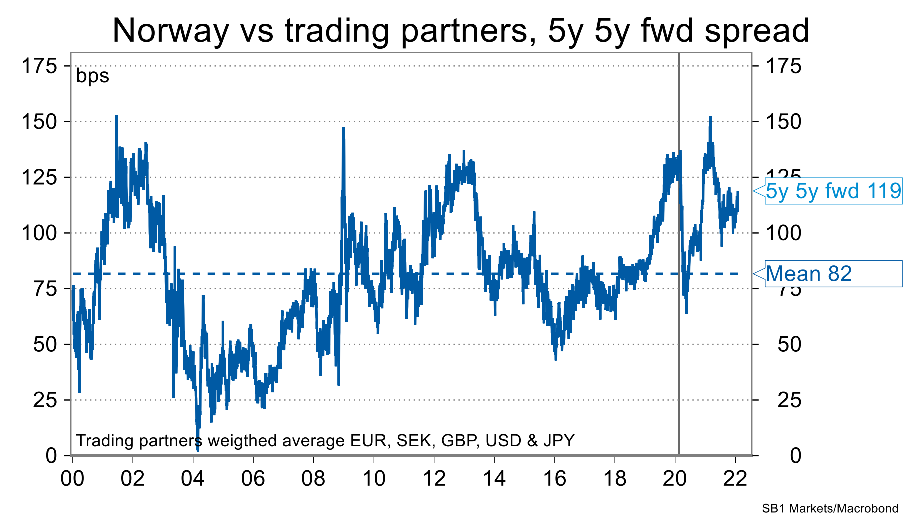


Spreads further out last week

Spreads are at the high side – but we do not have a short term narrowing case

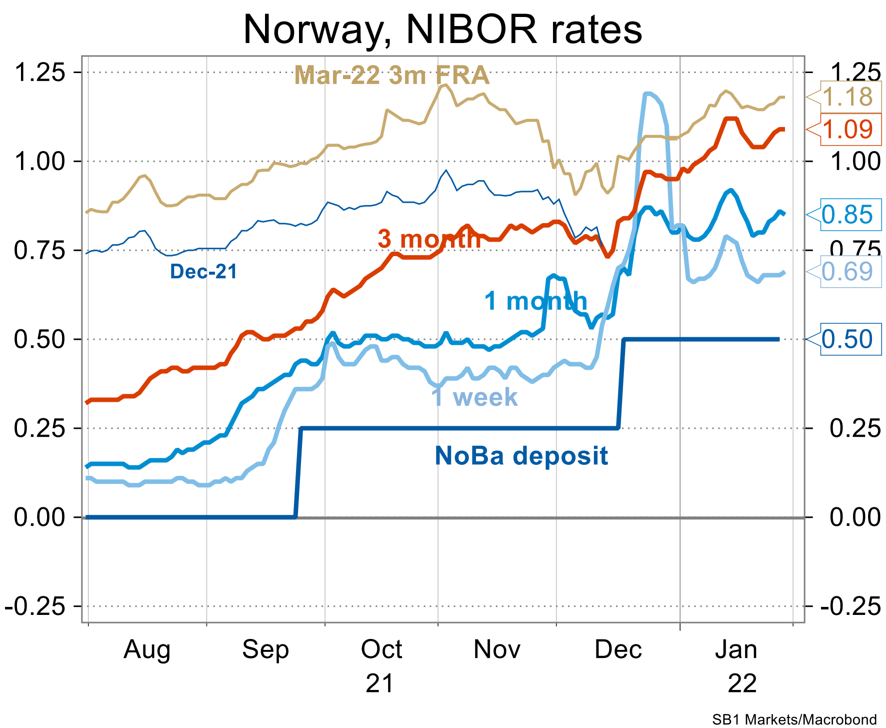


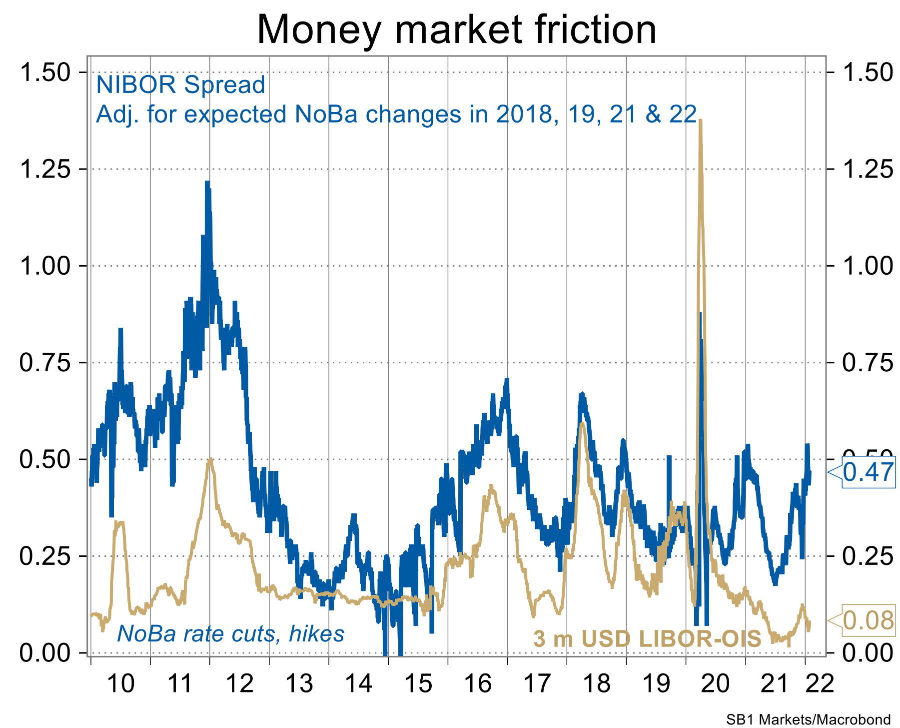




The 3m NIBOR up again, + 5bps to 1.09%

The NIBOR spread +3 bps to 47 bps, if we take a NoBa March hike for granted

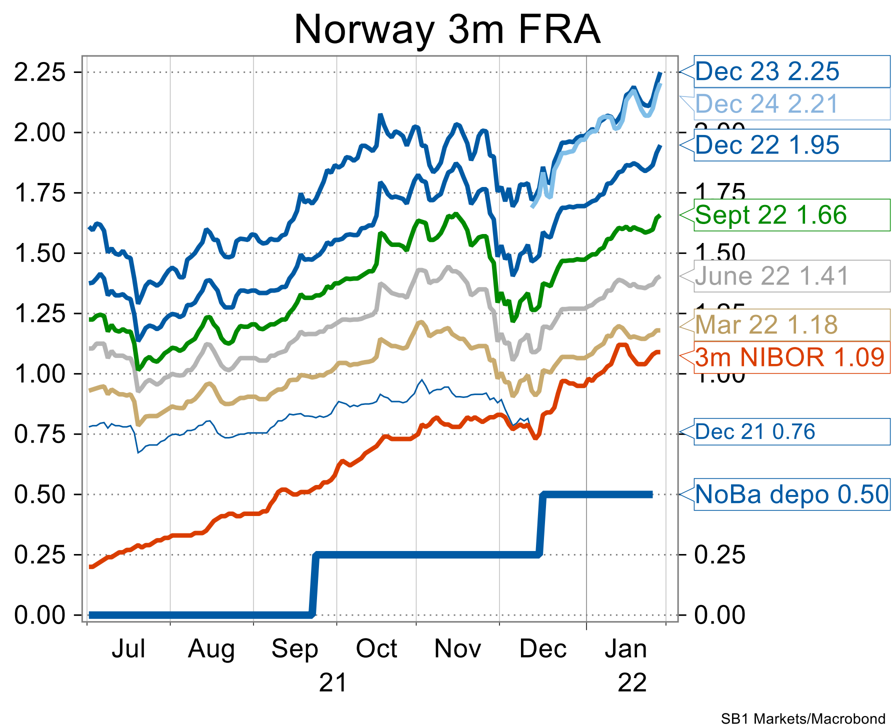


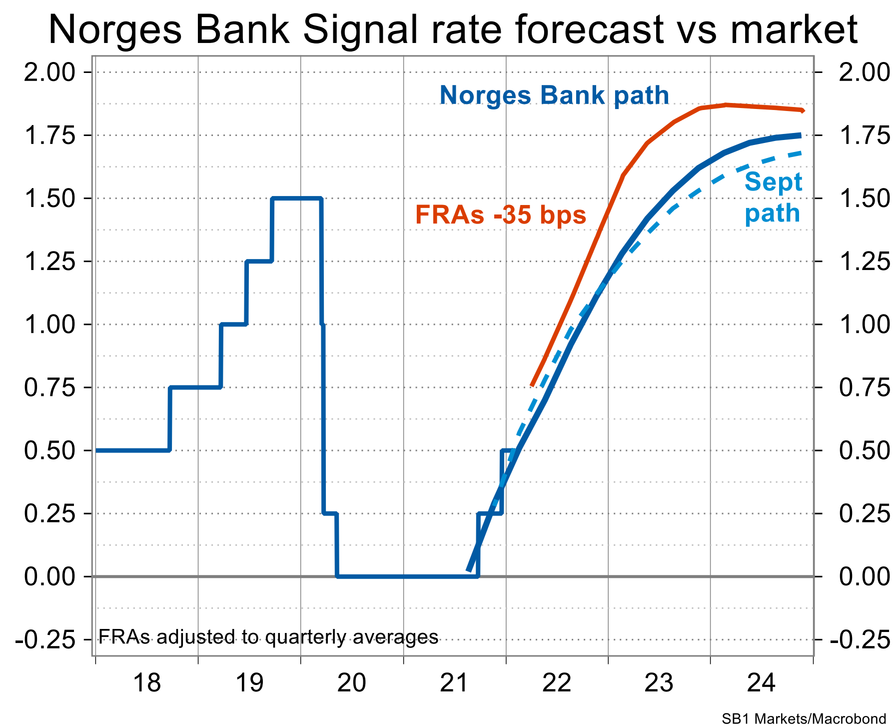


- The **3 m NIBOR** has been at elevated level recent weeks but the market calmed down when NoBa offered an F-loan to banks two weeks ago – as we expected the bank to do
- The **USD LIBOR-OIS spread** rose to 13 bps from 4 bps from October to end of December. Now it is back to 8 bps, not far above a record low level (but 2 bps up last week)

FRAs up by up to 13 bps last week, the curve is far above NoBa's

Which is reasonable, given the change in the interest rate climate (and so far strong economies)

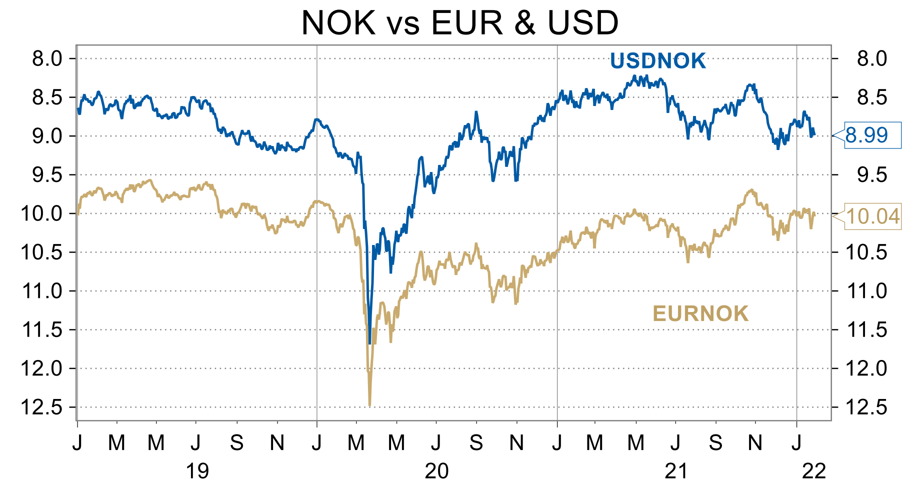


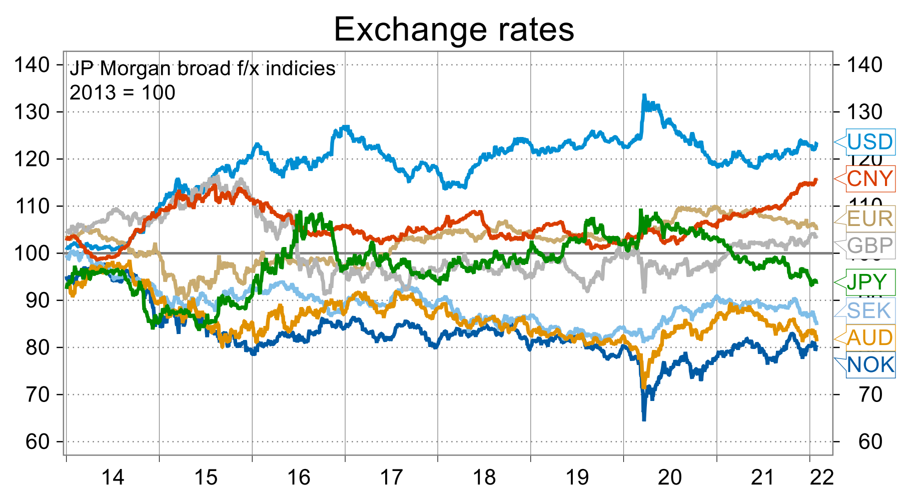


- Market FRAs are now discounting a steeper interest rate path than NoBa presented in December – <u>or the expected NIBOR spread widened substantially</u>
- If NoBa hikes March 24, the average NoBa rate will be 0.73% in the March FRA period
- Thus, the **March-22 3 m** contract at 1.18% implies 100% probability with a 45 bps NIBOR spread – or less than 100% of the expected spread is higher
- **NoBa's path** implied a 75% probability for a March hike, which we thought was a bit to cautious. So does the Bank? A March hike was strongly signalled last week

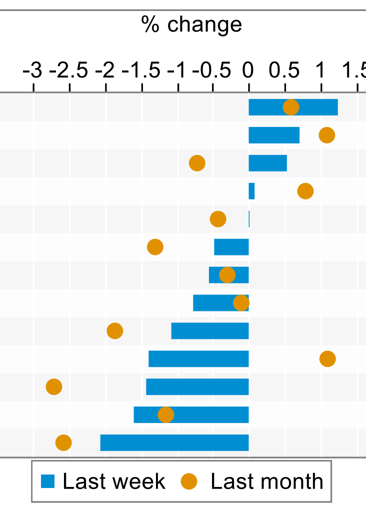
The USD up 1%, supported by the Fed? The EUR down

NOK flat, even if CAD, SEK and AUD fell significantly. An oil price at USD 90 helps?





F/x markets



JP Morgan f/x broad indices + 3 f/x crosses	Last week	Last month
USD	1.2	0.6
CNY	0.7	1.1
NOKEUR	0.5	-0.7
GBP	0.1	0.8
NOK	0.0	-0.4
JPY	-0.5	-1.3
EUR	-0.6	-0.3
CHF	-0.8	-0.1
USDNOK	-1.1	-1.9
CAD	-1.4	1.1
SEK	-1.4	-2.7
EURUSD	-1.6	-1.2
AUD	-2.1	-2.6

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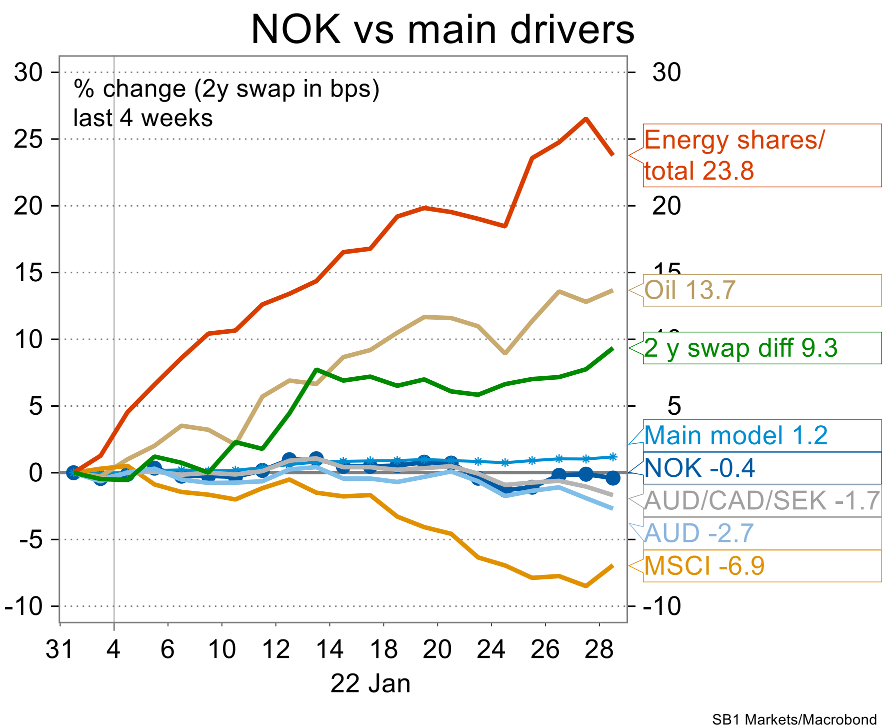
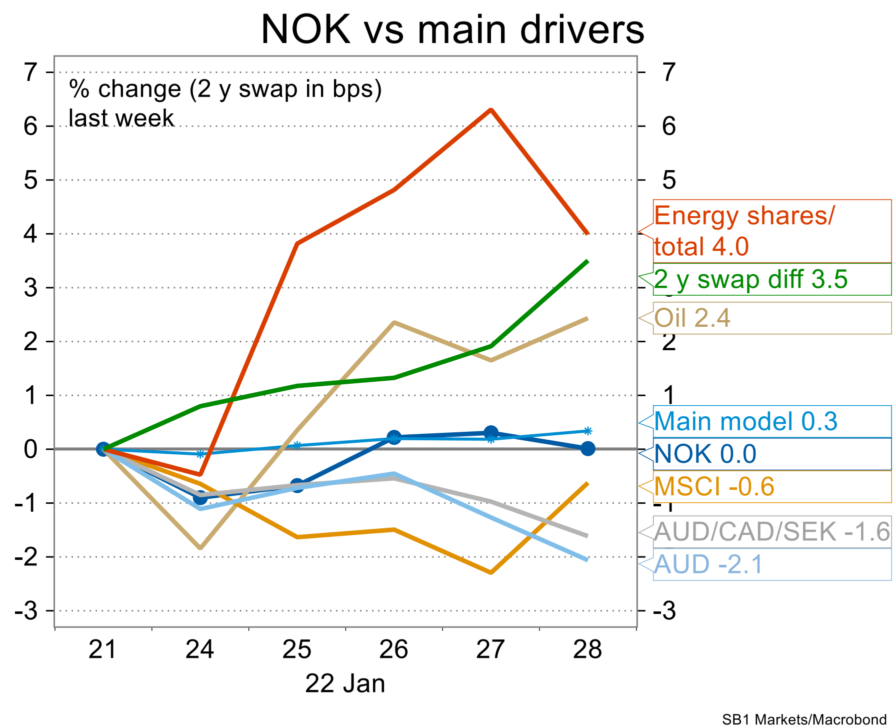
NOK flat last week, our model signalled an 0.3 strengtening

The oil price rose further, as did the interest rate spread. Global stocks fell, but not energy companies



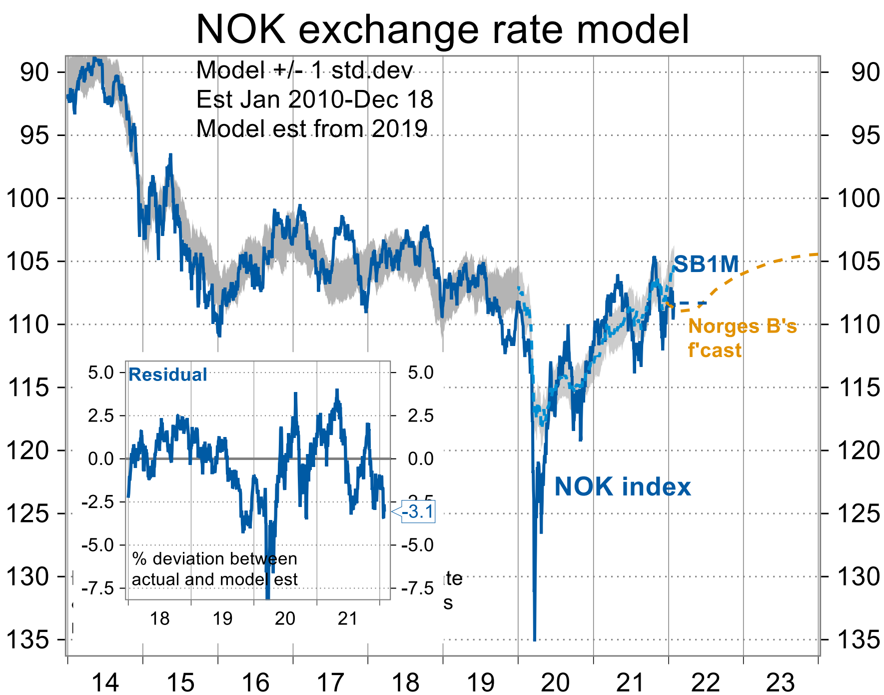


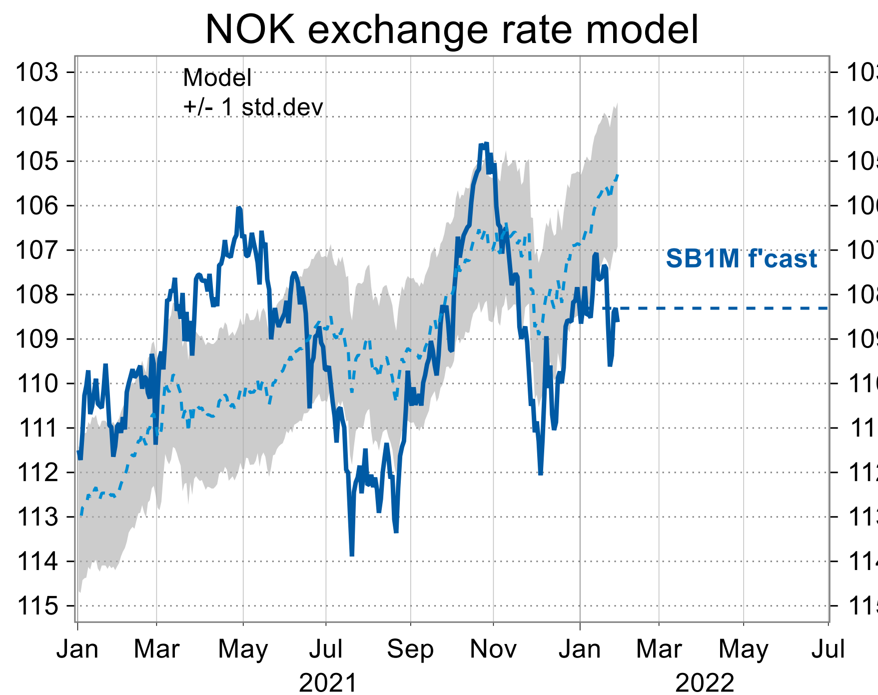
The status vs. the normal drivers:

- ***The NOK unch- The level 3.1% below the model est (from -2.7%)***
- The NOK is 4% <u>weaker</u> than our AUD/CAD/SEK-model, our 'super-cycle peers', predicts (unch). The AUD fell 2.1% last week!
- NOK is 4% <u>stronger</u> than a model which includes global energy companies equity prices (vs the global stock market), but less than last week (from 5%)

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 f/x crosses. There are no substantial difference between these two indices over time

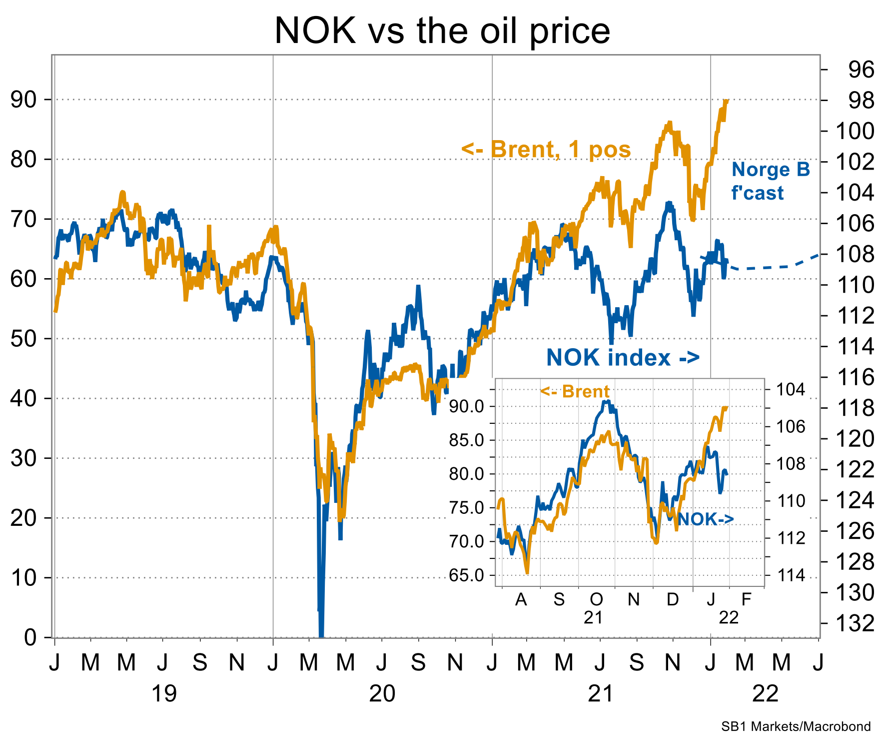
NOK lags our model again, by 3.1%, up from 2.7% the previous week

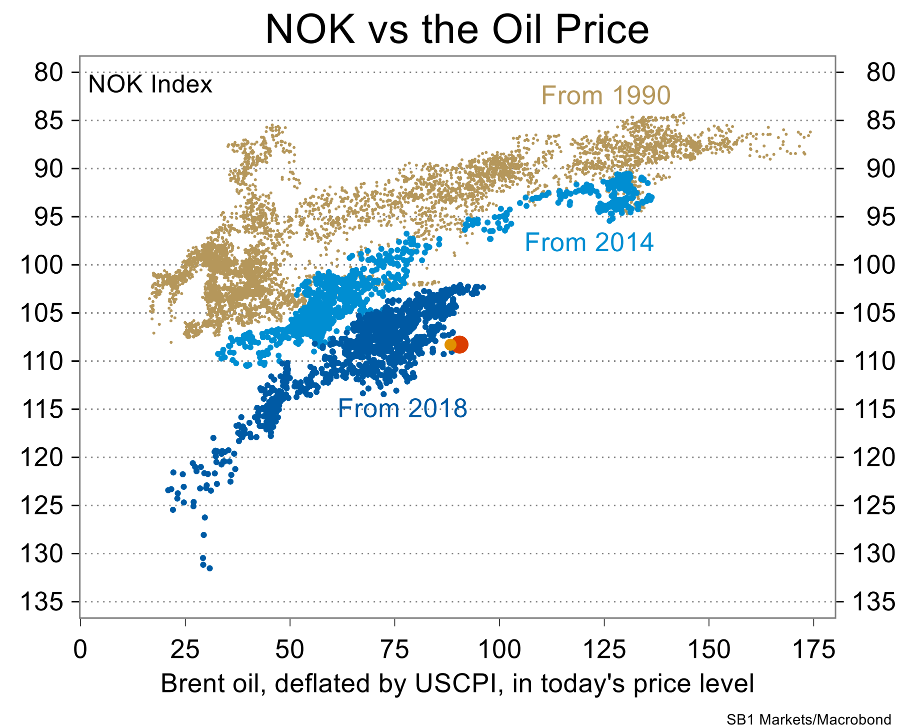




The gap to the oil prices widened further last week

But the NOK did not decline, like our f/x peers

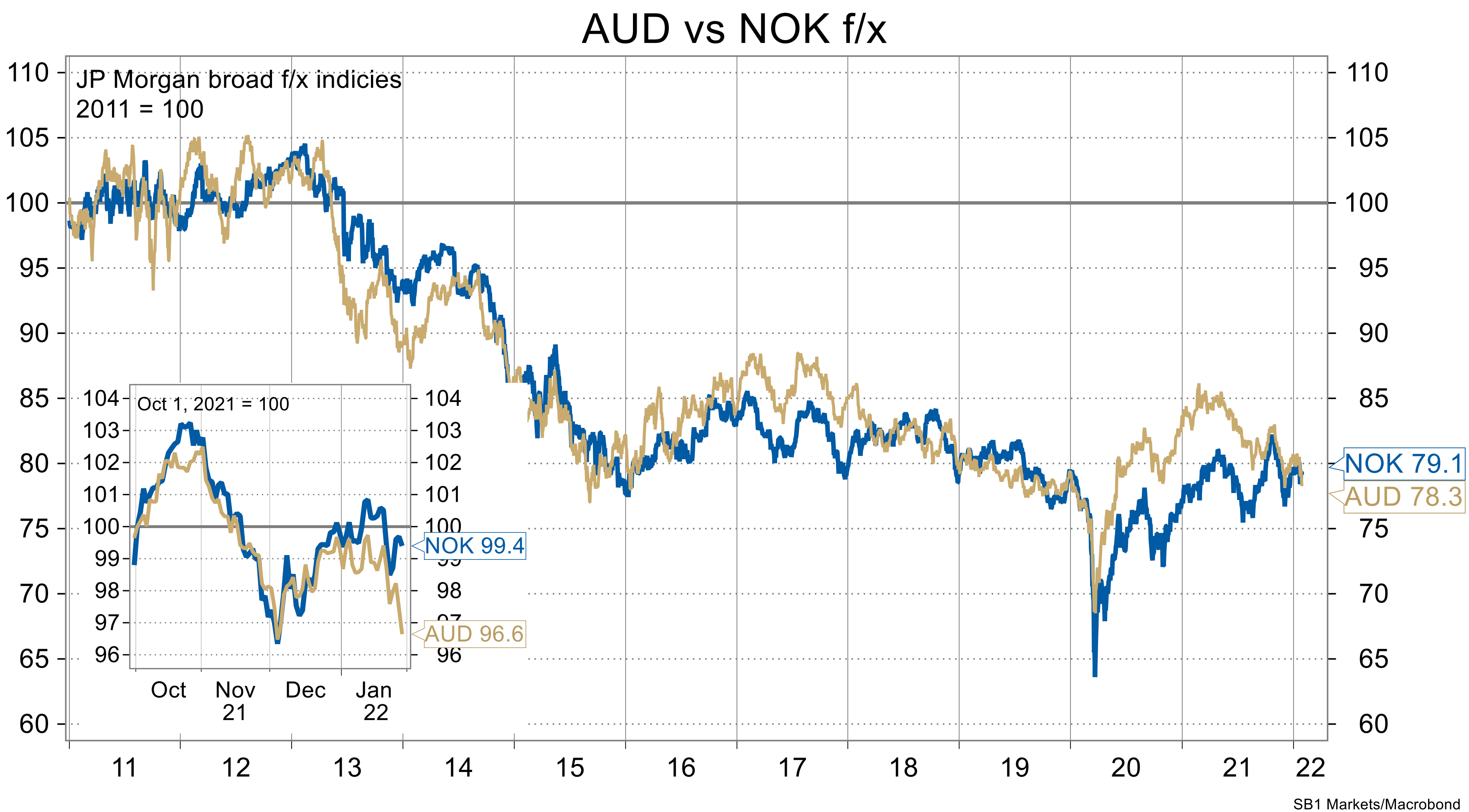




- NOK is still correlating quite closely to the oil price but at a lower level than before 2018 – and now the NOK is weak even vs the past 3 years' relationship
- A USD 10 drop in the oil price weakens the NOK by some 4%, as a partial effect. Within a broader model, the impact is smaller

The AUD has left us? Iron ore prices are strong

But Australia struggles with the virus?



The two f/x indices are back to the 2011 parity (vs each other, from which they never since have deviated much)

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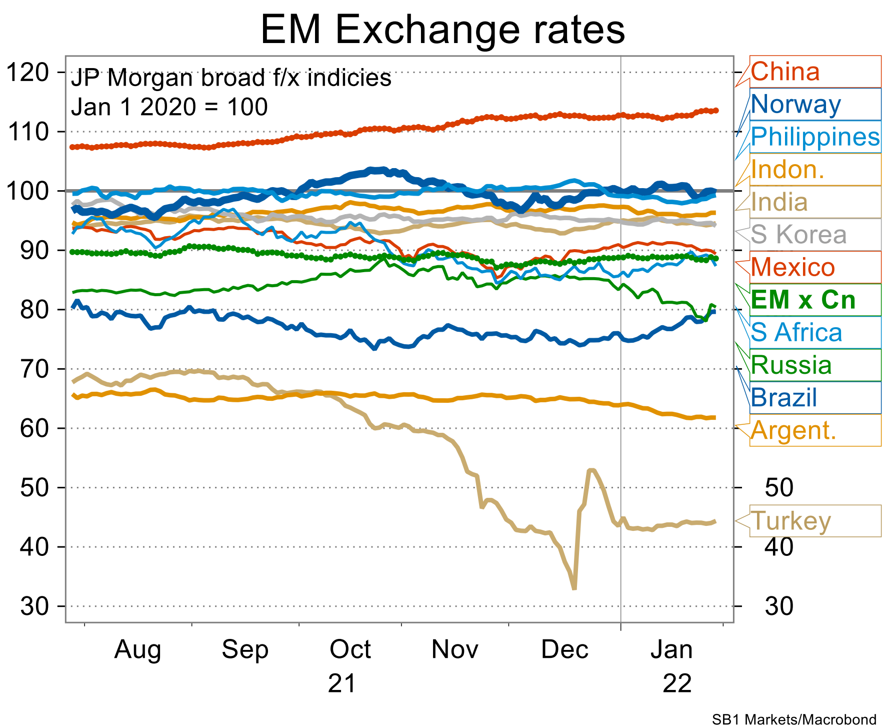
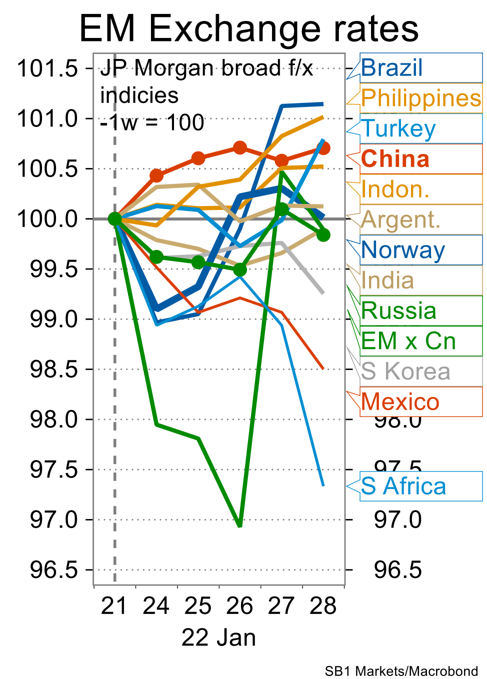
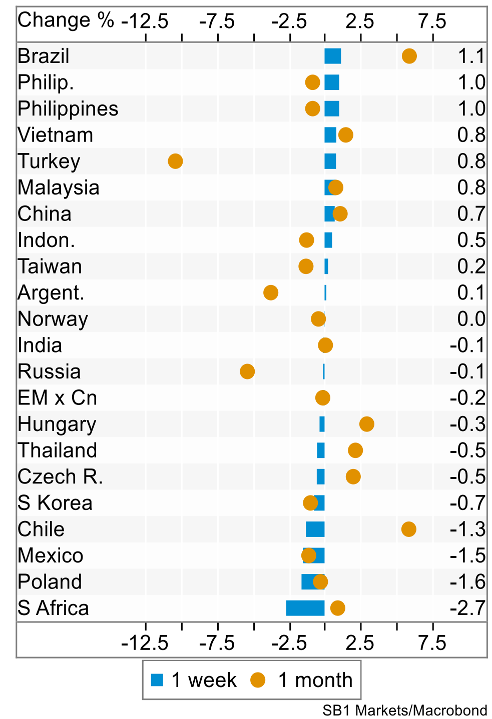
Brazil the winner last month, Russia the loser (alongside the volatile Turkey)







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